STORAGE NAME: h1761a.in
DATE: April 14, 1999

HOUSE OF REPRESENTATIVES
COMMITTEE ON
INSURANCE
ANALYSIS

BILL #: HB 1761

RELATING TO: Overinsurance

SPONSOR(S): Representative Patterson

COMPANION BILL(S): SB 1092(s)

ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:
(1) INSURANCE YEAS 11 NAYS 0
(2) GOVERNMENT RULES AND REGULATIONS
(3)
(4)
(5)

I. SUMMARY:

Disability insurance is insurance which pays a periodic income to the policyholder in the event the policyholder is unable to return to work due to a disabling accident or illness. The benefits payable under a disability policy are often referred to as "loss-of-time" benefits. Often, an insured will have disability coverage from more than one source. For example, it is possible for an insured to have coverage under a private disability income policy, workers' compensation, employer's liability insurance, union welfare plans, and salary continuance or pension plans. If the insured were to collect loss-of-time benefits from all sources, it is possible that the insured would collect more money than was earned prior to the disabling event. To address this situation, Florida law currently permits insurers to include a coordination of benefits provision in the insurance contract, which provides for a proportionate reduction of benefits payable when the total loss-of-time benefits from all sources exceeds 100 percent of the insured's pre-disability earnings.

This bill would permit insurers to include a provision in disability insurance contracts which enables the insurer, after 90 days of paying the loss-of time benefit, to adjust the loss-of-time benefit payable to an insured when all valid total loss-of-time coverages provided to the insured exceeds a certain percentage (less than 100 percent) of the insured's pre-disability earnings (called the "earnings replacement percentage"). Under the bill, "valid loss-of-time coverage" would include:

- coverage on the insured provided by governmental agencies;
- disability benefits;
- workers' compensation benefits;
- employer's liability benefits;
- benefits provided by labor-management trustee plans, union welfare plans, and salary continuance or pension programs; and
- any other coverage approved by the Insurance Commissioner.

The "earnings replacement percentage would be the greater of 60 percent or the total amount of all loss-of-time benefits from all sources divided by the insured's income at the time of application.

The bill would not have a fiscal impact on state or local government.

Amendments:

On April 13, 1999, the Committee on Insurance adopted two amendments to the bill. See the Amendments section of the analysis for an explanation of the amendments.

II. SUBSTANTIVE ANALYSIS:

A. PRESENT SITUATION:

Disability Insurance

Disability insurance (or "disability income insurance," as it is sometimes called) is insurance which pays a periodic income to the policyholder in the event the policyholder is unable to return to work due to a disabling accident or illness. The benefits payable under a disability policy are often referred to as "loss-of-time" benefits. Disability insurance is considered to be a form of health insurance. See s. 624.603, F.S. Generally, disability insurance coverage is provided through individual and group policies and governmental programs. A short-term disability policy generally pays for a limited number of weeks and a long-term policy will provide benefits on a monthly basis for a longer duration of time. Disability policies generally begin making payments after a specified waiting period has elapsed, and will not pay more than a certain percentage of the policyholder's total income before the disability, or up to a maximum amount.

In order to minimize the opportunity for individuals to profit from the occurrence of a disabling event, insurers provide certain limitations on the benefits provided through a disability policy. Typically, disability policies limit the maximum amount of coverage to 50 - 80 percent of the pretax income of the insured prior to the disabling event.

Coordination of Benefits

Often, an insured will have disability coverage from more than one source. For example, it is possible for an insured to have coverage under a private disability income policy, workers' compensation, employer's liability insurance, union welfare plans, and salary continuance or pension plans. Therefore, if the insured were to collect loss-of-time benefits from all sources, it is possible that the insured would collect more money than was earned prior to the disabling event. To address this situation, the law permits insurers to insert a provision in the insurance contract (called a "Relations of Earnings to Insurance" provision) which provides for a proportionate reduction of benefits payable, or coordination of benefits, subject to the limitation of s. 627.624, F.S.

Section 627.624, F.S., provides for a "Relation of Earnings to Insurance" clause to allow for a reduction in benefits. Generally, if the total monthly amount of loss-of-time benefits promised for the same loss under all valid disability/loss-of-time coverage upon the insured exceeds the monthly earnings of the insured at the time of the disability, the insurer is only liable for such proportionate amount of benefits under the policy as the amount of monthly earnings bears to the total amount of monthly benefits for the same loss under all disability coverages upon the insured at the time of the disability. Under this section, the insurer is also required to refund such part of the premiums paid during the 2 years that exceed the pro rata amount of the premiums for the benefits actually paid, with limitations. Also, this reduction in benefits may only be used in policies that are renewable to at least age 50 or, in the case of a policy issued after age 44, for at least 5 years, whichever results in the higher age.

