

STORAGE NAME: h1089a.fs

DATE: April 17, 1997

**HOUSE OF REPRESENTATIVES
COMMITTEE ON
FINANCIAL SERVICES
BILL RESEARCH & ECONOMIC IMPACT STATEMENT**

BILL #: HB 1089

RELATING TO: Insurance

SPONSOR(S): Representative Littlefield

STATUTE(S) AFFECTED: ss. 628.6017 and 627.215, F.S.

COMPANION BILL(S):

ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:

- (1) FINANCIAL SERVICES YEAS 14 NAYS 0
- (2) FINANCE & TAXATION
- (3) GENERAL GOVERNMENT APPROPRIATIONS
- (4)
- (5)

I. SUMMARY:

Insurers have been subject to financial tests since 1979 to determine if they have earned profits exceeding levels allowed in s. 627.215, F.S. -- the excess profits law. If profits are found to be excessive, the Department of Insurance (DOI) requires insurers to refund or credit the excess to the policyholders of record.

Assessable mutual insurance companies that convert to stock insurers, though exempt from the operation of the excess profits law, have been required to hold in surplus for five years any amounts that would have been refunded if the law were applied.

The bill repeals the excess profits law and removes all requirements on assessable mutual insurance companies related thereto.

The Committee on Financial Services adopted two amendments that are more fully described below in Section VI.

II. SUBSTANTIVE RESEARCH:

A. PRESENT SITUATION:

To avoid having insurers reap excess profits resulting from workers' compensation reforms -- particularly the creation of "wage loss" -- the Legislature enacted the Workers' Compensation Excess Profits Law (Chapter 79-40, Laws of Florida; s. 627.215, F.S.) (see *John Deere Ins. Co. v. State, Dept. of Insurance*, 463 So.2d 385, 388 (Fla.App. 1 Dist. 1985). Section 627.215, F.S., seeks to transfer the financial benefits of these public policy decisions back to the policyholders. Though initially limited to workers' compensation and employer's liability insurers, the law (since 1988) now applies to commercial property and casualty insurance.

Worker's compensation reforms similar in magnitude to those made in 1979 have occurred several times since then, most recently in November 1993 (see Chapter 93-415, Laws of Florida).

The law measures "excess" profits in terms of the size of an insurer's underwriting gain or loss for the three most recent calendar-accident years for each subject line. Profits are considered excessive "if the net aggregate underwriting gain for all these lines combined is greater than the net aggregate anticipated underwriting profit for these lines plus five percent of earned premiums" Policyholder refunds or credits towards the future purchase of insurance are required if excess profits are calculated for filings made in the years 1991 forward.

The allowable underwriting profit is calculated using a factor referred to as a "profits and contingency factor." Although a part of each insurer's rate filing, the factor is calculated by the National Council on Compensation Insurance (NCCI) in the case of workers' compensation insurance, and reflects the ultimate payout requirements of premium dollars received. The factor is applied to each year's earned premiums in the three year cycle, plus the five percent margin, to produce the allowable underwriting profit. The amount by which the allowable profit exceeds the underwriting gain or loss is the amount of excess profits.

The existence of excess profits is a part of the reasonableness test for the insurer's rates. As such, the DOI has discretion to adjust the profit and contingency factor to reflect overall operating demands.

According to the DOI, no excess profits were identified for worker's compensation carriers from 1985 through 1990. In 1991 and 1992, the data filed by insurers combined all lines of businesses together, and no distinct excess profits figure in worker's compensation could be derived. Data for 1993 -- the year the Legislature last enacted major workers' compensation reforms -- through 1995 is still under review.

Section 628.6017, F.S., governs the process by which an assessable mutual insurer may convert to become a stock insurance company. Assessable mutual companies are distinguished in that they issue no permanent capital stock. The procedures governing conversion to stock status include an exemption from s. 627.215, F.S. -- the excess profits law. Despite the exemption, an assessable converting to a stock insurer or nonassessable insurer is required to file the data necessary to determine the existence

of excess profits. If that data indicates excess profits would have resulted, the insurer is required to place the amount of any refunds into surplus for five years.

