

Department of Legislative Services
Maryland General Assembly
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FISCAL AND POLICY NOTE
First Reader

Senate Bill 388 (Senator Zirkin)
Finance and Judicial Proceedings

Civil Actions - Liability Insurance - Prohibition on Disclaiming Coverage

This bill prohibits an insurer from disclaiming coverage on a liability insurance policy on the ground that the insured, or a person claiming the benefits of the policy through the insured, has breached the policy by failing to cooperate with the insurer. The bill makes conforming changes to an existing statute.

Fiscal Summary

State Effect: Potential significant increase in general fund revenues from insurance premium tax revenues. Potential significant special fund revenue increase from the \$125 rate and form filing fee in FY 2020 only. Special fund expenditures increase by \$151,000 in FY 2020 only for review of amended forms.

Maryland Automobile Insurance Fund (MAIF) Effect: Nonbudgeted expenditures increase beginning in FY 2020 due to increased payment of claims on policies that are issued by MAIF. Nonbudgeted revenues are expected to fully offset nonbudgeted expenditures in all years.

Local Effect: The bill is not expected to materially affect local finances.

Small Business Effect: Potential meaningful.

Analysis

Current Law: An insurer may disclaim coverage on a liability insurance policy on the ground that the insured or a person claiming the benefits of the policy through the insured has breached the policy by failing to cooperate with the insurer or by not giving the insurer

required notice. The authority to disclaim applies only if the insurer establishes by a preponderance of the evidence that the lack of cooperation or notice has resulted in actual prejudice to the insurer.

State Revenues: General fund revenues may increase significantly beginning in fiscal 2020 from the 2% tax on insurance premiums. Special fund revenues may increase significantly from the \$125 rate and form filing fee in fiscal 2020.

Title 6 of the Insurance Article imposes a 2% premium tax on each authorized insurance company, surplus lines broker, or unauthorized insurance company that sells, or an individual who independently procures, any type of insurance coverage upon a risk that is located in the State. Revenues accrue to the general fund. Prohibiting an insurer from disclaiming coverage due to lack of cooperation of the insured or a person claiming benefits of the policy through the insured affects the ability of an insurer to investigate and evaluate claims. Increases in payments of or the amounts of paid claims will likely be transferred to policyholders in the form of increased premiums. The extent to which this occurs cannot be reliably determined at this time but may be significant when applied to the liability insurance market in the State.

While the Maryland Insurance Administration (MIA) charges a \$125 fee per rate and form filing, the amount is capped at \$1,000 per filing. Thus, an insurer does not pay a fee for forms in excess of the first eight forms per filing. MIA advises that while filings often contain multiple forms, it cannot provide a precise count of the additional filing fee revenue that may be expected under the bill. The extent of the increase in special fund revenues from filing fees depends on the number of forms included in each filing and the number of total filings generated by the bill.

State Expenditures: Special fund expenditures increase by \$151,030 in fiscal 2020 for MIA to review amended insurance forms.

MIA advises that all liability insurance contracts in use in the State will need to be refiled without the existing language that obligates the insured to cooperate with the insurer. While MIA does not have a precise count of the number of form filings that would need to be made, MIA advises that it could easily be in the tens of thousands. The Rates and Forms Unit in MIA is composed of 10 individuals, including a director, supervisor, and one vacancy in the process of being filled. The unit has a limited capacity to absorb additional filings. The staff reviews more than 500,000 pages of filing material each year. In fiscal 2018, the unit received 2,850 form filings with more than 25,000 individual forms. According to MIA, liability forms account for at least two-thirds of those totals.

In order to accommodate the increased volume of filings generated by the bill in a short amount of time, MIA requires additional contractual staff support. Special fund

expenditures increase by \$151,030 in fiscal 2020 only, which accounts for the bill's October 1, 2019 effective date.

This estimate reflects the cost of hiring five contractual form reviewers at the base grade for positions in the unit. It includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Contractual Positions	5
Salaries and Fringe Benefits	\$124,236
Operating Expenses	<u>26,794</u>
Total FY 2020 State Expenditures	\$151,030

This estimate does not include any health insurance costs that could be incurred for specified contractual employees under the State's implementation of the federal Patient Protection and Affordable Care Act.

MAIF Fiscal Effect: According to MAIF, policyholders often cooperate only when informed that their lack of cooperation will expose them to personal liability. MAIF advises that it disclaims coverage for approximately 15 to 20 claims per week for noncooperation. MAIF estimates that the bill's provisions will increase claims payments by approximately \$5.3 million to \$7.1 million annually. This would lead to an increase in premiums of 2.5% to 3.5% or \$60 to \$80 per policy for all MAIF policyholders. Assuming that the premium increase is set to cover additional costs incurred under the bill, there is no net impact on MAIF's finances.

Small Business Effect: The bill has a potential meaningful effect to the extent it increases insurance premiums for small businesses, especially small businesses engaged in activities that are frequently the source of claims (*e.g.*, transportation).

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Judiciary (Administrative Office of the Courts); Maryland Insurance Administration; Maryland Automobile Insurance Fund; Department of Legislative Services

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