Ohio Legislative Service Commission

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Fiscal Note & Local Impact Statement

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

Date: October 21, 2015

Status: As Reported by Senate Insurance

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

State Fiscal Highlights

STATE FUND	FY 2016	FY 2017	FUTURE YEARS
General Revenue Fund			
Revenues	- 0 -	- 0 -	Loss
Expenditures	- 0 -	- 0 -	- 0 -

Note: The state fiscal year is July 1 through June 30. For example, FY 2016 is July 1, 2015 – June 30, 2016.

- 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.

Local Fiscal Highlights

LOCAL GOVERNMENT	FY 2016	FY 2017	FUTURE YEARS
Counties, municipalities, townships, and public libraries			
Revenues	- 0 -	- 0 -	Minimal loss
Expenditures	- 0 -	Potential small increase	Potential small increase

Note: For most local governments, the fiscal year is the calendar year. The school district fiscal year is July 1 through June 30.

- 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. The additional premium rate is essentially capped at less than 2% annually, but actual additional premium is likely to be minimal.

Detailed Fiscal Analysis

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

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

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 this bill will be a result of the Guaranty Association 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 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.

[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.

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. 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.

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 would likely raise premiums to meet their obligations.

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 life and health 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

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[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.

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 1⁄10 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 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 longterm, 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.

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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.

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