

Research



Systemic Risk and Regulation: The Misguided Case of Insurance SIFIs

SEPTEMBER 20, 2016

The American Action Forum today released a paper by Scott Harrington, Professor at The Wharton School of the University of Pennsylvania, on the designation of nonbank Systemically Important Financial Institutions (SIFIs) by the Financial Stability Oversight Council's (FSOC). Dr. Harrington reaches three conclusions about FSOC's reasoning and methodology for designating insurance companies as Systemically Important Financial Institutions (SIFIs) under the authority given to them by the Dodd-Frank Act (Dodd-Frank): (1) There is no compelling evidence that any life insurer poses a threat to the financial stability of the United States, (2) Dodd-Frank's Section 113 and FSOC's regime of designating individual insurance organizations as subject to enhanced supervision is flawed both in concept and in execution, and (3) it would be preferable to move towards an activities-based approach to systemic risk monitoring and supervision.

Coming to these conclusions, the analysis explores an extensive array of research and debate over whether insurance companies pose systemic risk with a focus on U.S. life insurers. Dr. Harrington considers FSOC's designation process, its rationales for designating AIG, Prudential, and Metlife as SIFIs, and takes a deep dive into MetLife's lawsuit challenge to FSOC to rescind the designation as a case study for a discussion about life insurers and systemic risk.

In recommending an activities-based approach for systemic risk monitoring and supervision, Dr. Harrington cites the Financial Stability Board's recent movement toward such an approach for asset managers, which will focus on monitoring and supervision of specific activities with the potential for systemic risk as opposed to entire entities, as FSOC does. Dr. Harrington suggests that if U.S. regulators were to shift towards an activities-based approach for insurers, it might have positive spillover effects globally.

With regard to MetLife specifically, Dr. Harrington cites to a lack of any precedent discussed in FSOC's detailed designation for what might happen with the failure of an organization of the scale and scope of MetLife. He also points to the designation's consideration of the extent to which the companies were already regulated by state regulators and the complexity of resolving the institutions if necessary. In doing so, he quotes FSOC's own voting member with insurance expertise, Roy Woodall, who stated in dissent, "The underlying analysis utilizes scenarios that are antithetical to a fundamental and seasoned understanding of the business of insurance, the insurance regulatory environment, and the state insurance company resolution and guaranty fund systems. As presented, therefore, the analysis makes it impossible for me to concur because the grounds for the Final Determination are simply not reasonable or defensible, and provide no basis for me to concur."

[Click here](#) to view the research.