

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Committee on Banking and Insurance

BILL: SB 1866

INTRODUCER: Senator Broxson

SUBJECT: Loss-sensitive Workers' Compensation Insurance Programs

DATE: February 19, 2018

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Knudson	Knudson	BI	Pre-meeting
2.			CM	
3.			RC	

I. Summary:

SB 1866 amends the workers' compensation rating law to allow qualified insurers to issue a guaranteed cost workers' compensation insurance policy that is accompanied by a qualified loss-sensitive program of reinsurance. The employer, if a qualified insured, purchases the "guaranteed cost workers' compensation insurance policy" at a set premium based on approved rates multiplied by applicable class codes, which does not change because of losses during the policy period. The guaranteed cost policy is accompanied by a "qualified loss-sensitive program of reinsurance" agreement between the employer (qualified insured) and a qualified reinsurer wherein the employer participates in the underwriting profit or loss associated with the workers' compensation insurance policy issued to the insured. Thus, the employer's cost to procure coverage increases or decreases based on the terms of the reinsurance agreement and the employer's loss experience.

The bill exempts forms governing a qualified loss-sensitive program of reinsurance from the insurance policy form approval requirements of the Insurance Code.

The bill defines the parties that may enter into such agreements:

- A "qualified insurer" must be authorized in this state, have a combined loss ratio of less than 100 on January 1 of the 2 preceding years, have assets in excess of \$500 million on January 1 of the year the workers' compensation policy is issued, and an A+ rating from A.M. Best.
- A "qualified insured" must have its principal place of business in this state and an annual workers' compensation premium of at least \$500,000.
- A "qualified loss-sensitive program of reinsurance" must be effected through a separate reinsurance arrangement with a reinsurer admitted in a state accredited by the National Association of Insurance Commissioners (NAIC) in connection with a guaranteed cost workers' compensation policy, and contain a minimum and maximum loss participation limit.

II. Present Situation:

Administration of the Workers Compensation System in Florida

The Division of Workers' Compensation within the Department of Financial Services is responsible for administering ch. 440, F.S. These functions include the enforcement of coverage requirements,¹ administration of workers' compensation health care delivery system,² data collection,³ and assisting injured workers, employers, insurers, and providers in fulfilling their responsibilities under ch. 440, F.S.⁴ Workers' compensation is the injured employee's remedy for "compensable" workplace injuries.⁵ Employees generally cannot sue a covered employer for workplace injuries.⁶

Medical Benefits

Injured workers are entitled to receive all medically necessary remedial treatment, care, and attendance, including medications, medical supplies, durable medical equipment, and prosthetics, for as long as the nature of the injury and process of recovery requires.⁷ Medical services must be provided by a health care provider authorized by the carrier prior to being provided (except for emergency care).⁸ When the carrier has knowledge of a work-related injury, it will refer the injured employee to an authorized workers' compensation provider.

Authorized medical services and treatments are provided at no cost to the injured employee, except employees are required to pay a \$10 co-payment for medical services provided after they have reached "maximum medical improvement."⁹ Injured employees are entitled to one change of physician during the course of treatment for any one accident.¹⁰ After the initial examination and diagnosis, the workers' compensation health care provider is required to submit a proposed course of treatment to the carrier to determine whether such treatment would be recognized as reasonably prudent.¹¹

¹ Section 440.107(3), F.S.

² Section 440.13, F.S.

³ Sections 440.185 and 440.593, F.S.

⁴ Section 440.191, F.S.

⁵ "Compensable" means a determination by a carrier or judge of compensation claims that a condition suffered by an employee results from an injury arising out of and in the course of employment. s. 440.13(1)(d), F.S.

⁶ Section 440.11(1), F.S. Employers who fail to obtain required workers' compensation coverage may be sued by an injured worker in civil court. Likewise, an employee who is either exempt or excluded from workers' compensation coverage requirements may sue their employer in civil court for work-related injuries, even if the employer has coverage for their other employees.

⁷ Section 440.13(2)(a), F.S.

⁸ Section 440.13(3)(a), F.S.

⁹ The date of maximum medical improvement is the date after which further recovery from, or lasting improvement to, an injury or disease can no longer reasonably be anticipated, based upon reasonable medical probability. Section 440.02(10), F.S.

