ALASKA STATE LEGISLATURE
HOUSE LABOR AND COMMERCE STANDING COMMITTEE
April 15, 2002
3:25 p.m.

MEMBERS PRESENT

Representative Lisa Murkowski, Chair
Representative Andrew Halcro, Vice Chair
Representative Kevin Meyer
Representative Pete Kott
Representative Norman Rokeberg
Representative Harry Crawford
Representative Joe Hayes

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE BILL NO. 429
"An Act relating to certain licenses for the sale of tobacco products; relating to tobacco taxes and sales and cigarette tax stamps; relating to provisions making certain cigarettes contraband and subject to seizure and forfeiture; relating to certain crimes, penalties, and interest concerning tobacco taxes and sales; relating to notification regarding a cigarette manufacturer's noncompliance with the tobacco product Master Settlement Agreement or related statutory provisions and to confiscation of the affected cigarettes; and providing for an effective date."

- MOVED CSHB 429(L&C) OUT OF COMMITTEE

HOUSE BILL NO. 246
"An Act relating to confidentiality of records and to cease and desist orders of the division of insurance, to insurance company investments, to unauthorized insurers, to surplus lines insurance, to health insurance, to life insurance, to annuity insurance, to consumer credit insurance, to title insurance, and to hospital and medical service corporations; and providing for an effective date."

- MOVED CSHB 246(L&C) OUT OF COMMITTEE

HOUSE BILL NO. 66

"An Act relating to pesticide use; and providing for an effective date."

- SCHEDULED BUT NOT HEARD

PREVIOUS ACTION

BILL: HB 429
SHORT TITLE:TOBACCO TAXATION; LICENSING
SPONSOR(S): RLS BY REQUEST OF THE GOVERNOR

Jrn-Date	Jrn-Page		Action
02/15/02	2282	(H)	READ THE FIRST TIME - REFERRALS
02/15/02	2282	(H)	L&C, JUD, FIN
02/15/02	2282	(H)	FN1: (REV)
02/15/02	2282	(H)	GOVERNOR'S TRANSMITTAL LETTER
04/03/02		(H)	L&C AT 3:15 PM CAPITOL 17
04/03/02		(H)	Heard & Held
04/03/02		(H)	MINUTE(L&C)
04/08/02		(H)	L&C AT 3:15 PM CAPITOL 17
04/08/02		(H)	Scheduled But Not Heard
04/10/02		(H)	L&C AT 3:15 PM CAPITOL 17
04/10/02		(H)	Heard & Held MINUTE(L&C)
04/15/02		(H)	L&C AT 3:15 PM CAPITOL 17

BILL: HB 246
SHORT TITLE:OMNIBUS INSURANCE BILL
SPONSOR(S): LABOR & COMMERCE BY REQUEST

Jrn-Date	Jrn-Page		Action
04/17/01	1015	(H)	READ THE FIRST TIME - REFERRALS
04/17/01	1015	(H)	L&C, JUD
04/15/02		(H)	L&C AT 3:15 PM CAPITOL 17

WITNESS REGISTER

NEIL SLOTNICK, Deputy Commissioner
Office of the Commissioner
Department of Revenue
PO Box 110405
Juneau, Alaska 99811-0405
POSITION STATEMENT: During the hearing on HB 429, he discussed a formula to eliminate any additional competitive advantage being provided by the discount.

MIKE ELERDING
Northern Sales Company of Alaska
PO Box 8112
Ketchikan, Alaska
POSITION STATEMENT: During hearing on HB 429, testified that he was not opposed to stamping itself, however, he expressed the need to pass an unfair trade practices law before requiring stamping.

BOBBY SCOTT, Vice President
Jan's Distributing, Inc.
1807 W. 47th Avenue
Anchorage, Alaska 99517-3164
POSITION STATEMENT: During hearing on HB 429, testified that the governor's fiscal notes don't address any of the actual problems with regard to curbing the black market sale of cigarettes.

BOB GALOSICH, Vice President
Wholesale Operations
Alaska Commercial Company;
Operator, Frontier Expediters
(No address provided)
POSITION STATEMENT: Testified in opposition to HB 429.

JOHANNA BALES, Revenue Auditor
Tax Division
Department of Revenue
550 W. 7th Ave., Suite 500
Anchorage, AK 99501
POSITION STATEMENT: Answered questions with regard to HB 429.

BOB LOHR, Director
Division of Insurance
Department of Community & Economic Development
3601 C Street, Suite 1324
Anchorage, Alaska 99503-5948
POSITION STATEMENT: Presented HB 246.

KATIE CAMPBELL, Actuary L/H
Division of Insurance
Department of Community & Economic Development
PO Box 110805
Juneau, Alaska 99811-0805

POSITION STATEMENT: Answered questions during hearing on HB 246.

ACTION NARRATIVE

TAPE 02-57, SIDE A
Number 0001

CHAIR LISA MURKOWSKI called the House Labor and Commerce Standing Committee meeting to order at 3:25 p.m. Representatives Murkowski, Halcro, Meyer, Crawford, and Hayes were present at the call to order. Representatives Kott and Rokeberg arrived as the meeting was in progress.

HB 429-TOBACCO TAXATION; LICENSING

CHAIR MURKOWSKI announced that the first order of business would be HOUSE BILL NO. 429, "An Act relating to certain licenses for the sale of tobacco products; relating to tobacco taxes and sales and cigarette tax stamps; relating to provisions making certain cigarettes contraband and subject to seizure and forfeiture; relating to certain crimes, penalties, and interest concerning tobacco taxes and sales; relating to notification regarding a cigarette manufacturer's noncompliance with the tobacco product Master Settlement Agreement or related statutory provisions and to confiscation of the affected cigarettes; and providing for an effective date."

CHAIR MURKOWSKI reminded the committee that some time ago the committee heard the Department of Revenue's introduction of HB 429 and some limited public testimony. Since that time, the committee has received a couple of amendments. She informed the committee that she has been working with the department as well as Mike Elerding, who had expressed concerned with regard to how the stamping procedure would take place in Alaska. There was concern that local Alaskan distributors would be at a competitive disadvantage with those large out-of-state businesses who already perform tax stamping. She said that there was the hope that something could be worked out that would allow the department to eliminate/limit the amount of cigarette contraband while allowing small Alaskan businesses to compete.

Number 0238

NEIL SLOTNICK, Deputy Commissioner, Office of the Commissioner, Department of Revenue, informed the committee that the department did consider Mr. Elerding's proposal that the

stamping be required to take place in Alaska. However, Mr. Slotnick suggested that the aforementioned requirement not be pursued because he believes there would be serious constitutional problems. Requiring the stamping to take place in Alaska would exclude an interstate business from participating in Alaska trade. The U.S. Supreme Court is chary of allowing states to use their tax code to create a competitive advantage for in-state businesses versus out-of-state interstate businesses. Furthermore, Mr. Slotnick said he believes it would create difficulties for certain retailers who have done all they can to work with Alaska and comply with our tax. Moreover, such a requirement wouldn't address the competitive advantage the large wholesalers would have. Mr. Slotnick noted his agreement with Mr. Elerding that there is an economy of scale in stamping these cigarettes.

MR. SLOTNICK reminded the committee that in the original legislation he had proposed a split discount rate in which the distributor who stamps the cigarettes would keep a small portion of the tax in order to compensate that distributor for their costs. That split discount rate was in recognition of the aforementioned economies of scale. In discussions with Mr. Elerding, Mr. Elerding proposed a three-tiered discount rate. Mr. Slotnick said that the goal was to make stamping neutral so that the cost per cigarette so that everyone's cost per cigarette was approximately the same regardless of the size of the wholesaler. The discount worked out to be about eight-tenths of a cent per cigarette per stamping for most of the wholesalers. The proposal was that for $1 million or less in stamps, a 3 percent discount would be given. For all purchases of stamps between $1 million to $2 million there would be a 2 percent discount. Above $2 million but not more than $5 million there is only a .5 percent discount. Stamp purchases above $5 million don't receive a discount. This is the best formula that could be developed to eliminate any additional competitive advantage being provided by the discount.

