SUBCHAPTER FF. Credit Life and Credit Accident and Health Insurance

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1. INTRODUCTION. The Commissioner of Insurance adopts new §§3.5002, 3.5206, and 3.5603 and amendments to §§3.5001, 3.5105, 3.5201, 3.5202, 3.5307, 3.5502, 3.5601, 3.5602, 3.5604, 3.5607, 3.5608, 3.5610, 3.5901, 3.5905, and 3.6002, concerning credit life and credit accident and health insurance. Sections 3.5001, 3.5201, 3.5202, 3.5206, 3.5502 and 3.5610 are adopted with changes to the proposed

text as published in the November 19, 2004 issue of the Texas Register (29 TexReg 10684). Sections 3.5002 and 3.5603 and amendments to §§3.5105, 3.5307, 3.5601, 3.5602, 3.5604, 3.5607, 3.5608, 3.5901, 3.5905, and 3.6002 are adopted without changes.

2. REASONED JUSTIFICATION. The new sections implement legislation enacted by the 77th Legislature in House Bill (HB) 2159. HB 2159 amended Insurance Code Chapter 1153 with regard to the setting of premium rates for credit life and credit accident and health insurance by changing the way those rates are set. Previously, the Commissioner of Insurance, through a contested case proceeding, established a presumptive premium rate for all classes of business and terms of coverage, and insurers that experienced excessive loss ratios, as defined by rule, could request approval for deviations from the presumptive premium rate. The most recent presumptive premium rates were established by Commissioner's Order No. 00-0214 *Nunc Pro Tunc* (2000 rate order). HB 2159, however, requires that the commissioner set presumptive premium rates by rulemaking, rather than through a contested case. It also allows insurers to file their rates in an amount that deviates from the presumptive premium rates without seeking written approval from the commissioner, as long as the deviated rate is no more than 30% above nor 30% below the presumptive premium rate. HB 2159 also allows insurers that meet certain conditions to use rates that are more

than 30% above or below the presumptive premium rates, if the insurer obtains prior written approval from the commissioner.

Pursuant to the new ratemaking procedures of HB 2159, on June 1, 2004, the department published credit life and credit accident and health statistical data collected from credit insurers for the years 2000, 2001, and 2002 and solicited rate proposals from interested persons. The department's contracted actuary, Milliman, reviewed the published credit life and credit accident and health data, as well as submissions from interested persons, and prepared a rate assessment and recommendation based on that information. The department also made available for informal comment a draft proposal that incorporated Milliman's rate recommendations. The department posted the Milliman report, rate recommendations from interested parties, information responsive to inquiries about the recommendation, statistical data for 2000–2002, and comments on the proposed rule on its web site, and these items were also available to interested persons on request. The department also held informal meetings on the rate proposals and associated issues on October 26 and December 13, 2004.

Credit rates in Texas have traditionally been applied to predetermined classes of business, as defined in §3.5002. In reviewing industry expense and experience data supplied in response to the credit insurance data call, however, the department observed that the loss ratios and compensation percentages for one class, Class E--Dealers, were significantly different (lower for loss ratios and higher for commissions) than the other classes in both credit life and credit accident and health. The department

believes that this disparity establishes a basis for distinguishing between Class E and all other classes of business. In order to give interested persons the greatest latitude in commenting on this proposed change, the department published for comment two alternatives, one that established a presumptive premium rate for Class E alone, with a different presumptive premium rate for all classes other than Class E (Alternative 1), and a second alternative that established a composite presumptive premium rate for all classes of business combined (Alternative 2). The department sought comments on the alternatives as well as on which alternative to adopt. Likewise, for the same reasons, the department proposed two alternatives for comment with regard to the loss ratios in §3.5202 - one that established loss ratios for Class E alone, with different loss ratios for all classes other than Class E (Alternative 1), and a second alternative that established composite loss ratios for all classes of business combined (Alternative 2). After considering all comments, both for and against adoption of each alternative, the department has determined to adopt Alternative 1, with changes to the proposed language, for the loss ratios adopted in §3.5202 and for the presumptive premium rates adopted in §3.5206.

In response to comments, the department changed the calculation of the general expense component in the rates from a weighted average to the average of the experience for the period 1997 – 2002. This produced a new value for the general insurance expense component in the rate formula, which in turn produced different presumptive premium rates than those in the proposal. The new rates are found in

§3.5206. Because the loss ratios in §3.5202 are derived from the presumptive premium rates in §3.5206, the change in presumptive premium rates also caused those loss ratios to change.

In addition, minor changes have been made to §§3.5001, 3.5201, 3.5502 and 3.5610 to update references, correct typographical errors and remove redundant language.

3. HOW THE SECTIONS WILL FUNCTION. Section 3.5001 updates a statutory reference from Insurance Code Article 3.53 to Insurance Code Chapter 1153. Similar amendments to update statutory citations are found in §§3.5105, 3.5201, 3.5502, 3.5610 and 3.5905. Similarly, §3.5905 updates a statutory citation from a reference to Texas Civil Statutes, Article 5069, Chapters 3 - 6, 6A, 7 and 15 to the current citation, which is Finance Code Chapters 342 - 348. Finally, because this order relocates rule language and adopts new sections, it includes various amendments to assure correct citations to other rule sections, adherence to proper form, and enhanced readability.

Section 3.5002 includes definitions for the subchapter. All of the definitions that were previously found in §§3.5110 and 3.5603 are included in this new section. The new section also includes definitions for the terms actual earned premium, approved deviation by case, automatic deviation, class of business, credit disability, presumptive premium rate, pro rata method, rule of anticipation and sum of the digits method, also known as rule of 78 method.

Section 3.5202 provides that the test of reasonableness of the relation of benefits to premiums charged (loss ratio) applies only to approved deviations. Language was also added to clarify that the loss ratio comparison is to be applied to rates that would exist if an approved deviation is allowed to become effective. The loss ratios that serve as the parameters for the test of reasonableness addressed in §3.5202 were determined using the underlying proposed presumptive premium rates and their claims cost components. As noted earlier, this section also establishes separate loss ratios for Class E alone and for all other classes, pursuant to the adoption in §3.5206 of separate presumptive premium rates for Class E.

The ratemaking methodology set forth in the proposal was used and resulted in the presumptive premium rates that are set forth in §3.5206 and the corresponding loss ratios that are found in §3.5202.

Section 3.5307 deletes language from the section that was not pertinent and which could create confusion about the standard established by §3.5307.

Section 3.5601 requires that a request for an approved deviation must be presented on form CI-DRF and in accordance with §3.5602. The language of §3.5602 includes specific reference to form CI-DRF.

The text of adopted §3.5603 includes the credibility table that was a part of old §3.5603, that is being repealed simultaneously with this adoption order. The language of §3.5607 clarifies that the authorization addressed by that section is the upward approved deviated single account case rate.

The repeal of §§3.5110 and 3.5603 is published elsewhere in this issue of the Texas Register.

4. SUMMARY OF COMMENTS AND AGENCY RESPONSE TO COMMENTS.

GENERAL

Comment: A commenter believes that the proposed presumptive premium rates are excessive and do not satisfy the statutory requirement that credit insurance premiums be reasonable in relation to benefits provided. The commenter asserts that, in order to be reasonable and to harmonize the various provisions and requirements of Insurance Code Chapter 1153, including carriers' ability to take an automatic 30% upward deviation, the presumptive premium rates must be established at 1/1.3 of reasonable prima facie rates.

Another commenter notes that the department's proposal is for an overall rate decrease across all classes and plans combined of 8.4% for credit life insurance and 3.7% for credit accident and health insurance. While the commenter agrees with a rate decrease, he believes that a much larger decrease is appropriate. By not proposing a sufficiently large rate decrease, the commenter maintains that the department would be allowing credit insurance companies to charge excessive rates.

Agency Response: Insurance Code §1153.105, which authorizes automatic deviations, clarifies that a carrier may implement a deviation from presumptive premium rates of not more than 30% without seeking prior approval of the commissioner. This

standard, however, is independent of the directive in Insurance Code §1153.103(d) concerning the information that must be considered when setting presumptive premium rates. The regulatory scheme established by Chapter 1153 contemplates that the commissioner will set the presumptive premium rates based on the information required by §1153.103(d), and that thereafter insurers may use rates which deviate from the presumptive premium rates if they follow the required procedures. Simply reducing the calculated presumptive rates by the factor 1/1.3 would be inconsistent with the intent of the law.

In addition, these rules meet the statutory requirement that credit insurance premiums be reasonable in relation to benefits provided. The component methodology used to develop the presumptive premium rates adopted in this order is the same methodology used to develop the presumptive premium rates in the 2000 order and produces a rate that is consistent with the requirements of Chapter 1153. This is a generally accepted actuarial approach and the individual components in the formula were determined using sound actuarial principles and a fair evaluation of market conditions based on data from credit data calls.

REVERSE COMPETITION

Comment: A commenter states that the proposed presumptive premium rates are the result of an actuarial analysis that fails to acknowledge that there is reverse competition in credit insurance markets. The commenter concludes that the analysis

does not consider the reasonableness of the actual historical experience values of the various non-claim rate components. According to the commenter, reverse competition -- competition among credit insurers to sell group policies to lenders -- drives up credit insurance expenses by driving up lender/producer compensation. For example, a credit insurer that charges a premium of $1.00 would lose business to other credit insurers who charge a premium of $1.30, because lenders will choose the insurer with the rate which produces the larger commission. The commenter also cites the automatic deviation filings of credit insurers following the enactment of HB 2159, which show that every non-credit union credit insurer filed for the maximum 30% upward deviation, regardless of the insurers' claim experience. The commenter notes these carriers' common justification that the increase was needed to offset higher acquisition costs to remain competitive in the Texas insurance marketplace. The commenter also notes that insurers' filings did not cite a need to raise rates because of higher than expected claim costs. The commenter argues that these explanations reveal reverse competition because lenders demanded more compensation ("higher acquisition costs" for the credit insurer).

Agency Response: The department agrees that reverse competition does exist in the credit insurance market in Texas, and included a finding to that effect in the 2000 rate order. As noted by the commenter, reverse competition in this market manifests itself in the form of higher commissions paid by insurers to producers of credit insurance business. One answer might be to impose a cap on commissions. However, Insurance

Code §1153.103(e) specifically prohibits the commissioner from setting or limiting the amount of compensation actually paid by an insurance company to an agent. The rates adopted in this order do not violate that prohibition, because a credit insurer may continue to pay whatever commissions it believes are necessary to obtain business. The amount of commissions paid by insurers was among the information furnished to the department through its data call. Because of the effect reverse competition has on commissions in the credit insurance industry, the department believes it is reasonable that the commission component used in establishing these presumptive premium rates be 25%, which is in the lower range of commissions actually paid in the credit insurance market. This is also the same commission component value that was used in setting the current presumptive premium rates.

LOSS RATIOS FOR APPROVED DEVIATIONS

Comment: A commenter states that the loss ratios proposed as the standard for approval of upward deviations that exceed 30% of the presumptive premium rates are far too low to satisfy statutory standards. The commenter believes that the loss ratios fail the basic test of reasonableness because a credit insurance policy would be expected to pay out only 41 cents on each dollar of premium paid, which the commenter believes is not reasonable to consumers. The commenter argues that if insurers and agents disclosed the amount of expected benefits and the amount of producer

compensation associated with a credit insurance policy, consumers would not purchase these products.

While a component rating analysis is part of the overall evaluation of whether or not rates are reasonable, the commenter believes there must be some broader evaluation of the loss ratio to determine if the results of the component rating analysis do, in fact, produce rates with benefits that are reasonable in relation to premium. The commenter states that the department's witness in the 1999 contested case rate hearing testified that rates producing loss ratios less than 50% were not reasonable; however, the commenter believes that the current proposal has provided no such overall reasonableness evaluation. Rather, the commenter asserts that, even if claims dropped to zero, a component rating analysis could still produce a reasonable rate.

The commenter also contends that reliance solely on a component rating approach will inevitably lead to lower and lower loss ratios over time. At every hearing, the commenter contends, claim costs have dropped and, with a strict component rating analysis, insurers have incentive to continue to drive claims costs down with stricter underwriting and unfair claims settlement practices and spend greater amounts on expenses. The commenter believes that this occurs because the strict component rating approach rewards such behavior with lower loss ratio standards in each new set of rates. Finally, the commenter notes that the NAIC model regulation for credit insurance establishes 60% as the baseline for rates producing reasonable benefits in

relation to premium, and recommends a minimum loss ratio of 50% for credit life and 60% for credit disability.

Another commenter believes that the proposal requires a much smaller percentage of the premium be available to pay benefits to claimants, and allows insurance companies to keep a much larger percentage of the premium for expenses, commissions and profit. The commenter asserts that a change from a minimum loss ratio of 60% to one of 42% can raise the rates by 43%, but that the proposal has provided no reasonable basis as to why the minimum loss ratio applicable to approved deviations should be changed to allow such dramatic rate increases.

Agency Response: The attraction of credit insurance to the average consumer is that if the consumer dies or becomes disabled, the credit insurance will assure that certain items purchased by the consumer will be paid off, even if the consumer can't work and earn the money needed to make those payments. This benefits either the consumer or (typically) the consumer's family. Consequently, if a consumer were aware that a credit insurance policy could pay as little as 41 cents for each dollar of premium paid, he or she might still consider purchasing credit insurance.

