Compendium on Workmen's Compensation

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Chapter 15

Security Requirements and Arrangements

In order to guarantee the payment of workmen's compensation benefits, State legislatures have included security or insurance provisions in their statutes. These laws require employers to demonstrate their ability to satisfy their potential obligations to pay compensation. The nature of these security requirements, how they are enforced, the operations and regulation of private insurers, State funds, and self-insurers are critical elements in the workmen's compensation program.[1 2]

SECURITY REQUIREMENTS

In 1972, every State but Louisiana required private employers to insure their workmen's compensation obligation, or except in a few States, to demonstrate their ability to self-insure this obligation. Although Louisiana's legislature included a security provision in its workmen's compensation law, the courts declared this provision unconstitutional in 1920 and 1923. State legislatures feared that, without this insurance, wide fluctuations in their losses might prevent employers from paying injured employees. Public employees were subject to this condition in 34 States, but not in Georgia, Hawaii, Indiana, Iowa, Louisiana, Maine, Michigan, Minnesota, Nebraska, New Jersey, New Mexico, New York, Rhode Island, South Dakota, Texas, Utah, and Vermont. Apparently there is some reluctance to require public bodies to buy private insurance. In addition, many State governments and some cities have enough employees to predict their losses with a fair degree of accuracy.

Compliance Checks

Industrial commissions survey compliance with these security requirements. The first step is to identify new employers covered under the workmen's compensation laws. According to data we obtained early in 1972, new employer information from the Bureau of Employment Security is used in 8 States and new license information in 10 jurisdictions. (Not all States responded completely to the inquiry: Some not at all.) Insurance reports are used by some industrial commissions; spot checks, surveys, and trade journals in others. Several industrial commissions made no attempt to identify new employers but relied on the State requirement that employers register.

The second step is to learn whether or not an employer has purchased insurance for workmen's compensation or received permission to self-insure. The most frequently employed methods, we learned, were reports by State safety and labor standards inspectors and spot checks by staff. Only a few jurisdictions consulted reports by OSHA inspectors; others relied on insurer reports, coordination with other agencies, and programs of continuous surveillance by staff.

Extent of Noncompliance

There is scant information concerning the proportion of covered employers who fail to meet the security requirements. In response to our survey, most industrial commissions estimated noncompliance to be less than 0.5 percent or between

0.5 and 1.0 percent. Alabama indicated a 2.0 to 5.0 percent rate while both the District of Columbia and Florida reported 5.0 to 10.0 percent rates. Spot checks produced the highest State estimates. Other jurisdictions based their estimates on claims records, experience, or field contacts. In any event, the responses suggested a lack of reliable data or generally acceptable estimating procedures.

Penalties for Noncompliance

Our survey yielded no better information on actions of States to enforce security requirements. Three States reported fines and two mentioned legal action. Some jurisdictions referred contumacious employers to county or State prosecutors. Letters of admonition and threat of closure were mentioned in a few instances. Several States reported recent legislation providing for civil or criminal suits.

According to a 1969 search of the statutes in the 50 States, the District of Columbia, and Puerto Rico, 43 jurisdictions may impose fines of various amounts on noncomplying employers; 17 of these 43 jurisdictions may also imprison the offending employer. In 16 States, the employer may be enjoined from doing business. In 35 jurisdictions, the noncomplying employer is liable to suit with the three common law defenses abrogated.[3]

Types of Insurance Permitted

Depending upon the States where he operates, an employer must either obtain permission to self-insure or purchase insurance from a private insurer, a competitive State fund, or an exclusive State fund. A competitive State fund competes with private insurers; an exclusive State fund is the only workmen's compensation insurer in the jurisdiction.

Table 15.1 indicates for the 50 States, the District of Columbia, and Puerto Rico the types of insurers operating in that State and whether self-insurance is permitted. In some States the options for public employers differ from those for private employers. The options provided private employers can be summarized as follows:

Exclusive State fund only (4)

Nevada, Puerto Rico, North Dakota, Wyoming

Exclusive State fund or self-insurance (3)

Ohio, West Virginia, Washington

Competitive State fund, private insurer, or self-insurer (12)

Arizona, California, Colorado, Idaho, Maryland, Michigan, Montana, New York, Oklahoma, Oregon, Pennsylvania, Utah

Private insurer only

Texas

Private insurer or self-insurer

All others

Exclusive State funds were established on the assumptions that (1) these funds would have low expenses, permitting them to return most of their premiums as benefits, (2) all employers would be able to obtain insurance, and (3) private insurers should not make profits on social insurance. In several Western States, it was thought that private insurers were reluctant to underwrite workmen's compensation where employment was hazardous and widely scattered. Most jurisdictions, however, have no State funds; some have competitive State funds. Competition among insurers and the profit motive is supposed to provide the best combination of service and price. Many believe a competitive fund enhances competition among private insurers.

Table 15.1.—SECURITY PROVISIONS APPLICABLE TO PRIVATE AND PUBLIC EMPLOYERS, 1972

Jurisdiction	Security required		Types of insurer [1]		Self-insurance permitted	
	Private	Public	Private	Public	Private	Public
Alabama	Yes	Yes	I	I	Yes	Yes.
Alaska	Yes	Yes	I	I	Yes	Yes.
Arizona	Yes	Yes	C	E [2]	Yes	No [1].
Arkansas	Yes	Yes	I	I	Yes	Yes.
California	Yes	Yes	C	E	Yes	Yes.
Colorado	Yes	Yes	C	C	Yes	Yes.
Connecticut	Yes	Yes	I	I	Yes	Yes.
Delaware	Yes	Yes	I	I	Yes	Yes.
District of Columbia	Yes	(3)	I	(3)	Yes	(3)
Florida	Yes	Yes	I	I	Yes	Yes.
Georgia	Yes	No	I	I	Yes	Yes.
Hawaii	Yes	No	I	I	Yes	Yes.
Idaho	Yes	Yes	C	E	Yes	No [4].
Illinois	Yes	Yes	I	I	Yes	Yes.
Indiana	Yes	No	I	I	Yes	Yes.
Iowa	Yes	No	I	I	Yes	Yes.
Kansas	Yes	Yes	I	I	Yes	Yes.
Kentucky	Yes	Yes	I	I	Yes	Yes.
Louisiana	No [5]	No	I	I	Yes	Yes.
Maine	Yes	No	I	I	Yes	Yes.
Maryland	Yes	Yes	C	C	Yes	Yes.
Massachusetts	Yes	Yes	I	I	Yes	Yes.
Michigan	Yes	No	C	C	Yes	Yes.

See footnotes at end of table.

Table 15.1.—SECURITY PROVISIONS APPLICABLE TO PRIVATE AND PUBLIC EMPLOYERS, 1972

Jurisdiction	Security required		Types of insurer [1]		Self-insurance permitted	
	Private	Public	Private	Public	Private	Public
Minnesota	Yes	No	I	I	Yes	Yes.
Mississippi	Yes	Yes	I	I	Yes	Yes.
Missouri	Yes	Yes	I	I	Yes	Yes.
Montana	Yes	Yes	C	E	Yes	No.
Nebraska	Yes	No	I	I	Yes	Yes.
Nevada	Yes	Yes	E	E	No	No.
New Hampshire	Yes	Yes	I	I	Yes	Yes.
New Jersey	Yes	No [6]	I	I	Yes	Yes.
New Mexico	Yes	No	I	I	Yes	Yes.
New York	Yes	No	C	C	Yes	Yes.
North Carolina	Yes	Yes	I	I	Yes	Yes.
North Dakota	Yes	Yes	E	E	No	No.
Ohio	Yes	Yes	E	E	Yes	Yes.
Oklahoma	Yes	Yes	C	E	Yes	Yes.
Oregon	Yes	Yes	C	E	Yes	No.
Pennsylvania	Yes	Yes	C	C	Yes	Yes.
Puerto Rico	Yes	Yes	E	E	No	No.
Rhode Island	Yes	No	I	I	Yes	Yes.
South Carolina	Yes	Yes	I	I	Yes	Yes.
South Dakota	Yes	No	I	I	Yes	Yes.
Tennessee	Yes	Yes	I	I	Yes	Yes.
Texas	Yes	No	I	I	No	No.
Utah	Yes	No [7]	C	E	Yes	Yes.
Vermont	Yes	No [7]	I	I	Yes	Yes.
Virginia	Yes	Yes	I	I	Yes	Yes.
Washington	Yes	Yes	E	E	Yes	Yes.
West Virginia	Yes	Yes	E	E	Yes	Yes.
Wisconsin	Yes	Yes	I	I	Yes	Yes.
Wyoming	Yes	Yes	E	E	No	No.

[1] E=Exclusive State fund. C=Competitive State fund, private insurer. I=Private insurer.

[2] Elective after 1970 except for the State; self-insurance permitted after 1970 except for the State.

[3] Employees of the District of Columbia covered by congressional appropriation.

[4] Public insurers permitted to self-insure if they are rejected by insurers.

[5] Security is required of nonresident employers with immovable property valued at less than $25,000.

[6] Required only with respect to members of a board of education, volunteer firemen, and volunteer first aid or rescue squads.

[7] Optional for counties, cities, towns, and school districts in Utah; optional for municipalities in Vermont.

Guam, and American Samoa, like most States, are private insurance or self-insurance jurisdictions. The Virgin Islands have an exclusive State fund and prohibit self-insurance.

