

Moody's Says Obama Plan Could Shaft Some Creditors

by National-Underwriter

President Barack Obama's financial regulatory reform plan could leave creditors, with subordinate claims against failing insurance holding companies, stuck with underperforming assets, a Moody's report said.

Under the proposal, if an insurance company were failing, the Office of National Insurance that would be created would consult with the Federal Reserve and the FDIC to determine which parts of the insurance group to support, Moody's noted.

It said the ONI would have the power to sell or transfer all or any part of the assets of the firm in receivership to a bridge institution or other entity. This means that a number of creditors, especially the most junior ones, could be left with the part of the original entity that holds the underperforming assets.

For insurers, the report notes the most prominent aspect is the proposal to create the ONI which would also gather information, develop expertise, and coordinate with domestic and international regulators.

Over time, the report noted the ONI and Treasury Department would consider modernizing and improving the current regulatory framework.

Moody's said it will wait and see how this scenario plays out as the proposal moves through Congress.

The ONI would also identify insurers to be regulated by the Fed as Tier 1 Financial Holding Companies (FHC), the report states. These firms would be expected to have overall stronger risk management practices, including a tighter match between asset and liabilities, Moody's said. As such, the report notes it may be harder for Tier 1 insurers to generate returns at pre-crisis levels.

But the report states that higher prudential standards could ultimately help these firms obtain funding at lower costs, which could potentially offset the lower earnings from a risk-adjusted point of view.

National oversight may also reduce insurers' flexibility with state regulators, with whom insurers have maintained strong relationships, said Moody's.

These relationships, the firm said, have allowed insurers to receive latitude in getting regulatory approval to extract dividends and/or assets from operating companies.

However, the report adds that downward rating pressure resulting from this reduced flexibility could be offset by the positive implications of a more consistent regulatory framework across institutions and products.

Regulatory uniformity, both nationally and internationally, could also make for a healthier, arbitrage-free competitive environment that would improve the comparability of firms and products and should culminate in a credit positive for policyholders and senior creditors, Moody's said.

The Moody's Special Comment report is titled "Preliminary Assessment of the Obama Administration's Regulatory Reform Proposal."

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