F I S C A L   I M P A C T   R E P O R T

ORIGINAL DATE 2-2-2006
SPONSOR Stewart **LAST UPDATED** ______ **HB** 681

SHORT TITLE Interstate Insurance Product Regulation **SB** ______

ANALYST Dearing

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY06	FY07		
	NFI*		

(Parenthesis ( ) Indicate Expenditure Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Public Regulation Commission (PRC)
Attorney General's Office (AOC)

SUMMARY

Synopsis of Bill

House Bill 681 appears to be identical to SB 310. Enactment of this bill would result in New Mexico joining the Interstate Insurance Product Regulation Compact.

The Compact, prepared and approved by the National Association of Insurance Commissioners, creates a joint public agency known as the Interstate Insurance Product Regulation Commission. Under the compact, the commission is empowered to *pre-empt* New Mexico insurance law to develop uniform standards for certain insurance products and to approve product filings under these standards. Insurance products covered by the compact are individual and group annuities, life insurance, disability income and long-term care insurance. The compact does not cover other types of health or property and casualty insurance. The stated intent of the NAIC in developing this Compact is to secure a more uniform and efficient regulatory process and to discourage federal pre-emptive legislation.

The chief insurance regulatory officer of each participating state is a member of the Commission. The Commission is empowered to begin operation only after the compact has been enacted by a majority of the states or states representing forty percent of the total premium volume for the covered product lines.

A state that joins the compact can reject a specific uniform standard adopted by the Commission by legislation or by a specific administrative ruling.

If enacted, New Mexico would concede jurisdiction to a multi-state organization where New Mexico would have only a single vote. While the bill permits a state to withdraw from the compact, sovereignty once given up is difficult to re-acquire, and must occur through a legislative enactment to revert to status quo.

FISCAL IMPLICATIONS

According to the Public Regulation Commission, participation in the Compact has no fiscal impact on the participating states. The Compact is financed by filing fees paid by insures with funding from the National Association of Insurance Commissioners (NAIC). House Bill 681 would be revenue neutral. Existing statutory fees associated with forms and rate filings in the New Mexico Insurance Code would be collected by the *Interstate Compact Commission* and remitted to the State of New Mexico.

SIGNIFICANT ISSUES

If enacted, New Mexico would cede jurisdiction to a multi-state organization where New Mexico would have only a single vote. While the bill permits a state to withdraw from the compact, sovereignty once given up is difficult to re-acquire, and must occur through a legislative enactment to revert to status quo.

In order to opt out of an individual uniform product standard, states are allowed one of two options. Individual compact uniform standard would require item-specific legislation in order for New Mexico to opt-out. Or, the insurance regulator would need to promulgate findings of fact and conclusions of law through New Mexico's administrative procedures act to determine that the uniform standards does not provide reasonable protection to citizens.

It should be noted that the NAIC states that the compact *must be enacted in its un-amended state,* in order to be a participant of the compact.

PERFORMANCE IMPLICATIONS

House Bill 681 would relieve the Superintendent of the some day-to-day review and processing of form and rate filing review, approval and fee collection to a certain extent. Companies will retain the choice of filing products through the compact for directly with the Insurance Division. Insurance Division staff resources currently performing these functions may be reassigned and trained for other areas within the Insurance Division. The Superintendent would also be relieve of certain rule-making authority that would be assumed by the *Interstate Compact Commission*, although New Mexico could opt-out of a proposed uniform standard if it does not provide reasonable protection for the citizens of New Mexico.

ADMINISTRATIVE IMPLICATIONS

According to the terms of the compact, the Insurance Division would designate one voting member to represent New Mexico in the Compact and may serve on a management and legislative committees. This individual, most likely the Insurance Division's Chief Life & Health Actuary would attend meetings. The Superintendent would continue to perform form & rate review and fee collections for products filed directly by insurance companies.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Duplicates SB 310

Conflict, duplication, companionship or relationship between rules promulgated pursuant to the Insurance Code and rules promulgated by the *Interstate Compact Commission* would be duplicative. However, the implication would be dependent upon the number of insurance companies utilizing the filing system of the Compact versus filing directly with the New Mexico Insurance Division for the life, annuity, disability and long-term care products.

