Risk MANAGEMENT

Split Coverage for PEOs

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There are numerous business reasons why a PEO might need to split its workers' compensation exposures between more than one insurance carrier. While this issue has given regulators and the National Council on Compensation Insurance (NCCI) fits, there are no insurers within the voluntary market willing and/or able to provide workers' compensation coverage to all potential client companies within all jurisdictions. It should be noted that the split-coverage issue is a major focus of the National Association of Insurance Commissioners (NAIC) Task Force on Employee Leasing; their major concern being split coverage between the voluntary and involuntary markets. It is their fear, which is just, that the good business will flow into the voluntary markets and the bad into the involuntary.

My point of contention is that this happens every day in the non-PEO world when independent agents are forced to place business in the involuntary markets when there is not a voluntary market willing to write the exposure. So, what is the big deal? Just because an uninsurable business is part of a PEO, should that mean the PEO and its respective carrier partner(s) should sign off on a risk that should be in the pool? The PEO, after all, is not the carrier and should not have the ability to bind the carrier to business it would not normally entertain within or outside of co-employment.

There are a few variations of split coverage worth noting before we review the rationale behind it. The most common form of split coverage involves a PEO that has a master policy with one insurance carrier, but then procures client-based policies for specific client companies. Sometimes these client-based policies are written with a voluntary carrier, but more often than not, they are written by a state fund or assigned risk plan. In some states, such as Arizona and Louisiana, where client-based plans are mandated, the PEO will contract with several markets that will give it the ability to provide options.

In any event, why would a PEO have split coverage?

Geography

Many insurance carriers willing to underwrite PEO business are regional in nature and therefore cannot always cover the current or future geographic footprint of a PEO's client companies. As a result, PEOs often are forced to have two or more carriers and or state funds/pools in play to provide coverage in the respective states in which they do business.

Rating

Many insurance carriers willing to underwrite PEOs do not have an AM Best rating of A- or better. It is common for national general contractors, municipalities, and other entities to require those doing work on their premises or at their direction to have a workers' compensation carrier in place that has a Best rating of A- or better, which in theory assures the certificate holder that the workers' compensation carrier supplying coverage will be around to pay all claims. Unfortunately, companies such as Legion, Reliance, and Kemper have gone from A ratings to receivership in less than a year, thereby questioning the credibility of this rating process. All the same, if a client company requires rated paper, oftentimes split coverage is necessary.

Uninsurability

It has always been my belief that every employer in the country is a prime candidate for the services a professional employer provides, and as such, the insur-

To the Point...

- There are many valid business reasons to set up your PEO's business model by using multiple carriers, but the actual implementation of such needs to consider the pitfalls.
- Many insurance carriers willing to underwrite PEO business are regional and cannot always cover the current or future geographic footprint of a PEO's client companies.
- Many insurance carriers willing to underwrite PEOs do not have an AM Best rating of A- or better — if a client company requires rated paper, oftentimes split coverage is necessary.
- Unfortunately, many issues arise when more than one workers' compensation policy is issued to the same PEO. The cleanest structure seems to be when a PEO retains multiple federal employer identification numbers (FEINs) under its holding company and is able to have one insurer per FEIN/named insured.

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ability of their workers' compensation exposure should not be the only determinant of what is a viable client company.

Competition

On any given risk within any given jurisdiction, there are insurance carriers that are better suited from a service and pricing standpoint to underwrite a given client company. Why should a PEO limit itself to just one insurance carrier if the insurance carriers it has partnered with understand their roles to the PEO and are happy to underwrite business they receive from the PEO? The whole thought that a PEO should only have one insurance carrier in play at all times is an archaic one, in my opinion, and pigeon-holes the PEO to the target markets of the insurance carrier it has partnered with. If there is an insurance carrier out there that can write a given risk, what is the issue?

