

**FY 2010 BUDGET REDUCTIONS - SUMMARY OF ISSUES  
DEPARTMENT OF INSURANCE**

**GENERAL FUND**

**FY 2010 General Fund Budget      6,082,000**

**AGENCY REDUCTION TARGET - GENERAL FUND      \$912,300**

<b>Priority</b>	<b>Issue Title<sup>1</sup></b>	<b>Reductions Amount</b>
1	Establish DOI as a self-funded agency	N/A
2	Permanently eliminate currently vacant positions	\$399,000
3	Abolish ARS § 20-466 and eliminate the DOI Fraud Unit	\$239,017
4	Abolish ARS § 20-340 et seq. and eliminate investigation of unlawful insurance activity by agents, adjusters and other licensees	\$65,240
5	Eliminate managed care HMO oversight (aka HCSOs - Health Care Services Organizations)	\$209,043
	<b>Issue Total</b>	<b>\$912,300</b>
	<b>Fund Total as a Percentage of General Fund Reduction Target</b>	<b>100%</b>

<sup>1</sup> Please complete the attached Description and Impact Statement for each issue.

**FY 2010 BUDGET REDUCTIONS - SUMMARY OF ISSUES  
DEPARTMENT OF INSURANCE**

**ALL NON-GENERAL FUNDS**

FY 2010 All Non-General Funds Budget (less Federal Funds)      5,315,500

AGENCY REDUCTION TARGET - ALL NON-GENERAL FUNDS (w/o Federal Funds)      \$797,325

Fund	Reductions Amount	Percent Reductions
Fund 2034: Insurance Examiners' Revolving Fund	\$797,325	100.0%
<b>Issue Total</b>	<b>\$797,325</b>	

All Non-General Funds Total as a Percentage of Agency Non-GF Reduction Target      100%

DRAFT

**FY 2010 BUDGET REDUCTIONS - SUMMARY OF ISSUES  
DEPARTMENT OF INSURANCE**

**INSURANCE EXAMINERS' REVOLVING FUND**

<b>FY 2010 All Non-General Funds Budget (less Federal Funds)</b>	<b>5,315,500</b>
<b>AGENCY REDUCTION TARGET - ALL NON-GENERAL FUNDS (w/o Federal Funds)</b>	<b>\$797,325</b>

<b>Priority</b>	<b>Issue Title<sup>1</sup></b>	<b>Reductions Amount</b>
5	Eliminate managed care HMO oversight (aka HCSOs - Health Care Services Organizations)	\$119,805
6	Eliminate insurance market analysis and insurer examinations for oversight of unlawful insurance activity	\$677,520
	<b>Issue Total</b>	<b>\$797,325</b>
	<b>Fund Total as a Percentage of Non-General Fund Reduction Target</b>	<b>100%</b>

<sup>1</sup> Please complete the attached Description and Impact Statement for each issue.

**STATE OF ARIZONA  
FY 2010 BUDGET REDUCTIONS - ISSUE DESCRIPTIONS**

**Department of Insurance**

**Issue Title:** Establish DOI as a self funded agency

**Issue Priority: 1**

**Reduction Amounts:** This Issue Priority would remove the Department of Insurance (DOI) from General Fund appropriation, pay for DOI operations from licensing fees and fraud unit assessments, and deposit all other fees to the General Fund.

**Issue Description and Statement of Effects**

We propose the creation of the Department of Insurance Fund for the collection of all licensing fees collected pursuant to ARS §20-167 and assessments collected pursuant to ARS §20-466(J) in order to pay all expenses involved in DOI operations.

- This concept is not new - 33 state insurance departments have dedicated funds (maintaining all fees, assessments, fines and penalties the DOIs generate).
- 4 other state DOIs have “quasi-dedicated funds” which return the balance at the end of the year to the states’ general funds.
- Our proposal holds the General Fund harmless---DOI would return the excess of fees collected (see Exhibit A attached) at the end of the year to the General Fund, approximately \$3.1 million per fiscal year under the current fee schedule, in addition to the approximate \$432 million in insurance premium tax DOI collects annually.
- Preserves DOI’s current ability to provide consumer protection and assistance (approximately 50,000 complaints/inquiries per year), regulate the variety of insurance-related entities that we license (approximately 162,000 agents), license and monitor insurers to assure financial solvency (approximately 1,800 licensed insurers) and compliance with Arizona law.
- Absent adoption of this DOI Self Funding Proposal, Issues 2-7 herein set forth details on DOI Programs that may otherwise be eliminated and the consequential effects on Arizonans if DOI does not perform these essential insurance regulatory functions.
- The insurance industry would support this Self Funding Proposal as insurance companies and insurance agents would benefit from DOI’s continued ability to respond quickly to insurer product filings (Arizona law requires insurers to file policy rates, forms and contracts for DOI review and analysis to assure compliance with Arizona law), investigate insurance fraud, and issue licenses to companies and agents, ensure financial solvency and regulate their activity.

