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What the Local Government Center's Reorganization Means to Communities (And Taxpayers)

By Amanda Loder | December 6, 2012

The on-going fight between the state of New Hampshire and one of the nation's largest insurance risk pool managers is an important one, with millions of dollars of taxpayer money at stake.

It's also incredibly complicated.

As the Local Government Center implements changes ordered by a hearing officer–even as it appeals the ruling to the state's Supreme Court–we thought it would be a good time to bring everyone up to speed on the basics of the case, and why it matters.

In Case You Missed It: The Basics Of The LGC Case

The non-profit Local Government Center offers legal help, administrative workshops, and advocacy services for cities, towns, and school districts. It also manages risk pools for these groups. The idea is, if public workers and retired public workers from different communities band together as a massive group, they can get better rates from insurance companies.

Let's say you're a police officer with an LGC member community, like Portsmouth. Whatever the city pays on premiums goes into a large pot of money overseen by the LGC. The LGC then contracts with an insurance company. At this point, it's Anthem. So your health insurance card will read, "Anthem Blue Cross-Blue Shield" on top. And printed below that would be the manager of the risk pool, "Local Government Center." Your counterparts in Dover and North Hampton, who are also members of the pool, would have a similar card. As far as all these officers and their doctors are concerned, they have Anthem insurance. So, on the individual city worker level, the LGC is, for all practical purposes, invisible. It's only when you move up toward the administrative levels of local government that this entity is of any day-to-day concern.

The LGC isn't the only organization running these risk pools. There are hundreds all over the country. And Primex and SchoolCare also operate risk pools in New Hampshire.

But it's the LGC that's been the main focus of the state's ire.

Its health insurance pool, HealthTrust, is the largest in New Hampshire, insuring more than 50,000 people. The LGC also runs a Property-Liability Trust, and a Workers' Compensation program. Between these pools, the state reports the LGC manages about $500 million premiums. According to the journal *Business Insurance*, in 2009, HealthTrust alone was the third-largest risk pool in the country. In 2010, these three programs reported a combined $97 million in net assets–that's money beyond the premiums paid into the pools.

Under rules set up by the New Hampshire legislature in 1987, risk pool managers, like the LGC, have to maintain separate boards for each pool, and return surplus each year that members have paid into the system. In 2003, these pools and the New Hampshire Municipal Association (the LGC's forebear that provides legal, lobbying, and other services to members) consolidated into one group under the Local Government Center Board. It also involved some drama with LLC mergers in Delaware, which is summarized pretty well here. With the same people overseeing the whole system, the LGC beefed-up its net assets and reserves, and subsidized its Workers' Compensation program with money from other risk pools.

The Order: What The LGC Has To Pay Back

$33.2 million from HealthTrust

$17.1 million the Property-Liability pool siphoned from HealthTrust

$3.1 million from Property-Liability for communities that joined after June 14, 2010

Total: $53.4 million

The Secretary of State's Office, through the Bureau of Securities Regulation, argued these practices were illegal. They contended that the LGC was racking up money by overcharging cities, towns and school districts for health insurance and not returning enough surplus.

Hearing officer Donald Mitchell agreed. In August, he ordered the LGC to return more than $52 million to communities.* The Center appealed to the state Supreme Court and asked to halt implementing the order until the court issued a decision.

Last month, the court agreed to hear the LGC's appeal…but not to stay the order.

In the order, the Local Government Center was directed to do three key things: Restructure the organization to match legal requirements, pay more than $52 million back to communities, and buy reinsurance. That process will continue, even as the court hears the case.

In Excess: How Much Is Too Much?

The point that's gotten the most press is the $52 million refund. In his order, Mitchell noted part of the problem is that state law doesn't really spell out how much money is "excess" (surplus) that must be returned, or a way to calculate an appropriate figure for net assets (or "additional reserves").** So, until the legislature decides to hone the statute, Mitchell laid out what he called a "straightforward method of reserve calculation familiar to both the BSR and the LGC."

Beyond the various costs of doing business as a risk pool, the LGC is allowed to keep 15 percent of the cost of its claims as net assets–at the *most.* As far Mitchell's order is concerned, the rest goes back to communities.

