Texas Department of Insurance

Biennial Report to the 83rd Legislature

December 2012

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Commissioner of Insurance

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The Honorable Rick Perry, Governor
The Honorable David Dewhurst, Lieutenant Governor
The Honorable Joe Straus, III, Speaker

Dear Governors and Speaker:

In accordance with Section 32.022 of the Texas Insurance Code, I am pleased to submit the biennial report of the Texas Department of Insurance. The report summarizes needed changes in the laws relating to regulation of the insurance industry.

We are available to discuss any of the issues contained in the report and to provide technical assistance. Please contact me or Melissa Hamilton, Director of Government Relations, at 463-6123 with any questions or if you need additional information. Thank you for your consideration.

Respectfully submitted,

Eleanor Kitzman

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Commissioner of Insurance

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Texas Department of Insurance
Agency Overview and Update

Governance: TDI Commissioners

The commissioner of insurance is the chief executive of the Texas Department of Insurance (TDI), and the commissioner of workers' compensation serves as the chief executive for TDI's Division of Workers' Compensation (DWC). The governor appoints both commissioners subject to Senate confirmation. The commissioner of insurance and commissioner of workers' compensation regulate the Texas insurance industry and workers' compensation system, respectively, by administering and enforcing the applicable laws. The Texas Insurance and Labor Codes fully define TDI's regulatory authority, and the agency's regulatory rules are contained within the Texas Administrative Code.

TDI's mission is to protect insurance consumers by regulating the insurance industry fairly and diligently, promoting a stable and competitive market, and providing information that makes a difference.

Leading at state, national, and international levels

TDI has increased its leadership role within the National Association of Insurance Commissioners (NAIC) and International Association of Insurance Supervisors (IAIS). TDI leads or is an active participant in 44 NAIC committees and subcommittees and in four IAIS subcommittees and work groups. Our enhanced participation will enable Texas to be at the table during development and negotiation of national and international insurance regulation standards and to ensure that regulatory policymakers consider the Texas regulatory environment.

The most effective form of consumer protection is a strong, competitive, stable insurance marketplace. Therefore, TDI reallocated resources to its financial solvency function. This will improve our ability to financially monitor insurers, to detect problems early, and to ensure that insurers pay policyholder claims in a timely manner.

TWIA

Texas law establishes several quasi-governmental entities that are regulated by TDI, most notably, the Texas Windstorm Insurance Association (TWIA). TWIA was placed under administrative oversight on February 28, 2011, where it remains today.

TWIA's administrative oversight was amended August 7, 2012, and the consultant firm of Alvarez and Marsal Insurance Advisory Service, LLC (A&M) was retained by TDI to manage all of TWIA's claims for events occurring on or before December 31, 2011, and to explore options for restructuring TWIA. A&M subsequently released a report with the results of their evaluation, and a copy of the report is available on the TDI website.

As A&M's work progressed, it became evident that certain options, which would require legislation, should be considered. In addition, TWIA's current funding structure, which utilizes bonds, is untenable because no market currently exists for the bonds. The results of the A&M report, along with funding concerns, indicate a need for the Texas Legislature to take a closer look at TWIA and its long term sustainability. TDI will continue to devote significant resources to help TWIA and looks forward to working with the Texas Legislature and other stakeholders. Additional commentary and legislative considerations regarding TWIA are found on page 31 of this document.

Workers' Compensation

TDI-DWC administers the workers' compensation system, enforces the Texas Workers' Compensation Act and rules, administers the certified self-insurance program for individual employers, and resolves claim-level disputes about medical and income benefits.

The Texas workers' compensation system has undergone significant changes since the passage of House Bill (HB) 7 in 2005. Since 2005, DWC has implemented several initiatives to reduce and stabilize claim costs and improve injured employee outcomes (such as quality of care, access to care, and return-to-work outcomes). These initiatives include:

- adopting evidence-based treatment and return-to-work guidelines;
- adopting a closed pharmacy formulary – one of the first in the nation for workers' compensation;
- implementing a new enforcement structure to help align DWC enforcement activities with the rest of TDI;
- implementing changes to income benefits, including new work-search requirements for employees eligible for supplemental income benefits;
- streamlining dispute resolution processes and reducing the amount of time it takes to resolve income, medical fee, and medical necessity disputes;
- developing a performance-based oversight program to monitor health care providers and insurance carriers on key performance measures;
- implementing Medicare-based fee guidelines for professional services, inpatient and outpatient hospital services, and ambulatory surgical center services; and
- implementing a return-to-work reimbursement program for Texas employers.

As a result, Texas employers now have lower workers' compensation insurance rates, stabilized claims costs, and better return-to-work outcomes. Texas employees have improved access to quality medical care that helps them return to work quickly and safely. The Sunset Advisory Commission recently reviewed DWC and made several recommendations to align the regulatory authority of the Commissioner of Workers' Compensation with the Commissioner of Insurance; enhance DWC's enforcement authority, streamline the medical and indemnity dispute resolution processes; enhance DWC's oversight over designated doctors; and improve DWC's medical quality review process to improve oversight over medical care provided in the Texas workers' compensation system. Based on the Sunset review, the 82nd Texas Legislature passed HB 2605 in 2011. DWC has fully implemented HB 2605.

The remainder of this report sets forth TDI's legislative recommendations to the 83rd Legislature, as well as additional issues that the Legislature may wish to consider.

Recommendations

Financial

ORSA

Background:
TDI regulates both insurance carriers and the relationships between insurance carriers and their affiliates. TDI also monitors the financial condition and risk profiles of holding company systems or "groups" of affiliates. This is a foundational component in TDI's solvency regulation of insurance carriers, because risks posed by non-insurance operations can potentially spread to insurance companies and negatively impact their financial condition. The NAIC recently adopted the Own Risk Solvency Assessment (ORSA) Model Act in response to lessons learned from the global financial crises, as well as discussions held at the international level about group supervision. An ORSA is an internal assessment of the risks associated with an insurer's or insurance group's current business plan and the sufficiency of its capital resources to support those risks. The new NAIC model act requires insurance companies or insurance groups to perform their own risk and solvency assessment ORSA and to file an ORSA summary report with insurance regulators.

Issue:
Adding a requirement for certain insurance carriers to file ORSA summary reports with TDI will improve TDI's understanding of large insurance carriers and their holding company systems and will provide TDI with a group-level perspective on risk and capital. This would also enhance TDI's ability to participate in the supervision of insurers and insurance groups domiciled in multiple jurisdictions and improve regulatory coordination at the national and international levels. ORSA summary reports would provide TDI with a necessary tool to evaluate the financial condition of the largest insurance companies in order to better protect Texas policyholders.

Recommendation:
- Amend the Texas Insurance Code by adding a new chapter based on the *NAIC Risk Management and Own Risk Solvency Assessment Model Act*. The NAIC Model Act language is recommended in order ensure uniformity and consistency in regulatory requirements from state to state, which is important for insurance carriers with multistate operations.
    - The new recommended Code chapter should require large insurers and insurance groups to maintain a risk management framework; to regularly perform an ORSA; and to annually file an ORSA summary report with the commissioner. The report should also be available upon request.
    - The new chapter should also provide an exemption from these requirements for smaller insurers and insurance groups, address the confidentiality of the ORSA Summary Report, and outline other filing requirements.

