

oppaga Special Report



January 2004

Report No. 04-09

Office of Public Counsel Involvement in Medical Malpractice Rate Review Process May Help Limit Rate Increases

at a glance

Involving the Office of Public Counsel in the medical malpractice insurance rate determination process may help to limit premium increases. The office has been effective in helping lower consumer utility bills through its involvement in utility rate setting cases. States that have authorized involvement by similar entities in insurance rate cases report that these advocates help limit premium increases.

Scope

The 2003 Legislature directed OPPAGA to determine the feasibility and merits of authorizing the Office of Public Counsel to

- examine insurance rate filings for medical malpractice submitted to the Office of Insurance Regulation;
- make recommendations to the Office of Insurance Regulation regarding such rate filings; and
- represent the public in any hearing related to such rate filings.¹

In addition, the study evaluates the effectiveness of the current authority of the Office of Insurance Consumer Advocate to perform such functions.

¹ As specified in Ch. 2003-416, *Laws of Florida*.

Background

Patients injured while receiving health care can sue health care providers for medical malpractice. Medical malpractice insurance operates much like other types of insurance, with insurers collecting premiums from policyholders in exchange for an agreement to defend and pay future claims within the limits set by the policy.² Medical malpractice premiums are based primarily on anticipated losses on claims and related expenses and the expected income from investment of premiums payments. These premiums differ widely by medical specialty and geography. Premiums paid for traditionally high-risk specialties, such as obstetrics, are usually higher than premiums paid for other specialties, such as internal medicine. In Florida, premiums for medical malpractice insurance also vary across geographic areas within the state.

Beginning in the late 1990s, malpractice premiums began to increase at a rapid rate for most, but not all, physicians in some states.³ In Florida, rate increases for physicians and surgeons from the top 15 professional liability insurers (ranked by direct written premium in Florida as reported December 31, 2001) ranged from 33.5% to 149.9% between January 1, 2001, and January 1, 2003. Overall, rates increased by an average of 73%,

² *Medical Malpractice – Insurance – Multiple Factors Have Contributed to Increased Premium Rates*, GAO Report No. 03-702, August 2003.

³ *Medical Malpractice – Implications of Rising Premiums on Access to Health Care*, GAO Report No. 03-836, August 2003.

weighted for market share. Rate increases for the top three insurers ranged from 74.3% to 81.3% for the two-year period.⁴

The increased premium rates were attributed to several factors including increased losses on paid medical malpractice claims and decreases in insurers' income from premium investments.⁵ In response to these rising rates, the 2003 Legislature reformed many existing laws relating to medical malpractice in Florida. These reforms were designed to stabilize and reduce medical malpractice insurance premiums by limiting insurance company's losses on medical malpractice claims and by requiring the Office of Insurance Regulation to reassess the factors used to determine premiums for medical malpractice insurance.

Insurance rate review process

Florida regulates medical malpractice insurance to help ensure that rates used to calculate premiums reflect the lowest possible prices, while making certain that insurers will be able to pay for any future claims covered by the insurance policy.^{6,7} Maintaining a balance between these two objectives is beneficial to both the healthcare practitioners who purchase insurance and the patients receiving healthcare services from these practitioners. Healthcare practitioners benefit because they receive assurance that their premiums are not excessive and that they will be compensated for any future losses covered by the insurance policy. Patients benefit from effective regulation through lower overall health care costs and through greater assurance that medical malpractice insurance companies will be able to pay court-ordered awards resulting from medical malpractice claims.

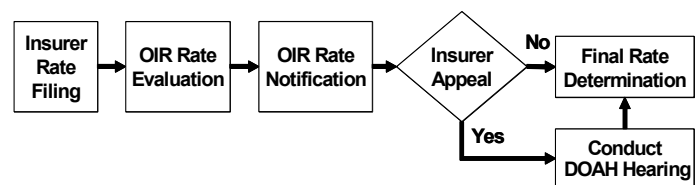
Two state entities participate in the rate review process for medical malpractice insurance. The Office of Insurance Regulation (OIR) performs a variety of regulatory functions related to insurance companies, including evaluating whether medical

malpractice rate changes proposed by insurers are excessive, inadequate, or unfairly discriminatory. The office is a unit of the Financial Services Commission within the Department of Financial Services.⁸ The commission is composed of the Governor and the Cabinet. For Fiscal Year 2003-04, the Office of Insurance Regulation was appropriated \$17.5 million and 264 full-time equivalent (FTE) employees.

The Office of Insurance Consumer Advocate was created in 1990 to represent the general public of the state in the insurance regulatory process.⁹ The insurance consumer advocate reports directly to the Chief Financial Officer, but is not otherwise under the authority of the department or of any employee of the department. For Fiscal Year 2003-04, the Office of Insurance Consumer Advocate was allocated \$350,000 and four FTE employees.

The process used to review medical malpractice insurance rates is similar to the process used for all other property and casualty insurance lines. As shown in Exhibit 1, the medical malpractice insurance rate review process begins when an insurer submits a rate filing to the OIR.¹⁰

Exhibit 1 Florida's Medical Malpractice Rate Setting Process Is Similar to Other Lines of Insurance



Source: OPPAGA analysis.

⁴ Legislative staff analysis for Ch. 2003-416, *Laws of Florida*.

⁵ *Medical Malpractice – Insurance - Multiple Factors Have Contributed to Increased Premium Rates*, GAO Report No. 03-702, August 2003.

⁶ As specified in s. 627.062, *F.S.*

⁷ A rate is the cost per unit of insurance. When used to calculate a premium, rates must be sufficient to pay expected losses according to frequency and severity, reasonable to the point that insurers do not earn an excessive profit, and not discriminatory or inequitable. Based on the amount of coverage needed, an individual will purchase the appropriate number of units of insurance with the total cost reflected in a premium payment.