And we're talking big money, here. By 2010, HealthTrust had racked up $86,782,000 in net assets by itself. In his order, Mitchell writes:

> *"These net assets derive from the earnings of the health trust and surplus allowed to accumulate from the premiums paid by the member political subdivisions and investment income. These remaining net assets when added to the substantial amount of funds transferred out of the health trust to LGC, Inc. represent an amount of earnings and surplus that may reflect a very successful "for profit" business, free in this instance of regulation by the insurance commission and exempted from paying any tax."*

The LGC is a non-profit, but contends it shouldn't have to give the whole $52 million back because it *already* returned tens of millions of dollars in surplus to member communities between 2003 and 2010. The organization answered most of our questions by way of email statements from LGC General Counsel David Frydman. He writes:

> *"The BSR is saying our reserves [net assets] should be less, but we don't think the amount they've suggested is prudent or conservative enough to protect the members of our pool and their employees…The level of capital reserves they are suggesting is too low, and therefore too risky, for members of the pool.*
>
> *In the end, the question is what is the proper level of net assets, i.e. reserves, that should be retained? We believe that decision should be left to the HealthTrust Board and the representatives of the HealthTrust pool who sit on that board."*

The LGC would have preferred to keep the equivalent of 20 percent of claim losses in net assets. The BSR argued it should be 10 percent.

So in the end, Mitchell split the difference and decided 15 percent should be enough–but not too much.

Refund Or Store Credit? How To Return $52 Million

But until that's settled in court, the LGC says it's paying municipalities and school districts back their surplus funds. The return is primarily happening through something called "contribution holidays." Basically, it's the insurance premium equivalent of store credit. When communities are due to renew their health insurance, they'll get a discount for the year based on the percentage they paid of the past year's surplus.

"Our board took action on the contribution holiday prior to the hearing officer's order," says LGC Deputy Director of Risk Pool Operations Wendy Parker.

2010 Net Assets Reported By LGC At The Hearing

HealthTrust: $86,782,000

Property-Liability"
$10,225,000

Workers' Compensation:
$177,000

Total: $97,184,000

Between this month and August of 2014, the board authorized a return of $20.8 million from HealthTrust alone. Combined with the Property-Liability surplus return, that works out to $22.5 million going back to communities.

Parker says the LGC hopes the Supreme Court will include that money in the $52 million the LGC was ordered to return. The LGC told StateImpact by email that their calculation "includes the accumulated net assets for all preceding years including 2003-2010,"–the period covering Mitchell's order.

But that doesn't sit right with Andru Volinsky. He's outside counsel for the Bureau of Securities Regulation.

"What the LGC has now done, is they've calculated their surplus for 2011. That's the $20 million. It has nothing to do with the hearing officer's calculation of the accumulation of surplus through 2010," Volinsky says.

Number-wrangling aside, it's the contribution holiday that's a tricky issue for some communities. Take Salem. For the period between 2003 and 2010, the LGC was ordered to pay members back their surplus in cash. Or, as the order lays out, "a negotiated plan may include prospective returns of cash or its equivalent."

As far as the BSR is concerned, that means the option of cash is on the table for communities that have opted to leave LGC coverage.

But the reality is different from where Salem Selectman Stephen Campbell is sitting. After hearing about the LGC's financial practices, he became a vocal supporter of leaving the its health insurance pool. Since May, town employees have been insured through Cigna

"The problem is that they've decided the way they're going to pay back the $52 million is a rate holiday," Campbell says. "Since we no longer get any insurance through LGC, there's nothing for them to discount. So we would not get our fair share, from having overpaid over the years. There's nothing for them to give us a rate holiday on."

He adds, "They were told that they were to pay back the money in cash. And so we're hoping that the state government will step in, squash this rate holiday nonsense, and pay the $52 million back to communities in cash. And then Salem will get what it's entitled to."

And even among municipalities that have stayed with LGC insurance, some are clamoring for cash. "The feeling is very strong that we want the money back," says Dover City Council member Catherine Cheney. Recently, she cosponsored a resolution calling for the LGC to return what the city estimates it's owed–$282,000–in cash. It passed, on a vote of 7-2.

