Fiscal Note & Local Impact Statement

122 nd General Assembly of Ohio

BILL: **Am. Sub. S.B. 67** DATE: **May 21, 1997**

STATUS: **As Reported by House Insurance** SPONSOR: **Sen. Gillmor**

LOCAL IMPACT STATEMENT REQUIRED: **Yes**

CONTENTS: **To define health insuring corporations and establish law governing their operations**

State Fiscal Highlights

STATE FUND	FY 1997	FY 1998	FUTURE YEARS
General Revenue Fund			
Revenues	- 0 -	Indeterminate effect	Indeterminate effect
Expenditures	- 0 -	- 0 -	- 0 -
State Special Revenue Fund – Insurance Operating Fund (554)			
Revenues	- 0 -	$42,000 to $97,000	$42,000 to $97,000
Expenditures	- 0 -	Not exceeding revenues	Not exceeding revenues

- The bill increases document filing fees for all Health Insuring Corporations, which are defined in the bill. The bill also brings some currently unregulated, managed care entities under the regulatory authority of the Department of Insurance (INS). The Department of Insurance Operating Fund, Fund 554, will receive the additional revenue from these actions, estimated to be between approximately $42,000 and $97,000 annually.

- INS's regulatory workload will be increased by the requirements of this bill. The department believes that it can absorb any additional costs, including staff costs, should additional staff be necessary. Revenue generated by the bill would permit the agency to hire new staff, according to LBO's projections. This issue is discussed further in the "Fiscal Effects on the Department of Insurance" section of this fiscal note.

- Costs incurred by INS related to market conduct examinations and audits performed to verify the behavior and solvency of the Health Insuring Corporations (HICs) regulated by the bill would be billable to those HICs.

- Changes in the tax status of entities regulated by this bill would likely affect the revenues received by the GRF and, in turn, the amounts received by the LGFs.

- Violations of the bill's provisions regarding the use of genetic testing information could generate costs for both INS and the Attorney General's office. Such violations permit the Superintendent of Insurance to use the powers ascribed to him by the Unfair and Deceptive Trade Practices Act. These powers are rarely used by the current Superintendent so the fiscal effect is likely to be minimal.

Local Fiscal Highlights

LOCAL GOVERNMENT	FY 1997	FY 1998	FUTURE YEARS
Counties			
Revenues	- 0 -	Indeterminate effect	Indeterminate effect
Expenditures	- 0 -	Potential minimal increase	Potential minimal increase

- The bill requires all political subdivisions to purchase insurance for employees from regulated Health Insuring Corporations, if they plan to provide employee insurance benefits. This provision may increase the cost of providing employee health benefits, in some cases, but does not mandate the provision of these benefits.

- Changes in the tax status of entities regulated by this bill would likely affect the revenues received by the GRF and, in turn, the amounts received by the LGFs.

- Violations of state law regarding the use of information from genetic testing would permit aggrieved parties to sue in common pleas courts, potentially increasing court costs for affected counties. The Superintendent of Insurance may also pursue violators of the bill's provisions in the Franklin County Common Pleas Court, which may have a financial impact on this court.

Detailed Fiscal Analysis

The bill would expand the regulatory authority of the Department of Insurance (INS) to include all managed care organizations which guarantee the provision of health care services, including those organizations that are not currently regulated. Some "Provider Networks" and any other new entities which assume the financial risk associated with guaranteeing coverage of health benefits whether in existence today, or created in the future, are examples of the entities which would be regulated under the requirements of the bill. Entities that are currently regulated, such as health maintenance organizations and preferred provider organizations, would remain within INS's regulatory purview and be regulated under the new ORC chapter 1751 proposed by the bill.

Current Ohio law specifically names the types of organizations under INS's regulatory authority: prepaid dental plans; health maintenance organizations; preferred provider organizations; and, health care corporations. This bill would delete those current definitions and state that any organization providing, or guaranteeing payment for, the health care services described by the bill would be subject to the regulations of INS. Any entity providing any of these services would be called a *Health Insuring Corporation (HIC)*. The requirements of this bill do not change the laws or rules INS uses to regulate accident and sickness insurers.

Fiscal Effects on the Department of Insurance

Because of the additional revenue INS will receive due to the expansion provisions of the bill, the agency expects to be able to pay for any additional costs incurred while enforcing the bill's requirements. INS will receive additional revenue from fees paid by newly regulated HICs when they file documents with INS, and from the Continuing Education fees that agents of the newly regulated HICs must pay to be licensed to market HIC services in Ohio. Additionally, new fees will be generated from currently regulated managed care entities because this bill increases the filing fee amounts. Lastly, the Superintendent of Insurance can charge HICs for INS's costs from market conduct examinations, audits, and "disciplinary" actions. (Such charges are currently allowed under HMO law and would be allowed for all HICs by this bill.)

