DEPARTMENT OF THE TREASURY
FEDERAL INSURANCE OFFICE (FIO)
FEDERAL ADVISORY COMMITTEE ON INSURANCE (FACI)

SUMMARY – 22 FEBRUARY 2018

The Federal Advisory Committee on Insurance (FACI) convened at 1:00pm on 22 February 2018 in the Cash Room at the US Department of the Treasury, 1500 Pennsylvania Ave., NW, Washington, DC, with Daniel Glaser, Chair, presiding.

In accordance with the provision of the Federal Advisory Committee Act, the meeting was open to the public.

Committee Members Present:
DANIEL GLASER, President and Chief Executive Officer, Marsh & McLennan Companies, Inc., Chair
STEVEN SEITZ, Deputy Director, Federal Insurance Office
AMY BACH, Executive Director, United Policyholders
LAURA BISHOP, Executive Vice President and Chief Financial Officer, USAA (By proxy, Erin Martinko
DAVID (BIRNY) BIRNBAUM, Executive Director, Center for Economic Justice
KURT BOCK, Chief Executive Officer, COUNTRY Financial
QUINCY BRANCH, President and Chief Executive Officer, Branch Benefits Consultants
ELIZABETH BROWN, Associate Professor, College of Business, University of Wisconsin – La Crosse
JOHN FRANCHINI, Superintendent, New Mexico Office of the Superintendent of Insurance
MARK GRIER, Vice Chairman, Prudential Financial, Inc.
GEORGE KEISER, Representative, North Dakota House of Representatives
JAMES (JIM) KELLEHER, Executive Vice President & Chief Legal Officer, Liberty Mutual Insurance
THEODORE MATHAS, Chairman, President and Chief Executive Officer, New York Life Insurance Company (by proxy, Julie Herwig)
ALFRED REDMER, Commissioner, Maryland Insurance Administration (by proxy, Nancy Grodin)
MARGUERITE SALAZAR, Executive Director, Colorado Department of Regulatory Agencies
MARIA VULLO, Superintendent, New York Department of Financial Services (by proxy, Scott Fischer)

ALSO PRESENT:
LINDSEY BALDWIN, Federal Insurance Office (delegated responsibilities of Designated Federal Officer)
TERRY WILLIAMS, Federal Insurance Office

WELCOME AND INTRODUCTION:

FIO Deputy Director, Steven Seitz, welcomed committee members who were able to attend the first FACI meeting of 2018. He gave a brief history of the role of the FACI and its mandate to present advice and recommendations to the Federal Insurance Office. Mr. Seitz also reiterated the continued importance of the FACI, especially in its ability to facilitate discussions that increase the Federal Insurance Office's understanding of certain issues. Mr. Seitz then turned the meeting over to Chairman Glaser.

Chairman Glaser welcomed all of the committee members in attendance and encouraged all members to share their thoughts and perspectives on the issues that the committee plans to review.

Discussion of the Long-Term Care Insurance Marketplace

Chairman Glaser highlighted recent challenges facing the long-term care insurance market, including the exit of several major insurers and the significance of losses incurred by major carriers. Mr. Glaser also noted that the Federal Insurance Office and Treasury have stressed the importance of finding solutions to stabilize the long-term care insurance marketplace in both the FIO 2017 Annual Report to Congress and in the Report on Asset Management and Insurance in response to Executive Order 13772. Mr. Glaser then introduced Professor Marc Cohen of the University of Massachusetts, Boston.

Mr. Cohen opened by thanking the committee for giving him an opportunity to present. Mr. Cohen then described the challenge of long-term care financing and opined that the challenge of long-term care will only grow in the years ahead. Mr. Cohen then noted that, given the nature of long-term care risk, that moving the long-term care system from a welfare based impoverishment model to an insurance-based approach will serve to achieve the best results. Mr. Cohen then detailed why the long-term care insurance market has underperformed and provided suggestions for how to create further growth in the private long-term care insurance marketplace.

Mr. Cohen explained that 50% of people turning age 65 will experience a significant need, meaning that they are going to have at least two functional limitations or be cognitively impaired before they die, but that we do not know which of us is going to need long-term care. As such, the risk is perfect for risk pooling. Mr. Cohen explained that the current system – namely Medicaid – requires that those in need spend their income and assets before being able to access the program, which is a threat to retirement security. Mr. Cohen also noted that the out-of-pocket cost provided by families will exceed $2.5 trillion over the next 10 years.

