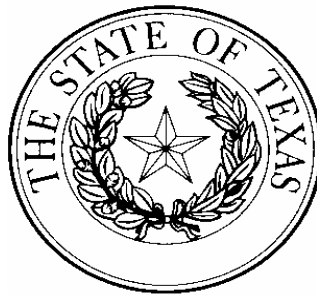


Texas Department of Insurance

Agency Strategic Plan

**For the
Fiscal Years 2007-2011 Period**



MIKE GEESLIN

Commissioner of Insurance

July 7, 2006

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Introduction

Overview

The *FY 2007-2011 Agency Strategic Plan* for the Texas Department of Insurance (TDI) is being submitted as the first step of Texas' Strategic Planning and Budgeting System. This Strategic Plan will serve as the foundation for TDI's Fiscal Years (FY) 2008-2009 appropriations request and budget structure.

As required by Government Code 2056.002, TDI prepared its strategic plan in accordance with the *FY 2007-2011 Instructions for Preparing and Submitting Agency Strategic Plans* developed by the Legislative Budget Board (LBB) and the Governor's Office of Budget, Policy, and Planning (GOBPP). TDI's *FY 2007-2011 Agency Strategic Plan* includes all required elements set forth by the instructions, including the state and agency planning elements, the internal and external factors affecting the agency, the workforce plan, and other statewide and agency strategic planning elements.

In an effort to make the agency strategic plan more accessible and comprehensible to its readers, TDI has organized the plan so that key factors influencing the agency are presented early in the report, which include:

- House Bill 7 (Workers' Compensation Reform and Organizational Impact)
- Changing Market Conditions
- Disaster Readiness and Response
- Insurance Fraud
- Fire Safety, and
- Legislative Changes.

TDI evaluated the possible effects of these key factors on the ability of the agency to provide effective and efficient regulation of the insurance industry. The agency has identified challenges for each of these factors and explains how the agency is responding to these challenges.

Other required elements of the plan are presented in the appendices, and include:

- Agency Overview
 - Agency Planning Process
 - Organizational Chart
 - Agency Budget Structure
 - Workforce Plan
 - Performance Measure Definitions
 - Five-Year Projections for Outcomes, and
 - Survey of Organizational Excellence.
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Statewide Planning Elements

Statewide Vision, Mission, Philosophy

The statewide planning elements, developed by the LBB and GOBPP, include a statewide vision, mission and philosophy that provide an inspiring view of the future of Texas, a statement of the purpose and role of Texas government, and a statement of values underlying Texas state government service. It also includes statewide priority goals and benchmarks.

Statewide Vision

The Texas Statewide Vision is as follows:

- assuring open access to an educational system that not only guarantees the basic core knowledge necessary for productive citizens but also emphasizes excellence and accountability in all academic and intellectual undertakings;
 - creating and retaining job opportunities and building a stronger economy that will lead to more prosperity for our people and a stable source of funding for core priorities;
 - protecting and preserving the health, safety, and well-being of our citizens by ensuring healthcare is accessible and affordable and by safeguarding our neighborhoods and communities from those who intend to harm us; and
 - providing disciplined principled government that invests public funds wisely and efficiently.
-

Statewide Mission

Texas state government must be limited, efficient, and completely accountable. It should foster opportunity and economic prosperity, focus on critical priorities, and support the creation of strong family environments for our children. The stewards of the public trust must be men and women who administer state government in a fair, just, and responsible manner. To honor the public trust, state officials must seek new and innovative ways to meet state government priorities in a fiscally responsible manner.

Statewide Philosophy

The task before all state public servants is to govern in a manner worthy of this great state. We are a great enterprise, and as an enterprise we will promote the following core principles:

- First and foremost, Texas matters most. This is the overarching, guiding principle by which we will make decisions. Our state, and its future, is more important than party, politics, or individual recognition.
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Statewide Planning Elements, Continued

**Statewide
Philosophy,**
continued

- Government should be limited in size and mission, but it must be highly effective in performing the tasks it undertakes.
- Decisions affecting individual Texans, in most instances, are best made by those individuals, their families, and the local government closest to their communities.
- Competition is the greatest incentive for achievement and excellence. It inspires ingenuity and requires individuals to set their sights high. Just as competition inspires excellence, a sense of personal responsibility drives individual citizens to do more for their future and the future of those they love.
- Public administration must be open and honest, pursuing the high road rather than the expedient course. We must be accountable to taxpayers for our actions.
- State government has a responsibility to safeguard taxpayer dollars by eliminating waste and abuse, and providing efficient and honest government.
- Finally, state government should be humble, recognizing that all its power and authority is granted to it by the people of Texas, and those who make decisions wielding the power of the state should exercise their authority cautiously and fairly.

**Relevant
Statewide Goals
and
Benchmarks**

The following priority goals and benchmarks from the *Pathway to Prosperity* link TDI's strategic plan and goals to the statewide mission.

Priority Goal

To ensure Texans are effectively and efficiently served by high-quality professionals and businesses by ensuring clear standards and compliance; establishing market-based solutions; and reducing the regulatory burden on people and business.

Benchmarks

- Average annual homeowners and automobile insurance premiums as a percent of the national average.
- Number of utilization reviews conducted for treatment of occupational injuries.
- Percent of new and renewed professional licenses issued via Internet.

Agency Planning Elements

**Agency Vision,
Mission and
Regulatory
Approach**

The agency planning elements include the vision, mission, regulatory approach and assessment of key factors impacting the agency. It also includes agency goals, objectives, strategies and performance measures. Action plans are another part of the Strategic Planning and Budgeting System that TDI develops internally through its business planning process.

Agency Vision

The Texas Department of Insurance envisions a financially stable and fair marketplace and an effective and efficient workers' compensation system.

Agency Mission

The Texas Department of Insurance regulates the marketplace firmly and fairly by enforcing and implementing the law. TDI strives to enhance internal and external communication for efficient and effective regulation and to promote outreach to educate the public.