OTHER SUBSTANTIVE ISSUES

The National Conference on State Legislatures recommends this proposal. Frequently asked questions are compiled in an appendix at the end of this document provided through the NCSL's fact sheet on this initiative.

Proponents would argue that this legislation would prevent federal pre-emption by offering a state-based solution that provides uniformity, speed-to-market and single-point filing, however, these marketing issues impacting the insurance industry, with the exception of uniformity, must be weighed against the concession of New Mexico's sovereignty within this area.

Opponents would argue that it diminishes the local "hands-on" authority of the Superintendent to regulate the life, annuity, disability and long-term care markets in New Mexico.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

The consequences of not enacting this legislation is that those applicable policies and products would be filed and regulated as they are currently, directly through the New Mexico Insurance Division.

PD/yr

Appendix 1

Responses to Frequently Asked Questions, as provided by the National Conference of State Legislatures,

Frequently Asked Questions (FAQ) on the
Interstate Insurance Product Regulation Compact

In an attempt to preserve sovereign state regulation of the nation's insurance industry, in July 2003, the Executive Committee of the National Conference of State Legislatures (NCSL) unanimously endorsed the Interstate Insurance Product Regulation Compact. The following FAQ offers answers to frequently asked questions about the Compact—it purpose, its structure, how it will work, and its implications for the future of state insurance regulation.

WHAT IS THE "INTERSTATE INSURANCE PRODUCT REGULATION COMPACT"?
If enacted, the Compact would be a multi-state agreement to create a streamlined system of product regulation. The new system would allow insurers to market certain types of insurance products more quickly on a national basis and to reduce the number of variations of the same product that a company must produce to meet state specific requirements. The Compact would create a national multi-state public authority to receive, review and quickly make regulatory decisions on insurance product filings according to national uniform standards that the member states would create.

WHAT TYPE OF INSURANCE POLICIES WOULD THE COMPACT COVER?
The Compact would cover individual and group products for life insurance, annuities, disability income and long-term care insurance. These products—also called "asset-based" insurance—are long-term, investment-oriented insurance policies that compete directly with other retirement and estate-planning instruments that are sold by banks and securities firms. The Compact would not include property and casualty insurance or health insurance.

WHAT ARE INTERSTATE COMPACTS?
Interstates compacts are contracts between states that allows them to cooperate on multi-state or national issues while retaining local control. Interstate compacts are mentioned specifically in the U.S. Constitution. Although they historically have been used to address border disputes and water rights, the use of interstate compacts has expanded significantly in recent decades to cover tax issues, drivers' licensing and vehicle registration, environmental issues, emergency management and other issues. Over 200 interstate compacts currently exist, and every state belongs to at least 14 compacts.

WHAT'S THE REASON FOR THE INSURANCE COMPACT?
The Compact promises to preserve the state system of insurance regulation against federal encroachment while raising insurance product standards, improving the quality of product review, and giving companies the regulatory efficiency that they need to compete in the modern marketplace. Insurance is now part of the integrated financial marketplace, and states are under increased pressure from Congress and others to develop a streamlined and simplified national system of product regulation that would allow insurers to market their products nationally more quickly and efficiently. The Compact would achieve this. At the same time, it would benefit consumers by Frequently Asked Questions on the Interstate Insurance Compact 2 promoting higher product standards and facilitating the development of new products that meet consumer needs.

The Compact also would allow states to pool their collective expertise to better review products and to make more valuable use of resources.

