OVERSIGHT HEARINGS

BEFORE THE

SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW

OF THE

COMMITTEE ON THE JUDICIARY HOUSE OF REPRESENTATIVES

NINETY-EIGHTH CONGRESS

SECOND SESSION

ON

COMPETITION IN THE INSURANCE INDUSTRY

APRIL 11, MAY 3, 10, JUNE 28 AND SEPTEMBER 13, 1984

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COMPETITION IN THE INSURANCE INDUSTRY

WEDNESDAY, APRIL 11, 1984

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The subcommittee met at 9:05 a.m., in room 2141 of the Rayburn House Office Building, Hon. Peter W. Rodino, Jr. (chairman) presiding.

Present: Representatives Rodino, Edwards, Crockett, Fish, and Moorhead.

Staff present: Alan A. Parker, general counsel; Warren S. Grimes and Jonathan Cuneo, counsel; Marilyn Falksen, research assistant; Alan F. Coffey, Jr., Thomas M. Boyd, and Charles E. Kern III, associate counsel.

Chairman RODINO. Today, the Subcommittee on Monopolies and Commercial Law begins hearings on the McCarran-Ferguson Act's antitrust exemption of the business of insurance.

Insurance is a mammoth, powerful, and sophisticated industry. Its operations traverse international boundaries. And, the industry touches virtually every American. Yet, I suspect that few, if any, people really understand their own policies, much less the workings of this complex and varied industry. The product it sells—a promise to pay should an unfortunate incident occur—is unique. The intangibility of insurance makes it difficult to inspect or test. And its complexity makes it hard to evaluate its financial soundness.

Yet, despite these qualities—size, universality, complexity and intangibility—the business of insurance is regulated almost entirely by the States. The Federal Government neither regulates the industry nor enforces private competition through the antitrust laws. The McCarran-Ferguson Act specified that the power to tax and regulate the business of insurance lies with the States and that the antitrust laws apply only to the extent that the business of insurance is not regulated by the States.

It is entirely appropriate for the subcommittee to address McCarran-Ferguson at this time. In fact, some would say that congressional review of the system of antitrust exemption and State regulation is long overdue. The subcommittee has a continuing duty to reevaluate existing exemptions; the insurance exemption—unquestionably one of the most important—can be no exception. Insurance is so important and its exemption so broad that we should not ignore it.

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The National Commission for the Review of Antitrust Laws and Procedures [NCRALP] on which I served with several other members of the subcommittee, recommended that the Congress reevaluate the McCarran-Ferguson Act with a view toward narrowing its scope.

During his tenure as Attorney General, our first witness, Judge Griffin Bell, was instrumental in the formation of NCRALP. Judge Bell is here to present us with that Commission's recommendations on insurance as well as his own views about their applicability today.

We will also hear from two members of the Commission: Mr. Robert McClory, former ranking minority member of the Judiciary Committee and of this subcommittee—we welcome him this morning—and Prof. Eleanor Fox from New York University School of Law. Our final witness today is a noted author, Andrew Tobias, who wrote "The Invisible Bankers," a popular overview of the insurance industry.

I recognize the gentleman from New York, Mr. Fish.

Mr. FISH. Thank you, Mr. Chairman. It has now been 5 years since the National Commission for the Review of Antitrust Laws and Procedures made its recommendations on the McCarran-Ferguson Act. Consequently, this morning we begin a congressional inquiry into the merits of their recommendations.

The McCarran-Ferguson Act was passed in 1945. It does grant the insurance industry a substantial exemption from the Federal antitrust laws. However, we should not proceed with this inquiry on the general assumption that therefore insurance goes totally unregulated at the Federal level. The facts are that numerous aspects of the insurance business are scrutinized by a variety of Federal agencies.

For example, the McCarran-Ferguson Act expressly provides for the application of the National Labor Relations Act and the Fair Labor Standards Act to the business of insurance. Insurance companies are also subject to SEC regulations with respect to the issuance of publicly held securities. The Federal Trade Commission regulates insurance company mergers. Additionally, a program administered by the Federal Emergency Management Agency, through the Federal Insurance Administration, involves the Federal Government, the States and private insurance companies in an undertaking to provide property insurance to persons affected by riots, civil disorders and floods. The Interstate Commerce Commission specifies the coverage required of interstate carriers. The Price-Anderson Act determines the limits of liability and establishes absolute liability on the operators of nuclear reactors. The Labor Department and HHS implement the Black Lung Program for coal miners. Finally, when the Federal Government imposed wage and price controls in the 1970's, they applied as well to insurance wages and premium rates.

So, while McCarran-Ferguson does limit the application of antitrust laws, it does not preclude Federal legislative and executive actions concerning the insurance industry. The act itself recognizes the continuing right of Congress to enact laws that "specifically relate to the business of insurance."

Any exemption from the Federal antitrust laws deserves close, periodic scrutiny by the Congress, as you have stated, Mr. Chairman. The regulation of insurance and the importance of the insurance business raise broad economic and social policy questions, as well as questions from an antitrust perspective.

I welcome the distinguished group of witnesses scheduled to appear before us this morning and look forward to their testimony, and particularly, welcome back our friend Judge Bell and wish a warm welcome to our friend and former colleague, Bob McClory. This room has been the scene for many of the important contributions that he made while serving as a Member of this body.

Thank you, Mr. Chairman.

Chairman RODINO. The gentleman from California.

Mr. EDWARDS. Thank you, Mr. Chairman. I echo the welcome expressed by our friend from New York, Mr. Fish. It is going to be a great pleasure to have Judge Bell and Mr. McClory, whom we miss very much on this subcommittee, testify today and I congratulate you, Mr. Chairman, for getting these hearings going.

It is really very important. It is an immense industry and it is certainly our job to determine whether State regulation is adequate, whether it is well financed and what part we should play on behalf of the consumer.

Mr. Chairman, I ask that my full statement be made a part of the record.

Chairman RODINO. Without objection.

Mr. EDWARDS. I regret I am going to have to leave to chair my own subcommittee.

[The statement of Mr. Edwards follows:]

MR. EDWARDS' STATEMENT

Mr. Chairman, I am pleased that the Subcommittee on Monopolies and Commercial Law is beginning its review of the antitrust exemption granted the insurance industry by the McCarran-Ferguson Act.

The insurance industry is vast and powerful. In 1982, its assets totalled approximately $820 billion—more than $3,500 for every man, woman and child living in the United States. Insurance touches the lives of virtually every person in this country. Most Americans own at least one insurance policy. And the cost of insurance is included in the price of the goods and services they buy.

Despite the size and influence of the insurance industry, no federal agency oversees its operations. The McCarran-Ferguson Act, passed in 1945, made clear that the business of insurance was to be regulated by the states, and the federal antitrust laws were to apply to insurance *only* in the absence of state regulation.

Almost 40 years have passed since Congress enacted this exemption from the antitrust laws. Our country's economy and needs are entirely different in 1984 than they were in the mid-1940's. Therefore, it is appropriate for us to examine the effects of this exemption in today's marketplace. No industry, especially one as large and as powerful as the insurance industry, should be immune from scrutiny by Congress.

As the people's representatives, it is our responsibility to ensure that the antitrust exemption enacted by Congress is not harming the individual; that the consumer is not paying artificially high prices or receiving an inferior product or poor service because of a lack of competition. As members of the Subcommittee on Monopolies and Commercial Law, whose responsibility it is to try to ensure that our nation's economy operates to the benefit of all—and not just the powerful few—we must ask if consumers are best served by this exemption.

Equally important is our duty to determine whether state regulation, mandated by the McCarran-Ferguson Act to take the place of the federal antitrust laws, is effective in promoting competition. We must ask ourselves whether state regulators,

often understaffed and underfunded, can adequately oversee the activities of these mammouth international companies.

Mr. Chairman, these are some of the questions I intend to ask during our insurance hearings. I look forward to working with you as we attempt to ascertain the answers.

Chairman RODINO. Thank you very much. It is now our pleasure to welcome once again to this committee room, and particularly before this subcommittee, the distinguished former Attorney General of the United States. He is a good friend of long standing, and appears now, however, in another role—one, from which I am sure we will be able to glean a great deal of information. It was under Mr. Griffin Bell's tutelage, guidance, and leadership that the Commission was organized to review the various exemptions under our antitrust laws. We thank him for that effort and for that initiative.

Judge, we are pleased to see you here once again. You are looking mighty well, I might say. Your smile is even broader than it's ever been. It is a delight to have you here.

Before we proceed with Judge Bell's testimony, I would like to point out that there has been a great deal of legislative history in this area, and I would like to recite some of it for the benefit of the subcommittee. I think the legislative history on this subject is very revealing and rather informative and, for that reason, I call it to the attention to the subcommittee. First let me say, from the documents that we have reviewed, it would seem that the Congress' primary purpose in passing the McCarran-Ferguson Act was not to exempt the industry from antitrust but to ensure that the States retained the right to regulate and to tax insurance companies. Second, the House Committee on the Judiciary made clear at the time in its report that the members valued a competitive marketplace.

The report stated, and I quote:

> Nothing in this bill is to be so construed as indicating it to be the intent or desire of Congress to require or encourage the several States to enact legislation that would make it compulsory for any insurance company to become a member of rating bureaus or charge uniform rates. It is the opinion of Congress that competitive rates on a sound financial basis are in the public interest.

Third, members of both Chambers of Congress, as well as the President, were concerned about the consequences of granting the insurance industry an exemption from the antitrust laws. There was a good deal of correspondence between President Roosevelt and Members of the Senate on this subject. As a matter of fact, it is very interesting to note that at that time, Mr. Bell, the President of the United States used to respond directly, and within a very short period of time, to the inquiring Members of Congress. That is hardly the practice today.

Anyhow, Members of both Chambers of Congress, as well as the President, feared the consequences of granting blanket immunity from the antitrust laws to the business of insurance. President Roosevelt wrote at that time, "There is no valid reason for giving any special exemption from the antitrust laws to the business of insurance." Congressman Celler, who later distinguished himself as chairman of this committee and subcommittee, voiced concern about the "power and potency of the various large insurance companies."

One of our most respected colleagues, then-Senator Claude Pepper, expressed great doubts about the wisdom of exempting an industry as large and as powerful as the insurance industry from the antitrust laws. As a matter of fact, he led the floor fight against final passage in the other Chamber. Although a previous commitment prevented him from being here today, the distinguished Member of Congress from Florida has submitted a statement, and I am going to ask that his statement be included in the record following my remarks.

Through this brief summary, I thought I would bring to the attention of the subcommittee some of the insights that were obtained from the documents which we reviewed. I think they will be interesting and very informative for the members of the subcommittee as we wrestle with this problem.

[Materials in appendix 1 at p. 545.]

[The statement of Hon. Claude Pepper follows:]

STATEMENT OF HON. CLAUDE PEPPER BEFORE THE SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW ON THE INSURANCE INDUSTRY'S ANTITRUST EXEMPTION

I appreciate the opportunity to submit this statement to the Subcommittee on Monopolies and Commercial Law on the troublesome exemption of the insurance industry from the Federal antitrust laws. I commend Chairman Peter W. Rodino, Jr. and the members of this distinguished Subcommittee for this opportunity.

The insurance industry has emerged as a multi-billion dollar business. Statistics indicate that the insurers of this country collected about $275 billion in insurance premiums in 1983 and returned to the insured consumers some sixty percent of the premiums collected. In administering this business, the insurers retain some $100 billion annually. No other large industry is exempt from the antitrust laws. I endorse the able Chairman's scrutiny of the insurance industry that has mushroomed since its antitrust exemption in 1945.

I would like to recount for the record the chronology of events that led to the exclusion of the insurance industry from the applicability of the antitrust laws since 1945.

The United States Supreme Court held in *Paul* v. *Virginia,* 75 U.S.C. (Wall.) 168 (1868) that the issuance of a policy of insurance was not a transaction of commerce. This holding prevailed for some seventy-five years and the insurance industry was not subject to the Federal antitrust laws until the landmark decision of *United States* v. *South-Eastern Underwriters Association et al,* 322 U.S. 533 (1944) Writing for the Court, Mr. Justice Black held that the insurance business is commerce within the meaning of the Constitution. The Federal government could regulate the insurance industry as well as the States. The decision did not overrule *Paul* v. *Virginia* to the effect that the States could not continue to regulate insurance as they had been doing since 1868. *South-Eastern Underwriters* held that the Federal government could regulate as well, as Congress had so intended by the enactment of the Sherman Act.

While the *South-Eastern* decision was pending in the Supreme Court, some Senators and Representatives made an effort to exempt the insurance industry from the antitrust laws. Such legislation did not become law, though there were efforts following the Supreme Court's decision to affect that holding in some way.

Legislation was introduced in both houses concerning the regulation of insurance after the *South-Eastern* decision of 1944. The Senate bill provided for a moratorium of three years, during which time the insurance officials and companies could adapt their conduct and regulations to the antitrust laws. Following this moratorium, the Senate bill provided further that the decision in *South-Eastern Underwriters Association* would apply. Senator Ferguson of Michigan added an amendment stating that the antitrust laws would be applicable following the moratorium despite any action the States might take. Yet, after the Senate bill went to the House, Senator Ferguson's amendment was deleted and the conference report became a compromise. The conference report was adopted by the vote of the House and came to the Senate floor. It was the adoption of this conference report that resulted in emasculating the Supreme Court's decision by exempting the business of insurance from the application of the antitrust laws.

The conference report added language that was not present in either the House or Senate bill. The report stated:

Provided, That After January 1, 1948, the act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance *to the extent that such business is not regulated by the State law.* (Emphasis added).

The final words of that provision determined that for all future time the antitrust laws and the Federal Trade Commission Act should not apply to the business of insurance except in a State which has not regulated the insurance business or to the extent a State has not denied the effect of the Federal acts. A perpetual moratorium had emerged giving the States the power to preempt the field covered by the antitrust laws. Senator Ferguson stated on the floor of the Senate that "regulation by State law" could mean any degree of encroachment upon the Sherman and Clayton Acts which a legislature may desire to exercise, except with respect to acts or agreements of boycott, coercion and intimidation.

I opposed that provision and stated on the Senate floor that I was not willing to give to the States the right to repeal or invalidate the antitrust laws. I saw no reason why we could not give the three year moratorium and then state that the antitrust laws would go into full force and effect. It was reasonable that the States should have been given the opportunity to adjust to the Supreme Court's decision over a period of three years. Yet, to permit the States to allow all offenses condemned by the antitrust acts, with the exception of boycott, coercion and intimidation was the vice of the provision to which I refer.

I am including a letter from President Franklin Delano Roosevelt to Senator Radcliffe of Maryland addressing the subject of the exclusion of insurance from the antitrust laws. The letter is dated January 2, 1945.

My dear Senator Radcliffe:

In your letter of December 20, you suggest that there should be some form of a moratorium during which insurance companies will have an opportunity to readjust their practices in order to bring them into conformity with the Supreme Court decision in the Southeastern Underwriters Association case, and during which legislation might be enacted. The Attorney General advises me that several months ago he told the Senate Judiciary Committee that no new antitrust prosecutions against insurance companies would be instituted during a reasonable readjustment period.

The responsibility for the regulation of the business of insurance has been left with the States; and I can assure you that this administration is not sponsoring Federal legislation to regulate insurance or to interfere with the continued regulation and taxation by the States of the businsess of insurance.

But there is no conflict between the application of the antitrust laws and effective State regulation of insurance companies, and there is no valid reason for giving any special exemption from the antitrust laws to the business of insurance. The antitrust laws do not conflict with affirmative regulation of insurance by the States such as agreed insurance rates if they are affirmatively approved by State officials.

Senator O'Mahoney introduced a bill in the last Congress which would have provided for a moratorium from the Sherman Act, except for acts of boycott, coercion, or intimidation, until March 1, 1946. This would appear to give sufficient time to permit the necessary readjustment to the Supreme Court decision. I would favor legislation of this general character. It would permit the orderly correction of abuses which have existed in the insurance business and would preserve the right of the States to regulate with full responsibility.

Very sincerely yours,

FRANKLIN DELANO ROOSEVELT.

As this letter reflects, President Roosevelt never contemplated that the regulation by the States should be so broad in character that it could be in conflict with and in limitation of the provisions of the Sherman and Clayton Acts.

The conference report that was urgently being pressed upon the Senate contained language that was not in the bill as it passed the Senate. A carte blanche was extended to the States that was contained in no previous legislation, that had passed neither the House nor the Senate, legitimizing the vices against which the antitrust laws were directed. The conference report was on the Senate floor for the first time with language permitting the States authority to repeal the applicability of the antitrust laws to insurance within their boundaries. I had seen conference reports voted on two or three times in the eight years I had spent in the Senate, and I stated that on the Senate floor.

I asked that we express ourselves on the conference report and after our debate was concluded that we express our opinions by roll call.

The result: yeas 68, nays 8 and not voting 20.

The conference report, that already had passed the House giving the States the power to preempt the field covered by the antitrust laws, then passed the Senate as well.

Chairman RODINO. Judge Bell, you may proceed.

TESTIMONY OF HON. GRIFFIN B. BELL, KING & SPAULDING, ATLANTA, GA

Judge BELL. Thank you Mr. Chairman and Mr. Fish. When I became Attorney General, the two most pressing problems in antitrust law were protracted litigation and loopholes in the coverage of the law. Both of these problems hampered the implementation of a uniform, effective national competition policy. I fully supported the formation of the bipartisan multidisciplinary National Commission for the Review of Antitrust Laws and Procedures on which the chairman, Mr. Seiberling and several former members of this subcommittee served with distinction. As you know, after grappling with the difficult issues, the Antitrust Commission formulated a series of recommendations. I am very pleased that Congress has implemented several of the Antitrust Commission's proposals.

The subject of the subcommittee's attention today is the McCarran-Ferguson Act's exemption of the business of insurance from Federal antitrust laws to the extent it is regulated by State law. The Antitrust Commission dealt with insurance as part of its treatment of exemptions. Before turning to that specific segment of the report, I want to recall the Antitrust Commission's conclusions concerning exemptions generally. The Commission found that free market competition should continue to be the principle for organizing our economy. The antitrust laws protect this fundamental American precept which, I am sure, all of us would endorse. The Antitrust Commission found that antitrust exemptions are rarely appropriate—they are justified only "where there is compelling evidence of the unworkability of competition or a clearly paramount social purpose." The Commission further found that exemptions should be as narrow as possible and that a reexamination of existing exemptions was in order.

The current statutory exemption for insurance arose from a curious confluence of historical events. In 1869, the Supreme Court held that the business of insurance was not commerce, and that insurance transactions were not interstate in nature. *Paul* v. *Virginia,* 75 Wall. (8 U.S.) 168 (1869). The decision left an unhindered path for State regulation to evolve. State regulation became the norm.

In subsequent years, judicial interpretation of the interstate commerce clause expanded, and the insurance business grew up as well. In the early 1940's, the Department of Justice's Antitrust Division challenged collusive arrangements in the insurance industry. In a landmark opinion, the Supreme Court found the antitrust laws applicable to the business of insurance. *United States* v. *South-Eastern Underwriters Ass'n,* 322 U.S. 533 (1944). In the next year, 1945, the Congress enacted the McCarran-Ferguson Act, which remains the law to this day. Although subsequent judicial interpretation has narrowed the exemption under that Act, the core business of insurance remains exempt from the antitrust laws.

Congress, I would respectfully observe, appeared to act not so much out of a considered judgment that State regulation and antitrust exemption were better for the country, but to avoid the turmoil that would have resulted from invalidating the existing manner in which the business of insurance was carried on and regulated.

It is entirely appropriate, therefore, that Congress review whether its prior choice was a correct one. There can be no question that a Federal basis for jurisdiction exists, and that insurance is sufficiently important to warrant the attention of even a heavily burdened Congress. Even considered alone, the insurance industry is a huge sector of American commerce. But it is more important than its mere size suggests. Insurance coverage is vital to almost every business and individual in our country. In this respect it is similar to transportation, banking, and communications. And like those other industries, continuous evaluation of the roles of antitrust and regulation is needed. I urge the committee to consider the issues carefully. Deregulation has already swept through the transportation, banking, and telecommunications industries. We should carefully apply the lessons from those other experiences to the insurance business.

The Antitrust Commission made three specific recommendations on insurance, and wrote an illuminating chapter to support its conclusions. I have attached these to my statement, and I would request that they be made part of the subcommittee's record.

Chairman RODINO. Without objection.

Judge BELL. The chapter speaks for itself. I will not review it in detail. I would like, however, to offer some specific insights about the report.

The Antitrust Commission recommended that the broad antitrust immunity of the McCarran-Ferguson Act should be repealed and replaced with more narrowly drawn legislation. This recommendation derives directly from our national commitment to free competition and a system of laws that applies equally to all individuals, granting special treatment only when necessary. The Antitrust Commission identified certain general concerns as valid policy reasons for granting exceptions. In judging the McCarran-Ferguson exemption against these criteria, I turn first to the concern with whether competition is workable in the insurance industry.

The Antitrust Commission found, broadly speaking, that the insurance industry is divided into two categories—life/health insurers and property/casualty insurers. Of these two, life and health insurers are more able to judge the risks they are assuming individually. The record does not show extensive cooperative activities in their branch of the industry. The Antitrust Commission essentially concluded that there is no basis for immunity for them.

For property/casualty insurance, risks are more difficult to gauge. Cooperative efforts, such as loss experience exchanges and pooling of large risks, have been more common, and varying forms of State rate regulation make the problem even more complex. Thus, joint efforts may be necessary for a particular insurance product to be offered at all or for small competitors to stay in business, but they also raise the possibility of artificially inflated prices. The Antitrust Commission acknowledged that rates emerg-

ing from that context were likely to exceed those that would exist in a fully competitive environment, but nonetheless recommended that statutory assurance be given to the lawfulness of a limited number of essential collective activities.

Before leaving the subject of whether competition is workable in the industry, I would like to say that my statement so far is obviously a simplification—perhaps some will say an oversimplification. Insurance is a vastly complicated industry, and doubtless the subcommittee will hear additional arguments about why competitive principles are unworkable. In addressing these arguments, it might be useful for the members to inquire what specific practices would violate the antitrust laws, and to what extent they are necessary for the industry. This should be balanced against the interest of free competition and lower prices that the antitrust laws seek to achieve. If it is unclear whether joint practices necessary for the industry would violate the antitrust laws, the subcommittee should evaluate the desirability of certainty in the law. As the members of this subcommittee are well aware, many would-be antitrust exemptions are predicated on an asserted need for certainty.

The second general area of concern arises from regulatory interests. The Antitrust Commission concluded, correctly in my view, that in balancing regulatory interests, social purposes sometimes take precedence over competition. There is considerable force behind the argument that insurance should be universally and easily available, and many would argue that there should be no discrimination on the basis of such factors as race or sex. These considerations apply with particular force in the types of insurance required by law. The Antitrust Commission recognized that one form of competition among insurers is to attempt to isolate and deal with groups of customers who pose the least risk. The result of unfettered competition may be that some individuals who do not fall into the targeted group have difficulty obtaining insurance or, even worse, cannot obtain it at all. For example, I believe that it would be wrong for our legal system to require an inner city youth to carry auto insurance and then deny it to him or price it so exorbitantly that he cannot afford to purchase it. Harmonizing these social goals with a competitive marketplace is, in my view, the single most challenging question of insurance regulation. And, I must confess, it is a task with no easy solution. There was disagreement on the Study Commission on this question. The Commission recommended that the States place maximum reliance on competition in pursuing these objectives. The Commission recommended further study on these questions as well as on the question of whether Federal legislation was appropriate. A number of Commissioners were less sympathetic to State regulation.

Mr. Chairman, two conclusions emerge from this. First, these matters deserve the subcommittee's close attention. Second—and this is a personal conclusion—this committee is particularly well suited to balance these interests because it is sensitive to both antitrust and broader social issues.

Mr. Chairman, that concludes my prepared statement. I commend you and your subcommittee for undertaking this task, but I do not envy you. Your work will be complex and controversial. But it is important and timely. Thank you.

[The statement of Judge Bell follows:]

TESTIMONY OF HON. GRIFFIN B. BELL

Mr. Chairman and Members of the Subcommittee, when I became Attorney General, the two most pressing problems in antitrust law were protracted litigation and loopholes in the coverage of the law. Both of these problems hampered the implementation of a uniform, effective national competition policy. I fully supported the formation of the bi-partisan multidisciplinary National Commission for the Review of Antitrust Laws and Procedures on which the Chairman, Mr. Seiberling and several former Members of this Subcommittee served with distinction. As you know, after grappling with the difficult issues, the Antitrust Commission formulated a series of recommendations. I am very pleased that Congress has implemented several of the Antitrust Commission's proposals.

The subject of the Subcommittee's attention today is the McCarran-Ferguson Act's exemption of the business of insurance from federal antitrust laws to the extent it is regulated by state law. The Antitrust Commission dealt with insurance as part of its treatment of exemptions. Before turning to that specific segment of the Report, I want to recall the Antitrust Commission's conclusions concerning antitrust exemptions generally. It found that free market competition should continue to be the principle for organizing our economy. The antitrust laws protect this fundamental American precept which, I am sure, all of us would endorse. The Antitrust Commission found that antitrust exemptions are rarely appropriate—they are justified only "where there is compelling evidence of the unworkability of competition or a clearly paramount social purpose." The Commission further found that exemptions should be as narrow as possible and that a re-examination of existing exemptions was in order.

The current statutory exemption for insurance arose from a curious confluence of historical events. In 1869, the Supreme Court held that the business of insurance was not commerce, and that insurance transactions were not interstate in nature. *Paul* v. *Virginia,* 75 U.S. (8 Wall.) 168 (1869). The decision left an unhindered path for state regulation to evolve. State regulation became the norm.

In subsequent years, judicial interpretation of the interstate commerce clause expanded, and the insurance business grew up as well. In the early 1940's, the Department of Justice's Antitrust Division challenged collusive arrangements in the industry. In a landmark opinion, the Supreme Court found the antitrust laws applicable to the business of insurance. *United States* v. *South-Eastern Underwriters Ass'n.,* 322 U.S. 533 (1944). In the next year, 1945, the Congress enacted the McCarran-Ferguson Act, which remains the law to this day.[1] Although subsequent judicial interpretation has narrowed the exemption,[2] the core business of insurance remains exempt from the antitrust laws. Congress, I would respectfully observe, appeared to act not so much out of a considered judgment that state regulation and antitrust exemption were better for the country, but to avoid the turmoil that would have resulted from invalidating the existing manner in which the business of insurance was carried on and regulated.

It is entirely appropriate, therefore, that Congress review whether its prior choice was the correct one. There can be no question that a federal basis for jurisdiction exists, and that insurance is sufficiently important to warrant the attention of even a heavily burdened Congress. Even considered alone the insurance industry is a huge sector of American commerce.[3] But it is more important than its mere size suggests. Insurance coverage is vital to almost every business and individual in the country. In this respect it is similar to transportation, banking and communications. And like those other industries, continuous evaluation of the roles of antitrust and regulation is needed. I urge the committee to consider the issues carefully. Deregulation has already swept through the transportation, banking, and telecommunications industries. We should carefully apply the lessons from those other experiences to the insurance business.

The Antitrust Commission made three specific recommendations on insurance, and wrote an illuminating chapter to support its conclusions. I have attached these to my statement, and I would request that they be made part of the Subcommittee's record. The chapter speaks for itself—I will not review it in detail. I would like, however, to offer some specific insights about the report.

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[1] Act of March 9, 1945, ch. 20, §§ 1-5, 59 Stat. 33-34 (codified at 15 U.S.C. §§ 1011-15 (1976)).
[2] *See, e.g., Group Life & Health Insurance Co.* v. *Royal Drug Co.,* 440 U.S. 205 (1979).
[3] U.S. Dept. of Commerce, *Statistical Abstract of the United States,* 1982-83, p. 500.

The Antitrust Commission recommended that the broad antitrust immunity of the McCarran-Ferguson Act should be repealed and replaced with more narrowly drawn legislation. This recommendation derives directly from our national commitment to free competition and a system of laws that applies equally to all individuals, granting special treatment only when necessary. The Antitrust Commission identified certain general concerns as valid policy reasons for granting exceptions. In judging the McCarran-Ferguson exemption against these criterias, I turn first to the concern with whether competition is workable in the insurance industry.

The Antitrust Commission found, broadly speaking, that the insurance industry is divided into two categories—life/health insurers and property/casualty insurers. Of these two, life/health insurers are more able to judge the risks they are assuming individually. The record does not show extensive cooperative activities in their branch of the industry. The Antitrust Commission essentially concluded that there is no basis for immunity for them.

For property/casualty insurance, risks are more difficult to guage. Cooperative efforts, such as loss experience exchanges and pooling of large risks, have been more common, and varying forms of state rate regulation make the problem more complex. Those joint efforts may be necessary for a particular insurance product to be offered at all or for small competitors to stay in business, but they also raise the possibility of artificially inflated prices. The Antitrust Commission acknowledged that rates emerging from that context were likely to "exceed those that would exist in a fully competitive environment," but nonetheless recommended that statutory assurance be given to the "lawfulness of a limited number of essential collective activities."

Before leaving the subject of whether competition is workable in the industry, I would like to say that my statement so far is obviously a simplification—perhaps some will say an oversimplification. Insurance is vastly complicated industry, and doubtless the Subcommittee will hear additional arguments about why competitive principles are unworkable. In addressing these agruments, it might be useful for the members to inquire what specific practices would violate the antitrust laws, and to what extent they are necessary for the industry. This should be balanced against the interests of free competition and lower prices that the antitrust laws seek to achieve. If it is unclear whether joint practices necessary for the industry would violate the antitrust laws, the Subcommittee should evaluate the desirability of certainty in the law. As the Members of this Subcommittee are well aware, many would-be antitrust exemptions are predicated on an asserted need for certainly.

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Two conclusions emerge from this. First, these matters deserve the Subcommittee's close attention. Second—and this is a personal conclusion—this Committee is particularly well-suited to balance these interests because it is sensitive to both antitrust and broader social issues.

Mr. Chairman, that concludes my prepared statement. I commend you and your Subcommittee for undertaking this task, but I do not envy you. Your work will be complex and controversial. But it is important and timely.

Thank you.

Chapter 11: Insurance

RECOMMENDATIONS

1. The current broad antitrust immunity for the business of insurance granted by the McCarran-Ferguson Act should be repealed. In its place, narrowly drawn legislation should be adopted to affirm the lawfulness of a limited number of essential collective activities under the antitrust laws.

2. States should place maximum reliance on competition in pursuing their regulatory objectives. Although the Commission recognizes that the state action doctrine would exempt from antitrust scrutiny private action compelled and effectively regulated by the state to achieve legitimate social goals, we nonetheless believe that narrowly targeted antidiscrimination, disclosure, and similar statutes are preferable to such anticompetitive economic regulation as state ratesetting.

3. Further study of economic regulation of insurance should be undertaken by the relevant Congressional committees or by a special commission established by the President. The study should include:

(a) the appropriate regulatory response to problems of equity and discrimination in insurance rates;

(b) the relationship between such regulation and the availability and affordability of insurance;

(c) procedures by which such regulatory goals may be achieved in the least anticompetitive manner; and

(d) the appropriate role, if any, of federal legislation with respect to the business of insurance.

Under the McCarran-Feguson Act of 1945,[1] the "business of insurance" is exempted from the Sherman, Clayton, and Federal Trade Commission Acts to the extent that it is "regulated by state law." Utilizing the freedom granted by that statute, the states have enacted regulatory schemes of various types to supervise the ratesetting activities of property and liability insurance, including the activities of industry-controlled rate bureaus. Under the prevailing interpretation of McCarran-Ferguson, insurance company activities may be exempted from the coverage of the antitrust laws by the mere presence of a state regulatory scheme, without regard to whether these regulatory powers have been utilized to supervise the insurance industry effectively. As a result, various types of collective insurance company behavior are, as a practical matter, wholly free from control by either state regulation or the federal antitrust laws.

The Commission believes that the current immunity is not only overly broad, but also unnecessary: those collective activities by insurers that are essential to the functioning of an efficient, competitive industry would likely pass muster under the traditional rule of reason analysis of Sherman Act Section 1. Similarly, where collective activity or other insurance company behavior is affirmatively mandated by a state in its capacity as sovereign, and effectively supervised by independent state officials, such behavior would fall within the judicially recognized "state action" exception to the antitrust laws.

Although there is general consensus that most segments of the industry are competitively structured, and that enhanced competition is an appropriate goal of state regulatory policy, many states adhere to regulatory schemes requiring prior approval of insurance rates, thereby discouraging independent pricing behavior. The costs of continuing the present system are not significant: where members of a competitively structured industry are allowed collectively published industry-wide rates—often without effective state supervision—in a regulatory environment that encourages uniform pricing, insurance premiums are likely to be higher than under a system that relies more heavily on independent pricing decisions. In some prior approval states, regulation may in fact keep rates below levels that would be produced by competition. Unduly low rates, however, may exacerbate availability problems.

Critics of proposals for reform do not argue that the existing board antitrust immunity and state regulatory mechanisms are necessary. Instead, some argue that complete removal of antitrust immunity will create undue uncertainty concerning the lawfulness of a few joint activities regarded as essential. Others contend that unregulated competition among insurers will have effects that are contrary to important social policies.

While the Commission has substantial sympathy for some of these arguments, it does not believe that they justify retention of the present system. Rather, the current broad antitrust immunity for insurance should be repealed, with provisions

[1] 15 U.S.C. §§ 1011-1015 (1976).

made for statutory assurance of the lawfulness of a limited number of essential collective activities. Further, state regulatory schemes should be structured to place maximum reliance on independent, competitive behavior. The Commission recognizes, however, that additional study is necessary to resolve questions of social policy raised by the functioning of the insurance market and to determine the appropriate role of the federal government in resolving problems of insurance policy.

A number of Commissioners believe that social policy goals of equity and availability of insurance are better addressed by disclosure and antidiscrimination laws than by state economic regulation. These Commissioners believe the further study recommended here should aim toward a federal statute prohibiting certain types of anticompetitive state regulation to complement McCarran-Ferguson repeal.

THE INSURANCE INDUSTRY

With assets of approximately $434 billion[2] and annual premium payments of about $130 billion,[3] the insurance industry is clearly an important sector of the economy. The industry is itself as complicated and diverse as is the set of risks from which consumers desire protection. In general, this industry is divided into two major components: life-health insurance, and property-liability insurance.

A key feature of all insurance "products" is that the insurance company does not know its costs at the time of sale. Faced with this uncertainty insurers need accurate information based on credible data to estimate future losses and set premium rates. The information and risk problems faced by life and health insurers are less severe than those of the property-liability industry, with life expectancy tables and health data being readily accessible and more predictable for future periods. As a result, life-health insurers have generally not engaged in extensive cooperative activities. Nor have they been subject to extensive state rate regulation. Thus there is no justification for continued antitrust immunity in these areas.[4] Consequently, the debate concerning the application of the antitrust laws to cooperative insurance activities and the reduction of state regulation of insurance ratemaking has focused on the property-liability lines. The Commission, therefore, targeted its inquiry on the property and liability lines.

In order to minimize uncertainty, property-liability insurers have engaged in cooperative assembling of loss statistics and in the sharing of large risks through pooling or other reinsurance mechanisms. Traditionally, property-liability insurers have utilized "industry advisory organizations" or rate bureaus. The activities of these organizations often go beyond the collection of industry loss data, and include the averaging of such information for specific risk classifications and the "trending" of the data for past years to predict probable loss expenses for specified future rate periods. After an expense component (administrative and sales overhead) is added, the resulting prices are published as "bureau rates" for the use of a bureau's members.

Characterized by a lack of significant economies of scale,[5] relatively standardized policies,[6] and low barriers to entry, the property-liability industry appears competitively structured. There are about 2,886 property-liability insurance companies of which the eight largest earned only 31.9 percent of total industry premiums in 1977, and only 38.7 percent of auto premiums.[7] In several lines, including automobile insurance, many firms deviate significantly from bureau rates except where such independent behavior is prohibited by state law.[8] Additionally, some of the larger automobile insurers do not utilize bureau rates since their policyholder base is large enough to permit them to use their own loss experience in setting premiums.

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[2] Insurance Information Institute, Insurance Facts, at preface (1977).

[3] *Id.* at 11 (1976 data).

[4] There may be problems involving lack of adequate consumer information in these lines which might be alleviated by regulatory intervention.

[5] Joskow, *Cartels, competition, and regulation in the property-liability insurance industry,* 4 Bell J. Econ. & Mgmt. Sci. 375, 388 (1973).

[6] National Association of Insurance Commissioners (NAIC), Monitoring Competition: A Means of Regulating the Property and Liability Insurance Business 370 (1974) [hereinafter cited as NAIC Report].

[7] Best's Insurance News Directory, July 10, 1978; *id.* July 31, 1978.

[8] *See* A Report of the U.S. Department of Justice to the Task Group on Antitrust Immunities: The Pricing and Marketing of Insurance 28–29 (1977) [hereinafter cited as Justice Insurance Report].

THE DEVELOPMENT OF STATE REGULATION OF INSURANCE AND THE INDUSTRY'S EXEMPTION

In 1868, the Supreme Court ruled that an insurance contract did not constitute "commerce" within the meaning of the Commerce Clause of the Constitution,[9] and thus placed the industry outside the federal government's powers. Beginning in 1911, several states passed statutes authorizing the fixing of fire insurance rates by rating bureaus under the general supervision of their insurance departments.[10] In the two-thirds of the states that had rate regulaiton in 1944, effective control over private bureau rates was often nonexistent.[11] Thus, insurance ratemaking for property-liability lines was largely in the hands of industry-controlled rate bureaus.

In its 1944 *South-Eastern Underwriters* decision, the Supreme Court, reversing precedent, held that transactions in insurance across state lines constituted interstate commerce and were subject to the federal antitrust laws.[12] The Supreme Court's action distressed much of the insurance industry. Similarly, state regulators feared that many state controls over insurance companies, especially tax statutes, might be invalidated as undue burdens on interstate commerce.[13]

To alleviate these concerns, in 1945 Congress passed the McCarran-Ferguson Act. The Act specifically reaffirmed the power of the states to regulate and tax insurance companies. In addition, it provided that no act of Congress, unless specifically relating to the business of insurance, was to be construed to invalidate or supersede state insurance regulation. The antitrust laws were to remain applicable to the business of insurance but only "to the extent that such business is not regulated by State Law." [14] By 1951, in response to McCarran-Ferguson, all states had adopted fire and casualty rating laws. Generally these statutes were patterned after a model law developed by the National Association of Insurance Commissioners (NAIC). That law required prior approval of insurance rates by state officials.[15]

Although the model statute contained language making it technically possible for member insurance companies to deviate from bureau rates, independent behavior was difficult and many insurers adhered to agreements not to deviate from bureau rates.[16] In the late 1950's, market conditions began to change, and some insurers began to establish independent rates. This movement was given a strong impetus by the growing number of direct insurance writers, who were able to charge significantly lower premiums. Many insurers also desired a rate structure more responsive to loss experience and inflationary pressures.[17] As a result, some states adopted statutory changes making it easier for member companies to deviate from bureau rates and for insurers to participate in the activities of a bureau for some lines of insurance and not for others.[18]

Today, there are a variety of state insurance regulatory mechanisms reflecting varying degrees of reliance on competition. In a few states, such as Massachusetts, a state agency sets rates. Other states require that insurers join a rate bureau and adhere to its rates, although deviations from bureau rates may be allowed with insurance department approval.[19] At the other extreme, Illinois, since 1971, has had no rating law at all and insurers are free to set their rates without state supervision.[20]

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[9] Paul v. Virginia, 75 U.S. (8 Wall.) 168, 183 (1868).

[10] Wiley, *Pups, Plants and Package Policies—Or the Insurance Antitrust Exemption Re-examined*, 6 Vill. L. Rev. 281, 313-14 (1961).

[11] Kimball & Boyce, *The Adequacy of State Insurance Rate Regulation: The McCarran-Ferguson Act in Historical Perspecitve*, 56 Mich. L. Rev. 545, 551-52 (1958).

[12] United States v. South Eastern Underwriters Ass'n, 322 U.S. 533 (1944).

[13] Kimball & Boyce, *supra* note 11, at 554.

[14] 15 U.S.C. § 1012(b) (1976). The Sherman Act, however, was to remain fully applicable to any agreement to "boycott coerce, or intimidate, or act of boycott, coercion, or intimidation." *Id.* § 1013(b).

[15] Prepared Statement of the National Association of Insurance Commissioners, to the Antitrust Commission 16-17 (July 27, 1978) [hereinafter cited as NAIC Prepared Statement].

[16] Justice Insurance Report, *supra* note 8, at 23.

[17] NAIC Report, *supra* note 6, at 64-65.

[18] Another indication of the trend toward more competitive state regulatory systems was the determination in 1968 by the National Association of Insurance Commissioners to endorse open competition style regulation. NAIC Prepared Statement, *supra* note 15, at 24-25.

[19] NAIC Report, *supra* note 6, at 54-57.

[20] Collecting, averaging, and projecting anything other than loss data are not specifically authorized by Illinois law, *see* Ill. Ann. Stat. ch 73, §§ 735A-1 to 735A-15 (1978 Supp.) (Smith-Hurd), so Illinois rate bureaus do not engage in those activities which would subject them to liability under the antitrust laws.

The majority of states continue to use the prior approval mechanism, which permits states to review premiums before they come into effect and disapprove them if they are found to be excessive, inadequate, or unfairly discriminatory. Under most prior approval statutes, a rate is deemed approved if it is not disapproved within a specific period of time. At least 17 states, however, now utilize various "open competition" statutes which permit insurers to introduce new rates without delay:[21] States generally do retain power to investigate rates once they are in effect to determine their lawfulness under the traditional standards utilized in prior approval states. According to the NAIC, open competition states account for approximately 48 percent of personal property and liability premiums, although certain regulatory mechanisms in some of these states may limit the extent to which actual open competition occurs.[22]

In sum, the property-liability industry has undergone a significant change since the passage of the McCarran-Ferguson Act in 1945. No longer can the industry be characterized as dominated by tight cartels, or by uniform regulatory supervision of collective ratemaking. The justification for antitrust immunity and of state regulation must therefore be evaluated in light of present industry conditions and emerging concerns about the role of competition in achieving particular social goals.

THE PRESENT BROAD INSURANCE IMMUNITY

Both the language of the McCarran-Ferguson Act, and the Act's legislative history, make clear that the purpose of the insurance immunity was to permit state regulatory mechanisms to function without federal intervention, and not to give the industry broad license to operate without antitrust scrutiny. As the Supreme Court recently noted, the purpose of making antitrust immunity dependent on state regulation was to end the " 'system of private government' " prevalent in the insurance industry before McCarran-Ferguson, and while agreements among insurers might be permitted, " 'public supervision of agreements is essential.' "[23]

Nevertheless, as historically interpreted by the courts, the exemption has in fact served as a broad grant of immunity for unsupervised collective behavior by insurers. Courts have refused to require that the state regulation be comprehensive or effective as a condition for permitting immunity to attach. Rather, as one court put it, "if a State has generally authorized or permitted certain standards of conduct, it is regulating the business of insurance under the McCarran Act."[24] Moreover, the ineffectiveness of state regulation does not invalidate the immunity. One Court of Appeals simply brushed aside allegations that the state of Ohio had never investigated a rate filing and did not possess the actuarial personnel to do so. It ruled that nothing in the McCarran-Ferguson Act supports "the thesis that the Act does not apply when the state's scheme of regulation has not been effectively enforced."[25] While some judges have disagreed with this approach, their views have been confined to dissent or dictum.[26]

The breadth of the antitrust immunity created by the prevailing interpretation of state regulation has been further expanded by the broad interpretation given to the "business of insurance." These activities include not only "the type of policy which could be issued, its reliability, interpretation and enforcement,"[27] but also the setting of agents' commissions and the relationship between insurance companies and agents,[28] and the selling and advertising of insurance policies.[29]

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[21] NAIC Prepared Statement, *supra* note 15, at 19 & n.30.

[22] *Id.* at 19.

[23] St. Paul Fire & Marine Ins. Co. v. Barry, 98 S. Ct. 2923, 2933-34 (1978) (quoting Senator O'Mahoney, floor manager of the McCarran-Ferguson Act).

[24] California League of Independent Ins. Producers v. Aetna Cas. & Sur. Co., 175 F. Supp. 857, 860 (N.D. Cal. 1959).

[25] Ohio AFL-CIO v. Insurance Rating Bd., 451 F.2d 1178, 1184 (6th Cir. 1971), cert. denied, 409 U.S. 917 (1972).

[26] Ohio AFL-CIO v. Insurance Rating Bd., 409 U.S. 917, 917-18 (1972) (Douglas, J., dissenting from denial of certiorari); Crawford v. American Title Ins. Co., 518 F.2d 217, 221 (5th Cir. 1975) (Godbold, J., dissenting); Fleming v. Travelers Indem. Co., 324 F. Supp. 1404, 1406 (D. Mass. 1971) (sham or pretense of regulation insufficient under McCarran-Ferguson) (dictum); cf. United States v. Chicago Title & Trust Co., 242 F. Supp. 56, 65-66 (N.D. Ill. 1965) (citation to law review note arguing that state law must provide for effective administration of insurance laws in order to qualify for exemption).

[27] SEC v. National Securities, Inc., 393 U.S. 453, 460 (1969).

[28] California League of Independent Ins. Producers v. Aetna Cas. & Sur. Co., *supra* note 25, at 860.

[29] FTC v. National Cas. Co., 357 U.S. 560, 562-63 (1958) (per curiam). Recently, some courts have also significantly expanded the "business of insurance" to include relationships between

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As presently interpreted, the McCarran-Ferguson Act effectively may immunize from the antitrust laws a broad range of anticompetitive activities which, in fact, serve no federal or state objectives. as one witness put it:

"This indiscriminate immunity is granted whether or not the practice is necessary for the effective functioning of the insurance industry, the improvement of the insurance product, or the fulfillment of state regulatory goals; whether or not the practice is condoned, authorized or punished by state authorities; and whether or not it is anticompetitive or anticonsumer."[30]

Just as importantly, the presence of antitrust immunity has permitted insurers and state regulators to avoid any inquiry into the appropriate limits that should be placed on insurance companies' collective activities. "[T]he states never at any point seriously considered what ought to be the minimum permissible limits of concerted activity on automobile and homeowners' ratemaking."[31] The need for a discriminating approach to collective activity is demonstrated by Illinois' experience. In many states, insurance companies receive from the bureau a "bureau rate" reflecting not only loss data but projected average administrative expenses for the insurers. On the other hand, Illinois, which has no rating law, permits rate bureaus only to collect and compute statistics based on the loss component of insurance premiums.[32] Consequently, unlike insurers in other states, each Illinois insurer is responsible for developing rates that reflect its own expense projections. This more limited role for rate bureaus apparently has been functioning in a satisfactory manner, thereby indicating the unnecessary breadth of collective information sharing in a number of states.

While the Commission is not aware of any studies that directly estimate the cost of the insurance exemption, we believe that, on the basis of the analytic framework developed in Chapter Nine, and by the Economic Advisory Panel Report,[33] the cost is significant. Under McCarran-Ferguson, competing insurers are able collectively to publish industry rates for future periods based on industry average costs, often without effective governmental supervision and under regulatory mechanisms that, in many states, discourage independent pricing behavior. It seems likely that the resulting rates exceed those that would exist in a fully competitive environment.

The Commission found little, if any, evidence in favor of the present blanket immunity. Rather, some testimony and submissions to the Commission argued that application of the antitrust laws might undercut the ability of states to regulate insurance,[34] or that it would place in doubt the legality of a few, specified practices that were argued to be essential to the functioning of a competitive industry.[35]

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insurers and third parties who provide services to policy holders on the rationale that such agreements, which generally set the prices that the providers will charge policy holders, are arguably designed to influence directly premium levels by controlling costs. Proctor v. State Farm Mutual Auto. Ins. Co., 561 F.2d 262, 268-69 (D.C. Cir. 1977), *petition for cert. filed*, 46 U.S.L.W. 3294 (Oct. 19, 1977) (No. 77-580); Frankford Hosp. v. Blue Cross of Greater Phil., 417 F. Supp. 1104 (E.D. Pa. 1976), *aff'd per curiam*, 554 F.2d 1253 (3d Cir.), *cert. denied*, 434 U.S. 860 (1977); Travelers Ins. Co. v. Blue Cross of W. Pa., 481 F.2d 80 (3d Cir.), *cert. denied*, 414 U.S. 1093 (1973), Manasen v. California Dental Servs., 424 F. Supp. 657 (N.D. Cal. 1976). The validity of this proposition is presently before the Supreme Court. Royal Drug Co., Inc. v. Group Life & Health Ins. Co., 556 F.2d 1375 (5th Cir. 1977) (third-party agreement held subject to antitrust laws), cert. granted, 435 U.S. 903 (1978). If the Court permits such third-party arrangements to escape antitrust scrutiny, the scope of the exemption will be substantially broadened.

[30] Prepared Statement of Albert A. Foer, Assistant Director, Bureau of Competition, Federal Trade Commission, to the Antitrust Commission 3 (Oct. 17, 1978) [hereinafter cited as Foer Prepared Statement].

[31] *Antitrust Commission Hearings* 69 (July 27, 1978, afternoon session) (testimony of Donald McHugh, Vice President and General Counsel, State Farm Mutual Insurance Companies).

[32] Similarly, in the commercial fire area, the Illinois Bureau supplies members with data that establishes only the relative risks among particular properties but does not determine an actual rate which may be charged by members. Justice Insurance Report, *supra* note 8, at 196.

[33] Paul L. Joskow. Competition and Regulation in the Property/Casualty Insurance Industry, in Report of the Economic Advisory Panel to the National Commission for the Review of Antitrust Laws and Procedures 5-6 (Nov. 9, 1978) [hereinafter cited as Joskow Report].

[34] *See, e.g., Antitrust Commission Hearings* 80-81 (Oct. 17, 1978, morning session) (testimony of Andre Maisonpierre, Vice President Alliance of American Insurers) (McCarran-Ferguson repeal would ultimately lead to increased federal regulation); id. at 55-56 (July 27, 1978, afternoon session) (testimony of Wesley Kinder, Insurance Commissioner, State of California, on behalf of the National Association of Insurance Commissioners); NAIC Prepared Statement, *supra* note 15, at 29-40.

[35] *See, e.g., Antitrust Commission Hearings* 73-74 (Oct. 17, 1978, morning session) (testimony of Arthur C. Mertz, President, National Association of Independent Insurers); *Id.* at 66-67 (July 27, 1978, afternoon session) (testimony of T. Lawrence Jones, President, American Insurance Association); NAIC Prepared Statement, supra note 15, at 50-51.

With respect to the first concern, we note that application of the antitrust laws to a particular industry does not oust a state regulatory agency from its jurisdiction. States remain free to implement programs designed to further the public interest as they define it.[36] State attempts to deal with problems of discrimination, equity, affordability and availability clearly fall within this principle. Moreover, under the state action exemption, private activities properly mandated and effectively supervised would not give rise to antitrust liability on the part of the private participants.[37] Elimination of the existing insurance antitrust immunity thus does not threaten the primary role of the states as regulators of insurance activities.[38]

On the second point, the extensive testimony before the Commission concerning the potential impact of the full application of the antitrust laws to traditional collective behavior by insurance firms does involve significant policy questions. In its 1977 report, *The Pricing and Marketing of Insurance,* the Department of Justice states that, under traditional antitrust theory and precedent, competing businesses can undertake joint activities in which there are economies of scale and which competing businesses can not undertake alone as long as such activities do not involve unnecessarily anticompetitive restraints. The Report, however, cautioned that the projection of future prices, or of large components of future prices, would raise serious antitrust questions. Consequently, the Report suggested that, where possible, insurance firms should rely on independent consulting organizations, rather than industry-controlled rate bureaus, to make those calculations. By so doing, antitrust risks could be minimized.[39]

While the basic accuracy of the Report's legal analysis was not disputed before the Commission, several witnesses argued that it was unwise to entrust a determination of the lawfulness of particular activities to case-by-case adjudication.[40] Not only would the government's legal arguments not bind either private plaintiffs or the courts, but the issue of ultimate lawfulness of specific practices under a rule of reason analysis would require careful balancing of possible anticompetitive effects against procompetitive benefits. Since such a rigorous analysis had not been necessary previously due to the presence of antitrust immunity, insurers might remain uncertain whether activities they believe essential, or otherwise procompetitive, were legal. A wrong guess could subject the insurers to substantial antitrust liability, while an overly cautious posture might deny insurers and the public the benefits of lawful efficiencies.

Given this concern, the Commission believes that new legislation, designed to confirm the lawfulness of enumerated essential collective activities, should replace the existing overly broad immunity.

THE JOINT ACTIVITIES THAT SHOULD BE LAWFUL FOR ANTITRUST PURPOSES

The Commission's recommendation that Congress adopt legislation setting out specific behavior that would be lawful for antitrust purposes is not intended to be a recommendation for antitrust immunity in the usual sense. That is, we do not recommend that Congress determine specific areas of insurance company behavior in which the principles of competition and methods of antitrust analysis are to be put aside because of a legislative determination that competition is either undesirable or unworkable in those circumstances.

Rather, we believe that Congress should pursue this task from a much more limited perspective, namely, that of assisting the transition of the insurance industry from that of a sector of the economy that has developed essentially devoid of antitrust scrutiny to one in which the antitrust statutes are applicable, consistent with federalism principles. In endorsing this approach, caution must be exercised to ensure that the occasion is not utilized as an indirect method for reintroducing broad antitrust immunity for the industry.

Consequently, in determining the kinds of activities that should be included in any such affirmative legislation, three criteria should be used: first, is the proposed joint activity so important to the insurance process that uncertainty as to its legal

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[36] *See* New York Motor Vehicle Bd. v. Orrin W. Fox Co., 47 U.S.L.W. 4017 (Dec. 5, 1978).

[37] *See e.g.,* Foer Prepared Statement, *supra* note 30, at 7, 12.

[38] Because its jurisdiction is limited to exemptions from the "antitrust laws," the Commission made no inquiry concerning the effects of removal of the McCarran-Ferguson immunity in subjecting the insurance industry to Federal Trade Commission jurisdiction.

[39] Justice Insurance Report, *supra* note 8, at 177-78.

[40] *See, e.g., Antitrust Commission Hearings* 73-76 (Oct. 17, 1978, morning session) (testimony of Arthur C. Mertz); id. at 53 (July 27, 1978, afternoon session) (testimony of Wesley Kinder); Prepared Statement of the National Association of Independent Insurers, to the Antitrust Commission 11-13 (July 26-27, 1978).

status would severely limit the ability of the industry to function in an efficient and competitive manner; second, is the activity in question one presently subject only to antitrust principles of broad generality rather than relatively detailed case law that would illuminate its antitrust legality, *i.e.*, is its lawfulness truly uncertain; third, under a rule of reason analysis would the activity in question be found to have the probable effect of not lessening competition within the industry. These are broad, decisional criteria. Particular conduct must be shown to meet these criteria by the proponents of the inclusion of that conduct.

The Commission does not have a sufficient record to make a recommendation with respect to each specific area of potential concern to insurers. On the basis of the information presented, however, we can offer some initial recommendations regarding the areas of key concern articulated by Commission witnesses.

The Commission heard extensive testimony that it is necessary for many insurers to utilize pooled statistics concerning past losses to develop actuarially sound data on the expected future losses for particular risk classifications. In addition, it was argued that joint activity is necessary to "trend" past data to make it useful for projecting expected losses in future rate periods, to compile and disseminate information concerning the administrative expense component of rates, and to promulgate bureau rates to its members in a form which might be more directly usable as an actual insurance rate without significant actuarial modification.[41]

Witnesses also stated that failure to permit several or all of these activities could have a harsh impact on many insurers, particularly small insurers, who would be unable on their own to develop economically all the data needed to establish their insurance premiums. As a result, some insurers might have to withdraw from particular lines or geographic markets, thus reducing the number of competitiors.[42] In the face of such claims, the issue becomes "[p]recisely where . . . the costs of cooperative behavior, in terms of price rigidity and a retardation in innovative ratemaking, outweigh the benefits associated with economies of scale" in rate calculation.[43]

We agree that in the case of joint pooling and calculation of past loss data efficiencies are likely to be great, and the anticompetitive potential small. As noted in the Department of Justice's Report, calculation of past cost data by an industry association for use by its members generally has been considered lawful by the antitrust courts.[44] Moreover, in the case of the insurance industry, where many firms will not have a sufficiently large policyholder base to make their own actuarially sound computations, such collective activity is likely to have a procompetitive effect. Increased numbers of small firms will be able to participate in the market on the basis of actuarial data as sound as that available to large firms.

In addition, some witnesses testified that many small firms could not independently trend past loss data supplied by bureaus.[45] They argued that the number of actuaries is limited, and that independent consulting organizations might not be available. The Commission, while questioning such claims, recognizes that this contention deserves inquiry by Congress.

The justification for bureau compilation and projection of the administrative expense component of bureau rates is even less clear.[46] Relevant expense data will normally be in the exclusive control of each individual company. Thus, we are unable to conclude that the vast majority of insurers would not be capable of developing independent premiums from pooled loss data.[47] The satisfactory operation of

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[41] *See, e.g., Antitrust Commission Hearings* 98-100 (Oct. 17, 1978, morning session) (testimony of Arthur C. Mertz); Submission of Antitrust Exemptions Committee Task Force, Section of Antitrust Law, American Bar Association, to the Antitrust Commission 3-7 (June 16, 1978).

[42] *See, e.g.,* Prepared Statement of the Alliance of American Insurers, to the Antitrust Commission 32-35 (July 26, 1978).

[43] Joskow Report, *supra* note 33, at 10-11.

[44] Justice Insurance Report, supra note 8, at 91-118.

[45] *See, e.g., Antitrust Commission Hearings* 98-100 (Oct. 17, 1978, morning session) (testimony of Arthur C. Mertz).

[46] The Economic Advisory Panel paper on insurance, for example, concluded that "while some of the cooperative activities that are now engaged in are indeed necessary to provide insurance efficiently, the range of necessity that is claimed by the industry, especially for class rate risks, is excessive." Joskow Report, *supra* note 33, at 12.

[47] The Federal Insurance Administration stated one of the major arguments for denying such extensive collection action:

"FIA has long and persistently advocated that insurers be denied any right to act in concert in respect to the expense component of the rate structure. Thus, FIA's position is that insurers should not only be allowed, but should be required, to compete with respect to expenses. Such competition in the expense element of the rate structure can only benefit the insurance consumer since its effect is greater efficiency. . . ."

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Illinois rate bureaus which limit their activities to only the collection of loss data indicates that the joint collection of expense data and publication of advisory rates is unnecessary.[48]

The Commission also received testimony that arrangements by which insurers provide for the reinsurance of risks by the pooled underwriting of large risks merit special antitrust consideration.[49] On the record before us, we are unable to reach a conclusion with respect to this contention, but agree that it also merits Congressional attention. We do note, however, that many firms, such as those engaged in construction and securities underwriting, frequently utilize joint ventures to permit firms to share the risk of a major undertaking or to enable small firms to participate collectively in activities when their resources are insufficient to permit them to participate individually. Proponents of this position thus have the clear burden of demonstrating why traditional antitrust analyses applicable to joint ventures in other sectors of the economy would not adequately protect both the need of insurers to spread risk and the interest of the public in being protected from joint ventures that unduly eliminate competition.

These recommendations are not dependent on changes in state law. Application of the antitrust laws—with the appropriate legislative clarification of the lawfulness of specific practices—should not only help achieve the competitive goals of antitrust, but also should accommodate and supplement the goals of state insurance regulation while preventing unneeded uncertainty in the provision of insurance services.

THE NEED TO MAXIMIZE COMPETITION UNDER STATE INSURANCE REGULATION

There remains the matter of state economic regulation itself. Given the competitively structured nature of the insurance industry, it is not surprising that the evidence presented to the Commission appears to demonstrate the regulatory schemes requiring prior state approval of rates have had an adverse effect on competition. The 1977 Department of Justice Report found that the benefits of open competition, when compared with prior approval regulation, included less adherence to bureau advisory rates, rates as reasonable or lower than in other states, and greater efficiency in distribution.[50] Other studies and economic commentaries generally have confirmed these findings.[51] Indeed, two recent reports concerning insurance company behavior in Illinois, the only state having no insurance rate regulation, came to the indentical conclusion that performance was, on average, as good or better than that in comparable, more regulated states.[52]

While some submissions to the Commission attempted to refute particular technical aspects of these studies, the consensus of the comments received by the Commission was that studies showing that open competition provided a better environment than did prior approval regulation were essentially correct. For example, the American Insurance Association concluded that the Justice Department Report "develops a convincing case that competitive rate laws serve the public much more effectively than laws requiring prior approval of rates." [53]

Many of those who favor substantial state regulatory intervention do so not from a belief that the industry is structured noncompetitively, but from a fear that unregulated competition may have adverse social effects.[54] Many states require indi-

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Submission of Gloria M. Jimenez, Federal Insurance Administrator, Dep't of Housing and Urban Development to the Antitrust Commission 9 (Nov. 6, 1978). Several other witnesses agreed that common expense data and rate projections did not warrant protection from antitrust scrutiny. *See e.g., Antitrust Commission Hearings* 89-90 (Oct. 17, 1978, morning session) (testimony of Albert A. Foer, Assistant Director, Bureau of Competition, Federal Trade Commission); *id.* at 97 (testimony of James M. Stone, Commissioner of Insurance, Commonwealth of Massachusetts); *id.* at 69 (July 27. 1978, afternoon session) (testimony of Donald McHugh).

[48] *See Antitrust Commission Hearings* 41 (July 27, 1978, afternoon sesssion) (testimony of Donald McHugh), and note 20 *supra.*

[49] The generally noted reasons for significant pooling in this industry are the need to accommodate particularly large and unusual riska and the desire to enable smaller cmpanies to collectively compete for the bigger risks that would otherwise all turn to the large companies. *See generally* NAIC Prepared Statement, *supra* note 15, at 43-45.

[50] Justice Insurance Report, *supra* note 8, at vi-vii, 36-90.

[51] *See, e.g.,* Joskow Report, *supra* note 33, at 5-6.

[52] Illinois Dept. of Insurance, Illinois Automobile Insurance Rate Study (1977); Illinois Insurance Laws Study Commission, The Automobile Insurance Rate Regulatory System in Illinois: A Comparative Study (1977).

[53] Prepared Statement of T. Lawrence Jones, President, American Insurance Association, to the Antitrust Commission 8 (July 27, 1978).

[54] *See, e.g., Antitrust Commission Hearings* 61-62 (Oct. 17, 1978, morning session) (testimony of James M. Stone); id. at 54-55 (July 27, 1978, afternoon session) (testimony of Wesley Kinder). *See*

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viduals to have specified levels of insurance coverage as a prerequisite for operating an automobile. Consequently, society, it is argued, has an interest in the availability of insurance to all individuals at a price that is within their reach, and at premiums that do not unfairly discriminate among individuals on the basis of certain arbitrary characteristics.

The central concern of those who believe that unregualted rate competition is at odds with the achievement of social objectives is "selection competition," the process by which competitive insurance markets tend to classify people by risk groups and charge them accordingly.[55] The impetus of competition is to segment markets into finer and finer classifications. Since premiums from each classification must cover expected losses from that class, groups with presumed high risk potential will be charged higher rates. In practice, such classifications may be seen as unfair, since they may place a particular driver in a high cost category despite "clean behavior". Moreover, those charged higher rates may be individuals, such as young inner-city males, with minimal financial resources.[56] Insurance for them thereby becomes unaffordable. Conversely, the individuals with higher income may well turn out to be those charged the lowest rates.

Thus, some of the categories that have been traditionally utilized to determine insurance premiums have been argued to be unfair because they may be based on socially "suspect" criteria or classifications over which the individual has little or no control, i.e., age, location (density of traffic or potential for theft), sex, and marital status.

Critics of selection competition argue that regulators may have an obligation to intervene in the functioning of the market to ensure that the pricing and availability of insurance comport with social objectives of equity and fairness. Such concerns may also include the notion that the burden of higher expected losses in places like the inner city should be shared by all since some of the factors contributing to higher risks may be viewed as the responsibility of society at large.[57]

The Commission believes that such concerns are legitimate and must be carefully evaluated in terms of defining the appropriate role of state insurance regulation. The Commission, however, is also impressed by arguments, including the testimony of our economic advisory panel, that establishment of regulatory solutions to ensure availability and affordability may lead to possible distortions requiring additional state intervention.[58]

For example, to the extent that classifications are restricted by regulation and contain individuals of varying potential risk, insurers have an incentive to reject those whose predicted losses are supposedly greater than the premium established for the class. Similarly, if a state limits rates that may be charged for certain individuals, insurers may not write coverage for those groups for whom the expected loss is greater than the premium. Such difficulties may also lead to an increased use of "residual market" mechanisms for those who cannot obtain insurance in the voluntary market. Although the evidence is relatively sparse, it does show that participation in such assigned-risk pools for automobile insurance tends to be higher in states that have stricter regulation of rates.[59] Finally, some states may require, as Massachusetts does, that property-liability insurers write insurance for all individuals within a given regulated classification.[60]

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generally Submission of James M. Stone, Commissioner of Insurance, Commonwealth of Massachusetts, to the Antitrust Commission (July 24, 1978) [hereinafter cited as Stone Subcommission].

[55] *See Antitrust Commission Hearings* 54 (July 27, 1978, afternoon session) (testimony of Wesley Kinder).

[56] Stone Submission, *supra* note 54, at 3.

[57] *Id.* (attachment entitled Testimony of Massachusetts Insurance Commissioner James M. Stone, United States House of Representatives, Subcommittee on Housing, March 22, 1978, at 2).

[58] Joskow Report, *supra* note 33, at 23-26. *See also Antitrust Commission Hearings* 68 (Oct. 17, 1978, morning session) (testimony of Dale R. Comey, Vice President, Hartford Insurance Group).

[59] Open competition states have only 1.8 percent of all drivers covered by some residual market plan, compared to the overall national average of 3.6 percent. Insurance Information Institute, Insurance Facts 29 (1977). Further examples include the rough comparison of three states with strict rate regulation, North Carolina, New Jersey and Massachusetts, with 18.4, 14.3 and 17.8 percent respectively of all insured under residual coverage, versus the open competition states of California and Colorado, with only 2.5 and 0.15 percent forced to obtain residual market protection. *Id.*

[60] Stone Submission, *supra* note 54 (attachment entitled Testimony of Massachusetts Insurance Commissioner James M. Stone, United States Senate, Subcommittee on Citizens and Shareholders Rights, January 17, 1978 at 3-4).

In some circumstances, utilization of the insurance mechanism as a means of carrying out cross subsidization may pose questions of fairness and efficiency. For example, the low-risk policyholders who must pay the subsidies from being placed in the same category as high-risk individuals may be individuals, such as retired persons, who are less financially able to pay high insurance rates than are those to whom the subsidy is directed. It is also argued that, ironically, "taxing" low-risk drivers through such cross-subsidization may discourage such drivers from operating automobiles, while encouraging grater automobile use by those more likely to be involved in accidents.[61]

The Commission takes no position on the ultimate merits of the issues raised by arguments for and against increased regulation of insurance to achieve social objectives. We do, however, believe that it is important that states not preclude reliance on market forces to establish rates for the majority of policyholders as part of an effort to ensure equitable, affordable, and available insurance for all its citizens.

The Commission's fundamental conclusion, reached in Chapter Nine, is that regulation should eliminate competition only when truly essential to the achievement of articulated pubic objectives and that regulatory techniques chosen should operate in the least anticompetitive manner possible. It is important for public officials to attempt to reconcile the maintenance of competition in the insurance industry with the objectives of those who favor social regulation of the industry. Such an effort requires creative analyses and may encompass various new regulatory approaches. We believe the use of specifically targeted antidiscrimination, disclosure, and similar statutes or publicly subsidized residual market mechanisms can prove to be satisfactory methods for achieving the objectives of encouraging competitive and independent pricing, while ensuring that social goals for insurance are also protected.

THE NEED OF FURTHER STUDY OF THE INSURANCE INDUSTRY

Our inquiry into state regulation of insurance raises several difficult issues involving a complex and diverse industry. We have concluded, however, that regulatory mechanisms existing in many states unduly restrict independent pricing and that true open competition laws are the preferable means of achieving available, reasonably priced insurance for a majority of consumers. In those instances in which the dynamics of the insurance market lead to results which are deemed unacceptable as a matter of public policy, *e.g.*, rates that are unfairly discriminatory or unaffordable for some, concerned state officials should seek to find regulatory solutions that do not needlessly eliminate the forces of competition that encourage insurers to set prices on the basis of their own costs and relative efficiencies.

In constrast to the issues of antitrust immunity, the Commission has not had the resources to go beyond these basic observations about competition and insurance regulation. Additionally, we recognize that a national statute affecting the ability of a state to regulate insurance in the manner of its own choosing poses significant issues of federalism. It is for these reasons that we recommend that further inquiry into state regulation of insurance promptly be undertaken by the appropriate Congressional committees or by a new study commission to be established by the President.

This insurance industry study should have several objectives:

1. To identify and analyze ways in which state regulation of insurance acts to restrict, and acts to strengthen, competition and independent pricing behavior in the various lines of insurance;

2. To identify ways in which states could ensure the achievement of social objectives without needlessly restricting competition in insurance markets; and

3. To suggest the appropriate mix, if any, of state and federal legislation with respect to the business of insurance and to determine the appropriateness of limiting the ability of states to achieve their regulatory objectives in an anticompetitive manner.

Several Commissioners wish to note that they do not believe an additional study is needed since techniques are presently available to adequately deal with problems of equity and discrimination. These Commissioners believe that open competition should be federally mandated now.

In any events, we do not believe that repeal of the current broad immunity should await the results of this inquiry. There is simply no justification for retention of the immunity in its present form. Adoption of a statute to affirm the lawfulness of specific essential collective activity, as recommended by the Commission, will deal ade-

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[61] *Antitrust Commission Hearings* 67-68 (Oct. 17, 1978, morning session) (testimony of Dale R. Comey).

quately with the industry's legitimate fears concerning the transition to an environment of antitrust scrutiny. Moreover, in the interim between repeal of the current immunity and the conclusion of the recommended study, the states' important social interests in regulation designed to achieve equity, affordability, availability and nondiscrimination will be protected from inappropriate antitrust attack by the application of the state action exemption.

Separate views on this chapter were filed by Commissioners McClory and Hatch, and are contained in Appendix B.

Chairman RODINO. Thank you very much, Judge Bell. The gentleman from Michigan has a unanimous consent request.

Mr. CROCKETT. Mr. Chairman, I ask unanimous consent that the committee permit the meeting this morning to be covered in whole or in part by television broadcast, radio broadcast and/or still photography under rule 5 of the committee rules.

Chairman RODINO. Without objection, it is so ordered.

It is true, Mr. Bell, that we do have a responsibility in this area; I think our review is long overdue. We feel that following the recommendation made by the Commission which you supervised and led, it is incumbent on us to try to find what that narrow scope of the exemption to which the insurance industry may be entitled might be. And with that, Judge Bell, let me ask this question.

You were at the helm and we do know that the Commission recommended a narrowing of the scope of the exemption. Yet, that presumes that the exemption would be preserved. Would you agree that, in order for the industry to even continue with some kind of exemption, it should bear the responsibility of proving that it is entitled to one?

Judge BELL. Well, I think that my view would be that we switch from exemptions to exceptions.

There could be, just as I said in the statement, some curious kinds of risk where you need to have some joint endeavors almost like joint ventures. You may need to have some exchange of information concerning risk to be able to get insurance. There are a lot of complicated things in the insurance industry, but there are a lot of simple things, too. So instead of providing a complete exemption for the insurance industry, you could have certain exceptions for specific activity.

That would be the approach I would take. There will have to be some exceptions, though, because you can't do business today in a lot of complex situations without special kinds of insurance.

Chairman RODINO. Well, let me ask a very broad question, to which you can give me a general response.

There is no inconsistency, is there, with an industry having the antitrust laws apply while leaving regulatory responsibility with the States?

Judge BELL. Not at all. It is just like the exemptions that have arisen under the antitrust laws under the *Parker* v. *Brown* doctrine, where if some State agency regulates something then you can't bring an antitrust suit. It is the same kind of thing. It is all run together.

In other words, you can be regulated by the State, and there are many things the States need to regulate, such as getting your claims paid on time. People have to have somebody to turn to if they are having trouble with an insurance company, but that does not mean you have to be exempt from the antitrust laws.

The chairman is entirely correct.

Chairman RODINO. Judge Bell, do joint activities on the part of property/casualty firms tend to artificially raise prices?

Judge BELL. It would be extremely difficult to artificially fix prices in life insurance. They are very competitive with many, many companies.

On some of these other kinds of risks you could fix prices, and that is where these rating bureaus and those kinds of things may run together.

It hasn't been many years ago that all the banks had clearinghouses, and they set the prices of checks and all the services. You don't see that anymore.

But we have had a vast change in our country in the direction of people obeying antitrust laws. There has been a lot of improvement. But so long as people can get together, then there is always a temptation to artificially inflate prices.

Chairman RODINO. Judge Bell, in your testimony you state—and I agree that deregulation has already swept through the transportation, banking, and telecommunications industries—"We should carefully apply the lessons from those other experiences to the insurance business."

What lessons are there to be learned from the deregulation of these other industries?

Judge BELL. Well, there is a free market in pricing, and there are all kinds of prices, and people are falling out and some are prospering, and we are going through what we might describe as trauma as we go from a regulated to a free enterprise system. The free economy in these areas hasn't run its full course yet.

But if you could deregulate those sorts of industries, I think it would be much easier than deregulating insurance.

Telecommunications is just in its infancy. We don't know what will happen eventually out of that deregulation.

Chairman RODINO. When you talk about trauma, just what are you suggesting?

Judge BELL. I am suggesting there is a certain trauma in the fact that some airlines are going broke, some are getting stronger, and a lot of new ones are starting. Some of those will go under. Some of them are in chapter 11 now. I don't think it has been a great problem in the trucking industry, although, as I recall, it is not completely deregulated yet. But there has been a lot of trauma in the airline industry.

But those are the sort of things that the committee will want to have in mind and not do something as upsetting to the insurance industry, to the extent of any of them going under, because a lot of people have their savings invested in insurance. It has to be done with extreme care.

Chairman RODINO. In other words, you are suggesting that we do it in a way that goes easily, slowly, in phases?

Judge BELL. Carefully.

Chairman RODINO. Phase in deregulation rather than do it quickly and cause a great deal of damage and disarray that may really have longstanding negative effects?

Judge BELL. That is exactly right. That is particularly true in the life insurance business where many of our fellow citizens have their savings. You have to be careful about that.

But I know the committee will proceed with caution and care, so I am not concerned about that.

Chairman RODINO. I want to thank you very much, Judge Bell. Mr. Crockett.

Mr. CROCKETT. Thank you, Mr. Chairman.

Judge Bell, in your statement you call attention to the great changes that have occurred in the insurance industry since the Supreme Court's decision in *Paul* v. *Virginia.* At that time it was essentially a State industry, and then it became a national industry.

Today I think you would agree it is a global industry. Considering the financial problems and other problems of our States, I raise the question whether or not they are in a position to regulate global industries of this type; or if that doesn't, in itself, mandate that the Congress take a look at that situation.

Judge BELL. Well, there are so many sides to regulation. Most people that you deal with—your constituents—would not be so worried about the rates because they can buy life insurance at any price they want. They would be worried about whether or not they could collect their money.

Things that are peculiarly global to me—I know in my State if you have a complaint against an insurance company you can get the insurance commission on the telephone and get action.

I would doubt you could get much action in Washington if you are living down in Texas or Detroit. I would hate to think you would have to get in touch with somebody in Washington because you have a claim against a local insurance company.

That is the sort of thing that ought not to be moved to Washington, in my judgment. It can be done better on a local level now.

When you come to things that are global, like casualty insurance, the way Lloyd's of London and other interests have collaborated with Americans on risk, I don't know that that is a problem, but I know it is global, and there is no State that could keep up with that sort of thing.

So there are several sides to it. There are many life insurance companies—in the thousands—and I doubt that they need any Federal regulation.

I don't know enough about the others to answer your question intelligently because I am not certain that there is any price-fixing going on.

Mr. CROCKETT. Also, in your statement you call attention to certain social objectives that we should address, including the question of unfair treatment of various minority groups. I know that the problem of discrimination, certainly with respect to property insurance, has been a continuing one in many States.

In my own State of Michigan, we passed legislation addressing that, but I am not persuaded that the same thing has been generally done in all of the other States.

Have you any comment on whether it isn't more appropriate to cover that subject by Federal legislation rather than to leave it to individual States?

In other words, we passed antitrust discrimination legislation with respect to education, housing, and employment. Why not go on and do the same with respect to insurance?

Judge BELL. I would do it, but I would do it without creating another Federal agency. I would do it by saying that the States had to do it and require the States to do it, which Congress has the right to do under the 14th amendment.

It would be very bad, as I said in my statement, if you couldn't get automobile insurance, then you couldn't get a job, many times. You have to have insurance available in certain instances, and I think the Congress ought to make certain that it is available, if there are instances where it is not available; I am not advised as to whether some States are not handling this properly. But it is certainly worth looking into.

Mr. CROCKETT. Thank you, Mr. Chairman.

Chairman RODINO. Thank you.

Judge Bell, talking about States and their ability to regulate, we must consider the fact that when we look at the insurance industry it can be far-flung; it can go way beyond the borders of the State. I think we recognize, especially in today's world, that we have insurance companies that are far-reaching in their impact on the everyday economy and on the lives of individuals. Sometimes that impact goes even beyond the Nation's borders.

Is it possible to have State regulation that would probably take into consideration the far-reaching impact of this far-flung insurance industry and be able to address itself to just particular items that come within the borders of that State?

Judge BELL. In most instances it is possible. On the regulation of claims that ought to be handled on a local basis. There is no agency that you could create that would be large enough to handle all the insurance claims in the country.

Another thing that can be left to the States is the balance sheets: Whether they are making unwise investments, although in some of those huge companies that are doing business all over the world, I don't know about that.

I am not certain we are doing a very good job regulating the banks right now. If we can't handle banks, I don't know if we can handle all those insurance companies on a Federal level.

But what is happening is that we have some companies in our country that are quite large, and they are what we call multinational companies, including banks, and we haven't found a mechanism by which you can keep up with them. I think some of the insurance companies are in that same category.

I think what you would have to do, Mr. Chairman, is to divide up the problems in the insurance industry and decide whether the activity is a problem. There might be 10 activities that you would consider, and there might be 8 that ought to be left with the States and 2 that ought to be dealt with on the Federal level once you consider them.

I am not enough of an expert to know the numbers or categories that you would consider, but that is the way I would approach it.

Chairman RODINO. You would agree we would have to take into account, Mr. Bell, that the States are limited, too, insofar as resources, staff, and ability to deal with some activities.

Is this what you are inferring?

Judge BELL. In most instances, the State staffs would be better than what you would have here. You would have to hire the same people and move them to Washington because there is no expertise in Washington on insurance companies.

Another thing that you would have to face as you get into this is whether you would create a Federal insurance board like the Federal Home Loan Bank. I think you would find many insurance companies you deal with will be asking you to do that. They would be glad to be under their own board if there is some Federal level problem that you find. Now, this is not the same as antitrust exemption.

Chairman RODINO. But you are not suggesting that there isn't a Federal role to be played, are you?

Judge BELL. I am not saying there is or there is not because I don't know. But I think once you break down the activities you may find that you would want to leave most of these things in the States, but there might be something that ought to be dealt with on the Federal level.

Chairman RODINO. You don't envision any right now?

Judge BELL. Not offhand. But I am not enough of an expert on casualty insurance—on either kind for that matter. I don't know what activities insurance companies are engaged in, and I think by the time you hear the other witnesses you will know more about the scope of their business.

There could be some problem also in the investment and loan area which you wouldn't pick up in State regulation but might pick up if somebody was looking at the whole financial situation in a company. That is worth looking into.

Chairman RODINO. Yes, that seems to be an area where currently some of the insurance companies certainly are deeply involved and go beyond State borders.

Judge BELL. Also they have gotten some of the investment bankers involved in some unusual kinds of insurance.

Chairman RODINO. I want to thank you very much.

Mr. Moorhead.

Mr. MOORHEAD. Thank you, Mr. Chairman.

It is good to see you, Mr. Bell, good to see you.

There was only one comment I wanted to make. I believe there was a fair housing bill introduced about a year ago that says that—if passed, it would say it is against the law to discriminate in insurance.

We haven't had hearings on that yet, but that is something that might take care of Judge Crockett's problem.

Judge BELL. Well, you would have to find out if there is a problem. I know that—having nothing to do with minorities—but I know one time the rate was quite different on young people from old. Say under 25, there was a rate that might be so high you couldn't get insurance even if it was available. I don't know all that firsthand anymore.

Chairman MOORHEAD. It is good to have you here this morning, and I want to welcome you.

Judge BELL. Good to be back again.

Chairman RODINO. Thank you very much, Judge Bell, for your presentation this morning.

Judge BELL. Thank you, Mr. Chairman.

Mr. RODINO. Our next witness is a very, very dear friend of long-standing and one certainly who is sorely missed by this committee for the important contributions he made. We are delighted to see him here again; he is a good friend whom we warmly admire and highly regard, the Honorable Robert McClory, who is now with Baker & McKenzie. Also on the panel with Mr. McClory is Prof. Eleanor Fox, New York University Law School.

Bob, it is a delight to see you here. I must say that, just as I noted with the former Attorney General—he smiles more readily and his demeanor is a lot easier—I see that broad, broad smile on your face as well.

Good to see you.

TESTIMONY OF HON. ROBERT McCLORY, BAKER & McKENZIE, WASHINGTON, DC, AND PROF. ELEANOR M. FOX, NEW YORK UNIVERSITY LAW SCHOOL, NEW YORK, NY

Mr. McCLORY. Thank you, Mr. Chairman. You want me to proceed?

Chairman RODINO. Please proceed.

Mr. McCLORY. Let me say, the smile results in part from the pleasure of being back in this committee room and being face to face with some of my former colleagues and being on a panel with the distinguished professor from New York University, Eleanor Fox.

My appearance before the subcommittee today is entirely on my own behalf as a former member of this committee and as a former member of the National Commission for the Review of Antitrust Laws and Procedures.

The National Commission, which reported to the President and the Congress on January 22, 1979, made numerous constructive recommendations, many of which have been translated into legislation and policy guidelines with substantial benefits to American commerce and industry, to the Judiciary and the legal profession and to the public.

We are dealing here today with only one of those recommendations; namely, a proposal to repeal the McCarran-Ferguson Act of 1945. Basically, McCarran-Ferguson granted to the business of insurance exemption from the Sherman, Clayton, and Federal Trade Commission Acts to the extent that it is regulated by State law.

Prior to 1944, the U.S. Supreme Court had held that the sale of insurance did not constitute interstate commerce, and therefore was not subject to the Federal antitrust laws.

However, in the case of the *South Eastern Underwriters Association*, the Supreme Court held that transactions in insurance across State lines did, indeed, constitute interstate commerce, and the parties involved were subject to the Federal antitrust laws.

Reaction in the States was immediate. State officials, including legislators, insurance department directors, and State taxing authorities, particularly, feared the loss of their prerogatives and revenues. The Congress acted promptly in enacting the McCarran-Fer-

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guson Act with broad bipartisan support which provided specifically that the "business of insurance" should continue to be subject to Federal antitrust laws but only "to the extent that such business is not regulated by State law."

Within a few years all of the States had adopted fire and casualty rating laws. State statutes were enacted and regulations were adopted to enable insurance companies to participate in rate bureaus and to benefit from this pooling of information concerning risks. Records of losses, life expectancy tables, and a broad range of data, upon which companies might choose to write policies of insurance—or to avoid involvement in particular lines of insurance, were pooled by these rating bureaus.

Some State insurance departments publish suggested or minimum rates for particular lines of insurance. While this practice tends to discourage competition, it has had the additional effect of spawning small insurance companies. Nevertheless, even such small companies are subject to strict regulation at the State level.

The effectiveness of the States' regulation of the business of insurance is generally recognized. Criticisms in the Commission's report and in the study for which the Commission contracted hardly seem to warrant the subordination of State control of the insurance business by Federal statutes and regulations.

The Commission study, conducted by Professor Paul Joskow, questions the system whereby insurance companies pool special risks and contribute funds to State agencies which assure coverage of individuals or businesses unable to obtain insurance through normal channels.

The "uninsured motorist" system in Illinois and "assigned risk" practices in various States have worked remarkably well. To replace such State systems with a new kind of federally mandated Federal Deposit Insurance program runs contrary to the present day entire concept of returning increased authority and responsibility in the States.

A more alarming prospect is alluded to in the 1979 Commission's majority report. It is pointed out there that by a repeal of McCarran-Ferguson, the immunity of the insurance industry from the FTC Act would end.

As a result, the FTC would be in a position to superimpose its authority on the insurance departments of the 50 States. The FTC could become directly involved in ratemaking. It should be observed, at least, that by inviting the FTC to participate in the ratemaking process, the burdens of a new and additional bureaucracy would be added to those already overseeing the insurance industry which include State insurance departments, local, State, and Federal taxing authorities, and others.

A highly paradoxical argument was advanced in the Commission report in support of a repeal of McCarran-Ferguson. It was proposed there that instead of pooling information upon which actuarial tables are established, insurance companies should hire consultants to compile such information.

This recommendation by Professor Joskow noted, incredibly, that if some firms are too small to determine rates efficiently, with the help of consultants, if necessary, but without resorting to published

rate books, then they probably should not be in the business of insurance.

A principal concern of some members of the 1979 Commission was to mandate fairness and equity in insurance rates and coverage through repeal of McCarran-Ferguson. While the Commission denied an intent to seek social changes through increased Federal controls of the insurance industry, that is precisely what the report suggests.

The majority of the Commission favored the operation of market forces that would establish rates for the majority of policyholders as part of an effort to ensure equitable, affordable, and available insurance for all of our citizens.

The Commissioners felt that some State regulation of insurance rates was unacceptable as a matter of public policy because it unfairly discriminated against some consumers, such as, presumably, retired persons, city residents, male motorists aged 18 to 25, and others.

As a senior citizen and a nondrinker with a good safety record, I am personally alarmed at the prospect of a new Federal bureaucracy mandating automobile insurance which would require me to subsidize the high risk motorist who gets behind the wheel.

It is quite inaccurate for critics to state that enactment of the McCarran-Ferguson Act granted blanket and unqualified exemption to the insurance industry from the Federal antitrust laws.

Mergers with other insurance companies or other companies, which would reduce competition or create a regional, national or categorical monopoly would continue to be subject to all of the restraints and penalties of the Sherman and Clayton Acts. Retail price maintenance agreements, which attempt to impose fixed commission charges, could run into strong opposition if the company attempted to rely on the McCarran-Ferguson immunity.

It is doubtful that Federal statutes aimed at eliminating unfair discrimination based on sex, race or other characteristics would require any amendments to the McCarran-Ferguson Act, as they do not refer to the Sherman, Clayton or Federal Trade Commission Acts.

Basically and fundamentally, the arguments in favor of a repeal of McCarran-Ferguson get down to the question of which level of government should control or regulate the business of insurance.

Within the past 8 years, there have been 3 major studies conducted at the Federal level dealing with the appropriateness of the McCarran-Ferguson immunity and the adequacy of State regulation.

The first of these was performed during the Ford administration by a special Justice Department task force. This task force favored a dual system of regulation which would enable insurers to opt between a State or Federal charter.

Legislation roughly parallel to the Justice Department proposal was introduced in the Senate by former Senator Edward Brooke and considered by the Senate Banking Committee. The Senate committee decided against acting on this legislation, in part because of a fear that it would result in a situation where State and Federal authorities would compete to see which level of government could offer the least stringent regulation, and in part because of a fear

that it would only serve to undercut entirely State regulatory authorities and disadvantage new and small companies.

The second report was performed by the GAO and released in 1981. This GAO report, which in my view was slanted very much toward the repeal of McCarran-Ferguson, reviewed the effectiveness of State insurance regulation and suggested that perhaps Federal regulation would be better, possibly more effective even—imagine—cheaper. It should be noted that this GAO report made no solid recommendations, and it characterized even its own findings as being preliminary and inconclusive.

Past developments lead me to conclude that it would be totally inappropriate for Congress to move precipitously to repeal McCarran-Ferguson. Nonetheless, I do feel the hearings which this subcommittee is conducting are necessary and constructive.

The threat of a repeal of McCarran-Ferguson and the spectre of a Federal statute to regulate the insurance industry at the national level has had two salutary consequences:

First, the threat of Federal control has encouraged State insurance departments to improve the quality of their regulation of insurance at the State level, and

Second, the private insurance companies, in order to avoid Federal controls, are embracing a social consciousness that disarms some critics without in any way threatening the solvency of their businesses.

Finally, there is no public demand for restructuring our Federal system so as to superimpose direct Federal regulatory oversight of every State department of insurance and the thousands of insurance companies, large and small, throughout the country.

With assets estimated at $500 billion and annual premiums of $150 billion, there is a strong temptation on the part of "regulators" to reach out and grasp increased control of the insurance industry. Repeal of McCarran-Ferguson would accomplish precisely that result.

This committee should oppose such action.

Thank you, Mr. Chairman.

[The statement of Mr. McClory follows:]

STATEMENT OF ROBERT MCCLORY

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Prior to 1944, the U.S. Supreme Court had held that the sale of insurance did not constitute interstate commerce, and therefore was not subject to the federal antitrust laws. However, in the case of the United States v. South Eastern Underwriters Assn. 322 U.S. 533 (1944) the Supreme Court held that transactions in insurance across state lines did, indeed, constitute interstate commerce, and the parties involved were subject to the federal antitrust laws.

Reaction in the States was immediate. State officials including legislators, insurance department directors, and state taxing authorities feared the loss of their prerogatives and revenues. The Congress acted promptly in enacting the McCarran-Ferguson Act with broad bi-partisan support which provided specifically that the "business of insurance" should continue to be subject to federal antitrust laws but only "to the extent that such business is not regulated by state law."

Within a few years all of the states had adopted fire and casualty rating laws. State statutes were enacted and regulations were adopted to enable insurance companies to participate in rate bureaus and to benefit from this pooling of information concerning risks. Records of losses, life expectancy tables, and a broad range of data, upon which companies might choose to write policies of insurance—or to avoid involvement in particular lines of insurance, were pooled by these rating bureaus.

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A principal concern of some members of the 1979 Commission was to mandate fairness and equity in insurance rates and coverage through repeal of McCarran-Ferguson. While the Commission denied an intent to seek social changes through increased federal controls of the insurance industry, that is precisely what the report suggests. The majority of the Commission favored the operation of market forces that would establish rates for the majority of policyholders as part of an effort to ensure equitable, affordable, and available insurance for all its citizens. The Commissioners felt that some state regulation of insurance rates was unacceptable as a matter of public policy because it unfairly discriminated against some consumers, such as, presumably, retired persons, city residents, male motorists aged 18 to 25, and others.

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Chairman RODINO. I want to thank you very much, Bob.

Professor Fox.

Professor FOX. Mr. Chairman, it is a pleasure to be here testifying before you today. It is a pleasure to be testifying with and before my very distinguished former colleagues on the Commission, Mr. Rodino.

Chairman RODINO. Please proceed.

Professor FOX. My basic premises are very close to Mr. McClory's. Yet we make different recommendations, and I will tell you where I think we differ.

I appear here today in support of the Commission recommendation. The Commission recommended, as Judge Bell so articulately testified, that the exemption from Federal antitrust laws is overbroad and should be at least narrowed. I testify for the narrowing of the exemption because I think that this will expose the insur-

ance businesses to competition and cause rates to be lower for the benefit of all of us, the insured.

I do not support shifting regulatory control from the States to the Federal Government, and so the spectre that Mr. McClory sees I do not.

First, let me say a word about the framework used by the Commission; second, I will apply the principles derived from that framework; and third, I will outline developments since our Commission report that I think further support the Commission report.

The framework is, as Judge Bell said, No. 1, the free market should control. The market and the competition that comes from the free play of the market benefits consumers; in matters of insurance it benefits the people who buy insurance policies.

No. 2, exceptions should be very narrow, and proponents of exemptions from the antitrust law should bear the burden of showing that there is a compelling case that competition is not working to produce the lowest price or that there is a clearly paramount social purpose that cannot be served by competition. No. 3, if an exception is warranted, it should be fashioned in the least anticompetitive way.

Let me turn to application of these principles to the insurance industry. The dilemma in the insurance industry is this: The Federal Government has provided for an exemption whenever the State regulates unless there is a boycott or coercion. States may minimally regulate, basically letting the private parties get together and fix prices.

When the State minimally regulates, the exemption comes in, and we are left in the hands of the private competitors to fix prices as they will.

In other words, the exemption combined with the possibility of minimal State regulation is authorization for private price fixing.

The Commission considered this problem against the following four sets of factors:

No. 1, we asked, was the structure of the industry such that competition could work to produce the lowest price? And we thought yes.

No. 2, as to State regulation and federalism, it seemed clear to us that States should have the right to regulate and do have the right and power to regulate as long as they actively regulate and supervise. States can do this and carry out their will without special exemption.

No. 3, we looked at the possibility that there were social goals that competition could not achieve and that perhaps regulation could achieve better. Certainly availability and affordability are appropriate social goals. We were not convinced that these goals could be better achieved by regulation than by competition, but we thought Congress should consider this question.

No. 4, we asked, is this industry different from most others? Are there certain kinds of collaborative efforts that should be undertaken in this industry for the benefit of insureds and yet the activity is so risky that the very existence of the antitrust laws will chill desired behavior?

Desired behavior could include pooling statistics, possibly trending data, possibly combining efforts to ensure high-risk categories.

In my No. 3 and No. 4 categories, we suggested that Congress should look into these matters. It should consider whether there are important social goals not served by competition and whether there are important procompetitive activities chilled by the antitrust laws, so that Congress should adopt legislation setting out what behavior is lawful in the insurance industry.

However, our Commission report was very clear as to what, if at all, it thought Congress ought to regulate. We listed three criteria that we thought should be satisfied before Congress does step in to list certain kinds of transactions or conduct that should be regulated: No. 1, that lawfulness is truly uncertain; No. 2, that probably after inquiry on all of the facts it will be found that the type of conduct on balance is not anticompetitive; and, No. 3, that the particular conduct is so important that uncertainty severely limits competitiveness and effectiveness of the insurance process.

For my third point, let me turn to current developments that I think make the move toward narrowing—indeed, maybe abolishing the exemption—even more appropriate today than it was at the time we submitted our report.

No. 1, as Judge Bell said, there is a determined movement toward deregulation. I think there is increased consensus that we should move away from special exemptions.

No. 2, I want to say a word about the State action doctrine, and this leads into my point that it is not clear to me at all that we need a Federal exemption or codification since the States have power to regulate as long as they supervise. The State action doctrine defines that area within which, if the State acts, antitrust is inapplicable.

One of the most important cases that came up since our Commission report is the *Midcal* case, in which California told all wine wholesalers that they must post resale prices at which their customers must sell wine. The Supreme Court held this regulation void because it allowed private price fixing. The State did not supervise at all.

The Supreme Court said that to come within the State action exemption the State policy that displaces competition must be clearly articulated; there must be a clear policy of the State; and, No. 2, there must be affirmative State supervision.

In the *Midcal* case there was not affirmative State supervision. Therefore there was no exemption. If you let the private parties get together and fix rates you can expect their ratesetting to injure the public; in this case to injure all of us who buy insurance policies.

A third important current development concerns the law that defines what is a restraint of trade. Most important is *Broadcast Music, Inc.*, v. *CBS*, decided by the Supreme Court in 1979, just after our report was presented. *BMI* made it clear that collaborative activities, even by numerous competitors, are not per se illegal and are likely to be upheld as reasonable if they are important to get a product to the market for the consumer.

I believe the case stands further for the following generalization: Procompetitive collaborative activities are lawful. Data sharing, sharing of data on past closed transactions, comes within this category. Joint risk taking, where it would be difficult for any one com-

pany to take the risk itself, including joint ventures to do so, are lawful.

In conclusion, I believe that the special exemption granted by McCarran-Ferguson should be reexamined, and I hope that this subcommittee will give serious consideration to the Commission's recommendations.

Also, I want to convey a personal view in light of developments that have given antitrust doctrine greater flexibility, and that is this: I would recommend that the special exemption be repealed entirely if Congress finds that States could, under the protection of the State action doctrine, serve any important social goal not likely to be served by competition. Thank you.

[The statement of Professor Fox follows.]

STATEMENT OF ELEANOR M. FOX, PROFESSOR OF LAW, NEW YORK UNIVERSITY, SCHOOL OF LAW

Mr. Chairman and members of the Committee: My name is Eleanor Fox. I am a Professor of Law at New York University School of Law. I served as a member of President Carter's National Commission for the Review of Antitrust Laws and Procedures and I am a past Chair of the New York State Bar Association Section of Antitrust Law.

I. INTRODUCTION

In 1978 and 1979, the National Commission for the Review of Antitrust Laws and Procedures ("the Commission") held hearings on and considered whether the antitrust exemption granted by the McCarran-Ferguson Act is justified and appropriate as a matter of public policy. The Commission concluded that the immunity is overbroad, that the broad immunity should be repealed, that narrowly drawn legislation should be adopted to affirm the lawfulness of a limited number of essential collective activities, and that further study of economic regulation of insurance should be undertaken by Congressional committees or a commission established by the President. Commissioner Hatch dissented in full and Commissioners McClory and Wiggins dissented in part.

I am pleased to accept the Subcommittee's invitation to testify today on the insurance industry's antitrust exemption and the Commission's recommendations for reform. I would like to review briefly the recommendations of the Commission, explain why I think those recommendations were sound when the Commission submitted its Report to President Carter and Attorney General Bell in 1979, and suggest that implementation today is even more clearly feasible and appropriate and consistent with the growing consensus for deregulation.

II. GENERAL PRINCIPLES

The Commission made recommendations for shifting from an environment of government regulation toward an environment of competition. It did so not only with regard to the insurance industry but also with regard to trucking, railroads, agriculture and ocean shipping. Before analyzing the facts regarding any of these industries, the Commission formulated a general approach. That general framework is summarized in Chapter Nine of the Commission's Report, as follows:

"1. Free market competition, protected by the antitrust laws, should continue to be the general organizing principle for our economy.

"2. Exceptions from this general principle should only be made where there is compelling evidence of the unworkability of competition or a clearly paramount social purpose.

"3. Where such an exception is required, the least anticompetitive method of achieving the regulatory objective should be employed."—Report of the Commission ("Report") 177.

The Commission considered that there should be a presumption against exceptions from competition, and it expressed this view as follows:

"*Presumptions.* As mentioned at the outset, an economic system based on marketplace competition has important implications for basic American values. A preference for competition is also empirically grounded. In diverse contexts, it has been shown that competition provides an irreplaceable spur to efficiency and to diversi-

fied source of innovation. Furthermore, in most instances competition maximizes consumer welfare. . . .

"The Commission, therefore, starts with a strong presumption against allowing exceptions from competition and, specifically, against immunities from the antitrust laws. Although careful factual inquiry should be a prerequisite to any decision to seek repeal or modification of an immunity, the burden of proof for purposes of the decisionmaking process should be on the proponents of continuing antitrust immunity to show a convincin· public interest rationale for abandoning competition. Each existing or proposea exemption should be justified in terms of empirically demonstrated characteristics of the specific industry that make competition unworkable. The defects in the marketplace necessary to justify an antitrust exemption must be substantial and clear.

"There may be specific cases, of course, in which regulation is necessary to achieve societal goals. Regulation of natural monopolies is a clear example. There also may be cases where the benefits of attaining certain vital social and political goals outweigh the economic costs of creating exceptions to the competitive rule. Even in this event, however, we believe that regulation need not be an all-or-nothing matter. Substantial competition can exist under many forms of regulation, and an exemption from the antitrust laws is not a necessary component of every system of regulation."—Report 185-86. (Footnote omitted.)

The Commission's conclusions regarding insurance flow naturally from an application of these principles to the facts, as I shall discuss.

III. INSURANCE: THE COMMISSION'S RECOMMENDATIONS

Congress passed the McCarran-Ferguson Act in 1945 in response to a Supreme Court opinion ruling that insurance was "commerce" and as such was subject to the federal antitrust laws. The act provides that "the business of insurance . . . [is] subject to the laws of the several States which relate to the regulation . . . of such business," and that no act of Congress shall supersede any such law, except that the antitrust laws apply "to the business of insurance to the extent that such business is not regulated by state law," and the Sherman Act applies to any "boycott, coercion or intimidation." 15 U.S.C. §§ 1012(a)-(b), 1013(b) (1976). The Supreme Court is hostile to antitrust exemptions because they tend to promote inefficiency and hurt consumers. It broadly construes the boycott exception[1] and it narrowly construes "the business of insurance,"[2] thereby exposing more activity to competition and antitrust oversight. However, where the state regulates the business of insurance, even with a minimal level of state involvement, the presence of the state regulation ousts antitrust jurisdiction. See Ohio AFL-CIO v. Insurance Rating Board, 409 U.S. 917 (1972) (Douglas, J., dissenting from denial of certiorari from 451 F.2d 1178 (6th Cir. 1971); FTC v. National Casualty Co., 357 U.S. 560 (1958).

The breadth of the antitrust immunity therefore creates a gap. States may have minimal regulation, without supervision, of collaborative activities at the heart of "the business of insurance," yet the business firms are immune from the antitrust laws and are free to behave like a cartel.

The Commission considered this problem in view of four sets of factors:

(1) The structure of the industry. It found that the industry was competitively structured and that competition could work to produce lowest costs for individuals and firms seeking insurance.

(2) State regulation. The Commission did not wish to impair the ability of states to decide that regulation was needed to serve important goals and to provide effective state oversight. It recognized the state action exemption from the federal antitrust laws, which shields conduct "compelled and effectively supervised by the state acting as sovereign." See Report at 183. The Supreme Court has since elaborated upon the standard, as I shall later relate.

(3) Social goals. The Commission recognized that states may wish to assure availability and affordability. The Commission seemed uncertain that regulation will better satisfy these goals than will competition. It reflected on distortions that may be caused by regulation, such as (1) insurers' avoidance of serving individuals where the revenues from service are less than the cost of service, and (2) the subsidizing

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[1] E.g., St. Paul Fire and Marine Insurance Co. v. Barry, 438 U.S. 531 (1978).

[2] See, e.g., Union Labor Life Ins. Co. v. Pireno, 102 S. Ct. 3002 (1982); Group Life & Health Ins. Co. v. Royal Drug Co., 440 U.S. 205 (1979), which were decided by the Supreme Court after the Commission submitted its Report.

See also United States v. Title Insurance Rating Bureau of Arizona, 700 F.2d 1247 (9th Cir. 1983), petition for cert. pending.

group of insureds may actually be more indigent than the subsidized group. Nonetheless, the Commission pin-pointed this area as an appropriate one for study and thought.

(4) Possible special needs of insurers to collaborate in ways that are risky under the state of the antitrust laws. The Commission considered insurers' needs to pool statistics concerning past losses, in order that they might develop actuarially sound data regarding expected further losses for particular classifications of risk; to collaborate in order to trend past data to make it useful for projecting expected losses; to compile and disseminate data on administrative expenses as a component of rates; to promulgate bureau rates to members in a form usable as actual rates, and to combine to insure high risk categories.

As mentioned, the Commission urged that Congress adopt legislation setting out specific behavior that would be lawful for antitrust purposes. This suggestion, however, was not an invitation to introduce new immunities. Rather, the Commission suggested that Congress consider including in legislation only conduct that satisfies all of the following criteria: (1) lawfulness is truly uncertain; (2) under a rule of reason the conduct would be found to have the probable effect of not lessening competition, and (3) the conduct is so important in the insurance process that uncertainty would severely limit the competitiveness and efficiency of insurers. Report at 236-37.

The Commission was skeptical toward some of the insurers' claims of special need to collaborate, and sympathetic toward others. Moreover, it believed that certain activities were procompetitive and clearly legal, and others anticompetitive. In any event, it recommended that Congress should consider the insurers' claims under the standard set forth above.

IV. THE COMMISSION'S PROPOSAL IN VIEW OF CURRENT DEVELOPMENTS

In my view, the Commission's Report outlines the correct approach. It is entirely in harmony with principles on which, I think, there is wide agreement: unnecessary government regulation, and unnecessary sheltering of private firms from competition, should be eliminated.

Since the Commission submitted its Report, there have been developments on three fronts that make the Commission's recommendations even more appropriate. First, there has been a determined movement towards deregulation and away from special exemptions.

Second, the Supreme Court has elaborated upon the proper scope of state regulation that qualifies for antitrust immunity under the state action doctrine. In California Retail Liquor Dealers Association v. Midcal Aluminum, 445 U.S. 97 (1980), the Supreme Court invalidated a state requirement that wine wholesalers fix the resale prices at which retailers would sell their wine in the state. It did so because, as it held, the state has no power to order private parties to fix prices and then to give them immunity from the law against price-fixing. The private price-fixing involved in *Midcal* was totally unsupervised by the state; such private price-fixing is bound to result in a bad deal for consumers.

At the same time, in *Midcal*, the Surpeme Court gave guidance as to the proper realm of immune state action. It said:

"The [ ] decisions establish two standards for antitrust immunity under Parker v. Brown. First, the challenged restraint must be "one clearly articulated and affirmatively expressed as state policy"; second, the policy must be "actively supervised" by the state itself. . . . The California system for wine pricing satisfies the first standard. The legislative policy is forthrightly stated and clear in its purpose to permit resale price maintenance. The program, however, does not meet the second requirement for Parker immunity. The state simply authorizes price-setting and enforces the prices established by private parties. The state neither establishes prices nor reviews the reasonableness of the price schedules; nor does it regulate the terms of fair trade contracts. The state does not monitor market conditions or engage in any "pointed reexamination" of the program. The national policy in favor of competition cannot be thwarted by casting such a gauzy cloak of state involvement over what is essentially a private price-fixing arrangement."—445 U.S. at 105-06.[3]

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[3] See United States v. Southern Motor Carriers Rate Conference, 702 F.2d 532 (5th Cir. 1983), petition for cert. pending. In the deregulated motor carrier industry, the court held that the motor carriers' combination, through rate bureaus, to discuss and agree on rates to be proposed to state public service commissions for approval was price-fixing illegal per se and was not sheltered by the state action exemption. None of the states required the competitors to combine to

Continued

The standard of *Midcal* fits precisely with the recommendations of the Commission. If private acts are anticompetitive and would otherwise violate the antitrust laws, they should not be sheltered in the absence of a clear state policy actively supervised by the state and subjected to "pointed reexamination."

The third development goes to the likelihood of antitrust liability even without state action protection. Since the Commission submitted its Report, Supreme Court developments confirm the Commission's statements that procompetitive and efficient collective action, such as sharing past loss data and pooling to underwrite large risks, will be judged under a rule of reason and will be upheld. The major Supreme Court case is Broadcast Music, Inc. v. Columbia Broadcasting System, 441 U.S. 1 (1979), wherein the Supreme Court rejected the claim that the pooling of thousands of musical compositions for distribution by a common licensing agency is illegal per se. The pooling was important to reduce costs and to enable the composers to get to market. On remand, the arrangement was upheld as legal. 620 F.2d 930 (2d Cir. 1980), cert. denied, 450 U.S. 970 (1981).

Moreover, lower court law and numerous business review letters granted by the Department of Justice confirm the legality of sharing past market information and combining to facilitate joint service. As the court in the *Southern Motor Carriers'* case, *supra* p. 10, noted:

"[T]he government did not seek to enjoin the rate bureaus from performing joint rate studies or from undertaking joint publication of individual rates and agreements involving two or more parties who provide joint service."—702 F.2d 532, 542 n.19.[4]

In sum, even without a special federal grant of immunity, insurers are free to engage in procompetitive activities. As to questionably or clearly anticompetitive activities, insurers should be free to try to make their case before Congress.

CONCLUSION

The Commission's recommendations reflect good and progressive public policy. I respectfully urge that Congress narrow the overbroad exemption provided by the McCarran-Ferguson Act.

Thank you.

Chairman RODINO. Thank you.

Mr. McClory, I know that you were very diligent and you were very concerned when, as members of the Commission, we undertook the review of our antitrust laws and exemptions. I recall, just as you stated, that you agreed generally with the recommendations of the Commission except in this one area of insurance, where you had some concerns you expressed even then about how repealing McCarran-Ferguson might be far-reaching, that some agency of the Government might get into other areas and unnecessarily burden the industry. I think that all of us are aware that this is a concern that we must deal with.

Why, in your view—and you can make your response very general—is it necessary to be so cautious in narrowing the McCarran-Ferguson exemption? Why is this so different from the others?

Mr. MCCLORY. Well, I think there is a great distinction, Mr. Chairman, between the insurance industry, for instance, and agriculture and monopolistic labor organizations. The insurance industry requires that there be a high degree of safety, that information with regard to risks, with regard to actuarial information, with regard to liabilities, with regard to investments, with regard to all

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fix proposed rates, and the court held that compulsion is a necessary element of the private party's defense. The court observed that if collective rate-making were so important to the system it would "be but a small step for the states to compel it of all carriers." *Id.* at 542.

Dissenting judges would have held that state compulsion is not essential to immunity.

[4] See also Quality Auto Body, Inc. v. Allstate Insurance Co., 660 F.2d 1195 (7th Cir. 1981), cert. denied, 455 U.S. 1020 (1982): Arrangements between insurance companies and automobile body repair shops under which insurers would prefer shops that followed the insurer's repair rate guidelines were held lawful.

kinds of things to protect the consumer and to assure that the benefits that we want to derive from insurance are there.

So I think we have to have a high degree of regulation with regard to the insurance industry. With respect to agricultural cooperatives, it seems to me that these are price-fixing organizations that establish, I suppose, a fair—at least an agreed-upon price for farmers who put their agricultural product and market agricultural goods and a variety of other goods through farm cooperatives, and that is just completely different from the insurance industry.

The insurance industry is similar in some ways to the banking industry, but I would not want to—as one of the witnesses will say—to put the banking industry into the insurance business, for instance. I think that would be wrong.

I think we do have to have intensive regulation, such as Judge Bell indicated, and I think we can do it best at the local level, at the State and local level.

Also, I would like to distinguish between the airline industry, the shipping industry, and trucking industry, in which there has been some action with regard to deregulation. I think they are all distinct. I think they all have to stand on their own feet, and I think it is too early to decide that the deregulation of the airline industry to the extent we have done it has been a great thing.

It certainly hasn't been a great thing for consumers. I pay about twice as much now for my flight out to Chicago on United as I used to. Several airline companies have—like Eastern and Braniff—have had pretty rough times with the action that has been taken, and we just couldn't stand that kind of dilemma in the insurance industry.

Judge Bell talked about trauma. Trauma, as I understand it, means pain, and he would anticipate quite a bit of pain if we undertook to do with the insurance industry what we have done with some other industries.

Chairman RODINO. Bob, the Commission in its final report stated—and I quote from it for your recollection—"Although careful factual inquiry should be prerequisite to any decision to seek repeal or modification of an immunity, the burden of proof for purposes of the decisionmaking process should be on the proponents of continuing antitrust immunity to show a convincing public interest rationale for abandoning competition."

Do you agree that the burden should rest on the proponents—those who want to continue to retain whatever immunity there might be?

Mr. MCCLORY. Well, when I used to practice law, I always thought the plaintiff had the burden of proof, and I think maybe the plaintiff here is those that want to repeal McCarran-Ferguson.

But aside from that, I would say on the basis of the record that we have before us—and you can look at the Attorney General's task force or the GAO report which was filed in 1981 and I suppose other surveys that have been made of what the State insurance agency departments are doing—I think there is a pretty good record. The incidences of deficiency at the State level are so few, and to superimpose a Federal agency because of the deficiencies, which are very infrequent at the State level, would seem to be

most unfortunate, and a dual system doesn't strike me as being any kind of an advance or in the direction of deregulation.

I think it is complicating the bureaucratic control, and as I see it, the real issue here is who is going to do the regulating, because we are not going to deregulate the insurance business. We are only going to shift regulation from the State level to the Federal level, and I think to suggest that that is going to be cheaper would be wrong.

The GAO report, the principal complaint that starts out with it says—one of the principal complaints is they don't pay the officials at the State insurance agencies enough money; they don't have high enough salaries; they don't hire enough professionals.

Well, if you are going to have higher paid people and you are going to have more professionals, you are going to have more expensive regulatory bureaucratic control, and I think that is a real threat which would follow repeal of McCarran-Ferguson.

Let me just add this: if anything is going to be done—and I am not saying that something or some changes should not be made—I would think that it might be well to undertake some amendments, some changes, and I think maybe the amendments with regard to providing greater—recognizing the social problems of minorities and so on may be a very appropriate area for some committee to consider. But it seems to me that the real issue is as to whether or not there should be any changes that can be undertaken without repeal. To repeal and then not know where we are going to go would be chaotic.

Chairman RODINO. Professor Fox, what practices of the insurance industry need antitrust protection, and why?

Professor FOX. I do not know if there are practices that need special protection. Practices explained to the Commission as in need of protection, such as pooling past data, are now even more clearly consistent with the antitrust laws.

In all businesses you can imagine cases that pose difficult questions. I don't see why the insurance industry is more in need of certainty at the margin than any other industry.

Also, I have a hard time understanding why State action does not solve the whole problem because the State can regulate. If it wants to set prices, it can set prices.

The present scheme creates a gap. The State can minimally regulate, and there is a total antitrust exemption, private price-fixing is authorized. I would like to close that gap and we can close it by repealing the antitrust exemption. Then if the States regulate, actively supervise, and scrutinize, their activity will be protected.

Chairman RODINO. Professor Fox, you mention in your statement on page 11 the *Broadcast Music* case, and you point out that it essentially held that collective action among competitors that serves competition was held to be legal under the "rule of reason" test. Isn't that correct?

Professor FOX. Yes, that is correct.

Chairman RODINO. Is it correct that you then draw the conclusion that, if that is the case, there is no need for statutory antitrust immunity for collective action among the insurance companies?

Professor FOX. Yes, I do.

Chairman RODINO. Do you see any distinction, though, between action that might be taken by insurance companies as against collective action taken by music companies?

Professor FOX. There are always distinctions, depending on the particular facts. The collective action in BMI happened to be a high degree of collective action, and so the principle is very clear.

There were tens of thousands of musical composers who actually pooled their products through a single licensing agency, and the claim was that this pooling was per se illegal. The Supreme Court rejected this claim, and showed how the collabaration might be useful to buyers.

The general principle of this case applies equally to the insurance industry.

Chairman RODINO. Professor Fox, I think it is a fair statement to say that your position is that the proponents or those who would preserve the immunity of the exemption should bear the burden of proving that it is necessary, isn't that so?

Professor FOX. Yes, I do. Of course, you are not bound by the rules used in courts and of course the rules in court are the other way around.

I think that there is a consensus that competition is good for the public, and if you deprive the public of competition and let private parties fix prices, you are going to hurt consumers and, in this case, insureds.

If you believe in that principle, I think as a matter of public policy you would want anyone who wants an exemption from competition to bear the burden of proving his or her case.

Chairman RODINO. Let me ask one final question, which has a couple of facets to it, to clarify some matters concerning the antitrust immunity of the insurance industry.

There are really, as I understand it, two immunities that are applicable in the context of State insurance regulation, the McCarran-Ferguson immunity and the immunity under *Parker* v. *Brown*, aren't there?

Professor FOX. That is right.

Chairman RODINO. So let's assume that Congress were to withdraw McCarran-Ferguson immunity completely.

Wouldn't the States be perfectly free then to pursue regulation for social purposes without any fear of antitrust liability?

Professor FOX. Yes. If the State has a clear policy and actively supervises, the conduct then comes within the State action exemption.

Chairman RODINO. And this is the important case which you cited, the *Midcal* case?

Professor FOX. That is right, yes.

Chairman RODINO. Then are you saying that the McCarran-Ferguson antitrust immunity is not necessary to achieve the social goals of insurance regulation?

Professor FOX. That is what I believe. I also believe your subcommittee ought to look into this and examine it because facts are important, and you must know all the facts.

If the State has a clear policy and actively supervises, McCarran-Ferguson is superfluous. But where the State has a policy but doesn't supervise, it says in effect to the insurers "Go ahead and

fix prices." Then McCarran-Ferguson is not superfluous; it gives the right of price-fixing.

Chairman RODINO. I take it that, notwithstanding what you seem to have concluded from what you at this time know and what you have learned in studying this matter, it is incumbent on this subcommittee to really review this with an open mind without proceeding on the basis that there ought to be the exemption or there ought not to be the exemption; am I correct?

Professor FOX. Yes, I do think so.

Chairman RODINO. Thank you very much.

Mr. Fish.

Mr. FISH. Thank you, Mr. Chairman. Welcome to our witnesses.

Professor Fox, I would like to read a part of the McCarran-Ferguson Act and then ask some questions about it:

> No act of Congress shall be construed to invalidate, impair or supersede any law enacted by any State for the purpose of regulating the business of insurance unless such act specifically relates to the business of insurance.

My first question is: doesn't this clause already allow Congress to enact laws specifically aimed at practices in the insurance industry?

Professor FOX. I believe so, yes.

Mr. FISH. And hasn't the Congress already responded by enacting federal laws dealing with riot reinsurance, flood insurance and crop insurance?

Professor FOX. Yes, I believe so, sir, but I am not an expert in those areas.

Mr. FISH. And is there anything in the McCarran Act that precludes Congress from enacting a stricter fair housing law covering insurance companies?

Professor FOX. No.

Mr. FISH. Does McCarran in any way prevent Congress from dealing with discrimination in insurance, such as age discrimination and sex discrimination?

Professor FOX. No.

Mr. FISH. Turning to the issue of the business of insurance under McCarran-Ferguson, on page 6 of your statement you note that the Commission's report was issued on January 22, 1979, which is one month before the Supreme Court's decision in the *Royal Drug* case.

And my question is, aren't the Commission's comments on the court interpretations of the term "business of insurance" less accurate today than they were prior to *Royal Drug*, the *Pireno* case, and other similar cases?

Professor FOX. I don't recall the Commission having made such comments, but you may be right.

In any event, those cases and the Supreme Court decisions thereafter have made it clear that whenever there is a case on margin, the Supreme Court holds: antitrust law applies; the exemption does not apply.

My particular problem with McCarran-Ferguson is not the margin. The gap that I worry about is right at the heart of the business of insurance by any construction of "business of insurance"; for example, rate bureaus.

Mr. FISH. So it is your view that the courts are taking an increasingly proconsumer point of view in cases evaluating the scope of the "business of insurance" language which is in the act?

Professor Fox. Yes. When they are able to carve away the "business of insurance," they are doing so.

Mr. FISH. I would like to refer now to the part of your testimony, starting on page 9, dealing with the *Midcal* case and the State action doctrine because I think this deals with an important element of the problem we face.

If McCarran-Ferguson is repealed, the States could then step in with a more detailed and active regulatory structure, as I understand it, that would meet the *Midcal* test—the test of clearly expressed State policy and active supervision by the State?

Professor Fox. Yes. Of course. They already have the power to do that.

But to follow up on your question, if they are regulating but not actually actively supervising, they can step in and actively supervise and get State action protection.

Mr. FISH. All right. Well, then what about this: couldn't the State adopt a narrow regulatory scheme that meets the twin test of *Midcal* but that would result in allowing insurance companies to act in a more anticompetitive way than under the McCarran Act?

Professor Fox. Yes. And I do not oppose that. It is part of our system of federalism that States have a lot of power to regulate. They may decide that competition is not in the public interest, and that is their right.

Mr. FISH. Well, I surely didn't expect that answer. You mean to say we are basing this whole premise on the public interest in competition, and yet you are willing to have a State regulatory scheme that could well be worse for competition?

Professor Fox. The answer is yes, but I don't expect it would be worse. The State could fix prices, and this is not a procompetitive solution but they are likely to get a better result for insureds because you would have a Government agency trying to keep prices down rather than private parties trying to keep prices up.

I would expect a better result if the State regulates than if the competitors regulate. I am not prepared to second-guess a State if the State says I don't want competition, I want regulation.

I believe in federalism.

Mr. FISH. Well, thank you.

Our colleague Mr. McClory—and this has to do with the work product of the Commission. It is my understanding that the Commission's research and analysis focused very heavily on the property/casualty insurance field. My question is: did the Commission consider in any detail how the McCarran-Ferguson Act antitrust immunity affected the life and health insurance industry as well as property/casualty?

Mr. MCCLORY. No, it didn't, and the interesting thing is that under McCarran-Ferguson there is in some of the States a great deal of competition—price competition—and there is almost complete deregulation along some lines of insurance, and it seems to me that the right to have competition is there right now, where competition produces more or better or broader coverage and still assures the benefits that the insured expects to have.

Now, with respect to some types of insurance, it seems to me that it is very appropriate—not only for the insurance companies to have the right to pool their information as to expectancy of risks and with respect to what rates--premium rates have to be charged in order to guarantee the payment of the benefits, but in addition it seems to me that this right has to exist for the benefit of the consumers.

I think that Judge Bell made a very good point, and that is he feels that there should be a high degree of certainty, especially in the insurance industry, and Professor Fox, in her statement, in my view, in my interpretation, takes the position that the principal benefits that the insurance companies require right now is assured pretty much because of the case law and existing law, and we don't need McCarran-Ferguson.

I think that it is better to have the certainty of McCarran-Ferguson than to not have it and to rely on what the courts may or may not decide with regard to exemptions, with regard to competition, with regard to other issues that might be involved.

Mr. FISH. I thank you for that, and my last question can be answered by either one of you or both.

I am told that States apparently received about $3.1 billion in tax revenues from the insurance industry. McCarran-Ferguson specifically recognizes the power of the States to tax in this area.

Now, were McCarran-Ferguson to be repealed, I wonder if there would be some question or shadow over the status of the authority to tax? Do you feel that a replacement statute would have to take cognizance of the State power to do so?

Mr. MCCLORY. I think there is some interest on the part of some insurance companies to get rid of State regulation and opt for Federal regulation. I think they feel that they would have a better deal with the Federal Government, just one regulatory agency instead of the multiple State agencies that they have to deal with.

I think it would be to the detriment of the small independent companies if that were to happen because they would probably not be able to compete with the larger companies. They would not be able to cope with the ramifications of Federal regulations.

Mr. FISH. So you think a Federal regulatory scheme would result in a number of small businesses going out of business?

Mr. MCCLORY. I think they would be in a much more precarious position.

Mr. FISH. Professor Fox, would you like to comment on the power to tax issue?

Professor FOX. I would like to make one closing suggestion if I could.

If the McCarran exemption is not repealed, but the statute is kept more or less intact, I think it would be very useful to allow the exemption only in cases of the business of insurance where the State actively regulates and supervises. Perhaps you could import the language of *Midcal* so that private price-fixing would not be insulated from the antitrust laws.

If the language of the statute were amended to import the *Midcal* language, this would greatly help to close the gap.

Mr. FISH. Thank you very much. Thank you, Mr. Chairman.

Chairman RODINO. We want to thank both of you. Bob, it is really a pleasure to see you looking so well, and thank you, Professor Fox.

The next witness is Mr. Andrew Tobias, the author of "The Invisible Bankers," a book dealing strictly with the insurance industry.

TESTIMONY OF ANDREW TOBIAS, AUTHOR OF "THE INVISIBLE BANKERS," NEW YORK, NY

Chairman RODINO. Mr. Tobias, I understand you have a Harvard MBA; is that correct?

Mr. TOBIAS. Yes, sir.

Chairman RODINO. What led you into this study of this industry?

Mr. TOBIAS. I had spent some years writing more popular books, and when the editors at Simon & Shuster suggested I do something serious and spend 2 years looking into something that had not been looked into—namely, the insurance industry—I decided this was, indeed, a serious and useful project, not tremendously commercial, but worth 2 years. It wound up taking 5 years.

Chairman RODINO. Will you proceed, please.

Mr. TOBIAS. Mr. Chairman, with your permission, rather than read the prepared testimony——

Mr. RODINO. Yes. We will insert your remarks in the record in their entirety.

Mr. TOBIAS. I am very pleased to have the opportunity to be here this morning, even though I would like to make it clear that there are limits on my competence. I am in no way an expert in the field of antitrust nor even really an expert as to the details of the insurance industry. The industry is so large and encompasses so many different facets that to be an expert in all the details of all of the facets would take more than a lifetime.

Having said that, though, I do feel, after 5 years' work on the book and a year of responding to the industry's response, that I have a good feeling for the overall structure of the industry and some problems in it. I have no problem with applauding the industry for the vital risk spreading, risk transfer, and capital formation functions that it provides, and I have no problem supporting the industry where the industry is under attack unfairly.

Last year at the height of the unisex insurance rates debates, I believed the industry position was correct and was happy to do my best to support it on the "Today" show. But ordinarily, I don't agree with the insurance industry. The major finding in my book is that this is an enormously inefficient industry. There are nearly 2 million people employed in the business—and I hasten to point out that these are by and large very fine, hard-working, dedicated, honorable people—but that's an awful lot of people to be employed in the provision of insurance for this country.

When I first found that number, I tried to understand just what it meant, because large numbers are difficult to grasp, and I looked for analogies. The first analogy I looked at was the Postal Service. Although I happen to be something of a fan of the Postal Service, very few people consider it a model of efficiency. And yet, here is an organization that is able to call on virtually every home and office in the country five or six times a week, to run 30,000 retail

stores that we call post offices, and to transfer and handle something like 119 billion pieces of mail each year, and it does all that work with a little bit more than one-third the number of people who are required to staff the Nation's insurance system.

So it struck me that this was a telling comparison. But coming closer to the insurance business, the banking industry sits on three times as much money and handles vastly more transactions than the insurance industry, and yet, at the time I wrote my book, even including the thrifts, there were a quarter of a million fewer people required to staff the Nation's banking system than the insurance system.

And then I simply looked back at history. In 1950, there were more than 7 million people employed in agriculture in this country and there were 800,000 people employed in the insurance industry. Over the last 34 years, the number of people required to grow the Nation's food and much of the world's food has declined from over 7 million to well under 3 million, where at the same time, the number of people required to provide the Nation's insurance has gone from 800,000 to nearly 2 million, more than double.

Of course, there's much more insurance to be provided, just as there's much more food being grown, but it strikes me that these last 34 years, if someone were to look back 100 years from now, would not be thought of as the years of the great tractor technology revolution, although there certainly has been improvement in agricultural technology, but the years of the computer revolution. Which precisely, it seems to me, affects the number crunching, paper shuffling sort of business that insurance is.

So for the employees to have more than doubled in this time, suggests to me that competition isn't working the way it might.

The inefficiency in the industry has to do with mistrust between insurer and insured, which makes for a highly inefficient claims settlement process, particularly on smaller claims. It has to do with isolation of an industry that has really lived in a world all to itself. There has been very little cross-fertilization within the industry or between this industry and others. It has to do with mutual ownership, which is such an important part of the ownership structure of the industry. It has to do with lack of disclosure, and it has to do with weak regulations and bad laws.

I might say that not everyone disagrees with my findings. Typically, as I went around defending the book, I found that people in the life insurance side of the business were quite adamant in agreeing with me about auto insurance and my stand for no-fault auto insurance, and so on. But, of course, disagreed in most cases on my points about life insurance, whereas people in the property/casualty side said everybody knows I'm right about life insurance, but I wasn't entirely right about property/casualty insurance.

The solution, it seems to me, or at least two of the solutions that would move things along and allow for improvement in the efficiency of the industry are, one, to allow a role for Federal oversight of the industry, because I do believe that State regulation has basically failed; and, second, to allow competition from without. This could be anyone, and the financial services marketplace is certainly becoming muddied and muddled these days with lots of different participants, but principally, in reality, this would be competition

from the banks. Appropriate safeguards would be necessary, but there is an awful lot of reason to think that the banks could spur the industry to greater competition and lower prices for consumers.

Thank you for your attention.

[The statement of Mr. Tobias follows:]

Testimony of Andrew Tobias

I am the author of a book about the insurance industry published in 1982, copies of which have been distributed to members of the subcommittee. I am delighted to have the opportunity to discuss some of its conclusions with you today.

Although there are those in the industry who must doubt it, I am a strong believer in our economic system. In college I ran the student business conglomerate. I am a Harvard MBA. I am an active investor. During the debate over unisex insurance rates last year, I appeared on the TODAY Show to support the industry position. I have no qualms about applauding the industry for its crucial role in our economy, in capital formation and in the spreading of risk. And I know the people in this industry are, for the most part, every bit as honorable, hardworking and dedicated as you and I. But I do not dwell on applause, because the industry has more than ample resources to applaud itself, and because, more to the point, there are some major structural flaws in the industry that have a real, negative economic impact.

I spent five years looking into the insurance industry and a sixth considering industry response when the book was published. I do not claim expert knowledge of every detail of the industry (nor certainly of the anti-trust laws). But I do believe I was able in those five years to grasp it in broad strokes.

AN ISOLATED INDUSTRY

Traditionally, insurance has been a cozy, isolated business. Few knew—or cared—much about it. The federal government, as you well know, left regulation of insurance to the states. And the only state legislators who much cared were, with few exceptions, those who were insurance agents themselves, or insurance company directors, or attorneys for insurance companies. And this is still largely the case.

It may be telling that my book appears to have been the first ever written for a general audience on the overall insurance industry. Here is this positively enormous industry, as I'll shortly describe, and at least until recently it has gone about its business largely ignored by the public, exempt from scrutiny by the federal government, and scrutinized at the state level in a manner often unrepresentative of the public interest.

This lack of scrutiny serves the industry well. I do not suggest any sort of "conspiracy"—although certainly in its early days, as has been well documented, the property-casualty side of the industry was a price-fixer's delight. I do suggest that, like any other, this industry is not eager to have people looking over its shoulder. It was Governor Nelson Rockefeller's insurance commissioner who told a group of industry executives: "Isolation is comfortable. How satisfying to be sure that no one understands us but ourselves."

Similarly, like any other, the insurance industry is not eager for competition. Yes, there are 5,000 insurance companies in the U.S., all vying for about $250 billion in annual premiums. (A pie that represents about $1,000 annually for each man, woman and child in the country.) But in fundamental ways the free market has been restrained.

THE OVERALL PROBLEM: INEFFICIENCY

The insurance industry is enormous. It surprises some people to know, for example, that State Farm (an outstanding company) has a larger capital base—more capital underlying its operations—than either Citibank or Bank of America. Which is fine. Size, in and of itself, is not in any way bad. What's bad is that the industry is also enormously inefficient. That is the entire thrust of my book: structural inefficiencies in the insurance industry, and how to fix them.

According to the industry's own numbers—and virtually all the numbers I use come from the industry—it employs nearly 2 million Americans. Nearly two out of every 100 Americans in the work force.

Naturally, employment is a positive thing. The problem is that, in my view, were these same services delivered rationally and efficiently, they could be provided by half as many people.

If you are one of the million employees whose jobs this notion threatens, inefficiency is not such a bad thing. But long-term, it cannot be good for the country, any more than it would be good to double employment in the automobile industry without increasing the output of cars.

The comparisons that follow are unscientific—and the industry is quick to dismiss them—but to me they are helpful in trying to gauge, in a general way, the efficiency of the insurance industry.

(1) Consider the U.S. Postal Service. The Postal Service—itself not generally considered 100% efficient—calls on virtually every home and office in this country five or six times a week . . . runs 30,000 retail stores we call post offices . . . and transfers more than 100 billion pieces of mail each year, much of it handwritten—and it does all this with just over *one third* the number of people required to staff the nation's insurance industry.

(2) Or consider the banks. The nation's banks sit steward over three times as much money as the insurance industry, process vastly more transactions (think how much more interaction people have with their banks during a year than with their insurers) . . . and yet at the time I wrote my book, a quarter of a million *fewer* people staffed the nation's banking system—including the thrifts—than were employed in the insurance industry.

(3) Finally, consider this: In 1950, 7.2 million Americans were required to grow the nation's, and much of the world's, food Today fewer than 3 million accomplish the same task. Agriculture is a highly competitive business; you have to be efficient to survive. By contrast, in 1950, 800,000 Americans provided the nation's insurance. Today the job takes nearly 2 million. Far from shrinking by more than half, the number has more than doubled. And yet I would submit to you that 100 years from now these past 34 years will not be remembered primarily as the years of the great tractor technology revolution, but as the years of the great computer revolution—the number-crunching, paper-shuffling revolution which, one would think, would impact few businesses as dramatically as insurance.

Yet over those years the insurance industry grew fatter and fatter. I doubt this could have happened in a truly competitive, free-market environment. One way or another, the consumer pays the price.

(It's true, of course, that life insurance rates have been declining. But this is the direct result of dramatic increases in longevity and interest rates, not increased productivity.)

Insurance raises questions of justice, equity and social structure. They are fascinating questions but basically unanswerable. One's answers depend largely on one's social philosophy. The question to which I think answers are possible is the question of efficiency. Because—Republican or Democrat, socialist or conservative—here is something we can all agree on:

Waste is bad; inefficient systems rob us all.

NOT EVERYONE IN THE INDUSTRY DISAGREES

Before I outline what I perceive to be causes of this alleged inefficiency, let me tell you that, despite it's obviously unpleasant conclusions, my book was not universally dismissed by the industry.

Without in any way suggesting that each of these individuals or journals endorses all aspects of the book, let me quote several:

"Tobias said that the business is inefficient. And he's right. He is clearly right. We spend too much money in distribution, administration, and in what is considered pure waste." (John Cox, then president of INA).

"Tobias is no slouch. He has done his homework." (*The Actuarial Review*, newsletter of the Casualty Actuarial Society).

"Tobias doesn't sacrifice accuracy in his quest for entertainment. The book is basically fair." (*The Actuary*, newsletter of the Society of Actuaries).

"I read every word of Mr. Tobias' book, which I didn't expect to do, but I found it extremely intelligent and extremely well written." (Benjamin Woodson, former chairman, American General Group).

"Must reading . . . an acid, perceptive, frequently funny and thoroughly researched dissection of the insurance industry in the United States." (Felix Kloman, noted insurance industry consultant.)

"Well done, substantially accurate in its conclusions." (Peter B. Lewis, chairman, Progressive Insurance Group.)

"Tobias obviously has a very breezy approach to our industry which is designed to sell books, but as far as I'm concerned many of the things he says are appropriate." (Collin Hampton, chairman, Unionmutual.)

"A serious, useful overview of the insurance industry." (Malcolm MacKay, senior vice president, New York Life.)

"Tobias is a balanced writer with a strong appreciation of insurance's basic virtues." (*Fortune.*)

"An extremely perceptive analysis . . . The surprising thing is how many [industry] experts agree with it." (*Institutional Investor*)

THE ANALOGY TO BANKING

U.S. insurance companies sit on $700-odd billion of our money. It is our collective savings for all manner of rainy days: cars crashing, buildings burning, appendices inflaming, breadwinners dying. Insurers are thus not unlike savings banks. Only, instead of each of us being able to withdraw what he or she deposits, plus a little interest, withdrawals are based on luck (the worse your luck, the more you get to withdraw).

When we collectively deposit $1 in a bank, we collectively get to withdraw $1 or $1.05 at the end of the year. Somehow, on the interest it earns on our money, the bank is able to pay for all its people and facilities and utilities and advertising and property taxes and the toasters it gives away and still is able to return our dollar, with interest, and, in most years earn a profit.

When we collectively deposit $1, by way of premiums, in many lines of insurance, we don't collectively get back $1.05 at the end of the year. Most of us get nothing, of course, and a few unfortunate souls get a great deal, but collectively we don't get back $1.05 or $1 or 90 cents or 80 cents. In many cases we get back only 75 cents or 65 cents or 55 cents or 45 cents—in some instances even less. The rest of our collective premiums get eaten up by the system.

Naturally, this varies dramatically from one type of insurance to another. Blue Cross returns 92 or 93 cents of each premium dollar in payment of claims. Some aggressively marketed cancer insurance politices return 50 cents or less (it being highly inefficient to provide insurance one disease at a time). Credit life insurance policies in some states return less than 30 cents of each dollar in benefits.

If this were the best we could do, then so be it. But it's not. A rational, properly competitive insurance system could greatly improve America's return on its premium dollar. I don't suggest we will ever get a fully rational system. Too many powerful interests stand in its way. But some improvements are surely possible. Said John Cox in a speech in Philadelphia in April, 1982: "We've got to deliver back to the buyer more than we do. . . . We spend almost 40 cents on the dollar between either distribution, administration of the underwriting or the administration of claims."

INDUSTRY INEFFICIECY AND WHAT TO DO ABOUT IT

The industry's structural inefficiency stems primarily from these causes:

Mistrust. The cost of investigating and adjudicating claims—or of not doing so, and thus allowing inflated or fraudulent claims to pass through the system—is enormous and, with respect to relatively small claims, inherently inefficient. Unfortunately, a "spiral of distrust" has developed between insurer and insured, and the friction of that relationship entails great cost. It is an important problem but, I think, beyond the focus of this Subcommittee.

Isolation. There has been almost no cross-fertilization of talent. An Aetna advertisement in 1980 was headlined, with admirable candor: "[Ours is] an industry that's spent the last 100 years listening mostly to itself."

Mutual Ownership. Who owns the large mutual insurers (which have so dominated the life insurance side of the industry, particularly)? For all practical purposes, no one does. The managements are, effectively, answerable to no one. Over the last century, with profit not a consideration, the incentives have been to grow large, not lean. To increase sales, not profit or efficiency. No general wants a smaller army.

The solution is not to outlaw mutual companies or to try to persuade policyholders to take an active interest in the workings of "their" company (in a recent election, 18.4 million Prudential policyholders were eligible to vote; 323 did). The solution is simply to let the free market work. Competition alone should force the mutuals to be efficient. But:

Disclosure. The free market doesn't work, in many lines of insurance, because only one party to the transaction—the seller—understands the product. Particularly in the sale of investment-oriented life insurance products, buyers have traditionally been unable to compare value. As a result, the industry has been under little pressure to provide it.

Price competition requires the ability of consumers to compare prices. The life insurance industry, while officially favoring disclosure, has effectively lobbied against

the sorts of simplified, standardized disclosure that would make comparing life insurance values practical.

Weak Regulation, Bad Laws

Until a few years ago, every state in the union had a law forbidding the sale of group auto insurance. An employer might want to offer it, employees might want to benefit from it, an insurer might be eager to underwrite it—but that didn't matter. It was against the law. We have group life insurance and group health insurance, and most people recognize these as valuable and efficient. But group auto insurance, even if all three parties to the transaction favored it, was illegal. Why? Because local insurance agents didn't want to lose commissions, and insurance agents are extremely powerful at the state level. (These laws have been overturned in some states over the last few years through the lobbying efforts of the Aetna and others eager to sell group auto.)

To this day it is illegal in every state for an independent insurance agent to rebate a portion of his commission. If an agent wanted to set up a high-traffic, discount operation to appeal for business on the basis of price, he would not be allowed to do so. I'm not sure, as a practical matter, lots of agents would want to set up such operations; and I am well aware that, these days in particular, there is not a lot of margin to spare in the P-and-L of the typical insurance agency. But it is interesting to me that there are laws in all 50 states forbidding this kind of price competition. Why? Because the agents don't want it.

Massachusetts Savings Bank Life Insurance, founded in 1907 by future Supreme Court Justice Louis Brandeis, has long been recognized as one of the very most outstanding consumer values available. But 47 states forbid the sale of savings bank life insurance; and in the three that don't, Massachusetts, New York and Connecticut, the banks have always been severely restricted. It is abundantly clear that these restrictions were for the benefit not of the people of Massachusetts, New York and Connecticut, but of the life insurers in those states.

There are stock industry arguments with regard to these three examples of restrained competition. It is said group auto insurance would discriminate against people who didn't have a group to belong to; rebating commissions could lead to dishonest dealings; banks have an unfair advantage in selling life insurance. Indeed, as is only reasonable and understandable, there are stock industry arguments with regard to virtually any criticism of the industry.

In many cases, and certainly with regard to the examples above, the arguments are not persuasive. But they generally prevail, because who is there to argue the other side? These are not popular issues; state legislation is largely controlled by the industry; and the federal government is required to step aside.

THE NEED FOR A FEDERAL PRESENCE IN THE REGULATION OF INSURANCE

In 1980, Harvard Business School professors Robert Miles and Arvind Bhambri conducted a national survey of state insurance commissioners. (Their recently published book: *The Regulatory Executives*, Sage Publications, Beverly Hills.) They asked the commissioners to identify and rank their various constituencies.

Eight constituencies were identified: state legislatures, insurance companies, agents' associations, the NAIC, the media, industry trade associations, the federal government and consumer groups.

Asked to rank these eight by "relative importance" to the policy-making process and "overall power," the commissioners ranked consumer groups and the federal government last. These two have the least influence.

Agents' associations ranked third in overall power (insurance companies ranked second). Opined *Life Association News*: "From any agent's point of view, [the survey] is pleasant reading, indeed."

True. But what about the public's point of view?

Ranked first in importance and power by the state commissioners, presumably for their power to fund the insurance departments, were state legislatures.

In that regard, I was privileged last year to be invited to speak to the Conference of Insurance Legislators, which comprises state legislators with a special interest in insurance. As it turns out, many of these legislators do indeed have a special interest in insurance.

One of the legislators I met told me that for many years he had run the largest insurance agency in his state, and that for ten of those years he had also chaired his state legislature's insurance committee. Then, he said, some years back, the press started getting onto a "conflict of interests" jag, and making a big fuss—"So here's what we did. I had this friend who chaired the roads committee. Well, I didn't know

anything about roads, and he didn't know anything about insurance—so we switched! And once a week, when the legislature's in session, we get together for lunch and he tells me what to do about roads and I tell him what to do about insurance. And so far," he told me, "the press hasn't caught on."

I believe this gentleman sees nothing improper in his motives or conduct. Who is better qualified to know what to do about insurance, he must wonder, than the state's leading insurance agent? But while I imply no intentional wrongdoing, I am equally convinced that the public has long been ill-served by our system of state regulation. Our state regulators range from a few exceptional ones who are competent and well-meaning but overwhelmed by the enormity of their task, to others who are unexceptional—and also overwhelmed.

THE TROUBLE WITH THE NAIC

There is, of course, a National Association of Insurance Commissioners. It's first priority, as best I was able to observe, is to stave off federal regulation.

Beyond that, its loyalties and priorities are unclear. Without doubting that much good thinking and policy-making has gone on within the NAIC, let me tell you what the NAIC has done on the issue of credit life insurance. (This is the coverage people are often persuaded to buy when they take out a loan. If they die, it pays off the loan balance.)

Most states have laws mandating the ceilings on credit life insurance rates. Presumably, the ceilings were imposed to keep the rates from being too high. Unfortunately, the mandated ceilings are themselves much too high. In most states, less than 50 cents of each dollar in credit life premium goes for benefits; in some, the figure is under 30 cents.

Disturbed by this situation, some state insurance commissioners moved the NAIC to adopt model regulation. But where that regulation could have recommended rates resulting in pay-outs of at least 75 cents in benefits, which would still have allowed handsome returns, the NAIC recommended a minimum 50-cent pay-out.

If the NAIC felt moved to deal with this matter in the first place, why not deal with it in the public interest?

TWO CONCRETE THINGS THAT CAN BE DONE

Solutions to the problems I've suggested are not all obvious. And even where they are obvious, as in the case of auto insurance, their practical implementation may be politically impossible. (The incalculable harm a handful of trial attorneys have done to the American people in the matter of auto insurance is the prime example.) But as a citizen, I would feel much better if there were a small corps of dedicated professionals at the federal level actively looking into these questions on an ongoing basis, and making recommendations they felt served the public. As it stands now, there is permanent, massive industry pressure on one side, and the occasional industry critic popping up on the other.

In 1980, over the President's opposition, the Senate passed a bill, by a margin of 77-13, banning the FTC from investigating or reporting on "the business of insurance." Was it because the senators had studied the industry and decided all was well? I doubt it.

The first thing that should be done is to remove the restriction on federal oversight of the insurance industry. The second is to allow competition from without. There are great efficiencies to be had in allowing the banks, among others, to sell life, auto and homeowners insurance. Certain safeguards would be necessary to assure the ability of the seller to meet its obligations and to prevent coercive sales tactics. But such safeguards would not be difficult to devise. In the case of credit life insurance, for example, the existing mandated rate ceilings, if we are to have them at all, could be lowered; anticipated benefit pay-outs could be prominently disclosed; customers could be given a 30-day right of cancellation, with a prominent, standard legend. (E.g., "It is illegal for a lending institution to force the sale of insurance by threatening to withhold credit. If for any reason you are not satisfied with this policy, you have 30 days from the date of issue to cancel without penalty.")

The lines between the insurance industry and other arms of the financial services industry are already blurring fast. One little-noted recent example is in the financing of tax-shelter investments. Where in the past banks did a large business issuing letters-of-credit to guarantee the future-year capital contributions of limited partners, insurers have recently captured much of this business, issuing surety bonds instead. The same credit-guaranteeing function is performed, only now the insurance industry gets to do the job instead of the banks. That's fine. The more competition the better.

But as the several arms of the financial services business become increasingly tangled—and on a global basis, at that—there is a need for the federal government at least to keep abreast of, and possibly to influence, events.

There is much more to be said. I ask you why the federal government is not permitted to develop and maintain the competence to say it?

Chairman RODINO. Thank you very much, Mr. Tobias.

On page 8 of your statement you state that the free market doesn't work in many lines of insurance, because only one party to the transaction—the seller—understands the product. What kinds of information does the potential buyer need to have in order to be able to compare products and make informed choices, especially in this industry?

Mr. TOBIAS. Well, the most important piece of information, in many instances, is simply the payout, how much of the consumer's dollar is going to be used to pay benefits, whatever type, and how much will be consumed in the selling and underwriting and processing process. If I can use the analogy of a charity, we all believe in charity, as I certainly believe in insurance, but when you come across a charity that is using only 20 cents of your dollar for the charitable purposes you intend and 80 cents—just to take an extreme example—for fundraising, you say, "Gee, this isn't the charity I want to support."

By the same token, if you are inundated with insurance offers through the mail, as many of us are, some of which are good and many of which, in my view, are not wonderful values—you, as a consumer, really don't have the resources to investigate how much value is provided. If there were a disclosure that either 80 cents or 50 cents or 20 cents of the premium dollar would be expected to go for benefits and the rest for overhead and profit, that would give the consumer an important piece of information. In the case of credit life insurance, there are States where less than 30 cents to the dollar is paid out in benefits and the remainder is consumed by the system.

I believe in the free market, and I believe in profits and private enterprise, so I wouldn't want to outlaw a company from offering a deal like that, but I would also like the buyer to know what, in essence, he or she is getting, and I think many buyers faced with that kind of statistic, or some of the travel insurance offers, where as little as 10 cents of the dollar may go for insurance, might, in many cases, decide this isn't the best place to put his or her money.

In the field of life insurance, which is really, in many senses, the most important—we have a Truth-in-Lending law which, I think, works quite well when people go to borrow money—but we have no truth in life insurance. And basically, for the more complicated products, other than simple term insurance, the average consumer is just not able to make an informed choice, and the problem is that when consumers can't compare value, the industry is under no great pressure to provide it. There's lots of competition in the industry, but it's not based on price or value, in many cases; it's based on marketing competition.

So we do need better disclosure.

Chairman RODINO. How would you make possible the providing of that information?

Mr. TOBIAS. Well, in the field of life insurance, to the extent a product is more complicated than term insurance, it seems to me that what is needed is a certain amount of standardization, which would certainly cause the life insurance industry a great deal of difficulty, because it is so marketing-oriented. But in homeowners' insurance, for example, there are two or three basic forms and policies. It doesn't seem to cause anyone in the industry too much trouble. In life insurance, if there were some standardization and if there were some unbundling in the price information, so that you knew what you were paying for insurance, then it would be possible to calculate what kind of interest you're earning on the investment portion of your policy dollar.

Basically, what is needed, because this is a by-product pricing situation, is to have one benchmark for life insurance rates, term insurance rates—which might distinguish between smokers and nonsmokers, and in other ways, but one benchmark that was commonly accepted. And using that as a price of insurance, you could then calculate the investment return on the investment portion of your life insurance. The benchmark that would be set would not, in fact, be any sort of mandated rate for insurance, any more than the EPA guidelines are the exact mileage you get, but the EPA guidelines for mileage allow people to compare one against the other.

There needs to be a common standard, so that a comparison could be made.

Chairman RODINO. Mr. Tobias, one of your recommendations is that the regulation of insurance become a Federal matter. Can you state, specifically, what might be done? Should Congress establish a federal insurance agency, for instance, akin to the SEC, and if we did, what would its functions be? Would the agency be required to mandate disclosure to bring to the insurance buying public the kind of information that would make it easier to compare alternative policies? Would it bring cases against companies that might be dishonest or fail to disclose? Set approved rates? Collect information? You mention in your statement the fact that in 1980, over the President's opposition, the Senate passed a bill by a margin of 77 to 13, banning the FTC from investigating or reporting on the business of insurance. Would removal of the legal restrictions on the FTC be enough?

Mr. TOBIAS. Mr. Chairman, I would not try to be so bold as to say exactly how the Federal Government should organize itself in this area, but I do have a few strong feelings. One is that I see no reason for the Federal Government to regulate insurance rates—or set insurance rates, I guess is the phrase you used. But if nothing else—and perhaps a lot more, is warranted—the Federal Government should have a free hand to develop competence in this area.

Speaking not as an expert in organization or in the Federal Government, I, as a citizen, would feel a lot better if there were four or five people at the Federal Trade Commission, four or five people at the SEC, and I believe four or five people at the Federal Reserve, whose job was to be professional, dedicated people in the area of insurance, even if they didn't have regulatory powers, which is the next question, but so that when you have a hearing like this, or when there are matters, as there so frequently are in the area of insurance, there is someone—not anti-industry, but who has the

consumers' and the people's interest first and is not on the payroll of the industry—who has the expertise to come and present their view of the situation.

Right now—I think it was mentioned earlier this morning—there really isn't the competence in Washington to do that. My view, having spent some time trying to see what the States do, is that while there are exceptions, by and large, State regulation really doesn't begin to represent the consumer—the insured. In fact, I refer in my testimony to a study by two Harvard Business School professors in 1980, who polled State commissioners and asked them who their constituencies were and how they ranked in importance and influence. And the commissioners cited eight different constituencies, and the two least important—the two least influential, the two least powerful in the whole process—were the Federal Government and the consumer groups. The most powerful were State legislators, many of whom, in fact, have a special interest in insurance, because they either are insurance agents themselves or are attorneys who represent insurance companies; insurance agent groups who have their own agenda; and insurance companies.

So there has to be, I think, at least the ability for the Federal Government to develop this competence, particularly in light of the fact that the financial services industry is proceeding the way it is. You can't really separate one aspect of financial services from all the rest anymore. The lines are becoming too blurred for that, and as a result, the first thing I would hope is that something like the ban on the FTC from looking into insurance would be lifted. I don't believe it was really enacted because the Senate felt the insurance industry was performing wonderfully, and I don't think the Senate had a chance to look into the insurance industry.

I think it was done under the very logical pressure you'd expect from this enormous and influential industry. I don't, in any way, begrudge the industry its right to look out for its own interests, but I wonder who is looking out for everyone else's interest.

Chairman RODINO. We have 50 States, each with its own insurance commission. We have different regulations governing insurance in the various States. The insurance industry is wide and diverse—we heard former Attorney General Bell talk about insurance companies getting into investments and banking. In your testimony you pointed out that a kind of structural inefficiency exists in the industry that results in uninformed and short-changed consumers. Based on this information and on your study of the industry, do you see the need for some Federal oversight to ensure equitable treatment for consumers?

Mr. TOBIAS. I think there absolutely has to be.

Chairman RODINO. Do you state in your book that one of the principal problems or weaknesses is really the inefficiency in the structure of this industry and that this inefficiency results in some problems that impact negatively on the purchaser?

Mr. TOBIAS. I do. In the broadest sense, I think the same services that are provided by this industry could be provided in theory—it's not going to happen—but in theory could be provided by half as many people, if the industry were organized differently. If that's true, that would portend a lot of pain for almost 1 million people and I don't relish that, although, in fact, it would be over a period

of many years and largely by attrition. Certainly no one is going to fire 1 million people tomorrow. But what that means is that 1 out of every 100 Americans in the work force—not an insignificant fraction—is an unnecessary insurance employee. Not unnecessary in the sense that these aren't hard-working people, but if we could get the same job done with a million fewer people or close to it, we would have 1 percent of our work force freed up to do other things. At a time when unemployment is high, this may seem kind of utopian, but looking at it the other way, who would want to add a million people to the payroll of the auto industry today, if those million people couldn't increase the output or the quality of cars in any way?

In the short run, it would be a nice welfare program for a million people added to the rolls of the auto industry, but clearly, it would devastate the productivity that industry is trying to achieve. Productivity we realize more and more in this country is fundamental to the success of the economy. And if the insurance industry could be a lot more productive by being more competitive and by removing some of the bad laws, then almost all of us stand to benefit.

Chairman RODINO. One final question, Mr. Tobias. On page 13 of your statement you suggest that it would be appropriate to allow competition from without. You also specifically mention banks as a source of competition in the sale of insurance products. If the insurance industry operates as inefficiently as you suggest in your book and there are efficiencies in permitting banks to offer life and auto and homeowners insurance, wouldn't there be a great deal of dislocation in the industry, if banks were suddenly allowed into the insurance markets?

Mr. TOBIAS. If it were done suddenly, there would be quite a bit of dislocation.

Chairman RODINO. And how would you deal with that?

Mr. TOBIAS. Realistically, I suspect it wouldn't be done suddenly. I'm not saying it shouldn't be done suddenly—at least, in areas of life insurance, because even if it were done "suddenly," in quotes, it would probably be a period of time before the banks had a big portion of this market. But in the area of life insurance, for example, you could allow banks to sell up to $25,000 of whole life and $50,000 of term insurance for the first year and gradually, over a period of several years, raise that to an unlimited ceiling. My only hesitation there is, I fear, with the power of the insurance lobby, even if such a scheme were instigated, at some point along the way the process would be halted. In three States, as you know—New York, Massachusetts, and Connecticut—there is savings bank life insurance. Savings banks are allowed to sell insurance, but they have been severely limited in the quantity. And yet it's commonly recognized that Massachusetts' Savings Bank Life Insurance is just about the best value to the consumer that's available, even with the limitations that have been placed on the savings banks in Massachusetts.

The reason, of course, that the insurance industry is so terribly adamant in its opposition to competition by the banks is that the banks, being structurally more efficient in many respects, would grab a large share of this market and that, in turn, as you suggest, would put a lot of insurance people out of work. But to the extent

that they do have hundreds of thousands of people doing work that could be done without them, this is fundamentally not in the long-run interest of the country.

In the area of homeowner's insurance, the banks now typically will make a mortgage, and as a result of that will have to do an appraisal of the property. What is the sense in having two appraisals done—because the insurance company should do an appraisal also? It's inefficient to send two appraisers out, to send two sets of bills. In fact, when the insurance company doesn't send out an appraiser, to save money, this can set up a situation of encouraging arson, because many times property will be insured for more than it's worth and burned down.

As long as there are safeguards to prevent the bank from unfairly using its credit-granting ability to force a sale—and I'm convinced that there are some simple, practical safeguards that could be derived—as long as there are those safeguards, the only reason not to let the banks compete is to protect an artificially high number of insurance employees. And while I wish those employees no ill, I think we want to get the job done in this country as efficiently as we can and to let the free market work, and competition has always been at the foundation of that.

Chairman RODINO. Mr. Fish. I just want to remind our members, unfortunately, we do have a rollcall vote, and we will try to——

Mr. FISH. Go over and come back?

Chairman RODINO. Well, Mr. Tobias is our last witness. We will take that time, unless—Mr. Edwards, do you want to come back afterwards? Do you have any questions? I think we'll take the time.

Mr. FISH. I don't know if I have that, because I have several questions.

Mr. Tobias, your book contains very little discussion about the matter before the committee this morning, the McCarran-Ferguson Act. In fact, I think your comments are restricted or confined to one page. And my question is: Is this lack of discussion an indication that the McCarran Act is really not a significant factor in your overall evaluation of the insurance industry?

Mr. TOBIAS. No, sir. I think it's a reflection, partly, of my not being an expert in antitrust law, and I don't pretend to know the specific details of how the Federal Government can assist in improving competition in the industry, but I do think that, in addition to that page, there are several references throughout that State regulation isn't enough and that the industry couldn't have grown as fast as it has in a truly competitive environment. So the thrust of the book, while not dealing in legislative specifics, is clearly that, although the industry is seemingly competitive, the competition really doesn't work as it should.

Mr. RODINO. Mr. Tobias, we're going to break now and go vote and return, so you will please wait here until we come back.

Mr. TOBIAS. Yes, sir.

Chairman RODINO. Thank you.

[Recess.]

Mr. EDWARDS [presiding]. The subcommittee will come to order. The gentleman from New York, Mr. Fish.

Mr. FISH. Thank you, Mr. Chairman. Thank you for being patient with us, Mr. Tobias.

I am going back to this question of inefficiency in the industry, and your reason for thinking so is, you claim the industry employs 1 million superfluous employees. Now aside from comparisons with the Postal Service or with agriculture, and so forth, can you explain, specifically, how you reached that figure of superfluous employees?

Mr. TOBIAS. Well, it's very clearly a rough figure and meant to be a rough figure and presented as a rough figure, but on page——

Mr. FISH. Page 18? I think it's page 18.

Mr. TOBIAS. Well, the pages are unnumbered, but it's 42 of the book. There is a pie chart, and it tries to go category by category over the area. The biggest two areas have to do with agents and brokers and clerical workers. And I'll just give you, if I may, one example. It doesn't directly concern the subcommittee, but in the case of auto insurance, we, as a Nation, believe very strongly that everyone who drives should have automobile insurance, not so much necessarily because we're worried about them, as because we are worried about us—they might hit us—and we want them to be insured. And if something befalls them, we want them to have adequate coverage, because one way or another, someone has to pay for their medical costs. And yet, even though we want everyone to have automobile insurance, we require people to buy one policy at a time, and we spend about 25 cents of every dollar in automobile insurance premiums selling and underwriting policies. This is an inherently inefficient system.

If we sold unemployment insurance the same way, the cost of providing unemployment insurance would be enormously higher. And I don't doubt there are any number of insurance agents who would love the opportunity to take a commission and sell it door to door.

So structurally—through no fault of any individual agent or any individual auto insurance company—structurally, this is inefficient. There are a lot more people involved processing these forms than are needed. In fact, as I point out in my statement, staying on the field of auto insurance, until recently, it was illegal in every State in this country to provide group auto insurance. I think there are very few members of the subcommittee who would doubt that group insurance, whether it be group life or group health, or in this case, group auto, has a certain efficiency attached to it. And in fact, group life and group health insurance are tremendously important in this country. But there has been, until recently, no State group auto insurance.

Now those laws are gradually beginning to change. But there were laws against this, not because group auto insurance was inefficient or was not in the interest of people who might want it, but because it was not in the interest of agents. And the agents are very powerful at the State level.

In the field of life insurance, which is a very big part of this inefficiency, we have a life insurance delivery system that was largely built before the advent of television and mass media advertising, before the advent of checking accounts and credit cards. We are selling life insurance much as we sold it in 1840. The world has

changed, but the industry hasn't changed all that much with it. And I would argue that one reason is that people haven't been able to compare life insurance prices.

The most interesting example to me is in the field of individual retirement accounts. Congress, in its wisdom—and I very heartily applaud this—2 years ago changed the law so anyone who earned money could open an individual retirement account. As a result, tens of millions of people have opened accounts, where they will put away as much as $2,000 a year in very much the same kind of situation that is involved in whole life insurance—the traditional life insurance product.

The life insurance people say you've got to have a huge sales force; you've got to sell life insurance one policy at a time, door to door; we need the hundreds of thousands of people we have, because you could never get somebody to take $1,000 or $2,000 a year and save it for retirement and not be able to touch it for 10 or 20 or 30 or 40 years. And yet give people something simple, which the IRA's are, unlike some of the life insurance products, give them some place convenient to get it, and there are already banks on just about every street corner—and give them an incentive to have it—and of course, there are tax incentives to the IRA, just as there are tax advantages to whole life—and amazingly, without $500 per account in sales charges or whatever the number would be, and without a force of hundreds of thousands of sales people, tens of millions of these accounts have been set up in the last 2 years.

And that's an awfully efficient way to enhance capital formation in this country, an awfully efficient way to get people to save for their retirement, and it just happens through no particular fault of the insurance industry that there are some things they are not structurally terribly well set up to provide.

So this is my approach to the numbers. I don't say a million is the exact right number, and I certainly don't say we're going to get all the reforms that would totally rationalize the industry. Someone else might say 700,000, someone else might say a million one.

Mr. FISH. I think we can both agree that these companies are profit-motivated, and I just find it difficult to believe that they would carry a million superfluous employees.

But in any event, I gather what you are talking about here is efficiency, and it may be a characteristic in the business of much more personal salesmanship than would appear in other industries.

But at least it has nothing to do with antitrust, as I understand it.

Mr. TOBIAS. Well, in the case of the life insurance industry, I don't think you would call it antitrust but——

Mr. FISH. I mean, you are not really asking us to get into regulation in order to add a million people to the unemployment rolls?

Mr. TOBIAS. I am sorry?

Mr. FISH. You are not really asking us to get into a regulatory scheme in order to add a million people to the unemployment rolls?

In other words, you use the word "free up" a million people to be unemployed.

Mr. TOBIAS. Well, put that way, the answer is no. But what I would like to see, if in fact through regulating adequate disclosure

and allowing true competition you wound up over a period of years—and I doubt it would be this extreme—but if you wound up trimming the ranks of the insurance industry by a million people you would also trim from the cost of consumers' purchases of insurance a million salaries and the overhead that goes with that.

Prices would come down, and, indeed, the economy would be more efficient. I really have a hard time thinking that this country would be better off if we could somehow add a million people to the payroll of the auto industry or any other industry you might name without creating——

Mr. FISH. A lot of my friends in Detroit would think so, though. Doesn't an industry with 5,000 companies competing indicate a very highly competitive operation?

Mr. TOBIAS. It is competitive in the sense there are a lot of companies, but the competition isn't in many cases based on price.

If I can just finish the thought. Obviously, if we had an auto industry in Detroit that could use a million people productively because we started exporting to Japan in great numbers, instead of vice versa, that would be wonderful for all of us and the country as a whole. But to add a million unproductive people to the rolls, if there is no need for them and nothing productive for them to do, would simply destroy the auto industry. To have people working unproductively is a terribly uneconomic, negative sort of thing for the American people as a whole.

Naturally, any individual life insurance salesman doesn't want to have to find a different field, and I feel for these people. It may not seem that way, but I do.

Mr. FISH. I get back to the point of inefficiency in the industry isn't necessarily an antitrust issue that needs to concern us. And, of course, there are people who are proponents of large make-work propositions in order just to give people jobs, and we keep saying wouldn't it be better to let the private sector do it, which they seem to be doing.

Let me turn to one final matter, and that is the banking and insurance analogy that you cite in your book and in your testimony.

You make this analogy between the two. The Commission report that we are working off of today, on page 228, states:

> A key feature in all insurance products is that the insurance company does not know its cost at the time of sale. That is, they have to predict their losses and spread risks in order to protect individual policyholders.

Now, banks, on the other hand, receive security and return for their loans in order to cover their business risks. Now, are these two industries really analogous?

Mr. TOBIAS. Well, in many respects they are. Insurance, certainly in the personal lines of insurance that I think we are largely concerning ourselves with today, is much less a risky business than the highly profitable business of transferring largely predictable risks, and I am all for profits, also.

You said before it is strange that there could be all these extra people on the payrolls when people are out to make a profit.

But it raises the important point especially on the life side of the industry—that mutual ownership is a very large part of the ownership structure, and, ironically, even though mutual ownership in

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theory should be for the benefit of the policyholders, in a mutual situation the emphasis is not on profit. The emphasis is not on efficiency. The emphasis is on size.

No general wants a smaller army, and if you run a mutual insurance company, the larger the company is and the larger its sales, by and large the happier you, as chief executive, are. There is also the point that you are responsible, at least from an ownership point of view, to no one, as the chief executive of a mutual insurance company.

And as a result, even though there are 5,000 companies, without allowing a free market to work through adequate disclosure, the pressure is not brought to bear to provide the sorts of efficiency that I think we all want.

My premise in writing the book was that there are all sorts of questions about insurance that are very interesting from a philosophical point of view, but I didn't try to address them because your answers depend on your own ideological framework.

But the one thing that seemed to me we all could agree on—Republican or Democrat, Socialist or capitalist, whatever—is that efficiency is good, inefficiency and waste are bad, and that over the longer run an economy that doesn't work to let the free market function, and to allow economies and efficiencies, is going to suffer, and I think a case could be made that over the last 10 years this is one of the reasons we have been suffering.

Mr. FISH. Mr. Tobias, I think we can also all agree that nothing in McCarran-Ferguson would preempt this Congress or any Congress from passing a law with respect to greater disclosure or disclosure of policies along the lines that you have been talking about.

That is all I have, Mr. Chairman.

Mr. EDWARDS. Thank you. You have been very helpful.

First of all, Mr. Tobias, of these people who are overemployed, the excess number of people employed in the industry, does that include people who are in local agencies, the little guy on the corner?

Mr. TOBIAS. Yes, sir.

Mr. EDWARDS. So some of them would have to close down? The State Farm guy who you see on TV taking care of the neighborhood?

Mr. TOBIAS. I think the hard reality is if you want a free market to work and if you want competition and you want efficiency, then to the extent I am right the ranks will be thinned—through attrition, I hope largely, but one way or another.

And, of course, as you know, this is a field with an enormously high turnover. Not so much the agent you are talking about for State Farm but certainly in the life insurance sales side of it. So there is quite an opportunity for attrition.

But if I am right that it is inefficient, then, yes, there will have to be dislocations, and that is the price you pay for a vibrant economy that changes with the times and evolves to remain efficient and competitive.

Mr. EDWARDS. Well, then the agent would be like the automobile dealer who is free to offer rebates; then the agent could offer rebates under what you suggest?

In other words, we would have real competition rather than these anti-rebate laws that practically all the States have where the agent is almost guaranteed a certain premium and can't give half back to the customer for coming to him, right?

Mr. TOBIAS. That is an interesting aspect of this. There is now, to my surprise, I found when I looked into this—and I believe this is still the case—every State in this country has a law forbidding agents from rebating commissions or discounting commissions. If an agent wanted to try to set up a high traffic, high volume, McDonald's type operation that charged low prices, he or she would be forbidden by law to do this rather competitive thing.

In point of fact, it is a tough world out there for the agents these days, and I don't think an awful lot of them would want to cut their commissions even if they were allowed to. So I don't think there is a tremendous savings to be realized, at least currently, to the public for changing this. But to me, the existence of these laws in every State says a lot, about the overall competitive framework. In 1975 we abolished the fair trade laws; in 1975 we unfixed the commissions on Wall Street; and yet here is one field where in every State there is a law specifically saying, hey, you can't compete this way. To me, this is indicative of just one more aspect of State regulation designed not to serve the public so much as the vested interests at the State level who really care about insurance.

And one of the problems with this industry is that with the occasional exception of some automobile rate cases, this is an industry that the public just doesn't have a great interest in. It is not terribly exciting.

So if the Federal Government isn't there to take the side of the people, you are left with the States doing it all, and in case after case I have found the State governments not tremendously responsive to the people.

Mr. EDWARDS. Well, what you are saying is that, because of their exemption from the Federal antitrust laws, they are not really in competition with each other to the same extent that we require other businesses to be in competition.

Now, if by making them subject to the Federal antitrust laws with regard to competition, would that mean that prices will come down?

Mr. TOBIAS. I am not an expert on antitrust law, and from a layman's point of view, it would seem reasonable to me that that would be the case.

The one thing I would say—from what I heard earlier today, since we are now, after 39 years, reevaluating this—is that the industry should have to show the areas in which it deserves some special treatment that no other industry has. If Congress in its wisdom decides the industry is right in those areas, fine.

But I suspect there aren't a lot of areas where the insurance industry needs a special exemption.

Mr. EDWARDS. Well, the exemption from the antitrust laws also exempts insurance companies from the Federal Trade Commission, and that is an agency that could force disclosures.

Mr. TOBIAS. That is particularly harmful because State regulation doesn't ultimately work. It makes no sense to me as both a State and Federal taxpayer that my Federal Government isn't al-

lowed at least to develop competence in these areas, to press its case, and probably—certainly with disclosure—to play a regulatory role.

The biggest investment a family may ever make isn't a stock or bond, it is some life insurance product.

And yet the SEC, even if it wanted to—it is charged with protecting the public in the areas of securities, but as soon as you put the mantle of insurance over it in a single premium-deferred annuity, such as the Baldwin-United annuity or in the case of universal life insurance or variable life insurance or whole life insurance—any of these products which are very largely investment products—the SEC, even if it wanted to, is not, as I understand it, in a position to have any oversight over this.

It just makes no sense to me except from the point of view of the insurance industry. And I don't think the laws should be written for the insurance industry. I think the laws should be written with their concerns in mind but for people as a whole.

Mr. EDWARDS. Well, I am wondering what percentage of the surplus employees that you describe as working for the insurance companies themselves—Aetna, Equitable—are agents.

How many are agents and how many are actual salaried employees of the insurance company?

Mr. TOBIAS. I couldn't honestly give you a very good estimate, especially because of the distinction between agents who are salaried and some who are independent, but in essence work for one company.

I don't have the expertise to give you a meaningful breakdown, but you can see all sorts of instances of both. It took this awful inflation we have had to bring it about, but, finally, consumers have begun focusing more on shopping for insurance, and certainly a part of the "regulatory" burden does fall on the consumer. One way to make the insurance industry more efficient is for consumers to become better shoppers. Having been motivated to do that by inflation in large part, there have been some changes in the insurance industry, and in fact for the first time perhaps since its founding the Equitable Life Insurance Association, for one, actually let people go. It was major headline news, and there are other examples in the book of companies that have tried to motivate their employees or institute new systems which, indeed, have made the companies more efficient.

But as to the breakdown as between company salaried and agents, I couldn't say.

Mr. EDWARDS. My last question is: you don't think that state regulation has been a success; do you think the States have the money and the staff and the inclination to do the job of regulating properly this immense industry?

Mr. TOBIAS. They don't currently have the budgets or the staff, and, more importantly, I think very few of them have the inclination, and that is the nub of it because the reality of the situation would appear to be in most States at most times that the only people who really care about this industry are the local people in the industry, and I can't blame them.

If I were one of them, I would care about it a great deal also, and I can't really blame the consumers for not being interested because it is complicated and it is boring.

So you have, on the one hand, a very powerful group of people who care a great deal, pleading their case and, on the other hand, in many cases nobody to plead the other side.

I was in a Western State talking on a panel where the State insurance commissioner was one of the speakers, and he said, "You know, you are right. I deplore the low payout ratio of credit life insurance. It is terrible in this State, and I think it is awful."

And at the question-and-answer period, I said, "Mr. Commissioner, there is something I don't understand. You say you deplore this and you have deplored it for some time. You are the commissioner of insurance for the State. Why don't you change it? Why don't you either force adequate disclosure so the people will recognize what a poor value it is and pass it by, or, since every State has a law that mandates ceilings on those rates, why not come out and recommend that the law be changed to be a good law that has a ceiling that would be appropriate so good value were provided?"

And he was somewhat nonplused by the question, and he said, "Well, you don't understand the realities of it. There's tremendous pressure from all sorts of people."

And I can understand that from his point of view. But we need to get a group of people who have a long-term professional interest in this at a level where, although there may be some influence brought to bear, you can have professional people, not part-time authors, coming in here to give you the information you need to make a proper decision.

Mr. EDWARDS. Thank you very much, Mr. Tobias, for very helpful testimony.

Mr. TOBIAS. Thank you, sir.

Mr. EDWARDS. At this time the subcommittee is adjourned.

[Whereupon, at 11:50 a.m., the subcommittee was adjourned, subject to the call of the Chair.]

COMPETITION IN THE INSURANCE INDUSTRY

THURSDAY, MAY 3, 1984

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The subcommittee met in room 2141 of the Rayburn House Office Building, Hon. Peter W. Rodino, Jr. (chairman) presiding.

Present: Representatives Rodino, Hughes, Fish, and Moorhead.

Staff present: Alan A. Parker, general counsel; Jonathan Cuneo and Warren S. Grimes, counsel; Marilyn Falksen, research assistant; Alan F. Coffey Jr., and Thomas M. Boyd, associate counsel.

Chairman RODINO. The subcommittee will come to order.

Mr. FISH. Mr. Chairman, I ask unanimous consent that the committee permit the meeting this morning to be covered in whole or in part by television broadcast, radio broadcast, and/or still photography pursuant to rule 5 of the committee rules.

Chairman RODINO. Without objection, it is so ordered.

Today, the Subcommittee on Monopolies and Commercial Law continues its oversight hearings on the McCarran-Ferguson Act and competition in the insurance industry. The topic the subcommittee will address this morning is whether there is enough buyer information for the insurance marketplace to operate efficiently.

Critics of the insurance industry claim there is a market failure, that the market does not operate efficiently and competitively, because of a lack of information. They suggest that only one party to the transaction—the seller—understands the product, and that it is very difficult for the average American to get objective, understandable information about insurance policies.

If buyers do not understand what they are purchasing, they cannot shop for the best product at the cheapest price. In this situation, there would be no incentive for insurance companies to compete on the basis of low price and good quality.

Inefficiencies could develop in the industry, and prices would rise for all buyers.

On the other hand, insurance is a very complicated product. It is not easy to say what kinds of buyer information are useful, what form that information should take, and through what medium it should be distributed. In addition, providing information does not come free; the cost of this service must also be considered by the subcommittee.

Today, we are attempting to collect information on whether or not a market failure exists because of inadequate information. The subcommittee intends to receive comments from all parties con-

cerned, including consumer advocates, insurance companies, agent groups, and State regulators. The subcommittee hopes to learn what kinds of information consumers need, what information is currently available, how and by whom it is produced, and how it is distributed to potential buyers.

Our first witness this morning is Federal Trade Commissioner Michael Pertschuk, who was Chairman of the Federal Trade Commission at the time the FTC studied several aspects of the insurance industry. We will then hear from a panel composed of Mr. Herb Jaffe, an investigative reporter for the Newark Star Ledger who has written about the insurance industry for a nearly 20 years; Dr. Joseph Belth, professor of insurance from Indiana University and noted life insurance expert; and Dr. Buford Brinlee, who operated an information service for automobile insurance buyers in Texas.

We will then hear from representatives of various insurance agents' groups—Frank Patterson on behalf of the Independent Insurance Agents of America; Mr. David Ream on behalf of the Professional Insurance Agents; and Mr. Robert Pierce, chartered life underwriter, on behalf of the National Association of Life Underwriters.

Before I call the Commissioner, does the gentlemen from New York have any comments?

Mr. FISH. No, sir.

Chairman RODINO. If not, we will proceed. First we will hear from Commissioner Pertschuk. Mike, we welcome you. I know that you're aware of the constraints that we have insofar as time is concerned. Of course, you have a wealth of information to impart, and I know that it's all contained in your prepared statement, which we will include in the record. We would urge you to summarize your statement, and then we will present you with some questions.

TESTIMONY OF HON. MICHAEL PERTSCHUK, COMMISSIONER, U.S. FEDERAL TRADE COMMISSION

Commissioner PERTSCHUK. Indeed, I will, Mr. Chairman. I will hit just the highlights of my prepared testimony.

Mr. Chairman, it's a cold fact that sales of investment-type life insurance policies as a whole are threatened by clear comprehensible disclosure, because such disclosures provide the opportunity for consumers to compare alternative investments, to the inevitable detriment of life insurance policies which are, as a whole, inferior investments.

Perhaps worse, the entire insurance agency edifice in this country is constructed upon perverse incentives. By and large, the poorer the investment, the higher the commission earned by the agent. Clear and useful life insurance cost disclosure requirements are not in the economic interest of a vast majority of life insurance agents.

And thus, like the cigarette industry, the life insurance industry has a deep economic stake in maintaining the status quo: A chronic state of consumer confusion without the Feds upsetting the applecart.

I am delighted to appear before you this morning to share my views on insurance cost disclosure, in particular, because I am on the verge of departing Government, and therefore have no particular reason to worry about the heavy-handed wrath of the insurance industry. [Laughter.]

For the same reason, I greatly admire your courage in undertaking this inquiry.

I detail in the first few pages of my prepared testimony the experience we had, particularly with the other body of the Congress, at the time of the presentation of our life insurance cost disclosure report. As you know, the study was fully supported by the relevant committees of Congress, which had asked for the report, insisted upon the report, and had no doubt of our authority to make the report. But when the report was forthcoming and caused upset in the industry, the attitudes of many Members of the Senate changed. And so we were almost prevented from even studying life insurance.

A proposal emerged from the Senate Commerce Committee, which was essentially a legislative prefrontal lobotomy, which prohibited the Commission from even thinking about life insurance. That was modified in conference so that the Commission couldn't think about it unless told to think about it by one or the other Commerce Committees, but no other bodies of the Congress. Indeed, the Commission is now undertaking several studies at the direct behest of the House Commerce Committee.

Moving to the substance of the issues that you've raised, Mr. Chairman, there's no doubt that industry witnesses will assure you that consumers are well served by the continuing absence of any Federal role. The argument generally is made that a proliferation of competitive sellers—there are lots of insurance companies—operating under historic State regulation ensures that all is well in the industry.

Now, I am not so sure. 1984 brings us an insurance market that has more complex products and less useful disclosures than the market in 1979 when the FTC published its study. It is true that competition from alternative investment opportunities, like market money funds, certificates of deposit and annuities, has forced the insurance industry to change its ways, but unhappily, the changes don't help consumers make better informed choices about their insurance purchases.

First, the marketing structure of the industry has not changed. Agents remain the primary source of information for consumers. Even the best have no incentive to disclose lower rates of return. They do have an incentive to sell the most expensive policies, and the higher the agent's commission, the less net value the policy is likely to have for the consumers.

Even if agents were inclined to provide consumers useful information, agents themselves often do not have adequate information to compare the costs and benefits of different policies and alternative investments.

The industry's major response to competition from other investment opportunities has been to introduce a new product: universal life insurance. I am told that universal life may be marginally a better investment than whole life. But it is so complex that con-

sumers are likely to have an even harder time deciphering its real investment value. Also, there are a myriad of universal life policies. A company may even compete with itself and sell two or more different forms of the product, offering the agent a higher commission on one but not the other. There is no disclosure mechanism for consumers to use to compare these competing, complex investments.

A quick look at the industry dispels the idea that State regulation has solved the problem of lack of consumer information.

Since 1976, the State insurance commissioners' association—that's the NAIC—has continued to propose model disclosure regulations. In all fairness, some of NAIC's proposals have been adopted, in part, in about two-thirds of the States, and some of them have been useful.

But even the reform-minded State commissioners have not been successful in getting any State to mandate the disclosure of the one missing piece of information the FTC staff found essential in 1979: the rate of return. Neither the introduction into the market of new products nor State regulation has worked to make the insurance industry function as effectively as it can. The application of standards of Federal disclosure to consumers is perhaps the only way to repair this massive market failure.

No doubt, the industry is uncomfortable with the idea of even careful, limited Federal intervention in situations where Federal consumer protection policies are violated, but it is time to hold the insurance industry to the same standards of business conduct that govern other industries in America. The Federal Trade Commission should be able to investigate complaints of deceptive advertising and marketing by insurance companies.

For example, I am informed that some companies have begun to market a no-load universal life policy, but there are indications that some of these policies are very loaded indeed, at both ends—with high charges deducted from the premium and high surrender charges when the consumer cashes in the policy.

A San Francisco area life insurance agent and securities agent told the Washington Post that the misrepresentations that go on in this business would bring license suspensions or revocations if they were selling stock instead of life insurance.

Again, a multitiered life insurance company has been accused by some of using high pressure tactics to sell consumers policies they don't need and don't understand. To my knowledge, not one State is investigating this company, and yet at the FTC we have considerable expertise with multilevel marketing schemes. We should be able to use that expertise to determine whether this company is violating the Federal law.

In my prepared testimony, I talk about the gaps in medigap insurance and the inability of consumers to compare value in that area, which, in part, results from the shape of Federal policies in Medicare and Medicaid, and yet we have no way of making certain that consumers have an ability to tell how the various Medigap policies fit into their health insurance coverage.

Mr. Chairman, investigations of alleged deceptive conduct, requiring clear presale information that consumers can use to make informed decisions, establishing a uniform Federal system of disclo-

sure on supplemental health insurance—these are modest suggestions for a limited Federal role in the insurance industry.

Insofar as the McCarran-Ferguson Act shields so basic an industry from national standards of fair dealing and informed competition, it remains a symbol of the political power of the insurance industry, not reasoned public policy.

Thank you, Mr. Chairman.

[The statement of Commissioner Pertschuk follows:]

TESTIMONY OF COMMISSIONER MICHAEL PERTSCHUK, FEDERAL TRADE COMMISSION

Dear Mr. Chairman: Insurance is very big business in this country. Estimates place insurance companies' assets between $500 and $700 billion. Consumers spend somewhere in the neighborhood of $140 billion in life insurance premiums. Two out of three Americans are life insurance consumers, with nearly 12% of most families' disposable income going to pay insurance bills. In fact, insurance is the 4th leading household expenditure, just behind food, housing, and taxes. And this industry that takes so much of our citizens' dollars conducts its business without having to abide by the standards governing business conduct that Congress has imposed on industries.

I have two main points I want to stress this morning. First, insurance consumers continue to suffer tremendous economic injury on a grand scale from inadequate disclosures, deceptive sales practices, and poor state regulation. Second, a substantial federal role in monitoring and policing the insurance industry is one major way to ensure that consumers are adequately protected against the shoddy practices in this industry. Since 1945, the states have had the opportunity to control the excesses of this industry. The deception and confusion that abounds in the insurance industry today is the best evidence that the states are either unwilling or unable to restrain this giant.

THE DEBATE OVER LIFE INSURANCE COST DISCLOSURE

There are many government/business issues which erupt in abrasions from time-to-time, but are capable of reasonably amicable resolution—such as advertising standards for deception in which all advertisers are required to play by the same rules. The interests of the industry as a whole and those of the public, as represented by government, are not inherently adversary. Though some members within an industry may lose, others can benefit; if the chronically deceptive are vigorously policed, the scrupulously truthful will benefit competitively—the government representing the broad public interest has no quarrel with the industry as a whole.

But that's not true with life insurance cost disclosure. Sales of investment-type life insurance policies as a whole are threatened by clear, comprehensible disclosure. Such disclosures provide the opportunity for consumers to compare alternate investments—to the inevitable detriment of life insurance policies, which are as a whole inferior investments. Perhaps worse, the entire insurance agency edifice in this country is constructed upon perverse incentives: by and large, the poorer the investment the higher the commission earned by the agent. Clear and useful life insurance cost-disclosure requirements are not in the economic interest of a vast majority of life insurance agents.

Thus, like the cigarette industry, the life insurance industry has a deep economic stake in maintaining the status quo: a chronic state of consumer confusion—without the feds upsetting the applecart.

I am delighted to appear before you this morning to share my views on insurance cost disclosure—in particular because I am on the verge of departing government and, therefore, no longer need fear the heavy handed wrath of the insurance industry. For the same reason, I greatly admire your courage in undertaking this inquiry.

Perhaps "heavy handed wrath" sounds melodramatic—exaggerated. It might be constructive for me to review with you the experience of the Federal Trade Commission in the late 1970s in undertaking simply to study—not to regulate—life insurance cost-disclosure in this country.

On July 10, 1979, I testified before the Senate Commerce Committee on the results of a life insurance cost-disclosure study that had been underway at the Commission since 1972.[1] I reported that the Commission's Bureau of Economics, in con-

[1] U.S., Congress, Senate, Committee on Commerce, Hearings on the FTC's Study of Life Insurance Cost Disclosure, 96th Cong., 1st Sess., 1979, p. 2.

sultation with several leading actuaries, had calculated that the average rate of return on the investment portion of all whole life insurance policies in the hands of consumers in 1977 was 1.3 percent per annum. The Commission had concluded—as many other students of life insurance marketing had also concluded—that this low level of return was directly caused by a marketing system that made it virtually impossible for a prospective policyholder—other than an actuary—to compare the interest yields of competing policies and of competing investment opportunities. The Commission had therefore developed a new model state life insurance cost disclosure law for consideration by state insurance commissioners. We did not propose federal intervention in insurance regulation.

All the Senate Committee members present expressed genuine interest and concern at the Commission's findings. Indeed, at the close of the hearings, Chairman Cannon took me aside and indicated that he had found the report so persuasive that he was reviewing all of his personal policies to determine whether they should be replaced.

The FTC study had been undertaken at the direct behest of the Senate Antitrust and Monopoly Subcommittee following its investigation during the early 1970s into life insurance marketing practices.[2] As recently as 1978, the House Commerce Oversight and Investigations Subcommittee had urged the Commission to complete its study, calling it "highly desirable, clearly justified," and "wholly lawful, proper, and appropriate." [3]

No murmur of discontent had been heard from the Senate Commerce Committee until the life insurance industry erupted in wrath. Then the members discovered the Commission's perfidy: One charged that the insurance investigation was a classic case of an agency running out from under Congress' control.

Chairman Cannon managed to contain his earlier private enthusiasm for the FTC report: "What we intend to do . . . is to be sure the FTC keeps its nose out of the investigation of the insurance industry." [4]

On November 20, 1979, the Senate Commerce Committee, by a vote of fifteen to zero, adopted an amendment to the FTC Act barring the Commission from ever studying insurance—a legislative prefrontal lobotomy. The Committee was so intent upon punishing the FTC for its imagined defiance of congressional will that it never considered the only relevant question that was before it as it considered amendments to the Commission's basic authority: was it not now in the public interest for the Commission to examine market and regulatory failures in the insurance industry?

That remains the basic question before you.

Fortunately Congress in 1980 left insurance consumers a small window of opportunity, by permitting the FTC to study insurance—but only at the direction of either the House or Senate Commerce Committee, and only through the end of a congressional session, unless there is a new request. While it is not clear whether anyone seriously thought this provision would be used—because of all its hurdles—the House Commerce Committee in fact recently directed that the Commission conduct three insurance studies. The strictures of this provision are so severe, however, that it is remarkable we have been authorized to do even these limited studies. The Commission's reports are due to the Committee by January 1, 1985.

Congressional action in 1979-80 showed me several things:

The publicity surrounding the Commission's findings on the low rate of return on whole life policies terrified the industry;

The industry cannot tolerate wide public understanding of the questionable investment value of whole life;

The industry's power over Congress was as awesome in 1979 as it had been in 1945 when it was successful in stampeding Congress to pass the McCarran-Ferguson Act.

INDUSTRY DEVELOPMENTS SINCE 1979

No doubt industry witnesses will assure you that consumers are well served by the continuing absence of any federal role. The argument that a proliferation of competitive sellers operating under historic state regulation insures that all is well

[2] U.S., Congress, Senate, Committee on Judiciary, The Life Insurance Industry, Hearings Before the Subcommittee on Antitrust and Monopoly, 93d Cong., 1st and 2d sessions., 1973-74.

[3] U.S., Congress, House, Committee on Interstate and Foreign Commerce, Life Insurance Marketing and Cost Disclosure, Comm. Print 95-72, 95th Cong., 2d Sess., 1978, p. 62.

[4] U.S., Congress, Senate, Congressional Record, 96th Cong., 2d Sess., February 7, 1980, 126, no. 18:1211.

in the industry is the standard theme trumpeted by the industry to justify perpetuating the McCarran-Ferguson exemption. I am not so sanguine. 1984 brings us an insurance market that has more complex products, and less useful disclosures, than the market in 1979.

It is true that competition from alternative investment opportunities like money market funds, certificates of deposit, and annuities, has forced the insurance industry to change its ways. But unhappily the changes don't help consumers to make better-informed choices about their insurance purchases.

First, the marketing structure of the industry has not changed. Agents remain the primary source of information for consumers; they simply have no incentive to disclose low rates of return. Agents do have an incentive to sell the most expensive policies, but the higher the agent's commission, the less net value the policy is likely to have for the consumers. And even if they were induced to tell consumers, agents themselves often do not have adequate information to compare the costs and benefits of different policies and alternative investments. The industry's major response to competition from other investment opportunities has been to introduce a new product—universal life insurance. I am told that universal life may be marginally a better investment than whole life, but it is so complex that consumers are likely to have an even harder time decifering its real investment value. Also there are a myriad of universal life policies—a company may even compete with itself and sell two or more different forms of the product, offering the agent a higher commission on one but not the other. There is no disclosure mechanism for consumers to use to compare these competing, complex investments.

A quick look at the industry dispels the idea that state regulation has solved the problem of lack of consumer information. Since 1976, the state insurance commissioners association (NAIC) has continued to propose model disclosure regulations. In all fairness, some of NAIC's proposals have been adopted in part in about two thirds of the states. But even the reform-minded state commissioners have not been successful in getting any state to mandate the disclosure of the one missing piece of information the FTC staff found essential in 1979—the rate of return.

A PROPOSAL FOR LIMITED FEDERAL INTERVENTION

Neither the introduction into the market of new products nor state regulation has worked to make the insurance industry function as effectively as it can. The application of standards of federal disclosure to consumers is perhaps the only way to repair the massive market failure.

No doubt the industry is uncomfortable at the idea of even careful limited federal intervention in situations where federal consumer protection policies are violated. But it is time to hold the insurance industry to the same standards of business conduct that govern other industries in America. The Federal Trade Commission should be able to investigate complaints of deceptive advertising and marketing by insurance companies. For example:

I am informed that some companies have begun to market a "no load" universal life policy. But there are indications that some of these policies are very "loaded" at both ends—with high charges deducted from the premium and high surrender charges when the consumer cashes in the policy.

A San Francisco-area life insurance agent and securities salesman told a *Washington Post* investigative reporter: "The misrepresentations that go on in this business would bring license suspensions or revocations if they were selling stock instead of life insurance."

A multi-tiered life insurance company has been accused by some of using high pressure tactics to sell consumers policies they don't need. To my knowledge not one state is investigating this company. The FTC has considerable expertise with multilevel marketing schemes. We should be able to use that expertise to determine whether this company is violating federal law.

