

ALASKA STATE LEGISLATURE
SENATE LABOR AND COMMERCE STANDING COMMITTEE

February 3, 2004
1:30 P.M.

TAPE(S) 04-3, 4

MEMBERS PRESENT

Senator Con Bunde, Chair
Senator Ralph Seekins, Vice Chair
Senator Hollis French
Senator Gary Stevens

MEMBERS ABSENT

Senator Bettye Davis

COMMITTEE CALENDAR

SENATE BILL NO. 273

"An act relating to the Alaska seafood marketing institute, the seafood marketing assessment, the seafood marketing tax, and the seafood product tax; and providing for an effective date."

HEARD AND HELD

HOUSE BILL NO. 305

"An act relating to the calculation and payment of unemployment compensation benefits; and providing for an effective date."

HEARD AND HELD

SENATE BILL NO. 276

"An act relating to the Alaska insurance guaranty association; relating to joint insurance arrangements and assessments to the association; relating to the powers of the Alaska industrial development and export authority concerning the association; and providing for an effective date."

HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: SB 273

SHORT TITLE: ASMI BOARD/ SEAFOOD TAXES & ASSESSMENTS

SENATOR(S): STEVENS G BY REQUEST OF SALMON INDUSTRY TASK FORCE

01/23/04 (S) READ THE FIRST TIME - REFERRALS
01/23/04 (S) L&C, FIN
02/03/04 (S) L&C AT 1:30 PM BELTZ 211

BILL: HB 305

SHORT TITLE: UNEMPLOYMENT COMPENSATION BENEFITS
REPRESENTATIVE(S): LABOR & COMMERCE

05/07/03 (H) READ THE FIRST TIME - REFERRALS
05/07/03 (H) L&C, FIN
05/09/03 (H) L&C AT 3:15 PM CAPITOL 17
05/09/03 (H) MOVED OUT OF COMMITTEE
05/09/03 (H) MINUTE(L&C)
05/10/03 (H) L&C RPT 4DP 2NR
05/10/03 (H) DP: CRAWFORD, GUTTENBERG, DAHLSTROM,
05/10/03 (H) ANDERSON; NR: LYNN, ROKEBERG
05/15/03 (H) FIN RPT 6DP 3NR
05/15/03 (H) DP: KERTTULA, BERKOWITZ, FOSTER,
05/15/03 (H) MEYER, HARRIS, WILLIAMS; NR: HAWKER,
05/15/03 (H) STOLTZE, MOSES
05/15/03 (H) FIN AT 8:30 AM HOUSE FINANCE 519
05/15/03 (H) MOVED OUT OF COMMITTEE
05/15/03 (H) MINUTE(FIN)
05/16/03 (H) TRANSMITTED TO (S)
05/16/03 (H) VERSION: HB 305
05/17/03 (S) READ THE FIRST TIME - REFERRALS
05/17/03 (S) L&C, FIN
05/19/03 (S) L&C AT 8:00 AM BELTZ 211
05/19/03 (S) HEARD & HELD
05/19/03 (S) MINUTE(L&C)
02/03/04 (S) L&C AT 1:30 PM BELTZ 211

BILL: SB 276

SHORT TITLE: ALASKA INSURANCE GUARANTY ASSOCIATION
SENATOR(S): RULES BY REQUEST OF THE GOVERNOR

01/23/04 (S) READ THE FIRST TIME - REFERRALS
01/23/04 (S) L&C, FIN
02/03/04 (S) L&C AT 1:30 PM BELTZ 211

WITNESS REGISTER

Senator Gary Stevens
Alaska State Capitol
Juneau, AK 99801-1182

POSITION STATEMENT: Sponsor of SB 273.

Mr. Ray Riutta, Executive Director
Alaska Seafood Marketing Institute (ASMI)
311 N. Franklin
Juneau AK 99801

POSITION STATEMENT: Supports SB 273.

Mr. Brent Paine, Executive Director
United Catcher Boats (UCB)
Anchorage AK

POSITION STATEMENT: Opposes SB 273.

Ms. Donna Parker
F/v Sea Storm
No address provided

POSITION STATEMENT: Supports SB 273 with changes.

Mr. Bruce Schactler, Marketing Chairman
United Fishermen of Alaska
211 4th Street, Suite 110
Juneau, AK 99801-1172

POSITION STATEMENT: Commented on SB 273.

Representative Tom Anderson
Alaska State Capitol
Juneau, AK 99801-1182

POSITION STATEMENT: Sponsor of HB 305.

Commissioner Greg O'Claray
Department of Labor & Workforce
Development
PO Box 21149
Juneau, AK 99802-1149

POSITION STATEMENT: Supports HB 305.

Mr. Bill Kramer, Chief
Unemployment Insurance Program
Department of Labor & Workforce
Development
PO Box 21149
Juneau, AK 99802-1149

POSITION STATEMENT: Supports HB 305.

