IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

METLIFE, INC., *Plaintiff,* v. FINANCIAL STABILITY OVERSIGHT COUNCIL, *Defendant.*	Civil Action No. 1:15-cv-45 (RMC)

BRIEF OF THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS AS *AMICUS CURIAE* IN SUPPORT OF PLAINTIFF METLIFE, INC.

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

PAGE

FEDERAL STATUTES

OTHER AUTHORITY

I. IDENTITY AND INTEREST OF *AMICUS CURIAE*

Founded in 1871, the National Association of Insurance Commissioners ("NAIC") is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia, and five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review, and coordinate regulatory oversight. NAIC staff supports these efforts, and the NAIC represents the collective views of state regulators domestically and internationally. The NAIC members, together with the centralized resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

The NAIC's purpose is to provide its members with a national forum enabling them to work cooperatively on regulatory matters that transcend the boundaries of their own jurisdictions. This not only allows for consistency in regulating companies that do business in multiple states, but it provides a central point of communication and facilitation for joint initiatives with federal and international regulators. The NAIC also regularly assists federal regulators, federal agencies, members of Congress and the Government Accountability Office by providing information and data related to state insurance regulation, health insurance issues, terrorism insurance, annuities, insurance fraud and many other topics. The NAIC is a founding member of the International Association of Insurance Supervisors and remains extensively engaged with our international counterparts in developing the elements of a stronger international insurance regulatory framework.

Collectively, the state insurance commissioners work to develop model legislation, rules, regulations, handbooks, white papers and actuarial guidelines that promote and establish uniform regulatory policy. Their overriding objectives are to protect consumers, maintain the financial solvency of insurance companies and the financial stability of the insurance industry as a whole.

The NAIC performs numerous crucial services on behalf of state governments including: developing and publishing model laws, regulations, bulletins, financial and accounting standards, white papers, consumer guides, handbooks, periodicals and the *Proceedings of the NAIC*. Hundreds of state and federal laws assign duties to the NAIC and incorporate NAIC standards, models and other publications. NAIC model laws, regulations and other standards as implemented by the states are a critical part of the robust regulatory structure in place to monitor the financial solvency of MetLife and other insurers. In addition, the NAIC manages and coordinates the accreditation review of insurance departments as well as maintains regulatory and financial databases of insurance company financial data.

The interest of the NAIC in this case arises out of the regulatory responsibility vested in each commissioner as part of the state-based system of insurance regulation. The insurance commissioners of the various states are charged with the responsibility of regulating the business of insurance within their respective jurisdictions pursuant to the McCarran-Ferguson Act of 1945, 15 U.S.C. §§ 1011 to 1015 (2012) ("McCarran-Ferguson Act"). The NAIC and its members have an interest in conveying to the Court the critical role state insurance regulation plays in monitoring the financial condition of an insurer and preventing, identifying, and reacting to any financial distress. Just as the Financial Stability Oversight Council (FSOC) is required to consider the degree to which a company is already regulated before it designates a company for consolidated supervision and oversight, it is critical that this Court understand and consider the regulatory structure already in place as it reviews FSOC's designation of MetLife.

II. ARGUMENT

FSOC is empowered to subject a U.S. nonbank financial company to supervision and certain prudential standards if the Council determines that material financial distress at that company could pose a threat to the financial stability of the United States. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 12 U.S.C.A. § 5323(a)(1) (2010). Congress took several steps to ensure that when the company under consideration for designation is an insurance company the views and expertise of state insurance regulators are considered. First, a state insurance commissioner serves as a non-voting member of the Council. *See* 12 U.S.C.A. § 5321(b)(2). Second, an independent member with insurance expertise is one of the voting members. *Id* at § 5321(b)(1). Third, the Council is required to consider "the degree to which the company is already regulated by 1 or more primary financial regulatory agencies." *Id* at § 5323(a)(2)(H). Finally, the Council is required to consult with the primary financial regulatory agencies before making a designation that the company is a systemically important financial institution ("SIFI"). *See* 12 U.S.C.A. § 5323(g).