Another example of constructive, selective federal intervention, concerns the unique insurance issues raised by supplemental medicare insurance. Because of the gaps in Medicare, the nation's elderly have turned to private health insurance; more than 50% have at least one policy. The annual premium volume of this Medicare supplement or "Medigap" business is unknown, but it has been estimated at $1 billion. In addition, large numbers of policies are sold to the elderly which are not true Medicare supplements, such as hospital indemnity plans and dread disease policies.

The lack of consumer information in the Medicare supplement market is so great that it is almost impossible to make rational purchase decisions. Very few people understand the complexities of Medicare and its gaps. Private insurance policies

often include a variety of options, making it difficult for buyers to comparison-shop. As a result, supplemental policies often do not compete on price and offer only a low rate of return.

In an effort to get complete protection, many people over 65 buy two or more policies which overlap. An estimated 23% of those who do buy private health insurance have some unnecessary duplication in coverage. Unscrupulous agents selling door-to-door or mail order advertisements often mislead or frighten them into "loading up" on two or more policies or replacing policies each year, a practice known as "twisting." When they file claims, many of them find that the coverage they thought would fill all the gaps in Medicare falls far short of their expectations. Most supplemental policies will not pay for pre-existing conditions or the major gaps in Medicare, such as nursing home care, excess provider charges and prescription drugs.

Several states have experimented with different regulatory solutions. And although since 1980, the federal Department of Health & Human Services has been authorized to administer a "voluntary certification program" under which companies that meet minimum standards may obtain a "federal seal of approval" for their Medigap policies, not one company has yet to seek certification. Massive consumer confusion about supplemental health insurance remains. A uniform system of disclosure, particularly about policy options and gaps in coverage, is essential.

Investigations of alleged deceptive conduct, mandating clear presale information that consumers can use to make informed decisions, establishing a uniform federal system of standardization and disclosures on supplemental health insurance—these are modest suggestions for a limited federal role in the insurance industry.

Insofar as the McCarran-Ferguson Act shields so basic an industry from national standards of fair dealing and informed competition, it remains a symbol of the political power of the insurance industry, not reasoned public policy.

Chairman RODINO. Thank you very much.

Commissioner, referring to the fact that your experience on the Commission has shown that the industry has been reluctant to disclose, is it your opinion that disclosure would be helpful in producing a more competitive atmosphere, or do you want disclosure for the sake of disclosure?

Commissioner PERTSCHUK. Certainly it's the former, Mr. Chairman. I recognize—and I hardly pose as an expert on insurance policies—that there are tradeoffs of values in information, that there are reasons for investing in life insurance policies other than their investment value. But the conclusions of our Commission study—and the work that was done went on for 7 or 8 years—was that there were vital pieces of information specifically related to the rate of return which would enable consumers to make the determination that a life insurance policy offered to them, as opposed to alternative choices for investment, would or would not be a good investment policy for them, and that's a crucial piece of information which they now don't have.

Chairman RODINO. Andrew Tobias, a witness who appeared before us last month, was not an economist, did not profess to be one, nor did he profess to be an expert on insurance; he was an author. He had however, studied the insurance industry for a long period of time. Mr. Tobias suggested that life insurance probably offered one of the lowest rates of return.

During the course of your study, was there any indication that this might be the case? I think that there was some other statistic in the FTC's report on life insurance that suggested the rate of return was 1.3 percent. That's a pretty low rate of return.

Do you think that, if this fact were known, individuals who invest in insurance would do so if there might be some other means of investment that could secure them as well and give them

a greater rate? We're talking about investment for moneymaking purposes as well as securing a risk.

Commissioner PERTSCHUK. Well, the fact of the matter is that a number of insurance companies sell products which have a better rate of return than that broad average—which was a figure which described the average rate of return, as I recall it, of all the policies then held by policyholders in the country. There are better rates of return offered. There are also many policies which offer, in effect, a negative rate of return, and that is precisely the thrust of what the Commission study showed, that consumers have to be able to benefit from knowing the nature of the rate of return they are going to get, even if it's a relatively crude comparative tool.

Chairman RODINO. Well, do you think that that's still a problem?

Commissioner PERTSCHUK. Yes, Mr. Chairman. As I indicated, the Commission also proposed a model State disclosure law. We were not trying to regulate. No State has adopted the model State regulation which requires disclosure of that rate of return.

Chairman RODINO. Do you believe that there are a substantial body of consumers that today are unknowingly investing their money in old policies with low rates of return?

Commissioner PERTSCHUK. Yes. I believe that still to be the case.

Chairman RODINO. To what extent is the possibility of withdrawal and replacement a factor in the competitive marketplace?

Commissioner PERTSCHUK. Well, it's hard for me to testify directly on that. Perhaps some of your panelists following who are more expert will know, but clearly, part of the fear generated within the industry by the Commission's report was just the threat that the report and the publicity surrounding the report would cause policyholders to look hard at those policies.

I referred in my prepared statement to then-Chairman Cannon of the Commerce Committee, who took me aside after the hearing and said: "I found your report very interesting. I am reviewing my policies to see whether I should turn them in."

Chairman RODINO. Some people look at the FTC and almost seem to suggest that there shouldn't be an FTC.

And there are some who oppose restoring FTC jurisdiction over the insurance industry who argue that it might bring the FTC into the ratemaking process. Does the FTC currently approve rates in any other industry?

Commissioner PERTSCHUK. No, Mr. Chairman.

Chairman RODINO. Let me ask, are you personally sympathetic to the idea of prior Federal Government approval of rates?

Commissioner PERTSCHUK. I think that it would be a serious mistake for the Federal Government and certainly for the Federal Trade Commission to get anywhere near the rate-setting process.

Chairman RODINO. So as a strong proponent of disclosure, nonetheless you're not suggesting that the FTC get into this area?

Commissioner PERTSCHUK. Absolutely not, Mr. Chairman.

Chairman RODINO. Could you characterize what has happened to the consuming public because of the failure of the insurance companies to provide them with the kind of information that we're now talking about?

Commissioner PERTSCHUK. Yes. I think that there is a failure of the information marketplace, and we're not talking about evil on

the part of the insurance industry. It is simply not in the interest of the sellers of most whole life policies to present to the consumer a clear, comparative ranking of whole life insurance, and most whole life insurance policies, as opposed to alternative policies.

You know, one of the arguments that the industry makes is that life insurance is more than just an investment, and that therefore providing this kind of information would confuse consumers. Well, there is nothing in any of these proposals to say that once the consumer has before him accurate comparative information on the relative value of whole life as an investment that the agent can't say to him, as a consumer, "Look, this is not as good an investment as others, but life insurance has other benefits, and you ought to consider them."

That's the way the marketplace should work. Then the consumer can make his decision, not in ignorance, but with full information.

Chairman RODINO. One final question: Recognizing the fact that there is a vast consuming public out there—it includes minorities, elderly people, people with stable and limited income derived from pensions and whatnot—do you think that the insurance industry's practices result in a prejudice to those people who are hard put at this time? Without suggesting that they are being victimized, as I have read in some reports, do you think the industry fails to provide them with the necessary kind of information to make a more informed judgment as to what alternative would be in their own best interests?

Commissioner PERTSCHUK. I think so. I don't think that disclosure alone would cure some of the problems of exploitation.

For example, in the area of so-called industrial life insurance policies. Those are policies sold to the lowest income consumers, traditionally on a door-to-door basis, which many of the major insurance companies have abandoned. There is evidence that low-income consumers are terribly exploited by those policies. They are a dreadful investment.

So more than life insurance cost disclosure is needed in some of the areas, but certainly, disclosure is an important first step.

Chairman RODINO. Why do you believe the insurance companies are reluctant to make this kind of disclosure? Is it a cost factor? Is the cost so prohibitive that it would probably have a terrible effect on the cost of insurance itself?

Commissioner PERTSCHUK. I think that consumer confusion is in the best economic interests of the life insurance industry as it is now structured; that they would not benefit from a clearer consumer understanding that other investment alternatives available to consumers would provide a better investment return. And therefore, I think they have a stake in preserving the status quo, which is confusion.

Mr. RODINO. Thank you very much Commissioner.

Mr. Fish.

Mr. FISH. Thank you, Mr. Chairman.

Commissioner, on page 5 of your prepared statement, you refer to an amendment to the Federal Trade Commission Act adopted by the Congress in 1980. I just don't want the record to leave an inference that by that amendment Congress changed the rules of the game. Because, as I understand it, the McCarran-Ferguson Act

states the FTC Act is not applicable to the business of insurance, if that business is regulated by State law. And wasn't the Senate Commerce Committee, and subsequently the Congress as a whole, really saying that the plain language of the McCarran-Ferguson Act meant what it said: that no portion of the Federal Trade Commission Act applied to insurance, because insurance is regulated by State law?

When I look at the legislative history of this amendment, it seems to say that Congress saw no distinction in McCarran-Ferguson between the enforcement functions of the FTC and the informational investigative functions. This was not a new restriction imposed by the Congress, but a reinforcement of the 1945 legislation.

Commissioner PERTSCHUK. Mr. Fish, there are two answers to that, I think. One is that at the time of that hearing briefs were submitted both by the Commission and by a number of the insurance companies, particularly Aetna, which argued different interpretations of the McCarran-Ferguson Act.

[FTC brief in appendix at p. 613.]

It was the Commission's position—and that was the position which had been upheld by several oversight committees, including the House Commerce Oversight Committee in 1978—that the Commission was exercising proper authority and responsibility in studying insurance. It is quite correct that McCarran-Ferguson prohibits the Commission from the exercise of its section 5 power, but, as I am sure you know, the Commission inherited in 1915 the authority of the old Bureau of Corporations in the Department of Commerce.

The Bureau of Corporations' responsibility was to do studies for the Congress on all manner of industrial organizational questions which were not subject to regulation, and it was under that general study authority that the Commission conducted its insurance study.

The only other point I had made in my testimony, Mr. Fish, is that it certainly was appropriate for members of the committee to review the legislative history and to conclude that the Commission did not have the authority. We disagreed, but that was certainly an appropriate decision.

The argument that we made at the time, and I would make here, is that the real question before the committee, because it was dealing with the Commission's authorization bill, was whether or not the Commission should have that authority; whether it was in the public interest to have the Federal Trade Commission studying insurance. If the Commission had been violating its mandate inadvertently, because there was no evidence that the Commission was deliberately exceeding its mandate, then that could have been corrected by the committee.

Instead, the whole focus of the question was, was the past intention of Congress this, or the past intention of Congress that? But with all due respect, it seemed to me the question in an authorization bill is what should the Commission's authority be. And no one addressed that question.

Mr. FISH. Well, it seems to me, Commissioner, that looking at the statute itself, when it simply says that the Sherman Act and the Clayton Act and the Act of September 26, 1914, known as the Fed-

eral Trade Commission Act as amended shall not be applicable to the business of insurance—you know, I mean, that's pretty straightforward. It doesn't say that the Federal Trade Commission Act shall not be applicable except for section 6, or except for anything else; it is just a flat prohibition.

But let's go on here. I actually think that if the Senate at that time saw fit to agree with the Commission that you should have this authority, well, then, they should have amended McCarran-Ferguson.

At this point, Mr. Chairman, I ask unanimous consent to insert in the record pages 13 and 14 of that Senate Report 96-500.

Chairman RODINO. Without objection.

[Material in the appendix at p. 641.]

Mr. FISH. Mr. Commissioner, could you amplify what you mean by a "substantial Federal role in monitoring and policing the insurance industry," that's page 1 of your prepared statement.

Commissioner PERTSCHUK. I——

Mr. FISH. Let me finish. Are you suggesting the creation of a new Federal regulatory agency concerning insurance? And if not, are you suggesting that an existing agency should perform this function?

Commissioner PERTSCHUK. Well, neither. I am not proposing that the Federal Government enter wholesale into the regulation of insurance. The specific suggestion I have made, which is that—at least in the area of life insurance cost disclosure, which is really the only area that I came here this morning to testify on, because I have not, frankly, reviewed other areas relating to McCarran-Ferguson—in the area of life insurance cost disclosure and the consumer protection area, that I see no justification for continuing the exemption against the Federal Trade Commission's performing its existing function, that is, the policing of deceptive practices.

In addition to that, I do suggest that Congress might want to consider granting some agency—and that might be the Federal Trade Commission—the authority to promulgate a life insurance cost disclosure rule, but that's the limit of the suggestions that I have made this morning. I do not propose that the Federal Government take over the rate regulation functions of the States, by no means.

Mr. FISH. Well, staying with the life insurance cost disclosure——

Commissioner PERTSCHUK. Yes, sir.

Mr. FISH.—area. You referred to a new model State life insurance cost disclosure law——

Commissioner PERTSCHUK. Yes, sir.

Mr. FISH.—in your testimony, developed by the Commission.

Could you tell the Subcommittee whether or not this proposal has been acted upon in the States, and generally what its current status is?

Commissioner PERTSCHUK. It has not been adopted by any of the States. In 1979, I believe, a committee, a task force of the National Association of Insurance Commissioners, reviewing the same material that the Commission was reviewing, came to most of the same conclusions that the Commission had come to, specifically the conclusion that there should be a disclosure of the rate of return, and proposed to the National Association of Insurance Commissioners

the adoption of a model law very similar to that proposed by the Commission. But that proposal by the task force of the NAIC was turned down by the NAIC and no further action has been taken in furtherance of that.

Mr. FISH. Could you submit a copy of your new model State law to the committee?

Commissioner PERTSCHUK. Certainly, it was a part of the Commission's report, which we certainly will make certain that all members of the committee have.

[Report on file with the subcommittee.]

Chairman FISH. Right. Thank you.

Mr. RODINO. Mr. Hyde.

Mr. HYDE. Thank you, Mr. Chairman. This may lose me some friends in the insurance industry, and I hope not, but I think an industry that has the enormous financial impact on the lives of most people does deserve a study, but—that is the difficulty.

As in so many things, I have an impression—and it's just an impression—that if the FTC undertook the study it would be like hatchet-wielding members of the WCTU approaching the nearest saloon in the early days of this century—not today, God knows. They're lovely people, and wouldn't——

[Laughter.]

Mr. HYDE [continuing]. Think of that. But——

Commissioner PERTSCHUK. I was going to say, Mr. Hyde, I clearly don't represent the majority of the Commission anymore, and so——

Mr. HYDE. I know that. I know that. But the problem is there is a certain zealousness that animates—and I am not saying it's misplaced, but it's there—the FTC staff, and I am just not too sure that whatever they would come up with would be helpful, but I do agree that the fragmentation of the industry in terms of supervision is an asset to the industry, and not necessarily to the consumers.

It is an enormously important institution and, as all enormously important institutions, it ought to be looked at and it ought to be looked at objectively and fairly and dispassionately; and then some legislative recommendations made.

Perhaps by a commission. That seems to be the vogue these days, but if properly chaired and staffed, the report would have credibility and would have balance and something that we could act on. But I agree.

I know a little bit about how it's operated in the States and I know the insurance companies like to have the commissioner one of theirs or as close to theirs as is possible. There's nothing wrong with that.

If I were in the insurance business, I'd like that, too. But we are protecting the public interest or we ought to protect the public interest and we ought to try to get a balanced assessment of their practices, their profits, their problems so that everybody would benefit.

So I'm not hostile to what you're suggesting. I just don't know how it could be effectively done. I don't think the FTC is the agency to do it and I just say that because of the political implica-

tions and the thrust of the FTC, which is to find something to justify what they've done.

That's really all I have to say. I think the law is clear that the FTC Act is inapplicable and until that law is changed, wrong as it may be or correct as it may be, it's still the law. Before the FTC plunges in I think there ought to be some statutory warrant for doing so; and I don't think that's there now under the Act.

That's really all I have to say and I think you have made a contribution to an enormously important problem. Thank you.

Chairman RODINO. Thank you very much, Commissioner, for your appearance and your testimony.

Mr. HYDE. Thank you, Mr. Chairman.

Chairman RODINO. Now our next witnesses will consist of a panel: Mr. Herb Jaffe of the Newark Star Ledger, Prof. Joseph Belth, and Prof. Buford Brinlee.

I want to welcome you here. I especially am pleased to welcome one of my good friends and a man from whom I have been learning over the years because of his intense interest in this problem. He has contributed greatly, I think, to informing the public about the need to know in this area. He is a reporter and comes here on his own representing himself because he has a concern about this problem. I'm referring to my good friend, Mr. Herb Jaffe. Herb, you're first to go. We're going to suggest that each of you summarize whatever you have to say.

TESTIMONY OF HERB JAFFE, REPORTER, NEWARK STAR LEDGER; DR. JOSEPH BELTH, PROFESSOR OF INSURANCE, INDIANA UNIVERSITY; AND DR. BUFORD BRINLEE, ASSISTANT PROFESSOR, POLITICAL SCIENCE AND PUBLIC ADMINISTRATION, UNIVERSITY OF NORTH FLORIDA

Mr. JAFFE. As you mentioned, Mr. Chairman, the views expressed in this statement are my own and are in no way intended to identify with those of my newspaper.

Insurance is unlike any other product sold on the open market. There is almost no information made available to the public which would allow consumers an opportunity to compare the same lines of insurance that are sold by companies which ostensibly compete.

Insurance companies do not advertise either their rates or the advantages for consumers of their respective policies in an atmosphere of product competition. Rather, theirs is an institutional form of advertising which relies largely on claims to the consumer relating to the company's history of reliability.

Insurance advertising for the general public deals largely with a theme of how good the company is instead of discussing the benefits in terms of cost and quality of one company's policy over the rest of the field. Even insurers who suffer financial difficulty will concentrate on advertising their reliability.

Unfortunately, the public has no way of knowing what a company's financial position or degree of responsibility might be under routine conditions. State insurance departments are entrusted with examining financial statements and other information that must be filed periodically by insurers.

However, most State insurance departments, if not all, do not possess sufficient staff or expertise and personnel to fully evaluate the financial condition of the hundreds of companies which they license. Another danger exists in the policies approved for sale by State insurance departments.

A genuine lack of sufficient qualified investigators often makes it impossible to guarantee that the policy approved by the regulator for sale is necessarily the same product, word for word and inclusive of all provisions, that is being sold to thousands of the company's policyholders.

It is almost universally acknowledged that insurance policy language is so awkward and complex that the average policyholder automatically relies on the State regulators to guarantee that the provisions in a policy are in accordance with State approval rather than depend on their own ability to comprehend the contents.

My home State, New Jersey, is a high risk auto insurance territory whose drivers already pay the highest premiums in the country. The most recent nationwide rate figures for the year 1982 show that the average New Jersey auto insurance policy cost $455.80, which was $68.31 more than the premiums paid by motorists in Massachusetts, the second highest State. That's according to the annual figures compiled by the A.M. Best Co. This was compared to a national average premium for all States of $298.30 in 1[illegible].

From my own findings, which became the basis of a seven-part series of articles which I wrote on auto insurance last December for the Star Ledger, I discovered that the State's auto premium structure will probably remain the highest in the country indefinitely because of a hybrid auto coverage. New Jersey presently offers the best of all worlds: unlimited no-fault payments for hospital and medical needs in addition to the choice of a dollar threshold so low that injured parties can sue with relative ease.

This was the compromise that the State legislators made last year to satisfy the trial bar rather than independently mandate the best possible policy at the lowest possible rates. Of particular significance in New Jersey is the fact that motorists are compelled to own auto insurance, but they do not have the freedom to choose the company or policy limits they might prefer.

In fact, the auto insurance market in New Jersey has been so constricted in recent years resulting from what the insurers commonly refer to as rate inadequacy that the companies have completly controlled the marketplace. In essence, the auto insurance policy being sold is not necessarily the choice of the consumer; but the consumer has become the choice of a highly selective auto insurance industry.

Such a climate further inhibits normal competitive factors. As a result, auto insurers in particular have adopted the position that there is no need to be competitive in such areas as cost of policy, quality of policy, speed and reliability of claim adjustment, claim settlement practices or any other factors which a consumer might weigh if given a choice in a truly competitive market.

Thank you very much for hearing me.

[The statement of Mr. Jaffe follows:]

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STATEMENT BY HERB JAFFE, INVESTIGATIVE AND SPECIAL ASSIGNMENT WRITER FOR THE STAR-LEDGER, NEWARK, NJ

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Even insurers who suffer financial difficulty will concentrate on advertising their reliability. Unfortunately, the public has no way of knowing what a company's financial position or degree of responsibility might be under routine conditions. State insurance departments are entrusted with examining financial statements and other information that must be filed periodically by insurers. However, most state insurance departments, if not all, do not possess sufficient staff or expertise in personnel to fully evaluate the financial condition of the hundreds of companies which they license.

Another danger exists in the policies approved for sale by state insurance departments. A genuine lack of sufficient qualified investigators often makes it impossible to guarantee that the policy approved by the regulator for sale is necessarily the same product, word for word and inclusive of all provisions, that is being sold to thousands of the company's policyholders. It is almost universally acknowledged that insurance policy language is so awkward and complex that the average policyholder automatically relies on the state regulators to guarantee that the provisions in a policy are in accordance with state approval, rather than depend on their own ability to comprehend the contents.

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As a result, auto insurers in particular have adopted the position that there is no need to be competitive in such areas as cost of policy, quality of policy, speed and reliability of claim adjustment, claim settlement practices, or any other factors which a consumer might weigh if given a choice in a truly competitive market.

Thank you for hearing me.

Chairman RODINO. Thank you. Professor Belth.

Dr. BELTH. Mr. Chairman, I am Joseph M. Belth, professor of insurance, school of business, Indiana University, Bloomington. I am editor of the Insurance Forum, a four-page monthly periodical. I

am author of "Life Insurance: A Consumers' Handbook," and various other books and articles on life insurance.

I am a past president of the American Risk Insurance Association, an organization of insurance professors and others interested in insurance education. I am not being compensated for the preparation of this statement. The views expressed in the statement are my own and not necessarily those of any institution, organization, or other individual.

I appreciate the invitation to present my views at this hearing.

Mr. Chairman, in the first section of my statement I express my views on several life insurance topics so you will be aware of any attitudes that might influence my approach to the subject matter of this hearing. To conserve time, I will not read that section.

In the second section of my statement I discuss the absence of requirements for disclosure of important information to life insurance consumers.

The prospective buyer of a life insurance policy is not provided with reliable information about the price of the protection component. When the policy includes a savings component, the prospective buyer is not provided with reliable rate of return information.

The owner of an existing life insurance policy is not provided with reliable information about the price of the protection component. When the policy includes a savings component, the policyowner is not provided with reliable rate of return information.

Long before any disclosure requirements were adopted for prospective buyers, the life insurance industry persuaded the National Association of Insurance Commissioners to recommend and many States to adopt requirements for disclosure in situations where the replacement of an existing policy is proposed. Such requirements do not provide for rigorous disclosure to policyowners.

Rather, the requirements are merely obstacles for agents and companies in the replacement business.

In recent years, several State insurance departments have abandoned even these meager requirements because the information usually is inaccurate and the information is of little or no value to the policyowner even when accurate.

In 1968 the late Senator Philip Hart, in a speech to a life insurance group, threatened truth-in-life-insurance legislation unless the industry began providing reliable price information to life insurance consumers. The speech was a major turning point because until that time neither the life insurance industry nor the State insurance departments had acknowledged the existence of a problem.

In 1973, the NAIC developed a model life insurance disclosure regulation. In 1976, the NAIC developed a revised disclosure regulation.

The life insurance industry has supported the NAIC approach and more than half the States have adopted a life insurance disclosure regulation. The NAIC system, however, constitutes pseudo disclosure.

Among the shortcomings of the system are its failure to require disclosure of: One, price information that would disclose the magnitude of the front-end load; two, price information beyond 20 policy years; three, information about the rate of return on the savings

component; and four, information on an annual basis to the owners of existing policies.

In 1979, a staff report published by the Federal Trade Commission recommended that the NAIC system be modified to provide for disclosure of information about the rate of return on the savings component. The life insurance industry successfully opposed the recommendation and also persuaded Congress to bar the FTC from further investigations of insurance unless requested by one of the Commerce committees.

In 1980, an NAIC committee strongly criticized the NAIC disclosure system. The life insurance industry successfully opposed the committee's efforts to develop a better system.

Today, neither the prospective buyer of life insurance nor the owner of an existing policy is provided with reliable information about the price of the protection component or the rate of return on the savings component.

Mr. Chairman, in the next section of my statement I discuss several reasons why the life insurance industry opposes rigorous disclosure for prospective buyers of life insurance and for owners of existing policies. To conserve time, I will read only portions of that section.

First, some companies charge much higher prices than other companies for essentially the same life insurance coverage. Second, deceptive sales practices are widely used and deeply imbedded in life insurance marketing.

Third, some companies engage in manipulation by charging low prices for the protection in some policies and high prices for the protection in other policies. For example, a company may advertise a low-priced policy on which small sales commissions are paid, but also offer a high-priced policy on which large commissions are paid.

Under these circumstances, agents acting in a professional manner sell the low-priced policy, but other agents sell the high-priced policy for the large commissions.

Fourth, some companies engage in manipulation by charging low prices for the protection in policies offered to new buyers and high prices for the protection in existing policies. For example, it is not unusual to find high prices being charged for the protection in policies that have been in effect for many years; but the policyowner has no way of knowing about it because reliable price information is not provided to the owners of existing policies.

Fifth, some companies engage in manipulation by charging competitive prices for the protection in the early policy years and noncompetitive prices for the protection in the later policy years. For example, it is not unusual to find sharp price increases beginning in policy year 21 because often no price information, reliable or otherwise, is provided beyond the first 20 policy years.

Sixth, many companies do not want their agents to have the information. Life insurance companies do not sell life insurance. Agents sell life insurance.

Life insurance companies are in the business of hiring, training and trying to keep good agents. If agents were provided with rigorous disclosure, companies charging high prices or engaging in manipulation would find it difficult to keep good agents.

Mr. Chairman, in the next section of my statement I describe briefly the elements of a system of rigorous disclosure for life insurance consumers. To conserve time, I will not read that section.

In conclusion, buyers of new life insurance and owners of existing policies are not provided with the information they need to make intelligent decisions in their own interests. For example, life insurance consumers are not provided with reliable information about the price of the protection component. When the policy includes a savings component, they are not provided with reliable rate of return information.

Developments during the past 20 years suggest that rigorous disclosure requirements will never be mandated by the State insurance departments. Industry opposition to such requirements is too strong. Nor do recent developments at the Federal level offer any hope for consumers.

Two years ago I concluded that rigorous disclosure requirements for life insurance will never be implemented and that consumers will have to obtain the important information for themselves. Since then I have written several articles designed to help consumers in that endeavor and I intend to continue such writing.

Thank you again for inviting me to present my views at this hearing.

[The statement of Professor Belth follows:]

STATEMENT OF JOSEPH M. BELTH

I am Joseph M. Belth, professor of insurance, School of Business, Indiana University (Bloomington). I am editor of *The Insurance Forum*, a four-page monthly periodical. I am author of *Life Insurance: A Consumer's Handbook* and various other books and articles on life insurance. I am a past president of the American Risk and Insurance Association, an organization of insurance professors and others interested in insurance education. I am not being compensated for the preparation of this statement. The views expressed in the statement are my own and not necessarily those of any institution, organization, or other individual. I appreciate the invitation to present my views at this hearing.

MY VIEWS ON LIFE INSURANCE

At the outset, I will express my views on several life insurance topics so you will be aware of any attitudes that might influence my approach to the subject matter of this hearing.

Life insurance serves two social purposes: the death protection function, through which financial protection is provided to the survivors of persons who die prematurely, and the financial intermediation function, through which the savings of individuals and businesses are channeled into capital investment. Both functions are important, but death protection is the unique province of the life insurance industry.

The purpose of life insurance is to make up the difference between the requirements of a person's dependents upon that person's death and the resources available upon that person's death. There is no substitute for life insurance, because there is no other way to make up the difference.

Life insurance is sold rather than bought, and there is no substitute for the face-to-face meeting between the life insurance agent and the prospective buyer. The most important function of the agent is to persuade the prospective buyer not to procrastinate in meeting his or her life insurance needs.

Both term insurance and cash-value insurance are useful types of life insurance. The choice between them depends upon the circumstances and objectives of the buyer.

It is appropriate for the policyowner to consider cash-value life insurance as consisting of a protection component and a savings component. The savings component is the cash value, which is an asset of the policyowner. The protection component is the excess of the amount payable on death over the cash value.

There is an urgent need for rigorous disclosure to life insurance consumers. Two of the most important elements of a system of rigorous disclosure are (1) information about the price of the protection component and (2) information about the rate of return on the savings component.

Deceptive sales practices are widespread in the life insurance business. Indeed, such practices are a national scandal.

Sometimes replacement of an existing life insurance policy is justified, sometimes replacement is not justified, and sometimes the situation is a toss-up. Replacement should be considered only in situations where it is justified. Generalizations about replacement cannot be made; rather, each situation must be considered individually.

THE ABSENCE OF RIGOROUS DISCLOSURE

The marketplace for individual life insurance is characterized by an absence of requirements for disclosure of important information to consumers. The prospective buyer of a life insurance policy is not provided with reliable information about the price of the protection component. When the policy includes a savings component, the prospective buyer is not provided with reliable rate-of-return information. The owner of an existing life insurance policy is not provided with reliable information about the price of the protection component. When the policy includes a savings component, the policyowner is not provided with reliable rate-of-return information.

Long before any disclosure requirements were adopted for prospective buyers, the life insurance industry persuaded the National Association of Insurance Commissioners (NAIC) to recommend and many states to adopt requirements for disclosure in situations where the replacement of an existing policy is proposed. Such requirements do not provide for rigorous disclosure to policyowners; rather, the requirements are merely obstacles for agents and companies in the replacement business. In recent years, several state insurance departments have abandoned even these meager requirements, because the information usually is inaccurate, and the information is of little or no value to the policyowner even when accurate.

In 1968 the late Senator Philip A. Hart, in a speech to a life insurance industry group, threatened truth-in-life-insurance legislation unless the industry began providing reliable price information to life insurance consumers. The speech was a major turning point, because until that time neither the life insurance industry nor the state insurance departments had acknowledged the existence of a problem.

In 1973 the NAIC developed a model life insurance disclosure regulation. In 1976 the NAIC developed a revised disclosure regulation. The life insurance industry has supported the NAIC approach, and more than half the states have adopted a life insurance disclosure regulation. The NAIC system, however, constitutes pseudo disclosure. Among the shortcomings of the system are its failure to require disclosure of (1) price information that would disclose the magnitude of the front-end load, (2) price information beyond 20 policy years, (3) information about the rate of return on the savings component, and (4) information on an annual basis to the owners of existing policies.

In 1979 a staff report published by the Federal Trade Commission recommended that the NAIC system be modified to provide for disclosure of information about the rate of return on the savings component. The life insurance industry successfully opposed the recommendation, and also persuaded Congress to bar the FTC from further investigations of insurance unless requested by one of the commerce committees.

In 1980 an NAIC committee strongly criticized the NAIC disclosure system. The life insurance industry successfully opposed the committee's efforts to develop a better system. Today neither the prospective buyer of life insurance industry nor the owner of an existing policy is provided with reliable information about the price of the protection component or the rate of return on the savings component.

INDUSTRY OPPOSITION TO RIGOROUS DISCLOSURE

As mentioned earlier, the life insurance industry has supported the disclosure system developed by the NAIC, and has opposed efforts to improve the system. There are several reasons why the industry opposes rigorous disclosure for prospective buyers of life insurance and for owners of existing policies.

First, some companies charge much higher prices than other companies for essentially the same life insurance coverage. Stated another way, some companies provide much lower rates of return on the savings component than other companies. It is not unusual, for example, to find a company charging $30 per $1,000 of protection in a particular policy year, and to find another company under similar circumstances charging $3 per $1,000 of protection. Stated another way, it is not unusual

to find a company providing less than a 2 percent rate of return on the savings component, and to find another company under similar circumstances providing more than an 8 percent rate of return.

Second, deceptive sales practices are widely used and deeply imbedded in life insurance marketing. For example, it is commonplace for sales material to suggest, through improper handling of the interest factor in cash-value life insurance, that the price of the protection component in most policy years is negative.

Third, some companies engage in manipulation by charging low prices for the protection in some policies and high prices for the protection in other policies. For example, a company may advertise a low-priced policy on which small sales commissions are paid, but also offer a high-priced policy on which large commissions are paid. Under these circumstances, agents acting in a professional manner sell the low-priced policy, but other agents sell the high-priced policy for the large commissions.

Fourth, some companies engage in manipulation by charging low prices for the protection in policies offered to new buyers and high prices for the protection in existing policies. For example, it is not unusual to find high prices being charged for the protection in policies that have been in effect for many years, but the policyowner has no way of knowing about it because reliable price information is not provided to the owners of existing policies.

Fifth, some companies engage in manipulation by charging competitive prices for the protection in the early policy years and noncompetitive prices for the protection in the later policy years. For example, it is not unusual to find sharp price increases beginning in policy year 21, because often no price information (reliable or otherwise) is provided beyond the first 20 policy years.

Sixth, many companies do not want their agents to have the information. Life insurance companies do not sell life insurance. Agents sell life insurance. Life insurance companies are in the business of hiring, training, and trying to keep good agents. If agents were provided with rigorous disclosure, companies charging high prices or engaging in manipulation would find it difficult to keep good agents.

ELEMENTS OF A SYSTEM OF RIGOROUS DISCLOSURE

As indicated earlier, a system of rigorous disclosure for life insurance consumers is urgently needed. The elements of such a system may be described briefly as follows:

(1) For buyers of new policies (at the point of sale):

(a) Certain raw policy data for each year for 30 years or to age 75, whichever is the longer period, or to the scheduled termination of the policy, if sooner. Included for each year would be the annual premium, the amount payable on death, the amount payable on surrender, and the annual dividend based on the company's current dividend scale.

(b) Certain derived data for each year over the same period. Included for each year would be the amount of protection, the price per $1,000 of protection, and the rate of return on the savings component. These items would be based on formulas and assumptions prescribed by the agency charged with the administration of the disclosure system.

(c) Certain summary data over the same period. Included here would be a breakdown of the policy into its major components, average annual rates of return on the savings component for various durations, and the cost of paying premiums other than annually. These items would be based on formulas and assumptions prescribed by the agency charged with the administration of the disclosure system.

(2) For owners of existing policies (annually after the sale):

(a) For the past year and for the forthcoming year, the price per $1,000 of protection and the rate of return on the savings component. These items would be based on formulas and assumptions prescribed by the agency charged with the administration of the disclosure system.

(b) Certain other important information about the policy, as prescribed by the agency charged with the administration of the disclosure system.

Further details concerning the elements of a system of rigorous disclosure are available elsewhere. For example, such a system was described in testimony I presented on May 24, 1979, before what was then the Subcommittee on Antitrust, Monopoly and Business Rights of the Senate Committee on the Judiciary.

CONCLUSION

Buyers of new life insurance and owners of existing policies are not provided with the information they need to make intelligent decisions in their own interests. For

example, life insurance consumers are not provided with reliable information about the price of the protection component. When the policy includes a savings component, they are not provided with reliable rate-of-return information.

Developments during the past 20 years suggest that rigorous disclosure requirements will never be mandated by the state insurance departments. Industry opposition to such requirements is too strong. Nor do recent developments at the federal level offer any hope for consumers.

Two years ago I concluded that rigorous disclosure requirements for life insurance will never be implemented, and that consumers will have to obtain the important information for themselves. Since then, I have written several articles designed to help consumers in that endeavor, and I intend to continue such writing.

Thank you again for inviting me to present my views at this hearing.

Chairman RODINO. Thank you very much, Professor. Professor Brinlee.

Dr. BRINLEE. Good morning, Mr. Chairman and members of the subcommittee. My name is Buford L. Brinlee. I'm an Assistant Professor of Political Science and Public Administration at the University of North Florida.

One of my research interests has been decisionmaking in regulated environments. I'm also the president of In-Quest, Inc., a Florida corporation, which developed a computerized information service for automobile insurance rates in the State of Texas.

While on academic leave in the fall of 1982, I implemented this consumer service in Dallas, TX, which identified specific companies and the rates they could charge for the type and level of coverage requested by the consumer. To my knowledge, we are the only company which has ever attempted to provide such information directly to clients and without any relationship to the industry.

I appreciate the opportunity to discuss this experience with the subcommittee and the importance of consumer information in this State-regulated environment. Very little research has been addressed as to how individuals within this regulated environment actually make decisions and to what extent a market system truly exists at the point of purchase; that is, between the consumer and the company representative.

Based on our experience in Texas, the answer is that the market system model is seriously misidentified. Consumers do not have sufficient information, time, or power to make optimum choices.

These barriers are not only well recognized by the sellers, but frequently exploited to their advantage. Indeed, at almost every point of the exchange transaction the advantage accrues to the seller rather than the buyer.

Perhaps the easiest way to convey the problems confronting the consumer and their correspondingly beneficial attributes for the seller is to consider the problem in terms of the costs of information necessary for rational decisionmaking.

Confronted with large amounts of information and complex problem-solving requirements, individuals do not select the optimal choice, but rather the first one which meets their immediate level of satisfaction. In Herbert Simon's terminology, they "satisfice."

The problem in auto insurance is that for most consumers "satisficing" is getting any coverage at all. Sell me any policy you can in a short time because I want to drive my new car off the lot or I want to get covered by next week before my insurance runs out.

The structure of the Texas State-regulated system actually consisted of four different rates. The State established a standard rate.

However, companies filed deviated rates below and above the standard rate, and also there are county mutuals which were exempted from any rate regulation at all.

The fact that there could be four different levels of rates under this system was a major source of confusion to consumers and one which was purposely reinforced by many agents. It suggested that the rate they were quoted was the only one legally possible for the particular consumer and that further search in the marketplace of sellers was unnecessary; a marketplace where product lines are seldom differentiated, where there is an oversupply of sellers, and rates are seldom given over the phone.

One of the benefits of requiring the client to come into the office is that the buyer has already incurred a significant cost. At the same time, the agent is able to ask questions other than those listed on the application form which will be used in his own decisionmaking process to determine what company to select for the client.

There are actually three decisions in this purchasing process. The agent decides what companies might insure the applicant, theoretically using underwriting criteria; determines the product mix for the client—that is, the types and levels of coverage; and then calculates the prices.

In all three instances, however, it is the seller who controls the information and the decisionmaking process. In what is truly a unique market exchange, the seller determines the product and price at the same time, and the consumer lacks the information to determine if this is, indeed, the best product or price mix available. The uniqueness of the environment is that the agent acts as an extension of State authority aided by the veneer of legality afforded under a State-regulated system.

Our service worked in the following way. Consumers could call or come to the office. We collected information off of an application form. Our computer analyzed the data, provided a list of the companies and the specific prices that they would charge for each type and level of insurance. And the consumer, at this point, had to reenter the market system and find an agent to purchase that insurance.

We then asked the consumer to call us and tell us what was happening in their interaction; and, indeed, that is the major source of our data.

When we opened the consumer information service we actually had an opportunity to see how the decisionmaking system works. Among agents, the response was generally negative. Indeed, in the first 2 or 3 weeks, most calls were from agents and companies.

They wanted to know what insurance companies we actually represented or sold. They wanted to know what insurance companies had financed our service. They were angry over the publicizing of the various companies available and especially the prices that they could charge.

At the same time, several agents were very supportive. They felt that the service provided a much needed neutral source of information and it would help their profession, and indeed make it more difficult for questionable agents to continue improper business practices.

Among clients the response was generally favorable. The dilemma also was their concern that we were trying to sell insurance.

We found the information was used by many of our clients. We assume about 70 percent used it to purchase insurance, many saving literally hundreds of dollars.

Our consumers were what we called intelligent consumers. They also wanted other data. They wanted to know, for example, the service claims record of agents and companies and the solvency of companies.

When we look at the interaction between the buyer and the seller, we can see how information is hidden and confusing. We also recognize the importance of underwriting criteria.

Underwriting criteria determine not only the class in which someone may be placed—that is, do they have young drivers and so forth—but they are also used to determine what company they may choose to put this client into. Some of the underwriting criteria are closely related to questions of risk; others, however, seem questionable.

For example, there is redlining in auto insurance—that is, what ZIP Code you live in might be used—even within the same ratemaking territory. They ask questions if the individual was divorced, for example; if the individual smoked; if they drank; criteria of that nature.

In fact, no true exchange occurs between the buyer and the seller. That is, instead of having an offer, consideration and acceptance, the offer is contingent and two of three parts of this buying exchange take place only on the part of the buyer.

We can then summarize the seller's behavior with four simple concepts: The questions of commissions, creaming, capturing, and churning.

The commission structure is one that drives the seller to try to place a client into the highest price because he gets a higher rate of return in his commission. Creaming is the practice that an agent prefers to take only the least risky business—no young drivers, only those with new cars and so forth—and for these people he requires high levels of coverage, thus protecting his commission.

Capturing entails making it difficult to switch companies. That is, companies have a 60-day grace period when they can refuse or cancel a policy without a reason to a newly insured risk. At the same time, people are afraid to file claims. This is, indeed, a hidden tax to keep the coverage of their existing company.

Churning is the systematic creation of new opportunities to force people out into the market at higher prices. Under churning we would suggest the idea of a scarlet letter. If you have been cancelled, you are then kicked out into the marketplace. You carry a stigma with you as if you had a scarlet letter, some, indicator to any other company of the right to charge you higher prices.

The combination of structural and behavioral factors suggests that under the current State-regulated system in Texas consumers are systematically removed from any true participation in the market system. Market shares, concentration ratios, and the presence of many sellers and buyers aside, at the level of the actual transaction, consumers are poorly served.

Now, these observations have been based on the Texas experience. Many of these same problems appear in other States.

In my opinion, the Texas system reveals the benefits which accrue to an industry in a partially regulated environment. I say "partially" because the two major regulatory mechanisms, rate regulation and agent licensing, actually have little effect on the way the market operates between buyers and sellers.

This is an especially discouraging observation, given the quality of the Texas State Insurance Commission staff. In my dealings with that State agency, I found the staff to be not only extremely knowledgable, but very professional in their approach and concern for public interest.

The problem, then, is not one of intent, but reflects the relative imbalance between independent States, on the one hand, and one of the largest industries of the Nation on the other.

No other industry with the size and influence of insurance has successfully exempted itself from national scrutiny and responsibility. Indeed, the very protections afforded by the McCarran-Ferguson Act hinder the ability of public servants at the State level to get an accurate picture of how the industry operates.

The combination of State regulation on the one hand and exemption from Federal scrutiny on the other has resulted in leaving consumers little power in their relationship with the industry. Indicative of the relative powerlessness of individuals in the system is the fact that the most important element in the overall decisionmaking process, the underwriting rules, are exempt from both State and individual review.

Indeed, underwriting is the ultimate hidden hand of the marketplace which is controlled by the industry and one which ultimately must be dealt with.

In conclusion, Mr. Chairman and members of the subcommittee, I would like to suggest that the market system can be made to work. It requires more consumer information, protection from unfair business practices, greater freedom of sellers to develop price competition within the framework of reasonable profits, administrative reviews of unilateral company decisions, removals of barriers which inhibit the free movement of buyers among sellers, and much more attention to the coercive opportunities associated with the marketing of a product which is virtually required by law.

With the subcommittee's permission, I'd be happy to submit additional analytical information which might further clarify some of the issues I've mentioned this morning. I thank the subcommittee for the opportunity to appear.

[The statement of Professor Brinlee follows:]

PREPARED STATEMENT OF BUFORD L. BRINLEE

Mr. Chairman and members of the subcommittee. My name is Buford L. Brinlee. I am an Assistant Professor of Political Science and Public Administration at the University of North Florida. One of my research interests has been decision-making in regulated environments. I am also the President of In-Quest, Inc., a Florida corporation which developed a computerized information service for automobile insurance rates in the State of Texas. While on academic leave in the Fall of 1982, I implemented this customer service in Dallas, Texas, which identified specific companies and the rates they could charge for the type and level of coverage requested by the consumer. To my knowledge, we are the only company which has ever attempt-

ed to provide such objective information directly to clients and without any relationship to the industry. I appreciate the opportunity to discuss this experience with the subcommittee and the importance of consumer information to the individual in this state-regulated environment.

While most research has focused on the structural characteristics of the industry and the extent to which it reflects a market system, very little has been addressed as to how individuals within this regulated environment actually make decisions and to what extent a market system truly exists at the point of purchase, i.e. between the consumer and the company representative. Based on our limited experience in Texas, the answer is that the market system model is seriously misidentified. Consumers do not have sufficient information, time, or power to make optimum choices. These barriers are not only well recognized by the sellers, but frequently exploited to their advantage. Indeed, at almost every point of the exchange transaction, the advantage accrues to the seller rather than the buyer. Perhaps the easiest way to convey the problems confronting the consumer and their correspondingly beneficial attributes for the seller is to consider the problem in terms of the costs of information necessary for rational decision-making. Economists have long noted the costs associated with the information search and analysis process. Confronted with large amounts of information and complex problem-solving requirements, individuals do not select the optimum choice, but rather the first one which meets their immediate level of satisfaction. In Herbert Simon's terminology, they "satisfice."

This perspective is especially applicable in purchasing insurance. Obviously, there is no requirement that government guarantee that consumers make the optimum choice possible. At the same time, however, even within regulated environments, every attempt should be made to facilitate the availability of information and the ease of consumer decision-making. Ironically, consumer information difficulties begin with the very fact that rates are regulated, continue throughout the purchasing cycle and foster oligopolistic prices.

The rate making system in Texas is relatively straight-forward. The Texas Automobile Insurance Service Organization (TAISO) is the industry rating bureau. It submits information to the State Board of Insurance to justify rates based on auto, driver and geographic classifications. This data is reviewed by the state agency staff, hearings are held and the commission certifies the use of a set of tables from which "standard rates" are to be calculated.

Unfortunately, the concept of standard rates is frequently misunderstood. Two factors obscure the price variations actually facing consumers. The first entails the practice of companies to file deviations from this standard rate. These deviations may be both above and below the standard rate, and are also approved by the state commission. Our research found 121 companies filed deviated rates, ranging from 33% below to 150% above the standard rate.

A second source of confusion to Texas consumers is the fact that approximately thirty companies in the state were not rate regulated, but rather had been exempted from this requirement under a grandfather clause included in the original 1927 legislation. These "county mutuals" were generally the most expensive and existed to provide insurance to the most difficult clients who other insurers would refuse to cover.

The structure of this state-regulated system actually consisted of four different levels of insurance prices: minus deviations from the standard rate, the standard rate, positive deviations from the standard rate, and county mutuals. The state also provided an assigned risk plan which, in some cases, was actually less expensive than county mutual rates. The computerized system only included state regulated companies.

The fact that there could be four different levels of rates under this system was a major source of confusion to consumers, and one which was purposely reinforced by many agents. It suggested that the rate they were quoted was the only one legally possible for the particular consumer, and that further search in the market place of sellers was unnecessary.

What appears at first glance to be a major strength of the market system, a large number of sellers (there were over 22 pages of agents listed in the Dallas Yellow Pages) actually serves as a deterrent to the search process. With the exception of direct writers and a few independent agents, few sellers actually listed the companies they represented. While some ads note the "lowest prices available" such claims are not identified with any particular company. The buyer thus enters the purchasing relationship with limited information on the products actually available from the seller. The cost of information search is further exacerbated by the fact

that few agents are willing to quote rates over the phone. Here is one product where, at the local level, your fingers cannot do the walking.

One of the benefits of having the client come into the office is that the buyer has already incurred a significant cost. At the same time, the agent is able to ask other questions than those listed on the application form which will be used in his own decision making process to determine what company to select for the client. There are actually three decisions in this process. The agent decides what companies might insure the applicant (theoretically using underwriting criteria), determines the product mix for the client (types and levels of coverage), and calculates the rates. In all three instances, however, it is the seller who controls the information and the decision-making process.

In what is truly a unique "market" exchange, the seller determines the product and price at the same time, and the consumer lacks the information to determine if this is indeed the best product/price mix available. The uniqueness of the environment is that the agent acts as an extension of state authority, aided by the veneer of legality afforded under a state regulated system.

Assuming that the client wants to do comparative shopping, this time-consuming process needs to be repeated. At this point, however, other features associated with state regulation actually serve as barriers to further search. Agents may assert that since the state regulates rates, the prices will be the same elsewhere. The fact that the same application form is mandated by state law and the same insurance policy is also provided appears to further support this contention. The regulated environment can thus be used to deter market behavior on the part of the buyer.

THE EFFECTS OF CONSUMER INFORMATION

The computerized information service was designed to limit the costs of the information search for consumers of automobile insurance, and provide them sufficient data to help them make more rational purchasing decisions. For a nominal charge ($15 for one car, $20 for two or more) the firm analyzed data provided by the consumer to calculate the rates companies had on file with the state regulatory commission. For each type and level of coverage requested, the computer program calculated the state standard rate, and identified the three lowest priced companies or listed prices for any company requested. A print-out of this information was provided directly to the consumer (Attachment A). Since most of the lowest priced companies were subsidiaries of larger holding companies, their parent firm was also identified so that the client would know what companies to contact and which insurance company rates to request. We also asked clients to call and tell us the results of their search.

This service provided significant information as to 1) how the industry would respond to consumer information identifying companies and prices, 2) the ability of consumers to bargain for better prices, and 3) the behaviors of market place which might explain oligopolistic pricing practices.

The industry's response to our radio and newspaper advertising program was immediate and generally negative. Most of our early calls were from agents who wanted to know what insurance we were selling and/or what insurance company had funded our project. The notion that consumers should have the right to request a specific company was seen as a threat, especially to the extent that it required agents to explain why a client could not qualify for a particular company.

In exposing the fact that a number of low priced companies existed, we also found that they had been reserved for special clients, which often required their willingness to purchase more than one type of insurance from the agent/company. They were the hidden loss-leaders of the industry and revealed the true amount of discretion agents held; discretion exercised behind the veil of consumer ignorance associated with "underwriting" criteria. From information provided by clients and reluctant agents, a file of underwriting criteria was developed which helped determine what companies consumers could qualify for.

Other agent responses ranged from disbelief that a small company would undertake such a task, to veiled threats to contact the state regulatory commission (they were encouraged to do so), offers to purchase our program and the availability of kickbacks (usually through auto club memberships) for referrals. The most angry agents were those whose clients took them copies of our printouts and asked them to justify the rates they were being charged.

At the same time, however, a few agents congratulated us on the approach. Some were pleased that a service existed so that they could refer shoppers to a single rating location rather than waste their time on too price conscious consumers. More importantly they expressed concern as to the questionable practices of some people

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in their industry and the possibility that our service might help raise consumer awareness and benefit more honest and efficient agents and companies.

The threat that this type of information might have on the industry can only be indirectly assessed. One indicator, however, is the apparent change in attitude evidenced by investment counselors, auto loan officers and a consumer credit counseling agency. Investment counselors expressed interest in the service and the time it would save them in searching companies for their clients; bank auto loan officers similarly thought it was an excellent idea, as did the head of the local counseling service for those having trouble making their installment purchases. After a few weeks, investment counselors failed to keep their appointed visit to the office and were suddenly unavailable, auto loan officers noted that the service was not a part of the bank's interest, and the head of the financial counseling service stated that his board "decided to stay neutral," as might be expected from an organization where banks and insurance companies were well represented on his board.

A less subtle response, and indeed the one I most appreciated, was made by a bank vice-president, who asked if we were "aware" of what we were doing and noted that an insurance company was one of their largest clients. No delayed reaction here—nor uncertainty as to the influence of the "invisible bankers."

The consumer response was generally enthusiastic. Like many agents, there was some reluctance to believe that we were not actually trying to sell insurance. The average consumers were what marketers refer to as innovators. Middle class and above, they recognized the need for information and the utility of the search in reducing their own information costs. Of the approximately two hundred clients we serviced, we estimated that over 70% actually used the data to select an insurance company. Savings were usually in the $80/yr. range, although many actually saved hundreds. Others used the service and found that their existing policies were very competitive, thus validating their sage choice in obtaining their current company. Many who called and decided not to use the service noted that their agent informed them that they were already receiving the lowest rate legally allowed. Our data suggested this was seldom the case.

While the computerized system only included rate regulated companies, consumer demand required that we also call county mutual companies for high risk clients. For this group, possible savings were immense. Once these companies realized that we were truly objective and only sought the lowest price for our clients, they eagerly sought to provide competitive prices. For especially lucrative cases, bidding wars actually ensued, with agents calling and asking how their quotes compared to others and going back and "recalculating" to stay in the running.

THE INSURANCE MARKET AT WORK

The experience of providing consumers additional information on the structure and prices of the auto insurance industry revealed four factors which help explain how consumers are treated in the exchange process and their relationship to oligopoly pricing practices. They include the commission structure, creaming, capturing, and churning practices.

Commissions are frequently based on an incentive system which pays higher rates for higher priced lines of insurance. For example, the same insurance may be available for $500 from one company and $700 from another, with the agent commission rate at 10% and 15% respectively. The agent faces an immediate $55 incentive to place the buyer in the higher priced company, in addition to similar positive rewards in future years. As are most elements in the insurance market transaction, the buyer is usually unaware of this difference.

Creaming is closely related to the commission structure. To be eligible for lower prices, the buyer must meet stringent underwriting criteria which pertain not only to his driving record, the lack of young drivers, etc., but also to the (1) age and type of car and (2) the types and amounts of insurance purchased. Companies justify this practice by saying that people with new cars and full coverages are preferred risks. At the same time, however, these eligibility criteria mean that lower rates will only be applied to high levels of insurance, thus providing a higher base for the agent's commission. Regardless of driving records or other personal characteristics, people with older cars (where the premium would be low) or those with high performance cars (where the risk is assumed to be too high), are excluded from this opportunity for low prices.

Capture helps explain why buyers are reluctant to switch companies. Many consumers expressed fear of changing companies, aware that to do so would put them at risk. For the first two months of a new policy, companies may cancel the policy without explanation. While ostensibly to allow the company to verify the buyer's

status, this practice actually serves to limit shopping and changing products. It is difficult to imagine that an industry which specializes in risk analysis and aversion is unaware of the immense pressure this unilateral power exerts on consumers.

Churning is the final concept we consider. It entails the systematic creation of new opportunities to force people out into the market place to search for insurance at higher prices. Cancellation is the most overt example of this process, although other opportunities exist when accidents, tickets, new drivers or different cars are considered. One of the most interesting aspects of this process is that the very criteria used to cancel or refuse insurance in one company also serves as a signal to other companies to deny lower prices. The attribute which made the consumer reenter the market at the insurance companies command serves as a scarlet letter to other members of the industry.

It should be noted that while discussed separately, auto insurance commissions, creaming, capturing and churning practices are systematically related. For example, rather than submitting claims to insurers, policyholders admit to avoiding the filing of claims rather than risk their captured status. I am not aware of any studies which have focused on this indirect tax consumers willingly endure to protect their insurance position.

IMPLICATIONS FOR PUBLIC POLICY

This combination of structural and behavioral factors suggest that under the current state regulated system in Texas, consumers are systematically removed from any true participation in a market system. Market shares, concentration ratios, the presence of many sellers and buyers aside, at the level of the actual transaction, consumers are poorly served. While these observations have been based on the Texas experience, many of these same problem appear in other states.

In my opinion, the Texas system reveals the benefits which accrue to an industry in a partially regulated environment. I say partially because the two major regulatory mechanisms, rate regulation and agent licensing, actually have little effect on the way the market operates between buyers and sellers.

This is an especially discouraging observation, given the quality of the Texas state insurance commission staff. In my dealings with the state agency, I found the staff to be not only extremely knowledgeable, but more importantly professional in their approach and with a sincere concern for the public interest. These qualities were abundantly clear among the rate making and actuarial sections. They are an excellent model for those of us in public administration who sometimes forget the difficulties and nebulous rewards associated with public service.

The problem then, is not one of intent, but reflects the relative imbalance between independent states on the one hand, and one of the largest industries in the nation on the other. No other industry with the size and influence of insurance has succesfully exempted itself from national scrutiny and responsibility. Indeed, the very protections afforded the industry by the McCarran-Ferguson Act hinder the ability of public servants at the state level to get an accurate picture of how the industry operates, most notably in the question of the handling of their reserves and the possibility of cross-state subsidies.

The ability of the industry to deal separately with each state not only increases overhead costs at the state level, but also prohibits governmental attention to the very issues of restraint of trade, monopoly behavior, the exclusive binding of sellers to particular products and the entire issue of fair trade practice which are of special importance to protect buyers in complex decision-making environments.

The combination of state rate regulation on the one hand, and exemption from federal scrutiny on the other has resulted in leaving consumers little power in their relationship with the industry. Indicative of the relative powerlessness of individuals in this system is the fact that the most important element in the overall decision-making process, the underwriting rules, are exempt from both state and individual review. Indeed, underwriting is the ultimate hidden hand of the market place which is controlled by the industry, and one which ultimately must be dealt with.

In conclusion, Mr. Chairman and members of the subcommittee, I would like to suggest that the market system can be made to work. It requires more consumer information, protection from unfair business practices, greater freedom for sellers to levelop price competition within the framework of reasonable profits, administrative reviews of unilateral company decisions, removals of barriers which inhibit the free movement of buyers among sellers and much more attention to the coercive opportunities associated with the marketing of a product which is virtually required by law.

With the subcommittee's permission, I would be happy to submit additional analytical information which might further clarify some of the issues I've mentioned this morning. I thank the subcommittee for the opportunity to appear.

ATTACHMENT A

INSURANCE CONSUMER SERVICE OF AMERICA
P.O. BOX [illegible] PHONE [illegible]
DALLAS, TEXAS [illegible] METRO [illegible] 0442

ON YOUR BEHALF ICSA HAS ANALYZED AUTOMOBILE INSURANCE COSTS USING THE INFORMATION YOU PROVIDED. THESE COSTS ARE BASED ON RATES FILED BY INSURANCE COMPANIES WITH THE TEXAS STATE BOARD OF INSURANCE. ACTUAL COSTS MAY VARY FROM THOSE LISTED BELOW IF DIFFERENT TYPES AND/OR LEVEL OF COVERAGE ARE CHOSEN.

ICSA DOES NOT SELL INSURANCE AND CANNOT GUARANTEE THAT THE COMPANIES NAMED BELOW WILL ACTUALLY WRITE A POLICY FOR YOU. YOU THE CONSUMER ARE OUR ONLY CLIENT. WE ARE PLEASED TO SERVE YOU IN COMPARATIVE AUTO INSURANCE SHOPPING.

BIG TEX
STATE FAIR GROUNDS
DALLAS COUNTY
DALLAS TX 75200

DATE. 11/18/82

CLIENT # 1- 2

AUTO YEAR 81 (2A2. 7) — AUTO BODY TYPE MALIBU 2DR
AUTO TRADE NAME CHEVROLET — MOTOR ID NUMBER 1G1AT69K0978l2138

TYPE/LEVEL OF COVERAGE → / INSURANCE COMPANIES	BODILY INJURY 25/50 (000)	PROPERTY DAMAGE 10 (000)	BI/PD COMBINED 0 (000)	COMP $ 100 DED	COLLISION $ 200 DED	PERS INJURY PROTECTION 5,000	UNINSURED MOTORIST 25/50 (000)	6 MO TOTAL COST
COMPANY A	31	51	0	31	128	12	11	263
COMPANY B	32	53	0	32	133	12	9	271
COMPANY C	34	56	0	34	142	13	9	288
STANDARD COST - THIS AUTO	40	66	0	40	167	16	11	339
HIGHEST COST - THIS AUTO	65	109	0	66	275	26	18	559

YOUR INSURANCE COST FOR THIS AUTO MAY VARY FROM A LOW OF $ 263 TO A HIGH OF $ 559
OR A DIFFERENCE OF $ 296 FOR SIX MONTHS, OR $ 591 PER YEAR.

AUTO YEAR 80 (1A:. 6) — AUTO BODY TYPE GRANADA
AUTO TRADE NAME FORD — MOTOR ID NUMBER 0E81D68035P32

TYPE/LEVEL OF COVERAGE → / INSURANCE COMPANIES	BODILY INJURY 25/50 (000)	PROPERTY DAMAGE 10 (000)	BI/PD COMBINED 0 (000)	COMP $ 100 DED	COLLISION $ 200 DED	PERS INJURY PROTECTION 5,000	UNINSURED MOTORIST 25/50 (000)	6 MO TOTAL COST
COMPANY A	20	34	0	20	50	10	11	144
COMPANY B	21	35	0	20	52	11	8	147
COMPANY C	21	35	0	20	52	11	8	147
STANDARD COST - THIS AUTO	26	44	0	26	65	13	11	184
HIGHEST COST - THIS AUTO	43	72	0	42	107	22	17	304

YOUR INSURANCE COST FOR THIS AUTO MAY VARY FROM A LOW OF $ 144 TO A HIGH OF $ 304
OR A DIFFERENCE OF $ 160 FOR SIX MONTHS, OR $ 319 PER YEAR.

AUTO YEAR — AUTO BODY TYPE
AUTO TRADE NAME. — MOTOR ID NUMBER

TYPE/LEVEL OF COVERAGE → / INSURANCE COMPANIES	BODILY INJURY (000)	PROPERTY DAMAGE (000)	BI/PD COMBINED (000)	COMP DED	COLLISION DED	PERS INJURY PROTECTION	UNINSURED MOTORIST (000)	6 MO TOTAL COST
STANDARD COST - THIS AUTO								
HIGHEST COST - THIS AUTO								

YOUR INSURANCE COST FOR THIS AUTO MAY VARY FROM A LOW OF TO A HIGH OF
OR A DIFFERENCE OF

• • • FIGURES BELOW ARE THE TOTALS OF ALL AUTOS PRINTED ABOVE • • •

INSURANCE COMPANIES	BODILY INJURY	PROPERTY DAMAGE	BI/PD COMBINED	COMP	COLLISION	PERS INJURY PROTECTION	UNINSURED MOTORIST	6 MO TOTAL COST
COMPANY A	51	84	0	50	178	22	22	407
COMPANY B	53	87	0	52	185	23	17	418
COMPANY C	55	91	0	54	194	24	18	435
STANDARD COST - ALL AUTOS	66	109	0	66	232	29	22	523
HIGHEST COST - ALL AUTOS	109	180	0	108	382	47	35	863

YOUR INSURANCE COST FOR THESE AUTOS MAY VARY FROM A LOW OF $ 407 TO A HIGH OF $ 863
OR A DIFFERENCE OF $ 455 FOR SIX MONTHS, OR $ 910 PER YEAR.

THE INFORMATION ABOVE IS BASED ON THE TEXAS STATE BOARD OF INSURANCE RECORDS AS OF 11/01/82. NUMBERS ABOVE MAY NOT ADD DUE TO ROUNDING.

THIS IS A SAMPLE OF THE RESULTS OF A RATE COMPARSION REQUEST. IN AN ACTUAL SEARCH, THE SPECIFIC NAMES OF THE INSURANCE COMPANIES ARE PRINTED (RATHER THAN COMPANY A, B OR C).

Chairman RODINO. Thank you very much.

Professor Brinlee, there was one statement you made during the course of your presentation which intrigues me and makes me wonder a little bit. You've been talking about the need for information. Then you talked about the purchaser of a car and his eagerness to just get the car out on the street.

Dr. BRINLEE. That's right.

Chairman RODINO. And, therefore, he wants to get any insurance policy quickly, just to know that he's covered.

Well, doesn't that suggest he doesn't care?

Dr. BRINLEE. No. I think it suggests the historical way in which this product of insurance has been sold. People assume there is no choice, and they assume and know to go out in the marketplace is a time-consuming endeavor they would rather avoid.

Indeed, when we went to an auto salesman and asked if they would like a service like this, we found that to the auto sales industry this is anathema. This is a hidden cost they don't want the buyer of the car to recognize at all.

Chairman RODINO. Do you think that if the person who was selling the insurance would say to that purchaser of the car, "Now, wait, I want to explain this," that, in view of what you said, he's going to be willing to stay there and listen, or that that's the information he's looking for? Is it going to make any difference; or does he just want to take that car out on the street?

It seems to me you're saying that's the attitude. Perhaps the companies know this and say, "Well, why do anything unnecessarily? The public isn't concerned."

Dr. BRINLEE. The small number of people who purchase new cars may, indeed, at the time of that purchase not go through a search process. Indeed, the salesman tries to get them to drive the car today. "I'll give you a special deal," and so forth and so on. The only time when insurance seems to occur when a car is purchased is for very high-priced insurance, where the agent knows the individual is eager to drive the car off and will help him get insurance right there. But otherwise, there's no matching of the search and the purchase of the car.

Chairman RODINO. Mr. Jaffe, how long have you been interested in this subject?

Mr. JAFFE. I would say about 20 years, Mr. Chairman.

Chairman RODINO. I know you've done a lot of reporting on it, and have written many, many articles. As the result of all those interviews and all the reporting you've done over 20 years, do you find that there is a failure on the part of the insurance industry to provide information?

Mr. JAFFE. That's basically a cursory synopsis of what I have found over the years. Yes, I think there's an absolute failure on the part of the industry to provide, or even any intent or enthusiasm on the part of the industry to provide any type of information that would give the consumer any choice comparison.

Chairman RODINO. Do you find what Professor Brinlee talked about, that there are people that just don't care or that the public is just interested in getting insurance without having been informed fully as to what the facts of the policy might be or what the cost or the rate of return is?

Mr. JAFFE. Mr. Chairman, I have found not only in automobile insurance, but in health insurance and in other lines of insurance, that the general attitude on the part of the consumer is that the consumer feels that insurance is a necessary evil. He doesn't always take the attitude that it's necessary to have insurance, he somehow feels he must have it, he must put up with it, he must contend with it. And with a lack of the information to him in terms of competitive choice, he's almost intimidated into buying insurance. And I think that's what the professor referred to when he was talking about the automobile dealer and someone driving the automobile out of a show room. I think that type of person almost feels as if it's absolutely essential that he must have it, yes, but he doesn't know what he has. He will accept whatever someone tells him he must have, and that's the attitude.

In New Jersey, that is the precise attitude, because there is no insurance market in New Jersey, especially in automobile insurance.

Chairman RODINO. Isn't New Jersey the State where we pay the highest rate for automobile insurance?

Mr. JAFFE. That is correct, sir.

Chairman RODINO. Do you find, or have you found during the course of your many interviews and inquiries regarding this subject that there are people who would have preferred to have this information disclosed to them and who feel that they just are not in a position as individual consumers to be able to correct this situation?

Mr. JAFFE. Well, I think that many consumers take the position that while they don't have the information, they're almost reluctant to ask too many questions because, again, it is the insurance industry that has the choice of selection rather than the consumer. The consumer in New Jersey does not buy automobile insurance as if he were to go out and retain a service from some other profession or industry or to go out and buy some other consumer product. He is practically at the mercy of the insurance industry. And he will get it the best way that he knows how, and that is, depending on whoever will make it available.

And I am not talking about a poor risk driver. I am talking about drivers who have good driving records, but because of a very restricted automobile insurance market in New Jersey, the product is just not available, and when it is, the consumer has very little choice, in terms of questioning the merits of the product, other than simply to buy it when it's made available to him.

Chairman RODINO. Mr. Jaffe, the 1979 FTC staff report noted that the FTC had contracted with a University of Wisconsin professor to study life insurance cost disclosures in New Jersey. The study was conducted in cooperation with the New Jersey Department of Insurance. New Jersey had adopted the model disclosure regulation recommended by the National Association of Insurance Commissioners. Upon reviewing that survey, I see that the results reflect large gaps in consumer knowledge about how the NAIC indices actually work. The FTC staff noted that the study raised serious questions about the effectiveness of the model regulation.

Do you believe that gaps in consumer knowledge about life, auto, homeowners, and health insurance continue to exist, as was indicated in that FTC report?

Mr. JAFFE. Without any question, Mr. Chairman. I believe there are great gaps in terms of information that is being made available, certainly, as I said before, by the industry, but perhaps even more so by the State insurance department. I think that the regulators are, indeed, very weak in the area of making that type of information available. There are press releases. There are press announcements that are made, but I think that if the consumer doesn't happen to read the story that particular day, there is no place that the consumer knows to go to get the kind of information that I think you're referring to. There is just no other way that that information is being made available.

Chairman RODINO. Do you believe the States require enough disclosure to make meaningful choices?

Mr. JAFFE. I believe that the States do not require—unfortunately, do not require sufficient disclosure of any type dealing with insurance. And I think—one drawback, I do believe is that the amount of money that is being spent by States to support their regulatory agencies is far, far insufficient, as compared to the amount of money that the regulatory agencies bring into the State, as a result of fees and taxes that are imposed on the insurance industry, either through underwriters or the license fees that brokers and agents pay.

I know that to be the case in New Jersey. I believe that the industry brings in somewhere between $30 and $35 million to the State, and yet the State insurance department is supported on an amount that is far, far less than that.

Chairman RODINO. In other words, you feel that the department itself which is supposed to regulate doesn't have sufficient personnel, the expertise and whatever else is necessary for that type of regulation?

Mr. JAFFE. Yes.

Chairman RODINO. Would you say that that's the situation in States other than New Jersey?

Mr. JAFFE. From every indication that I have, that seems to be the case in almost every State.

Chairman RODINO. I'd like to ask each of you one question, and each of you may comment on it: It seems that all of you, whether you're talking about life insurance, auto insurance, or whatever, talk about the need for consumer information, and apparently, as we have heard, a certain reluctance on the part of the industry to provide it. What is it going to take to assure that the industry recognizes the importance of providing the consuming public with this kind of information?

Mr. JAFFE. Well, if I may, Mr. Chairman, I think that one of the problems is that if government cannot force that type of response, then certainly, the consumer is at a far greater disadvantage than government. I recall this very committee, the Judiciary Committee hearings that were held back in the mid-1960's when you and, I believe at the time, Congressman Cahill, were very much involved in similar types of efforts, and similar types of questions were raised. Now that goes back a generation ago, and yet there——

Chairman RODINO. There was a certain reluctance at that time to undertake that study.

Mr. JAFFE. And the problem persists today.

Chairman RODINO. Would you care to comment on that, Professor?

Dr. BELTH. Mr. Chairman, I believe the industry recognizes the need for the information. And I think that they also recognize the consequences, if it were provided. And I think they have a very strong and sincere desire to make sure consumers do not have the information that is necessary.

Chairman RODINO. Well, the question then is, what is it going to take? Is it going to take legislation on the part of the National Government, a regulation, a statute, to require disclosure?

Dr. BELTH. Well, many years ago, Mr. Chairman, I concluded that it would never be done on any kind of voluntary basis by the industry, and I concluded that the only way that the information would ever be made available would be if it were mandated, by some agency with the power to mandate. Whether it be by law or by regulation, it would have to be mandated, but the experience—as I indicated in my statement—that I've had in recent years suggests that it will never be mandated.

Chairman RODINO. You're a pessimist.

Dr. BELTH. A realist, Mr. Chairman.

Chairman RODINO. Professor Brinlee.

Dr. BRINLEE. I think it will take two things. First, a strong statement on the part of National Government to say that insurance needs the protections of the marketplace as are provided for in other kinds of purchases like this. But I think another source of change will come from the agents themselves. I think that given the calls that I've had from many agents, who talked about how difficult their own industry was, that there is a latent recognition on the part of the sellers of this product. For the honest and more scrupulous members of this industry, this request would be very helpful. Competition would increase, efficiency would increase, and so forth.

So I think within the industry itself, that there is a movement there, but I think that at the highest levels of the industry, the movement will be consistently rejected.

Chairman RODINO. Well, why would the industry be threatened? This is information that out in the marketplace would provide a competitive atmosphere. We've talked about the need for competition. We've seen this administration, more than any other administration, talk about being out there and assuring that there is no impediment—that the marketplace is actually allowed to regulate itself, so to speak, by providing the kinds of goods and services that are competitive.

Why would that be a threat to the industry?

Dr. BRINLEE. As other researchers have found, the industry offers oligopolistic prices. If the information, price information, were available, we would find more insurance companies competing on price. Everyone would start to move to that price. So the oligopolistic price they charge us now, which is higher than a true market system, would be lost to them.

In fact, agents called us and said, "Could you tell us the lowest price companies? I want to go sell that type of insurance."

And we also had agents call and say "I know I don't offer the lowest price. I would like to know who does. And I want to buy it for my mother"—or "my brother"—or whoever—"because I know we're too expensive."

So it's simply maintaining oligopolistic price structures.

Chairman RODINO. Professor Belth, one question that the FTC report addressed was the question of low yields for buyers of life insurance. Do you believe that there are substantial numbers of Americans today that could profitably replace their old policies with newer policies or alternative investments?

Dr. BELTH. Mr. Chairman, your question really deals with replacement, which simply defined, would be replacing an existing policy with a new one. And it's my view that there are many situations in which replacement is justified. I believe equally strongly that there are many situations in which replacement is not justified and the unfortunate situation out there, the absence of information for owners of existing policies, is that they have no real way to determine which group they're in. And so they are subject to pressure from people—there is an entire industry developed that is engaged in replacement of life insurance. And the owners of existing policies simply have no way of sorting out the accurate from the inaccurate information being provided by those in the replacement industry.

Similarly, there's an entire conservation industry out there, people engaged in the business of trying to prevent people from replacing policies. And again, the consumers are not in the position to separate the accurate from the inaccurate information. They are simply trapped between these two industries without the information to make an intelligent decision in their own interests.

Chairman RODINO. The Chair is going to declare a recess until we will have voted.

Mr. FISH. I won't be able to come back. Could I just ask my questions?

Chairman RODINO. Sure.

Mr. FISH. Thank you.

I think, Mr. Chairman, I don't want the inference to be left here, as I think it was in Mr. Jaffe's testimony, that the fault lies mostly with insurance companies. I think this is an oversimplification. In fact, we have a situation in New Jersey where lots of companies have left the State, and this has to do with the restrictive nature of the regulation. There is a book published by the American Enterprise Institute for Public Policy Research entitled "Federal, State Regulation of the Pricing and Marketing of Insurance." In chapter 3, it maintains that the difference between regulatory schemes in different States—which is the subject of that chapter—and there's a clear inference here that the reason that the State of New Jersey auto owners pay more is, in part, due to the highly rigid State regulatory apparatus.

Now Professor Belth, I won't be back here to hear the answers, but I wonder if you'd address these questions, because—I understand this is a hearing on information for policyholders, but I would like to get us back to McCarran-Ferguson, if possible, and

your statement contains no recommendation to the subcommittee regarding the repeal of McCarran-Ferguson, which is the subject of this inquiry. And I would appreciate your personal views on that.

And second, with respect to the cost disclosure and rate of return information, why does McCarran-Ferguson present a problem? Couldn't the various States or even this Congress enact legislation mandating more disclosure even with the McCarran-Ferguson Act in place?

Thank you. Thank you, Mr. Chairman.

Chairman RODINO. The Chair will declare a recess until this vote is recorded, and in 15 minutes we'll be back here.

[Recess.]

Chairman RODINO. The subcommittee will proceed. I understand several questions were placed before you, Professor Belth, and you were asked to respond to them, in the absence of Mr. Fish. If you would, please proceed.

Dr. BELTH. Thank you, Mr. Chairman.

Congressman Fish presented two questions, and I'd like to respond to the second one first, the question of whether the existence of the McCarran-Ferguson Act poses a problem regarding price disclosure and rate of return disclosure.

I do believe that the various States could enact legislation, or the commissioners could adopt rules mandating rigorous disclosure, but as I indicated in my statement, my experience over the years with what has happened, simply has convinced me that such legislation or rules will never be adopted. As far as the Congress is concerned, I believe the Congress could enact some kind of model disclosure regulation, but there again, on the basis of what has taken place in the past, I do not anticipate any such thing happening.

The first question indicated correctly that my statement didn't contain any recommendations regarding repeal or modification of McCarran-Ferguson or direct Federal regulation. My personal view is that State regulation has serious shortcomings that I've observed over the years. I simply do not know whether Federal regulation would be better, and that's one reason why I just simply don't make any recommendations about Federal versus State regulation. And also for that reason, I really haven't made any specific suggestions on repeal or amendment of McCarran-Ferguson.

Chairman RODINO. Mr. Hughes.

Mr. HUGHES. Thank you, Mr. Chairman, and I too welcome the panel this morning.

I have just a few questions.

I want to welcome Mr. Jaffe, in particular, whom I've read for a number of years, and who is a very good investigative reporter.

Mr. Jaffe, the suggestion is that the insurance industry is not competitive enough, that in places like New Jersey—which I am more familiar with than any other jurisdiction, having been born and raised there and having spent much of my career in New Jersey—insurance, automobile insurance in particular, is not readily available. I think that was implicit in your suggestions, but I don't know that I buy that entirely, because I find that insurance is available in New Jersey. It's a little more expensive than I would like it to be, but on the other hand, we find that insurance companies do not want to write automobile insurance. It seems to me to

suggest that, indeed, it's not a very productive market. It's not an area where carriers want to have a presence. Indeed, New Jersey has had a very difficult time encouraging many of the companies to stay there.

Isn't that so?

Mr. JAFFE. Yes; that's absolutely so, Congressman. I think that—just to clarify one point. Insurance is available in New Jersey; however, the problem is that the motorist or the consumer does not have the choice of simply going to an insurance company representative and saying, I would like to question your insurance and compare it to somebody else's insurance, and then make the choice on my own as to whether I want to buy your insurance as against someone else's insurance.

Mr. HUGHES. What precludes them from doing that, Mr. Jaffe? I don't understand.

Mr. JAFFE. What precludes that is the fact that the insurers in New Jersey have suffered rate inadequacy over the years. That is what they claim to be the case and I believe there's evidence of that, that over the past 10 or 12 years, there has been some very strict regulatory practices on insurance company rate requests. I don't know for sure who's right. The insurance commissioners over the years have claimed that the insurance industry has not warranted the rate requests that they have made. As a result, there have been some 10 or 12 insurance companies out of over 400 which write automobile insurance in New Jersey, who have voluntarily left. In fact, I think that's even a high figure. I think it's something less than a dozen.

Mr. HUGHES. Well, that would suggest to me that something is wrong. After all, they're in the business to make money. And if, in fact, the business is so structured that it's productive, I would think we wouldn't have the exodus that we have. So obviously, something is wrong.

Mr. JAFFE. Well, I believe you're right. Something is wrong between the applications that are being made by insurance companies for rate relief as against what the insurance department considers to be the type of rate that the insurance companies should have. I think that the position of the insurance department has traditionally been that insurance companies are making money in New Jersey, whereas the industry claims that they're losing money. I think the industry says that they have lost something in the neighborhood of $1 billion over the last 10 years writing automobile insurance in New Jersey. The various commissioners over the years have disputed that and claim that, based on the information that's been requested of the insurance industry and made available to them, that figure does not warrant the type of rates that the insurance companies are requesting, that they haven't, in fact, lost that kind of money, but that they have, in fact, made money.

There has been an ongoing battle over disclosure of the type of information that the insurance department has requested as against what has been made available.

Mr. HUGHES. I followed that debate, and I must acknowledge that I really don't have the expertise to make a value judgment one way or the other. But the very fact that we have so many com-

panies that want to withdraw from the State suggests to me that there might be some merit perhaps to their suggestion that there's something wrong with our structure.

Let me move on to a couple other points. I don't want to use my whole 5 minutes on this issue.

I find that people—and again, it's my own perception—buy insurance from particular agents because they have a great deal of confidence in that agent. They have faith in an agent. I think of my own personal experience. While I'm sure there might be some criticism directed at agents for not providing information, I've always had a very good experience with my agents. There is one criticism I've always directed to agents, and I suspect it might be because it's policy, but I think it's wrong policy. Consumers, for instance, when they walk in to purchase automobile insurance, ordinarily purchase the minimum amount. That's what is required. They purchase a 10 and 20 policy. They don't understand that today $20,000 isn't very much insurance and that, in fact, if they have a serious accident and there's a $100,000 judgment, they're obligated for the difference, personally. That often is not disclosed. But again, I'm not sure just what the experience is around the country, because in my own situation, I know that the agents I've dealt with have been very candid about that.

Now I've heard a lot of complaints that other agents do not provide that information. I don't know whether that's an agent policy or whether that's a carrier policy, or what the policy is. Is that the type of information that you feel should be given to consumers besides the obvious interest in seeing that they have rate structures so they can make some comparison?

Mr. JAFFE. Congressman, I think that the type of insurance that is being sold today by the type of independent agent who has a choice of companies and who could take the time to consult with his policyholders, I don't believe that there is that volume of insurance being sold by that type of agent as there was some 10 and 15 years ago. I think that in New Jersey there are more direct writers. There are more people who are dealing directly with company representatives rather than with general agents. At one time an independent agent might have represented six or seven different insurance companies. Today he may represent one or two, simply because of the constricted nature of the market.

I think that the information that we're talking about, to the average consumer, a good independent agent, as you suggested, will provide that type of information, but I don't know that the average consumer either has the knowledge to ask for it or goes out of his way to ask for it. I think generally he kind of relies on the judgment of the agent. There is no other way to get that information.

Mr. HUGHES. I think, Mr. Jaffe, that an individual going to an agent views the agent almost like he views his attorney, in many respects. People in the community have faith in that individual. They go in, and they indicate that they want automobile insurance. I would venture to say that very few people ever read their automobile insurance policy. I must confess I haven't read the last ones that came out to my own home. But I know, for instance, that there are standard provisions that are found in all policies.

I think the point has been made by Professor Belth that we rely upon the regulators, and I think that there is some substance to that. We also know that the policies are pretty standard. And so I think that that accounts for why people do not raise more questions. I have very few people that have ever said to me, look, I'm not getting enough information on insurance. Now I have people that talk to me about a lot of things at parties, on the streets and other places. I must confess I've never, in 10 years, had anybody say to me, "I can't get any decent information about my insurance."

Now I've had people say to me, "These rates in New Jersey are ridiculous. When are you going to start doing something about these crazy automobile insurance rates." And that's accurate. I think that our rates in New Jersey are crazy. I think they're ridiculous. I think that we've got to do something about it, but we're not in a position to be addressing it at this level. But that's the only complaint I've ever heard.

Mr. JAFFE. The nature of insurance is such that we have come to accept the fact that our insurance agent makes insurance available to us and provides it. I think the comparison that you made of the insurance agent to the lawyer—I think there's a difference there. When you deal with a lawyer, you're dealing with a direct service. You deal with your doctor, you're dealing with a service. You're not going to shop one lawyer to another. You're not going to shop one doctor to another. But I think when you deal with insurance, you are dealing with a product. The product is nothing more than a piece of paper, and it's one that you know that you must have, in terms of a contract that backs up that piece of paper, but yet you are paying a substantial amount of money for that piece of paper, and you know that there are many companies that provide something similar to that piece of paper, but you don't know, basically, that all contracts are similar in a particular line of insurance.

If there are 400 companies that sell auto insurance in New Jersey, I don't think the average consumer recognizes the fact that you're dealing with a standard policy, for the most part. I think he knows that company A will not advertise the nature of its product or the cost, depending on where you live or how old you are or how many accidents you've had, as compared to what company B might advertise.

Mr. HUGHES. I must say to you that I understand there is a very decided difference between going to somebody who is your legal counsel and going to somebody who's your agent. I'm talking about perception. People go to agents because they have confidence in them. They're known in the community. They're in the Exchange Club or the Rotary Club with them. They're usually very prominent business people in the community, and there's a basic trust there. That's the point I make. You add to that the fact that most people recognize that the State does a fairly decent job in most States to provide standardization and some degree of regulation—the industry I'm sure feels it's overregulation and consumer groups all can feel it's underregulation. But I think when you combine those two factors, that might account for the fact that questions aren't being asked.

If I might move on——

Mr. JAFFE. Congressman, before you move on, I'd like to answer your question with another question to you, if I may.

You have approximately 4 million insured drivers in New Jersey. What do you do when 900,000 of those 4 million, or almost 25 percent, go to that very same agent that you're talking about and that agent cannot provide them with insurance, and yet those 900,000 have clean driving records, no accidents, no driving violations of any type?

Mr. HUGHES. Well, we have a serious problem in New Jersey, and you ask me what we do about it. In the first place, I would hope if I were at the State level, I would be voting for a more realistic and a more rational no-fault program. That's one of the things I might begin doing, and perhaps as these hearings progress, I'll learn a lot more about the industry and its structure, and we'll have some different opinions when we finish these hearings. After all, that's the purpose of hearings.

I'm just telling you what my perception is. I've seen the figures and, frankly, I'm confused. There are so many figures bounced around as to what it costs to write insurance and how much money the industry is losing and the State's position about how much the industry is making. And frankly, I don't know where the truth lies. I suspect it's perhaps somewhere in between, as is often the case. But I do know that the no-fault problem in New Jersey is part of the problem. I'm not sure it's the entire problem, because I'm not so sure that even when we were talking about different thresholds—ones that made more sense than the one we ended up with—that it was going to mean that much in rates when you compare them with other States. For instance, a policy in Washington, DC, for me would probably be about half of what I pay in New Jersey for automobile insurance. Now that my son is 17 years of age and is going to get his driver's license, hopefully tomorrow, I fear what I'm going to get in the mail next week. [Laughter.]

Thank you very much. I appreciate your testimony and I apologize to the rest of the panel that I got so interested in New Jersey, but I am interested in the premium issue in New Jersey and a whole host of other things. I did read your statements. They were very good statements, and I appreciate your contributions.

Thank you, Mr. Chairman.

Chairman RODINO. I thank each of you for having taken the time to come here, and I appreciate the information you've provided to us.

Mr. JAFFE. Thank you, sir.

Chairman RODINO. Our final panel is composed of representatives of three agents groups: Mr. Frank Patterson, Independent Insurance Agents of America; Mr. David Ream, National Association of Professional Insurance Agents; and Mr. Robert Pierce, Chartered Life Underwriter, on behalf of the National Association of Life Underwriters.

We're going to urge each of you to summarize your statements and whatever written statements you have will be inserted in the record in their entirety.

TESTIMONY OF FRANK PATTERSON, PATTERSON & ASSOCIATES, INC., ON BEHALF OF THE INDEPENDENT INSURANCE AGENTS OF AMERICA; DAVID REAM, L.F. REAM, INC., ON BEHALF OF THE NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS; AND ROBERT PIERCE, C.L.U., ON BEHALF OF THE NATIONAL ASSOCIATION OF LIFE UNDERWRITERS

Mr. PATTERSON. Thank you. I have a very brief written statement which I will further reduce as we go along.

I am president of Patterson & Associates, Inc., which is an insurance agency located in Chevy Chase, MD. We sell and service a full range of personal and business insurance. We maintain contractual relations with a number of insurance companies, permitting us to best represent our customers by matching them with the company and policy that best serves their needs.

I'm here today in my capacity as chairman of the Federal Affairs Committee of the Independent Insurance Agents of America. IIAA is, incidentally, the Nation's largest independent producer association, representing more than 220,000 agents and their employees. Its members offer all lines of insurance: property, casualty, life and health.

With me today, Mr. Chairman, is Larry Herman, who is director of congressional relations for IIAA.

Mr. Chairman, on behalf of myself and IIAA, I welcome the opportunity to participate in these hearings, addressing the McCarran-Ferguson Act and competition in the insurance industry.

I understand that you want to examine today consumer information in the insurance marketplace. At this point in our written testimony we make preliminary remarks concerning the regulation of insurance and the industry's limited immunity from the Federal antitrust laws. We're going to skip over that in the interest of time with simply the statement that we strongly believe, both as a matter of principle and based on well over a century of experience, that State regulation is most compatible with the public interest and most suitable to the types of regulatory issues associated with insurance such as ratemaking, insolvencies and claims practices.

I shall now turn to the specific questions you have posed to us concerning consumer information. In your letter of invitation, you observed, "As an independent insurance agent who deals directly with policyholders, you are in a unique position to comment on information needed by consumers and the ease with which they can obtain that information."

I couldn't agree more. Independent insurance agents are, in an important respect, consumer representatives, and our livelihoods depend upon our ability to effectively respond to the insurance needs of our clients, to answer their questions and work with them to tailor a policy that best serves them. As to the availability of such information, it is abundant. I distributed, along with my prepared statement, examples of the type of information, geared specifically to the average consumer, that is made available to the public by IIAA and by individual insurance agents and companies.

[Material on file with the subcommittee.]

Is it relevant? Well, you can judge for yourself. One covers auto, homeowners and renters insurance. It explains in lay terms the

various forms of coverage available to the consumer, auto collision coverage, the 80-percent coinsurance rule with respect to homeowners coverage, special options available to suit a particular client's needs. Similar pamphlets are made available by all the companies that we represent.

As I mentioned earlier, these, for example—and I think they were submitted to staff—are just some of the many that we have in our office alone. Incidentally, our national association, IIAA, puts out, which is distributed through all of our 220,000 agents and employees, "How To Choose the Right Insurance," with the picture of our national spokesman, Mr. Raymond Burr, on the front page. We have one for business insurance and one for personal insurance. Well done, we feel, and done not only for the public in general, but certainly for our potential customers.

While none of these brochures could enable consumers to become do-it-yourself underwriters, they adequately inform buyers of what to look for, what questions to ask, and most importantly, what to expect from their agent and company. The independent insurance agent must be far more than a mere intermediary processing insurance applications. Independent insurance agents should and do provide the insurance-buying public professional and practical advice to assist consumers in determining what coverage is right for them and to place that coverage with the most appropriate insurance company available.

Purchasing insurance is not like buying a loaf of bread. It's more than a list of ingredients—policy terms—stamping an expiration date and setting a price. Depending on one's economic circumstances, a particular automobile policyholder may be wise to absorb a high deductible at the front end and add a high level of catastrophic umbrella coverage at the back end. It was mentioned earlier by a previous witness that perhaps it's in the best interest of the customer if we don't try to sell them the higher limits. We don't feel that way, obviously.

Most customers would come into our shop, and if we didn't properly advise them, they would go away with minimum limits, because it's cheaper, but in today's judicial environment, that is simply not doing the job for our customer. Another individual may think himself adequately insured with a minimum, low-priced policy, even though he could seriously jeopardize his personal assets should an accident occur. It is our responsibility, our duty, to discuss these factors and others with our clients. We are, after all, fiduciaries, both before the law and more importantly, before our customers. We are in a position of trust, and we hold ourselves out to be responsible for providing the best coverage available for our clients. If we fall short of fulfilling our customers legitimate expectations, we can find ourselves liable before the law and, again, more importantly, before our clients.

As to your inquiries concerning the specific types of information such as company loss ratios, insolvency, rating practices, et cetera, there are no pat universal answers. Reliable information is today available to the agent and to the consumer. If asked, I could explain to any given customer loss ratios, soft markets, underwriting criteria, claims handling practices, et cetera. But the average consumer is not at all interested in most of these technical details. In

fact, I would suspect the consumer would walk next door to my competitor, should I engage in such a discourse.

Chairman RODINO. Excuse me. I wouldn't ordinarily interrupt, but you say he's not interested. Do you think that he'd be interested if he learned what it might be about, that one might be more beneficial than the other?

Mr. PATTERSON. Well, I guess what I'm referring to, Mr. Chairman, specifically, is that as Congressman Hughes mentioned earlier, they come to the agent because, in most instances, at least it's my experience, they don't like to be bothered with those details. They want to know that they're getting a reasonably priced product, but they want to rely on that agent to assist them in putting it with the right company, with good claims service, which they will follow up. They don't want to sit down and hear about the company's operating loss ratio that exceeds 100 percent. That was the point we were making there.

Chairman RODINO. Well, I don't think that's what we're talking about, though. We're talking about what could be pertinent information that might give the insured or the prospective insured the opportunity to elect whether or not he'd choose one policy over the other. What we're talking about is the ability to be able to choose and the ability to be able to provide something which will be more competitive.

I'm going to ask you some questions later.

Mr. PATTERSON. OK. Great. I would like to address that one again when we come back to it.

In a nutshell, while we do, indeed, have much information available for our customers, my colleagues and I are well prepared to respond to any of our customers' questions from the most mundane to the most technical and to volunteer information essential to serving our client's interest. There are many areas of legitimate consumer concern that should be explained to the client. The policyholder has a right to expect prompt claims handling from his company; a policyholder has the right to expect competitive premium rates. He certainly has the right and the responsibility to know what his policy coverage includes and what it excludes, and that the company with whom he is insured is financially sound.

Agents and companies have ample incentives to meet these needs. An agent is a professional, a fiduciary and often a friend. He is also a businessman, working within one of the most competitive industries in the country. If his customers aren't satisfied with his service, policy coverage or answers to their questions, there are plenty of other agents to fill this deficiency. We are motivated to keep our customers and to keep them satisfied. We certainly do monitor the claims handling practices of our companies, and if they prove to be slow and unreliable, we will not hesitate to terminate our contracts with them and place our customers' business elsewhere.

In closing, I would like to say that IIAA has been cooperating with the FTC in its investigation of the adequacy of consumer insurance information. As we have demonstrated today, we are prepared to cooperate with this body as well. I would anticipate that this subcommittee will conclude that local regulation facilitates the

flow of consumer information and that the state insurance departments are particularly sensitive to such matters.

From the insurance agent's perspective, however, the question of who sets rates, handles consumer complaints or deals with insolvencies, has very little to do with our obligation to provide customers with adequate information. This is our responsibility. It is our business.

Thank you for letting me report.

[The statement of Mr. Patterson follows:]

STATEMENT OF FRANK J. PATTERSON, REPRESENTING THE INDEPENDENT INSURANCE AGENTS OF AMERICA, INC.

Good morning Mr. Chairman. My name is Frank J. Patterson. I am President of Patterson & Associates, Inc., an insurance agency located in Chevy Chase, Maryland. We sell and service a full range of personal and business insurance. We maintain contractual relations with a number of insurance companies, permitting us to best represent our customers by matching them with the company and policy that best serves their needs.

I am here today in my capacity as Chairman of the Federal Affairs Committee of the Independent Insurance Agents of America, Inc. IIAA is the nation's largest independent producers association representing more than 220,000 agents and their employees. Its members offer all lines of insurance—property, casualty, life and health. With me is Lawrence R. Herman, Director of Congressional Relations for IIAA.

Mr. Chairman, on behalf of myself and IIAA, I welcome the opportunity to participate in these hearings addressing the McCarran-Ferguson Act and competition in the insurance industry. I understand that you want to examine today consumer information in the insurance marketplace. I would like to make some preliminary remarks concerning the regulation of insurance and the industry's limited immunity from the Federal antitrust laws, and then turn to some specifics about consumer information.

The McCarran-Ferguson Act explicitly precludes the application of the Sherman, Clayton, FTC, and Robinson-Patman Acts to the business of insurance—with the exception that the industry is subject to the anti boycott, coercion and intimidation rules of the Sherman Act. The continued taxation and regulation of insurance by the several States is extolled as being "in the public interest." While the Act entrusts the business of insurance to state regulation it does reserve to the U.S. Congress the right to enact legislation specifically relating to the business of insurance—a right that it has indeed exercised on occasion.

We strongly agree, both as a matter of principle, and based upon well over a century of experience, that state regulation is most compatible with the public interest and most suitable to the types of regulatory issues associated with insurance, such as rate-making, insolvencies and claims' practices. Furthermore, we believe that the limited federal antitrust immunity has permitted this unique business to function at peak efficiency, enhancing competition and reducing expenses and consumer costs as well. We believe that the elimination of this immunity would have the effect of curtailing insurance industry competition.

I would be happy to respond in more depth to any questions that you, or your colleagues, may have on these matters at the conclusion of my statement, but for the moment I shall turn to the specific questions you have posed to us concerning consumer information.

In your letter of invitation you observed: "As an independent insurance agent, who deals directly with policyholders, you are in a unique position to comment on information needed by consumers and the ease with which they can obtain that information." I couldn't agree more. Independent insurance agents are, in an important respect, consumer representatives, and, our livelihoods depend upon our ability to effectively respond to the insurance needs of our clients—to answer their questions and work with them to tailor a policy that best serves them.

As to the availability of such information—it is abundant. I distributed, along with my prepared statement, examples of the type of information, geared specifically to the average consumer, that is made available to the public by IIAA, and by individual insurance agents and companies.

Is it relevant? Judge for yourself. One covers automobile, homeowners and renters insurance. It explains in lay terms the various forms of coverage available to the

consumer: automobile collision coverage, the 80% rule with respect to homeowners coverage, special options available to suit a particular client's needs.

Similar pamphlets are made available by all the companies that we represent. Here are just a few that I brought with me. While none of them could enable consumers to become do-it-yourself underwriters, they adequately inform buyers of what to look for, what questions to ask, and most importantly, what to expect from their agent and company. The independent insurance agent must be far more than a mere intermediary, processing insurance applications. Independent insurance agents should and do provide the insurance buying public professional and practical advice to assist consumers in determining what coverage is right for them, and to place that coverage with the most appropriate insurance company available.

Purchasing insurance is not like buying a loaf of bread. It is more than a list of ingredients—policy terms—stamping an expiration date, and setting a price. Depending on one's economic circumstances, a particular automobile policyholder may be wise to absorb a high deductible at the front end, and add a high level of catastrophic, umbrella coverage at the back end. Another individual may think himself adequately insured with a minimum, low-priced policy, even though he could seriously jeopardize his personal assets should an accident occur.

It is our responsibility, our duty, to discuss these factors and others with our clients. We are after all fiduciaries, both before the law and more importantly, before our customers. We are in a position of trust and we hold ourselves out to be responsible for providing the best coverage available for our clients. If we fall short of fullfiling our customers legitimate expectations we can find ourselves liable before the law, and, more importantly, before our clients.

As to your inquiries concerning specific types of information such as company loss ratios, insolvency, rating practices, etc, I'm simply not sure how you want them addressed. There are no pat, universal answers. Reliable information is today available to the agent and to the consumer. If asked, I could explain to any given customer loss ratios, soft markets, underwriting criteria, claims handling practices, etc. But, the average consumer is not at all interested in most of these technical details. In fact, I would suspect the bored and irritated consumer would pick himself up and walk next door to my competitor should I engage in such a learned discourse.

In a nutshell, while we do indeed have much information available for our customers, people do not walk into my agency expecting to find a public library. My colleagues and I are well prepared to respond to any of our customers questions—from the most mundane to the most technical—and to volunteer information essential to serving our clients interests.

There are many areas of legitimate consumer concern that should be explained to the client. A policyholder has a right to expect prompt claims handling from his company. A policyholder has the right to expect a competitive premium rate. He certainly has the right—and the responsibility—to know what his policy coverage includes and what it excludes.

Agents and companies have ample incentive to meet these needs. An agent is a professional, a fiduciary and often a friend. He is also a businessman, working within one of the most competitive industries in the country. If his customers aren't satisfied with his service, policy coverage, or answers to his questions, there are plenty of other agents to fill this deficiency. We are motivated to keep our customers and to keep them satisfied. We certainly do monitor the claims handling practices of our companies, and if they prove to be slow and unreliable, we will not hesitate to terminate our contracts with them and place our customer's business elsewhere.

In closing, I would like to say that IIAA has been cooperating with the FTC in its investigation of the adequency of consumer insurance information. As we have demonstrated today, we are prepared to cooperate with this body as well, although the two inquiries at times appear redundant. I would anticipate that this subcommittee will conclude that local regulation facilitates the flow of consumer information and that the State insurance departments are particularly sensitive to such matters. From the insurance agent's perspective, however, the question of *who* sets rates, handles consumer complaints or deals with insolvencies has very little to do with our obligation to provide customers with adequate information. That is our responsibility. It is our business.

Thank you again for providing us with this opportunity to address the subcommittee.

Chairman RODINO. Thank you. Mr. Ream.

Mr. REAM. Mr. Chairman, and members of the subcommittee, I'm David L. Ream, president of L.F. Ream, Inc., an insurance

agency in Cleveland, OH. I am director of the National Association of Professional Insurance Agents and chair PIA's Public Information and Public Affairs Committee.

The National Association of Professional Insurance Agents is a trade organization representing over 40,000 independent insurance agents from every State and territory in our country. These members are agency principals, small businessmen, that typically oversee an agency staff of five and specialize in personal lines of property and casualty insurance.

In our modern society, most people have a rudimentary understanding of insurance, coupled with the competitive sales effort on the part of agencies and the national advertising programs of insurance companies, and we find today a public that is very aware of both the availability and desirability of insurance. Furthermore, not a month goes by that some newspaper or magazine doesn't contain an article on personal insurance. In many jurisdictions, we also find active programs on the part of the department of insurance to make consumers in their States more knowledgeable about insurance. Add to these information outlets, the fallout of the seventies' age of consumerism.

Three principles have become engrained in the consumer's buying habits, and they are: shop around, ask questions, and if you're dissatisfied, complain. As an agent, I can attest to the fact that people do shop. As evidence, you only need to sit in an agent's office and see how much time is devoted to quotations. Rare is a quote given that is not accompanied by some consultation. Not every proposal is accepted, but the free information and advice garnered by the consumers, assist them in gaining a better understanding of the product, the price and their insurance needs.

The public does shop. Agents are judged and wish to be judged on the completeness of their underwriting interview; knowledge of the marketplace and technical aspects of the product; and the ability to clearly communicate that to the consumer, either orally or with printed material, if the client so wishes. Consumers do not hesitate to use the Yellow Pages or ask neighbors, friends or relatives about insurance needs.

Comparing notes with others is a major tool used by consumers when shopping and/or determining if they're getting their money's worth in service. If the current producing agent or insurer isn't providing adequate claim service, keeping abreast with the client's changing insurance needs and offering a total package, which is both service and product, at a competitive price, the business will leave. Additionally, there are sufficient numbers of competitors in this industry. Even if the consumer hasn't thought of comparing insurance programs, there's certainly an agent willing to suggest that he can do it better.

So we have consumer shopping. We have information readily available from local sources. We have insurance counseling given, whether or not a policy is sold. We have word-of-mouth comparisons with people the consumer knows and trusts, and we have insurance competitors constantly soliciting new business. The result is an informal but very effective system of checks and balances. This has developed a highly competitive system with a vast array

of products, prices and services to fit each and every consumer need.

To specifically respond to the several items identified in the subcommittee's letter, we present the following:

Coverage. Upon request, there's sufficient wealth of information explaining auto and property coverages. Care has been taken to make the information understandable to the general public. And I can provide the subcommittee this morning with information readily available in my office, and I have it with me here this morning.

[Material on file with the subcommittee.]

Cost. Some have suggested the issuance of a price list. This actually could be a disservice to the public, for the following reasons:

One, rates change on an as-needed basis. This creates a timeliness problem with printed material.

Two, there are so many different rate combinations, practicality and cost dictate that average class be used. Insurer A may be very competitive in this average class, but not competitive in all other classes. Therefore, the information can very easily be misleading.

Three, cost comparisons don't take into account the differences in safe driver point charges, limit aggregates, primacy of medical coverages and other technical differences.

Four, these lists do not take into account service levels and solvency.

PIA firmly believes that you should teach the consumer how to shop, not do the shopping for him.

Service. Community sharing of information, which we've identified earlier, and a very active marketplace are most effective. Attempting to evaluate service is very difficult. One person's acceptable level of service is another's complaint. The freedom of the client to move his business when he wants is an excellent incentive to good service.

Payout ratios, rates of return, insolvency. The real question is, can you conceive a way of developing literature that would be both timely and understood by the public? We think not. These things are reviewed by the insurance regulators overseeing the ratemaking process. They have both the technical expertise and the public responsibility to do so, and we believe that's where the responsibility should lie.

Agents' commissions. Agents' commissions are a part of the price as stated. If the customer doesn't feel the complete package, which is service and the product, is satisfactory and at an acceptable price, he will go elsewhere. Segregating an agent's commission does not benefit this process.

In closing, we have provided you with a kit of the many consumer information activities in which PIA and our individual agent members participate: public service programs, such as our drunk driving and anti-arson efforts; programs and materials geared for our members to use in their communities, such as with high school students; information pieces made available to the general media, such as our consumer columns; experimental forums improving the insurance industry's response to consumers, such as ICAP, as well as many others, are evidence of the depth of commitment PIA and its members have to educating the public about insurance.

[Material on file with the subcommittee.]

Thank you for the opportunity to express our members' views, and we welcome your questions and comments.

[The statement of Mr. Ream follows:]

STATEMENT BY DAVID REAM, CIC, FMS, CHAIRMAN, PUBLIC INFORMATION AND AFFAIRS COMMITTEE OF THE NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS

The following statement is submitted to the Subcommittee on Monopolies and Commercial Law of the Committee on the Judiciary by the National Association of Professional Insurance Agents (PIA).

PIA is a national trade association representing more than 40,000 independent property and casualty insurance agents in all 50 states, the District of Columbia, Puerto Rico and the U.S. Virgin Islands.

The members of PIA are generally small independent business persons who are primarily the principals in their agency. They earn their living by obtaining appropriate insurance coverage to meet the needs of their clients from the several insurance companies for which they produce and are compensated on a commission basis. Independent agents are licensed and regulated by state insurance authorities.

PIA willingly accepted the Subcommittee's invitation to discuss the insurance information environment and how it meets the needs of the buying public for personal lines purchases. Our submission will consist of three sections. Presented first is an outline of the typical functions performed by our agent/members. This will be followed by a description of how most consumers approach the purchase of personal lines products, based upon our experience. Concluding will be a discussion of what materials are available, including projects PIA has undertaken.

The insurance products we offer are purchased on the strength of their protection, quality of service and competitive price. PIA members provide a wide range of services and access to the full scope of insurance markets, given the specific needs of our clients. This may include some or all of the following:

Interview—Conduct a detailed initial interview to determine the type and extent of a client's insurance exposure. This can include physical inspections of the property in question, taking pictures and noting particulars/valuables. For auto insurance, the consumer is asked driving record, particulars of driving habits and details of the car.

Coverage—Next, the coverage options are discussed. This includes a review of possible deductibles, coverages, policy packaging and limits to identify the appropriate response to the individual's needs/wants.

Search—Next, the agent turns to the companies he represents to secure an insurance package to the specifications requested by the client. Agents are always aware of the price competitiveness of their companies. In most instances, he can quickly determine the corresponding coverage needs with a competitive price. However, this market search may take the agent beyond the markets he has readily available in his agency to other carriers, insurance plans, or specialty markets. Generally speaking, no matter what the risk, our agent-members can find a market, hopefully at a price acceptable to the client.

Placement—When the quotations are secured, the agent informs the client of the choices, noting price, coverage, exceptions and obligations. The client makes his decision. The agent issues the policy(ies); bills and collects the premium on behalf of the company; or completes a formal application (binding coverage, in most instances), collects the correct premium from the client and forwards both to the company for processing.

Maintenance—During the policy term, changes, additions or deletions may occur. The client need only advise his PIA agent who will complete the necessary forms and calculate any change in cost. Prior to renewal, our member will review the insurance program with his client to be sure that the coverage is still appropriate. Changes in the policy in question may be necessary for the coming policy period or additional policies might be necessary/suggested, e.g., personal umbrella policy or recreational vehicle coverage.

Claims—In the event a loss occurs, the client calls upon his agent. Our members take the claim information, determine if the loss is covered (if possible), give preliminary instructions to the client, and inform the company. Most of our agent-members have authority to settle many property claims. This may require the assignment of an in-house claims adjustor or the contracting of an independent one. It may be as easy as instructing the client to have the minor damage repaired and the

resulting bill forwarded to the agency for payment on the company's behalf. During the claim settlement process, our agents are in constant communication with the client and company. This may include prodding along the claim's process/payment; or expressing the client's concerns/dissatisfaction.

There are a number of other functions PIA members provide for their clients. The aforementioned are the rock-bed of the insurance process. Not all agents provide all these services nor do all clients need the full range of each of these services. However, in an open and free competitive insurance market, a consumer can pick and choose; compare and contrast the service he is or is not receiving from his insurance agent/company. The consumer is not tied to a particular agent/company. He can and does pick up his business and leave when the price and service is unacceptable to him.

The people PIA agent-members serve run the full gamut. From the sixteen-year-old who needs insurance to drive, to the leading married corporate executive, our customers include all economic levels, ages, educational backgrounds, and residential areas (rural, suburban and urban). These various elements combine to from an endless array of insurance needs and differing approaches to insurance purchasing.

The age of consumerism and the efforts of its spokespersons has left its mark on the buying public. The success of *Consumer Reports* and other like publications is evidence of the public's desire to become informed as to the various purchases they make. Regardless of the product, three practices are followed by consumers when buying a product/service: shop around, ask questions and complain when unhappy with the results.

Make no mistake, insurance purchases are subjected to these three principles, as well. Our industry has been and is highly competitive. Here are some 1,600+ life and health carriers, 2,600+ property/casualty insurers and hundreds of thousands of insurance agents. The agents associations testifying today represent over 200,000 agents. This does not include the agency force of noted carriers such as State Farm, Nationwide or Allstate, three prominent carriers in the personal lines area.

Market participants at all these levels come and go. The objective of each of these entities is to develop a thriving, profitable business. You can only accomplish this by offering the public what it wants/needs. The number of competitors, and ease with which the consumer can move his insurance business, has always fostered competition in this industry.

How a consumer approaches insurance purchases depends greatly on their needs, level of sophistication and personal initiative in wanting to be informed. Most people's first experience with insurance is when they first get their driver's license and/or purchase their first car. As you study for your license, you learn from the state that you will be required to have insurance or evidence of financial responsibility, set at specific levels by state law. Parents know through their own experience with the liability requirements that society/courts place upon them and by the questions asked by their agent/company when securing their own automobile insurance (How many drivers in the household? Do you have any teenagers, and their ages?) that adding the youthful driver to the family policy is the first step. Depending on the circumstances of the teenager (living at home; own car with possible loan; driver education course, etc.), the agent can advise his parent client what alternative is best, with respect to price, liability exposure, and terms of the car loan, if applicable.

It is common for this price quote to shock most parents. People underestimate the cost of risk associated with the inexperienced, youthful operator. Be assured that parents readily inform their teenagers of this cost. The jolt, alone, sends many consumers price-shopping. With policy in hand or with the requirements of state law and loan obligation, they turn to the yellow pages and neighbors for agents and/or carriers to call. To verify this, you need only sit in an agent's office to see how much time is spent in giving price quotes. The person calls and requests a quote on auto insurance. The agent asks the particulars and furnishes a price. In most insurance purchases for personal lines, price is the—or one of the—major consideration(s). If the quote isn't competitive, the agent isn't going to secure the business. TV advertising by insurance carriers encouraging people to "Come on in and compare prices" has aided this natural consumer behavior to shop. These ads are generally keyed to highly visable programs to maximize consumer exposure, e.g., Monday Night Football, the Olympic Games, etc.

As we mature and participate more fully in society, our need for insurance changes. We take on more responsibility; own more things; and are exposed to a greater liability for our actions. From the very beginning, consumers are taught that insurance is purchased to assure financial security in the event of loss. That is communicated by the state, driver education courses, as aforementioned, and by

lenders who require some form of financial assurance when making loans on real and personal property. This is further explained by the agent when collecting the information necessary to "underwrite" (determine) the appropriate coverage. The client may come in with a preconceived notion of what coverage and limits he wants. However, during the underwriting interview the agent may surface additional insurance needs of which the client was unaware.

It is at this point that consumers realize price is important, but it is not the be-all-to-end-all. Being properly covered with the right policy and limits for your individual insurance needs is more important. Additionally, having someone who knows the insurance business and how its many product offerings respond to your needs is of great value.

Today we live in a world of abundance, with information and changing technology. It's hard enough keeping abreast of our own profession's needs, much less attempt to completely master an understanding of each product/service and its respective industry we will need throughout our life. While the consumer of today is better informed than the buyer of 20 years ago, most people still depend on professionals in a given field to expand on the rudimentary knowledge a consumer has acquired about a particular product/service.

This is the vital role filled by PIA agent-members. Our knowledge and expertise are given freely upon the request of our clients and potential insureds. Not every proposal is accepted, but that uncompensated advice benefits the consumer by providing a better understanding of the product, price or individual exposure to loss.

Agents are judged and wish to be judged on the completeness of their underwriting interview; knowledge of the marketplace and technical aspects of the product; and ability to clearly/understandably communicate that to the consumer. Price isn't the only thing upon which agents compete. If a client doesn't feel an agent has satisfactorily served his needs, there are hundreds of agents standing in the wings. Also, agents do not sit in their offices and wait for business to come to them, they go out and solicit. If an insured—on his own—hasn't considered shopping the market, there are many agents who will contact him and suggest that the consumer give him (the agent) a crack at the client's business. If the current producing agent isn't providing acceptable claim service; keeping abreast of his client's changing insurance needs; and offering the total package (service and product) at a competitive price, he will eventually see his clients leave.

The same is true for carriers, whether or not they are represented by our agent-members. If a client is dissatisfied with a particular carrier, the independent agent has the advantage of being able to shift the business to a more acceptable carrier upon the client's request. With or without an independent agent, consumers will change carriers if dissatisfied.

Similarly, if a carrier is providing poor service, and/or pricing itself too high above other companies represented by the independent agent, our members will not direct any new business to that carrier. Routinely, all agents will discuss these problems with the company's field representative in the hope of resolving them. If the improvements are not forthcoming or are minimal, an independent agent may consider moving the book of business to a more satisfactory carrier and/or terminating his representation of that insurer. The independent agent has this flexibility and duty to maintain quality companies because he is an independent contractor responsible for successfully operating his own small business which is an insurance agency. His economic success depends on his ability and his carrier's ability to deliver.

Likewise, insurance companies have a vested interest in seeing that they do a quality job so that: the public will view them positively and/or they (insurers) will attract and maintain quality agents. If a company is dissatisfied with an agent's performance, they have a great deal of latitude in remedying the situation. They can offer rehabilitation/retraining programs or, in more severe cases, unilaterally terminate the relationship.

The most important element of service is the claims settlement. If a company and/or agent does not handle this function (the actual product for which you purchase insurance) to the satisfaction of the insured, no amount of price competitiveness, technical knowledge or long-term good-ole-boy relationship will weather the storm. The client will be gone in a shot.

Clients must know what to expect from the policy they choose. This is why agents take the time to explain policy options to insureds. To facilitate this, we have encouraged our carriers to issue policies in plain language. PIA was a member of the NAIC Property/Casualty Readability Advisory Committee which developed a model governing the requirements of plain English policies. Despite the legal problems of

interpretation that had to be overcome, most carriers issue personal auto and property policies in readable form.

Prompt and courteous service is essential during a claim. Clients are generally upset in a claim situation, no matter how small. Agents must be sensitive to this. Additionally, incorrect instructions, lack of timeliness in communicating the loss to the carrier, and incomplete information can needlessly increase the insured's loss/liability in the matter. This could result in: a loss of the customer; perhaps a termination of the company contract; and/or a lawsuit against the agent. Agents are legally accountable for the errors and omissions they make. So there is not only a competitive incentive to "do things right," there is a legal one, as well.

Just as in selecting a lawyer or doctor, a consumer uses a number of avenues. The yellow pages has already been mentioned. However, consumers do not hesitate to ask their neighbors and friends or have advice volunteered by acquaintances regarding similar loss situations and what transpired. Comparing notes with others is a major tool used by consumers when shopping and/or determining if you're getting your money's worth.

"Who's your agent?" "What insurance company are you with?" "What kind of coverage do you have?" "How much are you paying?" "Are you satisfied with your agent?" "Ever had a loss? What happened?" These are the questions consumers ask each other to supplement the information they get from other sources.

Reputation is paramount in this industry. PIA agents are active members of their community, in part to promote their business profile. However, you must earn a good reputation to go along with that visibility in order to prosper. Word carriers fast in rural and suburban communities.

So, we see that competition among insurance industry participants (agents and companies), and general principles of consumer shopping, result in a highly competitive and mobile insurance market. In property/casualty, most people purchase their first insurance policy because of requirements set by the state or lenders. There is a basic understanding of what insurance does because of its 200+ years as a part of our society. Insureds sharpen their consumer insurance skills as they take on more responsibility in society. Most consumers choose the services of an agent to provide the more indepth knowledge of the market and product. The agent has a profit and legal incentive to do things right.

And, on top of all this is a state legislative/regulatory system to ensure the proper functioning of this industry.

Consumer information is very much a marketing tool in our industry. It does a company and agent well to be able to provide printed materials to supplement the insurance conseling they do for individual insureds. Additionally, as we stated in our discussions of claims, it is best if consumers have an acceptable level of understanding of just how the insurance product works. This lessens unrealistic expectations at the time a claim occurs.

Companies make materials available directly to consumer groups, educators and media, upon request, and to individual clients by enclosure in billing/policy mailings.

The greatest source of information is the agent. Our agent members get information from many of their carriers; answer the questions of clients who receive direct company mailings; may make their own client mailings; work with local schools and educators to bring the insurance concept and necessary shopping skills to high school students; and contact local media people, when appropriate.

The information can concern a specific company product, or provide generic information on insurance and/or a particular coverage. There are information pieces that compare and contrast different forms of coverage, such as the various forms of homeowners insurance.

Many school districts have "preparing for life" classes, where high school students learn the demands society will make on them upon graduation. Part of these courses deals with insurance.

Consumer publications and writers regularly address insurance issues. Hardly a month goes by when some widely-read publication, such as *Glamour, GQ, Working Woman,* airline magazines, local and syndicated columnists will publish an article on what life, auto, or property insurance to buy. There are a number of books available, as well.

Insurance trade associations have a number of information projects, also. PIA has a long established history of active participation in consumer information. We have worked with insurance regulators and insurers in developing the appropriate consumer affairs response to the public's need to know and seek satisfaction for complaints. Our sponsorship of the Insurance Consumer Action Panel (ICAP) was such an undertaking.

PIA issues a number of informational pieces for use by general media (*News for the Insurance Consumer*). We have designed materials for our agent-members, in conjunction with their community educational efforts or for their individual clients (Agency Impact Kit).

PIA has produced several films, informing the public about critical adverse social patterns that can affect their lives and insurance costs. Our drunk driving film has been aired on *210* PBS stations, and 190 newspapers across the U.S. We are active participants in passive restraints, child restraints, anti-drunk driving efforts, auto safety and anti-arson at the federal, state and local levels. All these PIA efforts are enhanced by the efforts of our state/regional affiliates and individual members.

Appropriate educational requirements for persons prior to securing an agent's license and follow-up education courses throughout their professional career are provisions PIA has supported for years. Consumers and society are best served by knowledgeable insurance agents.

From time to time, state insurance departments issue consumer information. PIA state/regional affiliates receive copies of these pieces, making them available to individual agent members.

To PIA, the important element is to teach consumers how to shop and make them aware that service, and appropriate coverage is more important than obtaining the lowest price. In the long term, a consumer is ill served by sacrificing coverage and service for a few dollars' difference.

Because there are so many combinations of consumer insurance needs, price lists are actually a disservice to consumers. Insurance rates change as need arises. The problem of keeping up-to-date information before the public is very real. Price quotes take "an average class" and rate (price) it. Most people do not fall into the selected class. A company could be quite competitive in the class published, but not so in the class that corresponds to your needs. Unwittingly, you may decide the price list did your shopping for you, choose the lowest priced company for the class listed, and eventually find out that, indeed, another company is offering more competitive rates for your needs. Price comparisons also ignore such essential differences as:

a. Standard liability coverages versus named driver's only options;
b. Single limits versus traditional approaches;
c. Primacy of medical coverage;
d. Differences in the various point charges for accidents/violation;
e. Differences in the increased factors for increased coverage limits; and
f. Package approaches to personal lines.

Some have suggested that price information should distinguish the agent's commission from the balance of the premium. Information on commissions is not readily available to the public and its need is questionable.

Consumers price shop and service shop. Knowing how much an agent earns will not change this. If the service and price is acceptable, the insured secures the policy and continues to renew same. If some company without an agent can do it better, the consumer will seek out the insurer. We need only to look at GEICO's success in meeting the needs of certain insurance buyers.

In conclusion, PIA can attest to the highly competitive nature of our business and a rather high level of understanding of the insurance product by the public. Various forms of consumer information are readily available from many sources. Members of the insurance industry reach out to inform the public at a regular basis, both nationally and locally.

We will provide a sample of these materials and information efforts to the Subcommittee. Additional copies of specific items will be made available, upon your request.

PIA thanks you for this opportunity to express our views and will be glad to answer your questions and receive your comments.

Chairman RODINO. Mr. Pierce.

Mr. PIERCE. Thank you, Mr. Chairman. I appreciate the opportunity to be here. My name is Robert Pierce. I am a life insurance agent from Tigard, OR. When I received your invitation, I was after the deadline; therefore, we have not prepared a written statement, and would request that we could submit one within 30 days.

Chairman RODINO. How about doing it sooner? Would it take you 30 days?

Mr. PIERCE. All right. We'll have it sooner. [Laughter.]

Chairman RODINO. Can you do it within the week? Next week?
Mr. PIERCE. Yes.
Chairman RODINO. Thank you.
Mr. Pierce's prepared statement was subsequently submitted for the Record].
Mr. PIERCE. I represent the National Association of Life Underwriters. I am a member of the national board of trustees of that organization. NALU is a federation of over 1,000 State and local associations which represent approximately 130,000 members. Our members market life and health insurance.

I believe that I'm typical of the members of our association, and I'd like to address three specific areas, though your invitation covers a very broad area: competition in the marketplace, compensation and public information.

Your panel is certainly going to have a difficult time with the volume of information you're receiving, but I believe that it's important that we look at this volume of material because it's what the consumer also is faced with.

I represent approximately 600 clients in the area in which I do business. During the course of a year I have business contacts with approximately 1,000 others. The business that we represent is more competitive and has more product availability and more in-depth information at this time than it ever has before. I've been in this business for 18 years, and I see a continuous trend toward the consumer being better served than in the past.

My particular responsibilities are to help individuals solve problems and in many cases help them discover problems they were not aware of and then find solutions that fit their circumstances.

I've heard it said and it's been said here today that there is an incentive for an agent to sell permanent insurance instead of term insurance. I find that that's not the case in the real world. 80 percent of the business that I place is term insurance. There is an incentive to build a clientele relationship, and by doing the proper job for my clients, I will remain in a position to take care of all of their future insurance needs in the areas that I market, as opposed to just dealing with them one time and then having them go elsewhere. That is where the real value of our service lies.

Recently, I had an opportunity to establish $100,000 in term insurance on a young couple in their early thirties. I was quite impressed by the fact that this young couple had read magazine articles, newspaper articles, listened to some radio or TV exposure, which they described to me, and then personally called over 20 life insurance offices to obtain the information on the lowest cost term insurance that they could obtain. I did agree that term insurance was the proper plan for their circumstance at this point. I think that shows that this certainly is not a noncompetitive industry. This is an industry where the only way that we can readily do business is by doing a thorough job and representing companies that are price competitive.

The National Association of Life Underwriters recently cosponsored grants to Dr. Larry Crosby, Ph.D., to do a study in conjunction with the University of Nebraska and the University of Arizona of consumer attitudes toward whole life. This was an extremely

well-planned study that we feel represents the unbiased sampling of over 2,000 respondents to the survey.

The findings of that survey, as recently published, are primarily that consumers who own whole life are aware of the strengths and the weaknesses of that product; and that the majority of them are pleased and satisfied with that product.

I would like to submit, at the same time we submit our statement, the published findings of that survey.

[Material submitted with statement:]

Yesterday, Mr. Chairman, I spoke with a client of mine who is an engineer and told him I would be coming to Washington and the purpose of the trip. This man owns five policies that I have established for him plus three others that had been established prior to my developing a relationship with him.

His statement was, "You tell the committee that no other area that I do business in provides more information to help me decide than the life insurance industry." I thought that that was an interesting piece of input from the consumer that we are trying to serve.

On compensation, on which your letter asked us to comment, Mr. Chairman, we frequently hear it said that the incentive to sell whole life is high and that commission rates are too high. A survey recently showed that the average length of time that a whole life policy stays in force is approximately 17 years and that the agent's commission on the premiums paid over that period of time represents approximately 6 percent of the premiums paid. That commission is paid, not at once, but stretched out over a 10-year time period. That does not seem out of line with the types of charges that are incurred in other product lines.

NALU provides a number of consumer services. One such program is referred to as the SCHIC Program. That stands for senior citizens health insurance counseling.

It is a program which in some States is conducted in conjunction with the insurance commissioner's office; in other States it's purely a public service project of life underwriters. We provide service and counseling through senior citizens' groups so they may properly understand and evaluate, on a nonprofit basis, Medicare supplements and the type of insurance programs that they should be considering.

Another area is in consumer education. Through our local associations, we serve high school education programs. There are hundreds of thousands of pieces of material per year concerning education on property and casualty, life and health insurance that are distributed to high school classes through our organization to help them become better informed about insurance.

I have found in my small community of Tigard, OR, that a large number of young people ask me to help them by letting them interview me as to insurance products and the industry, information that in the past probably was never available to the consumer; but through many such means the consumer is undoubtedly better informed now than in the past.

Another area that our association works actively in is continuing education training for our membership. We feel it's important that

our members be well qualified and competent to help the consumer with life insurance decisions.

Through the Life Underwriter Training Council, a designation is available after pursuing a 4-year educational process; and, of course, the Chartered Life Underwriter designation is available through The American College, and there are considerable training opportunities available through local and State associations.

We also have a requirement that all of our members must within the first 4 years of membership fulfill a continuing education requirement as a minimum to maintain membership; and we also support mandatory continuing education legislation in the States. My home State of Oregon is one of those that has a very rigid continuing education program which was supported by the Life Underwriters.

The result of that is, again, to provide a well-informed and competent sales organization so that the consumer will be better served.

Materials that we have available for the consumer include, just to name a few, some guidelines for deciding what kind of life insurance is the best buy; a Consumers' Guide to Life Insurance; "Your Life Underwriter and You;" "Plain Talk About Your Life Insurance Policy;" and several others here that I would like to submit for the record, Mr. Chairman.

[Materials on file with the subcommittee.]

I appreciate the opportunity to make this statement to you today. Thank you.

[Statement of Mr. Pierce follows:]

STATEMENT OF ROBERT A. PIERCE, CLU, THE NATIONAL ASSOCIATION OF LIFE UNDERWRITERS

Mr. Chairman, your letter inviting me to testify today stated that, as an agent who deals directly with policyholders, I might be in a unique position to comment on certain matters to be considered by your Subcommittee.

I have been a life insurance agent in the State of Oregon for the past 18 years. On the basis of that experience, I would agree that I am in a position to bring to your Subcommittee a viewpoint that might be unavailable from other sources.

Moreover, I speak today not only on the basis of my own personal experience, but as the representative of The National Association of Life Underwriters, an organization in which I have been an active participant for 18 years at the local, state and and national levels. I am currently a member of the NALU national Board of Trustees, and would point out for your information that NALU's affiliated state and local associations currently have a membership consisting of almost 130,000 men and women in every state whose business is life insurance sales.

Your letter of April 30, Mr. Chairman, said that the Subcommittee will examine the types of information that are important to individual buyers of insurance. That is the topic I feel qualified to address, because I talk about life insurance with about 1000 consumers each year; I think this has given me an appreciation of the things people really want to know about life insurance.

But since this series of hearings also seems to encompass virtually all aspects of the life, health, and property and casualty insurance business, there are obviously many matters contemplated by your letter to me of April 30 on which field sales people will not feel qualified to speak. For example, the actuarial and investment aspects of comparative costs, rates of return, and the technicalities of payout ratios and insurer solvency would be among these.

However, as I indicated, there are certain subjects in your letter of invitation that we do feel qualified to address. Chief among them are these:

I. CONSUMER INFORMATION

I believe the way in which I might be most helpful to your Subcommittee is to outline for you the types of information that I have found to be important to life insurance buyers and to comment from a field point of view on the availability of that information. (I believe my own experience to be typical of the kind of life insurance agent who is affiliated with our Association.)

In Oregon, where I live and work, I am required to deliver to each policyholder certain documents required by the Oregon Insurance Commissioner; these have been adopted for Oregon pursuant to the recommendation of the National Association of Insurance Commissioners.

One of these documents is a Policy Summary, which is a written statement describing the elements of the actual policy I have sold the applicant. This summary contains detailed information about the policy. For example, it sets forth, among other things, for the first five years of the policy and for representative years thereafter, the premiums payable, the guaranteed amounts payable upon death, the total guaranteed cash values, and cash dividends payable under the policy. The Policy Summary also contains life insurance cost indexes, as required by the Oregon regulation.

The other document required by the Oregon regulation (and by the regulations of about 36 other states) is a Life Insurance Buyers' Guide. This guide—also advocated by the NAIC—is designed to help consumers decide how much life insurance to buy, the kind of insurance to buy, and how to compare life insurance costs. It is written in layman's language, telling potential buyers the differences among the various kinds of life insurance, and helping them to find a low cost policy.

For the information of the Subcommittee, I am enclosing copies of the form of these two documents, identifying them as Attachment "A".

In addition to the two pieces of information just described, agents commonly provide prospective buyers of life insurance with ledger statements and computer printouts that are designed to inform the prospect in greater detail as to the costs and benefits of the policy or policies under consideration, year by year. For further information and benefit of the Subcommittee, I am including examples of such documents with my statement, identifying them as Attachment "B".

Nor are the documents specifically relating to particular policies the only life insurance information consumers receive. The National Association of Life Underwriters believes that an improved climate for the purchase of life insurance can be created only to the extent that the public understands and appreciates the role of life insurance in their lives and the function of the agent in providing life insurance service for them.

Therefore our association has produced a number of publications designed to enhance the public's knowledge of life insurance and those who sell it. To give your Subcommittee a more complete picture of the aggregate of life insurance information that is available to consumers, I am including copies of some of these publications as Attachment "C" to this statement.

[Material on file with the subcommittee.]

Scores of thousands of copies of this and similar consumer information are distributed annually through the 130,000 members of NALU's affiliated associations and by companies directly.

It is my belief that, with the Buyers' Guide, the Policy Summary, and the ledger statements or computer printouts that agents provide, as well as the general consumer information just described, the life insurance consumer is indeed placed in a position where he can make an informed purchase decision. Moreover, the sales process being what it is, the consumer has only to ask for additional information and it will be provided. It is undoubtedly safe to say that the prospective life insurance buyer receives more and better purchase information than do the buyers of most other consumer goods and services. As evidence of this, as Attachment "D" I am including an Executive Summary of a recent survey of consumer attitude toward the whole life insurance they have already purchased, which indicates, among other findings, that consumers, for the most part, remain satisfied with their purchases.

II. AGENTS' COMMISSIONS

In your letter to me, Mr. Chairman, you also stated that the Subcommittee desires information on agent's commissions. Although your letter did not specify exactly what kind of information the Subcommittee might desire, I will assume for purposes of this testimony that the Subcommittee would like to have some idea from me as to how agents are compensated. I welcome this opportunity, because I

believe an example of a typical agent's compensation for the sale of a whole life insurance policy will illustrate that the compensation of life insurance agents is reasonable, if that is indeed the purpose of the Subcommittee's inquiry about commissions.

The average whole life policy stays in force for approximately 17 years. Industry statistics show that among adult men, the average annual premium paid is $256. This would mean that, if the average policy were to stay in force the average length of time, a total of $4,352 in premiums would be paid.

A typical agent's contract provides for payment of a commission equal to 55% of the premium in the first year, 10% the second year, and 5% through the 10th year. The typical agent would therefore receive in commissions an amount equal to 105% of one annual premium—but only if the policy remains in force for 10 years. The total commission paid on such a policy would in that event be $269.

Therefore, the life insurance agent would receive as a commission a sum equal to 6% of the premium paid by the insured. However, as indicated, the agent would not receive this amount in a lump sum, as would be the case with most other salesmen of most other goods and services. The life insurance agent would typically have this compensation spread over a 10-year period.

Moreover, this compensation would always be subject to such adverse factors as: (1) reduction in the event of lapse of the policy during the first 10 years; (2) reduction to the extent of expenses incurred in the production and service of the policy; (3) erosion of value due to the time value of money. Obviously, any career life insurance agent's annual net income would be further substantially reduced to the extent of expenses incurred in the solicitation of business that never materializes.

The Subcommittee might also be interested in the contention that life insurance agents recommend whole life insurance over term life insurance because the commission is higher. I would offer two observations with respect to that contention: (1) in my own case, which is by no means atypical, 80% of the business I sell is term insurance. The reason for this is that there are many instances—for example young, married applicants—where term insurance, with its initially lower premiums and higher face amounts, is clearly preferable. Competent agents are trained to recognize these situations.

But industry statistics reveal that fewer than 1% of all term policies ever result in death claims. Aside from lapsation, a chief reason for this is that a great many term policies are subsequently converted to whole life policies under the option contained in most term policies to effect such conversion.

Indeed, most purchasers buy term insurance with the anticipation of converting to whole life insurance when the time is financially right to do so. The purpose of such conversion is to fix future premiums so that, unlike term insurance premiums, they will not increase. Conversion also has the effect of triggering cash value buildup and perhaps dividend payments.

Here again, in situations calling for the initial sale of term insurance, the competent agent takes care to provide convertible term insurance for his client. Then, provided the agent-insured relationship is maintained as it should be, and there is a subsequent term conversion, the converted policy will also pay a commission to the agent, so that in fact an agent can, in the long run, realize two commissions rather than one by recommending term insurance over whole life insurance. Since, as indicated earlier, the full comission on whole life insurance will not normally be realized before ten years anyway, and most term conversions occur during that time, it would often be to the agent's financial benefit to recommend convertible term insurance initially. I therefore do not subscribe to the argument that agents typically urge whole life on their clients in preference to term insurance, for the reason that often it would not be in the best interests of either the client or the agent to do so.

As to disclosure of commissions, it is my belief, Mr. Chairman, that no agent would object to disclosing commissions to a client. Certainly agents would do so on request, but they would want to do so in a full context, similar to the one I have outlined. Whether insurance agents should be singled out of all commissioned salesmen in this country, to be required to disclose their commissions on a mandatory basis as a matter of course is, I think, another matter. I would be of the opinion that, since commissions are such a small portion of the total cost of insurance, no worthy purpose would be served by mandating such disclosure.

I hope that the foregoing comments on the various kinds of information given to buyers, and on agent's commissions, will be of some value and interest to the Subcommittee. If any further information is desired, we would be happy to try to provide it.

ATTACHMENT A

**[Formerly "Life Insurance Premium Outlay Index." See 1976 NAIC Proceedings I 575]*

(G) Policy Summary. For the purposes of this regulation, Policy Summary means a written statement describing the elements of the policy including but not limited to:

1. A prominently placed title as follows: STATEMENT OF POLICY COST AND BENEFIT INFORMATION.

2. The name and address of the insurance agent, or, if no agent is involved, a statement of the procedure to be followed in order to receive responses to inquiries regarding the Policy Summary.

3. The full name and home office or administrative office address of the company in which the life insurance policy is to be or has been written.

4. The Generic Name of the basic policy and each rider.

5. The following amounts, where applicable, for the first five policy years and representative policy years thereafter sufficient to clearly illustrate the premium and benefit patterns, including, but not necessarily limited to, the years for which Life Insurance Cost Indexes are displayed and at least one age from sixty through sixty-five or maturity whichever is earlier:

   a. The annual premium for the basic policy.

   b. The annual premium for each optional rider.

   c. Guaranteed amount payable upon death, at the beginning of the policy year regardless of the cause of death other than suicide, or other specifically enumerated exclusions, which is provided by the basic policy and each optional rider, with benefits provided under the basic policy and each rider shown separately.

   d. Total guaranteed cash surrender values at the end of the year with values shown separately for the basic policy and each rider.

   e. Cash Dividends payable at the end of the year with values shown separately for the basic policy and each rider. (Dividends need not be displayed beyond the twentieth policy year.)

   f. Guaranteed endowment amounts payable under the policy which are not included under guaranteed cash surrender values above.

6. The effective policy loan annual percentage interest rate, if the policy contains this provision, specifying whether this rate is applied in advance or in arrears. If the policy loan interest rate is variable, the Policy Summary includes the maximum annual percentage rate.

7. Life Insurance Cost Indexes for ten and twenty years but in no case beyond the premium paying period. Separate indexes are displayed for the basic policy and for each optional term life insurance rider. Such indexes need not be included for optional riders which are limited to benefits such as accidental death benefits, disability waiver of premium, preliminary term life insurance coverage of less than 12 months and guaranteed insurability benefits nor for the basic policies or optional riders covering more than one life.

*8. The Equivalent Level Annual Dividend, in the case of participating policies and participating optional term life insurance riders, under the same circumstances and for the same durations at which Life Insurance Cost Indexes are displayed.

1984 GOV Competition in the Insurance Industry 739p bonknote.pdf

*[Added by 1976 NAIC Proceedings II 547 and remaining paragraphs renumbered accordingly.]

*9. A Policy Summary which includes dividends shall also include a statement that dividends are based on the company's current dividend scale and are not guaranteed in addition to a statement in close proximity to the Equivalent Level Annual Dividend as follows: An explanation of the intended une of the Equivalent Level Annual Dividend is included in the Life Insurance Buyer's Guide.

*[Amended by 1976 NAIC Proceedings II 547.]

10. A statement in close proximity to the Life Insurance Cost Indexes as follows: An explanation of the intended use of these indexes is provided in the Life Insurance Buyer's Guide.

11. The date on which the Policy Summary is prepared.

The Policy Summary must consist of a separate document. All information required to be disclosed must be set out in such a manner as to not minimize or render any portion thereof obscure. Any amounts which remain level for two or more years of the policy may be represented by a single number if it is clearly indicated what amounts are applicable for each policy year. Amounts in item 5 of this section shall be listed in total, not on a per thousand nor per unit basis. If more than one insured is covered under one policy or rider, guaranteed death benefits shall be displayed separately for each insured or for each class of insureds if death benefits do not differ within the class. Zero amounts shall be displayed as zero and shall not be displayed as a blank space.

Section 5. Disclosure Requirements.

(A) The insurer shall provide, to all prospective purchasers, a Buyer's Guide and a Policy Summary prior to accepting the applicant's initial premium or premium deposit, unless the policy for which application is made contains an unconditional refund provision of at least ten days or unless the Policy Summary contains such an unconditional refund offer, in which event the Buyer's Guide and Policy Summary must be delivered with the policy or prior to delivery of the policy.

(B) The insurer shall provide a Buyer's Guide and a Policy Summary to any prospective purchaser upon request.

(C) In the case of policies whose Equivalent Level Death Benefit does not exceed $5,000, the requirement for providing a Policy Summary will be satisfied by delivery of a written statement containing the information described in Section 4(G), items 2, 3, 4, 5a, 5b, 5c, 6, 7, 10, 11.

Section 6. General Rules.

(A) Each insurer shall maintain at its home office or principal office, a complete file containing one copy of each document authorized by the insurer for use pursuant to this regulation. Such file shall contain one copy of each authorized form for a period of three years following the date of its last authorized use.

(B) An agent shall inform the prospective purchaser, prior to commencing a life insurance sales presentation, that he is acting as a life insurance agent and inform the prospective purchaser of the full name of the insurance company which he is representing to the buyer. In sales situations in which an agent is not involved, the insurer shall identify its full name.

(C) Terms such as financial planner, investment advisor, financial consultant, or financial counseling shall not be used in such a way as to imply that the insurance agent is generally engaged in an advisory business in which compensation is unrelated to sales unless such is actually the case.

(D) Any reference to policy dividends must include a statement that dividends are not guaranteed.

(E) A system or presentation which does not recognize the time value of money through the use of appropriate interest adjustments shall not be used for comparing the cost of two or more life insurance policies. Such a system may be used for the purpose of demonstrating the cash-flow pattern of a policy if such presentation is accompanied by a statement disclosing that the presentation does not recognize that, because of interest, a dollar in the future has less value than a dollar today.

(F) A presentation of benefits shall not display guaranteed and non guaranteed benefits as a single sum unless they are shown separately in close proximity thereto.

(G) A statement regarding the use of the Life Insurance Cost Indexes shall include an explanation to the effect that the indexes are useful only for the comparison of the relative costs of two or more similar policies.

(H) A Life Insurance Cost Index which reflects dividends or an Equivalent Level Annual Dividend shall be accompanied by a statement that it is based on the company's current dividend scale and is not guaranteed.

(I) For the purposes of this regulation, the annual premium for a basic policy or rider, for which the company reserves the right to change the premium, shall be the maximum annual premium.

Section 7. Failure to Comply.

Failure of an insurer to provide or deliver a Buyer's Guide, or a Policy Summary as provided in Section 5 shall constitute an omission which misrepresents the benefits, advantages, conditions or terms of an insurance policy.

Section 8. Effective Date.

This rule shall apply to all solicitations of life insurance which commence on or after (insert a date at least six months following adoption by the regulatory authority.)

APPENDIX

Life Insurance Buyer's Guide

The face page of the Buyer's Guide shall read as follows:

Life Insurance Buyer's Guide

This guide can show you how to save money when you shop for life insurance. It helps you to:

—Decide how much life insurance you should buy,

—Decide what kind of life insurance policy you need, and

—Compare the cost of similar life insurance policies.

Prepared by the National Association of Insurance Commissioners

Reprinted by (Company Name)
(Month and year of printing)

The Buyer's Guide shall contain the following language at the bottom of page 2:

The National Association of Insurance Commissioners is an association of state insurance regulatory officials. This association helps the various Insurance Departments to coordinate insurance laws for the benefit of all consumers. You are urged to use this Guide in making a life insurance purchase.

This Guide Does Not Endorse Any Company or Policy.

The remaining text of the Buyer's Guide shall begin on page 3 as follows:

Buying Life Insurance

When you buy life insurance, you want a policy which fits your needs without costing too much. Your first step is to decide how much you need, how much you can afford to pay and the kind of policy you want. Then, find out what various companies charge for that kind of policy. You can find important differences in the cost of life insurance by using the life insurance cost indexes which are described in this guide. A good life insurance agent or company will be able and willing to help you with each of these shopping steps.

If you are going to make a good choice when you buy life insurance, you need to understand which kinds are available. If one kind does not seem to fit your needs, ask about the other kinds which are described in this guide. If you feel that you need more information than is given here, you may want to check with a life insurance agent or company or books on life insurance in your public library.

Choosing the Amount

One way to decide how much life insurance you need is to figure how much cash and income your dependents would need if you were to die. You should think of life insurance as a source of cash needed for expenses of final illnesses, paying taxes, mortgages or other debts. It can also provide income for your family's living expenses, educational costs and other future expenses. Your new policy should come as close as you can afford to making up the difference between (1) what your dependents would have if you were to die now, and (2) what they would actually need.

Choosing the Right Kind

All life insurance policies agree to pay an amount of money if you die. But all policies are not the same. There are three basic kinds of life insurance.

1. Term insurance
2. Whole life insurance
3. Endowment insurance

Remember, no matter how fancy the policy title or sales presentation might appear, all life insurance policies contain one or more of the three basic kinds. If you are confused about a policy that sounds complicated, ask the agent or company if it combines more than one kind of life insurance. The following is a brief description of the three basic kinds:

Term Insurance

Term insurance is death protection for a "term" of one or more years. Death benefits will be paid only if you die within that term of years. Term insurance generally provides the largest immediate death protection for your premium dollar.

Some term insurance policies are "renewable" for one or more additional terms even if your health has changed. Each time you renew the policy for a new term, premiums will be higher. You should check the premiums at older ages and the length of time the policy can be continued.

Some term insurance policies are also "convertible". This means that before the end of the conversion period, you may trade the term policy for a whole life or endowment insurance policy even if you are not in good health. Premiums for the new policy will be higher than you have been paying for the term insurance.

Whole Life Insurance

Whole life insurance gives death protection for as long as you live. The most common type is called "straight life" or "ordinary life" insurance, for which you pay the same premiums for as long as you live. These premiums can be several times higher than you would pay initially for the same amount of term insurance. But they are smaller than the premiums you would eventually pay if you were to keep renewing a term insurance policy until your later years.

Some whole life policies let you pay premiums for a shorter period such as 20 years, or until age 65. Premiums for these policies are higher than for ordinary life insurance since the premium payments are squeezed into a shorter period.

Although you pay higher premiums, to begin with, for whole life insurance than for term insurance, whole life insurance policies develop "cash values" which you may have if you stop paying premiums. You can generally either take the cash, or use it to buy some continuing insurance protection. Technically speaking, these values are called "nonforfeiture benefits". This refers to benefits you do not lose (or "forfeit") when you stop paying premiums. The amount of these benefits depends on the kind of policy you have, its size, and how long you have owned it.

A policy with cash values may also be used as collateral for a loan. If you borrow from the life insurance company, the rate of interest is shown in your policy. Any money which you owe on a policy loan would be deducted from the benefits if you were to die, or from the cash value if you were to stop paying premiums.

Endowment Insurance

An endowment insurance policy pays a sum or income to you - the policyholder - if you live to a certain age. If you were to die before then, the death benefit would be paid to your beneficiary. Premiums and cash values for endowment insurance are higher than for the same amount of whole life insurance. Thus endowment insurance gives you the least amount of death protection for your premium dollar.

Finding a Low Cost Policy

After you have decided which kind of life insurance fits your needs, look for a good buy. Your chances of finding a good buy are better if you use two types of index numbers that have been developed to aid in shopping for life insurance. One is called the "Surrender Cost Index" and the other is the "Net Payment Cost Index". It will be worth your time to try to understand how these indexes are used, but in any event, use them only for comparing the relative costs of similar policies. LOOK FOR POLICIES WITH LOW COST INDEX NUMBERS.

[Word "only" added by 1978 NAIC Proceedings I, after having been inadvertently left out of original draft]

What is Cost?

"Cost" is the difference between what you pay and what you get back. If you pay a premium for life insurance and get nothing back, your cost for the death protection is the premium. If you pay a premium and get something back later on, such as a cash value, your cost is smaller than the premium.

The cost of some policies can also be reduced by dividends; these are called "participating" policies. Companies may tell you what their current dividends are, but the size of future dividends is unknown today and cannot be guaranteed. Dividends actually paid are set each year by the company.

Some policies do not pay dividends. These are called "guaranteed cost" or "non participating" policies. Every feature of a guaranteed cost policy is fixed so that you know in advance what your future cost will be.

The premiums and cash values of a participating policy are guaranteed, but the dividends are not. Premiums for participating policies are typically higher than for guaranteed cost policies, but the cost to you may be higher or lower, depending on the dividends actually paid.

What Are Cost Indexes?

In order to compare the cost of policies, you need to look at:

1. Premiums
2. Cash Values
3. Dividends

Cost indexes use one or more of these factors to give you a convenient way to compare relative costs of similar policies. When you compare costs, an adjustment must be made to take into account that money is paid and received at different times. It is not enough to just add up the premiums you will pay and to subtract the cash values and dividends you expect to get back. These indexes take care of the arithmetic for you. Instead of having to add, subtract, multiply and divide many numbers yourself, you just compare the index numbers which you can get from life insurance agents and companies:

1. Life Insurance Surrender Cost Index. This index is useful if you consider the level of the cash values to be of primary importance to you. It helps you compare costs if at some future point in time, such as 10 or 20 years, you were to surrender the policy and take its cash value.

2. Life Insurance Net Payment Cost Index. This index is useful if your main concern is the benefits that are to be paid at your death and if the level of cash values is of secondary importance to you. It helps you compare costs at some future point in time, such as 10 or 20 years, if you continue paying premiums on your policy and do not take its cash value.

There is another number called the Equivalent Level Annual Dividend. It shows the part dividends play in determining the cost index of a participating policy. Adding a policy's Equivalent Level Annual Dividend to its cost index allows you to compare total costs of similar policies before deducting dividends. However, if you make any cost comparisons of a participating policy with a non participating policy, remember that the total cost of the participating policy will be reduced by dividends, but the cost of the non participating policy will not change.

How Do I Use Cost Indexes?

The most important thing to remember when using cost indexes is that a policy with a small index number is generally a better buy than a comparable policy with a larger index number. The following rules are also important:

(1) Cost comparisons should only be made between similar plans of life insurance. Similar plans are those which provide essentially the same basic benefits and require premium payments for approximately the same period of time. The closer policies are to being identical, the more reliable the cost comparison will be.

(2) Compare index numbers only for the kind of policy, for your age and for the amount you intend to buy. Since no one company offers the lowest cost for all types of insurance at all ages and for all amounts of insurance, it is important that you get the indexes for the actual policy, age and amount which you intend to buy. Just because a "Shopper's Guide" tells you that one company's policy is a good buy for a particular age and amount, you should not assume that all of that company's policies are equally good buys.

(3) Small differences in index numbers could be offset by other policy features, or differences in the quality of service you may expect from the company or its agent. Therefore, when you find small differences in cost indexes, your choice should be based on something other than cost.

(4) In any event, you will need other information on which to base your purchase decision. Be sure you can afford the premiums, and that you understand its cash values, dividends and death benefits. You should also make a judgement on how well the life insurance company or agent will provide service in the future, to you as a policyholder.

(5) These life insurance cost indexes apply to new policies and should not be used to determine whether you should drop a policy you have already owned for awhile, in favor of a new one. If such a replacement is suggested, you should ask for information from the company which issued the old policy before you take action.

Important Things To Remember - A Summary

The first decision you must make when buying a life insurance policy is choosing a policy whose benefits and premiums most closely meet your needs and ability to pay. Next, find a

policy which is also a relatively good buy. If you compare Surrender Cost Indexes and Net Payment Cost Indexes of similar competing policies, your chances of finding a relatively good buy will be better than if you do not shop. REMEMBER, LOOK FOR POLICIES WITH LOWER COST INDEX NUMBERS. A good life insurance agent can help you to choose the amount of life insurance and kind of policy you want and will give you cost indexes so that you make cost comparisons of similar policies.

Don't buy life insurance unless you intend to stick with it. A policy which is a good buy when held for 20 years can be very costly if you quit during the early years of the policy. If you surrender such a policy during the first few years, you may get little or nothing back and much of your premium may have been used for company expenses.

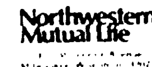
Read your new policy carefully, and ask the agent or company for an explanation of anything you do not understand. Whatever you decide now, it is important to review your life insurance program every few years to keep up with changes in your income and responsibilities.

Legislative History (all references are to the Proceedings of the NAIC)

1976 Proc. I 5[illegible]-527
1976 Proc. II 545-552
1978 Proc. I (corrected)

ATTACHMENT B

Ledger Statement for ______________________________



Amount and Plan of Insurance: $100,000 SELECT 100 — Age: 35 M

Annual Premium: $ 1,446.00

End of Year	(1) Dividend*	(2) Payment*	(3) Cash Value Increase	(4) Payment less C.V. Increase*	(5) Cash Value	(6) Total Payments*	(7) Paid-up Insurance	(8) Insurance*	(9) Cash Value Increase*	(10) Payment less C.V. Increase*	(11) Cash Value*	(12) Total Payments	(13) Paid-up Insurance*	Values at Age 65 if payments stopped (13) Cash Value*	(14) Paid-up Insurance*
	DIVIDENDS USED TO REDUCE PREMIUMS (PAYMENT IS THE ANNUAL PREMIUM LESS DIVIDEND)							DIVIDENDS USED TO PURCHASE PAID-UP ADDITIONS (PAYMENT IS THE ANNUAL PREMIUM)							
1	3	1443	0	1443	0	1443	0	100011	3	1443	3	1446	11		
2	26	1420	145	1275	145	2863	500	100102	171	1275	174	2892	602	2513	3993
3	51	1395	1448	53CR	1593	4258	5300	100280	1502	56CR	1676	4338	5580	21939	34857
4	150	1296	1489	193CR	3082	5554	9900	100786	1648	202CR	3324	5784	10686	39443	62668
5	276	1170	1531	361CR	4613	6724	14400	101707	1832	386CR	5156	7230	16107	55468	88128
6	404	1042	1568	526CR	6181	7766	18800	103053	2028	582CR	7184	8676	21853	70080	111344
7	537	909	1608	699CR	7789	8675	22900	104845	2248	802CR	9432	10122	27745	83445	132579
8	673	773	1649	876CR	9438	9448	26900	107100	2490	1044CR	11922	11568	34000	95674	152008
9	811	635	1688	1053CR	11126	10083	30800	109834	2753	1307CR	14675	13014	40634	106849	169763
10	952	494	1728	1234CR	12854	10577	34500	113067	3042	1596CR	17717	14460	47567	117056	185980
11	1093	353	1768	1415CR	14622	10930	38100	116815	3356	1910CR	21073	15906	54915	126354	200753
12	1220	226	1806	1580CR	16428	11156	41500	121060	3682	2236CR	24755	17352	62560	134741	214078
13	1352	94	1845	1751CR	18273	11250	44800	125835	4041	2555CR	28796	18798	70635	142339	226150
14	1485	39CR	1883	1922CR	20156	11211	48000	131166	4432	2986CR	33228	20244	79166	149160	236988
15	1623	177CR	1918	2095CR	22074	11034	51100	137091	4860	3414CR	38088	21690	88191	155285	246719
16	1765	319CR	1954	2273CR	24028	10715	54000	143650	5331	3885CR	43419	23136	97650	160824	255520
17	1908	462CR	1986	2448CR	26014	10253	56900	150879	5840	4394CR	49259	24582	107779	165855	263513
18	2053	607CR	2022	2629CR	28036	9646	59600	158819	6403	4957CR	55662	26028	118419	170326	270616
19	2206	760CR	2055	2815CR	30091	8886	62300	167530	7019	5573CR	62681	27474	129830	174379	277056
20	2360	914CR	2089	3003CR	32180	7972	64900	177059	7695	6249CR	70376	28920	141959	178051	282890
At Age														Years to*	
60	3280	1834CR	1809	3643CR	41148	191	73100	240834	11841	10395CR	120349	36150	213934	PAY UP	17
65	3973	2527CR	1789	4316CR	50163	11058CR	79600	334339	18212	16766CR	197656	43380	313939	ENDOW	24
74	5157	3711CR	1546	5257CR	65113	40059CR	87900	621616	38073	36627CR	451405	56394	609516		

Premiums per $1,000	Annual	Mo. ISA ◆
Male Insurance #	14.26	1.23
Female Insurance #	13.32	1.15
Policy Fee	20.00	1.72
Waiver Premium	.34	.03
Accidental Death	.76	.07
Additional Purchase	1.76	.16

— ex policy fee
◆ Does not include service charge
Additional benefits are subject to underwriting limits

At Age	Annual Income ▲
60	4225
65	5615
74	8885

At Age	Annual Income ▲*
60	12358
65	22127
74	61598

Interest Adjusted Surrender Cost Index — Basic Policy per $1,000

10 YEARS	20 YEARS
1.45	-2.82

* Dividends assume no loans. Loans will reduce dividends. Illustrated dividends reflect current claim, expense and investment experience and are not estimates or guarantees of future results. Dividends actually paid will be determined annually to reflect then current experience and are refunds of premium. They may be larger or smaller than those illustrated.

▲ Based on current installment refund rates and may change.

This illustration does not reflect that money is paid and received at different times.

Submitted by ______________________________ Date ______________

29-2807 - SC-100 - 1984 - 8% LOAN PROVISION - SELECT

POINTS TO CONSIDER WHEN BUYING LIFE INSURANCE

BENEFITS OF LIFE INSURANCE
Life insurance policies provide unique benefits They protect your beneficiaries against financial loss resulting from your death There are only two exceptions

1. The insurance is not payable if suicide occurs within one year of the policy issue date

2. "If the insured dies within two years after the Date of Issue claim may be denied for misstatements made in the application"

In these cases, premiums are refunded

Most policies also provide a living benefit in the form of a cash value If the policyowner surrenders the policy, he or she may take this value either in cash or as income under one of a variety of installment payment plans This value can also be used as collateral for loans while the life insurance is still in force However, any outstanding policy loan balance will be deducted from any proceeds otherwise payable under the policy

FORMS OF LIFE INSURANCE
Whole life insurance provides lifetime protection for a level premium Because mortality rates increase with age, this level premium produces reserves which are held by the Company Investment return on these reserves becomes an offset to the cost of protection

Term insurance provides protection for a limited period of time Normally, premiums increase with policy duration according to a predetermined schedule Coverage rarely extends beyond age 70 Conversion to whole life insurance without evidence of insurability is permitted during a specified period of time Because premiums do start low and increase over time and because the majority of insureds will outlive the period of coverage, the initial protection provided per dollar of premium is considerably greater than is the case with whole life For these same reasons reserves are minimal and such plans typically have no cash values

ADDED BENEFITS
Most forms of life insurance are available with optional benefits for additional premiums These benefits include waiver of premium in the event of disability, an additional death benefit in the event of accidental death and the right to purchase more insurance without evidence of insurability

The Northwestern has added an innovative benefit - Indexed Protection - which increases the value of a policy as the cost of living rises This benefit may be attached to most new policies Indexed Protection guarantees increases in life insurance at the Consumer Index Rate or 8%, whichever is lower Increases begin in the second policy year and continue through the tenth year Tomorrow's new insurance is guaranteed at today's rates

DIVIDENDS
The Company annually determines the divisible surplus Your policy's dividends represent your equitable share of this surplus

Dividends are refunds of premium and are dependent upon mortality, expense, and investment experience Dividends vary with the amount of loan balance Loans reduce dividends Dividend illustrations are neither guarantees nor estimates of future results, but are based on current experience

REPUTATION, CHARACTER AND STRENGTH OF COMPANY
The Northwestern Mutual has been in business continuously since 1857 Its assets total more than $14 billion Insurance in force exceeds $87 billion The Northwestern is a mutual company operated for the benefit of its policyowners

SALES AND SERVICE
The Northwestern provides sales and service through 6,200 representatives in 409 offices located in all states and the District of Columbia Insurance coverages available are term and permanent life insurance, disability income and annuities

THE LEDGER STATEMENT
The ledger statement illustrates the policy's costs and benefits at selected future dates It brings together the policy's basic financial elements premiums, dividends, cash values, death benefits, and payment plans

Premiums are the amounts paid to the Company for the protection provided by the insurance policy

Dividends have been described above The dividend illustrations used are neither guarantees nor estimates of future results but are based on current experience

Cash Value is the amount payable if the policy is terminated by the owner

Paid-up Insurance is the amount of fully paid life insurance available if premium payments are stopped

Insurance is the amount payable at death

A Life Income with Installment Refund guarantees that total annuity payments will at least equal the total payments It is one of several payment plans available

The income figure shown reflects rates which were effective on the date this form was prepared Such rates are not guaranteed By the time settlement of your proceeds takes place it is likely that these rates will be higher or lower because of changes in the Company's investment, mortality and expense experience

THE LIFE INSURANCE INTEREST - ADJUSTED SURRENDER COST INDEX
This index is an indicator for comparing the costs and values of similar policies issued at the same age The index recognizes the following premiums, dividends, cash value at the end of the index period, and interest at 5% to recognize the time value of money

The use of interest in the calculation of this index makes it possible to combine the costs and values even though they occur at different points in time A lower index indicates a better combination of costs and values than a higher one

Although the index is useful as a means of overall comparison, actual premiums, dividends, values, and benefits should be compared Consideration also should be given to the financial strength and reputation of the company and the services of the agent

THIS INFORMATION IS NOT A SUBSTITUTE FOR THE LIFE INSURANCE POLICY IT ILLUSTRATES PLEASE REVIEW THE POLICY, WHICH IS THE ENTIRE AND CONTROLLING LEGAL CONTRACT

ILLUSTRATION FOR POLICY NUMBER S[redacted] $12.925 WHOLE LIFE

INSURED MALE AGE 29 POLICY DATE 11-24-66

CURRENT ANNUAL PREMIUM $ 224.57 INCLUDING WAIVER OF PREMIUM

------------- DIVIDENDS USED TO REDUCE PREMIUMS - EXCESS DIVIDENDS PURCHASE ADDITIONS -------------

		1	2	3	4	5	6	7	8	9
END OF YEAR	CAL-ENDAR YEAR	INSUR-ANCE*	DIVI-DEND*	ANNUAL PAYMENT*	CASH VALUE INCR.*	PAYMENT LESS CV INCREASE*	CASH --- VALUES --- GUAR.	TOTAL*	PAID-UP -- INSURANCE -- GUAR.	TOTAL*
17	1983	17877	345	0	365	365CR	2676	4576	6966	11917
18	1984	18241	368	0	397	397CR	2871	4973	7250	12566
19	1985	18657	394	0	431	431CR	3069	5404	7535	13267
20	1986	19129	422	0	470	470CR	3271	5874	7793	13997
21	1987	19659	453	0	509	509CR	3476	6383	8039	14772
22	1988	20250	487	0	555	555CR	3684	6938	8284	15609
23	1989	20907	524	0	603	603CR	3894	7541	8517	16500
24	1990	21632	564	0	656	656CR	4108	8197	8737	17443
25	1991	22429	609	0	713	713CR	4323	8910	8957	18460
26	1992	23301	656	0	774	774CR	4541	9684	9150	19524
27	1993	24252	708	0	840	840CR	4760	10524	9344	20670
28	1994	25285	764	0	911	711CR	4982	11435	9538	21897
29	1995	26405	824	0	988	988CR	5204	12423	9706	23183
30	1996	27616	889	0	1069	1069CR	5428	13492	9887	24580
31	1997	28929	959	0	1160	1160CR	5652	14652	10042	26045
36	2002	37130	1404	0	1703	1703CR	6770	22005	10753	34961
				SUM FROM 1983						
@65	2002	37130	1404	0	1703	1703CR	6770	22005	10753	34961
@70	2007	48816	2078	0	2476	2476CR	7841	32732	11296	47188
@75	2012	65185	2994	0	3519	3519CR	8824	48120	11722	63986

ANNUAL INCOME* @65- 2463 @70- 4065 @75- 6732
BASED ON CURRENT INSTALLMENT REFUND RATES AND MAY CHANGE

*DIVIDENDS ASSUME NO LOANS. LOANS WILL REDUCE DIVIDENDS. ILLUSTRATED DIVIDENDS REFLECT CURRENT CLAIM. EXPENSE AND INVESTMENT EXPERIENCE AND ARE NOT ESTIMATES OR GUARANTEES OF FUTURE RESULTS. DIVIDENDS ACTUALLY PAID WILL BE DETERMINED ANNUALLY TO REFLECT THEN CURRENT EXPERIENCE AND ARE REFUNDS OF PREMIUM. THEY MAY BE LARGER OR SMALLER THAN THOSE ILLUSTRATED. BENEFITS WILL BE REDUCED BY ANY OUTSTANDING INDEBTEDNESS.

THE ABOVE ILLUSTRATION DOES NOT REFLECT THAT MONEY IS PAID AND RECEIVED AT DIFFERENT TIMES.

THE COMPARABLE INTEREST RATE OVER THE NEXT 20 YEARS IS 10.07%. AN EXPLANATORY LEAFLET IS AVAILABLE.

PREPARED 9-16-83 ON THE 1983 DIVIDEND SCALE 259053 E AGENT ROBERT SMARIGA

0047

Northwestern Mutual Life Insurance Company • Home Office Milwaukee

Northwestern Mutual Life

ILLUSTRATION FOR POLICY NUMBER S [redacted] $2?.375 65 LIFE

INSURED [blank] MALE AGE 26 POLICY DATE 5-06-63

CURRENT ANNUAL PREMIUM $ 544.00 INCLUDING WAIVER OF PREMIUM, $25,000 ACCIDENTAL DEATH

DIVIDENDS USED TO PURCHASE PAID-UP ADDITIONS

		1	2	3	4	5	6	7	8	9
					CASH	PAYMENT	CASH		PAID-UP	
END OF YEAR	CALENDAR YEAR	INSURANCE*	DIVIDEND*	ANNUAL PAYMENT*	VALUE INCR.*	LESS CV INCREASE*	--- VALUES --- GUAR.	TOTAL*	-- INSURANCE -- GUAR.	TOTAL*
21	1984	52980	1275	544	2002	1458CR	7871	17205	19886	43490
22	1985	56466	1420	544	2199	1655CR	8369	19404	20533	47624
23	1986	60233	1580	544	2418	1874CR	8878	21822	21150	52007
24	1987	64301	1756	544	2655	2111CR	9397	24477	21737	56662
25	1988	68693	1951	544	2917	2373CR	9927	27394	22325	61643
26	1989	73434	2166	544	3202	2658CR	10467	30596	22883	66947
27	1990	78549	2402	544	3517	2973CR	11017	34113	23441	72612
28	1991	84065	2662	544	3858	3314CR	11577	37971	23970	78659
29	1992	90011	2947	544	4233	3689CR	12148	42?04	24498	85121
30	1993	96417	3259	544	4641	4097CR	12730	46845	24998	92034
31	1994	103314	3601	544	5083	4539CR	13322	51928	25497	99429
32	1995	110738	3975	544	5566	5022CR	13925	57494	25996	107341
33	1996	118725	4384	544	6091	5547CR	14538	63585	26466	115828
34	1997	127315	4830	544	6657	6113CR	15164	70242	26936	124865
35	1998	136552	5319	544	7274	6730CR	15801	77516	27436	134636
40	2003	193956	8342	0	10732	10732CR	18876	124636	29375	193956
				SUM FROM 1984						
#65	2002	180973	7768	9792	10317	10317CR	18488	113904	29375	180973
#70	2007	256448	12051	9792	15006	15006CR	20371	177846	29375	256448
#75	2012	364454	18548	9792	22412	22412CR	22088	274047	29375	364454

ANNUAL INCOME* #65- 12751 #70- 22090 #75- 38342
BASED ON CURRENT INSTALLMENT REFUND RATES AND MAY CHANGE

*DIVIDENDS ASSUME NO LOANS, LOANS WILL REDUCE DIVIDENDS. ILLUSTRATED DIVIDENDS REFLECT CURRENT CLAIM, EXPENSE AND INVESTMENT EXPERIENCE AND ARE NOT ESTIMATES OR GUARANTEES OF FUTURE RESULTS. DIVIDENDS ACTUALLY PAID WILL BE DETERMINED ANNUALLY TO REFLECT THEN CURRENT EXPERIENCE AND ARE REFUNDS OF PREMIUM. THEY MAY BE LARGER OR SMALLER THAN THOSE ILLUSTRATED. BENEFITS WILL BE REDUCED BY ANY OUTSTANDING INDEBTEDNESS.

THE ABOVE ILLUSTRATION DOES NOT REFLECT THAT MONEY IS PAID AND RECEIVED AT DIFFERENT TIMES.

THE COMPARABLE INTEREST RATE OVER THE NEXT 20 YEARS IS 10.92%. AN EXPLANATORY LEAFLET IS AVAILABLE.

[illegible] DIVIDEND SCALE 055054 E AGENT ROBERT SMARIGA, CLU

The Northwestern Mutual Life Insurance Company • Home Office Milwaukee

ILLUSTRATION FOR POLICY NUMBER [redacted] $110,000 WHOLE LIFE
ILLUSTRATION ASSUMES POLICY IS AMENDED TO DIRECT RECOGNITION BEFORE 1984 ANNIVERSARY
INSURED [redacted] MALE AGE 25 POLICY DATE 7-12-77

CURRENT ANNUAL PREMIUM $ 1,644.00 INCLUDING WAIVER OF PREMIUM

DIVIDENDS USED TO PURCHASE PAID-UP ADDITIONS

END OF YEAR	CAL-ENDAR YEAR	1 INSUR-ANCE*	2 DIVI-DEND*	3 ANNUAL PAYMENT*	4 CASH VALUE INCR.*	5 PAYMENT LESS CV INCREASE*	6 CASH VALUES GUAR.	7 CASH VALUES TOTAL*	8 PAID-UP INSURANCE GUAR.	9 PAID-UP INSURANCE TOTAL*
7	1984	126365	1002	1644	2541	897CR	6706	10725	27280	43644
8	1985	130906	1151	1644	2770	1126CR	8192	13495	32230	53135
9	1986	135937	1318	1644	3026	1382CR	9725	16521	37070	63007
10	1987	141478	1500	1644	3304	1660CR	11303	19825	41690	73171
11	1988	147506	1686	1644	3337	1693CR	12672	23162	45210	82714
12	1989	154092	1903	1644	3664	2020CR	14085	26826	48730	92826
13	1990	161258	2139	1644	4018	2374CR	15544	30844	52030	103287
14	1991	169037	2398	1644	4402	2758CR	17045	35246	55220	114264
15	1992	177462	2682	1644	4819	3175CR	18588	40065	58300	125758
16	1993	186567	2992	1644	5271	3627CR	20172	45336	61380	137953
17	1994	196350	3318	1644	5749	4105CR	21797	51085	64240	150582
18	1995	206838	3670	1644	6267	4623CR	23464	57352	66990	163843
19	1996	218078	4057	1644	6833	5189CR	25173	64185	69740	177803
20	1997	230114	4479	1644	7449	5805CR	26925	71634	72270	192402
21	1998	243656	5195	1644	8096	6452CR	28447	79730	74030	207675
26	2003	325971	8280	1644	12396	10752CR	36466	132408	82060	298027
			SUM FROM 1984							
@60	2012	560580	18659	47676	26056	24412CR	52119	305511	92620	543152
@65	2017	761644	28597	55868	38425	36808CR	61009	471154	96910	748630
@70	2022	1038838	43664	63948	56010	54394CR	69523	713672	100210	1029073

TOTAL PAID-UP EXCEEDS FACE AMOUNT AT END OF YEAR 14*

ANNUAL INCOME* @60- 31372 @65- 52745 @70- 88645
BASED ON CURRENT INSTALLMENT REFUND RATES AND MAY CHANGE

*DIVIDENDS ASSUME NO LOANS, LOANS WILL REDUCE DIVIDENDS. ILLUSTRATED DIVIDENDS REFLECT CURRENT CLAIM, EXPENSE AND INVESTMENT EXPERIENCE AND ARE NOT ESTIMATES OR GUARANTEES OF FUTURE RESULTS. DIVIDENDS ACTUALLY PAID WILL BE DETERMINED ANNUALLY TO REFLECT THEN CURRENT EXPERIENCE AND ARE REFUNDS OF PREMIUM. THEY MAY BE LARGER OR SMALLER THAN THOSE ILLUSTRATED. BENEFITS WILL BE REDUCED BY ANY OUTSTANDING INDEBTEDNESS.

THE ABOVE ILLUSTRATION DOES NOT REFLECT THAT MONEY IS PAID AND RECEIVED AT DIFFERENT TIMES.

THE COMPARABLE INTEREST RATE OVER THE NEXT 20 YEARS IS 10.01%. AN EXPLANATORY LEAFLET IS AVAILABLE.
PREPARED 8-12-83 ON THE 1983 DIVIDEND SCALE F AGENT ROBERT E SMARIGA

0043

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Northwestern Mutual Life Insurance Company • Home Office Milwaukee

Northwestern Mutual Life

ILLUSTRATION FOR POLICY NUMBER 8 [redacted] $50.000 EXTRA ORDINARY LIFE

INSURED MALE AGE 46 POLICY DATE 1-15-83

CURRENT ANNUAL PREMIUM $ 930.50 INCLUDING WAIVER OF PREMIUM

DIVIDENDS USED TO PURCHASE PAID-UP ADDITIONS

END OF YEAR	CAL-ENDAR YEAR	1 INSUR-ANCE*	2 DIVI-DEND*	3 ANNUAL PAYMENT*	4 CASH VALUE INCR.*	5 PAYMENT LESS CV INCREASE*	6 CASH VALUES GUAR.	7 CASH VALUES TOTAL*	8 PAID-UP INSURANCE GUAR.	9 PAID-UP INSURANCE TOTAL*
1	1984	50000	53	931	53	878	0	53	0	148
2	1985	50000	207	931	667	264	458	720	1200	1909
3	1986	50000	254	931	845	86	1039	1565	2700	4077
4	1987	50000	306	931	915	16	1631	2480	4100	6253
5	1988	50000	364	931	994	63CR	2234	3474	5450	8498
6	1989	50000	430	931	1082	151CR	2847	4556	6750	10824
7	1990	50000	499	931	1175	244CR	3469	5731	8000	13228
8	1991	50000	580	931	1282	351CR	4101	7013	9150	15680
9	1992	50000	669	931	1396	465CR	4741	8409	10300	18287
10	1993	50000	765	931	1523	592CR	5390	9932	11400	21007
11	1994	50000	869	931	1639	708CR	6028	11571	12350	23744
12	1995	50000	978	931	1778	847CR	6671	13349	13300	26650
13	1996	50000	1098	931	1932	1001CR	7318	15281	14200	29687
14	1997	50000	1228	931	2096	1165CR	7970	17377	15050	32864
15	1998	50349	1373	931	2276	1345CR	8623	19653	15900	36249
20	2003	66221	2215	900	3316	2416CR	11887	34053	19400	55621
				SUM FROM 1984						
@65	2002	62601	2023	17658	3083	2183CR	11239	30737	18750	51351
@70	2007	83470	3172	22158	4423	3523CR	14400	50001	21600	75070
@75	2012	112250	4682	26658	6176	5276CR	17310	77203	23750	106000

ELP FULL PAID END OF YEAR 15* ANNUAL INCOME* @65- 3441 @70- 6210 @75- 10801
TOTAL FULL PAID END OF YEAR 19* BASED ON CURRENT INSTALLMENT REFUND RATES AND MAY CHANGE
*DIVIDENDS ASSUME NO LOANS. LOANS WILL REDUCE DIVIDENDS. ILLUSTRATED DIVIDENDS REFLECT CURRENT CLAIM. EXPENSE AND INVESTMENT EXPERIENCE AND ARE NOT ESTIMATES OR GUARANTEES OF FUTURE RESULTS. DIVIDENDS ACTUALLY PAID WILL BE DETERMINED ANNUALLY TO REFLECT THEN CURRENT EXPERIENCE AND ARE REFUNDS OF PREMIUM. THEY MAY BE LARGER OR SMALLER THAN THOSE ILLUSTRATED. BENEFITS WILL BE REDUCED BY ANY OUTSTANDING INDEBTEDNESS.
THE ABOVE ILLUSTRATION DOES NOT REFLECT THAT MONEY IS PAID AND RECEIVED AT DIFFERENT TIMES.

THE COMPARABLE INTEREST RATE OVER THE NEXT 20 YEARS IS 10.98%. AN EXPLANATORY LEAFLET IS AVAILABLE.
THE 1983 DIVIDEND SCALE 259053 H AGENT ROBERT SMARIGA

The Northwestern Mutual Life Insurance Company • Home Office Milwaukee

Northwestern Mutual Life

ILLUSTRATION FOR POLICY NUMBER 8-[redacted] $103,500 EXTRA ORDINARY LIFE

INDEXED PROTECTION INCLUDED - ASSUMES 3.5% INCREASES

INSURED FEMALE AGE 32 POLICY DATE 2-10-83

CURRENT ANNUAL PREMIUM $ 957.72 INCLUDING WAIVER OF PREMIUM

DIVIDENDS USED TO PURCHASE PAID-UP ADDITIONS

END OF YEAR	CAL-ENDAR YEAR	1 INSUR-ANCE*	2 DIVI-DEND*	3 ANNUAL PAYMENT*	4 CASH VALUE INCR.*	5 PAYMENT LESS CV INCREASE*	6 CASH VALUES GUAR.	7 CASH VALUES TOTAL*	8 PAID-UP INSURANCE GUAR.	9 PAID-UP INSURANCE TOTAL*
1	1984	103500	42	958	42	915	0	42	0	195
2	1985	107123	171	991	592	399	419	634	1759	2771
3	1986	110872	212	1025	973	52	1170	1507	4713	6736
4	1987	114753	258	1060	1107	47CR	2003	2714	7871	11062
5	1988	118769	311	1096	1256	160CR	2922	3970	11131	15668
6	1989	122926	370	1134	1421	287CR	3934	5391	14489	20555
7	1990	127228	437	1173	1598	425CR	5041	6989	17824	25619
8	1991	131681	515	1213	1797	584CR	6253	8786	21374	31125
9	1992	136290	601	1255	2012	757CR	7573	10778	25019	36959
10	1993	136290	1005	1196	2251	1055CR	8704	13049	28757	43149
11	1994	136290	1134	1196	2400	1204CR	9616	15447	31346	49368
12	1995	136290	1276	1196	2613	1417CR	10957	18062	33799	55768
13	1996	136290	1432	1196	2848	1652CR	12127	20910	36116	62366
14	1997	136290	1603	1196	3101	1905CR	13324	24011	38433	69317
15	1998	136290	1792	1196	3377	2181CR	14548	27388	40614	76508
20	2003	149371	3076	1196	5191	3995CR	21036	49407	50018	117615
				SUM FROM 1984						
@60	2011	229877	6594	32629	9946	8750CR	32378	110588	61194	209297
@65	2016	305340	10172	38581	14520	13352CR	39707	173424	66373	289939
@70	2021	408566	15563	44421	20914	19746CR	46795	264380	70189	396981

ELP FULL PAID END OF YEAR 19* ANNUAL INCOME* @60- 10480 @65- 17704 @70- 29742

TOTAL FULL PAID END OF YEAR 22* BASED ON CURRENT INSTALLMENT REFUND RATES AND MAY CHANGE

*DIVIDENDS ASSUME NO LOANS. LOANS WILL REDUCE DIVIDENDS. ILLUSTRATED DIVIDENDS REFLECT CURRENT CLAIM, EXPENSE AND INVESTMENT EXPERIENCE AND ARE NOT ESTIMATES OR GUARANTEES OF FUTURE RESULTS. DIVIDENDS ACTUALLY PAID WILL BE DETERMINED ANNUALLY TO REFLECT THEN CURRENT EXPERIENCE AND ARE REFUNDS OF PREMIUM. THEY MAY BE LARGER OR SMALLER THAN THOSE ILLUSTRATED. BENEFITS WILL BE REDUCED BY ANY OUTSTANDING INDEBTEDNESS.

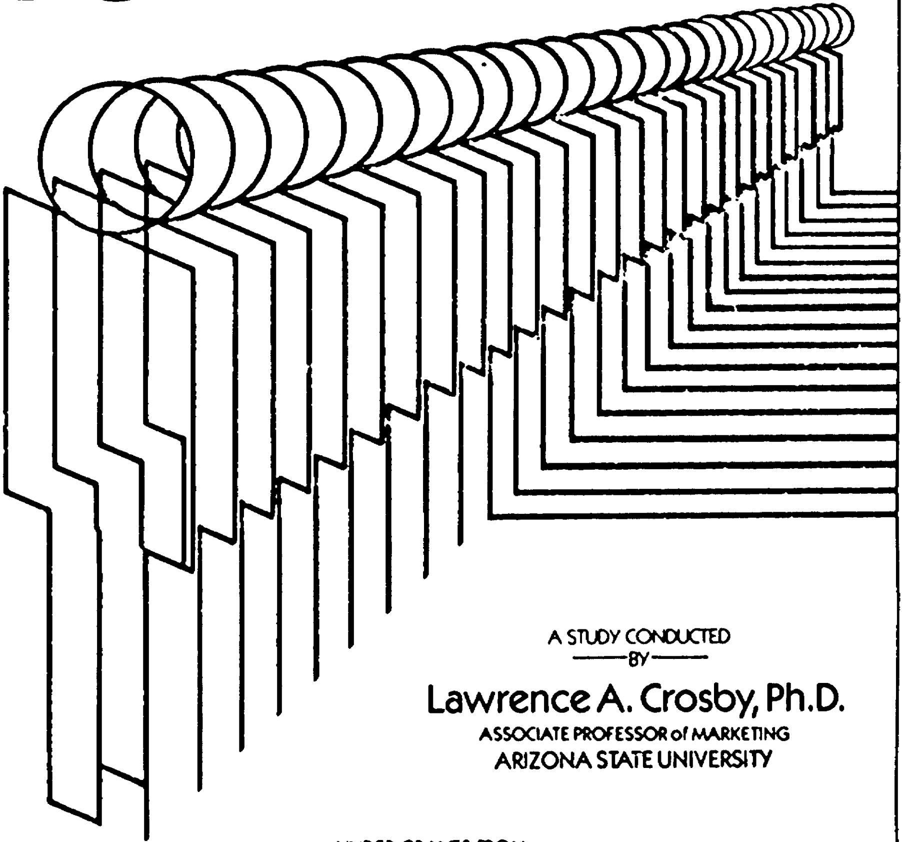
THE ABOVE ILLUSTRATION DOES NOT REFLECT THAT MONEY IS PAID AND RECEIVED AT DIFFERENT TIMES.

THE COMPARABLE INTEREST RATE OVER THE NEXT 20 YEARS IS 10.50%. AN EXPLANATORY LEAFLET IS AVAILABLE.

ATTACHMENT D

EXECUTIVE SUMMARY

Consumer Attitudes Toward Whole Life Insurance



A STUDY CONDUCTED BY

Lawrence A. Crosby, Ph.D.
ASSOCIATE PROFESSOR of MARKETING
ARIZONA STATE UNIVERSITY

UNDER GRANTS FROM

LIFE OFFICE MANAGEMENT ASSOCIATION

NATIONAL ASSOCIATION OF LIFE UNDERWRITERS

EXECUTIVE SUMMARY: Study Rationale

The persistency of whole life policies is both a controversial issue and a marketing objective. Is persistency in the individual consumer's best interest? At one end are those in the industry who claim that all replacement is bad and is invariably inspired by false or misleading information. At the other extreme are aggressive marketers of term insurance who claim that all replacement is good and base their pitch on the now familiar theme, "Buy term and invest the difference." Others, including consumerists and academics, have arrayed themselves at various points along this spectrum.

As the debate rages, many agents and companies are seeking guidance on how to conserve the business they have already created. As historical lapse rates demonstrate, persistency objectives are more difficult to achieve today.

Obviously, all lapsations do not involve replacement. When a customer with a "need" for protection decides to stop making payments or surrender the policy, a breakdown in marketing or customer service might be suspected. Has he or she forgotten or become confused about the needs which the product was designed to satisfy and which led to the initial purchase? Of the many suggestions for avoiding lapse due to a loss in perceived value or utility, more imaginative approaches have yet to be identified.

In the case of replacement, it is impossible to divorce persistency as an issue from persistency as an objective. If all existing policies were truly inferior, the consumer's "best" choice would be clear and the only viable long-run marketing strategies for keeping customers (as opposed to policies) would be policy upgrading or internal replacement.

Since it is doubtful that all existing policies are inferior, many replacements probably involve blatantly bad decisions by consumers. If some consumers are replacing for the wrong reasons, agents and companies need to know what these reasons are and what can be done about them.

Operating from this pragmatic perspective, the Life Office Management Association and the National Association of Life Underwriters have jointly funded a research study on the consumer behavior of persistency/termination as it applies to whole life policies. The study, concerned with all forms of termination including lapsation, surrender, and replacement, is based on certain assumptions -- that the industry's problems can be traced to a change in consumer behavior, that the behavior change is a response to the interaction of environmental and marketing stimuli, and that knowledge of these factors creates opportunities for improving persistency. Specific research objectives are:

- to identify antecedent factors that influence consumer decision-making regarding lapsation, surrender, and replacement;
- to classify these influences as controllable or uncontrollable from a marketing standpoint;
- to recommend specific actions that companies, agents, and trade associations can take to improve the industry's performance vis-a-vis customer satisfaction; and
- to provide data that will contribute to the development of a causal model representing the factors which operate in this problem situation.

To help accomplish these objectives, a nationwide survey was conducted among a representative sample of over 2,000 whole life policyholders between the ages of 25 and 44 during the spring of 1983. The survey represented the first wave of data collection and dealt with customers' experiences, attitudes, and intentions. "Consumer Attitudes Toward Whole Life Insurance," Volume One, contains the results of this survey. A second wave, planned for spring 1984, will measure the actual persistency behavior of the same consumers.

Based on analysis to date, the major conclusions of the study, along with supporting findings, are indicated below.

CONCLUSION 1: Consumers, for the most part, are satisfied with their whole life coverage and not in an active state of problem recognition.

The majority of customers in the sample (54%) indicated they were either "extremely" or "very" satisfied with this insurance coverage overall. Reasons for satisfaction varied somewhat. Comparable figures were: 67% extremely or very satisfied with the agent responsible for the policy, 61% with the company, 47% with the policy's features and characteristics, and 39% with the policy's contribution to their financial needs.

On more specific attributes, policyholders were most satisfied with the agent's personality and product knowledge and least satisfied with his or her efforts to stay in touch. Size, reputation and stability were positive company attributes cited. Respondents appeared to be less satisifed with company communication with policyholders. Protection aspects of policies received higher satisfaction scores than did the savings/ investment aspects, although the latter appeared to be more strongly linked to overall satisfaction.

On the average, consumers indicated little desire to acquire information about the value of their policies from various sources, nor were they inclined to initiate contact with agents to change coverage. This did vary, however, depending on the agent's identity. As an indication of their readiness to respond, 58% of the owners would meet with the responsible agent for the policy to discuss replacement, compared to 21% who would meet with a different agent. If they received a replacement recommendation from the responsible agent, 48% would give it serious consideration. Only 14% would seriously consider a replacement recommendation from a different agent.

Nine percent of those polled said there was a better than 50/50 chance they would lapse in the next 13 months. Among these, five percent plan to surrender, and 2-4% say they will replace.

CONCLUSION 2: Customer satisfaction provides a psychological barrier to lapsation, surrender, and replacement.

Analysis of the survey showed an inverse relationship between satisfaction (with the agent, company, policy features, and needs contribution) and the customer's readiness to be approached by a different agent or to lapse, surrender, or replace. When satisfaction with the agent responsible was coupled with dissatisfaction with the policy, customers were more willing to be approached by that agent and had more definite plans to lapse, surrender, and replace.

CONCLUSION 3: There is an opportunity to improve satisfaction and, consequently, persistency by effectively marketing the product after it is sold. Since the product is intangible, customers need periodic post-sale reinforcement from their agents and companies.

One of the most pervasive influences reflected in the data was the degree to which the agent responsible stays in touch with customers to make sure they are still satisfied. The frequency of agent contact was found to be positively related to satisfaction with the agent, company, and policy.

Other forms of post-sale reinforcement by agents which also make a positive contribution to agent satisfaction were: the frequency with which the agent explained the merits of the policy, and the number of times the policyholder had received a personal remembrance from the agent in the last two years (birthday card, holiday gift, etc.).

Survey data showed that many agents fail to take advantage of these opportunities for improving satisfaction and persistency. About a third of the policyholders (excluding those with orphan policies) had not been contacted in the last two years; 4 out of 10 owners were not appraised of changes in their insurance needs; only half received explanations on why they should keep the policy; and 60% received no cards or gifts.

Companies can also take responsibility for post-sale reinforcement. Statistical analysis revealed that higher levels of advertising exposure/recall in both print and broadcast media were associated with enhanced company satisfaction. These results are entirely consistent with consumer behavior theory. While half of the respondents had seen at least one company ad and 4 out of 10 had seen or heard a commercial, other forms of company-customer contact occurred much less frequently. Only 24% said they received company information on the merits of keeping the policy; about 1 in 8 had been assigned a customer service representative in the home office; and only 38% received information on the company's financial performance (which was related to satisfaction).

The opposite of reinforcement or reward is punishment. Punishment occurs in life insurance when the customer makes a request that is not properly dealt with, which requires more of the customer's time and energy. Survey data suggested that the company's failure to handle a request promptly or properly detracted from company satisfaction and, in particular, the image of being consumer-oriented. Similar failure on the part of the agent detracted from agent satisfaction. Fortunately, only about 5% of the policyholders had these types of experiences.

CONCLUSION 4: Undercoverage is a source of concern to many policyholders. There exists considerable untapped potential among present whole life owners.

The actual face amount of coverage was positively related to owner satisfaction with the policy's contribution to their financial objectives. Satisfaction with the amount of coverage was positively related to policy feature satisfaction. The more frequently the agent contacted the customer to sell additional coverage, the more satisfied the customer was with the agent. Of those dissatisfied with their coverage, 98% believed they had too little.

That these 25- to 44-year-old policyholders would desire more protection is not surprising. First, there is the matter of enhanced buying power. Since the policy was written, 41% have obtained a job promotion and 58% say they are better off economically. Perhaps because of these financial improvements, the affordability of premiums was rated the most satisfying policy feature; few felt that keeping the policy in force would strain their resources. Also, these policyholders now have more to protect. Since the date of issue, 43% experienced the birth or adoption of a child, 43% bought a new home, and 25% married.

Despite these changes, only modest selling activity by the company and agent responsible for the policy seemed to occur. Over a two-year period, 57% of the agents made no attempt to sell more insurance, and two-thirds of the owners received no promotional materials from their company. Coverage was increased on only 9% of the policies since they were written. As for future plans, the second most likely intention (next to maintaining the status quo) was to increase coverage on the existing policy.

Clearly, the 25- to 44-year-old market is highly motivated to buy and would welcome an opportunity to build on existing whole life coverage with additional term or permanent insurance. Otherwise, these customers may be inclined to go elsewhere.

CONCLUSION 5: Smaller companies can compensate for their size by doing a more effective job in the customer service area.

Factor analysis revealed two underlying dimensions of satisfaction with an insurance company. One had to do with the company's "market presence" -- being established and stable and having substantial assets and a strong reputation. The other was its "consumer orientation" -- quality of agents, friendliness of home office personnel, accessibility and responsiveness, and ability to communicate valuable information to policyholder. These two independent factors, market presence and consumer orientation, were equally predictive of overall company satisfaction. Strength in one area could compensate for weakness in the other. Exposure/recall of the company's advertising and commercials was positively related to satisfaction with its market presence. Company failures in the area of customer service, e.g., not handling requests properly or promptly, were negatively related to satisfaction with its consumer orientation.

CONCLUSION 6: Historical improvements in product and the upgrading of older policies are paying off.

It is well known that, due to improvements in mortality and investment earnings, today's whole life policies offer a "better deal" to the customer. This may partly explain the incremental improvements in customer satisfaction with the decreasing age of the policy. The most satisfied owners were those whose policies were issued in the 1980s (19% of the sample). The next most satisfied had policies issued in the 1970s (51%). Other factors contributing to this trend might be the relative "freshness" of reinforcement experiences (ref: Conclusion 3), policy size differences, or changes in the customer's needs.

Consumers whose policies had been upgraded in some fashion (e.g., more coverage at same cost, same coverage at lower cost, greater yield, larger dividends, etc.), tended to be more satisfied with the features of the policy and its contribution to their financial needs. Using a broad definition, 18% of the policies appeared to have been "upgraded" at least once in the last two years.

CONCLUSION 7: Being the customer's "personal agent" is a critical role. Agents are missing an opportunity to establish themselves as such.

Fifty-five percent of the respondents said they had a personal agent. The customer considered the agent responsible for the policy to be his/her personal agent in 52% of the cases. One out of four said the agent responsible had sold the policy or was later assigned to the policy, but they did not consider this person their "personal" agent, nor did they have a personal agent. When the agent responsible was the personal agent, customers tended to be more satisfied with the agent, the company, and the policy.

Among all respondents who received a replacement recommendation from an outside agent in the last two years (20% of the sample), the mean estimated probability of replacing in the next 13 months was 12%. When the agent responsible was not the personal agent, the probability figure doubled to 24%.

CONCLUSION 8: Competitive activities can sow seeds of doubt in the minds of policyholders. Prior inoculation should be considered.

