

- SUBJECT:** Continuation and operation of the Texas Department of Insurance
- COMMITTEE:** Insurance — committee substitute recommended
- VOTE:** 5 ayes — Smithee, Hancock, Hunter, Isett, Taylor
4 nays — Martinez Fischer, Deshotel, Eiland, Thompson
- SENATE VOTE:** On final passage, April 20 — 18-12 (Davis, Ellis, Gallegos, Hinojosa, Lucio, Shapleigh, Uresti, Van de Putte, Watson, West, Whitmire, Zaffirini)
- WITNESSES:** For — Beaman Floyd, Texas Coalition for Affordable Insurance Solutions; (*Registered, but did not testify:* Fred Bosse, American Insurance Association; Patricia Kolodzey, Texas Medical Association; Kandice Sanaie, Texas Association of Business; Annie Spilman, Independent Insurance Agents of Texas; Jay Thompson, AFACT; Joe Woods, Property Casualty Insurers Assn. of America)

Against — (*Registered, but did not testify:* Pamela J. Bolton, Texas Watch)

On — Chloe Lieberknecht, Sunset Advisory Commission; Jared Wolfe, Texas Association of Health Plans; (*Registered, but did not testify:* Joe Sanchez, AARP)
- BACKGROUND:** The Texas Department of Insurance (TDI), established in 1876, regulates the business of insurance in Texas to ensure that Texas consumers have access to competitive and fair insurance products. TDI regulates insurance companies' solvency, rates, forms, and market conduct. The department licenses individuals and entities involved in selling insurance policies and investigates and takes enforcement action against those who violate insurance law. Consumer-related functions include education about insurance and helping consumers resolve complaints. TDI also provides fire protection services.

The commissioner of insurance, appointed by the governor and confirmed by the Senate for a two-year term, directs department policy and operations. There is no policymaking body for TDI. At the end of fiscal

2007, TDI had 1,544 staff, including 828 dedicated to insurance-related activities. TDI is permitted 1,785 full-time equivalent positions, and its fiscal 2008-09 budget is about \$198 million.

TDI regulates all major insurance lines sold in Texas. Life, accident, and health lines include life, accident, health, annuity, credit, disability, and long-term care coverage. Property and casualty lines include protections for both private and commercial properties such as homes and vehicles, professional liability coverage, title insurance for owners of real estate, and workers' compensation. TDI has 14 statutorily-created advisory committees and councils that provide input on many of these insurance lines and other issues.

Preferred provider organizations (PPOs) contract with health care providers who provide health services to consumers according to reimbursement rates agreed to between the PPO and the provider. TDI has some authority over the benefit plans offered by PPOs and may regulate insurers or third-party administrators that own or contract with a PPO, but does not regulate independent PPOs as entities.

Most property and casualty insurance lines are subject to a type of rate and form regulation called file-and-use, in which insurers must file rates with TDI but may use the rates immediately once filed. The commissioner of insurance administratively may disapprove a rate deemed excessive, inadequate, or unfairly discriminatory before it has been implemented, or the commissioner may disapprove a rate-in-effect through a contested-case hearing. The commissioner may subject certain insurers to a prior approval process in which the commissioner must approve a rate or take no action to approve or disapprove a rate within 30 days of filing for a rate to take effect. Prior approval may be required only if the insurer's rates require supervision because of the insurer's financial condition or rating practices or there is a statewide insurance emergency.

TDI last underwent Sunset review in 1993 and was continued by the 73rd Legislature. If not continued by the 81st Legislature, TDI will be abolished September 1, 2009.

DIGEST: CSSB 1007 would continue TDI until September 1, 2021. The bill would add standard Sunset provisions governing conflicts of interest of the commissioner of insurance and agency staff, maintaining information

about complaints, use of technology to increase public access, and alternative rulemaking and dispute resolution procedures.

CSSB 1007 would add to the duties required of TDI protecting and ensuring the fair treatment of consumers and ensuring fair competition in the insurance industry in order to foster a competitive market.

Advisory committees. The bill would abolish all advisory committees established by the Insurance Code that did not have an expiration date and would transfer all their powers, duties, obligations, rights, contracts, funds, records, and property to TDI by February 28, 2010. The bill would make conforming changes to repeal references to these committees from the Insurance Code.

The commissioner would adopt rules regarding the purpose, structure, and use of advisory committees by the commissioner, the state fire marshal, or TDI staff, including rules governing an advisory committee's:

- purpose, role, responsibility, and goals;
- size and quorum requirements;
- qualifications for membership, including experience requirements and geographic representation;
- appointment procedures;
- terms of service;
- training requirements; and
- duration.

