The NAIC Accreditation Program

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§1 Introduction

The National Association of Insurance Commissioners (NAIC) Accreditation Program (Program) is a unique method of providing national cohesiveness in a state based regulatory system. The Program is the result of tensions between those believing that the regulation of the insurance industry in America is best headed by the federal government and those believing that such regulation is best if guided by the individual states. As an initial matter, I, therefore, present a brief background discussion of the regulation of insurance in the United States. The fundamental discord--whether the federal or the state governments should have the primary role in the regulation of the industry--shapes the debate regarding the Program. The result is a disagreement which is as basic as the goals which the Program strives to achieve.

I begin my analysis of the Program by addressing what the goals of the Program are said to be, what they are, and what they should be. Next, I focus on a particular area of contention in the debate regarding the Program--namely, sanctions. I, then, present more generally the various objections to the Program. These come from two--consistent with the fundamental discord--primary groups. They are (a) state level officials and those advocating the importance of state controlled regulation and (b) federal level officials and those advocating the importance of nationally controlled regulation. I follow this with a brief discussion of the reactions of the

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NAIC, in the form of its recent actions on the Program, to the criticism of these groups. Finally, I conclude my analysis of the Program by considering the particular situations of several states—primarily New York, Texas, and Vermont—as they inform the debate regarding the Program as a whole.

With the particulars of the debate regarding the Program thus presented, I continue by addressing the theoretical legal issues which underlie the Program. I first argue the advantages of a state regulatory system. I follow this with a rebuttal to the "Race to the Bottom" theory regarding state regulation.

At the conclusion of this piece, I endorse the Program and a number of changes in it. The first four suggestions, which are initially discussed at various points earlier in the paper, are closely related to, and derived from, the suggestions of various individuals and groups. These are followed by two original ideas—styled the "presumption method" and the "independent auditor review" concept.

§2 Regulation of Insurance in America

The regulation of the insurance industry is unique among financial intermediary regulation in America. Its distinctive feature is that the industry is regulated, almost entirely, at the state, not the federal, level. State regulation can be traced back to the case of Paul v Virginia2 where the U.S. Supreme Court held that insurance contracts are not "interstate

[2] 75 U.S. (8 Wall) 168 (1868)
commerce" for the purposes of the Constitution.\textsuperscript{1}

The National Association of Insurance Commissioners (NAIC) has played an invaluable role in the success of state regulation of the insurance industry. The NAIC began as a private trade organization attempting to coordinate regulatory efforts among the states.\textsuperscript{4} Its most significant achievements, prior to 1990\textsuperscript{5}, were the development of uniform blanks for the annual statements submitted to the various insurance departments and the development of relatively uniform methods of valuing assets and liabilities by insurance companies. These two accomplishments kept the state regulatory system from collapse.\textsuperscript{6} The role of the NAIC changed significantly beginning in 1990, and it has very recently changed its self-characterization to that of a "public entity."\textsuperscript{7}

The primacy of states in the regulation of the insurance industry was disrupted for a brief moment by the U.S. Supreme Court decision in United States v South-Eastern Underwriters Association\textsuperscript{8}, which held that for the purposes of the federal antitrust laws, insurance company practices are within the "interstate commerce" powers of the federal government. The insurance

\footnotesize{\textsuperscript{3}H. Jackson, Harvard Law School, Regulation of Financial Institutions, Course Materials at 304 (Fall 1994).  
\textsuperscript{5}In June of 1990 the Accreditation Program was begun by the NAIC.  
\textsuperscript{8}322 U.S. 533 (1944).}
industry reaction, championed by the NAIC, was swift and immediately effective. The NAIC quickly presented a bill to the Congress which, in substance, became the McCarran-Ferguson Act. The Act essentially nullified the South-Eastern Underwriters Association decision by exempting the insurance industry from the federal antitrust laws to the extent that regulation was accomplished by state law. This returned the states to their historical role as the sole regulators of insurance. It also brought to a head, the question which continues to shape insurance industry regulation: are the states or the federal government in a superior position to effectively and efficiently regulate the insurance industry? The direct result of this debate is the NAIC’s Financial Regulation Standards and Accreditation Program.

§3 Analysis of NAIC Accreditation Program

§3.1 What is the NAIC Accreditation Program?

In 1988, the National Association of Insurance Commissioners (NAIC) began developing Financial Regulation Standards (Standards) for the insurance industry. By June of 1989 these Standards had been formally adopted. A year later, the NAIC, using these Standards as the

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915 U.S.C. §1011


11Id.


13Id.
basis for its Accreditation Program (Program), certified the insurance department of New York. The NAIC Accreditation Program had begun. Currently, 48 states and the District of Columbia are accredited by the Program.

The Program certifies insurance departments based on three criteria. These criteria are styled "Laws and Regulations," "Regulatory Practices and Procedures," and "Organizational

12Id.


13To satisfy the "Laws and Regulations" portion of the accreditation program the jurisdiction must have laws and regulations "substantially similar" to model laws and regulations promulgated by the NAIC covering (a) Examination Authority: the insurance department must have authority to examine insurance companies when deemed necessary, (b) Capital and Surplus Requirement: the jurisdiction must require maintenance of capital by insurers in accord with the Risk Based Capital for Insurers Model Act by January 1, 1997, (c) NAIC Accounting Practices and Procedures: the jurisdiction must require companies to follow the NAIC Accounting Practices and Procedures and to file the appropriate NAIC annual statement blank, (d) Corrective Action: the jurisdiction must have the authority to take necessary action to prevent a company from entering a hazardous financial condition, (e) Valuation of Investments: the department must require companies to value investments according to the methods prescribed by the NAIC, (f) Holding Company Systems: the jurisdiction must have adopted the Model Holding Company Systems Act and its regulations, (g) Risk Limitation: the jurisdiction must set the maximum amount of risk to be retained by a property and liability company based on its capital and surplus--this must not exceed 10% of the capital and surplus, (h) Investment Regulations: jurisdictions must require that insurers meet certain requirements for diversity and liquidity in their investments, (i) Admitted Assets: the jurisdiction must identify assets permitted in the statutory financial statements of a company, (j) Liabilities and Reserves: the jurisdiction must prescribe minimum standards for liabilities and reserves of a company; the Standard Valuation Law must be adopted by July 1, 1996 and the Actuarial Opinion and Memorandum regulations must be adopted by January 1, 1997, (k) Reinsurance Ceded: the jurisdiction must have in place the Model Law on Credit for Reinsurance and regulation; the jurisdiction must adopt the 1992 Life and Health Reinsurance Agreements Model Regulation by July 1, 1996, (l) CPA Audits: the jurisdiction must require annual audits of insurers; the 1990 version of the Model Rule Requiring Annual Audited Financial Reports must be adopted by July 1, 1996, (m) Actuarial
Opinion: the jurisdiction must require an opinion on reserves and loss and loss adjustment expense. (n) Receivership: the jurisdiction must have a receivership scheme in place. (o) Guaranty Funds: the jurisdiction must provide for payment to policyholders on the insolvency of a company. §§3A and 5H of the Life and Health Insurance Guaranty Association Model Act must be adopted by July 1, 1996. (p) Participation in IRIS: the jurisdiction must require companies to participate in the NAIC Insurance Regulatory Information System (IRIS). (q) Risk Retention and Purchasing Groups: the jurisdiction must have in place the Model Risk Retention Act. (r) Producer Controlled Property/Casualty Insurers: the jurisdiction must have in place the Model Law for Business Transacted with Producer Controlled Property/Casualty Insurer Act. (s) Managing General Agents: the jurisdiction must have in place either the 1990 or 1993 Managing General Agents Act. (t) Reinsurance Intermediaries: the jurisdiction must have in place either the 1990 or 1993 Reinsurance Intermediaries Act. (u) Diskette Filings: the jurisdiction must require diskette filings for insurers (those operating only in their state of domicile may be exempted) by July 1, 1996. (v) Disclosure of Material Transactions: the jurisdiction must adopt the Disclosure of Material Transactions Model Act by July 1, 1996. NAIC, FINANCIAL REGULATION STANDARDS AND ACCREDITATION PROGRAM 6-11 (1995). All noted effective dates have been changed to July 1, 1997. NAIC Falls $1 Million Behind on Fees, THE INS. REGULATOR, Apr. 1, 1996, at 1 (1996 WL 5554456).

17To comply with the "Regulatory Practices and Procedures" portion of the Program, the insurance department must have the ability to perform the following functions: (a) Financial Analysis: the department must have sufficient staff and communication; the department must have a prioritizing scheme in place to deal with the most immediate problems, (b) Financial Examinations: the department must have sufficient budget, qualified staff; sufficient supervision; the department must follow procedures similar to those contained in the NAIC's Examiners Handbook; the department must have a prioritizing scheme to deal with the most immediate problems, NAIC Troubled Insurance Company Handbook: the department should follow the procedures in this book, (d) Communication with States: the department must have provisions for sharing confidential information concerning insurers with other jurisdictions by July 1, 1996, (e) Reporting of Regulatory Actions: the department must participate in the Regulatory Information Retrieval System (RIRS), the Special Activities Database (SAD), and the Complaints Database Systems (CDS) by July 1, 1996. NAIC, FINANCIAL REGULATION STANDARDS AND ACCREDITATION PROGRAM 11-14 (1995). All noted effective dates have been changed to July 1, 1997. NAIC Falls $1 Million Behind on Fees, THE INS. REGULATOR, Apr. 1, 1996, at 1 (1996 WL 5554456).

