



Legislative Fiscal Bureau

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Joint Committee on Finance

Paper #543

Treatment of Certain Revenues (Insurance)

[LFB 2001-03 Budget Summary: Page 427, #14]

CURRENT LAW

Ninety percent of revenues from license fees and other fees charged by the Office of the Commissioner of Insurance (OCI), fees paid by examinees to pay for the costs of OCI examination expenses and publication sales are credited to the agency's program revenue, general operations appropriation. The remaining 10% of these revenues are deposited to the general fund as GPR-earned revenues.

GOVERNOR

Specify that 90% of the revenues OCI collects to pay for: (a) expenses involved in the conversion of a domestic mutual to a stock corporation; and (b) reasonable costs incurred by OCI in employing experts to assist with industry examinations or reviews be deposited to the agency's program revenue, general operations appropriation. The remaining 10% of these revenues would be deposited to the general fund as GPR-earned revenues.

DISCUSSION POINTS

1. OCI is funded primarily from program revenue generated from license fees and other fees, fees paid by examinees to pay for the costs of OCI examination expenses and publications sales. In addition, OCI administers three insurance funds -- the patients compensation fund, the state life insurance fund and the local government property insurance fund -- that are supported by revenues contributed by participating individuals and local governments.

2. Requiring OCI to deposit 10% of the revenue the agency collects from specified revenues requires OCI to charge fees equal to approximately 111.1% of costs the agency would

otherwise charge to fully recoup the agency's costs. For example, for every \$100 in costs the agency incurs to provide a service, it must collect approximately \$111.10 in revenue that is subject to the 10% requirement, since OCI must deposit 10% of this revenue (approximately \$11.11) to the general fund and retains \$100.00 to support its costs of providing services.

3. In fiscal year 1999-2000, OCI deposited \$1,447,800 to the general fund as GPR-earned. These funds are intended to offset general state infrastructure costs, overhead and other services that support state employees and operations. This GPR revenue requirement recognizes that the agency receives indirect support from GPR-funded functions.

4. Current law does not specify how revenues that OCI receives to pay for their expenses involved in employing experts to assist with industry examinations and reviews, or in reviewing and approving certain conversions of insurance companies are to be treated.

5. Current law requires 10% of receipts that OCI receives from fees charged for examinations of insurance companies be deposited to the general fund. In practice, OCI has been including the costs of employing experts to assist with industry examinations in the agency's calculation of total costs charged to the insurance company that is subject to an examination, and depositing 10% of these total assessments to the general fund. Therefore, the proposed statutory change relating to the costs of employing experts would codify current practice, and no additional revenues would be deposited to the general fund if this provision were enacted.

6. The effect of the proposed statutory change relating to expenses involved in certain types of conversions of insurance companies is less clear. The statutory cite directly affected under the bill applies to conversions of domestic mutual companies to stock corporations. However, two other types of conversions – conversion of a nonprofit service insurance corporation to a stock insurance corporation and conversion of a for-profit insurance company to a stock insurance corporation - could be affected, through cross-references, depending on the interpretation of the language.

7. The proposed statutory change was based on a request submitted by OCI as part of its 2001-03 biennial budget to clarify the treatment of revenues received for reimbursement of OCI expenses related to the conversion of Blue Cross Blue Shield United of Wisconsin (BCBS), a conversion of a nonprofit service insurance company to a stock insurance corporation. OCI's request was the agency's response to an opinion of the State Controller as to how to treat the amounts OCI received as reimbursement for the costs it incurred in the conversion of BCBS. The State Controller consulted with the Department of Administration legal counsel and the State Budget Office and indicated, in a July 28, 1999, memorandum to OCI, that it was the State Controller's opinion that 100% of revenues from these types of conversions should be deposited to OCI's PR appropriation and none of these revenues should not be deposited to the general fund. The Controller also suggested that the language governing OCI's general program operations be modified to clarify that 100% of those revenues would be deposited to the PR appropriation.

8. Based on the Controller's opinion, OCI has retained 100% of the moneys it has

received from the BCBS conversion to cover the expenses OCI has incurred in its regulatory review of the conversion. In addition, OCI proposed a statutory change in its 2001-03 budget request to clarify that OCI would retain 100% of such revenues in the future. Instead of including the language requested by OCI in the bill, the Governor recommended that these types of revenues be treated in the same manner as other general operations revenues that OCI receives so that 10% would be deposited to the state's general fund. Based on the intent of the request, and the Governor's response incorporated in the budget bill, it would seem appropriate to modify the bill to clarify that the provision would apply to each of the different types of conversions that are cross-referenced to the reimbursement provision included under the bill to meet the Governor's intent.

9. OCI charged BCBS a total of \$784,400 in 1999-00, and \$214,800 through February, 2001. If the provision requiring OCI to deposit 10% of those revenues had been in effect in the 1999-01 biennium, OCI would have charged approximately \$87,200 in 1999-00 and \$23,900 in 2000-01 more than it charged BCBS and deposited those amounts to the general fund.

