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TO THE SENATE COMMITTEE ON COMMERCE, CONSUMER PROTECTION AND AFFORDABLE HOUSING

TWENTY-FOURTH LEGISLATURE
Regular Session of 2008

Thursday, February 21, 2008
9:00 a.m.

TESTIMONY ON SENATE BILL NO. 2314 SD1 – RELATING TO INSURANCE

TO THE HONORABLE RUSSELL S. KOKUBUN, CHAIR, AND MEMBERS OF THE COMMITTEE:

My name is J.P. Schmidt, State Insurance Commissioner ("Commissioner"), testifying on behalf of the Department of Commerce and Consumer Affairs ("Department"). The Department opposes S. B. 2314 SD1, which would weaken the anti-bundling provisions of the Insurance Code.

Under Hawaii Revised Statutes section 431:13-103(a)(4)(B), part of the unfair methods of competition and unfair and deceptive acts and practices in the business of insurance statute, insurance companies are prohibited from making the purchase of one class of insurance contingent upon the purchase of another class of insurance. This is known as the "anti-bundling" provision and is designed to protect consumers from an insurer who would seek to force consumers to purchase multiple types of insurance that the consumer may not want or need in order to buy a policy that they want. The rule does not prohibit an insurer from offering different classes of insurance together in an attractively priced package. There is no violation if the consumer has the option of taking the package or just taking the insurance wanted. The law only prohibits an

insurer from refusing to sell one policy unless another policy or other policies are also purchased.

In other words, under current law a health insurer could pair a life insurance policy with a health insurance policy and offer the package to consumers who are free to accept or reject the life insurance. However, under current law, the insurer can not refuse to sell the health policy if the consumer declines the life insurance.

S. B. 2314 SD1 would allow health insurers with less than a 5% market share to force customers to purchase a "bundle" of insurance products as a condition of sale. The Insurance Division is aware of only one insurer engaging in this practice presently and that is the health insurer Hawaii Management Alliance Association ("HMAA"). Presently, HMAA requires sole proprietors to puchase not only health insurance related coverages such as vision and dental insurance, but also life insurance. The Insurance Division is moving to halt this practice. This bill seeks to reverse the Division's action.

Although this bill only applies to insurers with less than 5% market share, the issue is not market share, the issue is what the U.S. Supreme Court in *Jefferson Parish Hosp. Dist. No. 2 v. Hyde* called "market power". The Court stated:

> ... we have condemned tying arrangements when the seller has some special ability-usually called "market power"-to force a purchaser to do something that he would not do in a competitive market. [citations omitted] [FN 20] When "forcing" occurs, our cases have found the tying arrangement to be unlawful.
>
> *Jefferson Parish Hosp. Dist. No. 2 v. Hyde,* 466 U.S. 2, 13-14, 104 S.Ct. 1551,1559 (U.S.La.,1984)

In footnote 20, the court noted:

> FN20. This type of market power has sometimes been referred to as "leverage." ... 'Leverage' is loosely defined here as a supplier's ability to induce his customer for one product to buy a second product from him that would not otherwise be purchased solely on the merit of that second product."

Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 14, 104 S.Ct. 1551, 1559 (U.S.La.,1984)

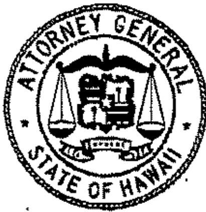
HMAA has that "leverage" -- although HMAA has less than a 5% share of the "accident and sickness insurance market", HMAA presently controls 100% of the market for group policies to sole proprietors.

Sole proprietors who don't qualify as "group of one" employers under Hawaii's HIPAA statute can get group health insurance only from HMAA. Other insurers could sell group insurance to sole proprietors but they are not required to do so by law (at least by our interpretation of Hawaii's HIPAA statute) -- so they don't. Because sole proprietors can only get group health insurance from HMAA, HMAA has "market power" even though it has less than a 5% share of the "accident and sickness insurance market."

The Committee should understand that allowing this practice does not mean lower premiums for the insured. In HMAA's case for example, HMAA got a profit-sharing rebate, or "kick-back" if you will, from the life insurer of profits on the insurance. This rebate was not passed on to the customer; it went to a HMAA affiliated company as additional profit. In addition to this rebate, another HMAA affiliated company got commissions for placement of the life insurance, again not to the benefit of the consumer but to increase the profit of a privately owned company acting as an insurance agent for HMAA.

