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2019]

DUAL REGULATION OF INSURANCE

CHRISTOPHER C. FRENCH*

ABSTRACT

Since this country was created, the insurance industry has been principally regulated by the states with infrequent Congressional interventions. As the insurance industry has evolved in recent decades, however, individual states have become unable to adequately regulate some insurers, such as multinational insurers and foreign insurers, because they lack jurisdiction over such entities. Simply having the federal government assume responsibility for regulating insurers will not solve the current regulatory problems, however, because Congress' past forays into regulating certain areas of insurance generally have yielded poor results. Consequently, this Article makes the novel proposal and argument that, with the creation of the Federal Insurance Office (FIO) in 2010, the time is ripe for dual state and federal regulation of insurance. The FIO could regulate the areas of insurance where states are unable to do so or have done so inadequately while the states could continue to regulate areas where they have demonstrated competence.

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I. INTRODUCTION

THE basic legal approach to regulating insurance has been the same in this country since 1782 when insurance companies first formed in the United States. It is time for a change, and this Article proposes a novel approach to regulating insurance in the twenty-first century.

Most of the scholarship regarding insurance regulation involves the McCarran-Ferguson Act of 1945,¹ which is the statute that reserved the regulation of the business of insurance to the states, and it has focused on whether the insurance industry should be exempt from federal antitrust laws and be permitted to collude regarding premium prices and the sharing of claims data.² This Article does not address that issue because the insurance industry generally is competitive today regarding pricing and extensive information regarding prospective policyholders and claims data is readily available in this age of “Big Data.”³ Consequently, the question

1. 15 U.S.C. §§ 1011-1015 (2018).

2. See, e.g., 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); Jay Angoff, *Insurance Against Competition: How the McCarran-Ferguson Act Raises Prices and Profits in the Property-Casualty Insurance Industry*, 5 YALE J. ON REG. 397 (1988); Earl W. Kintner, Joseph P. Bauer & Michael J. Allen, *Application of the Antitrust Laws to the Activities of Insurance Companies: Heavier Risks, Expanded Coverage, and Greater Liability*, 63 N.C. L. REV. 431 (1985); Alan M. Anderson, *Insurance and Antitrust Law: The McCarran-Ferguson Act and Beyond*, 25 WM. & MARY L. REV. 81 (1983); Larry D. Carlson, *The Insurance Exemption from the Antitrust Laws*, 57 TEX. L. REV. 1127 (1979); Spencer L. Kimball & Ronald N. Boyce, *The Adequacy of State Insurance Rate Regulation: The McCarran-Ferguson Act in Historical Perspective*, 56 MICH. L. REV. 545 (1958).

3. See, e.g., Macey & Miller, *supra* note 2, at 85 (“The insurance industry is ideally suited to rate setting by competitive forces.”); J. David Cummins, *Property-Liability Insurance Price Deregulation: The Last Bastion?*, in DEREGULATING PROPERTY-LIABILITY INSURANCE: RESTORING COMPETITION AND INCREASING MARKET EFFICIENCY 1, 7 (J. David Cummins ed., 2004) (“Advances in computing and databases allow

of whether the antitrust exemption provided under the McCarran-Ferguson Act should be repealed is not as important today as it may have been in the past. Instead, this Article asks and answers the question of whether the current regulatory regime, in which states are the primary regulators of insurance, is still the best regulatory approach in the twenty-first century. The answer is “no.”

The insurance industry has evolved and grown so much since this country was created in the 1700s, and since the McCarran-Ferguson Act was passed in 1945, that states are no longer able to adequately regulate many important aspects of insurance. Today, the insurance industry is dominated by large multinational and foreign insurers that are beyond the regulatory jurisdictions of individual states.⁴ Indeed, under the current regulatory regime, no regulatory entity in the United States is actually regulating foreign insurers or multinational insurers in a comprehensive way.

A prime example of how this lack of comprehensive regulation has become a problem was the financial collapse of American International Group, Inc. (AIG) in 2008 and the federal government’s subsequent \$182.5 billion bailout of AIG.⁵ AIG is a multinational insurer that does business throughout the United States and the world as a conglomeration of affiliated and subsidiary insurance companies.⁶ Each state, however,

all but the smallest insurers to analyze data and conduct actuarial calculations with a speed and sophistication unheard of in the past, reducing the need to rely upon rating bureaus with their potential for stifling competition.”); Max N. Helveston, *Consumer Protection in the Age of Big Data*, 93 WASH. U.L. REV. 859, 862 (2016) (“Insurers, always interested in refining their predictive capabilities, have been aggressively integrating Big Data methodologies into their business operations.”); Rick Swedloff, *Risk Classification’s Big Data (R)evolution*, 21 CONN. INS. L.J. 339, 340 (2015) (“Big data is at the insurance industry’s door.”).

4. See, e.g., Benjamin Elisha Sawe, *Largest Insurance Companies in the World by Revenue*, WORLD ATLAS (Mar. 6, 2018), <https://www.worldatlas.com/articles/largest-insurance-companies-in-the-world-by-revenue.html> [<https://perma.cc/Ry3F-N2AZ>] (listing the ten largest insurance companies in the world and noting the prevalence of multinational companies at the top of the list); *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 422 (2003) (“A basic principle of federalism is that each State may make its own reasoned judgment about what conduct is permitted or proscribed within its borders, and each State alone can determine what measure of punishment, if any, to impose on a defendant who acts within its jurisdiction.”); Macey & Miller, *supra* note 2, at 33.

5. See generally William K. Sjostrom, Jr., *The AIG Bailout*, 66 WASH. & LEE L. REV. 943 (2009).

6. See, e.g., Sjostrom, *supra* note 5, at 945 (“AIG is ‘a holding company which, through its subsidiaries, is engaged in a broad range of insurance and insurance-related activities in the United States and abroad.’”); Daniel Schwarcz, *A Critical Take on Group Regulation of Insurers in the United States*, 5 UC IRVINE L. REV. 537, 543–44 (2015) (“Historically, many large insurance holding companies adapted to the mismatch between state-based insurance regulation and the national and international scope of their operations by incorporating individual insurance entities within multiple different states.”); Daniel Schwarcz & Steven L. Schwarcz, *Regulating Systemic Risk in Insurance*, 81 U. CHI. L. REV. 1569, 1633 (2014) (“[I]nsurance holding companies operate in numerous jurisdictions through many different subsidiaries . . .”).

can only regulate the AIG entities that are doing business in its state.⁷ Consequently, although the states collectively were regulating the various pieces of AIG that did business in their states in 2008, AIG arguably collapsed because no single state or the federal government was actually regulating AIG as a whole. The states were looking at the various trees of AIG, but no one was looking at AIG the forest.

In addition to the lack of regulation of multinational and foreign insurers, the current regulatory regime is a patchwork quilt of inconsistent state laws.⁸ In practice, this means the outcomes of many insurance disputes are dictated by which party wins the race to the courthouse to secure the more favorable state law.⁹ This makes the resolution of insurance disputes appear to be ad hoc and arbitrary, which generally undermines the public's confidence in the fairness of the legal system.

Having fifty state insurance commissioners review and approve the dozens of policy forms that are used by insurers is also ineffective. Insurance policies are contracts of adhesion drafted solely by insurers and then sold on a take-it-or-leave-it basis to the public, which is required to buy insurance to ensure that victims of auto accidents, for example, have a source of compensation.¹⁰ Yet, state insurance commissioners' approval

7. *State Farm*, 538 U.S. at 422; Macey & Miller, *supra* note 2, at 33.

8. See PETER J. KALIS ET AL., POLICYHOLDER'S GUIDE TO THE LAW OF INSURANCE COVERAGE § 26.03[B] (1st ed. 1997 & Supp. 2018) ("Insurance contracts are interpreted according to state law. Not surprisingly, the manner in which the courts of the various states address similar interpretive issues can vary widely from one state to the next. The different interpretations given the same standardized language from one state to the next can mean the difference between a covered and a non-covered claim."); Charles R. McGuire, *Regulation of the Insurance Industry after Hartford Fire Insurance v. California; The McCarran-Ferguson Act and Antitrust Policies*, 25 LOY. U. CHI. L.J. 303, 352 (1994) ("It is extremely difficult for the federal government to regulate the international aspects of the insurance industry under the antitrust laws. It is virtually impossible for the states to do so.").

9. See, e.g., 2 STEVEN PLITT ET AL., COUCH ON INSURANCE § 24:1 (December 2017 Update) ("In theory, the laws of two states cannot control the interpretation of a contract of insurance, and the choice of which jurisdiction's law will govern can have serious consequences for an insurance dispute."). The courts' inconsistent interpretation of the "sudden and accidental" pollution exclusion is a prime example of courts in various states interpreting identical policy language to mean different things. Compare *Hecla Mining Co. v. N.H. Ins. Co.*, 811 P.2d 1083, 1092 (Colo. 1991) ("Although 'sudden' can reasonably be defined to mean abrupt or immediate, it can also reasonably be defined to mean unexpected and unintended. Since the term 'sudden' is susceptible to more than one reasonable definition, the term is ambiguous, and we therefore construe the phrase 'sudden and accidental' against the insurer to mean unexpected and unintended."), with *Am. Motorists Ins. Co. v. ARTRA Grp., Inc.*, 659 A.2d 1295, 1308 (Md. 1995) ("[T]he language of such an exclusion provides coverage only for pollution which is both sudden and accidental. It does not apply to gradual pollution carried out on an ongoing basis during the course of business.").

10. See, e.g., 1 JEFFREY W. STEMPEL & ERIK S. KNUTESEN, ON INSURANCE COVERAGE § 4.06[B], 4-65 (4th ed. 2018) ("The typical insurance policy sale is marked by formality and routinization. Consequently, insurance policies almost always are both standardized contracts and contracts of adhesion . . ."); Michelle Boardman,

of policy forms is essentially a rubber stamp without a substantive review of the terms and coverage provided in the policies, and no one involved in the process is representing the interests of consumers.¹¹ Indeed, the review and approval of policy forms is a classic example of regulatory capture wherein the regulators are oftentimes advancing only the interests of the regulated parties—the insurers.¹²

States also cannot police insurer misconduct that occurs on a nationwide basis.¹³ The United States Supreme Court highlighted this problem in *State Farm Mutual Automobile Insurance Co. v. Campbell*,¹⁴ when the Court set aside a punitive damage award intended to punish an insurer for the insurer’s nationwide policy and practice of preying upon powerless con-

Insuring Understanding: The Tested Language Defense, 95 IOWA L. REV. 1075, 1091 (2010) (discussing the “hyperstandardization” of policies); James M. Fischer, *Why Are Insurance Contracts Subject to Special Rules of Interpretation?: Text Versus Context*, 24 ARIZ. ST. L.J. 995, 996 (1992) (“[T]here is little, if any, freedom to negotiate the standardized language of the insurance contract that determines the scope of coverage.”); Susan Randall, *Freedom of Contract in Insurance*, 14 CONN. INS. L.J. 107, 125 (2007) (“[I]n some lines of insurance, all insurance companies provide identical coverage on the same take-it-or-leave-it basis Forty-seven states and the District of Columbia require automobile liability insurance covering bodily injury and property damage in specified amounts.”); MARTIN F. GRACE ET AL., *CATASTROPHE INSURANCE: CONSUMER DEMAND, MARKETS AND REGULATION* 83 (2003) (“[H]omeowners insurance . . . is essentially mandatory”); EMMETT J. VAUGHAN & THERESE M. VAUGHAN, *FUNDAMENTALS OF RISK AND INSURANCE* 539–41 (8th ed. 1999) (conducting a fifty-state survey of the compulsory automobile liability insurance laws).

11. See, e.g., KENNETH S. ABRAHAM & DANIEL SCHWARCZ, *INSURANCE LAW AND REGULATION: CASES AND MATERIALS* 131, 143, 146 (6th ed. 2015); Kenneth S. Abraham, *Four Conceptions of Insurance*, 161 U. PA. L. REV. 653, 663 (2013); Eugene R. Anderson & James J. Fournier, *Why Courts Enforce Insurance Policyholders’ Objectively Reasonable Expectations of Insurance Coverage*, 5 CONN. INS. L.J. 335, 336, 402–05 (1998).

12. See, e.g., Susan Randall, *Insurance Regulation in the United States: Regulatory Federalism and the National Association of Insurance Commissioners*, 26 FLA. ST. U.L. REV. 625, 639, 676–78 (1999) (the insurance industry is a classic example of regulatory capture); Anderson & Fournier, *supra* note 11, at 336 (“Insurance industry control over state insurance regulators is notorious.”); Richard B. Stewart, *The Refinement of American Administrative Law*, 88 HARV. L. REV. 1669, 1713 (1975) (“It has become widely accepted, not only by public interest lawyers, but by academic critics, legislators, judges, and even by some agency members, that the comparative overrepresentation of regulated or client interests in the process of agency decision results in a persistent policy bias in favor of these interests. Such overrepresentation stems from both the structure of agency decisionmaking and from the difficulties inherent in organizing often diffuse classes of persons with opposing interests.”). George J. Stigler is generally recognized as the person who popularized the concept of regulatory capture through his article, George J. Stigler, *The Theory of Economic Regulation*, 2 BELL J. ECON. & MGMT. SCI. 3, 3–21 (1971).

13. See, e.g., *Huntington v. Attrill*, 146 U.S. 657, 669 (1892) (“Laws have no force of themselves beyond the jurisdiction of the State which enacts them, and can have extraterritorial effect only by the comity of other states.”).

14. 538 U.S. 408, 409 (2003) (disallowing punitive damages award that was based upon nationwide insurer misconduct).

sumers. Without the power to police insurers on a nationwide basis, insurers can and do misbehave with limited consequences.¹⁵

States also cannot mandate specific coverages under insurance policies on a nationwide basis.¹⁶ For example, some of the most common and devastating catastrophic perils are floods and landslides. Floods have caused more than \$240 billion in damage in the United States over the past thirty years, for an annual average of approximately \$8 billion, and landslides cause approximately \$3.5 billion in property damage per year.¹⁷ Insurers, however, currently refuse to cover these natural catastrophes under homeowners policies even though these are the very types of catastrophic risks for which people most need insurance.¹⁸ Developed countries throughout the world have recognized the need for individuals to have insurance for natural catastrophes and they either provide such coverage under government insurance programs or require private insurers to include such coverage in the policies they sell.¹⁹ Due to political pressures, however, it is unlikely that each of the fifty states in America will mandate that insurers cover these types of catastrophic risks without federal intervention, particularly in light of the fact the states have not done so thus far.

15. See generally JAY M. FEINMAN, *DELAY, DENY, DEFEND: WHY INSURANCE COMPANIES DON'T PAY CLAIMS AND WHAT YOU CAN DO ABOUT IT* (2010).

16. See e.g., *Huntington*, 146 U.S. at 669.

17. See NAT'L OCEANIC AND ATMOSPHERIC ADMIN.'S NAT'L WEATHER SERV., HYDROLOGIC INFORMATION CENTER—FLOOD LOSS DATA (2013), <http://www.nws.noaa.gov/hic/> [<https://perma.cc/US99-MS5V>]; U.S. GEOLOGICAL SURVEY, *LANDSLIDE TYPES AND PROCESSES* (2004); Rob Risley, Comment, *Landslide Peril and Homeowners' Insurance in California*, 40 UCLA L. REV. 1145, 1146–47 (1993); *Landslides in the United States Since 2007*, NAT'L GEOGRAPHIC (Apr. 23, 2014), <https://news.nationalgeographic.com/news/2014/04/140422-surveying-american-landslides-interactive/> [<https://perma.cc/CS4R-UB7J>].