**Agency
Regulatory
Approach**

The Texas Department of Insurance will exemplify friendly, courteous, ethical, and professional behavior in all areas of performance by:

- providing the best value in services to the people of Texas
 - applying the law and the agency policy fairly and consistently throughout the state, and
 - communicating openly and providing timely and accurate information to the public we serve, and to all our fellow employees.
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Key Factors Influencing the Agency

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Challenge: HB 7 Workers' Compensation Reform

Analysis

Workers' compensation claims in Texas have been among the highest in the nation, driving up the cost of workers' compensation insurance for employers. Texas employees have experienced longer treatment durations and were away from work longer than injured employees in most other states. In addition, the process has been considered complex and cumbersome for the carriers, providers and injured employees participating in the system.

House Bill (HB) 7, passed by the 79th Legislature, transferred the functions of the Texas Workers' Compensation Commission (TWCC) to the Texas Department of Insurance (TDI), creating TDI's Division of Workers' Compensation (DWC). The bill mandates system reforms that are expected to result in significant improvements to the workers' compensation system in Texas. The goals of HB 7 include:

- providing access to prompt, high quality medical care within the statutory framework
- treating injured employees with dignity and respect
- providing a fair and accessible dispute resolution process, and
- providing services to facilitate an injured employee's return to work as soon as it is considered safe and appropriate by the employee's health care provider.

A primary goal of HB 7 is to provide injured employees with access to prompt, high quality medical care within the statutory framework. The current workers' compensation system may be burdensome for providers who must be certified to treat workers' compensation claimants and are subject to significant retrospective oversight and administrative requirements. As a result, doctors may choose not to participate in the workers' compensation system, which may create access issues for injured employees. HB 7's authorization of workers' compensation health care networks and the establishment of a framework for care delivered outside the network are expected to significantly change the delivery of health care in the workers' compensation system. As networks penetrate the market, access to quality health care should improve. The Commissioner of Workers' Compensation recognizes that to effectively address the needs of injured employees, DWC will also need to focus on improving customer service, simplifying processes and increasing communication among system participants.

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Challenge: HB 7 Workers' Compensation Reform, Continued

Analysis, continued

TDI is in the process of revamping DWC's current regulatory approach to establish a performance-based oversight system that includes key regulatory goals for assessing insurance carriers and providers. The new approach will focus regulatory resources on poor performers and will use incentives and increased penalty authority to encourage system compliance.

While roughly 80 percent of workers' compensation claims are handled without disputes, DWC receives more than 70,000 indemnity and medical disputes annually. These disputes can delay the delivery of benefits and require a considerable time investment for injured employees, staff, attorneys and other parties.

The ultimate goal of the workers' compensation system is to return injured employees to a productive life course, including work when possible. HB 7 includes numerous requirements for improving return-to-work outcomes, with the goal of providing services to facilitate an injured employee's return to work as soon as it is considered safe and appropriate by the employee's health care provider.

TDI's efforts for reforming the workers' compensation system are organized around the following focus areas, which are directly tied to HB 7 goals:

- health care delivery change
 - injured employee services
 - performance-based oversight
 - dispute resolution, and
 - return to work.
-

Strategic Response

Planned activities for addressing workers' compensation reform follow:

- **Health Care Delivery Change**

Ensure access to prompt, high quality medical care.

The use of certified health care networks and the development of a disability management framework for out-of-network care will reduce administrative burdens on providers and allow doctors and carriers to agree on an appropriate course of treatment on the "front-end." This framework involves the use of best practices, treatment planning, treatment guidelines, and the concentrated management of delayed recovery cases. TDI will monitor the quality and utilization of healthcare services in order to compare care delivered under network, non-network and group health plans.

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Challenge: HB 7 Workers' Compensation Reform, Continued

Strategic Response, continued

- **Health Care Delivery Change, continued**

Access to medical expertise plays a critical role in the development of appropriate policies and strategies for affecting health care delivery. DWC will involve its Medical Advisor when addressing or setting policy on medical issues. DWC will also strengthen education and technical support for providers in order to improve the provision of quality, cost effective health care in the workers' compensation environment. The Workplace and Medical Services section, formed after the creation of DWC, will modify methods to address both employer and provider inquiries and educational and customer service needs.

- **Injured Employee Services**

Improve DWC service delivery to injured employees.

To address the needs of injured employees, TDI will focus on improving customer service, simplifying processes, and increasing communication between system participants, with an emphasis on treating injured employees with dignity and respect. By the end of 2007, TDI plans to provide each injured employee with a single point of contact throughout the claims process.

TDI will continue to improve upon the information provided to system participants, with the goal of helping system participants navigate the claims process with the least difficulty possible. DWC is using seminars, bulletins, training and the TDI Web site to educate its staff and system participants on the various changes, being careful to present information in a manner that is clear, accessible and comprehensible to the user. Coordination with the newly established Office of Injured Employee Counsel (OIEC), which provides ombudsman and consultation services to injured employees and advocates on their behalf, will further improve service to injured employees.

- **Performance-Based Oversight**

Assess performance of carriers and providers and use enforcement authority to promote compliance.

To establish a performance-based oversight system, TDI will produce report cards that measure network performance, establish key regulatory goals, assess insurance carriers and health care providers against these goals and place them into regulatory tiers based on performance.

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Challenge: HB 7 Workers' Compensation Reform, Continued

Strategic Response, continued

- **Performance-Based Oversight**, continued
Changes to TDI's organizational structure and increased intra-agency communication on regulatory matters will improve agency consistency in enforcement actions and procedures. TDI has combined the functions of agency enforcement attorneys and has transferred criminal fraud investigation to TDI's Fraud Unit. Additionally, the Consumer Protection program and DWC are establishing an agency-wide complaints handling process. The agency will work with system participants to create a more proactive approach to achieving the reforms. Additionally, DWC will increase communication with stakeholders during the compliance process, by clearly outlining system expectations.

 - **Dispute Resolution**
Provide injured employees access to a fair dispute resolution process.
DWC has identified strategies to help streamline the dispute resolution processes and improve timeliness, efficiency, fairness and consistency of dispute resolution decisions. These strategies include training field staff to conduct quality review decisions, automating processes, developing low-cost alternatives to dispute resolution, and consolidating Independent Review Organization (IRO) functions to improve consistency and efficiency when assigning medical necessity disputes for independent review.

