

GAO

Briefing Report To The Chairman,  
Subcommittee on Commerce, Transport,  
and Tourism, Committee on Energy and  
Commerce, House of Representatives

January 1987

# INSURANCE DEPARTMENTS

## Trends in Resources and Workloads in Delaware, North Carolina, and Ohio



132118

*Released 2/9/87*  
RESTRICTED—Not to be released outside the General  
Accounting Office except on the basis of specific  
approval by the Office of Congressional Relations.

RELEASED

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

---

Office of the Chief Economist

B-225255

January 9, 1987

The Honorable James J. Florio  
Chairman, Subcommittee on Commerce,  
Transportation, and Tourism  
Committee on Energy and Commerce  
House of Representatives

Dear Mr. Chairman:

In response to your January 21, 1986, letter, we obtained information on insurance regulation by the state insurance departments in Delaware, North Carolina, and Ohio. We agreed to give you a briefing report on

- the types and amounts of financial resources available in recent years;
- the number and types of personnel resources available, including actuaries and other specialists;
- the departments' regulatory activities or workloads (e.g., numbers of rate filings reviewed and financial examinations conducted); and
- recent state initiatives concerning the availability and affordability of commercial liability insurance.

Our principal findings follow.

FINANCIAL RESOURCES

The financial resources available to each of the three state insurance departments increased considerably between 1980 and 1986.

- In current dollars, Delaware's state-provided insurance budget increased by 44 percent (from \$582,800 to \$837,600); North Carolina's by 135 percent (from \$5,093,543 to \$11,980,204); and Ohio's by 134 percent (from \$2,666,521 to \$6,232,099).

- Expressed in 1982 dollars to account for the effects of inflation, Delaware's state-provided budget increased by 4 percent (from \$711,382 to \$740,747); North Carolina's 70 percent (from \$6,217,324 to \$10,594,918); and Ohio's by 69 percent (from \$3,254,832 to \$5,511,474).

In addition to state-provided resources, Delaware received about \$725,300 in 1985 and \$804,000 in 1986 from non-government sources (i.e., regulated insurance companies and state guaranty associations) to fund the insurance department's Bureau of Examination, Rehabilitation, and Guaranty. Considering these non-government funds together with state-provided funds, the financial resources available to Delaware's insurance department increased by 182 percent in nominal dollars and by 104 percent in real, inflation-adjusted dollars between 1980 and 1986.

In each of the three states, the costs of state-required financial examinations are paid for by the insurance companies.

#### PERSONNEL RESOURCES

The personnel in each of the three insurance departments also increased between 1978 and 1986.

- Delaware's available staff increased by 80 percent (from 20 to 36); North Carolina's by about 19 percent (from 204 to 242); and Ohio's by about 40 percent (from 93 to 130).
- Selected specialists in each of the three insurance departments at least doubled between 1978 and 1986.

#### REGULATORY ACTIVITIES

- The National Association of Insurance Commissioners (NAIC) has established detailed guidelines for conducting financial condition and market conduct examinations. We found no other appropriate criteria to evaluate a state insurance department's performance in regulating the insurance industry.
- Trends between 1977 and 1985 in various workload measures were mixed. For example, Delaware and North Carolina processed more than twice as many applications for agent licenses in 1985 than in 1977 and Ohio processed nearly twice as many. On the other hand, North Carolina and Ohio conducted about the same number of examinations of state-chartered

insurance companies in 1985 as in 1977, while Delaware conducted over three times as many in 1985. The increase in Delaware resulted from a substantial growth in the number of Delaware-chartered companies during this time period.

- In each of the three states, the largest share of regulatory resources was for financial evaluation. According to insurance department officials, each of the states follows the guidelines established by NAIC for conducting financial condition examinations. Examinations of state-chartered insurance companies are routinely conducted once every 3 years in each state. At the time of our fieldwork, Delaware had 187 state-chartered companies, North Carolina had 103, and Ohio had 259. Delaware's insurance department contracts with certified public accounting firms to conduct its on-site financial examinations. In North Carolina and Ohio, department staff conduct these examinations.
- State insurance department officials in each of the three states also told us that they conduct in-house reviews of annual financial statements submitted by state-chartered and other insurance companies conducting business in their state. More than 1,000 insurance companies do business in each of these states.

#### RECENT STATE INITIATIVES

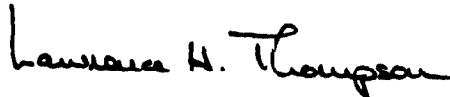
- Each of the three states has taken certain actions concerning the availability and affordability of commercial liability insurance. For example, according to state insurance officials, each state took executive or legislative action to limit mid-term policy cancellations.
- Legislation has been proposed in each of the three states to reform state liability laws, including proposals to cap contingency fees and to limit the size of punitive damage awards.

As you requested, we obtained oral comments from officials of the three state insurance departments. Their views have been incorporated into this briefing report where appropriate.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the report date. At that time we will send copies to the insurance departments in Delaware, North Carolina, and Ohio; the National Association of Insurance Commissioners; and other interested parties. We will also make copies available to others upon request.

Should your staff desire additional information on these matters, please call James L. Bothwell on 275-5985.

Sincerely yours,

A handwritten signature in dark ink, appearing to read "Lawrence H. Thompson". The signature is written in a cursive style with a large initial "L".

Lawrence H. Thompson  
Chief Economist

# C o n t e n t s

| SECTION    |   | <u>Page</u> |
|------------|---|-------------|
| 1          | BACKGROUND  | 7           |
| 2          | OBJECTIVES, SCOPE, AND METHODOLOGY  | 9           |
| 3          | FINANCIAL RESOURCES   | 10          |
| 4          | PERSONNEL RESOURCES   | 16          |
| 5          | REGULATORY ACTIVITIES   | 23          |
| 6          | RECENT STATE INITIATIVES  | 29          |
| <br>FIGURE |   |             |
| 3.1        | Changes in Financial Resources, Delaware Insurance Department, 1980-86                | 12          |
| 3.2        | Changes in Financial Resources, North Carolina Insurance Department, 1980-86          | 13          |
| 3.3        | Changes in Financial Resources, Ohio Insurance Department, 1980-86                    | 14          |
| 6.1        | Delaware Department of Insurance Responsibilities by Major Organizational Group       | 32          |
| 6.2        | North Carolina Department of Insurance Responsibilities by Major Organizational Group | 33          |
| 6.3        | Ohio Department of Insurance Responsibilities by Major Organizational Group           | 34          |
| <br>TABLE  |   |             |
| 3.1        | Financial Resources for Three State Insurance Departments, 1980-86                    | 15          |
| 4.1        | Available Full-Time Staff in 1978 and 1986  | 16          |
| 4.2        | Available Full-Time Staff by Occupational Category                                    | 18          |
| 4.3        | Classification of Selected Professionals for the Three State Insurance Departments    | 19          |

|     |   | <u>Page</u> |
|-----|---|-------------|
| 4.4 | 1986 Allocation of Authorized Personnel<br>by Function                | 21          |
| 5.1 | Workload Measures for the Three State<br>Insurance Departments        | 25          |
| 5.2 | Number of Insurance Companies and<br>Financial Examiners by State     | 28          |
| 6.1 | Recent State Initiatives Concerning<br>Commercial Liability Insurance | 30          |

#### ABBREVIATIONS

|      |   |
|------|---|
| CPA  | certified public accountant                     |
| GAO  | General Accounting Office                       |
| HMO  | health maintenance organization                 |
| NAIC | National Association of Insurance Commissioners |

## SECTION 1: BACKGROUND

Traditionally, state governments regulate the insurance industry. Each state has an insurance regulatory agency whose main mission is to (1) monitor the solvency of insurance companies conducting business in the state; (2) ensure that insurance rates are adequate, but not excessive or unfairly discriminatory; and (3) ensure that insurance is generally available in the state. In Delaware and North Carolina, the insurance regulatory agency is headed by an elected insurance commissioner who serves a 4-year term. In Ohio a superintendent of insurance appointed by the governor heads the insurance department.

