Insurance Association of Connecticut

Public Hearing

Legislative Program Review and Investigations Committee

September 25, 2012

Study -- Assessment Methodology and Process to Fund the Connecticut Insurance Department

The Insurance Association of Connecticut (IAC) appreciates the opportunity to speak to the Legislative Program Review and Investigations Committee (PRI) concerning its ongoing study entitled "Assessment Methodology and Process to Fund the Connecticut Insurance Department."

As we understand it, the study is generally intended to consider (1) the effects of expanding assessment responsibilities for funding the Insurance Department to all insurers doing business in the state, and (2) the funding mechanisms used by other states to fund their insurance regulatory agencies.

Currently the Insurance Department's operating costs are funded by an assessment against domestic insurers. While on its face an expansion of the assessment to include all insurers doing business in Connecticut might appear to be a positive change for domestic insurers, it actually will cause financial harm to Connecticut insurers that compete for business throughout the country by exposing them to increased retaliatory taxes in other states. Expanding the assessment base will result in increased tax collections in other states, benefiting their coffers, but will have a counterproductive effect on the state's insurance industry as those insurers compete for business in other states.

Forty-nine states, including Connecticut (C.G.S. 12-211), have retaliatory, or reciprocal, tax statutes. Retaliatory tax is the mechanism through which insurance companies are protected from excessive or discriminatory taxation when doing business in another state. In its simplest form, a retaliatory tax calculation compares the tax burdens between two states, the state in which the insurer is doing business (host state) and the insurer's state of domicile (home state).

When a state other than Connecticut (State X) determines what taxes a Connecticut insurer must pay to it, it compares the amount of taxes insurers pay for doing business in State X to the amount of taxes that Connecticut charges to insurers domiciled in State X for doing business in Connecticut. If Connecticut taxes are higher, then State X will assess a retaliatory tax on Connecticut insurers doing business in State X equal to the excess amount in order to "level the playing field".

If Connecticut expands the Department's assessment to include non-Connecticut insurers, Connecticut insurers doing business across the country will suffer increased retaliatory tax liabilities in numerous states. The degree of impact will vary from insurer to insurer, based on the specifics of their business.

Insurance is an export business. Well over 90% of the policyholders of Connecticut insurers are located outside of Connecticut. Expanding the assessment base, and a corresponding increase in retaliatory taxes paid to other states, will increase the cost of Connecticut insurers doing business in those states, putting them at a competitive disadvantage, and outweigh any local savings such an expansion may create.

The General Assembly has consistently recognized the potential adverse consequences of retaliatory taxes on Connecticut insurers by passing legislation over the years to minimize or eliminate those negative effects.

For example, in 2003 the General Assembly decided to fund the state's childhood immunization program by assessing life and health insurers annually for the cost of the program (C.G.S. 19a-7j). The assessment was limited to domestic insurers in order to prevent increased retaliatory taxes on Connecticut insurers (however, the assessment on domestic life insurers was repealed in the 2012 Special Session, as the General Assembly acted on IAC's longstanding complaint that there is no correlation or relationship between childhood immunizations and the life insurance business).

As another example, C.G.S. 38a-11 establishes various fees to be paid to the state for insurance agent appointments. As amended in 2005 and 2009, the section specifically provides that agent appointment fees are lower for non-Connecticut insurers than Connecticut insurers, that those non-domestic fees are further reduced if the insurer is domiciled in a state with a premium tax rate below Connecticut's rate, and that no appointment fees are required if the insurer is domiciled in a state which does not require any such filing fee, all in recognition of what would otherwise be corresponding counterproductive retaliatory tax effects on Connecticut insurers.

Expanding the Department's assessment base would not conform Connecticut law to a national model for funding an insurance department. Numerous states fund their insurance departments with general fund dollars. Some insurance departments also retain all fees and fines they collect as part of their funding base (in Connecticut, fees and fines are forwarded to the state's General Fund). Some states combine various types of assessments with fines and fees. There is no standard mechanism that states use to fund their respective departments.

Reviewing information published by the National Association of Insurance Commissioners in December, 2011, it appears that approximately 18 states and Washington DC use insurer assessments as a means of funding their respective insurance departments in whole or in part. Of those, several states have established mechanisms to protect their domestic insurers from retaliation. For example, New York and Connecticut only assess domestic insurers. Virginia gives a credit against premium taxes owed by Virginia insurers for any retaliatory taxes paid by those companies to other states (credit is not limited to the Department funding issue). Of the remaining states, most either do not have a major domestic insurer presence or have a low premium tax rate, so the retaliatory risk for their domestic industry is diminished. It should also be pointed out that several states (such as Kentucky, Maine and Massachusetts) with the statutory authority to assess insurers for funding purposes were reported to have made no such assessments in 2011.

The IAC respectfully submits that the assessment base for funding the Insurance Department should not be expanded. The IAC would welcome the opportunity to provide PRI staff with additional information and comment as they work to completion of the study.

Thank you for your consideration.