¹⁰ Section 440.13(2)(f), F.S.

¹¹ Section 440.13(2)(e), F.S.

Indemnity Benefits

Indemnity benefits¹² only become payable to employees who are disabled for at least 8 days due to a compensable workplace injury.¹³ The first 7 days of lost earnings may be paid retroactively to employees who are disabled for more than 21 days.¹⁴ These benefits are generally payable at 66 2/3 percent of the employee's average weekly wage (AWW),¹⁵ up to the maximum weekly benefit established by law.¹⁶ For 2016, this amount is \$863, which is the statewide average weekly wage (SAWW).¹⁷ Payments are due every 2 weeks.¹⁸ Indemnity benefits fall into one of four categories: temporary partial disability, temporary total disability, permanent partial disability, and permanent total disability.

- Temporary partial disability and temporary total disability benefits are payable for up to a combined total of 260 weeks.¹⁹
- Permanent partial disability benefits are payable as impairment income benefits that are provided for a variable number of weeks depending upon the value of the injured worker's permanent impairment rating pursuant to a statutory formula.²⁰
- Permanent total disability benefits are payable until the age of 75, unless the work-related accident occurs after the worker's 70th birthday, then the benefit is paid for 5 years.²¹

Workers' Compensation Coverage

Generally, employers may secure coverage from an authorized carrier or qualify as a self-insurer.²² Employers that are not self-insured and are unable to secure coverage from a carrier may purchase coverage from the Workers' Compensation Joint Underwriting Association

¹² Workers' compensation benefits received for an "occupational sickness or injury are fully exempt from [federal income] tax if they are paid under a workers' compensation act or a statute in the nature of a workers' compensation act." Internal Revenue Service, *Publication 525 (2016), Taxable and NonTaxable Income*, available at <https://www.irs.gov/pub/irs-pdf/p525.pdf> (last visited April 17, 2017).

¹³ Section 440.12(1), F.S.

¹⁴ *Id.*

¹⁵ An injured workers' average weekly wage is an amount equal to one-thirteenth of the total amount of wages earned during the 13 weeks immediately preceding the compensable accident. s. 440.14(1), F.S.

¹⁶ Section 440.15(1)-(4), F.S.

¹⁷ "Statewide average weekly wage" means the average weekly wage paid by employers subject to the Florida Reemployment Assistance Program Law as reported to the Department of Economic Opportunity (DEO) for the four calendar quarters ending each June 30, which average weekly wage shall be determined by the DEO on or before November 30 of each year and shall be used in determining the maximum weekly compensation rate with respect to injuries occurring in the calendar year immediately following. s. 440.12(b), F.S. See DFS website at <http://www.myfloridacfo.com/division/wc/Insurer/awwrate.htm#.WOPgOMHr2Uk> (last viewed Apr. 4, 2017).

¹⁸ Section 440.20(2)(a), F.S.

¹⁹ Section 440.15(2) and (4), F.S. Section 440.15(2)(a), F.S., specifies that temporary total disability benefits are payable for 104 weeks; however, the Florida Supreme Court has found this provision unconstitutional and the statute has reverted to 260 weeks of temporary total disability benefits pursuant to this case law. *Westphal v. City of St. Petersburg*, 194 So.3d 311 (Fla. Jun. 9, 2016). Section 440.15(4)(e), F.S., provides that temporary partial disability benefits; however, the 1st DCA applied the holding in *Westphal* to these benefits finding the limitation unconstitutional and reverted the limitation to the 260 weeks previously allowed. *Jones v. Food Lion, Inc.*, No. 1D15-3488, 2016 Fla. App. LEXIS 16710 (Fla. 1st DCA Nov. 9, 2016).

²⁰ Section 440.15(3), F.S.

²¹ Section 440.15(1), F.S.

²² Section 440.38, F.S.

(WCJUA).²³ The (WCJUA) is the insurer of last resort for workers' compensation insurance, also known as the residual market.

Florida Workers Compensation Rating System

The OIR regulates workers' compensation rates pursuant to authority granted under part I of ch. 627, F.S. Florida uses a full rate system, which requires the rate to include benefits, loss adjustment expenses, commissions, taxes, general administrative expenses and profits and contingencies. Seven states use an administered pricing or full rate system.

