

Initial Statement of Reasons
Title 8, Chapter 8, Subchapter 2
Articles 1, 6, 9, and 12

Article 1, Section 15201

Specific Purpose

Article 1 contains definitions of terms contained in Articles 2 through 13, dealing with self insurance of workers' compensation liabilities. The proposed amendments to these regulations will clarify existing definitions.

Section 15201(a) is amended to clarify the definition of an adjusting location in instances where a claims adjuster administers claims from his or her home on a telecommuting basis but reports to a local office of the claims administrator, and further clarifies that in such instances.

Section 15201(m) is amended to clarify that claim logs are required to list claims by year reported rather than by year in which the injury occurred, thus providing that claims will be listed on claim logs in the same manner that claims are reported on the Self Insurer's Annual Report, as required by Section 15251.

Article 6

Specific Purpose

Article 6 addresses standards for estimating future liabilities of claims. The proposed amendments to these regulations will clarify and make specific requirements for setting reserves on self insured workers' compensation claims.

Necessity

Private self insured employers are required to post security deposits with the Department of Industrial Relations in the form of a surety bond, stand-by irrevocable letter of credit, cash, or securities. If a self insured employer defaults on its workers' compensation obligations, the Director calls the security deposit, turns it over to the Self Insurers' Security Fund (SISF), and orders SISF to pay the claims. Beginning in 2003, Labor Code Section 3701.8 was enacted, which allows the Self Insurers' Security Fund to cover the security deposit of participating employers through an alternative security deposit, wherein SISF assesses members to establish an aggregate deposit. Monies are collected from participating employers through composite deposit assessments.

The security deposit for each private self insured employer, whether participating in the alternative security deposit program or not, is based on the estimated future liabilities of each employer. Pursuant to Labor Code Section 3701 and Title 8, California Code of Regulations, Section 15251, self insured employers are required to file Self Insurers' Annual Reports with the Office of Self Insurance Plans (SIP) annually, reporting paid costs and estimated future costs for all claims. Each employer's security deposit is adjusted at least annually, and the amount required to be at least 135% of estimated future liabilities, plus an average one year's estimated future liabilities. In addition, SIP audits a sample of claims of each private self insured employer no less frequently than once every three years. The purpose of the audits is to ensure that the estimates of future liabilities, and consequently the security deposit, are adequate to cover anticipated costs in case the employer is unable to pay its claims. Pursuant to Title 8, Section 15301, the Manager of SIP has the authority to increase the estimates of future liabilities and the deposit requirement of the employer following an audit to ensure that the deposit is adequate.

Over the past twenty years, approximately 60 self insured employers have defaulted on their workers' compensation liabilities. Security deposits have been inadequate to cover the costs of all claims to the extent that in 2003, the Self Insurers' Security Fund was operating with a deficit of over \$56 million. The deficit grew over the years in spite of the ability of the SISF to assess all self insured employers up to 2% of their paid indemnity to make up for the shortfall of the individually posted security deposits. The chief factor contributing to the huge deficit was the understatement of estimated future liabilities of claims on the part of self insured employers.

Regulations setting standards for estimating future liabilities must be clear and enforceable in order to address the problem of under-reserving. These amendments to Article 6 will address those needs.

Section 15300(b) is amended for grammatical clarity and to specifically state that estimates of future liability reported on the Self Insurer's Annual Report must indicate the estimates as of the ending date of the report.

Subsection (b)(1) is added to specify the various costs that must be included in estimates of future liability.

Subsection (b)(2) is added to indicate how estimates must be calculated in the event of conflicting medical reports.

Subsection (b)(3) is added to specify how estimates for medical treatment must be calculated in the event an injury has not reached a level of maximum medical improvement.

Subsection (b)(4) is added to specify how estimates for medical treatment must be calculated in the event an injury has reached a level of maximum medical improvement.

Subsection (b)(5) is added to clarify the manner in which recurrent and non-recurrent medical costs must be estimated.

Subsection (b)(6) is added to clarify the manner in which reductions based on utilization review of medical treatment or third party recoveries must be addressed in estimating future liabilities.

Subsection (b)(7) is added to specify the manner in which the life expectancy of injured workers must be estimated and to provide claims administrators with information on how to obtain life expectancy information.

Subsection (b)(8) is added to specify that supporting documentation is needed reduce estimates of permanent disability based on apportionment of part of the disability to factors not related to the claims.

Subsection (b)(9) is added to specify that estimates of lifetime benefits may not be reduced based on the value of those benefits being paid in a lump sum.

Subsection (c) is amended for clarity.

Subsection(d) is amended for clarity.

Subsection (g) is amended to specify that reserves must be immediately updated to reflect changes in the amounts of estimated liability and to specify that estimates of future liability must be reviewed and made current when a self insured employer changes administrators.

Article 9

Purpose

Article 9, dealing with record and audits, is amended to eliminate unnecessary duplication, to specify that claim file contents must include written itemized documentation of the calculation of estimated future liabilities, and to ensure that a third party administrator has access to all information needed to administer claims when records are transferred from one administrator to another.