HOW ARE THESE PRODUCTS REGULATED NOW?
Currently, insurance companies must seek individual state approval for all product filings, which creates a complicated and timely process for insurers to bring a new product to the market. Where banks can introduce an innovative product like a CD or money-market account in 30 days, and the Securities and Exchange Commission might take 60 days to approve a new securities product, like a mutual fund, receiving approval for a new life insurance or annuity product in all 50 states can take up to two years. Moreover, a company may require 30 or 40 versions of the same product to satisfy a wide-range of state-specific requirements. Driven by evermore demanding market forces, products have become increasingly sophisticated and their shelf life has reduced from 7 to 8 years to 2 to 3 years. These factors have increased the workload for the approximately 200 regulators—about 2 percent of the nation's total—who are charged with reviewing and making regulatory decisions on asset-based insurance products. By pooling state resources and expertise, the Compact promises to increase the quality and efficiency of product review.

WHY NOT JUST LET THE FEDS DO IT?
States have successfully and effectively regulated the business of insurance for over 150 years. Although federal government could create a new bureaucracy in Washington, D.C. to serve this function—and the industry and some in Congress advocate this—governors, state legislatures and insurance commissioners have long maintained that this would be bad for the states and worse for consumers. Why? First, insurance is a different kind of financial service. Where banking and securities are about access to capital and taking risks, insurance is about guarantees—promising to pay benefits if and when certain things happens, no matter what. As a result, insurance requires regulation that is accountable, accessible and responsive—traits more often associated with state government than federal bureaucracies. Second, state insurance regulation allows state legislatures to set policies that effectively serve the economic needs and social values of local markets. In doing so, states also serve the national economy more effectively than one-size-fits-all federal regulation. Finally, state insurance regulation ensures $12 billion dollars a year in state insurance revenues, which federal regulation could diminish or preempt. Of the $12.5 billion, 8 percent supports the cost of insurance regulation while the remaining 92 percent—over $11 billion—goes to state general funds to pay for other priorities.

DOES THE COMPACT REQUIRE CONGRESSIONAL APPROVAL?
No. The U.S. Constitution says, "No State shall, without the consent of Congress, enter into any Agreement or Compact with another State." However, the Supreme Court ruled in the 1893 case Virginia v. Tennessee that congressional consent was mandatory only for a compact tending to increase the political power and influence of the party states and to encroach upon federal authority. Because the Compact would perform a function that currently is reserved to the states, it does not require the consent of Congress.

HOW WOULD THE COMPACT BE GOVERNED?
The Compact would be governed by a multi-state Commission, which will include one member from each member state. A Management Committee of 14 members would oversee the day to day activities of the Compact. The Management Committee would include one member from each of the six largest states, four members from mid-sized states, and four members from smaller states by region. Rules and operating procedures would be made through a process that

conforms to the Model State Administrative Procedures Act.

HOW WOULD UNIFORM PRODUCT STANDARDS BE DEVELOPED?
The Management Committee would create uniform product standards through the rulemaking process. The Compact would require uniform standards to receive the approval of two-thirds of the Management Committee and two-thirds majority of the Commission to be adopted. A standard would be effective 90 days after promulgated or at a later date as determined by the Commission.

WHAT GUIDELINES FOR PRODUCT STANDARDS WOULD THE COMPACT HAVE TO FOLLOW?
The Compact agreement requires that uniform product standards prohibit the use any inconsistent, misleading or ambiguous provisions in a product. It also requires that the form of products made available to the public shall not be unfair, inequitable or against public policy as determined by the Commission.

COULD A STATE OPT-OUT OF PRODUCT STANDARDS AFTER IT JOINS THE COMPACT?
Yes. States can opt-out of uniform product standards in two ways. First, it may enact legislation opting out of any uniform standard at any time. Second, it may opt-out by regulation following the promulgation of a uniform standard if meets certain conditions.

HOW DO STATE LEGISLATURES PARTICIPATE IN THE COMPACT?
A state legislature must enact the compact model act through legislation without amendments in order to join the Compact. A state legislature also must designate the position or appointment process and conditions regarding who would represent the state on the Commission. Relevant state legislative committees would receive written notice of a uniform standard before it could be adopted by the Commission. The Compact also establishes a legislative committee of state legislators or their designees to monitor the operations of the Commission and make recommendations to the Commission. State legislatures would be able to opt-out of a uniform standard for any product line at any time through legislation. The Commission would be required to make an annual report, which shall include the findings of an independent audit, to the legislature and governor of each member state.