B. EFFECT OF PROPOSED CHANGES:

The repeal of the excess profits law ends the requirement that workers' compensation insurers and commercial property and casualty insurers refund or credit any amounts they receive as allowable profit over and above their underwriting gain or loss. The bill also makes conforming revisions to the conversion statute for assessable mutual insurance companies, to remove cross references to the excess profits law.

C. APPLICATION OF PRINCIPLES:

1. Less Government:

a. Does the bill create, increase or reduce, either directly or indirectly:

(1) any authority to make rules or adjudicate disputes?

No.

(2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

No.

(3) any entitlement to a government service or benefit?

No.

b. If an agency or program is eliminated or reduced:

(1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

Not applicable.

(2) what is the cost of such responsibility at the new level/agency?

Not applicable.

(3) how is the new agency accountable to the people governed?

Not applicable.

2. Lower Taxes:

- a. Does the bill increase anyone's taxes?

No.

- b. Does the bill require or authorize an increase in any fees?

No.

- c. Does the bill reduce total taxes, both rates and revenues?

No.

- d. Does the bill reduce total fees, both rates and revenues?

The bill eliminates refunds or credits that insurers pay to policyholders that are calculated as excess profits. Insurers may have additional revenues at their disposal.

- e. Does the bill authorize any fee or tax increase by any local government?

3. Personal Responsibility:

- a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

No.

- b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

No.

4. Individual Freedom:

- a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

Yes. The bill removes excess profits tests for insurers in several lines of business.

- b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

No.

5. Family Empowerment:

- a. If the bill purports to provide services to families or children:

- (1) Who evaluates the family's needs?

No.

- (2) Who makes the decisions?

No.

- (3) Are private alternatives permitted?

No.

- (4) Are families required to participate in a program?

No.

- (5) Are families penalized for not participating in a program?

No.

- b. Does the bill directly affect the legal rights and obligations between family members?

No.

- c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

No.

- (1) parents and guardians?

No.

(2) service providers?

No.

(3) government employees/agencies?

No.

C. SECTION-BY-SECTION RESEARCH:

Section 1. Amends subsection (4) in s. 628.6017, F.S., to remove references to s. 627.215. The bill also removes the requirement that insurers file data supporting the excess profits test, and the requirement that insurers hold in surplus any amounts that would have been designated as excess profits.

Section 2. Repeals s. 627.215, F.S -- the excess profits law for certain lines of insurance.

Section 3. Provides that the bill will take effect upon becoming law.

III. FISCAL RESEARCH & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. Non-recurring Effects:

None.

2. Recurring Effects:

The DOI will no longer conduct excess profits tests in the rate process. This will result in a minimal indeterminate savings.

3. Long Run Effects Other Than Normal Growth:

None.

4. Total Revenues and Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

None.

C. **DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:**

1. Direct Private Sector Costs:

Policyholders are not likely to lose refunds they might otherwise have received since no refunds or credits have been made in recent years.

2. Direct Private Sector Benefits:

Insurers would gain only minimal benefits, if any, by avoiding the excess profits tests, since no refunds or credits have been made in recent years.

3. Effects on Competition, Private Enterprise and Employment Markets:

None.

D. **FISCAL COMMENTS:**

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. **APPLICABILITY OF THE MANDATES PROVISION:**

B. **REDUCTION OF REVENUE RAISING AUTHORITY:**

C. **REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:**

V. COMMENTS:

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VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

The Committee on Financial Services adopted two amendments at its meeting on April 16, 1997, which accomplish the following:

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Amendment #1 provides that the profit and contingencies factor may not be less than zero for purposes of calculating worker's compensation excess profits; repeals excess profits statute effective January 1, 1999.

Amendment #2 extends the existing restriction on applying the excess profits law to commercial liability, to also restrict its application to commercial umbrella liability insurance.

VII. SIGNATURES:

COMMITTEE ON FINANCIAL SERVICES:

Prepared by:

Legislative Research Director:

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