The Tennessee Advisory Commission on Intergovernmental Relations

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MEMORANDUM

TO: Commission Members

FROM: Lynnisse Roehrich-Patrick
Executive Director

DATE: 23 October 2013

SUBJECT: Insurance versus Surety Bonds Legislation

A bill that would change current law to allow local governments to buy insurance as an alternative to individual surety bonds (Senate Bill 624 by Norris) was referred to the Commission for study by the Senate State and Local Government Committee. Current Tennessee law requires various local government officials to execute individual surety bonds in order to hold office. These bonds are used to protect against loss caused by public officials not faithfully performing their official duties. Attachment A, the research article *The Public Officials Bond—A Statutory Obligation Requiring "Faithful Performance," "Fidelity" and Flexibility*, describes those bonds and how they work.

Attachment B summarizes the risk management tools other states require or allow. There are basically five different methods:

- **Surety bond**—a contract between three parties in which one party (the surety company) guarantees to a second party (a city or county) that a third party (the public official) will successfully perform certain obligations. If those obligations are not successfully performed, the surety will pay the governmental entity, up to the bond amount, for any loss as a result of that failure. The public official is responsible for reimbursing the surety.
- **Blanket bond** (or blanket surety bond)—in the public official context, this term refers to coverage for a group of officials or employees of a designated office or political subdivision and allows for several individuals to be covered under one bond, instead of a separate bond for each.
- **Insurance**—a two-party contract that transfers the risk of loss from one party to another in exchange for payment (premium).

- **Self-insurance**—retaining risk by setting aside an amount of money to compensate for potential future loss.
- **Pool** (or group self-insurance)—a group of entities that self-insure by combining their funds. These pools are formed under state-specific laws. Each pool member shares in the risks of all other member entities.

State officials, stakeholders, and industry experts interviewed about Senate Bill 624 have raised questions about the bill's potential implementation. Attachment C summarizes the requirements of the bill, questions raised, and possible ways to address these concerns. As requested at the August Commission meeting, the following individuals have been invited to speak and respond to questions from the Commission.

- **John Evans**, President of Next Generation Underwriters. Mr. Evans has a long history of providing risk management for local governments and is a proponent of Senate Bill 624.
- **Sarah Hiestand**, Senior Counsel, Attorney General's Office. Ms. Hiestand has worked with staff of the Comptroller's office on surety bond issues.
- **Joyce Welborn**, Legislative Auditor, Comptroller of the Treasury. Ms. Welborn was responsible for the surety bonds filed with the Comptroller's Office. Before Public Chapter 315, Acts of 2013, which requires public official bonds to be filed with the county clerk, these bonds were filed with the Comptroller's office.
- **Brian Hoffmeister**, Director of Policy Analysis, Department of Commerce and Insurance.
- **Jack Spann**, President of Spann Insurance. Mr. Spann has extensive experience providing insurance and surety bonds to local governments.
- **Becky Brock**, Director of Member Services, Local Government Insurance Pool.
- **John Calvin**, Director of Underwriting, Tennessee Municipal League Risk Management Pool.