

**Comments of the Center for Insurance Research and
the Center for Economic Justice to the
NAIC Pet Insurance Working Group**

July 20, 2021

We start with the simple proposition that consumer protection should be the guiding principle in the development of any model law, including a pet insurance model law. The development of a model law should not be a mechanism for an industry concerned by diverse regulatory interactions to memorialize and legitimize troublesome, current industry practices.

Our comments focus on the use of a waiting period, wellness programs and free look periods.

Waiting Period

We oppose any provision in the model permitting a waiting period for coverage and urge the working group to include a specific prohibition against waiting periods.

NAPHIA and industry have offered three reasons for including a waiting period – avoiding adverse selection, reducing the costs of coverage, and providing more options and choice for consumers. None of these arguments holds up under scrutiny and, when examined, make the case for a prohibition on waiting periods.

First, the tools to address adverse selection are sound underwriting and pre-existing condition exclusions. A waiting period is not the tool to address adverse selection.

Consider when and how waiting periods are used in other lines of insurance. The most common examples are found with disability income or credit disability insurance. The purpose of waiting periods is to ensure the injury is, in fact, a disability as opposed to, say, an injury covered by health insurance.

A few examples illustrate how the use of a waiting period simply reduces legitimate and expected coverage instead of addressing adverse selection.¹ Consider a pet insurance policy with an effective date of January 1. The pet is injured in an accident on January 10. With NAPHIA's proposed waiting periods, no coverage is provided simply because the injury took place on January 10 instead of January 20. In this situation, the insured has no knowledge of "a higher than average probability of loss" and there is no Adverse Selection, per the NAIC's glossary of terms for consumers.

¹ The NAIC Consumer Glossary (https://content.naic.org/consumer_glossary) provides a definition for adverse selection "**Adverse Selection** - the social phenomenon whereby persons with a higher than average probability of loss seek greater insurance coverage than those with less risk."

Similarly, consider coverage effective January 1 for a healthy pet. The pet becomes ill on January 25. With NAPHIA's proposed waiting periods, no coverage is provided because the illness occurred on January 25 instead of January 31. Again, this would not meet the NAIC's definition of "Adverse Selection."

Now consider coverage effective January 1 for a healthy pet. On January 10, the pet is hit by a car and suffers "musculoskeletal" injury. In this instance, the so-called insurance does not cover any costs associated with treating the pet for injuries from the accident – including cuts – and won't cover any "musculoskeletal" damage for 120 days. Just as with the prior examples, this would not prevent "Adverse Selection" as there is prior knowledge of a "higher than average probability of loss" that a waiting period would cure.

In all of these instances, the waiting period has nothing to do with avoiding adverse selection and is inconsistent with a consumer's expectation of coverage when they purchase the policy.

NAPHIA's and industry's second argument is that waiting periods reduce claim costs and permit pet insurers to offer lower-cost coverage. This is more of a tautology than a rationale. Presumably any reduction in coverage or benefits should lead to a reduction in the price of the insurance. But the logical extension of this industry argument is that by hollowing out the policy to provide negligible benefits, the policy becomes more affordable for consumers. The model law must ensure the basic consumer protection that a pet insurance policy provides meaningful benefits to consumers in relation to the premium charged and that coverage meets consumer expectations – a goal achieved by prohibiting waiting periods, ensuring minimum benefits and ensuring reasonable loss ratios.

NAPHIA's third argument is that various combinations of waiting periods and pre-existing condition exclusions provides consumers with more options and greater choice. In fact, NAPHIA explained that they prefer no limitation on the use of waiting periods and believe any regulatory or consumer concerns can be addressed with disclosures.

There is a large and growing body of research about the limits of disclosure due to, among other things, too many options, too much complexity and lengthy texts, and consumer biases. Disclosures cannot transform a complex product into a simple product. Consumers will not spend the same amount of time studying a pet insurance policy prior to purchase as they would in planning a trip or even buying a television.

Further, the discussion at the last working meeting about the definition of "musculoskeletal" makes clear that any provision regarding musculoskeletal waiting periods would be incomprehensible to consumers. But, even simpler concepts, like injury and illness are open to wide variance in interpretation and understanding. The combination of pre-existing condition exclusions and waiting periods is particularly complex, confusing and inherently misleading to consumers.