Mr. Don Etheridge
American Federation of Labor - Congress of Industrial
Organizations (AFL-CIO)
710 West 9th Street

Juneau, AK 99801

POSITION STATEMENT: Supports HB 305.

Ms. Pam LaBolle, President
Alaska State Chamber of Commerce
217 2nd St., Ste 201
Juneau AK 99801

POSITION STATEMENT: Opposes HB 305.

Ms. Linda Hall, Director
Division of Insurance
Department of Community & Economic Development
PO Box 110800
Juneau, AK 99811-0800

POSITION STATEMENT: Supports SB 276.

Mr. Kevin Smith, Executive Director
Alaska Municipal League - Joint Insurance Association (AML-JIA)
807 G Street
Anchorage AK 99501

POSITION STATEMENT: Commented on SB 276.

Mr. Jeff Bush, Deputy Director
Alaska Public Entity Insurance (APEI)
431 N. Franklin, Ste. 301
Juneau AK 99801

POSITION STATEMENT: Commented on SB 276.

Mr. Mike Klawitter, Director
Risk Management
Anchorage School District

POSITION STATEMENT: Commented on SB 276.

ACTION NARRATIVE

TAPE 04-4, SIDE A

^#SB273

SB 273-ASMI BOARD/ SEAFOOD TAXES & ASSESSMENTS

CHAIR CON BUNDE called the Senate Labor and Commerce Standing Committee meeting to order at 1:30 p.m. Present were Senators Seekins, French and Chair Bunde. Senator Davis was excused. Senator Stevens arrived at 1:31 p.m. The first order of business to come before the committee was SB 273.

SENATOR GARY STEVENS, sponsor of SB 273, said the Joint Legislative Salmon Task Force had worked on this bill and it had also been discussed in his marketing subcommittee. He commented:

Very quickly it was apparent to all of us that the Alaska Seafood Marketing Institute (ASMI) is the focus of marketing for Alaska seafood. It's a very important element in the industry and whatever we do to it, we didn't want to damage it any more than it has been. But because of the loss of funding, primarily through salmon, the loss of the value of salmon as well as the volume, that has had an impact on ASMI. So we looked at the bottom line. We realized that ASMI - I believe and the committee believed, as well as the task force - that we need to keep around \$7 million coming into ASMI annually - plus assuming another \$2 million will come in from the federal funding, as well - in order to allow ASMI to do the job it is supposed to do - which is to market seafood products from Alaska. They are the generic marketer and do a very important job.

SENATOR STEVENS said one of the most contentious elements in SB 273 is the reduction in the size of the board from 25 members to nine. His own experience on large membership boards and observations at ASMI's twice-yearly meetings illustrate how difficult it is for 25 members to make decisions and move ahead. Nine is not a magic number, but he could defend nine members as being efficient and the number could always be increased.

Second, ASMI needs to bring in \$7.3 million annually to function properly. Currently, salmon fishermen have a 1 percent tax. Knowing the industry is in crisis, he argued to the salmon fishermen that it should be reduced to .5 percent; but almost to a person, they supported marketing and didn't want to reduce their tax.

SENATOR STEVENS recapped that SB 273 changes the board from 25 to nine members, keeps the 1 percent salmon tax, establishes the .3 of 1 percent processors' tax as mandatory instead of voluntary and levies a new tax on all other seafood products. The 1 percent salmon tax brings in \$1.672 million, the processors' tax would bring in \$3.112 million and all other species would bring in \$2.610 million. He advised the committee to keep an eye on the bottom line and not reduce taxes below \$7 million. ASMI's current \$4.5 million budget is less than it needs to do an adequate job.

CHAIR BUNDE asked Senator Stevens to expand on the controversy surrounding the size of the board.

SENATOR STEVENS elaborated that there are many elements in the fishing industry, all wanting to know how they are represented. If all were represented, the board would have 125 people instead of 25.

You have to assume that a board of nine or whatever the number might be...that the governor appoints and we approve, would really be looking at the whole industry.... I think you have to have a board that represents the whole state and when they're appointed realize they are statesmen, in a way, and not just representing their own particular interests....

He suggested the best solution for getting the board down to nine members, and one that he has already talked over with the administration, is for the governor to ask for all the current members to resign and then establish an entirely new board.

CHAIR BUNDE reminded the committee that ASMI's constitutionality had been an issue in the past and asked if there had been discussion about SB 273's constitutionality.

SENATOR STEVENS said he hadn't heard anything about that issue.

SENATOR SEEKINS asked if the board members were appointed or nominated by the governor for legislative approval.

SENATOR STEVENS replied that board members are appointed by the governor.

CHAIR BUNDE added that the board members are not confirmed by the Legislature.

SENATOR SEEKINS said he didn't know why the word "nominee" on page 1, line 14, is used if the nominee wasn't subject to some sort of approval. He then surmised it was because the nominations were made by people other than the governor. He asked why salmon is taxed at 1 percent and all other seafood products are taxed at only .3 of 1 percent.