Distribution of losses.—In 1970, private insurers paid about 63 percent of the $2,927 million of workmen's compensation losses paid by all insurers and self-insurers; State funds (including Federal workmen's compensation programs) paid 23 percent; self-insurers paid 14 percent. Since 1960, when the proportions were 63, 25, and 12 percent respectively, self-insurers have increased their share. The State fund share has declined.[4, 5, 6, 7]

Distribution of insurance premiums.—Of the $4,260 million in workmen's compensation insurance premiums earned in 1970, private insurers earned 84 percent and State funds 16 percent. The private insurer share has increased steadily during the past decade. In 1960 their share was about 80 percent.[8]

PRIVATE INSURER OPERATIONS

Private insurers dominate the coverage. The 10 leading groups wrote almost half the business; the top 20 about 68 percent, up from 62 percent in 1950, although the share of the top 10 has changed little. The 10 leaders wrote as much as 88 percent of the coverage in Hawaii to as little as 51 percent in Kansas and Nebraska. In four States, one insurer wrote one-fourth of the business.[9]

Only 36 of the 383 insurers earned workmen's compensation premiums of $20 million or more, but these 36 cornered more than 78 percent of the total. Companies with nationwide operations accounted for 83 percent. Insurers licensed in only one State, more than 20 percent of all insurance companies, wrote less than 4 percent of the premiums.[10]

Workmen's compensation is the second largest property-liability insurance line, topped only by automobile insurance. Workmen's compensation premiums are about 11 percent of the total premium income. Among the 10 leading private insurance groups, four derive at least one-third of their business from workmen's compensation.

Classifications of Insurers

Private insurers can be classified according to their legal form of organization, their marketing methods, and their pricing policies.

Legal form of organization.—Legally, insurers may be classified as proprietary or cooperative insurers. Proprietary insurers have owners who bear the risks of the insurer and whose representatives manage the operations. The leading example by far is the stock insurer owned by stockholders who elect the board of directors. In 1970, of the 383 private groups in workmen's compensation insurance, about 68 percent were stock companies, with about 70 percent of the total premium volume.

Cooperative insurers have no owners other than their policyholders. The leading example is the advance premium mutual whose board of directors is elected by those policyholders who exercise their right to vote.

Unlike stock insurers, these insurers have no capital stock. Instead, retained earnings serve as a cushion against adverse experience. In 1970, mutual insurers, about 32 percent of the private workmen's compensation insurers, wrote 30 percent of the premiums earned.

Almost all of the 1970 workmen's compensation insurance premiums not written by stock or mutual insurers were written by reciprocal exchanges which, in their modern form, closely resemble advance premium mutuals.

The relative importance of stocks, mutuals, and reciprocal exchanges varies among States. In several States, stock insurers write over 75 percent of the business. In a few States, mutual insurers dominate the private insurance field.

Since 1951, when their share was 59 percent, stock insurers have steadily increased their proportion of the business.

Marketing methods.—Private insurers market their services through independent agents and brokers or directly through their own employees.

Independent agents usually represent several insurers, receive a commission for the business they place with a given insurer, and retain the right to renew their customers' insurance contracts with a different insurer. Independents claim to render service better than the average company employee because they are better paid, with the same commission rate each year to encourage continuous stable service, and because, by their ability to allocate employers' accounts among several insurers, they exert more influence in behalf of the insured.

Independent agency insurers also obtain clients through brokers who, in their purest form, represent not the insurer, but the insured, for whom they seek the best combination of protection and price. Brokers may place the contract directly with the insurer of their choice or through an independent agent. As compensation, they receive all or part of the agent's commission or a brokerage commission paid by the insurer. Some brokers, like some large agencies, provide engineering and claims adjustment services for their clients.

When an insurer sells through commissioned or salaried agents or sales representatives who are its employees, representing only the insurer, it is called a direct writer. Usually its representatives are paid at a lower rate per policy than independent agents. Furthermore, commission rates and bonus scales are usually more generous for new policies written than for old contracts renewed. Finally, direct writers tend to perform much of the paperwork at their home or regional offices.

Insurance marketing is influenced also by consultants who, for a fee paid by the insured, advise on insurance needs and types.

Most, but not all, independent agency insurers are stock insurers. Most mutuals are direct writers.

In 1970, about 59 percent of the private workmen's compensation insurance premium volume was written by independent agency insurers operating nationally. Another 14 percent was produced by agency insurers restricting their writings to a single State or region. The direct writers controlled about 27 percent of the market.[11] During the past 5 years the relative position of agency insurers and direct writers has remained about the same. National agency insurers, however, have increased their share slightly, at the expense mostly of local agency insurers.

The relative market shares vary widely among States. In several States, agency insurers write more than 80 percent of the business. In Wisconsin, direct writers control more than half the market.

Pricing philosophy.—Private insurers also differ according to their pricing methods. They may be (1) either bureau or independent insurers and (2) either nonparticipating or participating insurers.

Bureau insurers use as their initial rates the rates developed by some rating bureau; independent insurers develop their own initial rates. Although exact data are lacking, all but a small fraction of the workmen's compensation insurance in force is written at bureau rates. As will be shown later, some State laws require all workmen's compensation insurers to use bureau rates. In most other States, all insurers have joined the rating bureau and use the bureau rates because they find it simpler to use the same rating philosophy nationally or they see advantages in the economics in establishing rates, in credible data on which to base rates, and in relief from destructive price competition.

The principal rating bureau is the National Council on Compensation Insurance, New York City. Its members include 338 stock insurers, mutual insurers, and reciprocal exchanges and eight State funds (Arizona, Colorado, Idaho, Michigan, Montana, Oklahoma, Oregon, and Utah).[12] Ninety-two additional insurers subscribe for its services. The National Council makes the rates and files them with the appropriate authorities in 28 jurisdictions. In six additional States, the National Council does not make the rates but prepares the basic data and processes this information in accordance with instructions from a local independent rating bureau. These independent bureaus then file the rates.

In the remaining 17 jurisdictions, among 50 States plus the District of Columbia, 6 have exclusive State insurance funds. Six others have autonomous independent rating bureaus that function on a State basis similar to the National Council: California, Delaware, Massachusetts, New Jersey, New York, and Pennsylvania. In Texas, the National Council, acting as an advisory organization, recommends rates to the State Board of Insurance which then recommends a common set of rates for all insurers in the State.

In Hawaii, Illinois, and Rhode Island, the National Council prepares only advisory rates. Stock-controlled rating bureaus file these rates on behalf of some insurers. In Alaska, the National Council calculates advisory rates, with each insurer responsible for filing its own rates.

Nonparticipating insurers charge a set price. The initial premium for nonparticipating insurance is also the final cost. Participating insurers, in contrast, refund part of the initial premium if their total income from premiums and investments exceeds their losses and expenses and the amount by which they elect to increase their surplus. The final cost is the initial premium less the dividend.

Most stock insurers write nonparticipating insurance but some pay policyholder dividends. Almost without exception, mutuals and reciprocal exchanges are participating insurers.

In 1970, nonparticipating stock insurers wrote about 55 percent of the total premiums earned and almost 80 percent of the premiums written by stock insurers. Participating stock insurers controlled about 14 percent of the market, mutuals almost 30 percent, and reciprocal exchanges 1 percent.[13]

Both nonparticipating and participating stock insurers have increased their shares slightly since 1960 when their shares were 52 and 12 percent respectively.

Operations

The operations of private insurers are discussed in several places in the *Compendium:* Claims administration in Chapter 14, medical care administration in Chapter 10, rehabilitation services in Chapter 11, pricing methods in Chapter 17, safety programs in Chapter 18, and expenses and profits in Chapter 16. The discussion here concerns mainly underwriting and assigned risk plans, reinsurance, and assets and liabilities, with brief mention of claims organizations and safety programs.

Underwriting and assigned risk plans.—Individual private insurers are free to reject any applicant they consider an undesirable risk. An employer may be undesirable because he has a poor loss record, is engaged in some activity that is unusually hazardous, or is so small that the premium is less than the expected cost of service.

Except in Louisiana, rejected employers must have insurance unless they obtain specific permission to self-insure. Where there are competitive State funds, except in Arizona, Colorado, Idaho, Michigan, and Oregon, the public insurer is obligated to accept all applicants. In practice, the Colorado, Idaho, and Oregon funds do accept all applicants. In States without public funds plus Arizona, Idaho, Michigan, and Oregon, private insurers have formed assigned risk programs to insure employers rejected by individual insurers. About one-fourth of the States require insurers to have such programs.

The usual procedure is to assign unacceptable applicants to individual insurers in proportion to the insurers' market share. Otherwise, the applicant is insured either by an assigned risk pool composed of all insurers writing workmen's compensation insurance in the State or by separate pools of stock and non-stock insurers.

Most assigned risk plans charge 8 percent more than the rates charged by individual insurers.

In 1971, the National Council on Compensation Insurance operated assigned risk plans in 24 jurisdictions. Employers insured under these programs totaled 41,364, about 5 percent of the total number insured and 16 percent more than in 1970. The estimated premium income was $37.8 million, an increase of 18 percent over 1970.[14]

Reinsurance.—Because workmen's compensation insurers are exposed to catastrophic losses when large numbers are injured, they generally shift some of the risk by obligating a reinsurer to pay some portion of the loss in excess of a stated amount. There may be several layers of such protection against excessive loss. Less frequently, insurers also purchase aggregate excess insurance that protects them against aggregate losses in a single year that exceed a specified proportion of their premiums. Reinsurance, therefore, contributes to insurer solvency.

The reinsurer is usually a specialist, the reinsurance department of a general insurer, or a pool whose members reinsure one another.

In 1970, workmen's compensation insurers paid reinsurance premiums totaling over 21 percent of the premiums earned on direct business.[15]

Other.—Private insurers adjust claims through adjusters who are their salaried employees or through independent adjusters compensated by fees for services. Independent adjusters usually are employed when the volume of business in an area is limited, in peak periods, or when special talents are needed. Adjusters operate out of a network of claims offices or their homes. Field adjusters may be authorized to settle all claims except unusual ones.

Most insurers have departments to inspect the operations of insured employers and suggest how they might reduce their loss potential. Large employers generally benefit more from these services than small employers. Insurers also conduct research and education activities through trade associations.

Regulation of Private Insurance

Private insurers are permitted to write workmen's compensation insurance in 44 States plus the District of Columbia. In each of these jurisdictions, these insurers are subject to some form of regulation but State regulation exhibits wide variations in both its substantive elements and institutional structure. State insurance departments are the principal regulators with respect to the formation of new insurers and licensing of foreign insurers, their continuing solvency, and their business practices, particularly their rates. The workmen's compensation agencies are most concerned with the claims-handling practices of insurers.

