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A REGULATOR'S GUIDE TO PET INSURANCE

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INTRODUCTION

In December 2016, an insurer in the pet health insurance (pet insurance) industry voiced concerns to the Producer Licensing (D) Task Force regarding the use of limited lines licensing for pet insurance. The insurer recommended that pet insurance be removed from the *State Licensing Handbook* (Handbook) Uniform Licensing Standard (ULS) No. 37 – Surplus Line Exam as a limited line. It was the insurer's opinion that a full property/casualty (P/C) line should be required to sell, solicit or negotiate pet insurance. Reasons cited include: 1) tremendous growth in the pet insurance market; 2) policy premiums that far exceed the cost of the covered item; i.e., the pet; and 3) complex policies with multiple coverage options and exclusions. Traditionally, limited lines products are designed to be incidental to the sale of another product, which, according to the insurer, is not the case with pet insurance. The Task Force decided it needed to better understand the complexities of pet insurance before offering guidance regarding the type of producer license required to sell the product. As a result, the Task Force made a referral to the Property and Casualty Insurance (C) Committee to draft a comprehensive white paper providing information on coverage options, product approval, marketing, ratemaking, claims practices and regulatory concerns.

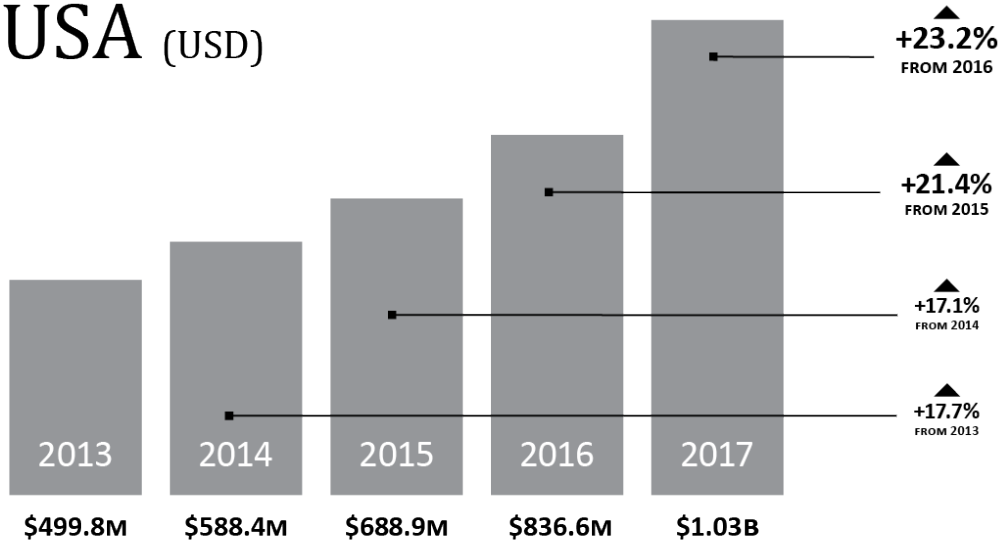
As discussed during the Property and Casualty Insurance (C) Committee's meeting at the 2018 Spring National Meeting, the Committee formed a drafting group to develop a white paper to provide an overview of the pet insurance industry. This white paper represents the Committee's findings. Please note that all websites and companies discussed in this paper are included for research only and are not endorsements by the NAIC.

Pet insurance provides accident and illness coverage for family-owned pets, primarily dogs and cats. Although pet insurance is classified and regulated as P/C insurance, it bears many similarities to human health insurance with annual coverage offered at an actuarially determined rate subject to various conditions and exclusions. This coverage was started in the U.S. in 1980 and has grown significantly since that time.

The North American Pet Health Insurance Association (NAPHIA) represents more than 99% of the U.S. and Canada pet insurance industry as an advocacy group. As shown in Figure 1, the total premium volume for NAPHIA members in 2017 was approximately $1.03 billion in the U.S.,

representing 23.2% growth over the prior year. The growth of the P/C insurance industry as a whole was only 4.7% from 2016 to 2017. The direct written premium in the U.S. (including the territories) was approximately $640 billion in 2017, so while the pet insurance market is growing faster than the total P/C market, pet insurance still represents a small percentage of the total.

FIGURE 1. PET INSURANCE PREMIUM VOLUME

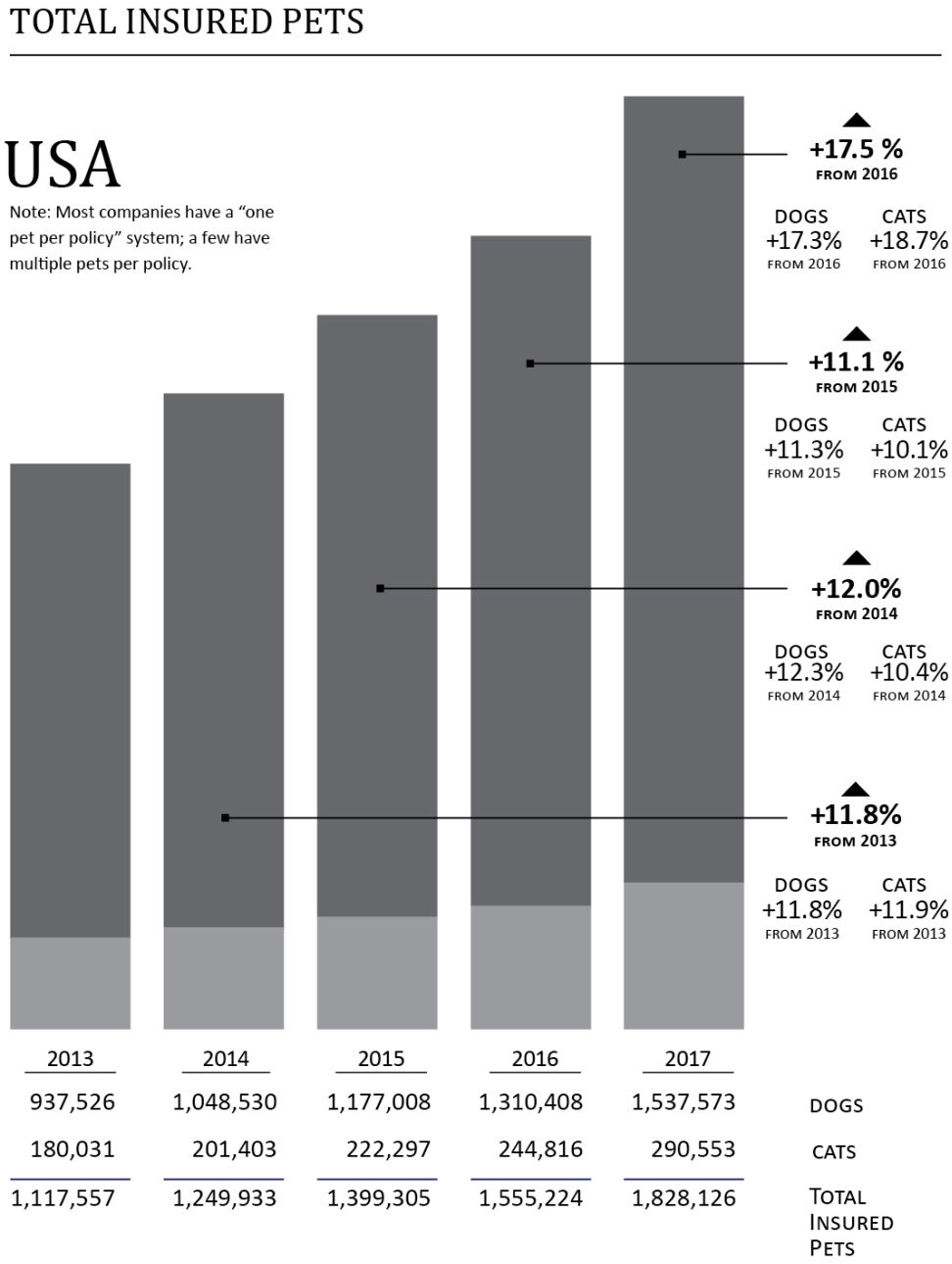


SOURCE: North American Pet Health Insurance Association. State of the Industry Report 2018. naphia.org/industry/research-and-reports/terms-conditions-use-state-industry-report

According to a survey conducted by the American Pet Products Association (APPA),[1] in 2017, approximately 68% of U.S. households, or 84.65 million families, owned at least one pet (dog, cat or other). 60 million of these households owned at least one dog, and 47 million of the households owned at least one cat. There are significant opportunities for growth in the pet insurance market, with approximately 90 million household dogs and 95 million household cats in the U.S. According to the NAPHIA, as shown in Figure 2 below, approximately 1.5 million dogs and 300,000 cats were insured in 2017, meaning fewer than 2% of dogs and less than 0.5% of cats owned in the U.S. were insured in 2017. As shown in Figure 2, the number of insured dogs and cats increased by 17.5% from 2016 to 2017.

[1] *https://americanpetproducts.org/Uploads/MemServices/GPE2017_NPOS_Seminar.pdf*

FIGURE 2. TOTAL INSURED PETS



SOURCE: North American Pet Health Insurance Association. State of the Industry Report 2018. naphia.org/industry/research-and-reports/terms-conditions-use-state-industry-report

HISTORY

The first "pet insurance"[2] policy was issued in 1890 in Sweden and focused on horses and livestock. In 1924, the first policy covering a dog was issued in Sweden. In 1947, the first pet insurance policy was issued in the United Kingdom (UK). In Sweden and the UK, modern pet insurance policies are designed with the ability to cover pet medical costs and liability to third parties for the action of pets. Sweden has a requirement that dog owners must maintain liability coverage and, as a result, 60–70% of pet owners retain pet insurance. In the UK, 25–30% of dog and/or cat owners maintain pet insurance.

The first pet policy in the U.S. was issued in 1982 by Veterinary Pet Insurance (VPI). VPI was founded by a veterinarian from Orange County, CA. For the majority of the 1980s and 90s, VPI had a near monopoly over the U.S. market. In the early 2000s, additional companies joined the market. At the time, VPI had approximately 80% of the market. As shown in Figure 3 below, VPI, which was purchased by Nationwide and operating under that name, maintained more than 35% of the market for pet insurance in 2017. The market has grown significantly from the 1980s. Figure 1 above shows the remarkable growth over the past five years alone.