In spite of all of these requirements and in spite of FSOC's assertion that it "considered the extent to which MetLife is subject to supervision and regulation," it appears FSOC largely ignored or discounted the state regulatory system and the views of state regulators and its own insurance expert in favor of speculation, assumptions about consumer and regulatory responses to distress that have no basis in fact or history, and a flawed analysis of the insurance business and its regulation. FSOC, *Explanation of the Basis of the Financial Stability Oversight Council's Final Determination that Material Financial Distress at MetLife Could Pose a Threat to U.S. Financial Stability and that MetLife Should Be Supervised by the Board of Governors of the Federal Reserve System and Be Subject to Prudential Standards*, p. 20 (December 18, 2014)

("Final Designation"). The State Insurance Commissioner Representative on FSOC, Commissioner Adam Hamm from North Dakota, made this point in his public statement on MetLife's designation:

> To effectively assess how regulation mitigates the risks the firm poses to financial stability, the Council should have sought to match the areas of concern to the authorities of existing regulators to address those concerns. The Basis fails to do this. As a result, the Basis fails to acknowledge that most, if not all, of the concerns it identifies (several of which have questionable merit) are addressed by the existing regulatory structure. This omission makes the Council's rationale for its decision fundamentally flawed. Final Designation at 305-306.

Similarly, Roy Woodall, the Council's Independent Member Having Insurance Expertise, dissented from the designation of MetLife and voiced concerns that it "failed to appreciate fundamental aspects of insurance and annuity products, and, importantly, State insurance regulation and the framework of the McCarran-Ferguson Act. . . The analysis discusses in detail, and is dismissive of, the U.S. State insurance regulatory framework, the panoply of State regulatory authorities, and the willingness of State regulators to act, thereby overstating shortcomings and uncertainties that are inherent in all regulatory frameworks, State or Federal." Final Designation at 299-300.

The size of MetLife is invoked over and over again by the Council in its basis for determination. State regulators and the NAIC do not dispute that MetLife is a large, complex company. But FSOC's analysis cannot stop at size. FSOC is also required to consider the robust system of regulation already in place and should have analyzed how this system serves to mitigate the risks FSOC identifies. State regulators have a vast arsenal of tools and statutory power to regulate for solvency and policyholder protection at the legal entity level, coordinate supervision at the group level, obtain early warning that a company may be troubled, take action if financial distress occurs, and proceed with orderly resolution if insolvency occurs. In submitting this brief, the NAIC seeks to assist the Court by describing in detail the regulatory scrutiny already applied to MetLife and in doing so, support MetLife's contention that FSOC acted arbitrarily and capriciously in failing to take existing regulation fully into account.

A. FSOC failed to adequately consider the full range of regulatory tools available to state regulators at the individual entity and group level.

The standard by which entities are subjected to a change in regulation, or deregulated, should be high. We agree with Commissioner Hamm's statement that "suggestions or assertions that a consolidated regulator would more effectively address the identified potential risks should be supported by a description of the tools, how they explicitly address the systemic risks identified, and experience from past financial crises." Final Designation at 307. FSOC has not compared the presumptive advantages of consolidated federal oversight with the existing state-based system, nor has it credited state regulators for their evolved and effective approach to supervision of legal entity insurance companies and holding companies[1].

Each of MetLife's insurance subsidiaries is subject to extensive regulation at the state level, including, but not limited to, investment limits, risk-based capital (RBC) and reserving requirements, reporting and statutory accounting standards, and "constant and ongoing supervision and examination." JA__Letter from Benjamin M. Lawsky, Superintendent, New York Department of Financial Services to Jacob Lew, Secretary of the Treasury (July 30, 2014)

[1] As an initial matter, the NAIC notes that misperception remains about the financial distress experienced by American International Group, Inc. ("AIG") in 2008. To whatever extent state-based insurance regulation might be disregarded because of AIG's failure, it bears repeating that "In September 2008, AIG's international insurance subsidiaries were thriving and profitable, but its Financial Products Division experienced a severe liquidity shortage due to the collapse of the housing market." *Starr Int'l Co. Inc. v. U.S.,* No. 11-779C, 2015 WL 3654465 at *6 (Fed. Cl. June 15, 2015). Strong consumer protection and reserve requirements at the state level were ultimately mitigating factors for AIG, and they would similarly benefit any holding company.

("Lawsky Ltr."). These highly regulated insurance subsidiaries account for 98% of MetLife's consolidated assets, 96% of its liabilities, and 95% of its revenues. Complaint at 13, *MetLife, Inc. v. Financial Stability Oversight Council*, No. 15-cv-45, 2015 WL 3422486 (D. D.C. May, 22 2015). New York also closely regulates MetLife's derivatives portfolio and securities lending activities. Superintendent Lawsky informed FSOC that MetLife's derivatives program is "well collateralized, conducted almost exclusively for hedging purposes, and not concentrated in any counterparty or group of counterparties…MetLife conducts its securities lending program within its life insurance subsidiaries alone, which in New York means the program is subject to restrictions on size, concentration limits, and counterparty creditworthiness." JA__Lawsky Ltr. at 2. FSOC conducted no analysis of the efficacy of the state regulatory system generally or the specific New York laws, regulations, and other standards applicable to MetLife.