Information on the regulation of insurers was determined in part through our survey in early 1972 of State insurance departments and industrial commissions.

Formation and Licensing

Persons desiring to form a stock insurance company must meet certain minimum capital and surplus requirements that usually vary by the types of insurance to be written. Mutual incorporators must have a minimum paid-in surplus, plus perhaps a minimum number of applications from a minimum number of applicants. In many States, in order to begin operations, these insurers must also deposit government bonds or some other securities or post a surety bond with the State insurance department.

Foreign insurers desiring to sell and service workmen's compensation insurance in the State must secure a license from the State insurance department. To obtain a license, the foreign insurer must meet essentially the same requirements as domestic insurers. They are often required to post surety bond or make some deposit for the protection of policyholders located in the State.

In all but a few States, except for the fact that the capital and surplus requirement may vary by line of insurance, no special formation or admission requirements are imposed upon insurers wishing to write workmen's compensation insurance in the State.

According to data from our survey, between 100 and 400 domestic and foreign insurers have been licensed to write workmen's compensation insurance in each open jurisdiction (table 15.2). Not every company writes this insurance in each State where it is licensed but, with few exceptions, it appears that more than 100 companies actually write workmen's compensation insurance in each open jurisdiction. As a general rule, from one-fourth to one-half of the licensed insurers do not write workmen's compensation policies in a given jurisdiction. While a few jurisdictions offered no data, each jurisdiction apparently can anticipate up to a dozen new applications each year for permission to write workmen's compensation insurance. The specific capital and other requirements probably serve as effective screening devices for specious applications. Permission was denied in only two States during 1970 and 1971. One withdrawal was reported in another State. In five States, the insurance department revoked one to three licenses during 1970 and 1971.

TABLE 15.2.—THE EXTENT OF PRIVATE INSURERS OF WORKMEN'S COMPENSATION, BY JURISDICTION, 1970–71

State	Number of companies licensed to write workmen's compensation insurance			Number of companies who wrote workmen's compensation insurance			Number denied permission to write workmen's compensation insurance		Number of applications to write workmen's compensation insurance received		Number of insurers who had licenses to write workmen's compensation insurance revoked	
	1970	1971	1969	1970	1971	1969	1970	1971	1970	1971	1970	1971
Alabama												
Alaska			243			77	0	0	(1)	(1)	0	0
Arizona	89	112		89	112		2	0	91	112	0	0
Arkansas	228	231		155	159		3	2	5	5	0	0
California	241	253		183		169	0	0	5	3	0	0
Colorado												
Connecticut												
Delaware												
District of Columbia		225		139			(2)	(2)	(2)	(2)	0	0
Florida	258							0	(3)	(3)	0	0
Georgia	226	228		174	185		0	0	5	4	0	0
Hawaii	116	118	119	84	(1)		0	0	8	11	0	0
Idaho		138		(1)	(1)		0	0	(1)	(1)	0	0
Illinois	(1)	335		(1)	(1)	94	0	0	(1)	(1)	1	0
Indiana	243	247		205	(1)		0	0	12	11	0	1
Iowa	400	400		179	(1)	182	0	0	(1)	(1)	0	0
Kansas	220	224		188	(3)	191	0	0	6	11	3	2
Kentucky	300	380		169							0	0
Louisiana	168			168			0	0	3	3	0	0
Maine												
Maryland		252			169			0		0		0
Massachusetts	176	179		132	134		0	0	6	6	0	0
Michigan												
Minnesota												
Mississippi												
Missouri	279			194				(4)	5	6		
Montana												
Nebraska		359		165	(5)		(3)	(3)	(3)	(3)	0	0
Nevada												
New Hampshire												
New Jersey	215	220		190	192		0	0	14	9	0	1
New Mexico												
New York	263	265		184	181		0	0	7	10	1	0
North Carolina	206	209			172		(1)	(1)	(1)	(1)	(1)	(1)
North Dakota												
Ohio												
Oklahoma												
Oregon	130	142		90	(1)		0	0	12	12	0	0
Pennsylvania												
Puerto Rico												
Rhode Island												
South Carolina	370	363		162								
South Dakota												
Tennessee	289	299					0	0	5	10	0	0
Texas												
Utah												
Vermont	319	324		(1)	(1)		0	0	5	4	0	0
Virginia												
Virgin Islands												
Washington												
West Virginia												
Wisconsin	214	219		176			0	0	8	9	0	0
Wyoming												

1 No data.
2 No such record is compiled.
3 Unknown.
4 One withdrawal.
5 Not available until April 15, 1972.

In almost every jurisdiction, the State insurance department determines eligibility to write insurance. Only in Indiana did the Industrial Commission have this responsibility. Where joint insurance-industrial commission responsibility was indicated, the response to our questionnaire clearly indicated the insurance department's authority over finances, forms, and rates.

The licensing of private insurers is seldom handled by staff specialists in workmen's compensation insurance. Only one or two such specialists were reported by a few States. Instead of specializing in types of insurance, the insurance department staff specializes in such aspects of property and liability insurance as licensing, examinations, forms, and pricing.

Table 15.3 indicates the principal standards applied by State insurance departments to qualify private workmen's compensation insurers. No State required a minimum premium volume as a condition for licensing or continued writing of workmen's compensation insurance but every State indicated some minimal capitalization and surplus. These requirements ranged from a combined $200,000 to $1,500,000, with most jurisdictions requiring between $500,000 and $1 million.

TABLE 15.3.—MINIMUM STATE STANDARDS FOR PRIVATE INSURERS OF WORKMEN'S COMPENSATION

	Premium volume		Minimum capital and surplus		Loss prevention facilities		Claims servicing		Minimum deposits		Other	
	Yes or no	Nature of requirement (thousands)	Yes or no	Requirement (thousands)	Yes or no	Requirement (thousands)	Yes or no	Requirement (thousands)	Yes or no	Requirement (thousands)	Yes or no	Requirement (thousands)
Alabama												
Alaska	No		Yes	$400	No		No		Yes	$200		
Arizona	No		Yes	$600	No		Yes		Yes	$600		
Arkansas	No		Yes	Capital $500; surplus $50			No		Yes	$50		
California	No		Yes	Capital $100; surplus $100	No		No		Yes	$100 not less		
Colorado												
Connecticut												
Delaware												
District of Columbia.	(1)											
Florida	No		Yes	Capital $500; surplus $750	No		No		No			
Georgia	No		Yes	$1,000	No		No		Yes	$50		
Hawaii	No		Yes	Capital $300; surplus $150	No		No		Both	Dom—No alien—300.		
Idaho	No		Yes	Capital $550; surplus $550	No		Yes	(2)	Yes	$25	Yes	(3).
Illinois	No		Yes	Capital $1,000; surplus $500	No		No		Yes	$330 [4]	Yes	(5).
Indiana	No		Stock	Capital $400; surplus $600 [6]	No		No		Yes	Retaliatory		
Iowa	No		Stock	Capital $200; surplus $300 [7]	No		Yes	Must be adequate.	No			
Kansas	No		Yes	Capital $300; surplus $200	No		No		Yes	$300	Yes	(8).
Kentucky			Yes	$150								
Louisiana			Yes	Capital $650; surplus $350								
Maine												
Maryland	No		Yes	Capital $250; surplus $250	No		Yes	(9)	Yes	(10)		
Massachusetts	No		Yes	Capital $400; surplus $400								
Michigan												
Minnesota												
Mississippi												
Missouri	No		Yes	Capital $200; surplus $200 [11]	No	Customary facilities.	No	Customary facilities.	Yes	$50 or bond		
Montana												
Nebraska	No		Yes	$500	No		No		Yes	Retal. basis		
Nevada												
New Hampshire												
New Jersey	No		Yes	Various	No		No		No		Yes	(12).
New Mexico												
New York	No	(13)	Yes	(14)	No		No		Yes	$250		
North Carolina	No		Yes	Capital $500; Surplus $500	No		No		Yes	$25	Yes	(15)
North Dakota												
Ohio												
Oklahoma												
Oregon	No		Yes	$1,500			Yes	(16)	Yes	(17)		
Pennsylvania												
Puerto Rico												
Rhode Island												
South Carolina	No		Yes	Capital $300; Surplus $600 [18]	No		No		No			

See footnotes at end of table.

TABLE 15.3.—MINIMUM STATE STANDARDS FOR PRIVATE INSURERS OF WORKMEN'S COMPENSATION—Continued

	Premium volume		Minimum capital and surplus		Loss prevention facilities		Claims servicing		Minimum deposits		Other	
	Yes or no	Nature of requirement (thousands)	Yes or no	Requirement (thousands)	Yes or no	Requirement (thousands)	Yes or no	Requirement (thousands)	Yes or no	Requirement (thousands)	Yes or no	Requirement (thousands)
South Dakota												
Tennessee	No		Yes	Capital $750; Surplus $375	No		No		No			
Texas												
Utah												
Vermont	No		Yes	$500	No		Yes	(19)	No			
Virginia												
Virgin Islands												
Washington												
West Virginia												
Wisconsin	No		Yes	(20)	No		Yes	(21)	Possibly retal. law		Yes	(22)
Wyoming												

1 Applicants for certificate of authority to act as insurer under insurance laws must meet requirements that are too extensive to enumerate on. Insurance laws are one of the most lengthy titles of our code.
2 Claims paying office in state.
3 Also licensed for surety.
4 At market for benefit of U.S. policy obligations.
5 Must subscribe to statutory assigned risk pool.
6 Mutual $1,000,000.
7 Also Mutual: —Capital——Surplus—$500,000.
8 Must be authorized to write workmen's compensation in home state—have authority in charter bylaws.
9 Local office in charge of competent person to handle claims.
10 Cash or securities not less than $100,000.
11 (Multiple line) Capital $400,000; Surplus $400,000.
12 Methods of operation.
13 Ratio $2 net writings to $1: Surplus to policyholders.
14 On organization, $300,000 and $150,000; maintain combined $300,000.
15 Must be member of Compensation Rating Bureau of North Carolina.
16 Competent to service.
17 Equal to formula loss reserves.
18 Also $300,000 surplus-stock.
19 Adequate claims organization.
20 Additional capital of $100,000 and surplus of $50,000 or $400,000 and $200,000 if workmen's compensation is the only line.
21 That they be adequate to service Wisconsin risks (Ins. 6.11).
22 Company will not be licensed for workmen's compensation until it is member of Workmen's Compensation Rating Bureau.