18To comply with the "Organizational and Personnel Practices" criteria the insurance department should have the following systems in place: (a) Professional Development: the department should provide for continuing education of its staff, (b) Organization: an individual shall have responsibility for all financial regulation and surveillance activities and shall report to the Commissioner or a designee, Evaluation of Staff: the department should periodically
complete an Initial Accreditation Review consisting of eighteen individual steps. A department requests review and files a self-evaluation with the NAIC. The Financial Regulation Standards and Accreditation Subcommittee (FRSAS) forms a Review Team which makes an on-site visit of three to five days. The on-site review consists of interviews with department personnel, review of laws and regulations, review of the department for its regulatory practices and procedures, review of the department for its organizational and personnel practices, inspection of files on selected companies, and a discussion of findings with the jurisdiction. The FRSAS considers all information obtained and makes a decision. If a jurisdiction does not meet the requirements for accreditation it may (a) withdraw its request, (b) request that the FRSAS delay a final decision pending corrective action, or (c) request that the FRSAS reconsider. If reconsideration is requested the FRSAS hears the jurisdiction's appeal.

evaluate the activities of its staff, (d) Minimum Educational and Experience Requirements: the department should have minimum requirements suited for each position, (e) Pay Structure: the department should have a competitively based pay structure, (f) Funding: the department's funding must be sufficient to meet its needs. NAIC, FINANCIAL REGULATION STANDARDS AND ACCREDITATION PROGRAM 14-15 (1995).

19 Id. at 2-5.
20 Id.
21 Id.
22 Id.
23 Id.
24 Id.
25 Id.
An accredited state receives its accreditation at the next NAIC national meeting. A jurisdiction which receives an unfavorable final decision receives a report stating reasons for the decision. Each year an accredited department must conduct a self-examination and submit a report of the findings to the NAIC. Also, each fifth anniversary of a department's accreditation is occasion for a successive round of review similar to the Initial Accreditation Review. If at any time the FRSAS believes a special review is necessary, it may conduct one. If, at any review, the department has fallen below the requirements for accreditation, its accreditation is suspended.

§3.2 The Goals of the Accreditation Program

According to James W. Schacht, a principal draftsman of the Program, the goal of the Program in 1988 was to provide state insurance departments with guidelines to create an effective financial surveillance regulation system that would ensure the safety and soundness of U.S. insurers doing multi-state business. Less than four years after the initiation of the

26 ld.
27 ld.
28 ld. at 5-6.
29 ld.
30 ld.
31 ld.
32 Former Acting Commissioner of Illinois

program, many—including Mr. Schacht—were calling for the NAIC to return to the original purpose of the Program.\textsuperscript{34} It is my position that this original statement of intent for the Program is an accurate statement of the appropriate goal for the Program. The Program has achieved this goal. The Program has also attempted to act in a number of ways which are not loyal to this goal. I will first consider the alternative (improper) goals some have claimed the program has pursued—or should pursue. I will then consider the alternative goals the program has not—and should not—pursue. Finally, I will return to the original goal and demonstrate that the Program has succeeded in this goal.

\textbf{§3.2.1 Strict Uniformity}

The United States General Accounting Office (GAO) has maintained from the beginnings of the Program that its principal goal is and should be national uniformity in regulation.\textsuperscript{35} It has also maintained (correctly) that the NAIC does not have the power to enforce a uniform national standard.\textsuperscript{36} Representative John Dingell (D-Mich) has joined in the belief that a proper goal for insurance regulation is a uniform national standard.\textsuperscript{37} He, too, has

\textsuperscript{34}Id.


\textsuperscript{36}Id.

correctly identified that the Program is not the appropriate vehicle for this effort.\(^{38}\) He has, then, used the inability of the Program to achieve his desired uniformity as a basis for contending that state regulation is unable to be successful.\(^{39}\) Representative Dingell has been the most vocal in advocating a national based regulation of the insurance industry.\(^{40}\) The role of Representative Dingell in the debate has, however, all but disappeared with the dramatic shift in the make-up of the Congress in November 1994.\(^{41}\)

Considering uniformity to be the goal of the Program ignores the advantageous and distinguishing feature of insurance regulation—that it is state, not nationally, based. It is, indeed, cause for worry when the NAIC acts in a manner which causes it to be a de facto national regulator.\(^{42}\)

The advantage in state regulation of insurance is that it allows room for each jurisdiction to tailor its regulatory scheme to the unique situation of the companies doing business in its

\(^{38}\)See id.

\(^{39}\)See id.


state. It allows for experimentation in methods of regulating. This will allow regulation to continuously become more effective and efficient through measured, careful change. It will not be necessary to wait for a major incident (i.e. the Savings & Loan crisis in that industry) to implement change to better the regulation of the insurance industry.

Numerous state regulators, and even the NAIC accreditation subcommittee, have recognized that strict uniformity is not an appropriate goal for the Program. The most important realization here is that strict uniformity in regulation places form over substance. Strict uniformity becomes nothing more than a formal reaction to the threat of federal regulation. It avoids it—but at the expense of everything which is desired by state regulation (see the paragraph immediately supra). This issue becomes obvious in the debate over the "sanctions" in the Program.


46The so called "results oriented" working group of the NAIC has suggested a more flexible approach to the model laws. Rather than "substantially similar" language being required, compliance with model laws would be judged by the achieving of results desired to be gained from each model law. This working group has also suggested reducing the Laws and Regulations standards (see note 16, supra) to 13. The recommendations of the "results oriented" working group have been unanimously accepted by the accreditation subcommittee. Some believe this should help pave the road to the reaccreditation of New York. L. H. Otis, NAIC Eases Deadlines On Accreditation Program, NAT'L. UNDERWRITER--LIFE & HEALTH, Sept. 18, 1995, at 3 (1995 WL 9129834); see §3.7 Situations of Several States, infra.

Strict uniformity should be a goal in only two circumstances. First, if there is consensus that the best method is known, it should be implemented in all jurisdictions according to strict uniformity. I assert that it cannot be said about any regulatory structure—in the United States or elsewhere—that there is a consensus within a nation that the best method for insurance solvency is known. This means that strict uniformity should be avoided. It is desirable to have 55\(^49\) different jurisdictions with the ability to adopt 55 different methods of insurance solvency so that we may continue to strive for the very best method. Second, if significant efficiency may be obtained for either the companies regulated or the customers of those companies by virtue of strict uniformity in regulation, it should be implemented. Several aspects of the insurance industry could gain by uniform regulation. Most obvious are gains to insurers—and through lower price, to insureds—from uniform policy blanks, standards for admission to do business in the state, etc. The sorts of items which yield efficient results for insurers—and through lower price, to insureds—do not implicate strict uniformity in solvency regulation. In fact, the advantage of the 'accreditation' provided by the Program is that proof of solvency in one state will act as proof of solvency in all jurisdictions—thus, eliminating the need for the solvency regulation to be uniform in all jurisdictions\(^50\).

\(^{48}\)See §3.3 Sanctions, infra.

\(^{49}\)The number of relevant jurisdictions in the United States—the states, the District of Columbia, and the territories

\(^{50}\)See §4.1 The Advantage of State Regulation, infra.
§3.2.2 Holding Off Federal Regulation

To a significant degree, the path which the Program has taken has been shaped by the desire to hold off federal regulation of the insurance industry. The Program, itself, was much a response to the threat of federal regulation.51 The same players52 are at issue here as in the strict uniformity goal. The evaluations of the Program by the GAO53 spurred the NAIC to take the Program in the direction of strict uniformity, supra, and sanction oriented enforcement54. The criticism of the Program by Representative Dingell centers on the lack of enforcement authority of the Program.55 This caused the Program to emphasize sanctions.56 Commentators agree, the states have supported the Program to stave off federal regulation.57

Virtually from the beginning of the Program, there were objections from the states regarding the NAIC’s reaction to the threat of federal regulation. As early as 1991, state legislators were attacking portions of the program (strict uniformity and sanction-oriented


52The GAO and Representative Dingell


54See §3.3 Sanctions, infra.


enforcement) which were a direct response of the NAIC to the threat of federal regulation.\textsuperscript{58} The National Conference of Insurance Legislators (NCOIL) began voicing objections to the perceived strict uniformity goal of the Program at least as early as 1992.\textsuperscript{59} The NAIC has denied that strict uniformity was or is a goal of the Program.\textsuperscript{60}

Some have claimed that the idea of an overt "threat" of federal regulation would be a positive step in successful insurance solvency regulation by the states.\textsuperscript{61} Others have voiced a like for dual regulation, as in banking.\textsuperscript{62} It is my position that the results of attempting to fend off federal regulation (strict uniformity and sanction-oriented enforcement) are destructive to the success of the Program and to successful, effective, and efficient insurance regulation. The controversy regarding the Program from about 1994 thru 1995 has centered on these methods of achieving this goal.\textsuperscript{63} Significantly since late 1994, when the make-up of Congress changed, the


\textsuperscript{60}Id.

\textsuperscript{61}Lisa S. Howard, Yet Another Option For National Solvency Standards, NAT'L. UNDERWRITER--PROP. & CASUALTY, Aug. 12, 1991, at 32 (1991 WL 2889342) (This is an extension of, and based on, the relationship between Congress and the states in the Medicare supplement area. When Congress changes the Medicare law, the NAIC must formulate—and the states must pass—a related model law. If the states do not pass appropriate legislation, the federal government preempts.)


\textsuperscript{63}See §3.4 The NCOIL Objections to the Program and §3.5 The GAO Objections to the Program, infra.
threat of federal regulation has been small.\textsuperscript{64} This provided an opportunity for an onslaught of criticism of the overreaching of the Program. It is at this point that the state legislators became very active in their effort to recapture state regulation for the states.\textsuperscript{65}

\section*{\S 3.2.3 Fraud}

There has been no significant suggestion that the Program should police fraud on a nationwide scale. This seems quite appropriate to me. The NAIC and the Program should make every effort to cooperate with criminal enforcement authorities to combat insurance fraud. However, the combating of fraud should not be a goal of the Program. There are already mechanisms in place in each of the jurisdictions to combat fraud, including insurance fraud. There also exist sufficient statutes\textsuperscript{66} at the federal level to combat such fraud. The Program has nothing significant to add to these schemes. In fact, the NAIC has on several occasions indicated that it believes a comprehensive federal solution to insurance fraud is appropriate.\textsuperscript{67}

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\textsuperscript{66}ie. mail fraud, RICO, etc.
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The National Governor's Association concurs with this stance. The National Conference of State Legislators also agrees. Some have suggested that an interstate compact regarding insurance fraud is the correct method of dealing with this issue. I express no opinion on the appropriate way of dealing with insurance fraud other than to say that it is not an appropriate part of the Program at this time.

