

MAINE STATE LEGISLATURE

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STATE OF MAINE

ONE HUNDRED AND NINTH LEGISLATURE

COMMITTEE ON BUSINESS LEGISLATION

February 15, 1980

Senator Richard H. Pierce
Chairman
Legislative Council
State House
Augusta, Maine 04333

Re: S.P. 627

Dear Senator Pierce:

Enclosed please find copies of the majority and minority reports of the Committees on Business Legislation and Education pursuant to S.P. 627.

Sincerely,

John D. Chapman
John D. Chapman
Senate Chairman

Howard M. Trotzky
Howard M. Trotzky
Senate Chairman

Robert S. Howe
Robert S. Howe
House Chairman

Laurence E. Connolly, Jr.
Laurence E. Connolly, Jr.
House Chairman

RF/lk

MAJORITY REPORT
of the
JOINT STANDING COMMITTEES
ON
BUSINESS LEGISLATION
AND
EDUCATION

A STATE PROGRAM OF FUNDED SELF-INSURANCE
FOR PUBLIC SCHOOLS
(S.P. 627)

Submitted to the
Legislative Council
109th Legislature

February 15, 1980

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SUMMARY

S. P. 627 directed the Committees on Business Legislation and Education to study the subject of a state program of funded self-insurance for public schools. A special subcommittee held several meetings and submitted its findings to the full committees.

The majority found that most school buildings are adequately insured and that the cost of adequate coverage is generally reasonable. Local school officials have also registered no complaints about excessive cost with the Commissioner of Educational and Cultural Services.

The majority found that a state school insurance program would probably not produce any real savings and that a state program is undesirable for many non-financial reasons. The majority concluded, for example, that a state program would not likely be able to manage the insurance needs of 250 different school systems, that local school officials should retain control over insurance, and that a state program would halt the development of private insurance alternatives such as the voluntary group plan being developed by the Maine School Management Association.

The majority made four brief recommendations concerning school insurance data collection, development of private alternatives, consideration of underwriting factors in school construction, and increased competition among agents through bid solicitation.

BACKGROUND

Revised Statutes, Title 20, section 3476 requires school systems to carry fire and allied insurance coverage "in the amount of the replacement cost" on any state-subsidized school construction project approved after June 30, 1977 (although the Commissioner of Educational and Cultural Services may modify this requirement if such coverage cannot be obtained at a reasonable cost); Title 20, section 3457 imposes a similar requirement with respect to any project approved before July 1, 1977. Though not legally required to do so, school systems generally buy other kinds of coverage as well such as motor vehicle fleet, employee health and accident, liability, and fidelity bonds. School systems normally purchase insurance individually through local agents from conventional commercial carriers. For state educational subsidy purposes, the premiums are treated as a normal operating expense.

L.D. 1525 was introduced in the 1st Regular Session of the 109th Legislature to establish a state program of funded self-insurance for public schools. Under the program proposed in L.D. 1525, each school system would be charged an initial fee proportionate to its current total annual premium; a substantial portion of these start-up monies would be set aside by the State to capitalize a "reserve" fund; the "reserve" fund would be used to self-insure a sizable deductible, also known as the "retained" risk; the balance would then be used to buy "excess" coverage from a conventional carrier to insure

the remainder of the risk; thereafter, every school system would be assessed periodically as necessary to maintain an adequate "reserve" and to purchase "excess" insurance.

S.P. 627 (Appendix) was introduced after the sponsor of L.D. 1525 was granted leave to withdraw; it directs the Joint Standing Committees on Business Legislation and Education to "study the feasibility of establishing a state insurance program for public educational institutions."

A special 8-member legislative subcommittee was appointed to conduct the study. The subcommittee held an organizational meeting, a public hearing and a work session. It heard testimony and received information and assistance from representatives of interested state agencies, school systems, businesses, and educational and insurance groups, as well as from concerned individuals.

This is the majority report.

ISSUES

I

DOES THE CONVENTIONAL INSURANCE MARKET OFFER ADEQUATE COVERAGE
TO PUBLIC SCHOOLS AT A REASONABLE COST?

