

**DEPARTMENT OF THE TREASURY
FEDERAL ADVISORY COMMITTEE ON INSURANCE (FACI)
SUMMARY - JANUARY 5, 2017**

The Federal Advisory Committee on Insurance (FACI) convened at 1:00 p.m. on January 5, 2017 in the Cash Room at the U.S. Department of the Treasury, 1500 Pennsylvania Avenue, N.W., Washington, D.C. 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
AMY BACH, Executive Director, United Policyholders
DAVID (BIRNY) BIRNBAUM, Executive Director, Center for Economic Justice
LAURA BISHOP, Executive Vice President and Chief Financial Officer, USAA
KURT BOCK, Chief Executive Officer, Country Financial
QUINCY BRANCH, President and Chief Executive Officer, Branch Benefits Consultants
ELIZABETH BROWN, Professor, 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
THEODORE MATHAS, Chairman, President, and Chief Executive Officer, New York Life Insurance Company (by Proxy, Julie Herwig)
AL REDMER, Commissioner, (by Proxy, Catherine E. Grason)
MARGUERITE SALAZAR, Commissioner
MARIA VULLO, Commissioner

Committee Members Not Attending:

JAMES KELLEHER, Executive Vice President & Chief Legal Officer, Liberty Mutual Insurance
TERESA MILLER, Commissioner, Commonwealth of Pennsylvania Department of Insurance
THEODORE (TED) NICKEL, Commissioner, Wisconsin Office of the Commissioner of Insurance
MICHAEL RILEY, Commissioner, State of West Virginia Offices of the Insurance Commissioner
CHRISTOPHER SWIFT, Chairman and Chief Executive Officer, The Hartford
KATHERINE (KATIE) WADE, Commissioner, State of Connecticut Insurance Department

Also Present:

MICHAEL McRAITH, Director, Federal Insurance Officer, U.S. Department of the Treasury
CHESTER McPHERSON, Designated Federal Officer, U.S. Department of the Treasury
DANIEL McCARTY, Federal Insurance Officer, U.S. Department of the Treasury
A. THOMAS FINNELL JR., Deputy Director, Federal Insurance Office, U.S. Department of the Treasury

Welcome Introduction and New Members

Director McRaith welcomed the members of the FACI and turned the meeting over to the FACI Chairman Daniel Glaser who officially convened the meeting.

Chairman Glaser welcomed the FACI Members and spoke of the changes for the upcoming year. He then acknowledged the Committee members who were reappointed for another three-year term: Superintendent John Franchini, Representative George Keiser, and Mr. Mark Grier. Chairman Glaser also noted that he too was reappointed for another three-year term. He then thanked the reappointed members for their continued service and congratulated them on their reappointment.

Mr. Glaser welcomed two new members to the Committee: Mr. Christopher Swift, Chairman and CEO of the Hartford, who, unfortunately, was unable to attend; and Mr. Quincy Branch, President and CEO, Branch Benefits Consultants.

Chairman Glaser concluded his welcoming remarks by recognizing the service of those members whose terms on the Committee recently ended:

- **Commissioner Nicholas Gerhart** of Iowa resigned in December 2016 as his state's insurance commissioner;
- **Commissioner Julie McPeak** of Tennessee recently assumed the role of President-Elect of the NAIC and because of her new responsibilities will not be able to continue as a member of the Committee;
- **Professor Brenda Cude** from the University of Georgia, who served as a consumer advocate representative; and
- **Loretta Fuller, CEO of Insurance Solutions Associates**, who served as an industry representative.

Chairman Glaser emphasized that, "this Committee helps FIO to fulfill its important role. It is work that would not be as meaningful without the contribution of all of our members." He thanked all members for their contribution.

Discussion of the Emerging Cost in Auto Insurance

Chairman Glaser introduced the topic and called on Mr. Peter Drogan, Vice President and Chief Actuary at Amica Mutual Insurance Company. Mr. Drogan focused his presentation on the increase in frequency and severity of auto insurance losses, and explored a range of contributing factors as certain drivers impact the cost of automobile insurance premiums. He noted that although most of his presentation was based on data related to personal auto, the trends can also be applied to commercial auto.