The Rationale Behind Split Coverage

Unfortunately, theory sometimes is easier than practicality. Many issues arise when more than one workers' compensation policy is issued to the same PEO. The structure that seems to be the cleanest is when a PEO retains multiple federal employer identification numbers (FEINs) under its holding company and is able to have one insurer per FEIN/named insured. A few PEOs use this structure when they have one insurer confined to a specific state and another insurer with multi-state capabilities or rated paper. When there is more than one workers' compensation carrier covering portions of the same FEIN/named insured, there are some issues that need to be considered.

The biggest exposure to the PEO is the issue of dual coverage. This can occur when a claimant files a claim against another insurance policy of the PEO even though there was never coverage intent. While the exclusive remedy provision should limit the coverage to that of the carrier of record for that particular client company, there have been cases in which two or more carriers have been forced to defend themselves for one claim. We experienced a case in Florida in which the PEO unknowingly allowed an insurance policy that covered a specific client company to lapse. The plaintiff's attorney, upon learning this information, successfully filed a claim against the other insurance carrier, which was forced to provide coverage.

In other cases in which it is concluded there is "duplicate coverage," what generally happens is the carrier the claim is reported to begins benefits and then finds out the employer has duplicate coverage. In Florida, statute dictates that the carrier of record for the same liability with the most recent effective date shall be deemed the carrier of record. If the duplicate coverage is after the first carrier's effective date, it will ask the second carrier to accept the claim and reimburse it for all payments. If the second carrier is not willing to accept the claim, the carriers litigate against each other and the claimant gets caught in the middle. In my experience, the first carrier, to keep favor with the courts, will generally continue benefits until the courts make a decision. However, sometimes both carriers will deny the claim and the claimant will not receive benefits at all until the issue between the carriers is resolved.

The best way to ensure against either of these scenarios is by using an NCCI endorsement, "Designated Workplaces Exclusion Endorsement" — WC 00 03 02. This endorsement allows certain workplace locations/client companies to be specifically excluded from the policy in question, typically the master policy, which excludes client companies that have been set up on individual policies. It also is extremely important to realize that each state has its own statutes in regard to split or duplicate coverage, and others may have some regarding this issue specifically for PEOs. Please note that all jurisdictions a PEO does business in should be examined regarding the issue prior to policies being bound.

Another concern comes from the various state regulators who audit certificates of insurance. If these examiners run across two certificates with the same company name, whether it be a PEO or not, fraud is assumed. The examiners will then conduct an investigation into the matter, which usually includes the client companies (certificate holders) of the PEO. While these situations are typically rectified unless fraud of some sort does exist, it exposes the PEO and its clients to unneeded scrutiny. The NCCI also tracks policy information by FEIN for statistical information purposes and scrutinizes multiple policy activity for one named insured/FEIN. In addition, because all of the experience for one named insured/FEIN rolls up into the same experience modification, tracking the statistical information submitted and ensuring its credibility can also be a challenge.

There are many valid business reasons to set up your PEO's business model by using multiple carriers, but the actual implementation of such needs to take into consideration the pitfalls previously mentioned. The designated premises endorsement is always a great tool to make sure each carrier knows what client companies it is insuring, and more importantly, not insuring. This endorsement should be monitored and updated as new clients are added throughout the year. The ability to have multiple named insureds/FEINs under the same PEO holding company provides a very clear approach if there is only one carrier of record per named insured/FEIN. While this approach still requires scrutinizing the statistical information submitted to the NCCI and rolled up into the experience modification of the PEO, it is the cleanest way of splitting coverage between insurance carriers and there should be no arguments of duplicate coverage and the corresponding issues of such. In terms of the regulators, permission is always better than forgiveness. It is no secret that many states view the industry with a jaundiced eye already and that any deviation from the norm will be looked upon as a way to beat the system. It can never hurt to request an audience with the regulators and review the ways in which the PEO will be providing insurance coverage to its respective client companies. This approach may prevent some surprises in the future for the PEO and its respective client companies. While it is exciting to see many more insurance carriers ready, willing, and able to work with PEOs to provide workers' compensation to their client companies, it should be done in a well thought out manner. After all, every business in the country is a candidate for co-employment.■

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