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REGULATE MUNICIPAL SELF-INSURANCE POOLS

House Bill 4213 as passed by the House
Second Analysis (10-9-87)

Sponsor: Rep. Mary C. Brown
Committee: Insurance

THE APPARENT PROBLEM:

Public Act 138 of 1982 allowed municipalities to collaborate in forming self-insurance pools. The law was passed after complaints by municipalities that they were unable to obtain necessary insurance coverages in the marketplace, or at least could not obtain insurance at reasonable rates. This was particularly a problem with liability coverages. The act created a means for municipal corporations (e.g. cities, counties, school districts, road commissions, public authorities) to spread their risks among themselves by creating an entity that would, in essence, act in the stead of an insurance company. Municipal self-insurance pools can provide casualty, property, automobile, surety and fidelity, and umbrella coverages, but not health care coverage. P.A. 138 specifically says, however, that self-insurance pools are not insurance companies under state law, and in carrying out their authorized activities are not conducting insurance business. This means they are not subject to the kind of regulation faced by insurance companies operating in the state. In fact, municipal self-insurance pools are virtually unregulated even though their operations give rise to the same concerns about financial stability and solvency, and rating and marketing practices, that have lead to the extensive regulation of the insurance industry. The Insurance Bureau has no official role in overseeing municipal pools, and bureau representatives have said they do not even know how many pools are operating in the state. The pools are only required to send financial statements annually to the treasury department, which complains both that the statements do not contain sufficient information for effective oversight and that the department is not equipped or authorized to provide it. (The first report to the state is thus not due until over a year after the pool has begun operations). Ultimately what lies behind a pool in the event of a financial crisis or insolvency is the taxpayer. While some might argue that the availability of taxes reduces the need for regulation, others believe that the nature of the financial risks involved in self-insurance demand that state regulators at least be informed about the existence and financial status of self-insurance pools and be empowered to act to head off financial crises.

THE CONTENT OF THE BILL:

The bill would amend Public Act 138 of 1982, which allows the formation of municipal self-insurance pools, to 1) provide for involvement by the Insurance Bureau, including disciplinary action against pools that fail to comply with financial requirements; 2) permit a reduction in the amount of aggregate excess insurance required of pools and permit a cash deposit to serve as an alternative to such insurance; 3) add penalties for misrepresentation; and 4) allow nonprofit public transportation corporations (i.e., bus companies that are not public authorities, which already qualify) to participate in pools.

Under the bill, a municipal pool would be required to file with the insurance bureau a copy of the intergovernmental contract creating the pool, a copy of each coverage document form, its aggregate excess insurance contract, the annual financial statements currently provided to the treasury department (whose role would be mostly eliminated, although they would receive from the bureau copies of the statements), and an annual certification by an independent actuary that the pool's reserves were adequate. (The bill would specify that pools must maintain cash reserves adequate to pay claims.) If a pool obtained reinsurance, a copy of the reinsurance contract or, if that were not available, other suitable documentation of coverage, would have to be provided to the insurance commissioner.

The insurance commissioner would be required to examine each municipal self-insurance pool to see if it was complying with the law. If a pool failed to comply with financial requirements, the commissioner would notify the pool (and the state treasurer), and the pool would have 30 business days to file a plan restoring compliance. Failure by the pool to file a plan would create a presumption that the pool did not meet financial requirements. If a plan was filed, the commissioner could grant a pool time to restore compliance if he or she was satisfied the pool was safe, reliable, and entitled to public confidence, and was satisfied the pool would suffer a material financial loss from an immediate conversion of its assets. If the plan was not approved, or if it was approved but the pool was not in compliance one year later, the commissioner could either grant more time or take action to suspend, revoke, or limit the pool's right to do business.