Number 0563

CHAIR MURKOWSKI requested that Mr. Slotnick provide her with some idea as to [which wholesalers] fall where [in regard to the amount of stamps purchased]. She asked if there would be any wholesaler that would purchase over $5 million and which wholesalers would fall into the category that receives the 3 percent discount.

MR. SLOTNICK answered that he could only say, due to confidentiality, that there would be wholesalers that would fall in both categories.

CHAIR MURKOWSKI asked if it would be the Wal-Mart and Costco type stores that would have volumes over $5 million. She said that she was trying to understand whether there would be a local Alaskan distributor that would fall in the over $5 million category.

MR. SLOTNICK indicated that the big box wholesalers do represent the largest category and those big box wholesalers have told the department that they probably will be stamping in the state, although there has been no firm commitment.

MR. SLOTNICK, in response to Representative Meyer, answered that this legislation only addresses cigarettes because the stamp was too difficult to place on the other tobacco products. There is no state that requires a stamp on other forms of tobacco because there is no automation available to stamp those products. The legislature has made a policy decision that individual importation of other tobacco products without the stamp liability is acceptable.

Number 0798

MIKE ELERDING, Northern Sales Company of Alaska, noted that the committee packet should include his written testimony. House Bill 429 seeks to create a tax stamp for cigarettes in Alaska. Currently, only four states, including Alaska, don't have some form of tax stamping. Alaska is also among the minority of states that doesn't have an unfair trade practices law. Mr. Elerding informed the committee that his concern with HB 429 is related to the unfair trade practices used by a number of nationally recognized chain stores in Alaska. These stores are selling cigarettes at or below cost. Basically, these stores are using cigarettes as a loss "leader" to attract shoppers. Furthermore, predatory pricing practices make it extremely difficult for Alaska-based distributors to make a profit on the products sold. For every $1 profit [distributors] make on cigarettes, the State of Alaska makes a profit of $14.29. The wholesale list price to the large grocers in Juneau is $14.29. Mr. Elerding directed the committee to a chart in the committee packet entitled, "Juneau, Alaska - April 2002 Wholesale List Price $39.12." He explained that of the $39.12 wholesale list price for a [carton of cigarettes], $26.81 represents the [wholesaler's] cost to the manufacturer, which amounts to 68

percent. The state receives $10 [per carton], which amounts to 26 percent. The City & Borough of Juneau's excise tax is $1.61 [per carton], which is 4 percent. He noted that the City & Borough of Juneau and the Municipality of Anchorage are the only two areas that charge an excise tax for cigarettes. The wholesale distributor profit for Northern Sales Company of Alaska is $.70 [per carton], which is 2 percent. Mr. Elerding said that although he isn't making a lot of money on cigarettes, there is at least one nationally recognized store in Juneau that is selling cigarettes in Juneau below their cost. With stamping there will be additional costs. Therefore, it's going to be difficult for Northern Sales Company of Alaska to continue in the cigarette business if the state doesn't develop an unfair trade practices law. Mr. Elerding wasn't opposed to stamping in and of itself, but the unfair trade practices law is necessary before implementing a law requiring state wholesale distributors to stamp cigarettes before selling them in the state.

Number 1032

REPRESENTATIVE MEYER asked whether it's a fairly common practice to have loss leaders to get people in the store in the hopes that loss is made up on other items.

MR. ELERDING agreed with the premise suggested by Representative Meyer. However, when it becomes a predatory practice it tends to drive competitors out of business and seems illegal. Furthermore, Mr. Elerding didn't believe it is in anyone's best interest to continue to sell cigarettes below cost to the detriment of local wholesalers. Mr. Elerding informed the committee that there is only one manufacturer that makes stamping equipment, and this manufacturer isn't currently doing business in Alaska. This stamping equipment manufacturer can't quote him a price for the stamping equipment and presently, this manufacturer has no plans to establish maintenance for this equipment. Mr. Elerding pointed out that [Northern Sales Company of Alaska] sells about 350,000 cartons of cigarettes a year, and therefore if there is a problem with the stamping equipment, there would need to be an immediate fix to the equipment. Mr. Elerding expressed the need for HB 429 to be coupled with assurances that [a company] in Alaska would be able to purchase the equipment to actually perform the stamping in the state and receive maintenance for that equipment.

Number 1140

REPRESENTATIVE ROKEBERG expressed concern with Mr. Elerding's comment that Alaska doesn't have an unfair trade practices statute. Representative Rokeberg said there is an unfair trade practices statute and surmised that perhaps [Mr. Elerding meant] that Alaska's statute doesn't speak to predatory pricing. Representative Rokeberg related his assumption that Costco and Wal-Mart, due to their purchasing power, are able to obtain cigarettes at a lower cost-to-goods-sold pricing. Therefore, those businesses would still make a profit although they could sell the cigarettes below what [Northern Sales Company of Alaska] could in Juneau or Anchorage. Representative Rokeberg asked if other states would consider such situations a predatory practice.

MR. ELERDING explained that everyone, whether it's [Northern Sales Company of Alaska] or Costco, purchasing [from the major tobacco manufacturer] for the same exact invoice price. Therefore, when one sels cigarettes at cost or below cost, that's the same as the raw cost from the manufacturers invoice.

REPRESENTATIVE ROKEBERG remarked that he found it interesting that there is a set wholesale price on a national basis.

MR. ELERDING interjected that it's also interesting that every time Phillip Morris raises its prices so do RJ Reynolds and Brown Williamson. The prices are exactly the same for the major brands.

REPRESENTATIVE ROKEBERG asked if the freight on board (FOB) is at a major distribution point.

MR. ELERDING answered that the FOB is the (indisc.) warehouse out of Seattle. There is only one bonded warehouse in Alaska and it's located in Anchorage.

CHAIR MURKOWSKI returned to the proposal for a four-tiered approach.

MR. ELERDING said that he liked the approach, which he worked on with Mr. Slotnick. In further response to Chair Murkowski, Mr. Elerding agreed that the [four-tiered approach] would help level the playing field somewhat for in-state distributors.

Number 1364

BOBBY SCOTT, Vice President, Jan's Distributing, Inc., testified via teleconference. He noted his agreement with Mr. Elerding.

Mr. Scott turned to the governor's fiscal notes, which do not address or target any of the actual problems with regard to curbing the black market sale of cigarettes. He expressed interest in obtaining statistics on that matter. Furthermore, the $14.29 profit the state receives is "very real" as is the additional costs the distributors would incur. Moreover, he inquired as to who would be in change of enforcement of stamping, which will probably be another cost to the taxpayers.

CHAIR MURKOWSKI recalled from the initial testimony that the state doesn't have very accurate numbers with regard to seized contraband material. She asked if the tiered approach helps Mr. Scott's business in terms of competing with [out-of-state] companies.

MR. SCOTT answered, "Other than having to add on extra employees to run them, it might." He agreed that it's better than the alternative of no discount.

Number 1484

REPRESENTATIVE ROKEBERG pointed out that Mr. Scott had indicated in his written testimony, included in the committee packet, that a stamping machine costs about $25,000. That cost didn't include freight fees and the required maintenance agreement. Representative Rokeberg inquired as to how many people would be required to operate the stamping machine.

MR. SCOTT explained that a representative of RJ Reynolds provided him with examples of [the number of employees] other states have used. The RJ Reynolds representative specified that at a minimum three people are required to operate the stamping machine.

