

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: CS/HB 405 Regulation of Not-for-profit Self-insurance Funds
SPONSOR(S): Government Operations Appropriations Subcommittee; La Rosa
TIED BILLS: **IDEN./SIM. BILLS:** CS/SB 830

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee	13 Y, 0 N	Lloyd	Cooper
2) Government Operations Appropriations Subcommittee	12 Y, 0 N, As CS	Keith	Topp
3) Regulatory Affairs Committee		Lloyd	Hamon

SUMMARY ANALYSIS

In general, self-insurance is the assumption of financial risk oneself, rather than paying an insurance company to assume it. Florida law recognizes many different types of self-insurance funds. Two or more corporations not for profit can form a self-insurance fund (fund) to share their property or casualty risks. There are specified requirements and parameters for such a fund and its members. One requirement is that a fund member must receive at least 75 percent of its revenue from local, state, or federal government sources.

There is one such fund in the state, though others may be formed at any time, if formed in compliance with the law. This fund has approximately 150 members. It relies on the member's federal tax returns to determine whether the members meet the governmental revenue threshold. The fund offers: Property General Liability; Professional Liability; Medical Practice Liability; Medical Legal Liability; Directors & Officers Liability; Workers' Compensation; Commercial Automobile; and, Employee Health Benefits.

Members of such a fund are also typically federally tax-exempt organizations. An entity must be determined by the Internal Revenue Service (IRS) to be a tax-exempt organization following the filing of an IRS application form prior to filing its returns as a tax-exempt organization. Most federally tax-exempt organizations must file Form 990 with the IRS. Whether an organization is a publically supported organization is determined using Schedule A to IRS Form 990 or 990EZ. Schedule A requires organizations to indicate the reason the organization is a "public charity" for the tax year, which may be dependent upon public support. The available reasons on Schedule A include organizations that normally receive a substantial part of its support from a governmental unit or from the general public. Presently, only governmental support is considered in regard to revenue for qualification to form a fund.

The bill expands the types of corporations not for profit qualifying for membership in a fund. Specifically, the bill allows a corporation not for profit that is a publically supported organization for IRS purposes due to receipt of 75 percent of its revenue from the general public to be a member of a fund. This federal tax return based test is presented as an alternative to qualifying under the standard requirement that 75 percent of the corporation's revenue come from governmental sources (which is retained in the law).

The bill establishes a requirement that publicly supported organizations qualifying for fund membership must maintain sufficient surplus at the 70 percent confidence level, as determined by a qualified actuary. In addition, the bill requires the fund to file with the Office of Insurance Regulation (OIR) a remedial plan addressing the financial condition of the fund if they do not maintain the 70 percent confidence level. The remedial plan is subject to determination by the OIR that the fund will operate on an actuarially sound basis and the fund does not pose a significant risk of insolvency. The bill specifies that funds operating before the effective date of the bill shall have until July 1, 2020, to comply with the actuarial confidence requirements.

Finally the bill requires that this type of fund maintain excess insurance with a reinsurer holding a rating of A- or higher from a statistical rating organization deemed acceptable by the commissioner of the OIR.

The Revenue Estimating Impact Conference determined that the bill has an insignificant negative fiscal impact to insurance premium tax revenues. The bill is expected to have no impact on local government and an undetermined positive impact on the private sector.

The bill is effective July 1, 2015.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

In general, self-insurance is the assumption of some or all insurance-related financial risk oneself, rather than paying an insurance company to assume it.¹ Florida law recognizes many different types of self-insurance funds.² Two or more corporations not for profit³ wanting to pool their property or casualty risks together can form a self-insurance fund under s. 624.4625, F.S.⁴ This statute outlines many requirements and parameters for the fund and the corporation not for profit members. One requirement set out is that each fund member receives at least 75 percent of its revenue from local, state, or federal government sources.

There is at least one corporation not for profit self-insurance fund in Florida, the Florida Insurance Trust (FIT). It has approximately 150 members.⁵ The FIT currently offers multiple lines of coverage in their self-insurance fund.⁶ According to the FIT, Form 990⁷ from the Internal Revenue Service (IRS) is the source the FIT uses to determine if potential members receive 75 percent of funding from governmental sources. In addition, most current members of the FIT indicate on Schedule A for Form 990 that they are an organization that normally receives a substantial part of its support from a governmental unit or from the general public and qualify as a publically supported organization for IRS purposes.