An advisory committee could not be responsible for rulemaking or policymaking. TDI periodically would evaluate an advisory committee to ensure its continued necessity. The department could retain or develop committees as appropriate to meet changing needs.

Regulation of independent preferred provider organizations. CSSB 1007 would define a preferred provider organization (PPO) as an insurer, third-party administrator, or other person that contracted with health care providers regarding reimbursements for health care services provided to enrollees of PPO plans. By November 1, 2009, the commissioner of insurance would adopt rules requiring an operator of a PPO, other than an insurer or third-party administrator already licensed by the Insurance Code, to hold a certificate of authority to organize or operate as a PPO in Texas. Unless a PPO held a certificate of authority as an insurer or third-

party administrator as of August 31, 2009, the PPO would be required to submit an application for a PPO certificate of authority not later than 60 days after the bill's effective date.

The bill would establish the requirements for applying for a PPO certificate of authority, including provision of the PPO's organizational documents, bylaws, listing of persons responsible for the PPO, and templates of any contracts to be made between the PPO and a health care provider. The applicant would pay a filing fee of up to \$1,000, to be credited to the TDI operating account, for application processing. The commissioner would approve an application if satisfied that granting the application would not violate federal or state law, the applicant did not attempt to obtain the certificate through fraud or bad faith, and the applicant had complied with TDI rules. Applicants for which application was denied would be provided a notice specifying the application deficiencies and the opportunity for a hearing to address the deficiencies.

The denial, suspension, or revocation of authority to act as a PPO would be subject to laws regarding professional conduct, disciplinary actions, and sanctions for license holders who were subject to the jurisdiction of TDI. The department would track and analyze complaints about PPOs.

Rate regulation for property and casualty insurance. The bill would revise rate regulation for property and casualty insurance lines, except those provided by certain exempted insurers or insurer's affiliates. The bill would specify that an insurer could use a rate on or after the date the rate was filed. The commissioner would establish rules for the process through which TDI would request supplementary rating and supporting information in conjunction with a rate filing, including the number of times TDI could request information and the types of information that could be requested.

The commissioner would have to disapprove rates that did not comply with statutory requirements before they took effect or within 30 days of the day the rate was filed. For good cause, the commissioner could extend the period for disapproval of a rate for an additional 30-day period. If the commissioner did not disapprove a rate prior to the date on which the rate took effect or the 30th day after the date the rate was filed, the commissioner could disapprove the rate only after a hearing.

TDI could request additional information related to rate filings, including those made by an insurer subject to prior approval. The time between the date TDI submitted a request and the date TDI received the requested information would not be included in the calculation of the 30 days TDI had to disapprove the rate.

If the commissioner determined, based on the findings of a required periodic assessment, that conditions no longer existed to subject an insurer to prior approval, the commissioner would excuse the insurer from prior approval. An order that specified the reasons the commissioner would subject an insurer's rate filings to prior approval also would explain any steps the insurer would be required to take or any condition that had to be met to be excused from the order. The commissioner would establish the financial conditions and rating practices that could subject an insurer to prior approval and the process by which the commissioner would determine there was a statewide insurance emergency.

TDI would track precedents related to disapprovals of rates filed by insurers subject to prior approval. TDI also would track, compile, and analyze the factors that contributed to the disapproval of rates and the volume and content of requests for additional information. TDI would make available to the public information concerning TDI's process and methodology for rate review, including disapproval of rates.

Subject to certain exceptions, an insurer group that accounted for less than four percent, rather than two percent, of the total amount of premiums collected by residential property insurers would be exempted from the full rate filing and approval requirements.

The revisions to rate regulation made by this bill would apply only to rates filed and insurers subjected to prior approval on or after September 1, 2009.

State Fire Marshal's Office. The state fire marshal periodically would have to inspect public buildings controlled by the Texas Facilities Commission as well as buildings leased to state agencies by the commission. Rules adopted for determining the schedule for inspection of state-owned and state-leased buildings would require adoption of guidelines for assigning fire safety risk and would require inspection of each of these buildings, regardless of a building's fire safety risk.

The bill would require the commissioner by rule to delegate to the state fire marshal the authority to take disciplinary and enforcement action, including the imposition of administrative penalties, against pyrotechnic operators and certain people licensed to provide certain fire-protection-related services. The rules would specify the types of disciplinary and enforcement actions delegated and a schedule of administrative penalties. The bill would specify the manner in which administrative penalties could be imposed and how a person could dispute the imposition of an administrative penalty.

A property owner or building occupant who requested an inspection by the fire marshal could be charged a reasonable fee.

