SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

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

BILL: CS/SB 1806

SPONSOR: Fiscal Policy Committee and Senator Thomas

SUBJECT: Workers' Compensation Insurance

DATE: April 19, 1999 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Emrich	Deffenbaugh	BI	Fav/1 amendment
2.	Hayes	Hadi	FP	Fav/CS
3.				
4.				
5.				

I. Summary:

The Committee Substitute specifies what constitutes the workers' compensation insurance premium which is used as the basis for collecting assessments from insurers to fund the Workers' Compensation Administrative Trust Fund (WCATF) and the Special Disability Trust Fund (SDTF) under the workers' compensation law, chapter 440, F.S. Specifically, the bill defines the term "net direct written premiums" to mean all premiums arising from workers' compensation policies issued by an insurer and includes ceded reinsurance premiums as well as the full premium value of the policy before applying any deductible amounts. The bill also changes the effective date of the assessment rates from July 1 to January 1 of each year.

The Committee Substitute delays the effective date until July 1, 2000, for Sections 1,2, and 3 of the bill and requires the Division of Workers' Compensation to report to the Legislature by January 1, 2000, an estimate of the amount of the reduction in the assessment rate needed to fund the anticipated expenses of administration for the division which result from the legislation.

Effective July 1, 1999, the Committee Substitute amends section 627.914, F.S., to:

- Delete the requirement that insurers report certain workers' compensation data to the Department of Insurance, which is duplicative of data that is submitted to the department by statistical agents for the insurers;

- Changes the date for a rating organization to submit an aggregate compilation of payrolls, premium, losses, and expense for all companies from April 1 to July 1 of each year, which will improve the ability to insure quality data and make the data more current;

The Committee Substitute creates a Workers' Compensation Rating Law Study Commission and provides for the study group to report its findings and recommendations to the President of the

Senate and the Speaker of the House of Representatives by December 15, 1999. The bill provides an appropriation of $100,000 for the Study Commission.

This bill substantially amends the following sections of the Florida Statutes: 440.02, 440.49, 440.51, and 627.914.

II. Present Situation:

The Division of Workers' Compensation within the Department of Labor and Employment Security is responsible for the administration of Florida's workers' compensation system. Pursuant to s. 440.51, F.S., insurance companies, individual self insured employers, group self insured funds, commercial self insured funds, assessable mutuals, and the Workers' Compensation Joint Underwriting Association are subject to the Workers' Compensation Administration Trust Fund (WCATF) assessment on "net premiums collected," or net premiums imputed for self-insurers, not to exceed 4 percent. The present assessment rate is 2.75 percent which will generate income to the WCATF of $74 million for fiscal year 1998-99.

Revenues generated through the WCATF assessment are used to primarily fund expenses for the Division of Workers' Compensation, the Division of Safety, the Office of Judges of Compensation Claims, a portion of the Agency for Health Care Administration, the Bureau of Workers' Compensation Fraud within the Department of Insurance, and a percentage surcharge to General Revenue. The total funding for these entities for fiscal year 1998-99 is $116,184,628.

The Special Disability Trust Fund (SDTF), also called the "second injury" fund, was created in 1955 as an incentive for employers to hire employees with pre-existing physical impairments (s. 440.49, F.S.). If an employee with a pre-existing injury was injured on the job, employers could make a claim to the SDTF to have a portion of the workers' compensation claim reimbursed by the SDTF. The funding for the SDTF also comes from assessments on workers' compensation carriers (insurers, group self-insurance funds, and individual self-insured employers) and is based on "net premiums written" by carriers. The present assessment rate is 4.52 percent (which is also the statutory cap) which will generate income to the SDTF of $122 million for fiscal year 1998-99.

Historically, carriers have reported all premiums to the division for these two assessments, including premiums ceded to reinsurers. However, recently some carriers have interpreted the phrase "net premiums" to *exclude premiums ceded to reinsurers*. As a result of this interpretation, some carriers are reporting less premium for purposes of assessment and are requesting refunds of past assessments. According to the Division of Workers' Compensation, more than $40 million in refunds covering the current year and past years have been requested.

Additionally, in recent years many large individually self-insured employers have discontinued their self-insured status and purchased large-deductible insurance policies from an insurer. According to the division, the number of individually self-insured employers has been reduced from approximately 670 in 1996 to approximately 460 as of February 1999. Also, according to the division, the market share of individually self-insured employers has dropped from 39.7 percent in 1996 to 28 percent as of July 1998. The impetus for the switch to a large-deductible policy is the manner in which assessments for the SDTF and WCATF are calculated. Each of these assessments are based on premium -- either the net premium written or the net premium collected by an insurer (for insurance companies) or the premium a self-insurer would pay if insured (for individually self-insured employers). Switching to a large-deductible policy from self-insured status eliminates the assessment for the previously self-insured employer. Instead, the assessment is paid by the employer's new insurer based on the direct premium written, which is much smaller than the normal premium calculated for the individually self-insured employer because of the size of the deductible.