An example of how this provision operates would be: an individual has two disability policies paying benefits of $300 (insurer A) and $400 (insurer B) per month respectively. However, the individual's pre-disability earnings were only $600 per month. Under this provision, the insurers A and B would proportionately reduce their benefits so that the insured receives a total of $600 in benefits monthly, instead of the $700 that would be payable absent the provision. The calculation would be as follows

> $600 (insured's monthly earnings) divided by $700 (total benefits payable under both policies), which equals 85.714 percent. Then, each company would pay 85.714 percent of their monthly benefit or $257.14 (insurer A) and $342.86 (insurer B), the sum of which equals $600.

Disability/loss-of-time benefits received by an injured employee are not taxable.

Presently, there is no provision in the Florida Statutes that would allow an insurer to reduce a proportionate share of the benefit payable in the event the total amount of disability benefits from all coverages exceed some amount that is less than 100 percent of the insured's prior income.

Workers' Compensation Offsets

Social Security - Under s. 440.15(10), F.S., carriers are authorized to take an offset against workers' compensation benefits to the extent that social security benefits and workers' compensation benefits exceed 80 percent of the employee's pre-injury wage.

Grice - In 1997, the Florida Supreme Court in Escambia County Sheriff's Department v. Grice, 692 So.2d 896 (Fla. 1997), held that an employee's workers' compensation benefits, social security benefits, and state disability retirement benefits, when totaled, may not exceed 100 percent of the employee's average weekly wage (AWW). If the total of these benefits exceeds 100 percent of the employee's AWW, the carrier is entitled to an offset against the employee's workers' compensation benefits.

National Association of Insurance Commissioners (NAIC) Model Act

The NAIC has developed model provisions relating to individual accident and sickness policies. See Uniform Individual Accident and Sickness Policy Provision Law, NAIC 180-1, et seq. Within this model law, there are three provisions relating to overinsurance. Two of the provisions relate to medical expense coverage under an accident and sickness policy. The third provision relates to loss-of-time coverage.[1]

B. EFFECT OF PROPOSED CHANGES:

Overinsurance Provision

Insurers would be permitted to include an overinsurance provision in their disability policies which would enable insurers, after benefits are payable for 90 days, to adjust the loss-of-time benefit payable to an insured when the total amount of all "valid loss-of-time benefits" payable to the insured under all coverages exceeds a certain percentage of the insured's prior income, expressed as the "earnings replacement percentage" of the insured's income.

The term, "valid loss-of-time coverage" would mean coverage as approved by the Department of Insurance, which may include:

- coverage on the insured provided by governmental agencies;
- disability benefits;
- workers' compensation benefits;
- employer's liability benefits;

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[1] The NAIC Model Act provides:

Overinsurance: After the loss-of-time benefit of this policy has been payable for ninety (90) days, the benefit will be adjusted, as provided below, if the total amount of unadjusted loss-of-time benefits provided in all valid loss-of-time coverage upon the insured should exceed [insert amount] percent of the insured's earned income; provided, however, that if the information contained in the application discloses that the total amount of loss-of-time benefits under this policy and under all other valid loss-of-time coverage expected to be effective upon the insured in accordance with the application for this policy exceeded [insert amount] percent of the insured's earned income at the time of such application, the higher percentage will be used in place of [insert amount] percent. The adjusted loss-of-time benefit under this policy for any month shall be only such proportion of the loss-of-time benefit otherwise payable under this policy as (i) the product of the insured's earned income and [insert amount] percent (or, if higher, the alternative percentage at the end of the first sentence of this provision) bears to (ii) the total amount of loss-of-time benefits payable for such month under this policy and all other valid loss-of-time coverage on the insured (without giving effect to the overinsurance provision in this or any other coverage) less in both (i) and (ii) any amount of loss-of-time benefits payable under other valid loss-of-time coverage which does not contain an overinsurance provision. In making the computation, all benefits and earnings shall be converted to a consistent [insert "weekly" if the loss-of-time benefit of this policy is payable weekly, "monthly" if the benefit is payable monthly, etc.] basis. If the numerator of the foregoing ratio is zero or is negative, no benefit shall be payable under this policy. In no event shall this provision operate to reduce the total combined amount of loss-of-time benefits for such month payable under this policy and all other valid loss-of-time coverage below the less of $300 and the total combined amount of loss-of-time benefits determined without giving effect to any overinsurance provision, or operate to increase the amount of benefits payable under this policy above the amount which would have been paid in the absence of this provision, or take into account or operate to reduce any benefit other than the loss-of-time benefit.