10. OCI indicates that some conversions, such as the conversion of a nonprofit insurance company to a stock insurance corporation, are very complex and require investment banker expertise to determine the value of the company and provide information related to stock transactions. Because of the complexity of these issues, the majority of costs involved in the Blue Cross and Blue Shield conversion were private consulting fees. Of the total costs of the conversion, consulting fees comprised \$590,400 (75% of the total conversion costs) in 1999-00 and \$206,500 (96% of the conversion costs) to date in 2000-01.

11. Because most of the expenses that OCI incurs in these types of conversions are private consulting fees that are passed through OCI to the converting company, it could be argued that adding an additional 11.1% on to the cost in order to deposit 10% of the revenue to the general fund is not warranted. On the other hand, the state does incur costs in the transaction. OCI administers the request for proposal process, hires the consultants, processes billings and monitors the transactions and expenses.

12. It is not possible to provide a reliable estimate of the amount of additional revenue that would be deposited to the general fund under the Governor's recommendation. The Governor's bill does not assume that additional revenue to the general fund will be available because of the proposed statutory change. The Insurance Commissioner gave final approval of the BCBS conversion on March 19, 2001, and the conversion took effect on March 23, 2001, when OCI issued the amended certificate of authority. OCI does not anticipate any further costs relating to the BCBS conversion in the 2001-03 biennium. Further, it is difficult to project future conversion proposals because a decision to convert is made at the discretion of the insurance company's board of directors. Typically, a company's management meets with OCI only shortly before filing for a conversion.

13. There are several other types of conversions for which the converting company is required to reimburse OCI for the agency's expenses. One could argue that treating the reimbursement expenses for different types of conversions differently would be arbitrary. For

example, 1997 legislation established a separate appropriation for restructuring expenses for mutual insurance companies that convert to mutual holding companies. To date, no revenues or expenditures have been credited or made from this appropriation. However, OCI is currently reviewing a conversion proposal submitted by the Employers Insurance of Wausau. OCI officials indicate that total expenses involved in the conversion will likely be less than \$50,000. None of this is, nor would it be under the bill, subject to the requirement that 90% of revenues be retained by OCI and 10% be deposited to the general fund.

14. Because, there is no policy rationale for making some types of conversions subject to the 90% provision, and some types of conversions not subject to the provision, the Committee could extend the provision to all types of conversions in which OCI receives reimbursement for its costs. Alternatively, the Committee could delete the Governor's recommended statutory change and instead clarify that revenues the agency receives relating to OCI's review of all conversions would be exempt from the 90% provision, as requested by OCI in its 2001-03 biennial budget submission.

15. In addition, while a separate continuing, program revenue appropriation was created for restructuring holding companies, other types of conversions are funded through OCI's annual general operations appropriation. For complicated conversions that involve a high level of OCI expenses, such as the BCBS conversion, the expenditure authority limit on the annual appropriation restricts OCI's ability to evaluate the proposed conversion until additional expenditure authority is approved under the s. 16.515 process.

16. State statutes require companies to gain approval from the Insurance Commissioner before restructuring. In order to effectively evaluate some of these types of conversions, OCI requires consultants to provide expertise in evaluating and advising the Commissioner as to how to proceed with the company's proposal to convert. Given that these requirements were created to protect the public, OCI officials indicate that they should be able to proceed without the delay and uncertainty of obtaining expenditure authority under s. 16.515. This appears to be the intent of the 1997 legislation, which established a separate, continuing appropriation for restructuring holding companies. This appropriation could be modified to apply to other types of conversions in which OCI receives reimbursement, if the Committee wanted to allow the Commissioner the same flexibility to provide services for other types of conversions.

17. On the other hand, except for the Blue Cross and Blue Shield conversion, OCI has been able to fund expenses related to conversions with funds budgeted in its PR general program operations appropriation. Therefore, it may not be necessary to modify the statutes to provide that all conversions be funded from a modified, continuing appropriation at this time.

ALTERNATIVES

A. Treatment of Agency Revenues

1. Approve the Governor's recommendation, as modified, to specify that 90% of the

revenues OCI collects to pay for: (a) expenses involved in the conversion of a domestic mutual to a stock corporation, a nonprofit service corporation to a stock insurance corporation and a for-profit service insurance corporation to a service corporation; and (b) reasonable costs incurred by OCI in employing experts to assist with industry examinations or reviews be deposited to the agency's program revenue general operations appropriation. The remaining 10% of these revenues would be deposited to the general fund.

2. Modify the Governor's recommendation to specify that 90% of the revenues OCI collects to pay for expenses involved in all types of conversions for which OCI receives reimbursement be credited to the agency's program revenue general operations appropriation.

3. Delete the Governor's proposed change in the allocation of revenues the agency receives to support the agency's costs of reviewing conversions. Instead, clarify current law to exempt revenues the agency receives to support the agency's costs of reviewing conversions from the 90% provision.

B. Use of Separate Appropriation for Conversions

1. Modify the appropriation for holding company restructuring expenses to apply to all types of conversions for which OCI receives reimbursement for their expenses.

2. Maintain current law.

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