REPRESENTATIVE ROKEBERG inquired as to how often the stamping machine would have to be run in order to deal with Mr. Scott's volume of business.

MR. SCOTT replied that he couldn't answer that question.

REPRESENTATIVE ROKEBERG related, "I think it relates to this issue about the amendment we have and you spoke to that. What's that going to generate and see if you can either basically try to recoup your costs by the discount amount because ... this sounds like a private fiscal note, this bill, versus what we can do to soften the blow to these people."

Number 1569

BOB GALOSICH, Vice President, Wholesale Operations, Alaska Commercial Company; Operator, Frontier Expediters, testified via teleconference. He informed the committee that Frontier Expediters is a DBA (ph) and the wholesale arm of the Alaska Commercial Company. The wholesale arm of the business employs about 17 people. Mr. Galosich said that he couldn't provide the committee with good numbers for cigarette sells in 2001 because the company didn't sell cigarettes for nine months of 2001 due to the municipal tax issue. However, Mr. Galosich estimated that in 2002 sales and distributions to its 24 [Alaska Commercial Company] stores will be approximately $20 million, of which about half is from tobacco products. An inventory of about $400,000 is maintained, including the $10 state tax in Anchorage. Mr. Galosich said that he was adamantly opposed to HB 429 as written because it adversely impacts small tobacco wholesalers.

MR. GALOSICH said that [small tobacco wholesalers] operate on thin margins for competitive reasons. Alaska is one of approximately 17 states that do not have a minimum sell law. This legislation would cause a substantial increase in operating costs for the wholesaler and that would continue to place [the small tobacco wholesalers] at a competitive disadvantage. Although the discount structure would help, one must keep in mind that in Alaska no one has stamping machines and no one has ever done stamping. Therefore, there is the combination of an investment, a learning curve, additional people costs, and air rate that's going to contribute to costs in the beginning. Mr. Galosich related his belief that no one has had enough time to study exactly what the impact would be other than to say that it would be a negative impact on business. Furthermore, the state has been unable to quantify the amount of lost revenue due to contraband cigarette sales. Mr. Galosich remarked that getting contraband cigarettes in Alaska is difficult. "Do the existing volumes justify the burden on the small businessmen in Alaska, I don't think at this point that they do," he concluded.

Number 1746

CHAIR MURKOWSKI returned to Mr. Scott's questions. With regard to the contraband, Chair Murkowski related that there doesn't seem to be anything firm in terms of what the Department of Revenue might expect to recover from any contraband.

MR. SCOTT specified that he wanted to know why the department has such a sense of urgency with the implementation of this tax stamp. Mr. Scott reminded the committee that he also inquired as to who would enforce this.

MR. SLOTNICK deferred to Johanna Bales. However, he said that the department cannot quantify the amount of contraband cigarettes coming into the state, although there is knowledge that it does happen due to Ms. Bales' work. Mr. Slotnick related the hope that the contraband is small, but Hawaii, which is also remote, became a quick target for importers of untaxed cigarettes. Hawaii's stamp law significantly reduced the contraband. Mr. Slotnick specified that the goal [with HB 429] is to perform reasonable enforcement action; the department doesn't want the state to be an attractive target for the importers of untaxed cigarettes. With regard to enforcement, Mr. Slotnick informed the committee that [the department] would need at least two additional positions to help enforce this law. Moreover, the department will cross-train with law enforcement and investigative officials who are in the field, which will include Village Public Safety Officers (VPSOs), troopers, city police, investigators, department investigators, and the Department of Health & Social Services. Additionally, Mr. Slotnick expected that the public would report sightings of unstamped cigarettes.

REPRESENTATIVE MEYER related his understanding then that this stamp would ensure that the state tobacco tax is being paid. He asked if there is a way in which the cities of Juneau and Anchorage could also ensure that they receive their tax as well, or will those cities need their own stamp.

MR. SLOTNICK answered that he believes the cities would need their own stamp.

Number 1908

JOHANNA BALES, Revenue Auditor, Tax Division, Department of Revenue, testified via teleconference. Ms. Bales said that the only city she knew of that had its own [cigarette] stamp is New York City. All the other states feel that the cities would have to have a stamp designating that the tax is paid. One of the problems with cities having their own stamp is that [the department] has confidentiality statutes that don't allow it to share information with the municipalities.

REPRESENTATIVE ROKEBERG inquired as to the percent increase in revenue Hawaii experienced after implementing the [tobacco] tax.

MR. SLOTNICK answered that when the stamp was imposed, Hawaii experienced a 25 percent increase in revenue collection.

MS. BALES, in response to Mr. Slotnick, specified that the cigarette tax in Hawaii increased from about $.60 to $1.00 a pack. Although She pointed out that it's difficult to decipher the amount of total revenue Hawaii saw, Hawaii's collection increased from $4 million a month before the stamp to $6.5 million a month in revenue [after implementation of the stamp].

REPRESENTATIVE ROKEBERG asked if the discounts in the amendment would be sufficient to cover the costs of applying the stamps.

MS. BALES pointed out that [the department] has seen a 22 percent reduction in reported taxable cigarettes once Alaska's tax rates increased. [The department] believes that is the result of a combination of people who have stopped smoking or cut back and bootlegging. Without a stamp, it's impossible for the department to determine what makes up the 22 percent. However, for every 1 percent increase, after implementing the stamp, [the state] will receive $400,000 more in revenue each year. A 10 percent increase would amount to an additional $4 million in revenue.

MR. SLOTNICK added that although this [discount proposal] won't cover all the distributor's costs, it narrows it to less than $.01 per cigarette. Mr. Slotnick related the belief that the distributors will experience an increase in revenue if there is, in fact, an increase in taxable sales. Mr. Slotnick acknowledged that the discount rate could be changed so that it covers all the distributor's costs, but it would result in a much higher fiscal note. Furthermore, Mr. Slotnick reiterated his belief that the distributors will experience an increase in sales with the passage of HB 429 and thus the [discount amendment] is generous.

Number 2072

REPRESENTATIVE ROKEBERG surmised then that Mr. Slotnick believes [under HB 429] sales would increase, and therefore the increased cost would be offset with the discount and the increased sales.

MR. SLOTNICK responded, "I'm not sure I'm willing to go quite that far. I don't know whether they will, in fact, offset all of their costs, but at least there's no competitive advantage."

REPRESENTATIVE ROKEBERG envisioned Wal-Mart or Costco doing this with a stamp machine outside of the state, and perhaps doing so cheaper.

MR. SLOTNICK said that the department expects there to be some out-of-state stamping. He reiterated that [some of the larger distributors] have indicated a high probability that they will stamp in the state. Some of the smaller wholesalers who operate out of Seattle and ship to remote communities will probably stamp out of state.

CHAIR MURKOWSKI informed the committee that Mark Johnson, Department of Health & Social Services, is present to answer any additional questions regarding the tobacco enforcement aspect of this. There were no questions of Mr. Johnson.

Number 2173

MR. ELERDING related that since the arrival of the national box stores in Anchorage, the volume of cartons that move through the bonded warehouse has steadily declined. Therefore, in Mr. Elerding's opinion, the majority of the stamping by the larger stores will be performed outside of Alaska.

CHAIR MURKOWSKI, determining there to be no one else to testify, closed public testimony.

Number 2215

REPRESENTATIVE MEYER commented that he is having difficulty getting excited about HB 429. Even with the amendments, [stamping] could still hurt the small business wholesalers in Alaska. He related that he wasn't convinced that Alaska has a [tobacco] bootlegging problem.