Potential Cost Increases

While the regulatory requirements of the bill would increase INS's workload, the department believes it can absorb the additional workload, especially since the bill will generate increased revenues for the agency. When LBO questioned an INS representative about the potential need to hire staff to perform the requirements of the bill, the response was that INS did not foresee the need to increase staff, at this time.

Additional staff may be necessary in the future depending on the number of HICs INS must regulate in the future. LBO cannot estimate the number of new hires necessary, however, LBO's projected revenue increases would permit INS to hire up to two new employees — Investigators and Contract Analysts being the two positions most likely to require additional personnel.

In 1994, salary and benefits for an Investigator totaled $35,200, and $42,200 for a Contract Analyst. Staff costs for one investigator and one contract analyst would be approximately $77,400, somewhat less than LBO's total revenue estimate of $96,688.

In addition to filing fees, the bill also authorizes INS to bill any HIC for the cost of "market conduct" examinations and audits the department must perform to verify the behavior and solvency of the HICs. This provision is currently in HMO statute and is being moved to the proposed HIC chapter of the Revised Code. INS believes that these fees, in conjunction with the filing fees, will allow them to absorb the additional costs associated with regulating additional entities as required by this bill.

Potential Revenue Increases from Filing Fees

The following three tables show the anticipated additional revenue from filing fees under the provisions of the bill. The first looks only at the additional revenues generated by licensing new HICs that come under INS regulation for the first time. (Note that three estimates of the number of newly regulated HICs are presented in order to illustrate a range of revenues: 10, 25, and 40.) The second addresses the total filing fee revenue from regulating HICs, the 43 currently regulated plus those which would become newly regulated. The third table looks only at the effect of increasing the various filing fees, comparing the revenues generated by the total number of HICs with and without fee increases.

Table 1

Estimate of Filing Fee Revenue from Newly Regulated HICs
depending on the number of New HICs INS must regulate (estimates here are 10, 25, or 40)

Description of Fee [1]	**Fee Amount** [2]	**10 New HICs**	**25 New HICs**	**40 New HICs**
Certificate of Authority	$1,500	$15,000	$37,500	$60,000
Service Area Expansion	$300	$1,500	$3,750	$6,000
Major Modification	$300	$3,000	$7,500	$12,000
Annual Report, per report	$25	$250	$625	$1,000
All Other Filings	$50	$1,500	$3,750	$6,000
TOTALS [3]	**not applicable**	**$21,250**	**$53,125**	**$85,000**

[1] These are document filing fees which the HICs must file with the Superintendent of Insurance in order to operate, or change their coverage, service areas, or premiums. The bill proposes the fees specified above in column 2, "Fee Amount," to cover the cost of analyzing and processing the actions proposed in these documents. INS has been charging filing fees for the last four years, approximately. The fee amounts, however, are raised by this bill, and one new fee is created.

[2] The fees shown in this column are proposed by the bill and are higher than current fees.

Current fees are
Certificate of Authority: $250
Service Area Expansion: $25
Major Modification: $25
Annual Report: $25
The "All Other Filings" fee is a new fee.

[3] **The dollar figures above are based on the following assumptions:** A) the Certificate of Authority fee is a one-time only fee; B) the new HICs will file an average of one-half of one Service Area Expansion and one Annual Report per year; C) one Major Modification filings per new HIC per year, on average; and, D) "All Other Filings" will total three per new HIC annually, on average.

Table 2

Estimate of Total Filing Fee Revenue
(based on estimated total number of HICs to be regulated 53, 68, 83)

Description of Fee [1]	Fee Amount [2]	53 Total HICs	68 Total HICs	83 Total HICs
Certificate of Authority [4]	$1,500	$15,000	$37,500	$60,000
Service Area Expansion	$300	$7,950	$10,200	$12,450
Major Modification	$300	$15,900	$20,400	$24,900
Annual Report, per report	$25	$1,325	$1,700	$2,075
All Other Filings	$50	$7,950	$10,200	$12,450
TOTALS [3]	**not applicable**	**$48,125**	**$80,000**	**$111,875**

[1] These are document filing fees which the HICs must file with the Superintendent of Insurance in order to operate, or change their coverage, service areas, or premiums. The bill proposes the fees specified above in column 2, "Fee Amount," to cover the cost of analyzing and processing the actions proposed in these documents. INS has been charging filing fees for the last four years, approximately. The fee amounts, however, are raised by this bill, and one new fee is created.

[2] The fees shown in this column are proposed by the bill and are higher than current fees.

