

ISSUES FOR THE 82ND TEXAS LEGISLATURE

TAKING CARE OF TEXANS: Financial Security and Economic Impact



TALHI 
Texas Association of
Life & Health Insurers



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Dear Members of the 82nd Texas Legislature:

The Texas Association of Life and Health Insurers (TALHI) represents more than 100 life and health insurers doing business in Texas. TALHI's members provide products to thousands of Texans, offering them financial stability for their futures and protection against unforeseen events. Our organization is here to serve as a resource to you in the development of public policy that allows us to make these products available.

Insurance, in all its forms, is about financial security. Individuals who purchase insurance products do so to provide themselves and their families a guarantee that their financial well-being will be stable even during difficult and unanticipated developments.

Our industry values the important role that the state plays to guarantee that insurers are solvent, scrupulous and living up to their contracted obligations. We also believe the state has a critical role in maintaining a healthy insurance market that contributes to price competitiveness and product diversity, and encourages insurers to bring capital to Texas.

TALHI is proud of its strong tradition of providing state leaders resourceful and insightful information about the issues affecting our industry and Texas consumers. We welcome the opportunity to support you during your deliberations and to work together to strengthen the industry's ability to continue providing financial security to the citizens of our state.

Thank you for your service to Texas.

Sincerely,

A handwritten signature in blue ink that reads "Jennifer Alvaron Cawley". The signature is written in a cursive style.

Jennifer Cawley, JD
Executive Director



About TALHI

Texas Association of Life and Health Insurers

TALHI is the trade association for life and health insurers doing business in Texas. It was formed when Texas Life Insurance Association and the Texas Legal Reserve Officials Association merged in 1997.

Now representing the majority of insurers in the state, TALHI has emerged as a leading voice for life and health insurers on legislative and regulatory matters.

TALHI is an open-door trade association boasting some of the most progressive life and health insurance company officials in Texas. We are united for the mutual benefit and development of a healthy and competitive insurance market.

The work that TALHI does in the public policy arena is intended to strengthen the insurance market by enhancing insurers' ability to provide Texans financial security for their future.

We welcome the opportunity to work with you.



Providing Financial Security

Insurance plays an integral role in the lives of Americans. Health insurers provide security from the financial uncertainties of health care costs for more than 200 million individuals.⁽¹⁾

In 2009, life insurers provided \$19 trillion in protection for American families. Some \$59 billion in death benefits were paid at a time when individuals and families needed it most. Helping to ensure long-term financial security, insurers provided individual annuity owners \$42 billion in annuity benefits.⁽²⁾

Additionally, life insurance companies paid billions more for long-term care insurance coverage and disability income to replace lost wages.

While life and health insurers provide vital services to millions of people in thousands of communities, the importance of the industry extends far beyond insurance. Life insurers:

- Have more than \$5 trillion invested in the U.S. economy, making them one of the largest sources of investment capital in the nation.⁽³⁾
- Have been the largest source of bond financing for corporate America since the 1930s, with \$2.6 trillion invested in 2009.⁽⁴⁾
- Held more than \$331 billion in government bonds at the end of 2009.⁽⁵⁾
- Owned approximately \$314 billion in commercial mortgages in 2009.⁽⁶⁾

Life and health insurers have comforted Texans through challenging times, whether it is the death of a loved one or a business partner, a health crisis, or the uncertainty of retirement.

In 2008, \$20 billion was paid to Texas residents in the form of death benefits, matured endowments, policy dividends, surrender values and other payments. Annuity benefits provided an additional \$4 billion.⁽⁷⁾

In 2007, health insurers paid more than \$22 billion in health care costs for Texans.⁽⁸⁾

Providing Financial Security for Texans

- Approximately **13.5 million** Texans are covered by private health insurance.⁽⁹⁾
- Texas residents have **\$2 trillion** in death benefit coverage.⁽¹⁰⁾
- There are **11 million** individual life insurance policies in Texas, with coverage averaging \$100,000 per policyholder.⁽¹¹⁾
- Group life insurance provides **\$720 billion** in coverage.⁽¹²⁾
- In 2008, **\$130 billion** of individual life insurance coverage was purchased in Texas.⁽¹³⁾





Investing in Texas

Insurance companies also provide critical investment capital to Texas businesses and governments for long-term projects. These investments help fund urban renewal and support the state’s infrastructure with projects ranging from transportation and hospitals to school construction.