Cheney says communities are entitled to their money. But at the same point, Dover isn't ready to give up on the LGC. "There aren't a lot of opportunities for people looking for insurance," she says. "They've been doing this a long time. So have a good HealthTrust program for the employees."

In fact, Cheney says, back in 2011, Dover decided to double-down with the LGC, joining the Property-Liability pool as well.

The “Handcuff Provision”

But complicating matters for communities that have left the LGC, like Salem, is something Volinsky calls a “handcuff provision” for some surplus return. Under last summer’s order, the LGC was required to pay back more than $52 million accumulated between 2003 and 2010. If communities that contributed to the LGC during that period left to go to another risk pool, under the order, they get their money back. In that case, a contribution holiday wouldn’t work.

But the 2011 surplus? It’s not covered by the order.

“In order to get that, members have to remain with the LGC for two years,” Volinsky says. “So even though they were overcharged in 2011, and the money is theirs and they’re entitled to it, under the LGC’s plan of return for 2011, member communities are handcuffed and must continue to purchase LGC insurance in order to get their share of the $20 million that is due to them.”

Since Salem left in May of 2012–before the scheduled refund disbursements for 2011–it’s out of luck.

For its part the LGC argues that its 2011 surplus return is consistent with its bylaws and the law governing risk pools and “with the agreement the Bureau of Securities (BSR) executed with Primex and SchoolCare.” The LGC’s David Frydman also notes in his email response:

> *“The rationale for this policy is that groups that join a risk pool are not required to pay their proportionate share of the required reserves in order to join the pool; and likewise, they are not entitled to a share of the reserves/surplus, if they have left the pool.”*

In other words, members can’t have their cake and eat it, too.

When Insurance Needs Insurance

Perusing the order, something that stands out is the requirement for the LGC to buy reinsurance. As the LGC’s Wendy Parker explains it, “That’s a type of insurance coverage that insurance companies or pools like ours can purchase to help absorb the impact of large losses.”

In the LGC’s case, they’re buying something called “Specific Stop-Loss Coverage.” That means if, say, a town government employee insured by the LGC gets cancer and racks up huge medical bills for treatment, the cost won’t drain the pool. An outside insurance company picks up the tab, instead. Parker is quick to say the reinsurance mandate is “a separate issue,” from the surplus refund.

So why was buying reinsurance part of the order?

"That's a good question!" Parker responds with a dry chuckle.

Volinsky's response is less than amused. "The Local Government Center has started a public relations effort to undermine the order by, at this point, focusing on the reinsurance piece," he says. "Reinsurance is something that the Local Government Center purchased through 2009. So this isn't a new concept."

In an statement to members published online on November 20, 2012, LGC Executive Director Maura Carroll explained the organization's position.

> *"HealthTrust stopped that practice in 2010 because, on the advice of HealthTrust's actuary, the reserves were strong enough to cover catastrophic claims, and there was no need to incur the expense of reinsurance…*
>
> *The end result is a potential one-time return of surplus and a yearly expense for reinsurance that will be a part of future rates."*

"You could hold hundreds of millions of dollars, and you'd have no risk of running out of money," Volinsky says. "But that's not how the legislature established risk pools. they're to act in a cost-efficient way for the benefit of their members. So this whole model was built on the idea that the insurer carry reinsurance so that they could return more surplus to the political subdivisions."

According to a November 19 memo issued by Parker to the HealthTrust Board of Managers, the reinsurance itself will cost $1.18 million a year. Tied to that are assessments the LGC will have to pay to the state: $1.37 million to the NH Vaccine Association and another $2.39 million to the NH Health Plan (the state's high-risk pool). Adding in a $60,000 broker fee, the LGC estimates the total annual cost at about $5 million.***

Reorganization: Rebuilding Boards…Or Not?

In his order, hearing officer Donald Mitchell found the LGC's 2003 reorganization of its risk pools under a single board to be illegal. He noted it "serves to diminish the priority interest and benefits" of the individual pools, adding, "The organizational relationship also results in a conglomerate imbued with conflicts of interest adverse to the required standards for operation of each pooled risk management program."

