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NEWS FROM THE VERMONT STATE HOUSE

CAPTIVE LEGISLATION PASSES BUT OVERALL SESSION NOT DONE YET

The Vermont General Assembly adjourned on May 18, two weeks after a targeted adjournment date, and without the usual fanfare as legislators knew a veto session was likely on the horizon. That was confirmed by Gov. Phil Scott (R) who all but promised vetoes of the FY18 budget and an education property tax bill in his adjournment comments to legislators and later with his pen returning those bills to the Legislature. While June 21 was set as the date to return to address those vetoes and any others, such as a marijuana legalization bill also vetoed by the Governor, this piece is written before the veto session so we can't speak with accuracy as to the outcome. We are confident, however, that regardless of the political winners and losers in this debate, there will be a budget in place before the start of the fiscal year on July 1, and municipalities will have guidance from Montpelier in setting the statewide property tax rates for the next year.

The delay in adjournment and the upcoming veto session revolve around potential savings in teacher health care contract negotiations and the mechanism under which to achieve those savings, all tied somewhat to the statewide property tax rates funding education, and to the General Fund budget. At a time when all teachers are renegotiating health care benefits because of a change brought on by the federal Affordable Care Act, Gov. Scott has proposed moving negotiation of those teacher benefits from the local, collective bargaining level between teachers and school boards to a statewide contract negotiated by the State. The Governor believes this can result in \$26 million in savings to Vermonters this year and further rebase the education fund going forward to ensure continued savings. While Legislative leaders floated alternative proposals that achieved similar savings, they ultimately could not give on collective bargaining, a long-held Democratic principle.

The Governor certainly seemed to have the majority of the public behind him in his call for the Legislature to achieve those \$26 million in savings to the taxpayers now, when many are still worried about their personal economics. The Governor successfully leveraged the power and resources of his office to bring this message to the public through a variety of means that put the Democratic leadership in the Legislature on its heels. It is likely, however, that the pendulum will now swing to the Legislature's side, and precisely because of the timing. With the State's fiscal year end set to expire June 30, that obviously does not afford a great amount of time to put an alternative budget in place before the start of the next fiscal year end. The Governor also does not want to be seen as the reason for a possible shutdown of state government. Legislative leaders extended the session and made several alternative proposals to the Governor, all of which he rejected.

The drama of recent weeks livened a legislative session that heretofore had been largely mundane. We knew it would take some time for the session to unfold with new leadership in the House and Senate and some changes in committee make-up. Add to that a new Governor and team that, in some cases, were still finding their offices and meeting their staff while the session had already been underway for a few weeks. This inexperience among the Legislature and Administration surely added to the clunky adjournment but will be a learning experience for all and largely forgotten – until this time next year. There will be no such excuses then nor will they likely be necessary.

In the meantime, and prior to this current stalemate, the Legislature was able to pass and the Governor sign into law a series of amendments to Vermont's captive insurance laws. Act 12 (introduced as H.85) became effective on May 1 with the Governor's signature in a public, ceremonial event at the State House. As is typical of Vermont captive legislation, the bill contains a series of technical amendments that reflect lessons learned in practice or implementation of the laws, as well as a series of new ideas aimed at enhancing Vermont's position among increasingly competitive captive domiciles.

Among the enhancements, Vermont will now entertain applications for agency captive insurance companies, albeit with a few Vermont-specific requirements. While other captive domiciles have authorized such formations, Vermont regulators were historically cool to the idea for a number of reasons. Those were partially satisfied by amendments aimed at transparency and highlighting to the policyholders the relationship between the agency captive and its affiliated insurance agency or brokerage. Specifically, agency captives and affiliated insurance agencies or brokerages must meet these requirements:

- An insurance agency or brokerage that owns or controls the agency captive insurance company remains in regulatory good standing in all states in which it is licensed;
- The agency captive insures only the risks of the commercial policies that are placed by or through an insurance agency or brokerage that owns or directly or indirectly controls the agency captive insurance company and, if required, provides the Commissioner the form of such commercial policies;
- The agency captive discloses to the original policyholder or policyholders, in a form or manner approved by the Commissioner, any limitations, rights, and obligations held by the agency captive insurance company as a result of its affiliation with an insurance agency or brokerage; and
- If required by the Commissioner in his or her discretion, the business written by an agency captive insurance company is:
 - Fronted by an insurance company licensed under the laws of any state.
 - Reinsured by a reinsurer authorized or approved by Vermont.
 - Secured by a trust fund in the United States for the benefit of policyholders and claimants or funded by an irrevocable letter of credit or other arrangement that is acceptable to the Commissioner.
- Maintain minimum capital and surplus not less than \$500,000.00.
- Be owned or directly or indirectly controlled by one or more insurance agencies or brokerages licensed under the laws of any state and that only insures risks of policies that are placed by or through such agency or agencies, or brokerage or brokerages, as applicable.
- Be incorporated as a stock insurer with its capital divided into shares and held by the stockholders, as a nonprofit corporation with one or more members, or as a manager-managed limited liability company.
- Comply, along with association captives and risk retention groups, with the investment requirements for traditional insurers.

Among other enhancements, Vermont's law allowing pure, sponsored or industrial insured captives to apply for a certificate of dormancy is now expanded to allow any captive insurance company to apply for such dormant status. All other aspects of the dormant law remain unchanged. And in the realm of technical amendments, the law now makes it clear that a captive may use statutory accounting principles or international financial reporting standards in its annual report without first receiving permission from the Commissioner. However, the captive must now state which reporting method it intends to use in its application for admission, and any change in the reporting method requires prior approval. In addition, protected cells that choose to incorporate are now only required to have "protected cell" or "IC" in their names and not the traditional corporate naming conventions in addition thereto. Governance standards for risk retention groups also have been further tweaked to provide relief from auditor partner rotation requirements, including the ability to

request a waiver from such requirements subject to certain conditions.

And finally, an amendment passed in another bill that revises and expands Vermont's premium tax credit for new captive formations. As they now see more and more states looking for a piece of the captive business, the Vermont Legislature and Governor responded to industry suggestions to try to make Vermont an even more attractive domicile for new captives, particularly for some of the smaller programs. The amendment increases the existing \$7,500 first year tax credit for new formations to \$10,000 over the first two years. The idea is that increasing and spanning the tax credit over a couple of years will be attractive to captives facing start-up costs in the first few years of formation. This amendment, while originally a part of H.85 as introduced, was taken from that bill and added to a miscellaneous tax bill that contained numerous tax-related issues. That bill, H.516, has yet to be signed into law by the Governor though that is expected to occur in the coming days. If so, the revised credit will take effect July 1 and apply to new formations on or after January 1, 2017.

We will continue to report on captive insurance legislative and regulatory matters in future issues, and on other developments impacting the captive insurance industry.

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