Although the specific laws, resources, and regulatory philosophies vary among the states, state insurance departments generally perform the same basic insurance functions.

1. License insurance companies and agents to conduct business in the state.
2. Examine the financial condition of insurance companies.
3. Implement statutory requirements for regulating such matters as insurance rates and the content of insurance policies.
4. Administer a complaint-handling office.
5. Enforce unfair trade practices laws.
6. Regulate residual market mechanisms designed to provide insurance for risks rejected by the voluntary insurance market, e.g., automobile assigned risk plans.

In addition, North Carolina's department of insurance performs certain functions not related to insurance regulation, such as administering fire safety programs. These non-insurance-related activities account for approximately 30 percent of the department's budgetary resources each year, and accounted for about 26 percent of the department's total authorized personnel in 1986.

States must regulate several types of insurance, types of companies, and ways of buying insurance. For example, one may buy insurance (1) directly from the employees of the company (direct writers); (2) from people who act as representatives of one or more companies (agents); or (3) from those who act as representatives of the buyer (brokers).

For the purposes of state insurance regulation, insurance is divided into two broad categories: (1) life, accident, and health and (2) property/casualty. Property and casualty

insurance covers over 20 lines of insurance, including property, automobile, burglary and theft, credit, workers' compensation, and liability (products, malpractice, etc.). Except for personal lines of insurance, such as automobile and homeowners, the property and casualty insurance business is primarily commercial. State insurance departments generally rely on competition as the means to ensure that property and casualty coverage is available and affordable to businesses.

The current affordability and availability difficulties in liability insurance are found principally in certain liability insurance lines. Medical malpractice and general liability insurance are two lines frequently mentioned by the media as having substantial difficulties.

## SECTION 2: OBJECTIVES, SCOPE, AND METHODOLOGY

The Chairman of the Subcommittee on Commerce, Transportation, and Tourism, House Committee on Energy and Commerce, asked us to review insurance regulation by the state insurance departments in Delaware, North Carolina, and Ohio. Our objective was to obtain information on

- the types and amounts of financial resources available in recent years;
- the number and types of personnel resources available, including actuaries and other specialists;
- the departments' regulatory activities or workloads (e.g., numbers of rate filings reviewed and financial examinations); and
- recent state initiatives concerning the availability and affordability of commercial liability insurance.

Another objective was to compare, where possible, the information obtained during this review with the information documented in GAO's 1979 report on state insurance regulation.<sup>1</sup>

The primary data source for our review was a questionnaire, developed from the one we used for our earlier report, sent to each of the three states. We did not independently verify the responses received, but we did ask state insurance department officials to review and verify the information in this report pertaining to their state insurance departments.

To supplement information from the questionnaire, we conducted fieldwork from March through May of 1986. We interviewed state insurance commissioners and their staff, key state legislators, and members of affected interest groups. We also interviewed members of several national insurance organizations and other knowledgeable individuals in an attempt to identify criteria for evaluating the adequacy of the three states' regulatory resources. Although the National Association of Insurance Commissioners (NAIC) has established detailed guidelines for conducting financial condition and market conduct examinations, we found no other criteria to evaluate either the adequacy of the resources available to state insurance departments or the departments' performance in regulating the insurance industry.

---

<sup>1</sup>Issues and Needed Improvements in State Regulation of the Insurance Business (PAD-79-72, Oct. 9, 1979).

### SECTION 3: FINANCIAL RESOURCES

In each of the three states reviewed, the nominal dollar amounts of the state-provided insurance budgets have increased considerably since 1980. Between 1980 and 1986, the budget increased by 44 percent in Delaware, 135 percent in North Carolina, and 134 percent in Ohio. Figures 3.1, 3.2, and 3.3 illustrate how each state insurance department's budget changed over the 7-year period. Table 3.1 shows the budget amounts for each state by fiscal year.

State insurance officials told us the following about recent budget increases:

- Delaware's increased funds were used to hire additional staff, purchase computers, and contract for services.
- North Carolina's increased funds were used to purchase computers, hire an actuary and additional financial examiners, expand the consumer complaint unit, and cover the costs of administering new risk management programs and of regulating workers' compensation self-insurance. The last responsibility was transferred to the department in 1985.
- Ohio's increased funds were used to purchase computers, establish a fraud division, raise financial evaluation staff salaries, and contract with actuarial consultants to analyze insurance rate requests.

When inflation is taken into account, the state-provided departmental budgets, expressed in terms of 1982 dollars, increased by 4 percent in Delaware, 70 percent in North Carolina, and 69 percent in Ohio between 1980 and 1986.

In 1985 Delaware established the Bureau of Examination, Rehabilitation, and Guaranty within the insurance department to (1) centralize and strengthen all those regulatory activities concerned with insurance company solvency, including the review of financial statements and insurance rates; (2) manage any insurance companies in rehabilitation; and (3) monitor the state's guaranty associations. The bureau is financed by special fees and charges levied on insurance companies and state guaranty associations, not by state-provided funds. When the bureau's funds, which totaled about \$725,300 in fiscal year 1985 and \$804,000 in fiscal year 1986, are added to the state-provided budget amounts, the financial resources available to Delaware's insurance department increased by 182 percent between 1980 and 1986 in terms of nominal dollars and by 104 percent in terms of real, inflation-adjusted dollars.

In addition to receiving the amounts reflected in their state-provided budgets, two of the three departments reported having other state resources available to them.

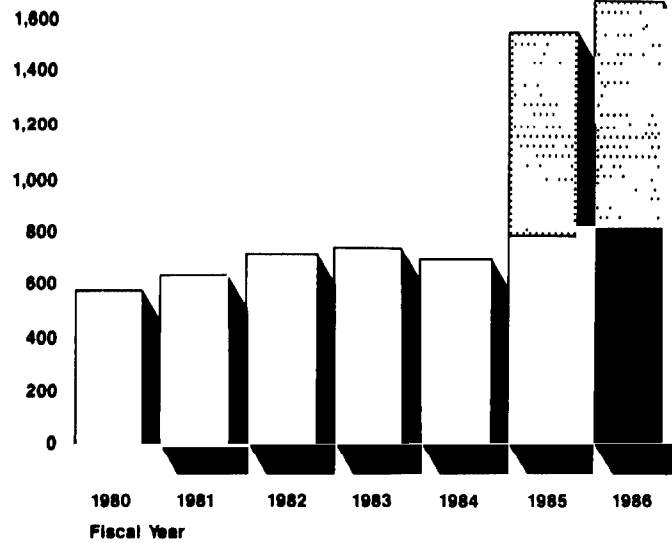
- The North Carolina department receives legal assistance from the state attorney general's office and reimbursements for any expenses related to state guaranty funds or placing companies in receivership.
- The Ohio department receives legal assistance from the state attorney general's office.

