

December 20, 2011

Hon. Kamala D. Harris  
Attorney General  
1300 I Street, 17<sup>th</sup> Floor  
Sacramento, California 95814

Attention: Ms. Dawn McFarland  
Initiative Coordinator

Dear Attorney General Harris:

Pursuant to Elections Code Section 9005, we have reviewed a proposed statutory initiative related to health, home, and automobile insurance rates (A.G. File No. 11-0072).

## Background

***Insurance Regulation.*** Various types of insurance are sold in California, including health, home, and automobile. Existing state law imposes a variety of requirements on companies providing insurance coverage in California. For example, state law authorizes the Insurance Commissioner, who heads the California Department of Insurance (CDI), to regulate companies that offer home and automobile insurance, as well as certain types of health insurance (known as indemnity insurance) that provide coverage for hospital, medical, or surgical benefits. The Department of Managed Health Care (DMHC) is authorized to regulate companies that offer other types of health insurance coverage, such as health maintenance organizations. Under current law, insurers pay various fees (such as filing fees) to CDI and DMHC to cover the costs of regulation. The revenue from these fees are appropriated each year by the Legislature and are available for expenditure upon enactment of the annual state budget.

***Review of Certain Health Insurance Rates.*** Existing state law requires health insurers to file information on rates for all individual and small group (typically consisting of no more than 50 employees) policies with the appropriate regulatory department at least 60 days before those rates go into effect. State law also requires health insurers to file information on “unreasonable” rates (as defined by federal law) for large group insurance policies at least 60 days before those rates go into effect. Although the Insurance Commissioner and DMHC review such health insurance rates, they are not statutorily authorized to approve these rates before they take effect. Under current law, the state generally requires insurers to provide a minimum level of health care services, which is commonly referred to as a benefits package.

***Approval of Automobile Insurance Rates.*** In 1988, California voters approved Proposition 103, which requires the Insurance Commissioner to review and approve rate changes for automobile insurance before such changes take effect. The proposition also requires that the

rate changes not be excessive, inadequate, or unfairly discriminatory. In general, the Insurance Commissioner is required to hold public hearings on proposed rate changes whenever they exceed certain percentages. In addition, a consumer can request that a hearing be held on a particular rate change.

***Insurance Premium and Corporation Tax.*** Under current law, insurance companies doing business in California generally pay an insurance premium tax instead of the state corporate income tax. The tax is based on the amount of insurance premiums earned in the state each year. However, companies that offer certain types of health insurance products—specifically, those regulated by DMHC—are required to pay the corporation tax.

## **Proposal**

***Definition and Approval of Health Insurance Rates.*** For the purposes of CDI’s regulations, this measure broadens the definition of health insurance “rates” to include certain other factors beyond premiums, such as benefits, discounts, co-payments, and deductibles. The measure also changes the state’s process for regulating health insurance rates to be more aligned with the regulation of automobile insurance, as established by Proposition 103. Specifically, the measure requires the Insurance Commissioner to approve all health insurance rates for individual and small group policies before they take effect, including certain types of health insurance coverage currently regulated only by DMHC. The measure also authorizes the Insurance Commissioner to approve rates for large group policies if (1) the employer or collective bargaining group files a petition requiring such approval or (2) the proposed rate increase exceeds a certain percentage.

The measure does not explicitly repeal any of the statutory requirements for DMHC to review certain health insurance rates and benefits packages. As a result, it is possible that under this measure, both CDI and DMHC would conduct rate reviews of some of the same health insurance policies, with CDI having the sole authority to approve the proposed rates.

***Insurance Filing Fees.*** Under the measure, revenues from the filing fees paid by insurance companies would be continuously appropriated (meaning a legislative appropriation is not required) to cover any operational or administrative costs resulting from the provisions of this measure.

***Credit History.*** The measure also states that an individual’s credit history shall not be used for determining eligibility for a health, automobile, or homeowner’s insurance policy, or generally for rates, premiums, and insurability.

## **Fiscal Effects**

***Increased State Administrative Costs.*** This measure would result in additional costs for CDI to conduct health insurance rate reviews and hearings pursuant to the provisions of this measure. These additional administrative costs would likely be in the low tens of millions of dollars annually. Under the measure, these costs would be funded from the revenue collected by filing fees on the insurance industry.

***Potential Change in Revenues.*** This measure could change health insurance rates and therefore affect insurance premium tax revenues. For example, if rate regulation had the effect of

lowering insurance rates, then this would tend to lead to a reduction in those revenues. The amount of a change, if any, in taxes that health insurance companies pay is unknown and would depend on if this measure resulted in lower insurance rates.

### **Summary of Fiscal Effects**

We estimate that this measure would have the following major fiscal effect:

- Increased state administrative costs in the low tens of millions of dollars annually to regulate health insurance rates, funded with revenues collected from filing fees paid by health insurance companies.

Sincerely,

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Mac Taylor  
Legislative Analyst

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Ana J. Matosantos  
Director of Finance