Necessity

In order for the Office of Self Insurance Plans to determine whether estimates of future liability of self insured employers are adequate, each workers' compensation claim file must contain documentation of all factors involving the handling of the claim that affect the amount of benefits due or potentially due. Documentation in the claim files must be maintained in a manner that can be readily accessed by auditors, and, to ensure that claims are adequately reserved, it must be clear that estimates of future liability may not be eliminated until there is no reasonable expectation of future costs. In addition, when a self insured employer changes administrators, the new administrator must be able to obtain all documentation from the previous administrator needed to administer the claims.

Section 15400(c) is amended to eliminate unnecessary duplication regarding requirements for establishing estimates of future liability that are specified in Article 6, Section 15300. Subsection (c) is also amended to specify that each claim file must contain written itemized documentation showing the basis for the calculation of the estimate of future liability and be maintained in an order to facilitate reviewing the progress of the claim in order to determine what benefits may be due or become due. Subsection (c) is also amended to specify that certain documents may be kept in electronic form, thus eliminating the need to store paper documentation when unnecessary.

Section 15400.2 is amended to specify that claims may be closed after two years of no activity, but only if there is no reasonable expectation that future benefits may be due.

Section 15402.4 is amended to require the old administrator to provide paper documentation to the new administrator at its own expense if its contract with the employer precludes transferring electronic file documentation to a new administrator.

Article 12

Purpose

Article 12 is amended to clarify existing language, to eliminate unnecessary language and information, and to increase the fees for taking the Self Insurance Administration Examination and the annual license fees for third party administrators.

Necessity

In order to ensure that workers' compensation claims for self insured employers are administered pursuant to California statutes and regulations, claims administrators are required to demonstrate competence in the handling of claims. The chief manner in which claims administrators demonstrate competence is by passing the Self Insurance Administration examination which tests technical knowledge related to claims handling and self insurance regulations. The examination is administered by the Office of Self Insurance Plans.

As part of the recent workers' compensation reform, the Department of Insurance is promulgating regulations that require all claims adjusters of workers' compensation claims to be certified and to meet minimum requirements for training. The proposed regulations allow claims adjusters that have passed the Self Insurance Administration examination to be considered as experienced adjusters, thereby reducing their continuing education requirements. In addition, because of the extensive changes to workers' compensation law after the enactment of SB 899 and other reform, the need has arisen to extensively revise the Self Insurance Administration examination so that knowledge of current law can be tested.

In the last year, the number of applicants taking the Self Insurance Administration examination has more than doubled. In order to keep up with the increased demands, Self Insurance Plans has been expanded its contract with Cooperative Personnel Services (CPS), the agency that administers the exam, to allow electronic registration for the exam and to revise the test extensively. It is the goal of Self Insurance Plans to have the exam pay for itself. Otherwise, self insured employers that fund the Office of Self Insurance Plans through application fees and annual license fees will be subsidizing individual adjusters that obtain certification, many of whom do not work for the employers, but work for insurance carriers or third party administrators that handle claims for insurance carriers as well as self insured employers. The fee for taking the exam has not increased from the current \$100 in twenty years, yet the anticipated cost of SIP to administer the exam is approximately \$160 per applicant for the first year, followed by a minimal reduction in cost in subsequent years.

In addition to certifying individual claims adjusters, SIP licenses third party administrators. Annual license fees for third party administrators also have not increased in twenty years, even though SIP's costs have increased. So that self insured employers do not subsidize the costs related to the licensing of third party administrators, it is SIP's goal to have that licensing function pay for itself as well.

Section 15450 is amended for clarity, both grammatically and to eliminate unnecessary and inaccurate information, not needed in the regulation.

Section 15450.1 is amended for clarity, both grammatically and to eliminate unnecessary and inaccurate information, not needed in the regulation.

Section 15452(a) is amended to clarify the requirements for demonstrating good cause for administering claims out of state by specifying what does *not* constitute good cause. The administration of California workers' compensation claims out of state has historically made it difficult for SIP to perform audits and effectively monitor the administration of the claims.

Section 15452(b) is amended grammatically for clarity.

Section 15452(c) is amended to eliminate the required application form required to be completed by a candidate for the Self Insurance Administration exam, thus allowing more flexibility in accepting applications.

Section 15452(d) is amended to increase the fee for taking the Self Insurance Administration exam from \$100 to \$150.

Section 15452(e) is amended to eliminate the unnecessary deadline for the issuance of a Certificate of Achievement.

Section 15454 is amended to increase the annual license fee for a third party administrator from \$650 to \$1,000, and to increase the additional location fee from \$100 to \$200 for each additional adjusting location.

TECHNICAL, THEORETICAL, AND/OR EMPIRICAL STUDY, REPORTS OR DOCUMENTS

The Department did not rely upon any technical, theoretical, or empirical studies, reports or documents in proposing the adoption of this regulation.

ALTERNATIVES TO THE REGULATION CONSIDERED BY THE AGENCY AND THE AGENCY'S REASONS FOR REJECTING THOSE ALTERNATIVES

No other reasonable alternatives were presented or considered by the Department.

ALTERNATIVES TO THE PROPOSED REGULATORY ACTION THAT WOULD LESSEN ANY ADVERSE IMPACT ON SMALL BUSINESS

The Department has not identified any reasonable alternatives or that have otherwise been identified and brought to the attention of the agency that would lessen any adverse impact on small businesses.

EVIDENCE SUPPORTING FINDING OF NO SIGNIFICANT ADVERSE ECONOMIC IMPACT ON ANY BUSINESS

SIP is not aware that there will be any significant adverse economic impact on business.