Figure 3 shows the 2017 U.S. premiums written by the top five insurers and branding entities with their 2017 premiums written established for the sale of pet insurance. Branding entities are programs that can be underwritten and sold by multiple insurers and are subject to change. Additionally, insurers may underwrite a variety of pet insurance programs. Branding entities may have programs underwritten by multiple insurers, and insurers may underwrite for multiple brands. The use of brand names is common in the industry which, without proper disclosure can cause confusion for state insurance regulators and consumers in determining the entity with a duty to indemnify.

[2] The use of the term "pet insurance" in this paper does not refer to insurance policies that cover horses and livestock, commonly referred to as "blood stock," which provide indemnity for animal mortality. The term "pet insurance" in this paper refers to the products commonly covering dogs and cats and providing indemnity for the cost of dogs' and cats' medical treatment. All of the participants in the market cover cats and dogs. A few participants also cover horses and exotic animals kept as pets.

FIGURE 3. TOP SELLERS

COMPANY/BRANDING ENTITY	USD (IN MILLIONS)	MARKET SHARE
Nationwide	$ 374.60	36.33%
Trupanion	$ 191.60	18.58%
Healthy Paws Pet Insurance and Foundation	$ 123.20	11.95%
Petplan Pet Insurance	$ 83.60	8.11%
Crum & Forster Pet Insurance Group	$ 69.20	6.71%
Other	$ 188.80	18.32%
TOTAL	**$ 1,031.00**	100.00%

SOURCE: North American Pet Health Insurance Association. State of the Industry Report 2018. naphia.org/industry/research-and-reports/terms-conditions-use-state-industry-report

Although the U.S. market has been growing by 15% or 20% a year for the last five years, it still only covers approximately 1% of the estimated 1.1 million dogs and cats kept as pets in the U.S. As noted in Figure 4, pet insurance coverage is concentrated in larger urban areas, with California and New York being the largest markets. However, over the last two decades, product offerings have expanded as additional insurers have entered the market. Caution should be used when contemplating data contained in Figures 1–4. Data for these figures was provided by the industry association NAPHIA, not the states or the NAIC. Data contained in Figures 1–4 include NAPHIA members only and, therefore, are not exhaustive of the entire market for pet insurance. As discussed later in the paper, premiums and losses for pet insurance policies are contained in the inland marine line of business on the NAIC annual financial statement; therefore, data for pet insurance, specifically, is indeterminate at this time.

A few states have initiated data calls or market conduct examinations concerning pet insurance. Massachusetts' data call was designed to identify pet insurance writers and their premium volume in the state. New Hampshire published a report of its data call, revealing that 20 companies filed forms in the System for Electronic Rate and Form Filing (SERFF) in 2017, but only nine reported premiums from 2015 through 2017. The two largest companies accounted for 59% of the market in New Hampshire in 2017.

FIGURE 4. POLICIES AND PREMIUMS BY STATE

2017	Number of Policies	Number of Policies (%)	Gross Written Premium ($)	Gross Written Premium (%)
U.S.	**1,832,592**		**$ 1.03 B**	
Alabama	7,254	0.4%	$3.79 M	0.4%
Alaska	5,720	0.3%	$2.62 M	0.3%
Arizona	34,485	1.9%	$19.21 M	1.9%
Arkansas	2,862	0.2%	$1.35 M	0.1%
California	362,727	19.8%	$219.54 M	21.4%
Colorado	53,986	2.9%	$30.81 M	3.0%
Connecticut	39,215	2.1%	$22.65 M	2.2%
Delaware	6,497	0.4%	$4.24 M	0.4%
District of Columbia	8,444	0.5%	$3.87 M	0.4%
Florida	116,855	6.4%	$64.94 M	6.3%
Georgia	31,757	1.7%	16.11 M	1.6%
Hawaii	9,073	0.5%	$5.19 M	0.5%
Idaho	5,003	0.3%	$2.51 M	0.2%
Illinois	62,149	3.4%	$34.53 M	3.4%
Indiana	15,336	0.8%	$7.40 M	0.7%
Iowa	6,522	0.4%	$3.01 M	0.3%
Kansas	6,981	0.4%	$3.28 M	0.3%
Kentucky	8,848	0.5%	$4.21 M	0.4%
Louisiana	9,724	0.5%	$4.76 M	0.5%
Maine	8,371	0.5%	$4.35 M	0.4%
Maryland	45,449	2.5%	$25.70 M	2.5%
Massachusetts	86,703	4.7%	$48.83 M	4.8%
Michigan	27,642	1.5%	$14.10 M	1.4%
Minnesota	17,552	1.0%	$8.85 M	0.9%
Mississippi	2,815	0.2%	$1.35 M	0.1%
Missouri	13,363	0.7%	$6.38 M	0.6%
Montana	2,759	0.2%	$ 1.28 M	0.1%
Nebraska	3,961	0.2%	$1.96 M	0.2%
Nevada	26,574	1.5%	$14.67 M	1.4%
New Hampshire	15,452	0.8%	$8.58 M	0.8%
New Jersey	104,884	5.7%	$61.96 M	6.0%
New Mexico	6,336	0.3%	$3.26 M	0.3%
New York	179,133	9.8%	$106.52 M	10.4%
North Carolina	40,557	2.2%	$21.51 M	2.1%
North Dakota	1,065	0.1%	$0.52 M	0.1%
Ohio	35,968	2.0%	$18.24 M	1.8%
Oklahoma	4,829	0.3%	$2.31 M	0.2%
Oregon	27,086	1.5%	$15.15 M	1.5%
Pennsylvania	87,570	4.8%	$46.10 M	4.5%
Puerto Rico	1,024	0.1%	$0.70 M	0.1%
Rhode Island	9,451	0.5%	$5.05 M	0.5%
South Carolina	16,776	0.9%	$7.96 M	0.8%
South Dakota	1,034	0.1%	$0.95 M	0.1%
Tennessee	15,405	0.8%	$9.70 M	0.9%
Texas	93,529	5.1%	$46.64 M	4.5%
Utah	7,987	0.4%	$3.91 M	0.4%
Vermont	4,455	0.2%	$3.55 M	0.3%
Virginia	60,310	3.3%	$33.75 M	3.3%
Washington	69,667	3.8%	$36.93 M	3.6%
West Virginia	5,052	0.3%	$1.71 M	0.2%
Wisconsin	16,395	0.9%	$8.63 M	0.8%

SOURCE: North American Pet Health Insurance Association. State of the Industry Report 2018.

naphia.org/industry/research-and-reports/terms-conditions-use-state-industry-report

A study of the more developed markets in other countries may help identify points of concern and direct the governing of pet insurance products in the U.S. There are no filing or producer licensing requirements in the UK or Sweden, so no instructive elements can be gleaned from their experience on these two issues. The Canadian market is similar to the U.S. market in both products and market penetration, having developed over a similar time period. Pet insurers report that 70% of sales are initiated online, and 30% of sales are initiated through call centers.

California is the only state with a law specifically governing pet insurance[3]. California Insurance Codes 12880–12880.4 were created in 2014 and can be found in Appendix 2. The laws require pet insurers to disclose baseline information regarding reimbursement benefits; preexisting condition limitations; and a clear explanation of limitations of coverage including coinsurance, waiting periods, deductibles, and annual or lifetime policy limits. The California laws also provide consumers with a 30-day "free look" period in which a pet insurance policy can be returned for a full refund. An earlier version of this bill attempted to prevent exclusions for preexisting conditions but was vetoed by the Governor of California. A pet insurance bill was introduced, but not enacted, in New York.

None of the failed bills or the California statute address producer or adjuster licensing. Most states require a full P/C license to sell, solicit or negotiate pet insurance, while a few states—Idaho, New Jersey, Rhode Island and Virginia—allow for use of a limited lines license.

CARRIERS

As noted above, insurance companies commonly advertise pet insurance products using the insurers' brand name (a practice referred to as "branding") rather than the insurance company name. Branding is common practice in many lines of business, not limited to pet insurance, and with proper disclosure it should not present any legal or regulatory concerns. Additionally, it is commonplace in the pet insurance market for branded entities to change underwriters for their pet insurance program with some frequency. This makes it difficult for examiners to identify licensed entities associated with the sale of pet insurance products and track compliance with regulatory

[3] California has a pending bill, CA AB 1535, that would require pet insurers to provide additional disclosures to consumers.

requirements. When insurers use a brand name, the insured must read the fine print at the bottom of the advertisement, application or website to find the identity of the underwriting company. In addition to use of brand names, one to three agencies may sell the pet insurance products for an insurer under a specified brand name. The agency communicates with the consumer and receives applications. In most cases, the agency is also responsible, as a third-party administrator (TPA), for claims processing and answering consumer inquiries. This practice can cause confusion for consumers in determining the entity responsible for paying claims and who should be named if they need to file a complaint with the state insurance department.

COVERAGE OPTIONS

Two coverage types are available through a majority of carriers selling pet insurance: 1) accident only; and 2) accident and illness. According to the NAPHIA, 98% of policies written in 2017 were for accident and illness insurance, which may include embedded wellness, while 2% were accident only. The average premium for accident and illness plans was approximately $516, while the average premium for accident only plans was approximately $181 per pet in the U.S. in 2017.

Some veterinary clinics offer agreements for preventive care. If the agreement is a two-party contract between the veterinarian and consumer where no risk is transferred or assumed and no third party is involved, these plans are not insurance. However, these may cause confusion for consumers as they may be construed as insurance. State insurance regulators should be aware that these exist, as they may be called upon to review the structure of the agreement.