⁸ Chapter 2002-404, *Laws of Florida*, created the Financial Services Commission within the Department of Financial Services.

⁹ In 1989, the Legislature passed a bill that expanded the authority of the Office of Public Counsel to include representing the public in certain rate cases and rules proceedings before the Department of Insurance. However, this legislation was subsequently vetoed by the Governor. As an alternative, the Commissioner of the Department of Insurance established the Office of Insurance Consumer Advocate in 1990. The 1992 Legislature codified this position in s. 627.0613, *F.S.*

¹⁰ As specified in s. 627.062(2)(a), *F.S.*, insurance filings are classified as either 'file and use' or 'use and file'. A 'file and use' filing is not generally implemented until after the OIR review of the filing is completed. The rate filing shall be deemed approved if the department does not issue a notice of intent to approve or disapprove within 90 days after receipt of the filing. A 'use and file' filing can be submitted up to 30 days after the effective date of a rate change; however, the insurer is potentially subject to an order by OIR to return to policyholders portions of rates found to be excessive.

Upon receipt, the filing is assigned to an in-house actuary who specializes in the line of business for which the insurer is seeking a rate adjustment. The actuarial analysis includes reviewing the data and the actuarial process used by the insurer in developing the proposed change in insurance rates. Parameters established in Florida law and administrative rule are used to determine if the proposed change in rates is excessive, inadequate, or unfairly discriminatory.¹¹

If OIR's evaluation of the insurer's rate filing indicates that the proposed change in premiums may be excessive, inadequate, or unfairly discriminatory, OIR develops its own recommended rate change. Should OIR's recommended rate change substantiate the findings of the initial evaluation, it will issue a Notice of Intent to Disapprove to the insurer. The insurer may then submit a new rate filing that responds to the findings included in the Notice of Intent to Disapprove or contest the findings through an administrative hearing with the Division of Administrative Hearings (DOAH).

Findings

Office of Insurance Consumer Advocate has not been involved in medical malpractice rate review process

The Insurance Consumer Advocate has chosen not to become involved in the medical malpractice insurance rate review process. The Office of Insurance Consumer Advocate primarily represents the public on appointed boards or applicable forums with the goal to increase consumer awareness on insurance-related issues. Although the office has sufficient authority in s. 627.0613, *Florida Statutes*, to submit a recommendation on a medical malpractice rate filing, it has chosen not to do so.¹² The insurance consumer advocate asserted that the office rarely becomes involved in insurance rate cases and has never challenged a determination by the Office of Insurance Regulation because she believes OIR's insurance rate determination process

has been effective in ensuring that insurance rates are not excessive, inadequate, or unfairly discriminatory. Consequently, she believes that intervening in an insurance rate determination case would not be a cost-effective use of the office's available resources. However, we determined from interviews with stakeholders and other states that the office's organizational placement within the Department of Financial Services could limit its independence, as the office would be required to challenge the rates approved by the officials to whom it reports.

Involvement of Office of Public Counsel in medical malpractice rate review process may help stabilize rates

Other states report that consumer representation in rate setting has stabilized rate changes. In the case of Florida, the Office of Public Counsel's involvement in utility rate determination has caused a reduction in consumer costs and, with sufficient authority, the office could represent Floridians in the process of reviewing medical malpractice rates.

Entities in other states report that consumer representation in the rate review process has stabilized rate changes

Several states authorize either a government or non-government entity to represent consumers in insurance rate cases.¹³ For example, the Texas Office of Public Insurance Counsel is a government entity, independent of the insurance regulatory process, dedicated to public representation in rate cases. The public insurance counsel represents the interests of consumers as a class on matters involving rates, rules and policy forms affecting various personal lines of insurance such as auto, homeowners, title, and credit insurance, and in rulemaking for life, accident, and health insurance. The public insurance counsel represents consumers in hearings before the Texas Department of Insurance, the State Office of Administrative Hearings, other state agencies, and in the courts. The public insurance counsel reported that as a result of its intervention activities, it saved Texas citizens over \$535 million in insurance premiums in 2001.¹⁴ Although the public insurance counsel

¹¹ Statutory parameters are codified in s. 627.062, *F.S.* Other parameters are established in Chapter 4 of the *Florida Administrative Code*. In addition, the evaluation incorporates technical guidelines relative to ratemaking and review published by the Casualty Actuarial Society.

¹² The Office of Insurance Consumer Advocate has statutory authority to examine rate and form filings submitted to the OIR and hire consultants to aid in the review process, make recommendations to the OIR, and represent the public at hearings related to rate filings.

¹³ We identified six states as authorizing intervention in the insurance rate review process by entities dedicated to public representation: California, Georgia, Maine, Maryland, South Carolina, and Texas.

¹⁴ This savings reflects the difference between the requested increase in insurance premiums and the amount that was approved for rate

does not intervene in medical malpractice rate cases, Texas' experience indicates that consumer representation in the rate review process by an independent entity can help mitigate increases in insurance premiums.

California has enacted legislation that, in addition to placing limits on medical malpractice lawsuits, allows consumers to intervene in the medical malpractice rate review process. In 1975, California passed the Medical Injury Compensation Reform Act, which provided liability limits for health care practitioners.¹⁵ In 1988, California's voters passed insurance reform Proposition 103, which required that all proposed insurance rate changes be approved by the Commissioner of the Department of Insurance.¹⁶ For medical malpractice insurance, Proposition 103 also required that the commissioner grant a hearing when challenged by a consumer or advocacy group if the proposed increase is greater than 15%.¹⁷ California's act and Proposition 103 reforms appear to have stabilized medical malpractice by limiting the losses that insurance companies incur from medical malpractice lawsuits and deterring insurers from requesting excessive rate increases.