Also, insurance companies in all three states bear the costs of state-required financial examinations. Delaware estimates that such costs amount to about \$3 million per year. In North Carolina and Ohio, insurance companies reimbursed the departments about \$1.1 million and \$2 million, respectively, in fiscal year 1985 for financial examination costs.

**Figure 3.1: Changes in Financial Resources, Delaware Insurance Department, 1980-86**

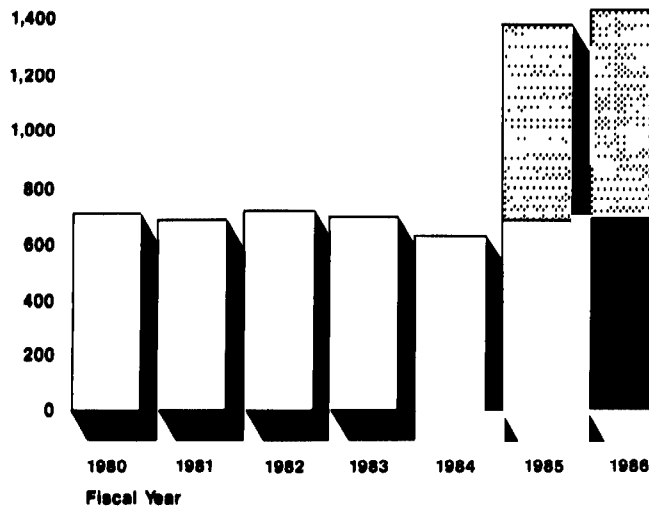
**Nominal Dollars**



(\$ Thousands)



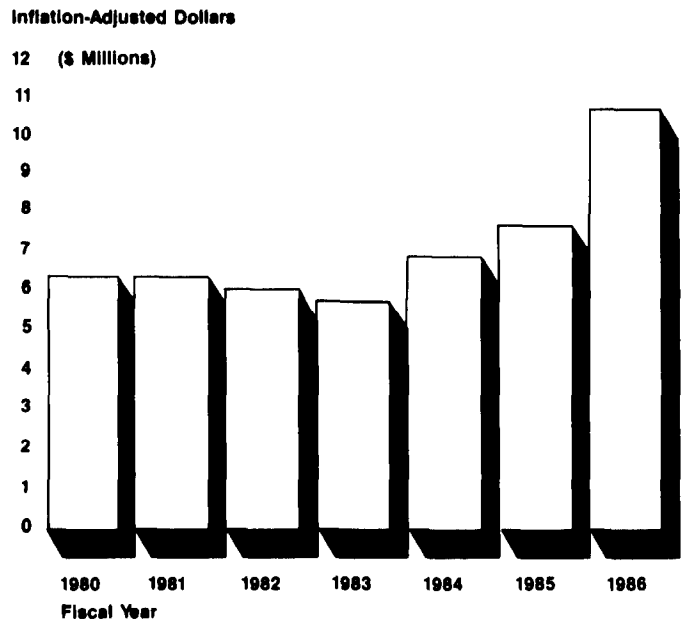
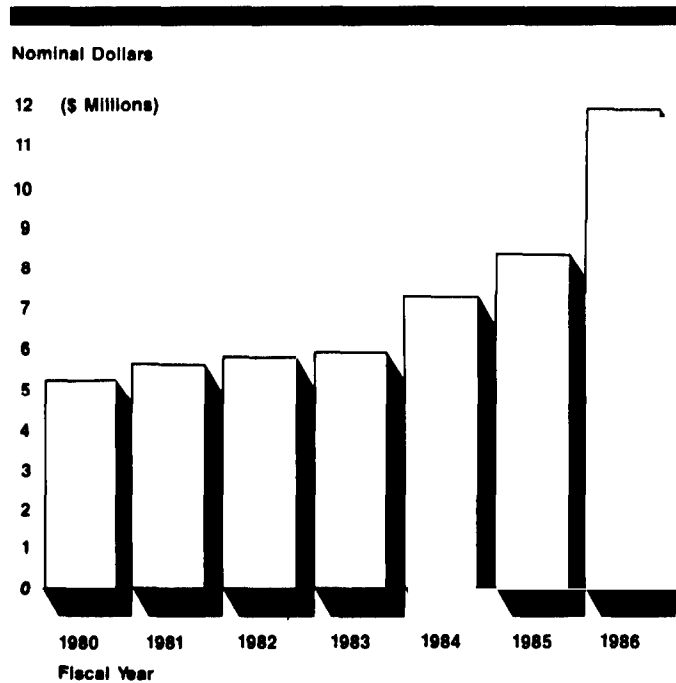
**Inflation-Adjusted Dollars**

(\$ Thousands)



-  State government appropriations
-  Bureau of Examination, Rehabilitation, and Guaranty funds

**Figure 3.2: Changes In Financial Resources, North Carolina Insurance Department, 1980-86<sup>a</sup>**



<sup>a</sup>According to department officials, the budget amounts shown include approximately 30 percent each year for non-insurance related activities such as enforcing building codes and conducting fire and rescue training

**Table 3.1: Financial Resources for Three State Insurance Departments, 1980-86**

| <b>Delaware<sup>a</sup></b>       |                        |   |
|-----------------------------------|------------------------|---|
| <u>Fiscal year</u>                | <u>Nominal dollars</u> | <u>Inflation-adjusted dollars<sup>b</sup></u> |
| ----- (thousands) -----           |                        |   |
| 1980                              | \$582.8                | \$711.4                                       |
| 1981                              | 626.2                  | 696.6   |
| 1982                              | 704.6                  | 724.2   |
| 1983                              | 721.9                  | 707.2   |
| 1984                              | 680.9                  | 643.0   |
| 1985                              | 1,531.4 <sup>c</sup>   | 1,396.0 <sup>c</sup>                          |
| 1986                              | 1,641.6 <sup>c</sup>   | 1,451.8 <sup>c</sup>                          |
| <b>North Carolina<sup>d</sup></b> |                        |   |
| <u>Fiscal year</u>                | <u>Nominal dollars</u> | <u>Inflation-adjusted dollars<sup>b</sup></u> |
| ----- (thousands) -----           |                        |   |
| 1980                              | \$5,093.5              | \$6,217.3                                     |
| 1981                              | 5,573.9                | 6,200.1                                       |
| 1982                              | 5,760.1                | 5,919.9                                       |
| 1983                              | 5,875.9                | 5,756.5                                       |
| 1984                              | 7,311.6                | 6,904.2                                       |
| 1985                              | 8,332.8                | 7,596.0                                       |
| 1986                              | 11,980.2               | 10,594.9                                      |
| <b>Ohio</b>                       |                        |   |
| <u>Fiscal year</u>                | <u>Nominal dollars</u> | <u>Inflation-adjusted dollars<sup>b</sup></u> |
| ----- (thousands) -----           |                        |   |
| 1980                              | \$2,666.5              | \$3,254.8                                     |
| 1981                              | 2,803.0                | 3,118.0                                       |
| 1982                              | 3,121.2                | 3,207.8                                       |
| 1983                              | 3,508.7                | 3,437.4                                       |
| 1984                              | 4,706.6                | 4,444.4                                       |
| 1985                              | 4,831.2                | 4,404.0                                       |
| 1986                              | 6,232.1 <sup>e</sup>   | 5,511.5                                       |

<sup>a</sup>Excludes amounts paid each year to contract examiners for financial examinations.

