

**INTERIM REPORT OF THE
JOINT SUBCOMMITTEE STUDYING THE
COMMONWEALTH'S INSURANCE COVERAGE**

TO

THE GOVERNOR

AND

THE GENERAL ASSEMBLY OF VIRGINIA



HOUSE DOCUMENT NO. 28

**COMMONWEALTH OF VIRGINIA
DEPARTMENT OF PURCHASES AND SUPPLY
RICHMOND**

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**Interim Report of the
Joint Subcommittee Studying the
Commonwealth's Insurance Coverage**

To

The Governor and the General Assembly of Virginia

Richmond, Virginia

November, 1977

To: Honorable Mills E. Godwin, Jr., Governor of Virginia

and

The General Assembly of Virginia

INTRODUCTION

The Joint Subcommittee Studying the Commonwealth's Insurance Coverage was established pursuant to House Joint Resolution No. 251 of 1977.

HOUSE JOINT RESOLUTION NO. 251

WHEREAS, the Commonwealth, frequently in conjunction with her political subdivisions, purchases a variety of insurance which extend various types of protection to State and local officials, agency heads, other employees required to be covered, and State-owned property; and

WHEREAS, the premiums on said insurance are expensive and the amount of liability coverage provided is in some instances disproportionate to the amount of possible loss or to loss experience; and

WHEREAS, it has been postulated that the State is confronted by a sizable budget deficit and that measures of austerity must be implemented; and

WHEREAS, from empirical data gathered to date there seems to exist

the distinct possibility that the Commonwealth may be able to realize considerable economies beneficial to her financial well-being if her insurance program is restructured; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That the House Corporations, Insurance and Banking Committee and the Senate Commerce and Labor Committee are hereby requested to appoint three members each to study the Commonwealth's present program of insurance coverage and bond requirements and make recommendations concerning a structured insurance program for Virginia. Such recommendations should take into consideration the possibility of self-insurance and any other structural change to the State's insurance program which may result in economies.

Upon completion of their study, the Committees shall make the recommendations and propose the legislation necessary to realize the conclusion of their study.

Gerald L. Baliles of Richmond, a member of the House of Delegates of Virginia and co-patron of House Joint Resolution No. 251, was elected Chairman. Madison E. Marye of Shawsville, a member of the Senate of Virginia, was elected Vice-Chairman.

Also appointed to serve from the House of Delegates were Archibald A. Campbell of Wytheville and William T. Wilson of Covington. Appointed to serve from the Senate were Edward E. Willey of Richmond and Nathan H. Miller of Harrisonburg.

L. Willis Robertson, Jr. and Hugh P. Fisher, III of the Division of Legislative Services served as staff to the Subcommittee.

H.J.R. 251 requested the House Committee on Corporations, Insurance and Banking and the Senate Committee on Commerce and Labor to undertake a joint study of the methods by which the Commonwealth procures insurance. It was felt that a comprehensive study might reveal ways in which significant savings could be realized.

It was within this framework that the insurance study was begun. Time constraints and the complexity of the issues confronting the Subcommittee forced it to narrow its inquiry at an early date. Three specific insurance fields were chosen for closer study: 1) Surety bonds for government officials, 2) Workmen's Compensation Insurance for State employees and 3) Property and Casualty Insurance.

The Subcommittee believes that considerable sums of money could be saved by requiring State agencies and local governments to purchase surety bonds under a blanket bond program. This would require eliminating the choice which currently exists, but the measure is justified on two grounds: First, the terms and conditions of the surety bonds would remain the same whether purchased on an individual or blanket basis and thus no protection will be lost. Secondly, the State, which shares the cost of even the local government bonds, and the local governments both stand to save about 50% of their cost.

The Subcommittee makes a similar recommendation for the purchase of Workmen's Compensation Insurance covering State employees. Purchase under a master or blanket program should result in significant savings in this area.

The study of the Commonwealth's insurance program in the Property and Casualty field was hampered by the absence of centralized information on the subject. Available data comparing the premiums paid and the losses experienced indicates that further study is in order. Accordingly, the Subcommittee recommends that its work in this area be continued for another year.

Appendix A consists of the legislation that would require blanket purchasing of surety bonds and Workmen's Compensation insurance. Appendix B consists of a resolution urging that the study be continued next year.

The Subcommittee used the following materials as its primary reference sources: (1) A booklet entitled "Initial Working Papers of the Joint House-Senate Insurance Study Committee" which was prepared and distributed by Delegate Baliles, (2) An American Bar Foundation article concerning government risk management and (3) A 1962 VALC study concerning insurance on State-owned buildings.

Discussion

1. Surety bonds for government officials should be purchased on a blanket basis.

The premiums for surety bonds required of county and city officials are shared by the State and the locality. In some instances the State contributes as much as two-thirds of the cost. It is no surprise, then, that the State takes an active interest in the purchase of these bonds. It is also plainly clear why the State takes an interest in the purchase of surety bonds by State agencies.