No State insurance agency reported requirements for safety or loss prevention services. Only seven insurance departments indicated minimal requirements for claims services, even in general terms, saying services must be adequate, customary, or competent, or that a payment office must be sited in the State. Wisconsin's statutory definition of unfair claims procedures is those that violate the statutory requirement of fair and equitable treatment.

All but six reporting jurisdictions reported minimum deposit or bond requirements. Although two reported $25,000 requirements, most were about $200,000. One State indicated no minimum requirements for domestic companies but required $300,000 for others.

Only New York mentioned a maximum (2 to 1) ratio of premiums to policyholders' surplus as a financial constraint. However, this ratio generally is one of a series of measures used to evaluate an insurer's financial condition.

In every State, these requirements must be maintained as a condition of continued licensing.

Solvency

Solvency is regulated primarily by checking on the valuation of insurer liabilities and the nature and valuation of their assets. State insurance departments check on these two aspects of insurer operations primarily through annual statements that provide detailed information on premiums, losses, expenses, assets, and liabilities; and periodic on-the-spot investigations of insurer assets, financial records, and operations.

Reserves.—The principal liabilities in an insurer's balance sheet are the unearned premium reserve and the loss reserve. The unearned premium reserve is established in recognition of the insurer's liability for losses during the unexpired portion of the policies in force for which the premiums have already been paid. State law requires that the unearned premium reserve be established by prorating the premium on each policy in force over the expired and unexpired portions of the policy period. For example, if an insurer writes a 1-year workmen's compensation insurance policy, effective July 1, for which the premium is $120, on December 31 one-half of this premium is assumed to be earned and one-half unearned. Consequently, the unearned premium reserve is $60. This procedure is generally assumed to be conservative, because insurers incur most of their acquisition and underwriting expenses at the time the policy is written. Only that portion of the unexpired premium designated for losses and loss adjustment expenses, plus some small margin for future expenses, is actually required to meet obligations incurred in the future if this insurer's original expense and loss assumptions are correct. Consequently, many analysts suggest that 30 to 40 percent of the unearned premium reserve, less the Federal income tax to be paid when these reserves are released, is really "hidden equity" that should be added to the surplus or retained earnings account. Because a substantial amount of compensation insurance premium is collected after the policy period is over as a result of a payroll audit that indicates an exposure in excess of that estimated or because of a retrospective premium adjustment, the redundancy of the unearned premium reserve requirement is less of a problem in this line. Because the redundancy errs in the direction of a tighter check on solvency, it is unlikely to be changed.

Loss and loss adjustment expense reserves are established to recognize the insurer's liability on outstanding claims. The greatest portion of these reserves is established to cover future payments on account of claims that have been incurred and reported, but not paid; the remaining portion covers claims that have been incurred but were not reported prior to the statement date. Loss and loss adjustment reserves are particularly important when the insurer writes mostly liability and workmen's compensation policies. Payments of workmen's compensation claims may extend indefinitely into the future. These reserves are established in one or more of the following ways: estimating the probable amount at which each reported claim can be settled and adding an allowance for unreported claims; multiplying the number of unsettled claims of each type by the probable average settlement value and adding some amount for unreported claims; or a loss-ratio formula method. Under this latter method, the amount actually paid for losses and loss adjustment expenses is subtracted from that portion of the premiums earned that was intended for this purpose (i.e., the premiums earned multiplied by the permissible loss ratio, including the percentage allowance for loss adjustment expenses). Presumably, the difference represents the amount still to be paid if the premiums were set at the correct level.

Because liability and compensation loss reserves are such significant items in the balance sheet, and because years ago many insurers tended to be optimistic in establishing reserves on individual claims, States prescribe certain minimum reserve requirements. Under a model bill approved in 1968 by the National Association of Insurance Commissioners, loss reserves must be computed in accordance with regulations made from time to time by the commissioner, but the minimum reserve requirement for unpaid workmen's compensation insurance losses and loss expenses incurred during each of the three most recent years shall not be less than 65 percent of premiums earned during each year less the amount already paid for losses and expenses incidental thereto incurred during said year.

This approach, which has already been adopted by many States, differs in some respects from the prior rule but retains the basic loss-ratio approach. This approach has been criticized first because the premiums earned may be an unreliable base. For example, if the premiums were inadequate, the reserves will be inadequate. Second, the 65-percent loss ratio may be too high for some insurers and too low for others. Nevertheless, this tested approach was considered by most to be safer and more understandable than the proposed alternatives.

Insurers are required to show in their official annual statements how their estimates of prospective losses compare with those eventually incurred.

Assets.—The assets of insurers are regulated with respect to how the insurer can invest its funds, how the assets are valued, and whether the assets are admitted or not admitted.[9] Although insurers invest some funds in real and personal property required to transact their business, the bulk of their assets is invested in bonds or stocks. State laws vary in their restrictions on these investments. The New York law, one of the more stringent, affects all insurers operating in New York and thus covers a substantial portion of the business. In that State, funds equivalent in amount to the required minimum capital and surplus and half the unearned premium and loss reserves must be invested in certain types of obligations. Funds equal to the minimum capital and surplus must be invested in U.S. Government bonds; bonds issued by New York State, local New York State governments, or other States; and mortgages upon New York State real estate. Funds equal to half the reserves can be invested in such instruments as bonds and preferred stocks of private corporations, mortgage loans, loans of insured savings and loan associations, stocks and debentures in housing projects, and cash. The remainder of the insurer's assets are subject only to certain quality checks and general restrictions, such as a prohibition against investing more than 10 percent of an insurer's assets in any one corporation, more than 10 percent in real estate holdings, and more than 50 percent in mortgages. Tables 15.4 and 15.5 show how stock and mutual insurers in the aggregate chose to invest their funds at the close of 1970. Differences among insurers reflect differences in investment philosophies, lines of insurance written, and taxation. For example, insurers specializing in compensation insurance do not have to maintain as liquid a position as property insurers because many of their serious claims are paid in installments.

Table 15.4.—BALANCE SHEET, 828 U.S. STOCK PROPERTY AND LIABILITY INSURERS, DEC. 31, 1970

[Dollars in billions]

Assets	Amount	Percent	Liabilities	Amount	Percent
Government bonds	$14.9	35.0	Loss and loss adjustment expense	$14.0	32.9
Other bonds	5.0	11.7	Unearned premium reserves	11.2	26.3
Mortgages	.1	.3	Other liabilities	3.4	8.0
Stocks	14.9	35.0	Total	28.6	67.1
Real estate	.6	1.5	Capital and surplus:		
Premium balances	3.4	7.9	Capital	1.9	4.5
Cash	1.1	2.5	Net surplus	9.3	21.8
Other	2.6	6.1	Voluntary reserves	2.8	6.6
			Total capital and surplus	14.0	32.9
Total	42.6	100.0	Total	42.6	100.0

Source: "Best's Aggregates and Averages," 1971 Alfred M. Best Co., New York, p. 52.

Table 15.5.—BALANCE SHEET, 321 U.S. MUTUAL PROPERTY AND LIABILITY INSURERS, DEC. 31, 1970

[Billions]

Assets	Amount	Percent	Liabilities	Amount	Percent
Government bonds	6.3	46.3	Loss and loss adjustment expense	5.6	41.5
Other bonds	2.9	21.2	Unearned premium reserves	3.3	24.4
Mortgages	.1	.8	Other liabilities	.9	6.7
Stocks	2.5	18.4	Total	9.8	72.6
Real estate	.3	2.3	Capital and surplus guaranty funds	.1	.7
Premium balances	.8	5.6	Net surplus	3.2	23.7
Cash	.3	2.2	Voluntary reserves	.4	3.0
Other	.4	3.3	Total capital and surplus	3.7	27.4
Total	13.5	100.0	Total	13.5	100.0

Source: "Best's Aggregates and Averages," 1971, M. Best Co., New York, 1971, p. 162.

Bonds in good standing are valued by amortizing or accruing discounts such that the value reaches par at maturity. Stocks are carried at their market value. Mortgages, if properly secured, are carried at the unpaid balance. Real estate is valued at its appraised value.

Assets that cannot be readily converted into cash for the payment of claims are considered nonadmitted assets. These include such items as furniture, office machines (but not computers which receive special treatment), automobiles, notes payable not secured by certain types of collateral, premiums due over 90 days, and investments not conforming to regulations.

In addition to the above solvency measures, all but four States now have special insolvency funds that will honor the workman's compensation obligations of defunct insurers.

In our survey, only two private insurer insolvencies were reported for 1970 or 1971 and they affected only six States.

Business Practices

State insurance departments are resourceful and versatile in regulating the business practices of insurers. Policy forms may have to meet requirements imposed by a State legislature and checked by the State insurance department for misleading language. Because all insurers use by agreement the same standard workmen's compensation and employers' liability policy and endorsements and because under this contract the insurer agrees to pay the obligations of the employer under the workmen's compensation law even if it is amended, language is seldom a problem. Agents and brokers are licensed and their activities supervised. State insurance departments also follow up justifiable complaints they receive from insureds or claimants. The State may influence insurer practices through moral suasion or the threat of license revocation. Of particular interest in this study are the regulations with respect to availability of insurance; rates, expenses, and dividends; and loss adjustments.