18. See Warren Kriesel & Craig Landry, *Participation in the National Flood Insurance Program: An Empirical Analysis for Coastal Properties*, 71 J. RISK & INS. 405, 405 (2004) (discussing the exclusion of coverage for flooding); Sample Homeowners Policy, Section I—Exclusions, §§ A.2 and 3, reprinted in CHRISTOPHER C. FRENCH & ROBERT H. JERRY, II, *INSURANCE LAW AND PRACTICE* 608–09 (2018) (reproducing the landslide and flood exclusions in ISO's 2010 standard form homeowners policy); Brian Mattis, *Earth Movement Claims Under All Risk Insurance: The Rules Have Changed in California*, 31 SANTA CLARA L. REV. 29, 36 (1990) (citing State Farm Fire & Cas. Co.'s Homeowners Policy Special Form 3, p. 7, Form FP-7103); *Ins. Servs. Office, Inc., Causes of Loss—Special Form, Commercial Property Form CP 10 30 10 12 § B.1.b.2. and g., at 1*, reprinted in BRUCE J. HILLMAN, *COMMERCIAL PROPERTY* 411 (4th ed. 2009) (reproducing the landslide and flood exclusions contained in ISO's 2007 standard form commercial property policy).

19. See Christopher C. French, *Insuring Floods: The Most Common and Devastating Natural Catastrophes in America*, 60 VILL. L. REV. 53, 77–78 (2015) [hereinafter *Insuring Floods*] (discussing coverage for flooding in United Kingdom, France, and Belgium); Christopher C. French, *Insuring Landslides: America's Uninsured Natural Catastrophes*, 17 NEV. L.J. 63, 89–94 (2016) [hereinafter *Insuring Landslides*] (discussing coverage for landslides in New Zealand, France, Belgium, Norway, Romania, Switzerland, Iceland, and Australia).

One obvious solution to these problems would be to give Congress exclusive power to regulate the insurance industry because the federal government does not suffer from the jurisdictional problem that states do. Despite the superficial appeal of such a solution, it would be a mistake because exclusive federal regulation of the insurance industry becomes problematic when one considers Congress' record in the area of insurance regulation.

Congress' past efforts to regulate some areas of insurance, such as the Employee Retirement Income Security Act of 1974 (ERISA)²⁰ and the National Flood Insurance Program (NFIP),²¹ reveals that consumers receive less protection under federal law in these areas of insurance than they would receive under state law in many respects. For example, state law remedies allow for an award of compensatory or punitive damages for bad faith denials of coverage, but such remedies are preempted and eliminated under ERISA.²² Thus, an insured that is wrongfully denied coverage generally is awarded only the amount of the claim that was wrongfully denied under ERISA so there is no downside financial risk for employers to wrongfully deny insurance benefits to their employees.²³

20. Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended in scattered sections of 29 U.S.C. §§ 1001–1003).

21. National Flood Insurance Act of 1968, Pub. L. No. 90-448, 82 Stat. 572 (codified as amended at 42 U.S.C. §§ 4001–4131 (2018)).

22. See *Aetna Health Inc. v. Davila*, 542 U.S. 200, 204 (2004) (affirming the dismissal of state law claims regarding the allegedly improper denial of health insurance benefits); *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 47–48 (1987) (affirming the dismissal of state law claims for punitive damages for allegedly denying disability insurance benefits in bad faith). Many legal scholars have been critical of the Supreme Court's interpretation of ERISA in this regard. See, e.g., Daniel Fischel & John H. Langbein, *ERISA's Fundamental Contradiction: The Exclusive Benefit Rule*, 55 U. CHI. L. REV. 1105, 1107 (1988) (“[T]he mess in ERISA fiduciary law cannot be ameliorated until courts . . . recognize the multiplicity of interests that inhere in the modern pension and employee benefit trust.”); Russell Korobkin, *The Failed Jurisprudence of Managed Care, and How to Fix It: Reinterpreting ERISA Preemption*, 51 UCLA L. REV. 457, 460 (2003) (“[T]he Supreme Court, in interpreting ERISA, rather than Congress in drafting it, . . . is most responsible for the current confused and illogical state of managed care law.”); John H. Langbein, *What ERISA Means By “Equitable”: The Supreme Court's Trail of Error in Russell, Mertens, and Great-West*, 103 COLUM. L. REV. 1317, 1365 (2003) (“The Supreme Court needs to confess its error in ERISA remedy law, much as it has recently confronted its mishandling of ERISA preemption, and to realign ERISA remedy law with the trust remedial tradition that Congress intended”); David L. Shapiro, *Justice Ginsburg's First Decade: Some Thoughts About Her Contributions in the Fields of Procedure and Jurisdiction*, 104 COLUM. L. REV. 21, 23 (2004) (arguing that Justice Ginsburg's dissent in *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204 (2002) was correct in stating that Congress did not intend to limit plan beneficiary's remedies under ERISA as it has been interpreted by the Supreme Court's majority).

23. ERISA does give courts discretion to award prejudgment interest and attorneys' fees so an aggrieved insured at least has a chance of obtaining a financially neutral result due to an improper denial of coverage. See 29 U.S.C. § 1132(g).

Similarly, under the NFIP, the private insurers who sell NFIP policies and adjust flood claims are immune to liability for bad faith conduct.²⁴ And, under the federal government's guidance and control, the NFIP program has been insolvent for many years with a current debt of approximately \$23 billion and even deeper losses on the horizon due to Hurricane Florence.²⁵ Thus, neither ERISA nor the NFIP, as examples of federal regulation of insurance, inspire confidence that exclusive federal regulation of insurance would be preferable to state regulation.

Consequently, instead of either state or federal regulation of insurance, this Article proposes a new approach—dual regulation of the insurance industry. States would still control those aspects of insurance they currently regulate for which they have demonstrated competence and have jurisdictional authority, such as ensuring that premium rates in their states are not excessive. The Federal Insurance Office (FIO), an entity created in 2010 under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act),²⁶ would be given authority to regulate other areas of insurance on a national basis. The FIO could draft insurance policy forms to be used nationally. The FIO also could adopt the best existing state consumer protection insurance laws at the federal level as regulations and create new rules to govern foreign and multinational insurers.

In explaining why a dual regulatory approach is warranted at this time, this Article proceeds in four parts. Part I sets forth the history of insurance regulation in the United States, including the reasons why insurance is regulated, the passage of the McCarran-Ferguson Act, and the federal government's current involvement in some areas of insurance such as ERISA, the NFIP, and the Affordable Care Act. Part II discusses the emergence and dominance of multinational, global insurers since the 1990s. Part II also discusses new alternative risk transfer mechanisms that have become prevalent, such as catastrophe bonds and reinsurance, which have changed the way insurers do business. Part III expounds upon some of the existing problems with states serving as the primary regulators of insurance, such as the inconsistent state laws, the inability to meaningfully regulate multinational and foreign insurers, and the inability to regulate insurers on a nationwide basis. Part IV sets forth the novel proposal of a

24. See, e.g., *Wright v. Allstate Ins. Co.*, 500 F.3d 390, 393 (5th Cir. 2007) (no recovery of extra-contractual damages under NFIP); *Gallup v. Omaha Prop. & Cas. Ins. Co.*, 434 F.3d 341, 344–45 (5th Cir. 2005) (extra-contractual state-law claims are preempted by federal law under NFIP); Ernest B. Abbott, *Floods, Flood Insurance, Litigation, Politics—and Catastrophe: The National Flood Insurance Program*, 1 SEA GRANT L. & POL'Y J. 129, 144–45, 147–50 (2008); Adam F. Scales, *A Nation of Policyholders: Governmental and Market Failure in Flood Insurance*, 26 MISS. C.L. REV. 3, 33–34, 38 (2006).

25. See U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-17-317, HIGH-RISK SERIES: PROGRESS ON MANY HIGH-RISK AREAS, WHILE SUBSTANTIAL EFFORTS NEEDED ON OTHERS 619 (2017).

26. 31 U.S.C. § 313 (2018).

dual regulatory regime in which the FIO would become the lead federal regulatory agency responsible for some areas of insurance while states would continue to regulate other areas.

II. THE HISTORY OF INSURANCE REGULATION

A. *The Reasons Why the Insurance Industry Is Regulated*

Broadly defined, insurance is the transfer of risk from one party to another party in exchange for a monetary payment.²⁷ Most entities purchase insurance in order to avoid uncertain, but possible, losses in the future.²⁸ In essence, someone who purchases insurance incurs a relatively small certain loss through the payment of a premium in exchange for the promise by the other party that it will bear the risk of larger, uncertain future losses.²⁹

How to characterize insurance (e.g., as a contract, a product, etc.), and the principal purpose of insurance, has been the subject of some debate among scholars.³⁰ In one conception, insurance fulfills a public function as a social safety net by which risks are distributed from individuals to a larger group or community, often using private entities as intermediaries.³¹ Its role as a quasi-public utility is one of many reasons why the insurance industry is regulated.³²

A second reason the insurance industry is regulated is that, in today's world, people and businesses cannot effectively function without insurance. Indeed, several lines of insurance are mandatory. For example, in

27. See, e.g., J. David Cummins, *Should the Government Provide Insurance for Catastrophes?*, 88 FED. RES. BANK OF ST. LOUIS REV. 337, 342 (2006).

28. See, e.g., ROBERT H. JERRY, II & DOUGLAS R. RICHMOND, UNDERSTANDING INSURANCE LAW 10 (5th ed. 2012) (noting that people become more risk averse as the potential magnitude of loss increases).

29. See, e.g., JERRY & RICHMOND, *supra* note 28, at 11 (describing how risk averse people prefer to lose one dollar with certainty rather than take a one in ten thousand chance of losing ten thousand dollars); FEINMAN, *supra* note 15, at 14 (an entity that purchases insurance prefers to “exchange a small, certain loss to avoid” a larger, uncertain loss).

30. See, e.g., Abraham, *supra* note 11, at 657 (describing four different conceptions of insurance: (1) as a contract, (2) as a public utility/industry, (3) as a product, and (4) as a surrogate government for regulating policyholder behavior); Daniel Schwarcz, *A Products Liability Theory for the Judicial Regulation of Insurance Policies*, 48 WM. & MARY L. REV. 1389, 1397–1400 (2007) (treating insurance policies as products); Jeffrey W. Stempel, *The Insurance Policy as Social Instrument and Social Institution*, 51 WM. & MARY L. REV. 1489, 1495–1513 (2010) [hereinafter *The Insurance Policy as Social Instrument*] (emphasizing the socially significant role insurance plays in modern society); Jeffrey W. Stempel, *The Insurance Policy as Thing*, 44 TORT TRIAL & INS. PRAC. L.J. 813, 835 (2009) (analyzing insurance policies as “things”).

31. See, e.g., Abraham, *supra* note 11, at 668; Christopher C. French, *The Role of the Profit Imperative in Risk Management*, 17 U. PA. J. BUS. L. 1081, 1092–93 (2015); Stempel, *The Insurance Policy as Social Instrument*, *supra* note 30, at 1497.

32. See Abraham, *supra* note 11, at 668–70 (describing insurance's similarity to utilities prompting further regulation).

order to purchase a house with a mortgage, the buyer must have homeowners insurance adequate to cover the mortgage amount.³³ Auto insurance is also mandatory.³⁴ Workers' compensation insurance is required in every state except Texas.³⁵ In many business transactions, such as construction contracts, one party is required to maintain insurance to cover the project.³⁶ Besides the mandatory lines of insurance, natural disasters such as hurricanes, tornadoes, and floods impact millions of people and businesses in every state. Without insurance, each passing storm would present the risk of financial ruin and bankruptcy.

A third reason is because there is a delay between when policyholders purchase policies and when insurers' obligations to pay claims arise. Consequently, there is a need to ensure that insurers are still solvent when the time to pay claims arises. Indeed, ensuring the solvency of insurers is one of the principal focuses of insurance regulation.³⁷

A fourth reason is because insurance advances the public policy of ensuring that injured parties will be compensated.³⁸ Many injuries would go uncompensated in the absence of insurance because most people are judgment proof—i.e., they do not have the money or assets needed to pay for their liabilities.³⁹ Thus, in the absence of insurance, many injured

33. See Stempel, *The Insurance Policy as Social Instrument*, *supra* note 30, at 1497; French, *supra* note 31, at 1094.

34. See *supra* note 10.

35. See, e.g., TEX. LAB. CODE ANN. § 406.002(a) (West 2015) ("Except for public employers and as otherwise provided by law, an employer may elect to obtain workers' compensation insurance coverage."); ABRAHAM & SCHWARCZ, *supra* note 11, at 421 ("[W]orkers compensation is a no-fault substitute for employers' tort liability and is mandated in every state except Texas, where employers may opt-out, and about one-third of employers do so."); GEORGE E. REJDA, *PRINCIPLES OF RISK MANAGEMENT AND INSURANCE* 556 (9th ed. 2005) ("All states today have workers compensation laws.").

36. See, e.g., Stempel, *The Insurance Policy as Social Instrument*, *supra* note 30, at 1498–99.

37. See, e.g., Carlson, *supra* note 2, at 1138–39 ("[T]he primary [reason for insurer regulation] seems to be the need to preserve the solvency and stability of insurers."); Kimball & Boyce, *supra* note 2, at 547–48 (noting that the number of insurance companies in the 1800s went from 4000 to 1000 due to insurer insolvencies following catastrophic fire events); JERRY & RICHMOND, *supra* note 28, at 61 ("Insureds commonly invest substantial sums of money in insurance policies that promise . . . payments . . . for loss of property and harm to other interests. Consequently, the bankruptcy of an insurer can cause substantial hardship and suffering for insureds . . .").

38. See, e.g., JERRY & RICHMOND, *supra* note 28, at 924–25 (stating the purpose of mandatory auto insurance coverage is to ensure that victims of automobile accidents have access to funds to cover their losses).

39. See, e.g., Stephen G. Gilles, *The Judgment-Proof Society*, 63 WASH. & LEE L. REV. 603, 606 (2006) (explaining why judgments generally are uncollectible); Kyle D. Logue, *Solving the Judgment-Proof Problem*, 72 TEX. L. REV. 1375, 1375–76 (1994) (analyzing insurance as a potential solution to the judgment-proof problem); S. Shavell, *The Judgment Proof Problem*, 6 INT'L REV. L. & ECON. 45, 47–52 (1986) (discussing the problems created by judgment-proof individuals).

people would not be able to pay their medical bills and they could not recoup their lost income.

A fifth reason the insurance industry is regulated is because it is one of the largest industries in the world. The insurance premiums paid in the United States alone total approximately \$1.9 trillion.⁴⁰ The insurance industry now accounts for approximately 2.5% of the United States' gross domestic product and employs 2.5 million people.⁴¹ Yet, despite its importance, insurance is the only major industry that is not regulated on a plenary basis by the federal government.⁴²

A sixth reason the insurance industry is regulated is that consumers need protection from insurer overreach because of how insurance policies are created and sold.⁴³ The creation and sale of insurance policies is a reflection of a bygone era. Insurance policies typically are long, complex, standard form contracts of adhesion drafted by insurers using antiquated jargon and then sold on a take-it-or-leave-it basis.⁴⁴

There are, however, some advantages to using standardized policy forms. For example, they allow for the mass sales of policies without negotiations for each policy.⁴⁵ This reduces transaction costs and eliminates the need to negotiate regarding the policy language.⁴⁶ In addition, the actuarial data that is used to price premiums would be unreliable if standardized language were not used because the claims data would not be based upon the same coverages sold.⁴⁷ Having insurers use the same pol-

40. See RAYMOND A. GUENTER & ELISABETH DITOMASSI, *FUNDAMENTALS OF INSURANCE REGULATION: THE RULES AND RATIONALE* 1 (2017).

41. *Id.*

42. See, e.g., Macey & Miller, *supra* note 2, at 14; Anthony J. Alt, *Congress' Self-Inflicted Sisyphian Task: The Insurance Industry's Federal Antitrust Exemption and the Insurance Industry Competition Acts of 2007 and 2009*, 16 *CONN. INS. L.J.* 399, 426 (2010).

43. See, e.g., Christopher C. French, *Understanding Insurance Policies as Non-Contracts: An Alternative Approach to Drafting and Construing These Unique Financial Instruments*, 89 *TEMP. L. REV.* 535, 551 (2017).

44. See *supra* note 10.

45. See *RESTATEMENT (SECOND) OF CONTRACTS* § 211 cmt. a (AM. LAW INST. 1981); Sajida A. Mahdi, *Gateway to Arbitration: Issues of Contract Formation Under the U.C.C. and the Enforceability of Arbitration Clauses Included in Standard Form Contracts Shipped with Goods*, 96 *NW. U.L. REV.* 403, 403 (2001).