Improvements in the health care delivery system, in combination with other system reforms, are expected to reduce the number of medical disputes in the system. While the volume of disputed cases may decline, HB 7 establishes a goal to provide injured employees access to a fair and accessible dispute resolution process.

 - **Return to Work**
Improve return-to-work outcomes.
TDI's primary role is to educate and train system participants on the benefits of early return to work for injured employees. To improve return-to-work outcomes, TDI will adopt guidelines to encourage best practices in returning injured employees to work as soon as safe and appropriate. DWC's Small Employer Pilot Program will reimburse employers for workplace modifications made to eliminate barriers to an employee's return to work. TDI will track return-to-work outcomes to evaluate the success of DWC activities in this area.

DWC will continue working with agencies such as the Department of Assistive and Rehabilitative Services and the Texas Workforce Commission to improve timely referrals, rehabilitation and job placement for injured employees who are candidates for these services.
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Challenge: HB 7 Organizational Impact

Analysis

As discussed above, the most significant piece of state legislation affecting TDI was HB 7. In addition to creating changes in workers' compensation regulation and service delivery, HB 7 merged two formerly independent agencies of equal size. The Texas Workers' Compensation Commission (TWCC) became the Division of Workers' Compensation (DWC) within TDI on September 1, 2005. HB 7 created a separate agency known as the Office of Injured Employee Counsel (OIEC) that is administratively attached to TDI. This structure requires TDI to create separate accounting, payroll, email, server networks, purchasing systems and reporting mechanisms for the OIEC. The legislation mandated or influenced several organizational changes.

First, the former TWCC board was eliminated and the Governor appointed the Commissioner of Workers' Compensation. The DWC is a separate division of TDI and the success of the agency requires close communication between the DWC and TDI Commissioners.

In order to operate as one agency, and because HB 7 requires that DWC be administratively tied to TDI, DWC's purchasing, human resources, information technology, financial services and staff services have been consolidated and DWC has adopted TDI's policies and procedures.

The change in processes created a learning curve for TDI and DWC staff, and training courses were conducted to familiarize staff with the new practices. In addition, liaisons were designated in each DWC division to assist with implementing and administering the new purchasing, budgeting, human resources, and information technology functions.

Administrative staff are also undergoing an adjustment process. Initially, the administrative workload approximately tripled with the addition of a variety of responsibilities including FY 2005 reports for TWCC, new reports for OIEC, federal funds accounting for DWC, and different needs of DWC and OIEC regarding purchases, personnel actions, travel processing, invoice payments, accounting transactions, and facility support for field offices. Administrative staffing levels did not increase proportionately to workload, but all five administrative divisions are finding more efficient ways to manage workloads in areas such as contracts, reports, and travel practices.

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Challenge: HB 7 Organizational Impact, Continued

**Analysis,
continued**

The Business Process Improvement (BPI TXCOMP) project began in FY 2000 and had total appropriations of \$13.18 million through FY 2007. The original study and plan for the project recommended modifications to business processes, replacement of the agency's workers' compensation mainframe system (COMPASS) and ultimately, acquisition and implementation of imaging technology to reduce the internal processing of paper. This project was less than 40 percent complete at the end of FY 2006.

Upon passage of HB 7, TDI conducted an analysis of the state of the BPI project, which revealed a need to significantly change the project's scope in order to comply with the required timeframes and budget. The agency considered various options for proceeding with the project and chose to focus on stabilizing the existing system and moving toward a web-based solution.

A Governor's veto proclamation created funding reductions of approximately \$8.8 million over the biennium. In order to comply with the reductions, TDI eliminated 61 positions that performed duplicative administrative or program functions and is operating within current funding reductions. The consolidation also helped the agency reduce non-salary expenses, such as IT maintenance costs. As a result of efficiencies and savings, the agency anticipates returning approximately \$0.5 million to the state this fiscal year.

TDI sought not only to achieve administrative consolidation but to improve customer service and leverage its resources by examining similar program functions. As a result of this process, all criminal fraud activities for the two entities are now performed under a single Fraud Unit at TDI and all enforcement attorneys are consolidated within one legal division. The agency is in the process of adopting rules to allow the consolidation and consistent practices regarding assignment of Independent Review Organization (IRO) requests and oversight of IRO review activities. A team of staff from across the agency is also working to create a uniform data-driven complaint handling process. Rulemaking is conducted in a coordinated manner, using teams comprised of staff from across all affected programs within TDI. Intra-organizational communication is enhanced through regular meetings of a TDI Workers' Compensation Steering Committee and a Data Strategies Group that identifies critical data needs for measuring reform progress.

To enable the organization to achieve the system reforms, the Commissioner of Workers' Compensation has reorganized the division by establishing four deputy-level units reporting directly to the Commissioner: Legal and Compliance, Dispute Resolution, Field Services, and Workplace and Medical Services. As part of this new structure, one operational unit now focuses on coordinating the services provided to employers, including safety and return-to-work services, with the goal of improving overall system performance.

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Challenge: HB 7 Organizational Impact, Continued

Analysis, continued

As is the case with most organizational changes of the magnitude prescribed by HB 7, the merger has created feelings of disruption and disorientation among staff affected by the changes. The differences in organizational culture and the difficulties of managing staff in two separate headquarter offices and more than 24 field offices present barriers to integration of all the staff into a truly cohesive agency.

Managers and staff have been required to think creatively, emphasize the positive, and work longer hours. Both DWC and Administrative Operations have experienced turnover due to the uncertainties engendered by the change.

Challenges facing the agency because of organizational issues associated with the HB 7 merger can be grouped into the following categories:

- governing structure
 - consolidation of administrative support functions
 - Business Process Improvement project (TXCOMP)
 - funding reductions, and
 - reexamining similar functions within TDI.
-

Strategic Response

• **Governing Structure**

Continue efforts to unify the agency.

The Commissioner of Insurance and the Commissioner of Workers' Compensation have been in constant and close communication to ensure consistency in policies. Their effort is essential to the success of the merger, and it will continue.

