



National Association of Insurance Commissioners

Via Electronic Mail

November 3, 2008

Ms Christine Lagarde
Minister for Economic Affairs, Finance and Employment - France
President, Economic and Financial Affairs Council
Council of the European Union
Rue de la Loi, 175 - 1048
Brussels, Belgium

Re: ***"Solvency II" Framework Directive***

Dear Ms. Lagarde:

With this letter, members of the National Association of Insurance Commissioners (NAIC) express serious reservations and concerns about several key aspects of the proposed "Solvency II" Framework Directive. Recent events have imposed real world challenges to some premises underlying the Solvency II proposal.

As the U.S. state government officials responsible for oversight of the world's largest insurance market, state insurance regulators, through the NAIC, agree with the commitment of the Economic and Financial Affairs Council, as expressed in its October 7 statement, which supported "further strengthening the existing prudential framework and risk management in the financial sector." We are further encouraged by the Council's recognition, specifically related to the Solvency II initiative, of "the need to modernize prudential regulation of insurance companies, given that existing solvency rules are out of date."

In the coming months, we are likely to see a shift in the financial regulatory paradigm. We all recognize that this new framework will need to remain committed to consumer protection and balance the respective roles of the public and private sectors in overseeing the safety and soundness of financial institutions. To meet this challenge, policymakers must successfully understand and incorporate "lessons learned" from the current financial crisis. Without question, some of the obvious lessons implicate critical elements of the Solvency II proposal:

- Reliance on institutions' enterprise risk management and use of internal models to set capital requirements;
- Allowance of diversification benefits in a group structure, including unregulated entities; and,
- Discriminatory treatment of non-EU insurers.

Although many essential components of Solvency II remain undefined, we question several features of the existing proposal, including the unbalanced focus on capital requirements and management's ability to assess and quantify risks using internal models. And, while we understand the EU struggle to design an effective approach to group supervision, recent events further emphasize that any approach must ensure that all entities within a financial holding company – and their policyholders or depositors – are treated fairly and their benefits and rights fully protected.

Further complicating these issues are inappropriately political comments from members of the EU Parliament, who, apparently relying upon false information or otherwise failing to understand the facts, disparage the state-

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based system of insurance regulation in the U.S. Comments expressing a preference for the creation of a federal regulator for insurance in the U.S. are similarly political, industry-focused comments that do not serve the interest of either constructive discussion or the consumers we protect. The misdirection of these comments, or the basis on which they were made, has led to the introduction of language in Solvency II that will impede any progress toward a shared goal of achieving “mutual recognition” of U.S. and EU insurance supervision.

Our comments are not intended to be an exhaustive catalogue of our concerns, which are numerous, but we look forward to the opportunity to present the details of these comments and our list of substantive concerns in further discussions at the earliest available time. It is also important that we note our commitment to continuing to work with our counterparts in regulatory policymaking in Europe in the European Commission and the Committee of European Insurance and Occupational Pension Supervisors (CEIOPS), and with parties to the legislative process in the EU to achieve the proper level of prudential oversight and consumer protection in the insurance sector and to find ways to achieve greater convergence of regulation worldwide, where appropriate. Should you have any questions, please feel free to contact George Brady in our Washington, D.C., Office at 202-471-3988 or by e-mail at gbrady@naic.org.

Sincerely,



Sandy Praeger
President of the NAIC
Commissioner, State of Kansas



Roger Sevigny
President-Elect of the NAIC
Commissioner, State of New Hampshire

Cc: - Dr. Thomas Steffen - BaFin/Germany; CEIOPS Chair
- Karel van Hulle – Head of Unit, Insurance and Pensions, European Commission