

10-15-2004

## 2004 Ballot Measure Report Measures 34 & 38

City Club of Portland (Portland, Or.)

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## 2004 Ballot Measure Report Measure 34

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### **State of Oregon Ballot Measure 34:**

REQUIRES BALANCING TIMBER PRODUCTION, RESOURCE CONSERVATION/PRESERVATION IN MANAGING STATE FORESTS; SPECIFICALLY ADDRESSES TWO FORESTS

Your committee finds that management of state forests requires the balancing of many competing interests, chiefly protecting the environment while maintaining timber harvests. Measure 34 would impose a new standard for balancing these interests and change the current plan for managing the Tillamook and Clatsop State Forests.

Your committee finds insufficient evidence that the long-term health of the forest lands is threatened by current management policies, or that the 50 percent reserve for the Tillamook and Clatsop State Forests mandated by Measure 34 would better serve the interests of the citizens of Oregon. Measure 34 does not offer a better approach to forest management policy.

**Your committee unanimously recommends a NO vote on Measure 34.**

*City Club members voted on October 15, 2004 to adopt the contents and recommendation of this report as the Club's official position. City Club recommends a NO vote on Ballot Measure 34.*

## I. INTRODUCTION

Ballot Measure 34 will appear on the ballot as follows:

**REQUIRES BALANCING TIMBER PRODUCTION, RESOURCE CONSERVATION/PRESERVATION IN MANAGING STATE FORESTS; SPECIFICALLY ADDRESSES TWO FORESTS**

**Result of "Yes" Vote:**

Requires managing state forests balancing, as equally beneficial, conservation/preservation and timber production; manages Tillamook, Clatsop forests half for restoration, half for production.

**Result of "No" Vote:**

Retains current law allowing mixed use state forest management; rejects: requiring management that values conservation and production equally, separately managing Tillamook, Clatsop Forests.

**Summary:**

Current law directs that Board of Forestry manage all state forests to maximize "permanent value" (defined by board) through mixed use, including timber sales, mining, protecting, conserving, utilizing forests. Measure requires management defining "permanent value" as balancing sustainable timber production with water, wildlife, watershed protection, recreation, forest restoration, considering resource conservation equally beneficial to timber production. Manages Tillamook, Clatsop Forests half for forest restoration, prioritizing drinking water, habitat, fish protection; half for sustainable timber production, with restoration management steps recommended by restoration science team. Addresses using timber revenues for common School Fund, forest restoration management (board providing additional funding as needed); continues current local school funding levels. Measure declares it replaces any other management plan for Clatsop, Tillamook Forests adopted in 2004 election. Other provisions.

**Estimate of Financial Impact:**

With respect to the Tillamook and Clatsop State Forests:

The measure is estimated to increase state expenditures by \$1.5 million to \$6.3 million per year;

The measure is estimated to decrease state revenue by \$4.2 million to \$10.3 million per year;

The measure is estimated to require approximately \$2 million of one-time state expenditures;

The measure is estimated to decrease revenues for local governments by \$17.2 million to \$19.4 million per year; and

There is no financial effect on local government expenditures.

The impact of the measure on other state forests cannot be determined.

*(The language of the caption, question, and summary was prepared by the Oregon Secretary of State.)*

The petitioners who placed Ballot Measure 34 on the November 2004 ballot seek to redefine current state forest management policy, and to set specific limits for the Tillamook and Clatsop forests. Proponents call Measure 34 the "50-50 plan" because it would set aside one-half of the Tillamook and Clatsop forests as a permanent reserve for "restoration of a native old growth forest," while allowing sustainable logging on the remaining half of the land. Measure 34 would also change the definition of the term "permanent value," which is employed in managing all state forests.

City Club created a committee of eight Club members to analyze Measure 34 and issue a voting recommendation to Club members and other voters. Committee members were screened to ensure that no person had an economic or personal interest in the outcome of the study or has taken a public position on the subject of the measure. The study was conducted from August 9 to September 22. The committee interviewed proponents and opponents of the measure and other interested individuals, and reviewed relevant articles, reports and other materials.

## **II. BACKGROUND**

### **State Forest Management and Measure 34**

Chapter 530 of the Oregon Revised Statutes authorizes the Oregon Board of Forestry ("the Board"), a group of private citizens appointed by the Governor, to obtain and manage state forest land.<sup>1</sup> State law and policy mandate that the Board be comprised of individuals representing a balance of interests. Current state law directs the Board to manage the forest land for the "greatest permanent value" through a mixed use approach that includes timber sales, mining, conservation and utilization of the forests.<sup>2</sup> The current definition of greatest permanent value requires that the Board manage "healthy, productive and sustainable forest ecosystems that over time and across the landscape provide a full range of social, economic and environmental benefits to the people of Oregon."<sup>3</sup> The Board directs the State Forester how to achieve the "greatest permanent value." The State Forester, in turn, manages state forestlands as the head of the Oregon Department of Forest ("the ODF"). At present, the state of Oregon owns approximately 3 percent of all forestlands in Oregon; the federal government and private landowners own most of the state's forests.

In January 2001, following several years of study and public input, the ODF adopted its current Northwest Oregon State Forests Management Plan ("Forest Management Plan" or "the Plan"). The Tillamook and Clatsop State Forests are among the forests managed pursuant to the Plan.

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<sup>1</sup> ORS 530.010

<sup>2</sup> ORS 530.050

<sup>3</sup> OAR 629-035-0020(1)

Measure 34 appears on the ballot following two unsuccessful efforts in the 2003 Legislature to change the management of the Tillamook and Clatsop forests. Senate Bill 430 would have enacted a version of the 50-50 plan now embodied in Measure 34. Another bill, House Bill 3662, would have required the state to pursue increased logging in the state forests. Neither bill became law.

A coalition of more than 30 businesses and conservation groups, including the Audubon Society, the Sierra Club, Oregonians for a Balanced Tillamook and The Wild Salmon Center, endorse the citizen initiative that will appear on the November 2004 ballot as Measure 34.

Passage of Measure 34 would require the Board to manage the Tillamook and Clatsop forests in a way that permanently restores "a native old growth forest on 50 percent of those lands over time." The other half of the forests would be managed for sustainable timber production. Measure 34 would create an Independent Restoration Science team to develop a management plan to meet these goals. Measure 34 would further change the definition of "permanent value" to require that the Department of Forestry, the Board of Forestry and the State Forester, when making management decisions for all state forests, to "consider the conservation of land for drinking water, recreation and fish and wildlife habitat to be as beneficial to the state as timber harvests."

#### **Tillamook and Clatsop State Forests: A Brief History**

Spanning Clatsop, Tillamook and a small portion of Washington and Columbia counties, the Tillamook and Clatsop State Forests comprise over 500,000 acres of primarily second generation growth forest, and about two-thirds of all state-owned forestland. These two forests within the northern Oregon Coast Range are part of the largest contiguous temperate rainforest in the lower 48 states.

The Tillamook State Forest is well known to many Oregon residents because of the "Tillamook Burn," the collective name for a series of wildfires that struck the northern Oregon Coast Range in the 1930s and 1940s. Four significant fires blackened more than 550 square miles of privately held lands and brought profound environmental, economic and social change to Northwest Oregon. These successive fires interrupted the normal regeneration that follows a forest fire.

After the fires, the owners of the affected forestlands allowed their property to be foreclosed by the counties rather than pay taxes. Counties began to deed land in the Tillamook Burn to the Board of Forestry in 1940, pursuant to a state law that authorizes counties to convey tax foreclosed forest lands to the Board of Forestry for reforestation. Under that law, the state manages the land as state forest land, and the state and the transferring county divide revenues derived from the land.<sup>4</sup>

In 1948, the Legislature submitted to voters a proposal for a \$12 million reforestation bond to finance the reforestation of the Tillamook Burn area. Reforestation started in November 1949.