CHAIR MURKOWSKI said that was her concern when the committee first heard the bill. However, the proposal being discussed as the four-tiered system addresses the competitive disadvantage and levels the playing field a bit. She recognized Representative Meyer's concern to be in regard to whether it's necessary to have a stamping operation in this state. She said the state doesn't want to be a target for contraband and she

questioned whether that would be the case if Alaska is one of the last states to monitor [cigarette contraband].

REPRESENTATIVE MEYER recalled an earlier point with regard to the difficulties of having a stamping machine in Alaska. The only state that would be similarly situated would be Hawaii, which has a larger population base that could fix a broken stamping machine.

TAPE 02-57, SIDE B

REPRESENTATIVE MEYER expressed concern that there could be some other inherent risks that could hurt the small businesses other than the volume.

Number 2331

REPRESENTATIVE HAYES moved that the committee adopt Amendment 1, which reads as follows:

> Page 7, lines 23-27:
> Delete: "For the first $1,000,000 in denominated value of stamps purchased by a licensee under this section in the same calendar year is equal to one percent of the denominated values of the additional stamps."
>
> Page 7, line 31, following "AS 43.50.500-43.50.700.":
> Insert: "The discount under this subsection is equal to the sum of the amounts calculated using the following percentages of denominated value of stamps purchased by a licensee under this section in a calendar year:
> (1) $1,000,000 or less, three percent;
> (2) the amount that is more than $1,000,000, but not more than $2,000,000, two percent;
> (3) the amount this is more than $2,000,000, but not more than $5,000,000, 0.5 percent;
> (4) the amount that is over $5,000,000, zero percent."

There being no objection, Amendment 1 was adopted.

REPRESENTATIVE HAYES related his belief that it's probably safe to assume that Alaska has some bootleg contraband because Alaska is one of only four states that doesn't know. Amendment 1 places a safeguard in the bill, which Representative Hayes said

made him more comfortable. With regard to the concerns that this stamping machine couldn't be fixed in Alaska, Representative Hayes said he believes there are plenty of good mechanics in the state who could probably fix it.

Number 2238

REPRESENTATIVE HALCRO moved to report HB 429 as amended out of committee with individual recommendations and the accompanying fiscal note. There being no objection, CSHB 429(L&C) was reported from the House Labor and Commerce Standing Committee.

HB 246-OMNIBUS INSURANCE BILL

CHAIR MURKOWSKI announced that the next order of business would be HOUSE BILL NO. 246, "An Act relating to confidentiality of records and to cease and desist orders of the division of insurance, to insurance company investments, to unauthorized insurers, to surplus lines insurance, to health insurance, to life insurance, to annuity insurance, to consumer credit insurance, to title insurance, and to hospital and medical service corporations; and providing for an effective date." [The committee's discussion was directed at Version 22-LS0743\J, Ford, 2/20/02.]

Number 2193

BOB LOHR, Director, Division of Insurance, Department of Community & Economic Development (DCED), specified that in [Version 22-LS0743\J, Ford, 2/20/02] there are two substantive issues and some miscellaneous provisions. The bill contains a number of confidentiality provisions, which would basically require the Division of Insurance to protect the confidentiality of insurance examination work papers in order to increase the willingness of insurers to share confidential information with the division during the examination process. Currently, the division has the authority to compel the production of documents, but at times the insurer will argue that production to the division risks access to those documents by third party litigators. The current protection in statute is somewhat limited; the director has the authority to make documents confidential when it is in the public interest and can do so for as long as necessary to protect the confidentiality. The statute basically provides for a situational standard that's designed to be somewhat temporary. This [legislation] would make [confidentiality] automatic with respect to certain categories of documents. Mr. Lohr emphasized that this change

is important so that Alaska will remain accredited by the National Association of Insurance Commissioners (NAIC), meaning that Alaska meets the minimum national standards for financial regulation of insurance companies. Furthermore, [this legislation] would make it possible for the division to share confidential information with federal and state regulators and to receive documents that other states and the NAIC have gathered about insurance companies. Mr. Lohr informed the committee that the Washington State insurance commissioner will not share investigative files with Alaska's Division of Insurance under the current confidentiality standards. He explained that Washington State wants a confidentiality agreement on a case-by-case basis. Furthermore, Washington State wants an agreement that is at least as protective as their law. Washington State wants to avoid someone going to another jurisdiction, such as Alaska, and seek production of documents under that jurisdiction's public records act when those documents weren't available directly from the insurance regulators in Washington State.

Number 2068

CHAIR MURKOWSKI recalled the credit scoring legislation introduced by Representative Crawford and the question regarding whether aspects or insurers' records would be considered confidential. She asked if the aforementioned would be an example of the confidentiality provisions being discussed now.

MR. LOHR replied no and pointed out that the provisions implicated by Representative Crawford's bill deal with rate making. Within the rate-making statute there is a provision specifying that once the division has concluded action on a requested rate, all of the supporting documents related to that rate request become public. Therefore, in order for an insurer to get a credit scoring model approved, the insurer would have to be willing for that model to become public. That provision wouldn't be impacted by HB 246.

Number 2011

MR. LOHR returned to [Version J] and the Multiple Employer Welfare Arrangements (MEWA), which consists of a group of employers that form a pool to provide health insurance to their employees. The division would like to encourage the formation of financially sound MEWAs. Furthermore, Alaska wants to attract additional responsible insurers and sound alternative health insurance arrangements to the state. He noted that

competition in this area is desirable. However, the current law requires MEWAs to obtain a certificate of authority as a health insurer and thus requires the MEWA to maintain approximately $2 million of capital and surplus and file financial statements that would be regulatory overkill, in Mr. Lohr's opinion. Mr. Lohr pointed out that [Version J] establishes capital surplus, reserve standards, financial reporting, et cetera that are more appropriate to the structure and type of business in which a MEWA engages.

MR. LOHR turned to the miscellaneous provisions of [Version J]. He noted that he has chosen only three examples of those provisions. One of the provisions would establish fees for late payment of premium taxes in order to encourage the timely payment of premium taxes, which are general fund revenues. Another provision would establish an annual fee to operate as a joint insurance arrangement (JIA) in order to offset the division's cost of enforcing the provisions of AS 21.76. Mr. Lohr explained that JIAs aren't regulated as insurance entities under state law. However, in order to preserve the competitive playing field, each of the JIAs have frequently requested that the division be the "competitive gatekeeper." The division incurs an expense for doing the aforementioned and if those expenses aren't covered by fees paid by the JIAs, then the expenses would be recovered through the fees to the division from the licensees. However, the division doesn't feel that it's appropriate to cross subsidize JIA activities out of licensing fees. Another provision would establish minimum attachment points consistent with NAIC's model law for stop-loss insurance policies that are purchased by employers to self-insure their health insurance plans. These minimums will help eliminate health insurance policies sold as stop-loss insurance in order to avoid compliance with health insurance laws, including guaranty issue, federal portability requirements, and benefit mandates. Mr. Lohr related his belief that this legislation isn't controversial because the text of this legislation has been "shopped" to all interested parties of which the division is aware. The division hasn't received substantial opposition and thus wouldn't predict controversy with regard to the provisions of the legislation.

REPRESENTATIVE CRAWFORD requested explanation of attachment points and retention limits.

Number 1827

KATIE CAMPBELL, Actuary L/H, Division of Insurance, Department of Community & Economic Development, explained that an attachment point is the point at which the insurance would actually kick in. Therefore, an employer who wanted to self-insure their health insurance benefits while protecting themselves from large claims or excessive numbers of claims [would use] the attachment point. Ms. Campbell pointed out that a small employer who wants to self-insure can't purchase a stop-loss policy with a retention of less than $10,000 per claim. Therefore, the employer would have to take the risk for any amount below $10,000, on an individual claim. Ms. Campbell explained that if the [attachment point] is low enough that all the risk is on the insurance company [that is] health insurance instead of stop-loss insurance. Stop-loss insurance policies aren't subject to health insurance laws and thus the employer wouldn't have credible coverage. A stop-loss policy isn't health insurance, she specified.