We understand that SD1 has been drafted so as to limit bundling to only dental and vision insurance, however, why should a consumer be required to take vision or dental insurance if they don't need or want that coverage? The consumer never benefits from being forced to purchase unwanted coverage – only the insurer benefits. Nothing in this bill requires that the increased profits that an insurer reaps from being allowed to bundle coverages are to be passed on to the consumer. The anti-bundling rules are there to protect Hawaii's consumers; it would be bad policy to allow so-called "small insurers" to use their market power to force consumers to take insurance they don't want or need.

We thank this Committee for this opportunity to testify and ask that this bill be held.



TESTIMONY OF THE STATE ATTORNEY GENERAL
TWENTY-FOURTH LEGISLATURE, 2008

ON THE FOLLOWING MEASURE:
S.B. No. 2314, S.D. 1, RELATING TO INSURANCE.

BEFORE THE:
SENATE COMMITTEE ON COMMERCE, CONSUMER PROTECTION, AND AFFORDABLE HOUSING

DATE: Thursday, February 21, 2008 **TIME:** 9:00 AM
LOCATION: State Capitol, Room 229
Deliver to: Committee Clerk, Room 407, 1 Copy

TESTIFIER(S): Mark J. Bennett, Attorney General
or James F. Nagle, Deputy Attorney General

Chair Kokubun and Members of the Committee:

We strongly oppose S.B. No. 2314, S.D. 1, which would weaken consumer protection by affecting the tying prohibition of the insurance code found at section 431:13-103(a)(4), Hawaii Revised Statutes. We disapprove of forcing a consumer to purchase one product as a prerequisite for buying another. We object to a seller's exploitation of its control over the tying product to force the buyer into the purchase of a tied product that the buyer either did not want at all or might have preferred to purchase elsewhere on different terms. We believe in consumer choice.

As noted by the Insurance Division ("Division"), this bill appears to involve the conduct of Hawaii Medical Assurance Association ("HMAA"). Currently, HMAA requires sole proprietors to purchase not only health insurance coverage but also life insurance coverage. HMAA counters that it occupies only about three percent of Hawaii's health insurance market and thus proposes this bill to allow it to tie its health insurance with life insurance from another producer. Although HMAA may have less than a five percent share of the "accident and sickness insurance market," the Division notes that HMAA presently controls one hundred percent of the market for group policies sold to

sole proprietors. Thus, sole proprietors would be denied competitive access to the tied product market (life insurance) on the basis of the HMAA's leverage in the tying product market (health insurance), thereby forcing those buyers to forego free choice between sellers.

The sole proprietor market in Hawaii is not insignificant. According to the Division, HMAA currently has agreements with approximately one thousand sole proprietors. Additionally, the bill raises such questions as which market is to be measured; who makes that market determination; how is that determination made; what happens if there is a dispute as to market share; what would happen if there is an error in the market share determination; and what happens if the market share exceeds five percent after the tying arrangement is implemented.

Thus, we oppose any changes to the anti-tying provision. That provision is meant to eradicate certain evils, including the denial of free access to the market for the tied product, forcing buyers to forego their free choice between competing tied products, and restraining free competition in the market for the tied product. Consequently, we respectfully oppose this measure and ask that it be held.

Blue Cross
Blue Shield
of Hawaii

An Independent Licensee of the Blue Cross and Blue Shield Association

February 20, 2008

The Honorable Russell Kokubun, Chair
The Honorable David Ige, Vice Chair

Senate Committee on Commerce, Consumer Protection and Affordable Housing

Re: SB 2314 SD1 – Relating to Insurance

Dear Chair Kokubun, Vice Chair Ige and Members of the Committee:

The Hawaii Medical Service Association (HMSA) appreciates the opportunity to testify on SB 2314 SD1 which would exempt small health plans that occupy less than five per cent of the health care market from adhering to a portion of the Insurance Code dealing with unfair methods of competition and unfair or deceptive acts or practices. HMSA opposes this measure in its current form.

Unfortunately, the current language of this measure would allow health plans with less than a five percent share of the local market to engage in an activity that would be prohibited for both HMSA and Kaiser Permanente. We believe that this would create an unlevel playing field for plans operating in the State and that regulation should not be selective.

If however, it is the Committee's will to move this measure forward we would request a small amendment to ensure that all health plans are regulated fairly. This would be accomplished by amending the language on Page 5, Lines 17 – 22 through Page 6, Lines 1-3 by removing reference to a health plan's market share. This section would then read as follows:

provided that this subparagraph shall not apply to any insurer subject to chapter 432 offering contracts for dental and vision insurance as a condition, agreement, or understanding to the new health insurance policy or renewal of a health insurance policy under chapter 432;

This would ensure that all health plans in the State are operating under the same regulatory guidelines. Thank you for the opportunity to testify on SB 2314 SD1.

