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OFFICE OF FEDERAL AWARDS MANAGEMENT (OFAM)

WRITTEN ONLY

TESTIMONY BY CRAIG K. HIRAI
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
TO THE HOUSE COMMITTEE ON GOVERNMENT REFORM
ON
HOUSE BILL NO. 1830

February 2, 2022
9:30 a.m.
Via Videoconference

RELATING TO STATE SELF-INSURANCE AGAINST PROPERTY AND CASUALTY RISKS

The Department of Budget and Finance (B&F) offers comments on House Bill (H.B.) No. 1830.

H.B. No. 1830 establishes the State Self-Insurance Against Property and Casualty Risks Special Fund (SIAPCRSF) to be administered by the Comptroller, through the Risk Manager, to provide the State with self-insurance against the State's property and casualty risks. The bill appropriates unspecified general funds in FY 23 to the Department of Accounting and General Services to be deposited into this newly established special fund and appropriates out of this special fund unspecified funds in FY 23 for the purposes of this Act.

B&F notes that the federal Coronavirus Response and Relief Supplemental Appropriations Act requires that states receiving Elementary and Secondary School Emergency Relief (ESSER) II funds and Governor's Emergency Education Relief II funds must maintain state support for:

- Elementary and secondary education in FY 22 at least at the proportional level of the state's support for elementary and secondary education relative to the state's overall spending, averaged over FYs 17, 18 and 19; and
- Higher education in FY 22 at least at the proportional level of the state's support for higher education relative to the state's overall spending, averaged over FYs 17, 18 and 19.

Further, the federal American Rescue Plan (ARP) Act requires that states receiving ARP ESSER funds must maintain state support for:

- Elementary and secondary education in FY 22 and FY 23 at least at the proportional level of the state's support for elementary and secondary education relative to the state's overall spending, averaged over FYs 17, 18 and 19; and
- Higher education in FY 22 and FY 23 at least at the proportional level of the state's support for higher education relative to the state's overall spending, averaged over FYs 17, 18 and 19.

The U.S. Department of Education has issued rules governing how these maintenance of effort (MOE) requirements are to be administered. B&F will be working with the money committees of the Legislature to ensure that the State of Hawai'i complies with these ESSER MOE requirements.

Additionally, B&F comments on the establishment of the SIAPCRSF. As a matter of general policy, the department does not support the creation of special funds which do not meet the requirements of Section 37-52.3, HRS. Special funds should: 1) serve a need as demonstrated by the purpose, scope of work and an explanation why the program cannot be implemented successfully under the general fund appropriation process; 2) reflect a clear nexus between the benefits sought and charges made upon the users or beneficiaries or a clear link between the program and the sources of revenue; 3) provide an appropriate means of financing for the program or activity; and 4) demonstrate the capacity to be financially self-sustaining. In regard to H.B. No. 1830, it is difficult to determine whether the special fund meets the criteria to establish a special fund.

Thank you for your consideration of our comments.

DAVID Y. IGE
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WRITTEN TESTIMONY
OF
CURT T. OTAGURO, COMPTROLLER
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES
TO THE

COMMITTEE ON GOVERNMENT REFORM

FEBRURARY 2, 2022, 9:30 A.M.
VIA VIDEOCONFERENCE, STATE CAPITOL

H.B. 1830

RELATING TO STATE SELF-INSURANCE AGAINST PROPERTY AND CASUALTY RISKS

Chair McKelvey, Vice Chair Wildberger and members of the Committee, thank you for the opportunity to testify on H.B. 1830.

The Department of Accounting and General Services ("Department") appreciates the intent of the measure and provides the following comments.

The proposed measure 1) adds a new section to chapter 41D, Hawaii Revised Statutes ("HRS"), to establish a special fund for the State to self-insure against property and casualty risks, 2) authorizes the governor to transfer an undetermined amount of general funds to the special fund on an annual basis to address payment of any losses for State of Hawaii property and casualty risks, 3) provides for the comptroller to establish deductibles for the state agencies for certain perils or classes of property or casualty risks, and 4) provides for the comptroller to request that the governor authorize an advance to the special fund of sufficient sums of money from other funds in the state when the fund balance is insufficient to keep the special fund actuarially sound and pay claims; advance to be repaid within ten years with interest, including the option to assess state agencies for the repayment as needed.