§3.2.4 Rate Regulation

Although some have suggested that the Program is an appropriate vehicle for rate regulation, such ideas have not received serious attention. Views on the propriety of rate regulation itself differ among jurisdictions and scholars. The idea of combining rate and solvency regulation is generally regarded as not a good one. The only interest states might have in the regulation of rates set by other states is the improper one of protecting their domestic insurers from price competition. Rate regulation has no place in the Program.

§3.2.5 The Original Goal

The NAIC Accreditation Program has been an overwhelming success. The Program has

68 Id.


caused every jurisdiction\textsuperscript{72} to enact insurance regulatory legislation\textsuperscript{73,74}. The Program was a significant force, probably the sole force, in maintaining--and even increasing--state insurance regulatory budgets\textsuperscript{75},\textsuperscript{76} in a period of severe cuts in virtually all areas of governmental spending.\textsuperscript{76} Each of the states have made a significant effort to be accredited.\textsuperscript{77} The Program allows for significant tailoring to meet unique situations of individual states. Maryland and Tennessee are examples.\textsuperscript{78} The GAO has acknowledged that the Program has "been a catalyst encouraging state insurance departments to regulate better."\textsuperscript{79} The District of Columbia and all but 2 states

\textsuperscript{72}The NAIC includes the 50 states, District of Columbia, and 4 territories.

\textsuperscript{73}In 1991, over 450 bills were enacted and 57 regulations were developed. In 1992 the numbers were almost as high and in 1993 the numbers remained significant. Lenore S. Marema, \textit{NAIC Must Slow Down and Assess Standards}, \textit{BEST'S REV.--PROP.-%CASUALTY}, June 1, 1994, at 72 (1994 WL 2861238).


\textsuperscript{75}The total budget for insurance regulation in all jurisdictions has been steadily increasing since the beginning of the Program. The budget in 1991 was $503.5 mm. The budget in 1992 was $518.3 mm. The budget in 1993 was $549.8 mm. Cynthia Crosson, \textit{NAIC Plans Major Drive For Accreditation of States}, \textit{NAT'L. UNDERWRITER--PROP. & CASUALTY}, Jan. 11, 1993, at 3 (1993 WL 3030396).


have been accredited to date.\textsuperscript{80} These remaining states are very near accreditation.\textsuperscript{81}

Although there will always be some problems, the insurance industry has continuously been successfully regulated. Most importantly, there has been no insurance company failures which could not be handled by the system. There is no indication that anything on the scale of the Savings & Loan and banking scandal could happen to the insurance industry. The very nature of the insurance solvency mechanism protects against this type of catastrophe\textsuperscript{82}.

\textbf{§3.3 Sanctions}

From the beginning of the Program, there has been significant support for sanctions to be imposed on non-accredited jurisdictions. Commentators have suggested various forms of sanctions which might have been associated with the Program\textsuperscript{83}. The NAIC finally adopted a set of sanctions to be imposed on non-accredited states as of January 1, 1994. The sanctions took

\textsuperscript{80}See note 15, supra.

\textsuperscript{81}Telephone Interview with Mark G. Noller, NAIC Senior Accreditation Manager (Feb. 2. 1996).

\textsuperscript{82}See \textit{§4.1 The Advantage of State Regulation}, infra.

\textsuperscript{83}Sam Friedman advocated some form of sanction. Sam Friedman, \textit{Time for Solvency Oversight Standards}, NAT'L. UNDERWRITER--PROP. & CASUALTY, June 12, 1989, at 22 (1989 WL 2495939). His suggestion was that states failing to meet the accreditation standards be placed on a "watch list" and given a limited time to come into compliance. \textit{id.} Failure to comply would result in notification to policyholders (through the mass media) or expulsion from the NAIC. \textit{id.} Another idea for sanction was to require an interstate insurer domiciled in a non-accredited jurisdiction to comply with the laws of an accredited state. Lisa S. Howard, \textit{NAIC Holds Off Putting Teeth in Financial Standards Program}, NAT'L. UNDERWRITER--LIFE & HEALTH, June 17, 1991, at 6 (1991 WL 2879220). This was not accepted. Schacht, acting director for Illinois, endorsed sanctions in his initial plans for the Program. \textit{Illinois Official Urges Accreditation Reform}, THE INS. ACCT., Oct. 3, 1994, at 3 (1994 WL 11229354).
the following form: examinations performed by a non-accredited state would not be accepted by regulatory authorities in an accredited state. There was, however, an alternative route built into the system. This involved an examination of a company in a non-accredited state participating with an examiner from an accredited state in the examination of the company. The practical reality of examinations was that they often involved regulators from several states. This, some contended, created a complete loophole in the sanctions.\textsuperscript{84} Accredited states would be allowed to accept such an examination. The NAIC responded to this sort of criticism by declaring that the sanctions were meant only to be a "hassle" to non-accredited states.\textsuperscript{85}

Despite the claims by some that the sanctions were completely illusory, a significant discussion arose concerning the propriety of sanctions. From the beginning of the Program, the GAO maintained that the NAIC had no authority to enforce any part of its Program\textsuperscript{86}. This became the rallying call for those who desired federal regulation of insurance. Arguments from the individual states became pronounced in late 1993, as the implementation of the sanctions was drawing near. Among the most vocal was New York\textsuperscript{87}, which had, by this time, become the sole jurisdiction to lose its accreditation. Unaccredited states initially tried to find methods of avoiding the impact of the sanctions by exploiting the "loophole", \textit{supra}, or by beginning

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\item \textsuperscript{86}See \textsuperscript{3.5} \textit{The GAO Objections to the Program}, infra.
\item \textsuperscript{87}See \textsuperscript{3.7} \textit{The Situations of Several States}, infra.
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numerous examinations in late 1993.\textsuperscript{88} As the first of the year passed, and the sanctions officially came into effect, unaccredited states began to fight the sanctions more vigorously. By mid 1994, Texas, Alaska and New York all had passed retaliatory legislation\textsuperscript{89} directed at the sanctions.\textsuperscript{90} Based on a combination of the use of the "loophole" by unaccredited states and the threat posed by the legislation, the retaliatory legislation was not utilized in any public manner.\textsuperscript{91}

Through 1994 and to the present, a number of states (accredited and unaccredited) have joined the GAO in its contention that the sanctions are not constitutionally permissible. The states, however, had a very different goal in making these claims. The states desired to prevent the NAIC from becoming a national legislator on insurance regulation.\textsuperscript{92} They posed these objections, \textit{inter alia}, in the form of antitrust arguments.\textsuperscript{93} NCOIL joined in these criticisms\textsuperscript{94}.

Several regulators, including Mr. Schacht, of Illinois, argued during 1994 that the


\textsuperscript{89}These laws essentially provide that any jurisdiction not accepting the legislating state's examinations of its domiciled insurers would not have their examinations of their domiciled insurers accepted by the legislating state.


\textsuperscript{91}Lenore S. Marema, \textit{NAIC Must Slow Down and Assess Standards}, BEST'S REV.--PROP.--CASUALTY, June 1, 1994, at 72 (1994 WL 2861238).


\textsuperscript{94}See \textsection 3.4 The NCOIL Objections to the Program, infra.
sanctions were premature and unwise. According to a staff member at the NAIC, the laws providing for sanctions were dropped as a requirement to accreditation at the end of 1994. A few states, including Illinois, acted swiftly to change their laws to reflect this new development. The majority of states, however, have not taken any action on eliminating the sanctions from their laws. Recent action and comment by several persons and groups has been somewhat puzzling. Throughout 1995, and even into 1996, New York's State Senator Guy Velella, the National Association of Independent Insurers (NAII), NCOIL, and the National Risk Retention Association (NRRA) continued to blast the NAIC about the sanctions in the Program. This criticism would appear to be misplaced.

I do not contend that the imposition of sanctions is impermissible, but I do maintain that


96Telephone Interview with Mark G. Noller, NAIC Senior Accreditation Manager (Feb. 2, 1996).

971995 Ill. Legis. Serv. 89-97, §10 (IL Legis 89-97).

98There has, however, been no public acknowledgment or accusation of the use of sanctions by these states.


they are unnecessary. First, without the threat or use of sanctions, each jurisdiction will want to be accredited. It is in the self interest of each jurisdiction to attain accreditation. Insurers domiciled in the jurisdiction considering the need for accreditation would desire and lobby for accreditation. Insurers have lower transaction costs when their state of domicile is accredited by the Program. Other jurisdictions in which the insurer wishes to do business will not impose additional cost on the insurer in the form of duplicative solvency regulation. These lower costs to the insurer lead to lower prices for the insureds. The insureds who are citizens of the jurisdiction considering the need for accreditation would then desire and push for accreditation of the jurisdiction's department of insurance. Second, for the sake of lower prices for the jurisdiction's insureds, each jurisdiction will desire that the Program have full participation from companies wishing to do business in the subject jurisdiction. Just as lower solvency regulation costs help insurers domiciled in the subject jurisdiction to keep prices down, lower solvency regulation costs help foreign domiciled insurers keep prices down for the insureds in the subject jurisdiction. Sanctions, then, should be repealed from the laws and regulations of each jurisdiction which adopted them in the belief that they would be required for their continued accreditation\textsuperscript{103}.