The Office of Public Counsel's involvement in utility rate determination cases has been effective in reducing costs for consumers

In response to concerns that the public's interests were not being adequately represented by the Florida Public Service Commission (PSC), the Legislature created the Office of Public Counsel in 1974 to provide legal representation for Florida's citizens in utility related matters.¹⁸ The office is independent of the PSC and has the statutory responsibility to advocate the interests of the Florida utility consumer. The office is under the auspices of the Legislature's Joint Legislative Auditing Committee. For Fiscal Year 2003-04, the office was appropriated 14 positions and \$2 million from the General Revenue Fund.

filings where OPIC intervened.

¹⁵ MICRA was challenged in court, but upheld by the California Supreme Court in 1985.

¹⁶ Proposition 103 was also challenged in court, but upheld by the California Supreme Court in 1989.

¹⁷ Prior to passage of Proposition 103, California was considered an 'open competition' state in which competition regulated the marketplace, with the state government role being limited to monitoring insurance company rating practices.

¹⁸ As specified in s. 350.061, F.S.

The Office of Public Counsel is authorized to intervene in all rate proceedings before the PSC involving the major telephone and electric utilities as well as numerous proceedings involving natural gas, and water and wastewater utilities. Intervener status allows the office to file testimony and cross-examine witnesses in rate case proceedings held by the PSC. In addition, when the office intervenes by participating as a party, it also has the right to appeal the commission's decision through Florida's appellate court system. The office reported that as a result of its interventions in utility rate proceedings, Florida utility customers saved over \$1.1 billion in charges for utility services in 2002.¹⁹

With sufficient authority, the Office of Public Counsel could represent the public in the medical malpractice insurance determination process

Public representation in the medical malpractice rate review process can be increased by authorizing Office of Public Counsel involvement in medical malpractice rate cases. To effectively represent the public interest in medical malpractice insurance rate reviews, the Office of Public Counsel would need the same intervention authority as currently authorized for utility rate filings.

For utility rate filings, the office is authorized to intervene in any case and recommend positions deemed to be in the public interest.²⁰ This includes the right to appear before an administrative law judge in a DOAH hearing or an appellate judge in Florida's judicial court system. The right to a hearing in a utility rate setting case is not subject to review and approval by the PSC or any other state entity.

If the Office of Public Counsel were authorized to intervene in medical malpractice rate cases, its decision to request a hearing in a medical malpractice insurance rate case would likely be based upon the results of an actuarial evaluation of the rate filing. This evaluation would determine if the proposed changes will adversely affect the interests of Florida's citizens. Upon this process, the office would notify OIR of the results of its evaluation, providing sufficient time to allow

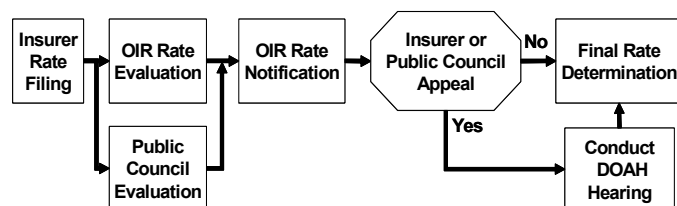
¹⁹ This savings reflects the difference between the requested increase in utility rates and the amount that was approved for rate filings that the Office of Public Counsel petitioned to intervene.

²⁰ As specified in s. 350.0611, F.S.

OIR to consider the results of the evaluation in its initial determination process.²¹

Upon notification to the insurer by OIR of its intent to approve or disapprove a proposed rate increase, either the Office of Public Counsel or insurer would then have the right to request that a hearing be conducted by DOAH.²² The DOAH hearing would allow the Office of Public Counsel, insurer, and OIR to present evidence pertaining to the rate filing. The DOAH administrative law judge would then issue a recommended order for consideration by OIR in their final rate determination.²³ Exhibit 2 depicts this proposed process.

Exhibit 2 Office of Public Counsel Involvement in the Medical Malpractice Rate Review Process Can Be Effectively Implemented



Source: OPPAGA analysis.

Establishing parameters could limit cost of Office of Public Counsel involvement in medical malpractice rate review process

Involving the Office of Public Counsel in medical malpractice insurance rate determinations would require increased funding. The initial evaluation of the rate filing by the Office of Public Counsel would be similar to the process currently used by the OIR in its rate determination process. Costs would be incurred for the time spent by staff and an actuary. For those cases in which the Office of Public Counsel requests an administrative hearing, the

office would incur additional costs.²⁴ The insurance companies submitting the rate filing also would incur costs when a hearing was conducted.

These costs could be limited by specifying the conditions under which the Office of Public Counsel would be involved, which would limit the number of cases that are evaluated and the pool of cases for which a hearing can be requested. These conditions could be based on the extent to which a proposed rate increase would affect statewide rates. For example, the Office of Public Counsel could be authorized only to become involved in rate determinations that reach a specific threshold in affecting statewide rates, such as an increase of 25% or more. As shown in Exhibit 3, there were 11 medical malpractice rate filings with an average statewide increase of 25% or more in Fiscal Year 2002-03.^{25, 26} A threshold would also limit the regulatory burden on insurance companies.

Exhibit 3 The Required Number of Rate Filing Evaluations Can Be Limited by Establishing Conditions for Office of Public Counsel Involvement

Medical Malpractice Insurance Rate Filings	FY 2002-03
Total medical malpractice insurance rate filings	55
Total filings with a statewide average rate change ¹	23
Filings with a statewide average rate change over 25%	11
Filings with a statewide average rate change over 15%	16

¹ The remaining rate filings included rule filings and changes in relativities or excess limit factors.

Source: Financial Services Commission, Office of Insurance Regulation and OPPAGA analysis.

Should the Legislature choose to authorize Office of Public Counsel involvement in the medical malpractice rate review process, the annual cost will be dependent on a number of variables including the number of rate filings reviewed, the number of hearings requested, and whether the

²¹ As specified in s. 627.062, *F.S.*, for a 'file and use' filing, the rate shall be deemed approved if the department does not issue a notice of intent to approve or a notice of intent to disapprove within 90 days after receipt of the filing. Should the Office of Public Counsel decide to not provide OIR with their evaluation results during its authorized review period, we recommend that it lose the right to subsequently intervene in a DOAH hearing.

