

2013

Workers'
Compensation
Annual Report



FLORIDA OFFICE OF
INSURANCE REGULATION

Kevin M. McCarty, Insurance Commissioner

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Executive Summary

Subsection 627.211(6), Florida Statutes, mandates the Office of Insurance Regulation (Office) provide an annual report to the President of the Senate and the Speaker of the House of Representatives that evaluates competition in the workers' compensation market in the state. The report is to contain an analysis of the availability and affordability of workers' compensation coverage and whether the current market structure, conduct and performance are conducive to competition, based upon economic analysis and tests. The report must also document that the Office has complied with the provisions of section 627.096, Florida Statutes, which require the Office to investigate and study the data, statistics, schedules, or other information as it finds necessary to assist in its review of workers' compensation rate filings.

As mandated, the analysis presented in this report finds the following:

1. Based on a comparative analysis across a variety of economic measures, the workers' compensation market in Florida is competitive.
 - a. The workers' compensation market in Florida is served by a large number of independent insurers and none of the insurers have sufficient market share to exercise any meaningful control over the price of workers' compensation insurance.
 - b. The Herfindahl-Hirschman Index (HHI) - a measure of market concentration - indicates that the market is not overly concentrated.
 - c. There are no significant barriers for the entry and exit of insurers into the Florida workers' compensation market and based on the record of new entrants and voluntary withdrawals with no market disruptions, the Florida workers' compensation market is competitive, well capitalized and robust.
2. Of the six most populous states, Florida is one of only two where private market insurers, rather than a state-sponsored residual market dominate the market. This degree of private activity indicates that coverage should be generally available in the voluntary market. The residual market is small, suggesting that the voluntary market is absorbing the vast majority of demand.
3. Reforms to section 440.34, Florida Statutes, which affected attorney's fee provisions, were a significant factor in the decline of workers' compensation insurance rates and the reforms continue to impact Florida's workers' compensation rates.¹ It is also the case, however, that most of the improvements resulting from these legislative changes may have been realized as there have been four rate increases after seven years of decreases.

¹ In *Murray v. Mariner Health*, (Florida Supreme Court October 23, 2008), the Florida Supreme Court held that the statute in the first part of the workers' compensation law did not limit attorneys' fees under a separate subsection (3) of the law, and therefore a lawyer representing a workers' compensation claimant is entitled to a "reasonable fee." House Bill 903 was passed into law during the 2009 Legislative Session. It restored the cap on attorney fees and clarified related statutory language that the Florida Supreme Court had determined to be ambiguous. As a result, workers' compensation rates have decreased even more.

4. Medical cost drivers, particularly in the areas of hospital inpatient, hospital outpatient and ambulatory surgical centers (ASC) are noticeably higher in Florida than a countrywide average. Legislative reform in the reimbursement of these services could produce substantial savings for Florida employers. The total saving would vary from 7.5% to 8.3% based on the percentage of Medicare that was adopted.
5. Affordability within the Florida Workers' Compensation Joint Underwriting Association, Inc. (FWCJUA), which is the residual market, has been an ongoing issue. Senate Bill 50-A enacted in 2003 and House Bill 1251 enacted in 2004 addressed affordability in the voluntary and residual market respectively and both markets remain stable. It is worth noting, however, that over this last year both policy count and premium at the FWCJUA increased significantly, though it still remains a very small portion of the overall workers' compensation market.
6. The Office is in compliance with the requirements of section 627.096, Florida Statutes.

Purpose and Scope

Subsection 627.211(6), Florida Statutes, mandates:

“The office shall submit an annual report to the President of the Senate and the Speaker of the House of Representatives by January 1 of each year which evaluates competition in the workers’ compensation insurance market in this state. The report must contain an analysis of the availability and affordability of workers’ compensation coverage and whether the current market structure, conduct, and performance are conducive to competition, based upon economic analysis and tests. The purpose of this report is to aid the Legislature in determining whether changes to the workers’ compensation rating laws are warranted. The report must also document that the office has complied with the provisions of s. 627.096 which require the office to investigate and study all workers’ compensation insurers in the state and to study the data, statistics, schedules, or other information as it finds necessary to assist in its review of workers’ compensation rate filings.”

To meet these mandates, this report provides analysis of the following areas:

1. The competitive structure of the workers’ compensation market in Florida by comparing select key financial performance ratios, the number of insurers actively participating in the market along with their respective market positions, and the number of insurers entering and exiting the market.
2. The availability and affordability of workers’ compensation insurance in Florida. This includes an analysis of rate increases in Florida’s admitted market, as well as the rating structure extant in the FWCJUA.
3. The market structure in Florida, which includes the market concentration in Florida compared with other states, and entry and exit of insurers from the Florida market.
4. Documentation of the Office’s compliance with section 627.096, Florida Statutes, by investigating all workers’ compensation carriers operating in Florida.
5. A comparison of pure loss costs for the ten largest workers’ compensation class codes for Florida compared to the other states using the National Council of Compensation Insurance (NCCI) as their statistical rating organization.

Summary of the 2012 Annual Report

The 2012 Workers' Compensation Annual Report was the ninth report resulting from the statutory mandate, and reached the same general conclusions as the previous annual reports. Specifically, the report showed that, during 2011:

- Florida's workers' compensation insurance market contained a large number of independent insurers, none of which had enough market share to individually exercise market control in an uncompetitive nature.
- The HHI indicated that Florida's market was not overly concentrated, and consequently exhibited a reasonable degree of competition.
- There were no significant barriers for entry and exit of insurers into and from the Florida workers' compensation insurance market.
- The residual market is small relative to the private market indicating that the voluntary market offers reasonable availability.
- There may be some small segments of the market which have difficulty obtaining workers' compensation insurance, including small firms and new firms.

The 2012 annual report does note that the Office approved a rate increase of 6.1% on November 2, 2012.

The 2013 Workers' Compensation Annual Report continues to examine the workers' compensation insurance market from the same perspective and provides the HHI to compare Florida's market concentration versus the other major workers' compensation markets by providing a comparative analysis of key market characteristics among the six most populous states. The five other states are: California, New York, Texas, Illinois, and Pennsylvania.

Additionally, the 2013 Workers' Compensation Annual Report presents findings on the cost drivers related to a fourth consecutive rate increase in the Florida market granted in 2013.

Snapshot of the Florida Workers' Compensation Market in 2012

Previous annual reports have documented the relative health and competitiveness of the Florida workers' compensation market following the legislative reforms implemented in 2003. This trend is evident in 2012 as well, though there may be some reason for caution moving forward.

In 2012, 245 privately-owned insurers actively wrote workers' compensation insurance in Florida. In total, these private sector insurers wrote \$2,013,465,276 of coverage. Moreover, during 2012, four insurers entered the Florida workers' compensation market, either as new companies or by adding the workers' compensation line of business to their certificate of authority. During 2012, five insurers voluntarily exited the Florida market. These new entrants and voluntary withdrawals had no disruptive impact on the marketplace, as should be the case in a competitive market.

