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 Commerce and Tourism

BILL: CS/CS/SB 810

INTRODUCER: Commerce and Tourism Committee, Banking and Insurance Committee, and Senator Simmons

SUBJECT: Wrap-up Insurance Policies

DATE: April 2, 2013 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Knudson	Burgess	BI	**Fav/CS**
2.	Malcolm	Hrdlicka	CM	**Fav/CS**
3.				
4.				
5.				
6.				

Please see Section VIII. for Additional Information:

A. COMMITTEE SUBSTITUTE.....	X	Statement of Substantial Changes
B. AMENDMENTS........................		Technical amendments were recommended
		Amendments were recommended
		Significant amendments were recommended

I. Summary:

CS/CS/SB 810 authorizes a wrap-up insurance policy for a nonpublic construction project to have a workers' compensation deductible of $100,000 or more if:

- The workers' compensation minimum standard premium calculated on the combined payrolls for all entities covered by the wrap-up policy exceeds $500,000;
- The estimated cost of construction at each specified worksite is $25 million or more;
- The insurer pays the first dollar of a workers' compensation claim without a deductible;
- The reimbursement of the deductible by the insured does not affect the insurer's obligation to pay claims;
- The insurer complies with specified workers' compensation filing requirements; and
- The insurer has a program to have the first-named insured reimburse the insurer for losses paid within the deductible.

This bill creates s. 627.4138, F.S.

II. Present Situation:

Wrap-Up Insurance Policies

Historically, for large construction projects, the project owners, the contractors, and the subcontractors purchase insurance independently to protect against their own potential financial losses related to the project. The contractor includes the cost of insurance in its bid and recovers the cost under the contract in the amount paid by the project owner. Under this arrangement, a contractor with a good safety record sometimes receives a rebate from its insurer as part of the provisions of the insurance contract. Because the contractor's cost of insurance has been recovered as part of the construction contract, any subsequent insurance rebates received by the contractor generate additional profits. In addition, a contractor with a good safety record can sometimes be awarded an additional bonus from the project owner.

In contrast to the traditional arrangement, consolidated insurance programs, often referred to as "wrap-up" insurance, are offered in the insurance market for large construction projects. Wrap-up insurance is a program or series of insurance policies purchased by one party (either the project owner or general contractor) to cover itself and all of its subordinate contractors and subcontractors for operations at a specific project site. Under wrap-up insurance, one party is responsible for purchasing insurance coverage that applies to all parties performing work, instead of the more traditional situation in which each party purchases its own coverage. Wrap-up policies may provide various coverages, but most commonly are used to provide workers' compensation and general liability coverage.

Wrap-up policies generally take the form of one of two types of consolidated insurance programs. In a contractor-controlled insurance program (CCIP), the general contractor purchases coverage for itself and each of its subcontractors. In an owner-controlled program (OCIP), the project owner purchases insurance to cover itself and all of its contractors and subcontractors. Under an OCIP, the project owner would receive any rebates that may be received from the insurer, based on the project's safety record.

In 1999, the U.S. General Accounting Office (GAO) published a report analyzing the advantages and disadvantages of wrap-up insurance for large construction projects. Based on an analysis of six large transportation projects, the report identified the following advantages and disadvantages of wrap-up insurance policies.[1]

Advantages

- Cost savings attributable to greater purchasing power and economies of scale available for large, labor-intensive projects.
- Elimination of overlap in coverage that can otherwise occur among the contractors and subcontractors insuring for the same accidents.
- More efficient claims handling processes and less litigation because a single insurer is used for reporting claims, conducting investigations, settling claims, and providing payment of claims.

[1] U.S. General Accounting Office, "Transportation Infrastructure: Advantages and Disadvantages of Wrap-Up Insurance for Large Construction Projects," Report No. GAO/RCED-99-155 (June 1, 1999), *available at* http://www.gao.gov/products/RCED-99-155 (last visited March 28, 2013).

- Facilitation of a well-managed, centralized safety program that results in fewer injuries.

Disadvantages
- Increased administrative costs. Although it may result in overall cost savings, the purchaser of the wrap-up product must devote additional resources related to emphasizing job safety, controlling losses, and managing claims.
- Potential for large premium payments at the start of a construction project and the establishment of a special reserve to ensure funds are available to pay deductible requirements on claims.

Workers' Compensation Insurance Policies with Large Deductibles
Large deductible workers' compensation insurance policies are regulated by the Office of Insurance Regulation (OIR) under Rule 69O-189.006, F.A.C. The rule establishes guidelines for large deductible (a deductible of $100,000 or more per claim) workers' compensation filings. In order to qualify for a large deductible policy, an employer must have a workers' compensation standard premium of at least $500,000.[2] Under large deductible programs, the carrier is obligated to pay the claim from the first dollar, but the insured (the employer) then reimburses the workers' compensation carrier, for each claim, for losses paid within the deductible.

The OIR reports that the typical large deductible policy will have a deductible credit that ranges from 30 to 90 percent.[3] As a result, the premiums paid by employers that purchase large deductible policies will be a fraction of the premiums paid for other workers' compensation plans. An ancillary effect of the availability of large deductible plans is that an increasing number of very large employers have ceased being individually self-insured and instead buy large deductible products.

