

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

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

BILL: CS/SB 1766

SPONSOR: Banking and Insurance Committee and Senator Alexander

SUBJECT: Florida Workers' Compensation Insurance Guaranty Association

DATE: April 18, 2003 REVISED: 4/22/03 _____

| | ANALYST | STAFF DIRECTOR | REFERENCE | ACTION |
|----|--------------------|--------------------|-----------|---------------------|
| 1. | <u>Deffenbaugh</u> | <u>Deffenbaugh</u> | <u>BI</u> | <u>Favorable/CS</u> |
| 2. | <u>Cibula</u> | <u>Maclure</u> | <u>CM</u> | <u>Favorable</u> |
| 3. | _____ | _____ | <u>JU</u> | _____ |
| 4. | _____ | _____ | _____ | _____ |
| 5. | _____ | _____ | _____ | _____ |
| 6. | _____ | _____ | _____ | _____ |

I. Summary:

The committee substitute expands the assessment base for funding the Florida Workers' Compensation Insurance Guaranty Association (FWCIGA or association), which pays workers' compensation claims of insolvent insurers and self-insurance funds. The committee substitute provides that the assessments against insurers and self-insurers of a specified percentage of workers' compensation premiums written in the state would be applied to the full policy premium value, without taking into account any discount or credit for deductibles. The committee substitute does not increase the percentage caps on assessments, but the expanded assessment base significantly increases funding for FWCIGA, which is facing mounting liabilities. A similar change was made in 2000 to the assessments levied against carriers to fund the state's costs of administering the workers' compensation laws.

The committee substitute also limits the obligation of FWCIGA to \$50,000, for covering claims for the return of unearned premiums. In addition, the committee substitute provides for a 6-month stay of all legal proceedings in which an insolvent insurer is a party, as the law currently provides if a self-insurance fund is a party to a legal proceeding.

The association is funded through annual assessments, capped at 2 percent of each insurer's net direct written premium in Florida, and capped at 1.5 percent for self-insurance funds. Assessments were levied at these maximum rates for 2002 and 2003. The law allows an *additional* 1.5-percent assessment against insurers (but not funds), totaling 3.5 percent, if necessary to meet fund obligations. This extra 1.5-percent assessment has never been levied, but some or all of this amount is expected to be levied later this year for 2003 obligations, primarily due to the insolvency of a large insurer. Whether the absolute maximum assessments are adequate to cover obligations in 2004 and beyond is in doubt, primarily due to the insolvency of this insurer and another large insurer that is insolvent, but not yet in liquidation.

This committee substitute substantially amends the following sections of the Florida Statutes: 631.913, 631.914, and 631.924.

II. Present Situation:

Florida Workers' Compensation Insurance Guaranty Association

In Florida and every other state, when the assets of an insolvent insurer are insufficient to pay claims, the claims for most types of insurance are paid in whole or in part by a guaranty fund.¹ Chapter 631, F.S., creates four different guaranty funds for different types of insurance, one of which is the Florida Workers' Compensation Insurance Guaranty Association (FWCIGA, or association).² The FWCIGA covers claims of insolvent authorized insurers (with a certificate of authority issued in Florida), as well as claims of insolvent workers' compensation insurance funds licensed in Florida.

Florida is one of only four states to have a separate guaranty fund for workers' compensation insurers. The FWCIGA was created in 1997 by merging the Florida Self-Insurance Fund Guaranty Association and the workers' compensation insurance account of the Florida Insurance Guaranty Association.³ The association evaluates workers' compensation claims made by injured employees against insolvent member companies or funds, and determines if such claims are covered and should be paid or settled with association funds. The association pays the claims of insolvent workers' compensation insurers and self-insurance funds, but does not pay claims for insolvent individually self-insured employers, which are covered by a separate guaranty association.⁴

Regulatory Authority

The Office of Insurance Regulation currently licenses and regulates workers' compensation insurers and self-insurance funds, as previously regulated by the Department of Insurance. However, the Department of Financial Services administers ch. 440, F.S., the Workers' Compensation Law. The department is also authorized to be appointed as receiver of an insolvent insurer or fund, as well as having oversight responsibility for the various insurance guaranty associations.⁵

¹ National Conference of Insurance Guaranty Funds, *Guaranty Fund Laws Summary*, July 31, 2002, available at <http://www.ncigf.org/> (last visited April 15, 2003).

² Sections 631.901-631.932, F.S.

³ Chapter 97-262, L.O.F.

⁴ Section 440.385, F.S.