Customers receiving one or more replacement recommendations from outside agents tended to be less satisfied with their present policy's contribution to their financial needs. Likewise, with increasing exposure/recall of competitors' print advertising, consumers were less satisfied with the policy's features. As previously noted, many companies and agents failed to prepare their customers with counter arguments explaining the merits of persistency. If customers do not hear these arguments from their companies and agents, they will probably not hear them at all.

Examination of policyholder beliefs regarding persistency showed that most lacked strong opinions about what their policies can or cannot do for them. While they may have few reasons for dropping the policy, they do not have strong arguments for keeping it. The lack of post-sale enforcement and the failure to inoculate policyholders with significant counter arguments make them more vulnerable to outside influence.

CONCLUSION 9: In the information war, the "other side" appears to be making inroads. The industry needs to step up its public relations and consumer education activities.

All of the major satisfaction components varied inversely with the frequency of exposure to negative newspaper and magazine articles. Negative articles are those which cause customers to question the value of their policies. Over 20% of the sample recalled one or more exposures to negatively slanted articles and a similar figure reported exposure to negative consumer education materials. Trade association information encouraging persistency was remembered by 10%; only 3% had requested information from government agencies.

Lack of product knowledge may be one reason why consumers have few strong opinions about the benefits of whole life ownership (except that it provides insurance even if health worsens). Instructed to have the policy in front of them, 20% "didn't know" whether the policy had an Automatic Premium Loan provision or a Variable Loan Interest Rate. Only two-thirds were aware of the Nonforfeiture Options. Forty percent "didn't know" the policy's present cash value and many others gave unrealistic estimates. Further evidence of a lack of differentiation was that none of the satisfaction components varied with the presence or absence of objective policy features.

The industry may be at a disadvantage when disseminating information since owners indicated a greater preference for non-marketer sources (e.g., consumer education, TV/radio programs, articles, etc.) unless the agent responsible for the policy was involved. Respondents indicated that they were more likely to seek information about the value of the policy from the agent responsible than from any other source. On the average, they were "very satisfied" with the agent's product knowledge. Clearly, agents have a major role as consumer educators and face a receptive audience.

CONCLUSION 10: Policy loans do not appear to be a major factor in persistency. They can work positively or negatively.

A surprisingly small 22% of the sample said they had a loan of any magnitude against the policy. Among those having a loan, the percent of cash value borrowed followed a bimodal distribution, with 27% borrowing less than one fifth and 27% borrowing over four-fifths. Despite claims that borrowing is often a prelude to replacement, only 4% (1% of total sample) said they took a loan to buy a new policy. In contrast, 10% (2% of total sample) were using the loan provision to help make premium payments. Respondent-estimated probabilities of borrowing to buy a new policy in the next 13 months were negligible.

PRELIMINARY ORDER FORM

Yes, I'm interested in receiving information on Consumer Attitudes Toward Whole Life Insurance (Volume One) when available.

- If a member of NALU, return card to:
  - Jack Bobo, FLMI, CLU
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Chairman RODINO. Thank you very much.

Mr. Ream, a task force of the National Association of Insurance Commissioners [NAIC] has written "The fact that adequate, meaningful and understandable consumer information is an essential ingredient of any competitive environment is not debatable."

How does that square with the statement that you made a while ago where you seemed to suggest that it's a disservice to provide a lot of information?

Mr. REAM. No, sir. I said it was a disservice to provide a price listing because those have been misused in cases where they have been tried.

As far as the consumer getting adequate information, PIA and the individual agents wholly support adequate information.

Chairman RODINO. Why would price listing, truthfully presented, be a disservice to anyone?

Mr. REAM. Well, sir, to review my testimony to you this morning: One, rates change——

Chairman RODINO. I know. I heard your testimony.

Mr. REAM. Yes, sir. Well, I think sometimes the difficulty lies in how the figures are interpreted and not always——

Chairman RODINO. Yes; but why don't you leave that to the consumer to determine or decide in his own best interests?

Mr. REAM. The consumer does make that decision, sir, because the consumer in my State, in my locale does a considerable amount of shopping and price is a substantial——

Chairman RODINO. But you're reluctant, at least in your statement, to provide him with a price listing because you think that it would be misleading.

Mr. REAM. No, sir. We provide them with quotations all the time; and most of the time those quotations are accompanied with some consultation as to what his insurance needs are, the availability of products and information of this sort.

The only thing we do not like, if you will, is posting of price listings, if you will, saying "This company is the lowest in this average classification" because those have been misused. But the availability——

Chairman RODINO. Well, you might say, but it doesn't necessarily follow, "This company is the lowest." We're talking about listing prices and letting the consumer decide.

Mr. REAM. The consumer does that in his shopping between various agents. He will compare my price with the price of the agent down the street or several other agents; and there are many sources from which they can get these prices.

Chairman RODINO. Well, let me ask a very general question. Do you think information is or is not useful to the consumer?

Mr. REAM. Consumers have to be informed, sir; but they have to get that information from a place that they trust—

Chairman RODINO. Do you think that the information that is being provided now is adequate?

Mr. REAM. Yes, sir. I believe that the agents and the free competitive marketplace are providing the consumers with price information, product information and service information; the three main ingredients in the decision-making process that the consumer needs.

Chairman RODINO. Do you think that the industry is providing you with the information that is necessary so that you might adequately inform the consumer?

Mr. REAM. I'd have to answer yes, sir. There's an old joke in our industry, that we'd rather own the stock in the paper companies that sell to the insurance companies than sell the insurance product itself. We are inundated, if you will, with brochures, pamphlets, comparison sheets, and everything else to assist us in helping our customers make a decision.

Mr. PATTERSON. Mr. Chairman, if I may just add onto that. I think it's important that the subcommittee realize that we aren't afraid of additional information for consumers. As a matter of fact, it might be to our competitive advantage, except that we just don't think it's necessary.

We think that there's plenty of it out there. There is nothing that we would have to lose by that data being there.

Chairman RODINO. You're making the decision, that it's not necessary?

Mr. PATTERSON. That's our opinion, yes.

Chairman RODINO. Well, one of the things we're trying to explore as a result of this series of hearings is whether or not there is enough information and the kind of information that the consuming public ought to have.

As a result of a commission of which I was a member, we had a study, and one of the recommendations was that we review the exemptions under the McCarran-Ferguson Act. Thus, we believe it's important that we review them.

One of the things that we think is certainly within the scope of this subcommittee's jurisdiction, and also important and essential for this subcommittee to know is whether or not there is adequate information.

We just heard from a panel of witnesses before you, two professors, one news reporter. Certainly, I have to say—without in any way questioning your objectivity—that they are people who are serving either the scholastic sector of this country or the information-providing sector. They have stated unequivocally that there isn't any of that necessary information being provided; and that, further, there's a reluctance to provide the kind of information that the consumer ought to have. That doesn't square with what you're saying.

Mr. PATTERSON. No, it certainly doesn't.

Mr. REAM. Sir, I would submit that in my particular case I have 17 years in this insurance business and I am involved in a very competitive environment. I have reams of material, if you'll excuse the pun, to hand out to my customers that is provided to me gratis by various insurance companies, and I represent seven groups of companies.

This material is readily available, and I actively solicit people, asking them to give me the opportunity to provide them with a competitive quote.

That is the whole meat of my business and that is how I survive.

Chairman RODINO. Mr. Pierce, you wanted to say something.

Mr. PIERCE. Yes, Mr. Chairman.

In the life insurance business, the advent of computers has given us an opportunity that we never had before. Purchase decisions, in the life insurance area, are not made in a vacuum anymore. Certainly they were at one time because we had nothing to support our contentions about future values.

But seldom are we in a circumstance where we're not using an actual computer proposal that shows, year by year, exactly what the factors are in a proposed plan—whether it's term or universal life or current interest assumption whole life or whole life—and it's not unusual to be in a circumstance where a client has a half dozen or more proposals from various agents and yours is only one of them, and he's in a position where he can sit there and accurately compare premium, death benefit, cash value and see the assumptions that are used.

That is much more useful than a reference number someplace that doesn't tell a comparative story.

Chairman RODINO. Do your computers provide you with data as to the rates of return on those investments?

Mr. PIERCE. They do show, in many cases, the interest rate that's being paid on the cash value part of the plan. You see, that's another area where the types of products——

Chairman RODINO. In all cases or in some cases?

Mr. PIERCE. In some cases.

The types of products that are available today are of a much broader range so that now the consumer can have plans that have current interest assumptions that will vary with Treasury bill rates or with portfolio rates of an insurance company or other indexes so that they can specifically see numbers they're familiar to comparing.

Chairman RODINO. Do you have any such data available that you can provide us?

Mr. PIERCE. We could provide some computer print-outs. I don't have them here.

Chairman RODINO. We would appreciate your providing them.

[The information was subsequently provided as a part of Mr. Pierce's prepared statement]

Mr. PIERCE. One additional part of that that I think is important is that many customers, many clients, though they have that material, are not really interested in it.

Chairman RODINO. I'm asking you to provide it to the subcommittee.

Mr. PIERCE. I know; but what I'm saying is the personal relationship of the individual, the trust relationship between the client and the insurance counselor is still, as Dr. Crosby's study pointed out, of paramount value to the consumer.

Mr. PATTERSON. Mr. Chairman, if I might just mention on that same subject, and it might be important to the subcommittee: We, too, in our end of the business use the computer nowadays.

When we have a client or prospective client that calls our agency and wants a quotation for auto insurance, based upon the characteristics of that individual client, we go to our computer where we have the rates for 16 companies that we represent and get for him the best price and the best coverage.

Chairman RODINO. Let me ask you a question. Whether or not you'll answer it is up to you. My understanding is that your organizations would oppose any requirement that the amount of an agent's commission be disclosed to the customer. Is that correct?

Mr. REAM. Well, sir, I feel that an agent's commission is a contractual thing between the agent and his company.

Chairman RODINO. I want to know, is it correct that your organizations would be opposed to any such disclosure? I'm not suggesting that we're going to do it. Is that the position?

Mr. REAM. We don't feel that's useful information, sir.

Chairman RODINO. So you're opposed to it.

Mr. REAM. Not necessarily. We'd be more than happy to discuss that on an individual basis.

Chairman RODINO. Well, suppose we thought that it might be helpful. Would you still oppose it?

Mr. REAM. No, sir.

Chairman RODINO. I would just like to point out, without in any way suggesting that that's what we're looking for, that I'm a little amazed because there are laws requiring that sellers of other sorts of financial services—realtors, stock brokers, bankers generally—are required by law to disclose their commissions.

It seems to me a little strange, a little inconsistent with what seems to be a kind of information that probably has been useful in these other areas.

Mr. PIERCE. NALU is not particularly opposed to that, but we feel it would be a confusing factor because there is so much more to be said about commissions than their flat rate.

For example, an agent's compensation may come in other ways from an insurance carrier; for example, in the way of office allowances, and whatever. So that a percentage, in itself, may not really be very meaningful or helpful to a consumer.

Mr. PATTERSON. IIAA is certainly not opposed. We have just always contended that it was not something that was important in every instance.

We tell clients regularly, if they ask us, "Well, how much are you making out of this?" We are willing to tell them.

Chairman RODINO. Well, if the subcommittee thought that it was important to have this information, would you find yourselves reluctant to provide it?

Mr. PATTERSON. I can only speak for myself. I would not, as an agent, have any problem with giving you that information.

Chairman RODINO. How about you, Mr. Ream?

Mr. REAM. No, sir; but it is on an individual basis and contracts do differ agent to agent.

Mr. PIERCE. Well, we have no problem except we have 1900 companies we're dealing with and it would be a long list.

Chairman RODINO. What do you say to the criticism that has been raised on the part of some people who are critics of the industry, that agents have an incentive to sell only those policies that provide for them the highest commissions, and, therefore, policies that have the highest premiums.

Mr. PIERCE. Mr. Chairman, I'd like to respond to that on the basis that any businessman—and I believe our membership are businessmen and women—or woman is in a position where there's

some conflict of interest, whether it's an attorney recommending a trust with a will, in which case his fee is larger, or a physician recommending an ongoing series of treatment instead of just "Take two aspirin and go to bed."

Yet in those professions, as in ours, I believe that the professional can objectively recommend the best, based upon his understanding of the client's need and his understanding of the products available for that client.

As I mentioned, the value in my business is not one sale at any time. It's the clientele relationship that I build with those 600 businesses or families to do business for many years in the future. So I don't believe that incentive taints us.

I believe that we respond very properly to the needs of the client.

Chairman RODINO. Well, I want to make it clear that though I ask the question, I don't necessarily agree with the criticism.

Mr. PIERCE. I appreciate that.

Chairman RODINO. I would hope that most of the agents who are out there are trying to provide their clients with the kind of information they need and hopefully that the client will be satisfied and then will be able to come back and tell somebody else.

This is why I think that information is so important.

Mr. PATTERSON. In today's market environment, if they don't function that way, then they don't stay in business very long, Mr. Chairman.

Chairman RODINO. Thank you.

Mr. Fish.

Mr. FISH. Thank you, Mr. Chairman.

Mr. Patterson, Mr. Ream, Mr. Pierce, I'd like to address a question to all of you. I think you were in the room when Professor Brinlee testified.

To quote from him, he said that "Few agents are willing to quote rates over the telephone." Would any one of you or all of you care to comment on the statement?

Mr. PATTERSON. Do you want to go from this direction?

Mr. FISH. Sure.

Mr. PATTERSON. That would probably be about 98 percent of our quotations, by telephone. We are not reluctant to quote by telephone.

Mr. FISH. So that statement is 98 percent incorrect, sir?

Mr. PATTERSON. From my viewpoint and many of my colleagues. No, I would disagree with that.

Mr. FISH. Mr. Ream.

Mr. REAM. I can only second the motion. We make our living on the telephone and I would have to agree that 98 percent of our quotes are given by phone.

Mr. FISH. Mr. Pierce?

Mr. PIERCE. The one example I mentioned was the one with the young couple in their thirties that, after having shopped 20 companies by phone, sat down and did business with me. So obviously if I hadn't been willing to give them numbers over the phone I would not have them now as clients for that future growth.

So, yes. Any opportunity for us to do PR over the phone is good, and that's what ratequoting is, as long as we have good products.

Mr. FISH. Thank you.

Now, gentlemen, in your experience, do State agencies effectively handle consumer complaints? Do you have any examples that come to mind that you can recall?

Mr. PIERCE. I have worked closely, Congressman Fish, with the insurance commissioners and department in the State of Oregon because of some responsibilities I've had in the Life Underwriters there.

Only a small percentage of the consumer complaints, I understand, through any State insurance department regard life or health insurance and a pretty large number of those have to do with health insurance complaints relative to understanding Medicare benefits and supplements.

Our public service program concerning the counseling of senior citizens is to address specifically that problem area, but it certainly appears that the insurance commissioners' staffs, their investigatory officers, do a very thorough job of responding quickly to the complaints in our areas. I'm not familiar with it in the property and casualty type of complaints.

Mr. PATTERSON. I deal, actually, or our agency does, with three jurisdictions; District of Columbia, Maryland, and Virginia. While fortunately we don't get many complaints, they do respond quickly. They're quite good.

Mr. FISH. Thank you.

Would any of you care to comment on what the insurance industry, itself, is doing in the area of policy simplification?

Mr. PATTERSON. I'm sorry.

Mr. FISH. Readable contracts. I mean, part of this problem apparently is that these policies are so complicated and people don't read them.

As you know, we've done the same thing to your 1040, so we're talking tax simplication there. We wonder if you have policy simplification in mind.

Mr. REAM. Yes, sir. I think actually the insurance industry has been one of the leaders in simplifying contract language, particularly when you compare that to some other things such as home purchases, mortgage agreements, credit card agreements, even Federal and State regulations.

The insurance policies today are very readable and PIA and the Independent Agents, both, have been very supportive of these efforts to make the policy more understandable to the consumer.

Mr. PATTERSON. Particularly in the personal lines areas, the auto and homeowners. They are greatly improved over where they were when I went in the business 25 years ago.

Mr. FISH. Very good. Good.

Mr. PIERCE. In the life area, all the companies I'm familiar with have used the new readability standards. Of course, in the life area it's a pretty simple contract. The definitions are quite clear.

Mr. FISH. Never a partial loss.

Mr. PIERCE. Never a partial loss; that's right.

Mr. FISH. Thank you very much. Thank you, Mr. Chairman.

Chairman RODINO. Mr. Patterson, there was just one question that occurs to me. If I recall your oral presentation, you recited a certain incident wherein you would talk with a prospective insured and he might be interested in minimum coverage. You said that

you thought it wouldn't do and so you probably advised or suggested something else because of that. I just wasn't clear.

Mr. PATTERSON. My point was that without the advice of an agent, a lot of people would, in fact, buy just minimum limits of coverage because it's cheaper. We obviously recommend higher limits. The minimum limits just don't do the job with lawsuits being as high as they are.

Chairman RODINO. Do you think insurers ought to eliminate minimum coverage because it doesn't do the job?

Mr. PATTERSON. Well, frankly I think the minimums ought to be higher; but, of course, it depends on the economic position or need of that individual as to how much they should have.

But, yes, I think that having the minimums as low as they are does a disservice in a way.

Chairman RODINO. Would you recommend, then, that the insurance industry eliminate that type of coverage since it doesn't do the job?

Mr. PATTERSON. Well, I guess they all have to start with some basic limit of protection.

Chairman RODINO. Apparently, from what you say, it's not benefitting the insured.

Mr. PATTERSON. Actually, that's been changed gradually over the years. The minimum limits have gone up from, like, $10,000 and $20,000 bodily injury to $25,000 and $50,000 in many jurisdictions. That's the amount required by law. That becomes the minimum.

I guess that's what we're looking at more than what the insurance company is saying. It's what the State requires, say in the District of Columbia, for that individual to get his auto tags; and that's all some people are concerned about.

Chairman RODINO. Well, then, the regulators aren't doing their job.

Mr. PATTERSON. In that area that's frequently true.

Mr. REAM. I think a lot depends on the needs, Congressman. If you have a young couple just starting out living in an apartment, they certainly could use minimum limits. But once a person acquires a visible tangible asset, such as a home, then his needs for insurance increase substantially. It's up to the agent, then, to advise them and counsel with them as to what are proper limits given their circumstances.

Chairman RODINO. Do you have any comment to make on that?

Mr. PIERCE. Well, yes. I would see that the same as in the life insurance area; that just because a company issues a minimum series of $10,000 or $25,000 or $50,000, our job is to understand that client's circumstance through fact-finding and then to recommend exactly what we feel is the proper thing.

But our job has been finished at that point because it's their job to make the choice as to whether to do anything or nothing, and if the choice is to do something, are they going to be satisfied with a small amount or a large amount?

All we can do is recommend based upon our professional assessment of that. I feel that's the same thing with their liability insurance needs.

You know, if you run into a school bus full of kids you don't want minimum limits.

Chairman RODINO. Gentlemen, thank you very much; we appreciate your having come here and having provided us with this information.

That concludes this hearing.

[Whereupon, the hearing was adjourned.]

COMPETITION IN THE INSURANCE INDUSTRY

THURSDAY, MAY 10, 1984

House of Representatives,
Subcommittee on Monopolies and Commercial Law,
Committee on the Judiciary,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:30 a.m., in room 2141, Rayburn House Office Building, Hon. Peter W. Rodino (chairman) presiding.

Present: Representatives Rodino, Edwards, Hyde, Sawyer, and Crockett.

Staff present: Alan A. Parker, general counsel; Jonathan Cuneo, counsel; Warren S. Grimes, counsel; Marilyn Falksen, research assistant; Thomas M. Boyd and Alan Coffey, associate counsels.

Chairman Rodino. Today the Subcommittee on Monopolies and Commercial Law continues to consider whether there is enough buyer information for the insurance marketplace to operate efficiently.

Although few would dispute the importance of buyer information for the individual and for the marketplace, there are fundamental disagreements on what information is important and whether it is available.

The subcommittee has received substantial testimony that a market failure exists—replete with higher prices and poor service—because of inadequate information. The subcommittee has also heard that the current system works well to benefit consumers. Today's hearing will provide us with further evidence on these questions.

Our first witness, Ralph Nader, is a well-known advocate of the consumer's right to information. Mr. Nader has a longstanding interest in the insurance industry.

After Mr. Nader has testified, we will hear from a panel representing the property/casualty side of the insurance industry—Ms. Ann Haney, a former State insurance commissioner from Wisconsin, who now is Director of Consumer Affairs for American Family Mutual Insurance Co. in Madison, WI; Mr. Donald W. Segraves, Executive Director of the All-Industry Research Advisory Council; and Ms. Nancy Golonka, Vice President of Consumer Affairs with the Insurance Information Institute.

The subcommittee intends to hold another hearing at a later date, which will be announced.

At this time, unless the gentleman from Illinois has an opening statement, I want to welcome Mr. Nader.

Mr. Nader, will you please come to the witness table? We appreciate your coming here. We ask you to summarize your prepared statement, and we will insert it in its entirety in the record.

TESTIMONY OF RALPH NADER, WASHINGTON, DC

Mr. NADER. Thank you very much, Chairman Rodino and members of the House Judiciary Committee.

Before I begin on the topic of disclosure, I'd like to briefly state my position on the general topic before you, which is the McCarran-Ferguson Act.

As I see it, Mr. Chairman, your committee has two major and separable questions before it. First, does the insurance industry, unique among large industries, require continued antitrust immunity, or can normal competitive forces be allowed to apply?

Second, notwithstanding the decision requiring antitrust immunity, who should regulate each aspect of the insurance transaction?

I see no reason to continue, by the way, this moratorium from the 1944 Supreme Court decision in the *South-Eastern Underwriters* case.

As you know, there was not a single day of hearing held 40 years ago before this McCarran-Ferguson Act was passed. It is, as you said, Mr. Chairman, long overdue that these hearings are being held.

I might also add, about 11 years ago I testified before a similar hearing by Senator Philip Hart over in the Senate Antitrust Subcommittee, and the subject before the subcommittee was insurance industry disclosure, so that no one can charge this committee with building on an empty historical record. Indeed, it's long overdue.

As every major independent study has concluded, this industry is too fat because of such activities as its cartel-like behavior, weak disclosure, and protective regulation and laws.

It is surprising that the Reagan administration, which states that it favors free market competition, has taken no steps to confront what is clearly the most overt cartel-like behavior; namely, the ratesetting bureaus which characterize much of the insurance industry.

Couple the remarkable inefficiency of this industry with recent State action in several States to withdraw rate regulation while allowing rate bureaus and other anticompetitive practices to abound, and you have a shocking situation indeed.

The question is this: Can consumers continue to afford to pay 12 percent of their disposable income into a system that has neither strong regulation nor strong competition? That's 12 cents out of every consumer dollar.

You will notice, of course, that the major media does not devote 12 percent of its time devoted to consumer issues to insurance. This is not only an industry that has escaped competition in significant respects and not only an industry that has escaped regulation in significant or even insignificant respects; it is an industry which has escaped media coverage.

These are major hearings by a major committee of the U.S. Congress, and I read the papers, and I have read no coverage in the

Washington Post or the New York Times on the hearings held before this committee in recent weeks.

That is not accidental. It could be ignorance, it could be indifference, it could be something else, but it also serves to note that this industry has a protective cover on it as no industry—not oil, not gas, not banking—has on them.

As respects regulation, it is clear that Congress must act to re-regulate certain areas as it also deregulates other aspects of insurance marketing. This may seem to be an ironic statement, but it is not.

Among the clearest regulatory needs are those which would enable competition to be fully effective. Although State regulation has demonstrably failed, symbolically, one only has to go to an annual meeting of the National Association of Insurance Commissioners and trip over every hospitality suite that the insurance companies are making available to these commissioners, many of whom seem to be engaged in on-the-job training before they go into the industry which they once were sworn to regulate.

Although State regulation has failed, you may well choose to allow regulation to remain in State hands. A century-plus of State coddling of this industry will not stop overnight, however.

In 1945, when Congress deregulated the regulation of insurance—delegated the regulation of insurance to the States via the McCarran-Ferguson Act, Congress neither enacted any standards for the quality of State regulatory efforts nor created any continuing oversight mechanism to assure that insurance regulation was not abusing the public.

You must not make that same mistake again if you choose to leave any part of insurance regulation at the State level.

I'll just give you an example. Last year, my father and some of his neighbors in Connecticut decided to try and buy a group homeowners' insurance policy. They figured that if they bought as a group, they could save some money.

So, they wrote several insurance companies in Hartford and asked, "We would like to buy a home insurance policy as a group in the town that we live in." Each insurance company wrote back saying, "Sorry; it's unlawful; we can't do it; State law prohibits it."

So, the group wrote to the insurance commissioner of the State of Connecticut, who wrote back saying the same thing.

In most States in this country, Chairman Rodino, it is unlawful for group home insurance policies to be sold. Now that is a caricature of the standard of competition which should prevail in this industry. Perhaps the Supreme Court of the United States will invalidate these laws in a forthcoming challenge.

Now as to the specific area of disclosure. When one views television, one sees the insurance industry's concept of disclosure. A typical insurance ad shows a man looking at his dented fender with a sad and puzzled face, but suddenly the cavalry charges down the hill—25 or so of them—to ride off into the sunset with the now gleefully smiling customer. This is not what consumers mean when we say we want disclosure.

Consider the mandatory nature of insurance. Twenty-six States require auto liability insurance. The physical damage part of the

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auto insurance package is required by lenders if you take a loan, in the same way as mortgage holders require protection on homes.

Life insurance is essential to a breadwinner with dependents. Insurance is not a luxury, as we are told time and time again by the industry, but, moreover, it is required by law or circumstance in many instances.

Then there is the intangible nature of insurance. What are consumers buying? With a car, one can kick the tires at least, but insurance is inscrutible, confusing, boring, obscure. What indeed is this piece of paper called the policy? What does it cover? What does it not cover?

Then the question of price and service comes up. How does one find out which company has the best price? How does one know which company has a good service record?

Add to this the fact that consumers can be denied insurance at the whim of an insurance underwriter, causing insurance customers great concern when shopping, and we can see that America's consumers are in a tough place as regards to shopping for insurance.

Is it any wonder, Mr. Chairman, that people buy the wrong products?—an obvious sign of lack of disclosure and manipulation that they find out about too late, manipulation by those who can take advantage of this dearth of information.

Too much whole life insurance sold has been demonstrated by the Federal Trade Commission, and the National Insurance Consumer Organization, Prof. Joseph Belth of the University of Indiana, and others.

Ask yourself, doesn't the very existence of junk coverages such as air travel life insurance, cancer insurance—imagine that as a specialty—cancer insurance, credit life insurance, Medigap scams, mugging insurance, car rental collision deductible insurance, and the multitude of low-cost group life and health insurance sales—that are really high-cost—prove the case that in insurance, nondisclosure is a disaster for consumers?

How does a consumer deal with this incredible lack of information and comparability and avoid the generous array of ripoffs in this market? Change in current practice is required.

Mr. Chairman, regulation is needed to enable consumers to get the information they need to make significant choices so that competition can be fully stimulated. Policies could be standardized, but that might stifle competition. A better choice would be to have insurance department experts rank policies into categories of actuarial equivalency.

Under this approach, each policy would have a ranking—say, a letter from A, which is full coverage, to D, minimum coverage—so that the consumer would know that a price of $100 for an A-rated policy is a better deal than the price of $100 for a D-rated policy.

Further, service information also needs to be obtained at point of sale—that is, just prior to the granting of coverage to the consumer.

The New York Insurance Department, to its credit, publishes information on insurance companies' complaint ratios and ratios of numbers of claims in suit to total numbers of claims. This is good information. In fact, New York's disclosure is arguably the best in

the country, but few consumers obviously can use it today. It is simply too remote vis-a-vis the sale of insurance—the point of sale of insurance.

It needs to be placed on the application or in some brochure required to be delivered as the sale is being made. A form that says: "This company ranks 10th worst of 250 insurers in service comparison rankings" would be most helpful to a buyer. A company's solvency ranking might also appear.

If the consumer knows how much coverage a policy contains, what quality of service a company offers, and how solvent it is, all that is needed is price to complete the picture.

A statement when a consumer is choosing insurance, such as "The price range for your class is $100 to $500 according to the insurance department" would be most helpful. Certainly it would be quite provocative for the consumer to think over the choice he or she is about to make. If the price being offered was $500, it would not take too long to show that insurance agent the door.

Consumer information can be generated by consumer information brokers, who could computerize the information and make it available to consumers. This is of great potential, given today's technological revolution, but this, too, requires some government action to insure that the basic accurate data on prices and service levels are available to such information brokers in a timely way.

I know the insurance people have said, "Well, there are all kinds of questions about how complete and precise this ranking would be, or this information would be," but it would be far, far more complete than the gap which now exists.

If they have a way to improve the disclosure standards, I am sure that they will find a hearty reception for their pioneering contribution to a more informed marketplace; but we have to start somewhere, and a great deal of progress could be made under existing concepts in the area of insurance disclosure.

After all the Government action over decades of study and debate, the life insurance industry has still been able to thwart meaningful disclosure such as the rate of return on the savings portion of whole life products. The only thing standing between the consumer's wallet and this industry are the consumers themselves.

In property/casualty insurance, the NAIC—that is, the National Association of Insurance Commissioners—itself found that it could not overemphasize the importance of adequate detailed price and other information for consumers if competition were to work as the regulator of prices.

To our knowledge, Mr. Chairman, no State has developed the kind of price information system that the National Association of Insurance Commissioners itself considered an essential precondition to the operation of a competitive rating system.

How NAIC reconciles its statements regarding disclosure with a lack of action by all States to disclose is puzzling.

I would suggest, Mr. Chairman, that the committee, even if it decided to do nothing, can, with one small piece of legislation, empower insurance consumers to do much. This would be getting past the McCarran-Ferguson Act, of course, by new legislation.

This would be simply requiring all insurance companies operating in interstate commerce twice a year in their premium billing

envelopes to insert a statement printed by a national consumer group chartered by the Congress and open to all consumer policyholders who choose to join—let's say, for $5 a year.

The little insert in the premium envelope which comes to millions of consumers would have a message such as the following:

> Are you concerned about poor service, high premium prices, and other issues involving the insurance companies? Are you concerned that they don't put some of their massive profits, with very few exceptions, into advancing health and safety in this country, which should be their vested interest? If you are, why not join the Nationwide Consumer Policyholder Action Group with your own full-time advocates in Washington and in various regional areas around the country?

That alone, Mr. Chairman—that provision alone, which would not cost the taxpayer a dime, which would not create another Government agency, and which would be voluntary to the consumer—that alone—opening up the premium envelope to an inserted notice by a duly chartered, nationwide consumer organization, open to anyone who cares to join, if they are policyholders—that one provision will empower the consumers of this country to achieve many of the objectives that you, I gather, would like to achieve as a result of these hearings.

So consumer empowerment should be considered by this committee as an alternative if the insurance lobby succeeds, as it always has, in humoring the Congress when hearings are held but blocking any legislation from being passed.

In conclusion, what needs to be done as respects insurance disclosure is reregulation, including Federal standards of disclosure, to make sure that people have the information they need to shop this market. Then, and only then, can competition be effective so that deregulation of rates can be effective.

The necessary information might be provided by Government, or by independent information brokers, or by this nationwide consumer group which I have just suggested to you. In either case, Government must gather the necessary data to facilitate complete disclosure.

In property/casualty insurance, the quality of coverage should be ranked by the Government specialists, so people know generally the quality of the contents of a policy.

The percent of premium expected to be paid out in claims should be disclosed. One would certainly rather purchase a policy that had an expected claim payout ratio of 80 percent than one with a 40-percent ratio.

Service level information, such as how long it takes a particular insurance company to pay claims compared to how long it takes the average company, the percentage of claims in suit for the company compared to the percentage for all companies, and the number of complaints for 1,000 policies compared to the same information for the average company must be disclosed prior to sale of insurance policies.

In life insurance, the rate of return on savings portions of whole life policies must at long last be disclosed. In all lines of insurance, agents should be required to disclose the percentage of the premium which is paid to them as commissions.

People who are good risks based on their driving record for auto insurance, their health for life insurance, and who have their

homes' quality up to par for homeowners' insurance should have the right to shop the market and act upon the information.

Insurers should be denied the luxury of underwriting by whim and hunch and thus making disclosure irrelevant. Redlining should be abolished by requiring insurers to take those meeting Government standards of insurability.

When these disclosures are in place and when rate bureaus—and I must emphasize—and when anti-rebate laws in all 50 States, and when anti-group laws in a majority of States, and other trappings of an anticompetitive, outrageous past are swept away, then deregulation of ratemaking can be undertaken with the assurance that consumers will be protected by market forces.

Mr. Chairman, to give you an idea—as if you need further information in this regard—but to give you an idea of what is in store for any proposals coming out of this committee, about 2 or 3 years ago, Congressman LaFalce held hearings on the State anti-rebate laws. These are laws which prevent insurance agents from taking customers away from their competitors by discounting a portion of their commission. It is prohibited in 50 States.

He had very informative hearings, and nothing came as a result. This during an administration, Mr. Rodino—during an administration that makes it appear as if they are for free market competition.

The States do not have the will nor the expertise to make the needed changes. The consumers of this country look to the Congress for the reform that will save them tens of billions of dollars every year. These savings can then be put back into the marketplace to go for furniture, for homes, for education, for all the other areas that consumers voluntarily would like to engage the market and purchase their goods and services in, leading to greater employment and to a more prosperous economy.

Whatever you do, Mr. Chairman, I hope you and the members of this distinguished House Judiciary Committee will consider the consequence for the health of the economy and the level of employment from saving insurance consumers tens of billions of wasted dollars every year, dollars which could be used for their own volitional expenditure in many other sectors of the economy. Thank you.

[The prepared statement of Mr. Nader follows:]

STATEMENT OF RALPH NADER

Mr. Chairman, Members of the Subcommittee, I appreciate your invitation to testify today.

THE McCARRAN-FERGUSON ACT

Before I begin on the topic of disclosure, I would like to very briefly state my position on the general topic before you, the McCarran-Ferguson Act.

As I see it, Mr. Chairman, your committee has two major, and separable, questions before it:

- does the insurance industry, unique among large industries, require continued anti-trust immunity, or can normal competitive forces be allowed to apply, and
- notwithstanding the decision regarding anti-trust immunity, who should regulate each aspect of the insurance transaction.

As respects anti-trust immunity, I see no reason to continue this "moratorium" from the 1944 Supreme Court decision in the Southeastern Underwriters case. I call this a "moratorium" because of the bizarre legislative history surrounding the McCarran-Ferguson Act's passage, in which not one second of public hearing was held and in which the extension of the moratorium into what is on the books today passed neither chamber originally but was created in the conference committee in what must be considered one of the Congress's least ennobling hours. It is, as you said Mr. Chairman, "long overdue" that these hearings are being held.

As every major independent study has concluded, be it from the Ford Administration's Justice Department, from the Carter Commission on Anti-Trust Laws and Procedures, from the work of the National Insurance Consumer Organization, or from Andrew Tobias, all conclude that this industry is too fat because of such activities as its cartel-like behavior, weak disclosure and protective regulation and laws. Some insurance executives have agreed, either orally (1) or by action (2).

Couple the remarkable inefficienty of this industry, with recent state action in several states (in response to heavy insurer lobbying) to withdraw rate regulation while allowing rate bureaus and other anti-competitive practices to abound, and you have a shocking situation in this industry.

The question is this: Can we continue to afford to pay 12% of our disposable income into a system that has neither strong regulation nor strong competition? Can we tolerate this massive inefficiency any longer?

The answer is "no". The McCarran-Ferguson Act should be repealed.

As respects regulation, it is clear that Congress must act to re-regulate certain areas as it also deregulates other aspects of insurance marketing. Among the clearest regulatory needs are those which would enable competition to be fully effective, such as overriding of state anti-rebate (vertical price-fixing) laws and anti-group (prohibition on sale of group policies in property/casualty insurance) laws, establish federal standards for disclosure and create meaningful insolvency protections (Baldwin-United should be the focus of one day of your hearings, for a lesson in how state regulation has failed to structure insolvency protection that is real while assuring an unsuspecting public that real protection is in place).

Although state regulation has demonstrably failed, you may well choose to allow regulation to remain in state hands. A century plus of state coddling of this industry will not stop overnight, however (3). In 1945, when Congress delegated the regulation of insurance to the states via the McCarran-Ferguson Act, you neither enacted any standards for the quality of state regulatory efforts nor created any continuing oversight mechanism to assure that insurance regulation was not abusing the public. You must not make that same mistake again if you choose to leave any part of insurance regulation at the state level. I encourage your careful consideration of Attorney General Bell's advice that you look at functions to see which the states do better and which the federal government would do better. You should establish federal standards for those objectives that you want to be sure states accomplish.

DISCLOSURE

When one views TV, one sees the insurance industry's concept of disclosure. A typical insurance ad shows a man looking at his dented fender with a sad and puzzled face but suddenly the calvery charges down the hill --25 or so of them -- to ride off into the sunset with the now gleefully smiling customer. This is not what consumers mean when we say we want disclosure.

Insurance is unique in many respects, and consumers need to understand what it is they are buying. First of all, the function of insurance is to spread the risk and, through the gathering together of many people, to make what seems like random events to an individual more certain by the grouping process, under what is known as "the law of large numbers". This process results in the creation of a common fund, a sort of large bank account, where those who suffer the insured event can draw out money to cover the financial consequences

of the event. Most people do not realize that they are the insurance company (the common fund is their money held in a sort of trust arrangement called "reserves") and the entity we call "the insurance company" is a bookkeeper we have hired to keep account of these common fund transactions. Insurance creates nothing, adds nothing to the wealth of the world; it is an income transfer mechanism and thus a very social, but needed, transaction.

A contrast that can confuse consumers is this: Fantasize going to a GM dealer to look at their "safety car" equipped with air bags, 10 MPH damage-free bumpers and so forth to ask, "What is your best price?" If they say "$8,000," and one says "I'll take it," there is a deal. The $8,000 represents an offer, the "I'll take it" represents an acceptance.

But, when one goes across the street to insure the shining new car and asks the company, "What's your best price?" and they say "$500," and one says, "I'll take it," what has happened? Only an offer. The company then has to say "yes" in order for an acceptance to occur. Thus, the insurance company is placed in the normal consumer role. It is a very odd situation, and one which presents problems of unfair insurer activities such as redlining (4).

It gets odder, though. Add to that the mandatory nature of insurance. For instance, 26 states require auto liability insurance through mandate, but other states in effect mandate it through laws which put significant pressure on drivers to have liability insurance. The physical damage part of the auto insurance package is required by lenders if you take a loan in the same way as mortgage holders require protection on homes. Life insurance is essential to a breadwinner with dependents. Insurance is not a luxury, it is required by law or circumstance.

Then there is the intangible nature of insurance. "What are consumers buying?" With a car one can kick the tires at least, but insurance is inscrutable, confusing, boring, obscure. "What is this piece of paper? What does it cover? What does it not cover?"

Then, the question of price and service comes up. How does one find out which company has the best price? How does one know which company has a good service record?

Another factor is the impact of "reverse competition" whereby agents can maximize their income by selling us the wrong product. And they do sell us a lot of the wrong products. The findings of a Wharton School professor, that agents decide half of the time where to place business based on what is best for the agent, is very disturbing (5).

Is it any wonder that people buy the wrong products, an obvious sign of lack of disclosure and manipulation by those who can take advantage of the dearth of information. Too much whole life insurance sold has been demonstrated by FTC, NICO, Professor Belth, and others. Ask yourself, doesn't the very existance of junk coverages such as air travel life insurance, cancer insurance, credit life insurance, Medi-gap scams, mugging insurance, car rental collision deductible "insurance" and the multitude of "low cost group" life and health insurance sales that are really high-cost prove the case that, in insurance, non-disclosure is a disaster for consumers?

How does a consumer deal with this incredible lack of information and avoid the incredible array of rip-offs in this market? Change in current practice is required.

1. Offer and Acceptance

The unusual offer/acceptance reversal has been resolved for auto insurance in five states (Massachusetts, Michigan, New Hampshire, North Carolina and South Carolina) and for homeowners insurance in one state (Michigan). In these states good drivers and homeowners who meet state standards of insurability are entitled to insurance from the insurer of their choice.

This is important to any discussion of disclosure simply because all the information in the world will not help a consumer in, say, a redlined district of a major city when the company can, even without cause, say "no" to a willing customer.

A very important and excellent study on this very point was published by the Department of Housing and Urban Development in 1974. Full Insurance Availability concluded that "more than 30 million persons (were then) currently uninsured, or . . . forced into the substandard or unlicensed markets, or into FAIR plans or automobile assigned risk plans." HUD called for state action to end abusive practices whereby millions of Americans who are good risks, who never had a claim, are forced into these situations. In short, HUD called for normal buyer/seller relationships to be mandated where "good risks" (as defined by the state) could get insurance from the company of that person's choice. Ten years later, only five states have responded to this call for reform.

2. Mandatory Insurance

Of particular interest is the decision of the Michigan Supreme Court in Shavers v. Attorney General (404 MICH, 554, 267 N.W. 2nd 72-1978) where the court held that the state's mandatory auto insurance law created a due process requirement whenever a driver was declined coverage. This

led to the adoption of the Essential Insurance Act by the Michigan legislature which, using techniques patterned after HUD's Full Insurance Availability report, required insurers to accept consumers who met state standards for insurability. This is a very positive consumer development and makes disclosure extremely useful in Michigan.

Mandatory insurance is not a problem in itself. There is a need to protect potential victims. But it is abusive to mandate insurance when the insurance sold is overpriced due to inefficiency or excessive profit or both due to lack of meaningful competition which is a direct result of the McCarran-Ferguson Act's anti-trust exemptions. It is particularly abusive to allow insurers a carte blanche capability to turn away people who have to buy the coverage by law and to dump them into high-priced assigned risk plans, often without cause. A federal standard to the effect that insurers must deal with good risks could be of significant assistance to consumers and make disclosure even more meaningful.

3. The Intangible Nature of Insurance/Quality of Service/ Price

In these three areas, the need for disclosure arises. Here's what GAO says about the current lack of such disclosure (6):

> Inasmuch as the causes of market failures include inadequate consumer knowledge . . . state remedies should specifically address these problems. Most State Insurance Departments do not actively attempt to correct the problem of consumers' lack of information . . . most departments do not compare claims handling procedures of companies, no do they inform consumers about the comparative complaint records of companies . . . Future service is the essence of the insurance product, but the consumer cannot now evaluate that aspect at the time of purchase . . . insurance departments do not do enough to provide consumers with specific information about price differences among companies . . . to increase consumer's understanding of insurance and their ability to compare insurance policies, regulators could adopt several different approaches. . . regulators could provide checklists of coverages so that consumers could at least make some comparison of what is being offered by competing policies . . . market competition will not be fully stimulated until consumers can readily understand all the policies they want to compare.

Mr. Chairman, regulation is needed to enable consumers to get the information they need to make significant choices so that competition can be fully stimulated. Policies could be standardized but that might stifle competition. A better

choice would be to have insurance department experts rank policies into categories of actuarial equivalency. Under this approach, each policy would have a ranking, say a letter from A (full coverage) to D (minimum coverage), so that the consumer would know that a price of $100 for an "A" rated policy is a better deal than a price of $100 for a "D" rated policy.

Further, service information also needs to be obtained at point of sale (that is, prior to the granting of coverage to the consumer). The New York Insurance Department, to its credit, publishes information on insurance companies' complaint ratio's and ratios of numbers of claims in suit to total number of claims. This is good information, in fact New York's disclosure is arguably the best in the country, but few consumers can use it today. It is simply too remote vis-a-vis the sale of insurance. It needs to be placed on the application or in some brochure required to be delivered as the sale is being made. A form that says this company ranks 10th worst of 250 insurers in service comparison rankings would be most helpful to a buyer. A company's solvency ranking might also appear.

If the consumer knows how much coverage a policy contains, what quality of service a company offers and how solvent it is, all that is needed is price to complete the picture. A statement, when a consumer is choosing insurance, such as "the price range for your class is $100 to $500, according to the insurance department" would be most helpful. If the price being offered was $500, it would not take long to show that agent the door!

Last week in your hearing, an agent representative told you that publication of price lists would be a "disservice" to the public and that the public would be "misled" because prices change and the use of printed price lists are often not current. Further, the agent opined, printed price lists are not consumer-specific, since they usually show a basic class and therefore a customer with a different class than might be printed in the price list could be misled. What the agent was really tell you is that, rather than giving America's consumers approximate knowledge, it is better to keep them totally ignorant (7).

In any event, the problem of approximation is moot if one puts the full price system on a computer. Consumer information can be generated by consumer information brokers who could computerize the information and make it available to consumers. This is of great potential given today's technological revolution. But this too requires some government action to assure that accurate data on prices and service levels are available to such information brokers in a timely way. The records of many state insurance departments are in poor shape.

I would like now to spend a few minutes discussing some disclosure topics in specific lines of insurance.

A) Life Insurance

Eleven years ago I testified before the late Senator Phillip Hart regarding disclosure by the life insurance industry. I said that, "the life insurance industry has been a smug sacred cow feeding the public a steady line of sacred bull." Nothing has changed, except the sacred cow is probably a little smugger today. Here's why:

In 1979, the FTC and President Carter had the audacity to agree that the "bull" had cost consumers billions of dollars (8). Congress, in an action roughly akin to know-nothingism, forbade the FTC to study insurance without prior Congressional approval (9). Think of it! An industry with virtually no federal regulation, inept, weak and will-less state regulation and now beyond even the look of the FTC. So the sacred bull, in a fit of revenge against the possibility of the truth being let out, raged through the federal china shop.

At the state level, the National Association of Insurance Commissioners (NAIC), after decades of debate, has still been unable to produce disclosure rules that are acceptable. Even NAIC's own task force called the NAIC model "fatally flawed" (10). The NAIC has not yet finished studying (believe it or not) the question of whether or not consumers should be told the rate of return they get on the savings element of their whole life policies. To pin our hopes on state regulation, given its pathetic track record, would be foolish.

After all of the government action over decades of study and debate, the life insurance industry has still been able to thwart meaningful disclosure, such as the rate of return on the savings portion of whole life products. The only thing standing between the consumer's wallet and this industry are the consumers themselves. It is, as an NBC documentary reported, not a fair match (11).

At the consumer level, there is some hope. In 1980, I helped to create the non-profit National Insurance Consumer Organization (NICO). NICO has been able to publish straightforward, useful consumer advice. Their life insurance guide "How to Save Money on Life Insurance" has been requested by thousands of persons (12). As the New York Times put it as they recommend NICO's work: "Impartial advice on life insurance is hard to come by . . ." (13). An example of the hunger for information is the fact that NICO has received 3,000 requests for information from the attached small mention in this month's Good Housekeeping magazine. Here's one such letter: "Please send me your Buyer's Guide to Insurance. Please hurry. I have two teenagers and renewal comes in May. Broke. Thanks." S.C., Arizona.

NICO has warned consumers of the dangers of buying whole life insurance, of the credit life insurance rip-off, of high cost group plans, etc. Recently, NICO warned of a new life insurance deception, the trend to so-called "no-load" universal life policies. This term, which has come to have a rather precise meaning in the mutual fund business, is being used to sell life insurance policies with very high sales loads. For instance, Aetna's "no-load" universal life policy, NICO points out, has a first year cash value of only 76% of NICO's recommended universal life policy sold by USAA. It is good that NICO is calling attention to such deceptive practices, but so much more needs to be done, so many more Americans need to be reached!

B) Property/Casualty Insurance

In property/casualty insurance, the NAIC itself found that it could not over-emphasize the importance of adequate, detailed price and other information for consumers if competition were to work as the regulator of prices. The NAIC said that "[a]dequate consumer information, including price information, is *essential*" for open competition, and that it "is a *precondition* to a reliable competitive market."(14)

The report of the NAIC Task Force to Develop Meaningful Consumer Information on Personal Lines, incorporated in the Alternative Model Act Report, was, if that were possible, even more emphatic about the importance of consumer information to the operation of competitive systems. It said (emphases added) that a

> system of price comparison was an *essential ingredient* of any consumer information activity designed to generate or exert downward competitive pressure on insurance prices. The generation or exertion of such pressure becomes even more important within the context of a rating law which places great reliance on competition as a primary obstacle to excessive consumer prices and is *unquestionably necessary* with respect to private passenger automobile and dwelling property insurance.

It said that there was "no viable substitute for direct price comparisons."

The NAIC committee reported that fewer than two dozen states had published buyer's guides respecting personal lines insurance and far fewer than that have any price information in them. To our knowledge, no state has developed the kind of price information system NAIC itself considered an essential precondition to the operation of a competitive rating system. How NAIC reconciles its statements regarding disclosure with lack of action by the states to disclose is unknown.

Other experts also conclude that better consumer information is a prerequisite for competitive insurance markets:

- the authors of Monitoring Competition noted that the premise for effectively competitive markets is that consumers have access to reliable comparative price information.

- Dr. Joskow noted that "there is no other product for which consumer ignorance is so prevalent." He thus recommended that insurance departments "play a consumer information . . . role" to see that the "greatest possible amount of price information should be put into the hands of consumers," including price comparisons and reports of companies "which have consistently poor payoff policies." (15)

- The General Accounting Office in its report on state regulation of insurance conditioned its recommendation for reliance on competition on "much greater regulatory action to inform consumers well enough to make the competitive market work beneficially and effectively." (16)

- A survey of consumer attitudes about insurance found that roughly one-third of consumers found price information for auto and homeowners insurance either difficult to obtain or obtainable but only with some effort (17). Almost half thought price information "readily available". But half, who did little comparative price shopping, also thought that premiums for all companies were about the same. And it was the people who said price information was readily available who thought there were few price differences. "Thus, those who do not shop for their auto and homeowners insurance, for whatever reason, are lulled into believing that all premiums are about equal and that information relating to such premiums is readily available when, in fact, neither assumption is correct."(18) Those who actually attempted to shop for insurance thus tended to be the ones reporting that information was difficult to obtain.

  These results were confirmed in actual experience in Massachusetts. When competitive rating went into effect in Massachusetts in 1976-1977, insurers and agents frustrated consumers' attempts to obtain price information, according to the Massachusetts insurance commissioner. Studies found consumers were able to obtain price

> information by telephone from only 12% to 20% of agents or companies. "[A]ttempts by buyers to engage in meaningful comparison shopping were 'totally thwarted'." (19)

There is yet another aspect to the problem: consumers have no choice but to purchase the product with no reliable knowledge about the quality of the product they are buying, that is, the ease or facility with which different insurers pay claims. "Future service is the essence of the insurance product, but the consumer cannot now evaluate that aspect at the time of purchase." (20) The NAIC Task Force on Consumer Information accordingly recommended that complaint ratio data be developed and made available to consumers (21).

Today, property/casualty disclosure is totally inadequate, Mr. Chairman, to make this industry anywhere near fully competitive. Consumers have great difficulty getting price and solvency information, and simply cannot get service information. As a result, billions of dollars are wasted by consumers in buying these vital forms of insurance.

CONCLUSION

Mr. Chairman, what needs to be done as respects insurance disclosure is re-regulation, including federal standards of disclosure to make sure that people have the information they need to shop this market. Then, and only then, can competition be effective so that deregulation of rates can be effective. The necessary information might be provided by government directly or by independent information brokers. In either case, government must gather the necessary data to facilitate complete disclosure.

In property/casualty insurance, the quality of coverage should be ranked by the government experts so people know, generally, the quality of the contents of a policy. Further, as Mr. Tobias suggested, the percent of premium expected to be paid out in claims should be disclosed. One would certainly rather purchase a policy that had an expected claim payout ratio of 80% than one with a 40% ratio. Service level information -- such as how long it takes the particular insurance company to pay claims compared to how long it takes the average company to pay claims, the percentage of claims in suit for the company compared to the percentage for all companies, the number of complaints per 1,000 policies compared to the same information for the average company -- must be disclosed prior to sale of insurance policies.

In life insurance, the rate of return on savings portions of whole life policies must, at long last, be disclosed.

In all lines of insurance, agents should be required to disclose the percentage of the premium which is paid to them as commissions (22).

People who are "good" risks based on their driving record for auto insurance, their health for life insurance, their home's quality for homeowners insurance should have the right to shop the market and act upon the information. Insurers should be denied the luxury of underwriting by whim and hunch and thus making disclosure irrelevant.

When these disclosures are in place, and when rate bureaus, anti-rebate laws, anti-group laws and other trappings of an anti-competitive past are swept away, then deregulation of ratemaking can be undertaken with the assurance that consumers will be protected by market forces.

Mr. Chairman, the states do not have the will or the expertise to make the needed changes. The consumers of the country look to the Congress for the reform that will save them tens of billions of dollars every year.

Thank you.

FOOTNOTES

(1) ". . . the business is inefficient . . . we spend too much money in distribution, administration and what is considered pure waste." John Cox, President, Insurance Company of North America.

(2) Reports of lay-offs already have been noted for many insurers. "Big layoffs are virtually inevitable," said the reporter in Will Hartford be the Next Detroit? Hartford Advocate, July 14, 1982. The Journal of Commerce of May 2,1984 reports that Fireman's Fund has laid off 1,200 employees because of "cost duplication and inefficiencies of the agency system . . ."

(3) The only major federal look at state regulation of insurance in the recent past was the 1979 GAO report "Issues and Needed Improvements in State Regulation of the Insurance Business." It found "serious shortcomings in state laws and regulatory activities with respect to protecting the interests of insurance consumers in the United States. In part, this is because GAO found that state regulation is "not characterized by an arms-length relationship between the regulators and the regulated."

(4) For evidence of the existance of extensive redlining, see, for instance, Insurance Crisis in Urban America, US Department of Housing and Urban Development, 1978; Insurance Redlining: Fact not Fiction, A report of the Midwestern Region of the US Commission on Civil Rights, 1979.

(5) Cummins, J. David and Weisbart, Stephen N., The Impact of Consumer Services on Independent Insurance Agency Performance, 1977.

(6) Issues and Needed Improvements in State Regulation of the Insurance Business, GAO, 1979, p. 95.

(7) The attitude of the agent witnesses last week is very revealing. Another witness said that customers would be "bored and irritated" if such "technical details" as how much of the premium dollar will be paid out in benefits on the "claims handling practices" (i.e., service levels) of the insurers were disclosed.

(8) Life Insurance Cost Disclosure, A Staff Report of the FTC, 1979. President Carter was moved by the findings to send a letter to all governors of the states suggesting that they require rate of return on the savings portions of life insurance policies be disclosed, citing "billions of dollars a year in unnecessary costs to consumers." Even today, no state requires such disclosure.

(9) Congress euphemistically called this the "FTC Improvements Act of 1980".

(10) 1980 Report to the NAIC by their Task Force on Life Insurance Cost Disclosure.

(11) Protection for Sale: The Insurance Industry, NBC News.

(12) How to Save Money on Life Insurance, James H. Hunt for the National Insurance Consumer Organization, 1984. Available from NICO, 344 Commerce St. Alex, VA 22314.

(13) New York Times, January 16, 1982.

(14) 1981-1 NAIC Proceedings at 361 (emphasis added).

(15) Dr. Joskow said consumers' difficulty and the need for a special role for insurance departments were due in part to the fact that comparative price shopping for insurance is different than for other products. Anyone can ask a neighbor what he or she paid for the new toaster-oven, Dr. Joskow wrote, but "price differences for comparable coverages are not readily available in printed form" and price information from friends, neighbors, or colleagues is of little use because, as he put it, "the fellow in the next office . . . is in a different risk class, lives in a different community, and drives a different kind of car." Joskow at 404.

(16) Ibid. GAO, p. 95-96.

(17) Cummins, J. David, McGill, Dan M., Winklevoss, Howard E. and Zelten, Robert A., Consumer Attitudes Toward Auto and Homeowners Insurance (Wharton School 1974).

(18) Ibid, Cummins, et.al. at 67,'71. The authors thus discounted their earlier observation that consumers appeared to be relatively indifferent to the price of insurance. They thought that if consumers "knew significant [price] differences exist, price would become a relatively more important factor."

(19) Operation of Competition Among Motor Vehicle Insurers, p.25.

(20) Ibid. GAO, p. 95.

(21) Ibid. 1981-1 NAIC Proceedings, p. 383.

(22) Even large buyers of insurance want this information. See the attached editorial from the April 30, 1984 edition of Business Insurance.

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Good Housekeeping May 1984

Money-Gram

Save up to 40% of the cost of auto-insurance premiums by eliminating certain types of coverage you don't need. Collision coverage, for example, might not be necessary if your car isn't too valuable; medical coverage may not be needed when you have adequate medical insurance. For a free booklet containing more money-saving tips on all kinds of insurance send a stamped, self-addressed, business-size envelope to: "Buyer's Guide to Insurance," National Insurance Consumer Organization, 344 Commerce Street, Alexandria, Va. 22314.

opinions

The real cost of broker services

DOES YOUR BROKER RECEIVE bonus commissions?

Chances are you don't know, and we think you ought to know.

The results of our recent survey of the *Business Insurance* Risk Management Board reveal that among a cross section of 50 risk managers, only 14—or 28%—have ever discussed these bonus commissions with their brokers (see story, page 1).

Bonus commissions are additional commissions that some insurers are paying some brokers as incentives to produce more business. Brokers, whose income has been squeezed by falling premiums, understandably are interested in the bonus commissions.

One could charge that these bonus commissions inflate an already too large expense component of the premium, especially bonus commissions paid to brokers upon placing a large account with an insurer. But, one could argue that bonus commissions paid to brokers who consolidate lines of business with a few insurers actually reduce the insurers' as well as their own expenses. And, profit commissions on a single account that does not produce many losses could encourage the broker to better assist with loss control.

Rather than debate the merits of bonus commissions at this time, we are more concerned that the existence of bonus commissions be disclosed to clients.

As the majority of the risk managers responding to our survey agree, brokers' objectivity can be influenced by the payment of—or promise to pay—bonus commissions.

Consider the broker that has whittled numerous bids down to two. One of the insurers has promised to pay a bonus commission if the broker's business with that insurer reaches a certain volume and the other insurer has no such agreement with the broker. All things being equal, who cares if the broker recommends the insurer paying the bonus commission? No one, we agree. But are all things often equal?

Consider the broker who will earn a one-time bonus commission if he places a new account with a particular insurer. Is there not an incentive to recommend that the client move the business to that insurer?

And consider the broker who will be paid a profit commission on a single account based on the profitability of the account. Where will the broker's interests lie when there is a dispute between the policyholder and insurer over a claim?

One could assume the worst and say the broker's objectivity and representation of the policyholder is undermined by these bonus commissions.

At best, we submit that a broker's objectivity and representation of the policyholder is undermined by these bonus commissions when the broker receives them without informing the client. Once the client has been informed, the client knows the broker's self-interest in recommending a market and can more carefully analyze the recommendation. And, more importantly, the client paying a fee or a negotiated commission can suggest that the broker's renumeration be reduced by the bonus commission if the client believes the bonus unfairly compensates the broker. Or the client can say, "Accept it."

Every risk manager should know what compensation a broker is receiving for placing insurance for his or her company. How else can the risk manager judge if the company is getting a reasonable quality of service for the compensation paid?

We disagree with the risk manager who equated the broker's commission to the profitablity of a manufacturer's product. In the first place, we find it demeaning to equate a broker's services with products. But, to maintain the analogy between a broker's service and a product, a broker's commission is not like a product's profit, but is like the price of a product. No one buys a product without looking at the price tag.

A risk manager should not buy a broker's services without knowing the broker's income.

Chairman RODINO. Thank you very much, Mr. Nader.

Mr. Nader, I was impressed with your initial statement commenting on the lack of coverage by any of the leading newspapers in this country and by the news media.

Mr. NADER. I might add, Mr. Chairman, the Wall Street Journal also has not covered these hearings—the Wall Street Journal. We have to go to the Journal of Commerce to learn about these hearings.

Chairman RODINO. Mr. Nader, would you please comment on the failure on the part of the press—which I consider a very grievous one indeed because this issue does affect a substantial portion of the economy—to cover these hearings? As you have concluded, a lot of the savings that might result if we were to find that insurance premiums could be reduced while maintaining effective insurance coverage might be put to better use.

Do you think, however, that failure of the press to cover these hearings or other related hearings has had any effect on the will of the insurance industry to come forth with further information in this area?

Mr. NADER. I think so, Mr. Chairman. I think it is hard to find an example in the last 20 years where Congress has initiated hearings pursuant to proper regulation of an industry, which hearings have resulted in enacted legislation, without widespread media coverage.

Widespread media coverage is the currency of democracy, and how can you get the points across to the American people, through the witnesses who come before you, and through your own statements and those of the members of the Judiciary Committee, if there are nothing but echoes in this room as a result?

If the insurance industry back in Texas, California, New Jersey, and Wisconsin saw that these hearings were being covered on television and radio and in the newspapers, I think they would be much more accommodating to the legitimate issues raised by this hearing.

Chairman RODINO. Mr. Nader, let me ask one question; then we are going to have to recess for a vote.

Mr. Nader, you make reference to the McCarran-Ferguson Act, and your statement not only suggests, but I think clearly states, that you feel that the antitrust exemption that is now accorded to the insurance industry should terminate.

The Commission which I was part of made a recommendation that we ought to at least narrow this exemption.

Do you feel that there should be a total repeal or should there be a narrowing of the antitrust exemption provided by the McCarran-Ferguson Act?

Mr. NADER. Ideally, it should be basically the end of the McCarran-Ferguson Act, but given the power of the insurance industry, we might have to settle for something short of that.

What the McCarran-Ferguson Act has done is, in effect, prevent almost all Federal regulatory impact on the insurance industry; allow State nonregulation; encourage ratemaking bureaus, in violation of standards of competition; and allow the States to regulate the consumers by anti-rebate laws and fictitious group laws.

Imagine a group of homeowners being told by the State insurance commissioner that they are a fictitious group. They look around; they say, "There's nothing fictitious about us; we live near each other."

That's the effect of the McCarran-Ferguson Act, and I would hope that it would be repealed.

Chairman RODINO. I'm going to yield to the gentleman from Illinois, since he won't be able to return to the hearing.

Mr. HYDE. Thank you, Mr. Chairman, and I deeply regret that. Unfortunately, we have the Central American title to the foreign aid bill on the floor immediately, and I'm on that subcommittee, and I have to be there.

I tend to agree with Mr. Nader. These are incredibly important hearings. Unfortunately, there isn't a bill before the committee, and they are just hearings. I say "just hearings" meaning there is no legislation as yet, and the news as theater sometimes rules out an overview of insurance.

Perhaps if we could dramatize it, they'd be interested in it, but the hearings are important, and I'm happy that the chairman is going into these matters in depth.

Mr. Nader, your statement calls for repeal of McCarran-Ferguson and seems to base its recommendation on an alleged dearth of consumer information about insurance.

Section 2(b) of the McCarran-Ferguson Act seems, however, to allow room for congressional action "specifically relating to the business of insurance." If so, why do we need to repeal the act when Congress appears already to have the power to require more consumer disclosure if it chooses to do so?

Mr. NADER. My opposition to the act transcends the consumer disclosure issue. Certainly Senator Hart came to the same conclusion that you did, but because of the whole variety of terrible regulation by the States of consumers as well as other issues—antitrust issues, securities issues—I favor the abolition of the McCarran-Ferguson Act, and thank you for clarifying that point.

Chairman RODINO. We are going to recess now. We will return in 15 minutes.

[Recess.]

Chairman RODINO. The subcommittee will come to order.

The gentleman from Michigan.

Mr. SAWYER. Mr. Chairman, I ask unanimous consent that the committee permit the meeting this morning to be covered in whole or in part by television broadcast, radio broadcast, and/or still photography, pursuant to rule 5 of the committee rules.

Chairman RODINO. Without objection, it is so ordered.

Mr. Nader, as I understand your statement, you are suggesting formation of a nationwide consumer group which would collect information and pursue various remedies on behalf of the consumer.

What exactly is your proposal? What do you envision? Is this something that the Congress would have to enact? Do you have such a proposal which you might submit to the subcommittee in writing? If so, we would appreciate it. Let's hear your comments now.

Mr. NADER. Mr. Chairman, the proposal is a simple one. Congress would charter, as it charters the Red Cross and other organi-

zations, a nonprofit, nationwide insurance policyholders group. It would then give the group the power to insert in the premium billing envelope of insurance companies its own notice, or its own message, inviting policyholders to join the group, say for $5 a year, and the policyholders would be members. They would regionally elect their council of directors, who would in turn hire the economists, actuaries, lawyers, writers, and other advocates to represent the interests of policyholders before all three branches of government at the Federal and State level, and to engage in information procurement and defense of policyholders, raise issues like why don't more insurance companies become more vigorous in the area of pollution control and health maintenance and safety, the way Allstate and State Farm have been, for example, in the area of airbags and auto safety.

In short, it's a wonderful solution to a longstanding problem, which is, how can we, with a minimum of bureaucracy and the minimum of conflict, empower policyholders to band together and defend themselves and rationalize the insurance marketplace for many good purposes and objectives?

A model for this is established in Wisconsin and several other areas of the country in the utility field. There are now two State laws—Wisconsin and Illinois—which require utility companies—electric, gas, telephone, and water—to insert periodically a similar notice by a statewide chartered consumer group open to any residential utility ratepayer, for $5 a year.

In Wisconsin there are 95,000 members; they have their own full-time staff; they proceed intelligently; they have even gotten some plaudits from electric companies. They participate before regulatory commissions, before the legislature, and they inform the ratepayer to demystify utility economics throughout the State in little meetings where the members gather to discuss the issues, and I think this is a very, very healthy development. I like to call it the frontier of the consumer movement.

I think conservatives and liberals would band together behind this idea, because in Wisconsin a Democratic legislature and a very conservative Governor both supported the legislation, and Governor Thompson of Illinois, a conservative Republican, signed this into law, because it doesn't cost the taxpayer a cent, it's voluntary to the consumer, and it doesn't build another Government agency.

Chairman RODINO. Mr. Nader, that sounds like a very fine idea. Is there such an organization in being? As you can appreciate, unless there were such an entity, it could not petition the Congress, and the Congress could not act on any application without there being such an entity. Is there such an organization in being?

Mr. NADER. No, there isn't, Mr. Chairman, because the Congress would have to create this nonprofit corporation, charter it, and give it the power to insert its message into the insurance companies' billing envelope.

You know, Congress has created corporations; they have created the Tennessee Valley Authority corporation, the Syn Fuels, and so on, and they can do this as well. It's well within the authority of Congress to do this, and it can be certainly justified on past constitutional decisions by the Supreme Court.

Chairman RODINO. Mr. Nader, in your statement, you propose a computerized system that would give the consumer information about the lowest priced insurance to meet his needs. As I understand your concept, it would be akin to the multiple listing service in real estate; is that correct?

Mr. NADER. Well, it would be more than that. It would be right at the point of sale for the consumer, and in that sense it is accessible to all, whereas the multiple listing service is pretty much in control of the realtors; so in that sense it would be accessible to all consumers directly.

Chairman RODINO. Mr. Nader, you speak of the need to reregulate insurance. In the past few years, regulation has come to be identified with anticompetitive notions, and some types of regulation are looked upon as anticompetitive.

Rate regulation, as it used to exist in some of the Nation's leading transportation industries, is an example. Other regulations—such as health and safety regulations—may be competitively neutral, at least among domestic manufacturers. But what you are proposing seems to be increased disclosure federally mandated. Would this type of disclosure be procompetitive or anticompetitive?

Mr. NADER. Well, I obviously think it would be very procompetitive. Anything that gives the consumer comparability information is information that would embarrass the high-priced company in comparison with, say, the more reasonably priced company, and if the information is not only comparable on price but it tends in the direction of comparability on service and other aspects of the insurance contract and delivery, it would only improve the quality of competition.

This is what we have seen in other areas in our country when there has been disclosure of comparable interest rates in banks in a local community or the tire quality grading system.

One cannot say that informed consumer choice is a desirable objective and then deny the consumer the information to make ever wiser and perceptive choices.

Chairman RODINO. It seems to me, Mr. Nader, that what we would have to do then to have increased federally mandated disclosure would be, frankly, to repeal McCarran-Ferguson. Wouldn't that be the case?

Mr. NADER. Well, obviously people can disagree on this, but I have no trouble with coming down on your implication, which is abolishing McCarran-Ferguson.

Chairman RODINO. And what of the FTC's role? Because McCarran-Ferguson withdraws FTC regulatory jurisdiction.

Mr. NADER. That's right.

Chairman RODINO. So in other words, all we'd have to do is repeal McCarran-Ferguson, and that would take care of everything.

Mr. NADER. Oh, yes. It would take care of the disclosure issue as well as other opportunities to rationalize the market in a more competitive way.

Chairman RODINO. From your experience—and you've had long experience—as a consumer advocate, can you tell us who is hurt most by lack of good information in this area? Does lack of information affect mostly older Americans, minority Americans, Ameri-

cans for whom English is a language that may be a little remote and distant?

Mr. NADER. Well, all consumers are adversely affected by a lack of accurate and comparable information about policy offerings and policy maintenance, but clearly poor people, minorities, the elderly are going to be hurt and are hurt more.

Just look at the hearings that Congressman Pepper had on the elderly and the Medigap scams, and just see the exploitation that is involved. I would think some of the more reputable sectors of the insurance industry would have long ago come down hard on the way these schemes are being peddled, but, once again, very good hearings, and in this case, some good coverage in the media—the Pepper hearings—but little effective action.

Some people think industrial life insurance is a thing of the past, Mr. Chairman, but it's still being sold to the poor.

Chairman RODINO. Mr. Nader, in your presentation, I think you departed from your prepared text and mentioned that example in which your parents were involved in wanting to get some group homeowners insurance and were unable to do so in the State of Connecticut.

Mr. NADER. Yes, sir.

Chairman RODINO. And you concluded by saying they couldn't do so because it was unlawful in that State to do so. Why did this happen? I really don't understand.

Mr. NADER. Well, these are called fictitious group laws—namely, that people who want to band together in a free democratic society to buy as a group are prohibited from doing so in the homeowners insurance area.

I mean it's hard to justify it, isn't it? The only reason I can see is that the insurance industry doesn't want to confront powerfully bargaining consumers. They will give another rationale. Their rationale is that each house is different and we can't make a group determination.

But insurance is sold as a group in other fields, and each policyholder is different, and actuaries have informed me that there's no reason at all why creative insurance underwriting cannot resolve these problems with proper actuarial predictability, and I think it's going to come. I think it's only a matter of time before the Supreme Court strikes down these laws.

But it just shows you how—I mean, what other industry gets away with this? What other industry gets away with the euphemisms, the escape from competition, that the insurance industry has gotten away with?

I mean, it's one thing if they said:

> Look. We are going to put the wood to you consumers. We are going to have rate bureaus. We are going to have anti-rebate laws, fictitious group laws, and we are going to regulate consumers, but in return we are going to take all this excess money, and we are going to take all these overbought insurance proceeds, and we are going to make this the safest, the cleanest, the healthiest country possible by going after the auto industry to build safer cars and going after the sources of fire which destroy so many homes, and we are going to be the sentinels, the advocates for health and safety.

Then you can say, "All right. It's a trade-off." But that isn't what you get. You get an industry that can be called a sacred cow feeding us a line of sacred bull.

Mr. RODINO. Thank you very much, Mr. Nader.

Mr. Edwards.

Mr. EDWARDS. Thank you, Mr. Chairman, and thank you very much, Mr. Nader. It is a fascinating discussion we are having—very important, I think.

To your knowledge, have the insurance companies—health insurance, life insurance, and so forth—put on useful campaigns with regard to health ideas like cigarette smoking?

Mr. NADER. Very minimal. Metropolitan Life, Prudential—they put out pamphlets. Once in a while they put out ads, but everybody knows that safety and health issues insofar as they involve toxic waste dumps and occupational disease and unsafe consumer products are political and economic power issues.

State Farm had to sue the Reagan administration to win the case in the Supreme Court that the Reagan administration's revocation of the auto crash protection standard was unlawful. They could have put an ad in; they could have put pamphlets out. They had to engage the arena of legitimate power decisionmaking, and I think Metropolitan Life and Prudential are two of the worst examples of abdication in this regard.

Just look at their assets. I believe that the assets of the insurance industry are something like nine times that of the oil industry. We are talking about cash cows of unbelievable quantification.

Think what they could do in areas close to your heart, of cancer prevention, fire prevention, and accident prevention, by making the engineering systems built in this country—the products built safer. It's just—it's not in the cards.

They should have their own testing laboratories. They should be watchdogs, sentinels, in this area, just out of the theory of claims reduction or loss prevention, just as Lloyds of London 300 years ago started requiring ships going to the Indies to have lifeboats and put lighthouses up, because they didn't want the ships to get wrecked, and pay out claims when they assembled in the coffee houses to figure out their profit and loss.

It's too bad the insurance industry today, with a few exceptions, exceptions which only prove the potential here, has done so little. It is because it has been so comfortable; it hasn't been provoked and challenged; and it is only strong consumers, banding together, who are going to provoke that challenge and also provide the climate for Congress to act.

Mr. EDWARDS. Well, there is so much ignorance about the issue. Also, people can't understand what they are signing when they buy an insurance policy, and they trust their local State Farm agent, who, after all, is a neighbor.

In California of course, the insurance commissioner is a political appointee of the Governor and sways with the wind. Whoever is the new Governor, you will notice almost immediately a great change in one way or the other in the enforcement of the California insurance laws.

Mr. NADER. Except, I must say, in California there hasn't been much change under either Jerry Brown or Deukmejian. The two

commissioners have been very pro industry, and that's—you might have chosen another State but California. Maybe New Jersey is a good example. There was a strong insurance commissioner in New Jersey.

Chairman RODINO. We did have one, yes. Hopefully he is going to testify before this subcommittee.

Mr. EDWARDS. If there was active competition, which is the basis of business in the United States, would you run into difficulties with some of these companies going broke and leaving policyholders hanging out there?

We have had problems in the past—I don't know if it has been true recently—when some States have been so lax about the financial situation and the qualifications for becoming an insurance company that buying an insurance policy is almost a joke, because if you ever had a loss, they wouldn't be able to pay more than two or three of them.

Mr. NADER. That's a good point.

Certainly there have been examples of poor regulation in the area of assuring solvency, and that again is an area that needs to be strengthened. The *Baldwin United* case has certainly not been a very encouraging sign here.

How some of these debacles can go on and on before they are uncovered, months and months, and yet you say:

> Hey, there are dozens of insurance commissioners who are supposedly supervising these companies. How come they missed it? How come their staff missed the danger signals?

As you can imagine, Baldwin United is a very, very sizable failure.

Mr. EDWARDS. Well, do you think that the exclusion from McCarran-Ferguson and the resulting benefits to the insurance industry have resulted in exorbitant profits and exorbitant salaries and benefits for the officers?

Mr. NADER. To some degree of course, although insurance company salaries are not as high as some of the ones you have been reading about in the papers recently.

Mr. EDWARDS. No; there's no way.

Mr. NADER. But it goes deeper than that. It's the gross, institutionalized inefficiency of what is collected by way of premiums, and what is paid out, and what is left over in the layers of bureaucracy and in the way insurance is marketed.

I think the insurance industry could teach the Federal Government a point or two about wasteful bureaucracy and layers of marketing without adequate value being returned to the policyholder.

Just look at some of the comparisons. I mean I'm sure your record is replete with examples of how insurance can be marketed efficiently and of how people can get a higher return on their premium dollar.

Mr. EDWARDS. Thank you very much. You are making a great contribution to our deliberations, Mr. Nader.

Mr. NADER. Thank you, sir.

Chairman RODINO. Mr. Sawyer.

Mr. SAWYER. Thank you, Mr. Chairman.

I understand that Wisconsin's utility mailing situation that you have alluded to is not really operating very successfully and is going to require some kind of State subsidy if it is going to keep going. Do you know anything about that?

Mr. NADER. Do you mean—are you referring to the utility group?

Mr. SAWYER. Yes.

Mr. NADER. Oh, no, sir, there is no State subsidy.

Mr. SAWYER. Not yet, but that they are anticipating there will have to be, or it is not going to keep operating, so I have heard.

Mr. NADER. Oh, no, no; it's on it's own. The statute in effect says it stands or falls on the level of its membership, which is voluntary.

Mr. SAWYER. Is it working?

Mr. NADER. Indeed it is. In the last few months, it has been working quite spectacularly. For example, on the merits, the consumer utility group defeated the telephone company's local measured rate service proposal.

Mr. SAWYER. Are you suggesting that we ought to, in effect, convert the insurance industry into a public utility?

Mr. NADER. Well, obviously, given the fact that it is regulated, it is viewed in some degree theoretically as having utility characteristics, but I agree with you, you can't possibly ascribe that characteristic to it now.

No; what I'm interested in doing is exposing it to greater competition, eliminating the regulation of consumers implicit in State antirebate and fictitious group laws, et cetera, and empowering policyholders to band together for more intelligent advocacy and more intelligent choice in insurance offerings.

Mr. SAWYER. But there is no law now prohibiting policyowners from banding together and doing anything they want, is there? And what you are suggesting is that government, in effect, do it for them.

Mr. NADER. No; I am suggesting the Government provide a facility, just like the Government has provided a facility for the beef producers and the cotton producers to get together and promote their wares.

Over at the Department of Agriculture, by the way, there are a few tax dollars being spent maintaining or supervising these kinds of marketing pools. There would be no money spent in the proposal—no tax money spent in the proposal that I mention. All it is is simply using the unused postage in the billing envelope to insert a message.

Mr. SAWYER. Well, you can refer to the unused postage, but there is a significant cost involved in stuffing envelopes, you know. I know that from just being in politics.

Mr. NADER. The cost is paid by the consumer group, as it is in Wisconsin. The printing, all the marginal costs, are paid by the consumer.

Mr. SAWYER. And the cost of handling the insertion and everything else?

Mr. NADER. Yes; with machines, it's very minimal, but it's paid by the consumer group.

Mr. SAWYER. I understand also that California, to which you alluded as being rather pro industry, as I recall your answer to Mr.

Edwards' question, is—perhaps has the lowest insurance rates in the country of any State.

Mr. NADER. Well, I'd have to look into that and see what——

Mr. SAWYER. Well, aren't you familiar with that? You seem to be familiar with the California system.

Mr. NADER. Well, I'm not familiar with the assertion that they have the lowest rates in the country.

Mr. SAWYER. And that New Jersey, that you alluded as being perhaps the most regulated, has among the highest in the country; is that true?

Mr. NADER. As you know, the density of vehicle population, if you are talking about auto insurance——

Mr. SAWYER. I'm talking about insurance in general.

Mr. NADER [continuing]. Is often used as an example. Given New Jersey's exposure to toxic chemicals and industrial pollution, I can imagine how the disease levels might be higher than in sunny California.

Mr. SAWYER. Well, in California they have just a kind of file-use rate system, as I recall it. You just file your rates and go ahead without any administrative oversight or hearings on it and let the marketplace fix the rates, and they come out with, as I understand it, the lowest rates in the country. You don't know that?

Mr. NADER. Again, I can certainly look into that. I believe that Mr. Hunter is going to testify before the subcommittee. You might ask him. He is quite aware of the various State levels.

Mr. SAWYER. You alluded to New Jersey though, and it has perhaps the—perhaps the most—highest degree of regulation and least reliance on market forces, and it has, as I understand it, the highest insurance rates in the country. Doesn't that tell you anything at all?

Mr. NADER. Are you talking about auto insurance?

Mr. SAWYER. Insurance in general.

Mr. NADER. Well, I can't verify your statements, so I'll have to suspend judgment on it. Perhaps the chairman may——

Mr. SAWYER. Well, automobile would be included, but property and casualty would be included, too.

Well, anyway—incidentally, if we repealed McCarran-Ferguson, obviously you'd have to have some substitute legislation, wouldn't you?

Mr. NADER. Well, no, you don't have to.

Mr. SAWYER. You'd subject the insurance companies to violate the antitrust law, because they'd engage in pooling and all this other exchange of information, which is in violation of the law.

Mr. NADER. But that's longstanding legislation. That's already on the books. You said you'd have to have——

Mr. SAWYER. I'm talking about McCarran-Ferguson, is the one that gives the exemption from that.

Mr. NADER. That's right, but if you abolish McCarran-Ferguson, then coming into play would be the Sherman and Clayton antitrust laws, which have been on the books, as you know, for years.

So the question you asked is, does this mean that new legislation is needed? I'm saying not necessarily. I would recommend some new legislation, but it's not triggered by the abolition of the McCarran-Ferguson Act.

Mr. SAWYER. Are you familiar with the Shenefield Commission?

Mr. NADER. With—yes.

Mr. SAWYER. That studied this——

Mr. NADER. Yes—the antitrust—yes.

Mr. SAWYER. They said that you'd have to——at the same time that you repealed McCarran-Ferguson, you'd have to replace it with a more narrowly drawn statute which permits certain kinds of collective activities by insurance companies, to include, for example, the joint collection and use of statistics on loss experience in the casualty insurance area and, two, joint pooling action to provide coverage for certain high risks, especially the automobile insurance areas.

So you would have to have—you agree with that, don't you, that you'd have to have some substitute?

Mr. NADER. No, no. What——

Mr. SAWYER. You don't agree?

Mr. NADER. What the Shenefield Commission was implying was that if you took off the protective cover of McCarran-Ferguson, the antitrust laws would have to be enforced against rate bureaus and pooling of data if the antitrust chief felt that they were violating the antitrust laws.

Mr. SAWYER. That's what it was inferring, or you think it was inferring. It suggested that they should be replaced with a more narrowly drawn statute that would permit these kind of activities, which otherwise would be in violation of the antitrust law. Isn't that true?

Mr. NADER. Exactly, but I disagree with them. I don't think the rate bureaus serve any useful function at all, other than to reduce price competition.

Mr. SAWYER. So you disagree with the Shenefield Commission; is that what you are saying?

Mr. NADER. In that regard, yes.

Mr. SAWYER. In 1979, the Federal Trade Commission was going to step into the field of insurance regulation, which has historically been handled by the States.

Mr. NADER. They were going to step into the field of insurance industry investigation.

Mr. SAWYER. Congress prevented that without prior approval—right?

Mr. NADER. Which I thought was a terrible decision. The idea of telling an independent regulatory agency that it can't even look into a problem unless it gets the OK of a House or Senate committee is just testimony to the awesome power of this industry. I can't conceive of any other industry being able to pull something off like this without upsetting the status and dignity, integrity, and pride of the U.S. Congress.

Mr. SAWYER. Back in the 1940's—and I forget now the name of the decision; I was at one time involved with it—but the Supreme Court decided for the first time that the business of insurance was commerce. Do you recall that decision?

Mr. NADER. Yes.

Mr. SAWYER. But, however, it very expressly provided in some followup legislation, that resulted in applications to abolish or declare illegal retaliatory taxes that some of the States have on in-

surance premiums and so forth, that the insurance industry, however, would remain, as it always has been, under the control of the individual States. Do you recall that?

Mr. NADER. Yes.

Mr. SAWYER. You think we should usurp all of the State regulations then and pull them into the Federal Government; is that what you are suggesting?

Mr. NADER. No; I favor dual State-Federal regulation, as occurs in many areas in our country—banking, for example.

Mr. SAWYER. You are in favor, then, of pyramiding more regulation and more administrative tribunals and bureaucracies; is that what you are suggesting?

Mr. NADER. No; I am in favor of more regulation where there is none now and where consumers need it, but I also am in favor of abolishing some of the regulatory statutes at the State level, as I mentioned, like the anti-rebate and fictitious group laws.

But I would rather end up with a system, sir, where there is much more higher quality competition and where consumers are empowered to bargain and to challenge in furtherance of their own insurance interests.

Mr. SAWYER. In your view, you foster better competition in the marketplace by more Government regulation; is that right?

Mr. NADER. Well, if you call antitrust law enforcement and securities law enforcement Government regulation, you are right. Most people look at this as setting the rules of the game so that competition, solvency, and nondeceptiveness prevail.

The more traditional definition of "regulation," where they say specifically, "Thou shalt not do this; thou shalt do that," is now being done by quasi-governmental authorities called rate bureaus, controlled of course by the insurance industry, and that I would like to see ended, thereby reducing bureaucracy and reducing this kind of detailed determination of rates.

Mr. SAWYER. I yield back, Mr. Chairman.

Chairman RODINO. Thank you very much, Mr. Nader. We appreciate your presence here this morning.

Mr. NADER. Mr. Chairman, I'd like to submit for the record some examples illustrating my points of insurance industry abuses as well as perhaps some more materials on the proposal for the nationwide consumer organization.

Chairman RODINO. Without objection, the subcommittee would appreciate receipt of that material.

[Material in the appendix at p. 647.]

Mr. NADER. Thank you.

Chairman RODINO. Thank you very much, Mr. Nader.

Mr. NADER. Thank you for holding the hearings.

Chairman RODINO. The second panel consists of Ms. Ann Haney, Mr. Donald Segraves, and Ms. Nancy Golonka.

Would you please come to the witness table?

We will ask Ms. Haney to begin. If you will, please summarize your statements, and then we'll ask questions.

TESTIMONY OF ANN HANEY, DIRECTOR OF CONSUMER AFFAIRS, AMERICAN FAMILY MUTUAL INSURANCE CO., MADISON, WI; DONALD W. SEGRAVES, EXECUTIVE DIRECTOR, ALL-INDUSTRY RESEARCH ADVISORY COUNCIL, OAK BROOK, IL; AND NANCY GOLONKA, VICE PRESIDENT OF CONSUMER AFFAIRS, INSURANCE INFORMATION INSTITUTE, ATLANTA, GA

Ms. HANEY. Thank you, Mr. Chairman, for the opportunity to testify today.

Before I start with my prepared comments, may I make some comments in response to Mr. Nader's discussion of the Citizens Utility Board?

Chairman RODINO. Yes, you may.

Ms. HANEY. Thank you very much. That's an issue that's very near and dear to my heart.

I think there were very few people outside of the initial movement to establish CUB in Wisconsin—which is the Citizens Utility Board—who had more interest in the success of that board than myself.

At that time, I was the head of the Wisconsin Department of Regulation and Licensing. That department regulated 26 different businesses and health professions, gambling, and other entities.

In that department there were 17 regulatory boards. All of them were dominated—I thought, at least—by the interests that they were supposed to be regulating.

What I was trying to do at that time was get more consumer members, more public members, on to these boards.

Watching CUB, then, was very important to me—what happens when citizens, when consumers, when the public has more say in what happens in Government.

I was there, as a matter of fact, when that bill was passed by the Wisconsin Senate, and I was also there when the Governor signed the bill, again, trying to gather more information about what is supposed to happen here.

Mr. Nader mentioned that there were 95,000 members of CUB in Wisconsin. I would question that number, but, on the other hand, I myself do not know the exact number.

He did mention something that I thoroughly disagree with. He said that this was a self-supporting, quasi-governmental structure in Wisconsin, and to my understanding, it's not. As a matter of fact, last summer there were fierce battles in the Wisconsin Legislature during the budget session, because when CUB was created, it was supposed to be self-sustaining after 3 years. That was the argument—the public will pay this small sum, $5, and it will cover all of our costs to stuff envelopes and do all these other things.

Now, again, I am wracking my memory to try to remember what finally became of that—whether it became State-subsidized continued, or industry-subsidized continued, but I know that they are not in the good financial state that they thought that they would be. I don't know why.

He also mentioned that the Governor—even a conservative Governor, had supported CUB. Again, this is the Governor I worked with on a daily basis. I was there when he signed the bill, and he paid his $5 to join. When he signed the CUB bill, he said that he

was doing this to show his support for consumers but he was still uncertain that this was the right way to go.

In fact—and I still remember it, because it made so much sense--he said he was really sorry that at this point in time consumers had become their own special interest group.

The single-mindedness that comes with an advocacy group, inability to compromise, to work with a situation as it is, to move the system along rather than fight it—this is the kind of thing that the Governor had apprehension about at that time, so it wasn't complete support.

He also had some concern because the push for CUB was coming from questionable—let me not say questionable, but he wondered where the support for that was coming.

This was a man, Governor Dreyfus, who was elected—he was a populist—and he was elected by out-State people.

So the people out-State were really electing Governor Dreyfus, and he was wondering why none of those people were people that he was hearing from; it was the city folks who were pushing for this, who knew what consumers wanted specifically.

But now Mr. Nader and Mr. Hunter want some kind of congressional approval for their own fan club. There again, that's bothersome to me. It's bothersome that someone—I'm from the Midwest, from Wisconsin—Mr. Nader himself called it the frontier of consumerism—and this proposal is coming from a group of people, specifically, a man who is concerned about his diminishing media appeal.

In Wisconsin, CUB is headed up now by a very—by a shrill advocate, someone who has disenfranchized many of the consumers, many of the people, like myself, who originally hoped that CUB would be a success.

Thank you, Mr. Chairman. I'll try to summarize and be brief on my comments.

You asked whether there is adequate consumer information for the insurance marketplace to work competitively. I believe that there is. My comments will be from the perspective of a former State regulator, and for a portion of that time as insurance commissioner, and now as director of consumer affairs for American Family Insurance. That's a property and casualty insurer in 11 Midwestern States.

From that background, I can assure you that the problem is not adequate information. Our big problem in the industry is the same problem that consumers have, and that's getting the information out so people can use it.

I further maintain that from the insurer's perspective, it's the informed consumer who makes our best customer, and that's what we believe in.

So right now, the industry is going through what we call underwriting losses—that is, that we are paying out more in claims than we are taking in in premiums. We are getting integrated with all kinds of financial services and products. We have this congressional review, which we agree is very important.

We have some adverse popular literature, which has been referred to earlier, and we are dealing with the usual anti-industry type of media that is coming out.

At any rate, we still seem to prosper, and I say seemingly because it has been a difficult financial management task to prosper under these circumstances.

The unspoken premise in this hearing seems to be that if consumers only knew—if they only knew, then they'd buy less, and then hopefully the seeming prosperity of the insurer would diminish. Again, this is from the testimony we heard earlier about some unknown outraged consumer, which I, in my position, have not seen.

But the idea that insurers somehow can keep consumers in the dark all of their lives is absurd when you consider the kind of age that we are living in right now.

So how do insurers inform consumers, and why is it that the informed consumers are the best customers? Let me list a few reasons.

First of all, informing consumers. How is it that we do that? Well, we do all of the things that you are going to be hearing about—the pamphlets, the consumer organizations, the industry organizations, everything like that—but the company has decided to do one more thing, and that is to tell consumers what they want to know. So, we do that; we answer their questions; we answer our mail; we answer our phone calls; and if they want to know, we try to tell them, and we try to tell them in words and phrases that we can all understand.

In this way, we do not decide for the consumer what information he or she wants. We respond to them directly.

It has been my experience that too often officials and advocates are quick to decide what consumers need. This is a nice trustee relationship. You assume a lot of responsibility this way, but you don't acknowledge the first and foremost right of any consumer, and that is the right to ask a simple question and get a reasonable answer. That's what we are trying to do.

But in addition to our nobler intentions of making sure that all consumers get information and their rights, we are also very cognizant of our regulator, because that regulator is close to the people in our State, and that's our market. The regulator is close, not far away, not in some forgotten bureaucracy, not without a face—a faceless regulator, but he or she is right there in our State.

So we have become enlightened that to give consumers information and to communicate is our wisest course of action under the circumstances.

We have a lot of consumers who want just the facts. They don't want to follow lengthy hearings in the newspaper. They get lost in long speeches of advocacy groups. When they call, when they write, or when they talk to an insurance person, they just want facts.

Our agents tell us that the most popular mode of communication right now for any consumer is to simply call his or her office, and they say, "Put it in writing. I want to take this out and do my own independent shopping. Don't call me again. I'll call you." And under those circumstances, we still prosper. Why? Because we give them the information that they want.

The argument has been put forth by some that products vary so greatly and consumers cannot perform adequate comparisons. Well, I would maintain that that's becoming less and less of a prob-

lem, the reason being that our competitors are giving the information, and if we don't, we won't be able to compete and survive.

With all of the availability of the different financial products and institutions, it's going to be the financial provider that best communicates and serves the needs of the consumer that survives.

The inaccessible financier with useless and confusing consumer information is dead, and we all know it in the industry.

Two very important consumer information areas are left to discuss before I talk about why I think the informed consumer is really our best customer. One is the technical decisions, and the other is the company's financial status.

Now, technical decisions are no small matter. They have a tremendous impact on the consumer. It's whether or not a claim is paid, how a person or property is underwritten, and it has to do with the pocketbook.

So when a person—let's take the example of a person—a policyholder where there is a decision made that the policyholder will become part of the nonstandard policyholder group. Whether the person is a current insured or prospective customer, it is vital that the insurer clearly communicate the criteria that went into that decision, and those criteria which will enable the consumer to return to preferred rates.

Now, in earlier times we didn't get the picture on this. We didn't quite see the market there, and right now our movement is to inform those consumers in that nonstandard market, work with them, educate them to bring them back to the preferred rate status.

So in this way, good communications and straightforward reckoning in decision-making creates and maintains a good business market.

How about information on the financial status of the company? Well, we do, you know, what we are required to do, and we do it in very specific terms. We submit our financial—annual financial statement to the—each of our commissioners and anybody else who wants it, and we also issue a financial report to the public. It's a nice summary of our business for the year and comparison of prior years.

But these have not proven to be real blockbuster consumer information items. So what do we have to turn to when people aren't interested in reading the financial statement or the annual report?

We turn to our commissioner. The State commissioner understands that, when a casualty or any kind of company goes under, that consumers pay millions of dollars in insurer assessments by guarantee funds in the 50 States set up to cover the losses of bankrupt companies.

Now, these failures shake the consumer's confidence in insurance, which is exactly the element—peace of mind—that we are selling. So given the scenario, we turn to the regulator.

Now, what does the regulator's office do at the State level? I was such a regulator, an insurance commissioner, and I have to say that I was terribly impressed with the number of consumers who called my office to ask before they purchased insurance. As a matter of fact, many of them called—we had many more consum-

ers call when there was any hint of any financial problem, and there is a financial grapevine out there for consumers as well.

In addition to consumers calling in, there is tremendous local media interest in just how well the consumer—the insurance department is doing.

Now, I maintain that a small casualty company in Wisconsin affects a lot of consumers, consumers right there, and that company is going to get far more attention from the State regulator than it will from the Federal bureaucracy.

Quickly now, I have, I think, four or five reasons why I think you should believe me when I say that the informed customer is really our best customer.

Obviously, the informed consumer makes wiser choices among products, has fewer problems, and is consequently a less costly consumer or policyholder for us to keep on our books.

It costs money to put business on the books, and you have heard from Mr. Nader all of the different places that we have been spending our money lately, some of them very invalid.

At any rate, when people don't have enough information to make a good decision about their insurance, they leave our company shortly afterwards, or leave any company, and when they leave the company, it causes a lot of costs, and they have really not brought in enough money. So it's important to us to have an informed consumer right at the outset to maintain that good, solid book of business in the long run.

Second, the informed consumers are better buyers of insurance. Contrary to what we have been hearing here, it is not my opinion that when consumers find out the real truth, that they stop buying insurance; they start buying it, and they insure adequately; they know what they are buying; they understand the coverages and the limitations; they cooperate with us on arson investigations, on child safety restraint projects, on drunk driving education. That's the informed consumer, the one that we want, the one we are trying to create.

Third, the informed consumer means less litigation and expensive misunderstandings. Also, the informed consumer takes up less time of the consumer affairs director.

Today in Boston there are, I think, about 200 other people who have my job in different insurance companies across the Nation, and what are they meeting on? They have five major topics, and in all areas they are exploring new ways to get information out to consumers, to develop that informed consumer policyholder.

Finally, companies are coming to the conclusion that the informed consumer is the key to the industry's longstanding problem with public perception. We have to have consumers who understand that a well managed, financially stable company that even, yes, prospers, is in their interest in the long run.

You asked whether there is adequate information for the insurance market to work competitively. In my opinion, yes, and by virtue of the current sentiment and technology, it is the consumer information that eventually will determine which one of us survives, and we hope we all will.

Thank you, Mr. Chairman.

[The statement of Ms. Haney follows:]

Statement of Ann J. Haney
Director of Consumer Affairs
American Family Insurance

You asked whether there is adequate consumer information for the insurance marketplace to work competitively. I believe there is. My comments will be from the perspective of a former state regulator of insurance and two dozen other businesses and professions. For the past year, I have served as the Director of Consumer Affairs for American Family Insurance, a multiple lines property and casualty insurer operating in eleven (11) midwestern states. Speaking from this background, I can assure you that the problem is not adequate information, it is how to get all of the available information out, and in a form consumers can assimilate and use in wise decision making. I further maintain that from an insurer's prospective, the informed consumer is our best customer.

Insurance is currently experiencing a period of:

* underwriting losses
* integration with other financial industries and subsequent competition with new financial products
* Congressional review and regulatory agency study and investigation
* adverse popular literature
* and dealing with our own share of anti-industry zealous advocates.

In spite of all of this activity and attention, insurers seemingly continue to prosper. I say seemingly, because it has been a difficult financial management task. For some there is only one reason for this resiliency, and that is there must be inadequate consumer information. The unspoken premise here is that if consumers only knew, they'd buy less, and the apparent prosperity of insurers would diminish. But the issue for those who believe this is their disdain for prosperity, not the consumer's need for information. To date, we've heard very little about exactly what kind of information it is that consumers need and more importantly how to furnish this information in a timely manner allowing consumers thoughtful selection. The idea that insurers can somehow keep consumers in the dark all of their lives is absurd. You have only to consider the technological age in which we produce and consumer to dispel this nonsensical notion.

How do insurers inform consumers? And, why is the informed consumer the best customer? Here are some practical and real examples of one insurer's efforts, and a discussion of the state insurance department's role in consumer information.

Informing Consumers

While we use pamphlets, premium inserts, publications and insurance and consumer information organizations, American Family has decided that one of the best ways to inform consumers is to tell them what *they* want to know, i.e. answer their

questions - all of them. To do this, the Company hired a former regulator and public servant, and charged me with responding to consumers in words and phrases that we can all understand. In this way, we do not decide for the consumer what information he or she wants, we respond directly to their calls and letters. It's been my experience that too often officials and advocates are quick to decide what consumers need. Although this "trustee" type approach is necessary to some extent, it seems to me that first and foremost among consumer rights, is the right to decide for themselves what they want to know and have their questions answered accordingly.

In keeping with the consumer's right to know are the important elements of availability and accessibility. In addition to our nobler intentions to afford consumers' rights, is the Company's awareness of state regulation. The near proximity of the state regulator to the public, our market, has proven to be a remarkable motivator. Further, even a cursory review of state insurance department personnel and resources, shows a substantial allocation to market conduct, (consumer related services) which in some states equals or exceeds the financial conduct component. To summarize my point, the unabashed inquiries and complaints of consumers, coupled with a state level regulator, known and accessible to those consumers, have enlightened insurers to the fact that full consumer information and communication is a wise course of action.

Many consumers have indicated to us that, at least in their insurance purchasing activities, they want just "the facts." To respond to these consumers, our agents are becoming computerized in their operations. Our agents tell me that it is the prevalent mode for a consumer to call in and request a quotation for certain individualized coverages, which he/she will ask to be mailed, so as to comparison shop. The argument is put forth by some, that products vary so greatly that consumers cannot perform adequate comparisons. I would maintain, that this is becoming less and less of a problem. Although consumers must and should be allowed to decide which product they wish to purchase (and those products do vary) the insurer must constantly look for new ways to condense and make the overwhelming amount of information more easily assimilated by the consumer. With the availability of products from any number of different financial institutions, it will be the financial provider that best communicates and serves the needs of the consumer that survives. The inaccessible financier with useless and confusing consumer information is dead.

Two very important consumer information areas remain to be discussed, technical decisions and company financial status. Technical matters include claims settlements, underwriting decisions and general policy administration. They have tremendous impact on the consumer. As an example, the decision to classify an auto policyholder as nonstandard, brings with it higher premiums. Whether the person is a current insured or a prospective customer, it is vital that the insurer clearly

communicate the criteria that went into that decision, and those which will enable the consumer to return to preferred rates. In earlier, less informed times, we did not realize the value of such a market. It is not unusual for our nonstandard insureds to move to preferred rates through increased awareness of the need for safety and improved driving. Good communications and straight forward reckoning in decision making, creates and maintains good business.

Information on the financial status of the company is perhaps the most difficult to get out in a manner which is comprehensivle and useful to the general public. In this area, we publish an annual report, and file an annual financial statement with state regulators. Neither of these tools, however, have proven to be blockbuster informational items with consumers. They should be; because it is the "Slippery Rock Casualty Company" that costs consumers millions of dollars in insurer assessments by guarantee funds in 50 states, set up to cover the losses of bankrupt companies. These failures shake the consumer's confidence in insurance -- when it is exactly that element, peace of mind, that we are selling. Given this scenario, what's the best way to keep consumers informed? Through the state regulator's office. Here is a believable source that is accessible to the consumer. As a regulator, I was impressed with the number of consumers who contacted my office before buying insurance. I was astonished by the direct and immediate questions of the media (and some consumers) whenever there was a hint of

financial trouble with one of our licensed insurers. To summarize, local consumer interest and media pressure are more likely to bring state than federal attention to the problems of "Slippery Rock Casualty Company."

The Informed Consumer - Best Customer

Why is the informed consumer our best customer? First, informed consumers make wiser choices among products, and have fewer problems and consequently are less expensive to deal with in the long run. It costs money to put business on the books. All new business needs to be clarified as to proper classification and nature of the risk. Further expenditures are made for sales fees, policy production and any initial services to familiarize the policyholder with the coverages. New policyholders who leave the company are expensive to all insureds. It is vitally important that the applicant have sufficient information to make long term decisions.

Secondly, informed consumers are better buyers of insurance. They adequately insure, they understand the coverages and limitations, and most importantly, they cooperate with and support those programs that keep rates competitive, such as arson investigations, child passenger restraint programs, and drunk driving education.

Thirdly, the informed consumer means less litigation and expensive misunderstandings. Insurers across the country are recognizing the simple financial advantage of keeping the

information moving to and from consumers. In Boston, today, a national organization of insurance consumer affairs people are meeting to explore ways to get information out and create that informed consumer and good customer.

Finally, companies are coming to the conclusion that the informed consumer is the key to the industry's long standing problem with public perception. Lately, the emergence of many financial products being compared and purchased by a broad range of consumers, has shown us the intrinsic value of a knowledgeable customer. These consumers understand the extent to which an insurer must justifiably prosper, and, how in the long run it is in their interest to have stable, well managed institutions. The well informed consumer is our best critic.

You asked whether there is adequate consumer information for the insurance marketplace to work competitively. In my opinion, yes. And, by virtue of current sentiment and technology, it is consumer information that will drive the market.

Chairman RODINO. Thank you.
Mr. Donald Segraves.
Mr. SEGRAVES. Thank you, Mr. Chairman.

I've been involved in developing communications with insurance consumers for the past 25 years. The last couple of years, I've been executive director of the All-Industry Research Advisory Council. I was involved in the creation of the Council about 7 years ago to do research on public policy issues, a lot of it consumer-oriented kinds of research.

I'm here at your invitation to talk about the two major questions you pose; that is, whether there is adequate consumer information for the marketplace to work competitively, and what types of information are important to individual buyers.

We have been asking consumers about those kinds of questions since 1980 in a series of surveys that are conducted for us by Yankelovich, Skelly & White. We do that every year. We include some auto insurance consumer questions on those surveys each year.

In addition to that, we currently have under way a much more comprehensive effort to ask consumers about their auto insurance shopping behavior. The Council decided to do that in March of 1983, some weeks prior to Congress' request to the FTC to study those same issues. We did that because we have been making strenuous efforts to improve our communications with consumers in recent years, and we needed to know how well we are doing.

I think these hearings have demonstrated that we cannot rely on our more vocal critics to give us that kind of feedback. It appears to me that they are still rehashing the old charges from the 1960's and 1970's. We decided to go directly to the people who buy our products and find out from them, from their own mouths, what they think about it.

When we found out that the FTC was going to conduct a study in similar areas, we contacted Mark Plummer and his associates; we told them of our plans; and we offered to share our findings with them as they became available.

We have been following through on that offer, and we will be providing additional information to them this summer when we get the results of two consumer surveys that are currently under way.

I would like to summarize what we have learned from our research thus far, recognizing that some of it is still in the field. One is that consumers are showing an increasing tendency to shop around for the best buy in auto insurance.

Each year since 1980, we have asked consumers what actions they have taken to lower their auto insurance costs during the past 3 years. Four years ago, 25 percent said they looked for a company that charges lower prices, and 15 percent said they had actually changed companies as a result.

In 1983, the most recent data we have available, the percentage who said they shopped around had risen to 31 percent, and with 20 percent actually changing companies.

Now, we have some preliminary indications from our current work that these numbers substantially understate the percentage of consumers who actually shop around. You will note that the question was directed only at shopping around for lower prices and does not reflect people who shop around for other reasons.

In our current research, we are going to be asking a series of questions that will get at those additional reasons for shopping.

Second, consumers are feeling more self-confident about their knowledge of auto insurance and about their ability to shop wisely. In 1980 and again in 1982, we asked the question this way: How well informed are you about what auto insurance is and how to buy it?

Seventy-four percent said they considered themselves at least fairly well informed in 1982, and that was up from 63 percent who gave that response in 1980.

Third, consumers have a wide variety of information sources available to them, and in the written testimony I cite some of those sources from the States that you represent.

Our surveys indicate that consumers make use of all of these sources to some extent. However, the three sources they consider most valuable to them are as follows: "Reading your own insurance policy" was No. 1. Second was "people you know"—relatives, friends, neighbors, or coworkers—and third was "insurance agents." These three sources were all rated as important sources for learning about auto insurance by more than 70 percent of the vehicle owners we surveyed.

Among the other sources that were listed, about half the respondents said "published rate comparisons" and "insurance company advertising."

Four other sources were rated as important by just over one-third of the respondents: "government booklets;" "stories in newspapers, TV, or radio programs;" "insurance company mail;" and "magazine articles."

Now, what consumers seem to be telling us with those responses is that they want information and advice specifically geared to their own situation rather than general information aimed at statewide or country-wide audiences.

In this connection, I heard several witnesses earlier in these hearings make remarks about the difficulty of reading your insurance policy. Yet our surveys show that consumers consider reading their policy the single most valuable source of information to them. Furthermore, there was a strong correlation between reading their policies and feeling well informed about auto insurance.

We found some 68 percent of vehicle owners said they had read part or all of their policies, most of them within the past 3 years. Among those who said they had read all of their policy, 90 percent said they were at least fairly well informed about the subject. Of those who said they had read part of their policy, 80 percent were well informed.

By contrast, among those who said they had never read their policy, 47 percent considered themselves very well or fairly well informed.

Nearly all auto insurers have rewritten their auto policies in recent years to simplify the language and to make them more understandable. I don't know how much that contributed to these improving results, but it's obvious that people are shopping more and that they are feeling more competent to shop wisely within the last 4 years, perhaps for a combination of reasons.

I would be glad to answer any questions you may have, Mr. Chairman.

[The statement of Mr. Segraves follows:]

TESTIMONY OF DONALD W. SEGRAVES, EXECUTIVE DIRECTOR
ALL-INDUSTRY RESEARCH ADVISORY COUNCIL

Mr. Chairman and Members of the Subcommittee:

My name is Donald W. Segraves and I am Executive Director of the All-Industry Research Advisory Council, located in Oak Brook, Illinois. The Council was formed by the property and casualty insurance business to do research on public policy issues affecting risk and insurance. We make our studies readily available to anyone who requests them.

Let me make it clear from the outset that I am not here in an advocacy role. We take no policy position on McCarran-Ferguson or on any other legislative issue. The associations and companies that support the Council's research program have people here in Washington to speak for them on those policy matters.

I am here at the invitation of the Subcommittee to talk about research relevant to some of the issues raised in these hearings. In your correspondence, you indicated that the Subcommittee wanted to know "whether there is adequate consumer information for the marketplace to work competitively." You also indicated that you would like to know "what types of information are important to individual buyers of personal and insurance" and whether those types of information are available to consumers.

The Council has been asking consumers some questions about those issues since 1980, and I will share our findings with you. In addition, we currently have underway a much more comprehensive research effort to find out directly from purchasers of auto insurance what kinds of information they ask for, and how satisfied they are with the answers they receive. This research already had been decided upon when Congress asked the Federal Trade Commission to

conduct a study of auto insurance shopping behavior. Fortunately, we were able to expand it to include items of particular relevance to that study, and we have kept the FTC staff informed of our plans so they can make use of the research to the extent they wish to do so. I'll describe the current program in more detail shortly.

Starting in 1980, the Council has been monitoring public attitudes toward a variety of topics related to risk and insurance, using face-to-face interviews conducted by the professional survey research firm of Yankelovich, Skelly and White. Each year they survey a representative sample of 1,500 households countrywide, and report the findings to us. One of the questions we have asked each year is what actions people have taken to lower their auto insurance costs within the past three years. The results indicate a steady increase in the percentages of households that have shopped arourd for lower prices.

In 1980, 25% of respondents said they looked for an insurance company that charges lower prices. The percentage of households that actively shopped rose to 29% in 1981, to 30% in 1982 and to 31% in 1983. There was a corresponding increase in the percentages of respondents who reported that they changed insurance companies in order to get a lower price. The figure was 15% in 1980, 19% in 1981 and 1982, and 20% in 1983.

The percentages who reported taking other actions to reduce their auto insurance costs, such as increasing the amount of deductibles or dropping part of their coverages, remained steady over the four years at 12% to 15% of respondents. In other words, shopping for a more competitive price is the predominant way that consumers try to reduce their insurance costs, and their tendency to shop has been increasing in recent years.

In 1982, we also asked a series of questions concerning the public's level of information about auto insurance and the various sources they use to acquire their knowledge about the subject.

The first question was: "How well informed are you about what auto insurance is and how to buy it?"

HOW WELL INFORMED ABOUT
AUTO INSURANCE?

Q. How well informed are you about what auto insurance is and how to buy it? Are you:

	1982	1980
Very well informed	24%	15%
Fairly well informed	50	48
Not too well informed	20	27
Not at all informed	7	10
Number	1,127	1,374

Twenty-four percent said they considered themselves "very well informed," up from 15% in 1980, the last previous time we asked that question. Another 50% said they were fairly well informed, compared to 48% in 1980. Therefore, as of 1982, 74% of the vehicle-owning households were at least fairly well informed, compared with 63% in 1980. Twenty percent said they were "not too well informed," and seven percent said they were "not at all informed."

We found that being well informed about insurance was highly correlated with readership of their auto insurance policies. Some 68% of vehicle-owning respondents said they had read part or all of their policy, most of them within the past three years. Among those who said they had read all of their policy, 90% reported that they considered themselves "very well" or "fairly well" informed about auto insurance and how to buy it. Among those who had read part of their policy, 80% were at least fairly well informed. By contrast, among those who said they had never read their policy, 47% considered themselves "very well" or "fairly well" informed.

ACTIONS TAKEN TO REDUCE AUTO INSURANCE COSTS

Q. This next card lists actions which people can take to lower their automobile insurance costs. Focusing on the past three years, please tell me if you have taken any of these actions to reduce your insurance costs.

	All Vehicle Owners			
	1983	1982	1981	1980
None	42%	41%	39%	47%
Looked for an insurance company that charges lower prices	31	30	29	25
Changed insurance to a company that charges lower prices	20	19	19	15
Increased the amount of deductible	13	15	14	14
Arranged for more frequent and smaller payments	13	13	13	12
Dropped part of your insurance coverage	12	12	12	11
Reduced the maximum amount payable per person or per accident under the policy	6	6	6	6
Traded in a car for one costing less to insure	5	4	5	5
Sold a car or truck and not replaced it	5	5	6	5
Removed a teenage driver from a policy	4	5	5	4
Dropped all of your insurance coverage	2	4	3	3
Other specified action	1	1	1	1
No answer	1	1	1	1
Number	1,380	1,127	1,377	1,374

Note. Percentages add to more than 100% because of multiple responses.

Source: Public Attitude Monitor 1983, All-Industry Research Advisory Council.

Finally, we asked a series of questions about specific sources that might be used by consumers to learn about auto insurance, and asked respondents to indicate how important each of them had been in helping them to learn about the subject.

SOURCES OF INFORMATION ABOUT AUTO INSURANCE

Q. How important has each of these been in helping you to learn about auto insurance?

Information Sources	Very Important	Somewhat Important	Not Too Important	Not at All Important
Reading your insurance policy	37%	37%	16%	10%
People you know - relatives, friends, neighbors, co-workers	34	41	17	8
Insurance agents	27	46	16	10
Published rate comparisons	15	35	33	17
Insurance company advertising	8	29	39	25
Government booklets	7	31	32	30
Stories in newspaper, TV, or radio program	6	31	32	30
Insurance company mail	6	28	39	27
Magazine articles	5	31	38	25

Source: Public Attitude Monitor 1982, All-Industry Research Advisory Council.

The three most highly rated sources of information were "reading your insurance policy," "people you know," and "insurance agents." All three were considered important sources by more than 70% of all vehicle-owning households. About half of the respondents listed "published rate comparisons" and "insurance company advertising" as important information sources. Four additional sources were rated as important by just over one-third of the respondents, including "government booklets," "stories in newspaper, TV or radio program," "insurance company mail" and "magazine articles."

The Council is currently undertaking a more comprehensive research program to explore how consumers obtain auto insurance and the kinds of information sources they use to help them decide what to buy. The decision to embark on this effort was made in March 1983 at a special planning session to determine the Council's research priorities for 1983-84. Several weeks later, the Federal Trade Commission was asked by Congress to study those same issues and to make a report by January 1985. We contacted the FTC staff, told them of our research plans, and offered to make available our findings as they become available. We have already turned over the results of one project, which involved surveying all 50 states to identify the kinds of auto insurance information sources available to consumers. This resulted in the collection of four large cardboard boxes of material, from such sources as state insurance departments, other state and federal offices, Better Business Bureaus, insurance information offices, trade associations, agents groups and individual insurance companies. Mark Plummer of the FTC staff reviewed all of this raw material and obtained copies of everything not already duplicated by his own staff's efforts. We are presently in the process of categorizing this mass of material so we can describe it in a written report at the end of the project.

Earlier this week, I looked through boxes to see what kinds of information programs are available to consumers in your home states. Here is a sample of what I found:

New Jersey - Shopper's guides geared specifically to New Jersey are published by the state insurance department, by the New Jersey State Insurance Information Service, and by the Insurance Information Institute. All three also respond to inquiries by phone and letter. In addition, there is an Insurance News Service that provides the media with news about insurance. The New Jersey Star Ledger also has published its own "Consumer Guide to Car Insurance," in addition to publishing an almost daily stream of news items.

New York - The New York Insurance Department publishes several auto insurance reports, including a Shopper's Guide, an annual report on complaints against insurance companies, and special pamphlets on no-fault and on "Insurance and Women." Auto insurance educational material also is available from the Insurance Information Institute and the American Insurance Association, both headquartered in New York City, and from such sources as the Direct Mail Marketing Association and the Joint Council on Economic Education.

California - The California Insurance Department has a Buyer's Guide on auto insurance. In addition, the Western Insurance Information Service has several consumer publications, and also has a very active Speaker's Bureau and film library. Information also is available from agents groups and from commercial publishers. For example, I ran across something titled "Consumer's Checkbooks/California," which is sold on the newsstands and in bookstores The same publisher puts out editions tailored to the insurance situations in other states as well.

Illinois - The Illinois Insurance Department also publishes a Buyer's Guide. There is also an Illinois Insurance Information Service to provide media with information of interest to consumers. Illinois is the home state of three major insurance trade associations (Alliance of American Insurers, National Association of Independent Insurers, and National Association of Mutual Insurance Companies), each of whom is a source of consumer-oriented printed materials and special information programs.

Ohio - The Ohio Insurance Department publishes two pamphlets on how to shop for auto insurance and on Ohio's financial responsibility requirements. The Ohio Insurance Institute has available numerous pamphlets and films, and operates a statewide speaker's bureau. The Insurance Board of Cleveland provides pamphlets and other information in the Cleveland area. Information about personal insurance also is available from the Ohio Vocational Home Economics

Adult Education program.

Michigan - The Michigan Insurance Department distributes a "Consumer's Guide to No-Fault Insurance," a special publication regarding the impact of their Essential Insurance Act on women, and a series of Insurance Consumer Alert bulletins covering a wide variety of consumer advice on insurance. Michigan State University also has a publication titled "Insurance For Your Family."

Texas - Two active insurance information services operate in Texas, one funded by domestic insurance companies and the other operating as a branch office of the Insurance Information Institute. Both provide printed materials and supply news media with timely information about insurance developments affecting Texas consumers. In addition, some of the domestic insurers have very active information programs, including audio-visuals.

Oklahoma - The Oklahoma Insurance Department publishes a Buyer's Guide. The state also is served by a state insurance information service.

These are examples of the special information sources available, in addition to the advice provided on an individual basis by insurance agents and companies and the countrywide programs conducted by the national trade associations and national insurance information services.

The All-Industry Research Advisory Council also is conducting two consumer surveys to learn more about how people shop for auto insurance. We have included several questions relevant to this topic in our annual countrywide survey conducted by Yankelovich, Skelly and White, and will have results available this summer for the FTC and for our own ongoing series of reports.

In addition, we are conducting independent surveys in six large states - New York, California, Illinois, Texas, Georgia and Wisconsin. These states represent a range of insurance environments which might generate different levels of consumer demand for information. Since the countrywide survey is

not large enough to permit reporting of results for individual states, we decided to supplement it with this separate study in six jurisdictions. Results from this survey also will be available this summer.

What have we learned from our research to date? I would summarize the findings in this way:

1. Consumers are showing an increasing tendency to shop around and to switch companies in order to get lower prices on auto insurance.

2. Nearly three-quarters of consumers say they feel at least fairly well-informed about auto insurance. In 1980, only 63% of respondents gave that answer.

3. Vehicle owners have a wide variety of information sources available to them. The three sources which they consider most valuable to them are their own insurance policies, word of mouth information from people they know, and their insurance agents. Pamphlets and other printed material receive a substantially lower rating, whether it is produced by the insurance industry, by the government, or by the news media.

What consumers seem to be telling us is that they want information and advice specific to their own insurance needs, rather than general information aimed at statewide or countrywide audiences.

We will have additional findings to report this summer when the results of our 1984 surveys are in hand.

Mr. EDWARDS [presiding]. Thank you, Mr. Segraves.

Our next member of the panel to testify is Ms. Nancy Golonka, vice president of consumer affairs, Insurance Information Institute, Atlanta, GA.

Ms. GOLONKA. Thank you. I appreciate the opportunity to present this testimony today.

I work for the Insurance Information Institute, which has for the past 25 years been a voluntary, nonprofit, public information and education organization for the property/casualty insurance industry. We are supported by 311 member insurance companies.

Our sole function is to monitor consumer concerns and to make information about property and casualty insurance available to consumers. We do this indirectly through the mass media, both broadcast and print, and directly through the publication of leaflets, newsletters, books, and audiovisual materials. In addition, we have an extensive program of publishing and distributing educational materials about insurance to the secondary schools.

I should emphasize that the Insurance Information Institute is not a lobbying organization, nor does it advance the industry's position with respect to legislative matters.

Over recent years, the property/casualty insurance industry's resources for providing information to consumers have expanded significantly.

Today I'd like to address two specific questions: Is information about insurance readily available, and is that information good information—that is, is it readily understandable? I believe I can answer both questions affirmatively.

At the Insurance Information Institute in recent years, we have prepared a series of easy-to-read brochures in both English and Spanish, written for a very grammar-school-level reader, the people that we find tend not to be as well informed generally about insurance.

In addition, we publish films, film strips, and slides and provide information for articles that appear in a variety of media, including popular national magazines.

Realizing that many people get their information not from printed materials but from the broadcast media, in recent years we have turned to broadcast mechanisms for getting our message across and for trying to communicate more effectively with consumers.

In the past 2 years, we have produced dozens of public service announcements, we have participated in open-line radio programs which allow consumers to call directly on the air to ask their questions, and these programs have aired in cities large and small all over the United States. We have also appeared frequently on local and network television talk shows.

During these media tours and also in our publications, consumers are invited to get answers to their insurance questions through the use of our national toll-free consumer information hotline. That number is 1-800-221-4954.

Since its beginning in February 1981, the hotline has served as an excellent source of information about consumers' concerns and has enabled the Insurance Information Institute to tailor its communications materials to respond to these concerns.

We also have held in a number of major cities in the United States dialog sessions between representatives of consumer organizations active in a local area and representatives of our member companies, with regulators present in these sessions. These sessions have helped us to discern the kinds of information consumers want and to respond to these wants.

We now use our print materials and the toll-free hotline as backup for our broadcast appearances and programs. That is, when I have an opportunity to appear on a television or radio show, I always make the point at the end of that program that if we have not been able to answer a viewer's or listener's insurance questions during that program, we will be happy to do so if they call our toll-free number.

The Insurance Information Institute's efforts are representative of those of several other insurance organizations and many individual insurance companies.

Let's turn now for just a moment to the second question regarding the quality of the consumer information produced by the insurance industry. Is it good information? Our response from the consuming public as well as consumer leaders and educators indicates that it is good information.

First, all our print materials are reviewed by consumer group leaders. We do not produce materials without input from its potential audiences—its prospective audiences.

Second, our hotline brings in calls every month from 49 to 50 States, and this means that we are in close touch with consumers all over the United States on a daily basis.

It is significant, I think, that we use the information gained from this input through this hotline for the benefit of developing our educational and informational materials.

Another indication that our information is usable is the cooperation of other organizations in helping us disseminate it. For example, upon introducing this series of basic information leaflets on home and auto insurance, we received letters from a diverse array of organizations asking for bulk quantities to distribute in their own communities, which we made available.

You also may be interested in this publication which we did cooperatively with a major national consumer organization—specifically, the National Association of Consumer Agency Administrators. This is the organization of local consumer protection officials, the government persons to whom consumers go with their questions or complaints. The entire purpose of this enormous effort was to equip these local officials to respond to the questions they get from consumers on the subject of insurance.

The insurance industry fully endorses the fact that information is vital to the effective functioning of consumers in a free enterprise economy. That is why the Insurance Information Institute and many other insurance organizations are carrying on activities such as the ones I have explained here to help consumers become better insurance buyers.

We will continue to do everything possible not only to make information available but to urge consumers to use that information when buying insurance. Thank you.

[The statement of Ms. Golonka follows:]

Statement of Nancy K. Golonka
Vice President-Consumer Affairs and Education

The Insurance Information Institute (III) is a voluntary, non-profit public information and educational organization for property/casualty insurance. This kind of insurance includes both automobile and homeowners insurance, as well as other specialty lines of insurance purchased by individuals. We are supported by 311 member insurance companies. Our sole function is to monitor consumer concerns and make information about property/casualty insurance available to consumers. We do this indirectly through the various news media, and directly through the publication of leaflets, newsletters, books and audio visual materials. In addition, we have an extensive program of publishing and distributing educational materials about insurance to the secondary schools.

I should emphasize that the Institute is not a lobbying organization, nor does it advance the industry's position with respect to legislative matters.

Over recent years, the property/casualty insurance industry's resources for providing information to consumers have expanded significantly.

Giving momentum to this trend was the organization in 1976 of the Insurance Industry Consumer Affairs Exchange. The purpose of this Exchange is to assist insurance company consumer affairs representatives in expanding their own programs of making information available to consumers and organizing mechanisms to be promptly responsive to consumer concerns. This group meets twice a year. It serves as a catalyst for individual insurance companies and the various insurance organizations as they plan and implement their consumer information programs.

Today, I'd like to address two specific questions. Is information about insurance readily available? And is that information readily understandable? I believe I can answer both questions affirmatively.

To provide sharper focus to its consumer activities, the Institute in September 1979 organized the Consumer Affairs Division, which I head. I have had extensive background in consumer affairs activities both with large international corporations and with educational institutions.

The Institute has developed a number of innovative programs designed to increase communication and the flow of information between insurance companies and insurance consumers. In doing so, we have made special efforts to develop the types of materials that are easy to read and easy to understand. These materials include leaflets in

English and Spanish, audio visual materials, a question and answer notebook for use by consumer protection officials, a book describing insurance coverages and giving practical recommendations as to how consumers can become better informed and a program for use at the secondary school level.

In addition, other Institute staff members and I regularly conduct media tours to discuss before both print and broadcast media how people can make better informed insurance decisions in the marketplace.

We have prepared a series of easy-to-read brochures in both English and Spanish which are made available widely to consumers throughout the United States. In addition, we publish motion picture films, filmstrips, slides and provide information for articles that appear in a variety of media, including national magazines.

Realizing that many people get their information from the broadcast rather than print media, in recent years we have turned to new mechanisms for communicating with consumers. In the past two years, we have produced dozens of public service announcements, participated in open line radio programs, allowing consumers to call directly to ask questions and appeared on local and network TV talk shows.

During these media tours, and also in III publications, consumers are invited to get answers to their insurance questions or to get additional information about insurance

through the use of our national, toll-free consumer hotline, 1-800-221-4954. This hotline has, since February 1981, served as an excellent source of information about consumers' concerns and has enabled the Institute to tailor its communications materials to respond to these concerns.

Also to keep closely in touch with consumer concerns, I maintain liaison with the National Association of Consumer Agency Administrators, Consumer Federation of America, National Consumers League, the American Home Economics Association, the American Council on Consumer Interests and many grass roots organizations.

In cooperation with some of these organizations, we have held dialogue sessions between their representatives and representatives of our member companies. These sessions help us discern the kinds of information consumers want and to respond to these wants.

We now use our print materials and the national toll-free hotline as back up for broadcast programs. That is, when I appear on a radio or TV program to talk about auto or homeowners insurance, I offer the toll-free hotline to viewers or listeners who have not gotten their questions answered during the live program.

The Institute's efforts are representative of those of several other insurance organizations and many individual insurance companies.

Let's turn now to the second question regarding the quality of the consumer information produced by the insurance industry. Is it good information?

Our response from the consuming public as well as consumer leaders and educators indicates that it is good information. First, all of our print materials are reviewed by consumer group leaders. We do not produce materials without input from its prospective audiences. Secondly, our hotline brings in calls every month from 49 and sometimes 50 states. This means that we are in close touch on a constant basis with consumers from all parts of the United States. We use the information gained from these callers as the basis for development of our educational and informational materials.

Another indication that our information is useable is the cooperation of other organizations in helping us disseminate it. For example, upon introducing our series of leaflets on the basics of home and auto insurance, we received letters from a diverse array of organizations asking for bulk quantities which we made available. Examples: The Department of Motor Vehicles throughout the state of California offers our "Auto Insurance Basics" brochure to consumers who come in to renew their license plates...The mayor of Santa Monica ordered 85,000 copies of "Tenants Insurance Basics" for the many apartment dwellers in his city whom he felt would benefit from this

information...Many police departments in New Jersey offer "Home Security Basics" to consumers in their precincts.

You also may be interested in this publication which we did cooperatively with the National Association of Consumer Agency Administrators. This is the organization of local consumer protection officials -- the government persons to whom consumers go with their questions or complaints. The entire purpose of this enormous effort was to equip these local officials to respond to the questions they get from consumers on the subject of insurance.

The insurance industry fully endorses the fact that information is vital to the effective functioning of consumers in a free enterprise economy. For the prudent person, insurance is a necessity if not a legal obligation. That is why the Insurance Information Institute and many other insurance organizations are carrying on activities to help consumers be better insurance buyers. We will continue to do everything possible not only to make information available but to urge consumers to use that information when making insurance decisions.

Mr. EDWARDS. Thank you very much.

The gentleman from Michigan.

Mr. SAWYER. Thank you, Mr. Chairman.

I understand—and I'd like to address this to Ann Haney—I understand there have been some five States, from what Mr. Nader said, that have adopted a so-called offer-acceptance approach, or, in other words, anybody that comes in the door gets a policy.

What has been the impact of that on the States, if you are aware—the States that have tried it on their rates?

Ms. HANEY. Well, the most logical first conclusion you can come to is that those rates will go up. It simply costs more to underwrite or to insure people who are not properly underwritten.

But more importantly, at least from the consumer information point of view, I think this is the absolute worst way to go, because right now consumers who have good information and who want good information can improve their lot as far as their rates. Say, for drivers, they can use auto passenger restraints with their children, they can be more careful and they can more or less buy the kind of coverage at a reasonable price that they deserve.

Under such an organization where you take all comers, so to speak, you then begin to subsidize the very poor risks and people who want to remain poor risks, who aren't interested in improving the rate that they are at, and eventually there is no motivation for anyone to become well informed to purchase insurance wisely.

Mr. SAWYER. I have seen some information that indicates that, in one of those States anyway, that the rates have quadrupled since they went to that offer and acceptance system. Are you aware of that?

Ms. HANEY. I would imagine that could be true, although I don't have any specific knowledge.

Mr. SAWYER. I understand that in New Jersey they have a joint underwriting association whereby the risk is distributed on a rotating basis and losses are therefore shared, and New Jersey also has, as I understand it, very high rates. Some seven national carriers have pulled out of the State altogether.

Can you explain how a reduction in available competition ultimately benefits the consumer?

Ms. HANEY. Obviously, it does not, and that's a very important reason why we should have these hearings—to take a look at the operation and information involved in insurance—and it's one of the reasons why State regulation should be maintained, so you have that close surveillance at a very local level, where very little gets by what's happening in the States, and businesses care, people care, about the health of the industry and want to maintain that business base for taxation purposes and ultimately for the benefit of the consumers.

So it's very important that our regulatory structure and our information is where it's at and continues in the direction that it's going today, to keep healthy companies and competition available.

Mr. SAWYER. Ms. Golonka, I've heard the charge and heard it again here today that State regulators are pretty much tied to the industry and speak for the industry rather than consumers, and I understand you studied that area, and what are your observations?

Ms. GOLONKA. Well, I did have an experience in that area. We conducted a series of 10 dialog sessions, which I mentioned briefly in my statement, in 10 major metropolitan areas in the United States. In each of these meetings, there was a representative of the regulator, in some cases the regulator himself or herself.

Invariably in these 10 sessions, which brought together local consumer representatives of the most active consumer groups in that given locale and local insurance industry people, the consumer representatives regarded the regulator as their advocate, and invariably this was the case.

So I thought that that was a very interesting statement when it came up a few days ago in these hearings that the regulator is never on the side, or is always very anticonsumer. This has not been our finding at all.

Mr. SAWYER. Thank you.

I yield back, Mr. Chairman.

Mr. EDWARDS. We appreciate your testimony very much.

Let's see. Ms. Golonka, in that book that you have there and in those pamphlets you pass out to consumers, do you have hard prices, comparisons of one company against another, so that a consumer can find out where he can get the lowest price?

Ms. GOLONKA. No; we do not.

Mr. EDWARDS. Why don't you?

Ms. GOLONKA. Because this information is the type of information which becomes obsolete almost before one can publish a pamphlet, for one thing. Second——

Mr. EDWARDS. Also, you would probably get fired, too; isn't that correct?

Ms. GOLONKA. I simply would not know about that.

The reason that it is not in our brochures is because we do not have the facility in our organization of gathering this kind of information.

We also have found that it is not always in the best interest of the consumer to be misled by some hypothetical information which is stated up front in such a brochure, and it is stated in many, many brochures produced by State insurance departments, I might add. That information is available in many States.

Mr. EDWARDS. Thank you. Do you have in those pamphlets, or in that book, complaint ratios as to volume of business and which companies have the most complaints in relation to the amount of business they do.

Ms. GOLONKA. No, sir. I do not feel that complaint ratios as to volume of business is a consumer issue. I don't think that consumers are concerned for such things.

What consumers who contact us on our hotline and who ask questions over the air, and so on, want to know from us is, "What about my insurance?" They ask personal questions about their own situations, and they are not interested in complaint ratios.

Mr. EDWARDS. Well, there are a lot of people who disagree with you on that, isn't that correct?

Ms. GOLONKA. I really wouldn't know.

Mr. EDWARDS. You mean you don't know the opinion of the National Association of Insurance Commissioners' 1980 Task Force on Consumer Information? That was one of their recommendations.

Ms. GOLONKA. Well, I simply have not had it to be my own experience that consumers themselves are interested in complaint ratios. That has not been my experience.

Mr. EDWARDS. Now, you told us about your toll-free hotline, and you said it was an excellent source of information about consumer concerns.

The subcommittee staff called your hotline yesterday and couldn't get any specific information about prices or about complaint ratios. All the staff could get when they phoned your hotline was a list of the largest companies in the area and advice to shop around. Do you think that is really first-class consumer information—to shop around?

Ms. GOLONKA. I certainly think that comparison shopping, when it comes to insurance, is as important as comparison shopping for any other major product or service that one is going to purchase, and I think that consumers must assume some responsibility for gathering price information, for making phone calls, and for comparing costs and services.

I also would say that, as Don mentioned in his statement, shopping for price information is not the only thing that insurance consumers are interested in. They are interested in what kind of service they are going to get when they have a claim; they are interested in the reputation of that local agent from whom they purchased a policy; they are interested in a number of other factors which are not necessarily limited to price.

Mr. EDWARDS. Do you come to these conclusions and prepare these papers and giveaways in consultation with consumer groups and consumer representatives like Mr. Nader's organization?

Ms. GOLONKA. I have not consulted with Mr. Nader's organization, no.

Mr. EDWARDS. Do you consult with the National Insurance Consumer Organization?

Ms. GOLONKA. When we produced these brochures, there was no National Insurance Consumer Organization; it was not in existence.

Mr. EDWARDS. How long have those brochures been——

Ms. GOLONKA. This was 1979.

Mr. EDWARDS. They haven't been updated?

Ms. GOLONKA. These are informational brochures which are not that quickly out of sync with the times.

Mr. EDWARDS. Thank you.

Mr. Segraves, do you publish any information for consumers?

Mr. SEGRAVES. Yes, sir, we do. We publish all of our reports, make them available to the world, one copy free.

Mr. EDWARDS. And in your reports, do you have hard prices and comparisons of prices between various companies?

Mr. SEGRAVES. In one of our reports on the cost of auto insurance, we had the prices that were the average premiums that people paid in various rate categories as of the time we did the survey, yes.

Mr. EDWARDS. The names of the companies?

Mr. SEGRAVES. We had the names of the companies who participated, yes.

Mr. EDWARDS. And were they broken down individually?

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Mr. SEGRAVES. You cannot—it would take a volume that would load down this table to list all of the prices listed by every company in the United States. There's no way you could do that in a practical sense.

On the other hand——

Mr. EDWARDS. Did you ever try?

Mr. SEGRAVES. On the other hand, any consumer can call agents and readily get price information specific to their own situation, which is the only thing that matters to them. There's absolutely no problem in getting prices.

Mr. EDWARDS. In these reports you issue, do you have complaint ratios as to volume of business—which companies have the most complaints vis-a-vis the volume of business they do?

Mr. SEGRAVES. That was not relevant to the study we did on the price of insurance. However, you can readily get that information from a number of State insurance departments. They put out news releases on complaint ratios every year. I've got some right here.

Mr. EDWARDS. Ms. Haney, let's see; your position is director of consumer affairs for the American Family Mutual Insurance Co., and do you publish information for consumers?

Ms. HANEY. Do we publish information for consumers?

Mr. EDWARDS. Yes.

Ms. HANEY. Yes, we do.

Mr. EDWARDS. All right. And do you have comparisons of prices?

Ms. HANEY. Yes, we do. Now, what I mentioned——

Mr. EDWARDS. By company?

Ms. HANEY. By——

Mr. EDWARDS. In other words, if some person wants to buy an insurance policy and really would like to know from a consumer organization such as your organization where to get the cheapest policy, is that the kind of information you publish?

Ms. HANEY. My position is director of consumer affairs within American Family Insurance. I don't publish information on the rates of other insurers. Our agents would probably carry that; but we have gone to getting those prices out there right now, when we are asked, because we feel we are competitive and because that's what people want to know; that's the way you have to operate in a market.

Mr. EDWARDS. So you're saying the agents themselves do have this information—is that correct?—so if a working man or working woman comes in and sits down, the agents will provide it. Don't the agents have a conflict of interest? Wouldn't they steer the business to a particular company, the one that they are working for?

Ms. HANEY. Our agents are agents for only our company. So if—for the 5 percent who actually do come in, and about 95, I guess, now are calling and say, "Just mail it to me."

Mr. EDWARDS. In the real estate business, the agent has to tell the seller how much commission is being paid. Do your agents tell the purchaser how much commission they are getting?

Ms. HANEY. They sure do.

Mr. EDWARDS. They do?

Ms. HANEY. And they get asked that. Sometimes people don't ask.

Mr. EDWARDS. People could ask about it. Do the agents tell them? Is it written down, and is that a part of the contract?

Ms. HANEY. No, I don't think it is part of the contract. I should say, I know that it's not. More or less, the agents can use that as a tool.

One of the things that we try to do, as I mentioned, is give consumers the information that they want, and if there is a sense there that maybe the consumer is wondering but not willing to ask, the agent will bring that up. It's a good relationship—consumer relationship tool, and everyone knows that we get paid for the work that we do.

Mr. EDWARDS. The 1979 GAO report suggested that it's very frequent in your industry for people to move from being an insurance regulator into the industry, like you did. Is this generally the practice?

Ms. HANEY. I don't know if it's generally the practice. I don't know at what ratio people do that. I was only commissioner for a short while. I was really a consumer regulator for most of the time I was in State government.

Now, in Wisconsin—the frontier of consumerism, as we were called—we do have a law which might be a helpful law in other States, and that is that if you move from a State regulator's post into one of the industries you have been regulating, you cannot interact with government—provide any statements, lobby; there are a number of things you can't do—by State law, you are prohibited from doing for a year.

So in my situation where there were 27 different groups, I was prohibited from doing a lot of things for an entire year, and I spent then a lot of time thinking and working with the company on what is it the people really want to know and how best can we get the information out for everyone's benefit.

Mr. EDWARDS. Thank you.

Mr. Segraves, in your statement you state that AIRAC has been monitoring public attitudes on insurance since 1980, and you cite yearly studies performed by Yankelovich, Skelly & White and also an ongoing study and also some specialized studies. Do you have any objection to turning these studies over to the subcommittee?

Mr. SEGRAVES. Sir, they are available to anyone who asks for them, including the subcommittee. I'd be happy to submit them for the record.

Mr. EDWARDS. Thank you. We will ask for them.

[Material on file with the subcommittee or available from AIRAC, 1200 Harger Road, Suite 222, Oak Brook, IL 60521, 312-920-1177.]

Mr. EDWARDS. Are there any questions?

Thank you very much. You have been very helpful.

This concludes the hearing for today.

[Whereupon, at 11:45 a.m., the subcommittee was adjourned.]

COMPETITION IN THE INSURANCE INDUSTRY

THURSDAY, JUNE 28, 1984

House of Representatives,
Subcommittee on Monopolies and Commercial Law,
Committee on the Judiciary,
Washington, DC.

The subcommittee met in room 2141 of the Rayburn House Office Building, Hon. Peter W. Rodino, Jr. (chairman) presiding.

Present: Representatives Rodino, Feighan, and Hyde.

Staff present: Warren S. Grimes and Jonathan Cuneo, counsels; Marilyn Falksen, research assistant; and Thomas M. Boyd, associate counsel.

Chairman Rodino. The Subcommittee on Monopolies and Commercial Law will come to order. I'll suspend until the gentleman from Ohio makes a unanimous consent request.

Mr. Feighan. Mr. Chairman, I ask unaminous consent that the committee permit the meeting this morning to be covered in whole or in part by television broadcast, radio broadcast, and/or still photography pursuant to rule 5 of the committee rules.

Chairman Rodino. So ordered.

In May, the Subcommittee on Monopolies and Commercial Law began hearings to address the question, "Is there adequate buyer information for the insurance marketplace to operate competitively?"

At these hearings, the subcommittee found widespread agreement that in fact buyer information is essential if the marketplace is to operate properly, providing the best products at the lowest prices. The subcommittee received conflicting views on whether an individual is able to obtain sufficient information to evaluate the alternatives in the insurance marketplace.

Although I expect that today we will again hear conflicting views, I hope that the testimony will aid us in obtaining a comprehensive understanding of disclosure issues.

Our first witness today—and we will have three panels—is Herbert S. Denenberg who was insurance commissioner of the State of Pennsylvania from 1971 to 1974. He was a pioneer in providing Shopper's Guides to consumers. I'm sure his testimony is going to be important and helpful to this subcommittee.

Following Commissioner Denenberg, we will hear from two representatives of the life insurance industry, Mr. Robert Hunstad, senior vice president and actuary with the Minnesota Life Insurance Co., who will be presenting testimony on behalf of the American Council of Life Insurance, and Mr. W. Wayne Perry, senior vice president, general counsel and corporate secretary, North

Carolina Mutual Life Insurance Co., speaking on behalf of the National Association of Life Companies and the Life Insurance Conference.

Finally, we will hear from the National Association of Insurance Commissioners represented by Mr. James P. Corcoran, superintendent of insurance for the State of New York. Mr. Corcoran will be accompanied by Mr. Bruce Foudree, insurance commissioner for the State of Iowa, and Mr. Lyndon Olson, chairman of the Texas State Board of Insurance.

Commissioner Denenberg, we will hear from you now. As you know, we are acting under strictures of time, and we would hope that you will limit your oral presentation. Your written statement will be included in the record in its entirety.

TESTIMONY OF HERBERT DENENBERG, FORMER INSURANCE COMMISSIONER OF THE STATE OF PENNSYLVANIA (1971-74)

Mr. DENENBERG. OK, thank you very much.

My name is Herbert S. Denenberg. I am the former insurance commissioner of Pennsylvania (1971-74), and as indicated in a biographical note on the cover page of my full statement, I have had other experience with the insurance industry.

State insurance regulation may be lousy, but Federal regulation would be worse. To borrow a phrase from Winston Churchill, State regulation of insurance is the worst method of regulation, except all the others that might be tried. Federal regulation would just give birth to a larger and more cumbersome, less flexible bureaucracy far removed from the issues.

But that doesn't mean that the Federal Government should not set standards for regulation and make applicable the antitrust laws and such other laws as might be necessary to assure fairness and competition in the insurance marketplace.

There's no reason why national policy should not set standards for State regulation. There's no reason why national policy should not outlaw attempts by State law to strangle group auto insurance, credit card insurance sales, and other efficient marketing methods.

Congressional committees, even when not legislating, have had dramatic impact on State regulation, by challenging its assumptions, calling it to accountability, and dramatizing its weaknesses and shortcomings.

Only recently, congressional committees put that junk, gimmick, Mickey Mouse coverage called cancer insurance into proper perspective, and helped bring about reforms in the rip-off plagued Medigap insurance market. In fact, most of the major insurance reforms over the years at the State level have been initiated or encouraged by congressional investigations such as this one.

Legislators like the late Senator Philip A. Hart of Michigan of the Senate Antitrust and Monopoly Subcommittee may have done more for State insurance regulation than all the State legislatures of his time put together.

This committee should recognize that State regulation and State legislation and the insurance industry, alone or together, are incapable of generating the kinds of changes in the marketplace that the consumer urgently needs.

Over the years, the insurance industry has largely called the shots on State regulation and legislation involving insurance and has certainly been able to exercise veto power over any basic changes.

The public requires more than regulation by a watered-down consensus of the insurance industry, bearing the rubber stamp of the insurance commissioner.

The fundamental problem was once again put into perspective by a recent incident in Pennsylvania. The Insurance Federation of Pennsylvania, the chief organization and lobbyist of the State's insurance industry, was seeking the repeal of the no-fault law.

During the ensuing debate, it was disclosed that the president pro tem of the Senate, Henry Hager, also a practicing lawyer, had been representing the Federation in a court proceeding, and had recently been offered a six-figure job by the federation. And it was reported that the Senator's law firm also represented other insurance companies.

This did not set off any great public stir, only a few news stories. This kind of activity was simply viewed as business as usual in the legislature.

Some, including the Senator, saw no conflict of interest or corruption in that kind of relationship, but for my money, it shows once again one of the many reasons why State government won't bring about the changes the consumer needs.

Certainly, there is abundant evidence that the insurance industry will not generate those changes on its own. My own experience as insurance commissioner found that even the most painless reforms on behalf of the consumer—for example, making insurance policies readable or giving the consumer information on the prices charged by different insurers in the form of shopper's guides—will be opposed by the industry.

The industry will act only if bludgeoned, badgered, and embarrassed by Government or public opinion.

Let me illustrate a few points for you. Take the readability issue, one that is useful because it is easily understood and represents the kind of change that should be implemented with ease and dispatch.

Eleven years ago, before the Senate Antitrust and Monopoly Subcommittee, I announced a campaign to disapprove insurance policies that were unreadable.

At the Pennsylvania Insurance Department, we had demonstrated that on a scale of readability, running from 100—most readable—on down, Einstein's work on relativity came in at about 17, the then standard auto policy at 10, and some homeowners policies came in with negative scores.

The insurance industry vigorously objected to my proposal for readable policies—they said it would destroy reliance on legal precedent and was an unproved and unworkable idea. Only because they were forced to do so did they start simplifying policies.

Soon the industry, despite its initial objections, saw the idea catching on and started utilizing so-called readable policies for advertising and public relations purposes.

So you would have assumed that in the last decade the industry would have been able to move toward readable policies.

Well, I checked the industry out by going to my own auto policy. It's called an easy reading policy and contains this provision which every Pennsylvania policyholder may have to face:

If an X is entered in one or both boxes below, coordination of benefits applies to the named insured and any relative.

Medical expenses is excess to a qualified primary source, including Medicare benefits, designated by the named insured. If the primary source is not available, a $250 deductible applies to the named insured.

Work loss is excess to a qualified primary source designated by the named insured. If the primary source is not available, a 2-week waiting period will apply to the named insured.

Now, that's the easy reading policy. Here's a provision from a commonly used life insurance policy that's not labelled easy reading so look out:

If default of premium payments occurs when the cash surrender value indicated in the Table of Guaranteed Values together with the cash value of paid-up endowment dividend additions and dividend accumulations less any indebtedness will purchase an amount of paid-up endowment insurance which exceeds the amount of extended term insurance which would be purchased under the paid-up extended term insurance provision described in section (1) above, then the Policy will be continued under the paid-up extended term insurance in lieu of the paid-up endowment insurance provision.

With that kind of language, the insurance company can claim any meaning they want. And the policyholder is left in the dark, unless he has a team of three Philadelphia lawyers, a linguist, and actuary and an insurance underwriter.

That is why I have to tell this committee what I told the Senate Antitrust and Monopoly Subcommittee 11 years ago: That despite pressures from all sides, the insurance industry seems to want to compete by confusion.

Take another issue. There's been a lot of talk about giving the consumer information on premiums, costs, and rates of return on policies.

One way to start doing that would be for State insurance departments to produce shopper's guides for each key line of insurance, make them widely available, and give them to every policyholder or customer who seeks a quotation on a policy.

We started in that direction in Pennsylvania in 1971, by publishing a series of guides with premium comparisons, and when necessary, cost indexes and pay-out ratios.

But even giving the public premium information was opposed by the Pennsylvania insurance industry. Despite the appeal of the idea, and remember it informs consumers, puts pressure on companies to lower rates and compete, and sharpens competition, the idea still has not caught on with the insurance industry or the insurance regulator.

Most insurance departments have still not put out guides with premium comparisons, and not a single insurance department has done a decent job of giving consumers needed price information. Their life insurance guides are almost nonexistent.

On May 10, 1984, you had an insurance industry witness before this committee tell you about the four large cardboard boxes of material they had collected on auto insurance information sources.

Well, I'd like to tell the committee what they ought to do with those four boxes. To give you an idea, examine what the witness told you about the material available in your home States.

I checked with the insurance departments of the eight home States he named and here's what I found about the auto insurance guides he talked about.

Not one of the eight States had available up-to-date auto insurance premium comparison information. California said they don't do such things. Ohio said they refer consumers to an independent insurance agent for such information.

New Jersey said premium comparisons are too big a job to prepare. New York had a guide with premium comparisions, but it has not been updated since 1981.

A few States—Oklahoma, Illinois, and Michigan—had auto insurance guides, but they did not contain premium comparisons and were little more than consumer advice columns.

Texas said they referred those seeking information about auto insurance to the Insurance Information Institute, an industry trade association, which, needless to say, does not publish premium comparisons either.

Some of the guides not only lacked premium comparisons, but also had nothing to say about how to shop for insurance or even how to select financially sound insurers.

Premium comparisions are difficult to come by for the typical consumer. But there is no excuse for not making these comparisons widely available and assuring their availability at point of sale, as part of a disclosure requirement.

Here's one suggestion for assuring some of that premium information. Now, under State law, rating bureaus set rates for their members, a form of legalized price-fixing. One such organization, Insurance Services Office, for example, periodically compiles auto and homeowners insurance rates as part of its activities and circulates them to member insurers. This is almost a ready-made shopper's guide.

Why not require these rating bureaus to disclose these comparisons to the public, and even make them automatically available to each customer at point of sale?

If the McCarran Act can legalize price-fixing, it should also require that price-fixers share the fruits of their labor with consumers.

There is good reason for the Federal law to set standards for insurance regulation that would require disclosure for all key lines of insurance.

That disclosure should include comparative premiums, agent's commissions, rates of return in the case of life insurance with a savings feature, and pay-out ratios, benefits per policyholder, and information on hypothetical claims, in the case of health insurance.

It's nothing short of a national scandal and a national miracle that the life insurance industry can sell billions of dollars in cash-value life insurance without giving policyholders information about rate of return—the interest rate earned on the savings portion of the policy.

This is the equivalent of a bank taking savings deposits without disclosing the rate of interest to be paid.

You have to wonder why an industry that is selling what is essentially an investment contract, a savings contract, not only won't disclose its rate of return, but even wants to deny the investment nature of its contract. When the contract is sold, the savings portion of the policy is emphasized. But when it comes time to ask for the rate of return, the industry takes the stance that somehow the contract is inseparable, and it doesn't make sense to talk about rate of return.

The reason the industry is so intent on covering up the facts is that its sales depend on covering up the facts and confusing the consumer. Who would save if he knew the rate of return was 2 percent? For decades the industry has managed to pull the wool over the eyes of the consumer, the regulator, and the legislator.

That's why disclosure is urgently needed, and that disclosure should include the agents' commission.

If an agent sells a term insurance contract, his first-year commission may be 35 percent. If he sells whole life, the commission may be 50 percent. That's one reason some agents may not recommend what is best for the consumer.

It's clear that the commission may be the key determinant of what the policyholder gets.

A field survey of 92 Pennsylvania agents found that most of them did not tell the customer about how to reduce premiums by taking no-fault discounts, even when pressed for cheaper prices. Only 30 percent of the agents volunteered this information.

The Pennsylvania Insurance Department, after that survey, concluded:

> There is no economic incentive for agents to make cost disclosure since lower premiums for the consumer mean lower commissions for the agent.

This was viewed by the department as:

> A widespread pattern of incompetence, professional negligence, general consumer abuse, and even outright fraud that draw us beyond the conclusion that this is merely the work of a few bad apples.

Disclosure would serve to reveal agent bias and help prevent that bias from denying the consumer the best price in the market. It would also discourage uneconomical and inefficient marketing methods.

In the securities industry, high commission, high load, low return products are harder to sell because of disclosure. But in the life insurance business, high commission, high load, low return products are a bonanza. The consumer is taken because there is confusion and cover-up, which make it impossible for him to get the facts.

This is not likely to be changed at the State level, because the political process has a built-in level of conflict of interest if not corruption due to the inordinate influence of the insurance industry on State government.

So any changes to amend the McCarran Act to achieve a greater measure of consumer protection are long overdue.

But more important than any substantive changes would be congressionally mandated changes that give the consumer a greater voice in the regulatory process. Then the consumer will be able to speak for himself.

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Two models that come to mind are the Citizens' Utility Board in Wisconsin and the Office of Consumer Advocate in Pennsylvania. These same concepts can be applied to insurance, and would give the consumer some measure of countervailing power, which is now almost totally lacking.

Unless Congress acts, we are likely to continue to have competition based on confusion and cover-up, and regulation based on conflict of interest and corruption. The bizarre regulatory results and the lack of consumer protection in recent decades demonstrates the problem the consumer now faces and will continue to face unless Congress acts now.

Thank you very much.

[The statement of Mr. Denenberg follows:]

STATEMENT OF HERBERT S. DENENBERG *

BEFORE THE

SUBCOMMITTEE ON MONOPOLIES

OF THE

COMMITTEE ON THE JUDICIARY

U.S. HOUSE OF REPRESENTATIVES

June 28, 1984

* Insurance Commissioner of Pennsylvania, 1971-74; Professor of Insurance at the Wharton School of the University of Pennsylvania, 1962-1971; Visiting Professor of Law at Temple University, 1974; Former consultant on insurance for the U.S. Department of Labor, Small Business Administration; U.S. Department of Transportation; U.S. Civil Rights Commission; U.S. Department of Justice; Federal Trade Commission; Atomic Energy Commission, President's National Commission on Product Safety, the legislatures of Alaska, Nevada, and Puerto Rico, the Mayor of Washington, D.C., the Kennedy Center for the Performing Arts, and other government and private agencies; Special Counsel and Research Director of the President's National Advisory Panel on Insurance in Riot-Affected Areas and Associate Director of the Staff of the Wisconsin Law Revision Panel. And currently consumer reporter for WCAU-TV (CBS) in Philadelphia (1975-84). Denenberg holds a Ph.D. (University of Pennsylvania); an LL.M. (Harvard); a J.D. (Creighton); a B.S. (Johns Hopkins), a C.L.U. and a C.P.C.U. He has writen extensively on insurance and insurance regulation.

My name is Herbert S. Denenberg. I am the former Insurance Commissioner of Pennsylvania (1971-74), and as indicated in a biographical note on the cover page of this statement, I have had other experience with the insurance industry.

The insurance consumer and this Committee ought to be asking this kind of basic question:

Why has the insurance industry been able to sell billions of dollars worth of whole-life insurance every year, without ever getting around to giving the consumer information on the rate of return--that is. the interest earnings--of the savings portion of that investment and savings contract?

Why do the insurance buyers of major corporations routinely get and use information on the financial strength of the insurance companies they deal with, while the average consumer probably doesn't even know such information exists?

Why does the insurance policyholder still have to confront policies that are unreadable, confusing and misleading?

Why does the insurance law itself of every state set up barriers in the path of the most economical and efficient methods of marketing insurance?

Why do state insurance laws permit insurance companies that engage in legalized price-fixing to compile informative premium comparisons of auto and homeowners insurance premiums for their own use, and yet not make their compilations automatically available to the public?

That is just a small slice of the kinds of problems state insurance regulation and the insurance industry inflict on the public. Most of the issues raised by those questions have caught on with the media and hence have been brought before the public and Congressional Committees.

But the total insurance marketplace has never been adequately explored by Congressional Committees or state regulators. Attention has been directed to the most obvious pathology--with recent investigations of Medicare insurance supplements and cancer insurance--but equally serious problems have been overlooked and neglected. So I would urge this Committee not to stop with the important issues it has already raised, but to continue an across-the-board investigation that will produce a basis for making any needed changes in the McCarran Act and in the present method of insurance regulation.

Overview.

I know this Committee has already been swamped with a flood of statistics, citations of authority, and specific proposals to improve the insurance marketplace.

So let me start with some perspectives on what I've learned in over thirty years of studying and dealing with the insurance industry.

There is a marked tendency to give the system of beliefs of the insurance industry more credence than it's due. This comes about for several reasons.

The insurance industry has traditionally controlled the expertise thought to be necessary for anyone to understand or judge its conduct.

The insurance industry, through economic pressure and favors, largely controls the viewpoints of those who work within the industry, those who consult on the industry, and even those in universities who spend most of their time teaching and researching on insurance subjects. There are few experts or specialists operating outside the control of the insurance industry.

The industry gets less in-depth, high quality media coverage than almost any other major industry in the United States and therefore its viewpoints are not always critically examined.

The industry traditionally hides behind technical language and actuarial mathematics that rarely get explained to the public, and is often not cooperative in informing the media or the public.

Finally, the insurance industry, through its abundant political power, has also managed to largely control insurance regulation and legislation at the state level, and as Commissioner Michael Pertschuk of the FTC has already testified, it can mobilize incredible pressure at the federal level as well.

This kind of political power was recently demonstrated when the Pennsylvania Insurance Federation, the major association of insurers in that state, decided they wanted the no-fault law repealed. During that debate, the Philadelphia Inquirer revealed that the President of the Pennsylvania Senate, Henry H. Hager had not only represented the Insurance Federation in court as a lawyer but was also being considered for a six-figure job for the Federation. His law firm also represented other insurance companies.[1]

Senator Hager was quoted as saying: "My position has been to drag the insurance industry to where they are today. In my own mind, I have never compromised my position."[2]

He also said: "I don't consider who I represent as an attorney when I vote on issues." And he added that if he accepted the job, "it would be clearly stated that I would still vote as I saw fit."

But regardless of the effect of that kind of ecomomic favors, the Pennsylvania Insurance Federation got its repeal of the no-fault law.

What emerges from all this strategy of the insurance industry is a system of regulation and lawmaking that is directed by the insurance industry, with little countervailing consumer power. The end product is not regulation, but self-regulation. With few exceptions this is how the system works in practice:

Insurance commissioners in each state -- sometimes together with the National Association of Insurance Commissioners at the national level -- work out an insurance industry consensus on matters of legislation and regulation that is passed off as regulation in the public interest.

Unfortunately, the public interest often requires something more than a watered-down insurance industry consensus carrying the rubber stamp of the insurance commissioner.

But that traditional consensus rarely if ever accepts changes that might be needed by policyholders rather than insurers. But it quickly brings about changes that it perceives to be in its own interest.

For example when the insurance industry wanted the right to raise the interest rate on policy loans in life contracts, when the insurance industry wanted federally-backed riot insurance after the civil disorders of the 1960's, the insurance industry consensus was swift and effective at the state level.

But as I quickly found out when I became insurance commissioner, the most modest steps required for consumers (rather than the industry) were bitterly opposed and could only be implemented if no legislation were required.

For example, I started publishing a series of "Shopper's Guides" as soon as I became insurance commissioner. Many of these guides contained

premium comparisons, and even had lists of the highest and lowest-cost companies in the state. (Some of the guides and a commercially published compilation of them are included in the Appendix to this statement).

The insurance industry in Pennsylvania, through its chief organization, the Insurance Federation of Pennsylvania, quickly attacked the guides for a variety of reasons: they would put too much emphasis on price rather than service, they would be quickly outdated, and they would require professional help to use.

One trade publication, Insurance Field, reflected the views of the industry in Pennsylvania when it editorialized: "All in all the guide adds to the buyer's confusion and fortifies his doubts, rather than clarifying anything for him. What it will do to otherwise orderly competition is frightening."

Many other examples of the irrational and traditional response of the insurance industry to consumer needs could be cited. For example, the opposition of major segments of the industry to readable policies, the opposition to ending the widespread and illegal rating, underwriting, and marketing discrimination against women and other minorities, and the opposition to repealing prohibitions on group auto insurance and other forms of mass marketing.

Anyone who views the last thirty years of insurance regulation will conclude that sound ideas and needed reforms will stand little chance of success, if the assumptions and arguments of the insurance industry are taken at face value. The industry will almost automatically object to any reforms needed by the policyholder, however compelling the arguments in their favor.

The insurance industry consensus, often cloaked in alot of pseudo-expertise, has to be approached with caution when reforms required by the consumer are at issue. And as a corollary to that proposition, if there is going to be needed change, it will most likely have to come from the federal government. If Congress does not take steps to provide the buyer with needed help, there is not likely to be any action.

Insurance Consumer's Profile: 1971 and 1984

Consumers face an endless series of tricks and traps in the marketplace, but nowhere do they feel more confused, put upon, and helpless than when they set out to buy insurance and when they later try to make a claim on their policy.

Nowhere does the consumer have more questions and nowhere does he get fewer good answers than in the insurance marketplace.

For ten years as a consumer reporter, I have been swamped with questions and problems on almost all areas of the marketplace. But confusion, helplessness, and sometimes even hopelessness in making consumer decisions are most obvious when insurance is involved.

And this is not just the plight of the uninformed and uneducated consumer. It is also commonplace among even sophisticated and educated consumers, even among professionals and businessmen, who make their living by their wits, but are made witless by insurance.

And these observations are not directed just to life insurance, which has received major attention before this hearing, but also to other lines of insurance, such as homeowners, auto, health, and personal liability.

About ten years ago, when I was Insurance Commissioner of Pennsylvania, I painted this picture of the all too typical insurance buyer:

He approaches an insurance agent, about half of whom are incompetent, to buy a policy, which neither he nor his agent is likely to understand.

He is quoted a premium, that is likely to be excessive, because he has not shopped around intelligently and because the agent may be more interested in a high commission for himself than a low-cost premium for his client.

He then gets placed in an insurance company, which chances are a knowledgeable insurance expert would have avoided. The experts stick to the top 10 or 20 percent of the market to obtain the security and certainty which are part of the very definition of insurance. But the typical buyer may end up in that 80% of the market, which the expert avoids.

That ill-fated insurance buyer then recieves a bundle of papers called an insurance policy, which contains a lot of promises. But those promises stand a good chance of being broken -- when the time for pay-off comes -- because of the confusion that surrounds the entire transaction.

And if the insurance buyer has troubles later, he can go to his state insurance commissioner, who may currently be negotiating his next job with the insurance industry, or at least contemplating his future employment with the industry, from whence, perhaps he came.

Now, every buyer does not face all of those sad outcomes, but they are sufficiently likely so they affect a substantial number if not a majority of insurance transations.

That was the picture I painted ten years ago. Unfortunately that picture is still the rule, and not the exception. But there is some good news. There has been some progress and some areas of improvement. The bad news is that there hasn't been much improvement, and most of that has

come about only because some insurance commissioner, other governmental official, an industry critic, or an irresistable tide of public opinion and public pressure badgered, bludgeoned, and embarrassed the insurance industry to implement some change.

Unreadable Policies: A Continuing Problem

Take the classic example of the so-called "readable policies." I can speak from an insider's point of view as I was the first insurance commissioner to start disapproving policies because they were gobbledygook.

We demonstrated on a widely recognized scale of readability that the then standard Family Auto Policy, and some homeowners policies, were less readable than Einstein's book, "The Meaning of Relativity."(3) We said this was all part of an insurance industry policy of competition by confusion.

We said the buyer ought to be able to read and understand his insurance policy. And, we said, that as a by-product of that, it would be touching novelty to see that, at last, agents and claims adjusters would be able to understand the policy, too.

The insurance industry responded with a virtually united front. The President of the Insurance Federation of Pennsylvania, Thomas J. Finley, objected to readable policies because he said there was no precedent for them. He said other insurance commissioners had never used such a readability approach, nor had the American Bar Association applied such concepts in writing other contracts. And finally, Finley also said legal contracts, moulded to reflect a history of judicial decisions, could not be crafted into readable prose. It was even argued that policies need not be readable, as consumers would not read them anyhow.(4)

In other words, the chief spokesman of the insurance industry in Pennsylvania said, as insurance spokesmen have been saying for decades, that if it has never been done before, it can't be done now. Put in still another way, the insurance spokesman doubted the possibility of doing something for the first time.

We were able to force the insurance industry to start rewriting their policies to make them at least more readable than Einstein's work on relativity.

The idea caught on. Now many insurance companies advertise their readable policies and point to their simplified policies as proof of their eagerness to serve the consumer.

A President of a major national insurance group, James S. Kemper, Jr., even publicly admitted he could not understand the homeowners policy issued by his own company until he spent a few hours with a technical expert.(5)

Now, I'm sure the insurance industry will undoubtedly tell you how they've become consumer-oriented and have come up with readable policies and do not need the pressure of legislation or regulatory action. But look at their record on readable policies. Even on a reform that they now admit was in their best interest, they resisted, dragged their feet, and even after ten years have not completed action on some of the most obvious steps.

For example, the infamous gobbledygook of the Standard Fire Policy of 1943 has remained embedded in the laws of almost every American jurisdiction. The Standard Fire Policy has all the usual insurance gobbledygook, and even contains a 237-word and a 228-word sentence, which may set a record for length if not clarity.

At the time I pressed for readable policies, Mr. Finley of the Insurance Federation noted that the Standard Fire Policy flunked the readability test. But the insurance industry has still not gotten around to getting the statutory requirement for the use of this policy repealed. Certainly, if they were interested in doing so, this task would have been accomplished long ago.

Even so-called readable policies that the industry brags about are not all that readable. Here is a provision from a policy which Nationwide describes as "insurance protection you can count on in a policy you can understand":

"Severability of insurance. The insurance applies separately to each insured. This condition will not increase our limit of liability for one occurrence."

That provision grants important legal rights to the policyholder, but probably not one in a thousand would be able to figure them out by reading the policy. (6)

I checked in my own auto policy, called an "Easy Reading Auto Policy," issued by a major national insurer. It includes a standard provision, used in every Pennsylvania policy, with this language:

"If an X is entered in one or both boxes below, Coordination of Benefits applies to the named insured and any relative.

☐ Medical Expenses is excess to a qualified primary source, including Medicare Benefits, designated by the named insured. If the primary source is not available, a $250 deductible applies to the named insured.

Work Loss is excess to a qualified primary source designated by the named insured. If the primary source is not available, a 2-week waiting period will apply to the named insured."

If that's "easy reading" you try reading it!

Or take this language from a commonly used life insurance policy:

> "If default on a premium payments occur when the cash surrender value indicated in the Table of Guaranteed Values together with the cash value of paid-up endowment dividend additions and dividend accumulations less any indebtedness will purchase an amount of paid-up endowment insurance which exceeds the amount of extended term insurance provision described in Section(1) above, then the Policy will be continued under the paid-up extended term insurance in lieu of the paid-up endowment insurance provision."(7)

Other "easy reading" policies can be found with the standard insurance gobbledygook, without even further definition being included in the body of the policy: Short rate table; Actual cash value; Abandonment; Inherent vice; Vermin. As you might imagine, these terms often have special and technical meaning in an insurance policy.

And sometimes the appearance of readability is simply a trap for the uninformed consumer, because language is used that has one meaning for the consumer and quite another meaning for the insurance adjuster when it comes time to pay a claim.

For example, the fire policy says it pays for loss due to fire. But what if someone accidentally throws her diamond ring into a blazing fireplace? That would seem to be loss by fire to a consumer. But court decisions say that the fire policy only covers "unfriendly fires" -- that is, those which have escaped from where they are supposed to be.

A "friendly fire" is one located where it's supposed to be -- in the fireplace -- and therefore any destruction it causes (of the diamond ring

accidentally tossed into the flame) is not covered.(8)

Despite that kind of misleading language, the insurance industry has been more than content to stick with the language of the fire policy, and other similarly misleading language.

In fact, few policy provisions are now written with sufficient clarity to prevent distortion at the moment of truth -- when it's time to pay or deny a claim.

The readable auto collision and comprehensive policy, in the event of a total loss, is supposed to pay "actual cash value of the stolen or damaged property; or the amount necessary to repair or replace the property." Yet, claims adjusters will often use a so-called "Red Book value" to come up with the amount to be paid -- which does not take into account the actual condition of the policyholder's vehicle. This has been one of the most common and persistent complaints I have received from policyholders over the years.

For example, a man buys a new car for $12,000 dollars. It's stolen a few days later. An adjuster attempted to apply a book value and depreciate it several thousand dollars. Only after I intervened, was the policyholder paid in full.

The same kind of problems occur on property under the homeowners policy, where depreciation may be unreasonably and improperly applied.

And another example of how bewildering policy language and interpretation becomes even on readable policies when it's time to pay a claim involves a common occurrence of a tree falling over on a house, due to a windstorm.

The homeowners policy pays for windstorm. But the usual interpretation is that the policy pays for the damage to the roof, but <u>not</u> for the cost of removal of the tree.

Despite much public relations lip service from the industry about readable policies, other examples could be catalogued at great length from every line and type of insurance. And this is an issue on which the industry has tended to be more responsive because of the intense public reaction to insurance fine-print and doubletalk.

But even here, as the surveys of the industry demonstrate, it has not been successful. A survey just reported by the Insurance Information Institute found 39 percent of those with homeowners policies believed they are not covered for tornadoes, hurricanes and windstorms, when that coverage is standard.(9)

That survey also found 30 percent of those living in California think their homeowners insurance covers earthquake, when in fact, experience shows only about 5 percent are covered. And the survey found 52 percent of policyholders in Texas think their homes are covered for flood damage, when in fact only 4 percent are so covered.

And this is only part of a larger failure of the insurance industry to make its product and price understandable to the consumer.

Need for Information on Quality of Insurers

Financial Strength of Insurer

The insurance industry and its regulators have done virtually nothing to educate the consumer on how to select financially sound insurance companies or to give the consumer vital information on this process.

It has often been said that insurance that is not certain is not insurance at all. Yet, the typical buyer is not provided with the information on financial soundness and reliablility that should be an automatic part of the selection of an insurer.

My quick review of the "Shopper's Guides" published by insurance departments and industry trade associations, did not uncover a single one with adequate advice on how to select a financially sound and reliable insurer.

"A Consumer's Guide to Life Insurance," published by the American Council of Life Insurance says: "Is the insurance company licensed in Florida?"

New York's "Consumers Shopping Guide for Life Insurance -- Cost Comparison Tables" says: "Deal with a New York licensed company."

But it would be easy to inform the consumer on the relative financial strength of the companies in the marketplace. When I was Commissioner in Pennsylvania, we published a booklet called a "Shopper's Guide to Financially Sound Insurance Companies," in which we listed all insurers licensed in Pennsylvania with the two highest financial ratings from the A.M. Best Company, the leading publishing authority on the financial strength of insurers.

We also included financial ratings in other guides, such as the "Shopper's Guide to Health Insurance." And in one life insurance guide we demonstrated that the 10 lowest-cost companies had the top financial ratings, while the highest-cost companies, more often than not, had low financial ratings.

Virtually all insurance experts utilize financial ratings when making decisions on the acceptability of an insurer. The conventional wisdom is to stick to one of the many companies with an A-plus or A rating from the A.M. Best Company.(10) And more recently, in view of the financial vulnerability of insurers, there has been a trend toward insisting on A-plus insurers -- who not only now hold that highest rating, but have also held it for a number of years.

This kind of information for the consumer is even more important now than ever before with the Baldwin-United fiasco still freshly in mind, and with insurance spokesmen predicting severe problems ahead.(11)

Quality of Claims Service

But financial ratings alone are not enough. The consumer knows little about a company if he does not know about the fairness of its claims policy and the efficiency of its policyholder service.

There is virtually no reliable, objective and easily consulted sources of information on insurer quality.

The New York Insurance Department has made a start at providing this kind of information with its publication of its "Annual Rankings of Automobile Insurance Complaints" (February 2, 1984).

The Department used complaints against each company "found to have been justified to some degree or which raised a question of fact or law beyond the Insurance Department's jurisdiction."

Then a complaint ratio was calculated by dividing the annual number of complaints by the annual automobile premium volume of each company, expressed in millions of dollars.

The Department concluded that despite the limitations of such a ratio, "the rankings provide a reliable and consistent method of evaluating the quality of carrier service over an extended period of time."

This kind of information is vital, not just in New York for auto insurance, but in every state for every line of coverage.

In some lines, this kind of claims information is even more important than in auto insurance. Certainly, when buying disability income insurance,

you're buying blind if you don't know a good deal about the claims paying policy of the company.

Need for Life Insurance Information.

Rate of Return.

Nor have insurance commissioners or companies given the consumer needed information on premiums, costs and rate of return.

Only after pressure from outside the insurance industry, were slow and reluctant steps taken toward cost disclosure in life insurance. But even here, after more than 15 years of debate, no disclosure information is forthcoming on rate of return on whole life insurance, which is nothing more than a combination of a savings account with an insurance policy.

Failure to give rate of return information is the equivalent of a bank taking deposits without disclosing the rate of interest that's going to be paid. But what is more astounding is that the life insurance industry has had remarkable success selling this financial pig in a poke.

When the whole life insurance product is sold, it is said to be a convenient way to save and invest. But when information is sought on the products rate of return, then we are told it should be viewed strictly as insurance, not as an investment instrument. Or explained another way, the argument is made that the insurance contract is inseparable, and that it can't be divided into a savings and insurance segment even for the purpose of determining rate of return. When it comes to word games, the life insurance industry in 1984 makes George Orwell look like an amateur.

And what is most astounding is that the industry has managed to get away with this farce by pulling the wool over the eyes of the regulator, the legislator, and the consumer.

You must assume that if the seller of an investment instrument wants to deny its investment nature and withhold information about its rate of return, there must be a reason. And there is. The 1979 study by the Federal Trade Commission demonstrated a rate of return on whole life insurance so low -- less than 2 percent -- that if it were disclosed no one would buy it. Others have demonstrated an equally low or lower rate of return.(12)

Form and Time of Disclosure

The disclosure now made in most states is inadequate on other counts as well. The one company the consumer is dealing with discloses information about the policy offered for sale.

If a would-be buyer wants information on more companies, he has to face a battery of life insurance agents -- which even the bravest buyer may not have the stomach for. And he has no guarantee even then that he'll come up with a low-cost company.

What the consumer needs -- at point of sale -- and also even before he enters the market is a "Shopper's Guide," showing premiums, cost indexes, and rates of return on all or a substantial segment of the insurance marketplace. The guide might even list the ten or twenty lowest-cost and highest-cost companies.

This could be done easily by preparing "Shopper's Guides" and offering them to the public and as part of a disclosure requireme . at time of sale or proposed sale. Now, a Guide may be used during disclosure, but it does not contain premium comparisons.

Now, it's a life time endeavor to get cost information from agents, and that's made doubly difficult by the unwillingness of many agents to quote premiums and cost indexes over the phone.

Need for Adequate "Guides" and Disclosure for Other Lines of Insurance.

Despite the power of "Shopper's Guides" to change the marketplace -- to force companies to lower excessive premiums and to eliminate gimmick policies -- to heighten competition -- to inform the consumer and enhance efficiency and satisfaction in the marketplace[13]-- insurance commissioners have been, as usual too little and too late, in giving the consumer his due.

This is true not only for life insurance, but for all other lines. Most of the "Shopper's Guides" produced by state insurance departments do not have premium comparison -- so they amount to nothing more than a consumer advice column.

And even in states that have produced guides, they are typically not available in all lines, and sometimes go for years without updating or revision.

Take my home state of Pennsylvania. Although we pioneered in the "Shopper's Guide" concept from 1971 to 1974, with guides for term, whole life, industrial life, auto, homeowners, mobile home insurance, snowmobiles, and health insurance, the Pennsylvania insurance commissioners over the last ten years have never produced a life or health guide and have only intermittently published homeowners and auto guides.

And even at this late date, many states have not yet published their first "Shopper's Guides" with or without premium comparisons. Only recently a major stir was initiated in the Baltimore papers by the Maryland Insurance Commissioner's announcement that he would soon publish a guide to auto insurance. Most states still have not published any guides with premium comparison.

Guides should not only be required on key lines of insurance (life, health, auto homeowners, perhaps other), but they should be part of a standard

disclosure at time of sale.

One of the reasons for requiring disclosure is the built in conflict of interest of the agent who is torn between the right policy for the customer and the highest commission paying policy for himself.

It is not difficult to surmise who comes out the victor in that tussle.

A field survey of 92 insurance agents in Philadelphia by the Pennsylvania Insurance Department found less than 30 percent volunteered information on no-fault discounts or collision or comprehensive deductibles which can reduce premiums 20 to 40 percent.(14)

Even when pressed for "cheaper prices" less than 50 percent of the agents told the customer about the no-fault discount offering mandated by law, which could reduce premiums.

Then Insurance Commissioner William Sheppard (who has since gone to work for the insurance industry) concluded "there is no economic incentive for agents to make cost disclosures since lower premiums for the consumer mean lower commissions for the agent."

He went on to say: "The best efforts of the consumer to get a fair deal are being thwarted at the very doorstep of the auto insurance marketplace -- the agent's office... We have uncovered widespread patterns of incompetence, professional negligence, general consumer abuse and even outright fraud that draw us beyond the conclusion that this is merely the work of a few bad apples."

One of the remedies Sheppard suggested was disclosure in connection with auto insurance sales.

And this Pennsylvania survey is in line with the other study cited before this committee, that found agents decide half of the time where to place

business based on what is best for the agent.[15]

Publication and Distribution of Guides as Condition of Legalized Price-Fixing.

While the consumer struggles for and goes without needed premium comparisons, price-fixing insurance companies are privately circulating premium comparisons for the information of insurers only.

For example, the Insurance Services Office sets rate for member companies for auto and homeowners insurance. And it circulates, a complete list of the rates, for the entire state, to each of its members on a periodic basis.

As this Committee of Congress is now re-examining the McCarran Act, it should consider, at the very least, requiring that rating bureaus, given the authority to set prices together, should also have the duty to make public their rate comparisons and provide them to each of their potential policyholders, along with needed explanatory material, to put the comparisons in perspective.

If the McCarran Act can sanction price-fixing, in the name of the public interest, it can also require the publication and distribution of premium comparisons, also in the name of competition.

Any revision of the McCarran Act should set down such standards for state insurance regulation and for disclosure and competition which the insurance industry would have to follow. The questions raised by the Committee point to some of those areas of concern, but different lines of insurance may require different treatments.

Pay-Out Ratio.

The pay-out ratio, sometimes referred to as the loss ratio or benefit cost ratio, should be available for buyers of medical and hospital expense

policies as well as other health insurance policies.

These policies are often so varied in their benefits, coverage and exclusions that they are not comparable and therefore premium comparisons are of more limited value.

A pay-out ratio gives the buyer some sense of the value of the policy by showing him how efficiently the company returns premiums in the form of benefits (that is, losses or claims paid), and how much of the premium dollar gets burned up in commissions, other expenses, and profits.

This pay-out ratio was used by the Pennsylvania Insurance Department in its "Shopper's Guide to Health Insurance" in 1973. That showed pay-out ratios on individual (as opposed to group) policies that ranged from 29.8 percent of the premiums dollar all the way up to 133.6 percent of the premium dollar.

That guide showed overall loss ratios for each company for all of its individual health insurance policies. Even more useful would be loss ratios for each particular class of policy.

Required disclosure of loss ratios would provide consumers with a better basis for policy comparisons but would also red-flag alot of junk insurance that has often been sold to produce extremely low pay-out ratios. That would include much of the airline flight insurance, cancer insurance and other dread disease coverage, and credit life insurance.

To supplement pay-out ratios, consumers could also be given other related information. That could include benefits per policyholder per year expressed in dollars. In addition, policyholders should be furnished with information on how much they would receive in the event of certain hypothetical claims.[16]

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Commission Information and Disclosure

Another piece of information that should be available to consumers is the commission that will be paid to the agent for the sale. The commission information will let the consumer know any incentives the salesman has for pushing one product rather than another, or one company rather than another.

Some companies pay higher commissions than others, and some companies have high and low commission policies. Some types of policies pay higher commissions than others. And agents may be able to provide lower cost coverage by moving to lower commission companies, or lower commission policies. Although reverse competition is most commonly mentioned in the credit life insurance business, there's an element of it in all other lines as well, with companies competing for agents with high commissions.

Commissions on life insurance may run 100 percent or more of the first-year premiums. Most of the low-cost companies pay about 50 percent on whole life and about 35 percent on term. And whole life premiums are often more than double or triple the premiums for term, for the same amount of coverage, so sometimes higher commissions are applied against a higher base.

Those commission differentials may be one reason an agent may push whole life rather than term and the consumer should at least be aware of the potential cause for bias.

Disclosure of commissions -- which are heavily front-end loaded in life insurance -- would also encourage the marketing of more efficient products once the consumer better understood where his money is going.

In the securities business, disclosure of loads and commissions has encouraged the sale of no-load funds rather than front-end loaded and other high commission products. In the securities business, it's difficult to market a high load, low return product. In the life insurance business, the

high load, low return products have been one continuing billion dollar bonanza.

Only by obscuring the facts and confusing the consumer, can the life insurance industry continue to profit on such a product.

McCarran Amendment to Outlaw Competitive Barriers

But disclosure alone won't destroy all the barriers to competition which the insurance industry has built into the fabric of insurance law and regulation.

Efficient marketing methods have been outlawed by the insurance law of every state. Group insurance has been outlawed in many states on the theory that lower rates for group auto insurance would be discriminatory even if justified on the basis of lower expenses.[17]

These and other provisions of state laws that outlaw or discourage more efficient forms of insurance marketing have been a national scandal for decades.

Back in 1970, in a study I co-authored for the U.S. Department of Transportation, it was concluded that: "There is an urgent need to strike down unreasonable barriers in the path of mass marketing so that it may help provide a more adequate and equitable insurance market."[18]

Among these barriers are prohibitions against using credit cards to sell insurance, prohibitions of group insurance sales, and prohibitions of other mass marketing techniques.

In order to eliminate these and other barriers, an amendment to the McCarran Act was proposed that would "forbid any unreasonable restraints on the free marketing of insurance." Details would be left to enforcement by the courts.

But details could be spelled out for barriers that should come down, but whose judicial classification might be problematical. Among such barriers are the anti-rebating laws found in the insurance codes of every state, which prevent agents from cutting their commission and giving it to the buyer.

One member of Congress has described anti-rebating laws as "anti-competitive" and "one of the most costly and enduring price fixing schemes ever perpetrated on the American public."[19]

<u>Institutionalizing Countervailing Consumer Power.</u>

You could do both the consumer and the insurance industry a favor by creating institutions to challenge and critique the performance of the insurance industry and its regulatory demands.[20]

The basic regulatory problem is that the insurance industry is allowed to wallow and rock along in the path of least resistance, opposing change, whether beneficial or detrimental to its interests, and hopelessly married to the status quo.

There are two possibilities to suggest. One would be for each state to set up an office of insurance advocate, with power to challenge the insurance industry in regulatory proceedings. This model has been implemented for utility regulation, and can provide some voice for the consumer.

Still another model is the Citizens' Utility Board (CUB) of Wisconsin which was created to provide testimony and evidence on behalf of consumers at utility rate hearings. CUB receives no government funds, but is supported by utility payer contributions. Each utility customer gets information about CUB in their bill envelopes and they may join for $3 and make other contributions.

CUB has received mixed reviews.[21] But I would certainly endorse Ralph Nader's suggestion to this committee that this type of organization is one of the few workable proposals on the table to provide some kind of voice for the consumer in insurance as well as utility matters.

Without some new methods of introducing the consumer's viewpoint to the process of insurance regulation, we are likely to continue to get the sorry and bizarre results that have been achieved in the past.

FOOTNOTES:

[1] Philadelphia Inquirer, June 2, 1984, p. 1B.

[2] Philadelphia Inquirer, November 11, 1983, p. 1A.

[3] The Flesch readability scale runs from 100 (most readable) on down, and negative results are possible. The Bible scores 66.97. Time Magazine, 52.30. Einstein's, The Meaning of Relativity, comes in at 17.72. The then standard auto policy came in at 10.31. And there were homeowners policies that came in with negative scores.

[4] Shapiro, How to Keep Them Honest (Emmaus, PA.: Rodale Press, Inc., 1974), p. 127.

[5] Kemper Insurance Press Release, December 23, 1975.

[6] For an explanation of the meaning of this provision, see Keeton, Basic Text on Insurance Law (St. Paul: West Publishing Co., 1977), p. 230.

[7] Alliance of American Insurers, Policy Kit (Schaumburg, Ill.: Alliance of American Insurers, 1983), p. 320. This is a collection of policies "commonly used by many insurers in the United States."

[8] Rejda, Principles of Insurance (Glenview, Ill.: Scott, Foresman & Co., 1981), p. 106.

[9] See discussion in article entitled, "Industry Urged to Stress Consumer Education," National Underwriter (Property and Casualty Edition), May 25, 1984. p. 14.

[10] For 1983, this was the classification of life and health companies by A.M. Best. A-plus, 268 companies; A, 255 companies; B-plus, 164 companies, B, 120 companies; C-plus, 57 companies; C, 27 companies; Omitted, 100 companies; Inapplicable, 172 companies; Deferred, 24 companies; Not Eligible, 349 companies; and Not Assigned, 35 companies. There are similar ratings for Property and Casualty Companies.

[11] For example, the President of Johnson & Higgins, a major insurance brokerage recently said that the strength of the property and casualty companies have been "sapped... to a dangerous degree." Business Insurance, June 18, 1984, p. 2.

[12] Hunt, Taking the Bite Out of Insurance (Alexandria, Virginia: National Insurance Consumers Organization, 1982), p. 33.

FOOTNOTES (CONTINUED):

[13] Denenberg, "A New Approach to Regulation," The Progressive, December 1972, p. 17.

[14] News Release of the Pennsylvania Insurance Department, September 25, 1978.

[15] Cummins and Weisbart, The Impact of Consumer Services on Independent Agency Performance, 1977.

[16] This approach was used in a recent article on Medigap policies, "Medicare-Supplement Insurance," Consumer Reports, June 1984, p. 347.

[17] Vanderhoof-Forschner, "Regulation of Group Auto, "Journal of Insurance Regulation, September 1983, p. 95.

[18] Kimball and Denenberg, Mass Marketing of Property and Liability Insurance (Washington, D.C.: U.S. Department of Transportation, 1970), p. 109.

[19] Congressional Record, September 16, 1981, p. H6321.

[20] Denenberg, "Insurance Regulation: The Search for Countervailing Power and Consumer Protection," Insurance Law Journal, May 1969, p. 271.

[21] For some recent critical comments see article entitled "Watchdog of Wisconsin Gets Mixed Reviews," National Underwriter (Property and Casualty Edition) May 25, 1984, p. 4.

APPENDIX:

1. A selection of "Shopper's Guides" published by the Pennsylvania Insurance Department.
2. "The Shopper's Guidebook," a commercially published compilation of the guides of the Pennsylvania Insurance Department.

Chairman RODINO. Thank you, Mr. Denenberg,

Mr. Denenberg, in your testimony, you mentioned that insurance gets less, and I quote, "indepth, high-quality, media coverage than almost any other industry and therefore its viewpoints are not always critically examined."

I served as a member of the National Commission which reviewed the exemption provided under McCarran-Ferguson and the recommendation made there was that we not only review but we consider narrowing the exemption.

We determined that it was important that we hold these hearings in order that this committee be better informed, and we have been seeking to get this kind of information so that we may know whether we should proceed in that direction legislatively.

Following up, though, on the quote to which I just now made reference, I, too, am a little surprised—in view of the substantial interest there is in this industry and the amount of money and the number of consumers that are involved—that these hearings have not been covered by the news media. Do you have any opinion as to why this is occurring?

It would seem to me that, in an area where the consumer is affected, certainly the news media, should have an intense interest because it's such a big industry, it's so vast. In addition, the National Commission for the Review of Antitrust Laws and Procedures recommended that Congress review and consider narrowing the insurance industry's antitrust exemption.

In light of this, can you tell us why there has been a lack of media coverage at these hearings?

Mr. DENENBERG. I think there are a lot of reasons. One reason is that I think the insurance industry has the media confused just like they have everybody else confused. They've been giving them double talk for a long time.

The second reason is that the insurance industry is really not open with the media. Despite the fact that it's regulated and theoretically all the information should be available, I had the leading financial reporter of the New York Times tell me that he quit the insurance beat because he could never get the insurance companies to talk and respond on questions.

I've even done stories where I've called major insurance companies, for example, to find out why their financial rating had dropped. For example, there's Best's Rating Service that rates them A plus, A, B, and I would get comments out of billion dollar insurers like, "We have no comment," even when you would think they would rush to come out with some kind of a defense to defend their financial integrity.

So I think it's a combination of that. The insurance industry has managed to confuse the issue and the insurance industry has also managed to really cover the facts up. It's very difficult to get information.

I think the sad part of it is it's really not as complicated as it seems. The insurance industry will always try to tell you that things can't be done and I found out that 9 times out of 10, it's the insurance industry that's confused; they don't know what they're talking about.

All the examples I could cite from the Pennsylvania insurance experience indicate that no matter what you want to do or no matter what anyone else wants to do, the Pavlovian response of the insurance industry is that it can't be done.

So I think that's why Congress, in effect, has to do something, because it's clear that the State legislatures won't.

Chairman RODINO. Mr. Denenberg, on page 4 of your prepared statement, you discussed the lack of countervailing power for the consumers of insurance. And later in your testimony, you also made reference to the proposal that was suggested by Mr. Nader, who appeared before this subcommittee. That proposal was to consider chartering a national organization of insurance consumers with voluntary membership and dues.

I wonder about this, because, isn't competition the best leveler? If the industry were to function competitively with complete information and no artifical barriers to competition, would there then be a need for such a group?

Mr. DENENBERG. Well, I would agree that if you could achieve competition, it would be the best solution, but I think you have to face the reality that we're far away from competition, that that's not going to come to pass quickly. In fact, the insurance industry talks in Orwellian inversions. When they talk about competition, they're usually talking about some anticompetitive measure. When they talk about competition, they're usually talking about their right to do what they want to do, in terms of setting rates.

So I think if someday you can bring about competition in the insurance industry through some of the things that your committee is considering, that would be the ideal solution, but I don't think that's about to happen. And I think one of the services an industry—rather one of the services a consumer organization could provide would be to push the insurance industry to do what it ought to do. It would be like a consultant to the industry, because they don't have enough sense to take the elementary measures that they ought to. They did not have enough sense to make policies readable. They don't have enough sense to give consumers premium information. They don't have enough sense to go toward more efficient insurance marketing methods.

So I think you'd be doing the industry a favor and the consumer a favor by getting someone in there who can raise issues. One of the difficulties—you talk about why the media doesn't cover insurance, typically, the only one that's prepared to talk about insurance are insurance people and they don't want to say anything, and when they say something, it's usually wrong.

Now they're all fine people, but I had one right before this committee hearing tell me—before I started to testify, tell me that it's no more difficult to tell the price of life insurance, whole life insurance, than the price of eggs. Now that's a great statement, but it's nonsense and everybody knows it.

Now one thing an insurance consumer organization could do is, it could at least provide spokesmen, so when you wanted to do a story you could have more than the double talk and the babbling confusion of the insurance industry. You construct a story. I think that's one of the great services of Ralph Nader's National Insurance Consumer Organization. There is someone you can go to, and

they will give you something other than the party line on insurance. The regulator, incidentally, should serve that purpose, but in Pennsylvania, I find most regulators come out of the insurance industry, or often come out of the insurance industry, and when they're done with their job, where do you think they want to go back? To the insurance industry cocoon. So how do you expect them to speak out on these matters?

They're not. There's nobody available in our society—it's absolutely incredible—to speak out on these issues.