\textit{§3.4 The NCOIL Objections to the Program}

The National Conference of Insurance Legislators (NCOIL) is a voluntary association of

\textsuperscript{103}See \textit{§4.1 The Advantage of State Regulation} and \textit{§4.2 The Race to Efficient Regulation}, infra.
insurance legislators representing 33 jurisdictions. Although it obviously represents only a portion of the relevant actors and participation in the Conference is minimal, it has been by far the most vocal of the groups criticizing the Program in recent years. The objections of NCOIL serve as a helpful representation of the arguments of all those who advocate the importance of state controlled regulation of the industry. The NCOIL criticism culminated in a March 25, 1995 release of its Report on the NAIC Accreditation Process (NCOIL Report).

The NCOIL Report evidences how the support for the Program has dwindled among state lawmakers and lists five key factors influencing this loss of support. The key factors identified in the NCOIL Report are (a) the large number of "must pass" model bills, (b) the requirement that each state adopt specific bills designed to address problems that did not exist in

104 Commentators indicate that when considering NCOIL positions, it must be remembered that nearly half the jurisdictions do not choose to participate in NCOIL. It can be said that NCOIL does not fairly represent a majority of insurance legislator thinking. Mark L. Schussel, Legislators to Ponder Legality of NAIC Program, BEST'S REV.--PROP.-CASUALTY, Sept. 1, 1994, at 10 (1994 WL 2861348). Some Commissioners have suggested that the NAIC should work with the National Conference of State Legislators (NCSL) instead of NCOIL. L. H. Otis, Acrimony Between NAIC, NCOIL Is On the Rise, NAT'L. UNDERWRITER--LIFE & HEALTH, Apr. 17, 1995, at 46 (1995 WL 8437087).

105 When the NAIC provided for joint meetings of the NAIC and NCOIL (in response to NCOIL requests for input in NAIC action), representatives of NCOIL were rarely, if ever, in attendance. Time for NCOIL to Step Up to the Plate, NAT'L. UNDERWRITER--PROP. & CASUALTY, Apr. 10, 1995, at 20 (1995 WL 8435094).


some states, (c) NAIC insistence of verbatim language and/or substantial compliance with the structures of the model laws, (d) confusion about what "substantial compliance" means, and (e) a shift in emphasis "from national minimums to national optimums." The NCOIL Report charges that the Program encroaches on state sovereignty, may be violative of antitrust laws, and is not administered in an "even-handed" fashion. Clare Farragher, chair of the NCOIL Special Solvency Accreditation Committee and a Republican member of the New Jersey Assembly, stated "the NAIC has moved beyond its role as an advisory organization and its objective of recommending minimum standards to a national agency for insurance regulation without legal authority." She goes so far as to say that the insurance industry could get along without the NAIC, if necessary.

Partially in response to its own NCOIL Report and the objections provided by others, NCOIL has suggested (a) the formation of a "legislative participation board" within the NAIC.

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108 Id.

109 Id.


110 Id.


113 L. H. Otis, NAIC Reforms Seen as "Step in Right Direction", NAT'L UNDERWRITER--LIFE & HEALTH, June 26, 1995, at 5 (1995 WL 9129537). This would essentially provide mandatory direct involvement of state legislators in the formulation of model laws. I believe this to be unnecessary. Legislator involvement in the form of solicited comments and a requirement that a certain number of states pass each model law prior to making it necessary for
(b) each state enact NAIC oversight legislation, (c) requiring a significant number of states to adopt a model law before the Program requires it for accreditation, (d) removal of the sanctions from the Program, (e) a change to fundamental regulatory tools and performance evaluation rather than strict model law adherence, and (f) abandonment of the Program in favor of regulation by interstate compact.

The NCOIL Report's five key factors are (for the most part) examples of valid and accreditation will provide for significant—and sufficient—legislator involvement and control. It will also avoid giving undue weight to the particular legislators serving on the board. See §5.1 New Standards, infra.


118Meg Fletcher, NCOIL Head Hopes to Form Agreement On Regulation, BUS. INS., Apr. 4, 1994 (1994 WL 3834344). Interstate compacts do have their place in regulation of the insurance industry—see §5.4 Interstate Compacts, infra. Interstate compacts, however, should not be used for solvency regulation. They should be used only for ministerial types of activities (i.e., ones where the advantages from innovation achieved by flexibility in a multi state approach are not so important).
constructive criticism of the Program. The first factor, that there have been too many new model laws too fast, is echoed by a number of interested parties. In response to the early developments, some states have taken action by delaying the adoption of new laws, while others have proposed changes to existing laws. For example, in 1994, the Texas Department of Insurance announced that it would delay the implementation of new laws until more data were available. This was in response to concerns raised by the Texas Insurance Commissioner, who stated that the new laws were too complex and would be difficult to implement.

Insurers have also responded to criticisms of the new laws. Many have argued that the new laws are too complex and difficult to understand, and that they will increase the costs of insurance for consumers. In response to these concerns, some insurers have proposed changes to the new laws, including simplifying the language and providing clearer explanations of the new requirements. For example, a number of insurers have proposed that the new laws be simplified to make them more understandable to consumers.

Despite these challenges, there is a general consensus that the new laws are necessary to address the increasing costs of insurance and to ensure that the industry remains financially stable. Many experts agree that the new laws provide a framework for the industry to address these challenges, and that they will ultimately benefit consumers by providing them with more choices and better protection.

119 Commentators have argued that more time is needed for the states to pass the model laws. The Sanctioned 16, BEST'S REV.--PROP.--CASUALTY, June 1, 1994, at 33 (1994 WL 2861246); Lenore S. Marema, NAIC Must Slow Down and Assess Standards, BEST'S REV.--PROP.--CASUALTY, June 1, 1994, at 72 (1994 WL 2861238); L. H. Otis, P-CRBC Model Not Included in Accreditation Standards, NAT'L. UNDERWRITER--LIFE & HEALTH, Dec. 13, 1993, at 8 (1993 WL 3023311). New York has been at the lead in complaining about constantly needing to change laws to come in line with the current "model laws". Legislators & Regulators Take Criticism of NAIC to Insurers, FED. & STATE INS. WK., Apr. 3, 1995 (1995 WL 8596014).

Insurers have called for testing of "model laws" before requiring them for accreditation. NAIC Accredits Two More States, Moves on Risk-Based Capital, FED. & STATE INS. WK., June 27, 1994 (1994 WL 2536479). The American Council of Life Insurers (ACL) compiled information demonstrating that the states were not in a good position for retaining their accreditation on January 1, 1996 based on the number of new model laws not passed as of August, 1995, though, they did not advocate anything in this demonstration. L. H. Otis, As Deaccreditations Loom, Some Push "Standstill", NAT'L. UNDERWRITER--LIFE & HEALTH, Aug. 21, 1995, at 10 (1995 WL 912745). In the past, the ACL has argued that too many new standards are being promulgated. Stephen Piontek, Bertrand Attacks "Overkill" on Regs., NAT'L. UNDERWRITER--LIFE & HEALTH, Nov. 22, 1993, at 2 (1993 WL 3023381). Commissioners from California, Illinois, New York, and Texas have suggested that the addition of model laws should be slower. L. H. Otis, New Commissioners Call for a Shake-up at NAIC, NAT'L. UNDERWRITER--LIFE & HEALTH, Mar. 27, 1995, at 6 (1995 WL 8436995). They suggested a four year waiting period and the adoption by 25 states before requiring a model law for accreditation. Id. Texas contends that requiring new model laws to be passed within two years is not enough time because their legislature only meets once every two years. L. H. Otis, States Battling NAIC Over Accreditation Process, NAT'L. UNDERWRITER--LIFE & HEALTH, Nov. 28, 1994, at 22 (1994 WL 8708276). Commentators contend that it takes an average of 3 years to pass any legislation. Id. New York suggested a review for model law compliance only once every five years. Id. Commissioner Walsh has argued that the Program is now in its mature phase and not so many new model laws need be introduced. L. H. Otis, Legislators Clash with NAIC Officials, NAT'L. UNDERWRITER--LIFE & HEALTH, Apr. 18, 1994, at 1 (1994 WL 2866068). Schacht of Illinois, the Northeast zone, and the Delaware commissioner have all suggested that too many new model laws are being created too fast. L. H. Otis, NAIC Changes, Reexamines Accreditation Program, NAT'L UNDERWRITER--PROP. & CASUALTY, June 12, 1995, at 3 (1995 WL 8435435). The Alliance of American Insurers (AAI) suggested standards for developing model laws for the Program be developed. Colleen Mulcahy, Cracks Seen in NAIC "Wall" of Authority, NAT'L. UNDERWRITER--PROP. & CASUALTY, Mar. 27, 1995, at 1 (1995 WL 8435021). The AAI also called for a moratorium on new model laws. Robert G. Knowles, "Jurassic Park" Dangers Loom, Insurers Warned, NAT'L. UNDERWRITER--PROP. & CASUALTY, May 30, 1994, at 3 (1994 WL 2866897). Schacht called for a 3 year waiting period on new model laws unless 75% of the committee agrees to waive the
criticism, the NAIC stated that by continually raising the "bar over which states must jump to achieve [accreditation], regulators are significantly elevating the level of protection consumers can expect from their state insurance departments."120 This was most likely still true in mid-1993, but (as many have indicated) the Program is now in a mature phase. There are enough accreditation standards in place to effectively regulate solvency (this is not to say that the Program has already achieved the best possible regulatory standards). A number of groups, including the NAIC "results oriented" working group, and individuals have even called for the number of requirements for accreditation to be reduced.121 Further, experience has shown that two years is not enough time for a legislature to pass an ordinary bill. Now that the Program has reached a mature phase, it is no longer advisable or realistic to attempt to treat all accreditation legislation on an emergency basis. The NAIC has recognized as much by delaying the date by which all of the pending model laws must be passed.122,123 The NAIC has also recognized this waiting period. L. H. Otis, NAIC Defers Accreditation-Standards Slowdown, NAT'L UNDERWRITER--PROP. & CASUALTY, Dec. 27, 1993, at 17 (1993 WL 3029197).

