


# WC'S NEW FRONTIER?

## What Does it Mean for the PEO Master Policy Platform?

Paul Hughes



After taking some severe blows over recent years, the PEO industry has survived through consolidation of the fittest and is poised for growth for years to come. Without a workers' compensation provider of some sort, however, a PEO cannot remain an ongoing concern. In my opinion, the master policy platform provides both the PEO and insurance carrier with the most effective platform to manage the profitability of a book of business.

The ability to manage risk is greatly enhanced through the master policy, with the PEO being able to dictate the use of important cost containment tools such as return-to-work programs and loss prevention incentives via the implementation of the client service agreement. Other ways to provide workers' compensation for client companies are being considered and used due to the lack of capacity in the marketplace, financial commitment of the specific arrangement being considered, and the ability to capture income outside of workers' compensation. These alternatives use different names such as multiple coordinated policies (MCPs), administrative services only (ASO) organizations, and individual client plans. For our discussion, we will refer to all individual client plans as MCPs.

### Threats to the Master Policy Platform

Unfortunately, outside market forces are lining up to threaten the ability to use

master policies. The lack of insurance carrier participation in underwriting PEO business is the foremost threat from which all of the issues seem to stem. The National Council on Compensation Insurance (NCCI) has been lobbying insurance carriers and regulators to adopt a multiple coordinated policy (MCP) platform for PEOs procuring workers' compensation for their client companies. On its Web site, [www.ncci.com](http://www.ncci.com), there is a section on "Employee Leasing" that provides valuable information on different states' requirements for co-employment relationships. It also provides NCCI's opinion on master policy platforms for PEOs, one that is less than reassuring to those of us who believe in that model. The options in working with PEOs include: the multiple coordinated policy approach (MCP); the master policy approach, with automation allowing client company data to be reported on an individual basis; and the master policy approach, with continued manual reporting of client company data. It is readily apparent that the NCCI is the least enamored with the last approach, one which does not allow it to properly collect individual client company data for use in setting rates, experience modifications, and expected loss rates. While many states, such as Florida, have enacted legislation requiring insurance carriers to report individual client data when a master policy is used, most insurance carriers do not have the automation systems to provide NCCI statistical data at the client company level without manual entry. This has somewhat

slowed momentum for the master with automation model, as present and past insurers of PEOs have either been unable to use current legacy systems to provide this data, and/or are unwilling to invest in new systems that will.

Another major force behind the way in which a PEO procures workers' compensation is the National Association of Insurance Commissioners (NAIC). Since 1991, NAIC has been lobbying for the MCP platform, "Whereby separate policies, classifications, and experience modifications are maintained for each client employer." A NAIC model rule for employee leasing mandated MCPs for companies in the state residual market.

NAIC's issues with master policies fall into the four categories of: experience ratings; ensuring all parties receive necessary information in a timely fashion (i.e., termination notices); PEO insolvencies and their effect on client companies and claimants; and most important to these regulators, the ability to identify and verify who is the insured; who is the insurer; and when does coverage begin and end? While some states, such as Louisiana, have mandated the use of multiple coordinated policies, other states, such as California, Texas, and Florida, have enacted their own statutes detailing how PEOs are to operate. At the same time, there are still six NCCI states (Alaska, Colorado, Hawaii, Idaho, Nebraska, and Oklahoma) that do not have any PEO-specific workers' compensation provisions. NAIC also recently came out with a draft white paper on

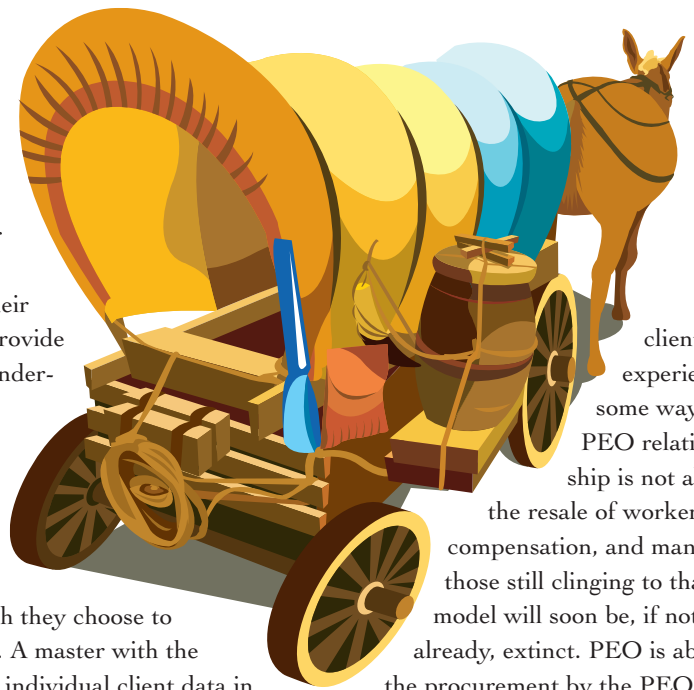
PEOs which questioned the legality of a PEO providing workers' compensation by using a large deductible policy, questioning the very basis of co-employer status (see NAPEO's response in this issue's feature, "PEO Large Deductible Policies Called Serious Risk: NAPEO Challenges Working Group Assertions"). One of NAIC's recent missions has been standardization amongst all of the states in some if not all areas of insurance regulation. There has also been some movement in promoting the federal regulation of insurance versus state-by-state regulation. It should further be noted that the present president of NAIC, Ernst Csiszar from South Carolina, has adopted the MCP model for the residual market in his home state and is on record as supporting it for all PEO arrangements on a national level.