HOW DOES A STATE OPT-OUT OF A UNIFORM STANDARD BY REGULATION?
A state may opt-out of a uniform standard by regulation that is duly promulgated by the insurance department under the state's administrative procedures act. To opt-out by regulation, an insurance commissioner, first, must give written notice of his or her intent to opt out no later than 10 days after a rule is promulgated or at the time the state joins the Compact. Second, the commissioner must reach a finding that the uniform standard does not provide reasonable protections to the citizens of the state, given the conditions in the state. In opting out, the insurance commissioner must detail the conditions that warrant a departure from the uniform standard and determine that the standard would not reasonably protect the citizens of the state. Once a state formally initiates the process of opting out of a uniform standard by regulation, while the process is pending, the state may to petition the Commission at least 15 days before the effective date, to stay the standard's effectiveness in the state. The Commission may extend the effective date by 90 days if the regulatory opt out has a reasonable chance of success but for no more than one year without extraordinary circumstances.

WHY IS LONG-TERM CARE INSURANCE INCLUDED IN THE COMPACT?
Long-term care (LTC) insurance is included in the Compact because it—like the other included products—is a long-term, investment-oriented insurance product that is used in retirement planning. It also is sold increasingly as a feature of life insurance and annuity products. However, during the drafting of the Compact, it was recognized that the LTC insurance market remains relatively new and evolving, and several insurance commissioners and interested parties expressed special concern about LTC consumer protections. To address these concerns, the Compact includes specific provisions aimed at LTC insurance. First, the Compact allows states to opt out of all LTC insurance uniform product standards in advance, when they enact the Compact. This provision allows states to join the compact but not for LTC insurance. Second, uniform standards for LTC insurance products must provide the same or greater consumer protections as those set forth in the NAIC Long-Term Care Insurance Model Act and Regulation, as adopted in 2001. This provision ensures a minimum threshold for consumer protections for LTC insurance products, which would be higher than those currently in most states, but does not limit the Commission's authority to enact even higher LTC insurance consumer protections.

HOW DO CONSUMERS PARTICIPATE IN THE COMPACT?
The compact model act directs the Commission to establish an advisory committee for consumer representatives. It directs a similar advisory committee for insurance industry representatives. These groups would participate in the process of creating uniform standards and would serve as a formal mechanism for consumer representatives to monitor the operations of the Compact and to make recommendations. The model act does not address whether the Compact will provide funding for the consumer advisory committee, but it is possible that financial assistance could be provided for it in the Bylaws in a manner similar to the NAIC funded-consumer representative program.

HOW WILL THE COMPACT RAISE PRODUCT STANDARDS?
Although the Compact does not precondition what standards will be created (except for long-term care insurance, where it sets a floor), it contains several key features designed to promote higher product standards. The most important feature is its voluntary nature. If product standards created by the Compact are not adequate, states will opt-out of the uniform standards and the Compact will not work. A second feature is geographic balance. Where all member states belong to the Commission, which must approve product standards before they're effective, the six largest states, which tend to have stronger consumer protections, have permanent seats on the Management Committee, where uniform standards must originate. Finally, the Compact requires supermajorities of both the Management Committee and Commission to approve uniform product standards. These features promote a consensus-based approach to decision-making, which promises to produce higher product standards to benefit consumers in exchange for an effective single point of filing with uniform standards that will provide insurers with the "speed to market" that they need to compete.

WHO ENFORCES DECISIONS OF THE COMPACT?
The state insurance commissioner would continue to oversee market regulation activities. However, the Commission would monitor member states for compliance with the bylaws, rules, uniform standards and operating procedures of the Commission. The Commission would provide assistance to state insurance departments in determining whether a violation of a uniform standard had occurred. Additionally, the Compact expressly preserves the authority of state attorneys general to enforce general consumer protection laws, such as unfair or deceptive trade practices statutes, including but not limited to maintaining any actions or proceedings, as authorized by

law.