Coverage options vary by carrier. Most companies write coverage for dogs and cats only. One carrier also has policies for exotic pets, such as reptiles and birds. Consistent with human or non-pet coverage, plans have varying deductibles, copayments and limits. In most cases, pet owners must pay the vet directly and wait to be reimbursed by the insurance carrier or account administrator. Reimbursement methods differ. Some include a benefit schedule based on illness or injury and coverage level. There are waiting periods and pre-coverage exams required in many cases. Pets must be above the minimum and below the maximum age limits to begin coverage. Many carriers exclude coverage for pets less than eight weeks old or older than 12 years. Exclusions exist for preexisting conditions, and there may be limitations on coverage for hereditary

or congenital conditions as well. Definitions of conditions are inconsistent across policies and, therefore, may have varying impacts on the consumer's ability to receive reimbursement for claims. Appendix 1 contains a glossary of terms as defined in California Assembly Bill No. 2056, Chapter 896, requiring use of the specified terms for all policies that are marketed, issued, amended, renewed or delivered to a California resident, on or after July 1, 2015. While there are many different policies on the market today with various coverage options, most policies include:

- **Two primary coverage types: accident only, or accident and illness plans.** Comprehensive policies may cover reasonable and necessary veterinary expenses that occur during the policy period for medical management, diagnosis or treatment of a pet's condition. Veterinary expenses or services include medical advice, diagnosis, care or treatment provided by a veterinarian. Other services and medical expenses that may be covered include the costs of the visit, prescription drugs, food, supplements and medical equipment, surgical procedures, physical therapy, and dental procedures.
- **Optional wellness and preventive coverage.** Such coverage may be available, which covers veterinary expenses during the policy period for preventive treatment or treatment provided to preserve or improve general nutrition or health when there are no underlying symptoms of an associated diagnosed medical condition. This typically includes vaccinations, flea and heartworm medication, wellness exams, blood tests, radiographs, heartworm tests, screens, urinalysis, deworming, pet identification (microchip), spaying or neutering, dental cleaning, genetic certification, etc.
- **Different plan options.** Pet health insurers may offer different plan options or tiers with varying policy limits.
- **Description of the veterinarians and clinics that may be used under the plan.**
- **Limits, which may be annual, lifetime, per procedure, per incident or a combination.** Optional coverages may have special limits.
- **Copayments applicable to the cost of each procedure, an overall limit or other basis.** Generally, there is a coinsurance percentage and/or deductible.
- **Waiting periods for injury, illness and orthopedic care.** Pet health waiting periods are usually broken up into two separate periods for illness and injury, but other pet health insurers may add longer waiting periods for specific coverages such as orthopedics or cruciate ligament events, etc. Although most of the definitions in pet

health policies for waiting periods include the language "these waiting periods are waived for continuous renewal," the waiting periods may apply again if there are policy changes.

- **Policy exclusions, which often include exclusions for preexisting conditions.** Some may even exclude coverage in renewal policies for conditions diagnosed or treated in prior coverage periods. Many policies also exclude coverage for congenital and heredity conditions, such as hip dysplasia, heart defects, cataracts and diabetes. Other typical exclusions may include: preventive treatment or wellness care; dental care; vaccinations; flea prevention; spaying or castration; behavioral training/therapy or treatment; procedures, services or supplements for a condition not covered by the policy; service or procedures not performed or prescribed by a licensed veterinarian; over-the-counter food or supplies; boarding or accommodation; transportation; grooming; membership fees; experimental and/or investigative treatment that is not within the standard of care; diagnosis, treatment, tests or procedures associated with breeding etc.
- **A schedule or plan for recovery of benefits.** Most plans include a reimbursement model, meaning the insured must pay out of pocket to the veterinarian and be reimbursed by the insurer. Only one carrier in the market today pays the veterinarian directly.
- **Nondiscretionary arbitration provisions.** Many contracts contain nondiscretionary arbitration provisions. Alternatively, some pet insurance policies contain language that set forth an arbitration process that requires peer review of the treatment provided by a veterinarian as opposed to engaging in an arbitration process conducted through the American Arbitration Association (AAA).

The coverage options and policy details associated with pet insurance are like those found in human health insurance. However, pet insurance is regulated and reported as P/C coverage because pets are considered property under the law. Provisions for in-network providers, co-insurance or co-payment, exclusions for preexisting conditions, age limits, and waiting periods are more like health insurance than P/C coverage.

Consumers may want to research policy provisions on their own prior to purchase. There are several consumer websites that provide guidance on pet insurance products. Consumers should also be aware that the price of insurance may increase substantially as the animal gets older. These websites also provide additional information on some of the policy provisions identified in the prior paragraphs.

POLICY FORMS

State law governs the requirements for policy review in a given line of business. State law may govern that the state is use and file, file and use, or prior approval. File and use means the form must be filed with the state insurance regulator but can be used before approval is obtained. Use and file means the form can be used before it is filed with the state insurance regulator. Prior approval requires that all insurance policy forms, riders and endorsements be approved by the state insurance commissioner/superintendent/director prior to being issued and sold to the public. While prior approval provides the highest level of oversight because policy forms cannot be used until approved, use and file, and file and use still provide states with the oversight to review filings for compliance with state-specific requirements.

A basic insurance policy form is an insurance contract delineating the terms, provisions and conditions of an insurance product. It includes endorsements and applications of which written application is required and is to be attached to the policy or be part of the contract.

Although state regulation of insurance was initially designed to prevent insurer insolvency, regulatory jurisdiction has evolved over the decades to protect consumers.[4] Policy form review is an integral part of market regulation. Policy forms are reviewed to ensure statutory compliance and that products are fair and not harmful to consumers. Regulatory review also helps insurance companies, as examiners may catch errors, inconsistencies, ambiguous or misleading language, and omission before products are offered to the public. This helps improve the quality of products offered and promotes consumer confidence.

[4] Kline, R., 1999. *A Regulator's Introduction to the Insurance Industry*, accessed at *https://www.naic.org/documents/prod_serv_marketreg_rii_zb.pdf.*

Policy form filings may be submitted through SERFF in most states. Currently, six states and the territories are not using SERFF for policy filing review. Policy form filings are generally submitted separately for each program. Insurers must be properly licensed for the appropriate line of business prior to submission of a form filing. Regulatory analysts review the policy forms submitted in the SERFF form filing to check for compliance issues relative to federal and state law, regulation, legislation or mandated language, and any state-specific advisory letters or bulletins issued by the state insurance commissioner/superintendent/director.

MARKETING STRATEGIES

Pet insurance may be sold via online marketing, veterinary clinics, pet stores, shelters and animal support and rescue organizations, or word of mouth referrals. Pet insurance may also be sold as part of an employee benefit package or through licensed insurance producers. The most common distribution methods are web-based marketing and referrals from veterinary clinics or friends and family. Veterinary offices, clinics or hospitals may promote pet insurance products to their customers or allow placement of printed materials throughout their office. Printed marketing materials may refer consumers to a website to obtain further information about a product. Materials sometimes include an application or phone number for the insurance company, a licensed insurance producer, or TPA. The veterinarian may partner with one brand exclusively or provide customers with brochures or pamphlets on several different brands. In addition, kennels and breeding clubs may promote coverage for pets or even have preferred carriers for specific breeds. Also, some organizations include information on pet insurance on their website to educate consumers about pet insurance and assist consumers in making comparisons among coverage options. However, as of this writing, none of that information has been vetted by the NAIC.

The fastest growing form of distribution is through an employee benefit package. Coverage may be sponsored in part by the employer or entirely employee paid. Special employee pricing is sometimes offered with group discounts. According to Nationwide, 50% of Fortune 500 companies offered pet insurance as an employee benefit in 2017.

LICENSING

To encourage uniformity, the Producer Licensing Uniformity (D) Working Group developed the ULS within the Handbook. Adopted originally in 2002, the ULS is a guide for state insurance regulators to use in their producer licensing process. In the November 2011 update, ULS No. 37 was added to address non-core limited lines licensure. Pet insurance was mentioned as an example, and a definition of "limited lines pet insurance" was included to mean an insurer designee, such as a managing general underwriter, managing general agent (MGA), or limited lines producer of pet insurance. As of September 2018, four states—Idaho, New Jersey, Rhode Island and Virginia—offer pet insurance as a non-core limited line.

Several market conduct enforcement actions on pet insurers were reported from 2015 to 2016. The issues identified in these actions included unlicensed sales, illegal inducements and rebating, improper use of rates, and unlawful claims practices.

The Producer Licensing (D) Task Force has held several meetings to discuss the type of license states should require of producers who are to sell, solicit or negotiate pet insurance policies.[5] "Negotiate" is defined in the *Producer Licensing Model Act* (#218) as "the act of conferring directly with or offering advice directly to a purchaser or prospective purchaser of a particular contract of insurance concerning any of the substantive benefits, terms or conditions of the contract, provided that the person engaged in that act either sells insurance or obtains insurance from insurers for purchasers." State insurance regulators agree that pet insurance should not be sold by unlicensed individuals, but they agree that what level of licensure and what steps should require licensure are open topics of discussion.

There is an open debate as to whether insurance producers and claims adjusters (in states where claims adjusters are licensed) should be required to have a full P/C license or a limited lines license to sell pet insurance. According to Model #218,[6] in order to obtain a resident license for the P/C line of authority, one must pass a written examination. According to the Handbook, states that require pre-licensing shall require 20 credit hours of pre-licensing education per major line of

[5] 2017 Summer and Fall National Meeting *Proceedings*.
[6] *https://www.naic.org/store/free/MDL-218.pdf*.

authority. The six major lines of authority identified in the Handbook are: 1) life; 2) accident and health (A&H) or sickness; 3) property; 4) casualty; 5) variable life and variable annuity; and 6) personal lines. Limited lines are considered alternatives to the major lines of authority. The products offered and the licensing requirements for limited lines tend to be more limited in scope. Except for crop and surety, pre-licensing examinations are not required for limited lines. Under both reciprocity standards set forth in Model #218 and the ULS, pre-licensing education is not required for nonresident applicants or nonresident producers who change their state of residency. Additionally, 24 credits of continuing education (CE) are required for each biennial compliance period only if the producer holds a license in one of the six major lines of authority. The Handbook also states that a person licensed as a limited lines producer in his or her home state shall receive a nonresident limited lines producer license, granting the same scope of authority as granted under the license issued by the provider's home state. This may be problematic if the type of license is inconsistent across states for a specified line of authority. A benefit of having the full licensing requirements is that education and testing requirements for licensure ensures that producers are competent and qualified to sell insurance to consumers, ultimately resulting in consumer protection. Alternatively, some take the position that the individuals most able to provide information on pets and pet insurance are those outside of the traditional insurance distribution channels. They may also argue that, under ULS No. 37, the traditional pre-licensing, testing and continuing legal education (CLE) do not include topics specific to pets or pet insurance; as such, the limited lines license model is more appropriate. As noted in the excerpt below, individuals offering insurance on a limited lines basis must receive a program of instruction or training subject to review by the insurance department.

