SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

BILL: SB 1786

SPONSOR: Senator Dawson

SUBJECT: Insurance (Life Insurance)

DATE: March 26, 2001 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Deffenbaugh	Deffenbaugh	BI	Favorable
2.				
3.				
4.				
5.				
6.				

I. Summary:

In recent years, the Florida Department of Insurance has focused attention on the problems associated with industrial life insurance and similar "low-value" policies, including a major settlement with an insurer charged with collecting racially-based premiums. Industrial life insurance has a small death benefit, typically under $1,000, sold to consumers as a way to cover burial expenses. Agents sold these policies door-to-door, collected weekly or monthly premiums, and signed a debit card as a receipt of money collected. Insurers have apparently stopped issuing new industrial life policies in Florida since 1997. However, there were about 1.2 million Floridians at the end of 1998 who were still paying premiums under industrial life policies in force. Also, other similar types of small amount, monthly debit ordinary life insurance policies continue to be sold which have high premiums relative to benefits.

The bill prohibits industrial life insurance policies from being issued in Florida on or after July 1, 2001. Each insurer that has such polices in force would be required to provide annual disclosures to policyholders, including the total premiums paid, the cash value, and the death benefits. If the insurer is unable to locate the policyholder, the policy must be converted to full paid-up status. The notice would not be required for polices that are in full paid-up status or converted to such status.

The bill requires life insurers to annually mail notice to each Florida policyholder who has a life insurance policy with a death benefit of $15,000 or less, the following information: the total amount of premiums paid, the cash value, and the amount of the death benefits.

The bill also would require life insurance policies issued after July 1, 2001, to increase the death benefit paid under the policy when the total premiums paid exceed a specified percentage of the death benefit. When the premiums paid exceed 250 percent of the death benefit, the insurer must

increase the death benefit by $0.50 for each additional premium dollar. When the premiums paid exceed 500 percent of the death benefit, the insurer must increase the death benefit by $1.50 for each additional premium dollar.

This bill substantially amends section 627.4555 of the Florida Statutes. The bill creates the following sections of the Florida Statutes: ss. 627.4553, 627.4587, and 627.5015.

II. Present Situation:

In recent years, the Florida Department of Insurance and its Office of the Consumer Advocate have focused attention on the problems associated with industrial life insurance and similar “low-value” policies (a term insurance representatives find biased, who prefer “small amount.”). Industrial life has a low death benefit, typically under $1,000 or $2,000, sold to consumers as a way to cover burial expenses. Also referred to as burial, debit, or home service policies, agents sold these policies door-to-door, collected weekly or monthly premiums, and signed a debit card as a receipt of money collected. A typical industrial life policy in force, according to the department, has a face value of $727 and premiums of $2.60 per month.

The states of New York (1980) and Arkansas (1988) have prohibited the sale of industrial life insurance policies. Florida law allows industrial life policies to be sold, but insurers have apparently stopped issuing such in the state since 1997. However, there were about 1.2 million Floridians at the end of 1998 who were still paying premiums under industrial life policies still in force. Also, other similar types of low value, ordinary life insurance policies continue to be sold, with monthly premiums, which have high premiums relative to benefits.

Industrial life policies are not subject to the same laws that apply to ordinary life insurance policies and typically have higher premiums relative to benefits than ordinary life insurance policies. The department cites as an illustrative case an 85-year-old man who paid $2,214 over 10 years on a burial policy with an $836 death benefit. Another example is a woman in her sixties who purchased four policies with a death benefit of $1,000 each and has paid a total of $7,754 in premiums. A third case is an 82-year-old woman was sold four small-value policies, with total death benefits of $1,750 who was still paying the premiums that had already amounted to $5,656.

Industrial life insurance policies are subject to the requirements of part IV of chapter 627, F.S. (ss. 627.501-627.522, F.S.). Insurers must report to the department all annual statement data regarding industrial life insurance. Under s. 627.522(2), F.S., the price of an industrial life insurance policy must be set forth in a "clear, conspicuous, and understandable manner." An insured is allowed a 30-day grace period for the late payment of premiums.

There are two main types of life insurance: "term" insurance, which is life insurance purchased for a specific period, and "whole life" insurance, which is coverage effective for life. Term insurance pays benefits only if the insured dies during the coverage period and does not usually accumulate cash value. Whole life insurance will pay the face amount at the insured’s death or at the policy’s maturity, usually at age 100, accumulates cash value, and premiums are usually at a fixed rate. There are many variations on these types of insurance, including policies that combine features of both.

Industrial life insurance can be either term or whole life, but it is separately classified and subject to different laws than "ordinary" term or whole life insurance. Some of these differences include:

- Under s. 626.790, F.S., insurance agents who sell industrial life policies may work for up to 6 months without meeting full licensure requirements. These persons receive a temporary license, and according to the Insurance Consumer Advocate, may lack sufficient insurance knowledge in dealing with their customers. With ordinary life insurance, agents must meet full licensure requirements.