<sup>b</sup>Computed using the gross national product implicit price deflator. Amounts are expressed in 1982 dollars. Nominal and inflation-adjusted dollar amounts for 1982 budgets are not identical because the gross national product deflator is based on the calendar year, while state budgets are for fiscal years.

<sup>c</sup>These figures include funds to operate the Bureau of Examination, Rehabilitation, and Guaranty, which was established in fiscal year 1985--about \$725,300 and \$804,000 in nominal dollars, respectively, and \$661,167 and \$711,033 in inflation-adjusted dollars, respectively, for fiscal years 1985 and 1986.

<sup>d</sup>Amounts shown for North Carolina include about 30 percent each year for non-insurance-related activities.

<sup>e</sup>Estimate.

## Professional Staff

Table 4.2 shows how the number of available full-time professionals and clerks changed in each of the three state insurance departments between 1978 and 1986.

- The number of professional staff increased by 58 percent in Delaware (from 12 to 19), by 12 percent in North Carolina (from 150 to 168), and by 74.6 percent in Ohio (from 59 to 103).
- The number of clerical staff increased by 112.5 percent in Delaware (from 8 to 17), and by 37 percent in North Carolina (from 54 to 74), and decreased by 20.6 percent in Ohio (from 34 to 27).

Table 4.3 shows further detail on specific job categories of some of the departments' professional staff. The total number of specialists in each of the three insurance departments increased at least twofold between 1978 and 1986. Increases in the number of certified financial examiners accounted for slightly more than half (54 percent) of the net increases.

Each state also reported that it supplements its professional staff by purchasing professional consulting services. Specifically, the states reported the following major purchases during fiscal year 1985.

- Delaware spent \$48,000 on computer assistance and contracted with certified public accountant (CPA) firms for insurance company examinations.
- North Carolina spent about \$246,000 on contracting services for actuarial, legal, and computer assistance.
- Ohio spent about \$432,000 for external legal services and \$82,500 for hearing officers and a consulting actuary, who reviews rate filings.

**Table 4.3: Classification of Selected Professionals for the Three State Insurance Departments**

| Delaware   |                |                |  |
|--|----------------|----------------|--|
| <u>Profession</u>                                  | <u>1978</u>    | <u>1986</u>    |  |
| Attorneys  | 1 <sup>a</sup> | 1 <sup>b</sup> |  |
| Economists   | 0              | 0              |  |
| Certified public accountants                       | 0              | 0 <sup>c</sup> |  |
| Chartered life, property and casualty underwriters | 0 <sup>a</sup> | 0              |  |
| Certified financial examiners                      | 0 <sup>a</sup> | 2              |  |
| Actuaries  | <u>1</u>       | <u>1</u>       |  |
| Total  | <u>2</u>       | <u>4</u>       |  |

| North Carolina                                     |                      |             |  |
|--|----------------------|-------------|--|
| <u>Profession</u>                                  | <u>1978</u>          | <u>1986</u> |  |
| Attorneys  | 6                    | 11          |  |
| Economists   | 0                    | 1           |  |
| Certified public accountants                       | 2                    | 10          |  |
| Chartered life, property and casualty underwriters | 5                    | 2           |  |
| Certified financial examiners                      | 5                    | 10          |  |
| Actuaries  | <u>0<sup>a</sup></u> | <u>2</u>    |  |
| Total  | <u>18</u>            | <u>36</u>   |  |

| Ohio   |             |                      |  |
|--|-------------|----------------------|--|
| <u>Profession</u>                                  | <u>1978</u> | <u>1986</u>          |  |
| Attorneys  | 5           | 10                   |  |
| Economists   | 0           | 0                    |  |
| Certified public accountants                       | 0           | 2                    |  |
| Chartered life, property and casualty underwriters | 0           | 5                    |  |
| Certified financial examiners                      | 10          | 30                   |  |
| Actuaries  | <u>2</u>    | <u>0<sup>d</sup></u> |  |
| Total  | <u>17</u>   | <u>47</u>            |  |

<sup>a</sup>These data are from current state insurance officials and differ from the states' responses to our 1978 questionnaire.

<sup>b</sup>The department reported it has five additional attorneys who do not practice law.

<sup>c</sup>Although the department has no CPAs on its staff, it contracts all of its field financial examinations to CPA firms.

<sup>d</sup>The department contracts with a consulting actuary, who reviews rate filings.

Table 4.4: 1986 Allocation of Authorized Personnel by Function

| <u>Delaware</u>                   |  |
|-----------------------------------|--|
| <u>Function</u>                   | <u>Percent of<br/>authorized personnel</u> |
| Legal                             | 2.6  |
| Financial evaluation <sup>a</sup> | 18.4                                       |
| Rate and policy form reviews      | 10.5                                       |
| Agent services                    | 10.5                                       |
| Consumer affairs                  | 26.3                                       |
| Administrative                    | 21.1                                       |
| Other insurance-related matters   | <u>10.5</u>                                |
| Total                             | <u>100.0</u>                               |

| <u>North Carolina</u>                        |  |
|--|--|
| <u>Function</u>                              | <u>Percent of<br/>authorized personnel</u> |
| Insurance-related matters                    | 74.2                                       |
| Legal  | 6.9  |
| Financial evaluation                         | 26.5                                       |
| Rate and policy form reviews                 | 10.3                                       |
| Agent services                               | 7.4  |
| Consumer affairs                             | 17.6                                       |
| Administrative                               | 12.3                                       |
| Other insurance-related matters <sup>b</sup> | <u>19.1</u>                                |
| Total insurance-related                      | <u>100.0</u>                               |
| Non-insurance-related matters <sup>c</sup>   | <u>25.8</u>                                |
| Total  | <u>100.0</u>                               |

## SECTION 5: REGULATORY ACTIVITIES

### Workload Measures

In addition to obtaining information on changes in departmental resources, we obtained updated information on five key workload measures: (1) number of rate filings requiring prior approval, (2) number of examinations of state-chartered companies, (3) number of policy form filings, (4) number of applications processed for insurance company licenses, and (5) number of applications for agent licenses. As shown in table 5.1, the changes in these measures between 1977 and 1985 were mixed among the three states.