Members of such a fund are also typically federally tax-exempt organizations. An entity must be determined by the IRS to be a tax-exempt organization following the filing of an IRS application form⁸ prior to filing its returns as a tax-exempt organization. Most federally tax-exempt organizations must file Form 990 with the IRS. Schedule A to Form 990 or 990EZ requires organizations to indicate the reason the organization is a “public charity” for the tax year, which may hinge upon public support. The determination whether a public charity is also a publically supported organization for IRS purposes is determined by the results of a computation of public support percentage set out on Schedule A.⁹ The computation takes into account certain receipts of the public charity for the past five years. Specifically, Schedule A requires organizations to disclose their aggregate receipts from the past five years from gifts; grants; contributions; membership fees; tax revenue; services or facilities furnished to the organization from a governmental unit; gross income from interest, dividends, payments received on securities loans, rents, royalties and income from other sources; net income from unrelated business activities; and other income. The amount of these receipts for certain tax years is used in the computation of a public support percentage, the result of which determines whether the organization qualifies as a publically supported organization for IRS purposes.¹⁰

¹ Glossary, <http://www.iii.org/services/glossary> (last viewed March 10, 2015).

² See s. 624.462, F.S., relating to commercial self-insurance funds; s. 624.4621, F.S., relating to group self-insurance funds; s. 624.4622, F.S., relating to local government self-insurance funds; s. 624.46226, F.S., relating to public housing authorities self-insurance funds; s. 624.4623, F.S., relating to independent nonprofit colleges or universities self-insurance fund; and s. 624.4626, relating to electric cooperative self-insurance fund.

³ Corporations not for profit are organized under Chapter 617, F.S. A corporation not for profit “means a corporation no part of the income or profit of which is distributable to its members, directors, or officers, except as otherwise provided under [ch. 617].” s. 617.01401(5), F.S.

⁴ The Office of Insurance Regulation reports that there is only one fund operating under s. 624.4625, F.S. (agency bill analysis on file with the Insurance and Banking Subcommittee).

⁵ <http://floridainsurancetrust.com/index.php> (last viewed March 10, 2015). The FIT has been in existence since 2007.

⁶ The FIT offers: Property General Liability; Professional Liability; Medical Practice Liability; Medical Legal Liability; Directors & Officers Liability; Workers’ Compensation; Commercial Automobile; and, Employee Health Benefits. See <http://floridainsurancetrust.com/coverage.html> (last viewed on March 10, 2015).

⁷ Non-profits whose incomes were less than \$500,000 and their assets less than \$1.25 million can file a Form 990EZ.

⁸ Form 1023, *Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code*, Form 1023-EZ, *Streamlined Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code*.

⁹ There are two ways an organization can qualify as a publically supported one: the 33 1/3 support test and the 10 percent facts and circumstances test. Calculations for both tests are set forth on Schedule A, Form 990 or Form 990EZ).

¹⁰ Schedule A (Form 990 or 990-EZ and Instructions for Schedule A available at [http://www.irs.gov/uac/About-Schedule-A-\(Form-990-or-990EZ\)](http://www.irs.gov/uac/About-Schedule-A-(Form-990-or-990EZ)) (last viewed on March 10, 2015).

The bill maintains current law allowing membership for corporations not for profit that receive at least 75 percent of their revenue from local, state, or federal government sources. By retaining current law in this regard, all current members of corporation not for profit self-insurance funds are essentially grandfathered in and thus, will be able to continue to qualify for fund membership, as long as their governmental funding level does not fall below 75 percent.

Presently, a member qualifies for a corporation not for profit self-insurance fund by drawing at least 75 percent of its revenue from governmental sources. The calculation of public support for purposes of IRS form 1099, Schedule A, includes support from the general public. Accordingly, the bill expands the potential membership of the fund(s) to include corporations not for profit that 75 percent of its revenue from the general public, rather than just those that receive at least 75 percent of their revenue from governments. Additionally, current law does not average the threshold 75 percent governmental funding over time. The revision proposed by the bill differs from the current standard in that under Schedule A, Part II, the level of funding necessary to determine public support is averaged over the preceding five tax years.

In addition, the bill establishes a requirement that organizations qualifying for fund membership based upon revenue from the general public must maintain surplus in a positive amount with the loss and loss adjustment expense reserve at the 70 percent confidence level,¹¹ as of the end of the fiscal year, as determined by the qualified actuary already evaluating the fund’s solvency, as specified in s. 624.4625(1)(d), F.S. If the fund does not maintain the 70 percent confidence level, it must file a remedial plan with the Office of Insurance Regulation (OIR) addressing the financial condition of the fund. The remedial plan is subject to determination by the OIR that the fund will operate on an actuarially sound basis and the fund does not pose a significant risk of insolvency. The bill specifies that funds operating on the effective date of the bill shall have until July 1, 2020 to comply with the solvency evaluation requirements of the bill.¹²

The bill requires that funds operating under s. 624.4625, F.S., maintain excess insurance with a rating of A- or higher from a statistical rating organization¹³ deemed acceptable by the commissioner of the OIR.¹⁴

¹¹ Actuaries express their assessment of the sufficiency of financial holdings to cover estimated losses in a given period as a “confidence level” on a percentage scale. A “70 percent confidence level” indicates that financial holdings will be adequate in seven out of ten years to meet estimated losses. *Understanding Confidence Intervals*, SIGMA Actuarial Consulting Group, Inc., www.sigmaactuary.com/download/tt_confidence.pdf. (Last viewed April 6, 2015)