Financial

Information-Sharing

Background:
Under certain circumstances, Texas law allows TDI to share confidential and/or privileged information about insurers with other insurance regulators. These laws include Texas Insurance Code, sections 32.023 and 823.011. Section 823.011 requires TDI to verify that the entities with whom it seeks to share information have laws that provide at least the same confidentiality protections as Texas law. These information-sharing provisions are important for TDI to coordinate with other jurisdictions in the supervision of groups of affiliated carriers and to monitor the solvency and financial condition of large insurers and groups that operate in multiple jurisdictions.

Issue:
Current Texas law does not provide a single, uniform information-sharing statute that allows TDI to share confidential or privileged information with other jurisdictions and which also protects the confidential or privileged nature of information TDI receives from other jurisdictions. Instead, TDI's authority for sharing and receiving confidential information exists in isolated sections throughout the Texas Insurance Code with variable requirements. This lack of uniformity obscures TDI's full authority to share information under the Texas Insurance Code and presents a challenge for the regulation of carrier groups. Specifically, just as TDI must verify the legal authority of another jurisdiction to maintain the confidential or privileged nature of the information before we can share information, other jurisdictions also must, in accordance with their laws, verify that TDI can maintain the confidential or privileged nature of the information it receives. This verification is often difficult, especially for international jurisdictions, because of the many and variable provisions regarding information sharing under the Texas Insurance Code.

Many lessons were learned following the downturn in the global economy after 2007. Clarifying and standardizing TDI's information-sharing authority would enable TDI to more effectively and efficiently supervise large insurers and groups of affiliated carriers. It would also enable TDI to better protect Texas policyholders from systemic and group-wide solvency and financial issues that can adversely impact large insurers and groups of carriers that operate in multiple jurisdictions.

Recommendation:
- Amend Chapter 32 of the Texas Insurance Code to add a section that would clarify and standardize TDI's authority to share and receive confidential and/or privileged information about the financial condition of an insurer or insurance group that operates both in Texas and in other jurisdictions. This new section would not create any new type or class of confidential information. Rather, it would address the treatment of information that is already confidential as a matter of law.
    - The new section should provide that the commissioner may, at the commissioner's sole discretion, share confidential or privileged information about the financial condition of an insurer or group of affiliated carriers with an insurance regulator or analogous financial

regulator in another jurisdiction for any legal or regulatory purpose if the commissioner verifies that:

  - the regulator has the legal authority to maintain the confidential or privileged nature of the information shared;
  - the other jurisdiction enters a written agreement to protect the confidentiality of the information shared; and
  - the insurer or insurance group to which the information pertains operates in the regulator's jurisdiction.

- The new section should also provide that TDI may receive similar confidential or privileged information from another jurisdiction and that the information received maintains the privileged or confidential status it had under the laws of the jurisdiction that shared the information. Additionally, the new section should provide that the commissioner may enter into information-sharing agreements, as appropriate, if those agreements comply with standards of the new section and would facilitate the sharing between jurisdictions.
  - TDI needs an enhanced ability to receive confidential information from other jurisdictions in order to improve TDI's capacity to effectively fight fraud in the state. This especially important given the sheer size of the Texas market. As the 12th largest insurance market in the world, a level of fraud is inherent in Texas.

Financial

Captives

Background:

Many other states and foreign jurisdictions have laws that provide for the formation of captive insurance companies. A "captive" generally refers to an insurance carrier that insures the risks of its owners. Under this model, the owners may participate in decisions that affect the management of the captive. While there are many different types of captives, the most traditional form is called a pure captive. A "pure captive" is typically owned by a large corporation, such as a Fortune 500 company, and is a form of self-insurance. Although there are some differences, the regulation of a pure captive is similar in many ways to the regulation of a traditional insurance carrier. Insurance commissioners in states that license captives typically have some discretion to set the captive's minimum financial requirements based on the financial strength of the captive's owner (parent). Captives often benefit from lower premium tax rates.

Issue:

There are many Texas-based corporations that may desire to form their own captives. Current Texas law, however, does not authorize the formation of a captive insurance carrier in Texas. As a result, a Texas based corporation must form its captive in another state or offshore. This involves additional expenses and administrative burdens because other states and jurisdictions typically require captives to:

- engage locally based management companies or other professionals;
- hold a minimum number of board meetings within their jurisdictions each year; and
- appoint a local resident to the board, resulting in increased compensation costs.

Moreover, an apparent unintended consequence of the federal Dodd Frank Act has had a chilling effect on the use of captives domiciled in other jurisdictions due to potential tax implications.

An opportunity exists to further enhance Texas' pro-business climate. Allowing the formation of Texas domestic captive insurance companies could help attract new businesses and retain existing Texas companies. In addition to touting the current benefits that Texas has to offer, Texas-based Fortune 500 and other corporations could benefit from reduced costs and administrative burdens related to their captive operations.

Recommendation:

- Add new provisions to the Texas Insurance Code to provide for the formation of Texas-based pure captives. The law could be modeled after other states to include a limited number of favorable financial incentives for pure captives and to provide for a reduced premium tax rate. This recommendation would address all of the issues noted above and would allow captives to be used for their intended purpose. This recommendation would also result in some additional tax revenue for Texas.

Special Note: The above recommendation is specifically limited to enacting laws that authorize the creation of pure captives by and for the benefit of Texas based corporations, such as Fortune 500 companies. TDI does not recommend (i) allowing the formation of other types of captives, nor (ii) allowing captives that fail to have a nexus to Texas.

Financial

Outdated and Inconsistent Provisions in Current Law:

(1) Clarify that the pre-licensing examination of an insurance claims adjuster must be held in a classroom setting.

Background:
Section 4101.056 of the Texas Insurance Code allows the licensing examination of adjusters to be performed in a private setting with limited oversight.

Issue:
Individuals obtaining all other types of licenses, including insurance agents, must complete the licensing examination in a proctored, controlled testing center environment.

Recommendation:
Amend Section 4101.056 to require that the adjuster licensing examination be held in a proctored, controlled testing center environment to create consistency for all license types.

(2) Eliminate the requirement that a licensed surplus lines agent also hold a property and casualty license.

Background:
Section 981.203 of the Texas Insurance Code requires a licensed surplus lines agent to hold an underlying property and casualty license.

Issue:
This requirement is inconsistent with the NAIC Producer Licensing Uniformity Guidelines related to surplus lines licenses. This requirement is also inconsistent with the laws of other states. As a result, Texas cannot accept certain surplus agent's licenses from other states and is therefore not as attractive to surplus lines agents as other states.

Recommendation:
Amend Section 981.203(a)(1)(B)(i) to remove the requirement for an underlying property and casualty license.

(3) Reconcile differences where Chapter 981 of the Texas Insurance Code is preempted by the Non-admitted and Reinsurance Reform Act (NRRA) for surplus lines.

Background:

Several provisions of Chapter 981 of the Texas Insurance Code conflict with and are preempted by the NRRA, which is a federal law that became effective on July 21, 2011. The NRRA addresses both non-admitted insurance and reinsurance. Non-admitted insurance is more commonly known as surplus lines insurance.

Issue:

The preemption of Chapter 981 by the NRRA creates confusion for surplus lines agents, insurers, and consumers.

Recommendation:

Amend Chapter 981 to limit the applicability of the section to insurance that is issued to an insured whose home state is Texas; exempt certain commercial purchasers from specified restrictions on the purchasing of surplus lines insurance; and address non-admitted insurer eligibility issues.

(4) Remove the requirement that the commissioner approve or deny a substitution or withdrawal of a security held as a statutory deposit by a formal order.