II

WOULD A STATE PROGRAM OF FUNDED SELF-INSURANCE PROVIDE THE
SAME OR BETTER COVERAGE TO PUBLIC SCHOOLS AT LESS COST?

FINDINGS

I

THE CONVENTIONAL INSURANCE MARKET OFFERS ADEQUATE COVERAGE TO PUBLIC SCHOOLS AT A REASONABLE COST.

The current method of insuring public schools has been criticized mainly on the grounds that many school buildings are allegedly underinsured and the cost of adequate coverage is supposedly often unreasonable. These criticisms are not substantiated by the facts.

A. Most school buildings are adequately insured.

There is no solid evidence that any school buildings are presently underinsured.

The few past "examples" which were cited to the subcommittee were not probative: many relevant circumstances were either unclear or unknown altogether, or the replacement cost (to which the actual insured value is compared) was obviously invalid (e.g., the "replacement cost" of an allegedly "underinsured" loss was calculated in hindsight on the basis of the construction cost of a much larger, more elaborate new building).

State law requires that school buildings be insured for their full replacement cost. It is reasonable to presume that local school officials know the law and use their best efforts to comply with it.

B. The cost of adequate coverage is generally reasonable.

The school insurance data which was available to the subcommittee was flawed and incomplete. It purported to show loss

ratios (which express the relationship between premiums and claims paid) that were inordinately favorable to the insurance industry. However, the data was not compiled for the study, but rather, routinely reported for the purposes of the state educational subsidy. As a result, critical information such as the amounts of coverage or the size of deductibles was omitted: the annual reports on which the data was based were never designed to collect such information. And it was uncertain what kinds of coverage were represented by the data collected. Its significance and credibility were also undermined by different accounting methods, variations among school insurance plans, and inevitable errors and omissions in reporting. In short, the data was neither meaningful nor reliable.

The few "examples" of allegedly "unreasonable" cost that were cited to the subcommittee were misleading and atypical. In one case, for example, local school officials had apparently not made a reasonable effort to publicize their insurance business and to solicit bids. Premium rates probably would have been attractive if they had encouraged open, active competition among local agents. In another case, it became evident that a substantial premium was reasonable and justified under the circumstances: the school system in question had recently erected a large secondary school building of wood-frame construction in a rural area far from any hydrants or an organized fire department.

No school system has ever requested modification of the law's requirement that buildings be insured for their replacement cost, although the requirement may be modified if the premium is excessive. It is reasonable to infer that local school officials

do not consider the cost of adequate coverage excessive.

Many school systems now enjoy very low premium rates, some apparently even lower than those enjoyed by state agencies under the State's own property self-insurance fund.

II

A STATE PROGRAM OF FUNDED SELF-INSURANCE WOULD NOT PROVIDE THE SAME COVERAGE TO PUBLIC SCHOOLS AT LESS COST.

It has been alleged that a state program of funded self-insurance for public schools would provide the same or better protection at less cost than the current method. This suggestion is not supported by the facts.

A. A state program would probably not produce any real savings.

Proponents of a state program were unable to make any firm projection of the savings they promise would result under their proposal because there is no meaningful, reliable school insurance data available.

It is doubtful that a state program would produce any "true" or net savings. Many school systems "pool" their insurance needs with those of their local municipalities so both can avail themselves of lower premium rates. A state program, particularly one in which participation were mandatory, would destroy such mutually advantageous arrangements. Substantial increases in local municipal rates would very likely follow. Similarly, if only more attractive risks such as property were insured under

a state program, school systems would be hard-pressed to buy special coverage at an affordable rate for less attractive risks such as motor vehicles or liability.

B. A state program is undesirable for many non-financial reasons.

There are approximately 250 separate school systems in the State. Each is different and has diverse insurance needs which demand individual attention. Local agents currently provide each school system with a wide variety of personalized services, from coverage consultation and loss prevention, to claims administration. It is doubtful whether a small state agency headquartered in Augusta could render either the quantity or quality of essential services now being delivered conveniently and ably by a state-wide network of local agents.