Insurance companies are the largest institutional investor of municipal bonds in the state. This capital contribution is manifested in a number of ways that benefit the state, including financing for public utilities and housing.

The stability of the insurance industry is essential to the state’s economy — providing jobs, tax revenue and important reinvestment in the state.

Some 145,000 Texans are employed in the life insurance industry, including 60,000 direct jobs and 85,000 indirect jobs. Life and health insurers are a stable source of employment, and the 145,000 jobs represent a \$7 billion annual payroll. Nationwide, about 2.5 million people are employed in the life insurance industry.⁽¹⁴⁾

In Texas, 598 life insurers are licensed to do business and 128 are domiciled in the state.⁽¹⁵⁾

Health insurers employ more than 23,000 Texans at an average wage of over \$50,000.⁽¹⁶⁾

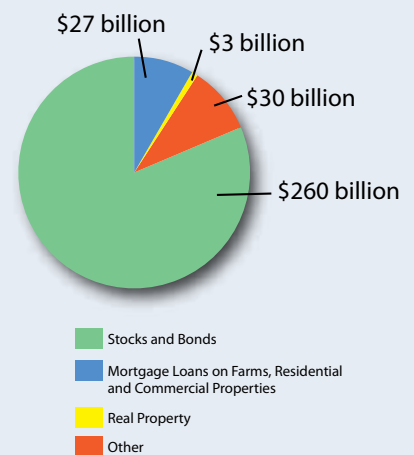
Reasonable Regulations Offer Consumer Protection and Market Stability

While insurers support the state’s regulatory role, regulations must remain fair and equitable to allow insurers to continue to invest in our country’s economic foundation.

Insurers place priority on working with policymakers to ensure that reasonable regulations exist to protect consumers while fostering a strong insurance market that offers competitive pricing and a diverse array of insurance products. Insurers understand better than anyone that maintaining confidence and stability in the insurance market is critical to both consumers and insurers.

In addition to relying on the worthiness of policies offered, consumers must also have confidence and trust in the agents and companies that offer insurance products. Licensure, suitability and disclosure laws protect consumers from unfair and fraudulent business practices. The insurance industry in Texas

Life Insurers Investing in Texas: \$320 Billion



Source: American Council of Life Insurers



is proud of its role in supporting past legislative efforts to ensure appropriate oversight and protections are in place. But the industry is also keenly aware of the adverse impact of over-reaching regulation.



For example, requiring companies to have greater reserves than are necessary to meet their obligations restricts the number of policies that can be offered. Price controls mandated by rate regulation make the market less attractive to insurers, limiting competition and reducing consumers' choices.

The Texas insurance industry supports fair regulation, but striking a balance between appropriate oversight and maintaining a healthy market is not always easy. Over-regulation and over-taxation of the insurance industry can produce a less attractive market, reduce the number of companies participating and decrease the number of products available for consumers. Less competition, fewer products and higher prices are not in the best interest of consumers.

TALHI recognizes the challenge of striking that proper balance and welcomes the opportunity to work with lawmakers, consumers and other stakeholders to ensure that Texas continues to benefit from a stable and competitive insurance market.

There are 11 million individual life insurance policies in Texas, with coverage averaging \$100,000 per policyholder.

Insurers' Taxes are Among Highest

In addition to the billions they invest in public and private projects, life and health insurance companies are also a major source of tax revenue for federal and state governments.

Life insurance companies paid \$15 billion in taxes to federal, state and local governments in 2009.⁽¹⁷⁾ As employers of more than 333,000 home-office personnel, U.S. life insurers also paid \$2 billion in Social Security taxes in 2009, a figure that does not include Social Security taxes paid by employees or self-employed agents.⁽¹⁸⁾ Miscellaneous taxes, licenses and fees accounted for more than \$1 billion in 2009.⁽¹⁹⁾ These taxes do not include amounts associated with investment management.

Taxes on premiums that life insurers collect in each state are another significant tax obligation. In 2009, U.S. life insurers incurred \$4 billion in state taxes on premiums collected from life, health and annuity business.⁽²⁰⁾ In Texas, insurers pay disproportionately higher taxes than they do in other states.

