

STATE OF ALASKA

TONY KNOWLES,
GOVERNOR

DEPARTMENT OF LAW
OFFICE OF THE ATTORNEY GENERAL

P.O. BOX 110300
JUNEAU, ALASKA 99811-0300
PHONE: (907)465-3600
FAX: (907)465-2075

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The Honorable Tony Knowles
Governor
State of Alaska
P.O. Box 110001
Juneau, Alaska 99811-0001

Re: SCS CSHB 184(JUD) -- relating to
insurance
Our file: 883-01-0095

Dear Governor Knowles:

At the request of your legislative director, we have reviewed SCS CSHB 184(JUD), a bill relating to insurance that amends the insurance code (AS 21). For the sake of brevity, SCS CSHB 184(JUD) will be referred to hereafter as "the bill."

The bill is lengthy at 54 pages and contains 92 sections. As reflected in sec. 1 of the bill, the primary purpose of the bill is to implement insurance reforms in AS 21 as required by federal law, P.L. 106-102, which is known as the Gramm-Leach-Bliley Act (GLBA). The reforms under this bill are aimed at conforming with the GLBA, modernizing financial services related to the business of insurance, and furthering this state as an attractive place for investment and other commerce involving the insurance industry. Other key parts of the bill update provisions of the insurance code that regulate insurance company investments and that regulate rate and form filing requirements for commercial insurance risks. The bill also adds a couple of new provisions that are aimed at protecting consumers from persons who have criminal convictions. One provision gives the

division of insurance (division) the authority to obtain national criminal background checks on persons applying for an insurance license. The other provision confirms a requirement under federal law for obtaining consent from Alaska's director for the division to engage in the business of insurance with respect to persons convicted of a felony involving dishonesty or breach of trust.

1. GLBA Reforms

Sections 10-74, 80-83, 85, 86, 88-90, and 92 of the bill all relate to implementing reforms in the insurance code (AS 21) that are necessitated by the GLBA.

The GLBA became law on November 12, 1999. It repealed Depression-era restrictions on the insurance, banking, and securities industries, and, more notably, removed some of the barriers that limited banks from engaging in the business of insurance. The GLBA applies to all financial institutions, including insurance companies. Under the GLBA, specific standards are established with respect to consumer privacy, consumer protection, insurance producer licensing, and insurance sales. State authority to regulate insurance is affirmed by this new federal law, but federal law may preempt that authority if the states fail to regulate insurance in a manner that is at least consistent with the GLBA or if the states regulate in a manner that prevents or significantly interferes with the ability of a bank or bank affiliate to engage in insurance sales activity.

The GLBA reforms under the bill focus on three principal areas: 1) establishing reciprocity for licensing nonresident insurance producers; 2) implementing the GLBA consumer privacy standards related to when financial institutions may share personal information with affiliates and nonaffiliates; and 3) implementing the GLBA consumer protection safe harbors related to the sale of insurance by financial institutions. The majority of the reforms are based on models adopted by the National Association of Insurance Commissioners (NAIC).

a. Reciprocity

By far the largest part of this bill is devoted to amending the insurance code to provide for reciprocity in the licensing of nonresident insurance producers pursuant to the GLBA. The GLBA seeks multi-state licensing reform and directs a majority of states (a minimum of 29 jurisdictions) to achieve either uniformity or reciprocity in licensing by November 2002. If this reform is not achieved, the states will lose the authority to license nonresident insurance producers and a national organization must be established under the GLBA to assume that role. The NAIC adopted the Producer License Model Act for states to use as a guideline in developing legislation to achieve reciprocity. For GLBA purposes, reciprocity means that a nonresident insurance producer will receive a license to transact insurance in this state to the same extent that the producer is licensed

in the producer's home state. Reciprocity also allows resident insurance producers to obtain licensing in other states without meeting state-specific requirements.

