

American Insurance Association

August 16, 2007

Response to Question No. 5

When the burden of funding a state's workers' compensation benefit delivery system (e.g., second injury funds or their equivalent, and workers' compensation administrative expenses) falls on insureds (by imposing liability for assessments on insurers or surcharges on insureds), then self-insured employers should share this funding burden. The total funding burden should be allocated between the insured and self-insured communities by applying a two-step calculation.

First, the funding burden should be equitably allocated between insured and self-insured employers based on losses "gross" of large deductible amounts (i.e., loss reimbursements or deductible credits). This approach helps to assure that the costs of supporting the benefit delivery system are shared in a manner that maintains a level playing field between insured and self-insured employers.

Second, the portion of the foregoing funding burden that is allocable to insureds should be allocated among insurers based on premium, which also should be determined "gross" of large deductible amounts. This second step helps to assure the equitable allocation of funding among insured employers, regardless of whether or not their workers' compensation policies include a large deductible feature. Furthermore, from a financial accounting standpoint, this basis for allocating funding allows the insurer to book the assessments when the premiums are written, rather than when losses are incurred.

In contrast to funding for the workers' compensation benefit delivery system, insurer funding for purposes of state general revenues (e.g., through premium taxes) and residual market mechanisms should be based on premium "net" of the large deductible amount. This approach is necessary because the cost of losses within the deductible (as a risk borne by the insured employer and not the insurer) does not constitute "premium." Where an insurer must pay losses on a 'first dollar' basis and seek reimbursement, the insurer bears a credit risk and not an insurance risk consistent with statutory accounting principles.

Response to Question No. 6

Not applicable in light of response to Question No. 5