WOULD THE PUBLIC BE ABLE TO ACCESS COMPACT RECORDS AND INFORMATION?
The Commission would be required to establish conditions and procedures to promote the public inspection of its information and official records with the limited exception of information and records related to individual privacy and trade secrets. Additional rules may apply to make information and records available to state and federal agencies. The Commission would be directed to establish procedures to mandate opening meetings. It would be allowed to meet in camera for specific reasons and only when a majority of the Commission votes to close them meeting. Additionally, it would be required to make public the vote to close the meeting and any votes taken while the meeting was closed. The Compact stipulates that Commission Bylaws be published and made available to the public.

WHEN WOULD THE COMPACT BECOME OPERATIONAL?
The Compact would come into existence when two states enact the compact model act. The Compact would become operational when 26 states or states representing 40 percent of the premium volume for life insurance, annuities, disability income and long-term care insurance join the Compact.

WHAT IS THE FISCAL IMPACT OF THE COMPACT ON MEMBER STATES?
Joining the Compact would have no direct fiscal impact on states. Filing fees, i.e., user fees, paid by insurers would finance Commission activities, and the model act authorizes the Commission to accept appropriate donations and grants of money, which could include a grant from NAIC to pay for start-up costs. States could realize performance efficiencies as companies file products with the Compact rather than state insurance departments. A portion of the approximately 200 state department employees who currently review products for asset-based insurance products could be reassigned or eliminated. Moreover, the Compact would preserve $12.5 billion a year in state insurance revenues, which would be threatened if Congress established a federal insurance regulator.

WHAT ADDITIONAL POWERS DOES THE MODEL ACT GIVE TO THE COMPACT?
The Commission would be able to designate products and advertisements that may be subject to a self-certification process without the need for prior approval. It also would have the authority to establish and maintain offices; to issue subpoenas; to purchase and maintain insurance and bonds; to borrow, accept or contract for services of personnel; to hire employees, professionals or specialists; and to elect or appoint officers. The Commission would be able to lease, purchase, and accept appropriate gifts or donations of property; to establish a budget and make expenditures; to borrow money; and to provide and receive information from and to cooperate with law enforcement agencies. It also would be have the authority to perform other functions as may be necessary or appropriate to achieve the purposes of the Compact consistent with the state regulation of the business of insurance.

WOULD A MEMBER STATE BE ABLE TO WITHDRAWAL FROM THE COMPACT?
Yes. A member state could withdrawal from the Compact at any time by repealing the statute that enacted the Compact into law. Withdrawal would be effective along with the statute, but products that were approved by the Compact as of the effective date of the withdrawal—unless upon the mutual agreement of the Commission and the withdrawing state—would not be affected by the withdrawal. However, a state would be able to use existing procedures under state

law for withdrawing approval of previously approved products.

COULD A MEMBER STATE BE KICKED OUT OF THE COMPACT?
Yes. A member state could be removed from the Compact if it defaulted in the performance of its obligations and responsibilities. After notice and a hearing, pending a cure to the default, the Commission could suspend it. If the defaulting state fails to cure the default within a specified period of time set by the Commission, the defaulting state would be terminated from the Compact.

HOW DOES THE COMPACT AFFECT THE PROSPECT OF FEDERAL REGULATION?
Congress signaled an era of increased federal interest in insurance regulation with the passage of the Gramm-Leach-Bliley Financial Modernization Act of 1999. Since that time, states have respond with tremendous success to congressional pressure to streamline and simplify state systems by reevaluating and adjusting virtually every aspect of the state systems. These efforts continue. However, experience thus far has shown product regulation for asset-based insurance to be one regulatory function that requires a national system to meet the needs of the modern financial marketplace. By providing a national, state-based system that addresses legitimate industry concerns while preserving the strengths of the state system, the Compact denies proponents of a federal regulator their best argument for federal regulation and thereby weakens their case. Although congressional interest in insurance regulation is certain to continue, the successful implementation of the Compact will preserve the state system by focusing the debate on ways to further modernize the state system rather than replace or diminish it with a new federal bureaucracy.