

# ARIZONA STATE SENATE

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46TH LEGISLATURE  
FIRST REGULAR SESSION

## MINUTES OF COMMITTEE ON APPROPRIATIONS

**DATE:** March 26, 2003

**TIME:** 1:30 p.m.

**ROOM:** SHR 109

**CHAIRMAN:** Senator Burns

**VICE CHAIRMAN:** Senator Waring

**ANALYST:** Deborah Johnston  
Carolyn Atwater

**COMMITTEE  
SECRETARY:** Tracey Moulton

**INTERNS:** Benjamin Wing  
Christopher Kresge

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### ATTENDANCE

### BILLS

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<u>Committee Members</u>	<u>Pr</u>	<u>Ab</u>	<u>Ex</u>	<u>Bill Number</u>	<u>Disposition</u>
Senator Anderson	X			HB 2152	DPA
Senator Arzberger	X				
Senator Bee	X				
Senator Cannell	X				
Senator Giffords	X				
Senator Harper	X				
Senator Martin	X				
Senator Mead	X				
Senator Rios	X				
Senator Soltero	X				
Senator Verschoor	X				
Senator Waring, Vice Chairman	X				
Senator Burns, Chairman	X				

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### GOVERNOR'S APPOINTMENTS

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Chairman Burns called the meeting to order at 1:35 p.m. and attendance was noted.

## **APPROVAL OF MINUTES**

**Senator Burns announced without objection, the following minutes be APPROVED as distributed: February 26, 2003, March 5, 2003 and March 12, 2003.**

## **CONSIDERATION OF BILLS**

### **HB 2152 –captive insurers– DO PASS AMENDED**

**Denisse Gee, Research Analyst**, explained HB 2152 allows the formation of several new types of captive insurers (captives) and permits the Department of Insurance (DOI) to retain a portion of fees collected from the licensing of captive insurers to administer the captive insurance program. She stated that H.B. 2152 allows the formation of agency captives, protected cell captives and expanded forms of group captives. This legislation also allows DOI to use a portion of fees collected from captive insurance licensing to promote and regulate the captive insurance program. Currently, the captive insurance program is funded by an annual appropriation of \$93,000. According to DOI, expanding the captive insurance program will not require additional monies on top of the \$93,000 annual appropriation. Additionally, DOI contends that in three fiscal years it will no longer need the \$93,000 annual appropriation because there will be enough captive insurers holding certificates of authority to fund the captive insurance program through licensing and renewal fees.

Ms. Gee noted that the Finance Committee passed an amendment that clarified that captive insurer that provide workers compensation must still qualify under the current self-insurance statute. This language is the result of discussions between the Industrial Commission of Arizona and the DOI and there is no opposition to the amendment.

Ms. Gee explained the 4-line Burns amendment dated 3/24/03, 3:12 p.m. subjects all monies in the captive insurance regulatory and supervision fund to legislative appropriation authority and makes a clarifying change.

In response to Senator Harper, Senator Burns commented that the State would not own the fund, but rather the Legislature would authorize the amount of money that could be spent from the fund each year. Ms. Gee stated that the \$93,000 is a current appropriation already approved.

Senator Harper stated that the \$93,000 is seed money, just like the Legislature gave the State Compensation Fund (SCF).

Senator Burns commented that the two funds are not comparable. He stated that the SCF was a constitutional requirement and there is no requirement of any kind to create this particular insurance setup.

In response to Senator Harper, **Debbie Johnston, Research Analyst**, explained that the workers compensation fund is the result of a constitutional requirement. The SCF was one mechanism by which the State started to provide workman's compensation insurance for those companies that were not able to access insurance in the private market place. She stated that the way the SCF was established is different than this fund and most other funds that the State administers. She

remarked that this is a fund that would be comprised of fees that the State assesses on captive insurers and used for the operation of DOI to regulate those insurance companies as well as provide for marketing. She stated that this would be a normal regulatory fund and the way that the bill is drafted, the fund is continuously appropriated and the Burns amendment subjects the fund to Legislative appropriation.

Senator Harper asked if the Legislature would have access to the fund and be able to "sweep" the seed money back from the fund should the fund grow to a sizable level. Ms. Gee stated that the amendment would require DOI to request an appropriation from the Legislature each year. She noted that should the Legislature decide to reduce or increase the appropriation, that would be under the purview of the Legislature.

Carolyn Atwater, Research Analyst, referring to page 15 of the bill, stated that all unencumbered monies in the fund exceeding \$100,000 revert to the State general fund at the end of each fiscal year.

**Senator Waring moved HB 2152 be returned with a DO PASS recommendation.**

**Senator Waring moved the 4-line Burns amendment dated 3/24/03, 3:12 p.m. be ADOPTED (Attachment A). The motion CARRIED by voice vote.**

Senator Burns announced the individuals who registered their position on the bill (Attachment B).

**David Childers, Law Firm of Low and Childers**, testified in support of the bill and remarked his firm has formed a number of captives around the country and out of the country. He noted that this legislation would probably not affect his firm.