Ten Largest Insurers

The largest insurer, Bridgefield Employers Ins. Co., as measured by premium written in the chart below, had 12.20% of the market, and the largest ten insurers had a cumulative 43.78% of the market. This spread of premium across insurers suggests that no one firm can be seen to have an overly dominant impact on the market. These insurers are:

Company Name	State of Domicile	Workers' Compensation Direct Premium Written	Market Share (%)	Cumulative Market Share (%)
Bridgefield Employers Ins Co	FL	\$245,671,477	12.20	12.20
Zenith Ins Co	CA	119,003,149	5.91	18.11
FCCI Ins Co	FL	115,836,805	5.75	23.86
Twin City Fire Ins Co	IN	72,040,987	3.58	27.44
RetailFirst Ins Co	FL	70,873,514	3.52	30.96
Amerisure Ins Co	MI	63,758,610	3.17	34.13
FFVA Mut Ins Co	FL	54,936,776	2.73	36.86
Technology Ins Co Inc	NH	52,663,272	2.62	39.47
Liberty Ins Corp	IL	44,780,877	2.22	41.70
Charter Oak Fire Ins Co	CT	41,994,269	2.09	43.78

Four of these companies are domiciled in Florida; the remaining six are domiciled in the eastern, mid-western and western United States. This shows that the Florida workers' compensation market is not served exclusively by Florida-only companies; there is some geographical diversification.

The ten largest companies also display a range of product line diversification. Some, such as Bridgefield and RetailFirst write all, or nearly all, of their business in the Florida workers' compensation market, while the others write a broader mix of workers' compensation in other

states, other lines of business, or both. The table below highlights the relative size of the Florida workers' compensation market to each of the ten largest firms portfolio mix of business. This mix of business by geography and line of business adds to the stability of the Florida market.

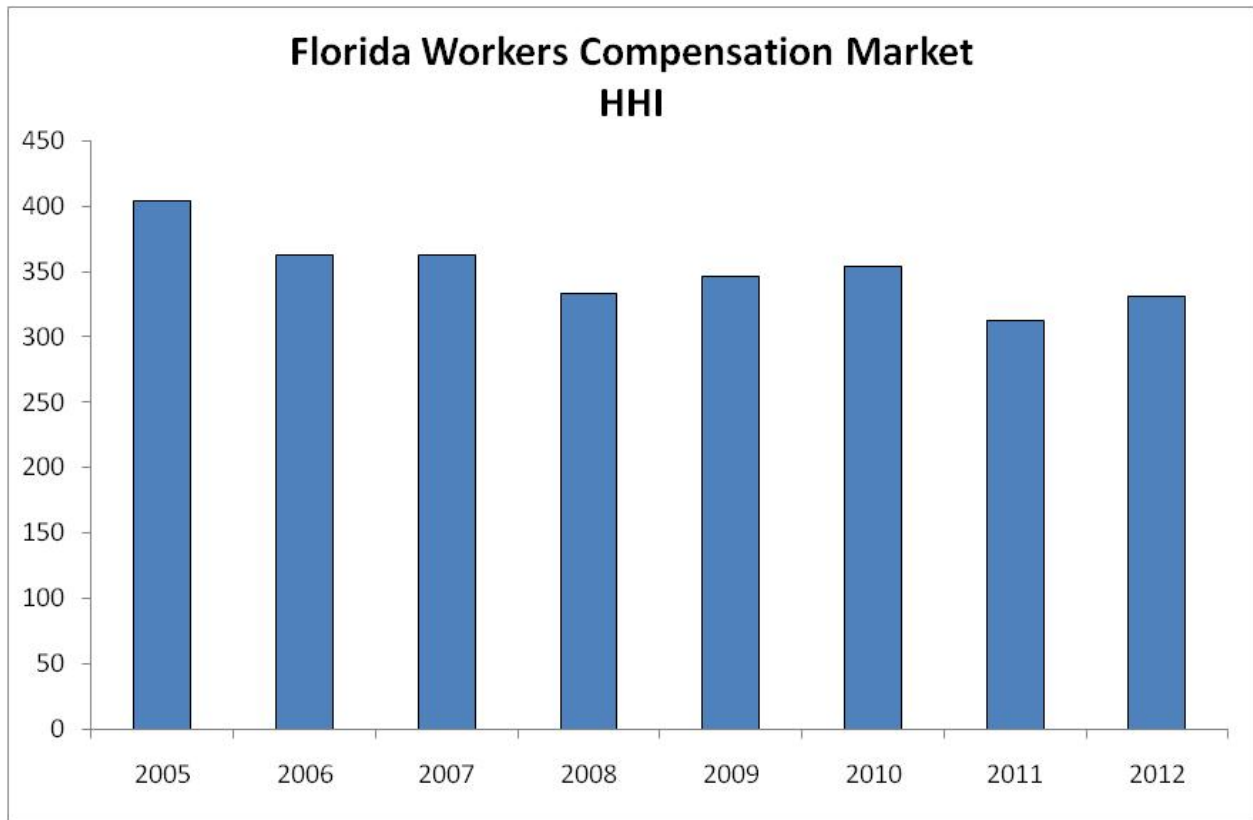
Company	Florida Workers' Comp Premium Written	Florida Workers' Comp/All Workers Comp Premium Written	Florida Workers' Comp /All Premium Written	All Workers' Comp/All Premium Written
Bridgefield Employers Ins Co	\$245,671,477	93.61%	93.61%	100.00%
Zenith Ins Co	119,003,149	23.20%	22.34%	96.30%
FCCI Ins Co	115,836,805	73.20%	48.32%	66.01%
Twin City Fire Ins Co	72,040,987	9.89%	5.30%	53.60%
RetailFirst Ins Co	70,873,514	100.00%	100.00%	100.00%
Amerisure Ins Co	63,758,610	39.23%	21.61%	55.09%
FFVA Mut Ins Co	54,936,776	56.37%	56.37%	100.00%
Technology Ins Co Inc	52,663,272	13.11%	10.76%	82.11%
Liberty Ins Corp	44,780,877	4.77%	2.28%	47.85%
Charter Oak Fire Ins Co	41,994,269	12.57%	3.08%	24.54%

Measured Market Concentration: The Herfindahl-Hirschman Index

A widely recognized measure of market concentration can be applied to the Florida workers' compensation market. The Herfindahl-Hirschman Index (HHI) is a calculation designed to determine market concentration and first appeared in A.O. Hirschman's *National Power and Structure of Foreign Trade* published in 1945.

The HHI calculation is straightforward. The measured market share of every company operating in the identified market is squared. The highest index value is then defined as 10,000 (100 percent squared --- a monopoly), and the lowest outcome is close to zero. The U.S. Department of Justice (DOJ) uses this index when researching acquisitions and mergers for compliance with the anti-trust legislation, most notably, the Sherman Anti-Trust Act of 1890. DOJ considers a result of less than 1,000 to be a "competitive" marketplace. Results of 1,000 to 1,800 are considered "moderately concentrated." Results over 1,800 are considered "highly concentrated," and consequently, not very competitive.