46. See *RESTATEMENT (SECOND) OF CONTRACTS* § 211 cmt. a and cmt. b (AM. LAW INST. 1981); Robert A. Hillman & Jeffrey J. Rachlinski, *Standard-Form Contracting in the Electronic Age*, 77 *N.Y.U. L. REV.* 429, 437–39 (2002); Mark A. Lemley, *Terms of Use*, 91 *MINN. L. REV.* 459, 465 (2006).

47. See Michelle E. Boardman, *Contra Proferentem: The Allure of Ambiguous Boilerplate*, 104 *MICH. L. REV.* 1105, 1116 (2006) (“[T]he cost of each clause becomes increasingly clear as actuarial data is collected and pooled.”); Macey & Miller, *supra* note 2, at 53 (“In the absence of form standardization, it would be difficult to compile an adequate statistical data base on which to base risk assessments.”).

icy forms also allows consumers to compare insurers based upon the price of the policy being sold.⁴⁸

Currently, either individual insurers or the Insurance Services Office, Inc. (ISO), a private company, drafts almost all of the standardized policy forms used in the United States.⁴⁹ Insurers pay fees for ISO membership, and, as members of ISO, insurers are entitled to use ISO's policy forms.⁵⁰ In addition, "[f]or each of its standard policy forms, ISO also supplies actuarial and rating information: it collects, aggregates, interprets, and distributes data on the premiums charged, claims filed and paid, and defense costs expended with respect to each form"⁵¹

The advantages of using standardized policy forms evaporate, however, if the policy forms created and used do not provide good insurance coverage for the purchasers of the policies. Consequently, one would expect that consumers would have a significant role in the drafting of the language and coverages set forth in insurance policies to ensure that the policies are good, but they actually do not have any role in the drafting or approval process.⁵² Indeed, the purchasers of insurance typically do not even get an opportunity to review the policy they are purchasing before payment is due. Instead, the purchaser gets a copy of the policy long after it has paid at least the initial premium for it.⁵³ To some extent, the timing of when the policy is provided to the purchaser is not that important, however, because policyholders rarely read the policies they do receive and they generally cannot understand the policies anyway due to policies' length and complexity.⁵⁴

As a result of these dynamics—incomprehensible policies created by a massive industry that are sold on a take-it-or-leave-it basis to the public who is legally required to buy the policies to ensure that injured parties are compensated—there is little debate that the insurance industry needs to

48. See Macey & Miller, *supra* note 2, at 18 (“[A]ccurate information cannot be developed—and consumers cannot easily comparison shop on the basis of price—unless firms in the industry have access to standardized forms.”).

49. ISO's membership is comprised of approximately 1,400 property and casualty insurers and “is the almost exclusive source of support services in this country for CGL [commercial general liability] insurance.” *Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 772 (1993). In fact, “most CGL insurance written in the United States is written on [ISO] forms.” *Id.*

50. See, e.g., ABRAHAM & SCHWARCZ, *supra* note 11, at 36–37.

51. See *Hartford Fire*, 509 U.S. at 772 (internal citations omitted).

52. See, e.g., French, *supra* note 43, at 548.

53. See, e.g., Boardman, *supra* note 47, at 1120; Randall, *supra* note 10, at 107; Michael B. Rappaport, *The Ambiguity Rule and Insurance Law: Why Insurance Contracts Should Not Be Construed Against the Drafter*, 30 GA. L. REV. 171, 174 (1995).

54. See, e.g., Abraham, *supra* note 11, at 660; Boardman, *supra* note 47, at 1120; Robert E. Keeton, *Insurance Law Rights at Variance with Policy Provisions*, 83 HARV. L. REV. 961, 968 (1970); Randall, *supra* note 10, at 107, 125; Rappaport, *supra* note 53, at 174.

be regulated.⁵⁵ The question then becomes, “Who should regulate the insurance industry?”

B. *State Regulation of Insurance between 1752 and 1944*

Like many aspects of American history, insurance in the United States can trace its roots to England. Lloyd’s of London was the first insurer of vessels and cargo in the late seventeenth century and, after the Great Fire of London in 1666, London insurers also began selling insurance that covered non-marine properties for fire losses.⁵⁶ The first U.S. insurance company was the “Philadelphia Contributorship for Insuring Houses from Loss by Fire,” which was established in Philadelphia in 1752 with Ben Franklin as one of its first directors.⁵⁷ Since its initial creation in the United States, the insurance industry has been principally regulated by the states, not the federal government.⁵⁸

Ironically, insurers have changed their position over the years regarding whether they prefer that the states or the federal government regulate their industry. State regulation of insurers initially was somewhat haphazard, with each state creating its own rules.⁵⁹ By the 1860s, insurers had grown weary of the patchwork regulation of insurance by the various states and they were urging Congress to create national standards for the insurance industry that were analogous to the ones created for financial institutions.⁶⁰

In an effort to remove states as the primary regulators of the insurance industry, several New York insurance companies created a test case designed to bring an end to state regulation. Paul, a Virginia resident, was appointed by the New York insurance companies to act as their agent.⁶¹ Paul applied for a Virginia insurance license, but he refused to comply with a Virginia law that required him to deposit bonds with the state treasurer.⁶² Paul was denied a license, but he nonetheless sold insurance to a Virginia resident.⁶³ As a result, he was charged and convicted of violating

55. Carlson, *supra* note 2, at 1138–39 (“Scholars have advanced several reasons why insurance should be regulated, but the primary one seems to be the need to preserve the solvency and stability of insurers.”); Alt, *supra* note 42, at 427 (“It is generally agreed that the purpose of antitrust laws is to promote the welfare and best interests of consumers. It is also widely held that entirely unregulated competition in the insurance industry is not an alternative.”); Schwarcz & Schwarcz, *supra* note 6, at 1580 (“The central goal of state insurance regulation is to protect consumers from various risks involved with purchasing insurance coverage.”).

56. *See, e.g.*, JERRY & RICHMOND, *supra* note 28, at 16–18.

57. FEINMAN, *supra* note 15, at 21.

58. *See* JERRY & RICHMOND, *supra* note 28, at 64–69.

59. *Id.* at 65.

60. *Id.*

61. *Paul v. Virginia*, 75 U.S. 168 (1868), *overruled in part by* *United States v. S.-E. Underwriters Ass’n*, 322 U.S. 533 (1944).

62. *Id.* at 169.

63. *Id.*

Virginia's licensing statute.⁶⁴ The Virginia Supreme Court affirmed Paul's conviction.⁶⁵ Paul appealed his conviction to the United States Supreme Court, arguing that Virginia's stricter requirements for foreign insurers violated the Privileges and Immunities Clause of the U.S. Constitution and that the federal commerce power bestowed exclusive power on the federal government to regulate insurers.⁶⁶

In 1869, the Supreme Court rejected Paul's arguments, which effectively terminated insurers' efforts to shift insurance regulation from states to the federal government.⁶⁷ In reaching its decision, the Court held that insurance was not interstate commerce subject to federal regulation under the Commerce Clause:

Issuing a policy of insurance is not a transaction of commerce. The policies are simple contracts of indemnity against loss by fire, entered into between the corporations and the assured, for a consideration paid by the latter. These contracts are not articles of commerce in any proper meaning of the word. They are not subjects of trade and barter offered in the market as something having an existence and value independent of the parties to them. They are not commodities to be shipped or forwarded from one State to another, and then put up for sale. They are like other personal contracts between parties which are completed by their signature and the transfer of the consideration. Such contracts are not inter-state transactions, though the parties may be domiciled in different States. The policies do not take effect—are not executed contracts—until delivered by the agent in Virginia. They are, then, local transactions, and are governed by the local law. They do not constitute a part of the commerce between the States any more than a contract for the purchase and sale of goods in Virginia by a citizen of New York whilst in Virginia would constitute a portion of such commerce.⁶⁸

The Supreme Court adhered to its ruling in *Paul* for the next seventy-five years, which meant the individual states continued to regulate insurance companies throughout that time period.

Things changed, however, in 1944. By then, insurers were content with state regulation of the insurance industry, but the federal government was not. Insurers had become cartels, controlling premium rates and boycotting insurance companies that refused to join their cartels.⁶⁹ States were not taking appropriate actions to stop insurers from engaging

64. *Id.*

65. *Id.*

66. *Id.* at 170.

67. *Id.* at 185.

68. *Id.* at 183.

69. *See* United States v. S.-E. Underwriters Ass'n, 322 U.S. 533, 535 (1944).

in these activities, so the federal government sued under the Sherman Act⁷⁰ to stop insurers' collusive, anti-competitive conduct.⁷¹

Specifically, the federal government indicted the South-Eastern Underwriters Association and its membership of nearly 200 fire insurance companies as well as twenty-seven individuals.⁷² The insurers who belonged to the association did business in Alabama, Florida, Georgia, North Carolina, South Carolina, and Virginia.⁷³ The association and its member insurers allegedly controlled 90% of the property insurance market in those states, fixed insurance premium rates at noncompetitive prices, and acted to prevent nonassociation insurers from doing business.⁷⁴ Their defense was that the Sherman Act did not apply to them pursuant to the Supreme Court's decision in *Paul*.⁷⁵

Although the lower courts agreed with the insurers, the Supreme Court did not. In a 4-3 decision, the Supreme Court overruled *Paul*. The Court held insurance was central to the conduct of business in the United States and did constitute commerce that was subject to Congressional regulation under the Commerce Clause:

The modern insurance business holds a commanding position in the trade and commerce of our Nation. Built upon the sale of contracts of indemnity, it has become one of the largest and most important branches of commerce. Its total assets [are] the approximate equivalent of the value of all farm lands and buildings in the United States. Its annual premium receipts exceed . . . the average annual revenue receipts of the United States Government during the last decade. Included in the labor force of insurance are . . . almost as many as seek their livings in coal mining or automobile manufacturing. Perhaps no modern commercial enterprise directly affects so many persons in all walks of life as does the insurance business. Insurance touches the home, the family, and the occupation or the business of almost every person in the United States.

This business is not separated into 48 distinct territorial compartments which function in isolation from each other. Interrelationship, interdependence, and integration of activities in all the states in which they operate are practical aspects of the insurance companies' methods of doing business.⁷⁶

70. Sherman Antitrust Act of 1890, 15 U.S.C. §§ 1-7 (2018).

71. *S.-E. Underwriters Ass'n*, 322 U.S. at 535

72. *Id.* at 534.

73. *Id.* at 535.

74. *Id.* at 535-36.

75. *Id.* at 536.

76. *Id.* at 539-41 (citations omitted).

Thus, beginning in 1944, the insurance industry became subject to federal regulation and federal antitrust laws.

This change in the regulatory regime was of great concern to both insurers and the states.⁷⁷ After *Paul*, insurers faced both lower profits and potential jail time for collusive, noncompetitive behavior, while states faced a loss of tax revenue.⁷⁸ And, of course, there would be a regulatory vacuum until Congress or its delegated authority created national insurance laws and regulations.⁷⁹

C. *The McCarran-Ferguson Act and State Regulation of Insurance Since 1945*

In response to the *S.-E. Underwriters Ass'n* decision, insurers and the states joined forces to attempt to get Congress to overrule the decision.⁸⁰ To that end, the National Association of Insurance Commissioners (NAIC), an association comprised of the leaders of state insurance departments, drafted a proposed statute that would return power to the states to regulate insurance.⁸¹ The primary concerns addressed by the draft legislation were the preservation of: 1) the state regulatory scheme and 2) states' ability to tax insurers.⁸² A secondary purpose of the proposed statute was the creation of an exemption from federal antitrust laws for insurers.⁸³ The principal argument in favor of allowing states to continue to regulate the insurance industry was that states were better situated to take into account local or regional considerations.⁸⁴

With some modification, Congress enacted the NAIC's proposal, which was sponsored by Senator Pat McCarran and Senator Homer Fergu-

77. See, e.g., Alt, *supra* note 42, at 414; Spencer L. Kimball & Barbara P. Heaney, *Emasculation of the McCarran-Ferguson Act: A Study in Judicial Activism*, 1985 UTAH L. REV. 1, 9 (1985).

78. See, e.g., Kimball & Heaney, *supra* note 77, at 9.

79. *Id.*

80. *Id.*

81. *Id.*

82. See *Prudential Ins. Co. v. Benjamin*, 328 U.S. 408, 429 (1946) ("Obviously Congress' purpose was broadly to give support to the existing and future state systems for regulating and taxing the business of insurance."); Carlson, *supra* note 2, at 1332-33 ("[B]oth the states and private insurance companies feared the implications of *South-Eastern*. The states were concerned about the validity of taxing and licensing laws from which they derived substantial revenue."); Kimball & Boyce, *supra* note 2, at 554 ("The most serious immediate danger to the states was that state insurance taxation might be invalidated as an undue burden on commerce.").

83. See *Grp. Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 218 (1979) ("A secondary concern [addressed in the McCarran-Ferguson Act] was the applicability of the antitrust laws to the insurance industry."); Carlson, *supra* note 2, at 1133 ("The [insurance] companies . . . were fearful of the Sherman Act's application to price fixing and other anticompetitive conduct in which they had engaged with impunity since *Paul*.").

84. See, e.g., Macey & Miller, *supra* note 2, at 86.

son, resulting in the statute now known as the McCarran-Ferguson Act.⁸⁵ The McCarran-Ferguson Act provides:

§1. Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

§2. (a) State regulation. The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) Federal regulation. No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended [15 U.S.C.A. 41 *et seq.*], shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

§3 . . . (b) Nothing contained in this Act shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

§4. Nothing contained in this Act [15 U.S.C.A. 1011 *et seq.*] shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935, as amended, known as the National Labor Relations Act [29 U.S.C.A. 151 *et seq.*], or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938 [29 U.S.C.A. 201 *et seq.*], or the Act of June 5, 1920, known as the Merchant Marine Act, 1920.⁸⁶

In short, states had three years in which to pass statutes that regulated the “business of insurance” and, if passed, insurers would then be exempt from federal antitrust statutes. Insurers would not, however, be exempt from federal antitrust statutes with respect to any “agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.” In addition, the statute expressly provided that the National Labor Relations Act, the Fair Labor Standards Act, and the Merchant Marine Act still applied to the insurance industry. Finally, Congress remained free to regu-

85. See, e.g., Kimball & Heaney, *supra* note 77, at 9 (“The National Association of Insurance Commissioners (or ‘NAIC’) draft bill, with only modest changes, became the McCarran-Ferguson Act.”).

86. McCarran-Ferguson Act, 15 U.S.C. §§ 1011–1015 (2018).

late the “business of insurance” by passing other statutes so long as the statutes were clear that Congress intended the statutes to apply to the business of insurance.

Following the passage of the McCarran-Ferguson Act, the states, again through the NAIC, immediately began creating model insurance statutes for adoption. The model statutes primarily addressed four areas: 1) rate regulation, 2) insurer solvency, 3) policy form approval, and 4) unfair trade practices. Every state eventually adopted some form of the NAIC’s model acts.⁸⁷

In general, the rate regulation statutes provide that insurance rates should not be “excessive, inadequate, or unfairly discriminatory.”⁸⁸ The solvency statutes generally impose capital and reserve requirements on insurers, dictate the types of investments insurers can make, and specify the accounting practices insurers should use to ensure that insurers’ financial reporting provides a clear picture of the insurers’ financial health.⁸⁹ The policy form approval statutes empower state insurance commissioners to review and approve policy forms. In doing so, they can reject terms that are “unfair,” “ambiguous,” “unreasonable,” and/or “contrary to public policy.”⁹⁰ The unfair trade practices statutes generally empower the state insurance commissioners to investigate and take action against insurers for, among other things, misrepresentations, false advertising, unfair claims handling practices, and unfair discrimination.⁹¹

Primarily due to antitrust concerns regarding the insurance industry’s collusive behavior concerning the sharing of policy forms, pooling of claims data, and policy pricing, there have been numerous efforts since 1945 to repeal the McCarran-Ferguson Act and eliminate states’ dominance regarding the regulation of the insurance industry.⁹² To date, all such attempts have failed.

