American Insurance Association

Testimony of the

American Insurance Association

before the

Commonwealth of Massachusetts

Office of Consumer Affairs and Business Regulation

Division of Insurance

Regulatory Review Public Comment Session Pertaining to Workers' Compensation

Regulation 211 CMR 115.00

Requirements Applicable to Workers' Compensation Deductible Policies

and

Regulation 211 CMR 113.00

Requirements Regarding Workers' Compensation Insurance Deductibles

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Good morning. My name is Alison Cooper and I serve as the Vice President for the Northeast Region of the American Insurance Association (AIA). AIA is a national trade association of approximately 325 property-casualty insurers whose members write a significant portion of the workers' compensation insurance in the Commonwealth of Massachusetts. AIA appreciates the opportunity to provide our views on current workers' compensation regulations.

I will be focusing my comments exclusively on Regulation 211 CMR 113.00 – Requirements Regarding Workers' Compensation Insurance Deductibles and Regulation 211 CMR 115.00 – Requirements Applicable to Workers' Compensation Deductible Policies. AIA has previously testified before the Division of Insurance (DOI) on this issue, when the Division submitted proposed amendments to these regulations back in 2013.

In general, it is critical that the rules and regulations pertaining to large deductible policies provide maximum flexibility as they provide employers with another option to a traditional workers' comp policy. Some employers may not want to or may not qualify for a self-insured option, whereby they would be taking on all of the risk. A large deductible option allows employers to take some of the risk (the risk up to the deductible amount) and insure the rest of it. Large deductible policies thus fill an important gap in the market for certain employers.

AIA strongly supports amendments that would revise some of the current requirements for companies who seek to file a large deductible option in the Commonwealth. The current definitions section of the regulation (211 CMR 115.06) provides that the minimum allowable threshold in Massachusetts for a large deductible plan is $75,000 per occurrence. AIA strongly believes that there should be an expanded range of deductible options that insurers can offer policyholders in between the current $5,000 medium deductible and $75,000 large deductible offerings. This could be done by either increasing allowed deductibles for medium deductible plans or allowing lower deductibles within the definition of "large deductible plan." Authorizing a wider range of deductibles will allow policyholders to better tailor insurance programs to their particular needs. This would also bring Massachusetts into line with surrounding states.

AIA would also like to suggest changes to Section 211 CMR 115.06 which lays out the premium eligibility requirements for a large deductible policy. It requires varying combinations of Massachusetts and non-Massachusetts workers' compensation premium. AIA does not understand why the requirements should be linked to *Massachusetts* premium at all. In the context of large deductible policies, premium paid is an indicator of the budgetary size of the entity being insured and of the ability to absorb a certain portion of that entity's workers' compensation claims. Whether the premiums are generated in Massachusetts or in another state is irrelevant in this context. In fact, all the other New England states and New York use countrywide premium figures for determining the eligibility for large deductible policies. Under the current regulation, as well as with the proposed amendments, if $100,000 in total countrywide premium is sufficient if a policyholder generates some non-Massachusetts workers' compensation premium, then $100,000 should be sufficient for Massachusetts-only workers' compensation risks. In fact, under the current regulation, a Massachusetts-only entity with $100,000 in workers' compensation premiums would have less insurance options than an entity that generated $100,000 in workers' compensation premiums, but only a small portion of this total in Massachusetts. This section seems to discriminate against Massachusetts companies.

AIA also has concerns with Section 211 CMR 115.06(2) which requires that every workers' compensation policy include a *"reasonable aggregate deductible limit."* We believe this requirement can be detrimental to a policyholder's wishes and interests. AIA's members have encountered situations where large policyholders do not want an aggregate limit, yet are forced to accept one because of this regulation. This requirement applies even when the Massachusetts exposure is a small portion of a larger, interstate account. In these cases, the policyholder would have retained a greater portion of the risk in return for lower premiums. This mandatory aggregate limit requirement has the effect of forcing policyholders to purchase more coverage than they may want or need. AIA recommends that the regulation be changed to require carriers to ***offer*** a "reasonable aggregate deductible limit," while allowing insureds to decline this feature of the coverage, if so desired. This proposed change would give policyholders more options to tailor an insurance program to their specific needs.