In June 2015, the New Jersey Department of Banking and Insurance, Division of Insurance adopted N.J.A.C. 11:17-2.4 adding pet insurance to the list of limited lines coverage. The proposed rule cited the following reasons: 1) pet insurance products are offered by pet stores, veterinarian offices, pet training facilities, and other similar establishments, and are incidental to the services offered by such businesses; and 2) the knowledge and training needed to offer the product is unrelated to typical property and casualty insurance products and, as such, qualifies pet insurance as a limited line.

In November 2015, the former Producer Licensing Uniformity (D) Working Group adopted the following addition to ULS No. 37 in the Handbook:

> "A state is not required to implement any non-core limited line of authority for which a state does not already require a license or which is already encompassed within a major line of authority; however, the states should consider products where the nature of the insurance offered is incidental to the product being sold to be limited line insurance products. If a state offers non-core limited lines (such as pet insurance or legal expense insurance), it shall do so in accordance with the following licensing requirements. Individuals who sell, solicit or negotiate insurance, or who receive commission or compensation that is dependent on the placement of the insurance product, must obtain a limited line insurance producer license. The individual applicant must: 1) obtain the limited lines insurance producer license by submitting the appropriate application form and paying all applicable fees as set forth in applicable state law; and 2) receive a program of instruction or training subject to review by the insurance department."

The Working Group defined pet insurance as "health insurance coverage including, but not limited to, coverage for injury, illness and wellness for pets such as birds, cats, dogs and rabbits."

Another issue to consider regarding producer licensing is claims handling. One approach could be to require the business to hold or maintain a license and designate one person to be licensed within the organization. This is similar to the license required for portable electronics insurance which is sold to cover the cost of repair or replacement of the electronic device being sold. Employees assisting in claims handling would not be required to be licensed under certain circumstances if their claim-related activity was limited to pet insurance. Due to the complex coverage options offered by pet insurance policies, it may not be in the best interest of the consumer to allow unlicensed individuals to adjust pet insurance claims. Alternatively, adjusters must review veterinary records, including non-standard pet health codes, which may require technical knowledge and expertise in animal science. This is not dissimilar to other lines of business in which subject matter experts (SMEs) work in conjunction with licensed adjusters or adjusters need specialized training to effectively handle claims where a high level of technical knowledge is

required. A combination of adjuster training and access to SMEs is needed to properly adjust pet insurance claims. Other lines of business may have separate licensing requirements for producers and adjusters requiring a full property casualty license for producers and a limited lines license for adjusters.

RATES

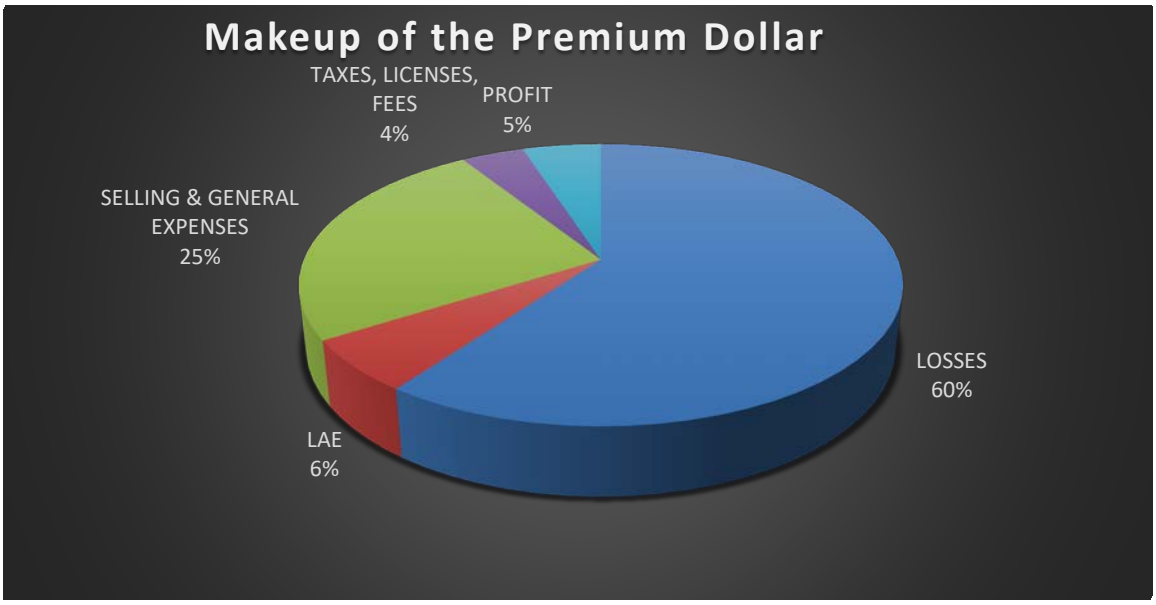
Pet insurance is regulated as a P/C insurance line of business included in the annual statement under inland marine. There is no specific financial reporting line for pet insurance, which makes it difficult to track the premiums attributable to pet insurance. Like most P/C lines, the rates and rating rules are regulated by the department of insurance (DOI) of the state in which the policies are written. SERFF contains a specific sub-type of insurance for pet insurance plans (9.0004). However, its use is not consistent in all states. For instance, in Rhode Island, pet insurance policies are filed under inland marine, a personal insurance code, rather than under the pet sub-type of insurance. Florida and, until recently, Virginia require pet insurance to be filed under livestock. Proposed rates and rating rules are frequently scrutinized by insurance professionals working within or under contract for the DOI to ensure that the rates are not inadequate, excessive or unfairly discriminatory.

When an insurer initiates a pet insurance program in a given state, and each time it wishes to change the rates and/or rating rules, the insurer files its proposal, with supporting documentation and various state-specific information, with the DOI. The DOI reviews the filing and either approves or disapproves the insurer's plan. State-specific filing guidance can be found at each state DOI's website. (See *https://www.serff.com/serff_filing_access.htm*.)

Like in other lines of insurance, for pet policies, the rate or premium charged is intended to cover the three basic costs of the insurer: 1) claim costs (also known as losses); 2) the insurer's expenses; and 3) a profit provision. The claim costs represent the largest portion of the insurance premium dollar (60%–70% for most P/C lines) and include loss adjustment expenses (LAEs). The expenses of the insurer include commissions paid to agents, general operating expenses, premium taxes, and other fees paid to the states. The profit provision (also known as profit and contingencies) affords a reasonable return on the insurer's invested capital. A significant amount of capital must be

available to guard against poor claim experience and catastrophes. Figure 5 shows the typical components of each premium dollar charged for pet insurance.

FIGURE 5. MAKEUP OF THE PREMIUM DOLLAR



As discussed in detail under the coverage options section above, many pet insurance carriers offer more than one health plan. By far the most common is an "accident and illness" plan covering both fortuitous injuries, as well as health issues of the pet (subject to various limitations and exclusions). A less expensive alternative is an accident-only plan, which may cost around 60% less than an accident and illness plan. Most policies are written on an annual basis.

For an additional charge, typical plan options can include (on a bundled or unbundled basis):

- Preventive/wellness care
- Dental care
- Spay/neuter
- Cancer treatment
- Diabetes coverage
- Inherited/congenital conditions
- Behavioral therapy
- Prescription coverage

- Alternative medicine
- Lost pet recovery
- Ambulance care
- Euthanasia/cremation/funeral coverage
- Accidental death benefit
- Travel/vacation coverage
- Boarding/kenneling (unforeseen circumstances)

Few insurers offer preventive or wellness as a stand-alone coverage. It is typically offered as an add-on to an accident and illness policy.

RATING

To understand pet insurance rates, one can think of an overall rate level and a rate structure. The overall rate level is usually represented by a base rate. A base rate is the starting point before various rate structure modifications are made. The rate structure can be viewed as a set of tables of multiplicative factors that modify the base rate according to various risk characteristics.

Given a rate structure, the base rate can be viewed as a scaling factor that adjusts the overall rate level to an appropriate magnitude. Consider a highly simplified example in which the rate structure recognizes two species (dog and cat) and two geographic classifications (rural and urban). Let us say the rate structure has the following rating factors:

	Geographic Class	
Species	Rural	Urban
Dog	1.00	2.00
Cat	0.60	1.20

In this rate structure, all else equal, the cat necessitates 40% less cost than the dog, and urban areas entail 100% more cost than rural areas. Of course, the insurer must select an overall dollar rate level to apply to the four rating factors as appropriate. Let us say the insurer selects an annual base rate of $300. Then, a table of annual rates can be laid out as the above table of rating factors, multiplied by $300, which represents the dollar-denominated scaling factor for the rating system:

	Geographic Class	
Species	Rural	Urban
Dog	$300	$600
Cat	$180	$360

Building the rates upon an overall rate level and rate structure allows the insurer to easily analyze and adjust rates over time. Inflation in veterinary costs will cause the base rate to increase over time. The rate structure will often stay stable for years at a time. Modest adjustments may be needed due to changes in cost drivers. Insurers typically monitor known cost drivers for increases over time.

Pet insurance rate structures are relatively similar across insurers, but they will have some variances in the risk characteristics, the rating factors for those risk characteristics, or both. Insurers generally use the same rate structure in all the states where they operate, but there may be exceptions based on a company initiative or state regulatory requirement.

Policy premium is the amount charged to the insured for coverage. An installment fee may be applied if the insured elects to pay for the insurance in installments rather than paying in full at the beginning of the policy term. Installment fees typically vary from $1 to $6 per pay period, depending on the insurer and the mode of payment (electronic funds transfer [EFT], credit card, etc.). An insurer may charge other fees such as non-sufficient fund fees, late fees, and reinstatement fees. These ancillary fees generally vary from $10 to $30 each. All fees, including ancillary fees, must be properly disclosed in rate filings along with supporting documentation.