⁵ Effective January 7, 2003, the Department of Insurance was transferred to the Department of Financial Services and to the Office of Insurance Regulation. (ch. 2002-404, L.O.F.) The 2002 act provides that the Office of Insurance Regulation (OIR) is responsible for all matters relating to insurers and other risk-bearing entities. However, the Department of Financial Services (DFS) was assigned the Division of Workers' Compensation, as well as the Division of Rehabilitation and Liquidation. (s. 20.121, F.S.) This session, CS/CS/SB 1712, amends the Florida Statutes to make conforming changes to the 2002 act, including a requirement that the OIR license and regulate insurers and self-insurance guaranty funds, and that the DFS administer the provisions of ch. 440, F.S., the Workers' Compensation Law. The committee substitute also authorizes DFS to petition a circuit court for an order in a delinquency proceeding against an insurer, upon being required to do so by the OIR, and to be appointed as receiver, liquidator, or rehabilitator of the insurer; authorizes DFS to approve plans of operation and have oversight responsibilities for insurance guaranty associations; and authorizes the Chief Financial Officer

Assessments by FWCIGA; Current Status

The Florida Workers' Compensation Insurance Guaranty Association is funded by assessments against all workers' compensation insurance and self-insurance funds. The association is authorized to determine whether an assessment against its members is necessary to pay covered claims or to reimburse the association for its administrative expenses. Section 631.914, F.S., authorizes the association to annually assess insurers up to 2 percent, and self-insurance funds up to 1.5 percent, of their annual net direct written premium for workers' compensation policies in Florida. If the 2-percent assessment against insurers and 1.5-percent assessment against self-insurance funds is insufficient for the FWCIGA to make reimbursements then owing to claimants, then upon certification by the FWCIGA board, the Department of Financial Services shall levy additional assessments of up to 1.5 percent of the insurer's net direct written premiums during the calendar year next preceding⁶ the date of such assessments against insurers (but not self-insurance funds) to secure the necessary payment of funds. (s. 631.914(1)(c)1., F.S.)

The obligations of the FWCIGA have grown significantly over the past two years and are projected to rise even further. FWCIGA reports that it levied a .05 percent assessment against insurers and funds in 2000, a 1.0-percent assessment in 2001, and the "maximum" (first level) assessment of 2.0 percent against insurers and 1.5 percent against funds in both 2002 and 2003. The extra 1.5-percent assessment against insurers that is authorized has never been used, but some or all of this amount is projected to be necessary to fully cover obligations for 2003. Without the extra 1.5-percent assessment, the association projects a deficit of about \$10.2 million on December 31, 2003. The additional 1.5-percent assessment would generate additional revenue of about \$38.9 million. Whether the absolute maximum assessments are sufficient to meet obligations for 2004 and beyond is in doubt. The board has already approved a 2-percent assessment (and a 1.5-percent assessment for funds) for 2004, to be levied in January of that year.

The recent insolvency of a very large insurer, Reliance, has caused a major drain on the guaranty fund. Another large insurer has been found insolvent, but has not yet been placed in liquidation. The association is handling the estates of 54 insolvent insurers and 2,878 open claims by injured workers. According to FWCIGA's *Cash Flow Forecast for 2003*, FWCIGA will have a negative \$10.2 million cash balance at the end of December 2003.

The assessments levied by FWCIGA are levied on "net direct written premiums," meaning the direct gross premiums written in the state, less return premiums and dividends paid or credited to policyholders. (s. 631.54(8), F.S.) The assessment is not applied to any deductible amount. That is, the assessment is not applied to the amount of the discount or credit received by the policyholder from the full premium. In contrast, the assessment levied against carriers to fund the state's costs of administering the workers' compensation laws is applied to the deductible

(who is head of DFS) to make those appointments to the boards of insurance guaranty funds which were previously made by the Insurance Commissioner.

⁶ The term "next preceding" is not defined in the Florida Statutes. However, the use of the term "next preceding" as used in the context of *State v. White*, 73 Fla. 426 (Fla. 1917) appears to mean "preceding" or "immediately preceding." "The word 'month' as used in [certain] statutes ... means a calendar month, or that period of time elapsing between a given date and the corresponding date of the next preceding month by name." *Id.* at 431.

amount.⁷ The inclusion of the deductible amount in calculating the administrative assessment was made in 2000, after it became apparent that an increasing number of large deductible policies were being obtained, for the ostensible purpose of mitigating the costs of the assessment.⁸ This activity may be still occurring, to mitigate FWCIGA assessments.