SENATOR STEVENS replied that the current tax structure taxes salmon at 1 percent because salmon fishermen are aware of the importance of marketing and see no reason to reduce it.

SENATOR SEEKINS asked if he had received any feedback from the "others" who were going to have a mandatory tax.

SENATOR STEVENS replied that one of the responses was:

You know, I've never put money into ASMI, so I can't complain about what ASMI is doing and actually I wouldn't mind it if some of my taxes went to ASMI, because then I would have expectations of what ASMI does with that money and I could have some demands on how that money is spent.

Other responses from various processing firms and fishermen indicated they don't want any new taxes.

SENATOR SEEKINS reflected that the salmon industry is more distressed than the rest, yet they [salmon fishermen] are paying the most. He asked if other segments of the industry need the marketing support as well or is this assessment meant to be industry's contribution to the salmon marketing effort.

SENATOR STEVENS clarified that even though fishermen of other species have not been taxed, the processors of those species have. He estimated that twice as much money would be coming to ASMI from the processors than from salmon fishermen and almost half again as much from fishermen of other species.

1:47 p.m.

SENATOR HOLLIS FRENCH asked Senator Stevens to elaborate on the elimination of the geographic distribution requirement for board members.

SENATOR STEVENS replied that other fishing organizations in the state, like the North Pacific Fisheries Management Council (NPFMC), operate with fairly small boards and don't geographically divide up the state for their board membership. By dividing the state geographically, the board could conceivably end up with all salmon fishermen on it instead of other parts of the industry being represented. "If you really try to be totally representational by gear type, by fisheries, by geographical area, that way leads to insanity."

SENATOR FRENCH surmised that another danger might be having a nine-member board whose members are all from the Lower Cook Inlet and asked what in the bill would keep that from happening.

SENATOR STEVENS replied that that responsibility is on the shoulders of the governor who does the appointing.

MR. RAY RIUTTA, Executive Director, Alaska Seafood Marketing Institute (ASMI), said ASMI supports SB 273 and thanked everyone for their efforts to help identify the problems it is facing. He related how ASMI has become extremely dependent on federal grants and how the value of [wild] salmon has decreased while the world markets have been flooded with farmed salmon. Funding that comes from the industry to ASMI has decreased in proportion to that decrease in value. Federal grants have been taking up that slack for a number of years, but one grant for \$1 million ends this year and won't be repeated. Another grant for \$2 million is carrying ASMI through this year and partially into next year, but its continuance beyond that is in question.

MR. RIUTTA projected that ASMI would receive \$2 million to \$3 million in federal grants to fund its market access program (export program overseas) and very little other money to support domestic marketing operations. He said the board figures ASMI needs a \$10 million to \$11 million annual budget. ASMI is not asking for an increased budget, but a stable budget that doesn't fluctuate wildly with the swings of the fisheries market. With the estimated \$2 million in federal funds, it needs \$7 million to \$8 million of additional baseline funding. The white fish industry is having the same problems as the salmon industry did 10 years ago. Part of the across-the-board assessment is to help address that problem.

SENATOR SEEKINS asked if the red meat scare had any effect on demand for seafood.

MR. RIUTTA replied that it is too early to measure, but people are increasingly moving from red meat to seafood. The marketplace for seafood has great opportunities in the months ahead.

MR. BRENT PAINE, Executive Director, United Catcher Boats (UCB), Anchorage, said they had been in existence for 11 years and are primarily based in Seattle. They represent most of the catcher vessels that fish for Pollock and cod and half their vessels fish for crab in the Bering Sea. There are 63 member vessels from the roughly 112 catcher boats that fish the Bering Sea for pollock and cod and the 300 vessels that fish for crab. UCB is primarily involved with fisheries at the federal level and less at the state level, since National Marine Fisheries Service is the primary manager of their fishery.

UCB strongly opposes increased taxation on their fleet for marketing services by ASMI for ground fish at this time. He informed them that the pollock fleet in the Bering Sea harvests roughly 600,000 metric tons of pollock a year and they would be responsible for paying almost half of the increased taxation or almost \$1 million.

Members' concerns include not knowing what the money would be used for and that it would address problems in the salmon industry, not in the white ground fish industry. They don't like filling in the gap to solve the falling revenues of salmon fishermen. Marketing of their products is done at a private level through the producers of the final product made from the fish that they catch.

MR. PAINE bewailed the fact that this measure is taxation without representation because most of the Bering Sea fishermen are not Alaskan residents. Further, shrinking the size of the board doesn't allow for representation of all fisheries that are being taxed.

MR. PAINE pointed out that the UCB is made up of fishermen and not marketing experts and he felt that the board needed to be made up of professional marketing people, not necessarily fishermen or processors.

SENATOR SEEKINS asked him to repeat what percentage of his fleet is Alaska owned.

MR. PAINE replied that the fleet that fishes in the Bering Sea is probably about 95 percent non-Alaskan.

2:00 p.m.

