Ohio Legislative Service Commission

Thomas Kilbane

Fiscal Note & Local Impact Statement

Bill: S.B. 223 of the 131st G.A.

Date: December 9, 2015

Status: As Enacted

Sponsor: Sen. Bacon

Local Impact Statement Procedure Required: No

Contents: Amends coverage benefit limits and exclusions for the Ohio Life and Health Insurance Guaranty Association, temporarily suspends H.B. 64 provision regarding subrogation recovery, amends life insurance company reinsurance regulations, updates prompt payment claim codes, and adds an emergency clause for certain provisions

State Fiscal Highlights

- The bill increases the liability limits of the Ohio Life and Health Insurance Guaranty Association. Higher liability limits would require larger assessments to Association members in the event of an insolvent insurer. Members are afforded future tax offsets for the assessments, so the bill will decrease insurance tax revenue. The GRF would bear the majority of the revenue loss.
- If Penn Treaty Network America Insurance Company is liquidated by the Pennsylvania court system and assessments to Association members become necessary within Ohio's current fiscal biennium, the bill could decrease GRF revenues by an estimated $400,000 annually beginning in FY 2018.
- Future insolvencies beyond Penn Treaty are unforeseeable, but very likely. Through 2013, the Association assessed members for approximately $5.25 million annually on average. The liability limitation changes in this bill could result in a 25% increase in necessary assessments, meaning an average annual decrease to the GRF of approximately $1.3 million in perpetuity. Actual increases to the assessments and decreases to the GRF would be irregular, however the tax offsets are structured to be delayed and normalized in comparison to the assessments to member insurers.
- In the event of multiple large health or life insurance company failures within a short period of time, the loss to the GRF could be substantially larger.
- The temporary suspension of the subrogation provision enacted in H.B. 64 will allow higher cost recovery by the state's self-funded insurance programs through December 31, 2016.

Local Fiscal Highlights

- A portion of GRF tax receipts is distributed to the Local Government Fund (LGF) and the Public Library Fund (PLF), with the LGF receiving 1.66% of GRF tax revenue and the PLF receiving 1.70%. Thus, any reduction in GRF tax receipts from the bill would also reduce the amount distributed to the LGF and PLF.
- A $1.3 million annual decrease to the GRF would result in an approximately $21,000 annual loss to the LGF and PLF. The loss to the LGF and the PLF in some years would be greater than $21,000, but unlikely to ever be above $100,000.
- Approximately 30% of local governments and school districts could see higher premium rates for their health and disability insurance policies due to the changes to the Guaranty Association. The additional premium rate is essentially capped at less than 2% annually, but actual additional premium is likely to be minimal.
- For the approximately 70% of local public health insurance plans which are self-funded, the suspension of the subrogation provision enacted in H.B. 64 will allow higher cost recovery through December 31, 2016. The remaining 30% of local health insurance plans may see minimal temporary savings on premium rates due to the change.

Detailed Fiscal Analysis

Changes to Ohio Life and Health Guaranty Association

The bill amends existing coverage limits and exclusions for the Ohio Life and Health Insurance Guaranty Association when an insurer becomes impaired or insolvent. It increases the Association's maximum benefit liabilities for one life/payee, regardless of the number of policies or contracts, to the following amounts by type of policy or contract:

Ohio Life and Health Insurance Guaranty Association Benefit Liabilities		
Policy/Contract	**Existing Limit**	**Limit Under S.B. 223**
Basic hospital, medical, and surgical insurance or major medical insurance	$100,000	$500,000
Disability insurance	$100,000	$300,000
Long-term care insurance	$100,000	$300,000
Structured settlement annuity[1]	Not specified	$250,000

The new benefit limitations under S.B. 223 are the recommended standards by the National Association of Insurance Commissioners (or NAIC) and similar limitations have been adopted in most other state legislatures. All other benefit types and amounts for which the Guaranty Association may become liable under existing law remain unchanged.

The bill also clarifies coverage for U.S. citizens living abroad and non-Ohio resident beneficiaries of structured settlement annuities, explicitly excludes policies issued in relation to Medicare Part C (Medicare Advantage plans) and Medicare Part D (Medicare Prescription Drug plans), and removes the authority of the Superintendent of Insurance to declare an insurer "impaired." The majority of the fiscal effects of the bill's provisions related to the Guaranty Association will be a result of the benefit liability limitation changes. The net fiscal effects of all other changes are determined to be negligible.

Background

The Ohio Life and Health Insurance Guaranty Association is a nonprofit association of insurance companies that sell life insurance, health insurance, and annuities in Ohio. It was created in 1989 by Ohio law to provide protection for Ohio policyholders against the insolvency and liquidation (i.e., bankruptcy) of an insurance company licensed to sell in Ohio. All insurance companies licensed by the state to sell life, health, and annuity policies must belong to the Guaranty Association. If a company

[1] An annuity purchased to fund periodic payments to a plaintiff or claimant in a personal injury case.

is liquidated, the Guaranty Association steps in to cover claims of the company's policyholders up to the limits established by Ohio law.