The examination authority referenced by Superintendent Lawsky and other state regulators who submitted information to FSOC is crucial to the demonstrated success of state-based insurance regulation. All insurance commissioners have the authority to examine companies whenever deemed necessary, as well as a requirement to examine all domestic insurers no less frequently than every five years. *See Accreditation Program Manual*, NAIC, pg. 125 (January 1, 2015).[2] In order to create best practices and promote consistency in financial regulation for each state's domiciled insurers, the NAIC continuously updates the Financial Condition Examiners' Handbook, which is the standard referenced in all states' laws. *See id.*

[2] The NAIC's accreditation program establishes and maintains standards to promote sound insurance company financial solvency regulation. Regulation of multi-state insurance companies is enhanced and adequately monitored with emphasis on adequate solvency laws and regulations, financial analysis and examination processes, appropriate organizational and personnel practices in each accredited state, and effective and efficient review of organization, licensing and change of control. The NAIC reviews each state's laws, regulations and department practices to determine compliance with Accreditation Standards. All U.S. states are currently accredited.

The NAIC's Risk-Focused Surveillance Working Group regularly reviews the effectiveness of financial analysis and examination functions, and it creates a forum for peer reviewing among state departments of insurance.

While effective oversight of insurance companies that are part of a larger holding company is undoubtedly more complicated, the NAIC and its members have been enhancing this authority since the initial adoption of the Insurance Holding Company System Regulatory Act in 1969 ("Holding Company Act"). See 1 NAIC *Model Laws, Regulations and Guidelines*, 440-1 to 440-38, 20XX WL 8342889 (1969, amended 2010). The Holding Company Act requires the insurer to file annual reports detailing material intercompany contract terms and relationships. The commissioner is also empowered to review and approve cost-sharing agreements, material management agreements, major reinsurance agreements, material transactions and requests for extraordinary dividends. This reporting and regulatory review and approval of intercompany transactions helps ensure the insurance company's assets and expenses are closely monitored.

FSOC claims that "state insurance regulators generally do not have direct authority to require a non-mutual holding company of a state-licensed insurer or any non-insurance company subsidiary to take or not take actions outside of the insurer for the purpose of safety and soundness of the insurer." Final Designation at 242. There are two problems with this statement. First, it discounts the value of state regulatory authority to order production of books and records in the possession of the insurer's affiliates, a power that has existed in the Holding Company Act since 2001. Second, it ignores the significant expansion of and enhancements to state-level group supervision that was implemented in 2010 and will be required for each state's continued accreditation as of January 1, 2016.

The NAIC and state regulatory response to the financial crisis of 2008 included many revisions to the Holding Company Act to strengthen the state supervisory system:

> One of the lessons learned from the financial crisis was the need for regulators to be able to assess the enterprise risk within a holding company system and its impact or contagion upon the insurers within that group. Therefore, U.S. insurance regulators want to enhance certain prudential features of group supervision within the models and monitoring practices, providing clearer "windows" into group operations, while building upon the existing "walls" that provide solvency protection for insurers. Kris DeFrain, *Insurance Group Supervision*, (Center for Insurance Policy & Research/NAIC), April 2012.

Under the revised Act, the commissioner has the power to examine any insurer authorized to do business in that state and which is a member of an insurance holding company system, and its affiliates, "to ascertain the financial condition of the insurer, including the enterprise risk to the insurer by the ultimate controlling party, or by any entity or combination of entities within the insurance holding company system, or by the insurance holding company system on a consolidated basis." 1 NAIC *Model Laws, Regulations and Guidelines*, 440-24, 20XX WL 8342889 (1969, 2010). Group supervision conducted by state insurance regulators provides for submission of financial statements of the entire holding company system including non-regulated entities and unrestricted access to information in the possession of the insurer, the parent or any other entity within the system including non-regulated entities.[3] It also includes fit and proper requirements, rights of inspection and approval and intervention powers for certain transactions involving insurers. *See* JA__Letter from Thomas B. Leonardi, Commissioner,

[3] A related initiative in this area is the NAIC Risk Management and Own Risk and Solvency Assessment Model Act ("ORSA"), which requires an insurer or insurance group to maintain a risk management framework commensurate with the nature, scale and complexity of the insurer or group. Topics for the filing include an assessment of risk exposure and group assessment of risk capital and prospective solvency. This model act is scheduled to become an accreditation standard in the next few years.

Connecticut Insurance Department to Jacob Lew, Secretary of the Treasury, Schedule A, p. 6 et. seq. (October 24, 2014) ("Leonardi Ltr.").