- Necessary statutory amendments are minimal and straightforward. (See Exhibit A attached).
- Eliminates the legislature's need to suspend laws that otherwise require DOI to reduce its fee schedule and thus General Fund revenues (ARS §§20-167(F) & 20-466(J)).

DRAFT

Exhibit A  
Summary of Necessary Statutory Changes  
to Establish the DOI as a Self Funded Agency

1. Modify ARS § 20-167 to create a new “Department of Insurance Fund” for the deposit of all license fees collected in accordance with ARS §20-167; DOI to use these fees to pay salaries, compensation and other expenses involved in DOI’s operation per ARS §20-155. Fund to be effective as of July 1, 2010. (\$6.1 million total licensing revenues expected in FY 2010, meeting the Department’s \$6.08 million budget.)
2. Modify ARS § 20-167 to allow the Director to annually adjust the fee schedule to collect 95%-110% of the Department’s budget from the prior fiscal year.
3. Modify ARS § 20-167 to require that by September 30 of each year, the Department shall revert to the General Fund the balance of the Department of Insurance Fund as of the end of the prior fiscal year, less any prior year outstanding encumbrances and current year rent, risk management and employee benefit costs.
4. Modify ARS § 20-466 to create an “Insurance Fraud Investigation and Deterrence Fund” to pay for DOI fraud unit operations and fraud prosecution expenses. Modify ARS § 20-466(J) to specify that proceeds from insurer assessments would be deposited to this Fund.

**STATE OF ARIZONA  
FY 2010 BUDGET REDUCTIONS - ISSUE DESCRIPTIONS**

**Department of Insurance**

**Issue Title:** Permanently eliminate currently vacant positions

**Issue Priority: 2**

**Reduction Amounts:**

General Fund: \$399,000

**Total: \$399,000**

**Issue Description and Statement of Effects**

- Last year's budget reductions required DOI to reduce its General Fund workforce by 40% -- from 106.5 authorized FTEs to 64.0 filled FTEs -- severely restricting our ability to assist and protect insurance consumers. This Issue Priority would make last year's cuts permanent.
- Continued reduced insurance fraud and consumer fraud investigations.
- Continued reduced insurance consumer assistance and protection.
- Down from 14 filled FTEs in FY08, DOI now has 4 filled FTEs to handle the approximate 2,500 insurance fraud cases reported to DOI each year. Permanently eliminating the 10 vacant positions would render DOI permanently ineffective in investigating and facilitating prosecution of insurance fraud in Arizona, especially considering the increased fraudulent activity as the result of last year's economic downturn.
- Beginning in FY2011, the General Fund will lose approximately \$330,000 in revenue by operation of ARS § 20-466 (insurer fraud assessments must match fraud unit budget).
- Down from 19 filled FTEs in FY08, DOI now has 12 filled FTEs to handle the approximately 50,000 consumer complaints and inquiries submitted to DOI each year. No other state agency or entity has the expertise to handle insurance consumer inquiries or complaints. DOI acts as an intermediary with the insurance company or agent to resolve consumer complaints and facilitated \$8.3 million in settlements/recoveries for Arizona insurance consumers in FY09 (\$6.1 million in FY08, \$6.2 million in FY07).
- Apart from DOI's Self Funding Proposal (Issue #1 herein), there is no alternative funding mechanism for these regulatory and consumer protection activities.
- Arizona Const. Art. 15 § 5 ("Domestic and foreign insurers shall be subject to licensing, control and supervision by a department of insurance as prescribed by

law"); ARS § 20-466 *et seq.* requires DOI to investigate and facilitate prosecution of insurance fraud; ARS § 20-441 *et seq.* (Unfair Practices and Frauds Act) provides the statutory authority for DOI's consumer protection and enforcement activities.