The loss ratios in §3.5202 provide an initial test of whether a request for rate deviation beyond 30% is reasonable. Meeting the loss ratio test does not guarantee approval of the deviation request. But the loss ratios should be reflective of the underlying rates. This linkage of the loss ratios and the underlying rates effectively provides the overall reasonableness evaluation sought by the commenter. The

alternative is to simply choose a target loss ratio, such as the loss ratio in the NAIC model regulation. The component rating approach is a more reasonable approach to just selecting a target loss ratio, because the component rating approach reasonably mirrors the economic model on which the insurance industry is based. The presumptive premium rates were developed using actual data provided by Texas credit insurers, and reflect the actual underlying expense structure of the credit insurance industry in Texas.

The comment that posits a scenario in which claims costs might be zero and still yield a reasonable rate must be evaluated in the realistic context of today's market. If circumstances of zero claims cost persist, demand will plummet. Consumers will stop purchasing credit insurance products. Under such circumstances, the department would need to re-evaluate the presumptive premium rates. Those circumstances do not currently exist. The component rating methodology is a realistic model of today's market, and was used by this commenter to make recommendations in this process.

The expressed concern that, with a strict component rating analysis, insurers have incentive to continue to drive claims costs down with stricter underwriting and unfair claims settlement practices and to spend greater amounts on expenses is not *per se* a valid criticism of the proposal. Any insurer that is willing to use unreasonable underwriting or unfair claims settlement practices is likely to do so no matter how the presumptive premium rates are set. However, after receiving this comment the department reviewed its complaint records pertinent to credit insurance issues and found that the department had received a total of 244 justified complaints for the period

from September 1, 1999 to April 15, 2005. Of these, 10 could be construed as complaints about unfair underwriting and 124 could be construed as claims handling issues. In a universe of the many thousands of credit insurance transactions that occurred during that period of several years, the complaint history does not confirm the commenter's suggestion that the credit insurance industry is manipulating the development of rates by using unfair claims or underwriting practices.

PROFIT COMPONENT

Comment: A commenter notes that the proposal uses an underwriting profit provision of 5.75%. The commenter contends that this compares to the underwriting profit provisions underlying the current rates of -2% for credit life insurance and -4% for credit accident & health insurance. The commenter concludes that the proposed change in the underwriting profit provision underlying the presumptive premium rates increases the otherwise indicated rates by approximately 12% for credit life insurance and by approximately 15% for credit accident and health insurance.

A commenter believes that the profit component used in the development of the proposed rates is excessive and not based on any analysis of actual historical investment gains. The proposed premium presumptive rates include a profit component of 5.75%, which the commenter characterizes as an increase of 7.75 percentage points above the -2.0% profit component used in the 2000 rate order. The commenter believes that the profit component in the proposed rates ignores the impact of

investment income, which actual historical data show exceeds 15% of premium for credit life and disability insurance.

The commenter also disagrees with the statement in the proposal that investment income is already reflected in the single premium discount provision, and argues that the profit component should be rejected because there is no data or analysis to support it and because actual historical data demand a much lower profit provision.

Finally, the commenter disagrees with the reasoning offered by another commenter that “surplus strain” associated with single premium credit insurance products demands a higher profit provision, arguing that lenders should not be rewarded for choosing to offer only the single premium product because it is unfavorable to many consumers.

Another commenter believes that the proposal’s use of an investment profit value of 3.5% is too Iow and lacks reasonable support. The commenter cites information regarding the actual investment returns earned by insurance companies, which during the last decade ranged from about 5 1/2% to 9%, with an average of about 7 1/2%. The commenter notes that in the most recent title rate order, the commissioner found that a reasonable investment income rate was 6.0%. The commenter notes that the proposal’s 3.5% investment return was based on past and current yields for U.S. Treasury and corporate bonds with durations of less than five years, but argues that these are not the only types of investments made by life and accident and health

insurance companies. By ignoring the actual investments made by insurance companies, the commenter says, the proposal has understated the expected investment return, which results in an inflated rate level.

Agency Response: The profit component of 5.75% was based in part on an assumption of an investment income factor of 3.5%, which is in turn based on an estimate of expected new money investment rates during the time these new presumptive premium rates are expected to be in effect. For single premium business, insurers earn investment income, because premiums are received soon after the issue date, but policy benefits are paid over the term of the policies. The department agrees with Gary Fagg, that prudent business practices dictate that insurers invest policy funds in investment vehicles that match the terms of the investments with the terms of the liabilities. (Mr. Fagg is a Fellow of the Society of Actuaries and a Member of the Actuarial Association of America. He presented this consideration to the National Association of Insurance Commissioners' Committee on Credit Insurance, at a public hearing on December 4, 1994, in a paper entitled "Component Rating in Credit Insurance".) This same principle was emphasized by a commenter, an actuary, at the public hearing on the proposal.

Following this matching principle, the department reviewed yield rates on U.S. Government bonds maturing in two, three, and four years, as reported in the Wall Street Journal. In August of 2004, these yields ranged from 2.68% to 3.45%. We also reviewed yields on corporate bonds of six major companies with maturity dates ranging

from April, 2007 to January, 2009. These corporate bond yields ranged from 3.39% to 4.32%. The department also reviewed bond and yield data compiled by Bloomberg for 3- and 5-year U.S. Treasury notes and bonds for the period 2000 through 2003. The average yield was approximately 3.5%.

The proposal's assumption of 3.5% represents a mix of U.S. Government and corporate bond investments with terms that reasonably match the expected terms of liabilities in the credit insurance market, which are typically very short. This approach is an effort to distinguish investment income directly related to premiums from credit insurance business from the average investment income an insurance company may accrue from all of its investments over a given period.. The companies in Texas that sell credit insurance generally also sell products in other lines of insurance, which have liability terms that are different from credit insurance. The terms of the investment vehicles associated with those other lines will vary just as their liability terms vary. Thus, an insurance company may have total investment income that is very different from 3.5% of total premium, because of the diversity of products and lines of insurance that it offers.

Additionally, the historical returns on investment income noted by one commenter are not reasonably expected in the current market conditions. The assumption of 3.5% is reasonable in today's market, based on considerations just discussed.

With regard to the commenter's disagreement with the statement in the proposal that investment income is already reflected in the single premium discount provision, the formula used in the proposal to develop the base prima facie rate recognizes an interest component in the denominator of the fraction. The rate determined by each formula is lowered by an estimate of the interest expected to be earned on the single premium. The rate is reduced further by a discount factor to develop the premium rate scale to be charged to the borrower. This treatment reflects the interest component twice. In order to alleviate this "double counting," the proposal sets the interest component used in the presumptive rate formula at zero.

Surplus strain occurs in credit insurance under statutory accounting rules when a policy is issued and the single premium is only partially recognized as income (the "earned premium") but the expenses in issuing the policy (including commissions) and reserves for expected claims are immediately recognized as expense. The result is a temporary depletion of statutory surplus, until the full premium is earned over the term of the policy. To make up this depletion of surplus, the insurance company must commit additional equity in the form of assets invested in relatively conservative investments, yielding less investment return than would normally be required by the owners. The foregone investment return on these committed assets is viewed as a cost associated with selling the credit insurance and can only be compensated for through an additional profit margin. Therefore, it is appropriate to recognize the cost of surplus

strain in pricing credit insurance, and such recognition does not unfairly reward the insurance company for writing credit business.

The method used in determining the profit component is consistent with the method used in the 2000 rate order and includes an allowance for surplus strain. The premium to equity ratio used in the proposal was also used in the 2000 order, and is derived in part by risk based capital requirements, along with recognition that surplus strain on single premium business may require additional commitments of equity by the insurance carrier.

GENERAL INSURANCE EXPENSE

Comment: More than one commenter discusses the observation in the proposal that expense ratios inexplicably dropped suddenly in 2000. Because of that observation, the proposal assigns a weight of 25% to the new expense data, and 75% to the expense data from the prior period. One commenter asserts that giving only 25% weight to the most recent expense experience violates actuarial principles which require that more current experience be given greater weight. The commenter also asserts that the proposal provided no discussion or explanation why the older expense experience better reflected future expense experience. The commenter believes that giving more weight to 1999 and earlier expense experience improperly uses very old experience as a predictor of future experience. The commenter also argues that it is logical that expenses should have declined from the 1990s to the 2000s because there has been

considerable consolidation in the credit insurance industry, creating greater economies of scale in what is essentially a fixed cost business. The commenter also believes that the proposal treats the expense component as a trend and argues that there is no goal or actuarial standard defining the expense component as a trend.

Another commenter suggests leaving the expense component used to develop the current rates unchanged in developing the new rates. This commenter argues that there is no reason to believe that industry general expenses have truly dropped as a percentage of premium, asserting that nationwide premium rates have dropped slightly, production levels are down significantly, and inflation is low but positive. The commenter does not see the value of replacing the expense component currently used with data that is not fully understood and produces a result that is not supported by observed industry trends.

Another commenter also questions the drop in expenses suggested by the data, because the 2000 rate order not only lowered the rates significantly, but it also altered the method by which premiums and refunds are calculated, which required a retooling of administrative software, producer software, and annual statement software and methods. These costs of implementation would, the commenter argues, be understated by the proposal's implicit assumption that Texas business costs no more on a "per certificate" basis than any other state during this time. The commenter believes this assumption is incorrect and believes that the most recent expense data should not be given any weight.

Another commenter states that prior credit insurance rates have relied upon expenses during the most recently available three year period. The commenter believes that there has been no showing that the experience from 2000 to 2002 is not reliable, and that this experience is fully credible from an actuarial perspective. Therefore, the commenter believes that the most recent three years of expense experience, from 2000 to 2002, should be given 100% weight in the rate calculation. In the alternative, the commenter states that if the older data from 1997 to 1999 is to be used, then the more recent experience from 2000 to 2002 should be given a weight of 75% and the older experience should be weighted at 25%.

Agency Response: The data relied upon to derive the general insurance expense component was collected from the industry in the credit insurance data call, certified as accurate by insurers that submitted it, and thoroughly reviewed by department staff and Milliman. At the end of that review, the department had no reason to reject or question the data. The anomalous change in expenses reflected by the data from 1999 to 2000 and beyond currently stands without certain explanation, which gave rise to the department's initial idea of weighting the general insurance expense data from the different timeframes. The explanations offered by various commenters about why the data should or should not be believed are plausible, but are not accompanied by other data that would lead a reasonable person to conclude that the reliability of the data relied upon by the department should be questioned. In light of comments about the weighting of historical data, the apparent reliability of data available to the

department, and the unexplained change in general insurance expenses industry wide after 1999, the department has concluded that it is most reasonable to use an average of the data from the six year period of 1997 – 2002, rather than a weighted average. The presumptive premium rates and the rule are changed accordingly.

Comment: A commenter believes there is an error in the compilation of the expense data contained in the actuarial report that was relied upon in the proposal. The actuarial report contained exhibits showing credit life insurance expense data and credit accident and health insurance expense data. Those exhibits show expense data by component (i.e., rent, salaries and wages, etc.) and also as a total. However, in every instance in the actuarial report, the total values are higher than the sum of the individual expense items. This has led the commenter to conclude that the expense values used in the proposal are higher than the actual sum of the reported expenses by about 7% for credit life insurance and by about 5% for credit accident and health insurance.

Agency Response: It is true that the total expense values reflected in the Milliman report are higher than the sum of the individual expense items identified on the exhibits to the report. The data collection method explains this disparity. The credit insurance data call requested that the insurers provide expense information in the categories identified in the exhibits. The department was contacted by at least one insurer because some of the insurer's expenses did not fit into any of the categories specified in the data call, and there was no "other expense" or "miscellaneous expense" category made available in the data call. Because the categories used in the data call

did not necessarily accommodate all expenses of all the responding insurers, only the total expense line included all expenses. For that reason, the calculations used to set the presumptive premium rates relied on the expense totals provided by the insurers, rather than on a separate calculation of total expenses using the categories identified in the exhibits to the Milliman report. This is the most accurate method to assure that all expenses are taken into account.

ALTERNATIVE 1 vs. ALTERNATIVE 2

Comment: A commenter asks that the department confirm its intent to allow insurers to continue to combine classes of business for rating purposes under the presumptive rate established for “Alternative 2" for classes of business other than Class E.

Agency Response: By this order, the commissioner adopts Alternative 1, which establishes separate rates for Class E and for all other classes of business. Under the adopted rules, insurers can combine classes of business other than Class E for rating purposes. Class E rates must be handled separately.

Comment: A commenter believes that proposed Alternative 1, which would establish separate rates for Class E and for all other classes of business, is contrary to the law. The commenter argues that Insurance Code §1153.103(a) requires the commissioner to adopt a single presumptive rate for all classes, and only allows individual insurers to file separate rates for various classes. This commenter contends

that Insurance Code §1153.102(a) applies to rate setting by insurers, and not to the authorized rate promulgation process of the department or commissioner. The commenter therefore argues that a reasonable conclusion to be drawn from these provisions is that the insurer may revise its schedules of premium rates for various classes of business, after the commissioner has established a single promulgated rate.

Agency Response: The department disagrees. Insurance Code §1153.103(a) authorizes the commissioner to "…adopt a presumptive premium rate for various classes of business and terms of coverage." The wording of the statute allows the commissioner to adopt a different rate for each class of business and even for differing terms of coverage within a single class. The legislature more clearly expressed its intent that the department consider separate rates for different classes in the language of Insurance Code §1153.103(d), which requires the commissioner to consider the type or class of business when determining the presumptive premium rate.