Background:

Section 406.006 of the Texas Insurance Code requires the commissioner to approve or deny a substitution or withdrawal of a statutory deposit by order.

Issue:

The current law requires approval or denial by a commissioner order, which is a formal and labor intensive process. By removing the formal requirement of a commissioner order and allowing for a TDI letter to serve as an approval or denial, the process would be more efficient while maintaining the same approval or denial authority and improving overall customer service.

Recommendation:

Amend Section 406.006(d) to delete the requirement that approvals or denials of a substitution or withdrawal of a security must be by a commissioner order and allow the approval or denial of a substitution or withdrawal of a security held in special deposit by a TDI letter.

(5) Remove the requirement of a $50,000 statutory deposit for general casualty companies.

Background:

Section 861.252 of the Texas Insurance Code requires general casualty companies to deposit $50,000 in cash or securities with TDI as a statutory deposit.

Issue:

Other lines of insurers are not required to make similar deposits, and the requirement is so minimal that it is virtually meaningless. Additionally, TDI has the authority to require deposits for hazardous financial conditions, which means that these companies have adequate regulatory oversight.

Recommendation:

Amend Section 861.252 to remove the requirement for a $50,000 statutory deposit for general casualty companies.

(6) Amend and delete requirements that TDI approve policyholder dividends before companies can pay them.

Background:

Chapters 403 and 1806 of the Texas Insurance Code require TDI to approve policyholder dividends by order before companies pay them.

Issue:

Under the current statute, TDI reviews and issues orders on all distributions regardless of the proportion of the distribution to the financial condition of companies. Most of the policyholder dividend filings TDI has received in the past are minimal compared to the financial condition of companies. Additionally, the current statute requires a multi-level administrative process, causing delays in the distribution of dividends to policyholders.

Recommendation:

Amend sections 403.001, 1806.056, 1806.057, 1806.106, 2052.004, 1806.058(b), 403.002(b), and 1806.105(c)(2) of the Texas Insurance code to establish a threshold that the annual policyholder dividend amount must exceed before a company must obtain prior approval from TDI. For policyholder dividends that do not meet the threshold, notice must be provided to TDI 10 days prior to the payment.

Regulatory Policy

Refund of Premium:
Homeowners and Personal Automobile Insurance Policies

Background:
Section 558.002 of the Texas Insurance Code requires carriers to "promptly refund" premium owed to policyholders upon the cancellation of a policy. This money is commonly known as "unearned premium." While Section 558.002(b) requires insurers to "promptly refund" the unearned premium, the section does not define "promptly refund" nor does it specify time limits for insurers to refund unearned premium to consumers.

Issue:
TDI receives hundreds of complaints annually from consumers regarding the length of time it takes insurers to refund their unearned premium following a policy cancellation. As a result, TDI often has to step in to resolve complaints between policyholders and carriers. In calendar year 2010, TDI received 438 complaints relating to refund of premium for personal automobile and homeowners insurance, 461 complaints in calendar year 2011, and 445 complaints thus far in calendar year 2012.

Recommendation:
- Amend Section 558.002 to require insurers to return unearned premium to consumers on homeowners and personal automobile insurance policies within 15 business days from the effective date of cancellation.

Regulatory Policy

Outdated and Inconsistent Provisions in Current Law: Uninsured/Underinsured Motorists Coverage (UM/UIM) – *Stracener* Case

Background:

Section 1952.103 of the Texas Insurance Code states: "underinsured motor vehicle" means an insured motor vehicle on which there is collectible liability insurance coverage with limits of liability for the owner or operator that were originally lower than, or have been reduced by payment of claims arising from the same accident to, an amount less than the limit of liability stated in the underinsured coverage of the insured's policy.

Until 1989, the courts in Texas took the position that, where the individual responsible for the harm had liability limits that equaled or exceeded the limits provided under the affected party's underinsured motorist coverage, the affected party was not "underinsured" by definition. This was changed in *Stracener v. United Serv. Assoc., 777 S.W.2d 378*. In *Stracener,* the Texas Supreme Court held that a "negligent party (individual responsible for the harm) is underinsured whenever the available proceeds of his liability insurance are insufficient to compensate for the injured party's actual damages." (*Stracener, Id.)*

Stracener specifically addressed whether or not to prohibit, stacking of UM/UIM benefits. "Stacking" is defined as collecting from more than one policy on the same claim. 19 states either allow, or do not prohibit, stacking of UM/UIM benefits. In Texas, according to the Stracener ruling stacking is allowed *(Stracener v. United States Automobile Association,* 777 S. W. 2d 378 (Tex. 1989)) except where specifically prohibited by the policy. (*Upshaw v. Trinity Companies,* 842 S. W. 2d 631 (Tex. 1992)).

Following *Stracener*, TDI revised the Texas promulgated policies to comply with the court's ruling. Further, TDI issued Commissioner's Bulletin B-0032-11 in July 2011, stating that UM/UIM coverage must be offered separately. In November 2011, TDI issued Commissioner's Bulletin No. B-1147-11 withdrawing the previous bulletin because it changed long-standing interpretation and practice regarding insurers' offering of UM/UIM coverage.

Issue:

Section 1952.103 of the Texas Insurance Code conflicts with the 1989 Texas Supreme Court ruling in *Stracener v. United Serv. Assoc., 777 S.W.2d 378*. The Legislature has not amended the Insurance Code to reflect this ruling. The current language in Section 1952.103 may be interpreted contrary to *Stracener*. As a result, consumers may not receive the UM/UIM coverage to which they are entitled. This has also resulted in confusion in the market relative to regulatory requirements. Currently, TDI relies on the court decision in its review of policy form filings. Some carriers file policy forms using language as outlined in the Insurance Code Section 1952.103 which is not consistent with the *Stracener* decision.

Recommendation:

- Amend Section 1952.103 to incorporate the policy language required by the Texas Supreme Court ruling in *Stracener v. United Serv. Assoc., 777 S.W.2d 378*.
- Amend Section 1952.105 of the Texas Insurance Code to clarify whether insurers must offer UM/UIM bodily injury and property damage coverage separately, thus allowing "stacking" or whether insurers may offer combined UM/UIM bodily injury and property damage coverage only, thus prohibiting "stacking".

Regulatory Policy

Three-Share Program Oversight

Background:
The 80th Texas Legislature created regional or local health care programs, known as three-share premium assistance programs, when it enacted Senate Bill 10, which added Health and Safety Code Chapter 75. Initially, six areas of the state formed three-share programs. Today three remain operational, Central Texas, University of Texas Medical Branch Galveston, and Harris County. Programs in El Paso, North Texas, and Brazos Valley have closed. In each of the past three legislative sessions, the Legislature appropriated grant funds for the research, planning, development, and operation of these three-share premium assistance programs.

The table, *Total State-Administered Grant Funds*, provides a summary of all grants awarded since the first grant funding was appropriated in the 2008-2009 biennium through the current 2012-2013 biennium. TDI awarded grants through a competitive application process to three-share premium assistance programs since 2008, when the Legislature first appropriated funds for these programs. The current TDI grant comes from two funding sources:

- General Revenue Fund, and
- revenue from fines, penalties, and sanctions that TDI assesses to health insurers.