In addition, the revised Act requires the ultimate controlling person of the insurer subject to registration to file an annual enterprise risk report that will "identify the material risks within the insurance holding company system that could pose enterprise risk to the insurer." 1 NAIC *Model Laws, Regulations and Guidelines*, 440-7 and 440-18, 20XX WL 8342889 (1969, 2010). The revised version of the Holding Company Act has been adopted by 49 jurisdictions[4], including states such as New York and Connecticut with primary regulatory authority over MetLife. *See* NAIC, Implementation of 2010 Revisions to Model #440, Insurance Holding Company System Regulatory Act [status as of June 9, 2015], www.naic.org/documents/committees_e_related_smi_dashboard.pdf.

The 2010 revisions also granted to the commissioner the power to initiate a supervisory college for any domestic insurer that is part of an insurance holding company system with international operations. A supervisory college may be convened as a temporary or permanent forum to assess the insurer's business strategy, financial position, legal and regulatory position, risk exposure, risk management and governance processes. The New York State Department of Financial Services, which supervises MetLife's largest insurance subsidiary and serves as the lead insurance regulator for the MetLife group of companies, hosts an annual supervisory college for MetLife and also holds "telephonic meetings in the interim to facilitate collaboration, cooperation and coordination among supervisors." JA__Lawsky Ltr. at 3. As the Connecticut

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[4] The number of states that have not implemented Model #440 is three. The NAIC provides this information to correct the Scholars of Insurance Regulation estimate of six outstanding states. *See* Brief of Scholars of Insurance Regulation Amicus Br. at 9, *MetLife, Inc. v. Financial Stability Oversight Council*, No. 15-cv-45, 2015 WL 3422486 (D. D.C. May, 22 2015) ("Scholars Br."). Correction of the Scholars on the scope of state regulators authority relative to non-insurer affiliates and holding companies is contained above.

Insurance Commissioner told FSOC, "the college greatly enhances and facilitates both the sharing of information about MetLife's financial performance and in the understanding of its global risk management processes. Most importantly, the college provides for comprehensive, coordinated regulation of MetLife." JA__Leonardi Ltr. at 3.

FSOC in its designation focuses only on its view that supervision of MetLife by state regulatory authorities does not include direct authority over every entity in a holding company system. However, in doing so, FSOC fails to adequately consider the totality of the state regulatory system and, as Commissioner Hamm noted, fails to identify what additional regulatory tools could address the risks FSOC identifies. Instead of conducting any analysis of the efficacy of coordinated regulation at the state level, FSOC dismissed it. Given the success of the NAIC's members in effectively regulating MetLife and in expanding available state regulatory tools after the financial crises, the designation of MetLife as a SIFI might fairly be called a fix in search of a problem.

B. FSOC failed to assess the risk of asset liquidation against existing regulatory authority to actively prevent a "run on the bank" scenario, including early warning through risk-based capital requirements and stays on surrender activity.

FSOC continues to raise the specter of a "run" on a large insurer by policyholders, which could throw a troubled company (and apparently the life insurance industry) into full-blown insolvency seemingly overnight. *See* Final Designation at 138. As Commissioner Hamm pointed out:

> Fears of surrenders leading to mass asset liquidation are thus unfounded, as insurance regulators have the ability and, moreover, the responsibility to take action in such an event…It is worth noting that our authorities are flexible and provide us substantial means to quell panic. Final Designation at 306.

The practical aspects of insurance products, particularly in the area of life insurance, simply don't support these fears. The very process of underwriting for life insurance policies demonstrates the overall predictability of payouts. Actuarial forecasting allows life insurers to anticipate their liability with an enviable amount of specificity, relative to other industries. Furthermore, life insurance and annuity products are valued by consumers for the long-term savings buildup. Unlike countless banking products, insurance products are not designed to allow access to funds on demand, and often contain deterrents such as the policy limitations or penalties for early withdrawal.

In addition to not adequately considering the nature of insurance and annuity products and likely responses from insurers and insurance consumers, FSOC also failed to adequately consider the many tools state insurance regulators have to ensure that adequate resources are maintained to meet insurer obligations and to step in if financial distress occurs. State insurance commissioners are consistent in mandating certain capital standards because of accreditation requirements and the NAIC's Risk-Based Capital for Insurers Model Act ("RBC Act"). See 1 NAIC *Model Laws, Regulations and Guidelines*, 312-1 to 312-14, 20XX WL 83428733 (1993, amended 2011). The RBC Act was adopted in 1993 to require capital levels to correspond with the risk factors of the policy type:

> The Act's main purpose is to ensure that insurers' risk-capital levels reflect a rational relationship with the riskiness of the policies that are insured. The Act provides "trigger points" by which regulatory bodies can gauge the strength of insurers and assess the need for state regulatory intervention. Conrad D. Brooks, *Risk-Based Capital: Provide for the Computation of Risk-Based Capital Levels for Insurers and the Submission of Risk-Based Capital Reports by Insurers; Provide for the Authority of the Commissioner of Insurance to Take Action; Provide Immunity from Civil Action to Receivers*, 13 Ga. St. U. L. Rev. 212, 213 (1996).