I have difficulty getting an intelligent criticism of the insurance industry in Philadelphia. I might have to come to Washington to get anyone who's willing to challenge the insurance industry. You can't even go to the universities, because the university teachers of insurance are often on grants from the insurance industry, and they've turned our universities into vast intellectual houses of prostitution.

So you would serve a great function by creating an institution that would generate criticism, that would generate countervailing power and that would generate rational discussion.

Chairman RODINO. I think, in your statement, you stated that you were opposed to Federal regulation.

Mr. DENENBERG. When I say I am opposed to Federal regulation, I mean I'm opposed to taking what we now know as State insurance regulation and turning it over to the Federal Government. I am not opposed to repealing the McCarran Act. I am not opposed to Congress saying: "Hey, you guys have to meet reasonable standards of regulation in the State, or we're going to regulate insurance ourselves."

In other words, I don't see why the people of America should be subjected to what everybody knows is a set up job where the insurance industry, by and large, decides how insurance is going to be regulated, where the insurance industry calls all the shots, because the insurance industry, and everybody will certainly have to agree with that, will not do what the consumer needs. They're going to do what the insurance industry needs. In their whole history—you can look at the history of regulatory reform, they have not managed to come up, in my opinion, with a regulatory reform of any note. It's always been forced down their throat. And unless Congress jams it down their throat, it's not going to get jammed down their throat.

Chairman RODINO. Well, when you're talking about the repeal of McCarran-Ferguson, are you talking about the total repeal of the antitrust exemption provided by McCarran-Ferguson? The Commission, as I recall it, merely recommended that there be a review of the exemption with a suggestion that there be a narrowing of the exemption. And the question I'd like to ask is, would a minor amendment to the McCarran-Ferguson Act that merely repealed the prohibition on FTC disclosure regulation have some significant beneficial effects?

Mr. DENENBERG. Well, I think what the committee ought to do is to decide what's wrong with the insurance marketplace and then decide what has to be repealed in terms of what's wrong with it.

For example, about 12 years ago, I did a study with a professor named Kimball for the Department of Transportation on mass

marketing and property and liability insurance. We found that the States were forbidding the marketing of group auto insurance, not for any good reason, but just for anticompetitive reasons. We found that some States were forbidding the marketing of insurance through credit cards. At that time, for that problem, we suggested that Congress, in effect, amend the law so these unreasonable barriers to competition cannot continue.

Now if you find other areas that are improper, I think the law can be amended to require what you're trying to achieve, and I would see nothing wrong with Congress repealing the McCarran Act and putting certain standards on the States, in terms of what regulation has to live up to. In other words, when Congress passed the Act, they simply said, "You're home free, as long as you regulate insurance," but they never got around to saying what is insurance regulation.

Insurance regulation is simply a rubber stamp of the insurance industry today. So I think what Congress has to do is say, if you're going to continue to function as you are, you have to make regulation meaningful, and I don't see any reason why Congress can't impose standards.

Chairman RODINO. Let me ask you a final question.

How important is the lack of information relative to the other competitive problems that are found in the industry?

Mr. DENENBERG. Well, frankly I think there are so many problems, that it is hard to say which is the most important. But I think, certainly——

Chairman RODINO. Is the lack of information high on your list?

Mr. DENENBERG. Well, I think—the reason I like to stress information is that it is a device to bring about immediate change without the need for any laws, without the need, really, to disrupt anyone. And it is something that nobody can possibly object to.

When I was insurance commissioner and put out these shoppers' guides——

Chairman RODINO. Well, excuse me, at that point. I don't know whether you can say that nobody can object to providing more information. We've had previous testimony, some of which has been that there's adequate information, that the information is sufficient, and as a matter of fact, sometimes it's overwhelming.

Mr. DENENBERG. Well, I think you're going to get people that are going to tell you 2 plus 2 is 8.

My opinion is that when you investigate the facts—when you go out—I don't know who these guys are talking to. I talk to dozens of consumers every day, and they are so confused, it's pathetic. If somebody is telling you the information is there, I say they're out of their mind, they're nuts or they're lyin', because it just ain't there. I am a man who studied insurance for 30 years, and when I want insurance information, I have difficulty getting it. It's very difficult to compile, and there is no reason it should not be readily available. It's actually there.

As I point out in my testimony, the insurance companies that are fixing prices actually compile this information for their own benefit. The Insurance Services Office actually puts out a shopper's guide which they give to the companies, but which they don't give to the public.

Chairman RODINO. Mr. Denenberg, we've had testimony from agents for insurance companies who've come here and who have said that they're always available to the prospective insured, and any information that he seeks, they're willing to give. They feel that they provide consumers with sufficient information. They've got loads and loads of brochures or whatever it is that the company provides them. They say they are no more than a telephone call away, that they will be glad to make comparisons for prospective policyholders and that this benefits the insured.

Mr. DENENBERG. Well, you try doing that. I mean, you can call up insurance agents. No. 1, they don't even like to talk to you over the phone. No. 2, they would not be able to make the premium comparisons if they wanted to, and they probably don't have the information themselves. I'd say that is pure baloney, and I'd say something else about insurance agents. One of the problems with insurance agents is that they don't tend to be too competent. They often don't understand what they are doing themselves. When I was insurance commissioner, I used to make—if I may—I made various estimates in connection with my work about the number of incompetent lawyers, the number of incompetent doctors. I said, for example, that perhaps 5 percent of the doctors are incompetent, 15 percent of the lawyers are incompetent. When I made those estimates, I always got criticism. People always said that estimate is way too high.

When I estimated that 50 percent of the agents were incompetent, the president of the agents association in Pennsylvania called me up, and he said, "Your estimate is too low. It's more than 50 percent." Maybe it's 70 or 90 percent. I don't think you can count on getting this kind of advice from insurance agents. They tend not to be competent, and even the competent ones don't have the information you're talking about. It should be available. We put it out when I was in Pennsylvania. And you check these guides that they were talking about. They came before you and they gave you this baloney about here is your home State. And we have all this information. And they said they had four big boxes of material. I'll tell you where you can put those boxes. I'd better not tell you where they can put those boxes, because those boxes aren't going to have the information that you need.

You can put out the stuff. I have a lot of it here, but it's junk. It's Mickey Mouse stuff, because it just gives you a lot of bland consumer advice. The consumer wants premium information. He wants information he can use in shopping. And it's not fair. It's difficult to get. And it should not be.

Chairman RODINO. Mr. Denenberg, I'm not going to defend the agents———

Mr. DENENBERG. That's good.

Chairman RODINO. Well, I'm not going to defend them, because it's not within my jurisdiction to defend anyone, and I don't know that they need any defense from me, except when you suggest they're incompetent. They seem to be doing all right.

Mr. DENENBERG. Well, there's no connection between making money and competence in our society. You've discovered that, haven't you? [Laughter.]

Chairman RODINO. I'm not going to answer that. [Laughter.]

Mr. DENENBERG. Nothing personal, mind you. [Laughter.]

Chairman RODINO. Thank you very much, Mr. Denenberg. Mr. Hyde.

Mr. HYDE. Well, Mr. Chairman, if this was such an exciting subject, and we should have the room jammed with reporters and television cameras and recording devices, I would think those of us whose vocation is plumbing into the depths of industries to find the conspiracies that lurk therein and exposing them to the light of day, would have showed some interest. The fact is, everybody's got 42 things to do, and the media probably finds Eden Pastore more glamorous than Mr. Denenberg. I don't know why. [Laughter.]

I find Mr. Denenberg infinitely more fascinating than Eden Pastore, but—

I just want to say a couple of things. First of all, I think this series of hearings is important. It is long overdue. I think there's much to be learned about an arcane industry from our point of view and from the consumer's point of view. At the same time, sometimes hyperbole gets in the way of a measured, and I hope successful, investigation into the esoterica of the insurance industry. So, you know, to call half of the agents incompetent isn't helpful, but it does grab attention. But you have an awful lot to say of importance, Mr. Denenberg, and I regret that these hearings cannot be held in a more—I use the word "leisurely," let's say thoughtful environment, without the pressures of the end of the session. And I am sure these are simply the beginning.

We were here to 1 o'clock this morning. Many of the members of this subcommittee have been involved in a bankruptcy conference, working out with the Senate some enormously complicated differences, and so my criticism of the inattention of this subcommittee is more a criticism of the workload rather than lack of interest.

But I think these hearings must proceed, and I hope into next year, and we can serve the consumer and the public, and I think you have a great contribution to make. If we can plow through the hyperbole about—to me it's hyperbole; to you it's understatement.

Mr. DENENBERG. I was trying to be conservative. I just thought I'd make that statement.

You might ask some other experts, because, as I said, a representative of the Pennsylvania agents association thought my number was too low. Now you probably have a good agent, you know——

Mr. HYDE. OK [chuckling].

Mr. DENENBERG. Because of your position, but a lot of other people aren't that fortunate. There is a shortage of competent people in our society. The experts now agree that, you know, 5 percent of the doctors are incompetent. Now if 5 percent of the doctors are incompetent, and they receive 8 years of training, you've got to think how many percent of the agents are going to be incompetent when they may be churned out in a matter of days or weeks. Right?

Mr. HYDE. Sure. Sure. OK, I have no further questions, and I thank you.

Mr. FEIGHAN [presiding]. Thank you. Mr. Denenberg, I think it is only regrettable that you are not able to see the attentiveness of

your audience this morning. They're ready to grab me as soon as I'm done. They all represent the insurance industry. [Laughter.]

Mr. DENENBERG. I'd like to go out this way, if I may. [Laughter.]

Mr. FEIGHAN. We've done that frequently ourselves.

Mr. DENENBERG. I have to turn my back to them too. You can at least watch them.

Mr. FEIGHAN. I was interested by your comments regarding the prospects of Federal regulation and your commentary that, as inadequate as you feel State regulation might be, it's the better alternative. And yet I wonder if that is not a commentary applicable only to the current or perhaps even the former state of insurance, that as the insurance industry, being the dynamic industry that it is, continues to change in its character, Federal regulation may become more and more appropriate. And in fact, the industry itself may find itself pursuing Federal regulation in lieu of State regulation.

I make that comment particularly in light of a commentary offered in the cover story of Business Week, and if I could read a brief statement from that. It reads:

> That suggests the sort of vacuum that in the past has attracted Federal regulation to other financial industries. Insurers are far less dogmatically opposed to regulation—that being Federal regulation—than they were before they were all tarred by the Baldwin United brush. "Besides," notes John Carter, president and chief executive officer of Equitable Life Assurance Society, "a plan to offer a variable policy linked to a checking account, for example, would need the approval of State insurance and banking departments of 50 States and also have to conform to 50 different securities laws. That" Carter declares, "is a ridiculous way to do business. It drives us toward a system of Federal regulation in a single regulatory body." [Article in app. 4, at p. 705.]

Under those circumstances and with the changing characteristics of the insurance industry, is it conceivable that we might all agree, consumer advocates, as well as industry representatives, that, in fact, Federal regulation would be much preferable?

Mr. DENENBERG. Well, I think there's a lot to what you're saying and what that article said. There is much to be said for uniformity, and it does get very difficult to deal with 50 different States, especially when they're going in different directions. But I think that more fundamentally, State insurance regulation may not be quite as efficient in the sense that it can't lay down these uniform standards.

I think that even the insurance industry would probably prefer State regulation, if they had some real experience with what a Federal regulator would be. When I started favoring State regulation, it was back in my days as insurance commissioner, when I had to deal with the Federal Government. Now if somebody had an insurance problem in Pennsylvania, they could actually talk to me and they could talk to one of my key people. During the—I guess it was during the Nixon administration they put on some kind of a wage-price freeze and Secretary Connolly was in charge of administering the wage-price freeze, and he put out some edict that the wage-price freeze on insurance would be administered by the insurance commissioners of each State.

I tried calling up Connolly or someone in his department to find out what was going on. And I could not even talk to the 85th assistant of Secretary Connolly. We couldn't get any information, and I

finally said, "Hey, if the Federal Government wants to administer this program, they can do it themselves, because I am not going to do it for them, because I can't even talk to them."

I think the Federal bureaucracy is just hopeless in terms of getting to it, and I think the great benefit of State insurance regulation is, it's there, it's accessible, you can talk to the people involved. You could call up any insurance commissioner today and talk to him if you had to.

When you get something like that in the hands of some Federal bureaucracy, you're not going to be able to get through to them. It's just too big. So I would say that there are a lot of arguments—you know, you could write books on the advantages of Federal regulation, but I think in the final analysis you're going to conclude that with all its defects, State regulation is still the best, because it's accessible, it's closer to the issues, and it's closer to the people.

Mr. FEIGHAN. Well, I would agree with your assessment of the Federal bureaucracy, and if I were in the industry, I would certainly—even from this position—argue against Federal regulation; however, it would seem that given the changing characteristics of the industry, something has got to be done from both the industry perspective, in order to facilitate the marketing of new products, and from the consumer's perspective, in order to insure that the incredible burden that the industry would have to go through in every State does not increase consumer costs.

Mr. DENENBERG. Well, I would say that maybe that just points to the need to improve State regulation, and also improve the market place so you don't have to regulate so much. One of the reasons that so much regulation has been required is that you have this noncompetitive marketplace and if you don't regulate, the consumer is going to get ripped off totally.

Now, to the extent that you can structure a State-Federal system that brings about competition that will be the regulator, you won't have to do as much of this detailed regulation. That's one of the problems. They are regulating everything and it would be better if competition would take the place of all the regulation. Competition is faster. It's cheaper. It's more efficient.

Mr. FEIGHAN. In the expectation of ending on a very positive note here, I was particularly interested in your commentary about readability. It would seem to me that there would be no factor more compelling in the marketplace than the interest in expanding sales. If the insurance industry made an aggressive effort to increase the readability of their contracts, their sales might very well expand.

What industries would you point to as being the vanguard industries in—not industries but particular insurers—as being in the vanguard of increasing the readability of their contracts, increasing the readability of material that they provide to the consumers. Surely the marketplace itself more than regulatory agencies is forcing that on insurance carriers.

To whom would you point to as those——

Mr. DENENBERG. Well, I think it's hard to really single out an industry. There has been some progress in banking and a lot of people did jump on improved readability of contracts because it has

great public relations appeal. But I don't think there's one industry that really stands out.

I don't see any real industry standouts, but I would agree with what you are saying that really smart people in the business see the readability concept as a sales tool because they know that if a contract is readable it's going to be easier to sell and it's also going to be easier to administer. In other words, there was no question about it that the standard auto policy, which I said was less readable than Einstein's theory of relativity, could not be understood by insurance agents, it could not be understood—James Kemper—president of two major national insurers—admitted publicly he could not understand his homeowner's policy. These policies could not be understood by claims people either.

So when you make policies readable, if you really want an efficient organization, that should accomplish miracles for you. Many insurance leaders didn't want to improve the readability of policies at first, but some of the smart ones used to come around and say it's a good idea. For example some of the mail order health insurance people saw the benefits of readability because they said we have to sell and people have to understand the contract. They said they don't have the agent out there to explain the contract. So I think smart people in the insurance industry caught on to the value of making policies readable.

The sad part of it is it doesn't look like there has been much progress. They're apparently so ingrained with their ways that the normal forces don't seem to work on them. I mean the fact that they had to be pushed into readability tells you one thing. The fact that 10 years after they were pushed into readability you still get policies like that [pointing to excerpts quoted in statement]. You ought to ask these life insurance guys to translate that one provision I quoted in my statement. See if they can do it.

Mr. FEIGHAN. Well, we may put them to that test.

Mr. DENENBERG. Would you like me to leave it for you so they can try it?

Mr. FEIGHAN. Well, I'm sure they'll remember it.

Mr. Denenberg, thank you very much for your testimony this morning. It's been very informative and provocative. Thank you.

Next we'll hear from representatives of the life insurance industry. Again, we ask that each of you confine your comments, if you can, to a few minutes. Your written testimony will be included as part of the record.

We are very pleased to welcome this morning Mr. Robert Hunstad, senior vice president and actuary of the Minnesota Mutual Life Insurance Co. of St. Paul, MN. He will be testifying on behalf of the American Council of Life Insurance.

Also, joining Mr. Hunstad will be Mr. W. Wayne Perry, senior vice president, general counsel and corporate secretary of North Carolina Mutual Life Insurance Co. of Durham, NC. Mr. Perry will be speaking on behalf of the National Association of Life Companies and the Life Insurers Conference.

Gentlemen, thank you for joining us. We will begin with Mr. Hunstad.

TESTIMONY OF ROBERT HUNSTAD, SENIOR VICE PRESIDENT AND ACTUARY, THE MINNESOTA MUTUAL LIFE INSURANCE CO., ST. PAUL, MN; W. WAYNE PERRY, SENIOR VICE PRESIDENT, GENERAL COUNSEL AND CORPORATE SECRETARY, NORTH CAROLINA MUTUAL LIFE INSURANCE CO., DURHAM, NC

Mr. HUNSTAD. Mr. Chairman, members of the subcommittee, my name is Robert Hunstad and I'm senior vice president and actuary of the Minnesota Mutual Life Insurance Co. Today, as you stated, I'm appearing on behalf of the American Council of Life Insurance and with me is Richard Minck, executive vice president of the council.

I appreciate the opportunity to present the council's views on the important issues of adequacy and availability of consumer information regarding life insurance products. I should point out that the council has long been a proponent of increasing the flow of consumer information and in fact allocates a substantial portion of its resources to consumer education and the production and distribution of consumer information about insurance.

I'd like to spend a few minutes discussing the various consumer information activities in which the council and its member companies are engaged.

A description of all our currently available materials and programs is attached as an appendix to this statement. Mr. Chairman, I'd ask that these examples of our consumer education materials which I brought along today be accepted as exhibits for this subcommittee record.

[Materials on file with the subcommittee.]

Mr. HUNSTAD. The council works to promote the distribution of consumer materials to a wide variety of audiences through contacts with national consumer and community organizations, better business bureaus, consumer affairs agencies, aging groups, state insurance departments and adult educators such as the extension service of the U.S. Department of Agriculture.

The general public is made aware of the availability of consumer education materials through extensive institutional advertising and the council's toll free consumer hot line. We also reach the general public through broad based media contacts.

In addition, our member companies distribute consumer materials to their policyholders. Over the years millions of booklets have reached consumers in this fashion and I have examples of those and ask that they be accepted as exhibits for the record as well.

[Materials on file with the subcommittee.]

Mr. HUNSTAD. Finally, the council tracks information on life insurance that's available to consumers through outside sources, and for your information, I have here and I'd like to give to you, a computer listing of all the articles that we've kept track of in recent days.

[Listing on file with the subcommittee.]

Mr. HUNSTAD. There is no question there is a tremendous amount of information available for consumers on the subject of life insurance products, and any individual who wants to know about products or companies or cost comparisons can get that information from a wide variety of sources.

One must acknowledge that even with the best information and motivation, most people would find it difficult to grasp, particularly in a short period of time, all the intricacies of various life insurance products acting on their own. That's why we believe the role of the agent is important. With extensive training, expertise and knowledge of the particular needs and goals of the individual consumer, the agent is uniquely able to recommend the appropriate amount and type of life insurance necessary to achieve the intended result.

The most valuable insurance information source for a consumer is the agent.

Mr. Chairman, the life insurance business through the American Council of Life Insurance is committed to providing the most comprehensive, understandable and the most useful information possible about life insurance products. The best. We think we are doing it. But we are never closed to suggestions for improvements. If after reviewing this material you feel that we are falling short in any area of providing consumer information, please let us know.

On a separate topic, the subcommittee has indicated a particular interest in the subject of life insurance cost disclosure. I'd like to address that now. I am the chairman of the American Council of Life Insurance Subcommittee dealing with that subject.

The council strongly supports the concept of cost disclosure and has done so for almost 15 years now. Specifically, we support the model cost disclosure regulation of the National Association of Insurance Commissioners. Today, disclosure requirements based on the NAIC model regulation have been enacted in 38 States and, in addition, are being voluntarily complied with elsewhere, meaning that well over 80 percent of the sales made involve disclosure information.

The NAIC model regulation has been updated and improved twice since it was first adopted in 1973. It requires life companies to give all prospective purchasers a policy summary and a buyer's guide as basic disclosure tools. Included in the policy summary are two types of cost indexes by which the consumer can compare the cost of similar policies.

The NAIC cost indexes answer two key questions. First, if the policy is kept in force for a given number of years, how much will a buyer have paid for it? Second, if the buyer surrenders the policy for cash after a given number of years, what's the net amount the buyer will have paid?

The NAIC Buyer's Guide is a booklet to help people shop for life insurance. It describes how much insurance to buy, what kind to buy and how to compare the price of similar policies. An important objective of the cost disclosure process is to provide enough information on which to base a sound purchasing decision without overburdening the buyer with so much factual data as to generate confusion.

We believe the NAIC model cost disclosure regulation draws such a balance.

I'd like to underscore the fact, despite the testimony that you've heard earlier today, that the system of cost disclosure in this discussion operates in an environment for life insurance that is very competitive today. In the case of my own company, we've made five

changes in price over the last 2 years. Other companies have had similar experiences.

The introduction of new products, such as are referred to in the Business Week article, that you made mention of Mr. Chairman, reflect the increased competitive pressures in the marketplace.

Now, other cost disclosure systems have been suggested from time to time. These other systems we find on analysis offer no fundamental improvement in consumer information. Furthermore, it's clear that some of these alternative disclosure systems provide potentially misleading information and an example of this is the so-called rate of return disclosure.

This approach, the rate of return approach, does not actually produce a rate of return as you would calculate for a savings account but rather makes several assumptions and hypotheses to develop a rate of return index. The danger of using it is that the prospective purchaser is likely to compare this index, this rate of return index, with interest yields offered by savings media such as bank accounts or certificates of deposit, without giving proper consideration to several important facts.

First, this index is very sensitive to the assumptions used in the calculation so it will vary considerably, depending upon the assumptions used. Second, the rate of return index does not take tax affects into account. Because the tax treatment of life insurance differs from that afforded savings accounts and investments, the rate of return index is essentially an after-tax measure. It's doubtful that most people looking at the index would appreciate this.

Finally, an insurance policy where coverage continues for the entire lifetime of the insured, referred to as a permanent insurance policy, has important benefits that are not considered in the rate of return calculation and are not available from savings or investment media.

Another major disadvantage of the rate of return index is that it's not relevant with respect to term insurance. Term insurance now constitutes about half of the individual life insurance purchases in this country, and additional shortcomings are pointed out in my prepared statement.

In summary, Mr. Chairman, we believe that cost disclosure is an extremely important tool for insurance consumers and that the cost disclosure method developed by the NAIC is superior to any that has been suggested.

Once again I express my thanks to the subcommittee for this opportunity to testify and I'd be pleased to answer any questions the subcommittee might have.

[The statement of Mr. Hunstad follows:]

STATEMENT OF

AMERICAN COUNCIL OF LIFE INSURANCE

Before the

SUBCOMMITTEE

on

MONOPOLIES AND COMMERCIAL LAW

of the

HOUSE COMMITTEE ON THE JUDICIARY

on

INSURANCE INFORMATION FOR CONSUMERS

June 28, 1984

Statement Made By:

Robert Hunstad
Senior Vice President & Actuary
Minnesota Mutual Life Insurance
Company

Mr. Chairman and members of the Subcommittee, my name is Robert Hunstad and I am Senior Vice President and Actuary of the Minnesota Mutual Life Insurance Company. I am appearing today on behalf of the American Council of Life Insurance. The Council is the principal trade association for life insurance companies with 598 members, accounting for 95% of the life insurance in force in the United States.

I appreciate the opportunity to present the Council's views on the important issue of the adequacy and availability of consumer information regarding life insurance products. I should point out that the Council has long been a proponent of increasing the flow of consumer information and in fact allocates a substantial portion of its budget to consumer education and the production and distribution of consumer information about insurance.

I. Life Insurance Cost Disclosure

The Subcommittee has indicated a particular interest in the subject of life insurance cost disclosure, an area which has received a good deal of attention from other Congressional committees in previous years.

In an appearance before the Senate Committee on Commerce, Science and Transportation in 1979, we offered the following statement of the life insurance industry's approach to cost disclosure:

"It is simple to summarize our industry's position on cost disclosure. We are in favor of it. We have supported

it for more than 10 years. We have worked diligently to support state regulation to help bring it about on a uniform basis throughout the country. We specifically support the model cost disclosure regulation of the National Association of Insurance Commissioners (NAIC). It was produced four years ago and has already been adopted by 28 of the states. It is being used voluntarily in all states by companies that account for at least 60 percent of the sales being made today. The system of disclosure and cost comparison required by that regulation is carefully designed to help consumers make good purchase decisions."

Now, almost five years later, we can with confidence reiterate the industry's strong support of adequate disclosure to the consumer and can report on additional substantial progress that has been made since the time of the earlier statement. Today, disclosure requirements based on the NAIC model regulation have been enacted in 38 states, and are being voluntarily complied with in well over 80 percent of the sales being made.

Of at least equal significance has been the effort of the NAIC, working together with the industry, to respond to changes in the insurance marketplace. The original model cost disclosure regulation, developed in 1973, was revised and improved in 1976. Last December the NAIC adopted a still further improved version of the regulation. This action was supplemented by the concurrent adoption of

special disclosure requirements for highly popular universal life insurance, in recognition of the special features of this product.

The NAIC model regulation requires life insurance companies to give all prospective purchasers a specific "Policy Summary" and "Buyer's Guide" as basic disclosure tools. The Policy Summary must include figures on premiums and benefits for the policy under consideration. Figures must be shown for certain prescribed policy years so as to provide a representative selection from all the financial facts that might be reported about a policy.

Also included in the Policy Summary are two types of cost indexes by which the consumer can compare the cost of similar policies. On this matter, we should emphasize that no cost index measures the "true cost" of a life insurance policy to an individual. The true cost cannot be determined when a policy is bought. Only after the policy has terminated -- because of death, surrender, or maturity--can one compare the out-of-pocket costs of the policyholder with the benefits actually received. The cost indexes in the model regulation can, however, show how the relative expected costs of different policies compare. Certain assumptions have to be made in calculating these indexes or any other indexes. For this reason, these cost measures are not absolute, and the relative rankings of policies change if a different set of assumptions is used.

The NAIC cost indexes answer two key questions. First: "If a policy is kept in force for a given number of years, how much will a buyer have paid for it?" Second: "If the buyer surrenders the policy for cash after a given number of years, what is the net amount the buyer will have paid?"

The NAIC Buyer's Guide is a booklet to help people shop for life insurance. It describes how much life insurance to buy, what kind to buy, and how to compare the price of similar policies. There are brief, straightforward descriptions of the basic types of policies and instructions on how to use cost comparison indexes. One of the major improvements in the new model regulation adopted by the NAIC this past December is a substantial revision of the Buyer's Guide to take account of recent product developments and to make it more readable; these improvements should greatly enhance the Guide's usefulness.

An important objective of the cost disclosure process is to provide enough information on which to base a sound purchasing decision without overburdening the buyer with so much factual data as to generate confusion. We believe the NAIC model cost disclosure regulation draws such a balance.

The Council has been consistently supportive of the NAIC actions on cost disclosure including last December's action in adopting the improved model. Recently, the Council wrote to all the state insurance commissioners to encourage them to adopt this new regulation in the individual states.

Realizing that this subject is not of a static nature, the Council has a standing subcommittee on cost disclosure matters whose responsibility it is to monitor and review developments affecting the cost disclosure area and make appropriate recommendations.

It is natural that in a subject area as broad as this one there would be a variety of ideas as to an ideal disclosure system. As mentioned previously, a basic aim in the development of the NAIC system has been to provide the consumer adequate information without creating confusion by furnishing too much. Worse than too much information is information that is of no value or is misleading and can be misinterpreted. In this connection, we would like to focus on two concepts that have been suggested as required disclosure to consumers, rate of return disclosure and commission rate disclosure.

The "rate of return" approach that has been suggested in testimony before this Subcommittee does not produce a true or actual rate of return in the same manner as, say, an interest rate credited on a savings account. Rather, it is a rate of return <u>index</u> since the number that is developed is not an actual interest rate or yield but is an index number based on a number of assumptions and hypotheses. The calculation of a rate of return index for a policy uses exactly the same data as to

premiums and benefits as does one of the NAIC indexes called the surrender cost index. Consequently, a policy that shows up favorably, or otherwise, according to the rate of return index will have consistent results on the surrender cost index. Thus, the consumer gains no additional insight from having rate of return as well as surrender cost indexes.

But, even more important from the consumer viewpoint than the redundancy of the rate of return indexes is the capacity that there is for these indexes to mislead an insurance purchaser. The danger is that the purchaser will compare the rate of return index with interest yields offered by savings media such as bank accounts, or certificates of deposit, without giving proper consideration to several important facts:

(1) The index is very sensitive to the assumptions used in the calculations, so it will vary considerably when different assumptions are used.

(2) The rate of return index does not take tax effects into account. The tax treatment of life insurance differs from that of savings accounts and investments. The calculated rate of return is essentially an after-tax yield. It is doubtful that most people looking at a rate of return index would appreciate this.

(3) An insurance policy where coverage continues for the entire lifetime of the insured, referred to as a permanent insurance policy, has important benefits that are not considered in the rate of return calculation and are not available from savings or investment media.

Another major disadvantage of the rate of return index is that it is not available for most term insurance, which is insurance that runs for a specified number of years instead of for the entire lifetime of the insured. Since term insurance constitutes about half of all individual life insurance purchases, the needs of a very substantial part of the insurance market would be left unmet by use of the rate of return method.

Also, the rate of return calculations typically portray lower rates of return, which implies higher prices, for larger policies than for smaller ones. This is a misleading consequence of the way in which the rate of return index is calculated. Actually, the cost per thousand dollars of life insurance generally drops as policy size increases. The surrender cost indexes do not suffer from this defect.

Another suggestion which has been put forth is that the commission payable to the agent be disclosed to a life insurance purchaser. This is once again an area which has the potential to seriously mislead and confuse a buyer and which would not serve any meaningful purpose.

The commission rate is only one of many factors that affect life insurance costs. Actually, it is only one of the items included in the category of company expenses, which in turn is only one of the determinants of life insurance costs (interest and mortality rates are two of the others). For this reason the policy with the lowest commission rate will very often not be the policy with the lowest cost. The commission rate is therefore a poor criterion on which to base a purchase decision.

The issue of commission disclosure is one which I believe the National Association of Life Underwriters addressed in some detail in their written statement of May 3, 1984 so I will not go into it any further at this time.

II. Consumer Information Availability

In testimony by several previous witnesses before this Subcommittee, the view was expressed that consumers are not informed about insurance products and do not know where to obtain insurance information if it, in fact, exists. We can only assume that the individuals who made those statements are simply out of touch with the U.S. insurance industry. Frankly, most people would probably say that they are the recipients of too much rather than too little insurance information.

I would like to spend a few minutes discussing the various consumer information activities in which the Council and its member companies are engaged.

As noted previously, the Council allocates a substantial portion of its budget to the production and distribution of consumer education materials.

Through the years, hundreds of Council-generated booklets, audiovisuals, programs, public information activities, public service announcements and other resources have been distributed to many millions of insurance consumers. Mr. Chairman, a description of our currently available materials and programs is attached as an appendix to this statement. I would also ask that the examples of our consumer education materials which I have brought along today be accepted as exhibits for the Subcommittee record. We are encouraged by the success of these activities, as our research has shown that over the years the public has greatly increased its understanding about life insurance products and policies.

Promotion of Council Materials

Through its various public relations departments the Council works to promote the distribution of consumer materials to a wide variety of audiences. For example, consumers are made aware of the available materials through our work with national consumer and community organizations, Better Business Bureaus and consumer affairs agencies, aging groups, state insurance departments and formal adult educators such as the Extention Service, USDA.

As part of this program, a Council-produced pamphlet, A Consumers Guide to Life Insurance, is now being distributed through the Federal governments' Consumer Information Catalog. In addition, we are sponsoring the development of a Question and Complaint Handling Manual on Life and Health Insurance by the National Association of Consumer Agency Administrators for state and local consumer agency professionals.

The general public is made aware of the availability of consumer education materials through extensive institutional advertising and the Council's toll free consumer hotline. We also reach the general public through broad-based media contact. This includes annual visits to some 200 newspaper editors, seminars for reporters, advertising to the media encouraging them to call the Council for consumer information and periodic news releases on new consumer materials.

Other Sources of Consumer Information

The Council encourages its member companies to distribute the National Association of Insurance Commissioner's (NAIC) Buyer's Guide through their sales forces. Presently, 38 states mandate that the 1976 Buyer's Guide be delivered upon receipt of the policy. A new Buyer's Guide has been produced that reflects recently developed insurance products. As noted previously the Council is actively promoting its adoption by the states.

In addition, Council member companies regularly distribute our consumer materials to their policyholders. Over the years, millions of booklets have reached consumers in this fashion. These materials are also made available to the National Association of Life Underwiters (NALU) for distribution by their agents to schools and community groups as part of NALU's educational efforts.

Further, it is common for our member companies to have their own extensive consumer information operation. Many companies have toll-free telephone numbers for their policy-holders and produce their own consumer publications. Examples of these company efforts have been provided by the Aetna, Pruden-tial, Allstate and Metropolitan insurance companies and I ask that these also be accepted as exhibits for the Subcommittee record. These materials are distributed to schools, civic organizations, public interest groups and policyholders.

Finally, the Council has been tracking information on life insurance that is available to consumers from outside sources. Over the past several years, our information and media departments have identified thousands of articles, bulletins, newsletters and columns devoted to the subject of life insurance and consumer understanding. As graphic evidence of this, we have included in our exhibits a computer printout of many of these recent articles.

The Role of the Agent

There is no question that a tremendous amount of information is available for consumers on the subject of life insurance products, beyond the strictly promotional materials that appear in the daily mail. And any individual who wants to know about products or companies or cost comparisons can get that information from a variety of sources. The major problem that we and other principal providers of insurance information face is an apparent lack of interest on the part of consumers in taking advantage of what is available from all of the previously mentioned sources. It is simply not possible to become an insurance authority as the result of an afternoon's reading, and the average insurance consumer will probably not spend any more time on it than that.

One also has to acknowledge that, even with the best information and motivation, most people would find it very difficult to grasp in a short period of time the intricacies of the various life insurance products on their own. That is why the role of the agent is so important. With extensive training, expertise, and knowledge of the particular needs and goals of the individual consumer, the agent is able to select the appropriate amount and type of insurance necessary to achieve the intended result. We believe the most valuable insurance information source for a consumer is the agent.

Summary

In conclusion, Mr. Chairman, the life insurance business, through the American Council of Life Insurance, is committed to providing the most comprehensive, the most understandable,

and the most useful information possible about life insurance products. The best. And we are doing it.

There is no question that up to date information on life insurance products is readily available to anyone who desires it from a wide variety of sources.

We also feel that cost disclosure is an extremely important tool for insurance consumers, and that the cost disclosure method developed by the NAIC is superior to any other that has been suggested, including the so called "rate of return" method.

Once again I wish to express my thanks to the Subcommittee for this opportunity to testify. I would be pleased to answer any questions the Subcommittee might have.

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APPENDIX

I. Product Information

A. Consumer Hotline

ACLI sponsors a toll-free consumer telephone life (800/423-8000) for requests for information on life insurance, annuities and insurance companies.

B. Consumer Spokeswoman

A full-time staff person is available for speeches and workshop presentations on a variety of life insurance topics. ACLI's spokeswoman is promoted through brochures that go out to national and state organizations and through the central work of ACLI's Community and Consumer Relations Department.

C. Publications

All general consumer information published in booklet form is written in plain language and is available free for individuals and groups by writing to ACLI. All multi-media materials are available on a free loan basis.

1. A Consumer's Guide To Life Insurance. This booklet helps consumers make decisions about their life insurance needs and purchases. It describes what life insurance is, how it works and the major types of coverage available.

   A Consumer's Guide ... is presently being distributed through the federal government's Consumer Information Catalog. All costs are being paid by ACLI

2. Plain Talk About Your Life Insurance Policy. This brochure explains the technical terms found in a life insurance policy in simple language.

3. The Booklet You Have In Your Hand Is Not Designed To Sell You Life Insurance. This booklet uses a question and answer format to provide information about traditional life insurance policies and how they are used by families.

4. Understanding Your Life Insurance. This simplified text on life insurance provides product information and a basic introduction to the concepts and principles of life insurance.

5. What You Should Know About Annuities. This booklet provides a simplified explanation of what annuities are, how they work, the different types of annuities available, how much they cost, and tax considerations updated to latest law. It features a glossary of annuity language.

6. What You Should Know About IRAs. This booklet explains individual retirement accounts (IRAs) -- how they work and why people set them up. It also discusses all of the IRA savings and investment vehicles available. It includes up to date information on savings and a glossary of important terms.

7. A Guide To Life Insurance For Women Only. This booklet answers questions women have about life insurance and annuities. It describes the different kinds of coverage appropriate for single and married women.

8. Policies For Protection. This text-workbook presents various activities to involve students in learning about risk sharing, the uses of life and health insurance, the types of policies available, and the economics of personal insurance.

D. Newssheets

1. Life Insurance News Data and The Family Economist. These bi-monthly news sheets are mailed to business and lifestyle page editors of daily newspapers. They carry information on insurance matters -- from how to shop for life insurance to definitions of technical terms.

E. Instructional Materials

All publications are available free to teachers. Other materials are available on a cost recovery basis.

1. Teaching Topics. A semi-annual newsletter for educators that looks at topics related to life insurance and provides instructional advice.

2. Dealing With Life Insurance. A card game for high school students to familiarize players with the variety of options available in life insurance coverage as well as provide basic definitions of life insurance terms. Set includes five decks of playing cards and instructions for use.

3. Sets, Probability and Statistics. A booklet for students to learn the mathematical concepts of sets, probability, and statistics by relating them to life insurance. A computer program based on this publication is available in Apple Pilot language. Included in the package are four discs and teacher materials.

4. Life Insurance Teaching Kit. This package contains an outline of basic life insurance information and suggested teaching ideas as well as sample life insurance contracts. Teachers can use the unit as a whole or select one of the topics for classroom instruction. The content covers: general insurance principles, the purpose of life insurance products, buying life insurance, the life insurance contract, and selecting an insurance agent.

5. The Basics of Life Insurance. This sound and color filmstrip presents four consumers involved in a discussion of life insurance. Students follow the panel as they assess the various kinds of life insurance and its uses in contributing to financial security.

F. Answering Media Queries

Media requests for product and other consumer information are handled routinely by staff in both Washington and New York. Consequently, articles on how to shop for annuities, the role of universal life insurance, and how much insurance to buy appear in major newspapers and magazines.

G. Consumer Dialogues

ACLI hosts a series of dialogues with the leadership of various national organizations -- consumer, professional aging and civic groups -- on life insurance topics and issues. These include such groups as the Consumer Federation of America, the National Consumer League, American Association of Relied Persons, Business and Professional Women and the Coalition on Consumer Education.

H. Programs Cosponsored with Professional Agencies and Organizations

1. Better Business Bureau (BBB) Telephone Tips. A series of questions and answers on life insurance products and uses, claims procedures and settlement options was developed with the Pennsylvania BBB for use on a telephone call-in basis. This project is a prototype for a nationwide series.

2. Life and Health Insurance Question and Complaint Handlers Manual. A manual for use by state and local consumer agency professionals is being developed by the National Association of Consumer Agency Administrators and sponsored by the ACLI and HIAA. It will help consumer professionals better answer questions and handle complaints on life and health insurance products and claims procedures.

I. Library Services

1. Allows public access to General Library in-house database which contains citations to articles on topics of interest to the life and health insurance business.

2. Provides reference assistance to public on questions regarding life and health insurance. General Library participates in Inter-Library Loan with other libraries; materials loaned are on subjects related to life and health insurance.

3. Produces series of bibliographies on life and health insurance related topics. General Library distributes multiple copies to anyone who requests them.

II. Financial Planning Information Containing Information on Life Insurance Products and Uses

A. Publications

All financial planning materials are available free for individuals and groups by writing to ACLI.

1. Financial Planning, Especially For Women. This booklet provides comprehensive information for women in the fundamentals of financial planning, the selection and use of financial advisors and the array of products and services available through banks, thrift institutions, life and health insurance companies and brokerage and investment companies.

2. Planning With Your Beneficiaries. This booklet encourages the policyholder and the beneficiary to plan together for future financial security. It discusses wills, trusts, investments and life and health insurance.

3. Let's Talk About Money. This booklet helps families and individuals develop sound financial plans. It provides a breakdown of various types of investments, tips on estate planning, savings, life and health insurance, and credit.

4. Planning For Retirement. This booklet encourages families and individuals to examine financial resources and anticipate future needs in preparation for retirement. It focuses on Social Security, pensions, annuities, IRAs, employee benefits and life and health insurance.

B. Multimedia Programs

All multimedia programs contain slides, a narrative cassette and a user's manual. They are designed for use with groups and are available on a two-week, free-loan basis by writing to the ACLI.

1. Plan For Retirement. This slide/tape presentation illustrates how two couples--one younger and one older--set goals, examine financial resources and anticipate future needs in preparation for retirement.

2. Plan For Your Future. This slide/tape presentation illustrates how to determine financial plans by examining wants and needs, short-and long-range goals and financial resources at various points over the life cycle. The program will help viewers develop financial plans that fit their ages, life-styles and household needs.

3. Your Estate: Planning With Your Beneficiaries. This slide/tape presentation gives general guidelines for estate planning, covering such basic topics as wills, life and health insurance, pensions and other employee benefits and encourages the use of professional advisors in developing an estate plan.

4. A Game Plan For Employee Benefits. This slide/tape presentation explains how to best utilize the employee benefits plan available to you and takes a look into the future, discussing the changes most likely to occur in employee benefits packages.

C. Instructional Materials

Most materials are available free to teachers. Mailing and handling fees are charged.

1. Personal And Family Financial Planning: Strategies For Teaching. A collection of 30 instructional strategies to teach elements of personal and family financial planning. Contains lesson plans, student materials, and teacher resources.

2. The Resourceful Ones: A Systematic Approach in Financial Planning. This filmstrip package helps students understand the financial planning process. They will explore their own financially-related goals (Cost: $25).

3. Personal And Family Financial Planning: A Staff Development Workshop for Secondary School Trainers And Teachers. This 18-hour workshop is designed to help secondary school teacher trainers improve and update financial planning knowledge and teaching strategies.

4. Personal and Family Financial Planning for Multicultural Adults: A Staff Development Program for Adult Basic Education Teachers and Trainers. This 12-hour workshop is designed to train adult educators to help recent immigrants and native Americans from differing cultural backgrounds deal with money management and financial planning.

5. Personal and Family Financial Planning: A Staff Development Workshop for Community College Trainers and Faculty. This 18-hour workshop is designed to help community college faculty and trainers update and expand financial planning knowledge and teaching strategies.

6. Adult Financial Planning Matrices, Parts I and II. These worksheets are designed for professionals in the field of financial planning to help teach individuals how financial needs and responsibilites change over time.

Mr. FEIGHAN. Thank you, Mr. Hunstad. Mr. Perry.

Mr. PERRY. Mr. Chairman, members of the subcommittee, my name is Wayne Perry. I'm senior vice president, general counsel and corporate secretary of the North Carolina Mutual Life Insurance Co., Durham, NC. I'm here today representing two associations for life insurance companies: The Life Insurers Conference, with the president, G. Mason Connell, seated at my left, an association of some 80 companies engaged in the home service market, and the National Association of Life Companies, which is represented by the executive vice president, Roy Woodall, an association of 460 small to medium-sized life companies.

The 1976 version of the NAIC cost disclosure regulation is now the basis of the cost disclosure requirements in 33 States. The newest version of the model regulation was adopted by the NAIC last December.

Shortly after the 1976 revised model regulation was adopted, both the LIC and the NALC urged the adoption of the new model. However, by the time the FTC entered the picture in 1979 and issued its staff report urging a new approach to cost disclosure, it was becoming apparent that new insurance products and the changing marketplace had already made the 1976 model cost disclosure regulation somewhat obsolete. The NAIC's own study recognized that the 1976 model was outmoded and so it initiated proceedings in 1980 to revise the model again.

It was during this period that we began to question the need or value of any mandated disclosure system. With the dynamics of a free marketplace operating continually to develop new products to meet consumer demand, any disclosure system geared to a certain type or generation of life insurance products will obviously be outdated as soon as the products themselves change.

During the period of NAIC's deliberations to update the 1976 model regulation, it became abundantly clear that no system of disclosure was without its faults and that each one proposed grew so

increasingly complex so as to defeat its purpose of educating the life insurance purchaser.

Therefore, rather than joining the fray to try to devise the ideal disclosure system of the moment, we feel that it is now the time to pause and ask some fundamental questions.

One, is there really a need for Federal Government interference in the area of life insurance sales through a mandated disclosure system?

Two, what are the costs involved in any mandated disclosure system?

Three, does a mandated disclosure system discriminate against small companies and small policyholders?

The purpose of my testimony is to address these questions and ask your subcommittee to do the same.

As to the need for mandated disclosure, it is our position that there is no such perceived general need on the part of the public and that there is already more than adequate information available to those purchasers who wish to compare products and prices.

Shortly after the FTC released its report in 1979, the NALC filed a request under the Freedom of Information Act requesting all of the complaints received by the FTC from insurance consumers that supposedly precipitated the study. When the FTC finally complied with the request, it produced a total of only 208 life insurance consumer communications. Only 68 related to cost disclosure and 39 of those arose as a result of the publicity concerning the FTC report. Twenty-two of those, incidentally, were favorable to the FTC investigation and 17 were critical.

Thus, only 29 communications from the public regarding cost disclosure had been received prior to the staff report publicity. However, all 208 communications were classified by the FTC as complaints against the insurance industry. No credible study that we know of has concluded that the general life insurance buying public is ill informed.

To the contrary, the January 1984 study conducted by Dr. Lawrence A. Crosby of Arizona State University, which was referred to in your hearings last month, concluded that consumers, for the most part, are satisfied with their life insurance. A similar study on home service insurance in Florida conducted in 1980 by Dr. Robert Ladner of the Behavioral Science Research Corp. found that 90 percent said that their agents had explained satisfactorily to them the policy and benefits coverage.

Life insurance is a very competitive business, and there is more detailed information available as to cost and coverage on a comparative basis than you can find on just about any product in the market. The responsible media increasingly is recognizing this, as can be illustrated by an article that appeared June 4, 1984 in the U.S. News & World Report entitled "Better Bargains Today in Life Insurance." [Article in app. 4; at p. 712.]

As early as 1980, Consumer Reports published a two-part special report on purchasing life insurance. For example, just last month a comparative analysis of the universal life policies of 200 life companies was published by the A.M. Best Co. This gives information on initial expense charges such as policy fees, premium load, renewal expenses, premium charges, guaranteed interest rate, current in-

terest rate, policy loan rate and surrender charges. Other Best's comparisons are available on participating whole life policies and 20-year dividend comparisons. The National Underwriter publishes annually a Life Rates and Data on adjustable premium plan policies and an Interest-Adjusted Index giving specialized policy comparison information covering contracts of over 300 life insurance companies.

This information is provided by our free enterprise system available to those buyers and sellers alike who want it. To mandate that an agent must in addition furnish certain comparative information to a prospective buyer is a negation of our free enterprise system. In what other industry is a salesman of a product or a service under an obligation to describe the cost of competing products or services to prospective buyers?

As to the costs involved in any mandated disclosure system, it is our position that they far outweigh any of the alleged benefits. The Federal Government has set the precedent of requiring that a regulatory analysis, including a cost impact study, be made of any proposed regulation before it is adopted. Our review of the projected costs and impacts of compliance involved in the 1980 NAIC model proposal would severely impact and even threaten the solvency of many smaller companies.

One NALC member company with a premium income of $4 million writing about 4,000 new policies each year did a breakdown of the increased cost and concluded that the added compliance costs for the 1st year would be $124,000 or the approximate amount of its entire previous year's statutory gain.

Just last month another member formally notified the commissioner that to comply with Colorado's new cost disclosure would cost over $95,000, almost three times its previous year's statutory gain. As a result the company has notified its agents and policy holders that it will cease all sales operations in the State effective July 1, 1984. The company in question writes only small burial-type life insurance policies with less than a $10,000 face amount. Do its policyholders need or want, or could they even understand what added benefits mandated cost disclosures would give them? Costs of mandated disclosures would obviously be less per policy as the size of the company increases. Thus we have a situation where the economies of scale alone allow a large company to spread the added cost over a larger base and thus gain a competitive cost edge over smaller companies.

In a recent statistical analysis commissioned by the NALC, the financial statements of 1,491 U.S. life insurance companies were analyzed. Of these, 1,351 or 90.6 percent would be considered as small companies under the new Life Insurance Tax Act, but collectively they hold only 12.5 percent of the assets of the life insurance industry. The other 87.5 percent of the assets are held by the 140 large life companies. These are the companies that can grind out computerized cost disclosures to satisfy any mandated method at a cost per policy significantly less than the smaller companies, especially those smaller companies selling small basic life protection and burial-type plans.

As to the answer to our three questions, we trust that we have illustrated to you today one, that there's no need for governmental

interference in the area of life insurance sales through a mandated disclosure system.

Two, that the costs involved in any mandated disclosure system far outweigh any alleged benefits.

Three, that a mandated disclosure system discriminates against small companies and small policyholders.

I thank you for giving me the opportunity to testify. It's a privilege to appear before you today.

[The statement of Mr. Perry follows:]

STATEMENT OF THE

LIFE INSURERS CONFERENCE

and the

NATIONAL ASSOCIATION OF LIFE COMPANIES

Before the

SUBCOMMITTEE

on

MONOPOLIES AND COMMERCIAL LAW

of the

HOUSE COMMITTEE ON THE JUDICIARY

on

INSURANCE INFORMATION FOR CONSUMERS

June 28, 1984

Statement Made By:

W. Wayne Perry, Senior Vice President
General Counsel & Corporate Secretary

North Carolina Mutual Life Insurance Co.

Durham, North Carolina

Mr. Chairman and members of the Subcommittee, my name is W. Wayne Perry, and I am the Senior Vice President, General Counsel and Corporate Secretary of the North Carolina Mutual Life Insurance Company of Durham, North Carolina. I am here today representing two associations for life insurance companies: the Life Insurers Conference (LIC), an association of some 80 companies engaged in the home service market, and the National Association of Life Companies (NALC), an association of 460 small to medium-sized life companies.

Federal interest in cost information available to prospective life insurance policyholders started as early as 1968 when the late Senator Philip Hart urged that improvements be made and subsequently in 1975 when he introduced his Consumer Insurance Information and Protection Act. During this same period of time the states were developing a model NAIC Cost Disclosure Regulation. The first version was completed in 1973 and then revised in 1976. This 1976 version is now the basis of cost disclosure requirements in 33 states. The newest version of the Model Regulaion was adopted by the NAIC last December.

Shortly after the 1976 revised Model Regulation was adopted, both the LIC and the NALC urged the adoption of the new Model. However, by the time the FTC entered the picture in 1979 and issued its Staff Report urging a new approach to cost disclosure, it was becoming apparent that new insurance products and the changing marketplace had already made the '76 Model Cost Disclosure Regulation somewhat obsolete. The

NAIC's own study recognized that the 1976 Model was "outmoded" and so it initiated proceedings in 1980 to revise the Model again.

It was during this period that we began to question the need or value of any mandated disclosure system. With the dynamics of a free marketplace operating continually to develop new products to meet consumer demand, any disclosure system geared to a certain type or generation of life insurance products will obviously be outdated as soon as the products themselves change. During the period of NALC's deliberations to update the 1976 Model Regulation, it became abundantly clear that no system of disclosure was without its faults and that each one proposed grew so increasingly complex so as to defeat its purpose of educating the life insurance purchaser. It also became apparent that the mandated disclosure could even be used to distort and misrepresent life insurance products. Therefore, rather than joining the fray to try to devise the ideal disclosure system of the moment, we feel that now is the time to pause to ask some fundamental questions:

1. Is there really a need for governmental interference in the area of life insurance sales through a mandated disclosure system?
2. What are the costs involved in any mandated disclosure system?
3. Does a mandated disclosure system discriminate against small companies and small policyholders?

The purpose of my testimony is to address these questions and ask your subcommittee to do the same.

As to the need for mandated disclosure, it is our position that there is no such perceived general need on the part of the public and that there is already more than adequate information available to those purchasers who wish to compare products and prices. Shortly after the FTC released its Report in 1979, the NALC filed a request under the Freedom of Information Act requesting all of the so-called "complaints" received by the FTC from insurance consumers that supposedly precipitated the study. When the FTC finally complied with the request, it produced a total of only 208 life insurance consumer communications. Only 68 related to cost disclosure and 39 of those arose as a result of the publicity concerning the FTC Report, 22 of those being favorable to the FTC investigation and 17 being critical. Thus only 29 communications from the public regarding cost disclosure had been received prior to the staff report publicity; however, all 208 communications were classified by the FTC as complaints against the insurance industry. No creditable study that we know of has concluded that the general life insurance buying public is ill informed. To the contrary, the January 1984 study conducted by Dr. Lawrence A. Crosby of Arizona State University, which was referred to in your hearings last month, concluded that consumers, for the most part, are satisfied with their life insurance. A similar study on home service insurance in Florida conducted in 1980 by Dr. Robert Ladner of the Behavioral Science Research Corporation found that 90% said that their agents had explained satisfactorily to them the policy and benefits coverage.

Life insurance is a very competitive business, and there is more detailed information available as to cost and coverage on a comparative basis than you can find on just about any product on the market. The responsible media increasingly is recognizing this, as can be illustrated by this article which appeared in the June 4, 1984 U.S. News & World Report entitled "Better Bargains Today in Life Insurance." We feel that this article does a better job of describing the basics of how to shop for life insurance than the materials mandated by present or proposed requirements. As early as 1980, Consumer Reports published a two-part special report on purchasing life insurance. Other publications provide detailed information on a comparative basis on various insurance products. For example, just last month, a comparative analysis of the universal life policies of 200 life insurance companies was published by the A. M. Best Company. This gives information on initial expense charges such as policy fees and premium load, renewal expenses, premium charges, guaranteed interest rate, current interest rate, policy loan rate and surrender charges. Other Best's comparisons are available on participating whole life policies and 20-year dividend comparisons. The National Underwriter publishes annually a Life Rates and Data on adjustable premium plan policies and an Interest-Adjusted Index giving specialized policy comparison information covering contracts of over 300 life insurance companies. (Copies of reprints of some of these publications will be available to be passed out). (Materials on file with the Subcommittee.)

This is information provided by our free-enterprise system - available to those buyers and sellers alike who want it. To mandate that

an agent must in addition furnish certain comparative information to a prospective buyer is an affront to human nature and a negation of our free-enterprise system. In what other industry is a salesman of a product or service under an obligation to describe the costs of competing products or services to prospective buyers?

As to the <u>costs</u> involved in any mandated disclosure system, it is our position that they far outweigh any of the alleged benefits. The Federal government has set the precedent of requiring that a regulatory analysis, including a cost impact study, be made of any proposed regulation before it is adopted. Our review of the projected costs and impact of compliance involved in the 1980 NAIC Model proposal would severely impact and even threaten the solvency of many smaller companies. One NALC member company with a premium income of $4 million writing about 4,000 new policies each year did a break-down of the increased costs and concluded the added compliance cost for the first year would be $124,500, or the approximate amount of its entire previous year's statutory gain. Just last month, another member formally notified the Commissioner of Colorado that to comply with Colorado's new cost disclosure regulation would cost over $95,000 or almost three times its previous year's statutory gain and would amount to an average increase in cost per policy of $63.77. As a result, the company has notified its agents and policyholders that it will cease all sales operations in the state effective July 1, 1984. The company in question writes only small burial-type life insurance policies with less than a $10,000 face amount. Do its policyholders need, or want, or could

they even understand what added benefits mandated cost disclosures would give them? Costs of mandated disclosures will obviously be less per policy as the size of a company increases. Thus we have a situation where the economies of scale alone allow a large company to spread the added costs over a larger base and thus gain a competitive cost edge over smaller companies.

In a recent statistical analysis commissioned by the NALC, the financial statements of 1,491 U.S. life insurance companies were analyzed. Of these, 1,351 or 90.6% would be considered as small companies under the pending new Life Insurance Tax Act, but collectively they hold only 12.5% of the assets of the life insurance industry. The other 87.5% of the assets are held by only 140 large life insurers. These are the companies that can grind out computerized costs disclosures to satisfy any mandated method at a cost per policy significantly less than the smaller companies, especially those small companies selling small basic life protection and burial-type plans.

As to the answer to our three questions, we trust that we have illustrated to you today:

1. That there is no need for governmental interference in the area of life insurance sales through a mandated disclosure system.
2. That the costs involved in any mandated disclosure system far outweigh any alleged benefits.
3. That a mandated disclosure system discriminates against small companies and small policyholders.

Thank you for giving me the opportunity to testify on behalf of the smaller life insurance companies and the small life insurance policyholders.

Mr. FEIGHAN. Thank you Mr. Perry. I am a little concerned about the direction of your testimony and its criticism of mandating cost disclosure by arguing that there's no other industry where it would be mandated that the costs of a competitor's product be delivered to a potential customer.

But I don't understand where anyone is recommending that an insurance company would be required to deliver to a potential customer the costs of a competitor of that agency or that insurer.

Mr. MINCK. May I respond, sir?

Mr. FEIGHAN. If you would. If you'd begin by introducing yourself, please.

Mr. MINCK. American Council of Life Insurance.

Mr. FEIGHAN. Your name, again?

Mr. MINCK. Richard Minck, executive vice president of the American Council of Life Insurance.

I think that the basic information about your own contract, that is, such information as the premiums charged for the contract, the death benefits, cash values, other benefits, is certainly given now to every customer. There's no debate about that.

What commissioner, or Professor Denenberg, was talking about earlier this morning, was I think, requiring that everybody deliver to the prospective customer a complete listing of other people's costs and contracts.

I think that's the area of discussion which this response was addressed to.

Mr. FEIGHAN. But separating that then, obviously I would agree that that would be very burdensome to have to carry that material. An individual agent certainly would not have any way of being able to verify the accuracy of that information and that clearly would be costly.

But separating that, the information of your own coverage and the cost disclosure of your own product certainly could not result in substantial cost.

What is the additional cost in giving information regarding an agent's commission, for example? That's a fairly negligible calculation in terms of its cost.

That kind of information, I would think, could very easily be provided.

Mr. MINCK. Again, I think the cost disclosure systems that have been considered by the NAIC, and by other groups, are generated by the calculation of cost indexes. And the purposes for which cost indexes are calculated is to permit ready comparison of one contract with another.

The basic information about the policy, that is the premium actually charged, the benefits actually available, and perhaps illustrations of dividends if the contract is sold on a participating basis, those things are all available, they are all given to the policyholders; it's not part of the cost problem.

It's the additional stuff because of a mandated system of disclosure that generates the cost. The costs are due to setting up computer systems, training agents to use them and to explain these indexes and related matters.

Mr. FEIGHAN. If we were using instead a rate of return calculation, wouldn't that be a fairly simple one to compute and some-

thing that would be fairly easy to provide to the customer? In fact, it would be much more valuable to the customer than the information he is currently receiving.

Mr. MINCK. A short answer to both questions, I believe is no, but Mr. Hunstad is an expert on the subject and——

Mr. HUNSTAD. Let me respond to that, if I may, Mr. Chairman. I think there are several aspects involved in your question and let me state very simply that the calculation of a rate of return is a complex process.

It is far more difficult and more time consuming to develop than is the calculation of the cost indexes now called for in the current National Association of Insurance Commissioners' models.

Mr. FEIGHAN. I appreciate—if you don't mind me interjecting at this point—I appreciate in your testimony where you've made reference to some of the factors that might make that rate of return information less than beneficial for comparative purposes to a potential customer.

But I would think that most of those items could be footnoted in the rate of return information, so that the customer does have a piece of information in terms of rate of return that can be used for comparison purposes in evaluating other kinds of investment.

Mr. HUNSTAD. Well, Mr. Chairman, there are so many questions that you've asked, let me try and sort through some and see if I can answer them one at a time.

I think one of the questions is what are we trying to compare? Are we trying to compare the cost of life insurance policy A with life insurance policy B? If that's the case, then we can evaluate the rate of return approach versus the cost indexes provided for in the current NAIC system.

On doing so, we find that there are no fundamental differences between the two systems. That if you look at the ranking of costs from low cost to high cost, under the current NAIC method and you substitute a rate of return calculation instead, the rankings are very similar if not identical. And the reason they are is that the fundamentals are the same.

If we move beyond that to compare life insurance rates of return with other investments—Mr. Denenberg said earlier this morning that life insurance is an investment. I have to disagree. Life insurance may have some investment characteristics, but it's not an investment.

If we want to determine what's the best way of saving a sum of money to put a child through college, with no insurance needs, then an insurance product that provides for death benefits in addition to that savings accumulation is going to be, by definition, a less efficient product.

Mr. FEIGHAN. Well, if insurance is viewed as an investment by the majority of Americans, that's the result of its portrayal over several decades by the industry.

Mr. HUNSTAD. I can't respond to that.

Mr. PERRY. The small companies, Mr. Chairman, supported the NAIC disclosure model bill that is now in effect. They felt then and now that that bill was a bill that they wanted to support.

The companies, however, that are small don't see life insurance as an investment. These people are buying small policies that a

number of people refer to as burial policies. You mentioned earlier about an article that appeared in Business Week, on June 25. I'd like to read to you what Business Week had to say:

> Comparing the cost and benefits of one company's policies with those of another has always been a near impossible task, often driving people to throw up their hands and go for the lowest premium. Don't succumb. Premiums tell only part of the story and the whole story is well worth understanding.
>
> If you are mathematically inclined, there are formulas to help you calculate the best deal. But there is no one universally accepted method for comparing costs.

The fact is that in 1976 the NAIC model bill was introduced and adopted, and by 1980 it was necessary to come forth with a new bill. It's the small companies' feeling and thinking that they should be exempt from this cost disclosure.

Mr. FEIGHAN. I fail to understand though what is so burdensome about calculating and providing rate of return information. And it does go to the question of how we view life insurance, how we view insurance generally. Is it an investment? Clearly if it did not have investment characteristics, you would not be marketing whole life. You would be focusing exclusively on term.

Mr. MINCK. I think the reason that we're marketing whole life, sir, is that people want life insurance protection for a period of longer than to, say, age 60 or 65.

The premium costs for term insurance, once you hit age 65 or 70, become prohibitive. In fact the State of New York has long prohibited such sales, and what you have when you buy a whole life contract is a contract that will provide protection and death benefit until you die, even if that's age 90, with a level premium. I think that's the reason we're selling the contract.

Mr. FEIGHAN. Well, I understand that. But I also think that most prospective buyers of insurance would like information that would make it helpful for them to make a comparison between whole life and term insurance and the advantage then of individual investment of the balance. Then the customer should be able to compare that selection with any of the new kinds of policies that are available or with other forms of investment.

I mean, that's a fact of the marketplace today. That is how the typical American purchaser of life insurance views that kind of decision.

Mr. MINCK. I think again one reason that we have problems with this index is that it doesn't produce an answer for term insurance, which is more than half of our business. I mean, we have no——

Mr. FEIGHAN. Well, I understand that. And I think that that's the kind of clarity that we would like to make sure that consumers are dealing with.

Mr. MINCK. Right. The second thing is that if you calculate a rate of return index, the answer that you get will depend upon the assumptions that you've built into it.

For the same block of policies you can produce rates of return indexes that range from, say, 2 percent to 12 percent.

What you have as a result of that index, it tells you more about the assumptions you made than about what the company has put into its pricing. Or the interest rates, say, the company's actually using in calculating either dividends, premiums, or other benefits.

It's the sort of thing that would be attractive if, in fact, there were a unique answer as to a rate of return. But there isn't such a thing.

And in fact the witnesses that have appeared that have talked to you about rates of return are talking to you about what turn out to be two or three or four different rates of return and different calculations.

There's no agreement among people who think a rate of return would be a good thing to have as to what it is.

Mr. FEIGHAN. Well, I think that that could be fairly standardized.

Pardon me, Mr. Hunstad, let me ask this question. I read earlier the statement of Mr. Carter from Equitable. Is he on point? Does it concern you, that the new options available in the insurance industry today may, in fact, be driving us predictably to Federal regulation? Is this an option that perhaps none of us would welcome, but would find necessary in order to be relieved from the burdensome process of dealing with 50 different regulatory agencies, in fact, multiple regulatory agencies, because of the varying characteristics of new products?

Mr. HUNSTAD. I'm sure he reflects the concern that a company such as his that operates in all States faces in that situation. We're in much the same kind of situation, operating in several States.

We, however, don't see any compelling reason that State regulation of insurance would be abandoned if we were to add a Federal regulatory process on top. We suspect that would be more regulation than we'd be subject to today.

I think there may well be—I'll let Mr. Perry speak for himself—companies that don't operate nationwide may have a distinctly different feeling about Federal versus State regulation.

Mr. PERRY. I would yield to Roy Woodall, who is the executive vice president of NALC.

Mr. WOODALL. I think the reference has been made that a lot of our member companies may be licensed in two or three States. There's an old joke about 50 monkeys or 1 gorilla, which is worse?

And sir, to your one question on the cost of compliance, we furnished the studies the two companies mentioned in Mr. Perry's statement made on how much it would cost them to comply with a mandated procedure to the staff this morning and have extra copies of those. These are companies that are selling a small number of policies, and when you add the startup costs to comply with any mandated procedure, especially some of the ones that we've been discussing here, you add substantially to the cost—in one case as much as $63 on a one-time load to a policy. And that would put that company completely out of business. In fact that company has given notice to the State of Colorado it was disbanding its business, and it was a Colorado company.

Mr. FEIGHAN. Well, I would welcome the opportunity to look at that information. Thanks very much.

[Materials in appendix 4; at p. 655]

Mr. FEIGHAN. Mr. Hyde.

Mr. HYDE. Thank you, Mr. Chairman. I too appreciate the time and effort spent by our witnesses. It's been most instructive. I just parenthetically take note of the fact that there was some benign

complaint by the chairman and our previous witness, Mr. Denenberg, that the media wasn't covering this important testimony. And I note there was a television camera in the room while Mr. Denenberg testified, that may have—as soon as these distinguished gentlemen representing the industry assumed the witness chair, the camera has dissolved somewhere and is off pursuing other more newsworthy occurrences, so——

Mr. FEIGHAN. I was so self-centered, I thought it occurred when I assumed the chair. [Laughter.]

Mr. HYDE. I rather suspect that was a factor. [Laughter.]

But other than that I have no questions, and I thank you.

Mr. FEIGHAN. I'd like to thank the panelists very much. Your testimony has been very helpful.

We're pleased now to welcome representatives of the National Association of Insurance Commissioners.

Mr. James Corcoran will be the lead witness. He is the Superintendent of Insurance for the State of New York and he will be accompanied by Mr. Bruce Foudree, the Insurance Commissioner of the State of Iowa, and Mr. Lyndon Olson, Chairman of the State Board of Insurance in Austin, TX.

Mr. Foudree, I understand that you would like to begin with some comments and an introduction of Mr. Corcoran. Then, if we have some time, we will begin with the opening comments of Mr. Corcoran.

We have just received notice that we have a rollcall pending. We will recess when we hear the second bell. That will provide you approximately 5 minutes before our recess.

Mr. Foudree.

TESTIMONY OF JAMES P. CORCORAN, SUPERINTENDENT OF INSURANCE, STATE OF NEW YORK; BRUCE FOUDREE, INSURANCE COMMISSIONER, STATE OF IOWA; AND LYNDON OLSON, CHAIRMAN, TEXAS INSURANCE BOARD; ALL REPRESENTING THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Mr. FOUDREE. Good morning, Mr. Chairman, members of the subcommittee.

I have with me here this morning Superintendent James Corcoran from the State of New York and Commissioner Lyndon Olson, Chairman of the Texas Insurance Board. Also with me are my deputy commissioner for Market Conduct and Consumer Affairs Division of the Iowa Insurance Department, and my chief examiner. Also present in the audience here today are Commissioner Josephine Driscoll from Oregon, Commissioner Roger Day from Utah, and Commissioner Ed Muhl from Maryland.

No doubt many of those appearing before you and claiming to represent consumers are well intentioned, but too much of what has been said by them does not reflect reality. And there are those publicity-seeking groups who do not know, or who do not care to know, what is going on in the marketplace. These people are operating under the misconception that if you put more and more facts and figures on paper, the public will somehow be better off and competition will flourish.

The public is "informationed" to death. The market is already fiercely competitive. Consumers do not want more literature. They want someone they can talk to and ask questions about their insurance needs and their particular insurance complaint. That is what agents and what State insurance departments provide today.

Consumer groups attacking the McCarran-Ferguson Act are playing into the hands of some very large insurers who apparently would like to see Federal regulation. I mean those companies who criticize State regulation the loudest. See, for example, the recent remarks by the president of Equitable Life Assurance Society of the United States in the recent Business Week article that's been referred to earlier.

This subcommittee should ask itself, what is their motivation? Is it that they would prefer that the States not look at the financial condition of the holding companies and affiliated insurers and not disclose examination reports to the public something that the Federal Government does not require of banks? Is it that they seek to use their vast financial and personnel resources to increase their market share by driving out other and smaller companies, thereby dramatically reducing competition?

Federal regulation would mean little or no personal direct contact between individual consumers and Government regulators, elimination of State-by-State review of products and companies for suitabilities, cost, more cost and bureaucracy in the Federal Government and less competition.

Today, we are submitting statements by three States—Florida,[1] Iowa, and New York—as examples of how States provide information to the public. We would be glad to provide further information to the subcommittee if this would be helpful.

I would like at this time to introduce Superintendent Corcoran who is here to comment in response to questions from the chairman about how state insurance regulators protect and help consumers. Thank you.

[The statement of Mr. Foudree follows. The attachments referred to in his statement are on file with the subcommittee.]

[1] Submission from Florida in appendix—at p.—.

Statement of the
National Association of Insurance Commissioners

Submitted to the
Subcommittee on Monopolies and Commercial Law
U.S. House Committee on the Judiciary

by
Bruce W. Foudree
Insurance Commissioner of the State of Iowa

and
Vice-President of the NAIC

June 28, 1984

Insurance departments provide a number of services and engage in many regulatory activities which enhance the consumers' ability to make insurance decisions and which help them with problems they encounter with insurance companies and agents. These include complaint handling procedures, speeches, public service announcements, brochures, regulations specifically designed for consumer protection, rate and policy forms approval, company examinations and agent licensing. This statement of activities in Iowa is provided as an example of what states do.

Consumer Complaint Handling

Iowa employs attorneys who devote full time to handling consumer complaints and inquiries. During the past year, we have had approximately 30,000 phone calls, 1,000 walk-ins and 6,000 written complaints (each written complaint initiates a formal action by the Department). In 1983, the Department recovered over $2,200,000 for Iowa consumers. This year to date, we have recovered almost $1,600,000.

When consumers phone or come to the Department offices, one of the staff or attorneys spends time talking with them, trying to determine what the problem is and answering any questions the consumer may have. Our first concern is to determine if it is an emergency situation. If so, we attempt to resolve the problem immediately or, if it is clear this is not an insurance problem, we would route the consumers to

appropriate governmental agencies, such as Citizens Aid or the Department of Social Services.

If it is not an emergency situation, my staff interviews people to bring out the important aspects of their complaint so that they know how to write it up clearly for the insurance company's consideration. If a consumer only has a question, we try to answer it immediately or, if research is necessary, as soon as possible.

Once we have the complaint in writing, we send it to the insurance company for response with a cover letter asking for any information the company may have on the complaint including any supplementary documentation. Once the complaint response is received back in the Department, it becomes a case for an attorney. The attorney analyzes the complaint and the response and takes the appropriate action, which may include closing the file with the resolution of the dispute, mediating the dispute, either writing the company, the agent or the consumer for further information and forwarding it to the other party or perhaps bringing out some points that were overlooked in the company's initial review. At times, a fact question or legal question arises which the Department does not have the authority to determine. In these cases, we explain the problem to consumers and suggest they seek the services of a private attorney if they feel the situation warrants further action. Of course, when the company was right in the first instance, we explain it to the consumer as best we can.

Complaints are recorded on our computers. Statistics are maintained on different aspects of the complaints. These are by: company; agent; status of complainant (whether the complainant is the insured, the beneficiary or a third party); who the complaint is against; the type of coverage; the reason for the complaint (major reasons include underwriting problems, marketing and sales, claim handling and policyholder service); and disposition.

(A copy of the form we use for recording the data as well as the optional complaint forms we have for consumers to complete is attached. Also, attached is a recent printout of our complaint statistics.)

My Department does not prepare ratios of complaints to premiums or policies in force. This is because we feel there is no fair way to do it. We recognize there are different lines of business, types of coverage and types of consumers. We do keep records of absolute numbers of complaints.

All states provide service to their citizens who have complaints against insurers.

Public Presentations

My staff and I make at least 100 presentations per year in front of various consumer groups, e.g., Alzheimer Support Group, I Can Cope (cancer patients), Lions Club, Rotary, American Association of Retired Persons, etc. We perform this service free of charge, upon request, if there is a staff person knowledgeable on the particular area available at the time. Our presentations are generally directed toward informing the consumers of issues they should be aware of, problems the Department has seen recently, and a question and answer period. Most states provide this service for consumer groups.

I have also done a number of public service announcements that are aired by the various radio and television stations in Iowa. Recently, I have prepared public service announcements on our new replacement regulation for life insurance and annuities, Medicare supplemental coverage, group conversions of life, accident and health insurance, automobile insurance and, a 60 second announcement on cancer insurance.

(Attached is a copy of a few of these public service announcements.)

When an issue becomes controversial in the area of insurance, I try to do a public service announcement on it so that we can get the broadest dissemination of the necessary information to the buying public. This seems to be working fairly well for us in Iowa. Other states prepare public service announcements to some degree or other as well.

Rate Approval

Property and casualty rates are controlled by statute, which is common from state to state. Those rates are a matter of public record and can be reviewed by a consumer in our offices during regular business hours. The statutory standard that is used for property/casualty rates is that they must be adequate but not excessive and not unfairly discriminatory. On the life, accident and health side, the rates are not controlled by statute although sometimes the Department gets informational filings, which, of course, would be available to consumers. Credit insurance, such as credit life and disability, is controlled by statute, and therefore those rates are really very standardized.

Quite often during the year, we get inquiries about insurance rates and the specific types of coverage. The Department provides assistance to all consumers who seek rate information, be it specific or general, for a type of insurance. My staff in the policy approval division provides individual counseling to consumers on rates. While we do not recommend specific companies, we do give out factual information so the consumer can make an informed choice regarding the rates. Inherent in the nature of rates is that no company has the best rates all the time. Rates vary by classification, e.g. age, driving record, health condition, limits of liability, etc. As a special service to consumers, the Department has the rates for a number of the larger companies doing business in Iowa that sell auto and homeowners insurance, which are set out for the various areas in the state and under certain set conditions. This enables a consumer to check the rates of their own insurance company with those of the larger insurance companies based on a standard classification. This service and method of rate regulation are common among states but is not universal.

Policy Form Approval

Every policy sold in Iowa must have a prototype approved by our Department, which is on file and available for consumers to come in and compare, if they so desire. Additionally, our attorneys will counsel consumers on specific questions, especially in the property/casualty area where the policies are very standardized. Our attorneys talk freely about what the policy covers.

Life, accident and health policies are more variable but they do conform to basic requirements such as the standard non-forfeiture and valuation laws which define minimum standards for reserves for life and annuity contracts and minimum cash values and nonforfeiture benefits. Health policies must conform to minimum standards for individual accident and health insurance. We discuss these with consumers too.

Consumer Pamphlets

Iowa is a small enough state that we can easily handle inquiries on an individual basis. Therefore the Department has a limited number of consumer brochures available to the public but that is also because the Iowa experience is that the bulk of our inquiries are problem-related, mostly claims, but also sometimes the agent's conduct is questioned. In those cases, the pamphlet would not be of much use. However, a number of states do produce brochures and have had very good luck with them.

(Attached are some brochures to show a sampling of what is available in the various states to consumers. Addendum 2 lists these by title.)

Regulations

Iowa has several regulations that have been promulgated in response to specific consumer concerns. These regulations are based on model NAIC language, with specific state adaptations.

These regulations include the life insurance solicitation regulation, which has a requirement that each purchaser of life insurance be given a buyers guide. The regulation also specifically details what is to be included in that buyers guide.

(Attached is a copy of the pamphlet as put out by the NAIC.)

A second regulation is the Medicare Supplemental Insurance Regulation. This requires insurers issuing Medicare supplement policies to provide the policyholder with a buyers guide entitled "Guide to health insurance for people with Medicare" which has been developed jointly by the NAIC and the U.S. Department of Health and Human Services.

(Attached is a copy of that pamphlet.)

The Department has also recently adopted the Life Insurance and Annuity Replacement Regulation. This requires a notice to be given to consumers at the time a replacement is proposed. The notice informs consumers that replacement may or may not be in their best interest and that they should look at both sides before purchasing the new policy. Also, the replacing insurance company is responsible for notifying the replaced insurance company of the replacement so that the company may attempt to re-explain the policy, if it so chooses.

(Attached is a copy of that regulation.)

We also have a series of regulations applicable to specific Iowa problems. Most states have adopted these and similar regulations to help consumers with the various

problems that they encounter when attempting to purchase insurance.

Examinations

Roughly half of my staff is composed of financial examiners, whose responsibility includes licensing and examining insurance companies for compliance with the various laws in Iowa. We are required to perform an examination at least once every three years but the Department does have a right to examine companies as needed. As a part of every examination, in addition to the financial solvency area, there is the market conduct aspect which reviews the interaction of the company and the consumer in the marketplace, including sales, policyholder service and claims. During that aspect of the examination, our examiners review consumer complaints, which the companies are required by regulation to keep. These include any consumer complaints received by the company, whether or not the consumer also complained to the Department. As part of the exam report, our examiners may include a sampling of claimants, and always included is a review of claims filed. That review includes measuring company response time and amount of payment, fairness, and the service the company gave the consumer.

In addition to the examinations, that division also answers questions about which companies are licensed and exactly what that means in Iowa. Information requests are also taken on company status, which would include an analysis of their financial status and a reference to Best's Review, upon request. As a service to all Iowa citizens, this division annually prepares a list of all companies that are licensed in Iowa and also a list of all Iowa domestic companies with the officers' names and the home office mailing addresses of those companies.

(Attached are the current lists.)

Another service that the examinations division provides for consumers is that of researching the historical background of a company for name changes, mergers, or acquisitions that have taken place in the past and that a consumer may not yet be aware of. Upon request, we will review both our history book and old volumes of Best's Review to research the current name and location of a company that a consumer may feel he has a policy with. For example, a consumer may have a life insurance policy with the XYZ company that was issued in 1940 and became paid up in 1960. However, he cannot locate XYZ company. The consumer calls the Department and we check to see if that is the current name of the company and, if not, we will check to determine the new name and address of the company, and whether the change was because of a merger or merely a name change by the company at some past date.

An annual statement, which is required of each company each year, is filed and reviewed by this division annually. The statement shows the gross premiums, gross claims by line of insurance, assets, expenses, complaints, etc. These statements and examination reports are a matter of public record and a consumer is free to come in and study them. Our examiners review them to be sure that a company is maintaining the required level of financial solvency and is paying claims in a timely manner.

(Attached are copies of the different types of statements.)

Based on the annual statements, the Department prepares a public annual report containing statistics for the past calendar year which detail the financial condition of all insurance companies licensed to do business in Iowa. This report is quite lengthy and documents a great deal of statistical information about premiums collected, claims paid, assets, liabilities and surplus of companies.

(Attached is the 1983 report.)

Agents Licensing

Annually the Department issues approximately 33,000 licenses for insurance agents to do business in Iowa. This includes added lines for an agent and duplicate licenses as well as new licenses. We currently have 25,700 active licensed agents, both resident and nonresident. To become licensed, we require the agent to pass an examination for each line of insurance he wishes to sell. The applicant must also submit to a review of his character and competency by the Department.

(Attached are copies of the licensing applications.)

Subsequent to an agent's licensure, the Department monitors his performance through the complaints that we receive from consumers about his actions. If it appears that there has been a pattern of practice of some behavior that is violative of the rules or statutes in Iowa, a notice of hearing will be drawn on the agent to begin disciplinary proceedings. In 1983, we entered approximately 85 orders against insurance agents, ranging from a simple cease and desist with a small fine to permanent revocation of the agent's license. In 1984 to date, 52 such orders have been entered. The Department feels this is a very important aspect of consumer information and protection, because we have a standard for agents to comply with and when they fail to do so, their license is affected. This permits the Department to sanction agents when consumers are not being treated lawfully.

The notice of hearing that begins the disciplinary proceeding and the order or consent to order that ends it, are matters of public record which can be accessed by the consuming public as well as the insurance companies that appoint these agents. This gives a consumer a chance to get an idea about whether or not an agent has a "clean record".

(Attached are copies of a sample notice and order.)

All states have some sort of licensing mechanism for insurance agents and some method of disciplining them. A number of states also license insurance brokers and counselors and other types of insurance professionals. This is just an additional check on the marketplace and those who are permitted to practice there.

Conclusion

We feel that the steps that we take to inform consumers and also to help them with any problems they have with companies and agents go a long way in making consumers feel they have a choice, that there is an alternative and that information can be received without having to rely on someone with a vested interest in such information. The states will continue to act in the best interests of insurance consumers in order to assure their protection and their ability to make informed decisions.

Thank you again for letting me present this information to the Subcommittee.

ADDENDUM 1

1. NAIC sheet
2. Consumer complaint form -- property/casualty
3. Consumer complaint form -- life/accident and health
4. Computer printout off NAIC sheet
5. Public Service Announcements:

   Cancer (60-second)
   Auto (30-second)
   Medicare Supplement (10-second)

6. Life Insurance Buyer's Guide -- pamphlet
7. Guide to Health Insurance for People with Medicare -- pamphlet
8. Replacement Regulation
9. List of Iowa insurance companies -- with officers' names and home office addresses
10. List of all admitted companies in Iowa
11. Convention statement(s)
12. Annual report to the Governor
13. Resident agent application
14. Nonresident agent application
15. Sample Notice of Hearing
16. Sample Order
17. Continuing Education Providers List -- this is available to agents upon request. The list contains all courses approved for CE credit that are still to be given, updated monthly.

ADDENDUM 2

AUTO INSURANCE

- Private passenger auto insurance - AL
- Consumer's shopping guide - AR
- Shopping for auto insurance - CT
- Auto insurance price comparison guide - CT
- A Colorado buyer's guide to auto insurance
- Compulsory/No-fault Motor Vehicle Insurance Act of 1982 - D.C. (Spanish and English)
- Florida consumer's guide to auto insurance
- No-fault insurance - Hawaii
- Buyer'g guide to auto insurance - IL
- Are you confused by your auto insurance? - IN
- Kansas auto insurance facts to help you
- Do not buy insurance for your auto until you read this - KY
- Auto insurance premium comparison report - ME
- Missouri consumer's guide to auto insurance
- Written notice/buyer's guide and coverage selection form - NJ
- What older Ohioans should know about auto insurance
- Pennsylvania consumer's guide to no-fault auto insurance rates
- South Carolina auto insurance guide
- Consumer's guide to auto insurance - WA
- Consumer's guide to auto insurance - WV
- Buyer's guide to auto insurance - WI

HEALTH INSURANCE

- Buyer's guide to Medicare Supplement for insurance for Californians
- A Colorado buyer's guide to health insurance
- Florida consumer's guide to health insurance - FL
- Women and health insurance -- your rights as a Florida consumer - FL
- Medicare supplement insurance shopper's guide - FL
- Understanding your health insurance - IN
- Health insurance facts to help senior citizens - KS
- Food & nutrition for health in later years - KS
- Health insurance facts to help you - KS
- Kentucky guide to health insurance
- Medicare supplement insurance guidelines - MN
- Insurance fraud advice for older Missourians
- Adding to Medicare - NJ

- Health insurance and the senior citizen - NB
- What older Ohioans should know about health and accident insurance
- Virginia health insurance consumer's guide
- Consumer's guide to health protection - WA
- 1984 Health insurance guide for senior citizens - WA
- Senior health insurance benefit advisors - WA
- State of Wisconsin health insurance risk sharing plan outline
- Fact sheet on mandated benefits in health insurance policies
- Buyer's guide to health and disability income insurance - WI
- Health insurance advice for senior citizens - WI
- Fact sheet on insurance terminations, denials, and cancellations - WI
- Information sheet on cancer insurance
- Guide to health insurance for people with Medicare
- Your Medicare recordkeeper - Dep't Health & Human Services

LIFE INSURANCE

- A Colorado buyer's guide to life insurance
- Florida consumer's guide to life insurance an annuities
- Buyer's guide to life insurance - IL
- Life insurance facts to help you - IN
- Buying premium financed life insurance - IN
- Life insurance facts to help you - KS
- Kentucky guide to life insurance
- Consumer's guide to life insurance in Michigan
- What older Ohioans should know about life insurance
- A buyer's guide to life and health insurance for senior citizens - TN
- Consumer's guide to life insurance - WA
- State life insurance fund - WI
- A consumer's guide to life insurance

HOMEOWNERS INSURANCE

- Alaska 1983 homeowner's insurance
- Homeowner's insurance guide - AZ
- A Colorado buyer's guide to homeowner's insurance
- Homeowner's premium comparison - CO
- Florida consumer's guide to homewoner's insurance
- Consumer's shopping guide for homeowner's insurance - Hawaii
- Buyer's guide to homeowner's insurance facts to help you
- Consumer report homeowner's insurance - KY
- Homeowner's insurance premium comparison report - ME

- Homeowner's insurance your right to protection - MN
- Missouri consumer's guide to homeowner's and renter's insurance
- Missouri consumer's guide to mobil home insurance
- A shopper's guide to homeowner's insurance - NJ
- Consumer's shopping guide for homeowner's insurance - NY
- What older Ohioans should know about homeowner's insurance
- Pennsylvania consumer's guide to homeowner's insurance
- Consumer's guide to homeowner's insurance - WA
- West Virginia consumer's guide to homeowner's insurance
- Buyer's guide to homeowner's insurance - WI
- Disaster preparedness - questions and answers - WI
- A brief guide to tenant's insurance - WI
- Home insurance basics -- Insurance Formation Institute

FLOOD INSURANCE

- Flood insurance facts to help you - KS
- After the flood -- handbook on salvage and insurance - PA
- Buyer's guide to flood insurance - WI
- Questions and answers on the National Flood Insurance Program

MISCELLANEOUS INSURANCE

- Insurance guide for women - WI
- Fact sheet on mandated benefits for the treatment of alcoholism, drug abuse, and mental and nervous disorders - WI
- Wisconsin buyer's guide to annuities
- What is arson - WV
- Your insurance rights explained - WA
- Serving the peopole - NC
- Insurance facts for Nebraskans
- Do you have an insurance problem? - IN
- Credit insurance information - IN
- Insurance in Florida
- Your right to know - CT
- Insurance information for Californians
- Insurance rating problems - CA
- Straight talk about insurance - MD
- May we help you - AZ
- Press release - commissioner of insurance - WV
- Insuring the small business - MI
- Insurance consumer alerts - MI
- 1982 Annual Statistical Report - MI

1984 GOV Competition in the Insurance Industry 739p bonknote.pdf

42-049 O—85——11

Mr. CORCORAN. Good morning, Congressman.

Before I start the paraphrasing of the written statement, I'd like to provide to you the nonexistent cost disclosure material that New York provides. A quick summary of them. Very heavy and weighty. One is a Medicare supplement insurance guide—I'll provide them to the counsels—shopping guide for life insurance which is dated 1982 and we are updating again this year, consumer shopping guide for automobile insurance, shopping guide for homeowners insurance, and a consumer shopping guide for life insurance. That's a conceptual breakdown.

[Material on file with subcommittee.]

Mr. CORCORAN. Now, all these materials are being updated now by my department. It's a substantial piece of work no doubt, but they are available to the public.

Mr. FEIGHAN. Mr. Corcoran, before you leave that point, can you tell us what the method and extent of distribution is of that information?

Mr. CORCORAN. Yes; we require the companies to notify prospective purchasers. They can write to the department and get any copies of this any time they want. We have consumer outreach programs around the State. I go around the State with my staff. We publish it in the local newspapers. We tell them to come in. We have the guides there and they can ask questions. We are also right now forming a telephone system where you can call an 800 number to my department prior to entering into any insurance transaction and we'll give you some basic fundamental questions to ask the agent or the company.

So we really think in that situation it's kind of a preventive medicine. So the guides are available. They are very difficult to update and you must—first, I always stress with the consumer when they talk to me, yes, the premium is important, but in this day and age service, the solvency of the company, your own financial needs are important, too.

So, premium really should not be the one criteria but we want to make sure they do have that material and we in New York have made a substantial effort to get that. We are updating these guides every other year. It's very expensive to do it but we do do it. We made sure the public has access to it.

Mr. FEIGHAN. We'll hear more of your testimony after we recess for a period of 15 minutes. Thanks very much.

[Recess.]

Mr. FEIGHAN. Ladies and gentlemen, we'll reconvene the hearing.

Mr. Corcoran, if you would like to continue with your commentary.

Mr. CORCORAN. Well, these materials which are allegedly nonexistent are really the result of the efforts of the NAIC of the last, I guess, 10 or 15 years subsequent to Mr. Denenberg's being a commissioner.

Things have changed drastically and I think it's an important note that we stress with the Congress that there has been a tremendous change in the attitudes of the commissioners and the cost disclosure that has been going on, and in general the products that have been provided.

The competition has been a very effective tool and by having State regulation in the various jurisdictions not only does it, to a certain extent, isolate and insulate us from pure political considerations, it provides an experiment where certain States might allow certain products. We all get to see how it works and then open up the new fields.

That's very similar to the way that these new interest-sensitive products—universal life, variable life insurance—have developed and we now permit them in New York after watching many of the other States permitting it. So it's very important to see that State regulation to a certain extent has provided flexibility, and now with these new interest-sensitive products, to a certain extent cost disclosure is not as crucial as it used to be with the pure whole life products because these are purely investment mechanisms. The individual knows what the rate of return is. So you do have a new era of generic insurance products.

With that I'd like to glean through my testimony, which I'm sure you don't want me to read, which does note I'm here on behalf of the NAIC as superintendent of insurance and stressing that the staffs and the expertise of the State insurance departments of the last 100 years have now developed to meet all the new challenges that we face.

Although the list is not inclusive which we present to you about State regulation, I think the most important one is our ability to license. Without the ability to take and to give licenses, State regulation, even if we have a very strong consumer department which most of us do have, proportionally most of the departments have a high percentage of their staff on consumer complaints. If you don't have the ability to take and give licenses, without that leverage, you don't have the ability to make and settle complaints and offer and give good consumer service.

Also, we subject the companies to very comprehensive periodic examinations which include among other things a review of whether claims are paid on a fair and prompt basis and whether policyholder complaints are handled properly and fairly. I think it's even been stressed by Mr. Denenberg that the idea of calling Washington or having a Federal mechanism in the State handling complaints would not be as sensitive to the region and would not be as readily accountable to the various voters in the State, and would not be as productive.

Now, health policies must meet certain standards of benefits and the premiums must be reasonable in relation to the charges. We in New York have taken the position of minimum benefit ratios required for accident health policies. Congress now basically requires that for every dollar that was paid in premium we make sure that 70 to 80 percent benefits are received back. Our examination procedures are geared to make sure that requirement is complied with.

As I noted before, the complaint or consumer service bureau is typically one of the largest bureaus in any insurance department.

Now, in order to aid each other, the other commissioners, we—the NAIC, as you know, is made up of all 50 commissioners and the basic object, of course, is we represent the consumers. Now we want to make sure that the consumers are treated fairly and rea-

sonably and have sufficient information upon which to make a decision.

Now, the NAIC has sought to promote uniformity when appropriate, has developed model laws and regulations to address various issues and has conducted studies and research projects on insurance related problems. The NAIC, therefore, provides flexibility and a mechanism for discussion in improvement of the regulation of insurance.

It's very important that we realize that the insurance companies right now are going through a watershed period. There's a tremendous change in the product lines and there's a dynamic situation by having a flexible State regulatory environment which has enhanced that and made it possible. It provides a forum for consideration of the innovations each State presents for the development of model regulations, when appropriate.

Now, during it's 100-year history, the NAIC has developed a number of model laws and regulations designed to meet a nationwide pattern of activity and thus we adopted, when appropriate.

Whether local or universal, all are drafted with the protection of the insurance consuming public in mind, since either directly or indirectly all affect the public. Of particular interest to this committee today, of course, is model legislation regarding cost disclosure which has been adopted I believe in just about every State.

The NAIC has also developed regulations concerning misleading advertising. And, also, in New York, as I stressed before, we offer consumer guides to life insurance which contain cost comparison tables with sample prices on typical policies for all life insurers licensed in New York. But I'd like to stress at this time, though, that the whole life insurance product is not the product that I believe in the future will be purchased. It's more like universal life.

I think Mr. Carter in his presentation in Business Week noted that 47 percent of their new sales is universal life, interest-sensitive products.

In the area of accident/health products, there are models addressing the advertising of accident/health insurance, and requirements on outlining of the benefits provided in accident/health insurance policies. The NAIC has also developed regulations setting forth the minimum benefit requirements in these policies.

The NAIC has separate models requiring an outline of coverage and the setting forth of minimum benefits for Medicare supplemental insurance policies on which the Congress had held hearings a number of years ago.

We annually in New York produce a Medicare supplement insurance booklet, a consumer booklet providing comparative pricing information on policies that meet New York standards for covering the Medicare gaps. New York also publishes a consumer shopping guide for auto insurance and a consumer shopping guide for homeowners insurance with the comparison pricing of the 20 largest sellers of each type in the State.

Now, I would stress at this point, all of this activity has taken place between now and the time that Mr. Denenberg was commissioner.

Now, a widely enacted and utilized model providing broad consumer protection is the Model Act Relating to Unfair Methods of

Competition and Unfair and Deceptive Acts and Practices in the Insurance Business. Now this model prohibits such activities as misrepresentation and false advertising of insurance policies, entering into agreements to coerce, defamation by distributing false information about personal finances, unfair discrimination as in refusing of coverage for a person because of sex or marital status, and tie-in sales.

The NAIC has also developed model complaint reports maintained by the State insurance departments. Now, most of the States maintain complaint records and analyze these records as another regulatory tool and are constantly in contact with each other, which obviously will flag a problem company.

A trend in complaints in a particular line or by a particular company in a State may aid an insurance department to move quickly to identify a problem that might be developing in that State.

States address the needs of insurance consumers by means other than legislation by promulgating regulations. Most States issue brochures on various types of insurance, including automobile, homeowners and health, and several State departments, including my own now, are developing a hotline or toll free numbers to answer the questions of consumers.

Now, it's impossible in this time period to list all the State initiatives, statutory enactments, and administrative regulations designed to aid the insurance buying public. The NAIC has recognized and continues to recognize the value of competition in the insurance market. The NAIC is continuing to support the efforts to foster and preserve the competition in the markets.

We now see the competition forming new products and to a certain extent aiding the consumer directly in the fact that these interest-sensitive products in and of themselves would pay interest. Nevertheless, we continue to believe that information to consumers is a vital factor in competition. The NAIC also believes it is in the public's interest to retain a comprehensive oversight by the States of the insurance industry.

Now, the apparent intent with the antitrust laws is to promote competition. The NAIC believes that the State regulatory system has fostered that competition while protecting the interests of the insurance buying public. The insurance consuming public's best interest is served by retaining a comprehensive oversight by the States of the insurance industry. The State insurance departments are local and easily accessible to the insurance buying public.

The consumer can readily contact his or her insurance department to seek redress and to have questions answered and to apply pressure for action at the State level, thus enhancing accountability to the consumer. The State insurance departments can regulate local, regional, and nationwide insurers with equal ease and efficiency. Many of the problems faced by the insurance business are statewide or regional in nature and can be more readily understood and addressed at that level.

Where uniformity is needed, the NAIC has proven to be a valuable facility for cooperation, an impetus for action and a means to achieve uniformity in the appropriate situations. The regulatory network established by the States provides comprehensive oversight of the insurance industry.

Now, Congress has retained powers under McCarran-Ferguson, coupled with the States' initiatives to provide a regulatory environment which fosters competition while protecting our Nation's consumers and keeping them well informed.

Thank you very much.

[Statement of Mr. Corcoran follows:]

STATEMENT OF JAMES P. CORCORAN

SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK

Mr. Chairman and members of the Subcommittee. My name is Jim Corcoran. I appear before you as a representative of the National Association of Insurance Commissioners and as Superintendent of Insurance for the State of New York. The energies, expertise, and resources of the chief insurance regulators of the states and their staffs are directed toward protecting the interests of the insurance-consuming public. The consumer is the focal point of the state insurance regulatory system.

Monitoring financial solvency, licensing companies and agents, promulgating minimum benefit standards, requiring adequate disclosure, handling policyholder complaints, approving policy forms or rates, and disseminating information are state regulatory responsibilities which benefit the consumer. Although not all inclusive, the following are some of the responsibilities of state regulators in regulating the insurance industry:

1. Insurers and agents as well as claim adjustors in many states must obtain and retain licenses in order to do business. This, in turn, requires compliance with statutes

and regulations pertaining to formation, financial standards concerning assets, capital and surplus, permissible investments, adequacy of reserves, and qualifications as to the character of management, experience and knowledge of the business. Licensees may be fined and licenses may be suspended or revoked for failure to comply with the law or when the public interest so requires. Most fines, suspensions, and revocations originate with complaints from insurance consumers.

2. Insurers must file comprehensive annual and periodic reports under oath in each state in which they do business. Such reports permit state regulators to routinely track solvency, payout ratios, rates of return, and commissions to producers.
3. Insurers are subject to comprehensive periodic examinations which include, among other things, the financial condition of the company, a review of whether claims are paid on a fair and prompt basis and whether policyholder complaints are handled properly and fairly. The examinations permit in-depth analysis of payout ratios, rates of return and commissions, as well as a check on the periodic reports filed.
4. Statutory standards regarding policy content and, in some jurisdictions, requirements for policy form approval, serve

to preclude misrepresentation and other unfair practices that may be harmful to consumers.

5. State regulators implement the basic standards that rates shall not be excessive, inadequate or unfairly discriminatory, thus controlling pricing limits and practices of property liability insurers. Health policies must meet the standard that benefits be reasonble in relation to the premium charged. New York for example, has minimum benefits ratios required for accident and health policies.

6. Market practices are controlled, in part, by law governing the qualifications of agents and brokers in their licensing, prohibitions against certain practices such as false and misleading advertising and misrepresentation, control over policy forms, rate controls in some jurisdictions and establishing complaint system mechanisms. The Complaint or Consumer Services Bureau is typically one of the largest bureaus in any insurance department.

7. Various residual market mechanisms have been devised and implemented to assure the availability of insurance for certain types of insurance for less desirable risks. For example, automobile insurance assigned risk plans, FAIR Plans, medical malpractice and joint underwriting

associations. When the voluntary market mechanism fails to produce an insurer willing to undertake risks considered essential to consumers, residual markets are made available. Although developed by the individual states, residual markets represent a failure of the voluntary market and states strive to reduce the residual population as well as the need for such markets.

8. When all else fails the chief insurance regulator of a state may apply for a court order of rehabilitation, liquidation or conservation in an attempt to save the company and protect consumers from insurers unable to meet their future obligations. Although rehabilitation formerly meant virtual certainty of liquidation, the states have had notable successes in recent years in rehabilitating insurance companies to the benefit of all policyholders.

9. Among the sanctions available for enforcement of the insurance laws are criminal and civil penalties; cease and desist orders; injunctions; removal of offiers and directors; fines; revocation of or refusal to renew licenses of agents, adjusters, brokers and insurers. The powers and sanctions, plus the informal powers, sanctions and alternative modes of relief, extend far beyond what most industries experience. States exercise those powers comprehensively, not merely on a showcase basis.

To aid each other in our endeavors to protect the public, the states joined together at the invitation of a New York Superintendent, George Miller, in 1871, and formed the National Association of Insurance Commissioners. Today NAIC membership consists of the insurance regulators of the 50 states and the U.S. territories. As stated in the NAIC constitution:

> "The objective of this body is to serve the public by assisting the several State insurance supervisory officials, individually and collectively, in achieving the following fundamental insurance regulatory objectives:
>
> (1) Maintenance and improvement of State regulation of insurance in a responsive and efficient manner;
> (2) Reliability of the insurance institution as to financial solidity in guaranty against loss;
> (3) Fair, just and equitable treatment of policyholders and claimants."

The NAIC has sought to promote uniformity when appropriate, has developed model laws and regulations to address various issues, and has conducted studies and research projects on insurance related problems. The NAIC, therefore, provides a flexible and timely mechanism for discussion and improvement of the regulation of insurance. It provides a forum for consideration of the innovations each state presents and for development of the models each state may adopt.

During its more than 100-year history, the NAIC has developed a number of model laws and regulations. Some models

are designed to meet a nationwide pattern of activity and thus may be appropriately adopted by most, if not all, of the states. However, states do not always face the same issues so some models are adopted by the NAIC primarily for the use and guidance of those states that need to address a particular issue. Models may also be adopted by the individual states with variations that take regional conditions into account.

Whether local or universal, all are drafted with the protection of the insurance consuming public in mind, since either directly or indirectly all affect the public. Of particular interest to this Committee today is the model legislation that exemplifies aid to the consumer in understanding the insurance products available.

The NAIC has adopted the Life Insurance Disclosure Model Regulation, which includes a consumers' buyer's guide. The Regulation's preamble states that:

> "The purpose of this regulation is to require insurers to deliver to purchasers of life insurance information which will improve the buyer's ability to select the most appropriate plan of insurance for the buyer's needs, improve the buyer's understanding of the basic features of the policy which has been purchased or which is under consideration, and improve the ability of the buyer to evaluate the relative cost of similar plans of insurance."

Among other models, the NAIC has developed a regulation addressing the issues of misleading advertising of life insurance products and a regulation to protect the

interests of the policyholder when a life insurance product is being replaced by another product. Models have also been adopted by the NAIC requiring disclosure to the policyholder of the policy provisions and annual status reports of the policy for universal and variable life products. New York offers a Consumers Guide to Life Insurance, a copy of which is being distributed to you. It contains cost comparison tables with sample prices on typical policies for all life insurers licensed in New York.

In the area of accident and health products, there are models addressing the advertising of accident and health insurance and requiring an outline of the benefits provided in the accident and health insurance policy. The NAIC has also developed a regulation setting forth minimum benefits required in accident and health policies. Moreover, the NAIC has separate models requiring an outline of coverage and the setting forth of minimum benefits for Medicare supplemental insurance policies. We annually produce "Medicare Supplement Insurance in New York State" a consumer booklet providing comparative pricing information on policies that meet New York's standards for covering the Medicare gaps.

In personal lines, the NAIC has a model addressing disclosure in termination or cancellation of property insurance policies. Models also have been drafted to provide for the

simplification of language in the policy contracts of property insurance as well as in various other lines. New York, publishes a "Consumers Shopping Guide for Auto Insurance" as well as a "Consumers Shopping Guide for Homeowners Insurance" with comparison pricing for the 20 largest sellers of each type of insurance in the State.

A widely enacted and utilized model providing broad consumer protection is the Model Act Relating to Unfair Methods of Competition and Unfair and Deceptive Acts and Practices in the Business of Insurance. The model prohibits such activities as misrepresentation and false advertising of insurance policies; entering into agreements to boycott, coerce, or intimidate; defamation by distributing false information about a person's financial condition; unfair discrimination as in refusing coverage for a person because of sex or marital status, and tie-ins between acquiring credit and insurance.

The unfair trade practices model has been adopted in almost every state, and in the few states that have not adopted the model there is some form of legislaton addressing unfair trade practices. A related NAIC model regulation is the unfair claims settlement practices model which has been adopted by the majority of the states and which provides standards for what is considered prompt, fair and equitable settlements for all policyholders.

The NAIC has also developed model complaint reports to be maintained by the state insurance departments. Most of the states maintain complaint records and analyze these records as another regulatory tool. A trend in complaints in a particular line or by a particular company in a state may aid an insurance department to more quickly identify a problem that might be developing in that state.

New York also produces a complaint listing which ranks auto insurers. Since the automobile line accounts for half of all complaints received, the numbers are adequate to develop a ranking, albeit with imperfections. The auto complaint list is reported by the media each year and is available to the public upon request. It provides a measure of service and reliability.

States address the needs of insurance consumers by means other than through legislation and the promulgation of regulations. Most states distribute brochures on various types of insurance including automobile, homeowners and health, and several state departments have consumer hotlines or toll-free numbers to answer the questions of consumers. I have already distributed and discussed the brochures produced in New York. Brochures may include comparisons of costs, although some states publish cost comparisons separately. New York is about to embark on a new initiative in an attempt to get updated,

instant information to consumers. We will shortly begin a consumer tape information system permitting consumers to phone for immediate information.

Geographically larger states may have other offices and/or conduct outreach programs to address particular areas of abuse or concerns of policyholders or to reach geographically isolated regions of the state. An example of such a program is the SHIBA program of the State of Washington. The SHIBA (Senior Health Insurance Benefit Advisors) provides senior citizens with information concerning various governmental programs, including Medicare and Medicaid, and private insurance products such as supplemental policies.

New York conducts a consumer outreach program to some cities on a regular basis and to others as requested or needed. The New York Department is also included in the State Disaster Preparedness program and will send staff to affected areas to assist consumers when disaster strikes. The Pennsylvania Department was called in to assist at the time of the Three Mile Island incident. At all such disasters, the states work cooperatively with Federal Government agencies, particularly FEMA (Federal Emergency Management Agency).

It is impossible in this limited paper to list all the state initiatives, statutory enactments, and administrative regulations designed to aid the insurance buying public.

Insurance regulation encompasses the oversight of a broad range of insurance lines including but not limited to automobile, fire and casualty, homeowners, title, surety and fidelity bond, boiler and machinery, workers' compensation, accident and health, group health (e.g., Blue Cross/Blue Shield), flood and crop, avaiation, inland marine, ocean marine, credit, warranty and life. In addition, some lines include both group and individual policies.

There has been a tremendous amount of discussion conerning the McCarran-Ferguson Act and whether its antitrust exemptions are either healthy or necessary for the insurance industry. Much has been discussed about the importance of competition in the insurance industry and the benefits competition has or would have for the insurance consuming public.

The NAIC has recognized and continues to recognize the value of competition in the insurance market and the NAIC has continually supported efforts to foster and preserve that competition in insurance markets. We continue to believe that information to consumers is a vital factor in competition. The NAIC also believes that it is in the public's best interest to retain a comprehensive oversight of the insurance industry.

The apparent intent of the antitrust laws is to promote competition. The NAIC believes that the state

regulatory system has fostered competition, while protecting the interests of the insurance buying public. Although competition is an important element of the insurance mechanism the NAIC believes other legitimate concerns of the public must also be addressed.

State insurance regulators are constantly attempting to strike a balance between the benefits that can be derived from highly competitive markets and other public objectives. In any consideration of regulatory responsibility, the following factors must be balanced with competition:

1. The market availability of needed coverages;
2. Solvency and the reliability of insurers;
3. The price of insurance;
4. The quality of services; and
5. The fairness in dealing with all insurance claims and transactions.

The overriding concern of the regulators is whether repeal or modification of McCarran-Ferguson would inhibit or impede the proper balance necessary to protect policyholders. Under the current system, state insurance regulation is in the best position to continually monitor and balance the conflicting public policies of competition, spreading the risk and fairness in the insurance markets.

Two NAIC task forces in 1980 issued reports noting the importance of providing information to the consumers to effectively create or maintain a competitive market. The Life Insurance Disclosure Task Force stated:

> "An essential condition of effective competition is a sufficiently large body of informed consumers who will make rational economic choices."

Both task forces in recognizing the need for a consumer information system also noted the necessity of consumer initiative. The Task Force to Develop Meaningful Consumer Information on Personal Lines stated:

> "It is not possible to construct a consumer information system which will eliminate the need for individual buying initiative.

Information, however, must be compiled and made available to the consumer as much as possible. In addition to the state insurance departments' supplying information to the consumer, companies and agents also provide explanatory material to the insurance buying public. Various trade associations and the Insurance Information Institute also distribute such information.

The insurance consuming public's best interest is served by retaining a comprehensive oversight of the insurance industry at the state level. State insurance departments are local and easily accessible to the insurance buying public. The consumer can readily contact his or her insurance

department to seek redress, to have questions answered and to apply pressure for action at the state level. State insurance departments can regulate local, regional, and nationwide insurers with equal ease and efficiency. Many of the problems faced by the insurance business are statewide or regional in nature and can be more readily understood and addressed at the state level. Where uniformity is needed, the NAIC has proven to be a valuable facility for cooperation, an impetus for action and a means to achieve uniformity in appropriate situations. The regulatory network established by the states provides comprehensive oversight of the insurance industry and protects the public by monitoring the financial solveney of the insurance companies and the costs and availability of insurance products.

Congress's retained powers under McCarran-Ferguson coupled with the states' initiative provide a regulatory environment which fosters competition while protecting our nation's consumers and keeping them well-informed.

Mr. FEIGHAN. Mr. Olson, did you have comments that you wanted to make at this point or are you available just for questioning?

Mr. OLSON. Not at this point, Mr. Chairman. I'll respond to any questions that may be presented to my colleagues or myself.

Mr. FEIGHAN. I wonder then if any member of the panel, just for openers, would care to respond to Mr.—I'm not sure if Mr. Denenberg is still here—but if they would care to respond to Mr. Denenberg's specific concern addressed to the competency of agents. It seems to me that there's certainly minimal value in increasing the kind of disclosure requirements, increasing the kind of information, the quality of information that we provide to prospective purchasers unless they are dealing with individuals who are competent to explain the specifics of that information and to provide some comparative analysis for the fairly unsophisticated purchaser.

Mr. Denenberg had commented that in his opinion at least 70, 80—I think he even hazarded the guess that perhaps 90 percent of the agents in this country were simply incompetent. I wonder if any of the panelists are provoked into some kind of response to that suggestion?

Mr. OLSON. Mr. Chairman, of course, Mr. Denenberg could provoke—he could do just about anything that you wanted to do to

him. I went out in the hall and told him I was going to physically attack him if he didn't go into the men's room simply because we had a conversation. We talked about those agents and I said, "Herb, it depends on whether you talk to the president that year, or the president the next year." I think the level of competence of agents is something that I find it very difficult to quantify.

I can't tell you, Mr. Chairman, what the level of the competence of an insurance agent is overall. I can tell you that there are a lot of insurance agents in this world, in this country and, by and large, there are those agents that when they do violate certain statutes and when they do misrepresent things and that kind of gets us to the cost disclosure question that's been raised all morning long about an agent selling a product to you. There's no question in my mind that there is probably some incompetence amongst insurance agents just like there is incompetence amongst lawyers, doctors, State regulators of the business of insurance, in all kinds of professions.

I think that the issue is understanding what's going on in the marketplace. Today the people, the agents that I deal with, that I see on a fairly frequent basis, are generally very competent because they've got to survive in the marketplace. The forces of the marketplace with the newness of products, for instance, has forced the agent to be a lot more than a high binder that goes in and gets a license and walks out, if they are going to continually compete in the marketplace in the long haul.

Let me kind of demythologize something without being presumptive with the Chair and that is that whole issue of life insurance cost disclosure, Mr. Chairman, it is an issue that—I have been the president of the National Association of Insurance Commissioners and I chaired a task force called the Life Insurance Cost Disclosure Task Force. All God's children chair task forces from time to time and chair committees from time to time, and there's really nothing magic about cost comparison.

Let me give you——

Mr. FEIGHAN. If I might interrupt, Mr. Olson. That task force report was fairly critical, wasn't it——

Mr. OLSON. Yes, sir.

Mr. FEIGHAN. Of NAIC's regulations with respect to cost disclosure. What has been the reaction to the task force's criticism?

Mr. OLSON. Well, let me tell you, you can adopt a model regulation but you cannot necessarily always pass it. And let me tell you, in Texas we have a very large market share. Many other States have large market shares, too. Just because you're from Texas, doesn't mean it's the only one that has it. But we've gone completely the other way. I have two colleagues. We are appointed by the Governor. We are confirmed by the senate and we serve 6 years as an independent agency.

In the last few years there's been incredible turmoil in the marketplace as to products, as to indeterminant premiums, universal life, second generation universal life, variable life. For instance, I would say, yes, an insurance policy is indemnification but it's also a security.

It's also an investment. I wouldn't make the absolute statement that it is not a security, because it is. What happens is, products

are coming on market that are investment and security-sensitive, and as a result of that, they turn over every day. There is no way that you can honestly communicate to an insured what's going on.

In Texas, you had the NAIC model replacement regulation, where if you, Mr. Chairman, have an insurance policy and some agent or some individual wants to replace your policy or you choose to, you've had to jump through a lot of hoops, one does, to replace the policy. You give everybody notice—the company notice, the agents notice, and they all come out, and you go back and forth, and as a general rule, the way I work, and I am chairman of that insurance commission, I go, "Well, what do I want? What do I want?" Don't hand me a bunch of paper. I can read exponential and linear progression. I can't look at the shark's teeth in all these curves. You know, I just don't want to do all that. I mean, there are things in my life I want to do besides that.

Now, we're going to make that available, but that doesn't turn people on. You don't go to bed with that. You don't read that. You don't talk about that, but what you do is, you make sure you got a regulatory system that can give you that information if you want it. But this is where the problem is, in this particular area.

We had a comparison statement in Texas that many other states now have. We do in this country have a company that markets very aggressively, and they replaced what we refer to as the old whole life policy with what was called a deposit term policy. There was incredible—and I am not given to hyperbole. I am a little different than Mr. Denenberg in that respect, unless I get lathered up on something. This is not one of those issues I do. There was an incredible amount of misrepresentation, at least misrepresentation. Maybe at least some unethical conduct in the marketplace. We have about an 850-person department with about a $28 to $29 million budget.

We got a guerrilla force when it comes to business practices and procedures. We told our staff to get out there and our investigators to get out there in the field. We had people going into training seminars; we had people going in behind agents. We knew everything that was going on. But let me tell you what happens with all these kinds of cost disclosure statements. As a practical matter—I'm not saying it's good or bad, and I'm not against the consumer knowing what's going on. But as a practical matter, when you certify that to the attorney general of your State for the purposes of civil litigation, revocations of license and/or the revocation of the certificate of authority, from an evidentiary standpoint, the more material you have out there to hang somebody up that should be hung up, the more material you flood in that marketplace, the tougher it is from an evidentiary standpoint to prove up a case of misrepresentation. And what we did, we abolished the comparison statement and are using the Unfair Trade Practices Act for treble damages for all other kinds of legal remedies to deal with the practical problem in the marketplace.

I might also say that with the advent of financial integration, you're going to have a lot of people doing a lot of advertising and a lot of representation of what this policy is and or does. You are going to have somebody walking down the aisles of K mart—you already got that. You're going to have folks in Sears doing the

same thing. You're going to have folks in grocery stores doing the same thing. And the point is, in order to protect the insured, are you going to create such a cloud that; one, you have to be able to provide the information if they want it; but two, to make sure there are no sanctions attendant, because in order to get to that misrepresentation, it's just daggone hard to do.

Mr. FEIGHAN. Mr. Corcoran had suggested that the vast majority—I think that was your statement—the vast majority of States have adopted the NAIC model regulations on cost disclosure; is that correct?

Mr. CORCORAN. Yes.

Mr. FEIGHAN. I forget how many States you mentioned, but it was nearly 40, I think, that had adopted those regulations. The most recent regulations with respect to cost disclosure were proposed in 1983. However, can you update us on how many States have adopted those most recent and presumably more comprehensive stringent model regulations?

Mr. CORCORAN. Well, because in New York we have a point of sale comparison disclosure, unlike the model. So we have a different approach, but——

Mr. FEIGHAN. It was required by State law, even prior to the NAIC model regulation?

Mr. CORCORAN. Yes, that's right.

Mr. FOUDREE. Mr. Chairman, I might respond by saying that the process of developing the models is an ongoing process, because, as Mr. Olson has said, the marketplace is constantly changing. And so, in fact, right now, the NAIC has a life insurance cost disclosure task force which is studying these very issues and looking at disclosure items, such as rate of return which you were interested in earlier, and how to provide this information to the public. We have also placed consumer representatives on that task force for input.

So it's an ongoing process. And the States, once the models are promulgated, then turn to those models for guidance in promulgating their own State statutes.

Mr. FEIGHAN. Let me ask you this: Does the pre-1983 model regulation regarding cost disclosure require advanced disclosureto the customer, prior to the point of purchase?

Mr. FOUDREE. You're saying prior to 1983?

Mr. FEIGHAN. Well, prior to the 1983 regulation. You have the 1983 model regulation which has not been adopted by most States. Thirty-five to 40 States are operating under the 1976 model regulation. Does the 1976 model regulation require advanced disclosure, disclosure prior to sale?

Mr. FOUDREE. You mean at point of sale disclosure?

Mr. FEIGHAN. Yes.

Mr. FOUDREE. You have to provide information at the point of sale, or at delivery of the policy but there's also the right for a 10-day free look. So, in fact, the consumer has the right to change his or her mind. And the current situation—if you're talking about now, there must be a buyer's guide delivered and with respect to other types of coverage, an outline of coverage must be provided, for example, with respect to Medicare supplement policies. So that the more complex the policy, the more the regulations seek to focus on disclosure to the consumer at the point of sale.

Mr. FEIGHAN. I am just trying to understand the procedure on this, because we seem to have some information that suggests particularly that the information gathered into the indices is not provided prior to the point of sale, it's provided after the sale, but there is then, subsequently, a 10-day cooling-off period.

Mr. FOUDREE. I would yield to Commissioner Day from Utah on that point.

Mr. DAY. Mr. Chairman, I believe there——

Mr. FEIGHAN. Would you introduce yourself just for the record.

Mr. DAY. Yes; I'm Roger Day, the insurance commissioner from the State of Utah.

I am not reviewing notes as I provide this answer, but I believe the previous regulation said that by the time the policy was delivered or before, the cost disclosure information had to be provided, and that does leave some room for improvement. In my mind, we are, therefore, looking at that in addition to the other amendments, but that was also linked to the 10- or 20-day free look, which are the basic patterns and, in essence, was a compromise provision where the rigid cost disclosure was somewhat obviated by the possibility of having a cooling-off period, so that the sale could be canceled with a total rescission.

Mr. CORCORAN. In New York State we have point of sale disclosure and then 30 days after delivery, so it could be longer than 30 days between the prospect of purchasing.

Mr. FEIGHAN. Is that a 30-day cancellation, effectively?

Mr. CORCORAN. Yes.

Mr. FEIGHAN. Let me ask any one of the panelists if they would respond to the dialog that we had earlier on readability of policies. That, as I suggested, is an issue in which the marketplace would be the most compelling factor. Maybe there are some who suggest that's not the case. In fact, we had a good example presented by Mr. Denenberg, suggesting that despite what might be the industry's best effort, readability is far from a perfected science in insurance policies.

Mr. DAY. Mr. Chairman, I'd be happy to take a crack at that. I think the basic improvement that has occurred because of the marketplace and also because of the attention that Mr. Denenberg, being a great showman, gave to the issue of readability, as well as putting the insurance commissioners on the map, generally, has been the use of policy summaries. I do find, personally, some validity in the notion that an established contract that is well settled in the law, probably shouldn't be cavalierly tinkered with, but the notion that you can reform it to do what it's supposed to do from a legal standpoint should not get in the way of providing a summary that explains what the coverage really is.

Through the use of summaries that are made a part of the contract and the notion of strict agency, in terms of the agent's representations, I think we have the best of both worlds now of maximum benefit and summaries have improved dramatically.

I'd also like to point out in terms of your previous question that in terms of market share, most of the market is served by very competent agents. If there are 10,000 agents in the State, whether 50 percent are competent or not is not the issue; how competent are the agents selling 90 or 95 percent of the business is the issue,

and in that case I would say 90 or 95 percent of the agents selling 90 or 95 percent of the business are, in fact, competent, and getting progressively more competent.

Mr. CORCORAN. New York enacted the readability statutes and all our policies are in compliance, I think there is a test, it's quite technical. So it's in place right now. It's been in place for a couple of years. But I'd like to diverge for a second and stress for you now that we are entering this full financial service mentality, nationally. I think it's very important. And the NAIC is making every effort now to look at enhancing the accountability of the agents and the company, because suitability of products is very important, especially with these dynamic interest-bearing instruments, which are really investments.

So, perhaps maybe 10 or 15 years ago, we would have been right on point at these hearings, to a certain extent because a lot has happened between ours and Mr. Denenberg's tenure in office. And what we really have to look at, and that's what my office is looking at, is the suitability, heightened accountability. We take an awful lot of licenses away from agents. We fine a lot of agents. I don't know what other industry does that. I don't know how many bank tellers have been indicted lately for misrepresenting a loan or something. The fact of the matter is, we do, very aggressively, watch the professional behavior of agents. We have replacement regulations. We have an open complaint bureau which receives complaints. We call agents down. The agents in my State know that if we get a complaint, we're going to act on it.

So we do have accountability. Now, we have to have continued education, because, as you know, we've been telling you there are new products, new products out there that are interest sensitive and the public knows that, and the industry knows that. Forty-seven percent of Mr. Carter's new products are interest sensitive, then the whole life product, to a certain extent, is not what we should be looking at. We should be looking at now the accountability of the agents and the suitability of the products and perhaps readability shouldn't be—what we should be saying to the agents, if you sold this to this person and you represented this, then you're accountable. So, there is another whole layer of activity that we're into.

Mr. FEIGHAN. Does that trend, that you just described as a trend identified by Mr. Carter at Equitable, indicate to any of the commissioners that we are likely to see a two-tiered approach to regulation in the very new future—State regulation with sort of a Federal overlay?

Mr. CORCORAN. Absolutely not. There's no reason for any two-tier regulation. If banks were to get into insurance or anyone who's in insurance in my State, we wall off the assets, we separate the entities and holding company structure. You know, to a certain extent, the Baldwin United phenomenon did not occur in New York, because pursuant to our holding company regulations with the model now being looked at by the NAIC, we look at intraholding company transactions to make sure that the insurance function is separate and distinct from any other function of the holding company structure. And if someone is licensed to sell insurance, a Merrill Lynch, we control that license. The licensing function is the key to good

consumer service. If we don't have the power to give and take licenses, we can fine and they can weigh if it's worth taking this risk and paying a fine. It may be worth doing a certain abusive practice. We feel that there will be no fuzziness; we will be actively using our expertise to regulate insurance, no matter who is in the industry.

Mr. FOUDREE. Mr. Chairman, I might also point out that the phenomenonal rate at which these new life products have taken off, the universal life and the so-called U-2 type products that are being proposed or marketed, I think is itself proof positive or a very good example, of the fact that there is competition occurring in the marketplace and that the public is sensitive to price and is able to get ahold of the information. I think it is a demonstration of that.

Mr. OLSON. Mr. Chairman, I wanted to say that I think—if I may refer to Mr. Denenberg only in this sense—Mr. Denenberg didn't mind playing fast and loose with what his opinion was about everything.

I think that as a State regulator, under our licensing statutes, that the question of the competency of an agent has to be that under the police powers of our individual States, we, as to the health, safety and welfare of our particular constituents in our State, license agents, and that act of licensing agents defines a level of competency at which the State has said, if you attain that level of competency, you can sell insurance. And I think it's at that point that you have to assume that all agents are competent, based on the licensure statute.

Now that doesn't mean whether you like some fellow in a polyester suit or high binder or some big whatever moving around on you. I'm not talking about that. I'm talking about the legal definition of whether a person is competent. I have my opinions about whether—some agents I don't like. A lot of agents I do like. It depends on whether you want my political opinion. It depends on whether you want my philosophical opinion. It depends on what part of my opinion you do want.

In Texas we have readability on homeowners, we have readability on automobile, we have readability in comprehensive. And the one thing that has concerned me more about readability than anything is, I do know that those contracts are extremely complicated. I'm the major regulator in my State, and I go to my technicians and say, "Tell me what that means?" What you have to watch out for about easily readable policies is what the industry will take away from you. What I'm saying, it forces the momentum in the marketplace, in that they just want something that's more easily readable, let's give it to them. In the process, they may take away. In Texas, there was a dispute over what was their duty to defend. And there are those kinds of things where those answers are just not that easy, because there are things that are taken away in that contract that through all kinds of statutory and legal proceedings, historically, have established what that contract means.

Mr. CORCORAN. Mr. Congressman, an awful lot of these phrases have been interpreted by the courts, and once you start tinkering with them, you might hurt the consumer.

Mr. FEIGHAN. Let me return to the disclosure issue just momentarily and ask what the posture of the NAIC has been and is currently with respect to the disclosure of the financial strength of a particular company. I think that becomes particularly relevant in light of the Baldwin United experience.

Mr. FOUDREE. Well, I think we have in place probably the most unique system for financial disclosure of the financial condition of insurers or any other operating businesses in the United States today. Every State has a convention statement which it receives from every insurer doing business in its State, which is reviewed every year. I have such a convention blank which I have given to the subcommittee. That information is public, open, for people to come in and look at. My people will sit down, as will the staffs of the other departments, and explain it to the public. Furthermore, the information which is gleaned in examination reports is also public. Anyone can come in, including the press, and look at that information and have it explained to them by the examination department.

Mr. FEIGHAN. But I wonder what the value of that is. It's of value to examiners; it's of value to commissioners in discharging their responsibilities as overseers of the industry, but does that have any real value to a potential purchaser? Potential purchasers are not about to try to find out where the State commission is located and who they should contact and what questions, they should ask with respect to getting some indication of the financial solvency of a particular company.

Shouldn't the company have some requirement to provide that information directly to a customer?

Mr. FOUDREE. In fact, people do want to know where the department is, and in fact, they do come in and visit us every day. They call us by the thousands. And in fact, when people come in to visit us, what do they really want to know? Yes, some of them want to know what premiums are, and we will give them a customized review of the premiums for the kind of insurance that they want. But many people who come in want to know, is this company a good company? Is this a sound company? How long has it been around? What is its financial condition? They want to know if it's a safe company that they are going to put their money into. That is what they really want to know. If they want price information, we can give that, and we do give that to them, but that is not the focus of what people who contact us want—I'm just speaking from my experience now.

Mr. FEIGHAN. Well, what percentage, though, of the buying public would you expect makes contact with a State commission? It has to be negligible.

Mr. OLSON. Very few.

Mr. CORCORAN. Congressman, I would like to stress one point though. If you're licensed in New York State, that's a good company, as far as I'm concerned, and that's all the public has to know. They're licensed. They're duly licensed. We will regulate their solvency. Now you don't want the situation where the public would actually say the biggest is best, because that's not true. What we want the public to do is buy the best product, the most competitive product. For that reason, we have a guarantee fund. If a company

actually did go under, when it became bankrupt, the other companies would pick it up through the guarantee fund and the contract between the policyholder and the company would be kept valid. No one in the history of the Insurance Department of the State of New York has ever—any consumer in my State has ever lost a nickel on a life insurance problem.

Mr. FEIGHAN. Yes, sir.

Mr. DAY. I'd like to just interject briefly, in regard to your last question, that in commercial lines, there are very sophisticated buyers that do make use of the financial information available. That includes not only information from State regulators but also independent regulatory bodies such as the Best's Reviews and other companies. On personal line products, which are standard auto and homeowners' products, the agency represented by the independent agent or the company, if it is a direct writing company, also supplements that. So if there is enough at risk, there is a very sophisticated buyer. If not, the system does provide some adjunct to aid in consumer information. So the solvency issues, though they are not absolutly cut and dried, are material and are of import to consumers.

Mr. FEIGHAN. I would very much like to continue the dialog. I think it is very helpful and I think we're building a very important record for the subcommittee's consideration. Unfortunately, I cannot stay because of another commitment, and now we are getting a call for another vote.

I would like to ask the panelists if they would indicate their willingness, however, to submit to some additional questions in writing and provide written responses to those questions.

Mr. CORCORAN. Certainly, we would be glad to.

Mr. FEIGHAN. I would very much like to thank the panelists this morning. You've been very helpful in your testimony. I particularly would like to thank the NAIC for its help and its cooperation with the subcommittee over the past several weeks in preparation for this hearing today.

You will receive notice of any further hearings that the subcommittee will conduct.

Thank you very much and this ends today's hearing.

[Whereupon, at 12:15 p.m., the hearing was adjourned.]

COMPETITION IN THE INSURANCE INDUSTRY

THURSDAY, SEPTEMBER 13, 1984

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW
OF THE COMMITTEE ON THE JUDICIARY,
Washington, DC.

The subcommittee met, pursuant to call, at 9:30 a.m., in room 2141, Rayburn House Office Building, Hon. Peter W. Rodino (chairman) presiding.

Present: Representatives Rodino, Edwards, Schumer, and Fish.

Staff present: Warren S. Grimes, counsel; M. Elaine Mielke, general counsel; Marilyn Falksen, research assistant; Alan Coffey and Thomas M. Boyd, minority counsel.

Chairman RODINO. Today, the Subcommittee on Monopolies and Commercial Law continues its review of the antitrust exemption granted the insurance industry by the McCarran-Ferguson Act.

We will look at the effect of collective activities, particularly joint ratemaking, on competition and on prices in the insurance industry.

Insurance costs are a significant portion of most Americans' budgets. We will hear today that, in 1983, 11.8 percent of the Nation's disposable income was spent on insurance.

A study recently released by the Department of Transportation found that insurance fees now account for 19 percent of the cost of owning a mid-sized American car. Over the typical 12-year lifespan of this car, the consumer will pay $6,700 for insurance, more than the $6,650 he will pay for gasoline. The study predicts that insurance rates will continue to rise.

Is the consumer getting a good buy for his or her insurance dollar? Critics of the industry charge that unnecessary collective activities inhibit competition, create inefficiencies, and lead to artificially high prices for consumers.

The industry responds that, unlike most products, the cost of providing insurance can only be estimated at the point of sale. Large amounts of data must be collected and "massaged" in order to set rates that are both fair and adequate.

The antitrust exemption and the joint activities it protects, they argue, merely provide a mechanism to allow small companies to enter the market, thus increasing rather than decreasing competition.

However, a major question confronting the subcommittee is whether we have been drawing the line correctly between competitive and anticompetitive cooperative activities.

1984 GOV Competition in the Insurance Industry 739p bonknote.pdf

Our first witness this morning is Ms. Nancy Baerwaldt, who is the insurance commissioner for the State of Michigan. She will be testifying about Michigan's experience with a competitive rating system for workers' compensation insurance. I understand that this is a new, open-competition law and that so far it has produced some favorable and pro-competitive results.

Next, we will hear from J. Robert Hunter and John W. Wilson. Mr. Hunter is an actuary. He has worked for rating organizations and for the Federal Insurance Administration. Currently, he is president of the National Insurance Consumer Organization. Mr. Wilson is an economist and also president of J.W. Wilson & Associates, a consulting firm that specializes in regulation and antitrust matters. They will discuss the anticompetitive effects of joint conduct permitted by the antitrust exemption.

Finally, we will hear from a panel of rating organization representatives—Ms. Mavis Walters, senior vice president of the Insurance Services Office; Mr. Donald T. DeCarlo, vice president and general counsel for the National Council on Compensation Insurance; and Mr. Melvin DeYoung, president of the American Association of Insurance Services. Mr. DeYoung will be accompanied by Mr. Alden A. Ives, president of the Patrons Mutual Insurance Co. These witnesses will speak on the need for collective activities in the insurance industry.

Ms. Baerwaldt, we welcome you here today. We are interested to hear what you have to say about Michigan's new open and competitive rating law for workers' compensation insurance. Please proceed.

TESTIMONY OF NANCY A. BAERWALDT, COMMISSIONER OF INSURANCE, STATE OF MICHIGAN

Ms. BAERWALDT. Thank you, Mr. Chairman, and members of the Subcommittee on Monopolies and Commercial Law.

It's indeed my deep pleasure and privilege to be here today to explain to you the situation in Michigan under open and competitive rating of workers' compensation.

Prior to the open and competitive rating law, the Michigan Legislature, especially the house, held hearings on the cost of workers' compensation insurance. Michigan businesses told the committee that they had paid some of the highest rates in the country, that they did not understand the rating system, and that they thought that the pricing and marketing of the coverage had some unfair trade practice problems.

The committee also observed rate increases that were granted that were in excess of inflation from 1976 through 1979. Employers also told of 40 percent savings if they went to self-insurance or group self-insurance arrangements.

The legislature, listening to this testimony, carefully crafted a new open and competitive rating law which went into effect January 1, 1983.

The law provides that its purposes are to protect employers and insurance companies against inadequate and unfairly discriminating rates, to promote price competition, and, further, to assure that

rates are as low as possible consistent, of course, with the benefits that are provided under the Workers' Compensation Act.

It also provides that regulatory controls are to be imposed if there is not competition, and to improve fairness in the sale and the marketing of the insurance, and to assure availability.

The insurance industry stated, in addition to opposing the law, that they were worried about the impact of the elimination and the data base on which rates were made.

The legislature carefully considered those comments and believed that the insurance industry was indeed correct and that the rates did need the technical expertise of the experts in order that proper rates were made. However, they did want to promote competition in the marketing and sale of the coverage.

To this end, they formed something called the Data Collection Agency to oversee the collection of data, what was in the data, and how it was disseminated.

It should be noted that the Data Collection Agency has broad representation—representatives from small insurance companies, medium-sized insurance companies, and large insurance companies.

The data that is disseminated to insurance companies for making rates does not include trends, expenses, or profits. In other words, it includes historical data, and the insurance companies add to that historical data what their expectations are for their expenses and what their needs are and what their expectations for profits should be, and their own marketing ideas are incorporated into this as well.

In other words, the legislature, while wanting open and competitive rating, did believe that the industry did have a good point when they said that the data base did need to be retained.

This system also includes a careful monitoring of competition. The legislature ordered the commissioner to monitor competition, to report back to the legislature every January with a tentative report and every August with a final report on the findings of the open and competitive rating system in the preceding year. This must be preceded with a hearing, so all the insurance agents who were marketing, employer insureds, and insurance companies can come and give their qualitative and quantitative assessment as to what has occurred in the market in the previous year.

The commissioner, under the monitoring system the legislature put in place, is required to look at the control of the marketplace by one insurer, control being defined as 15 or more percent, the number of companies, the disparity of rates, the availability of coverage, and the share of people who are put into the residual market.

This report has been made to the legislature, and then the legislature must look at it, by a joint resolution agree or disagree with the findings of the commissioner, and permit the system to go forward or put into effect regulatory controls.

In other words, the open and competitive rating not only has the data base, but it has the close monitoring by the commissioner and, in addition, has ordered that if something goes wrong under open and competitive rating, that the commissioner is to implement remedies: a plan to create competition where it doesn't exist. There is a device whereby that could be done in the State of Michigan to

regulate excess profits, to set rates, and to make sure availability is present for all areas of the State and for all types of classifications.

The impact to date has been entirely positive on the Michigan business community. Rates have gone down, they have gone down substantially; the market structure has over 200 insurance companies writing; the top four insurers have less than 23 percent of the market; the agents report a great deal of front-end competition; the loss ratio, which is an insurance company measure of profitability, has increased from 55 to 79 percent from 1982 to 1983; and the availability of coverage has even gone up, and the residual market share has gone down.

So the legislature, in summary, created a carefully crafted law that provides for monitoring, that provides for remedies, and reviews annually the impact, and the law has worked highly well and very successfully in Michigan.

I must say, the insurance industry and the agent community have been extremely cooperative with the Bureau in making sure the system works, and I would say that the impact to date has been one of a very positive situation for the Michigan business climate.

There are still some problems, the competition is not perfect, but those are problems for us to look at, monitor, and perhaps solve in the years to come.

Thank you again, Mr. Chairman.

[The statement of Commissioner Baerwaldt follows:]

U.S. House of Representatives

Committee on the Judiciary

Subcommittee on Monopolies and Commercial Law

EXPERIENCE UNDER THE NEW OPEN AND COMPETITIVE PRICING LAW FOR WORKERS' DISABILITY COMPENSATION INSURANCE IN THE STATE OF MICHIGAN

by

Nancy A. Baerwaldt
Commissioner of Insurance
State of Michigan

September 13, 1984

The Old Cartel Pricing System

Michigan businesses, prior to the implementation of open and competitive pricing of workers' disability compensation insurance on January 1, 1983, had paid some of the highest workers' compensation insurance rates in the country. This was the September 1981 finding of the Michigan Legislature's Joint Subcommittee of the House Labor and Insurance Committees that had been formed to study how this line of insurance was priced and marketed.

This bipartisan committee, which carefully reviewed the operation of the workers' disability compensation insurance market over the past several years, also noted that since 1976 successive workers' disability compensation rate increases of 16.5, 26.2, 14.3, and 4.0 percent were granted by the Commissioner of Insurance, well in excess of the rate of inflation. These rate increases swelled the total cost of workers' disability compensation insurance to well over $900 million in 1979 and 1980. Attention was also given by the committee to the fact that the loss ratios for workers' disability compensation insurance had averaged around sixty percent, below most other property and casualty lines, making it one of the most profitable lines of insurance in the state with 40% of the premium going for overhead and profits. Concomitant with rising workers' compensation insurance rates and the high profits in the industry was the growth in the number of group self-insurance arrangements. Employers told the committee that they were experiencing

workers' disability compensation rate reductions of 30 to 40 percent when they switched from insurance to self-insurance or group self-insurance. At the time of the Subcommittee's review 40 to 45 percent of total benefits paid to injured workers were from self-insured arrangements, and the share of workers' disability compensation benefits paid by insurers was declining.

Employers, were, of course, disturbed about what were relentless increases in costs, but they also reported to the Joint Subcommittee that they found the rating and classification system difficult, if not impossible, to understand, and most were unaware of how they might appeal their classification and rate.

Further, employers advised that they often found that as a condition of even getting workers' disability compensation insurance they had to purchase some other type of insurance from the insuraance company, sometimes had to wait an unusually long time to receive dividends that were due and owing or not receive the dividends unless they renewed the coverage with the company, and noted that, especially in times of declining employment, that their payroll base had declined but the insurance company often did not do a payroll audit until well after the year had ended, thus delaying their receipt of refunds of excess premiums.

The rating, pricing, and marketing system described above was the product of noncompetitive cartel pricing in Michigan, a system which had evolved since prior to 1934 when all companies were

ordered by the Insurance Commissioner to use uniform rates and classifications, because of apparent destructive competition. The Michigan Legislature recognized that while this system may have had its purpose in its early years, cartel pricing in the late seventies and early eighties had resulted in rates that were too high, and a pricing system that was slow to take account of myriad marketplace changes or the ever-changing legal climate which affects the eligibility for, the benefit levels of, workers' disability compensation.

Statutory Features of the New Open and Competitive Rating Law

Reviewing the impact of the cartel pricing system, the objections of the industry to open and competitive rating, and the importance of the availability at reasonable prices of this line of insurance to the business community who must, as a matter of law, have security for the payment of workers' disability compensation benefits, the Legislature adopted a carefully crafted open and competitive rating law that has as its purposes the following:

(a) the protection of policyholders against the impact of inadequate or unfairly discriminatory rates;

(b) the promotion of price competition among insurers so as to encourage rates that will be as low as possible consistent with benefits provided under the Worker's Disability Compensation Act;

(c) the implementation of regulatory controls in the absence of adequate competition; and

(d) the improvement of fairness, and availability in the workers' disability compensation system.

1. The Data Base

Realizing that open and competitive rating was a dramatic shift from over 60 years of cartel pricing and recognizing the insurance industry's valid concerns that the data base on which workers' disability compensation rates were made should be preserved under an open and competitive pricing system, the Legislature provided in the open and competitive rating statute a requirement that insurers shall have access to a properly constructed data base to enable them to construct their rating systems. Insurance companies indicated that the availability of accurate loss data by occupation and industry classification was vital to the determination of rates that were truly reflective of loss, and to small companies who often relied upon statistical services in order to make their own rates.

To implement the requirements of the law that accurate rating data be made available to insurance companies, the Legislature mandated both an agency to oversee the assembling, collecting and dissemination of the data and to prescribe what data could be provided. The data collection agency, which is the agency mandated by law, has among its required membership representatives from large, medium, and small insurance companies, as well as an individual representing employers, insurance agents, and the general public.

Under the law the data collection agency is required to establish a plan for the collection of pure premium data, and the law further requires that these data must not contain (1) actuarial projections or trending factors, (2) profits, and (3) expenses, although loss adjustment expenses can be included. These data are disseminated to all insurers writing workers' disability compensation in the state and the companies, of course, add in their own profit and expense factors and do their own trending and actuarial projections. In addition, insurance companies are permitted to develop their own rating systems that may or may not comport with the basic features of the data that is disseminated to insurance companies. However, insurers are required to have a mechanism for the reporting of data that does conform to the basic statistical plan for the data that is to be disseminated. To date this system has worked well and insurers have learned how to utilize the data that is provided to them in order to make rational rating plans.

2. Monitoring of Competition

The Legislature, while believing that the marketplace is the best regulator of workers' disability compensation insurance rates, also was aware that competition could create distortions that might lead to availability problems in certain geographical areas or for certain occupational and industry classifi-ficatiions. To closely watch for these problems and to implement solutions in the event that competitive pricing caused marketplace problems, the Legislature required a periodic

examination of the marketplace by the Commissioner of Insurance. By August 1 of each year the Commissioner of Insurance is required to submit to the Michigan Legislature a report detailing the status of competition in the workers' disability compensation insurance market. To evaluate the status of competition the Commissioner must hold a public hearing and examine all relevant data available to determine the statewide status of competition in the industry and to determine for what industry and occupational classifications competition does not exist or is deficient.

In the examination to determine whether there is adequate competition in the workers' disability compensation insurance market, the Commissioner is required by statute to examine the following factors:

(a) the extent to which any one insurer controls the workers' compensation insurance market, or any portion thereof ("Control" is defined as more than a 15 percent market share.);

(b) whether the total number of companies writing workers' compensation in Michigan is sufficient to provide multiple options to employers;

(c) the disparity among workers' compensation insurance rates and classifications to the extent that such classifications result in rate differentials;

(d) the availability of workers' compensation insurance to employers in all geographic areas and all types of businesses;

(e) the residual market share;

(f) the overall rate level, which is not to be excessive, inadequate, or unfairly discriminatory; and

(g) any other factors the Commissioner considers relevant.

This report is subject to review by the public and by the Legislature. Any person who has a disagreement with the report may request a contested case hearing pursuant to the state's administrative procedures act, not more than 60 days after the issuance of the tentative report in January of each year. The contested case hearing process thereby provides the public a right to challenge the views of the commissioner vis-a-vis the findings regarding competition in the tentative report.

3. Remedies to be Implemented in the Absence of Competition

In addition the Michigan Legislature has prescribed certain remedies in the event that the Commissioner finds, and the Legislature agrees by concurrent resolution, that there does not exist a reasonable degree to competition in the workers' disability compensation insurance market. These remedies include:

(a) a plan to create competition where it does not exist, which may include, through the State Accident Fund, pricing which includes cost transfers and the creation of competition where it does not exist;

(b) the authorization of joint underwriting activities;

(c) the modification of the open and competitive rate approval process in a manner to increase competition which may include a return to prior approval of rates;

(d) the regulation of excess profits; and

(e) the establishment of workers' compensation insurance rates through commissioner order.

Taken together, the annual public hearing at which agents and employer insureds can voice their concerns regarding the functioning of the marketplace from their own experiences, the annual marketplace evaluation that is to be conducted by the Commissioner, the monitoring and overseeing that is provided by the Legislature, and the remedies that can be implemented to assure availability for all employers means that employers who must provide security for the potential payment of workers' disability compensation are availed this coverage at the lowest rate possible, consistent with the benefits that are provided under the workers' disability compensation act.

The Impact of the New Law to Date

As required, the Commissioner of Insurance did prepare a report that detailed the findings on competition in the workers' disability compensation insurance marketplace by reviewing insurance company market concentration, marketplace conduct, the rates charged by insurers for this line of coverage including company pricing behavior, and the profitability of this line of insurance. The overall conclusion of this report was that there had been a significant increase in competition in the Michigan workers' compensation insurance market in 1983 with the introduction of open competitive rating, but that there was also room for further progress.

1. Market Structure

The report found concentration within the Michigan workers'

compensation insurance market not to be inordinately high or at a level that would jeopardize competition. For 1983, the largest insurer group possessed a market share of 9.5 percent of total industry written premiums and the top four insurers had a combined market share of less than 23 percent. Overall more than 100 insurer groups had sold workers' compensation insurance policies in Michigan during the first nine months of 1983. Further the report indicated that the structure of the workers' compensation insurance market was not stagnant but was relatively dynamic. The degree of shifts in the insurers' market shares from 1982 to 1983 increased markedly from the degree of shifting between 1981 and 1982, the last year of cartel pricing. At the same time there was a fair level of entry into and exit out of the market between 1982 and 1983, resulting in a net increase in the total number of insurance companies writing this line of insurance in Michigan. There was, however a slight increase in market concentration between 1982 and 1983.

2. Market Conduct

Testimony at the public hearing on the impact of open and competitive rating was received from a number of parties, including several workers' disability compensation insurance agents whose reported experiences under the new regulatory environment were particularly instructive. All of the agents who testified commented on the considerable increase in front-end price competition from 1982 to 1983. Several agents testified to a significant decrease in the premiums being quoted to their

clients from the previous year, even for renewal business and for accounts that sometimes are considered less desirable by their insurance companies. Agents also testified, and the statistics verify their assertion, that the residual market business was down. Insurance company representatives also commented on the dramatic rise in competition in the workers' compensation insurance market. The insurance company representatives who testified also noted the considerable drop in premium volume despite the fact that the number of policies they wrote increased.

3. Rates

The fundamental component in the premium calculation is the manual rate. The Michigan Insurance Bureau conducted a survey of 1983 manual rates for 47 insurance companies and the 100 largest occupational classifications. The survey revealed a considerable degree of price variation within each classification among the sampled companies. In class 3081 (iron foundry), for example, the highest rate was more than double the lowest rate. This degree of disparity in manual rates among insurers contrasts sharply with uniform cartel rating and indicates that insurers are not continuing to fix rates under the new system. While the apparent lack of price fixing is a good sign, the high degree of disparity in manual rates raises concerns. The initial implication is that not all carriers are behaving competitively. Some insurers are charging and some employers are paying, very high rates.

There are some caveats to these disparities across companies in manual rates for the same classification. First, it is possible that differences in rates are substantially offset by differences in schedule credits, experience rating premium discounts, the quality of service provided by the insurer, etc. In other words insurers with high manual rates might also offer more generous schedule credits or better service than those with low manual rates. Some time must be allowed for both insurers and employers to adjust to the new regulatory environment. Insurers may be testing different marketing strategies under the new system.

Looking at the overall rate level, the average rate decreased by 10 percent from 1982 to 1983. This decrease followed a 22 percent decrease in the overall rate level from 1981 to 1982. (The former rate decrease resulted when the Legislature mandated that the average manual workers' compensation rates must in 1982 be reduced by at least 20 percent from the 1981 level.) The quantitative data therefore are consistent with the agents' and individual insurer's perceptions of the change in the marketplace.

4. Profitability

It is encouraging to note, with respect to profitability, that the 10 percent decrease in the overall rate level occurred between 1982 and 1983 despite the fact that statewide pure premium indicators suggested an increase of 5.6 percent in pure

premiums. This result is, of course, consistent with an increase in competition. Another index of the industry's overall efficiency and profitability is the statewide loss ratio, which can be calculated by dividing incurred losses and loss adjustment expense by earned premium. The loss ratio reveals the amount of actual loss protection received from each premium dollar paid. The portion of premiums not paid out in losses and loss adjustment expense is available for overhead and profits. Calendar year loss ratios for Michigan increased from .550 in 1982 to .788 in 1983.

5. Availability

Statistics on the distribution of covered payroll, written premiums, and the number of policies written between the assigned risk plan and the voluntary market provided the primary evidence on availability in the Michigan workers' compensation insurance market. Statewide data indicate a decline in the proportion of insured payroll in the residual market from 2.51 percent to 1.64 percent between 1982 and 1983.

While some occupational and industry classifications have a greater than average participation in the residual market, it is encouraging to note that every classification has experienced a decrease in its participation in the residual market. However, smaller risks tend to be overrepresented in the residual market relative to their representation in the voluntary market, a competitive marketing problem that needs review and continued monitoring.

Salutary Impact on Employer Insureds

Prior to the implementation of this new open and competitive rating law, the Insurance Bureau, as well as other state government agencies, received numerous complaints about the high, and unrelenting increase in, workers' disability compensation insurance costs. With the implementation of the new law, which provides not only for open and competitive pricing but for fair trade practices and appeal rights for insureds, complaints about prices and the system have all but evaporated. It is not surprising why. In 1981 Michigan businesses paid over $859 million for workers' compensation insurance; that number, based on current estimates, will be under $500 million this year, a decrease of 43 percent in 3 years. And over the 1981 to 1983 time period while rates were decreasing, the portion of each premium dollar which went to pay losses increased from about 62 percent in 1981 to 79 percent in 1983. Further, employers are now assured of fair trade practices in the marketing and selling of this line of insurance.

In summary, the impact of the new open and competitive pricing law has been positive, although there is some concern about the disparity in manual rates, the disproportionate number of small risks in the residual market, the slight increase in market concentration, and the continued use of dividend plans. These factors will be closely watched in the ensuing year.

Chairman RODINO. Thank you very much for your very excellent statement. I will advise you that your prepared statement will be inserted in the record in its entirety. We appreciate your giving us information about Michigan's experience with open and competitive rating.

Ms. Baerwaldt, you say that open competition has helped bring down insurance rates. Is that not the conclusion you have reached?

Ms. BAERWALDT. That is the conclusion, yes.

Chairman RODINO. You mentioned specifically the workers' compensation rates. What about high-risk groups? What has been the effect?

Ms. BAERWALDT. The impact has been universal. The high-risk groups have had rate decreases roughly proportionate to those the low-risk groups have had. So we've seen positive impact across all risk groups.

It should be noted that, simultaneously with the insurance reforms, there were reforms of the benefit side as well. So some of the high risk groups, through that legislative change, became lower risk groups.

So it can be said quite clearly that it's across all groups that the positive effect has been noted.

Chairman RODINO. Can you draw any conclusions about Michigan's experience with the new open competition law for workers' compensation that might apply to automobile or homeowners insurance?

Ms. BAERWALDT. Yes, I can. Michigan went pro-competitive—open and competitive rating for auto and home insurance 2 years prior, on January 1, 1981. That marketplace, especially the auto, is more concentrated structurally than is the workers' compensation, with the highest share being about 26 percent of the marketplace, whereas for workers' compensation it's considerably lower—6 or 7 percent.

We have had experience with open and competitive rating for auto and home insurance in 1981, 1982, and 1983, and to date the pressure on private passenger automobile insurance rates has been very moderate. In Best's report, the latest year data available for 1982 show only a slight increase in auto insurance rates.

So we have seen pro-competitive rates, and those have been beneficial to the consumer as well.

Chairman RODINO. Commissioner, do you think that the antitrust laws have a place in making the insurance industry generally more competitive, and, if so, what do you think that role should be?

Ms. BAERWALDT. I must first say that I'm not a lawyer, but I will say that I think——

Chairman RODINO. That might be helpful.

Ms. BAERWALDT. I will say that, clearly, the insurance companies are very good at competing. They understand marketing, they know how to price. So I think in a way it sells them short to have them jointly make rates, and I think that subjecting them to antitrust is another positive toward moving them toward being more competitive.

Chairman RODINO. One of our later witnesses will testify that the use of deviations from suggested rates promotes competition in workers' compensation insurance.

Now we've heard your statement about the kind of law that you have in your State. As I understand it, Michigan did allow deviations prior to 1982.

Would you say that the ability of insurers to deviate from bureau rates led to a competitive environment in Michigan prior to 1982?

Ms. BAERWALDT. That's a very good question and a very tough one to answer. Let me just say that yes, it is correct that deviations were permitted under the old cartel pricing. However, there was very little deviation from the rates that were filed, only in a few agricultural classes, for example.

There was really no incentive to deviate because of the cartel pricing structure that was put into effect. You would simply reduce your income.

So we found few deviations in Michigan, but once open and competitive rating went into effect, we found the use of discounts on a greater scale, the use of scheduled credits.

So we are achieving, I think, quicker and faster than we could have through deviations, the impact of competition by having an open and competitive rating law.

Chairman RODINO. Ms. Baerwaldt, just a question relative to your experience. How long have you been a commissioner of insurance?

Ms. BAERWALDT. Since 1980.

Chairman RODINO. Is your position an appointive one, an elective one, or——

Ms. BAERWALDT. I am appointed by the Governor.

Chairman RODINO. I want to thank you very much, Ms. Baerwaldt, for your testimony this morning. You may not be a lawyer, but you certainly bring to us the kind of experience and the kind of testimony that is not only understandable but certainly makes it possible for us to really be able to get a handle on some of these issues. Thank you.

Mr. Edwards.

Mr. EDWARDS. Mr. Chairman, I ask unanimous consent that the committee permit the meeting this morning to be covered in whole or in part by TV broadcast, radio broadcast, or still photography.

Chairman RODINO. Without objection, it is so ordered.

Mr. EDWARDS. Thank you, Mr. Chairman.

Commissioner, as a result of the changes in the conduct of insurance in Michigan, how do the rates compare with other States?

Ms. BAERWALDT. We still have probably rates that are sometimes higher and sometimes lower than other States.

There, of course, is the Workers' Compensation Act itself which determines the benefits to which one is entitled under the Work Comp Act. So we still have in some places some rates that are higher than average, and we also have some rates that are lower than average.

It's kind of hard under open and competitive rating to actually get the exact rate, because the marketplace changes quicker sometimes than we can measure, but I would say that on balance, there is an averaging and moving toward the average of the country in work comp rates for Michigan.

Mr. EDWARDS. Under the cartel system they were higher, as I think your testimony indicated.

Ms. BAERWALDT. That is absolutely correct; yes.

Mr. EDWARDS. The chairman in his opening statement pointed out how very expensive automobile insurance really is. Are your automobile insurance rates lower or higher than the average of other States?

Ms. BAERWALDT. The latest Best's reports that I saw indicate that Michigan's auto insurance rates average around $6 or $7 or $8 higher than the national average per year, and that indicates about an average rate nationally that is also what you would find in Michigan.

Mr. EDWARDS. Well, why isn't competition bringing those rates down?

Ms. BAERWALDT. Competition brings those rates down because the consumers and the business persons in the case of work comp become informed. When they learn that there is open and competitive rating, they understand that there is a payoff to shopping around.

So it's a learning process, and over time insurance companies, quite frankly, compete quite vigorously.

The data on rates are available in our office, and competitors come and look to see what their competitors are doing and then perhaps go back and revise their own rates on the basis of that.

So it permits the marketplace to change immediately with benefit changes or legal changes. So the informed buyer and the informed insurance company make for a very competitive market.

Mr. EDWARDS. Would they be in violation of Michigan antitrust law or other Michigan law if the companies got together and fixed rates?

Ms. BAERWALDT. Yes, they would. It is, under the Work Comp Act, prohibited to join a rating organization, and likewise there is an advisory organization for auto, but it is advisory; they do not make rates.

So all of the rating for auto, home, and work comp are open and competitive rating and filed and used with the State.

Mr. EDWARDS. Has the new system inaugurated in Michigan resulted in more insolvencies?

Ms. BAERWALDT. No, it has not.

Mr. EDWARDS. And you have a staff that issues regulations so that the insurance companies maintain an appropriate level of reserves and operate according to State law?

Ms. BAERWALDT. Yes, and the Michigan law on that point—reserves and investments—is probably very similar to other States; yes.

Mr. EDWARDS. Thank you, Mr. Chairman. It is excellent testimony.

Chairman. RODINO. Thank you.

Commissioner, before you go, first of all, the subcommittee may send you some written questions to which we hope you would respond.

Ms. BAERWALDT. I'd be happy to.

Chairman RODINO. Before you leave, there are a couple of other questions I want to ask. I think it would be helpful for us to get a response to them from you.

You mentioned a while ago that the consumer—the purchaser of insurance—especially in the State of Michigan, has had an opportunity to go around and shop. I think you mentioned workers' compensation specifically. Was that the question you addressed?

Ms. BAERWALDT. Yes. In workers' compensation and in auto insurance—

Chairman RODINO. And auto?

Ms. BAERWALDT. Both.

Chairman RODINO. You did include auto insurance.

Do you think that there is sufficient information being supplied by the industry to the consumer which makes it possible for him to be able to make a judgment about which alternative best meets his needs?

Ms. BAERWALDT. It's really a very tough judgment, especially with auto insurance where there are many options in the coverage package you buy.

In work comp, really, the benefits are provided by law, so the employer doesn't get benefit differentials across companies, but the purchase of auto insurance is extremely complicated.

In Michigan, with a no-fault package, there are some mandatory coverages and some minimum liability coverages.

Now, it's tough to shop, and you also have to make the decision as to whether to buy comprehensive or collision insurance because those are optional coverages.

So I think the purchase of automobile insurance is a very complicated process. We do provide from our Bureau as much information as we can, but the more interest they take in making that purchase decision, the better they are going to make it for themselves.

So it's a complicated decision, and we are putting out rates across companies and for various locations in the State on auto.

Chairman RODINO. Do you think, though, that the kind of information that is available for the consumer as to rates is sufficient to give him enough knowledge to make a judgment?

Ms. BAERWALDT. It probably can always be better. I would think that the availability of the information from the Insurance Bureau is good information, but it may not be specific to the particular consumer.

It's also very hard to keep the information timely under an open and competitive rating system because companies can immediately change rates and file them with the Bureau.

But it is no doubt the case that we can't inform the consumer too much. A consumer can't be too informed when he or she buys auto insurance. It's a complicated decision.

Chairman RODINO. Finally, as insurance rates go down under a more competitive environment, do you think that there is a greater risk that companies would become insolvent?

Ms. BAERWALDT. There certainly is a need to watch and make sure that the rates do not get too low.

The Legislature in Michigan has established open and competitive rating with the purpose of rates being as low as possible but only consistent with the benefits. So in other words, there's an implied floor below which rates should not go, and there is a very long tail——

Chairman RODINO. Well, who's going to do the watching?

Ms. BAERWALDT. It is clearly the responsibility of the insurance departments of the States to do the watching to assure that solvency is there.

Chairman RODINO. And is that department equipped with all of the necessary information, facilities, or mechanisms to be able to deal with those insolvencies should they occur?

Ms. BAERWALDT. Michigan has a small staff relative to other States. We have an Insurance Bureau staff of about 120 people, which is about average in terms of its size, although Michigan is a large State. We do have a very competent staff of good examiners.

There's no question, with only 15 or 16 examiners, that we are short staffed and put our efforts into priority companies.

We do, fortunately, have a life and health and property and casualty guarantee association to pay the claims of insolvent insurance companies. So we do, I think, a very good job of that although our staff is quite skimpy.

Chairman RODINO. Well, thank you very much again for your very excellent testimony, Commissioner.

Ms. BAERWALDT. Thank you very much.

Chairman RODINO. Our next witnesses will be Mr. J. Robert Hunter, president, National Insurance Consumer Organization; and Mr. John W. Wilson, president, J.W. Wilson Associates, who will testify as a panel.

We will, of course, ask that you restrict your oral testimony to not more than 5 minutes each, and we will ask you questions.

Mr. Hunter, you may proceed first.

TESTIMONY OF J. ROBERT HUNTER, PRESIDENT, NATIONAL INSURANCE CONSUMER ORGANIZATION; AND JOHN W. WILSON, PRESIDENT, J.W. WILSON ASSOCIATES, INC.

Mr. HUNTER. Thank you, Mr. Chairman.

We live in an era where the public demands efficiency, and as a result, there has been a move toward deregulation and moves in the Government for more efficiency and so on.

Insurance has moved in the direction of open competition ratemaking. However, open competition in insurance is unusual in that it still means the cartels operate; consumer information is not supplied; and other impediments to competition remain in place, not that they move into the mainstream of the American economy.

Insurance is a very large industry; 11.8 percent of the disposable income is paid into insurance.

Impartial studies of insurance—an example is Andrew Tobias' book—have shown that monumental inefficiencies exist. Insurance executives have said that Mr. Tobias is right.

For each $5 of premium currently paid into fire and homeowners insurance, only $3 is delivered in benefits, $2 in overhead and profits.

This inefficiency led Tobias to say that, "Republican or Democrat, socialist or conservative, there is something upon which we can all agree: waste is bad; inefficient systems rob us all." The problem is that the country has not decided if it wants insurance to be regulated or not.

Federal policy is embodied in the McCarran-Ferguson Act and comes down four-square in favor of regulation. As Senator Ferguson put it in the Senate floor debate,

> The bill would permit, and I think it's fair to say is intended to permit, rating bureaus. I think the insurance companies have convinced many Members that we cannot have open competition in fixing rates on insurance; if we do, we will have chaos.

Thus, the McCarran-Ferguson Act exempted the business of insurance from the full impact of Federal antitrust law but made the exemption contingent upon State assumption of authority in regulation. The law of the land is, in a word, to regulate.

But regulation is a failure, as GAO told you in 1979. Even the creators of the current system of State regulation, the State insurance regulators, have recently found remarkable deficiencies in the State regulatory framework.

NICO's research into the quality of State regulation confirms its weaknesses. Too little money is spent on regulation, 20 States have no actuaries on their staff, making sophisticated reviews impossible; some States have no examiners at all; many States spend less than $1,000 per company on regulation.

No wonder the New Jersey insurance commissioner recently said the archaic procedures and equipment of the New Jersey Insurance Department in regulating the megabillion-dollar insurance industry are woefully inadequate.

All of this leads to the conclusion that if regulation is to do an effective job, massive increases in State budget allocations are necessary; even the States have said so. But I feel it's unlikely that this will happen, given the current adversity to budget increases in the States.

If regulation is weak, certainly competition should do better. Every major study has concluded that in theory it should. We agree, but our studies show that under current conditions there is no effective competition in this industry for personal lines of insurance.

I have some charts, that are attached to my statement, that show that the insurance industry made exceptional profits in recent years, which manifested themselves in very high increases in stock prices. [Charts follow Mr. Hunter's statement.]

Mr. HUNTER. Surprising, however, as this chart shows (pointing to chart No. 3) Mr. Chairman, the profits, even in an era where profits have been excessive in the insurance industry, have been even higher on average in the States that have gone to open competition.

Why does open competition do so poorly? Competition works too well, some would say, in commercial lines of insurance, and I think it does work well in commercial lines of insurance, because commercial buyers are sophisticated, and they have choices; they don't have to buy insurance, they can self-insure, they can have offshore captives. Personal line insureds, auto and homeowners insurance purchasers, do not have those options.

The problems in competition include price fixing, the fact that the wholesale level still establishes the retail level's price, just like the old fair trade law days, and so on, but I'm going to focus on price fixing, because that's what you've asked me to do.

"Cartel" is defined as a combination of independent commercial enterprises designed to limit competition. Surely rate bureaus qualify to be called cartels by that definition.

The National Council on Compensation Insurance is classic in its cartel structure. Its constitution bluntly requires adherence. No wonder that in those States that have gone to open competition, such as Michigan, rates have dramatically fallen.

The Insurance Services Office does not have the adherence requirement, but the practices it engages in are clearly anticompetitive. It sets price for rival sellers in many States.

They publish premium comparisons in every State but make such information only available to insurance companies and agents, not to the public. In other States, the rate bureau may establish only part of the rate, but nonetheless they thwart competition.

There is a cancer on insurance; the cancer is the rate bureau, and it's malignant.

It is clear that the rate bureau is intended to lessen compétition, giving members a forum for obtaining intimate knowledge of the pricing guidance dispensed to rivals as well as the pricing of competitors without doing the same for buyers.

This does not mean that such things as joint data collection are not necessary. Surely small insurance companies need joint historical experience, but that can be generated by the State or otherwise, far short of permitting massive price fixing. That's what Michigan has done.

Data on price behavior published by the insurance services office show that the cartel is alive and well in personal lines. On page 19 of my statement, I show those data.

Whereas the Supreme Court in 1944 may have found that the cartel was going 100 miles an hour in the 25-mile-an-hour antitrust zone, it's clear that the ISO now goes about 80 and that the national council still goes near 100.

There is little doubt that without the antitrust exemptions that belong to this industry by statute, rate bureau practices would be seen as crossing the line that separates collective service to meet the public need from criminal activity.

What are we do to? The choice is yours. We must choose as a nation regulation or competition. If you choose competition, you must amend the McCarran-Ferguson Act to stop these anticompetitive practices. If you choose regulation, I believe Federal standards to assure quality regulation should be enacted.

I encourage you to choose competition to begin to move America's insurance industry into the mainstream of the American economic forces.

The existence of cartels must cost people money. What cartel would set a price that would make its least efficient member go under?

As State Farm Insurance Co. put it:

> The current State-sanctioned joint method of rate setting which functions in many States weakens the beneficial effects that independent insurers otherwise would have on rate sufficiency and availability. Sheltered by rating bureaus, there is currently limited incentive for many insurers to sharpen their rate structures, pare their costs, or seek out new markets.

The insurers are asking you to do something very radical when they ask you to continue to exempt them from the full forces of competition. Insurance belongs in the normal free enterprise system, and it's time Congress acted to put it there.

Thank you.

[The statement of Mr. Hunter follows:]

IMPACT OF RATE BUREAUS ON COMPETITION AND INSURANCE CONSUMERS

Testimony of

J. Robert Hunter, FCAS, MAAA 1/
President, National Insurance Consumer Organization

before the
Subcommittee on Monopolies and Commercial Law
Committee on the Judiciary
United States House of Representatives

September 13, 1984

344 Commerce Street
Alexandria, Virginia 22314
(703) 549-8050

Mr. Chairman, and members of the Subcommittee, it is a great pleasure for me to appear before you today in response to your request to comment upon the impact of joint insurer activities, particularly joint ratesetting, upon competition and upon insurance consumers.

INTRODUCTION TO THE PROBLEM

We live in an era where the public seeks efficient and effective governmental and private organizations. Thus, there has been a revolution in federal government spending, Proposition 13-type impacts at the state and local government level, and a move to deregulation of many industries.

Deregulation seems successful; some say "airline deregulation has been fabulously successful," 2/ citing lower and varied fares, better service, innovative new entrants,

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1/ Mr. Hunter is a property/casualty actuary, a Fellow of the Casualty Actuarial Society and a Member of the American Academy of Actuaries. He worked for rate bureaus for over 11 years, including supervisory actuarial work in predessor organizations to today's Insurance Services Office (ISO), the major rate bureau for property/casualty insurance, and the Automobile Insurance Plans Service Office (AIPSO). Mr. Hunter also served 10 years in the federal government, as Chief Actuary of the Federal Insurance Administration (appointed by George Romney in 1971), Acting Federal Insurance Administrator (appointed by James Lynn in 1974), Federal Insurance Administrator (appointed by Carla Hills in 1976) and Deputy Federal Insurance Administrator (appointed by Patricia Harrison in 1977). He founded NICO in 1980, where he serves on a pro-bono basis, as President. He earns his living by serving state governments and the federal government as a consulting actuary and public policy consultant. He has been appointed to three committees to advise the NAIC on public policy, ratemaking and profitability issues.

2/ Benefits and Costs of Insurance Deregulation, Stelzer and Alpert, NERA, October, 1981.

and more efficient utilization of capacity. Deregulation of the securities industry has resulted in significant savings for customers.

Even in insurance, a form of deregulation has occurred, as many states have moved to "open competition" ratemaking for property/casualty insurance. Insurers have extolled the virtues of competition, and have called for more and more freedom for pricing. 3/ "Open competition" needs careful definition, however, because the way it is defined by the insurers means that cartels are free to operate, consumer information is not supplied, and other major impediments to competition remain in place -- not that they move into the mainstream of the American economy.

BACKGROUND

Insurance is a mammoth industry, whose premium collections in 1983 represented 11.8% of the nation's disposable income. 4/ It is the fourth leading purchase Americans make, after food, housing and just behind personal income taxes, although it may surpass the latter within the next two or three years. Roughly ten dollars is spent on insurance for each dollar spent on religion and private welfare in the United States, an interesting comment on faith and priorities in this generation.

3/ See, for example, Report of the Advisory Committee on Competitive Rating, NAIC Proceedings-1980, Volume II, p. 414.

4/ See Exhibit 1, attached.

When major impartial studies of insurance have been made, they find inefficiencies of monumental proportions. 5/ Studies we have done confirm the high cost of writing insurance. 6/ For each $5.00 of premium paid into fire and homeowners insurance only $3.00 of benefits is delivered. Think of the inefficiency! Auto insurance isn't much better, only $3.13 of benefit per $5.00 of premium. Compare this to efficiently delivered group health insurance which for each $5.00 of premium delivers about $4.20 worth of benefits, or state run workers compensation programs that deliver benefits at half the cost of insurance company workers compensation plans, at about $4.35 of benefit for each $5.00 of premium and you can see the system is way overpriced.

The industry activity of recent years, mergers and lay-offs of sizable numbers of employees, confirm an extant inefficiency; their passionate fight to exclude banks from entering insurance is further evidence of fear of efficient competition. When Fireman s Fund pruned its staff by 1200 people earlier this year, its chief exceutive officer said that, "he, like veteran insurance executives, is vexed by the cost duplication and inefficiencies of the agency system in writing personal lines. 7/

5/ ". . . the number of superfluous insurance industry employees is probably (close) . . . to a million." The Invisible Bankers, Andrew Tobias; Linden Press, 1982. P. 24.
(Emphasis, the author's.)
"Tobias says the industry is inefficient, and he's right. We spend too much money in distribution, administration and in what is considered to be pure waste." John Cox, then-President of the Insurance Company of North America, quoted in Insurance Advocate, June 12, 1982, p. 16.

6/ Loss and Expense Ratios, New York Insurance Department.

7/ Journal of Commerce, May 2, 1984, p. 7A.

DIAGNOSIS

What is causing this inefficiency, that led one observer to state, "the question to which I think answers are possible is the question of efficiency. Because -- Republican or Democrat, Socialist or Conservative -- there is something on which we can all agree: Waste is bad; inefficient systems rob us all." 8/

The problem is, in a nutshell, that this country has not decided whether it wants insurance to be regulated or not. That is the key question before you to decide, because, either way a more efficient system can be created. But we can't have both -- and thus neither effectively -- without paying the price of monumental waste and inefficiency. Today we, as a nation, allow 12% of our disposable income to drift along in a sort of never-never land between regulation and competition, the cost of which easily amounts to tens of billions of dollars annually to the American people.

ALTERNATIVE #1 -- REGULATION

Federal policy, as embodied in the McCarran-Ferguson Act comes down four-square in favor of regulation. As Mr. Ferguson quite candidly put it in the Senate floor debate:

> This bill would permit -- and I think it is fair to say that it is intended to permit -- rating bureaus . . . I think the insurance companies have convinced many members . . . that we cannot have open competition in fixing rates on insurance. If we do we shall have chaos. 9/

8/ The Invisible Bankers, op. cit.

9/ Congressional Record, Senate, February 27, 1945, p. 1481.

Thus, the McCarran-Ferguson Act exempted the business of insurance from the full impact of federal anti-trust law but made the exemption contingent upon state assumption of authority in regulation. 10/

The law of the land as pertains to insurance is, in a word, REGULATE!

Regulation is a demonstrable failure, as the GAO told you. 11/ It lacks the will or the resources to do an effective job. Even the creators of the current system of state regulation, the state insurance legislators, have found remarkable deficiencies in the current state regulatory framework:

> The state regulatory apparatus is underfunded, understaffed and underequipped . . . When it comes to computers, while the state-of-the-art is futurist, the art of the state is an heirloom. 12/

NICO's own research into the quality of state regulation confirms its weakness, both as to lack of will and lack of way. For instance, a study by professors from Harvard found that 62 percent of state regulators saw themselves as arbiters (i.e., as judges) rather than as agents (i.e., as

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10/ Although President Roosevelt thought that the bill required the states to "effectively perform" the responsibility of regulation, the courts have held that the mere existence of any state law ousts the anti-trust laws. See Statement of President Roosevelt on signing the McCarran-Ferguson Act, March 10, 1945.

11/ Issues and Needed Improvements in State Regulation of the Insurance Business, GAO, 1979.

12/ Risk, Reality, Reason, Conference of Insurance Legislators, September, 1983.

representing the public interest and not the insurance industry.) 13/ The troubling fact is that the judge hears only one side, thus making Mr. Ralph Nader's suggestion to you of the need for a national consumer presence a very valuable idea.

Thus, the will is weak, even by their own admission. The way, soundly criticized by the state insurance legislators, is pathetically short of needed levels, viz:

- o Twenty states have no actuaries at all on their staffs, making sophisticated review of rate filings or competitive levels impossible.
- o Of 7,318 actuaries in the country, 61 work for state insurance departments.
- o The amount spent on regulation by the states is 5% of the taxes and fees paid into the states by insurance companies, the range being from 1.8% in Missouri to 12.2% in New York.
- o On a per-company licensed basis, eleven jurisdictions spend less than $1000 per company for all regulation (Arizona, Delaware, DC, Hawaii, Idaho, Montana, North Dakota, South Dakota, Utah, West Virginia and Wyoming.)
- o New York spends an average of $28,726 per company, roughly twice as high as the next state, California.
- o Five states have no examiners at all.
- o The average number of companies in the nation, per examiner, is 5.3.
- o Delaware spends $409 per licensed company -- barely enough to keep the names and addresses of the boards of directors current.

13/ The Regulatory Executives, Miles and Bhambri, Harvard Business School, Sage Press, 1983. They noted that 53% of the respondant insurance commissioners had worked for the insurance industry previously; a percentage consistent with GAO's findings, op. cit.

- o North Dakota's total staff divided into the number of licensed companies shows that each staff member is "responsible" for 58.3 companies (can they even memorize all the names?).

- o Montana has 559 licensed companies per examiner (but that's not bad compared to those five states listed above with no examiners at all). 14/

No wonder the new New Jersey insurance commissioner could issue a press release earlier this year noting that he had just recognized the states of Alaska and Hawaii by ordering a 50-star flag to replace the 48-star flag in the Department's hearing room. He called this step "indicative of the archaic procedures and equipment (the Department) has to labor with in regulating the mega-billion dollar insurance . . . industry." 15/

An example of the overwhelming inadequacy of state regulation is that, unlike utility regulation, it has never challenged one cent of expenses, allowing insurers to fully pass through junkets to Hawaii, the millions spent in lobbying against unisex legislation, institutional "puff-up" advertising, charitable contributions (they're nice -- but should consumers, who have no say in who gets the money, bear the cost?), etc.

All of this leads to the conclusion that, if regulation is to do a truly effective job, massive increases in state

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14/ Sources: Insurance Industry Committee of Ohio, year ended December 31, 1981 report; Life Insurance Fact Book, American Council of Life Insurance; Year Book, American Academy of Actuaries, 1984.

15/ Official News Release, State of New Jersey, Department of Insurance, May 17, 1984.

budget allocation to such effort is necessary. We feel that this is highly unlikely given the current adversity to budget increases in the states and the tremendous lobbying clout of the insurance industry. 16/

ALTERNATIVE #2: COMPETITION

If regulation is so weak, certainly competition should do better. Every major study has concluded that, in theory, it should. 17/

NICO agrees that, in theory, competition would be superior to regulation, but our studies show that, under current conditions, there is no effective competition in this industry for personal lines of insurance.

Chart #1 shows that the property/casualty insurance industry made exceptional profits during the period 1976 - 1983. 18/ Chart #2 shows the inevitable impact of such profitability upon insurers' stock prices *vis-a-vis* all American industry stock prices.

Charts #3 and #4 show the surprising fact that profits for private passenger car insurance (about one-third of the

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16/ "I once asked a friend in the game how come the Connecticut Insurance Department only had 29 examiners," says a former state regulator, "and he said 'because the Travelers doesn't want them to have thirty.'." The Invisible Bankers, op. cit.

17/ See, for example, The National Commission for the Review of Anti-Trust Laws and Procedures, Report, 1979; Pricing and Marketing of Insurance, The Justice Department, 1977; Staff at Federal Trade Commission, Report, 1978.

18/ Our studies show that this is a below average risk business which should obtain only an average profit. See, Investment Income and Profitability in Property/Casualty Insurance Ratemaking, J.W. Wilson and J.R. Hunter, 1983, Chapter 5.

total income of the property/casualty industry) were higher in open competition states than in prior approval states. Over the study period, the chance for having a profit in a state greater than the countrywide average profit was 50% for prior approval states, but 76% for open competition states. In "open competition states" the chance for profiting was 50% higher; the actual profit in "open competition" states was more than twice that of prior approval states. One is forced to ask the question: Is the "open" in "open competition" really the door to excessive profits?

COMMERCIAL LINES PROPERTY/CASUALTY INSURANCE

Competition does seem to work, some would say too well, in the commercial lines of property/casualty insurance. The reason it works better there, it seems to me, is three-fold:

- Commercial buyers of insurance are sophisticated, can get and understand the needed information and can run bids on needed coverages. They have, because of their size, considerable leverage.

- Commercial buyers have choices (e.g., captive insurers now write $7 billion in premiums up from zero in the early 1960's 19/; self-insurance now represents many more billions), options personal lines insureds don't have. 20/

19/ Journal of Commerce, "Captive Insurance Trend Continues" May 23, 1984.

20/ The reason that self-insurance has grown, according to James A. Kinder, Executive Vice-President of the Self-Insurance Institute of America, Inc. is as follows: "Only after years of ineffective rate-making policies, declining service and an inability to respond favorably to consumer needs did self-insurance emerge." Doubtless, this is, in part, a criticism of rating bureaus. Unfortunately, the options open to commercial business is unavailable to personal lines insureds.
A Dialogue on Industry Issues, NILS Publishing Company, June 6, 1984.

- Commercial buyers have political clout. Thus, for instance, when the product liability insurance market was tight, Congress was successfully lobbied to allow creation of risk retention groups, over-riding anti-competitive state anti-group laws. Personal lines buyers, the American public, are not well-organized and have not overcome such laws.

PATHETIC COMPETITION

Why did pathetic regulation do better than competition? The answer is pathetic competition.

GAO found that "insurance rates in the voluntary private passenger automobile insurance market need not be regulated if there is appropriate action to lessen the current limitations on competition." 21/ The limitations GAO cited included lack of consumer information, prohibitions on group marketing of insurance and allowance of extensive free underwriting periods.

The degree of industry competition is traditionally evaluated in terms of the economic structure, conduct and performance in relevant markets. On each of these scores the property/casualty insurance industry falls short of attaining the status required to justify the conclusion that insurance regulators need not bother regulating in the faith that competition will do that job for them. In this industry, the hand of competition is not merely invisible; in many ways it isn't there.

The degree of real competition in property/casualty insurance, particularly personal lines, is problematical at

21/ Issues and Needed Improvements in State Regulation of the Insurance Business, op. cit.

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best. Substantial factors, common in most states, run strongly against the heroic conclusion that competition provides consumers with sufficient protection from excessive rates, as Chart #3 demonstrates. In particular:

- Price-fixing beyond that considered advisable by the NAIC continues to be permitted in most states, and price-fixing beyond the limit found appropriate without further inquiry by the National Commission for Review of Anti-Trust Laws and Procedures is permitted in all states. I will discuss these rate activities in a moment in detail.

- Market allocation agreements for which there is no economic justification are tolerated. For example, the AAA's insurance company in Southern California does not venture into the territory of Northern California where the AAA of Northern California operates an insurer.

- In all states, laws permit private restraints on private competition by permitting resale price maintenance. 22/ Under these "anti-rebate" statutes, the retail (agent's) price is set by the wholesaler (insurance company). Thus, if you decide to buy your insurance from the Hartford Insurance Company, no matter which agent for Hartford you choose, you will pay the same price. If an efficient agent chooses to compete for market share by lowering his price by cutting commission, he or she cannot do so. This practice is precisely like the old fair trade law days which this nation outlawed years ago.

- The potential for downward pressure on prices is siphoned off into non-price channels such as relaxed underwriting standards which enhance carrier revenues and assets rather than reducing policy-holder costs. 23/

22/ Only last month a Florida court overturned the state anti-rebate statute. See National Underwriter, Property/Casualty Edition, August 24, 1984.

23/ See the report, Full Insurance Availability, Federal Insurance Administration, 1974. This gives an excellent overview of the devastating nature of underwriting in thwarting competition. "Underwriting" is the practice whereby an insurance company decides whether or not to insure a specific risk. When properly done, for cause such as claims, it is a proper practice. When done for gender, racial (i.e., redlining), occupational or other such purposes, it is inappropriate.

> In this way consumers get little or no benefit, while their lack of market sophistication and the threat of coverage denial or cancellation stultifies willingness to shop for the best price.

This conduct occurs in insurance markets that are not properly structured for or amenable to competition in the first place:

- o Although comprehensive, understandable and accurate comparative price and product information is an essential precondition for effective price competition, most consumers, especially in personal lines markets, are disadvantaged by inadequate information.
- o Personal lines markets are increasingly and now significantly concentrated in most states, with a small number of firms enjoying a dominant market share.
- o "Entry barriers" for nationwide direct writers are high, muting competitive pressure where competition could otherwise be possible. The direct writers, we find, are the real price competition, with roughly a ten point expense advantage. Lack of entry here really hurts meaningful competition. Where entry barriers are low for the agency writing segment of the industry, competitive potential is crippled by anti-rebate statutes, rate bureaus and other factors that inhibit lower prices for consumers.
- o State laws often impede competition in other ways, such as by prohibiting true group underwriting, and by requiring all firms to share losses though guaranty funds if any carrier fails.

For a full discussion of all of these anti-competitive structural problems and practices, I have attached Chapter 4 of a study I undertook with John Wilson. 24/

24/ Investment Income and Profitability in Property/Casualty Insurance Ratemaking, op. cit.

RATE BUREAUS

As you requested, I will focus my attention on rate bureaus, surely the primary impediment to personal lines competition.

"Cartel" is defined as "a combination of independent commercial enterprises designed to limit competition." 25/ Surely rate bureaus qualify to be called cartels.

The National Council on Compensation Insurance is classic in its cartel structure; its Constitution bluntly states:

> Each member shall adhere to all filings made by the National Council on its behalf with state supervisory authorities, except to the extent that such members shall obtain the right to depart from such filings in accordance with the requirements of law specifically applicable thereto or the applicable law precludes, either directly or indirectly, agreements to adhere . . .

No wonder that, in those states that have gone to open competition and freed the companies from the NCCI, rates have drastically fallen.

The Insurance Services Office Certification of Incorporation does not have an adherence requirement. Indeed, it states:

> No insurer shall be required, as a condition of membership . . . to charge those rates or use those rules or forms that are recommended by the corporation.

Nice words, but the practices in which ISO engages tilt strongly in a contrary direction:

25/ Webster's New Collegiate Dictionary.

1. They publish premium comparisons in each state for the major lines of insurance, but they make such information available only to insurance companies. 26/ I am advised that this practice would be illegal, if it were not for the McCarran-Ferguson Act, in that it is an anti-competitive practice.

2. Final prices are filed on behalf of "rival" sellers in about half of the states. Competition is significantly reduced thereby.

3. In other states, the rate bureau may establish either an advisory pure premium (that is the "loss cost" or loss and loss adjustment part of the rate) and/or the advisory rate is set absent any insurer committee oversight. In the former case, the ISO establishes about two-thirds of the final rate, making very significant joint actuarial judgments on such matters as data base, trend and projection for inflation and frequency, loss development and loss adjustment expenses. Further, it is a simple step to calculate a final ISO rate when one knows (as all the insurers do) the countrywide ISO expenses and the ISO profit factor of 5%. Thus, the cartel still functions at near full efficiency under the pure premium scenario. In the latter case of staff-only rate development, "the bureau would not necessarily be insulated from anti-trust attack for such activities because its staff had been delegated authority to formulate rates 'independent' of the membership, given the very possible indirect effect of the members' interest on staff decision-making." 27/

26/ In preparation for this hearing, I called ISO and requested a copy of such documents. I was asked if I was an insurance company and, when I said "No", I was informed that the documents are not for sale except to insurance companies.

27/ The Pricing and Marketing of Insurance, Department of Justice, 1977, page 170.

I can tell you that, actuarially, the staff method is not at variance with the committee method in any respect. In all cases I revieved, the staff follows the countrywide formula laid down by the committee. In other words, in setting rates, the staff does not overrule their bosses, who pay their salary.

There is a cancer on insurance; that cancer is the rate bureau, and it is malignant.

The ISO claims to be benign because of independent or deviated pricing and its lack of adherence requirement. This was summarily dismissed by the Justice Department with the statement:

> Nor would the bureau be protected (from anti-trust attack) by the voluntary nature of the arrangement or by the fact that a large proportion of the members priced independently of (or deviated by a fixed percentage from) the bureau rate. 28/

It is small wonder that a State Farm executive recently stated:

> . . . as long as this Achilles' heel of cartel ratemaking continues virtually unmolested, Congress will constantly agitate for re-examining and refining the McCarran-Ferguson Act . . . by any definition, when competitors are permitted to come together and produce an ultimate rate, that is price-fixing and it couldn't be sanctioned in any form under the Sherman Act or Section 5 of the FTC Act. 29/

28/ Ibid.

29/ Statement of Donald P. McHugh, Vice-President and General Counsel, State Farm Insurance Companies, as reported in the Insurance Advocate, June 11, 1983.

It is clear that the rate bureau is intended to lessen competition, giving members a forum for obtaining intimate knowledge of the pricing guidance dispensed to rivals as well as the pricing of competitors, without doing the same for buyers. It is simply wrong to view this industry as a group of unrelated competitors when they proceed to march forth into markets in united cadence to deal with widely separated and unorganized consumers who are often ignorant of the insurance marketplace including the alternatives available.

Pricing data of different kinds are collected and distributed to carriers by rate bureaus for some intended purpose; certainly they must produce some effect on competition. We must start with that proposition because it would not be logical to suppose that the collection and dissemination of data by the industry to its members is an idle exercise. Members of the industry pay for rate bureau services only because they serve a useful commercial purpose. That these activities are currently lawful, of course, does not address their impact on competition. It is all too familiar that an otherwise lawful act can be anti-competitive if it is done in the furtherance of an anti-competitive end. Businessmen do not undertake and stick with costly business activities that have no value. When they act collectively, as in the property/casualty insurance industry through rate bureaus, as though they believe that the activities contribute to market control, it is persuasive evidence that they do.

Whether rate bureaus prepare and promulgate proposed or suggested final rates or stop just short of that ultimate step, merely leading the herd to the trough of rates through the preparation and distribution of "loss cost" only rates, involving uniform data on trending, experience periods, class selection, territories, differentials, etc. -- the detailed underpinnings which permit and encourage consciously parallel "independent" rate determinations -- their anti-competitive impact cannot be construed as small.

This does not mean that all potential rate bureau activities are or ought to be *per se* unlawful. Such organizations, or alternative governmental entities, may be able to perform useful public activities; for example, the dissemination of necessary market information to consumers. Surely small insurance companies need to have access to joint historical experience, but that can be generated by the state or otherwise far short of permitting massive price fixing (for small and/or large insurers).But if we are to rely upon enterprise and competition as the disciplinary forces within our economy, concerted industry action through rate bureaus, particularly in areas related to pricing, is dangerous. If, on the other hand, cooperative endeavors are to exist in the area of pricing (especially pricing guidance), responsibility and authority should go hand in hand. That is, regulatory authorities with ultimate responsiblity to protect consumer interests should exercise control in the ratemaking process.

In practice, although property/casualty insurance rate bureaus are now portrayed by the industry as merely rendering attentive

service to the needs of a competitive marketplace, they actually stifle market rivalry with a suffocating obsequiousness that is characteristic of traditional collective restraints on competitive trade.

That the rate bureau still exercises cartel-like control over personal lines of insurance is clear; from 1980 through late 1983, ISO suggested certain price changes for Commercial lines and Personal lines. The industry adopted something quite at variance with ISO's advice for Commercial lines, but tracked ISO closely for personal lines, viz:

	ISO told co.'s to raise prices by:	Co's actually raised by:	Difference
COMMERCIAL LINES			
Automobile	+40%	0%	40%
General Liability	+12	-15	27
Multi-peril	+30	+ 3	27
PERSONAL LINES			
Automobile	+26%	+21%	5%
Homeowners	+26	+24	2

The cartel is alive and well in personal lines. Whereas the Supreme Court, in the SEUA case 30/, may have found the cartel going 100 MPH in the 25 MPH anti-trust zone, it is now clear that the current cartel is going about 80 MPH in the same zone.

There is little doubt that without the anti-trust exemptions that now belong to this industry by statute, rate bureau trade practices would be viewed as having crossed that fine line that separates collective service to meet public needs from criminal activity.

30/ United States v. Southeastern Underwriter's Ass'n, 322 US 533 (1944).

PRICE FIXING AND TRACKING

To the extent that insurers continue to engage in joint ratemaking, property/casualty insurance markets cannot be viewed as fully competitive. Such joint ratemaking is prohibited as illegal price-fixing for industries not enjoying anti-trust immunity. When Congress expressed its approval of joint ratemaking in its consideration of the McCarran-Ferguson Act, it did so on the understanding that the rates would ultimately be made by state officials or that they would be directly subject to state approval. 31/ This was, of course, the practice contemplated under the original NAIC model rate regulation acts. That is, joint ratemaking was approved exactly because competition was not to be the principal regulator of insurance rates in light of the industry's asserted need to conduct joint activities not permitted under the anti-trust laws.

Such joint ratemaking plainly would violate the anti-trust laws absent legislative protection. Price-fixing among would-be competitors is the most clear and most plainly anti-competitive of antitrust violations. 32/ No explicit or even

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31/ 91 Cong. Rec. 1441, 1485-1486 (statement of Senator O'Mahoney, floor manager).

32/ The Supreme Court's most recent statement respecting price-fixing came in a summary *per curiam* reversal of a decision holding that an agreement among wholesalers not to extend credit to retailers was not price-fixing, that is *per se* illegal. Catalano, Inc. v. Target Sales, Inc., 446 US 643, 646-647 (1980) (an "agreement to fix prices is the archetypal example" of "'certain agreements or practices (that) are so" plainly anti-competitive ". . . that they are conclusively presumed illegal without further examination.'").

implicit agreement to adhere to set prices is required to cross the line between permissible information collection and impermissible price-fixing. 33/ Moreover, because price is he "central nervous system of the economy" 34/ the anti-trust laws have been applied to a wide range of agreements among sellers designed to tamper with price competition, typically by giving sellers detailed knowledge of what their competitors are doing and putting customers at a distinct disadvantage. Even arrangements to share information on a seller-only basis can be *per se* violations of the anti-trust laws because of their effect in dampening price competition. 35/

33/ That question was definitely settled long ago. See, e.g., United States v. Nat'l Ass'n of Real Estate Boards, 339 US 485 (1950). Thus, joint ratemaking in open competition states prohibiting agreements to adhere would enjoy no better standing under the anti-trust laws than joint ratemaking agreements requiring adherence.