Availability.—Assigned risk plans for employers rejected by individual insurers were discussed above. In our survey, agencies were asked whether they ever contested cancellation of an existing insurance contract and to comment on their assigned risk plans.

Roughly half of the respondents reported contesting cancellation or nonrenewal of a workmen's compensation insurance contract. Although these departments have responded to complaints raised by employers by checking for compliance with contractual terms for cancellation or with statutory provisions where extant, it appears that cancellation is not a major issue. Few mentioned nonrenewal. Possibly assigned risk plans provide an effective safety valve that channels nonrenewal conflicts into other offices. The use of assigned risk plans or State insurance funds was the standard procedure for providing workmen's compensation coverage to those unable to secure protection from private insurers directly.

In almost every instance, an 8 percent surcharge was imposed upon assigned risk plan coverage. In 10 States, no additional charge was imposed. While no State was able to estimate the number of employees covered in such manner, many were able to identify the number of employers covered. These ranged from 350 in Alaska in 1969 to 17,873 in New Jersey in 1971. More typically, between 1,000 to 3,000 employers were covered in a given State. When asked to identify any common characteristics of these companies, the State insurance departments usually specified hazardous aspects of employment (e.g., offshore drilling, high rise construction, parking plant, underground coal mining, or window washing) and the small premium.

Rates.—In 1968, most property and liability insurance rates were regulated in about two-thirds of the States under a model law endorsed in 1946 by the National Association of Insurance Commissioners or a closely related version. Under this law, an insurer's rate must be reasonable, adequate, and not unfairly discriminatory. These terms are not defined in the model law itself, but they have been interpreted to mean that the rates should not be too high on the average; they should not be so low as to threaten the solvency of the insurer; and each insured should pay his fair share of the cost. Insurers must file the rates they intend to charge with the State insurance department. They cannot use these rates until the insurance commissioner approves them or until a certain period, such as 20 days, has expired with no action on his part. Despite the fact that this law permits rates to become effective without affirmative prior approval by the commissioner, the model law is commonly called "prior approval" legislation. The rates can be disapproved at any time. Although rating bureaus can file for members and subscribers, membership is optional and members and subscribers can request permission to deviate from bureau rates. This approach represents a compromise between almost complete reliance upon competition as a regulator and a one-price prior approval system. Many insurers were and still are unhappy with this regulatory plan because they have been denied rate increases, particularly in automobile insurance, that they considered reasonable, and because in their opinion the system results in unnecessary delays, political pressures upon department decisions, arbitrary actions, and an unproductive use of limited insurance department resources.

Many would prefer a more flexible procedure, such as that in California where insurers need not file their rates, although the commissioner upon examination subsequently can disapprove the rates. Another less stringent approach is a "file-and-use" law under which insurers must file their rates but can use them immediately subject to subsequent disapproval. In December 1968, following extensive research, the NAIC Subcommittee on Rates and Rating Organizations concluded that price competition in insurance is much more effective today than it was in the late forties. In States where an increase in competition indicates that "greater reliance on competition in the regulation of rates would be appropriate," the subcommittee recommended that either (1) the insurance commissioner be authorized to suspend the "prior approval" requirement of the model law for any line, subdivision, or class of insurance where this is warranted, or (2) the "prior approval" requirement be suspended with power invested in the insurance commissioner to reimpose prior approval upon any line, subdivision, or class of insurance for which he finds that the competition is insufficient or irresponsible.[16] In the late sixties and early seventies, several States replaced model laws with less restrictive regulation.

At the same time, some States have become more stringent in regulation. North Carolina requires all automobile liability insurers to belong to a single rating bureau and use bureau rates approved by the insurance commissioner. The Texas State Board of Insurance itself establishes the rates for several lines of insurance.

Workmen's compensation insurance rates are subject to more restrictive regulation than other property and liability insurance rates. Table 15.6 classifies the 45 regulatory laws applicable to private workmen's compensation insurance rates according to their approval and rating bureau provisions.

All States require insurers to file their rates. Only Delaware and the District of Columbia permit insurers to file workmen's compensation rates and use them immediately.

Among the remaining 43 private-insurer jurisdictions, 18 apply the 1946 model law provisions to workmen's compensation insurance rates. Although Connecticut uses model law filing and approval procedures, unlike any other State it prohibits insurers from agreeing to adhere to bureau rates. The other 24 have laws more restrictive than the model. In 11 of these 24 States, the regulation differs from that prescribed by the model laws only in that prior approval of the rate structure is required.

Six jurisdictions—California, Minnesota, New Jersey, North Carolina, Pennsylvania, and Wisconsin—require all insurers to belong to a single rating bureau, prohibit use of the bureau rates until they have been approved by the State insurance department, and permit no deviations from the approved bureau rates. The Texas State Board of Insurance itself establishes State rates. Regulations in the other six States are more closely akin to model law philosophy. They differ only in that all insurers must belong to a rating bureau (Arizona and Montana), all insurers must belong to a rating bureau with no rate deviations permitted (Idaho and Iowa), or prior approval is

TABLE 15.6.—TYPES OF WORKMEN'S COMPENSATION INSURANCE RATE REGULATION, BY STATE, 1968–72

Jurisdiction	Rate approval provision	Rating bureau provision
Alabama	Model law	Model law.
Alaska	do	Do.
Arizona	do	Mandatory bureau.[1]
Arkansas	do	Model law.
California	Prior approval [2]	Mandatory bureau, no deviation.[1]
Colorado	Prior approval	([3])
Connecticut	Model law	No agreement to adhere to bureau rates.
Delaware	File-and-use	Model law.
District of Columbia	do	Do.
Florida	Prior approval	Do.
Georgia	do	([4]).
Hawaii	Model law	Model law.
Idaho	do	Mandatory bureau, no deviation.[3]
Illinois	do	Model law.
Indiana	Prior approval [5]	Do.
Iowa	Model law	Mandatory bureau, no deviation.
Kansas	do	Model law.
Kentucky	do	Do.
Louisiana	Prior approval	Do.
Maine	do	Do.
Maryland	Model law	Do
Massachusetts	Prior approval	([4])
Michigan	Model law	Model law.
Minnesota	Prior approval [2]	Mandatory bureau, no deviation.
Mississippi	Model law	Model law.
Missouri	Prior approval [2]	([4]).
Montana	Model law	Mandatory bureau, uniform percentage deviation.
Nebraska	do	Model law.
New Hampshire	Prior approval	Do.
New Jersey	do	Mandatory bureau, no deviation.
New Mexico	Model law	Model law.
New York	Prior approval	Do.
North Carolina	do	Mandatory bureau, no deviation.
Oklahoma	Model law	Model law.
Oregon	do	
Pennsylvania	Prior approval	Mandatory bureau, no deviation.
Rhode Island	Model law	Model law.
South Carolina	do	Do.
South Dakota	do	Do.
Tennessee	do	Do.
Texas	State makes rates	Advisory organizations only.
Utah	Model law	Model law.
Vermont	Prior approval	Do.
Virginia	do	Do.
Wisconsin	Prior approval	Mandatory bureau, no deviation.

[1] All insurers must belong to a rating organization. No rating organization can have less than five members.
[2] Minimum rate approved for each class.
[3] No reference.
[4] Rating provision of model law but no deviations permitted (Missouri). Or no mention of rate deviations (Georgia and Massachusetts).
[5] Minimum pure premium approval for each class together with minimum and maximum expense loadings.
[6] Minimum pure premium and expense loading approved.

required and member insurers cannot deviate from bureau rates (Missouri and Oregon).

No State imposes less restrictive rate regulation on workmen's compensation insurance than on other property and liability insurance lines. Indeed the difference in regulatory philosophy is sometimes dramatic. California, a rigid regulator of workmen's compensation rates, does not require even the filing of other property and liability insurance rates.

Why are workmen's compensation insurance rates subject to more stringent regulation than other lines? Why in some instances are workmen's compensation insurers required to charge the same minimum rates? One frequently cited reason is that, because workmen's compensation insurance is social insurance, the prices charged by private insurers should be subject to careful public scrutiny. Another is that regulation is needed even where price competition is permitted by law because insurers have tended to adopt a uniform price system. The public has tended to accept or even require uniform pricing in this line subject to prior approval because solvency is a prime consideration in workmen's compensation and might be endangered by unrestrained price competition; price competition might affect adversely the loss prevention services and claims handling attitudes of insurers; and, in order to prevent unfair discrimination, insured payroll should be divided into so many industrial classes that few, if any, insurers would have credible experience in each class. Another frequently advanced argument is that experience rating would become chaotic if insurers competed on rating plans with no orderly system for exchanging experience. A final reason is historical. In the early days, the three preceding arguments particularly were persuasive. Most States had rating laws applicable to workmen's compensation insurance shortly after they enacted workmen's compensation laws. By the early forties, fire insurance rates were effectively regulated in only 18 States and automobile insurance rates in only 7 States but workmen's compensation insurance rates were effectively regulated in about 36. Consequently, it is not surprising that workmen's compensation insurance rates were commonly excepted from the new rate legislation patterned on the model law in the late forties.

Workmen's compensation insurance rates continue to receive special treatment under more recent legislation. Several States such as Colorado, Connecticut, Florida, Georgia, Indiana, Louisiana, Minnesota, Oregon, and Wisconsin have in the past 5 years converted their general regulatory philosophy from a model law or more stringent approach to one permitting insurers more flexibility in filing and using rates but their workmen's compensation rating law was not changed. Montana, a file and use State in other lines, tightened its regulation of workmen's compensation rates.

Dividends and expenses.—Dividends affect the final cost of workmen's compensation insurance but whereas initial workmen's compensation rates are subject to stringent regulation, dividends are not. Generally, dividends may not be declared if the funds are needed to protect the solvency of the insurer. Only 15 States have statutes specifically prohibiting unfair discrimination in the payment of workmen's compensation insurance dividends. These statutes vary with respect to what is considered unfair discrimination, the types of insurers (mutual or stock, domestic or foreign) whose practices are so regulated, the manner in which regulations are enforced, and the degree of effective enforcement.