The reasoning suggested by the commenter actually leads to the conclusion that the commissioner must set one rate – the same rate – for all credit life products and all credit accident and health products. No one has ever suggested that should happen, because those products are so different that it would not make sense. This is a clear example of the commissioner considering the different types of business when determining the presumptive premium rate. The same logic can be applied to the question of the commissioner's authority to set different rates by class of business. The available data indicate a sound basis for setting different rates based on class of

business. Pursuant to §1153.103(d), the commissioner must consider that data and set rates accordingly.

Comment: Several commenters recommend that Alternative 2 be adopted, contending that no actuarial data or conclusions regarding mortality or morbidity rates, actual or expected, were used in deriving the separate Class E proposed presumptive rates. They argue that there is no evidence to suggest that life expectancy or propensity to become disabled is related to the location of the purchase of the credit insurance policy. One commenter also states that the experience data collected by the department's credit data calls do not provide any reason for the difference in experience by class of creditor.

Another commenter that disagrees with Alternative 1 noted that in reviewing industry expense and experience data supplied in response to the data call, the department observed that the loss ratios and compensation percentages for Class E were significantly different than the other classes. But this commenter complains that the department has not articulated what is meant by ''significantly different" that would require a regulatory change to allow for presumptive rates by class. The commenter expresses an understanding of the department's concern with regard to this class of business, but believes that the department has failed to illustrate if the difference was a result of failure to report information accurately in the data call or if the data truly supports a change in the method for developing presumptive rates for that class of business.

One commenter notes that Class E contains a variety of dealer types, including auto dealers and retail stores, and says that the amount of credit life insurance needed to cover a furniture or jewelry account could be significantly less than the amount financed for a new car.

A commenter notes that Class E includes auto dealers, but that banks, finance companies and credit unions – which are included in different classes -- also make car loans, and the mortality and morbidity of a consumer buying credit insurance through one of these producers should not be different than through an auto dealer. They contend that establishing rates that vary depending on where the credit insurance is purchased is nonsensical and actually discriminatory.

Agency Response: The loss ratios and compensation percentages for Class E differed materially from the loss ratios and compensation percentages for the other credible classes of business (Classes A, B and C). For credit life, the loss ratio and compensation percentage for Class E were 31.41% and 42.7%, respectively. The credit life loss ratio for the other statistically credible classes of business ranged from 52.01% to 53.46%. The credit life compensation percentages for the other statistically credible classes of business ranged from 2.93% to 28.76%. For credit disability, the loss ratio and compensation percentage for Class E were 40.17% and 41.44%, respectively. The loss ratio and compensation percentage for the other statistically credible classes of business were 54.39% and 17.39%, respectively.

Even without the guidance of a specific legal definition for what constitutes a "significant difference" between loss ratios and compensation percentages between the various classes, the substantial differences observed between the loss ratios and compensation percentages in Class E and those in all other classes called for serious consideration of setting different rates by class of business.

It is also not necessary to establish classes on the basis of mortality or morbidity. Insurers that have in the past sought approval of deviations from the presumptive premium rates did not necessarily rely on mortality or morbidity information. Instead, they based their requests on loss ratios and the insurer's profitability relative to specific customer groups in much the same manner that this order establishes separate rates by class of business. The noted difference in loss ratios and compensation percentages is an actuarially sound basis for rate distinctions, and Texas credit insurers have used it to justify different rates for their various customers. Because the basis for the distinction is actuarially sound, factoring it into the setting of presumptive premium rates does not constitute unfair discrimination.

The point that there are a variety of dealers that fit into Class E is true. The department, however, does not have enough reliable data to establish separate rates for subclasses, and none of the other classes include dealers at all. Therefore, the proposal could not refine the rates more specifically.

Comment: One commenter highlights a concern about disparate impact with the following example. A single company has a majority of the auto dealer business in the

state and has a substantially lower loss ratio than other insurance companies classified as auto dealers. The commenter believes this set of circumstances creates an unfair bias against the rest of the auto dealer companies in the presumptive premium rate development.

Agency Response: It is important to note that the commenter has presented a hypothetical scenario, rather than an actual observed phenomenon in the Texas credit insurance market. The department has developed presumptive premium rates that are not confiscatory. There will likely be specific impacts of the presumptive premium rates that affect each credit insurance carrier uniquely. That result is driven, in part, by the unique circumstances of each company. After assessing the impacts of implementing the presumptive premium rates, each company can determine whether to ameliorate perceived problems by adopting an automatic deviation of as much as 30% variation from the presumptive rates, or by seeking specific approval to use rates that deviate even more than 30%.

Comment: Another commenter states that one of the reasons credit life and credit accident and health insurance have been so popular with both borrowers and creditors is the simplicity of the products and their administration, and one of the key elements of that administrative simplicity is the rate structure. The commenter believes that establishing rates by class of business represents a first step toward a rate structure that is more complex and more expensive to administer.

Another commenter states that presumptive premium rates developed by class of business would be unduly burdensome to the industry, in addition to raising the specter of opportunistic litigation or regulatory unfairness. The commenter is concerned that the proposal does not provide a mechanism for determining under what class a particular business may fall. It is left to the discretion of insurers to determine to which class of business a particular program would belong. The commenter believes that the classes of business defined under §3.5002(7) are sufficiently broad that a particular class of business could be classified under multiple categories. For example, a retail store's credit program could be classified under either Class E-Dealer or Class A-Commercial Bank, if a national bank is the creditor of the underlying debt.

Agency Response: The concerns that setting presumptive premium rates by class and plan of business may add slight complexity may be true for some companies, but it should not be a problem for consumers because they don't shop for credit insurance. They simply decide whether or not to purchase whatever credit insurance product is offered by a retail salesperson when the consumer is purchasing a consumer product.

The potential additional costs to insurers of administering a rate structure that includes separate rates by class are associated with the costs that would be incurred to revise the computer systems that the insurers use to track rates and inform business producers (dealers and financial institutions) about the rates. Once the computer revisions are accomplished, the commenter's concerns in this regard should be

resolved. This order establishes January 1, 2006 as the date the new rates will take effect, an ample time for insurers to prepare.

The department does not agree that setting presumptive premium rates by class and plan of business necessarily creates the kind of confusion that will lead to speculative or opportunistic litigation. The classes identified in the rules can be summarized as dealers, financial institutions and others. The classes are determined by the entity that sells the credit insurance product, not the entity that sells the consumer product; thus, dealers should not be confused about whether they are financial institutions.

Comment: A commenter states that rating by class would be unduly burdensome on insurers attempting to administer multiple programs for each class of business, and will be burdensome on the department when reviewing deviations by class for each insurer. In order to alleviate this, the commenter recommends that the department provide a process for insurers to develop rates that are actuarially equivalent to the presumptive rates by class of business. Insurers would develop rates internally, consistent with methods previously filed and approved by the department, and submit an informational filing for the department's review.

Agency Response: Once the computer revisions necessary for implementation of the new rates are accomplished, the commenter's concerns that insurers and the department will encounter undue burdens should be resolved. The insurers in the credit insurance market typically sell other lines of insurance, some of which include multiple

products. Their experience demonstrates that they are capable of accommodating this change without difficulty. The department's experience managing the review and oversight of multiple product offerings also demonstrates that there should not be a problem. The rule sets forth procedures for obtaining approval of rates and deviations, and the department declines to adopt the procedural change suggested by the commenter.

Comment: A commenter stated that having rates that vary by class creates additional expenses for companies that write dealer business and other business and the proposal does not reflect this additional expense. This commenter sees that as a problem because the commenter believes Texas already has one of the nation's lowest presumptive credit accident and health insurance rate structures, but the credit accident and health claim cost is average compared to other states.

Agency Response: Variance should not be an undue burden on any credit insurance company. The department stated in the proposal that the probable economic cost to persons required to comply with the sections will be the possible revenue impacts from the changes in rates and the costs associated with reprogramming to effect the new rates. This includes reprogramming changes that insurers that write dealer business and other business will make. The department has set the effective dates of the new presumptive premium rates with enough lead time to accommodate insurer needs. The companies that write dealer business and other business will possibly encounter more reprogramming costs than companies that sell to only one

class of customers. The actual impact will vary from company to company. The date for effective implementation of these rates is January 1, 2006. That allows sufficient time for credit insurers to modify their business systems, even if they offer a variety of products. The commenter's concern about the Texas credit insurance rate structure and claim cost should be improved by instituting separate rates by class, because the classes with higher costs should have the higher rates. The presumptive rate structure will more closely mirror actual industry circumstances.

Comment: Another commenter supports adoption of Alternative 1, stating that there are sufficient credible consistent differences between Class E and the other classes of business to justify different rates. The commenter disagrees with the argument that the use of class rating would be too confusing, and points out that widespread use of computers makes it just as simple to have multiple class rates as only one class rate. The commenter also points out that for some lines of insurance, such as private passenger automobile insurance, there are thousands of possible different class rates, which has not presented a problem. The commenter believes that the objection that separate class rates would cause confusion among consumers is a much more hypothetical concern than a reality because consumers very rarely shop for credit insurance, which is sold concurrently with the purchased consumer product. The commenter also points out that the use of deviations will mean that rates between sellers of credit insurance will vary anyway. The commenter also contends that if the credit insurance rates are not set by class, it is likely that some classes of business for

which that one uniform rate is too low will use higher rates, while those for whom that rate is too high will not use lower rates. This will lead to an unbalanced situation where consumers are being charged overall premiums that are excessive and confiscatory. The commenter concludes that it is completely consistent with actuarial and regulatory principles to use credit insurance rates that vary by class of business.

Another commenter believes that the potential of a "low cost" class of business subsidizing a "high cost" class is the strongest reason to support rates by class of business if one believes that the differential in income between different classes of producers should be small. The rates by class would then lead to rates that more closely reflect the level of claims actually being produced by borrowers who purchase coverage through the respective classes. The commenter believes that if separate rates by class of business are to be adopted, it is appropriate to look for the largest possible reasonably homogeneous groupings of claim cost, as was done in the proposal.

A commenter who supports varying rates by business class observes that the proposed rate difference for credit disability is small enough that it would not be worth much extra administrative cost to maintain the separation, but the proposed rate difference for credit life is material. The commenter goes on to say that if maintaining separate presumptive rates for one of the two coverages causes the administrative cost to be incurred and the second product does not add much cost, it would make sense to use separate rates for both credit disability and credit life.

Agency Response: The department agrees with the observations of these commenters and notes that their observations are responsive to some of the comments that precede them in this order.

Comment: A commenter argues that, just as the claims experience for Class E is significantly different than for other classes, the claims experience for single premium and monthly outstanding balance (MOB) business are significantly different. This commenter believes that the same logic that dictates separate rates for Class E versus other classes should apply to single premium versus MOB products. That is, plans and classes of business with significantly different claims experience warrant different presumptive premium rates. The commenter believes that the proposal has incorrectly ignored the substantially different claims experience for single premium credit life and MOB credit life.

Agency Response: The department agrees that the same logic that dictates separate rates for Class E versus other classes should apply to single premium versus MOB products. The proposal did not ignore the different claims experience for single premium credit life and MOB credit life. Exhibits 15-2 and 15-3 in the Milliman report identify the loss ratios for single premium business and for MOB business. The difference between the losses experienced by those plans of business was taken into account and this data was relied upon in the proposal and in this order.

Comment: A commenter asks that the department confirm that an insurer that files rates or has rates on file that are equivalent to the presumptive rates shown in

§3.5206 of this rule, to the extent adjusted pursuant to §3.5202 of this rule, may use those rates without further proof of their reasonableness. The commenter believes such a provision would allow for insurers to comply with the presumptive premium rate in a more timely manner and alleviate the department's burden in approving rate filings.

Agency Response: The department cannot comply with the request. Pursuant to §1153.102, insurers must submit new filings to demonstrate that their rates are in compliance with the new rule requirements.

THE JOINT LIFE MULTIPLIER

Comment: A commenter complains that the joint life loss ratio is only 143%, but the proposal concluded that the 150% joint multiplier remains appropriate – without any analysis or explanation. The commenter also complains that the proposal employs a strict component rating analysis to establish single life rates but for joint life rates the component rating analysis is not used. The commenter explains that this is an example of the proposal departing from its stated procedure when it benefits insurers and agents and harms consumers.

A commenter recommends that the joint life multiplier should be 125%. The commenter assumes that claim costs are 50% of single life rates. Thus, the claim costs per dollar of premium for joint life would be 143% of 50 cents, or 72 cents. By adding 50 cents of non-claim expenses, the result is a multiplier of approximately 125%. The commenter acknowledges that this is not a precise calculation because some non-claim

expenses vary with claim costs, but contends that this example makes it clear that a component rating analysis for joint life will produce a significantly lower joint life multiplier than 150%.

Another commenter states that the joint life multiplier of 1.5 is low and asserts that industry studies have shown the need for a multiplier in the range of 1.6 to 1.75.

A commenter believes that claims are frequently reported incorrectly, especially with regard to life claims being reported as a single life claim or a joint life claim. For this reason, the commenter believes that comparison of losses between single life and joint life from reported data should always be viewed with caution. Rather than rely on reported data, the commenter prefers a theoretical approach, and recommends a joint life multiplier for credit life of 165%.