- Unlike ordinary life insurance, an industrial life policyholder may not borrow against the cash value of the policy. Under s. 627.458, F.S., whole life or term insurance policyholders may do so.

- Section 625.121, F.S., requires that the price of industrial life insurance policies be based on the 1961 Mortality Table, while ordinary life insurance is priced according to the 1980 Mortality Table. Using an older mortality table may result in higher rates because life expectancies were not as long. (A mortality table is a statistical table used by the industry to identify death probabilities by age.)

The number of new industrial life policies issued in Florida declined dramatically in the 1990's and apparently are no longer being sold. Fewer than 1,000 industrial life policies were issued in Florida in 1994, 1995, and 1996, combined. In 1996, only three companies issued industrial life policies in Florida, i.e., Conger, Metropolitan and Western & Southern. (On November 18, 1997, Conger Life Ins. Co. went into receivership.) According to the department, no industrial life policies were issued in the state in 1997, 1998, or 1999.

In 1999 the Florida Department of Insurance began investigations against five insurers regarding sales practices of industrial life insurance, which led to the filing of a cease and desist order against American General Life and Accident Insurance Company alleging that the insurer was collecting higher premiums from African Americans based solely on their race. A private class-action suit was also filed against the insurer. Although racially-based policies were no longer being sold, the insurer allegedly did not eliminate or reduce the higher premiums on existing policies that were sold on a discriminatory basis. Many of the policies were sold by companies that had been acquired by American General, which said it unknowingly acquired racially priced policies. Besides the race issue, the department sought to address the issue of policyholders paying more in premiums than the face value.

In June 2000, the department and American General entered into a Regulatory Settlement Agreement concurrent with a settlement of the private class action suit. The settlement applied to the insurer's nationwide business and was ratified by insurance regulators from 26 states and approved by the federal court hearing the class-action lawsuit. Under the settlement terms, the insurer agreed to pay a $7.5 million penalty to be split among the states and $206 million in restitution to policyholders, including cash refunds, increased death benefits, and premium reductions. In addition to the race-based policies, the settlements covered industrial life policies that were sold without race being a factor, which had premiums that exceeded the face value.

In July 2000 the Florida and Georgia Departments of Insurance filed cease and desist orders against 28 other insurers to stop any collections of higher premiums from African Americans based on their race.

Even though industrial life insurance policies are apparently no longer being sold in Florida, low-amount, monthly premium (debit) ordinary life insurance policies continue to be sold for which premiums vary widely among insurers. According to the department, there is less competition among insurers in the low value market, generally categorized as policies providing less than a $15,000 death benefit. This allows insurers to charge rates in excess of what a more competitive market would allow. Also, the expenses associated with low-value policies are greater as a percentage of the benefits than for higher-value policies, which increases the premium to benefit ratio. As the case with industrial life polices, low-amount ordinary life policies are often sold to persons of low income, who are elderly, and lack insurance knowledge or sophistication of insurance products and have overall less expendable income. An industry survey of insurers[1] who specialize in the low-amount market found that the average face amount issued in 1997 was $6,265 and the average face amount in force was $4,600.

Insurance industry position papers[2] counter that small amount policies are well-understood and accepted by consumers, typically sold to elderly persons to cover death-related expenses. The policies have very limited underwriting of purchasers who have much higher mortality risk than younger or healthier populations. Many policies are paid with a single premium, but for those consumers who prefer a small monthly premium, the additional risk and reduced interest to the insurer must also be factored into the premiums. Examples of persons who pay one or two month's premium and receive full death benefits can be offered to counter worst-case examples. Even under whole life, large amount policies, premiums can accumulate, with interest, to exceed benefit levels. An industry survey of 22 insurers that specialize in the small amount market have a premium to death benefit ratio that is 58 percent greater than the industry average.

According to the industry position papers cited, if expense and risk charges are ignored, focusing only on claims and interest, the single premium cost of $1,000 of insurance for a male age 65, who wishes to make a single payment, would be approximately $400. This means that if all men aged 65 put $400 into an interest-earning fund, there would be enough in the fund to pay $1,000 at each death with normal interest rates. If, however, each man, age 65 wanted to make his payment in level monthly installments, instead of a lump sum, the fund would earn less interest and would receive less than the amount needed to fund benefits for those who die early. The monthly premium would be approximately $3.25, if expenses and risk charges were ignored. A person who lives to age 100 in this group will have paid $1,365 for his $1,000 of insurance.

The Standard Non-Forfeiture Benefit law, s. 627.476, F.S. applies to both ordinary life and industrial life insurance policies (s. 627.501, F.S.). This law provides certain minimum benefits that the insurer must guarantee if the policyholder stops paying the premiums. However, these values are based on the amount of life insurance benefits provided under the policy and are not affected by the premiums paid for the policy. This law also requires life insurance policies to

[1] "Small Policy Purchases by Seniors" (Draft), National Alliance of Life Companies (May 26,1999).