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<sup>4</sup> ORS 530.010 to 530.170

While many Oregonians remember participating in replanting the Tillamook Burn as schoolchildren, in fact, helicopter seeding, hired workcrews and prison inmates accomplished the vast majority of the replanting.

On July 18, 1973, Governor Tom McCall dedicated the acreage affected by the Tillamook Burn as the Tillamook State Forest. The replanted trees began maturing in the 1980s and 90s. The first commercial harvest of the lands was conducted in 1983 and logging continues to this day.

The Clatsop State Forest includes a small portion of the Tillamook Burn area, and otherwise consists primarily of logged-over land that was tax-foreclosed by the counties starting in the 1930s. Parts of the Clatsop State Forest were subject to the reforestation efforts associated with the Tillamook Burn. Commercial harvesting of mature trees in that forest started in the mid-1950s.

### **III. ARGUMENTS PRO AND CON**

#### **A. Arguments Advanced in Favor of the Measure**

Proponents of Measure 34 contend the following:



management of the Tillamook and Clatsop State Forests is inadequate because

1. The Forest Management Plan leaves most of the land open to logging at some point in the future;
2. The Forest Management Plan does not give adequate consideration to preserving and enhancing recreation, water quality, and fish and wildlife habitat. The forests' indirect economic value from tourism, fishing and recreation exceeds the value of the timber harvest;
3. The Forest Management Plan relies on "structure-based management," which has not been tested on a large scale;
4. Timber harvests from the Tillamook and Clatsop forests have increased in recent years, and this is a threat to the health of the forests; and
5. The timber industry dominates management of the state forests and creates pressure to increase harvests. In addition, forest managers receive direction from within state government to increase harvests in order to stimulate the economy and generate operating funds for state and local governments.

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## City Club of Portland

ent definition of "greatest permanent value" as part of the policy for managing state  
flawed because it does not give adequate weight to conservation of land for drinking  
water, recreation, and fish and wildlife habitat.

34's 50-50 plan for the Tillamook and Clatsop forests will benefit the environment and  
my because

1. Reserving half the forests for restoration of native old-growth forests will preserve and enhance recreation, water quality, and fish and wildlife habitat;
2. Measure 34 requires the creation of well-paid reforestation jobs;
3. The number of jobs expected to be lost by the timber industry as a result of creating the 50-percent reserve is not significant;
4. Creating the 50-percent reserve will encourage recreation and spur new recreation-related jobs;
5. Logging revenues should not significantly change under Measure 34, and the measure provides that school funding will not be affected even if revenues do decrease; and
6. Measure 34 provides that an Independent Restoration Science Team would be selected by the chairs of the biology departments of three state universities to develop a plan for managing the forests. This team would be immune from the political pressures brought to bear on the ODF and the Board of Forestry.

### B. Arguments Advanced Against the Measure

Opponents of Measure 34 contend the following:

management of the Tillamook and Clatsop State Forests is adequate because

1. There is no evidence that the Forest Management Plan fails to protect recreation, drinking water, and fish and wildlife habitat. Recreation activities are thriving. Fish counts in the forests' streams and rivers are increasing;
2. Managing reforested land through selective thinning will result in older forest structures sooner than if the trees are left unmanaged. The Forest Management Plan contemplates managing the forest to have significant stands of older forest structure over time;
3. The Forest Management Plan is the result of a lengthy process involving study of the best scientific methods and compromise among many competing interests; and
4. Harvests have increased in recent years because the trees planted following the Tillamook Burn are becoming mature, not because the managers of the forests are unduly influenced by political pressure to increase harvests.

ent definition of "greatest permanent value" to guide forest management does require,  
er things, maintenance and restoration of aquatic and wildlife habitats, conservation of nat-  
ural resources, and provision of recreation opportunities, as well as promotion of timber harvesting.



34's 50-50 plan will be harmful because

1. A 50-percent set-aside will decrease revenues from logging, which will decrease revenues to the state, schools and coastal counties;
2. Counties in which the forests are located will likely file suit claiming that Measure 34 violates an arrangement between the counties and the state that the Tillamook and Clatsop forests would generate logging revenues to fund schools and county government. Logging is likely to stop altogether while any legal challenges are resolved; and
3. A 50-percent set-aside will cause a loss of family-wage jobs in the timber industry. Measure 34 seeks to encourage recreation-based jobs, which tend to be minimum-wage, not family-wage, jobs.

#### IV. DISCUSSION

The Tillamook Rainforest Coalition, sponsor of Measure 34, expresses concern that (1) the statutory mandate to manage the state's forests to the "greatest permanent value" emphasizes increased logging yields and de-emphasizes preservation, habitat and water quality, and (2) that the state's main forest policy-making agency, the Board of Forestry, is improperly influenced by the timber industry. Measure 34 proposes a new definition for "greatest permanent value" that calls for "balancing" sustainable timber harvest with water quality, habitat conservation and recreation. And, with respect to the Tillamook and Clatsop State Forests, it puts the key decisions regarding allocation of the forests to those purposes under the control of an independent science team.

Your committee's investigation and analysis focused on two questions: (1) Is the current plan for management of the Tillamook and Clatsop State Forests, and of state forests generally, so flawed that it should be abandoned?; (2) If so, then is Measure 34 the right solution? The following discussion addresses these questions.

##### **A. Should the Forest Management Plan as applied in the Tillamook and Clatsop State Forests be abandoned?**

Management of public lands requires the balancing of many diverse interests. The Tillamook and Clatsop State Forests were created with the understanding that the reforested timber would be

***The Tillamook and Clatsop State Forests were created with the understanding that the reforested timber would be harvested and would generate revenues for the counties in which they are located.***



harvested and would generate revenues for the counties in which they are located. At the same time, the proximity of the forests to heavily populated areas means that they are widely used for outdoor recreation, including fishing, hunting, ATV use, camping and hiking. Environmental concerns in recent years have put a focus on protecting habitat for fish and other wildlife, as well as protecting drinking water supplies. The westernmost portions of the Portland metropolitan area rely on these forests' watershed for their water supply.

Proponents of Measure 34 perceive that the current Forest Management Plan does not adequately address environmental, conservation and recreation concerns, and that it significantly undervalues the income currently generated and available in the future from recreational use as compared to revenue from timber sales and related activities. Further, the proponents argue that the Plan does not expressly set aside substantial areas for permanent protection from logging.

Your committee's investigation found that the Forest Management Plan, issued in 2001, is the product of several years of investigation and deliberation. A diverse group of professionals, including foresters and specialists in fish and wildlife habitat, soils, and air and water quality, participated in the development of the Plan. The ODF held public hearings on the Plan. It is a lengthy and detailed document that outlines steps to protect watersheds, to protect wildlife and to encourage recreation, while providing for significant timber harvest. The Plan states that it supports long-term protection of the forests as well as protection of timber jobs and production of revenues for the state and counties.

The ODF states that it selected structure-based management for the Tillamook and Clatsop State Forests because, in their current condition, they are not old-growth forests.<sup>5</sup> In particular, the area of the Tillamook Burn was logged, severely burned, logged for salvage and then densely reforested with a single species of tree, Douglas-fir.

Structure-based management seeks to produce diversity in the forests. It calls for the forest to be thinned, other native tree species introduced and other management activities carried out to a point where, in the coming decades, the forest would include an older, complex forest structure. That complex structure is desirable because it is the most suitable habitat for many endangered wildlife species. The ODF contends that structure-based management will achieve a complex forest structure much more quickly than would simply allowing half the reforested trees to grow without significant management. At the same time, under the Forest Management Plan certain areas will be subject to minimal or no active management either because the terrain is not suitable for logging or to protect rivers, streams and identified nesting areas of endangered birds.