Mr. Drogan observed that there are several continuing forces placing upward pressure on costs and premiums; he classified them into three main categories and offered his views on each, namely: the economy, society, and technology. The economy – Mr. Drogan said that more employment opportunities and low gas prices will continue to increase the number of miles driven, although he observed that increasing employment is a more important causal factor to the miles driven than gas prices. Mr. Drogan identified some societal factors that are also cost drivers, such as: speeding – the repeal of the national maximum speed limit may be a contributing force to increasing auto fatalities and injuries; increasing use of marijuana and drug use – Colorado has reported increases in traffic deaths involving marijuana, while California has reported that drivers killed in car crashes who test positive for drugs increased by nearly 40

percent from 2009 to 2013; and distracted walking – another major growing problem that has contributed to more accidents. On the technology front, Mr. Drogan noted that although cameras and sensor equipment are largely present only in higher end cars, manufacturers are moving quickly to incorporate new, costly technology into their entire fleet. New technology means more cost. Repair costs are increasing as a result of more of vehicles on the road that are equipped with the new technology. Mr. Drogan said that the increasing costs of repairing cars are a national trend, not a state specific trend. Mr. Drogan concluded that policymakers should continue to work on increasing preventive measures to curve these adverse trends by enacting new laws and enforcing the distracted and impaired driving laws, adopting responsible speed limits, and continuing to educate and increase public awareness of these issues. Mr. Bock, Ms. Bach, and Mr. Birnbaum asked questions of Mr. Drogan.

Discussion of Blockchain Technology in the Insurance Sector

Chairman Glaser introduced and welcomed Mr. Matt Higginson, Associate Partner at McKinsey & Company, who shared his views on an emerging technology called “Blockchain.” Mr. Higginson described Blockchain technology as a cryptographic or encoded distributed ledger that is comprised of a digital log of transactions that can be shared across either a public or a private network. He noted that because Blockchain uses a more secure cryptographic key system than anywhere else in the financial services, it lends a degree of security not seen before. Mr. Higginson shared that in order for the industry to successfully deploy Blockchain, it must first undertake digitizing data from paper records to digital records, which he acknowledged will be a major undertaking. He explained that the successful application of the Blockchain related technology requires a distributive ecosystem, and, therefore, is not a solution that can be pioneered by individual insurance companies working on their own. He said that Blockchain requires a degree of cooperation, which is a major challenge for the financial services industry because it does not have a good history of collaborating constructively. Mr. Higginson said insurance companies, regulators, technology companies, and ultimately the government will need to cooperate in order to make Blockchain successful.

Mr. Higginson noted that over the last two years more than \$1 billion has been invested on Blockchain related technology. Mr. Higginson stated that approximately half of the industry is actively participating in experiments with Blockchain, while the other half is in a wait see mode; and, acknowledged that it will take upwards of five years for Blockchain to become applicable on a commercial scale and be a reality across the industry.

Mr. Higginson concluded that commercial grade Blockchain technology solutions will not be developed in a hurry; and, instead, the industry will take time to understand the technology, to build prototypes, and eventually to find a way of working together for the benefit of the whole industry. In doing so, it will gradually overcome some of these big hurdles and resolve some of the existing regulatory challenges.

Mr. Glacier, Ms. Bach, Superintendent Franchini, and Mr. Bock asked questions of Mr. Higginson.

Discussion of an Overview of Insurance Fraud

Chairman Glaser introduced and welcomed Mr. Alan Haskins, Director, Government Affairs, National Insurance Crime Bureau (NICB). Mr. Haskins provided a brief overview of the NICB, a nonprofit organization with 1,100 property and casualty insurance member companies and that has been in business for approximately 104 years. Mr. Haskins explained that NICB’s mission is to be the preeminent organization fighting insurance fraud and vehicle crime by working with insurers, law enforcement

agencies, and representatives of the public and private sectors. Mr. Haskins noted that investigations are the core of the work performed by NICB, done in conjunction with prosecutors and attorney generals' offices around the country.

Mr. Haskins said that by law, NICB member companies have to report suspected insurance fraud to the departments of insurance all around the country, and the data included in those reports are used to focus NICB's investigative resources on insurance fraud issues such as medical, commercial fraud, and auto-related crimes. He said these cases tend to be concentrated in the larger states: California, Florida, New York, and Texas. Mr. Haskins also shared about NICB significant legislative work on such issues as strengthening states' anti-fraud laws; and working with states to adopt anti-solicitation laws to prevent third-parties from soliciting victims of insured losses.