Examination of title insurance agents. The bill would establish requirements for TDI to examine each title insurance agent and direct operation licensed in Texas, including which information would be examined. The Texas Title Insurance Guaranty Association would pay fees and reasonable expenses that TDI incurred in examining a title agent or direct operation.

CSSB 1007 would specify the manner in which the examination would be conducted and the frequency with which examinations could occur. The examiner would have free access to all books and papers related to the business of the person being examined and could examine under oath an officer, agent, or employee of the person. A title agent or direct operation could be subject to disciplinary action for failure to comply with an examination request.

The bill would establish TDI's authority with respect to use and release of a final or preliminary examination report of the title insurance agent or direct operation and related documents. These reports and related documents would be confidential and not subject to public disclosure. At least every five years, the commissioner would evaluate if TDI needed additional information examined to promulgate title insurance rates.

Engineers for windstorm inspections. TDI would be required to contract with, rather than appoint or employ, engineers who conducted windstorm inspections. The bill would require TDI to:

- establish procedures for contracting with and oversight of windstorm inspectors;

- compile a list of qualified, contracted inspectors; and
- report possible licensing violations by the inspector to the Board of Professional Engineers.

Electronic transactions. The bill would authorize entities regulated by TDI to conduct business electronically if each party to the business agreed to do so. The business would be required to be conducted in accordance with rules adopted by the commissioner.

Data collection for personal auto or residential property insurance. Personal automobile and residential property insurers would be required to file aggregate claims information for a filing period, including the number of claims:

- filed during the reporting period;
- pending on the last day of the reporting period;
- closed with payment and closed without payment during the reporting period; and
- carrying over from the preceding reporting period.

TDI would post aggregate data on its website in a manner that did not reveal proprietary or trade secret information.

The bill would take effect September 1, 2009. Unless otherwise specified, the provisions of this bill would apply to insurance policies, contracts, or evidences of coverage delivered or renewed on or after January 1, 2010.

**SUPPORTERS
SAY:**

CSSB 1007 would implement revisions, including a number of recommendations of the Sunset Advisory Commission, that would improve the operations of the Texas Department of Insurance. The bill would clarify the regulation of property and casualty rates under the file-and-use system, providing insurers more certainty about the acceptance of rate filings and the condition under which rates could be denied. Unnecessary advisory committees would be abolished, and the commissioner of insurance would be granted the flexibility to establish advisory committees as needed by rule.

By requiring PPOs to obtain a certificate of authority to operate in Texas, TDI would have more information about the operation of these entities and could take enforcement action against them as necessary. About 4.5

million Texans are insured through PPO plans, and TDI needs a mechanism to protect these consumers against financial and medical harm.

The bill would provide the commissioner of insurance with more data with which to promulgate title insurance rates, and examinations of title agents would assess their financial solvency.

Regulation of property and casualty rates. The bill would bring clarity to the file-and-use system, in which insurers rarely file and use rates immediately for fear of the legal and administrative costs they could incur if rates later were disapproved. Contested case hearings are costly to conduct, and insurers must justify their rates against the findings of actuaries from both TDI and the Office of the Public Insurance Counsel. Costs increase further if an insurer must appeal a rate ruling to a district court. In 2008, only 12.6 percent of homeowners' insurers actually filed and began to use new rates on the same day.

The bill would strengthen the existing prior approval processes by giving TDI rulemaking authority to establish the processes and standards by which an insurer could be placed under prior approval. In 2007, about 45 percent of homeowners' insurers were subject to prior approval. CSSB 1007 would require the commissioner to establish the financial conditions and rating practices that could subject an insurer to prior approval, and to provide disclosures to insurers on how they could be freed from prior approval.

The file-and-use system proposed in this bill would be better for consumers than a full prior approval regulatory system because it would enhance market competition. A healthy, competitive insurance market with many participating insurers is the best way to ensure companies strive for efficiencies to keep costs down and to keep rates low enough to attract a large consumer base. File-and-use allows insurers to assess risks and immediately begin use of an actuarially justified rate. Prior approval systems allow the state regulatory agency to interfere in an insurer's implementation of rates that an insurer has deemed will keep the insurer solvent with a reasonable buffer to guard against annual fluctuations in claims filings.

