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BILL ANALYSIS

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Senate Fiscal Agency

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**Senate Bills 110 through 114 (as passed by the Senate)**

Sponsor: Senator Rudy Nichols

Committee: Human Resources and Senior Citizens

Date Completed: 3-24-87

**RATIONALE**

Public Act 10 of 1912 first provided for an accident fund as part of Michigan's original workers' compensation Act. Because workers' compensation was then in its infancy and many casualty companies were reluctant to enter the field, in order to increase the availability of workers' compensation insurance the Legislature provided that five or more employers could request the Insurance Commissioner to establish a fund, which was to be created within the State Treasury. The Fund was later incorporated under the Worker's Disability Compensation Act of 1969, which provides for a 15-member advisory board of employer-members to "advise the Commissioner regarding the means and methods of administering the affairs of the Accident Fund".

Reportedly, despite the fact that the Act describes the board as "advisory" and provides for the Fund to be under the supervision of the Insurance Commissioner, the board historically has managed the Fund with little involvement of the Commissioner. And, despite its statutory creation, the Fund is considered by many to be an autonomous entity. A 1976 Attorney General opinion, however, held that the Fund is a State agency and that the Fund's employees are employees of the State. Further, in the last few years a number of actions were taken by the Executive branch which are viewed by some as an attempt to assert State control over the Fund and its surplus of \$140-\$160 million.

As a result of these activities, the Fund initiated a lawsuit in Federal court in 1981. The Federal judge ruled that the court did not have jurisdiction, and the Fund and the State have agreed only that the assets of the Fund are trust funds. More recently, the State sued in Ingham County Circuit Court to enjoin the Fund's rate hike in May 1986. The judge ruled that the Insurance Commissioner is the administrator of the Fund, and that ruling is pending appeal. Meanwhile, the Fund raised its rates again last January, and the parties will be back before the court in May. In order to resolve the legal status of the Fund once and for all, many persons believe that legislation is needed to provide for the Fund's reorganization as an independent entity separate from the State.

**CONTENT**

Senate Bill 110 would add a new chapter to the Insurance Code to recreate under the code the Accident Fund that is currently organized under Chapter 7 of the Worker's Disability Compensation Act. The bill would repeal Chapter 7 of the workers' compensation Act and do the following:

- Specify that the Fund under the Insurance Code would be an independent membership organization, separate and distinct from the State.
- Authorize the Fund to provide workers' compensation insurance.

- Provide for the administration of the Fund by a governing board.
- Propose various provisions similar to existing provisions under the workers' compensation Act, including those pertaining to the determination of premiums, resolution of controversies, record-keeping and inspection of books and records, and payments to employees of member employers.
- Revise existing Insurance Code provisions that pertain to competition in the workers' compensation insurance market.

Senate Bill 111 would amend the State Insurance Act to require the State to provide for workers' compensation benefits for State employees by one of the methods described in the Worker's Disability Compensation Act, and to delete references to the Accident Fund. Senate Bill 112 would amend Public Act 71 of 1919, which establishes the duties of the Auditor General, to delete reference to the State Accident Fund. Senate Bill 113 would amend the Michigan Occupational Safety and Health Act to replace references to the "State Accident Fund" with references to the "Accident Fund". Senate Bill 114 would amend the State Employees Retirement Act to delete a reference to employees of the State Accident Fund.

All of the bills would take effect on May 1, 1987, and are tie-barred to each other and to Senate Bill 67, which would amend the Worker's Disability Compensation Act.

Senate Bill 110Fund Creation and Management

The bill provides that the Accident Fund created under the Worker's Disability Compensation Act would be the Accident Fund under the proposed chapter, and would have all the rights, liabilities, and duties provided for in the Insurance Code. The bill specifies that the Accident Fund would be an independent membership organization, separate and distinct from the State, and that the Fund would be neither an agency nor an instrumentality of the State. Except as provided in the proposed chapter, the Fund would be subject to the Insurance Code, and any other laws of the State and the rules promulgated by the Insurance Commissioner that pertain to domestic mutual insurers authorized to transact the business of insurance in this State. The Fund would be vested with the corporate powers provided by the Code and other applicable State laws. Member employees of the Accident Fund created under the Worker's Disability Compensation Act would become members of the Accident Fund organized under the new Insurance Code chapter.