The funds to pay the claims and cover associated administrative costs come from assessments on the Association member insurance companies, which are only made when funds are needed. Each member's assessment is determined by the proportion of premiums in the state that it receives, and cannot exceed 2% of its average annual premiums.

Fiscal effects

Fiscal effects of this bill will only be realized upon the liquidation of an insurer with policyholders in Ohio. Even then, effects of the bill will only be incurred when policyholder claims are larger than previous liability limits. When this happens, increases to the Guaranty Association's existing benefit liability limits could affect public finances in two ways.

First, Guaranty Association members can offset the assessment against their future premium tax liabilities. Therefore, higher liability limits would require larger assessments, resulting in larger offsets to the premiums tax. Receipts from the premiums tax are deposited into the GRF which would bear the majority of the revenue loss from the assessment offset. Additionally, a portion of GRF tax receipts is subsequently transferred to the Local Government Fund (LGF) and the Public Library Fund (PLF), with the LGF receiving 1.66% of GRF tax revenue and the PLF receiving 1.70%.[2] Thus, any reduction in GRF tax receipts from the bill would also reduce the amount distributed to the LGF and PLF.

Tax liabilities can be offset by 20% of the assessment in each of the five years beginning after the fiscal biennium in which the assessment was paid. If the eligible offset amount in a given year exceeds a member's tax liability, the excess is carried forward to be used in future years. The cap on assessments for any one Association member is 2% of average annual premiums. S.B. 223 does not change that cap, however, raising the Association's liability limits will raise the necessary assessment amount for any insurer under the cap. In particular, the bill's effects will be incurred only when claims in excess of previous limits (typically $100,000) are filed by Ohio policyholders of the liquidated insurer. According to data used in a 2012 paper at the U.S. Bureau of Economic Analysis (BEA),[3] less than 0.5% of medical insurance claims are over $100,000. However, due to the extraordinarily high cost of those claims, the additional money needed to cover the new liability limits will make up a much larger percentage of the assessment on Association members. The actual difference in assessments due to this bill will also depend on the size and type of the liquidated insurer.

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[2] H.B. 64, the current operating budget act, temporarily increased the PLF share to 1.70% for FYs 2016-2017. In the absence of action by the General Assembly, the percentage will revert to 1.66% beginning in FY 2018.

[3] Aizcorbe, Ana, et al. *Measuring health care costs of individuals with employer-sponsored health insurance in the US: A comparison of survey and claims data*. Statistical Journal of the IAOS 28.1 (2012): 43.

Second, policyholders of Guaranty Association members could experience premium increases. As explicitly stated by Ohio law, member insurers may consider assessment obligations when setting premium rates. Any local governments, school districts, universities or transportation authorities who provide medical, disability, or long-term care insurance for employees and students through nonself-funded programs could be susceptible to premium rises by Guaranty Association members. Under existing law, member insurers would be expected to raise premiums to cover assessments in the event of an impaired or insolvent insurer. If benefit liability limits are raised by S.B. 223, total Association liabilities would be expected to rise, forcing members to pay more in assessments and increasing the amount by which they could raise premiums to meet their obligations. Premium increases may be partially or fully mitigated by the tax benefit explained above.

All state of Ohio employee plans are self-funded, as are a portion of local municipalities. According to the State Employee Relations Board 2015 Annual Report on the Cost of Health Insurance in Ohio's Public Sector, about 70% of local public health insurance plans are self-funded and would not be susceptible to premium rises. That means approximately 30% of local governments and school districts could see higher premium rates for their health and disability insurance policies than they would without S.B. 223. The size of the additional premium rise for each local entity would depend on the size of the liquidated insurer, the proportion of state premiums written by their own insurer, and the proportion of the assessment that their insurer chooses to recoup through premiums. Given the assessment cap to Association members of 2% of premiums written annually, the additional premium rise for policyholders due to this bill is likely to be much lower than that.

Since effects of the bill are entirely conditional on the insolvency of insurers, the future frequency of which is unknowable, the potential fiscal effects have a wide range of possible outcomes. The most immediate threat of insolvency, Penn Treaty Network America Insurance Company and its subsidiary American Network Insurance Company, both based in Pennsylvania, has been involved in court proceedings regarding liquidation since 2009. These companies are long-term care insurers and as of December 31, 2013, had about 2,500 policyholders in Ohio. If we assume 8%[4] of the policyholders file a claim, about ⅒ of those result in claims over $100,000, and of the claims over $100,000, the average payout from the Association is $200,000 (capped at $300,000 for long-term care), then the additional assessment needed from the Association members due to the changes made in S.B. 223 would be around $2 million. That additional amount could be taken as a tax offset in increments of 20% beginning in the next biennium. By these estimates, the GRF could see a decrease of $400,000 in annual revenue beginning in FY 2018 due to changes to the Association liability limits. Additionally, since a portion of GRF tax receipts is subsequently transferred to the LGF

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[4] Estimated from historical data in a 2010 report by the American Association for Long-Term Care Insurance. Full report can be found at https://www.aaltci.org/subpages/resources/claimsreport.pdf.

and the PLF, the potential revenue loss to those local funds would total about $6,600 annually for a period of five years.