We urge the working group to adopt a prohibition on waiting periods for coverage in the model. Industry has failed to provide logical or empirical support for what benefits waiting periods would provide given that pre-existing condition exclusions are already permitted. More important, the inclusion of waiting periods will make a complex product even more complex and inevitably lead to consumer confusion, unmet expectations and regulatory intervention.

Free-Look Period

We support the working group's decision to include a free-look period in the model. We won't rehash the arguments for such a free-look period, but wish to suggest that the language regarding the free-look period in the NAIC travel insurance model be used in the pet insurance model for several reasons.

First, the nature of travel insurance and travel insurance sales methods are very similar to those of pet insurance – a bundling of coverages typically sold by retailers or through web sites.

Second, travel protection plans include insurance coverage and non-insurance products – similar to the offer of pet insurance and non-insurance wellness services from pet insurers and related providers.

Third, the free-look period provisions in the travel model were thoroughly vetted and recognize the different methods of product distribution.

Fourth, it makes sense for consistency for consumer protection features among NAIC models unless there is some unique feature of a product to justify differences. No such rationale is present between travel and pet insurance.

We have edited the relevant portion of the travel insurance model to provide a brief free-look period provision for the working group's consideration:

Unless the insured has filed a claim under the Pet Insurance policy, the insured may cancel the policy for a full refund of the premium from the date of purchase of the Pet Insurance policy until either:

- (a) At least fifteen (15) days following the date of delivery of the Pet Insurance policy by postal mail; or
- (b) At least ten (10) days following the date of delivery of the Pet Insurance policy by means other than postal mail.

For the purposes of this section, delivery means handing the Pet Insurance policy to the policyholder or certificate holder or sending the Pet Insurance policy by postal mail or electronic means to the policyholder or certificate holder.

Wellness Programs

NAPHIA has offered a proposal that permits pet insurers and pet service providers to define what is or is not insurance and what is or is not a non-insurance wellness program:

NAPHIA believes pet wellness and health maintenance products should be treated as pet insurance when they are sold as part of a pet insurance contract, either embedded into the base policy or offered as an endorsement/rider, by a licensed pet insurance entity. NAPHIA also believes that pet wellness and health maintenance products should not be treated as insurance, but the Model Law should provide standards for a regulated entity to observe when they are marketing and selling such non-insurance products as complementary products (i.e., sold alongside) to a pet insurance contract.

This approach is flawed for two major reasons. First, it divorces the identification of pet insurance from any objective definition of insurance. Instead of pet insurance being defined as coverage for the transfer of risk, including risk prevention products and services, NAPHIA suggests that pet insurers and pet service providers be the arbiters of what is or is not insurance.

Second, the proposal creates an irreconcilable conflict of interest that will encourage conversion of insurance coverage into non-insurance wellness programs, thereby depriving taxpayers of premium tax and consumers of insurance regulatory oversight and protection.

Regarding the conflict of interest, consider the common situation of a pet service provider who distributes pet insurance and also offers a non-insurance wellness program. The pet service provider distributing the pet insurance product for the pet insurer has the market power because they control if and what pet insurance products they will distribute. The pet service provider can direct the pet insurer to remove coverages from the pet insurance policies offered to enable the pet service provider to include more services in the wellness program.

To illustrate, let's assume there are 15 coverages that are insurance (including prevention coverages like flea and tick treatment, nail trimming, periodic check-ups) and 2 services that are non-insurance (say, pet tracking tags and grooming). The pet service provider distributing the insurance tells the pet insurer to remove certain coverages from the policy because the pet service provider wants to offer a broader (and more expensive and more profitable) non-insurance wellness program.

We want to be clear that we are not assigning or suggesting nefarious motive or intent to any entity. Rather, we are identifying the role of market forces and conflicts of interest that will lead certain participants to act in their self-interest at the expense of consumers.

To address these issues, we suggest the model clearly define what is or is not pet insurance. ***Pet insurance should be defined as coverage for any services to heal injured or ill pets, to maintain the health of the pet or to prevent pet illness or injury.*** By clearly and broadly defining pet insurance, the ability of pet insurers and pet service providers to engage in regulatory arbitrage is limited.

We believe that a consumer's frame of reference for pet insurance is their own personal health insurance. Stated differently, consumers will consider pet insurance as a health insurance product and not as a property-casualty product. The consumer's expectation will be based on their personal health insurance experience, not on their auto or home insurance experience. No amount of disclosure will change that and the model must be designed to minimize consumer confusion, which we believe our recommendations would address.