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TO THE SENATE COMMITTEE ON WAYS AND MEANS

TWENTY-FOURTH LEGISLATURE
Regular Session of 2008

Friday, February 22, 2008
11:00 a.m.

WRITTEN TESTIMONY ONLY

TESTIMONY ON SENATE BILL NO. 3011, S.D. 1 – RELATING TO INSURANCE.

TO THE HONORABLE ROSALYN BAKER, CHAIR, AND MEMBERS OF THE
COMMITTEE:

My name is J. P. Schmidt, State Insurance Commissioner (“Commissioner”), testifying on behalf of the Department of Commerce and Consumer Affairs (“Department”). The Department strongly supports this Administration bill, with two suggested amendments to this version of the bill.

The purpose of this bill is to amend the formula used to determine the assessment amount to the compliance resolution fund (“CRF”) that should be made by insurers regulated under the Insurance Code. This version of the bill has a defective effective date of July 1, 2050.

The CRF is used to fund, among other things, the operations of the Insurance Division. Amended by Act 1, Special Session Laws of 2005 (“Act 1”), the current formula in HRS § 431:2-215(d) authorizes the Commissioner to assess insurers to the extent the proposed fiscal year budget exceeds the cash balance at the end of the prior fiscal year after deducting other anticipated revenues. This entails that the Insurance Division manage its budget to achieve zero funds in reserve at the end of the fiscal

year. The current statute also requires a minimum 60-day notice to insurers of the Commissioner's intent to levy an assessment.

Although the fiscal year closes on June 30, the prior fiscal year's ending cash balance is not known until a few months later, after allowing for fourth quarter encumbrances and closing of the books by the Department of Accounting and General Services.

Under the current formula, the likelihood of a cash shortfall in the first quarter of the fiscal year is an annual certainty, given the 60-day notice requirement and the closing which usually takes up to two months.

In the late 1990s and early years of this decade, assessments were increased significantly resulting in a large reserve, which the Legislature then transferred to the general fund. Act 1 was enacted in 2005 to provide reasonable limits on assessments and to prevent transfer of funds intended for the regulation of insurance to the general fund.

In 2003, the Insurance Division began reducing the reserves by cutting assessments by 60%. In 2004 and 2005, no assessments were made. An assessment was made in Fall 2006 for FY 2007, in accordance with the new formula in Act 1. In FY 2008, the Insurance Division has not made an assessment. The projected cash balance on June 30, 2008 is \$259,361. The Insurance Division is closing out contracts and looking at services and expenditures that can be delayed in order to have sufficient funds on June 30 so that we can continue operations on July 1, 2008.

It is impossible for the Insurance Division to continue operations if it is unable to assess until there is a zero cash balance on June 30. The Insurance Division requires cash on hand on July 1 of the next fiscal year to fund payroll and on-going expenses.

Basing the assessment calculation on 125% of the proposed fiscal budget will allow for sufficient reserve to fund operational needs during the first quarter of the fiscal year. This will provide funds for continued operation of the Insurance Division until fees and assessments for the new fiscal year are received. This also maintains a reasonable safeguard to prevent large increases in assessments or transfers of assessment funds for other purposes.

Without this adjustment to recognize government accounting and budget requirements, the Insurance Division will continually head into the end of each fiscal year with funds approaching zero, creating an untenable situation for the Insurance Division's operation.

In the alternative, the Department suggests amending the statute to allow the assessments based on the "projected" balance in the Insurance Division's sub-account, as a means to avoid the timing problem we currently have. Under this alternative, the Department respectfully requests adding the word "projected" in subparagraph (A) such that page 2, line 16 in section 2 of the bill, reads as follows:

(A) Less projected funds in the insurance regulation

The Department also respectfully requests amending the effective date on page 3, line 14 in section 4 of the bill such that this bill is effective "upon approval".

We thank this Committee for the opportunity to present testimony on this matter and ask for your favorable consideration.



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Alison Powers
Executive Director

TESTIMONY OF ALISON POWERS

SENATE COMMITTEE ON WAYS AND MEANS
Senator Rosalyn H. Baker, Chair
Senator Shan S. Tsutsui, Vice Chair

Friday, February 22, 2008
11:00 a.m.

SB 3011, SD1

Chair Baker, Vice Chair Tsutsui, and members of the committee, my name is Alison Powers, Executive Director of Hawaii Insurers Council. Hawaii Insurers Council is a non-profit trade association of property and casualty insurance companies licensed to do business in Hawaii. Member companies underwrite approximately 60% of all property and casualty insurance premiums in the state.

Hawaii Insurers Council **opposes** SB 3011, SD1. This bill allows the Insurance Commissioner to assess the insurance industry 25% more than the insurance division's budget ceiling approved by the Legislature.

The insurance sub-account, which is part of the Compliance Resolution Fund, is 100% funded by the insurance industry for the purpose of its own regulation.

In 2006, Hawaii Insurers Council won in Circuit Court its lawsuit filed in 2004 against the State. In relevant part, on Count IX of the Declaratory Judgment, granting in part Hawaii Insurers Council's motion for summary judgment, the Court stated "the methods of calculation and amounts of at least a portion of the insurance division's assessments,

including those related to reserve margins, overhead of the DCCA and overhead of the DBF [Department of Budget and Finance], run afoul of the requirements of *Medeiros*¹.”

In addition to the Declaratory Judgment from First Circuit Court, Judge Ahn went further and issued a stay as requested by the State so as not to change the status quo. In her order dated January 23, 2006, she outlined certain requirements of the Insurance Division pending this case's appeal. In relevant part, the Judge required the Insurance Division to “inform the Plaintiff (Hawaii Insurers Council) thirty days prior to any future assessment of:

- a. The amount in the insurance regulation sub-account of the Compliance Resolution Fund on June 30th of the prior fiscal year;
- b. How much money they project to receive for the insurance sub-account of the Compliance Resolution Fund from non-assessment sources for the fiscal year of that assessment; and
- c. What the Insurance Division proposes its budget to be for the fiscal year of that assessment.”

