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Testimony of the Department of Commerce and Consumer Affairs

**Before the
House Committee on Intrastate Commerce
Tuesday, February 12, 2019
9:45 a.m.
State Capitol, Conference Room 430**

**On the following measures:
H.B. 1127, RELATING TO THE DEPARTMENT
OF COMMERCE AND CONSUMER AFFAIRS
and
H.B. 1332, RELATING TO THE BUDGET OF THE
DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS**

Chair Ohno and Members of the Committee:

My name is Catherine Awakuni Colón, and I am the Director of the Department of Commerce and Consumer Affairs (DCCA or Department). The Department supports H.B. 1127, which appropriates funds for the fiscal biennium (FB) 2019-2021 operating budget of the DCCA's Insurance Regulatory Services (INS or Division), program ID CCA-106, under the purview of this committee. The Department also supports H.B. 1332, which establishes additional amounts to be appropriated or authorized for the FB 2019-2021 operating budget of the INS.

Functions

The INS is responsible for overseeing the State's insurance industry, which includes insurance companies, insurance agents, self-insurers, and captives. The INS

ensures that commercial and individual consumers are provided with insurance services that meet acceptable standards of quality, equity, and dependability at fair rates by establishing and enforcing appropriate service standards and by monitoring the solvency of insurers. The INS licenses, supervises, and regulates all insurance transactions in the State under HRS title 24 (Insurance Code). Legal Service Plans also fall within the INS' regulatory oversight.

Sources of Revenue

The INS is primarily funded by company and producer license fees, captive insurance premium taxes, an annual Compliance Resolution Fund assessment of insurers, reimbursement of examination costs, and multi-state settlements and fines. Premium taxes of \$160 million collected by the INS are deposited into the general fund and not used by the INS for regulatory purposes.

Non-General Fund Balances

- **Drivers Education Fund (S-309):** \$430,332 balance as of 6/30/18. An annual fee is paid by insurers and self-insurers for each vehicle, motorcycle, and motor scooter insured. All collected revenues are disbursed to the Judiciary, Department of Education (DOE), and Department of Transportation (DOT). Judiciary's funds are expended for the operation of the drivers' education program. DOE's funds support drivers' education for high school students. The DOT uses its funds to operate a drivers' education program for operators of motorcycles, motor scooters, or similar vehicles.
- **Compliance Resolution Fund – Insurance Regulation Fund (S-313):** \$3,964,565 balance as of 6/30/18. Used to defray any administrative costs associated with INS programs, including personnel costs and costs incurred by supporting offices and divisions.
- **Captive Insurance Administrative Fund (S-317):** \$7,632,751 balance as of 6/30/18. Used to license, monitor, regulate, and develop captive insurance companies, and to promote Hawaii as a captive insurance domicile pursuant to HRS chapter 431, article 19, including defraying any administrative costs, employment, or retention of hearings officers, attorneys, investigators,

accountants, examiners, and other necessary professional, technical, and support personnel.

- **Grants to States for Health Insurance Premium Rate Review Cycle II (S-205):** \$3.0 million federal grant used to enhance the current capacity to review and, to the extent permitted by state law, approve or deny rate increases in individual and group health insurance markets. This grant ended on 9/30/18.
- **Planning/Implementing the Insurance Market Reforms, Part A, Title XXVI, Public Health Service Act – Cycle I (S-501):** \$1.2 million federal grant to contract with consultants and hire market reform personnel. The period of this grant is 10/31/16 to 10/31/19.
- **Premium Taxes Paid Pending Appeal (T-916):** \$1,905,274 balance as of 6/30/18. This trust account holds premium taxes paid in protest against denials of high-tech tax credits.
- **Commissioner’s Education and Training Fund (T-917):** \$1,388,284 balance as of 6/30/18. The fees are collected from rate and form filings to reimburse staff and personnel for various education and training expenses, including insurance and computer courses, conferences, and seminars. This fund is used to publish the annual Report of the Insurance Commissioner, present insurance information to Hawaii consumers, and purchase books and periodicals for staff education and training.
- **Service Contract Provider’s Financial Security Deposits (T-927):** \$50,000 balance as of 6/30/18. This trust account holds financial security deposits placed in trust with the Insurance Commissioner by service contract providers for all service contracts issued and in force in this state.
- **Captive Insurance Companies Letters of Credit Escrow (T-931):** \$526 balance as of 6/30/18. The Insurance Commissioner may draw upon the letters of credit when the captive licensee does not comply with HRS chapter 431, article 19. The cash drawn from the letters of credit is used to cover

liabilities and other obligations of the captive licensee, including policyholder claims, operating expenses, taxes, fees, and fines.