Your committee heard testimony that the management of the Tillamook and Clatsop forests is

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<sup>5</sup> The Forest Management Plan states that structure-based management "is designed to produce and maintain an array of forest stand structures across the landscape in a functional arrangement that provides for the social, economic and environmental benefits called for from these state forest lands ... Structure-based management is designed to emulate many aspects of natural stand development patterns and to produce structural components found in natural stands, but in fewer years." p.S-11.

hampered by an outdated inventory of the timber available for harvest. Governor Ted Kulongoski supports the Forest Management Plan but has called for its continued refinement to take into account, among other things, the up-to-date timber inventory that is expected to be completed soon. In this respect, the Forest Management Plan is dynamic, allowing for mid-course corrections and requiring interim reviews and achievement of particular benchmarks.

Proponents and opponents of Measure 34 made conflicting claims regarding current management policies, including whether the timber industry exercises improper influence over the management of the forests, and the extent to which the Forest Management Plan protects resources such as drinking water and wildlife habitats.

Though it was difficult for your committee to assess the validity of these claims, we did determine that the 2001 Forest Management Plan is the product of considerable deliberation and compromise by forestry experts, and represents a balancing of the various competing interests. Representatives of the timber industry, as well as proponents of environmental interests, had input into the Plan. It should not be discarded so soon after its adoption, but should continue to be reviewed and refined as conditions and the state of scientific knowledge warrant. Your committee concludes that the proponents of Measure 34 have not proved that the Forest Management Plan presents such a threat to the health of the forests that it should be abandoned.

**B. Does Measure 34 set a better course for management of state forests?**

Proponents of Measure 34 seek to override the Forest Management Plan and to create a new paradigm for managing the forests. This would occur both by changing the definition of "permanent value" in connection with managing all state forests, and by setting aside half of the Tillamook and Clatsop forests for restoration of a "native old growth forest."

Proponents of Measure 34 claim that setting aside a 50-percent reserve in the Tillamook and Clatsop State Forests will not adversely affect the level of timber harvest and the resulting revenues to the state and counties, and will have a positive impact on employment in the area. Opponents disagree, and foresee dire consequences for the economy and funding of schools and state and local government.

Measure 34 does contain provisions to protect funding of schools and to fund the new management plan that it would mandate. It anticipates that the funds neces-

***Proponents of Measure 34 claim that setting aside a 50-percent reserve in the Tillamook and Clatsop State Forests will not adversely affect the level of timber harvest and the resulting revenues to the state and counties, and will have a positive impact on employment in the area.***

***Opponents [of Measure 34] foresee dire consequences for the economy and funding of schools and state and local government.***

sary to implement the new management plan would be drawn from 10 percent of the revenues from timber sales. It also provides that 5 percent of timber revenues will be directed to the Oregon Common School Fund.<sup>6</sup> This mandate is apparently intended to ensure that "the local public school districts [presumably aimed at Tillamook and Clatsop County schools] shall not receive less funding than the revenue represented in their 2002/03-budget period from timber harvests in the Tillamook and Clatsop State Forests."

In contrast, the state's estimate of the financial impact of the measure does not see the financial impact as neutral. It projects that the timber harvest will drop from its current level, revenues to the state and local governments will decrease, and state expenditures will increase, if Measure 34 passes. Your committee was unable to resolve the competing claims regarding the likely economic effects of Measure 34. The uncertainty regarding the level of harvest in the Tillamook and Clatsop State Forests under the measure lead your committee to conclude that Measure 34 is not a preferable alternative to the current Forest Management Plan.

Measure 34 provides for an Independent Restoration Science Team to develop a plan for managing the Tillamook and Clatsop forests. Proponents contend this team would be immune from the pressures brought by the timber industry on the ODF and the Board of Forestry. Your committee was not convinced that the timber industry has excessive influence on the management of state forests. The lengthy, broad-based and open effort to develop the Forest Management Plan suggests that parties on all sides of the issues are able to have their voices heard. There is no assurance that a team of scientists, which would not be required to operate with the same level of public input, would create a better management plan.

***The state's estimate of the financial impact of the measure does not see the financial impact as neutral.***

Your committee has concerns about the propriety of addressing the scientifically and economically complex subject of forest management in a citizen initiative. In an interview with your committee, Governor Kulongoski asserted his opposition to Measure 34, stating that forest management policy should not be made through the initiative process. While the 50-50 formulation—half of the forests held in reserve, half open to logging—has an initial appeal insofar as it suggests a balanced approach to management, your committee believes that flexibility is critical in managing a forest, and that restricting forest managers with the 50-50 formula is inappropriate.

<sup>6</sup> Oregon Common School Fund is used to support and maintain public education statewide. ORS 327.405

Measure 34 is too vague in certain respects, including a lack of clarity as to how the 50-percent reserve is to be measured. It is undisputed that, under the current management plan, some portions of the Tillamook and Clatsop forests are unavailable for logging because of topography and proximity to rivers and streams. It is unclear whether the 50-percent reserve under Measure 34 would consist of half of the areas otherwise available for logging, or would consist of half of the entire forest area, including portions not suitable for logging.

Your committee, in addition, was not persuaded that the current formulation of "greatest permanent value" as a principle to guide forest management inadequately protects environmental and recreational interests. The existing definition of "permanent value" does require, among other things, maintenance and restoration of aquatic and wildlife habitats, conservation of natural resources, and provision of recreation opportunities, as well as promotion of timber harvesting.<sup>7</sup> The change to that definition mandated by Measure 34 would not appear to provide significantly more protection to the environment.

***Your committee has concerns about the propriety of addressing the scientifically and economically complex subject of forest management in a citizen initiative.***

***Your committee ... was not persuaded that the current formulation of "greatest permanent value" as a principle to guide forest management inadequately protects environmental and recreational interests.***

An important concern regarding Measure 34 is its possible effect on the sharing of timber revenues by the state and the counties of the north coast. As previously noted, the state forests consist of tax-foreclosed land transferred by the counties to the state under a statutory program requiring an allocation of timber proceeds between the state and the transferring counties. Representatives of the counties' governments contend that taking half the Tillamook and Clatsop forests out of active timber production would violate the state's obligation to generate timber revenues for the counties.

A previous threat of this sort led a number of counties to sue the state in the early 1980s. The claim arose from the state's plan to compel Linn County to trade revenue-producing timberland for forestland to be set aside for a park. In a 1987 opinion, the Oregon Supreme Court held that the state violated the statutory revenue-sharing arrangement because Linn County had a protected, recognizable interest in the agreement that was violated when the state conveyed away the forestland.<sup>8</sup> It is possible that the 50-percent set-aside under Measure 34 will be viewed as a similarly unlawful violation of the revenue-sharing arrangement.

<sup>7</sup> ORS 530.050, OAR 629-035-001 0, OAR 629-035-0020

<sup>8</sup> *Tillamook County v. State Board of Forestry*, 302 Or 404 (1987)

To date, county commissions in Tillamook, Clatsop, Lincoln, Deschutes, Linn, Coos and Douglas counties have announced their opposition to Measure 34. If the affected counties pursue a legal challenge to Measure 34 as an unlawful change in the revenue sharing arrangement, logging could stop altogether for a period of years while the courts resolve the issue. Your committee concludes that the possible benefits to the environment and recreation under Measure 34 are outweighed by the risk of disruptive litigation.

Because of these concerns about the uncertain impact of the 50-50 plan, your committee concludes that Measure 34 is not a better alternative to current forest management policies.

## V. CONCLUSION

Your committee concludes that the proponents of Measure 34 have failed to show that the current Forest Management Plan and the current definition of "permanent value" represent such a threat to the long-term health of the forests that they should be abandoned. Your committee found insufficient evidence that the 50-50 plan for the Tillamook and Clatsop State Forests is preferable to the policy choices of the state foresters as reflected in the current Forest Management Plan.