The calculated HHI for the Florida workers' compensation insurance market in 2012 is 330.93. Following DOJ guidelines, this measure suggests a competitive market. Moreover, the Florida workers' compensation market has become progressively more competitive following the legislative reforms at least as given by the HHI measure. As the chart on the next page shows, the calculated HHI of 404 in 2005 has declined to the 2012 value of 330.93.



Underwriting Strength

An important measure of the health of an insurance market is the underwriting performance of the insurers in the market; that is, the combination of pricing, risk management and application of effective underwriting guidelines that contribute to a viable and sustainable market. Two commonly used measures are employed in this report; the loss ratio (defined as direct losses incurred divided by direct premiums earned) and a broader measure that includes direct losses incurred and defense cost containment costs (DCC) incurred as a percentage of direct premiums earned. Ratios approaching or exceeding 100 for either measure are not considered profitable in their core business.

For the Florida workers' compensation market in 2012, these aggregate ratios are:

- Direct Loss Ratio 55.53%
- Direct plus DCC Ratio 62.89%

While there is natural year-to-year variation in these ratios and too much importance should not be given to year over year changes, it is worthwhile to note that both of these measures are higher than reported for the Florida market in 2011 (41.3% and 48.6% respectively), but lower than reported for the Florida market in 2010 (66.1% and 76.1% respectively).

Self-Insurance Funds

In addition to the private market described above, which writes over 96% of the workers' compensation insurance in Florida, coverage is also provided by the residual market, as represented by the FWCJUA and through self-insurance funds (SIFs)².

Comparison of the Six Major Market States

Florida is a large economically and demographically diverse state. To provide meaningful context on the Florida workers' compensation market as described above, it is instructive to provide comparison to similarly situated states. This section of the report focuses on the six most populous states, and excludes SIFs. In addition to Florida, the five most populous states used here are California, Texas, New York, Illinois and Pennsylvania.

The table below highlights some of the key comparisons between the Florida workers' compensation insurance market and those of the other five states considered in this peer group.

State	Direct Premium Written 2012	Rank By Direct Premium Written	HHI	Number of Entities Collecting Premium in 2012	Largest Provider	Largest Provider Market Share (%)	State Population Rank*
CA	\$9,003,018,342	1	274.17	232	State Fund	10.04	1
NY	4,754,647,391	2	1743.31	275	State Fund	40.88	2
IL	2,600,631,024	3	106.50	326	Private Insurer	3.97	5
PA	2,528,539,637	4	157.40	325	State Fund	7.59	6
TX	2,445,019,290	5	1451.65	283	[1]	37.07	3
FL	2,013,465,276	6	330.93	245	Private Insurer	12.20	4

[1] The largest writer is Texas Mutual Insurance, an insurer created originally by the Texas Legislature in 1994. It was granted independence in 2001, but still responsible for the residual market.

*Based on July 2011 estimates from the U.S. Bureau of Census

² "Self-Insurance" groups are a broadly defined group of entities that include group self-insurance funds, commercial self-insurance funds and assessable mutual organizations. By the early 1990s, self-insurance funds were a dominant part of the Florida workers' compensation insurance market, capturing more than half of the voluntary market. Legislative reforms in 1993 transferred the regulation of group self-insurance to the Department of Insurance, which later became the Office of Insurance Regulation. This legislative change occurred concurrently with the formation of the FWCJUA. Together, these two changes transformed the Florida workers' compensation insurance market as self-insurance funds began converting into insurance companies. In 1994 there were 35 defined self-insurance funds, but by 2000 there were only four of these entities. There were four group self-insurance funds at the start of 2010 but the largest fund, Florida Retail Federation Self Insurer's Fund converted to a stock company in November 2010. As a result of legislation passed in 2009, the Florida Rural Electric SIF is governed by section 624.4626, F.S., which does not require the Fund to file an annual statement with OIR. Thus, the Florida Rural Electric SIF is no longer included in this report. See Appendix A for the Florida Statutes that govern SIFs that are not subject to OIR regulation. The remaining SIFs are the Florida Citrus, Business, & Industries Fund and the FRSA Self Insurer's Fund.

As might be expected, there is a positive correlation between state population and workers' compensation insurance written premiums. Note however, that while Florida is the fourth largest state by population, it ranks sixth in terms of total workers' compensation premium written.

In terms of the number of insurance entities writing in each market, Florida ranks fifth with 245 private firms (not considering the FWCJUA or the two SIFS identified earlier). By this measure, Florida has a comparable number of entities operating within its borders relative to other populous states.

From the perspective of market competition, the six states are compared using their calculated HHI's. For the purposes of this report, comparing the HHI among states is difficult, as the data for the self-insurance trust funds for other states must be calculated. Moreover, while some states have their state funds report financial information to the National Association of Insurance Commissioners (NAIC), other states, such as Florida with its FWCJUA, do not. This report includes a calculation of Florida's HHI without the SIFs included to be comparable to the other populous states. Of the six most populous states, California (274.17), Illinois (106.50) and Pennsylvania (157.40) have lower HHI indices than Florida (330.93), suggesting that Florida has one of the four most competitive workers' compensation markets of the major populous states.

Dominant Firms and Competition

A particularly interesting comparison is to review the largest competitor in each of the six most populous states to determine if there is a "dominant firm." Notice that only Florida and Illinois have markets where the largest insurer is a private entity. In the other four states, the largest provider is either a state fund, or in the case of Texas, a mutual company that was originally created by the state and is still responsible for the provision of residual market workers' compensation insurance.

Bridgefield Employers Insurance Co.'s business in Florida has the largest market share of any private insurer in the six most populous states. However, it should be noted that at 12.20% of the market, it is unlikely that this is enough of a market share to create an uncompetitive marketplace.

Underwriting Strength in the Most Populous States

Finally, to provide context for the Florida market results presented earlier, a comparison of aggregate loss ratios across the six most populous states was conducted. The results are presented below:

State	Direct Loss Ratio	Direct Loss +DCC
CA	73.24%	84.82%
IL	72.15%	79.66%
NY	85.14%	89.43%
PA	69.29%	76.83%
TX	47.71%	53.00%
FL	55.53%	62.89%

For 2012, Florida's aggregate loss ratios, using either measure, are the second lowest among the six most populous states. As such, the Florida market compares favorably to the other five largest states as a healthy, likely profitable market for insurers.