120California and Rhode Island Added to NAIC-Accredited States, FED. & STATE INS. Wk., June 28, 1993 (1993 WL 2771817) (comment of Steven Foster, then president of the NAIC).


122The date for nine standards was changed from January 1, 1996 to July 1, 1996. More recently, the effective dates of all new standards was changed to July 1, 1997. NAIC Falls $1 Million Behind on Fees, THE INS. REGULATOR, Apr. 1, 1996, at 1 (1996 WL 5554456). See notes 16 and 17, supra, for information on the standards.

realty by implementing standards for the creation of new model laws in September of 1995. 124

The new policy states that any addition or change to the accreditation standards must be presented with written evidence of the following: (a) a statement and explanation of how the standard suggested is directly related to solvency regulation and why it should be included in the Program, (b) a statement explaining why the standard suggested should be enacted by every jurisdiction, (c) a statement of how many jurisdictions have a similar law and how it has worked to date, (d) any language which must be enacted "exactly or substantially similar" to the model and why the strict uniformity is necessary, (e) an estimate of the cost for insurer compliance and impact on the insurance department, and (f) the potential impact on consumers if the suggested standard is not implemented. 125 These actions are a definite step in the right direction. 126

The second factor, that each state has been required to adopt specific bills designed to address problems that did not exist in all states, relates to a debate that has been in existence since the beginning of the Program. This is the debate about the goal of strict uniformity. 127

The third factor, that the NAIC has required verbatim or substantially similar enactments of model laws, is an accurate statement. The NAIC states repeatedly in its description of the


126 See §5 My Suggested Changes in the Program, infra.

127 See §3.2.1 Strict Uniformity, supra.
Program that model laws, or substantially similar language, are to be enacted for accreditation.\textsuperscript{128} I assert this is basically a good method of accreditation. The alternative is to base accreditation on creating legislation to meet several general statements of desired policy. Then, each jurisdiction would try to come up with a law which meets each general statement of desired policy. This would seem to provide less of the advantage that comes from a national coordinating effort. If the entire (national) industry works toward a formulation of specific language, the laws of each state have the benefit of this effort. The results of this effort, the language of the model laws, could then work as a presumption (in the mode of a safe-harbor) of what meets the Program requirements. There should be a procedure for proving that alternative formulations meet the policy targeted by the model law at issue.\textsuperscript{129}

The fourth factor, that there is confusion about what "substantial compliance" means, is an unproductive statement of the obvious. "Substantial compliance" means, in any particular instance, what the particular Review Team says it means. "Substantial compliance," in general, means the accumulation of meaning gathered from every decision of a Review Team regarding whether a particular item is in "substantial compliance" with the relevant model law. This is no different than the extensive history in the common law tradition of deciding cases based on a "reasonable man test," a "rational basis test," or the like. I am not suggesting that the Review Team is the same as the esteemed courts of this nation, but simply that a concept defined only by

\textsuperscript{128}NAIC, \textit{FINANCIAL REGULATION STANDARDS AND ACCREDITATION PROGRAM 6-15} (1995); see note 16, \textit{supra}.

\textsuperscript{129}See §5.5 \textit{The Presumption Method}, infra.
successive determinations based on that concept is nothing unusual.\textsuperscript{130}

The final factor in the NCOIL Report, that there has been a shift in emphasis "from national minimums to national optimums," is nothing more than a restatement of the second factor.\textsuperscript{131} This is simply another way of saying that the Program is placing too much emphasis on strict uniformity.\textsuperscript{132}

\section*{§3.5 The GAO Objections to the Program}

The United States General Accounting Office (GAO), at the behest of Representative Dingell, has conducted an investigation and review of the Program each year from its inception thru 1994. It reported its findings to the United States House Commerce Committee (Committee) in 1991, 1992, and 1993. There is expected to again be hearings of the Committee on the Program in the Spring of 1996.\textsuperscript{133} Past GAO and Committee comments can be said to represent the view and arguments that the insurance industry should be regulated at the federal level. Representative Dingell's most recent attack on state regulation, entitled "Wishful Thinking..." is the object of a vigorous dissent from the national regulatory recommendation by Committee Republicans.\textsuperscript{134} As a result, however, of the changing political tide in Washington

\textsuperscript{130}See §5.6 The Independent Auditor Review Concept, infra.


\textsuperscript{132}See §3.2.1 Strict Uniformity, supra.

\textsuperscript{133}\textit{Late News}, BUS. INS., Feb. 27, 1995, at 1 (1995 WL 7496820); Interview with Mark G. Noller, NAIC Senior Accreditation Manager (Feb. 2, 1996).

and the capitols of each state in 1994, Representative Dingell has found himself with a diminished role and voice. 135 It is the new conservative force within the state governments that have caused the self-examination of the NAIC in the mode described. supra, under the heading of NCOIL objections. 136 I assert the American people have spoken against national regulation.

In its first review after the implementation of the Program, the GAO concluded that the Program was a laudable effort, but was certain to be ineffective. 137 The GAO began with the premise that the insurance industry should be regulated according to several principles derived from the experience of the federal government in regulating the various components of the financial services industry. 138 These principles are that a regulatory organization would need the authority to (a) establish rules for safe and sound operation of insurers, (b) establish minimum standards for effective solvency regulation by state insurance departments, (c) monitor state insurance department functions, and (d) compel the state regulators to enforce the system. 139


138 Query whether the federal government has been very successful with the Savings & Loan and banking industries.

While I am in agreement with the first three identified principles, the fourth is not necessary to effective or efficient regulation of insurance industry solvency. It is this forth principle which is the primary area of displeasure of the GAO with the Program. The GAO maintains, quite simply, (a) that the NAIC must have the authority to force compliance with the Program; (b) it does not; (c) therefore, the Program cannot succeed. This is but one view in the argument over sanctions. I (a) maintain that the ability to force compliance with the Program is not necessary; (b) express no view on whether the NAIC has authority to force compliance; and (c) maintain that the Program is a success. Inherent in the analysis by the GAO is the belief that regulation must be strictly uniform to be effective. The report even implicitly

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140 The GAO identifies three problems with the Program. First, even if the standards of the Program were implemented in all the states, it would provide only an appearance of uniformity. Second, the Program has significant shortcomings which indicate it is not a credible system (i.e. that accreditation does not have any significance). Finally, the NAIC has no authority to compel compliance with the Program. Id. at 25. The first problem is based on a false assumption regarding strict uniformity identified immediately infra in the text. See also §3.2.1 Strict Uniformity, supra. The second problem is a combination of two criticisms by the GAO. The first is that there are no criteria for assessing compliance with the Program. This is a combination of the misunderstanding involving strict uniformity identified supra and the use of a "substantially similar" requirement for compliance. The "substantially similar" requirement is discussed, supra, in §3.4 The NCOIL Objections to the Program. The second is that there is a lack of documentation supporting the accreditation decisions. This is a valid criticism and is addressed in §5.3 Sunlight and §5.6 The Independent Auditor Review Concept, infra. The GAO maintains that even if the first two problems can be solved, the third problem is sufficient to cause the entire Program to be a failure.

141 See §3.3 Sanctions, supra.

142 Id.

143 See §3.2.5 The Original Goal, supra.
attributes this goal to the NAIC.\footnote{Insurance Regulation: Assessment of the National Association of the Insurance Commissioners, GAO/T-GGD-91-37 at 24-25 (May 22, 1991) (statement of Richard L. Fogel, Assistant Comptroller General, General Government Programs) (Compare "NAIC's efforts to achieve uniformity" and "According to the NAIC, its new accreditation program will have the effect of establishing a national system of solvency regulation consistent across all the states.".)} Attributing a goal of strict uniformity\footnote{See §3.2.1 Strict Uniformity, supra.} to the Program, however, is the result of a misunderstanding of what it means for the NAIC to establish a "national system of solvency regulation consistent across all states."\footnote{Insurance Regulation: Assessment of the National Association of the Insurance Commissioners, GAO/T-GGD-91-37 at 24-25 (May 22, 1991) (statement of Richard L. Fogel, Assistant Comptroller General, General Government Programs).} It does \textit{not} mean a single system of regulation or precisely replicated regulatory systems in each state. This can necessarily only be achieved by overt or \textit{de facto} national regulation.\footnote{De \textit{facto} national regulation is something that supporters of state regulation particularly wish to avoid. \textit{E.g.}, \textit{Keep the Momentum Going}, Bus. Ins., June 19, 1995, at 8 (1995 WL 7497431).} The conclusion of the GAO is predetermined using its analysis. The appropriate meaning to be attributed to the phrase is that a nationwide issue (solvency regulation of the insurance industry) will be dealt with in a manner which achieves uniform results \textit{(i.e. solvency in the industry)} in each state. It is the result of a solvent national insurance industry which will be the uniform goal of the regulation in each state. The precise method of achieving that goal \textit{cannot} be strict uniformity without predetermining that state regulation is inappropriate (or that national regulation is the only option).\footnote{See §4.1 The Advantage of State Regulation, infra.}
with the progress of the Program, but concludes that there is significant room for improvement. The report ignores the issue of primary focus in the first report (and significant later debate)—that is, the authority to compel compliance. This report identifies three problems in the Program. First, the GAO identifies as a problem that the standards are interpreted permissively. This is a repeat of the strict compliance (misunderstanding and) argument, supra, the GAO made the previous year. The second problem identified is too little focus on implementation of state solvency regulation programs. The claim here is that the existence of the appropriate programs—without the requirement that the programs are successfully implemented—is sufficient to gain accreditation. The NAIC disagreed with the GAO concerning the factual circumstances leading to this conclusion. It is apparent that (a) the accreditation standards requiring certain department funding for accreditation and (b) a direct requirement that the jurisdiction has "properly implemented all law and regulation standards" are

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150 For example, the GAO complains that one state was accredited even though its commissioner has the authority to "waive virtually all the provisions of the" holding company regulation adopted by the state. Also, the GAO noted variety in examiners' "approach, style, and scope of work" suggesting (to the GAO, at least) that individual states were not following the NAIC Examiner's Handbook. Id. at 4-6.

