Department of Planning and Budget
2004 Fiscal Impact Statement

1. **Bill Number** SB601

   House of Origin ☐ Introduced ☐ Substitute ☐ Engrossed

   Second House ☐ In Committee ☐ Substitute ☒ Enrolled

2. **Patron** Newman

3. **Committee** Passed Both Houses

4. **Title** Medical professional liability insurance; state risk management plan

5. **Summary/Purpose:** The bill would provide professional medical liability insurance to physicians and sole community hospitals under the state's risk management plan under certain cases if they were not able to acquire adequate private insurance coverage. A physician qualifies to enter the risk management plan if he or she holds a valid medical license, practices mainly in Virginia, participates in the Medicaid program or provides services at a "free clinic", participates in the Virginia Birth Related Neurological Injury Fund if eligible, and has active hospital privileges or participates in a quality assurance committee. The final requirements to qualify for the state plan are to participate and cooperate at their own expense with a medical risk management plan and to fulfill other criteria as required by the Division of Risk Management. A sole community hospital has the same requirements as a physician to qualify for the state plan.

   The physicians and hospitals that qualify would be required to pay premiums to cover all the costs of the risk management plan including the costs to administer the plan by the Division of Risk Management in the Department of the Treasury. The physicians and hospitals that choose to purchase coverage under the state plan would also have the option to purchase extended reporting period endorsement coverage for a period not to exceed 10 years from the date of retirement. The coverage under the state plan can be renewed for as long as the physician and hospital meet the requirements of the state plan. The division is also authorized to provide coverage for general liability to sole community hospitals.

   The bill has a second enactment clause that requires the chairman of the Senate Committee on Rules to appoint three members of the Senate and the Speaker to appoint four members of the House of Delegates to a joint subcommittee to study the availability and affordability of professional liability insurance for physicians and hospitals in the Commonwealth. The Office of the Clerk of the Senate and the Division of Legislative Services shall provide staffing, Bureau of Insurance at the State Corporation Commission shall provide technical assistance and the subcommittee shall receive information and input from the Medical Society of Virginia, the Virginia Trial Lawyers Association, the Virginia Hospital and Healthcare Association and other interested parties. The subcommittee is limited to four meetings and direct costs of no more than $7,000. The findings of the subcommittee shall be reported to the Senate Committee on Courts of Justice and the House Committee for Courts of Justice by December 1, 2004.

The bill has a third enactment clause stating that the provisions of the bill allowing the purchase of general liability and medical malpractice insurance under the state risk management plan shall not take effect until July 1, 2006.

6. **Fiscal Impact Estimates are final:** SEE ITEM 8.

6a. Expenditure Impact: This impact only shows the impact on the state budget.

Fiscal Year	*Dollars*	*Positions*	*Fund*
2003-04	$0	-	-
2004-05	$7,000	-	GF
2005-06	$0	-	-
2006-07	$2,099,000*	1.00	GF
2007-08	$99,000*	1.00	NGF
2008-09	$99,000*	1.00	NGF
2009-10	$99,000*	1.00	NGF

*In any year where the fund has insufficient cash to pay claims, funding from a treasury loan would have to be used to cover the claims.

6b. Revenue Impact: SEE ITEM 8.

7. **Budget amendment necessary:** No. The only impact in the 2004-2006 biennium is for the cost of a study, which will be funded from existing resources.

8. **Fiscal implications:** The bill would have a fiscal impact on the Commonwealth. A study required by the bill is authorized to expend up to the $7,000 for direct costs, which will be funded from existing funds at the discretion of the General Assembly. Beginning in fiscal year 2007 when certain provisions of the bill go in effect the bill would add, under the state's risk management plan, medical liability coverage for physicians and community hospitals. The state's risk management plan primarily provides coverage for public entities, but this bill extends coverage to private individuals and private entities. Therefore, in order to provide such coverage the Department of the Treasury would have to set up a separate risk management plan. The current risk management plan is self-insured. Therefore, the department charges premiums to cover all of the costs of the plan. Including coverage for non-governmental entities requires such coverage to be segregated into a separate plan so that public funds are not mixed with private funds. This already occurs in the case of local government liability, which is segregated so that only local government premiums support the plan and not state funding.

With regard to the cost of the bill to the state, the risk management plan (hereafter "plan" references the risk management plan created by this bill) is impacted in two ways: administrative and programmatic. The Department of the Treasury will incur additional costs for one staff position and operating costs to handle the increased workload and to deal with the specialized nature of the insurance coverage provided. The following details the administrative costs.

Administrative Costs	FY 2007	FY 2008
Program Manager	$89,000	$89,000
Operating Costs	$10,000	$10,000
TOTAL	**$99,000**	**$99,000**

The administrative costs of the plan include staffing for one additional position within the department. This includes $89,000 for a program manager ($70,000 annual salary and $19,000 for fringe benefits) and $10,000 in operating costs for administration of the contract with a third party administrator. Due to the specialized nature of the insurance coverage, the department would contract with a third party administrator to handle all aspects of the administration of the insurance program, such as claims management, eligibility, actuarial analysis, premium collections, and legal representation. The position in the Division of Risk Management will be responsible for handling all aspects of managing the contract with the third party administrator to ensure that all provisions of the insurance program are handled properly. The state would also be responsible for making the claim payments.