RATING VARIABLES

A rating variable is a characteristic of a rating plan. Typical rating variables for pet insurance include geographic area, deductible, copay, limit, species, pet age, breed, etc. These rating variables are discussed in more detail below.

Geographic Area

Pet insurance rates generally vary by state and often by territory within the state. These territories are usually drawn along the boundaries of counties or ZIP code groupings. Generally, the rates will be higher in urban areas due to higher costs of veterinary services and other socioeconomic factors. For pet insurance, geographic rating factors may range from 1.000 on the low end to 2.000 for the highest cost areas in the U.S.

Deductible

A deductible is the amount of money an insured has agreed to pay for pet treatment before the insurer begins paying out on provided coverage. The deductible is intended to ensure that the insured seeks only necessary pet health treatment and pays for much or all of the smaller claims, with the insurer paying out only for larger claims. Discounts are provided for higher deductibles, resulting in lower annual premiums. Typical deductibles range from $50 to $250, although higher deductible plans can be purchased at a substantial premium savings.

Deductibles are typically provided by insurers on a per incident or annual basis. Some insurers allow the insured to select either annual or per incident options, while others only have one reimbursement method. Coverage typically costs more with an annual deductible because it tends to result in a higher cost for the insurer and lower cost for the insured. Coverage with an annual deductible routinely costs 4–6% more than a per incident deductible plan.

Co-Insurance or Copay

The co-insurance percentage (sometimes referred to as copay) is the percentage of loss the insured has agreed to pay after the deductible is satisfied. Much like the deductible, the co-pay is intended to encourage the insured to use the insurance judiciously, with some “skin in the game” in partnering with the insurer to keep costs at a necessary and reasonable level. Copays are usually provided as multiples of 10; i.e., 10%, 20%, 30% and possibly higher. As compared with a 10% co-pay, a 20% co-pay can save between 5% and 25% of the insurance cost, depending on the insurer. Premium discounts are provided for out-of-pocket costs in the form of the copayments for the insured. Plans with 0% copay may be available for a higher premium amount.

Limit

Insurance policy limits are the maximum dollar amount an insurer will pay for claims. Policy limits are normally expressed on a per incident basis, as well as an aggregate policy term basis. Many insurers have both per incident and aggregate limits for one policy. Few insurers also use maximum lifetime limits; i.e., for the life of the pet. Higher limits are more expensive because they could ultimately result in higher claim payments for the insurer. An illustration follows:

Deductible	$100
Deductible Type	Per Incident
Copay	20%
Per Incident Limit	$1,000
Annual Limit	$10,000

(1) Amount Charged for Pet Treatment (three different scenarios shown)	$75	$150	$1,500
(2) Amount Paid by Insurer	$0	$40	$1,000
(3) Amount Paid by Insured	$75	$110	$500

NOTES:

$75 treatment:	$0 = $75 – $100, subject to a minimum of $0
$150 treatment:	$40 = ($150 – $100) x (100% – 20%)
$1,500 treatment:	$1,000 = ($1,500 – $100) x (100% – 20%), subject to a maximum of $1,000; i.e., the per incident limit
	(3) = (1) – (2)

Also: If there had been 12 $1,500 treatments in the course of an annual policy term, the insurer would have paid the first 10 only at $1,000 each, since the insurer's annual limit (maximum liability) of $10,000 would have been reached at that point.

Species

Most pet insurance carriers offer insurance for dogs and cats. Only one insurer offers coverage for other types of animals, such as birds and reptiles, under its exotics policy.

Pet Age

Most insurers will not cover pets less than eight weeks old or more than 12 years old. Health risks tend to be greater for these age ranges. For both dogs and cats, older pets can cost two to four times as much, depending on the insurer.

A few insurers use the age at which the pet was initially enrolled for health insurance, either in addition to or in lieu of the pet's current age. Use of initial enrollment age allows an insurer to guard against adverse selection (e.g., an older pet in failing health being insured for the first time). If the exact age of a pet is not known, the insurer may ask the insured to obtain an estimate from the pet's veterinarian. At least one insurer uses four different age curves for dogs depending on their weight. Typically, the heavier the dog, the steeper the age curve.

Breed

There are more than 100 dog breeds and around 50 cat breeds. Some of the most common dog breeds in the U.S. are Mixed Breed, Labrador Retriever, Golden Retriever, German Shepherd, Rottweiler, Bulldog, Poodle, Terrier and Boxer. Common cat breeds are the American Shorthair, Maine Coon, Oriental, Persian, Ragdoll, Siamese, Sphynx, Birman and Abyssinian. Most insurers group the breeds into 10 or 12 rating categories, with each category assigned a rating factor. Smaller dogs and mixed breeds are frequently in the lower rating categories, while larger pure bred dogs are assigned to the higher rating categories. Dogs in the highest rated category can cost 50–75% more than the lowest rated group. Cost variances for cats tend to be less. The cat breed factor curve will usually be significantly flatter, with the highest rated costing 0–50% more versus the lowest rated breed. This reflects the fact that breeds are significantly more homogeneous for cats than dogs in terms of size, build and other characteristics.

Multi-Pet

Many insurers offer a multi-pet discount because of the reduced administrative expenses per pet for a multi-pet policy. Multi-pet discounts are often in the 5–10% range.

Group Marketing

Many insurers offer a group marketing discount, also known as an association or affiliation discount. Marketing discounts recognize the cost efficiencies of partnering with different types of organizations in promoting the insurer's product and offering seminars, pamphlets and other services that strive to lower pet health costs. Typical partners include designated corporate groups—i.e., group benefit plans—affinity groups, strategic partners and veterinary clinics, for which the employees and/or members may receive the discount. Group marketing discounts are often in the 5–10% range.

Miscellaneous

Other rating variables used by some insurers include:

- Policy term; i.e., pro rata factor if other than one year.
- Waiting period length (discount for longer periods).
- Renewal discount.
- Claim-free discount.
- Pet gender; i.e., females rated about 5% less than males.
- Spay/neuter discount.
- Wellness plan discount.
- Predictive test discount.
- Exam fee coverage (discount for exclusion).
- Microchip/identification tattoo discount.
- Service or therapy dog discount (or surcharge).
- Military discount.
- Animal health employee discount.
- Shelter adoptee discount.
- Automated clearing house (ACH) payment discount.
- Premium paid-in-full discount; i.e., no installment plan used.

- Online enrollment/paperless policy administration discount.

RATING EXAMPLE

For a typical accident and illness plan, an illustrative and hypothetical example of the workup of a rate follows:

Overall Rate Level:	
Annual Base Rate*	$300
*Reflects:	
Geographic Area	#1
Deductible	$100
Deductible Type	Per Incident
Co-Pay	10%
Per Incident Limit	$1,000
Annual Limit	$10,000
Species	Dog
Pet Age	Less than 1 year
Breed Group	1
Multi-Pet	No
Group Marketing Member	No

Rate Structure Adjustments:	
Geographic Area (#3)	1.160
Deductible ($150)	0.955
Deductible Type (Annual)	1.060
Co-Pay (20%)	0.925
Per Incident Limit ($2,000)	1.280
Annual Limit ($10,000)	1.000
Species (Dog)	1.000
Pet Age (5)	1.240
Breed Group (4)	1.050
Multi-Pet (No)	1.000

Group Marketing Member (Yes)	0.950
Final Rate	$516; i.e., $300 x 1.160 x … x 0.950

RATEMAKING

Ratemaking represents the estimation of a set of rates needed to manage an insurance program. Rating uses a set of rates to determine which rate is appropriate for a particular risk given its risk characteristics. Generally, ratemaking is performed by an actuary; rating is performed by an underwriter. An overview of actuarial science is provided in Appendix 3.

Actuarial Standards of Practice (ASOPs) set forth principles and considerations for an actuary estimating costs associated with the transfer of risk. Principle 1, Principle 2 and Principle 3 from the Casualty Actuarial Society's (CAS) *Statement of Principles Regarding Property and Casualty Insurance Ratemaking* are particularly relevant:

Principle 1: A rate is an estimate of the expected value of future costs.
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.

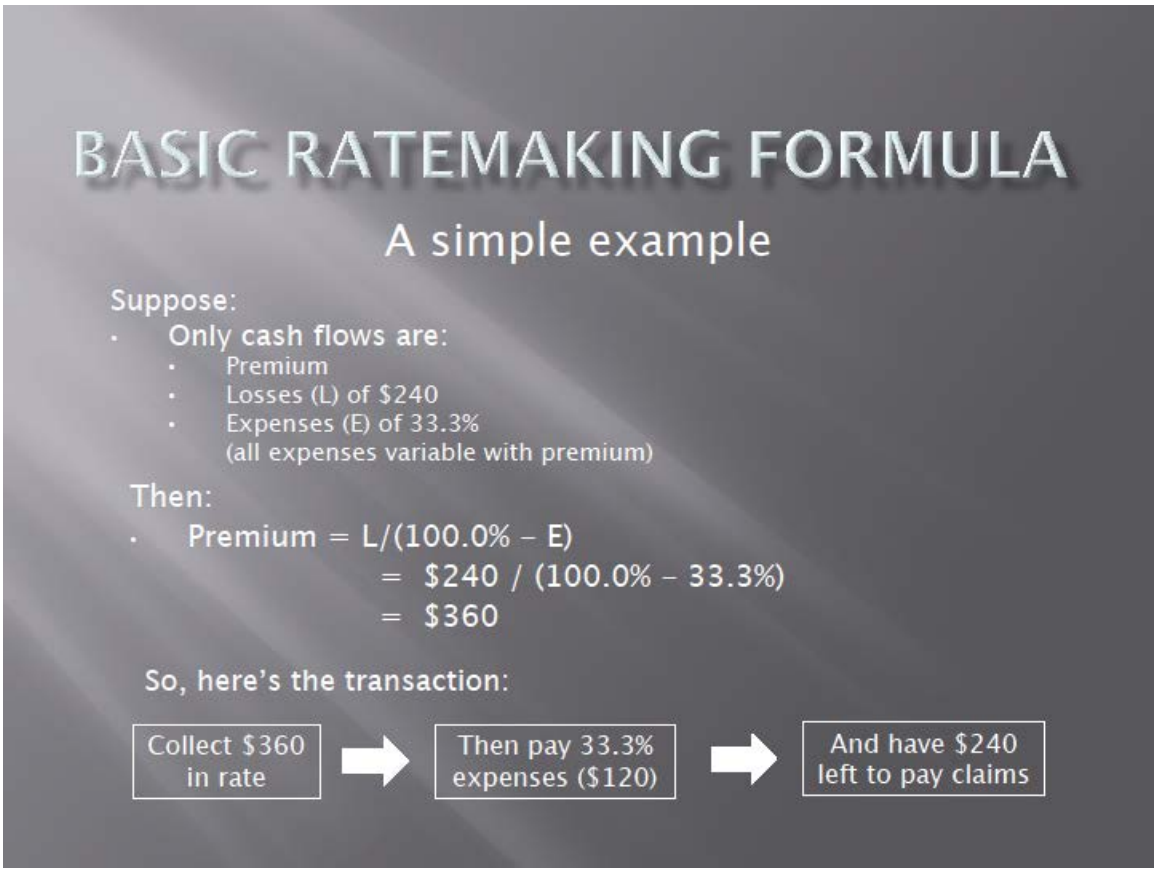
Adherence to these principles should lead to P/C rates that are reasonable, not excessive, and not unfairly discriminatory.