Local governments now have the option of purchasing surety bonds on either an individual basis or through participation in the State Blanket Surety Bond Program. Significant savings for both State and local governments could be realized, without sacrificing any insurance protection, if this choice was eliminated.

A few examples will illustrate the soundness of this recommendation. Information collected in connection with the purchase of surety bonds revealed that forty-seven counties did not participate in the blanket program for the surety bonds of their Treasurers, choosing to purchase individual bonds instead. The State's share in the cost of these bonds (one-half) amounted to \$58,223.50. The State's share for identical bonds purchased under the blanket program would have been only \$29,440. Eliminating the Counties' choice for Treasurer's bonds alone would result in savings of \$28,783.50 on these bonds.

Prior to 1975 the Supreme Court of Virginia was spending \$29,499 annually for surety bonds for district court judges, clerks and magistrates. A blanket surety bond was negotiated, however, in 1976 and the total premium was only \$2,332.58, resulting in annual savings of \$27,166.42. During the four year life of the bond, savings will be \$108,665.68.

Once again it should be emphasized that these savings may be realized without reduction in the insurance coverage. Rather than reducing protection, the blanket program results in savings by spreading the risk over a larger insurable base. For these reasons the Subcommittee recommends that surety bonds be purchased under a blanket bond program.

2. Workmen's Compensation Insurance should be purchased on a blanket basis.

The Subcommittee believes that purchasing this insurance on a blanket basis would result in substantial annual savings for the Commonwealth. Mr. Charles Walker, State Comptroller, spoke to the Subcommittee on this topic. Mr. Walker reported that each State agency is currently carrying its own Workmen's Compensation Insurance. He indicated that if all State agencies and institutions were under a blanket policy, the State could expect annual savings of 5-15% over present costs. In dollar figures, this would mean an annual savings of \$100,000-200,000. The basic insurance principle shown in the surety bond area, that insurance costs decline as the risk is spread over a larger group, is equally as valid in the Workmen's Compensation area. Therefore, the Subcommittee recommends that legislation be enacted which would place all State agencies and institutions under a blanket Workmen's Compensation plan.

3. The Subcommittee should be continued for another year in order to study in more detail the State's present property and casualty insurance programs.

State government and private business share many common risk situations. There are, however, many differences and these place the State in a unique position for effective risk management. Unlike private business, a state government continues to exist even after a catastrophic loss; although bondholders, suppliers and those benefiting from government services will ultimately feel the loss. Also, government risk management decisions differ from those of private industry because the former necessarily has a political character; typically shown in a preference for private insurance and measures designed to prevent improper influence in state insurance decisions.

Perpetual existence, taxing power and a large base upon which to distribute losses allows a state significant flexibility in its choice of property and casualty insurance programs. It is now recognized that reasonable alternatives exist to placing reliance totally on insurance purchased from insurance companies. The State may underwrite varying degrees of its own risks, including self-insurance for full value and all risks.

Virginia cannot, however, make an informed choice without full consideration of the appropriate facts. Herein lies the dilemma of the Subcommittee. Responsibility for the State's Property and Casualty insurance programs is currently vested in the Department of Property Records and Insurance. The Administrator of this department is assisted by the State Insurance Board, the State Fire Marshall and the advice of private insurance companies. Unfortunately, the Department's limited staff, (three members), precludes it from playing a vigorous role in the policy planning stage. The Department's staff is simply inadequate for the role it was meant to play: appraising all State property and advising the agencies on the kind and amount of insurance which they need. In practice most State agencies now seek this advice from private insurers who then write policies on the basis of their advice.

The Department's problems were shared by the Subcommittee. The Subcommittee was unable to surmount the initial, threshold problem: There is no centralized information upon which property and casualty insurance policy decisions can be made.

The information that was available did support the need for study, however. For example, the 1975 Biennial Report of the Department of Property Records and Insurance showed that in many cases the agencies were paying far more in premiums than they were experiencing in losses. The Department of Corrections, for example, paid annual premiums of \$95,207 between 1970 and 1975, but losses averaged only \$8,665 per year. During the same period the Alcoholic Beverage Control Commission spent an average of \$31,431 for Property and Casualty insurance. The ABC Commission's annual losses averaged only \$731. The net totals for all State agencies from 1970 to 1975 showed premium payments of \$909,611 and

average annual losses of only \$177,363.

One possible alternative which should be explored in depth is a program of self-insurance. However, as emphasized before, the Subcommittee lacked the information necessary for a responsible decision on this alternative. In the course of reviewing these insurance problems, the Subcommittee invited Mr. John Day, the Commissioner of Insurance, to meet with its members.

