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SENATE COMMITTEE REPORT

FIRST COMMITTEE OF REFERRAL

Date of 5-DAY NOTICE 4/7/89 *Waived*
IN ACCORDANCE WITH UNIFORM RULE 23

FURTHER

**FISCAL NOTE(S) MUST BE ATTACHED
IN ACCORDANCE WITH AS 24.08.035

DATE TURNED INTO OFFICE 4/10/89

4/4/89
Mr. President:

FINANCE Committee considered SB 258

state exemption from certain insurance premium taxes; efd

and recommended:

- replace with CS SB 358 (Fin) same title
- attached amendment(s) and new title
- _____ letter of intent adopted

do pass

do not pass

no recommendation

individual recommendations

further referral to _____

FISCAL NOTE(S) attached ^{DELETED} zero
 appropriation no FN attached

fiscal impact
 Gov. FN introduced w/ bill

MEMBERS SIGNING DO PASS

OTHER RECOMMENDATIONS

[Handwritten signatures]

Committee backup attached

Chair: signature and recommendation

[Handwritten signature] Co-CHAIR

[Handwritten signature] DO PASS

R/o SFC 4-10-89

STATE OF ALASKA
1989 LEGISLATIVE SESSION

BILL VERSION: CS SB 258 (Finance)
PUBLISH DATE: _____

FISCAL NOTE

REQUEST:

Revision Date: _____ Agency Affected: Commerce & Econ. Dev.
Title: State exemption from certain BRU: Insurance
insurance premium taxes
Sponsor: Rules (Health Care Cost Components: _____
Requester: Senate Finance /Containment Task Force)

EXPENDITURES / REVENUES : (Thousands of Dollars)

OPERATING	FY 89	FY 90	FY 91	FY 92	FY 93	FY 94
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0	0	0	0	0	0

CAPITAL	0	0	0	0	0	0
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REVENUE	0	0	0	0	0	0
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FUNDING: (Thousands of dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL	0	0	0	0	0	0

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME						
TEMPORARY						

ANALYSIS: (Attach a separate page if necessary.)

Prepared by: Paul Roller, Director Phone: 465-2515
Division: Insurance Date: 4-7-89

Approved by Commissioner: Larry Mercurieff Phone: 465-2500
Agency: Department of Commerce & Economic Development Date: 4/10/89

Distribution (by preparer):

- Legislative Finance
- Legislative Sponsor
- Requestor
- Office of Management and Budget
- Impacted Agency(ies)

Changes in the Fin CS have no fiscal effect. This fiscal note is appropriate. SFC: 4/10/89

page ____ of ____

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Original sponsor: Rules/Health Care Cost
Containment Task Force

1 IN THE SENATE

BY THE FINANCE COMMITTEE

2 CS FOR SENATE BILL NO. 258 (Finance)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 SIXTEENTH LEGISLATURE - FIRST SESSION

5 A BILL

6 For an Act entitled: "An Act relating to the state exemption from certain
7 insurance premium taxes; and providing for an effec-
8 tive date."

9 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. AS 21.09.210(i) is amended to read:

11 (i) Premiums paid by the state for insurance policies and con-
12 tracts purchased under the provisions of AS 39.30 are exempt from
13 taxation under this section. An insurer may not include the tax
14 imposed under this section in a premium charged on an insurance policy
15 or contract purchased by the state under the provisions of AS 39.30.
16 An insurer may claim the [CLAIMS FOR] exemption [SHALL BE MADE] on
17 forms provided by the division of insurance.

18 * Sec. 2. This Act takes effect January 1, 1989.

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OFFICE OF THE PRESIDENT

MEMBER

TENTH ALASKA LEGISLATURE
ELEVENTH ALASKA LEGISLATURE
TWELFTH ALASKA LEGISLATURE
THIRTEENTH ALASKA LEGISLATURE
FOURTEENTH ALASKA LEGISLATURE
FIFTEENTH ALASKA LEGISLATURE
SIXTEENTH ALASKA LEGISLATURE



SENATOR TIM KELLY

APR 6 1989

P.O. BOX V
JUNEAU, ALASKA 99811
(907) 465-3822

P.O. BOX 210001
ANCHORAGE, ALASKA 99521
(907) 561-7612

April 6, 1989

Senator Rick Uehling, Co-chair
Finance Committee
Alaska State Senate
Box V
Juneau, Ak 99811

Re: Scheduling SB 257 and SB 258.