Total State-Administered Grant Funds*

Three-Share Program -- Grant Period	Total Grant Funding
2008-2009 Biennium	$624,638
2010-2011 Biennium	$3,212,039
2012-2013 Biennium	$1,358,289
Total	**$5,194,966**

** Includes TDI and HHSC administered grant funds*

Issue:
Since awarding the first grant, TDI has monitored the implementation, enrollment, and operational progress of the three-share premium assistance programs. Programs have seen some successes over their tenure, more recently finding additional local funding sources and refining outreach efforts for each region's target populations. However, they have also experienced some challenges during development. TDI's key findings include:

- slower than expected enrollment
- difficulty diversifying funding sources as TDI's collection of fines, penalties, and sanctions are not providing a steady funding source
- three of the six initial programs closing
- problems with grant accounting and financial management.

A report issued by TDI under separate cover provides more detailed information about the following recommendations to the Legislature for expanded oversight of existing programs. Additionally, the report provides details about the three-share premium assistance programs currently operating in Texas, the process for selecting grantees for the current biennium, and a description of current oversight processes.

Recommendation:

If the Legislature continues funding grants for the three-share programs in the future, TDI recommends giving TDI oversight authority beyond grant administration powers. While oversight of TDI grant funds has given TDI some insight into financial and operational issues, a more formal oversight relationship could provide three-share premium assistance programs with a framework for stronger operational and fiscal management. The additional authority should not extend to the full scope of regulation afforded insurance companies, but rather should be tailored to these entities, including

- providing initial approval to operate within the state
- allowing TDI to conduct periodic financial audits to evaluate financial stability
- setting appeals and complaint requirements, and
- ensuring an adequate network.

Regulatory Policy

Leveling the Playing Field

TDI is committed to maintaining and expanding competition in the Texas insurance markets. We have identified several instances where current laws give inequitable advantages to certain types of insurance providers, thereby creating an unlevel playing field. We present these issues for the Legislature's review and consideration.

(1) Amend Chapter 1952 or Chapter 912 of the Texas Insurance Code to prohibit all insurers from limiting an individual's right to choose a repair shop.

Background:

Chapter 1952 of the Texas Insurance Code prohibits insurers from limiting the policyholder's ability to choose their own repair person or facility to fix their vehicle. Chapter 912 of the Texas Insurance Code, however, exempts county mutual insurers from this prohibition. County mutual insurers represent approximately 42 percent of the Texas personal automobile insurance market.

Issue:

Since county mutual insurers cover almost half of the Texas personal auto market and current law does not prohibit them from requiring customers to use their preferred motor vehicle repair shops, a large number of consumers in Texas may not be able to choose their own repair facilities and are not afforded the same protections as their counterparts across the state. All consumers in Texas need to receive the same benefits and protections.

Recommendation:

- Amend Subchapter G of Chapter 1952 and Chapter 912 of the Texas Insurance Code to prohibit all insurers, including county mutuals, from steering consumers to preferred motor vehicle repair shops.

(2) Expand the withdrawal exemption allowed when business is being moved between affiliates to include Lloyds, reciprocals, county mutuals, and farm mutuals.

Background:

Chapter 827 of the Texas Insurance Code requires insurance carriers to file withdrawal plans before exiting the Texas market. Section 827.002 exempts most insurance carriers from the requirements of Chapter 827 when those carriers transfer their insurance business to an affiliated insurance carrier that is within the same group. However, Section 827.002 does not include Lloyds, reciprocals, county mutuals, and farm mutuals from the withdrawal exemption when transferring business between affiliates.

Issue:

The statutory requirement that Lloyds, reciprocals, county mutuals, and farm mutuals file withdrawal plans when they transfer business to affiliated insurance carriers creates administrative burdens for both TDI and the industry.

Recommendation:

- Amend Section 827.002 to expand the exemption when business is transferred between affiliates to include Lloyds, reciprocals, county mutuals, and farm mutuals.

Compliance

Punishment Provisions for Acting as an Agent after License Suspension or Revocation

Background:

Under the Texas Insurance Code, Section 101.106, a person who conducts the business of insurance without a license may be found guilty of a third-degree felony and punished by imprisonment for a term of two to 10 years and up to a $10,000 fine. Section 4005.151 provides that acting as an agent after license suspension or revocation may result in punishment by a fine not to exceed $5,000 and imprisonment for a term of not more than two years.

Issue:

The punishments for these offenses are inconsistent. A licensed agent who has his or her license revoked or suspended by TDI is subject to lesser penalties than a person who conducts the business of insurance without a license.

Recommendation:

- The Texas Insurance Code, Section 4005.151 should be amended to mirror the language and punishment of Section 101.106.

Compliance

Fraud Investigations

Background:

Section 701.102 of the Texas Insurance Code includes references to subsection 35.02(a) of the Penal Code. Subsequent amendments have expanded Chapter 35 of the Texas Penal Code since the original enactment of this law. Now this section of the Penal Code includes application fraud and claim fraud across all lines of insurance with its subsections (a), (a-1), and (b). These subsections are all relevant to the Texas Insurance Code, Chapter 701, and specifically for Section 701.102, Investigations of Certain Acts of Fraud. Fraudulent insurance acts are defined in the Insurance Code's Section 701.001 as "an act that is a violation of a penal law and is: (A) committed or attempted while engaging in the business of insurance; (B) committed or attempted as part of or in support of an insurance transaction; or (C) part of an attempt to defraud an insurer."

Issue:

There is no longer a need for Section 701.102 to refer to a specific criminal law subsection because a fraudulent insurance act and violation of penal law would cover all offenses.

Recommendation:

- Texas Insurance Code Section 701.102 should be amended to remove references to the Penal code.

Compliance

Special Prosecutors

Background:

Texas Insurance Code Section 701.102 provides that the commissioner may conduct investigations related to potential fraud. TDI currently employs special prosecutors in the Dallas County District Attorney's Office, the Harris County District Attorney's Office, and the Bexar County District Attorney's Office. There are many other counties in Texas with fewer resources that could use assistance and expertise that a TDI prosecutor could offer. An in-house prosecutor, based in Austin at TDI, could travel to offer assistance to different counties to fight insurance fraud.

Issue:

Texas counties with fewer resources do not have access to expertise that TDI and the special prosecutors have.

Recommendation:

- Texas Insurance Code, Section 701.102, should be amended to permit the commissioner of insurance to assist authorized governmental agencies in investigating and prosecuting fraud.

Compliance

Insurer's Duty to Provide Information

Background:

Texas Insurance Code Section 701.108 provides insurers with a duty to provide information or material relating to a matter under investigation. Criminal investigations are time-sensitive. Important evidence can be lost or altered if too much time passes before the fraud investigators obtain the information. Language clarifying the timeframe in which the requested information is due is necessary and clarifying that requests from the Fraud Unit are covered by this section will provide additional support to Fraud Unit staff in their investigations.

Issue:

Currently the statute does not provide timeframes for an insurer to produce information the Fraud Unit requested.

Recommendation:

- Texas Insurance Code, Section 701.108, should be amended to establish a 10-day timeframe within which responses are due to the Fraud Unit. This will assist in the efficient investigation of fraud in Texas.

Compliance

Confidentiality Provisions of Texas Insurance Code, Section 701.151

Background:
Texas Insurance Code Section 701.151 relates to confidentiality of information or materials required by TDI that is relevant to an investigation by TDI's Fraud Unit. Currently information and materials received under Section 701.151 are subject to discovery requests.

Issue:
TDI's regulatory processes to revoke licenses or institute disciplinary actions currently may be used as a discovery tool by persons inappropriately seeking information about a criminal case or investigation. This could cause some people not to report crimes out of fear of retaliation or civil litigation by criminals.