Some of the most important ASOPs published by the Actuarial Standards Board (ASB) that pertain to pet insurance ratemaking include:

- ASOP 12 – Risk Classification
- ASOP 13 – Trending Procedures in Property/Casualty Insurance
- ASOP 23 – Data Quality
- ASOP 25 – Credibility Procedures
- ASOP 29 – Expense Provisions in Property/Casualty Insurance Ratemaking
- ASOP 30 – Treatment of Profit and Contingency Provisions and the Cost of Capital in Property/Casualty Insurance Ratemaking
- ASOP 41 – Actuarial Communications

RATEMAKING EXAMPLE

If the actuary can estimate the expected losses for a given policy and knows the expense structure, he/she can estimate the needed rate as a grossing up of the expected losses. This approach is often used at the onset of an insurance program.



As the insurance program grows and develops a significant amount of premium, the actuary will normally analyze the performance annually to determine the indicated rate change. The goal is to estimate how much the premiums would need to be adjusted to bring the relationship between losses and premiums (loss ratio) in line with the targeted loss ratio as implied by the expense structure. An example is provided below.

Overall Rate Indication

A simple example

Assume all expenses are variable with premium and add to 33.3% of premium.
Earned premium and incurred losses have been "adjusted to current levels."

Accident Year	Earned Premium	Incurred Losses	Loss Ratio
2013	125,000	50,000	40.0%
2014	370,000	209,000	56.5%
2015	490,000	220,000	44.9%
2016	600,000	355,000	59.2%
2017	720,000	395,000	54.9%
Total/Average	$2,305,000	$1,229,000	53.3%

Expected and Projected Loss Ratio	53.3%
Permissible Loss Ratio (= 100.0% - 33.3%)	66.7%
Indicated Rate Change	**-20.1%**

Notes: Loss Ratio = (Incurred Losses)/(Earned Premium): -20.1% indication = 53.3%/66.7% - 1

Example of Rate Structure Change:

Assuming the book of business is equally weighted among rural dogs, rural cats, urban dogs and urban cats, the rating factors are as follows:

	Geographic Class	
Species	Rural	Urban
Dog	1.000	2.000
Cat	0.600	1.200

Average rating factor = 1.200 = (25% x 1.000) + (25% x 0.600) + (25% x 2.000) + (25% x 1.200)
Average rate = $360 = ($300 base rate) x (1.200 average rating factor)

If the loss experience in the rural category is 10% better than expected and the urban experience is 25% better than expected (overall experience 20% better than expected), then the indicated rating factors would be:

	Geographic Class	
Species	Rural	Urban
Dog	0.900	1.500
Cat	0.540	0.900

Average rating factor = 0.960 = (25% x 0.900) + (25% x 0.540) + (25% x 1.500) + (25% x 0.900)

The rural dog is intended to be the starting point in the rating system with a factor of 1.000, so all four factors need to be multiplied by 1.111 to rebase the starting point.

	Geographic Class	
Species	Rural	Urban
Dog	1.000	1.667
Cat	0.600	1.000

Average rating factor = 1.067 = (25% x 1.000) + (25% x 0.600) + (25% x 1.667) + (25% x 1.000)

The average rate started at $360 and the experience came in 20% better than expected, so the new system should have an average rate of $288 ($360 x [100% – 20%]). Because the new rate structure has an average rating factor of 1.067, the new base rate should be $270 ($288 / 1.067).

ANNUAL STATEMENT DATA

Pet insurance is a health insurance policy for a pet. This is a relatively new product to the insurance market and is regulated as P/C. Pet insurance is filed within the NAIC *Financial Annual Statement on the Exhibit of Premiums and Losses* (state page) for inland marine (line 09). This is unique to P/C because the policy is not purchased to insure an animal for purely monetary reasons. Pet owners purchase this type of insurance to protect their pet's health and help manage the cost of

veterinary bills. Coverage includes veterinary care plan insurance policies. Veterinary care plan policies provide coverage for the insured's pet in the event of illness or accident. Insurance companies report total premium for pet insurance under inland marine insurance, which may include other coverages such as travel insurance, jewelry, and other scheduled personal property. As a result, determining the exact premium volume for a product within the inland marine line is challenging. The NAPHIA provides premiums by state in its annual *State of the Market Report* for a fee. However, the information does not provide a breakdown by company, and such information would likely require a separate data call or modification to the NAIC *Financial Annual Statement*. Modification could include a separate line item on the state page specifically for pet insurance.

Although inland marine (line 09) of the state page will account for most pet insurance data, additional data may be found under farmowners multiple peril (line 03), commercial multiple-peril (line 05), and aggregate write-ins for other lines of business (line 34). Also, depending on the type of animal insured, there could be additional categories in other inland marine areas, such as livestock (line 9.0001). Finally, homeowners policies (line 04 on the state page) may include insurance coverage if a pet causes someone injury, as in a dog bite. However, homeowners insurance covers the owner's liability only and does not provide medical coverage for the insured's pet. Several exclusions, including specified dog breeds, apply.

CLAIMS PRACTICES

According to the NAPHIA's 2018 *State of the Industry Report*, approximately 1.83 million pets in the U.S. were covered by pet insurance, with 98% of those being accident and illness policies, earning insurers more than $1 billion in premiums. In a high frequency, low severity product line, how claims are handled has a significant impact on an insurer's profit, as well as its ability to attract and maintain customers.

State insurance regulators have historically identified claim practice concerns through the tracking of consumer complaints. However, this information is not readily available for pet insurance for a couple of reasons. The first reason is pet insurance is not separately identified in most state complaint databases. To remedy this lack of information, states using State Based Systems (SBS) could include a separate item in the complaints section for pet insurance. The second reason for

the lack of information regarding consumer complaints tied to pet insurance could be because consumers do not know how to file claims or which entity they should report due to the use of brand names.

The NAPHIA provided complaints data representing the number of complaints reported to the state DOI for each of its member companies. The total represents the minimum number of complaints reported, as it does not include information for all companies, nor does it consider complaints filed directly with the insurer or via any method other than those filed directly with the state DOI. According to the NAPHIA, in 2017, a total of 320 complaints were filed with a DOI. This represents a 0.0174% complaint ratio (320 complaints/1.8 million policies). Without a measurable system to track all complaints specific to pet insurance, it is difficult to determine if the low complaint volume is attributable to consumer satisfaction with the products available in the market.

To supplement the data obtained from the NAPHIA, independent research into pet insurance claim practices was conducted using available online consumer review resources such as *https://www.consumeradvocate.org*, *https://www.consumeraffairs.com*, *https://www.consumerreports.org* and the Better Business Bureau.

Online consumer reviews found on these pages suggest that complaints against pet insurers fall into categories similar to those of other P/C lines of business: claim delay, claim denial, and partial or insufficient claim payments.

Some complaints may be attributed to the consumer's misunderstanding of coverage and the policy terms and conditions. Restrictions, waiting periods, fee schedules, excluded preexisting, and congenial and hereditary conditions are often not obvious to the consumer until after they have a loss. Companies can serve their policyholders better by providing clear and understandable information regarding:

- Whether congenital and hereditary conditions (such as hip dysplasia, heart defects, cataracts or diabetes) are covered.

- How reimbursement is calculated (cased on the actual vet bill, a benefit schedule, or usual and customary rates).
- Whether the deductible is on a per-incident or annual basis.
- Whether there are limits or caps applied (per incident, per year, age, or over the pet's lifetime).
- Whether there is an annual contract that determines if anything diagnosed in the prior year of coverage would be considered a preexisting condition and excluded from coverage in subsequent policy terms.
- What conditions may be considered preexisting.
- How to appeal claim denials.
- Whether the vet is paid directly by the insurance carrier or the insured must pay the vet and be reimbursed by the carrier.

A Feb. 13, 2018, NAIC Consumer Alert[7] lists other critical details that a consumer should know, including, but not limited to:

- Can I choose any veterinarian?
- Does the policy cover annual wellness exams?
- Are prescriptions covered?
- Are spaying and neutering covered?
- How long does it take to pay a claim?
- Does the plan have end of life benefits?

California recognized the need for coverage disclosure. Assembly Bill No. 2056, which can be found in Appendix 2, requires insurers to disclose the basis or formula on which the insurer determines claim payments, the benefit schedule used, and the usual and customary fee limitation. Disclosures must be made within the policy and through a link on the main page of the insurer's website.

[7] NAIC, 2018. "Pet Insurance: It Could Save Your Pet's Life, Could Save You Money."