Dear Senator Uehling,

I would appreciate the scheduling SB 257 and SB 258 for a Finance Committee hearing at your earliest convenience. These two bills are recommended by the Health Care Cost Containment Task Force. They are in the nature of technical changes to existing law. Their enactment would allow the Department of Administration to affect substantial health care cost savings for both FY 89 and FY 90.

For your information, the Task Force will be meeting again on Wednesday, April 12.

Thank you for your consideration of this request.

Sincerely,

A handwritten signature in cursive script that reads "Tim".

TIM KELLY
Alaska State Senator

SB 258

2.01 PREMIUM TAXES

Currently, required by State Law (AS 39.30), Aetna charges a premium tax based upon the total premium collected, applies for a tax refund at the end of the year, and then credits the retention charge.

During our review, it was discovered that Aetna had collected the 1987 calendar year refund, but it had not been credited. The 1988 refund has not been applied for as of yet (estimated 1987 credit \$1,650,000, estimated 1988 credit \$1,750,000, for a total of \$3,400,000).

It is recommended that Aetna reduce the premiums due during remaining year 1989 by the amount of the 1987 & 1988 tax credit.

2.01A AS 39.30

This law should be amended to exempt the State from paying this premium tax. It would simplify the administration and retain the money in Alaska.

STATE OF ALASKA HEALTHCARE COST CONTAINMENT TASK FORCE

Provided by: Arthur J. Gallagher & Co.
Aetna Life Insurance Company

April 3, 1989

At its March 29, 1989 meeting, the Healthcare Cost Containment Task Force requested additional information on three financial issues. The following material provides Arthur J. Gallagher's and Aetna's comments on the three issues.

1. **Premium Taxes.** There is a great deal of confusion on the Premium Tax issue. Currently, premium taxes are paid to the State on the Health plans and then Aetna files for a refund of the taxes. Thus, the net effect on the plan should be zero. In determining the State's premium rates it is assumed there is no tax liability.

In order to recover the 1987 tax credit of \$1,700,000 (\$1,300,000 active and \$400,000 retirees) the following needs to occur:

1. Combine plan financials at year end. This allows Aetna to cross apply Premium Stabilization Account Funds.
2. The State Revenue Department has to issue 1988 premium tax refund to Aetna prior to July 1, 1989.
3. Section 1 AS21.09210 (i) is amended effective January 1, 1989.

Aetna will credit \$1,700,000 as directed by administration.

2. **Extended Liability Reserves.** Under the State's plan there is an extension of benefits which continues Medical coverage for up to 12 months for employees who are totally disabled at contract termination. This is deferred liability which cannot be measured while the plan is active.

Aetna provides for this liability by establishing reserves at each renewal. The extended liability reserves established as of the July 1, 1988 renewal are as follows:

	<u>Extended Liability</u>	<u>Extended Maturity</u>	<u>Total</u>	<u>80%</u>
Actives	\$2,178,045	\$857,139	\$3,035,184	\$2,400,000
Retirees	1,162,282	27,189	1,189,471	900,000

Note: These reserves were outlined on page 18A of Arthur J. Gallagher's March 29, 1989 Report on the Task Force.

Aetna would be agreeable to transferring the extended liability to the State in the event of contract termination. With the transfer of liability, 80% of the reserves would no longer be required. The remaining 20% of the reserves would be required to provide for extended liabilities while the contract is in force.

To accomplish the transfer of liability, Aetna would need to make a change to the contract with the State. Also, a notice would need to be provided to employees indicating that the State has assumed this liability.

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If the State wishes to proceed with this change we would need an effective date. Once implemented, Aetna would credit the State for that portion of the reserves. Aetna will credit Extended reserves of \$3,300,000, as directed by Administration.

3. **Minimum Premium.** Aetna has a minimum premium product available called the Split Funded Group Plan (SFGP). There are two types of SFGP available: one where Aetna retains terminal liabilities and reserves, and one where terminal liabilities and reserves are transferred to the State. All further discussion will assume the State is responsible for terminal liabilities and reserves.