SB 3011, SD1 clearly violates the spirit of the Judge's order in that requiring an accounting to the Hawaii Insurers Council by the Insurance Division is to ensure the assessments in their aggregate are not excessive.

This bill also attempts to overturn Count IX of the Declaratory Judgment, which says in part that the Insurance Division's assessments for reserves runs afoul of the *Medeiros* case.

This bill usurps the Legislature's authority to approve the budget ceiling, lends itself further to abuse, and violates Judge Ahn's order while this case is pending a decision by the Intermediate Court of Appeals. In addition, we are awaiting the State Auditor's

¹ *State v. Medeiros*, 89 Hawaii 361, 973 P.2d 736 (1999). Under *Medeiros*, the assessment must (1) apply to the direct beneficiary of a particular service, (2) be allocated directly to defraying the costs of providing the service, and (3) be reasonably proportionate to the benefit received. The Circuit Court ruled that the Insurance Division's assessment did not meet this test.

report, mandated by Act 1, SSLH 2005, which requires the Auditor to conduct a financial and management audit of the insurance regulation sub-account of the Compliance Resolution Fund. This audit report was due prior to the convening of the 2008 legislative session.

Therefore, we ask that this bill be held.

Thank you for the opportunity to testify.



**Property Casualty Insurers
Association of America**

Shaping the Future of American Insurance

1415 L Street, Suite 670, Sacramento, CA 95814-3972

To: The Honorable Rosalyn H. Baker, Chair
Senate Ways and Means Committee

From: Samuel Sorich, Vice President

RE: **SB 3011 SD1 – Relating to Insurance**
PCI Position: Oppose

Date: Friday, February 22, 2008
11:00 a.m.; Conference Room 211

The Property Casualty Insurers Association of America (PCI) is an association of property/casualty insurers. There are more than 100 PCI member companies doing business in Hawaii. PCI members are responsible for approximately 45 percent of the property/casualty insurance premiums written in Hawaii.

PCI opposes SB 3011 SD1 because the bill is unfair and unnecessary.

Insurers pay annual assessments to fund the regulation and administration of the insurance division. Insurance companies support sound, effective insurance regulation. Insurers have no objection to paying fair assessments so that the insurance commissioner has the resources he needs carry out his regulatory responsibilities.

The fundamental problem with SB 3011 SD1 is that it would impose assessments that are unfair. By its very terms, SB 3011 SD1 would mandate assessments that are 25 percent greater than what the insurance commissioner determines are the division's budgetary needs. As such, SB 3011 SD1 seeks to raise revenue in excess of what is determined to be reasonable expenses of the division and the proposed assessment is not allocated directly to defraying costs of providing the service and is not reasonably proportionate to the benefit received. See State v. Medeiros, 89 Haw. 361, 973 P.2d 736 (1999).

SB 3011 SD1 is not a temporary measure. The statutory change proposed by the bill would permanently force insurers to pay assessments that are recognized to be 25 percent in excess of the funds needed to operate the insurance division. These excess funds would be part of the Compliance Resolution Fund which is available to support state activities unrelated to insurance regulation. This would create an injustice imposed on insurers and insurance consumers. Insurers, and

ultimately their customers, would be forced to pay, in the guise of insurance regulatory assessments, money that is diverted from any legitimate insurance purpose.

SB 3011 SD1 is unnecessary. Concerns have been raised that the bill is needed because the 60-day notice requirement for assessments could create a cash flow problem for the insurance division. Those concerns are satisfied by the division's existing authority to obtain temporary funding from the Compliance Resolution Fund. There is no justification to address a potential temporary cash flow problem with a permanent statutory change that on its face is excessive and unfair.

PCI requests that the Committee vote No on the bill.

**SENATE COMMITTEE ON
WAYS AND MEANS**

February 22, 2008

Senate Bill 3011, SD 1 Relating to Insurance

Chair Baker and members of the Senate Committee on Ways and Means, I am Rick Tsujimura, representing State Farm Insurance Companies, a mutual company owned by its policyholders.

State Farm supports the intent of Senate Bill 3011, SD 1 Relating to Insurance and the Insurance Division's need for funds to operate the Division. We recommend that the committee keep this measure alive by defecting the date to allow continued dialogue between the industry and the Division on the level of funds necessary to adequately and sufficiently run the Division.

Thank you for the opportunity to present this testimony.

TESTIMONY OF THE AMERICAN COUNCIL OF LIFE INSURERS
COMMENTING ON S.B. 3011, S.D. 1, RELATING TO INSURANCE

February 22, 2008

Via E Mail: testimony@capitol.hawaii.gov

Senator Rosalyn H. Baker, Chair
Committee on Ways and Means
State Senate
Hawaii State Capital, Conference Room 211
415 S. Beretania Street
Honolulu, HI 96813

Dear Chair Baker and Committee Members:

Thank you for the opportunity to comment on S.B. 3011, S.D. 1, relating to Life Insurance.

Our firm represents the American Council of Life Insurers ("ACLI"), a national trade association whose three hundred fifty-three (353) member companies account for 93% of the life insurance premiums and 94% of the annuity considerations in the United States among legal reserve life insurance companies. ACLI member company assets account for 93% of legal reserve company total assets. Two hundred sixty-one (261) ACLI member companies currently do business in the State of Hawaii.

ACLI is in the process of reviewing S.B. 3011, S.D. 1, with its member companies and may offer testimony on the bill in the future

Again, thank you for the opportunity to comment on S.B. 3011.

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