Workers' Compensation Rates

A comprehensive slate of reforms was passed into law during the 2003 Legislative Session. The package known as Senate Bill 50-A (Chapter 2003-412 Laws of Florida) continues to dramatically impact Florida's workers' compensation insurance rates. Some of these reforms included a reduction (cap) in attorneys' fees, tightening of construction industry requirements, doubling impairment benefits for injured workers, increasing the medical fee schedule, and eliminating the Social Security disability test.³

Subsequently, workers' compensation rates had declined by 64.7% in Florida as of July 1, 2010. In 2000, Florida had the highest workers' compensation insurance rates in the country. In 2003, the Office approved a 14% rate reduction, with an additional reduction of 5.2% in 2004. These annual rate reductions continued unabated through the rate reduction of 6.8% that took effect on January 1, 2010. The rate changes during this seven-year period include the three largest decreases ever in Florida, namely -18.6% for 2009, -18.4% for 2008, and -15.7% for 2007. These seven filings represent the largest consecutive cumulative decrease on record in Florida for workers' compensation rates – dating back to 1965. Since July 1, 2010, NCCI has filed four consecutive annual rate increases.

Before the reforms, Florida consistently ranked as the first or second state with the highest workers' compensation rates in the country. Post-reform, Florida dropped out of the top ten rankings. By 2008, Florida dropped to 28th place and by 2010 Florida had fallen to 40th place. The latest ranking based on the January 1, 2012 rates shows that Florida has risen to 29th highest but is still below the national median rate. This means there are 22 states with a lower average rate than Florida.

On August 15, 2013, NCCI proposed an overall workers' compensation rate level increase of 1.0% for the voluntary market to be effective January 1, 2014. The Office conducted a hearing on October 1, 2013, and heard testimony from NCCI, industry experts and the public about NCCI's initial rate filing. On October 22, 2013, Commissioner Kevin McCarty issued an order finding the 1.0% rate increase in NCCI's filing was not justified. The order requested NCCI to modify its original filing and resubmit it. On October 28, 2013, NCCI resubmitted an amended filing in accordance with the Office order. The Commissioner approved the amended filing for an average rate increase of 0.7% on October 30, 2013. With this rate increase, Florida's rates are still 56% below what the rates were prior to the 2003 reforms.

With the implementation of the 0.7% increase, the rate impact for the main industry groups will be as follows in the chart listed on the next page:

³ "Florida Cracks Down on Construction Sites without Workers' Compensation Insurance," *Best Wire*, August 2, 2005, which utilizes information from an earlier article in *BestWire*, July 15, 2003.

Industry Sector	Rate Adjustment 01/14	Cumulative since 2003
Manufacturing	-3.5%	- 53.9%
Contracting	+3.2%	- 57.6%
Office and Clerical	+0.0%	- 58.3%
Goods and Services	+0.8%	- 54.4%
Miscellaneous	+0.6%	- 54.1%
TOTAL	+0.7%	-56.0%

The rate increase has been justified and should keep Florida competitive with neighboring states. However, Florida's recent advantage over other states in attracting employers based on the lowest workers' compensation rates has disappeared.

Cost Drivers for Workers' Compensation

At the rate hearing on October 1, 2013, NCCI presented testimony regarding the potential savings that could be realized by addressing some of the cost drivers legislatively. NCCI compared the medical cost distributions for Florida versus all states combined to show that Florida has a higher portion of cost paid for drugs, hospital inpatient, hospital outpatient and ambulatory surgical center (ASC). Substantial rate reductions would occur if the cost in Florida were brought in line with other states for drugs, inpatient hospital, outpatient hospital and ASC reimbursements rates.

A summary of the NCCI findings and the impact on workers' compensation costs was provided and is summarized in the Table below.

Medical Cost Distributions

Florida vs. Countrywide

	Florida ¹	Countrywide ²	Difference
Physicians	31.8%	39.8%	-8.0%
Drugs	15.1%	11.2%	+3.9%
Supplies	5.8%	7.6%	-1.8%
Other	1.8%	4.4%	-2.6%
Hospital Inpatient	18.6%	15.0%	+3.6%
Hospital Outpatient	18.8%	16.7%	+2.1%
Ambulatory Surgical Center	8.1%	5.3%	+2.8%
Total	100%	100%	0%

¹ Source: Derived from data provided by the Florida Division of Workers' Compensation (FLDWC) for Service Year 2012

² Source: Derived from NCCI Medical Data Calls for Service Year 2012 for the following 37 states:

AK, AL, AR, AZ, CO, CT, DC, FL, GA, HI, IA, ID, IL, IN, KS, KY, LA, MD, ME, MO, MS, MT, NC, NE, NH, NM, NV, OK, OR, RI, SC, SD, TN, UT, VA, VT, and WV

As highlighted in the Table, recent experience shows medical costs in Florida to be above the countrywide average in four key categories: drugs, hospital inpatient, hospital outpatient and ASC.

Physician Drug Dispensation

Since 2008, more than 95% of the reimbursement dollars spent on repackaged drugs in Florida has been the result of physician dispensing; and, in 2011, 97.9% of the dollars spent were the result of physician dispensing.⁴

A by-product of repackaging/relabeling has been that the average unit price of a repackaged drug can be many times that of the drug in its non-repackaged form.⁵ A July 2012 study released by the Workers Compensation Research Institute (WCRI) titled *Physician Dispensing in Workers' Compensation* shows that in states like Florida and Illinois, physician dispensed drugs have been priced between 60% and 300% more than what is charged by pharmacies.

A number of states have addressed this developing issue by placing either an outright ban on physicians dispensing drugs (Massachusetts, New York, Texas, Montana, and Utah) or by placing price controls and using other regulatory tools to address the price disparity between repackaged and non-repackaged drugs (Arizona, Colorado, Georgia, and South Carolina).

In Florida, the drug repackaging issue was partially addressed by passing SB 662. Other options to reduce drug costs are:

- Restrict physician dispensing
- Lower reimbursement rate
- Lower dispensing fee
- Introduce drug formulary
- Strengthen prescription drug monitoring program

Hospital and Surgical Center Reimbursement

Florida has a charge-based system for reimbursing hospital outpatient services. Currently, these services are, by statute, reimbursed at 75% of “usual and customary charges” for non-scheduled surgeries and 60% for scheduled surgeries⁶. The term “usual and customary charge” is not defined by Florida statute. Several attempts to provide clarity to the meaning of “usual and customary” charges by administrative rule have yet to be successful. A new approach was approved at the Three-Member Panel meeting held on January 9, 2013, but it is still progressing through administrative rulemaking.

⁴ See *Florida Department of Financial Services, Division of Workers' Compensation, 2012 Results and Accomplishments*, at page 117.

⁵The per unit markup can be as much as 679% according to the NCCI testimony provided at the August 18, 2011 workers' compensation premium rate hearing. This same testimony was again provided at the November 16, 2011 Three-Member Panel meeting.

⁶ Subsection 440.13(12)(a) and (b), F.S.

Other states have moved away from charge-based reimbursement and have adopted other methodologies that are seen to provide more predictability and offer greater opportunity for cost containment. States such as Oregon, California, Colorado, North Dakota, South Carolina, Tennessee and Washington use the Medicare Outpatient Prospective Payment System (OPPS) as a basis for reimbursement. NCCI estimates that rates could be reduced by 4.9% if Florida reimbursed hospital outpatient care and ASC's at 120% of Medicare. At 140% of Medicare, the rate could be reduced by 4.5%.