- The number of rate filings requiring prior approval declined by about 79 percent in North Carolina but increased by 31 percent in Ohio. The decline in North Carolina was, at least in part, due to a 1977 change in the state's prior approval law; some lines of insurance which used to require prior approval are now regulated under a file-and-use system.<sup>1</sup> The change in Delaware's number of rate filings is uncertain because, according to a state insurance official, the number given to us in 1978 probably included policy form filings as well as rate filings. Thus, the number of Delaware rate filings shown in table 5.1 for 1977 is probably overstated.
- North Carolina and Ohio conducted about the same number of examinations of state-chartered companies in 1985 as in 1977, while Delaware conducted over three times as many in 1985. According to an insurance department official, this increase in examinations was due to a substantial growth in the number of Delaware-chartered insurance companies over this time period.
- The number of policy form filings increased by 50 percent in North Carolina and declined by about 6 percent in Ohio. The change for Delaware is indeterminate.
- The number of applications processed for insurance company licenses declined from 42 to 0 in Delaware, increased from 138 to 158 in North Carolina, and increased from 108 to 204 in Ohio. A Delaware insurance

---

<sup>1</sup>Prior approval laws are state laws under which insurers must file their proposed rates with the state insurance department and provide data with these filings to support the contention that the rates are not excessive, inadequate, or unfairly discriminatory. Proposed rates may not be used unless explicitly approved by the insurance commissioner. File-and-use laws are state laws under which insurance rates become effective immediately upon filing, with no affirmative action of the insurance commissioner required.

**Table 5.1: Workload Measures for the Three State Insurance Departments**

| Delaware   |                     |        |                |
|--|---------------------|--------|----------------|
| Measure  | 1977                | 1985   | Percent change |
| Number of rate filings requiring prior approval                  | 11,740 <sup>a</sup> | 1,329  | a              |
| Number of examinations of state-chartered companies <sup>b</sup> | 18                  | 56     | 211.1          |
| Number of policy form filings                                    | <sup>c</sup>        | 16,311 | <sup>c</sup>   |
| Number of applications processed for insurance company licenses  | 42                  | 0      | -100.0         |
| Number of applications for agent licenses                        | 1,119               | 2,300  | 105.5          |

| North Carolina   |        |        |                |
|--|--------|--------|----------------|
| Measure  | 1977   | 1985   | Percent change |
| Number of rate filings requiring prior approval                  | 2,485  | 530    | -78.7          |
| Number of examinations of state-chartered companies <sup>d</sup> | 49     | 42     | -14.3          |
| Number of policy form filings                                    | 10,902 | 16,402 | 50.4           |
| Number of applications processed for insurance company licenses  | 138    | 158    | 14.5           |
| Number of applications for agent licenses                        | 22,530 | 48,393 | 114.8          |

| Ohio   |        |         |                |
|--|--------|---------|----------------|
| Measure  | 1977   | 1985    | Percent change |
| Number of rate filings requiring prior approval                  | 5,750  | 7,552   | 31.3           |
| Number of examinations of state-chartered companies <sup>e</sup> | 96     | 93      | -3.1           |
| Number of policy form filings                                    | 18,784 | 17,737  | -5.6           |
| Number of applications processed for insurance company licenses  | 108    | 204     | 88.9           |
| Number of applications for agent licenses                        | 57,000 | 112,261 | 96.9           |

<sup>a</sup>Because the 1977 figure probably includes policy form filings as well as rate filings, the percent change is uncertain.

<sup>b</sup>Delaware also reported participating in 38 examinations of foreign companies in 1977.

<sup>c</sup>Not available.

<sup>d</sup>North Carolina also reported participating in 32 examinations of foreign companies in 1977.

<sup>e</sup>Ohio also reported participating in six examinations of foreign insurance companies in 1977 and five in 1985.

Note: Data shown for 1977 are on a calendar year basis and data for 1985 are on a fiscal year basis.

Table 5.2 shows the examination workloads of each of the three state insurance departments. If domestic insurance companies are examined on schedule, the number of field examinations conducted in any one year should be about equal to one-third the number of domestic companies in each state. At the time of our fieldwork,

- Delaware had 187 domestic, state-chartered companies; North Carolina had 103; and Ohio had 259. In each state, about 1,000 foreign firms also did business.
- North Carolina had a staff of 23 field examiners, and Ohio had 52 field examiners. Delaware reported having no field examiners on its staff because these examinations are conducted by CPA firms under contract.
- Each of the three states receives more than 1,000 annual financial statements for in-house reviews. To accomplish this task Delaware, North Carolina, and Ohio employ 3, 11, and 6 examiners, respectively.

The states' efforts to monitor the financial condition of insurance companies through field examinations and in-house reviews are supplemented by an early warning system--known as the Insurance Regulatory Information System. This system, developed and operated by NAIC, seeks to provide early identification of insurance companies with potential financial problems. It comprises two phases. The first is a statistical phase using key financial ratios, lists of insurers and affiliated groups of insurers, and key financial statement data. The second, an analytical phase, is a review of the annual financial statement and financial ratios by experienced financial examiners.

Insurance companies generally submit their annual financial statements to NAIC for input into the Insurance Regulatory Information System. About 95 percent of Delaware's domiciled insurance companies, 60 percent of North Carolina's domiciled companies, and 59 percent of Ohio's domiciled companies submitted their 1985 financial statements for this review.

## SECTION 6: RECENT STATE INITIATIVES

Because of recent concern about the affordability and availability of commercial liability insurance, various initiatives have been proposed or undertaken in each of the three states we reviewed. We asked insurance department officials in each of the states about (1) those initiatives undertaken in the last 2 years that address these issues, and (2) any proposed legislation in the last 2 years that they were aware of concerning these issues.

Table 6.1 shows the types of initiatives that were undertaken in each of the three states and whether they were undertaken by legislation or by regulatory action by the insurance commissioner or superintendent. The table reveals that each of the three states undertook some action during this period to address the affordability or availability of insurance, and that most of these actions were by legislation. It also shows that legislation has been proposed in each of the three states to reform state liability laws, including proposals to cap contingency fees and to limit the size of punitive damage awards.

Table 6.1: continued

| TO REFORM STATE LIABILITY LAWS:  |   |             |             |
|--|---|-------------|-------------|
| Cap suits against local governments  |   | C           | Legislation |
| Cap contingency fees   | C | C           | C           |
| Limit frivolous suits  |   | Legislation | C           |
| Modify joint and several liability   | C | C           | C           |
| Limit punitive damage awards   | C | C           | C           |
| Introduce pain and suffering thresholds  | C | C           | C           |
| Exclude or limit coverage for punitive damage                                      |   | Legislation |             |
| Provide civil immunity for hazardous material cleanup activities                   |   |             | Legislation |
| Provide tort immunity to volunteers and unpaid members of non-profit organizations |   |             | Legislation |

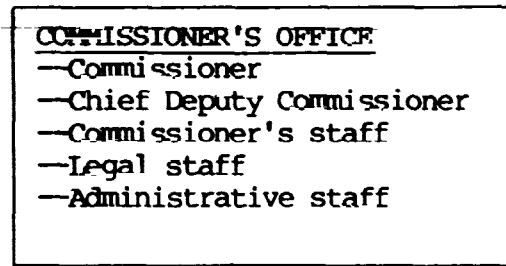
<sup>a</sup>This table does not account for similar or identical initiatives that Delaware and Ohio enacted and/or regulated before 1984.

<sup>b</sup>Market assistance programs are designed to match businesses unable to locate coverage with insurers who have the capacity and willingness to write the risk.

<sup>c</sup>Legislation has been proposed, but not yet enacted.

<sup>d</sup>This regulatory initiative has also been introduced as proposed legislation.