Furthermore, if the commissioner had probable cause to believe that a group self-insurance pool (or anyone else) was in violation of the governing act, he or she would, pursuant to the Administrative Procedures Act, notify the pool (or other person) in writing of the complaint and of the proceedings being contemplated. Before issuing a notice of hearing, the pool would have an opportunity to confer and discuss the complaint with the Insurance Bureau and the matter could be disposed of summarily by agreement of the parties. If a hearing was held and the commissioner determined a violation existed, he or she would reduce the findings to writing and issue a cease and desist order. The commissioner could also order payment of a fine of up to $500 per violation not to exceed $5,000 in the aggregate (or of up to $2,500 per violation with an aggregate of $25,000 in any six-month period if the pool knew or should have known it was in violation). Restitution could also be required. Further, the commissioner could suspend, limit, or revoke the pool's right to conduct business, and could order liquidation and receivership as with an insurance company. Violation of a cease and desist order could result in a civil fine of up to $10,000 per violation.

Currently, municipal self-insurance pools must carry a minimum of five million dollars of aggregate excess insurance. The bill would allow the insurance commissioner to determine that a lesser amount was adequate. Also,

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the bill would allow a pool instead to deposit $5 million (or less) in unimpaired surplus with the state treasurer or maintain some combination of aggregate excess insurance and surplus deposit.

The bill would also prohibit municipal self-insurance pools, generally speaking, from misrepresenting their policies or those of competitors. Such behavior would be a misdemeanor punishable by imprisonment for up to 90 days or by a fine of up to $100 per violation.

MCL 124.5 et al.

FISCAL IMPLICATIONS:

The Department of Licensing and Regulation, which houses the Insurance Bureau, says the bill has no budgetary or revenue implications. (9-22-87)

ARGUMENTS:

For:

The bill would provide modest but much-needed oversight of municipal self-insurance pools. The Insurance Bureau now has no regulatory powers over such pools and is not even routinely notified of their existence. Because pools operate much like insurance companies, which are extensively regulated, the public needs some assurance that pools have the financial wherewithal to pay claims. If a pool is not prepared for large losses, its members could be forced to raise taxes to pay special assessments. Most of the requirements in the bill merely involve the pools notifying the Insurance Bureau of basic information about their formation and financial status. The bureau would be authorized to take action only when financial requirements were not being met, and pools would then have the opportunity to formulate a plan of compliance. The bill would also impose restrictions on marketing similar to those that apply to insurance companies and penalize pools for misrepresenting their products and those of competitors. Many of the municipal corporations that participate in pools are not sophisticated insurance consumers, despite some claims to the contrary, and need basic protections when making what can be an enormously confusing set of decisions about insurance coverages. It should be noted that a great many requirements imposed on insurance companies as to capitalization, rates, reserves, policy forms, etc., would still not apply to municipal pools.

For:

The bill would authorize some bus companies that were formed as non-profit corporations to participate in self-insurance pools along with public transportation authorities, which they closely resemble.

Against:

There are fears that increased regulation will make it more difficult for pools to provide municipal corporations with essential coverages. It must be remembered that the pools have grown so dramatically because municipalities could not get coverage from insurance companies or, at least, could not afford what was available. Pools are an alternative to being uninsured, which certainly poses far more serious risks to small municipalities and public authorities than do self-insurance pools. Some people also object to the $5 million aggregate excess insurance requirement.

Response: The $5 million aggregate excess coverage requirement was part of the original enabling legislation for pools. The bill would allow a lower amount with the approval of the insurance commissioner and permit alternative methods of meeting the requirement (putting up a cash deposit). Most of the people involved in operating the self-insurance pools consider the substitute bill useful and beneficial.

POSITIONS:

The Department of Licensing and Regulation supports the bill. (9-22-87)

The Department of Treasury supports the bill. (6-9-87)

The Michigan Municipal League supports the substitute. (9-25-87)

The Michigan Liability and Property Pool (an MML affiliate) supports the bill. (9-25-87)

The Michigan Townships Association supports the bill. (9-25-87)

The County Road Association of Michigan supports the bill. (9-25-87)

The Independent Insurance Agents of Michigan supports the bill. (9-25-87)

SET/SEG Inc. (school boards-affiliated organization) supports the bill. (9-22-87)