

**STATE OF CALIFORNIA  
DEPARTMENT OF INSURANCE  
45 Fremont Street, 24<sup>th</sup> Floor  
San Francisco, California 94105**

**INITIAL STATEMENT OF REASONS**

**Date: October 14, 2011**

**Regulation File: REG-2011-00020**

**INTRODUCTION**

The Insurance Commissioner proposes to adopt amendments to California Code of Regulations (“CCR”) Title 10, Chapter 5, Subchapter 2, Article 1, sections 2202(b), 2202(c), 2202(d) and 2202(e). (All references to the CCR in this Notice are references to sections in CCR Title 10.) The Commissioner proposes to amend these sections under the authority granted by California Insurance Code (“CIC”) sections 742.43, 779.21, 10168.92, 10192.3, 10234, 10327, 10506, 10506.3, 10704, and 12973.9.

The Commissioner proposes to amend sections 2202(b), 2202(c) and 2202(d) to adjust the fees he charges insurance providers for processing, indexing and maintaining copies of documents defined in CCR sections 2201(a) and 2202(a). In addition, the Commissioner proposes to amend section 2202(e) to allow the Commissioner the flexibility to adjust a fee, when circumstances warrant, in a manner that is not necessarily uniform with fee adjustments in other filing classifications.

**SPECIFIC PURPOSE AND REASONABLE NECESSITY FOR THE PROPOSED AMENDMENTS TO THE REGULATIONS**

The specific purpose of each amendment and the rationale for the Commissioner’s determination that each amendment is reasonably necessary to carry out the purpose for which it is proposed is set forth below.

**Amendments to the fees set forth in CCR sections 2202(b), 2202(c,) and 2202(d):**

Under existing law, when the Insurance Code requires that a document (defined by CCR sections 2201(a) and 2202) be filed with, submitted to, or approved by the Commissioner, “fees as provided for by [CIC section 12973.9] shall be paid to the commissioner to cover the expenses of processing and indexing the same and maintaining copies of the same.” Insurance Code section 12973.9. The fees which the Commissioner may charge for actions on documents submitted to him are set forth in CCR sections 2202 and 2203. The documents categorized in these provisions reflect various health, life and workers' compensation forms, among others, that are ultimately reviewed by the Department's Policy Approval Bureau ("PAB") and Financial Surveillance Branch ("FSB").

On October 19, 2009, the Commissioner noticed regulations designed to rectify a shortfall

between the fees collected (revenue) and the Commissioner's direct and indirect costs associated with processing, indexing and maintaining copies of the filings. (See Regulation File: REG-2009-00023). At the time of this rulemaking, there had been no fee increase for documents submitted pursuant to CCR sections 2202 and 2203 for a period of twelve years. This effectively required other fee-generating sections of the Department to make up the shortfall. This filing was approved by OAL on March 29, 2010, resulting in the Commissioner's implementation of a fee increase on the same date. In measuring the revenue obtained by the fee increases, however, it became clear that the Commissioner was not fully rectifying the shortfall between costs and revenue and a closer look at the methodology used to calculate the fee increases was required. From this analysis, it became clear that only partial recoupment was occurring because the methodology earlier employed used erroneous data in calculating the number of annual filings received by the Commissioner pursuant to CCR sections 2202 and 2203. Specifically, the Commissioner relied upon using the number of policy forms filed annually to calculate the fee increase, not taking into account that many filings have multiple forms. This led to the use of an artificially high number to use for annual filings, and thus, even the fee increase did not yield sufficient revenue to offset the Commissioner's costs in performing the processing functions.

For Fiscal Year (FY) 2010-11, there is currently a \$3.7 million shortfall in the revenue collected by the Commissioner for review of filings pursuant to CCR sections 2202 and 2203. Other revenue sources of the Department of Insurance, primarily general fees and license revenue, will be required to cover this shortfall. This is on top of the revenue shortfall of \$4.4 million for FY 2009-10 despite the implementation of the new fee schedule in the second half of the fiscal year. Until this shortfall is rectified, other revenue sources of the Department will be required to cover the multi-million annual shortfall between expenses incurred and fees charged insurers for document processing. In effect, the Department's other revenues are subsidizing insurance company operating expenses because current fee levels are inadequate.

The data and methodology have since been thoroughly reviewed and corrected and the fees in the proposed regulation are expected to come into full alignment with the Commissioner's costs. The proposed fee increase requires a uniform percentage increase for all fees in CCR section 2202(a) except for the class of forms referenced in sections 2202(a)(12) and 2202(a)(13). The latter forms include the categories of "Life Insurance Policies and Annuity Contracts Subject to Nonforfeiture Laws" and "Grants and Annuities." These categories of forms rely more heavily on the review by employees of FSB as opposed to PAB. After careful consultation with the FSB, it was determined that two of the forms actually merited a decrease, and one of the forms, while requiring an increase, required such at a much lower percentage than the other filings included in CCR section 2202, subdivision (a).

The proposed amendments amend the fees set forth in CCR sections 2202(b), 2202(c), and 2202(d) in order to cover the cost of processing insurance filings. The fee changes do not exceed the amounts calculated by the Department of Insurance's Budget Office as necessary to cover all direct and indirect costs of the unit(s) for the next succeeding fiscal year and years thereafter. There are no other moneys received or projected to be received for the unit(s) processing the documents subject to such fees. The purpose of the

proposed amendments is to correct fee levels so that fees charged reflect more accurately the actual costs incurred in processing, indexing, and maintaining documents as required by law. It is reasonably necessary to make these corrections in order to stop the unsustainable cash flow imbalance currently taking place.

Amendment to CCR section 2202(e):

This rulemaking also makes proposed changes to section 2202(e). Specifically, as currently worded, this provision generally requires a uniform percentage for any increase or decrease in the fees for filings under CCR sections 2202 and 2203. However, it also contains a confusing series of purported exceptions to this rule. Moreover, while it makes sense as a general proposition for the Commissioner to raise or lower rates on a uniform basis, the fundamental goal of exacting fees is to capture to the extent possible the processing costs associated with each filing classification. Thus, it makes much more sense for the Commissioner to have the flexibility to adjust a fee, albeit in a manner not always uniform with other fee changes, to allow for any variation in the expenses associated with that specific filing classification. The language in section 2202(e) has been modified accordingly.

### **SPECIFIC TECHNOLOGIES OR EQUIPMENT**

Adoption of the proposed amendments to the regulations would not mandate the use of specific technologies or equipment.

### **IDENTIFICATION OF STUDIES**

There are no specific studies relied upon in the adoption of the proposed amendments to the regulations.

### **REASONABLE ALTERNATIVES**

The Commissioner has determined that no reasonable alternative exists to carry out the purpose for which the amendments to the regulations are proposed. Performance standards were considered but were rejected as an unreasonable and impracticable alternative to simply amending the existing regulations.

### **ECONOMIC IMPACT ON SMALL BUSINESS**

The Commissioner has identified no reasonable alternatives to the proposed regulations, nor have any such alternatives been brought to the attention of the Department, that would lessen any impact on small businesses. Although performance standards were considered as an alternative, they were rejected because they were not as effective as amendments to the regulations in revising fee amounts. The Commissioner has made an initial determination that the adoption of the proposed amendments will not affect small businesses because insurers are not small businesses under Government Code section 11342.610(b)(2).

## **PRENOTICE DISCUSSIONS**

The Commissioner has not conducted prenotice public discussions pursuant to Government Code Section 11346.45 because he has concluded that the proposed regulation amendments do not “involve complex proposals or a large number of proposals which cannot be easily reviewed during the comment period.” Government Code section 11325.46(a).