151 Id. at 6.

152 Id.

153 Id. at 8.
as complete and direct of a counter to this criticism as any regulatory system could provide.\textsuperscript{154} The Program does provide for a focus on implementation. The problem identified by the GAO is, actually, only a criticism of the lack of strict uniformity approached from a different angle. Because the implementation of a strictly uniform regulation in each state cannot be identified, the GAO has claimed that there has been a general lack of implementation. Once exposed for the true criticism proffered, it may be dealt with as the others relating to strict uniformity, \textit{supra}. The final problem identified is the lack of documentation supporting the accreditation decisions.\textsuperscript{155} This is a valid criticism. Although the NAIC's effort to maintain confidentiality (primarily of insurers) is the reason for the lack of documentation, I assert that there should be sufficient documentation to support all decisions regarding accreditation.\textsuperscript{156}

The third, and most recent, report again praises the accomplishments and efforts of the NAIC in its Accreditation Program.\textsuperscript{157} It continues to identify areas of concern with the program and acknowledges that some past identified problems\textsuperscript{158} have been partially remedied.\textsuperscript{159} It


\textsuperscript{156}See \S\S 5.3 \textit{Sunlight} and \S\S 5.6 \textit{The Independent Auditor Review Concept}, infra.


\textsuperscript{158}Specifically, the lack of documentation complained of in 1992 has been addressed and the situation has improved. GAO states, however, that documentation remains inadequate. \textit{Id.} at 3.
recognizes that no system of regulation is perfect—and that the Program is doing quite well—but falls back on its original criticism that the NAIC cannot force compliance with the Program.\textsuperscript{160} Again the GAO concludes that this means that the Program will be a failure.\textsuperscript{161} The arguments put forth supra explain why this criticism is not successful.

The areas of concern identified in the 1993 report are two mentioned in the 1992 report\textsuperscript{162} and the growing resistance\textsuperscript{163} to the Program by the state legislators.\textsuperscript{164} The GAO contends that the "growing resistance" is a problem because of the lack of enforcement ability by the NAIC.\textsuperscript{165} This is, again, a "bootstrap" criticism by the GAO. As identified supra, this method of analyzing the Program starts with the conclusion that only overt or \textit{de facto} federal regulation is effective and then uses it to justify the predetermined conclusion that only overt or \textit{de facto} federal regulation is effective.

\begin{itemize}
\item \textsuperscript{159}Id.
\item \textsuperscript{160}Id.
\item \textsuperscript{161}Id.
\item \textsuperscript{162}GAO objects to (a) a lack of specific standards which allows for permissive interpretation and (b) a lack of focus on performance which allows states with weak examination quality to be accredited. These have been addressed adequately in the discussion of the 1992 report, supra. \textit{Insurance Regulation: The National Association of Insurance Commissioners' Accreditation Program Continues to Exhibit Fundamental Problems,} GAO/T-GGD-93-26 at 4-6 (June 9, 1993) (statement of Richard L. Fogel, Assistant Comptroller General).
\item \textsuperscript{163}See, \textit{inter alia,} §3.4 \textit{The NCOIL Objections to the Program} and §3.3 \textit{Sanctions, supra}, regarding the growing resistance of state legislators.
\item \textsuperscript{164}\textit{Insurance Regulation: The National Association of Insurance Commissioners' Accreditation Program Continues to Exhibit Fundamental Problems,} GAO/T-GGD-93-26 at 4-6 (June 9, 1993) (statement of Richard L. Fogel, Assistant Comptroller General).
\item \textsuperscript{165}Id.
\end{itemize}
§3.6 Recent NAIC Action on the Program

The NAIC has recently been working diligently to address the concerns outlined supra. To this end, the following has been accomplished. The deadline for enacting nine new standards necessary to receive/maintain accreditation was extended from January 1 to July 1, 1996.\textsuperscript{166} More recently, the deadlines for all new standards was changed, again, to July 1, 1997.\textsuperscript{167} In June of 1995, the NAIC declared itself to be "a group of public officials imbued with the public trust and/or an instrumentality of the states."\textsuperscript{168} The NAIC began a comprehensive review of the Program and held a public hearing to solicit comments in September, 1995.\textsuperscript{169} To this end, the

\footnote{166}{\textit{NAIC Wrangles with Multiple Issues at Meeting}, \textit{BEST'S REV.--LIFE-HEALTH}, Nov. 1, 1995, at 10 (1995 WL 10756290).}

\footnote{167}{\textit{NAIC Falls S1 Million Behind on Fees}, \textit{THE INS. REGULATOR}, Apr. 1, 1996, at 1 (1996 WL 5554456).}

\footnote{168}{\textit{Keep The Momentum Going}, BUS. INS., June 19, 1995, at 8 (1995 WL 7497431). This is a significant change from past policy. The NAIC has always regarded itself as a private trade association. This move is significant because it tends to be an admission by the NAIC that its activities cannot remain secretive. It is also significant because it goes a significant distance to eliminating the antitrust action threat facing the NAIC and the Program. As noted supra in the text, Senator Velella of New York has requested an antitrust probe of the NAIC. \textit{N.Y. Lawmaker Requests Probe of NAIC for Restraint of Trade}, \textit{BEST'S REV.--LIFE-HEALTH}, Dec. 1, 1995, at 10 (1995 WL 10756368). The National Association of Independent Insurers (NAII) and the National Risk Retention Association (NRRA) have both indicated that the Program has antitrust problems. \textit{NAIC Accreditation Program Faces New Attacks}, \textit{THE INS. ACCT.}, Aug. 14, 1995, at 4 (1995 WL 7151331). Mr. Schacht of Illinois has called the program "a lawsuit waiting to happen." \textit{Illinois Official Urges Accreditation Reform}, \textit{THE INS. ACCT.}, Oct. 3, 1994, at 3 (1994 WL 11229354). In dicta, a federal judge has indicated that the NAIC may not have antitrust immunity. Preferred Physicians Mutual Risk Retention Group v Cuomo, 865 F. Supp. 1057, 1072 (S.D.N.Y. 1994). The antitrust issue is related to the private/public nature of the NAIC and to the sanctions of the Program. See §3.3 Sanctions, supra.}

\footnote{169}{\textit{NAIC, THE FINANCIAL REGULATION STANDARDS AND ACCREDITATION PROGRAM} 16 (1995).}
NAIC has engaged Ernst & Young to perform an operational audit of the Program.\textsuperscript{170} The "results oriented" working group has been established to address problems with the Program.\textsuperscript{171} The group plans to have public hearings on the idea of "core" standards.\textsuperscript{172} In September, 1995, the NAIC adopted a policy requiring written evidence of several factors before a proposed standard would be considered for becoming part of the Program.\textsuperscript{173} Finally, the new president of the NAIC, Brian Atkinson of Maine, has stated that "we owe it to ourselves to evaluate the accreditation program" and that "[i]f the NAIC were a company[,] I would ask if we were moving away from our core product line."\textsuperscript{174} Mr. Atkinson has identified solvency regulation as the essence of insurance regulation.\textsuperscript{175}

\textsuperscript{170} Telephone Interview with Mark G. Noller, NAIC Senior Accreditation Manager (Feb. 2, 1996).


\textsuperscript{173} See \textsection 3.4 The NCOIL Objections to the Program, supra; NAIC, FINANCIAL REGULATION STANDARDS AND ACCREDITATION PROGRAM 17 (1995).


\textsuperscript{175} Id.
§3.7 Situations of Several States

Information regarding the accreditation review of any particular state is regarded by the NAIC as non-public confidential information. In my opinion this is not appropriate.

A limited quantum of information regarding several states has come into the public domain, or is considered by the NAIC to be public, and is worthy of consideration. The NAIC has made limited comment on the deficiencies in the two unaccredited states' regulatory systems. The two states, New York and Nevada, are each said to be lacking in the Laws and Regulations area.

New York is generally considered—even by the NAIC—to have one of the best insurance regulatory systems in the country. It was one of the first states to become accredited under the Program. It is, notably, also the only state to have lost its accreditation. The NAIC identified three reasons for the suspension of New York's accreditation. These had to do with

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176 Letter from David B. Simmons, Executive Vice President of the NAIC, to the GAO, (Jan. 14, 1993).

177 See §5.3 Sunlight and, generally, §5 My Suggested Changes in the Program, infra.

178 Telephone Interview with Mark G. Noller, NAIC Senior Accreditation Manager (Feb. 2, 1996).


181 New York lost its accreditation on March 8, 1993.

182 (a) New York had insufficient control over managing general agents; (b) New York had insufficient control over reinsurance intermediaries; and (c) New York did not have in place
New York not having in place two model laws (or substantially similar language) newly required for maintaining accreditation. At the time New York's accreditation was suspended, substantially similar bills were pending in the state legislature. 183 They were expected to be passed with almost no opposition. 184 Interestingly, New York remains unaccredited. Throughout its suspension, New York has remained a vocal part of the NAIC and the Program. Recently, New York's commissioner made several NAIC and Program reform proposals in coordination with California, Illinois, and Texas. 185 New York is also taking a lead role in the "results oriented" working group recently formed at the NAIC to consider changes in the Program. 186

New York has also taken many actions, regarding the Program, outside of the NAIC. State Senator Guy Velella deliberately stalled the passage of the legislation necessary to regain

sufficient procedures designed to make it easier for enforcement agencies from various states to exchange sensitive information. Meg Fletcher, New York's Accreditation Suspended, BUS. INS., Mar. 15, 1993 (1993 WL 7805568).