[2] Id.; "Small Amount Life Insurance," Life Insurers Conference (October 1994).

include a statement of the mortality table used and the cash surrender and paid-up nonforfeiture benefits available under the policy on each policy anniversary during the first 20 policy years or during the term of the policy, whichever is shorter.

The current law provides what appears to be an illusory benefit for industrial life insurance policies. Section 627.5045, F.S., provides that industrial life insurance policies issued on or after October 1, 1997, for which premiums are paid monthly, which have been in force for at least 1 year, and that cover or are owned by persons 64 years of age or older, may not be lapsed for nonpayment of premium unless, after expiration of the grace period (30 days) and at least 21 days before the effective date of such lapse, the insurer has mailed a notice of impending lapse in coverage to the policyowner and to a specified secondary addressee designated by the policyowner. Persons who apply for such policies must be notified by the insurer of the option to designate a secondary addressee at the time of application. However, this section also states, "This section does not apply to any life insurance contract under which premiums are payable monthly or more frequently and are regularly collected by a licensed agent." This provision effectively nullifies the statute because industrial life insurance is defined as that form of life insurance for which premiums are payable monthly or more often, bearing the words "industrial policy" or "weekly premium policy," and issued under a system of debit collection by an agent (s. 627.502, F.S.).

III. Effect of Proposed Changes:

Section 1. Creates s. 627.4553, Annual Notice. This section requires life insurers to annually mail notice to each Florida policyholder who has a life insurance policy with a death benefit of $15,000 or less, the following information: the total amount of premiums paid, the cash value, and the amount of the death benefits.

Section 2. Amends s. 627.4555, Secondary Notice. The current law provides that industrial life insurance policies issued on or after October 1, 1997, covering persons 64 years of age or older, may not be lapsed for nonpayment of premium unless the insurer has mailed a notice of impending lapse in coverage to the policyholder and to a specified secondary addressee designated by the policyholder. As explained in Present Situation, above, the current statute appears to be meaningless because it exempts all policies that meet the definition of an industrial life insurance policy. The bill limits this exemption to policies that are issued prior to July 1, 2001. Yet, even though this section of the bill would apply the secondary notice requirements to industrial life insurance policies issued after July 1, 2001, section 4 of the bill would prohibit industrial life insurance policies from being issued after July 1, 2001.

Section 3. Creates s. 627.4587, F.S., Benefit Enhancement. The bill would require life insurance policies issued after July 1, 2001, to increase the death benefit paid under the policy when the total premiums paid exceed a specified percentage of the death benefit. Specifically:

- When the premiums paid exceed 250 percent of the death benefit, the insurer must increase the death benefit by $0.50 for each premium dollar paid in excess of 250 percent of the death benefit.

- When the premiums paid exceed 500 percent of the death benefit, the insurer must increase the death benefit by $1.50 for each premium dollar paid in excess of the 500 percent of the death benefit.

The benefit enhancements of this section were included in the terms of the Regulatory Settlement Agreement entered into between the Department of Insurance and American General, discussed in Present Situation, above.

Section 4. Creates s. 627.5015, F.S., Industrial life insurance prohibited; disclosure. The bill prohibits new industrial life insurance policies from being issued in Florida on or after July 1, 2001. Each insurer that has an industrial life insurance policy in force in Florida would be required to provide annual disclosures to the policyholder or to the person who pays premiums on an industrial life policy, including: the total amount of premiums paid, the cash value of the policy, and the total amount of death benefits payable under the policy. If the insurer is unable to locate the policyholder, the policy must be converted to full paid-up status. The notice would not be required for polices that are in full paid-up status or converted to such status.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

Section 4 of the bill requires insurers to convert in-force industrial life insurance policies to full paid-up status if the insurer is unable to locate the policyholder to provide disclosures required by the bill. This provision may constitute an unconstitutional impairment of contracts in violation of Article I, section 10, of the Florida Constitution.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

The bill requires insurers to increase benefits of life insurance policies if premiums exceed specified percentages of the death benefit. This would financially benefit policyholders at the expense of life insurers. The specific benefit enhancements were included in the

Regulatory Settlement Agreement that the Department of Insurance reached with American General, described above. It is unknown how many new policies would be affected by such limits and to what extent insurers would either reduce premiums or limit availability for monthly debit ordinary policies as a result.

Life insurers would be subject to the expense of annually mailing notice of certain information to all policyholders who have policies with a death benefit of $15,000 or less. Such insurers would also be subject to the expense of converting policies to full paid-up status if the insurer is unable to locate the policyholder.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

Section 2 of the bill applies the secondary notice requirements of s. 627.4555, F.S., to industrial life insurance policies issued after July 1, 2001, but section 4 of the bill would prohibit industrial life insurance policies from being issued after July 1, 2001. However, section 2 would potentially have effect if the prohibition in section 4 is not enacted or later amended to allow for the sale of industrial life policies.

VII. Related Issues:

None.

VIII. Amendments:

None.