²² As specified in Ch. 120, *F.S.*

²³ Should the insurer disagree with the final determination by OIR, it can appeal to the First District Court of Appeals. The Office of Public Counsel should not be a party in this proceeding as the appeal involves a dispute between OIR and the insurer.

²⁴ Additional costs would depend on the time needed to prepare for the administrative hearing. For example, OIR reported that the time it takes to prepare for a DOAH hearing ranges from several days to several weeks.

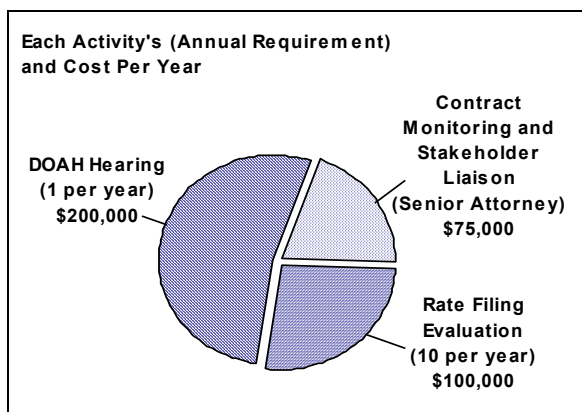
²⁵ As specified in s. 627.41495, *F.S.*, insurers are required to notify policyholders of proposed rate changes with an average statewide increase of 25% or more.

²⁶ In Fiscal Year 2002-03, 55 medical malpractice insurance rate filings were submitted to OIR. Twenty-three of these rate filings had an impact on the statewide average rate. The remaining rate filings included rule filings, changes in relativities, and changes in excess limits factors, etc.

associated activities are contracted or performed by Office of Public Counsel employees. Based on recent rate filing data and OIR activities, we estimated the Office of Public Counsel would require \$375,000 in funding annually. As shown in Exhibit 4, these costs are based on an assumption that the Office of Public Counsel would need one additional full-time employee, be involved in 10 rate filing evaluations a year, and request one DOAH hearing per year. Our estimate is explained in more detail in Appendix A.

Involving the Office of Public Counsel in medical malpractice rate reviews may help to effectively control rate increases. If Florida's experience parallels that of Texas and California, the increased funding for the Office of Public Counsel should be more than offset by savings to health care practitioners from lower malpractice insurance premiums. If the Legislature authorizes the Office of Public Counsel to become involved in medical malpractice rate reviews, the Office of Public Counsel should maintain data on this outcome. Information on the return on this investment will assist the Legislature in making future decisions as to whether funding should be continued or increased.²⁷

Exhibit 4
The Annual Cost of Office of Public Counsel Involvement in the Medical Malpractice Rate Review Process Would Be Approximately \$375,000



Source: OPPAGA analysis.

²⁷ To help determine the direct effect of Office of Public Counsel intervention, we recommend collecting data that compares the percentage of rate increases that insurers sought to the percentage of rate increases that were approved as a result of intervention on behalf of the public. In addition, we recommend collecting data that compares increases in statewide medical malpractice insurance premiums to increases in the national medical malpractice insurance premiums.

Alternatives exist for funding Office of Public Counsel involvement in medical malpractice rate review process

We considered two alternatives to fund the costs associated with involvement of the Office of Public Counsel in the medical malpractice rate review process: using general revenue funding and assessing an annual fee for each medical malpractice insurance policy. Each alternative has advantages and disadvantages. However, it may be more equitable to fund the cost of the Office of Public Counsel's involvement in medical malpractice rate reviews through an increase in insurance premium taxes so that the direct recipients of this service pay for its funding.

As with utility regulation, involvement by the Office of Public Counsel in medical malpractice insurance rate reviews could be fully funded by state general revenue. For Fiscal Year 2003-04, the office was appropriated \$2 million from the General Revenue Fund. This amount covers the costs of all its activities relating to utility regulation. As discussed earlier, we estimate that the office would require an annual funding increase of \$375,000 and one staff position to also provide effective public representation in the medical malpractice rate review process. Using general revenue to support this function offers the advantage of simplicity in that the Office of Public Counsel would have one funding source for all of its activities. It also can be argued that since the public in general benefits from reduced medical malpractice premiums through reduced medical costs, funding of this activity through general revenue may be more appropriate.

However, state general revenue is limited and subject to numerous competing needs, so the Legislature may prefer establishing a dedicated funding source to pay for the Office of Public Counsel's involvement in medical malpractice rate reviews. Funding involvement of the Office of Public Counsel through proceeds from a tax on insurance premiums would ensure that the policyholders who are direct beneficiaries also pay for a significant portion of the costs of associated activities. This alternative also introduces a healthy dynamic, as policyholders are likely to resist fee increases and will question underlying cost increases if not fully justified. Insurance premium tax revenue is the source currently used in Florida to fund all of the activities performed by

both the OIR and the Office of Insurance Consumer Advocate.²⁸ Proceeds from a tax on insurance premiums are also used to fund the Texas Office of Public Insurance Counsel.

We estimate that the costs associated with Office of Public Counsel involvement in the medical malpractice insurance rate review process would require increasing the current insurance premium tax on medical malpractice insurance premiums from 1.75% to 1.80%. This would represent an average increase of approximately \$11 per year for each medical malpractice insurance policyholder in Florida.²⁹

Conclusions and Recommendations

Involving the Office of Public Counsel in the medical malpractice insurance rate determination process may help to limit increases in premiums. States that authorize involvement of entities dedicated to representing consumers reported that it benefits consumers by limiting rate increases. Consumers in Florida have benefited through lower utility bills by the office's involvement in utility rate setting cases.