Under the RBC Act, every domestic insurer reports its RBC levels on an annual basis in accordance with NAIC-issued RBC instructions. The instructions contain a formula that was developed (and is regularly updated) as an additional tool to assist regulators in the financial analysis of insurance companies. The purpose of the formula is to establish a minimum capital requirement based on the types of risks to which a company is exposed. Separate RBC models have been developed for each of the primary insurance types: Life, Property/Casualty, Health and Fraternal. This reflects the differences in the economic environments facing these companies.

After RBC filings are submitted, the NAIC conducts quality assurance by cross checking the RBC information against the remainder of the company's annual financial reporting. Data validation failures are reported back to the company for an opportunity to resolve the inconsistency, after which any unresolved validation issues are reported to the domiciliary regulator.

Under the RBC system, regulators have the authority and statutory mandate to take preventive and corrective measures that vary depending on the capital deficiency indicated by the RBC result. If the total capital level is not sufficient in light of attendant risks, the commissioner has the authority to order specific corrective action. See 1 NAIC *Model Laws, Regulations and Guidelines*, 312-7 to 312-9 20XX WL 83428733 (1993, amended 2011). These preventive and corrective measures are designed to provide for early regulatory intervention to correct problems before insolvencies become inevitable, thereby minimizing the number and adverse impact of insolvencies.

The NAIC RBC formula generates the regulatory minimum amount of capital that a company is required to maintain to avoid regulatory action. There are four levels of action that can be triggered under the formula: company action, regulatory action, authorized control and mandatory control levels. Each RBC level requires some particular action on the part of the regulator, the company, or both. For example, an insurer that breaches the Company Action Level must produce a plan to restore its RBC levels. This could include adding capital, purchasing reinsurance, reducing the amount of insurance it writes, or pursuing a merger or acquisition to bolster its financial reserves.

The RBC system operates as a tripwire that gives regulators clear legal authority to intervene in the business affairs of an insurer upon the occurrence of one of the action levels specified in the RBC law. RBC alerts regulators to undercapitalized companies while there is still time for the regulators to react quickly and effectively to minimize the overall costs associated with insolvency. RBC provides a baseline of objective standards and regular reporting without diminishing a commissioner's flexibility to obtain and consider additional information under more general authority granted by a state's insurance code.

In addition to this objective, uniform, maintenance-focused RBC standard, state insurance regulators also have a variety of tools in the case of a specific troubled company, including the longstanding authority to impose stays on policyholder surrenders. Under the Insurer Receivership Model Act, a rehabilitation plan for a life insurer "may also propose imposition of a moratorium upon loan and cash surrender rights under policies, for a period not to exceed one year from the entry of the order approving the rehabilitation plan, unless the receivership court, for good cause shown, shall extend the moratorium." 1 NAIC *Model Laws, Regulations and Guidelines*, 555-38, 20XX WL 8342898 (1936, amended 2007). FSOC acknowledges that a state regulator may issue a stay "at its discretion to preserve assets or to calm fears that the insurer will be unable to meet its obligations to policyholders." Final Designation at 21. A commissioner can even consider need-based exceptions for release of funds on a case-by-case basis. FSOC's scenario of mass surrenders and withdrawals by MetLife policyholders assumes, with no evidence or historic precedent, that state regulators would not act to prevent the financial distress of an insurer and then would sit idly by as these unprecedented events occurred. In its designation, FSOC managed to create a scenario where declining to issue a stay or deciding to issue a stay would have equally disastrous consequences, suggesting that "the imposition of a stay on discretionary withdrawals could cause a loss of confidence, particularly if other insurers are simultaneously experiencing some level of financial distress." Final Designation at 144-145. Again, FSOC's analysis is stripped of meaning when it assumes any decision a state regulator might make to be too little, too much, too soon or too late.

