

Summary of 2014 Workers Compensation Report by OIR

Summary of 2014 Workers Compensation Annual Report Released December 23, 2014

**ISSUED BY OFFICE OF INSURANCE REGULATION
DEPARTMENT OF FINANCIAL SERVICES
STATE OF FLORIDA
KEVIN M. MCCARTY, INSURANCE COMMISSIONER**

The Office of Insurance Regulation (Office) is mandated by subsection 627.211(6), Florida Statutes, to provide an annual report to the President of the Senate and the Speaker of the House of Representatives evaluating competition in the workers' compensation market in the 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. It must also document that the Office has complied with the provisions of Section 627.096, Florida Statutes, which requires 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.

The finding of the 2014 Workers' Compensation Annual Report, released December 23, 2014 by the Office stated that Florida's workers' compensation market is competitive, well capitalized, and robust, with lower amounts of loss. In a nutshell, the 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; the Herfindahl-Hirschman Index (HHI) - a measure of market concentration - indicated the market is not overly concentrated; and there are no significant barriers for the entry and exit of insurers into the Florida workers' compensation market.

In 2013, 254 privately-owned insurers actively wrote workers' compensation insurance in Florida. In total, these private sector insurers wrote \$2,296,680,613 of coverage. 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 and three insurers voluntarily exited the Florida market. These events had no disruptive impact on the marketplace, illustrating its competitiveness.

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The largest insurer, Bridgefield Employers Ins. Co., had 11.34% of the market, and the largest 10 insurers had a cumulative 42.62% of the market. This would suggest that no one firm had an overly dominant impact on the market. The report noted that six (6) of the market's ten (10) largest writers are now based in Florida, up from four the year before, writing 28% of the premiums.

The 10 largest companies also displayed a range of product line diversification. For example, Bridgefield, RetailFirst, and Comp Options 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. This mix adds to the stability of the Florida market. Liberty Mutual Group is the largest provider of workers' compensation insurance in Florida with 16.9% of the total market based on 2013 NAIC Annual Statement data. The largest individual company in Florida, Bridgefield Employers Ins. Co., is a member of the Liberty Mutual Group. None of these groups have a prevailing impact on the market, supporting the competitive aspects of the Florida workers' compensation market.

Underwriting Strength

Underwriting performance, an important measure of an insurance market, is strong and getting even stronger. Florida's loss ratios – the amount of direct loss relative to direct earned premium – are second only to Texas among the big states. The report also showed positive movement since last year among different classes of workers in loss costs – the amount of the rate used to pay actual claim expenses. For the Florida workers' compensation market in 2013, the aggregate ratios were Direct Loss Ratio (50.77%) and Direct plus Defense Cost Containment Ratio (57.10%). Both of these measures are lower than reported for the Florida market in 2012 (55.53% and 62.89%, respectively).

Self-Insurance Funds

The private market writes more than 95% of workers' compensation in the state, making Florida one of the most competitive markets of the largest states in the country and one of only two that do not rely largely on state-created residual market entities. Coverage is also provided by the residual market, as represented by the FWCJUA, and through self-insurance funds (SIFs). However, 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 254 private firms (not considering the FWCJUA or SIFS). By this measure, Florida has a comparable number of entities operating within its borders relative to other populous states. The calculated HHI for the Florida workers' compensation insurance market in 2013 is 302.83. This measure suggests a competitive market, according to DOJ

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guidelines. This value has declined since 2005. Of the six most populous states (California, New York, Illinois, Texas and Pennsylvania), only Illinois (112.75) and Pennsylvania (168.69) have lower HHI indices than Florida. In addition, Florida is one of only two where a private market insurer is the largest insurer rather than a state-created residual market entity. This degree of private activity indicates coverage should be generally available in the voluntary market. The residual market is small, suggesting the voluntary market is absorbing the vast majority of demand.