Sections 10 – 65 of the bill amend the licensing chapter of the insurance code (AS 21.27) to establish a framework for reciprocity. One of the principal reciprocity provisions is in sec. 30, which repeals and reenacts AS 21.27.270 relating to the licensing of nonresident producers. Under this rewrite of AS 21.27.270, the director is required to issue a license to a nonresident applicant on terms reciprocal with those in the applicant's home state, subject to a few enumerated conditions. The nonresident applicant must be currently licensed and in good standing in the applicant's home state, must pay license fees to Alaska, and must submit to the director the license application submitted to the applicant's home state or a completed uniform application. The director also is given the authority to waive by order any license application requirement in AS 21.27 to achieve reciprocity. The director retains the authority to deny or refuse to renew a nonresident license under AS 21.27.410 and, in any event, is not required to issue a license to a nonresident applicant if the applicant's home state does not award nonresident licenses to residents of Alaska on the same basis as does this state.

Under sec. 30 of the bill, the director also is given the discretion to require an applicant to furnish fingerprints as required under AS 21.27.040(e), to maintain a bond under AS 21.27.790 if the applicant is applying for a surplus lines broker license, and to comply with the fiduciary account requirements of AS 21.27.360, all of which are mandated under existing law. Unchanged from existing law is the requirement that a nonresident licensee appoint the director as attorney to receive service of legal process issued against the licensee in this state.

Two other provisions key to reciprocity are in secs. 24 and 29 of the bill. Section 24 adds a new subsection to AS 21.27 related to lines of authority for which an insurance license may be issued. This subsection is based on the NAIC producer model law and it helps establish a framework for achieving reciprocity in licensing among the states. Specifically, the new section AS 21.27.115 defines the major lines of authority for which a license will be issued to include: life, health, property, casualty, variable life and annuity, personal lines, limited lines credit insurance, and other insurance for which a limited lines license may be issued.

Section 29 amends AS 21.27.150, which establishes the types of limited lines licenses that may be issued under the insurance code. "Limited lines" is defined under the bill to mean those lines of insurance specifically referenced in AS 21.27.150 and any other line of insurance that the director designates by order as a limited line. Under the amendments in sec. 29, most of the existing types of limited lines licenses are retained, except for the health insurance limited producer license and the retired producer license, which are eliminated under this bill. New types of limited lines license are established

for persons selling limited lines credit insurance and for nonresident producers holding limited lines licenses in their home state. A miscellaneous category also is established for persons that transact insurance in this state with authority that is less than the total authority for a line of authority described in AS 21.27.115.

Sections 10 – 65 of the bill also encompass many other changes to the licensing chapter to fully implement reciprocity and to allow reciprocal treatment of resident insurance producers in other states. These changes include the following types of amendments for consistency with the NAIC producer model law and certain licensing requirements in other states:

(1) Clarification of the scope of exemptions from licensing under AS 21.27.010(e) primarily related to certain insurance company personnel to be consistent with the NAIC producer model law. (Secs. 10 and 11).

(2) Lowering of the minimum age to hold an insurance license to 18 and removal of the requirement for having a high school diploma or GED. (Sec. 12).

(3) With respect to firm licensing, replacement of all references to principal or manager of a firm with reference to the compliance officer designated by the firm, who must be a licensed person. (Secs. 13, 19, 27, 28, 33, 42 – 44, 50, 53, 56, and 62 – 64).

(4) Removal of the requirement for a nonresident to meet Alaska's continuing education requirement. (Sec. 14).

(5) Clarification of the required notice by a licensee to the director regarding actions taken against a licensee (including termination of employment). (Secs. 15 and 16).

(6) Removal of the requirement for notarized signatures on license applications but including a statutory requirement to submit fingerprint cards for a national criminal background check. (Secs. 17 and 18).

(7) Removal of prelicensing examination requirements for certain persons including a person applying for a license in this state who was previously licensed for the same lines of authority in the person's prior home state; certain stated conditions that are uniform with other states. (Secs. 20 and 21).

(8) Removal of the requirement to file separate appointment forms with the division of insurance when multiple insurers within an insurer's holding company appoint the same licensed person to act as their agent. (Sec 22).