Aside from the authority to issue stays, insurance commissioners also have the benefit of central organization, communication and administrative support through the NAIC to manage the resolution of a large, complex holding company. The NAIC and its members have a tremendous amount of experience in coordinating multistate regulation, including examinations, investigations, and dealing with troubled companies, as well as multiple appropriate forums for such a response. Starting with early detection of distress, state regulators work together through the NAIC's Financial Analysis Working Group ("FAWG") to analyze nationally significant insurers and groups that exhibit characteristics of being financially troubled. FAWG allows regulators to confer on appropriate regulatory actions and strategies that will prevent further deterioration. The NAIC's Receivership Financial Analysis Working Group continuously monitors nationally significant insurers in receivership. Supervisory colleges, implemented through the Holding Company Act and discussed above, can also be called in order to coordinate a response among nations where necessary[5].

[5] The NAIC offers this discussion of collaborative action in part as a rebuttal to the Scholars of Insurance Regulation's claim that state insurance regulators are frequently not able to coordinate effectively among themselves. *See* Scholars Br. at 17.

These resources and the record of success for coordinated responses clearly demonstrate that the fear of "contagion" resulting from a run on insurer assets is greatly overstated. The Council expresses concern that state regulatory authorities "have never been tested by an event of the material financial distress of an insurance company of the size, scope, and complexity of MetLife's large insurance subsidiaries" without continuing this notion to its logical conclusion - state authorities have not been so tested because the existing regulatory structure has not allowed a comparable insurance failure. Final Designation at 22.

C. FSOC failed to assess the risk of MetLife's ultimate failure against the deliberate, incremental process that applies to troubled companies supervised by state insurance commissioners.

Capital requirements, investment limitations, reserving methods, risk-focused surveillance, and regular financial examination are similar to preventative medicine. Regulators' vigilance in these matters reduces the likelihood of serious infirmity in the future. In those cases where surveillance indicates a company's financial health could become a hazard to policyholders, state insurance regulators have direct authority to immediately order corrective action. Insurance commissioners have flexibility here, as "each legal entity insurer has unique characteristics and writes different products…accordingly, each insurance entity would react to stress differently and its regulator would appropriately respond differently to those specific circumstances." Final Designation at 307.

The authority to determine whether continued operation of an insurer might be hazardous to policyholders is provided in the NAIC's Model Regulation to Define Standards and Commissioner's Authority for Companies Deemed to be in Hazardous Financial Condition (#385). See 1 NAIC *Model Laws, Regulations and Guidelines*, 385-1 to 385-5, 20XX WL 8342884 (1985, amended 2008). First, under Section 3, the Model Regulation lays out conditions which may, either on their own or in combination with each other, be considered by the commissioner to make the determination:

A. Adverse findings reported in financial condition and market conduct examination reports, audit reports, and actuarial opinions, reports or summaries;

B. The NAIC Insurance Regulatory Information System and its other financial analysis solvency tools and reports;

C. Whether the insurer has made adequate provision, according to presently accepted actuarial standards of practice, for the anticipated cash flows required by the contractual obligations and related expenses of the insurer, when considered in light of the assets held by the insurer with respect to such reserves and related actuarial items including, but not limited to, the investment earnings on such assets, and the considerations anticipated to be received and retained under such policies and contracts;

D. The ability of an assuming reinsurer to perform and whether the insurer's reinsurance program provides sufficient protection for the insurer's remaining surplus after taking into account the insurer's cash flow and the classes of business written as well as the financial condition of the assuming reinsurer;

E. Whether the insurer's operating loss in the last twelve-month period or any shorter period of time, including but not limited to net capital gain or loss, change in non-admitted assets, and cash dividends paid to shareholders, is greater than fifty percent (50%) of the insurer's remaining surplus as regards policyholders in excess of the minimum required;

F. Whether the insurer's operating loss in the last twelve-month period or any shorter period of time, excluding net capital gains, is greater than twenty percent (20%) of the insurer's remaining surplus as regards policyholders in excess of the minimum required;

G. Whether a reinsurer, obligor or any entity within the insurer's insurance holding company system, is insolvent, threatened with insolvency or delinquent in payment of its monetary or other obligations, and which in the opinion of the commissioner may affect the solvency of the insurer;

H. Contingent liabilities, pledges or guaranties which either individually or collectively involve a total amount which in the opinion of the commissioner may affect the solvency of the insurer;

I. Whether any "controlling person" of an insurer is delinquent in the transmitting to, or payment of, net premiums to the insurer;

J. The age and collectability of receivables;

K. Whether the management of an insurer, including officers, directors, or any other person who directly or indirectly controls the operation of the insurer, fails to possess and demonstrate the competence, fitness and reputation deemed necessary to serve the insurer in such position;

L. Whether the management of an insurer has failed to respond to inquiries relative to the condition of the insurer or has furnished false and misleading information concerning an inquiry;