MS. DONNA PARKER, F/V Sea Storm, said she and her husband fish for pollock and cod and also own a gillnetter in Southeast Alaska. She is the former fisheries liaison with ASMI and helped draft the original legislation.

She suggested making all the assessments in SB 273 voluntary and felt that the duties of the board should be expanded to all seafoods on a species by species basis. Finally, language in SB 273 proposes to tax the boat, the permit, the quota and all the deck hands and she favored an assessment on the vessel only because:

Having been a fisherman for many years in Kodiak, I know how it filters down to the back deck. These costs are taken off of the top, so we would pay for it at that point - on the expenses of the boat, then taken off the top in terms of expenses for the quota and by the time it got down to us who are on the back deck, we already would have paid for two or three times. So, I think that language should be amended to be a specific assessment to the vessel.

CHAIR BUNDE responded that Senator Stevens was making notes of her concerns for further discussion.

MR. BRUCE SCHACTLER, Marketing Chairman, United Fishermen of Alaska, said he is also president of the United Salmon Association. He felt the tax proposal was fair and had heard the white fish industry vigorously asking for money to begin addressing the marketing problems they foresee in their industry. While he supported a smaller board, Mr. Schactler felt that the issue should be dealt with in separate legislation, because it wasn't connected to taxation at all.

CHAIR BUNDE thanked everyone for their testimony and asked Senator Stevens to notify him when he was ready to hear the bill again.

SENATOR STEVENS thanked ASMI members for their input and reiterated that the real goal is to establish stable long-term funding so that ASMI can continue to operate into the future.

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^#HB305

HB 305-UNEMPLOYMENT COMPENSATION BENEFITS

CHAIR CON BUNDE announced HB 305 to be up for consideration.

2:13 p.m.

REPRESENTATIVE TOM ANDERSON, sponsor of HB 305, said it provides an 8.2 percent increase in the maximum weekly unemployment benefit amount. The increase would be phased in a three-year period and minimizes impact to employers and employees. Alaska currently ranks 47th in the nation with a maximum benefit of \$248. Alaska would rank 28th if the benefit was fully increased to \$308 in 2006. He reminded the committee members that this would not take effect for several years. In 2005, the maximum benefit for base period wages exceeding \$26,750 will increase

and in 2006, the maximum weekly benefit amount will increase for Alaskan's whose base period wages exceed \$29,750. In 2007, wages will be \$32,750.

REPRESENTATIVE ANDERSON concluded by saying that unemployment insurance promotes economic stability and creates a balance for those who are not working.

CHAIR BUNDE reminded the committee that the business community was being impacted with increased workers' compensation assessments, as well.

TAPE 04-3, SIDE B

CHAIR BUNDE asked where Alaska stands among other states in terms of qualification for benefits.

REPRESENTATIVE ANDERSON deferred to the commissioner.

COMMISSIONER GREG O'CLARAY, Department of Labor and Workforce Development, said Governor Murkowski recently launched his Alaska hire program that pressures employers to meet and exceed the 90 percent Alaskan hire rule and the importance of the unemployment benefits are often overlooked. He further apprised the committee that:

Over \$150 million went on the street in unemployment benefits that stayed within Alaska's boundaries. That kept skilled workers here that could afford to remain in Alaska at those rates. I think it's important to remember we haven't had an increase in several years and this particular bill does push out the negative impact or the rate increases some two years from the effective date of the new benefits....

CHAIR BUNDE asked if it was possible for someone to draw Alaska unemployment benefits in another state.

COMMISSIONER O'CLARAY deferred to Bill Kramer, Chief, Unemployment Insurance Program.

MR. BILL KRAMER, Chief, Unemployment Insurance Program, replied that Alaska is part of the National Interstate Benefit Agreement. He explained that a client who has an unemployment claim based on wages he earned while working in Alaska may move about the country and continue to draw benefits based on wages he earned while he was in Alaska.

CHAIR BUNDE asked if he knew how many people do that.

MR. KRAMER replied that about 17 percent of the benefits annually go to interstate clients.

CHAIR BUNDE asked where Alaska ranked among other states for eligibility for the unemployment insurance program.

MR. KRAMER replied that the department tracks the recipient rate and that Alaska ranks within the top 20 percent.

SENATOR SEEKINS asked if someone files for unemployment in a state other than Alaska, are they paid at the Alaska rate.

MR. KRAMER replied that claims are based on Alaska's unemployment insurance law and an individual would be paid based on the wages earned while in Alaska.

CHAIR BUNDE commented: "So, it logically follows that if we're 47th, they might want to move to someplace that was a little higher on the scale than that."

SENATOR SEEKINS asked the commissioner if the zero fiscal note is still accurate.

COMMISSIONER O'CLARAY replied that the fiscal note is still zero. He added that the State of Washington ranks second in the United States for its maximum weekly benefit.

What usually occurs when an Alaskan worker in the construction trades, as an example, moved or relocated in the Washington area, they would choose to return to work in order to get at this [Washington state's] benefit rather than ours. That's the concern that I have in terms of the construction workers - is that we are losing valuable trained workforce - that end up staying south when our construction season starts. And so, it's going to lead to a shortage at some point among our trained journeymen. We're already looking at a 20 percent replacement factor in our journeymen construction workers over the next five years....