If the Legislature wishes to provide public representation in the medical malpractice insurance rate review process, we recommend that the Legislature amend s. 627.41495, *Florida Statutes*, to provide the Office of Public Counsel with the same authority to intervene in medical malpractice insurance premium cases as it

²⁸ Insurance Premium Tax receipts are deposited in the Insurance Commissioner's Trust Fund, which the Legislature used to fully fund these entities in Fiscal Year 2003-04.

²⁹ This estimate is based on \$829,122,375 in premiums written for approximately 37,000 policies in Florida for 2002. Based on these premium amounts and number of policies, a .05% increase in the insurance premium tax on medical malpractice insurance premiums would produce \$414,561 in additional revenue, which would result in an average annual increase of \$11.24 per policy.

currently has for utility rate filings. To limit the costs of this activity, the Legislature may wish to establish conditions for involvement by the office. The Office of Public Counsel would require \$375,000 in annual funding if it intervened in those cases in which insurers proposed statewide increases in medical malpractice insurance that averaged 25% or more. This could be funded by general revenue or by increasing the Insurance Premium Tax rate for medical malpractice insurance from 1.75% to 1.80%.

To ensure that data is available to measure the extent to which Office of Public Counsel involvement in the rate review process impacts malpractice insurance premiums in Florida, we recommend that the Legislature require the Office of Public Counsel to maintain data showing the savings to healthcare practitioners resulting from its interventions in rate proceedings, which would enable the Legislature to consider the return on this investment.

Agency Response

In accordance with the provisions of s. 11.51, *Florida Statutes*, a draft of our report was submitted to the Office of Public Counsel, the Department of Financial Services, and the Office of Insurance Consumer Advocate for each to review and respond.

The Office of Public Counsel expressed no opinion on the option in its response, the Office of Insurance Regulation within the Department of Financial Services strongly opposed the option of involving the Office of Public Counsel in the medical malpractice insurance rate review process in its response, and the Office of Insurance Consumer Advocate chose not to respond. Responses in their entirety are available on our website.

OPPAGA supports the Florida Legislature by providing evaluative research and objective analyses to promote government accountability and the efficient and effective use of public resources. This project was conducted in accordance with applicable evaluation standards. Copies of this report in print or alternate accessible format may be obtained by telephone (850/488-0021 or 800/531-2477), by FAX (850/487-3804), in person, or by mail (OPPAGA Report Production, Claude Pepper Building, Room 312, 111 W. Madison St., Tallahassee, FL 32399-1475).

Florida Monitor: <http://www.oppaga.state.fl.us/>

Project supervised by Debbie Gilreath (850/487-9278)

Project conducted by Chuck Hefren (850/487-9249) and Lyndon Rodgers (850/487-3805)

Gary R. VanLandingham, OPPAGA Interim Director

Appendix A

Estimate of Cost of Office of Public Counsel Involvement in Rate Review Process

Should the Legislature choose to authorize Office of Public Counsel involvement in the medical malpractice rate review process, the office's funding requirements will be dependent on a number of variables including the number of rate filings reviewed, the number of hearings requested, and whether the associated activities are contracted or performed by Office of Public Counsel employees. Based on recent rating filings data and Office of Insurance Regulation activities, we estimated the total cost to be \$375,000 annually. These costs are based on an assumption that the Office of Public Counsel would need one additional full-time employee, be involved in 10 rate filing evaluations a year, and request one DOAH hearing per year, as described below.

- To effectively perform activities associated with medical malpractice rate reviews, the Office of Public Counsel would need one additional senior attorney position. This position would be responsible for reviewing each medical malpractice rate filing to determine whether it meets the threshold for an actuarial evaluation. The position would require expertise in insurance matters and the ability to monitor contracted actuarial services. The cost to fund the salary and benefits of this position is estimated at \$75,000 per year.³⁰
- Based on the medical malpractice insurance rate filings submitted in Fiscal Year 2002-03 and a threshold of a 25% average statewide increase for the Office of Public Counsel to become involved in medical malpractice rate filings, the Office of Public Counsel would need to conduct approximately 10 rate filing evaluations each year. These evaluations would be conducted by a contracted actuary at an estimated cost of \$10,000 per evaluation or \$100,000 per year.³¹ We believe that at a 25% rate increase threshold, it would be more cost-effective for the Office of Public Counsel to use contracted services to perform the initial evaluation of the rate filing and participate in public hearings. However, if a lower threshold is chosen or the actual level of activity exceeds our projections, it may be more cost-effective to enable the Office of Public Counsel to perform these activities internally.
- We were unable to definitively establish the number of rate cases that the Office of Public Counsel may refer to a DOAH hearing. However, based on the experience of the Office of Public Counsel with Florida utility rate cases and reported involvement by other states that authorize intervention on behalf of consumer groups, we believe that public hearings will be requested for a very limited number of cases. Therefore, we estimated that the number of hearings requested by the Office of Public Counsel and conducted by DOAH will be limited to an average of one per year, at a cost of \$200,000.³²

³⁰ The estimated cost of a senior attorney position was based on the average salary for a senior attorney position in the Office of Insurance Regulation plus associated benefits.

³¹ This estimate is based on the reported average time OIR spends on their medical malpractice insurance rate filing evaluations and the hourly rates charged by a typical company providing these actuarial services,

³² This represents estimated costs for a typical DOAH hearing relating to a medical malpractice rate determination case and includes the costs associated with Office of Public Counsel preparation and involvement in the hearings as well as the costs incurred by DOAH to conduct the hearing. Actual costs will vary depending on the complexity of the rate filing and the number of affected policyholders.