Although expenses incurred with respect to workmen's compensation insurance are not regulated separately by statute, expense regulation is part of rate regulation. The expense loading in the manual rates, the gradation of expense loadings in premium discount and retrospective rating plans, and the program for modifying individual insured expense provisions are subject to review by State insurance departments.

The profits of insurers also are regulated through rate regulation. Insurers generally are permitted to include a profit factor of 2.5 percent in their manual rates. (See Chapter 16.)

In addition to these State regulations, increases in expense allowances in the premiums are subject to phase II controls under 1972 Federal price control regulations.

Claims handling.—According to our survey, regulation of claims handling activities is handled by the insurance departments in nine jurisdictions and by the industrial commission in 15 States. Claims handling regulation ranges from the follow-up of complaints to the continuous evaluation of insurer performance to assure fair treatment of injured workers. In some States, the industrial commission calls in top level executives of those insurers whose performance is considered unsatisfactory. Fines and license revocation may follow if this talking stage fails to provide improved performance. Claims handling records, such as speed of handling and the mechanics of establishing reserve funds, are mentioned by several jurisdictions as their means of regulating claims handling. It appears that State insurance departments tend to use informal procedures that focus on complaint follow-up and that industrial commissions favor formal reviews.

Promptness of payment is used as a regulatory measure in 10 jurisdictions. The ratio of contested cases to total cases is considered by some industrial commissions. No claims handling analyses are undertaken in 6 jurisdictions. Less than half of the respondents indicated that they could provide data of claims handling performance. Even fewer publish such data.

State insurance departments report scarcely any regulation of the insurer's loss prevention activities. The closest approximation is the feedback of loss reduction through experience rating plans, where authorized. Moreover, almost all insurance department respondents indicated that no such regulation was provided by any other State agency. Only a few suggested that such regulation might be conducted by that State's industrial commission. In the rare State which regulates loss prevention activities, the industrial commissions indicated that the State labor department's safety inspections were the means of regulation.

Reports From and About Insurers

There is a degree of unanimity in the extent to which insurance companies must file periodic reports. All insurance departments require the annual statement; several require quarterly reports. Although none of the insurance departments require reports on the nature and settlement of claims handling, 12 respondents indicated that such reports are required by their State's industrial commission.

Only one State indicated that reports on the insurer's loss prevention activities were required and that report went to the Department of Labor and Industry. Most insurance departments require insurers to file annual reports on expenses other than claims payments. At a minimum, this is the annual expense exhibit, but some States, e.g., New Jersey, require additional information.

The performance of individual insurers or all insurers is the subject of few regulatory reports by State agencies. Reports on financial condition are published in 14 jurisdictions. Fourteen jurisdictions have prepared reports in the past on the promptness of payment of claims, namely, Alabama, California, District of Columbia, Florida, Idaho, Michigan, Minnesota, Nebraska, New Hampshire, New Jersey, New York, Oregon, Texas, and Wisconsin. Of these States only Alabama, California, Florida, Michigan, New York, and Wisconsin have distributed detailed reports in the recent past. However, few States provide reports on the relation of contested claims to all claims and loss prevention activities.

STATE FUNDS

Of the 20 State and territorial funds, 12 compete with private insurers or self-insurers. Six of the State funds are exclusive insurers as are both territorial funds. A discussion of each of the two major classes of State funds below parallels the treatment of private insurers.

Exclusive Funds

Washington established the first exclusive State fund in 1911. North Dakota in 1919 was the last to establish an exclusive State fund. Ohio has the largest; its premium volume exceeds the national business of all but four private insurers. Table 15.7 shows the 1970 premium volume of the six.

Table 15.7.—PREMIUMS WRITTEN BY EXCLUSIVE STATE FUNDS, 1970

[In millions]

	Premiums written
Jurisdiction:	
Nevada	$14.1
North Dakota	5.5
Ohio	175.3
Washington	70.5
West Virginia	29.5
Wyoming	4.3
Total	299.1

Source: 1971 Argus F. C. & S. Chart, 95th annual edition, The National Underwriter Co., Cincinnati, 1971.

Classification of insurers.—Because the State fund is exclusive and insurance compulsory, the State has no marketing expense.

Each exclusive State fund makes its own rates. Only the Nevada fund has paid dividends as a participating insurer.

Operations.—Exclusive funds must accept all applicants for insurance. This inability to select risks affects the loss experience of the fund.

Exclusive State funds write only workmen's compensation and, in some instances, employers' liability insurance. The workmen's compensation promise can cover only employees hired in the State but most will protect the employer against actions brought under the workmen's compensation law of another State by a home-State employee injured in that other State.

None of the exclusive State funds has purchased reinsurance to protect itself against shock losses despite the small size of some. All States except North Dakota and West Virginia have branch claim offices or adjusters in the field. In these two States, claims are usually handled by mail. In all jurisdictions, most checks are issued from the home office of the fund.

Some State funds have no safety programs. Ohio and Washington, however, have fairly extensive programs. The Washington fund operates a special rehabilitation center.

Regulation.—Because the exclusive fund is the arm of the State and does not compete with private insurers, regulation is viewed in a special perspective.

In no jurisdiction is the State fund responsible to the insurance commissioner. In all jurisdictions, some financial audits are required, usually annually, with responsibility for the audit assigned to the State auditor, examiner, or controller.

Like private insurers, exclusive funds maintain unearned premium reserves reflecting the obligation of the fund to provide protection in the future because of premiums or deposits in hand. Washington and Wyoming do not maintain such reserves because they collect premiums after they are earned.

Loss reserves tend to be established on individual or average case estimates. Most, but not all, employ professional actuaries to make these estimates. After the Washington fund was advised that its loss reserves were inadequate in 1965, this deficiency was corrected.

In all jurisdictions, the statute prescribes the nature of the fund's investments and prescribes who is to make and control the investments. The constraints generally restrict investments to securities permitted insurance institutions or savings banks, including local, State, or Federal bonds. Common stock investments are permitted by Nevada in limited amounts. The funds' investments generally are managed by a State official. In relatively few jurisdictions do the funds' managers assume the investment function, except to decide the availability of funds for investment.

No exclusive fund has encountered financial difficulties in recent years except for the Washington incident noted above.

The North Dakota legislature has specifically guaranteed the solvency of its fund. What other legislatures would do in a crisis is uncertain. An exclusive State fund does have the advantage, however, that it can raise premiums to avert insolvency without fear of losing its clients.

The rates charged by exclusive State funds are not subject to external regulation.

The claims practices of exclusive State funds, like those of private insurers, are reviewed by their industrial commissions. The difference, however, is that in Nevada, North Dakota, West Virginia, and to some extent Ohio, the industrial commission manages both the workmen's compensation program and the fund. In addition, in Washington the first step of adjudication is handled by the State fund, not by an independent agency. Although this dual responsibility raises questions of conflict of interest, States with this system claim economy, efficiency, close scrutiny, and uniformity of application as virtues of this system.

Competitive Funds

Michigan, followed closely by California and New York, was the first to establish a competitive State fund. Most of the other funds were organized prior to 1920 but Arizona did not act until 1925 and Oklahoma not until 1933. Oregon had an exclusive State fund until 1965 when it was converted into a competitive fund.

The 12 competitive funds differ with respect to size, philosophy, and practices. The California fund is the largest; only five private insurers write more premiums. As shown in table 15.8, the share of the total State premium volume controlled by the State fund also varies among States.

Table 15.8.—PREMIUM VOLUME AND MARKET SHARES OF 12 COMPETITIVE FUNDS, 1971

	Premium volume (millions)		Market share (percent)
	Total	State fund	
State:			
Arizona	$55.6	$29.3	53
California	677.9	143.9	21
Colorado	37.5	21.2	57
Idaho	13.3	3.0	23
Maryland [1]	68.4	4.6	7
Michigan	227.3	12.9	6
Montana	13.0	6.8	52
New York	464.9	104.6	22
Oklahoma	46.8	4.9	10
Oregon	80.4	49.9	62
Pennsylvania	152.9	10.0	7
Utah	9.0	5.3	59
Total	1,847.0	396.4	21

[1] Maryland premium estimated by extrapolating 1966 premium volume in Williams-Insurance Arrangements, op. cit., p. 153 at same rate of growth as average state fund

Source: State fund data from 1971 Argus F. C. & S. Chart, Ninety-fifth annual edition-The National Underwriter, Cincinnati, 1971. Private insurer data required to calculate market shares from "Property/Liability Insurance Marketing," Best's Review, Property and Liability Insurance Edition, October 1971, 31.

Classification of insurers.—Although most funds do not solicit business, Arizona, California, New York, and Oregon employ salaried salesmen to market their services. Although the New York fund has sales representatives, their principal function is to provide services to companies already insured. The Michigan fund derives almost all of its business from private insurance agents who receive a commission on the business they submit. Seven of the 12 funds use private-insurer bureau rates. Four charge bureau rates less a flat discount. Only the Maryland fund make its own rates. All funds except Maryland and Pennsylvania paid dividends to policyholders in recent years. Both the Maryland and Pennsylvania funds may pay dividends in the future.

Operations.—All competitive funds except those in Arizona, Colorado, Idaho, Michigan, and Oregon must accept all applicants for insurance. In practice, Colorado, Idaho, and Oregon do accept all applicants. The Arizona and Michigan funds participate in the assigned risk programs in their States. The California fund can reject an applicant not meeting State safety standards.

Most contracts cover employers' liability losses as well as workmen's compensation. Like the exclusive funds, the competitive funds cover only home State employees.

All but the Arizona, Colorado, and Montana funds have reinsurance against shock losses.

Eight of the 12 have a network of branch office or field representatives to adjust claims. Arizona and Maryland have limited branch claims facilities, Colorado and Utah have none.