SENATOR SEEKINS sought to clarify whether the change in rate would have a fiscal effect on employees of the State of Alaska.

COMMISSIONER O'CLARAY replied that was correct, but the rate increase would happen in 2006.

CHAIR BUNDE added that employers would feel the full impact in 2010 and that employees would be impacted with a 0.4 percent increase.

COMMISSIONER O'CLARAY replied that was correct, but 0.4 percent is not a major increase.

SENATOR SEEKINS said the state would be impacted fiscally in 2006. He explained that in the previous session this bill had a significant fiscal note and now the fiscal note for the same bill is zero. He pondered:

In my mind, I was just trying to figure out, if the State of Alaska were anticipating no one from state employment drawing unemployment, then I understand that it could have a zero fiscal impact. I'm not trying to be argumentative, but just trying to qualify it. I see zeros across the board all the way through 2009, but yet I see an increase in the rate. Is the State of Alaska exempt from that rate increase or does the state participate in that rate increase and, therefore, result in a fiscal note? That's the only thing I am trying to determine.

MR. KRAMER replied that Senator Seekins' thinking is accurate.

The State of Alaska pays dollar for dollar for any benefits that are paid out on their former employees' behalf. So, starting in, depending on when this bill is effective, if it's effective next January 2005, as the department pays out unemployment benefits to individuals whose claims are based on their wages from the State of Alaska, the State of Alaska will receive a bill - dollar for dollar - for any benefits that we pay out. So, there will be some increase in the cost of their benefits, because we will be paying out a higher benefit amount for them.

SENATOR SEEKINS wondered if the fiscal note should be revised for accuracy and clarity.

CHAIR BUNDE noted that the bill's sponsor was taking note of that question. He asked the next person to testify, Don Etheridge.

MR. DON ETHERIDGE, Alaska Federal of Labor - Congress of Industrial Organizations (AFL-CIO), supported HB 305 saying:

This is our third year trying to get something moved through to help the unemployed of our state to be able to remain here.

He related how a laborer who just transferred to Alaska from Washington State was getting ready to move back there because he can survive much better on Washington unemployment payments when he is out of work. "Half my list is talking about moving to Washington and starting to go to work, now."

MR. ETHERIDGE urged the committee to move an immediate effective date rather than January 2005, but said he could live with HB 305 the way it is if it is allowed to move out of committee now.

SENATOR SEEKINS asked Mr. Etheridge to comment on the huge disparity in the construction trades' wages in the State of Alaska versus the State of Washington, because:

At one time, the incentive was for people to remain in the workforce because of the disproportionately higher wage rate that they received up here. Is that still there?

MR. ETHERIDGE replied that wages are not as disproportionate as they used to be and some areas of the country have wages that are higher than Alaska's. He reiterated that:

We are comparable with the state of Washington on most of our construction trades.... There is not a big incentive for them to stay here anymore when they can go down there and make almost as much an hour on the paycheck and benefits and then draw a lot more on unemployment when they aren't working.

He pointed out that tax rates are the major difference.

MS. PAM LABOLLE, President, Alaska State Chamber of Commerce, said qualifications and benefits of the unemployment insurance program have historically been confusing. Few states provide a benefit for dependents and Alaska does. Nearly half of the claims in Alaska include a dependent benefit and the extra \$72 per week puts Alaska in the middle of the pack; the increase

would put Alaska in the top 10 percent. Further, she said the increase would cost employers \$8 million.

MS. LABOLLE said in the past the Chamber of Commerce has supported the first year increase and half of the second increase in the past. She painted the employers' big picture by pointing out that the minimum wage increased last year and a significant workers' compensation increase started just this month, an average increase of 21 percent.

MS. LABOLLE agreed that the Department of Labor would have a zero fiscal note, because it just administers the program, but felt strongly that the state [as an employer] should provide a fiscal note. She informed the committee that Washington State is overhauling its [unemployment] tax structure because companies, like Boeing, are leaving in part or considering leaving totally. Alaska, on the other hand, is trying to create a business friendly climate.

MS. LABOLLE stated that the unemployment insurance program was created for people who become unemployed through no fault of their own. Forty-six states provide for a complete denial of benefits for the duration of a claimant's unemployment until he gets another job, earns a certain level of wages and applies again. Of the other four states, Alaska's policy is the most liberal.

SENATOR SEEKINS asked her to briefly comment on last year's task force on this issue.

MS. LABOLLE responded that the Alaska State Chamber of Commerce was asked to join a working group last year, but because of various scheduling problems, didn't make any of the three meetings. It was not because of unwillingness to attend.

SENATOR FRENCH asked if other states have a separate dependent provision like Alaska's.

MS. LABOLLE replied that Alaska pays \$24 per dependent child up to three children and is one of twelve states that do that. About 44 percent of claimants in 1999 or 2000 received dependent benefits.