JAMES E. "JIM" KING, JR.
President

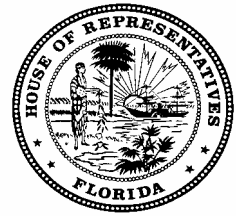


Harold McLean
Public Counsel

STATE OF FLORIDA
OFFICE OF PUBLIC COUNSEL

c/o THE FLORIDA LEGISLATURE
111 WEST MADISON ST
ROOM 812
TALLAHASSEE, FLORIDA 32399-1400
850-488-9330

JOHNNIE BYRD
Speaker



January 21, 2004

Gary VanLandingham, Interim Director
Office of Program Policy Analysis and
Government Accountability
111 West Madison Street, Room 312
Tallahassee, FL 32399-1475

RE: OPPAGA Special Report

Dear Mr. VanLandingham:

Thank you for our copy of OPPAGA's Special Report entitled "Office of Public Counsel Involvement in Medical Malpractice Insurance Rate Setting May Help Limit Rate Increases."

I congratulate you and staff on a thorough report which I think comprehensively deals with this important issue. Of special concern to me was your assessment of the resources my office would need to accomplish the task. It appears to be a reasonable assessment in every respect.

As I'm sure you know, I take no position regarding the wisdom of such a program; that matter is of course the province of the Legislature. I do say, however, that should the Legislature entrust this program to this office, we will earnestly undertake the task.

Thank you for giving us the opportunity to respond to your Special Report. If I can be of any further assistance, please do not hesitate to call upon me at your convenience.

Sincerely,

/s/

Harold McLean
Public Counsel



DEPARTMENT OF FINANCIAL SERVICES
FINANCIAL SERVICES COMMISSION
OFFICE OF INSURANCE REGULATION

KEVIN M. MCCARTY
DIRECTOR

JEB BUSH
GOVERNOR

TOM GALLAGHER
CHIEF FINANCIAL OFFICER

CHARLIE CRIST
ATTORNEY GENERAL

CHARLES BRONSON
COMMISSIONER OF
AGRICULTURE

January 28, 2004

Mr. Gary R. VanLandingham
Interim Director
Office of Program Policy Analysis and
Government Accountability
111 West Madison Street
Room 312
Claude Pepper Building
Tallahassee, Florida 32399-1475

RE: Office of Public Counsel Involvement in Medical Malpractice Insurance Rate
Review May Help Limit Rate Increases

Dear Mr. VanLandingham:

This letter is being forwarded in response to your letter of January 15, 2004, pursuant to Section 11.51(5), Florida Statutes.

The Office of Insurance Regulation (OIR) has reviewed the draft OPPAGA Special Report No. 04-xx of January 2004. Apart from the Discussion Section, the information and comments that are provided in the enclosed OIR response to your draft report are keyed to your draft report insofar as this could reasonably be achieved.

Owing to the great importance that my agency places on medical malpractice insurance with respect to consumers, medical practitioners and insurers within the state of Florida, I appreciate the opportunity to respond to your draft Special Report.

Sincerely,

Kevin M. McCarty

Enclosure

cc: Tom Gallagher, Chief Financial Officer, Department of Financial Services
Elsie Crowell, Insurance Consumer Advocate, Department of Financial Services
Dave Harlan, Inspector General, Department of Financial Services

• • •

INFORMATION AND COMMENTS PREPARED BY THE OFFICE OF INSURANCE
REGULATION (OIR) IN RESPONSE TO OPPAGA'S SPECIAL REPORT, REPORT NO. 04-
XX, JANUARY 2004 – OFFICE OF PUBLIC COUNSEL INVOLVEMENT IN MEDICAL
MALPRACTICE INSURANCE RATE REVIEW MAY HELP LIMIT RATE INCREASES

DISCUSSION

OIR is aware that there have been multiple factors that have contributed to increased medical malpractice insurance rates in recent times. For now, however, we believe that the era of rate increases of 25 percent or more is changing. The hard market for many lines, which is part of the normal insurance cycle, appears to be turning.

The state of Florida is well known for having one of the most thorough medical malpractice rate review processes in the country. Moreover, OIR has one of the most experienced and credentialed actuarial staffs of any regulatory agency in the country. This is mentioned here because of the overriding concern at OIR that rates that are approved by this office are actuarially sound: not excessive, not inadequate and not unfairly discriminatory.

Increased rates that medical malpractice insurers have requested in recent years, after almost a decade of essentially flat rate increases, are a result of losses that the insurers encountered. Artificial suppression of rates or attempts to require rates that are not truly indicative of insurers' loss experiences will only tend to exacerbate the financial challenges such insurers face.

It is the opinion of OIR that involving the Office of Public Counsel (OPC) in the medical malpractice insurance rate filing and review process would add unnecessary effort and costs to this process. Simply stated, the OIR rate filing and review process works well. Accordingly, involvement of the OPC would add costs, would likely delay the rate filing and review process and could ultimately adversely impact the availability of insurers who are writing medical malpractice insurance in Florida.

From a logistics perspective, should the OPC be involved in the rate filing and review process, insurers would be required to submit filings – with from 100 to over 300 pages of documentation – to both OIR and OPC. This would be an unnecessary and duplicative process for the insurer. In this regard, filings are currently made electronically via OIR's I-File System, a system that routes various parts of filings to appropriate analysts or actuaries and supports internal processes of each rate filing. The rate filing efficiency that the I-File System provides to carriers will be lost by having carriers create paper filings.

Six major insurers are currently available to write new medical malpractice insurance in Florida with various others having some market share. This situation clearly belies the assumption that some seem to make that excessive rates are being approved by OIR. Contrary to this assumption, medical malpractice rates approved by OIR are consistent with the statutory framework.

We believe that insurers are now on a sounder financial footing with respect to medical malpractice insurance and that this, coupled with the recently enacted presumed factor requirement, has helped to calm the Florida environment considerably.

To summarize, we believe that adding another bureaucratic layer, with its associated costs, would be functionally duplicative and wasteful of Florida taxpayers' resources.

The remaining information and comments that follow are provided in response to, and keyed to, the draft Special Report, Report No. 04-xx, of January 2004, that was forwarded as an enclosure to OPPAGA's letter of January 15, 2004.