The business of the Fund would have to be managed by its governing board. An annual meeting of the member employers would have to be called by the board chairperson in Lansing each October. Notice of the meeting would have to be sent by first class mail at least 10 days

S.B. 110-114 (3-24-87)

before the meeting. At the meeting, the members would have to nominate and elect 15 members to constitute a governing board, who would serve for one calendar year. If a vacancy occurred on the board, the remaining members could appoint a member to fill the vacancy pending the next annual meeting. The board would have to elect one member as chairperson and four who, with the chairperson, would constitute an executive committee.

The books, records, and payrolls of each member employer always would have to be open to inspection by the Fund or its agent for the purpose of ascertaining the correctness of the amount of the payroll reported, the number of persons employed, and other information required for administering the Fund. The Fund itself would have to keep complete records of all business transacted by it. The Fund also would have to give the Commissioner an annual statement concerning its affairs. The Fund could employ necessary personnel as authorized by the governing board. In any administrative or judicial proceeding, such personnel would be conclusively presumed not to be in State service.

Assets of the Fund would accrue to the benefit of the member employers. The Fund would be required to maintain facilities necessary for its operations and could acquire and hold real estate according to the State insurance laws.

#### Workers' Compensation Insurance

The Accident Fund could provide workers' compensation insurance, and employers' liability insurance for employers written in connection with workers' compensation insurance, including longshoremen's and harbor worker's compensation insurance, as required. Subject to the requirements of Chapter 6 of the workers' compensation Act (which requires employers subject to the Act to secure the payment of compensation by specific methods), the Accident Fund could engage in the business of servicing any approved workers' compensation self-insurance program for an individual or group of employers. Membership in and coverage by the Fund could be provided to employers who requested membership and coverage in writing and whose risk was insurable and ratable according to generally accepted underwriting practices and rating procedures.

The bill provides that the Fund would qualify for a certificate of authority to transact insurance in this State and would be subject to the provisions of the Insurance Code in the same manner as a domestic mutual insurer authorized to transact all kinds of insurance as defined in Chapter 6, except life insurance. (Chapter 6 provides for disability, life, property, marine, inland navigation and transportation, automobile, casualty, and surety and fidelity insurance.)

The Fund would be permitted to reinsure its catastrophic risks with authorized insurers, and it would have to be a member of the Property and Casualty Insurance Association. It also could secure membership in other insurance organizations and in an advisory or statistical organization.

Every member employer would have to be furnished with a policy showing the period the insurance was effective. The period would have to be for one year or more, although a shorter period could be specified pursuant to a mutually agreed upon anniversary date. A policy would have to contain a cancellation provision describing the conditions, terms, and procedures under which the Fund or the member employer could cancel the policy. The cancellation provision would have to conform to the requirements of the Insurance Code and Chapter 6 of the workers' compensation Act.

All payments from the Fund to or for employees of member employers would have to be made pursuant to the workers' compensation Act and the governing rules of the Bureau of Workmen's Disability Compensation.

#### Premiums

The Fund would be required to levy and collect from member employers premiums established according to Chapter 24 of the Code. The Fund also would have to determine and collect fees for specific and apportioned expenses of administration relevant to servicing approved workers' compensation self-insurance programs.

The Fund would be required to determine the amount of the premiums that an employer had to pay to the Fund and prescribe when and how the premiums would be paid. The Fund also could change the amount of premiums with respect to an employer as circumstances required and the condition of the employer's plants, establishments, or workplaces with respect to workers' safety necessitated. Insurance rates, rating systems, and plans and practices used to determine premiums would have to be determined in accordance with Chapter 24 of the Code and any other applicable State laws.

Any controversy between the Fund and a member employer would be subject to review provided by section 2419 of the code and the law regarding controversies arising between insurers and insured employers. (Section 2419 provides for a meeting between a management representative of the insurer and an insured who believes premiums are excessive because of unreasonable reserves or the unreasonable redemption of a claim, and for a determination by the Commissioner if the dispute remains unresolved.) A controversy between the Fund and a claimant for benefits would have to be determined under the workers' compensation Act and any other applicable laws.