But the LGC contends member services and efficiency were key drivers behind its reorganization. Responding to StateImpact's questions about the reorganization by email, Frydman laid out the LGC's argument:

> *"One board was able to provide one stop shopping, with programs designed to meet all the needs of the members, in the most cost effective and efficient manner. The one board model recognizes the value of developing integrated products, overlapping*

trainings and common risk mitigation activities designed to reduce total cost and risk to the members and their employees."

The organization also notes that three separate boards–HealthTrust's, Property-Liability Trust's and the New Hampshire Municipal Association's–voted to consolidate under one board, so "each thought it was in their members' interests to consolidate into the single board model."

In November, the LGC announced it's switching back to the pre-2003 multi-board model, in compliance with the order.

But attorney Andru Volinsky and the Bureau of Securities Regulation aren't convinced the organization is in full compliance.

"They don't have new board members. Everyone who's at Health[Trust] now, and who's on the Board of Managers for Property-Liability was and is an LGC Board member," Volinsky says. "They're the same people with the same senior executive staff. If you want to look at this operationally, nothing has changed."

He says the BSR is reviewing the paperwork and considering what, if anything, it should do about the LGC reorganization. But, "their initial impression is that this was a reorganization that does not comply with the spirit of the law."

The LGC takes exception to that characterization, noting that it's done exactly what the hearing officer ordered–create two separate boards for the Property-Liability and HealthTrust pools, each with their own bylaws and members. And while everyone on these two boards *is* a member of the LGC board, at the same time, membership in the two risk pool boards *doesn't* overlap.

The organization also points out in emails to StateImpact that during the last annual meeting, "two brand new individuals were elected to the LGC Board." And, the statement said, one now sits on the HealthTrust Board, while the other new member is on the Property-Liability Board.

What's Next?

The LGC reports that in 2011, nine out of ten local New Hampshire governments participated in at least one of its lines of insurance coverage. That means that despite some defections from communities like Salem, numerous town managers, workers, and labor groups will be dealing with the LGC for the foreseeable future.

Professional Firefighters of New Hampshire President Dave Lang has been an early–and vocal–critic of the LGC. "Every single time we're at the bargaining table, across the state, one of the things that continually comes up is the rising cost of health care," Lang says. "And we find ourselves in this uncomfortable situation of having to defend health care benefits for full-time employees when we don't have the assurances that the money being paid into this risk pool is money that's actually going for health care."

Dover City Councilwoman Catherine Cheney is concerned negotiations could have been compromised with city workers. "If we'd been charged the rates we should've been charged, we would've had more money as a community to say, "Well, this is how much we can compromise on" in any contracts," Cheney says. "Because that's what it's all about, when you sit down with different unions in the city. What do you hope to see as an employee in the next few years? And what do we hope to see as an employer over the next few years?"

Lang says that the state's biggest population centers–Manchester and Nashua–aren't part of the LGC. So there, at least, past negotiations haven't been compromised by the LGC's practices.

While the order aims to fix these kinds of problems for LGC member communities in the future, Lang expects it to be a continuing problem. "I think they're trying as hard as they can to continue business as usual."

For its part, the LGC says it's in full compliance with the order–which it's also trying to overturn.

While the New Hampshire Supreme Court has agreed to hear the LGC's appeal of Mitchell's decision, it hasn't set a date yet. Volinsky says the BSR is considering whether it's worth bringing a new case against the LGC alleging it violated the order before the appeal makes it to court.

**It's popularly referred to in the media as "more than $52 million" or just "$52 million," but the numbers as laid out in the order actually add up to more than $53 million.*

***The LGC frequently refers to its net assets as "reserves." In his order, Mitchell often calls net assets "reserves" or "additional reserves." As BSR outside council explained it to StateImpact, when state law refers to "reserves," it means the amount of money a risk pool manager has to keep back for things like end-of-year claims. In other words, if someone goes to the Emergency Room on December 31, 2012, the bill won't show up until 2013. The LGC, then, would need to hold some money from 2012 in reserve to take care of these late bills.*

****Professional Firefighters of New Hampshire President Dave Lang disputes that the LGC is required to pay these assessments.*

Ed. Note: We corresponded with the Local Government Center through spokesperson Laura Simoes. Originally, this story named Simoes as responding for the LGC. After posting, she contacted us to clarify that the answers were actually composed by LGC General Counsel David Frydman. The attributions have been changed to reflect this clarification.

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