The commenter also claims to have seen experience and heard from other industry actuaries that the proper multiple for credit disability may be greater than 200%, and recommends a joint life multiplier for credit disability of 175%.

Agency Response: The joint coverage mortality cost averaged 143% of the single coverage mortality cost during 2000-2002, based on industry data. The experience fluctuates considerably. The ratio was 125% in 2000, 157% in 2001 and 150% in 2002. Historically, the department has used 150% and the history of fluctuation in these three years justifies not lowering it to 143%, just because of the average. This experience also does not justify lowering it to 125%. The experience generally hovers around 150%, and in some years it exceeds that percentage by just a

few points, while in other years it is a few points less than 150%. Accordingly, the department believes that a multiplier of 150% is reasonable.

Comment: Another commenter states that the definition of average lives is unclear.

Agency Response: There is no definition for “average lives.” The definition for “average number of life years” has been in this subchapter for years. The proposal moved the definition to a different section but did not include the language of the definition. Because of the comment, the department reviewed the definition and could not discern what makes the definition unclear to the commenter. Therefore, it will not be changed.

ADJUSTMENT TO PRIMA FACIE PREMIUMS AND LOSS RATIOS

Comment: A commenter believes that certain patterns of earned premiums relative to prima facie premiums and losses incurred suggest that consistent and appropriate adjustments were not made to the actual earned premiums to produce the presumptive premium rate equivalent. The commenter constructs a simple model to approximate the potential claim cost understatement. The model concludes that prima facie earned premiums are overstated by approximately 11% for the period 2000-2002. The commenter believes that this adjustment is further supported by the following analysis. The proposal calculated the single life decreasing term claim cost per $100 per year from the losses incurred and the mean insurance in force. This value is .1187.

The single life decreasing term loss ratio for the 2000-2002 period is 36.47%. Applying that ratio to the 36-month prima facie rate of .281 (per $100 per year) yields .1025. The claim cost based on the mean insurance in force is approximately 15.8% greater than the claim cost based on the loss ratio times the prima facie rate. The commenter believes this demonstrates that the 11% adjustment is appropriate.

Agency Response: As previously noted, insurers provided the data relied upon to derive the presumptive premium rates in the credit insurance data call, and certified the data they submitted as accurate. The data was rigorously reviewed by department staff and Milliman. At the end of that review, the department had no reason to reject or question the data. The model constructed by the commenter included certain key simplifying assumptions that the department questions. For example, the commenter assumed that no company with policies issued in 1999 and prior years correctly reported premiums at presumptive rates (PEP) on those policies during the 2000-2002 experience period at the $.30 rate in effect during that period, but instead reported it at the $.36 rate in effect when those policies were issued. The commenter also assumed that all policies are written for a term of 36 months even though it is clear that policies are written for other terms. In the final analysis, the department believes it is more reasonable to rely on the actual data rather than the modeled scenario offered by the commenter.

PROFIT AND CONTINGENCY MARGIN

Comment: One commenter calculates profit and contingency margins based on asset share methods with target surplus, contending that this is the only appropriate method appropriate for multi-year contracts involving significant surplus strain.

Agency Response: An appropriate methodology for calculating profit and contingency margins, including cases with multi-year contracts where significant surplus strain is involved, must include several factors. Consideration of a target return on equity (ROE) acknowledges that insurance companies must make more profit than they could make if they simply invested their money instead of underwriting the risk of others. Thus it follows that there must be a reasonable estimate of net investment income derived from equity and, to assure sufficient reserves if underwriting results are not favorable, an appropriate premium to equity ratio. The department acknowledges that the asset share method takes these factors into consideration, but the proposal does as well. Accordingly, the proposal's approach to determining the profit and contingency margin component and the asset share approach preferred by the commenter are both actuarially sound methods. The method used in the proposal is also consistent with the method used in the 2000 rate order.

Comment: A commenter argues that there is a serious fallacy in using the ROE calculation used in the proposal and the 2000 rate order. The commenter believes that surplus strain associated with issuing new single premium credit insurance business can easily exceed 50% of the single premium. The commenter notes that the cost of this surplus can vary by insurance company, but is generally equal to the required ROE.

Thus, if a carrier has a 15% pre-tax cost of capital and a 3.5% investment return, there is an 11.5% gap that must be recovered from underwriting gains. Also, the commenter has observed that some analyses have alleged that the profit formula should be reduced by "investment income on reserves." The commenter disagrees and responds that since a large portion of the reserves represent borrowed surplus, most companies have a significant cost of maintaining reserves not reflected in these ROE analyses.

Agency Response: The premium to equity ratio of 2.0 used in the development of the profit margin component of the rating formula recognizes that surplus strain on single premium business may require additional commitments of equity by the insurer. Because surplus strain is taken into consideration in the premium to equity ratio, the ROE calculation used to derive the profit component is appropriate and reasonable.

Comment: Another commenter observes that for the target after-tax ROE, the proposal uses a value of 12.0%. The commenter believes that this is an excessive value without reasonable support. The commenter conducted an analysis which indicated that an appropriate after-tax ROE is 9.7%. The commenter also points out that the most recent department decision on the cost of capital issue was in the Texas title insurance biennial rate hearing where the commissioner found 10.5% to be a reasonable cost of capital. The commenter believes that the recommendation in this proposal for the 12% after-tax cost of capital is unscientific and unreliable and appears to be based totally upon the rate of return that insurance companies want to earn, which will lead to an excessive profit provision.

Agency Response: To evaluate an assumption for a ROE, the department reviewed the annual statement and Best Reports of five major carriers in the credit insurance market.. The effective tax rate of these carriers fluctuated between 24% and 43%.

To properly compare the ROE recommendations of commenters and the department, it is important to use the same effective tax rate for each recommendation. The commenter's reference to the proposal's use of a 12% after-tax ROE fails to acknowledge that the effective tax rate yielding that result is 20%. This cannot fairly be compared to the commenter's ROE recommendation of 9.7%, because the effective tax rate yielding that result is 25%.

The proposal included the statement that "for comparison purposes, a 15% pre-tax rate of return is equivalent to a 12% after-tax rate of return with a 20% effective tax rate, or to a 10.5% after-tax rate of return with a 30% effective tax rate." This 10.5% is the same cost of capital that the commenter argues should be used because the commissioner found it reasonable in the most recent title insurance rate case.

Only two commenters provided ROE recommendations, one who does not represent credit insurers, and one whose recommendation was adopted by several credit insurers. At a 25% effective tax rate, the non-insurer commenter's recommendation for ROE was 9.7%. This calculates to a 12.93% before-tax ROE. The insurer recommendation for after-tax ROE was 11.5%, which is the same rate adopted by the commissioner in the 2000 rate order. At a 25% effective tax rate, this calculates

to a before-tax ROE of 15.3%. The proposal's recommendation of 10.5% after-tax ROE, at a 25% effective tax rate, calculates to a before-tax ROE of 14.0%. At an effective tax rate of 30%, the non-insurer recommendation is a 13.85% ROE and the insurer recommendation is 16.42% The proposal's recommendation is 15.0%. At an effective tax rate of 35%, the non-insurer recommendation is a 14.9% ROE and the insurer recommendation is 17.69% The proposal's recommendation is 16.15%.

At all these tax rates, the proposal's recommendation falls very close to the midpoint between the non-insurer and insurer recommendations. The department did not make its proposal with that objective, but these numbers indicate that the ROE recommendation in the proposal is reasonable.

DISCOUNT FACTOR

Comment: A commenter addresses the conclusion in the proposal that the investment income on reserves should be 0.0% because single premium rates are currently discounted for interest and because the investment income in MOB business is negligible. The commenter believes that this approach is correct only if two conditions are met: (i) the premiums at current presumptive rates used in the rate calculation were appropriately adjusted for the discounting of single premium business and (ii) the interest rate used to discount single premium business in the future is appropriate. The commenter believes there are serious concerns with regard to whether or not the first of these assumptions is satisfied. The commenter notes that the

proposal states that in the data call, the earned PEP were subject to, potentially, the greatest misstatement. Because when current presumptive premium rates were set, two factors were utilized that could have caused confusion in the reporting of the PEP, one of which was the implementation of a discount factor. With regard to the second assumption, the commenter believes the 3.5% interest rate proposed to discount single premium rates is significantly lower than the actual return that can be expected by insurance companies.

Another commenter agrees with the component rating formula in the proposal, observing that this method was used in the 2000 rate order setting the current presumptive premium rates. This commenter agrees that the absence of an interest component in the denominator of the formula is appropriate because the result of the calculation is discounted to reflect the timing differences of receipt of the premiums.

A commenter believes that the discounting of single premiums at interest is not appropriate, based on his perspective of the standpoint of equity between policyholders. Only the policyholder may cancel single premium contract. The insurer is bound to continue coverage. The commenter believes this factor increases the risk of cumulative anti-selection, which he asserts is true of many other guaranteed renewable coverages. Conversely, in MOB plans, the insurer usually retains the right to cancel coverage upon 30 days notice. In addition, whether the risk is life or disability, the commenter believes the yearly increase in expected claim costs more than offsets any potential interest discount. The commenter believes that if the interest discount concept remains, the

interest should be reduced to the 3.5% that was included in the proposal. The commenter believes that the discount should not be higher for disability coverage. He contends that a "mortality discount" is not appropriate on single premium credit disability insurance, because when an insured dies, the disability contract is cancelled and the disability premium is refunded. Thus, there is no need for a "mortality discount."

A commenter observes that the department's proposal applies different discounts for credit life premiums (4.5%) versus credit accident and health premiums (5.63%) and believes that part of the proposal is without any reasoned justification or other explanation.

A commenter believes that the application of discount factors to the proposed premium presumptive rates duplicates discounts already used in the ratemaking process. The proposal uses a 3.5% discounted internal rate of return which the commenter believes already accounts for earned investment income on surplus. The commenter believes that to apply an additional discount factor to the presumptive premium rates unreasonably duplicates a discount and recommends that the use of discounts applied to the presumptive premium rates should be eliminated.

A commenter believes that the use of a 3.5% interest rate to discount the single premium credit insurance rates is a reduction from the interest rates currently used to discount single premium credit insurance rates of 4.5% for credit life insurance and 5.63% for credit accident and health insurance and characterizes this as a "hidden" rate increase.

A commenter states that the 3.5% interest rate included in the proposal is too low and does not reflect the actual expected investment results of insurance companies and contends this will result in excessive credit insurance premiums.

A commenter recommends that the department use a 7% interest rate to discount the rates for single premium business to the extent that the manual rates do not fully reflect investment income.

Agency Response: The credit life insurance presumptive premium rates recommended in the proposal were developed independent of the presumptive earned premiums reported for the experience period. Therefore, any misreporting of the presumptive earned premiums would not have affected the recommended credit life presumptive premium rates. Any misreporting of premiums by the companies might, however, have affected the recommended presumptive premium rates for credit accident and health if it actually occurred. Since the department has no indication of misreporting of the data, however, any adjustment we would attempt to make would be purely arbitrary. As noted previously, the department and Milliman engaged in a rigorous review of the credit data call submissions prior to utilizing that data to set the presumptive premium rates. The department found no reason to question the data. Furthermore and perhaps most significantly, as of this date, some eighteen months after the reporting of the data to the department, no company has stepped forward to suggest that they now believe their data reporting was in error.

The discounts applied by the department's proposal are 3.5% for both the credit life premiums and the credit accident and health premiums. This follows from the determination that 3.5% is the appropriate value to use for investment income. The reasoning that led to that conclusion has already been explained in response to comments about investment income.

The department respectfully disagrees with the commenter that believes the discounting of single premiums at interest is not appropriate. A consumer that pays a single premium for coverage at the inception of the policy loses the time value of that money. Application of the discount rate offsets this loss to the consumer and effectively lowers the amount an insurer receives for investment.

CLAIM COST

Comment: A commenter believes that the department should calculate a rate for a central type of coverage, such as single premium single life decreasing term, and then use existing and theoretical relationships to develop the other rates. The commenter contends that in calculating the central coverage type, it is most appropriate to use the claim experience of as broad a spectrum of coverage as possible. This would avoid anomalies, such as basing a rate on experience that does not include the experience under that type of coverage. In calculating the base rate for single premium single life decreasing term, the commenter used the adjusted loss ratio for the entire credit life line of business. The overall three-year prima facie loss ratio for credit life

was 41.91%. The commenter adjusted the loss ratio because he believes misreporting of premiums is common, and got 46.64%, which produced a claim cost of 13.11 cents per $100 per year. The commenter contends that the method used in the proposal erroneously used only the single premium single life decreasing term experience, but should have used the ratio of losses to mean insurance in force to arrive at the claim cost component.

For the claim cost component for credit disability, the commenter believes that the 14-day retroactive plan at an appropriate term is the best choice for the central coverage type. A percentage or other appropriate adjustment can then be applied across terms, elimination periods and premium types. In calculating the base rate for single premium disability 14-day retroactive coverage, the commenter used the adjusted loss ratio for the entire credit disability line of business. The overall three-year prima facie loss ratio for credit disability was 48.08%. He adjusted the loss ratio because he believes misreporting of premiums is common, and got 53.16%, which produced a claim cost of $1.368 per $100 for the three-year plan. The commenter argues that the proposal erroneously used only the 14-day retroactive experience, but should have used adjusted overall loss ratios to develop the claim cost component.