- benefits provided by labor-management trustee plans, union welfare plans, and salary continuance or pension programs; and
- any other coverage approved by the Insurance Commissioner.

The "earnings replacement percentage" would be the greater of either:

- 60 percent of the insured's earned income, or

- the total amount of benefits divided by the insured's earned income at the time of application.

The earnings replacement percentage would have to be shown on the insured's policy schedule. This provision would be applicable to individual disability policies only.

Overinsurance Formula

The overinsurance provision would establish a formula which determines the adjusted loss-of-time benefits payable to an insured. Under the formula, the adjusted loss-of-time benefit (ALOTB) under a policy would be determined by multiplying the unadjusted loss-of time benefit (ULOTB) by a factor determined by multiplying the earnings replacement percent (ERP) by earned income (EI) divided by all unadjusted valid loss-of-time coverages (all ULOTBs).

ALOTB = ULOTB x [(ERP x EI) / All ULOTBs]

Limitations on Overinsurance Provision

Under the overinsurance provision, loss-of-time benefits would not be adjusted for insured's who suffer a "catastrophic disability." A catastrophic disability would be defined to mean a total and permanent loss of speech, loss of hearing in both ears, loss of sight of both eyes, loss of the use of both legs, loss of the use of both arms, or loss of the use of one arm and one leg.

The overinsurance provision would not be permitted to operate to reduce the total combined amount of loss-of-time benefits below an amount that is the lesser of $300 or the total combined amount of loss-of-time benefits determined without considering any overinsurance clause. The provision would also not be permitted to increase the amount of benefits payable under the policy above the amount that would have been paid in the absence of this provision or take into account or operate to reduce any benefit other than loss-of-time benefit or to reduce the unadjusted loss-of-time benefit if the insured has suffered a catastrophic disability.

The overinsurance provision would be applicable only in a policy that:

- is payable for at least 52 weeks,
- is issued on the basis of selective underwriting, and
- the insured has the right to continue in force, subject to the timely payment of premiums until at least age 50, or in the case of a policy issued after age 44, for at least 5 years after its date of issue.

Refund of Unearned Premium

If the application of the overinsurance provision affects a material reduction of benefits otherwise payable under the policy, the insurer would be required to refund for the period of 2 years preceding the disability for which a claim is made, any premium unearned on the policy by reason of such reduction of coverage. The insurer would be authorized to provide in the policy that no such reduction in benefits or refund will be made unless the unearned premium to be refunded amount to $5 or more.

Required Disclosure to Applicants

An application for a policy containing the overinsurance provision authorized by this bill is required to include a statement disclosing that the benefits payable under the policy may be reduced, if the total loss-of-time coverage in effect exceeds a stated percent of the applicant's income.

Rulemaking Authority

The Department of Insurance would be authorized to enact rules to prescribe definitions, forms, and procedures necessary to administer the provisions of the bill.

Effective Date of Overinsurance Provision

The bill would take effect on October 1, 1999. Since this bill authorizes an insurer to include an overinsurance provision in the insurance contract, it would follow that the overinsurance provision in the bill would only apply to insurance contracts entered into after October 1, 1999.

Similarity to NAIC Model Act

The provisions of this bill are similar to the model “overinsurance” regulations issued by the NAIC. However, this bill is different than the NAIC model in three ways:

- the bill includes a provision requiring insurers to refund 2 years of unearned premium;
- the bill includes a provision prohibiting benefit reduction for “catastrophic disability”; and
- the calculation formula for adjusting benefits in the bill has been simplified by eliminating the subtraction of other valid loss-of-time coverage that does not contain an overinsurance provision.