The Commissioners are supportive of the coordinated rulemaking that involves teams comprised of staff from across all affected areas.

In addition, the Commissioners have recognized the difficulty of creating a truly cohesive agency with two headquarter offices. Accordingly, they have asked the Texas Building and Procurement Commissioner (TBPC) to work with TDI to identify options for co-locating DWC with the rest of TDI. The physical consolidation of the agency is critical to unification efforts.

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Challenge: HB 7 Organizational Impact, Continued

Strategic Response, continued

- **Consolidation of Administrative Support Functions**

Ensure appropriate administrative support to the entire agency.

Efforts to improve efficiency of administrative services will continue, as will training and change management for DWC staff on administrative procedures.

TDI will continue to provide administrative support for OIEC, using separate accounting, payroll, e-mail, server networks, purchasing systems and reporting mechanisms.

- **Business Process Improvement Project (TXCOMP)**

Complete the TXCOMP project within standards set by the Commissioners.

Staff of DWC and Information Technology Services (ITS) will continue working to stabilize and complete the TXCOMP project, including the initiative to move from a mainframe to a server environment. TDI has restructured the project to allow for better accountability and decision making. The overall change in approach will provide necessary automation and improve business processes of workers' compensation oversight and regulation.

- **Funding Reductions**

Ensure appropriate funding for the agency.

During the 80th Legislative Session, TDI will request appropriate funding levels to support the redesigned agency.

- **Reexamining Similar Functions within TDI**

Integrate functions where possible to achieve greater efficiencies and consistency of services.

TDI will continue integrating similar functions, as it has done with criminal fraud investigations, oversight of Independent Review Organizations and legal enforcement. For more efficient and consistent handling of complaints, DWC will pursue a project to expand TDI's paperless complaint-handling process to include workers' compensation complaints.

Challenge: Changing Market Conditions

Analysis

The primary responsibility of TDI is to regulate the insurance industry. TDI must adapt its regulatory practices and workforce to respond to changing market conditions. For FY 2007-2011, TDI anticipates that emerging industry practices for minimizing disaster losses, health insurance costs, technological advancements, innovative risk management, and increased insurer consolidation will impact how TDI continues to regulate the industry.

Hurricane experience in FY 2006 could have an impact on the price and availability of residential and commercial property insurance in the Texas coastal region due to rising catastrophe reinsurance costs, readjustment of catastrophe models, and reevaluation of business models that manage catastrophe exposure. As a result of these changes, TDI began to see voluntary market insurers limiting their wind coverage along the coast after Hurricane Rita. This initial reaction may be an indicator of an increased reluctance by the industry to offer coverage in disaster prone areas, regardless of insurers' ability to raise rates.

Approximately 30 percent of Texans reside in counties along the Texas Coast and adjacent counties. When wind coverage is not available through the voluntary market, eligible Texans may obtain coverage through the state's catastrophe pool, the Texas Windstorm Insurance Association (TWIA)¹. The existing funding mechanism for TWIA losses places the State General Revenue Funds at risk if the statutorily designated sources of funding are not sufficient to pay claims. For this reason, a critical issue will be to adequately fund TWIA.

The affordability and availability of health insurance are also key issues facing TDI for FY 2007-2011. Texas has one of the highest uninsured rates in the country and increasing numbers of Texans may be underinsured. In 2004, the Current Population Survey, U.S. Census Bureau reported that more than 25 percent of the Texas population was uninsured, compared to a national average of 15.7 percent. Rising health insurance costs, high percentage of immigrants, low participation rates in employment-based insurance and in government-sponsored plans all contribute to Texas' growing uninsured population. Through a federal State Planning Grant on Health Care, TDI conducted surveys in 2001 and 2004 to better understand the uninsured and underinsured populations. Among uninsured small businesses, 73 percent reported that high costs made health insurance unattainable. Consumer choice plans were established to address this issue, but initial response to these plans has only been moderate.

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¹ Created in response to Hurricane Celia in 1971, TWIA provides windstorm and hail coverage for property owners in areas of the state where it is not readily available.

Challenge: Changing Market Conditions, Continued

**Analysis,
continued**

Another way small-business owners have tried to overcome the problem of affordability of health insurance is by purchasing plans with very limited benefits. Though these plans may provide some coverage of routine medical needs such as occasional doctor visits, limited lab services and medications, they do not meet the insurance needs of individuals with chronic conditions, or catastrophic illness or injuries. In addition, the fact that such a plan is available to them, even if they chose to decline the coverage, precludes them from seeking coverage from the Texas Health Insurance Risk Pool.

Although the agency strives to ensure that affordable health insurance options are available in Texas and will continue to do so, it is important to note that health insurance is not synonymous with health care. Health care supply drives demand. In other words, as new treatments and means for paying for them become available, consumers expect access to these expanded services. Further, insurance or risk transfer business models may not hold up in the future because cost increases and utilization seem inevitable as the population ages and their health care demands increase. Insurance business models work most efficiently for infrequent but measurable events.

Market conditions are a direct result of the business practices of insurance companies, which are driven by company leadership. The current demographic profile of the industry does not adequately reflect the diversity of the state of Texas and TDI is aware that company policy decisions could be enriched by more diverse management.

Recent technological advancements in the administration and processing of insurance related transactions have transformed much of the insurance industry in a relatively short period of time. In 1996, Congress enacted Health Insurance Portability and Accountability Act (HIPAA). Among its many provisions, the law imposed a standard format and data content requirement for all electronic insurance claims beginning in October 2003. As companies have adapted to the federal legislation and subsequent state clean claims requirements for electronic transactions, TDI has worked closely with insurers and HMOs to ensure that companies take appropriate steps to convert from old claim processing systems to new, standardized systems required under both federal and state law. Failure to comply with the new standards can result in significant financial penalties, but, more importantly, have the potential to delay the processing and payment of insurance claims for services already provided. Widespread problems could potentially affect the financial solvency of both insurers and providers if doctors and hospitals encounter significant delays in receiving payment for services provided.