87. See Carlson, *supra* note 2, at 1137 (“By 1951 every state had enacted rate regulatory laws, most of them substantially similar to the model bills . . . By 1963 all the states had passed statutes based on [the model Unfair Trade Practices bill.]”).

88. See, e.g., FRENCH & JERRY, *supra* note 18, at 796–97.

89. *Id.* at 792–93; GUENTER & DITOMASSI, *supra* note 40, at 21 (“Among the regulatory techniques employed are minimum capital requirements, restrictions on investments, maintenance of reserves against losses and other policy obligations, the filing of financial statements, and on-site financial examinations.”).

90. See, e.g., ALA. CODE § 27–14–9 (2016); GA. CODE ANN. § 33–24–10 (2016); NEB. REV. STAT. § 44–7513 (2016).

91. See, e.g., FRENCH & JERRY, *supra* note 18, at 793–94; Carlson, *supra* note 2, at 1137; ABRAHAM & SCHWARCZ, *supra* note 11, at 147.

92. See, e.g., Health Insurance Industry Antitrust Enforcement Act of 2013, H.R. 99, 113th Cong. (2013) (eliminating most of the exemptions under the McCarran-Ferguson Act for the insurance industry); S. 430, 102d Cong. (1st Sess. 1991) (modifying the antitrust exemption applicable to insurance industry); H.R. 10, 102d Cong. (1st Sess. 1991) (same); S. 719, 101st Cong. (1st Sess. 1989) (same); S. 1299, 100th Cong. (1st Sess. 1987) (same); S. 804, 100th Cong. (1st Sess. 1987) (proposing Insurance Competition Act of 1987 which would eliminate federal deference to the McCarran-Ferguson Act); S. 80, 100th Cong. (1st Sess. 1987)

D. *The Supreme Court's Limitation of the Scope of Exclusive State Regulation under the McCarran-Ferguson Act*

On its face, the McCarran-Ferguson Act appears to be a broad grant of regulatory authority to the states over insurance matters. As interpreted by the United States Supreme Court, however, that delegation of authority is somewhat limited. Through a series of decisions issued between 1979 and 1993, the Supreme Court has narrowly interpreted the reverse preemptive effect of state insurance laws on federal laws that indirectly regulate the insurance industry.⁹³ The Court did so by narrowly interpreting the phrase “business of insurance” and broadly interpreting the term “boycott” used in the McCarran-Ferguson Act.

First, in 1979, in *Group Life & Insurance Co. v. Royal Drug Co.*,⁹⁴ the Court held that agreements between health insurers and pharmacies that limited the cost of the prescription drugs did not qualify for antitrust exemption under the McCarran-Ferguson Act because the agreements were not part of the “business of insurance.” According to the Court, the phrase “business of insurance,” which was undefined in the McCarran-Ferguson Act, does not mean the same thing as the “business of insurers.”⁹⁵ The Court’s review of the legislative history of the McCarran-Ferguson Act revealed that the business of insurance was understood by Congress to involve the underwriting of risk as well as the relationship and transactions between insurers and their policyholders.⁹⁶ There was no legislative intent to exempt agreements or transactions between insurance companies and entities outside the insurance industry.⁹⁷ Because the agreements with the pharmacies did not have the effect of spreading risk, they were not exempt from antitrust scrutiny under federal laws.⁹⁸ To the contrary, the agreements merely saved the insureds money and enhanced the insurers’ profits.⁹⁹

Second, in 1982, in *Union Labor Life Insurance Co. v. Pireno*,¹⁰⁰ the Court held that insurers’ use of outside chiropractors to review the reason-

(proposing repeal of the McCarran-Ferguson Act); The McCarran-Ferguson Act—State Antitrust Action Against Insurance Agencies: Hearings on S. 1299 Before the Senate Comm. on the Judiciary, 100th Cong. (2d Sess. 1988); To Repeal or Revise the McCarran-Ferguson Act: Hearings on S. 80 and S. 1299 Before the Senate Comm. on the Judiciary, 100th Cong. (1st Sess. 1987); see also Alt, *supra* note 42, at 401–02 (discussing repeal efforts from 1977 to 2010); McGuire, *supra* note 8, at 321 (discussing repeal efforts in the 1990s).

93. See, e.g., Kimball & Heaney, *supra* note 77, at 11–29 (discussing the Supreme Court decisions that restricted the scope of the reverse preemption of the McCarran-Ferguson Act).

94. 440 U.S. 205 (1979).

95. See *id.* at 211.

96. *Id.*

97. *Id.* at 216, 224.

98. *Id.* at 213–14.

99. *Id.*

100. 458 U.S. 119 (1982).

ableness of bills submitted by chiropractors for payment did not constitute the business of insurance; thus, such practices were not exempt from federal antitrust scrutiny.¹⁰¹ The Court reiterated its commitment to the three-prong test it first used in *Royal Drug* to determine whether a practice is part of the business of insurance:

Royal Drug identified three criteria relevant in determining whether a particular practice is part of the “business of insurance” exempted from the antitrust laws by § 2(b): *first*, whether the practice has the effect of transferring or spreading a policyholder’s risk; *second*, whether the practice is an integral part of the policy relationship between the insurer and the insured; and *third*, whether the practice is limited to entities within the insurance industry. None of these criteria is necessarily determinative in itself.¹⁰²

In applying that test, the Court concluded the practice of reviewing the chiropractors’ bills was not related to the spreading of risk, was not integral to the insurer-policyholder relationship, and was not limited to entities within the insurance industry because chiropractors are outside the industry.¹⁰³ Thus, the practice was not part of the business of insurance and consequently, it was subject to federal laws.¹⁰⁴

Third, in 1993, in *Hartford Fire Insurance Co. v. California*,¹⁰⁵ the Court took a relatively expansive view of the meaning of the term “boycott” that is used in the McCarran-Ferguson Act. In the *Hartford* case, nineteen states and numerous private parties sued a group of insurance companies that allegedly conspired to force all primary insurance companies to sell only “claims-made” general liability policies and to make other changes to the general liability policy form that traditionally had been sold by insurers.¹⁰⁶ In deciding whether the insurers’ alleged behavior constituted an illegal boycott under the McCarran-Ferguson Act, which would mean the conduct was subject to scrutiny under federal antitrust laws, the Court reasoned it could constitute an illegal boycott because it was a threat “to withhold, wholly or in part, social or business intercourse from, as . . . means of coercion.”¹⁰⁷ Thus, the Court essentially interpreted the boycott exception to the reverse state law preemption provisions of the McCarran-Ferguson Act to mean concerted behavior by entities regarding one business activity that was intended to coerce a party to agree to another business activity.

101. *Id.* at 134.

102. *Id.* at 129.

103. *Id.* at 130–32.

104. *Id.*

105. 509 U.S. 764 (1993).

106. *Id.* at 770–72.

107. *Id.* at 801 (quoting WEBSTER’S NEW INTERNATIONAL DICTIONARY 321 (2d ed. 1950)).

In sum, the scope of the reverse preemption provision of the McCarran-Ferguson Act is fairly narrow under the *Royal Drug*, *Union Labor*, and *Hartford* cases. Consequently, as the McCarran-Ferguson Act has been interpreted, the power of states to displace federal statutes that indirectly regulate insurer behavior is limited.

E. *The Federal Government's Direct Regulation of Certain Areas of Insurance Since 1945*

Although the power to regulate the business of insurance was delegated to the states under the McCarran-Ferguson Act, Congress has had the authority to regulate insurance whenever it chooses to do so since *S.-E. Underwriters Ass'n* was decided in 1944. Congress has exercised that power in a few areas of insurance such as Medicaid and Medicare health insurance;¹⁰⁸ Social Security disability insurance;¹⁰⁹ terrorism insurance;¹¹⁰ employment insurance benefits (ERISA);¹¹¹ flood insurance (NFIP);¹¹² and health insurance for the uninsured (Affordable Care Act).¹¹³

Although all of these areas are worthy of discussion, to illustrate the pros and cons of federal regulation of insurance based upon Congress' record, this Article will focus upon the last three areas identified above: ERISA, the NFIP, and the Affordable Care Act.

1. *ERISA*

Many types of insurance, such as health insurance, life insurance, and disability insurance, are provided by employers to their employees as fringe benefits. There are a number of reasons employers provide these types of insurance to their employees. One, employer-provided insurance generally is not considered taxable income of the employees.¹¹⁴ Two, any portion of the premium paid by an employee generally can also be used by the employee to offset taxable income.¹¹⁵ Three, group insurance minimizes insurer concerns regarding adverse selection because a larger pool of people being insured decreases the chances that the insurer will only be

108. Health Insurance for Aged and Disabled, 42 U.S.C. § 1395 (2018).

109. 42 U.S.C. § 401 (2018).

110. Terrorism Risk Insurance Act, 107 P.L. 297, 116 Stat. 2322 (2002).

111. Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended in scattered sections of 29 U.S.C.).

112. National Flood Insurance Act of 1968, Pub. L. No. 90-448, 82 Stat. 572 (codified as amended at 42 U.S.C. §§ 4001-4131 (2018)).

113. Patient Protection and Affordable Care Act of 2010 (Affordable Care Act), Pub. L. No. 111-148, 124 Stat. 119-1025 (codified as amended in scattered sections of the U.S. Code).

114. See FRENCH & JERRY, *supra* note 18, at 826.

115. *Id.*

covering high risk insureds.¹¹⁶ Four, good fringe benefits can be used to attract better workers and increase worker satisfaction and loyalty.¹¹⁷

ERISA was passed following several high profile pension plan defaults and it primarily was intended to address pension plans.¹¹⁸ ERISA, however, also comprehensively regulates employee welfare benefit plans that, “through the purchase of insurance or otherwise,” provide benefits to employees and their beneficiaries in the event of sickness, accident, disability, or death.¹¹⁹ According to Congress, ERISA’s purpose is to “protect . . . participants in employee benefit plans and their beneficiaries, . . . by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing for appropriate remedies, sanctions, and ready access to the Federal courts.”¹²⁰ ERISA expressly provides that it “shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan. . . .”¹²¹ Consequently, ERISA is an example of where Congress expressly intended to regulate an area of insurance, despite the McCarran-Ferguson Act’s preservation of states’ rights to regulate the business of insurance.

In light of Congress’ goal of “protecting” benefit plan participants, as it has been interpreted by the United States Supreme Court, ERISA has fallen short of that goal in many respects. For example, state law remedies that allow for an award of compensatory or punitive damages for bad faith denials of coverage have been preempted and are eliminated under ERISA.¹²² Thus, an insured that is wrongfully denied coverage generally is awarded only the amount of the claim that was wrongfully denied, so there is no downside financial risk under ERISA for employers to wrongfully deny insurance benefits to their employees.¹²³

116. *Id.* Adverse selection is “the disproportionate tendency of those who are more likely to suffer losses to seek insurance against those losses.” Kenneth S. Abraham & Lance Liebman, *Private Insurance, Social Insurance, and Tort Reform: Toward a New Vision of Compensation for Illness and Injury*, 93 COLUM. L. REV. 75, 102 n.82 (1993); see also Peter Siegelman, *Adverse Selection in Insurance Markets: An Exaggerated Threat*, 113 YALE L.J. 1223, 1223 (2004) (arguing that insurers’ alleged concerns regarding the actual impact that adverse selection has on policyholders’ behavior are overblown).

117. See FRENCH & JERRY, *supra* note 18, at 826.

118. See, e.g., Brendan S. Maher & Peter K. Stris, *ERISA & Uncertainty*, 88 WASH. U.L. REV. 433, 440 n.29 (2010) (“Few dispute that the statute was passed, in part, as a response to several high-profile pension defaults that arose from company failures that devastated the pensions of many workers.”); Langbein, *supra* note 22, at 1322 (“ERISA was primarily designed to protect pension plan participants and beneficiaries against two hazards, default risk and administration risk, that had revealed themselves in pre-ERISA practice.”).

119. 29 U.S.C. § 1002(1) (2018).

120. 29 U.S.C. § 1001(b).

121. 29 U.S.C. § 1144(a).

122. See *supra* note 22.

123. See *supra* notes 22 and 23.

The fact that the United States Supreme Court has concluded the remedies available under ERISA provide less protection than state law suggests Congress may not be competent to enact insurance legislation if Congress intended ERISA to provide employees with greater protections than they had under state law but it does not as drafted.¹²⁴ Stated differently, why would Congress pass a statute it intended to increase protections for plan beneficiaries but actually provides the beneficiaries with fewer remedies for denials of benefits than they previously had under state law?¹²⁵

Another area in which ERISA is less favorable to consumers than state law is the rules that apply to the interpretation of insurance benefits plans. *Contra proferentem*¹²⁶ and the reasonable expectations doctrine,¹²⁷ which are interpretive rules that favor insureds and are used by the courts when interpreting insurance policies under state law, do not apply under ERISA.¹²⁸

124. See, e.g., Langbein, *supra* note 22, at 1332 (“Dissenting in *Mertens*, Justice White lamented ‘the anomaly of interpreting ERISA so as to leave those Congress set out to protect—the participants in ERISA-governed plans and their beneficiaries—with “less protection . . . than they enjoyed before ERISA was enacted.””).

125. One explanation that has been advanced by one scholar is that the Court was afraid that allowing extra contractual liabilities to be imposed on employers under ERISA would discourage employers from offering employee benefit plans. See Maher & Stris, *supra* note 118, at 445, 451 (“Congress wished to make benefit promises more secure, but not so costly as to result in appreciably fewer or less generous benefit promises being made overall.”).

126. See, e.g., Crane v. State Farm Fire & Cas. Co., 485 P.2d 1129, 1130 (Cal. 1971) (“Any ambiguity or uncertainty in an insurance policy is to be resolved against the insurer.”); RPM Pizza, Inc. v. Auto. Cas. Ins. Co., 601 So.2d 1366, 1369 (La. 1992) (“[A]ny ambiguity must be construed against the insurance company and in favor of the reasonable construction that affords coverage.”); Ohio Cas. Ins. Co. v. Flanagan, 210 A.2d 221, 226 (N.J. 1965) (“If the controlling language will support two meanings, one favorable to the insurer, and the other favorable to the insured, the interpretation sustaining coverage must be applied.” (quoting Mazzilli v. Accident & Cas. Ins. Co. of Winterthur, 170 A.2d 800, 803 (N.J. 1961))).

127. See, e.g., ROBERT E. KEETON, ALAN I. WIDDISS & JAMES M. FISCHER, INSURANCE LAW: A GUIDE TO FUNDAMENTAL PRINCIPLES, LEGAL DOCTRINES, AND COMMERCIAL PRACTICES § 6.3(a)(5), at 538 (2d ed. 2017) (“In some circumstances, the scope of coverage should be predicated on the reasonable expectations of an insured even though an insurance policy includes an explicit and unambiguous limitation that could have been discovered by an insured”); Nat’l Mut. Ins. Co. v. McMahon & Sons, Inc., 356 S.E.2d 488, 495–96 (W. Va. 1987) (the reasonable expectations doctrine provides that the policy should be construed in a manner that a reasonable person standing in the shoes of the insured would expect the language to mean, even though painstaking examination of the policy provisions would have negated those expectations).

128. ABRAHAM & SCHWARCZ, *supra* note 11, at 396 (“Application of this abuse of discretion standard effectively reverses the normal *contra proferentem* rule when it comes to judicial review of coverage claims, creating a presumption against coverage when the relevant policy language is ambiguous and coverage under a group policy has been denied.”); FRENCH & JERRY, *supra* note 18, at 847 (“The effect of the abuse of discretion standard of review is that *contra proferentem* and the reasonable expectations doctrine effectively do not apply to the construction of policy language.”).

In addition, under state law, the interpretation of a policy is a question of law that is reviewed *de novo* by appellate courts.¹²⁹ In contrast, under ERISA, if the insurance benefits plan reserves discretion to the claims administrator to determine coverage under the insurance policy, then courts review coverage determinations under an abuse of discretion standard.¹³⁰ In practice, because almost all insurance benefits plans reserve discretion to make coverage determinations to the claims administrator, the deferential standard of review almost always governs.¹³¹

Additionally, under ERISA, an insured must exhaust all internal review processes that the insurance benefits plan provides before an insured can even seek judicial review of a denial of coverage.¹³² Consequently, the review process can be more cumbersome and time consuming. And, finally, unlike under state law, jury trials are not available to insureds for denial of coverage claims under ERISA.¹³³

In sum, even though ERISA was originally passed with the intention of increasing consumer protections with respect to insurance benefits, as worded and interpreted by the Supreme Court, insureds actually have more protection under state law than they do under ERISA. Nonetheless, Congress has declined to amend ERISA to address this problem.