Issues Relating to the Overinsurance Provision

As drafted, the bill does not require insurers to include an overinsurance provision in disability policies. The bill provides that insurers "may" include such a provision. However, the overinsurance provision may operate to require insurers that do not have such a provision to pay higher benefits than those that do. For example, assume an employee has two disability policies with private insurers and only one contains the bill’s overinsurance provision. If this bill was not enacted, each insurer would take a proportionate reduction to the extent the combined benefits exceed 100 percent of the employee’s pre-disability earnings. However, under the bill, the insurer having the overinsurance provision would reduce the benefits paid to the extent the employee’s combined benefits exceed the earning replacement percent (at least 60 percent) of the pre-disability earnings. In the latter case, the insurer having the overinsurance provision would pay less than the insurer that does not. This may provide an incentive for all insurers to include the overinsurance provision so as not to pay more than other insurers.

The bill’s overinsurance provision would provide for an adjustment of loss-of-time benefits payable by an insurer where the combination of all valid loss-of-time coverage exceeds the earnings replacement percentage (at least 60 percent). This means that an insurer with an overinsurance provision would have priority over other loss-of-time coverages -- i.e., it would be authorized to adjust benefits where other loss-of-time coverages would not. For example, a workers’ compensation carrier would not be able to adjust benefits like those insurers who have overinsurance provisions.

The bill’s overinsurance provision authorizes insurers to adjust the loss-of-time benefit payable based on the sum of all loss-of-time coverages, including workers’ compensation. However, the bill does not specify whether the workers’ compensation benefits are to be included in the calculation before or after offsets for Grice are taken. See the Comments section of the analysis for further discussion of this issue.

Finally, the bill sets forth a calculation which determines how an insurer may adjust the loss-of-time benefits payable under the policy. This calculation involves adding together the total loss-of-time coverages. Some loss-of-time coverages, such as workers’ compensation, may cease after a certain period of time or may change. In such situations, the overinsurance adjustment calculation would need to be redone in order for the employee to receive the correct amount of benefits. The bill does not contain language relating to recalculation in such circumstances. See Comments section of the analysis for further discussion of this issue.

C. APPLICATION OF PRINCIPLES:

1. Less Government:

a. Does the bill create, increase or reduce, either directly or indirectly:

(1) any authority to make rules or adjudicate disputes?

Yes. The bill authorizes the Department of Insurance to enact rules to prescribe definitions, forms, and procedures necessary to administer the provisions in the bill.

(2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

N/A

(3) any entitlement to a government service or benefit?

N/A

b. If an agency or program is eliminated or reduced:

(1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

N/A

(2) what is the cost of such responsibility at the new level/agency?

N/A

(3) how is the new agency accountable to the people governed?

N/A

2. Lower Taxes:

a. Does the bill increase anyone's taxes?

No.

b. Does the bill require or authorize an increase in any fees?

No.

c. Does the bill reduce total taxes, both rates and revenues?

No.

d. Does the bill reduce total fees, both rates and revenues?

No.

e. Does the bill authorize any fee or tax increase by any local government?

No.

3. Personal Responsibility:

   a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

      No.

   b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

      N/A

4. Individual Freedom:

   a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

      N/A

   b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

      N/A

5. Family Empowerment:

   a. If the bill purports to provide services to families or children:

      (1) Who evaluates the family's needs?

          N/A

      (2) Who makes the decisions?

          N/A

      (3) Are private alternatives permitted?

          N/A

      (4) Are families required to participate in a program?

          N/A

      (5) Are families penalized for not participating in a program?

          N/A

   b. Does the bill directly affect the legal rights and obligations between family members?

      N/A

   c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

(1) parents and guardians?

N/A

(2) service providers?

N/A

(3) government employees/agencies?

N/A

D. STATUTE(S) AFFECTED:

This bill creates s. 627.6245, F.S.

E. SECTION-BY-SECTION ANALYSIS:

Section 1: Creates s. 627.6245, F.S., authorizing insurers to include an overinsurance provision in disability insurance contracts which enables insurers to adjust loss-of-time benefits payable to an insured when the total loss-of-time coverages available to the insured exceed a certain percentage of the insured's earned income.

For a detailed discussion of the new provision see the "Effect of Proposed Changes" section of the analysis.

Section 2: Provides an effective date of October 1, 1999.

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

N/A

4. Total Revenues and Expenditures:

N/A

B. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

   N/A

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

1. Direct Private Sector Costs:

   There could be costs to private individuals who purchase a disability insurance policy because the benefits under the policy could be reduced if the individual purchases an additional policy with an overinsurance provision. Policyholders could also incur costs in that they would be limited to a refund of only 2 years of unearned premium under this bill.

2. Direct Private Sector Benefits:

   Insurers could benefit because limits could be placed on benefits to insureds provided under a disability policy.