Life and health insurance companies operating in Texas are subject to a gross receipts tax known as premium tax, while most other financial institutions and general corporations are subject to the state's lower franchise tax. As a result, in fiscal year 2009, insurance companies in Texas paid more than \$1.4 billion in premium taxes; nearly three times more than what they would have paid under the franchise tax.⁽²¹⁾



The Texas premium tax is based on gross premiums received by an insurer operating in the state. The corporate franchise tax is based on net taxable capital or net taxable earned surplus (net income) apportioned to Texas. A 2005 study by Ernst & Young found that because the premium tax applies to a tax base much larger than the base of the franchise tax, the premium tax, combined with other state and local taxes, imposes a significantly higher tax on life/health insurers than if they were taxed as general corporations.

New or higher taxes also put the industry at a competitive disadvantage because increased taxes must be reflected in premium rates. As rates increase, the amounts companies must pay in premium taxes also rises, thus increasing insurers' overall tax burdens disproportionately. Higher taxes in Texas also put Texas insurance companies that operate in other states at a competitive disadvantage as the other states retaliate with higher taxes on Texas-based companies.

A sluggish economy and the prospect of additional taxes could jeopardize the industry's ability to continue to serve as a key source of capital for state and local governments. Additionally, increasing taxes on insurers at a time when the industry is adjusting to major federal reforms in the financial and health care sectors will add to the increasing administrative costs that are often passed on to consumers in the form of higher premiums.

Given these circumstances, TALHI would be opposed to an increase in taxes on insurers during the 2011 legislative session.

Sunset Review of the Texas Department of Insurance

As the Legislature undertakes sunset review of the Texas Department of Insurance (TDI) this session, attention will be drawn to the critical role TDI plays in determining the strength and viability of the Texas insurance market.

Because of its fair and balanced approach, TALHI believes TDI is among the premier state regulatory agencies in Texas and is a leader among the state insurance regulators in the United States. Adopting the Sunset Advisory Commission's recommendations will continue TDI's position of strength and effectiveness in its oversight of the insurance industry.

TALHI supports the commission's recommendation to continue TDI and believes the agency's statutory duties should be updated to better reflect its role in protecting consumers and encouraging a competitive insurance market in Texas. Specifically, the standard across-the-board requirement for the Sunset Commissioner to develop a policy regarding negotiated rulemaking and alternative dispute resolution should be applied.

Health insurers employ more than 23,000 Texans at an average wage of over \$50,000.





The Sunset Commission also found that the department's statute has not kept pace with available electronic transaction technologies. TALHI endorses and supports the 2008 findings of the Sunset Advisory Commission relating to electronic transactions technologies and supports recommendation 7.1 of the Sunset Advisory Commission report on electronic commerce transactions.

Sunset review is an opportunity to strengthen TDI's regulatory process and modernize its operations. Increasing the use of information technology for the agency's reporting and data collection will streamline the form-filing process while improving communications between consumers, health plans and providers. Eliminating outdated and extraneous reporting requirements on health plans can improve the efficiency of the agency's oversight and reduce unnecessary costs for the state and insurers.

No one better understands the essential role of fair and efficient regulation for their industry than insurers. It is for that reason that insurers place a high priority on working with state policymakers and regulators to ensure consumers are protected while promoting a stable market that offers competitive pricing and a wide range of insurance products.

In 2008, \$20 billion was paid to Texas residents in the form of death benefits, matured endowments, policy dividends, surrender values and other payments.



Adoption of NAIC Model Life and Health Guaranty Association Act Will Strengthen Texas' Guaranty Fund

The Texas Life, Accident, Health and Hospital Service Insurance Guaranty Association (Association) was created by the Texas Legislature in 1973 to protect the state's resident policyholders should their Texas-based insurance company become insolvent or be placed in liquidation. In the event of an insolvency or liquidation, the Association continues insurance coverage and pays claims and certain policy benefits up to specific limits, similar to how the FDIC insures bank deposits on the federal level.

Membership in the Association is mandatory for an insurance company licensed to sell life, health or annuity policies in the state. Should a member insurer become insolvent or be placed in liquidation, the other estimated 1,100 licensed insurers in Texas are assessed the amount needed to meet the failed company's obligations.

The current coverage limit for benefits provided by the Association for annuity contracts is \$100,000 per life. This level of protection has not been changed since it was established in 1973 at the time the



Association was created. Because the limit is lower than that for residents of other states, Texas consumers could be unfairly penalized if their annuity company becomes insolvent.