AT A GLANCE

We believe that requiring medical malpractice insurers to deal with yet another government entity, specifically OPC, during the rate filing and review process will inject delays and increase costs to the state of Florida, insurers, healthcare providers and Florida residents. We do not believe that the draft Special Report contains specific evidence that demonstrates unequivocally that involving OPC in the malpractice insurance rate filing and review process will help to limit premium increases.

The validity of comparing the results of an OPCs' intervention activities in other states with regard to lowering utility rates to the future possibility of an OPC's intervention activities in Florida resulting in the lowering of insurance rates is questionable. With regard to utilities, factors such as availability and cost of fuels, acquisition, maintaining and replacing plant and equipment, providing stockholders with acceptable rates of return on their investments and perhaps other factors play into the overall rate setting process. The medical malpractice insurance rate filing and review process, on the other hand, involves in-depth actuarial evaluations that address such things as loss development factors, loss trend factors and reinsurance in order to ensure, among other things, that key principles set forth in the Actuarial Standard of Practice (ASOP) No. 9 -- "Documentation And Disclosure In Property And Casualty Insurance Ratemaking, Loss Reserving And Valuations" -- are not violated.

It may be useful to note that the rate review process employed by OIR produces loss estimates that are actuarially sound. Rates that are derived from such loss estimates must, in turn, comply with four criteria that are used by both actuaries and OIR. Namely, such rates must: be reasonable; not be excessive; not be inadequate; and not be unfairly discriminatory.

OIR places strong emphasis on compliance with the principles that are set forth in ASOP No. 9 during the rate filing and review process, including the process that is applicable to medical malpractice rate filings and reviews.

SCOPE

With regard to the Insurance Consumer Advocate, it should be noted that OIR has a long established, excellent working relationship with that office. Moreover, the Insurance Consumer Advocate is well aware that representatives from that office could, and would, intervene on behalf of consumers should OIR approved rates proposed by insurers that are excessive, inadequate or unfairly discriminatory. OIR is well known to only approve rates that are actuarially sound; therefore, the Insurance Consumer Advocate has not found direct intervention in the OIR rate filing and review process to be necessary. Nonetheless, we believe that the value of the Insurance Consumer Advocate with respect to safeguarding the interests of consumers is unquestionable.

BACKGROUND

As most are aware, ratemaking is prospective simply because rates must be developed prior to the actual transfer of risk. Relevant principles that are provided in ASOP No. 9 that are considered to be relevant in this regard are provided below for information and reference.

Principle 1: A rate is an estimate of the expected value of future costs. Ratemaking should provide for all costs so that the insurance system is financially sound.

Principle 2: A rate provides for all costs associated with the transfer of risk.

Principle 3: A rate provides for the costs associated with an individual risk transfer.

Principle 4: A rate is reasonable and not excessive, inadequate, or unfairly discriminatory if it is an actuarially sound estimate of the expected value of all future costs associated with and individual risk transfer.

With regard to pages 1 and 2 of the draft OPPAGA Special Report, second paragraph – “Beginning in the 1990s, malpractice premiums began to increase at a rapid rate...” we would suggest that this paragraph be replaced by the following from “The Florida Senate,” -- Interim Project Report 2004-163, January 2004:

“Medicare malpractice insurance premiums began rising in 2000, after almost a decade of essentially flat prices. Rate increases for physicians and surgeons from the top 15 professional liability insurers (ranked by direct written premium in Florida as reported December 31, 2001) ranged from 25 percent to 125 percent for the 2 and ½ year period from January 1, 2001, through July 1, 2003. On average there was an 81 percent rate increase, weighted for market share, during this period.”

INSURANCE RATE REVIEW PROCESS

OIR does not regulate medical malpractice insurance to insure that rates used to calculate premiums reflect the lowest possible prices, while making certain that insurers will be able to pay for any future claims covered by the insured. OIR’s goal is to perform rate filing and review processes that produce rates that are actuarially sound and are not excessive, not inadequate and not unfairly discriminatory.

It should be noted that it is in the interest of the insurance system, health care providers and consumers to have multiple insurers writing medical malpractice insurance in the state of Florida. This is necessary in order to assure that: medical malpractice insurers are available to Florida health care providers; competition among medical malpractice insurers is preserved; and that rate changes that are proposed by medical malpractice insurers are tempered not only by sound actuarial principles, but also by sound competition in the marketplace.

Footnote 9 on page 2 of the draft Special Report discusses Legislation in 1989 to expand the authority of the OPC to include representing the public in certain rate cases. This legislation was subsequently vetoed by the Governor. Similar legislation was passed in 1983, but was repealed in a Reviser’s note on its own terms on October 1984. It is interesting to note that Bill Analysis (HF-4-F) of June 3, 1982 indicated that in order to intervene at selected rate hearings the public counsel would need the following staff:

- An Attorney IV;
- A Legislative Chief Analyst (Property and Casualty Actuary);
- A Legislative Analyst III or IV (Economist – MA or Ph. D); and
- A Secretary.

Moreover, if a second team were to be funded, the second team would consist of:

- An Attorney III;
- A Legislative Chief Analyst (Actuary); and
- A Secretary.

This is being noted here to indicate and emphasize that the rate filing and review functions that would be performed by the OPC would potentially be both labor and resource intensive. Moreover, they would be duplicative of functions that are already being performed very well by a highly trained and credentialed OIR staff.

OIR and insurers of all types exercise very effective and iterative two-way communications during the rate filing and review process, using both correspondence and questions and answers, as required. This permits OIR to add value to the overall rate filing and review process and to ensure that this process employs much more than a “check the box” approach with regard to this very important activity. We would suggest that Exhibit I of the draft Special Report should be annotated to reflect the added value that OIR brings to the rate filing and review process by maintaining effective information exchanges with insurers.