Mr. Cohen then discussed the long-term care insurance marketplace and the difference between stand-alone LTCI policies and combination products. Mr. Cohen noted that the characteristics of people who purchase LTCI as a stand-alone product, and that, typically they can be categorized as younger, wealthier individuals: People who are buying the products are now wealthier in terms of both assets and income. Mr. Cohen also noted the relative ease by which insureds can file claims and their positive experience with the claims management process.

Mr. Cohen then discussed the current marketplace, and noted that there was a "perfect storm" of events that got us to where we are now. He explained that most policies are now administered by companies no longer in the LTCI market. When considering how to increase the role of private insurance, Mr. Cohen explained that there are only three methods: lower the cost of the product; change tastes to the product; and/or encourage insurers to come back to the market.

Mr. Cohen thanked the committee.

Chairman Glaser invited Charles “Chuck” Piacentini, Associate General Counsel, American Council of Life Insurers, to speak.

Mr. Piacentini opened by discussing that the burden that families will face, will likely hit both state and federal welfare programs very significantly if there is not a role for other mechanisms, such as private insurance. Mr. Piacentini then detailed some of the National Association of Insurance Commissioners (NAIC) progress on long-term care insurance, including the creation of a joint task force to study the issue.

Mr. Piacentini noted that the NAIC is focused on a number of product and financing innovations, with specific focus on hybrid products, the most popular of which are life insurance or annuity policies that provide an accelerated benefit rider that pay a significant sum to individuals to mitigate the cost of long-term care services.

At the federal level, Mr. Piacentini noted that the NAIC brought forward a number of key financing options, including allowing retirement plan participants to utilize 401(k)s for premium and long-term care costs. Mr. Piacentini also reiterated Mr. Cohen’s point on familial impact. Mr. Piacentini stated that caretakers for disabled individuals may also need services and support.

Mr. Piacentini thanked the committee again and turned the floor over to Chairman Glaser.

Chairman Glaser opened the floor to questions from the committee.

Amy Bach questioned the notion that rate increases had not been granted quickly enough. She also noted that she considered the biggest barrier to people purchasing LTCI is the fear that premiums are going to be too high to be affordable. Ms. Bach asked Mr. Cohen where standalone products would go and asked Mr. Piacentini whether ACLI supported non-forfeiture provisions.

Mr. Cohen agreed that simple coverage is better than none and that, perhaps, some insureds were actually over-insured

Mr. Piacentini explained, with respect to rate increases, that it was his opinion that many state regulators believed that their rate increase may subsidize the policies in other states, which was frustrating. He also noted that non-forfeiture benefits are included in terms of most states’ model acts, which provides protection.

Kurt Bock explained that persistency of COUNTRY LTCI policies remains at 99% after a rate increase, which means that their policyholders are more apt to keep and retain their current benefit levels. Mr. Bock asked Mr. Cohen whether he has customer research to back the statements on rate increases (as opposed to claimant information, which is a much narrower subset).

Mr. Cohen explained that older people with LTCI who go back into the LTCI marketplace will experience higher premiums, and are concerned about whether they would pass underwriting. Mr. Cohen also explained that, while it does not make logical sense, there are behavioral issues associated with sunk costs.

George Keiser asked Mr. Cohen how many states have signed the Partnership Agreement and whether a long-term care policy was portable in light of the Partnership Act.

Mr. Cohen explained that a major benefit of the Partnership Agreement was that, for purposes of eligibility for Medicaid, a certain percentage of assets, would be shielded and that you would be permitted to retain those assets, which would induce people to consider insurance. Mr. Cohen suggested that over 30 states have Partnership policies.

Marguerite Salazar asked whether the presenters have data on what the costs of long-term care actually are versus where they should be.

Mr. Cohen explained that there is good cost information on long-term care and that a number of carriers do surveys on this. He explained that carriers have, in the past, tried to negotiated preferred provider rates, but that he does not know how active that approached is today.

Mr. Piacentini pointed out that a significant portion of LTCI benefits are paid on an indemnity basis, which would benefit the policyholder directly, not the provider.

John Franchini explained that there are some bad actors that sold LTCI that regulators are now having to deal with. He explained that he would like to see a way to allow companies to sell their policies into a reinsurance market, and in return, they would pay into the market all of the money collected.