Workers' Compensation Rates

Comprehensive reforms were passed into law during the 2003 Legislative Session. The package known as Senate Bill 50-A (Chapter 2003-412 Laws of Florida) dramatically impacted 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. As of July 1, 2010, workers' compensation rates declined in Florida by 64.7%. In 2000, Florida had the highest workers' compensation insurance rates in the country, and in 2003, the Office approved a 14% rate reduction, with an additional reduction of 5.1% effective January 1, 2005. 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 included the three largest decreases ever in Florida, (18.6% for 2009, -18.4% for 2008, and -15.7% for 2007). 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 10 rankings. By 2008, Florida dropped to 28th place and by 2010 Florida had fallen to 40th place. However, with rate increases from 2010 to 2014, Florida shows a rise to the 28th highest. However, while Florida has risen in the rankings, the average Florida rate still remains below the national median rate at 98% of the study median rate.

On August 22, 2014, NCCI proposed an overall workers' compensation rate level decrease of 2.5% for the voluntary market to be effective January 1, 2015. This was subsequently amended on September 22, 2014, to reflect a revised overall rate level decrease for the voluntary market of 3.3% which included an additional 0.8% decrease to reflect a change to the *Florida Workers' Compensation Reimbursement Manual for Hospitals*. The hospital manual was revised to update the reimbursement schedules for hospital inpatient and outpatient services, establishing maximum reimbursement allowances for certain qualifying procedure codes for hospital outpatient services and increased both the per-diem reimbursement amount and stop-loss amount for hospital inpatient services. The Commissioner approved the amended filing for an average rate decrease of 5.2% on November 12, 2014. This rate filing reflects the first annual

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decrease in rates since 2010, and with the rate decrease, Florida's rates are 58.3% below what the rates were prior to the 2003 reforms. Our rates remain competitive with neighboring states; however, the recent advantage we had over other states in attracting employers based on the lowest workers' compensation rates has disappeared.

Cost Drivers for Workers' Compensation

While costs for physicians' services and supplies in Florida are below the national average, the costs for drugs, hospital inpatient, hospital outpatient and ambulatory surgical center (ASC) services continue to be higher in Florida than the national average. The report stated that substantial rate reductions would occur if those costs were brought in line with other states. Likewise, further reform on drug repackaging by physicians would help lower costs. Legislative reform in the reimbursement of these services could produce substantial savings for Florida employers.

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 2012, 97.1% of the dollars spent were the result of physician dispensing. A by-product of repackaging/relabeling has been the average unit price of a repackaged drug can be many times that of the drug in its non-repackaged form. The Workers Compensation Research Institute (WCRI) released a study in July 2013 titled *Physician Dispensing in Workers' Compensation* showing 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 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, California, Colorado, Georgia, and South Carolina). In Florida, the drug repackaging issue was partially addressed by passing Senate Bill 662 effective July 1, 2013 which reduced rates by 0.7%. The primary cost reducing component of Senate Bill 662 linked the reimbursement rate of 112.5% for repackaged or relabeled drugs dispensed by a dispensing practitioner to the Average Wholesale Price (AWP) set by the original manufacturer of the underlying drug plus an \$8.00 dispensing fee.

Hospitals

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 surgeries. Since 2007, the Division of Workers' Compensation (Division), in conjunction with the Three-

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Member Panel has attempted to revise the *Florida Workers' Compensation Reimbursement Manual for Hospitals* in order to synchronize case law and statute relating to the calculation of "usual and customary charges" for hospital outpatient services. Effective on January 1, 2015 a 2014 edition of the manual will replace the 2006 edition. The manual was adopted by reference as part of Rule 69L-7.501, Florida Administrative Code. The revised manual included:

- Establishing MRAs for certain qualifying procedure codes for hospital outpatient services.
- For hospital inpatient services, the per-diem reimbursement amount increased at trauma centers from \$3,305 to \$3,850.33 for surgical stays, and from \$1,986 to \$2,313.69 for non-surgical stays,
- For hospital inpatient services, the per-diem rates at acute care hospitals increased from \$3,304 to \$3,849.16 for surgical stays, and from \$1,960 to \$2,283.40 for non-surgical stays, and
- For hospital inpatient services, the Stop-Loss Reimbursement threshold was increased from \$51,400 to \$59,891.34.