183 Id.
184 Id.
185 These proposals include more openness in meetings and finances, slower addition to the Program requirements--a four year wait on "desired" standards, and requiring 25 states to adopt a model law before it is a requirement for accreditation. L. H. Otis, New Commissioners Call for a Shakeup at NAIC, NAT'L UNDERWRITER--LIFE & HEALTH, Mar. 27, 1995, at 6 (1995 WL 8436995).

New York passed retaliatory legislation in 1994. This legislation provided the New York insurance department with the ability to respond in kind to other state insurance departments who sanctioned New York domiciliary insurers for the department's lack of accreditation. New York was also one of the first states to introduce a bill to its legislature which provides for NAIC oversight. New York has also gone so far as to call for an antitrust probe of the NAIC. New York has, in these ways, benefitted the Program by helping to shape it in a manner that provides true individual state regulation with the benefits of a national coordinating unit.

In 1994, Texas provided the impetus for a lively discussion regarding the credibility of the Program. This discussion was, of course, hampered significantly by the insistence of the NAIC on a strict and broad policy of confidentiality. Essentially, Texas was deficient in one of its regulatory laws. A Texas legislator and the Texas commissioner met with the NAIC,

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188 New York Governor Signs Retaliatory NAIC Legislation, BEST'S REV.--LIFE-HEALTH, May 1, 1994, at 12 (1994 WL 2860511). Texas and Alaska also passed retaliatory laws at this time. Id.

189 See §3.3 Sanctions, supra.


192 The deficiency was in the area of extraordinary dividends. Thomas Ressler, Texas Status Unchanged, NAIC Challenges Attacks on Accreditation Sanction, THE INS. REGULATOR,
and the result was that Texas retained its accreditation—even though technically not in compliance.\textsuperscript{191} The discussion that was generated centered around the fact that only a year earlier, New York's accreditation was suspended for seemingly the same problem—deficiency in one or two laws.\textsuperscript{192} The explanation given by the NAIC for the discrepancy is that the Texas issue was simply a matter of a one word deletion in an act of the legislature, which only meets once every two years, and that the New York problem was more serious.\textsuperscript{193} I express no opinion on the apparent discrepancy except to say that more documentation and disclosure are needed in the accreditation/suspension process.\textsuperscript{196}

The accreditation of Vermont is another interesting episode in the Program. Vermont’s difficulties in achieving accreditation stem from its treatment of alternative risk transfer entities (ie. risk-retention groups and captives). Vermont is recognized as having an extremely good track record in regulating these entities separate from traditional insurers.\textsuperscript{197} After several years

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\textsuperscript{197}Telephone Interview with Mark G. Noller, NAIC Senior Accreditation Manager (Feb. 2, 1996); L. H. Otis, States Battling NAIC Over Accreditation Process, NAT'L. UNDERWRITER--LIFE & HEALTH, Nov. 28, 1994, at 22 (1994 WL 8708276).
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\textsuperscript{196}See §5.3 Sunlight and §5.6 The Independent Auditor Review Concept, infra.
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\textsuperscript{197}Illinois, which is accredited, also regulates these entities separate from traditional insurers. Dick Heydinger, The Case for Vermont: NAIC is Wrong to Insist Vermont Must Comply With All Model Laws, BUS. INS., Feb. 28, 1994 (1994 WL 3832555). Query why there is
of Vermont criticizing the Program, primarily through NCOIL and the National Governor's Association (NGA), the NAIC decided to exclude the regulation of risk-retention groups from the Program. This was followed by a "favorable review" of the Vermont department in late 1995. Vermont has since been accredited. This should be recognized as another example of regulatory system working to recognize innovation and unique needs of individual states in regulation.

§4 Theoretical Issues

§4.1 The Advantage of State Regulation

As discussed supra, in §2 Regulation of Insurance in America, it is without question that the federal government has the power to regulate the insurance industry pursuant to the Commerce Clause. It is by action of the United States Congress, in the form of the McCarran-

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a discrepancy in the treatment. It could have to do with the relatively small portion of Illinois insurers which fall into this alternative category and the relatively large portion of Vermont insurers falling into this alternative category. This might tend to indicate less risk of solvency problems stemming from this issue in Illinois.


Ferguson Act\textsuperscript{20} that the responsibility of the regulation of the insurance industry has been given to the states. State regulation provides for a much better system of regulation that could be produced via federal regulation. Three advantages achieved through state regulation are innovation, specification, and diversification.

Mr. Justice Brandeis said that one of the unique strengths of our form of government is that each state may be given the freedom to "serve as a laboratory; and try...novel economic experiments."\textsuperscript{20} One of the major advantages of the state regulation of the insurance industry is that new and innovative ideas regarding solvency regulation may be experimented with by various states. This experimentation will have a relatively small impact on the industry if not successful and will serve as an example to be used by each state to benefit the entire industry and entire citizenry if successful. Also, by virtue of the smaller number concerned in the regulation in any one state (than in the entire nation), it is more susceptible to these new ideas. Fewer persons need be convinced of an idea to allow experimentation in that idea. No one has attempted to suggest that the perfect method of regulating the insurance industry—or any industry, for that matter—has been found. The continuous process of experimentation by the states is one of the only ways, and virtually the only practical manner, of improving regulation and coming closer to the "perfect" method.

State regulation of the insurance industry allows for state specific solutions to state specific problems. As the NAII states, the substantial benefits to consumers attained by state

\textsuperscript{20} 15 U.S.C. §1011

\textsuperscript{20} New State Ice Co. v Liebmann, 285 U.S. 262, 311, 52 S. Ct. 371, 387 (1932) (Brandeis, J., Dissenting)
regulation are, *inter alia*, diversity and flexibility allowed by such a system. Mr. Schacht, of Illinois, has explained that the Program is *not* intended to hamper the ability of individual states to tailor regulation to the needs of their citizens. In 1816, Thomas Jefferson said that "[i]n government, as well as in every other business of life, it is by division and subdivision of duties alone, that all matters, great and small, can be managed to perfection." He was advocating decentralization in the functions of government. "Perfection" in managing the affairs of the insurance industry can best be attained by regulation which allows for tailoring specific solutions to specific problems.

Finally, state regulation provides a diversification function. It is elementary finance that diversification serves to reduce risk. By having 55 jurisdictions monitor the solvency of insurers in America, there is significantly less risk of complete industry failure than there would be in a single national solvency regulation system. Significant development of this idea is beyond the scope of this paper.

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208 The Savings & Loan industry provides a nice example of nearly complete industry failure while monitored by a single national solvency regulatory system.
§4.2 The Race to Efficient Regulation ("Race to the Bottom" Theory Does Not Apply)

The phrase "race to the bottom" has its origins in the corporate law. The theory states that a federal system of regulation should be preferred because multiple state regulation will lead to destructive competition (in the form of less effective regulations) among states to become the domicile of regulated businesses. The theory has come under attack recently as not applying to other disciplines and has even been questioned in some applications to corporate law. This theory does not apply to insurance regulation or the Program. First, any state crafting

20 The phrase was originally styled "the race for the bottom" and was invented by Professor William L. Cary in William L. Cary, Federalism and Corporate Law: Reflections Upon Delaware, 83 Yale L.J. 663, 666 (1974).

21 Richard L. Revesz, Rehabilitating Interstate Competition: Rethinking the "Race-to-the-Bottom" Rationale for Federal Environmental Regulation, 67 N.Y.U. L. Rev. 1210 (1992). Professor Revesz traces the argument against "race to the bottom" theory to Tiebout. Charles M. Tiebout, A Pure Theory of Local Expenditures, 64 J. Pol. Econ. 416 (1956). Tiebout argues that persons will move to the jurisdictions that provide them with their individual preferential mix of taxes and public services and that these jurisdictions will be of optimum size. He concludes that provision of services at the local level, and competition between these jurisdictions, is preferable to national provision of services. Professor Revesz concludes that the theory is not appropriate in the environmental context and demonstrates that the corporate and banking contexts have characteristics making them different from other regulatory schemes in such a way that even if the theory is appropriate in those two contexts it should not be automatically extended to other regulatory schemes. In the corporate context the distinguishing characteristic is the principal-agent problem. The literature indicates that the theory may not even apply to corporate law in contexts not implicating the principal-agent problem. Lucian A. Bebchuk, Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law, 105 Harv. L. Rev. 1435, 1485-1495 (1992). In the banking context the distinguishing characteristic is the presence of the FDIC. Henry N. Butler & Jonathan R. Macey, The Myth of Competition in the Dual Banking System, 73 Cornell L. Rev. 677, 715 (1988). This factor is clearly not present in the insurance context, as there is no federal guaranty agency associated with insurance solvency (the guarantee funds are also at the state level).

21 Jonathan R. Macey & Geoffrey P. Miller, The McCarran-Ferguson Act of 1945: Reconciling the Federal Role of Insurance Regulation, 68 N.Y.U. L. Rev. 13 (1993). Macey & Miller conclude that the "race to the bottom" theory does not apply in the insurance regulation context. They base this conclusion on three items. First, customers would choose to purchase
insurance regulation will want to protect the insureds within its borders from the companies domiciled within the state. Effective solvency regulation imposed on the state’s domiciled insurers will serve to protect the in-state insureds doing business with those companies. Next, any state crafting insurance regulation will want to protect insureds within its borders from insurers domiciled in other states. This means they will either want (a) other states to have effective insurance regulation or (b) they will want to regulate out-of-state (foreign) insurers. If the states choose option (b), there will be multiplicative regulation of all insurers. If the states collectively choose option (a), there will not be unnecessary multiplicative effort.\textsuperscript{212} The choice of option (a) is the choice of the Program. Insurers will also want option (a) because of the obvious lower cost associated with this option. This lower cost will benefit each state in the form of lower costs to its insureds.

