MEMORANDUM

To: Banking Committee

From: Board Office

Subject: Iowa Mutual Medical Insurance Company (SUI)

Date: September 8, 2003

Recommended Actions:

1. Recommend the Board authorize the University of Iowa to assist with the formation of a captive mutual insurance company for the purpose of providing medical liability insurance, within defined limits, for the participants of the Carver College of Medicine Faculty Practice Plan.

2. Discuss the recommended capitalization (funding mechanism) of the mutual insurance company, and, recommend the Board authorize the University of Iowa to purchase surplus notes from the mutual company to be formed in the amount of $20 million to meet the statutorily required insurance surplus.

Executive Summary:

On January 1, 2003, the Faculty Practice Plan (FPP) at the University of Iowa Carver College of Medicine (CCOM) lost its commercial medical liability insurance. In March of this year, the Board authorized the University of Iowa to formalize a self-insurance program to protect the state and members of the FPP from liability claims, within defined limits, resulting from the operation of the Plan. The Board also delegated the Board's Executive Director authority to review and approve the self-insurance program, based upon the counsel and advice of the Board and the Board president, prior to implementation.

The University created a Task Force with representatives from the CCOM FFP, the Office of the General Counsel, the University Risk Manager, Board leadership, Board Office personnel, and other relevant parties, that considered alternate methods of liability coverage for the FPP.

The University proposes to assist with the formalization of a mutual insurance company to insure the professional medical liability exposures of the University of Iowa Carver College of Medicine (CCOM) FPP. This memorandum sets forth the history of the FPP's insurance coverage, identifies the benefits of the establishment of a mutual insurance company, and details the establishment of the Iowa Mutual Medical Insurance Company (IMMIC).

In addition to authorizing the University to assist with the establishment of IMMIC, the Banking Committee is requested to discuss the proposed capitalization for the mutual insurance company by the issuance of a surplus note to be purchased by the University of Iowa.

Background:

Historical Perspective

The University of Iowa Carver College of Medicine (CCOM) Faculty Practice Plan (FPP) has purchased commercial insurance at least since the 1950s. The coverage originated when the state was exempt from tort liability, an exemption that did not extend to the University of Iowa physicians.

When the state enacted the Tort Claims Act, Iowa Code Chapter 669, (the Act) in 1966, it waived its tort exemption. This did not significantly change the exposure for the Plan members; therefore, the commercial insurance coverage was continued.

In 1977, the Act was modified to define the state's obligation to defend, indemnify, and hold harmless state employees from liability arising out of their employment. While employees of the University of Iowa, including those in the FPP, are entitled to indemnification and defense pursuant to the Act, commercial coverage was continued as specifically authorized by the Act.

Liability Insurance

The FPP purchased the level of commercial insurance it determined was needed to cover its participants.

In December 2001, the St. Paul Fire and Marine Insurance Company, which provided the FPP's insurance, announced its decision to phase out its medical liability program. That coverage expired December 31, 2002, and was not renewed.

In March 2003, the Board authorized the University of Iowa to formalize a self-insurance program through a 28E intergovernmental agreement with the Attorney General, Appeal Board, Executive Council, University of Iowa, and Board of Regents, to protect the state and members of the FPP from liability claims. The coverage provides $5 million per claim with an annual aggregate limit of $9 million per year. Initially, the program would terminate on June 30, 2004, with options for renewal for additional one-year terms.

Task Force

The University created a Task Force with representatives from the CCOM FFP, the Office of the General Counsel, the University Risk Manager, Board leadership, Board Office personnel, and other relevant parties, to consider alternate methods of liability coverage, which included:

- The purchase of commercial insurance to replace the St. Paul coverage was not obtainable at a reasonable cost.

- Informal self-insurance potentially exposes the FPP and the University to possible catastrophic risk.

- The establishment of a mutual insurance company.

Analysis:

Mutual Company Benefits

The Task Force agrees that a mutual company:

- Represents a solution for liability coverage in the present environment
- Creates a formal structure for segregating loss funds
- Sets a framework for claims management
- Provides the ability to separate average predictable losses from infrequent potentially catastrophic losses.
- Offers similar benefits to those previously provided by St. Paul Fire and Marine Insurance Company;

IMMIC

A non-profit mutual insurance company, the Iowa Mutual Medical Insurance Company (IMMIC), would be formed effective January 1, 2004, (the date policies will be issued to individual FPP physicians) to insure the professional medical liability exposures of the CCOM FPP.

It would be an Iowa-domiciled mutual insurance company owned by the policyholders.

- The FPP is limited to faculty within the CCOM who are involved in clinical care.
- Those individuals and the FPP would be the policy holders of the IMMIC.

In exchange for payment of each policyholder's premium by the FPP, the faculty members will proxy their member votes to the Dean of the CCOM.

Initial Board of Directors will consist of seven members:

- Five faculty in the CCOM.
- Two members from the University administration outside the CCOM. (The University has representation on the IMMIC Board by virtue of the proposed funding mechanism identified below.)

Consultation was received from the Offices of the Iowa Attorney General and the Iowa Insurance Division. No objections were raised.

Proposed Coverage

The FPP would continue to maintain a self-insured retention (SIR) of $3 million per event.

Each IMMIC policy would cover $2 million per event above the SIR.

The coverage by IMMIC would be a claims-made policy and subject to a self-insured retention (SIR) similar to the coverage previously provided by St. Paul.

Claims arising out of occurrences prior to that date would remain the responsibility of the FPP self-funded program.

Pursuant to a proposed amended 28E agreement, and as required by the Act, the State of Iowa would agree to defend and assume responsibility for any loss exposure to the FPP resulting from aggregate claims paid by the FPP and IMMIC in excess of $5,000,000 per occurrence and $9,000,000 aggregate per fiscal year.

Funding Mechanism

The start-up funding for the mutual company would need to consist of the first year of premiums and the required statutory insurance reserve surplus.

The University of Iowa would purchase $20 million in surplus notes from IMMIC (effectively loaning funds to IMMIC) to meet the statutory surplus requirement.

- The issuance and any repayment of surplus notes at maturity by the mutual insurer would be subject to the approval of the Iowa Insurance Division.
- IMMIC will pay the University interest on the note quarterly at a rate of no less that the average return received from the investment of the University's other operating funds.
- The University will appoint members to the IMMIC's Board of Directors, as authorized by Iowa Code §515.20.
- The surplus notes can be carried as part of non-admitted liabilities, making them useful financing tools to raise regulatory capital.

Under the mutual insurer option, individual policies will be issued to the insured physicians, with premiums paid by the FPP, on behalf of the individuals covered.

Dividends, as may be declared by the IMMIC Board of Directors and as allowed by statute, would be based on the amount of premiums paid and the number and types of policies held. Those dividends would be remitted to the FPP, which paid the premiums.

Specific Benefits of IMMIC

The Task Force agrees that IMMIC would:

- Allow the University to segregate funds committed to the medical liability exposure. Over time, the IMMIC could build capabilities that would increase risk retention options.
- Provide continuity as the IMMIC would work with the same claims administrator (Cambridge) that the FPP utilized in managing claims under the previous self-insured retention program
- Allow the FPP to isolate frequent, predictable losses from large, infrequent and unpredictable losses.
- Allow the FPP to access reinsurance on favorable terms if necessary in the future.