The insurance industry is based on assessment of risk, and insurers must assess a variety of consumer, environmental, and regulatory standards, as well as the performance of the financial market when setting rates. A prior

approval system would introduce yet another risk to an insurer because the insurer would not know if insurance regulators would approve the rates. This could lead to worse outcomes for consumers because insurers would try to set higher rates to account for the higher risk and also could decide to exit the market or reduce the number of policies they wrote to avoid losses. The regulatory history of the Texas insurance market demonstrates the trend of significant declines in insurer participation when regulation is increased, and reduced competition leads to higher rates for consumers. While efforts to increase regulation are well-intended, they lead to worse consumer outcomes.

The biggest risk to consumers would be to regulate insurer rates such that insurers became insolvent and could not pay consumer claims following a catastrophe because state regulators had prevented the insurer from establishing an adequate reserve. Although insurer profits were very high in 2006 and 2007, the reserves generated from business during those years allowed many insurers to stay in business despite the extreme natural-disaster-related losses they paid in consumer claims for 2008.

Commissioner of insurance. The insurance commissioner should be an impartial regulator, not an elected official. The best way for an insurance commissioner candidate to appeal to citizens would be to run on the premise of lowering insurance rates, yet the market does not always safely allow this goal. An insurance commissioner elected with the mandate to lower rates could implement policies that could jeopardize insurer solvency.

Regulation of forms. By allowing insurers to file different forms, market competition would be enhanced not only through pricing differences but also through product offerings. Uniformity in forms can lead to property owners paying for coverage they did not need rather than selecting a plan at the price and coverage level they desired.

Credit-scoring. Those who seek to abolish the use of credit rating in establishing premiums make the inaccurate assumption that the industry is indicating that a low credit-score increases the likelihood of poor driving. However, credit-scoring has proved an accurate way to measure risk, because studies consistently have demonstrated that people with low credit ratings have a greater likelihood of making a claim when other consumers may have chosen not to. Whatever the factor that drives the risk

association between credit and claim rates, insurers should be able to measure this indicator of risk.

OPPONENTS
SAY:

CSSB 1007 would not take advantage of the opportunity to revise processes at TDI in the interest of consumer protection.

Regulation of property and casualty rates. This bill would continue the file-and-use system that would allow insurers to file notice of a rate change with TDI and begin to use that rate immediately. TDI could not disapprove a rate-in-effect, even if deemed unfair or excessive, without an administrative hearing and possible appeal to a district court. Insurers should not be allowed to deem whether their own rates were fair. The file-and-use system was supposed to decrease Texas' insurance rates, which are the highest in the nation, yet this system has not lived up to this expectation.

Implementing a prior approval system would allow TDI to review and approve all rates before they were passed along to policyholders. Insurers could not enact steep rate increases and engage in price gouging to recoup losses too rapidly. Prior approval places the burden of proof on the insurer to justify that their rate filings were necessary and justified.

The insurance market is not a standard competitive marketplace because consumers in some instances are mandated to obtain coverage or may greatly need the benefits of coverage. This environment necessitates rate review so that insurers do not take advantage of consumer vulnerability.

Regulatory interventions do not influence the amount of market participation to the extent that some file-and-use proponents claim. Before 2003, when there were benchmark rates, insurers were not allowed to have different rating tiers. Because of this, insurers spun off affiliates so that each affiliate could act as a surrogate for a rating tier. These affiliates no longer were needed when regulatory changes were made in 2003, and many affiliate operations were ceased. The actual decline in insurer group participation was negligible, even if the total number of companies seemed to decrease significantly.

Commissioner of insurance. While the commissioner directs policy that influences homeowners, patients, and other consumers, the commissioner only is accountable to the governor. Many more Texans are affected by the actions of the insurance commissioner than by the actions of the elected

agriculture and railroad commissioners, yet Texans do not have a say in choosing their insurance commissioner. Eleven other states allow their citizens to have a say in who would best govern a fair insurance market through election of their insurance commissioners, and Texans should have this ability too.

Regulation of forms. This bill should have required homeowner's policies to offer standard coverage. When consumers are offered the same policies by different insurers, they easily may shop the market by comparing the prices offered by different insurers. Today, it is difficult if not impossible for consumers to interpret and compare complex and differentiated policies to determine appropriate, cost-effective coverage. Today's homeowner's policies provide much less coverage than they provided under standard forms, but rates have not dropped correspondingly to reflect the decreased coverage.

Credit-scoring. Texas should not allow the use of credit scores in setting rates. Credit scores are determined based on a person's payment history, amounts owed, length of credit history, new credit, and types of credit. None of these criteria reflects the measure of risk associated with a consumer's driving behavior. Many consumers unfairly have faced rate increases solely based on their credit score when they never have filed a claim.

NOTES:

The fiscal note indicates no impact to general revenue funds during fiscal 2010-11 because TDI is required to generate revenues equal to its costs of operation.