STATE OF NEW HAMPSHIRE
DEPARTMENT OF STATE

Docket No. C-2011000036

IN THE MATTER OF:

Local Government Center, Inc., et al.

Bureau of Securities Regulation's Expanded Objection to Petition to Obtain Permission to Issue New and Renewal Coverages

Now comes the New Hampshire Bureau of Securities Regulation ("BSR"), through counsel and pursuant to the oral order issued by the Presiding Officer on April 3, 2015, and files this statement of objection to the request by Property Liability Trust ("PLT") for permission to issue new and renewal coverages.

Objection

The BSR objects to the grant of permission to renew or issue new coverages, generally referred to herein as "permission," because the BSR does not believe the PLT can establish that it is financially secure enough to justify permission, as required by the Consent Decree signed by the parties on July 25, 2014 and approved by the Presiding Officer on August 4, 2014. Of necessity, the BSR relies on the documents submitted by the PLT in support of its petition for permission and matters that are in the historical record. The BSR has not had time to create its own original analysis. To the extent that the PLT's representations are wrong, the BSR reserves the right to expand this Objection. As well, this Objection is submitted less than ten days after the filing of the PLT's voluminous petition. The BSR continues to review the petition. The BSR's Objection depends upon analysis of the specific representations of the party that has the burden of proof, that being the PLT.

Historical Subsidization of Workers Compensation Continues

The BSR considers historical facts relevant to consideration of the PLT's petition, not to dredge up old disputes, but because the historical facts place the petition in context. The workers compensation coverage line of PLT has historically been subsidized from its more recent inception in 2000 through the present. The initial subsidy for the workers compensation coverage line was in the form of $1 million in contributions from the health coverage members and the property liability coverage members. An additional $17.1 million was contributed as subsidy to the workers compensation program from 2003 through 2010 in the form of disguised contributions to the LGC parent. In addition, the property liability coverages and workers compensation coverages were combined in 2007 primarily to bolster the balance sheet of the workers compensation program.

Subsidization of the workers compensation program has continued since 2010 in the form of the payment of almost all of the $17.1 paid to HealthTrust being drawn from property liability funds and not from workers compensation funds. As well, the over $14 million in securities pledged to the New Hampshire Department of Labor ("DOL") came from property liability program investments. Both of these actions have left the property liability coverage line in PLT in the red with a net position (formerly referred to as "surplus") of a negative $2,057,087 million. The crippled financial position of the property liability coverage program and workers compensation's apparent continuing need for subsidy---and the absence of any plan to make property liability whole—should give the Presiding Officer pause when reviewing PLT's request for permission.

The Membership in PLT is Falling and So are Member Contributions

According to the petition at para. 10, PLT has 303 current members, of which 154 participate (51%) in only the property liability coverage program. Conversely, 149 members participate in the workers compensation program in addition to receiving property liability coverage. Use of the assets of property-liability-only members to support the workers compensation program both shows the workers compensation program cannot stand on its own financials and may raise questions about PLT's improper use of surplus.[1]The PLT petition, at para. 24, acknowledges that the success of the PLT program going forward depends on its maintenance of members during the proposed seven year review period. In support of its arguments, PLT asserts that "PLT has continued to maintain all of its members since July 1, 2014." Petition at para. 25(a). While this may be a true statement, it is somewhat misleading because the key degradation of PLT's membership rolls occurred on or before June 30, 2014, which was the first opportunity, consistent with a fiscal year, for members to exit after the Supreme Court's decision in Appeal of the Local Government Center which was issued on January 10, 2014. 165 N.H. 790 (2014). The June 30th date was also the first fiscal year end exit date after the Bureau's enforcement action was filed challenging the secret agreement that was reached by the LGC programs on October 28, 2013 and not disclosed until January 10, 2014.

The supporting materials submitted by the PLT include information that documents the membership figures for the immediately preceding fiscal year; that is, the year ending June 30, 2014. Exhibit C is the financial statement for the ten months ending June 30, 2014. At the conclusion of this fiscal year, PLT had 329 members overall with 192 in the workers compensation program. Exhibit C at 11. Thus, PLT lost 27 members between June 30, 2014 and the present. Notable among the members who departed were Dover and Portsmouth, both large cities who exited because of the illegal subsidization of workers compensation,

[1] This may also raise questions about whether proper notice was given to the property-liability-only members before their assets were misapplied.

and Hopkinton[2], which exited because of PLT's claims adjustment practices. Also, related to the decrease in members, was a decrease in member contributions.

Member contributions on a ten-month basis in the FY 2014 financial statement were reported as $8.6 million for the property liability coverage program and $5.5 million for the workers compensation coverage program. If these figures are annualized, assuming equal monthly contributions, the contributions total $10.32 million and $6.6 million for property liability and workers compensation, respectively, per annum. Exhibit D to the petition is an unaudited statement of financial position for PLT for the six months ending January 31, 2015. A similarly annualized (12 months) contributions calculation projected from the statement of financial position indicates that, over 12 months, the contributions for the property liability coverage program will fall to $8.3 million and the workers compensation coverage program contributions will fall to $6.4 million, yielding contribution losses of $2.22 million on a consolidated basis. Property liability will lose $2.02 million based on this projection and workers compensation will lose $200,000.