According to the division, the premium base, which serves as the basis for SDTF and WCATF assessments, has been reduced as a result of self-insured employers moving to large-deductible policies and the fact that ceded reinsurance premiums have been excluded by some carriers. The premium assessment base has steadily declined in recent years, from the high of $3.61 billion in 1994, to $2.813 billion in 1998. The 1999 premium base is estimated to be $2.714 billion, which is a $900 million reduction within the last 5 years. Division representatives maintain that this continuing downward spiral will result in a shortfall in funding for the administration of the workers' compensation system and may lengthen the amount of time necessary to pay off SDTF claims. (See Economic Impact, below, for more detail.)

The Division of Risk Management within the Department of Insurance operates the casualty claims coverage program which provides workers' compensation coverage for all state employees. In January 1998, the division purchased a large deductible workers' compensation policy provided by North American Specialty Insurance Company at an annual premium of $598,000 (January 1, 1999-2000). North American pays the assessment to the SDTF and WCATF based on this annual premium. According to representatives with the Risk Management Division, prior to purchasing this large deductible policy, they estimate that the division would have paid a total assessment to both the trust funds of $4.8 million for fiscal year 1997-98.

Under current law, the effective date of the assessment rates as determined by the Division of Workers' Compensation is July 1 of each year. This date has caused problems for businesses and local governments because it is applied retroactively by the division, and businesses and governments have not been able to plan in advance for their workers' compensation program expenses. The division cannot actually determine the expenses for the WCATF, and thus the assessment rate, until several months *after* July because the audit of the Fund is not completed until the end of September. Notification to workers' compensation insurers and local governments of their assessment rate is not completed until October.

In 1997, legislation was enacted which terminated the claims against the SDTF, effective for injuries occurring on or after January 1, 1998, (ch. 97-262, L.O.F.). At that time it was estimated that the undiscounted liability of the Fund was $4.05 billion. (Undiscounted liability represents the cumulative amount of the claim payments at the time that the final claim payment is expected to be made.) As of December 31, 1998, the undiscounted liability was $3.60 billion, while the discounted liability of the Fund was $1.59 billion, using a 6 percent discount rate. (Discounted liability represents the current value of the losses adjusted to reflect investment income from December 31, 1998, to the final assumed payment.) According to a recent actuarial analysis by Milliman and Robertson, based on the assumption that the current 4.52 percent assessment rate would not be changed, it is estimated that the SDTF would experience a positive cash flow in fiscal year 2013-2014. At that time, the current pay lag would have been eliminated and claims could be reimbursed as they are audited and approved.

Last year, the Legislature passed a measure which provided a mechanism to create a financing corporation for the purpose of transferring and privatizing the liabilities of the SDTF to a qualified entity (ch. 98-199, L.O.F.). The bill created a Special Disability Trust Fund Commission to determine whether the state could realize savings by privatizing the responsibilities and liabilities of the fund. The Commission has not yet made this determination and is in the process of preparing requests for proposals.

III. Effect of Proposed Changes:

Section 1. Amends s. 440.02, F.S., 1998 Supplement, to define the term "net direct written premiums" to mean premiums arising from workers' compensation policies issued by an insurer in Florida, adjusted for premiums arising from endorsements, cancellations, audits, retrospective rating plans, and dividends, but *without deduction* for ceded reinsurance premiums transferred to another insurer for reinsurance purchased. Additionally, when insurers report deductible policy premium for the purposes of the Special Disability Trust Fund (SDTF) under s. 440.49, F.S., and the Workers' Compensation Administrative Trust Fund (WCATF) under s. 440.51, F.S., the full policy premium value must be reported *prior* to the application of deductible discounts or credits.

Section 2. Amends s. 440.49, F.S., 1998 Supplement, relating to the SDTF, to provide that net direct written premiums by carriers and the amount of premiums calculated by the Division of Workers' Compensation (DWC) for self-insured employers, in accordance with the *National Council of Compensation Insurance Basic Manual for Workers' Compensation and Employers Liability Insurance for Self-Insurers* (1999 Edition), are the basis for computing the amount to be assessed as a percentage of net premiums.

Section 3. Amends s. 440.51, F.S., relating to the WCATF, to provide that the DWC shall, before November 15 in each year, determine the anticipated expenses of administration for the next calendar year to determine the amount to be assessed against each carrier in order to provide for the expense of administrating the workers' compensation provisions. The determined assessment rate shall be announced by the DWC and becomes effective January 1. However, for fiscal year 2000-2001, the DWC shall impose an interim rate to facilitate the transition period. Additionally, the net direct written premiums by carriers and the amount of premiums calculated by the DWC for self-insured employers are the basis for computing the amount to be assessed.