Sincerely,

Jennifer Diesman
Director, Government Relations

**SENATE COMMITTEE ON
COMMERCE, CONSUMER PROTECTION AND
AFFORDABLE HOUSING**

February 21, 2008

SB 2314, SD 1 Relating to Insurance

Chair Kokubun and members of the Senate Committee on Commerce, Consumer Protection and Affordable Housing, I am Rick Tsujimura, representing State Farm Insurance Companies, a mutual company owned by its policyholders.

State Farm supports Senate Bill 2314, SD 1 Relating to Insurance as drafted and urges passage unamended.

Thank you for the opportunity to present this testimony.

LATE

BEFORE THE

SENATE COMMITTEE ON COMMERCE, CONSUMER PROTECTION, AND AFFORDABLE HOUSING
Senator Russell S. Kokubun, Chair
Senator David Y. Ige, Vice Chair

SB 2314, SD1 RELATING TO INSURANCE

TESTIMONY OF
JOHN HENRY FELIX
Chairman of the Board and Chief Executive Officer

February 21, 2008, 9:00 am
State Capitol Conference Room 229

Chair Kokubun, Vice Chair Ige, and Committee Members:

My name is John Henry Felix, Chairman of the Board and Chief Executive Officer of Hawaii Medical Assurance Association (HMAA). HMAA **STRONGLY SUPPORTS** SB 2314, SD1, which would enable small insurers that occupy less than five percent of the health insurance market to continue combining different types of health and sickness-related insurance benefits into a single unified policy. **SB 2314, SD1 has been amended to limit its application to health insurers only, as reflected in the addition of the applicable statutory language "accident and health or sickness" insurers.**

I. Background to HMAA and the Need for this Bill

By way of background, HMAA is a non-profit mutual benefit society which provides health insurance to over 30,000 Hawaii residents. HMAA occupies about three percent of Hawaii's health insurance market. As a small insurer, HMAA takes special pride in providing health insurance to sole-proprietors and small businesses, a segment of Hawaii's market which has a difficult time obtaining affordable health related insurance.

SB 2314, SD1 is intended to help self-employed workers and small businesses by continuing to allow broader coverage for less cost. This bill is necessary because the current administration has recently chosen to interpret Hawaii law in a different way than it has ever been interpreted by prior administrations, to prohibit the combination of drug and medical coverage, or the combination of medical, dental and drug coverage,

or any other combination of health related coverages, into one insurance policy. Numerous Hawaii laws already permit the combination of various types of health coverages under one policy, and this should be encouraged, not discouraged, to help provide the broadest health coverage possible for Hawaii's residents.

II. The Insurance Commissioner's Departure from Practice and Judicial Precedent

Since its inception in 1989, HMAA's medical plans have always included life insurance, and its sole proprietor/independent contractor plans have always included medical, dental, vision, and prescription drug coverage.

Although prior Insurance Commissioners have accepted HMAA's practice for the last 18 years, the current administration has departed from those years of acceptance and deemed these combined benefits as a violation of state anti-tying laws. This administration is doing so even though the U.S. Supreme Court has made clear that a company with less than 30% market share has no coercive power in the marketplace and cannot violate federal anti-tying laws. *Jefferson Parish Hospital v. Hyde*, 466 U.S. 2 (1984). Consistent with the federal standard, SB 2314, SD1 will encourage the existing practice by smaller accident and sickness insurers to "bundle" together different classes of insurance, such as health, dental, and vision, thereby continuing the State's historical acceptance of this practice by small insurers who lack coercive power in the marketplace. In these circumstances, bundling provides broader health care coverage in single unified policies, ultimately resulting in lower overall premiums, fostering greater competition within the Hawaii insurance marketplace, and providing consumers with greater flexibility, coverage and pricing options.

SB 2314, SD1 codifies into Hawaii law the same rules applicable to similar federal anti-tying laws, though using a more conservative standard of 5% market share. SB 2314, SD1 does not change the Prepaid Health Care Act in any way, but rather simply provides that HMAA's 18 year practice of providing broad, cost- effective benefits to Hawaii's smallest business groups is not an unfair insurance practice. Without passage of SB 2314, SD1 hundreds of sole-proprietors, small businesses, and their families currently insured by HMAA could be forced to shop for more expensive individual policies with much less coverage.