The insurance rate is the "unit charge by which the measure of exposure or the amount of insurance specified in a policy of insurance or coverage thereunder is multiplied to determine the premium."²⁴ A manual rate per \$100 of payroll is developed for each of the 600 classification codes that reflects the potential for loss associated with a group of employers engaged in the same type of business or industry. This rate is multiplied by the employer's payroll to determine the unadjusted premium. Then, the unadjusted premium is multiplied by the employer's experience modification factor to determine the adjusted premium. An experience rating compares an employer's actual losses and the losses that would be expected to occur for an average employer with a similar business.

The OIR must approve or disapprove rates in the voluntary market prior to becoming effective.²⁵ In determining whether to approve or disapprove a workers' compensation rate filing, the OIR considers certain statutory standards and factors specified in ss. 627.062 and 627.072, F.S.²⁶ The standard for approving insurance rates in Florida and most states is that the rate may not be excessive, inadequate, or unfairly discriminatory.

Florida law requires every workers' compensation insurer to file with the OIR its rates and classifications that the insurer proposes to use.²⁷ However, the law allows an insurer to satisfy this obligation by becoming a member of a licensed rating organization, which makes such filings on its behalf.²⁸ All workers' compensation insurers in Florida have chosen to become members of the NCCI.

The law and the rating plans approved by OIR allow for mechanisms for insurers to vary premiums. Insurers may use the following pricing tools to compete on price, as described below:

- **Consent to Rate** – The insurer and employer agree to a rate in excess of the approved rate. The insurer must limit this option to no more than 10 percent of policies written or renewed in each calendar year.
- **Deviations** – An insurer is allowed to file a uniform percentage increase or decrease applicable to all rates an insurer charges or to rates for a particular class or group of classes of insurance.

²³ Section 627.311(5)(a), F.S.

²⁴ Section 627.091, F.S.

²⁵ Section 627.101, F.S.

²⁶ Section 627.151, F.S.

²⁷ Section 627.211, F.S.

²⁸ Section 627.091, F.S.

- Intermediate Deductibles – For a reduced premium, the employer agrees to reimburse the insurer for each claim up to the deductible amount. Intermediate deductibles range from \$5,000 to \$75,000. Similar to small deductible policies the insurer is responsible from first dollar of loss (i.e. losses below the deductible).
- Large Deductibles – Large deductible policies operate similarly to the small and intermediate deductible, but have a deductible amount of \$100,000 and above. In order to qualify for the large deductible program, an employer must have a standard premium of at least \$500,000.
- Large Risk Alternative Rating Option (LRARO) – In most states, LRARO is defined as a flexible retrospective rating plan mutually agreed to by the employer and carrier. In Florida, LRARO is a provision within the currently approved retrospective rating plan that allows for negotiation of a premium between the employer and the insurer.
- Policyholder Dividends – Insurers reward their policyholders by returning some of their profit at the expiration of the policy by issuing policyholder dividends, which may be based on the policyholder's, the carrier's experience, and other factors.

Reinsurance

Reinsurance transfers to reinsurer the potential financial consequences of certain loss exposures for the purpose of protecting the financial solvency of the ceding insurer and enabling it to meet its obligations to policyholders and claimants.²⁹ Reinsurance contracts are exempt from rate and form regulation under Florida law, but all reinsurance must comply with the provisions of s. 624.610, F.S., which provides criteria for when credit for reinsurance must be allowed. Sections 624.81, F.S., and 624.83, F.S., require reinsurance to be for the benefit of the ceding insurer.

According to the Office of Insurance Regulation, the only employers that may purchase reinsurance are qualified self-insured employers because s. 440.38, F.S., states that only self-insureds are an employer for purposes of ch. 440, F.S.³⁰

III. Effect of Proposed Changes:

Section 1 amends s. 627.072, F.S., which governs workers' compensation insurance ratemaking, to specify that if a qualified insurer in this state issues a guaranteed workers' compensation insurance policy on an approved form and with approved rates to a qualified insured, an accompanying form governing a qualified loss-sensitive program of reinsurance must be filed with the OIR for informational purposes but does not require approval.

