

# Issue Brief

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## Rate Modernization, Underwriting Freedom to Top 2006 State Legislative Activity

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### Introduction

State legislatures have begun to convene for the year, and lawmakers already are facing more than 3,000 active, carryover or prefiled bills. That number will increase dramatically in the next few months with legislatures in 44 of the 50 states in session. The Arkansas, Montana, Nevada, North Dakota, Oregon and Texas legislatures are not meeting.

Legislation will again be affected by election-year politics. Thirty-six gubernatorial races will be contested in November 2006 with Arkansas, Colorado, Florida, Idaho, Iowa, Massachusetts, Nevada, New York and Ohio holding “open” races. Insurance commissioners will be elected in California, Georgia, Kansas, Oklahoma and Washington. Notably, the California contest will be an “open” race as Commissioner John Garamendi intends to run for lieutenant governor. In Florida, the position of chief financial officer, who oversees the Office of Insurance Regulation, will be an “open” race since current CFO Tom Gallagher is running for governor.

The following is a preliminary assessment of nine key issues that the NAMIC advocacy staff will be focusing on across the country in 2006. This report was compiled with the help of the association’s five State Affairs Managers (SAMs), in collaboration with their state trade association advocacy partners.

### Rate Modernization

This issue continues to be a priority for NAMIC, and at this point, it appears at least six states may deal with rate modernization reforms in 2006. In **Hawaii**, a legislative panel has been examining whether to modernize its rating provisions. NAMIC anticipates that a flex-rating bill and/or a “speed-to-market” regulation or legislation will be offered during the session.

By contrast, NAMIC and our advocacy partners continue to oppose anti-competitive legislation unveiled earlier this year by **Michigan** Gov. Jennifer Granholm to impose a 20 percent rate rollback in auto and homeowners insurance and to remove the provision in existing law that would eliminate the requirement that a lack of competition must exist for rates to be deemed excessive.

In **Massachusetts**, the Romney administration has pushed hard for legislation to introduce competitive rating to the auto insurance market, but the fate of the proposal is uncertain due to several factors, including a substantial rate reduction and regulatory changes aimed at reducing inequities in the high-risk pool.

In **New York**, the state trade is planning to push for comprehensive modernization legislation that would allow insurers to file and use rates and forms in markets deemed to be competitive.

**Indiana** and **Iowa** are both looking at less restrictive language for commercial lines. And, **Connecticut** may see flex rating proposals this year similar to the NCOIL model.

### **Underwriting Freedom**

Bills that would impose limitations on the use of insurance scoring or loss-history reports are likely to continue to be introduced this year. A preliminary assessment by the SAMs shows that as many as 40 states may introduce bills. While a few states may continue efforts to prohibit insurance scoring outright, most bills are likely to seek restrictions where individuals may be involved in “extraordinary life circumstances.”

As the industry continues to monitor efforts to ban the use of credit-based insurance scoring, NAMIC’s advocates will be paying particularly close attention to Michigan in 2006. Early in 2005, the Michigan Office of Financial and Insurance Services (OFIS) promulgated an administrative rule prohibiting insurance companies from providing lower rates to policyholders with good credit.

The industry, including NAMIC, filed suit contending OFIS overstepped its authority in issuing the rule. In April, a Barry County Circuit Court judge ruled in the industry’s favor finding the rule to be “illegal, invalid and unenforceable.” The OFIS appealed and the case is currently pending before the state Court of Appeals.

In October, Gov. Granholm, who is up for reelection this year, unveiled a package of anti-competitive legislative proposals including a bill calling for a ban of the use of credit-based insurance scoring. As of this writing, the bill has yet to be introduced.

### **Preventing the Application of SOX to Non-Public Insurers**

NAMIC continues to oppose efforts by the NAIC to extend the Sarbanes-Oxley Act’s Section 404 content on internal control to mutual insurers via the NAIC’s Model Audit Rule.

In December, an NAIC subgroup adopted a so-called “alternative” proposal that would lower aggregate first-year compliance costs for non-public insurance companies from \$300 to \$80 million. Most property/casualty companies are spared altogether

from any increased audit burden and accompanying costs. The alternative proposal will now be considered by the NAIC-AICPA Working Group in March, but NAMIC remains opposed to the proposal.

However attractive the alternate proposal might be, NAMIC believes that it is still subject to change by regulators who are on record as seeking greater SOX-like regulation for non-public insurers, regardless of logic or costs. A scaled-back version of the original initiative, if approved by the NAIC and placed into state law, would exist as an attractive target for regulators to build on in the future.

Similarly, insurers already in compliance with SOX (SEC registrants for the most part) have demonstrated little sympathy, with the arguments that the addition of 404 measures to state solvency regulation for all insurers is unwarranted. Indeed, this has been a recurring theme or problem in discussions among industry representatives regarding compromise with the regulators. This division increases the possibility that further negotiations, given the participation of SEC registrants, may result in more stringent requirements for non-public insurers.

NAMIC’s position has received vital support from Chairmen Michael Oxley and Richard Baker of the U.S. House Financial Services Committee as well as the National Conference of Insurance Legislators and the American Legislative Exchange Council.