(9) Clarification of the notice and disclosure requirements related to the termination of a company appointment. (Sec. 23).

(10) Removal of the requirement of separate licenses for each branch location of a firm. (Sec. 32).

(11) Removal of express references to fiduciary accounts to be maintained by licensees, but retention of the requirement that licensees hold premium monies as fiduciaries and retention of the prohibitions on commingling such monies with other funds or assets of the licensee. (Secs. 34 –39, 45, 46, 48, 49, 51, 54, 57, and 59).

(12) Clarification that an unlicensed person may receive compensation for referring a customer or potential customer to a licensee as long as the person does not discuss specific terms and conditions of a policy or give opinions or advice regarding insurance and the compensation for each referral is nominal, on a one-time basis, and does not depend on whether insurance is purchased or on the volume of insurance transacted. (Sec. 40).

(13) Removal of mandatory bond requirements for insurance producers and surplus lines brokers, but the director is given discretion to adopt regulations to require a bond in an amount acceptable to the director. (Sec. 61).

(14) Addition of new definitions to implement the changes related to reciprocity including a new definition of “transact” for purposes of licensing under AS 21.27 and new definitions for “sell,” “solicit,” and “negotiate.” (Secs. 65 and 66).

In addition, sec. 80 of the bill rewrites AS 21.89.080 to remove any barriers to allowing electronic submissions of information or written submissions required under the insurance code. Allowing electronic submissions will help to achieve reciprocity and will speed up licensing and provide better customer service.

b. Consumer Privacy

Consumer privacy is a key component of the GLBA reforms. The GLBA requires financial institutions including insurers to establish and disclose privacy policies to their customers and requires these institutions to give their customers the ability to “opt out” of any policy to share a customer’s personal financial information with third parties not affiliated with the financial institution. “Opt out” means only that the institution will advise the customer that information may be shared with nonaffiliated third parties unless the customer expressly prohibits such sharing. The GLBA, however, allows these institutions to share customer information with affiliated entities without restriction. The GLBA directs the states to adopt and enforce minimum privacy standards related to

personal information of consumers, but provides that state standards more protective of consumer privacy than the federal standards will be upheld. Adopting privacy standards in Alaska is important because under GLBA failure to do so could result in Alaska losing the ability to enforce state consumer protection standards with respect to financial institution insurance sales. Moreover, without this bill there are no express privacy protections in Alaska for financial and health information that consumers provide to insurance companies.

Under sec. 67 of the bill, a new section is added to the trade practices chapter of the insurance code (AS 21.36), relating to the privacy of personal financial and health information of consumers. While this new section is small, it generated the most debate in the legislature. There was much discussion on whether to implement an “opt in” or “opt out” standard for privacy. An “opt in” standard is more restrictive than “opt out” in that it prohibits sharing of personal information without the permission of the consumer in advance. Virtually all of the debate in the legislature supported an “opt in” standard for health information. Rather than implementing a particular standard in statute, the legislature delegated authority to the director to adopt regulations regarding the release of personal financial and health information. Any regulations, however, must be at least as restrictive (i.e., protective of consumer privacy) as the model law adopted by the National Conference of Insurance Legislators (NCOIL). This model law follows a standard of “opt out” for sharing of personal financial information and “opt in” for sharing personal health information. NCOIL’s approach is similar to the approach taken by the NAIC in its model regulation on release of personal financial and health information.

c. Consumer Protections – GLBA Safe Harbors

The last key piece of the GLBA reforms relates to consumer protection. Sections 67 – 70 of the bill implement these reforms through amendments to the trade practices chapter of the insurance code (AS 21.36). Under the GLBA, 13 “safe harbors” were established that preserve the states’ authority to regulate insurance transactions by financial institutions. These “safe harbors” relate to the sale, solicitation, and marketing of insurance products by banks and other financial institutions. Sections 67 – 70 of the bill expand the consumer protections in existing law related to the sale of insurance in connection with a loan transaction. The bill also adds new sections to AS 21.36 that clarify the licensing requirement for persons transacting insurance for a financial institution, establish new standards for disclosures in financial institution sale of insurance, and prohibit practices that tend to mislead or deceive consumers regarding the insurance purchased through a financial institution. With respect to these reforms, new definitions are added for consistency with terminology used under the GLBA.