2. *NFIP*

The NFIP is another area of insurance law that Congress has expressly chosen to regulate. Flooding is the most common natural disaster in the United States and the world, causing approximately 90% of all catastrophic losses annually.¹³⁴ In the thirty years preceding 2009, flooding caused approximately \$240 billion in damage in the United States, for an

129. *See, e.g.*, *Sonson v. United Servs. Auto. Ass'n*, 100 A.3d 1, 2, 5 (Conn. App. Ct. 2014) (“Standardized contracts of insurance continue to be prime examples of contracts of adhesion The interpretation of a contract presents a question of law subject to *de novo* review.”).

130. *See, e.g.*, *Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101, 115 (1989). Scholars also have been critical of the deferential judicial review given to denial of benefit determinations under ERISA. *See, e.g.*, Brendan S. Maher, *Creating a Paternalistic Market for Legal Rules Affecting the Benefit Promise*, 2009 WIS. L. REV. 657, 679 (2009) (“[T]here is a procedural system likely to promote fair and accurate review: *de novo* review. Aside from the obvious merit of itself being ‘fair and accurate,’ *de novo* review has the additional benefit of consonance with ERISA’s language.”).

131. *See, e.g.*, Maher & Stris, *supra* note 118, at 472.

132. *See, e.g.*, *Davenport v. Harry N. Abrams, Inc.*, 249 F.3d 130, 133 (2d Cir. 2001).

133. *See, e.g.*, *Muller v. First Unum Life Ins. Co.*, 341 F.3d 119, 124 (2d Cir. 2003).

134. *See* Shannon Doocy, Amy Daniels, Sarah Murray & Thomas D. Kirsch, *The Human Impact of Floods: A Historical Review of Events 1980–2009 and Systematic Literature Review*, PLOS CURRENT DISASTERS (Apr. 16, 2013), <http://currents.plos.org/disasters/index.html%3Fp=6695.html> [<https://perma.cc/4BWN-XJ84>] (discussing impacts of flooding).

annual average of approximately \$8 billion.¹³⁵ Three major storms since 2005—Hurricane Katrina, Superstorm Sandy, and Hurricane Harvey—alone caused over \$280 billion in damage.¹³⁶

By the 1960s, most insurers had decided that insuring flood losses was not a risk they were willing to underwrite. Consequently, since then insurers almost uniformly have refused to insure flood losses under homeowners insurance policies.¹³⁷

As a result of insurers' refusal to cover flood losses, the NFIP was created by Congress under the National Flood Insurance Act of 1968 to fill the void.¹³⁸ A secondary reason the NFIP was created was to recoup some of the monies the federal government was spending on flood relief efforts by attempting to get the people who were most likely to be flood victims to pay premiums to help offset some of the government's post-disaster relief costs.¹³⁹

Many of the major flooding events have exposed the deficiencies in the NFIP. For example, the program has been insolvent on and off for decades.¹⁴⁰ The program is currently insolvent in the approximate amount of \$23 billion.¹⁴¹

The NFIP is actuarially unsound by design. It intentionally has been charging subsidized premium rates for old homes grandfathered into the program for decades, which is one of the reasons for the periodic insolvency of the program.¹⁴²

135. See NAT'L OCEANIC AND ATMOSPHERIC ADMIN.'S NAT'L WEATHER SERV., *supra* note 17.

136. See Harriett Torry & Sarah Chaney, *Big Storm Leaves Small Mark on the U.S. Economy*, WALL ST. J. (Sept. 15, 2018), <https://www.wsj.com/amp/articles/big-storms-leave-small-marks-on-the-u-s-economy-1537027200> [<https://perma.cc/WN78-GPPX>]; Christopher C. French, *The Aftermath of Catastrophes: Valuing Business Interruption Insurance Losses*, 30 GA. ST. U.L. REV. 461, 463 (2014) (Hurricane Sandy caused over \$60 billion in damage); Christine A. Klein & Sandra B. Zellmer, *Mississippi River Stories: Lessons from a Century of Unnatural Disasters*, 60 SMU L. REV. 1471, 1499 (2007) (Hurricane Katrina caused approximately \$100 billion in damage).

137. See Kriesel & Landry, *supra* note 18, at 405. There are some insurers, however, that are willing to provide flood coverage under commercial property policies. See, e.g., *Penford Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 662 F.3d 497 (8th Cir. 2011) (litigating the issue of whether an "all risk" commercial property policy provided \$50 million or \$20 million in coverage for flood losses).

138. See National Flood Insurance Act of 1968, Pub. L. No. 90-448, 82 Stat. 572 (codified as amended at 42 U.S.C. §§ 4001–4131 (2018)).

139. See U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-14-297R, OVERVIEW OF GAO'S PAST WORK ON THE NATIONAL FLOOD INSURANCE PROGRAM 3 (2014), <http://www.gao.gov/products/GAO-14-297R>; Klein & Zellmer, *supra* note 136, at 1490 (citing Rutherford H. Platt, *Review of Sharing the Challenge: Floodplain Management into the 21st Century*, ENV'T 25 (Jan.–Feb. 1995)) ("[The NFIP] was also intended to defray the after-the-fact expense of federal disaster relief by encouraging floodplain occupants to pay premiums before disaster struck.")

140. See 42 U.S.C. § 4012a(b)(4)(B); Abbott, *supra* note 24, at 129–30.

141. See *supra* note 25.

142. See U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-14-297R, OVERVIEW OF PAST WORK, *supra* note 139, at 4.

In addition, the claims handlers under the NFIP have conflicts of interest. The NFIP is currently administered by the Federal Emergency Management Agency (FEMA), which uses private insurance companies to: 1) sell the NFIP policies on behalf of FEMA¹⁴³ in exchange for a 30% sales commission, and 2) handle flood claims when they arise for additional claims handling fees.¹⁴⁴ These private insurers also sell homeowners insurance that excludes coverage for flood damage.¹⁴⁵ Consequently, when property damage is caused by a hurricane, there often is an issue of whether the damage was caused by flooding or the high winds. The private insurers that are handling the homeowners' claims have a financial incentive to characterize the damage as flood damage, as opposed to wind damage, in order to push the loss onto the federal government.¹⁴⁶ Indeed, one insurer's practices in this regard resulted in a whistle-blower lawsuit being filed against the insurer following Hurricane Katrina because the insurer instructed its claims handlers to characterize hurricane losses as flood losses.¹⁴⁷ The case made its way to the Supreme Court, which affirmed a \$3.7 million verdict in favor of the whistle-blowers.¹⁴⁸

The actual insurance coverage provided to consumers under NFIP policies is also poor. The maximum amount of NFIP coverage available for a residential property is only \$250,000 for the building itself and \$100,000 for personal property.¹⁴⁹ Coverage for basements, which is defined as any spaces below ground level, is limited to things like fuel tanks, furnaces, and water heaters.¹⁵⁰ That means a lot of items routinely found in basements are not covered. NFIP policies also do not cover property that is located outside of the house—e.g., landscaping, septic systems, decks, patios, fences, hot tubs, and swimming pools.¹⁵¹

In valuing losses, unlike “replacement cost” policies that pay the actual cost needed to rebuild the home or “valued” policies that pay the full limit of the policy in the event of a total loss, the policyholder receives the *lesser* of the replacement cost or actual cash value (i.e., the depreciated value) of damaged items under NFIP policies.¹⁵² A displaced homeowner

143. Scales, *supra* note 24, at 13–14.

144. See 42 U.S.C. § 4012a; see also Scales, *supra* note 24, at 14.

145. See Christopher C. French, *Hurricanes, Fraud and Insurance: The Supreme Court Weighs in but Does Not Wade Into the Concurrent Causation Conundrum in State Farm Fire and Casualty Company v. Rigsby*, 165 U. PA. L. REV. ONLINE 99, 100 (2017).

146. *Id.* at 101 (discussing the problem as it arose in the context of *State Farm Fire and Casualty Company v. United States ex rel. Rigsby*, 137 S. Ct. 436 (2016)).

147. *Id.*

148. *Rigsby*, 137 S. Ct. at 444–45.

149. See 42 U.S.C. § 4013(b)(2)–(3) (2018); U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-14-297R, OVERVIEW OF PAST WORK, *supra* note 139, at 3.

150. See FEDERAL EMERGENCY MANAGEMENT AGENCY, FEMA F-679, NATIONAL FLOOD INSURANCE PROGRAM: SUMMARY OF COVERAGE 3 (2012).

151. See *id.* at 2.

152. See *id.* at 4.

also does not have coverage for the cost of temporary housing under NFIP policies.¹⁵³

There also are more pitfalls to getting covered claims paid under the NFIP than there are under state law. For example, under the NFIP, the policyholder must prepare and submit a “proof of loss” form within sixty days that includes, among other things, bills, receipts, and related documents.¹⁵⁴ Unlike under state law, if the policyholder fails to strictly comply with the proof of loss requirements or fails to bring a lawsuit within a year in accordance with the terms of an NFIP policy, then coverage is forfeited under the NFIP.¹⁵⁵ Also, unlike under state law, FEMA and the private insurers who sell NFIP policies and then adjust the claims on FEMA’s behalf are immune from liability for underpaying claims or acting in bad faith.¹⁵⁶

The NFIP also historically has used outdated floodplain maps due to a lack of funds needed to create accurate ones, so in many instances homes that are located in high risk flood areas have not been insured.¹⁵⁷ For example, the flood map for the New York City area that was being used at the time of Superstorm Sandy was based upon data and modeling that was over thirty years old.¹⁵⁸ The new version of the map for the New York City area that was released in June 2013 essentially doubled the number of houses that are located in high-risk flood zones (i.e., the 100-year floodplain).¹⁵⁹ In sum, if the NFIP is representative of what one can expect from the federal government in the area of insurance regulation, then it is hard to argue that it should have a larger role in the regulation of insurance.

3. *Affordable Care Act*

The Affordable Care Act is one of the federal government’s most recent regulatory efforts in the area of insurance. In fact, it is the federal government’s first significant regulatory effort in the area of health insurance since the Health Insurance Portability and Accountability Act of

153. *See id.* at 2.

154. *See* FEDERAL EMERGENCY MANAGEMENT AGENCY, F-122, DWELLING FORM: STANDARD FLOOD INSURANCE POLICY § VII.J. 3–4 (2015), https://www.fema.gov/media-library-data/1449522308118-6752c210f65aed326a9ddf4a0ddaca1f/F-122_Dwelling_SFIP_102015.pdf [<https://perma.cc/ZYU3-T26V>].

155. *See, e.g.*, *Shuford v. Fid. Nat’l Prop. & Cas. Ins. Co.*, 508 F.3d 1337, 1342 (11th Cir. 2007).

156. *See supra* note 24.

157. *See* Cummins, *supra* note 27, at 358; Beth A. Dickhaus & Darrin N. Sacks, *Recent Developments in Insurance Regulation*, 42 TORT TRIAL & INS. PRAC. L.J. 571, 582 (2007); U.S. GOV’T ACCOUNTABILITY OFFICE, GAO-14-297R, OVERVIEW OF PAST WORK, *supra* note 139, at 36–37; Kriesel & Landry, *supra* note 18, at 406–07.

158. *See* LLOYD DIXON ET AL., RAND CTR. FOR CATASTROPHIC RISK MGMT. & COMPENSATION, FLOOD INSURANCE IN NEW YORK CITY FOLLOWING HURRICANE SANDY I (2013), http://www.rand.org/content/dam/rand/pubs/research_reports/RR300/RR328/RAND_RR328.pdf [<https://perma.cc/W3GL-U6UA>].

159. *Id.* at 2.

1996,¹⁶⁰ which, among other things, addressed employees' rights to health insurance when their employment terminated.

Most people have health insurance through their employment or under Medicare or Medicaid.¹⁶¹ Prior to the Affordable Care Act, however, there was a gap in health insurance for individuals who did not get health insurance through their employment or under Medicare or Medicaid.¹⁶² This gap was large, with approximately 46 million uninsured people prior to the Affordable Care Act.¹⁶³ The number of uninsured people in America continues to be a problem, but the number has fallen to approximately 27 million since the Affordable Care Act was passed.¹⁶⁴

One of the biggest reasons there were so many uninsured people prior to the Affordable Care Act was because individuals who had preexisting conditions could not buy individual health insurance because the available policies contained exclusions for preexisting conditions and insurers would refuse to even sell health insurance to people with serious preexisting conditions.¹⁶⁵ Insurers were also free to rescind a person's health insurance if the person misrepresented anything material regarding his health when applying for the insurance even if the misrepresentation was innocent or related to a health issue unrelated to the person's subsequent illness for which the person sought insurance payment.¹⁶⁶

The Affordable Care Act eliminated many of these restrictions because health insurance is not conceptually viewed as just a contract between two parties. Instead, access to health care is viewed by many people as a basic human right that can be provided through insurance.¹⁶⁷

160. Health Insurance Portability and Accountability Act of 1996, Pub. L. No. 104-191, 110 Stat. 1936 (codified as amended in scattered sections 42 U.S.C. § 210).

161. See ABRAHAM & SCHWARCZ, *supra* note 11, at 344.

162. See Amy B. Monahan, *On Subsidies and Mandates: A Regulatory Critique of ACA*, 36 J. CORP. L. 781, 782 (2011).

163. U.S. CENSUS BUREAU, JESSICA C. BARNETT & EDWARD R. BERCHICK, HEALTH INSURANCE COVERAGE IN THE UNITED STATES: 2016 (2017), <https://www.census.gov/library/publications/2017/demo/p60-260.html> [<https://perma.cc/NM5Q-JPYY>].

164. *Id.*

165. ABRAHAM & SCHWARCZ, *supra* note 11, at 349; HENRY J. KAISER FAMILY FOUNDATION, *How Accessible Is Individual Health Insurance for Consumers in Less-Than-Perfect Health?* (June 2001), <https://kaiserfamilyfoundation.files.wordpress.com/2013/01/how-accessible-is-individual-health-insurance-for-consumer-in-less-than-perfect-health-report.pdf> [<https://perma.cc/NHH9-8GSU>].

166. ABRAHAM & SCHWARCZ, *supra* note 11, at 350.

167. See, e.g., Tom Baker, *Health Insurance, Risk, and Responsibility After the Patient Protection and Affordable Care Act*, 159 U. PA. L. REV. 1577, 1579, 1584 (2011) ("The Affordable Care Act embodies a social contract of health care solidarity The Act, for the first time in U.S. history, explicitly recognizes a national entitlement to health care for all of the poor."); G.H. Jones & H. Kantarjian, *Health Care in the United States—Basic Human Right or Entitlement?*, 26 ANNALS OF ONCOLOGY 2193, 2193 (2015) ("Eighty-three percent of Americans say having health insurance is absolutely essential or very important, and 70% say it is important that the

With that in mind, under the Affordable Care Act, insurers are required to accept any individual who applies for insurance so insurers can no longer exclude coverage for preexisting health conditions.¹⁶⁸ Insurers also cannot refuse to renew a policy simply because the insured person is ill.¹⁶⁹ Nor can insurers place annual or lifetime coverage limits on their policies.¹⁷⁰ In addition, insurers' ability to charge different premium rates based upon the risk classification of the prospective insured is severely restricted and the policies must provide essential health care benefits.¹⁷¹

Medicaid was also expanded under the Affordable Care Act to include people who previously did not qualify.¹⁷² In addition, people who do not qualify for Medicaid but cannot afford health insurance are charged subsidized premium rates based upon the individual's income level.¹⁷³ Consequently, individuals with incomes up to 400% of the federal poverty line are eligible for the subsidies with the subsidy level increasing as the income level decreases.¹⁷⁴

As originally enacted, the purchase of health insurance was mandatory under the Affordable Care Act, in that people who did not purchase health insurance had to pay a "penalty."¹⁷⁵ This so-called "individual mandate" was based upon adverse selection¹⁷⁶ concerns—i.e., only the old and sick would buy health insurance if young and healthy people were not otherwise coerced into doing so.¹⁷⁷ Opponents of the individual mandate objected to it on the grounds that it violates the principals of federalism and individual autonomy because the federal government should not be able to mandate that people buy health insurance.¹⁷⁸ In-

nation has universal health care coverage (as in Medicare for Americans 65 years or older).").