Recommendation:

- Texas Insurance Code, Section 701.151, should be amended to prevent civil or administrative discovery of Insurance Fraud Unit cases and investigative materials, including privileged or confidential information acquired from other law enforcement or regulatory agencies.

State Fire Marshal's Office

Inspections of State Owned Facilities

Background:

Section 417 of the Texas Government Code directs the State Fire Marshal's Office (SFMO) to periodically inspect buildings under the charge and control of the Texas Facilities Commission (TFC). As the authority having jurisdiction over fire and life safety issues in state buildings, SFMO also conducts periodic inspections of other state owned facilities that are not part of TFC's inventory. Examples of these are buildings that house state universities, the Texas Department of Public Safety, the Texas Department of Transportation, the Texas Department of Criminal Justice, state supported living centers and hospitals, and others.

Issue:

SFMO does not have sufficient resources to regularly inspect all state owned buildings at intervals recommended by the National Fire Protection Association (NFPA). A 1978 study conducted by the National Fire Protection Association and the Urban Institute recommends that all public buildings be inspected on an annual basis, since more frequent fire inspections have been shown to result in lower fire rates. This is merely a recommendation; while research shows that more frequent inspections yield better results, a best-practice inspection frequency has not been established. NFPA recommends that all buildings be inspected periodically, and that facilities that are identified as having a higher risk are inspected more frequently. If SFMO were to inspect each state-owned building and space leased by TFC annually, the number of inspectors would need to be increased nearly threefold. Fire departments throughout the country face similar challenges and annual inspections of all facilities within a jurisdiction are rarely achieved.

SFMO's ultimate goal is to inspect all state owned facilities on a regular basis. In lieu of inspecting all facilities annually, SFMO proposes to inspect residential and other high-risk facilities on a one- to three-year cycle, all other buildings would be inspected on a schedule determined by available resources. Currently SFMO employs 11 inspectors, after inspecting the priority facilities mentioned above and other inspection duties, the remaining state buildings would only be able to be inspected once every 14 years. SFMO feels that 14 years is far too long for any building to go without an inspection. SFMO recommends that each building should be inspected at least once every five years.

Recommendation:

- SFMO has analyzed inspector workloads and the total state building inventory (15,000 buildings) and has determined that a total of 15 inspectors would be needed to inspect all state buildings on a minimum 5 year schedule, with residential and other high-risk facilities being inspected on a one- to three-year schedule, in addition to fulfilling other inspection duties. SFMO should be granted the resources and authorization to hire four additional inspectors to ensure that all state owned facilities are inspected regularly in order to maintain a safe environment for state employees and the citizens that they serve.

Workers' Compensation

Clarify Labor Code to State that TDI's and DWC's Names May Not Be Used in a Deceptive Manner

Background:

In 2005, the Texas Legislature passed HB 7, which added Section 419.002 to the Labor Code. The new provision prohibits the misuse of DWC's name and logo, the name and initials of TDI, and any combination of the words "Texas" and "Workers' Compensation" by a person offering or performing workers' compensation services in this state. HB 7 also set up civil and administrative penalties for the violation of this statutory provision and DWC rules and gave the attorney general or a district attorney the authority to take legal action to enjoin or restrain a violation or threatened violation under certain circumstances. These provisions were added to the statute in response to situations in which medical clinics were locating in buildings that housed the field offices for the former Texas Workers' Compensation Commission (DWC's predecessor) and using similar names, such as "Texas Workers' Compensation Clinic," in conjunction with the state seal. This created confusion for injured employees who visited these clinics.

Issue:

Section 419.002 is currently being challenged in federal court. This lawsuit claims that the statute violates the plaintiff's rights to free expression under the First Amendment to the U.S. Constitution. The plaintiffs also contend that the statute violates the Fifth Amendment's prohibition of takings and the Fourteenth Amendment's guarantee of equal protection and due process. A federal district court dismissed the plaintiff's Fifth and Fourteenth Amendment claims and declined to consider the plaintiff's First Amendment challenge. The plaintiff appealed and, on October 30, 2012, the Fifth Circuit United States Court of Appeals upheld the district court's dismissal of the plaintiff's Fifth and Fourteenth Amendment claims and remanded the plaintiff's First Amendment challenge back to district court to permit the parties to more fully develop the record on this issue (*see Gibson v. Tex. Dep't of Ins. – Div. of Workers' Comp.*, No. 11-11136, 2012 U.S. App. LEXIS 22375 (5th Cir. Tex. Oct. 30, 2012). The Appeals Court also affirmed the district court's ruling that the regulation at issue is content-neutral and does not amount to a prior restraint. DWC proposes new Labor Code Section 419.001 and amendments to Labor Code Section 419.002 to address potential constitutional issues that may currently exist with the current statute. These changes are meant to clarify the existing statute so that it aligns with the way DWC has applied these requirements in individual cases – to prohibit the use of the agency's name, certain terms, and state symbols in a deceptive manner. A similar amendment to DWC's Sunset bill was unanimously passed by the House of Representatives last session without controversy; however, the amendment was removed by the Senate in order to preserve only Sunset recommendations in the final version of DWC's Sunset bill, HB 2605.

Recommendation:

- Create new Labor Code Section 419.001 and clarify existing Labor Code Section 419.002 to state that TDI's name, DWC's name, and other terms and state symbols may not be used in a "deceptive manner" in an effort to create a false impression that something is endorsed, approved, sponsored, authorized or associated with TDI, DWC, or the State of Texas.

Legislative Considerations

Texas Windstorm Insurance Association

Background:
When Hurricane Celia struck the Texas coast in 1970, many insurance companies ceased selling property insurance in the Gulf Coast region. In 1971, the Texas legislature created a mandatory association of all property and casualty insurance companies, now known as the Texas Windstorm Insurance Association (TWIA), for the benefit of coastal consumers.

TWIA provides wind and hail insurance in the 14 coastal counties of Texas and certain parts of Harris County to consumers unable to obtain such insurance in the voluntary (private) market. The fourteen coastal counties eligible for TWIA coverage, along with the select portion of Harris County, are Aransas, Brazoria, Calhoun, Cameron, Chambers, Galveston, Jefferson, Kenedy, Kleberg, Matagorda, Nueces, Refugio, San Patricio, and Willacy Counties. Together, these 14 counties and portion of Harris County are known as Tier 1. TWIA functions similarly to other insurers in that it issues policies, collects premiums and pays claims.

TWIA began experiencing a significant growth spurt in 2006 as insurers again reduced their writings following back-to-back horrific hurricane losses in 2004 and 2005, which included Katrina, Rita and Wilma. TWIA's exposure (direct liability in force) has grown from $23.3 billion as of December 31, 2005 to $74.3 billion as of September 30, 2012.

On September 13, 2008, Hurricane Ike struck the Galveston area. As the largest insurer of wind and hail in Tier 1, TWIA was inundated with over 92,000 claims. TWIA's losses for Ike claims exceed $2.53 billion to date.

In 2009, the Texas legislature enacted major changes to TWIA operations with the passage of HB 4409, including the clarification of TWIA's purpose as the insurer of last resort for windstorm and hail insurance in the seacoast territory.

