

RESEARCH SUMMARY

Administrative Browbeating and Insurance Markets

Some state insurance regulators are using their regulatory power to coerce insurers into furthering the regulators' political ends. In "Administrative Browbeating and Insurance Markets," George A. Mocsary argues that regulators are undermining the benefits that a properly functioning insurance market can provide and offers options for reform.

INSURANCE IS AN ENABLER

Insurance enables people to engage in socially desirable activities that would otherwise be too risky.

Without homeowners' insurance, for example, many families could not bear the risk of owning a home because one fire or hurricane could wipe out their savings. Insurance allows for the transfer of these risks to an insurer through a manageable payment scheme that amounts to a fraction of the home's value. Regulators typically don't understand the nuances of such arrangements as well as the insurer or the insured do.

INSURANCE REGULATORS CAN CAUSE HARM

When they (a) prevent private parties from freely transacting in the insurance marketplace or (b) seem to make decisions on the basis of politics rather than in pursuit of their regulatory mission, regulators can

- prevent consumers from engaging in legal activities by removing the safety net that insurance can provide to them;
- target disfavored outgroups or entities whose activities are not risk-free, are not illegal, and may even be socially desirable (e.g., gun ownership and home ownership); and
- hurt markets by depriving them of data on safety and risks.

State regulators, courts, and state legislatures are unlikely to rein in these abuses. And while the insurance regulators' trade association can take steps to begin to address the problem, the constituent regulators may block attempts to curb their own abuses. Real reform must be enabled by the US Congress.

THE FEDS CAN HELP—A MINIMALIST APPROACH

Congress granted the states power over insurance regulation because it believed the states were better positioned to ensure the stability of such markets. As a result, the "business of insurance" is unique among the financial services in that it is subject only to state-level regulation. That means federal regulators currently lack the power to intervene in insurance markets.

Neither the insurance industry nor state regulators would want thorough federal oversight of the type that exists in the banking sector. But to counter administrative browbeating by state insurance regulators, Congress can

- enable existing federal agencies to serve as intermediaries between Congress and the states;
- pass legislation that creates a federal regime that insurers can join—an opt-in system that leaves state regulation untouched; or
- pass legislation that targets abuses by state regulators.

These steps can help protect and restore the role of properly functioning insurance markets in the modern economy.