168. See 42 U.S.C. §§ 300gg-1, 300gg-4 (2018).

169. See 42 U.S.C. § 300gg-2.

170. See 42 U.S.C. § 300gg-11.

171. See 42 U.S.C. § 300gg.

172. States receive federal funding to expand Medicaid rights under the Affordable Care Act. See 42 U.S.C. § 1396a; Nat'l Fed'n of Indep. Bus. v. Sebelius, 567 U.S. 519, 542 (2012). Thus far, thirty-four states have expanded Medicaid. See HENRY J. KAISER FAMILY FOUNDATION, *Status of State Action on the Medicaid Expansion Decision* (June 8, 2018), <https://www.kff.org/health-reform/state-indicator/state-activity-around-expanding-medicaid-under-the-affordable-care-act/?currentTimeframe=0&sortModel=%7B%22colId%22:%22Location%22,%22sort%22:%22asc%22%7D> [<https://perma.cc/SZ57-AFGF>].

173. See 26 U.S.C. § 36B.

174. See 42 U.S.C. § 18071.

175. See 26 U.S.C. § 5000A.

176. See *supra* note 116.

177. See, e.g., Baker, *supra* note 167, at 1586 ("The individual mandate is an important part of the solidarity equation because it requires everyone to be in the health insurance risk pool, addressing the adverse selection problem"); Monahan, *supra* note 162, at 787 ("To combat this likelihood of adverse selection, the individual mandate seeks to get everyone, particularly healthy individuals, into the risk pool.").

178. See Nat'l Fed'n of Indep. Bus. v. Sebelius, 567 U.S. 519, 540 (2012).

deed, one district court that struck down the individual mandate stated that if the mandate were upheld by courts, then “Congress could require that people buy and consume broccoli at regular intervals, not only because the required purchases will positively impact interstate commerce, but also because people who eat healthier tend to be healthier, and . . . put less of a strain on the health care system.”¹⁷⁹

The Supreme Court ultimately disagreed with these types of arguments and held the penalty for failing to purchase health insurance was really a tax and the federal government has the power to tax.¹⁸⁰ In 2017, the opponents of the individual mandate finally succeeded in defeating it, however, by eliminating the penalty for noncompliance when Republicans gained control of both houses of Congress and the White House.¹⁸¹

The Affordable Care Act sought to balance federalism concerns by federally mandating certain aspects of health insurance coverage but allowing states to create health insurance exchanges to provide a marketplace for the sale of the policies.¹⁸² That vision of shared regulation was not realized across the entire country, however, because many states declined to create health insurance exchanges, and instead, the federal health insurance exchange was used as the default option.¹⁸³

III. THE RISE OF MULTINATIONAL INSURANCE COMPANIES AND ALTERNATIVE RISK TRANSFER MECHANISMS

The evolution of insurance companies and risk transfer mechanisms over the past two hundred years is another piece of the puzzle regarding state versus federal regulation of the insurance industry. Although mutual companies were the dominant corporate form when insurance companies were first created in the United States, competition for insurance premium dollars and capital has driven many mutual companies out of the market for many lines of insurance.¹⁸⁴

Since the 1990s, there has been a dramatic shift in the financial structure of insurance companies from the mutual company form to the for-

179. *Florida ex rel. Bondi v. U.S. Dep’t of Health & Human Servs.*, 780 F. Supp. 2d 1256, 1289 (N.D. Fla. 2011), *aff’d in part, rev’d in part sub nom.*, *Florida ex rel. Att’y Gen. v. U.S. Dep’t of Health & Human Servs.*, 648 F.3d 1235 (11th Cir. 2011), *aff’d in part, rev’d in part*, *Nat’l Fed’n of Indep. Bus. v. Sebelius*, 567 U.S. 519 (2012).

180. *Sebelius*, 567 U.S. at 574.

181. *See* Tax Cuts and Jobs Act of 2017, Pub. L. 115-97, 131 Stat. 2054, Title I, § 11081(a)(2)(B) (repealing the penalty portion of the individual mandate, 26 U.S.C. § 5000A).

182. *See* 42 U.S.C. § 1396w-3 (2018).

183. *See* HENRY J. KAISER FAMILY FOUNDATION, *State Health Insurance Marketplace Types* (2018), <https://www.kff.org/health-reform/state-indicator/state-health-insurance-marketplace-types/?currentTimeframe=0&sortModel=%7B%22collId%22:%22Location%22,%22sort%22:%22asc%22%7D> [https://perma.cc/8TE9-CA6P].

184. *See* FEINMAN, *supra* note 15, at 48.

profit, publicly traded stock form.¹⁸⁵ The principle justification for this change is that stock companies can raise capital and diversify into other lines of insurance more easily than mutual companies.¹⁸⁶ Mutual companies' primary means of raising capital is through retained earnings, unlike stock companies, which can simply issue and sell additional shares.¹⁸⁷ The shift to stock company form was also driven by the changes in the federal income tax laws in the 1980s that eliminated the favorable tax treatment that mutual insurance companies had been receiving.¹⁸⁸

The change in corporate form for insurance companies is not a mere legal technicality. Stock companies are run for the benefit of shareholders with profit maximization as the governing principle.¹⁸⁹ For stock insurance companies, policyholders are viewed as revenue streams and adversaries with respect to the payment of claims because each dollar paid in claims is a dollar less of profits for shareholders.¹⁹⁰ Mutual companies, on the other hand, are owned by policyholders and thus, they are run with the best interests of the policyholders in mind.¹⁹¹ Consequently, the goals of the two types of companies are completely different.

Insurance companies are also vastly different in size and scope today than they were in the 1940s when the McCarran-Ferguson Act was passed.¹⁹² Today, multinational, global insurance companies dominate the market.¹⁹³ Some of these global insurers have tens of thousands of employees and market capitalizations of tens or hundreds of billions of dollars.¹⁹⁴ Although these global insurers sell insurance to policyholders across the United States and throughout the world, they are forced to

185. See Otgontsetseg Erhemjamts & J. Tyler Leverty, *The Demise of The Mutual Organizational Form: An Investigation of the Life Insurance Industry*, 42 J. MONEY, CREDIT & BANKING 1011, 1011 (2010).

186. See, e.g., James A. Smallenberger, *Restructuring Mutual Life Insurance Companies: A Practical Guide through the Process*, 49 DRAKE L. REV. 513, 518–19 (2001) (detailing competitive market advantages for corporations); Henry Hansmann, *The Organization of Insurance Companies: Mutual versus Stock*, 1 J. L. ECON. & ORG. 125, 138 (1985) (discussing fundraising by corporations through bond issuances).

187. See Hansmann, *supra* note 186, at 138.

188. See *id.*; Smallenberger, *supra* note 186, at 523.

189. See, e.g., JERRY & RICHMOND, *supra* note 28, at 47–48; French, *supra* note 31, at 1093; Smallenberger, *supra* note 186, at 518.

190. See French, *supra* note 33, at 1093.

191. See *id.*; JERRY & RICHMOND, *supra* note 28, at 47–48 (noting that the purpose of mutual companies is to provide insurance to the policyholder members of the company, not maximize profits for shareholders).

192. See, e.g., McGuire, *supra* note 8, at 353 (“In the almost half-century since the McCarran-Ferguson Act was passed, a number of changes have occurred that call the purposes of the Act into question. Insurance has become big business, far larger than it was in 1945, with larger firms operating on a national and international scale.”).

193. See, e.g., Sawe, *supra* note 4 (listing the ten largest insurance companies in the world and noting the prevalence of multinational companies at the top of the list).

194. American International Group, Inc. (AIG), for example, sells insurance in more than 80 countries around the world, had \$49.5 billion in revenue in 2017,

maintain artificial corporate structures due to states' regulation of the business of insurance pursuant to the McCarran-Ferguson Act. Specifically, although they present themselves to the world as a single insurance company, the "company" actually has numerous subsidiaries and affiliated companies that are licensed to do business in each of the various states in which they sell insurance in order to comply with the various states' insurance laws.¹⁹⁵ These related companies act as one, however, in sharing various administrative services.¹⁹⁶

Although reinsurance has been around for centuries, it also plays a much larger role in the United States today that it did in the 1944 when the McCarran-Ferguson Act was passed.¹⁹⁷ Today, reinsurance is a worldwide business wherein global reinsurers insure all or portions of other insurers' risks.¹⁹⁸ The reinsurance business crosses state and country lines. Indeed, most reinsurance purchased today by U.S. insurers is sold by European and Bermuda companies, which are not subject to regulation by the states in the United States.¹⁹⁹ Indeed, two of the three largest reinsurers

and has a market capitalization of approximately \$65.1 billion. See AM. INT'L GRP., INC., ANNUAL REPORT i (2017).

195. See, e.g., Schwarcz, *supra* note 6, at 543–44; Schwarcz & Schwarcz, *supra* note 6, at 1633.

196. See, e.g., Schwarcz, *supra* note 6, at 538.

197. See, e.g., FED. INS. OFFICE, U.S. DEP'T OF TREASURY, THE BREADTH AND SCOPE OF THE GLOBAL REINSURANCE MARKET AND THE CRITICAL ROLE SUCH MARKET PLAYS IN SUPPORTING INSURANCE IN THE UNITED STATES 5 (2014), <https://www.treasury.gov/initiatives/fio/reports-and-notice/Documents/FIO%20Reinsurance%20Report.pdf> [<https://perma.cc/F6QQ-HMCB>] ("During the latter part of the 20th century, few new U.S.-based reinsurers were established despite the economic growth during the period. Bermuda, however, emerged as an international reinsurance center during this period.")

198. See, e.g., BARRY S. OSTRAGER & THOMAS R. NEWMAN, HANDBOOK ON INSURANCE COVERAGE DISPUTES § 15.03[a], at 1357–58 (18th ed. 2017); NAT'L ASS'N INS. COMM'RS, NATURAL CATASTROPHES AND GLOBAL REINSURANCE—EXPLORING LINKAGES 22 (2013), http://www.naic.org/cipr_newsletter_archive/vol6_nat_cat_global_re.pdf?68 [<https://perma.cc/537G-ZKUE>]; SWISS RE, THE ESSENTIAL GUIDE TO REINSURANCE, at 9 (2010), http://media.swissre.com/documents/The_Essential_Guide_to_Reinsurance_EN.pdf [<https://perma.cc/YYN6-PCLE>] ("There are many different forms and types of reinsurance contracts: They either cover entire insurance portfolios or just relate to single risks; they may involve a sharing of all premiums and losses or they may just cover losses exceeding a certain threshold.")

199. See, e.g., GUENTER & DITOMASSI, *supra* note 40, at 10 ("[Reinsurance] is also an international business dominated by non-U.S. companies."); NAT'L ASS'N INS. COMM'RS, *supra* note 198, at 22 n.2 ("US insurers cede (transfer) nearly twice as much in premium volume to European reinsurers than European insurers cede to US reinsurers."); U.S. GOV'T ACCOUNTABILITY OFFICE, GAO/GGD-90-82, INSURANCE REGULATION: STATE REINSURANCE OVERSIGHT INCREASED, BUT PROBLEMS REMAIN 3 (1990) ("An individual state has no direct authority to regulate reinsurers in other states or countries who are not licensed in that state."); *Top 25 Non-Life Reinsurers: Swiss Re Leads, Berkshire Drops in A.M. Best's 2016 Ranking*, INS. J. (Sept. 12, 2016), <https://www.insurancejournal.com/news/international/2016/09/12/426023.htm> [<https://perma.cc/V4CJ-V9AD>] (most of the world's largest reinsurers are European companies); FED. INS. OFFICE, U.S. DEP'T OF TREASURY, BREADTH AND SCOPE, *supra* note 197, at 5 ("[I]n 2013 approximately \$46 billion in total (P/

in the world are Swiss Re and Munich Re, European companies.²⁰⁰ The five largest reinsurers in the world account for 67% of reinsurance capacity for the entire world.²⁰¹

Unlike in past decades, insurers also now sell catastrophe bonds to institutional investors that cover specific types of catastrophes, such as hurricanes and earthquakes.²⁰² Catastrophe bonds emerged in the 1990s following Hurricane Andrew in Florida and the Northridge Earthquake in California as a new way to diversify insurers' and reinsurers' risks with respect to catastrophic events.²⁰³ Under many types of catastrophe bonds, the investors receive interest payments on the bonds and the return of their principal at the end of the bond term unless the specified catastrophe occurs, in which case the insurer keeps the principal and does not owe any additional interest payments.²⁰⁴ The retained bond money is then available to pay the insured losses.

In 2017, a new record of \$12.6 billion of catastrophe bonds were sold.²⁰⁵ Many sellers and buyers of catastrophe bonds are not regulated by the states' insurance laws because they are foreign companies or are located in other states.²⁰⁶

IV. THE PROBLEMS WITH STATES CONTINUING TO SERVE AS THE PRIMARY REGULATORS OF INSURANCE

There are a number of deficiencies in the current state regulatory regime for the insurance industry. This Part of the Article addresses some of the principal ones.

C) reinsurance premiums were ceded by U.S.-based insurers to unaffiliated reinsurers; of this amount, approximately \$28.4 billion of premiums were ceded to non-U.S. reinsurers and approximately \$17.6 billion of premiums were ceded to U.S. professional reinsurers.”); Schwarcz & Schwarcz, *supra* note 6, at 1615 (“[R]einsurance is an international business—the largest companies are located in Europe and Bermuda . . .”).

200. See Schwarcz & Schwarcz, *supra* note 6, at 1615.

201. *Id.*

202. See Scales, *supra* note 24, at 46; see, e.g., Al Yoon & Leslie Scism, *Investors Embrace ‘Catastrophe Bonds’*, WALL ST. J. (Apr. 23, 2014), <https://www.wsj.com/articles/investors-embrace-catastrophe-bonds-1398292623> [<https://perma.cc/7U2X-SDBH>].

203. See U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-02-941, CATASTROPHE INSURANCE RISKS: THE ROLE OF RISK-LINKED SECURITIES AND FACTORS AFFECTING THEIR USE (2002) 15–16, <https://financialservices.house.gov/media/pdf/100802d2.pdf> [<https://perma.cc/L64R-L4Q3>].

204. See Scales, *supra* note 24, at 46.

205. See *\$12.6bn of Catastrophe Bonds in 2017 Take Market to New \$31bn High*, ARTEMIS (Jan. 2, 2018), <http://www.artemis.bm/blog/2018/01/02/12-6bn-of-catastrophe-bonds-in-2017-take-market-to-new-31bn-high/> [<https://perma.cc/DG5B-TEFR>].

206. See *id.*; see also AON BENFIELD, AON SEC. INC., *Insurance-Linked Securities: Alternative Capital Breaks New Boundaries* (2017), <http://thoughtleadership.aonbenfield.com/Documents/20170907-securities-ils-annual-report.pdf> [<https://perma.cc/8Y9N-HZSP>].

A. *Inconsistent Resolution of Disputes*

Because there is no uniformity in the state courts' interpretation of the meaning of standardized policy language, whether a claim is covered by identically worded insurance policies varies from state to state.²⁰⁷ Similarly, although the NAIC has drafted model statutes for adoption by the states, the NAIC has no authority to pass any laws so there are variations from state to state in even the model statutes that have been adopted.²⁰⁸ Thus, the outcomes of many insurance coverage disputes are dictated more by which state's law is applied than the merits of the case due to the differences in insurance law from state to state.²⁰⁹ This, in turn, means the race to the courthouse and choice of law battle can be the most important factors in winning many insurance cases.²¹⁰

The outcome of cases being decided by which party reaches the courthouse first creates the appearance that insurance cases are decided in an ad hoc, almost random way. In order for a legal system to be legitimate,

207. For a further discussion of the difficulties inherent in regulating different states' interpretation of standardized policy language and issues with international aspects of insurance left to state regulation, see *supra* notes 8 and 9.