Mr. Cohen explained that a reinsurer can be considered the same as an insurer in these instances and that they would be unlikely to find these policies attractive.

Mr. Piacentini explained that care should be taken to ensure that a pool of bad business is not created.

James Kelleher asked whether LTCI was viable in the United States

Mr. Cohen explained that one commonality across all jurisdictions with LTCI markets is that there is a wraparound to some social insurance program. He explained that there are higher take up rates in other countries because consumers know exactly what they will get from the government.

Mr. Piacentini added that there are differences in familial structures in other countries and that the U.S. is more mobile.

Discussion of Cybersecurity Risks to Insurers

Chairman Glaser introduced Mr. Ronald Bushar, vice president of global government services for FireEye to discuss cyber risks that the insurance industry could face.

Mr. Bushar introduced his colleague, Chris Porter, the Chief Intelligence Strategist for FireEye and thanked everyone for the invitation. Mr. Bushar explained that systemic cyber risk in the insurance and reinsurance market is a new and emerging area that is challenging because of the lack of history to study. He explained that, traditionally, attacks have been met with new defenses that creates a constant game of escalation. He explained that the financial services industry falls into an umbrella that nation-state actors target for their information. Mr. Bushar explained that the solution to defending critical infrastructure is unlikely to be solved with software and hardware, but rather will be solved by policy and governance.

Mr. Bushar explained that meeting minimum thresholds, such as the NYDFS Cyber Regulations, is not sufficient, and does not focus on how to operate systems in a more resilient manner. Mr. Bushar rhetorically asked how to translate risk into a management model or a model that can be communicated at a senior level in organizations to think through in a more holistic manner. In cyberspace, response cycles need to be swift and have to be tightly integrated with business operations so that down times are minimized.

Mr. Bushar noted that third party vendors must be considered for purposes of resilience as well because of their contributions to most enterprises. Understanding exposures and risks, especially as data and assets are transferred among service providers, is a critical risk area that needs to be well-understood.

Mr. Bushar recommended to the committee that they begin by starting at a high-level planning, including the use of drills. Today, most companies are no longer able to hold close a breach. This is due to a few factors: first, the media attention and focus in this area has increased significantly; second actors themselves have increased incentives to publicize what has occurred, either from a political or an information operations perspective, or from an extortion perspective.

Organization need to apply their own business models and their own unique elements of risk to the plans to make sure that resilience policies – perhaps based on the NIST framework – address their unique needs. Notifications, communication planning, how to deal with the media, how do you think about mitigation to both victims, customers, and employees, are all “underlooked.”

Mr. Bushar explained that companies need to prioritize certain assets, what he calls the “crown jewels” of an organization, including key data assets, key information technology assets, key individuals that must be protected rigidly. From there, companies need to build resiliency in. Mr. Bushar explained that organizations often struggle to figure out the appropriate balance between securing the “crown jewels” and the remainder of the organization.

Mr. Bushar noted that FireEye often finds that its clients either abandon or fail to maintain security controls that FireEye recommends because they are painful. Humans are incentivized to bypass security controls because they are annoying and they get in the way.

Mr. Bushar opined that FireEye believes that destructive attacks this year will come in the form of both CryptoLocker, Ransomware, and destruction of data and systems to cover tracks after a cyberattack, all of which will become more common.

Mr. Bushar noted that attribution is becoming increasingly important, because of the importance in understanding the bad actor being dealt with. Responses will be tailored depending on whether an attack is coming from a nation state, criminal group, terrorist, etc.

As a recommendation, Mr. Bushar suggested that all stakeholders need to do a better job of sharing information, knowledge, threats, vulnerabilities, etc. Mr. Bushar followed this by saying that he predicts that a cyber attack may eventually lead to significant damage to health and safety or, potentially, a loss of life.

Mr. Porter asked the rhetorical question of why an attacker would conduct a cyber attack. To provide perspective he explained that money centers are the most targeted, which are attacked after months of preparation by a sophisticated actor or organized crime group. Insurance, is the third most targeted group of the financial services sector. One reason for this may be to cause systemic risk to the entire U.S. economy. Why would a nation-state go after an insurer? Why would a criminal organization go after an in surer? For criminal groups, it is because insurers hold a lot of sensitive data that can be used for follow-on crime. For nation-states, the reason may be to get information on who customers are, or they utilize the trustworthiness that insurers have to gain access to other information that is more exploitable: hacking an insurer may be a side-door to get access to what a hacker really wants.