The OIR notes that in some recent insolvencies there have been problems with large deductible policies and the lack of collectible collateral. The remaining obligations of insolvent companies are paid by the Florida Workers' Compensation Insurance Guaranty Association (FWCIGA),[4] which is ultimately covered by assessments against all workers' compensation policyholders in Florida.[5]

Limited Availability of Wrap-Up Policies With Large Deductibles
Though remote, the possibility currently exists that a Florida wrap-up policy for a nonpublic construction project could provide for a large deductible for workers' compensation claims. Among the criteria to be met would be that each entity covered under the wrap-up policy has a

[2] Before the availability of large deductible programs, retrospective rating plans were the dominant rating plan for large employers. Under a retrospective rating plan, the final premium paid by the employer is based on the actual loss experience of the employer during the policy, plus insurer expenses and an insurance charge. If the employer controls the amount of claims, it pays lower premiums.
[3] *See* Office of Insurance Regulation, Analysis of HB 343, (Feb. 11, 2013) (on file with the Senate Committee on Commerce and Tourism).
[4] FWCIGA's purpose is to provide a mechanism for the payment of covered claims, to avoid excessive delay in payment, and to avoid financial loss to claimants in the event of the insolvency of a member insurer. *See* http://www.fwciga.org.
[5] For additional discussion on employer and insurer solvency concerns and large deductible policies *see* "Workers' Compensation Large Deductible Study," NAIC/IAIABC Joint Working Group Study (March 2006), *available at* http://www.naic.org/store/free/WCD-OP.pdf (last visited March 28, 2013).

minimum workers' compensation standard premium of $500,000.[6] Satisfaction of this requirement would likely be rare, as every entity on a construction project would need to be an extremely large employer and small subcontractors would be excluded.

III. Effect of Proposed Changes:

Section 1 creates s. 627.4138, F.S., regarding wrap-up insurance policies for nonpublic construction projects. The bill defines a "wrap-up insurance policy" to mean a consolidated insurance program or series of insurance policies issued to the nonpublic owner or general contractor (or a combination of the two) of a construction project through a consolidated insurance program that provides workers' compensation coverage, various forms of liability coverage, or a combination of such coverages for the contractors and subcontractors working at a specified contracted work site of the construction project.

The bill authorizes a wrap-up insurance policy to include a deductible of $100,000 or more for workers' compensation claims if all of the following prerequisites are met:

- The workers' compensation minimum standard premium calculated on the combined payrolls for all entities covered by the wrap-up policy exceeds $500,000;
- The estimated cost at each specified contracted worksite is $25 million or more;
- The insurer pays the first dollar of a workers' compensation claim without a deductible;
- The reimbursement of the deductible by the insured does not affect the insurer's obligation to pay claims;
- The insurer complies with all workers' compensation filing requirements under ch. 440, F.S., for losses, including those below the deductible limit;
- The insurer files unit statistical reports with the National Council on Compensation Insurance (NCCI) which show all losses, including those below the deductible limit;
- Any unit statistical reports needed to calculate an experience modification factor for the insured are filed with the NCCI;
- The insurer complies with NCCI aggregate financial calls, detail claim information calls, unit statistical reporting, and other required calls; and
- The insurer establishes a program for having the first-named insured, whether the owner, the general contractor, or a combination thereof, reimburse the insurer for losses paid within the deductible.

Section 2 provides an effective date of July 1, 2013.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

[6] *See* Rule 69O-186.006, F.A.C.

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:

The Office of Insurance Regulation anticipates the bill will greatly expand the use of large deductibles for wrap-ups. Currently, workers' compensation wrap-up construction project policies require that the general contractor and all sub-contractors on the project receive individual policies because the workers' compensation law prohibits any employer from being added as an "additional insured" on any other employer's policy.[7]

The bill safeguards the payment of workers' compensation benefits to injured workers by requiring the insurer to pay the first dollar of a workers' compensation claim without applying the deductible and specifying that the failure of a policyholder to reimburse an insurer for the deductible does not affect the insurer's obligation to pay claims.

C. Government Sector Impact:

According to the Florida Workers' Compensation Insurance Guaranty Association (FWCIGA), large deductible policies were a factor in three of the seven liquidations that occurred from January 2009, through June 2012, requiring reimbursement from the association. The FWCIGA incurred losses of approximately $49 million due to the three companies. If the FWCIGA requires additional funds to pay its obligations, it will levy assessments on workers' compensation insurers, who are authorized to include assessments as an appropriate factor in the making of rates.[8]

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

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[7] *Supra* note 3.
[8] Florida Workers' Compensation Insurance Guaranty Association, *Workshop on Proposal for Large Deductible Legislation* (March 12, 2013) (presentation available on file with the Senate Committee on Commerce and Tourism).

VIII. Additional Information:

A. Committee Substitute – Statement of Substantial Changes:

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

CS/CS by Commerce and Tourism Committee on April 1, 2013:
The committee substitute:

- Clarifies that a wrap-up insurance policy can include a deductible of $100,000 or more for workers' compensation claims if, in addition to other requirements, the estimated cost at each specified contracted worksite is $25 million or more; and
- Clarifies that the insurer must have a program for having the first-named insured reimburse the insurer for losses paid within the deductible.

CS by Banking and Insurance Committee on March 14, 2013:
The CS specifies that a wrap up policy is a consolidated insurance program for non-public construction projects and makes the owner and general contractor of a non-public construction project responsible for reimbursing an insurer for workers' compensation costs paid within the policy's large deductible.

B. Amendments:

None.