SENATOR FRENCH commented that he had just entertained his 15-year old son over the weekend in Juneau and, "Twenty-four dollars would barely get you through the first pizza party."

CHAIR BUNDE set HB 305 aside and encouraged the sponsor to consider the enforcement issues and to try to find middle ground between labor and the chamber.

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^#SB276

SB 276-ALASKA INSURANCE GUARANTY ASSOCIATION

CHAIR CON BUNDE announced SB 276 to be up for consideration.

MS. LINDA HALL, Director, Division of Insurance, recapped:

The Alaska Insurance Guaranty Association (AIGA) is formed under Alaska statute - the purpose is to minimize financial loss to policyholders and claimants. Assessments are made through that guaranty association to pay the claims of insolvent insurers. In July 2003, Fremont Insurance was declared insolvent by the Los Angeles Superior Court and even though they had actively written business for approximately two and a half years, they left \$60 million in claims and outstanding claims reserves. When they were an active insurer in our state, they insured 27 percent of our workers' compensation premium. The magnitude of this insolvency far surpassed any prior insolvency and dramatically exceeds the resources of the association.

There are actually three other insolvent insurance companies in the Guaranty Fund right now. Those are Reliance, Paula and Legion. So, the problem we have was created with the massive insolvency of Fremont, but we're still dealing with four insolvent workers' compensation insurers.

I am asked regularly for the causes, what happened, how did it get here, and they become very technical. I would put forth that generally there are many factors that cause insolvencies in insurance companies - poor management is high on that list, lack of adequate reserving for future claims, and there are allegations that they have lower income due to price discounting. In the case of Fremont, we saw a rapid growth that was unable to be sustained. There have been no allegations of fraudulent behavior, misappropriation of funds - the types of things we read about in some of the large national funds. I would throw that out.

When there are insufficient funds in the Guaranty Association to pay claims, statute allows for the prorating of payments to claimants. That has a great impact on the beneficiaries of the payments from the Guaranty Fund. That prorating today, I just checked statistically yesterday, as of 2/4/04, there are still open claims of 580 injured workers being handled by the Guaranty Association. There were originally approximately 700 Fremont claims; approximately 200 of those have been settled and finalized, but we still have almost 600 injured workers whose claims are being handled.

When a claim is prorated, that injured worker will get a prorated amount of their weekly wage payment; they will get a prorated amount to pay for medical benefits. So, the worker will suffer with the result of that pro-ration. Ultimately, the workers compensation obligation is an obligation of the employer. If there are insufficient funds to pay the claims of the injured workers, that statutory obligation will revert to the employer. So, we have currently - and I checked these statistics yesterday, also - we have currently, claims of 380 employers being handled by the Guaranty Association. So, we have a potential impact of 380 employers who purchase a workers' compensation policy in good faith, who now will get that obligation back. I think that has the potential for a pretty dramatic impact on some of our small businesses that are certainly not prepared for that kind of unanticipated financial cause.

CHAIR BUNDE asked if receiving only a prorated benefit could be viewed as a breach of contract [because workers' compensation law says an injured worker can't sue his employer] and allow the injured worker actionable cause against his employer.

MS. HALL deferred the liability question to Mr. Lisankie and continued to brief the committee:

We are in very uncharted territory. Not only has that never occurred here, to the best of our research ability, it has never occurred any place in the country. So, procedurally, we're really aren't sure what would happen. In likelihood, those injured workers would apply first to the workers' compensation board to enforce that statutory obligation. So, in

that process we would have some forms of litigation whether it was through the Workers' Compensation Board or through the courts for the employer to take back that responsibility for payments.

CHAIR BUNDE said the committee would like expanded information on what the liability would likely be if the Legislature chose not to take any action [going to pro-ration].

MS. HALL informed the committee that for the month of January, the division received a \$2.1 million claims payment and that is the size of the obligation for that month. The payments get smaller as they are projected out in time, because of settlements and workers going back to work. The magnitude of the problems is estimated to reach its maximum [more than \$20 million] in 2008. That is the obligation that would go back to employers, however it is prorated.

2:50 p.m.

MS. HALL said the goal of SB 276 is, "To find a method of securing a stream of funds without a bailout of the industry...."

SB 276 attempts to utilize the traditional philosophy of insurance, which is to spread the risk across a large number of people and to spread the cost of the current crisis across a large population. This is not a popular proposal, because no one wants to pay more.

MS. HALL likened the Guaranty Fund to a safety net to protect policyholders and claimants in the event of a insolvency. It has covered insolvencies for 20 years and works well in other states. She said the policy question the Legislature must decide is, "Do we want to have that safety net in place for the protection of our claimants and our policyholders?"

The Guaranty Fund has three accounts: workers' compensation, automobile and "others" and SB 276 changes how assessments are done.