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Challenge: Changing Market Conditions, Continued

**Analysis,
continued**

While these changes should, over time, improve the efficiency of the health insurance and health care system, they also continue to pose new challenges for the insurance and health care industries, as well as TDI staff. As part of TDI's oversight and enforcement of clean claim requirements, TDI reviews electronic transactions that are the subject of disputes when complaints are filed by providers or insureds.

In addition to technology for electronic claim transactions, technology has also shaped the regulatory process for filings by allowing companies to submit forms through the NAIC System for Electronic Rate and Form Filing (SERFF) and the Multi-State Review (MSR) electronic filing process.

Legislators, regulators and insurers recognize the need to add efficiencies to the current system of form and rate review and approval. A more efficient review and approval process that maintains consumer protections, gives the consumers more timely access to competitive, approved product options. Texas is one of 27 states to enact the Interstate Insurance Product Regulation Compact (IC), which supports more effective and efficient submission, review and approval of life, annuity, long-term care and disability insurance products. TDI has actively participated in a National Association of Insurance Commissioners (NAIC) working group developing standards, bylaws and filing rules for the IC. As a member of the IC, Texas will continue to participate in the finalization and adoption of bylaws, rules product standards and ongoing management oversight. Because the standards will reflect multiple states' interests, TDI will need to monitor adopted standards for inconsistencies with life, annuity, long-term care and disability insurance products filed with TDI rather than the IC.

MSR is another initiative to support more efficient and timely review and approval of insurance products. TDI worked with regulators from Florida and California to develop annuity standards that met all requirements of each of the state's insurance laws. The states agreed to use the Florida electronic filing system to accept the annuity forms, jointly review for compliance, and approve for use in all participating states. Since its introduction, the MSR initiative has grown to include Washington DC, Georgia, Louisiana, and Nevada.

Challenge: Changing Market Conditions, Continued

**Analysis,
continued**

Insurers are now using data mining technology and methodologies to establish rates. In the insurance context, data mining can be defined as a data search to identify unknown relationships that may predict differences in expected losses among insured, thus establishing new risk classifications. Although the use of credit scoring is perhaps the most extensively used example of data mining to differentiate among risks today, insurers are looking at additional information such as a policyholders' occupation or educational level as another means of differentiating risks. The impact of this practice is that individual policyholders may experience large rate differentials as insurers try to further segment the market by isolating Texans that fall into the new risk classification groups. Individuals disadvantaged by the new classification schemes, which have not been analyzed for actuarial soundness by the agency, may not be able to find affordable alternatives and may forgo insurance altogether.

Due to the complex relationship among insurance carrier insolvency, guaranty funds and revenue to the state, TDI and the Legislature have placed a high importance on financial analyses and examination of companies. Insolvencies adversely impact policyholders and, ultimately, state revenue.

The increasing practice of insurers merging into large multi-state companies creates challenges for state regulators. Insurance companies operating within groups often share risk through pooling agreements or reinsurance agreements and a catastrophic loss occurring anywhere in the world may directly affect the financial condition of an insurer located in, or doing business in Texas. As state regulators adapt to consolidation and/or globalization, a more comprehensive approach to insurance regulation is needed. Additionally, transactions at the holding company level, which affect parent or affiliated companies, may not themselves be regulated by insurance laws but require TDI attention because of the solvency implications for insurers (parent or affiliate).

TDI's analysis of changing market conditions concentrates on the following areas:

- availability and funding of wind and hail coverage
- affordability and availability of health insurance
- electronic transactions and technology
- data mining
- insurer solvency, acquisitions and mergers, and
- development of future insurance professionals.

Continued on next page

Challenge: Changing Market Conditions, Continued

Strategic Response

TDI will pursue a number of initiatives and activities to address changing market conditions.

- **Affordability and Availability and Funding of Wind and Hail Coverage**

Improve solutions for providing wind coverage along the Texas Coast.
Bills introduced in the 79th legislative session (2005) considered changing the funding structure of TWIA, and a legislative committee was formed to further study funding alternatives in the interim. Additional legislative proposals are anticipated in upcoming sessions. TDI will work with the Legislature as lawmakers consider new approaches to solving the TWIA funding issue. Some suggestions for this approach may include the use of bonds, a more flexible rating scheme for TWIA, and expanded use of reinsurance.

Additionally, TDI will monitor the national debate regarding the need to establish a comprehensive, federal catastrophe program to cover losses from wind storms, floods, and hurricanes.

- **Availability of Health Insurance**

Ensure access to affordable health care options.

Developing affordable alternatives and educating the public about health insurance will remain a priority for TDI. TDI will also continue to evaluate the effect of newly established health care cooperatives and consumer choice health care plans on insurance costs and rates of participation. TDI is currently evaluating data collection requirements and will develop a comprehensive approach to collect adequate data for evaluating factors contributing to increasing health insurance claims. TDI will continue to expand the information available to consumers and will increase efforts to educate the public about the value of health insurance through a variety of methods, including providing public speakers, updating and expanding consumer publications and information materials. TDI has also developed a website (www.TexasHealthOptions.com) specifically designed to help consumers shop for health insurance and identify other health care resources.

- **Electronic Transactions and Technology**

Assist with industry's transition to electronic technology.

As more electronic transactions become standardized under HIPAA, TDI will continue to work with the industry to ensure a smooth transition that minimizes disruptions for providers and consumers while achieving the improved simplification and administrative cost savings that are the goals under HIPAA.

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Challenge: Changing Market Conditions, Continued

Strategic Response, continued

- **Electronic Transactions and Technology, continued**

Additionally, just as TDI developed new training materials and processes to ensure staff were adequately prepared to process complaints regarding electronic claims transactions, TDI will update staff training as additional HIPAA transactions are deployed. Finally, TDI will continue to review electronic transactions that are the subject of disputes when complaints are filed by providers or insureds as required by oversight and enforcement of clean claim requirements.

Technological changes are also being added to the form and rate review process with the introduction of the Interstate Compact, MSR process and SERFF. TDI will monitor the product standards adopted for the Interstate Compact and, where appropriate, apprise committee members and/or the Texas Legislature if they do not align with Texas statutes, and rules. TDI will develop MSR standards for life insurance to provide the industry with similar electronic filing opportunities for life insurance products.