According to the *Los Angeles Times*,[8] a 2016 report found that 37% of all pet insurance claims were denied in California. No commensurate figure for the U.S. could be found, but one could extrapolate similar numbers. The subject of the article was a nearly $13,000 claim that was denied, appealed and denied again. It was not until the *Los Angeles Times* stepped in to do an exposé that the claim was paid.

In most cases, especially in emergency situations, the expense is incurred before the insured has an opportunity to check with the insurer regarding coverage. This is another point of contrast, with most other types of property coverage where an adjuster may conduct an appraisal before most expenses are incurred.

REGULATORY CONCERNS

Although pet insurance products have been around for many years, the demand for insurers willing to offer the coverage have increased. The regulatory framework and reporting requirements may be less familiar to the more recent entrants to the market. Development of a model to place all carriers on a level playing field may benefit insurers and consumers. State insurance regulators have identified several concerns that might be served by the development of a model act. Insurance regulation is in place to ensure consumer protection and includes requirements for licensure, reporting, policy procedures, marketing and sales. Market conduct activity is a concern for all insurance products, and the issues presented are not representative of the entire pet insurance industry.

In 2013, the Washington State Office of the Insurance Commissioner (OIC) began monitoring a pet insurer due to suspected use of non-licensed producers to market and sell its pet insurance products. The Washington OIC launched a targeted market conduct examination on July 15, 2014. The examination was conducted to address concerns regarding: failure to disclose the legal company name in operations; use of non-licensed producers to market and sell pet insurance; use of the brand name, implying that it is an insurance company; use of non-filed or approved policy

[8] Lazarus, D., 2018. "Be Ready to Fight If a Pet Insurer, Like a People Insurer, Denies a Valid Claim," Los Angeles Times, accessed at *http://www.latimes.com/business/lazarus/la-fi-lazarus-pet-insurance-denials-20180126-story.html*.

forms; and offering discounts not included in approved filings.[9] These issues are exacerbated by the use of brand names and the changing landscape of insurer to branding entity relationships.

Market Conduct Concerns

Conducting Business in Legal Insurer Name

Marketing by brand name causes confusion not only for consumers, but also for employees of the agencies, TPAs, and partners such as veterinary clinics and hospitals.

According to the *Unfair Trade Practices Act*[10] (#880), "making, publishing, disseminating, circulating or placing before the public, or causing, directly or indirectly to be made, published, disseminated, circulated, or placed before the public, in a newspaper, magazine or other publication, or in the form of a notice, circular, pamphlet, letter or poster, or over any radio or television station, or in any other way, an advertisement, announcement or statement containing any assertion, representation or statement with respect to the business of insurance or with respect to any insurer in the conduct of its insurance business, which is untrue, deceptive or misleading" is considered an unfair trade practice.

If consumers have difficulty identifying the underwriter, they may not know how to file a complaint with the state DOI. Branding entities may change underwriters or use multiple underwriters, making it difficult even for state insurance regulators to track the insurer with a duty to indemnify claims. Additionally, consumers may file complaints instead with the branding entity, agency or insurer directly. Review of various social media sites reveals a growing number of consumer complaints regarding claims handling and marketing practices. Due to confusion as to the direct underwriter, these complaints may never be effectively reported. Often, consumers have complaints regarding conditions or what is actually covered in the policy. The California bill addressed these issues by requiring insurers to provide certain disclosures, including the policy exclusions and claim reimbursement methods to policyholders, as well as post them on the

[9] *https://www.insurance.wa.gov/sites/default/files/documents/american-pet-insurance-company-exam-report.pdf*
[10] *https://www.naic.org/store/free/MDL-880.pdf?25*

insurer's website. Without proper reporting, these issues do not get addressed with the underwriting carrier. Failure to maintain a complete record of all the complaints insurers receive since the date of its last examination is considered an unfair trade practice according to Model #880.

If a model act is drafted, it should address the disclosure of the statutory insurance company to the consumer.

Use of Non-licensed Producers to Market and Sell Pet Insurance

During the Washington OIC's targeted market conduct exam, it was determined that a pet insurer used appointed agencies to market and sell its pet insurance policies. Both entities were licensed producers; although, they employed unlicensed, non-appointed call center representatives to solicit and sell policies to consumers.

Additional insurance departments have found that some pet insurance products are being marketed through unlicensed producers, including veterinarians. In some instances, veterinarians and their staff are incentivized to market specific products with potential for rewards like gift cards, products or even paid vacations. Use of non-licensed personnel for the marketing of insurance products creates a need for additional regulatory investigations and may result in insurer examination.

Form and Filing Review and Oversight

Pet insurance products are subject to Model #880 and filed with the state. Unfortunately, it has been found that some branding entities have marketed policy language and rates not filed with the state DOI. There are also concerns regarding premium waivers, unfiled discounts, and satisfaction guarantees made when products are sold. Some pet insurance branding entities offer discounts and/or coupons through online retail sites or flyers and business cards left in veterinarian offices, animal shelters and retail stores. Any discounts or coupons should be reported by the pet insurance carrier and filed with the state DOI.

Additionally, it has been found that pre-dispute arbitration clauses are being used in some pet insurance products. States may want to determine if that is appropriate for this personal line product.

As with many insurance products, consumers may not fully understand the products offered for sale to them. These policies can contain exclusions for coverage due to preexisting or congenital conditions. Treatment of preexisting conditions and how they are applied to the policy are of concern to state insurance regulators. Preexisting conditions should be thoroughly defined, including whether a condition found in one policy term would be excluded in future terms and if a relative condition could be excluded because it may have resulted from a preexisting condition. Coverage options may be added back through additional riders in some, but not all, instances. Plans may also have annual or lifetime limits for payment. The billing process varies by carrier and brand/agency/TPA. Consumers either must pay out of pocket and be reimbursed or billing software may be set up for the insurer to pay the veterinarian directly.

Lack of Pet Specific Product Data

Premium Data

States may have difficulty measuring growth in their individual markets without a known resource such as the NAIC annual statement because pet insurance does not have its own line. Pet insurance products are to be reported under inland marine, which incorporates several miscellaneous coverages. This makes it difficult to measure the pet insurance market specifically. Therefore, state insurance regulators may want to explore the determination of market share in a coordinated manner through the NAIC. As discussed above, this could be through a specific data call or modification to the NAIC annual financial statement.

Complaint Data

Complaint data may be difficult to identify for pet insurance, specifically as it is not always labeled as such in the NAIC state-based system complaint tracking database, the NAIC consumer

information source, or individual state complaint tracking resources. The lack of data regarding complaint data, specifically for pet insurance products, could be partially remedied by the modification to allow pet products to be easily identified in complaint databases. Additional concerns regarding complaints due to the use of brand names are outlined above.

Reciprocal Producer Licensing

Some states may grant a limited lines pet insurance producer license. If these producers apply to another state that does not have a limited lines pet insurance license, depending on the state reciprocity rules, the producer may be granted a full lines P/C producer license, limiting the producer to the authority provided by the resident state. For example, Idaho issues a resident limited lines producer license for pet insurance; however, Washington does not offer this limited line. In a reciprocal licensing approach, Washington would issue a non-resident producer P/C license to the Idaho resident, restricting this producer to the authority granted in Idaho. It should be noted that there is no way to reflect that this license is restricted to pet insurance, and the national licensing database as well as the Washington website will reflect the non-resident license issued as a P/C line of authority.

States should address with clarity the licensing obligations for the sale, solicitation and negotiation of this product and, if applicable in the individual state, the licensing obligations for claims adjustment. For states that permit limited line producer licenses, products will need to be filed that align with the authority permitted by the limited license. Producers will also require monitoring to make sure they are not selling homeowners or other products that exceed the limited line authority.

RESOURCES

www.naic.org/cipr_topics/topic_pet_insurance.htm

www.naic.org/documents/cmte_ex_pltf_producer_licensing_exposure_pet_insurance_presentation.pdf

https://www.aspcapetinsurance.com/research-and-compare/pet-insurance-basics/pet-insurance-basics/

APPENDICES

Appendix 1: Glossary of Terms

Chronic condition means a condition that can be treated or managed, but not cured.
Congenital anomaly or disorder means a condition that is present from birth, whether inherited or caused by the environment, which may cause or otherwise contribute to illness or disease.
Hereditary disorder means an abnormality that is genetically transmitted from parent to offspring and may cause illness or disease.
Pet insurance means an individual or group insurance policy that provides coverage for veterinary expenses.
Preexisting condition means any condition for which a veterinarian provided medical advice, the pet received treatment for, or the pet displayed signs or symptoms consistent with the stated condition prior to the effective date of a pet insurance policy or during any waiting period.
Veterinarian means an individual who holds a valid license to practice veterinary medicine from the Veterinary Medical Board pursuant to Chapter 11 of Division 2 of the Business and Professions Code or other appropriate licensing entity in the jurisdiction in which he or she practices.
Veterinary expenses means the costs associated with medical advice, diagnosis, care or treatment provided by a veterinarian, including, but not limited to, the cost of drugs prescribed by a veterinarian.
Waiting or affiliation period means the period of time specified in a pet insurance policy that is required to transpire before some or all of the coverage in the policy can begin.

Source: California Assembly Bill No. 2056, Chapter 896.

Appendix 2: California Assembly Bill No. 2056, Chapter 896

An act to add Part 9 (commencing with Section 12880) to Division 2 of, the Insurance Code, relating to insurance.

[Approved by Governor September 30, 2014. Filed with Secretary of State September 30, 2014.]

legislative counsel's digest

AB 2056, Dababneh. Insurance: pet insurance.

Existing law governs the business of insurance and authorizes the Insurance Commissioner to provide oversight over the insurance industry including, life and disability insurance, health insurance, workers' compensation, and liability insurance. The commissioner is authorized to, among other things, conduct investigations and bring enforcement actions against insurers for violations of the laws governing the business of insurance.

This bill would regulate pet insurance policies that are marketed, issued, amended, renewed, or delivered, whether in California, to a California resident, on or after July 1, 2015, regardless of the situs of the contract or master group policyholder, or the jurisdiction in which the contract was issued or delivered. The bill would define certain terms and specify certain disclosures a pet insurer is required to make to consumers. The bill would also require an insurer transacting pet insurance in this state to disclose, among other things, whether the policy excludes coverage because of a preexisting condition, a hereditary disorder, a congenital anomaly, or a chronic condition, and would require that pet insurance policies have a free look cancellation period of not less than 30 days, as provided.