The first piece of the funding proposal will be to deal with the assessments as they stand today. Currently, there is a statutory cap of 2 percent of assessments made on the line of business - work comp, auto or other and we're proposing that that line of business cap be increased to 4 percent. That

generates, obviously, double the 2 percent cap. Right now we generate \$4.2 million; with our 2 percent assessment it would obviously double. That is a projection. We have \$2.4 million - I just mentioned in January the expenditures were \$2.1 million. So, we're only generating at best with that four months worth of payments of claims.

The second piece of the assessment would be to allow assessing the other two unaffected funds up to a maximum of 2 percent. These two provisions expand the current statutory assessment base just for the cost of the whole crisis. Neither increasing the assessment to pay for the loss of others nor assessing the accounts involved is a popular solution. The Guaranty Fund, again, functions as a safety net and the premise is that the cost of the safety net is spread across the insured population.

MS. HALL explained that the proposed approach, although it's controversial, is not unique to this state [18 other states have one guaranty fund within their property casualty account] and that Alaska already has a .5 percent assessment for homeowners, commercial property, boat and whatever because of the insolvency of one insurance company [primarily] that wrote medical malpractice.

The second piece of SB 276 is the assessment of other entities that are not currently part of the assessment pool, which includes self-insureds and joint insurance arrangements. The division has considered either bringing them into the fund or starting a separate guaranty fund for self-insureds. However, that idea has been tried in other states, but hasn't worked because there is no "hammer" to collect assessments.

MS. HALL informed the committee that her division has oversight of traditional insurance companies, but not for any of the entities she is proposing to assess. That means if she concluded that a financial statement wasn't stable, she couldn't stop the company from continuing to do business.

Therefore, I don't think it's fair to put them in this Guaranty Association. I do recognize that these entities did not create the crisis but, again, the general philosophy of this whole proposal [is] to spread the cost of risk to the broadest possible population.

She has been asked if doing that is fair and her response has been that it may not be fair, but she didn't know if it was fair for the injured worker to suffer a loss of benefits or for a small business employer to get the cost of the claim back. She continued to explain:

The third component of this legislation is the ability to allow [the] Alaska Industrial Development & Export Authority (AIDEA) to provide guarantees for the Guaranty Association to obtain loans. The Guaranty Association by statute currently has the ability to borrow, but they are not really a viable commercial loan prospect. They don't have any assets. Their only asset is the stream of assessments that by the current cash flow projections is going to be used up until 2010. So, we've got six where that would not be available to pay back loans. So on its own, they are not a commercial viable prospect. Legislation does cap the maximum outstanding principal balance at any one time at \$30 million.

We've worked with financial experts to find the most efficient cost effective manner of finding funds and this seemed to be the best route as we've looked at that. We have explored various options with commercial lenders, with other states - insurance companies have been willing to step forward and talk about making loans to the Guaranty Association. As we evaluated the cost of all of those - and cost is of concern, because that repayment cost will still be part of the assessment process, this seemed to be the most viable of all those options....

In closing...SB 276 contains painful, expensive unpopular provisions. I do not believe, however, that the provisions are as painful as doing nothing. I think that the outcomes of doing nothing and allowing prorating and allowing injured workers without immediate access to their payments they have been getting every two weeks, to have employers potentially out of business because they cannot afford this obligation is more painful - more painful to the economy.

I would urge you to focus on the overall major issue at hand. If we allow ourselves to get sidetracked by

each of the individual components of the bill, we have groups that oppose this piece, but not this piece, I don't think we're going to find a solution....

MS. HALL said in the six months since this problem was brought to her attention, she has not found any other viable solutions brought to her, but she is willing to talk about anything that would work.

CHAIR BUNDE noted that she had spread the assessment over the widest possible base of employers only and asked if spreading it over the general public had been considered.

MS. HALL replied no and she wasn't sure of how that would be accomplished. She tried to keep the assessment within the industry.

3:05 p.m.

SENATOR SEEKINS asked why insurance for health and life have separate guaranty associations.

MS. HALL replied that those are separate funds in every state.

SENATOR SEEKINS asked how much money the State of Alaska has in the separate guaranty accounts.

MS. HALL replied that they don't keep cash in the accounts and don't assess until there is a loss [post-loss assessment].

SENATOR SEEKINS asked if that meant they would start being assessed now.

MS. HALL replied that the maximum 2 percent assessments started in August 2003 as soon as this problem became known. The 2004 [for the whole year] assessment was made in January. This is the only way prorating was averted.

SENATOR SEEKINS asked if the assessment included homeowners and auto.

MS. HALL replied no, only a workers' compensation account can be assessed.

TAPE 04-4, SIDE A

SENATOR SEEKINS asked what cash reserves AIDEA has and what the rate of return is, if they are invested.

MS. HALL answered that AIDEA doesn't make loans.

CHAIR BUNDE asked the committee to hold their questions so that people on-line could testify. He noted that this bill would be heard again.

SENATOR FRENCH asked if there was a sunset provision, assuming this bill is adopted and solves the crisis.

