LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 85TH LEGISLATIVE REGULAR SESSION

April 3, 2017

TO: Honorable Larry Phillips, Chair, House Committee on Insurance

FROM: Ursula Parks, Director, Legislative Budget Board

IN RE: **HB1940** by Turner (Relating to the use by the comptroller of public accounts of certain forms in connection with administration and enforcement of certain insurance premium tax laws.), **As Introduced**

Estimated Two-year Net Impact to General Revenue Related Funds for HB1940, As Introduced: a negative impact of ($32,500,000) through the biennium ending August 31, 2019.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2018	($288,000)
2019	($32,212,000)
2020	($17,345,000)
2021	($18,195,000)
2022	($19,105,000)

All Funds, Five-Year Impact:

Fiscal Year	Probable (Cost) from *General Revenue Fund* 1	Probable Revenue (Loss) from *General Revenue Fund* 1	Probable Revenue (Loss) from *Foundation School Fund* 193
2018	($288,000)	$0	$0
2019	$0	($24,159,000)	($8,053,000)
2020	$0	($13,009,000)	($4,336,000)
2021	$0	($13,646,000)	($4,549,000)
2022	$0	($14,329,000)	($4,776,000)

Fiscal Analysis

The bill would amend Chapter 201 of the Insurance Code, regarding collection of revenue and administration of funds. The bill would require the Comptroller to allocate premium or revenue with respect to premium tax based solely on the premium allocated by state as reported on the applicable form prescribed by the National Association of Insurance Commissioners (NAIC).

The bill would take effect January 1, 2018.

Methodology

Under current law, insurance premium tax is allocated by state based on the location of the insured risk. The Comptroller's Audit Division frequently finds that insurance companies incorrectly allocate premium on their tax reports by using the information by state on the forms prescribed by the National Association of Insurance Commissioners. The Comptroller then makes adjustments, both assessments and refunds, of premium tax on those companies. During fiscal years 2011-16 adjustments based on incorrect premium allocation averaged $12,620,000 per year. The bill would eliminate or dramatically reduce the effectiveness of insurance company audits for the various insurance tax types. The bill would require insurers and health maintenance organizations to report premiums based on the NAIC reports rather than the risk-based reporting required in the Insurance Code under Sec. 221.002(b), Sec. 222.002(b) and Sec. 223.003(b).

This analysis assumes that under current law the Comptroller's Audit Division would assess $12,620,000 in tax year 2018 and that the amounts assessed thereafter would increase at the growth rate of Texas nominal gross state product. Under the provisions of the bill audit assessments would not be affected in fiscal 2018, but would be zero thereafter.

Captive insurance companies, Mexican casualty insurance companies, and farm mutual insurance companies are not required to report premium to the NAIC. Total premium tax paid by those types of insurers in fiscal 2017 was $2,345,000. It is assumed that under current law premium tax collections from those insurers would increase at the growth rate of Texas nominal gross state product. Under the provisions of the bill, premium tax collections from those types of insurers would not be affected in fiscal 2018, but would be zero thereafter. In addition, these insurers would be eligible for a refund of tax year 2018 prepayments in fiscal year 2019.

Premium tax for tax year 2018 will begin to be collected in fiscal 2018 through two semi-annual prepayments. These prepayments would be based on the prior year's tax return so there would be no revenue effect in fiscal 2018. However, in fiscal 2019 there would be a refund of a portion of those prepayments based on the changes made in the bill, so the revenue loss in fiscal 2019 includes a loss from tax year 2018.

Insurance maintenance taxes are allocated to GR Account 0036 - Texas Department of Insurance Operating to fund the operations of the Texas Department of Insurance. As this is a self-leveling account, any decrease in maintenance taxes paid by one group of insurers would result in an equivalent increase in maintenance tax paid by other insurers. Under the provisions of the bill, captive insurance companies, Mexican casualty insurance companies, and farm mutual insurance companies would no longer be required to pay maintenance taxes. The maintenance tax rate for life, accident and health insurers is at the maximum rate permitted by statute. Therefore, the amount and share of maintenance taxes paid by property and casualty insurers would increase. The bill would not, however, have any effect on total maintenance tax revenue collected.

The bill would require the Comptroller to accept the amounts reported on the NAIC reports as filed by insurers and health maintenance organizations. The NAIC, the Texas Department of Insurance, and other states' insurance departments do not audit the numbers on the NAIC reports that would be used for tax allocation. Although Texas insurance premium tax rates are below those of most other states, there are several states that have significantly lower rates than Texas. Under the provisions of the bill, insurers would have an incentive to allocate premium for risks located in Texas to states with lower premium tax rates. Foreign (domiciled in a state other than Texas) insurance companies paid a combined $1.05 billion in insurance premium taxes in fiscal

2017. If foreign insurers reallocated five percent of premium to other states, premium tax collections would be reduced by an additional $53 million per year. Domestic Texas insurers with business in other states could also reallocate premium in this way.

Technology

There would be a one-time technology cost of $228,000 in fiscal 2018 for an estimated 1920 hours of application revisions and programming for both web and paper reporting. The agency estimates the bill would require a full rewrite of data entry, edit and processing and all related programs, including web filing and online transaction corrections. Major changes would also need to be made to output reports currently used to assist the Enforcement and Audit Divisions as well as changes to the comprehensive audit transaction system.

Local Government Impact

No fiscal implication to units of local government is anticipated.

Source Agencies: 304 Comptroller of Public Accounts, 454 Department of Insurance

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