These current market forces are very real, and there is already an NAIC model rules group in place to address the way in which a PEO offers workers' compensation. NCCI's and NAIC's concerns in areas of statistical reporting, insurer/insured relationships, PEO insolvencies, and policy issuance and endorsements still need to be satisfactorily addressed in the opinion of these bureaucratic entities. While it is hoped that through the presentation of effective alternatives and expert testimony about the benefits of PEOs NAPEO will be able to influence these bodies in a way to make any changes palatable to the industry, unfortunately there is no guarantee of the outcome. What is known, though, is that both of these bodies endorse movement toward MCPs or individual client plans, and are well down the road in proposing a new system of some kind to address their areas of concern.

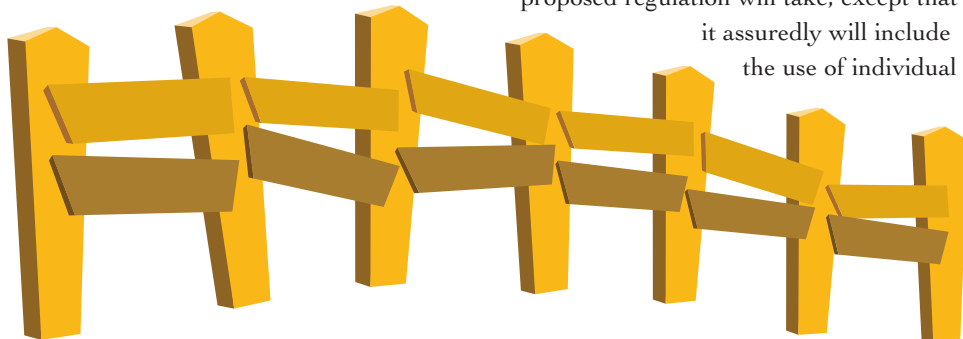
## The New Frontier?

It is still my hope that carriers will be given the option of being able to provide master policies or individual client plans based on their own abilities to provide data, their own underwriting appetites, and their own abilities to manage within the regulatory environments of the states in which they choose to conduct business. A master with the ability to manage individual client data in the same way, as if they were written on individual policies, seems to be the perfect compromise, but many carriers do not seem to want to change their internal legacy systems to meet this challenge. Our firm has deployed an automated payroll system that will allow us to capture payroll and loss information all the way down to the employee level, thereby making it a "push the button" process to provide our carrier-partners and ultimately NCCI and other regulators with the statistical data necessary to track individual clients within a master. We have discussed this platform with both NCCI and a few state regulators, and it has been very well received. Unfortunately though, most still are not able to provide necessary data in managing a master and therefore the regulators have stepped in to address their areas of concern.

Nobody truly knows what shape any proposed regulation will take, except that it assuredly will include the use of individual



client experience in some way. The PEO relationship is not about the resale of workers' compensation, and many of those still clinging to that model will soon be, if not already, extinct. PEO is about the procurement by the PEO and deployment of services in the areas of workers' compensation management, HR, benefits, payroll, and risk management. These services can be provided using a variety of models, each with its own set of pros and cons to the PEO, regulators, and the insurance marketplace. While it is no foregone conclusion that PEOs will lose the ability to use master policies in covering their clients, it could happen, and it would therefore behoove all of us to consider our respective business models in the event individual client plans are mandated. There is an ability to still profitably provide services in the case of individual policies as well as retain most of the controls in place that allow the PEO to be an effective co-employer of the client company. It is not the status quo and will make necessary some significant changes to the ways in which PEOs do business, but if it makes the long-term viability of PEOs more secure, is it not worth it? While not perceived to be best case for the PEO, if this model brings insurers back to the table and makes the industry a more investable model for years to come, we may have lost a battle, but we'll win the war against those who would prefer the PEO model to meet extinction as a whole.



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