Figure 6.2: North Carolina Department of Insurance Responsibilities  
by Major Organizational Group



| <u>COMPANY SERVICES GROUP<sup>a</sup></u>  | <u>PUBLIC SERVICES GROUP<sup>b</sup></u>  | <u>FIELD SERVICES GROUP<sup>c</sup></u>  | <u>NON-INSURANCE GROUP<sup>d</sup></u>   |
|--|---|--|--|
| —Licenses insurance companies<br><br>—Reviews financial statements<br><br>—Collects taxes<br><br>—Conducts field audits<br><br>—Analyzes and approves policies and forms<br><br>—Encourages rates which are not excessive or unfairly discriminatory | —Responds to consumer questions and complaints<br><br>—Examines, licenses, and regulates individuals and corporations who sell policies in North Carolina | —Conducts criminal investigations<br><br>Regulates insurance premium finance companies, collection agents, motor clubs, and bailbondsmen | —Regulates mobile homes<br><br>—Enforces building codes<br><br>—Is the state's risk manager<br><br>—Administers the Firemen's Relief Fund<br><br>—Develops and conducts fire training programs |

<sup>a</sup>This group, headed by a senior deputy commissioner, includes 4 divisions: (1) company operations, (2) field audits, (3) life, accidents, and health, and (4) fire and casualty.

<sup>b</sup>This group, headed by a senior deputy commissioner, includes the divisions of agent services and consumer services.

<sup>c</sup>This group, headed by a senior deputy commissioner, includes the divisions of special services and investigations.

<sup>d</sup>This group includes the department's safety services divisions—engineering, manufactured housing, risk management, fire and rescue, and the Property Fire Fund.

---

Requests for copies of GAO reports should be sent to:

U.S. General Accounting Office  
Post Office Box 6015  
Gaithersburg, Maryland 20877

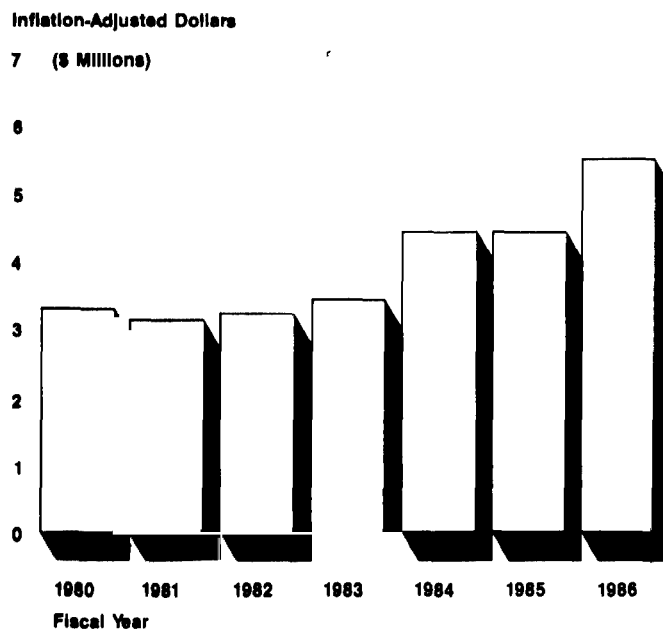
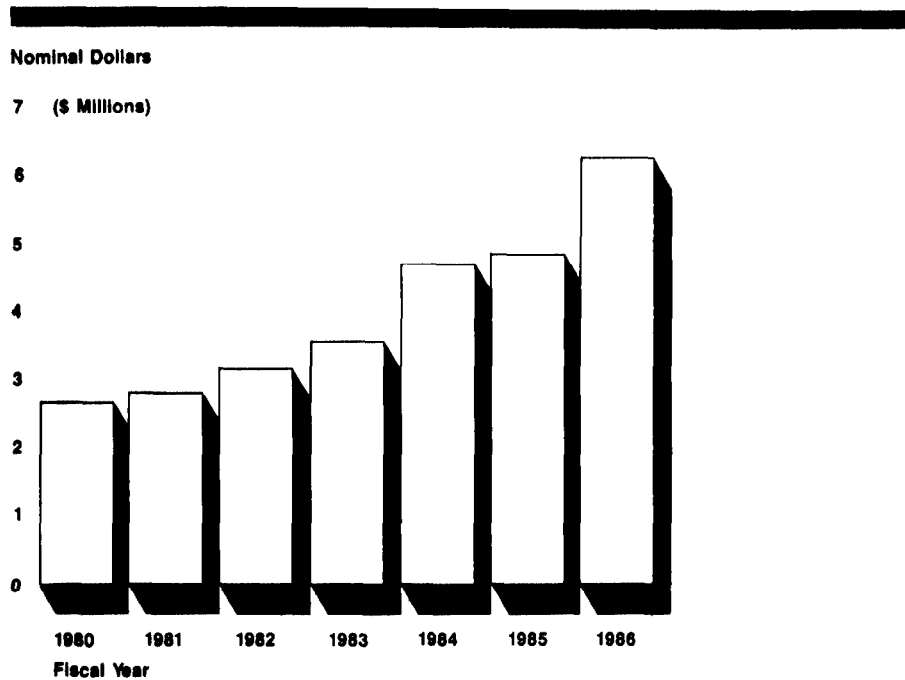
Telephone 202-275-6241

The first five copies of each report are free. Additional copies are \$2.00 each.

There is a 25% discount on orders for 100 or more copies mailed to a single address.

Orders must be prepaid by cash or by check or money order made out to the Superintendent of Documents.

**Figure 3.3: Changes in Financial Resources, Ohio Insurance Department, 1980-86**



#### SECTION 4: PERSONNEL RESOURCES

Table 4.1 shows the growth in the number of full-time equivalent staff in the three departments from 1978 to 1986. Comparing state-reported data in 1986 to those reported in 1978, Delaware's available staff increased by 80 percent (from 20 to 36); North Carolina's by about 19 percent (from 204 to 242); and Ohio's by about 40 percent (from 93 to 130). Our analysis of the staff increases revealed the following information.

- Most of Delaware's staff increases are attributable to the 1985 authorization for 11 positions to staff the Bureau of Examination, Rehabilitation, and Guaranty.
- Nearly all of North Carolina's staff increases have occurred since fiscal year 1985. The majority of the new staff were assigned to solvency oversight; agent and consumer services; new state and local risk management programs; and the regulation of workers' compensation self-insurance, which was transferred to the insurance department in 1985.
- Ohio's most recent staff increases occurred as a result of hiring additional examiners, consumer affairs investigators, and staff for a newly established fraud division.

Table 4.1: Available Full-Time Staff in 1978 and 1986

| <u>State</u>   | <u>1978</u> | <u>1986</u>      | <u>Percent change</u> |
|----------------|-------------|------------------|-----------------------|
| Delaware       | 20          | 36 <sup>a</sup>  | 80.0                  |
| North Carolina | 204         | 242 <sup>b</sup> | 18.6                  |
| Ohio           | 93          | 130 <sup>b</sup> | 39.8                  |

<sup>a</sup>As of May 1986.

<sup>b</sup>As of August 1986.