Future insolvencies beyond Penn Treaty are both unforeseeable and very likely. Through 2013, the Association had supported 35 insolvencies since its inception, resulting in approximately $126 million in assessments billed to member insurers (net of refunds). Assessment composition has been 38% life insurance policies, 15% health insurance policies, and 47% annuity contracts, with an annual average[5] of $5.25 million in total assessments. A generally conservative estimate is that the bill would add 25% to those annual costs over the long term, which would result in about $1.3 million extra in assessments to insurers per year on average, and subsequent annual decreases to the GRF of the same amount (due to the tax offset). The actual increase in assessments and decrease to the GRF in some years would be greater than those figures, but would also be accompanied by some years in which there is no difference at all. There is some potential for the cost of this bill to be much larger in future years due to the possibility, however remote, of industry-wide failure in life and health insurance, resulting in multiple large insurers being liquidated within a short period of time. In that case, increased Association liability limits would be beneficial to policyholders of the liquidated insurers, but the increased assessments to remaining member insurers would result in greater tax offsets and widespread premium increases which could be in the tens or even hundreds of millions.

Subrogation provision suspension

The bill suspends a provision[6] enacted in Am. Sub. H.B. 64 of the 131st General Assembly which provided that a subrogee's claim be reduced proportionally (between insurer and injured party) whenever less than the full value of a tort action is recovered. This type of proportionate sharing of recovery is currently required by law in 35 other states. When enacted in H.B. 64, this provision had the potential to decrease costs recovered by insurance companies, possibly resulting in a rise of future premium rates to consumers. The provision in H.B. 64 took effect on September 28, 2015. The provision in S.B. 223 suspends this action from the effective date of the bill until January 1, 2017.

Fiscal effect

This would temporarily reverse the fiscal effects of the provision from H.B. 64, and could impact the state's and local governments' costs of providing health benefits to employees and their dependents. This provision will affect governments differently based on (1) whether their insurance programs are self-funded and (2) when (and if) the H.B. 64 provision would be taken into consideration in setting premiums for their health plans. For the state and approximately 70% of local public health insurance plans which are self-funded, the suspension will allow higher cost recovery (as before H.B. 64)

[5] Based on 24 full calendar years of data since the Association began (1990-2013).

[6] R.C. 2323.44

through December 31, 2016. For these entities, the fiscal effect of the provision should be a net positive. The state, for example, typically sets health premiums in May each year for the fiscal year that begins the following July. Thus, FY 2016 health insurance premiums were determined in May 2015, possibly before the H.B. 64 provision was known to the Department of Administrative Services (DAS), and therefore assuming cost recovery from subrogation. The H.B. 64 provision would have prevented the cost recovery that may have been assumed in setting premiums; this provision of S.B. 223 allows the cost recovery for FY 2016, and DAS will be able to factor the lack of such cost recovery after January 1, 2017 into premiums set for FY 2017.

For the remaining 30% of local governments and school districts, the fiscal effect of the suspension would be indirect, and dependent on when their insurers set health premium rates which they pay on behalf of their employees. The suspension may have the potential to temporarily ease upward pressure on premiums, but its fiscal effects would be dependent on when the premiums are set and whether or not the insurer factors the subrogation change (and suspension) into the price. The magnitude of this fiscal effect is difficult to determine. Many health insurance carriers have already finalized their premium rates for part or all of 2016, but LSC does not know whether the H.B. 64 provision was factored into determining those rates by any given insurer. Also, subrogation only comes into play when an insured person is severely injured and the costs of the accident greatly exceed the at-fault party's insurance limits. As a portion of all claims, this happens in relatively few cases which means the effects on premiums spread out over all consumers, or cost recovery for self-funded plans, could be minimal even without this temporary suspension.

Other provisions

The bill amends language for reinsurance contract requirements. A domestic life insurance company will require approval of the Superintendent of Insurance to enter into reinsurance agreements above certain thresholds of magnitude. The bill also updates prompt payment claim codes, and adds an emergency clause to the Ohio Life and Health Insurance Guaranty Association changes and the suspension of the subrogation provision from H.B. 64. The emergency clause added to the suspension should result in an extra 90 days of cost recovery by self-funded programs. The emergency clause added to the Guaranty Association provision may result in additional state revenue loss if there is an insolvency (such as Penn Treaty) declared during the first 90 days after the bill's effective date. The timing of the potential revenue losses would depend on when the Guaranty Association members pay their initial assessments, and the initial tax year for which tax credits are claimed. The fiscal effects of the provisions regarding reinsurance requirements and prompt payment claim codes are estimated to be negligible.

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