Florida workers' compensation law provides that the maximum reimbursement allowances for inpatient hospital care shall be based on a schedule of per diem rates to be approved by the Three-Member Panel no later than March 1, 1994.⁷ If Florida were to reimburse hospital inpatient care at 120% of Medicare, workers' compensation rates could be reduced by 3.4% according to NCCI. At 140% of Medicare, the rate could be reduced by 3.0%.

More details on all the medical issues can be found in the Three-Member Panel Biennial Report for 2013. Using Medicare as a basis for hospital inpatient, hospital outpatient and ASC's will reduce workers' compensation rates substantially depending on the percentage above Medicare that is used. At 140% of Medicare the total savings would be 7.5% (-3.0%+-4.5%). At 120% of Medicare, the total savings would be 8.3% (-3.4%+-4.9%).

Comparative Rates and Premiums

Comparative rates and premiums between states for the workers' compensation line of business is complicated by several factors. State law varies as to coverage and payment for claims, tort restrictions, and the basis for rate determination. Nonetheless, such a comparison, noting the above difficulties, can be useful.

In 2013, the Office requested from NCCI a comparison of loss cost estimates for the ten largest class codes of workers' compensation insurance in force in the Florida market with the loss costs for the same class codes in the other 36 jurisdictions for which NCCI is the statistical rating agent. The pure loss cost was considered the metric of choice chosen as it is calculated in a consistent manner across class codes and jurisdictions. Final allowed rates begin with the loss costs as a foundation, and are then modified for risk loads and profit factors in different manners across jurisdictions.

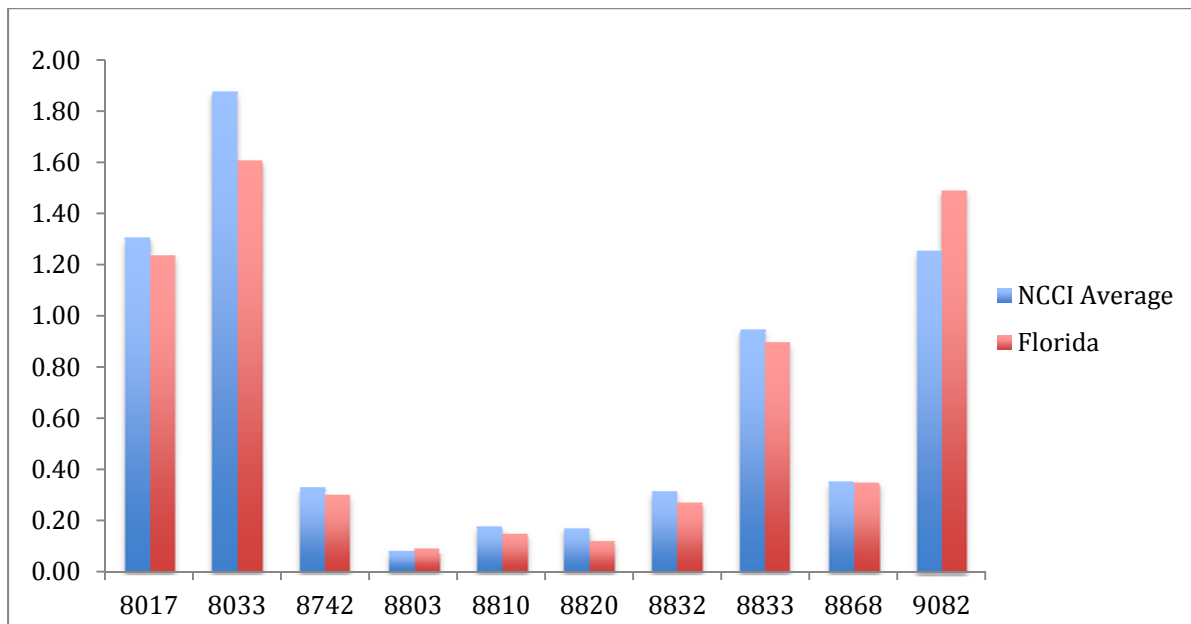
Initially, there are two commonly used definitions of calculating the "largest" class codes; by exposure amounts (e.g. the amount of insured exposure in dollars) and by policy count. The analysis below is repeated for each definition.

When measured by exposure, the ten largest class codes, the average loss cost across NCCI jurisdictions based on the most recent available data as of December 2012, Florida's loss cost and Florida's rank among jurisdictions (one being highest, 37 being lowest) are reported on the next page:

⁷ Subsection 440.13(12)(a), Florida Statutes

Comparative Pure Loss Cost: Largest Class Codes by Exposure				
Class Code	Class Description	NCCI Average	Florida	Florida Rank
8017	STORE: RETAIL NOC	1.31	1.24	21
8033	STORE: MEAT, GROCERY AND PROVISION STORES COMBINED-RETAIL NOC	1.88	1.61	26
8742	SALESPERSONS OR COLLECTORS-OUTSIDE	0.33	0.30	22
8803	AUDITOR, ACCOUNTANT, OR COMPUTER SYSTEM DESIGNER OR PROGRAMMER - TRAVELING	0.08	0.09	9
8810	CLERICAL OFFICE EMPLOYEES NOC	0.18	0.15	20
8820	ATTORNEY-ALL EMPLOYEES & CLERICAL, MESSENGERS, DRIVERS	0.17	0.12	29
8832	PHYSICIAN & CLERICAL	0.31	0.27	23
8833	HOSPITAL: PROFESSIONAL EMPLOYEES	0.95	0.90	18
8868	COLLEGE: PROFESSIONAL EMPLOYEES & CLERICAL	0.35	0.35	17
9082	RESTAURANT NOC	1.25	1.49	10