208. See Schwarcz & Schwarcz, *supra* note 6, at 1632 (“[C]oordination is substantially impeded by the fifty-plus different insurance jurisdictions, each of which may be represented by commissioners with very different views about regulation generally and about the prospect of systemic risk in insurance in particular.”); see also FED. INS. OFFICE, U.S. DEP’T OF TREASURY, HOW TO MODERNIZE AND IMPROVE THE SYSTEM OF INSURANCE REGULATION IN THE UNITED STATES 31 (2013) (“Under the current system of state regulation, consistency can occur only by adoption and implementation of [uniform] standards and rules. As noted, however, the regulatory system has not resulted in consistent implementation of solvency oversight, notwithstanding coordination efforts through the NAIC, because regulators have interpreted and enforced even similar standards differently.”), <https://www.treasury.gov/initiatives/fio/reports-and-notices/Documents/How%20to%20Modernize%20and%20Improve%20the%20System%20of%20Insurance%20Regulation%20in%20the%20United%20States.pdf> [<https://perma.cc/3X3V-XEX2>].

209. See KALIS ET AL., *supra* note 8, § 26.03[B] (“Insurance contracts are interpreted according to state law. Not surprisingly, the manner in which the courts of the various states address similar interpretive issues can vary widely from one state to the next. The different interpretations given the same standardized language from one state to the next can mean the difference between a covered and a non-covered claim.”); 2 PLITT ET AL., *supra* note 9, § 24:1 (“In theory, the laws of two states cannot control the interpretation of a contract of insurance, and the choice of which jurisdiction’s law will govern can have serious consequences for an insurance dispute.”).

210. See, e.g., Larry Kramer, *Choice of Law in Complex Litigation*, 71 N.Y.U. L. REV. 547, 553–54 (1996) (“Conflicts scholars don’t fight bitterly about the differences among approaches [to determining choice law] because we disagree about their aesthetic qualities. We fight because the differences matter in terms of outcomes.”); Peter J. Kalis, James R. Segerdahl & John T. Waldron III, *The Choice-of-Law Dispute in Comprehensive Environmental Coverage Litigation: Has Help Arrived from the American Law Institute Complex Litigation Project?*, 54 LA. L. REV. 925, 933 (1994) (“The patchwork of state law that has evolved over the past decade or so has raised dramatically the profile of the choice-of-law issue in [complex] environmental coverage disputes. The resolution of this issue can be dispositive of whether a claim is covered, or, at a minimum, can substantially affect the value of the claim.”).

the dispute resolution process must at least appear to be fair. Currently, with each of the fifty states adopting their own insurance laws and interpretations of policy language, the outcomes of many insurance coverage disputes are not decided by the facts or justness of each party's respective position, but rather, by which state happens to hear the case.²¹¹

B. *Inadequate Regulatory Oversight of Multinational Insurers
and Foreign Insurers*

States cannot adequately regulate multinational insurers and they cannot regulate foreign insurers even though they are responsible for reinsuring large amounts of losses by U.S. citizens and companies.²¹² States only regulate the finances of insurance companies that are domiciled in their states.²¹³ This means a multinational company that is doing business across the entire United States cannot be effectively regulated because each state can only regulate the portion of the insurer's business that is related to its state. Consequently, there is only piecemeal regulation of national and multinational insurers. Indeed, state insurance regulators focus on the subsidiaries that do business in their states and they do not even collect financial information from the parent holding companies of those subsidiaries.²¹⁴

The AIG bailout in 2008 is a prime example of this problem. State insurance regulators were focused upon the AIG insurance subsidiaries within their states, but they missed the fact that noninsurance affiliates of AIG were engaging in risky security transactions.²¹⁵ Specifically, AIG Financial Products, a non-insurance AIG subsidiary, issued credit default swaps to other companies that guaranteed payment in the event of the default of mortgage-backed securities that were linked to homeowners mortgage payments.²¹⁶ When the housing market collapsed in 2008, AIG

211. See FRENCH & JERRY, *supra* note 18, at 33–34.

212. See SWISS RE, *supra* note 198, at 15 (“On average, about 9% of the premium volume in primary insurance is ceded to reinsurers, accounting for USD 196 billion in 2009.”).

213. See, e.g., *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 422 (2003) (states only have jurisdiction over activities that occur within their borders); Schwarcz, *supra* note 6, at 543 (“[T]he state in which an insurer is domiciled also reviews [the insurer’s financial data] to ensure that various regulatory requirements—such as capital, reserve, and investment restrictions—are satisfied.”); Macey & Miller, *supra* note 2, at 33 (“More problematic is the constitutional question of the geographic or jurisdictional reach of state regulatory power—its legislative jurisdiction.”).

214. See Schwarcz & Schwarcz, *supra* note 6, at 1633 (“Insurance regulators do not even require aggregate financial reporting at the holding-company level, much less regulate core financial measures at the holding-company level, such as capital levels.”). State regulators are trying to improve in this area, but their jurisdiction is limited by states lines. *Id.* at 1633 nn.339–41.

215. See *id.* at 1634.

216. See *id.* at 1584–85.

faced massive liabilities.²¹⁷ The end result was that the company was on the verge of bankruptcy and ultimately a federal government bailout of the company totaling \$182.5 billion was provided to prevent catastrophic financial ripple effects that would have occurred if AIG had defaulted on its financial obligations to numerous other companies.²¹⁸ AIG might not have financially collapsed if a single entity had regulatory authority over AIG as a whole, instead of fifty states and the Office of Thrift Supervision²¹⁹ regulating the various pieces of AIG.

The regulatory gap problem is even worse for foreign insurers that either are doing business as “surplus” insurers, which basically means they are not regulated by states at all,²²⁰ or as reinsurers that are covering risks insured primarily by another insurer.²²¹ In both scenarios, no state has regulatory authority over the foreign insurers.²²²

C. *Inadequate Policy Form Review and Approval*

States’ review and approval of policy forms is also currently inadequate. States’ regulation of the insurance industry in general, and their approval of policy forms in particular, is an exemplar of the concept of “regulatory capture.” Regulatory capture is a situation in which the regulation of the industry is so dominated by the industry itself that the industry is actually regulated for its own benefit.²²³

Even though state insurance regulators are specifically empowered by statutes to reject policy forms and language that could be considered un-

217. See *id.* at 1585.

218. See Sjoström, *supra* note 5, at 945 (“Government aid [to AIG] has since grown to \$182.5 billion.”).

219. The federal Office of Thrift Supervision was the regulatory body overseeing the AIG Federal Savings Bank, one of many AIG subsidiaries. See Sjoström, *supra* note 5, at 988.

220. See, e.g., JOHN F. DOBBYN & CHRISTOPHER C. FRENCH, *INSURANCE LAW IN A NUTSHELL* 517 (5th ed. 2016) (“‘[S]urplus line’ insurers . . . are not licensed in the state [T]he premium rates charged by surplus line insurers are unregulated, the policy provisions are not reviewed and approved by state regulators, insolvency assurances are not provided, and guaranty fund protections are unavailable.”); GUENTER & DITOMASSI, *supra* note 42, at 295 (“The activities of non-admitted insurers take place outside the jurisdiction in which the insured resides. They are shielded to a significant degree from the application of the state’s insurance laws by Constitutional due process restrictions.”).

221. See McGuire, *supra* note 8, at 355 (“State law is also simply unable to deal with international insurers in any effective manner. Huge international firms, including both direct writers, reinsurers, and retrocessional insurers are simply too large, too complex, and too powerful for most states to control.”).

222. See, e.g., 1A STEVEN PLITT ET AL., *supra* note 9, § 9:5 (“[T]he majority of reinsurance agreements involve a reinsurer that is not directly subject to the regulatory authority of the state in which the reinsured is admitted.”); McGuire, *supra* note 8, at 352 (“It is extremely difficult for the federal government to regulate the international aspects of the insurance industry under the antitrust laws. It is virtually impossible for the states to do so.”).

223. For a further discussion of regulatory capture in the insurance industry, see *supra* note 12.

fair, ambiguous, unreasonable, or contrary to public policy, they rarely exercise that authority.²²⁴ In fact, insurance regulators often do not even require insurers to submit policy forms for approval unless the insurers are changing policy language, which means that policy language that was approved decades ago is not actually reviewed by current regulators even though it is approved.²²⁵ In addition, state regulators often are former employees of insurers who return to work for insurers after they have served as regulators.²²⁶ Further, only insurers have advocates, including attorneys, who participate on their behalf during the policy form approval process.²²⁷

Consequently, the policy form approval process can be described as perfunctory. Indeed, the *Hartford Fire Insurance Co. v. California*²²⁸ case, in which insurers allegedly colluded to force consumers to purchase an unfavorable policy form despite state insurance commissioners' power to disapprove the policy form at issue, is a prime example of why insurers and state insurance regulators cannot be trusted to create and approve policy forms on their own.

In contrast to the current system, many arguments can be advanced in favor of having a single, independent third-party draft policy language for each line of insurance that would be used throughout the entire country.²²⁹ First, using a single drafting entity to produce insurance policy forms would ensure that the policy language used is consistent throughout the country. Second, consumers would not have to be concerned about whether the policy one insurer is selling contains the same terms and conditions as a policy sold by a different insurer. Consequently, consumers could compare insurers based upon price and quality of service instead of the terms and conditions of the policies, which generally are inscrutable to most consumers anyway. Third, using a single third party to draft policy forms, instead of the current system in which ISO or individual insurers draft the policy forms without any input from consumers, would allow con-

224. See ABRAHAM & SCHWARCZ, *supra* note 11, at 143, 146 (“[M]ost regulators generally do not invoke [their] broad authority [to disprove policy terms or forms] in the vast majority of cases” and the “filing of forms is not [even] required when the coverage is intended for policyholders who have a risk manager or whose premiums, net worth, or workforce exceeds specific thresholds.”); Keeton, *supra* note 56, at 967 (“Regulation is relatively weak in most instances, and even the provisions prescribed or approved by legislative or administrative action ordinarily are in essence adoptions, outright or slightly modified, of proposals made by insurers’ draftsmen.”).

225. See ABRAHAM & SCHWARCZ, *supra* note 11, at 146 (“A 2011 study found that most state insurance departments do not have complete copies of different carriers’ homeowners insurance policies in their records. The reason was that insurers typically only filed with regulators the specific policy language they sought to change, but not the entire policy . . .”).

226. *Id.* at 131.

227. See Anderson & Fournier, *supra* note 11, at 402–05.

228. *Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 770–71 (1993).

229. See generally French, *supra* note 43, at 569–70.

sumers' interests to be considered during the drafting process.²³⁰ Fourth, taking the drafting of policy language out of insurers' hands would allow policy forms to use simpler language that could be understood by the average consumer.²³¹

In sum, although state insurance commissioners have the authority to regulate the language and coverages contained in policy forms, they do not exercise that authority in a meaningful way.

D. *Inability to Require Coverage Nationwide*

States also cannot mandate that policies provide specific insurance coverages on a nationwide basis because they lack the authority and jurisdiction to do so.²³² For example, natural catastrophes, such as landslides and floods, currently are not covered under standard form homeowners insurance or commercial property policies.²³³ Yet, these types of natural catastrophes that can completely destroy people's homes and businesses are exactly the types of risks that should be covered by insurance because the purpose of insurance is to transfer large uncertain risks from individuals to entities that can spread and bear those risks. Indeed, most countries in the developed world have recognized this point and either provide coverage through state sponsored insurance programs or mandate that private insurance cover such risks.²³⁴

In the United States, however, because each state theoretically controls, vis-à-vis its insurance commissioner, what perils are covered under the policy forms sold in its state,²³⁵ one would need each of the fifty states to agree that natural catastrophes should be covered by property policies in order for natural catastrophes to be covered nationwide. For numerous political and practical reasons, that is unlikely to occur under the current system of state regulation.

First, insurers historically have contended that many natural catastrophes, such as flooding, are uninsurable, correlated risks so insurers do not want to cover such risks.²³⁶ Correlated risks are risks in which numerous people in the same geographic area suffer the same type of losses at approximately the same time.²³⁷ Insurers contend correlated risks are uninsurable because they cannot be predicted with enough accuracy to charge

230. *Id.* at 570.

231. *Id.*

232. *See, e.g.,* *Huntington v. Attrill*, 146 U.S. 657, 669 (1892) ("Laws have no force of themselves beyond the jurisdiction of the state which enacts them, and can have extraterritorial effect only by the comity of other states.").

233. *See supra* note 18.

234. *See supra* note 19.

235. *See supra* notes 10 and 11.

236. *See, e.g.,* Scales, *supra* note 24, at 10–11.

237. *See, e.g.,* Véronique Bruggeman, Michael Faure & Tobias Heldt, *Insurance Against Catastrophe: Government Stimulation of Insurance Markets for Catastrophic Events*, 23 DUKE ENVTL. L. & POL'Y F. 185, 187 (2012); Cummins, *supra* note 27, at 342-43.

actuarially sound premiums.²³⁸ Thus, if forced to do so, insurers contend they would be at risk of becoming insolvent.²³⁹ States apparently have accepted this argument for decades, as evidenced by the fact that no states mandate that property policies cover flood losses and the NFIP was created as a result. Nonetheless, despite the claim that floods are uninsurable, some private insurers actually sell coverage for flooding under commercial property policies²⁴⁰ and AIG currently sells flood insurance to homeowners in thirty-seven states²⁴¹ so perhaps it is time to question insurers' historic contention that flooding is an uninsurable correlated risk.

Second, some opponents of requiring private insurers to cover flood risks may argue that the risks the people in one state face are not the same risks people face in other states so they should not be forced to purchase coverages they do not need or want.²⁴² For example, why should people who live in Montana be required to have insurance that covers flooding caused by hurricane-induced coastal storm surges?

Third, some people also may argue that they should not be required to subsidize other people's insurance rates, which people who have lower risk profiles for various natural catastrophes inevitably would be required to do if all policies covered the same risks.²⁴³ Any amount of premium that a person in Montana pays for hurricane storm surge coverage necessarily must be subsidizing some other person's losses.²⁴⁴ Ironically, in some respects, this argument actually favors having insurers sell insurance na-

238. See Bruggeman et al., *supra* note 237, at 187; Cummins, *supra* note 30, at 342–43.

239. See Bruggeman et al., *supra* note 237, at 188; Cummins, *supra* note 29, at 342–43.

240. See, e.g., *Penford Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 662 F.3d 497, 500–02 (8th Cir. 2011) (litigating whether the policyholder had \$50 million or \$20 million in coverage for flood losses under an “all risk” commercial property policy).

241. See *About Us—Private Market Flood*, THE FLOOD INSURANCE AGENCY, <http://www.privatemarketflood.com/about-us/> [<https://perma.cc/7TGU-97QK>] (“We currently offer [flood] coverage in 37 States and insure over \$4.5 billion dollars of property values.”) (last visited Jan. 4, 2019).

242. This argument is not well founded because people currently are forced to purchase coverage they do not want or need because the policy forms are standardized and sold on a take-it-or-leave-it basis regardless of whether the person needs or wants all of the coverages provided under the policy. See *supra* note 10.

243. Because homeowners insurance is effectively mandatory, the additional premiums charged to cover such risks would be spread across the 69 million homeowners with a wide range of risk profiles so the additional premiums for each individual homeowner should not be significant. See French, *supra* note 20, at 79.

244. One response to such an argument is that the purpose of insurance is to serve as a social safety net and it is not intended to simply be a contract in which the premium charged to each individual is the precise actuarial amount needed to cover that person's predicted risk of loss. Instead, insurance is a reflection of community solidarity in which each person contributes to a pool of money to help the unfortunate few who suffer losses and to provide peace of mind to the majority of people who do not suffer losses. See, e.g., FEINMAN, *supra* note 15, at 21–23; Stempel, *supra* note 30, at 1489.

tionwide without regard to state boundaries. If insurers could sell policies nationwide instead of state by state, then the risk profiles of the pool of insureds being covered by each insurer would be much more diversified and insurer concerns regarding adverse selection and correlated risks would be diminished.²⁴⁵

Fourth, other opponents may argue that any government mandate regarding what risks should be covered by insurance is inconsistent with freedom of contract and the concept of freedom in general, which Americans highly value. Self-governance dictates that people should be allowed to choose what they purchase.²⁴⁶

In short, based upon these arguments, under the current system of state regulation, achieving nationwide coverage under homeowners policies for natural catastrophes is highly improbable. And that is one of the reasons why some people, insurers, and states advocate for the continuation of the current system. But, is that what is best for homeowners and local business owners?

