

HOUSE BILL REPORT

HB 1670

As Reported by House Committee On:
Business & Financial Services

Title: An act relating to additional requirements for the oversight of regulated self-insurance programs by the state risk manager.

Brief Description: Addressing the regulation of self-insurance programs by the state risk manager.

Sponsors: Representatives Kirby, Bailey, Blake, Eddy, Rodne, Hurst and Springer.

Brief History:

Committee Activity:

Business & Financial Services: 2/8/11, 2/10/11, 2/11/11 [DPS].

Brief Summary of Substitute Bill

- Requires a joint self-insurance program to have an operating certificate.
- Requires operating certificates to be renewed annually.
- Provides the State Risk Manager with authority to oversee self-insurance programs.

HOUSE COMMITTEE ON BUSINESS & FINANCIAL SERVICES

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 8 members: Representatives Kirby, Chair; Kelley, Vice Chair; Bailey, Ranking Minority Member; Blake, Condotta, Hurst, Ryu and Stanford.

Minority Report: Do not pass. Signed by 5 members: Representatives Buys, Assistant Ranking Minority Member; Hudgins, Parker, Pedersen and Rivers.

Staff: Jon Hedegard (786-7127).

Background:

Self-insurance Programs.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Local government entities have the authority to:

- individually or jointly self-insure against risks;
- jointly purchase insurance or reinsurance; and
- contract for risk management, claims, and administrative services.

Subject to specified conditions, local government entities may enter into joint self-insurance programs with similar entities from other states.

A nonprofit corporation may form or join a self-insurance risk program for property and liability risks with one or more nonprofit corporations or with one or more local government entities.

Oversight.

The Risk Management Division within the Office of Financial Management is responsible for the regulation of these programs. An entity or entities proposing self-insurance must submit a plan of management and operation to the State Risk Manager (SRM) and the State Auditor (Auditor) that provides specified information. If a program is approved by the SRM, there are ongoing reporting and oversight requirements. The programs are subject to audit by the Auditor.

The SRM must charge a fee in an amount necessary to cover the costs for the initial review and approval of a self-insurance program. The actual costs of subsequent reviews and investigations must be charged to the self-insurance program being reviewed or investigated.

If the SRM determines that a self-insurance is violating the law or is operating in an unsafe financial condition, the SRM may order the program to cease and desist from the violation or practice.

Every joint self-insurance program covering liability or property risks, excluding multistate programs, must provide for the contingent liability of participants in the program if assets of the program are insufficient to cover the program's liabilities.

The SRM has rule-making authority.

The programs are excluded from the definition of "insurer" under the Insurance Code and are not subject to the provisions of the Insurance Code.

Summary of Substitute Bill:

Operating Certificate Requirement.

An operating certificate issued by the SRM is required to operate a joint local government self-insurance program covering:

- property or liability risks; or
- a health and welfare benefits program.

An operating certificate is not required for an individual self-insurance program. However, an individual health and welfare benefits program must be approved by the SRM prior to starting operations.

Any entity or entities proposing to create a joint self-insurance program must apply to the SRM for an initial operating certificate. Any joint self-insurance program currently in operation must apply for an initial operating certificate at least four months before the expiration of the program's fiscal year in 2013.

An operating certificate is subject to an annual renewal based on the joint self-insurance program's fiscal year end. Operating certificates continue in force until revoked or not renewed.

Applications and Approval.

Applications to create or to renew a joint self-insurance program must contain:

- all articles of incorporation, bylaws, or interlocal agreements;
- copies of all the insurance coverage documents;
- a description of the program structure and financial details;
- an actuarial analysis;
- a list of contractors and service providers; and
- other information required by rule of the SRM.

If the SRM finds that a joint self-insurance program has met the all applicable requirements, the SRM must issue an operating certificate. In lieu of denial, the SRM may issue a conditional operating certificate. A conditional operating certificate may not exceed one year and a consecutive conditional operating certificate may not be issued.

Denial, Refusal to Renew, and Revocation of Operating Certificates.

The SRM may deny, refuse to renew, or revoke a joint self-insurance program's operating certificate if the program:

- fails to submit an application with all required information;
- fails to meet the requirements of the chapter and rules adopted by the SRM;
- is operating in an unsafe financial condition;
- fails to comply with an order of the SRM or an operating certificate condition; or
- fails to pay its assessments and other fees.