MR. LOHR surmised that a self-insured party isn't subject to the insurance code in the way that an insurer would be. Therefore, if a self-insured party can eliminate all risk to itself by virtue of a high deductible and a low attachment point, the self-insured is [risk free] and still isn't treated as an insurer.

REPRESENTATIVE ROKEBERG directed attention to page 12, line 25, which specifies the regulated type institutions. "We're not talking about a self-insured here," he asked.

MS. CAMPBELL explained that insurance companies actually write the stop-loss policy, and therefore it's insurance, but not health insurance. The [stop-loss insurance] is similar to employer liability in which the employer purchases a stop-loss policy to cover any losses incurred in their health plan over the [specified] dollar amount.

REPRESENTATIVE ROKEBERG inquired as to how a MEWA would issue a stop-loss insurance policy.

MS. CAMPBELL clarified that [a MEWA] would have to purchase a stop-loss insurance policy. She related that the goal was to cover anyone who could have a license to write an insurance policy. Therefore, any stop-loss policy issued by anyone who has a license to write insurance is subject to the same standard, including the MEWAs. She agreed with Representative Rokeberg that the self-insured can't be covered under the Employee Retirement and Income Security Act of 1974 (ERISA).

Number 1609

CHAIR MURKOWSKI turned attention to the sectional analysis [done by the Division of Insurance] and the definition of the health care insurance plan [found in Section 36 of Version J on page 14]. The sectional analysis says, "The unintended consequence is that individual short-term medical coverage must comply with health benefit mandates." The sectional analysis goes on to say, "This section amends the definition of health care insurance plan in order to exclude short-term individual health coverage from the benefit mandates." She asked if the aforementioned means that under [Version J individual short-term medical coverage] wouldn't be required to carry coverage for prostrate screening and breast cancer screening.

MS. CAMPBELL replied yes and explained that this federal definition wasn't translated into our laws accurately. The intent was that it shouldn't apply to individual short-term medical coverage, such as a three-month period when an individual is between coverage. There are some insurers who actually want to market such short-term coverage.

Number 1526

CHAIR MURKOWSKI surmised then that [Version J] is consistent with the Health Insurance Portability and Accountability Act (HIPAA).

MR. LOHR agreed, adding that HIPAA compliance is an important element in keeping the federal government "off our back."

CHAIR MURKOWSKI related her understanding then that [Version J] only takes on two policy issues: the confidentiality components and the MEWA regulations.

MR. LOHR replied yes and added that there are other potentially controversial provisions such as the possibility that JIAs might believe paying any fee at all is inappropriate and thus oppose it. Currently, there is an exemption under the surplus lines taxation law for aircraft regularly engaged in interstate commerce. This legislation proposes to change the language to refer to "primarily engaged".

CHAIR MURKOWSKI inquired as to whether "primarily engaged" has been defined.

MR. LOHR answered that it isn't defined in this legislation and it may be an appropriate subject for regulation. The division wanted to clarify the statute before taking on the regulatory effort.

Number 1428

REPRESENTATIVE ROKEBERG directed attention to Section 35 on page 14 and inquired as to why that language was included.

MS. CAMPBELL explained that the insurance companies interpreted the original provision to mean that they didn't have to provide at least $1,500 [of coverage]. Therefore, this language merely clarifies the original intent that a health care insurer can't provide less than $1,500 per year. This was discovered when the division reviewed the contracts.

REPRESENTATIVE ROKEBERG recalled the debate on this matter revolving around why if someone didn't use all their benefit that they would have to lose their benefit or why would the insurer have to pay more if the $1,500 wasn't used.

CHAIR MURKOWSKI related her understanding that the insurance companies interpreted the language to mean that they weren't required to provide anything unless it was up to $1,500.

MS. CAMPBELL indicated that the original language "up to $1,500" created the problem. The language in [Version J] specifies that an [insurer] has to provide up to $1,500 of benefit.

REPRESENTATIVE ROKEBERG asked if the language in [Version J] says that.

MS. CAMPBELL said, "So they have to provide at least $1,500 for a covered person."

REPRESENTATIVE ROKEBERG inquired as to a situation in which the person doesn't want to spend $1,500.

CHAIR MURKOWSKI said that the language doesn't seem to allow for [coverage] of less [than $1,500].

Number 1256

REPRESENTATIVE ROKEBERG turned to Section 41 and interpreted that section as adding MEWAs to the Alaska Comprehensive Health Insurance Association (ACHIA).

MR. LOHR agreed with Representative Rokeberg's interpretation. He added that the division is trying to broaden the base of inclusion.

CHAIR MURKOWSKI returned to the current language relating to diabetes education and pointed out that it says, "coverage for the cost of diabetes training or education is limited to $1,500 for a covered person in a year."

MS. CAMPBELL explained that the insurance companies were interpreting the existing language as allowing them to provide benefits up to $3,000. In other words, the existing language seemed to cap the benefit.

CHAIR MURKOWSKI recalled that the intent was not to put in place an unlimited requirement that an insurer had to provide diabetes education and training at an unrestricted amount. Therefore, the $1,500 was a compromise. If the insurer wanted to provide more coverage, the existing language was construed as restraining.

Number 1146

MR. LOHR offered the following language: "The health care insurer shall provide benefits not to exceed $1,500 and may provide benefits in excess of this amount."

MS. CAMPBELL agreed that the aforementioned language might get to the problem. Ms. Campbell pointed out that other benefit mandates such as with alcohol and drug abuse and those established limits haven't been interpreted to mean that if someone didn't use it, the benefit still had to be paid.

REPRESENTATIVE ROKEBERG remarked that the language [in Section 35] isn't clear to the average person.

MS. CAMPBELL suggested that the language [in Section 35] could refer to "coverage" rather than "benefits".

CHAIR MURKOWSKI agreed that the change to "coverage" seems appropriate.

MS. CAMPBELL interjected that the term "limited" in the existing statute seemed to cause the problem.

Number 1022

REPRESENTATIVE ROKEBERG moved that the committee adopt conceptual Amendment 1, as follows:

Page 14, line 10,
Delete "benefits"
Insert "coverage"

There being no objection, conceptual Amendment 1 was adopted.

CHAIR MURKOWSKI noted that the committee packet includes several amendments [to Version J] and asked whether Mr. Lohr cared to speak to them.

MR. LOHR pointed out that the legislation seems to have an error in which "small" and "large" are reversed and thus there is the need to amend that. The change from "large" to "small" confirms the lower retention limits for a smaller entity. It doesn't make sense to have stricter standards for the large entity than for the small entity. For actuarial purposes, the smaller entity needs additional sidebars. The same amendment inserts a section that references AS 21.07, the codified Patients' Bill of Rights, and AS 21.18.080-21.18.086, the health reserving standards. The addition of these references were included to ensure that the provisions in the case of hospital medical service corporations, of which Blue Cross is an example, [were included]. He informed the committee that the Blue Cross statute includes a provision that other provisions of the code don't apply to them unless explicitly listed. Although Blue Cross has treated the aforementioned provisions as if they apply, a strict reading of the code wouldn't apply them as a matter of law.

Number 0810

REPRESENTATIVE HAYES moved that the committee adopt Amendment 2, which reads as follows:

Page 13, line 1
replace "large" with "small"

Page 13, line 8
replace "small" with "large"

Page 29, line 27
Insert new bill section to read:

***Sec. ____.** AS 21.87.340 is amended by adding a new paragraphs to read:

(22) AS 21.07;

(23) AS 21.18.080-21.18.086

There being no objection, Amendment 2 was adopted.