Mr. Haskins concluded by providing an overview on the costs of insurance fraud; he conceded that there are no definitive sources that track the actual cost of insurance fraud, and any estimation is, at best, a guess. He pointed to references that the FBI estimates there is annually \$40 billion of non-healthcare fraud, and \$250 billion for healthcare related fraud.

Mr. Birnbaum, Superintendent Franchini, and Commissioner Salazar asked questions of Mr. Haskins.

Discussion of an the Opportunities and Challenges to Insurance Regulation and Consumer Protection from Insurers' Use of Big Data

Chairman Glaser introduced and welcomed Mr. David (Birny) Birnbaum, Executive Director, Center for Economic Justice. Mr. Birnbaum shared that "Big Data" poses an existential challenge to the state-based system of insurance regulation. He defined Big Data as "massive databases of information about millions of individual consumers, associated data mining and predictive analytics applied to those data, and scoring models produced from these analytics." Mr. Birnbaum identified a number of changes in the market place as a result of insurers' using Big Data, such as using it in insurance pricing, marketing, and managing claims settlements. Mr. Birnbaum said that Big Data has the huge potential to benefit consumers and insurers by transforming the insurer-consumer relationship. He indicated that Big Data could be used to discover new insights into loss mitigation, but at the same time, it also has significant implications for fairness and affordability of insurance, and for regulators' ability to keep up with the changes and protect consumers from unfair practices.

Mr. Birnbaum shared that the current insurance regulatory framework in most states does not provide regulators with the tools to effectively respond to insurers' use of Big Data. He said that regulatory reform that emphasizes regulators collecting, analyzing, and publishing consumer market outcomes will yield more efficient and effective regulation for consumers, insurers and producers; and, further, will promote more competitive markets that will foster quicker adoption of innovative technologies that benefit consumers and fulfill public policy goals. Mr. Birnbaum suggested that in order to identify insurers' use of data, it is necessary to monitor market outcomes, and this can be done by creating a resource for the states for Big Data analytics and develop a 21st century approach to the oversight of risk classifications, including oversight of modelers acting as advisory organizations.

Ms. Bach and Mr. Bock asked questions of Mr. Birnbaum.

Discussion of the IAIS Proposed Insurance Capital Standard

Chairman Glaser introduced and welcomed Mr. A. Thomas Finnell Jr., Deputy Director, Regulatory Policy, FIO. Mr. Finnell provided an update on the development of the proposed insurance capital standard (ICS) of the International Association of Insurance Supervisors (IAIS). He reported that the ICS work is in the fourth year of annual field testing, and that the 2016 field test – the most recent – involved analyzing data from approximately 40 firms including some U.S.-based firms. Mr. Finnell shared that a number of issues related to the ICS work stream have been discussed and tested, including: (i) a market-adjusted basis of valuation (MAV); (ii) a “GAAP with adjustments” basis of valuation, also called “GAAP Plus”; (iii) the qualifying amount and classification as Tier 1 or 2 capital of various capital resources such as retained earnings, common stock, and various financial instruments such as senior debt and surplus notes; and (v) the issue of non-paid-in capital.

Mr. Finnell also shared that the International Accounting Standards Board and the Financial Accounting Standards Board here in the United States are expected to make changes to their respective accounting standards pertaining to accounting for insurance contracts.

Mr. Finnell concluded his remarks with a reminder that the current ICS work plan contemplates adoption by late 2019. He also noted that the ICS, if adopted, is not self-executing, and would have to be implemented by the appropriate authorities in individual jurisdictions.

Director McRaith Announced His Resignation

In addition to the presentations made at the meeting, Director McRaith announced that he would be resigning as the FIO Director after five and a half years in the position. He thanked the FIO members for their service, with special acknowledgement of Chairman Glaser for his work and persistent attendance, leadership, and friendship. In his remarks, Director McRaith also thanked the FIO staff for their service, and also Secretaries Geithner and Lew for their leadership during his tenure.

New Business

Prior to the Committee adjourning, Chairman Glaser raised the item of new business and discussed with members whether to meet in February as was planned or to meet instead on May 11. The members agreed to May 11 for the next meeting.

Chairman Glaser thanked the presenters and members of the Committee for attending the meeting, and extended a special thank you to Director McRaith.

At 4:30 p.m., Chairman Glaser concluded the meeting.