HB 4409 also revamped TWIA's funding mechanism in the event that losses exceed the total of TWIA's cash on hand, the catastrophe reserve trust fund and any available reinsurance proceeds. Prior to HB 4409, such excess losses were funded through assessments on member insurers in proportion to their statewide property insurance market share. Insurers recouped any assessments over $300 million via credits against their premium taxes owed to the state over five or more years. HB 4409 replaced the assessment/premium tax credit method with a program of post-event bonds to be issued by TWIA. The bond program provided for up to $2.5 billion of bonds in any one catastrophe year, in three tranches, with repayment through a combination of TWIA premiums, surcharges on most property and casualty policies issued in Tier 1 (the 14 coastal counties) and up to $800 million in assessments on insurers (with no provision for premium tax credits).

HB 4409 further directed TDI to develop incentive programs to encourage authorized insurers to write wind and hail insurance on a voluntary basis and to minimize the use of TWIA as a means to obtain insurance.

In 2011, the Texas legislature again enacted major changes to TWIA operations with the passage of HB 3. HB 3 included numerous claims and claims handling related reforms. HB 3 also fine-tuned the bond program by authorizing issuance of pre-event bonds, but did not increase the total amount of bonding capacity from $2.5 billion in any one catastrophe year.

Concerns:

On February 28, 2011, TWIA was placed under administrative oversight by TDI when it was found to be "in a condition that makes its continuation in business hazardous to the public or to policyholders." Since that time, TWIA has replaced most of its senior management and has implemented many improvements to its policies, procedures and management practices, although the ongoing influx of mostly Ike-related claims continues to strain TWIA's management and financial resources.

TDI has been unable to identify meaningful incentives for insurers to write more wind and hail coverage in Tier 1 solely through our administrative authority. Many insurers have written some wind and hail coverage in the "back-end" of Tier 1 (the area furthest from the coastline), thus making them eligible for "take-out" credit in the event they would be assessed for excess losses. Other insurers have simply decided to risk paying their share of any assessment rather than write wind and hail coverage at what they consider TWIA's inadequate rate level. (If insurers charge more than TWIA, the consumer will choose TWIA over the private insurers.)

By far, the most troubling aspect of TWIA's current state is its lack of secure, predictable, viable funding in the event of even a fairly low level hurricane. In 2012, TWIA's maximum funding capacity was estimated at $3.5 billion, which equates to about a 1-in-63 year storm. Moreover, this estimate assumes that TWIA would have been able to issue all $2.5 billion in authorized bonds, which was deemed unlikely by the Texas Public Finance Authority.

Issues for Consideration:

On September 7, 2012, TDI presented a report from Alvarez & Marsal Insurance Advisory Services, which offered much useful information and many concrete options for restructuring TWIA in order to shore up its finances. While improving TWIA's funding is a high priority, any such fix will only be temporary unless steps are taken to reduce TWIA's exposure by increasing voluntary market participation.

Legislative Considerations

Attracting New Capital to Texas

Background:

Texas consumers and businesses paid more than $106 billion in insurance premiums last year, making Texas the 12th-largest insurance market in the world. Currently, more than 400 insurance companies are based in Texas. Many are small- and medium-sized regional carriers.

Concerns:

In relation to the size of the state's insurance market, Texas is home to only an average number of insurance companies. Texas is also average in terms of the number of large insurers (defined as insurers writing $500 million or more in annual premiums). By comparison, other states retain a greater number of domestic insurers in relation to the size of their insurance markets and serve as the home to a disproportionately higher number of large insurance companies.

TDI believes an opportunity exists to attract more insurance companies to Texas, particularly large insurers. The benefits of attracting more companies include:

- increased competition;
- support for the growth of the Texas economy; and
- enhanced ability of the state, including TDI, to influence regulatory developments at the national and international levels.

Suggested Considerations:

The Texas Legislature may wish to:

- reduce costs borne by Texas-domestic insurers by spreading the costs of TDI's examination overhead assessments to all insurers licensed in Texas;
- strengthen the protection of the confidential regulatory information used by various regulators and law enforcement officials;
- allow additional investment authority for the largest, most financially stable insurers;
- amend regulatory approval thresholds in the Texas Holding Company Act based on the NAIC model act language to enhance uniformity and consistency from state to state;
- grant discretion to the commissioner of insurance, with concurrence from the comptroller of public accounts, to grant credits for premium or maintenance taxes for temporary periods of time for insurers who locate their physical operations in Texas;
- appoint a study group to review Texas premium tax rates; and
- update and streamline the incorporation and licensing statutes for insurance companies.

Legislative Considerations

Named-Driver Policies

Background:

Policy forms generally must be approved by TDI before an insurance carrier can use them in Texas. TDI currently approves a type of personal automobile policy that provides coverage for only two types of drivers: (1) a person whose name is listed on the policy, and (2) other drivers who are not members of the policyholder's household but have permission to drive the insured vehicle. These policies are known as "named-driver" policies. TDI approved the first named-driver policy in 2004, and the Texas Department of Public Safety (DPS) has indicated that named-driver policies comply with the technical requirements for safety responsibility in Section 601.072 of the Texas Transportation Code.

TDI also approves a comparable type of personal automobile policy known as a "named-driver exclusion" policy. Although somewhat similar to the named-driver policy, the named-driver exclusion policy generally provides coverage to all drivers, except those specifically excluded by name on the policy. In many ways, it is the reverse of a named-driver policy.

While TDI receives few inquiries on the protections afforded by named-driver exclusion policies, we receive a number of inquiries from consumers and legislators questioning whether named-driver policies truly meet the safety and financial responsibility requirements in the Texas Transportation Code.

Concerns:

Since a named-driver policy provides coverage only for those drivers specifically named on the policy and nonhousehold permissive drivers, an issue can arise when a member of the policyholder's household, who is not named on the policy, drives the insured vehicle. When this situation occurs, the driver is not covered by the policy, regardless of whether they have permission from the policyholder to drive the automobile. Many policyholders and drivers, however, do not understand these coverage restrictions. Others understand the restrictions but choose to ignore them.

In either scenario, named-driver policies can leave a third-party driver, whose car or body is injured by the noncovered driver, with little recourse against the driver who caused the damage. The injured third party might have to rely on the uninsured motorist coverage provided by his or her automobile policy. Uninsured motorist coverage is usually less substantial than other coverage provided on a person's policy, so the injured person can be left with more out-of-pocket expenses.

While named-driver policies have limitations, they have some benefits as well. Named-driver policies provide insurers with more certainty about the risks they are insuring, which can lead to better rating and underwriting decisions. The ability to make better rating and underwriting decisions can, in turn, allow insurers to offer coverage or charge lower premiums to consumers, making insurance more available.

Suggested Considerations:

Since TDI currently has the statutory authority to approve named-driver policies and DPS has indicated these policies to meet Transportation Code requirements, the decision about whether to continue to allow named-driver coverages in Texas is a public policy decision. Thus, TDI will continue to approve named-driver policies that meet regulatory and statutory conditions unless given a different directive from the Texas Legislature.

Legislative Considerations

PPOs and EPOs

A History of Network Adequacy and Balance Billing in Texas

2005-2006 – Senate State Affairs Interim Charge to study reimbursement of health care plans for out-of-network claims, adequacy of health plan networks, the impact of balance billing and the accurate disclosure of out-of-pocket costs.

2007 – SB 1731 directs TDI to work with an advisory committee and make recommendations to the legislature. No consensus could be reached among stakeholders.