Number 0772

REPRESENTATIVE KOTT moved to adopt CSHB 246, Version 22-LS0743\J, Ford, 2/20/02, as the working document. There being no objection, Version J was before the committee.

The committee then proceeded to restate the motions for conceptual Amendment 1 and Amendment 2, which were adopted again without objection.

Number 0708

REPRESENTATIVE ROKEBERG moved that the committee adopt Amendment 3 [22-LS8004\A.5, Ford, 4/4/02], which can be found at the end of this section of minutes.

REPRESENTATIVE KOTT objected for discussion purposes.

MR. LOHR explained that Amendment 3 addresses the property casualty guaranty fund, which is set up as a backstopping mechanism to protect the consumer. When a consumer purchases an insurance policy, the consumer wants to know that the premium dollars paid to the company will be used to provide the claims coverage promised. If the company goes under, this mechanism ensures that all other companies participate in a guaranty fund designed to pay claims against insolvent companies. Mr. Lohr said this works very well because it provides a level of insurance to the insurance system. "Every company that is participating in a line of insurance is required, as a condition of that access to that market, to agree to pay its pro rata share on claims based on its market share in that line of insurance," he explained. It's very important that this amendment be in place, he said.

MR. LOHR specified that Amendment 3 would change the mechanism of calculating the assessment. Currently, the assessment is done at the end of the year in which the insolvency occurs. For example, if a company became insolvent August 15, 2001, at the end of 2001 the assessment would be based on the market share of each company in the workers' compensation or property casualty

market in Alaska for that year only. This legislation would provide that one year later there would be an adjustment of that assessment based on the market share that occurred during the subsequent year [of insolvency]. He explained that it intends to address the current situation in which a new entrant into the market during the year [of another company's insolvency] would bear no assessment for the failure of the other company. However, the new entrant may inherit a lot of business due to the failure of the other company and thus there wouldn't be a level playing field in that market at that time. Based on a recalculation of that assessment one year later, the new entrant would pay its fair share based on its market share at the time of the insolvency of the other company. In response to Representative Rokeberg, the new entrant would have its assessment calculated one year subsequent to the prior assessment. Mr. Lohr commented that this [amendment] would establish a level playing field that wouldn't allow the new entrant to enter the market for free. Furthermore, this would result in a proportionately lower assessment to each of the other players in the market and thus the total market doesn't change but rather is reallocated. Mr. Lohr noted that this proposal has been submitted to the board of directors of the guaranty fund, which he understood had no opposition to this concept.

REPRESENTATIVE KOTT asked if [Amendment 3] would be the new Section 50.

MR. LOHR answered in the affirmative.

Number 0288

REPRESENTATIVE ROKEBERG asked if the board of the guaranty association has representatives from each of the firms participating in the association.

MR. LOHR related his belief that the members of the board of the guaranty association represent the largest insurers in the market. Furthermore, he said he believes that the voting is weighted proportional to the member's market share. He noted that he has heard no opposition from this board and the language was submitted to this board. He mentioned that he received e-mail confirmation from the board's staff that the board was comfortable with the language.

REPRESENTATIVE KOTT withdrew his objection.

Therefore, Amendment 3 was adopted.

Number 0130

REPRESENTATIVE MEYER moved that the committee adopt Amendment 4, which reads as follows:

Page 5, line 19:
Insert new bill section to read:
***Sec.___**. AS 21.09.200(a) is amended to read:
(a) Each authorized insurer shall annually, before March 2, file with the director **or his designee** a full and true statement of its financial condition, transactions, and affairs as of the preceding December 31. The reporting format for a given year is the most recently approved National Association of Insurance Commissioners' annual financial statement blank form and instructions, supplemented for additional information as required by the director. The director may require the statement to be filed on electronic media. The statement shall be verified by the oath of the insurer's president or vice-president, and secretary, or, if a reciprocal insurer, by oath of the attorney-in-fact or its like officers if a corporation unless verification is waived by the director of insurance. **The filing locations will be published by the director at least annually.**

Page 5, line 24:
Insert new bill sections to read:
***Sec.___**. AS 21.09.200(e) is amended to read:
(e) An insurer shall pay to the division $100 for each day the insurer fails to file the annual statement in the form **and location** required and within the time established in (a) of this section. The authority of the insurer to enter into new obligations or issue new or renewal policies of insurance in this state may be suspended by the director if the annual statement has not been filed by March 1.
***Sec.___**. AS 21.09.205(b) is amended to read:
(b) A quarterly financial statement, if required, is due **45** [60] days after the end of the quarter to which it applies.

Page 8, line 15:
Insert new bill section to read:
***Sec.___**. AS 21.27.330(b) is amended to read:

(b) If a licensee that is a firm transacts business at more than one place of business [IN THIS STATE], the licensee shall pay a license fee for each place of business.

CHAIR MURKOWSKI objected for the purpose of discussion.

MR. LOHR explained that that the amendment would allow the director of the Division of Insurance to delegate responsibility to receive these annual statements. Furthermore, it would allow the division to indicate the location of the filing annually. This would typically be done in the annual statement of instructions that the division already publishes for insurance companies. The amendment also deals with the location of the filing and amends the deadline for filing from 60 days to 45 days after the end of the quarter. Therefore, an insurance company has a month-and-a-half to submit the requirement, which he said he believes to be consistent with NAIC's standards for quarterly reports.

TAPE 02-58, SIDE A

MR. LOHR continued by pointing out that Amendment 4 inserts a new section that deletes the language "in this state". He explained that [the language was deleted] because it has been argued by an outside nonresident applicant for a license that this language means that those not located in Alaska don't have to pay this license fee. However, the division feels that a nonresident applicant should pay their fair share, he said.

REPRESENTATIVE MEYER asked if these are conceptual amendments.

CHAIR MURKOWSKI said that the drafter can work out the sections.

Number 0069

REPRESENTATIVE ROKEBERG turned to the last portion of Amendment 4, which inserts a new bill section on page 8, line 15. He questioned the drafting.

MR. LOHR, in response to Representative Rokeberg, explained that the argument is that if a [nonresident] applicant doesn't intend to open an office in Alaska, those applicants shouldn't pay any fee at all for multiple places of business.

REPRESENTATIVE ROKEBERG pointed out that the current language is more ambiguous because it says "the licensee shall pay a license

fee for each place of business" regardless of the state. He recommended leaving the language "in this state" in the bill and including language that specifies that if the licensee doesn't have a premise in the state, the licensee is still required to purchase a license.

CHAIR MURKOWSKI asked if the language read "If a licensee that is a firm transacts business at more than one place of business, the licensee shall pay a license fee for each place of business in this state." would address Representative Rokeberg's concern.

REPRESENTATIVE ROKEBERG said that the language could state, "A business that has no premises in the state still must pay a licensing fee."

MR. LOHR said he considered Representative Rokeberg's suggestion as a friendly amendment.

REPRESENTATIVE ROKEBERG moved that the committee adopt an amendment to Amendment 4 that would result in the new section to be inserted on page 8, line 15, to read as follows: "If a licensee that is a firm transacts business at more than one place of business, the licensee shall pay a license fee for each place of business in this state. If a licensee does not have a place of business in this state, he is still required to pay a license fee."

REPRESENTATIVE MEYER noted his acceptance of that amendment to Amendment 4.

MR. LOHR said that the person that should be consulted is the director of the Division of [Occupational] Licensing and the licensing supervisor who suggested the amendment. He offered to consult with the [licensing supervisor] and hold that portion of the amendment until the next committee of referral.