Ten of the 12 have safety divisions. The California, Montana, New York, and Oregon funds probably offer the most complete services. The Maryland and Pennsylvania funds have no safety division but the Maryland fund has hired a private consulting firm to service its insured.

Regulation.—Unlike exclusive insurers, six competitive funds must submit reports on their financial condition to the State insurance department. However, only the California and New York funds are subject to the triennial examination applicable to private insurers. All funds other than the New York fund are subject to audits by the State auditor or a similar official.

All competitive funds have established uninsured premium reserves reflecting premiums already received for protection to be provided in the future.

States establish their loss reserves by various means. Arizona and Colorado funds use outside actuaries to determine their loss reserve requirements. In California, the fund's loss reserve standard is basically that prescribed for private insurers by the National Association of Insurance Commissioners. The Oklahoma fund uses the amounts established by the State legislature for its known losses and an "educated guess" on first notices. Subsequent changes are made as the fund secures sufficient knowledge of these new claims. Maryland also utilizes actuarial analysis at the end of each fiscal year. In Montana the fund reviews individual cases and bases aggregate special reserve levels on experience and projected trends. An outside consulting firm is used to evaluate periodically the adequacy of loss reserves. In general, actuarial analysis, individual case history, fund experience, and judgment are used by the several funds. Responses indicate that not every State uses all of these procedures. Some funds, in fact, may use only one of these bases.

In 1966 the Pennsylvania fund was technically insolvent when steps were taken to correct loss reserves that had been underestimated previously. In 1967 the loss reserves of the Arizona fund also were declared inadequate by a consulting firm. Both situations were remedied.

Competing State funds are subject to the same investment restrictions as exclusive funds.

The only technical insolvencies in recent years were noted above. No State has a statutory obligation to help a fund in financial difficulty but several fund managers believe the legislature would come to their aid if necessary. Unlike exclusive insurers, competitive insurers cannot raise their rates without losing clients.

In Arizona, California, Montana, Oregon, and Pennsylvania, the State fund is subject to the rate regulatory laws applicable to private insurers. The California, Michigan, Montana and New York funds are specifically authorized, through scheduled or judgmental surcharges, to increase the rates paid by poor risks.

The claims practices of competitive State funds are subject to review by the industrial commission or corresponding agency. Only the Colorado and Montana funds, being administered by their industrial commissions, are subject to the conflict of interest noted in connection with some funds. In competitive-fund States, there is a potential conflict in reviewing workers' claims and in regulating the State fund in relation to private competitors.

SELF-INSURERS

In all jurisdictions except Nevada, North Dakota, Puerto Rico, Texas, the Virgin Islands, and Wyoming, employers are permitted under certain conditions to self-insure workmen's compensation. Although most jurisdictions reported 200 or fewer self-insurers, self-insured employers in 1970 paid 14.1 percent of the workmen's compensation benefits.

Self-insurance is becoming popular among those who qualify. In 1960 self-insurers paid only 12.4 percent of the benefits. Most States report an increase also in the number of self-insurers. Possible explanations are increasing cost consciousness, sales activities of agencies who seek to manage self-insurance programs, and the business merger movement which increases the size of firms and their ability to self-insure.

Self-Insurance Arrangements

Self-insurance plans can be categorized according to their arrangements for safety and claims adjusting, and how they are funded.

Safety and Claims Adjustment.—Employers who elect to self-insure must assume some responsibilities that would otherwise be handled by insurers. They must consult injured employees to evaluate their condition and arrange for the payment of benefits in accordance with the law. Although a self-insurer does not have to provide any safety services (except for minimum compliance with the safety laws), only a short-sighted employer would fail to do so.

Some employers have their own employees provide both types of services. Others hire independent agencies to provide either or both types of services. Independent adjusters, who may also serve insurers, are often retained to investigate and settle claims. Similarly, agencies specializing in safety work may be hired to provide loss prevention and reduction services. Both claims adjustment and safety services are provided by management service organizations who, in effect, take over the administration of the self-insurance plan for the employer. Typically, these organizations collect a fee equal to some percentage, say 25 percent of the premium that would be paid by the employer if he were class rated and not entitled to premium (expense) discounts. For this fee the contractor provides the administrative services plus excess aggregate or "stop-loss" insurance that protects the insured should annual losses exceed the remaining portion of the fund allotted in view of the "normal" premium.

Funding.—Self-insurance plans may be pay-as-you-go with each year's losses treated as a current operating expense or temporary drain on retained earnings or there may be advance funding. The advantages of pay-as-you-go are that it is simple to administer and permits the employer to keep assets invested in operations. The principal disadvantage is that if the loss experience fluctuates markedly from one period to the next, the net income statements may provide a distorted view of the firm's operations. If there is an unusually large loss in a single year, the business may suffer severe disruptions to its cash flow because of its failure to make any advance preparations. Even if the experience is fairly stable from year to year, the dollar outlay in the early years will increase because of the accumulation of long-term claims.

This last problem can be handled by charging against each year's operations, in addition to losses paid on claims occurring that year, the present value of all benefits to be paid in future years on behalf of all workers who were disabled or died as a result of accidents occurring during that year. At the close of any accounting period, the firm's balance sheet would include this present value among the liabilities. As reported below, some States force the self-insurer into computing this present value by requiring a deposit with the industrial commission as security for all or most outstanding liabilities. When the business is required to make such a deposit or when it voluntarily earmarks assets equal to this liability amount and invests them in marketable securities, its income may be less than if it were able to invest these funds in current operations.

In order to even out fluctuations in accident rates over time, the self-insurer may charge against each year's operations an amount equal to its annual expected loss. On its balance sheet, the firm earmarks some retained earnings (or establishes a liability item) equal to the cumulative expected losses less those losses that have been paid. The earmarked amount would cover the outstanding liability described in the preceding section plus a reserve for future losses. The self-insurer may or may not segregate certain assets or maintain a deposit equal to a portion or all of this retained earnings account.

The most formal way to fund a self-insurance plan is to form a captive insurer which, usually as a subsidiary corporation or part of a holding company, insures only its owner's risks. The principal attractions of this approach over other advance funding techniques are that premiums paid to the captive insurer are tax-deductible expenses, and the captive insurer can purchase protection from reinsurers that the employer would not be able to secure from insurers selling their product directly to the public. The principal disadvantages are the resources that must be devoted to the formation and operation of an insurer and the State premium taxes and other special expenses incurred by insurers.

Reasons for self-insurance.—Self-insurance is attractive primarily because it may be less costly than insurance. An insurance premium is designed to pay the losses and expenses of the insurer and provide a margin for profit or contingencies. The self-insurer hopes to save money on the loss or the expense and profit components of the premium.

The loss component equals the average loss the insurer expects the employer and others like him to experience. If the employer is so much better than the average employer in his class that his expected loss may be less, he would save money by self-insuring. In the short run, however, the loss experience may differ substantially from the expected loss. Indeed the loss in a single year might be catastrophic. The larger the number of employees, the less the risk of fluctuation in annual losses. For most employers, the risk is such that self-insurance is out of the question. For others, the comparison between actual and expected loss is an important consideration.

By self-insuring, the employer can save that part of the premium charged to cover selling expenses, some general administration expenses, and profits. There may also be savings on loss prevention and loss adjustment services even though these services must still be performed.

Other considerations include the relative quality of the safety and claims services provided by insurers, by management service organizations, and by employers themselves; tax factors; and the opportunity cost of paying an insurer a premium instead of paying losses and expenses as they occur.

Regulation of self-insurers.—The determination of eligibility and continued eligibility for self-insurance is a major responsibility. The regulations applicable to prospective and present self-insurers are discussed briefly below.

Licensing.—In response to our survey nearly every response indicated that the industrial commission, court, or agency director was responsible for licensing self-insurers. In a few States, the insurance department makes the determination. Legal and accounting skills were most frequently cited as the disciplines of the person responsible for analyzing eligibility.

There are no uniform interstate qualifications for self-insurance. Table 15.9 indicates the extent

496-632 O - 73 - 18

to which potential self-insurers must meet minimum financial, size, and administrative standards. Although almost every State has established some financial criteria, these frequently are quite subjective. Most States admit to few other requirements. Several States base eligibility on minimum net worth, with $100,000 or $150,000 mentioned by three jurisdictions, but the more common response was a vaguely defined "financial ability to pay claims"

Table 15.9.—SELF-INSURER LICENSING REQUIREMENTS, BY JURISDICTION, 1971

Jurisdiction	Financial condition	Payroll size	Number of employees	Nature of business	Safety record	Loss prevention facilities	Medical service facilities	Claims handling facilities	Other
Alabama	(1)	No	No	No	(2)	No	No	(3)	No.
Alaska									
Arizona									
Arkansas	Financially stable.	No	No	No	No	No	No	No	No.
California		No	No	No			No		No.
Colorado	$100,000	No	300	No	No	No	Yes	Yes	No.
Connecticut									
Delaware									
District of Columbia		Yes	Yes	Yes			Yes	Yes	
Florida	$150,000 minimum net worth.	No	No	No	No		No	(4)	No.
Georgia	Yes	No	No	No	Yes	Yes	No	Yes	No.
Hawaii		No	No	No	No	No	No	No	No.
Idaho	Financial statement.	$150,000 per year.	No	No	No	No	No	Resident claims manager.	(5).
Illinois	Financially stable.	No	No	No	Good		Close to operation.	Company representative or service agency.	No.
Indiana									
Iowa									
Kansas	Yes			Yes	Yes				
Kentucky	Latest financial statement.	No	No	No	No	No	No	No	No.
Louisiana									
Maine	Yes				Yes	Yes		Yes	
Maryland	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No.
Massachusetts									
Michigan	Capital equals average for 3 years based manual premium.	No	100	No	Give evidence of positive program.	No	No	Positive program.	Surety bond or security may be required.
Minnesota	Financial ability to pay comp.	No	No	No	Yes	No	No	Have system to promptly pay benefits.	
Mississippi									
Missouri	Financially able to carry own insurance.		Qualifies as "major employer"	Yes	Yes	Yes		(6)	No.
Montana	Reviewed by administration.		No	No	Reviewed by administration.	Reviewed by administration.	No	(7)	No.
Nebraska									
Nevada									
New Hampshire	Annual statement.	No	No	No	No	No	First aid station.	Same as insurers.	No.
New Jersey									
New Mexico									
New York		No	No	No	Yes	Yes	Yes	Yes	(8).
North Carolina	No								

See footnotes at end of table.