We understand that the DOI has in the past raised concerns about the financial sophistication of the policyholders making the decisions on aggregate deductibles. While the industry believes a countrywide premium threshold of $500,000 should be sufficient to waive the mandatory aggregate deductible requirement, we would be willing to accept some sort of payroll threshold overlay as well.

For most class codes, the industry believes a countrywide payroll threshold of $5 million, in addition to the $500,000 countrywide premium requirement, would be sufficient to waive the mandatory aggregate deductible limit. However, for many non-construction class codes, payroll would have to be in the tens of millions of dollars before $500,000 in premium was reached. For example, a financial services firm would likely need to generate hundreds of millions of dollars in payroll before reaching $500,000 in premium. Yet it would be hard to argue that a financial services firm generating "only" $250,000, let's say, in premium, is not financially sophisticated enough to waive the aggregate deductible limit.

Therefore, we respectfully urge the DOI to waive the mandatory aggregate deductible limit requirement if a policyholder has either a combination of at least $500,000 in countrywide premium and $5 million in countrywide payroll OR simply $10 million in countrywide payroll. Meeting either one of these criteria should be a sufficient proxy for financial sophistication, evidencing that policyholder's ability to determine whether an aggregate deductible limit in its workers' compensation policy is appropriate for that entity.

Additionally, we would like to address is the possibility of combining the Large Risk Alternative Rating Option (LRARO) and a large deductible program. Massachusetts General Laws Chapter 152, Section 25A(4)(d) states, *"Premium reductions for deductibles shall be determined by the commissioner of insurance."* This statute has been previously cited by the DOI as prohibiting LRARO policies from including a large deductible option. Respectfully, the industry believes that this interpretation of the foregoing statute misses the distinction between deductible credits and retrospective adjustments under a LRARO. Deductible credits and retrospective rating

adjustments are two different components of the premium algorithm from different but not opposing rating plans and serve two different functions. A deductible credit, which is assigned a specific statistical code, is a restrictive credit for a specific risk characteristic, while a retro adjustment allows for a more flexible approach to crediting or debiting larger eligible risks based on their overall loss experience and other unique individual risk characteristics. LRARO/large deductible combinations are not filed on a risk by risk basis in those states that permit the combination; rather, the LRARO is part of the overall rating plan which the carrier files for regulatory approval. Thus, an insurer could have a LRARO/large deductible rating plan approved by the DOI that allows for lower rates for those policyholders electing large deductibles without violating 25 (A) (d). An insurer could specifically lay out in the LRARO filing what the discounts for electing a large deductible option would be. In this situation, the Commissioner would know exactly what discounts were being provided to policyholders for the election of this large deductible option and could make informed decision on whether to accept the filing. In the industry's view, this is consistent with both the letter and spirit of 25A(4)(d).

There is a good public policy reason to allow this combination. The combination of these two policy features allows for maximum flexibility for an insurer and large commercial policyholder to tailor a workers' compensation policy to meet the specific needs of that policyholder, much as Massachusetts law currently permits carriers to do for other forms of coverage for large commercial risks. LRARO/large deductible combinations are particularly appealing to insureds with multi-state or multiple in-state locations. The policyholder can determine how much risk it wishes to retain, in return for appropriate, mutually acceptable premium savings, and also better assess the loss experience for each individual location. This is why most states allow this combination. As there seems to be no statutory prohibition to combining the Large Rating Alternative Rating Option and large deductibles, we urge Massachusetts to join the majority of other states in allowing this and providing large policyholders the resulting benefits.

Finally, I want to briefly mention another option to provide additional flexibility for large, sophisticated risks. We suggest that you also consider promulgating regulations to permit negotiation on large deductible discounts between carriers and insureds. This would be for sophisticated risks that meet the eligibility requirements and would be similar to what is already permitted for insurers taking advantage of the Large Risk Alternative Rating Option (LRARO). Currently, DOI establishes the exact formula and rating values with prescribed outcomes. This extension of a manual rating approach is often not workable for large, sophisticated risks.

AIA thanks the Division of Insurance for the opportunity to present our views on the current regulations. I would be happy to answer any questions or provide any follow-up information you would like.