<u>Approvals of DOL and the Presiding Officer are Required</u>
<u>(DOL must also release its Security Agreement)</u>

PLT acknowledges in its strategic plan that it must obtain the permissions of the Commissioner of DOL and of the Presiding Officer to write new and renewed coverages and to emerge from run-off.[3] This is a legal requirement imposed by the DOL's administrative

[2] See Exhibit C at 15 at which the financial statement represents that policy limits generally follow members' valuations. This was not the case in Hopkinton where the LGC encouraged a higher insured value and then refused to pay the higher insured value when a Hopkinton town building was destroyed in a fire.

[3] This acknowledgement is redacted from Exhibit E-1, at 18. The BSR does not agree to the redactions submitted by PLT. The redacted submission also includes information about anticipated rates during the seven-year review period. E-1 at 19. Further, at the top of 21, PLT redacts a "major caveat." Finally, PLT characterizes its current financial condition in a certain way at the top of page 25, second full paragraph, and makes confidential information about how the $17.1 million was repaid. This information is all highly relevant to the Presiding Officer's decision in this matter and the BSR's arguments and should not be redacted.

order and the consent order approved in this matter. Approval by DOL is also required to allow PLT to meet its financial responsibilities. PLT does not currently have DOL's approval to come out of run-off or to release any collateral.

The property liability coverage program is operating with a negative net position presented in Exhibit D at January 31, 2015 as negative $2,862,666. As of June 30, 2014, this figure was a negative $2,059,087. Exhibit C at 53. Property liability's net position is worsening, not improving, according to the data submitted by PLT.

The materials submitted by PLT contain this caveat: "Many of these assumptions are subject to significant business, economic and regulatory and other uncertainties and contingencies, many of which may beyond the control of PLT or the DOL." Exhibit E at 18. As this entire page is blacked out in the non-confidential version of this exhibit, Exhibit E-1, the BSR currently refrains from listing the assumptions to which this warning refers. However, it would be inappropriate not to publicly disclose the considerable caveats included in PLT's own materials, especially in light of PLT's agreement to accept the burden of proof in this matter.

Conclusion

The Presiding Officer identified conflicts of interest that were endemic to the parent and subsidiary model that was previously utilized by the LGC in his August 16, 2012 Final Order. The Supreme Court upheld this approach. 165 N.H. at 798. The Court also recited the Presiding Officer's finding that funds paid by the HealthTrust and Property Liability Trust to subsidize the Workers Compensation Trust did not "reasonably qualify as costs and reserves permitted to be retained by the statute." Id. at 801.

The Supreme Court upheld the Presiding Officer's rulings as follows:

> RSA 5–B:3 does not sanction what the presiding officer found occurred here. Here, three pooled risk management programs shared a *single* board of directors, even though RSA 5–B:5, I(b) requires each program to have its own board. Two of those programs then transferred funds to the third program, despite the fact that the three programs had *807 different members. Thus, funds that otherwise would have been returned to some political subdivision members were instead used to subsidize a pooled risk management program **402 that benefitted *other* political subdivisions. Under those circumstances, we cannot conclude that the presiding officer's finding that the post–2003 transfers from HealthTrust and P–L Trust to Worker's Compensation Trust violated RSA chapter 5–B was unlawful, unjust, or unreasonable.

Id. at 806-07. Here, PLT seeks permission to re-open for business using the same model that was so rife with fiduciary conflicts of interest that it was condemned by the Presiding Officer and the Supreme Court. In the current scenario, PLT claims sufficient financial health to re-open for business even though about half of the members do not participate in the workers compensation line of coverage, yet monies raised through premiums paid by these property-liability-only members were used to pay the $17.1 million debt and to post the $14 million in securities now with the DOL. The Bureau does not believe the PLT should be permitted to carry its burden of proof in this way.

As was raised by Justice Lynn during the argument in this matter, it is not the responsibility of the Court, nor of the BSR, to choose financial winners and losers. If a risk pool has adequate resources and has run a fair race, it should be permitted to compete in the market place. However, if a risk pool, such as PLT, has only competed through the use of illegal subsidies, it should not be permitted to compete just for the sake of promoting competition. As PLT has not shown it will carry the burden of proof to establish that both its programs are financially sound and able to operate without benefit of illegal subsidy, the BSR objects and urges the Presiding Officer to deny permission in this matter.

Respectfully submitted,
Bureau of Securities Regulation,
By its attorneys,
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Certificate

This pleading was served on all other counsel of record through the electronic filing system this 8th day of April, 2015.

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