III. Misleading Testimony Provided to Date

This bill, and its companion H.B. No. 2256, H.D.1, have come under irrational, unfair and at times outright false criticism to which I must respond so that this Committee may have the benefit of an accurate record.

A. False Testimony Regarding HMAA's Market Power

In prior testimony with respect to H.B. No. 2256, H.D.1, the Insurance Commissioner attempted to confuse the issue by claiming that HMAA has nearly one hundred percent (100%) of the "market" for accident and sickness insurance policies issued to sole proprietorships. *See* Testimony of Insurance Commissioner dated February 14, 2008 re: H.B. No. 2256, H.D.1, at p. 2, and that HMAA therefore has "market power" even though HMAA has less than five percent (5%) of the market for accident and sickness insurance policies generally.

However, the Insurance Commissioner admits that "[o]ther insurers could sell group insurance to sole proprietors but they are not required to do so by law . . . so they don't." *Id.*, at p. 3. Plainly, if other insurers are free to sell group insurance to sole proprietors, HMAA cannot have any market power because if HMAA raises its premiums above competitive levels, other insurers would be free to start selling policies to sole proprietors. Thus, the Insurance Commissioner's claim that, on the one hand, HMAA has market power *vis a vis* sole proprietors, but, on the other hand, other insurers can sell group policies to sole proprietors, is contradictory and illogical.

In fact, HMAA does not control a majority of the sole proprietor / independent contractor market. HMAA currently covers 932 of these individuals. The annualized gross premium is currently $5.4 million out of HMAA's 2007 actual gross premium of $96 million. The premium is not significant, but the benefit to the sole proprietor/independent contractor is. *If HMAA were to cease offering this plan, the loss of premium would be equivalent to HMSA losing a single large group.*

The Attorney General's own testimony of February 14, 2008 stated "The sole proprietor market in Hawaii is not insignificant. According to the latest U.S. Census Bureau report (2004), 16,503 out of 31,605 Hawaii business, or 52%, have one to four employees." (emphasis added). *This would suggest that HMSA's Individual Business Plan, and not HMAA's plan that covers only 932 individuals, has the market share.*

Given the foregoing, and in light of the Insurance Commissioner's necessary concession that "[o]ther insurers could sell group insurance to sole proprietors," the attempt to impute market power to HMAA even though HMAA has less than a five percent (5%) market share must be rejected. Other insurers can sell group insurance to sole proprietors. If HMAA or another insurer offers bundled products that consumers do not want, other insurers can step in to offer products to satisfy that demand. This is how competitive markets work. If anything, the Insurance Commissioner's anti-bundling rules are anti-competitive because they prevent the development of bundled products in a competitive market by insurers who lack coercive market power.

B. False Testimony Regarding the Practice of Bundling

Also in prior testimony regarding H.B. 2256, the Insurance Commissioner asserted that HMAA is the only health insurer which bundles, stating "H.B. 2256 would allow insurers with less than a 5% market share to force consumers to purchase a bundle of insurance products as a condition of sale. The Insurance Division is aware of only one insurer engaging in this practice presently and that is the health insurer ....HMAA".

This statement is not true. HMSA's "Individual Business Plan" has been available to sole proprietors and independent contractors for the last decade. It, too, combines medical, drug, vision, dental, and life insurance in one plan. However, HMSA and other insurers elect to treat the sole proprietor and independent contractors as individuals for insurance purposes, and not as 'groups' protected by the Hawaii Prepaid Health Care Act.

This election by other insurers reduces benefits and imposes additional eligibility rules to the detriment of sole proprietors and independent contractors, including the ability to deny coverage and a 12-month waiting period before benefits begin for certain conditions, such as:

Aids and HIV	Reflux Disease
Alzheimer's Disease	Hearing Loss
ALS	Heart, blood, and blood vessel diseases
Anemia for congenital or hereditary blood disorders	Hepatitis other than Hepatitis A
Arthritis	High blood pressure
Asthma	Multiple sclerosis
Cancer	Osteoporosis
Cataracts	Pelvic inflammatory disease
Cerebral Palsy	Radiculopathy
Cirrhosis of the liver	Reconstructive surgery for a previous illness or injury
Chronic Obstructive Pulmonary Disease	Sleep Apnea
Cohn's Disease	Spinal disk problems
Diabetes	Surgery and services related to hemorrhoids, hernia, tonsils, adenoids, and varicose veins
Diverticulitis	Thyroid conditions
Dysfunctional uterine bleeding	Tuberculosis
Endometriosis	Ulcers
Fibromyalgia	Urinary Incontinence
Gall Bladders disease and gallstones	Transplants

HMAA protects the sole proprietors and independent contractors by electing to treat them as regular groups. This means that there is **no waiting period** before benefits begin. This has been HMAA's mission since its inception. It was formed specifically to give the 'little guy' as good or better benefits as so-called regular companies including the 'big guys'.