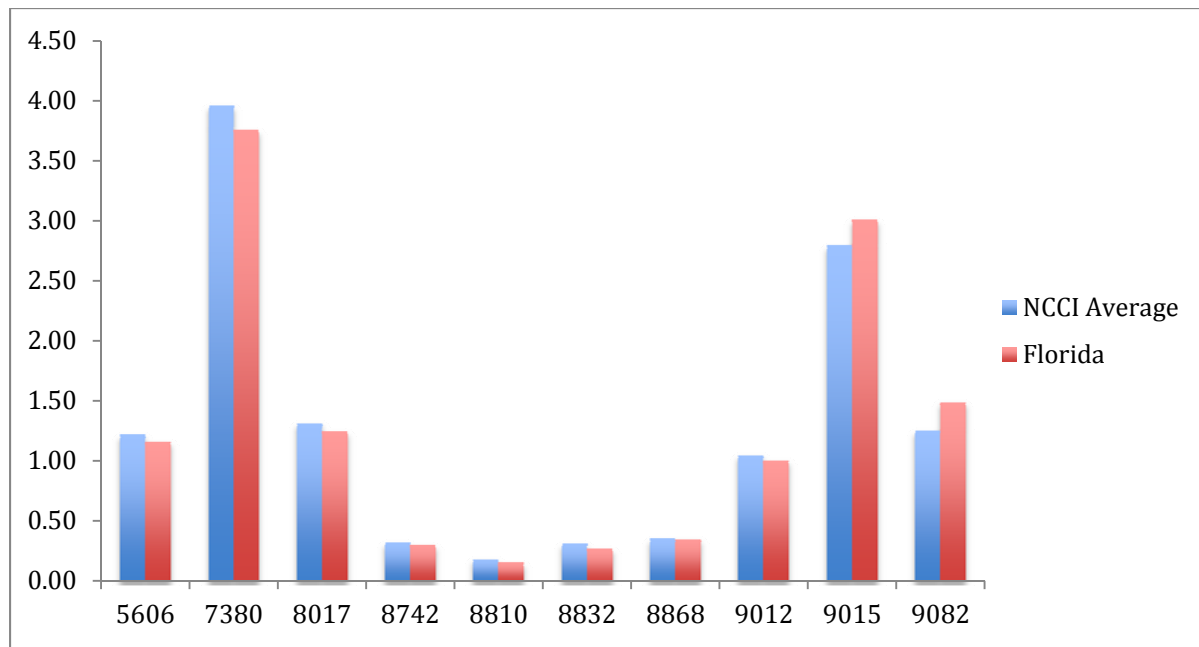
Graphically, this data shows that in eight of the ten classes, Florida's loss cost is below the average, as it was in 2011, but unlike 2010's analysis in two cases Florida's loss cost is higher than the average in two classes and the rankings are generally somewhat lower. While there is natural year-to-year variation in loss costs, these comparisons will be watched for future trend.



When the same analysis is done using the results generated by defining the ten largest classes by policy count, the results are similar to the above, but more pronounced.

Comparative Pure Loss Cost: Largest Class Codes by Policy Count				
Class Code	Class Description	NCCI Average	Florida	Florida Rank
5606	CONTRACTOR--PROJECT MANAGER, CONSTRUCTION EXECUTIVE, CONSTRUCTION MANAGER OR CONSTRUCTION SUPERINTENDENT	1.22	1.16	19
7380	DRIVERS, CHAUFFEURS, MESSENGERS AND THEIR HELPERS NOC-COMMERCIAL	3.96	3.76	18
8017	STORE: RETAIL NOC	1.31	1.24	21
8742	SALESPERSONS OR COLLECTORS-OUTSIDE	0.33	0.30	22
8810	CLERICAL OFFICE EMPLOYEES NOC	0.18	0.15	20
8832	PHYSICIAN & CLERICAL	0.31	0.27	23
8868	COLLEGE: PROFESSIONAL EMPLOYEES & CLERICAL	0.35	0.35	17
9012	BUILDING OR PROPERTY MANAGEMENT - PROPERTY MANAGERS AND LEASING AGENTS & CLERICAL, SALESPERSONS	1.04	1.00	20
9015	BUILDING OR PROPERTY MANAGEMENT - ALL OTHER EMPLOYEES	2.80	3.01	12
9082	RESTAURANT NOC	1.25	1.49	10

In 2012, Florida's loss cost was higher than the NCCI average in seven of the ten classes, and the rankings were again lower than in 2011.



Florida Workers' Compensation Joint Underwriting Association (FWCJUA)

One of the most significant indicators of an availability problem in an insurance market is the size of the residual market mechanism. In Florida, the FWCJUA is the market of last resort. Only employers that cannot find coverage in the voluntary market are eligible for coverage in the FWCJUA. Thus, the size of the FWCJUA is a measure of availability of coverage in the voluntary market.

While the FWCJUA has had significant increases in the number of policies and in written premium for 2012 and 2013, the FWCJUA is still a very small portion of the total workers' compensation market in Florida. NCCI presented data at its State Advisory Forum that showed Florida had the smallest residual market as a percent of premium for the 26 states except for Idaho that were included in the calendar year 2012 analysis. The NCCI presentation also showed that the FWCJUA had fewer policies than all 26 states except Idaho and the District of Columbia.

The Florida Workers' Compensation Insurance Plan (FWCIP) was the residual market for Florida until the FWCJUA was created on January 1, 1994. All insurance companies writing workers' compensation in Florida funded the FWCIP. If there was a deficit in the FWCIP, then those workers' compensation carriers were assessed to cover the deficit. In 1993, the FWCIP issued 48,430 policies with written premiums of \$328 million. The FWCJUA in contrast has varied from 13,933 policies to 773 policies, with written premium varying from \$77.5 million to \$1.2 million. At the end of October 2013, the FWCJUA had 1,636 policies on its book with corresponding premiums of \$29.4 million. The FWCJUA's written premium as a percent of total market has not exceeded 2% since 1995 and has been below 1% for most years.

The rate differential for FWCJUA versus the voluntary market rates has varied from 1.25 to 3.278 and was 1.429 prior to the reforms. There are surcharges in addition to the rate differential that affect the total premium paid by FWCJUA policyholders. There was a 99% surcharge applied to Sub-plan "C" premiums in excess of \$2,500, an Assigned Risk Adjustment Program (commonly known as "ARAP") surcharge for experience rated policies and a \$475 flat surcharge added to every policy. The creation of Tiers 1, 2 and 3 by House Bill 1251 resulted in a restructuring of the rates and surcharges used by the FWCJUA. Tier 1 is for employers with good loss experience; Tier 2 is for employers with moderate loss experience and non-rated new employers; and, Tier 3 is for employers not eligible for Tiers 1 or 2. Specific eligibility requirements can be obtained from the FWCJUA.

As of January 1, 2014, the premium for Tier 1 is 5% above the voluntary rates, Tier 2 is 20% above voluntary and Tier 3 is 75% above (1.75 times the voluntary rates), plus the ARAP surcharge applies for Tier 3. Additionally, all three tiers have a flat surcharge of \$475. Tier 3 policyholders have a burden that Tiers 1 and 2 do not have. Tier 3 policies are assessable if premiums are not sufficient to cover losses and expenses.

It is unrealistic to expect that an actuary's best estimate, which is a prediction of future contingent events, will always coincide with future results. It is understood and usually explicitly

acknowledged that the results for a particular year can be higher or lower than the actuary's estimate. The consequences of the results being higher or lower than the estimate affect the actuary's judgment and ultimate selections.

In a situation where an insurance entity has substantial financial resources, it may be acceptable for the actuary's estimate to be high half of the time and low half of the time, as long as over time the predictions coincide with the average result. In other words, if there is a billion dollars in surplus, the company may not be concerned if the actuary's estimate is \$50 million high or low in a particular year as long as it balances over a number of years.

If, however, there is only \$10 million in surplus, the company cannot afford for the estimate to be \$10 million lower than the actual because they will be bankrupt. In this latter situation, the consequences of being low are more important than the consequences of being high and this will impact the degree of conservatism that is appropriate in the actuary's selection.