§5 \hspace{1em} **My Suggested Changes in the Program**

In suggesting changes to the Program I assume, and based on the analysis supra I assert, products which do not contain features harmful to their welfare. Because of a desire to retain consumer demand, insurers would not demand lax legal regimes. Second, insurers cannot export costs (\textit{i.e.} detrimental policy terms) to customers in other states because these items will be regulated by the state in which the insured resides. In items such as exported costs related to solvency, established insurers, the ones with political clout, will want to maintain high standards as barriers to entry and as reputational enhancements. Finally, there is an elaborate mechanism for state insurance departments to cooperate and communicate (\textit{i.e.} the NAIC and the Program). The practical necessity of working together provides a significant disincentive to beginning a "competition in laxity."

\textsuperscript{212}An example of this choice in action is Hawaii’s decision last year to allow any company domiciled in three accredited states to automatically receive its license to conduct business in Hawaii. Susanne Sclafane, \textit{Brokers Push Deregulation Theme, NATL UNDERWRITER--PROP. & CASUALTY}, Mar. 18, 1996, at 4 (1996 WL 8650101).
the following to be true. The Program has caused to be put in place in each accredited jurisdiction, and to a significant extent in each of the currently unaccredited states, an effective basic plan for insurance solvency regulation. Further, the Program can be said to be in a "mature" phase. By this I intend that major revision is not needed, that the Program can currently be said to have attained its goal, and that the Program represents the extent (the maximum) of the present agreement on what is to be included in an effective regulatory system. Finally, state—not federal—regulation is the most effective and efficient choice for insurance regulation. With these assumptions/assertions in mind, I will proceed to recommend several ideas closely related to and derived from suggestions, outlined and attributed to supra, by various individuals and groups. I will then put forth two suggestions for change in the Program which I believe to be original.

§5.1 New Standards

The first suggestion, promoted primarily by those believing that more state legislative control is needed over the Program 213, is to require any suggested new standard to be implemented by at least 25 jurisdictions prior to becoming part of the Program and becoming necessary to gaining or maintaining accreditation. The figure of 25 is fifty percent, plus one of

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the jurisdictions currently accredited. It is also half the states. While the precise number is not of great importance, the idea is that requiring about half the jurisdictions to implement (this means that their respective legislatures have approved them with no overt pressure from the NAIC) any suggested new standard will ensure that there is true agreement as to the importance and universal applicability of the standards that become part of the Program. I do not suggest that this is an easy standard (25 jurisdictions). It is not. However, because the Program is in a mature phase, it should be difficult to form new requirements for continued accreditation. The basic regulatory structure is present, these would simply be improvements.

§5.2 Limits on Repeal of Standards

The next suggestion is to limit repeal of the existing standards in the Program. The repeal of the inclusion of any standard in the Program should be achieved by a 3/4 vote of the commissioners in the NAIC. Here, also, the precise number is not important but should be significantly greater than that needed to make a new standard part of the Program. This is again based on the Program being in a mature phase. As identified in §4.1 The Advantage of State Regulation, supra, the various jurisdictions should desire procedures designed to keep the Program consistent and at a high level of effectiveness.

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214 This suggestion is a reaction to the recommendation to the work of the "results oriented" working group to decrease the standards to 13 "core" standards. The suggestion is not so much in opposition to the idea of the group as it is a desire for caution in implementing it recommendations. L. H. Otis, NAIC Eases Deadlines On Accreditation Program, NAT'L UNDERWRITER—LIFE & HEALTH, Sept. 18, 1995, at 3 (1995 WL 9129834).

215 This number is derived from the amendment procedure in the U.S. CONST. art. V.
§5.3 Sunnylight

The NAIC should make disclosure of its decisions and actions regarding particular states. Now that the NAIC has conceded that it is a "public entity", it seems that the next logical step is to make its findings public.\(^{216}\) I do not disagree with the idea that private\(^{217}\) insurance companies have a right to confidentiality. I do, however, disagree with any suggestion that any jurisdiction has any interest in maintaining its regulatory structure or activities in confidence. Openness about Reviews of state insurance departments for compliance with the Program will only serve to give credibility to the Program and improve each insurance department. "Sunlight" is a key ingredient in the growth of effective and fair government.

§5.4 Interstate Compacts

The idea of interstate compacts has been suggested several times in conjunction with insurance regulation.\(^{218}\) I believe that interstate compacts do have a role in insurance regulation-

\(^{216}\)See §3.6 Recent NAIC Action on the Program, supra.

\(^{217}\)Query whether any insurance company can be considered "private."

although not in solvency regulation. The use of interstate compacts should be limited to "ministerial" types of regulation. By "ministerial" I intend things which lack significant controversy, make the activities of national insurers more efficient, and serve state interests collectively without threatening the states not a party to the particular compact. The division of the NAIC into four zones provides a workable framework for generating these compacts and identifying the states to be involved in each. The Midwest Zone has been active in this area. Examples of "ministerial" types of regulation include harmonization of policy forms and NAIC oversight legislation focussing on disclosure. Examples of items to avoid in the interstate compact area are rate regulation and solvency regulation. I mention this idea primarily because of its possible value in enacting NAIC oversight legislation. As mentioned at several points in this paper, state control, fairness, effectiveness, and efficiency in the Program can be bolstered by the introduction of legislation requiring the NAIC to make public certain types of information regarding the Program. NCOIL and NCSL can be helpful in this endeavor. I do not express an opinion regarding whether the goal should be a single interstate compact or four (one for each NAIC zone) on this issue.

§5.5 The Presumption Method

The next change I advocate, I will call the "presumption method". This is essentially a


219 The U.S. Congress will ensure that this last goal is met. U.S. CONST. art. I, § 10.

variation and extension of the present system of model law regulation within the Program.

Currently several of the standards call for the enactment of specific model laws or "substantially similar" language.\textsuperscript{221} This has been the basis for objections to the Program from a number of fronts.\textsuperscript{222} The "presumption method" works as follows. A state comes into compliance with the Program by enacting laws and regulations that meet each of the standards of the Program. Enactment of a model law, or language "substantially similar" to a model law, will be regarded as a presumption—a non-exclusive safe harbor—of meeting the relevant standard at issue. The jurisdiction applying for accreditation, or wishing to demonstrate compliance to retain accreditation, would have the burden of showing that its alternative method of meeting the substance of the standard at issue will be effective. This is to be shown by expert legal and economic analysis of the proposed alternative method. In this analysis, an expected time line for the production of practical evidence of the success of the alternative method in achieving the substance of the Program standard at issue shall be produced. The analysis of a proposed alternative method is deemed to have met the burden of proof if 1/3 of the commissioners from all the accredited states approve it. The reason for setting a relatively low threshold is twofold. First, the effect of an alternative method is felt most by the host jurisdiction. The effect on the remaining jurisdictions is secondary only. Second, it is desirable to encourage experimentation. This is one of the major advantages of a state system of regulation.\textsuperscript{223}

\textsuperscript{221}See note 16, supra.

\textsuperscript{222}See \textsection 3.4 The NCOIL Objections to the Program and \textsection 3.5 The GAO Objections to the Program, supra.

\textsuperscript{223}See \textsection 4.1 The Advantage of State Regulation, supra.
The proposed time line must coincide with the next scheduled Review of the jurisdiction's compliance with the Program.\textsuperscript{224} If the proposed time line does not coincide with the next scheduled Review, the jurisdiction must get approval of the commissioners from 2/3 of the accredited jurisdictions. This will have the effect of keeping review costs down (i.e. there would be no need for a special review to determine if the alternative method has met its goal) and causing the jurisdictions to limit their suggestions of alternative methods to a reviewable timetable (i.e. this will channel suggestions of alternative methods to five year intervals for each state—allowing for some degree of isolation of the effects of the different alternative methods being implemented in any particular state at any particular time).

\textbf{§5.6 The Independent Auditor Review Concept}

The final suggested change to the Program, I will call the "independent auditor review" concept. The Program has been criticized for having the same body which accredits (the NAIC) perform the accreditation evaluation (the NAIC, again).\textsuperscript{225} The "independent auditor review" idea states, quite simply, that the Review Team\textsuperscript{226} should be replaced with a certified independent auditor, preferably one of the Big Six accounting firms.\textsuperscript{227} The audit teams should

\textsuperscript{224}Recall that Reviews are scheduled every five years.

\textsuperscript{225}National Underwriter P+C, November 28, 1994. The GAO has also criticized this aspect of the Program. See §3.5 The GAO Objections to the Program, supra.

\textsuperscript{226}NAIC, FINANCIAL REGULATION STANDARDS AND ACCREDITATION PROGRAM 2 (1995).

\textsuperscript{227}Unless determined to represent a conflict of interest, it appears that Ernst & Young would be an economical choice due to the expertise it is currently gaining in association with its operational audit of the Program. I am, however, not endorsing any particular firm.
consist of accountants and attorneys. The Accreditation Review process is nothing more than an audit. CPA firms have extensive experience in this field. It is what they do. They are also regarded as credible and independent. This should go a significant distance in providing credibility to the Program and removing the suggestion of conflict of interest on the part of the NAIC.

§6 Conclusion

The NAIC Accreditation Program has made significant progress since its beginning in 1990. All but two states are currently accredited—and these are very close to accreditation. The insurance departments in all jurisdictions have improved because of the Program. While a national crisis in some financial intermediaries has come to pass, there is generally not significant concern that such a thing could happen in the insurance industry. The Program may appropriately be called a success.

This is not to say that the Program is without flaws or room for improvement. I have made several suggestions, supra, regarding possible improvements in the Program. None of these are huge or sweeping changes—that is simply not necessary. They are all items which could be implemented with limited disruption to the Program or the industry. I believe they would help improve the credibility of the Program and bolster the advantages of state regulation of the insurance industry.