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INSURANCE REGULATORY EXAMINERS SOCIETY

Regulating Health Insurance Rates

Ario: Feds Can Set Standards but States Must Enforce

by *Steve Tuckey*

Special to The Regulator

The federal government could play a useful role in the regulation of health insurance rates, just as long as it does not take over the whole show, said one veteran commissioner.

Pennsylvania Insurance Commissioner Joel Ario told *The Regulator* shortly after the Health Care Summit on Feb. 27 that “there should be a partnership between the state and federal governments in that the federal government could set strong rate review standards as long as the states have the final authority to implement and enforce them.”

Last month President Obama proposed setting up a Health Insurance Rate Authority in an attempt to restart stalled health care negotiations.



Joel Ario

The move came in response to outrage sparked by a proposed 39% rate increase proposed by Anthem Blue Cross in California.

The new federal authority would go beyond what was contained in either the House or Senate bill on the issue. States currently have varying degrees of authority over the regulation of health insurance rates with more than half allowing increases to go into effect without any prior approval, even those as large as Anthem’s. California falls into that category.

Ario said he would welcome additional authority provided under the guise of a federal mechanism to regulate rates in Pennsylvania. But he warned that states have to have the final authority so that all stakeholders in the process know where the buck finally stops.

Jane Cline, West Virginia Insurance Commissioner and president of the National Association of Insurance Commissioners, agreed that a federal-state partnership in which the states have the final say remains the best solution for keeping insurance premiums affordable.

“We understand that the final language will simply establish a federal backstop to assist those regulators who do not have full rate review authority under state law and ensure that the proposed rate increases are truly justified and receive a thorough review before they become effective,” she said.

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Permitted Practices Pose Problems for Insurance Consumers

by *J. Robert Hunter*

The major investment banks Bear Stearns and Lehman Brothers failed because of weak capital standards. When insurance giant AIG failed, the NAIC and individual state insurance regulators were quick to point out that, because of stronger capital and reserve requirements, AIG’s insurance units were financially sound.

Yet, state insurance regulators have been, over the past year, loosening some of the very standards that have helped keep insurance companies sound.

Some think that the life insurance industry narrowly missed a major meltdown a year ago and is not yet entirely out of the woods as potential mortgage issues remain to be dealt with. For example, Fitch Ratings, a global credit rating agency, now predicts \$15 billion in future real estate losses for the industry. In the face of such potential danger, American consumers need

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Defective Drywall Distresses Consumers, Insurers

by Steve Tuckey

Will purportedly dangerous Chinese drywall turn out to be the next mold-like issue threatening the stability of the homeowners' insurance market?

At this point that seems highly unlikely. But that has not stopped regulators and insurers from being concerned about the property damage and health hazards said to be stemming from drywall manufactured in China and whether the damage can be remediated in a cost-efficient and equitable manner.

Jack McDermott, director of communications for the Florida Office of Insurance Regulation, said that the term "defective drywall" is now being used since not all the material in question comes from China.

As for insurer liability, he said the standard homeowners' contract does not cover the risk of defective building materials, including defective drywall, as insurers do not incorporate that risk into their underwriting and rates.

McDermott said that one potential solution could be to create a fund similar to one for asbestos removal. "Ideally, builders, contractors and suppliers and the federal government could contribute to this fund and affected consumers could make claims against this fund in exchange for waiving their legal claims," he said.

Overall, McDermott termed the issue "very dynamic and involves pending litigation and legislative proposals at the state and federal levels."

Following a hearing at its December annual meeting last year, the National Association of Insurance Commissioners is expected to offer some interim conclusions. But they are not anticipated to be made public before the spring session at the end of this month.

David Golden, senior vice president for the Chicago area-based Property Casualty Insurers Association of America (PCI), termed the entire issue as "developing."

"We still don't know what the actual process is that is causing the sulfurous emissions that have been correlated with the drywall coming out of China," Golden said.

But he did hold out hope that evolving science around the issue could come up with a solution for remediating the problems caused by the drywall short of tearing it all out, while agreeing that would not settle the question of who should pay for it.

As of January 25, the U.S. Consumer Product Safety

Commission reported 2,833 incidents related to drywall from 37 states with more than 90% coming from five states: Florida (59%), Louisiana (21%), Mississippi (6%), Alabama (5%) and Virginia (4%).

The Commission said that it was working closely with the Lawrence Berkeley National Laboratory to analyze draft emissions testing data "that will

likely confirm our hypothesis that there are elevated emission rates for hydrogen sulfide from some Chinese drywall compared to non-Chinese drywall given the type of corrosion that we have seen in the homes we have visited."

As for the question of insurer liability, Florida's Citizens Property Insurance Corp. said that it would continue covering James and Maria Ivory, a retired couple whose Gulf Coast home was built with problem materials that emitted sulfuric fumes that corroded pipes.