We appreciate the general intent to save the State the cost of its annual insurance premiums by establishing and administering self-insurance coverage, but would like to highlight the following areas of concern with the measure:

- Amending Section 41D-2, HRS, to eliminate the Comptroller's discretion to purchase property and casualty insurance for the State. The current language within Section 41D-2, HRS, states that the Comptroller, through the risk manager, shall have discretion to purchase casualty and property insurance. Without this discretion, the State will be left with only one option, that of total self-insurance. The current statute allows for both insurance purchases and self-insurance as options, depending on insurance market conditions. It would be prudent to have options in protecting the State against catastrophic losses and to minimize the total cost of insuring risk. As such, amendments to Section 41D-2, HRS, would not be recommended.

- Furthermore, there may be insurance requirements and risk management considerations in procurement/financing agreements, e.g., financiers involved in the State's option to pursue Public-Private Partnerships (P3) for future projects may require certain levels of insurance to satisfy their requirements. FEMA may also require certain levels of insurance due to past funding provided to the State of Hawaii. Absent of any insurance policy to cover past FEMA proceeds received (such as a flood), could void additional funding from FEMA for the same type of loss in the future. Additionally, limiting the ability of the state to buy insurance could raise questions with credit rating agencies and affect the analysis they conduct on governance practices.

- The amount of reserves needed for self-insurance to ensure that the self-insurance fund can be operated on an actuarially sound basis. One of the factors to be considered is funding for this initiative. To date, the following policies are in effect and provides the following coverage limits:

Property	$200,000,000
Terrorism	$100,000,000
Excess Liability	$7,500,000
Crime	$10,000,000
Cyber	$5,000,000
Total	**$322,500,000**

In essence, the minimum amount of an up-front appropriation for total self-insurance would be $322,500,000 which would be equivalent to removing all insurance policies. This amount and type of appropriation would require a long term commitment void of any defunding of the self-insurance fund as monies must be maintained and made available to address any unforeseen events like a hurricane or cyber-attack.

Incremental infusions into a self-insurance fund in order to reach the desired target level cannot be considered as it will place the State of Hawaii at a great financial disadvantage; at the current general fund appropriation level, it will take more than 30 loss-free years to optimally fund a self-insurance fund and provide the capital equivalent to the coverage at current levels. If a severe loss should occur during the interim, the State of Hawaii will experience a financial deficit absent of supplemental insurance policies. Without an assessment of the State's capacity to absorb uncertainty and take on 100% of the risk while capitalizing the fund would be a huge financial/fiscal risk. Hence, the need to keep the comptroller's discretion to purchase insurance will still be needed to eventually reach a total self-insured level if that option is deemed feasible.

- The requirement for the proposed special fund to repay the monies advanced for insufficiencies may not be attainable because the only potential revenue source for the special fund will come from state agency assessments. State agencies will be required to budget for amounts that are difficult to plan for since the time and amounts of the insufficiencies are unpredictable.

- Finally, the department annually reviews and analyzes the insurance program for its effectiveness to ensure it manages the cost of the state's insurable risks. During the 2017 legislative session, Act 62 was enacted which allowed the risk management office to procure insurance policies on a flat fee basis instead of the traditional commission fee basis. This approach has saved over $8.4 million over 4 fiscal years for an average of over $2.1 million per year. The proposed measure will eliminate the purpose and intent of Act 62. The Department, thus, recommends that the risk management office continues its efforts in evaluating options to manage the costs of its insurance premiums while effectively managing risks and minimizing the State's loss exposure.

In summary, the Department appreciates the intent of this bill for self-insurance as a cost-savings measure but has concerns regarding the risks and costs associated with it. Preserving the Department's flexibility to exercise its discretion on how to finance its cost of risk is vitally important. As such, changes to the current Risk Management statute are not needed as the risk management program has the latitude to explore options in managing costs.

Thank you for the opportunity to testify on this matter.

HB-1830
Submitted on: 2/1/2022 4:47:09 PM
Testimony for GVR on 2/2/2022 9:30:00 AM

Submitted By	Organization	Testifier Position	Remote Testimony Requested
Tracy Kitaoka	State of Hawaii	Comments	Yes

Comments:

I am available for comments.