DRAFT

**STATE OF ARIZONA  
FY 2010 BUDGET REDUCTIONS - ISSUE DESCRIPTIONS**

**Department of Insurance**

**Issue Title:** Abolish ARS § 20-466 and eliminate the DOI Fraud Unit

**Issue Priority:** 3

**Reduction Amounts:**

General Fund: \$239,017

**Total:** \$239,017

**Issue Description and Statement of Effects**

- ARS §20-466 establishes a Fraud Unit in DOI to investigate alleged insurance fraud in Arizona. ARS §20-466(G) requires insurers to report all claims in which the insurer believes “a fraudulent claim has been or is being made” against the insurer.
- Due to last year’s reduction in force, DOI is down from 14 filled Fraud Unit FTEs to only 4 filled FTEs left to handle the approximate 2,500 insurance fraud cases reported to DOI each year. With the severity of the economic downturn this past year, the number of fraudulent insurance claims has drastically increased.
- At this point, with only 4 FTEs the Fraud Unit can now handle only a very limited number of only the most egregious fraud cases. It takes significantly longer to investigate cases, we are referring fewer cases for prosecution to the Attorney General’s and County Attorney’s Offices and we are recovering less restitution for insurance companies.
- ARS § 20-466(J) requires DOI to collect assessments from Arizona-authorized insurers to recover DOI’s appropriated Fraud Unit budget. Eliminating the DOI Fraud Unit means eliminating this assessment revenue to the General Fund.
- Apart from DOI’s Self Funding Proposal (Issue #1 herein), or moving the Fraud Unit to the Attorney General’s Office, there is no alternative funding mechanism for DOI Fraud Unit operations.
- Arizona Const. Art. 15 § 5 (“Domestic and foreign insurers shall be subject to licensing, control and supervision by a department of insurance as prescribed by law”); ARS § 20-466 provides the statutory authority for Fraud Unit enforcement activities.

**STATE OF ARIZONA  
FY 2010 BUDGET REDUCTIONS - ISSUE DESCRIPTIONS**

**Department of Insurance**

**Issue Title:** Abolish ARS § 20-340 *et seq.* and eliminate investigation of unlawful insurance activity by agents, adjusters & other licensees

**Issue Priority:** 4

**Reduction Amounts:**

General Fund: \$65,240

**Total:** \$65,240

**Issue Description and Statement of Effects**

- DOI licenses approximately 162,000 insurance agents, adjusters and bail bond agents. DOI's Administrative Enforcement Section (AES) investigates allegations of unauthorized and/or unlawful insurance activity and insurance code violations by agents and other professional service licensees (including predatory sales practices, deceptive or misleading advertising, misappropriation of premium payments, illegal withholding of bail money, phony insurance companies and products, and other unlawful insurance practices).
- Due to last year's reduction in force, AES is now down to only 2 FTE investigators and both positions would be eliminated if we implemented this option.
- DOI devotes a disproportionate amount of resources on complaints, investigations and licensing problems related to bail bond agents and bail recovery agents. There are only approximately 200 Arizona resident bail bond agents, yet they easily consume more than 2/3rds of the agency's administrative investigations.
- Loss of these regulatory investigation activities increases the likelihood that some insurance companies and agents will not comply with Arizona insurance laws and regulations, thus increasing fraud, complaints, and reducing civil penalty revenue to the General Fund. There will be little if any disciplinary action against insurance agents and other professional licensees.
- Apart from DOI's Self Funding Proposal (Issue #1 herein), there is no alternative funding mechanism for AES operations. DPS or the sheriffs' offices would be more efficient and logical agencies to regulate bail bond agents and bail recovery agents.
- Arizona Const. Art. 15 § 5 ("Domestic and foreign insurers shall be subject to licensing, control and supervision by a department of insurance as prescribed by law"); ARS §§20-142 & 20-152 provide the statutory authority for AES enforcement activities.