2. Other Amendments Unrelated to the GLBA

The bill also amends the insurance code with respect to commercial insurance rate and form filing, insurance company investments, and persons who are convicted of a felony involving dishonesty or breach of trust. A description of these changes follows.

a. Commercial Rate and Form Filing

Sections 2 and 75 – 78 were added to the bill late in the session to provide for exceptions to the prior approval requirement for form and rate filings related to commercial insurance. Current law requires prior approval for all forms and rates used in this state. Under the bill, “commercial insurance” is defined to include insurance that is for business and professional interests, but does not include workers’ compensation insurance for purposes of rate and form filing requirements under the insurance code. The changes under the bill are ultimately directed at large commercial insurance purchasers that do not need the protection of prior approval, because they have the ability to evaluate the coverage and price of an insurance product on an equal basis with an insurer. Under current law, the director already has authority to exempt, certain rate or form filings from prior approval, by order. The changes under the bill, however, require the director to adopt regulations by July 1, 2002, that are consistent with a NAIC model law regarding form and rate filings. The model law contains high thresholds for qualifying for reduced rate and form filing review to ensure that only transactions by knowledgeable purchasers will be affected.

b. Insurance Company Investments

Sections 3 – 9, 79, and the repealers in sec. 84 of the bill represent a complete reform of the law regulating insurance company investments to reflect changes in investment types and to establish a framework for new investment limitations that are consistent with limitations in other states. The current investment law was originally enacted in 1966 and has been modified on only a few occasions since then. The law is now out of date. Central to the bill’s reforms is the requirement that the director adopt regulations that are consistent with the defined limit standards for insurance company investments as adopted by the NAIC. To that end, the above sections of the bill amend and repeal the outdated statutory provisions to ensure consistency with the defined limit standards.

c. Compliance with 18 U.S.C. 1033 and 1034

In 1994, the Violent Crime Control and Law Enforcement Act became law; it requires persons who have a felony conviction involving dishonesty or breach of trust to have the express written consent of a state’s insurance regulator before working in the business of insurance. In sec. 71 of the bill, a new provision is added to the insurance

code that effectively codifies this federal requirement in state law. This new provision prohibits persons with felony convictions involving dishonesty or breach of trust from engaging or participating in the business of insurance without the prior written consent of Alaska's director of insurance. The provision also prohibits any person engaged in the business of insurance from knowingly permitting the participation in the business of insurance by a person who does not have the required consent.

3. Effective Dates

Sections 88 - 92 of the bill establish various effective dates for key reforms under this bill. In particular, the GLBA reforms related to privacy and consumer protection will become effective July 1, 2001. January 1, 2002, is the effective date for the majority of the GLBA reforms related to licensing reciprocity, which conforms to the timeline established under the GLBA for reciprocity. There are some reciprocity provisions related to the handling of premiums and other monies held by a licensee as a fiduciary that do not become effective until July 1, 2002, to allow time to amend division regulations, if necessary. There are also a few reciprocity provisions related to license applications and electronic submissions that will take effect immediately when the bill is signed to allow for immediate implementation of uniform applications and electronic submissions. The sections of the bill related to insurance company investments will take effect 30 days after the lieutenant governor certifies to the revisor of statutes the effective date of regulations initially adopted by the director of insurance under sec. 8 of the bill.

In closing, SCS CSHB 184(JUD) is consistent with the state's authority to regulate insurance under the McCarran-Ferguson Act, 12 U.S.C. 1011 - 1015, and as preserved under the GLBA. Based on our review, the bill does not present any legal or constitutional problems to prevent this bill from becoming law.

Sincerely,

Bruce M. Botelho
Attorney General

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