A state program would retard or even halt the development of private alternatives, most notably a voluntary group plan being devised by the Maine School Management Association. A "mandatory" state program would eliminate this prospect while an "optional" one would compete with it to the probable detriment of both.

Local school officials are most accountable to local citizens and most concerned about adequate coverage and reasonable cost. A state program would remove school insurance from their direct control. Local control should be preserved because it is the best way to assure that a school system's insurance needs are satisfactorily met at the least expense.

The school insurance fund proposal fails to take into account

a fundamental difference between it and the state property self-insurance fund. The difference is that the state property fund handles insurance essentially for a single entity - the State. Management and decisionmaking can be effectively centralized in Augusta. A state school insurance program, on the other hand, would be required to deal with 250 different school systems around the State and with hundreds of individual superintendents and school board members. Efficient administration of the program would therefore be very difficult.

The current method serves public schools well. Any problems which may exist are already being addressed, or would be addressed if our recommendations were followed.

RECOMMENDATIONS

I

COSTS AND OTHER CRITICAL ASPECTS OF SCHOOL INSURANCE SHOULD BE REVIEWED PERIODICALLY IN A COMPREHENSIVE, SYSTEMATIC FASHION.

The Department of Educational and Cultural Services, the various state educational associations, some other appropriate party, or any combination of these should periodically review school insurance by undertaking comprehensive, systematic surveys of the State's school systems and their local agents and by making public their findings and recommendations.

II

INNOVATIVE PRIVATE MEANS OF MINIMIZING SCHOOL INSURANCE COSTS AND MAXIMIZING COVERAGE AND SERVICE SHOULD BE DEVELOPED.

The subcommittee was advised that the Maine School Management Association is studying the possibility of creating a group insurance plan for its member school systems. This kind of effort should be encouraged.

III

UNDERWRITING FACTORS SHOULD BE WEIGHED MUCH MORE CAREFULLY IN PLANNING AND CONSTRUCTING NEW SCHOOL BUILDINGS.

Local agents and school officials should confer and cooperate during a building's planning and construction phases in order to avoid creating unattractive underwriting risks. The State Board of Education and the Department of Educational and Cultural Services should monitor school construction projects closely for their

conformity with optimal underwriting standards.

IV

COMPETITION FOR LOCAL SCHOOL INSURANCE BUSINESS SHOULD BE ENCOURAGED BY PUBLICITY AND ACTIVE BID SOLICITATION.

There is reason to believe that a few school systems may pay comparatively high premiums because they fail to stir much interest on the part of local agents. These school systems should promote competition by publicizing their business and actively soliciting bids so that their premium rates would become more attractive.

STATE OF MAINE

In Senate June 13, 1979

Whereas, educational institutions are one of the most valuable assets of any state; and

Whereas, the loss of benefit to society that would result from the inability of an educational institution to function is unmeasurable; and

Whereas, many public educational institutions in this State are vulnerable to such an eventuality because of inadequate insurance protection; now, therefore, be it

Ordered, the House concurring, subject to the Legislative Council's review and determinations hereinafter provided, that the Joint Standing Committee on Business Legislation/^{and} the Joint Standing Committee on Education, shall jointly study the feasibility of establishing a state insurance program for public educational institutions; and be it further

Ordered, that the committees report their findings and recommendations, together with all necessary implementing legislation in accordance with the Joint Rules, to the Legislative Council for submission in final form at the Second Regular Session of the 109th Legislature; and be it further

Ordered, that the Legislative Council, before implementing this study and determining an appropriate level of funding, shall first ensure that this directive can be accomplished within the

limits of available resources, that it is combined with other initiatives similar in scope to avoid duplication and that its purpose is within the best interests of the State; and be it further

Ordered, upon passage in concurrence, that a suitable copy of this Order shall be forwarded to members of the committees.

IN SENATE CHAMBER
TABLED BY SEN. SEN. P
OF OF KENNEBEC

JUN 13 1979

PENDING *Passage*
MAY M. ROSE, Secretary

IN SENATE
TAKEN FROM TABLE OF SEN. P

BY SEN. P AND SEN. P

JUN 15 1979

SEN. RAJZ
OF KENNEBEC

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