

## STATES VS. U.S.: WHO WILL POLICE INSURANCE FIRMS? BY JOSEPH B. TREASTER, NEW YORK TIMES

In the summer of 2002, Maurice R. Greenberg, the chief executive of the [American International Group](#), was facing problems with the brokers who sold commercial insurance policies for his company.

[Marsh & McLennan](#) Companies, the world's largest insurance broker, was making another request for higher incentive payments and wanted to expand them to additional lines of coverage. At the same time, A.I.G. was being sued in California over these incentives, widely referred to as contingency commissions.

For years, brokers had been quietly taking the commissions for increasing the sales and profits of insurance companies while promising their customers unbiased advice on coverage. But to Mr. Greenberg, the incentive payments were an irritating extra expense - ultimately passed on to customers - that he would have happily seen eliminated.

So he decided to ask the insurance regulators in New York whether the payments were proper. More than two years later, he received an answer. It came not from the New York superintendent of insurance, but from Eliot Spitzer, the New York attorney general, who sued Marsh on Oct. 14, asserting that the incentive payments constituted a conflict of interest.

Mr. Spitzer's lawsuit touched off a wave of investigations into the insurance industry and intensified a debate over the adequacy of insurance regulation in America.

Insurance has long been regulated state by state, generally by officials who are woefully outmatched in money and expertise by the companies they are supposed to oversee. But the question increasingly confronting the state regulators is whether they can transform themselves into strong, effective overseers or whether their job or aspects of it should be turned over to Washington.

"There is a window of opportunity," said Brian K. Atchinson, a former president of the National Association of Insurance Commissioners and now the executive director of the Insurance Marketplace Standards Association, a life insurance industry group that promotes ethical practices. "If the states can't do it, there is little doubt that Congress will."

Even before Mr. Spitzer's lawsuit, the insurance companies were pushing for federal involvement to simplify and speed up the approval of new insurance products and to deregulate commercial coverages and prices for auto and home insurance.

Senator Richard C. Shelby, a Republican who is the chairman of the Senate Banking Committee, plans to conduct hearings on insurance next year and others in Congress may also do so. "If the state regulators are not up to the task of regulating the insurance industry, we may have to look at alternatives," said Andrew Gray, a spokesman for Mr. Shelby.

So far, there is no consensus on what alternatives are best. State regulators and consumer advocates, often at

odds, have joined in a loose alliance against handing over regulation of insurance to federal officials. But many insurance companies are pushing hard for some federal involvement.

The New York regulators' experience with the question of incentive payments for brokers underscores the difficulty of one important aspect of regulation: resolving potential conflicts of interest in arcane and entrenched industry practices.

"Everybody is talking about the adequacy of state regulation and whether the regulators were asleep on this," said Gregory V. Serio, the superintendent of insurance in New York. "No, we weren't. But we had to start from scratch."

Gov. George E. Pataki announced yesterday that Mr. Serio would leave the insurance department next month. Michael F. Barry, a spokesman for the department, said Mr. Serio, who had given no indication that he planned to leave, submitted a letter of resignation to the governor early yesterday afternoon, saying he planned to take a job in the private sector that was "an outstanding opportunity that he couldn't pass up." Mr. Barry said the resignation "had nothing at all to do" with the investigation being conducted by Mr. Spitzer and that Mr. Serio had "absolutely not" been forced out. Mr. Barry said Mr. Serio was not available for an interview.

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New York, alone among the state regulators, began to look into contingency commissions in 1997, after corporate risk managers, the executives who buy insurance for major companies, raised concerns that Marsh and other dominant brokers might be tempted to steer business to the insurers that paid them the most.

In August 1998, the New York regulators issued a "policy guidance document" declaring that all compensation arrangements between brokers and insurance companies should be disclosed to customers. The "undisclosed receipt of additional compensation" by brokers, it said, was "sufficient to create the perception that brokers are conflicted in their loyalties" and could violate insurance regulations "as a dishonest and untrustworthy practice."

But the brokers, as it turned out, did not fully comply with the guidance. Many told customers that they received compensation from insurers. But they did not volunteer details and often, risk managers say, would not supply them when asked.

Still, until Mr. Greenberg raised the issue, at a time when compensation arrangements with mutual funds were becoming an issue, no one had complained to the department, Mr. Serio said in an interview earlier this month. Neither the regulators in New York nor in any other state had seen reason to question the payments.