Current fees are
Certificate of Authority: $250
Service Area Expansion: $25
Major Modification: $25
Annual Report: $25
The "All Other Filings" fee is a new fee.

[3] **The dollar figures above are based on the following assumptions:** A) the Certificate of Authority fee is a one-time only fee; B) the new HICs will file an average of one-half of one Service Area Expansion and one Annual Report per year; C) one Major Modification filings per new HIC per year, on average; and, D) "All Other Filings" will total three per new HIC annually, on average.

[4] Certificate of Authority (COA) fees will not be refiled by currently regulated entities such as HMOs. For this reason the revenue estimate for COA fees is based on the estimated number of HICs (53, 68, or 83), which includes the 43 HMOs that will have their current Certificate of Authority grandfathered by this bill. The estimated number of new COAs is estimated to be 10, 25, and 40 in the table above.

Table 3

Estimate of Additional Filing Fee Revenue
(Due to fee increases)

If the Number of HICs to be regulated is 53 ...				
Description of Fee [1]	**New Fee**	**Old Fee**	**Difference**	**New Revenue [2]**
Certificate of Authority [3]	$1,500	$250	$1,250	$12,500
Service Area Expansion	$300	$25	$275	$7,288
Major Modification	$300	$25	$275	$14,575
Annual Report, per report	$25	$25	$0	$0
All other Filings	$50	$0	$50	$7,950
TOTAL				$42,313

If the Number of HICs to be regulated is 68 ...				
Description of Fee [1]	**New Fee**	**Old Fee**	**Difference**	**New Revenue [2]**
Certificate of Authority [3]	$1,500	$250	$1,250	$31,250
Service Area Expansion	$300	$25	$275	$9,350
Major Modification	$300	$25	$275	$18,700
Annual Report, per report	$25	$25	$0	$0
All other Filings	$50	$0	$50	$10,200
TOTAL				$69,500

If the Number of HICs to be regulated is 83 ...				
Description of Fee [1]	**New Fee**	**Old Fee**	**Difference**	**New Revenue [2]**
Certificate of Authority [3]	$1,500	$250	$1,250	$50,000
Service Area Expansion	$300	$25	$275	$11,413
Major Modification	$300	$25	$275	$22,825
Annual Report, per report	$25	$25	$0	$0
All other Filings	$50	$0	$50	$12,450
TOTAL				$96,688

[1] These are document filing fees which the HICs must file with the Superintendent of Insurance in order to operate, or change their coverage, service areas, or premiums. The bill proposes the fees specified above in column 2, "Fee Amount," to cover the cost of analyzing and processing the actions proposed in these documents. INS has charged filing fees for the last four years, approximately. The fee amounts, however, are raised by this bill, and one new fee is created. LBO has estimated three different numbers of HICs: 53, 68, and 83 in the 3 tables above.

[2] **The dollar figures above are based on the following assumptions:** A) the Certificate of Authority fee is a one-time only fee; B) the new HICs will file an average of one-half of one Service Area Expansion and one Annual Report per year; C) one Major Modification filings per new HIC per year, on average; and, D) "All Other Filings" will total three per new HIC annually, on average.

[3] Certificate of Authority (COA) fees will not be refiled by currently regulated entities such as HMOs. For this reason the revenue estimate for COA fees is based on the estimated number of HICs (53, 68, or

83), which includes the 43 HMOs that will have their current Certificate of Authority grandfathered by this bill. The estimated number of new COAs is estimated to be 10, 25, and 40 as in the prior tables.

Effects on Health Care Premiums Paid by Public Employers

The effect of this bill on the health care premiums paid by public employers depends entirely upon whether the employer currently contracts with entities that are regulated by INS under existing law. The state contracts with health maintenance organizations, preferred provider organizations, and one insurer. Since these contractors are currently regulated by INS, the state should see very little change in its premium costs due to the requirements of this bill. However, state universities and colleges, and local governments may see changes in their employee health benefit costs depending on how they now provide employee benefits.

Any state college or university, or local government contracting with a currently unregulated entity, which becomes a regulated entity under the terms of the bill, **may** see their premiums rise. These entities, such as risk-bearing Provider Networks, may increase premiums to recoup the costs associated with meeting regulations, potentially for the first time in their history. (*It should be noted, however, that not all Provider Networks (PNs) will be considered HICs*. Some Provider Networks do not accept the financial risk associated with guaranteeing coverage of health service costs. These PNs which do not accept risk are usually formed by or operate in conjunction with insurers or HMOs which maintain the ultimate burden of paying for all covered, health services provided to members. These PNs, which are called "intermediary organizations" by this bill, are not subject to the bill's requirements.)