Mr. Childers stated that there have been six captives formed under this law and anticipates that Arizona will eventually become an attractive captive domicile. The changes that are being made in HB 2152 make it much more attractive and competitive with the laws in Vermont, Hawaii and South Carolina, which are the three most prominent of the 21 captive jurisdictions in the country.

Mr. Childers commented that the captive industry is a lucrative industry. He stated that the estimates are that in Vermont the industry generates approximately \$1 billion or more to the Vermont economy every year with approximately 600 captives. Arizona currently has 100 captives, and he opined that Arizona would provide competition to those other states. He noted this legislation would give commercial entities that are having difficulty in getting insurance an attractive alternative that has not been available in the past.

Mr. Childers remarked that he was in support of the bill and stated that he was not necessarily in support of making funds a legislative appropriation. He asked the Committee to reconsider whether it is necessary to make this an appropriated fund.

Senator Burns commented that by appropriating the fund, the Legislature is protecting the companies from DOI.

Senator Harper asked if captive insurers pay the same taxes as insurers in the open market. Mr. Childers stated that they do not. He explained that in most of the competitive captive states, like Vermont, Hawaii and South Carolina, the captive jurisdictions charge a fee and then a graduated premium tax, which is normally paid by insurance companies. He stated the current tax rate is

approximately 2.2%, which generates almost \$200 million a year. He noted that Vermont's graduated tax rate generates about \$10-\$11 million per year in income with 10% of that going to the agency for funding the captive program and the remainder going to the general fund. Under Arizona law, it is funded strictly on fees. There is a \$1,000 fee initially and a \$5,500 fee for every year thereafter, but there is no premium tax in Arizona, which was designed for competition.

**Vista Brown, Legislative Liaison, DOI**, remarked that the point of the captive law is to attract businesses from out of state. She noted of the six captives that DOI has licensed so far, only one has been an instate company. The rest have been businesses where the risks are located out of state and have been attracted to establish their domicile in Arizona. She stated that if they had been buying insurance in their state of residence on risks in that state, they would have been paying premium taxes in those states. The other point about captive insurance is that it is typically formed by very large enterprises that would otherwise self-insure, so they would not necessarily be buying on the commercial market anyway.

Senator Harper stated that in earlier conversations with Ms. Brown she was not able to supply him with the names of the six companies that belong to the program. He asked if she had any additional information on the companies. Ms. Brown stated the company's names are: Triad Commercial Captive Insurance Company; Sequoia Commercial Captive Insurance Company; Wilson Captive Insurance Company; LP Captive Inc.; WTC Captive Insurance Company; and TTG Captive Insurance Company. One is a privately held chain of hospitals, one is a communications company from Kansas, one is a set of assisted living facilities, another is a communications company from Kansas and an Illinois based manufacturer.

Senator Anderson asked why these captive insurance companies would be able to provide insurance for companies, while other insurance companies are not willing or able to. Ms. Brown stated that this question relates to why typically these companies would self-insure. A pure captive would rather go through a commercial insurer or self-insure company. She stated that a business would be buying insurance from an insurance company that it had set up to meet its own needs. There are business and tax advantages for doing this such as premiums, deductibles and access to capital markets. She stated that a business would be forming a company to insure its own risks, which is why it is regulated in a very different way. The reason why the insurance market is so difficult, particularly in the commercial area right now, is based on multiple factors, both national and local. One that is often heard about is investment income. Due to declines in the market, insurers have less investment income. She stated that sometimes business plans change and for whatever reason, the business decides to market to a different set of risks. The unpredictability created by the September 11<sup>th</sup> attacks has caused some disruptions in the market. She stated that historically, markets have gone through economic cycles, which are influenced by multiple factors.

Senator Soltero asked why this issue is coming to light at this time. Ms. Brown stated that there are 22 states that have captive insurance laws on their books. She stated that Representative Carpenter became interested in this idea when he was newly elected to office and began working on a bill in 1999. She stated that there were further discussions about the bill and there was an interim study committee on the issue. She stated the issue from DOI's perspective was that the bill needed to be technically sound, as this is a regulatory program. The other issue DOI had was regarding resources to run the program. She stated that the technical bill passed in 2001 and funding was established for the program. Due to the various budget problems, the second year funding was eliminated, leaving the \$93,000 as part of the base funding. With that, DOI has a captive administrator. She noted that there is no money for promotion, but a website has been set

up and brochures have been developed. She stated that DOI is actively trying to compete and market this program.

Senator Soltero asked if the State of Arizona could have a self-insurance program. Ms. Brown replied that she would have to investigate that possibility.

Senator Martin remarked that this model may be the solution needed to answer the self-insurance problem that was discussed last year with a way to lock away those reserves so the State would not squander them in an economic shortfall, leaving no way to pay claims. He remarked that he was going to speak to the Director of ADOA.

**Senator Waring moved HB 2152 be returned with an AS AMENDED, DO PASS recommendation. The motion CARRIED with a roll call vote of 13-0-0 (Attachment 1).**

Without objection, the meeting adjourned at 2:10 p.m.

Respectfully submitted,

Tracey Moulton  
Committee Secretary

(Tapes and attachments on file in the Secretary of Senate's Office/Resource Center, Room 115.)