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SFA BILL ANALYSIS

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Senate Bill 666 (Substitute S-2 as enrolled)
Sponsor: Senator Bill Bullard, Jr.
Committee: Financial Services

Date Completed: 10-23-01

RATIONALE

Life insurance companies are required to maintain certain levels of reserves according to standards set by the Insurance Code and the Commissioner of the Office of Financial and Insurance Services. These standards dictate the amount of capital that insurers must set aside for various types of policies. The relevant provisions of the Code were last amended by Public Act 274 of 1995. Before Public Act 274 took effect, the Code required life insurers to use what is commonly called the "unitary method" of calculating reserves for policies and contracts issued before 1996, for which gross premiums varied by duration. The 1995 amendments deleted that requirement but also included language permitting the unitary method unless it is otherwise prohibited by the Commissioner. This language is contained in Enacting Section 2 of Public Act 274.

At the time Public Act 274 was enacted, the insurance industry recognized both the unitary method and another method of calculating reserves, commonly called the "Triple X" method. Since that time, Triple X has become the industry standard. In 2001, Michigan also adopted the Triple X method, when the Commissioner issued a bulletin requiring insurers to comply with practices and procedures of the National Association of Insurance Commissioners (NAIC). Nevertheless, the Commissioner still must specifically prohibit insurers from using the unitary method, due to the language of Enacting Section 2 of Public Act 274. It has been suggested that this language be eliminated.

CONTENT

The bill would amend the Insurance Code to repeal Enacting Section 2 of Public Act 274 of 1995, effective January 1, 2002. Enacting Section 2 contains the following language:

> This amendatory act does not prohibit an insurer from calculating valuation net premiums as a uniform percentage of all the respective gross premiums or premiums guaranteed in the policy or contract for any policy or contract for which gross premiums vary by duration..., so long as not specifically prohibited from doing so by the commissioner.

BACKGROUND

Public Act 274 of 1995 was enacted in the aftermath of 1994 amendments to the Insurance Code that incorporated model NAIC legislation. The adoption of the 1994 measures was necessary to ensure that Michigan's insurance regulatory program met the NAIC's accreditation standards, and that insurers incorporated in Michigan therefore could conduct business in other states.

Part of the 1994 amendments addressed the way in which life insurers determine their reserves. The legislation retained a provision requiring companies to use the unitary method of calculation for certain policies and contracts issued before January 1, 1996. Since the NAIC model does not recognize the unitary method, it was subsequently suggested that this provision should be removed from Code but the practice should not actually be prohibited. Public Act 274 of 1995 accomplished this by deleting the language from the Code but, in Enacting Section 2, allowing insurers to continue using the unitary method unless the Commissioner prohibits its use.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

When the Insurance Code was amended in the mid-1990s, the Commissioner and the life insurance industry saw the value of retaining the unitary method of calculating reserves, while the so-called Triple X method was being developed and refined. Evidently, insurers in other states were allowed to use the unitary method, and some people believed that Michigan-based companies would be at a competitive disadvantage if they could not do so, as well. Public Act 274 of 1995 addressed this concern by bringing the Code into conformity with the NAIC model, while allowing the unitary method for certain policies as long as it is not prohibited by the Commissioner. Presently, the Triple X method is the industry standard for these policies, and the Commissioner has mandated its use through the issuance of an annual bulletin. The existence of Enacting Section 2, however, means that the Commissioner also must specifically prohibit insurers from using the unitary method. Should the Commissioner fail to do so in any given year, there would be some ambiguity as to which valuation method insurers should use. By repealing Enacting Section 2, the bill would eliminate this potential for confusion and inconsistency in the law.

Legislative Analyst: S. Lowe

FISCAL IMPACT

The bill would have no fiscal impact on State or local government.

Fiscal Analyst: M. Tyszkiewicz

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