C. False Testimony Alleging Kick-Backs

In his prior testimony regarding H.B. 2256, the Insurance Commissioner alleged that HMAA "got a rebate, or "kick-back" if you will, from the life insurer of profits on the bundled life insurance." **This statement is an absolute falsehood.** HMAA's contract with Hartford Life insurance contains a *profit sharing* provision. This is *not* a rebate and *not* a 'kick-back'.

For policy year ended 1/31/02, HMAA received a profit sharing check in the amount of $34,909. This money went directly to the mutual benefit society, as recorded in HMAA's audited financial results. There have been no profit sharing payments since 2002.

HMAA's subscribers personally choose the beneficiary of their life insurance policy, whether it be a family member, child, grand child, or significant other.

HMAA's life insurance benefits paid to consumers for policy years ending January 31 since 2002 have been:

$347,817
$419,208
$387,536
$467,358
$262,222
$540,000 for policy year ended January 31, 2007

for a total of $2.9 million.

These benefits have gone to families that in most cases had no other life insurance. It has made a substantial difference to the loved ones of HMAA subscribers. These benefits include all of payments to HMAA subscriber beneficiaries, and not just sole proprietors. Although the insurance division's testimony refers only to sole proprietors, it is on record as also opposing life insurance included in HMAA's medical plans for larger groups.

If the legislature eliminates this benefit for sole proprietors/independent contractors, the Division's likely next step is to also eliminate it for larger groups.

D. Misleading Testimony Regarding Benefits to Consumers

The Insurance Commissioner further claims that bundling will hurt the consumer because it will eliminate consumer choice and that any savings will be retained by HMAA. Specifically, in his prior testimony regarding H.B. 2256, the Commissioner represented that "[t]he Committee should understand that allowing this practice does not mean lower premiums for the insured."

This statement is also incorrect. HMAA's actuary, Thomas J Parciak, FSA, MAAA, of AON Consulting, has made the following analysis of the consequences of un-bundling:

> "For HMAA to unbundle their various product offerings, the premiums you would need to charge would increase from current levels, likely to a point of becoming prohibitively expense for this population.
>
> You would also need to seriously consider whether HMAA should continue to offer some of these products.... At all, as they have a very high likelihood of anti-selection [adverse selection] when offered separately.
>
> Finally, further fragmenting this already small population into coverage-specific groups would potentially jeopardize the credibility of the various groups for pricing purposes, making it very difficult for HMAA to effective price any of the coverages. This puts the viability of these Small Business Plan offerings into question."

This information was provided to the Insurance Division in 2006. And, the Commissioner knows that his position, if unchanged, will also require health plans to incur additional costs - that will be passed on to consumers - for administering numerous different policies instead of a unified policy. His actions will deprive Hawaii's businesses and employees low cost, broad coverage health policies, and will destroy cost efficiencies and lower prices that can result from combining broad health coverage within the same insurance policy.

E. Bundling of Life Insurance is Mandated by Current Law

For groups of two or more, HMAA's plan includes life insurance and accidental death and dismemberment benefits. The Division's insistence that these benefits be "unbundled" is contrary to existing Hawaii law, which requires mutual benefit societies to bundle life insurance if they choose to offer it:

431:10D-208. Mutual benefit society groups.

The lives of a group of individuals may be insured under a policy issued to a mutual benefit society, which shall be deemed the policyholder, to insure members of the society for the benefit of persons other than the society or any of its officials, subject to the following requirements:

. . .

(7) The amounts of insurance under the policy must be based upon some plan precluding individual selection either by the members or by the society.

See Haw. Rev. Stat. § 431:10D-208(7) (emphasis added). Plainly, the only reasonable interpretation of the statutory mandate to offer the insurance in such a manner so as to "preclude[] individual selection either by the members or by the society" is to require that it be uniformly provided to all members, just as HMAA has been doing for years. The Division's position is squarely at odds with section 431:10D-208(7), and should be rejected accordingly.

Thank you for the opportunity to correct the record, and to testify on this matter of critical importance. HMAA **STRONGLY SUPPORTS** SB 2314, SD1 and urges the passage of this measure.

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