34/ Nat'l Society of Professional Engineers v. U.S., 435 US 679, (1978), quoting U.S. v Socony Vacuum Oil Co., 310 US 150, 226 n. 59 (1940); see also NAIC Competition Subcommittee, Report on the NAIC Property and Casualty Model Alternative Competitive Pricing Law (NAIC Alternative Model Act report), 1981-2 Proceedings of the NAIC 353, 362:

> Since price is the single most important factor in the functioning of the market mechanism, the removal of pricing in concert is an essential step in the effectuation of an open competition oriented public policy . . . .

35/ United States v. Container Corp. of America, 393 US 333 (1969); American Column & Lumber Co. v. United States, 257 US 377 (1921); United States v. American Linseed Oil Co., 262 US 371 (1923); Pricing and Marketing of Insurance at 97-118.

The industry has in the past recited a great deal of opinion and anecdotal information to support the claim that joint ratemaking is necessary even in open competition states. But none of those who have studied the matter closely agree, and virtually all would curtail sharply the cooperative activity historically engaged in by rating bureaus, although to somewhat different degrees.

WHAT NEEDS TO BE DONE

The choice is yours -- if you choose regulation, federal standards for quality regulation are essential. If you choose competition, you must eliminate joint ratemaking and adopt federal standards to assure workable competition by outlawing anti-competitive state laws (such as anti-group and anti-rebate laws). NICO encourages you to choose competition, to move America's insurance industry into the mainstream of the American economic system, but either choice will be a vast improvement over today's intolerable situation.

If you choose competition, NICO believes it is imperative that the McCarran-Ferguson Act be repealed and federal standards to assure workable competition will exist be adopted. Of paramount concern would be the creation of a fully competitive environment through elimination of rate bureaus, data collection by the state or its non-industry contractor, full dissemination of such information to small insurers (who need it for ratesetting) and the public, full price and service disclosure, limitations on abusive

underwriting for potential insureds who meet standards of insurability, 36/ requirements for solvency protection that is real and does not interfere with the forces of competition and other standards.

You need no additional lengthy study to know that the McCarran-Ferguson Act is clobbering the public. Everyone 37/ who has independently studied the issue has concluded that the McCarran-Ferguson Act must be repealed or significantly amended. There is no contrary opinion except, as you would expect, those of the members of the cartel themselves.

You know the existence of a cartel costs people money. I have studied hundreds of ISO filings and they always overreach in pricing. They must: what cartel will set a price that makes its least efficient member go under? As State Farm puts it, ". . . the current state-sanctioned joint method of ratesetting which functions in many states weakens the beneficial effect which independent insurers otherwise would have on rates, efficiency and availability. Sheltered by rating bureaus, there is currently limited incentive for many insurers to sharpen their rate structures, pare their costs or seek out new markets . . ." 38/ State Farm thus joined the ranks of those calling for McCarran-Ferguson "reform".

36/ For instance, redlining practices should be outlawed. See Full Insurance Availability, op. cit.

37/ The Federal Trade Commission, the General Accounting Office, the Department of Justice, the National Commission, Professor Joskow, etc., etc.

38/ State Farm Position Paper, An Outline of the Affirmative Case for McCarran-Ferguson Reform and Insurance Rate Deregulation, May, 1979.

Insurance belongs in the free enterprise system. It is time Congress acted to put it there. We would offer any assistance we might be in a position to give in your drafting of the necessary legislation.

Thank you very much.

EXHIBIT I

CALCULATION OF NUMBER OF DAYS
AMERICANS WORK FOR VARIOUS EXPENDITURES

Item	(1) 1983 Amount Spent in Billions(1)	(2) Column (1) ÷ 1983 Disposable Income of $2,335.6 Billion(1)	(3) Column (2) x Number of Working Days
Food	422.5	18.1%	47.1 days
Housing	363.6	15.6	40.6
Personal Income Taxes	289.5	12.4	32.2
INSURANCE(2)	275.4	11.8	30.6
Medical Services	240.4	10.3%	26.8
Household Operations	154.8	6.6	17.2
Motor Vehicles	132.8	5.7	14.8
Clothing and Shoes	125.6	5.4	14.0
Furniture and Appliances	101.6	4.4	11.4
Gas and Oil	90.6	3.9	10.1
Transportation Services	72.9	3.1	8.1
Recreation	52.2	2.2	5.7
Religion and Private Welfare	27.5	1.2	3.1

1. Source: US Department of Commerce, Bureau of Economic Analysis, Telephone Call of January 23, 1984.

2. Source: Best's Management Reports, January 2, 1984, page 1.
1983 Life Insurance Fact Book, page 56.
Blue Cross Association, Telephone Call of January 23, 1984.

EXHIBIT II

FROM

INVESTMENT INCOME AND PROFITABILITY IN PROPERTY/CASUALTY INSURANCE RATEMAKING

An Independent Report

To The

National Association of Insurance Commissioners

Task Force on

Profitability and Investment Income

January 1983

Prepared by

John W. Wilson
J. Robert Hunter

With A Legal Analysis by

Robert A. Jablon
Daniel J. Guttman
Ron M. Landsman

Spiegel & McDiarmid
2600 Virginia Avenue, N.W.
Washington, D.C. 20037

J. W. WILSON & ASSOCIATES, INC.
ECONOMIC COUNSEL
1010 WISCONSIN AVENUE, N.W. • WASHINGTON, DC 20007

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IV. COMPETITION IN THE PROPERTY/CASUALTY INSURANCE INDUSTRY

The degree of industry competition is traditionally evaluated in terms of the economic structure, conduct and performance in relevant markets. On each of these scores the property/casualty insurance industry falls short of attaining the status required to justify the Industry Advisors' conclusion that insurance regulators need not bother giving explicit attention to investment income in the faith that competition will do that job for them. In this industry, the hand of competition is not merely invisible; in many ways it isn't there.

The degree of real competition in property/casualty insurance, particularly personal lines, is problematical at best. Indeed, the prime argument of the Industry Member Advisors, that there is sufficient competition to prevent excessive rates, was not even addressed substantively by the Advisory Committee despite repeated requests to do so. 1/ To the contrary, substantial factors, common in most states, run strongly against the heroic conclusion that competition provides consumers with sufficient protection from excessive rates so that regulators

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1/ See footnote #1 at page 2, above.

simply need not worry about investment income. In particular:

- Price-fixing beyond that considered advisable by the NAIC continues to be permitted in most states, and price-fixing beyond the limit found appropriate without further inquiry by the National Commission for Review of Antitrust Laws and Procedures is permitted in all states.

- Market allocation agreements for which there is no economic justification are tolerated.

- State laws permit private restraints on price competition by permitting resale price maintenance.

- The potential for downward pressure on prices is siphoned off into non-price channels such as relaxed underwriting standards which enhance carrier revenues and assets rather than reducing policyholder costs. In this way consumers get little or no benefit, while their lack of market sophistication and the threat of coverage denial or cancellation stultifies willingness to shop for the best price.

This conduct occurs in insurance markets that are not properly structured for or amenable to competition in the first place:

- Although comprehensive, understandable and accurate comparative price and product information is an essential precondition for effective price competition, most consumers, especially in personal lines markets, are disadvantaged by inadequate information.

- Personal lines markets are increasingly and now significantly concentrated in most states, with a small number of firms enjoying a dominant market share.

- "Entry barriers" for nationwide direct writers are high, muting competitive pressure where competition could otherwise be

possible. Where entry barriers are low for the agency writing segment of the industry, competitive potential is crippled by anti-rebate statutes, rate bureaus and other factors that inhibit lower prices for consumers.

- State laws often impede competition in other ways, such as by prohibiting true group underwriting, and by requiring all firms to share losses through guaranty funds if any carrier fails.

A. INDUSTRY STRUCTURE

Recent decades have brought significant changes in the structure of the property/casualty insurance industry. A small group of large direct writers with nationwide marketing organizations now sells an increasing share of all personal lines coverage in local markets where they are recognized by their fellow underwriters as the price and product leaders. Their relationships with each other are more in the nature of compromise than competition. These large underwriters, even though falling short of being monopolies in a technical sense, are nevertheless able to exert substantial influence over smaller underwriters, would be competitors, and even customers. Because they are large, they have financial resources that enable them to out-bid, out-spend, and even out-lose smaller rivals. They can command the best marketing organizations and financial talents; they can diversify into related financial service areas through congolmerate acquisitions; they can integrate backwards into related investment banking ventures

or forward into complementary retail investment services; in short they can, without breaking the law, free themselves from many of the fortuities of the market. There may be disagreement as to the relevancy of these facts, but few can deny that they are the facts.

1. Market Definition

In evaluating competition in the property/casualty insurance industry, the reliance upon broad national statistics is not meaningful as they fail to fully reflect the importance of individual carrier dominance in the distinct geographic markets that exist in each state.

Because customers currently purchasing personal lines coverage in one state cannot substitute similar coverage purchased from a carrier in another state, the relevant market from the buyers' perspective is statewide at most. 1/

As a general rule, markets must be defined in terms of the meaningful options that are practically and economically available to buyers. Physical similarities between insurance products (e.g., the fact that Company X's automobile policies may read the same in both Minnesota and South Carolina) are

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1/ Studies undertaken by the Federal Government and others indicate that insurance "redlining" denies individuals in some cities any choice at all. See: Meeting The Insurance Crisis of Our Cities - Report by The President's National Advisory Panel (1968), Insurance Crisis in Urban America, U.S. Department of Housing and Urban Development (1978), Insurance Redlining: Fact Not Fiction, U.S. Commission on Human Rights (1979).

meaningless if practical barriers (such as geographic proximity or licensing restrictions) prevent consumers from actually making competitive substitutions. Because of such geographic barriers to substitution, the market for personal lines property and casualty insurance is a local market. Whereas two adjacent towns in a single state, each served by a single agent, might not be deemed to be monopolized markets where practicable economic entry can be easily effectuated from a nearby location, broader geographic distances and the licensing restrictions at state boundaries are significant market entry barriers which invalidate the use of nationwide data as a basis for assessing the degree of market concentration.

The classification of each state as a distinct geographic market also corresponds to "commercial realities" within the industry. In most instances, rate structures separate from those applicable to other states have been proposed by companies and approved by Commissions. Moreover, because claim services (which are, after all, the ultimate product being purchased) must be rendered at a localized point, market realities dictate narrower geographic market definition parameters than those which may be appropriate in industries where transaction points are more flexible.

Indeed, the property/casualty insurance industry's own actions verify the fact that each state is a distinct market.

Rates are prescribed and implemented on a state-by-state or even a community-by-community basis, and it is frequently suggested that profitability should be evaluated on a state-specific basis. Rational businessmen do not conduct their affairs in ways that are pointless. The fact that the property/casualty industry manages its pricing and other practices as though it believes that it operates in individual state markets is substantial evidence that it does. The industry's own business conduct in this regard is a significant factor in concluding that markets cannot be defined more broadly than the state level.

When measured by traditional tests, the structure of the property/casualty insurance industry cannot be described as competitive. These tests include the availability of information for consumers to make meaningful choices among competitors, the level of concentration within the industry, "entry barriers," and "reverse competition." As described below, the available evidence shows that the industry's provision of adequate information to consumers has long been deficient, and that the effect of this deficiency is to impede price competition; that the property/casualty insurance industry is increasingly concentrated; and that it has other structural characteristics inconsistent with workable price competition.

2. Consumer Information.

In its consideration of open competition, the NAIC found that it could not over-emphasize the importance of adequate, detailed price and other information for consumers if competition was to be the regulator of prices. The NAIC Alternative Model Act Report said that "[a]dequate consumer information, including price information, is essential" for open competition, and that it "is a precondition to a reliable competitive market." 1981-1 NAIC Proceedings at 361. 1/

The report of the Task Force to Develop Meaningful Consumer Information on Personal Lines incorporated in the Alternative Model Act Report was, if that were possible, even more emphatic about the importance of consumer information to the operation of competitive systems. It said that a:

> system of price comparison was an essential ingredient of any consumer information activity designed to generate or exert downward competitive pressure on insurance prices. The generation or exertion of such pressure becomes even more important within the context of a rating law which places great reliance on competition as a primary obstacle to excessive consumer prices and is unquestionably necessary with respect to private passenger automobile and dwelling property insurance. (emphasis added)

The NAIC committee reported that fewer than two dozen states had published buyer's guides respecting personal lines

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1/ The Competitive Model Act is an alternative to the Prior Approval Model Act. The Industry Members' Report incorrectly implies that the NAIC's sole position is in favor of the Competitive Model Act.

insurance; it did not report whether any had gone further and developed the kind of price information systems it considered an essential precondition to the operation of a competitive rating system. 1/ See id. at 380-381. Most others who have studied competition in property/casualty insurance come to the same conclusion: better consumer information is a prerequisite for competitive insurance markets. 2/

3. Concentration.

Concentration has been increasing in the property/casualty insurance industry, particularly auto insurance, for at least three decades. After thirty years, the trend has produced the predictable result. Major lines of insurance are far more concentrated than in the 1940's, and many state markets are concentrated at oligopoly levels.

Current data indicate uniformly higher levels of concentration compared to the concentration levels reported a decade ago. As shown below, the 4-firm state market share is significantly higher than 10 years earlier, and most states have 4-firm shares in excess of 50% for one or both auto lines:

Average 4-Firm Concentration Ratios

	Homeowners	Auto Liability	Auto physical damage
1970	32.6%	39.2%	37.8%
1980	43.6%	49.8%	49.5%

1/ To our knowledge, no state fully meets the requirements of the Alternative Model Act.

2/ See Appendix A.

Also, in contrast to circumstances ten years ago, today most homeowners markets and almost all auto markets are sufficiently concentrated to conform to the traditional broad definition of oligopoly: 1/

Number of States With Oligopoly Markets

	Homeowners	Auto Liability	Auto physical damage
1971	16	20	30
1980	38	50	48

Similarly, while there were no states with highly concentrated markets under a more strict test 2/ in 1971, there are now 27 highly concentrated state-product markets; and 12 more are borderline: 3/

1/ Kaysen and Turner have defined an oligopoly market as one where eight firms have 50% of the business, and 20 firms have 75% or more. These are referred to as the eight-and twenty-firm ratios.

The few states not concentrated in auto lines are smaller states where the markets fall short of being concentrated by only slight amounts. Kentucky (phys. dam., 55.5%/74.9%); New Hampshire (liab. 49.0%/80.1%; phys. dam., 46.5%/78.3%); North Carolina (phys. dam. 50.9%/74.6%).

2/ Dr. Willard Mueller defined an oligopoly market as one with four- and eight-firm ratios of 50% and 70%, respectively. Monitoring Competition at 261.

3/ A state is borderline if it falls short of the high concentration boundaries by a total of no more than 2 percentage points (e.g., 48/70, 49/69, or 50/68), so that at present trends it will cross the high concentration line by the end of 1982.

Number of Highly Concentrated States

	Homeowners	Auto Liability	Auto physical damage
1971	0	0	0
1980			
Very High	4	14	9
Borderline	2	5	5

The states that are highly concentrated in both auto lines include a number of major open competition states, such as California, 1/ Michigan, and Virginia.

4. Entry.

Ease of entry in insurance is determined, in part, by the type of marketing that a company intends to employ. There are two major types of firms distinguished by their marketing systems. The "direct writers" sell through employees or exclusive agents; the "agency writers" sell through a system of independent agents. Direct writers have grown over the past 30 years to become dominant in the industry. Entry into the agency writing business is relatively easy, but entry into

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1/ The California data recognize the fact that two major insurers do not compete in each other's territories, and, for competitive purposes, they are treated as one. Even without that adjustment, California is highly concentrated in liability insurance under the strict test (55.0%/70.5%) and almost so for physical damage (55.1%/68.8%).

direct writing is not. Entry barriers are inherent in both the economics of direct writing and in the legal barriers resulting from old common law rules. 1/ Consequently, entry into the dominant part of the industry, the part marked by relatively high concentration for private passenger auto insurance, is not easy.

The ease of entry into agency writing benefits consumers only if new entrants can make their presence felt at the consumer level through price and other competition. To the extent that agency writing companies use or track bureau rates, competition from this segment of the industry is reduced; it is also reduced by resale price maintenance, inadequate consumer information, reverse competition, and investment income underwriting.

5. Reverse Competition.

Reverse competition occurs where sellers compete for the services of the most effective sales agents, typically through

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1/ Direct writing requires an extensive distribution system, whether through employees or exclusive agents, and substantial public name recognition. This all requires substantial initial funding. A legal barrier cited by Joskow is the common law rule that the "property rights" to an insurance customer belong to the agent, not the company, so that an existing agency company cannot move with its existing insureds into the direct writing business. Joskow at 404, citing National Fire Insurance Co. v. Sullard, 89 N.Y.S. 934 (1904). Indeed, the Insurance Company of North America (INA) attempted to enter the direct writing field, but was forced to give up the attempt when its agents threatened retaliation.

higher commissions (which tends to increase prices), rather than competing directly for the business of consumers (commonly through lower prices). This occurs most generally where consumers have relatively little knowledge about the product they are buying. 1/

A study of the independent agent system 2/ confirmed the presence of reverse competition. It found that agents tend to steer their clients to insurers that pay the agents higher commissions. The vast majority of customers who used independent agents relied entirely on the agent for selection of the insurer, 3/ and even where the client expressed a preference, the agent would try to convince the individual to use a different company well over half the time. 4/ Significantly, the study found that

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1/ It is especially severe in insurance markets where the policy is ancillary to a much larger purchase which is the consumer's main concern, such as with consumer loans and credit life insurance on home sales and title insurance, see Pricing and Marketing of Insurance at 254-258. 275-277. It may also occur with life insurance, id. at 280-282. Prudential Insurance Company has testified in several state hearings that it writes very little credit life insurance because other underwriters' offerings are structured to be far more lucrative to the seller. Prudential stated that they were not competitive; their rates were too low to provide for enough commissions to attract lender and car dealer interest.

2/ Cummins, J. David and Weisbart, Steven N., The Impact of Consumer Services on Independent Insurance Agency Performance (IMA Education and Research Foundation, Glenmont, N.Y. 1977).

3/ For roughly 70% of the firms in the survey, at least 94% of the clients expressed no preference. Only about 16% of the agencies reported that more than 10% of their clients expressed a preference for a particular company.

4/ Id. at 59 (Table 3.10).

the leading criteria used by agents to select a company for their clients was which offered the best commission, so long as other factors -- price, service, and coverage -- were "satisfactory". They relied on commission levels in 47.9% of the cases; "best price" was a distant second at 17.2%. 1/

6. Insolvency Funds.

In virtually no other business do competitors collectively guarantee their rivals against insolvency. Insurers do. Through state "guaranty funds" and similar mechanisms, each state provides for a funding arrangement by which all of the insurers doing business in a state, along with certain self-insurers, are compelled to provide the resources to handle claims against an insolvent insurer. 2/ While the ways in which insurers bear these costs and other features vary from state to state, the key element that is common to all is that each company must bear a substantial loss if any one firm actually goes bankrupt. There is no reason from an economic point of view to think these arrangements enhance

1/ Id. at 62 (Table 3.12).

2/ Citations to the statutes as of July 1, 1982, are collected in American Insurance Association, Summary of Selected State Laws and Regulations Relating to Automobile Insurance (1982), Table H, page 82.

competition, and the disincentives to compete aggressively, if that would result in bankrupt rivals, is apparent. 1/

7. Group Underwriting And Marketing.

State laws and regulations also impede competition by prohibiting the underwriting of property/casualty insurance on a group basis. While group insurance is familiar in health and life insurance markets, it is largely absent in property/casualty lines such as private passenger auto and homeowners. Among the reasons for this, are state prohibitions or limitations on group underwriting.

States, by law or regulation, may require all members of the group to have the same risk characteristics, or set minimum group size, minimum percentage participation requirements, or a minimum period of existence. 2/ They may prohibit charging a lower premium to a group member (reflecting the lower expense component) than to a non-group member as "unfairly discriminatory." 3/ Or they may require that the premium rate for an

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1/ This is not to say that there should not be regulatory protection for consumers against insurer insolvency. But while such protection is warranted, it might be structured in a way that better preserves competitive incentives.

2/ These and the following restrictions are summarized in Product Liability Risk Retention Act of 1981, S.Rep.No. 97-172, 97th Cong., 1st Sess. (July 30, 1981), at page 17.

3/ This, for example, is the interpretation of the D.C. Insurance Department of D.C. Code §§ 35-1533. It may be circumvented, at some expense, through creation of a separate subsidiary corporation.

individual in a group be no more than 5% less than that of other individuals, not in the group, with similar risk and similar coverage. And, in some states, employers for employee group plans may be required to obtain a license as an agent to meet state agency licensing laws.

All of these limitations and restrictions restrain potential competition through group underwriting.

B. INDUSTRY CONDUCT

The casualty insurance industry is characterized by practices which are commonly considered to be anticompetitive in other settings. But for the McCarran-Ferguson Act, 15 U.S.C. 1011 *et seq*, which partially exempts the insurance business from application of the antitrust laws, these practices would be of very doubtful legality in the insurance industry as well. Practices traditionally viewed as anticompetitive but which continue to be permitted, and in some cases flourish, include, most prominently: (a) procedures for explicitly or tacitly fixing prices among competing sellers; (b) agreements among sellers not to compete for markets; and (c) agreements between companies and agents that restrict the ability of agents to reduce prices in order to gain sales. Other conduct bearing on competition includes (d) practices designed to avoid competition for marginally attractive sales.

1. Rate Bureaus

In addition to the pervasive and growing impact of the industry's dominant firms, traditional cartel activities continue to stifle the remaining potential outlets for enhanced competitive rivalry. The agenda of rate bureaus does not include supplying information to buyers. The exchange of detailed information and the provision of pricing recommendations is reserved for the benefit of "rival" sellers. In view of the fact that information dissemination is reserved for the bureau's seller-members, it is clear that these efforts, especially pricing guidance, are more essential for cooperative than for competitive market operations. Rate bureaus have not been designed merely to ensure an intelligent and informed business rivalry by which competitive relationships may be established. On the contrary, they involve a cooperative interpretation and dissemination of market data and at least a strong effort at the coordination of market policy designed to bring security and profits to underwriters at the expense of those who purchase coverage. These bureaus provide their members with a forum for obtaining intimate knowledge of the pricing guidance that is dispensed to rival suppliers. It is thus hardly appropriate to view the property/casualty industry as a group of unrelated atomistic competitors when they proceed to march forth into markets in united cadence to deal with widely separated nd unorganized consumers who are frequently

ignorant of the true conditions under which personal lines coverages are sold or the alternatives available to them in the market place.

Pricing data of different kinds are collected and distributed to carriers by rate bureaus for some intended purpose; certainly they must produce some effect on competition. We must start with that proposition because it would not be logical to suppose that the collection and dissemination of data by the industry to its members is an idle exercise. Members of the industry pay for rate bureau services only because they serve a useful commercial purpose. That these activities are lawful, of course, does not address their impact on competition. It is all too familiar that an otherwise lawful act can be anticompetitive if it is done in the furtherance of an anticompetitive end. Businessmen do not undertake and stick with costly business activities that have no value. When they act collectively, as in the property/casualty insurance industry through rate bureaus, as though they believe that these activities contribute to market control, it is persuasive evidence that they do.

Whether rate bureaus prepare and promulgate proposed or suggested final rates or stop just short of that ultimate step, merely leading the herd to the trough of rates through the preparation and distribution of uniform data on trending,

experience periods, class selection, territories, differentials, etc. -- the detailed underpinnings which permit and encourage consciously parallel "independent" rate determinations -- their anticompetitive impact can not be construed as benign. 1/

This does not mean that all potential rate bureau activities are or ought to be *per se* unlawful. Such organizations, or alternative governmental entities, may be able to perform useful public activities; for example, the dissemination of necessary market information to consumers. But if we are to rely upon enterprise and competition as the disciplinary forces within our economy, concerted industry action through rate bureaus, particularly in areas related to pricing, is dangerous. If, on the other hand, cooperative endeavors are to exist in the area of pricing (especially pricing guidance), responsibility and authority should go hand in hand. That is,

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1/ On January 5, 1983, the Insurance Service Office (ISO) issued a press release announcing that it would develop "only prospective loss costs" in competitive rating states, although it would continue to "develop advisory rates" and file rates of behalf of members in non-competitive rating states. While ISO avers that "the insurance industry has always been highly competitive", it further believes that this move "will further stimulate independent pricing decisions." This small step in the right direction is debilitated by ISO's companion announcement that it will determine the "average loss experience...as well as the loss development and trend factors" in these so-called "competitive rating" states.

regulatory authorities with ultimate responsibility to protect consumer interests should exercise control in the ratemaking process. 1/

In practice, although property/casualty insurance rate bureaus are now portrayed by the industry as merely rendering attentive service to the needs of a competitive marketplace, they actually stifle market rivalry with a suffocating obsequiousness that is characteristic of traditional collective restraints on competitive trade. Indeed, there is little doubt that without the antitrust exemptions that now belong to this industry by statute, rate bureau trade practices would be viewed as having crossed that fine line that separates collective service to meet public needs from criminal activity.

2. Conscious Parallelism

Even ignoring the competitive suffocation imposed by the industry's dominant firms and rate bureaus, an unexceptionably salient fact that is totally ignored in the Industry Members' Advisory Report is that the leading property and casualty underwriters have developed among themselves (even through their mutual interests in Advisory Committees) an *esprit de*

1/ Various rating bureaus are clearly cartels in their classic configuration. The National Council on Compensation Insurance, for instance, has rate and rule adherence requirments in its Constitution.

corps, a live-and-let-live code of ethics, commercial interrelationships, intermingled interests through reinsurance, and a spirit of reciprocal recognition of priorities of interest, all of which tend to lessen the vigor of competitive rivalry and to replace that vigor with communal approaches to regulatory and market issues. These arrangements, at times, are as effective as formal cartels in monopolizing markets.

3. Price-Fixing And Tracking.

To the extent that insurers continue to engage in joint ratemaking, property/casualty insurance markets cannot be viewed as fully competitive. Such joint ratemaking is prohibited as illegal price-fixing for industries not enjoying antitrust immunity. When Congress expressed its approval of joint ratemaking in its consideration of the McCarran-Ferguson Act, it did so on the understanding that the rates would ultimately be made by state officials or that they would be directly subject to state approval. 1/ This was, of course, the practice contemplated under the original NAIC model rate regulation acts. That is, joint ratemaking was approved exactly because competition was not to be the principal regulator of insurance rates in light of the industry's asserted need to conduct joint activities not permitted under the antitrust laws.

1/ 91 Cong.Rec. 1441, 1485-1486 (statements of Sen. O'Mahoney, floor manager).

Such joint ratemaking plainly would violate the antitrust laws absent legislative protection. Price-fixing among would-be competitors is the most clear and most plainly anticompetitive of antitrust violations. [1] No explicit or even implicit agreement to adhere to set prices is required to cross the line between permissible information collection and impermissible price-fixing. [2] Moreover, because price is the "central nervous system of the economy" [3] the antitrust laws have been applied to a wide range of agreements among sellers designed to tamper with price competition, typically by giving sellers

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1/ The Supreme Court's most recent statement respecting price-fixing came in a summary per curiam reversal of a decision holding that an agreement among wholesalers not to extend credit to retailers was not price-fixing, that is per se illegal. Catalano, Inc. v. Target Sales, Inc., 446 U.S. 643, 646-647 (1980) (an "agreement to fix prices is the archetypal example" of "'certain agreements or practices [that] are so "plainly anticompetitive" ... that they are conclusively presumed illegal without further examination'").

2/ That question was definitely settled long ago. See, e.g., United States v. Nat'l Ass'n of Real Estate Boards, 339 U.S. 485 (1950). Thus, joint ratemaking in open competition states prohibiting agreements to adhere would enjoy no better standing under the antitrust laws than joint ratemaking agreements requiring adherence.

3/ Nat'l Society of Professional Engineers v. U.S., 435 U.S. 679, (1978), quoting U.S. v. Socony Vacuum Oil Co., 310 U.S. 150, 226 n. 59 (1940); see also NAIC Competition Subcommittee, Report on the NAIC Property and Casualty Model Alternative Competitive Pricing Law (NAIC Alternative Model Act report), 1981-2 Proceedings of the NAIC 353, 362:

> Since price is the single most important factor in the functioning of the market mechanism, the removal of pricing in concert is an essential step in the effectuation of an open competition oriented public policy...

detailed knowledge of what their competitors are doing and putting customers at a distinct disadvantage. Even arrangements to share information on a seller-only basis can be *per se* violations of the antitrust laws because of their effect in dampening price competition. 1/

The industry has in the past recited a great deal of opinion and anecdotal information to support the claim that joint ratemaking is necessary even in open competition states. But none of those who have studied the matter closely agree, and virtually all would curtail sharply the cooperative activity historically engaged in by rating bureaus, although to somewhat different degrees. 2/

4. Horizontal Market Agreements.

Horizontal market allocation agreements have long been held to be *per se* illegal under the antitrust laws because they lack any redeeming economic justification. 3/ Their use in insurance clearly thwarts competitive goals. For example,

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1/ *United States v. Container Corp. of America*, 393 U.S. 333 (1969); *American Column & Lumber Co. v. United States*, 257, U.S. 377 (1921); *United States v. American Linseed Oil Co.*, 262 U.S. 371 (1923); *Pricing and Marketing of Insurance* at 97-118.

2/ See Appendix A for a detailed account of these views.

3/ *United States v. Topco Associates, Inc.*, 405 U.S. 596 (1972), *cited with approval in Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36,57-58, nn. 27, 28 (1972).

direct writers affiliated with the American Automobile Association have operated for many years under an agreement not to compete with each other. 1/ Whether or not such agreements would be actionable under state insurance laws, 2/ or even many state antitrust laws, 3/ they restrain competition with no redeeming economic justification. There are thus no offsetting public benefits for the reduced competition which is the result of agreements such as these.

5. Vertical Price Restraints.

Insurance is the last stronghold of "fair trade" or resale price maintenance laws. State "fair trade" statutes, permitted

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1/ The clubs associated with the principal insurers and their locations are: Automobile Club of Southern California, California State Automobile Association (northern California and Nevada), Automobile Club of Michigan, Automobile Club of Missouri (including parts of Illinois), and the Chicago Motor Club (northern Illinois and Indiana).

2/ Approximately a year ago, the commissioners in California, Michigan and Virginia (where the AAA has its national headquarters), all open competition states, were asked to investigate the legality of the AAA agreement under their laws. Both the California and Michigan commissioners found that they had no power to act against such agreements so long as there was some competition in the state in auto insurance; the Virginia commissioner did not find the activity inappropriate.

3/ The state laws are sometimes read more broadly (to prohibit more conduct or practices) than the Sherman Act, on which they are modeled. Cf. Oakland-Alameda County Builder's Exchange v. F.T. Lothrop Construction Co., 482 P.2d 226, 93 Cal. Rptr. 602 (1971), with Cullum Electric & Mechanical Inc v. Mechancial Contractors Ass'n, 436 F. Supp. 417 (D.S.C. 1976), Aff'd 569 F.2d 82 (4th Cir. 1978).

for some years as an exception to the antitrust laws, authorized manufacturers to set the price at which their goods could be sold at retail. Under such laws, every retailer was required to take the mark-up or commission established by a manufacturer making use of the law, without regard to whether the retailer could sell at a lower price because he was able to cut his cost margin by operating more efficiently or by imposing lower profit requirements. Congress repealed the general authorization for such state laws in 1975, 1/ and in 1980 the Supreme Court held that such state laws authorizing manufacturer determination of wholesale and retail prices for alcoholic beverages, arguably still permitted under the 21st Amendment, were pre-empted under the federal antitrust laws. 2/ Of course, private agreements setting retail prices are similarly illegal. 3/

But, insurers using the independent agency system still continue to enjoy the effect of fair trade laws, whether or not still permitted in light of Midcal, and Group Life and Health Ins. Co. v. Royal Drug Co., 440 U.S. 205, 210, 217, 220-224 (1979). Most states authorize insurers to control

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1/ Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801, amending 15 U.S.C. §§ 1, 45(a).

2/ California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980).

3/ Albrecht v. The Herald Co., 390 U.S. 145 (1961).

retail prices through private agreements by statutes prohibiting "adjustment in premium as an inducement to buy insurance not included in the policy ..." (emphasis added). 1/ An agent otherwise might do this by reducing the price he charges his customers for insurance, in effect taking a lower commission than the insurer provided.

The effect of anti-rebating laws is especially significant given the industry's market structure. It is undisputed that direct writing is concentrated and enjoys consistently high profits. Advocates of competition note that there are numerous agency companies able to compete and that entry into that sector is relatively easy. 2/ But anti-rebate laws dam this potential source of price competition in the marketing stream, for they prohibit effective price competition by agents at the consumer level.

6. Classification And Underwriting Selection.

Classification and selection are the related practices by which insurers seek to "maximize...profits by beating the averages": 3/

1/ Kulp and Hall, Casualty Insurance (4th ed. 1968), at 1023; see also Pricing and Marketing of Insurance at 290.

2/ Joskow at 388-391; Pricing and Marketing of Insurance at 9.

3/ "Presentation on Behalf of the National Association of Insurance Commissioners to the National Commission for the Review of Antitrust Laws and Procedures," July 27, 1978, at page 55; see also Hanson, Jon, "The Interplay of Antitrust, Competition, and State Insurance Regulation on the Business of Insurance," 28 Drake L.Rev. 767, 813 (1979).

> [T]he insurer attempts to write insurance on those insureds in the class whose loss experience the insurer believes will be better than that of the class average. Ultimately, the insured whose loss experience is perceived to be worse than average either will not be able to obtain coverage except through the residual market mechanism or will find himself in a new class which has a higher rate. 1/

The first practice -- seeking out those with below average risk for their class and refusing to insure others -- is underwriting selection or selection competition.

> It is to the insurer's advantage continually to identify those within a class which have better, worse and average perceived loss expectation. The better risks within the class are actively competed for by insurers. 2/

The second practice -- putting those "perceived [by insurers] to be worse than average ... in a new class which has a higher rate" -- is risk classification.

Successful selection competition does not reflect efficiency in the familiar economic sense of producing a good or service at lower costs. The costs in question are losses that will occur in any event. The effect of selection competition is not to reduce those losses, but rather to shift them around, either from one insurer to another, or from auto insurers to the person who could not obtain coverage, his or her victims, or their insurers. This fact, unique to insurance, was one of

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1/ NAIC Presentation at 55-56; Hanson at 813.

2/ Id.

the reasons Congress elected to partially exempt insurance from the antitrust laws in the first place. 1/

But, selection competition between insurers does not necessarily lead to enhanced competitive market alternatives for customers. Indeed, those customers whose underwriting risks are perceived to be relatively high (because of their track record, or where they live, or their economic or demographic condition, or otherwise) are often left in a considerably less competitive environment. Although even the industry has acknowledged that the high risk segment of personal lines property/casualty markets is not competitive, 2/ the Industry Members of the Advisory Committee chose to ignore this significant contingent of policyholders in concluding that investment income was not worthy of explicit regulatory recogni-

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1/ The theory of insurance is the distribution of risk according to hazard, experience, and the laws of averages. These factors are not within the control of insuring companies in the sense that the producer or manufacturer may control cost factors.

H.R. Rep. No. 873, 81st Cong., 1st Sess. 8-9 (1943), quoted in Royal Drug, supra at p. 22, 440 U.S. at 221.

2/ See the Report of the Advisory Committee on Competitive Rating in Residual Markets "not subject to competition." In addition to the high risk markets that are created by selection competition, few would deny that title insurance, credit insurance and workers compensation insurance (where cartelized adherence to standard rates is required) are noncompetitively priced lines. NAIC proceedings -- 1980, Vol. II, p. 431.

tion in ratemaking. Since these high risk markets are admitedly not workably competitive and since they too generate substantial investment income, it seems unexceptionably clear that the explicit inclusion of investment income is essential in regulating rates that are applicable in these markets in all states.

7. Investment Income Underwriting

Investment earnings are now the sole source of net income for the property/casualty business as a whole, and for most property/casualty insurance lines. 1/ In theory, high investment income could translate into lower rates for insurance coverage if carriers competed with each other by reducing prices as investment earnings increased. But that has not happened in personal lines markets where consumers have, instead, been treated to the industry's alternative, two-pronged response to rising investment income. The first pronging is

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1/ In 1981, all but two of the 25 largest groups recorded underwriting losses, yet they had good overall results because of record high investment income. Investment income has been the main source of income for the industry since the mid-1950s, but the gap between investment earnings and underwriting profits (or losses) has grown sharply since 1978., See William Kinder, "A Look at the Leaders: Why Worry About Underwriting Profits?" Best's Review, September 1982, at 16, 18 (Exh. 2), 123 (Exh. 5)

The Insurance Services Offices reports the same; see ISO, "The Road Ahead: A Commentary on the State of the Property-Liability Insurance Industry", at 9 (undated but with mid-1982 data) ("Investment income has become the only source of industry profit").

that, rather than cutting prices to existing policyholders, carriers have relaxed underwriting standards in order to attract more premiums and add further to their lucrative investments. The second is that investment income from personal lines coverages has been used to offset premium requirements in commercial lines where greater customer knowledge and buying power have extracted price concessions not offered to smaller personal lines accounts. 1/

As a result of reduced underwriting standards, there have been carrier-imposed cross subsidies from low risk to high risk customers. This tactical response to rising investment income is apparently preferred to rate reductions in the personal lines property/casualty market environment because it permits carrier growth and increases carrier assets and revenues rather than reducing the firm's revenue and asset size as would occur if underwriting standards were maintained and competitive price cuts were instituted to the extent permitted by

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1/ See, for example, the very recent (January 13, 1983) Wall Street Journal account of this practice which states:

> NEW YORK -- Prepare to pay higher premiums for automobile and homeowners insurance.
>
> Property and casualty insurance companies, facing sharply rising underwriting losses on commercial insurance policies, plan to boost rates for personal insurance customers...

investment income gains. The fact that carriers have responded to investment income gains in personal lines markets through non-price rivalry, is one clear signal that carrier competition is not sufficiently structured to best serve all customers' economic interests.

Likewise, although private passenger automobile premiums have kept pace with ISO advisory rate increases (which do not factor in current investment income) the premium growth for commercial auto has been far below the recommended ISO rate increases. In "The Road Ahead", ISO reported that commercial premium growth lagged 35% behind bureau-advised rate increases, but subsequently the ISO also reported that private passenger automobile rates stayed remarkably in step with bureau advice. Specifically, according to ISO, the following occurred during 1980, 1981 and the first half of 1982: 1/

	Written Premium Effect of Advisory Rate Level Charges	Actual Industry Premium Growth	Difference
Commercial Automobile	+36.5%	+1.8%	(34.7%)
General Liability	+10.1%	-12.6%	(22.7%)
Commercial Multi-Peril	+22.7%	+5.1%	(17.6%)
Private Passenger Auto	+22.5%	+21.2%	(1.3%)

1/ Correspondence with Mr. David E. Ostwald, V.P., Corporate Communications of ISO. The CMP data include the effect of rating programs. For private passenger auto, rating programs impacts are estimated by ISO to be "2% for 1980, 3% for 1981 and 3 1/2% for 1982... These rating programs apply only to physical-damage coverages" (Letter of December 30, 1982).

Clearly serious questions of cross subsidy from small, manually rated insureds to larger accounts exist. Even if it could be shown that commercial lines competition reduced the overall profit levels of property/casualty carriers to a fair level (an industry argument that is not borne out by the facts), the resolution of unfair and discriminatory anticompetitive practices in personal lines markets would still require regulatory rate action providing for the explicit recognition of investment income in personal lines markets. 1/

The problem can be stated as follows: If the investment income associated with personal lines customers paying manual rates, with a built-in standard underwriting margin, is used to subsidize large accounts not paying manual rates and enjoying what the industry calls "cut throat" competition, the need for regulatory concern about who gets the benefit of personal lines investment income is obvious.

During the course of the Advisory Committee's deliberations, Mr. E. McAlenney of Conning and Company, a consultant hired by the Industry, advised the Committee that competition was greater in commercial lines of insurance than in personal lines. Evidence of this appeared in a front page article in the National Underwriter on November 20, 1981:

1/ All state laws require that the regulatory authority assure that rates be "not unfairly discriminatory."

> A large commercial umbrella risk came up for renewal and was rated at $105,000, about the same as the previous year. But the insured was not satisfied. Aware of the aggressive rate competition in the commercial lines market today, he decided to shop around. He approached a second agent, who submitted the very same risk to a different company, which offered to write it for just $20,000.
>
> But the insured was still not happy. He continued shopping and eventually the original company, which initially wanted $105,000 came back and took the business for $5,000. That's right $5,000. (emphasis added)

The authors of this Report were unable to find examples of personal lines auto or homeowners customers getting similar competitive market benefits.

Further, Robert A. Bailey, writing for Bests' Insurance Damages Reports said on December 6, 1982:

> while this industry aggregate is profitable, those profits are not evenly spread. The premium growth this year comes entirely from personal lines. Commercial lines premium is flat. Consequently, results for commercial lines are deteriorating much more seriously. Expense ratios, while relatively flat in personal lines for the past five years, have risen substantially for commercial lines and continue to do so. (emphasis added)

In the January 4, 1982 issue of Bests' Insurance Management Reports, it was stated:

> private passenger constitutes approximately 82% of the total auto value and commercial 18%, but the 10 year aggregate loss of $7.3 billion belongs 75% with private passenger and 25% with commercial, showing that commercial is doing more than its share in pushing up the loss ratios. In 1981 commercial business is estimated to have produced a combined ratio of 110% vs 105.71% for private passenger business and commercial had the greater rise in loss ratio.

These figures were subsequently updated in the January 3, 1983 issue of Bests' Insurance Management Review to show that in 1981 commercial business actually produced a combined ratio of 111.68% vs 105.35% for private passenger and, further, that the 1982 estimates were 118.87 for commercial and 107.37 for private. These figures are clearly inconsistent with the apparent conclusion of the Industry Members' Advisory Report that personal lines customers' interests in investment income are adequately protected by competitive market forces, so that regulators need not even concern themselves with the matter.

Consumers of personal lines insurance coverage have thus been deprived of the full potential benefits of price competition as investment income has risen in the property/casualty insurance industry. Enriched by growing investment income, carriers have generally elected to relax underwriting standards and subsidize commercial markets. This has fostered premium and investment portfolio growth rather than passing through the benefits of growing investment income to low risk personal lines customers.

Underwriting selection has also intimidated or discouraged price shopping by consumers, muting the principal source of competitive pressure for lower rates. Faced with uncertainty over the effect of claims on cancellation or non-renewal, and arguably relying on the premise (whether or not correct) that

an insurer is less likely to cancel an old customer than a new one, consumers simply elect not to shop competitively for insurance. 1/

C. PERFORMANCE

In view of the property/casualty industry's market structure and conduct, it is not surprising to observe that its performance also lacks important competitive characteristics. In industries where market performance is competitive, the typical end result is efficient and independent sellers offering more and better products at lower prices to consumers.

The Industry Members' Advisory Report mistakenly identifies the industry's investment income underwriting practices, which voluntarily reduce underwriting income in order to maximize premiums written and investment income, as clear evidence of workably competitive market performance. While investment income underwriting is a type of rivalry between sellers, it is clearly not the type of meaningful price or product competition that provides protection and benefits to the typical personal

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1/ Indeed, the Massachusetts Commissioner found, based on record evidence, that these fears were well-founded; and that disproportionate percentages of insureds who changed companies ended up in the high-priced assigned risk plan. "In this matter, companies apparently frustrated the shopping desires of [those] who attempted to switch." Operation of Competition Among Motor Vehicle Insurers (1977, at pages 50-56.

lines customer. Whereas a typical buyer of personal lines coverage would like to see his rates fall when investment income rises (as, no doubt, he would in a market that were really workably competitive), that is not what typically happens in the property/casualty insurance industry. Instead, rate levels are typically maintained (or, even raised) 1/, and the carriers' investment income windfall is used for a combination of other objectives including: higher equity returns (in the case of stock companies), reduced underwriting restrictions (so as to attract more funds for investment purposes), investment portfolio growth, and cross subsidies to commercial lines where buyer savvy and more meaningful market options mandate a higher level of price responsiveness. For the typical personal lines customer, insult is then often added to injury when these carrier maneuverings to exploit investment income potential produce the expected underwriting profit reductions and those reductions then serve as an unwarranted rationalization for further rate increases.

Thus, despite the illusion of competition that is created by lower underwriting income in periods of high investment income, regulators and the public should not be lulled by the

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1/ See footnote 1, page 67.

industry into a complacent acceptance of the false argument that lower underwriting returns, under these conditions, are a manifestation of workable price competition between property/ casualty underwriters in personal lines markets.

As will be shown in more detail in Chapter VII, below, total returns in the property/casualty insurance industry have been in excess of the market cost of capital. While this fact is consistent with the conclusion that the industry, as it is presently structured and operates, is not adequately competitive, it should be noted that even if profits were genuinely not excessive, that fact alone would throw no light on the fundamental question: Have these profit results been compelled by a competitive system or do they simply represent the dispensations of shrewd management which, with wide discretionary latitude at its disposal, decided for the time being to "play it smart" in view of the potential regulatory consequences. 1/

1/ Monopoly rents need not show up in profits. They can manifest themselves in excessive expenses and other inefficiencies. In Invisable Bankers, Linden Press, 1982, Andrew Tobias finds that insurers are grossly inefficient.

D. CONCLUSION

The Industry Members of the Advisory Committee have declared that property/casualty insurance markets are competitive. From that foundation they reason that regulation is unwarranted and unnecessary -- so why should regulators concern themselves any further with the stormy issue of investment income? The answer is written:

> ...a wise man built his house on the rock. The rain came down, the stream rose and the winds blew and beat against the house; yet it did not fall, because it had its foundation on the rock...a foolish man built his house on sand. The rain came down, the streams rose and the winds blew and beat against the house, and it fell with a great crash 1/

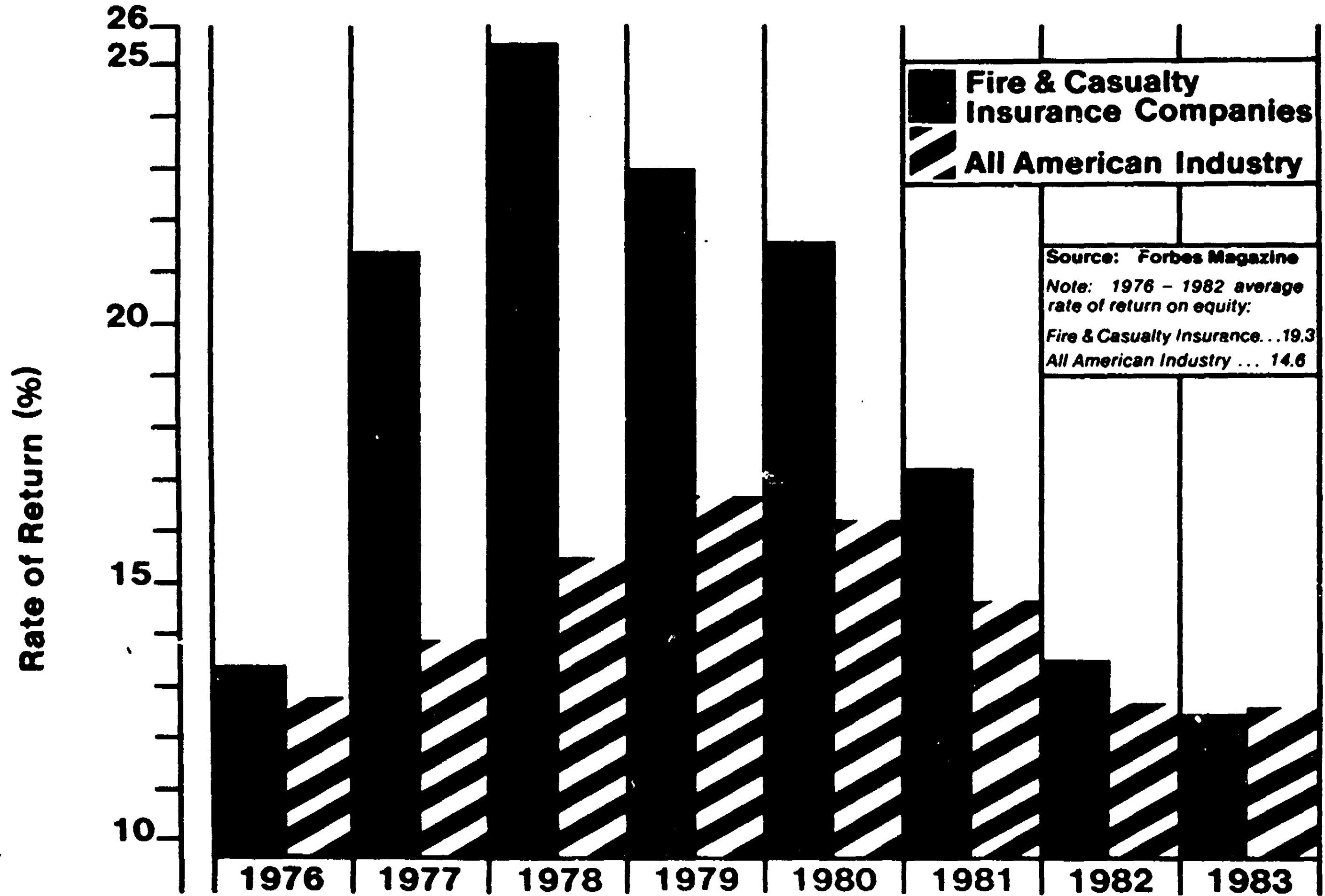
"Have faith," chant the industry's visionaries, "and behold the rock of competition."

"Dispense," they shout, "with your needless cares about investment income."

But the vision is made of sandier stuff.

1/ Matthew 7:24-27

CHART No. 1



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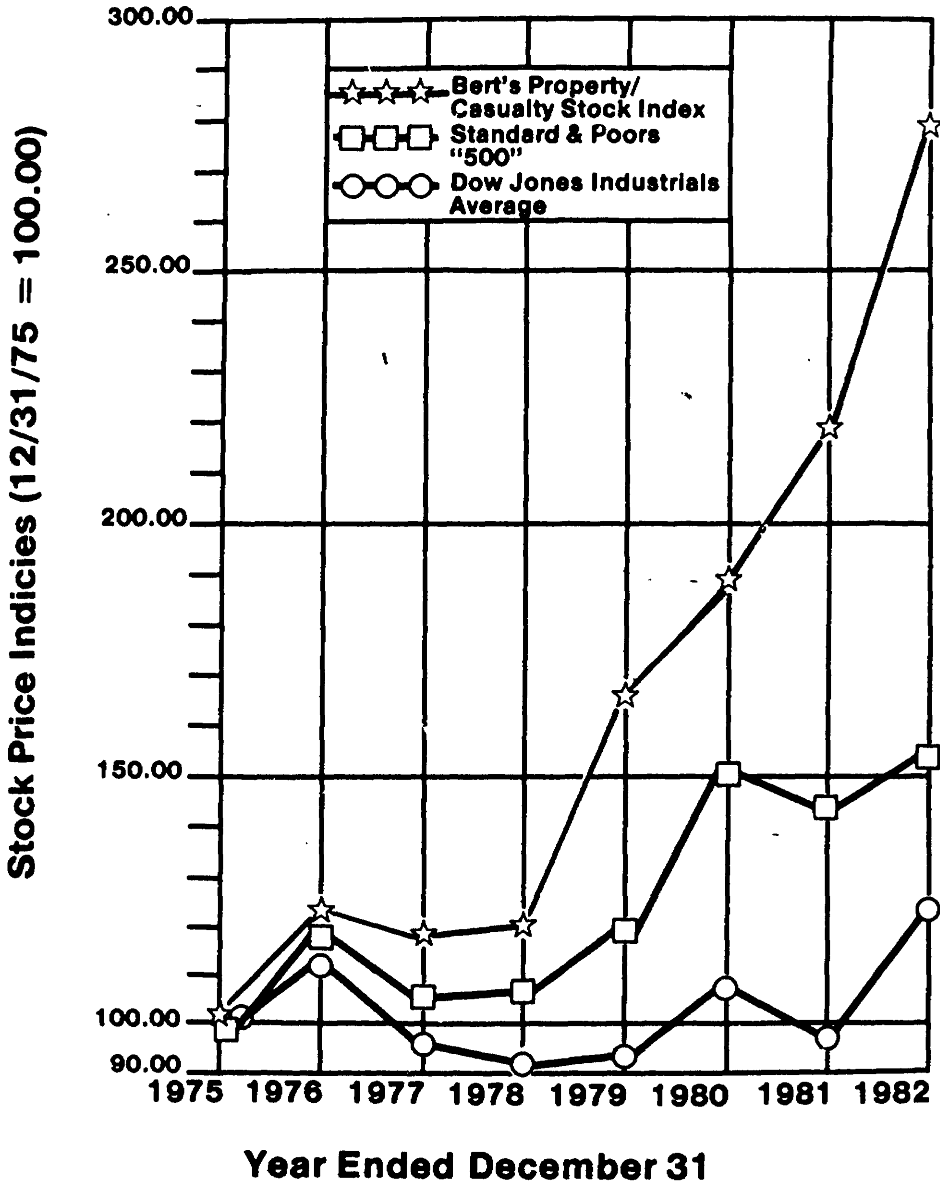

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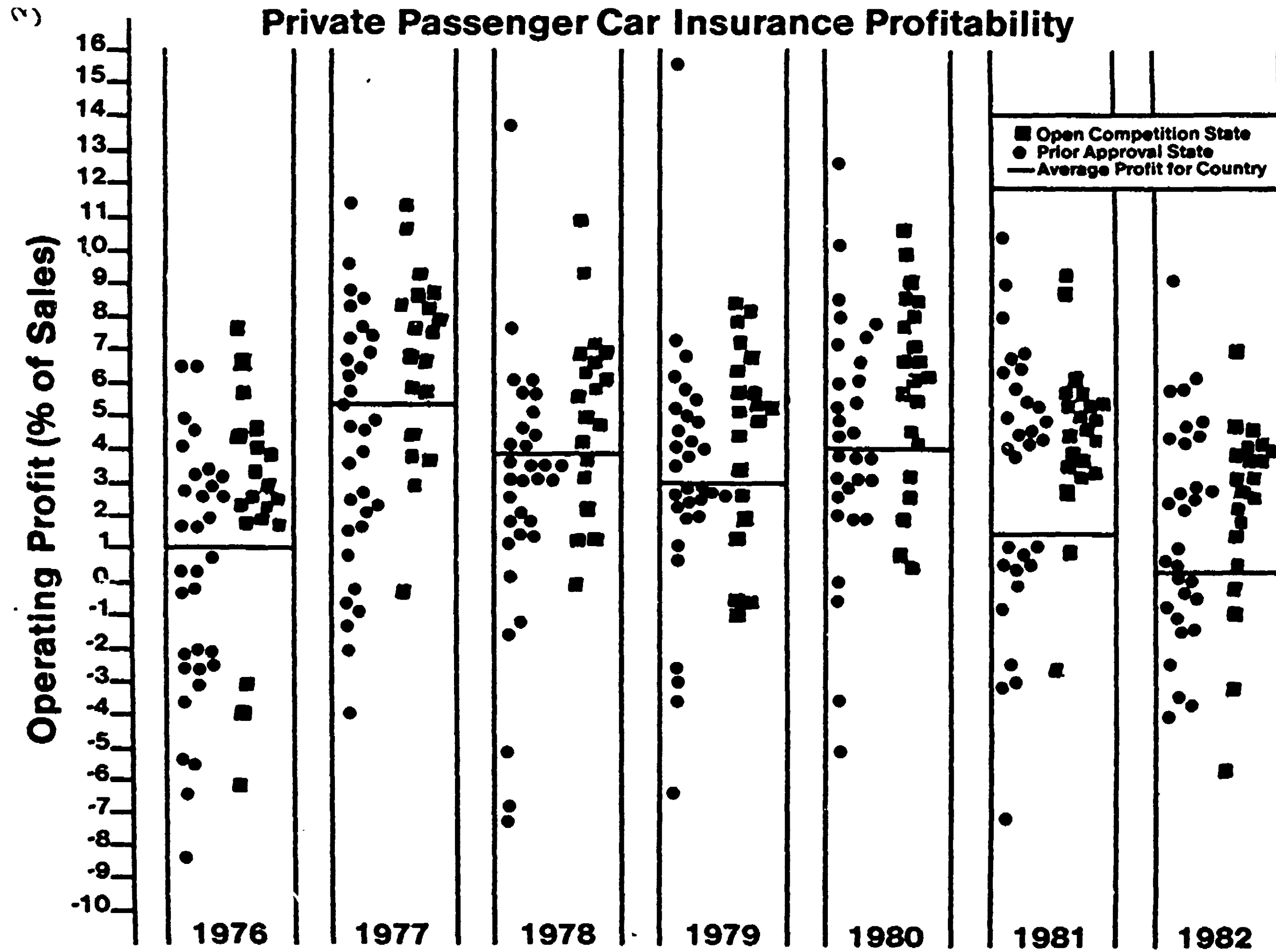

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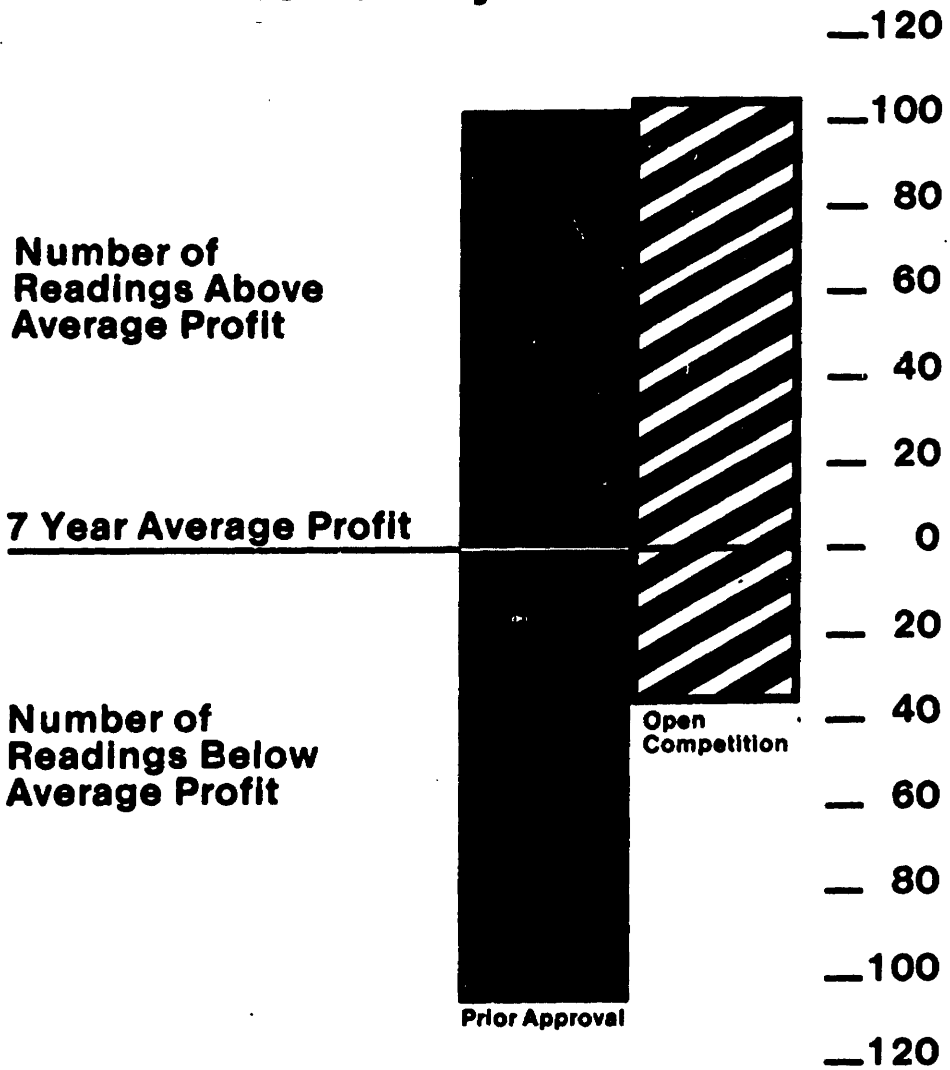
CHART No. 4



Chairman RODINO. Thank you.

Mr. Wilson.

Mr. WILSON. Mr. Chairman, Mr. Edwards, it's nice to see both of you again.

On several previous appearances before this committee, we discussed anticompetitive problems in the petroleum industry, and I would just like to draw a parallel that I think is an important one between some of the problems that you've recognized in that industry previously and some that exist in insurance.

The petroleum industry, I've always stressed to this committee, has the problem of joint ventures at the production level that impede what could otherwise be a great deal of potential competition between a large number of producers of oil and natural gas.

The same type of joint activity takes place within the insurance industry, but it's even worse because of the antitrust exemption that exists.

There certainly is the structural potential, with a large number of insurers, to have a competitive environment in many lines in many markets, but the joint rate-making activity and other joint activities that are engaged in by insurers, as protected under the McCarran-Ferguson exemption, inhibits that potential from being realized.

Another similarity that you have to deal with, and I think we should be aware of, is the tremendous political power that both of these industries have. Legislation that has favored the insurance industry has been promoted and has been sustained at the State and Federal levels for decades, and it's related to the political power that the industry has, which is sometimes overlooked.

When you look at lists of the top corporations in the United States in the past before the AT&T divestiture, you had AT&T on top, and then you had your Exxons and your General Motors and so on.

The fact is that there are insurance companies that are bigger than the largest corporations in the United States. They're not included in those lists because they are not corporations; they are mutual firms. Prudential is substantially larger than AT&T was before the divestiture.

Large firms like State Farm that have dominance in many markets in products such as homeowners and automobile have similar types of market power, and it's a type of market power that is substantially unrestrained and a type of political power that is substantially unrestrained by the regulatory process.

When State regulatory commissions in California or New Jersey regulate companies like PG&E—Public Service Electric and Gas—they ride close herd on the expenditures of those companies, particularly expenditures that are made for the interests of the owners of the firm, such as lobbying expenditures, expenditures that are made to influence legislation, and other types of activities at the State and Federal level. That type of activity is not prohibited, but if it's engaged in by a regulated firm in the utility industry, it's disallowed for rate-making purposes.

There is no such scrutiny or regulation or expense disallowance, that I'm aware of, in any jurisdiction in the United States when it comes to insurance.

So we have parallels, and many of the problems are the same.

I might mention another parallel which Bob Hunter's comments brought to mind. I think the last time I appeared before Mr. Edwards, we were talking about competitive problems in telecommunications, and this was before the AT&T divestiture.

One of the serious problems that existed in telecommunications was the cross subsidies that took place between noncompetitive markets in which the Bell System had monopoly control and competitive markets, such as terminal equipment, where they were attempting to engage in competitive activities vis-a-vis independent rivals. There were tremendous amounts of funds which, of course, the Justice Department and Judge Greene were concerned about, that were flowing from the monopoly areas to cross subsidize the competitive areas. You have that type of parallel in insurance as well.

The profitability, particularly the investment income profitability, that is obtained by insurance companies in personal lines markets, such as private passenger automobile and homeowners insurance, is used by these diversified property and casualty companies to cross subsidize many of their commercial underwriting activities.

The problem isn't that the regulatory control is different in the different markets, but the level of consumer sophistication is drastically different.

The commercial buyer has a great deal of sophistication and is capable of evaluating and playing off various underwriters in the purchase of commercial lines of insurance.

The private purchaser of automobile insurance or homeowners insurance doesn't have the sophistication and doesn't have the economic motivation as an individual to get the type of counsel and get the type of expertise that is necessary in order to make a potentially competitive system work.

So many of the problems that you've confronted in other industries—economic problems, regulatory problems, political problems—are transferred to the insurance industry; they exist here too, but they are substantially more serious because of the antitrust exemption that exists.

I'm going to briefly summarize the formal statement that I've presented; I'm not going to attempt to read it to you.

I would like to mention that along with the statement, I've submitted for the committee's interest, a study that Robert Hunter and I performed last year on insurance ratemaking.

[Study on file with the subcommittee or available from J.W. Wilson Assoc., 1010 Wisconsin Ave. NW., Washington, DC 20007, 202-333-7442.]

Mr. Wilson. I'd like to, in particular, recommend chapter 4 of that study, which deals extensively with competition issues that are of concern to the committee, and there's an excellent legal appendix in that study that was prepared by some lawyers who were associates of ours in the preparation of it, and I think that would be interesting, too.

Property/casualty insurance is characterized by practices that are commonly considered to be anticompetitive in other settings. But for McCarran-Ferguson, these practices would be illegal in the insurance industry as well. They include procedures for price fixing, agreements among sellers not to compete, resale price maintenance, and agreements to avoid competitive activities for marginally attractive sales.

Recent decades have brought significant changes in the structure of the property/casualty insurance industry. A small group of large writers with nationwide marketing organizations now sells an increasing share of all personal lines coverage, and they are recognized as the price and product leaders in the markets where they operate. Their relationships with each other in personal lines markets are more in the nature of compromise than competition.

One test of seller competition in any industry or market is whether there is a sufficient number of truly independent—and I emphasize independent—sellers in that market to preclude excessive seller influence. The emphasis on independent can't be overstressed. If you simply have a large head count but the firms function together, you are not going to have a competitive end result.

There is an absence of adequate competition when, as in the insurance industry, sellers are able to exercise discretion in establishing prices, and this is a discretion that is permitted under McCarran-Ferguson on a joint basis.

Where firms have such latitude, they possess excessive market power, and the outcome of such a free market, if it is unregulated, is monopolistic rather than competitive.

Although insurance regulators must be concerned about a number of diverse regulatory issues, certainly the regulation of rates is the major problem.

While the imposition of economic regulation is necessary to protect pubiic interests in industries or market circumstances where the forces of competition alone are not sufficiently strong, the remaining complementary role of competition should not be ignored.

Here's at least a difference in emphasis between some of the things that Bob said and something that I feel very strongly about. I'm not sure we have a substantive difference here, whether it's a difference in focus, but I would urge the committee that it's important to recognize that in most cases, including the insurance industry, it is not really a question of choosing between regulation and competition. Instead, competition can be made to serve as an integral and complementary force within a regulatory framework.

Arguments that antitrust goals should be subordinated to the goals of regulation or that deregulation should follow where regulated industries have not obtained optimal performance records, I think, miss the point.

The goals of regulation and competition are not mutually exclusive. Where the two forces can complement each other, the mutual objective can be better obtained, and we can see that course of action taking place in other regulated industries.

Telecommunications is an example. Electric utility operations and competition between public systems and private systems and between investor-owned utilities for industrial loads is an excellent example of the type of competition that is possible within a regula-

tory framework. I think the potential in insurance is much more so on the competitive side than in many of your traditional utility-type regulated industries.

Insurers have questioned the need for detailed control of rates on grounds that regulated insurance companies find it in their own interests to hold expenses and rates to the minimum level, but that's not likely and it's not the fact where, as in personal lines property/casualty insurance, cooperatively inclined sellers move toward the mutual pursuit of collective interests unencumbered by antitrust restraints.

Moreover, in companies where there is little direct ownership control—that is the other type of discipline—the discipline imposed by the stockholder is absent in many of the largest firms in this industry, especially the mutual insurance companies, and the managements of these firms can derive substantial personal gain without significant owner-imposed restrictions.

Diversified corporate entities that have substantial holdings in the insurance industry—and that's becoming more and more of a problem as insurance companies expand into various related lines—can achieve large private profits by requiring their insurance and noninsurance affiliates to engage in highly lucrative transactions with each other.

To guard against the likely consumer abuse, the expenses of insurance company operations should be examined in detail by regulatory authorities. But in practice, insurance regulators have not been vigorous in controlling insurer costs. Regulators have also tended to accept significant rate discounts for large commercial lines accounts.

These failures can be attributed to three main causes. First, insurance commissioners have been compelled by an industry they regulate and by their lack of resources, which is a very serious problem, to devote most of their energy to the struggle over the level of profitability, and they've had little time, energy, or resources left to spend in the interests of reforming cost allocation or improving expense controls.

Second, they have been deceived by methods of accounting that are employed to obscure cross subsidies and justify discrimination; and, third, they have been deterred from overhauling the structure of the insurance industry and its ratemaking by the fact that many of its parts have become so deeply embedded in established tradition.

I'd like to emphasize that there are major steps in some States, that I'm aware of, that are moving in the direction of rectifying that problem, and New Jersey under the leadership of Commissioner Rodriguez on consumer affairs, and the new insurance commissioner, Mr. Merin, I think, shows great promise in that regard.

If they get the resources and if they get the political support and the legislative support that's necessary to do the job, I think those are the kinds of people that will, and with their resources and with those kinds of public servants pursuing consumer interests at the State level with Federal support, I think that a much more significant contribution can be made by competition.

I've put figures into my testimony on concentration, showing how concentration has increased in the industry in recent years.

I'm going to skip over that, both because I suspect you are familiar with the figures and because the question of concentration is not the significant issue in assessing insurance competition; it's the institutional setting, the direct evidence of market independence, the rate bureaus, the collective activities that are the critical considerations.

Concentration, after all—I guess all economists and certainly members of legislatures who deal with antitrust matters are aware—means virtually nothing in and of itself. It's an important measure only in that it infers something about something else, and let me be specific about that, because it's very important.

As I said previously, whether or not there is competition depends on whether there is an adequate number of truly independent, self-motivated sellers. Independence is the key. Without independence, self-motivation will bind sellers together in the mutual pursuit of common objectives at the expense of consumers.

That's the problem with concentration ratios. They suggest that there are large numbers of sellers and that concentration is not dramatically high, but if you look beyond the concentration ratios to the direct evidence of mutual interdependence through rate bureaus that is achieved under the auspices of the antitrust exemption, you'll find that the potential for competition is being thwarted.

In conclusion, let me say that I have several recommendations, the first of which is that the insurance industry is potentially workably competitive, but to get it there, the antitrust exemption has to be removed. At the same time, steps should be taken to improve regulation.

Even with the repeal of McCarran-Ferguson, no one familiar with our antitrust track record could be overly optimistic about the outcome without some new manifestation of the strongest possible congressional support. In short, antitrust itself, given the level of enforcement that exists, is not the answer.

The industry is not competitive, present regulation is not working well, there are ways in which competition can be increased, and there are also ways of improving regulation.

There are two solutions that are clearly bad. One would be continuing as is, without recognizing the need for change; the other would be turning the control over to the private monopolists in the industry.

Essential regulatory improvements should be made, and we need to begin the long, hard process toward competition, but that doesn't mean simply freeing the industry from regulatory constraints without imposing competitive requirements.

Thank you, and I apologize for running a little bit over.

[The statement of Mr. Wilson follows:]

COMPETITION IN THE INSURANCE INDUSTRY

Testimony of

Dr. John W. Wilson

Before the

Subcommittee on Monopolies and Commercial Law

Committee on the Judiciary

United States House of Representatives

September 13, 1984

J. W. WILSON & ASSOCIATES, INC.
ECONOMIC COUNSEL
1010 WISCONSIN AVENUE, N.W. • WASHINGTON, D.C. 20007

Mr. Chairman and members of the Subcommittee, I appreciate your invitation to appear before you today to testify on matters pertaining to the McCarran-Ferguson act and the effect of insurers' joint ratemaking activities on competition and on insurance consumers. Along with my prepared statement I am submitting for the record a detailed study on Insurance Rate-making which I completed last year together with Robert Hunter, who has also been asked to testify in this hearing. Chapter IV of our 1983 study deals extensively with the competition issues that are of concern to the Subcommittee. In addition, Appendix A of the study presents a detailed legal analysis of competition in the property/casualty insurance industry and I recommend that as instructive background reading for you and your staff.

The property/casualty insurance industry is characterized by practices which are commonly considered to be anticompetitive in other settings. But for the McCarran-Ferguson Act, 15 U.S.C. 1011 et seq, which partially exempts the insurance business from application of the antitrust laws, these practices would be of very doubtful legality in the insurance industry as well. Practices traditionally viewed as anticompetitive but which continue to be permitted, and in some cases flourish, include, most prominently: (a) procedures for explicitly or tacitly fixing prices among competing sellers; (b) agreements among sellers not to compete for markets; and (c) agreements between

companies and agents that restrict the ability of agents to reduce prices in order to gain sales. Other conduct bearing on competition includes (d) practices designed to avoid competition for marginally attractive sales.

Recent decades have brought significant changes in the structure of the property/casualty insurance industry. A small group of large direct writers with nationwide marketing organizations now sells an increasing share of all personal lines coverage in local markets where they are recognized by their fellow underwriters as the price and product leaders. Their relationships with each other are more in the nature of compromise than competition. Freed of antitrust constraints by the McCarran-Ferguson Act, these large underwriters, even though falling short of being monopolies in a technical sense, are nevertheless able to exert substantial influence over smaller underwriters, would-be competitors, and even customers. Because they are large, they have financial resources that enable them to out-bid, out-spend, and, in selected markets, even out-lose smaller rivals. They can command the best marketing organizations and financial talents; they can diversify into related financial service areas through conglomerate acquisitions; they can integrate backwards into related investment banking ventures or forward into complementary retail investment services; in short, given the antitrust exemption

that they enjoy, they can, without breaking the law, free themselves from many of the fortuities of the market. There may be disagreement as to the relevancy of these facts, but few can deny that they are the facts.

One test of seller competition in any industry or market is whether there is a sufficient number of truely independent sellers in that market to preclude excessive seller influence and control over price, quantity, and the nature of the product provided in the market place. There is an absence of adequate competition when, as in the insurance industry, sellers are able to exercise great discretion in establishing prices, supply conditions and other marketing strategies. Where firms have such latitude, they possess excessive market power, and the outcome of such a "free market", much to the detriment of consumers and the public interest, is monopolistic rather than competitive. That is a fundamental reason for rate regulation in the insurance industry.

Although insurance regulators must be concerned about a number of diverse regulatory issues, including insurer solvency, non-discriminatory insurance availability, and the dissemination of accurate market information to customers, the regulation of rates is, by far, the major essential task in the regulatory process.

The effective regulation of insurance rates has two aspects: control of rate level and control of rate structure. Rate level regulation has to do with the size of an insurer's profits, whereas rate structure regulation has to do with the allocation of costs between lines and between states and, therefore, the particular rates paid for various coverages by various customers. The fundamental regulatory concern with respect to rate level is that the profit realized under the approved rates be neither so high as to exploit consumers nor so low as to undermine the financial solidity of an efficiently managed and operated insurance company. The central regulatory issue with respect to rate structure, on the other hand, is discrimination. Insurance commissioners must be concerned not only about the level of costs, but with the allocation of costs between lines of coverage, regions and risk classifications so as to preclude unfair and unreasonable discrimination which favors certain customers or groups of customers while harming others.

While the imposition of economic regulation is necessary to protect public interests in industries or market circumstances where the forces of competition alone are not sufficiently strong, the remaining complimentary role of competition should not be ignored.

While regulation contributes substantially to the performance of these industries, there is virtually a unanimity of opinion among economists that regulation is, at best, an imperfect substitute for competition. It also is widely accepted that greater reliance should be placed on competitive forces whenever that is possible.

While efficient regulation can be an effective deterrent to many traditional monopolistic abuses, it does not provide sufficient positive incentives for maximum advancement in the fields of management efficiency, cost control, innovation, and price reductions. These are areas where competition can be especially stimulating.

There are numerous instances and situations within the regulated sector of our economy where competitive stimulus tends to provide a valuable and irreplaceable supplement to discretionary public control.

It is important to emphasize in this regard that in most cases, including the insurance industry, it is not really a question of choosing between regulation and competition. Instead, competition can be made to serve as an integral and complementary force within the regulatory framework. While regulation can be an effective negative restraint against monopolistic excesses, regulatory commissioners (unlike market competition)

are extremely limited in their ability to force firms to accept risk in the interest of advancement and innovation.

Arguments that antitrust goals should be subordinated to the goals of regulation or that deregulation should follow where regulated industries have not obtained optimal performance records misses the point. The fact is that the goals of regulation and competition are not mutually exclusive. In many respects they are identical. Where the two forces can complement each other, the mutual objective can be better attained.

Insurers have questioned the need for detailed control of rates on grounds that regulated insurance companies find it in their own interests to hold expenses and rates to the minimum efficient level. But that is not likely to be the case in imperfect markets such as those where personal lines property/casualty insurance is sold to relatively unsophisticated buyers by cooperatively inclined sellers whose mutual pursuit of collective interests is unencumbered by antitrust restraints, and where expenditures made on behalf of investors or management may be charged to consumers. Management in companies where there is little direct ownership control (e.g., especially mutual insurance companies), can derive personal gain without significant owner-imposed restrictions.

Diversified corporate entities that have substantial holdings in the insurance business can achieve large private profits by requiring their insurance and noninsurance affiliates to engage in highly lucrative transactions with each other. In some cases, the groups controlling regulated insurance companies may be incompetent. In others, they may merely be private profit maximizers. To guard against the likely consumer abuse inherent in either of those situations, the expenses of insurance company operations should be examined in detail by regulatory authorities.

In practice, insurance regulators have not been vigorous in controlling insurer costs. While their authority to do so in most jurisdictions and the economic need for such control is clear, no state regulatory authorities have promulgated rules or established standards to govern insurer expenditures.

Regulators have also tended to accept significant rate discounts for large commercial purchasers of property/casualty insurance even though such discounts invariably mean that a larger percentage of expense overheads must be recovered from the remaining undiscounted group of smaller personal lines policyholders. The resulting higher rates which then go to small businesses and households, where the demand for specific coverage tends to be more inelastic and where regulatory pro-

tection is most urgently required, underscores the failure of insurance regulation to give adequate protection to those who need it most.

These failures can be attributed to three main causes. First, insurance commissioners have been compelled by the industry they regulate and by their lack of resources to devote most of their energy to the struggle over the level of profitability, and they have had little time, energy or resources left to spend in the interest of reforming cost allocation or improving expense control. Second, they have been deceived by methods of accounting that are employed to obscure cross subsidies and justify discrimination. And third, they have been deterred from overhauling the structure of insurance ratemaking by the fact that many of its parts have become so deeply embedded in established tradition.

At the same time, concentration has been increasing in the property/casualty insurance industry, particularly auto insurance, for at least three decades. After thirty years, the trend has produced the predictable result. Major lines of insurance are far more concentrated tha they were several decades ago, and many state markets are concentrated at oligopoly levels.

Current data indicate uniformly higher levels of concentration compared to the concentration levels reported a decade

ago. As shown below, the 4-firm state market share is significantly higher than 10 years earlier, and most states have 4-firm shares in excess of 50% for one or both auto lines:

Average 4-Firm Concentration Ratios

	Homeowners	Auto Liability	Auto physical damage
1970	32.6%	39.2%	37.8%
1980	43.6%	49.8%	49.5%

Also, in contrast to circumstances ten years ago, today most homeowners markets and almost all auto markets are sufficiently concentrated to conform to the traditional broad definition of oligopoly: 1/

Number of States With Oligopoly Markets

	Homeowners	Auto Liability	Auto physical damage
1971	16	20	30
1980	38	50	48

1/ Kaysen and Turner have defined an oligopoly market as one where eight firms have 50% of the business, and 20 firms have 75% or more. These are referred to as the eight-and twenty-firm ratios.

The few states not concentrated in auto lines are smaller states where the markets fall short of being concentrated by only slight amounts. Kentucky (phys. dam., 55.5%/74.9%); New Hampshire (liab. 49.0%/80.1%; phys. dam., 46.5%/78.3%); North Carolina (phys. dam. 50.9%/74.6%).

Similarly, while there were no states with highly concentrated markets under a more strict test 1/ in 1971, there are now 27 highly concentrated state-product markets; and 12 more are borderline: 2/

	Number of Highly Concentrated States		
	Homeowners	Auto Liability	Auto physical damage
1971	0	0	0
1980			
Very High	4	14	9
Borderline	2	5	5

The states that are highly concentrated in both auto lines include a number of major open competition states, such as California, 3/ Michigan, and Virginia.

1/ Dr. Willard Mueller defined an oligopoly market as one with four- and eight-firm ratios of 50% and 70%, respectively. Monitoring Competition at 261.

2/ A state is borderline if it falls short of the high concentration boundaries by a total of no more than 2 percentage points (e.g., 48/70, 49/69, or 50/68), so that at present trends it will cross the high concentration line by the end of 1982.

3/ The California data recognize the fact that two major insurers do not compete in each other's territories, and, for competitive purposes, they are treated as one. Even without that adjustment, California is highly concentrated in liability insurance under the strict test (55.0%/70.5%) and almost so for physical damage (55.1%/68.8%).

The industry's concentration is significant, but given the institutional setting which we know exists in the industry, it should probably be viewed as an ancillary factual observation. Unfortunately, many of the analysts who have addressed the competition issue treat concentration as being alpha and omega, and then rush headlong to judgement without ever having weighed the critical direct factual evidence bearing upon the industry's institutional framework. Concentration, after all, means virtually nothing in and of itself; it is an important measure only in that it infers something about something else.

Let me be as specific as possible on this point because it is quite critical, and it appears to be the slippery plank where a number of otherwise learned and capable analysts seem to have fallen overboard. As I said previously, whether or not there is competition depends upon whether there is an adequate number of truly independent, self-motivated sellers. Independence is the key. Without independence, self-motivation will bind interdependent sellers together in the mutual pursuit of common objectives at the expense of consumers. With independence and the vigorous conflict of real competitive rivalry, the market system can serve consumers admirably. Consequently, in attempting to determine whether a market is workably competitive, economists search for evidence bearing upon the presence or absence of seller independence.

Often times, however, good direct evidence on the degree of seller independence is unavailable, or that which is, is inadequate. Then, of course, it is necessary and appropriate to look for secondary evidence which may have inferential value in assessing the primary issue--information from which one can obtain some insight on the specific question at hand. Information on concentration frequently provides such an insight on the question of seller interdependence, in that it provides an analytical base from which probabilistic conclusions can be derived. In other words, concentration serves as a basis for logical conclusions derived via the classical deductive method of logic:

> e.g., in industries dominated by a few large firms, each of the participants is aware of the fact that his actions will affect the others in that industry significantly, and that they, in turn, will react and affect him. They are all interdependent! Vigorous competition will therefore be stifled by their own self-interest in peaceful coexistence.

Or, as stated more elegantly:

> A large concern usually must show a regard for the strength of other large concerns by circumspection in its dealings with them, whereas such caution is usually unnecessary in dealing with small enterprises. The interests of great enterprises are likely to touch at many points, and it would be possible for each to mobilize at any one of those points a considerable aggregate of resources... Hence, there is an incentive to live and let live to cultivate a cooperative spirit, and to recognize priorities of interest in the hope of reciprocal recognition.1/

1/ Corwin D. Edwards, "Congolomerate Bigness as a Source of Power" 1955.

Simply put, that is why economists (should) concern themselves with concentration ratios. These ratios are an admirably designed foundation from which deductive logic can proceed. If concentration is high, we deduce that firms are not likely to behave independently, and if they don't behave independently the market will not be competitive.

My point in belaboring this discussion is to establish the fact that concentration ratios are only important when it is necessary to use deductive logic to determine whether firms are interdependent. If the answer to that question is known directly, as in the case of joint rate bureau activities in the insurance industry, then whether the four firm concentration ratio is, say, 0.3 or 0.6 is really quite moot.

Much more important than the increased level of market concentration that has evolved as a result of the pervasive and growing impact of the industry's dominant firms, traditional cartel activities continue to stifle the remaining potential outlets for enhanced competitive rivalry. The agenda of rate bureaus does not include supplying information to buyers. The exchange of detailed information and the provision of pricing recommendations is reserved for the benefit of "rival" sellers. In view of the fact that information dissemination is reserved for the bureau's seller-members, it is clear that these efforts,

especially pricing guidance, are more essential for cooperative than for competitive market operations. Rate bureaus have not been designed merely to ensure an intelligent and informed business rivalry by which competitive relationships may be established. On the contrary, they involve a cooperative interpretation and dissemination of market data and at least a strong effort at the coordination of market policy designed to bring security and profits to underwriters at the expense of those who purchase coverage. These bureaus provide their members with a forum for obtaining intimate knowledge of the pricing guidance that is dispensed to "rival" suppliers. The leading property and casualty underwriters have developed among themselves an _esprit de corps_, a live-and-let-live code of ethics, commercial interrelationships, intermingled interests through reinsurance, and a spirit of reciprocal recognition of priorities of interest, all of which tend to lessen the vigor of competitive rivalry and to replace that vigor with communal approaches to regulatory and market issues. These arrangements are as effective as formal cartels in monopolizing markets.

In view of the property/casualty industry's market structure and conduct, it is not surprising to observe that the industry's performance also lacks important competitive characteristics. In industries where market performance is competi-

tive, the typical end result is efficient and independent sellers offering more and better products at lower prices to consumers.

Industry spokesmen often point to the industry's investment income oriented underwriting practices, which voluntarily reduce underwriting income in order to maximize premiums written and investment income, as evidence of workably competitive market performance. While investment income oriented underwriting is a type of rivalry between sellers, it is clearly not the type of meaningful price or product competition that provides protection and benefits to the typical personal lines customer.

Investment earnings are now the sole source of net income for the property/casualty business as a whole, and for most property/casualty insurance lines. 1/ In theory, high investment income could translate into lower rates for insurance coverage if carriers competed with each other by reduc-

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1/ In 1981, all but two of the 25 largest groups recorded underwriting losses, yet they had good overall results because of record high investment income. Investment income has been the main source of income for the industry since the mid-1950s, but the gap between investment earnings and underwriting profits (or losses) has grown sharply since 1978. See William Kinder, "A Look at the Leaders: Why Worry About Underwriting Profits?" Best's Review, September 1982, at 16, 18 (Exh. 2), 123 (Exh. 5)

The Insurance Services Offices reports the same; see ISO, "The Road Ahead: A Commentary on the State of the Property-Liability Insurance Industry", at 9 (undated but with mid-1982 data) ("Investment income has become the only source of industry profit").

ing prices as investment earnings increased. But that has not happened in personal lines markets where consumers have, instead, been treated to the industry's alternative, two-pronged response to rising investment income. First, rather than cutting prices to existing policyholders, carriers have relaxed underwriting standards in order to attract more premiums and add further to their lucrative investments. Second, investment income from personal lines coverages has been used to offset premium requirements in commercial lines where greater customer knowledge and buying power have extracted price concessions not offered to smaller personal lines accounts. 1/

As a result of reduced underwriting standards, there have been carrier-imposed cross subsidies from low risk to high risk customers. This tactical response to rising investment income is apparently preferred to rate reductions in the personal lines property/casualty market environment because it permits carrier growth and increases carrier assets and reve-

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1/ See, for example, a recent (January 13, 1983) Wall Street Journal account of this practice which states:

> NEW YORK -- Prepare to pay higher premiums for automobile and homeowners insurance.
> Property and casualty insurance companies, facing sharply rising underwriting losses on commercial insurance policies, plan to boost rates for personal insurance customers...

nues rather than reducing the firm's revenue and asset size as would occur if underwriting standards were maintained and competitive price cuts were instituted to the extent permitted by investment income gains. The fact that carriers have responded to investment income gains in personal lines markets through non-price rivalry is one clear signal that carrier competition is not sufficiently structured to best serve all customers' economic interests.

Clearly, serious questions of cross subsidy from small, manually rated insureds to larger accounts exist. Even if it could be shown that commercial lines competition reduced the overall profit levels of property/casualty carriers to a fair level (an industry argument that is not borne out by the facts), the resolution of unfair and discriminatory anticompetitive practices in personal lines markets would still require regulatory rate action providing for the explicit recognition of investment income in personal lines markets. 1/

The problem can be stated as follows: If the investment income associated with personal lines customers paying manual rates, with a built-in standard underwriting margin, is used to subsidize large accounts not paying manual rates and enjoying what the industry calls "cut throat" competition,

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1/ All state laws require that the regulatory authority assure that rates be "not unfairly discriminatory."

the need for regulatory concern about who gets the benefit of personal lines investment income is obvious. Whereas a typical buyer of personal lines coverage would like to see his rates fall when investment income rises (as, no doubt, he would in a market that was really workably competitive), that is not what typically happens in the property/casualty insurance industry. Instead, rate levels are typically maintained (or, even raised), and the carriers' investment income windfall is used for a combination of other objectives including: higher equity returns (in the case of stock companies), reduced underwriting restrictions (so as to attract more funds for investment purposes), investment portfolio growth, and cross subsidies to commercial lines where buyer savvy and more meaningful market options mandate a higher level of price responsiveness. For the typical personal lines customer, insult is then often added to injury when these carrier maneuverings to exploit investment income potential produce the expected underwriting profit reductions, and those reductions then serve as an unwarranted rationalization for further rate increases.

Thus, despite the illusion of competition that is created by lower underwriting income in periods of high investment income, we should not be lulled by the industry into a complacent acceptance of the false argument that lower underwriting returns, under these conditions, are a manifestation of workable price

competition between property/casualty underwriters in personal lines markets.

Even if profits were genuinely not excessive, that fact alone would throw no light on the fundamental question: Have these profit results been compelled by a competitive system or do they simply represent the dispensations of shrewd management which, with wide discretionary latitude at its disposal, decided for the time being to "play it smart" in view of the potential regulatory consequences. 1/

Consumers of personal lines insurance coverage have thus been deprived of the full potential benefits of price competition as investment income has risen in the property/casualty insurance industry. Enriched by growing investment income, carriers have generally elected to relax underwriting standards and subsidize commercial markets. This has fostered premium and investment portfolio growth rather than passing through the benefits of growing investment income to low risk personal lines customers.

Underwriting selection has also intimidated or discouraged price shopping by consumers, muting the principal source of

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1/ Monopoly rents need not show up in profits. They can manifest themselves in excessive expenses and other inefficioncies. In Invisable Bankers, Linden Press, 1982, Andrew Tobias finds that insurers are grossly inefficient.

competitive pressure for lower rates. Faced with uncertainty over the effect of claims on cancellation or non-renewal, and arguably relying on the premise (whether or not correct) that an insurer is less likely to cancel an old customer than a new one, consumers simply elect not to shop competitively for insurance.

Selection competition does not reflect efficiency in the familiar economic sense of producing a good or service at lower costs. The costs in question are losses that will occur in any event. The effect of selection competition is not to reduce those losses, but rather to shift them around, either from one insurer to another, or from auto insurers to the person who could not obtain coverage, his or her victims, or their insurers. This fact, unique to insurance, was one of the reasons Congress elected to partially exempt insurance from the antitrust laws in the first place. 1/

But, selection competition between insurers does not necessarily lead to enhanced competitive market alternatives for customers. Indeed, those customers whose underwriting

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1/ The theory of insurance is the distribution of risk according to hazard, experience, and the laws of averages. These factors are not within the control of insuring companies in the sense that the producer or manufacturer may control cost factors.

H.R. Rep. No. 873, 81st Cong., 1st Sess. 8-9 (1943), quoted in Royal Drug, supra at p. 22, 440 U.S. at 221.

risks are perceived to be relatively high (because of their track record, or where they live, or their economic or demographic condition, or otherwise) are often left in a considerably less competitive environment. Even the insurance industry has acknowledged that the high risk segment of personal lines property/casualty markets is not competitive. 1/

Market control in the insurance industry, especially personal property/casualty lines, is held by a closely tied consortium of individual insurers whose joint activities are now largely exempted from antitrust enforcement by the McCarran-Ferguson Act. These firms, working in cooperation with each other, have the ability to substantially control insurance underwriting.

State regulation of insurance rates was supposedly designed to deal with this matter. Apparently, it is not working well. No one can deny that policy changes are needed. The prescription offered by the insurance industry and its spokesman is for unrestrained "market freedom" -- a situation wherein

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1/ See the Report of the Advisory Committee on Competitive Rating in Residual Markets "not subject to competition." In addition to the high risk markets that are created by selection competition, few would deny that title insurance, credit insurance and workers compensation insurance (where cartelized adherence to standard rates is required) are noncompetitively priced lines. NAIC proceedings -- 1980, Vol. II, p. 431.

the industry (not the public) would be "free"; free, that is, to extract the maximum possible price that the market will bear. That, of course, is really nothing other than a monopoly price; even a totally monolithic monopolist would be unable to charge more than his product is worth. The essence of monopoly is the ability to extract a price equal to full commodity value, regardless of how exorbitant the profit. Unless capitulation to the monopoly power of private economic interests is now viewed as a national policy alternative, this prescription makes no sense. Certainly, from the consuming public's view, it cannot be described as rational.

The first and foremost step which must be taken in order to make the insurance industry more workably competitive is to eliminate the antitrust exemption which insurers are now able to use as a shield to defend their collective, rather than competitive, approach to personal lines markets. At the same time, steps should be taken to improve insurance rate regulation.

It should be rather obvious that it is somewhat unfair to expect outstanding results if the tools provided are inadequate to the task, and it is perhaps also unfair to expect great enthusiasm from those assigned a task if the overriding conditions make that task next to impossible. In short, regulation and regulators could be far more successful if the institutional blockages noted here are eliminated and regulatory resources are improved.

Even with the repeal of McCarran-Ferguson no one familiar with our recent antitrust track record could be overly optimistic about the outcome without some new maninfestation of the strongest possible Congressional support.

Summary, at this point, is quite simple. The industry is not competitive. Present regulation is not working well. There are ways in which competition can be increased, and there are also ways of improving regulation.

There are two "solutions" which are clearly "bad": continuing as is as if no change is needed, and turning control over to the private monopolists.

I believe that essential regulatory improvements are needed immediately; they can have an immediate impact and help pave the way for more effective competition. At the same time, we should begin the long hard process of restructuring market conduct in the insurance industry so as to reform the underlying market fabric that is now dominated by collective industry arrangements rather than by effectively competitive conditions. But that is a long-run goal, not to be confused with the "free market force" rhetoric which flows unmindful of the prevailing market facts and unwary of the consequences of turning matters over to an unrestrained insurance industry cartel.

BIOGRAPHICAL SKETCH OF JOHN W. WILSON

John W. Wilson is President of J.W. Wilson & Associates, Inc., a consulting firm specializing in regulation and anti-trust matters.

Dr. Wilson received his Ph.D. in Economics from Cornell University in 1969. Prior to founding J.W. Wilson & Associates, Dr. Wilson was an independent insurance agent (licensed in the State of Wisconsin), Captain in the U.S. Army, Associate Professor of Economics at West Point and Chief of the Division of Economic Studies at the Federal Power Commission.

Dr. Wilson has published numerous papers and articles and has worked as a consultant to the U.S. Department of Justice, other Federal agencies, State agencies, corporations and trade groups in the United States and Canada.

Chairman RODINO. Thank you very much.

We want both of you to understand that your prepared statements will be part of the record, together with the other information which you have attached, which I'm sure we will find very helpful.

Mr. Wilson, I recall you mentioned that the New Jersey Insurance Commissioner is committed to competition; what steps can be taken to bring down auto insurance rates there?

Mr. WILSON. Well, one step that New Jersey has already moved in the direction of, largely at the prodding of Commissioner Rodriguez before Commissioner Merin was on the scene, is to recognize investment income of insurance companies in the ratemaking process, and there are a number of States that are doing this.

Insurance companies are, in a sense, like banks. They take in money from people, and they hold it, and at some later date they dispense a portion of it to settle claims.

Many of these claims take many years to settle. Most claims take some period of time, and insurance revenues are always collected in advance. Consequently, insurance companies make vast amounts of money on investments. That's a big part of the business that they are in, and the fact is that in recent years, with interest rates rising, virtually all of the profitability in the insurance industry has been achieved through the investment side of the house. But they are investing consumers' dollars, and there are many States where the recognition of this investment income doesn't go into the ratemaking process.

New Jersey has moved in a positive direction, and a variety of other States have in that regard as well.

A second problem, and one that I think is just being considered at this point in New Jersey, and is not even contemplated in probably 40 States around the country, is the question of detailed scrutiny of insurer expenses.

The contrast that I mentioned between the type of careful examination of what is allowable for recovery through rates that takes place in regulating a Southern California Edison or a Public Service Electric & Gas, as opposed to the total absence of scrutiny of expenses when it comes to insurance companies.

The insurance regulators nationwide have traditionally simply accepted the expenses that insurance companies have shown on their books without going into any detail as to what those expenses are for and acting as a cost pass-through device.

Whether it's political lobbying activities, whether it's benefits for the private interests of the stockholders of the company, or whether it's a legitimate expense in the service of the insured, the expense gets flowed through to the ratepayer without scrutiny, and I would say that's a very major area that New Jersey, California, and other States recognize—that the regulatory situation in California is not the same but States ought to be looking at it as an effort to bring insurance costs down and prevent some of the abuses and excesses that the carriers are implementing at the present time.

Chairman RODINO. Thank you very much.

Is it fair to say that both of you believe and would recommend repeal of the exemption that's provided by McCarran-Ferguson and

that repeal would bring about more competition? Do both of you believe that with more competition we would have the kind of results that would bring about lower rates and provide better service?

Mr. WILSON. I certainly do, yes.

Mr. HUNTER. The answer is yes, as long as you also make sure that competitive factors are in place. That is, I do think information needs to flow for competition to work, for example.

Chairman RODINO. Since lower rates with better service is the result that we are looking for, what's so bad with the situation which Commissioner Baerwaldt described where State regulators, with the help of some new State laws, can bring about the kind of competition that would bring about lower rates?

Do you support such a proposition, or do you feel that it's better to go the way that you have just expressed—repeal the exemption to open the market to more competition?

Mr. HUNTER. Even Commissioner Baerwaldt said that she would be in favor of repealing the exemption. It would obviously encourage greater competition to have national competition rather than just trying to do it on a State-by-State basis.

Additionally, as I pointed out in my testimony, competition really works quite well in the commercial lines, such as workers' compensation, if the shackles are taken off, because you have informed consumers who have choices, such as self-insurance.

When you take off the shackles in auto insurance but leave the cartel in place, which is the current situation in Michigan and other places, the competition does not flow at the same level, because you don't have those informed consumers. Consumers must buy auto insurance and don't have choices to do something else, and the cartel still functions.

So I think the Federal move is necessary, even in the auto insurance situation in Michigan, to make it work completely.

Mr. WILSON. I'd emphasize that the commissioner's statements were focused, I think, largely if not exclusively, on workers' compensation, and workers' compensation is substantially a different animal than the other types of personal lines—property/casualty coverage—that we've been talking about this morning.

I have a corporation here in the District of Columbia, and I buy workers' compensation insurance and spend about $5,000 a year on it. I can shop till my nose is blue, going to agents all over the city; I'm going to get one price, because legally nobody's going to deviate; everybody's going to give me the same price on workers' compensation insurance.

There might be a little bit of difference in States where deviation is permitted, but if you have uniform deviations or if you have uniform pricing, the antitrust problem is essentially the same, and certainly the type of fixed price for workers' compensation insurance that you have in the District of Columbia and many other jurisdictions is the worst of all possible worlds. Anything in the direction of competition would be beneficial there.

The step toward open competition, I think, is positive. The regulator has to be concerned about price discrimination, however, that could take place between large and small accounts, so that the regulatory role doesn't go away.

Chairman RODINO. Mr. Hunter, in your recommendation for repeal of the McCarran-Ferguson exemption, would you consider carving out certain legitimate collective activities that might be necessary?

Mr. HUNTER. I'm not an attorney; I will make that clear at the outset; I'm an actuary.

There are some legitimate activities. I heard earlier witnesses say that they would probably pass muster without an exemption; Griffin Bell, I believe, said that.

If that's right, then I wouldn't encourage any little safe harbors, or whatever you want to call them. If it isn't right, then you have to list some collective activities that are essential, such as data collection, although the State might be able to do it, I think, without having an industry bureau do it, because the people need data as well as the companies.

Mr. WILSON. I think that's an important point.

I think you've got to look at insurance industry associations the same way that trade associations in other industries are viewed. There are some actions that could be legitimate and some that are illegitimate.

Chairman RODINO. Such as?

Mr. WILSON. For example, the dissemination of pricing information. Bob Hunter emphasized this in his prepared remarks. The exclusive dissemination of that information only to the sellers but refusal to provide the information to buyers in the marketplace can't serve a competitive purpose.

Buyer information, consumer intelligence, is essential in order to make markets work. So if you have associations that collect information on rates and disseminate that information on rates to everybody—to the sellers so that they know what the prices are that they have to beat, and make it available to buyers so that they know what the options in the marketplace are—that could be a positive contribution, but the way that it works now, with the exclusive function as being pricing guidance to sellers, is clearly anticompetitive.

Chairman RODINO. Mr. Hunter, I was interested in noting from your biographical sketch that you have worked for rating organizations and now you're the president of a consumer organization. In your prepared statement you describe some of these organizations as cartels. Do you have any examples of cartel-like activities in which some of these ratemaking organizations are involved?

Mr. HUNTER. I listed some in my statement. Of course they set prices; that's obviously cartel like. They disseminate data only to their affiliates, not to the public; that's obviously cartel-like. But even in the way they think in their committees they show cartel-like behavior.

I can recall, on the question of investment income that John Wilson just discussed, we went through a long rate hearing in Virginia where the question of investment income was raised. The staff of the insurance services offices—the National Bureau of Casualty Underwriters at that time—suggested to the actuarial committee that maybe we ought to factor investment income into the rate-setting process. The response of the committee was, "Why should we give it up? In a few States we may have to lose it, but

we don't lose anything, and, besides, it gives consumers and others who would intervene in rate cases a kind of a plum that they can have without us losing anything; so let's leave it the old traditional way."

I think that's cartel-type thinking, and I think that continues to exist. You'd expect that when they get together—to set prices and set policies that will maximize their profits.

Chairman RODINO. Dr. Wilson, I take it from some of your statements and the examples, especially in New Jersey, that you don't see that there is any conflict or opposition, which would work against competition or against bringing about a reduction in rates if there was an application of antitrust along with State regulation. Is that correct?

Mr. WILSON. I can see absolutely nothing that should impede the imposition of antitrust. I can see no negative consequences of making the industry subject to competitive requirements.

I would emphasize that even if the industry is subjected to antitrust requirements, however, that does not necessarily preclude the need for concern about cross subsidies and discrimination and the concern about the differences on the part of the buyer to function in a competitive market efficiently on the commercial side as opposed to personal lines.

I think there is still a regulatory role that will be necessary.

Chairman RODINO. Finally, as an economist, you don't see any reason why the insurance industry should, because it claims uniqueness, enjoy the kind of exemption that it does have currently under the McCarran-Ferguson Act?

Mr. WILSON. No; none at all.

Chairman RODINO. Thank you very much.

Mr. Fish.

Mr. FISH. Thank you, Mr. Chairman.

Mr. Hunter, in response to the question by the chairman, and I think also in your statement, you recommend repeal of McCarran-Ferguson and a substitution of—and I quote—"Federal standards to insure competition." I'm interested in what form this Federal regulation that you have in mind would take.

Mr. HUNTER. I don't know—I don't think it has to be done by the Federal Government. I think the States can enforce it. But I'm talking about things like making sure that information is available to consumers. It does not exist today in the open rating States, the kind of information consumers need to make a wise auto insurance choice, for example.

As Commissioner Baerwaldt indicated, in Michigan, that's a key problem in auto insurance in that State. There needs to be that sort of information. Those are the kinds of things I'm talking about.

Mr. FISH. In your testimony you use the words "Federal standards," but now you're telling us that these could be Federal standards but administered by the States?

Mr. HUNTER. Oh, yes.

Mr. FISH. Also, could you tell me, would you embrace Ralph Nader's suggestion that he made before this subcommittee in testimony on May 10 of this year?

The suggestion was that Federal law should require all insurance companies operating in interstate commerce to include in their premium billings a statement printed by a national consumer group chartered by the Congress.

Mr. HUNTER. I do think that's a good idea, particularly as long as you have a regulatory scheme.

As I pointed out in my statement, Harvard University studied the insurance commissioners of this country, and by far the vast majority of them considered themselves judges to weigh the interests of the industry in what they say versus what the consumers come in and say.

Unfortunately, in every rate case, in every proceeding, there's only one side heard. I think Mr. Nader's idea is quite intelligent to redress that imbalance.

Mr. FISH. Are you thinking in terms of your own organization in this light?

Mr. HUNTER. No. As Mr. Nader said, it would be a federally-chartered organization, as I understand it. I'm not so chartered.

Mr. FISH. Would you like to be?

Mr. HUNTER. No.

Mr. FISH. On page 12 of your testimony, Mr. Hunter, you refer to market allocation agreements, and I wonder if you could tell me how you define that phrase.

Mr. HUNTER. Well, I gave an example in the testimony. In California, there are two AAA organizations that have agreed not to compete with each other, even though they are two very major insurance companies within the State. They've allocated the market. They've said, "I won't come into your territory." So they are not competing; they've agreed not to compete. That's a market allocation.

Mr. FISH. So you are suggesting that companies agree to divide up spheres of influence.

Mr. HUNTER. I'm saying there's an example of one, and I don't think they should be allowed. That's all I'm saying.

Mr. FISH. You're getting close to charging an antitrust conspiracy, aren't you?

Mr. HUNTER. I can't charge it. The McCarran-Ferguson Act is in place.

Mr. FISH. Well, it seems to me that, you know, it's one explanation for behavior that is done solely in order to divide up a lucrative pie there. It seems to me there could be valid business reasons also why companies would not want to go into every area of insurance or every part of a State.

Can you name any other companies that you make this allegation against?

Mr. HUNTER. I don't have any other incidents of any others. There are other farm bureau type companies that stay within one State and things like that, even though they get fairly large, but I don't know that they've actually agreed with other farm bureaus not to compete.

Mr. FISH. Mr. Wilson, you cited Andrew Tobias in your statement, and he was——

Mr. WILSON. I think Mr. Hunter cited Tobias, but I'm familiar with the work.

Mr. FISH. OK. He, as you know, was a witness before us in April.

Mr. WILSON. I wasn't aware of that.

Mr. FISH. Do you agree with him that the elimination of the McCarran-Ferguson Act would result in greater efficiency within the insurance community because it would result in the reduction of 1 million jobs? That was the basis of his statement, and I wonder if you embrace this view that the insurance industry overemploys to that extent.

Mr. WILSON. I have no basis for agreement or disagreement with the number, but I would observe that in industries where monopolistic circumstances are replaced by competition, one of the things that you find is that inefficiency, including labor inefficiency, tends to be removed.

One of the things that we are seeing, for example, now with respect to the restructured AT&T is that both AT&T and the Bell operating companies at the State level—C&P in Virginia—are able to do the job with less expense, including less labor expense, than they had prior to the divestiture.

So the suggestion that monopoly breeds not only high profits and high cost to consumers, but also manifests itself in inefficiency and high operating costs on the part of the monopolist, I think is generally true.

Mr. FISH. My time has expired, but may I proceed with one or two more questions?

Chairman RODINO. Yes; you may.

Mr. FISH. Thank you, Mr. Chairman.

Dr. Wilson, I think it is on page 7 of your statement where you address the availability of significant rate discounts for large commercial purchasers of property/casualty insurance. How is this any different from normal market discounts for other products where large commercial purchases are involved?

Mr. WILSON. Under Robinson-Patman, price discrimination would be prohibited if it weren't cost justified, and price discrimination that was not cost justified would be subject to Federal and, in many cases, State enforcement.

The problem that you have is not one of price discounts that are cost justified; I'm all for that, and I, in fact, have defined price discrimination in my testimony as price differentials that are not cost justified; but what I'm saying is that price differentials that are not cost justified between commercial lines of insurance and personal lines of insurance are violations of our antitrust laws.

Mr. FISH. Thank you very much.

Thank you, Mr. Chairman.

Chairman RODINO. Mr. Edwards?

Mr. EDWARDS. Thank you, Mr. Chairman.

Mr. Hunter, you're the president of the National Insurance Consumer Organization. What is that?

Mr. HUNTER. It's a nonprofit, 501(c)(3) type organization. Its purpose is to educate consumers and do research into consumer issues dealing with insurance, and we publish books on how to buy insurance and that sort of thing.

Mr. EDWARDS. And how is it supported?

Mr. HUNTER. It was supported by foundation grants originally. Now most of our income has to do with book sales and memberships, and that sort of thing.

Mr. EDWARDS. Mr. Wilson, do you see anything going on in the insurance industry that will make it more competitive?

Mr. WILSON. I see two trends; they're both very slow; things take a long time to happen in the insurance industry. Mostly what you get is more of the same.

For example, just this year, 1984, the National Association of Insurance Commissioners, after 60 years, changed their orientation with respect to the uniform profit formula that was adopted back in 1924, and ever since the 1930s people have been explaining why it should be junked.

Change takes place slowly, but I do see some changes that are taking place, and it's unclear which is most dominant at this point.

You see a growth on the part of large companies, both because of their national marketing activities and because advertising and other types of selling activities have gone national rather than local in scope permitting many of the biggest firms in the industry to grow. At the same time, there are mergers that are taking place that are enhancing the size of the largest firms.

So I see a movement in the industry that is troublesome, because what it says is that even after you get rid of the joint activity that is achieved through rate bureaus, you are already tending toward a situation where you have a conventional monopolistic problem simply because of the size of the largest firms.

Companies like State Farm account for 20, 30, 40 percent of sales in some personal lines in some markets.

The other trend that I see that is much more positive is a trend in the direction of enlightened regulatory activity. I've mentioned New Jersey as an example of that.

One of the institutions that exists in New Jersey—and it exists in some other States such as South Carolina, and it exists in the District of Columbia—is a public advocate to represent consumer interests at regulatory proceedings. It is very important if the insurance commissioner considers himself a judge to have representation of both sides at these proceedings, and it's rare that that happens.

New Jersey is a State that has a public advocate, D.C. has a public advocate, South Carolina has a public advocate; they are empowered to go before the insurance commissioner and represent consumer interests.

At the same time, there are some State regulatory commissions—certainly Florida is one that I would stress is at the forefront—that are moving in the direction of greater levels of investigation, greater levels of scrutiny at the regulatory level—the regulatory process itself. I think that some potential and promise exist for that in New Jersey, but the proof of the pudding there is not in yet.

Mr. EDWARDS. Aren't some of the companies starting to sell their policies directly to the consumers without the use of independent agents? Is that a good trend?

Mr. WILSON. That, of course, has been a trend that moved forward vigorously ever since the 1950s. I think that direct writing

has and can provide a certain type of competitive stimulus, but it's certainly not the answer in and of itself.

The local agent is somebody who did provide a type of service that was important to many policyholders and still does.

I think that if you are an insurance buyer, you should have an option of buying different types of services, and an agent-provided service may be a different quality product than the service of a direct writer.

Another problem with some direct writing activities is that they tend to focus on very limited market sectors, as opposed to generally making their insurance available.

You may have a thousand companies licensed to operate in a State, but in any particular market you may only have half a dozen or so that are actively participating. So the mere fact that a direct writer is there and licensed doesn't necessarily sustain competitive activity, regardless of what Professor Bommell says.

Mr. HUNTER. The other problem, Mr. Edwards, with direct writing is, it's very difficult to enter the market as a direct writer—extremely hard, because you have to have name recognition, you have to have outlets, you've got to have quite a bit of capital, and so on.

It's easy, we could agree among ourselves, to form an insurance company tomorrow that uses agents; but, if competition is really at the direct writing end, what you need is some new entrants there; and that's not easy. That's one of the reasons I think the fight is so vigorous against bank entries, because they have that kind of opportunity.

Mr. EDWARDS. Thank you very much.

Thank you, Mr. Chairman.

Chairman RODINO. Well, I want to thank both of you, Dr. Wilson and Mr. Hunter, for very valuable testimony and for your appearance here this morning.

Mr. HUNTER. Thank you.

Dr. WILSON. Thank you, sir.

Chairman RODINO. Our next witnesses will be Ms. Mavis Walters, senior vice president of Insurance Services Office; Mr. Melvin DeYoung, president, American Association of Insurance Services, who will be accompanied by Mr. Alden A. Ives, president, Patrons Mutual Insurance Co., on behalf of the National Association of Mutual Insurance Companies; and Mr. Donald DeCarlo, vice president and general counsel, National Council on Competition Insurance.

Again, I'm going to urge that each member of the panel, the three who are going to be presenting testimony, be limited to 5 minutes of oral presentation. We will include your prepared statements in their entirety in the record.

Ms. Mavis Walters, you may proceed.

TESTIMONY OF MAVIS WALTERS, SENIOR VICE PRESIDENT, INSURANCE SERVICES OFFICE, INC.; MELVIN H. DeYOUNG, PRESIDENT, AMERICAN ASSOCIATION OF INSURANCE SERVICES, ACCOMPANIED BY ALDEN A. IVES, PRESIDENT, PATRONS MUTUAL INSURANCE CO., ON BEHALF OF THE NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES; AND DONALD T. DeCARLO, VICE PRESIDENT AND GENERAL COUNSEL, NATIONAL COUNCIL ON COMPENSATION INSURANCE

Ms. WALTERS. Thank you, Mr. Chairman.

Before I begin summarizing my already short statement, I would like, if I could, to introduce into the record three volumes, and the reason I'd like to do this is I noted Mr. Wilson introduced into the record his and Mr. Hunter's study.

That study was actually a part of a three-volume report of the Advisory Committee to the NAIC Task Force on Profitability and Investment Income. Theirs was a minority report of the full committee. That is, as I say, actually a three-volume work, and I believe it will be helpful to the committee to have the entire study rather than just one piece of it.

Chairman RODINO. Thank you very much. That will be made part of the record.

Ms. WALTERS. Thank you.

[Material on file with the subcommittee.]

Ms. WALTERS. I am Mavis A. Walters, senior vice president of Insurance Services Office. I am also not a lawyer; I am a fellow of the Casualty Actuarial Society and a member of the American Academy of Actuaries.

Insurance Services Office is a nonprofit corporation serving property/casualty insurance companies in all 50 States, the District of Columbia, and Puerto Rico. Typically, we are authorized to operate as a statistical agent, advisory organization, and/or rating or rate service organization. We are not a trade association, and we do not lobby; we are a technical service organization.

ISO was actually formed as a voluntary association of property/casualty insurance companies in 1971 through the consolidation of many separate national, regional, and State service organizations. We incorporated in 1982.

Although ISO today performs many of the essential functions of the predecessor organizations, it operates in a manner so different from that of its historical antecedents that the term "bureau" is no longer appropriate.

ISO has no mandatory membership requirements, nor do we have adherence requirements with respect to advisory rates, loss costs, policy forms, or programs. In fact, we actively encourage independent action by participating insurance companies.

I feel, Mr. Chairman, this point should be emphasized since Mr. Hunter mentioned earlier that years ago, and, I would venture, more than 15 years ago, long before ISO was formed, Mr. Hunter had some personal experience with the predecessor organization. We are so different now from what we were then; it is totally irrelevant to today's operation.

ISO's primary mission is to serve participating insurers by gathering, storing, and disseminating statistical information to regulators as required by law and to insurers for their own use.

We also develop and assist in implementing programs that help define and cover risk; and, finally, we promulgate advisory rates in a few jurisdictions or advisory prospective loss costs in most jurisdictions for 16 different lines of insurance.

We believe it's very important that this committee appreciate the role that ISO plays in the property/casualty insurance industry today as contrasted with the historical view of rating bureaus.

Thirty years ago, these bureaus were organized along local and regional or national lines, and they specialized in either property or casualty coverage. Collectively, those bureaus became known as the insurance cartel. They did have mandatory membership requirements; complete adherence to rates, rules, and forms; and if a company affiliated for one service, it affiliated for all of them.

Those days are long gone. Indeed, the monolithic cartel had already virtually disappeared by the time Insurance Services Offices were formed in 1971.

From its inception, ISO has encouraged individual insurers to make their own rate level decisions. Significant changes in the regulation of insurance pricing have been occurring over the past 20 years and even more significantly over the last 5 years.

Over half the States have joined California in turning away from strict prior approval and adopting less administered forms of price regulation, at least for some lines of insurance. That trend continues.

It is today ISO's corporate policy, endorsed by our board, that for private passenger and homeowners in competitive-type-rate regulatory States, we distribute advisory loss costs developed by staff only, with no committee involvement, and we do not develop final rates.

Prospective loss cost is a single most important product which we believe we must continue to develop and distribute to insurers.

Based on aggregate insurer data, this prospective loss cost provides essential information in determining overall rate level needs and actuarial equity between various risk classifications.

We should emphasize over and over again that insurance is quite different for most lines of insurance, since we must determine the price before the time of sale. Consequently, insurers must base rates on anticipated and estimated future losses, and these, of course, are based on historical data.

The data base from which future losses are estimated is essential and we believe a broad aggregate data base must be used. ISO's data base improves credibility and increases confidence that the prediction of future losses or future costs is an accurate one. With this confidence, insurers need less of an overall profit margin in the prices they charge their insureds.

We believe that to restrict some of the necessary collective functions would ultimately do harm to the insuring public and consumers.

Thank you.

[The statement of Ms. Walters follows:]

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STATEMENT OF
MAVIS A. WALTERS
SENIOR VICE PRESIDENT
INSURANCE SERVICES OFFICE, INC.

SEPTEMBER 13, 1984

SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW

OF THE

COMMITTEE ON THE JUDICIARY

UNITED STATES HOUSE OF REPRESENTATIVES

Insurance Services Office, Inc. (ISO) is a non-profit corporation serving property-casualty insurance companies in all fifty states, the District of Columbia and Puerto Rico. Typically, we are authorized to operate as a statistical agent, advisory organization and/or rating or a rate service organization.

ISO was formed as a voluntary association of property-casualty insurance companies in 1971 through the consolidation of many separate national, regional, and state service organizations or bureaus. It incorporated in 1982. Although ISO today performs many of the essential functions of the predecessor organizations, it operates in a manner so different from that of its historical antecedents that the term "bureau" is no longer appropriate. ISO has no mandatory membership requirements, nor do we have adherence requirements with respect to advisory rates, loss costs, policy forms or programs. In fact, we actively encourage independent action by participating insurance companies.

ISO's primary mission is to serve participating insurers by gathering, storing and disseminating statistical information to regulators--as required by law--and to insurers for their own use. We also develop and assist in implementing programs that help define and cover risk; and finally, we promulgate advisory rates or advisory prospective loss costs for sixteen different lines of insurance in the various jurisdictions.

Some of the specific services offered by ISO are as follows: We develop programs and coverage documents for possible use by insurers. These programs are designed to meet the minimum coverage requirements of the insurance marketplace. By drafting standardized documents we provide insurers with basic tools to help them define, price and deliver coverage economically.

We serve as a statistical agent which involves the development of statistical plans and the collection and compilation of statistical data from participating companies. The aggregate data are submitted to regulatory authorities, thereby fulfilling state requirements and providing statistics in a common format for regulatory use and review.

We also perform actuarial services which involve the preparation, review and analysis of statistical data to develop reasonable projections of rate level need, overall, by class and by territory. This results in either advisory rates or advisory prospective loss costs, which may or may not be filed with regulatory authorities in different jurisdictions depending upon the type of rating law or regulatory requirements. This information is also provided to participating insurers, each of whom may elect to use, modify or disregard that information depending upon their own needs or requirements.

Our wholly-owned, non-profit subsidiary, ISO Commercial Risk Serivces, Inc., conducts commercial property insurance rating surveys throughout most of the country to help establish specific building rates for fire insurance and other property coverages. The reports which are issued from these surveys give insurers a better picture of the rating conditions at the buildings they cover and therefore help individual insurers rate their risks more accurately.

We believe it is important that this Committee appreciate the role that ISO plays in the property-casualty insurance industry today as contrasted with the historical view of "rating bureaus". Thirty years ago these bureaus were organized along local, regional and national lines. They specialized in either property or casualty insurance, for one or more lines of coverage. Collectively these bureaus came to be regarded as an insurance cartel. They were

characterized by mandatory membership requirements, complete adherence to rates, rules and forms and full indivisible services. If a company was affiliated for one service it was affiliated for all of them. An affiliated insurer was required to use and to adhere to bureau programs and rates.

Those days are long gone. Indeed, the monolithic cartel had already virtually disappeared by the time Insurance Services Office was formed in 1971. From its inception, ISO has encouraged individual insurers to make their own rate level decisions. Significant changes in the regulation of insurance pricing have been occurring for over twenty years. Over half the states have joined California in turning away from strict prior approval rate regulation and in adopting less administerial forms of price regulation, at least for some lines of insurance. And the trend is continuing.

While these changes in the regulation of insurance pricing were evolving, the traditional bureaus were transformed into a modern advisory rating organization which can perform many necessary services more efficiently than individual firms. Indeed, in today's competitive environment, insurers will only participate in a rate service organization under two conditions: (1) where that organization performs functions which can best be performed collectively and (2) where economies of scale in certain collective activities enhance rather than diminish competition. This is why we view ISO's essential task to be the development of information which will assist participating insurers in the making of informed, intelligent and independent pricing decisions.

To that end it is ISO's corporate policy, endorsed by the ISO Board of Directors, that for private passenger auto and homeowners insurance, in

competitive type rate regulatory states, ISO will:

- promulgate and distribute to insurers prospective loss costs only,
- separately provide insurers with aggregate expense data,
- develop the rate-related information without any insurer committee involvement.
- not develop any final advisory rates.

By providing only prospective loss costs for private passenger auto and homeowners insurance in competitive type regulatory states ISO further encourages independent pricing while continuing to provide essential information to insurers to aid them in making intelligent and informed pricing decisions.

Of the three components of a final advisory rate, the prospective loss cost is the single most important product which a centralized, company-supported rating and advisory organization must continue to develop and distribute to insurers. Based on aggregate insurer data, the prospective average loss cost provides essential information in determining both overall rate adequacy needs and actuarial equity between various risk classifications. It is particularly valuable because it is developed from a credible and reliable data base, which no single insurer can replicate for all lines of insurance.

It is this point, more than any other, which this committee should understand. A distinguishing characteristic of insurance is that the cost of the product is not known until long after the product has been sold. Yet the price must be determined before the time of sale. Unlike most other businesses, the insurance business cannot base its prices on the known cost of materials, labor, equipment, or operations. Instead, insurers must base their rates on anticipated and estimated future losses (claims ultimately paid and related

costs). Such estimates in turn are based on historical data gathered for insurance policies written in the past and claims paid or incurred on those policies.

Indeed, an entire profession, the casualty actuarial profession, has evolved and developed to find technical analytical solutions to the problem of determining prices before the costs are known. A popular definition of an actuary is a professional who is trained in evaluating the current financial implications of future contingent events.

Central to the process of ratemaking is the data base from which the future costs must be estimated. With a broad aggregate data base the actuarial analysis of expected losses is more reliable. ISO's large data base improves credibility thereby increasing confidence that the prediction of future costs is an accurate one. With confidence in the calculations of future costs, insurers need to seek less of an overall profit margin in the prices they charge their insureds. In addition, to the extent that ISO's economies of scale reduce the cost of many necessary insurance company functions, insurance consumers reap the benefit.

We believe that the services provided by ISO are important to insurers in their own ratemaking and pricing activities and are conducive to increased competition. The aggregation of data into classification detail requires not only a countrywide data base of many insurers but also special technical expertise and experience. With a centralized service organization providing these products and services, smaller and medium sized firms are able to compete and operate more efficiently and effectively. These services also provide certain economies even to larger insurers, permitting them to enter into new product lines and markets.

By improving insurers' knowledge of their true costs and by introducing economies of scale, ISO confers benefits to the insuring public through lower costs. According to many, the repeal or substantial modification of the McCarran-Ferguson Act would cast a pall of uncertainty over the legitimate and useful functions of rating organizations and thereby impair the benefits which the insuring public derives from them.

Over the years various commentators have speculated on the impact of the repeal of the McCarran-Ferguson Act. They have identified many functions of rating organizations which some might claim to be violations of federal antitrust laws. Among those functions are:

- The collection, combination and distribution of data.
- The collective development of policy forms.
- The development and filing of rate structures, rates and rating plans.
- The surveying and classification of risks.

ISO's operations ultimately benefit the insuring public as well as many small insurance companies. The pall that would be cast over these essential operations by the repeal or substantial modification of McCarran-Ferguson could be enough to severely curtail them. The result would be a disservice not only to insurers, large and small, but to the insuring public as a whole.

Chairman RODINO. Thank you very much.
Mr. DeYoung.

Mr. DEYOUNG. Thank you, Mr. Chairman.

Good morning. I'm Melvin H. DeYoung and am president of the American Association of Insurance Services, commonly known as AAIS.

Located in Bensenville, IL, AAIS is a voluntary association of 400 smaller insurance companies and is an affiliated member of the National Association of Mutual Insurance Cos., commonly known as NAMIC. NAMIC is located in Indianapolis, IN.

I am presenting this statement on behalf of both AAIS and NAMIC. We have submitted a more detailed report for your information, and it has been filed.

NAMIC is a trade association of 1,226 members, mostly medium, small, mutual property and casualty insurance companies operating in 35 States.

Mr. Alden A. Ives, president of Patrons Mutual of Glastonbury, CT, is with me today. Mr. Ives is a past chairman of AAIS and also past chairman of NAMIC. He is uniquely situated to respond to any questions you might have concerning the utility of rating bureaus to insurers and to customers.

Washington counsel for NAMIC is Collier, Shannon, Rill & Scott. A partner of the firm, James M. Nicholson, is with us today. Mr. Nicholson is a former Commissioner of the Federal Trade Commission and was a member of the National Commission to Review the Antitrust Laws and Procedures.

AAIS and its predecessor organizations began to provide services to smaller insurance companies in 1936. From a narrow and specialized base, AAIS has expanded in coverage and lines of insurance so that it today provides its members with loss experience and expense information which are vital to the continued existence of these members.

The record demonstrates that some smaller companies which operate exclusive of rating bureau services experience higher loss ratios and greater expense levels than those that use rating bureaus.

The services which AAIS provides to its members would have to be provided within each member company—the need doesn't go away—if not by the companies, by a consultant, absent AAIS. This additional duplicative cost would provide significantly less information to the individual companies and would ensure the early demise of the smallest companies.

Absent the kind of data now provided by AAIS, many individual companies would be unable to evaluate the viability of providing various lines of insurance, because they would have an inadequate base of loss and expense data.

Unlike the experience of the trucking and airline industries under deregulation which gave rise to intense price competition and the emergence of a number of smaller, highly competitive new entries to those industries, a removal of the present limited exemption provided by McCarran-Ferguson to the insurance industry will assure the demise of smaller, viable insurers which are presently a procompetitive factor in the market.

Is there a consumer benefit in the McCarran-Ferguson exemption? The answer is clearly yes. The regulatory systems of all the various States permits the kinds of information and data collection and dissemination which AAIS provides.

Absent the limited exemption, serious antitrust issues would be presented and would limit the ability of the smaller insurers to determine average loss experience and average expense factors essential to the decision of whether to provide or remain in specific lines of insurance coverage. The result would be a decrease in the number of competitors in specific lines of insurance to the detriment of the insurance consumer.

Another result would be that those companies which continue to write insurance lines about which they had inadequate information would be denied an assurance of the adequacy of their rates. This could lead to rates which are too low. Rates which are too low lead eventually to problems of solvency, which has serious adverse consumer impact.

The functions of the services provided by AAIS to its members place those companies on a competitive basis with the larger insurers. The combined resources and total insurance written by AAIS members about equals the resources and insurance written by one major company. These major companies have available in house the kinds of data, information, and services provided by AAIS.

Thus, AAIS enables smaller companies to compete on a greater parity basis with the larger competitors, thus providing more and better competition, a clear consumer benefit.

What is the role of expenses in insurance companies in ratemaking? AAIS does not take a philosophical position. However, the smaller companies which utilize various people in a variety of lines need assistance in helping to allocate accurately expenses among the various lines to establish the costs. AAIS provides this assistance to the smaller companies and therefore helps them even in determining their average expenses.

Let me conclude by giving a summary statement about NAMIC. NAMIC concurs with the views expressed in this joint statement. It would like to point out, however, that its members are primarily rural property/casualty companies which serve the ranchers and farmers of this Nation. It stands for the mutual insurance concept, neighbor helping neighbor.

Member companies, many over 100 years old, have been providing insurance coverages at costs below what would have been otherwise available. Larger companies have shown varying cycles of interest in this business. Small companies are necessary in the marketplace. These companies depend upon AAIS for the rate indications to measure whether their level of premiums are adequate or not.

With the limited antitrust exemption of McCarran-Ferguson, these member companies are today able to provide the ranchers and farmers of our country with lower cost insurance than would otherwise be available.

Thank you for allowing us to come and present our views to you.

[The statement of Mr. DeYoung follows:]

PREPARED STATEMENT OF
MELVIN H. DeYOUNG
ON BEHALF OF THE
AMERICAN ASSOCIATION OF INSURANCE SERVICES

AND THE
NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

BEFORE THE
SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW
OF THE
COMMITTEE ON THE JUDICIARY

SEPTEMBER 13, 1984

THE McCARRAN-FERGUSON ACT
15 U.S.C. §1011-§1015

Good morning, my name is Melvin H. DeYoung. I am President of the American Association of Insurance Services, commonly known as AAIS. We are located at 1035 S. York Road, Bensenville, Illinois 60106. We are a voluntary association of insurance companies which provides services to our members at a proportionately lower cost than would be the case if they had to individually provide the service themselves.

We are an affiliated member of the National Association of Mutual Insurance Companies, 3707 Woodview Trace, Indianapolis, Indiana 46268, commonly known as NAMIC. We are presenting this statement jointly with that organization. NAMIC is a trade association of 1,226 members, mostly mutual property and casualty insurance companies. The majority of these companies are in the medium and small category, and are spread among 35 states. Representing the National Association and sitting with me at the table today is Mr. Alden A. Ives, President of the Patrons Mutual of Glastonbury, Connecticut. Mr. Ives is uniquely situated to discuss the functions of a rating bureau and its impact on a company, since he has been a past Chairman of the Board of the AAIS, and also a past Chairman of the Board of the National Association of Mutual Insurance Companies. As the top executive in a medium-sized mutual property and casualty insurer, Mr. Ives has developed views concerning the utility of the rating bureau concept to companies of his size, and to the consumer. He will be happy to share these views with you today. We both thank you for the opportunity to testify.

Washington Counsel for NAMIC is Collier, Shannon, Rill & Scott, 1055 Thomas Jefferson Street, N.W., Washington, D.C. 20007.

A partner of their firm, James M. Nicholson, is with us today. Mr. Nicholson is a former Commissioner of the Federal Trade Commission and was a member of the National Commission to Review the Antitrust Laws and Procedures.

We will attempt to give a brief history of our organization, and set the framework which can provide a reference for the position occupied by the rating bureau within the insurance industry. We feel that we are a valuable part of the insurance mechanism and that we perform services not only valuable to insurance companies, but to the American Consumer.

With reference to universal business functions, (ie, buying, selling, transporting, standardizing, financing, risk-taking, and providing market information), the American Association of Insurance Services (AAIS) functions to facilitate insurance coverage standardization and to provide market information. Universal business functions must be performed in all macro systems regardless of whether an economy is planned or market directed. In the property insurance industry, our economy is planned (controlled) in some instances, depending upon the regulatory choice of each state under McCarran. We have absolutely no experience without McCarran and, therefore, it is unclear, what effect a narrowing of McCarran or its removal will have in shifting the insurance economy from a planned to a market directed environment with property insurance regulation. In all probability, such changes will simply shift regulatory jurisdiction to the federal level. but such a shift will not satisfy or eliminate any of the universal business functions.

One can more specifically view the functions of AAIS from the perspective of the marketing needs of an insurance company. A "planned economy" is differentiated from a "market-driven" economy by the regulatory allowances with insurance coverage and price considerations. Where both are determined by regulation rather than by the market place, the economy is "planned." In all types of regulatory climates, AAIS functions to provide insurance coverage and pricing information by classification to support the needs of AAIS affiliated companies. In both instances AAIS functions to provide the product and price needs. The present count of companies served by AAIS exceeds 400.

AAIS provides a comprehensive array of rating products and services. During recent years AAIS has become a leader in residential property insurance and now offers an alternative to the Insurance Services Office.

The history of AAIS begins in 1936 with the formation of the Mutual Marine Conference. This conference was concerned with rates and research involving Inland Marine coverages.

In 1944 the McCarran-Ferguson Act (Public Law 79-15) affected the Mutual Marine Conference as it did all other underwriting or service organizations at the time. Subsequent to the passage of Public Law 79-15, the various states enacted rating laws which required among other things the filing of Inland Marine rates. As a result of these state laws, in 1947 the conference became known as the Transportation Insurance Rating Bureau (TIRB) (transportation having to do with Inland Marine insurance). The TIRB operated nationally as

a recognized statistical agent and a licensed rating organization in each state.

TIRB had little resemblance to AAIS as it operates today. TIRB existed primarily to service the needs of insurers who deviated from the major industry programs. It also provided a forum for mutuals to have a voice in determining their coverage and price requirements. (At the time, mutuals were denied any governing role at the major industry rating bureaus.) TIRB allowed mutuals, stocks and reciprocals alike to participate in the governing of its affairs. AAIS has always operated as a voluntary association with no adherence requirement that companies use information or products that it provides.

During the 60's the major insurers, including the large mutuals sponsored national rate service organizations to service multiple lines insurance. TIRB cooperated with these organizations and also furnished its statistics to them.

The Insurance Services Office assumed the assets, functions, and products of these major industry sponsored organizations in the early 1970's.

With the formation of the Insurance Services Office, the traditional dichotomy of stock versus mutual shifted to large versus small and medium size insurers. Many of the smaller insurers which were affiliated with TIRB desired to maintain their own rate service organization. These companies urged TIRB to expand to accommodate the casualty services which had been provided by a sister organization which was to default to the ISO. TIRB responded by expanding its

license, and with the permission of the sister organization, it took over the filings for additional lines of insurance countrywide. It was this expansion which gave rise to the new organization and the name change to the American Association of Insurance Services.

Companies report their statistics to AAIS for a variety of reasons. The primary one is to comply with statutory requirements. Another reason is to provide a basis for association ratemaking. In this regard, AAIS utilizes only the data of companies which use the association sponsored programs of rules and rates in determining the rate indications. The other data reported, while they remain in the statistical data base, are isolated from the rate reviews. It is this specific and homogeneous type of date review which helps the smaller insurers affiliated with AAIS to compete with large insurers in the competitive insurance market.

The AAIS statistical plans utilize a coordinated approach. In fact, we could consider all of the AAIS plans as being a single statistical plan which is separated into modules to accommodate separate lines of insurance activity. The modules are, however, self-contained statistical plans in their own right.

This approach is clearly user-oriented. The user is not required to understand or become familiar with lines in which the company is not active. Many smaller insurers do not write all lines. Generally speaking, the smaller company specializes in a few lines and therefore, finds it cumbersome to deal with the complexity of an integrated statistical plan as furnished by other rating organizations.

The AAIS approach supports accurate reporting. The utilization of data processing technology in smaller companies lags behind the developments in the major industry. AAIS, therefore, must deal with companies which report on bordereau listings or on key-punched cards. AAIS will conceivably be involved with this complexity of reporting for many years. We are, however, also equipped with modern data-processing communications technology to accommodate larger insurers, as well. The association is also exploring ways to help smaller companies gain access to the latest technology. This is another example of how AAIS helps companies remain competitive.

Possibly the greatest advantage of reporting data to AAIS is the accessibility of the statistical data. All of the reports which are developed for rate reviews are available to each affiliated company along with similar reports with a company's own data. Each company can, therefore, better judge what its own rate levels should be in reference to the average levels provided by AAIS. In addition, AAIS provides a series of standard reports. For instance, we provide multi-dimensional reports which display cause of loss by policy size. All parameters that our statistical plans provide can be specified and run expeditiously. A sample of report offering is attached.

AAIS is a voluntary association of insurance companies and as such must function in an economical manner. In other words, AAIS must function and provide service products to its affiliates at a lower cost than the individual insurer would otherwise have to accommodate itself. We provide collectively the functions which would have to be repeated within each company (or by a consultant).

Our comments are arranged according to anticipated points of interest, and they are qualified. These are comments made by M.H. DeYoung as president of AAIS. It is not to be assumed that they reflect the position of individual companies served by AAIS.

WHAT IS THE CURRENT BENEFIT TO THE CONSUMER OF THE COLLECTIVE RATEMAKING ANTI-TRUST EXEMPTION?

The first benefit, is the clear recognition that regulation of insurance rates is within the province of state administration. Any narrowing or lifting of the exemption will act to confuse this jurisdiction and will probably result in an increased cost due to dual federal and state involvement. We believe that regardless of what the federal government does about McCarran, the current layer of state regulations will continue to exist.

The exemption allows AAIS to provide a needed service to the smaller insurance companies which, in turn, serves consumers better because it enables more companies to compete in the marketplace. Because under the shield we are able to provide price information which is based upon the average loss costs and average expenses of similarly operating insurers, the AAIS companies compete with general assurance of rate adequacy. This assurance of rate adequacy would be absent if the exemption is removed.

The price stability that is afforded by the collective ratemaking activity serves a most important consumer benefit -- the assurance that industry solvency will be maintained and that all losses will, therefore, be payable. Even without the exemption the regulatory concern of each state is with solvency. Regulators depend

on the average indications to determine criteria for price adequacy, non-excessiveness, and fairness of discrimination.

IF THIS EXEMPTION IS REMOVED, WHAT WOULD BE THE EFFECT ON THE AVERAGE CONSUMER?

We have heard from management of major insurers that there would be no impact on the consumer if the exemption is removed. The point being that the major industry would be able to underwrite all of the insurance when the smaller companies were unable to compete due to increased costs of operation. AAIS staff takes issue with this view. We contend that our functions and service products are no different from functions and service products that would be provided individually within the major industry companies -- at least until the AAIS service was provided to a substantial share of the market.

At the moment, we serve a minority share of the market. Our collective share is in line with the market shares of the larger single insurers. Certainly we are not a threat to competition in any sense of anti-trust. (With recent mergers, we are not at all sure what level of market share triggers an anti-trust concern.)

We have read repeatedly that concertive pricing activity is a per se violation of anti-trust. Despite these assertions, AAIS does not act in any manner of agreement to "fix" a price for insurance, other than to satisfy the filing requirements of a state. And, in this regard, we provide to consumers a basis for assuring the adequacy, non-excessiveness and fair discrimination of prices. Even under a strict regulatory environment, the AAIS companies most often deviate according to their own level of expenses. Such deviations are

maintained as independent actions. There is, therefore, rate competition among AAIS companies as well as among all other companies within the industry.

The removal of the exemption would cause confusion and as has previously been stated would cause an increase in the operations cost for each of the affiliates of AAIS. The increased cost incurred by AAIS companies would impact adversely upon consumers.

WHY ARE THERE RATE-MAKING BUREAUS?

First, we exist to provide cost efficiencies with functions which are common to all insurers. We exist to provide research and development. Research is becoming far more important these days. With the extreme changes which are occurring, new business developments require new insurance approaches. The insuring public is served by our research which provides coordinated coverage options with recommended rate levels to underwrite the anticipated risk. Two examples of recent new coverage developments are home computers and dish antennas. Companies turn to us for guidance on how to provide this coverage at adequate rates and for help in drafting policy language.

We provide a forum for collecting all of the pertinent loss information. In some instances, large insurance companies have sufficient loss data to forecast adequate pricing requirements on their own. Smaller companies cannot forecast accurately on the basis of their own data alone, and therefore, must rely more heavily on the aggregate loss data collectd by AAIS.

Our existence enhances competition by providing easy entry (and exit) of companies into new markets. AAIS companies are, generally speaking, growth-oriented and they are continuously expanding into new markets served by AAIS.

There simply do not exist enough technical experts for each company to have its own technical services department. AAIS provides a pool of technical expertise. In this sense we are the technical arm of each company that we serve.

WHAT IS THE ROLE OF THE INSURANCE COMPANY EXPENSES IN THE RATEMAKING PROCESS?

AAIS does not take a philosophical position with regard to the inclusion or exclusion of expenses in establishing rate indications. We recognize the need of smaller insurers to pool expense data even as they pool loss data to determine their pricing needs. Their problem is one of how to divide a single person between various lines of insurance that he administers. On an all lines basis, they know what their expenses are, but they simply have not separated the expenses to the separate insurance lines as required to establish prices for each line. Through jointly sharing of expense data and with research provided by AAIS, an equitable average expense allocation is made to the separate insurance lines.

Once again, we emphasize that we take no philosophical position for including or excluding insurance company expenses in the ratemaking process. We provide information in either format as needed.

COULD SMALLER INSURANCE COMPANIES HAVE LOWER RATES IF THEY DID NOT PARTICIPATE IN RATING BUREAUS?

The answer is emphatically no. We have looked at the average performance of insurers which claim to be independent against those who are affiliated with AAIS. As to the loss ratio, AAIS companies tend to produce better loss experience. From the expense ratio standpoint, the independent companies tend to expend more than the AAIS companies. These facts confirm the assertion that AAIS provides functions which otherwise must be accommodated at each insurance company and that our services are beneficial to consumers.

IF RATING BUREAUS JUST COLLECTED THE STATISTICS COULD COMPANIES MAKE THEIR OWN RATES?

This has been addressed in the above comments. We would qualify "rate" to necessarily fit within the criteria of being adequate and not excessive and of being applied without unfair discrimination.

Smaller companies, it has been suggested, can easily follow the rates which are administered by larger insurers. However, this puts them in an untenable position of following a rate that may have been deliberately lowered and is inadequate with the intent to capture a greater market share. It would be hazardous for any smaller company to select its rates on this basis. Without a measuring point for determining the adequacy point as furnished by AAIS, the smaller companies would have to either hire technical expertise or use consultants and, therefore, their costs would increase should they be required to "make their own rates."

WHAT IS THE ROLE OF THE RESIDUAL MARKETPLACE?

Regardless how refined risk classifications become, there will always be exceptions within each classification that are not underwritten within the open market. The fact that loss experience of the residual market is consistently greater than the premiums will support is evidence of the underwriting wisdom that is applied in the open market. While the residual market is a social problem, we believe the insurance industry has come to recognize its support as being a cost for conducting business. We believe that the current mechanisms should be perpetuated in any event, and with special allowance for concertive activities. Substantial evidence exists to support forms of regulation which allow a market driven insurance economy to exist as such an economy tends to depopulate the residual market.

WHAT ROLE DOES REINSURANCE PLAY IN RATE-MAKING?

We decline to comment here beyond acknowledging that re-insurance is transacted exclusively from direct insurance. As to reinsurance rate-making, we are not involved with the procedures of a reinsurer to separate the ceded portion of risk and to establish a rate for it.

WHY IS THE BUSINESS OF INSURANCE DIFFERENT FROM OTHER BUSINESS IN THE FACT THAT IS NEEDS AN ANTI-TRUST EXEMPTION?

The extremely high degree of public interest with insurance is reflected by its regulation. Because of this public interest, insurance has been included with other businesses which by tradition have been exempteed from anti-trust.

Any consideration to restrict or to eliminate the McCarran exemption must anticipate new dimensions of regulatory administration. Most recently we have witnessed the federal government's rescue of a major bank to avert an adverse public interest effect. The solvency issue with insurance cannot be swept aside or diminished by a mandate for companies to establish their own rates in an open market. To the extent that rating organizations are prohibited from helping companies to determine adequacy or to furnish to regulators with the information regarding adequacy criteria, government will necessarily have to fill this role should such current activities be prohibited.

Insurance is dissimilar from most industries by the fact and nature of risk determination. The only current effective method that we have for measuring risk is upon an assumption of continuity of past experience. By collecting the losses which have occurred during a past period, we can project within certain tolerances of accuracy, what the prospective average cost for a specific classification of risk will be. Again, we do not have, nor do we expect to have soon any better tools than statistics for determining this necessary business fact. Cost information is crucial to the efficient operation of any industry and cost information based on past statistics is a crucial peice of information for each company in the insurance industry. Therefore, concertive activity in the development of average rates should be allowed, but an average rate should not be required to be used by any insurer.

As indicated earlier, we are joined in this statement by the National Associaiton of Mutual Insurance Companies. This organization, NAMIC, was founded in 1895 and currently has more member companies, and a greater variance in the size of these companies, than any other property and casualty company insurance trade association operating nationally. The bulk of the membership of the National Association of Mutual Insurance Companies is made up of rural, property and casualty carriers that serve the farmers and ranchers of this nation; however, many large mutuals are also on the rolls of NAMIC. The Association has traditionally stood for the maintenance of the mutual insurance concept -- neighbor helping neighbor -- which was carried West by the pioneers of our nation. Many of the member companies of NAMIC are over 100 years old and have provided insurance coverages at costs below what would otherwise have been the case had these companies not been present. They have done so, consistently, throughout the varying cycles of interest in the rural consumer of insurance exhibited by larger companies. It is our belief that they form the bedrock of the insurance marketplace in the rural areas of our country.

Many of NAMIC's members utilize the services of the rating bureaus you have heard from today. They must have this information or cease to offer certain coverages to their insureds. Some members do not belong to rating bureaus. Even those who do not utilize rating bureau services, however, are grateful that a scientific cross-check for the rates being charged by their company is available against which to measure the premium or assessment which must be paid by the

insured. Thus it can be said, ironically, that the rating bureaus serve a purpose even to those who are non-subscribers. It can also be said, that in the absence of such rating bureaus, many companies would wander dangerously through the thicket of rates which must be quoted and charged, without benefit of the experience of history or the law of large numbers upon which the principle of insurance is based. Such inaccurate wandering would have to eventually result in the death or serious impairment of these companies.

We think that the particulars which have preceded this in our joint statement are technically correct and dispositive of the main thrust of the Committee's call as we understand it.

We would like to reflect a moment on the need for the anti-trust exemption currently enjoyed by the insurance industry. We think that the basis for this need is the unique nature of the products which we offer. We offer, simply, a promise to pay in the future in the event of a certain contingency. To adequately fund that promise and make it certain of performance, information must be gathered and shared, over a wide geographical area and over a long period of time, in order to properly allocate the risk among all insureds. No other industry, no other segment of our economy is faced with this unique challenge. It is the uniqueness then of our responsibility which makes necessary the exemption currently in place. Further, the fact that the exemption makes possible dynamic and meaningful state regulation, which is clearly in the best interest of both the companies and the consumers of this nation in an area as complex and differentiated as the insurance needs in or country, makes it worthy of continuance.

We both want to thank the Committee again for the opportunity to appear before you today, and to bring the views of our members to you.

Chairman RODINO. Thank you very much.

Mr. Donald DeCarlo.

Mr. DECARLO. Thank you, Mr. Chairman.

The National Council on Compensation Insurance is a licensed rating organization for workers' compensation in 32 jurisdictions. We're not a lobbying organization. However, I think I can help this committee with an overview of the activities of the National Council on Compensation Insurance.

We're involved in designing workers' compensation data bases, collecting and monitoring data to ensure integrity of that data for developing occupational classifications and rates for workers' compensation insurance.

The data bases maintained by the NCCI necessarily provide credibility to the more than 600 occupational classifications. These classifications are based on the nature of an employer's business and are not affected by geographic location or personal characteristics of the employees.

It's commonly recognized that statistical accuracy increases with the size of the sample. Even larger carriers do not have sufficient data to form their own credible data base for all classifications. Smaller carriers need this assistance to even a greater extent. Since larger carriers do not have sufficient data to establish rates for the 600 classes, then clearly the smaller carriers would not be able to develop such data on their own.

Indeed, it's questionable whether smaller carriers could prudently enter into the marketplace at all without guidance and information supplied by the NCCI.

Classification rates and any accompanying rules are filed in States where the NCCI is licensed to do so on behalf of its members. In some States the rates and other filings are advisory, while in other States members of the NCCI are required to adhere, though provision is made for deviations and other adjustments by individual carriers.

Competition in workers' compensation insurance is through State statutes and de facto competition. The diversified services of the NCCI are being performed in an atmosphere of increasing competition in the business of writing workers' compensation insurance. The vast majority of States of this country have enacted prior approval statutes in which a rating organization such as the NCCI is authorized to propose rates to the State regulator for approval.

About one-third of the States have enacted some type of competitive rating law or are currently considering legislative changes in that direction.

There are three significant factors in the development of competitive rating laws. First, the movement towards competitive rating laws, while increasing, is still in the embryo stage. The first such law was enacted only in 1981.

Second, State legislators have chosen diverse paths to force competition under the particular circumstances present in their State. Some States emphasize elimination of prior approval of rates; others emphasize rating organization filings must be limited to accumulated loss experience, not rates; and still others place their emphasis on precluding certain cooperative activities in ratemaking.

Third, State legislators have recognized that while competition should be encouraged, consideration must also be given to ensuring that mandatory workers' compensation coverage is available and affordable and due consideration is given to ensuring the availability of rating information.

The Illinois law is typical in its recognition that promotion of competition depends on availability of necessary statistical information and rate guidance to serve insurers and protect the public, and in my paper I have an example of the Illinois law.

I do not advocate that one of these approaches best fosters competition. Frankly, with all of the laws having been enacted in the past 3 years, there has not been sufficient experience to make such an evaluation, but I would like to emphasize that the various State legislators, acting to boost competition while maintaining access to reliable rating information, have opted for different approaches which they consider best suited to their needs in the particular State.

De facto competition is the actual marketplace working without a specific statute requiring such activity. Such examples would be, at the front-end of the pricing process, many insurers have liberally taken advantage of the opportunity to request deviations for manual rates in all States where NCCI operates, and these deviations are routinely approved by regulators. Moreover, scheduled rating, retrospective rating, and other rating plans affect competition in workers' compensation.

Of course considerable competition also takes place at the end of the pricing process in the form of dividends. These are dividends not to stockholders but to policyholders. In 1983, members of the National Council gave back in the form of dividends $1.5 billion, which encourages safety and is a form of competition.

The effects of repeal or narrowing the McCarran-Ferguson exemption would be of substantial concern to a rating organization whose practices we feel are procompetitive.

The only case on point as to a rating organization and their activities is the old *South-Eastern Underwriters* case, and we clearly know, without the McCarran-Ferguson protection, price fixing in concert would be illegal.

Beyond that, analogies to other cases—in fact, a case cited by Professor Fox, the *BMI* case—are really no help, and considering the severe penalties for violations of the antitrust laws, there would be no comfort in operating absent that protection.

Chairman RODINO. Mr. DeCarlo, we'll have to ask you to conclude your testimony, because we've got to go over to the floor to vote, and you've already consumed more than 5 minutes.

Mr. DECARLO. OK, Mr. Chairman.

In conclusion, the antitrust laws are vague in connection with rating bureaus; there does not appear to be a comfort level considering the severe sanctions for even an inadvertent violation; workers' comp systems, laws, and insurance have served the public well over the last 70 years; the very existence of NCCI promotes procompetitive, proconsumer objectives; NCCI exists in order to provide information in the marketplace both to insurers and to consumers about the loss history, trends, various pricing levels, rating plans.

Since most rate service organization activities are procompetitive but are indirectly related to the pricing mechanism, it seems likely that many such beneficial services would be chilled, if not precluded, by a significant dilution of McCarran-Ferguson.

Thank you very much.

[The statement of Mr. DeCarlo follows:]

Statement of Donald T. DeCarlo,
Vice President and General Counsel,
National Council on Compensation Insurance (NCCI)
before
The Subcommittee on Monopolies and Commercial Law
of the Committee on the Judiciary,
United States House of Representatives

INTRODUCTION

The National Council on Compensation Insurance (NCCI) is a voluntary, non-profit research, statistical and licensed rate making organization, specializing in workers compensation insurance. NCCI is an unincorporated association of 719 insurance companies, including mutual and stock companies, and state funds, all of whom are members or subscribers, and to whom services are provided as outlined in NCCI's Constitution. The organization's central function is the collection of workers compensation loss and expense statistics and the development of workers compensation premiums, rates, classifications and policy forms. In addition, NCCI also has the important responsibility of serving as administrator of various workers compensation assigned risk plans and reinsurance pools.

I wish to emphasize that NCCI is not a lobbying organization and cannot state the insurance industry's position on legislative matters. I can, however, provide the committee with an overview of the diversified activities of the NCCI in the increasingly competitive business of workers compensation insurance.

ACTIVITIES OF THE NCCI

The NCCI is involved in designing workers compensation data bases and collecting and monitoring data to ensure the integrity and utility of the data base as a tool for developing occupational classifications and rates for workers compensation insurance. The data base maintained by NCCI is necessary to provide credibility to the more than 600 occupational classifications. These classifications are based on the nature of employer's business and are not affected by geographic location or personal characteristics of the employees. It is commonly recognized that statistical accuracy increases with the size of the sample. Even larger carriers do not have sufficient data to form their own credible data base for all classifications. Smaller carriers need this assistance to even a greater extent. Since larger carriers do not have sufficient data to establish rates for the 600 classes, the smaller carriers would not be able to develop such data on their own which might result in smaller carriers not entering the market or increasing rates for the unknown risk factor to the detriment of the policy holders. Indeed, it is questionable whether smaller carriers could prudently enter into the marketplace at all without guidance and information supplied by NCCI. Classifications, rates and any accompanying rules are filed in states where the NCCI is licensed to do so on behalf of its members. In some states, the rates and other filings are advisory, while in other states, members of NCCI are required to adhere to bureau rates, though provision is made for deviations and other adjustments by individual carriers. Naturally, in the six jurisdictions where there is an exclusive state fund for workers compensation insurance, NCCI's members do not compete and thus, our activities are more limited. Other NCCI functions include the development of policy forms and

endorsements to ensure complete coverage as required by law under the varied state and federal workers compensation statutes; evaluations of benefit changes under the workers compensation law for any interested party, including federal and state legislators, state regulators, insurers, labor, or researchers, seeking an analysis of the impact of changes in workers compensation laws; and economic and actuarial research which is made available to both our members and the public. The NCCI also serves as administrator for numerous assigned risk plans and pools, and serves as an advisor to other plans and pools.

COMPETITION IN WORKERS COMPENSATION INSURANCE - STATE STATUTES

The diversified services of the NCCI are being performed in an atmosphere of increasing competition in the business of writing workers compensation insurance. The vast majority of the states of this country have enacted prior approval statutes in which a rating organization such as NCCI is authorized to propose rates to the state regulator for approval. That approval may result from either a hearing by the regulator, or by the regulator merely allowing newly filed rates to go into effect. About one-third of the states have enacted some type of competitive rating law or are currently considering legislative changes in that direction. There are three significant factors in the development of competitive rating laws. First, the movement towards competitive rating laws, while increasing, is still in the embryo stage; the first such law was enacted only in 1981. Second, state legislators have chosen diverse paths to foster competition under the particular circumstances present in their state; some states emphasize elimination of prior approval of rates; while

others emphasize that rating organization filings must be limited to accumulated loss experience, not rates; still others place their emphasis on precluding certain cooperative activities in ratemaking. Third, state legislators have recognized that while competition should be encouraged, consideration must also be given to ensuring that mandatory workers compensation coverage is available and affordable, and that due consideration is given to ensuring the availability of rating information, both for the information and protection of the public, and to guard against the growing threat of insurer insolvency. These goals may be accomplished only be permitting certain cooperative activities among the competing insurers.

Thus, the Minnesota competitive rating law recognizes that one of its purposes is to "promote quality and integrity in the data bases used in workers compensation insurance ratemaking." The Illinois law is typical in its recognition that the promotion of competition depends upon the availability of necessary statistical information and rate guidance to serve insurers and protect the public.

Thus, the Illinois law permits:

Cooperation among rating organizations and companies and specifically, permits a rating organization to require that its members adhere to

rate classification systems
rating rules
rating plans
policy forms
underwriting rules

However, the Illinois Law prohibits agreements to adhere to, and other cooperative action as to:

rates
schedule rating plans
regulation of dividends

This is where the competitive balance has been struck in Illinois.

As another example, the new competitive rating bill in Vermont requires adherence to the manual rules and uniform experience rating plans of designated service organizations; however, insurers are required to take some affirmative rate action by either making an independent rate filing or adopting the rates and supplementary rating information of a service organization or another insurer. In addition, insurers are permitted to develop sub-classes of manual classifications.

A list of those states which have adopted competitive rating laws and a summary of important provisions relating to rating organizations is attached as Appendix A.

I do not advocate that one of these approaches best fosters competition. Frankly, with all of the laws having been enacted in the past three years, there has not been sufficient experience to make such an evaluation. But I would like to emphasize, that the various state legislatures, acting to boost competition while maintaining access to reliable rating information, have opted for different approaches which they consider best suited to the needs of their particular states.

INCREASED DE FACTO COMPETITION IN WORKERS COMPENSATION INSURANCE

Increased competition has not been limited to the enactment of

state competitive rating laws. All jurisidictions have experienced an increase in de facto competition due to the way insurers market their workers compensation business.

At the front end of the pricing process, many insurers have liberally taken advantage of the opportunity to request deviations from manual rates in all states where NCCI operates, and these deviations are routinely approved by regulators. Moreover, schedule rating plans filed by NCCI in at least ten states and by individual insurers in several other states give insurers the right to adjust manual rates based on their judgment of an individual risk's characteristics such as condition of the risk's premises, medical facilities available, use of safety devices, employee selection, training and supervision, and management cooperation and attention to safety.

Of course, considerable competition also takes place at the end of the pricing process, i.e., in the form of dividends, as both stock and mutual insurance companies return significant dividends to policy holders at year's end. The net effect of these competitive practices can be appreciated in the attached chart (Appendix B) showing the number of workers compensation insurance rate deviations in the State of Florida, a state with a prior approval rating law.

EFFECTS OF REPEAL OR NARROWING OF McCARRAN-FERGUSON EXEMPTION

The question has been asked how NCCI might operate absent the McCarran-Ferguson exemption or under a more narrow exemption. The answer to this question is uncertain as antitrust decisions are constantly

changing the interpretations of antitrust laws, and are vague as to rating service activities. Under the decision of the Supreme Court in United States v. South-Eastern Underwriter's Ass'n, 322 U.S. 533, rehearing denied, 323 U.S. 811 (1984), we can be reasonably certain that agreements to make final rates would be per se violation of the antitrust laws, but we cannot be certain of anything else. For example, it has been suggested by Professor Fox, who testified before this committee in April, that even without broad McCarran- Ferguson protection, ratemaking organizations could collect past loss data for pure premium calculations under the decision of the Supreme Court in Broadcast Music, Inc. v. CBS, 441 U S. 1 (1979), the decision holding that the issuance by the music publishing clearinghouses ASCAP and BMI of blanket licenses to perform copyrighted music is not a per se violation of the federal antitrust law. I think it is safe to say that rating organizations would find little comfort in this decision which attempted to resolve over fifty years of antitrust uncertainty surrounding these clearinghouses. Indeed, courts relying upon the BMI case as precedent for the type of lenient antitrust treatment suggested by Professor Fox have been quickly disappointed. For instance, in Arizona v. Maricopa County Medical Society, 643 F.2d 553 (9th Cir. 1980), the Court of Appeals, following BMI, applied a rule of reason analysis to the defendants' system of setting maximum fees for its physician members. The Supreme Court promptly reversed in Arizona v. Maricopa County Medical Society, 457 U.S. 332 (1982), finding the reliance on BMI misplaced because of the peculiar facts presented in the BMI case. The pooling of musical copyrights is a far cry from the collection and dissemination of past loss data, particularly since past loss data is relevant to the sensitive antitrust area of pricing. I also note that the Supreme Court in BMI v. CBS gave great weight to the unique antitrust backgound of BMI & ASCAP and

the fact that the music clearinghouses had been acting within the constraints of earlier antitrust consent decrees for several decades. In any event, insurance is a unique contract for the future; unlike the case of fungible goods, the transaction begins with the delivery of the product, i.e., the insurance contract. In many instances, past loss experience is of little utility without at least some attempt to analyze future trends. For example, in the realm of occupational disease, past loss experience for asbestos-related and coal dust-related diseases prior to 1975 would be of little utility in predicting the asbestos and black lung claim landslide that occured several years thereafter. The NCCI analyzes future trends not only for its ratemaking activities, but also in its research activities, such as analyses of the impact of proposed legislation for the benefit of interested parties. The NCCI is currently involved in a National Association of Insurance Commissioners study of the compensation and funding problems caused by occupational diseases on the state workers compensation systems. Such activities which are clearly not uncompetitive, and which benefit our members and the public as well, would nevertheless be chilled because strict antitrust scrutiny applies to any cooperative activity which is even tangentially related to predictions of future prices.

NCCI activities which work to a pro-competitive end in the de facto rate competition which I discussed would also be jeopardized. Schedule rating plans foster competition by encouraging a consideration of the individual characteristics of a risk. Without these plans, carriers, particularly smaller carriers, would not have the resources to provide such individualized rating and the result would inevitably be anticompetitive standardization of rates for disparate risks. Yet the plans themselves, which encourage individual carriers to make independent

assessments of individual risks, would be in jeopardy.

Another valuable service of NCCI which would be suspect under the antitrust laws is the standard policy and endorsements. The standardization of coverage is not anticompetitive; indeed standardization is necessary to ensure that all risks are insured for all relevant work-related injuries as is required by the various state workers compensation laws. Insurers cannot compete by offering less than the coverage required by law; full coverage is mandatory. Individual insurers would lack the expertise and economic motivation to provide forms and endorsements which are in compliance with all state and federal insurance requirements.

The NCCI just completed a six year project which culminated in a new Standard Policy clarifying coverage for occupational diseases. Most significantly, the policy is written in clear and simple language which can be understood by lay individuals. While many states require life and casualty policies to be written in clear and straightforward language, only a handful of states applied this requirement to workers compensation policies. Without NCCI efforts, it is doubtful that any carriers would have invested the resources and the time required to implement an improved policy on a nationwide basis. The 1984 Standard Policy has now been approved in all states. Of course, a policy which can be understood by the consumer will encourage competition, yet the very standardization which is necessary would be suspect under the antitrust laws.

The NCCI's administration of state assigned risk plans and reinsurance pools is another service the status of which would be unclear. Even states with the broadest possible competitive rating laws, such as Kentucky, permit cooperative ratemaking in the assigned risk market; competition is not threatened since this coverage is mandatory, and is almost

invariably provided at a considerable loss. The availability of this coverage, and protection against insurer insolvencies, are the paramount considerations in this marketplace. The high risk employer might be unable to commence or continue its business operations absent assigned risk plans. It is therefore the policy holders who would suffer most from curtailment of these activities. But the federal antitrust consequences of cooperative ratemaking in assigned risk markets would be unclear at best. As was evident from Professor Fox's presentation, it is questionable whether NCCI would find any comfort in the "state action" exemption if the present exemption were modified. The statutory schemes of the various states permit, but do not require, the various activities of NCCI that I have discussed. Thus, the lack of state compulsion which may be a necessary element of the "state action" defense is absent. United States v. Southern Motor Carriers Rate Conference, 702 F.2d 532 (5th Cir. 1983).

CONCLUSION

In sum, the antitrust laws are vague in connection with rating bureaus, and there does not appear to be a comfort level considering the severe sanctions for even an inadvertent violation of the law. Workers compensation systems, law and insurance have served the public well over the last 70 years, and with particular regard to insurance, legislated competitive rating and the de facto competitive actions of insurers make the marketplace more competitive than it has ever been while maintaining the essential flow of information and guidance provided by rate service organizations.

The very existence of NCCI promotes pro-competitive and pro-consumer objectives. NCCI exists in order to provide information to the marketplace

(both insurers and consumers) about loss history, trends, various pricing levels, rating plans, and other necessary information. Without this information provided by NCCI, many small insurers, who use NCCI information to greatly lower the cost of entry into the marketplace, could not themselves compete in the workers' compensation insurance market. In addition, NCCI's information protects the small consumer from improper discrimination. Thus, NCCI's providing information in reliance upon the McCarran-Ferguson exemption to both competitors and consumers allows the insurance marketplace to function more effectively and to the greater fulfillment of competitive and consumer objectives.

I appreciate the opportunity to have appeared before the Subcommittee and offer my further assistance.

APPENDIX A

Summary of Statutory Provisions in States which have enacted Competitive Rating Laws

As of September 1, 1984, the following state have enacted competitive rating laws, see attached law summaries.

Arkansas
Georgia
Illinois
Kentucky
Michigan
Minnesota
Oregon
Rhode Island
Vermont

The following is a brief summary* of the laws pertaining to the powers of rating organizations in states with competitive rating laws:

* All statutory summaries (except for the recently enacted competitive rating bill in Vermont) are reprinted from Workers' Compensation Rating Laws - A Digest of Changes, Appendix C.

ARKANSAS

Effective Date: June 17, 1981

Senate Bill 557 has been viewed as introducing competitive rating to workers' compensation in Arkansas by providing in Section 66-3120 (Subsection (a) (1)) that every insurer is to file with the Commissioner every manual of classifications, rules and rates, every rating plan, and every modification of any of the foregoing which it proposes to use. Insurers are also required to file with the Commissioner every manual, minimum, class rate, rating schedule or rating plan, and every other rating rule and every modification of any of the foregoing which it proposes to use. Subsection (a) (4) completed this transition by providing that an insurer may satisfy the above filing obligation by reference to the rates and supplementary information filed by a licensed rate service organization with which the insurer is a member or subscriber. However, it must be noted that filings made by a licensed rate service organization shall be for advisory purposes only and shall not be made on behalf of any insurers.

While embracing competitive rating, the new law states that each of the above-mentioned filings shall state a proposed effective date which shall not be less than thirty days after said filing. A filing shall be deemed to meet the requirements of this Section unless it is disapproved by the Commissioner within 30 days of the filing.

Senate Bill 557 did not tamper with the procedure for the filing of policy forms. Such filings are still governed by the provisions of Section 66-3209 of the Arkansas Insurance Code which requires that all policy forms be filed with the Commissioner and be approved before their use.

The residual market is governed by Section 66-3115 (apportionment agreements among insurers) of the Arkansas Insurance Code. The section provides that agreements may be made among insurers with respect to the equitable apportionment among them of insurance to be afforded applicants who are unable to procure insurance through ordinary methods. The section further provides that insurers may agree among themselves on the reasonable rate modifications.

GEORGIA

Effective Date: January 1, 1984

Georgia's approach to competitive rating was ushered in with the enactment of Senate Bill 379. Pursuant to Section 3 of the act (new Code Section 33-9-21), "every insurer shall maintain with the Commissioner copies of rates, rating plans, rating systems, underwriting rules, and policy or bond forms used by it." The same section continues on to qualify the above requirements by providing that the maintenance of the above items with the Commissioner by a licensed rating organization of which an insurer is a member or subscriber will be deemed sufficient compliance to the extent that the insurer uses, or in the case of a workers' compensation insurer uses or proposes to use, the rates, rating plans, rating systems, underwriting rules, and policy or bond forms of the rating organization. However, "when he deems it necessary," the Commissioner may require the above items to be filed by insurers independent of any filing made on its behalf or as a member of a licensed rating organization.

Subsection 2 of new Code Section 33-9-21 further provides that, "when he deems it necessary," the Commissioner may require workers' compensation insurers "to file such insurer's own individual rate filing for premium rates to be charged for workers' compensation coverage written in this state. Such premium rates shall be developed and established based upon each individual insurer's experience in the State of Georgia." The Commissioner is also authorized to accept such rate classifications as are reasonable and necessary for compliance with this chapter, or he may set said rates for said insurer on the best information available. In addition, the Georgia rating law is further modified by deleting a requirement that insurers file policies for workers' compensation at a rate prescribed by the Commissioner.

As for the residual market, pursuant to new Code Section 34-9-133, the State Board of Workers' Compensation shall prescribe rules and regulations for apportioning rejected workers' compensation policies and may establish an equitable assignment of such policies. This provision is qualified to the extent that the Insurance Commissioner is authorized to establish or approve a method to apportion on a pro rata basis any rejected workers' compensation policy where four insurers have refused in writing to cover said risk. (In formulating this method of assignment, a minimum loss ratio will be considered by the Commissioner.) After the above rejection, such established or approved method of assignment shall assign an insurer to write such risk.

ILLINOIS

Effective Date: August 18, 1982. However, many of the changes embodied in the new law will not become operative until January 1, 1983.

Senate Bill 1496 establishes a form of competitive rating for workers' compensation by amending various sections of Article XXIX of the Illinois Insurance Code.

Pursuant to Subsection (1) of new Section 457 of the law, every company is to file with the Director every manual of classifications, every manual of rules and rates, every rating plan, and every modification of the above which it intends to use. Such filings shall be made on a use and file basis, with the required filings being made not later than 30 days after they become effective. A company may satisfy the above filing requirements by adopting the filing of a licensed rating organization of which it is a member or subscriber in total or by notifying the Director in what respects it intends to deviate from such filing. An insurer may also adopt the pure premiums filed by a rating organization except that such insurer must file the modification factor it will use for profits and expenses.

Subsection (2) of new Section 457 requires that, beginning January 1, 1983, each licensed rating organization shall file, utilizing a 30-day use and file procedure, every manual of rules and advisory rates, every fully adjusted and fully developed pure premium, every rating plan, and every modification of any of the above which it intends to recommend for use by its members and subscribers. Subsection (2) also requires that the rating organization shall file the rate classification system, all rating rules, rating plans, policy forms, underwriting rules, or similar materials which it requires its members and subscribers to adhere to at least 30 days before their proposed effective date. It should be noted, however, that adherence requirements concerning rates or schedule rating are prohibited, as is cooperation between insurers in making rates or in the use of rates or schedule rating. This latter prohibition was effective upon enactment (August 18, 1982.)

As for the residual market, new Section 468 requires all insurers to participate in a plan providing for the equitable apportionment among them of insurance which may be afforded applicants who are in good faith entitled to, but who are unable to procure, such insurance through ordinary methods. Insurers are required to submit a plan for the Director's approval within 60 days of the Act's effective date. The rates to be used in such a plan must be submitted to the Director for approval at least 30 days prior to their effective date. Furthermore, rating organizations may make and file rates under this section.

KENTUCKY

Effective Date: July 15, 1982

Senate Bill 274 moves Kentucky into the category of a competitive rating law state by providing in Section 5 (KRS Chapter 304, Subtitle 13) that "In a competitive market, every insurer shall file with the Commissioner rates and supplementary information to be used in this state for commercial risks as designated by the Commissioner and for all personal risks." The above referenced filings are generally to be on a use and file basis, with the rates and supplementary rate information to be filed not later than 15 days after the date of the first use of the rates. In addition, every insurer is to file with the Commissioner all rating manuals and underwriting rules that it uses in this state on the same 15-day use and file time frame. The Commissioner may exempt an insurer from filing supporting information if the insurer files by reference, with or without deviation, to a filing which is in effect for another insurer or an advisory organization. (Supporting information is defined as "the experience and judgement of the filer and the experience of data of other insurers or organizations relied on by the filer, the interpretation of any statistical data relied on by the filer, descriptions of methods used in making the rates, and other similar information required to be filed by the Commissioner.")

Pursuant to Section 9(2) of the new law, "every advisory organization shall file with the Commissioner every statistical plan, manual of rating rules, rating schedule, and modification of any of these proposed for use in this state not more than 15 days after it is distributed to its members." However, the next section (Section 10) delineates certain prohibited activities relating to advisory organizations:

1. prohibited from making an agreement with an insurer or another advisory organization that has the purpose or effect of substantially lessening competition in an insurance market;

2. after January 1, 1983, prohibited from compiling or distributing recommendations relating to rates that include profit or expenses, except loss adjustment expenses;

3. prohibited from filing rates or other information on behalf of an insurer.

Section 11 of the new law provides a laundry list of permitted activities for an advisory organization. For purposes of this summary, it should be noted that among the most important of the permitted activities are:

"1. collect statistical data from members or any other source;
2. develop statistical plans including territorial and class definitions;
3. distribute pure premium data, adjusted for loss development and loss trending, in accordance with its statistical plans;
4. distribute manuals of rating rules and rating schedules, except that manuals may not include final rates or permit calculation of final rates without outside information;...
8. prepare policy forms and endorsements and consult with members and others on use and application;
9. conduct research and field inspections to collect information for calculating rates or collecting statistics relating to individual risks;..."

Section 14 of the new act takes up the question of residual market rates by providing that insurers participating in joint underwriting, pools, or residual market mechanisms may, in connection with such activity, cooperate in the making of rates, rating systems, policy forms, underwriting rules, surveys, inspections and investigations, the furnishing of loss and expense statistics and other information, and the undertaking of research. Any plan or agreement to implement a residual market mechanism is to be submitted to the Commissioner for approval. In addition, rates and supplemental rating information for a residual market mechanism shall not become effective until approved by the Commissioner. (Section 5(5)).

MICHIGAN

Effective Date: January 1, 1983

The ratemaking aspects of workers' compensation in Michigan have undergone considerable change as a result of the enactment in 1982 of House Bills No. 5162 and 5176.

At the outset, it is important to emphasize that, pursuant to Section 2421, an insurer authorized to write workers' compensation is prohibited from being a member of a rating organization in Michigan for workers' compensation or having any rates, rules, or forms files on its behalf with regard to workers' compensation in Michigan by a rating organization. Insurers are generally prohibited from sharing information in establishing rates or rating systems. Furthermore, no insurer shall agree with any other insurer or with an advisory organization to adhere to or use any rate, rating plan, rating schedule, rating rule, or underwriting rule with regard to workers' compensation in Michigan, except as necessary to operate the residual market.

Pursuant to Section 2406 of the new law, every insurer is to file with the Commissioner all rates and rating systems not later than January 1, 1983. Thereafter, the rates and rating systems regarding workers' compensation shall be filed not later than the dates the rates and rating systems are to be effective (file and use). These filings shall be considered to meet the requirements of the rating law chapter unless and until disapproved by the Commissioner pursuant to Section 2418.

For purposes of effectuating the workers' compensation data requirements of the new law, Section 2402 creates a "data collection agency." The data collection agency is to designate one advisory organization for the purpose of collecting historical data from all insurers and compiling pure premium data pursuant to the statistical plans of the designated advisory organization approved by the Commissioner. The designated advisory organization is also to distribute to the data collection agency pure premium data for dissemination to all insurers.

Section 2407 (Subsection 4) contains specific prohibitions regarding the activities of the data collection agency and the designated advisory organization. Neither organization shall collect, compile, or make available to insurers any information regarding:

1. actuarial projections or trending factors
2. profits
3. expenses, except loss adjustment expenses.

Exceptions to this prohibition are allowed to the extent necessary to establish proper residual market rates and studies necessitated by any significant change in a law resulting from a subsequent statute or subsequent court decision.

As alluded to above, the development of residual market rates is to be outside the procedure established for the voluntary market. Pursuant to Subsection (2) (b) of Section 2407, the designated advisory shall make and file rates, rating systems, and policy forms for the residual market in accordance with chapter 23. Subsection (2) (c) further provides that the data collection agency shall establish a plan providing for the collection of data, in addition to pure premium data, by the designated advisory organization to the extent necessary to establish proper residual market rates. The plan is to be submitted to the Commissioner for approval or amendment.

MINNESOTA

Effective Date: July 1, 1983

Chapter 346 of the Minnesota Advance Laws (1981) sets the stage for a gradual transition from a prior approval jurisdiction to competitive rating. It should be noted that during the transition period - July 1, 1983 until December 31, 1985 - rates are to be determined in accordance with rules to be adopted by the Commissioner. Said rules shall require (1) that a hearing be held pursuant to Section 79.071 to consider any petition requesting a modification of rates and (2) that following the hearing, the Commissioner shall adopt a schedule of rates.

The new law presumes the existence of a competitive market (unless after a hearing the Commissioner finds otherwise), and in such a market, each insurer is required to file a complete copy of its rates and rating plan, and all changes and amendments thereto, within 15 days after their effective dates (use and file). An insurer need not file a rating plan if it uses a rating plan filed by a data service organization. However, if an insurer uses a rating plan of a data service organization but deviates from it, then all deviations must be filed by the insurer.

Pursuant to Subdivision 2 of Section 27 (79.26) of the new law, the Commissioner may, in certain instances, require that an insurer file rates at least 30 days before their effective date (file and use). The specific instances referred to in the statute are:

(1) if the Commissioner determines, based upon reasonable evidence, that an order is appropriate due to the insurer's financial condition; or
(2) due to a prior finding of unfairly discriminatory rating practices; or
(3) due to a prior finding of inadequate rates.

Section 29 (79.58) preserves the ability of the Commissioner to disapprove a rate filed by an insurer subsequent to the rate's effective date. The statute states that the Commissioner shall disapprove a rate if, after a hearing on the record, he finds that:

(1) the premium is inadequate or unfairly discriminatory; or
(2) a competitive market for workers' compensation does not exist and rates are excessive; or
(3) the insurer failed to comply with filing requirements.

Similarly, the Commissioner may disapprove a rating plan of a data service organization if, after a hearing, he finds that it is unfairly discriminatory.

Section 30 (79.59) of the new law sets out a number of prohibited activities for insurers and data service organizations. Except as specifically authorized, no insurer shall agree with any other insurer or with a data service organization to adhere to or use any rate, rating plan, rating schedule, rating rule, or underwriting rule. In addition, no data service organization is to participate in the development or distribution of rates, rating plans, or rating rules except as specifically authorized.

MINNESOTA - continued

The required activities for a data service organization are set out in Section 32 (79.61). It should be noted that a data service organization is to prepare a merit rating plan and is required to file statistical plans, including classification definitions, with the Commissioner for approval. A data service organization is also required to prepare a periodic ratemaking report which is to include development factors, trend factors, law evaluations, and pure premium relativities, but such pure premium relativities are <u>not</u> to include a loading for expenses or profit.

As for the residual market, Section 34 (79.63) provides that the Commissioner shall appoint a licensed data service organization to administer the assigned risk plan. The appointed data service organization shall submit to the Commissioner for approval a plan and rules for administering the assigned risk plan.

OREGON

Effective Date: July 1, 1982

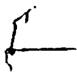
The new Oregon competitive rating law significantly changes the process by which workers' compensation rates are developed for filing. A key change in this process involves prohibiting a rating organization from filing any rates or rating plan values for the voluntary market which include allowances for expenses, taxes, or profit.

The specifics of this new process are set out in Section 737.205 of the Oregon Revised Statutes which generally states that every insurer shall file rates, rating plans, and rating systems used by it. Each filing is to become effective on the date specified therein but not earlier than the date such filing is received by the Commissioner. Furthermore, an insurer may satisfy its filing obligations for workers' compensation rating plans or rating systems by authorizing the Commissioner to accept the filings made by the insurer's rating organization, so long as they do not include allowances for expenses, taxes, or profit. In effect, carriers may reference the rating organization's pure premium indications but must file their own expense loadings. Carriers wishing to use a retrospective rating plan must file their own rating values.

The above paragraph describes a file and use procedure for rates which are not below the advisory pure premium indications filed by the rating organization. However, if an insurer's rate filing includes a rate which is lower than that filed by the rating organization (i.e., the pure premium indications) then the effective date of the filing can be no earlier than the 15th day after the date the Commissioner receives the filing. Such a filing shall be deemed to meet the requirements of the chapter unless disapproved by the Commissioner within the waiting period or any extension thereof.

It should be pointed out that Section 737.560, as amended, requires every workers' compensation insurer, including the State Accident Insurance Fund Corporation, to be a member of a workers' compensation rating organization. The Commissioner is to prescribe by rule the statistical plan for workers' compensation and such statistics are to be reported to the workers' compensation rating organization of which the insurer is a member. In addition, pursuant to Section 737.265, agreements to adhere to a rating organization's filings are otherwise generally prohibited, except as to policy forms - to which adherence is required.

Section 737.312 takes up the question of residual market rates. In rather standard language, the section states "that agreements may be made among insurers with respect to the equitable apportionment among them of insurance which may be afforded applicants who are, in good faith, entitled to such insurance but who are unable to procure such insurance through ordinary methods. Such insurers may agree among themselves on the use of reasonable rate modifications for such insurance, such agreements, and rate modifications to be subject to the approval of the Commissioner."



RHODE ISLAND

Effective Date: September 1, 1982

Senate Bill 2427 introduces a measure of competitive rating to workers' compensation in Rhode Island. Specifically, the new law requires that insurers writing 2% or more of the total workers' compensation and employers' liability premium volume in Rhode Island may not satisfy their obligation to file rates by having a rating organization file on their behalf. Section 27-9-8 applies only to the filing of "rates," and the rating organization may still satisfy the obligation of the 2% insurers (as well as those carriers writing less than 2%) to file with the Commissioner every manual of classification, rules, rating plan, rating system, and every modification of the foregoing which an insurer proposes to use.

Sections 27-9-7 and 27-9-10 of the Casualty Insurance Rating Chapter were not amended by the new law. As a result, the requirement of a 30 day waiting period remains intact as to the required filing of the items set out above. A filing is generally deemed to meet the requirements of the chapter and to become effective unless disapproved by the Commissioner within the waiting period or any extension thereof.

Similarly, Section 27-9-26 of the Casualty Insurance Rating Chapter was not amended by the new law. While permitting deviation filings, the section generally requires members and subscribers of a rating organization to adhere to the filings made on its behalf by a rating organization. Adherence as to policy forms is also permitted in Rhode Island.

The new law has only a marginal effect on the previous residual market structure. Section 27-9-43 was amended to require the filing (and use by all insurers) of all of the manuals of classifications, rules and rates, rating plans, rating systems, and every modification of the same to be used by insurers pursuant to their agreements as to the equitable apportionment of the residual market.

VERMONT

Effective Date: July 1, 1984

House Bill 639 introduces a measure of competitive rating to workers compensation in Vermont. The bill permits individual insurers to file rates on a use and file basis. Schedule rating plans are not permitted.

Under Section 4677 of the Insurance Code, insurers are required to adhere to the uniform classification system, uniform experience rating plan and manual rules that are developed by a designated advisory or service organization, and are required to report their experience to such organization. However, insurers may develop their own subclassifications of the uniform classification system upon which a rate is made.

Under Section 4678, insurers are permitted, but not required, to file by reference to the rates filed by an advisory or service organization or another insurer, but such "reference filing" does not relieve an insurer of its other filing requirements under the law.

APPENDIX B

FLORIDA

TYPE OF DEVIATION

A member of or a subscriber to a rating organization "... may make written application to the department for permission to file a uniform percentage decrease or increase to be applied to the premium produced by the rating system so filed for a kind of insurance, for a class of insurance which is found by the department to be a proper rating unit for the application of such uniform percentage decrease or increase, or for a subdivision of workers' compensation...insurance: (a) Comprised of a group of manual classifications which is treated as a separate unit for ratemaking purposes, or (b) For which separate expense provisions are included in the filings of the rating organization."
(Section 627.211 (1))

CURRENTLY FILED DEVIATIONS

COMPANY	*DEVIATION*	*EFFECTIVE DATE*
Aetna Fire Underwriters Insurance Company	15%	6/1/83
Aetna Insurance Company	10%	6/1/83
Agricultural Insurance Company	15%	9/1/83
AIU Insurance Company	12%	10/1/83
All America Insurance Company	15%	4/1/84
Allstate Indemnity Company	15%	4/1/84
American Alliance Insurance Company	15%	5/1/83
American Automobile Insurance Company	15%	10/1/83
American Casualty Company of Reading, Pennsylvania	25%	10/1/83
American Centennial Insurance Company	20%	6/1/83
American Employers Insurance Company	15%	11/1/83
American Guarantee & Liability Insurance Company	15%	6/1/83
American Liberty Insurance Company	10%	11/1/83
American Manufacturers Mutual Insurance Company	15%	8/1/83
American Mutual Insurance Company of Boston	15%	10/1/83
American Mutual Fire Insurance Company	15%	9/1/83

FLORIDA Continued

COMPANY	*DEVIATION*	*EFFECTIVE DATE*
American Mutual Liability Insurance Company	15%	1/1/84
American States Insurance Company of Texas	15%	8/1/83
American Zurich Insurance Company	25%	7/1/83
Argonaut Insurance Company	15%	11/1/83
Argonaut-Midwest Insurance Company	20%	10/1/83
Aspen Indemnity Company	20%	2/1/84
Associated General Insurance Company	15%	4/1/84
Assurance Company of America	15%	9/1/83
Atlantic Insurance Company	20%	1/1/84
Atlantic Mutual Insurance Company	17%	2/1/84
Automobile Insurance Company of Hartford, Connecticut	15%	12/1/83
Auto-Owners Insurance Company	10%	6/1/83
Bankers Insurance Company	20%	4/15/83
Bankers Standard Fire & Marine Company	20%	11/1/83
Bankers Standard Insurance Company	25%	9/1/83
Bituminous Fire and Marine Insurance Company	15%	2/1/84
Camden Fire Insurance Association	15%	7/1/83
Canal Insurance Company	20%	7/1/83
Casualty Reciprocal Exchange	15%	1/1/84
Catawba Insurance Company	15%	4/1/84
Centennial Insurance Company	17%	2/1/84
Central National Insurance Company of Omaha	15%	Pending
Church Mutual Insurance Company	15%	8/1/83
Cincinnati Insurance Company	15%	2/1/84
Commercial Insurance Company of Newark, New Jersey	15%	4/1/84

FLORIDA Continued

COMPANY	DEVIATION	EFFECTIVE DATE
Compass Insurance Company	15%	10/1/83
Cotton States Mutual Insurance Company	15%	4/1/84
Covenant Insurance Company	15%	8/1/83
Eagle Star Insurance Company of America	15%	7/1/83
Empire Fire & Marine Insurance Company	12%	9/1/83
Employers Mutual Casualty Company	15%	12/1/83
Enterprise Insurance Company	15%	3/31/83
Excelsior Insurance Company of New York	13%	5/1/83
Federated Mutual Insurance Company	20%	6/1/83
Fidelity & Guaranty Insurance Company	15%	7/1/83
Fire & Casualty Insurance Company of Connecticut	15%	3/1/84
Fireman's Fund Insurance Company	25%	10/1/83
Fireman's Fund Insurance Company of Wisconsin	15%	10/1/83
Firemen's Insurance Company of Newark, New Jersey	15%	3/31/84
Florists' Mutual Insurance Company	10%	10/1/83
Globe Indemnity Insurance Company	10%	9/1/83
Graphic Arts Mutual Insurance Company	15%	10/1/83
Great Global Assurance Company	20%	2/1/84
Great Northern Insurance Company	20%	Pending
Great Plains Casualty Corporation	20%	9/1/83
Gulf American Insurance Company	10%	4/1/83
Hartford Casualty Insurance Company	25%	12/1/83
Hartford Fire Insurance Company	15%	1/1/84
Home Insurance Company	15%	6/1/84

FLORIDA Continued

COMPANY	*DEVIATION*	*EFFECTIVE DATE*
Illinois National Insurance Company	12%	11/1/83
Indemnity Insurance Company of North America	20%	9/1/83
Indiana Lumbermens Mutual Insurance Company	15%	1/1/84
Integon General Insurance Company	15%	5/1/83
International Business & Mercantile Reassurance Company	15%	4/1/84
International Insurance Company	12%	7/1/83
Investors Insurance Company of America	18%	4/1/83
Iowa National Mutual Insurance Company	15%	6/1/83
John Deere Insurance Company	15%	4/1/84
Kent Insurance Company	20%	8/1/83
Kentucky Central Insurance Company	12%	2/15/84
Liberty Insurance Corporation	20%	12/31/83
Liberty Mutual Fire Insurance Company	15%	12/31/83
Liberty Mutual Insurance Company	15%	6/30/83
Lumber Mutual Insurance Company	15%	8/15/83
Lumbermen's Mutual Insurance Company	15%	2/1/84
Lumbermen's Underwriting Alliance	15%	4/1/84
Massachusetts Bay Insurance Company	15%	10/1/83
Mid-Century Insurance Company	15%	12/1/83
Middlesex Insurance Company	20%	5/1/84
Midland Property and Casualty Insurance Company	18.5%	1/1/84
Mission Insurance Company	20%	1/1/84
Mission National Insurance Company	22.5%	1/1/84
Morrison Assurance Company, Inc.	15%	8/1/83
National Fire Insurance Company of Hartford	15%	8/1/83
National General Insurance Company	10%	1/1/84

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FLORIDA Continued

COMPANY	*DEVIATION*	*EFFECTIVE DATE*
Nationwide Mutual Fire Insurance Company	20%	8/1/83
Niagara Fire Insurance Company	20%	pending
North River Insurance Company	20%	3/1/84
Northbrook Indemnity Company	20%	8/1/83
Northbrook National Insurance Company	20%	8/1/83
Northern Insurance Company of New York	10%	3/1/84
Northwestern National Insurance Company	15%	1/1/84
Old Dominion Insurance Company	20%	11/1/83
Owners Insurance Company	15%	3/1/84
Pacific Indemnity Company	25%	11/1/83
Peninsular Fire Insurance Company	10%	11/1/83
Pennsylvania National Mutual Casualty Insurance Company	15%	4/1/84
Planet Insurance Company	15%	11/15/83
Preferred Mutual Insurance Company	10%	Pending
RGAF Underwriters Insurance Company	15%	10/1/83
Rockwood Insurance Company	25%	3/1/84
Royal Indemnity Company	15%	9/1/83
Safeco Insurance Company of America	15%	12/1/83
Safeguard Insurance Company	25%	3/1/84
St. Paul Mercury Insurance Company	15%	9/25/83
Select Insurance Company	15%	1/1/84
Shelby Mutual Insurance Company	20%	10/1/83
Southeastern Fire Insurance Company	20%	7/1/83
Standard Fire Insurance Company	15%	12/1/83

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FLORIDA Continued

COMPANY	DEVIATION	EFFECTIVE DATE
State Farm Fire & Casualty Company	10%	9/1/83
Transamerica Indemnity Company	25%	9/17/83
Transamerica Insurance Company	15%	8/1/83
Transcontinental Insurance Company	15%	8/1/83
Transit Casualty Company	15%	1/1/84
Travelers Indemnity Company of America	15%	10/1/83
Travelers Indemnity Company of Rhode Island	20%	10/1/83
Underwriters Insurance Company	21%	9/1/83
Universal Casualty Insurance Company	15%	Pending
Utica Mutual Insurance Company	15%	1/1/84
Valley Forge Insurance Company	25%	10/1/83
Virginia Surety Company	20%	11/1/83
Wausau Underwriters Insurance Company	21%	9/1/83
West American Insurance Company	20%	11/1/83
Western Employers Insurance Company	15%	1/1/84

Chairman RODINO. Thank you.