After asking the New York insurance department about the payments, Mr. Greenberg and his staff went back and forth with the regulators for the next two years. Mr. Serio

said in the interview that he had begun an inquiry but had been unable to reach a conclusion about the payments.

Part of the reason, he said, was that Mr. Greenberg would not provide details of his dealings with brokers; also, none of the more than 100 brokers and insurers to whom Mr. Serio sent written questions suggested any serious problems. Mr. Serio said he received no response from Mr. Greenberg when he offered to conduct an undercover investigation of Marsh, whose chief executive at that time was Mr. Greenberg's eldest son, Jeffrey W. Greenberg.

"We are a public company," Maurice Greenberg said in an interview. "We are not a government agency that conducts undercover operations. I don't know what kind of liability we'd be confronting. If the department wants to do something undercover, they don't need us."

As for his refusal to provide details of his concerns about contingency commissions, Mr. Greenberg said: "I don't think it's right for us to disclose things like that. We gave them enough information to do what they thought had to be done. If they made a decision not to do anything, it was up to them."

When Mr. Spitzer's office notified the insurance regulator in March that it was beginning an investigation, Mr. Serio said, "we essentially handed over to him what we had and he became the lead agency on this."

While Mr. Spitzer's inquiry began because of questions about contingency commis-

sions, which he later described as kickbacks, investigators say they then discovered that Marsh, with the collusion of several insurance companies, had been rigging bids.

Five insurance executives, including two at A.I.G., have been arrested, and shortly after Mr. Spitzer filed his lawsuit, Jeffrey Greenberg resigned as Marsh's chief executive.

Maurice Greenberg said he never envisioned such a calamitous outgrowth of his questioning of contingency commissions in 2002.

"I didn't think there was anything that violently wrong," Mr. Greenberg said. "I thought there would be a clarification, a clarification for everybody. I didn't know what the department was going to do because contingent commissions have been around for longer than you and I have been alive. I just felt we needed clarification."

Mr. Serio has been leading efforts to strengthen state regulation nationally. Before his resignation was announced, Mr. Serio that in an effort to bolster regulation in New York, he was considering asking the legislature to expand his department's power to examine insurance brokers and obtain data from holding companies. He said he would also seek greater penalties for violating insurance regulations.

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Mr. Serio has ordered executives of Marsh and Universal Life Resources, an employee benefits broker in California that has also been sued by Mr. Spitzer, to appear at public hearings in January. The insurance superintendent has the authority to revoke the license of a broker or insurer and put it out of business, but his agency has never taken such action against a major company.

Mr. Serio had also begun advocating the creation of an industry organization similar to NASD, the regulatory arm of the securities brokerage business, that would set standards, monitor business practices and discipline offenders. Governor Pataki said he intended to nominate a state assemblyman, Howard D. Mills III, to succeed Mr. Serio as superintendent of insurance. Mr. Mills, a Republican, ran unsuccessfully in November for the United States Senate against Charles E. Schumer.

Mr. Spitzer has acknowledged the New York insurance department's assistance in his investigation. In testimony in November before a Senate subcommittee, he said he did not think that Washington should pre-empt the state regulation of insurance. But, he said, "there are too many gaps in regulation across the 50 states, and many states have not been sufficiently aggressive in terms of supervising this

industry."

State regulators face a formidable force. The insurance industry reported sales of \$1.1 trillion in 2003. It is layered over with lawyers, lobbyists, underwriters, marketing specialists and tens of thousands of local agents and brokers working in towns and cities around the country.

**"The states need to pass laws to make regulation tougher."**

Taxes on the sale of insurance are intended to pay for insurance regulation. But most of the money goes into the general funds of the states instead of for regulatory work. Even amid the recent controversy over insurance practices, state regulators, as a group, have responded with half-steps. For example, instead of proposing to eliminate contingency commissions, as some companies, including A.I.G. and Marsh, have

already done, the national association has begun working on a proposal to require full disclosure of all payments received by brokers and agents.

As anemic as the state regulators' response to the upheaval in the insurance industry may seem, consumer advocates worry that federal regulation would be even weaker.

"Federal regulation would substitute a deregulated environment that would wipe out what pitifully limited regulation exists at the state level," said Harvey Rosenfield, a California lawyer and founder of the Foundation for Taxpayer and Consumer Rights in Santa Monica. "The states need to pass laws to make regulation tougher."

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