M. Whether the insurer has failed to meet financial and holding company filing requirements in the absence of a reason satisfactory to the commissioner;

N. Whether the management of an insurer either has filed any false or misleading sworn financial statement, or has released false or misleading financial statement to lending institutions or to the general public, or has made a false or misleading entry, or has omitted an entry of material amount in the books of the insurer;

O. Whether the insurer has grown so rapidly and to such an extent that it lacks adequate financial and administrative capacity to meet its obligations in a timely manner;

P. Whether the insurer has experienced or will experience in the foreseeable future cash flow or liquidity problems;

Q. Whether management has established reserves that do not comply with minimum standards established by state insurance laws, regulations, statutory accounting standards, sound actuarial principles and standards of practice;

R. Whether management persistently engages in material under reserving that results in adverse development;

S. Whether transactions among affiliates, subsidiaries or controlling persons for which the insurer receives assets or capital gains, or both, do not provide sufficient value, liquidity or diversity to assure the insurer's ability to meet its outstanding obligations as they mature;

T. Any other finding determined by the commissioner to be hazardous to the insurer’s policyholders, creditors or general public.

Item G in particular would allow the commissioner to consider whether any entity in the holding company system is insolvent, delinquent or threatened with insolvency. It is important to note these conditions may come to the attention of state regulators in many ways. They are not necessarily tied to scheduled financial examinations or annual reporting. This demonstrates not only the flexibility of state authority in this area, but the scope.

Next, the Model Regulation turns to the actions a commissioner may order once he or she has determined that continued operation of the insurer may be hazardous. Under Section 4(B), the commissioner may issue an order requiring the insurer to:

> (1) Reduce the total amount of present and potential liability for policy benefits by reinsurance;
>
> (2) Reduce, suspend or limit the volume of business being accepted or renewed;
>
> (3) Reduce general insurance and commission expenses by specified methods;
>
> (4) Increase the insurer's capital and surplus;
>
> (5) Suspend or limit the declaration and payment of dividend by an insurer to its stockholders or to its policyholders;
>
> (6) File reports in a form acceptable to the commissioner concerning the market value of an insurer's assets;
>
> (7) Limit or withdraw from certain investments or discontinue certain investment practices to the extent the commissioner deems necessary;
>
> (8) Document the adequacy of premium rates in relation to the risks insured;
>
> (9) File, in addition to regular annual statements, interim financial reports on the form adopted by the National Association of Insurance Commissioners or in such format as promulgated by the commissioner.
>
> (10) Correct corporate governance practice deficiencies, and adopt and utilize governance practices acceptable to the commissioner.
>
> (11) Provide a business plan to the commissioner in order to continue to transact business in the state.
>
> (12) Notwithstanding any other provision of law limiting the frequency or amount of premium rate adjustments, adjust rates for any non-life insurance product written by the insurer that the commissioner considers necessary to improve the financial condition of the insurer.

Each state is required to maintain language similar to Sections 3 and 4B of the Model Regulation. *See Accreditation Program Manual* at 130. The regulation, initially passed in 1985, was amended to strengthen this regulatory discretion and authority in 2008. Robust state laws and regulations such as this Model allow for early detection of financial distress and swift remedial action to prevent harm to policyholders and minimize the impact of financial distress.

A troubled company, once identified by state regulatory authorities, is not necessarily bound for insolvency proceedings. As early detection has improved, some insurers may be helped by alternative mechanisms including run-off or restructuring. *See Alternative Mechanisms for Troubled Insurance Companies*, NAIC white paper, p. 1 (2009). In a run-off situation, "the insurer ceases writing new business on all lines of business, but continues collecting premium and paying claims as they come due on existing business." *Id* at 5. Ultimately, operations will close while the company is still solvent. Voluntary restructuring, meanwhile allows a court to approve and implement an agreement with all creditors in order to accelerate the run-off. *Id.* at 11.

Should these alternative mechanisms not be appropriate for the insurer, progression to the insolvency phase is highly structured. As described in detail in the Insurance Receivership Model Act (#555), a commissioner continues to have a great deal of flexibility to determine the degree of intervention required. See 1 NAIC *Model Laws, Regulations and Guidelines*, 555-1 to 555-101, 20XX WL 8342898 (1936, amended 2007). Some situations may be addressed by rehabilitation or conservation. However, when a company is in more serious financial distress, the inquiry will proceed to liquidation:

> A typical liquidation order will: cancel all insurance policies issued by the insolvent insurer; stay all actions pending against the insolvent insurer; forbid the insolvent insurer from continuing to defend its policyholders; and temporarily stay all actions against the policyholders to afford the receiver sufficient time to arrange for their defenses. Francine

> L. Semaya & Lenore S. Marema, *An Overview of the State Insurance Receivership System*, 27 Brief 12, 13(Fall, 1997).