Number 0394

REPRESENTATIVE ROKEBERG pointed out that the amendment could be conceptual.

CHAIR MURKOWSKI said that she wasn't sure she understood because she thought that one would pay a license fee based on the locations, although it has been determined that there might not be locations within Alaska.

MR. LOHR recommended deleting from Amendment 4, the following language:

> Page 8, line 15:
> Insert new bill section to read:
> ***Sec.**___. AS 21.27.330(b) is amended to read:
> (b) If a licensee that is a firm transacts business at more than one place of business [IN THIS STATE], the licensee shall pay a license fee for each place of business.

MR. LOHR said that the division can deal with the enforcement issue through current statute, if necessary.

Number 0543

REPRESENTATIVE ROKEBERG withdrew his amendment to Amendment 4 and then moved to delete from Amendment 4, the following language:

> Page 8, line 15:
> Insert new bill section to read:
> ***Sec.**___. AS 21.27.330(b) is amended to read:
> (b) If a licensee that is a firm transacts business at more than one place of business [IN THIS STATE], the licensee shall pay a license fee for each place of business.

There being no objection, the amendment to Amendment 4 was adopted.

CHAIR MURKOWSKI withdrew her objection to Amendment 4, and there being no other objection, Amendment 4 [as amended] was adopted.

Number 0597

REPRESENTATIVE ROKEBERG remarked that the July 1, 2002, effective date seemed unusual. For example, the omnibus insurance bill had different effective dates for different sections.

MR. LOHR said that he didn't believe the changes would require substantive retooling by the insurers. Therefore, a uniform effective date [seems appropriate].

REPRESENTATIVE ROKEBERG turned to the MEWA regulations and asked if Mr. Lohr believes [this legislation] has lessened the burden of entering in this market versus the current situation.

MR. LOHR answered, "Most definitely."

REPRESENTATIVE ROKEBERG requested an example of the amount of money that [an insurer] has to put forth for their solvency provisions upon operation.

MS. CAMPBELL directed the committee to the bottom of page 21, which specifies that $200,000 must be deposited with the director to cover insolvency. The language also requires a written plan of operation and the insurer also has to submit financial statements to assure stop-loss coverage.

MR. LOHR pointed out that the current insolvency requirement for insurance companies is $2 million.

REPRESENTATIVE ROKEBERG asked if there is a provision that would allow the money to be released once the plan reached a certain size with a certain balance sheet.

MR. LOHR informed the committee that the capital surplus requirement for an insurance company is a perpetual requirement. These requirements are typically maintained on an interstate basis. A multi-state insurance company isn't required to have a separate dedicated capital surplus reserve for Alaska. The insurance company is allowed to invest the aforementioned [capital surplus revenue]. The capital surplus requirement is maintained for the life of the company.

REPRESENTATIVE ROKEBERG asked whether the money would be deposited with the directors of insurance in the various states.

MS. CAMPBELL explained that the $200,000 requirement is an initial requirement occurring when the [company] qualifies to become a MEWA. The requirement is certified and recommended by a qualified actuary. Ms. Campbell pointed out that this $200,000 is what the [insurer] is actually holding, no additional money is being given to the director; there is merely an initial deposit during startup.

Number 0863

REPRESENTATIVE ROKEBERG presumed that [the insurer] could dip into the [$200,000] fund at a certain point or the director would allow them the use of that money.

MR. LOHR noted that question has come up after the September 11th tragedy. The company must maintain the minimum capital surplus requirement in order to be in good standing. A company seeking a lower level of reserve would have to speak with the regulator. Mr. Lohr informed the committee that Ms. Glover should be available to discuss reserving requirements.

REPRESENTATIVE ROKEBERG turned to page 23, paragraph (5) [of Version J] and inquired as to what that's about.

MS. CAMPBELL answered that ERISA requires that MEWAs hold fidelity bonds. In further response to Representative Rokeberg, Ms. Campbell said that the fidelity bonds have to do with the solvency aspects. Unlike a health insurance company, these MEWAs aren't covered under the guaranty fund and thus there are some additional requirements.

Number 1007

MR. LOHR noted that there have been some MEWA wannabes which have claimed that they are exempt from federal law because they are state regulated and vice versa. In these situations, these [companies] can be turning premium into personal income and never pay a claim. It takes vigilant review and coordination among state regulators to deal with these. Mr. Lohr said that he wasn't sure that [the division] has been able to document any at this time, although there have been some that are located in other states and have written some business in Alaska. This law would assist in [enforcement].

MR. LOHR, in response to Representative Rokeberg, said that the division has had communications with the MEWA forming in Fairbanks. At this time, that MEWA has been informed that it must comply with the full-blown requirements of being an insurance company. The division has also advised this MEWA of HB 246.

REPRESENTATIVE ROKEBERG surmised then that without the passage of this legislation, the MEWA forming in Fairbanks would be put out of business.

MR. LOHR agreed that without this legislation, the requirements would be burdensome.

Number 1164

REPRESENTATIVE MEYER moved to report CSHB 246, Version 22-LS0743\J, Ford, 2/20/02, as amended out of committee with individual recommendations and the accompanying zero fiscal note. There being no objection, CSHB 246(L&C) was reported from the House Labor and Commerce Standing Committee.

The following is Amendment 3:

Page ____, line ____:
Insert new bill sections to read:
"*** Sec. ___.** AS 21.80.060 is amended to read:
Sec. 21.80.060. Powers and duties of the association. (a) The association

(1) is obligated to pay covered claims existing before the order of liquidation and arising within 30 days after the order of liquidation, or before the policy expiration date if less than 30 days after the order of liquidation, or before the insured replaces the policy or causes its cancellation if the insured does so within 30 days after the order of liquidation, but this obligation includes only that amount of each covered claim that is less than $500,000, except that a covered claim for return of unearned premium may not exceed $10,000 for each policy, and except that the association shall pay the full amount of any covered claim arising out of a workers' compensation policy; the association is not obligated

(A) to a policyholder or claimant in an amount in excess of the obligation of the insolvent insurer under the policy from which the claim arises; or

(B) to pay a claim filed with the association after the final date set by the court for the filing of claims against the liquidator or receiver of an insolvent insurer;

(2) is considered the insurer to the extent of its obligation on the covered claims and to that extent has all rights, duties, and obligations of the insolvent insurer as if the insurer had not become insolvent;

(3) shall allocate claims paid and expenses incurred among the three accounts separately, and assess member insurers separately for each account

amounts necessary to pay the obligation of the association under (1) of this subsection subsequent to an insolvency, the expenses of handling covered claims subsequent to an insolvency, and other expenses authorized by this chapter; under this paragraph,

(A) the assessments of each member insurer must **initially** be **based on a uniform percentage, as determined by the association, of** [IN THE PROPORTION THAT] the net direct written premiums of **each** [THE] member insurer for the **last year for which annual statements have been filed** [CALENDAR YEAR PRECEDING THE ASSESSMENT] on the kinds of insurance in the account**; this initial assessment shall be adjusted by applying the same uniform percentage as initially used to each member insurer's net direct written premiums for the calendar year following the year in which the initial assessment was issued; any difference between the initial assessment amount and the adjusted assessment amount allocated to a member insurer shall be levied against or credited back to the member insurer, as appropriate, by the association; the association shall calculate and issue all appropriate levies and credits as soon as practical after all member insurers have filed their annual statements for the calendar year following the year in which the initial assessment was issued** [BEARS TO THE NET DIRECT WRITTEN PREMIUMS OF ALL MEMBER INSURERS FOR THE CALENDAR YEAR PRECEDING THE ASSESSMENT ON THE KINDS OF INSURANCE IN THE ACCOUNT; EACH MEMBER INSURER SHALL BE NOTIFIED OF THE ASSESSMENT NOT LATER THAN 30 DAYS BEFORE IT IS DUE];