Agency Response: In developing the claim cost component of the presumptive premium rates, the department used claims experience in the plans that have the largest volume of business in force. This approach uses a homogeneous group of credit insurance consumers and is consistent with the method used in prior rate

decisions. The approach derives the claim cost component for other plans by applying a factor to the largest volume plan to represent the actuarial value of the coverage differential between the various plans. This method gives reasonable results, is actuarially sound, and is a generally accepted industry practice. Some plans may have a different composition of credit insurance consumers, with age and gender characteristics that differ from the largest volume plan. The department has historically refrained from varying presumptive premium rates in credit insurance because of the age and gender of the insured. To the extent that an individual company's composition of credit insurance customers in a specific plan causes the actual experience in the plan to vary materially from that assumed in the presumptive rate development, a rate deviation solution is available to the company. The commenter's approach, while somewhat different, is also a reasonable approach to developing the claim cost component. But since the other components of the rate (commissions, general expenses, and profit and contingency margin) also represent common assumptions for all plans, it is not necessary to use the commenter's approach in order to develop reasonable presumptive premium rates.

INTEREST

Comment: A commenter agrees with the treatment of interest used in the proposal.

Agency Response: The department appreciates the comment.

COMMISSION COMPONENT

Comment: One commenter believes that the commission component should reflect the level of compensation actually paid to producers. The commenter argues that credit insurance competes with other products for "shelf space" in the producer's fee income sources. If an alternate product, or offering no product at all, is more attractive to the producer, credit insurance will simply not be offered. Another commenter disagrees that the proposed commission component of 25% is inadequate, contending that the average commission paid for all classes exceeds that amount. The commenter reasons that a presumptive rate with a commission component less than average would be inadequate for some insurers, agents or both in violation of Insurance Code §1153.103(f). Further, the commenter points out that, pursuant to Insurance Code §1153.103(e), the Commissioner may not set a presumptive premium rate that sets or limits the amount of compensation paid to an agent. Another commenter states that by setting the commission component well below the average, the new proposed presumptive rate could require insurers or agents to have commissions set or limited. This commenter believes that problem is exacerbated if the order adopts Alternative 1, under which separate rates for Class E have the same commission component as all other classes. The commenter asserts that the average amount actually reported and paid for Class E is over 45%, whereas the actual amount reported and paid for credit unions and savings institutions is significantly less than 25%.

Agency Response: As previously noted in this order, and well-documented historically, reverse competition exists in the credit insurance market through producer commissions. For that reason, the department believes it would be unreasonable to set the commission component in the higher range of actual commissions paid by some companies. The statute specifies that reasonable acquisition costs are only one component of the presumptive rate. The value of 25% is in the lower range of actual commissions reported by carriers, and is more reasonable. It is also the same value used for the commission component in the 2000 rate order. The use of 25% as the value for the commission component does not, however, prevent any company from paying higher or lower commissions as it sees fit. Therefore, this rate order does not set or limit the amount of compensation actually paid to a company or agent, and does not violate the prohibition found at Insurance Code §1153.103(e).

Comment: A commenter points out that Insurance Code §1153.103(d) enumerates various types of data which the Commissioner must consider in determining the presumptive premium rate. The commenter notes that the claims cost component and the general expense component in the proposal were based upon data submitted by insurers through the data calls, but believes that the commission component was not. The commenter believes that the proposal ignored the compensation data provided by insurers which would violate the Commissioner's statutory obligation to consider all relevant data and the statutory prohibition against attempting to set or limit commissions. The data requested from and provided by

insurers regarding commissions indicates that, on average, commission levels are around 40% for both credit life insurance and credit accident and health insurance.

A different commenter states that continued use of a 25% commission component in the current presumptive premium rates fails to reflect that credit insurance companies now have the ability to receive an automatic 30% upward deviation from the presumptive premium rates, which was not available at the time of the 2000 rate order. The commenter believes that it is appropriate to use a provision for commissions lower than the value that was used when the automatic upward deviation was not available, and suggests the use of a value of no more than 20%.

Agency Response: The department did consider actual data submitted regarding commissions paid by credit insurance companies, and determined that because of the effect of reverse competition that was discussed previously, 25% is a reasonable value to use for the commission component, which is in the lower range of commission payments reported by credit insurance companies.

The department does not believe it is appropriate, however, to reduce the commissions component because of the automatic upward rate deviations allowed by Insurance Code §1153.105. As noted previously, the regulatory scheme established by Chapter 1153 of the Insurance Code requires the commissioner to set the presumptive premium rates based on the information required by §1153.103(d). Thereafter, insurers may use deviated rates if they follow the required procedures. Reducing the calculated

presumptive rates or any individual component by a factor of 1/1.3 because of allowable rate deviations would be inconsistent with the intent of the law.

MINIMUM PREMIUM

Comment: Several commenters recommend that the order establish minimum premiums and refunds. One commenter observes that, in recent times consumers have begun to finance smaller purchases, which has resulted in significantly smaller initial credit insurance face amounts (many less than $1,000) and smaller premiums per policy with no reduction in per-policy administration costs to the producer and the insurer. The commenter recommends that the commissioner establish a minimum premium of $10.00 per policy and a minimum policy refund upon policy cancellation of $5.00 to assist in defraying the increasing policy administration costs associated with smaller face amount policies.

A commenter points out that banks incur the following costs in managing their credit insurance business: personnel time in taking applications, explaining policies and assuring that documents are completed correctly for Truth-In-Lending as well as Gramm-Leach-Bliley and state law disclosure; data processing entry; per-loan costs to data processors if the institution uses outside processors; postage and supplies relating to transmitting certain documents including certification to carriers and policy delivery to customers as appropriate; compliance costs including licensing of the institution as a special agent, and ongoing training of employee. In reviewing community bank

activities with a credit insurance carrier, the commenter learned that approximately 45% of community banks credit insurance premiums are under $10.00. These commenters believe the imposition of minimum premiums and refunds will not unduly burden consumers, and will reduce the amount of money insurers are currently losing by accepting small premium policies and certificates.

Agency Response: The proposal made no mention of minimum premiums or refunds. The department believes that it would be outside the scope of the notice provided by the proposal to make these changes in the rules.

§3.5608: A commenter disagrees with this section's requirement for annual review of approved deviated rates, arguing that a three year approval period is more appropriate. The commenter believes that rates will be "kept in line" by the expiration of deviations every three years, noting that in states with a shorter approval period there is more fluctuation of rates rather than a trending over time. The commenter also believes that a shorter period would create extra costs for filers and the department with no corresponding public benefit.

Agency Response: The timeframes in §§3.5607 and 3.5608 are longstanding and this proposal made no mention of changing them. Therefore, the department declines to change them. The commenter's interest is noted and the department will maintain awareness of the issue as the new rates are implemented.

Comment: Some commenters believe that the proposed effective date of March 1, 2005 does not allow the time required for filing and system conversion.

Agency Response: This order establishes an effective date of January 1, 2006, which should allow sufficient time for the industry to make the business process changes necessary to achieve timely compliance.

5. FINDINGS AND CONCLUSIONS REQUIRED BY INSURANCE CODE §1153.103(c). The following Findings are made, as required by Insurance Code §1153.102(c).

GENERAL PROCEDURE

1) On June 1, 2004, the department published credit life and credit accident and health statistical data for the years 2000, 2001, and 2002 and solicited rate proposals from interested persons.

2) The department's contractor, Milliman, reviewed the submissions and prepared a rate assessment and recommendation based on that information and the published statistical data.

3) The department made the report prepared by Milliman, rate recommendations from interested parties, information responsive to inquiries about staff's recommendation, and statistical data for 2000–2002 were made available to the public on the department's web site, along with comments on the proposed rule. Interested persons could also request a copy of this

information by contacting the Life/Health Division at 512-322-3401 or lifehealth@tdi.state.tx.us.

4) A proposal for the amendment of presumptive premium rates for credit life plans and credit accident and health plans was published in the Texas Register on November 12, 2004.

5) The department held two informal meetings to discuss the procedure that would be followed at the public hearing and invited known interested parties to attend.

6) The Commissioner of Insurance conducted a public hearing to receive public comments on the proposal on January 6, 2005.

REVERSE COMPETITION

7) There is reverse competition in the credit insurance industry.

8) Reverse competition in the credit insurance market means that insurers direct their competitive efforts at the producers of insurance business rather than at the ultimate consumers of credit insurance.

9) Reverse competition in the credit insurance market raises credit insurance rates consumers pay, without adding benefits, because it forces insurers to pay higher acquisition costs (i.e; commissions) to producers in order to attract more business.

GENERAL RATEMAKING

Classes of Business

10) The following classes of business exist in the credit life insurance and credit accident and health insurance market:

Class A--Commercial banks, savings and loan associations and mortgage companies;

Class B--Finance companies and small loan companies;

Class C--Credit unions;

Class D--Production credit associations (agriculture and horticulture P.C.A.s);

Class E--Dealers (including auto and truck, other dealers, and retail stores); and

Class F--All others not included in classes A through E.

ALTERNATIVE 1 VS. ALTERNATIVE 2

11) In reviewing industry expense and experience data supplied in response to the data call, the department observed that the loss ratios and compensation percentages for one class, Class E--Dealers, were significantly different than the other classes in both credit life plans and credit accident and health plans. This disparity established a basis for distinguishing between Class E and all other classes of business.

12) The department published for comment two alternatives. Alternative 1 established a presumptive premium rate for Class E alone, with a different presumptive premium rate for all classes other than Class E. Alternative 2 established a composite presumptive premium rate for all classes of business combined. The department specifically invited comments on the alternatives as well as on which alternative to adopt.

13) After consideration of all available information, including comments from the public, it is reasonable to adopt Alternative 1, establishing presumptive premium rates for credit life insurance and credit accident and health insurance based on plan and class of business.

COMPONENT RATING FORMULA

14) The proposed presumptive premium rates for both credit life insurance and credit accident and health insurance were developed using a method known as the component rating methodology. Component rating considers each element of income and expense and builds the premium rate as a combination of the components.

15) The components utilized in developing the presumptive premium rates were claims cost, general insurance expenses, investment income, premium taxes and fees, commissions, and profit.

16) The formula used to develop a premium rate for both credit life plans and credit accident and health plans, using the component rating method, is: Component Rate = (claims cost + general insurance expenses)/(1 + investment income – premium taxes and fees – commissions – profit).

COMPONENTS IN THE DENOMINATOR OF THE FORMULA

17) The values for the components in the denominator of the formula are the same for credit life plans and credit accident and health plans.

18) An annual earning rate of 3.5% is reasonable for the investment income component. This rate is based on review of past and current yield for U.S. Treasury and corporate bonds with durations of less than five years.

19) Investment income is excluded from this proposal because single premium rates are currently discounted for interest in the presumptive premium rate calculation formula and because the investment income in outstanding balance business is negligible.

20) A percentage of 2.75% is a reasonable value to use as the component for state premium taxes, licenses, fees and other assessments. The commissioner used this same value in his 2000 rate order. Insurance Code Chapter 222 requires insurers selling life insurance to pay taxes at a rate of one-half of 1.75% on the first $450,000 of gross premiums and 1.75% on gross premiums above that amount.

21) It is reasonable to use a value of 25% for the commissions component. This is unchanged from the assumption the commissioner used in the 2000 rate order.

22) The commission component does not fix or limit the amount an insurer may pay in commissions.

23) It is reasonable to use a value of 5.75% of premium for the profit component. This factor is calculated as follows: (target before-tax return on equity (15%) minus net investment income on equity (3.5%)) divided by the premium to equity ratio of 2.0.

24) The overall target return on equity of 15% used in the profit component calculation is equivalent to a 10.5% after-tax rate of return with a 30% effective tax rate. This is very nearly midway between the return on equity recommendations provided by representatives of the credit insurance industry and representatives of credit insurance consumers.

25) The premium to equity ratio of 2.0 used in the calculation of the profit component is an assumption that reflects surplus targets for the industry, driven in part by risk-based capital requirements, along with recognition that surplus strain on single premium business may require additional commitments of equity by the insurance carrier. The commissioner also used a ratio of 2.0 in the profit margin calculation in the last presumptive premium rate order.

COMPONENTS IN THE NUMERATOR OF THE COMPONENT RATING FORMULA FOR CREDIT LIFE

Plans of Benefits for Credit Life Insurance

26) The following Plans of Benefits exist in the Credit Life Insurance market:

Plan 1 Single Premium, Reducing Coverage, Single Life

Plan 2 Single Premium, Level Coverage, Single Life

Plan 3 Outstanding Balance, Revolving Loan, Single Life

Plan 4 Outstanding Balance, Other, Single Life

Plan 5 Single Premium, Reducing Coverage, Joint Life

Plan 6 Single Premium, Level Coverage, Joint Life

Plan 7 Outstanding Balance, Revolving Loan, Joint Life

Plan 8 Outstanding Balance, Other, Joint Life.

Claim Costs

27) The department initially attempted to calculate presumptive premium rates for credit life plans using actual claims cost experience information plan by plan. However, some plans had an insufficient volume of business to provide reliable data for rate setting purposes. In addition, the actual claim

experience by plan does not reflect the actuarial value of the coverage and benefit differences by plan.

28) For credit life plans, the claims cost component represents the annual mortality costs based on experience data for the years 2000, 2001 and 2002. This data was submitted by carriers through the department's annual credit data call.