Table 15.9.—SELF-INSURER LICENSING REQUIREMENTS, BY JURISDICTION, 1971—Continued

Jurisdiction	Financial condition	Payroll size	Number of employees	Nature of business	Safety record	Loss prevention facilities	Medical service facilities	Claims handling facilities	Other
North Dakota									
Ohio									
Oklahoma		No	No	No	No	No	No	No	No.
Oregon	Board has right to refuse applications.	No	No	No	No	No	No	Claims must be handled in Oregon.	
Pennsylvania									
Puerto Rico									
Rhode Island									
South Carolina	$100,000 net worth.	No	No	No	No	No	No	Person or agency for handling claims.	No.
South Dakota									
Tennessee									
Texas									
Utah	Annual financial statement.	No	No	No	No	No	No	No	No.
Vermont									
Virginia									
Washington									
West Virginia	Discretionary	No	No	No	No	No	No	No	No.
Wisconsin	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes.
Wyoming									
Guam									

[1] Financially able to pay claims.
[2] Considered as part of financial condition.
[3] Must be handling program in order to retain self-insurer status.
[4] Employees must have 5 years experience in workmen's compensation claims adjusting.
[5] Must file surety bond based on size of payroll.
[6] Capable to process claims promptly and accurately.
[7] Reviewed by administration—Must be responsive.
[8] Length of time in business—Injury and accident experience.

The second most frequently cited requirement is claims handling ability. Florida requires each self-insurer to have at least one employee with a minimum of 5 years of claims-handling experience. Idaho requires a resident claims manager. Missouri looks for the ability to process claims promptly and accurately. In Montana, the difficulty of setting general criteria is recognized by the requirement that the company be considered "responsive" after review by the Commission. Oregon simply requires that claims be handled in Oregon.

Almost no jurisdictions set a minimal size for a company, per se. Six respondents suggested minimum payroll size criteria, eight indicated some criteria for the number of employees, and six authorities showed concern for the nature of business. Idaho, however, required a $1.5 million annual payroll; Michigan looked for at least 100 employees; Colorado required 300 or more employees; and Missouri required the self-insurer to be a "major employer." Frequently, the particular criteria were not indicated.

A good safety record and evidence of a positive program were cited by 14 jurisdictions as a special requirement for self-insurers. Most of these same jurisdictions indicated concern for loss prevention and medical service facilities.

License renewal.—Most jurisdictions require annual renewal of the self-insurance privilege. In a few States, such as California, the license continues indefinitely until revoked. California indicated that revocation could occur for failure to increase deposits, to comply with rules and regulations, to remain solvent, or to fulfill obligations, as well as repeatedly inducing claimants to accept less than their due compensation or discharging their obligations in an unlawful manner. These specific grounds for the most part compare with those cited by other jurisdictions, including those with an annual review program.

Few States ordered a halt to specific self-insurance programs during 1970 or 1971. Alabama halted two companies in 1970 and three in 1971 and ordered others to post bonds and reinsure against excess loss. In California, nine were halted in 1970 and 16 in 1971. Florida stopped one in 1970 and two in 1971. In Kansas, three companies were ordered to stop self-insuring in 1970 and six in 1971. Minnesota halted one company in 1970. In five States, the insurance department revoked one to three licenses during 1970 and 1971.

In most jurisdictions, between 50 and 500 companies were allowed to self-insure. Relatively little information was provided the Commission on the importance of self-insurance. Although 28 jurisdictions indicated the number of self-insurers, only eight provided even aggregate data for the number of employees so covered.

Two variations of traditional self-insurance and private insurance organizations have developed in recent years: (1) Group self-insurance, or the pooling of workmen's compensation risks by similar companies, and (2) captive private insurers or the use of wholly owned subsidiaries (or affiliate corporations) to provide for the parent and sister companies' insurance needs.

Group self-insurance of workmen's compensation is permitted in seven States. Because the members of a group self-insurance arrangement pool their risks, the plan could be considered a form of cooperative insurance, subject to regulation by the State insurance department, but no special requirements for group self-insurance are imposed in Alabama, the District of Columbia, and Illinois. South Carolina merely requires member businesses to be of a like or similar nature. Similarly, Florida requires that all members of the group be in the same or a similar type of business and members of the sponsoring bona-fide trade association, subject as a group to an indemnity agreement providing joint and several liability for all claims against the group. The Florida Department of Commerce determines the minimum aggregated and specific reinsurance requirements. In New York, group self-insurers must be in the same industry. The initial security deposit is determined by the chairman of the Workmen's Compensation Commission and the superintendent of insurance.

Captive insurance companies must be considered an unknown quantity vis-a-vis workmen's compensation. From the questionnaire responses, it appears that neither captive nor substantially captive insurers are identified as such to any significant extent. The State insurance departments in Arizona, Arkansas, and the District of Columbia identify captive insurance companies. In Arizona and the District of Columbia, the insurance departments also identify substantially captive companies. None of these insurance departments considers workmen's compensation coverage by captive companies as self-insurance.

Although a slightly greater number of industrial commissions indicates that captive and substantially private insurers are identified, only the District of Columbia considers their workmen's compensation coverage as self-insurance. Captive insurers are identified by industrial commissions in Idaho, Illinois, Indiana, Maine, Oregon, and Wisconsin. The District of Columbia, New Hampshire, Oregon, and Wisconsin identify substantially captive insurers.

Self-insurer solvency.—Only one self-insurer insolvency was reported in 1970 and two in 1971. No employee losses were experienced. In one instance, the security deposit was able to absorb the losses. In other instances the parent and sister companies were responsible. Although some States have established self-insurer solvency funds, the required bonds are the principal defense.

Security deposits as a means of assuring that employees of self-insurers will receive workmen's compensation benefits are not uniformly applied. The deposits are always required in 20 jurisdictions and sometimes required in 16 jurisdictions. Somewhat surprisingly, security deposits are never required in at least one State.

Reinsurance is not required widely. Only nine States require such coverage as a condition for self-insurance. Five other jurisdictions indicate that reinsurance is required in some instances; ability to pay claims, size of company, and risk are relevant factors in the decision. Several agencies merely recommend reinsurance. Others report it is widely adopted voluntarily.

Security deposits apparently are subject to considerable discretion even where they are required of all self-insurers. Many respondents reported that the amount of deposit was not determined by formula. Frequently, the employer's financial condition, nature of business, and general risk are the considerations influencing the size of the deposit. Some States, however, require minimum bonds of $25,000. In two instances, Colorado and Oregon, the basic bond is $100,000. Despite the discretion exercised in most States, 12 respondents indicated that all of the self-insurers' liability on outstanding claims must be covered by the security deposit. An additional six jurisdictions require only part of the outstanding workmen's compensation liabilities to be covered by the security deposit. Generally, the employer's deposit liability can be satisfied by either cash, negotiable bonds, or surety bonds.

Reports from self-insurers.—Self-insurers must file some information with regulatory authorities each year but, as with private insurers, the requirements exhibit little consistency. Almost every State requires self-insurers to submit annual reports on their financial condition. Although in some instances, the report need be filed only with applications for renewal of self-insurance, quarterly or triennial requirements have been adopted elsewhere.

In 15 jurisdictions responding to our questionnaire, self-insurers must report, usually annually, on reserves on unpaid claims. Reports on the nature and settlement of all individual claims also must be filed in 23 jurisdictions. Payroll information by industrial classification must be reported in 21 jurisdictions.

Only seven jurisdictions require reports of loss prevention activities. One jurisdiction requires this only with the initial application; one other State, only on request. Such reports must be filed annually in the remaining five jurisdictions. Self-insurers must file reports on expenses other than claims payments in six jurisdictions.

Regulatory reports on self-insurers.—Few regulatory authorities publish reports on the performance of either individual self-insurers or of self-insurers as a group. Although promptness of payment reports are provided by only six jurisdictions answering our survey, this is the most frequently issued report. In contrast, reports on financial condition are released by three States, reserves on unpaid claims by three authorities, contested claims relative to total claims by four, expenses other than claims payments by one, and loss prevention activities by none.

References to Chapter 15

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3. C. A. Williams, Jr., *op. cit.*
4. Alfred M. Skolnik and Daniel N. Price, "Another Look at Workmen's Compensation Insurance," Social Security Bulletin, XXXIII, No. 10, October 1970, 9.
5. "Workmen's Compensation Payments and Costs, 1970," Social Security Bulletin XXXV, No. 1, January, 1972, 30.
6. 1970 data on private insurers are from "Property/Liability Insurance Marketing—1970," Best's Review, Property and Liability Insurance Edition, October, 1971, p. 11.
7. 1970 State fund data from "Argus Casualty and Surety Chart," 1971.
8. For the shares from 1917 to 1967, see C. A. Williams, Jr., *op. cit.*, pp. 12–13.
9. Best's Review, *op. cit.*, pp. 30–2.
10. A. M. Best Co. data.
11. Best's Review, *op. cit.*, p. 30.
12. National Council on Compensation Insurance, Annual Report, March 2, 1972, p. 26.
13. Derived from "Insurance Expense Exhibit For the Year Ending Dec. 31, 1970," compiled in 1971 by the National Council on Compensation Insurance.
14. National Council on Compensation Insurance, *op. cit.*, p. 19.
15. "Insurance Expense Exhibit For the Year Ending December 31, 1970," *op. cit.*
16. For the complete recommendation and a summary of the research and hearing that preceded this conclusion, see Proceedings of the National Association of Insurance Commissioners, 1969, Vol. I, pp. 307–381.