

## The Effect of the AIG Outcry

By Kenneth R. Auerbach, Esq.

By the time you read this, the nation wide controversy surrounding the payment of retention bonuses by AIG to some of the people in its financial products division may have receded from the daily news cycle. But maybe not. One thing is certain; it has had and will continue to have an effect on the tenor of the impending debate in Congress about financial services regulatory reform. The question is, what will the effect be?

While nobody likes seeing people whose mistakes almost tanked a company and did damage to the American economy requiring multiple taxpayer buyouts rewarded with questionable million dollar plus special payments, there is a risk that over indulging in outrage could cause us to lose sight of the bigger picture.

Outrage is not a rational basis for sound public policy. And it is certainly not the way to advance what needs to remain our number one priority; the recovery of our nations battered economy. As poet Ralph Waldo Emerson once noted, "Cursing the darkness only delays the dawn."

Since the AIG bonus controversy erupted, Congress has been falling all over itself to point fingers of blame at everyone but itself. There have been multiple hearings in the House and Senate, one including a strong grilling of AIG CEO Edward Libby.

But if there is one positive aspect to all the sound and fury being generated by the AIG bonuses, it is this; amid all the rancor, some common sense is managing to seep into the discussion about the future of insurance regulation. You have to listen closely, but it can still be discerned.

State insurance regulators have been among those called to testify during the spate of congressional hearings. They have pointed out repeatedly that the insurance operations at AIG were financially sound and remain so. The problem

was in the AIG financial Products unit. As Pennsylvania Insurance Commissioner Joel Ario noted in his testimony before the House Financial Services Committee on March 18, "...what happened at AIG demonstrates the strength and efficiency of state insurance regulation ... AIG's insurance companies remain strong, in part because state regulation continues to wall them off from the high risk activities engaged in by AIG Financial Products."

And a recent report and testimony by the Government Accountability Office (GAO) agrees with our state insurance regulators that these issues did not arise in AIG's insurance operations, which remain sound.

As Congress moves from serving as a conduit for public outrage to the more serious task of crafting legislation to strengthen the regulation of all financial services, it should be remembered that the AIG that got into trouble was not any of the 71 AIG insurance companies, which remain strong thanks to state insurance regulation. It was the entity and its operations that were supervised not by the state, but by Federal Office of Thrift Supervision (OTS) which recently admitted that it failed to properly understand the AIG Financial Products unit's implications and made wrong oversight decisions in 2004.

Terri Vaughan, the NAIC's chief executive officer, notes in her interview with PIA in the March issue of PIA Connection that measures to address systemic regulation of financial services should build upon, not replace, and the successful national system of state based insurance regulation. We agree.

A danger that needs to be avoided is inadvertently enacting laws that have unintended consequences, such as stifling competition in the marketplace, or encouraging rather than limiting the "to big to fail" syndrome. We believe that an optional federal charter would have such unintended consequences, in addition to encouraging regulatory arbitrage that would weaken effective supervision.

Although it is not part of the oath they take, members of Congress would be well advised to observe their own version of the Hippocratic Oath as they set about remaking the financial oversight structure of our country which, despite its recent failings, has served us well: "First, do no harm."

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