The FWCJUA has been in a situation where the consequences of reserving too low or having rates that are too low (i.e. retroactive assessments to policyholders) have been greater than the consequences of reserves being too high or rates too high. If the rates are too high, there may be some complaints from policyholders and others but, if there are assessments due to the rates being too low, every policyholder is affected, even those whose policy has expired. At the extreme, some of the policyholders could face severe financial distress or even be put out of business as a result of the assessment.

As a result of these circumstances, the degree of conservatism used in determining FWCJUA rates and surcharges has contributed to the level of rates needed. The main contributor to the FWCJUA rates, however, has been the level of expenses and losses incurred. Both of these were adversely impacted when the volume of FWCJUA business decreased in the late 1990s. As a result of all these factors and others, the FWCJUA rates have historically been very high in comparison to the residual markets in other states, but other states have increased the surcharges in their residual market such that several states now have higher surcharges than the FWCJUA.

Currently, the Tier 1 and Tier 2 rates for most employers are much more affordable than the previous sub-plans A, B and C. However, Tier 3 rates remain high compared to the residual market in other states.

Having the goal of a small residual market is desirable, but it needs to be balanced with having an affordable residual market. The FWCJUA has been small in comparison to the total voluntary market from 1997 to the present. This occurred during a period when the FWCJUA rates were not very affordable to many employers and the voluntary market was very competitive. The high premiums in the FWCJUA discouraged many employers from even applying to the FWCJUA. These employers decided to close their business, go without coverage (which may be unlawful), or sought the services of a Professional Employer Organization (PEO). Coupled with a very competitive market by insurers who aggressively sought new policyholders, this created an extremely small residual market.

Ultimately, availability should not be an issue as coverage can be found in either the voluntary

market or the FWCJUA, although affordability may well remain an issue for employers utilizing the FWCJUA.

Composition of the Buyer

Analysis of the workers' compensation market is typically done at a high level, either at the insurer level or in market aggregates. The reality is that the workers' compensation market is segmented based on a number of characteristics, such as size of employer, type of industry, past experience of the employer or the lack of experience. The market for large employers versus small employers can be markedly different. The market for construction risks is different from employers with office workers. New businesses typically face noticeable frictions in obtaining coverage owing to their lack of historical experience, which can be a measure of not only the insurance exposure but also the credit worthiness of the insured.

Employers with a combination of these characteristics can sometimes be difficult to place in the voluntary market. In some cases, coverage is related to the availability of agents in the local area and the number of insurers the local agents represent. The Division of Workers' Compensation, within the Department of Financial Services, monitors and enforces compliance with the workers' compensation laws.

In fiscal year 2012-2013, the Division's Bureau of Compliance conducted 34,150 on-site inspections of an employer's job-site or business location to determine compliance with workers' compensation coverage requirements. The Bureau also issued 2,858 enforcement actions against non-compliant employers, which resulted in \$7.2 million in insurance premium generated and 13,143 in new employees covered by workers' compensation insurance, a 44% increase from the previous fiscal year. The Bureau conducted 66 free training sessions and 34 webinars on workers' compensation coverage, compliance requirements and workplace safety for over 2,900 employers statewide.

The Bureau of Workers' Compensation Fraud, within the Division of Insurance Fraud, made 418 workers' compensation fraud-related arrests for fiscal year 2011-2012, an increase of 53% from the previous fiscal year.

PEO's have been a part of the Florida workers' compensation market since the early 1990s, especially for small employers. The PEO market is not, however, always without challenges regarding availability of coverage from workers' compensation insurers (see the *Workers' Compensation Large Deductible Study*, National Association of Insurance Commissioners/International Association of Industrial Accident Boards and Commissions Joint Working Group, March 2006).

A survey, conducted by the Florida Association of Professional Employment Organizations (FAPEO) in 2010 found that they provided more than 69,000 companies with more than 900,000 work-site employees, representing a payroll in excess of \$25 billion.⁸

⁸The Florida Association of Professional Employer Organizations (FAPEO) [2010 Census Brochure](#)

Market Structure, Conduct and Performance to Promote Competition

The previous sections of this report do not suggest any obvious impediments to a workers' compensation market found to be reasonably competitive. This section concentrates on the ability of the market to promote competition.

Mandatory Rating Plans

Before discussing the methods workers' compensation insurers use to compete in the marketplace, it is useful to summarize the rating and premium pricing variations that result from the mandatory rating plans currently in effect. The following rating plans are required of all insurers in the state of Florida:

- Experience Rating Plan – This plan recognizes differences between individual employers by comparing the actual experience of an individual employer with the average expected experience of employers in the same classification. The plan produces an experience modification factor that may increase or decrease premiums. An employer is eligible for this program if the average annual premium is at least \$5,000.
- Premium Discounts by Size of Policy – The premium discount plan adjusts the employer's premium to reflect that the relative expense of servicing large premium policies as a percent of premium is less than that for small premium policies. For example, the policy issuance costs for a \$200,000 policy may be higher than those for a \$20,000 policy, but the costs are not ten times as high.
- Drug-Free Workplace Premium Credit – A 5% premium credit provided to employers that certify the establishment of a drug-free workplace program.
- Employer Safety Premium Credit – A 2% premium credit provided to employers that certify the establishment of a safety program.
- Florida Contracting Classification Premium Adjustment Program - A premium credit is provided for policies with one or more contracting classifications that pay above average hourly wages. The credit amount increases as the average wage paid increases. The credit is calculated based on payroll and hours worked information submitted by the employer to NCCI.
- Small Deductibles - For a reduced premium, the employer agrees to reimburse the insurer for each claim up to the deductible amount and the carrier covers benefits for each claim above the deductible amount. Small deductibles range from \$500 to \$2,500 and are required by section 440.38(5), Florida Statutes. An insurer may refuse to issue a policy with a deductible based on the financial stability of an employer.
- Coinsurance - For a reduced premium, the employer agrees to reimburse the insurer 20% of each claim up to \$21,000. This option is required by section 440.38(5), Florida Statutes. An insurer may refuse to issue a policy with a coinsurance amount based on the financial stability of the employer.

Optional Plans Used by Insurers to Compete Based on Price

Insurers use the following plans to compete on price:

- 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 experience, the carrier’s experience, and other factors.
- Deviations – Section 627.211, Florida Statutes, allows insurers to file a uniform percentage increase or decrease that is to be applied to all rates an insurer charges or to rates for a particular class or group of classes of insurance.
- Intermediate Deductibles - For a reduced premium, the employer agrees to reimburse the insurer for each claim up to the deductible amount and the carrier covers the amount of the claim above the deductible amount. Intermediate deductibles range from \$5,000 to \$75,000.
- 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.
- 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% of policies written or renewed in each calendar year.
- Retrospective Rating Plans – 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, they pay lower premiums. Before there were large deductible programs, retrospective rating plans were the dominant rating plan for large employers.
- Waiver of Subrogation - For an additional premium, the insurer may waive its right of recovery against specifically named parties liable for injury covered by the policy.