The subcommittee will stand in recess until we have completed our voting on the matter in question, and we'll be back in 15 minutes.

[Recess.]

Mr. SCHUMER [acting chairman]. The hearings will come to order.

Mr. DeCarlo, had you finished your statement when the hearing briefly adjourned?

Mr. DECARLO. Yes, just about. Can I just add one thing at this point?

Mr. SCHUMER. Please go right ahead.

Mr. DECARLO. OK. This is more in response to something that was said on the earlier panel, and I think it's important that it be clarified for the record.

A former panelist indicated that market sharing, or dividing up the market in other industries, and maybe alluded to the fact that it may go on in the insurance industry. It would appear from the former panelist to be something that repeal of McCarran-Ferguson would avoid, when in fact that's not the case, because there are things, even with the protection of McCarran-Ferguson, that are illegal under the antitrust laws; boycott is one of them. So I don't think that repeal of McCarran-Ferguson would be any help in the cited situation.

Mr. SCHUMER. Thank you very much, Mr. DeCarlo.

We are now ready for questions. I have several to start.

The National Commission for the Review of Antitrust Laws and Procedures, on which Chairman Rodino served, concluded that national rating organizations, such as those you represent, perform a valuable service in collecting and disseminating data that permits companies to set realistic rates.

After listening to your testimony, I certainly agree that this type of service is extremely important. However, collecting and disseminating data is an entirely different activity from developing and distributing suggested rates.

The first question is—and this is for all the panelists—do you believe that it is procompetitive for your organization to distribute proposed rates that include a company's estimated expenses, even on an advisory basis?

Mr. DECARLO. Our organization does that pursuant to the State laws, as you probably know, and I think it is procompetitive.

The reaction we've had from our members and from those viewing the law would indicate that smaller companies could not enter the insurance market for the 600 or so classifications involved, in my particular line of insurance workers' comp, without the comfort of those rates either as the final rate or maybe a benchmark rate. They would either not be able to enter the market at all, or they might enter the market trying to compensate by increasing the risk factor, which would be to the detriment of the consumer—in other words, a higher price.

Mr. SCHUMER. Won't such advisory rates inevitably have a stabilizing effect on the price at which insurance is actually sold?

Ms. WALTERS. We should identify here that we're talking about three separate rate service organizations, and the answers to the

questions, I'm sure, would be consistent but may have different nuances.

We at Insurance Services Office certainly believe that the distribution of advisory rates in those few jurisdictions where we perform that function is highly competitive, does not result in artificially high rates, and, in fact, does not result in anticompetitive practices.

I believe it is important that we should note for the record that, particularly in the personal lines of insurance, we have, I would say, a minimum of 200 insurance companies providing private passenger and homeowners insurance in virtually all jurisdictions.

We should also note that the leading providers of those personal lines of insurance are in no way affiliated with rating and rate service organizations. So it is difficult to conclude that rate service organizations play a significant or major role in terms of determining prices for the majority of the marketplace. Facts will not allow that conclusion to be drawn.

Mr. SCHUMER. Other comments?

Mr. DEYOUNG. On your first question regarding the ratemaking activities, with smaller companies that AAIS serves, we provide a service that is technical in nature, and the companies that we serve do not have technical staffs on hand to provide this information so necessary to be competitive.

We exist simply by the virtue of the concept to share the costs, and you could consider AAIS as being the technical arm of the companies that we serve.

Combined, these companies are, as I mentioned in my oral statement, no larger than a single major insurer, so the combined market share is rather insignificant when you look at us from an antitrust standpoint.

We do not provide any technical service that is different from services that are available within a major insurer, whereas we are providing the technical functions to the minor industry to allow them to compete head on with the major industry. You take that away, and, as I suggested, the costs would increase for the minor industry and would cause them to disappear, at least the smaller of them, from the marketplace.

Mr. SCHUMER. Couldn't several, or a group of different consultants, provide the same role that you would play with——

Mr. DEYOUNG. Why would you suggest that AAIS is not a consultant?

Mr. SCHUMER. I am not suggesting that it is not a consultant.

Mr. DEYOUNG. That's the point that I make. We are in fact operating as a consultant to provide necessary functions that the companies would have to provide on their own.

Ms. WALTERS. If I could add to that, too, I think we should remember that private consulting firms, be they actuarial consulting firms, or economic consulting firms, or anything else, as Mr. DeYoung just pointed out, certainly could be formed to provide the identical services, or very similar services, to his organization or my organization.

But another thing to remember is, if that were true—these kinds of identical services were being provided by consulting firms—they are for-profit firms; those firms would build in not just the costs of

providing the same services we do but would want to make a profit on the work they provide for insurance companies.

His organization and mine is a company-sponsored organization that merely bears the expenses, but there is no profit involved.

So I think you would see higher expenses, higher profits for the consulting firms, hence higher costs to consumers.

Mr. SCHUMER. I'd just make two points in response to that. First, am I correct in saying that the consultants would not be composed of the industry groups?

Ms. WALTERS. That's exactly correct. They would be independent professionals, professional actuaries presumably, who, of course, would be in business, and the consulting business wants to make money.

Mr. SCHUMER. There's a benefit to that, regardless of the cost. The second point on the cost issue is that it is one of the tenets of our economy that the profit motive makes things more efficient, not less efficient. Therefore I query whether there would be higher costs or not?

Yes, Mr. DeYoung?

Mr. DEYOUNG. If I might just comment. Ms. Walters mentioned that ISO has been changing over the years. AAIS has also been responding to the needs of our companies.

The needs of companies are far different today than what they have been in the past. To your point of becoming more like an entrepreneur, the point that Ms. Walters makes with regard to unbundling of services, the companies that we serve are also not bound in any way, shape, or form to take our services.

We, in fact, are entrepreneurs, and we are consultants in that respect to the companies that we serve, except that we are providing a cost efficiency because of the sharing of a facility.

As an organization that is supported by the companies, the risk capital involved with the entrepreneurial activity is put forth by a nucleus of companies, but we sell our services very cost-effectively on a consulting basis.

Mr. SCHUMER. Thank you.

Isn't an individual company in the best position to determine what its expenses are?

Mr. IVES. As a small company, we certainly know our expenses, but I'd like to sort of go across the gamut that you've started here because, for example, we have 19 employees operating in two States. We're not sophisticated, as the large insurers, in allocating every dollar of expense to each line of insurance, for example.

We happen to do a lot of farm insurance; we have farm inspectors. We tend to allocate expenses based on premium writings; and, sure, we can take the time to do it, but it's not cost-efficient for a small operation to do it that way.

I heard an awful lot this morning about no competition in the insurance industry. We have been increasing business at the rate of 15 percent for the last 3 years, and in the first 6 months of this year, we have added 31 percent new business to the books and netted eight.

If you don't think that's competition, trying in the insurance industry today—and I'm talking personal lines now, because that's

all we write, personal lines—is unbelievable, at least in the States of Connecticut and Massachusetts, and churning is expensive.

Mr. SCHUMER. The National Association of Insurance Commissioners in 1980 found that the use of industrywide expense data in determining advisory rates "provides a protective umbrella for less efficient insurers and renders strenuous cost containment by the more efficient companies less necessary than under a fully competitive system. In turn, this means a higher price for the consumer."

What is your response, Mr. Ives?

Mr. IVES. Well, in the marketplace—and I have to talk again from Connecticut and Massachusetts, which I'm very familiar with—it just isn't so.

People tend to think that because the giants are in Connecticut—Travelers, Hartford, and Aetna, and so forth—that they write the most insurance. The largest writer of homeowners in Connecticut is a small mutual insurance company; it writes more than the Aetna or the Travelers, not combined, but individually. They write it because their rates are lower and they provide a better service.

Now their expense ratio—and I don't know what their expense ratio is—may be higher than the Travelers, but the net rate to the consumer is less, and I don't think expense ratio, per se, has a great deal to do with it; it's what the final dollar charged to the consumer is.

Mr. SCHUMER. On the other hand, it might be that you could combine the most efficient of each operation and get the lowest price.

Mr. IVES. It could be.

Mr. DECARLO. Can I add, on the expense question, even taking expenses in final or advisory rates, those expenses are scrutinized by State regulators, and, unlike some statements that were made on the earlier panel, I have been involved in several actions involving litigation over whether the expenses were proper or not in conjunction with State regulation, which is an important factor.

In Illinois, we were involved in protracted litigation over whether the expense rates were not acceptable or whether they were acceptable. More recently in New Hampshire, in connection with assigned-risk plans which we administer, the same issue came up, as to whether the expenses used by the insurance company servicing that business were adequate. So those expenses are policed.

The second thing I'd like to point out in response to your question is, if you start out with average expenses in workers' comp, we find that that's the basis for deviation for the smaller companies, aside from the scrutiny of regulators. The companies taking a look at their own book of business may go down—in fact, frequently do—based on reduced expenses.

Mr. SCHUMER. Thank you.

I have several other questions, but I'd be happy to yield to the gentleman from New York for his questions now.

Mr. FISH. Thank you. I'll be brief, Mr. Chairman. I appreciate it.

Ms. Walters, I believe you heard the previous panel testify.

Ms. WALTERS. Yes, sir.

Mr. FISH. Mr. Hunter was criticizing the Insurance Services Office for its refusal to make rate information available to consumers. I think he particularly talked about rate bureaus, which I

gather collect data, make projections, and what not—that this information is not available to the consumer, and it is his belief that it should be. I wonder if you could explain to us what's involved here and why it's not available to the consumer.

Ms. WALTERS. Yes, sir. I guess this subject certainly came up before today, and I think it's come up at some previous panels, too. I think Mr. Denenberg may have referred to our premium comparisons, and I think other witnesses may have done so also.

I think there's a fundamental misunderstanding as to what this document is that we call premium comparisons, which is a service that we provide to our insurance companies.

First let me say that this is a product which we provide to any insurer. Not only that, it is a product which is provided to every State insurance department as well; so it is not just to insurance companies.

These premium comparisons as a product are extremely limited in terms of the information which is made available. The information provided reflects the premium charged by no more than 10 or 11 insurers operating in a particular State. The particular classes which are displayed on the premium comparison exhibits are no more than a handful in each State and each territory.

These documents, Mr. Fish, were designed to be understood by insurance company people who do understand the complexity of the product and the variety of classes involved.

As a consumer product, it would be worse than useless. It would be incredibly misleading, for the two reasons I mentioned. There are only a handful of companies, so most of the companies would not be included in this document.

Only a small handful of classes are covered, and it would be incorrect to conclude—which I'm afraid most consumers would—that if you looked in a particular territory, for example, in a particular class, and you saw that company A had a lower rate than all of the other companies displayed—the other eight or nine companies—for that one class, then company A may be or must be the lowest rated company; it would be absolutely incorrect, that would be the wrong assumption.

So it was not designed to be understood or available to consumers; it was not designed as a consumer product; it would be misunderstood by consumers.

I should also point out that Insurance Services Office is an insurance industry association. We are formed to provide technical products to insurance companies. So it is not a part of our charter to be a consumer agency anymore than it is a governmental agency. We frankly cannot be all things to all people.

But there are, Mr. Fish, other organizations which have as their primary purpose dealing with consumer information, and I'm sure you would remember an entire panel, in fact an entire day of hearings on the subject of consumer information was held by this committee, and we did have representatives from, for example, the Insurance Information Institute, which was formed for the express purpose of dealing with consumers.

So there are organizations available which do this. ISO is not one of them.

Mr. FISH. Ms. Walters, when you use the words "premium comparison," is that synonymous with rate information and rate bureau? I think "rate bureau" was the term that——

Ms. WALTERS. No. I think Mr. Hunter or Mr. Wilson used the term "rate bureau" to refer, I believe, to Insurance Services Office. As my direct testimony explained, that term went out at least 15 years ago and is not a term which applies to our organization.

Mr. FISH. You just told us that this information, the premium comparison, was filed with the State insurance offices.

Ms. WALTERS. Yes, it is.

Mr. FISH. Is there any reason why it wouldn't be made available to the public through that disclosure to the State?

Ms. WALTERS. I am certain that in every State, whatever the laws and rules are which apply to information filed with them would be available, and so that——

Mr. FISH. So if anybody wanted it, they could have it anyway.

Ms. WALTERS. Get it through the State insurance departments—that's correct.

Mr. FISH. Even if it wouldn't be helpful.

Ms. WALTERS. That's correct.

Mr. FISH. Now you may have heard me ask Dr. Wilson about his criticism of significant rate discounts. What he was saying was that significant rate discounts for large purchasers are simply not cost-justified, and I wonder if any one of you would care to comment on that.

Ms. WALTERS. I'd like to make a stab at it, and perhaps Mr. DeCarlo would also make some comments.

When the discussion took place earlier dealing with personal lines and commercial lines, I believe Mr. Wilson or Mr. Hunter said that there are large discounts, as he described them, available to commercial lines buyers, and I think we should understand that the commercial lines area, while we use it to describe one type of business, actually involves many different types of coverages and policy forms.

The actual rates or premiums that are paid by large commercial buyers reflect a whole host of factors, all of which are, I would say, cost-related.

Experience and schedule rating plans, to a large degree, would influence the rates that are paid by commercial buyers. That is, the actual claims that they have and the number of claims and the cost of settling those claims.

The type of coverage that those commercial carriers would purchase, is it broad coverage? is it narrow coverage? The actual dollar amount of coverage that they would purchase.

It is not uncommon for commercial buyers to have very high self-insured retentions, what we might call deductibles on the personal lines side, so that, for example, a very large risk might decide that it's more cost-effective for them to pay smaller claims themselves directly, rather than through an insurance company. So they may only buy insurance for amounts over $1,000 per claim, or $5,000 per claim, or something like that.

All of these factors which relate to the coverage are, of course, cost-related, and I think one other point I would make here is, when we look at the prices and the premiums in the commercial

lines area, that also is a strong indicator of the fundamental problem that we, as actuaries, deal with when we're talking about insurance, and that is, we're really trying to predict the future; it's a very difficult thing to do.

The entire actuarial profession developed to deal with the problem of estimating the current financial implications of future contingent events. It's a very difficult thing to do. An entire profession grew up in this area.

When we look after the fact and we see that actually the costs turned out to be higher than the premium dollars that were charged, that doesn't mean that there was a deliberate attempt to do that; it simply means we are not omniscient.

Mr. FISH. Mr. Chairman, I'm out of time, but there was some indication that Mr. DeCarlo wanted to comment on this question, too. Would that be all right if he proceeded?

Mr. SCHUMER. Certainly.

Mr. DECARLO. The only thing I would add to that—you know, there's the same activity in workers' comp as there are in the lines that Ms. Walters was talking about. There are other rating plans, scheduled rating, retro rating, dividends, deviations.

There is the need for some assistance in a uniform product, the policy form, but I think more importantly and directly related is the fact that workers' comp is a commercial line of insurance that you're dealing with a sophisticated buyer for the most part.

Unlike the person who goes out and maybe buys an automobile policy, who may or may not accept the information he gets, the commercial buyer is going to make sure that he gets the best price so he could factor that into his contract maybe with one of his suppliers.

Mr. FISH. Thank you.

Mr. SCHUMER. Thank you very much, Mr. Fish, and now I recognize the gentleman from California.

Mr. EDWARDS. Thank you, Mr. Chairman.

When a State like Michigan tries to instill a measure of competition by law, what do you people do? Do you resist it, or do you get involved? Do you mention it in your newsletters? Do you lobby?

Mr. DECARLO. Can I respond to that, because that law specifically relates to workers' comp, and our general approach—the national council—and this comes from a resolution of our board—is to service the workers' comp system no matter what rating law is in place.

The commissioner in Michigan portrayed a very nice picture with her law, and that's good; I'm glad it's working. There are other States with completely different rating laws that work effectively in their State. So each legislature has chosen a different way to go, which we're willing to accommodate.

For example, the statistics that I heard this morning about reduction in rates in Michigan, reduced number of risks in the assigned risk plans, there's just generally a trend nationally.

We have in the last, I guess, 3 years, seen about a 13-percent reduction in workers' comp rates notwithstanding what the rating laws are. Some are price-administered laws versus competitive rating laws.

Florida, one of our biggest national council States, had a 26-percent reduction. My home State of New York had a 47-percent reduction in rates. In residual market, or assigned risk plans, the premiums have gone down nationally about 20 percent, and the numbers of risks in the assigned risk plans have gone down almost 8 percent.

Unrelated to any specific law, it's not so much what appears in the rating law but what's happening in the workers' comp law. Are the benefits proper benefits? Are they being administered properly? The net result of that is reflected in the marketplace.

Mr. EDWARDS. Thank you.

Mr. DeYoung, can you think of any reason why the banking and securities industries, or even the telephone or telecommunications industry, are subject to antitrust when your industry is not?

Mr. DEYOUNG. As I understand it, it is because of McCarran-Ferguson. I presume that that is the difference that kept regulation at the State level with insurance, and I think properly so.

This whole issue is something that we as a rating service organization do not directly become involved with. We are not a lobbying entity, we are a service entity to the insurers under the regulation that is provided to us.

We prefer to operate under McCarran-Ferguson because of the reasons contained in the testimony that we gave to you today. Simply, we cannot conceive that we can do the things which are necessary in determining the cost of the product for the customers that we serve, information that is essential for them to market properly, without engaging in activities that, as we understand it, are, per se, violations of antitrust laws.

Ms. WALTERS. Mr. Edwards, if I might, I'd like to add to Mr. DeYoung's answer.

From my study of the issue, it seems to me the fundamental reason why there is a difference between the insurance industry and banking and the other financial industries that you referred to relates directly to my answer to Mr. Fish's question about determining rates and prices in the insurance industry, and that is that in determining the correct and accurate—accurate—rate, because we must determine the price before we know the costs. This is unlike many other areas, or almost any area I can think of, in the American economy.

When General Motors has to price its car, it knows the labor costs involved. It knows the price of steel, it knows the price of all the products that are going into its product before it sets its price.

In insurance, we have to determine the price, but we're not going to know the cost for several years, and in some lines of insurance it's going to be 10 or 15 years before the actual costs are going to be known.

I believe this was fundamentally what was at issue in 1944 in the *SEUA* case, in 1945 when the McCarran-Ferguson Act was passed. We're dealing with an industry that must estimate future costs.

In order to do that, the only tools we have available are past loss statistics, but we can't just use the past unless everything else stays equal. As long as there are changing economic conditions, we have to somehow use that body of aggregate data in the past to estimate the future costs.

If you're dealing with a very small body of data, just a small amount, you are not going to have reliable estimates of future costs.

What we absolutely must have in order to have accurate rates is a very large body of data, aggregate pooled loss statistics that have statistical credibility, so that when we are making our estimates of future cost, it will be as accurate as possible, and I believe that's the fundamental difference between insurance and some of these other industries.

Mr. DeCarlo. Mr. Edwards, can I add to that?

Mr. Edwards. Yes, of course.

Mr. DeCarlo. I agree with Ms. Walters, but I have also a slightly different perspective, too, not inconsistent with—but if you look at workers' comp or any line of insurance as a social system, the insurance feature being just one part of it, back to the early 1900's there was a tradeoff where there would be provided no-fault benefits to the injured worker. In return, the worker would not sue the employer.

That was felt to be a very beneficial system, rather than a lot of litigation between employers and employees, very productive for the economy, and the way they implemented that system was by establishing ways to secure the liability of those employers for ultimately paying the injured employee.

Unlike airlines, for example, where, if they are deregulated and there's some problem that someone may not have the right airline tickets, if someone is a quadriplegic and there's no money around to pay for those benefits, I think there's more serious consequences.

So that within the scheme, insurance is one method of funding that social system. State funds is another—some States have chosen to go with a monopoly State fund—and most States now allow self-insurance. Larger employers can fund by just posting bonds.

If you look at that as an entire package, I think it's something well worth preserving, and if you tinker with any part of it, by restricting the insurance mechanism in the way prices are set or advice on prices given or collected data, you may disrupt the entire balance of what appears to be a workable system.

Mr. DeYoung. Mr. Edwards, may I say just one more thing?

Mr. Edwards. Yes, please.

Mr. DeYoung. As a service organization, should a bank become involved in insurance, they can buy services from AAIS, the only point being that we take no issue with banks becoming aligned with insurance activity as a service organization.

We provide the service to anyone who is legitimately within the insurance market and is in need of the information that we provide, and they pay for the service.

Mr. Edwards. Well, this important collective function that you people provide, why couldn't that be provided without McCarran-Ferguson?

Mr. DeCarlo. From a legal standpoint, in my prepared statement I indicated in advising my client, the National Council, I would have no comfort in the case law for collecting statistics, notwithstanding some cases that are used as analogies as to how you can collect that information.

The largest member of our organization tells us they cannot gather on their own sufficient statistics to come up with a rate for one of the 600 classes. Smaller or medium-sized carriers would have no hope if the larger carriers can't.

To then take away the ability of us to deal with that collective statistical gathering, I think, is just to the detriment of the system.

Mr. EDWARDS. Congress could provide for that service to continue as a partial exemption.

Mr. DECARLO. Well, if you talk about——

Mr. EDWARDS. We do that from time to time.

Mr. DECARLO. I'm sorry, Mr. Edwards.

Mr. EDWARDS. We do that from time to time.

Mr. DECARLO. Yes. I don't know that—if you talk about just segregating that piece of it, that's a start, but how would you do that? I'm not sure; I haven't seen any legislation, and I don't know that I'd be prepared to specifically comment on it without studying it; but every attempt, it appears, to address any antitrust questions without specific previous case law, or even with McCarran-Ferguson protection, is absent any comfort.

Analogies don't work, as indicated by the *BMI* case, and I'm not sure that analogies would work for ratemaking organizations.

Ms. WALTERS. Mr. Edwards, I'd like to add something to that, too.

In my formal statement, also, I indicated that even a substantial modification of McCarran-Ferguson, as it's currently drawn, certainly would create a great deal of uncertainty over what are legitimate and useful functions of a rate service organization, and what would be the functions which would not be permitted.

I am an actuary and not a lawyer, but from my review of all of the studies that have been done over the years on McCarran-Ferguson and what would be protected and what wouldn't be protected, the one thing that strikes me is, it appears that no two lawyers can agree on what would be protected functions in a certain area, what wouldn't be protected functions absent McCarran-Ferguson, and if we are dealing with carving out a certain area of limited functions, there is disagreement among the legal experts as to what would be protected even under different modifications.

I would say none of us can give a firm answer as to what we think would be adequate or inadequate unless we were to see specific language, but even then I suspect our lawyers would take, and insurance companies would take, little comfort over one group of lawyers' opinions when it hadn't been tested in the courts.

I think what we fear is the pall of uncertainty that could be created, which would limit the usefulness of some of the collective services that we do perform, which we believe are ultimately beneficial to the consumers.

Mr. EDWARDS. Are you all public firms? Is your stock owned publicly?

Mr. DECARLO. The national council is a nonprofit, unincorporated association.

Mr. EDWARDS. It's nonprofit; I see.

Ms. WALTERS. We are a nonprofit corporation also, Mr. Edwards, not a publicly owned company.

Mr. DeYoung. We are two corporations. One is nonprofit, the other is for profit. Where I suggested that we were moving toward becoming entrepreneurial, the service corporation does provide services individually to companies that are not members of the association. We are opening up our services through this mechanism. That is a wholly owned subsidiary of the nonprofit corporation.

Mr. Edwards. Thank you very much, Mr. Chairman.

Mr. Schumer. Thank you.

The chairman would like to end the hearing at noon, so I will ask one last question and then ask, with the permission of the witnesses, that any member of the subcommittee be allowed to submit questions for answers in writing. Thank you.

The final question is to Mr. DeCarlo. Why does the constitution of the national council require its members to adhere to the rate files? Isn't that anticompetitive?

Mr. DeCarlo. I would say it's not anticompetitive, and that's a reflection of what's in the rating laws as to workers' comp.

Going back to what I indicated to Mr. Edwards, the legislators at the time of first enacting rating laws as they applied to workers' comp—and we have some different rating laws than other lines—felt it necessary that they preserve the solvency and stability of that system.

But in addition to that, and in spite of that language being in there, I think the exceptions have swallowed up the rule, because there is so much competition, in a number of ways that I've explained in my paper, that the adherence requirement is really a misnomer at this point.

Mr. Schumer. Doesn't what you say contradict directly what the Michigan Insurance Commissioner had to say?

Mr. DeCarlo. No. We say adherence to the extent permitted by law. We operate in competitive rating law States as well as noncompetitive rating law States, and whatever that law requires we go with. So we have the exceptions for that law in our constitution.

Mr. Schumer. Thank you very much, and I thank all the witnesses for their testimony.

Mr. DeCarlo. Thank you.

[Whereupon, at 12 noon, the subcommittee was adjourned.]

APPENDIXES

Historical Material Submitted by Chairman Rodino

A. Legislative History for the McCarran-Ferguson Act including:
1. Senate Judiciary Committee Report.
2. House Judiciary Committee Report.
3. Conference Committee Report.
4. Excerpts from Congressional Record containing floor debate on the McCarran-Ferguson Act.

B. Exchange of correspondence between President Franklin D. Roosevelt and Senator George L. Radcliffe regarding an antitrust exemption for the insurance industry.

C. President Roosevelt's statement on signing McCarran-Ferguson Act.

APPENDIXES

APPENDIX 1

The McCarran-Ferguson Act (15 U.S.C. §§1011-1015)

CHAPTER 20—REGULATION OF INSURANCE

Sec.
1011. Declaration of policy.
1012. Regulation by State law; Federal law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948.
1013. Suspension until June 30, 1948, of application of certain Federal laws; Sherman Act applicable to agreements to, or acts of, boycott, coercion, or intimidation.
1014. Applicability of National Labor Relations Act and the Fair Labor Standards Act of 1938.
1015. Definition of "State."

§ 1011. Declaration of policy

Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

(Mar. 9, 1945, ch. 20, § 1, 59 Stat. 33.)

SEPARABILITY

Section 6 of act Mar. 9, 1945, provided: "If any provision of this Act [this chapter], or the application of such provision to any person or circumstances, shall be held invalid, the remainder of the Act, and the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected."

SHORT TITLE

Act Mar. 9, 1945, ch. 20, 59 Stat. 33 [this chapter], is popularly known as the McCarran-Ferguson Act.

§ 1012. Regulation by State law; Federal law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948

(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended [15 U.S.C. 41 et seq.], shall be applicable to the business of insurance to the extent that such business is not regulated by State Law.

(Mar. 9, 1945, ch. 20, § 2, 59 Stat. 34; July 25, 1947, ch. 326, 61 Stat. 448.)

REFERENCES IN TEXT

The act of July 2, 1890, as amended, known as the Sherman Act, referred to in subsec. (b), is classified to sections 1 to 7 of this title.

The act of October 15, 1914, as amended, known as the Clayton Act, referred to in subsec. (b), is classified to sections 12, 13, 14 to 19, 20, 21, and 22 to 27 of this title and to sections 52 and 53 of Title 29, Labor. For further details, see References in Text note set out under section 12 of this title.

The act of September 26, 1914, known as the Federal Trade Commission Act, as amended, referred to in subsec. (b), is classified generally to subchapter I (§ 41 et seq.) of chapter 2 of this title. For complete classification of this Act to the Code, see section 58 of this title and Tables volume.

AMENDMENTS

1947—Act July 25, 1947, substituted "June 30, 1948" for "January 1, 1948".

§ 1013. Suspension until June 30, 1948, of application of certain Federal laws; Sherman Act applicable to agreements to, or acts of, boycott, coercion, or intimidation

(a) Until June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act [15 U.S.C. 41 et seq.], and the Act of June 19, 1936, known as the Robinson-Patman Anti-Discrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.

(b) Nothing contained in this chapter shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

(Mar. 9, 1945, ch. 20, § 3, 59 Stat. 34; July 25, 1947, ch. 326, 61 Stat. 448.)

REFERENCES IN TEXT

The act of July 2, 1890, as amended, known as the Sherman Act, referred to in subsecs. (a) and (b), is classified to sections 1 to 7 of this title.

The act of October 15, 1914, as amended, known as the Clayton Act, referred to in subsec. (a), is classified to sections 12, 13, 14 to 19, 20, 21, and 22 to 27 of this title and to sections 52 and 53 of Title 29, Labor. For further details see References in Text note set out under section 12 of this title.

The act of September 26, 1914, known as the Federal Trade Commission Act, referred to in subsec. (a), is generally classified to subchapter I (§ 41 et seq.) of chapter 2 of this title. For complete classification of this Act to the Code, see section 58 of this title and Tables volume.

The act of June 19, 1936, known as the Robinson-Patman Anti-Discrimination Act, referred to in subsec. (a), is act June 19, 1936, ch. 592, §§ 1 to 4, 49 Stat. 1526. For complete classification of this Act to the Code, see Short Title note set out under section 13a of this title, and Tables volume.

AMENDMENTS

1947—Act July 25, 1947, substituted "June 30, 1948" for "January 1, 1948".

§ 1014. Applicability of National Labor Relations Act and the Fair Labor Standards Act of 1938

Nothing contained in this chapter shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935, as amended, known as the National Labor Relations Act [29 U.S.C. 151 et seq.], or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938 [29 U.S.C. 201 et seq.], or the Act of June 5, 1920, known as the Merchant Marine Act, 1920 [46 U.S.C. 861 et seq. and 911 et seq.].

(Mar. 9, 1945, ch. 20, § 4, 59 Stat. 34.)

REFERENCES IN TEXT

The Act of July 5, 1935, as amended, known as the National Labor Relations Act, referred to in text, is classified generally to subchapter II (§ 151 et seq.) of chapter 7 of Title 29, Labor. For complete classification of this Act to the Code, see section 167 of Title 29 and Tables volume.

The Act of June 25, 1938, as amended, known as the Fair Labor Standards Act, referred to in text, is generally classified to chapter 8 (§ 201 et seq.) of Title 29. For complete classification of this Act to the Code, see section 201 of Title 29 and Tables volume

The Act of June 5, 1920, known as the Merchant Marine Act, 1920, referred to in text, is classified generally to chapters 24 and 25 (§§ 861 et seq. and 911 et seq.) of Title 46, Shipping. For complete classification of this Act to the Code, see References in Text note under section 889 of Title 46 and Tables volume.

§ 1015. Definition of "State"

As used in this chapter, the term "State" includes the several States, Alaska, Hawaii, Puerto Rico, Guam, and the District of Columbia.

(Mar. 9, 1945, ch. 20, § 5, 59 Stat. 34; Aug. 1, 1956, ch. 852, § 4, 70 Stat. 908.)

AMENDMENTS

1956—Act Aug. 1, 1956, included "Guam" in the definition of state.

ADMISSION OF ALASKA AND HAWAII TO STATEHOOD

Alaska was admitted into the Union on Jan. 3, 1959, upon the issuance of Proc. No. 3269, Jan. 3, 1959, 24 FR 81, 73 Stat. c16, and Hawaii was admitted into the Union on Aug. 21, 1959, upon the issuance of Proc. No 3309, Aug. 21, 1959, 24 FR 6868, 73 Stat. c74. For Alaska Statehood Law, see Pub. L. 85-508, July 7, 1958, 72 Stat. 339, set out as a note preceding section 21 of Title 48, Territories and Insular Possessions. For Hawaii Statehood Law, see Pub. L. 86-3, Mar. 18, 1959, 73 Stat. 4, set out as a note preceding section 491 of Title 48.

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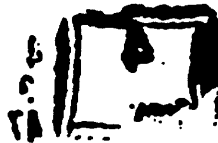
79TH CONGRESS : : : : 1ST SESSION

JANUARY 3–DECEMBER 21, 1945

SENATE REPORTS



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79TH CONGRESS } SENATE { REPORT
1st Session } { No. 20

EXPRESSING THE INTENT OF THE CONGRESS WITH REFERENCE TO THE REGULATION OF THE BUSINESS OF INSURANCE

JANUARY 24, 1945.—Ordered to be printed

Mr. McCARRAN, from the Committee on the Judiciary, submitted the following

REPORT

[To accompany S. 340]

The Committee on the Judiciary, to whom was referred the bill (S. 340) to express the intent of the Congress with reference to the regulation of the business of insurance, having considered the same, favorably report the bill to the Senate with an amendment with the recommendation that the bill, as amended, do pass.

On page 2, line 23, after the word "any", insert the words "agreement or".

GENERAL STATEMENT

From its beginning the business of insurance has been regarded as a local matter, to be subject to and regulated by the laws of the several States. This view has been fostered and augmented by decisions of the United States Supreme Court for a period of more than 75 years, leading to the generally accepted doctrine that the business of insurance was not subject to Federal law.

On June 5, 1944, in the case of *U. S.* v. *Southeastern Underwriters Association et al.*, the Supreme Court decided that the business of insurance was commerce and, therefore, subject to the Sherman Act of July 2, 1890, as amended, and the Clayton Act of October 15, 1914, as amended.

The Attorney General, in several appearances before the Judiciary Committee, frankly stated that the Department of Justice had no opposition to an extension of time to the insurance industry in order to make necessary adjustments to this decision.

Inevitable uncertainties which followed the handing down of the decision in the *Southeastern Underwriters Association case*, with respect to the constitutionality of State laws, have raised questions in the

minds of insurance executives, State insurance officials, and others as to the validity of State tax laws as well as State regulatory provisions; thus making desirable legislation by the Congress to stabilize the general situation.

Bills attempting to deal with the problem were considered in both the House and the Senate during the Seventy-eighth Congress, but failed of enactment. Your committee believes there is urgent need for an immediate expression of policy by the Congress with respect to the continued regulation of the business of insurance by the respective States. Already many insurance companies have refused, while others have threatened refusal to comply with State tax laws, as well as with other State regulations, on the ground that to do so, when such laws may subsequently be held unconstitutional in keeping with the precedent-smashing decision in the *Southeastern Underwriters case*, will subject insurance executives to both civil and criminal actions for misappropriation of company funds.

The committee has therefore given immediate consideration to S. 340, together with a similar measure (S. 12, introduced by Senators O'Mahoney and Hatch), so that the several States may know that the Congress desires to protect the continued regulation and taxation of the business of insurance by the several States, and thus enables insurance companies to comply with State laws. What is more, the Congress proposes by this bill to secure adequate regulation and control of the insurance business.

PURPOSE OF THE BILL

The purpose of the bill is twofold: (1) To declare that the continued regulation and taxation by the several States of the business of insurance is in the public interest; and (2) to assure a more adequate regulation of this business in the States by suspending the application of the Sherman and Clayton Acts for approximately two sessions of the State legislatures, so that the States and the Congress may consider legislation during that period. It should be noted that this bill, by the moratorium proposed therein, does not repeal the Sherman and Clayton Acts, but opportunity will have been granted for the States to permit agreements and contracts by insurance companies which otherwise might be in violation of the Sherman and Clayton Acts. It should be noted further that no moratorium is granted from the Sherman Act relative to agreements or acts of boycott, coercion, or intimidation.

ANALYSIS BY SECTION

Section 1 declares that the continued regulation and taxation by the States of the business of insurance is in the public interest.

Section 2 provides that the insurance business, and all persons engaged in such business, shall be subject to State laws relating to the regulation and taxation of such business; and (*b*) that no act of Congress shall be construed to invalidate, impair, or supersede any State law which regulates or taxes the insurance business, unless such act specifically so provides.

Section 3 provides that the Federal Trade Commission Act and the Robinson-Patman Antidiscrimination Act shall not apply to the insurance business, or to acts in the conduct of such business.

Section 4 suspends the application of the Sherman Act to the business of insurance until June 1, 1947, and suspends the application of the Clayton Act until January 1, 1948—

for the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress—

and (*b*) provides that at no time are the prohibitions in the Sherman Act against any agreement or act of boycott, coercion, or intimidation, suspended. These provisions of the Sherman Act remain in full force and effect.

Section 5 provides that the enactment of this act shall not affect, in any manner, the present application of the National Labor Relations Act, or the Fair Labor Standards Act, to the business of insurance.

Section 6 defines the term "State."

Section 7 provides for separability of provisions.

CONCLUSION

In the considered judgment of your committee, S. 340 represents a most commendable effort on the part of insurance companies and State insurance commissioners to effect the adjustments and reorganization in and among the financial operations of insurance companies and in State laws which have been made necessary by the decision in the *Southeastern Underwriters case*. It should be emphasized that the bill has received the overwhelming endorsement of the principal national organizations of State insurance commissioners, insurance executives, agents, brokers, and underwriters, including the National Association of Insurance Commissioners, the American Life Convention, the American Mutual Alliance, the Association of Casualty and Surety Executives, the Inland Marine Underwriters Association, the National Association of Insurance Agents, the National Association of Mutual Insurance Agents, the National Board of Fire Underwriters, Insurance Executives Association, National Association of Insurance Brokers, Inc., the National Association of Casualty and Surety Agents, the Surety Association of America, the National Fraternal Congress of America, and the Health and Accident Underwriters Conference. Opportunity is granted to the State legislatures during their present and forthcoming sessions for 1945, 1946, and 1947 to consider the welfare of policyholders.

Enactment of this bill will (1) remove existing doubts as to the right of the States to regulate and tax the business of insurance, and (2) secure more adequate regulation of such business.

79TH CONGRESS : : : : 1ST SESSION

JANUARY 3-DECEMBER 21, 1945

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79TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
1st Session } { No. 143

EXPRESSING THE INTENT OF THE CONGRESS WITH REFERENCE TO THE REGULATION OF THE BUSINESS OF INSURANCE

FEBRUARY 13, 1945.—Referred to the House Calendar and ordered to be printed

Mr. WALTER, from the Committee on the Judiciary, submitted the following

REPORT

[To accompany S. 340]

The Committee on the Judiciary, to whom was referred the bill (S. 340) to express the intent of the Congress with reference to the regulation of the business of insurance, having considered the same, report favorably thereon with an amendment with the recommendation that the bill, as amended, do pass.

The committee amendment is as follows:

Strike out all after the enacting clause and insert the following:

That the Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

SEC. 2. (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically so provides.

SEC. 3. Nothing contained in the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, or the Act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall apply to the business of insurance or to acts in the conduct of that business.

SEC. 4. (a) Until January 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, shall not apply to the business of insurance or to acts in the conduct thereof.

(b) Nothing contained in this section shall render the said Sherman Act inapplicable to any act of boycott, coercion, or intimidation.

SEC. 5. Nothing contained in this Act shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935, as amended, known as the National Labor Relations Act, or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938 or the Act of June 5, 1920, known as the Merchant Marine Act, 1920.

2 INTENT OF CONGRESS WITH REFERENCE TO INSURANCE

SEC. 6. As used in this Act, the term "State" includes the several States, Alaska, Hawaii, Puerto Rico, and the District of Columbia.

SEC. 7. If any provision of this Act, or the application of such provision to any person or circumstances, shall be held invalid, the remainder of the Act, and the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected.

GENERAL STATEMENT

From its beginning the business of insurance has been regarded as a local matter, to be subject to and regulated by the laws of the several States. This view has been fostered and augmented by decisions of the United States Supreme Court for a period of more than 75 years, leading to the generally accepted doctrine that the business of insurance was not subject to Federal law.

On June 5, 1944, in the case of *U. S.* v. *Southeastern Underwriters Association et al.*, the Supreme Court decided that the business of insurance was commerce and, therefore, subject to the Sherman Act of July 2, 1890, as amended, and the Clayton Act of October 15, 1914, as amended.

The Attorney General, in several appearances before the Judiciary Committee, frankly stated that the Department of Justice had no opposition to an extension of time to the insurance industry in order to make necessary adjustments to this decision.

Inevitable uncertainties which followed the handing down of the decision in the *Southeastern Underwriters Association case*, with respect to the constitutionality of State laws, have raised questions in the minds of insurance executives, State insurance officials, and others as to the validity of State tax laws as well as State regulatory provisions; thus making desirable legislation by the Congress to stabilize the general situation.

Bills attempting to deal with the problem were considered in both the House and the Senate during the Seventy-eighth Congress, but failed of enactment. Your committee believes there is urgent need for an immediate expression of policy by the Congress with respect to the continued regulation of the business of insurance by the respective States. Already many insurance companies have refused, while others have threatened refusal to comply with State tax laws, as well as with other State regulations, on the ground that to do so, when such laws may subsequently be held unconstitutional in keeping with the precedent-smashing decision in the *Southeastern Underwriters case*, will subject insurance executives to both civil and criminal actions for misappropriation of company funds.

The committee has therefore given immediate consideration to S. 340, together with a similar measure, H. R. 1973, so that the several States may know that the Congress desires to protect the continued regulation and taxation of the business of insurance by the several States, and thus enables insurance companies to comply with State laws. What is more, the Congress proposes by this bill to secure adequate regulation and control of the insurance business.

Nothing in this bill is to be so construed as indicating it to be the intent or desire of Congress to require or encourage the several States to enact legislation that would make it compulsory for any insurance company to become a member of rating bureaus or charge uniform rates. It is the opinion of Congress that competitive rates on a sound financial basis are in the public interest.

INTENT OF CONGRESS WITH REFERENCE TO INSURANCE

It is not the intention of Congress in the enactment of this legislation to clothe the States with any power to regulate or tax the business of insurance beyond that which they had been held to possess prior to the decision of the United States Supreme Court in the *Southeastern Underwriters Association case*. Briefly, your committee is of the opinion that we should provide for the continued regulation and taxation of insurance by the States, subject always, however, to the limitations set out in the controlling decisions of the United States Supreme Court, as, for instance, in *Allgeyer* v. *Louisiana* (165 U. S. 578), *St. Louis Cotton Compress Co.* v. *Arkansas* (260 U. S. 346), and *Connecticut General Insurance Co.* v. *Johnson* (303 U. S. 77), which hold, inter alia, that a State does not have power to tax contracts of insurance or reinsurance entered into outside its jurisdiction by individuals or corporations resident or domiciled therein covering risks within the State or to regulate such transactions in any way.

PURPOSE OF THE BILL

The purpose of the bill is twofold: (1) To declare that the continued regulation and taxation by the several States of the business of insurance is in the public interest; and (2) to assure a more adequate regulation of this business in the States by suspending the application of the Sherman and Clayton Acts for approximately two sessions of the State legislatures, so that the States and the Congress may consider legislation during that period. It should be noted that this bill, by the moratorium proposed therein, does not repeal the Sherman and Clayton Acts, but opportunity will have been granted for the States to permit agreements and contracts by insurance companies which otherwise might be in violation of the Sherman and Clayton Acts. It should be noted further that no moratorium is granted from the Sherman Act relative to agreements or acts of boycott, coercion, or intimidation.

ANALYSIS BY SECTION

Section 1 declares that the continued regulation and taxation by the States of the business of insurance is in the public interest.

Section 2 provides that the insurance business, and all persons engaged in such business, shall be subject to State laws relating to the regulation and taxation of such business; and (*b*) that no act of Congress shall be construed to invalidate, impair, or supersede any State law which regulates or taxes the insurance business, unless such act specifically so provides.

Section 3 provides that the Federal Trade Commission Act and the Robinson-Patman Antidiscrimination Act shall not apply to the insurance business, or to acts in the conduct of such business.

Section 4 suspends the application of the Sherman Act and the Clayton Act to the business of insurance until January 1, 1948; and (b) provides that at no time are the prohibitions in the Sherman Act against any act of boycott, coercion, or intimidation suspended. These provisions of the Sherman Act remain in full force and effect.

Section 5 provides that the enactment of this act shall not affect, in any manner, the present application of the National Labor Relations Act, the Fair Labor Standards Act, or the Merchant Marine Act, to the business of insurance.

Section 6 defines the term "State."
Section 7 provides for separability of provisions.

CONCLUSION

In the considered judgment of your committee, S. 340, as amended, represents a most commendable effort on the part of insurance companies and State insurance commissioners to effect the adjustments and reorganization in and among the financial operations of insurance companies and in State laws which have been made necessary by the decision in the *Southeastern Underwriters case*. It should be emphasized that the bill has received the overwhelming endorsement of the principal national organizations of State insurance commissioners, insurance executives, agents, brokers, and underwriters, including the National Association of Insurance Commissioners, the American Life Convention, the American Mutual Alliance, the Association of Casualty and Surety Executives, the Inland Marine Underwriters Association, the National Association of Insurance Agents, the National Association of Mutual Insurance Agents, the National Board of Fire Underwriters, Insurance Executives Association, National Association of Insurance Brokers, Inc., the National Association of Casualty and Surety Agents, the Surety Association of America, the National Fraternal Congress of America, and the Health and Accident Underwriters Conference. Opportunity is granted to the State legislatures during their present and forthcoming sessions for 1945, 1946, and 1947 to consider the welfare of policyholders.

Enactment of this bill will (1) remove existing doubts as to the right of the States to regulate and tax the business of insurance, and (2) secure more adequate regulation of such business.

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EXPRESSING THE INTENT OF CONGRESS WITH REFERENCE TO THE REGULATION OF THE BUSINESS OF INSURANCE

FEBRUARY 22, 1945.—Ordered to be printed

Mr. SUMNERS of Texas, from the committee of conference, submitted the following

CONFERENCE REPORT

[To accompany S. 340]

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (S. 340) to express the intent of the Congress with reference to the regulation of the business of insurance, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the Senate recede from its disagreement to the amendment of the House and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the House amendment insert the following:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

SEC. 2. (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: Provided, That after January 1, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall

be applicable to the business of insurance to the extent that such business is not regulated by state law.

SEC. 3. (a) Until January 1, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the Act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.

(b) Nothing contained in this Act shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

SEC. 4. Nothing contained in this Act shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935, as amended, known as the National Labor Relations Act, or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938 or the Act of June 5, 1920, known as the Merchant Marine Act, 1920.

SEC. 5. As used in this Act, the term "State" includes the several States, Alaska, Hawaii, Puerto Rico, and the District of Columbia.

SEC. 6. If any provision of this Act, or the application of such provision to any person or circumstances, shall be held invalid, the remainder of the Act, and the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected.

And the House agree to the same.

HATTON W. SUMNERS,
FRANCIS E. WALTER,
C. E. HANCOCK,
Managers on the part of the House.

PAT McCARRAN,
JOSEPH C. O'MAHONEY,
HOMER FERGUSON,
Managers on the part of the Senate.

STATEMENT OF THE MANAGERS ON THE PART OF THE HOUSE

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendment of the House to the bill (S. 340) to express the intent of the Congress with reference to the regulation of the business of insurance, submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report:

The House amendment struck out all of the Senate bill after the enacting clause. The committee of conference recommends that the Senate recede from its disagreement to the amendment of the House, with an amendment which is a substitute for both the Senate bill and the House amendment, and that the House agree to the same.

It was the purpose on the part of the managers of the House to have the agreement between themselves and the managers on the part of the Senate to state in as clear language as possible that a moratorium be granted to the insurance business from the operation of the act of July 2, 1890, as amended, known as the Sherman Act, and the act of October 15, 1914, as amended, known as the Clayton Act, and the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, until January 1, 1948, leaving the taxing and regulatory powers of the several States fully protected.

The principal difference between the conference report and the bill as it passed the House lies in the inclusion of the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, in the moratorium provision, and making clear the intention of the Congress that the acts of boycott, coercion, and intimidation are subject to the operation of the suspended statutes even during the moratorium period.

HATTON W. SUMNERS,
FRANCIS E. WALTER,
C. E. HANCOCK,
Managers on the part of the House.

O

REGULATION OF THE BUSINESS OF INSURANCE

Mr. FERGUSON. Mr. President, I move that the Senate proceed to the consideration of Senate bill 340.

The VICE PRESIDENT. The bill will be stated by title for the information of the Senate.

The LEGISLATIVE CLERK. A bill (S. 340) to express the intent of the Congress with reference to the regulation of the business of insurance.

The VICE PRESIDENT. The question is on agreeing to the motion of the Senator from Michigan.

The motion was agreed to; and the Senate proceeded to consider the bill, which had been reported from the Committee on the Judiciary, with an amendment, in section 4, on page 2, line 24, after the word "any", to insert "agreement or", so as to make the bill read:

Be it enacted, etc., That the Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States

SEC. 2. (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically so provides.

SEC. 3. Nothing contained in the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, or the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall apply to the business of insurance or to acts in the conduct of that business.

SEC. 4. (a) For the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress, until June 1, 1947, the act of July 2, 1890, as amended, known as the Sherman Act, shall not apply to the business of insurance, or to acts in the conduct of such business, and until January 1, 1948, the act of October 15, 1914, as amended, known as the Clayton Act, shall not apply to such business or to acts in the conduct thereof.

(b) Nothing contained in this section shall render the said Sherman Act inapplicable to any agreement or act of boycott, coercion, or intimidation.

SEC. 5. Nothing contained in this act shall be construed to affect in any manner the application to the business of insurance of the act of July 5, 1935, as amended, known as the National Labor Relations Act, or the act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938.

SEC. 6. As used in this act, the term "State" includes the several States, Alaska, Hawaii, Puerto Rico, and the District of Columbia.

SEC. 7. If any provision of this act, or the application of such provision to any person or circumstances, shall be held invalid, the remainder of the act, and the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected.

The VICE PRESIDENT. The question is on agreeing to the amendment reported by the committee.

Mr. FERGUSON. Mr. President, until June 5, 1944, the business of insurance had been regarded as a local matter, and subject to regulation or taxation by the several States. While that view had been contested many times by various insurance companies, various decisions of the United States Supreme Court had fostered and augmented it for a period of more than 75 years, until on June 5, 1944, in its opinion in the case of United States against Southeastern Underwriters Association and others, the Supreme Court held in effect that the business of insurance was commerce and, therefore, subject to the Sherman Act of July 2, 1890, as amended, and the Clayton Act of October 15, 1914, as amended.

Since that decision was rendered, the States have been greatly concerned about the business of insurance, insofar as regulation and taxation are concerned.

Mr. McKELLAR. Mr. President, will the Senator yield?

Mr. FERGUSON. I am glad to yield.

Mr. McKELLAR. As I understand the bill its purpose and effect will be to establish the law as it was supposed to be prior to the rendering of the recent opinion of the Supreme Court of the United States. Is that correct?

Mr. FERGUSON. No. I would say that subsection (b), at the bottom of page 2, would allow the provisions of the Sherman Act to apply to all agreements or acts of boycott, coercion, or intimidation, and subsection 4 (a) would suspend the application of the provisions of the Sherman Act and the Clayton Act, insofar as States may regulate and tax such companies, until certain dates or until Congress may act in the meantime in respect to what Congress thinks should be done with the business of insurance.

In other words, the bill would establish a moratorium on the application of the provisions of those acts until the date set forth in the bill.

Mr. McKELLAR. I thank the Senator.

Mr. FERGUSON. Mr. President, in order to show the importance of this matter to the States, let me say that this morning I received word that Commissioner Charles F. J. Harrington, of Massachusetts, who is chairman of the com-

mittee on Federal legislation of the insurance commissioners body, was advised by William P. J. Hodges, insurance commissioner for the State of North Carolina, that some insurance companies had given notice to their States that they would not pay the tax which is being levied in those States, or that they would pay it under protest. Under the law, it would be necessary to suspend the licenses of such companies and of all their agents. The insurance tax would have to be paid by February 15. In South Carolina, Kentucky, and Tennessee the tax is due on February 1.

So it is advisable that the bill be passed quickly, if it is possible to do so.

Mr. WHITE. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. WHITE. Let me inquire whether I am justified in understanding that the bill comes before the Senate with a unanimous report in its favor from the Committee on the Judiciary?

Mr. FERGUSON. The report is unanimous.

Mr. McKELLAR. Mr. President, as I understand the situation, the bill is entirely satisfactory to the State insurance companies.

Mr. FERGUSON. It is entirely satisfactory to the insurance commissioners; and the various organizations of insurance companies have, without exception, so far as my knowledge goes, taken the position that it is satisfactory to them. There is no objection. The bill is a compromise measure; it is the best that could be agreed upon at this time.

Mr. McKELLAR. I am very much in favor of the bill, and I hope it will pass.

Mr. MURDOCK. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. MURDOCK. Does the bill in its present form contemplate that a State legislature may enact laws which would permit agreements in violation of the Sherman Act?

Mr. FERGUSON. I would say that until June 1, 1947, State legislatures could enact laws which would be in conflict with the Sherman Act, but could not pass laws which would permit either an agreement or an act on the part of an insurance company, or insurance companies, of boycott, coercion, or intimidation. If, in the meantime, Congress passed legislation contrary to the laws passed by State legislatures, such State laws would be nullified because, under this bill, and subject to certain exceptions set forth in the bill, insurance is treated as interstate commerce.

Mr. MURDOCK. If I followed correctly the distinguished Senator, he takes the position that the respective State legislatures may pass laws permitting agreements in violation of the Sherman Act.

Mr. FERGUSON. Yes; if the agreements do not violate paragraph (a) or (b) of section 4 of the bill.

Mr. MURDOCK. I invite the distinguished Senator's attention to that part of the report on page 2 which appears under the heading "Purpose of the bill." It is as follows:

It should be noted that this bill, by the moratorium proposed therein, does not repeal the Sherman and Clayton Acts, but opportunity will have been granted for the States to permit agreements and contracts by insurance companies which otherwise might be in violation of the Sherman and Clayton Acts.

It seems to me that while this bill may not specifically repeal the Sherman Act, it does provide for repeal of the Sherman Act by the State legislatures by permitting them to enact laws which would allow agreements and contracts in violation and in derogation of the Sherman Act. Is that not what the bill would do? I believe that its language accomplishes that very thing.

Mr. FERGUSON. As I have already stated, the intent of the bill is to permit State legislation along the line mentioned in the excerpt which the Senator has read, if it does not violate paragraphs (a) and (b) of section 4 of the bill.

Mr. MURDOCK. I invite the Senator's attention to paragraph (b) of section 2 of the bill, reading as follows:

(b) No act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically so provides.

That part of the bill is applicable, is it not, to Federal statutes now in existence?

Mr. FERGUSON. That is the purpose of the section.

Mr. MURDOCK. It is also applicable, is it not, to any Federal statutes which may be enacted in the future?

Mr. FERGUSON. Yes; provided the statutes do not specifically relate to insurance.

Mr. MURDOCK. If the Senator will pardon me, I agree with him that the language affects only statutes the subject of which is insurance.

Mr. FERGUSON. Or specifically relating to insurance.

Mr. MURDOCK. Yes. But certainly that part of the bill to which I have referred would allow repeal by State legislatures of the Sherman Act so far as it relates to insurance unless the Congress of the United States should amend the Sherman Act so as to provide specifically either the repeal, invalidation, or impairment of such a State law.

Mr. FERGUSON. I appreciate the Senator has used the word "repeal." The bill would not go so far as to repeal the Sherman Act except as there would be a temporary repeal until the dates mentioned in the so-called moratorium section.

Mr. MURDOCK. That is the very point which I am making. While the language would not specifically repeal the Sherman Act with regard to insurance or the regulation thereof, it would confer, so far as Congress can confer power on the State legislatures to repeal by State statute the Sherman Act insofar as it relates to the insurance business.

Mr. FERGUSON. Yes; except paragraphs (a) and (b) of section 4. I do not believe that under the bill a State could pass a law permitting an agreement or an act of boycott, coercion, or intimidation.

Mr. MURDOCK. Let us look at that phase of the subject for a minute. We now leave section 2 of the bill and drop down to section 4. Paragraph (a) of section 4 provides for a moratorium, or a suspension of the Sherman and Clayton Acts insofar as they relate to insurance, for a period, respectively, until June 1, 1947, so far as the Sherman Act is concerned, and until January 1, 1948, so far as the Clayton Act is concerned.

Mr. FERGUSON. The Senator is correct.

Mr. MURDOCK. Paragraph (b) reads:

(b) Nothing contained in this section shall render the said Sherman Act inapplicable to any agreement or act of boycott, coercion, or intimidation.

Would the Senator agree to an amendment of the bill which, instead of limiting paragraph (b) of section 4, by the word "section" on page 2, line 23, would strike out that word and insert the word "act"? In that way we would not be limited merely to that one section.

Mr. FERGUSON. The only reason why I believe it should not be done is that the Sherman Act is the only act which relates to boycott, coercion, or intimidation.

Mr. MURDOCK. I do not believe the Senator gets my point.

Mr. FERGUSON. Perhaps I do not.

Mr. MURDOCK. If the Senator will look at page 2, beginning in line 23 of the bill, he will find the following language:

Nothing contained in this section—

Referring to section 4 of the bill—

shall render the said Sherman Act inapplicable to any agreement or act of boycott, coercion, or intimidation.

My suggestion is to strike out the word "section" and insert in lieu thereof the word "act", so that the language would then read:

Nothing contained in this act shall render the said Sherman Act inapplicable to any agreement or act of boycott, coercion, or intimidation.

Mr. FERGUSON. I see no reason for not changing the word "section" to "act," because I am of the opinion that that was the intention of all concerned.

Mr. MURDOCK. I think it would improve the bill very materially.

Mr. O'MAHONEY. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. O'MAHONEY. Perhaps the Senator first wished to make a statement in response to the Senator from Utah.

Mr. FERGUSON. No; I will yield to the Senator from Wyoming.

Mr. O'MAHONEY. Mr. President, in order to have a clear understanding of the bill, the attention of the Senate should be called to the fact that, as the Senator from Michigan has said, over a long period of years the courts have held that insurance is subject to State regulation. It will also be remembered that the question as to whether the Federal antitrust laws applied to insurance was never decided until the Southeastern Underwriters case was before the Supreme Court. On the day on which that

case was decided the Supreme Court handed down another decision in what is known as the Polish-Alliance case in which it held that the National Labor Relations Act applied to insurance. In the Polish Alliance case the Supreme Court said by unanimous decision that the business of insurance was so affected with a national commercial interest that the National Labor Relations Act, which was passed under the commerce clause, applied to the business. On the same day by a divided Court it held that the antitrust laws applied.

It should be pointed out that every case involving the construction of insurance regulation laws which had been passed upon by the Supreme Court down to the time when the Southeastern Underwriters case was decided involved State statutes. Every such case, so far as I am advised, was brought to the Supreme Court because insurance companies had endeavored to escape State regulation. Before the Southeastern Underwriters case was decided bills were introduced in the Congress to exempt insurance wholly and altogether from the effect of the antitrust laws. Those bills failed of enactment. As the unanimous report of the committee says on the first page:

> The Attorney General, in several appearances before the Judiciary Committee, frankly stated that the Department of Justice had no opposition to an extension of time to the insurance industry in order to make necessary adjustments to this decision.

It is stated in another part of the report, on page 2:

> What is more, the Congress proposes by this bill to secure adequate regulation and control of the insurance business.

Another paragraph, under the heading "Purpose of the bill," reads as follows:

> The purpose of the bill is twofold: (1) To declare that the continued regulation and taxation by the several States of the business of insurance is in the public interest; and (2) to assure a more adequate regulation of this business in the States by suspending the application of the Sherman and Clayton Acts for approximately two sessions of the State legislatures, so that the States and the Congress may consider legislation during that period. It should be noted that this bill, by the moratorium proposed therein, does not repeal the Sherman and Clayton Acts.

The Sherman antitrust law contains two primary provisions. The first section of that law, which takes its name from Senator Sherman, of Ohio, makes illegal contracts or agreements in restraint of trade. The second section of the law makes it a misdemeanor for any person or group to make any contract or agreement which monopolizes or attempts to monopolize any part of trade or commerce.

The questions which have been raised by the Senator from Utah prompted me to ask the Senator from Michigan this question: Does the Senator from Michigan conceive that the pending bill as reported by the Judiciary Committee, with the language which I have just read, has the effect of making it possible for a State to legalize contracts in restraint of trade or has the effect of making it possible for any State to authorize attempts on the part of any group of insurance companies to monopolize the business of insurance. I did not understand that to be the opinion of the Senator from Michigan.

Mr. FERGUSON. No. I will answer that by saying that if agreements in restraint of trade or to monopolize amounted either to a boycott and/or coercion and/or intimidation, they would be absolutely void, because they would contradict the bill which is now being considered by the Senate and which it is hoped will be passed today. But certain agreements might be permitted in the States if they did not violate the terms of this bill.

Mr. O'MAHONEY. Does the Senator desire to tell the Senate that it is his purpose and the purpose of the pending bill to say to the State legislatures that laws may be enacted which will permit monopoly to be created in the insurance industry?

Mr. MURDOCK. Mr. President, will the Senator from Michigan yield to me?

Mr. O'MAHONEY. May I ask the Senator from Michigan to respond to the inquiry before he yields?

Mr. FERGUSON. I should like to yield to the Senator from Utah so that he may answer the question.

Mr. O'MAHONEY. I would rather have an answer from the Senator from Michigan.

Mr. FERGUSON. I will answer it later, if the Senator please.

Mr. MURDOCK. I call the attention of the distinguished Senator from Wyoming to the report itself, from which I quote, as follows:

"It should be noted that this bill, by the moratorium proposed therein, does not repeal the Sherman and Clayton Acts but opportunity" is granted to the States by subsection B of section 2 to accomplish this very purpose. Certainly the Congress does not want to do that.

This is the important part of the report, and I think it is in full conformity with the bill itself "but opportunity will have been granted for the States to permit agreements." What kind of agreements? Agreements which do not conflict with the restrictions in subsection (b) of section 4, but "agreements and contracts by insurance companies which otherwise"—"which otherwise"—and I stress these words of the report "might be in violation of the Sherman and Clayton Acts."

Certainly the very purpose of the bill, if subsection B of section 2 is not stricken, is to provide that State legislatures, if they so desire, may relieve insurance companies from contracts in restraint of trade which are prohibited by the Sherman Act, so long as such contracts and agreements do not come within the inhibition of subsection (b) of section 4, which refers to agreements or acts of boycott, coercion, or intimidation. The report itself, in my opinion, answers the Senator from Wyoming.

Mr. FERGUSON. Mr. President, I will answer the question of the Senator from Wyoming in the same way the able Senator from Utah has answered it. Just as he read, the bill provides that agreements or contracts may be permitted by State legislature within the moratorium period if they do not violate paragraph (b) of section 4.

As I read the bill proposed by the able Senator from Wyoming, his measure would permit the same thing if the State acts specifically so provided.

Mr. O'MAHONEY. Mr. President, the bill which was presented by the Senator from Wyoming contained a section which does not appear in the pending bill, a section which undertook to exempt from the effect of the antitrust law certain types of combinations and agreements, but certainly not such an agreement as would enable any State to be in the position of authorizing the establishment of monopoly. It was clearly with the understanding that the bill was a good-faith attempt not to get around the antitrust laws, or the decision of the Supreme Court, but to enable the insurance industry and the States to accommodate themselves to the decision and to the antitrust laws, that the Judiciary Committee made a unanimous report.

I am somewhat surprise, I am frank to say, that the Senator seems to have taken the position now that the intent is to enable any State which so desires to permit national organizations to monopolize the business of insurance. Have I correctly interpreted the Senator?

Mr. FERGUSON. Subject——

Mr. O'MAHONEY. Subject only to a boycott, intimidation, or coercion.

Mr. FERGUSON. In section 4 it is provided "for the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress."

If any State should attempt to pass such legislation, Congress in the meantime could pass laws specifically providing that contracts made thereunder were void, or, if such an act was passed after the moratorium, then it would be void.

Mr. O'MAHONEY. Does the Senator from Michigan desire that the bill, if it shall be passed by this body, shall be interpreted anywhere as an intention of Congress to permit monopoly to be established in the insurance industry?

Mr. FERGUSON. No; by no means does the bill anticipate that any act would or should be passed which would create monopoly.

Mr. O'MAHONEY. Then, does the Senator believe that the bill as it now stands permits that interpretation?

Mr. FERGUSON. It would permit it. I understood the Senator from Wyoming to be familiar with the language on page 2, which was read by the able Senator from Utah, and I think the bill is broad enough to allow a State to pass a law allowing any agreement or contract other than those inhibited in paragraph (b) of section 4. But it is not the purpose of the bill at all to foster monopoly, or to anticipate that any act will be passed permitting or even encouraging monopoly. A State law relating to taxation, a law relating to regulation, for instance, the fixing of rates, or the fixing of the terms of a contract of insurance, which might under some definitions of monopoly be monopolistic, would be permitted under the pending

bill; but if the State law undertook to authorize a boycott, a coercion, or an intimidation, or an agreement to do any one of those three things, then it would be clearly void because Congress would have already spoken, and once Congress speaks on interstate commerce, no State can speak contrary to the congressional declaration.

Mr. MURDOCK. Will the Senator yield on that point?

Mr. FERGUSON. I yield.

Mr. MURDOCK. The bill does not say what the Senator has indicated. What the bill says is that every act of Congress in existence now or which may be enacted in the future dealing with the question of insurance or the regulation of insurance shall not be construed—and that is pretty strong language—"to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically so provides."

So we would do what? We would say to the State legislatures, "You can pass any law you desire with reference to insurance and the regulation thereof which does not involve agreements or acts of boycott, coercion, or intimidation, unless the Congress at some future date specifically repeals or invalidates your State law."

I wonder if the Congress of the United States wants to do that.

Mr. FERGUSON. The bill does not go as far as that.

Mr. MURDOCK. Will the Senator yield for a further observation?

Mr. FERGUSON. I yield.

Mr. MURDOCK. My understanding of what the Senate Judiciary Committee wanted to do and what I hoped it would do was that we would by the enactment of a bill of this kind call the attention of the respective States of the Union to the fact that the Supreme Court of the United States had held that the business of insurance is commerce, and knowing that certain hardships were inevitable because of past practice and procedure, it was my intention, and I thought the intention of the Committee on the Judiciary, to say to the States, "For a certain period, long enough for you to take action, you will be allowed to make adjustments of your State laws to harmonize with the decision of the Supreme Court of the United States." But under the bill we would not do that. In my opinion, we would do exactly what the Senator from Wyoming implies we would do—that is, invite the respective State legislatures to pass acts which would permit agreements which would otherwise be in violation of the Sherman Act.

Mr. FERGUSON. Mr. President, I think an explanation of paragraph (b) of section 2 should be made at this time. The purpose of that provision is very clear, that Congress did not want at the present time to take upon itself the responsibility of interfering with the taxation of insurance or the regulation of insurance by the States. We were able to single out and to indicate that we had in mind three acts of which we wanted to make exceptions, because they did not relate to insurance. I read from the bill:

> SEC. 3. Nothing contained in the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, or the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall apply to the business of insurance or to acts in the conduct of that business.

Now on page 3, and we find section 5:

> SEC. 5. Nothing contained in this act shall be construed to affect in any manner the application to the business of insurance of the act of July 5, 1935, as amended, known as the National Labor Relations Act, or the act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938.

Mr. MURDOCK. Will the Senator yield?

Mr. FERGUSON. Permit me a further word of explanation.

Mr. MURDOCK. Very well.

Mr. FERGUSON. If there is on the books of the United States a legislative act which relates to interstate commerce, if the act does not specifically relate to insurance, it would not apply at the present time. Having passed the bill now before the Senate, if Congress should tomorrow pass a law relating to interstate commerce, and should not specifically apply the law to the business of insurance, it would not be an implied repeal of this bill, and this bill would not be affected, because the Congress had not, under subdivision (b), said that the new law specifically applied to insurance. I think that makes the bill very clear.

Mr. MURDOCK. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. MURDOCK. I am quite satisfied that it is the intention of the Senator and the intention of the Committee on the Judiciary to grant a moratorium and invite the States to step in and regulate the insurance business. It seems to me that if the Senator would agree to striking from the bill subsection (b) of section 2, and then agree to the other amendment which I suggest in subsection (b) of section 4, that we would do that very thing; but we would not take the long step which has been indicated today by the Senator from Wyoming of inviting State legislation, permitting violation of the Sherman Act as to monopolies and agreements in restraint of trade. I do not believe that any Senator wants to invite any State legislature to step into the insurance field and permit contracts and agreements in restraint of trade or contracts and agreements which would evade the monopoly provisions of the Sherman Act.

Mr. McKELLAR. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. McKELLAR. I simply wish to ask, Why is not the Senator willing to accept that amendment? It seems to me it is a very proper amendment.

Mr. FERGUSON. Mr. President, with this one explanation——

Mr. MURDOCK. Does the Senator say that he will agree to that amendment?

Mr. FERGUSON. I wanted to make a statement.

Mr. MURDOCK. I think the amendment would clear the matter.

Mr. FERGUSON. Provided the word "agreement" in subsection (b) of section 4 is understood to relate to boycott, coercion, or intimidation. Is it the interpretation of the Senator from Utah that the word "agreement" in that paragraph relates to boycott, coercion, or intimidation?

Mr. MURDOCK. Yes.

Mr. FERGUSON. With that explanation on the record——

The VICE PRESIDENT. The Chair will state that the pending question is on the committee amendment in line 24, on page 2, and that another amendment is not now in order until the committee amendment is disposed of.

Mr. FERGUSON. At the proper time I shall consent that the word "section" be changed to "act."

Mr. RADCLIFFE. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. RADCLIFFE. I hesitate to differ with the Senator from Utah [Mr. MURDOCK], but I want to call his attention to a fact which is, of course, very obvious, that the difficulties of working out the insurance readjustment following the decision of the Supreme Court are colossal. I do not believe anyone who does not come very closely in contact with the insurance business can realize that the decision by the Supreme Court to which reference has been made is one of the most far-reaching ever rendered by that Court. It means that an enormous business which, with the unqualified approval of the Federal Government, has operated for many years in a certain way, must now meet the new and fundamental conditions involved necessarily in any passage from State to Federal regulation. That does not involve merely one but a thousand-and-one different problems to be handled, many of them around the first of the present calendar year.

Ever since this problem arose it has received the closest attention. On June 6, 1944, the day after the decision of the Supreme Court was rendered, I wrote a letter to the President of the United States and asked for a moratorium, and he wrote me a letter in reply. Subsequently, on December 20, 1944, the day after the adjournment of the last Congress, I again wrote the President in regard to a moratorium, to which he replied on January 8. I do not desire to delay the Senate by reading the correspondence, but I ask permission that the letters addressed by me to the President and his replies thereto be printed in the RECORD at the conclusion of my remarks.

The VICE PRESIDENT. Without objection, permission is granted.

(See exhibit A.)

Mr. RADCLIFFE. Mr. President, I called the President's attention to the gravity of the situation and asked for a moratorium. His response was favorable, as it was later in answer to my letter of December 20. Of course, no one knows what legislation any State might try to pass. It might try to pass any sort of legislation, but it is extremely unlikely that any State, knowing that as

the end of several years the moratorium provided for in this bill will come to an end would try to run amok and pass any such law as the Senator from Utah suggests.

In subsection (b) there are several purposes contemplated. The insurance commissioners and many of the insurance companies have been in very great doubt as to how they could operate at this time with respect to matters of collection of premiums, general regulations, the issuing of licenses, and many other aspects of the business. Therefore, it seems very desirable that somewhere in this measure there should be a statement that the right of the States to regulate and to collect taxes should not be terminated or should not be repealed by implication. Otherwise, I think the States may find themselves from time to time in a very serious situation in trying to function. Unless it is clearly stated somewhere that there is not a repeal by implication, such omission is likely to throw restraint upon or put serious hindrance in the way of the States functioning properly. In giving a moratorium to a business and to State governments harrassed greatly by the effect of the decision of the Supreme Court, let us not do so begrudgingly or in a halfway fashion which might prove to be gravely insufficient to meet situations which we cannot today foresee.

EXHIBIT A

Hon. FRANKLIN D. ROOSEVELT,
President of the United States,
The White House.

MY DEAR MR. PRESIDENT: The decision of the Supreme Court yesterday, reversing the long-time settled law in that the Court decided that insurance comes under the supervision of the Sherman Antitrust Act, is I think, one of the most far-reaching which has been rendered for a long time.

Of course it means in substance probably that the insurance industry, one of the largest in the country, will be turned over from the supervision of the States to that of the Federal Government. The demand upon manpower and time of the Federal Government to take over this gigantic industry cannot be satisfied, I assume, without very heavy strain upon the energies of the Federal Government in carrying on our war program.

Several months ago in talking to Attorney General Biddle I urged that if *Paul v. Virginia* were reversed that the Government should not only be slow to attempt to upset all the existing arrangements authorized by the States, but should also issue reassuring statements that there would be no haste. I have the impression that the Government intends to show some restraint in this matter.

The Bailey-Van Nuys bill has been held in the Judiciary Committee awaiting the decision of the Supreme Court in the case just decided.

It is very fortunate that the insurance interests, although under State control, stood very staunchly during the depression, and I understand that State officials, boards of trade, and insurance interests quite generally have registered vigorous opposition to the suggested shift from State control to Federal.

I have studied the matter carefully for years and have seen no adequate justification for such a shift. It seems to me that such a transfer in time of war, and I may add in a political campaign, is especially unfortunate.

Very respectfully.

GEORGE L. RADCLIFFE.

THE WHITE HOUSE,
Washington, June 10, 1944.

Hon. GEORGE L. RADCLIFFE,
United States Senate, Washington, D. C.

MY DEAR SENATOR RADCLIFFE: I have your letter of June 6 with respect to the recent decision of the Supreme Court deciding that insurance comes under the provisions of the Sherman Act. You suggest that this would probably mean supervision by the Federal Government.

The Attorney General advises me that he does not believe that this alternative is inevitable or even probable. He tells me that there is nothing in the decision which prevents the regulation by the States of insurance rates as long as that regulation does not interfere with the provisions of the Sherman Act.

Personally, I know of no effort at this time to bring insurance companies under over-all Federal regulation. Whether or not such control were adopted would depend, I think, very much on the attitude of the companies themselves in complying with the provisions of the Sherman Act.

The Attorney General assures me that he is anxious that the insurance companies and the State insurance officials shall have a reasonable time within which to conform their practices and statutes to the decision of the Supreme Court.

With best regards always,

Very sincerely yours,

FRANKLIN D. ROOSEVELT.

DECEMBER 20, 1944.

MY DEAR MR. PRESIDENT: I am writing this note in regard to the insurance situation. On June 6, 1944, one day after the very far-reaching decision of the Supreme Court reversing *Paul v. Virginia*, I wrote a letter to you emphasizing what I thought was the gravity of the situation. I suggested that you declare a sort of moratorium during which essential adjustments could be made to the new decision. I also requested that you issue a reassuring statement to the industry suddenly facing problems of a grave and unprecedented nature. On June 10 you very kindly wrote me a letter in which your position was, on the whole, favorable to what I had requested.

Since that time the insurance industry, insurance commissioners, certain officials of the Federal Government, Members of Congress, and others have been endeavoring to work out an arrangement which would seem to be adequate. Likewise the status as to State taxation and other forms of State regulation have been questioned in some channels.

The adjournment of Congress has come before such plans could really be carried out. I have been in close touch with Attorney General Biddle, who has been very helpful. It is my impression that he is in favor of a suitable moratorium, but there are some departments of the Federal Government closely involved which do not come under the supervision of the Attorney General.

I again very respectfully suggest that you give expression to some form of moratorium under which State activities could continue freely pending Federal and State legislation which will undoubtedly be passed and put into operation within the very near future.

I am sure everyone is in accord with the idea you expressed in your letter to me of June 10, that the insurance industry which is one of the largest and most important in this country should have every reasonable opportunity for readjustment.

Sincerely yours,

GEORGE L. RADCLIFFE.

JANUARY 2, 1945.

MY DEAR SENATOR RADCLIFFE: In your letter of December 20, you suggest that there should be some form of a moratorium during which insurance companies will have an opportunity to readjust their practices in order to bring them into conformity with the Supreme Court decision in the South-Eastern Underwriters Association case, and during which legislation might be enacted. The Attorney General advises me that several months ago he told the Senate Judiciary Committee that no new antitrust prosecutions against insurance companies would be instituted during a reasonable readjustment period.

The responsibility for the regulation of the business of insurance has been left with the States; and I can assure you that this administration is not sponsoring Federal legislation to regulate insurance or to interfere with the continued regulation and taxation by the States of the business of insurance. But there is no conflict between the application of the antitrust laws and effective State regulation of insurance companies, and there is no valid reason for giving any special exemption from the antitrust laws to the business of insurance. The antitrust laws prohibit private rate fixing arrangements between insurance companies and acts of boycott, coercion, or intimidation. The antitrust laws do not conflict with affirmative regulation of insurance by the States such as agreed insurance rates if they are affirmatively approved by State officials.

Senator O'MAHONEY introduced a bill in the last Congress which would have provided for a moratorium from the Sherman Act, except for acts of boycott, coercion, or intimidation, until March 1, 1946. This would appear to give sufficient time to permit the necessary readjustment to the Supreme Court decision. I would favor legislation of this general character. It would permit the orderly correction of abuses which have existed in the insurance business and would preserve the right of the States to regulate with full responsibility.

Very sincerely yours,

FRANKLIN D. ROOSEVELT.

Mr. MURDOCK. Mr. President, will the Senator yield?

Mr. FERGUSON. I should like to answer the question of the Senator from Maryland first. The language of section 2 answers the question:

> The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

That is the insurance business. So the bill specifically provides that the State laws shall apply to taxation and regulation of insurance.

Mr. MURDOCK. Mr. President, will the Senator now yield?

Mr. FERGUSON. I yield to the Senator from Utah.

Mr. MURDOCK. I wanted to make exactly the statement to the distinguished Senator from Maryland that the Senator from Michigan has made, and that is that nothing could be more emphatic or plainer than subsection (a) of section 2:

> The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

When we go that far Congress expresses itself emphatically that the regulation of the insurance business should be under State law. But when we take the next step in subsection (b) it is an invitation, in my opinion, to do the very thing that I, and I hope the Senator from Maryland, want to prohibit.

Mr. RADCLIFFE. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. RADCLIFFE. I agree with the Senator from Utah that the statement in subsection (a) of section 2 is quite definite and clear. But it has seemed to those who have been working upon this bill that there was some need or at least advisability that there should not be any repeal by implication. The statement beginning on page 1 is a general statement setting forth the purposes.

Since there seems to be doubt in the minds of certain people that there might be repeal by implication or that a general statement might have some crimping effect, it would not be at all unusual if a saving clause were put in the bill. It may not be necessary, but in the spirit of caution I think it might be desirable, especially knowing the very serious problems which have been confronting the insurance companies and the various States to leave them free to meet conditions some of which cannot now be foreseen. We want the companies to understand clearly and we desire the States to realize definitely that the States can go ahead and issue permits, collect taxes, and do the various other things which are necessary to be done. For that reason I think that full and unmistakable emphasis upon that right is essential. It is unnecessary and unwise to create any doubt as to the right of the States to go ahead and function freely in handling insurance.

Mr. FERGUSON. Mr. President, I agree that it should be very clear that the States can regulate and can tax insurance in all its phases. Section 2, in my humble judgment, is a very clear provision providing for such taxation and such regulation. The language of the bill makes clear the purpose of the legislation, that the taxation problem will be taken care of, and that there will be no excuse for paying under protest or not paying at all.

The VICE PRESIDENT. The question is on agreeing to the committee amendment on page 2, line 24.

The amendment was agreed to.

Mr. MURDOCK. Mr. President, I move to amend by striking subsection (b) of section 2 from the bill.

The VICE PRESIDENT. The question is on agreeing to the amendment offered by the Senator from Utah [Mr. MURDOCK].

Mr. FERGUSON. Mr. President, I should like to speak for a few moments on the amendment.

The purpose of the bill would be nullified if the amendment were to be adopted. Today the various States have laws relating to insurance. It would be a physical impossibility to examine, in a short time, all those State laws and their ramifications. One State law provides that the insurance companies may fix rates subject to the approval of the insurance commissioner. Others provide that rates may be fixed if the Commission does not repeal them.

Mr. O'MAHONEY. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. O'MAHONEY. Does not subsection (a) of section 2 take complete account of that fact, and grant complete protection to existing State laws?

Mr. FERGUSON. I agree that, as to existing State laws, subsection (a) of Section 2 does so provide.

Mr. O'MAHONEY. Let me read it:

> The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

That is complete.

Mr. FERGUSON. I think that is correct.

Mr. O'MAHONEY. There is no reason for misunderstanding on the part of any State official or any insurance company or any policyholder with respect to the meaning of that subsection as it applies to existing law.

Mr. FERGUSON. As it applies to existing law, that is correct. However, subsection (b) provides for something further. It provides that no Federal legislation relating to interstate commerce shall by implication repeal any existing State law unless such act of Congress specifically so provides.

Mr. O'MAHONEY. The Senator puts his finger upon the precise center of this dispute, or misunderstanding. Let me say to the Senator that, recognizing the complexity of this problem, and the desirability of maintaining State regulation and State taxation, members of the Judiciary Committee who were opposed to the proposal to grant a blanket exemption from the antitrust laws desired to go as far as was humanly possible in the direction of giving the States a clear-cut opportunity to adjust State laws in accordance with Supreme Court decisions and the antitrust laws.

It is no secret that Senate bill 12, introduced by the Senator from New Mexico [Mr. HATCH] and myself, and Senate bill 340, the bill which was reported by the committee, are modifications of a measure which was originally drafted by the legislative committee of the National Association of Insurance Commissioners. So there was an effort to work with those groups. In drafting those two bills we sought to spell out each particular law which might apply to insurance. We referred specifically to the Federal Trade Commission Act, the Robinson-Patman Act, the National Labor Relations Act, and the Fair Labor Standards Act. In other words, a good-faith attempt was made to specify every single law which had an application, or might have an application, to insurance.

Section 2 (b) was drafted and written into the bill which I introduced, in the belief, not that it would be interpreted as an additional exemption from the antitrust laws, but that it would be a sort of catch-all provision to take into consideration other acts of Congress which might affect the insurance industry, but of which we did not have knowledge at the time.

I am sure that the Senator from Michigan does not wish to ask the Senate, in view of the interpretation which has been placed upon this section, to enact that provision. To do so would put us in the position of saying that any State, if it so desires, may authorize monopolies. I suggest to the Senator from Michigan that the elimination of subsection (b) of section 2, as suggested by the Senator from Utah, would not in any way, shape, or form prevent carrying out the understanding which was had with State insurance commissioners.

The bill which we drafted grants a clear-cut moratorium for a much longer period than the Department of Justice had originally suggested, which was acceptable to some Members of the Senate and some of the insurance companies. Furthermore, it grants a moratorium from those provisions of the Clayton Act which have to do with interlocking directorates. In that case the moratorium is 6 months longer than that proposed to be granted for the purpose of adjusting State laws to the antitrust laws.

Section 4 provides as follows:

> For the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress until June 1, 1947, the act of July 2, 1890, as amended, known as the Sherman Act, shall not apply to the business of insurance—

And so forth. I submit to the Senator from Michigan that this represents a good-faith effort on the part of all concerned to extend to the States an opportunity to approach this problem in the light of the Supreme Court decisions and in the light of the antitrust laws.

No one is more ready than I to acknowledge that the insurance industry is a very complex industry, and that opportunity ought to be extended for necessary adjustments. However, the charges which have been made have been made not by the Government but by persons engaged in the insurance industry; not by any Member of Congress but by policyholders and agents and those who have been affected by the insurance industry. It has been charged that improper attempts have been made to monopolize this business.

As I understand, it is not the purpose of the Senate to grant opportunity for such monopoly. It is the purpose to enable the States and the Congress to make a good-faith effort to adjust themselves to the industry and the conditions which now exist; and I trust that the Senator from Michigan will accede to the suggestion made by the Senator from Utah and accept the amendment.

Mr. BUSHFIELD. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. BUSHFIELD. This whole controversy arose, Mr. President, because of the custom and practice, which had grown up in this country during a period of 75 years and which had been upheld by the courts of the country, of not considering insurance to be commerce. The Supreme Court finally decided otherwise.

Subsection (b), which has been referred to in the present discussion, does not, it seems to me, relate at all to the learned remarks just made by the Senator from Wyoming.

The subsection reads in part as follows:

> SEC. 2. (b) No act of Congress shall be construed to invalidate, impair, or supersede any law—

And so forth. The whole crux of the subsection is the word "construed."

The purpose of the framers of the bill, Mr. President, was to provide against a sudden adverse decision by some court in construing this Act or some State act thus throwing the business of insurance into confusion. The word "construed" is the whole crux of that particular subsection. I think to eliminate it would destroy the assurance given by the bill to the insurance business, and I would vote against eliminating it.

Mr. FERGUSON. Mr. President, I think it can fairly be stated that today absolute chaos exists in the insurance world, and it has been caused by the decision of the Supreme Court to which we have referred. The pending bill is an attempt to remove and dissipate that chaos by enacting a law by which the insurance companies will be able to abide for the time being.

As I said before, the State of North Carolina, which I am informed uses the revenue obtained from the taxation of such companies for the payment of pensions, has advised us that by February 15 of this year it will be compelled to suspend the licenses of certain insurance companies and all their agents to do business there because the companies have decided that under the present chaotic conditions they do not wish to pay the tax. They do not know whether they should or should not pay it. If subsection (b) is deleted, I am of the opinion that we shall accomplish nothing by enacting the bill; because the insurance companies will still be unable to decide what they can or cannot do, and for that reason they will abide by the provisions of the State laws, and the present chaos will continue.

I think it is fair to say that a great deal of time and attention have been devoted to preparation of the pending bill. The able chairman of the Committee on the Judiciary is the coauthor of the bill. It was submitted to various insurance companies—fire insurance, life insurance, marine insurance, and casualty insurance companies, and so forth—through the insurance commissioners of the various States, because the Commissioners were aware of the chaotic condition which exists at the present time.

After almost a week of work upon the bill, which in similar form was introduced in the last session, it was possible to reach an agreement under which the insurance companies believed they could work, for the time being, until January 1, 1947, and until January 1, 1948. The two separate dates were provided because we wished to allow sufficient time for two sessions of the State legislatures to be held. For instance, the Clayton Act applies to interlocking directorates. It was the opinion of the insurance commissioners and the insurance companies that it would be impossible to change the interlocking directorate laws of the State unless a considerable period of time were allowed. That is the reason why two dates for the so-called moratorium are provided.

The bill does not provide for repeal of the Clayton Act or of the Sherman Act, because if an attempt were made to repeal them, before they could again become effective it would become necessary to reenact them. So the language of the bill is such as to provide that they will be in full force and effect, except there will be a moratorium for a certain period. Thus there will be no necessity for the reenactment of those laws so as to make them apply to insurance in the future, unless Congress desires to do so by specific legislation.

Mr. TAFT and Mr. MURDOCK addressed the Chair.

The VICE PRESIDENT. Does the Senator from Michigan yield, and if so, to whom?

Mr. FERGUSON. I yield to the Senator from Ohio.

Mr. TAFT. I wish to ask whether it might meet the objection of the Senator from Wyoming if the word "heretofore" were inserted in subsection (b), so as to make it read:

> No act of Congress shall be construed to invalidate, impair, or supersede any law heretofore enacted by any State—

And so forth. That would certainly eliminate the possibility of its application to future State action. My interest is to preserve the State laws of Ohio, for instance, which tax insurance companies and bring in certain amounts of revenue. I do not wish to have those laws changed.

Mr. FERGUSON. Mr. President, I should like to say a word in my own right on that point. By the provisions of the bill we are in effect asking the legislatures to put their own houses in order during the next 2 years. The danger of inserting the word "heretofore," as the able senior Senator from Ohio has just proposed, is that the legislatures would be unable to pass any laws which in their opinion might violate the provisions of that subsection.

Mr. TAFT. We wish to have them put their houses in order by adopting laws which do not conflict with the Sherman Act. As I understand the provisions of the bill, it would allow a period of 2 years during which such legislation might be adjusted to the provisions of the Sherman Act or other existing Federal statutes.

Mr. FERGUSON. At the present time, every State rate-fixing authority violates the Sherman Act or the Clayton Act, or both. There are many State laws which violate the Sherman Act and the Clayton Act. It is our purpose to permit those laws to continue in force and effect until at least 1947 and 1948.

Mr. TAFT. Yes; but this section will not cease to be effective in 1947 or 1948; it will go on forever. If the Senator could provide a limit—for instance, until 1947—that would be helpful, although it is difficult for me to understand how it is possible to provide that an act of Congress shall be construed one way for 2 years and another way thereafter. It seems to me it would be necessary to change the language of the section.

Mr. FERGUSON. I would have no objection to inserting the words "until January 1, 1948."

Mr. MURDOCK. Mr. President, will the Senator yield to me for a question?

Mr. FERGUSON. I yield.

Mr. MURDOCK. I think the distinguished senior Senator from Ohio has put his finger on the crux of the matter. If it is the intention of the Senator from Michigan to provide a moratorium for the States, in order to allow them to put their houses in order, so that their laws may conform to the decision of the Supreme Court of the United States, then certainly it is inconsistent to include subsection (b) of section 2 in its present form. I am in agreement with the Senator from Ohio in believing that in all probability the amendment offered by me would be fully taken care of if the word "heretofore" were inserted at the proper place in subsection B of section 2, rather than to strike out the whole subsection. The language then would read:

> No act of Congress shall be construed to invalidate, impair, or supersede any law heretofore enacted by any State—

And so forth. I know the Senator certainly will agree to the adoption of my amendment, with the change suggested by the Senator from Ohio.

Mr. FERGUSON. Mr. President, the purpose of the bill is not only to permit the States to put their houses in order, but to attempt to do away with the confusion and chaos which now exist, so that at least until the date stated in section 4, the moratorium section, the respective States may enact legislation on such subjects, except as forbidden in the bill. I hope that the Senate today will approve the bill in its present form so that it may be made applicable by February 1 in order that the States may tax and regulate.

Mr. MAYBANK. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. MAYBANK. Earlier in the day the Senator from Michigan spoke to me about the situation in South Carolina and with regard to communications which were received last year with reference to the pending subject. I wonder if the Senator from Michigan has any comment to make upon what others who are interested in the matter thought with regard to the particular section under discussion.

Mr. FERGUSON. I have been in touch with two officers of the legislative committee of the State insurance commissioners and they have advised me that the various commissioners desire that the bill be passed in its present form. So far as I know, no objection to the bill in its present form has been made by the commissioners.

Mr. MAYBANK. I thank the Senator for the information he has given, which accords with the information I had already received.

Mr. RADCLIFFE. Mr. President, as the Senator from Michigan said a few moments ago, the purpose of the bill is not only to afford time to the States to readjust themselves to the decision of the Supreme Court, but to give them an opportunity to function without hindrance. Efforts were made by some persons connected with the insurance business, by insurance departments, and by the Department of Justice, to draft legislation immediately and to come before the Congress with the statement that they thought such legislation was necessary in order to comply with the deci-

sion of the Supreme Court. But after the matter had been given careful consideration it was realized that the drafting of a necessary bill could not be done quickly. Therefore it is highly imperative that time should be afforded for certain studies to be conducted, and they cannot be made unless a moratorium is granted.

It is not now possible to foresee all the questions which may arise for consideration in the future, and it is likewise not possible for us to know what may be the restrictive effect of some of the Federal statutes now in existence. It is gravely dangerous to assume that there are no hidden restrictions which may arise to plague and harass us. Because of the present language of the bill, difficulties might arise and seriously interfere with the work of transition from State to Federal regulation, which is one of the most far-reaching moves with which any industry in this country has ever been confronted. I believe that language should be inserted in the bill which would protect us from such a danger. The insurance commissioners also believe such precautionary provisions should be inserted. Many persons who have studied the matter very carefully feel that obstacles may arise which cannot now be foreseen and provided against, and, therefore, that the bill we pass should be very clear and clean-cut. I believe that is the justification for the provision to which reference has been made.

Mr. TAFT. Mr. President, will the Senator yield?

Mr. MURDOCK. I yield.

Mr. TAFT. I think there is an ambiguity in the bill. Assume that no more legislation were enacted and in 1948 a case should arise involving the question. Does the Sherman Act invalidate any State law under this bill? In section 4 (a) of the bill it is implied that in 1948 the Sherman Act shall again come into force unless something has been done in the meantime. However, in section 2 (b) it is implied that even in 1948 the Sherman Act shall not invalidate any State regulatory law. I think that in that respect the bill is ambiguous on its face. We should straighten out the difference between the two sections.

Mr. RADCLIFFE. I would assume that at the end of the period of moratorium the Clayton Act and the Sherman Act would apply.

Mr. TAFT. Paragraph (b) of section 2 of the bill states that "No act of Congress shall ever presume to invalidate a State law on the subject of insurance."

Mr. FERGUSON. I suggest that we could remedy the defect by making the subsection read: "Until January 1, 1948, no act of Congress," and so forth.

The VICE PRESIDENT. Does the Senator from Michigan offer that as an amendment to the amendment offered by the Senator from Utah [Mr. MURDOCK]?

Mr. FERGUSON. I offer it as an amendment to the amendment.

Mr. RADCLIFFE. If what the Senator from Ohio has said is true, or if there is any doubt of it, it would be well to clarify the language. It was clearly the understanding of those drafting the bill that at the end of 1948 the moratoriums would come to an end.

The VICE PRESIDENT. Will the Senator from Michigan state his amendment to the amendment?

Mr. FERGUSON. On page 2, in line 4, after "(b)", I move to strike out "No" and insert the words "Until January 1, 1948, no."

Mr. MURDOCK. Mr. President, as I understand, the pending question before the Senate is my amendment.

The VICE PRESIDENT. The Senator from Utah offered to amend by striking out paragraph (b) of section 2 on page 2. The Senator from Michigan [Mr. FERGUSON] has offered a perfecting amendment which takes precedence over the amendment of the Senator from Utah.

Mr. MURDOCK. May I ask the Senator from Michigan to state again what he is offering by way of amendment?

Mr. FERGUSON. On page 2, in line 4, after "(b)", I move to amend by striking out "No" and inserting "Until January 1, 1948, no."

The VICE PRESIDENT. The question is on agreeing to the amendment offered by the Senator from Michigan to the amendment of the Senator from Utah.

Mr. MURDOCK. Mr. President, I ask for time to enable me to understand clearly the proposed amendment of the Senator from Michigan. My present understanding is that the Senator offers to amend——

The VICE PRESIDENT. The Chair will ask the clerk to read the amendment of the Senator from Michigan.

The LEGISLATIVE CLERK. On page 2, line 4, after "(b)", it is proposed to amend by striking out the word "No" and inserting the words "Until January 1, 1948, no", so that the subsection will then read: "(b) Until January 1, 1948, no act of Congress shall be construed to invalidate, impair", and so forth.

Mr. MURDOCK. Mr. President, it is my judgment that the amendment of the Senator from Michigan would bring about complete harmony between section 2 and section 4. I ask unanimous consent to withdraw my amendment at this time in order that the Senate may act upon the amendment offered by the Senator from Michigan.

The VICE PRESIDENT. Without objection, the amendment of the Senator from Utah is withdrawn.

Mr. REVERCOMB. Mr. President, I have listened with interest to the discussion concerning the amendment to paragraph (b) of section 2. It occurs to me that not only does the proposed act provide for a suspension of the Clayton Act and the Sherman Act, but the very purpose of it is to restore the control of the insurance business to the States. If we make the change proposed in this section and say "until January 1, 1948", then the bill in its completeness will end in 1948. The present provision is—and this was the measure reported unanimously by the Committee on the Judiciary—

No act of Congress—

Existing at this time, or passed before this, or to be passed in the future—

shall be construed to invalidate, impair, or supersede any law enacted by any State * * * unless such act specifically so provides.

I do not think there should be any limitation of time in the provision. We do not want the law to end on January 1, 1948. We want the business left in the control of the States, unless by enactment in the future we specifically state that we do not want something they are doing to be continued.

Therefore, I call to the attention of the able Senator from Michigan the fact that if the language suggested by him shall be written into the bill, this very section will become ineffective on January 1, 1948.

What is the danger of the language as written?

Mr. MURDOCK. Will the Senator yield?

Mr. REVERCOMB. Not at the moment. What is the danger of the language as written, when it provides that no act of Congress shall be construed to invalidate a State law dealing with insurance unless the act of Congress specifically states that it is intended so to do? That saves the power of Congress. Why provide an automatic ending of this provision, if it is the intent of Congress today to leave to the States the conduct of the insurance business and the taxing of the insurance business, because if the States cannot control the companies, the States cannot tax them. The companies are refusing to pay taxes to the States, and that is one of the things which have brought forth this proposed law. Why provide an automatic termination upon a declaration of policy by fixing a date of termination?

Mr. TAFT. Mr. President, will the Senator yield?

Mr. REVERCOMB. I yield.

Mr. TAFT. The Senator's suggestion might be pertinent if it were not absolutely contradicted by section 4, which provides that on June 1, 1947, the Sherman Act shall again apply to the business of insurance. If we leave that provision in the bill, the one now being discussed is inconsistent with it, because if the Sherman Act applies to the business of insurance, any State law which authorizes a rating bureau becomes invalid, or those engaged in the business are subject to Federal prosecution for complying with the State law.

Mr. REVERCOMB. The only two Federal laws mentioned are the Clayton Act and the Sherman Act, and the purpose of mentioning those specifically is to require the States so to enact legislation as not to violate those two existing laws. If any legislation is enacted in the future, whatever it may be—I cannot contemplate it today—if any law shall be enacted by the Congress on interstate commerce which could possibly affect the business of insurance and bring it within the general term "interstate commerce," it would apply. Why not let the provision stand that it shall not apply unless Congress specifically says in an act that it shall apply to the business of insurance, which we are now trying to return to the States?

Mr. MURDOCK. Will the Senator yield?

Mr. REVERCOMB. I yield.

Mr. MURDOCK. If I understand the Senator correctly, he intends by the proposed act to bring about the repeal of the Sherman Act insofar as it applies to insurance.

Mr. REVERCOMB. No, if by "repeal" is meant specific repeal of the act. What we mean to do is to say to the States, "You can regulate insurance, but you cannot provide for anything that will violate the Sherman antitrust law or the Clayton Act, after the dates fixed in the bill, namely, 1947 and 1948.

Mr. MURDOCK. If the Senator will indulge me for a moment, if that is what the Senator intends, then certainly what has been called to his attention by the distinguished Senator from Ohio is applicable. What subsection (b) does, and what I object to, is that very thing. It permits the States to repeal the Sherman Act. The Senator does not want that, nor do I. What we do want to do is to grant the States a moratorium during which they can make their State laws conform to the Supreme Court decision, and regulate insurance. But if we pass the proposed law with subsection (b) of section 2 in it, it not only refers to the existing laws of the Federal Government, but to all future laws of the Federal Government. What the Senator from Michigan proposes brings subsection (b) of section 2 in line with section 4, which follows, and grants what the distinguished Senator from West Virginia wants, if I understand him, that is, a moratorium until June 1, 1947.

Mr. REVERCOMB. As I see it, two things are proposed by this bill. Not only a moratorium with respect to the Sherman Act and the Clayton Act—and we all agree that that is its purpose—but it goes further than that, if I may say so to the able Senator, and carries out the purpose of giving power to the States of regulation of insurance and the taxing of insurance companies, so long as they do not get into conflict with a Federal law. The section before us provides that no act of Congress shall be construed to invalidate a State law unless the act of Congress specifically states that the State law is in conflict with the Federal act and is designed to override it.

Mr. MURDOCK. Will the Senator yield further?

Mr. REVERCOMB. I yield.

Mr. MURDOCK. Then it is applicable, it does apply, does it not, to the Sherman Act, and also to the Clayton Act, presently, because neither one of those acts specifically repeals or impairs or invalidates any State law?

Mr. REVERCOMB. I do not agree with that conclusion, because section 4 of the bill specifically says that the Clayton Act and the Sherman Act shall again be in force on the dates mentioned.

Mr. MURDOCK. That is what the Senator from Ohio called to the Senator's attention, that there is an inconsistency in the two sections, which is clarified by the amendment offered by the Senator from Michigan.

Mr. REVERCOMB. I do not think there is an inconsistency when they are read together. One says that no act of Congress shall be construed to invalidate unless Congress specifically says that it shall invalidate. Section 4 provides specifically with respect to the Sherman Act and the Clayton Act. Subsection (b) of section 2 would apply to all other laws. Section 4 (a) applies to the Sherman Act and the Clayton Act. I think the sections can be read together. But I wish to say to the Senator from Michigan that if he inserts the language "until January 1, 1948," as the time to which that section shall be in effect, he automatically terminates it at that time, and automatically terminates the control of the States over insurance.

Mr. FERGUSON. Mr. President, after a little more thought about the language proposed, I am of the opinion that we could make the bill further the purpose we had in mind by not changing it as suggested by the able Senator from Ohio, but changing it in this way, making it read:

> No act except the Sherman Act—

And inserting the date—

> and/or the Clayton Act—

Inserting the date—

> shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically so provides.

In other words, the case before the Supreme Court was a case applying the Sherman Act and the Clayton Act. We wanted to have the Clayton Act and the Sherman Act apply to insurance, but we did not want to go back into all the laws which had been enacted respecting interstate commerce and apply them to the business of insurance. So I should like to have the able Senator from Ohio withdraw his amendment.

Mr. TAFT. I did not offer the amendment; the Senator himself offered it.

Mr. FERGUSON. I withdraw the amendment.

The VICE PRESIDENT. The Senator has the right to withdraw his amendment.

Mr. FERGUSON. I propose an amendment in line 4, on page 2, after the words "No act," to add "except——

Mr. REVERCOMB. Mr. President, I suggest to the Senator from Michigan the phraseology "except as hereinafter provided in section 4."

Mr. FERGUSON. I think we should refer specifically to the two acts by name and by date. I think the language should be:

> No act—

And then we should insert the words:

> except the act of July 2, 1890, as amended, known as the Sherman Act, and/or the act of October 15, 1914, as amended, known as the Clayton Act.

Mr. O'MAHONEY. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. O'MAHONEY. That amendment should come in after the word "Congress" and not after the word "act."

Mr. FERGUSON. That is correct. The amendment should come after the word "Congress."

The VICE PRESIDENT. The amendment will be stated, so that Senators may understand it.

The LEGISLATIVE CLERK. On page 2, line 4, after the word "Congress", it is proposed to insert "Except the act of July 2, 1890, as amended, known as the Sherman Act, and/or the act of October 15, 1914, as amended, known as the Clayton Act."

Mr. MURDOCK. Mr. President, will the Senator yield to me?

Mr. FERGUSON. I yield.

Mr. MURDOCK. I think the language now proposed by the Senator from Michigan is more clarifying than anything he has offered heretofore, and in my opinion, Mr. President, brings subsection (b) of section 2 and section 4 in complete alinement and harmony. I hope the amendment will be adopted.

Mr. TAFT. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. TAFT. What bothers me about the amendment is that it implies that the measure may invalidate fees or taxes upon such business. The Senator might add at the end of section 4 "or to be construed to invalidate, impair, or supersede any law enacted by any State for this purpose", and so forth, during that period. The difficulty with the Senator's amendment is that it suggests at least that these two acts, even before 1947, although they do not apply to the business, might possibly invalidate a State law. I do not want the bill to carry that implication.

Mr. FERGUSON. Would the Senator explain again just where he would insert his proposal?

Mr. TAFT. At the end of section 4, line 22 on page 2, the Senator might add this language "or to be construed to invalidate, impair, or supersede any law enacted by any State", and so forth.

Mr. FERGUSON. Does the Senator feel that the words "shall not apply" are not as broad as the words now proposed by the Senator? We would use language to the effect that the Sherman Act shall not apply; we except it in subsection (b), and then we say it shall not apply. So if it does not apply, I do not see how we can say that it would interfere with the taxation or the regulation of insurance.

Mr. TAFT. Perhaps I am unduly concerned, but I am afraid the insurance companies which are doubting the validity of the taxes imposed upon them will not be greatly soothed by subsection (b) of section 2 as proposed to be amended by the Senator, because it excepts the two laws. I think we will then have to look to section 4.

Mr. FERGUSON. We eliminate everything from subsection (b) except two laws, and then we say in section 4 that those two laws shall not apply until certain dates. I think the language now is very clear as to what we mean.

Mr. ELLENDER. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. ELLENDER. The fact remains that the Sherman and Clayton Acts are excepted by your amendment, therefore they shall be construed to invalidate, im-

pair, or supersede any State laws enacted for the purpose of regulating the business of insurance, or which imposes a fee or tax.

Mr. FERGUSON. Then we say in section 4 that they shall not apply, and that is an all-inclusive application, that they shall no longer so apply.

Mr. ELLENDER. There is a conflict. I do not see the necessity for the amendment. It nullifies one of the purposes for which the bill is being enacted. Mr. President, I ask that subsection (b), as proposed to be amended, be now read and I will ask the close attention of Senators.

The VICE PRESIDENT. The clerk will read.

The legislative clerk read as follows:

(b) No act of Congress, except the act of July 2, 1890, as amended, known as the Sherman Act, and/or the act of October 15, 1914, as amended, known as the Clayton Act, shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically so provides.

Mr. ELLENDER. Mr. President, as I understand the pending measure it has two main purposes: First. A declaration of policy by the Congress that the continued regulation and taxation by the several States of the business of insurance is in the public interest and that the States shall continue to regulate and tax it, unless Congress specifically legislates on the subject matter to the contrary. Second. A moratorium is declared making ineffective the Sherman and Clayton Acts for a time specified in section 4 (a) of the bill so that States can adjust their laws on the subject. The Judiciary Committee made a careful study of the problems involved and has reported the bill and I believe that the bill as it came from the committee is not ambiguous, but carries out the purposes above set forth by me.

The pending amendment, in my judgment, nullifies the first purpose of the bill. Although the Clayton and Sherman Acts are suspended by section 4 (a), they shall be construed to invalidate, impair, or supersede any law enacted by a State for the purpose of regulating the business of insurance or which imposes a fee or tax upon such business, if the pending amendment is adopted.

Many insurance companies refuse to pay licenses and taxes in many States, I am informed, because of the Supreme Court decision in United States against Southern Underwriters Association et al., and to now except those two acts, which formed the basis of the decision and, in effect, state that they shall be construed to invalidate State laws on the question of taxation and regulation of the insurance business is bound to lead to much confusion.

Mr. FERGUSON. I take it the language now used would be very confusing. The bill excludes all acts except those enumerated. We will have to change the language so as to make all other acts not applicable except the Sherman Act and the Clayton Act. Then we except those acts in the next section.

Mr. TAFT. Mr. President, will the Senator yield to me for a moment?

Mr. FERGUSON. I yield.

Mr. TAFT. I return to my original suggestion. I do not think the words "shall not apply to such business and the acts or the conduct thereof" are as broad as section 2. It is said there specifically that these acts shall not apply to the insurance business, but that does not necessarily mean that the States might not be deprived also of the power of taxing or regulating because the insurance business is interstate commerce. I do not quite see why, in view of what the Senator now wishes to accomplish, he cannot add to his amendment at the end of section 2 the words I suggested, that no act of Congress shall apply to such business and shall not invalidate, impair, or supersede the law of any State for the purpose of regulating the business of insurance. Then other acts are covered entirely and the Sherman and Clayton Acts are covered entirely in section 4 (a), and explained in detail.

Mr. ELLENDER. Such language put in the proper place would cover the objection I suggested to the pending amendment. However, I am not advocating it, because I think the bill as reported by the Judiciary Committee is clear. I think all of us agree that the States should retain the right of regulating and taxing the insurance business within their respective borders.

Mr. FERGUSON. Does the Senator from Ohio move that the bill be amended as he has suggested? I have no objection to it.

Mr. TAFT. I do not want to move any further amendment until there is some general agreement as to what we are trying to accomplish.

Mr. O'MAHONEY. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. O'MAHONEY. It is my opinion that the amendment which the Senator from Michigan has just offered has completely cleared up the situation, and that his comment in response to the Senator from Ohio is absolutely correct. The language in section 4, as the Senator from Michigan points out, says that these antitrust laws shall not apply to such business, which means the business of insurance. It would be perfectly impossible, it seems to me, under that language, for a court to say that the Sherman and Clayton laws, which Congress says during this period shall not apply to insurance, shall nevertheless apply to State laws affecting insurance. I think the Senator from Ohio is endeavoring to be oversecure in gaining the point which is covered, it seems to me, by the amendment offered by the Senator from Michigan. The two sections are now drawn into complete harmony, as I see it.

Mr. REVERCOMB. Mr. President, will the Senator yield?

Mr. FERGUSON. I yield.

Mr. REVERCOMB. We have discussed changing language which has been very carefully studied with respect to the legislation on this subject, and each time a change is made or suggested we look farther down in the bill and we see a conflict with the suggested change. The bill was discussed at length in the Committee on the Judiciary of the Senate. It was unanimously reported. It has as its purpose giving to the States the control of insurance and creating a moratorium, so called, with respect to the Sherman Act and the Clayton Act, to fix dates of 1947 and 1948, respectively, and then it provides that nothing contained in this measure shall render the Sherman Act inapplicable if any agreement or act of the State or an insurance company under a law of the State creates a boycott, coercion, or intimidation.

I wish to call the attention of the Senate to the fact that the bill is very complete. It was better worked out in committee than it can be here on the floor of the Senate, acting as we are now, almost as a committee. I hope the bill may be passed in the form in which it was reported from the committee after study, and without the shot-from-the-hip amendments which are being offered. I believe that a great mistake would be made if, after careful study of this proposed legislation and framing it in the language in which it was reported, these changes should be made. I hope that the suggested amendments may be rejected, and that the bill may be passed as it was reported to the Senate unanimously by the Committee on the Judiciary.

Mr. RADCLIFFE. Mr. President, if I correctly understand the amendment which has been offered, it provides that no act of Congress, with certain exceptions, shall apply to the business of insurance. Is not that equivalent to stating that the Sherman Act and the Clayton Act shall supersede any State laws?

Mr. FERGUSON. Except that in section 4 it is provided that those two acts shall not apply to insurance.

Mr. RADCLIFFE. First it is provided that they shall invalidate State laws. Then later it is said that there shall be a moratorium. That is not the most felicitous way of stating it. If it can be construed that section 4 clearly modifies section 2 (b), we are safe; but it seems to me that that is running a rather unnecessary risk, because subsection (b) of section 2 clearly states that those two acts shall invalidate State laws.

Mr. WHERRY. Mr. President, I should like to ask the distinguished Senator from Michigan a question. If what he says be true, why is it necessary to have an amendment to subsection (b) of section 2 at all? I think we could put both sections together and do exactly what is desired.

As a member of the Committee on the Judiciary, I am for the bill as it came from the committee. The reason I voted for it was that it would put the regulation of the insurance business in the hands of the States. That is the important thing in this bill. I believe that the amendments which have been suggested would be confusing and conflicting. In my judgment the bill would be better if it were left as it was reported from the committee than if we were to try to amend it on the floor of the Senate. I hope the amendments will be rejected.

The VICE PRESIDENT. The question is on agreeing to the amendment offered

by the Senator from Michigan [Mr. FERGUSON], which will be stated.

The LEGISLATIVE CLERK. In section 2, on page 2, line 4, after the word "Congress", it is proposed to insert the words "except the act of July 2, 1890, as amended, known as the Sherman Act, and/or the act of October 15, 1914, as amended, known as the Clayton Act."

Mr. O'MAHONEY. Mr. President, I urge the Senate to adopt the pending amendment. I do so for this reason: The Senator from Michigan and the Senator from Wyoming have given a great deal of time and attention to this measure. It is not a problem without difficulties. I am satisfied that the purpose of the Senator from Michigan and my purpose are identical. The purpose is to enable the States and the Congress to have time to adjust a very complicated business to a decision of the Supreme Court and to the antitrust laws. There is no purpose to issue an invitation from the United States Senate to the States to enact laws which would establish monopolies in this business.

The moratorium as proposed in the bill, and as now proposed by the Senator from Michigan in his amendment, covers the entire field, and does it in such a way that there can be no misunderstanding. We are extending to the States complete immunity for their State tax laws, and, as stated in section 4, we are granting a moratorium for the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress. I believe the issue is quite clear. The purpose would be attained by the language of the bill together with the amendment of the Senator from Michigan, and I hope the amendment will be adopted.

The VICE PRESIDENT. The question is on agreeing to the amendment offered by the Senator from Michigan [Mr. FERGUSON]. [Putting the question.] The Chair is in doubt.

Mr. WHERRY. I ask for a division, Mr. President.

On a division, the amendment was agreed to.

The VICE PRESIDENT. The bill is before the Senate and open to further amendment. If there be no further amendment to be proposed, the question is on the engrossment and third reading of the bill.

The bill (S. 340) was ordered to be engrossed for a third reading, read the third time, and passed, as follows:

Be it enacted, etc., That the Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

SEC. 2. (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No act of Congress, except the act of July 2, 1890, as amended, known as the Sherman Act, and/or the act of October 15, 1914, as amended, known as the Clayton Act, shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically so provides.

SEC. 3. Nothing contained in the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, or the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall apply to the business of insurance or to acts in the conduct of that business.

SEC. 4. (a) For the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress, until June 1, 1947, the act of July 2, 1890, as amended, known as the Sherman Act, shall not apply to the business of insurance, or to acts in the conduct of such business, and until January 1, 1948, the act of October 15, 1914, as amended, known as the Clayton Act, shall not apply to such business or to acts in the conduct thereof.

(b) Nothing contained in this section shall render the said Sherman Act inapplicable to any agreement or act of boycott, coercion, or intimidation.

SEC. 5. Nothing contained in this act shall be construed to affect in any manner the application to the business of insurance of the act of July 5, 1935, as amended, known as the National Labor Relations Act, or the act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938.

SEC. 6. As used in this act, the term "State" includes the several States, Alaska, Hawaii, Puerto Rico, and the District of Columbia.

SEC. 7. If any provision of this act, or the application of such provision to any person or circumstances, shall be held invalid, the remainder of the act, and the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected.

LEGISLATIVE PROGRAM

Mr. McFARLAND. Mr. President, on behalf of the senior Senator from Alabama [Mr. BANKHEAD], I give notice that when the Senate reconvenes next Monday the Senator from Alabama will move to take up Senate bill 338 to amend the Agricultural Adjustment Act of 1938.

Mr. HILL. Mr. President, let me say to my distinguished friend from Arizona that the senior Senator from Louisiana [Mr. OVERTON] gave notice earlier in the day that as soon as the Senate convenes on Monday it will be his purpose to move to take up the river and harbor bill. I do not think it will require very long to dispose of that bill, in view of the fact that all controversial matters have evidently been eliminated from the bill. After action on the river and harbor bill is completed, I know of no reason at this time why a motion should not be made to take up the bill referred to by the Senator from Arizona.

Mr. McFARLAND. Such a motion will be made.

EXECUTIVE SESSION

Mr. HILL. I move that the Senate proceed to the consideration of executive business.

The motion was agreed to; and the Senate proceeded to the consideration of executive business.

EXECUTIVE MESSAGES REFERRED

The VICE PRESIDENT laid before the Senate messages from the President of the United States submitting sundry nominations, which were referred to the appropriate committees.

(For nominations this day received, see the end of Senate proceedings.)

EXECUTIVE REPORTS OF COMMITTEES

The following favorable reports of nominations were submitted:

By Mr. WALSH, from the Committee on Naval Affairs:

H Struve Hensel, of the District of Columbia, to be Assistant Secretary of the Navy;

Vice Admiral Frederick J. Horne, United States Navy, to be an admiral in the Navy, for temporary service, to continue while serving as Vice Chief of Naval Operations;

Capt. Frank G. Fahrion, United States Navy, to be a rear admiral in the Navy, for temporary service, to rank from the 21st day of February 1943;

Capt. Marshall R. Greer, United States Navy, to be a rear admiral in the Navy, for temporary service, to rank from the 28th day of August 1943;

Capt. Peter E. Fischler, United States Navy, to be a rear admiral in the Navy, for temporary service, to rank from the 11th day of May 1943;

Commodore Thomas P. Jeter, United States Navy, to be a commodore in the Navy, for temporary service, to continue while serving as chief of staff to commander, Battleship Squadron 2, and until reporting for other permanent duty, to rank from the 20th day of October 1944; and

Sundry aviators of the Marine Corps Reserve, and citizens, to be second lieutenants in the Marine Corps.

By Mr. GEORGE (for Mr. McCARRAN), from the Committee on the Judiciary:

T. Hoyt Davis, of Georgia, to be United States district judge for the middle district of Georgia, vice Bascom S. Deaver, deceased.

By Mr. McKELLAR, from the Committee on Post Offices and Post Roads:

William M. Payne, to be postmaster at Natchitoches, La.

The VICE PRESIDENT. If there be no further reports of committees, the clerk will state the nominations on the Executive Calendar.

FOREIGN SERVICE

The legislative clerk read the nomination of Edwin C. Wilson to be Ambassador Extraordinary and Plenipotentiary of the United States of America to Turkey.

The VICE PRESIDENT. Without objection, the nomination is confirmed.

POSTMASTERS

The legislative clerk proceeded to read sundry nominations of postmasters.

Mr. McKELLAR. Mr. President, I ask unanimous consent that the nomination of Myrtus P. Spangenberg to be postmaster at Waymart, Pa., go over until the next session.

The VICE PRESIDENT. Is there objection? The Chair hears none, and it is so ordered.

Mr. McKELLAR. I ask unanimous consent that all other postmaster nominations on the calendar be confirmed en bloc.

The VICE PRESIDENT. Without objection, all other postmaster nominations are confirmed en bloc.

THE NAVY

The legislative clerk proceeded to read sundry nominations in the Navy.

Mr. HILL. I ask that the Navy nominations be confirmed en bloc.

The VICE PRESIDENT. Without objection, the Navy nominations are confirmed en bloc.

The SPEAKER. Is there objection to the request of the gentleman from Texas?

There was no objection.

Mr. SUMNERS of Texas. Mr. Speaker, comparatively recently a private citizen in Virginia has entered upon a course of conduct claiming he is contesting the seats of, I believe, 71 Members of the House of Representatives. A colleague of mine the other day asked me to make some examination and write him a letter. I made that examination and have written him the following letter:

FEBRUARY 12, 1945.

MY DEAR COLLEAGUE: Supplementing the statement made to you over the telephone this morning with reference to notice to appear and give testimony in proceeding by Moss A. Plunkett, of Roanoke, Va., representing himself as contesting your right to a seat in the House of Representatives, beg to advise that I have looked over a copy of the paper served upon you and other Members of the House of Representatives, including myself, and have also made some examination of chapter 7, title 2, of the United States Code, which deals with the subject of contested elections.

The House of Representatives, under the Constitution, of course, is sovereign and independent with reference to the determination of the election and the qualification of its own Members. No act of Congress could, in the slightest degree, affect the exclusiveness of power of the House of Representatives to determine with reference to those who are entitled to be a part of its membership.

Section 7 of title 2 referred to therefore is merely an act of comity on the part of the Congress for the purpose of aiding the House of Representatives to whatever degree the House of Representatives may see fit to avail itself thereof. But this alleged contestant, Moss A. Plunkett, does not even come within the provision of this title.

Section 226, the last section of chapter 7, title 2, referred to, contains these words as the first part of the first sentence:

"No contestee or contestant for a seat in the House of Representatives shall be paid exceeding $2,000 for expenses in election contests."

The contest contemplated by the Congress in which it sought to give aid by statute is a contest by a "contestant" and "contestee," "for a seat in the House of Representatives."

Even if this language were not incorporated in the statute, common sense and public necessity would preclude any notion that the Congress intended to put it within the power of any person so disposed to institute proceedings to oust many persons who happen to be Members of Congress, and require them to turn aside from the discharge of their public duties to appear and give testimony at the summons of such a person who had not even been a candidate for Congress and who could not therefore be a "contestant for a seat in the Congress."

It seems to me to be not only the right, but the duty, of the Members of the House against whom this proceeding has been attempted, not to turn aside from the discharge of their official duties to give attention in the slightest degree to that which the said Plunkett is attempting.

Sincerely yours,

HATTON W. SUMNERS.

Mr. McCORMACK. Mr. Speaker, will the gentleman yield?

Mr. SUMNERS of Texas. I yield to the gentleman from Massachusetts.

Mr. McCORMACK. Will the gentleman advise the House how, in his opinion, this unreasonable situation should be met?

Mr. SUMNERS of Texas. By paying no attention to it.

The SPEAKER. The time of the gentleman from Texas has expired.

Mr. RANKIN. Mr. Speaker, I ask unanimous consent to address the House for 1 minute.

The SPEAKER. Is there objection to the request of the gentleman from Mississippi?

There was no objection.

Mr. RANKIN. Mr. Speaker, following up what the Member from Texas [Mr. SUMNERS], the very able chairman of the Committee on the Judiciary, has said, I want to call attention to the fact these radicals who are attempting to harass Members of Congress about this matter have not a leg to stand on. They really are acting in contempt of the House, and in contempt of the Senate, because they have attempted to subpena Senators, as well as Members of the House.

This question has been thrashed out before. The fourteenth amendment to the Constitution provided that where certain people were denied the right to vote in any State, representation from such State should be proportionately reduced.

Mr. Blaine, in his Twenty Years in Congress, calls attention to the fact that it means when they are denied such rights by State laws or acts done under State authority.

But, as Mr. Blaine also points out, the fifteenth amendment states that no such law shall be passed, and as he says, that to all intents and purposes wiped out that section of the fourteenth amendment.

If there is anything wrong with the State law, the place to contest it is in the courts. If there is anything wrong with a Member's right to sit in this House, the place to contest it is before a committee of the House, by a resolution introduced in the House by the person who is directly affected.

So these attempts to harass the Members of the House and Senate are simply in contempt of both Houses, and as the chairman of the Judiciary Committee [Mr. SUMNERS] said, they should be ignored.

CONSIDERATION OF INSURANCE BILL

Mr. McCORMACK. Mr. Speaker, I ask unanimous consent to address the House for 1 minute.

The SPEAKER. Is there objection to the request of the gentleman from Massachusetts?

There was no objection.

Mr. McCORMACK. Mr. Speaker, this afternoon the Committee on the Judiciary will exercise its privileges under the Calendar Wednesday rule, and, as I understand, the insurance bill will be called up. I take this brief period to advise the Members of the House, and particularly the new Members, as to the situation.

If the bill called up is on the House Calendar, there will be 1 hour of debate on it. If it is on the Union Calendar, the bill will be considered in the Committee of the Whole House on the state of the Union and there will be 2 hours of general debate, the time being equally divided and controlled by the Member in charge on the majority side of the committee and by the ranking minority Member present of the committee.

However, the latter situation will not obtain in the consideration of the bill that will be called up later. That bill will be called up and be considered under the rules of the House, and the Member in charge of the bill can at the end of an hour move the previous question. If the previous question is ordered, of course, that eliminates any opportunity for amendments to be offered to the bill and eliminates the possibility of debate upon such amendments.

I simply call this to the attention of the Members so they will have the situation in mind. Of course, the time for debate will be under the control of the chairman of the Committee on the Judiciary or the member in charge. I see that the gentleman has risen, and I yield to him.

Mr. SUMNERS of Texas. May I suggest for the information of the House and for the information of the leader that if we have time this afternoon we have another bill, the reorganization bill, that we should like to have considered under this clause of the rules.

Mr. ANDERSON of New Mexico. Mr. Speaker, will the gentleman yield?

Mr. McCORMACK. I yield to the gentleman from New Mexico.

Mr. ANDERSON of New Mexico. The gentleman says that it will be impossible to offer amendments, but if the motion for the previous question is voted down it will be possible to offer amendments.

Mr. McCORMACK. My purpose is to advise the House as to the situation without expressing my own position. Of course, if the previous question is voted down, then the situation is entirely different. Then a Member who is recognized thereafter to offer an amendment will have the floor for 1 hour and will have control of the time during that period. Therefore, the gentleman's statement, as I understood him, is correct.

Mr. RANKIN. As I understand it, this is to be taken up under the Calendar Wednesday rule?

Mr. McCORMACK. Yes; under the Calendar Wednesday rule. But the bill being on the House Calendar and not on the Union Calendar, it will be considered under the regular rules of the House and not in the Committee of the Whole House on the state of the Union.

Mr. RANKIN. When it is disposed of, the next committee will be called, I presume, under the Calendar Wednesday rule?

Mr. McCORMACK. I assume that if the committee has another bill to call up, it would be in order. But I would not want to undertake to state just what will be called up.

Mr. RANKIN. What I am trying to get at is, you are not dispensing with Calendar Wednesday?

Mr. McCORMACK. No; we are not dispensing with Calendar Wednesday. It is quite probable that the Committee on

the Judiciary will answer the call and the first bill will be the insurance bill. I have risen at this time to advise the House of the unusual circumstances under which it will be brought up, and that the Member in charge will have control of the time and that at the end of an hour he can move the previous question, which will preclude the offering of amendments. In order for the offering of amendments to be in order, the previous question would have to be voted down.

CALENDAR WEDNESDAY

The SPEAKER. This is Calendar Wednesday. The Clerk will call the committees.

The Clerk called the committees, and when the Committee on the Judiciary was called:

REGULATION OF INSURANCE BUSINESS

Mr. WALTER. Mr. Speaker, by direction of the Committee on the Judiciary, I call up the bill (S. 340) to express the intent of Congress with reference to the regulation of the business of insurance, as amended.

The SPEAKER. The Clerk will report the bill and the amendment.

The Clerk read as follows:

Be it enacted, etc., That the Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

Sec. 2. (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No act of Congress, except the act of July 2, 1890, as amended, known as the Sherman Act, and/or the act of October 15, 1914, as amended, known as the Clayton Act, shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically so provides.

Sec. 3. Nothing contained in the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, or the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall apply to the business of insurance or to acts in the conduct of that business.

Sec. 4. (a) For the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress, until June 1, 1947, the act of July 2, 1890, as amended, known as the Sherman Act, shall not apply to the business of insurance, or to acts in the conduct of such business, and until January 1, 1948, the act of October 15, 1914, as amended, known as the Clayton Act, shall not apply to such business or to acts in the conduct thereof.

(b) Nothing contained in this section shall render the said Sherman Act inapplicable to any agreement or act of boycott, coercion, or intimidation.

Sec. 5. Nothing contained in this act shall be construed to affect in any manner the application to the business of insurance of the act of July 5, 1935, as amended, known as the National Labor Relations Act, or the act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938.

Sec. 6. As used in this act, the term "State" includes the several States, Alaska, Hawaii, Puerto Rico, and the District of Columbia.

Sec. 7. If any provision of this act, or the application of such provision to any person or circumstances, shall be held invalid, the remainder of the act, and the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected.

With the following committee amendment:

Strike out all after the enacting clause and insert:

"That the Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

"Sec. 2. (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

"(b) No act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically so provides.

"Sec. 3. Nothing contained in the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, or the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall apply to the business of insurance or to acts in the conduct of that business.

"Sec. 4. (a) Until January 1948, the act of July 2, 1890, as amended, known as the Sherman Act, and the act of October 15, 1914, as amended, known as the Clayton Act, shall not apply to the business of insurance or to acts in the conduct thereof.

"(b) Nothing contained in this section shall render the said Sherman Act inapplicable to any act of boycott, coercion, or intimidation.

"Sec. 5. Nothing contained in this act shall be construed to affect in any manner the application to the business of insurance of the act of July 5, 1935, as amended, known as the National Labor Relations Act, or the act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938 or the act of June 5, 1920, known as the Merchant Marine Act, 1920.

"Sec. 6. As used in this act, the term 'State' includes the several States, Alaska, Hawaii, Puerto Rico, and the District of Columbia.

"Sec. 7. If any provision of this act, or the application of such provision to any person or circumstances, shall be held invalid, the remainder of the act, and the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected."

The SPEAKER. The gentleman from Pennsylvania [Mr. WALTER] is recognized for 1 hour.

CALL OF THE HOUSE

Mr. HILL. Mr. Speaker, a point of order. I make the point of order that a quorum is not present.

The SPEAKER. Evidently a quorum is not present.

Mr. WALTER. I move a call of the House.

A call of the House was ordered.

The Clerk called the roll, and the following Members failed to answer to their names:

[Roll No. 17]

Anderson, Calif.	Brumbaugh	Combs
Biemiller	Cannon, Fla.	Courtney
Bolton	Clevenger	De Lacy
Boren	Colmer	Dondero
Eaton	Lyle	Shafer
Elston	McGregor	Sheridan
Fernandes	McMillan, S. C.	Short
Gardner	Madden	Sikes
Gwinn, N. Y.	Morgan	Taylor
Hare	Mott	Thomas, N. J.
Harless, Ariz.	O'Hara	Vorys, Ohio
Harness, Ind.	Plumley	Vursell
Havenner	Powers	Wasielewski
Hébert	Reece, Tenn.	West
Heidinger	Rees, Kans.	White
Henry	Rivers	Wilson
Izac	Robsion, Ky.	Winter
Johnson, Lyndon B.	Rooney	Woodrum, Va.
King	Rowan	
	Schwabe, Okla.	

The SPEAKER. On this roll call 375 Members have answered to their names. A quorum is present.

By unanimous consent, further proceedings under the call were dispensed with.

DOMESTIC RAISING OF FUR-BEARING ANIMALS

Mr. BLAND. Mr. Speaker, I ask unanimous consent that the Committee on the Merchant Marine and Fisheries be discharged from further consideration of the bill (H. R. 2115) relating to the domestic raising of fur-bearing animals, and that the same be rereferred to the Committee on Agriculture.

The SPEAKER. Is there objection to the request of the gentleman from Virginia?

There was no objection.

REGULATION OF INSURANCE BUSINESS

Mr. WALTER. Mr. Speaker, the measure under consideration represents a compromise. If you will recall at the last session of the Congress, by a vote of 283 to 54, the House, in most unmistakable terms, signified its belief that the law as it was understood to be up to June 5, 1944, should be reaffirmed.

When the Supreme Court handed down the unusual decision, written by a minority of that Court, in which 75 years of well-accepted, well-known law was changed, the insurance business of this country was confronted with a very serious situation. Both Justice Jackson and Justice Frankfurter, in well-considered minority views, pointed out the chaos that would come through the hurried action of the Court, and through a sudden change in the well-known theory with respect to insurance companies. Their predictions have come true. I say that because within the last month the attorney general of the State of North Carolina has held that the State can no longer collect the taxes paid by insurance companies doing business in the State of North Carolina because insurance is now interstate commerce and therefore the regulations imposed by the several States are not legal.

It is very significant, in considering this entire question, to bear in mind that when the rule of law was first laid down, upward of 75 years ago, in the case of Paul against Virginia, the case got to the Supreme Court of the United States by an insurance company resisting the right of the State of Virginia to impose any regulation on its business. Today we find ourselves in the position where the insurance companies are at a loss to know just exactly where they stand.

Since the law was first laid down, through a series of legislative enactments, through all sorts of regulatory

provisions, the business of insurance grew into one of the biggest businesses in our Nation. The companies, through their own experience, were able to regulate themselves in a manner that has been satisfactory to almost every one. When I spoke a moment ago of this compromise, I spoke advisedly. Personally I would prefer to see the bill, that we passed at the last session of the Congress so overwhelmingly, reenacted, but I recognize the practical side of this situation and I am entirely in accord with this compromise measure.

In that connection I would like to call your attention to the fact that after the impasse was reached in the Senate, at the suggesion of the chairman of the Committee on the Judiciary of the House of Representatives, and of several Senators, representatives of all phases of the insurance business, through a series of conferences held over a period of at least 3 months, agreed on this compromise measure. That is the compromise measure that was reported by the Committee on the Judiciary of the House, with the exception of the language contained in section 4 (a) of the Senate bill. This is the bill that was agreed on by the insurance commissioners of all of the States, the American Life Convention, the American Mutual Alliance, the Association of Casualty and Surety Executives, Inland Marine Underwriters' Association, National Association of Insurance Agents, National Association of Mutual Insurance Agents, National Board of Fire Underwriters' Insurance Executives Association, the National Association of Insurance Brokers, the National Association of Casualty and Insurance Agents, they being all of the people in the industry affected through the decision of the Supreme Court.

Mr. GRAHAM. Mr. Speaker, will the gentleman yield?

Mr. WALTER. I yield.

Mr. GRAHAM. Is it not a matter of record that since the passage of the bill referred to in the House, the Supreme Court has denied a petition for a rehearing of the Southeastern Underwriters' Association, which makes this action imperative?

Mr. WALTER. Yes; an application was made to the Supreme Court for a rehearing, and it is, indeed, unfortunate there was not a rehearing participated in by a majority of the Court. I think this decision by a vote of 4 to 3 was shocking, to say the least, because where a well-accepted rule of law is changed, as Justice Marshall put it a great many years ago, the change should come only when a majority of the Court participate in the decision. This is another reason why it is imperative that something be done immediately; but the most important practical phase of the whole situation is that taxes due and owing to the insurance departments of the several States are collected between the 20th of February and the 10th of March. It will be easy to compromise our views with the bill passed by the Senate; our views are contained in the bill recommended by the Committee on the Judiciary of the House.

Mr. CRAWFORD. Mr. Speaker, will the gentleman yield?

Mr. WALTER. I yield.

Mr. CRAWFORD. I have carefully and with a great deal of interest read the gentleman's bill and the committee report. I believe I am very much in favor of both. I wish, however, to submit this question: The gentleman read a list of those organizations that go to make up the insurance industry; is that group all agreed on the House bill as now presented to us as a substitute for the Senate bill?

Mr. WALTER. That is the group that agreed on the House bill with the exception that in the House bill the following language in section 4 (a) of the Senate bill was stricken out:

For the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress.

With the exception of the omission of that language the two bills are similar.

Mr. BRADLEY of Pennsylvania. Mr. Speaker, will the gentleman yield?

Mr. WALTER. I yield.

Mr. BRADLEY of Pennsylvania. I preface my question by saying that I ask it for the purpose of obtaining helpful information. Can the gentleman tell us what the attitude of the Department of Justice is with respect to this bill? I presume we are considering H. R. 1973.

Mr. WALTER. H. R. 1973 was the bill reported by the committee and subsequently made an amendment to S. 340. So the amendment of S. 340 is H. R. 1973.

As to the attitude of the Attorney General, frankly I do not know. He testified before our committee, and when various changes were suggested he agreed with the position we took. I am sure his testimony will bear out that statement. The other day when the bill was called up on the Consent Calendar the gentleman from New York [Mr. CELLER], I believe it was, made the statement that the Attorney General was opposed to the bill as reported by the House committee. I subsequently called the Attorney General and asked him what his objections were, and he told me he had not read the bill. This is as much as I know about his attitude; but I believe that is immaterial. I would say to my good friend from Pennsylvania that, after all, this is a compromise. The Committee on the Judiciary did what the President of the United States in a letter to a Senator from Maryland suggested be done, namely, that a moratorium be granted so these great companies could find out just exactly where they stood and what they have to do to meet the new thought, if you please.

Mr. COCHRAN. Mr. Speaker, will the gentleman yield?

Mr. WALTER. I yield.

Mr. COCHRAN. The President of the United States by no means recommended section 3 as in the bill passed by the Senate and also in the bill reported by the House.

Mr. WALTER. Why, of course, he did not; all he did was to write a letter in which he suggested a moratorium. I do not know of any other way to provide for a moratorium than as provided in this measure. We merely state that until January 1, 1948, the laws under which the insurance companies were prosecuted are not applicable except for certain things. It seems to me that there is the moratorium the Chief Executive suggested should be granted to these companies.

Mr. COCHRAN. The gentleman certainly does not want to stand on the floor of this House and tell the Members that he is in favor of insurance companies or insurance brokers putting out false advertising in connection with the conduct of their business.

Mr. WALTER. Well, if they do, it seems to me that is a matter that can be very easily reached. We are not concerned with things of that sort. This is merely a moratorium. That is all it is. It is to give these people a breathing spell so that they can decide how they may operate their business in the future. That is all this is; it is a moratorium.

Mr. COCHRAN. I agree with the gentleman that far, but when he says "we" I do not know for whom he speaks. I, as one Member, will not vote for the moratorium if you leave section 3 in the bill.

Mr. WALTER. I do not think the gentleman voted for the bill when it passed the House previously.

Mr. COCHRAN. I voted against the bill and I will not vote for this one, unless section 3 is eliminated.

Mr. CELLER. Mr. Speaker, will the gentleman yield?

Mr. WALTER. I yield to the gentleman from New York.

Mr. CELLER. In order to keep the record straight, I communicated with the Attorney General when the bill was on the Consent Calendar and he told me he was absolutely opposed to the bill as it is now written and as it is now before the House. I asked him why and he said he was opposed to it because there was stricken from the bill language which would proscribe and make unlawful not only acts to intimidate, boycott, and to coerce but also agreements to coerce and to boycott.

Mr. WALTER. That is not what the Attorney General said when he testified before the Committee on the Judiciary. But what his personal views are is immaterial to me. He did testify on this very subject before the Judiciary Committee of the House.

Mr. CELLER. I am simply giving the conversation.

Mr. WALTER. We pointed out to him the possible construction that could be placed on the word "agreement" that was put in the bill and he agreed with us. There is no question about that.

Mr. CELLER. I am only repeating what he told me.

Mr. WALTER. It bears out what I have stated.

Mr. CELLER. I am repeating his conversation with me over the telephone.

Mr. WALTER. Mr. Speaker, I reserve the balance of my time.

Mr. COCHRAN. Mr. Speaker, a point of order.

The SPEAKER. The gentleman will state his point of order.

Mr. COCHRAN. The gentleman from Pennsylvania yielded back the balance of his time.

The SPEAKER. The gentleman stated he reserved the balance of his time.

Mr. WALTER. Mr. Speaker, I yield 5 minutes to the gentleman from New York [Mr. HANCOCK].

Mr. HANCOCK. Mr. Speaker, the unfortunate decision of the Supreme Court in the Southeastern Underwriters case, decided last June, has thrown the insurance business into a state of utter confusion. That decision by four members out of nine members of the Supreme Court changed the established law of the land, it reversed the will of Congress and created a new policy regarding the control and regulation of the business of insurance. The decision has been rightly called judicial legislation.

A committee of the National Association of Insurance Commissioners, of which the Honorable Robert E. Dineen, of my State, is a member, drafted a bill several months ago that contains much of the language of the bill now before us but has a much stronger section 4 than the one in the present bill. You can find it and an interesting discussion of it in the 1944 annual report made by Mr. Dineen to the New York State Legislature. The attitude of the State commissioners is reflected by the declaration made by the committee to accompany its proposed legislation. I quote a portion of that statement:

> The National Association of Insurance Commissioners sincerely believes that the States can adequately regulate the insurance business, and because of legal considerations and the close proximity of State supervisory officials to the people affected, are in a better position to regulate that business than the Federal Government. In that regard it has regulatory machinery available, including regulatory statutes and trained personnel.

Heretofore the insurance business has been subject to regulation by the States because an unbroken line of decisions of the Supreme Court have held not only that insurance is not interstate commerce, but that it is not commerce at all. The decision makes insurance interstate commerce, and therefore subject to all the statutes we have enacted dealing with interstate commerce. There are four, I believe: The Federal Trade Commission Act, the Patman Antidiscrimination Act, the Clayton Act, and the Sherman Act.

Unfortunately, we cannot repeal the decision of the Supreme Court. What we can do, however, is to suspend the operation of the statutes we have passed, limit their scope, and grant exemptions or exceptions.

Under that decision insurance, if written by a company in more than one State, is, as matter of law, interstate commerce today and will be so until another Supreme Court comes along and reverses this decision. Therefore the taxes imposed on insurance companies in many States may be regarded as burdens on interstate commerce and, therefore, unlawful. As a result, many companies are refusing to pay their insurance taxes, that is, taxes on the insurance written within the several States. Others are paying taxes under protest, because they are threatened with stockholders' suits. The officials of an insurance company may not with impunity pay unlawful taxes. They are liable personally to their stockholders if they do so. Therefore it is imperative, if we are to preserve the rights of the States to tax the insurance companies on business written within their boundaries, that we pass an act authorizing them so to do. We have attempted to accomplish that purpose by sections 1 and 2 of the committee amendment to S. 340. I am not certain that we can do it but this bill goes as far as we can in an effort to maintain the rights of the States to tax the insurance business within their respective boundaries. A vast amount of State revenue is involved, and it is a matter of extreme importance to the States that action be taken to meet an immediate emergency.

There are only two main features in the bill. The second is to grant a moratorium on the application of the antimonopoly laws until January 1948. Personally, I would rather go much further than this bill goes. I was a strong supporter last year of the Walter bill, and I would support it today, plus this provision with reference to taxes. But we believe we cannot pass that bill as the Senate is now constituted, and we are told with some assurance that the President would veto it. So the best we can do now is to ask for a moratorium and leave the final decision open; not with instructions to the Congress or the various legislatures to pass laws to conform to the Supreme Court decision, and not with instructions either to the Congress to pass laws to exempt insurance permanently from all the antimonopoly laws. As we have written this bill, and brought it to you, we have left the question wide open.

There are quite conflicting views on this question among the commissioners of the various States, among the group of people who desire complete Federal control, and that other and larger group that believes in State control of the business of insurance. There are some slight differences between this bill and the bill as passed by the Senate, but they are not important in my view.

This bill is, in effect, what has been agreed upon by the insurance commissioners of all the States and by various insurance groups, the fire-insurance companies, the casualty companies, and the life-insurance companies and agents.

I hope this bill will receive practically unanimous support so that your conferees can go to the Senate with strong backing by this House.

Mr. WALTER. Mr. Speaker, I yield 5 minutes to the gentleman from New York [Mr. CELLER].

Mr. CELLER. Mr. Speaker, this bill is the result of a compromise, but it is well to keep in the background the tremendous power and potency of the various large insurance companies. We have to make a decision sooner or later as to whether or not we are going to be ruled by a cabal or a combination of these powerful companies or whether we are going to allow the small independent companies to function under competitive conditions in the various States.

The American Farm Bureau Federation, which is interested indirectly in quite a number of the small farm mutual companies, has expressed grave concern that even this compromise will force these small companies catering to the farmers to jack up their rates. Already, for example, the State of Montana, realizing that this compromise bill may go through, has passed a statute compelling every insurance company in the State of Montana to join a rating bureau and to apply to their policyholders uniform rates. This means in essence that in every State where large insurance companies exercise control, and they do exercise control in many of the States, there is no blinking that fact—I can give you any amount of evidence to prove it, but time will not permit at this juncture—these companies, through powerful lobbies, will cause enactment of bills forcing companies with lower rates to jack them up, so that in the State of Montana and other States these small companies are compelled to join the rating bureaus, are compelled to abide by uniform rates, and in many instances, under guise of uniformity, competition goes out the window. Low rates must be upped.

Therefore, during this period of moratorium you will have the larger insurance companies rushing into the various State legislatures asking for these uniform rates and compulsory joining of rating bureaus, to the very grave disadvantage of all of these small mutual companies catering to the farmers.

I am going to put into the RECORD a communication received from the American Farm Bureau Federation under date of February 3, 1945, in that regard. It follows at the end of my remarks.

Further, there has been left out of this bill that has come out of the Committee on the Judiciary a very important word. That word is "agreement." There is, properly, proscribed in the wording of the pending bill acts "of boycott, coercion, or intimidation." You will find that on page 4, lines 19 and 20 of the bill before you. The Senate version, however, had in addition to "any act of boycott, coercion, or intimidation" the word "agreement" to boycott, coerce, or intimidate.

What is the danger in leaving that word out? There is a great deal of danger. These great companies can issue a blacklist. It need not be in writing, there need not be a so-called overt act, it could be an oral blacklist, and they would frighten the wits out of all these small companies. In addition there could be an "agreement" for what is known as separation. Let me tell you something about the "separation." Under "separation," if an agent wrote insurance for an outside or marked or proscribed company, or a blacklisted company, he was immediately stripped of his privileges; that is to say, he was not permitted to write insurance for any of the members of the self-constituted governing organizations known as boards. If a member of any of the boards wrote business through that agent which represented independent or nonmember companies, such member company was subject to punishment and was compelled to give up the business.

That is why I want the word "agreement" put back into the bill. We have no opportunity to amend the bill and to

put it back. For that reason, I must perforce oppose the bill, and the Attorney General for that reason is opposed to this bill.

AMERICAN FARM BUREAU FEDERATION,
Washington, D. C., February 3, 1945.
Honorable CHAIRMAN,
Judiciary Subcommittee,
House of Representatives,
Washington, D. C.

MY DEAR CHAIRMAN: The American Farm Bureau Federation is a national nonprofit membership organization, representing approximately 850,000 farm families in 46 States. The organization is a federation of State organizations.

The American Farm Bureau Federation does not own, control, or operate any insurance company. The State organizations, however, have developed mutual insurance services for the individual farm-family membership within their several States. Seven of the State Farm Bureaus have organized and are operating mutual insurance services for Farm Bureau members and farm families in 30 or more States. Experience seems to justify the conclusion that farmers, as a class, in many lines of insurance have more favorable experience than the public generally, or of certain other groups. With few exceptions, the Farm Bureau companies have not operated on manual or bureau rates. Rates have been established that experience seems to justify, and even under such rates that are generally lower than manual or bureau rates permit the distribution of policy dividends. The American Farm Bureau Federation, therefore, and its member States for their farm families, is very much interested in any legislation, either Federal or State, that affects the operation of insurance companies operating on the principle of giving the insured the lowest possible rates consistent with safety.

Having been advised by our general counsel that S. 340, as amended by your subcommittee of the Judiciary Committee, is dangerous from the viewpoint of the many casualty and fire insurance companies affiliated with the Farm Bureau and other farm organizations, and against the interests of farmers and others insured by these and similar low-cost companies, we urge you to take steps to correct the situation.

As we understand it, the effect of the removal of the Senate amendment in lines 3, 4, and 5 of page 2 of the bill as it came to the House, is to give to insurance companies a permanent exemption from the Sherman Act and the Clayton Act (as to any acts authorized or permitted by a State law) despite the references in section 4 to a temporary and partial exemption, unless and until Congress at some later date passes legislation making these acts specifically applicable to insurance.

In view of the fact that bills are now being introduced in a number of State legislatures which would result in the fixing of compulsory uniform rates, tend toward monopoly, and prevent our members and others from securing insurance at lower costs, we believe that your committee and the Congress should make it clear that it is not the intent or purpose of S. 340 to encourage such price-fixing and monopoly-forming legislation, but on the contrary, Congress desires to exercise some measures of restraint over such developments.

As a first step in this direction, we strongly urge the restoration of the Senate amendment which would eliminate permanent exemption from the Sherman and Clayton Acts. This would serve as a strong deterrent to present undesirable trends in State legislation.

Even with the Senate amendment restored, the bill should be safeguarded further by adding at the end of section 4 (a) a proviso approximately as follows:

"*Provided, however,* That this exemption from the Sherman Act and the Clayton Act shall not apply to any new State legislation which would result in fixing compulsory uniform rates for all companies of a given class or other restrictions that would have the effect and result of requiring all companies of a given class to charge approximately the same rates or costs to the insured."

If the Senate amendment is not restored to section 2 (b) the above proviso should be attached to that section rather than to section 4 (a).

As the bill now stands with your subcommittee amendments, it is an open invitation for those insurance companies who do not like competitive rates to rush into the State legislatures to secure the enactment of laws which will give them all the rate-fixing and monopolistic privileges they have heretofore partially attained through collusive action which, until recently, was free from the restraints of the Sherman and Clayton Acts. Under your section 2 (b), the opportunity held out to such insurance companies or associations to secure the same or greater rate-fixing results and full immunity by the enactment of State laws is already resulting in tremendous pressure upon State legislatures.

Surely your committee and the Congress should do something to safeguard this situation. The amendment we suggest would give such a safeguard and still retain all necessary immunities from the Sherman and Clayton Acts.

We note with approval your committee's amendment eliminating the first clause in section 4; that is, the words "for the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress." This language has been cited in some States as evidence that Congress expects the States to enact legislation presented by certain insurance groups and which, if adopted, would have the effect of eliminating competitive rates.

But we feel that this mere elimination of language is not sufficient to correct wrong impressions already developed. In view of some of the language contained in previous committee reports on this and similar bills, we ask you to state explicitly in your committee report that it is not the intent or purpose of Congress to encourage price fixing through compulsory uniform rating bureaus or other monopolistic practices, and that any such tendencies in new State legislation might quickly result in the withdrawal by Congress of the immunities granted.

Respectfully yours,
EDW. A. O'NEAL,
President.

Mr. WALTER. Mr. Speaker, I yield 1 minute to the gentleman from Massachusetts [Mr. MCCORMACK].

Mr. McCORMACK. Mr. Speaker, the question raised by the gentleman from New York interests me. Subsection (b) of section 4 on page 4 reads as follows:

> Nothing contained in this section shall render the said Sherman Act inapplicable to any act of boycott, coercion, or intimidation.

It has been called to my attention that under that language an act of boycott, coercion, or intimidation will be illegal, but a combination, conspiracy, or compact to coerce, boycott, or intimidate will be free from legal consequences.

It has been suggested to me by the Attorney General that if the following language is used that would be corrected:

> to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

I would like to ask my friend in charge of the bill if this language is objectionable to him, and if not, when this bill goes to conference, if it does, if the gentleman would agree to accept that language?

Mr. WALTER. Of course, I would. I would like to point out to the gentleman that when there is the kind of agreement he speaks about then it becomes an act and then under the very language of the law it is a violation.

Mr. McCORMACK. I will not take issue with the gentleman on that, but will the gentleman accept that language?

Mr. WALTER. Yes.

Mr. Speaker, I yield 9 minutes to the gentleman from New Mexico.

Mr. ANDERSON of New Mexico. Mr. Speaker, let me say at the very outset that the colloquy just participated in by the gentleman from Massachusetts and the gentleman from Pennsylvania should remove a great many objections to this bill in the minds of the Members of the House. I am not completely satisfied with the bill, as will develop. But I do think it is a fine evidence of the desire to work something out that the gentleman has accepted that language suggested by the gentleman from Massachusetts.

Mr. BRADLEY of Pennsylvania. Mr. Speaker, will the gentleman yield?

Mr. ANDERSON of New Mexico. I yield.

Mr. BRADLEY of Pennsylvania. Perhaps he can give some additional information which I was going to seek from the distinguished majority leader who quoted the Attorney General. I would like to know if the language is accepted as stated by the gentleman from Massachusetts, whether he is or you are authorized to say then the bill would be acceptable to the Department of Justice.

Mr. ANDERSON of New Mexico. I can say that I have discussed that very language time after time with officials of the Department of Justice. I am convinced that language at least would be acceptable to the Department of Justice. Is that not correct?

Mr. McCORMACK. Mr. Speaker, let me say to my friend I was addressing myself to that particular part of the bill and no other, and apparently the gentleman from Pennsylvania [Mr. WALTER] has stated he will accept that language if the bill goes to conference.

Mr. ANDERSON of New Mexico. Mr. Speaker, I would like to proceed with what I have to say.

Mr. BRADLEY of Pennsylvania. I want to vote for this bill if it is a compromise agreement between all parties concerned. But I am in a quandary because the Antitrust Division of the Department of Justice informed me just 10 minutes ago they were irrevocably opposed to the bill.

Mr. ANDERSON of New Mexico. They are; and that is exactly what I want to discuss, if the gentleman will permit me to do so.

I desire to call to the attention of the Members House Report No. 68, which is the report of the Committee on the Judiciary upon this bill and which in its conclusion states that this bill has been endorsed by a great number of organizations, including the National Association

of Insurance Commissioners, the American Life Convention, and so forth.

I want to challenge the statement and say to you that if what the Committee on the Judiciary wanted was something that had been endorsed by these groups, then it should have reported to the House the bill H. R. 1590, of which the gentleman from Pennsylvania [Mr. WALTER], is also the author. I would say to him in the words of St. Paul, "That which you have worshipped without knowing come I to declare unto you," because this is this bill, H. R. 1590, and not the other that the insurance commissioners have approved. It was H. R. 1590 that has been submitted as a compromise bill and not the other. I think it too bad that the statement has been made here that it has been endorsed by these groups, because it has not been so endorsed. I will tell you why it has not been endorsed. The American Life Convention, the American Mutual Alliance, the Association of Casualty and Surety Executives, and all these other groups referred to, issued a press release which I have in my hand and which everyone is at liberty to examine. That press release clearly points out why the language that the Committee on the Judiciary has stricken out is in this bill. That press release says:

For the purpose of enabling the business to make necessary adjustments in organization and operating methods, and in order that the legislatures of the various States may have time in which to adopt laws designed to authorize concert of action in rate making and other cooperative activities when approved by State supervisory officials, section 4 of the compromise bill granting a moratorium on the Sherman law to June 1, 1947—

And so forth. That is the basis of the moratorium. That is the basis upon which the letter was sent to Senator RADCLIFFE by the President of the United States. I told the House of Representatives when I opposed the Bailey-Walter bill that you were just marching your army up the hill to march it down again, because there was not any chance of its final enactment. Months later we find out that that is true.

I tell this House if you adopt the bill, H. R. 1973, you have again marched up the hill and got precisely nowhere because you must put into that compromise the things that the contracting parties have agreed to. They have all agreed that that language which recites the reasons for the moratorium should be in the bill; that it belongs in the bill, and that it must not be taken out of the bill. I say to you that 41 out of the 44 State insurance commissioners who were present at the meeting approved the bill with that language in it. If you doubt it, here is a report from the Superintendent of Insurance of the State of New York. I hold it in my hand. You may look at it at page 9 if you wish. Here is a report of the Chamber of Commerce of the State of New York and similar reports by other organizations recommending S. 340 as it was, which included the compromise language.

They have endorsed a bill that states the reason for a moratorium. If somebody wants to look at it, it is here.

Mr. WALTER. Will the gentleman yield?

Mr. ANDERSON of New Mexico. I yield.

Mr. WALTER. The fact of the matter is that the bill (S. 340), as these parties have agreed upon, is not the bill passed by the Senate at all.

Mr. ANDERSON of New Mexico. Exactly. The gentleman is correct. S. 340 was not the bill agreed upon in the industry compromise. That is entirely correct. If this House will vote down the previous question I would like to offer the bill earlier presented by the gentleman from Pennsylvania [Mr. WALTER], H. R. 1590, which is the bill agreed to by everybody, which the insurance commissioners have approved, and which the Department of Justice has approved. On the basis of that, the Attorney General went to the President of the United States with this bill, and on the basis of an examination of this bill a letter was sent to Senator RADCLIFFE, indicating that moratorium legislation would be approved. Why gum up the works at this late date?

Mr. CASE of South Dakota. Will the gentleman yield?

Mr. ANDERSON of New Mexico. I yield.

Mr. CASE of South Dakota. Even though the language of the committee substitute does not specifically direct the State legislatures or encourage them, does it not by the moratorium create the opportunity for the State legislatures to take action?

Mr. ANDERSON of New Mexico. I agree with the gentleman, but the point is that the commissioners themselves desire that it be stated in the bill that the moratorium shall be for specific purposes. The insurance companies realize that they are now in a serious position. The verdict of the Supreme Court of the United States is the law of the land, whether you like it or not. These people who are subject to the decision are in a terrible spot if something does not happen. So they went to the Attorney General and said, "Give us time and we will put our house in order." Consequently into the bill was written words designed to permit them time to make the adjustments. Then the insurance commissioners came in and said, "We are not ready with our rate-making structures. We have to ask the State legislatures to pass new laws." Therefore, into the bill went words to permit the States time to enact legislation. That is why H. R. 1590 carries the statements of the purposes in the moratorium. They are the words in the language of the bill as drafted by every interested party. No one can contradict that. The press release issued January 15, by the National Association of Insurance Commissioners is here for your inspection. There is no need to be misled by the committee report that says this has been approved by organizations that did not approve it.

Mr. PATMAN. Mr. Speaker, will the gentleman yield?

Mr. ANDERSON of New Mexico. I yield.

Mr. PATMAN. Is the gentleman also opposed to section 3 of this bill?

Mr. ANDERSON of New Mexico. I think it would be a fine thing if legislation relating to the Federal Trade Commission Act, now included in section 3, could be stricken from the bill, but I would not oppose the passage of H. R. 1590 with that language in it, because we could thereafter proceed to pass other necessary legislation to take it out. I would like to carry out the terms of the agreement exactly as originally agreed upon. Then I know there is some chance of final enactment of our bill. Every State in the Union is up against a serious problem, and you do not serve your constituents if you unnecessarily bog this down by passing a bill that nobody wants and that neither the industry nor the Commissioners have approved.

Mr. PATMAN. Is it not a fact that section 3 is permanent law—not just a moratorium? It goes away beyond any agreement.

Mr. ANDERSON of New Mexico. I will not argue with the gentleman because I am not a lawyer, but I know it is too bad if we do not vote down the previous question and substitute the bill which everybody has agreed upon.

Mr. FOLGER. Mr. Speaker, will the gentleman yield?

Mr. ANDERSON of New Mexico. I yield.

Mr. FOLGER. As I understand the gentleman his request is that we vote down the previous question in order that he may offer the agreement as made?

Mr. ANDERSON of New Mexico. That is right. I would then offer H. R. 1590. I would like also to point out, as the gentleman from Pennsylvania [Mr. WALTER] pointed out, that S. 340 did not conform to that agreement either. I think the House has a right to pass something that exactly conforms to the agreement.

Mr. COCHRAN. Will the gentleman yield?

Mr. ANDERSON of New Mexico. I yield.

Mr. COCHRAN. Why cannot the gentleman take out the section that relates to the Federal Trade Commission and the Robinson-Patman Act?

Mr. ANDERSON of New Mexico. I have tried to explain it. I want to see a bill passed that can be enacted into law prior to the closing days of February, at which time the insurance companies must pay their taxes to maintain the insurance departments in the various States. There is a specific date involved. Personally I would like to see it out, but I want to see a bill passed today.

The SPEAKER. The time of the gentleman from New Mexico has expired.

Mr. WALTER. Mr. Speaker, I yield 10 minutes to the gentleman from Iowa [Mr. GWYNNE].

Mr. GWYNNE of Iowa. Mr. Speaker, when the Supreme Court last year decided the Southeastern Underwriters case it immediately made applicable to the business of insurance many laws that we have heretofore passed regulating interstate commerce. When we passed those acts, Congress did not have in mind insurance; as a matter of fact when Congress passed the Sherman Act it was with

the distinct understanding that it did not apply to insurance, because insurance at that time was not interstate commerce, under Supreme Court decisions. The net result of the Supreme Court decision therefore was to put the Federal Government in the field of control then being exercised by the States. The methods of control exercised by the States and by the Federal Government are conflicting, and the sole purpose of this bill is to take out as much of that conflict as possible until we can determine whether Congress will regulate insurance, or whether it will permit the States to regulate it.

I believe there is no substantial difference, no difference of consequence, between the bill passed by the Senate and the bill we now have before us. I intend to take up the amendments that have been discussed here a little later. Before I do that let me say a word about H. R. 1973. It starts out with the statement that insurance shall be subject to State control. The Congress, of course, cannot delegate to the States the power to regulate insurance. What we are trying to do is to make it clear to the States and to the insurance companies that we are as far as possible removing ourselves from the field.

The second thing the bill states is that no act of Congress governing interstate commerce shall apply to insurance unless the act specifically so states.

The third section goes on to enumerate two acts. I believe section 3 is not necessary in the bill, but it was inserted, I suppose, to make it clear that the Federal Trade Commission Act should not apply to insurance and that the Robinson-Patman Act should not apply to insurance. The reason is this: The Robinson-Patman Act was passed with the intent that it should regulate and control the sale of commodities. It was not meant to cover insurance any more than it was meant to cover the banking business. If the Members wish a bill of the character of the Robinson-Patman Act to cover insurance, then I submit a special bill should be introduced which should cover it more equitably and more accurately than the Robinson-Patman Act, which was not written with insurance in mind.

The bill before us states in another section that it will not affect the coverage of the Wagner Act and the Wages and Hours Act so far as insurance is concerned. The Court has already held in the Polish Alliance case, you remember, that the Wagner Act did apply to insurance because insurance was something that affected interstate commerce.

The important part of the bill is that section which provides for a moratorium as far as the application of the Sherman and Clayton Acts are concerned. Part of the Sherman Act is in effect right now; in fact, that part having to do with boycotts, coercion, and intimidation. The rest of the Sherman Act and the Clayton Act will not take effect until January 1, 1948.

I wish now to say a word or two touching some things that were in the Senate bill that have been taken out. If you will turn to the bill, you will notice that the provision dealing with boycotts, and so forth, is made to apply to an act, not to an agreement, as the Senate bill had provided. The House took out the word "agreement" because we believed that to do so brought the law into line with our general notion of criminal law. For instance, if you and I agree to kill someone we will be punished by the courts. I have read in the Bible that he who thinks evil is as guilty as he who commits it, or words to that effect.

In the courts no prosecution could be had until some act had been committed in pursuance of that unlawful agreement. However, the use of the word "agreement" would open up to the prosecuting agencies of this Government an opportunity to constantly investigate agreements between insurance companies. I think that is the purpose in trying to get the word in there. In my judgment, it would have no effect whatever, so far as the legitimate prosecution for boycotting, coercion, and intimidations are concerned.

Another sentence we took out, and to which the gentleman from New Mexico has referred, is found in section 4—"for the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress," and so forth.

Whether that is in or out makes not the slightest difference to the bill. What the bill does is to grant a moratorium. It provides that until January 1, 1948, there will be no prosecutions under the Sherman Act except as indicated above. During this period of time a State may revamp its laws, and the Congress may revamp the laws. Why you should make so much fuss about a pious expression in a bill that means nothing is more than I can understand.

Mr. JENKINS. Mr. Speaker, will the gentleman yield?

Mr. GWYNNE of Iowa. I yield to the gentleman from Ohio.

Mr. JENKINS. As I understand the bill we are considering amounts to a moratorium until 1948?

Mr. GWYNNE of Iowa. That is correct, except as to acts of boycott, coercion, and intimidation.

Mr. JENKINS. Will the amendments which the gentleman from New Mexico proposes to offer change it? In other words, I would like to vote for a bill that would circumvent the decision of the Supreme Court entirely.

Mr. GWYNNE of Iowa. You cannot do that.

Mr. JENKINS. That is not politically wise or it may not be parliamentarily wise. But does the gentleman's amendment go further than this bill?

Mr. GWYNNE of Iowa. The amendment the gentleman talks about does not make one bit of difference.

Mr. AUGUST H. ANDRESEN. Mr. Speaker, will the gentleman yield?

Mr. GWYNNE of Iowa. I yield to the gentleman from Minnesota.

Mr. AUGUST H. ANDRESEN. What is there to stop the Attorney General from disregarding the provisions of this bill and going ahead, getting a grand jury and going after the insurance companies?

Mr. GWYNNE of Iowa. This is what we do in substance: We repeal, so to speak, or at least we suspend the operation of the Sherman and Clayton Acts until 1948 except as to acts of boycott by insurance companies.

Mr. JENNINGS. Will the gentleman yield?

Mr. GWYNNE of Iowa. I yield to the gentleman from Tennessee.

Mr. JENNINGS. I am inclined to agree with the gentleman. He referred to this proposed amendment as a pious gesture.

Mr. GWYNNE of Iowa. That is right.

Mr. JENNINGS. In this day of promulgation of administrative law, in this day of judicial decisions which worm in and worm out and leave everybody in doubt as to whether the snake that made the crack was going in or backing out, it is a pretty good idea to keep things on the surface mighty clear, is that right?

Mr. GWYNNE of Iowa. That is right.

Mr. ANDERSON of New Mexico. Mr. Speaker, will the gentleman yield?

Mr. GWYNNE of Iowa. I yield to the gentleman from New Mexico.

Mr. ANDERSON of New Mexico. If these words do not mean anything or make 5 cents difference, why is the gentleman afraid of them?

Mr. GWYNNE of Iowa. I cannot see any reason for putting in a bill the reasons why we are writing the bill, and that is all that amounts to. We give them a moratorium. Why should we undertake to tell the States anything beyond that fact? If they want to revamp their laws during the period of moratorium, that is up to them. Why should we express the hope that they will write other laws to conform with the notions of some Members of Congress?

Mr. ANDERSON of New Mexico. The gentleman understands the Attorney General has the duty to prosecute these people; but he says, "I shall not do it, provided you get your house in order."

Mr. GWYNNE of Iowa. The Attorney General has no business advising the States what kind of laws they should enact; neither do we.

Mr. CRAWFORD. Mr. Speaker, will the gentleman yield?

Mr. GWYNNE of Iowa. I yield to the gentleman from Michigan.

Mr. CRAWFORD. Has any testimony been submitted as to the amount of taxes involved running to the States and Territories?

Mr. GWYNNE of Iowa. This bill will not entirely clear that up, but the amount in my State is about $3,000,000. The total amount in the country for 1 year is about $120,000,000.

Mr. CRAWFORD. That, of course, is a tremendous sum as related to the budgets and the treasuries of these particular units of government.

Mr. GWYNNE of Iowa. That is true. There are two limitations as far as the States are concerned when they tax insurance companies. One is the Constitution. I am afraid some of the taxing policies of some of the States will have to be revamped, because they are probably unreasonably impeding interstate commerce. We cannot do anything about that, of course. The other limitation of the right of the States to tax in-

surance companies would arise if Congress itself would move into the field. In this bill we are making it clear that we do not move into the field.

Mr. WALTER. Mr. Speaker, I yield 1 minute to the gentleman from Michigan [Mr. MICHENER].

Mr. MICHENER. Mr. Speaker, I think we all appreciate that this legislation is desirable in some form. There is a difference of opinion as to just the particular form. The House passed a bill last year in the form that suited the House. The Senate passed a compromise bill which, with certain committee amendments, is now before us.

It seems to me that the sensible thing to do is to pass this bill expeditiously and send it to conference. There the differences may be worked out. If they are not worked out, the bill will be sent back to the House for another vote on the conference report, which is the final passage. If the House does not want to accept what the conferees have agreed upon, then it can vote against the report, which will be a vote against the bill.

Mr. WALTER. Mr. Speaker, I yield 5 minutes to the gentleman from West Virginia [Mr. BAILEY].

Mr. BAILEY. Mr. Speaker, George Washington once said:

> In proportion as the structure of government gives force to public opinion, it is essential that public should be enlightened.

A casual glance at Senate Resolution 340—the McCarran bill—which is before the House for concurrence, well illustrates Washington's idea that the people should know the facts. This is particularly so since the legislation proposed affects many millions of our citizens and in its present form is decidedly dangerous to a large group of citizens—particularly the little businessman.

Instead of this legislation being sent, as it was, to the Senate and House Committees on the Judiciary, it could better still have gone to the special committee set up by this House to study the problems of the small businessman. This proposal, if approved, will add a burden to those least able to carry it. It grants favor to the very group that has grown rich and strong at the expense of the weak and the defenseless. It presents the picture of the big bully convicted of kicking the little fellow around, who then comes to Congress and asks the privilege of going on kicking the little fellow for another year or two until Uncle Sam can do something about it.

It is beyond doubt the most selfish and most vicious piece of proposed legislation that has been brought to the floor of this House in the past decade. It is a surprise to me that the backers of this class of legislation are not contending that this is necessary to win the war.

For the past 75 years it has been the practice of this very group—the stock fire-insurance companies—now begging for special favors, to resist the efforts of the several States to regulate insurance. Their stock argument being that they were above and beyond the State's power to regulate. In other words, they were engaged in interstate commerce. Now, that the Supreme Court of the United States has held that the business of insurance does come under the commerce clause of our Constitution, they plead with Congress to approve legislation that will excuse them and exempt them from the provisions of the Sherman Antitrust Act, the Clayton Act, and in fact any other act that in any way interferes with their doing business at the same old stand and in the same old way.

The peremptory and summary manner in which the legislation was rushed through the Senate and House committees without the formality of public hearings finds its equal only in the act of a dictatorship for which the world is paying so dearly today—in tears and sweat and blood.

The proponents of this legislation take far too much for granted. Because the insurance officials of a few States, whose political policy is controlled and directed by the ramifications of these huge insurance combines, approve the McCarran bill, they would have the Members of Congress believe that a satisfactory agreement has been reached and that this bill has been sugar-coated so it pleases everybody. I doubt seriously if any of the "sugar" got into the bill. I shall later show how and why it will be "sour grapes" to the little businessman in the cities, villages, and at the crossroads who cannot pay his Federal, State, and local taxes, and at the same time pay tribute to these insurance barons.

They even imply in their press releases that Attorney General Biddle, who so stoutly opposed the passage of this legislation in the Seventy-eighth Congress, is satisfied—now that he can look through the dim mists of the future to a time when he will be permitted to enforce the law, provided the Eightieth Congress does not spread this immunity over another twilight zone, and provided further that the Attorney General does not get the double-cross on this legislation.

It is a significant fact that the gentleman from Indiana, Representative LAFOLLETTE, who waged such a gallant but losing fight against a similar bill in the last Congress, is absent from the Capital on official business, at a time when this crime against the millions of insurance policyholders is being perpetrated. It is further significant that he was also chairman of the Judiciary Subcommittee handling this legislation and refused to permit my appearance in an effort to amend this bill.

The gravity of the situation forces me to cast aside my determination to sit silently through the first session of the Seventy-ninth Congress—as all good freshmen are expected to do. I cannot help but protest and plead that this House ponder well the evils that are sure to result. I know not why others, who once fought this legislation, are now crying compromises or are permitting their names to be used as being party to a compromise. For me there can be no compromise—so long as there is discrimination.

It is dangerous legislation in that it sets a bad precedent. If this grant of immunity is voted, the insurance industry, what is to prevent—let us say Kuhn, Loeb & Co., one of the Nation's largest investment brokers—from demanding similar exemption from the provisions of the Securities Exchange Act? What, may I inquire, is to prevent even the Standard Oil Co. from resuming its monopolistic practices—through Congressional fiat.

It is unfair to legalize the practice of rate discrimination. Especially is that true when the violations are so flagrant, and the States are left powerless to protect themselves.

For better than 8 years, as assistant State auditor of my home State of West Virginia, it was my duty to assist in administration of the insurance laws. In West Virginia the State auditor is ex officio State insurance commissioner. I believe the Members of this House will readily agree that a man of even average intelligence could learn something about the intricacies of even so complicated a matter as the insurance business.

In West Virginia, and I am sure similar conditions exist in many other States, statistics indicate 40 percent of all insurance written is written outside the authority of the State insurance commissioner and without even the knowledge—at that time—that such insurance is being written. Here is the story of how it is done:

In the New York metropolitan area and in the adjoining State of Connecticut a group of old-line stock fire-insurance companies conspire—and I use this word advisedly—to set up a dummy or better still a "pup" insurance company. This dummy outfit has no assets beyond some gilded policy forms and the glittering diamond studs in the shirtfront of regular company officials "sitting in" at their board meeting. This dummy company is not licensed to do business in West Virginia or any other State, with the possible exception of New York. It has no assets that would qualify it to do business in my State.

Soon after the dummy is ready for business, its offices are visited by concerns having property in all sections of our country. They apply for and get a blanket policy covering their property in many and often all the States. They are given this blanket policy and within the matter of hours or days at the most, this dummy policy is underwritten or reinsured by one or more of the old-line companies back of the dummy set-up.

The rate per $100 of insurance paid under this blanket policy is as low in some instances as 10 cents. One such company—and there are scores of them—owns property in my State of West Virginia. They own a building on the main street of our capital city of Charleston. The building adjoining is occupied by a small businessman. The rate on his property is determined by a rating bureau in the adjoining State of Ohio and he pays a rate of $1.57 on the $100 and this is not the worst of it. If one of the properties covered by one of these blanket policies should burn, as they often do, then the full 100 percent of loss is charged against West Virginia's loss experience for rate-making purposes which in turn boosts the rate on the independent businessman. There, once again, the discrimination is in favor of the stock-insurance company.

West Virginia has a 2-percent tax on each $100 of premium paid on all fire-insurance policies. In this instance, the tax is on the 10-cent rate of premiums and not on the $1.57 rate. Since our State collects an annual tax of $1,000,000 from 60 percent of the insurance business it stands to lose $500,000 annually in taxes, by reason of this discrimination in rates.

There is a third major reason why this legislation is objectionable. It creates a "no man's land" zone in which irresponsible, fly-by-night concerns, not able to qualify in any State, continue to ply their trade of selling policies through the mails, by newspaper advertising and over the radio. It is estimated that millions of dollars have and are being invested in this worthless form of insurance. These practices are beyond State regulations and are just one more proof that a sizable part of the insurance, if regulated at all, must come under the commerce clause of our Constitution as was recently affirmed by our Supreme Court.

It is perfectly clear and obvious that the intent of the Judiciary Committees of both House and Senate were not to grant a moratorium so much as their intent seems to be to escape responsibility and defer a troublesome question to some later session of Congress.

If the moratorium were proposed to expire September 1, 1945, it would be easy to understand that the moratorium provisions of the bill were the full intent and purpose of Congress. The legislatures of 40 States are in session today and will be in session for at least another 30 days. Do the Members of Congress think that the several States are so dumb that they are unable to solve their own particular difficulties without the help of the insurance company lobby? In the meantime, a congressional grant of monopoly and price fixing, and all of the other insidious practices that have been prevalent in the insurance business for many years is being imposed upon the people of this Nation. The State of West Virginia is capable of managing and handling its own affairs without the assistance of the supergovernment or lobby of the insurance industry, but if this bill becomes law, the companies' lobby will come into our legislature and probably successfully defeat any corrective legislation that may be introduced in our legislature.

I am impressed with the idea that the Members of Congress have been led astray by the insurance lobby and have gone far afield by proposing to grant a monopoly by specific act for a period of 2½ years with respect to the Sherman Act and a period of 3 years with respect to the Clayton Act. It is worthless to the people of the United States and is of no particular value to the various States' insurance departments, and only tends to confuse the situation in the 40 State legislatures which are now in session to the point where it will be impossible for any corrective legislation to be adopted by the several State legislatures.

I am not opposed to the idea of granting a brief immunity to the stock fire-insurance companies. I understand it is necessary to revamp their present method of procedure to prepare for eventual Federal regulation. Two simple amendments which I shall offer (a) to remove discrimination in rates, (b) to effectively control and safeguard our citizens against fake and worthless insurance, would make this proposed legislation entirely satisfactory.

Unable to get a public hearing before either of the committees handling this legislation, I have no other recourse than to oppose its passage. If it cannot be amended, then my urgent plea to the Members of this House is that it be defeated. I trust it will be your pleasure to do so.

Mr. WALTER. Mr. Speaker, I yield 3 minutes to the gentleman from Indiana [Mr. SPRINGER].

Mr. SPRINGER. Mr. Speaker, the gentleman who just preceded me referred with vehemence to the measure now before us as class legislation, but that has no application to this measure. The bill now under consideration is an effort to try to protect the States, and the insurance business in the several States, following the decision in the case of the United States against the Southeastern Underwriters Association.

Mr. BAILEY. If the gentleman will yield, I may say that it was my desire to bring out the fact that I want to amend the present bill. I will approve the present bill if it can be amended. However, I did not have time to bring that out.

Mr. SPRINGER. This bill provides a moratorium. That is the important feature contained in this bill. Everyone knows that great consternation developed following the decision in the case of the United States against Southeastern Underwriters Association, et al. The States did not know what to do following that decision, and the insurance companies certainly did not know what to do. The question of taxation was involved, and the question of the control and regulation of insurance companies by the several States was also involved. At the present moment, unless this measure, or similar legislation, is passed to protect the States and protect the insurance companies with regard to their control and the question of taxation, utter confusion will result and utter chaos will reign in the several States.

My thought has been, as has been stated on the floor of the House by others, that I would far prefer to take the question of insurance entirely out of the commerce clause of the Constitution and entirely away from any Government control. But this emergency is immediate and it is necessary to pass this legislation now. The States do not know what to do with respect to the collection of taxes and the insurance companies do not know what to do with respect to the payment of taxes. The several States have no charted course with respect to the control or the regulation of insurance companies, since the case above cited, has been decided. Confusion and chaos has been brought about by that very peculiar decision.

Mr. Speaker, since this measure has been pending many insurance companies, and many State state officers, have written to me respecting that resulting confusion. It is essential that this measure be passed promptly in order to avoid confusion in the future.

This measure seeks only to establish a moratorium until January 1948 in order that the several States may continue their control and regulations over the insurance business and to proceed with the collection of taxes, in the manner and form intended by Congress. At the end of that period I hope—and I am confident a majority of the Members also hope—that this matter may be worked out in a proper manner—preserving to the several States their rights to control and regulate the insurance business within such States, and to collect the taxes now permitted—all without Government interference. I intend to support the measure.

The SPEAKER. The time of the gentleman from Indiana has expired.

Mr. WALTER. Mr. Speaker, I yield to the gentleman from New York [Mr. HANCOCK].

Mr. HANCOCK. Mr. Speaker, I ask unanimous consent to revise and extend my remarks in the RECORD and include some quotations.

The SPEAKER. Is there objection to the request of the gentleman from New York?

There was no objection.

Mr. WALTER. Mr. Speaker, I yield to the gentleman from Tennessee [Mr. KEFAUVER] such time as he may desire.

Mr. KEFAUVER. Mr. Speaker, there are a good many provisions of the bill as reported by the House which I do not like and which I thought should have been changed before the bill was brought before the House for consideration. For instance, I doubt the wisdom of section 3. I doubt if the Members of Congress should, without giving the question fuller consideration, permanently exempt insurance from the provisions of the Federal Trade Commission Act and the Robinson-Patman Act. It seems to me it would have been much better to have included these acts under section 4 and thereby declare a moratorium on their operation for 2 years and in the meantime we would have an opportunity of going into the situation more fully to determine just what final courses should be taken. Also, section 4-b should be amended so as to include any "agreement to boycott, coerce, or intimidate." In the committee I offered an amendment to this effect but it was voted down. The chairman of the subcommittee the gentleman from Pennsylvania [Mr. WALTER] has indicated that in conference he will accept this amendment to section 4-b. Also, in conference, I greatly hope that the provisions of section 3 may be included in section 4-a as I do not think at this time we have enough information to justify the permanent exclusion of these two acts insofar as they relate to the business of insurance.

This is, of course, emergency legislation. It is necessary that some legislation be passed to meet the necessities of the immediate situation. I hope that in conference the bill may be amended in the manner I have above suggested. If it were amended in this way, I think the bill would pretty closely follow the plan of the agreement which was reached by all parties concerned.

Mr. WALTER. Mr. Speaker, I yield the balance of the time to the gentleman from Texas [Mr. SUMNERS].

Mr. SUMNERS of Texas. Mr. Speaker, in the time allotted to me I hope I may be able to state the facts with reference to the insurance situation in such a manner as to be helpful to the Members in making up their minds. Prior to the decision of the Supreme Court, which has been referred to, the business of insurance was in the control of the States. The decision of the Supreme Court establishing the interstate commerce characteristics in insurance disestablished State control in large measure, established Federal power, and put the whole thing in a state of chaos, as has been discussed by Members who have preceded me. I am one of those who regret this shift of governmental responsibility. I know it is not an easy job. A good many people in this country, however, feel the time is at hand when the States should have some hard, tough meat to chew on if they are to retain their governmental teeth. The fact that there are difficulties in the State handling of this matter is not, in the judgment of some people, a good reason why it ought to be moved into the Federal Government. But since this decision of the Supreme Court the whole thing is in a state of chaos, as I have stated. Insurance companies are hesitating to pay taxes to the respective States, and so forth. This bill is brought here for the purpose of creating a moratorium until everybody can find out just what the situation is and what should be done about it, what can be done about it. That is the purpose of the bill.

Mr. PATMAN. Mr. Speaker, will the gentleman yield on that point?

Mr. SUMNERS of Texas. I will be glad to yield.

Mr. PATMAN. The gentleman has stated it is a moratorium. Is not section 3 permanent law?

Mr. SUMNERS of Texas. I get the purport of the gentleman's question. I think, and I am very candid with the gentleman, section 3 should at least be moved down into section 4, where the expiration date is 1948. But section 3 is not permanent law in an absolute sense, of course. Congress can repeal section 3 at any time. I do not want to dodge the point. I agree with the gentleman. I think it ought to be down in section 4, but it is not permanent law except in a technical sense.

Mr. KEFAUVER. Mr. Speaker, will the gentleman yield?

Mr. SUMNERS of Texas. I yield to the gentleman from Tennessee.

Mr. KEFAUVER. As a matter of fact, would not section 3 be subject to be changed in conference?

Mr. SUMNERS of Texas. I think we can do something about it.

Mr. PATMAN. No; the gentleman is mistaken.

Mr. SUMNERS of Texas. I do not know whether it can or not, but it does not make so much difference, because it is not permanent law except in the sense that it has no expiration date. Congress could repeal it even before 1948. Section 3 suspends no law or power which obtained before the Supreme Court decision referred to. Section 3 is in line with the moratorium objective, lacking only the expiration date. It is to be suspended. I want it distinctly understood, however, I would be willing to change it in conference so as to make its suspension terminate in 1948. I think perhaps it can be done. If it cannot, I would support an independent act, if necessary. Let me speak now to the point which my distinguished friend, for whom I have great respect, the gentleman from New Mexico [Mr. ANDERSON], has raised. He objects to the elimination from section 4. I quote:

For the purpose of enabling adjustments to be made and legislation to be adopted by the several States and Congress.

That language violates the principle of absolute moratorium and ought to be out of this bill. That is my position. It is not substantive law, I admit, but I hope in the intervening time we may be able to work out an arrangement under which the Federal Government may work out a policy which will be as adjusted, as possible, to the desire of the Congress and the people and that the States be aided and not hindered in assuming more and more governmental responsibility.

Mr. Speaker, if in the interim we can work out a system that would reestablish the power of the States to control insurance, would not that be a good thing to do? With all the power in this country moving into the Federal Government ought we not try to halt that movement if we can? I do not want an expression in this bill declaring that the moratorium is exclusively for the purpose of enabling the States to accommodate themselves to this new expression of Federal power. I want this time to be spent in seeing if we cannot work out a plan to contract in some degree this Federal power. At least that time should be not committed. It should be an open period for broad examination of the whole matter for everybody—those who want more power in Washington and those who want less.

I would like to have an opportunity to see what we can do within the entire picture. These bills have been drawn in the House and in the Senate under great pressure. New facts come in from time to time which indicate there should be some changes. There is not much difference. We cannot compose it here. In such a situation this is what I think we should do: Get this legislation to conference as quickly as we can, let the conferees, with all the information we have, get together and work out the best bill they can, and bring it back and submit it to the judgment of the House.

They will have a very good picture of the problem of the insurance companies and the problems of the States. They will have a good picture of the differences in the House.

Mr. COOPER. Mr. Speaker, will the gentleman yield?

Mr. SUMNERS of Texas. I yield.

Mr. COOPER. I would like to invite attention to the fact that it is the bill S. 340 that is now under consideration. The House committee proposes to strike out all after the enacting clause and insert a new bill. That means the whole thing would be in conference. The gentleman is correct, section 3 could be rewritten or could be taken out entirely in conference.

Mr. SUMNERS of Texas. Thank you, Jere. When I hear the distinguished gentleman from Tennessee speak I just wish the Lord had made two people as smart as he is, and that I was one of them.

I have nothing further to say, Mr. Speaker.

The SPEAKER. The time of the gentleman from Texas has expired.

Mr. WALTER. Mr. Speaker, I move the previous question on the bill and amendment to final passage.

The question was taken; and on a division (demanded by Mr. ANDERSON of New Mexico) there were ayes 152 and noes 59.

So the previous question was ordered.

The SPEAKER. The question is on agreeing to the amendment.

The amendment was agreed to.

The SPEAKER. The question is on the third reading of the Senate bill.

The bill was ordered to be read a third time, and was read the third time.

The SPEAKER. The question is on the passage of the bill.

Mr. COCHRAN. Mr. Speaker, I offer a motion to recommit.

The SPEAKER. Is the gentleman opposed to the bill?

Mr. COCHRAN. I am, in its present form.

The SPEAKER. The Clerk will report the motion offered by the gentleman from Missouri.

The Clerk read as follows:

Mr. COCHRAN moves to recommit the bill to the Committee on the Judiciary with instructions to report the bill back forthwith with an amendment striking out section 3.

Mr. WALTER. Mr. Speaker, I move the previous question on the motion to recommit.

The previous question was ordered.

The question was taken; and on a division (demanded by Mr. COCHRAN) there were—ayes 62, noes 171.

So the motion was rejected.

Mr. MARCANTONIO. Mr. Speaker, I ask for the yeas and nays.

The yeas and nays were refused.

The SPEAKER. The question is on the passage of the bill.

Mr. WALTER. On that I ask for the yeas and nays.

The yeas and nays were ordered.

The Clerk called the roll; and there were—yeas 315, nays 58, not voting 59, as follows:

[Roll No. 58]

YEAS—315

Abernethy	Barrett, Wyo.	Brumbaugh
Adams	Barry	Bryson
Allen, Ill.	Bates, Ky.	Buck
Allen, La.	Bates, Mass.	Buckley
Andersen, H. Carl.	Beall	Buffett
	Beckworth	Bulwinkle
Anderson, N. Mex.	Bell	Bunker
	Bender	Burch
Andresen August H.	Bennet, N. Y.	Burgin
	Bennett, Mo.	Butler
Andrews, Ala.	Bishop	Byrne, N. Y.
Andrews, N. Y.	Blackney	Byrnes, Wis.
Angell	Bland	Camp
Arends	Bonner	Campbell
Arnold	Boren	Canfield
Auchincloss	Bradley, Mich.	Carlson
Baldwin, Md.	Brehm	Case, N. J.
Baldwin, N. Y.	Brooks	Case, S. Dak.
Barden	Brown, Ga.	Chapman
Barrett, Pa.	Brown, Ohio	Chelf

Chenoweth
Chiperfield
Church
Clark
Cisson
Clevenger
Cole, Kans.
Cole, Mo.
Cole, N. Y.
Combs
Cooley
Cooper
Corbett
Cox
Cravens
Crawford
Cunningham
Curley
Curtis
Daughton, Va.
Davis
Delaney, James J.
Dingell
Dirksen
Dolliver
Domengeaux
Doughton, N. C.
Douglas, Ill.
Drewry
Durham
Dworshak
Earthman
Eberharter
Ellis
Ellsworth
Elsaesser
Engel, Mich.
Engle, Calif.
Ervin
Fallon
Fellows
Fenton
Fisher
Flannagan
Flood
Fogarty
Forand
Fuller
Fulton
Gallagher
Gamble
Gathings
Gavin
Gearhart
Geelan
Gerlach
Gibson
Gifford
Gillespie
Gillette
Gillie
Goodwin
Gorski
Gossett
Graham
Granahan
Granger
Grant, Ala.
Grant, Ind.
Gregory
Griffiths
Gross
Gwynne, Iowa
Hagen
Hale
Hall, Edwin Arthur
Hall, Leonard W.
Halleck
Hancock
Hand
Harris
Hartley
Hedrick
Hendricks
Herter
Heselton
Hess
Hill
Hinshaw
Hobbs
Hoch
Hoeven
Hoffman
Holmes, Mass.
Holmes, Wash.
Hope
Horan
Howell
Jarman
Jenkins
Jennings
Jensen
Johnson, Calif.
Johnson, Ill.
Johnson, Ind.
Johnson, Luther A.
Johnson, Okla.
Jones
Jonkman
Judd
Kean
Kearney
Keefe
Kefauver
Kilburn
Kilday
Kinzer
Knutson
Kopplemann
Kunkel
Lane
Lanham
Larcade
Latham
LeCompte
LeFevre
Lemke
Lewis
Luce
Ludlow
Lyle
McConnell
McCormack
McCowen
McDonough
McGehee
McGlinchey
McKenzie
McMillen, Ill.
Mahon
Maloney
Manasco
Mansfield, Mont.
Mansfield, Tex.
Martin, Mass.
Mason
Merrow
Michener
Miller, Nebr.
Mills
Monroney
Mundt
Murdock
Murphy
Murray, Tenn.
Murray, Wis.
Norrell
O'Konski
O'Neal
Pace
Patman
Patrick
Peterson, Fla.
Peterson, Ga.
Philbin
Phillips
Pickett
Pittenger
Ploeser
Plumley
Poage
Price, Fla.
Priest
Quinn, N. Y.
Rabaut
Rains
Ramey
Ramspeck
Randolph
Rankin
Reed, Ill.
Reed, N. Y.
Resa
Rich
Richards
Riley
Rizley
Robertson, N. Dak.
Robertson, Va.
Robinson, Utah
Robsion, Ky.
Rockwell
Rodgers, Pa.
Roe, Md.
Roe, N. Y.
Rogers, Fla.
Rogers, Mass.
Rogers, N. Y.
Ryter
Sasscer
Satterfield
Schwabe, Mo.
Scrivner
Sharp
Simpson, Ill.
Simpson, Pa.
Slaughter
Smith, Maine
Smith, Ohio
Smith, Va.
Smith, Wis.
Snyder
Sparkman
Springer
Starkey
Stefan
Stevenson
Stewart
Stigler
Stockman
Sumner, Ill.
Sumners, Tex.
Sundstrom
Taber
Talbot
Talle
Tarver
Taylor
Thom
Thomas, Tex.
Thomason
Tibbott
Tolan
Towe
Traynor
Trimble
Vinson
Vursell
Wadsworth
Walter
Weaver
Welchel
Welch
West
Whitten
Whittington
Wickersham
Wigglesworth
Winstead
Wolcott
Wolfenden, Pa.
Wolverton, N. J.
Wood
Woodhouse
Woodruff, Mich.
Woodrum, Va.
Worley
Zimmerman

NAYS—58

Bailey
Bloom
Bradley, Pa.
Cannon, Mo.
Carnahan
Celler
Cochran
Coffee
Crosser
Dawson
Delaney, John J.
Dickstein
Douglas, Calif.
Doyle
Feighan
Folger
Gordon
Green
Hart
Healy
Holifield
Hook
Huber
Hull
Jackson
Kee
Kelley, Pa.
Kelly, Ill.
King
Kirwan
Lea
Lesinski
Link
Marcantonio
Miller, Calif.
Morgan
Neely
Norton
O'Brien, Ill.
O'Brien, Mich.
Outland
Patterson
Powell
Price, Ill.
Rabin
Rayfiel
Rooney
Russell
Sabath
Sadowski
Savage
Sheppard
Somers, N. Y.
Spence
Sullivan
Torrens
Voorhis, Calif.
Weiss

NOT VOTING—59

Anderson, Calif.
Biemiller
Bolton
Boykin
Cannon, Fla.
Clements
Colmer
Courtney
D'Alesandro
De Lacy
Dondero
Eaton
Elliott
Elston
Fernandes
Gardner
Gwinn, N. Y.
Hare
Harless, Ariz.
Harness, Ind.
Havenner
Hays
Hebert
Heffernan
Heidinger
Henry
Izac
Johnson, Lyndon B.
Keogh
Kerr
LaFollette
Landis
Lynch
McGregor
McMillan, S. C.
Madden
Martin, Iowa
May
Morrison
Mott
O'Hara
O'Toole
Pfeifer
Powers
Reece, Tenn.
Rees, Kans.
Rivers
Rowan
Schwabe, Okla.
Shafer
Sheridan
Short
Sikes
Thomas, N. J.
Vorys, Ohio
Wasielewski
White
Wilson
Winter

So the bill was passed.