To make Texas limits consistent with most other states, TALHI supports the adoption of the National Association of Insurance Commissioners (NAIC) 2009 Model Life and Health Guaranty Association Act recommendation that annuity coverage limits be increased to \$250,000 per life. Specifically, the Model Act recommends annuity limits be increased to:

- \$250,000 per life;
- \$250,000 per life for each participant in 401, 403(b) or 457 governmental retirement plans with unallocated annuities; and
- \$250,000 for payees for structured settlement annuities.

While such an increase will almost certainly raise the assessments made against insurers to fund claims against an insolvent or liquidated company, the industry believes the change is important to ensure consumers are protected and to sustain confidence and stability in the insurance and annuity markets.

The Model Act also clarifies the Association's rights with respect to statutory or special deposits. Currently, the Texas Insurance Commissioner may require an insurer to deposit funds in Texas as security against insolvency. How those funds are dispersed during insolvency often results in disputes and uncertainty.

A Model Act provision pertaining to the Association rights regarding reinsurance is also important. The Association's reinsurance rights are not currently spelled out, creating unnecessary conflicts and hampering the Association's attempts to transfer policies to solvent insurers. Because the Association is obligated to continue insurance coverage in addition to paying claims, the reinsurance that is associated with the policies is a vital component of providing coverage and on transferring the policies to a solvent insurer. It is in the consumers' interest for their policies to be assumed by a solvent insurer, rather than have long-term coverage provided by the Association.

TALHI supports the adoption of the provisions from the Model Act that specify the Association's rights with respect to reinsurance, specifically regarding its ability to assume the rights and obligations of an insolvent member insurer. Specifying the Association's right in this regard benefits Texas consumers by ensuring valuable reinsurance remains in place while the Association continues coverage and as it transfers policies to a solvent insurer.

The Texas Department of Insurance has also voiced its support for the adoption of the NAIC 2009 Model Life and Health Guaranty Association Model Act.



In Texas, 598 life insurers are licensed to do business and 128 are domiciled in the state.



Texas Is Among Nation's Leaders in Providing Consumer Protections During Sale of Annuities

Annuities are an important financial tool for consumers. They allow individuals to prepare for anticipated financial needs by making deposits into a fund that will yield regular payments at a predetermined future date – most often retirement.



The life insurance industry nationally is the largest source of bond financing for corporate America, and has been since the 1930s, with \$2.6 trillion invested in 2009.

The financial security that annuities can offer heightens the importance of ensuring consumers' interests are protected through the annuity sales process and that the integrity of the agents who offer these products remains strong.

TALHI is pleased to have worked side by side with Texas legislators to help pass national model reform acts that give new powers to the Texas Department of Insurance (TDI) to stop fraud and the potential for abuse in the sale of annuities. As a result, Texas lawmakers are among the leaders in the nation in safeguarding seniors and others from unscrupulous practices in the sale and marketing of annuities.

In 2007, Texas adopted the National Association of Insurance Commissioners (NAIC) model regulation, setting standards and procedures to ensure agents or insurers will recommend annuity products that are suitable to the insurance and financial needs of consumers at the time of purchase. Lawmakers also approved minimum standards for the conduct of agents and insurers for transactions involving replacement of a life insurance or annuity product.