The Subcommittee secured, through Mr. Day, the assistance of risk managers from Reynolds Metals Company, Southern States and the City of Virginia Beach, who comprise the Risk Management Advisory Committee. Mr. William H. Murphy is the Reynolds Metals risk manager, while Mr. Bernard M. Hulcher is from Southern States and Mr. Robert W. Esenberg is from the City of Virginia Beach. It should be noted that these risk managers, who have no connection with any private insurance companies, have voluntarily offered their time and advice to the Subcommittee during the next year in developing a program for evaluating the State's insurance needs.

Consideration of the State's overall insurance needs and the development of a comprehensive insurance program must await the answer to three fundamental questions:

- 1) What is the premium/loss ratio in the State government?
- 2) What are the risk exposures of the State agencies?
- 3) What types of insurance does the State need and how should it be obtained?

Because the necessary information is not readily available and because additional time will be necessary to analyze this data, the Subcommittee recommends that it continue its study of Virginia's Property and Casualty insurance programs and acceptable alternatives for another year. The indications are that significant savings may be realized for the Commonwealth.

CONCLUSION

During its first year in existence, the Subcommittee has concentrated on correcting the uneconomical tendencies present in the Commonwealth's method of purchasing surety bonds and Workmen's Compensation insurance. The members look forward next year to studying viable alternatives to the State's present method of purchasing Property and Casualty insurance.

Respectively submitted,

Gerald L. Baliles, Chairman

Madison E. Marye, Vice-Chairman

Edward E. Willey

Nathan H. Miller

Archibald A. Campbell

William T. Wilson

APPENDIX

A BILL to amend the Code of Virginia by adding in Chapter 5.6 of Title 2.1 a section numbered 2.1-51.29, relating to the establishment of blanket surety bond and group workmen's compensation insurance plans for State employees.

Be it enacted by the General Assembly of Virginia:

1. That the Code of Virginia is amended by adding in Chapter 5.6 of Title 2.1 a section numbered 2.1-51.29 as follows:

§ 2.1-51.29. Secretary to establish blanket surety bond and group workmen's compensation insurance plans for State employees.—The Secretary of Administration and Finance shall initiate and implement a program of blanket surety bonding to provide surety for the faithful performance of duty for all State employees required by statute be bonded, and for other agency employees handling funds or having access to funds whose function in the opinion of the agency head and Secretary of Administration and Finance should be bonded.

Local employees or Constitutional officers, other than those already covered by programs of the Supreme Court under § 19.2-39 of the Code of Virginia, for whom the Commonwealth pays all or part of the costs of surety bonds, shall be required to participate in the blanket surety bond program promulgated by the Secretary of Administration and Finance through the Comptroller and the Compensation Board. Before implementing the program, the Secretary shall determine that such program will be of less cost to the Commonwealth than the aggregate of individual bonds costs.

The Secretary of Administration and Finance shall initiate and implement a group workmen's compensation insurance program for all State employees through a program that accumulates maximum premium discounts on a Statewide basis. Before implementing the program, the Secretary shall determine that such program will be of less cost to the Commonwealth than the aggregate of individual agency policies.

APPENDIX B

HOUSE JOINT RESOLUTION NO.....

Requesting that the Joint Subcommittee of the House of Delegates Committee on Corporations, Insurance and Banking and the Senate Committee on Commerce and Labor's study on the Commonwealth's Insurance Coverage be continued.

WHEREAS, the Commonwealth, frequently in conjunction with her political subdivisions, purchases a variety of insurance programs which extend various types of protection to State and local officials, agency heads, as well as other employees required to be covered, and State-owned property; and

WHEREAS, from empirical data gathered to date there seems to exist the distinct possibility that the Commonwealth may be able to realize considerable economies beneficial to her financial well-being if her insurance program is restructured; and

WHEREAS, House Joint Resolution No. 251 of nineteen hundred seventy-seven General Assembly authorized the Joint Subcommittee of the House of Delegates Committee on Corporations, Insurance and Banking and the Senate Committee on Commerce and Labor's study on the Commonwealth's Insurance Coverage to examine the Commonwealth's insurance-procuring policies and to recommend changes in the purchase of such insurance; and

WHEREAS, although the Subcommittee has made significant progress in studying certain areas of the Commonwealth's insurance coverage and in offering recommendations which would effect needed changes in the purchase of such insurance, more work needs to be done; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That the Joint Subcommittee of the House of Delegates Committee on Corporations, Insurance and Banking and the Senate Committee on Commerce and Labor's study on the Commonwealth's Insurance Coverage is hereby continued. The Subcommittee is requested to focus next year on the Commonwealth's method of purchasing property and casualty insurance for State-owned property. However, the Subcommittee shall also study any other area of the Commonwealth's insurance program that warrants further scrutiny.

The present six members shall continue to serve on the Subcommittee. If a vacancy occurs for any reason, a successor shall be appointed by the appropriate person or persons pursuant to the method of appointment specified in House Joint Resolution No. 251 of the nineteen hundred seventy-seven General Assembly. All agencies of the Commonwealth shall assist in this study.