Powers of the SRM.

The SRM may:

- bring actions to collect sums due to the state;
- review or investigate any third-party administrator of a joint self-insurance program;
- contact insurers or reinsurers to verify insurance coverage or receivables;
- contact members to verify receivables or reassessments owed by any member;
- order a program to cease and desist from a violation or practice that resulted in an unsafe financial condition;
- deny or revoke an operating certificate; and
- engage in other actions that are necessary to terminate the self-insurance program.

Review of Operations.

The SRM may review the operations, transactions, and records of any authorized joint self-insured property and liability program and any individual and joint local government self-insurance health and welfare program at any time. The SRM must review a program at least once every three years. The SRM or his or her employee must be given records or access to records. Failure to produce information within 30 days of a written request may result in the denial or revocation of an operating certificate or an order to cease and desist.

Revocation.

The SRM must give a joint self-insurance program written notice at least 30 days before a revocation is effective. The revocation decision may be appealed.

Termination of a Program.

If an operating certificate is not renewed or revoked, the SRM must terminate the operation of the joint self-insurance program. The SRM may appoint a trustee. The SRM or trustee must immediately take charge of a self-insurance program. All termination costs must be paid by the program. The SRM or trustee may:

- hire financial experts;
- hire and fire employees;
- terminate contracts;
- act on behalf of the board and the members to wind down the program;
- provide insurance options for the members to cover outstanding claims and lawsuits; and
- determine the amount of reassessments to members to cover the final costs after termination of the joint self-insurance program.

Administrative Hearings.

The Director of the Office of Financial Management (Director) or the Director's designee may hold a hearing for any purpose within the scope of this chapter. The Director must hold a hearing:

- if required by law; or
- if any person aggrieved by any act or failure of the SRM requests a hearing in writing.

Rules.

The SRM must adopt rules regarding standards for qualifications and the selection of trustees to terminate the operations of any joint self-insurance program.

Immunity.

No cause of action may arise nor may any liability be imposed against the SRM, his or her employees, authorized representatives, or appointed trustees, for statements made or conduct performed in good faith while carrying out this chapter.

Substitute Bill Compared to Original Bill:

Several language changes were made to clarify that certain provisions of the bill apply to all joint self-insurance pools. A pair of language changes were made to clarify that certain provisions of the bill only apply to joint self-insurance programs, not individual programs.

Appropriation: None.

Fiscal Note: Available.

Effective Date of Substitute Bill: The bill takes effect 90 days after adjournment of the session in which the bill is passed.

Staff Summary of Public Testimony:

(In support) The risk programs are overseen by the SRM. Local governments can pool their risk and their resources. Beginning in 2004 nonprofit organizations were allowed to participate in pools. In 2004 there were seven pools and all were local government programs. Today there are 15 programs. The SRM looks at solvency. The program members determine membership. The SRM looks at the financials of the programs to make sure that the programs can pay claims. The standard that is used is 70 percent solvency. If there are not enough assets to pay claims, a program will have to assess members to make up the deficiency. Solvency issues have occurred in recent years. The only tool that the SRM has to use is a cease and desist order. Creating an annual operating certificate would provide an additional tool to the SRM. If a program could not meet the appropriate standards, a process is created to terminate the program. It is not clear if the insolvency of a program would be handled under current law. The immunity provisions were recommended by the staff of the Attorney General. Nine programs support the bill. These programs represent local governments that believe that solvency concerns warrant higher standards of review. There was a cease and desist order last year against a program. The problems stemmed from issues several years in the past that were not detected under the current system of regulation. Many programs buy reinsurance and are concerned about how those reinsurers will view the entire group of programs if other solvency issues develop. Solvent, well-managed programs may be dragged down by programs using lesser standards. Better information should be provided and if action is necessary, it should be taken in a timely fashion. The process to develop the bill was a good process. No boards were invited. It was the program administrators who know the business that participated. The bill allows a struggling program a chance to become solvent. The actuarial standards that are used are recognized nationally. Some programs may retain more risk than others. The issue is whether or not they can cover that risk if there are claims. A better process would have prevented the need for the cease and desist action. Some programs want to make sure that best practices are being followed by all programs. The bill will not increase costs for many programs. The objection to an annual operating certificate is a surprise. Many professionals and businesses have to renew licenses on an annual basis. In reviewing the financials of a program, issues were discovered. The insurance policy that was supposed to cover certain claims did not exist and amounts listed as receivables were actually liabilities. The program was insolvent. The only tool that the SRM had to use was a cease and desist order. It will take about five years to get that program back to solvency. An annual operating certificate would have helped avoid the issue. Programs can be a great option. It is important to make sure those programs remain solvent.