Representatives of FWCIGA state that the association is responsible for paying workers' compensation claims of insolvent insurers, even for the amount of any deductible under the policy. This is so, according to the association, because the association stands in the place of the insolvent insurers and self-insurance funds and must pay all claims. The employer, however, is responsible for reimbursing the insurer or self-insurance fund up to the amount of the deductible on the insurance policy purchased by the employer. Although an employer is ultimately liable for claims paid up to the amount of the deductible, only the receiver of the insolvent insurer or self-insurance fund may pursue the claim.

The law provides that the 2-percent (or lower) assessment against carriers "shall be included as an appropriate factor in the making of rates." (s. 631.914(1)(b), F.S.) This indicates that such costs may be included in the rate filing that is made by the insurer or the rating organization (the National Council on Compensation Insurers, or NCCI) that files rates on behalf of all workers' compensation carriers in the state, subject to approval by the Office of Insurance Regulation. However, the extra 1.5-percent assessment that may be levied provides that each insurer or a licensed rating organization may make a rate filing within 90 days after being notified of the assessment. If the rate filing reflects a percentage rate change equal to the difference between the rate of the assessment and the rate of the previous year's assessment (referring only to the extra 1.5-percent assessment), the filing shall be deemed approved when made.

Claims for Unearned Premium Refunds

The FWCIGA is also liable for payment of claims of unearned premiums owed to employers of insolvent workers' compensation carriers. There is no statutory limit on such claims. In s. 8.A.(1)(a)(ii) of the Post-Assessment Property and Liability Insurance Guaranty Association Model Act, by the National Association of Insurance Commissioners, claims for return of unearned premiums are limited to \$10,000.

Stay of Legal Proceedings

Currently, s. 631.924, F.S., provides that all legal proceedings in which an insolvent self-insurance fund is a party are stayed for 6 months to allow for the association to defend covered claims. By its terms, this section does not apply to legal proceedings in which an insurer is a party. According to the association, a court has never denied the association's request to stay legal proceedings in which an insolvent insurer was a party; however, there is no statutory entitlement to a stay.

⁷ Section 440.51(1)(b), F.S. The administrative assessment is capped at 2.75 percent of premium. The law provides that when reporting deductible policy premiums for purposes of computing assessments levied after July 1, 2001, full policy premium value must be reported prior to application of deductible discounts or credits. However, the assessment levied against carriers to fund the Special Disability Trust Fund, pursuant to s. 440.49(9)(b), F.S., does not include the deductible amount. (ch. 2000-150, L.O.F.)

⁸ Chapter 2000-150, L.O.F.

III. Effect of Proposed Changes:

The committee substitute expands the premium assessment base to fund the obligations of the Florida Workers' Compensation Insurance Guaranty Association, to include the full policy premium value, without taking into account any discount or credit for deductibles. (Section 2, amending s. 631.914, F.S.) This is the same accounting that is used for assessments to fund the Workers' Compensation Administration Trust Fund under s. 440.51, F.S.

By applying the assessment levied against insurers and self-insurance funds to the full policy value, including the deductible amount, the association estimates that its assessment base will increase from about \$2.6 billion to \$4.1 billion. As a result, the 2-percent assessment levied against insurers would generate \$81.1 million, rather than \$51.8 million.

The committee substitute also provides that the association's obligation to return any unearned premium to an employer shall not exceed \$50,000 per policy. (Section 1, amending s. 631.913, F.S.)

The committee substitute amends s. 631.924, F.S., to extend this section's application regarding the mandatory stay of proceedings regarding insolvent self-insurers to include proceedings against insolvent insurers. Currently, all legal proceedings in which an insolvent self-insurance fund is a party are stayed for 6 months to allow for the association to defend covered claims. The committee substitute applies this same provision to insurers that are parties in a legal proceeding.

The committee substitute takes effect upon becoming a law.

IV. Constitutional Issues:**A. Municipality/County Mandates Restrictions:**

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

By applying the assessment to the full policy value, including the deductible amount, the Florida Workers' Compensation Insurance Guaranty Association estimates that its

assessment base will increase from about \$2.6 billion to \$4.1 billion. As a result, the 2-percent assessment levied against insurers would generate \$81.1 million, rather than \$51.8 million.

C. **Government Sector Impact:**

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

The effective date of upon becoming law applies to the \$50,000 limit on the Florida Workers' Compensation Insurance Guaranty Association's obligation to pay employer claims for unearned premium. It may not be clear if this would apply to current insolvencies for which claims have already been filed, or would be limited to employer claims filed after the effective date, or orders of liquidation entered after the effective date, or some other triggering event.

VIII. Amendments:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.