Table 4.2 Available Full-Time Staff by Occupational Category

| Delaware                         |             |             |                           |
|----------------------------------|-------------|-------------|---------------------------|
| <u>Occupational<br/>category</u> | <u>1978</u> | <u>1986</u> | <u>Percent<br/>change</u> |
| Professional                     | 12          | 19          | 58.3                      |
| Clerical                         | <u>8</u>    | <u>17</u>   | 112.5                     |
| Total                            | <u>20</u>   | <u>36</u>   | 80.0                      |
| North Carolina                   |             |             |                           |
| <u>Occupational<br/>category</u> | <u>1978</u> | <u>1986</u> | <u>Percent<br/>change</u> |
| Professional                     | 150         | 168         | 12.0                      |
| Clerical                         | <u>54</u>   | <u>74</u>   | 37.0                      |
| Total                            | <u>204</u>  | <u>242</u>  | 18.6                      |
| Ohio                             |             |             |                           |
| <u>Occupational<br/>category</u> | <u>1978</u> | <u>1986</u> | <u>Percent<br/>change</u> |
| Professional                     | 59          | 103         | 74.6                      |
| Clerical                         | <u>34</u>   | <u>27</u>   | -20.6                     |
| Total                            | <u>93</u>   | <u>130</u>  | 39.8                      |

## Allocation of Resources

Because insurance department budgets typically use object categories, such as salaries and capital expenditures, we analyzed the 1986 allocation of each department's authorized personnel to determine the functional uses of resources. Since most of the department budgets cover personnel costs, an analysis of how authorized personnel are allocated by function should also approximate how the three state insurance departments allocated their financial resources. The allocation shown in table 4.4 is summarized below.

- Delaware allocated the largest portion of its authorized personnel (26.3 percent) to consumer affairs. However, Delaware's authorized personnel do not include those individuals who conduct on-site financial examinations because such examinations are performed by CPA firms under contract. If the individuals conducting these evaluations in Delaware were assigned to the department, as in North Carolina and Ohio, financial evaluation, not consumer affairs, would represent Delaware's largest use of regulatory resources.
- North Carolina allocated the largest portion of its authorized, insurance-related personnel to financial evaluation (26.5 percent) and the next largest portion (except for "other insurance-related matters") to consumer affairs (17.6 percent).
- In Ohio, the largest share of resources (46 percent of authorized personnel) was also allocated to financial evaluation, and the next largest (15.9 percent) was allocated to agent services.

Table 4.4: continued

| Ohio   |  |
|--|--|
| <u>Function</u>                              | <u>Percent of<br/>authorized personnel</u> |
| Legal  | 4.8  |
| Financial evaluation                         | 46.0                                       |
| Rate and policy form reviews                 | 8.7  |
| Agent services                               | 15.9                                       |
| Consumer affairs                             | 11.9                                       |
| Administrative                               | 4.0  |
| Other insurance-related matters <sup>d</sup> | <u>8.7</u>                                 |
| Total  | <u><u>100.0</u></u>                        |

<sup>a</sup>Does not include financial examiners responsible for conducting financial solvency examinations because the department contracts with CPA firms for this task.

<sup>b</sup>Includes regional office staff and individuals concerned with (1) investigating criminal activities, (2) regulating special services such as premium finance companies and collection agencies, and (3) regulating state programs, such as workers' compensation self-insurers and local government risk management.

<sup>c</sup>Includes such matters as enforcing building codes and administering fire safety programs.

<sup>d</sup>Includes individuals investigating criminal and health-related matters, plus allegations of unethical conduct by insurance agents and companies.

Note: For Delaware, based on a total of 38 authorized personnel as of March 1986; for North Carolina, based on a total of 275 total authorized personnel, including 71 non-insurance-related staff, as of July 1986; for Ohio, based on a total authorized staff of 126 as of April 1986. Percentage totals may not add to 100 because of rounding.

official told us that the number of applications for company licenses declined because out-of-state companies are now discouraged from domiciling in Delaware.

- The number of applications for agent licenses substantially increased in all three states between 1977 and 1985.

Because state insurance departments use different ways of counting and defining what constitutes a rate filing and other types of regulatory activities, it is difficult to evaluate the significance of the changes in these workload measures. Also, we were unable to establish sufficient criteria to evaluate whether insurance department resources are adequate to handle existing workloads.

## Financial Evaluation

Because financial evaluation represents the single largest use of regulatory resources in each of the three states, we obtained additional information about this regulatory activity.

- Each of the three states performs two types of financial evaluations: (1) statutory-required financial examinations, or on-site field examinations, of "domestic" insurance companies--i.e., those firms chartered or domiciled in the state, and (2) "in-house" reviews of annual financial statements of all companies licensed to do business in the state, both domestic and foreign.<sup>2</sup> In addition, each state may participate in financial examinations of foreign companies and receives copies of the financial examination reports for those foreign companies licensed to do business in the state.
- In conducting field examinations, Delaware, North Carolina, and Ohio follow NAIC guidelines. In North Carolina and Ohio, field examinations are conducted by departmental staff. In Delaware, these examinations are conducted by CPA firms under contract.
- Delaware, North Carolina, and Ohio each reported that field examinations of domiciled companies are conducted once every 3 years.
- In conducting in-house reviews, staff examiners in each state review annual financial statements for accuracy. They also compare financial data with standardized ratios to develop trends for early detection of financially troubled companies. A Delaware official told us that these reviews could take anywhere from 2 hours to 21 days to complete, but on average required half a working day. North Carolina and Ohio officials said that these reviews took 1 to 2 days to complete.
- Over the past 5 years, Delaware reported having four insolvencies, Ohio two, and North Carolina none. A Delaware official told us that consumer complaints and examinations disclosed the financial condition of its four insolvent companies, and Ohio said examinations disclosed the condition of its two insolvent companies.

---

<sup>2</sup>Domiciled companies are commonly known as domestic companies, whereas a company conducting business in other than its chartered state is referred to as a foreign company.