Initially, the Commonwealth will have to use its own funding to cover the startup administrative expenses of the plan until premiums are collected and the plan becomes self-supporting. After premium revenue begins to be collected, the third party administrator will provide some of the revenue to the state for its share of administrative expenses for the program.

Programmatic Costs
The major cost to the state, at least initially, will be the programmatic expenses of the plan involving claim payments. Until the premium revenue is sufficient to cover the full costs of the program, the Commonwealth would have to use its own resources to cover such costs.

The initial estimate of upfront state funding for programmatic costs is $2.0 million. This amount is based on the fact that enough funding should be available to pay one significant claim. The current medical malpractice limit for damages is limited to $1.7 million under state law. Allowing some leeway for other claims brings the estimate to a total of $2.0 million. If for some reason the claim payments were higher, then the state would have to cover those costs to ensure the plan has sufficient funding to cover its costs. However, the claims costs for the first year should not be significant since it generally takes a substantial period of time to settle a medical malpractice claim.

Impact on the State
State funding is impacted in two ways by the bill. First is the amount of initial funding that is necessary to begin to pay expenses of the plan until premium revenue is sufficient to cover those costs. This amount is expected to be $2,099,000 ($2,000,000 programmatic and $99,000 administrative) in FY 2007. This amount of funding must be funded from state resources in order to start the insurance program.

The second impact on the state could occur due to insufficient funding of premium revenue to cover all of the plan's expenses. The actual number of physicians and community hospitals to enroll in the plan is a significant unknown and indeterminable at this time. There are 14 community hospitals and hundreds of physicians who could potentially enroll in the plan depending on the criteria setout by the Division of Risk Management. Therefore, with the size of the pool and thus the state's ultimate liability a significant unknown, the state would have to use its resources to make sure all the expenses of the plan are paid. Considering that the plan provides for extended coverage for up to 10 years after physicians retire, it is not possible to determine the state's total financial exposure of the plan at this time. However, any actuarially determined unpaid claims liability will be reported on the Commonwealth's balance sheet along with the appropriate footnote disclosure on the risks on the plan.

Assuming that the premium revenue, once it begins to be collected, is sufficient to cover all the costs of the plan, then the initial funding provided by the state can be repaid. Therefore, the plan will likely have higher premiums initially in order to pay off the upfront costs.

The Department of the Treasury does have a line of credit authorized in the Appropriation Act in the amount of $15 million. The line of credit allows the agency to use general fund cash balances on a temporary basis. Since using the line of credit would cost the state interest on those balances and since it is designed to be an emergency reserve for the entire risk management program, it should not be used for the initial cost of starting a plan for physicians and community hospitals. However, since this bill expands the risk management program and creates a potential cash flow shortfall for the state, the line of credit should be increased to cover any potential losses.

Premium Cost of the Plan's Coverage
According to information the Department of the Treasury has received, the initial plan may have very few physicians and potentially one community hospital that qualify for coverage. Based on the initial estimate of upfront costs of nearly $2.1 million, the amount of premiums charged for the first year would likely match that amount. However, it is difficult to estimate the amount to be charged since the size of the insurance pool is not really known with any certainty and there is no claims history available to make an actuarial estimate. The total pool itself is likely to be extremely small making it hard to spread the risk. Therefore, it is unknown whether the premium level will be any more affordable than insurance provided through the private sector. The premium of each physician and community hospital will be based on claims history and other criteria as determined by the Division of Risk Management and the third party administer of the insurance program.

9. **Specific agency or political subdivisions affected:** Department of the Treasury and the General Assembly.

10. **Technical amendment necessary:** No.

11. Other comments: The State of West Virginia created a similar program within its risk management program in December 2001. Premium rates are required to be at least as high as any insurer with at least five percent of the market in the state.

During the fiscal year-ended June 30, 2003, the program insured 1,193 physicians, 15 hospitals, and 19 clinics. The program sustained an operating loss of nearly $2 million during the year on premium revenues of nearly $21 million. Program assets totaled nearly $56 million, which included a $24 million loan to the West Virginia Tobacco Settlement Fund. Current liabilities exceeded $42 million, including a loan from the State of West Virginia of $24.5 million. Long-term liabilities primarily consisted of estimated claims incurred but not reported of $16 million. At year-end, the program's unfunded liability totaled nearly $2.7 million.

Effective July 2004, newly passed legislation will end the West Virginia program under the state's risk management program and all the insured physicians, hospitals and clinics will be transferred to a newly created physicians mutual insurance company. The West Virginia statute that makes the change states that the change is due to the state's determination that the state-run program is a substantial actual and potential liability to the state. The state legislature also found that a physicians mutual insurance company has been a successful mechanism in other states. The company is a domestic, private, nonstock, nonprofit corporation, which has been incorporated and is in the process of becoming licensed. West Virginia has committed to providing the physicians mutual company with a $24 million capital loan.

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cc: Secretary of Finance