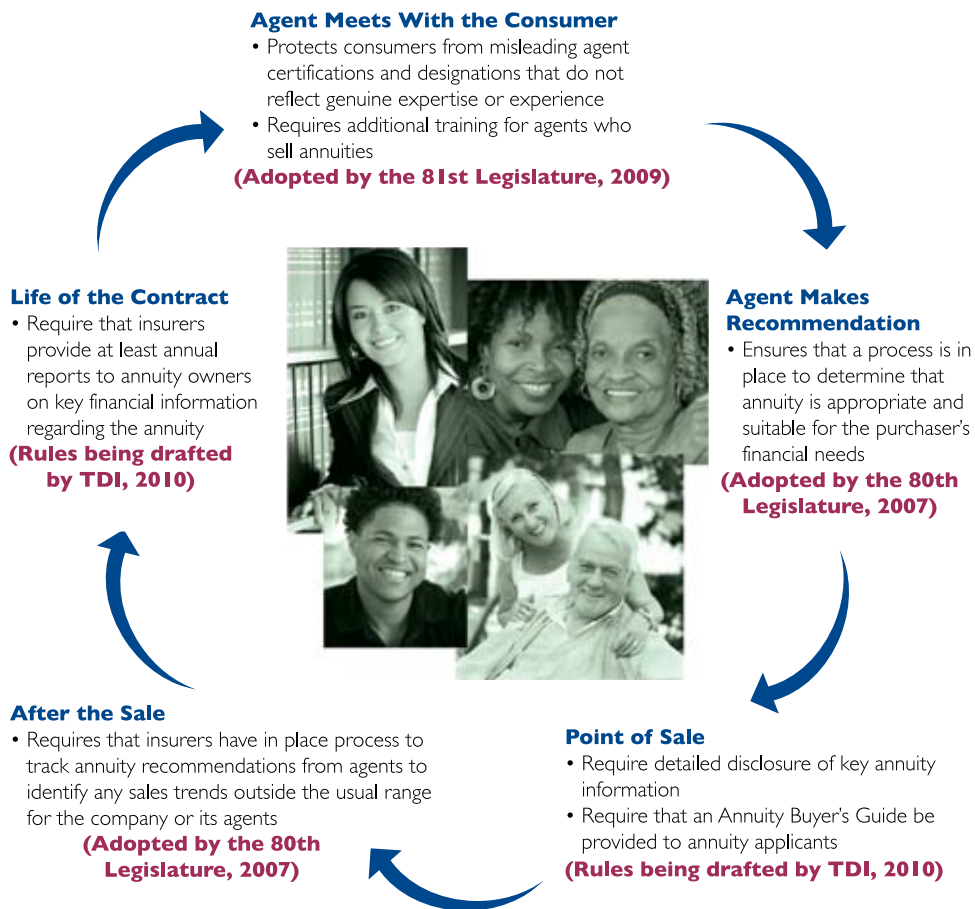
Both laws provided the Texas Insurance Commissioner the authority to order full restitution for Texas residents harmed during the sale of an annuity and to revoke or cancel the insurer's certificate of authority or the license of the agent responsible for the sale.

In 2009, the Texas Legislature took additional steps to protect consumers from rogue agents who use designations and certifications that are not earned, are self-conferred or that imply a level of professional qualifications the agent does not possess. As a result, the TDI adopted permanent rules requiring four hours of initial training and four hours of annual continuing education requirements for agents who sell, solicit or negotiate an annuity contract or represent an insurer in relation to annuity products.

Lawmakers also adopted a bill requiring detailed disclosure of annuity rates, including key information explaining how rates change and a summary of options and restrictions. The governor supported the consumer provisions in the bill, but he vetoed it based on his belief that it would create a new private cause of action. The governor directed the Texas Insurance Commissioner to adopt the consumer protections contained in the bill in the form of new rules. Once adopted, the new guidelines will outline



Buying an Annuity in Texas



the types of information about an annuity contract that must be provided to Texas consumers and the method for disclosure.

The Next Step in the Regulation of Annuity Sales

To build on the progress being made to ensure consumer suitability in the sale of annuities, the NAIC has adopted the Suitability in Annuity Transactions Model Regulation (SAT).

The proposal, supported by TDI, includes an expanded list of consumer suitability information, new supervisory responsibilities when an insurer has contracted functions to a third party, a review of all recommended sales, and the establishment of standards for general annuity training and insurer product-specific training of all agents.



TALHI believes the SAT could be improved to ensure that enforcement actions for unsuitable sales are appropriate by basing sanctions on a “pattern or practice” as applied by the Unfair Trade Practices Act rather than a single violation. TALHI also believes the third party training requirements and timing contained in the SAT can be refined to more closely track what insurers are required to provide and what may be obtainable within the proposed time frame.

TALHI supports the SAT, with the aforementioned refinements, and believes its passage is important to maintaining the momentum state leaders have established in protecting senior Texans and others from unscrupulous practices in the sale and marketing of annuities. TALHI welcomes the opportunity to work with the Texas Legislature toward the passage of the SAT to ensure such safeguards are in place.



The life insurance industry nationally has more than \$5 trillion invested in the U.S. economy, making it one of the largest sources of investment capital in the nation.

Federal Health Care Reforms Impact on the Texas Market

Whatever the ultimate fate of the federal health care reforms of 2010, it’s clear the debate and adoption of the Patient Protection and Affordable Care Act (PPACA) will serve as the foundation for the redefining of our nation’s health care system. While the goal of the reforms to provide universal access to affordable health care coverage is embraced by most, the path to such an achievement is a difficult one fraught with risks that could undermine the very objective being sought.