The Clerk announced the following pairs:

On this vote:

Mr. Schwabe of Oklahoma for, with Mr. Havenner against.

Mr. Gwinn of New York for, with Mr. De Lacy against.

Mr. Dondero for, with Mr. Pfeifer against.

Mr. Short for, with Mr. Sheridan against.

Mr. Vorys of Ohio for, with Mr. O'Toole against.

Mr. O'Hara for, with Mr. Heffernan against.

Mr. Shafer for, with Mr. Lynch against.

Mr. D'Alesandro for, with Mr. Rowan against.

General pairs:

Mr. Keogh with Mr. Eaton.

Mr. Colmer with Mr. Harness of Indiana.

Mr. Hébert with Mr. Anderson of California.

Mr. Boykin with Mr. Elston.

Mr. Morrison with Mr. Wilson.

Mr. Wasielewski with Mr. Rees of Kansas.

Mr. Cannon of Florida with Mr. McGregor.

Mr. Kerr with Mr. Thomas of New Jersey.

Mr. Izac with Mr. Reece of Tennessee.

Mr. Courtney with Mr. Martin of Iowa.

Mr. Hare with Mr. Powers.

Mr. Lyndon B. Johnson with Mrs. Bolton.

Mr. May with Mr. Winter.

Mr. Elliott with Mr. LaFollette.

Mr. McMillan of South Carolina with Mr. Landis.

Mrs. NORTON changed her vote from "aye" to "no."

Mr. MAY. Mr. Speaker, I desire to vote.

The SPEAKER. Was the gentleman present and listening when his name was called?

Mr. MAY. No, Mr. Speaker; I was attending a committee hearing.

The SPEAKER. The gentleman does not qualify.

The result of the vote was announced as above recorded.

A similar House bill (H. R. 1973) was laid on the table.

EXTENSION OF REMARKS

Mr. CHIPERFIELD asked and was given permission to revise and extend his own remarks.

Mr. SMITH of Wisconsin asked and was given permission to extend his own remarks in the RECORD.

Mr. MICHENER. Mr. Speaker, I ask unanimous consent that the gentleman from Washington [Mr. HORAN] may extend his own remarks in the RECORD and include an article.

The SPEAKER. Is there objection to the request of the gentleman from Michigan?

There was no objection.

Mr. LEA. Mr. Speaker, I ask unanimous consent to extend my own remarks in the RECORD and to include therein a letter from the Civil Aeronautics Authority.

The SPEAKER. Is there objection to the request of the gentleman from California?

There was no objection.

Mr. GRANT of Indiana. Mr. Speaker, I ask unanimous consent to extend my own remarks in the RECORD and include an article from Our Sunday Visitor.

The SPEAKER. Is there objection to the request of the gentleman from Indiana?

There was no objection.

Mr. GRANGER. Mr. Speaker, I ask unanimous consent to extend my own remarks at this point in the RECORD.

The SPEAKER. Is there objection to the request of the gentleman from Utah?

There was no objection.

JUSTIFICATION OF PRESIDENT ROOSEVELT'S FOURTH TERM

Mr. GRANGER. Mr. Speaker, I am what is generally referred to as a party man. I have believed in, and do now support generally, the policies of the present administration. Even so, there has always been in my mind the question of whether or not there was any justification for the departure from our long accepted precedent in limiting the term of the Presidency to 8 years.

I have never believed in the indespensability of any man as I have always thought there would be raised, or some individual would arise, who would meet any emergency of our country.

The events of the last week, however, in my opinion, have justified the action of the American people by breaking that long cherished precedent. Not that President Franklin D. Roosevelt is the only individual that could have cooperated with our allies in the establishing of what I believe is the basis of an enduring peace, but by his action he has demonstrated that he has accomplished what the American people wanted done. He has not failed them.

If he had failed the people, the third and fourth term certainly would not have been unjustifiable, but because of the action taken at the recent Crimean Conference, it certainly justifies the action and historians will record the wisdom of the American people in this instance. If we build wisely on the foundation now laid, the world can look forward to a long period of peace. The high patriotic position of the leadership of the minority party is equally praiseworthy. It has not been, and cannot be, a partisan peace. But an American peace. To endure it must have the same popular support as has the Monroe Doctrine.

PERMISSION TO ADDRESS THE HOUSE

Mr. MICHENER. Mr. Speaker, I ask unanimous consent that on Wednesday, February 21, after the disposition of the legislative business of the day and other special orders, the gentleman from Ver-

The SPEAKER pro tempore. The time of the gentleman from Mississippi has expired.

DEFERMENT OF FARM WORKERS

Mr. MAY. Mr. Speaker, at the suggestion of the Chair, I took up with the leadership of the minority side of the House the question of a unanimous-consent request for the consideration of House Joint Resolution 106, commonly known as the Flannagan resolution.

Mr. MARTIN of Massachusetts. Will the gentleman explain to the House what the Flannagan resolution is?

Mr. MAY. I want to make the request first and then I will explain it.

I ask unanimous consent, Mr. Speaker, that House Joint Resolution 106 may be made in order next week, to be taken up under the rules of the House when the leadership is able to do so; that 1 hour of general debate be had on the resolution, the time to be equally divided and controlled by the chairman of the Committee on Military Affairs and the ranking minority member of that committee.

The SPEAKER pro tempore. Is there objection to the request of the gentleman from Kentucky [Mr. MAY]?

Mr. MARTIN of Massachusetts. Mr. Speaker, reserving the right to object, will the gentleman explain what this bill is so that the House may know?

Mr. MAY. The Selective Training and Service Act, section 5 (k), commonly known as the Tydings amendment, provides for the deferment of farm workers. There has been a question raised as to the proper construction of that provision of the act or at least the construction being placed upon it by the Director of Selective Service. The resolution undertakes to and does place an interpretation on section 5 (k) of the Selective Training and Service Act, which is claimed to be the construction that was intended by the Congress, and I believe it is what the Congress intended. It was reported by the House Committee on Military Affairs without amendment, and the purpose of this unanimous-consent request is to get it disposed of as promptly as possible.

Mr. MICHENER. Mr. Speaker, further reserving the right to object, the Lemke resolution was reported out by the Rules Committee some days ago. The Lemke resolution is a concurrent resolution and reiterates what the intent of Congress was when it adopted the Tydings amendment. It also sets up a committee of six to investigate the interpretation of the Tydings amendment. As I understand the Flannagan bill it writes into law what the Lemke resolution suggests is the intent of Congress. What I am interested in is, when is the gentleman from Kentucky going to call up the Flannagan bill, if his request is granted?

Mr. MAY. I will say to the gentleman that my request contains the statement that I would take it up at the pleasure of the leadership of the House. It is my purpose to take it up at the very first opportunity.

Mr. MICHENER. The Lemke resolution comes from the Rules Committee. Therefore it cannot be delayed more than 7 days after being reported. If the chairman of the Rules Committee does not call it up within the 7 days then any member of the Rules Committee can call it up. In this case, time is of the essence. I do not want to consent to something that will sidetrack something else. We want assurance that the Flannagan bill will be brought up expeditiously and disposed of.

Mr. SABATH. Mr. Speaker, will the gentleman yield?

Mr. MICHENER. I yield.

Mr. SABATH. The Lemke resolution, Mr. Speaker, is a concurrent resolution and proposes that a committee of three Members of the House and three Members of the Senate be appointed to make an investigation relative to the matter. In accordance with ordinary practice and procedure the Rules Committee has prepared a resolution for the consideration of the resolution which either has been or will be filed by the gentleman from Georgia [Mr. COX].

The resolution reported by the Committee on Military Affairs will take effect immediately upon its passage, whereas the Lemke resolution may delay action by the House for a long while, because we know that joint committees generally take their time.

Immediate action is demanded and urged. I myself believe there is justification for it, because only this morning I noticed that the general average of men still on the farms, men between 18 and 25 for each State, which should be about 4 percent, was in the case of the State of North Dakota 25 percent. Surely they can have no complaint from that State. What applies to his State applies to half a dozen others.

Later I shall ask unanimous consent to insert in the RECORD the table of figures as it applies to all the States in the matter of men in the age group 18-25 who are still on farms. I believe this table will prove that those who claim that States with large city populations are enjoying the advantage will find that the contrary is true.

Mr. MICHENER. Mr. Speaker, answering my distinguished friend, the chairman of the Rules Committee, I may say that the Rules Committee is well aware of his position and his belief that legislation of this kind is not required.

I make this reservation because the Rules Committee some days ago ordered the Lemke resolution reported, but an unusual thing has happened and the resolution has not yet even been reported by the committee to the House, and the 7-day period begins to run only from the time the resolution is reported to the House.

Inasmuch as the chairman of the Committee on Military Affairs has brought this matter up this morning and our distinguished chairman states that if this committee is given just a little more time, it will report the Lemke resolution. We are interested in knowing that definite action will be taken soon. In the meantime, these boys are being taken from the farms, right or wrong, but in line with the Tydings amendment, as understood by General Hershey. Time is important and certainly the chairman of the Committee on Military Affairs should not ask permission to bypass the rules of the House and leave the matter in the discretion of the majority leadership, in which event the 7-day rule would not apply. I favor the consideration of the Flannagan bill at the earliest opportunity. The Flannagan bill will result in a law with all that a law implies. The Lemke resolution is not a law, simply expresses an intent and provides for the appointment of a committee. The bill and the resolution each require action by the House and the Senate. The Flannagan bill requires the signature of the President.

Mr. LEMKE. Mr. Speaker, reserving the right to object, may I suggest first that the distinguished chairman of the Rules Committee is attempting to juggle my resolution out of existence because he does not correctly state the effect of the resolution. The resolution contains two parts.

The first part defines clearly what the Tydings amendment is, and I will read it so that the gentleman and the Members will understand it in the future. It reads as follows:

> That in order that there may be no further misinterpretation of the will and the desire of the Congress in enacting subsection K, section 305, title 50, United States Code, commonly known as the Tydings amendment to the Selective Service Act, Congress reaffirms the necessity to our war effort of said subsection K and again expresses its will and desire that the local selective-service board, in classifying the registrant, observe subsection K and concern itself solely with the registrant's essentiality to an agricultural occupation or endeavor and to the question of whether or not a satisfactory replacement can be obtained.

Why ignore that part of the resolution? I am for the Flannagan resolution, but I am not for this juggling. My resolution is effective when passed. Mr. Flannagan's will have to go to the President, and he may veto it; then we will be nowhere unless we have both.

Mr. HOFFMAN. Mr. Speaker, I demand the regular order.

The SPEAKER pro tempore. The regular order is demanded. Is there objection to the request of the gentleman from Kentucky [Mr. MAY]?

Mr. LEMKE. Mr. Speaker, I object.

CONFERENCE REPORT—REGULATION OF THE BUSINESS OF INSURANCE

Mr. WALTER. Mr. Speaker, I call up the conference report on the bill (S. 340) to express the intent of Congress with reference to the regulation of the business of insurance, and I ask unanimous consent that the statement of the managers on the part of the House may be read in lieu of the full report.

The SPEAKER pro tempore. Is there objection to the request of the gentleman from Pennsylvania?

There was no objection.

The Clerk read the statement of the managers on the part of the House.

The conference report and statement are as follows:

CONFERENCE REPORT

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (S. 340) to express the intent of the Congress with reference to the regulation of the business of insurance, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the Senate recede from its disagreement to the amendment of the House and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the House amendment insert the following:

"*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled*, That the Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

"SEC. 2. (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

"(b) No act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after January 1, 1948, the act of July 2, 1890, as amended, known as the Sherman Act, and the act of October 15, 1914, as amended, known as the Clayton Act, and the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

"SEC. 3. (a) Until January 1, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the Act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.

"(b) Nothing contained in this Act shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

"SEC. 4. Nothing contained in Act shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935, as amended, known as the National Labor Relations Act, or the act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938 or the Act of June 5, 1920, known as the Merchant Marine Act, 1920.

"SEC. 5. As used in this act, the term 'State' includes the several States, Alaska, Hawaii, Puerto Rico, and the District of Columbia.

"SEC. 6. If any provision of this Act, or the application of such provision to any person or circumstances, shall be held invalid, the remainder of the Act, and the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected."

And the House agree to the same.

HATTON W. SUMNERS,
FRANCIS E. WALTER,
C. E. HANCOCK,
Managers on the part of the House.

PAT MCCARRAN,
JOSEPH C. O'MAHONEY,
HOMER FERGUSON,
Managers on the part of the Senate.

STATEMENT

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendment of the House to the bill (S. 340) to express the intent of the Congress with reference to the regulation of the business of insurance, submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report:

The House amendment struck out all of the Senate bill after the enacting clause. The committee of conference recommends that the Senate recede from its disagreement to the amendment of the House, with an amendment which is a substitute for both the Senate bill and the House amendment, and that the House agree to the same

It was the purpose on the part of the managers of the House to have the agreement between themselves and the managers on the part of the Senate to state in as clear language as possible that a moratorium be granted to the insurance business from the operation of the act of July 2, 1890, as amended, known as the Sherman Act, and the act of October 15, 1914, as amended, known as the Clayton Act, and the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, until January 1, 1948, leaving the taxing and regulatory powers of the several States fully protected.

The principal difference between the conference report and the bill as it passed the House lies in the inclusion of the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, in the moratorium provision, and making clear the intention of the Congress that the acts of boycott, coercion, and intimidation are subject to the operation of the suspended statutes even during the moratorium period.

HATTON W. SUMNERS,
FRANCIS E. WALTER,
C. E. HANCOCK,
Managers on the part of the House.

The SPEAKER pro tempore. The question is on agreeing to the conference report.

The conference report was agreed to.

A motion to reconsider was laid on the table.

CONDUCT OF MEMBERS

Mr. SMITH of Virginia. Mr. Speaker, I ask unanimous consent to address the House for 1 minute.

The SPEAKER pro tempore. Is there objection to the request of the gentleman from Virginia?

There was no objection.

Mr. SMITH of Virginia. Mr. Speaker, I regret again to bring up the incident that occurred on yesterday, but as I was engaged with the gentleman from Georgia in the preparation of a resolution of censure, I do not want my position on the matter to remain obscure or misunderstood. I feel today as I felt yesterday, that there should be a resolution of censure. I think that, regardless of who the person may be, when language of the type that was used yesterday on the floor of this House is used by a Member, the House cannot ignore it without lowering the dignity and the standing of the House in the country.

I regret very much that no further action was taken on the matter. I was endeavoring to obtain recognition by the Chair to offer a resolution of censure, and would have done so had the Speaker recognized me.

FARM DRAFT SITUATION

Mr. SHORT. Mr. Speaker, I ask unanimous consent to address the House for 1 minute.

The SPEAKER pro tempore. Is there objection to the request of the gentleman from Missouri?

There was no objection.

Mr. SHORT. Mr. Speaker, I ask for this 1 minute to discuss very briefly the Lemke resolution and the so-called Flannagan resolution which was reported yesterday by the Committee on Military Affairs.

May I say for the information of the membership of the House that this is just one more instance where Congress is embarrassed and humiliated by executive misinterpretation of statutory law. All that the Flannagan resolution does is simply to say that the Congress meant what it said when it passed the Tydings amendment, which has been ignored or misconstrued.

Mr. Speaker, food and fiber are the primary weapons of war. We are threatened with shortages of both. Today men are being drafted from farms into our armed services in clear violation of the law. This is not the fault of Congress but of enforcement officials. Such nefarious practice must stop, and stop now.

I think it is high time that we started some impeachment proceedings against certain executive officers of our Government in order to put an end to this nonsense.

The only difference between the Flannagan resolution and the Lemke resolution is that the President can veto the Flannagan resolution, but he cannot veto the Lemke resolution because it is a concurrent resolution which must be passed by both Houses, and the President's signature is not required. I am in favor of both resolutions but I prefer the Lemke resolution. It will achieve quicker and better results.

Mr. COCHRAN. Mr. Speaker, I ask unanimous consent to address the House for 1 minute and to revise and extend my remarks.

deposits, or by contracting with farmer-owned cooperatives for such development to be financed by Government loans. New sources of potash should be developed on the same principle. These developments need not interfere with present private operation if consumption should be sufficiently expanded to use the potash produced from both sources.

Most potash presently produced is shipped either through the Panama Canal from California or by rail from New Mexico to Gulf ports and thence to mixing plants. After it is mixed into mixed fertilizer, another long shipping haul is necessary to get it to farmers. This shipping cost must be cut down by location of plants near sources.

2. Nitrogen: The Department of Agriculture interbureau committee that recently reported on war ammonia plants says up to 1,200,000 tons of fixed nitrogen ought to be supplied for civilian consumption in the United States. This is a low estimate, if the Government undertakes the kind of program put forward here. Systematic promotion of fertilizer use, such as T. V. A. has encouraged, could well run consumption up to 1,500,000 or more tons, or double the capacity of the Government-owned nitrogen plants. This would leave a considerable market for private industry, larger than it now has, and even would leave room for such imports as are regarded as economically desirable, and as needed in the interest of international harmony.

These plants, like the T. V. A., are the property of the whole people and should be retained in their hands, either for direct Government operation or for operation by farmer-owned cooperatives under governmental supervision.

3. Superphosphates: The T. V. A. has shown both that phosphate consumption can be expanded tremendously, to the advantage of the farmer and the Nation, and that miraculous results can be achieved in restoring soil by use of phosphates. Fortunately, the United States has tremendous resources of phosphate. The limiting physical factor in full use of present superphosphate plant capacity has been a shortage of sulfuric acid. Present war plants are producing as byproducts a considerable amount of sulfuric acid. A peacetime program for stand-by maintenance of these plants should provide for an expanded program of Government production of sulfuric acid, and such of the plants as are adaptable to the purpose without too great expense and as are not to be maintained for military eventualities, should be converted to uses that will produce additional quantities of sulfuric acid. The Government should use this supply to reduce the cost of commercial phosphates.

In addition, future programs for resources development such as T. V. A. should include specific authorization for bringing the T. V. A. fertilizer program to other areas. Wherever power development is authorized—in the proposed Arkansas, Missouri, Columbia, or other authorities—provision should be made for electric furnaces or other appropriate installations that will meet the regional needs of farmers for ever-expanding use of phosphates.

4. Mixing plants: All of the elements for which separate programs have been proposed here must be combined into mixed fertilizer, at least so far as most farmers are concerned. A major factor in limiting fertilizer use is the uneven distribution of mixing facilities over the country, adding to freight charges and making it difficult for farmers to obtain fertilizer at the precise time when they need it most. Fertilizer use not only is seasonal but must be timed almost to the day. Thus a governmental program of the kind put forward here should include provision for a $100,000,000 revolving fund for loans to farmers' cooperatives to establish small mixing plants as widely throughout the United States as possible, with at least one in each State and with several in those States with large farm population. These may be spaced so as to avoid serious competition with present plants, so far as possible, yet at the same time to provide a gage on charges by those plants.

5. Plant food content: It has been estimated that the inert matter presently used as "filler" in mixing with vital elements costs American farmers a minimum of $11,000,000 a year. It is probable that the actual cost is more than that sum, and it is certain that any great expansion of fertilizer use would require a uniform increase in plant-food content per ton and a corresponding reduction in filler if much more than $11,000,000 in costs is to be saved. A number of States now have laws governing the plant-food content of fertilizer. Some of these are inadequate, however, and the unevenness of State regulation works a hardship on the fertilizer industry and farmers alike. A Federal statute providing for continuing and strengthening the uniform wartime Federal grades is badly needed, and this law should require a far higher proportion of vital to inert matter than is now the case. Extension of the fertilizer program proposed here to any State should be contingent on enforcement by that State of uniform grades. Such a law could well take advantage of experience with the model Soil Conservation Districts Act. Plant-food content now averages about 20 percent. This is indefensibly low. The maximum consistent with farm practices and machinery should be prescribed, as determined by scientists. Such a change would call for changes in design of some farm machinery but if manufacturers were advised sufficiently far ahead of time, they could make such changes without too great strain.

The objective should be to establish such plants where they are most needed.

In conclusion, I should like to add that such a program calls for other subsidiary action, for instance a vigorous educational campaign through State and Federal agencies, and for a complementary program for liming acid land throughout the Nation. I have thought it best, however, not to attempt to spell out in detail here all that would be necessary.

What is needed now is thorough congressional exploration of the whole subject. To that end I suggest that farm State Members of Congress insist on early hearings on the bill S. 2055, sponsored by Senator LISTER HILL, of Alabama. His bill is excellent. The proposals made here could be readily incorporated in his measure "to provide for a national fertilizer policy and program." Many phases of this legislation ought to be in operation well before the end of the war.

I should appreciate your reaction to these proposals.

Sincerely,

JAMES G. PATTON,
President, National Farmers Union.

REGULATION OF THE BUSINESS OF INSURANCE—CONFERENCE REPORT

Mr. McCARRAN. Mr. President, I move that the Senate proceed to the consideration of the conference report on Senate bill 340, to express the intent of the Congress with reference to the regulation of the business of insurance.

The motion was agreed to; and the Senate proceeded to consider the report.

The PRESIDING OFFICER (Mr. FULBRIGHT in the chair). The question is on the adoption of the report.

Mr. MURDOCK. Mr. President, will the Senator yield for a question?

Mr. McCARRAN. I yield.

Mr. MURDOCK. As I understand the conference report which is now before the Senate, it provides for a 3-year moratorium, which is fixed as ending on January 1, 1948, against the invoking of the Sherman Act and the Clayton Act, and it provides that they shall again be in force after that period without any affirmative action on the part of the Congress, except as regulatory matters have been enacted by the States relating to subjects covered by those acts——

Mr. McCARRAN. During the moratorium. Regulatory acts must be enacted by the several States in each of the several States. Otherwise the antitrust acts become effective after January 1, 1948.

Mr. MURDOCK. But is it not the purpose of the bill and does not the bill accomplish this——

Mr. McCARRAN. It accomplishes a moratorium for 3 years against the operation of the acts mentioned, namely, the Sherman Antitrust Act, the Clayton Act, the Federal Trade Commission Act, as amended, and the Robinson-Patman Antidiscrimination Act.

Mr. MURDOCK. So that during the moratorium it is intended, is it not, that the States shall affirmatively step into the regulation of the insurance business?

Mr. McCARRAN. That is correct.

Mr. MURDOCK. And it is intended that on the expiration of the moratorium the Sherman Act, the Clayton Act, and the other acts mentioned will again become effective except——

Mr. McCARRAN. Except as the States themselves have provided regulations.

Mr. MURDOCK. I thank the Senator.

Mr. ELLENDER. Mr. President, will the Senator yield?

Mr. McCARRAN. I yield.

Mr. ELLENDER. At the end of the 3-year period will the taxing and regulatory powers of the States be in anywise affected should the Congress not take any action at all?

Mr. McCARRAN. No; they will not be affected.

Mr. ELLENDER. They will not be affected?

Mr. McCARRAN. That is correct.

Mr. President, let me make one statement which I think should be placed in the RECORD here. It should be stated here, as it was stated in the report which went to the House, from which I read that—

> It is not the intention of Congress in the enactment of this legislation to clothe the States with any power to regulate or tax the business of insurance beyond that which they had been held to possess prior to the decision of the United States Supreme Court in the Southeastern Underwriters Association case. Briefly, your committee is of the opinion that we should provide for the continued regulation and taxation of insurance by the States, subject, always, however, to the limitations set out in the controlling decisions of the United States Supreme Court, as, for instance, in *Allgeyer v. Louisiana* (165 U. S. 578); *St. Louis Cotton Compress Co. v. Arkansas* (260 U. S. 346); and *Connecticut General Insurance Co. v. Johnson* (303 U. S. 77).

That expression should be made a part of this explanation. In other words, we give to the States no more powers than those they previously had, and we take none from them.

Mr. HATCH and Mr. WHITE addressed the Chair.

Mr. McCARRAN. I yield first to the Senator from New Mexico.

Mr. HATCH. I shall be glad to defer to my colleague the Senator from Maine.

Mr. WHITE. I thank the Senator from New Mexico.

Mr. President, let me ask the Senator from Nevada whether the report represents a complete agreement on the part of the conferees.

Mr. McCARRAN. It does.

Mr. WHITE. Is the report signed by all the conferees on the part of the Senate?

Mr. McCARRAN. Yes; it is signed by all of them.

Mr. O'MAHONEY. Mr. President, will the Senator yield?

Mr. McCARRAN. I yield.

Mr. O'MAHONEY. I was going to remark that, as I listened to the Senator when he read from the committee report, I noticed that he was reading from the report of the House Judiciary Committee to the House on the occasion when the bill was reported to the House.

Mr. McCARRAN. That is correct.

Mr. O'MAHONEY. Of course, the conference report has deviated from the bill which was reported by the House Judiciary Committee, so that the language the Senator has read does not in any way modify or alter any language in the conference report.

Mr. McCARRAN. No; I do not intend that it should be so implied.

Mr. HATCH. Mr. President, the question I was going to propound to the Senator from Nevada arises in connection with subparagraph (b) on page 2 of the conference report, reading as follows:

(b) Nothing contained in this act shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

There is no moratorium at all as to these matters, is there?

Mr. McCARRAN. No; there is no moratorium at all as to them.

Mr. PEPPER. Mr. President, will the Senator yield?

Mr. McCARRAN. I yield.

Mr. PEPPER. I have read hastily the conference report, but I am a little disturbed by what I have discovered in paragraph (b) of section 2. I read beginning with section 2 (a):

SEC. 2. (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically relates to the business of insurance: *Provided*, That after January 1, 1948, the act of July 2, 1890, as amended, known as the Sherman Act, and the act of October 15, 1914, as amended, known as the Clayton Act, and the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

Does that mean that after January 1, 1948, the States may determine whether or not the Sherman and the other acts become applicable to the business of insurance?

Mr. McCARRAN. The answer to that question is "Yes." During the 3-year moratorium the States may, if they see fit to do so, enact legislation for the purpose of regulation. If they do enact such legislation, to the extent that they regulate they will have taken the business of insurance in the respective States out from under the Sherman Anti-trust Act, the Clayton Act, and the other acts. If during the moratorium the States do not enact legislation for regulatory purposes, then on January 1, 1948, the Sherman Act, the Clayton Act, and the other acts will become immediately applicable.

Mr. PEPPER. Mr. President, does that not necessarily mean that we would give to the several State legislatures power, the character and outlines of which we do not define, to determine whether a Federal law enacted for the protection of all business and against all kinds of monopolies and restraints of trade shall be effective in the American Union?

Mr. McCARRAN. The bill does not go that far. The Senator will recall the Southeastern Underwriters case. The decision was startling. It created consternation in the insurance business because by previous decisions rendered during the past 50 years or more we were entitled to believe that the business of insurance was not to be classified as interstate commerce. The Supreme Court of the United States specifically, directly, and emphatically put it into the category of interstate commerce. It put it squarely under the Sherman Act, the Clayton Act, and other acts. The pending bill is for the purpose of creating a moratorium for 3 years in order that the business of insurance shall not be interfered with by any Federal power under either the Clayton Act or the Sherman Act. So during the period of moratorium the various States themselves may take steps to regulate the business of insurance.

Mr. PEPPER. Mr. President, I have one further question. While I believe that the decision of the Supreme Court was eminently correct, and that it was an example of justice too long delayed, I do not wish to see anything done which will destroy the effectiveness of that decision. If there are reasons which make proper a moratorium for 3 years under the understanding that at the end of such a period of time the Clayton Act, the Sherman Act, and the other acts shall go into effect, well and good, but, so far as I am concerned, I shall not consent to postponing until January 1, 1948, the effective date of the law, and according to the States the privilege of enacting some mild form of legislation which they may call regulatory, thereby defeating the purpose of the Supreme Court decision and defeating the act itself. Apparently the conference report goes further than I had understood it to go. It does not stop with a moratorium at the end of 3 years. At the end of 3 years the moratorium would continue if in the meantime a State had regulated the business to any extent whatever. That would defeat the Supreme Court decision.

Mr. McCARRAN. The moratorium would not be continued; but if in the meantime the States themselves had regulated the business of insurance, the Sherman and Clayton Acts and the other acts would not become effective.

Mr. FERGUSON. Mr. President, will the Senator yeild?

Mr. McCARRAN. I yield.

Mr. FERGUSON. I believe that a statement as to the fair construction of the act would add to the helpfulness of what the Senator from Nevada has said. There are certain things which a State cannot interfere with. It cannot interfere with the application of the Sherman Act to any agreement to boycott, coerce, or intimidate, or an act of boycotting, coercion, or intimidation.

Mr. McCARRAN. Not at any time.

Mr. FERGUSON. Not at any time.

Mr. McCARRAN. Nor is the control of those matters under the specified antitrust acts removed at any time.

Mr. FERGUSON. That is correct. After the moratorium has expired, if a State has not legislated on the subjects covered by the three acts to which reference has been made, those acts shall be applicable to the business of insurance. But insofar as the State is concerned which has specifically legislated on the subject, the three acts shall not apply.

Mr. O'MAHONEY. Mr. President, will the Senator yield?

Mr. McCARRAN. I yield.

Mr. O'MAHONEY. I believe the Senator from Michigan went a little further than was his intention when he said that if the States have legislated certain things will take place. The bill says if the States have regulated.

Mr. FERGUSON. I had reference to legislation dealing with regulation and taxes.

Mr. O'MAHONEY. The bill attempts to provide for a moratorium. I ask for the attention of the Senator from Florida in order that I may give him my interpretation of the bill.

While the Southeastern Underwriters case was pending in the Supreme Court an effort was made to deprive the court of jurisdiction by passing a bill which, in effect, provided that the Sherman and the Clayton Acts should not apply to the business of insurance in any way, shape, or form.

Mr. PEPPER. Knowing how actively the insurance companies of my State fought me because I opposed the bill, I should remember it.

Mr. O'MAHONEY. That bill was not enacted. The pending bill provides for a moratorium. It contains a declaration that for a period of time the Sherman and Clayton Acts, as well as the other acts, shall not apply.

Section 4 specifically declares that the National Labor Relations Act, the Fair Labor Standards Act, and the Merchant Marine Act shall apply. Nothing in the proposed act shall be construed to affect their application. In other words, there is a positive declaration that those three specific Federal laws which were enacted by Congress to apply to commerce apply also to insurance.

Then we have a clear recommendation of the principle of the Supreme Court decision in the Southeastern Underwriters case.

Now, with respect to the section to which the Senator himself refers, it follows the declaration in the very first section that "Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest." So now we endeavor to convey that power of regulation to the States—to recognize it, I should say, rather than convey it—to recognize as desirable the regulation.

Mr. PEPPER. Will the Senator from Nevada yield?

Mr. McCARRAN. I yield.

Mr. PEPPER. Does that mean that the States can by their own laws defeat the applicability and operation of the Sherman Antitrust Act and the Clayton Act?

Mr. O'MAHONEY. I think the answer to that question will be clear when I point out that there are certain agreements which can normally be made in the insurance business which are in the public interest, but which might conceivably be a violation of the antitrust law, which prohibits combinations and agreements in restraint of trade.

Mr. PEPPER. Would it not be better that those agreements, if there are such that are legitimatized, be identified in the statute?

Mr. O'MAHONEY. I quite agree with the Senator, and I endeavored to the very best of my ability to induce the committees of Congress to write into the law specific exemptions from the antitrust law, but I was unable to prevail in the Committee on the Judiciary and I was unable to prevail on the floor of the Senate. But now we have this declaration that with respect to these particular acts, the Sherman Act, the Clayton Act, the Federal Trade Commission Act, no act of Congress shall be construed to invalidate the law of any State passed for the regulation or the taxing of the business of insurance, and then the proviso.

Mr. PEPPER. Will the Senator read the proviso?

Mr. O'MAHONEY. It provides that after January 1, 1948, these several acts——

Mr. PEPPER. That is, the Sherman Act and the Clayton Act.

Mr. O'MAHONEY. Yes. They "shall be applicable"—there is a positive declaration—"to the business of insurance to the extent that such business is not regulated by State law," as was stated by one of the House Members of the conference committee. I interpret that to be a clear statement that if the States do not regulate, the power of Congress to regulate is clearly enunciated. I do not conceive this to be a grant of power to the States to authorize by permissive legislation obviously adverse combinations which would be against the public interest.

Mr. PEPPER. Am I correct in saying that under the proviso which the Senator has just read, if a State made it an offense, under the laws of the State, to engage in combinations in restraint of trade, the Sherman Antitrust Act could not apply to combinations and restraints of trade by companies engaged in business in that State? Is not that what it means?

Mr. O'MAHONEY. No; I think that, for example, a rating bureau, formerly agreement among insurance companies, under the supervision and regulation of the State, would be permitted.

Mr. PEPPER. That may relate to the getting together and filing of proper data and obtaining certain statistical information and disseminating it, and all that, but the legal effect of the proviso which the Senator has just read is that a State can absolutely prevent the applicability of the Sherman Antitrust Act and the Clayton Act to insurance companies doing business in the State by passing a State act which will make combinations and restraints of trade unlawful in that State. As a practical matter, we know that the States cannot and will not enforce these laws against these insurance companies.

Mr. WHITE. Mr. President, is it not perfectly clear that the force and effect of these Federal statutes may be applicable and shall be applicable to whatever extent the State law fails to occupy the ground and engage in regulation? As I take it, there are two jurisdictions.

Mr. McCARRAN. There always are.

Mr. WHITE. There is the State, authorized to act to whatever extent seems proper.

Mr. McCARRAN. That is correct.

Mr. WHITE. Then the Federal Government can come in, and it does come in and may legislate beyond the limit of the State legislation.

Mr. McCARRAN. To the extent that the State does not regulate.

Mr. WHITE. To the extent that the State does not regulate.

Mr. MURDOCK. Mr. President, does the Senator from Maine take the position that, under the conference report, it becomes necessary for the Congress to act again affirmatively, subsequent to any State action taken?

Mr. WHITE. Not at all; that is not my view of the matter at all. My view is that the State may regulate. If, however, the State goes only to the point indicated, then these Federal statutes apply throughout the whole field beyond the scope of the State's activity.

Mr. McCARRAN. That is a correct statement.

Mr. MURDOCK. Without any subsequent action on the part of Congress?

Mr. WHITE. Without any subsequent action on the part of Congress.

Mr. MURDOCK. I think that therein lies a very important feature of this whole matter. I agree thoroughly with the Senator from Maine that insofar as the States step into the picture affirmatively and act by regulation, they may do so. As the Senator from Wyoming has said, we convey no authority, we simply recognize their right to regulate. Insofar as they fail to cover the same ground covered by the Sherman Act and the Clayton Act, those acts become effective again.

Mr. BARKLEY. Mr. President, will the Senator yield?

Mr. McCARRAN. I yield.

Mr. BARKLEY. I should like to ask, in this connection, whether, where States attempt to occupy the field—but do it inadequately—by going through the form of legislation so as to deprive the Clayton Act, the Sherman Act, and the other acts of their jurisdiction, it is the Senator's interpretation of the conference report that in a case of that kind, where the legislature fails adequately even to deal with the field it attempts to cover, these acts still would apply?

Mr. McCARRAN. That is my interpretation.

Mr. PEPPER. Mr. President, I wish to address myself to the report before it is acted on, and I should appreciate very much if it might be allowed to go over so that I would have that opportunity. At the present time I am not disposed to let the matter go through without addressing myself to it.

The PRESIDING OFFICER. The question is on agreeing to the conference report.

Mr. PEPPER. Mr. President, I wish to address myself to the subject, then, and I shall simply have to delay the Senate, because I wish to discuss the report. I shall be frank; I think the conference report bill practically destroys the effect of the Supreme Court decision, and I am against that. At least I wish to have time to go into it. I do not know of any emergency which requires that the report be agreed to this afternoon. I should appreciate the privilege of considering the matter a little.

Mr. McCARRAN. The Senator is correct regarding the 3-year moratorium, but beyond that he is in error.

Mr. PEPPER. I would not expect Senators, even if they had the power, to change the report on the floor, and I am perfectly willing to have provided a 3 or 4 or 5 year moratorium, but I am not willing to see the decision of the Supreme Court emasculated. I wish to study the matter before I can give my consent to it. Otherwise, I certainly wish to address myself to it.

Mr. McCARRAN. Just one question to the Senator, then I shall yield and the conference report may go over, so far as I am concerned. Does the Senator oppose State regulation of insurance?

Mr. PEPPER. I do not oppose State regulation which is not inconsistent with the operation of the Sherman antitrust Act and the Clayton Act. On matters of taxation, general regulation, and all that sort of thing, I think the States should regulate, but I think that now that insurance has been brought, by the decision of the Supreme Court, up to the bar of the Clayton Act and the Sherman Act, we should not give the insurance companies immunity from the applicability of those acts.

Mr. McCARRAN. I am willing that the matter should go over, but I should like to call it up tomorrow.

Mr. PEPPER. That is all right. I appreciate the Senator's consideration.

The PRESIDING OFFICER. Without objection, the consideration of the conference report will go over.

EXECUTIVE SESSION

Mr. BARKLEY. I move that the Senate proceed to the consideration of executive business.

time we induct a man it will be at least 6 months before he is available on the front, actually in battle.

Now, to answer your specific question, for the ground force replacement, the actual training period is 15 weeks. We recently cut it down from 17. We had 13 weeks originally and were able to work it up to 17, and then, due to the fact in January we had some heavy calls we had to meet, we reduced it to 15 weeks. The man must be inducted and go through processing and then he has 15 weeks training, and some take longer than that.

Senator HILL. Those who do not show themselves proficient are turned back.

General HANDY. Yes.

The CHAIRMAN. This comes to us very often, General. Will you explain why the exceptions are made and how it happens that a man almost as soon as he is inducted is rushed over because he belongs to a certain unit and fills a place in it?

General HANDY. Those cases that have gone over rather quickly are Infantry replacements. That has been the big difficulty, and 90 percent of our ground losses have been in the Infantry, and they have had to be replaced quickly and by young men. These young men are the ones who are suitable and the only ones who can stand the gaff. I imagine some men have been gotten over there in less than 6 months, but the average time I would say would be at least 6 months before we get a man to the front.

Mr. THOMAS of Utah. Mr. President, I thank the Senator from South Carolina.

I cannot add much to what General Irvine has said or to the statement the Senator from South Carolina has had inserted in the RECORD. Of course, it is unfortunate that we have reached such a point in the war that at times it is necessary to use men who have not had all the training they should have had. If Senators will keep in mind what replacement means in the Army, I think they will realize that no matter how well a plan may be made there will be exceptions to it. Not only must there be replacements of individuals in a given unit but there must also be replacement of units by other units. In that way individual soldiers find themselves in a unit of which they become so much a part of the team or group that to remove them would be fatal to the efficient operation of the unit and would be contrary to the best tactics and the most efficient way of conducting the operations of the Army.

I know it goes without saying that the Senate was most loath to adopt the amendment to the Selective Training and Service Act which reduced the age of selectees from 20 to 18 years. We had long hearings with regard to that matter. We were told, as the Senator from Ohio [Mr. TAFT] has stated, that, of course the aim would always be to give all the training which could be given before the men entered actual combat. Such training will always be desired by all right-thinking officers, because it will mean a better army and a better chance for success.

The things which have been done have been done because of the necessities of the situation. Sad to relate, due to the way the war is going, probably there will be many more occasions when it will be necessary to depart from the ordinary method of procedure. The Senator from Massachusetts stated that, of course, we cannot ever satisfy the parents. I do not know whether there is ever a satisfactory explanation for any losses in war, except, perhaps, those for which soldiers are honored or losses incident to the cause they serve when they offer themselves for their country and make the supreme sacrifice. Everyone knows that if officers of the Army or Navy were derelict in their duty and were not thoughtful of the welfare of the men under them, such officers would immediately be removed. Although the present war is the most terrible of all wars which have ever been fought, undoubtedly it can be said without fear of contradiction that in the present war the officers are more thoughtful of the welfare of their men than officers have ever been able to be in any other war. I think that statement should be made, and that we should have that much of an understanding. I am sure the Senator from Ohio has that understanding, and I am confident that there is no need for me to inform him of that situation.

Mr. TAFT. Mr. President, nothing which has been read or said denies the facts I stated. Today the facts are that soldiers who are inducted at 18 years of age are given 13 or 15 weeks' training immediately following their induction and then are shipped abroad as soon as they can be shipped, and as soon as they are abroad they are assigned to units which are engaged in combat at the front. Nothing which has been said denies that that is the case.

I think such a policy is wholly without justification. It seems to me that a unit with 90 men in it is no better off by having 10 new men who know nothing about combat sent to it as replacements. I think the new men should have a period of 2 or 3 months in training behind the lines until they are familiar with the operations of their unit and until they know what they are supposed to do.

I cannot conceive that our country, with 10,000,000 men in the Army, is unable to provide other men for replacements. However, if it is not able to do so, I think the various units are better off if they do not have new and comparatively untrained men sent to them as replacements when they are actually engaged in combat. Of course, the Army says it is not using such new men to make up entire units, but is using them simply as replacements in units previously formed.

I hold in my hand some 10 or 20 telegrams and letters which cite specific cases of men who have been assigned to combat duty after less than 7 months in the Army. I think that is in violation of the policy suggested by Secretary Patterson, and I think the Army should immediately revise it. If it is necessary to send them abroad so soon, very well; but I think that to send them into combat when they have had so little training is most unfair to the men, does no good to the Army, and certainly is in violation of the principles laid down by the Senate, at least, when it revised the Selective Training and Service Act. I think the Army could revise that policy and still exercise due care, and I very much hope the Army will do so.

REGULATION OF THE BUSINESS OF INSURANCE—CONFERENCE REPORT

The Senate resumed the consideration of the report of the committee of conference on the disagreeing votes of the two Houses on the amendments of the House to the bill (S. 340) to express the intent of the Congress with reference to the regulation of the business of insurance.

The PRESIDENT pro tempore. The question is on agreeing to the report.

Mr. PEPPER. Mr. President, I do not wish to delay the Senate, but I desire to speak briefly about the pending conference report on the insurance bill, and there will have to be a vote upon it. So I suggest the absence of a quorum. Perhaps the roll can be called quickly, but I wish to have as many Senators as possible present.

The PRESIDENT pro tempore. The clerk will call the roll.

The legislative clerk called the roll, and the following Senators answered to their names:

Aiken	Gurney	Overton
Bailey	Hart	Pepper
Ball	Hatch	Radcliffe
Bankhead	Hawkes	Reed
Barkley	Hayden	Revercomb
Bilbo	Hickenlooper	Robertson
Brewster	Hill	Russell
Bridges	Hoey	Saltonstall
Buck	Johnson, Calif.	Shipstead
Burton	Johnson, Colo.	Smith
Bushfield	Johnston, S. C.	Stewart
Butler	Kilgore	Taft
Byrd	La Follette	Taylor
Capehart	Langer	Thomas, Okla.
Capper	McCarran	Thomas, Utah
Chandler	McFarland	Tobey
Chavez	McKellar	Tunnell
Cordon	McMahon	Tydings
Donnell	Maybank	Vandenberg
Downey	Mead	Wagner
Eastland	Millikin	Walsh
Ellender	Moore	Wheeler
Ferguson	Morse	Wherry
Fulbright	Murdock	White
George	Murray	Wiley
Gerry	Myers	Willis
Green	O'Daniel	Wilson
Guffey	O'Mahoney	

The PRESIDING OFFICER (Mr. MAYBANK in the chair). Eighty-three Senators have answered to their names. A quorum is present.

Mr. PEPPER. Mr. President, if I may have the attention of the Senate for only a few minutes, I promise not to trespass unreasonably upon its patience.

We all know that last June, in the Southeastern Underwriters case, the Supreme Court of the United States held that the insurance business came within the interstate commerce clause of the Constitution, and that therefore the Clayton Act and the Sherman Antitrust Act were applicable to such business.

Mr. President, an effort was made by Senators and Representatives while this case was pending in the Supreme Court to enact legislation which would have explicitly exempted the insurance business from the applicability of the Sherman and Clayton Acts. However, the legislation which had been submitted was not adopted by the Senate, although, I believe, it was adopted by the House. After the decision of the Supreme Court holding that insurance is interstate commerce within the meaning of the commerce clause of the Constitution, legislation has been initiated in both Houses

of the Congress to affect in one way or another the Supreme Court's decision. I feel that the adoption of the conference report which embodies such legislation would have the effect of emasculating the Supreme Court's decision, and holding by congressional action that the Sherman and the Clayton Acts do not apply for all practical purposes to the business of insurance. That is the exact point to which I wish to address myself.

The exact language to which I wish to direct criticism appears in section 2 (b) of the conference report now lying on the desks of Senators, and reading as follows:

Provided, That after January 1, 1948, the act of July 2, 1890, as amended, known as the Sherman Act, and the act of October 15, 1914, as amended, known as the Clayton Act, and the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

I am not complaining about any other provision of the conference report. In other sections of the conference report it is provided that the States shall have the power to regulate and tax the business of insurance. I am not complaining about that. In another part of the conference report it is provided that there shall be an unqualified moratorium on the applicability of the Sherman Act, the Clayton Act, the Federal Trade Commission Act, and the Robinson-Patman Antidiscrimination Act to the business of insurance until January 1, 1948. In other words, none of those four Federal acts would be applicable to the business of insurance until January 1, 1948. That would be a longer moratorium than the President, in two letters to which I will refer, indicated he would prefer, but I am not complaining even about a 3-year moratorium. There is considerable justification for the States being given an opportunity to modify their laws respecting the insurance business so that they shall not be in conflict with the four Federal acts enumerated in the provision to which I have referred. But I do object, Mr. President—and I believe the Senate, when it reflects upon the matter, will object—to the provision which I read providing that for all future time the Sherman Act, the Clayton Act, and the Federal Trade Commission Act shall not apply to the business of insurance except in a State which has not regulated the insurance business or to the extent a State has not denied the effect of such Federal acts.

Mr. President, if that language had contained the limitation that the State regulation, in order to be valid, must not be inconsistent with the Clayton Act or the Sherman Act, I should have no objection to it. But under the language which I have read, and to which I am addressing my criticism, namely, that the Sherman Act, the Clayton Act, and the Federal Trade Commission Act shall be applicable to the business of insurance to the extent that such business is not regulated by State law, the State would be given the right to determine when, whether, and to what degree those three acts were applicable to the business of insurance. The various States, without any limitation upon their power, or without any requirement that State regulation shall not be inconsistent with the Sherman Act, the Clayton Act, and the Federal Trade Commission Act——

Mr. McCARRAN. Mr. President, will the Senator yield?

Mr. PEPPER. I yield.

Mr. McCARRAN. The Senator undoubtedly recognizes the fact that the Congress of the United States would not attempt to tell a State how and upon what subject it should legislate. The Senator will agree with that statement, will he not?

Mr. PEPPER. On the contrary, Mr. President, I may say that I am not willing to leave the applicability and the effectiveness of the Sherman Act and the Clayton Act to the decision of a State legislature. By doing so the Congress would be abrogating its power with respect to the subject exclusively to the several legislatures, that is, if we pass this law without imposing any limitation upon the States in the exercise of their regulatory power that it must be not inconsistent with the Clayton Act or the Sherman Act.

Mr. McCARRAN. Under the provisions of the section in the conference report to which the Senator addresses himself, the States are advised and warned that they have a moratorium of 3 years during which they may bring themselves into compliance by way of regulation. If at the end of the 3 years they have not brought themselves into compliance, if they have not regulated the business of insurance, then they must take the consequences because after that period is over the Sherman Act and the Clayton Act and the other acts become immediately again in force as regards the business of insurance. That is all there is to that provision.

Mr. PEPPER. Mr. President, I realize that, but will the Senator tell the Senate if I am not correct in saying that under the conference report provision to which I referred the States can regulate the business of insurance in a way inconsistent with the Sherman Act and the Clayton Act.

Mr. McCARRAN. If they do it, they do it at their own hazard.

Mr. PEPPER. What does the Senator mean by "their own hazard"?

Mr. McCARRAN. Congress has always the power over interstate commerce.

Mr. PEPPER. The Senator means we may change the law.

Mr. McCARRAN. The States cannot take the Congress out of a position where it can regulate interstate commerce.

Mr. PEPPER. We have taken ourselves out of that position in this case.

Mr. McCARRAN. We have done so for 10 years.

Mr. PEPPER. Oh, no; that is a question of fact. What I want to say—and I should like to have the Senator address himself to this point—is that when this bill passed the Senate it contained an absolute 3-year moratorium; when it passed the House it contained a 3-year moratorium, and there was nothing in it which suggested the language to which I now object—and I should like to make this very clear:

Provided, That after January 1, 1948, the act of July 2, 1890, as amended, known as the Sherman Act, and the act of October 15, 1914, as amended, known as the Clayton Act, and the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

That is new language, which was put in by the conference committee. It did not appear in the Senate bill; it did not appear in the House bill, and were it not for our broad interpretation of the power of conferees when the text of a Senate bill is stricken out and an entirely new bill inserted by the other House conferees may practically rewrite a bill, that provision would be outside the scope of the authority of the conferees.

Mr. McCARRAN. Let me say to the Senator the language which he has just read to the Senate was put in by the conferees within the scope of their authority, and if it did anything it made more airtight the very provision the Senate had passed in the first instance and which the House had also passed.

Mr. PEPPER. Mr. President, I respectfully disagree with my able friend, and I should like to state why. Here is the language of the Senate bill as passed by the Senate:

That the Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

Then the Senate bill went on to provide:

No act of Congress, except * * * the Sherman Act and/or the Clayton Act shall be construed to invalidate, impair, or supersede any law enacted by any State or for the purpose of regulating the business of insurance.

Then it proceeds further:

Nothing contained in the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, or the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall apply to the business of insurance.

Then it goes on to provide a 3-year flat moratorium.

But, Mr. President, nowhere in the Senate bill and nowhere in the House bill is there any authority to the States to prevent the applicability of the Sherman Act and the Clayton Act after 3 years to the business of insurance in the States. That is the vice of the provision to which I am now referring.

Mr. O'MAHONEY. Mr. President, will the Senator yield?

Mr. PEPPER. If the Senator will permit me to proceed for a few moments, then I will yield.

Now, Mr. President, I wish to read two letters from the President to the Senator from Maryland [Mr. RADCLIFFE] affecting this subject, which will point out the distinction I am trying to make in what I have to say. On the 10th of June in response to a letter from the able Senator from Maryland to him, as appears

on page 482 of the RECORD of January 25 of this year, the President replied to the able Senator from Maryland as follows:

MY DEAR SENATOR RADCLIFFE: I have your letter of June 6 with respect to the recent decision of the Supreme Court deciding that insurance comes under the provisions of the Sherman Act. You suggest that this would probably mean supervision by the Federal Government.

The Attorney General advises me that he does not believe that this alternative is inevitable or even probable. He tells me that there is nothing in the decision which prevents the regulation by the States of insurance rates as long as that regulation does not interfere with the provisions of the Sherman Act.

As long as that regulation does not interfere with the Sherman Act.

Personally, I know of no effort at this time to bring insurance companies under over-all Federal regulation. Whether or not such control were adopted would depend, I think, very much on the attitude of the companies themselves in complying with the provisions of the Sherman Act.

The Attorney General assures me that he is anxious that the insurance companies and the State insurance officials shall have a reasonable time within which to conform their practices and statutes to the decision of the Supreme Court.

With best regards, always,

Very sincerely yours,

FRANKLIN D. ROOSEVELT.

The President said there that he was in favor of a moratorium to give the States time to do what? To bring their laws into conformity with the Sherman Act and the Clayton Act.

The second letter from the President dated January 2, 1945—the other letter was dated June 10, 1944—and addressed like the first letter, to the able Senator from Maryland, is as follows:

MY DEAR SENATOR RADCLIFFE: In your letter of December 20, you suggest that there should be some form of a moratorium during which insurance companies will have an opportunity to readjust their practices in order to bring them into conformity with the Supreme Court decision in the Southeastern Underwriters Association case, and during which legislation might be enacted. The Attorney General advises me that several months ago he told the Senate Judiciary Committee that no new antitrust prosecutions against insurance companies would be instituted during a reasonable readjustment period.

The responsibility for the regulation of the business of insurance has been left with the States; and I can assure you that this administration is not sponsoring Federal legislation to regulate insurance or to interfere with the continued regulation and taxation by the States of the business of insurance.

I call the attention of Senators to this sentence:

But there is no conflict between the application of the antitrust laws and effective State regulation of insurance companies, and there is no valid reason for giving any special exemption from the antitrust laws to the business of insurance. The antitrust laws prohibit private rate fixing arrangements between insurance companies and acts of boycott, coercion, or intimidation. The antitrust laws do not conflict with affirmative regulation of insurance by the States such as agreed insurance rates if they are affirmatively approved by State officials.

Senator O'MAHONEY introduced a bill in the last Congress which would have provided for a moratorium from the Sherman Act, except for acts of boycott, coercion, or intimidation, until March 1, 1946. This would appear to give sufficient time to permit the necessary readjustment to the Supreme Court decision. I would favor legislation of this general character. It would permit the orderly correction of abuses which have existed in the insurance business and would preserve the right of the States to regulate with full responsibility.

Very sincerely yours,

FRANKLIN D. ROOSEVELT.

Mr. President, those two letters indicate the point that I am trying to make at the present time, namely, that the President thought that it was proper to give the insurance companies time to readjust to the decision of the Supreme Court and to give the States time to adjust their laws so that they would be in conformity with the Sherman Act and the Clayton Act. The President never contemplated and the Senator from Wyoming [Mr. O'MAHONEY] in the bill he introduced, as I understood his able address, never contemplated that the regulation by the States should be so broad in character that it could be in conflict with and in limitation of the provisions of the Sherman Act and the Clayton Act.

The Senate, when it passed this bill, provided for a moratorium, which is all right. It was longer than the President seemed to indicate, but no one raised any question about the moratorium being 3 years. The House carried the same provision and provided a 3-year moratorium, and I am not complaining about that, and if the conferees had not changed the provisions of the Senate bill and the House bill, but had put in everything they have in this conference report, leaving 3 years as the absolute moratorium during which these laws could not apply, I should be willing to accede to that. But the language to which I object is the language which I read in the conference report, which carries, not a 3-year moratorium, but a perpetual moratorium. This is the language to which I object:

Provided, That after January 1, 1948, the act of July 2, 1890, as amended, known as the Sherman Act, and the act of October 15, 1914, as amended, known as the Clayton Act, and the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

Mr. RUSSELL. Mr. President——

Mr. PEPPER. If the Senator will allow me another minute, I shall lay a predicate I should like to have him discuss, if he would like to do so.

This is my contention, that under that provision we have given to the States the power to preempt the field covered at the present time by the Sherman Act and the Clayton Act. If the States move into that field, if they occupy that territory, that, by the provisions of this report, makes the Sherman Act and the Clayton Act inapplicable to that extent. This is the way it would work out, in violation of the Sherman Act and the Clayton Act. The vice I complain of in the case which eventually reached the Supreme Court, and was decided by the Supreme Court, was the practice of the insurance companies in the Southeastern States of getting together in what they called rate bureaus. They come together and, for all practical purposes, it was charged in the indictments, they fixed rates in all the Southern States of this country, one of which happens to be my State.

What was the effect of that policy? From the decision of the Supreme Court itself I have it—and I am reading from the language of the Supreme Court on page 542, of Three hundred and twenty-second United States:

During the period 1931-41 a total of $488,000,000 in premiums were collected by local agents in the six States, most of which was transmitted to home offices in other States; while during the same period—

Ten years—

$215,000,000 in losses was paid by checks or drafts sent from the home offices to the companies' local agents for delivery to the policyholders.

That means that in those Southern States affected by the decision, in a 10-year period, these stock fire-insurance companies collected in premiums $488,000,000 and paid out $215,000,000.

Mr. President, in my State of Florida—and these figures are furnished me by the Department of Justice—in the period from 1931 to 1940 these stock fire companies received in net premiums written $89,191,740. The losses paid in Florida in the same period of 10 years were $30,215,253; that is, $89,000,000 premiums received in 10 years in Florida, and $30,000,000 paid in losses, nearly three times as much received in premiums during the 10-year period in that one State by that particular group of companies covered by the indictment; and that was not all the companies doing business in the South during that time.

Mr. President, I am not an insurance man, and perhaps that sum is a reserve which should be created, but it seems to me that the vice in price fixing is there well illustrated, the vice of people who fix prices gouging excessive profits out of the people who pay the premiums. That is what they have been doing. They were indicted in the Southeastern Underwriters' case, and it was held that even if all these things charged were committed, nevertheless insurance was not commerce, and the Sherman Act and Clayton Act could not apply anyway.

In a monumental opinion that was written by Mr. Justice Black, the Supreme Court held that the insurance business as carried on at the present time is commerce within the meaning of the Federal Constitution, and therefore that the Sherman Act and the Clayton Act are applicable to that business, as they are applicable to all other businesses. They should be applicable to that business as to all other businesses. What right is there in an insurance company, per se, to have some sanctuary behind some immunity by which it may fix prices, may squeeze out a competitor, may commit monopoly, may combine with others in restraint of trade, and do all the other things prohibited by the Sherman Act and the Clayton Act, and

yet not be amenable to the law as all other business is? Yet, after the Supreme Court has made that monumental decision, I have very deep concern, Mr. President, and I believe the language of this conference report to which I have adverted bears it out, that a State could provide by statute that insurance companies may belong to a rating bureau, as they have been having one, and that that rating bureau may continue to fix rates, as they have been fixing rates, and the Clayton Act and the Sherman Act would not have any applicability against that offense they might attempt to commit.

Mr. O'MAHONEY. Mr. President——

The PRESIDING OFFICER. Does the Senator from Florida yield, and if so, to whom?

Mr. PEPPER. I yield first to the Senator from Wyoming, and then I shall yield to the Senator from Georgia.

Mr. O'MAHONEY. I sympathize very deeply with the concern which the Senator from Florida has expressed this morning lest anything should be done by the Congress which would enable private abuses to continue in the insurance field. I am convinced, however, that the apprehensions which the Senator states with respect to this conference report are not well founded.

I wish to call the Senator's attention to the Supreme Court decision in the case of Parker against Brown, reported in 317 United States Reports at page 341. Reading from page 350, I find this language:

> Section 1 of the Sherman Act (15 U. S. C., sec. 1) makes unlawful "every contract, combination * * * or conspiracy, in restraint of trade or commerce among the several States." And section 2 (15 U. S. C., sec. 2) makes it unlawful to monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States." We may assume for present purposes that the California prorate program—

Which was an agricultural program—

> would violate the Sherman Act if it were organized and made effective solely by virtue of a contract, combination or conspiracy of private persons, individual or corporate.

I take it that the Senator is apprehensive lest a statute passed by a State attempting to give validity to a private agreement to regulate would be recognized under this language. I think it would not, because on page 351 of the same case, Parker against Brown, I find this language from the Supreme Court:

> True, a State does not give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful (*Northern Securities Co. v. United States*, 193 U. S. 197, 332, 344-347).

Therefore I have no doubt in my own mind that no State, under the terms of the conference report, could give authority to violate the Sherman antitrust law. But we have this field in which definitions may be a little bit difficult and vague.

Mr. PEPPER. If the Senator will permit me on that point——

Mr. O'MAHONEY. Will the Senator allow me to conclude?

Mr. PEPPER. Very well.

Mr. O'MAHONEY. There has never been any doubt, so far as I have been able to discern, among those who have been taking the position which the Senator from Florida has taken on this insurance bill, that private agreements by which these rates were enforced were violations and are violations of the antitrust laws. There is nothing in the conference report that relieves insurance companies from the prohibition of the antitrust law, because there has been written back into the bill language which was taken out by the House which would have exempted agreements from the prohibition of the antitrust law. Therefore any attempt by a small group of insurance companies to enter into an agreement by which they would penalize any person or any business which was attempting to do business in the insurance field in a way that was disapproved by them, would be absolutely prohibited by this provision.

Mr. PEPPER. Let me reply to the able Senator. In the first place let me say that he and the able Senator from Utah [Mr. MURDOCK], who is on the Senate floor, have been perfectly splendid in their efforts to keep the United States Supreme Court decision from being emasculated by legislation. But may I address myself to the point which the Senator from Wyoming has made? The Senator cited the Parker against Brown case, which was a case where a State approved of apportionment of the field, and the question was whether or not these companies which complied with that State decision were guilty of violating the Sherman Act or the Clayton Act, and it was held that where the State approved by law what they did, that that was all right, or rather where the State itself determined that that was the thing to do, the companies were not violating the law.

But here is the difference between that case and what we are considering. That was a case which did not involve a Federal statute containing the language which I object to in the conference report, namely, that the Sherman Act and the Clayton Act shall be applicable to the business of insurance to the extent that such business is not regulated by State law. If the States regulate or legislate on the subject by saying that it is all right for insurance companies to belong to a rating bureau, and it is all right for the companies, through that rating bureau, to fix rates, then is not that State legislation on the subject? Is not that State regulation of the companies? Then it is not a question of whether that would give immunity against a Federal prosecution to those favorably affected by that regulation. It is a question of whether, under the language of the proposed statute which is embodied in the conference report, we do not legitimize any such regulation or any such legislation as that.

I admit I would be satisfied with the applicability of the Parker against Brown case, I will say to the Senator, if it were not for this language to which I am addressing myself. If only the rest of the language of the original bill were in there, and they were only given the right to regulate as they are given the right to do in the first part of this bill, then I am confident that the courts would hold that if they tried to legitimize a private agreement which per se violated the Sherman Act or the Clayton Act, that that would not be called regulation so as to protect them from prosecution.

But if we say—which we do say by the language, in my humble opinion—that if they preempt this field by regulating it by State legislation, then the Federal act shall not apply; there is not anything to prosecute. There is not any juridical question that is raised. We have then given them carte blanche to legislate on anything they want to, and have said that if they regulate, then we withdraw from the field to the extent that they have covered it, and if we legitimize a rate they have fixed in practice can anybody deny that they have covered the subject, that they have regulated the field, and that they have occupied the domain? If they have, then we have by our own act provided that the Sherman Act or the Clayton Act shall not have any effect in a case of that sort.

Mr. MURDOCK. Mr. President——

The PRESIDING OFFICER (Mr. DOWNEY in the chair). Does the Senator from Florida yield to the Senator from Utah?

Mr. PEPPER. I yield.

Mr. MURDOCK. The Senator in speaking of the language of the report indicates that it would permit absolute preemption of the field by the State, so far as regulation of insurance is concerned; that it would allow a State to repeal all its insurance laws and give carte blanche to insurance companies.

Mr. PEPPER. A State has the right, without any legislation, to regulate anything pertaining to the insurance business, and to the extent that it regulates it has legitimized in its regulations so far as these Federal acts are concerned, and by the proposed legislation we would give them the right to go as far toward cutting down or toward emasculating the Sherman Act and the Clayton Act as they choose to go. The able Senator from Utah in his argument concerning the legislative history of the bill on the 25th of January pointed out time after time that even the original bill to a considerable extent gave that authority, and then when there was some clarification of that in section 2 by the amendment of the Senator from Michigan [Mr. FERGUSON] to make the Sherman Act and the Clayton Act particularly applicable, then they came right back in the conference—no doubt unintentionally, but they came right back in the conference and in my opinion gave the States the right to do anything they wanted to do relative to regulation without any limitation that it must not be an encroachment upon the Sherman Act and the Clayton Act.

Mr. MURDOCK. If the Senator will permit, let us look at the legislative history. The Senate bill, after the amendment of the Senator from Michigan [Mr. FERGUSON] was included, made the Sherman Act and the Clayton Act applicable regardless of what the several States might do, except during the moratorium. When the bill went to the House that

language, the amendment of Senator FERGUSON was stricken out entirely. The conference report is a compromise certainly between the position taken by the Senator from Florida and the position taken by, let us say, the proponents of the Bailey bill. But certainly the language here is sufficient, and if I did not think so I would not support the measure to protect Congress in any future action it might take in the event of failure by the respective States to adequately regulate the business of insurance. The language I refer to reads as follows:

> Shall be applicable—

Referring to the Sherman Act and the Clayton Act—

> to the business of insurance to the extent that such business is not regulated by State law.

Does the Senator take the position that the States could absolutely repeal all their insurance laws and still be regulating insurance?

Mr. PEPPER. Well, if they repeal the laws and had no regulation, of course, that would not be regulation.

Mr. MURDOCK. That would not be regulation. If the Senator will permit me, let us take the next step. Let us say that they do regulate, but that their regulations were in conflict with the Sherman Act and the Clayton Act or permitted actions or activities violative of those acts. Would the Senator say that by reason of the fact that they had so regulated, such regulation removed the insurance business in that State from the application of the Sherman Act and the Clayton Act?

Mr. PEPPER. If the Senator were to read on paper what he has just asked me, he would see that in his hypothesis he assumes that the State regulation was not in conflict with the Sherman Act and the Clayton Act I am only speaking, I will say to my friend, about the case where State regulation invades the domain of the Sherman Act and the Clayton Act, and after the Senator states his opinion I should like the Senator from Michigan, who handled this bill, to advise the Senate whether or not under this language to which I am objecting it is possible for a State by its own regulation to curb and cut down the extent and the effect and the applicability of the Sherman Act and the Clayton Act.

Mr. FERGUSON. I am glad to answer that question.

Mr. PEPPER. Is that possible under this language?

Mr. FERGUSON Under the language which is now in the bill as it appears in the conference report, if a State passes an act regulating insurance or taxing insurance, and that regulation is contrary to the Sherman Act or the Clayton Act, with three exceptions, then the State law would be the law. Here are the exceptions:

> Nothing contained in this act shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

In other words, under the terms of the bill, there are six things on which a State could not legislate. They are boycott, coercion, or intimidation, or agreements to boycott, coerce, or intimidate. But with respect to anything else, if the States were specifically to legislate upon a particular point, and that legislation were contrary to the Sherman Act, the Clayton Act, or the Federal Trade Commission Act, then the State law would be binding. That is exactly what we attempted to do in the bill. It is clear what we intended to do. After a conference with the House, we believed that the States should regulate insurance, and taxation on the insurance business. But we spelled out certain things on which we thought Congress should not allow the States to legislate. Those are the things which I have mentioned. As to the others, the State has full power to act by legislation—not by agreement but by legislative act. The Senator from Florida was talking about an agreement which related to many States. This bill would not permit such an agreement, because no State law could allow a monopoly to exist outside the State.

Mr. PEPPER. I thank the able Senator for his clarity and candor. Let me ask the Senator a question. Suppose the State of Florida, through its legislature, were to provide that insurance companies may belong to a rating bureau, the headquarters of which is in Atlanta, and that such rating bureau may be the instrumentality through which rates are fixed, and that those rates, when fixed, shall be applicable within the State of Florida. Would the State legislature have authority to do that under the language to which I am addressing myself?

Mr. FERGUSON. This bill would permit—and I think it is fair to say that it is intended to permit—rating bureaus, because in the last session we passed a bill for the District of Columbia allowing rating. What we saw as wrong was the fixing of rates without statutory authority in the States; but we believe that State rights should permit a State to say that it believes in a rating bureau. I think the insurance companies have convinced many members of the legislature that we cannot have open competition in fixing rates on insurance. If we do, we shall have chaos. There will be failures, and failures always follow losses.

The sale of insurance is not the same as the sale of an article in a store. When one buys an article in a store, he brings it home with him. In the case of insurance, he buys a promise to pay upon the happening of a certain event, and that event may be the burning of his home. If the company is not sound and solvent at the time the house burns, or at the time claim is made, there is no insurance at all. That is what we have tried to avoid.

Mr. PEPPER. In other words, the Senator believes in a form of rate fixing?

Mr. FERGUSON. Yes. There is no doubt that the bill allows it; but we believe that all the wisdom is not here in Congress. We believe that there is some wisdom left in the legislatures of the various States, and that they should exercise their judgment and regulate insurance, except in the respects which we have enumerated.

Mr. PEPPER. Mr. President, the able Senator has made a good argument for price fixing and rate fixing. The same argument could be made for cartels. The same argument could be made for price fixing in the lumber industry or the steel industry. The people engaged in those industries are not criminals. When they fix prices, they believe that it is a good thing for the industry. Many of them believe that price fixing is a good thing for the country. But the Clayton Act and the Sherman Act have put the Government of the United States on record against price fixing. We are rapidly going on record against cartels. We believe in a system of free enterprise which will give business the right and duty to compete upon a fair basis. That is the American way, Mr. President.

The able Senator from Michigan has been very candid. It is intended by the proponents of this measure that the right of rate-fixing shall be preserved. The Senator has said that if rates are fixed by a rating bureau, and if the State legislation legitimizes that practice, it is intended by the language to which I have referred to approve it.

Mr. MURDOCK. Mr. President, will the Senator yield?

Mr. PEPPER. I yield.

Mr. MURDOCK. If we were to move completely out of the field, I could probably agree with the Senator. But, in my opinion, the first sentence in subsection (b) of section 2 is the answer. It reads as follows:

> No act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such act specifically relates to the business of insurance.

We were confronted in the Senate and in the House, not with a theory but with a fact. We were confronted with a choice between the Bailey bill or something better. I believe that while the conference report does not wholly satisfy me, it is better than the Bailey bill.

Let us assume that the State does the very thing which the Senator from Florida says it may do in order to permit rate making. According to the Senator from Michigan, under State regulation the States permit rate making by the companies. Suppose the Congress thinks that the States have gone too far. Let us assume that the Congress construes such action to be a deliberate attempt to get out from under the beneficial provisions of the Clayton Act and the Sherman Act. If the conference report were agreed to, the Congress would not entirely give up the field. The Congress would still retain the power—if it needed to be retained—by an act specifically relating to insurance, to invalidate an objectionable regulation on the part of the State. Such regulation would be superseded, in my opinion, by affirmative action by Congress on the same subject. Does not that answer the Senator's question?

Mr. PEPPER. The able Senator is absolutely correct in saying that under the decision of the United States Supreme Court the Congress has the authority to

regulate the business of insurance as interstate commerce. We may withdraw the leave we grant to the States to limit, impair, curtail, or defeat the Clayton Act and the Sherman Act, except in respect to boycott, intimidation, or coercion. We can withdraw the power we give to the States; but I raise the question, Mr. President. Why give away the power in the first place?

Let me read the brief letter from the President, to show how clearly he saw this issue. In reply to a letter from the able Senator from Maryland [Mr. RADCLIFFE] he said——

Mr. MURDOCK. Mr. President, before the Senator reads the letter, let me ask him a question. Does the Senator believe that the President of the United States was fully apprised as to the trend in the Congress of the United States, and as to the attitude of a majority of Congress on this subject? That is the problem with which we in the Judiciary Committee were confronted.

Mr. PEPPER. Of course, I cannot comment upon that point, because I am not advised; but let me read again the language of the President in his letter to the able Senator from Maryland. The letter is dated June 10, 1944:

> MY DEAR SENATOR RADCLIFFE: I have your letter of June 6 with respect to the recent decision of the Supreme Court deciding that insurance comes under the provisions of the Sherman Act. You suggest that this would probably mean supervision by the Federal Government.
>
> The Attorney General advises me that he does not believe that this alternative is inevitable or even probable. He tells me that there is nothing in the decision which prevents the regulation by the States of insurance rates as long as that regulation does not interfere with the provisions of the Sherman Act.
>
> Personally, I know of no effort at this time to bring insurance companies under over-all Federal regulation. Whether or not such control were adopted would depend, I think, very much on the attitude of the companies themselves in complying with the provisions of the Sherman Act.
>
> The Attorney General assures me that he is anxious that the insurance companies and the State insurance officials shall have a reasonable time within which to conform their practices and statutes to the decision of the Supreme Court.

That means bringing them into harmony with the Sherman Act and the Clayton Act. That is the bill which the Senate passed.

I have the bill before me. I could read it to the Senate. As the Senate passed the bill it carried out the thought I have mentioned, except it provided for a moratorium of 3 years, during which the insurance officials and insurance companies could square their conduct and their regulations with the Sherman Act and the Clayton Act. That is the bill the House passed. I wish to read to the Senate the report of the House managers to show that in their report to their own body they did not intimate any such provision as the one about which I am complaining today. As one reads the report he would think that the bill was as passed by the Senate. It permitted them to regulate. It provided for a 3-year moratorium and provided that after the 3 years had elapsed the antitrust laws were absolutely to go back into effect.

I read the statement of the managers on the part of the House:

STATEMENT OF THE MANAGERS ON THE PART OF THE HOUSE

> The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendment of the House to the bill (S. 340) to express the intent of the Congress with reference to the regulation of the business of insurance, submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report.
>
> The House amendment struck out all of the Senate bill after the enacting clause. The committee of conference recommends that the Senate recede from its disagreement to the amendment of the House with an amendment which is a substitute for both the Senate bill and the House amendment, and that the House agree to the same.
>
> It was the purpose on the part of the managers of the House to have the agreement between themselves and the managers on the part of the Senate to state in as clear language as possible that a moratorium be granted to the insurance business from the operation of the act of July 2, 1890, as amended, known as the Sherman Act, and the act of October 15, 1914, as amended, known as the Clayton Act, and the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, until January 1, 1948, leaving the taxing and regulatory powers of the several States fully protected.

They mean within the 3-year moratorium.

I read further from the statement:

> The principal difference between the conference report and the bill as it passed the House lies in the inclusion of the act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the act of June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, in the moratorium provision, and making clear the intention of the Congress that the acts of boycott, coercion, and intimidation are subject to the operation of the suspended statutes even during the moratorium period.
>
> HATTON W. SUMNERS,
> FRANCIS E. WALTER,
> C. E. HANCOCK,
> *Managers on the part of the House.*

What do they say? They say they are reporting to the House the bill about insurance, with the understanding that the Sherman Act and the Clayton Act will *go into full effect*, but *only after* an intervening moratorium period of 3 years, and that during that 3-year moratorium the States will be able to pass any legislation they wish to pass insofar as the Clayton Act, the Sherman Act, and the other mentioned acts are relevant, with the exception of legislation pertaining to the boycott, coercion, and intimidation sections.

They state that with the exception of such legislation, during the 3-year period the States can do anything they wish to do—but with the clear implication that after the 3 years have elapsed the Sherman Act, the Clayton Act, and the decision of the United States Supreme Court will go into full force and effect.

But the conference report added a matter to which no reference is made in that statement. The conference report added the language to which I object, as follows:

> Provided, That after January 1, 1948, the Act of July 2—

In other words, the Sherman Act, the Clayton Act, and Federal Trade Commission Act, and so forth—

> shall be applicable—

And we must realize that that will be after the moratorium period—

> to the business of insurance to the extent that such business is not regulated by State law.

The Senate has heard the able Senator from Michigan say that regulation by State law may mean any degree of encroachment upon the Sherman Act and the Clayton Act which a legislature may desire to exercise, except with respect to the coercion, intimidation, and boycott sections.

Mr. MURDOCK. Mr. President, will the Senator yield?

Mr. PEPPER. I yield.

Mr. MURDOCK. Is there any question, after reading the President's letter, that what the President contemplated was that the States would be given an opportunity to regulate the insurance business? The President's letter contemplates that; does it not?

Mr. PEPPER. Yes—but not inconsistently with the Sherman Act.

Mr. MURDOCK. Very well. Let us take the Senator's position on that point. The President did contemplate affirmative regulation by the States; did he not?

Mr. PEPPER. That is correct.

Mr. MURDOCK. All right. Let us take the next step. They cannot do that if the Congress of the United States preempts the field; can they?

Mr. PEPPER. That is correct.

Mr. MURDOCK. And is it not a reasonable thing for the Congress to do; and is it not even expedient for the Congress to say to the States that we do trust them to a certain extent, and, as the able Senator from Michigan expressed it, we recognize that all wisdom is not lodged in the Congress of the United States. If we believe—and I think the great majority of the Congress do so believe—that the regulation of insurance should continue under State regulation, then why not be willing to give the States within the 3-year period an opportunity to step into the field, and also why not be willing to have confidence that the States will do a good job when they step into it?

Now we come back to the first sentence of the language to which the Senator from Florida has referred. If we find that they have not done it, if we find that they have tried to evade and circumvent and get away from the Sherman Act and the Clayton Act, the Congress will still be in a position to step in and undo everything they have done; will it not?

Mr. PEPPER. Mr. President, the reason why I cannot agree with my able friend the Senator from Utah is because I believe in the Sherman Act and the Clayton Act.

Mr. MURDOCK. I do, too.

Mr. PEPPER. That is the reason why I am not willing to give the States the

power pro tanto to repeal or invalidate either one of those acts, and that is what the language to which I am addressing myself would permit them to do, as stated very candidly, ably, and clearly by the able Senator from Michigan.

I am opposed to that. I do not see any reason for giving them the authority to do it in the first place, and then saying, "We will take it away from you at some subsequent time." Why not let the Congress preserve the integrity of the Sherman Act and the Clayton Act and of the monumental decision of the Supreme Court of the United States by simply providing, "We will give you a 3-year moratorium period, but after the 3-year moratorium the Clayton Act and the Sherman Act will go into full force and effect"?

Mr. McCARRAN. Why give them a 3-year moratorium at all, then? Why not say there will be no such legislation?

Mr. PEPPER. All right; I will reply to that question. It is because in the opinion of some—and I am not quarreling with them—the States should have some opportunity to adjust their regulatory legislation to square with the Sherman Act and the Clayton Act.

Mr. McCARRAN. But if they did, the Sherman Act and the Clayton Act would not impinge; is not that correct?

Mr. PEPPER. If we cut it down to conformity with the Sherman Act and the Clayton Act, then they would not impinge. But I am not talking about the period within the 3-year moratorium. Under the language of the conference report to which I have adverted, after the 3-year moratorium period, as the Senator from Michigan has pointed out, they can curtail by State legislation the Sherman Act and the Clayton Act to any degree that they desire to do so, except as respects the boycott, coercion, and intimidation sections.

Mr. RADCLIFFE and Mr. MURDOCK addressed the Chair.

The PRESIDING OFFICER (Mr. La FOLLETTE in the chair). Does the Senator from Florida yield; and if so, to whom?

Mr. PEPPER. I yield first to the Senator from Maryland.

Mr. RADCLIFFE. Mr. President, I do not share the lack of confidence which the Senator from Florida has in State regulation. We have seen an enormous industry—the insurance industry—built up in the last 100 years, to be one of the biggest industries in this country. On the whole it has been constructed soundly. We know that a few years ago when the depression was with us, with all of its terrors and calamities, and when many other forms of business were rocked to their foundations, the insurance business as a whole remained sound. One of the greatest blessings we had during those distressing days was that the insurance business did stand stanch and weathered safely the financial cataclysm.

Do not forget that the insurance industry was under State regulation. When we attempt to consider what may happen we must not ignore the fact that State regulation has resulted in the development of a tremendous industry which is vital to the welfare of the people of the country. I believe that any attitude of mind which assumes that the States, after having on the whole very wisely and very securely built up a great business, would now take advantage of an opportunity to misuse and abuse their trust is a reflection on State administration and is entirely unwarranted.

Under the conference report the States would have certain opportunities to regulate. There are special reasons why that should be done. However, they would be given such a real opportunity. If they have acted well in the past, why is it not reasonable now to show some confidence in them with respect to the future? If they should attempt to enact any laws which would permit boycotting or unjust discrimination, this bill would intervene and prevent. If the Congress of the United States should feel at any time that its confidence had been misplaced, the Federal Government could step in.

In regard to the rating bureaus, I may say that some companies utilize them and some do not under existing laws and regulations.

Allow me to remind the Senator from Florida of one characteristic of the insurance business. An insurance company can be organized very quickly. It does not require an enormous plant, as does the steel business, for instance, or use of special materials. Whenever an insurance company acquires profits which seem to be excessive, or whenever an apparent opportunity is afforded to make money in the insurance business, a new insurance company is likely to come into existence. And such a course would continue under this act. Whether a new or old company desires to go under a rating bureau or not will be decided by its management. I do not believe that it is necessary for us at this time to assume that the States will run out on their obligations and treat the act as waste paper. I hope the conference report will be adopted.

Mr. PEPPER. Mr. President, if we do not expect the States in their regulation to encroach upon the Sherman Act and the Clayton Act, why give them authority to do so? If we believe in the Sherman Act and the Clayton Act, why should we delegate to State legislatures the right to cloud them and curtail their effectiveness should they wish to do so?

Mr. O'MAHONEY. Mr. President, will the Senator yield?

Mr. PEPPER. I yield.

Mr. O'MAHONEY. I should like to answer the Senator's question specifically. First, however, the matter is not a theoretical one. It is an extraordinarily practical matter. I am viewing it from the point of view of a person who has lived with the problem of State and Federal regulation almost from the moment the original bill to exempt insurance from all aspects of the antitrust laws was introduced.

Mr. President, there are three forms of regulation. There is State regulation, concerning which the Senator from Maryland has spoken so clearly. There is Federal regulation as a legal possibility, but no one is urging it now.

The third, and this has been harmful to the public interest, is regulation by private combinations and groups; a type of regulation which has been enforced by private combinations and groups through private rules and regulations under which persons engaged in the insurance industry could be tried and convicted for the violation of private law. That type of regulation would be absolutely outlawed should the conference report be adopted.

Mr. PEPPER. Not if the State legislatures decided otherwise.

Mr. O'MAHONEY. Mr. President, there is not a line or sentence in the proposed act, as I have read it, which would delegate to any State the power to legislate in the field of interstate and foreign commerce. State regulation must be for the State and not for the United States. The bill does not sacrifice the power of Congress to regulate in the field of interstate commerce, but, wisely, it seems to me, undertakes to say in effect to the State, "For this period take the responsibility and regulate insurance in the interest of the public."

Mr. PEPPER. Not for this period; but indefinitely.

Mr. O'MAHONEY. For this period so far as the antitrust laws are concerned, it would be a moratorium.

Mr. PEPPER. Oh, we are not talking about a moratorium; we are talking about the period beyond the moratorium.

Mr. O'MAHONEY. Mr. President, the Senator cannot separate his interpretation of the conference report from the word "moratorium." It is the purpose of the proposed act to grant a moratorium. It would be an absurd construction to say that in one section of the law a moratorium is provided, but in another section it is provided that there shall be no moratorium.

Within its own boundaries the State may authorize agreements for rate making just as the Congress of the United States, by passing the Interstate Commerce Act, authorized rate making by combinations in the railroad field, and just as practically every State in the Union has authorized public utility rate making within the States. But what I wish to say to the Senator from Florida, and to other Senators as well, without any reservation, is this: When the moratorium period passes, the Sherman Act, the Clayton Act, and the Federal Trade Commission Act come to life again in the field of interstate commerce, and in the field of interstate regulation. Nothing in the proposed law would authorize a State to try to regulate for other States, or authorize any private group or association to regulate in the field of interstate commerce.

Mr. PEPPER. Mr. President, I should like to clarify in my mind the Senator's distinction. The able Senator from Michigan said a moment ago, in response to my invitation, that if the insurance companies doing business in the Southeastern States were to fix their rates through a rating bureau centered in Atlanta, and if they applied in the State of Florida for the rates which had been fixed, but did so by authority of the State Legislature of Florida, it would be consistent with this proposed act, and

would be lawful. Am I correct in my statement?

Mr. FERGUSON. Mr. President, will the Senator yield?

The PRESIDING OFFICER (Mr. La Follette in the chair). Does the Senator from Florida yield to the Senator from Michigan?

Mr. PEPPER. I yield. I invite the able Senator from Michigan to state whether I was correct in my statement.

Mr. FERGUSON. If the Senator's statement was that the proposed act would permit a State to regulate interstate commerce—insurance is interstate commerce—in the various States, the State could not do it.

Mr. PEPPER. No one is claiming that. I am asking the Senator whether or not, under the conference report it would be lawful for the State of Florida, through its legislature, to authorize the charging in Florida of premiums which had been fixed by the insurance companies through the instrumentality of a rating bureau in Atlanta, or anywhere else.

Mr. FERGUSON. I think that under this bill they could allow a rate-making bureau to sit anywhere to fix the rates for Florida.

Mr. PEPPER. Of course, the able Senator has made it very clear that they could, and, of course, they could. So the distinction about intrastate and interstate commerce, of course, is not applicable to that particular point.

Now, Mr. President, I desire to conclude my remarks by saying that if the Senate would reject the conference report, with the direction to the conferees or with the implicaton arising from its rejection, that the Senate would like this language to be stricken or to go back to conference with the House to reconsider this matter, it is possible that the language could be eliminated. But what I am complaining about is not the regulatory power of the States respecting insurance companies or respecting tax matters; I am not even complaining about a 3-year moratorium during which period the Sherman Act or the Clayton Act do not have any authority at all, except as they may affect boycotts, coercion, or intimidation; but I am complaining about the conference report giving to the State legislatures after the 3-year moratorium period the power to curtail, to cut down, to negative, or to repeal the Sherman Act and the Clayton Act. I do not believe the Senate, with due respect for those laws which have been on the statute books respectively since 1890 and 1914, protecting the people of this country against monopoly and against combinations in restraint of trade—I do not believe that the Senate wants to give an invitation to the States to let insurance companies continue to exercise the trade practices under which in my State of Florida in the last 10 years they got premiums of $90,000,000 and paid out losses of $30,000,000, in round figures.

Mr. MURDOCK. Mr. President——

The PRESIDING OFFICER (Mr. La Follette in the chair). Does the Senator from Florida yield to the Senator from Utah?

Mr. PEPPER. I shall yield in a moment. I do not believe that the Senate knowingly wishes to legitimatize a law which would give the insurance companies the power to continue, even under State legislative authority, practices, which, according to the finding of the United States Supreme Court, in the Southeastern States in the last 10 years permitted them to collect premiums—I say in the last 10 years, it was in the period from 1931 to 1941—of $488,000,000 and to pay out losses of $215,000,000. That is what Mr. Justice Black, in the majority opinion of the United States Supreme Court, said they did, exercising the rate-fixing authority with complete immunity from the Sherman Act and the Clayton Act at a time when every other business enterprise in America was restrained by those laws from indulging in practices of that sort. But the insurance companies, cloaked in the holy garments of some kind of immunity that the Supreme Court should never by dicta have conferred upon them, and due to the failure of the Supreme Court before last June to set aside the language of previous decisions, were sanctioned and protected in almost legalized robbery up until June 5 of last year. Senators know that as soon as the decision of that date was rendered the insurance companies scurried like frightened animals to the sanctuary of Congress, seeking here that they might be clothed again by legislation with the privileges and prerogatives they had previously enjoyed until that Supreme Court decision was rendered. And here in the Senate while that case was pending legislation was introduced, and in the House legislation was introduced, to keep the Sherman Act and the Clayton Act from being applicable to the business of insurance. Either of those bills, if enacted, would have nullified the decision of the Supreme Court when it was finally rendered.

Now Mr. President——

Mr. MURDOCK. Mr. President, will the Senator yield?

The PRESIDING OFFICER. Does the Senator from Florida yield to the Senator from Utah?

Mr. PEPPER. In a moment I will yield.

Mr. President, after the House passed a bill that provided a moratorium, giving the States the opportunity to correct their laws and bring them into conformity with the Sherman Act and the Clayton Act, after the Senate did the same thing, after the Attorney General came here and testified before the Senate Judiciary Committee that he had no objection to a reasonable moratorium in order to let them put their house in order, and after the President wrote two letters to the able Senator from Maryland saying that he had no objection to a reasonable moratorium, what are we faced with here today? A carte blanche authority at this late date which has been contained in no previous legislation, which has not passed the House or the Senate; we are now confronted with the language of this conference report which for the first time gives the States carte blanche to legitimatize the very vices against which the Clayton Act and the Sherman Act were directed, to which acts the insurance companies at last have been made amenable by the decision of the United States Supreme Court.

Mr. MURDOCK. Mr. President——

The PRESIDING OFFICER. Does the Senator from Florida yield to the Senator from Utah?

Mr. PEPPER. I now yield to the Senator from Utah.

Mr. MURDOCK. The Senator from Florida paid the able Senator from Wyoming [Mr. O'Mahoney] and myself a great compliment some moments ago.

Mr. PEPPER. The two Senators deserve it.

Mr. MURDOCK. We derived a great deal of comfort from it, and thought that we were on the same side as the Senator from Florida. I desire now to compliment the Senator from Florida on the fine argument he has made; and if he will be patient with me, I want again to call his attention to the fact that we are now confronted, as we have been heretofore, with a practical situation and not a theory. The Senator evidently would have the Senate believe that the House passed a bill which would be more desirable and more satisfactory to him than the conference report. Certainly the Senator does not know what was in the House bill when he takes that position.

What we were confronted with, in the first place, was that the House pass by an overwhelming majority the bill introduced by Representative Walter and Representative Hancock, of New York, which absolutely removed insurance from the Sherman Act and the Clayton Act. That bill came to the Senate and was held up by the Senator from Wyoming, with a little help from a few other Senators, until a decision from the Supreme Court was handed down. Then after many months had gone by, I would say by a herculean effort on the part of the Senator from Wyoming, with a little help from some other Senators, there was brought out a bill which in my opinion, was not nearly so good as the pending conference report. That bill was sent over to the House. The language of which I am sure the Senator from Florida approves, was stricken out by the House and new matter inserted; the bill was returned to the Senate, and the chairman of the Judiciary Committee asked for a conference.

The Senator's argument is the same argument I would have made here a few months ago; but, confronted with the fact that we had to take either the bill which was passed by the House at the last session or something else, I finally consented to support the conference report, which, in my opinion, not only grants a moratorium but allows the States to come affirmatively into the picture. If they do something objectionable, something we do not want done, then the Congress reserves the right to strike it down, and, with arguments such as those the able Senator from Florida is making, we could make both the Clayton Act and the Sherman Act applicable in their full vigor against anything the States might do.

So, I ask why not join us at this time and give the States the opportunity under this conference report to do what, in my opinion, they will do, and that is the right thing.

Mr. PEPPER. Mr. President, I want to compliment the Senator from Utah——

Mr. McCARRAN. Mr. President, will the Senator yield?

The PRESIDING OFFICER. Does the Senator from Florida yield to the Senator from Nevada?

Mr. PEPPER. I yield.

Mr. McCARRAN. I desire to supplement what the Senator from Utah [Mr. MURDOCK] has said with a little further history. The bill which first passed the House set aside the decision of the Supreme Court completely and declared a policy by Congress. That drifted along in the Judiciary Committee for some time, but the bill that came out was a decided improvement on that policy-making piece of legislation. The Senate passed that improved bill. Mind you, Mr. President, that was the first step, and in that step the Senate had gained its point.

The House then struck out our bill completely, after the enacting clause, and sent over a bill which again the Senate refused to accept, and again the Senate and House went into conference and we brought out an improved bill. On each occasion the Senate has won its point, right straight along.

This conference report was adopted by the House by a vote yesterday, and is now before the Senate. Let us either do something that is progressive, which will relieve an industry of an embarrassing situation, or do nothing, and leave chaos and confusion.

If the Senator were correct in his assumption we could go back, but the Senator's argument has been made time and again in various places. I am sorry to say he is in error in his whole premise in this matter, which is unusual for him. This conference report should be adopted as it is.

Mr. PEPPER. Mr. President, let me say two things. First, the able Senator from Wyoming and the able Senator from Utah, joined in by other Senators on the floor, particularly I remember by the Senator from Louisiana [Mr. ELLENDER], have fought valiantly in their effort to avoid the very result against which I am trying to protest here today. I am not complaining at the policy of these gentlemen in stopping their fight at this point. Perhaps they are right in saying that there is a practical situation which they cannot surmount, and therefore we have to yield our individual convictions and subscribe to their view. However, I will say that in my 8 years in the Senate I have seen conference reports voted on here as many as two or three times. This conference report has not been voted on by the Senate before. Am I correct in saying that? On the contrary, this conference report contains language which was not in the bill as it passed the Senate. If the conferees had been back again and again to the House, and the House were adamant, then the members of the conference might properly say to their colleagues, "Gentlemen, we ask to be discharged, because we have done our very best." But the difficulty which our representatives may encounter it would seem to me would preclude the Members of this body from expressing their sentiments on this subject. If, after further effort, they should again meet failure on account of the adamant resistance they encountered from the House, well and good. But, Mr. President, right here, for the first time, this conference report is brought up, with the full knowledge that the legal effect of it, and the intended effect, not intended by the able Senator from Wyoming and the able Senator from Utah, but by the proponents of this series of legislation, is that the States shall have authority to repeal, pro tanto, the applicability of the Sherman Act and the Clayton Act to insurance within their borders. To accept that view at first blush without a protest, but giving countenance and acquiescence to that policy, seems to me to impugn the integrity of the Supreme Court decision, and our long insistence upon adherence to the Sherman Act and the Clayton Act.

I merely appeal to the Senate, that we express ourselves on this conference report. If it is the opinion and the pleasure of Senators that they prefer that the States have that authority, if they believe in rate fixing, if they believe that it is a good thing to let practices persist under which these innumerable insurance companies in my State in 10 years collected three times as much in premiums as they paid out in losses, they have a right to take that position. But I did think it might with propriety be brought to the attention of the Senate, and I want Senators to have an opportunity to express their opinions by a roll call when the debate on the subject shall be concluded.

Mr. O'MAHONEY. Mr. President, let me say, first, in connection with the concluding remark of the Senator from Florida, that as a direct result of the debate in the Congress of the United States over this insurance legislation there has already been a substantial reduction of insurance rates by the authority of the State regulatory bodies of several of the States, including the State of New York. But I desire to call particular attention to the fact that now, as the Senator from Utah has said, we are confronted by a practical problem and not a theoretical dispute.

Of course, it has been found in the past to be in the public interest to permit corporations and persons engaged in businesses affecting the public to agree upon rates. We have eminent precedent for that in the Interstate Commerce Act; we have precedent for it in innumerable State public-utility acts.

PRIVATE INSURANCE GOVERNMENT OUTLAWED

The vice in the insurance industry, Mr. President, was not that there were rating bureaus, but that there was in the industry a system of private government which had been built up by a small group of insurance companies, which companies undertook by their agreements and understandings to invade the field of Congress to regulate commerce. These private groups sought, by the imposition of penalties, by writing rules and regulations, and by holding secret trials, or at least claiming the right to do so, to enforce not public regulations written by public authority but regulations for the insurance business which they wrote themselves in their wholly private and exclusive associations.

To me, Mr. President, this conference report represents a tremendous gain because it outlaws completely all steps by which small groups have attempted to establish themselves in control in the great interstate and international business of insurance.

I have here in my hand, Mr. President, the rules and regulations of the Insurance Executive Association, a national organization of a small group of private companies which occupy a throne at the top of a vast hierarchy of regional associations, by which they had attempted successfully to say who should and who should not engage in the insurance business, what commission an agent should receive or should not receive, who could have desk room in the office of the representative of an insurance company, and how the business should be conducted. This organization is governed not freely by members all on an equal basis, but wholly upon the basis of economic power measured by the amount of premiums collected by its members.

Let me read to the Members of the Senate just a few words from these rules and regulations with respect to the manner in which the association was governed:

> The number of votes to be cast by members at meetings shall be based on their assessable premium incomes as elsewhere herein provided. There shall be two methods of voting—one to be on ordinary association matters and the other to be on appeals from fines or other penalties for violation of rules or ethics. On ordinary association matters the voting shall be as follows:
>
> Group premiums of less than $7,500,000 shall entitle a member to one vote.

Let us remember that we are dealing, now, not with individuals, but with the corporations which the individuals represented.

> Group premiums of $7,500,000 and over but less than $10,000,000 shall entitle a member to two votes.
>
> Group premiums of $10,000,000 and over but less than $12,500,000 shall entitle a member to three votes.
>
> Group premiums of $12,500,000 and over but less than $15,000,000 shall entitle a member to four votes.
>
> Group premiums of $15,000,000 and over but less than $20,000,000 shall entitle a member to five votes.
>
> Group premiums of $20,000,000 shall entitle a member to six votes, and for each full multiple of $5,000,000 of premium income in excess of $20,000,000 a member shall be entitled to one additional vote.

This is the extraordinary manner in which the Insurance Executives Association, which operates in the field of interstate and foreign commerce from one end of the country to the other, is governed. It would be impossible to imagine a more effective system of concentrating economic power over a business in the hands of those who are financially most powerful. The company with the biggest cash account occupies the most powerful place. Equality of merit has no place in the philosophy of this group.

The trustees of this association were given tremendous power.

In addition to their other duties—

And I am reading now—

the trustees shall be especially charged with the following duties:

(a) They shall recommend to the association for adoption such changes in the methods of conducting the insurance business as may in their judgment benefit member companies and render better and more comprehensive service to the insurance public.

(b) They shall enforce the rules and principles of this organization and/or cooperate in the enforcement of the rules of the several territorial and special organizations and in case of violation or evasion of such rules and principles shall also institute such punitive and/or competitive measures as may effectually deter companies from indulging in unfair practices.

"Benefits" for member companies. That was the first consideration of the trustees. "Comprehensive service," whatever that may be, for the insuring public came second, but paragraph (b) with its penalties shows clearly that this group has set up its own little private N. R. A. to regiment the insurance business.

It would be impossible, Mr. President, to imagine language better calculated to place into the hands of a small private group the power to exercise complete control over a vast industry.

Here is the section on complaints and charges:

Complaints and charges may be filed with the president, who shall present the complaints or charges to the board of trustees. If so requested, the president shall not at any time reveal the name of the complainant to the member complained against, to any member of the board of trustees, or to any other person.

Imagine that in a nation the law of which is based upon the principle that any accused person is entitled to be confronted by the person who brings the charge against him. The Insurance Executives Association undertook by regulation to coerce, intimidate, and boycott its own members and compel them to obey the rules and regulations the association itself prescribed.

PENALTIES AND DECISIONS

Whenever the trustees by a vote of two-thirds of their membership shall decide that any member has been guilty of unfair or unethical conduct involving violation or evasion of the rules or principles herein outlined, they shall impose upon such member any penalty they may believe to be most appropriate and fitting, including expulsion from membership, or they may refer their finding to the territorial or special organization having jurisdiction for the imposition of a proper penalty. In case the trustees shall impose a fine upon a member because of any unfair or unethical act or practice the amount of such fine shall be determined by them, having regard to the importance of the matters involved and the evidence of deliberate intent on the part of the member found guilty.

No monetary fine in excess of $10,000 shall be imposed upon a member for any single offense.

In addition to or in lieu of a fine the board of trustees may require that the offending member shall retire from risks or agencies involved for such period as the board of trustees may decide upon and/or that such member shall make adequate restitution when possible to the member or members who may have been injured by the unfair or unethical act of the offending member.

Mr. President, such is the record of one agreement to coerce and intimidate persons engaged in the insurance business. Such is the bald story told in the rules and regulations of the Insurance Executives Association, under the auspices of which came the proposal in the first instance when a Federal indictment was brought in Atlanta, that the Congress of the United States calmly and completely surrender its jurisdiction in the field of interstate commerce so that the Insurance Executives Association could govern in that field according to its own will.

Mr. BARKLEY. Mr. President, will the Senator yield for a question?

Mr. O'MAHONEY. I yield.

Mr. BARKLEY. In subsection (b) of section 3 of the conference report we find this language:

Nothing contained in this act shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

That language does not seem to apply to combinations among insurance companies within the States or among their agents. Why was that language limited to boycott, coercion, or intimidation, which does not include combinations that do not involve either boycott, coercion, or intimidation?

Mr. O'MAHONEY. Because the committee was cognizant of the fact that many salutary combinations might be proposed and which ought to be approved, to which there was no objection. From the very beginning, Mr. President, of this controversy over insurance I have always taken the position that I saw no objection to combinations or agreements among the companies in the public interest provided those combinations and agreements were in the open and approved by law. Public supervision of agreements is essential.

Mr. BARKLEY. Let me ask this question: Suppose the regulatory laws of a State permit combinations which might be regarded as violative of the Sherman or Clayton Acts, and over which Congress itself might wish to exercise jurisdiction, are such combinations so sanctioned by the laws of the States to be allowed, even if Congress itself should decide to exercise jurisdiction?

Mr. O'MAHONEY. No; my judgment is that every effective combination or agreement to carry out a program against the public interest of which I have had any knowledge in this whole insurance study would be prohibited by the very section the Senator from Kentucky has quoted.

Moreover, this proposed act leaves wholly undisturbed, indeed, it fortifies the decision of the Supreme Court that insurance is commerce. It leaves the antitrust laws in full force and effect, even during the moratorium period, against boycotts and agreements to boycott. As I was saying, it is a matter of confronting the facts or arguing on theory. There are agreements and combinations in the public interests which can safely be permitted, but this agreement from which I have been reading is the sort of agreement which ought to be condemned, which ought to be outlawed, and which, in the language of section 3 (b) of the conference report, which the Senator has now read, would be completely outlawed. I refer to the prohibition against agreements to coerce or intimidate.

Let me say to the Senator that when the Senate bill was passed it contained a prohibition against agreements of this kind. When the bill was reported upon the floor of the House the prohibition against such agreements had been eliminated. It was restored in conference; and my feeling is that the great gain which has been achieved by the complete agreement of the Senate and House conferees, to the effect that agreements as well as acts of boycott, coercion, and intimidation should be outlawed, is so distinctly in the public interest that we should not risk its loss.

Mr. BARKLEY. Mr. President, will the Senator yield?

Mr. O'MAHONEY. I yield.

Mr. BARKLEY. I am anxious to have the Senator's interpretation in the RECORD, because it may have some bearing on the future course, not only of legislation, but of court decisions.

Mr. O'MAHONEY. I think the interpretation has already been set forth very clearly.

Mr. BARKLEY. Is it the Senator's interpretation of the conference report that if a State legislature, in its attempt to regulate the insurance business within the confines of the State, should sanction combinations and agreements, Congress itself, if it should determine, after looking into the matter, that such combinations and agreements were against the public interest, would not, by the terms of the proposed law, be estopped from dealing with such combinations and agreements?

Mr. O'MAHONEY. No; the right of Congress to legislate in the field of insurance is explicitly recognized in this report. Let me read the language——

Mr. BARKLEY. I am familiar with the language, but the Senator might put it into the RECORD. Even the proposed law could be repealed by the next Congress if it should see fit to do so.

Mr. O'MAHONEY. That is correct.

Mr. BARKLEY. What I am anxious about is to know that I, as a Senator, will not be estopped in the future from voting upon any legislation regulating insurance, which has been declared to be interstate commerce, and which I have always believed to be interstate commerce. If I vote for this conference report, I am not estopped, as a Senator, from voting for any law which may be under consideration hereafter by Congress dealing with insurance, to the extent that any State authority does not touch the subject, or, if it touches it, does not deal adequately with it.

Mr. O'MAHONEY. In response to the Senator's question, let me say that one of the House conferees, in the course of the conference, used this sentence, which I thought was extremely apt: "This is a bill to authorize the States to regulate the insurance business; and if the States

do not regulate it, the Federal Government can."

Mr. BARKLEY. I thank the Senator.

Mr. O'MAHONEY. I think there can be no doubt about that.

Mr. PEPPER. Mr. President, will the Senator yield?

Mr. O'MAHONEY. I yield.

Mr. PEPPER. What the Senator has said is addressed to future conduct under the prohibition against the Congress enacting an ex post facto law. If this bill were enacted into law, we could not at any time go back and provide for the penalization of anyone who had acted pursuant to a State statute prior to any corrective legislation on the part of Congress, even though such conduct pursuant to the State statute was contrary to the Sherman Act or the Clayton Act.

Mr. O'MAHONEY. My interpretation of the language which I have just read—and I am sure that all the other conferees are in agreement—is that it would permit the Federal Government to continue to indict and prosecute any person or any group for any agreement or act of boycott, intimidation, or coercion, in the past or in the future.

Mr. PEPPER. Mr. President, will the able Senator further yield?

Mr. O'MAHONEY. I yield.

Mr. PEPPER. I did not, of course, limit my question to boycott, coercion, or intimidation, because surely boycott, coercion, and intimidation are not coextensive with the offenses described in the Sherman Act or the Clayton Act. There are other offenses which may be committed under the Sherman Act and under the Clayton Act, in addition to boycott, coercion, and intimidation, are there not?

Mr. O'MAHONEY. Yes.

Mr. PEPPER. So all the conference report does is to limit the legislatures, in authorizing violation of the Sherman Act and the Clayton Act, only with respect to boycott, coercion, or intimidation. However, all the other offenses which are condemned by the Clayton Act or the Sherman Act may, under the proposed legislation, be authorized pursuant to State laws.

AN INVITATION TO THE EXERCISE OF GOOD FAITH

Mr. O'MAHONEY. When the Senator says "may" I agree with him; but it must be remembered that the Sherman antitrust law is such a simple law, expressed in so few words, that it has been variously interpreted and variously misunderstood. Many a great industry has been bothered for fear that it would be in violation of the antitrust law when undertaking to pursue a course which seemed to be in the public interest. I confess that I have had great sympathy with the attitude of some of the oil companies, which, for example, under N. R. A., at the invitation of Congress, did combine and cooperate to do certain things. After the N. R. A. was struck down by the decision of the Supreme Court, they were prosecuted under the Sherman law for doing one of the very things the N. R. A. had invited them to do.

What I think should be done here is to bring clarity out of a situation of confusion. The conference report would give to the States, to the Congress, and to industry the opportunity so to adjust the laws and insurance practices as to bring clarity into the whole situation, in the public interest. It is an invitation to the States to legislate in good faith. It is an invitation to the insurance industry to operate in good faith in the halls of the various State legislatures, and of Congress.

During this controversy, time after time executives of insurance companies spoke to me and told me of the things which I have brought out, but said, "Do not quote me. Do not mention my name." One day toward the close of the last session I met a group of insurance executives who were in Washington at the time the Judiciary Committee had reported a previous bill, in December. They were concerned about the interpretation of the bill. They were in conference here with State insurance commissioners working out this compromise. I said to them, "If you agree with me, why do you not say so?" The answer of one of them, who is a nationally known figure, was, "We cannot afford to." They could not afford to because of secret practices such as those enumerated in the document from which I have been reading.

Mr. FERGUSON. Mr. President, will the Senator yield?

Mr. O'MAHONEY. I yield.

Mr. FERGUSON. I think it should be added in reply to the Senator from Kentucky [Mr. BARKLEY] that there is no attempt here to have Congress throttled in the future in acting upon insurance legislation. Subsection (b) of section 2 provides that if Congress does act, the act shall specifically relate to the business of insurance.

Mr. O'MAHONEY. That is correct.

Mr. FERGUSON. What we have in mind is that the insurance business, being interstate commerce, if we merely enact a law relating to interstate commerce, or if there is a law now on the statute books relating in some way to interstate commerce, it would not apply to insurance. We wanted to be sure that the Congress, in its wisdom, would act specifically with reference to insurance in enacting the law.

Mr. O'MAHONEY. In other words, no existing law and no future law should, by mere implication, be applied to the business of insurance.

Mr. FERGUSON. That is correct.

Mr. O'MAHONEY. That was the understanding.

Mr. FERGUSON. In other words, we would not repeal this law by implication.

Mr. O'MAHONEY. The Senator is quite correct.

Mr. President, it is for those reasons that I feel that this legislation, as embodied in the conference report, is decidedly in the public interest, and should be enacted.

The PRESIDING OFFICER. The question is on agreeing to the conference report.

Mr. PEPPER. I suggest the absence of a quorum.

Mr. BARKLEY. Mr. President, will the Senator withhold his suggestion of the absence of a quorum for a moment?

Mr. PEPPER. Yes.

Mr. BARKLEY. Mr. President, I wish to make a very brief statement with reference to the conference report.

When I first came to Congress years ago, and became a Member of the House of Representatives, there existed in my State an intolerable condition with reference to insurance practices. It applied more to fire, tornado, and other types of insurance than it did to life insurance.

Recognizing that situation, I went to see the Attorney General of the United States, who at the time happened to be James B. McReynolds, later an Associate Justice of the Supreme Court under the appointment of President Wilson, to inquire if some action could not be taken against the practices which then were obtaining in my State under the Sherman antitrust law. Of course, I was confronted with the statement that the Supreme Court of the United States had held that insurance was not interstate commerce, and therefore the Federal Government could do nothing about it. I then expressed myself as believing, despite the decision of the Supreme Court, that insurance was interstate commerce; for I have always believed that a policy of insurance issued in the city of New York and sent to Kentucky or to San Francisco is just as much interstate commerce as is a certificate of stock issued in New York and sent to Kentucky or San Francisco or any other State.

Therefore, I need not say that when the Supreme Court reversed its previous decision in the insurance case, and held that insurance is interstate commerce, I was greatly pleased and encouraged.

As we all know, prior to that decision of the Supreme Court, there was introduced in Congress a bill, the object of which was by means of legislation to take insurance out of the category of interstate commerce. I presume that the object of the bill was to anticipate any possible decision of the Supreme Court, so that, no matter what the Court might decide, Congress would have previously declared the insurance business not to be interstate commerce. I wish to pay tribute to the Senator from Wyoming [Mr. O'MAHONEY], the Senator from New Mexico [Mr. HATCH], the Senator from Utah [Mr. MURDOCK], and other Senators on and off the Judiciary Committtee for the fight they made to prevent the enactment, in advance of a decision, of legislation, which would have made the decision of the Supreme Court a moot question, if the legislation then in contemplation had been enacted.

Of course, I said then—and I said it to many men in the insurance business—that I might not vote in the Senate for a bill setting out the details of the regulation of the insurance business, but I certainly would not vote for a bill which would exempt insurance companies from regulation by Congress. The two propositions are entirely different. I doubt whether I would vote to exempt any character of business which can be interpreted as interstate commerce from the application of the Clayton Act, the Sherman Act, or any other act regulating interstate commerce.

Now we have had all that, and now we come to the proposition that, the Senate, having passed a bill and the House having passed a bill, the bill as passed by the House, as one Senator said to me in private, almost ruined the bill passed by the Senate; so the matter had to go to conference.

I have been somewhat disturbed by the provision in subsection (b) of section 2 of the conference report. However, I think that under the interpretation given it by the conferees my doubts have been resolved, and I intend to vote for approval of the conference report. But I wish it to be understood that in voting for approval of the conference report I am accepting the interpretation placed upon it by the conferees, namely, that if any State, through its legislature, undertakes to go through the form of regulation merely in order to put insurance companies within that State on an island of safety from congressional regulation, that effort will be futile, and not only can Congress deal with any phase of the insurance business not dealt with by a State legislature, but even in a case in which a State legislature deals with any phase of it, but does not deal with it adequately in the opinion of Congress, Congress is not in any way barred by the conference report from dealing with that subject and with the phase of it which Congress deems to have been inadequately dealt with by the State; so that hereafter we can enact such legislation as we may deem proper and wise to have enacted in connection with the regulation of this business, which clearly is interstate commerce.

On that theory I shall vote for acceptance of the conference report, because I realize that we cannot change it. We must either accept it or reject it. If we were to reject it, we might get something even worse. There is no guaranty that we would not.

Therefore, Mr. President, I feel that I am justified in voting for acceptance of the conference report with this interpretation placed upon it by the conferees, and I accept that interpretation as my own.

The VICE PRESIDENT. The question is on agreeing to the conference report on Senate bill 340.

Mr. PEPPER. Mr. President, will the Senator yield?

Mr. BARKLEY. I yield.

Mr. PEPPER. If we were not to accept the conference report at all, would not the States then, under existing law, have authority to legislate with respect to anything which is not in violation of a Federal law in that field?

Mr. BARKLEY. Yes; the States would. In other words, the States could regulate the intrastate phases and aspects of insurance, but probably they could not legislate with reference to the interstate character of insurance, because under the decision of the Supreme Court the antitrust laws apply. In other words, Congress has occupied the field. Having occupied it, the States are more or less estopped from dealing with that field, except only as it applies to the intrastate character of the insurance business.

Mr. PEPPER. Mr. President, will the Senator yield further?

Mr. BARKLEY. I yield.

Mr. PEPPER. Would not the States have all the authority, in the opinion of the able Senator, which they would have under the conference report, except in respect to legislating or regulating in violation of or inconsistently with any paramount Federal law?

Mr. BARKLEY. They would; there is no question about that. But I will say to the Senator that in view of the fact that the two Houses have seen fit to grant what we have called a moratorium, and in view of the fact that the President declared himself in favor of the moratorium, and now we are undertaking to deal with it, in order to give the States themselves an opportunity to regulate, to see what they will do about it within this period, I have reached the conclusion that by granting the moratorium which has been referred to we are denying ourselves as a Congress no authority ultimately to deal with the subject.

Mr. RADCLIFFE. Mr. President, will the Senator yield?

Mr. BARKLEY. I yield.

Mr. RADCLIFFE. If we do not enact any legislation at this time, the situation will be a very serious one. The State insurance commissioners do not know what to do. For instance, they do not know whether they can collect taxes or issue permits. The insurance companies do not know whether they can pay taxes. The insurance commissioners do not know whether they can issue regulations. The entire operation of the insurance business is now in more or less a chaotic condition due to uncertainties which require immediate legislative action. We must have some legislation at the earliest possible moment.

Mr. BARKLEY. I appreciate that. I may also say that the bill was not worked out by the insurance companies. It was largely worked out by a conference of insurance commissioners, who represent the people of the States, and who did not take the viewpoint, I will say, expressed by the insurance companies, namely, to instigate certain legislation in an effort to anticipate the decision of the Supreme Court and to make it nugatory.

I am not uneasy about the situation; I do not believe that hereafter the Congress will not have full authority to deal with the subject if the States do not do so.

Mr. PEPPER. Mr. President, I suggest the absence of a quorum.

The VICE PRESIDENT. The clerk will call the roll.

The Chief Clerk called the roll, and the following Senators answered to their names:

Aiken
Bailey
Ball
Bankhead
Barkley
Brewster
Burton
Bushfield
Butler
Byrd
Capehart
Capper
Chandler
Chavez
Cordon
Donnell
Downey
Eastland
Ellender
Ferguson
Fulbright
George
Gerry
Green
Guffey
Gurney
Hart
Hatch
Hawkes
Hayden
Hickenlooper
Hill
Hoey
Johnson, Calif.
Johnson, Colo.
Johnston, S. C.
Kilgore
La Follette
Langer
McCarran
McFarland
McKellar
McMahon
Maybank
Mead
Millikin
Moore
Morse
Murdock
Murray
Myers
O'Daniel
O'Mahoney
Overton
Pepper
Radcliffe
Revercomb
Robertson
Russell
Saltonstall
Shipstead
Smith
Stewart
Taft
Thomas, Okla.
Thomas, Utah
Tunnell
Tydings
Vandenberg
Walsh
Wheeler
Wherry
White
Wiley
Willis
Wilson

The VICE PRESIDENT. Seventy-six Senators have answered to their names. A quorum is present.

The question is on agreeing to the conference report on Senate bill 340, the so-called insurance bill.

Mr. WHITE. I ask for the yeas and nays.

The yeas and nays were ordered, and the legislative clerk called the roll.

Mr. THOMAS of Utah. I have a general pair with the Senator from New Hampshire [Mr. BRIDGES]. I transfer that pair to the Senator from North Dakota [Mr. MOSES]. I am not advised how either Senator would vote if present and voting. I vote "yea."

Mr. HILL. I announce that the Senator from Florida [Mr. ANDREWS], the Senator from Missouri [Mr. BRIGGS], the Senator from Illinois [Mr. LUCAS], the Senator from Washington [Mr. MITCHELL], the Senator from North Dakota [Mr. MOSES], and the Senator from Nevada [Mr. SCRUGHAM] are necessarily absent.

The Senator from Mississippi [Mr. BILBO] is detained at one of the Government departments on matters pertaining to the State of Mississippi. The Senator from Idaho [Mr. TAYLOR] is detained in a conference at the White House. The Senator from Washington [Mr. MAGNUSON] and the Senator from Arkansas [Mr. MCCLELLAN] are detained on public business.

The Senator from Texas [Mr. CONNALLY] is a delegate to the International Conference in Mexico. The Senator from Virginia [Mr. GLASS] is absent because of illness.

I further announce that the Senator from New York [Mr. WAGNER] has a general pair with the Senator from Kansas [Mr. REED].

Mr. WHERRY. The Senator from Vermont [Mr. AUSTIN] is absent on official business as a delegate to the Inter-American Conference at Mexico City. If present, he would vote "yea."

The Senator from Illinois [Mr. BROOKS] and the Senator from Idaho [Mr. THOMAS] are necessarily absent. Both Senators would vote "yea" if present.

The Senator from Kansas [Mr. REED] is detained on official business. He has a general pair with the Senator from New York [Mr. WAGNER]. If present, the Senator from Kansas would vote "yea."

The Senator from New Hampshire [Mr. BRIDGES], who is detained on official business, has a general pair with the Senator from Utah [Mr. THOMAS]. If present, the Senator from New Hampshire would vote "yea."

The Senator from Delaware [Mr. BUCK] is absent on official business. If present, he would vote "yea."

The Senator from New Hampshire [Mr. TOBEY] is detained on departmental business. If present, he would vote "yea."

The result was announced—yeas 68, nays 8, as follows:

YEAS—68

Aiken	Hart	O'Mahoney
Bailey	Hatch	Radcliffe
Ball	Hawkes	Revercomb
Bankhead	Hayden	Robertson
Barkley	Hickenlooper	Russell
Brewster	Hoey	Saltonstall
Burton	Johnson, Calif.	Shipstead
Bushfield	Johnson, Colo.	Smith
Butler	Johnston, S. C.	Stewart
Byrd	La Follette	Taft
Capehart	Langer	Thomas, Okla.
Capper	McCarran	Thomas, Utah
Chandler	McFarland	Tunnell
Chavez	McKellar	Tydings
Cordon	McMahon	Vandenberg
Donnell	Maybank	Walsh
Eastland	Mead	Wheeler
Ellender	Millikin	Wherry
Ferguson	Moore	White
Fulbright	Morse	Wiley
George	Murdock	Willis
Gerry	Myers	Wilson
Gurney	O'Daniel	

NAYS—8

Downey	Hill	Overton
Green	Kilgore	Pepper
Guffey	Murray	

NOT VOTING—20

Andrews	Connally	Reed
Austin	Glass	Scrugham
Bilbo	Lucas	Taylor
Bridges	McClellan	Thomas, Idaho
Briggs	Magnuson	Tobey
Brooks	Mitchell	Wagner
Buck	Moses	

So the conference report was agreed to.

UTILIZATION OF MANPOWER RESOURCES

The Senate resumed the consideration of the bill (H. R. 1752) to amend the Selective Training and Service Act of 1940, and for other purposes.

The VICE PRESIDENT. The question is on the amendment reported by the committee in the nature of a substitute. Amendments to the amendment are now in order.

Mr. BURTON. Mr. President, I should like to address the Senate on the substitute proposed by the committee. It has been my privilege to attend the hearings of the Military Affairs Committee on the so-called work-or-fight bill, and the development of the legislation through those hearings has convinced me that the proposal recommended by the committee meets the situation, and meets it in the best interests of the Nation with a view to the most rapid solution of our production problem.

I believe it will be helpful to review what is accomplished in the light of the bill as it passed the House and as it stands before the Senate today. First of all, I believe that the whole matter is set forth well and appropriately in the committee report, and I urge Members of the Senate to read the report.

Next, I wish to admit, as everyone does admit, I believe, and as, I think, has been clearly established, that there is a substantial need for additional production of war materials in order to meet our essential requirements in the critical months ahead of us. It has also been established that there may come a crisis 1, 2, 3, 4, or 5 months ahead which makes it necessary for us to take every possible precaution in order to be ready for whatever emergency may arise. I believe that the Senate should pass the pending bill in the light of the circumstances which confront us and do whatever is necessary to meet the production need established by the War Department and asked for by them.

The only real issue is as to which method will best meet that need. Some members of the committee opposed this committee substitute because it was too drastic; others opposed it because it was not drastic enough. That situation in itself should recommend the substitute as a reasonable middle ground.

First, I wish to point out that I believe that House bill 1752 is not adequate and is a dangerous bill in the form in which it came from the House. I take this position for two reasons. First of all, the bill passed the House as a labor draft bill, amounting to a national selective service act on a small scale. It applies only to one-third of the labor force of the United States, while what we need is some measure to reach the whole labor force of the United States, if we are going to solve the production problem equitably and justly. I say the House bill reaches only one-third of the labor force for the reason that it applies only to men between the ages of 18 and 45. The statistics presented to the committee showed that by leaving out the women and leaving out men under 18 and men over 45, there would be left out about two-thirds of the labor force of the United States. Therefore, while there may be reason for applying the bill only to this one-third, yet it is obvious that it does not reach the whole labor force, although it is that whole labor force that is required to meet the emergencies of production as adequately as our whole military manpower meets our military emergencies of combat and supply.

Secondly, the bill as it passed the House attempts to allocate this one-third to appropriate essential work through use of the Selective Service System. We had no testimony before our committee which supported such a method of allocation. It was pointed out that the Selective Service System is adapted to the drafting of men; it is not adapted to the allocation of men to the several branches of industry where they may be most needed. At present we have the War Manpower Commission doing this under its voluntary system. Accordingly, if the bill as it passed the House were to stand, it would create confusion in that it would apply the Selective Service System to one-third of those involved in industry, whereas two-thirds would still be operating under the voluntary administration of the Manpower Commission, thereby applying a conflicting system to the two groups.

Furthermore, the Selective Service System, as was shown by the testimony to my satisfaction is not designed or prepared to handle the allocating of men to particular industrial units. As General Hershey said, it is adapted to drafting men and pushing them up for military service as they are needed. It is not adapted to selecting them for industrial work or channeling them into places where they are needed in industry. The change from the Manpower Commission to the Selective Service System would provoke delay rather than eliminate delay in allocating men to the places where they are most needed.

Therefore, it seemed clear to the committee as a whole, although no express vote was taken on it, that if the bill as it passed the House were to be made the basis of legislation, it should be modified so that its mechanism would come within the hands of the War Manpower Commission under the direction of the War Mobilization and Reconversion Office. I believe that even so modified it would not be a sound solution of the problem.

Mr. BREWSTER. Mr. President, will the Senator from Ohio yield?

Mr. BURTON. I am glad to yield to the Senator from Maine.

Mr. BREWSTER. Did General Hershey indicate that he had not previously supported the so-called May bill as a practical solution of the problem?

Mr. BURTON. He indicated that he would be glad to support it with the amendments which would put the administration of the allocation of labor under the direction of the War Mobilization and Reconversion Office.

Mr. BREWSTER. Did the War Manpower Commission convince the Senator that they had hitherto adequately handled this problem?

Mr. BURTON. They convinced me that they had made a great deal of progress with it. They convinced me further that if they were given the backing of some legislative support, plus two or three additions in the bill which I shall mention, they would meet the need more adequately than it could be met by changing the whole system over to a draft system at this late time.

Mr. BREWSTER. Did Mr. McNutt point out that he had hitherto always opposed any legislation as entirely unnecessary until the crisis became so acute it could no longer be ignored?

Mr. BURTON. I do not think he testified on that point, but he did indicate that there had been thus far no legislative authority behind his system, but that his system, as he put it, had been highly successful, although they had made a number of errors as they had proceeded.

Mr. THOMAS of Utah. Mr. President, will the Senator yield?

Mr. BURTON. I yield.

Mr. THOMAS of Utah. I wonder if the Senator from Ohio would not like to have us get into the RECORD at this point the words of General Hershey himself when the questions were put to him in regard to his support of the amendment. If the Senator from Ohio will permit, I should like to read just a paragraph or two from the record, beginning on page 152. Before General Hershey made any statement at all, the chairman asked this question:

> The CHAIRMAN. General Hershey, first of all, may I ask you this question: In your report to us on the bill you are the only one of the departmental chiefs, or nearly the only one, that did not mention the suggested amendments; now, shall we assume that you are against those amendments?
>
> General HERSHEY. No, sir.
>
> The CHAIRMAN. We may assume that you are for the amendments?
>
> General HERSHEY. Yes, sir. If the committee wants, I can tell you why that letter was written as it was.

Exchange of correspondence between President Franklin D. Roosevelt and Senator George L. Radcliffe regarding an antitrust exemption for the insurance industry.

WALTER F. GEORGE, GA., CHAIRMAN
...SH, MASS. | ROBERT M. LA FOLLETTE, JR., WIS.
... BARKLEY, KY. | ARTHUR H. VANDENBERG, MICH.
... CONNALLY, TEX. | JAMES J. DAVIS, PA.
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BENNETT CHAMP CLARK, MO. | JOHN A. DANAHER, CONN.
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GEORGE L. RADCLIFFE, MD.
SCOTT W. LUCAS, ILL.
CHRISTIE B. KENNEDY, CLERK

United States Senate

COMMITTEE ON FINANCE

THE WHITE HOUSE
JUN 6 2 13 PM '44
RECEIVED

June 6, 1944

My dear Mr. President:

The decision of the Supreme Court yesterday, reversing the long-time settled law in that the Court decided that insurance comes under the supervision of the Sherman Anti-trust Act, is, I think, one of the most far-reaching which has been rendered for a long time.

Of course it means in substance probably that the insurance industry, one of the largest in the country, will be turned over from the supervision of the States to that of the Federal government. The demand upon manpower and time of the Federal government to take over this gigantic industry cannot be satisfied, I assume, without very heavy strain upon the energies of the Federal government in carrying on our war program.

Several months ago in talking to Attorney General Biddle I urged that if Paul vs. Virginia were reversed that the Government should not only be slow to attempt to up-set all the existing arrangements authorized by the States, but should also issue reassuring statements that there would be no haste. I have the impression that the Government intends to show some restraint in this matter.

The Bailey-Van Nuys bill has been held in the Judiciary Committee awaiting the decision of the Supreme Court in the case just decided.

It is very fortunate that the insurance interests, although under state control, stood very staunchly during the depression, and I understand that state officials, boards of trade, and insurance interests quite generally have registered vigorous opposition to the suggested shift from state control to federal.

I have studied the matter carefully for years and have seen no adequate justification for such a shift. It seems to me that such a transfer in time of war, and I may add in a political campaign, is especially unfortunate.

Very respectfully,

George L. Radcliffe

George L. Radcliffe

Honorable Franklin D. Roosevelt
President of the United States
The White House

June 10, 1944

My dear Senator Radcliffe:

I have your letter of June sixth with respect to the recent decision of the Supreme Court deciding that insurance comes under the provisions of the Sherman Act. You suggest that this would probably mean supervision by the Federal Government.

The Attorney General advises me that he does not believe that this alternative is inevitable or even probable. He tells me that there is nothing in the decision which prevents the regulation by the states of insurance rates as long as that regulation does not interfere with the provisions of the Sherman Act.

Personally I know of no effort at this time to bring insurance companies under over-all Federal regulation. Whether or not such control were adopted would depend, I think, very much on the attitude of the companies themselves in complying with the provisions of the Sherman Act.

The Attorney General assures me that he is anxious that the insurance companies and the state insurance officials shall have a reasonable time within which to conform their practices and statutes to the decision of the Supreme Court.

With best regards, always,

Very sincerely yours,

FRANKLIN D. ROOSEVELT

Honorable George L. Radcliffe,
United States Senate,
Washington, D. C.

WALTER F. GEORGE, GA., CHAIRMAN
[illegible], MASS. — ROBERT M. LA FOLLETTE, JR., WIS.
[illegible] BARKLEY, KY. — ARTHUR H. VANDENBERG, MICH.
[illegible] CONNALLY, TEX. — JAMES J. DAVIS, PA.
[illegible] W. BAILEY, N. C. — HENRY CABOT LODGE, JR., MASS.
BENNETT CHAMP CLARK, MO. — JOHN A. DANAHER, CONN.
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GEORGE L. RADCLIFFE, MD.
SCOTT W. LUCAS, ILL.
CHRISTIE B. KENNEDY, CLERK

United States Senate

COMMITTEE ON FINANCE

December 20, 1944

My dear Mr. President:

I am writing this note in regard to the insurance situation. On June 6, 1944, one day after the very far-reaching decision of the Supreme Court reversing Paul vs. Virginia, I wrote a letter to you emphasizing what I thought was the gravity of the situation. I suggested that you declare a sort of moratorium during which essential adjustments could be made to the new decision. I also requested that you issue a reassuring statement to the industry suddenly facing problems of a grave and unprecedented nature. On June 10, you very kindly wrote me a letter in which your position was, on the whole, favorable to what I had requested.

Since that time the insurance industry, insurance commissioners, certain officials of the Federal Government members of Congress and others have been endeavoring to work out an arrangement which would seem to be adequate. Likewise the status as to state taxation and other forms of state regulation have been questioned in some channels.

The adjournment of Congress has come before such plans could really be carried out. I have been in close touch with Attorney General Biddle who has been very helpful. It is my impression that he is in favor of a suitable moratorium, but there are some departments of the Federal Government closely involved which do not come under the supervision of the Attorney General.

I again very respectfully suggest that you give expression to some form of moratorium under which state activities could continue freely pending federal and state legislation which will undoubtedly be passed and put into operation within the very near future.

I am sure everyone is in accord with the idea you expressed in your letter to me of June 10, that the insurance industry which is one of the largest and most important in this country should have every reasonable opportunity for readjustment.

Sincerely yours,

George L. Radcliffe

George L. Radcliffe

Honorable Franklin D. Roosevelt
President of the United States
The White House

January 2, 1945

My dear Senator Radcliffe:

In your letter of December twentieth, you suggest that there should be some form of a moratorium during which insurance companies will have an opportunity to readjust their practices in order to bring them into conformity with the Supreme Court decision in the South-Eastern Underwriters Association case, and during which legislation might be enacted. The Attorney General advises me that several months ago he told the Senate Judiciary Committee that no new antitrust prosecutions against insurance companies would be instituted during a reasonable readjustment period.

The responsibility for the regulation of the business of insurance has been left with the states; and I can assure you that this Administration is not sponsoring federal legislation to regulate insurance or to interfere with the continued regulation and taxation by the states of the business of insurance. But there is no conflict between the application of the antitrust laws and effective state regulation of insurance companies, and there is no valid reason for giving any special exemption from the antitrust laws to the business of insurance. The antitrust laws prohibit private rate fixing arrangements between insurance companies and acts of boycott, coercion or intimidation. The antitrust laws do not conflict with affirmative regulation of insurance by the states such as agreed insurance rates if they are affirmatively approved by state officials.

Senator O'Mahoney introduced a bill in the last Congress which would have provided for a moratorium from the Sherman Act, except for acts of boycott, coercion or intimidation, until March 1, 1946. This would appear to give sufficient time to permit the necessary readjustment to the Supreme Court decision. I would favor legislation of this general character. It would permit the orderly correction of abuses which have existed in the insurance business and would preserve the right of the states to regulate with full responsibility.

Very sincerely yours,
FRANKLIN D. ROOSEVELT

Honorable George L. Radcliffe,
United States Senate,
Washington, D. C.

President Roosevelt's statement upon signing the McCarran-Ferguson Act.

139. Moratorium for Insurance Companies

139 ¶ The President's Statement on Signing a Bill Granting Insurance Companies a Moratorium Under the Anti-trust Laws. March 10, 1945

I HAVE given my approval to S. 340, the insurance bill, which passed the Congress last week. This bill grants the insurance business a moratorium from the application of the anti-trust laws and certain related statutes, except for agreements to boycott, coercion, or intimidation, or acts of boycott, coercion, or intimidation, until January 1, 1948. The purpose of this moratorium period is to permit the States to make necessary readjustments in their laws with respect to insurance in order to bring them into conformity with the decision of the Supreme Court in the *Southeastern Underwriters Association* case. After the moratorium period, the anti-trust laws and certain related statutes will be applicable in full force and effect to the business of insurance except to the extent that the States have assumed the responsibility, and are effectively performing that responsibility, for the regulation of whatever aspect of the insurance business may be involved. It is clear from the legislative history and the language of this Act, that the Congress intended no grant of immunity for monopoly or for boycott, coercion, or intimidation. Congress did not intend to permit private rate fixing, which the Anti-trust Act forbids, but was willing to permit actual regulation of rates by affirmative action of the States.

The bill is eminently fair to the States. It provides an opportunity for the orderly correction of abuses which have existed in the insurance business and preserves the right of the States to regulate in a manner consonant with the Supreme Court's interpretation of the anti-trust laws.

NOTE: On October 9, 1944, the United States Supreme Court in the case of *U. S.* vs. *Southeastern Underwriters Association et al.*, 322 U. S. 533, decided that the business of insurance was commerce, and

1984 GOV Competition in the Insurance Industry 739p bonknote.pdf

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Testimony of Maxwell M. Blecher, who was a member of the National Commission for the Review of Antitrust Laws and Procedures, submitted for the record.

THE INSURANCE INDUSTRY ANTITRUST EXEMPTION

TESTIMONY OF
MAXWELL M. BLECHER
BEFORE THE SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW
COMMITTEE ON THE JUDICIARY
UNITED STATES HOUSE OF REPRESENTATIVES
APRIL 11, 1984

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE, I AM MAXWELL M. BLECHER OF THE LOS ANGELES LAW FIRM OF BLECHER, COLLINS & WEINSTEIN. I APPRECIATE THIS OPPORTUNITY TO TESTIFY BEFORE THIS SUBCOMMITTEE ON THE TOPIC OF THE ANTITRUST EXEMPTION GRANTED TO THE BUSINESS OF INSURANCE BY THE MCCARRAN-FERGUSON ACT.

AS YOU MAY KNOW, I WAS A MEMBER OF THE NATIONAL COMMISSION FOR THE REVIEW OF ANTITRUST LAWS AND PROCEDURES, WHICH RECOMMENDED REPEAL OF THE MCCARRAN-FERGUSON EXEMPTION AND ITS REPLACEMENT BY NARROWLY-DRAWN LEGISLATION ADDRESSING SPECIFIC ISSUES. AS I WILL SHOW BELOW, THAT RECOMMENDATION IS EVEN MORE APPROPRIATE TODAY.

THE RECOMMENDATION OF THE NATIONAL COMMISSION

THE NATIONAL COMMISSION FOR THE REVIEW OF ANTITRUST LAW AND PROCEDURES (HEREINAFTER "COMMISSION") WAS CREATED BY PRESIDENT CARTER IN DECEMBER 1977. THE COMMISSION CONTAINED A CROSS SECTION OF PRIVATE ATTORNEYS, GOVERNMENT AND REGULATORY AGENCY REPRESENTATIVES AND MEMBERS OF THE CONGRESS.

ONE OF THE TOPICS CONSIDERED BY THE COMMISSION WAS THE ANTITRUST EXEMPTION OF IMMUNITY FOR THE BUSINESS OF INSURANCE. THE COMMISSION TOOK EXTENSIVE TESTIMONY ON ISSUES SUCH AS THE DEGREE OF COMPETITION IN THE INSURANCE INDUSTRY, THE EFFECT OF STATE REGULATION, AND THE NEED FOR COOPERATIVE ACTIVITIES.

IN ITS FINAL REPORT, THE COMMISSION RECOMMENDED REPEAL OF THE BROAD ANTITRUST IMMUNITY GRANTED BY THE MCCARRAN-FERGUSON

ACT. FEARS WERE EXPRESSED, HOWEVER, THAT REPEAL OF THE EXEMPTION WOULD PLACE THE LEGALITY OF MANY LEGITIMATE INSURANCE INDUSTRY PRACTICES IN DOUBT. ACCORDINGLY, THE COMMISSION RECOMMENDED FURTHER STUDY OF THOSE PRACTICES AND WHETHER NARROWLY-DRAWN LEGISLATION SHOULD BE ADOPTED TO AFFIRM THEIR LAWFULNESS.

IN ITS REPORT, THE COMMISSION RECOGNIZED THAT, UNDER THE STATE ACTION DOCTRINE, STATE REGULATION OF INSURANCE WOULD EXEMPT INSURANCE ACTIVITIES TO THE EXTENT THAT A STATE AGENCY COMPELLED THE ACTIVITY AND ACTIVELY SUPERVISED IT. THE COMMISSION, HOWEVER, EXPRESSED A PREFERENCE FOR NARROWLY-TARGETED STATE REGULATION ADDRESSED TO DISCRIMINATION, DISCLOSURE, AND SIMILAR PROBLEMS, AS OPPOSED TO MORE BLANKET REGULATION ENCOMPASSING COMPETITIVE ISSUES SUCH AS RATES. THE COMMISSION ALSO RECOMMENDED FURTHER STUDY OF INSURANCE REGULATION, INCLUDING THE TOPICS OF APPROPRIATE REGULATORY RESPONSES TO THE PROBLEMS OF EQUITY AND DISCRIMINATION IN INSURANCE RATES AND THE ROLE OF FEDERAL LEGISLATION WITH RESPECT TO THE BUSINESS OF INSURANCE.

THE CONTINUED VALIDITY OF THE COMMISSION'S RECOMMENDATIONS

THE CASE FOR REMOVAL OF ANTITRUST IMMUNITY IN THE INSURANCE INDUSTRY, AS RECOMMENDED BY THE COMMISSION, IS JUST AS COMPELLING TODAY. THE ANTITRUST DIVISION IN ITS 1977 REPORT ON THE INSURANCE INDUSTRY, AND THE COMMISSION IN ITS OWN REPORT, DOCUMENTED THE INDUSTRY'S CARTEL-LIKE BEHAVIOR AND RESULTING INEFFIENCIES. A MORE RECENT STUDY IS ANDREW TOBIAS'S THE

INVISIBLE BANKERS (1982), WHICH DOCUMENTS, IN TERMS READILY ACCESSIBLE TO THE LAYMAN, THE GROSS INEFFECIENCIES IN THE DELIVERY OF INSURANCE CAUSED BY THE LACK OF EFFECTIVE COMPETITION. AS HE PUTS IT SO COGENTLY, THE PRESENT SYSTEM HAS RESULTED IN TOO MANY UNDERWRITERS, TOO MANY AGENTS, TOO MANY SUPPORT PERSONNEL, TOO HIGH PRICES, AND TOO LITTLE INFORMATION AND OPTIONS AVAILABLE TO THE CONSUMER. THESE CONDITIONS, I SUBMIT, CONSTITUTE THE CLASSIC EFFECTS OF RESTRICTED COMPETITION THAT THE ANTITRUST LAWS WERE DESIGNED TO REDRESS.

A. DEREGULATION IN OTHER INDUSTRIES

THE RECENT EXPERIENCE WITH OTHER DEREGULATED INDUSTRIES, IN PARTICULAR THE TRANSPORTATION INDUSTRIES, DEMONSTRATES THE PROCOMPETITIVE EFFECT OF REMOVAL OF ANTITRUST IMMUNITY AND THUS VINDICATES THE POSITION TAKEN BY THE COMMISSION. THE COMMISSION, YOU MAY RECALL, RECOMMENDED THE ABOLITION OF ANTITRUST IMMUNITY FOR SURFACE TRANSPORTATION INDUSTRIES AND THE RELAXATION OF REGULATORY BARRIERS TO ENTRY. THE RAIL INDUSTRY WAS SUBSEQUENTLY DEREGULATED IN THE STAGGERS RAIL ACT OF 1980 (PUB.L. 96-448) AND THE TRUCKING INDUSTRY IN THE MOTOR CARRIER ACT OF 1980 (PUB.L. 96-296). THE AIRLINES, OF COURSE, HAD BEEN DEREGULATED IN THE AIRLINE DEREGULATION ACT OF 1978 (PUB.L. 95-504).

WHILE IT IS ADMITTEDLY TOO EARLY FOR DEFINITIVE CONCLUSIONS ON THE EFFECT OF THE RECENT DEREGULATION (AND LOSS OF ANTITRUST IMMUNITY), IT IS CLEAR THAT THE CHAOS THAT SOME PREDICTED HAS NOT OCCURRED. RATHER, THE AVAILABLE, IMPRESSIONISTIC

EVIDENCE INDICATES LOWER PRICES, NEW ENTRANTS, AND FOR THE EFFICIENT COMPETITORS, CONTINUED PROFITABILITY. SEE, E.G., DEREGULATING AMERICA, BUSINESS WEEK AT 80 (1983). INDEED, SOME INDUSTRIES SUCH AS THE RAILROADS, SEEM TO HAVE PROSPERED AS A DIRECT RESULT OF DEREGULATION. SEE, E.G., M. WINES, THREE YEARS AFTER DEREGULATION, 15 NAT. JOURNAL 2560 (1983).*

TO BE SURE, THERE HAVE BEEN FINANCIAL DIFFICULTIES EXPERIENCED BY LESS EFFICIENT COMPANIES; WE SEE THIS MOST DRAMATICALLY IN THE AIRLINE INDUSTRY, WITH THE SPATE OF RECENT BANKRUPTCIES. THIS KIND OF DISLOCATION, HOWEVER, IS TO BE EXPECTED WITH THE ADVENT OF VIGOROUS COMPETITION. THE IMPORTANT POINT IS THAT THESE DEREGULATED INDUSTRIES APPEAR TO BE FUNCTIONING: AIRLINE TICKETS ARE STILL BEING WRITTEN FOR TRAVEL ALL OVER THE COUNTRY; THE RAILROADS SEEM BUSIER THAN EVER; TRUCKS CONTINUE TO HAUL VAST QUANTITIES OF OUR NATION'S FREIGHT. IN SHORT, THEY HAVE NOT BROKEN DOWN. THEREFORE, TO THE EXTENT THAT THE INSURANCE INDUSTRY ASSERTS THAT THEY WILL NOT BE ABLE TO FUNCTION WITHOUT THE EXEMPTION, SO THAT POLICIES WILL NOT BE WRITTEN OR THE PUBLIC NOT PROTECTED, THE EXPERIENCE WITH DEREGULATION EMPHATICALLY CONTRADICTS THAT. INSURANCE COMPANIES WILL HAVE TO SCRAMBLE HARDER FOR BUSINESS, BUT, I PREDICT, THE PUBLIC WILL STILL HAVE AMPLE ACCESS TO INSURANCE.

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* FOR EXAMPLE, WEEKLY TON-MILES OF RAIL SHIPMENTS WERE RISING BY AS MUCH AS TEN PERCENT IN THE THIRD QUARTER OF 1983. THE NORFOLK SOUTHERN REPORTED A 1983 THIRD-QUARTER EARNINGS GAIN OF 37%, THE BURLINGTON NORTHERN A 55% GAIN. T. COOK, TRANSPORTATION, FORBES AT 149 (JAN. 2, 1984).

B. Supreme Court Trends

Since the Commission's report, the Supreme Court has stepped in to whittle-down the insurance exemption. Group Life and Health Insurance Co. v. Royal Drug Co., 440 U.S. 205 (1979) and Union Labor Life Insurance Co. v. Pireno, 102 S.Ct. 3002 (1982). In Royal Drug Co., the Court held that the "business of insurance" did not include agreements between insurance companies and drug stores as to maximum prices for prescriptions.

In Pireno, the Supreme Court refined the analysis in Royal Drug to set forth the following three-part test, namely whether the challenged activity (1) involves the underwriting or spreading of risk; (2) involves the insurer-insured relationship; and (3) is limited to entities within the insurance industry that the Act intended to protect. Applying this test, the Court held that an agreement between an insurance company and an association of chiropractors for review of chiropractors' bills was not the business of insurance.

This trend in Supreme Court decisions is laudable and conforms to the pro-competition philosophy expressed in the Commission's report. I would note in passing that, although the practical impact of the Court's decisions may at present be slight, I perceive no great disruption to the industry caused by them.

THE PURPORTED RATIONALES FOR THE EXEMPTION

A. EXCHANGE OF INFORMATION.

AS NOTED IN THE COMMISSION'S REPORT AT PAGES 238-39, A CHIEF ARGUMENT FOR THE EXEMPTION IS THE INDUSTRY'S PURPORTED NEED TO EXCHANGE, ON A REGULAR BASIS, INFORMATION PERTAINING TO INSURANCE RISKS (E.G., THE AMOUNT AND FREQUENCY OF PREVIOUS CLAIMS). WITHOUT THE EXEMPTION, THE ARGUMENT GOES, SUCH EXCHANGE OF INFORMATION COULD CONSTITUTE PRICE FIXING.

THE CASE LAW IS CLEAR, HOWEVER, THAT COMPANIES CAN EXCHANGE VAST QUANTITIES OF RELEVANT INFORMATION WITHOUT FEAR OF ANTITRUST LIABILITY. E.G., MAPLE FLOORING MANUFACTURERS ASS'N V. UNITED STATES, 268 U.S. 563 (1925); TAG MANUFACTURERS INSTITUTE V. FTC, 174 F.2D 452 (1ST. CIR. 1940). AS LONG AS THE DATA IS REASONABLY HISTORIC IN CHARACTER (I.E., IT IS NOT REPORTED ON A DAILY BASIS) AND IS REPORTED IN AGGREGATE (NOT INDIVIDUAL) FORM, COMPETITORS ARE FREE TO EXCHANGE PRICE, COST AND QUANTITY DATA. ID.

HERE IN WASHINGTON THERE ARE HUNDREDS OF TRADE ASSOCIATIONS REPRESENTING COUNTLESS INDUSTRIES THAT HAVE WELL-ESTABLISHED, PROCEDURES FOR EXCHANGING AND PUBLISHING INDUSTRY DATA ON A VARIETY OF TOPICS. SEE GENERALLY, G. WEBSTER, LAW OF ASSOCIATIONS (1982). THESE ASSOCIATIONS ACCOMPLISH THIS USEFUL, LAWFUL ACTIVITY WITHOUT ANY SPECIFIC ANTITRUST EXEMPTION, BUT RATHER BY COMPLYING WITH RUDIMENTARY ANTITRUST GUIDELINES DISCUSSED ABOVE.

B. THE PURPORTED NEED FOR JOINT UNDERWRITING AGREEMENTS.

AS NOTED IN THE COMMISSION'S REPORT AT PP. 235, 239, ANOTHER RATIONALE FOR THE MCCARRAN-FERGUSON EXEMPTION IS TO PROTECT THE INDUSTRY'S COMMON PRACTICE OF AGREEING TO SHARE THE RISKS ON VARIOUS TYPES OF INSURANCE. AS THE COMMISSION'S NOTED, HOWEVER, ANTITRUST IMMUNITY IS NOT NECESSARY TO PROTECT SUCH AGREEMENTS FROM LIABILITY. UNDER CURRENT CASE LAW (AND THE ENFORCEMENT AGENCIES' PHILOSOPHY AS EMBODIED IN THE RECENT APPROVAL OF THE GM-TOYOTA JOINT VENTURE), COOPERATIVE AGREEMENTS AMONG COMPETITORS ARE VIOLATIVE OF THE ANTITRUST LAWS ONLY IF THEY CONSTITUTE A CLEAR-CUT RESTRAINT ON COMPETITION. E.G., BERKEY PHOTO, INC. V. EASTMAN KODAK CO., 603 F.2D 263, 301-302 (2ND CIR. 1979), CERT. DENIED, 444 U.S. 1093 (1980); SEE, ALSO, ANTITRUST GUIDE CONCERNING RESEARCH JOINT VENTURES (ANTITRUST DIVISION, NOV. 1980). IT WAS THE COMMISSION'S VIEW, WHICH IS STILL VALID TODAY, THAT TRADITIONAL UNDERWRITING OR RISKSHARING ACTIVITIES COULD BE CARRIED ON WITHOUT OFFENDING THE ANTITRUST LAWS. AS THE COMMISSION POINTED OUT, THE SECURITIES AND CONSTRUCTION INDUSTRIES COMMONLY OPERATE IN A JOINT VENTURE FASHION.

AGAIN, THE EXPERIENCE IN RECENTLY-DEREGULATED INDUSTRIES COULD BE FERTILE GROUND FOR EVALUATING THE IMPACT ON JOINT INDUSTRY ACTIVITIES. THE COMMITTEE SHOULD INVESTIGATE WHETHER THESE DEREGULATED INDUSTRIES HAVE IN FACT REDUCED THE SCOPE OF THEIR JOINT ACTIVITIES, AND IF SO, WHETHER THAT HAS

REDUCED THE EFFICIENCY OF THE INDUSTRY AS A WHOLE. I SUSPECT THAT THE ANSWER WILL BE THAT PROCOMPETITIVE JOINT ACTIVITIES ARE STILL BEING CONDUCTED, TO THE BENEFIT OF THE INDUSTRY AND THE CONSUMER.

CONCLUSION

THE COMMISSION'S RECOMMENDATION FOR REPEAL OF THE McCARRAN-FERGUSON ANTITRUST EXEMPTION IS AS VALID TODAY AS IT WAS WHEN FIRST PROPOUNDED IN 1979. THE INSURANCE INDUSTRY CAN FUNCTION EFFECTIVELY, INDEED AGRESSIVELY, WITHOUT THE ANTITRUST EXEMPTION.

APPENDIX 2

May 3, 1984

Legal memorandum on the FTC's authority to study the insurance industry, prepared by the FTC in 1979.

Attachment III

Analysis of the FTC's Authority Under Section 6 of the FTC Act to Collect and Report Information on the "Business of Insurance"

Since 1976, the Federal Trade Commission ("FTC" or "Commission") has had an active program[1] to provide state insurance commissions and the Congress with information they can use to increase price competition among industry members or otherwise benefit consumers by improving the quality of insurance regulation. The goals of this program do not go beyond providing information. More specifically, in full recognition of the McCarran-Fergusen Act, it is not intended that the Commission will exert any regulatory authority over the business of insurance to the

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1 The insurance program is made up of five investigations, each of which is designed to collect and report information about insurance problems. The specific investigations within this program deal with:

(1) sales abuses and other problems in the sale of "medi-gap" insurance to the elderly;

(2) sales abuses and other problems in the sale of extremely expensive "debit" insurance principally to low income, inner city and rural consumers;

(3) the lack of adequate price competition among sellers of whole life insurance (this project is in its final stage -- answering requests for information and assistance following release this past summer of the Life Insurance Cost Disclosure Report);

(4) the availability of adequate cost information to small businessmen who purchase insurance to fund pension plans for their businesses; and

(5) the fairness of high auto insurance rates paid by some consumers solely because of their age, sex, marital status or geographical location.

extent that it is regulated by state law.

In a memorandum submitted for the October 17, 1979 hearings before the Senate Committee on Commerce, Science and Transportation, Aetna Life and Casualty Company ("Aetna") argues that the McCarran-Ferguson Act denies the Commission authority to investigate and report on the "business of insurance" in situations where the states are regulating. Aetna argues that the Commission's insurance investigations violate this principle, and that Congress should "clarify" the FTC's authority by amending Section 6 of the Federal Trade Commission Act (FTCA) to explicitly prohibit the Commission from investigating and reporting on the "business of insurance."[2] If this recommendation is adopted, the Commission's insurance program will be terminated.

The first section of this memorandum demonstrates that Aetna's legal analysis is incorrect. In adopting the McCarran Act, Congress' limited goal was to recognize and preserve the authority of the states to tax and regulate insurance. The statute was narrowly crafted to do nothing more than to make inapplicable to the business of insurance, federal legislation[3] that would, or could be used to, preempt under the Supremacy Clause of the Constitution inconsistent state insurance regulation. The McCarran Act was never intended to, and does not,

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2 Aetna Life and Casualty Company, Removal of FTC's Fact-Finding and Reporting Powers by the McCarran-Ferguson Act, at 10 [hereinafter cited as the Aetna memo].

3 This refers, of course, to federal statutes of general applicability.

withdraw federal authority to engage in activity, such as providing information, that does not conflict with the states' right to regulate and tax. In stating the opposite conclusion, Aetna's analysis contradicts the legislative history of the McCarran Act, the language of the statute and the findings of a subcommittee of the House of Representatives.

It must be recognized, however, that the issue at this point goes beyond the Commission's legal authority under existing statutes. The larger question raised by Aetna is whether the Commission should continue to study and report on important issues facing insurance regulators. The second section of this memorandum sets forth the important public policy considerations indicating the value of continuing the FTC's insurance program.

I

The FTC has Legal Authority to Investigate the "Business of Insurance."

A. Investigating and Reporting Authority Under Section 6, FTCA

Before addressing the merits of Aetna's argument, it may be helpful to review the Commission's authority under Section 6 of the FTCA. Under that section the FTC possesses authority, quite apart from its regulating functions, to gather and report information of value to Congress, the states and the public. Indeed, the legislative history of the FTCA indicates that Congress intended the FTC to be, in the words of the Senate Report, "an indispensible instrument of information and publicity."[4]

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4. S. Rep. No. 597, 63d Cong. 2d Sess. pp. 6-7 (1914).

Section 6(a) authorizes the Commission ". . . to gather and compile information concerning the organization, business, conduct, practices, and management of unexcepted corporations engaged in commerce. . . ." Section 6(f) authorizes the Commission "[t]o make public. . . information obtained by it . . . and [report] to the Congress and to submit . . . recommendations for additional legislation; and to provide for the publication of its reports for public information or use." The Commission's investigatory powers under Section 6 have been consistently construed to be broader and entirely different from its regulatory power under Section 5 of the FTCA.[5]

B. McCarran's Legislative History

The legislative history of the McCarran Act indicates that Congress never considered the Act's potential impact on the Commission's information reporting responsibilities under Section 6 of the FTCA. It also establishes that the McCarran Act was adopted for a limited purpose -- to preserve the states' authority (1) to tax and (2) to regulate in ways that would violate the federal antitrust laws if they applied. A statute intended only to preserve the states' legal authority to tax and regulate should not be construed to preclude the FTC from providing advice to the states on how they might regulate more effectively (action which recognizes the primacy of state author-

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5 Appeal of FTC Line of Business Report Litigation, 595 F.2d 685, 702 (D.C. Cir. 1978) cert. denied, 99 S. Ct. 362 (1978); Ash Grove Cement Co. v. FTC, 577 F.2d 1368, 1375 (9th Cir. 1976).

ity). Moreover, the framers of the McCarran Act repeatedly assured other members of Congress that they recognized Congress' responsibility to ensure that state regulation served the public interest and to step in if it did not. It would be inconsistent with those assurances to construe the McCarran Act as denying to Congress and its various committees the benefit of information on the effectiveness of state regulation.

The McCarran Act was a direct response to the Supreme Court's decision in United States v. South-Eastern Underwriters Association, 322 U.S. 533 (1944) (hereinafter cited as South-Eastern).[6] The Court held that the business of insurance conducted across state lines was interstate commerce and therefore subject to the prohibitions of the Sherman Act.[7] For more than 75 years prior to the decision the Supreme Court had maintained that the business of insurance was not commerce, either intrastate or interstate.[8] It therefore followed that the business of insurance was not subject to the federal antitrust laws, since these laws are founded on the federal commerce power.

South-Eastern raised two fundamental questions about state authority. The first concerned the states' taxing powers. During the year prior to the decision the states had raised

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6 FTC v. Travelers Health Ass'n., 362 U.S. 293, 299 (1960).

7 322 U.S. 533, 539, 560 (1944).

8 Paul v. Virginia, 75 U.S. (8 Wall.) 168, 183 (1868).

$126 million[9] in revenues by taxing insurance. Once the Supreme Court decided that insurance was interstate commerce, some argued that taxes levied on companies which wrote policies in more than one state might be regarded as unlawful burdens on interstate commerce.[10] Within one year of the decision, court actions were filed challenging tax laws in eleven states and taxes were paid under protest in thirty-one states.[11]

The second question raised by South-Eastern went to the very legality of the state regulatory systems that had evolved over the seventy-five years prior to 1944.[12] Many states permitted (indeed encouraged) industry members to use rating bureaus to set insurance rates collectively (in other words, to fix prices). The legality of this form of price fixing, given the

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9 W. Freedman, Richards on the Law of Insurance 178 n.9 (5th ed. 1952).

10 In his dissenting opinion, Justice Jackson stated:

> The Court's decision at very least will require an extensive overhauling of state legislation relating to taxation and supervision. The whole legal basis will have to be reconsidered. What will be irretrievably lost and what may be salvaged no one can say, and it will take a generation of litigation to determine. Certainly the states lose very important controls and very considerable revenues.

322 U.S. 590 (Jackson, J. dissenting in part).

11 Insurance Field (Life ed.), May 25, 1944, at 17-20. See also the editions for March 16, 1945, at 3 and March 23, 1945, at 3.

12 Dissent by J. Jackson, supra note 10.

applicability of the Sherman Act, was problematical after the South-Eastern decision. Moreover, the seriousness and urgency of these questions was underscored by the fact that South-Eastern was a criminal matter, initiated by an indictment against South-Eastern Underwriters Association, twenty-seven of its officers and its 198 members.[13]

The Congressional debate over insurance regulation began in earnest after the Supreme Court's decision in South-Eastern was handed down. Initially, the two Houses of Congress were unable to agree on the appropriate interplay between state regulation and the antitrust laws. The Senate wanted the states to adopt regulatory systems that conformed to the Sherman Act. In the words of Senator Taft, "[w]e wish [the states] to put their houses in order by adopting laws which do not conflict with the Sherman Act."[14] The House, on the other hand, believed that state insurance regulation should not be controlled by the federal antitrust laws.[15] Another difference concerned the FTCA. Both the House and Senate had passed bills which provided that "nothing" in the FTCA "shall apply to the business of insurance, although both bills also provided that the Sherman Act and the Clayton Act would become applicable to insurance

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13 322 U.S. at 534.

14 91 Cong. Rec. 484 (1945).

15 Id. at 1084-85, 1208.

after a moratorium period.[16] But during the House debate, several members objected to the provision exempting insurance from FTCA coverage.[17] To overcome these objections, Representative Sumners, Chairman of the House Judiciary Committee, assured his colleagues that in Conference he would make the FTCA applicable to the business of insurance following the moratorium period.[18]

The McCarran Act represents the compromise worked out on these issues in the Conference Committee. It passed the House without debate.[19] The Conference Report contains little more than the draft bill.[20] Therefore, the only legislative history directly pertaining to the bill that was finally adopted is the floor debate which took place when the Senate took up the Conference report.

The Senate debate centered on the principal issue which had earlier separated the House and Senate -- when state insurance regulation authorized activity proscribed by the antitrust acts, which regulatory system would prevail? The debate makes clear that the purpose of the compromise bill was to preserve the states' authority to tax and, with certain exceptions, to regulate in ways that would violate the antitrust laws if they

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16 Id. at 1005, 1027.

17 Id. at 1027-28, 1086, 1089-94.

18 Id. at 1093.

19 Id. at 1396.

20 H.R. Rep. No. 213, 79th Cong. 1st Sess. (1945).

applied. The debate also makes clear how the statute was intended to accomplish that goal: where state law and the antitrust laws conflicted, the statute was to resolve that conflict[21] in favor of state regulation, with certain prescribed exceptions; and where there was no conflict because the states were not regulating and thus state authority was not threatened, the antitrust laws were to apply with their full force and effect.

During an exchange with Senator Pepper, Senator Ferguson, one of the conferees, summarized the bill's conflict-resolving purpose as follows:

> Mr. Ferguson: Under the language which is now in the bill as it appears in the conference report, if a state passes an act regulating insurance or taxing insurance, and that regulation is contrary to the Sherman Act or the Clayton Act, with three exceptions, then the State law would be the law. Here are the exceptions:
>
> > Nothing contained in this act shall render the said Sherman Act inapplicable to any agreement to boycott, coerce or intimidate, or act of boycott, coercion, or intimidation.
>
> * * * * *
>
> But with respect to anything else, if the States were specifically to legislate upon

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21 This is not intended to suggest that our position is that the federal government may regulate concurrently with the states. If the states are regulating, those regulations occupy the regulatory field, and the federal government is without authority to regulate, either consistently with or inconsistently with the state regulation. But in occupying the field for purposes of regulation, the states do not preempt federal authority to engage in non-regulatory activities.

> a particular point, and that legislation were contrary to the Sherman Act, the Clayton Act, or the Federal Trade Commission Act, then the State law would be binding. That is exactly what we attempted to do in this bill. It is clear what we attempted to do.[22]

Soon after this comment, the following colloquy appears.

> Mr. Ferguson: This bill would permit-- and I think it is fair to say that it is intended to permit -- rating bureaus. . . [W]e believe that State rights should permit a State to say that it believes in a rating bureau.
>
> * * * * *
>
> Mr Pepper: In other words, the Senator believes in a form of rate fixing?
>
> Mr. Ferguson: Yes. There is no doubt the bill allows it; but we believe that all the wisdom is not here in Congress. We believe that there is some wisdom left in the legislatures that they should exercise their judgment and regulate insurance, except in the respects which we have enumerated.[23]

Senator O'Mahoney, another of the conferees, summarized the purpose of the bill as follows:

> So now we endeavor to convey that power of regulation to the States -- to recognize it, I should say, rather than convey it -- to recognize as desirable [state] regulation.[24]

Senator Murdock repeated the thought:

> as the Senator from Wyoming has said, we

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22 91 Cong. Rec. 1481 (1945) (emphasis added).

23 Id. (emphasis added).

24 Id. at 1444 (emphasis added).

> convey no authority, we simply recognize [the State's] right to regulate.[25]

That the compromise bill, and especially the "proviso" to Section 2(b),[26] was simply intended to apply the full force of the antitrust laws to insurance where the states were not regulating (in other words, to preserve the residual federal authority to regulate) can be seen from the following:

> Mr. Pepper: Will the Senator read the proviso?
>
> Mr. O'Mahoney: It provides that after January 1, 1948, these several acts. . .
>
> Mr. Pepper: That is, the Sherman Act and the Clayton Act. . .
>
> Mr. O'Mahoney: Yes. They "shall be applicable" -- there is a positive declaration -- "to the business of insurance to the extent that such business is not regulated by State law," . . . . I interpret that to be a clear statement that if the States do not regulate, the power of Congress to regulate is clearly enunciated.[27]

Later in the debate, Senator O'Mahoney reinforced the point.

> . . . one of the House conferees, in the course of the conference, used this sentence, which I thought was extremely apt: "This is a bill to authorize the States to regulate the insurance business; and if the States do not regulate it, the Federal Government can.[28]

While the legislative history is filled with indications

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25 Id. (emphasis added).

26 See text accompanying notes 39-43 infra.

27 91 Cong. Rec. 1444 (1945) (emphasis added).

28 Id. at 1486-87.

that the purpose of the bill was to preserve states' authority to tax and to regulate in ways that would otherwise be proscribed by the antitrust laws, there is no evidence indicating that Congress intended for the bill to go beyond that purpose. Indeed, nowhere in McCarran's legislative history is there _any_ mention of the FTC's authority under Section 6, or its investigating and reporting functions, or that in providing for these, the FTCA was different from the Sherman and Clayton Acts. Thus, there is no evidence in the legislative history that Congress intended that the McCarran Act go beyond preserving states' legal authority, to withdrawing from the FTC authority to collect and report to the states and Congress information on how that authority might be used more effectively.

After acknowledging the absence of such evidence,[29] Aetna proceeds to argue that Congress could not have overlooked the Commission's important information gathering and reporting function and, therefore, that it must have intended to preclude the Commission's Section 6 authority as well.[30] However, if Congress had considered this issue, it is very unlikely that some indication of that consideration would not appear somewhere in the legislative history. At a minimum, the absence of any direct Congressional expressions on this issue leaves the issue an open one -- and in no event is it dispositive of the question

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29 Aetna memo, _supra_ note 2, at 5.

30 _Id_.

as Aetna would suggest.

The conclusion that McCarran was enacted to achieve a limited goal is by no means novel. Since 1945, the courts have on several occasions examined McCarran's legislative history and commented on its limited purposes. In Maryland Cas. Co. v. Cushing,[31] Mr. Justice Frankfurter observed:

> Suffice it to say that even the most cursory reading of the legislative history of this enactment makes it clear that its exclusive purpose was to counteract any adverse effect that this Court's decision in United States v. South-Eastern Underwriters Association . . . might be found to have on state regulation of insurance.[32]

Similar language appears in Wilburn Boat Co. v. Fireman's Fund Insurance Co.[33]

> The measure Congress passed shortly thereafter, known as the McCarran Act, was designed to assure that existing state power to regulate insurance would continue.[34]

Finally, Aetna argues that Congress intended to protect the states from FTC reports which might point out inadequacies in state regulation.[35] Nothing in the legislative history even suggests that Congress intended to shield the states from such information. Indeed, the opposite is true. During the debates

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31 347 U.S. 409 (1954).

32 Id. at 413 (emphasis added) (citation omitted).

33 348 U.S. 310 (1955).

34 Id. at 319 (emphasis added) (citation omitted).

35 Aetna memo, supra note 2, at 5-6.

which immediately preceded passage of the Act, several senators inquired as to what steps would be taken to assure that state regulation served the "public interest" and what would be done if it did not.[36] Assurances were given by the framers of the Act that Congress reserved the right to overturn the regulatory system permitted by the McCarran-Ferguson Act if states did not act in the best interests of their citizens.[37] It is inconsistent with the spirit of those assurances to interpret McCarran as denying the Commission's authority to report information that would permit the Congress to judge the adequacy of state regulation.

Congress' limited purpose in adopting the McCarran Act is clear from the above.[38] That purpose now defines the scope of this statute.

C. The Language of the Statute

The limited scope of the McCarran Act -- preserving the states' authority to regulate and tax -- is not only demonstrated by the legislative history; it is made clear by the language of the statute itself.

The Act states that its purpose is to "express the intent of

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36 91 Cong. Rec. 1447, 1481-84, 1487-88 (1945).

37 Id.

38 For a more complete review of the legislative history, see Weller, The McCarran-Ferguson Act's Antitrust Exemption For Insurance, History and Policy, 1978 Duke L.J. 587 (1978).

the Congress with reference to the regulation of . . . insurance."[39] The first section of the Act provides:

> Be it enacted . . . , that the Congress hereby declares that the continued regulation and taxation by the several States of . . . insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.[40]

Section 2(a) states that "the business of insurance . . . shall be subject to the laws of the several States which relate to the regulation or taxation of such business."[41]

Aetna relies heavily for its argument on Section 2(b), which provides as follows:

> (b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: Provided, that after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by state law.[42]

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39 Preamble to McCarran-Ferguson Act, c. 20, 59 Stat. 33 (emphasis added).

40 Id. § 1 (emphasis added).

41 Id. § 2(a) (emphasis added).

42 Id. § 2(b).

Aetna argues that the proviso, which states that the FTCA "shall be applicable to the business of insurance to the extent that . . . [it] . . . is not regulated by state law,"[43] (and which thus preserves residual regulatory authority in the federal government), forces the conclusion that where the states are regulating, the FTC lacks both regulatory and non-regulatory authority.[44]

The principal and controlling clause of Section 2(b) is narrowly focused on the possibility of federal law "invalidat[ing], impair[ing], or supersed[ing]" (in other words, preempting in whole or part) state insurance laws. By addressing itself to laws which might threaten states' authority to regulate, this clause brings Section 2(b), including the proviso, into conformity with the rest of the statute.

In concluding that the proviso has sweeping effect, Aetna apparently reads the proviso without reference to the principal clause of Section 2(b).[45] The restrictive "invalidate, impair,

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43 Id. (emphasis added).

44 Aetna memo, supra note 2, at 1-2.

45 It is possible that Aetna believes that the second clause is, in reality, an "exceptions clause," or, in other words, that it exempts the three antitrust statutes from the principal clause, (and its restrictive standard) and subjects those Acts only to the standards of the proviso. (For an explanation of "exceptions" clauses, see 1A. C. Sands, Statutes and Statutory Constructions § 21.11 (4th ed. 1972)). But such a reading would also be incorrect.

The legislative history indicates that both clauses were intended to refer to the antitrust statutes and thus, by implication, that the proviso should not be read as an exceptions clause but in a customary way.

(Footnote Continued)

or supsersede" standard set forth in the principal clause establishes the context for the proviso and limits its meaning.[46] Aetna's construction is therefore at odds with the well-established principle of statutory construction that the main or dominant body of an enactment is assumed to express the legislative purpose and to be controlling.[47] Moreover, when there is doubt as to

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45 (Footnote Continued)

First, Senator O'Mahoney, one of the Senate conferees, stated during the Senate debate immediately preceding Senate adoption of McCarran that both clauses of section 2(b) would apply to the antitrust acts. 91 Cong. Rec. 1444. Second, Congress had abandoned the Ferguson amendment which, as adopted by the Senate, provided "no act of Congress, except. . . the Sherman Act, and/or. . . the Clayton Act, shall be construed to invalidate, impair or supersede any law enacted by any State for the purpose of regulating the business of insurance. .. ." Id. at 487. If Congress had intended to exclude the three antitrust acts from the first clause, it could have simply retained the Ferguson amendment and added the FTC Act.

Moreover, as one commentator argues persuasively:

> Even if the proviso were treated as an exceptions clause, the "invalidate, impair, or supersede" standard of the first clause should still be applied as a minimum test for federal antitrust immunity. Since the House had adopted that standard and the Senate demanded a stricter standard, the proviso compromise could not have been anything less than that to which the House had already agreed.

Weller, supra note 38 at 605 n.91.

46 Id; but for an important qualification, see supra note 21.

47 Id; 2A C. Sands, Statutes and Statutory Construction §§ 47.08, 47.09 (4th ed. 1972).

their scope, provisos are strictly construed.[48]

In summary, the statute as a whole, and even the very section which Aetna relies on, demonstrates McCarran's limited purpose and scope: to perserve the states' regulatory and taxing authority. These may not be expanded, through an inappropriate reading of a proviso clause, into a broad prohibition against the FTC providing information and analysis that does not threaten the states' legal authority, and in fact should help the states exercise it more effectively.

D. Findings of a House Subcommittee

During 1978, the Subcommittee on Oversight and Investigations of the Committee on Interstate and Foreign Commerce held hearings on life insurance marketing and cost disclosure. As part of those hearings, the Oversight Subcommittee considered specifically the Commission's legal authority to investigate and report on the business of insurance. The Subcommittee concluded that

> . . . besides its direct regulatory authority under the FTC Act, the Commission is empowered to investigate the conduct of any corporation "excepting banks and common carriers," 15 U.S.C. § 46(a), and to make reports to Congress recommending legislation, 15 U.S.C. § 46(f). We do not think that such non-regulatory activities are affected by the McCarran Act. Cf. H. App. 30B.[49]

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48 Id.

49 House Subcommittee on Oversight and Investigations of the Comm. on Interstate and Foreign Commerce, 95th Cong., 2d Sess., Report on Life Insurance Marketing and Cost Disclosure 63 n.275 (Comm. Print 1978) [hereinafter cited as Moss Comm. Rep.].

E. A Lack of Case Law:

While the FTC's authority to investigate the business of insurance has been upheld on several occasions,[50] there are no cases which specifically address the interplay between Section 6 of the FTCA and the McCarran Act.[51]

F. Conclusions

The McCarran Act on its face, its legislative history, and findings by the House Oversight Subcommittee all support the view that the Commission has authority under Section 6 of the FTCA to investigate and report on the business of insurance whether or not states are regulating in the specific area of Commission inquiry.

II

Public Policy Reasons Why Aetna's Proposed Amendment Should be Rejected

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50 See, e.g., FTC. v. Crafts, 355 U.S. 9 (1957).

51 One commentator, after analyzing the Supreme Court's decisions concerning the McCarran Act, reached the following conclusion:

> It may be argued that the McCarran Act was designed only to restrict the FTC's power to regulate, not to investigate. This interpretation is easily justified since it would leave the FTC FTC free to gather facts for later presentation to Congress should it appear that the public interest no longer is compatible with giving the states primary authority to regulate the insurance business.

Comment, Per Curiam Decisions of the Supreme Court:1957 Term, 26 U. Chi. L. Rev. 297, 305 (1959).

The first section of this memorandum explains why Aetna's legal analysis of the Commission's Section 6 authority to investigate the "business of insurance" is incorrect. But whether or not Section 6 should be amended is not as much a question of law as it is one of public policy: what should be the Commission's future authority to investigate and report on the "business of insurance?" This section sets forth the strong public policy reasons why Congress should allow the Commission to retain such authority.

State officials attempting to regulate in the "public interest" need information about industry performance. So does the Congress if it is to know whether the continued delegation of its reponsibilities to regulate interstate commerce in the area of insurance is in the public interest.[52] To meet their respective responsibilities each must know, for example, if the industry is competing on the basis of price; if it is operating efficiently from the consumers' perspective (if it pays out in benefits a high percentage of what it collects in premiums); if consumers have the information they need to distinguish low-cost sellers from high-cost sellers (for comparable products); if attempted regulatory solutions to known problems are effective; and so on. Without information of this type, insurance regulation is a guessing game played with trillions of dollars in consumer resources. Moreover, it is appropriate for the public to have information that will

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52 U.S. Const. art. 1 § 8.

alert it to, and help it avoid, existing consumer problems. It is also appropriate that the public be advised of the effectiveness of regulatory systems adopted in its name.

The FTC is in a unique position to provide some of this information. As indicated by the National Commission for the Review of the Antitrust Laws and Procedures,[53] and demonstrated empirically in the FTC's staff report on Life Insurance Cost

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53 In its recommendations to the President and the Attorney General, the National Commission for the Review of Antitrust Laws and Procedures concludes:

> Although there is general consensus that most segments of the industry are competitively structured, and that enhanced competition is an appropriate goal of state regulatory policy, many states adhere to regulatory scheme requiring prior approval of insurance rates, thereby discouraging independent pricing behavior. The costs of continuing the present system are not insignificant: where members of a competitively structured industry are allowed collectively published industry-wide rates -- often without effective state supervision -- in a regulatory environment that encourages uniform pricing, insurance premiums are likely to be higher than under a system that relies more heavily on independent pricing decisions. In some prior approval states, regulation may in fact keep rates below levels that would be produced by competition. Unduly low rates, however, may exacerbate availability problems.

National Commission for the Review of Antitrust Laws and Procedures, Report to the President and the Attorney General 226-27 (1979).

Disclosure,[54] certain major sections of the insurance industry do not adequately compete on the basis of price. It appears that the most effective remedy to address these problems may be to provide consumers with information that will increase their ability to price shop and thereby induce sellers to compete on the basis of price. The Commission has been working with competition problems and informational remedies for over 50 years. As a result, it has developed a great deal of experience and expertise on these issues, as well as the technical skills (in economics, data processing, statistics, and others) their analysis requires. The Commission's role in the insurance area is to make its experience, expertise, and technical capabilities available to insurance policymakers to use or disregard as they see fit.

Perhaps the value of FTC analyses on insurance issues is best indicated by the demand for it. During the last two years, FTC representatives have been invited to testify before Congress on insurance issues on ten different occasions. These invitations came from committees and subcommittees of both Houses.[55] In

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54 Federal Trade Commission, Staff Report on Life Insurance Cost Disclosure 50-62 (1979).

55 During the years 1978 and 1979, Commission representatives testified before the following Congressional Committees and Subcommittees:

<u>96th Congress</u>

October 11, 1979	House Committee on Small Business; Subcommittee on General Oversight and

(Footnote Continued)

addition, over the last two years Commission representatives have been asked to testify before five states on insurance issues.[56] Moreover, during the same period of time, representatives from more than twenty state insurance commissions have, at their

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55 (Footnote Continued)

	Minority Enterprise
October 16, 1979	House Committee on Interstate and Foreign Commerce: Subcommittee on Health and the Environment
July 10, 1979	Senate Committee on Commerce, Science and Transportation
March 12, 1979	Senate Committee on the Judiciary
June 14, 1979	Senate Committee on Banking, Housing and Urban Affairs
<u>95th Congress</u>	
February 24, 1978	House Committee on Ways and Means: Oversight Subcommittee
April 10, 1978	House Committee on Government Operations: Subcommittee on Commerce, Consumer, and Monetary Affairs
June 29, 1978	Senate Special Committee on Aging
August 7, 1978	House Committee on Interstate and Foreign Commerce: Subcommittee on Oversight and Investigations
November 28, 1978	House Select Committee on Aging

56 Maine, North Carolina, Texas, Washington and Wisconsin.

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initiation, informally discussed insurance issues with the Commission staff.[57] After the release of the staff's recent economic analysis documenting the lack of price competition among sellers of whole life insurance, the National Association of Insurance Commissioners (N.A.I.C.) invited FTC representatives to appear and testify before its task force to evaluate the N.A.I.C.'s model cost disclosure regulation. In addition, because of her extensive analysis of medicare supplement insurance problems, an FTC staff member was asked to serve on an advisory committee to the NAIC Task Force on Medicare Supplement Insurance.

The evidence of the value of Commission analysis on insurance issues is not all circumstantial. Before the life insurance cost disclosure investigation was completed, but after staff had released preliminary findings, the Commission received a letter from the State Insurance Commissioners of Massachusetts, Minnesota, New Jersey, North Carolina, North Dakota and Wisconsin advising that:

> We have followed with interest the work of the Federal Trade Commission on life insurance cost disclosure. . . . We find the FTC staff comments constructive and worthy of consideration. . . . The FTC would be doing us a service by continuing with its study and by providing assistance in this

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57 These include representatives from Alaska, Arkansas, California, District of Columbia, Florida, Illinois, Indiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Nevada, New Jersey, New York, North Carolina, Pennsylvania, Virginia, Washington, and Wisconsin.

> field to those states which would benefit from it.[58]

Members of Congress have encouraged and supported the Commission in its insurance investigations. For example, after learning of certain budgetary problems the Commission was facing in funding its study of medicare supplement insurance, Senators Lawton Chiles, Frank Church and Pete V. Domenici of the Senate Special Committee on Aging wrote to the Commission and advised

> [w]e hope, however that this . . . will not preclude your initiatives in this area and that you will be able to go ahead at the earliest date possible.
>
> We would appreciate being kept informed of Commission decisions and actions and once again offer our assistance and support.[59]

Of course, every year since 1977, Congress has been informed of the Commission's involvement in the insurance area through the budget process.[60] Moreover, in response to FTC budget submissions on insurance, both Houses explicitly approved of the Commission working with the states in this area.[61]

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58 Letter from the Insurance Commissioners to Michael Pertschuk, Chairman of the Federal Trade Commission (Sept. 22, 1979), Moss Comm. Rep., supra note 49 at 815.

59 Letter from Senators Lawton Chiles, Frank Church and Pete Domenici (present Chairman, former Chairman and ranking minority member) of the Senate Special Committee on Aging, to Michael Pertschuk, Chairman of the Federal Trade Commission (Oct. 6, 1978).

60 See, [1977] Fed. Trade Comm. Prog. Budget Justification to Cong. 142; [1978] Fed. Trade Comm. Prog. Budget Justification to Cong. 143; [1979] Fed. Trade Comm. Prog. Budget Justification to Cong. 8-9.

61 In a report to Congress the Senate Committee on Appropria-
(Footnote Continued)

In addition, the President recently wrote to the State Governors advising them of his view that:

> The model regulation [developed as part of the life insurance cost disclosure project] is designed to provide meaningful disclosure of life insurance costs. Under the law, only the states can act to require this kind of disclosure. This is an important initiative the states can take to promote price competition and to ensure that the life insurance market is responsive to the needs of con-

---

61 (Footnote Continued)

tions stated:

> The Chairman of the FTC advised the Chairman of this Committee that. . . the FTC. . . on the subject of life insurance cost disclosure. . . would seek to encourage meaningful regulation of this area at the State level. The Committee does not disagree with the efforts of the Commission to work with the states. . . .

S. Rep. No. 1043, 95th Cong., 2d Sess. 74 (1978); The House Committee on Appropriations in referring to the FTC's investigation of the life insurance industry stated:

> [T]he Committee strongly recommends that the Commission not take any final action during fiscal year 1979 which might be inconsistent with the model regulation of the National Association of Insurance Commissionors. Such a course will provide time for appropriate committees of Congress to consider the matter.

H.R. Rep. No. 1253, 95th Cong., 2d Sess. 46-47 (1978). Later that year the House Subcommittee on Oversight and Investigations of the Committee on Interstate and Foreign Commerce held hearings on life insurance marketing and cost disclosure. The subcommittee concluded that the FTC had the authority to investigate the industry and that the FTC's role was "wholly lawful, proper, and appropriate." Moss Comm. Rep., _supra_ note 49 at 63.

> sumers. I hope that the resources invested in this study by the Federal government will yield a dividend of increased Federal-State cooperation. I urge you and your insurance officials to give the model regulation the most careful consideration.[62]

The compelling public policy reasons why the Commission should continue to collect and report on insurance issues were, perhaps, best stated by the House Oversight Subcommittee after it held extensive hearings on the subject:

> . . . the infusion of fresh views by an agency experienced in consumer protection activities is highly desirable. . . . [t]he size of the insurance industry, its importance to consumers, and its methods of doing business clearly justify the expenditure of some FTC resources to maintain at least an advisory federal presence.[63]

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62 Letter from President Jimmy Carter to the Governors of the 50 states (Jan. 8, 1980)(copy attached).

63 Moss Comm. Rep., *supra* note 49 at 62-63.

THE WHITE HOUSE

WASHINGTON

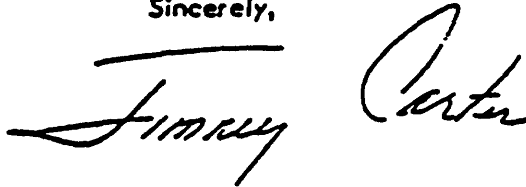
To Governor

Americans spend over $30 billion a year on life insurance premium payments. Yet too often, consumers lack the basic cost information they need to find the best policy at the lowest price. The Federal Trade Commission has recently recommended a model state regulation on life insurance cost disclosure to help achieve this purpose.

On the basis of economic study and consumer research, the Commission concluded that whole life value insurance policies not held to maturity pay a relatively low rate of return on their cash values, and that consumers are not getting the information they need to understand the true costs of their policies. The result is billions of dollars a year in unnecessary costs to consumers.

I am enclosing a copy of the model state regulation and other material which summarizes the key findings and recommendations. The model regulation is designed to provide meaningful disclosure of life insurance costs. Under the law, only the states can act to require this kind of disclosure. This is an important initiative the states can take to promote price competition and to ensure that the life insurance market is responsive to the needs of consumers. I hope that the resources invested in this study by the Federal government will yield a dividend of increased Federal-State cooperation. I urge you and your insurance officials to give the model regulation the most careful consideration.

Sincerely,



Excerpt from Senate Report 96-500, the Senate Committee on Commerce, Science and Transportation's report on the Federal Trade Commission Act of 1979.

Calendar No. 536

96TH CONGRESS
1st Session

SENATE

REPORT
No. 96-500

FEDERAL TRADE COMMISSION ACT OF 1979

REPORT

OF THE

SENATE COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

ON

S. 1991

together with

ADDITIONAL VIEWS

DECEMBER 14 (legislative day, NOVEMBER 29), 1979.—Ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE
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(II)

INVESTIGATIONS OF INSURANCE

Section 5.—Section 5 of the bill amends section 6 of the Federal Trade Commission Act. Under the amendment, the FTC's investigative and reporting powers are made explicity inapplicable to the business of insurance (except to the extent authorized under subsections 6(c) and 6(d) relating to antitrust investigations).

For purposes of this amendment, the term "business of insurance" has the same meaning as used in the McCarran-Ferguson Act, 15 U.S.C. §§ 1011–1015. The amendment would not; however, affect the FTC's power to conduct investigations, pursuant to section 6(c) of the FTC Act, to determine whether parties are in compliance with judicial decrees enjoining violations of the antitrust laws. Finally, the amendment does not affect the existing authority of the FTC, under sections 5 and 18 of the FTC Act, to carry out law enforcement responsibilities or to issue trade regulation rules to the extent consistent with the McCarran-Ferguson Act.

Section 5 is made necessary because the FTC is misconstruing the jurisdictional limitations clearly set forth in the McCarran-Ferguson Act and is engaging in unauthorized activities which cannot effectively be challenged or halted in the Federal courts.

The McCarran Act was passed in 1945 in reaction to *United States* v. *South-Eastern Underwriters Ass'n.*, 322 U.S. 533 (1944), in which the Supreme Court overruled earlier decisions holding that insurance transactions were not interstate commerce. Insurance thus became subject to Federal statutes—including the Federal antitrust laws—enacted under Congress' authority to regulate interstate commerce. The Supreme Court's decision created widespread apprehension that application of Federal laws would preempt or impair the extensive systems developed by the States to regulate and tax insurance. Accordingly, in section 1 of the McCarran-Ferguson Act, 15 U.S.C. § 1011, Congress declared its policy "that the continued regulation and taxation by the several States of the business of insurance is in the public interest." To implement this policy, section 2(b) of the McCarran Act, 15 U.S.C. § 1012(b), provides that the Sherman, Clayton and Federal Trade Commission Acts are "applicable to the business of insurance" only "to the extent that such business is not regulated by State law."

The Committee has undertaken a thorough legal analysis of the statutory language and the underlying legislative history. Both make it clear that the authors of the McCarran Act intended, where the statutory prerequisites for exemption were satisfied, that the FTC have no jurisdiction under any provision of the Federal Trade Commission Act. In particular, Congress in the McCarran Act made no distinction between the provisions of the Federal Trade Commission Act which govern the Commission's law enforcement function (principally section 5 of the FTC Act) and those which govern its separate factfinding function (section 6 of the act). In either case, where an activity comprises part of the "business of insurance" and is "regulated by State law," Congress divested the FTC of jurisdiction so as to eliminate the possibility that the State's regulatory efforts would be invalidated, impaired or superseded.

The Committee believes that additional legislative action, in the form of a clarifying amendment, is now needed because of FTC actions inconsistent with the jurisdictional limitations imposed by the McCarran Act. In testimony before Congress and in its various reports on insurance, the Commission has erroneously interpreted the McCarran Act to preclude only enforcement action under sections 5 and 18 of the FTC Act, but not factfinding investigations or the issuance of public reports under section 6.

Acting under the incorrect assumption that it has jurisdiction, in the last 18 months the FTC has devoted a considerable portion of its resources to a broad program of insurance-related investigations, many culminating in the release of highly publicized reports. In these investigations, the Commission has in effect assumed the social and economic policymaking role which Congress has reserved exclusively for the States. Two recent investigations illustrate this problem. FTC consultants are presently studying the fairness of risk classification and pricing in the area of private passenger automobile insurance, and the FTC staff is engaged in an investigation of the extent to which the Los Angeles insurance market is adequately served. Neither study was undertaken at the request of Congress.

These FTC investigations are in areas clearly outside the Commission's jurisdiction. Both focus on ratemaking and related activities which the Supreme Court has consistently held to be the "business of insurance" within the meaning of the McCarran Act. *See, e.g., SEC* v. *National Securities, Inc.*, 393 U.S. 453, 460, (1969); *Group Life & Health Insurance Co.* v. *Royal Drug Co.*, 99 S. Ct. 1067, 1078–1080 (1979). Of most serious concern, especially in light of the basic purpose of the McCarran Act, is that the Commission's investigations concern matters which are subject to extensive State regulation. Indeed, several subjects being investigated by the FTC are under active examination by State insurance departments and by the National Associaton of Insurance Commissioners (NAIC) with a view toward legislative and regulatory changes where needed. The Committee accordingly, is of the belief that such duplication should be avoided.

Section 5 would add a proviso to the end of existing section 6 of the FTC Act, 15 U.S.C. section 46, prohibiting the FTC from initiating any investigation of the business of insurance or issuing any reports, findings or recommendations on the insurance business. The amendment does not require the existence of "State regulations" as is required under the McCarran-Ferguson Act. Thus it precludes the FTC from merely studying, evaluating or criticizing the philosophy, scope or direction of State insurance regulation. However, the amendment does not affect existing authority. Section 6(d) of the FTC Act, as modified by 15 U.S.C. section 46a, which provides that the Congress or the President may direct the FTC to investigate alleged violations of the antitrust statutes and to report all facts to the Congress. Further, the amendment in no way affects the constitutionally founded legislative authority of the Commerce Committee to conduct investigations on insurance-related subjects, by such means as obtaining testimony from FTC officials or requesting the assistance of State regulatory officials. Similarly, the amendment leaves intact section 6(c) of the FTC Act, under which the Commission has power to conduct investigations and issue reports in connection with the question whether parties are in compliance with final decrees restraining violations of the antitrust laws.

Letter from David L. Ream, Professional Insurance Agents concerning May 3 testimony.

PROFESSIONAL INSURANCE AGENTS
GOVERNMENT AFFAIRS OFFICE
600 PENNSYLVANIA AVE. S.E. SUITE 203, WASHINGTON, D.C. 20003
(202) 544-8713

May 10, 1984

The Honorable Peter W. Rodino, Jr.
Chairman, Committee on the Judiciary
Monopolies and Commercial Law Subcommittee
B353 Rayburn House Office Building
Washington, D.C. 20515

Re: Subcommittee on Monopolies and Commercial Law of the Committee on Judiciary May 3, 1984 Hearing: Consumer Information - Insurance

Dear Mr. Chairman:

On behalf of PIA, I again thank you for inviting our participation in the above-captioned hearing. The issue of consumer information in any industry is very important. PIA actively participates, as our testimony and submissions supports, the development and dissemination of useful consumer information for the buyer of insurance.

There are two points I would like to restate to assure no misunderstanding of PIA's position on this issue. The first concerns our reservations regarding the issuance of price comparison lists. PIA strongly encourages price shopping by consumers. As I stated, 98% of my and my staff's time is spent giving price quotations over the phone. The homeowners quote form we use in our agency (copies were provided for the Subcommittee) clearly shows our view on price comparisons. We provide space on the form for such comparisons. These forms are given to the prospective customer. The benefit of the form is that it allows the consumer to compare apples to apples. The coverage form, ratings, amounts, deductibles and any applicable endorsements are clearly listed. All the consumer has to do is open a telephone book or ask a friend for other agents, call and ask for a comparable quote.

There have been some attempts to take over this responsibility and do the price shopping for the consumer. These attempts have been referred to as price lists and have been used - to my knowledge - exclusively in the auto area. Generally speaking, auto insurance has 161 possible class ratings. This number

1984 GOV Competition in the Insurance Industry 739p bonknote.pdf

does not include the different combinations for varying coverage limits, deductibles, applicable endorsements, and territory to name a few. As yet, PIA has not seen a general price list that has included all the possible class and coverage combinations available. Out of practicality, price lists have identified an "average" or "most used" class.

Price lists do not address the coverage application questions we raised. The consumer does not get an apple-to-apple comparison as with the homeowners form we give them. They can unwittingly be mislead. If a price list could be developed to overcome the many serious deficiencies we outlined in our written and oral statements, our concerns would be set aside.

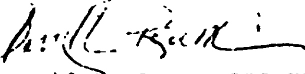
Second, PIA does not oppose consumers having the ability to inquire and be told of their agent's commissions. There are some consumers who are aware of the earnings their agent/broker receives on a piece of business. However, it is still the total cost of the package and service that counts, and upon which the consumers shop.

I respectfully request that this letter be entered into the permanent hearing record following PIA's prepared statement dated May 3, 1984.

For further information, please do not hesitate to call on Patricia A. Borowski at our Capitol Hill office. Pat will be very happy to answer your questions, provide more material and/or share your comments with our membership.

Thank you.

Sincerely,



David L. Ream, CIC,FMS
Chairman, Public Information
and Affairs Committee

PAB:mc

cc: Jonathan Cuneo, Esq., Asst. Counsel
Marilyn Falksen, Research Asst.
Alan F. Coffey, Jr., Esq., Chief
Minority Counsel

APPENDIX 3
ADDITIONAL SUBMISSION BY RALPH NADER

June 14, 1984

Chairman Peter Rodino
House Judiciary Committee
House of Representatives
Washington, D.C.