29) The establishment of the credit life claims component relies on the claims experience in Plan 1, which contains over 50% of all credit life earned premium during the experience period, to develop a presumptive premium rate for that plan. The presumptive premium rates for all other credit life plans use the rate relationships below, which reasonably represent the actuarial value of the coverage and benefit differences in each plan.

$$SP_n = ((n \times (n+1))/2n^2) \times (12/10) \times Op = ((12 \times (n + 1))/20n) \times Op$$

And, for level term insurance on single lives:

$$LT_n = (12/10) \times Op$$

where,

SP_n = Single premium rate per year of coverage per $100 of initial decreasing indebtedness repayable in "n" equal monthly installments.

LT_n = Single premium rate per year of coverage per $100 of level life insurance where the indebtedness remains level during the term of the coverage and is repayable in a single sum at the end of the term.

Op = Monthly outstanding balance premium rate per $1,000 of insured indebtedness.

n = Original repayment period, in months; assumed to be twenty-four months.

30) It is reasonable to use claims cost components of .1048 for Class E alone and .1558 for all classes except Class E in determining the presumptive premium rates for Alternative 1 credit life plans.

General Insurance Expense

31) For credit life plans, the general insurance expenses were estimated using information reported by the companies in the annual credit data calls summary expense report. The percentage ratio of the mean Texas certificates in force to the mean nationwide certificates in force was calculated for the years 2000, 2001 and 2002. This percentage was then multiplied by the total of all expense items to produce an estimate of the Texas expenses for all plans for each year. The estimated Texas expenses were then divided by the total presumptive earned premium to develop Texas expenses as a percentage of presumptive earned premiums. Estimated annual expenses per plan were determined by applying that percentage to the presumptive earned premiums by plan. The annual plan expense costs per $1,000 were then calculated by dividing the estimated annual expenses per plan by the

plan mean insurance in force, which were then converted to expense per plan.

32) A significant change from previous studies appeared in the ratio of Texas estimated expenses to presumptive earned premium. That ratio dropped from the 20 - 21% range for studies over the six years prior to the current study period to 14% for 2000 through 2002. Because of the significant difference in this number from one observation period to the next, this value for this component was proposed to be determined by using a weighted average expense ratio, applying a 25% weight to the current study period data and a 75% weight to the prior study period. As a result, the general insurance expense component used in the proposal for a new presumptive premium rate for credit life was .0642.

33) Commenters questioned the use of the weighted average expense ratio approach. Some questioned the proposal's reasoning for weighting the more recent expense data at 25% and weighting the older data at 75%. Some recommended giving 100% weight to the expense data for the years 2000-2002. Others recommended giving no weight at all to the data for those years.

34) Department staff carefully reviewed the data submitted in response to the credit data calls and found no reason to discard the data. At the same time,

the drastic difference from one observation period to the next is without certain explanation.

35) A reasonable way to reconcile these concerns is to average the expense information reported in credit data calls for the six years immediately preceding this proceeding. That calculation yields a general insurance expense component of .0580 for credit life, which is reasonable.

COMPONENTS IN THE NUMERATOR OF THE COMPONENT RATING FORMULA FOR CREDIT ACCIDENT AND HEALTH

Plans of Benefits for Credit Accident and Health Insurance

36) The following Plans of Benefits exist in the Credit Accident and Health Insurance market:

Plan 10 Single Premium 14-day Retroactive

Plan 11 Single Premium 30-day Retroactive

Plan 12 Single Premium 14-day Non-Retroactive

Plan 13 Single Premium 30-day Non-Retroactive

Plan 14 Single Premium 30-day Non Retroactive

Plan 16 Outstanding Balance Revolving 14-day Retroactive

Plan 17 Outstanding Balance Revolving 30-day Retroactive

Plan 18 Outstanding Balance Revolving 14-day Non-Retroactive

Plan 19 Outstanding Balance Revolving 30-day Non-Retroactive

Plan 22 Outstanding Balance Other 14-day Retroactive

Plan 23 Outstanding Balance Other 30-day Retroactive

Plan 24 Outstanding Balance Other 14-day Non-Retroactive

Plan 25 Outstanding Balance Other 30-day Non-Retroactive

Plan 26 Outstanding Balance Other 90-day Non-Retroactive.

Claim Costs

37) Experience pertinent to credit accident and health plans presented the same problem identified in Finding 27. Therefore, the department relied on the claims experience in Plans 10 and 17 for credit accident and health to develop presumptive premium rats for those plans. The presumptive premium rates established for Plans 10 and 17 are the starting points for establishing the presumptive premium rates for all other credit accident and health plans.

38) For credit accident and health plans, the claims cost component was calculated as the ratio of incurred claims to presumptive premiums multiplied by the current presumptive premium rate.

39) The Plan 10 percentages of the current presumptive premium rates were applied to the current presumptive premium rate schedule to determine the recommended presumptive premium rates for Class E alone and all classes

except Class E for all single life, single premium plans and all outstanding balance other plans. The Plan 17 percentages were used for all single life, outstanding balance revolving account plans.

40) It is reasonable to use claims cost components of 1.1480 (Plan 10) and .5130 (Plan 17) for Class E alone in determining the Alternative 1 presumptive premium rates for credit accident and health plans.

41) It is reasonable to use claims cost components of 1.6886 (Plan 10) and .6034 (Plan 17) for all classes except Class E in determining the Alternative 1 presumptive premium rates for credit accident and health plans.

General Insurance Expense

42) For credit accident and health plans, general insurance expense was determined by multiplying the ratio of total general insurance expense to presumptive earned premium by the current presumptive premium rate. As in credit life, there was an inconsistency between the general insurance expense calculated using the 2000-2002 data and general insurance expense using the experience data reported for 1997-1999. As a result, a weighted average component was calculated in the proposal for new presumptive premium rates using a weight of 25% for 2000-2002 experience data and a weight of 75% for the 1997-1999 experience data. The general insurance

expense component for credit accident and health using that calculation was .5501 (Plan 10) and .2918 (Plan 17).

43) Commenters questioned the use of the weighted average expense ratio approach. Some questioned the proposal's reasoning for weighting the more recent expense data at 25% and weighting the older data at 75%. Some recommended giving 100% weight to the expense data for the years 2000-2002. Others recommended giving no weight at all to the data for those years.

44) Department staff carefully reviewed the data submitted in response to the credit data calls and found no reason to discard the data. At the same time, the drastic difference from one observation period to the next is without certain explanation.

45) A reasonable way to reconcile these concerns is to average the expense information reported in credit data calls for the six years immediately preceding this proceeding. That calculation yields a general insurance expense component for credit accident and health of .5111 (Plan 10) and .2711 (Plan 17).

JOINT COVERAGES

46) It is reasonable to establish presumptive premium rates for both credit life insurance and credit accident and health insurance coverages on joint lives at

150% of the corresponding single life presumptive premium rates. A comparison of the experience for single life and joint life rates was made by type of plan. While there was variability within the plan sub-groups, the overall ratio of the annual claims cost of joint life to single life business is 1.434 (143.4%) for the years 2000-2002. This result confirms the reasonableness of the use of the 150% multiplier for joint credit life rates.

DISCOUNT FACTOR

47) It is reasonable to use a discount rate of 3.5%. This rate is based on a review of the past and current yield for U.S. Treasury and corporate bonds with durations of less than five years.

LOSS RATIOS/ REASONABLENESS TEST

48) The department proposed loss ratios to serve as a test of reasonableness of the relationship of benefits for applications that seek approval of deviations from the presumptive premium rates that exceed 30%.

49) Because the department observed that the loss ratios and compensation percentages for one class, Class E--Dealers, were significantly different than the other classes in both credit life plans and credit accident and health plans, the department also proposed two alternatives for comment with regard to loss ratios: Alternative 1 presented loss ratios based on plan and class of

business. Alternative 2 presented composite loss ratios for all classes of business combined for credit life policies and all classes of business combined for credit accident and health policies.

50) After consideration of all available information, including comments from the public, it is reasonable to adopt Alternative 1, establishing loss ratios based on plan and class of business.

51) The anticipated loss ratios for credit life plans and credit accident and health plans, separated by Class E and all classes except Class E, were determined using the underlying proposed presumptive premium rates and their claim cost components.

52) It is reasonable to establish a standard for approval of deviations from the presumptive premium rates that exceed 30% that, unless it can be reasonably anticipated that a loss ratio of claims incurred to earned premiums will, after the increase becomes effective, be no less than the following:

(A) Loss Ratios For Class E Only:

(i) credit life--43%

(ii) credit accident and health:

(I) 46% for Plans 10 – 14 and 22 – 26 identified in Finding 36; and

(II) 44% for Plans 16 – 19 identified in Finding 36.

(B) Loss Ratios For All Other Classes:

(i) credit life--48%;

(ii) credit accident and heath:

(I) 51% for Plans 10 – 14 and 22 – 26 identified in Finding 36; and

(II) 46% for Plans 16 – 19 identified in Finding 36.

PRESUMPTIVE PREMIUM RATES with DISCOUNT FACTOR

53) The following presumptive premium rates are reasonable and shall be used on or after January 1, 2006.

See Figure: 28 TAC §3.5206

The following Conclusions are made, as required by Insurance Code §1153.103(c).

1) The Commissioner of Insurance has jurisdiction over this matter pursuant to Chapter 1153 of the Insurance Code.

2) Insurance Code §1153.103(a) authorizes the Commissioner of Insurance to adopt a presumptive premium rate for various classes of business and terms of coverage. This statute does not limit the authority of the commissioner to setting one presumptive premium rate; it authorizes the commissioner to set a separate presumptive premium rate for each of the various classes of business, and allows the commissioner to set additional separate rates when the terms of coverage make that appropriate.

3) The presumptive premium rates set by this order were developed after a consideration of all factors set forth in Insurance Code §1153.103(d), which requires the commissioner to consider the type or class of business when determining the presumptive premium rate.

4) Insurance Code §1153.103 does not mandate the use of a specific ratemaking methodology. It only mandates the consideration of specific factors in any methodology relied upon by the commissioner.

5) The regulatory scheme established by Chapter 1153 of the Insurance Code is that the commissioner is to set presumptive premium rates without consideration of the fact that Insurance Code §1153.105 allows insurers to use rates that are up to 30% higher or lower than the presumptive premium rates.

6) There is reverse competition in the credit insurance industry.

7) Because of reverse competition, it would be unreasonable to set presumptive premium rates using a value for the commissions component that is in the middle to higher end of the range of commissions actually paid by credit insurers.

8) Neither the producer commissions component of the presumptive premium rate calculations, nor any other part of this order, sets or limits the amount of compensation that can actually be paid by insurance companies to agents.

9) The loss ratios to be included in §3.5202, which this order adopts to establish a standard for approval of deviations from the presumptive premium rates that exceed 30%, strike a reasonable balance between the benefits returned to consumers and the premiums charged.

10) The adoption in this order of the loss ratios to be included in §3.5202 (relating to Reasonable Relation of Benefits to Premiums for Approved Deviations) does not restrict in any way the commissioner's authority to approve or disapprove a rate application because of other lawful considerations.

11) The presumptive premium rates for credit life insurance adopted in this order are just, reasonable, adequate, and nonconfiscatory, and are not excessive to insureds, insurers or agents.

12) The presumptive premium rates for credit accident and health insurance that are adopted in this order are just, reasonable, adequate, and nonconfiscatory, and are not excessive to insureds, insurers or agents.

13) The presumptive premium rates adopted in this order shall be in force and effect on January 1, 2006.

6. NAMES OF THOSE COMMENTING FOR AND AGAINST THE SECTIONS.

Against: Texas Automobile Dealers Association.

Neither for nor against, with changes: The Office of Public Insurance Counsel, Texas Association of Life and Health Insurers, American National Insurance Company,

Resource Life Insurance Company, Consumer Credit Insurance Association, Assurant Solutions, Center for Economic Justice, Independent Bankers Association of Texas, Cuna Mutual Insurance Company, Protective Life Insurance Company, Union State Bank.

7. STATUTORY AUTHORITY. The new sections and amendments are adopted under the Insurance Code Chapter 1153 and §36.001. Chapter 1153 addresses requirements for Credit Life Insurance and Credit Accident and Health Insurance, and Subchapter C specifically addresses rates. Section 36.001 provides that the Commissioner of Insurance may adopt any rules necessary and appropriate to implement the powers and duties of the Texas Department of Insurance under the Insurance Code and other laws of this state.

8. TEXT.

Division 1. General Provisions

§3.5001. Authority and Scope. This subchapter is adopted pursuant to the authority provided in Insurance Code, Chapter 1153. This subchapter applies to all life insurance and all accident and health insurance sold in connection with loans and other credit transactions, the premium for which is charged to or paid for in whole or in part either directly or indirectly by the debtor, regardless of the nature, type, or plan of the credit insurance coverage or premium payment system, which shall include any such credit

insurance which purports to be on a "cost free," "no cost," "give away," or other "no charge" basis insofar as a debtor is concerned, but shall not apply to:

(1) insurance issued or sold in connection with a loan or other credit transaction of more than 10 years' duration;

(2) insurance issued or sold in connection with a credit transaction that is:

(A) secured by a first mortgage or deed of trust; and

(B) made to finance the purchase of commercial real property or the construction of or improvement to a building other than a single family dwelling on the real property if the purchase, construction, or improvement is secured by a lien on the real property, or to refinance a credit transaction made for those purposes; or

(3) insurance issued or sold as an isolated transaction on the part of the insurer not related to an agreement or a plan for insuring debtors of the creditor.