This bill would authorize the commissioner to hold a hearing to determine if an insurer is in violation of the provisions governing pet insurance and to assess a civil penalty, which is to be determined by the commissioner but not to exceed $5,000 for each violation, or $10,000 for a willful violation. The hearing would be required to be conducted pursuant to the Administrative Procedure Act, except as specified, and a person found to be in violation may have the proceedings reviewed by means of any remedy pursuant to a specified statute or the Administrative Procedure Act. The bill would authorize the commissioner to adopt reasonable rules and regulations, as necessary, in accordance with the Administrative Procedure Act in order to implement these requirements.

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The people of the State of California do enact as follows:

SECTION 1. Part 9 (commencing with Section 12880) is added to Division 2 of the Insurance Code, to read:

PART 9. PET INSURANCE

12880. For purposes of this part, the following definitions shall apply:

(a) "Chronic condition" means a condition that can be treated or managed, but not cured.

(b) "Congenital anomaly or disorder" means a condition that is present from birth, whether inherited or caused by the environment, which may cause or otherwise contribute to illness or disease.

(c) "Hereditary disorder" means an abnormality that is genetically transmitted from parent to offspring and may cause illness or disease.

(d) "Pet insurance" means an individual or group insurance policy that provides coverage for veterinary expenses.

(e) "Preexisting condition" means any condition for which a veterinarian provided medical advice, the pet received treatment for, or the pet displayed signs or symptoms consistent with the stated condition prior to the effective date of a pet insurance policy or during any waiting period.

(f) "Veterinarian" means an individual who holds a valid license to practice veterinary medicine from the Veterinary Medical Board pursuant to Chapter 11 (commencing with Section 4800) of Division 2 of the Business and Professions Code or other appropriate licensing entity in the jurisdiction in which he or she practices.

(g) "Veterinary expenses" means the costs associated with medical advice, diagnosis, care, or treatment provided by a veterinarian, including, but not limited to, the cost of drugs prescribed by a veterinarian.

(h) "Waiting or affiliation period" means the period of time specified in a pet insurance policy that is required to transpire before some or all of the coverage in the policy can begin.

12880.1. A policy of pet insurance that is marketed, issued, amended, renewed, or delivered, whether or not in California, to a California resident, on or after July 1, 2015, regardless of the situs of the contract or master group policyholder, or the jurisdiction in which the contract was issued or delivered, is subject to this part.

12880.2. (a) An insurer transacting pet insurance in California shall disclose all of the following to consumers:

(1) If the policy excludes coverage due to any of the following:

(A) A preexisting condition.

(B) A hereditary disorder.

(C) A congenital anomaly or disorder.

(D) A chronic condition.

(2) If the policy includes any other exclusion, the following statement: “Other exclusions may apply. Please refer to the exclusions section of the policy for more information.”

(3) Any policy provision that limits coverage through a waiting or affiliation period, a deductible, coinsurance, or an annual or lifetime policy limit.

(4) Whether the insurer reduces coverage or increases premiums based on the insured’s claim history.

(b) (1) If a pet insurer uses any of the terms in paragraph (1) of subdivision (a) in a policy of pet insurance, the insurer shall use the definition of those terms as set forth in Section 12880 and include the definition of the term in the policy. The pet insurer shall also make that definition available through a link on the main page of the insurer’s Internet Web site.

(2) Nothing in this subdivision or Section 12880 in any way prohibits or limits the types of exclusions pet insurers may use in their policies, nor does it require pet insurers to have any of the limitations or exclusions defined in Section 12880.

(c) A pet insurer shall clearly disclose a summary description of the basis or formula on which the insurer determines claim payments under a pet insurance policy within the policy and through a link on the main page of the insurer’s Internet Web site.

(d) A pet insurer that uses a benefit schedule to determine claim payment under a pet insurance policy shall do both of the following:

(1) Clearly disclose the applicable benefit schedule in the policy.

(2) Disclose all benefit schedules used by the insurer under its pet insurance policies through a link on the main page of the insurer’s Internet Web site.

(e) A pet insurer that determines claim payments under a pet insurance policy based on usual and customary fees, or any other reimbursement limitation based on prevailing veterinary service provider charges, shall do both of the following:

(1) Include a usual and customary fee limitation provision in the policy that clearly describes the insurer’s basis for determining usual and customary fees and how that basis is applied in calculating claim payments.

(2) Disclose the insurer’s basis for determining usual and customary fees through a link on the main page of the insurer’s Internet Web site.

(f) The insurer shall create a summary of all policy provisions required in subdivisions (a) through (e), inclusive, into a separate document titled “Insurer Disclosure of Important Policy Provisions.”

(g) The insurer shall post the “Insurer Disclosure of Important Policy Provisions” document required in subdivision (f) through a link on the main page of the insurer’s Internet Web site.

(h) (1) In connection with the issuance of a new pet insurance policy, the insurer shall provide the consumer with a copy of the “Insurer Disclosure of Important Policy Provisions” document required pursuant to subdivision (f) in at least 12-point type when it delivers the policy.

(2) In addition, the pet insurance policy shall have clearly printed thereon or attached thereto a notice stating that, after receipt of the policy by the owner, the policy may be returned by the insured for cancellation by delivering it or mailing it to the insurer or to the agent through whom it was purchased.

(A) The period of time set forth by the insurer for return of the policy shall be clearly stated on the notice, and this free look period shall be not less than 30 days. The insured may return the policy to the insurer or the agent through whom the policy was purchased at any time during the free look period specified in the notice.

(B) The delivery or mailing of the policy by the insured pursuant to this paragraph shall void the policy from the beginning, and the parties shall be in the same position as if a policy or contract had not been issued.

(C) All premiums paid and any policy fee paid for the policy shall be refunded to the insured within 30 days from the date that the insurer is notified of the cancellation. However, if the insurer has paid any claim, or has advised the insured in writing that a claim will be paid, the 30-day free look right pursuant to this paragraph is inapplicable and instead the policy provisions relating to cancellation apply to any refund.

(i) The disclosures required in this section shall be in addition to any other disclosure requirements required by law or regulation.

12880.3. (a) A person who violates a provision of this part is liable to the state for a civil penalty to be determined by the commissioner, not to exceed five thousand dollars ($5,000) for each violation, or, if the violation was willful, a civil penalty not to exceed ten thousand dollars ($10,000) for each violation. The commissioner may establish the acts that constitute a distinct violation for purposes of this section. However, when the issuance, amendment, or servicing of a policy or endorsement is inadvertent, all of those acts constitute a single violation for purposes of this section.

(b) The penalty imposed by this section shall be imposed by and determined by the commissioner pursuant to Section 12880.4. The penalty imposed by this section is appealable by means of any remedy provided by Section 12940 or by Chapter 5 (commencing with Section 11500) of Part 1 of Division 3 of Title 2 of the Government Code.

12880.4. (a) Whenever the commissioner shall have reason to believe that a person has engaged or is engaging in this state in a violation of this article, and that a proceeding by the commissioner in respect thereto would be to the interest of the public, he or she shall issue and serve upon that person an order to show cause containing a statement of the charges in that respect, a statement of that person’s potential liability under this part, and a notice of a hearing thereon to be held at a time and place fixed therein, which shall not be less than 30 days after the service thereof, for the purpose of determining whether the commissioner should issue an order to that person to pay the penalty imposed by Section 12880.3 and to cease and desist those methods, acts, or practices, or any of them, that violate this article.

(b) If the charges or any of them are found to be justified, the commissioner shall issue and cause to be served upon that person an order requiring that person to pay the penalty imposed by Section 12880.3 and to cease and desist from engaging in those methods, acts, or practices found to be in violation of this part.

(c) The hearing shall be conducted in accordance with the Administrative Procedure Act (Chapter 5 (commencing with Section 11500) of Part 1 of Division 3 of Title 2 of the Government Code), except that the hearings may be conducted by an administrative law judge in the administrative law bureau when the proceedings involve a common question of law or fact with another proceeding arising under other Insurance Code sections that may be conducted by administrative law bureau administrative law judges. The commissioner and the appointed administrative law judge shall have all the powers granted under the Administrative Procedure Act.

(d) The person shall be entitled to have the proceedings and the order reviewed by means of any remedy provided by Section 12940 or by the Administrative Procedure Act.

12880.5. The commissioner may adopt reasonable rules and regulations, as are necessary to administer this part, in accordance with the rulemaking provisions of the Administrative Procedure Act (Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code).

Appendix 3: Overview of Actuarial Science

Considering the ratemaking discussion in this paper, a few words about actuarial science may be helpful.

Actuarial science is the discipline that applies mathematical and statistical methods to evaluate risk in insurance and other business endeavors. Actuaries are professionals who become experts in their field based upon years of education and experience.

Many universities have undergraduate and graduate degree programs in actuarial science. The actuarial profession is well-known for its rigorous professional examinations which must be passed to be recognized as a Fellow of the Society of Actuaries (FSA) or Fellow of the Casualty Actuarial Society (FCAS).

Actuarial science represents several interesting fields, including mathematics, probability theory, statistics, accounting, finance, economics, information technology, law and insurance.
In the U.S., there are several actuarial societies serving various functions:

- The Society of Actuaries (SOA)
- The CAS
- The American Academy of Actuaries (Academy)
- The ASB (part of the AAA)

In the P/C insurance company arena, the most common functions that an actuary serves are ratemaking (also known as pricing) and loss reserving. Ratemaking represents the estimation of future costs, and thereby needed premium, for future policies; loss reserving represents the estimation of future claims payments for policies already written by the insurance entity. Such future claims payments represent an important liability for the insurer and also play an important role in the ratemaking process because future costs are estimated based on past costs along with inflation and other adjustments.

Most P/C actuaries work for an insurance company or reinsurance company; some work for a consulting or brokerage firm; and others work for a state DOI, a college or university, a rating bureau, a modeling firm, or other type of entity.