Kurt Bock asked whether it would be true that the largest companies are the most targeted and that the smallest companies are the most vulnerable and, if so, what smaller companies can do.

Mr. Bushar responded that he was not sure that there was a direct correlation to size, but that depending on the actor, oftentimes they are looking for an easy advantage, which is to say that they are looking for an easy way to gain access. So, if a smaller organization gives them entry, they will use it to get to whatever their ultimate target is.

Mr. Porter added that, on the PII side, bad actors do not care about who holds the data, but rather the data itself. For instance, bad actors care less about the insurer and more about who they are insuring.

Mr. Bushar added that a sad but true fact is that the organizations too small to afford the cost of cybersecurity protections are more exposed and that as a collective we need to think about how to help.

Steven Seitz asked how cybersecurity companies balance the need to maintain large companies as clients versus the need to understand the needs of and assist smaller insurers.

Mr. Bushar responded that a shared model, perhaps supported through a government-sponsored agency, might be a model for smaller insurers. He gave the concept that HHS is attempting to start to play in the health insurance sector by supporting small and regional healthcare systems and markets by providing access to more of the information at no cost.

Amy Bach explained that cybersecurity insurers are providing some information at no cost to policyholders to mitigate the potential for breaches and to increase resilience.

Julie Herwig asked if the presenters had a sense of a breakdown between the P&C, L&H as targets.

Mr. Bushar explained that they did not, but that more state actors are interested in the finance sector than health care.

Scott Fischer asked about the potential of systemic risk and the potential to have correlation that companies are not even aware of.

Mr. Bushar explained that it is difficult for insurers to underwrite some risk because of the potential for systemic risk.

Discussion of the National Flood Insurance Program, National Mitigation Investment Strategy, and Resilience

Chairman Glaser opened discussion by noting that the NFIP provides a vital service to the people and places that have been hit by a natural disaster and that no part of the country is truly immune from flood damage. He noted that a longer term NFIP extension is important because it would allow the program reforms being considered by Congress to be implemented efficiently and effectively.

Chairman Glaser then introduced Tyler Corson-Rickert of FEMA.

Mr. Corson-Rickert began by talking about the NFIP, noting that Congress created the program in the 1960s because of the tremendous challenge that flooding poses to the U.S. Floods are the nation’s most common and costly natural disaster, and, on average cost America approximately $8.2 billion. Mr. Corson-Rickert explained that the NFIP is more than just a federal insurance program: NFIP is also a program to identify flood risk across the nation and to work with communities and households to reduce flood risk through the flood plain management requirements and mitigation assistance. After detailing some of the work of the NFIP, Mr. Corson-Rickert concluded that the NFIP rose to the occasion to handle the recent natural disasters and that FEMA would continue to carefully integrate lessons learned from each flood event.

Mr. Corson-Rickert highlighted FEMA’s commitment to developing a culture of preparedness in closing insurance gaps across the nation and reminded everyone of the importance of purchasing flood insurance. He noted that there is a 26% chance that a home in a special flood hazard area will experience a flood over the course of a 30-year mortgage. He explained that the average premium for an NFIP policy is just $700, but that the average claim payment is $43,000. He noted that FEMA is working to transform the NFIP into a provider that the policyholders and communities value and trust.

Mr. Corson-Rickert explained that one of Congress' and FEMA's biggest challenges with the NFIP is creating a sound financial framework for the program. He also noted that NFIP has over 5 million policies in force, nearly two-thirds of the U.S. population use credible flood risk data products, over 1,400 communities participate in the FEMA community rating system to better manage their risk, and that FEMA has avoided an estimated $46 billion in losses through mitigation investments in the life of the program.

Mr. Corson-Rickert then shifted the discussion to the National Mitigation Investment Strategy. Mr. Corson-Rickert noted that last year's declared disasters create a significant opportunity to increase mitigation efforts using federal dollars. Specifically, up to 20% of amounts spent in recovery efforts in presidentially declared disasters can be allocated to mitigation projects. However, FEMA also needs its partners to communicate the value of investing in mitigation to ensure the long-term health and sustainability across the country.