MS. HALL replied that she has considered a sunset provision, but she wanted to make sure that the mechanism they use solves not only the current crisis, but provides sufficient ability to handle another crisis down the road.

SENATOR FRENCH commented:

Maybe it's my background as a prosecutor, but when I see a \$60 million hole in the ground that really developed before your watch began, my approach might be to throw somebody in the hole, if I'm being asked to fill it.

He wanted to see some reassessment of the decisions that were made that got the state into this mess.

MS. HALL added that one of the division's major focuses is an analysis of the situation. She said that Alaska veered higher than the national average for a couple of years in the discounting area, but was lower in a number of years. The state's loss ratios have tracked in many ways, although for the last three years it has significantly outpaced national loss averages. Put together with rates and discounting, there has been an overall effect.

MS. HALL said she meets quarterly with regulators around the country and discusses things like solvency regulations. Alaska defers to the state of domicile of an insurer for the oversight of every insurance company that does business in Alaska annually but today, the division is much more aware of the combined impact of discounting, reserving practices and the rate making process.

CHAIR BUNDE said he joined Senator French in asking her for an expanded suggestion for a solution.

MR. KEVIN SMITH, Executive Director, Alaska Municipal League - Joint Insurance Association (AML-JIA), said the JIA is a self insurance program for 140 Alaskan cities, boroughs and school districts that would ordinarily be considered too small to self insure on their own, but as a group are able to take a self insured retention in workers' compensation of \$300,000 and purchase excess insurance above that.

AML-JIA pays an actuary to calculate the estimated losses in the self-insured retention layer. The estimate is a best guess figure and, if the guess is too low, the JIA already has a mechanism to assess its own membership to come up with the cash. The AML-JIA is not entitled to and does not expect or need access to the Alaska Guaranty Fund.

MR. SMITH said he estimated that \$1 million of the proposed assessment would come from the self-insured employers - \$317,000 from the State of Alaska and about \$500,000 from local governments and school districts. About \$90,000 would come from the AML-JIA and be due in this fiscal year with no prior notice. He said the AML-JIA does not have the funds that an insurance organization, which shows profits to stockholders, does.

AML-JIA's goal is to run on a narrow margin. It would have to ask for additional monies from local governments that are already struggling with retirement issues, the increasing cost of health insurance, diminishing revenue sharing and municipal assistance and increased costs in workers' compensation.

MR. SMITH said he did not think asking for a user fee from people who can't use the fund is good public policy.

Is it fair? No, it's not fair. It's not even right. Essentially, this money would have to come from the classrooms; this money would come from police departments; this money would come from snow removal budgets and I would ask that we eliminate the self-insureds and the joint insurance arrangements from the bill.

SENATOR SEEKINS said that most entities in the AML have the ability to raise taxes locally.

MR. SMITH replied that is theoretically correct and that is why joint insurance arrangements are restricted to public entities only [and not entities like tribes, for example].

SENATOR SEEKINS reasoned that if those employers had to share in this unexpected burden along with the private sector, they would have a mechanism to recover those losses.

MR. SMITH replied that would depend on the size of the community. Some communities, like Koyuk, would have to figure out how to survive.

SENATOR SEEKINS asked if those same entities were asking the non-public employees of the State of Alaska to jointly help them address the PERS and TRS shortages.

MR. SMITH replied that was beyond his scope to comment on.

SENATOR GARY STEVENS asked where a school district that was at its cap already could get funds.

MR. SMITH responded that he is not a school finance expert, but in that case, it would seem that securing those funds would have to be taken from the classroom.

CHAIR BUNDE thanked him for his testimony.

MR. JEFF BUSH, Deputy Director, Alaska Public Entity Insurance (APEI), said he represents 27 Rural Education Attendance Areas (REAAs) and school districts and 12 municipalities. Based on National Council on Compensation Insurance (NCCI) estimates, local government workers' comp premiums could go up 22 - 32 percent. The proposal in SB 276 talks essentially about a tax on top of that premium increase.

MR. BUSH emphasized the fact that school districts don't have the power to tax, making it difficult to come up with extra money. "So, it would, in fact, come out of the classroom and many of our school districts around the state are struggling right now...."

He added that many municipalities don't have powers of taxation, because they are in the unorganized borough.

MR. BUSH said APEI would be charged approximately \$32,000 this year if SB 276 passes. He joined Mr. Smith in saying that assessing APEI is not fair because it does not participate in the [Guaranty Fund] program and their local funding would go to subsidizing the program. He asked the committee to delete

sections of the bill that apply to joint insurance arrangements and self-insureds.

MR. MIKE KLAWITTER, Director, Risk Management, Anchorage School District, said SB 276 would cost the school district \$127,000 in unexpected and unfunded assessments or about 2.5 teaching positions. He pointed out that the district could not use the [Guaranty] fund in any way.

CHAIR BUNDE thanked Mr. Klawitter for his testimony and said he would hold the bill for further work. There being no further business to come before the committee, he adjourned the meeting at 3:27 p.m.

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