2009 – Network Adequacy Advisory Committee and TDI report to the Legislature. HB 2256 enacted to provide for mediation on certain high-cost claims. Same legislation also requires TDI to write rules on network adequacy, and TDI begins the discussion with a concept paper.

2011 – PPO rule adopted in July, to be effective in May 2012, to accommodate possible legislative changes. HB 1772 enacted, creating EPOs. PPO rule is placed on hold in December to review for incorporation of EPO requirements.

2012 – 2011 EPO/PPO rule is withdrawn and re-proposed. After receiving stakeholder input the rule was again modified and re-proposed with anticipated adoption in early 2013.

Background:

Most health insurance today is provided under a "network" in which insurers contract with healthcare providers, including physicians and hospitals, to provide care to the insurers' policyholders according to a set of agreed to terms, conditions, and charges. These types of insurance agreements and networks are commonly referred to as preferred provider organizations (PPOs). Policyholders using "in-network" providers in a PPO are generally responsible for a relatively low co-payment and providers in the network agree not to charge the policyholders more than the provider has agreed to accept from the insurer under the network agreement.

These network plans typically include higher co-payments for out-of-network care. Likewise, non-network providers often charge more than network providers because the provider is not bound by contract to any network agreement with the insurer. These charges are commonly referred to as "billed charges." Because there is no agreement between the provider and the insurer regarding payment, the non-network provider may "balance bill" the policyholder for the difference between the amount the insurer pays and the billed amount if the insurer does not pay the full billed charge.

When the policyholder knowingly chooses an out-of-network provider, the policyholder generally understands the ramifications. Problems arise, however, when the policyholder unknowingly receives treatment from an out-of-network provider, usually an anesthesiologist, pathologist, radiologist, or other specialist, at an in-network hospital. Often times, the insurer has been unable to contract with any such specialty providers in the hospital, and, therefore, cannot offer the policyholder a complete network solution, including agreed-to contract terms on the level of reimbursement, for the policyholder's healthcare. Unfortunately, the insurer's inability to find a complete network solution often results in balance bills and higher out of pocket costs to the policyholder.

Concerns:

In 2009, Chapter 1301 of the Texas Insurance Code was amended to require TDI to adopt, by rule, certain network adequacy standards applicable to PPOs. In 2011, Chapter 1301 was amended again to authorize "exclusive" provider organizations (EPOs), which resemble PPOS but contain more stringent out-of-network requirements. These legislative changes, however, were not the first revisions made to the laws regarding healthcare provided through networks. As the box on this page illustrates, efforts on this issue span a period of time of over seven years, three insurance commissioners, and four legislative sessions. Despite the best efforts of everyone involved, there remains no consensus among the stakeholders.

Against this backdrop of dissension, TDI began fulfilling the mandate set forth in Section 1301.0055 of the Texas Insurance Code requiring TDI to "ensure the availability of, and accessibility to, a full range of contracted physicians and healthcare providers to provide healthcare insurance to insureds..." TDI's options in crafting a rule to meet the demands of this mandate, however, are extremely limited since TDI cannot require providers to contract with insurers. TDI can only regulate the behavior of one party to the contract and one stakeholder among the various stakeholders -- the insurer. TDI, therefore, attempted to craft a rule giving insurers and policyholders an opportunity to coordinate a complete network solution for medical treatment and thereby avoid balance billing situations in the first place. In the event a complete network solution is unavailable, the proposed rule sets a high bar for insurers to protect the policyholders from being billed for additional charges by the healthcare provider. Stakeholder comments to TDI's proposed rule, however, reflect both overall dissatisfaction with the rule and the general intractability of the parties on this issue.

For example, some stakeholders like the protections against balance billing included in TDI's latest proposed rule, but asked TDI to go a step further and require insurers to provide certain disclosures on their websites that would be of minimal benefit to policyholders. Other stakeholders dislike the balance billing protections in the proposed rule and provided TDI with an actuarial study indicating that premiums will increase if insurers are required to essentially hold policyholders harmless from balance billing. Still other stakeholders acknowledge that premiums will increase if policyholders are protected from balance billing to the degree required by TDI's proposed rule, but they maintain that TDI's approach provides the best protection for consumers. In contrast, another group of stakeholders oppose any rule that will result in an increase in premiums, yet offer no alternative approaches that would both protect consumers from balance billing and maintain current premiums. The result of these varying and contradictory positions, coupled with the statutory limitations imposed on TDI's authority, leave TDI at a loss for creating consensus among the various stakeholders through the rulemaking process.

Request for Additional Guidance:

TDI's currently proposed rule establishes a much higher standard for insurers with respect to their network adequacy requirements and further requires insurers to pay "usual and customary" charges to providers, if necessary, to protect policyholders from balance billing issues when a complete network solution is unavailable. (Usual and customary charges are generally less than billed charges, but still higher than what insurers consider reasonable.) This approach represents TDI's best efforts to protect consumers and meet legislative mandates within the confines of TDI's authority. Still, the approach arguably represents a "slippery slope" of governmental intervention in contractual relationships between private parties.

Accordingly, TDI's rule on network adequacy will not be fully implemented until after the Texas Legislature adjourns to allow the only entity with policymaking authority over all parties to provide additional guidance.

Legislative Considerations

Section 1033 Waiver

Background:

The federal Violent Crime Control and Law Enforcement Act of 1994 prohibits individuals convicted of a state or federal felony involving dishonesty or a breach of trust from engaging in the business of insurance without the written consent of an insurance official with regulatory authority over those individuals. The federal citation for this Act is U.S.C Chapter 1033 and the waivers granted under the Act are referred to as 1033 waivers. The Act also makes it a crime for insurers to employ individuals who have not obtained this written consent. TDI receives applications periodically from individuals subject to the act, and has been granting 1033 waivers in practice. TDI issued seven waivers in 2011. Often these felonies involve youthful indiscretions from many years ago, and evidence reflects that the individuals subsequently turned their lives around to become productive members of society.

Concerns:

There is not an express provision in Texas law regarding the commissioner's administration of the federal act. Current Texas law, specifically Section 31.021 of the Texas Insurance Code provides that the "commissioner shall administer and enforce this code, other insurance laws of this state, and other laws granting jurisdiction or applicable to TDI or the commissioner." Various other laws in the Insurance Code address the competency and trustworthiness of officers and directors of insurance carriers and other regulated parties, such as insurance agents and claims adjusters. Since the commissioner of insurance is the chief executive and administrative officer with the authority to enforce laws applicable to TDI, TDI believes that federal act and the state laws, when read together, authorize the commissioner to administer the federal act. TDI believes, however, that the Insurance Code or administrative law should be clarified to specifically address the commissioner's administration of the act, including specifying the parameters the commissioner should consider in deciding whether to exercise the discretion contemplated by the federal Act.

TDI believes individuals subject to the federal Act would benefit from a more formal structure and understanding of the factors that will be considered before the commissioner decides whether to grant a waiver. Such factors should encompass various parameters, including the length of time since the action that resulted in the conviction, the severity of the action, whether restitution was owed and paid, aggravating and mitigating circumstances, etc. The factors should also include letters of reference, such as letters from current employers and church and community leaders.

TDI further believes that the insurance industry would benefit, as this would widen the pool of potential employees and prospective insurance agents, which helps to ensure the availability of insurance in the various geographic areas of the state.

Suggested Considerations:

TDI published a proposed rule in the Texas Register regarding the commissioner's administration of the act. No public comments were received in response to the proposed rule. TDI would like to give the Legislature an opportunity to provide guidance or clarify the Insurance Code by providing specific authority to the commissioner to administer the federal act if it wishes to do so. Otherwise TDI intends to proceed with the rule adoption process.