Non-Price Competition

In addition, insurers compete in ways unrelated to the determination of premium such as:

- Offering premium payment plans that vary the amount of money paid initially and through installments;
- Demonstrating the availability and effectiveness of specialized loss control;
- Demonstrating the effectiveness of their claims handling including fraud detection;
- Paying higher agent commissions or providing other incentive programs, and/or;
- Emphasizing policyholder service in auditing, policy issuance or certificates of insurance.

Deviations

In the mid 1980’s, the use of deviations as a means of competing was commonplace. From 1983 to 1985, over 40% of the market was written at deviated rates. However, by 1989 only 9% of the market was written at deviated rates. After the two-year legislatively required moratorium (1990

and 1991) on deviations, the use of deviations ceased to be a meaningful factor in the workers' compensation marketplace in Florida.

Despite the changes in section 627.211, Florida Statutes, made by chapter law 2004-82 (Senate Bill 1926) to allow for easier approval of deviations, only three insurers have been approved for a new deviation since the law became effective on July 1, 2004 and one of these was the transfer of an existing deviation. The Office has disapproved five deviations since 2004 for lack of justification. One insurer has renewed its prior deviation and one insurer will let their deviation expire on 12/31/2013. Consequently, on January 1, 2014, there will only be three insurance companies with a deviation in Florida (two of the deviations are downward 10% and the other one is downward 5%).

Large Deductibles

In the early 1990's, insurers approached the Department of Insurance (Department) about filing a rating plan for large employers (defined as having \$500,000 in standard premium) that would be more flexible in how the premium would be determined. The justification for the flexibility would be based on the following general concepts:

- The rating plan would be used only for very large employers. These employers would generally be eligible to be individually self-insured.
- Rating is similar to rating for excess insurance that is purchased by individual self-insureds.
- The minimum deductible is \$100,000 and could be in the millions. Thus, the employer would be responsible for the vast majority of claims.

The Department ultimately agreed to these type plans with restrictions that were incorporated in Administrative Rule 69O-189.006 (formerly 4-189.006).

As large deductible programs have been implemented, there has been a dramatic shift in premiums. The typical large deductible policy will have a deductible credit that can range from 30% to 90%. Thus, the premiums paid by employers and reported by insurers will be a fraction of premiums paid for other rating plans. This means premiums in the annual statement and premiums reported for assessments and taxes are much lower than they were previously.

As the volume of large deductible policies written in Florida has increased, the effect has been to lower the base for assessment and taxes such that section 440.51(1)(b), Florida Statutes, have been revised to require premiums to be reported without the deductible credit.

An ancillary effect of large deductibles has been the movement for very large employers to cease being individually self-insured and to buy an insurance policy from an insurance company with a large deductible program.

In recent insolvencies, there have been problems with large deductible policies and the lack of collectible collateral. This will result in the Florida Workers' Compensation Insurance Guaranty Association (FWCIGA) paying over \$50 million that will ultimately be assessed to all workers' compensation policyholders in the state of Florida. The FWCIGA established a workgroup to

study this problem and make recommendations for corrective action. The FWCIGA Board has adopted the report of the workgroup and will be making recommendations for legislative changes to strengthen the collateral requirements and limit the size of the deductible assumed by policyholders.

Conclusion

Based on the number of entities and market shares of actively writing companies in the market, the number of entities entering and exiting the market and the financial performance of the entities in the market, Florida's workers' compensation market can readily be characterized as a competitive market.

Availability does not appear to be a significant concern in the aggregate. The residual market is small, suggesting that the voluntary market is absorbing the vast majority of demand. While not without risk, the growth of the use of PEOs among smaller employers has, as well, helped availability by making coverage affordable.

For an employer, availability is not particularly important if the coverage is not affordable. As of January 1, 2014, the voluntary market rates have declined by 56% since reform legislation was passed. There is some concern, however, about the direction of workers' compensation rates in Florida and the ability of the state to retain its important economic competitive advantage in this area.

The economic impact of the legislative reforms of 2003 have delivered the desired result and lowered costs dramatically in the state. It is likely, however, that the impact of these reforms has reached its limit.

Workers' compensation insurance rates have risen in each of the last four years. Medical cost drivers, particularly in the areas of drug costs, hospital inpatient, hospital outpatient and ASC's are noticeably higher in Florida than a countrywide average. SB 662 was passed to address the drug repackaging issue. NCCI estimates that substantial savings could be achieved with legislative reforms for the reimbursement of hospital inpatient care, hospital outpatient care, and ASC care. The total saving would vary from 7.5% to 8.3% based on the percentage of Medicare adopted.

Office Certification of Compliance with Section 627.096, Florida Statutes

Section 627.096, Florida Statutes, was created in 1979 as part of the “wage loss” reform of the workers’ compensation law. This statute has three basic requirements as it pertains to this report:

1. An investigation and study of all insurers authorized to write workers’ compensation in Florida. The Office has accomplished this objective by its thorough review of the quality and integrity of the data submitted in the most recent NCCI filing.
2. A study of the data, statistics or other information to assist and advise the Office in its review of filings made by or on behalf of workers’ compensation insurers. Also, there are public hearings regarding the NCCI filing which further allow an opportunity for third parties to register their opinions and input.
3. The statute gives the Financial Services Commission the authority to require all insurers to submit data to the Office. The NCCI has been collecting workers’ compensation data in Florida for more than 50 years; therefore, the Office has contracted with NCCI to perform these statistical services for the state of Florida.

Appendix A
Florida Statutes Governing Workers' Compensation Self-Insurance Funds
Not Subject to Office Regulation

Section 624.4622 – Local government self-insurance funds

- Must be comprised entirely of local elected officials
- Limited financial reporting only

Section 624.46226 – Public housing authorities self-insurance funds

- Must be a public housing authority as defined in Chapter 421
- Has a governing body which is comprised entirely of commissioners of public housing authorities who are members of the fund
- Limited financial reporting only

Section 624.4623 – Independent educational institution self-insurance funds

- Must be an independent nonprofit college or university accredited by the Commission on Colleges of the Southern Association of Colleges and Schools or independent nonprofit accredited secondary educational institution
- Has a governing body which is comprised entirely of independent educational institution officials
- Limited financial reporting only

Section 624.4625 – Corporation not for profit self-insurance funds

- Must be a not for profit corporation located in and organized under Florida law
- Must receive at least 75% of revenue from local, state or federal governmental sources
- Has a governing body which is comprised entirely of officials from not for profit corporations that are members of the fund
- Limited financial reporting only

Section 624.4626 – Electric cooperative self-insurance fund

- Must be an electric cooperative organized pursuant to Chapter 425 and operates in Florida
- Must subscribe to or be a member of a rating organization prescribed in section 627.231
- Has a governing body comprised of a representative from each member of the fund
- No reporting requirements



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