E. *Inability to Police Insurer Misconduct Nationwide*

States also cannot police insurer misconduct that occurs nationwide. *The State Farm Mutual Automobile Insurance Co. v. Campbell*²⁴⁷ case illustrates this problem. In *Campbell*, the policyholder attempted to pass six vans while driving. In doing so, an oncoming driver swerved to avoid a collision with the policyholder, which in turn caused the oncoming driver to hit another car head on.²⁴⁸ The accident resulted in the death of one person and another person being permanently disabled.²⁴⁹ There was little question that the policyholder was at fault, but the insurer nonetheless refused to settle and went to trial.²⁵⁰ The jury awarded damages in an amount in excess of the policy limits so the insurer instructed the policyholder to sell his house in order to satisfy the excess judgment.²⁵¹

Eventually, the insurer paid the excess judgment instead of the policyholder, but in a subsequent bad faith lawsuit brought by the policyholder it was revealed that the insurer had a nationwide corporate policy of paying less than the fair value of claims and it had instructed its claims han-

245. See, e.g., French, *Insuring Floods*, *supra* note 19, at 79 (arguing that mandatory flood coverage under homeowners insurance would spread the risks associated with floods across 69 million policyholders instead of just the 5.5 million who currently purchase flood policies under the NFIP).

246. This argument is ill informed because consumers currently do not have any input into the policy language so freedom of choice regarding the policy language is only an illusion. Moreover, state insurance regulators, not consumers, currently have power to dictate what coverages policies provide, but they do not exercise that power. See *supra* notes 10–11.

247. 538 U.S. 408 (2003).

248. *Id.* at 412–13.

249. *Id.* at 413.

250. *Id.*

251. *Id.*

dlers to falsify records in order to support the unfair payment amounts.²⁵² Under this corporate policy, claims handlers also were instructed to “target ‘the weakest of the herd’—‘the elderly, the poor, and other consumers who are least knowledgeable about their rights and thus most vulnerable to trickery or deceit, or who have little money and hence have no real alternative but to accept an inadequate offer to settle a claim at much less than fair value.’”²⁵³

After a jury awarded the policyholder \$2.6 million in compensatory damages and \$145 million in punitive damages based upon jury instructions and evidence that allowed the jury to punish the insurer for its nationwide bad faith misconduct, the Supreme Court vacated the amount of the punitive damages award on appeal. The Supreme Court held, among other things, that it was improper for the jury to consider the insurer’s nationwide misconduct in awarding punitive damages because states do not have the authority to punish insurers for actions that occur outside of their borders:

A basic principle of federalism is that each State may make its own reasoned judgment about what conduct is permitted or proscribed within its borders, and each State alone can determine what measure of punishment, if any, to impose on a defendant who acts within its jurisdiction.²⁵⁴

Thus, the Supreme Court vacated the punitive damage award and remanded the case for a new punitive damages award determination that was based only upon the insurer’s misconduct within the state.²⁵⁵

In short, under the current regulatory regime, states do not have the power to deter or punish nationwide insurer misconduct. Instead, an insurer’s nationwide misconduct must be addressed on a state-by-state basis, with each state concerning itself only with the misconduct that occurs within its own borders.

V. DUAL REGULATION INVOLVING BOTH THE STATES AND THE FEDERAL INSURANCE OFFICE

The current system in which states are the primary regulators of insurance with Congress periodically interjecting itself in certain areas, such as ERISA, NFIP, and the Affordable Care Act, has room for improvement. States cannot adequately regulate multinational insurers and foreign reinsurers even though such insurers dominate insurance markets.²⁵⁶ States currently do not regulate policy forms in a way that is protective of consumers.²⁵⁷ Nor can states mandate that particular coverages, such as for

252. *Id.* at 432.

253. *Id.* at 433.

254. *Id.* at 422.

255. *Id.* at 429.

256. *See supra* Part IV.B.

257. *See supra* Part IV.C.

natural disasters, be included in policies on nationwide basis.²⁵⁸ States also lack jurisdiction to police insurer misconduct on a nationwide basis.²⁵⁹ And, the lack of uniformity in state insurance laws means that insurance disputes are often won by the party who wins the race to the courthouse and secures the more favorable state law, as opposed to the party whose position is more just.²⁶⁰

Yet, completely turning the regulation of insurance over to the federal government is unappealing as well. In addition to the enormous federalism issue that such a change would create, states have been regulating insurers for over 200 years at this point so there is an existing body of state statutes, regulations, and case law that provide guidance to insurers and consumers alike with respect to insurance matters. Nothing comparable currently exists in the federal system so a transfer of complete regulation of insurance matters to the federal government would be a massive undertaking that would create great uncertainty for all parties for an extended period of time.

In addition, federal law in the areas in which Congress has intervened regarding insurance—e.g., ERISA, the NFIP, and the Affordable Care Act—provide little comfort that exclusive federal regulation of insurance would be better for either consumers or insurers. For example, consumers currently have more remedies available to them, including the right to assert claims for bad faith and seek punitive damage awards, under state laws than they do under ERISA.²⁶¹ Further, the standard of review for coverage determinations under ERISA is much more deferential to insurers than state law—abuse of discretion versus *de novo*.²⁶² Consequently, few consumer advocates would advocate for federal regulation of other areas of insurance if ERISA would be the template.

Similarly, the NFIP has been a poorly administered insurance program so if it is the model that federal regulation of insurance would follow, then again consumers would say, “No thanks.” The NFIP often is insolvent.²⁶³ The insurance coverage provided under an NFIP policy is inadequate for many homes in many parts of the country.²⁶⁴ The flood maps used in the program historically have been woefully inaccurate with many homes in high risk flood areas listed as being located in low risk areas.²⁶⁵ The private insurers that are administering claims under the program have conflicts of interest when it comes to paying hurricane claims because they typically issue the homeowners policies that cover the

258. *See supra* Part IV.D.

259. *See supra* Part IV.E.

260. *See supra* Part IV.A.

261. *See supra* Part II.E.1.

262. *See supra* Part II.E.1.

263. *See supra* Part II.E.2.

264. *See supra* Part II.E.2.

265. *See supra* Part II.E.2.

properties.²⁶⁶ Consumers also have worse legal rights under the program than they do under most states' laws. For example, as discussed, the untimely presentation of a proof of loss results in a forfeiture of coverage under the NFIP, but it would not under most states' laws.²⁶⁷

If the Affordable Care Act, on the other hand, is what the country could expect under a federal regulatory regime, then there may be more cause for optimism. The Affordable Care Act actually has done a good job of achieving one of its primary objectives, which was to lower the number of uninsured people in America with respect to health insurance.²⁶⁸ But, the Affordable Care Act has been under constant Congressional attack since it was passed so its future viability remains in question with each election.²⁶⁹ It makes little sense to have Congress regulate insurance if the governing statutes and rules will change with each election every two years as the balance in Congress swings back and forth between a Democratic majority and a Republican majority. Moreover, with the elimination of the individual mandate, it is questionable whether insurers will even be able to continue to sell affordable health insurance under the Affordable Care Act if they are left insuring only old and sick people.²⁷⁰ Thus, if the Affordable Care Act is the best recent example of Congress' efforts in the area of insurance regulation, then perhaps Congress should not be entrusted with the important responsibility of regulating the insurance industry on a nationwide basis in other lines of insurance.

So, is there a better way? Here is one proposal: dual regulation of the insurance industry. Do not strip states of regulatory authority over insurers by repealing the McCarran-Ferguson Act, as many people have advocated in the past.²⁷¹ In some areas, such as rate regulation, states generally do a fine job, but in other areas the federal government is better positioned. So, the state or federal agency that can best regulate the particular insurer or aspect of insurance at issue should regulate it.²⁷² To that end, empower the Federal Insurance Office (FIO) with some regulatory authority over the insurance industry. Create a system of dual regulatory authority. That technically is already the system in place under the McCarran-Ferguson Act, but Congress rarely exercises its authority to regulate insurance matters so a federal agency with delegated powers should assume that role. The FIO might be perfect for the job.

266. See *supra* Part II.E.2.

267. See *supra* Part II.E.2.

268. See *supra* Part II.E.3.

269. See Ed O'Keefe, *The House Has Voted 54 Times in Four Years on Obamacare. Here's the Full List.*, WASH. POST (Mar. 21, 2014), https://www.washingtonpost.com/news/the-fix/wp/2014/03/21/the-house-has-voted-54-times-in-four-years-on-obamacare-heres-the-full-list/?noredirect=on&utm_term=.f4c9a618051d [<https://perma.cc/D8E8-6Q5V>] (The House of Representatives has voted to repeal the Affordable Care Act more than fifty times).

270. See *supra* Part II.E.3.

271. See *supra* notes 2 and 92.

272. See Schwarcz & Schwarcz, *supra* note 6, at 1628–29.

In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) established the FIO within the U.S. Department of the Treasury.²⁷³ The President appoints the director of the FIO.²⁷⁴ The FIO currently, however, only has authority to study various aspects the insurance industry, write reports, and make recommendations.²⁷⁵ It does not have the authority to make insurers or states actually do anything with respect to insurance matters. Indeed, as currently empowered, states generally ignore the FIO.²⁷⁶ Yet, because it already exists and has expertise regarding insurance matters, it would be well positioned to start to exert some federal regulatory authority over insurers and issues that states cannot, or will not, address.

For example, multistate and international insurers need an entity that has power to regulate them. They have become too large and important to U.S. insurance markets for no U.S. governmental authority to provide effective oversight.²⁷⁷ States do not, and cannot, have that authority due to the limits on their jurisdiction,²⁷⁸ but the FIO could.

The FIO also could replace insurers and ISO as the drafter of policy forms and issue policy forms to be used on a nationwide basis. In that process, it could receive input from experts and advocates who represent the interests of both insurers and consumers.²⁷⁹ The FIO could shorten the length of policy forms and use language that can be understood by consumers.²⁸⁰ As a federal agency, it also could mandate that certain coverages, such as coverage for natural disasters, be included nationwide.²⁸¹

If insurers do not like the language or the coverages provided in the policy forms created by the FIO, then they could simply choose not to sell those lines of insurance. Of course, such an approach raises the risk that some insurers may exit some lines of insurance. It seems unlikely, however, that a competitive insurance market would not continue to exist across most major lines of insurance. The emergence of multinational and global insurers, worldwide reinsurance, and the advent of catastrophe bonds that spread the risks that insurers face makes it unlikely that insurers could not offer broader coverage profitably because risks can be

273. See 31 U.S.C. § 313 (2018).

274. See 31 U.S.C. § 313(a).

275. *Id.* § 313(c); see also Schwarcz & Schwarcz, *supra* note 6, at 1631 (“[T]he FIO itself has no actual regulatory authority over the insurance industry.”).

276. See Schwarcz & Schwarcz, *supra* note 6, at 1637 (“To this point, states have either resisted or ignored many of the FIO’s suggestions. For instance, states have refused to allow the FIO to attend meetings of supervisory colleges—wherein regulators discuss the risks associated with entire holding companies—by arguing that the FIO’s involvement would not be appropriate.”).

277. See *supra* Part IV.B.

278. See *supra* Part IV.B.

279. See French, *supra* note 43, at 570–72 (advocating for an independent government entity to assume responsibility for drafting insurance policies).

280. *Id.* at 569–70.

281. See *supra* Part IV.D.

spread worldwide today in ways not possible in past decades.²⁸² Thus, if a risk can be broadly spread, then the only issue is ensuring that actuarial sound, but fair, premium rates are charged for the entire pool of insureds.

Similarly, the FIO could issue regulations that govern insurer conduct regarding the advertising and sale of insurance, as well as claims handling practices, that apply nationwide.²⁸³ The states already have adopted model acts drafted by the NAIC that could serve as templates for nationwide statutes.²⁸⁴ The difference, however, would be that the FIO and aggrieved consumers could police insurers' conduct throughout the United States, as opposed to just within a particular state's borders. That would address the current problem highlighted by the *State Farm* case—i.e., punitive damage awards that are based upon violations of state law must be limited to conduct that occurred within the applicable state.²⁸⁵ Thus, if an insurer were to violate a federal FIO regulation across the country, then the aggrieved consumers or the FIO itself could bring a lawsuit seeking damages, penalties, and/or injunctive relief based upon the nationwide misconduct.

It also is important that the extra contractual remedies that currently are available under state law, but not under ERISA and the NFIP, be available nationwide in a dual regulatory system.²⁸⁶ Extra contractual damages create some downside risk for insurers that is needed to deter insurer misconduct. Unlike under state law, there currently is no economic downside for insurers to deny claims in bad faith under the NFIP and ERISA because an insurer is only liable for the contractual amount owed plus some nominal interest if it is found liable.²⁸⁷ This means that, under ERISA and the NFIP, insurers are economically incentivized to deny claims and hold money owed to insureds as long as possible, which is bad for consumers.²⁸⁸ That would need to change if the FIO were to become responsible for policing insurer behavior nationwide.

If the FIO were given this additional authority, then one of the biggest concerns would be regulatory capture—a problem that currently

282. See *supra* Part III.

283. See *supra* Part IV.D.

284. See, e.g., MODEL UNFAIR TRADE PRACTICES ACT (NAT'L ASS'N INS. COMM'RS 2011), <http://www.naic.org/store/free/MDL-880.pdf?20> [<https://perma.cc/LZ2Z-6UJK>]; MODEL UNFAIR CLAIMS SETTLEMENT PRACTICES ACT, (NAT'L ASS'N INS. COMM'RS 2010), <http://www.naic.org/store/free/MDL-900.pdf?19> [<https://perma.cc/6AF6-C5CZ>].

285. *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 422 (2003).

286. See *supra* Parts II.E.1 and II.E.2.

287. See, e.g., JERRY & RICHMOND, *supra* note 28, at 161 (explaining that bad faith remedies were created because of “the apparent inadequacy of contract remedies to compensate insureds and deter insurers from elevating their own interests above their insureds’”).

288. See, e.g., French, *supra* note 31, at 111921 (arguing for the creation of other financial disincentives, in addition to bad faith claims, to deter insurers' improper denials of claims).

plagues state insurance regulators.²⁸⁹ Safeguards would need to be put in place to ensure that the FIO did not simply replace state insurance commissioners as captured agents of the insurance industry regarding the drafting of policy forms and the policing of insurers. For example, public hearings and comment could be required to approve policy forms and regulations drafted by the FIO to ensure that they are not simply serving the interests of the insurance industry. In addition, either insurers or consumers could seek judicial review of FIO decisions or FIO rules at a standard higher than abuse of discretion to ensure that a disinterested third party provides some oversight of the FIO. Thus, even though the director of the FIO would be appointed by the executive branch and have authority to promulgate regulations, the FIO's actions would be subject to meaningful judicial review.

VI. CONCLUSION

Since the United States was created, insurers have been regulated primarily by the states, with a few areas in which Congress has intervened. As the insurance industry has evolved, however, states have become unable to adequately regulate some insurers, such as multinational and foreign insurers, due to a lack of jurisdiction. In other areas, such as the coverages provided by and the language used in policy forms, states have simply failed to adequately regulate insurers.

Simply turning the regulation of insurance over to Congress is not a good remedy for inadequate state regulation, however, because the areas of insurance in which Congress historically has interjected itself has led to less than exemplary results. To the contrary, in many circumstances, consumers have less protection under federal law than they had under state law.

With the creation of the FIO, it is time to consider dual state and federal regulation of insurance. The FIO could regulate the areas in which states are unable to do so or have done so inadequately. The states, on the other hand, could continue to regulate the areas in which they have proven competency such as, for example, policy rate oversight and insurer solvency for local and regional insurers.

289. *See supra* notes 12 and 223.