- **Data Mining**

Ensure rates are actuarially justified and inform Legislature of changes in rate classifications.

TDI will monitor rates and work with insurers to ensure the factors used to classify and rate risks are actuarially justified. As classification systems become more refined, the price differential between those who receive the best rates and those incurring the worst rates may become substantial. TDI will apprise the Legislature and other policymakers of the impact the new classifications may have on various segments of the market, such as underserved areas.

- **Insurer Solvency, Acquisitions, and Mergers**

Improve TDI monitoring and examination processes to ensure insurer solvency and to preserve insurance options for Texans.

By automating monitoring tools and developing staff, TDI will improve the financial examination processes, thereby increasing the agency's ability to monitor industry solvency.

TDI will continue to coordinate with other state insurance department examinations staff to participate in joint-examinations of insurers. As company transactions become larger and more complex, such cooperation is essential for TDI to handle its statutory mandates in light of the increased depth and scope of financial regulation. A comprehensive approach to insurance regulation should include sharing of information among state regulators and monitoring activities at the holding company level.

Continued on next page

Challenge: Changing Market Conditions, Continued

Strategic
Response,
continued

- **Development of Future Insurance Professionals**

Work with universities and public education institutions in Texas to offer insurance-specific curriculum.

This TDI initiative aims to improve insurance literacy and insurance leadership skills, focusing on diverse populations. By partnering with universities and public education institutions to offer insurance curriculum to the future leaders of Texas, TDI hopes to generate interest in the insurance field and encourage students from diverse backgrounds to pursue careers in insurance.

Challenge: Disaster Readiness and Response

Analysis

TDI staff members participated in the response and recovery efforts to Hurricanes Katrina and Rita by providing evacuees with insurance information and assisting the evacuees with insurance claims at the Federal Emergency Management Agency Disaster Recovery Centers (DRCs). In addition to staffing the DRCs, the agency's consumer assistance activities expanded to include answering telephone inquiries for extended hours and on weekends, delivering ice and water to rural areas, completing fire safety surveys, promoting consumer awareness, and inspecting repairs to homes and commercial buildings so consumers could qualify for windstorm coverage.

The impact of Hurricanes Katrina and Rita emphasized the critical need for preparedness so that local, state, and federal agencies can execute a rapid, coordinated response to disasters and other emergencies.

TDI must be proactive by promoting consumer awareness and monitoring industry preparedness. TDI must also be ready to respond and assist consumers with insurance related issues immediately following a disaster. Equally important, TDI has a responsibility to monitor insurers' overall financial condition, including the ability to continue coverage and services in the event of a disaster.

Consistent with TDI's expectation that the industry be able to respond to and continue operating following a disaster, TDI's FY 2006 Homeland Security Strategic Implementation Plan sets forth strategies for agency response to terrorism, man-made disasters, and natural hazards. Additionally, the implementation plan outlines the agency processes to ensure business continuity following a disaster. Business continuity processes and procedures are further detailed in TDI's program and agency disaster recovery plans.

The initiatives and activities TDI has planned for disaster readiness and response fall into the following categories:

- communication and coordination
- public awareness and assistance
- insurer readiness
- insurer solvency surveillance, and
- TDI business continuity planning.

Continued on next page

Challenge: Disaster Readiness and Response, Continued

Strategic Response

TDI's approach for meeting this challenge are described below.

- **Communication and Coordination**

Increase efforts to foster communication and coordination among key players.

Communication among all key players – the Federal Emergency Management Agency (FEMA), the Governor's Division of Emergency Management (GDEM), other state agencies, local government agencies, insurers, HMOs, agents, trade associations, consumer groups, and individual consumers – is essential. TDI leads the Texas State Disaster Coalition (TSDC), whose members include the above entities and whose objective is to facilitate coordination and communication in the event of a major disaster. TSDC places TDI in the unique position to bring these groups together on an ongoing basis to identify opportunities for improvement and share best practices so that all are ready to assist Texans when disaster strikes.

- **Public Awareness and Assistance**

Promote public awareness and continue public assistance efforts.

Public education and assistance is essential to minimizing the negative impacts of a disaster. TDI plans to expand education efforts to improve public awareness about disaster preparedness. For example, TDI has added a home inventory checklist to its Web site. TDI also plans to partner with other state agencies and consumer groups to reach more consumers with disaster readiness tips.

TDI will increase promotion of the Insurance Assistance Centers, sites where TDI representatives and insurance company representatives co-locate to provide direct and timely assistance to consumers who have disaster claims.

TDI continues to improve its disaster response activities. TDI's Executive Management Team has made this a priority, identifying specific solutions for efficient and effective response. Through training, planning and increased inter- and intra-agency communication, TDI hopes to improve its already effective customer assistance activities.

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Challenge: Disaster Readiness and Response, Continued

Strategic Response, continued**• Insurer Readiness**

Ensure that insurers have catastrophe plans and business continuity plans. TDI has taken steps to protect the insurance sector and Texans in general from the adverse affects of a regional or state disaster by surveying insurers to assess disaster preparedness. In response to the most recent survey, 99 percent of companies certified that they had business continuity plans in place and 90 percent certified that they had plans to address a surge in claims during a regional or state disaster.

As part of the financial examinations monitoring process, TDI reviews insurers' disaster plans to verify that they have adequate management and systems controls to continue operations and financial reporting to TDI during a disaster. This review also includes verifying that companies have an adequate plan for preserving books and records, as well as an adequate plan for backup and recovery of essential data. TDI will continue to use these surveys and examinations to identify exposure and, when appropriate, take actions to encourage companies to mitigate exposures and effectively recover critical functions.

TDI will consider expanding monitoring activities to address recommendations set forth through a November 2005 United States Government Accountability Office report on "Insurance Sector Preparedness." Improvements may include requesting evidence of plan testing, confirming insurer contingencies for addressing staffing deficiencies during a disaster, consulting the TSDC regarding guidelines for insurer catastrophe response plans, and adjusting regulatory tools to require the industry to address identified disaster planning deficiencies.

• Insurer Solvency Surveillance

Monitor insurers' financial condition to ensure solvency following a regional or state-wide disaster.