Legislative Considerations

Pre-Dispute Arbitration

Background:

Texas statutes provide a variety of individual rights for resolving disputes, including disputes between a policyholder and their insurance carrier. Chapter 541 of the Texas Insurance Code authorizes a person to bring certain actions against a carrier in a court of law. Arbitration is also a remedy provided to policyholders in Texas. Arbitration can be binding and can be decided upon as a method of resolving disputes either before or after a dispute actually arises between a policyholder and their carrier.

When parties enter into pre-dispute binding arbitration, neither party knows what kind of dispute may arise, how much money a dispute may involve, or the extent of resources necessary for resolution of the dispute. Accordingly, there is an inherent degree of uncertainty involved in pre-dispute arbitrations.

In contrast, when parties enter into post-dispute binding arbitration, the parties agree to arbitration with a more informed idea of what is at stake since the parties have experience with each other and know the precise nature of the disagreement between them.

Concerns:

Carriers sometimes file insurance coverage forms proposing to limit covered individuals to pre-dispute mandatory binding arbitration as the sole means to resolve all disputes that arise between them. Carriers assert that arbitration is good public policy, which results in cost savings to both carriers and covered individuals. Insurance contracts, however, resemble other contracts of adhesion and provide no opportunity for the covered individual to negotiate the bulk of the contract's terms or conditions. Therefore, while arbitration has some benefits for carries and policyholders, there are also aspects of pre-dispute mandatory binding arbitration that create negative consequences for policyholders who purchase a contact with dispute resolution terms already determined by the carrier. TDI's main concern, therefore, is the extent to which carriers are utilizing a tool that binds the contracting parties to a very limited set of rights once a dispute arises, but unlike other contract negotiations, one party, the policyholder, does not have the ability to negotiate the terms of the contract.

Suggested Considerations:

TDI is considering a rule proposal to prohibit pre-dispute mandatory binding arbitration provisions in insurance products. The rule would apply to policy or contract coverages for individuals for personal noncommercial use in lines such as personal automobile and residential property (homeowners). The basis of the proposed prohibition stems from the fact that pre-dispute mandatory binding arbitration precludes covered persons, who are not able to negotiate the terms of their contract with the carrier in the same way that other contracting parties are able to negotiate their contract terms, from exercising substantive rights provided by the Texas Insurance Code. The proposed prohibition would apply to group or individual policy forms providing coverage in life, accident, and health; annuity; credit; and property and casualty products.

TDI posted a request for informal comments from stakeholders on this concept to receive input on substantive rights provided by current statutes and the protections of those rights. The request for input posted to the TDI's website on October 18, 2012, and the comment period ended on November 16, 2012. TDI received comments from a variety of sources both in favor and opposed to a ban on pre-dispute binding arbitrations in insurance policies. TDI has reviewed those comments and will use them as a guide to assist the agency as we develop a rule prohibiting pre-dispute binding arbitration clauses in certain insurance contracts.

Since issues about access to the courts and the substantive rights of individuals are public policy concerns well within the purview of the Texas Legislature, TDI decided to refrain from posting the formal rule until the end of the legislative session. This delay gives the Texas Legislature the opportunity to comment on our proposed policy of prohibiting pre-dispute mandatory binding arbitration should legislators choose to do so. TDI welcomes input from legislators on this issue, and if no action is taken by the Legislature, we will proceed with the posting of and adoption of a rule prohibiting the inclusion of pre-dispute binding arbitration in policies.

Legislative Considerations

Amusement Rides

Background:

TDI is the state's administrator for the Amusement Ride Safety Inspection and Insurance Act under Occupations Code, Section 2151. To operate legally in Texas, an amusement ride owner or operator must file with TDI an insurance policy with certain limits of bodily injury coverage for persons using the ride, an annual amusement ride safety inspection certificate, and a $40 filing fee per amusement ride. There are no other regulatory requirements.

For nearly three decades TDI has served as the Texas administrator for the Amusement Ride Safety Inspection and Insurance Act. The Amusement Ride Safety Inspection and Insurance Act encompasses a broad spectrum of rides, from mobile carnival rides and theme park rides to mechanical bull and bounce-house rentals. TDI has seen a steady increase in the number of amusement rides in the state over the last several decades. During FY 2012, TDI issued 6,618 compliance stickers.

TDI discovers noncompliant rides through competitors reporting noncompliant owners or operators, comparing online searches of amusement ride businesses with the TDI database of amusement rides, and injury inquiries from consumers. Currently, if TDI is aware of a noncompliant ride, TDI will send the owner or operator a notice of noncompliance requesting the owner or operator to demonstrate compliance with the statute. If compliance is not demonstrated, TDI notifies the Office of the Attorney General (OAG), the owner or operator, and local law enforcement, among others.

Concerns:

TDI does not have an effective and efficient means of monitoring compliance with the requirements of the Amusement Ride Safety Inspection and Insurance Act or an effective means of recourse when instances of noncompliance are identified. TDI has seen a nearly 400 percent increase in the number applications filed since 2005. This increase can be attributed to the increase in amusement ride rentals for public use, such as bounce houses and rock climbing. While these are the areas that are increasing the most, they are also the most difficult for TDI to monitor.

Ultimate enforcement authority lies with the OAG, and local law enforcement officials. It is discretionary for law enforcement to charge owners or operators with a Class B misdemeanor if they are found operating a noncompliant amusement ride.

Suggested Considerations:

The Texas Legislature may wish to:

- provide TDI with adequate authority to effectively enforce the state's amusement ride statutes and remove the discretionary provision for law enforcement; and

- review the role of TDI as the insurance regulator and determine if the administration of the Amusement Ride Safety Inspection and Insurance Act, Occupations Code Section 2151, fits in with TDI's mission. Identify whether a different state agency may be better equipped or have the appropriate mission to regulate the amusement ride industry.

Appendix A: Reduced Rate Filing Requirements Study

Legislative Charge – House Bill 1951, 82nd Legislature

HB 1951 requires TDI to conduct a study on the impact of increasing the market share percentage of insurers and report on the effect it will have on companies that qualify for reduced rate filing requirements on residential property insurance.

Background

As part of their rate filing, insurers are normally required to submit rates, supplementary rating information, and actuarial support. TIC Section 2251.252 allows reduced rate filing requirements for companies meeting certain market share criteria. These criteria include:

- having a group market share of less than 2 percent;
- writing at least half of their business covering policies valued at less than $100,000; and
- writing at least half of their business designated in underserved areas.

Companies meeting these requirements and seeking this exemption must file the Exemption Compliance form with TDI. Upon TDI acceptance of this form, a company is only required to submit a rate filing exhibit which helps TDI verify that rate increases are under the 10 percent threshold required for the exemption.

TDI staff performs calculations on an annual basis to determine which companies qualify for the reduced rate filing exemption. There are currently 13 qualified companies. The largest company that qualifies for this exemption has a market share of 1.41 percent.

Study Results

TDI used the 2011 residential statistical plan data. We evaluated the effect of increasing the market share threshold to 3, 4, and 5 percent, as well as removing it entirely, while keeping the other criteria required to qualify for the exemption constant. The result shows there is no change in the number of companies qualifying for exemption. This is due to qualified companies being well under the 2 percent market share threshold, or unqualified companies not meeting all of the other required criteria.