## VI. RECOMMENDATION

**Your committee recommends a NO vote on Measure 34.**

Respectfully submitted,

Tim Carman  
John Doussard  
Kerry Forell  
Bonnie Gee Yosick  
Leslie S. Johnson  
Ellen Price  
Bryan Rhoads  
Lori Irish Bauman, *chair*

Denise Bauman, *research adviser*  
Wade Fickler, *research director*

## VII.APPENDICES

### Witnesses

Mari Anne Gest,Campaign Director,Oregonians for a Balanced Tillamook  
David E.Ivanoff,Vice President-Resources, Hampton Resources, Inc.  
Tim Josi,Tillamook County Commissioner  
Governor Ted Kulongoski,State of Oregon  
Mark W. Labhart, District Forester,Tillamook District,Oregon Department of Forestry  
Doug Maguire,Silviculture Specialist, Forest Science Department, Oregon State University  
Ivan Maluski,Volunteer Coordinator,Sierra Club, Oregon Chapter  
Hans D. Radtke, Natural Resource Economist  
Guido Rahr, President,The Wild Salmon Center  
Senator Charlie Ringo, State of Oregon  
Tom Savage, District Forester, Astoria District,Oregon Department of Forestry  
Ray Wilkeson, Legislative Director,Oregon Forest Industries Council

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# 2004 Ballot Measure Report Measure 38

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## SAFETY ZONE

### State of Oregon Ballot Measure 38:

ABOLISHES sAIF; sTATE MusT REINsuRE, sATisFy sAiF's OBLIGATIOns;  
DEDICATEs PROCEEDs, POTENTIAl suRPLus TO PuBLIC PuRPOSEs

your committee finds that sAIF performs a valuable service to Oregon's businesses and the benefits of retaining sAIF far outweigh any potential benefit from abolishing it.

your committee's analysis of the arguments for and against Measure 38 show that sAIF is not and will not become a monopoly under Oregon's three-way system for workers' compensation insurance. However, if Measure 38 were to pass, access to voluntary insurance for Oregon's small businesses would be at risk and those companies would face higher premiums if forced into the assigned risk pool. your committee found no evidence that confirms premiums would decrease if sAIF is abolished, while some evidence does suggest premiums could increase. With respect to insurance underwriting policies, your committee finds sAIF to be operating consistently with the mission established by the Legislature. sAIF's financial reserves are at a prudent level. should sAIF be abolished, ownership of any excess reserves would be in dispute.

your committee recognizes that sAIF is under investigation and faces many ethical and legal challenges. We believe a complete and thorough investigation by the Governor is warranted. However, your committee concludes that the decision to vote "yes" or "no" on Measure 38 should not rest on the widely publicized concerns regarding sAIF's management practices.

**Your committee recommends a NO vote on Measure 38.**

*City Club members voted on October 15, 2004 to adopt the contents and recommendation of this report as the Club's official position. City Club recommends a NO vote on Ballot Measure 38.*



## I. INTRODUCTION

Ballot Measure 38 will appear on the ballot as follows:

### **ABOLISHES SAIF; STATE MUST REINSURE, SATISFY SAIF'S OBLIGATIONS, DEDICATES PROCEEDS, POTENTIAL SURPLUS TO PUBLIC PURPOSES**

#### **Result of "Yes" Vote:**

"yes" vote abolishes sAiF; state must reinsure, satisfy sAiF's current obligations (including pending policyholder claims against sAiF); dedicates proceeds, potential surplus to specified public purpose.

#### **Result of "No" Vote:**

"No" vote retains law authorizing sAiF, a public corporation, to sell and administer workers compensation insurance and to administer an accident fund for that purpose.

#### **Summary:**

state Accident insurance Fund (sAiF) is a public corporation selling, administering workers compensation insurance, and administering accident fund for the purpose. Measure abolishes sAiF. Requires state to assume sAiF's authority over accident fund; reinsure fund; satisfy sAiF's obligations under its existing policies; use fifty percent of any excess surplus (meaning any funds exceeding reserves and surplus necessary to satisfy future liabilities) to satisfy policyholder claims in litigation before October 2003; transfer forty percent of any excess surplus to new fund; sell sAiF's assets; transfer proceeds to same fund; and reinsure, otherwise resolve sAiF's remaining liabilities. Dedicates new fund to supporting schools, local law enforcement; providing medications to seniors, medically needy; promoting job growth. Requires certain reports to legislature regarding rates for insurance premiums. Other provisions.

#### **Estimate of Financial Impact:**

The measure would reduce state revenue by approximately \$405 million per year and would reduce state expenditures by approximately \$301 million per year due to the elimination of sAiF.

The measure would require additional state government expenditures of \$1.8 million to \$5.5 million per year on a recurring basis with an additional one-time expenditure of \$2.2 billion to \$2.4 billion.

There will be a one time increase of state revenues of \$32.6 million from sale of real property.

The measure would require local government expenditures of \$2.6 million to \$10.5 million per year on a recurring basis.

There is no financial effect on local government revenues.

*(The language of the caption, question, and summary was certified by the Oregon Secretary of State.)*

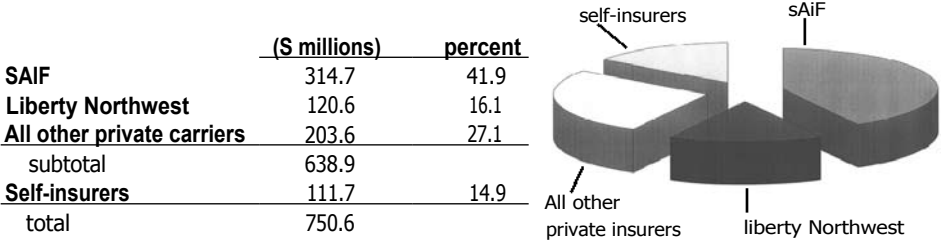
Ballot measure 38 was placed on the November 2004 ballot by initiative petition. the effort to qualify the initiative for the ballot was led by Oregonians for Accountability, a political action committee financed primarily by liberty Northwest insurance, sAiF's chief competitor.

City Club created a committee of nine Club members to analyze measure 38 and issue a voting recommendation to Club members and other voters. Committee members were screened to ensure that no member had an economic or personal interest in the outcome of the study or had taken a public position on the subject of the measure. your committee conducted its research between August 10 and september 20, and interviewed more than a dozen proponents, opponents and others with relevant expertise. your committee also reviewed numerous articles, reports and other documents related to the topic.

## II. BACKGROUND

Workers' compensation insurance pays for medical care and physical rehabilitation of injured workers and helps to replace lost wages while injured workers are unable to work. state law, which varies significantly state to state, governs the benefits paid and other compensation provisions. two corporations control more than half of Oregon's workers' compensation insurance market: one is a quasi-governmental agency (sAiF), the other, a private corporation (liberty Northwest). these two carriers provided coverage for 58 percent of the Oregon market in 2003. 2 the chart below shows the total division of Oregon's market share in 2003.

**Workers' Compensation Market Share as Percentage of Direct Premium Earned \*\***



\*\*Includes assigned risk business.

Workers' Compensation Market Characteristics Report, Oregon Department of Consumer and Business Services [www.cbs.state.or.us/jmd/wc\\_ins.html](http://www.cbs.state.or.us/jmd/wc_ins.html)

<sup>1</sup> insurance information institute, [www.iii.org](http://www.iii.org)

<sup>2</sup> DCBs Questions & Answers about Workers' Compensation, sAiF and Ballot measure 38

Oregon's Workers' Compensation Division is housed in the Department of Consumer and Business services. The mission of DCBs is "to protect and serve Oregon's consumers and workers while supporting a positive business climate in the state."

DCBs administers state laws and rules governing a wide variety of activities affecting consumers, workers, business and economic growth in the state of Oregon. In addition to administering Oregon's Workers' Compensation insurance Division, DCBs also administers rules involving occupational health and safety, real estate appraisal activity, building codes, securities markets and many other areas of operation.