§3.5002. Definitions. The following words and terms, when used in this chapter, shall have the following meanings unless the context clearly indicates otherwise.

(1) Account--The aggregate credit life insurance or credit accident and health coverage for a single class of business written through a single creditor, or written through more than one creditor under common control or ownership, by the insurer, whether coverage is written on a group or individual policy basis.

(2) Actual earned premium--The total of all premiums earned at the premium rates actually charged and in force during the experience period.

(3) Approved deviation by case--A premium rate or premium rate schedule adjusted in accordance with the deviation procedures set out in Division 6 of this subchapter (relating to Deviation Procedures).

(4) Automatic deviation--A premium rate that is filed pursuant to Insurance Code §1153.105.

(5) Average number of life years--The average of the number of group certificates or individual policies in force each month during the experience period (without regard to multiple coverage) times the number of years in the experience period.

(6) Case---Either a "single account case" or a "multiple account case" as follows:

(A) Single account case--An account that is at least 25% credible or, at the option of the insurer, any higher percentage as determined by the credibility table set out in §3.5603 of this subchapter (relating to Credibility Table). An insurer exercising this option must in writing notify and obtain written approval of the commissioner, of the credibility factor it will use to define a "single account case." Once the commissioner is so notified, the credibility factor will remain in effect for the insurer until a different election has been filed in writing by the insurer and approved by the commissioner.

(B) Multiple account case--A combination of all the insurer's accounts of the same class of business with experience in this state, excluding all single

account cases of the insurer defined in subparagraph (A) of this paragraph: or with the approval of the commissioner, "multiple account case" also means two or more accounts of the insurer, having like underwriting characteristics which are combined by the insurer for premium rating purposes, excluding all "single account cases" as defined in subparagraph (A) of this paragraph and other "multiple account cases" defined previously.

(7) Class of business--A class of business listed as follows:

(A) Class A--Commercial banks, savings and loan associations and mortgage companies;

(B) Class B--Finance companies and small loan companies;

(C) Class C--Credit unions;

(D) Class D--Production credit associations (agriculture and horticulture P.C.A.s);

(E) Class E--Dealers (including auto and truck, other dealers, and retail stores; and

(F) Class F--Other than subparagraphs (A) – (E) of this paragraph.

(8) Closed-end transactions--Credit transactions other than "open-end transactions" as defined in this section.

(9) Credibility factor--The degree to which the past experience of a case can be expected to occur in the future. The credibility factor is based either on the average number of life years or the incurred claim count during the experience period

as shown in the credibility table set out in §3.5603 of this subchapter. The insurer shall notify the commissioner in writing, and obtain written approval of the commissioner, about which of the two methods it will use in measuring credibility. Once the commissioner is so notified, the method will remain in effect for the insurer until a change has been filed with and approved by the commissioner.

(10) Credit disability--Credit Accident and Health.

(11) Earned premium at presumptive premium rate--Premium earned during the experience period at the presumptive premium rate set forth in §3.5206 of this subchapter (relating to Presumptive Premium Rates). If the rate for a case is not the presumptive premium rate, premium earned at the presumptive premium rate must be determined in accordance with the conversion method set forth in Form CI-EP-L or Form CI-EP-DIS, as appropriate, provided by the department for that purpose, and set out in an attachment by the insurer to its deviation request form. The forms can be obtained from the Texas Department of Insurance, Filings Intake Division, MC 106-1E, P.O. Box 149104, Austin, Texas 78714-9104. The forms can also be obtained from the department's internet web site at www.tdi.state.tx.us.

(12) Experience--The earned premiums and incurred claims for a single or multiple account case. Experience will be the most recent experience in this state for a class of business, and may include the experience of the case while with a prior insurer to the extent necessary to achieve credibility.

(13) Experience period--The period of time for which experience is reported, but not for period longer than three years.

(14) Incurred claim count--The number of claims incurred for the case during the experience period. This means the total number of claims reported during the experience period (whether paid or in the process of payment) plus any incurred but not reported at the end of the experience period less the number of claims incurred but not reported at the beginning of the experience period. If a debtor has been issued more than one certificate for the same plan of insurance, only one claim is counted. If a debtor receives disability benefits, only the initial claim payment for that period of disability is counted.

(15) Incurred claims--The liability resulting from the happening of the contingency insured against whether paid, reported, not reported or resisted on accounting dates, valued by date of occurrence and, without reduction for reinsurance, at amounts, excluding claims expenses, sufficient to discharge the company from all liability and is equal to claims paid minus unreported claims beginning of period plus unreported claims end of period minus claim reserve beginning of period plus claim reserve end of period.

(16) Open-end transactions or revolving accounts--Transactions in which credit is extended by a creditor under an agreement whereby:

(A) the creditor reasonably contemplates repeated transactions;

(B) the creditor may impose a finance charge from time to time on an outstanding unpaid balance; and

(C) the amount of credit that may be extended to the debtor during the term of the plan (up to any limit set by the creditor) is generally made available to the extent that any outstanding balance is repaid.

(17) Presumptive premium rate--The rate established by the commissioner and set out in §3.5206 of this subchapter.

(18) Pro rata method--A method used in determining premium refunds based on the assumption that premiums are earned in equal increments over the term of the policy. The premium refunds are calculated by multiplying the original gross premium by a factor determined by the formula *t/n*, in which *t* is the number of months remaining from its evaluation date to the end of the loan and *n* is the number of months in the original term.

(19) Rule of anticipation (aka the single premium method)--A method used in determining premium refunds in which the unearned premium is equal to the gross single premium for the remaining term and remaining benefits.

(20) Sum of the digits method, aka rule of 78 method--A method used in determining premium refunds in which an unearned premium factor is calculated by dividing the sum of the original number of monthly payments by the sum of the remaining number of monthly payments. The premium refunds are calculated by multiplying the original gross premium by a factor determined by the formula *(t * (t+1)/(n*

* *(n+1)*, in which *t* is the number of months remaining from its evaluation date to the end of the loan and *n* is the number of months in the original term.

Division 2. Applications and Policies

§3.5105. Application Provisions.

(a) If said individual policy or group certificate of insurance is not delivered to the debtor at the time the indebtedness is incurred, a copy of the application for such individual policy or a notice of such proposed group insurance coverage shall be delivered to the debtor at the time such indebtedness is incurred. However, when insurance is voluntarily applied for more than 30 days later by the debtor, and such application for insurance is a transaction separate and apart from the credit transaction and is not a requirement of the creditor, and in the absence of a prior identifiable insurance charge to the debtor in the loan involved, a copy of such application or such notice conforming to these sections shall be delivered to the debtor when executed.

(b) Every application, enrollment form, or notice of proposed insurance shall provide for the signature of the debtor and shall set forth:

(1) the name and home office mailing address of the insurer, and on notices of proposed group insurance, debtor's applications for group insurance or enrollment forms for group insurance, an identification of the master policy;

(2) the name and age of the debtor or debtors;

(3) the full amount of premium or the total identifiable insurance charge, if any, to the debtor, separately for credit life and for credit accident and health insurance;

(4) the amount of coverage;

(5) the effective date of insurance, if accepted by the insurer, and the termination date of insurance which shall not extend more than 15 days beyond the scheduled maturity date of the indebtedness except when extended without additional cost to the debtor;

(6) a brief description of the coverage applied for; and

(7) a statement that upon acceptance of the insurance by the insurer and not later than 45 days after the date upon which the indebtedness is incurred (or, if the indebtedness is an open-end transaction, not later than 30 days from the date of application for coverage) the insurer shall cause the individual policy or the group certificate of insurance to be delivered to the debtor, and that if the insurance is not accepted by the insurer or by a substituted insurer as authorized by Insurance Code §1153.158, then any insurance charge made for such insurance shall be fully refunded and the creditor shall immediately give written notice to such debtor and shall promptly make an appropriate credit to the debtor's account in accordance with Insurance Code §1153.203.

(c) The copy of such application or notice of proposed insurance shall refer exclusively to insurance coverage and shall be separate and apart from the loan, sale, or other credit statement of account, instrument, or agreement, unless the information

above required appears in type of at least equal size and prominence as the other provisions of said statement of account, instrument, or agreement.

(d) The application, enrollment form, or notice of proposed insurance shall not contain language which requires the debtor to attest or acknowledge that he/she is eligible or ineligible for the insurance coverage.

(e) If eligibility conditions of employment and/or good health are required, the debtor's application shall contain a space for the debtor's and/or joint debtor's signatures whereby they can attest to those specific conditions of eligibility.

Division 3. Filing and Approval of Forms and Rates

§3.5201. Submission of Form and Rate Filings.

(a) Every insurance company, when submitting a schedule of rates for automatic or approved deviations from the presumptive premium rate, shall identify the rates to be used with the policy form submitted for approval. The face page of every form or schedule submitted to the commissioner, shall include with its identifying form number the additional identification: "(3.53)" if the form is an individual life and/or individual accident and health form and used only within the scope of Insurance Code Chapter 1153; “(3.53 and 3.50)” if the form is a group life and/or group accident and health form and used only within the scope of Chapter 1153; "(3.53 R.A.)" or "(3.53 O.E.)" if the form is a credit life and/or credit accident and health form and is written on open-end transactions. The designations "(3.53 R.A.)" or "(3.53 O.E.)" may not be used on forms

or schedules providing insurance coverage on closed-end transactions. The additional identification, as required by this subsection, will only be used on credit life and/or credit accident and health insurance written under the scope of Insurance Code, Chapter 1153.

(b) All form and rate filings are to be filed in accordance with the requirements of Subchapter A of Chapter 3 of this title (relating to Submission Requirements for Filings and Departmental Actions Related to Such Filings.

§3.5202. Reasonable Relation of Benefits to Premiums for Approved Deviations. As the basic test of the reasonableness of the relation of benefits to the premium charges for approved deviations, to be applied separately by policy form number, it is hereby declared that the benefits of credit life insurance or credit accident and health insurance, individual or group, shall not be considered to be reasonable in relation to the premium charges, unless it can be reasonably anticipated that a loss ratio of “claims incurred” to “earned premiums” will, after the increase becomes effective, be no less than the following:

(1) Loss Ratios For Class E Only:

(A) credit life--43%;

(B) credit accident and health:

(i) 46% for Plans 10 – 14 and 22 – 26 on the Presumptive Premium Rate Chart found at §3.5206 of this subchapter (relating to Presumptive Premium Rates); and

(ii) 44% for Plans 16 – 19 on the Presumptive Premium Rate Chart found at §3.5206 of this subchapter.

(2) Loss Ratios For All Other Classes:

(A) credit life--48%;

(B) credit accident and heath:

(i) 51% for Plans 10 – 14 and 22 – 26 on the Presumptive Premium Rate Chart found at §3.5206 of this subchapter; and

(ii) 46% for Plans 16 – 19 on the Presumptive Premium Rate Chart found at §3.5206 of this subchapter.

§3.5206. Presumptive Premium Rates. The following presumptive premium rates are adopted by the commissioner and shall be used on or after January 1, 2006.

Figure: 28 TAC §3.5206: Exhibit 22-3
Figure: 28 TAC §3.5206 Exhibit 22-4
Figure: 28 TAC §3.5206 Exhibit 22-5
Figure: 28 TAC §3.5206 Exhibit 22-6
Figure: 28 TAC §3.5206 Exhibit 21

Division 4. Presumptively Acceptable Relation of Credit Life Insurance Benefits to Premiums

§3.5307. Standard for Additional Benefits. If a contract of insurance includes other lawful benefit or benefits for which standards or reasonableness of benefits in relation to premium are not elsewhere in these sections determined or described, any premium charged therefor in excess of the rates set forth in these sections shall be shown to the satisfaction of the commissioner of insurance to be based upon credible statistics, and shall be reasonable in relation to the additional benefit provided.

Division 5. Standards of Benefits for Credit Accident and Health Insurance

§3.5502. Joint Credit Accident and Health Insurance.

(a) Joint debtors, for purposes of credit accident and health insurance written under Insurance Code, Chapter 1153 means only spouses or business partners, and such persons must be jointly and severally liable for repayment of the single indebtedness and be joint signers of the instrument of indebtedness. Endorsers and guarantors are not eligible for credit insurance coverage. Joint accident and health coverage shall not be written covering more than two debtors.

(b) Coverage may be provided by either of the methods set forth in paragraphs (1) and (2) of this subsection:

(1) each debtor is insured for 100% of the disability payment;

(2) each debtor is insured for a portion of the disability payment. The total of the portions shall equal 100% of the disability payment. The joint disability insurance

benefit cannot exceed the amount of insurance that would have been provided if coverage had been issued on a single debtor.

(c) Joint disability coverage shall be evidenced by an individual policy or, in the case of group insurance, by a certificate of insurance. The form shall specify the amount of disability benefit to be provided on each debtor. The coverage shall not be provided by two single individual disability policies or by two single group disability certificates of insurance. Jointly indebted persons shall not both be covered separately at single accident and health rates.