Dear Chairman Rodino:

During my testimony before your Committee last month, specific information was requested to be supplied for the printed hearing record. Accordingly, I enclose the following materials:

1. Data on auto insurance rates and profits in New Jersey and California;

2. Descriptive material on the Citizen Utility Board concept, now law in Wisconsin and Illinois statewide. You were interested in this proposal affecting utility consumer organizational rights by way of a possible approach that could be adapted for insurance policyholder rights.

3. An article describing a request for group purchase of homeowners insurance in Connecticut that was rejected by several insurance companies as constituting a "fictitious group" and upheld by the Insurance Commissioner. The article highlights just one of many state laws which were lobbied by the insurance industry in order to limit competition.

Your interest in the CUB proposal was most appreciated. If you and your staff wish to pursue this idea toward a legislative draft, please know that we stand ready to help. CUB is truly a new idea with enormously beneficial consequences for the justice and efficiency of our economy--all voluntary to the consumer and without any tax dollars required.

Sincerely,

Ralph Nader

According to the December 5, 1983 edition of Best's Insurance Management Reports, New Jersey passenger auto rates were the highest in the nation, averaging $456. California rates, far from being the lowest, were sixth highest in the nation, averaging $358. The average for the nation was $275. Thus, New Jersey rates were 27% higher than California.

This is not surprising. According to the US Department of Transportation, there are 130.7 cars per mile of highway in New Jersey (33,692 miles of highway and 4,402,000 registered cars). In California, the comparable figure is 80.6 cars per mile of highway (173,888 miles of highway -- 14,016,000 cars). Thus, New Jersey traffic density is 62% higher than California, and this does not factor in the increased traffic density New Jersey "enjoys" as the country's leading "corridor" state.

In fact, for the US as a nation, the traffic density is 32.4 cars per mile of highway, which surely is the paramount reason for New Jersey and California's high auto insurance prices.

We also reviewed miles driven, and find that California drivers drive 2.8% more miles than New Jersey drivers who, in turn, drive 2.6% more than the national average.

On a profit basis, California property/casualty insurers earned all lines profits 24% above the national average for 1977-1981, whereas New Jersey insurers profits were 85% below the national average.(1) This occurred during a period of time when, according to Forbes magazine, property/casualty insurer profits were 41% above the profits for all industries in America (although property/casualty insurers are of average or below-average risk compared to all American industries).

(1) Source: Reports on Profitability by Line and by State of the National Association of Insurance Commissioners.

CUB Testimony by Ralph Nader before the N.Y. Public Service Commission, January 26, 1984, Albany, New York

Chairman and members of the Commission, thank you for providing me the opportunity to appear before you today to discuss the creation of a Citizens' Utility Board in New York State. The Citizen Utility Board (CUB) model is a self-starting new approach to public participation in energy policy-making that deserves your support. The CUB concept is something that many liberals and conservatives endorse, because it provides a greatly needed mechanism for effective ratepayer representation at no cost to the taxpayer.

CUB is a nonprofit statewide organization that primarily represents residential consumers on energy, electric, gas, telephone and water issues before government bodies. It receives no tax dollars and is funded by voluntary contributions. Members govern the organization by democratically electing a board of directors.

What is most unique about CUB is that it is given the right to enclose notices inside monthly utility bills to communicate with the public and solicit memberships. CUB pays for this enclosure. "Piggybacking" the utility's mailing is a convenient and effective way to communicate with residential utility consumers. It also provides a basis for economic self-sufficiency and financial accountability. Any residential utility consumer can join CUB by contributing a minimum amount each year ($5.). Each member has one vote in the elections for a statewide board of directors. These directors decide what CUB should do and

allocate funds accordingly. The directors who serve without pay, hire full-time staff people such as accountants, attorneys, economists, organizers, and lobbyists. The staff can intervene in rate proceedings, lobby the legislature, research issues of concern to consumers, survey public opinion on energy issues, provide analysis of utility complaint handling, and provide information and assistance to consumers interested in conserving energy.

CUB is designed to balance the utility regulatory process. Utility companies each spend tens of thousands of dollars of ratepayer money to advocate their interests before the Public Service Commission (PSC) and the legislature. Residential consumers as a group have a substantial interest in these issues; however, they lack the resources, organization, or expertise to respond to utility company arguments. In fact, the complexity of the process effectively prohibits many individuals from participating at all.

Most efforts to right this imbalance have failed to provide representation that is both technically competent and accountable to consumers. Some citizen groups have tried to fill this void by intervening. While the contributions of such groups have been valuable, much more needs to be done. The Consumer Protection Board and the Attorney General's office make important contributions to the rate making process-- both, however, represent all ratepayers--not just residential ratepayers. And while these units of government are now responsive to the

concerns of most citizens-- under a different administration they may not be as responsive. Moreover, state agencies cannot encourage public participation in the decision-making processes the way a knowledgeable and broader-ranging statewide citizen-funded, citizen-controlled organization can.

Utility bills now sap away 10-15% of the average household's income-- and as much as 25-50% from the elderly. Compounding the financial aspects of the utility burden is the frustrating feeling that there is nothing anyone can do about it--nothing that is, but pay the bill. Consumers of utilities are helplessly captive.

The Wisconsin experience demonstrates CUB's potential. Since November of 1980, when the first enclosures were mailed, over 92,000 residents have joined Wisconsin CUB. The first elected board of directors included a local union representative, an educator, a farmer, and an environmentalist. With its first year budget of $250,000, the board hired an economist, an attorney, a lobbyist, a researcher, and an organizer. Following the agenda set by the board, the staff has successfully challenged utility rate increase attempts, successfully opposed a local measured telephone service proposal, lobbied the state legislature, studied the consumer complaint handling process of the Wisconsin Public Service Commission, and conducted educational programs on energy.

The Wisconsin experience has shown that the enclosure process is

inexpensive and that it imposes no financial burden on the utility companies. Most importantly, Wisconsin CUB has proven that thousands of people will join and become actively involved in such groups. While CUB's primary objective is to represent consumer needs by promoting utility efficiency and fairness, CUB is not always at odds with utilities. For example, Wisconsin CUB has worked with utilities and the PSC in developing conservation and education programs. The chairman of the Wisconsin Public Service Commission expressed unqualified approval of CUB, labeling it as "indispensable in utility rate hearings" for its role in bringing competition to the Commission proceedings.

Three states have now adopted CUB proposals--the Illinois legislature passed CUB in July of 1983 and it was signed into law by Governor James Thompson in October of that year. The California Public Utility Commission recognized a CUB organization in the San Diego area in March of 1983, that already has 55,000 members. CUB is also being introduced in the Rhode Island legislature in February, it is scheduled to go on the ballot in Oregon this November, it is scheduled for consideration by the Montana Public Service Commission in March and it is scheduled to be introduced in West Virginia this week.

Last year Governor Cuomo put forth a legislative proposal to create one statewide CUB. The Assembly passed CUB by a vote of 143 to 3. No action was taken by the Senate. On September 9, 1983, Governor Cuomo asked this Commission to consider adopting a CUB proposal. This action by the Governor deserves praise. By

advocating CUB, which has great potential to promote citizen participation in the energy policy-making arena, the governor has compensated for the Senate's failure to recognize the contribution citizens could make through a Citizens Utility Board. As Governor Cuomo, an avid CUB supporter has said, "In numbers, there is power. By joining together through the Citizen's Utility Board, individual citizens will have a stronger voice in our utility practices."

Neighbors Discover Themselves 'Unreal' in Eyes of Insurance Companies

Nathra Nader

Not long ago, several neighbors and I were referred to by the Connecticut Insurance Department as a "fictitious group" and therefore were not allowed to buy homeowners insurance as a group.

The department was not discriminating only against us. None of you or your neighbors are able, under Connecticut law, to save money by buying homeowners insurance as a group. The law is to the insurance companies' liking, as we found out when we wrote the following letter to The Travelers Cos., Aetna Life & Casualty and Cigna Corp.:

"We are homeowners who are concerned about the high price of homeowners insurance. In researching costs, we see that companies pay commissions of about 20 percent, have 'other acquisition' expenses of about 5 percent, and other overhead of about 6 percent, for a total of over 30 percent of the rate.

"It seems to us that this would be sharply lowered if a group policy were written (similar expenses for group health insurance often are in the 5 percent to 10 percent range).

"We have talked to many of our neighbors who would like to save money as well. If we could put together a group and would volunteer to do premium collection and some other services for you, would you quote us a group rate? If agents must be involved, how low could they lower their commission, in your estimation?"

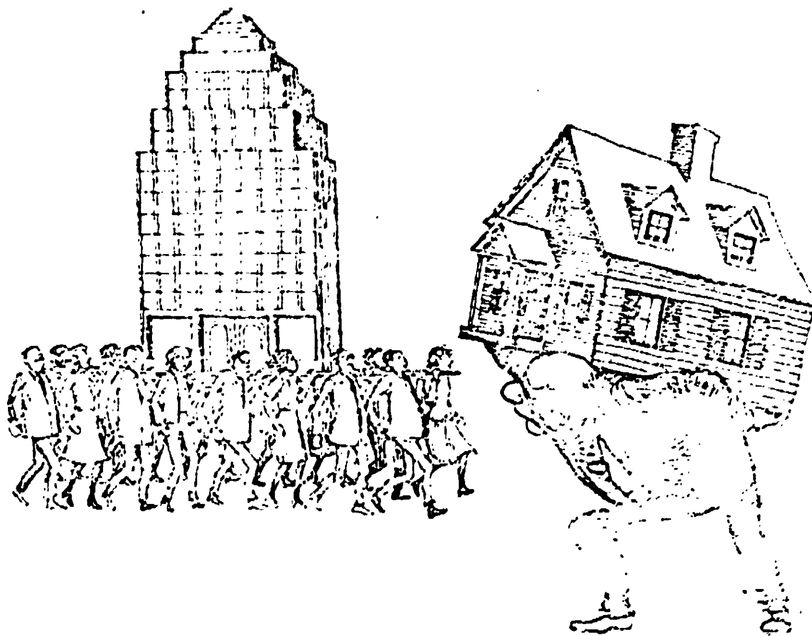
All three companies referred to Connecticut law, which prohibits what Cigna described as "a group of neighbors or townspeople" from buying a group policy. All three companies conveyed their support for such a law. The state insurance commissioner, Peter W. Gillies, agreed with the companies. He urged us to shop the marketplace of 150 homeowners insurers in the state.

In his letter Gillies wrote that Connecticut law "effectively says that it is unfair to an insurer's other customers to give a preferred price to a 'fictitious group' of customers." Group health and group life insurance are sold throughout the state. Why is homeowners insurance not sold to groups of any kind — "fictitious" or real (whatever the latter means)?

An additional implicit bias operates in the 37 states that have these bans on so-called fictitious groups. The law thinks that employees of a company constitute a "real" group, but that neighbors constitute a "fictitious" group. This bias undermines the strength of neighborhoods to band together and use their group bargaining power to obtain less expensive policies and better service.

The insurance industry generally does not like federal or state regulation. At the same time, the industry supports state regulation of consumers to keep policyholders from using the marketpace to work for them. This may fairly be called a double standard that invites either judicial or legislative correction. It is these laws, and not neighborhood groups, that should be viewed as "fictitious." They should be repealed.

Nathra Nader, a retired businessman, lives in Winsted.



APPENDIX 4

June 28, 1984

Letters submitted by Roy Woodall, Jr., Executive Vice President, National Association of Life Companies, showing cost to two small insurers of complying with life insurance cost disclosure regulations.

SOUTHERN EDUCATORS

LIFE INSURANCE COMPANY

Ike F. Williams, Jr.
Executive Vice President

November 17, 1980

TO: Roy Woodall, Executive Vice President
National Association of Life Companies

Roy, in our conversation of last week, you asked that we review General Bulletin No. 29 94 of the American Council of Life Insurance regarding life insurance cost disclosures. We have, at your request, hurriedly tried to apply what we feel to be a conservative cost estimate of the expense of implementing this totally new consumer disclosure approach.

Southern Educators is a small life insurance company with approximately 13,000 policies in force. We are writing new policies at the rate of approximately 4,000 per year. We are computerized on an IBM System 3, Model 10 and have 22 salaried home office employees with 30 managers in the field and approximately 120 agents. We are licensed in only three states. Our premium income during 1980 will be approximately $4 million and our investment income will be approximately $1 million. I will attempt to apply cost to the major items which we feel this consumer cost disclosure would entail.

	COST
ITEM 1 - All policy forms would require refiling with each insurance department and a specimen preliminary policy summary would need to be filed with each policy form.	
Anticipated Cost Here Would Be	$ 5,000.00
ITEM 2 - We would be required to give at the point of sale (or first interview) the following disclosure: A buyer's guide, suitability form and preliminary policy summary would be required at each interview given by our field force whether or not a sale is made. We estimate our field force gives 15,000 interviews per year and that this information would cost $2.50 per interview.	
Cost Per Year	$37,500.00

Mr. Roy Woodall -2- November 17, 1980

COST

ITEM 3 - All application forms would need to be redesigned and reprinted in order that the agent could attest his compliance at the point of sale to this customer cost disclosure. We use two insurance department approved applications.

Cost of Reprinting and Redesigning	$ 2,500.00

ITEM 4 - At delivery of the insurance policy, a full policy summary for the specific plan purchased is required. We currently sell only 10 plans of insurance. We estimate cost disclosure factors could be generated outside our office for $500 per plan.

Cost for Factors	$ 5,000.00

We also estimate at the time of computer issue we could generate this full policy summary for approximately $1 per policy issued.

Cost Per Year	$ 4,000.00

ITEM 5 - An annual disclosure form is required each year and must be designed to cover two policy years for comparative purposes. This disclosure must be mailed on an annual basis to each policy owner. For our 13,000 policies in force, we feel to generate and deliver this annual disclosure would cost $2.50 per policy.

Cost Per Year	$32,500.00

ITEM 6 - Retraining of our agency force for this new cost disclosure would be a must. We estimate retraining cost for 30 managers to be $250 per manager and retraining cost for 120 agents to be $150 for each agent.

Managers Training	$ 7,500.00
Agents Training	$18,000.00

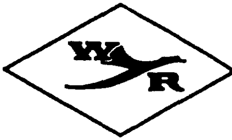
	COST
ITEM 7 - Hardware and software costs must also be considered. We feel our hardware would be adequate to handle this cost disclosure even though it is more extensive than the current cost disclosure. We are currently computerized for the cost disclosure now required. We estimate to develop the programs necessary to comply with this proposed cost disclosure would require an investment of approximately $12,500 if we did all the necessary changes in house.	
Software	$ 12,500.00
TOTAL FIRST YEAR IMPLEMENTATION AND ON GOING COST	$124,500.00

We realize some of these items would possibly be non-reoccurring; but, Roy, we would like to call your attention to the fact that in 1979 Southern Educators' statutory gain was $137,854. This changing horses in the middle of the stream would certainly have a tremendous financial impact on companies that are smaller than we and on companies that are larger than we. We feel this should be taken into consideration when this new cost disclosure is being discussed.

SOUTHERN EDUCATORS LIFE INSURANCE COMPANY

Ike F. Williams, Jr.
Executive Vice President

IFW,Jr/t



WESTERN RESERVE LIFE INSURANCE COMPANY

To: Policyholders

This is to inform you that effective July 1, 1984, Western Reserve Life Insurance Company will cease all sales operations in the State of Colorado for an indefinite period of time. This action is necessary because of regulatory actions taken by the Insurance Board for the State of Colorado and the excessive cost to be subjected on Western Reserve Life to implement such regulations. Copy of my letter attached.

Regretfully this will affect 130 agents with a payroll of approximately $300,000.

Sincerely,

WESTERN RESERVE LIFE INSURANCE COMPANY

J. King Clemons
President

JKC/am

Home Office • 2755 North Ave. • P.O. Box 609 • Grand Junction, Colorado 81502 • Ph 303/242-6291

NOTICE TO ALL AGENTS AND SALES MANAGERS
IN
THE STATE OF COLORADO

Effective July 1, 1984, Western Reserve Life will suspend all sales activities in the State of Colorado.

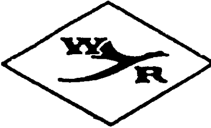
The Insurance Division for the State of Colorado through the Colorado Insurance Board have promulgated Regulation 84 - 1 concerning life insurance solicitation. This solicitation regulation is completely foreign to that which is used in all other states that use this kind of regulation and uses indices that at this point in time have not been developed in any state. A copy of the regulation is attached.

The economic impact on Western Reserve Life is felt at this point in time to be too severe to continue sales operations in Colorado. A copy of the most recent testimony to the Insurance Board is also attached.

We regret this action as we feel we have been a good citizen in the State of Colorado and fully understand that this will affect 130 agents and a payroll annually of approximately $300,000.

Telegrams and letters concerning this action should be sent directly to:

Mr. John Kezer
Commissioner of Insurance
State of Colorado
1st Western Plaza Bldg.
303 W. Colfax - 5th Floor
Denver, CO 80204



WESTERN RESERVE LIFE INSURANCE COMPANY

September 21, 1983

Commissioner of Insurance
106 State Office Building
Denver, CO 80203

Dear Dick:

I am responding both to the September 1, 1983 Insurance Division hearing on cost disclosure as well as to your letter of September 1, 1983 to State Representative Jim Robb.

You indicated that the Colorado cost disclosure regulation is patterned off of the NAIC model, which of course is true, however, it varies to very significantly in the regulation, indicies and consumer guide that separate items will have to be developed to compliance with the Colorado regulation.

I believe in the hearing you indicated a personal preference of a small policy exemption, of which I obviously would be in favor.

You also indicated in your letter to Jim Robb that you had some disagreement with my numbers on cost and indicated in the hearing that it was not Colorado's intention to require comparison with other companies rather only the indice be provided.

Accordingly, I would like to update our involved costs:

o Colorado Life Insurance Buyer's Guide	$ 7,650.00
o Redesign of applications	$ 2,500.00
o Policy summaries	$ 8,500.00
o Cost of programming including purchase of a non-compatible program, purchase of compiler, purchase of labor for conversion	$60,000.00
o Retraining of agents	$12,000.00
	$95,650.00

Since we sell approximately 1500 policies a year average increase in cost per policy per year of $63.77. If that is spread over five years an average cost increase each year for five years of $12.75 per policy.

Next I would like to address the Buyer's Guide. Page 100 of the 1983 catalog published by Pictorial Publishers, 8081 Zionsville Road, P.O. Box 68520, Indianapolis, Indiana 46268 (copy attached) shows that 15,000 of the NAIC Buyer's Guide costs only $1,335.00 while the Illinois and Maine Buyer's Guide costs $1,198.00 for 20,000 copies, somewhat less. We have a cost for the Colorado Life Buyer's Guide produced locally of $7,650.00, a huge differential. Additionally, a two page policy summary run off on a photocopy machine in your office would cost .50¢ each.

Home Office • 2755 North Ave. • P.O. Box 609 • Grand Junction, Colorado 81502 • Ph 303/242-6291

1984 GOV Competition in the Insurance Industry 739p bonknote.pdf

Once again, I strongly urge that if Colorado truely believes this is in the public interest and absolutely necessary then we should move to the NAIC model despite the fact that it would cost me three years profits to pay for it.

Sincerely,

WESTERN RESERVE LIFE INSURANCE COMPANY

J. King Clemons
President

JKC/dg

CC: Jim Robb
Vickie Armstrong
Tillie Bishop
Stanley Johnson

Submitted for the record by Bill Gunter, President of the National Association of Insurance Commissioners and Insurance Commissioner of the State of Florida.

(The attachments referred to in Mr. Gunter's statement are on file with the Subcommittee.)

WRITTEN SUBMISSION BY BILL GUNTER AS PRESIDENT OF THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS AND INSURANCE COMMISSIONER OF THE STATE OF FLORIDA

I.

INTRODUCTORY REMARKS

Mr. Chairman and Members of the Subcommittee, I appreciate the opportunity to submit the following comments.

I am presently serving as Insurance Commissioner of the State of Florida and as President of the National Association of Insurance Commissioners; however, ten years ago I represented Florida in the House of Representatives. As a result, I feel that I have a somewhat unique ability to appreciate the perspective of both the members of this Subcommittee and the state insurance regulators on insurance issues.

Let me begin by stating emphatically that I am in total agreement with the testimony which has been presented that it is essential that adequate information be provided to insurance consumers. However, I disagree with the argument that insurance consumers under state regulation have not been provided with that information. In addition, I disagree with the opinion that enhanced federal regulation will lead to better protection of insurance purchasers from potential abuses. Based on my experience, the states have made significant progress in getting information to consumers and I feel the states are in a better position than the federal government to respond to the needs of insurance consumers and to effectively regulate the transaction of insurance.

Before addressing the issue of consumer awareness, I would like to offer some general observations concerning the McCarran-Ferguson Act.

The McCarran-Ferguson Act was passed by Congress in 1945 in response to the U. S. Supreme Court's decision in United States v. South-Eastern Underwriters Association. For about 75 years prior to the SEUA case, insurance transactions had been considered not to constitute "commerce" thereby placing the business of insurance beyond the scope of the federal

antitrust laws. In SEUA, the Supreme Court held that the previous line of cases related only to the validity of state regulation in cases involving the taxation of insurance and not the federal government's power to regulate interstate activities of the insurance business. In effect, the Supreme Court held that insurance business was interstate commerce and thus subject to the federal antitrust laws.

Until the SEUA decision, the regulation of insurance had been left almost exclusively to the states and, therefore, by the 1940s, state regulation was well established. The Supreme Court's decision, however, catapulted the insurance industry and state regulation into a period of uncertainty and potential chaos. Congress, however, after careful study, recognized the unique aspects of the insurance industry and the special abilities of the states to protect the insurance consumer and responded by adopting the McCarran-Ferguson Act. The Act constituted federal endorsement of state regulation and taxation of the insurance business. The Act also created a general antitrust immunity for the business of insurance that was regulated by state law and provided that the specified acts of boycott, coercion or intimidation by the insurance industry remain subject to the antitrust laws.

Thus, after numerous hearings and extensive study, Congress decided it was in the public's best interest to preserve state regulation of insurance. The NAIC agrees with that Congressional mandate and believes that the McCarran-Ferguson Act continues to be in the public's best interest.

From the perspective of a state insurance regulator, the McCarran-Ferguson Act contains two critical provisions. First, that no Act of Congress shall be construed to impair or supersede any state law enacted for the purpose of regulating insurance; and second, that the Sherman Act, Clayton Act and the Federal Trade Commission Act are applicable to the business of insurance if that business is not regulated by state law.

Apparently this subcommittee is considering the narrow issue of whether or not the antitrust immunity of the insurance industry should be preserved or, more specifically, whether the Sherman and Clayton Acts should be fully applicable to the business of insurance. However, there is some ambiguity in this regard and there have been some rather general comments to the effect that this subcommittee is considering repeal of McCarran-Ferguson in its entirety. I would hope that the subcommittee has no such intent.

I feel that competition supplemented by effective state regulation is working and there is no need to subject the insurance industry to federal antitrust legislation. However, I would also stress that outright repeal of McCarran-Ferguson or the application of the Federal Trade Commission Act to the business of insurance would be an error of monumental porportions. Any such action would result in the applicability of general federal laws which conflict with state regulation. Under the supremacy clause of the Federal Constitution, this would result in the invalidation of state insurance laws and the demise of state insurance regulation.

I would also like to briefly address the belief, apparently held by some, that the federal government is somehow better equipped to regulate insurance than the states.

During the 100-plus years since the United States Supreme Court decision in Paul v. Virginia, the states have developed a great deal of expertise and detailed regulatory systems based on state statutes as interpreted in enumerable court decisions.

The diverse regulatory systems developed by the states permit experimentation with new concepts and with solutions to recurring problems in the real world but on a limited basis. In addition, where geographically localized problems are present, a single state or a small number of states where the problem is presented can quickly deal with the problem legislatively and administratively. The pluralistic and adaptable system of state regulation has proven itself more able to regulate the business of insurance than a monolithic and sometimes ponderous federal approach.

Two relatively recent examples of the benefits of state insurance regulation come to mind--the so-called verbal threshold in automobile no-fault statutes and the wage loss reimbursement system in workers' compensation insurance.

No-fault automobile insurance began as a concept only. It was first implemented in Massachusetts. When it worked, a number of states including Florida enacted no-fault statutes.

However, as time passed, a problem became evident in Florida. Our state, like many others, had a dollar threshold of medical expenses which had to be surpassed in order to initiate civil action against a negligent driver. The amount in Florida was $1,000 and after a few years of experience, it became evident that the law was less and less able to curtail the filing of negligence actions; with rising health care costs and experienced attorneys, it was very easy to incur $1,000 in medical expenses.

In response to the problem, the Florida Legislature scrapped the dollar threshold and substituted a verbal threshold. Now a civil court action may be initiated for pain and suffering only if there is a permanent injury, permanent loss of a body function, permanent significant scarring or disfigurement or death.

The amendment of the Florida No-fault statute to adopt a verbal threshold has enabled the law to again function as intended--to reduce the exorbitant number of lawsuits arising from automobile accidents. Other states are considering or have adopted similar verbal thresholds.

Another example of rapid and effective state regulation is in the field of workers' compensation insurance. Five years ago in Florida, workers' compensation insurance premiums paid by Florida employers were soaring. The workers' compensation system was designed to avoid litigation and to assure that injured workers received benefits expeditiously. However, five years ago, protracted and costly litigation was rapidly becoming the rule rather than the exception. Customarily, attorneys received a substantial portion of the award which should have gone to the claimant himself.

In large part, the reason for the proliferation of litigation was the basis upon which compensation awards were determined. Except for extreme cases, such as loss of a hand or eye where a schedule was used, each individual industrial accident had to be rated as a percentage of disability to the body as a whole. This determination would involve intricate questions of fact and proof and, therefore, attorney involvement was required. To correct this situation, the Florida Legislature adopted a wage loss reimbursement system under which claimants are compensated on the basis of actual wage loss rather than subjective determinations of the value of bodily injury.

Implementation of wage loss reimbursement resulted in an immediate and substantial reduction in workers' compensation insurance premiums and has caused a decrease in both the frequency and duration of litigation. As a result, more of the insurance premium is flowing to injured claimants and benefits are paid more quickly than before. Florida's experiment with wage loss has been a resounding success and a number of other states with problems similar to those experienced by Florida in the past are considering implementation of the wage loss system.

The no-fault verbal threshold and workers' compensation wage loss are good examples of state insurance regulation at work. I would like to contrast those examples with the experience we had for almost 8 years with self-funded multiple employer

health care programs established by entrepreneurs and marketed in purported compliance with the Federal Employee Retirement Income Security Act (ERISA).

ERISA, as its name implies, was primarily designed to deal with pension plans. However, during the final stages of its consideration by Congress, the act was extended to encompass health care programs as well as retirement plans. In addition, a broad preemption provision was included indicating that ERISA programs were exempt from state insurance regulation.

In my opinion, the extension of ERISA to deal with health programs was ill conceived. While the legislation devotes a great deal of attention to the funding of retirement plans, no standards or provisions were included to assure adequate funding of health care programs.

Further, given the broad definitions contained in the law and the broad preemption, a number of entrepreneurs established purported ERISA plans, marketed the programs to employers in a number of different states and purported to be exempt from state insurance regulation. State regulatory officials were forced to initiate civil litigation in order to close down the programs. Typically it took over a year to secure sufficient information in order to establish state jurisdiction and to prevail in these actions. As a result, while the litigation proceeded, the programs continued in operation and oftentimes became insolvent leaving many millions of dollars in unpaid claims throughout the country. In Florida alone, at least eight of these programs were marketed and later became insolvent, leaving several million dollars in unpaid claims. (The Employee Security Benefit Association, the National Business Conference Employee Benefit Association, and the First Foundation Trust are examples.)

The states dealt with the problems as best they could. The NAIC pointed out the problems of the entrepreneural programs as early as 1976. (Activity Report of the House Committee on Education and Labor, House Report No. 94-1785, January 3, 1977) However, it was not until January of 1983, some 8 years after ERISA's effective date, that the Erlenborn-Burton Act was passed limiting ERISA's broad preemption and again providing clear jurisdiction to the states to regulate non-collectively bargained programs covering employees of different employers which should never have been exempt from state regulation in the first place.

The states have demonstrated an ability to quickly address problems and adopt needed refinements on a local basis and in an expeditious manner. When the practical operation of a program or new theory indicates the need for change, the states have been able to quickly take remedial action. In contrast, in one of the few federal incursions into the insurance field, a fundamental and costly mistake was made which then took eight years to remedy.

II.

AVAILABILITY OF CONSUMER INFORMATION

Turning from these preliminary comments, I would now like to describe what is being done in Florida to make certain that consumers are given accurate and comprehensive information regarding insurance. The Florida Department has at least 5 different means of providing information: (1) A network of service offices, (2) A Consumer Hot Line, (3) Consumer brochures, (4) Consumer Outreach Presentations, and (5) News media.

1. Service Offices

The Bureau of Field Operations in our Division of Insurance Consumer Services employs about 116 people in 20 offices throughout the state of Florida. Personnel in these offices are responsible for providing consumers with programs and services to explain benefits, coverages and costs, to assist with claims problems and to otherwise help Florida insurance consumers.

The local offices of the Department are staffed with professional insurance specialists who are available to discuss and provide assistance with regard to a wide variety of inquiries and complaints. When needed, the local offices receive assistance from the Department's central offices in Tallahassee, which includes a staff of 18 attorneys.

The local service office provides the consumer with a place where he can meet and talk with the agency regulating insurance and where he can go for consultation and advice concerning insurance problems. It is a place where the consumer can go to speak with a local representative who is known in the community. It is a place where the consumer can obtain needed information regarding insurance prices, policy provisions, and policy benefits in order to make informed decisions regarding insurance coverage.

The local service office provides consumers with an opportunity to discuss insurance problems and concerns with knowledgeable representatives who have no financial interest in the transaction being discussed. One of the paramount responsibilities of the service offices is to protect insureds from unfair trade practices by agents and insurers. The service office also provides prompt intercession on behalf of consumers when needed to assure that their interests are guarded and that benefits due are promptly paid.

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To give you some idea of the extent of the activities of the Florida Department's service offices, in the 1982-83 fiscal year, the Bureau of Field Operations and its service offices handled 638,349 telephone calls. We estimate that approximately one-half of the contacts involve inquiries regarding rates and coverage for automobile, health and life insurance.

In addition, the service offices logged 72,318 actual consumer visits during the 1982-83 fiscal year. And, as a result of the visits and phone calls, in 50,856 instances the service offices initiated formal action in order to assist consumers. These actions ranged from simple telephone calls to administrative prosecutions of agents and companies.

In addition to providing consumer information, these local offices provide an early warning system for the Department enabling us to identify patterns of problems such as delay in claims payments which may reflect financial problems of an insurer. Also, through those inquiries, the service offices often are able to detect violations by agents or companies which might not otherwise come to the attention of the Department.

For example, one of our South Florida service offices recently received a request for general information regarding automobile insurance rates. The consumer received a copy of the Department's automobile shoppers' guide indicating typical rates charged by 20 different insurers. He attempted to obtain coverage from one of the insurers and was advised that there were no agents in his geographic area. He again contacted the service office which identified an agent in an adjoining county. However, upon contacting that agent, the individual was advised that the insurer would not write coverage in the county in which he resided. The individual again contacted the service office. As a result, a further examination was conducted and administrative charges were filed against the insurer for refusal to write business in the county in question. The issue was finally resolved upon the insurer's payment of an administrative penalty and agreement to write coverage in the geographic area in question.

2. Consumer Hot Line.

The Florida Department currently has 4 toll-free WATS lines available to consumers. The telephone lines are staffed

by experienced insurance specialists who provide assistance regarding a variety of insurance complaints, problems and inquiries.

Presently we are receiving an average of 4,000 calls per month. Of this number, 75% of the calls are terminated by providing guidance and assistance over the telephone. The remaining calls require further correspondence and in some instances a visit to the service office.

The Department maintains a log identifying the nature of each inquiry and if a complaint or violation is indicated, the nature thereof and the identity of the insurer. This information is then consolidated in a computerized records system. As a result, persons calling the toll-free line or a local service office have access to information regarding Department experience with any given company or agent. In addition, the consolidated recordkeeping aids the Department in identifying recurring problems industrywide or on a company-by-company basis. In addition, this system will indicate recurring inquiries and allow the Department to determine those areas in which to concentrate its consumer education efforts.

3. Consumer Brochures, Consumer Outreach Presentations and News Media.

The service offices and toll-free telephone lines provide a means for the consumer to ask questions and seek assistance, as well as a means for the Department to respond. However, in addition to simply responding to consumer inquiries, the Department has also taken the initiative and developed a variety of programs to actively seek out the consumer and provide needed information to the general public.

(a) Shoppers' Guides.

The Department's Bureau of Consumer Research and Education has developed a number of consumer oriented publications. This program provides facts and information on insurance policies and the law, as well as price comparisons of auto, homeowners and medigap contracts with no charge to the public. Beside the above-mentioned publications, there are a variety of other booklets distributed covering topics of life, health, mobile home, accident insurance and reports on insurance companies. (Composite Attachment)

During the fiscal year 1982-83, the Department distributed 308,760 of these booklets to the consumers of Florida.

(b) Consumer Outreach Presentations.

Another consumer program in Florida which formally began July 1, 1983, is the Department's consumer outreach presentations (COP). Under this program, our professional employees conduct or participate in organized programs on specific insurance topics which are presented to various groups in each community. The purpose of these presentations is to have the group become more acquainted with insurance products, sales, coverages, costs and the law regulating insurance.

In an attempt to penetrate every segment of the State's population, we have addressed numerous consumer groups such as senior citizens, residential communities, schools and business groups. For a six (6) month period ending December, 1983, the field offices were responsible for conducting a total of 1,693 COP's. To illustrate the growth and interest of the public for these programs, there was only a total of 949 consumer presentations made during the entire 1982-83 fiscal year.

(c) News Media.

A final method used by the Department of Insurance in educating the public is the aggressive use of printed and electronic news media. Many Department personnel, myself included, often take part in radio and television programs on a variety of topics in order to educate the public regarding various insurance issues. The Department's Bureau of Consumer Research and Information generates press releases on a continuing basis which are widely used by the media in disseminating information on important insurance issues. In addition, the Department provides a column in a question and answer format which is used in a number of newspapers throughout the state to provide answers to questions frequently asked by consumers.

III.

STATUTES AND RULES

In addition to the various programs just described which were specifically developed to provide necessary information to insurance consumers, the Florida Department has also been instrumental in effectuating a wide variety of statutes and rules which are designed to assure that consumers receive accurate and comprehensible information from agents and insurers regarding insurance coverages.

1. Unfair Trade Practices.

Florida's Unfair Insurance Trade Practices Act (Attachment 1) contains a number of general statutory provisions requiring the dissemination of accurate information to insurance consumers. Among the more important provisions are:

(a) Section 626.9541(1)(a) which prohibits misleading statements or omissions generally.

(b) Section 626.9541(1)(b) prohibiting false information and advertising and

(c) Section 626.9541(1)(l) prohibiting misleading or incomplete comparisons of competing insurance products.

The Florida law is based upon a Model Act developed by the National Association of Insurance Commissioners. The NAIC Model or similar legislation has been implemented in all states.

2. Policyholders' Bill of Rights - §626.9641.

The Policyholders' Bill of Rights (Attachment 2) was enacted in Florida in 1976 and provides several general requirements regarding consumer information which have been used by the Florida Department of Insurance as authority for various rules relating to the marketing of insurance.

The statute provides in part that:

"(a) Policyholders shall have the right to competitive pricing practices and marketing methods that enable them to determine the best value among comparable policies...
(c) Policyholders shall have the right to insurance advertising and other selling approaches that provide accurate and balanced information on the benefits and limitations of a policy...
(f) Policyholders shall have the right to a readable policy."

3. Life Replacement and Health Replacement Rules.

Based upon the general statutory prohibitions of twisting and making unfair or deceptive statements or omissions by those transacting insurance (§626.9541), Florida has adopted detailed rules governing the replacement of both life and health insurance coverages.

The Rules are based upon model provisions drafted by the National Association of Insurance Commissioners and protect insurance consumers by establishing minimum standards of conduct to be observed by agents and insurance companies where the replacement of a policyholder's life or health insurance coverage is involved. The procedures and information required by the rules assure that the policyholder will receive sufficient information to make an intelligent decision between his existing coverage and new coverage being proposed. The rules also reduce the opportunity for misrepresentation or incomplete disclosures.

(a) Rule 4-24.
Rule 4-24 relating to replacement of Life Insurance (Attachment 3) requires that a Notice prescribed by the Department be completed by the replacing agent and left with the insured. The Notice emphasizes the importance of receiving comparative information from the existing and replacing insurer and indicates some of the factors to be considered in replacing life insurance coverage, including limitations on coverage and the incontestable clause which provides that coverage cannot be challenged after a life policy has been in effect for two years. In addition to the general information provided by the Notice, both the replacing insurer and the existing insurer are required at the request of the consumer to provide comparative information describing the benefits and costs of the two competing policies. This information enables the insured to make an informed decision concerning the replacement of his life insurance coverage.

(b) Rule 4-44.
Rule 4-44 relating to the Replacement of Accident and Health Insurance (Attachment 4) requires agents to complete and leave with the insured a Notice developed by the Department of Insurance. The Notice points out a variety of factors which should be considered before replacing existing coverage such as the fact that pre-existing conditions may not be covered by the replacing insurer.

4. Readable Policy Requirements.

In 1977, the Department promulgated a rule requiring that automobile insurance policies be "readable," that is, "designed to be read and reasonably understood by a person without special knowledge or training" (Attachment 5).

Thereafter in 1982, the State Legislature enacted a statute requiring that all new policy forms used in Florida for all types of insurance coverage had to be in a readable format. (§627.4145, Florida Statutes, Attachment 6).

The statute requires to the extent possible the use of plain English and also requires the use of section headings and a table of contents in order to allow the insured to find specific provisions he may have questions about.

It is our feeling that requiring that policies be readily comprehensible is a major step in assuring the existence of informed insurance consumers. The readable policy law when combined with the statutory requirement that any policy form delivered in Florida must be approved in advance by the Department of Insurance (Section 627.410, Florida Statutes, Attachment 7) assures that consumers will be able to understand the provisions of their insurance contracts and allows for the identification and correction of misleading or deceptive provisions before harm occurs.

5. Medicare Supplement Disclosure.

In order to assure that purchasers of Medicare Supplement insurance coverage obtain accurate, complete, and comprehensible information, the State of Florida has enacted the Florida Medicare Supplement Reform Act (Sections 627.671 - 627.675, Florida Statutes, Attachment 8), Rule 4-46, governing the solicitation of Medicare Supplement insurance policies (Attachment 9) and Rule 4-51 which establishes detailed requirements as to the content of the coverage and the information provided by the insurer to the insured (Attachment 10).

On June 9, 1980, Public Law 96-265 was signed into law. This law (the Baucus Amendment) was designed to address some of the abuse in the sale and marketing of Medicare Supplement policies by providing for the application of federal minimum standards to Medicare Supplement policies. Florida was the first state in the nation to have its Medicare Supplement program approved under the federal guidelines.

But even prior to the passage of Public Law 96-265, Florida was active in regulating the sale of Medicare Supplement policies. On July 1, 1979, a Department rule (4-46) was implemented providing for the regulation of the direct solicitation and sale of these policies. It was a safeguard to assure that persons eligible for Medicare benefits would not be subjected to unfair or deceptive acts or practices by licensed agents.

Some examples of the acts or practices we were determined to eliminate and which, among others, were included in our rule were:

(1) Making any verbal or written statement which implies or conveys the impression that any Medicare supplemental insurance plan is affiliated with or authorized by the Federal government.

(2) Making any misrepresentation or incomplete comparison, by commission or omission, for the purpose of inducing or tending to induce Medicare eligible persons to purchase or otherwise change existing insurance.

(3) Performing any act which causes an applicant to sign any form, application or document in blank.

(4) Utilizing any sales material or presentation which does not disclose that an insurance product is involved.

Our Rule 4-46 also requires the completion of a certification form, signed by the agent and the applicant, in which the agent certifies that he has explained the provisions of the policy applied for and that he has clearly explained that any benefits of this plan are a supplement to any benefits the applicant may be entitled to receive from the Medicare program of the Federal government.

In addition, Rule 4-51 and the Florida Medicare Supplement Reform Act (Sections 627.671 - 627.675, Florida Statutes) require disclosure of a variety of information relating to effectuation of individual and group Medicare Supplement policies. Included are requirements that:

(a) The policy specify renewal provisions on the first page which clearly state the duration of the coverage,

(b) The policyholder agree in writing to effectuation of any riders or endorsements which would reduce benefits or increase premiums,

(c) The policy specifically identify under a separate caption and Pre-Existing Conditions Limitations, and that

(d) The policy define the terms "usual and customary," "reasonable and customary" or words of similar import establishing standards for the payment of benefits.

Perhaps most important of all, Florida's statute and rule require delivery of an outline of coverage at the time application is made, which clearly describes the coverages provided by Medicare and the supplemental benefits provided by the insurer. The Outline of Coverage must contain a brief summary of major benefit gaps in Medicare Parts A & B and, among other requirements, a description of supplementary benefits or a statement that the policy does or does not offer coverage from a required list of supplementary benefits. Provisions with respect to renewability or continuation of coverage are also included in this outline as well as the amount of premium for the policy.

I would note that the Outline of Coverage required by Florida is patterned on a Model form adopted by the National Association of Insurance Commissioners in June of 1979, which was specifically incorporated into the later Baucus Amendment.

6. Outline of Coverage.

Section 627.642, Florida Statutes (Attachment 11) requires that an Outline of Coverage be provided in conjunction with every individual or family accident or health insurance policy delivered in Florida. Section 626.99, Florida Statutes (Attachment 12) establishes a similar requirement as to life insurance.

The Outline of Coverage is in effect a simplified version of the policy and it allows the policyholder to better understand the important points in the policy.

The Outline of Coverage must be delivered with the policy or when the application is taken. It is reviewed in advance by the Department to determine that it identifies the category of coverage and gives a brief description of the benefits and coverages. It is also reviewed to make sure it gives a summary of the exclusions, limitations, reductions, deductible, co-insurance, any age restriction, renewal and cancellation provisions, as well as premium payable.

7. Advertisements of Health and Life Insurance Coverages.

The State of Florida has implemented detailed rules governing the advertising of both life and health insurance coverages (Rule Chapters 4-6 and 4-35, Composite Attachment 13). Among the more important provisions of these rules are requirements that the format and content of advertisements shall be sufficiently complete and clear to avoid deception or the tendency to mislead or deceive; that benefits, premiums and losses covered be clearly described; that exceptions, reductions or limitations on coverage be clearly identified; that provisions relating to renewability and termination of coverage be clearly described; and that the insurer and policy form advertised be clearly identified.

The Department's service offices have been extremely useful in identifying advertising violations. In addition, the advertising rules require insurers to maintain advertising files in their home offices (Rules 4-6.18 and 4-35.17). The Department periodically conducts market conduct examinations and reviews the insurer's advertising files. During the 1983 calendar year, the Department examined the advertising materials used in the State of Florida by 264 companies.

The Department imposes stringent penalties on companies determined to have violated our advertising rules. We have required insurers to discontinue distribution of questionable materials and have also in some instances required insurers to distribute corrective advertisements and explanations.

During the calendar year 1983, as a result of market conduct examinations and referrals received from our service offices, the Department imposed administrative penalties totalling $169,750 against 28 insurers as a result of advertising violations.

8. Life Insurance Cost Disclosure.

Section 626.99, Florida Statutes (Attachment 12), requires life insurers to provide prospective consumers with information to assist purchasers in determining which policies may best fit their needs. This information includes a buyers guide, a summary of policy provisions, and cost disclosure indexes to assist in comparing similar policies.

The cost disclosure indexes include a net payout cost index and a life insurance surrender cost index for 10 and 20 years for comparison purposes. The annual premiums and guaranteed death benefits for the first five years and for representative years thereafter, are also required as is information regarding guaranteed surrender values, policy loan interest rates and policyholder dividends. If the insurance proposed is intended to replace existing insurance, then the company whose policy is being replaced

must be notified in order that a detailed comparison of the policy being replaced and the proposed policy may be made. The Florida law also requires that use of a life insurance cost index be accompanied by a statement that indexes are useful only for comparison of the relative costs of two or more similar policies as well as a statement that dividend projections are based on the insurer's current dividend scale and are not guaranteed.

These procedures provide substantial information to consumers for the purpose of assisting the consumer in comparison shopping among the wide variety of products available. All of the materials presented to consumers should be used in the decision making process. No single comparative measure such as a cost index, can address all of the differences among consumers as to their personal needs, the type of insurance most suited to fill their needs, and the wide variety of benefit combinations available in the market.

The Florida Department of Insurance is always concerned with finding ways to improve consumer awareness as well as improving the amount and quality of information available to consumers. While, to date, no single cost index has been developed in Florida or in the nation which is adequate to serve by itself as a measure which can take all policy variations and consumer differences into account, the Department and the NAIC continue to search for meaningful innovations aimed at improving consumer awareness and information.

The issue of life insurance cost disclosure is an extremely complex one. It has proven extremely difficult to devise a method which will provide a means of comparing dissimilar life policies. And it has been difficult to develop a means of comparison which can be readily understood by the average insurance consumer.

The NAIC has devoted a great deal of time and effort to this issue. For example, the 1980 Interim Report of the NAIC Task Force on Life Insurance Cost Disclosure (Attachment 14) presents a summary of a variety of possible systems of disclosure and recommends a method which in effect would provide consumers with an indication of the percentage of premium dollars over the life of the policy which the insurer is likely to retain for its expenses and profits.

Further refinements of a system of cost disclosure are presently being considered by the NAIC in order to deal with this complex issue and to provide insurance consumers with a means of accurately comparing the costs of competing life products.

* * *

The various statutes and rules described above help to make sure that insurance consumers are provided with complete and reliable information concerning insurance products marketed by insurance agents and companies.

And there are ample avenues for the state to pursue in enforcing those requirements, including criminal and civil penalties, cease and desist orders, injunctions, removal of officers and directors and imposition of fines. Perhaps most important of all, state insurance laws typically authorize the revocation or suspension of the license of any insurance agent or company violating any statute or rule regulating the transaction of insurance. In effect, an insurer or agent violating any of the requirements mandating disclosure of consumer information does so at the risk of loss of the authority to transact business. As a result, the Florida Department has generally not encountered many serious violations of these requirements.

And, in this regard, while I have used Florida as an example, many of our state's laws and rules are derived from one or more of over 100 different models developed by the NAIC. All states have regulatory provisions which are comparable to those which have been described. Coupled with the benefits of pluralistic state regulation is the fact that in those instances where common problems are presented or where uniformity of regulation is necessary, the states through the NAIC have an ability to provide homogeneous solutions as well. As a result, insurance consumers generally have access to sufficient information in order to make intelligent decisions with regard to the purchase of insurance.

IV.

STATE REGULATION IS NEEDED TO SUPPLEMENT COMPETITION

Collectively, the state programs and regulatory measures described above help to assure that competition is working properly in the insurance industry.

However, in discussing the issue of state regulation, I feel it is important to comment on one of the recommendations of the National Commission for the Review of Anti-Trust Laws and Procedures. The Commission concluded that states should place maximum reliance on competition and that state rate setting regulations and other forms of anti-competitive economic regulation should be avoided.

In this regard, I would emphasize that the sale of insurance involves the sale of a promise of future performance, and because of this, unbridled competition is not appropriate in the field of insurance. One of the primary objects of state insurance regulation has always been company solvency. This goal is just as important now as it ever was. At present in the state of Florida, there are approximately 40 insurers which are being rehabilitated or liquidated by our Department. State regulation to make certain that insurance rates are not inadequate continues to be a very real responsibility.

On the other side of the coin, state regulation is necessary to protect against excessive rates. State rate regulation is a necessary complement to competition.

In Florida, the standard of review for automobile insurance rates is founded on the principle that rates should be neither excessive, inadequate nor unfairly discriminatory. The Department of Insurance employs professional actuaries who review rate filings when filed to determine whether sufficient actuarial justification is submitted with regard to the rates selected by the various insurers. In the last two years, numerous rate filings have been challenged as excessive by the Department of Insurance through legal notices which required the insurer to submit additional information and further justify its rate level. As a result of these legal notices, rate level reductions for the top ten companies alone amounts to approximately $16,000,000 since January of 1982.

One aspect of assuring that automobile rates are neither excessive nor inadequate which has been particularly significant in recent years is the consideration of investment income in automobile insurance rate making. The consideration of investment income in insurance rate making recognizes the fact that an insurer can during periods of high interest income, realize a portion of its total needed return based upon income generated from investment of policyholder supplied funds. In response to this fact, the Department of Insurance in Florida promulgated an administrative rule whereby an insurer is obligated to consider the impact of investment income in setting the underwriting profit allowance included in its rates. Simply stated, if an insurer is realizing increasing levels of investment income from policyholders funds, the underwriting profit needed by the insurer to realize a reasonable rate of return must be correspondingly reduced.

The initial review of automobile insurance rates to determine whether they are excessive, inadequate or unfairly discriminatory generally occurs when the rates are initially filed. Thus, rate setting by insurers and the review function by the Department is on a prospective basis, and in effect is an exercise in prognostication. However, predictions based on past experience are often distorted by legislation which reduces insurers' exposure and hence losses. For example, implementation of a verbal threshold for no-fault insurance and the wage-loss basis for claims payment in workers' compensation insurance created windfall profits for insurers. Consequently, when these reforms were implemented, the Florida Legislature determined that as to both automobile and workers' compensation insurance, it was necessary to supplement prospective rate review with an excess profits law.

Through implementation of the excess profits law, the Department of Insurance examines the underwriting profit realized by an insurer or insurer group over a three year period to determine on a retrospective basis whether the underwriting profit actually realized by the insurer or insurer group exceeds the underwriting profit which it has anticipated in its rate filings by more than an additional 5% of earned premium. If the actual underwriting profit in fact exceeds the anticipated profit, plus 5% of earned premiums, any profit above this level is designated excessive profit and is returned to policyholders through refunds or renewal credits. Since 1977, more than $97 million dollars have been identified as excess profits for auto insurance in Florida. Further, the Department of Insurance has identified approximately $19 million dollars in excessive profits for workers' compensation insurance for the first review period spanning the period from 1979 through 1981.

The fact that state regulation is a necessary complement to insurer competition is further demonstrated by the variety of residual market mechanisms in evidence in the various states. If governed only by the forces of competition, insurers simply would not insure certain types of loss exposure or certain individuals. As a result, state regulation establishing automobile insurance assigned risk plans and medical malpractice and windstorm underwriting associations has been required in order to assure that needed coverage is available for certain individuals or types of exposure. In Florida, we have recently enacted legislation creating a Comprehensive Health Association in order to assure that health insurance coverage is available to all residents of our state.

Under state regulation, insurance has become far more competitive than it was when the McCarran-Ferguson Act was first passed. The rating bureaus have become more and more advisory and information gathering organizations and are becoming less of a factor in rate setting.

Competition is presently working in the field of insurance. Life insurance is one of the few products which costs less now than it did in years past. And the decrease in cost cannot be entirely explained by increased longevity. Life insurers are competing with one another in marketing different types of coverage. I think most of you are familiar with the activities of A. L. Williams and others in marketing term life insurance on the theory "buy term and invest the difference". And the traditional insurers are competing with one another by creating new products such as Universal Life and Variable Life and by adopting such innovative measures as non-smoker discounts.

In the field of Workers' Compensation insurance, despite the fact that our statute provides for prior approval of filings of the National Council on Compensation Insurance to which all insurers subscribe, it is estimated that almost 40% of the business insured in Florida is written pursuant to downward rate deviations filed by individual insurers as permitted by our statutes.

Competition is working in the field of automobile insurance. If you examine Florida's Consumers' Guide to Auto Insurance, you will find that typical rates charged by the 20 largest-volume insurers vary from over 100 to 200% in each area of the state.

Under the McCarran Act, the federal government retains the authority to prevent the worst forms of anti-competitive behavior--boycott, coercion and intimidation. In addition, Congress has the authority to regulate specific insurance matters if it feels a need to do so. Consequently, there appears to be no need to modify the McCarran Act.

Repeal or even modification of the McCarran-Ferguson Act would restrict and could even prevent effective state regulation of the insurance industry. I do not believe that is the intent of the subcommittee. On behalf of the State of Florida and the National Association of Insurance Commissioners, I would ask that the members of the subcommittee not initiate any action which would have a debilitating effect on state regulation.

The states have established a regulatory network to protect the insurance consuming public by monitoring the solvency of the insurance companies and the cost and availability of insurance products. State regulation is dynamic. States are in the unique position to respond effectively when problems arise in different lines of insurance or in different parts of the country.

State insurance regulation is working well. To the extent there may be problems, the states have historically demonstrated an ability to deal with those problems in an effective and expeditious manner. History proves that in most instances if a regulatory problem is perceived, it is better to attempt to solve the problem within the existing context of regulation rather than scrap the entire system and substitute another. I urge you not to impair state regulation and substitute federal regulation which will pose different and as yet unforeseen problems--problems which I fear will be greater than any perceived shortcomings of state insurance regulation.

State regulation does not needlessly or unduly burden competition. To the contrary, insurer competition complemented by effective state insurance regulation will in my view help to guarantee that insurance consumers will get the future benefits promised in their insurance contracts, that the choice between competing products will be an informed one and that the price paid will be the lowest possible, consistent with concerns for insurer solvency.

Submitted for the record by James H. Hunt, representing the National Insurance Consumer Organization.

Statement of

James H. Hunt, FSA, MAAA
National Insurance Consumer Organization

on

RELATIVE COST DISCLOSURE IN LIFE INSURANCE

before the

Subcommittee on Monopolies and Commercial Law
Committee on the Judiciary
U. S. House of Representatives

June 28, 1984

I am a Fellow in the Society of Actuaries and a member of the American Academy of Actuaries. I began in the life insurance business in 1955 with National Life of Vermont. In 1965, I was appointed Commissioner of Banking & Insurance in Vermont and served until 1969. Since that time I have worked as an actuary with the state insurance departments in New Hampshire (1972-1976) and Massachusetts (1976-1980). I served as an actuarial consultant to the Federal Trade Commission in 1980. I testified before Congress in 1967, 1969 and 1979 on consumer credit insurance; also in 1979 I was the lead-off witness in support of S. 2002, a bill that would have restricted the use of the Rule of 78 in consumer credit. I prepared the technical aspects of ex-Senator John Durkin's testimony during the life insurance hearings of 1974 when he was Commissioner of Insurance in New Hampshire. I have been a member of many committees and task forces of the National Association of Insurance Commissioners (NAIC). I have testified before insurance departments in several states, in addition to those I worked in, on life insurance cost disclosure matters. Since 1980, I have been associated with the National Insurance Consumer Organization (NICO), a non-profit consumer organization formed with the assistance of Ralph Nader; for two years, I was a half-time employee of NICO, and I continue as a director and, to a large extent, as the organization's voice on life and health insurance. Since January 1, 1983, I have been employed four days a week as an actuary with Massachusetts Savings Bank Life Insurance, an organization that sells low cost life insurance through savings banks in Massachusetts under statutory authority and limitation on amount (currently $62,000 per person).

I am the author of a consumer guide published and distributed by NICO called How To Save Money On Life Insurance, which has sold more than 10,000 copies. NICO provides a computerized "rate of return" service to its members that I devised and administer: we estimate the average annual interest rate implicit in the savings portion of any cash value life insurance policy (one that combines death protection and savings, as distinguished from term insurance that provides pure death protection only). We believe that rate of return disclosure is the only effective and understandable way life insurance consumers can (1) comparison shop for cash value life insurance and (2) tell whether it pays to buy cash value coverage instead of term insurance. In 1979,

344 Commerce Street
Alexandria, Virginia 22314
(703) 549-8050

I completed a draft of a paper entitled The Case for Rate of Return Disclosure in Life Insurance, which was distributed to a number of trade association and company actuaries and others interested in the technical aspects of this subject. In 1980, I prepared a discussion of an actuarial paper, An Extension of the NAIC System for Life Insurance Cost Comparisons by Charles L. Trowbridge, FSA, former Chief Actuary of the Social Security System, that recommended a technical correction in the NAIC index method to make it more useful; I supported the change, though I expressed my opinion that rate of return disclosure was far more helpful to consumers. I have supplied copies of these two papers to the Subcommittee staff as a way of adding technical support to some of the comments I will make in my testimony.

I want to discuss relative cost disclosure in life insurance. What does this mean and why is it necessary? Life insurance is a long-term, intangible purchase of considerable financial complexity; in legal terms, it is a "contract of adhesion," meaning that any contractual ambiguities are construed against the company issuing the contract, presumably because the typical buyer can't be expected to bargain for the purchase at arms length. In its financial make-up, there are at least two, and usually more, streams of benefits and payments stretching far into the future, indeed, often for a lifetime. In its simplest form, there would be, for any age at issue, sex and smoking or other classification, one level death benefit and one level premium -- a $50,000 whole life policy with a premium of $1,300, for example, that develops a certain cash value pattern, starting at zero and reaching $50,000 at age 100, usually. If the cash value pattern were standardized for all companies, shopping would be relatively simple: find the policy with the lowest premium. But in practice, for any given amount of insurance, premiums vary in a wide range, cash value patterns vary correspondingly, and many of the lowest cost companies pay dividends, whose incidence and slope vary widely, as well. Even if death benefits are level from year to year, which they need not be, consumers are faced with trying to manipulate two or three long series of differing cash flows -- premiums, cash values, and, usually, dividends -- if they are to compare different companies' policies. The obvious impossibility of doing so gave rise to the (NAIC) Model Life Insurance Solicitation Regulation.

The NAIC Model Regulation requires the disclosure of a reasonable amount of the cash flow information mentioned above. The heart of the regulation, for purposes of comparing relative costs of policies from company to company, is the index numbers -- the "Surrender Cost Index" and the "Net Payment Cost Index". Taking into account the time value of money at 5% interest, these indexes -- known as interest-adjusted cost indexes -- attempt to summarize the cash flows mathematically into average annual "costs" for ten and twenty years, periods of time most critics would agree are sufficiently representative. Armed with the disclosed index numbers, theory has it that consumers can compare them among companies and choose the company with the lowest cost index.

With this background and in full recognition that volumes have been written and spoken about life insurance cost disclosure over the last fifteen years, all to little avail, I have the following relatively brief opinions about the effectiveness of the NAIC Model Regulation in serving the needs of life insurance consumers.

The NAIC Relative Cost Indexes Are Useless To Consumers

The Surrender Cost Index (SCI) and Net Payment Cost Index (NPCI) in recent years have become subject to extreme distortions that will be identified shortly, but even if this were not so the life insurance consumer faces great difficulties in using the indexes:

1. The twin disclosures of SCI's and NPCI's leave the consumer in the position of being whipsawed by competing agents between the two indexes. The agent for a company with low NPCI's will argue that since the consumer does not intend to surrender his contract after ten or twenty years (indeed, which of these does the consumer focus on?), he or she should buy on the basis of NPCI's. Technically, the SCI is a better measure of lower long-term cost for the continuing policyholder. The twin disclosures were a compromise in the early 1970's between competing industry factions: dividend paying companies and non-dividend-paying companies, the latter often having lower NPCI's and higher SCI's. The compromise ensured that neither faction would lose market share, and it also ensured consumer confusion. It is noteworthy that the NAIC Buyer's Guide accompanying a policy advises that the SCI "is useful if . . . cash values [are] of primary importance to you. It helps you compare costs if . . . you were to surrender the policy . . ." In fact, the SCI is useful whether or not one surrenders his policy in ten or twenty years for two reasons: the cash value thereby taken into account is an asset of the policyholder of obvious value whether surendered or continued; and, the higher the cash value the less the future amounts at risk and, all other things equal, the lower death protection costs in subsequent years.

2. A technical deficiency of the NAIC disclosure indexes (that Trowbridge's modification would correct) is that they may not be used to compare dissimilar policies. This means, especially, that term and cash value policies may not be compared. The Buyer's Guide advises, "Your first step is to decide . . . the kind of policy you want. Then . . . [use] the life insurance cost indexes . . . Compare index numbers only for the kind of policy you intend to buy." The technical deficiency happens to produce lower cost indexes for whole life than term, other factors equal, and it would be a naive observer who did not think this fact is used by many agents to sell whole life rather than term that may be more suited to the buyer's financial security. Even if this critical weakness is overlooked, it is further the case that high premium whole life policies can appear less costly than low premium whole life policies, even though an accurate measure of cost would show them to be inferior. This can be seen in Appendix A, where State Mutual ranks ahead of Massachusetts SBLI in 20-year cost indexes -- $13 to $27, apparently a wide margin -- yet SBLI's rate of return (yield) over all periods is significantly higher. (The rate of return technique is a more accurate relative cost measure.) There are technical reasons for this distorted result connected to the difference in premiums --

$236 for SBLI and $331 (40% higher) for State Mutual. No standard definition of "similar policies" is available to aid the consumer (or financial writers and others who advise consumers) in interpreting this limitation; the NAIC Buyer's Guide says, "The closer policies are to being identical, the more reliable the cost comparison will be." Anyone who knows anything about the life insurance business knows that there are virtually limitless combinations of protection and savings in cash value policies; it is only an accident that two policies are nearly "identical."

Combine these barriers to consumer understanding with the fact that sales of life insurance almost always take place in an environment that makes comparison shopping difficult: the buyer eyeing a $4.36 SCI has no means of knowing whether the number means the policy is high or low in cost. Even if he calls in another agent and is lucky to see a similar policy, he only knows which of these two companies is likely to be cheaper; in fact, he may be dealing with two high-priced companies. In other words, the index numbers have no intrinsic meaning. (This weakness has led several to suggest the need for a "yardstick" to accompany the disclosure of the indexes, so that the indexes would have context for consumers, but it is highly unlikely that any salesperson in America will ever have to tell his prospect where his product ranks on a scale of 10.) On the other hand, one who is advised that his rate-of-return over twenty years is 4% is likely to spot a poor consumer value; conversely, a 9% return would convey the notion of good value, particularly if the agent explained the tax advantages of life insurance.

It is NICO's opinion that the NAIC Model Regulation is useless to consumers -- any narrow advantages in comparing nearly identical policies are offset by the potential for use of the indexes to manipulate consumers into buying high-priced cash value policies instead of low cost term or high premium whole life policies instead of low premium whole life policies.

(The NAIC indexes are more useful in comparing term insurance prices, where the technical deficiency is irrelevent. One could make a good case for using the NAIC indexes on term insurance and a rate-of-return technique on cash value policies.)

Rising Interest Rates Have Distorted The Indexes

During the 1960's, industry critics began to complain that comparisons of life insurance policies were being made improperly because the time value of money was not taken into account under the "net cost" method of comparing policies. The net cost method for ten or twenty years was simply to add up premiums, subtract the total of dividends, if any, and subtract the last year's cash value; the method assigned the same weight to $1 due in, say, twenty years as to $1 due immediately. The consequence was that lower net costs could be achieved by raising premiums (due immediately) and holding back portions of early dividends -- which could be improved over the years not only with interest but as a result of not paying such portions to those who dropped their policies or died in the intervening years -- for later payment in larger amounts. The notion of interest-adjusted

indexes -- later the NAIC NPCI's and SCI's -- arose during this time, and the proposal of an industry group was for an interest rate of 4%. About 1976, this interest rate was increased to 5%, where it remains today. In 1968, Moody's Composite Average of Yields on Corporate Bonds was 6.5%; in 1976, it was 9.0%; today, it is in the range of 13%-14%. In both 1968 and 1976, the use of 4% and 5% was reasonably related both to after-tax company investment returns and to savings yields available to average investors. That is no longer true. Many companies are now crediting upwards of 10% or 11% to new policies (and sometimes older, non-borrowed policies). The spread of more than 5 percentage points between earnings rates and the 5% interest-adjusted rate is more than the difference between the old net cost method that 1960's critics complained of, which technically was an "interest-adjusted" calculation at 0%, and the 4% originally used by companies in the early 1970's.

Why does the failure of the industry to change the 5% interest rate in the interest-adjusted calculation matter? One reason is that it narrows considerably the range of policies that can be considered "similar," since a whole life policy with high premiums per $1,000 gets a rapidly widening advantage as interest rates increase. A second reason is that SCI's become negative numbers, often quite large negative numbers, causing further confusion to non-mathematicians trying to understand the NAIC system. Sellers of universal life policies, advertising rates of interest of as much as 12%, put out index numbers for the sake of complying with the NAIC regulation that have no meaning to either the companies selling the policies nor their customers; in many cases, they don't even bother to compute the indexes using the current interest rate, since the result is ridiculous. The president of a prominent universal life company, one of the first companies to have such a product, told me the NAIC indexes were completely irrelevant to his operations.

Why, then, do the companies continue to go through the motions of producing the index numbers? Since their systems are in place, the cost of doing so slight and the presence of even a flawed relative cost disclosure system helps diffuse industry critics: few, if any, authorities complained to bother to take time to understand why the indexes are not working.

The NAIC System Fails To Help Consumers Decide Whether To Replace Old Policies

In recent years, the replacement of older cash value policies with new ones has become endemic. Most consumers who have been persuaded to cash in their old policies have acted against their own interests. The process resembles "churning" in the securities business, where brokers trade in old securities for new ones to generate commissions. The analysis of whether or not to give up an old policy for a new is exceedingly complicated, and such systems as are in place in some states to aid consumers are either not helpful or, worse, give the state's imprimatur to the replacement.

It is technically feasible to prepare interest-adjusted index numbers on old policies so that they may be compared with new ones -- Mr. Trowbridge's method is suited to this goal. But the NAIC disclosure system cannot be used to compare old and new policies

because they are, by definition, dissimilar. A few years ago, a report of the Virginia Insurance Department suggested that a new replacement regulation in that State could in the future include index numbers suitable to aid consumers in evaluating replacements, but nothing ever came of this.

When an agent recommends replacement, he or she is tinkering with someone's personal property and should be held to the highest standards of ethical and professional behaviour. In life insurance, there are no such standards; suggestions by me in several forums that there be a suitability requirement for replacements have been dismissed by the industry. The failure of the industry and its regulators to make any effort to change the system of cost disclosure to apply to existing policies is consistent with the notion that the public's life insurance assets are fair game for churning.

Implications of Universal Life for Cost Disclosure

In 1981, universal life policies constituted 2% of the market; in 1984, it is estimated that sales of such policies will capture 25% of the market. The advent of such policies, which are a form of cash value life insurance featuring the disclosure of the interest rate credited to policy cash values, is somewhat ironic. Those of us who have been calling for rate of return disclosure -- such as the Federal Trade Commission in its 1979 report -- found that market forces supplied what we were unsuccessful in urging. At the least, the unprecedented success of universal life proves we were not wrong in arguing that the public would respond positively to such disclosure. But, of course, universal life has its own set of misleading and confusing disclosures. Two companies can advertise the same interest rate, but wide differences in the array of sales, administrative and death vprotection charges can make them completely different consumer values.

In its May 1984 issue, Best's Review, a popular industry trade publication, compared the universal policies of 200 companies. The specifications were, to a large extent, standardized: a $2,000 annual premium for a male non-smoker age 45 with a death benefit of $100,000 plus the policy cash value. Cash values were shown after 1, 5, 10, 15 and 20 years at an assumed interest rate of 10%. This standardized analysis allowed one to see just what differences the assortment of sales, administrative and death protection charges could make in the cash values. The table below summarizes the best and worst companies:

	Cash Surrender Values		
Years Held	Best Company	Worst Company	Difference
1	$ 1,760	$ 0	$ 1,760
20	94,081	66,304	27,777

Note: One company showed better figures than USAA Life, the "Best Company", but its figures appeared to be wrong. The study's design does not allow accurate comparisons for 5, 10 and 15 years.

The differences noted are, of course, astonishing. The present worth

at 10% interest of $27,777 due at the end of 20 years is $4,128, so we could say the consumer shopping for a policy is faced with making more than a $4,000 wrong choice in his purchase decision (considerably more than $4,000 if years beyond 20 are taken into account). And we have not factored in the lower benefits on death into this $4,000 number.

Another way of way of looking at the differences between the two policies illustrated is to assume that the best policy really does return 10% interest over 20 years (a reasonable assumption, though NICO's rate of return service would show 9.6%). By actuarial analysis, we can work out that "Worst Company's" real yield is not 10% but about 7.8%. For a ten year period, the USAA policy returns about 9.0%, while "Worst Company" returns about 4.8%. Perhaps it is not analogous, but the Truth-in-Lending Act requires Annual Percentage Rates to be accurate to an eighth of one percent.

The relatively high premium used by Best's -- $2,000 -- tends somewhat to obscure differentials in sales, administrative and death protection charges when advertised current rates of return in universal life policies are compared with derived rates of return by the method NICO uses -- known as a "Linton Yield" to actuaries. A Life of Virginia agent recently presented one of Massachusetts SBLI's customers a proposal for that company's universal policy, which on the date of the proposal was advertised as yielding 11%; SBLI currently credits 9.44% to cash values in its dividend formula. By the use of a particular combination of whole life and term riders, SBLI was able to show that for the same annual premium its policy had slightly higher death benefits throughout a twenty year comparison period and, at the end of 20 years, had higher a cash value -- $15,222 to $9,340. When subjected to NICO's rate of return analysis over twenty years, SBLI yielded 9.2% and Life of Virginia only 5.4%, more than five percentage points lower than it was advertising. Appendix B shows this comparison in more detail.

In short, there is no NAIC system for letting consumers know that 11% in one company means something entirely different from 11% in another company. It doesn't take a lot of imagination to see that life insurance agents all over the country are having a field day with universal life. It is bad enough that consumers are fooled into buying what appear to be high-yield policies; what is worse is that many are enticed into giving up older policies whose prospective rates of return are higher than those implicit in universal life policies.

Consumers Would Benefit From Rate of Return Disclosure

When consumers buy a non-standardized package of death benefits and savings, whose mix can vary almost infinitely, they cannot by any stretch of the imagination discern whether the package represents good or bad value without some help. The purchase of a cash value life insurance policy is analogous to the purchase of a bag of papayas and guavas; unless someone tells you how many of each are in the bag and unless you're well informed about the fair price for each, there's no way to know how much to pay for the bag. Even if life insurance buyers were told the mix of savings and protection, they don't know how much the protection should cost so that they can work out the price of (return on) the savings; the calculation is too difficult, anyway. But

the industry knows what fair value is for protection, and can easily provide standardized rates of return to consumers; the calculation is made with the same data as that for the interest-adjusted calculation.

Such rate of return discloasures would aid consumer purchases immensely. One can even speculate that increased consumer confidence would follow; surely life insurance companies have not kept pace in recent decades in maintaining their share of personal savings, and the reason may be the mystery and deception that accompany most sales. Cash value life insurance should be a good investment, considering the tax advantages and the abilities of insurance companies to get excellent returns on their investments. Those, like NICO, who advise consumers shouldn't have to warn them away from cash value life insurance because its purchase is so hazardous to one's financial health. Increased consumer understanding of relative values in life insurance will put pressure on the industry to become more efficient; in turn, better consumer values will result.

Appendix A

Ratings of cash-value insurance policies *continued*

Type: Participating Amount: $25,000 Age: 25

Listed in order of increasing cost, based primarily on 19-year cost index (see story). Rates are for men's policies; rates for women at the same age are generally lower. Where company and policy listings are the same, difference is indicated by footnote. In addition to standard abbreviations, the following are used: LIC (Life Insurance Co.), LAC (Life Assurance Co.). All data are based on 1979 rates and include waiver of premium in event of disability.

Company and policy	Annual premium*	Cost indexes 20-yr.	9-yr.	19-yr.	29-yr.	Net payment index	Yields 9-yr.	19-yr.	29-yr.
The 40 lowest-cost policies									
Teachers Ins. & Annuity Assoc. of Amer. Ordinary Life [F]	$302	$10	◉	◉	◉	◉	1.90%	7.28%	7.86%
State Mutual LAC of Amer. Non-Smoker Whole Life [B]	331	13	◉	◉	◉	◉	6.15	7.42	7.39
Massachusetts SBLI Straight Life [C]	236	27	◉	◉	◉	◉	8.54	7.97	7.85
New York SBLI Straight Life [D]	280	48	◉	◉	◉	◉	5.65	6.34	6.51
New England Mutual LIC Ordinary Life [A]	296	48	◉	◉	◉	◉	3.64	6.26	6.45
Massachusetts Mutual LIC Convertible Life	302	55	◉	◉	◉	◉	3.40	5.98	6.08
Standard Ins. Co. Whole Life [B]	306	55	◉	◉	◉	◉	3.44	5.98	6.34
New England Mutual LIC Ordinary Life	305	57	◉	◉	◉	◉	2.69	5.81	6.12
Northwestern Mutual LIC Whole Life	364	60	◉	◉	◉	◉	3.19	5.65	6.17
Home LIC Whole Life NSR [B]	277	31	◓	◉	◉	◉	1.84	7.05	6.97
Phoenix Mutual LIC Ordinary Life, NSB [B]	384	35	◉	◉	◉	◓	3.77	6.20	6.30
Home LIC Whole Life	289	43	◓	◉	◉	◉	0.48	6.35	6.47
Central LAC Special Whole Life	340	52	◉	◉	◉	◓	5.91	5.98	5.88
Phoenix Mutual LIC Ordinary Life	388	39	◉	◉	◉	○	3.50	6.06	6.20
Union Mutual LIC Whole Life [B]	391	49	◓	◉	◉	◓	2.68	5.68	5.95
Guardian LIC of Amer. Pension Trust Whole Life [A]	376	51	◓	◉	◉	○	2.56	5.66	6.06
Guardian LIC of Amer. Modified 3 Whole Life [A]	385 (3)	53	◓	◉	◉	○	2.64	5.65	6.00
Guardian LIC of Amer. Whole Life [A]	376	55	◓	◉	◉	○	2.51	5.52	5.88
Guardian LIC of Amer. Pension Trust Whole Life	382	57	◓	◉	◉	○	2.14	5.44	5.90
Union Mutual LIC Whole Life	399	58	◓	◉	◉	○	2.13	5.38	5.73
Guardian LIC of Amer. Modified 3 Whole Life	391 (3)	59	◓	◉	◉	○	2.15	5.40	5.83
Mutual LAC of New York Whole Life [A]	417	49	○	◉	◉	◒	0.84	5.63	5.82
Continental Assurance Co. Whole Life	335	56	◓	◉	○	○	1.80	5.61	4.69
Mutual LAC of New York Whole Life	427	59	◒	◉	◉	◒	0.19	5.29	5.58
USAA LIC Modified-One Whole Life	282 (1)	65	◉	◓	◓	◉	3.96	5.56	5.85
Manufacturers LIC Permanent Economic Protection	306	64	○	◓	◉	◉	−0.21	5.45	6.19
Standard Ins. Co. Whole Life	316	66	◓	◓	◓	◉	2.41	5.42	5.95
Connecticut Mutual LIC Econolife (Whole Life)	281	74	◉	◓	○	◉	3.69	5.12	5.34
Guardian LIC of Amer. Whole Life	382	61	◓	◓	◉	○	2.09	5.29	5.72
Union Mutual LIC Exec. Life (Non-NY) [B]	400	68	◓	◓	◉	○	2.62	5.08	5.63
Indianapolis LIC Ordinary Life [B]	345	69	◓	◓	◓	◓	2.22	5.15	5.40
New York LIC Modified 2 Whole Life	374 (2)	69	○	◓	◓	◉	−0.53	5.12	5.83
Columbus Mutual LIC Life—100	288	71	○	◓	◓	◉	−0.85	5.12	5.62
Farm Bureau (Iowa) Exec. Pfd. Par	349	72	◓	◓	◓	◓	2.05	5.01	5.40
USAA LIC Ordinary Life	345	68	◓	◓	◓	○	1.63	5.15	5.52
Indianapolis LIC Exec. Protector [B]	386	68	◓	◓	◓	○	3.11	5.16	5.34
John Hancock Mutual LIC Pfd. 25 [A]	397 (3)	70	◓	◓	◓	○	1.31	4.98	5.62
State Mutual LAC of Amer. Non-Smoker Exec. Protector Endowment [B]	391	71	◓	◓	◓	○	2.34	4.96	5.53
Minnesota Mutual LIC Econo-Life	310	72	○	◓	◓	◓	−0.64	5.01	5.63
Bankers Life Co. Special Whole Life	303	73	◓	◓	○	◓	1.00	5.04	5.22
The 5 highest-cost policies									
All Amer. Life & Casualty Co. Life Paid Up at 65	452	136	●	●	●	●	−0.99	2.84	3.61
Aetna LIC Whole Life	453	141	●	●	●	●	−6.40	2.68	3.78
Imperial LAC of Canada Exec. Protector	475	148	●	●	●	●	−1.24	2.49	3.50
Security Life & Acc. Co. Whole Life	438	153	●	●	●	●	−5.54	2.12	3.60
Fidelity Life Assoc. Ordinary Life	468	181	●	●	●	●	−4.89	1.22	2.32

Premium changes after number of years in parentheses.

[A] Available only to "preferred risks."
[B] Available only to nonsmokers.
[C] Available only in Massachusetts.
[D] Available only in New York.
[E] Available only to Lutherans.
[F] Available only to people in certain jobs.
[G] Available only to members of a fraternal organization.

Appendix B

WHAT YOU SEE IS NOT WHAT YOU GET IN UNIVERSAL LIFE
or
HOW SBLI'S 9.44% BEATS LIFE OF VIRGINIA'S 11%

Recently one of our banks sent us a four page proposal for a $50,000 Universal Life (UL) policy called "The Charger" and sold by Life of Virginia (LOV), which may have the largest advertising budget for UL in the country. Below we show a summary of that policy, assuming that LOV credits 11% to cash values in the future. Along side, we show a concoction we brewed from SBLI's new series to match (as closely as possible) LOV's premiums and death benefits.

$50,000, Male 42, Nonsmoker

LOV's 11% UL vs. SBLI's $15,947 SL/$34,053 DT25

Policy	Premiums		Death Benefits		Cash Values	
Year	SBLI	LOV	SBLI	LOV	SBLI	LOV
1	$ 434	$ 434	$ 50,000	$ 50,000	$ 326	$ 0
2	434	434	50,393	50,000	678	0
5	434	434	51,910	50,000	1,929	681
10	434	434	53,581	50,000	4,815	2,822
20	434	434	54,943	50,000	15,222	9,340

We used the dividend additions option on the SBLI combination of Straight Life (SL) and Decreasing Term Rider (DT25). Note how much better SBLI's cash values are for the same premium and a somewhat higher death benefit schedule. How can 9.44% beat 11%? LOV has an assortment of expense and protection charges that far exceeds SBLI's and that, in effect, lowers the 11% rate you see but don't get. How much does it lower it? We can compute a rate of return (ROR) for each policy. An ROR is the answer to this question: If instead of buying a cash value policy I buy a Yearly Renewable Term (YRT) policy and invest the premium differences, what interest rate (ROR) do I need to earn over the period of time for which the calculation is made such that (a) the death benefits of the cash value policy and the ART/Investment program are the same and (b) the cash value at the end of the period equals the Investment? We can use SBLI's YRT rates to make the calculations. Here is what we get:

Years Policy Kept	LOV	SBLI
5	-26.9%	6.5%
10	- 1.2	8.2
15	3.9	9.0
20	5.4	9.2

We see the 11% contract is more like 5.4% when held 20 years, much worse for shorter periods. SBLI comes out to 9.2% for 20 years, much closer to the 9.44% we say we credit to cash values. (The reason 9.2% falls a little short is that DT25 is a higher cost policy than YRT.)

We can't beat every UL policy this badly, and a few beat us over 20 years. The message is: Don't be intimidated by a UL policy in your customers hand; by all odds, there's some combination of SBLI policies and riders that's better.

SAVINGS BANK LIFE INSURANCE 05/29/84 00:03
(ONE OF THE BEST LIFE INSURANCE BUYS IN AMERICA)
RATES EFFECTIVE FOR POLICIES ISSUED 6/1/84 AND AFTER

FOR: JAMES H. HUNT CLASS: NON SMOKER AGE: 42 DIVIDENDS BUY ADDITIONAL INSURANCE (OPT3)

	PLAN	AMOUNT	INITIAL PREMIUM
BASIC POLICY:	STRAIGHT LIFE	$15,947	$ 263.73
RIDERS:	INSURED D25	$34,053	$ 170.27
	TOTAL ANNUAL PREMIUMS		434.00

TAX-DEFERRED CURRENT INTEREST RATE CREDITED TO CASH VALUES: 9.44%

GUARANTEED POLICY INTEREST RATE 5%

			COVERAGE ON INSURED			
			END YEAR CASH AVAILABLE		BEGINNING YEAR DEATH BENEFIT	
YEAR	TOTAL PREM	ANN PREM	GUARANTEED	TOTAL	GUARANTEED	TOTAL
1	434.00	434.00	197	326	50,000	50,000
2	434.00	434.00	401	678	49,864	50,393
3	434.00	434.00	612	1,061	49,659	50,756
4	434.00	434.00	833	1,477	49,455	51,160
5	434.00	434.00	1,062	1,929	49,557	51,910
6	434.00	434.00	1,300	2,420	48,944	51,988
7	434.00	434.00	1,546	2,951	48,604	52,383
8	434.00	434.00	1,800	3,525	48,229	52,787
9	434.00	434.00	2,058	4,145	47,787	53,173
10	434.00	434.00	2,322	4,815	47,310	53,581
11	434.00	434.00	2,590	5,539	46,731	53,950
12	434.00	434.00	2,863	6,322	46,084	54,316
13	434.00	434.00	3,140	7,167	45,335	54,648
14	434.00	434.00	3,420	8,078	44,483	54,950
15	434.00	434.00	3,705	9,060	43,496	55,193
16	434.00	434.00	3,995	10,118	42,372	55,374
17	434.00	434.00	4,287	11,259	41,044	55,426
18	434.00	434.00	4,581	12,485	39,546	55,396
19	434.00	434.00	4,876	13,804	37,843	55,257
20	434.00	434.00	5,174	15,222	35,868	54,943

DIVIDENDS AND ANY BENEFITS PROVIDED BY DIVIDENDS REFLECT CURRENT CLAIM, EXPENSE AND INVESTMENT EXPERIENCE; THEY ARE THEREFORE NOT GUARANTEED AND MAY INCREASE OR DECREASE IN THE FUTURE. DIVIDENDS ON ANY RIDERS ARE APPLIED TO THE BASIC POLICY. RIDERS HAVE NO CASH VALUE.

SURRENDER COST INDEX (5%) ON BASIC POLICY 10 YEARS: -.62 20 YEARS: -2.08

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Articles mentioned at June 28, 1984 hearing

BusinessWeek

JUNE 25, 1984 A McGRAW-HILL PUBLICATION

UPHEAVAL IN LIFE INSURANCE

CAN NEW PRODUCTS BOLSTER A LAGGING INDUSTRY? PAGE 58

GENERAL DYNAMICS: THE TANGLED TALE OF TAKI VELIOTIS PAGE 114

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HOW MUCH TOP UNION LEADERS ARE PAID PAGE 109

Cover Story

UPHEAVAL IN LIFE INSURANCE

HUNDREDS OF COMPANIES MAY NOT SURVIVE THE ERA OF 'NEW WAVE' POLICIES

Prudential's rock doesn't look much like Gibraltar anymore. The nation's largest life insurer recently unveiled a sleek, abstract version of its famous logo—a "dynamic rock" is what Robert A. Beck, chairman of Prudential Insurance Co. of America, calls it. "All of us in life insurance are having to rethink everything, our whole reason for being," says Beck, explaining the redesign. "There are no good old days to go back to."

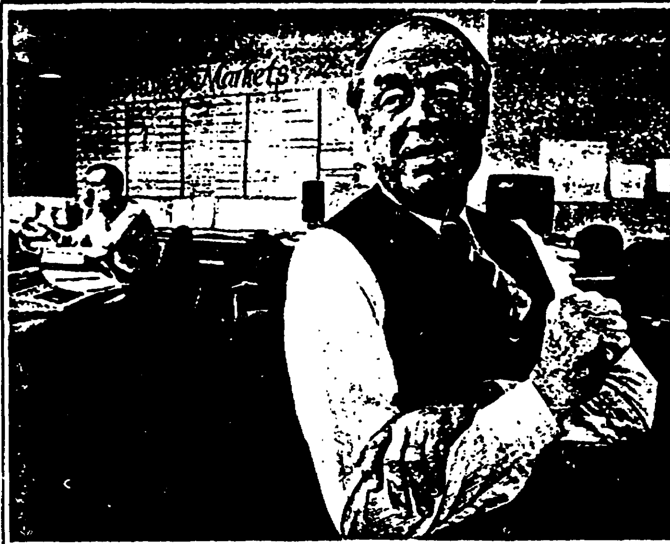
A backwater for decades, life insurance today is in the throes of radical change. Seemingly resigned to the steady erosion of their share of the consumer dollar throughout most of the 20th century, the huge old-line companies that dominate the industry stubbornly clung to their founding formula: selling whole life—which combines insurance with a low-interest savings plan—through the career agent. This system is now collapsing under the weight of its cost inefficiency and the pressures of intensifying competition. The once-staid life insurance business is in upheaval as the awakening giants of the business scramble to adjust.

> The universal life policy's fast takeoff 'definitely surprised us.... What we see is constant change'
>
> JOHN J. CREEDON
> Chairman, Metropolitan Life Insurance Co.

The forces reshaping life insurance became jarringly evident as early as 1981, when Prudential paid $385 million for the securities firm, Bache Group Inc. But the pace of change has greatly accelerated in just the past few months. "If it rained a little in previous years, now we are up to hurricane stage," says Richard E. Stewart, formerly insurance commissioner of New York and now an industry consultant.

The storm is a delayed reaction to the sweltering inflation and torrid interest rates of the late 1970s. With whole life in disrepute, new kinds of policies offering variable rates of return were created and promoted by upstart insurers. Bitterly opposed at the outset, the industry establishment is finally capitulating. In

PHOTOGRAPHS BY ANDREW POPPER



the past year nearly every one of the two dozen giant companies that dominate life insurance have unveiled their own versions of universal life, variable life, or other "new-wave" policies.

At Metropolitan Life Insurance Co., the second-largest insurer, a universal policy introduced in mid-1983 is pulling in an astounding 47% of new premiums. The fast takeoff of universal—a flexible-premium, higher-yielding version of whole life—"definitely surprised us," says John J. Creedon, chairman and chief executive officer of Metropolitan. The company also has introduced variable life, which allows the buyer to shift among stock, bond, and money market funds. "What we see happening is constant change."

GNAWING UNEASE. Skyrocketing sales of the new policies are giving a sorely needed lift to an industry that was devastated by fierce price-cutting and the runaway inflation of the late 1970s. The life insurance industry's financial health is difficult to gauge because it is dominated by mutual companies, which are theoretically non-profit institutions owned by their customers. However, the earnings growth of stockholder-owned companies is picking up, reviving Wall Street's long-dormant interest in insurance shares.

Still, the insurance industry today is pervaded by a gnawing sense of unease. Instability is anathema to insurance companies, which are used to making their money by selling long-term financial guarantees based on finely honed calculations of the incidence of death. The industry's mortality tables remain a marvel of precision. But in most other respects, the life insurance industry is operating in the dark. Says Robert Posnak, head of the insurance group at the accounting firm Ernst & Whinney: "Insurance companies are not sure where they fit in strategically, they are not positive about their financial condition as they go forward, and they are not even sure how to monitor their business."

The sharp rise in interest rates since January is reviving unpleasant memories of the crunch of 1980-81 throughout the insurance world. A huge jump in policyholder loan demand quickly depleted insurers' supply of cash and forced them to line up emergency lines of credit. But this time the industry faces a different and potentially more frightening nightmare. As rates rise, policyholders en masse might cash in old policies to buy the new ones the industry is now promoting so zealously. That would not only strain cash reserves but also undermine profitability for years.

'Banks should be kept out' of the insurance business. 'Assets backing a policy . . . can't be in Argentina'

JOHN B. CARTER
Chairman, Equitable Life Assurance Society

'There is certainly the danger that companies will . . . take some outsized risks'

FRANK J. HOENEMEYER
Vice-Chairman, Prudential Insurance Co. of America

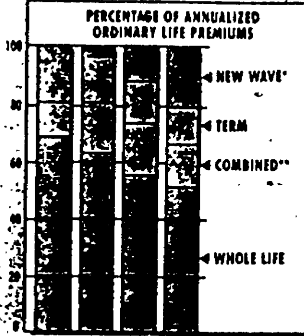
The threat of fleeing policyholders is already exerting new pressure for high rates of return on the industry's $658 billion investment portfolio. "Investment performance is the engine that will drive the industry," says Jerome S. Golden, president of Monarch Resources Inc., a major writer of variable life. "If an investment manager can outperform you by one or two percentage points a year, it doesn't matter what esoteric variations you make in policy design."

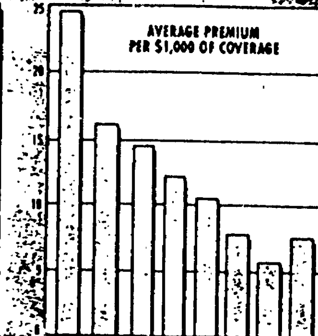
OUTSIZED RISKS. As competition heats up, many in the industry worry that some companies will promise more than they can deliver. "There is certainly the danger that one way or another companies will get behind the eight ball and take some outsized risks to catch up," says Frank J. Hoenemeyer, vice-chairman of Prudential.

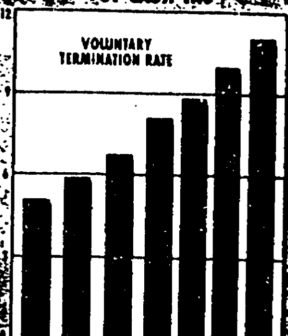
While the new investment-oriented policies are the centerpiece of their expanded product lines, many insurance companies are also adding mutual funds, limited partnerships, and other securities-based investment packages. Some are snapping up money-management firms and regional brokerage houses. Contends Ardian Gill, chairman of Gill & Roeser Inc. and a prominent actuary: "It is not the life insurance business anymore. It's the investment business."

At the same time, the century-old system of selling policies through local agencies is under assault as more and more banks, brokerage houses, and mass marketers begin selling insurance. Citicorp and other big bank holding companies hope to underwrite life insurance when the law permits—and in New York, Governor Mario Cuomo is pushing legislation allowing unrestricted bank entry into insurance as of next Jan. 1. Though the banks' attempt to enter in-

Cover Story







surance underwriting via state-chartered banks in South Dakota was blocked in January by the Federal Reserve Board, that ban faces court challenges.

Agent groups, with fierce lobbying in Washington and state capitals, are leading the industry's campaign to keep banks out of life insurance underwriting. But insurance executives are in high dudgeon, too. "Banks should be kept out of the business of making lifetime promises," says John B. Carter, chairman and chief executive officer of Equitable Life Assurance Society. "The assets backing a policy have got to be there when it comes time to deliver on that promise. They can't be in Argentina."

FULL-SCALE INVASION. Meanwhile, the bank threat has prompted the industry to get serious about cutting costs and improving the productivity of its army of 250,000 insurance agents. Many more companies are risking the wrath of their agents by experimenting with new channels of distribution—banks and brokerage houses among them. The full-scale bank invasion that many insurance executives expect "changes the whole ball game," says Jacob B. Underhill, president of New York Life.

But even before the entry of unwelcome outsiders, life insurance was becoming uncomfortably crowded. Mounting competition drove down the price of insurance sharply and caused extreme shifts in market share. Some companies have been so weakened that they now lack the financial muscle to reposition themselves in this capital-intensive industry. Insurance companies, of course, must set aside reserves to back newly sold policies. Yet they cannot amortize their selling costs, even though it takes at least a decade before they begin making money on the average policy.

As the new policies spread, voluntary terminations of existing insurance are rising. In 1982, one of every 10 policyholders canceled—a "lapse" rate of 10%, up from only 6.6% in 1978. The industry is bracing for a leap in lapses this year. "Surrender rates are going up much higher than many people seem to realize," contends Fred Carr, chairman and chief executive of First Executive Corp.

Meanwhile, companies must invest enormous sums to upgrade their computer systems and retrain their sales forces to cope with the new investment-oriented policies. The day is fast arriving when every insurance agent must have a personal computer and a license to sell securities. Given all the additional costs, "the jury is out on the profitability of universal and variable life," says Posnak of Ernst & Whinney.

Even the biggest insurers might not be able to afford both to realign their basic business and to diversify more broadly into financial services. Although the profitability of individual life insurance has withered, it remains the industry's key earnings source. Group life and health is marginally profitable for most companies, and the industry has only a modest stake in retail securities brokerage—though the giants have built huge pension fund management operations.

The industry's need for management talent probably is even more acute than its need for capital. "There are very few industries that have gone on so well for so long with so little management," says one particularly critical investment banker. "I used to say stupidity alone couldn't ruin a life company—you had to be malicious. That's not true anymore."

AUTOMATIC PILOT. Until a decade ago, the placidness of the business permitted life insurance companies to run on automatic pilot. As a result, the industry today is desperately short of homegrown managers. To date, though, there has been no infusion of outside talent. That is a result in part of the industry's dull, strait-laced image, and to the comparatively low compensation level.

As mutuals, Prudential, Metropolitan, Equitable, John Hancock, and New York Life distribute almost all of their earnings as policyholder dividends. As recently as 1978 the president of Equitable was chastised by a director for merely mentioning the word "profit" in a presentation to the board. And mutuals cannot, by definition, entice or encourage management by granting stock options.

Long a target of outside critics for its emphasis on volume rather than cost efficiency, the mutual system is now being challenged from within. Indeed, most mutuals are thinking of converting to stock ownership. What is envisioned as the tortuously complex and lengthy process of "demutualizing" is under way now at Union Mutual Life Insurance Co. "Whatever happens, we want to be ready," says Colin Hampton, president and chief executive officer of the old-line Maine company, with assets of $4 billion.

Although even the giants are studying conversion, investment bankers privately doubt whether investors would swallow a string of multibillion-dollar mutual company offerings, particularly when most insurance shares are still selling at steep discounts to book value. "For a sizable company, it is just not a practical idea," says one investment banker. "They may be trapped."

'COMBAT ZONE.' Many in the industry concede that hundreds of the 1,900 U.S. insurance companies—mainly small and mid-sized ones—are doomed. "There is a big shakeout coming," says Kenneth C. Nichols, president of Home Life Insurance of New York. "We have gone from the comfort zone to the combat zone, and mediocrity can no longer survive."

Unlike the banking industry, insurance has never lived through an epidemic of failures, nor does it have the banker's panoply of federal agencies to orchestrate rescues. Overseeing of the insurance industry is left totally to the states (page 66), and the limitations of that approach have been ominously underscored by what is known throughout the field as the Baldwin-United "fiasco." Says Joseph Belth, professor of insurance at Indiana University: "People in the industry would like to think Baldwin-United was a freak accident, but it's a freak thing that could happen again."

A piano company that rapidly transformed itself into a financial services giant, Baldwin-United Corp. in March, 1983, filed for bankruptcy under Chapter 11 when it could not repay $900 million in short-term debt. The courts took control of Baldwin's insurance subsidiaries after realizing that the value of the assets backing some $4 billion in single-premium deferred annuities (SPDAs) it sold was far less than what they owed investors.

More recently, Charter Co., an acquisition-minded conglomerate that was the No. 1 SPDA vendor, filed for Chapter 11 protection after its oil-refining business collapsed. Devastated by the woes of Charter and Baldwin-United and by stricter tax treatment of SPDA income, annuity sales plummeted last year and remain depressed, depriving the industry of what had been its fastest-growing source of income.

UTTERLY DOMINANT. Baldwin and Charter were pioneers in transforming the annuity from a mundane insurance staple into a hot investment. Originally, the annuity was a poor man's retirement account, in which regular cash could accumulate tax-free at a guaranteed rate to be withdrawn via annual payments. Developed in the late 1970s, the SPDA substituted a single, up-front payment for the periodic cash contribution feature of the standard annuity. Thus, the SPDA was more like a tax-free bond than like insurance; the vast majority of Baldwin's and Charter's sales were made through brokerage houses.

MONARCH RESOURCES' GOLDEN: THE DRIVE IS ON FOR "INVESTMENT PERFORMANCE"

Now, life insurance is similarly being recast as a high-performance investment. The purest and earliest form of ordinary life is term insurance—a guaranteed benefit payable on death. Whole life was developed in 18th century England to smooth out term's steeply graduated premium schedules. This was done by building a savings plan into the policy and greatly overcharging the buyer at the outset. The company invested the excess and credited a portion of its gains to the policyholder.

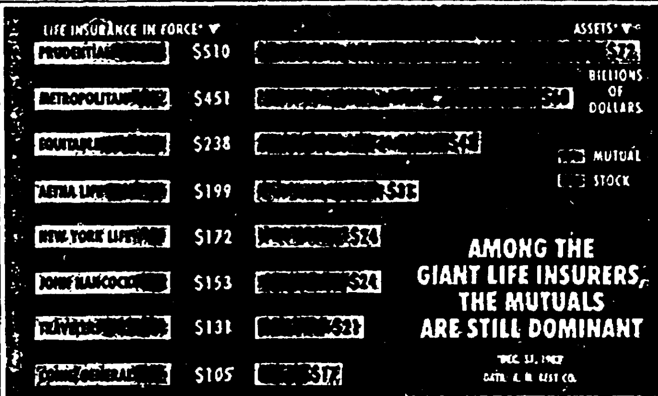
Whole life remained utterly dominant until the inflation of the 1970s made the 4% to 6% yearly returns look pathetic. "Buy term and invest the difference" became the battle cry of a host of upstart companies. Term once again became dominant. And because it is much cheaper than whole life, total life insurance premiums stagnated despite healthy gains in the face amount of sales. To counter the crippling switch to term, universal life was developed and first marketed by E. F. Hutton & Co. in 1979. Universal life lets policyholders vary the amount of insurance protection and the size and timing of premium payments. The premium is split apart or unbundled, enabling buyers to see how much goes for the death benefit and how much to cash value. Moreover, the premiums are placed in separate accounts and invested in securities yielding far more than the old bonds in the company's general account.

Variable life, introduced by Equitable in 1976, also features an unbundled premium and separate-account investing—in its case, in a wider range of assets. However, unlike universal, the premium payments for variable life are fixed.

Universal life came into its own only last year, as its share of new premium income doubled to 18%. The Life Insurance Research Marketing Assn. is projecting that universal will command as much as 35% and variable life as much as 7% (up from 2% in 1983) of the market this year. Waiting in the wings is yet another new policy known as "universal II" or "universal variable." It combines the flexible premiums of universal life with the investment options of variable life. The Securities & Exchange Commission, which has applications from a dozen companies, seems to be leaning toward approval.

HOW BIG A MARKET? The insurance world is divided into evangelical camps contending that universal or variable or universal variable is the key to the future. Further dramatic shifts in market share appear inevitable, but all the jockeying for position tends to obscure the critical question: How big is the market for all these forms of cash-value life insurance?

Recent results offer the industry some encouragement. After staying on a plateau for eight years, the number of individual policies sold jumped 7% in 1983, and cash-value policies accounted for most of the increase. Premium income



from ordinary life jumped an impressive 12.1%, more than double the rate during the dog days of 1980-81. Moreover, in the last three years the decades-long slide in ordinary life's share of personal disposable income has been reversed—though at 1.7% it is only about half of what it was in 1940.

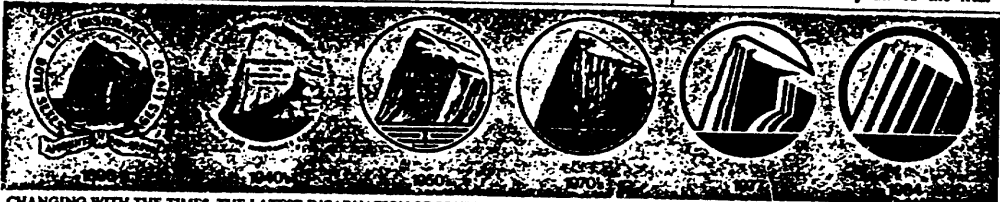
Although insurance companies have plenty of rivals for consumer savings, they do have a couple of advantages. The biggest one is the tax-favored status of life insurance. Investment earnings within the policy—the "inside buildup"—are not subject to tax while the policy is in force. In some new-wave policies, such a tiny portion of the premium payment is used for the death benefit that Congress was recently moved to tighten up, and some universal policies must now be restructured. But there are no signs of a broad-based political challenge to the inside buildup.

Another advantage: The life insurance "the companies have used only a fraction of the agent's ability. They told him to just go out and sell whole life."

The industry's stubborn adherence to its narrow traditional mission wreaked havoc with its distribution system. As consumers became more demanding, agents working for a company that was slow to update its product line unofficially began selling policies developed by the upstarts. Even as they lost control over their sales forces, the main-line companies were socked with big increases in the cost of training and maintaining agents. Slow to pick up on the extent of unacknowledged brokering, the industry was constrained in its response by the agent's control of the customer relationship. But economics dictated that something had to give.

Although most of the main-line companies believe that the vast majority of insurance sales will be made through the agent for years to come, some insurers outright acquisition or through joint venture. Although—to their regret—many brokerages sold huge volumes of Baldwin and Charter SPDAs, only E. F. Hutton to date has demonstrated an ability to sell ordinary life in quantity. After concluding that its account executives were unable or unwilling to sell insurance, Merrill Lynch & Co. a year ago began putting professional agents in its branch offices to sell variable-life policies developed by Monarch Resources. Team-selling experiments also are under way at Prudential, where Pru agents and Pru-Bache brokers have paired off and pooled clients.

But few of the main-line companies appear willing to associate with banks, which suggests that they view them as the bigger threat. Capitol Holding Corp., a large stockholder-owned company, will station some of its agents in selected Bank of America branches beginning this fall. But virtually all of the hun-



CHANGING WITH THE TIMES: THE LATEST INCARNATION OF PRUDENTIAL'S LOGO IS THE RECENTLY UNVEILED "DYNAMIC ROCK"

agent seems better qualified as a financial planner than the salespeople in other financial industries. "The insurance agent must work laboriously to build a relationship before he can make a sale," says John G. Kneen, an insurance specialist at the consulting firm of Cresap, McCormick & Paget. As a result, "the successful life agent has a remarkable ability to empathize with the customer."

On the other hand, surveys show that insurance companies are far behind banks or brokerage houses in being perceived by the public as full-service providers. Although the individual retirement account would seem to be a natural for an industry geared to providing long-term financial security, insurers got a meager 12% of the $40 billion invested in IRAs in 1982. With rare exceptions, insurers have been singularly unsuccessful over the years at selling anything but insurance.

LITTLE INCENTIVE. The huge front-end commissions on life insurance—often amounting to 100% of the first-year premium—make the commissions on securities seem puny to agents. And because their payout is so heavily front-loaded, agents have little financial incentive to maintain customer relationships over the long term. Until recently, Kneen says, are shrinking or even dismantling their agency systems. "Their bottom line will probably look good for a couple years, but I wouldn't want to be running one of those companies 10 to 15 years from now because they will pay dearly," says Randy Procter, an executive vice-president of Equitable. "People still like to do business with people."

Still, Equitable and like-minded companies are now overhauling their agency systems to boost productivity. Acknowledging that they can no longer cost-effectively underwrite every kind of insurance, many main-line companies now allow their agents to fill in gaps in product lines with offerings from others. Some companies are also beginning to market their wares through general agencies and in some cases have even set up their own broker-dealers to market the new policies. This latter tactic restores a measure of control over distribution. To sell variable life or universal variable, an agent must be licensed by the National Association of Securities Dealers and operate under the supervision of a registered broker-dealer.

For that reason, and to gain an additional distribution channel, many big insurance companies have linked up with stock brokerage houses, either through dreds of banks and thrifts selling low-cost term do so by mass mailings to their credit-card holders and other customers. Banks apparently believe that their high degree of computerization will enable them to turn a profit even as they wrest market share away from traditional insurers by cutting their prices.

BIGGEST THREAT. Market research by Cresap, McCormick & Paget suggests that only about 50% of American adults depend on an agent in selecting a policy. An additional 25% reach their own decision and buy term from an agent, and the remaining 25% loathe commission salesmen and don't buy any life insurance. "It's quite clear that the independent types will welcome a reputable new channel like the banks," Kneen says. "The banks may not make money in insurance, but they can certainly do a lot of damage finding that out."

But the biggest threat to the life insurance industry may be coming from within. With no federal safety net, the promise backing an insurance policy is only as good as the company making it. In the midst of mounting turmoil in the marketplace, many companies today know they are struggling for survival.

Furthermore, the new generation of policies is building an element of uncer-

tainty into an instrument created to protect against the unknown. In exchange for potentially higher returns, the buyer accepts returns that will vary with the uncertain course of the economy and financial markets. To be sure, the new-wave policyholder is not dragged down by an insurer's past investment errors. But neither is he or she shielded from volatile markets by the vast portfolios that are backing whole-life policies.

In launching the new generation of policies, the industry believes it is bowing to consumer demand. But is the demand really for greater control over one's own investment destiny or simply for what is billed as a better deal? If it is the latter, the public's appetite for the new policies could easily be ruined by disappointing investment performance.

"Security and guarantees were the things the life insurance business was built on," says Thomas H. McAboy, an executive vice-president of Travelers Corp. "Life insurance is still life insurance, and an investment is an investment. I'm not against bringing them closer together, but let's not get mixed up and believe that life insurance is an investment. That's the danger." ■

STATE WATCHDOGS ARE 'OUTMANNED AND OUTGUNNED'

In the office of the Commissioner of the New Jersey Insurance Department, an American flag with only 48 stars [illegible]. That says it all, sighs Kenneth D. Merin, the acting commissioner. "Nothing has changed here in 25 years." Yellowed files in cardboard boxes are stacked in the hallways of the [illegible] department's [illegible] where Merin and his staff of 200 labor. Yet the New Jersey department, which has embarked on a modernization program, is considered one of the best in the country. New York and California are widely regarded as being in a class by themselves, but New Jersey is usually mentioned in the next tier, along with Florida, Texas, and Illinois.

ILL-EQUIPPED. The 50 state insurance departments are the sole monitors of insurance companies' solvency—a role that predates the explosion of federal regulation of banks and securities firms in the 1930s. While a state tends to devote most of its resources to insurers chartered there, it is responsible for policing all companies doing business in its domain. The states also must approve new kinds of policies, license insurance agents, and resolve policyholder disputes.

It is a task for which most states are ill-equipped. In many cases, insurance departments lack the statutory or administrative powers needed to keep up with the fast-changing world of life insurance. Almost all are short on staff and computer power. A study by a group of state legislators found South Dakota with two auditors for 1,070 companies. "This may have been all right for the 1960s, but there is no way the system can keep up with the insurance companies today," says Merin. "The supposed watchdogs of the industry are outmanned and outgunned."

The National Association of Insurance Commissioners (NAIC) [illegible] states by distributing financial data about problem companies through its early warning system. But the system is not computerized, and information [illegible] outdated by the time it reaches the states. It did not alert regulators to serious problems at six companies owned by Baldwin-United Corp., which filed a Chapter 11 bankruptcy in 1983.

New York State Senator John R. Dunne, head of a national task force on state insurance regulation, has proposed that insurance companies report on their solvency to regulators quarterly in computer-ready form. Several states—including New York—are moving that way now. However, a nationwide system would require insurance regulators to pry millions of appropriations dollars from legislatures. Says Dunne: "Insurance regulation is not as politically appealing as fighting crime or catching welfare cheats."

TARRED BY SCANDAL. Dunne suggests such a computerized monitoring system would have been particularly useful in the Baldwin-United case. Baldwin was making so many acquisitions and selling annuities at such a rapid clip that regulators simply could not keep pace in monitoring the financial condition of the insurance subsidiaries. "The way money flows through the corporations today, you [illegible] ting at the treasurer's desk to find out what's really going on," says [illegible] Carlson, deputy insurance commissioner for Michigan [illegible].

That suggests the kind of vacuum that in the past has attracted federal regulation to other financial industries. Insurers are far less dogmatically opposed to regulation than they were before they all were tarred by the Baldwin-United brush. [illegible] John B. Carter, president and chief executive officer of Equitable Life Assurance Society, a plan to offer a variable policy linked to a checking account, for example, would need the approval of state insurance and banking departments of 50 states and also have to conform to 50 different securities laws. "That," Carter declares, "is a ridiculous way to do business. It drives us toward a system of federal regulation and a single regulatory body [illegible]." Adds the president of another big insurance company: "It's hard to see a call for federal regulation coming from the Reagan Administration. But one day there will be federal regulation, and it will grow out of being [illegible]."

NEW JERSEY'S MERIN: A 48-STAR FLAG AND FILES IN CARDBOARD BOXES [illegible]

Better Bargains Today In Life Insurance

New and different policies build values faster, but you should take time to shop around and compare costs.

Despite an explosion of new ways to make money, some investors are turning back to a traditional method of saving—life insurance.

Winning attention is the type of insurance known as whole life. These policies charge the same premium every year. Part of the payment is used to cover the death benefit—the face amount of the policy. The rest goes to work in a savings plan managed by the insurer.

Today's whole-life policies offer lower premium rates and build bigger cash values than did older plans that fell into disfavor during the inflationary 1970s. Moreover, two new variations of whole life—universal life and variable life—offer consumers considerable flexibility in meshing their insurance needs with their savings programs.

The initial step in choosing life insurance is deciding just how much you need. A childless, two-career couple may find that the amounts provided by their employers are enough. A household with small children, a big mortgage and few assets needs a lot of protection—perhaps as much as $250,000—on the breadwinner. Yet few people in their 20s or 30s can afford the hefty annual premiums that go with a whole-life policy half that size.

The least costly approach would be term insurance. Term policies provide death benefits but do not build cash values. Premiums rise as you get older.

Experts suggest that those who can afford it may want to meet part of their insurance needs with term policies and the rest with whole life. That's because the latter has a number of features that appeal to savers—

- One is the rate of return. A policy's yield depends on the issuer's financial savvy. The better companies offer yields comparable to those paid on bonds or other fixed-income investments, says Joseph Belth, professor of insurance at Indiana University.
- You do not pay any income taxes on the interest your whole-life policy earns while you are paying premiums.
- Whole-life policies provide a ready source of funds. Policyholders can redeem their cash values by terminating their contracts, use their insurance policies as collateral for bank loans or borrow all or part of the cash value directly from the insurer. When you die, any outstanding loans will be subtracted from the sum paid to your beneficiaries.
- Whole life's regular premiums can offer a savings discipline to those who find it hard to put money away.

Under traditional whole-life plans, the cash value grows at least at a minimum rate set by the insurer. With two variations of whole life now available, the policyholder can influence the yield.

One, called universal life, combines term insurance with a savings program. The policyholder may change the coverage amount and vary the premium.

Today, a 35-year-old, nonsmoking male can buy a universal-life policy with a death benefit of $300,000 from the E. F. Hutton Life Insurance Company for an annual premium of $2,400. If at age 50, the policyholder decides to drop his insurance coverage to $150,000, he can reduce his premium by $600 or put that much more into the savings portion of the plan.

Most of the 100 or so universal plans now offered earn market yields, although the actual return to the policyholder may be lowered by management fees. Tax laws limit the amount of money a policyholder can put into a universal-life plan at given levels of insurance coverage.

Choice of Investments. Variable-life insurance lets the policyholder direct where cash values are to be invested. Among the choices are stock, bond and money-market funds. The death benefits have guaranteed minimums but could go higher, depending on the results of the chosen investment program.

A whole-life policy's cash value grows as long as premiums are paid; however, after 20 or 30 years, many people redeem their policies and collect the accumulated savings. Many investors prefer to put the proceeds of their policies into another plan sold by insurance companies—annuities. These contracts promise an income stream, usually in the form of monthly or annual payments, which can be made for a specified time period or for life.

While whole-life insurance may be appropriate for your savings program, experts stress that the primary purpose of any insurance plan is financial protection for your dependents. Take care to buy neither too little nor too much, and shop hard to find the best deal. □

APPENDIX 5

(September 13, 1984)

Letter from Chairman Rodino to the insurance commissioners of those states that have competitive rating for workers compensation insurance.

NINETY-EIGHTH CONGRESS

PETER W. RODINO, JR. (N.J.), CHAIRMAN

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BILL McCOLLUM, FLA.
E. CLAY SHAW, JR., FLA.
GEORGE W. GEKAS, PA.
MICHAEL DEWINE, OHIO

U.S. House of Representatives
Committee on the Judiciary
Washington, D.C. 20515
Telephone: 202-225-3951

GENERAL COUNSEL:
ALAN A. PARKER

STAFF DIRECTOR:
GARNER J. CLINE

ASSOCIATE COUNSEL:
ALAN F. COFFEY, JR.

August 24, 1984

Dear [illegible]

The Subcommittee on Monopolies and Commercial Law of the House Judiciary Committee is currently reviewing the McCarran-Ferguson Act. The Subcommittee is seeking to determine whether the current situation of exemption from federal antitrust laws and state regulation of the insurance industry best serves the consumer or whether some other mechanism would be preferable.

As part of its study, the Subcommittee will hold a hearing on September 13, 1984, to receive testimony regarding the effect collective activities of insurers, and particularly joint ratemaking, have on competition in the marketplace and on the prices consumers pay for the insurance product. It is my understanding that your state recently changed from a rigid system of prior approval and mandatory adherence to bureau-devised rates for workers' compensation insurance to a competitive rating system. It would be helpful to the Members' consideration of this issue if you would provide the Subcommittee with information about your state's experience with the competitive rating system for workers' compensation insurance.

In particular, your response to the questions listed below would be most helpful. However, please feel free to add additional material which you feel would be helpful to the Subcommittee.

1. Have rates changed appreciably since you initiated competitive rating for workers' compensation insurance? If so, how have they changed?

2. What has happened to rates for small businesses?

3. Has the change affected the availability of workers' compensation insurance to businesses?

4. Has the change had a detrimental effect on small insurers? If so, please explain.

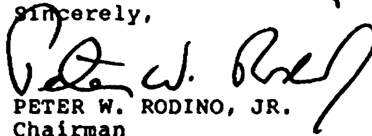
5. Has the change resulted in an increase in market concentration among firms offering workers' compensation insurance? If so, please explain.

6. Has the competitive rating system lead to monopolistic or oligopolistic practices? Please explain your answer.

7. How has the change affected collection and use of a statistical data base for workers' compensation insurance?

I would appreciate receiving the requested material by September 10, 1984, so that the Members may review it in preparation for the hearing. Your assistance is greatly appreciated.

Sincerely,



PETER W. RODINO, JR.
Chairman

PWR:mfl

Responses from state insurance commissioners to Chairman Rodino's letter.

ARKANSAS INSURANCE DEPARTMENT

400 University Tower Building ■ Little Rock, Arkansas 72204

Linda N. Garner
Insurance Commissioner

Ph 501 371-1325

September 13, 1984

The Honorable Peter W. Rodino, Jr.
Chairman
Committee on the Judiciary
Washington, D. C. 20515

Dear Chairman Rodino:

Arkansas enacted a competitive rating statute in 1979 for most of the property and casualty lines of insurance. Workers' compensation insurance was excluded from the 1979 law, as was the pattern in open competition legislation in other states. In 1981, Act 906 of the Arkansas legislature brought workers' compensation under the competitive rating scheme.

Insurers are required to file compensation rates on an individual basis. Insurers may reference the advisory filing submitted by the designated rate service organization. Deviations are premitted. Unlike the "file and use" provisions for other property and casualty lines, workers' compensation filing are submitted on a prior approval basis.

Statutory provisions allow the Commissioner thirty days to review and take action on compensation rate filings. The following will address the questions from your August 24, letter.

1. The impact of our competitive rating legislation has produced increased activity in workers' compensation rate filings. Since the effective date (1981) of this legislation, 24 insurers have filed and received Departmental approval for across-the-board percentage deviations, with the percentage range between 5 to 20 percent. The most significant evidence of competition in Arkansas is the submission of various schedule rating plans. Schedule rating refers to the method by which an underwriter debits or credits an employer's premium based on the physical characteristics of the risk. Since 1981, 147 insurers received Departmental approval for schedule rating plans with the credit or debit swing capped an average of 35%.

2. Rates and premiums charged to small employers (premiums under $1,000) are fairly uniform. Most of the deviation filings submitted during the first two years after enactment of competitive rating provided that the deviation was applicable to risks developing a premium of at least $2,500. In 1983 and 1984, schedule rating filings have lowered the minimum premium eligibility

Page Two

requirements to $750, which expanded the positive effects of competitive rating to include the small business. Competitior for workers' compensation business under $1,000 is understandably less than the medium or large accounts, although the smaller accounts are attractive when presented as a part of an overall package. In these instances, the smaller account becomes integrated with other types of insurance and is susceptible to account pricing techniques. The smaller employer also has increasing opportunities to join safety groups and enjoy the cost advantages that the insurance marketplace can provide through this mechanism of combining smaller risks into larger, more cost-effective accounts.

3. Under Arkansas' form of competitive rating, availability coverage has markedly increased. The reasons why our law provides availability are: because insurers may price workers' compensation insurance using their own rates, rules and plans; because we have a non-restrictive filing law; and because insurers have access to and use of suggested rates, rules and rating plans of the advisory organization.

4. No

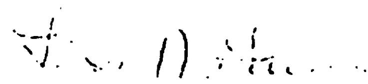
5. The activity in workers' compensation deviation filings submitted by insurers, and the entry of insurers into this market indicated a greater market concentration among insurers offering workers' compensation insurance. One reason more firms are entertaining the writing of workers' compensation insurance is the flexibility allowed under our law to adjust rates, thus creating a more manageable pricing environment. Under this scheme, insurer managements are more confident that workers' compensation results are easier to manage and control. Our experience indicates that prices do change more often than pre-competitive rating, but prices are not subject to the sharp and severe swings found in a more restrictive regulatory environment.

6. We have observed no evidence of monopolistic or oligopolistic practices. The latest compilation of premiums written in Arkansas show that in 1982, 193 companies were writing workers' compensation with a total direct premium written volume of $137,527,000 in comparison to 1980 when there were 215 companies writing with a total of $134,221,000 in direct premiums written. However, the premiums reflect that the company in 1980 writing the largest volume ($14,735,000) is still the same company in 1982 but the amount of premiums written were not as great ($10,521,000).

7. The use of the statistical data base has not changed, however, if a company uses either a scheduled rating plan or deviation or both, he must report the statistics to the National Council using the standard premium. The NCCI calls this the carriers' designated reporting level. It usually only necessitates the adding of a formula into their computer to come up with the standard premium. If a company offers a 10% schedule rating then the formula would then load the 10% back in.

Jan Taylor on my staff has prepared this information requested. Ms. Taylor has been with the Department for several years and has had direct experience with the competitive rating law for workers' compensation.

Sincerely,



Linda N. Garner
Insurance Commissioner

LNG:dj

OFFICE OF
COMPTROLLER GENERAL
7TH FLOOR WEST TOWER
NO. 2 MARTIN LUTHER KING JR. DR.
ATLANTA, GEORGIA 30334

JOHNNIE L. CALDWELL
COMPTROLLER GENERAL
COMMISSIONER OF INSURANCE
SAFETY FIRE COMMISSIONER
INDUSTRIAL LOAN COMMISSIONER

September 5, 1984

The Honorable Peter W. Rodino, Jr.
Chairman
Committee on the Judiciary
U. S. House of Representatives
Washington, D.C. 20515

Dear Chairman Rodino:

Thank you for your letter of August 24, 1984, which was received in my Office on August 29, 1984, concerning our recently effective open competition rating law for workers' compensation insurance.

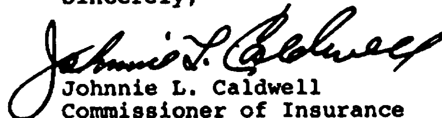
Since the law change was effective January 1, 1984, very few filings have been received in this short time. Thus, I do not feel sufficient time has elapsed for an evaluation to be made that would respond to questions one through six of your inquiry.

However, open competition on other lines of insurance has been a reality since July, 1967. In these other lines, open competition has not led to monopolistic or oligopolistic practices, nor has it had an adverse effect on small businesses or small insurers. I see no reason to expect any different results in workers' compensation.

In response to question seven, our law and regulation were structured with the intent of preserving the data base. As permitted by the regulation, a statistical agent has been designated to collect and maintain data from all workers' compensation insurers for the State of Georgia in order to meet this objective and, under our system, we do not foresee any loss or depletion in reliability or substance of the components that make up the data base. Our current system continues and will integrate the past, present and future data that comprises the workers' compensation insurance data base.

If there is any way I can be of further assistance, please do not hesitate to call on me.

Sincerely,



Johnnie L. Caldwell
Commissioner of Insurance

JLC:jp

STATE OF ILLINOIS
DEPARTMENT OF INSURANCE
SPRINGFIELD, ILLINOIS 62767

ACTUARIAL STAFF SERVICES

CASUALTY ACTUARY
LIFE ACTUARY
(217) 782-1795

October 3, 1984

The Honorable Peter W. Rodino, Jr.
U.S. House of Representatives
Committee on the Judiciary
Washington, D.C. 20515

Dear Representative Rodino:

In response to your letter to Director Washburn on competitive rating, our new open competition rating law for Workers' Compensation has proven to be very successful. Effective January 1, 1983, companies began making individual rate filings instead of automatically adopting the advisory rates filed by the National Council on Compensation Insurance (NCCI). There were a number of rate deviations filed in addition to widespread use of schedule rating credits; downward rate adjustments based on subjective evaluation of each individual risk. The overall effect was startling. Even though the number of risks being written in the voluntary market increased, premium income dropped from $797,000,000 in 1982 to $698,000,000 in 1983.

The volume of business being placed in the assigned risk plan (residual market) is down with the majority of the remaining risks being written at or near minimum premium. It is therefore unlikely that these risks will leave the plan. Those risks that have left the plan are apparently being placed in the voluntary market since the self-insurance market shows signs of decreasing.

Companies are clearly operating independently of the NCCI. In January of 1984 the NCCI filed an advisory rate increase of 11%. As late as June of 1984 less than 50% of the insurance companies had adopted this change. Because of a highly competitive market place, companies have been reluctant to raise rates. Further evidence of company independence is the size of schedule rating credits being filed. Finally, an at random survey of agents underlined just how volatile the market is.

This market activity has manifested itself in a shift of individual company market shares, an unprecedented drop in premiums of $100,000,000 and an increase in the direct loss ratio to 84%. This loss ratio begins to threaten gains made by investment income in last year's high yield environment.

In answer to your specific questions:

1. Yes, premiums have decreased 14%.
2. Small business premiums are often at the minimum premium level and therefore schedule credits generally are not used. Their premiums have not changed substantially. Those risks in the residual market have actually had premium increases in the neighborhood of 13%.

1984 GOV Competition in the Insurance Industry 739p bonknote.pdf

3. Yes, the size of both the residual market and the self-insured market have decreased.
4. No, not to date.
5. No, market shares are still well distributed and are changing on an individual company basis in both upward and downward directions.
6. No
7. The change has increased the technical responsibilities of the companies and the NCCI. Because there are so many rate levels in affect, adjustments to a common bureau level for rate filing purposes becomes a major task. The NCCI has put a great deal of effort into helping company statisticians and actuaries overcome this hurdle. It will be a few years before we can really determine how accurately the conversions have been made.

The Illinois Department is currently putting together a report on the first year of open competition rating for Workers' Compensation insurance. We will forward a copy when the study is finalized.

Respectfully submitted,

Robert W. Gossrow

Robert W. Gossrow, ACAS, MAAA
Casualty Actuary

RWG/ss

cc: Director Washburn
Richard Rogers

RECEIVED
SEP 10 1984

DEPARTMENT OF INSURANCE
P.O Box 517
FRANKFORT KENTUCKY 40602

GIL McCARTY
COMMISSIONER

MARTHA LAYNE COLLINS
GOVERNOR

September 7, 1984

Honorable Peter W. Rodino, Jr.
Congressman
U. S. House of Representatives
Committee on the Judiciary
Washington, D. C. 20515

Dear Congressman Rodino:

In response to your letter of August 24, 1984, requesting information concerning the change in Kentucky from "a rigid system of prior approval and mandatory adherence to bureau devised rates to a competitive rating system", please be advised as follows:

1. Have rates changed appreciably since you initiated competitive rating for workers' compensation insurance? If so, how have they changed?

   Prior to open competition all manual rates for workers' compensation were the same for each classification. Enclosed herewith is a synopsis of the various companies' filings, most of which are deviations downward from manual rates. Many insurers have filed their own plans, but in almost every instance there has been a significant rate reduction.

2. What has happended to rates for small businesses?

   The great majority of small businesses have shared in this overall reduction resulting from our open competition law. It should be pointed out that under our open competition rating system it is still mandatory to have prior approval of rates for the residual market, and a public hearing was conducted at the time the new rates were proposed in January 1984, and a substantial rate increase was approved.

3. Has the change affected the availability of workers' compensation insurance to businesses?

   In our opinion, the market has opened up. In 1983 there were 232 companies writing workers compensation as compared to 205 in 1982. Prior to open competition the market for workers' compensation on deep coal mining risks was constricted. Open competition has not solved that problem.

4. Has the change had a detrimental effect on small insurers? If so, please explain.

   Under the old prior approval program the regulator's concern was a determination of whether the rates filed were excessive or inadequate. Under open competition the regulator's concern shifts to the financial condition of the insurer rather than the individual rates. At this point in time it is too early to determine whether there has been an adverse effect on the smaller insurer.

5. Has the change resulted in an increase in market concentration among firms offering workers' compensation insurance? If so, please explain.

   We find no evidence that there is an increase in market concentration among firms offering workers compensation. In fact more companies now offer it. This also means more agents are available to market workers' compensation.

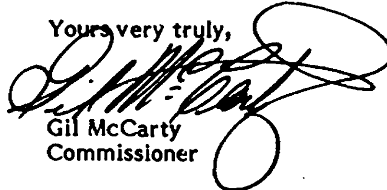
6. Has the competitive rating system lead to monopolistic or oligopolistic practices? Please explain your answer.

   Generally speaking there are no known monopolistic practices in Kentucky. Prior to open competition, one insurer had dominated the voluntary market in workers compensation for deep coal mine risks.

7. How has the change affected collection and use of a statistical data base for workers' compensation insurance?

   We are currently trying to make a determination of this matter by working with the National Council of Compensation Insurers, and our review is incomplete at this time. The only area in which open competition may not be functioning as anticipated is the area of under ground coal mine risks, and we are currently monitoring this situation to determine if this line of business should be declared non-competitive, with the idea of re-establishing a requirement of prior approval of rates.

Yours very truly,



Gil McCarty
Commissioner

Enc.

COMMONWEALTH OF KENTUCKY
DEPARTMENT OF INSURANCE
Frankfort, Kentucky 40601

LIST OF COMPANIES REFERENCE FILING TO THE NATIONAL COUNCIL ON COMPENSATION PURE PREMIUM OF JANUARY 1, 1984
SOME COMPANIES HAVE APPLIED FACTORS TO THE PURE PREMIUM RATES AND ALSO HAVE ADOPTED NEW DIVIDEND AND SCHEDULE RATING PLANS SINCE THE ENACTMENT OF SENATE BILL 274
(MANY COMPANIES HAVE NOT ADOPTED NCCI PURE PREMIUM RATES AND FILE INDEPENDENTLY AS LISTED IN PAST REPORTS)

COMPANY	DEVIATION
Aetna Life & Casualty Group Aetna Casualty & Surety Standard Fire Automobile of Hartford, CT	20% Overall Reduction in Rates 25% Maximum Schedule Rating for the Entire Group
Allianz Ins. Co.	Maximum 25% Schedule Rating Plan
Allstate Companies Allstate Insurance Co. Allstate Indemnity Co.	Maximum Schedule Rating Plan 60%
Northbrook National Northbrook Indemnity	Participating Dividend Plan and Schedule Rating Plan, Revised from 25% to 60% Maximum Credit
Northbrook National Northbrook Indemnity	1984 Revised Flat Dividend Plans
Northbrook Property & Casualty	Schedule Rating Plan, Revised from 25% to 60% Maximum Credit
Northbrook Indemnity	Flat Dividend 5 to 10% Maximum Credit
American Automobile Insurance Co.	3 Sliding Scale Dividend Plans
American Business & Mercantile Ins. Mutual Inc.	Workers' Compensation Coal Only-Tonage Rates $1.00 Per Ton Deep Mine $ .25 Per Ton Surface Mine (Revised) Plus Coal Only Experience Rating Plan Schedule Rating 25% Maximum Revised 4 Codes 8810, 8742, 8233, 0164

Company	Filing
American Centennial Insurance Co.	60% Maximum Schedule Rating Plan
American Employers' Ins. Co.	Revised Dividend Plans Maximum Credit 63% - No Losses
American Guarantee & Liability	Maximum Schedule 25% Credit
American Guarantee & Liability	Revised Participating Dividend Plan (available for insureds whose annual premium is $25,000 or more)
American Guarantee & Liability	Revised Safety Participating Dividend Plan (dividends depending on losses)
	17.1% Increase in Pure Premium Base Rates
American Hardware Mutual	1/1/84 NCCI Pure Premium Rates Adjusted by Factor 1.193 (4.8 increase in rates) Safety Group Dividend Plan · Group Minimum Premium $100,000.00
American Home Assurance Co.	Maximum 25% Schedule Rating Plan
American International Companies Granite State Ins. Co. New Hampshire Ins. Co. Illinois National Ins. Co. AIU Ins. Co.	NCCI Pure Premium 1984 Rates 17.1% Expense Constant $75 + Rate Factor 1.456
American International Group American Home Assurance Birmingham Fire of PA Commerce & Industry National Union Fire Ins. Co. of Pitts PA Ins. Co. of the State Pennsylvania	Revised WC Rates Effective 2/1/84 + Expense Factor 1.414
Ins. Co. of State of Pennsylvania	Participating Dividend Plan
American Mutual Liability	Schedule Rating Plan 60% Maximum Credit. Increase in base rates 11.1%
American Mutual of Boston	Schedule Rating Plan 60% Maximum Credit. Increase in base rates 11.1%
American Mutual of Boston	Revised Safety Group Dividend Plan (dividend determined by losses)

Company	Plan
American States Companies American States American Economy	Schedule Rating Plan 40% Maximum Credit Revised expense constant $60 to $35 NCCI 1984 Pure Premium Reduced by factor 1.609
American Economy	Participating Dividend Plan
Associated General	Flat 15% Reduction in Rates
Assurance Company of America	Flat 15% Reduction in Rates Schedule Rating Maximun 25%
Atlantic Mutual Ins. Co.	Retention Dividend Plan
Bituminous Group Bituminous Fire & Marine	Variable Dividend Program (loss ratio of 5% or less, possible 30% maximum dividend)
Bituminous Fire & Marine Bituminous Casualty	Schedule Rating Plan 25% Maximum Credit
Bituminous Fire & Casualty Bituminous Casualty	NCCI Pure Premium Adjusted By Factor 1.380
Brotherhood Mutual	NCCI Adjusted by Factor 10% Increase
CNA Insurance Companies Continental Casualty National Fire American Casualty Transportation Transcontinental Valley Forge	Schedule Rating Plan 50% Maximum Credit
Kansas City Fire & Marine	Five Loss Ratio Plans (available depending on premium size and losses)
Carriers Ins. Co.	9.9 Increase in Base Rates
Casualty Reciprocal Exchange	Schedule Rating Plan 40% Maximum Credit
Celina Mutual Ins. Co.	Maximum Schedule of 25% 5.5% Maximum Flat Dividend Plan

Company	Plan
Chubb Group of Insurance Companies Federal Sun Vigilant Pacific Indemnity Great Northern Alliance	Schedule Rating Plan 50% Maximum Credit
Church Mutual Ins.	17.1% NCCI Pure Premium
Cigna Group Insurance Company of North America Indemnity Ins. Co. of North America INA Underwriters Aetna Insurance Company Aetna Fire Underwriters Century Indemnity Bankers Standard Pacific Employers Insurance Co.	Schedule Rating Plan 25% Maximum Modification Safety Group Dividend Plan Sliding Scale Dividend Plan Revision of Expense Factor Loading, Complete Revision in Rates & Rating Values Reference NCCI 17.1% Pure Premium Adjusted by Factors
Aetna Fire Underwriters	Three Participating Sliding Scale Dividend Plans (Insured must produce annual premium of $5,000 or more; dividend based on loss ratio of 5% or less - 40%)
Pacific Employers	Three Sliding Scale Plans (eligibility $5,000 or more annual premium, maximum credit of 40.6% for 5% or less loss ratio)
Bankers Standard	Participating Dividend Plans (Each plan is open to all risks developing $5,000 or more annual standard premium)
Cincinnati	Schedule Rating Plan 25% Maximum Credit Revised Base Rates 1/1/84
City Ins. Co.	NCCI Pure Premium Revision -14.8% Factor - 1.507
Commercial Union Companies Commercial Union Employers' Fire Northern Assurance	Schedule Rating Plan 25% Maximum Credit
Compass	Schedule Rating Plan 25% Maximum Credit
Connecticut Indemnity	Participating Dividend Plan 10% Increase in Base Rates

Company	Rate Action
Continental Insurance Companies	Revised Base Rates, Increased Expense Constant from $35 to $60 25% Maximum Schedule Rating
Boston Old Colony Ins. Co. The Buckeye Union Ins. Co. Commercial Ins. Co. of Newark, NJ The Continental Ins. Co. The Fidelity & Casualty Co. of NY Firemen's Ins. Co. of Newark, NJ The Glens Falls Ins. Co. Kansas City Fire & Marine Ins. Co. London Guarantee & Accident Co. of NY National-Ben Franklin Ins. Co. of ILL Niagara Fire Ins. Co. Phoenix Assurance Co. of New York	
The Fidelity & Cas. Co. of NY	8% increase in rates from Continental
Firemen's Ins. Co. of Newark, NJ	-12% decrease from in rates from Continental
Niagara Fire Ins.	-12% decrease in rates from Continental
Kansas City Fire & Marine Ins. Co. Niagara Fire Ins. Co.	New Retention Plan
Cumis Ins. Society Inc.	Ref. NCCI 17.1% Pure Premium 15% Increase
Eagle Star Insurance Co. of America	Flat 15% Reduction in Base Rates
Electric Mutual	State Wide Increase in Base Rates 7.98 effective 1/1/84
Employer's Casualty Co.	NCCI 1/1/84 Pure Premium Adjusted by Factors
Employers' Fire Ins. Co.	Sliding Scale Dividend Loss Ratio Plans - Maximum 28 to 45%
Enterprise Insurance	NCCI 1/1/84 Adjusted with Factor 1.325
Equity Mutual Insurance Co.	Maximum 40% Schedule Rating Plan
Excalibur	Participating Dividend Plan
Excel Ins. Co.	Variable Dividend Plan Maximum 60% Credit Schedule Rating Plan Maximum 25%

Federated Mutual	Schedule Rating Plan 25% Maximum Credit Revised Rates For 5 Codes Base Rates Same as Effective 7/15/81
Federated Rural Electric	10% Off Base Rates of NCCI Pure Premium
Fidelity & Deposit of Maryland	25% Maximum Schedule Rating
Fire and Casualty of Connecticut	Flat 15% Reduction in Rates Plus 30% Maximum Schedule Rating Plan Plus 5 to 20% Maximum (Coal) Loss Ratio Dividend Plan
Fireman's Fund Companies Fireman's Fund American National Surety Corporation American Automobile American Automobile of Illinois	Schedule Rating Plan 25% Maximum Credit
Fireman's Fund American National Surety Corp. American Automobile Associated Indemnity Corp. Fireman's Fund of WI	NCCI Base Rates 1/1/84 Applied Factor 1.567
General Accident Group General Accident Ins. Co.of America	Revised Rates Back to 1/15/81 Base Rates 10% Reduction
Camden Fire Ins.	+25% Schedule Rating 1/15/81 Base Rates
Pennsylvania General Ins.	1/15/81 Base Rates 10% Decrease in Base Rates
Georgia Casualty and Surety Co.	NCCI Pure Premium Filing +17.1% 1/1/84
Great American Insurance Companies American National Fire Agricultural American Alliance	Schedule Rating Plan 25% Maximum Credit
Great America Ins. Co.	NCCI Pure Premium Rates with Factor of 1.31
American National Fire Agricultural American Alliance	Factor of 1.541 Factor of 1.31 Factor of 1.31
Great Central Ins. Co.	Maximum 50% Schedule Rating

Great West Casualty Co.	60% Maximum Schedule Rating Plan
Hanover Companies Hanover Insurance Massachusetts Bay	Schedule Rating Plan 25% Maximum Credit
Harco National Ins. Co.	Schedule Rates Maximum 25%
Hartford Fire	15% Reduction in Base Rates Applied for all Companies NCCI Pure Premium 1/1/84
Hartford Accident and Ind. Hartford Casualty Ins. Co. New York Underwriting Ins. Twin City Fire Ins. Co.	Factor Applied 1.453 8.7% Increase
Home Insurance	Schedule Rating Plan 40%Maximum Credit
Home Insurance	Variable Participating Dividend Plan (Dividends based on final earned premium)
Home Indemnity Home Indemnity of Indiana City Ins.	NCCI Pure Premium Factor 1.507 - +14.8%
Home Ins.	NCCI Pure Premium Factor 1.281 - 2.4% Decrease
Ideal Mutual Insurance Co.	10% Off Base Rate Plus Maximun 50% Schedule Rating 10 Safety Dividend Plans A1 through 10
Indiana Insurance Companies Indiana Consolidated	Schedule Rating Plan 40% Maximum Credit
Indiana Lumbermens Mutual	Schedule Rating Plan 40% Maximum Credit
Insurance Company of State of PA	Adoption of NCCI Basic Manual 11.1% Rate Increase
International Business & Mercantile Reassurance	Underground Coal Mine Rates Effective 10/1/83
Iowa National Mutual Insurance Co.	NCCI Pure Premium 17.1% + Factor 1.6835

Company	Rating Plan
Kemper Group Lumbermen Mutual Casualty Co. American Motorists Insurance Co. American Motorists Ins. Co. American Manufacturers Mutual Ins. Co. American Protection Ins. Co.	NCCI 1/1/84 Pure Premium with Factor 1.505 Applied
Kentucky Central	Schedule Rating Plan Maximum 30% Credit
Kentucky Farm Bureau Mutual Ins.	11.2% Increase in Base Rates 1/1/84
Liberty Mutual Companies Liberty Mutual Liberty Mutual Fire Liberty Insurance Corp.	Expense Constant $35 Premium Discount 0-17% Maximum Credit Base Rates for Industrial WC Reduced 7.8% From NCCI Jan 1 Loss Cost Rates Schedule Rating Table Maximum 50% Modification
Lumbermens Underwriting Alliance	Schedule Rating Plan 50% Maximum Credit
Maryland Casualty Co. Valiant Ins. Co.	Schedule Rating Maximum 25% NCCI 1/1/84 Pure Premium 1.541 Factor Applied
Assurance Co. of America	1.310 Factor Applied
Northern Ins. Co. of New York	1.310 Factor Applied
Meridan Mutual Ins. Co.	Revised Schedule Rating 40% Maximum NCCI Pure Premium Revision of 1/1/84
Michigan Mutual Group Michigan Mutual Associated General	Schedule Rating Plan Credits/Debits up to 25%
Mid-Century Ins. Co.	"Sliding Scale" and Expense Factor Dividend Plan
Midland Insurance Co.	Maximum 25% Schedule Rating Plan
Midwestern Indemnity	Schedule Rating Plan 30% Maximum Credit 1/1/84 NCCI Pure Premium Factor 1.54 Applied

Company	Rate Action
Mission Ins. Group Inc. Mission Ins. Co. Mission National Ins. Co.	1/1/84 NCCI Pure Premium Rates +1.325 Factor
Morrison Assurance Co.	7/15/81 Base Rates
Motorist Mutual Insurance Co.	Maximum 25% Schedule Rating Plan - 15% Increase in Current Base Rates
National Mutual Ins. Co.	15% Off Base Rates Sliding Scale Loss Dividend Plan Flat Credit Plan
National Union Fire	Adoption of NCCI Basic Manual 0.1% Rate Increase
Nationwide Mutual Ins.	Maximum 25% Schedule Rating Plan
Nationwide Mutual Fire Ins. Co.	Maximum 25% Schedule Rating Plan
Northern Insurance Company of N. Y.	Flat 15% Reduction in Rates Schedule Rating Maximum 25%
Occidental Fire & Casualty Co. of N. C.	Maximum 25% Schedule Rating Plan NCCI Pure Premium 1/1/84 Filing Base Rates 17.1% Increase in Rates
Ohio Casualty Group American Fire & Casualty Ohio Casualty West American	NCCI Pure Premium Base Rates 40% Maximum Schedule Rating 17.5% NCCI Pure Premium Increase in Rates
West American	Revised Dividend Plan to 25%
American Fire & Casualty	Eliminated Dividend Plan
Old Republic Ins. Co.	Maximum 25% Schedule Rating Plan
	Revised Rates for Executive Officer who Waive the Act
Pennsylvania Millers Mutual Ins.	NCCI Premium Filing Base Rates Increase 17.1%

Company	Plan
Pa. Nat'l Mutual Casualty	Schedule Rating Plan 30% Maximum Modification
Preferred Risk Mutual Ins. Co.	NCCI Pure Premium Filing + Factor 1.414 Base Rates Insured 2.8
Providence Washington Group Providence Washington Motor Vehicle Casualty	Schedule Rating Plan Range from -25% to +25%
Reliance Companies Reliance Planet United Pacific	Schedule Rating Plan 25% Maximum Credit 67 Classifications Reduced 20% The Remaining Classifications -8% Maximum Schedule Rating 40%
Republic Western Ins. Co.	Excess Insurance for Self-Insurers
Royal Insurance Group	
Globe Indemnity	Schedule Rating Plan 40% Maximum Credit
Royal Indemnity	Loss Ratio Participating Plan (possible 24.7% dividend credit on risks producing $50,000 or more premium and 5% or less loss ratio) Schedule Rating Plan 25% Maximum Credit New Company Participating Retention Plan Program Possible Maximum 60% Dividend Sliding Scale Loss Ratio Maximum 20% Credit New Loss Ratio Participating Plan - Minimum Premium $2,500
American & Foreign	Participating Dividend Plan (eligibility rule revised from $50,000 to $25,000)
Safeguard	Revised Filing 40% Schedule Maximum Rating Plan
American & Foreign Royal Indemnity Co.	One Year Early Dividend Plan Annual Premium 50,000 or More
Royal Insurance Group Factors	NCCI Pure Premium Rates with
American and Foreign Ins.	8.2% increase
Globe Indemnity Co.	3.4% increase
Newark Ins. Co.	8.2% increase
Royal Ins. Co. of America	8.2% increase
Royal Indemnity Co.	8.2% increase
Safeguard Insruance Co.	3.4% increase

Company	Rating
Safeco Insurance Co. of America	Maximum 25% Schedule Rating Plan
St. Paul Companies St. Paul Fire & Marine St. Paul Mercury	Schedule Rating Plan 25% Maximum Credit 1/1/84 NCCI Base Rates 17.1% Increase
Security Group Security of Hartford Connecticut Indemnity	Schedule Rating Plan 25% Credit Only 1/1/84 NCCI Pure Premium 17.1% Increase in Base Rates
Seibels, Bruce and Company South Carolina Consolidated American Ins. Co. Kentucky Insurance Co.	1/15/81 NCCI Base Rates Increased 10% for all 3 co.
Sentry Insurance	Schedule Rating Plan 25% Maximum Credit NCCI Pure Premium Some Classes Reduced by 1.58
Sentry Ins. A Mutual Co.	20 to 25% 22 Classes Manual Rates all other classes 15%, Sliding Loss Ratio Plan 20% Maximum Credit
State Farm General	NCCI Pure Premium
Tokio Marine and Fire Ins. Co., Ltd.	Maximun 50% Schedule Rating Plan
Tower Insurance Co.	Flat 15% Rate Reduction in Base Rates
Transamerica	Schedule Rating Plan 20% Maximum Credit Revised to 40% Adoption by Reference NCCI 1983 Pure Premium Less 5%
Transamerica	Net Retention Participating Plan Will Not Ref. NCCI 1984 Pure Premium
Transamerica Indemnity	Schedule Rating Maximum 40% Credit
Transamerica Ins. Co. of Michigan	Adoption Pure Premium 1983 Loss Ratio NCCI Rate Level Schedule Rating 40% Maximum

Transamerica Transamerican Ins. Co. of Michigan	Keeping Old Rule and Rates in Effect
Transit Casualty Co.	Sliding Scale Loss Ratio Dividend Plan 50% Maximum Schedule Rating
Transport Indemnity	Average Rate Increase of 13.3% 5/1/84
The Travelers Insurance Co. Group The Travelers Insurance Co. The Travelers Indemnity Co. The Travelers Indemnity Co. of Illinois The Travelers Indemntly Co. of RI The Charter Oak Fire Insurance Co. The Phoenix Insurance Co.	Maximum Schedule 40% Plus Participation Plan 1.5 Decrease in Base Rates Adopted NCCI 1/1/84 Pure Premium Filing
The Travelers Indemnity Co. of America	+16.3% Reduction in Base Rate
The Travelers Indemnity Co. of RI	Minimum Premium Charge Reduced for 3 Year Policy $200 to $125
U. S. F. & G Group Fidelity & Guaranty Ins. Underwriters United States Fidelity & Guaranty Co.	Maximum 25% Schedule Rating Plans
United States Fidelity & Guaranty Co.	Base Rates 1.7% Below NCCI 1/1/84 Filing
Fidelity & Guaranty Underwriters Fidelity & Guaranty Ins.	Revised Loss Ratio Dividend Plans based on Premium Size and Losses Revised Expense Constant Reduced Overall Base Rate 1.7% Preferred Risk Dividend Plan
Fidelity & Guaranty Underwriters	Revised Expense & Retention Dividend Plan
Fidelity & Guaranty Ins.	Participating Dividend Plan
U. S. Insurance Group United States Fire North River Westchester Fire International	Schedule Rating Plan 50% Maximum Credit NCCI Pure Premium 1984 Base Rates Reduced for all By Factors
North River Westchester Fire	Participating Dividend Plan

Company	Plan
Universal Underwriters	Independent Rate Revision (Reduce NCCI base rates effective 7/15/81 approx. 5.3%)
Utica Mutual	Schedule Rating Plan Maximum 25% NCCI Pure Premium 1/1/84 + Factor 1.567
Wausau Companies Employers of Wausau Wausau Underwriters Worldwide Insurance	Schedule Rating Plan 40%Maximum Credit
Wausau Underwriters	Schedule Rating Plan Flat 15% Reduction in Rates (Plus 25% Credit under Schedule Rating Plan, for a possible 40% Reduction)
Employers of Wausau Wausau Underwriters	Graduated Dividend Plan (Deferred Final Premium Computation) Plan #3500
Western Insurance Companies Western Indemnity Western Casualty & Surety Western Fire	Schedule Rating Table 25% Maximum
Westfield Companies Westfield Ohio Farmers	Schedule Rating Plan 25% Maximum Credit
Zurich Insurance Co.	Maximum 25% Schedule Rating Plan NCCI Pure Premium 1/1/84 17.1% Increase in Rates

Up-dated June 1, 1984

All Pages Printed with State Funds.

Department of Commerce
INSURANCE DIVISION
COMMERCE BUILDING, SALEM, OREGON 97310 PHONE (503) 378-4271

September 6, 1984

Honorable Peter W. Rodino, Jr.
Chairman, Committee on the Judiciary
U. S. House of Representatives
Washington, D. C. 20515

Dear Mr. Chairman:

Thank you for inviting our comments on competitive rating for workers' compensation insurance in Oregon. We are pleased with the effect of the new law on Oregon insurance buyers.

Competitive rating has been emerging as the style of state insurance regulation for several years. Workers' compensation is the last property-casualty insurance coverage to be removed from rigid prior approval control. As the results from Oregon and other states become known, you can be confident other states will take similar action.

Oregon had the highest workers' compensation insurance rates in the nation as recently as 1979. One of the undeniable benefits of the McCarran-Ferguson Act has been allowing states to seek solutions to these problems which can be tested and proven before being adopted in other parts of the country.

Here is a brief history of our workers' compensation rating laws: Prior to 1966, Oregon was a "monopolistic" state. All workers' compensation insurance was written by a state fund. Employers could elect not to be subject to the Workers' Compensation Act and could purchase employers liability insurance. Several leading workers' compensation insurers were servicing that market. The State Accident Insurance Fund (SAIF) has competed with private insurers since 1966. All insurers were required to adhere to the bureau rates, rating plans and systems, and policy forms. SAIF insured about half the market.

The Honorable Peter W. Rodino, Jr.
September 5, 1984
Page Two

Insurers were allowed by 1977 law to file percentage deviations from bureau rates. About 15 insurers used this privilege to file downward deviations, generally 15 to 20%.

Fully-competitive rating became effective July 1, 1982. Each insurer must independently file its entire rating system. The National Council on Compensation Insurance, the licensed rating organization, became essentially advisory and is prohibited from filing any provisions for expenses, taxes, profit or contingencies. All insurers have adopted the Basic Manual of the National Council for their basic classification and rating system, with several filing subclasses and exceptions.

The National Council files claim cost data ("pure premiums") for each classification. Insurance companies may file rates and use them without waiting for our approval ("file-and-use") so long as they are not below the pure premium rates (claims cost). Each insurer must independently file its own premium discount schedule, minimum premiums, expense constants, and other rating values. There has been competitive pressure as well as regulatory constraint on all these filings.

With that background, we shall answer your specific questions.

1. <u>How have rates changed?</u> The costs of claims, or "pure premium" rates, are a good standard denominator. If mandatory adherence to bureau rates were still required, rates would be about 46% above pure premiums (or claims would be about 68% of premium rates). The percentage deviations in effect prior to 1982 would lower the average rate level to about 35% above pure premiums.

   Our latest estimates of rate levels filed under competitive rating is an average of only about 15% above pure premium. This is equivalent to a <u>22%</u> decrease from standard bureau rates.

The Honorable Peter W. Rodino, Jr.
September 5, 1984
Page Three

We are not able to precisely estimate the effect of the several subclasses filed by insurers. These are likely to reduce the average rate level by 3 to 5% further. Some subclasses have reduced specific rates 30 to 50% below rates for the standard parent classes.

2. <u>What has happened to rates for small businesses?</u> The very smallest businesses have premiums determined only by manual rates for their classes or by insurer minimum premiums. These have benefited most directly by the changes in rate levels. Minimum premiums remain at pre-1982 amounts while they have been increasing in states where insurers adhere to bureau filings.

   We know of several instances where small employers are being accepted by insurers with the lowest rates. Even those businesses insured at higher-than-average rates are paying substantially less than they would pay at standard bureau rates.

   The next larger-sized businessses may qualify for one of the accelerated premium discount plans filed by several insurers. Some of these plans begin discounting premiums at $2000 while the bureau standard plans in other states start at $5000 premiums.

   Subclasses directly benefit small business in the affected industries. A few examples of approved subclasses are: log truck hauling, parts departments of automobile dealers, school cafeterias, restaurants in nursing homes or hospitals, plus security workers in sawmills and some other plants.

3. <u>Has availability been affected?</u> We have had few problems with availability either before or after competitive rating was enacted. The State Accident Insurance Fund, and other insurers, are willing to cover most businesses. The Assigned Risk Plan, started in 1979, remains very small.

The Honorable Peter W. Rodino, Jr.
September 5, 1984
Page Four

4. <u>How have small insurers been affected?</u> Small independent insurers usually have selected market segments to which they remain loyal and offer excellent service. Most of these have retained their market shares. Small insurers affiliated with large corporate groups have been affected by shifts in marketing strategy within the groups. You should appreciate this distinction when receiving any statistical data presented to your committee.

5 and 6. <u>Has there been an increase in market concentration?</u> No clear long-term trend has been observed yet. SAIF's share of the insured market has been reduced from 50% to 45%. Some self-insured employers have elected to become insured. The number of insurers active in the market has increased. A few insurers which had major market shares have chosen to withdraw or reduce their Oregon business. Some others have increased marketing efforts. No increased tendency toward an oligopoly can be identified.

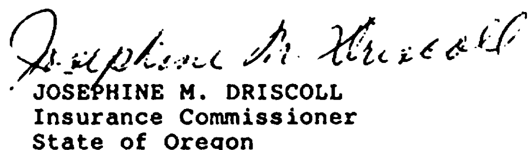
7. <u>How has the statistical data base been affected?</u> Our statutes and administrative rules both require adherence to a uniform statistical plan. Insurers with subclasses and other non-standard rating provisions are required to convert data to the standard basis for reporting to the National Council. The quality and usefulness of the data base should be unchanged.

Fears that insurers with non-standard rating plans would report non-standard data are no longer often heard. We believe we have given sufficient regulatory attention to assuring data integrity. A standardized data base is appreciated by insurers as being useful to them and is probably the original reason for forming rating bureaus.

Some information others have compiled on the effects of our competitive rating law are enclosed.

We hope this description of Oregon law helps your committee understand how states are able to serve the public under the McCarran-Ferguson Act.

Sincerely,



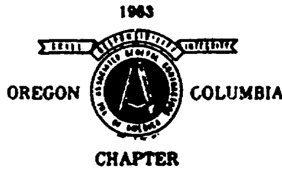
JOSEPHINE M. DRISCOLL
Insurance Commissioner
State of Oregon

JMD:lls

Enclosures

DEC 1 1983

THE ASSOCIATED GENERAL CONTRACTORS
of America, Inc.



November 29, 1983

Mr. Dick Franzke
Stoel, Rives, Boley, Fraser & Wyse
900 SW 5th Avenue
Portland, Oregon 97204

Dear Dick:

In 1976, which was during the period of time you chaired the AGC Workers' Compensation Committee, the Committee produced a report containing several recommendations for changes in Oregon's Workers' Compensation statutes.

Some of those have been implemented by the legislature. While the results of those efforts were not immediately measurable, they are now.

You may remember that in 1977 we produced a comparison of the costs of this insurance in Oregon with the costs in adjacent states. A copy of that comparison is enclosed.

I am again making a new comparison, and while that is not yet completed, I thought you would be interested in seeing what has happened with regard to rates in Oregon. Listed on the next page is a tabulation of the most common construction industry employment classifications and the rates for each in 1977 and 1983.

Overall, these rates have decreased an average of 47.26 percent in that six year period. The smallest decrease is 26.84 percent, while the largest is 60.32 percent. It should be noted that the 1977 rates do not include the Department assessment which, as I recall, was about 6 percent of the premium. The 1983 rates do include the 16.8 percent assessment. If the 1977 assessment had been included, the rate changes would appear even more dramatic.

/cmber 29, 1983
age 2

		OREGON RATES $/$100 of payroll		PERCENT
		[illegible]	[illegible]	REDUCED
1463	Asphalt Works	[illegible]	9.58	49.87
1624	Quarries, NOC	[illegible].43	8.63	44.07
4000	Sand or Gravel Digging	12.42	6.21	50.00
5213	Concrete Construction, NOC	15.00	8.80	41.33
5221	Concrete Work, Floors, etc.	9.15	5.93	35.19
5403	Carpentry, NOC	24.97	10.28	58.83
5506	Road Construction, Paving or Repaving	15.70	6.23	60.32
5507	Road Construction, Clearing of Right-of-way	17.53	8.87	49.40
5508	Road Construction, Rock Excavation	22.39	16.38	26.84
6003	Pile Driving, Building Foundations	31.40	18.70	40.45
6217	Excavation, NOC	1[illegible].97	6.07	59.45
6306	Sewer Construction	[illegible].41	11.59	54.39
6319	Gas and Water Main Construction	[illegible].71	6.27	54.27
8227	Contractors' Permanent Yards	[illegible].12	5.72	37.28

Two factors must be remembered. First, the 1977 rates were the gross cost of this insurance and would be reduced by individual dividends. Dividends are not available in 1983. Secondly, the changes can be largely attributed to the work performed by Karl Frederick of the Associated Oregon Industries.

But, even taking these factors under consideration, the AGC becoming involved during these past few years under your leadership and guidance was a major factor in these rate reductions. Policies established then are still being pursued diligently by our current committee, chaired by Dick Tuttle in an equally capable fashion.

Those in the construction industry owe you a debt of gratitude for the time and effort you spent during those years. I offer that on their behalf.

As I write this, I am reminded of the enormity of the gratuitous service provided by the Stoel, Rives, Boley firm for this trade association. I would be remiss if I did not specifically name Dick Alexander and John Bradach among the several members of the firm that have given far more than could be expected. I only wish we could somehow better acknowledge the major contribution all of you have made to Oregon's construction industry.

With best wishes,

Jack Kalinoski
Public Affairs Manager

lt
enclosure
cc/Bob Wilson
Dick Tuttle
Charles Schrader
Ken Twedt
AGC Workers' Compensation Committee

wcd news bulletin

A SPECIAL REPORT
ON THE
WORKERS' COMPENSATION SYSTEM

JUN 1 1983

Over the last few years, the Workers' Compensation Department has increased its efforts in supervising and enforcing claims processing requirements of the law. These efforts have resulted in noticeable performance improvements by insurance companies, in processing claims of their insured employers. This improvement has resulted in higher morale of injured workers, and reduced litigation and penalty costs, which eventually become employer expenses.

For example, the law requires that when a worker is injured and off the job, his first time loss check must be paid within 14 days of the employer's knowledge. If this is not done, the insurer (and thereby the employer) is liable to an additional amount of 25 percent of the amount due, plus the cost of attorney fees.

In 1978, insurers were only paying 76.8 percent of their first payments on time. Our increased efforts in supervision and enforcement had, by March 1983, resulted in insurers paying 90.7 percent of their claims on time.

FILE AND USE

Since 1982, Oregon has been under a "file and use" workers' compensation premium system.

MORE

2-2-2-2

This system allows all workers' compensation insurers to use any premium rate they wish, as long as the rate doesn't fall below a certain base rate. That rate is set by the state's Insurance Commissioner, through a national rating organization.

Insurers determine the cost factors (administrative cost, profit amount) on which they can operate, then add that to the base rate and file their rates with the commissioner for marketing use.

This has resulted in a very competitive market, and has contributed to a significant reduction in premium rates.

The significance is shown in the following three examples, from one of the state's largest insurers. The examples compare 1978 rates with current rates, and demonstrate the reductions realized with the file and use system.

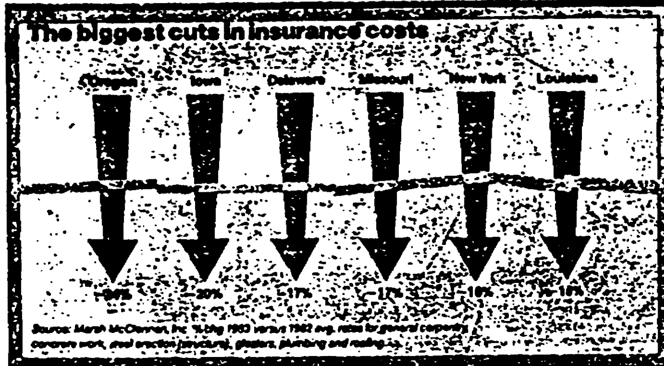
*SIC	Job Title	1/1/79 Premium Rate per $100 Payroll	1/1/83 Premium Rate per $100 Payroll	Percentage Reduction
2702	Logger	$31.69	$19.04	40
8292	Warehouseman	$ 7.81	$ 5.55	29
8387	Service Station Attendant	$ 7.94	$ 4.63	[illegible]

*Standard Industrial Classification

OCT 14 1983
...CTOR'S OFFICE

Workers' insurance costs climb 1.6%

Workers' compensation rates edged upward in 1983, according to a sample study of ENR's annual survey of rates for construction trades nationwide. The survey, prepared by Marsh McLennan, Inc., New York City, measures the dollar amount paid by contractors into insurance funds per $100 of payroll. Because the frequency and severity of accidents and resulting claims and settlements help determine individual rates, they vary widely from trade to trade and from state to state for the same trade. But an analysis of seven major trades in 44 states reveals a moderate upward trend despite rate reductions in a number of states.



The average cost of insurance coverage for carpenters, bricklayers, concrete workers, glaziers, plumbers, roofers and steel erectors fell into two equal camps: 20 states reporting higher rates and 20 states lower rates compared to 1982. Increases outweigh the declines, however, and in the U.S. as a whole contractors now pay an average workers' compensation rate of $10.67. This is up 1.6% from 1982's average of $10.50. (In four states insurance cost are unchanged. The remaining six state have separate state funds and are not included in the survey.)

Two New England states led the move to higher rates. Contractors in Massachusetts experienced the largest hikes in insurance costs as the average rate for the seven sample trades jumped 78%. This boosts the average workers' compensation rate in Massachusetts to $19.70, the fourth highest rate in the nation. Rhode Island rates made the second largest gain, climbing 34% to $15.07.

Hawaii replaced the District of Columbia as the most expensive area in the nation to insure workers, posting the third largest increase in workers' compensation rates. Workers in Hawaii now require $32.31 in insurance coverage for every $100 in pay, 31% above 1982's average rate. The District of Columbia backed down from 1982's peak of $30.08 as rates fell 29% over the year. It still ranks second in insurance costs at $21.20, just ahead of Connecticut's $19.85.

Last year Oregon's compensation rates, at $16.14, were the sixth highest in the nation. In 1983, however, insurance rates for the seven trades spotlighted by ENR were slashed 34%, to $10.72. This was the largest rate rollback reported in 1983 and helped drop Oregon insurance costs to 18th place among the states reported by Marsh McLennan.

A number of states received substantial reductions in insurance rates over the year (see chart). Average insurance costs are down 20% in Iowa, where contractors will get a big cost break on steel erection for structures. Insurance rates for this category tumbled over $8 per $100 of payroll in the past year to the current level of $16.49. In Delaware, Missouri and New York, rates have declined about 16% for the seven trades studied.

Missouri's hefty decline brought its average rate to $4.71 to become the second lowest rate in the nation. Industrial Indiana, however, still holds the lowest rate for the sample group, dropping from last year's low of $2.93 to $2.41, according to the Marsh McLennan survey.

Contractors hiring steel erectors for structures will, on average, be chipping in about one-fifth of their payroll, or a rate of $20.27, to the workers' compen-

Compensation insuranc

RATE IS PER $100 PAYROLL, COMPILED BY MARS

Effective July 1, 1983

CLASSIFICATION OF WORK	Ala.
Carpentry—1, 2 family residence	4.67
Carpentry—3 stories or less	5.05
Carpentry—interior cab wk.	2.80
Carpentry—general	5.6[illegible]
Chimney—construction brick con	7.11
Concrete work—bridges culverts-C	7.11
Concrete work—dwelling 1-2 family	2.96
Concrete work—N.O.C.	4.83
Concrete or cement work—floors, sidewalks	2.56
Electrical wiring—inside	2.06
Excavation earth N.O.C.	5.53
Excavation—Rock	—
Glaziers	4.95
Insulation work	4.51
Lathing	2.93
Masonry	3.12
Painting and decorating	5.34
Pile driving	14.06
Plastering	4.08
Plumbing	2.80
Roofing	8.84
Sheet metal work—erection—inst. & repair	4.1[illegible]
Steel erection—doors and sash	3.43
Steel erection—interior ornamental	3.49
Steel erection—structure	6.20
Steel erection—dwelling 2 stories	10.75
Steel erection—N.O.C.	8.56
Tile work—interior	3.14
Timekeepers and watchmen	2.61
Waterproofing (brush) interior	5.34
Waterproofing (trowel) interior	4.80
Waterproofing (trowel) exterior	3.12
Waterproofing (pressure gun)	4.83

CLASSIFICATION OF WORK	Miss.
Carpentry—1, 2 family residence	3.18
Carpentry—3 stories or less	4.56
Carpentry—interior cab wk.	3.15
Carpentry—general	6.29
Chimney—construction brick con	9.20
Concrete work—bridges culverts-C	9.20
Concrete work—dwelling 1-2 family	3.21
Concrete work—N.O.C.	3.43
Concrete or cement work—floors, sidewalks	2.80
Electrical wiring—inside	4.33
Excavation earth N.O.C.	5.52
Excavation—Rock	—
Glaziers	5.06
Insulation work	3.57
Lathing	3.56
Masonry	2.5[illegible]
Painting and decorating	2.73
Pile driving	17.73
Plastering	4.42
Plumbing	2.3[illegible]
Roofing	7.23
Sheet metal work—erection—inst. & repair	4.45
Steel erection—doors and sash	4.35
Steel erection—interior ornamental	4.35
Steel erection—structure	15.87
Steel erection—dwelling 2 stories	11.91
Steel erection—N.O.C.	6.18
Tile work—interior	3.51
Timekeepers and watchmen	2.84
Waterproofing (brush) interior	2.73
Waterproofing (trowel) interior	4.42
Waterproofing (trowel) exterior	2.57
Waterproofing (pressure gun)	3.43

● Specialty rates are left blank, refer to company ● ...

sation fund. This is the highest rate among the trades reported. Piledrivers, who are traditionally in a high-rate category, saw their national average compensation rate climb an added 2%, to $18.21.

The biggest rate hike among the 33 trades was 10.2% for roofers. This pushed their average rate to $17.87, the third highest in the nation. Employers of plasterers will have to contribute 7% more to cover their workers this year. Plasterers carry an average rate of $6.98. Over the same period, the average rate for electricians increased 4%, to $3.94

Workers involved in rock excavation had their rates cut by a third from 1982's level and now average $6.18. Tile workers also received a large downward adjustment of 10.4%.

Last year's highest rated category, wrecking, has been redefined and is now represented in seven new classifica-

...ase rates for construction workers

...LEHMAN, INC., NEW YORK, N.Y. ALL RATES EFFECTIVE 7/1/83 RATES ARE SUBJECT TO CHANGE ACCORDING TO EXPERIENCE RATING

Ala.	Ariz.	Ark.	Cal.	Colo.	Conn.	Del.	D.C.	Fla.	Ga.	Hi.	Idaho	Ill.	Ind.	Iowa	Kan.	Ky.	La.	Me.	Md.	Mass.	Mich.	Minn.
7.90	8.06	7.29	9.80	7.05	12.84	7.78	10.10	7.38	4.43	20.36	9.37	8.26	1.79	4.79	4.83	4.06	8.16	6.50	10.89	8.52	6.90	8.19
8.62	8.51	6.84	9.98	6.11	12.84	8.13	10.10	7.38	4.43	15.42	9.37	6.50	2.18	4.45	4.83	4.67	8.32	6.50	10.00	8.52	6.98	8.19
7.16	6.12	3.77	—	4.74	9.28	—	9.08	4.42	3.10	15.87	4.11	4.57	1.43	3.13	3.73	2.52	4.49	7.84	7.73	4.57	5.21	8.19
8.35	10.84	6.90	11.85	7.27	11.45	8.13	15.00	8.86	4.70	84.13	7.82	8.46	2.35	7.72	5.48	5.82	7.84	19.90	9.57	16.12	10.86	15.06
5.67	10.80	10.44	15.91	10.03	18.98	6.20	21.58	10.83	5.76	47.77	9.86	12.00	1.91	12.21	7.10	4.96	7.90	18.75	15.77	13.95	14.94	10.45
5.47	10.80	10.44	15.91	10.03	18.92	—	21.58	10.83	5.76	47.77	9.86	12.00	1.91	12.21	7.10	4.96	7.80	18.75	15.77	13.95	14.94	10.45
8.99	4.21	3.35	—	6.36	8.79	8.74	13.52	5.77	2.27	14.88	4.48	3.29	1.08	3.42	3.20	2.96	3.26	8.36	14.17	8.31	9.78	5.21
8.08	6.44	5.77	9.85	7.14	18.42	8.74	20.40	8.20	4.75	27.08	5.85	13.45	1.84	7.16	4.43	3.52	5.16	14.58	22.10	12.64	11.44	10.18
8.82	5.50	4.03	—	5.23	11.42	4.81	8.80	6.12	3.14	13.77	3.48	4.75	1.20	4.36	3.69	3.51	3.75	7.71	7.20	6.57	7.28	4.04
7.38	4.54	2.72	4.36	3.35	3.87	2.83	10.71	3.87	2.83	13.13	3.83	3.93	1.07	5.22	1.86	2.50	2.56	5.73	6.80	3.50	3.83	3.06
7.47	4.06	6.41	5.68	7.13	7.86	6.78	12.97	8.82	4.58	27.75	8.00	4.85	1.55	5.20	3.90	3.70	5.82	11.50	8.72	5.32	8.20	8.18
—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
2.06	5.88	5.41	10.57	5.78	14.01	7.97	16.73	6.83	6.52	33.20	8.34	6.24	2.53	5.33	5.45	4.25	5.41	11.18	10.23	8.46	6.90	10.46
6.95	4.30	5.21	15.84	7.45	14.82	8.13	11.21	8.12	4.33	16.18	5.87	6.50	1.86	3.90	6.69	3.83	4.30	10.36	9.86	6.20	7.36	8.56
7.87	5.07	4.14	6.26	5.34	6.18	7.22	8.50	6.08	2.50	15.30	4.46	4.12	1.18	3.84	3.73	3.25	3.17	7.54	7.47	6.03	6.61	—
6.78	9.19	4.00	8.27	9.79	14.17	6.20	20.77	8.83	3.87	18.88	5.48	5.10	1.40	4.14	4.22	2.87	3.46	10.04	9.40	10.41	7.10	7.43
6.00	4.48	5.23	8.62	5.07	10.19	10.46	13.66	6.05	3.83	16.80	8.10	6.82	2.02	4.90	5.45	5.74	6.27	11.30	10.74	11.00	—	10.58
2.44	17.83	24.28	19.74	23.02	24.33	12.20	38.99	12.08	9.83	44.30	17.58	19.85	3.52	10.84	16.17	7.53	18.02	30.32	30.82	14.00	18.43	17.48
8.50	9.95	4.35	11.48	7.24	10.14	7.22	10.12	6.75	4.33	22.90	8.73	6.46	1.83	4.00	4.06	3.04	5.22	10.32	6.87	7.20	6.81	6.81
8.05	4.84	3.62	5.57	5.18	5.80	3.22	12.47	4.80	3.44	11.57	3.82	4.86	1.20	3.90	2.73	2.40	4.00	7.30	8.40	5.25	4.54	6.19
9.99	17.16	12.25	24.67	16.93	27.27	24.01	22.80	17.31	7.70	44.35	17.26	13.40	4.12	9.38	13.63	10.83	11.84	27.20	24.86	52.80	47.86	24.40
8.76	4.54	5.33	6.62	5.44	10.03	9.68	13.54	5.54	4.88	11.48	4.42	5.58	1.86	5.12	4.49	3.23	4.56	8.41	8.83	7.33	7.54	5.99
4.26	9.87	6.14	7.68	4.80	13.49	8.54	15.72	5.16	3.83	11.46	6.02	8.84	1.15	4.04	3.82	3.64	4.49	9.07	8.06	7.82	7.00	10.33
4.26	9.87	6.14	7.68	4.80	13.49	—	15.72	5.16	3.03	11.46	6.02	8.84	1.15	4.04	3.82	3.64	4.49	9.07	8.06	7.92	7.00	10.33
14.30	6.90	18.84	16.17	12.61	47.80	—	40.45	12.19	9.98	37.11	12.81	20.79	3.46	14.49	8.90	10.73	11.31	34.50	45.57	30.32	21.00	20.58
10.56	17.65	18.45	—	15.11	29.49	—	—	15.86	12.85	46.71	—	18.84	3.96	12.58	13.63	10.50	13.50	27.17	21.33	38.70	—	—
13.63	11.90	9.55	16.47	14.30	25.70	16.25	43.33	11.23	11.50	42.12	9.51	21.57	5.53	18.30	16.17	6.57	8.93	19.85	23.30	28.70	16.17	20.13
6.70	4.20	3.30	5.80	4.07	7.32	5.05	25.58	4.10	2.35	13.90	4.65	3.78	1.04	2.82	3.23	2.82	4.30	7.24	6.85	5.65	7.25	5.90
5.28	3.33	6.36	—	3.77	6.19	—	14.25	3.82	4.34	13.50	3.79	4.84	1.00	2.83	2.72	2.46	5.24	8.55	5.00	8.58	5.00	—
10.00	4.49	5.23	8.82	5.07	10.19	—	13.60	6.05	3.83	16.60	6.10	6.82	2.02	4.90	6.45	5.74	6.27	11.33	10.74	11.03	—	10.56
9.50	9.95	4.35	11.48	7.24	10.14	—	10.12	6.75	4.33	22.92	8.73	8.46	1.63	4.00	4.08	3.04	5.22	10.32	8.87	7.20	8.91	6.81
16.78	9.19	4.00	8.27	9.79	14.17	6.20	20.77	8.83	3.87	18.66	5.48	6.10	1.40	4.14	4.22	2.87	3.46	10.04	9.40	10.41	7.10	7.43
8.06	6.44	5.77	9.85	7.14	18.42	—	20.40	8.20	4.75	27.00	5.65	13.45	1.84	7.16	4.43	3.52	8.18	14.58	22.10	12.64	11.44	10.18

Mo.	Mont.	Neb.	Nev.	N.H.	N.J.	N.M.	N.Y.	N.C.	N.D.	Ohio	Okla.	Ore.	Penn.	R.I.	S.C.	S.D.	Tenn.	Tex.	Utah	Vt.	Va.	W.Va.	Wisc.
3.18	9.65	4.18	—	8.35	8.32	8.28	6.63	4.00	—	—	7.20	8.98	8.16	7.20	5.90	4.22	5.13	8.87	—	3.32	5.72	—	4.76
3.18	9.65	4.30	—	8.35	7.74	10.87	6.63	4.00	—	—	8.07	10.75	7.56	8.14	5.98	4.22	5.13	9.54	—	3.32	8.06	—	3.54
3.44	6.44	2.66	—	4.29	5.45	6.71	—	2.87	—	—	4.45	6.58	—	5.37	4.86	3.01	2.94	6.12	—	2.89	6.17	—	3.51
3.35	13.37	5.80	—	8.52	7.40	9.83	5.24	5.80	—	—	7.79	11.20	7.56	9.28	8.82	6.97	5.07	9.54	4.81	4.26	7.72	—	7.30
3.73	13.46	6.48	—	11.73	7.90	22.73	6.58	6.83	—	—	18.07	13.98	9.00	13.17	8.15	8.27	6.37	18.97	6.43	7.84	10.84	—	11.01
3.73	13.46	8.48	—	11.73	7.90	22.73	6.58	6.03	—	—	18.07	13.98	—	13.17	8.15	8.27	6.37	—	6.43	7.64	10.84	—	11.01
2.15	5.07	2.65	—	7.65	8.33	7.94	—	2.80	—	—	4.28	6.32	12.36	7.23	3.53	2.64	2.36	—	3.11	2.93	3.85	—	3.16
4.51	5.09	3.66	—	11.26	6.06	14.51	10.49	4.10	—	—	7.52	9.66	12.36	10.02	5.02	4.78	3.99	8.85	5.30	5.54	7.05	—	5.76
2.76	5.80	3.10	—	5.42	—	6.72	5.29	2.62	—	—	4.36	6.52	4.50	6.09	3.35	3.00	3.81	—	3.72	2.80	4.78	—	4.50
1.71	4.33	2.81	—	4.26	2.81	5.08	3.04	2.00	—	—	3.56	2.77	4.30	5.14	5.23	2.36	2.64	4.00	2.09	2.71	3.85	—	2.72
3.22	8.15	3.85	—	12.77	8.18	9.32	7.61	4.45	—	—	7.14	4.67	8.24	7.84	5.75	5.42	4.77	—	3.57	6.23	5.42	—	4.00
—	—	—	—	—	6.18	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
4.27	7.82	3.76	—	8.21	6.37	8.01	7.82	4.18	—	—	6.84	5.82	9.14	9.73	4.71	4.63	3.48	6.23	5.07	4.30	5.07	—	4.64
4.36	10.66	4.50	—	9.68	6.06	9.56	4.91	4.87	—	—	7.23	4.26	7.50	7.82	4.71	4.26	4.06	9.30	4.48	4.06	5.80	—	7.81
2.47	4.86	3.04	—	7.32	5.43	6.28	6.29	3.06	—	—	4.27	6.13	7.42	5.07	3.71	3.06	3.36	4.46	4.17	3.24	6.37	—	4.11
3.08	12.75	4.45	—	7.65	7.86	8.08	7.53	2.80	—	—	5.82	8.76	9.00	8.37	4.58	3.34	3.48	6.64	3.01	4.24	6.90	—	3.67
4.12	10.38	2.92	—	8.66	8.70	6.98	6.58	4.86	—	—	6.13	8.23	12.16	9.18	7.39	3.63	3.58	5.98	3.78	3.79	7.24	—	4.31
9.83	27.11	11.28	—	20.39	10.53	34.82	16.41	13.27	—	—	21.43	20.52	13.01	24.41	11.19	10.34	10.34	21.53	14.88	12.83	11.49	—	12.23
2.92	9.00	4.47	—	9.27	5.43	10.13	11.24	3.45	—	—	6.50	9.90	7.42	8.30	4.94	3.92	3.46	10.18	3.84	4.82	5.94	—	3.52
2.86	7.00	2.65	—	5.19	3.57	7.27	4.03	2.00	—	—	5.10	3.91	6.11	3.74	3.96	2.81	2.00	5.14	3.11	2.18	4.36	—	3.59
7.31	25.10	14.20	—	26.35	10.28	21.52	—	8.97	—	—	21.18	19.58	16.82	24.12	13.78	11.30	7.58	19.15	10.27	10.66	18.18	—	14.13
2.94	7.42	2.94	—	4.88	5.30	4.88	5.21	4.13	—	—	4.92	5.05	9.13	6.12	6.15	3.26	3.79	8.76	3.32	3.58	5.84	—	3.88
3.66	7.18	3.28	—	6.71	—	8.38	3.48	3.24	—	—	6.50	7.90	9.42	7.33	4.47	3.50	3.33	6.40	3.98	3.87	7.05	—	3.90
3.60	7.18	3.28	—	6.71	—	9.38	3.48	3.24	—	—	6.50	7.90	—	7.33	4.47	3.50	3.33	6.40	3.98	3.87	7.06	—	3.90
7.76	32.17	8.64	—	26.74	21.30	20.80	16.42	17.27	—	—	20.88	16.02	—	40.84	15.26	9.36	7.10	36.48	—	13.33	24.05	—	11.32
7.86	22.74	9.64	—	25.74	9.71	24.80	7.24	10.28	—	—	30.61	18.24	—	—	12.85	11.23	8.42	—	11.80	10.71	16.10	—	12.84
10.00	20.61	12.40	—	12.40	10.00	13.36	14.83	6.25	—	—	17.13	15.76	22.94	36.15	11.20	8.24	8.46	12.33	5.91	10.47	20.17	—	8.29
2.87	5.29	2.96	—	2.96	3.36	7.25	6.16	2.86	—	—	4.11	6.20	6.16	4.77	3.00	2.00	2.62	3.03	2.71	2.79	4.32	—	3.08
2.71	4.86	2.28	—	7.28	4.52	4.86	6.33	3.76	—	—	5.11	4.01	—	8.76	3.29	2.11	2.00	4.31	3.14	3.83	3.91	—	4.85
4.12	10.38	2.92	—	8.66	9.70	5.90	6.58	4.86	—	—	6.13	8.23	—	9.18	7.30	3.83	3.58	5.98	3.78	3.79	7.24	—	4.31
2.92	9.00	4.47	—	9.27	5.43	10.13	11.24	3.45	—	—	6.50	9.90	—	8.30	4.94	3.92	3.46	10.18	3.84	4.82	5.94	—	3.52
3.08	12.75	4.45	—	7.85	7.86	8.06	7.53	2.80	—	—	6.82	8.76	9.00	8.37	4.30	3.34	3.46	6.04	3.01	4.24	6.90	—	3.67
4.51	6.80	3.66	—	11.28	6.06	14.51	10.49	4.10	—	—	7.52	8.06	—	10.09	5.02	4.76	3.89	8.85	5.30	5.54	7.05	—	5.76

N.D., Ohio, W.Va., state monopolistic rates.

ESU3++

10-26-83

NOV 3 1983

Daily Journal of Commerce USPS 143-580 PRICE FIFTY CENTS

Workers' comp costs low for high-tech firms

By KEVIN RENNER
Daily Journal of Commerce staff

If you run a high-tech company and you want workers' compensation costs slashed, move to Oregon.

Or so suggests a recent study that surprised even its author.

Research just completed by a consulting firm shows Oregon with the second lowest workers' compensation rates for high-technology manufacturing among nine states with high concentrations of high-tech industry.

According to PlanTek, a Salem-based information and data base management company, Oregon's high-tech employers pay lower rates than their counterparts in Texas, California, Massachusetts, Florida, Arizona, Washington and Michigan. Only Colorado offers high-tech employers lower workers' compensation rates, concludes the five-month study.

Rodney Stubbs, president of PlanTek, notes Oregon's average workers' compensation rate is skewed by large industries, especially logging, with high injury rates. State-by-state comparisons on such averages are therefore meaningless, Stubbs says.

Stubbs agrees that many observers would be surprised by his study's findings. "I was surprised by what we found," he admits. [illegible] he did not see the low rates for high-tech until he began analyzing state figures this summer while doing research for Mitsubishi Corp.

Stubbs says other factors have contributed to low workers' compensation rates for high-tech industry here. He says state legislative changes since 1977 have cut workers' compensation rates by 50 percent. In eight job categories involving high-tech manufacturing, rate reductions ranged from 3.6 percent to 75.1 percent between Jan. 1, 1979 and Jan. 1, 1983, PlanTek reports.

Stubbs acknowledges state-by-state comparisons are difficult, but not impossible. While different job classifications are used by different states, Stubbs was able to match the high-tech categories. And to make payroll rate comparisons meaningful, all information was translated to rates per $100 of payroll.

A state compensation expert says he is "pleased that the study came out favorable to Oregon." But, cautions Stanley Sparks, regional director of the National Council on Compensation Insurance, such comparisons can be dangerous.

While costs to employers may be compared, benefit levels are not always in line with costs, he says. And, he continues, compensation rates do not reflect the final cost of insuring workers. Companies with less frequent accident records get reimbursements, he notes.

Even given those considerations, Stubbs says the report bodes well for the state. He says Oregon, contrary to the opinions of many, is in a strong position to attract high-technology manufacturing when the industry starts working near capacity in 1984 and 1985.

"With the facts out, Oregon rates very highly," for high-tech manufacturing, Stubbs says. "As we go into the latter part of next year, site search activity should start picking up and continue a stronger push into 1985. And there are a lot of people in preliminary search phases for locations interested in the Pacific Northwest."

FYI
Dick

BEST AVAILABLE COPY

Letter from The Hon. Mary Rose Oakar, Member of Congress, to Chairman Rodino.

MARY ROSE OAKAR
20TH DISTRICT, OHIO

DISTRICT OFFICE:
523 FEDERAL COURT BUILDING
215 SUPERIOR AVENUE
CLEVELAND, OHIO 44114
(216) 522-4927

WASHINGTON OFFICE:
2436 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-5871

Congress of the United States
House of Representatives
Washington, D.C. 20515

COMMITTEES:
BANKING, FINANCE AND URBAN AFFAIRS

POST OFFICE AND CIVIL SERVICE
Chair, Subcommittee on Compensation and Employee Benefits

SELECT COMMITTEE ON AGING
Chair, Task Force on Social Security and Women

COMMITTEE ON HOUSE ADMINISTRATION

WHIP AT LARGE

September 13, 1984

The Honorable Peter Rodino
Chairman
Subcommittee on Monopolies
and Commercial Law
Washington, D.C. 20515

Dear Chairman Rodino:

Thank you for your leadership in holding these hearings today on how insurance prices are set. Although I understand your discussion today will be on more technical matters, I would like to call your attention to a new rate-setting policy for health insurance that is unfair and dangerous to Ohio senior citizens.

A constituent has written to me, appalled that his monthly health insurance premium jumped $150 on his 60th birthday. This is because Blue Cross/Blue Shield is now basing their premiums on age for individual and small-group subscribers in Ohio. For people over 50 years old, this new policy means rates have risen as high as 50 to 100 percent. A recent article in the Cleveland Plain Dealer, describing this situation more fully, is enclosed for your information.

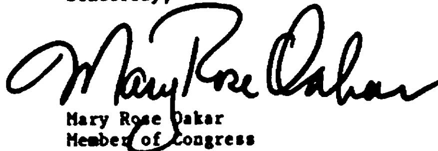
Blue Cross/Blue Shield calls the new age-rating system fair. I call it blatant age discrimination. The purpose of health insurance is to spread risk over a large group so that all individuals can be assured of protection. Age-rating, however, isolates the elderly. It singles out those who are more likely to experience health problems because of their years, and penalizes them with unaffordable premiums just when they most need the protection insurance promises. This is, unquestionably, not fair.

The issue of fairness in insurance rates is of great concern to all Americans. We spend 12 percent of our disposable income on insurance premiums, making insurance our fourth largest purchase after food, housing and taxes. We do this to prevent the financial disasters of serious illness or injury. Therefore, we cannot afford inequity or discrimination.

Congress has delegated authority to the states to regulate the insurance industry and provide for consumer protection. But this does not mean we can wash our hands of matters like the one in Ohio. Unfair insurance rates and practices are everyone's concern. If states cannot or will not control them, the responsibility to do so rests here in this Congress.

Mr. Chairman, I commend you and your Committee for your investigation into these matters. I respectfully request that this letter and enclosure be entered into the record as but one example of the problems that remain to be solved.

Sincerely,



Mary Rose Oakar
Member of Congress

Cleveland Plain Dealer   August 26, 1984

Birthday greeting from Blue Cross: 'Pay more'

By Bob Becker

When Nate Anselmo celebrates his 50th birthday Sept. 7, his enjoyment will be tempered. That is the day his Blue Cross/Blue Shield bill will zoom $53 a month.

It will rise 20%, from $271 a month to $324 a month, and Anselmo is frustrated. He doesn't know why it is happening and he doesn't know what to do about it.

Anselmo is a short, intense, wiry man who works 16 hours a day wholesaling fresh produce and hustling snacks at Johnny's Hot Dog at the West Side Market.

Hard physical work has been his life, but lately he is distracted by the nagging burden of high health insurance bills and the fear of serious illness.

The worry gnaws away at the cushion he wants in his middle age. His secure family life and the comfort of his Valley View home do not diminish it.

"I'm not crying poor. I'm crying justice That's my future," he said.

Three brothers and a sister have died of heart disease and a nephew just had open heart surgery, so Anselmo worries more these days about doctors and hospitals.

"It's such a fear," he said. "You have to have hospitalization."

Anselmo looks around and sees plants closing and middle-aged people losing their jobs. That $324 a month health insurance bill looms large when he wonders if

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the same could happen to him.

"Why should they be penalized at this age, when they should stop worrying?" he asked.

For Anselmo and for thousands of others here who buy their own Blue Cross/Blue Shield plans, a tougher bottom-line attitude at "Mother Blue" means they will pay more as they get older.

On July 1, Blue Cross/Blue Shield introduced "age rating" for some 75,000 subscribers enrolled in small group and individual subscriber pools. Some subscribers in those pools, especially those older than 50, saw their rates climb by 10% to 100.%

Insurance industry statistics show that people run up higher hospital and doctor bills as they age. Blue Cross/Blue Shield officials say they had to raise their rates because competitors were grabbing all the best risks while its own aging subscribers were not paying their fair share.

"It's fair and equitable for people to pay their load," said company spokesman Jerome W. Rogers.

These single and small group subscribers have not in the past paid premiums equal to what the company paid out in claims for them, according to Rogers.

"We believe they are finally paying their share," he said.

But Anselmo said he wonders if Blue Cross executives and its board are doing their best in holding down hospital costs and in running the company.

"How much does the president make? Who's on the board? Do they benefit from this? I'm sure they have good reasons (for their decisions), but do they think of the other guy?" he asked.

Some of that information won't be available to consumers any more.

The merger that was approved by the Ohio Department of Insurance July 17 allowed Blue Cross and Blue Shield (formerly Medical Mutual of Cleveland Inc.) to escape reporting the salaries of top executives and where subscribers' premiums are invested.

In 1983, Blue Cross reported to the Ohio Department of Insurance that it paid President Donald R. Riordan $120,000. Two assistants earned $90,000 and seven other Blue Cross executives made between $56,000 and $70,000.

Rogers contends company executives are doing a good job and they are paid less than the industry going rate. The state will still require Blue Cross/Blue Shield to prove it is doing a good job in holding down costs whenever it applies for a rate increase.

But Anselmo doesn't know the fine points of Ohio's easygoing regulation of health insurance companies, under which most rates charged are not controlled.

He only knows that it hurts a lot when he has to pay the bill.

"Blue Cross used to be good security for the people. But somewhere along the way they've gone mad," he said.

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Letter from Bill Gunter, President, National Association of Insurance Commissioners, to Chairman Rodino.

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS
1125 Grand Avenue Kansas City, Missouri 64106 (816) 842-3600

September 28, 1984

The Honorable Peter W. Rodino, Jr.
Chairman
Committee on the Judiciary
2462 Rayburn House Office Building
Washington, D.C. 20515

Re: McCarran-Ferguson Act Hearings

Dear Mr. Chairman:

I am the President of the National Association of Insurance Commissioners (NAIC). The NAIC requested, but was not given the opportunity, to testify at the recent hearings on ratemaking and open competition in the insurance industry. The NAIC has a wealth of information on this topic which can be made available to your Committee for its deliberations. The NAIC stands ready to provide this information upon your request.

The NAIC is the association of the chief insurance regulators of all of the U.S. states and territories. Each state has its own rating and competition laws. These laws vary from state to state and are tailored to the needs of each individual state. It is the firm belief of the NAIC that individual state laws are more responsive to the needs of the citizens of those states than could be any blanket federal law, which would of necessity be the same in each of the states. The McCarran-Ferguson Act provides that the regulation of the business of insurance is best handled at the state level. Ratemaking and competition laws are yet another example of the wisdom of this Act.

At the hearings which took place on September 13, the Commissioner of Michigan, Nancy Baerwaldt, testified. Ms. Baerwaldt is a member of the NAIC. However, she was not representing the NAIC in her testimony, and some of her remarks do not represent the position of the NAIC.

Very truly yours,

Bill Gunter

Bill Gunter
President
NAIC

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