3. Effects on Competition, Private Enterprise and Employment Markets:

   N/A

D. FISCAL COMMENTS:

   N/A

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

   N/A

B. REDUCTION OF REVENUE RAISING AUTHORITY:

   N/A

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

   N/A

V. COMMENTS:

Effective Date

SB 1092, the Senate companion to this bill, contains the same effective date as this bill (October 1, 1999), but specifies that the overinsurance provision only applies to contracts entered into after the effective date. This bill does not contain such language. However, the bill's omission of language relating to the application of the overinsurance provision does not mean that the overinsurance provision could be applied to insurance policies entered before the effective date. Insurance policies are contracts. Therefore, insurers cannot enforce a provision which is not a part of the contract. But, it would seem that insurers could include the overinsurance provision in the policy when the policy is renewed.

Grice

An issue not addressed in the bill is which adjustment occurs first -- the Grice offset for workers' compensation or the overinsurance adjustment in the bill. In Grice, the Florida Supreme Court stated that the carrier is entitled to an offset to the extent that benefits from workers' compensation, social security,

and "other collateral sources" exceeds 100 percent of the employees pre-injury wages. The phrase "other collateral sources" has not been fully defined by Florida courts. As such, it is possible that disability benefits payable under a private disability insurance policy could be included in the calculation of a Grice offset. If this is the case, the issue arises as to whether the overinsurance adjustment occurs before the disability benefits are included in the Grice offset calculation. And, vice versa, whether the Grice offset occurs before the workers' compensation benefits are included in the overinsurance adjustment calculation.

Overinsurance Adjustment Calculation

The bill does not contain any language relating to when the overinsurance adjustment calculation would take place. It is possible that certain other coverages (such as workers' compensation) would cease or change during the duration of the disability, thus changing the benefit adjustment under the overinsurance provision. It is possible that the bill could be interpreted so that the calculation occurs each time a payment is made (usually monthly). If this is the case, changes in the other loss-of-time coverages could be taken into account in the recurring overinsurance calculation.

Definitions

The bill provides definitions of several terms, including "earned income" and "catastrophic disability." The term, "earned income," is defined in the bill as the greater of the monthly earnings at the time of the disability or the average monthly earnings for a period of 2 years preceding the disability. Under current law, "earned income" is separately defined in s. 443.036(16), F.S. (the unemployment compensation act). For clarification purposes, the definition of "earned income" in the bill could be qualified so that it applies only in overinsurance calculations for disability policies.

The bill also defines the term "catastrophic disability" as a "total and permanent loss of speech, hearing in both ears, sight in both eyes, use of both legs, use of both arms, or use of one arm and one leg." While this term is referred to as a catastrophic "disability," the definition does not make a connection between the listed impairments and the individual's inability to work, which is the essence of a disability. For example, a computer programmer may lose both legs in an accident but still have the ability to work (i.e., not be disabled). Therefore, the term may be more appropriately referred to as a "catastrophic injury." If this term were used, however, it would have to be distinguished from the term "catastrophic injury" found in s. 440.02, F.S. (the workers' compensation act).

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

On April 13, 1999, the Committee on Insurance adopted two amendment to the bill.

Amendment 1 by Patterson (p. 2, line 26): would modify the proposed calculation of "earned income" in the bill so that "earned income" is the greater of the monthly earnings of the insured at the time of the disability or the average monthly earnings for the **5** years prior to the disability. The bill currently provides that earned income is the greater of the monthly earnings of the insured at the time of the disability or the average monthly earnings for the **2** years prior to the disability.

Amendment 2 by Patterson (p. 4, lines 6 through 26): would make several changes to the bill including:

- permitting policy applicants to indicate on the application that other loss-of-time coverage will be continued, thus excluding those coverages from the overinsurance adjustment calculation;
- specifying the information needed by insurers as part of the proof of claim in order to administer the overinsurance provision;
- extending the proposed period for refunding unearned premium from 2 years to the entire period of the policy from the date of issue to the date of claim;
- requiring the proposed disclosure statement to be on both the application and the face page of each policy and requiring the disclosure to be in boldface 10 point type; and

- modifying the proposed disclosure statement to clarify that the overinsurance provision applies to the insured's income at the time a claim is made.

VII. SIGNATURES:

COMMITTEE ON INSURANCE:

Prepared by:	Staff Director:
______________________	______________________
Robert E. Wolfe, Jr.	Stephen Hogge