(B) **on an annual basis, the association shall determine if funding is required for any of the three accounts; based on this determination, the association shall, during November of each year, issue initial assessments as may be necessary to cover the projected reasonable costs of claims and expenses to administer the association for the following year; the association shall use the services of an independent actuary to assist the association to evaluate and make the projection; an initial assessment may be made at any other time if the association determines funding is necessary, except that** a member insurer may not be assessed **initial assessments** [IN ANY YEAR] on any account **in** an amount greater than two percent of the member insurer's net direct written premiums for the **applicable** calendar year [PRECEDING THE ASSESSMENT ON

THE KINDS OF INSURANCE IN THE ACCOUNT];

(C) the association may pay claims in any order that it determines reasonable, including the payment of claims as they are received from claimants or in groups or categories of claims; however, if the maximum assessment, together with the other assets of the association in any account, does not provide in any one year in any account an amount sufficient to make all necessary payments from that account, the funds available shall be prorated, and the unpaid portion shall be paid as soon thereafter as funds become available;

(D) the association may defer, in whole or in part, an assessment of any member insurer if the assessment would endanger the ability of the member insurer to fulfill the insurer's contractual obligations or cause the member insurer's financial statement to reflect amounts of capital or surplus less than the minimum amounts required for a certificate of authority by any jurisdiction in which the member insurer is authorized to transact insurance; however, during the period of deferment, the member insurer may not pay dividends to shareholders or policyholders; a deferred assessment may only be paid when the payment does not reduce capital or surplus below minimums required by law; a member insurer who pays a larger assessment as a result of a deferment given to another member insurer shall receive a refund when the deferment ends or, at the election of the member insurer, receive a credit against future assessments;

(E) each member insurer may set off against an assessment authorized payments made on covered claims and expenses incurred in the payment of these claims by the member insurer if they are chargeable to the account for which the assessment is made;

(4) shall investigate claims brought against the association, adjust, compromise, settle, and pay covered claims to the extent of the association's obligation, and deny all other claims, and may review settlements, releases, and judgments to which the insolvent insurer or its insureds were parties to determine the extent to which settlements, releases, and judgments may be properly contested;

(5) may, subject to AS 21.89.100, appoint, substitute, or direct legal counsel retained under an insurance policy for the defense of a covered claim;

(6) shall handle claims through its employees or through one or more insurers or other persons designated as servicing facilities; a servicing facility shall operate and maintain its principal office in this state unless the use of a servicing facility located outside of the state would result in operating cost savings of at least 10 percent and would not result in material delay in claim payments; designation of a servicing facility is subject to the approval of the director, but designation may be declined by a member insurer;

(7) shall reimburse each servicing facility for obligations of the association paid by the facility and for expenses incurred by the facility while handling claims on behalf of the association and shall pay the other expenses of the association authorized by this chapter.

(b) The association may

(1) employ or retain those persons necessary to handle claims and perform other duties of the association;

(2) borrow funds necessary to effect the purposes of this chapter in accord with the plan of operation;

(3) sue or be sued;

(4) negotiate and become a party to those contracts that are necessary to carry out the purposes of this chapter;

(5) perform all other acts necessary or proper to carry out the purposes of this chapter;

(6) **retain amounts excess of claims, expenses, credits, and other liabilities in any account to be applied to reduce future assessments in that account, except that, if, in any year, the association determines that significant funds in excess of projected claims, expenses, credits, and other liabilities exist in an account, the association shall return amounts to policyholders, through procedures established by the association, whereby the association reimburses member insurers for providing uniform credits against rates and premiums charged for all policies applicable to the account issued during the next calendar year** [REFUND TO THE MEMBER INSURERS IN PROPORTION TO THE CONTRIBUTION OF EACH MEMBER INSURER TO THAT ACCOUNT THAT AMOUNT BY WHICH THE ASSETS OF THE ACCOUNT EXCEED THE LIABILITIES IF, AT THE END OF ANY CALENDAR YEAR, THE BOARD OF GOVERNORS

FINDS THAT THE ASSETS OF THE ASSOCIATION IN ANY ACCOUNT EXCEED THE LIABILITIES OF THAT ACCOUNT AS ESTIMATED BY THE BOARD OF GOVERNORS FOR THE COMING YEAR].

*** Sec.** ___. AS 21.80.070(c) is amended to read:

(c) The plan of operation must

(1) establish the procedures whereby all the powers and duties of the association under AS 21.80.060 will be performed;

(2) establish procedures for handling assets of the association, including procedures for handling assets received from the estate of an insolvent insurer;

(3) establish the amount and method of reimbursing members of the board of governors under AS 21.80.050;

(4) establish procedures by which claims may be filed with the association and establish acceptable forms of proof of covered claims; notice of claims to the receiver or liquidator of the insolvent insurer is considered notice to the association or its agent, and a list of these claims shall be periodically submitted to the association or similar organization in another state by the receiver or liquidator;

(5) establish regular places and times for meetings of the board of governors;

(6) establish procedures for records to be kept of all financial transactions of the association, its agents, and the board of governors;

(7) provide that any member insurer aggrieved by a final action or decision of the association may appeal to the director within 30 days after the action or decision;

(8) establish the procedures whereby selections of the board of governors will be submitted to the director;

(9) provide for a member insurer serving on the board of governors to appoint an individual to represent the member insurer on the board, including appointment of an alternate or substitute representative for the appointed person;

(10) contain additional provisions necessary or proper for the execution of the powers and duties of the association**;**

(11) establish procedures whereby the association shall, concurrent with making any initial

assessments for the following year under AS 21.80.060(a)(3)(B), determine uniform surcharge percentages that may be applied by member insurers to all policies related to an account;

(12) establish procedures whereby the association shall determine surcharge percentages related to an account so that adjusted assessments match, as closely as possible, the amounts that would be collected by member insurers, in the aggregate, if the surcharge percentages were applied to all new and renewal policies issued by member insurers during the applicable 12-month period; any estimated or actual difference between the aggregate assessment and maximum allowable surcharge amounts related to an account shall be taken into account by the association in determining future surcharge percentages.

*** Sec. ___.** AS 21.80.140 is amended to read:

Sec. 21.80.140. Recognition of assessments in surcharge rates. The rates and premiums charged for insurance policies to which this chapter applies may include **surcharge rates** [AMOUNTS] sufficient to offset the **adjusted assessments** [ASSESSMENT] made under this chapter and paid to the association by [THE] member **insurers** [INSURER LESS AMOUNTS RETURNED TO THE MEMBER INSURER BY THE ASSOCIATION], and these **surcharge** rates may not be considered excessive because they contain an amount reasonably calculated to offset **the full amounted of adjusted** assessments paid by [THE] member **insurers. The association shall notify the director of each surcharge percentage determined by the association, and this surcharge percentage shall be the maximum surcharge rate that may be applied by member insurers related to the assessment, except that a member insurer may make application to the director to apply a higher surcharge rate** [INSURER]. The amount charged on a policy shall be shown separate from the premium for coverage on the policy. [A RATING ORGANIZATION MAY MAKE A PROVISION IN ITS RATE FILING TO RECOVER AN ASSESSMENT UNDER THIS CHAPTER FOR THE ORGANIZATION'S MEMBER AND SUBSCRIBER INSURERS.] The **surcharge rate** [ASSESSMENT CHARGE] is not considered a premium and is not subject to the premium tax imposed under AS 21.09.210."

The committee took an at-ease from 5:23 p.m. to 5:24 p.m.

ADJOURNMENT

There being no further business before the committee, the House Labor and Commerce Standing Committee meeting was adjourned at 5:20 p.m.