#### Transfer of Assets/Liquidation

All or a portion of the assets and obligations of the Fund could be transferred to any other insurer by the governing board subject to review and approval by the Insurance Commissioner. The Commissioner could not approve the transfer unless the transfer would be considered within the purposes of the proposed chapter and the assets to be transferred were reasonably related to the obligations to be assumed. The Commissioner could attach reasonable and necessary conditions to a transfer, binding on both the transferee and the transferor, including conditions that would do the following:

- Assure continued workers' compensation insurance coverage at a reasonable price for eligible employers.
- Require the insurer to guarantee, assume, or reinsure, or cause to be guaranteed, assumed, or reinsured all contracts and policies of the Fund.
- Assure the termination of all obligations of the Fund.

Any proceedings for the liquidation of the Fund or for appointment of a receiver would have to comply with the Insurance Code and any other applicable State laws.

#### Other Provisions

The bill provides that the Commissioner would order the Michigan Worker's Compensation Placement Facility, rather than the State Accident Fund, to develop mechanisms to create competition or availability where it does not exist.

For purposes of the annual report on competition in the workers' compensation insurance market, the Commissioner must consider the extent to which any insurer controls the market; with respect to statewide competition, an insurer is not considered to control unless it has more than 15% of the market. The bill would delete the exception to this provision for the State Accident Fund. The

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Commissioner also must consider whether the total number of companies writing workers' compensation insurance in the State is sufficient to provide multiple options to employers; the bill would include the Accident Fund among those companies.

MCL 500.2409 et al.

#### Senate Bill 111

The bill would amend the Act under which the State is required to obtain certain insurance, to require that the Department of Management and Budget provide for workers' compensation benefits for State employees by one of the methods described under the Worker's Disability Compensation Act (MCL 418.611). Those methods include:

- Receiving authorization to be a self-insurer from the Director of the Bureau of Workmen's Compensation.
- Insuring against liability with an authorized insurer.
- Insuring against liability with the Accident Fund.

The bill also would delete provisions that require the State Accident Fund annually to determine the premium necessary to pay benefits under the State Accident Fund Act to persons in State service, and require that amount to be credited by the State Treasurer to the Fund.

MCL 550.706

#### Senate Bill 112

The bill would amend Public Act 71 of 1919 to delete the requirement that the Auditor General review the audit of the State Accident Fund that was performed by the Insurance [Commissioner].

MCL 21.45

#### Senate Bill 113

The Michigan Occupational Safety and Health Act creates a safety education and training Fund and requires assessments from insurance carriers licensed to do workers' disability compensation business, from each self-insured employer, and from the State Accident Fund. The bill would require assessments from the Accident Fund, instead of the State Accident Fund.

MCL 408.1055

#### Senate Bill 114

The bill would amend the State Employees Retirement Act to delete the provision under which an employee of the State Accident Fund may become a member of the retirement system.

MCL 38.13

### **BACKGROUND**

The Worker's Disability Compensation Act provides that:

An accident fund is created . . . under the supervision of the Commissioner of Insurance . . . Upon compliance with the rules concerning insurance . . . membership in and coverage by the fund shall be provided to employers who request such membership and coverage of the fund in writing. Thereupon the accident fund shall assume charge of levying and collecting from employers such premiums or assessments as may be necessary . . . Neither the Commissioner nor the state shall be liable or responsible for the payment of claims . . . beyond the extent of the sums so collected and received.

### **FISCAL IMPACT**

Senate Bills 110 and 111 would have no fiscal impact on the State because the budget for the State Accident Fund

is not appropriated. The bill would have no fiscal impact on local government.

Senate Bill 112 would result in a small cost savings for the State by removing the requirement that the Auditor General review the audit of the Accident Fund by the Insurance Bureau. The bill would have no fiscal impact on local government.

Senate Bill 113 would have no fiscal impact on State or local government.

Senate Bill 114 would have no fiscal impact on the State because the State Accident Fund is not an item budgeted in appropriations legislation. It would be necessary for the State Employees' Retirement System to separate the assets for Accident Fund employees who have vested rights to retirement and provide accounting for employees who currently are members. There would be no fiscal implications for local governments.