Mr. Corson-Rickert discussed a study by the National Institute of Building Sciences that shows that for every $1 invested in mitigation, $6 are saved and losses avoided. He explained that FIMA is leading development of the NMIS with a working group including members of the Federal Insurance Office. The NMIS is about closing the nation's hazard mitigation and insurance gap. Goals of the NMIS are to to increase the effectiveness of existing federal housing mitigation programs to incentivize greater state, local, and private sector contributions to long term risk reduction and provide guidance that governments and private sector entities can use to consider in making resource allocation decisions. The strategy is intended to deliver actions that will lead to the following national outcomes: improved coordination, innovative financing, shared accountability, access to data, risk informed communication, and a resilient built environment.

Mr. Corson-Rickert yielded back to Chairman Glaser

Chairman Glaser introduced Amy Bach, FACI Member and Executive Director of United Policyholders.

Ms. Bach discussed the importance of the NFIP and noted that UP is a steadfast supporter of NFIP, but also very focused on helping move the needle to get more people to buy flood insurance.

Ms. Bach explained that the reality is that unless a lender, an agent or broker, or a financial advisor who requires or recommends buying flood insurance, most people fail to buy it. This is why we only have 5 million of the 117 million households in this country that have an NFIP policy, and then the private insurers share is in the .00 percent of homes that are insured through private flood policies.

Ms. Bach explained that there is innovation on the flood front: there are a limited number of hybrid products on the market; there have been a number of private carriers that include a flood endorsement for, typically, higher end customers; and there is increased interest from reinsurers; there is a multi-state consortium looking at ways to create a multi-state or national all perils product.

Ms. Bach noted that, regarding mitigation, NFIP/FEMA should not be forced to bear the entire burden, and that private insurers should have a role in facilitating mitigation of flood damage. By that, policyholders should be told what they can do in helping to contribute to the research and publicity around making their homes less damaged in the event of a flood.

Ms. Bach noted that many states have stepped up to assist with flood mitigation, specifically New Jersey after Superstorm Sandy. Ms. Bach then yielded the floor to Chairman Glaser.

George Keiser asked Mr. Corson-Rickert if there was discussion in FNIP regarding the grandfathered status of some properties.

Mr. Corson-Rickert responded by providing an overview of the grandfathered status of properties during remapping, which was addressed in part by Congress in the Biggert Waters Flood Insurance Reform Act. Mr. Corson-Rickert explained that FEMA is continuing the practice and explained that the primary factor is work on risk rating redesign, which is a fundamental look at how FEMA maps flood risk, and how to turn that into insurance ratings and the premiums that policyholders pay. Generally, FEMA is hoping to move away from the current maps that are based on paper and whether you are in or out of the flood plain.

John Franchini asked whether FEMA's reinsurers made a profit on the $1billion of flood risk coverage that they provided FEMA for $150 million in coverage.

Mr. Corson-Rickert explained that they worked with 25 different reinsurers who paid out in full and that, although he was unaware of how this played out on their balance sheets, that there was an appetite to insure the risk again in 2018.

Mr. Franchini then asked if the NFIP could go into a DIC program, instead of just flood.

Mr. Corson-Rickert responded that, as the administrator talks about the national insurance gap, he is talking about a range of kinds of insurance coverage that could help Americans, but that there are specific parameters around which NFIP can operate. Mr. Corson-Rickert noted that FEMA would certainly welcome any discussion of additional catastrophes/risks in Congress about how the NFIP can evolve.

James Kelleher asked whether Mr. Corson-Rickert had a view on the NFIP requirement that NFIP servicers are precluded from engaging in the private market.

Mr. Corson-Rickert explained that, as he understands it, the non-compete clause relates only to a specific entity of an insurer that services WYO products, not other entities within the organization, such that a subsidiary of the insurer may be able to sell competing products. Mr. Corson-Rickert also noted that independent agents are welcome to sell whatever product that they want to sell.

Kurt Bock asked Ms. Bach how the industry can respond to the problem of underinsurance.

Ms. Bach responded that competition may help provide more attractive options and that agents need to recommend flood insurance when appropriate.

New Business and Closing Remarks

Chairman Glaser turned the floor over to Steven Seitz to provide a brief update.

Mr. Seitz highlighted the FIO's work on the U.S./EU Insurance Project, big data, and discussed FIO/Treasury efforts to be more open and transparent with colleagues at the state level, in Congress, and with all stakeholders.

Chairman Glaser motioned to approve the minutes from the August 17, 2017 and December 6, 2017 meetings. Member Keiser seconded the motion.

At 4:22 pm, Chairman Glaser concluded the meeting.