TDI will continue to examine and monitor insurers' overall financial condition, including possible exposure to national or state disasters. In this way, TDI identifies those companies that may have potential exposures that would significantly affect their ability to serve Texas policyholders, for example, issues with a company's geographical distribution of exposures, catastrophic reserves, and reinsurance. TDI plans to continue working directly with insurers to develop action plans to mitigate potential financial impacts.

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Challenge: Disaster Readiness and Response, Continued

Strategic Response,
continued

- **TDI Business Continuity Planning**

Maintain and refine planning to ensure continuity of operations following a disaster affecting the agency.

TDI will expand business continuity planning to include a more thorough risk analysis of exposures to TDI field offices and staff. The merger of the workers' compensation agency into TDI presents new opportunities and challenges for disaster recovery planning. Having two "headquarters" facilities in Austin and field offices throughout the state requires TDI to establish more complex back-up capabilities to perform key functions and to address the unique circumstances of each location in disaster recovery planning efforts. TDI will look for opportunities to better utilize the Division of Workers' Compensation (DWC) central office and field offices for improved response and recovery of agency operations.

Challenge: Insurance Fraud

Analysis

Insurance fraud occurs when people deceive an insurance company into paying a claim to which they are not entitled or when an agent or insurer deceives a consumer into purchasing bogus coverage. Efforts to measure losses due to insurance fraud have been difficult because so much goes undetected. The Coalition Against Insurance Fraud estimates that insurance fraud costs Americans at least \$80 billion a year, or nearly \$950 for each insured family annually.

The detection and prosecution of insurance fraud cases is a continuing challenge for TDI, the state, and the insurance industry as a whole. Technology is changing the face of fraudulent actions. The Internet alone has facilitated an increase in identity theft incidents and in the number of fake insurance companies and products marketed.

Maintaining effective relationships with fraud and law enforcement entities throughout the country is essential to developing cases that can be prosecuted. TDI recognizes the importance of coordination and cooperation among various parties to strengthen working relationships and to develop a proactive approach to addressing fraud. Communication among parties helps identify new insurance fraud trends and develop investigation techniques for more successful prosecution.

TDI's Insurance Fraud program is striving to change the wide-spread perception that insurance fraud is a victimless crime. As mentioned above, insurance fraud is an offense that proves costly to insurance companies and consumers alike. By educating the public on the consequences of this crime and raising awareness, the program hopes to both reduce the number of fraud cases committed, as well as increase detection.

TDI's Fraud program is certified as a law enforcement agency, which employs licensed peace officers and other professionals who investigate fraud cases and make referrals to criminal district attorneys and federal prosecutors. Insurance fraud cases include various claim fraud schemes, deceptive agency practices, fraudulent activities of company officers and directors, unauthorized insurance fraud schemes and worker's compensation fraud. TDI's fraud prevention activities will focus on the following:

- technological advancements
- coordination and cooperation, and
- public awareness.

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Challenge: Insurance Fraud, Continued

Strategic Response

TDI's approach for effectively identifying and prosecuting insurance fraud cases will include the following.

- **Technological Advancements**

Adapt investigative processes to keep pace with schemes allowed by recent technological advances.

TDI will continue to stay abreast of the changing investigative processes associated with technology advances in the financial business world. This new era will require increased emphasis on training in advanced forensic white-collar crime processes and the acquisition of technology equipment for law enforcement. Technology can also be used to enhance the agency's prosecution efforts. To improve the management and handling of cases being investigated, TDI will pursue solutions for replacement of the Fraud program's current case management system.

- **Coordination and Cooperation**

Develop and enhance cooperative efforts between the industry, government and law enforcement.

Through a cooperative effort between TDI's Fraud program and the Dallas County District Attorney, TDI hired a special prosecutor that was assigned to the Dallas District Attorney's office and appointed as a special assistant district attorney to handle cases referred by the Fraud program. With the expertise and assistance of TDI's special prosecutor, insurance fraud cases referred by TDI receive special handling, which results in faster legal actions within the court system. The special prosecutor initiative has exceeded expectations, enhancing prosecutions and outreach efforts in the greater Dallas area. TDI will evaluate options for pursuing similar initiatives in other major cities throughout the state.

TDI will also work with the insurance industry to explore opportunities for cooperative initiatives involving the investigation of organized fraud groups that perpetrate fraud against insurance companies.

In cooperation with anti-fraud organizations and the industry, TDI will look for opportunities to identify and support strengthening laws against insurance fraud and developing pro-active enforcement strategies to prevent or reduce fraud occurrences.

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Challenge: Insurance Fraud, Continued

Strategic
Response,
continued

- **Public Awareness**

Educate public and industry on insurance fraud trends and issues.

TDI will develop strategies to educate the public and the industry to change the perception that insurance fraud is not a “victimless” crime. TDI hopes its education efforts will positively influence behavior to reduce insurance fraud. Strategies will include providing information to consumers through TDI’s Web site and conducting formal presentations for industry representatives.

Challenge: Fire Safety

Analysis

TDI's State Fire Marshal's Office (SFMO) develops and promotes methods of protecting the lives and property of the citizens of Texas from fire and related hazards. The SFMO works with the public, regulated fire service industry, all branches of the fire service, local governments, and other state governments.

The SFMO strives to gain a greater understanding of the problems and trends associated with fires in Texas. To achieve this mission, the SFMO conducts direct fire safety inspections and fire cause investigations. Currently the SFMO operates reactively rather than proactively; most often providing services as a response to a specific request, rather than proactively assessing the needs of the communities they serve.

The State Fire Marshal has identified a need to redefine the SFMO's service delivery model to be more proactive. The strategy includes reprioritizing operations to enhance service quality, with the goal of reducing the loss of life and property on the broadest scale possible. The delivery model encompasses all areas of the state, not just those communities that receive direct inspection or investigation services.

Activities can be grouped as follows:

- enforcement
 - public awareness and assistance, and
 - communication and coordination.
-

Strategic Response

SFMO will use the following strategies to meet the ongoing challenge.

- **Enforcement**

Organize operations to meet enforcement responsibility.