### **ARGUMENTS**

#### **Supporting Argument**

By protecting the Fund and its assets from a takeover by the State, Senate Bill 110 would, in fact, merely reaffirm the status quo of the Fund as an independent entity. Historically, the Fund has been run by the advisory board and is required by statute to be self-supporting. The Insurance Commissioner was given only initial authority to supervise the Fund, and the Commissioner's supervisory authority today is merely nominal. Not only did the State provide no money for the Fund's creation, but it was expressly absolved of any liability for the Fund. The solvency and efficiency of the Fund have always been the responsibility of the policyholders through the advisory board. The board hires its employees and determines their salaries and benefits, and the Fund owns its own building and parking lot.

The Insurance Code recognizes the Fund as an insurer and prohibits the Insurance Commissioner from being a stockholder in, or directly or indirectly connected with the management and affairs of any insurer. Although the Commissioner cannot both run and regulate the Fund, that is exactly what has been attempted by the administration's actions in the last few years. Among those actions were an order to reduce rates by 17%, the installation of a deputy Insurance Commissioner as overseer of the Fund, an attempt to cut off payments to the Fund's lobbyists and attorneys, a threat to fire the Fund's manager, and an attempt to rescind the authority of the Fund's comptroller to sign checks. More recently, the Commissioner has sought an injunction against the Fund's rate hikes. While it may be questionable whether the State should be in the insurance business at all, it is certain that the State should not be allowed to run private insurers out of Michigan and create a monopoly as the sole provider of workers' compensation insurance in this State.

#### **Supporting Argument**

In recent years, insurance agents have become reluctant to place business with the Accident Fund. In the late 1970's, when compensation loss ratios had soared and private insurers began withdrawing from Michigan, the Fund moved into the number one position in terms of employers insured and volume of premiums. The Insurance Commissioner claimed that the Fund did not have enough surplus for the volume it was writing, and advised a 10% cut in commissions and dividends. The advisory board agreed, which angered agents and policyholders. The Commissioner then approved higher rates and business began moving out of the Fund. Now, although the Fund has since increased commissions and dividends, agents

and policyholders remain suspicious, in part because State-run companies tend not to become or remain solvent.

### ***Opposing Argument***

The Accident Fund is and always has been a State agency. It was authorized by State legislation and created within the State Treasury. The State is responsible for the receipt and disbursement of Fund money, and the Insurance Commissioner has the authority to decide whether it is necessary to dissolve the Fund. A duty is imposed on the Commissioner to promulgate rules regulating the qualifications of employers to become members and to determine and collect premiums and assessments. Employees of the Fund are required to be members of the State Employees Retirement System. Unpaid premiums and assessments, and penalties for the failure to submit records for inspection, are to be collected in an action brought in the name of the State as plaintiff. Moreover, the Fund fulfills a statutorily mandated public purpose of providing workers' compensation insurance coverage to employers within the State. Finally, it has recently been judicially reaffirmed that the Insurance Commissioner is the administrator of the Fund.

### ***Opposing Argument***

The only beneficiary under the bills would be the cartel of insurers that manipulated rates until 1983. By eliminating one of the most important checks on workers' compensation costs, the bills would pave the way for higher rates. The propensity of the Fund itself to hike its rates has been demonstrated amply by the Fund's attempt to increase rates by a total of 49% in the past year. While those rate hikes are being litigated, the Fund nevertheless claims that it wants to disburse some 33% of its surplus to its policyholders. Should the fund be declared to be a private insurer, however, as it contends it is, the amount of tax liability that would then accrue to the Fund could wipe out both its surplus and its reserves.

**Response:** The Fund's rate increase may promote competition within the workers' compensation insurance market and mitigate the Fund's monopoly of the industry.

### ***Opposing Argument***

If the Fund is found to be a private entity, it should be required to repay the State for much of the administrative fees paid over the years by the State to the Fund. Legislation passed in 1976 (and later found unconstitutional on other grounds) would have restricted the fee to 17% of the amount paid in claims on the State's behalf. For decades, however, the Fund had been charging the State 38.5%. Thus, for many years, the State in effect was subsidizing all of the private employers insured by the Fund, and should be repaid.

### ***Opposing Argument***

The insurance industry is presently going through a tightening-up period, and many entities — from bars to barbers — have had trouble obtaining workers' compensation insurance. It's reassuring to know that the Fund is available to write policies for these companies, and that it is big enough to grow. This availability in the marketplace is essential and must be maintained.

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