Citizens at first not only denied the claim made in October of last year but announced it would not renew the policy because of the defective drywall that could lead to other losses. But according to Citizens spokesman John Kuczanski, further inspection revealed that the damage was not as extensive as previously thought and coverage would be renewed.

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California-based insurance attorney Charles Miller suggested that the regulators may consider joining in a multi-state market conduct exam to ensure proper investigations of Chinese drywall claims and complaints are being conducted.

Covered or Not?

The question then becomes whether the loss that resulted from the defective drywall is covered or not. In the case of the Ivory home, corrosion damage to the heating and plumbing systems was not, but there are perils that could be covered.

But that still raises the issue of homeowners who file Chinese drywall claims and not only see those claims denied, but their coverage nonrenewed as a result. The Associated Press reported two other insurers in Florida cancelled policies after Chinese drywall claims.

Late last year, Louisiana Insurance Commissioner James Donelon said his state's laws protect policyholders who have been covered for more than three years from any cancellation or premium-hike threat as a result of reporting Chinese drywall problems.

Golden said homeowner policies are not warranty products and therefore would not cover any replacement of defective drywall. But any final determination of a claim would of course depend on the results of that particular claim investigation, he added.

The current problem stems for the most part from drywall imported from China between 2005 and 2007 when the combination of a housing boom and the back-to-back 2004-2005 catastrophe seasons created a shortage of materials.

At the December NAIC hearing, speakers agreed the issue was complicated and evolving as attempts are being made to determine both the cause of the drywall defects, and the nature of the illnesses they are said to cause.

The NAIC's Regulatory Division Director Eric Nordman said there was a bill introduced in Congress that would prevent insurers from cancelling or not renewing homeowners' policies due to the presence of certain types of drywall in the home. In addition, the bill would authorize the homeowner to bring a private

cause of action against the insurer if the homeowner's policy was cancelled.

Nordman described what he termed "heartbreaking" stories about people forced out of their homes because of health conditions. "In many cases people abandoned their homes and have gone to stay in other places," he said.

Also at the hearing, PCI representative David Kodama said despite the fact that Citizens rescinded its nonrenewal action, "our entire industry's public reputation suffered in the resulting media news

coverage." But private insurers will nonetheless continue to operate under the terms of their policy contracts and state-regulated insurance practices, he added.

California-based insurance attorney Charles Miller suggested that the regulators may consider joining in a multi-state market conduct exam to ensure proper

investigations of Chinese drywall claims and complaints are being conducted. Examiners could include insurance consumer representatives. "This in my view would tend to add greater assurance to the general public that their interests are being covered in the examination process," he said.

In addition, he suggested that regulators develop model guidance for the insurance industry so carriers can understand how commissioners expect the applicable insurance provisions to be interpreted and applied. ■

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identify vulnerabilities, create a plan to address them and reduce the risks.

In order to ensure continuity of business, proactive security measures must be taken and be a part of daily operations. Routine security testing and regularly scheduled assessments and third-party security audits should be performed.

A business should work with its insurer to create a plan for continuity in the event operations are disrupted. Relevant questions to consider are:

- Does the business have an emergency response plan?
- Does the business have employee and vendor lists?
- Has the business identified sources of business disruptions?

- Does the business have plans to restore critical systems?

The Bottom Line

In today's litigious world, protecting customers, employees and others from identity theft is not just a matter of public relations; it goes directly to the bottom line. Lost or stolen data can generate embarrassing media attention and legal complications. In addition, the costs of notifying affected individuals and helping them restore their identities can be huge. We encourage businesses and regulators to learn more about these important coverages. ■

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Cline added that the proposed new federal authority would not be used to overturn state determinations. Cline also reiterated her opposition to any bill in which the federal government allows insurance carriers to sell their products in states using regulatory rules of another state.

“This misguided proposal would increase premiums for those who need insurance the most and eliminate important consumer protections,” she said. “It would also fragment the insurance market and expose consumers to increased fraud and abuse.”

The proposal has gained traction in the past few weeks as one measure that both Democrats and Republicans seemed to agree on, although varying interpretations of how it would be implemented and what it would mean to consumers indicate that passage of such a measure would prove challenging.

At the beginning of the year, the Democrats seemed headed toward passage of an overall bill that would bring 30 million new customers into the system in exchange for certain cost control measures and the elimination of pre-existing conditions exclusions.

But that consensus seemed to disintegrate with the unexpected election of Republican Scott Brown to the U.S. Senate from Massachusetts that not only deprived the Democrats of their filibuster-proof supermajority but also suggested a general national reluctance to move ahead with radically changing the health care system in the country.

Ario said that reforming the entire fee-for-service concept to one in which all services are paid for under what he termed a global payment system will be a key cost control measure, along with the introduction of a stronger evidence-based system of authorizing health care procedures.

Such measures cannot work, however, without including millions of new payers in a system that would require new subsidies and the taxes and fees to fund them. ■

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