The number of state colleges and universities or local governments which may be affected due to this bill's effect on their contractors cannot be estimated. A recent survey of political subdivisions by the State Employment Relations Board (SERB) showed that nearly half of survey respondents contract with Provider Networks to provide some or all of their employee benefits. The survey was not designed to gather data showing whether or not these Provider Networks are risk-bearing or merely intermediary organizations, thus there is no reliable way to estimate how many local governments may see premium changes based on the provisions of this bill, although potentially it could be as many as half of them. The impact on these subdivisions could be above the local impact thresholds of: (a) $1,000 per affected village or township with a population of less than 5,000 people, or a school district with an average daily membership of less than 1,000 students; or (b) $5,000 for counties, municipal corporations, or townships with 5,000 or more residents, or a school district with an average daily membership of 1,000 or more.

Tax Implications

Those entities that are not currently regulated by INS, but would be regulated as HICs under the bill, fall into one of two categories — those that are currently subject to the corporate tax and those that escape taxation. LBO has no way of knowing how many of the newly regulated entities currently pay corporate taxes. The analysis of the tax impact of the bill is further complicated by the current proposal in H.B. 215 (the FY 1998-99 budget bill) to change the insurance tax. Both the current scenario and the H.B. 215 scenario will be discussed below in regard to those entities currently paying corporate taxes. For those entities that are not currently subject to the corporate tax, however, the effect is clear — the regulation would result in an increase in taxes paid to the GRF (through the domestic insurance tax), no matter whether the current scenario or the H.B. 215 scenario is in place.

Current Law and Newly-Regulated Entities Currently Paying Corporate Taxes

Those entities that are currently subject to the corporate tax but would become, under the bill, HICs that are regulated by INS and subject to the domestic insurance tax, would likely pay the same amount or less in taxes to the GRF. The following example will best illustrate the reasoning behind this claim. Although the fictional corporation in the example in no way should be construed to serve as a proxy for a median corporation — it is merely one of many examples that can be used to demonstrate a variety of results — it produces the outcome that is cited most frequently in discussions surrounding this tax issue. Most importantly, the example demonstrates the mechanics of the two taxes.

The fictional entity in this example has a net worth of $3.0 million, and a net income of $250,000. Under Title 57, a corporation must pay the higher of a 5.82 mill tax on net worth or a tax on net income. In this example, the net worth tax would be $17,640 and the net income tax would be $20,350, so the net income tax would be paid.

Under current law, the domestic insurance tax is the lower of 2.5 percent of premiums or 0.6 percent of the sum of capital and surplus (cap & surplus). Because cap & surplus is frequently close to net worth (we are told), we use $3.0 million as our fictional entity's cap & surplus amount. This amount would result in an $18,000 tax. If we assume the entity receives $12.5 million in premiums, a $312,500 premium tax results. Because the domestic insurance tax allows the lower tax to be paid, the cap & surplus tax of $18,000 would be paid.

Thus, the regulation of the entity by INS, in this example, would result in a net loss of $2,350 in state taxes (a loss of $20,350 in corporate taxes and a gain of $18,000 in domestic insurance taxes). The loss to the GRF would be smaller, at $1,375, since the GRF gets 95.2 percent of corporate taxes, and the LGFs get the other 4.8 percent. Therefore, LGFs would lose $975 in our example.

H.B. 215 and Newly-Regulated Entities Currently Paying Corporate Taxes

The proposal included in H.B. 215 provides that a five-year transition period to a straight 1.5 percent premium tax would result in the payment of a "blended" tax, based partly on the old capital and surplus method and partly on the proposed new 1.5 percent of gross premiums method. No matter what blending rate is used, the most likely result is a long-run increase in tax revenue, especially following full implementation of the straight 1.5 percent premium tax.

Penalties for Genetic Testing Violations

In accordance with the Unfair and Deceptive Trade Practices Act (ORC 3901.19-3901.26), the bill permits INS to collect penalty fees when HICs fail to follow the bill's genetic testing requirements. These fees range from $1,000 to $10,000 per incident and would be payable to Fund 554 of the SSR (INS's operating fund) to pay operating costs of the Department of Insurance. The Superintendent may also impose an administrative penalty up to $100,000 for gross violations instead of revoking the HIC's certificate of authority to operate in the state.

Furthermore, the Superintendent may issue a cease and desist order against an insurer. If such an order were to be ignored, the Superintendent may request the Attorney General to begin a class action suit or other action on behalf of policyholders.

Additionally, the Franklin County Common Pleas Court may impose a civil penalty up to $100,000 for violations of the bill's provisions, plus INS's costs in pursuing the violator in the courts. Again this penalty would be credited to the INS operating rotary fund (Fund 554 of the SSR). Costs of such judicial actions would be paid by the county.

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