FINDINGS

Office of Insurance Consumer Advocate has not been involved in medical malpractice rate review process

Obviously the Office of Insurance Consumer Advocate must speak for itself with regard to this finding. On the other hand, OIR agrees with that office's assertion that OIR's insurance rate determination processes have been effective in ensuring that insurance rates are not excessive, not inadequate and not unfairly discriminatory.

OIR is not aware that placement of the Office of Insurance Consumer Advocate has served to impair the independence of that office in any way.

Involvement of the Office of Public Counsel in medical malpractice rate review process may help stabilize rates

OIR does not believe that involving the OPC in malpractice the rate filing and review process is necessary, would add value to the process or would be cost effective. Please refer to our comments in the Discussion Section above.

Entities in other states report that consumer representation in rate review process has stabilized rate changes

With regard to Texas involving its Office of Public Insurance Counsel (OPIC) in its rate filing and review process, it is important to observe that the Texas example is specific to **personal lines** of insurance only. With regard to **commercial lines** of insurance, which include medical malpractice insurance, consumers have knowledge (AMA publications, medical association publications, training) and resources (hospital risk managers, attorneys, etc.) to make correct decisions when they are purchasing insurance.

The \$535,000,000 savings that are attributed to the Texas OPIC are questionable. As noted in footnote 14, this savings reflects the differences between the requested increases in insurance premiums and the amount approved for rate filings where the OPIC intervened. Insurers in Florida often file for rates that are lower than their overall indications. Perhaps insurers in Texas file for a higher rate indication than they would have in the past in anticipation of OPIC challenges. If this were so, then filing for higher rate indications would amount to nothing more than insurers inflating their requests.

California has operated under Proposition 103, which permits the public to challenge rates if it does so within 45 days of public notice of such rates. Based on a discussion with a representative of the California Department of Insurance, rates have been challenged from time to time since Proposition 103 became effective in 1989. However, only one hearing has taken place since Proposition 103 became effective and that took place over a period of nine months, beginning in late 2002 and ending in mid 2003. According to the Department of Insurance representative, the hearing was not only lengthy, but it was also disruptive and labor and cost intensive for all concerned.

Limitations on litigation and damages are often cited as reasons for California's rate stability.

The Office of Public Counsel's involvement in utility rate determination cases has been effective in reducing costs for consumers

While the involvement of OPC in utility rate reductions appears to have been successful, we do not believe that involvement of the OPC in the medical malpractice insurance rate filing and review process would be equally successful due to the differences in the business types as discussed earlier.

With sufficient authority, the Office of Public Counsel could represent the public in the medical malpractice insurance determination process

OIR's rate filing and review process is effective and serves the interests of the public by producing rates that are not excessive, not inadequate and not unfairly discriminatory. OIR's has the responsibility and authority to only approve rates that are actuarially sound and that are in conformance with ASOP No. 9. Should the OPC be permitted to intervene in rate filing and review cases, it would have to duplicate, at considerable cost to Florida and its taxpayers, the analyses and actuarial processes that are currently being performed effectively and well by OIR.

Establishing parameters could limit cost of Office of Public Counsel involvement in medical malpractice rate review processes

OIR agrees that funding would be required should OPC be permitted to become involved in medical malpractice rate setting. Simply stated, the OPC would have to create and deploy precisely the same rate filing and review capabilities as those that are already in place within OIR.

As indicated above, OIR believes that the insurer requests for large medical malpractice insurance rate increases – 25 percent or more – are not likely to occur for the foreseeable future. Accordingly, it does not appear that funding in the amount of \$375,000 to create capabilities within the OPC that already exist within OIR could easily be justified.

With regard to purported savings that are attributed to involvement of Offices of Public Counsel in insurance rate setting in other states, Texas' OPIC does not intervene in medical malpractice insurance rate setting activities. Savings in California appear to likely be attributed to a stricter insurance regulatory environment that now prevails in that state rather than being attributed to OPC intervention in insurance rate setting processes. In view of the foregoing, the argument that increased funding for the OPC should be more than offset by savings to healthcare practitioners from lower malpractice premiums is not a compelling one.

Alternatives exist for funding Office of Public Counsel involvement in medical malpractice rate review process

Assessing an annual fee for each medical malpractice insurance policy, or increasing the insurance premium tax on medical malpractice insurers, is decidedly undesirable at this time. Funding, using such a taxing vehicle would not be well received among a struggling group of malpractice insurers and could further exacerbate the problem of ensuring that an adequate number of insurers continue to write malpractice insurance in Florida. OIR believes that any additional costs being placed on medical malpractice insurers at this time, however small, could have an immediate deleterious affect on the availability of medical malpractice insurance in Florida.

CONCLUSIONS AND RECOMMENDATIONS

OIR does not concur with the conclusions or recommendations that are set forth in the OPPAGA draft Special Report. OIR believes that adding OPC to the medical malpractice insurance rate filing and review process would be unnecessary, costly and largely a waste of scarce resources in a period of fiscal austerity within the state of Florida.

Appendix A – Estimate of Cost of Office of Public Counsel Involvement in Rate Review Process

OIR is unable to fully evaluate the estimates of cost that are provided in Appendix A of OPPAGA's.

It might be useful to note that the OPC would be confronted with rather steep and lengthy learning curves that it would have to overcome before it could participate effectively in a rate filing and review process. This would involve, but perhaps would not be limited to, learning such things as: the insurance market; the healthcare provider community; the application of actuarial principles and techniques to medical malpractice insurance; rate filing documentation, analysis and rate review; and use of procedures and mechanisms that are currently deployed by OIR to assist insurers in submitting documentation and participating in the rate filing and review process with OIR. Should OIR be required to assist in training the OPC staff, this would represent yet additional OPC start up costs.

We hope that the information and comments provided above are found to be useful.
Please feel free to contact us, if additional information or clarification on any of the issues discussed above is required.