The following table outlines the reserves available to the State:

	<u>Actives</u>	<u>Retirees</u>
July 1, 1988 Reserves:		
Unpaid claim	\$ 7,808,469	\$4,127,414
Extended Liability	<u>3,035,184</u>	<u>1,189,471</u>
Total	\$10,843,653	\$5,316,885
Estimated Float Claims	<u>-2,175,000</u>	<u>-925,000</u>
	\$ 8,668,653	\$4,391,885
Reserve Release Charge	<u>-346,746</u>	<u>-175,675</u>
Net Reserve Release	<u>\$ 8,321,907</u>	<u>\$4,216,210</u>

Note: SBS Option I benefits are combined with basic benefits to avoid producing two separate claim transactions and the expenses associated with two transactions. It is assumed that Option I would also convert to SFGP to continue these expense savings.

Aetna would need to retain a portion of the reserves to cover "float" claims outstanding on the conversion date. Float claims are those claims where a claim check has been issued but not recorded as paid. The liability is estimated to be approximately two weeks of claims.

In addition, if the reserves are released in a lump sum there is a charge made to cover the opportunity costs associated with the conversion of assets to cash. Currently, the charge is equal to 4% of the lump sum payment. The charge would be waived if the reserves were released in 12 installments.

Upon the conversion to SFGP, Aetna's costs would increase as follows:

	<u>Actives</u>	<u>Retirees</u>
Lost Interest	\$ 867,492	\$425,351
Banking and Administration	86,000	37,000
Additional Risk	<u>54,218</u>	<u>26,584</u>
TOTAL	<u>\$1,007,710</u>	<u>\$488,935</u>

Currently, Aetna is crediting interest to the State on the claim reserves at an annual rate in the range of 7.5% to 8.5%. This interest is used to offset some of the expenses under the plan. Once released, the net expenses increase by the amount of the lost interest. Aetna has assumed 8% in this illustration.

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The banking and administration charges cover the added costs associated with SFGP. Although terminal liabilities and reserves shift to the State, Aetna guarantees payment of these liabilities in the event the State cannot provide the funds. Aetna assesses an additional risk charge for this guarantee. The risk charge could be waived if there is Letter of Credit for 120% of the reserves.

It would be necessary to increase the "conventional" premium rates to provide for these additional expenses.

Under a SFGP arrangement, the following additional documents are required to implement SFGP:

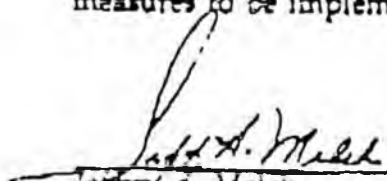
- The Letter of Intent (Exhibit A) outlines the State's desire to implement SFGP and accepts in principal the various Agreements.
- The Banking Agreement (Exhibit B) sets up the wire transfer of funds between the State and Connecticut National Bank.
- The Split Funded Agreement (Exhibit C) amends the insurance contract and outlines the various terms and conditions of the arrangement.
- The Retrospective Premium Agreement (Exhibit D) provides for the call on any unused Claim Liability Limit to fund an accounting deficit.
- The Termination Liability Fund (Exhibit E) is necessary to assure that adequate reserve funding is available at all times.

In addition to these documents, a notice needs to be sent to the employees announcing the change to SFGP.

Under SFGP, the conventional premium would be split into two components. A basic premium component equal to the estimated expenses would be developed and paid to Aetna monthly. The basic premium level is not guaranteed and would be "trued up" at year end based upon actual plan costs. The remainder of the conventional premium would be retained by the State's for claim payment.

Due to associated costs and ease of administration, it is recommended that the State review Split Funding where Aetna retains terminal liabilities and reserves. The net impact of this on FY 89, 90 depends upon the actual claims paid and the State's accounting practices.

It is further recommended that the Task Force continue to pursue Cost Containment measures to be implemented in FY 90.


 Jeffrey A. Malek
 Assistant Area Vice President
 Employee Benefits
 Arthur J. Gallagher & Co.


 Philip B. French
 Assistant Vice President
 Western Home Office
 Aetna Insurance Co.