**STATE OF ARIZONA  
FY 2010 BUDGET REDUCTIONS - ISSUE DESCRIPTIONS**

**Department of Insurance**

**Issue Title:** Eliminate managed care HMO oversight  
(aka HCSOs - Health Care Service Organizations)

**Issue Priority:** 5

**Reduction Amounts:**

General Fund: \$209,043

Insurance Examiners' Revolving Fund: \$119,805

**Total:** \$328,848

**Issue Description and Statement of Effects**

- The Department's Managed Care HMO Oversight Program operates within our Life and Health Insurance Regulation Division and regulates the operations and medical services delivery (including HMO "in network" adequacy) of HMOs and prepaid dental plans doing business in Arizona. The legislature transferred these regulatory responsibilities from DHS to DOI in 2001.
- Eliminating the Program would require laying off 6 filled FTEs.
- Elimination of DOI's Managed Care HMO Oversight Program would mean the loss of enforcement of Arizona laws requiring timely insurance payments to doctors, hospitals and other healthcare providers, and oversight of compliance with Arizona health care appeals laws.
- We receive and investigate grievances from healthcare providers alleging insurance law violations. Our examination results frequently show that insurers adjudicate claims inaccurately and illegally and may not have the "grievance system" the law requires. Without this DOI oversight, consumers will be harmed because they generally have to pay the healthcare providers whatever the insurer does not pay.
- Elimination of the Managed Care HMO Oversight Program means DOI would not be able to enforce insurance laws (via civil penalties and corrective action orders) when HMOs and prepaid dental plan insurers wrongfully delay or deny medical services claims; there would be no enforcement of timely and accurate payment to healthcare providers; there would be no regulation and oversight of HMO network adequacy (ensuring HMO has adequate "in-network" doctors, hospitals, etc.).
- Alternative funding would be under the DOI's Self Funding Proposal (Issue #1 herein), or, we could pay for a greater portion of Managed Care HMO Oversight

activities from the Insurance Examiner's Revolving Fund ("IERF") and recoup the expenses from insurers. Note that this Program is partially self-supporting because insurers pay for examination costs (IERF). Reductions in IERF examination costs will result in even greater reductions to revenues that we collect to cover direct and indirect Program expenses. DOI would have to charge insurers more for other examinations to recoup indirect Program costs, including the \$595,600 in fund transfers required by HB 2643, and the IERF would not have any additional surplus to transfer to the General Fund.

- Arizona Const. Art. 15 § 5 ("Domestic and foreign insurers shall be subject to licensing, control and supervision by a department of insurance as prescribed by law"); ARS §§20-1001 *et seq.*, 20-1051 *et seq.*, 20-2301 *et seq.*, 20-2530 *et seq.*, 20-3101 *et seq.*, AAC R20-6-1901 *et seq.* provide the statutory authority for DOI's regulatory oversight of HMOs, prepaid dental plans, timely payments & grievance law and healthcare appeals law regulation and enforcement.

DRAFT

**STATE OF ARIZONA  
FY 2010 BUDGET REDUCTIONS - ISSUE DESCRIPTIONS**

**Department of Insurance**

**Issue Title:** Eliminate insurance market analysis and insurer examinations for oversight of unlawful insurance activity

**Issue Priority:** 6

**Reduction Amounts:**

Insurance Examiners' Revolving Fund: \$677,520

**Total:** \$677,520

**Issue Description and Statement of Effects**

- The Market Oversight Division (MOD) protects Arizona consumers in 2 ways: (1) analyzing insurer specific information and industry-wide market trends and consumer complaint data to identify and prevent problems as early as possible; and, (2) performing targeted on-site examination of insurers - their policies, procedures, correspondence, policy applications, claims files and other information demonstrating insurer marketing, underwriting and claims settlement practices, for possible insurance law violations, corrective action plans, restitution to policyholders and civil penalties to the General Fund.
- Implementing this option would mean laying off all 4 remaining MOD employees.
- In FY09, MOD conducted 24 insurer examinations, imposed \$102,480 in civil penalties paid to the General Fund (\$236,500 in FY06; \$362,740 in FY07; \$551,000 in FY08) and recovered \$26,168 in restitution for Arizona consumers (\$141,994 in FY06, \$75,078 in FY07, \$69,464 in FY08).
- Eliminating MOD's market detection system could impact Arizonans with increased coercive and deceptive insurance practices, unfair/unlawful discrimination in the underwriting, sale and marketing of insurance, unfair claims practices, unlawful claim delays and denials.
- MOD is an entirely self supporting program - insurers pay all expenses associated with this Program (salaries, administration, contract examiners, etc.). Eliminating this Program would cost more than it saves, eliminating \$939,200 in revenues that we collect to cover direct and indirect Program expenses. DOI would have to charge insurers more for financial examinations to recoup indirect Program expenses, including the \$595,600 in fund transfers required by HB 2643, and the IERF would not have any additional surplus to transfer to the General Fund.

- As an alternative to eliminating this Program, apart from DOI's Self Funding Proposal (Issue #1 herein), the DOI could increase charges to insurers for indirect examination costs from 70% to 120% of examiner fees to generate a surplus that could be transferred to the General Fund. This may not be a lawful means to create a continued revenue stream for the General Fund and may be viewed as a hidden tax on insurers.
- Arizona Const. Art. 15 § 5 ("Domestic and foreign insurers shall be subject to licensing, control and supervision by a department of insurance as prescribed by law"); ARS § 20-441 *et seq.* (Unfair Practices and Frauds Act) provides the statutory authority for MOD's enforcement activities.

DRAFT