### About SAIF

Industrial accident insurance in Oregon began with the Oregon's Workers' Compensation Law of 1913, by which the Legislature appropriated \$50,000 for the industrial Accident Fund. The law was changed in 1965 with the advent of the state Compensation Department and the Workers' Compensation Board, as well as the introduction of private insurers to the marketplace. The 1965 legislation created a system that allows employers the following three options for workers' compensation insurance: (1) purchase insurance from the state of Oregon; (2) purchase insurance from a private insurer; or (3) become a self-insured employer.

In 1979, the Legislature created sAiF (state Accident insurance Fund) as an independent public corporation. It was created to conduct "workers' compensation insurance business formerly transacted by the state industrial Accident Commission." sAiF is an "insurance company" that operates similarly to a private insurance carrier. It owns real and personal property, employs a staff, litigates, contracts and administers the industrial Accident Fund.<sup>4</sup> sAiF is governed by a five-member board of directors appointed by the Governor and confirmed by the senate.

The industrial Accident fund is the heart of sAiF. It is the repository for the employer-paid premiums and the revenue source for paying the expenses of the corporation. The investments of the fund are managed by the state Treasurer. sAiF is not supported by tax dollars. Its only income is generated by premiums paid by customers and investment returns on the funds set aside to pay benefits to injured workers.

### About Liberty Northwest Insurance Corporation

In February 1983, Liberty Northwest insurance Corporation was established by a group of former sAiF executives with a \$55 million investment from Boston-based Liberty Mutual Group. As an independent operating company within the Liberty Mutual Group, Liberty Northwest is licensed in Alaska, Idaho, Montana, Oregon and Washington. Liberty Northwest has the option of offering

<sup>3</sup> ORs 656.751 (1)

<sup>4</sup> Memo from then Attorney General Dave Frohnmayer to Representative Al Riebel, January 26, 1982

insurance and related services in all other states through related companies in the Liberty Mutual insurance Group.

in its first year of operation, Liberty Northwest controlled less than 1 percent of the Oregon workers' compensation market. Liberty Northwest has grown from the four employees who founded it to more than 950, most of whom are in Oregon. in 2003, Liberty Northwest held a 16.1 percent market share in Oregon. Today it is the largest private writer of workers' compensation in Idaho, Montana and Oregon .5

## **Setting the Stage for Measure 38**

in 1990, the Legislature enacted the "Mahonia Hall Reforms," a series of legislative actions that provided clearer definitions of compensable claims and focused attention on accident prevention in the workplace. The reforms instilled greater certainty within the workers' compensation system and, in turn, reduced the number and cost of individual claims. Workers' compensation insurance rates have declined or remained stable in each year since 1990.<sup>6</sup>

From 1991-2003, various bills were introduced in the Oregon Legislature that would have amended sAiF's operations. From 1994-2003, a number of bills would have required the sale of sAiF. Often these bills saw no committee action. However, in 2001, a bill which would have forced sAiF to contribute funds to the state's "rainy day fund" in lieu of paying policyholder dividends was withdrawn before the final House vote.

in 1997, attorney and lobbyist John DiLorenzo, Chuck sides and former National Federation of independent Business state Director Joe Gilliam created Oregonians for a sound Economic Policy, a nonprofit that would investigate possible misconduct by sAiF. The Oregonian recently reported that Liberty Northwest has acknowledged extensive funding ties to OsEP, having donated \$785,000 over the past six years.

Questions about sAiF's operations surfaced when attorney DiLorenzo sued sAiF on behalf of OsEP on the grounds that it unfairly limited dividends paid to policyholders. The plaintiffs lost at summary judgment, but the case is now under appeal. During the third special session of the 2002 Legislature, a proposal, while ultimately not introduced as legislation, would have required sAiF to offer \$125 million to settle the outstanding suit. Language in Measure 38, which DiLorenzo's law firm helped draft, would direct 50 percent of sAiF's "excess" reserves to satisfy this legal claim.

During the 2003 regular session, the same idea was introduced as senate Bill 649, but received no committee action. A number of bills were introduced in the House that would have (a) required sAiF to be sold; (b) required sAiF to be mutualized; and (c) removed sAiF's ability to manage existing claims.<sup>7</sup> sAiF officials contend that Liberty Northwest was the driving force behind the intro-

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<sup>5</sup> [www.libertynorthwest.com/about/index.asp](http://www.libertynorthwest.com/about/index.asp)

<sup>6</sup> DCBs Questions & Answers about Workers' Compensation, sAiF and Ballot Measure 38

duction of many of these bills.

in the midst of legal proceeding, OsEP requested records from sAiF, invoking state law that provides that "[t]he records of the state Accident insurance Fund Corporation, excepting employer account records and claimant files, shall be open to public inspection."<sup>7</sup> sAiF produced volumes of information, but declined to disclose all of the records requested, claiming additional exceptions contained in the Public Records Law.<sup>8</sup> in addition, House Bill 3093, which was introduced in the 2003 regular session, would have eliminated the applicability of the Public Records Act to sAiF and prevented the supreme Court review of the pending case.<sup>10</sup>

The documents that were turned over revealed underreported consulting and lobbying fees and allegations that sAiF employees were directed to withhold certain records. OsEP continued its pursuit of the records that were withheld. in December 2003, sAiF director Katherine Keene resigned.

in August 2004, Marion County Circuit Court Judge Paul Lipscomb found sAiF in contempt for not releasing all of the records required by law and issued a \$2 million fine. sAiF attorneys subsequently admitted that former director Keene had instructed an assistant to destroy meeting minutes from an executive session. sAiF officials have said they are committed to complying with Judge Lipscomb's order and will present a plan for finding all remaining documents covered by the order.

Following Keene's resignation, Governor Ted Kulongoski issued a letter to sAiF stating major concerns with the organization. since then, he ordered a top-to-bottom review and appointed Brenda Rocklin to lead sAiF through this process. Rocklin commissioned state archives employees to search for public documents and, more recently, sAiF was cleared of an ethics accusation for underreporting lobbying payments. still, some charges against sAiF remain. The contempt of court case and a widening federal and state criminal investigation of the destroyed documents are active.

in July 2004, Measure 38 qualified for the November 2 ballot. Liberty Northwest sponsored the measure for the stated intention of creating a "fair, open and competitive workers' compensation market to protect [Oregon businesses] and their employees with the best [workers compensation] coverage options."

### III. ARGUMENTS PRO AND CON

<sup>7</sup> These bills also received no committee action.

<sup>8</sup> ORs 656.702(1)

<sup>9</sup> ORs 192.410 to 192.505

<sup>10</sup> While these provisions passed the senate, they were later removed in conference committee.

The following arguments for and against Measure 38 are those of the proponents and opponents of the measure.

## Arguments Advanced in Favor of the Measure:

- Measure 38 would end sAiF's dominance and encourage more competition in the market-over insurance rates and improved service would result.
- abandoned its mission. Previously an insurer of last resort, sAiF acts like a private but with special privileges accorded to government agencies.
- Measure 38 would free excess monetary reserves to fund the Oregon Priorities Fund.<sup>11</sup>
- sAiF rates unethically and uses poor management practices. Measure 38 would end the attracts and bad decisions that have been exposed in the media in recent months.
- sAiF's annual rate of claims is unacceptably high.

## Arguments Advanced Against the Measure:

- sAiF's customers are satisfied. Why abolish sAiF when it works well for its customers?
- sAiF's workers' compensation system is the envy of neighboring states. its low rates and relative ease help to sell Oregon as a place to do business.
- Private rates will increase if sAiF is abolished.
- sAiF insures high-risk companies and occupations that private insurance companies will not insure.
- sAiF insures small businesses that are not financially attractive to private carriers.

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<sup>11</sup> The Oregon Priorities Fund is a creation of Ballot Measure 38. if funded, it would use potential surplus reserves from the liquidation of sAiF to support specific public services identified in the language of the measure.