New restrictions on health plans’ medical loss ratios (MLR) will force insurers to alter how they fund their administrative operations and will likely force reductions in the programs and support health plans provide to improve the quality of health care for their enrollees. The limits have already contributed to decisions by several insurers operating in Texas to exit the health insurance market. Should such a trend persist, disruption in the Texas health insurance market could result, leaving consumers and businesses with fewer choices and higher prices for coverage. To minimize market disruption, TALHI encourages the state to exercise its option to seek a waiver from immediate enforcement of the new MLR standards to provide a transitional period for their implementation.

While much of the federal debate focused on insurance premiums, the legislation does little to address rapidly rising medical costs – the underlying cause of premium increases. Federal and state regulatory review of insurance premiums may provide public assurance that the government is watching. However, to maintain a stable insurance market, such a review must be based on fundamental insurance principles and be tied directly to the actuarial soundness of those rates.



The ability of health insurers to offer coverage without regard to pre-existing medical conditions is a central tenet of the reforms. This guarantee of coverage is made possible by an expanded risk pool across which the increased risk (health costs) can be spread. The requirement that all Americans obtain health coverage is the key to creating an expanded risk pool. Without such a mandate, the Congressional Budget Office has projected that insurance premiums could rise as much as 30 percent, making coverage less affordable, increasing the number of uninsured and leading insurers to exit the market.

Of special importance to Texas is the requirement that every state establish a regulated market for the purchase of health insurance. These markets, to be known as Health Benefit Exchanges, are to be established by January 1, 2014, and will offer a series of standard policies that will provide comprehensive health coverage. In those states that opt not to establish an Exchange, the federal government will manage it for them. States that choose to establish their own must demonstrate their ability to do so by 2013.

The federal government has projected that by 2019, as many as 24 million individuals may seek their health coverage through an Exchange. With Exchanges serving as a primary market for the purchase of health coverage, it is anticipated that most states will want to retain their traditional insurance regulatory role by managing their own Exchanges. TALHI supports and encourages Texas leaders to maintain control of this key component of the state's insurance market. Doing so will ensure regulatory consistency and stability both inside and outside the Exchange.

While the major medical policies providing comprehensive coverage will be offered both inside and outside the Exchange, supplemental insurance policies will continue to be available for consumers wishing to purchase them outside the Exchange.

Supplemental policies offer additional protection for expenses that may not be covered by primary insurance. These are especially beneficial for self-employed individuals, families with children, those unable to manage large medical bills or time off from work, and those on Medicare. Medicare supplement, long-term care and cancer policies are among the more popular types of supplemental insurance.

Coverage provided by supplemental policies was explicitly exempted from the Health Insurance Portability and Accountability Act (HIPAA) of 1996. The PPACA builds upon the statutory structure adopted through HIPAA and, as a result, exempts supplemental policies from the market reforms contained in the 2010 federal reforms.

The state can ensure that Texans' access to a broad range of supplemental coverage choices remains intact by ensuring their exemption from new state regulations that may result from the PPACA.

In fiscal year 2009, Texas insurance companies paid more than \$1.4 billion in premium taxes, nearly three times more than what they would have paid if subject to the state's lower franchise tax.





Footnotes

¹ U.S. Census Bureau

² American Council of Life Insurers, www.acli.org

³ Ibid

⁴ Ibid

⁵ Ibid

⁶ Ibid

⁷ Ibid

⁸ www.window.state.tx.us/comptrol/cra07/ch03.html

⁹ U.S. Census Bureau

¹⁰ American Council of Life Insurers, www.acli.org

¹¹ Ibid

¹² Ibid

¹³ Ibid

¹⁴ Ibid

¹⁵ Ibid

¹⁶ 2007 Health Insurance: Overview and Economic Impact in the States, www.ahip.org

¹⁷ American Council of Life Insurers, www.acli.org

¹⁸ Ibid

¹⁹ Ibid

²⁰ Ibid

²¹ Ibid



TALHI Membership

REGULAR

Aegon USA, & Affiliates
AFLAC
Variable Annuity Life Insurance Company
Allianz Group
American Fidelity Group
American National Insurance Company
Americo Group
Assurant Group
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Central States Group
Colonial Life Insurance Co. of Texas
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National Life Group
National Teachers Associates Life Insurance Company
Nationwide
New York Life Group
Pacific Life Insurance Company
Physicians Mutual Group
Primerica Life Insurance Company
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