(d) Joint disability forms shall provide that if coverage on one of the joint debtors is terminated, the coverage on the other debtor shall be continued under a single individual disability policy or a single group disability certificate. Coverage may be terminated for any of the reasons stated in paragraphs (1) - (4) of this subsection:

(1) the coverage is successfully contested;

(2) the coverage was issued in error to a joint insured who exceeded the eligibility age limits and who correctly stated his age. Under these circumstances, the insurer has the right to terminate the portion of coverage provided on such insured as long as the adjustment is handled as set forth in §3.5106(b) of this title (relating to Prohibited Provisions and Practices) addressing excess coverage;

(3) coverage was issued in error to a joint insured who did not meet the eligibility employment requirements, if required, and who correctly stated his employment status in writing. Under these circumstances, the insurer has the right to

terminate the portion of coverage provided on such insured as long as the adjustment is made as set forth in §3.5106(b) of this title addressing excess coverage;

(4) suicide or any other life exclusions, as set forth in the policy and/or certificate of insurance.

(e) If termination occurs for any of the reasons set forth in subsection (d)(1) - (3) of this section, the amount of premium refund required will be equal to the difference between the premium charged for joint disability coverage and the premium that would have been charged if only single disability coverage (on a single insured) had been provided at the time the coverage was originally issued. If termination occurs for the reason set forth in subsection (d)(4) of this section, the amount of premium refund required will be equal to the unearned portion, at the date of death, of the premium charged for joint disability coverage minus the unearned portion, at the date of death, of the premium that would have been charged if only single disability coverage (on the single "surviving" insured) had been provided at the time the coverage was originally issued. The refund for joint disability coverage is to be paid in addition to the refund for joint life insurance coverage, in accordance with §3.5104(a)(2) of this title (relating to Benefits and Refunds), if joint life coverage was issued.

(f) If a separate identifiable premium is charged for the joint disability coverage, and if joint coverage is desired by the debtors, each debtor must elect and sign for the joint coverage.

(g) The maximum premiums to be charged for joint disability coverage when each debtor is insured for 100% of the disability payment must be equal to the amount set forth in the latest adopted presumptive premium rates for joint credit disability coverage. The maximum premiums to be charged for joint disability coverage when each debtor is insured for a portion of the disability payment, with the total of the portions equal to 100% of the disability payment, must be equal to the premium that would have been charged if 100% of the disability insurance amount was provided on a single life, as set forth in the latest adopted presumptive premium rates for single life credit disability coverage.

(h) The annual experience data reports required under §3.5701 of this title (relating to Statistical Data and Annual Experience Calls) shall be submitted as follows:

(1) if joint disability coverage is provided on each debtor for 100% of the disability payment, the experience data will be reported as joint disability coverage 1;

(2) if joint disability coverage is provided on each debtor for a portion of the disability payment, with the total of the portions equal to 100%, the experience data will be reported as joint disability coverage 2.

Division 6. Deviation Procedures

§3.5601. Deviation by Case Allowed. Two types of rate deviation are allowed, automatic deviation and approved deviation as defined in §3.5002 of this title (relating to Definitions).

(1) Automatic Deviation. An insurer electing to deviate from the presumptive premium rate established by the commissioner shall file with the commissioner the insurer's proposed rate for credit life and credit accident and health insurance. On filing the rate with the commissioner, the insurer may use the filed rate until the insurer elects to file a different rate. Except as provided in paragraph (2) of this section, an insurer may not use a rate that is more than 30% higher or 30% lower than the presumptive premium rate.

(2) Approved Deviation by Case. Notwithstanding the determination by the Commissioner of Insurance of presumptive premium rates which are reasonable in relation to the benefits of a policy providing the coverage to which the rates are applicable, an insurer who has experienced excessive loss ratios or who fails to develop the minimum loss ratio as defined in §3.5202 of this title (relating to Reasonable Relation of Benefits to Premiums for Approved Deviations), for a case consisting of a single account or combination of accounts, as defined in §3.5002 of this title, will be permitted, at its own request, or may be required by the commissioner, to adjust the premium rate or premium rate schedule for such case in accordance with the deviation procedures set out in this subchapter. An approved deviation request shall be presented with form CI-DRF and §3.5602 of this division (relating to Request for an Approved Deviated Premium Rate).

(3) The commissioner may disapprove a request for an approved deviated rate on the grounds that the rate is not actuarially justified, or is unjust,

unreasonable, excessive or inadequate. A rate is excessive if it is unreasonably high for the coverage provided and a reasonable degree of competition does not exist with respect to the classification to which the rate would be applicable. A rate is inadequate if the rate is insufficient to sustain projected losses and expenses, or the rate substantially impairs, or is likely to substantially impair, competition with respect to the sale of the product.

(4) The insurer may use the rate if the commissioner does not disapprove it before the 60th day after the date the insurer filed the rate.

§3.5602. Request for an Approved Deviated Premium Rate. A request for an approved deviated rate must be made in writing and shall include all of the information which is required under this subchapter. It must be accompanied by a list of the creditors whose experience is the basis for such request, and must be attested to by an officer of the insurer. The use of any approved rate deviation approved by the commissioner is limited to those creditors whose names appear on such list. No rate deviation may be used unless and until approved by the commissioner in writing. Any request for an approved deviated rate shall be submitted to the commissioner through the Filings Intake Division in the manner prescribed on Form CI-DRF provided by the department for that purpose. The form can be obtained from the Texas Department of Insurance, Filings Intake Division, MC 106-1E, P.O. Box 149104, Austin, Texas 78714-9104. The form can also be obtained from the department's internet web site at

www.tdi.state.tx.us. In order to provide the commissioner sufficient time for review, all requests for approved rate deviations must be submitted a minimum of 60 days prior to the proposed effective date of the approved deviated rate.

§3.5603. Credibility Table. The following table shall be used to determine the credibility factor of a case, as defined in §3.5002 of this title (relating to Definitions).

Figure: 28 TAC §3.5603:

Credibility Table

AVERAGE NUMBER OF LIFE YEARS

CREDIT LIFE	7 DAY	14 DAY	30 DAY	90 DAY	INCURRED CLAIM COUNT	CREDIBILITY FACTOR Z
1	1	1	1	1	1	.00
1,800	95	141	209	327	9	.25
2,400	126	188	279	429	12	.30
3,000	158	234	349	536	15	.35
3,600	189	281	419	643	18	.40
4,600	242	359	535	821	23	.45
5,600	295	438	651	1,000	28	.50
6,600	347	516	767	1,179	33	.55
7,600	400	594	884	1,357	38	.60
9,600	505	750	1,116	1,714	48	.65
11,600	611	906	1,349	2,071	58	.70
14,600	768	1,141	1,698	2,607	73	.75

17,600	926	1,375	2,047	3,143	88	.80
20,600	1,084	1,609	2,395	3,679	108	.85
25,600	1,347	2,000	2,977	4,571	128	.90
30,600	1,611	2,391	3,558	5,464	153	.95
40,000	2,106	3,125	4,651	7,143	200	1.00

§3.5604. Minimum Change.

(a) For credit life insurance, the currently charged premium rates will be considered the case rates if the single premium (or its equivalent) case rate per $100 of initial amount of insured indebtedness repayable in 12 equal monthly installments as determined under this subchapter is within 5.0% of the corresponding premium under the currently charged premium rates for the case.

(b) For credit accident and health insurance, the currently charged premium rates will be considered the case rate if the case rate as determined under this subchapter is within 5.0% of the currently charged premium rates for the case.

§3.5607. Termination of Upward Deviated Case Rate. An upward approved deviated single account case rate shall continue for a period equal to the experience period on which it was based, not to exceed three years, subject however to the provisions of §3.5608 of this title (relating to Annual Review of Approved Deviated Rates). If a change of insurers occurs, an upward approved deviated single account

case rate may be continued by the replacement carrier by giving written notification to the commissioner, within 30 days of the effective date of providing coverage to the account, of the new carrier's intent to continue the upward approved deviated single account case rate. The period of continuance shall not go beyond the expiration date originally granted to the previous insurer for that account. If a change of insurers occurs, an approved deviated multiple account case rate shall not be continued by the replacement insurer beyond the date the original carrier lost the account unless all of the accounts forming the multiple account pool are taken over. If all accounts are taken over, the requirements for continuation are the same as mentioned in the preceding paragraph for single account cases.

§3.5608. Annual Review of Approved Deviated Rates. All approved deviated rates shall be filed for review for each case in accordance with this subchapter each year for each case. At the time of such review of approved deviated rates, adjustments may be made in the rates if the commissioner finds that experience shows that an adjustment is appropriate.

§3.5610. Determination of Approved Deviated Case Rates.

(a) For cases which are not of credible size, or have no experience, no approved deviation shall be made in the presumptive premium rates under these deviation

procedures; except that nothing herein shall be construed as preventing any insurer from filing an automatic deviation pursuant to Insurance Code, §1153.105.

(b) For purposes of this section: if the coverage for a single creditor which qualifies as a case has been in force with the insurer for less than the experience period:

(1) the claim experience of the creditor while covered by any prior insurer shall be included to the extent necessary in determining the appropriate case ratios; and

(2) the experience considered in the determination of multiple state case rates shall be Texas experience for the case unless the insurer makes the one-time election to use only nationwide experience. The election to use only nationwide experience must be accompanied by a certification that the insurer uses the same nationwide basis in determining the case ratios in each state in which the case has experience. A grouping of states may be used subject to the same requirements of consistency and certification.

(c) Schedule of new case rates. When submitting a Request for Deviated Rate pursuant to §3.5602 of this title (relating to Request for an Approved Deviated Premium Rate) the insurer shall also file a schedule of new case rates as determined by this section.

(d) Approved Deviation Request Form. As required by §3.5602 of this title any request for approved deviated rates shall be submitted to the commissioner through the Filings Intake Division in the manner prescribed on the form provided by the department

for that purpose. The form can be obtained from the Texas Department of Insurance, Filings Intake Division, MC 106-1E, P.O. Box 149104, Austin, Texas 78714-9104. The form can also be obtained from the department's internet web site at www.tdi.state.tx.us.

Division 9. Premium Refunds

§3.5901. Refund of Unearned Premiums. With respect to policies issued and certificates delivered after the effective date of these sections:

(1) the refund of an unearned amount paid by or charged to a debtor for credit life insurance, or for credit accident and health insurance, on which charges to the debtor are payable by other than a single sum must not be less than the pro rata gross unearned amount charged;

(2) the refund of an unearned amount paid by or charged to a debtor for credit life insurance, or for credit accident and health insurance, on which the insurance charges to the debtor are paid in a single sum must be computed by the rule of anticipation, as defined in §3.5002 of this title (relating to Definitions), or by another method which produces a substantially equal amount and is approved by the commissioner of insurance. This paragraph shall not be interpreted to preclude refunds for credit accident and health insurance to be computed by the mean of the gross unearned premium calculated by the "sum of the digits" (rule of 78) and the pro rata method.

§3.5905. Refunds. No refund of premium need be made of an amount paid or charged to the debtor for credit insurance regulated under the Insurance Code, Chapter 1153, in the event of termination of the indebtedness or the insurance prior to the scheduled maturity date of the indebtedness if the amount of such refund is less than $3.00. (For insurance coverage subject to Finance Code Chapters 342 - 348, a refund must be made, except that no cash refund shall be required if the amount thereof is less than $1.00.)

Division 10. Responsibilities and Obligations of Insurance Companies and Their Agents and Representatives

§3.6002. Delegation by Insurer of Responsibilities of Policy Issuance and Premium Collection.

(a) The insurer, by its group policy, may authorize the group policyholder-creditor to issue certificates of group insurance or may authorize a legally appointed insurance agent of the insurer to issue certificates of insurance or policies of insurance, and respectively, to collect the insurance charge under the group policy, or premium therefor under an individual policy, provided that the master group insurance policy with the creditor or the agent's agreement with the agent under which such authority is granted shall require that:

(1) the creditor issue such group certificate, or the agent issue such certificate of insurance or insurance policy in the name of the insurer, and payment of

the respective policy premium shall be by a check payable to the insurer or by deposit to an account of the insurer under the sole control of the insurer;

(2) a "home office" copy of each certificate or policy so issued, or electronic or other data therefor which can be substantiated by such certificate or policy, together with the premium therefor, shall be delivered to the insurer within 30 days after the close of the calendar month in which the certificate or policy is issued;

(3) refunds of unearned premiums shall be made in accordance with this subchapter; and

(4) no creditor or creditor agent may knowingly issue any group certificate of insurance which, alone, or in conjunction with other group certificates issued on the same risk, will in the aggregate exceed the group credit life insurance limits of this state.

(b) No insurer may authorize, and no insurance agent, or group policyholder within their respective capacities may issue any policy or certificate of insurance or collect any premium or insurance charge therefor or make any refund of premium, except only pursuant to and in accordance with either a master group insurance policy or an agent's agreement in compliance with this section.

CERTIFICATION. This agency certifies that the new sections as adopted have been reviewed by legal counsel and found to be a valid exercise of the agency’s legal authority.

Issued at Austin, Texas, on _____, 2005.

_____
Gene C. Jarmon
General Counsel and Chief Clerk
Texas Department of Insurance

IT IS THEREFORE THE ORDER of the Commissioner of Insurance that new §§3.5002, 3.5206, and 3.5603 and amendments to §§3.5001, 3.5105, 3.5201, 3.5202, 3.5307, 3.5502, 3.5601, 3.5602, 3.5604, 3.5607, 3.5608, 3.5610, 3.5901, 3.5905, and 3.6002, concerning credit life and credit accident and health insurance, are adopted.

AND IT IS SO ORDERED.

_____
Jose Montemayor
Commissioner of Insurance

ATTEST:

_____
Gene C. Jarmon
General Counsel and Chief Clerk

COMMISSIONER'S ORDER NO._____