In March 2014, based on proposed Florida Senate Bill 1580/House Bill 1351, NCCI estimated rates could be reduced by 3.8% if Florida reimbursed hospital outpatient care at 140% of the Medicare OPPS rates. In addition, if Florida were to reimburse hospital inpatient care at 140% of the Medicare inpatient prospective payment system (IPPS) rates, workers' compensation rates could be reduced by 3.2% according to NCCI.

Workers' Compensation Court Cases

The report pointed out concerns that the state's significant gains in lowering costs from 2003 - 2010 could be eroded further, noting several pending court cases that have the potential to negatively affect workers' compensation rates in the future, to wit:

Westphal v. City of St. Petersburg. In September 2013, on rehearing en banc, the First District Court of Appeal withdrew a panel decision in which the court declared the 104-week statutory cap on temporary total disability (TTD) benefits unconstitutional and revived prior law allowing up to 260 weeks of TTD benefits. The court held that "a worker who is totally disabled as a result of a workplace accident and remains totally disabled by the end of his or her eligibility for temporary total disability benefits is deemed to be at maximum medical improvement (MMI) by operation of law and is therefore eligible to assert a claim for permanent and total disability benefits." In this case, the claimant exhausted TTD benefits without having reached MMI, creating a "gap" period wherein the injured claimant would no longer receive benefits but also not be at MMI for purposes of receiving permanent disability benefits. In its opinion, the en banc court certified this case to the Florida Supreme Court for review. The decision is still pending.

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Castellanos v. Next Door Company. In October 2013, the First District Court of Appeal declared the statutory attorney fee formula (s. 440.34, F.S.) unconstitutional and certified the question for review by the Florida Supreme Court. In this case, the judge of compensation claims, constrained by the statutory formula set forth in section 440.34(1), Florida Statutes (2009), awarded claimant's counsel an attorney's fee of only \$164.54 for 107.2 hours of legal work. The award was calculated in strict accordance with the statutory formula applied to the \$822.70 value of benefits secured by the claimant's attorney. The court upheld the constitutionality of the statute and affirmed the fee award. However, the court certified the question of "whether the award of attorney's fees in this case is adequate, and consistent with the access to courts, due process, equal protection, and other requirements of the Florida and federal constitutions." Previously in 2008, the Supreme Court found the predecessor 2003 law vague and ambiguous and vacated the law in *Murray v. Mariner Health*, holding 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. The decision is still pending.

Morales v. Zenith Insurance Company. The Eleventh Circuit in April 2013 asked the Florida Supreme Court to determine whether the family of a landscaping employee killed on the job can collect a \$9.5 million judgment from his employer's insurer, which issued a two-part policy capping workers' compensation coverage. A three-judge panel certified the question to the Florida Supreme Court, saying the issue of standing needed to be settled before it could rule on an appeal of a lower court finding that a workers' compensation exclusion in Part 2 of the liability policy barred Zenith Insurance Co. from having to cover the \$9.5 million judgment Morales won in a wrongful death action in 2005. Morales received a separate settlement from Zenith for workers' compensation benefits, but sued Zenith in 2010 to force it to pay the \$9.5 million judgment won against Lawns Nursery in the earlier wrongful death suit. If Morales has standing, the panel said, Florida's high court should also determine whether the provision in the employer liability policy, which excludes from coverage "any obligation imposed by workers' compensation ... law" operate to exclude coverage of the estate's claim against Zenith for the tort judgment, according to the opinion. While the wrongful death suit was still pending, the estate and Zenith reached a settlement in which the insurer agreed to pay the estate more than \$100,000 in workers' compensation benefits under Part 1 of the Lawns Nursery policy. The United States Court of Appeals for the Eleventh Circuit certified the following questions of Florida law: (1) does the estate have standing to bring its breach of contract claim against Zenith under the employer liability policy? (2) if

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so, does the provision in the employer liability policy which excludes from coverage “any obligation imposed by workers’ compensation . . . Law” operate to exclude coverage of the estate’s claim against Zenith for the tort judgment? and (3) if the estate’s claim is not barred by the workers’ compensation exclusion, does the release in the workers’ compensation settlement agreement otherwise prohibit the estate’s collection of the tort judgment?