### **Guaranty Fund Reforms**

For the second year in a row, NAMIC has joined forces with the National Conference of Insurance Guaranty Funds (NCIGF) and the other national property/casualty trade associations to work collaboratively on seeing various guaranty fund provisions enacted in a number of states. This year, much of those efforts will be focused on states expected to act on the new Insurer Receivership Model Act (IRMA) that was adopted by the NAIC in December.

IRMA makes changes to the model in several areas, including intervention of state guaranty associations, receiver financial reporting requirements, jurisdiction of the receivership court, priority of guaranty association expenses and settlement of reinsurance balances.

States likely to introduce IRMA legislation include: **California, Florida, Illinois, Michigan, New Jersey, New York, Pennsylvania, Utah and Virginia.**

### Finite Reinsurance

When the NAMIC state advocacy agenda was developed, it appeared finite reinsurance might be an issue ripe for possible legislative activity in 2006. However, insurance commissioners adopted a set of disclosure provisions in October that apply to finite reinsurance. Insurers will be required to report to state insurance regulators any finite reinsurance agreement that has the effect of altering policyholders' surplus by more than three percent, or representing more than three percent of ceded premium or losses.

Additional reporting requirements regarding contract terms and management's intention in entering the contract have been included to improve transparency. These provisions will apply to the 2005 annual statement.

No legislative activity is contemplated at this time as most states adopt by reference any new annual statement requirements.

### Security Breach Notices

Twenty-one states enacted security breach notification laws in 2005, making it one of the most active types of legislation seen across the country. That level of activity is not likely to subside this year. As many as 33 states are expected to introduce bills, including **Maine** and **New Jersey**, which intend to re-visit the issue after passing legislation this year.

Last fall, the National Association of Attorneys General (NAAG) sent a letter to members of Congress outlining what provisions its organization wished to see in a possible federal security breach law. So far, congressional activity on this issue largely has been confined to different lawmakers introducing bills, but little committee activity. The AGs are likely to weigh in on state bills and insist on more control over penalties imposed on business entities that have security breaches.

NAMIC has joined a "loose" coalition of financial services entities that are monitoring state bills. One issue of concern is the provision requiring a business entity to report a breach to consumer-reporting agencies. This is problematic for multi-state businesses because the states that have adopted this provision each require a different notice trigger.

### Market Conduct Reform

**Missouri** could see market conduct related reforms

this coming year. The self-evaluative privilege bill that nearly made it through the legislature last year likely will be re-introduced. The Department of Insurance has proposed a bill to eliminate the 15 percent "administrative" charge imposed on insurers that receive market conduct exams. The lost revenue presumably would be replaced by changing other departmental fees. NAMIC is still reviewing the DOI proposal.

Other states considering interest in addressing market conduct laws are likely to delay bill introductions since NCOIL agreed at its annual meeting in November to re-open debate on its model act. Most trade associations, including NAMIC, favor a version of the NCOIL model that was adopted in February 2004 before amendments subsequently were added by the NAIC in June 2004.

### Asbestos Reform

At least four states – **Illinois**, **Michigan**, **Missouri** and **West Virginia** – are expected to tackle asbestos reform this year. In Michigan, lawmakers began deliberations on a bill in 2005, and it is expected to carryover to this year.

The proposals will define a process for identifying and prioritizing claimants as other state enacted laws have done.

### Farm Mutual Modernization

**Illinois** and **Tennessee** may see farm mutual legislation this year, with the most dramatic changes coming in Tennessee, where NAMIC and the Tennessee Association of Mutual Insurance Companies have been working with the Department of Insurance on a rewrite of the state's county mutual statute. Among other things, the new proposal calls for new annual statement reporting requirements and the licensing of any agents connected with the county mutuals. In return, the county mutuals would have the ability to expand their coverages and the geographic boundaries where they can sell their products.

### Emerging Issues

The NAMIC SAMs are also tracking several other issues that likely will emerge during the 2006 legislative session. Chief among them is whether states affected by the 2005 hurricane season (Alabama,

Florida, Louisiana and Mississippi) will enact stronger building codes.

NAMIC already has joined a coalition of insurers in Mississippi who are hoping to persuade lawmakers to adopt a statewide building code similar to the one enacted by Louisiana in October.

Hawaii is also considering this issue, and currently has a legislative task force studying the various building codes on the different islands.

Florida lawmakers are likely to see a bill that attempts to eliminate the exemption from the statewide building code that the counties in the Panhandle enjoy. Lawmakers are also likely to deal with revisions to its high-risk carrier, Citizens Property Insurance Corporation.

Other issues include: local government emergency service fees, correcting court decisions viewed as misguided by the industry, certain traffic safety issues, construction defect and/or contractor liability issues, no-fault auto laws, event data recorders and workers' compensation reforms.

For additional information on any of the legislative initiatives listed in this Issue Briefs, please contact Senior State Advocacy Director Neil Alldredge at (317) 875-5250, ext. 1103, [nalldredge@namic.org](mailto:nalldredge@namic.org) or any the state affairs manager directly.

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