The workers' compensation insurance system should not be a profit-making industry.

sAiF's monetary reserves are prudent. Actuaries have reviewed sAiF's reserves and concluded they are within a reasonable range.

sAiF's monetary reserves belong to policyholders. The money cannot be used to finance the Oregon Priorities Fund.

sAiF is improving its management practices.

sAiF has followed its mission as determined by the Legislature: to provide low-cost workers' compensation insurance to Oregon businesses.

## IV. DISCUSSION

### What Problem is Measure 38 Trying to Solve?

Proponents of Ballot Measure 38 argue that sAiF will become a monopoly because private carriers aren't allowed to compete on a level playing field. As sAiF's dominance increases, the quality of service from sAiF will decline, and in the long run, Oregon businesses will be poorly served. Proponents told your committee that the abolition of sAiF would attract more carriers to the marketplace, increase competition, and lead to lower rates and improved service. They point to recent and highly publicized management problems to allege that sAiF operates unethically. They also claim that sAiF has "lost its mission" and treats workers poorly, by refusing to insure new businesses and by maintaining a higher rate of denying claims than private insurers.

Proponents believe that Measure 38 addresses all of these problems by abolishing sAiF. According to the proponents, if sAiF is liquidated or sold, its reserve and surplus funds, which proponents believe to be in excess of amounts needed, would be released to policyholders and the Oregon Priorities Fund.

### Your Committee's Analysis

your committee sought data to evaluate proponents' arguments and determine whether Oregonians would receive a net benefit from the passage of measure 38. We interviewed witnesses, studied documents and investigated workers' compensation rates and laws in other states. Our criteria focused on how measure 38 would affect the insurance market, rates, workers' satisfaction and the state budget. In some cases, the data proved inconclusive at best. However, we found enough evidence to analyze the major arguments outlined below.

## **Will SAIF Become a Monopoly?**

sAIF's market share has varied over the years as economic conditions have varied. The Department of Consumer and Business Services describes the market forces as follows:

*Over the past 25 years, overall insurance market trends have driven SAIF and competing private insurance companies' market shares up and down. During "hard market" cycles, private companies are generally less willing or able to provide coverage, thereby increasing SAIF's market share. In "soft market" cycles, private insurance companies tend to lower their premiums and expand their business, while SAIF's market share tends to decrease. Nationally and in Oregon, workers' compensation insurance has been going through a "hard market" cycle for the past several years.*

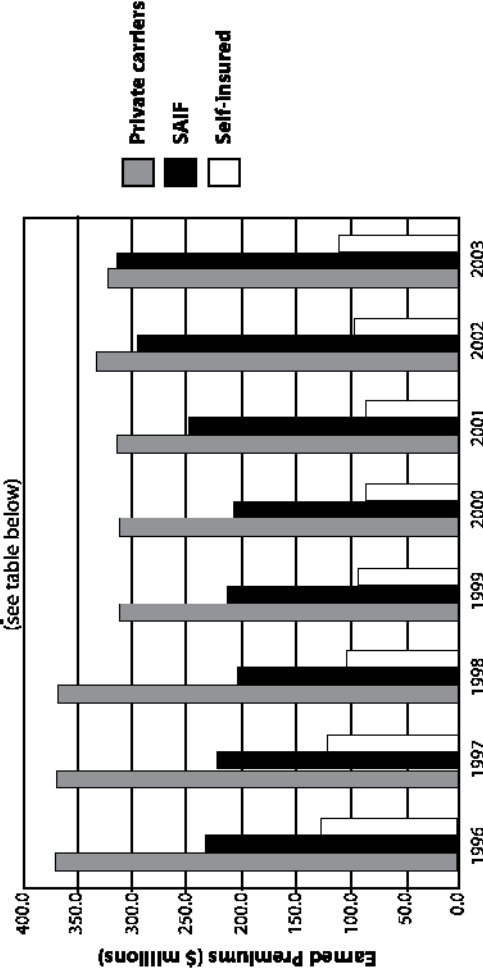
In 2003, 187 private insurance companies were actively providing workers' compensation coverage to Oregon employers. Although many of these companies provide insurance to only a few Oregon businesses, 39 private insurance companies earned more than \$1 million from workers' compensation premiums in Oregon in 2003. With a 16.1 percent market share in 2003,<sup>12</sup> Liberty Mutual holds an unusually dominant position among private insurers in the states your committee investigated.

***Thirty-nine private insurance companies earned more than \$1 million from workers' compensation premiums in Oregon in 2003.***

Because sAIF covers only workers who are employed in Oregon, all multi-state businesses



## Workers' Compensation Market Share



## Earned Premiums in \$ Millions

|                         | 1996        | 1997        | 1998        | 1999        | 2000        | 2001        | 2002        | 2003        |
|-------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| <b>Private carriers</b> | \$368.2 51% | \$368.5 52% | \$367.0 54% | \$310.0 51% | \$311.0 51% | \$313.2 48% | \$331.0 46% | \$324.0 43% |
| <b>SAIF</b>             | 233.1 32%   | 223.0 31%   | 203.0 30%   | 211.5 35%   | 208.7 34%   | 248.0 38%   | 295.0 41%   | 314.6 42%   |
| <b>Self-insured</b>     | 126.0 17%   | 121.9 17%   | 104.7 16%   | 90.6 15%    | 86.4 14%    | 86.0 13%    | 97.6 13%    | 111.7 15%   |
| <b>Total</b>            | \$727.3     | \$713.4     | \$674.7     | \$612.1     | \$606.1     | \$647.2     | \$723.6     | \$750.3     |

Source: Department of Consumer and Business Services

must choose a private carrier or self-insure. in addition, one insurance broker interviewed by your committee testified that his brokerage seeks quotes for their customers from sAIF and from private carriers. Often, he says, the private carriers win the contract.

*SAIF does not have a monopoly on the market now, and your committee found little evidence to support the claim that a monopoly would develop under Oregon's current three-way system.*

### **how Would Abolishing SAIF Affect the Number and Diversity of Carriers in Oregon?**

your committee compared Oregon with a sampling of other states to assess whether the enactment of measure 38 would diversify carrier choices in Oregon. We also attempted to evaluate the impact of a predominantly private market on employers. Our work was somewhat inconclusive because laws governing workers' compensation insurance differ greatly from state to state.

your committee found that 26 states, or about half, have state funds providing workers' compensation insurance. most of these states have three-way systems like Oregon's. in nearly all states with state funds, the state-operated or state-supported carriers dominate their respective markets. the number of private carriers writing workers' compensation insurance in any given state often exceeds 100, with occasionally over 250 carriers, regardless of the presence or absence of any version of state insurance.

your committee believes that large employers who are well served in the current system will likely continue to be well served if measure 38 passes. the more ominous question is whether Oregon's small and difficult -to-insure businesses would be able to find affordable and adequate coverage if sAIF were abolished.

As of June 2004, 88,465 Oregon employers were covered by an external workers' compensation policy or were self-insured. Approximately 58,000 of these employers were small businesses paying less than \$2,500 in annual workers' compensation premiums. sAIF insures 27,500 small employers (47.4 percent) .

Witnesses told your committee that writing policies for small businesses is generally not lucrative for private carriers. employers who are denied coverage in the voluntary market are entitled to buy coverage through an "assigned risk pool" administered by the National Council on Compensation insurance. the assigned risk pool guarantees that employers will have access to insurance, but it comes at a cost. insurance premiums are higher for employers in the assigned risk pool. Approximately 10,000 Oregon small businesses are in the assigned risk pool.

your committee is concerned that,if measure 38 passes, private carriers would not voluntarily provide insurance for Oregon's small businesses if measure 38 passes. your committee was persuad-

ed by witness testimony from insurance brokers and the National Federation of independent Businesses and Associated general Contractors that small businesses would be thrown into the more expensive assigned risk pool if sAiF were abolished. A common sentiment among business people contacted by your committee was that "normally, i would want business to be conducted in the private sector<sup>13</sup> as much as possible, but i don't support the abolition of sAiF. it performs a valuable service."