(With concerns) Insurers have no position on the bill or on the existing regulation of programs. It was mentioned that the Office of the Insurance Commissioner (OIC) should be explored as a potential regulator for the programs. The OIC is funded by insurers who pay for their regulation. Insurers would be very concerned if OIC staff was diverted to the oversight of programs. If OIC regulation is contemplated, then the programs must be required to fully pay for their own regulation. The OIC's highest duty is to ensure solvency. The tools that the OIC have are significantly greater than proposed here. If there is an insurer insolvency, a guaranty fund will pay the claims of the insolvent insurer. Insurers would strongly oppose any effort to include a program in a guaranty fund. Programs are not members of a guaranty fund, are not liable for assessments, and any program insolvency should not be paid for by a guaranty fund.

(Opposed) Several programs oppose the bill. Insurance is a highly competitive arena. The programs that oppose the bill want maximum flexibility to address the issues. Not all of the programs were included in the development of the bill. There is a concern that the bill allows for over-regulation. There are cost concerns for programs under the provisions of the bill. The bill is not a good long-term answer for programs. Some programs are open to discussing a switch in regulator from the SRM to the Insurance Commissioner. That issue could be studied. It is open for all programs to work together to develop an outcome that works for all programs. Fire equipment is expensive. Years ago, members of a fire district program had a number of expensive claims. In recent years, there have been no claims at all. The current law encourages innovation. Risk is well-managed under current law. The bill will only make many programs pay more to do the same things that those programs are doing under current law. Those increased costs will be passed along to local governments and nonprofits. Programs have reinsurance for losses over a certain amount. The bill would make programs less competitive. The fact that a program must be reauthorized annually creates some unpredictability. The feasibility studies prior to the creation of a program are not taken lightly. Programs have been able to manage their risk and save millions of dollars for members. The solvency concerns are not real. No property or liability program has ever failed. Local control built the programs. This proposal takes power away from program members and gives the power to the SRM. Not all programs use the same model for risk management. The recent rule-making by the SRM did not incorporate suggestions made by some programs. Those programs did not participate in the development of the bill because they felt the SRM would not listen to their suggestions. The OFM rules strengthened reporting and solvency requirements. Those new requirements increased the costs to programs. It is not clear that more regulation is needed now. Producers may work with programs as advisers on risk management issues. Some parts of the bill create new requirements but do not reduce costs or exposure.

(Commented) The nonprofit program provides stable, affordable insurance to members. Nonprofits receive risk management and marketing services. In 2004 the insurers began to walk away from some types of risks. The law was changed to allow nonprofits to participate in programs. Programs are audited annually and are governed by members. Members must sign an agreement allowing for additional assessments if necessary. Premiums have been flat since the program was started. Additional regulation is welcome if it saves money or encourages innovation. Several principles should be used in evaluating new regulation including, a single regulator, a clear authority for actions of the regulator, the use of

insurance professionals to evaluate programs, and a fair application of standards to all programs. The proposal is less effective than current law.

Persons Testifying: (In support) David Grimm, Washington Collector's Association; Julie Murray, Office of Financial Management; Lew Leigh, Washington Cities Insurance Authority; David Hayasaka, Washington Schools Risk Management Pool; Allen Hatten, Washington State Transit Insurance Pool; and Lisa Thatcher, Thatcher Incorporated.

(With concerns) Mel Sorensen, Property Casualty Insurers Association of America.

(Opposed) Wes Crago, City of Ephrata; Wayne Senter, South Kitsap Fire and Rescue; Darren Brugman, Senior Services of Snohomish County; Larry Stuckart, Spokane Neighborhood Action Partners; Jim Lux, Washington Fire Commissioners Association; and Bill Stauffacher, Independent Insurance Agents and Brokers.

(Commented) Eric Homer, Canfield Insurance and Risk Management Specialists.

Persons Signed In To Testify But Not Testifying: None.