The insolvency of an insurance company is separate and distinct from a traditional bankruptcy process for a very important reason: the protection of the policyholders whose premiums have financed the company's course of business. Actions that proceed under the federal bankruptcy code will be subject to the requirement that the cost of administration and government claims are the first to be paid in full. The insolvency approach is different:

> Costs of administration usually receive top priority, followed by wage claims of the insurer's former employees, usually up to a specified dollar amount. A high preference is then afforded to a group consisting of policyholders, beneficiaries, insureds, third-party liability claimants, and guaranty funds, while general creditors are placed in a priority at or close to the bottom of the list, often immediately above those with ownership interests in the insolvent insurer. Claims of government entities for taxes, fines, and other amounts past due are also given a relatively low priority by contrast to the federal bankruptcy system. Id. See also NAIC *Model Laws, Regulations and Guidelines,* 555 § 801, 20XX WL 8342898 (2007).

In addition to setting out priority of claims, insolvency statutes identify the applicable state court with jurisdiction over the insolvency proceedings. This process is intended to advance at the state level, with judicial oversight during the transition.

As has been pointed out to FSOC by state regulators throughout its designation process, "the nature of the fundamental insurance promise . . . makes insurance companies considerably easier to resolve than banks." JA__Lawsky Ltr. at 2. Life insurance company insolvencies are slow moving and can be deliberately managed by regulators, working with the state guaranty funds to keep policyholder losses to a minimum. This was demonstrated in the late 1980s and early 1990s, when a misplaced reliance on junk bonds caused several large life insurers to become impaired and, in some cases, insolvent:

> State insurance regulators placed a number of large insurers into rehabilitation and liquidation proceedings and imposed moratoriums on policy surrenders, policy loans, and cash withdrawals, subject to certain hardship exceptions. These actions, in combination with participation by Life Guaranty Associations, permitted the companies to either

> transfer blocks of business to other insurers or restructure policy obligations and to restructure investment holdings in a reasonable manner. JA__Letter from Dave Jones, Commissioner, California Department of Insurance, to Jacob Lew, Secretary of the Treasury, p. 3 (October 27, 2014).

As Commissioner Jones noted, this kind of supervision and restructuring effectively manages withdrawals and prevents a "run on the bank".

FSOC theorizes that, because its Interpretative Guidance requires consideration of obstacles to a "rapid and orderly resolution," taking adequate time to wind down an insurer's obligations favors designation. Final Designation at 252, n. 1190. This illustrates a fundamental misunderstanding of insurance company resolutions and the policyholder obligations they are designed to protect, and it favors "rapid" over effective. FSOC does not attempt to account for any state regulatory intervention as it hypothesizes an accelerating MetLife failure careening through regular financial examination, stringent RBC and other requirements, undetected under any hazardous financial condition standard, and liquidated in a haphazard and uncoordinated manner.

III. Conclusion

It appears that even if FSOC acknowledged the rigorous authority recounted here - the carefully applied capital standards, the ongoing financial examination and analysis, the expansion of group supervision authority, and the stringent, orderly progression of insolvency – FSOC's final word on the matter would be that MetLife is large and complex. Many insurance holding companies are large. Will each designation, when addressing Dodd-Frank's existing regulatory structure provision of § 5323(a)(2)(H), be identical? Other than conclusory statements, FSOC conducted no analysis to demonstrate that supervision by the Federal Reserve, under enhanced prudential standards that have yet to be determined, would do more to mitigate the alleged threat MetLife poses to financial stability in the U.S. than the existing robust system of state-based regulation.

The NAIC urges the Court to consider what FSOC is required to consider and what FSOC was told by its own voting insurance expert, the non-voting state insurance representative, and every state regulator who was consulted by or presented information to it: MetLife is a highly regulated company and the existing regulation has served the Company and its policyholders well. Simply put, FSOC acted in an arbitrary and capricious manner when it misunderstood, misconstrued, and dismissed the state regulatory system. For this reason, the NAIC supports MetLife's Motion for Summary Judgment.

Dated: June 26, 2015

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, the undersigned, hereby certify that I electronically filed the foregoing Brief of the National Association of Insurance Commissioners as *Amicus Curiae* in Support of Plaintiff MetLife, Inc. with the Clerk of the Court by operation of the CM/ECF system for the U.S. District Court for the District of Columbia. All participants are registered CM/ECF users and will be served by the Court's CM/ECF system.

Dated: June 26, 2015

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