Table 5.2: Number of Insurance Companies and Financial  
Examiners by State

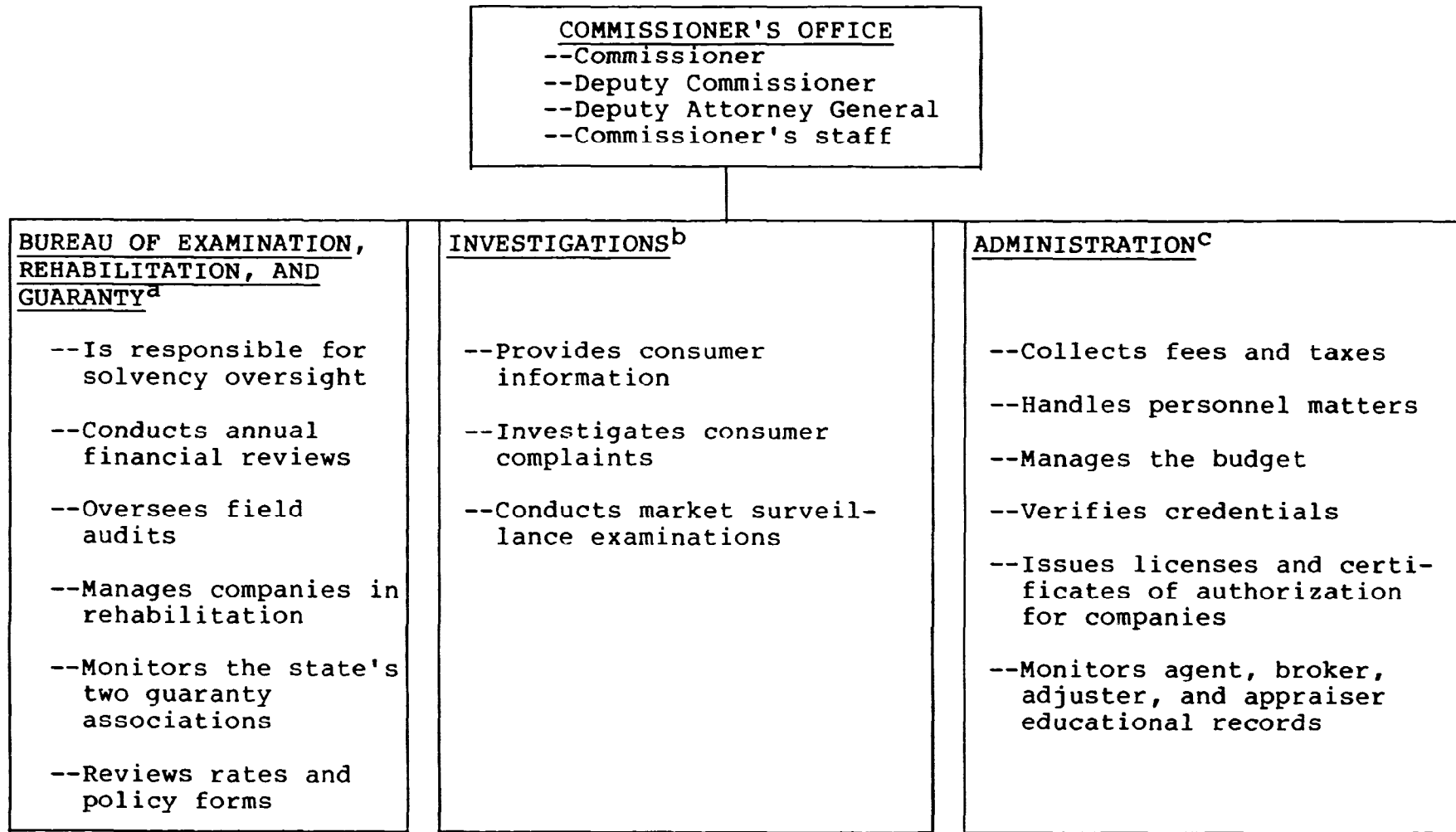
|                   | <u>Number of companies</u> |                |              | <u>Number of examiners</u> |                |                |
|-------------------|----------------------------|----------------|--------------|----------------------------|----------------|----------------|
|                   | <u>Domestic</u>            | <u>Foreign</u> | <u>Total</u> | <u>In-house</u>            | <u>Field</u>   | <u>Total</u>   |
| Delaware          | 187                        | 1,086          | 1,273        | 3                          | 0 <sup>a</sup> | 3 <sup>a</sup> |
| North<br>Carolina | 103                        | 942            | 1,045        | 11                         | 23             | 34             |
| Ohio              | 259                        | 1,162          | 1,421        | 6                          | 52             | 58             |

<sup>a</sup>Delaware contracts all of its field examinations of domestic insurance companies to CPA firms.

**Table 6.1: Recent State Initiatives Concerning Commercial Liability Insurance<sup>a</sup>**

| <u>INITIATIVES</u>  | <u>Delaware</u>   | <u>North Carolina</u> | <u>Ohio</u>                    |
|---|-------------------|-----------------------|--------------------------------|
| <b>TO INCREASE AVAILABILITY:</b>  |                   |                       |                                |
| Authorize joint underwriting associations   |                   | Legislation           | <sup>c</sup>                   |
| Establish market assistance programs <sup>b</sup>   | <sup>c</sup>      | Regulatory action     | Regulatory action <sup>d</sup> |
| Limit mid-term policy cancellations   | Regulatory action | Legislation           | Regulatory action <sup>d</sup> |
| Provide at least 30-day prior notices on non-renewals of policies                                 | Regulatory action | Legislation           | <sup>c</sup>                   |
| Extend fair plan to cover entire state  |                   | Legislation           |                                |
| <b>TO INCREASE AFFORDABILITY:</b>   |                   |                       |                                |
| Require use of state loss data and experience in justifying rates                                 | <sup>c</sup>      | Legislation           |                                |
| Require companies to justify rate increases   |                   | Legislation           |                                |
| Require lower insurance coverage for amusement park operators                                     |                   |                       | Legislation                    |
| Require a 60-day waiting period before new fire and casualty company rates can be put into effect |                   | Legislation           |                                |
| Order refunds or adjustments on rate disapprovals resulting from hearings                         |                   | Legislation           |                                |
| Order rate modifications if appropriate due to changes in civil laws                              |                   | Legislation           |                                |
| Allow education school board members to buy group insurance through the school                    |                   |                       | Legislation                    |

Figure 6.1: Delaware Department of Insurance Responsibilities  
by Major Organizational Group



<sup>a</sup>This unit reports directly to the commissioner's office.

<sup>b</sup>This unit is headed by the director of investigations.

<sup>c</sup>This group is headed by the administrative officer.

**Figure 6.3: Ohio Department of Insurance Responsibilities  
by Major Organizational Group**

| <div style="border: 1px solid black; padding: 5px; text-align: center;"> <u>DIRECTOR'S OFFICE</u><br/> --Director<br/> --Deputy Director<br/> --Director's staff </div>  |  |   |   |
|--|--|---|---|
| <u>ADMINISTRATIVE<sup>a</sup></u>  | <u>TECHNICAL<sup>b</sup></u>   | <u>EXECUTIVE<sup>c</sup></u>  | <u>RESEARCH<sup>d</sup></u>   |
| --Oversecs the development and the administration of licensing examinations<br><br>--Licenses agents and companies<br><br>--Accounts for all fees and taxes owed the state<br><br>--Prepares the department's annual budget<br><br>--Directs the day-to-day operations | --Investigates consumer complaints<br><br>Is a liaison between companies and their policyholders<br><br>Presents evidence before departmental hearings | Reviews property/casualty rules, rates, and policy forms<br><br>Reviews liability and automobile rates<br><br>Audits the financial records of all domestic insurers every 3 years<br><br>Reviews filing submission and corporate documents<br><br>--Oversecs insurance research<br><br>--Provides legal support | Licenses health maintenance organizations (HMOs)<br><br>Reviews all HMO filings and provider/subscriber contracts<br><br>--Monitors quarterly and annual HMO financial statements<br><br>Investigates/resolves HMO provider and subscriber complaints<br><br>Reviews contractual provisions of all life and accident policies<br><br>--Reviews the life, accident, and health premium structure |

<sup>a</sup>This group, headed by the assistant director for administration, includes five separate divisions: (1) testing, (2) licensing, (3) finance, (4) data systems, and (5) administration.

<sup>b</sup>This group, headed by the assistant director for technical services, includes the divisions of policyholder services and enforcement.

<sup>c</sup>This group includes the divisions of property and casualty and exam and audit as well as the legal staff. It also covers the functions of the business manager and legislative and public information office. This group reports directly to the deputy insurance director.

<sup>d</sup>This group is headed by the assistant director for research, who is responsible for the divisions of health maintenance organizations and life, accident, and health.

---

United States  
General Accounting Office  
Washington, D.C. 20548

First-Class Mail  
Postage & Fees Paid  
GAO  
Permit No. G100

---

Official Business  
Penalty for Private Use \$300

Address Correction Requested

---