SFMO will evaluate statutory authority and realign operations to increase the administrative effectiveness of enforcement activities. This process will ensure that statutory responsibilities are met based on the guidance and direction taken from all relevant sources including incident and event requests.

SFMO will use enforcement data, such as information gained from individual inspections and investigations, as well as data from other applicable sources in order to develop educational fire prevention programs and provide fire safety information to benefit all Texans.

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Challenge: Fire Safety, Continued

**Strategic
Response,
continued****• Public Awareness and Assistance**

Provide community outreach programs to develop strategies for fire prevention.

SFMO will produce and deliver educational programs and information that support fire prevention in Texas and address state-wide, regional, and community-based needs. Individual SFMO staff will be assigned specific regions of the state for monitoring community needs.

The SFMO will identify which populations are most vulnerable to fire hazards based on relevant data and potential for the greatest loss of life and property. The SFMO will determine how to best apply resources for preventing and alleviating the problems associated with identified vulnerable populations.

SFMO will respond to the needs of Texans in emergency situations, such as natural disasters, by working to ensure fire safety is included in state and local emergency response plans. The SFMO will work to provide educational material on fire safety to Texans likely to be affected by natural disasters such as hurricanes, tornados, and flooding.

• Communication and Coordination

Enhance fire prevention services through partnerships.

SFMO will leverage its resources by creating and maintaining partnerships with cities, counties, and other external entities, including the creation of customer groups to advise on fire-related issues. SFMO will collaborate with state and federal agencies to optimize resources in support of fire prevention and safety in the community.

Legislative Changes

Analysis

New legislation at both the state and federal levels may affect agency operations and regulatory authority. Some of the more significant legislative initiatives at both the state and federal level are discussed below. At the state level, the 79th Legislature passed, Senate Bill (SB) 1670, which mandates an insured vehicle verification program. At the federal level, initiatives that limit state regulatory authority, if passed, could greatly impact agency operations.

The Texas Financial Responsibility Verification Program (FRV), requires TDI, in consultation with the Texas Department of Public Safety (DPS), the Texas Department of Transportation (TxDOT), and the Texas Department of Information Resources (DIR), to “establish a program for verification of whether owners of motor vehicles have established financial responsibility.” SB 1670 requires implementation of the verification program for vehicles covered under a personal auto insurance policy, followed by vehicles covered under a commercial insurance policy as the implementing agencies deem feasible. The primary goals of the program are to reduce fraud and expand insurance coverage of vehicles operating in the Texas. More than 30 states operate some form of FRV program. Experience in states operating programs similar to the Texas program indicates that this approach can lower the uninsured motorist rate. Based on extensive research and feedback from stakeholders, critical factors that could affect enforcement include data integrity and public awareness.

The McCarran-Ferguson Act is a 1945 federal law that provides that states, rather than the federal government, have the authority to regulate the business of insurance. Persistent advocacy for moving to federal regulation of insurance includes industry complaints of non-uniformity in insurance regulation by the 50 states. Proponents favor the federal government preempting, wholly or partially, the state regulation of insurance. While there has been no repeal of McCarran-Ferguson and no wholesale preemption of state insurance regulation, statutes have been passed at the federal level that supersede state insurance law. For example, federal law does not allow the agency to regulate self-funded Employee Retirement and Income Security Act (ERISA)² plans even though much of the health care coverage in Texas is provided through self-insured or self-funded ERISA plans.

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² ERISA is a federal law governing certain employer established benefit plans. This law has been in place since 1974. Federal law provides that ERISA preempt state laws relating to self-insured or self-funded ERISA plans.

Legislative Changes, Continued

Analysis, continued

There are also several draft bills in Congress that would alter state regulation, including the State Modernization and Regulatory Transparency Act (SMART)³ and the National Insurance Act of 2006 (Optional Dual Charter)⁴. SMART, if enacted, could preempt significant areas of state regulation of insurance, such as rate and policy form approval as well as market conduct and financial examinations. The Optional Dual Charter if enacted could significantly impact state regulation of insurance and could negatively affect the state's consumer protection authority.

Challenges facing the agency because of federal and state legislative changes can be grouped into the following categories:

- Financial Responsibility Verification (FRV) program, and
 - regulatory authority.
-

Strategic Response

• **Financial Responsibility Verification (FRV) Program**

TDI will continue to be the lead agency in implementing and operating the FRV program.

First, TDI will provide sufficient data testing and a clean-up phase. While this will not eliminate 100% of the anticipated errors, it is expected that the data quality will continue to improve as data problems are identified and resolved. TDI anticipates establishing a high threshold for data matches, which must be met before the program can be fully implemented.

In addition, TDI and other implementing agencies will develop a media campaign to inform consumers about the new program. The media campaign will encourage consumers to proactively ensure consistency between the vehicle identification number (VIN) on their insurance policy, the VIN on their vehicle registration, and the VIN on the vehicle itself. The media program will also serve to encourage citizens to comply with financial responsibility laws prior to the implementation of the FRV program.

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³ The goal of this draft bill is uniformity in insurance regulation.

⁴ This legislation would create an alternative to state regulation of insurance. The legislation would create a new federal agency to regulate national insurers.

Legislative Changes, Continued

**Strategic
Response,
continued**

- **Financial Responsibility Verification (FRV) Program**, continued
Next, TDI and other implementing agencies will seek to develop a robust and dynamic system that can be readily modified to accept changes in design and format. TDI will continually assess the cost effectiveness of the FRV program and advances in technology to improve and modify the program as necessary.

Finally, TDI and other implementing agencies will work together to propose future legislation aimed at improving the effectiveness of the FRV program. The proposed legislation will include enforcement tools to be incorporated by DPS and/or TxDOT.

- **Regulatory Authority**
Influence state and federal legislation as possible to maintain state regulatory authority.
TDI will continue to work with the National Associations of Insurance Commissioners (NAIC), the National Conference of State Legislators, and the National Conference of Insurance Legislators to advise them regarding all pending federal legislation.

At the state level, TDI will continue to cooperate with legislators' effort to achieve consistency between Texas insurance statutes and those of other states, where appropriate.