*Your committee concludes that while the number of private companies is likely to remain at a healthy level, access to the voluntary insurance market for Oregon's small businesses would be jeopardized if Measure 38 passes.*

### **Would the Abolition of SAIF Lead to Lower Rates?**

the National Council on Compensation insurance is the rating bureau for workers' compensation insurance in 39 member states, plus the District of Columbia. NCCI develops "pure premium" rates, subject to approval by DCBs. Pure premium is the amount of premium necessary to pay expected losses. in calculating the pure premium rate, NCCI looks at the combined claim costs of sAiF and private insurance companies and performs the necessary actuarial calculation under the supervision of DCBs. the pure premium reflects NCCI's prediction of the actual cost of all workplace injury and illness claims in Oregon.

under Oregon's competitive system, each insurer develops an expense loading factor, subject to DCBs approval, to cover operating expenses, taxes, profit and contingencies. this factor is multiplied by the pure premium rate to arrive at the rate to be applied to the employer's payroll. the premium differences between insurers are caused mainly by the individual insurer's expense loading.<sup>14</sup> Actual rates paid by individual employers may also vary based on their losses and other factors.

since 1990, sAiF's average expense loading factor has been lower than the average expense loading factors of private insurance companies. in 2003, the average expense loading factors for the top 30<sup>15</sup> private workers' compensation insurers in Oregon were 20.5 percent higher than that of sAiF. Consequently, the fiscal impact statement that will appear in the voters' pamphlet estimates that state and local governments' costs will increase due to higher workers' compensation rates if measure 38 passes.

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13 to the surprise of fiscal conservatives on your committee who typically believe that the absence of government providers competing with private enterprise will lead to more competition, lower prices and more participants in the market, our findings were the opposite. We found that in the workers' compensation insurance market, states with only private carriers did not offer consistently lower rates. in fact, rates were often higher and the number of carriers in the market was not dramatically different than states with public-private systems.

14 Oregon Workers' Compensation Premium rate ranking 2002,

[www.cbs.state.or.us/jmd/rasums/2083/02web/02\\_2083.pdf](http://www.cbs.state.or.us/jmd/rasums/2083/02web/02_2083.pdf)

your committee compared rates among Oregon and other states. Proponents point to Michigan and Nevada as positive examples where both states eliminated their state-owned funds and experienced a decline in rates. However, your committee found such comparisons unconvincing for several reasons: (a) Michigan's fund was purchased by Blue Cross/Blue Shield, not abolished; (b) Nevada's state fund was insolvent, whereas Oregon's is not; (c) neither Michigan nor Nevada resemble Oregon in population or employment patterns, which suggests that they would differ substantially from Oregon in overall business and market conditions, thereby affecting the workers' compensation market.

Your committee examined states that share Oregon's population and employment patterns, such as Colorado and Oklahoma. These states also offer alternative models for providing workers' compensation insurance, but have different definitions for self-insured categories, different roles for state insurance and different organizational structures to administer worker's compensation insurance. Therefore, the conclusions your committee could draw were limited.

Comparisons with other states illustrated the following:

According to recent data (2002), Oregon enjoys low workers' compensation insurance rates, 5th among all 50 states and the District of Columbia. For the last 10 years, it has ranked 11th and 35th. 16

Among states with comparable populations (Connecticut, Colorado and Oklahoma) Oregon's is the lowest. 17

Connecticut and Mississippi, with populations similar to Oregon, have only private carriers' workers' compensation coverage. Oregon's system would be similar if Measure 38 passes. Connecticut's rates are 12th highest in the nation, 23 states above Oregon in cost ranking. Mississippi is slightly more expensive than Oregon. 18

States with three-way carrier systems and comparable populations such as Kentucky, Colorado and Oklahoma, ranked 15th, 18th and 20th respectively. 19

Oregon ranks behind only Utah and Arizona for the lowest workers' compensation premiums in the manufacturing sector. 20

Your committee also heard from an NCCI executive that Oregon's long history of stable premiums was highly unusual among his member entities.

16 [www.cbs.state.or.us/imd/rasums/2083/02web/02\\_2083.pdf](http://www.cbs.state.or.us/imd/rasums/2083/02web/02_2083.pdf)

17 *ibid.*

18 *ibid.*

19 *ibid.*

20 Actuarial technologies solutions, a workers' compensation rating bureau for manufacturers

*Your committee found some evidence that workers' compensation rates could increase if Measure 38 passes, and no evidence that rates would decline.*

**Should Recently Publicized Problems with SAIF's Management be grounds for Abolishing SAIF?**

Proponents of Measure 38 allege that sAiF's legal and ethical challenges and its disputed management practices are reasons to abolish sAiF. Both proponents and opponents agreed that sAiF's management has made serious mistakes. However, your committee was persuaded that sAiF plays an important role in Oregon's workers' compensation industry and that a decision to abolish sAiF should not rest on the mistakes of prior management. your committee has confidence in Governor Kulongoski's decision to appoint Rocklin as sAiF's interim director. she has earned high marks for her efforts to fulfill Judge Lipscomb's order to produce public records previously withheld.

*Your committee concludes that the decision to vote "Yes" or "No" on Measure 38 should not rest on the publicized concerns about SAIF's management and business practices.*

**has SAIF "lost Its Mission?"**

initially, sAiF's predecessor, the state industrial Accident Commission, was the "insurer of last resort" and was required to provide workers' compensation insurance to any employer. The Legislature changed sAiF's mission in 1965 to the following: "The mission of sAiF Corporation is to make insurance available to as many Oregon employers as inexpensively as may be consistent with the overall integrity of the industrial Accident Fund ... and sound principles of insurance."21 sAiF's mission allows it to determine which employers it will cover. Opponents of Measure 38 point to sAiF's low rates and market share to say that sAiF is doing exactly what the Legislature intended.

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sound principles of insur-**

*Your committee concludes that, with respect to insurance underwriting policies, SAIF is operating consistently with its mandate from the Legislature.*

**Does SAIF Treat Workers Unfairly by Denying More**

<sup>21</sup> ORs 656.752

**Claims than Private Carriers?**

DCBs documents state that, historically, sAiF has denied claims at a higher rate than private insurers and self-insured employers. In 2003, sAiF denied 19.5 percent of all worker injury claims, while private insurers rejected only 14.6 percent of claims on average.

Bob Shiprack, representing the Building Trades Council and speaking in opposition to Measure 38, testified that while workers are safer and there is much greater certainty in resolving claims since the 1990 Mahonia Hall reforms, sAiF's high denial rate reflects a problem with its "attitude toward workers." Similarly, an attorney who represents workers whose claims have been denied said that sAiF is more difficult to work with than are private carriers.

On the other hand, Bradley Witt, secretary of the AFL-CIO, testifying before the Senate General Government Committee in June 2004 said that efforts to privatize Oregon's workers' compensation system would "also eliminate the very carrier who sets the benchmarks in our state for claims acceptance. With regard to disabling claims, which constitute some of the more serious and oftentimes complicated cases, sAiF accepts these claims twice as quickly as do its private sector counterparts."