The bill is intended to allow qualified insurers to issue a guaranteed cost workers' compensation insurance policy that is accompanied by a qualified loss-sensitive program of reinsurance. The employer, if a qualified insured, purchases the "guaranteed cost workers' compensation insurance policy" at a set premium based on approved rates multiplied by applicable class codes, which does not change because of losses during the policy period. This is a different premium structure than is currently used to calculate workers' compensation premiums that are loss-sensitive.

²⁹ Ann E. Myhr and James J. Markham, *Insurance Operations, Regulation, and Statutory Accounting*, at pg 1.28 (2007).

³⁰ Office of Insurance Regulation, *Agency Legislative Bill Analysis SB 1866*, pg. 2. (Jan. 12, 2018).

The guaranteed cost policy is accompanied by a “qualified loss-sensitive program of reinsurance” agreement between the employer (qualified insured) and a qualified reinsurer wherein the employer participates in the underwriting profit or loss associated with the workers’ compensation insurance policy issued to the insured. Thus, the employer’s cost to procure coverage increases or decreases based on the terms of the reinsurance agreement and the employer’s loss experience. The “qualified loss-sensitive program of reinsurance” would not be subject to regulation by the OIR, thus the premium ultimately paid by the employer would essentially be unregulated.

The bill defines the following terms:

- A “guaranteed cost workers’ compensation insurance policy” is a workers’ compensation insurance policy that is based on approved rates multiplied by applicable class codes and is not changed by losses in the period for which it is used.
- A “qualified insurer” must be authorized in this state, have a combined loss ratio of less than 100 on January 1 of the 2 preceding years, have assets in excess of \$500 million on January 1 of the year the workers’ compensation policy is issued, and an A+ rating from A.M. Best.
- A “qualified insured” must have its principal place of business in this state and an annual workers’ compensation premium of at least \$500,000.
 - Under current law, a retrospective rating plan is allowed if the employer has an estimated standard premium in Florida of at least \$100,000, and an estimated countrywide standard premium of at least \$750,000 for workers’ compensation.
- A “qualified loss-sensitive program of reinsurance” must be effected through a separate reinsurance arrangement with a reinsurer admitted in a state accredited by the National Association of Insurance Commissioners (NAIC) in connection with a guaranteed cost workers’ compensation policy, and contain a minimum and maximum loss participation limit.
 - Reinsurance is the transfer of an insurance company’s loss exposure to the reinsurer. Here, the insured is a party to the reinsurance agreement and participates in the underwriting risk associated with the workers’ compensation policy.

Section 2 amends s. 627.4102, F.S., to provide that forms governing a qualified loss-sensitive program of reinsurance, as defined in s. 627.072(6), F.S., is exempt from form approval under s. 627.410, F.S.

Section 3 provides an effective date of July 1, 2018.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

Indeterminate.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

The OIR may find it difficult to enforce the requirement on lines 25-27 that a qualified insured must have an annual workers' compensation premium of at least \$500,000 because premium is estimated at policy inception. Workers' compensation policies have different types of premiums, thus specifying the definition of premium being used here would improve clarity.

The bill should specify on lines 25-31 whether the requirements as to a qualified insured's annual premium and a qualified insurer's loss ratio refer to premium or loss ratio in Florida, or countrywide.

VII. Related Issues:

The Office of Insurance Regulation recommends that if the insurance product created by this bill is sold in this state, policyholders should be provided extensive disclosures regarding their potential liabilities under the qualified loss-sensitive program of insurance.³¹ The California Department of Insurance recently entered into a settlement agreement with a workers' compensation insurer regarding such a product that requires disclosures to potential insureds.³²

VIII. Statutes Affected:

This bill substantially amends the following sections of the Florida Statutes: 627.072 and 627.4102.

³¹ See *OIR Agency Legislative Bill Analysis SB 1866* at pg. 6.

³² California Department of Insurance, *Berkshire Hathaway Subsidiary Applied Underwriters Settlement Information*, <https://www.insurance.ca.gov/0400-news/0100-press-releases/2017/BerkshireHathawayInfo.cfm> (last accessed Feb. 19, 2018).

IX. Additional Information:

- A. **Committee Substitute – Statement of Changes:**
(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

- B. **Amendments:**

None.

This Senate Bill Analysis does not reflect the intent or official position of the bill's introducer or the Florida Senate.