Section 4. Amends s. 627.914, F.S., to delete that insurers report certain workers' compensation data to the Department of Insurance, which is duplicative of data that is submitted to the department by statistical agents for the insurers; changes the date for a rating organization to submit an aggregate compilation of payrolls, premium, losses, and expense for all companies from April 1 to July 1 of each year; provides technical changes to transfer the reference to self-insurance funds from subsection (5) to subsection (4) to conform to the fact that the Department of Insurance now regulates self-insurance funds, while individual self-insureds are still regulated by the Department of Labor; deletes subsection (6) regarding a report to the Legislature in 1986.

Section 5. Requires the Division of Workers' Compensation to report to the Legislature by January 1, 2000, an estimate of the amount of the reduction in the assessment rate needed to fund the anticipated expenses of administration for the division which result from the amendments contained in this act.

Section 6. Provides that to the extent this act substantively changes the calculation of the premiums subject to assessment, it shall apply only to policies issued or renewed on or after its effective date.

Section 7. Creates the Workers' Compensation Rating Law Study Commission for the purpose of studying Florida's Workers' Compensation rating law and other state workers' compensation rating law alternatives; requires the analysis to consider prior approval full rate, lost costs, and open competition rating laws and their impact on rates and premiums; provides for membership; requires appointments to be made by July 1, 1999, and the commission's first meeting must be held by August 15, 1999.

Section 8. Provides duties and responsibilities for the Workers' Compensation Rating Law Commission; requires that the study group must report its findings and recommendations to the President of the Senate and the Speaker of the House of Representatives by December 15, 1999.

Section 9. Provides an appropriation of $100,000 from the Insurance Commissioner's Regulatory Trust Fund for implementing the provisions related to the Workers' Compensation Rating Law Study Commission.

Section 10. Provides that sections 7, 8, and 9 of this act shall take effect upon becoming law.

Section 11. Provides an effective date of July 1, 2000, except as otherwise provided in this act.

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:

See Private Sector Impact, below.

B. Private Sector Impact:

Sections 1, 2, and 3, take effect July 1, 2000, which provide a definition of "net written premium" and revise the method of determining assessments for funding the Workers' Compensation Administration Trust Fund and the Special Disability Trust Fund. According the Division of Workers' Compensation, if these changes were effective on July 1, 1999, the bill would have resulted in an increase in the amount of premiums reported for assessment purposes from an estimated $2.714 billion in the 1999 fiscal year to approximately $3.2 to $3.4 billion the following year. Representatives with the division state that this increase in premium would have translated into a reduction in the WCATF assessment percentage from 2.75 percent to approximately 2.02 to 2.2 percent.

In addition, since the bill is expected to increase the assessment premium base for the SDTF, the division estimates that the gross revenue generated for the SDTF would be increased from the current $122 million to between $150 and $155 million. As a result of this revenue increase, the SDTF may be able to pay the existing claims in a shorter period of time.

Absent the bill, the Division of Workers' Compensation would probably be able to raise enough funds to administer the workers' compensation system by simply raising the assessment percentage for the WCATF for the next couple of years. (Currently the WCATF assessment rate is 2.75 percent, although its cap is 4 percent; the SDTF assessment rate is presently 4.52 percent, which is the statutory cap.) However, the division estimates the premium base would eventually shrink to the point where, given the current statutory assessment caps, the division would be unable to raise enough money to administer the workers' compensation system. This bill will enable the division to generate the assessments necessary to administer the workers' compensation program without reaching the 4 percent (WCATF) cap. Additionally, the bill will ensure a more equitable distribution of the expenses associated with the two trust funds over all insurance companies, self insurance funds, and self insured employers.

The effect of this bill could result in an increase in assessments for carriers who currently do not report premiums ceded to a reinsurer or who write large-deductible policies. However, those carriers not ceding premiums to a reinsurer or currently reporting premiums ceded to a reinsurer could receive lower assessments as a result of this bill. As a result, the bill's effect on carriers' assessments depends on the individual carrier's practice.

By providing a July 1, 2000, effective date, and requiring the Division to estimate its impact by January 1, 2000, businesses and governments should be able to estimate their and plan for their workers' compensation program expenses.

The amendments to s. 627.914, F.S., which delete certain reporting requirements for insurers will result in cost savings to insurers.

C. Government Sector Impact:

See Private Sector Impact, above, for the impact on the Division of Workers' Compensation.

According to the Division of Risk Management which provides workers' compensation for all state employees, if the bill's changes were effective for FY 1999-2000, this bill would have had the effect of increasing the state's workers' compensation insurance by approximately $6,788,000 for that fiscal year. Pursuant to the workers' compensation policy the Division of Risk Management has with North American Specialty Insurance Company, the division would be responsible for paying the $6.7 million assessment or any other assessment amount that is imposed on the insurer.

VI. Technical Deficiencies:

None.

VII. Related Issues:

The provisions of Sections 7, 8, and 9, which create the Workers' Compensation Rating Law Study Commission, are also contained in CS/SB 2338 by the Banking and Insurance Committee and Senator Clary. See the staff analysis to that bill for additional information about Florida's workers' compensation rating laws.

VIII. Amendments:

None.