

**SUBJECT:** Penalties for insurers that unsuccessfully appeal rate rollbacks

**COMMITTEE:** Insurance —favorable, without amendment

**VOTE:** 6 ayes — Smithee, Seaman, Eiland, Keffer, Taylor, Thompson  
1 nay — Isett  
2 absent — Oliveira, Van Arsdale

**SENATE VOTE:** On final passage, April 21 — 31-0, on Local and Uncontested Calendar

**WITNESSES:** *(On House companion bill, HB 1585 by Smithee:)*  
For — Ollie Besteiro, AARP; Ware Wendell, Texas Watch  
  
Against — Will Davis, USAA; Beaman Floyd, Allstate, State Farm, Nationwide, American Insurers Association, TCAIS; Jay Thompson, AFACT  
  
On — Bill Peacock, Texas Public Policy Foundation

**BACKGROUND:** In 2003, the Legislature enacted SB 14 by Jackson, which overhauled homeowners and auto insurance regulation in Texas. The bill was enacted largely in response to a dramatic increase in homeowners insurance rates between 2000 and 2003. SB 14 made all personal auto and residential homeowners insurers, including those whose rates previously were unregulated, subject to “rate standards” requiring that all rates be just, fair, reasonable, adequate, not confiscatory, not excessive, and not unfairly discriminatory.

By July 1, 2003, residential property insurers were required to file their rates with the insurance commissioner, who had 60 days to approve, reject, or modify the rates and could order refunds or credits if rates were found to be excessive. In August 2003, the insurance commissioner ordered 37 companies to reduce rates by a total of \$510 million, which amounted to an overall reduction of 12 percent.

Two of the state's largest property insurers — State Farm Lloyds and Farmers — were ordered to cut their rates by 12 percent and 17.5 percent respectively. These companies filed appeals in state district court claiming that the new statute and TDI's method of determining the rate cuts violated the companies' constitutional and statutory due process rights.

In October 2004, State District Judge Suzanne Covington of Austin found in favor of the companies and ordered TDI to conduct rate hearings. In December, 2004, Farmers agreed to cut future rates by between 5 percent and 20 percent, but retained \$88 million in disputed overcharges. State Farm has not agreed to a rate reduction.

Under the 2003 legislation, companies that unsuccessfully appeal a commissioner's rate reduction decision in court must refund to consumers the amount they have collected over the state-ordered rate, plus interest of the prime rate plus 1 percent.

**DIGEST:**

CSSB 14 would increase the interest required if an insurer unsuccessfully appealed a rate refund in court. The interest would be the lesser of 18 percent or 6 percent plus the prime rate for the calendar year in which the commissioner's order was issued. Interest would accrue beginning on the date on which the commissioner issued the order and would continue to accrue until the refund was paid. An insurer would not be required to pay any interest penalty if the company prevailed in an appeal of the commissioner's order.

An insurer also would be prohibited from claiming a premium tax credit to which it otherwise would be entitled if it did not comply with the requirements of the bill.

The bill would take effect September 1, 2005.

**SUPPORTERS  
SAY:**

By imposing stiff penalties on insurers that unsuccessfully challenge rate rollbacks in court, CSSB 14 would provide fair compensation to consumers and serve as a deterrent to companies that try to game the system. The penalties in existing law are not severe enough to prevent insurers from using court challenges as a stalling tactic when a refund is ordered.

The bill would help deter companies from charging consumers excessive or unfairly discriminatory premiums, as State Farm has continued to do

even though TDI ordered the company to roll back its rates by 12 percent in 2003. By using the courts as a stalling tactic, State Farm has withheld from consumers an estimated \$155 million in overcharges each year. Stiffer penalties are needed to prevent such actions in the future.

**OPPONENTS  
SAY:**

CSSB 14 is unnecessary because the current penalty of 1 percent interest is sufficient to prevent a company from pursuing an unsuccessful appeal in court as a stalling tactic. The bill would not have affected State Farm and Farmers because their appeal was successful, and State Farm continues to contend that its rates are justified.

**NOTES:**

SB 14 originally failed to be reported by the House Insurance Committee by a vote of 4-4 on May 3, but a new committee substitute was considered and approved on May 16. The committee substitute eliminated a provision in the Senate-passed version that would have made new rate filings subject to prior approval by the commissioner until the expiration of an appeal period. The committee substitute also eliminated a provision that would have made the bill apply only to policies issued or renewed on or after January 1, 2006.

The House companion bill, HB 1585 by Smithee, was considered in a public hearing and left pending in the Insurance Committee on March 21.