¹² The FIT does not include the qualified actuary’s confidence level in its financial filing with the OIR, therefore, the effect that requiring a 70 percent confidence level on the part of the fund’s qualified actuary is unknown. However, the current financial condition of the FIT can be obtained from financial information that the FIT has filed with the OIR, which includes the following information:

	Jun 2012 – May 2013	Jun 2013 – May 2014
gross written premium	\$17,245,204.00	\$21,457,250.00
excess insurance (ceded premiums)	\$7,264,403.00	\$8,015,477.00
net written premium	\$9,980,801.00	\$13,441,773.00
surplus at year end	\$734,565.00	\$786,507.00

Financial Statements and Independent Auditor’s Report, Florida Insurance Trust, May 31, 2013, and *Financial Statements and Independent Auditor’s Report*, Florida Insurance Trust, May 31, 2014, on file with the Office of Insurance Regulation and the Regulatory Affairs Committee.

¹³ There are several financial strength rating organizations, including: A.M. Best (www.ambest.com), Fitch (www.fitchratings.com), Moody’s Investor Services (www.moody.com), and Standard & Poor’s (www.standardandpoors.com).

¹⁴ The FIT reports that they currently utilize 14 reinsurers to place their required excess insurance. See *Florida Insurance Trust 2014-2015 Program Carrier Partners* on file with the Regulatory Affairs Committee. All are rated between A++ (Superior) and A- (Excellent) on the A.M. Best financial rating scale, with only one of their reinsurers being rated A-. A.M. Best’s Financial Strength Rating is divided between “Secure,” with ratings between A++ and B+, or “Vulnerable,” with ratings of B or lower. Among the “Secure” ratings, A++ and A+ are described as “Superior,” A and A- are described as “Excellent,” and B++ and B+ are described as “Good” in terms of A.M. Best’s opinion of the company’s ability to meet financial obligations. See *Guide to Best’s Financial Strength Ratings*, A.M. Best, <http://www.ambest.com/ratings/guide.pdf>. (Last viewed April 6, 2015)

B. SECTION DIRECTORY:

Section 1: Amends s. 624.4625(1), F.S., relating to corporation not for profit self-insurance funds eligibility criteria.

Section 2: Provides an effective date of July 1, 2015.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

According to the Revenue Estimating Impact Conference held on March 6, 2015, there will be an insignificant negative fiscal impact¹⁵ to insurance premium tax revenue collections.¹⁶ Premium tax revenues will be impacted to the extent that increased participation in corporation not for profit self-insurance funds moves premiums from the generally applicable rate of 1.75 percent of premium to the 1.6 percent of premium applicable to funds organized under s. 624.4625, F.S.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Corporations not for profit that choose to self-insure their risks by joining or forming a corporation not for profit self-insurance fund should be able to obtain savings over purchasing coverage of these risks in the general market. This would reduce their fundraising burdens and/or allow revenues to be redirected to other purposes. The extent of the savings has not been estimated.

D. FISCAL COMMENTS:

The impact to premium tax revenue collections as a result of this legislation could potentially be mitigated if corporations not for profit choose to obtain self-insurance for lines that they do not currently carry, thus increasing premium tax revenue.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to: require counties or municipalities to spend funds or take an action requiring the expenditure of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or reduce the percentage of a state tax shared with counties or municipalities.

¹⁵ The Revenue Estimating Conference denotes that an insignificant negative impact is less than \$50,000.

¹⁶ Revenue Estimating Conference impact analysis (March 6, 2015) available online at <http://edr.state.fl.us/Content/conferences/revenueimpact/index.cfm> (Last visited March 11, 2015)

2. Other:

None.

B. RULE-MAKING AUTHORITY:

None.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

On March 17, 2015, the Government Operations Appropriations Subcommittee adopted a strike-all amendment and reported the bill favorably as a committee substitute. The amendment:

- Amends s. 624.4625(1), F.S., to expand the types of corporations not for profit qualifying for membership in a corporation not for profit self-insurance fund to include those that receives at least 75 percent of their funding from the general public, in addition those 75 percent funded from governmental sources.
- Provides a minimum acceptable confidence level by the qualified actuary providing a financial evaluation under the statute regarding the sufficiency of its surplus to meet estimated losses for any fund that has members qualifying for participation based upon funding from the general public.
- Provides remedial actions for funds qualifying under this legislation, which do not maintain the requisite positive surplus and actuarial confidence level.
- Provides a compliance date of July 1, 2020, for corporation not for profit self-insurance funds operating prior to the effective date of the bill, to meet the positive surplus and actuarial confidence level required for funds with members qualifying based upon funding from the general public.
- Provides a requirement that all funds operating under s. 624.4625, F.S., maintain excess insurance with a rating of A- or higher from a statistical rating organization deemed acceptable by the commissioner of the OIR, without qualification as to their inception date or membership's funding source.

This analysis is drafted to the committee substitute as passed by the Government Operations Appropriations Subcommittee.