In a unanimous opinion issued on December 4, 2014, the Florida Supreme held that, under Florida law, the estate has standing, but that the workers’ compensation exclusion and the release prevent it from collecting the tort judgment from Zenith. Accordingly, the court answered all three certified questions in the affirmative. Having answered the certified questions, the Florida Supreme Court returned this case to the United States Court of Appeals for the Eleventh Circuit.

Julio Cortes v. Velda Farms LLC; also captioned Florida Workers’ Advocates, Workers’ Injury Law & Advocacy Group, Elsa Padgett v. State of Florida. On August 13, 2014, the circuit court judge entered an Order on Amended Motion for Summary Final Judgment, declaring the exclusive remedy provision of the Workers’ Compensation Act (the Act) unconstitutional. According to the judge, the current workers’ compensation law is unconstitutional because it does not provide adequate benefits to injured workers giving up their right to sue and is therefore inadequate as an exclusive remedy for all injured workers. The State of Florida, through the Attorney General, appealed the circuit court decision to the Third District Court of Appeal of Florida, on August 26, 2014. On October 16, the 3rd DCA denied appellee’s motion to certify question requiring immediate resolution by the Supreme Court pursuant to Florida Rule of Appellate Procedure. The case arises in a 2012 instance where a state government worker, Elsa Padgett, sustained an on-the-job injury. After a fall, Padgett had to have a shoulder surgically replaced and was forced to retire due to complications. Padgett argued that her workers’ compensation benefits were inadequate and the law unfairly blocked her constitutional right to access the court. The decision is still pending.

Comparative Rates and Premiums

In 2014, the Office requested from NCCI a comparison of loss cost estimates for the 10 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 data showed in nine of the 10 class codes, Florida’s loss cost is below the NCCI average. This is an improvement over last year’s analysis which showed Florida’s loss cost was above or equal to the average for three class codes. When the same analysis is completed using the results generated by defining the 10 largest classes by policy count based on Florida exposure for Policy Years 2011

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and 2012, the results are similar. The data for the 10 largest classes by policy count reveals Florida's loss cost was lower than the NCCI average in eight of 10 class codes. This is an improvement over last year's analysis which showed Florida's loss cost was above or equal to the average for three class codes.

Florida Workers' Compensation Joint Underwriting Association

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 Florida Workers' Compensation Joint Underwriting Association (FWCJUA) is the market of last resort for workers' compensation insurance. 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. It is worth noting, however, that over the last several years both policy count and premium at the FWCJUA increased significantly, though it still remains a very small portion of the overall workers' compensation market. The NCCI presentation also showed the FWCJUA had fewer policies than all states included in the analysis except Idaho, the District of Columbia, South Dakota and Alabama. Only 1.8% of Florida policyholders obtained coverage through the FWCJUA, which represents only 1.2% of the Florida voluntary market direct written premium excluding self insurance funds.

The Bureau of Workers' Compensation Fraud, within the Division of Insurance Fraud, made 477 workers' compensation fraud-related arrests for fiscal year 2013-2014, an increase of 14.1% from the previous fiscal year. Workers' compensation premium fraud being facilitated by nontraditional money service businesses or check cashing stores continues to be a major focus of the Division's Bureau of Workers' Compensation Fraud.

Conclusion

Based on the 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 is a competitive market. Availability does not appear to be a significant concern in the aggregate. The residual market is small, which could suggest that the voluntary market is absorbing the demand. The growth of PEO usage among smaller employers has helped availability by making coverage affordable. As of January 1, 2015, the voluntary market rates have declined by 58.3% since the 2003 reform legislation was passed indicating the reform has delivered the desired result and lowered costs dramatically in the state. This impact may have plateaued.

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Concerns 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 were raised.

While the workers' compensation rate filing effective January 1, 2015 decreases Florida rates, 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. NCCI estimates substantial savings could be achieved with legislative reforms for the reimbursement of hospital inpatient care, hospital outpatient care, and ASC care. Senate Bill 662 passed in 2013 partially addressed the drug repackaging issue, but other legislative options could be explored to further reduce drug costs in Florida.

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