Base Budget for Fiscal Year (FY) 2019

The INS' base budget for FY 2019 is \$19,780,768. This includes special funds of \$18,119,862, trust funds of \$200,000, and federal funds of \$1,460,906. The following is a breakdown of the INS' special fund budget:

- Drivers Education Fund (S-309) - \$3,600,000
- Compliance Regulation Fund - Insurance Regulation Fund (S-313) - \$11,675,781
- Captive Insurance Administrative Fund (S-317) - \$2,844,081

Number of Positions

- 95 permanent positions
- 1 temporary position
- 6 temporary federally funded positions

Number of Vacancies

INS had ten vacancies as of November 30, 2018: 1 civil service, 8 exempt-included, and 1 exempt-excluded.

Requests for FB 2019-2021

The INS is requesting an appropriation out of the CRF of:

- \$2,500,000 for FY 2019-2020 and \$500,000 for FY 2020-2021 to fund the replacement of the Hawaii Insurance Database System and corresponding licensing, maintenance, and independent verification and validation costs.
- \$417,736 for FY 2019-2020 and \$417,736 for FY 2020-2021 to fund fringe benefit costs for collective bargaining and salary adjustments.

Expenditures

By way of background, the Division's expenditure appropriation consists of operating and personnel expenses. Personnel expenses account for over 70% of all expenditures. Some of the significant operating expenses include: the assessment for central services; professional service contracts with auditing firms to provide expertise with the examination of domestic insurers and with actuarial professionals to assist with

analysis of rates and reserves of company filings; and the renting of office space for the INS' health branch. The current allocated ceiling amount for these contracts is \$2.5 million. Contractual services for actuaries and auditors can greatly fluctuate from year to year, depending on the volume and difficulty of rate filings received and the complexity of the insurer being examined. An example of this fluctuation would be a comparison of FY 2014 contractual expenditures of \$2.2 million with FY 2018 contractual expenditures of \$635,000. Additionally, INS is working diligently to fill vacant positions and to increase expenditures toward the appropriated ceiling amount.

For the Committee's information, an encumbrance is the name given to funds that have been reserved when a contract or purchase is finalized and encumbered. When a contract or purchase is processed, funds are placed aside for that transaction. These funds are no longer available for use in other transactions and are not included in the actual expenditure balance, because a payment has not yet been generated. The purpose and main benefit of encumbrance accounting is to avoid budget overspending.

The following is a summary of encumbrances as of June 30, 2018:

| Summary of Encumbrances | | | | |
|--------------------------------|---------------------|---------------------|---------------------|---------------------|
| at June 30, 2018 | | | | |
| | <u>S-313</u> | <u>S-317</u> | <u>S-501</u> | <u>T-917</u> |
| <u>Contracts</u> | | | | |
| Actuarial | 238,604.02 | | 150,000.00 | |
| Examination | 105,056.81 | | | |
| Legal | 13,087.94 | | | |
| Office Space | 10,989.35 | | | |
| <u>Purchase Orders</u> | | | | |
| Equipment | 356.02 | 1,271.20 | | |
| Computer Services | - | 271.20 | | |
| Mileage | 1,365.37 | | | |
| Parking | 273.75 | | | |
| Payroll | 10,955.32 | 5,281.11 | | |
| Software | 282,941.29 | | | |
| Software Maintenance | 38,768.20 | | | |
| Telephone | 64.41 | | | |
| Transcription Services | 17,186.14 | | | |
| Travel | 5,818.80 | 2,326.69 | | 20,612.41 |
| | 725,467.42 | 9,150.20 | 150,000.00 | 20,612.41 |

Reserve Amount

The reserve balance of the Compliance Resolution Fund – Insurance Regulation Fund (S-313) as of 6/30/18 is \$3,964,565, which represents less than four months of planned expenditures in FY 2019. The reserve balance of the Captive Insurance Administrative Fund (S-317) as of 6/30/18 is \$7,632,751, which the INS expects to use in FY 2020 and FY 2021 to develop and maintain its IT replacement project. In addition, anticipated future expenditures, including replacing the air conditioning system of King Kalākaua Building, repairing structural damage and roofing damage caused by Hurricane Lane, and developing a department-wide document management system, will require use of these reserves. Current revenues and reserve balances sufficiently support the INS’ budget requests.

Thank you for the opportunity to testify on these bills.