DCBs reports that while sAiF historically has a higher rate of denying claims than the rest of the industry, fewer denials by sAiF are appealed. When they are appealed, sAiF's denials are affirmed at a slightly higher rate than its counterparts. 22

*Your committee found that SAIF's denial rate for claims is higher than private insurers. Witnesses suggest this reflects SAIF's attitude toward workers. SAIF officials maintain they are acting responsibly to catch suspicious claims. Your committee could not resolve this issue in the time allowed for this study, but, nonetheless, your committee concludes that SAIF's denial rate is not grounds for abolishing it.*

**Does SAIF Have Excess Funds, and if SAIF is Abolished, are Those Funds Available to Finance the New State Fund Proposed by Measure 38?**

Proponents of Measure 38 argue that sAiF has reserve funds in excess of the amount necessary to satisfy future claims and protect the company. Ballot Measure 38 dedicates the net proceeds from abolishing sAiF to "specified public purposes," according to the ballot measure summary. Measure 38 provides that 50 percent of any excess surplus is to be used to satisfy policyholder claims in litigation before October 2003, and 40 percent is to go to a new state fund dedicated to supporting schools, local law enforcement, and other public needs. Proponents estimate that the

new fund would contain \$346 to \$732 million depending on the amount set aside to satisfy poli-

cyholder claims. 23

your committee found considerable disagreement among witnesses about whether there would be net proceeds from abolishing sAiF. some think that the costs of reinsurance and liquidation or sale of sAiF would exceed the reserves. some disagree about whether the net proceeds that might exist would be available to the state. sAiF's policyholders argue that any excess surplus that may exist should be returned to them. The fiscal impact statement included in the ballot title, as prepared by the secretary of state's office, does not answer this question .24

Measure 38 sets aside 50 percent of any excess surplus to satisfy policyholder claims in litigation before October 2003.in fact, only one pending lawsuit was filed before October 2003. That is, Artisan Laboratories, inc.et al v. sAiF, a proposed class action suit brought on behalf of all employers insured by sAiF from January 1, 1990 to the present. The suit was filed by John DiLorenzo and funded by Oregonians for sound Economic Policy. The suit asks that the court return a portion of any excess surplus accumulated by sAiF to its policyholders.

All insurance companies are required to maintain reserves sufficient to pay their claims. The Legislature has charged sAiF with being the trustee for the industrial Accident Fund. The state's insurance Division retained an independent actuarial firm to audit the reserves. Their report, dated June 2004, did not recommend that sAiF reduce its reserves and said that sAiF's reserves were within an acceptable range.

if Measure 38 passes, the state would be required to purchase reinsurance to cover future liabilities for workers that were previously covered by sAiF. The cost of this insurance would determine whether the reserves were adequate or excessive. The state estimates the cost will be \$2 billion-\$2.2 billion. your committee relies on the opinion of the independent audit.

There are legal questions about whether sAiF has excess resources and, if they indeed exist, whether they would be available to fund the Oregon Priorities Fund as stipulated in Measure 38. History may tell us something here.

in 1980, the Oregon Legislature attempted to apply some of sAiF's funds to other state needs. sAiF's policyholders sued the state and won, and the state was required to repay all funds with interest. since then, the law has been changed. The new law seems to suggest that the Legislature

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23 The Measure is unclear about the disposition of 10 percent of the excess that may result from abolishing sAiF. Presumably, 10 percent is held for contingencies until all costs have been paid and liabilities addressed. At that time, any remaining excess would be paid to the Oregon Priorities Fund.

24 The transfer of sAiF's surplus to a new state fund is not shown as a revenue source because transfers from one state account to another are not considered new revenue under the administrative rules governing the preparation of fiscal impact statements.

25 ORs 656.634

could direct the disposition of sAIF's surplus leading proponents to argue that Measure 38 can legally direct excess funds to state purposes. <sup>25</sup> sAIF's policyholders disagree. They argue that any surplus funds in sAIF belong to them and should be paid as dividends.

*Your committee concludes that, based on the judgment of an independent auditor, SAIF's reserves are prudent, and that if excess reserves surface later, the rightful owner will be determined in court.*

## V. SUMMARY CONCLUSIONS

your committee analyzed the arguments of the proponents and opponents of Measure 38 and concluded the following:

not become a monopoly if Measure 38 is defeated.

o voluntary insurance for Oregon's small businesses would be at risk if Measure 38

re 38 is defeated, the number of private carriers would likely remain at healthy levels.

compensation premiums would not decrease, and could even increase, if Measure 38 passes.

pect to insurance underwriting policies, sAIF is operating consistently within its legisla-  
ate.

erves are prudent, and ownership of excess reserves is in dispute.

sion to vote "yes" or "no" on Measure 38 should not rest on the widely publicized con-  
ut sAIF's management practices.

in summary, your committee finds that the proponents' arguments to abolish sAIF were not per-  
suasive. your committee believes sAIF performs a valuable service to Oregon's businesses, small and  
large, and that the benefits of retaining sAIF far outweigh any potential benefit from abolishing it.



your committee recognizes that sAIF is currently under investigation and faces many ethical and legal challenges, but concludes that Measure 38 is not the solution to sAIF's management problems. A complete and thorough investigation by the Governor is warranted.

years before Measure 38 qualified for the ballot, Oregonians for sound Economic Policy, a group funded largely by Liberty Northwest, was formed as a "sAIF watchdog organization." Liberty Northwest has since provided most of the financial support for Measure 38, and the measure itself was written by Liberty Northwest's staff and attorneys who share a financial stake in its passage. your committee did not identify any private insurance company operating in Oregon, other than Liberty Northwest, that publicly supports Measure 38. These facts collectively raise questions about whether Measure 38 was intended to serve a public good, or whether the proponents of Measure 38 are using Oregon's initiative system for private gain. your committee believes voters should act cautiously approving any ballot measure when the proponents, financial backers and greatest potential beneficiaries represent an extremely narrow interest, as is the case with Measure 38.

## VI. RECOMMENDATION

**Your committee unanimously recommends a NO vote on Ballot Measure 38.**

Respectfully submitted,

Whitney Bates  
Linda s. Craig  
Robert D. Geary  
Mary Ella Kuster  
Dylan Parkins  
susan Pearce  
Roger F. smith  
Roz Elms sutherland  
Hillary Barbour, *chair*

Tim Hemstreet, *research adviser*  
Wade Fickler, *research director*

### ACKNOWLEDGMENTS

your committee thanks our Research Adviser, Tim Hemstreet, City Club Research Director Wade Fickler and all others who made significant contributions in research and fact finding to help put this report together.

**VII. APPENDICES****uWitnesses**

Jessica Harris Adamson, Government and Legislative Affairs Manager, Associated General Contractors, Oregon-Columbia Chapter

Nik Blosser, Principal, Celilo Group

Brian Boe, Vice President Public Affairs, Liberty Northwest insurance Corporation

Angela Burke Boston, Assistant Commissioner, Product and Producer Regulation, Iowa insurance Division

Peter Burton, senior Division Executive, state Relations National Council on Compensation insurance

Charles Cheek, Legislative Counsel, Office of the Attorney General, state of Oregon

Jim Cross, Broker/Owner, insurance World; secretary-manager, Oregon Loggers Conference and Equipment show

Chris Davie, Government Affairs Coordinator, sAiF

Trey Davis, Chief of staff, Oklahoma Department of Labor

Gene Derfler, retired senate President, state of Oregon

Jim Mahoney, Owner, Valley Contractors supply, inc.

Debbi Hart-Bertone, Oklahoma Board of Property and Casualty

Evol F. Malagon, Attorney at Law, Malagon Moore & Jensen LLP

Peter Miecznikowski, statistical Division, state of Connecticut, Workers Compensation Commission

Richard C. Newlands, insurance Broker, Campbell, Galt & Newlands

Carol O'Bryan, Chief Market Analyst, Colorado Division of insurance

E. Jay Perry, Attorney at Law, Employers Defense Counsel

Louis D. savage, senior Policy Advisor, Oregon state Department of Consumer and Business services

Bob shiprack, Executive secretary, Oregon Building Trades Council

Cory streisinger, Director, Oregon Department of Consumer and Business services

Jim Wildish, President, Wildish sand and Gravel, Wildish Construction Co., Wildish Land Co.

J. L. Wilson, Oregon state Director, National Federation of independent Businesses

Bradley Witt, secretary-Treasurer, Oregon AFL-CIO

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[www.libertynorthwest.com](http://www.libertynorthwest.com)

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