

**DEPARTMENT OF INSURANCE****Legal Division, Government Law Bureau**

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**TO:** Certain Interested and Affected Parties  
**FROM:** Christopher A. Citko  
**DATE:** April 30, 2013  
**RE:** Invitation to Pre-Notice Public Discussions on Workers' Compensation  
Insurance Dividend Regulation Amendments and Revisions

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Pursuant to California Government Code Section 11346.45, California Insurance Commissioner Dave Jones will hold Pre-Notice Public Discussions regarding amendments and revisions to California Code of Regulations, Title 10, Chapter 5, Subchapter 3, Article 9, Workers' Compensation, Dividends (Refunds) to Policyholders. You are invited to participate in Pre-Notice Public Discussions. The purpose of these discussions is to permit certain interested and affected persons an opportunity to present statements or comments about the contemplated amendments and revisions.

Public discussions will be held at the following date, time, and location:

Date: June 4, 2013  
Time: 9:00 a.m. to 12:00 p.m. The discussions will end at 12:00 p.m., or as soon after 9:00 a.m. as all those present wishing to speak have done so, whichever is earlier.  
Location: California Department of Insurance  
300 Capitol Mall, 6<sup>th</sup> Floor, Room 635  
Sacramento, CA

Participants are requested to RSVP by May 28, 2013, to one of the contact persons below by providing your name, the name of the organization (if any) that you represent, your mailing address, telephone number, and email address. Space is limited, so we ask that you limit your organization's representation to one individual.

The facility to be used for these public discussions is accessible to persons with mobility impairments. Persons with sight or hearing impairments are requested to notify one of the contact persons below by May 28, 2013 in order to make special arrangements.

All inquiries regarding these Pre-Notice Public Discussions should be directed to one of the contact persons below.

## **DRAFT REGULATIONS ATTACHED FOR DISCUSSION**

For purposes of promoting discussion, below is a draft version of the proposed regulation text. Participants should be prepared to present specific comments on, and alternative language or revisions for, the attached draft regulation text at the scheduled public discussion. All persons are invited to submit written statements, particularly if you are unable to attend in person.

**Please be prepared to specifically provide comment or input regarding the economic impact you believe these proposed regulations may have and how they may or may not affect the creation or elimination of jobs within the State, the creation of new businesses or the elimination of existing businesses within the State, and the expansion of businesses currently doing business within the State.**

## **THIS IS NOT A FORMAL PUBLIC HEARING ON THESE REGULATIONS**

Please be advised that participation in these Pre-Notice Public Discussions will be in addition to, and not a substitute for, participation in any formal rulemaking process that may occur. This invitation to Pre-Notice Public Discussions does not constitute a Notice of Proposed Action under the Administrative Procedure Act. Consequently, comments (verbal or written) received in connection with this Pre-Notice Public Discussion will not be included in the rulemaking file.

The Department is not required to respond to comments received before a Notice of Proposed Action is issued and a rulemaking file opened. For this reason, if you wish to have comments included in the rulemaking file, or to require the Department to respond to them as part of the process by which it may adopt these regulations, it is required that you present your comments during the formal public comment period according to the procedures outlined in the Notice of Proposed Action when it is issued, regardless of whether the comments have been made in connection with these Pre-Notice Public Discussions.

## **CONTACT PERSONS**

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## **DRAFT REGULATIONS FOR PUBLIC DISCUSSION**

Text proposed to be added is displayed in underline type.

Text proposed to be deleted is displayed in ~~strikeout~~ type.

### **Title 10. Investment**

#### **Chapter 5. Insurance Commissioner**

##### **Subchapter 3. Insurers**

###### **Article 9. Workers' Compensation Insurance. Dividends (Refunds) to Policyholders.**

###### **~~Regulations Governing Classification of Risks and Premium Rates, Policy and Endorsement Forms.~~**

###### **§ 2500. Application and Effective Date of Article.**

This article applies to all stock, mutual and reciprocal inter-insurance exchange insurers and to the State Compensation Insurance Fund. ~~The provisions of this article are effective April 1, 1976, except as otherwise provided in Sections 2507.2 and 2508 hereof.~~

Note: Authority cited: Sections 790–790.10 and 12921, 11630–11663 and 11730–11742, Insurance Code. Reference: Sections 380, 381, 383, 750–766, 780–784, 790, 790.01 790.10, 1420, 11630, and 11631–11663 and 11730–11742, Insurance Code.

###### **§ 2501. Purpose.**

Compliance with and enforcement of Insurance Code Sections 380, 381, 383, 750 through 766, 780 through 784, 790 through 790.03, 790.034(a), 790.035, 790.036, 790.04 through 790.10, 1420, 11630, 11650 through 11663, 11730 through 11742, 11751.1 and 12921, and the regulations contained in this article are hereby declared to be necessary in the public interest to protect the rights of injured employees and their dependents, to protect prospective participating workers' compensation policyholders from misrepresentations and unfair practices concerning potential dividends, to prevent certain unfair and coercive practices in the payment of dividends, and to effectuate the purpose of the statutes governing the classification of risks and premium rates and policy and endorsement forms and the approval filing of such forms for workers' compensation insurance.

Note: Authority cited: Sections 790.10, 11739 and 12921, Insurance Code. Reference: Sections 380, 381, 383, 780 through 784, 790 through 790.03, 790.034(a), 790.035, 790.036, 790.04 through 790.10, 1420, 11630, 11650 through 11663, 11730 through 11742, 11751.1 and 12921, Insurance Code.

###### **§ 2502. Relevant Statutes, Rules and Regulations.**

All references to "seetion" herein refer to a seetion of the California Insurance Code unless otherwise stated.

~~Dividends: Workers' compensation insurers are authorized by Section 11738 to issue participating compensation policies. A dividend (refund) under such a policy can only be paid from surplus accumulated from premiums on workers' compensation policies issued pursuant to laws of California governing workers' compensation insurance. However, Section 1420 authorizes, in the case of reciprocal insurers, savings or credits to be returned to subscribers irrespective of the source from which such savings or credits accrue whenever such returns do not constitute an impairment of the assets or reserves required to be maintained.~~

~~Policy Forms: Under Section 11658, all workers' compensation policies and endorsement forms, including participating provisions relating to the payment of dividends thereunder, must be approved as to substance and form by the Commissioner prior to use. Rule III of the "Manual of Rules, Classification and Basic Rates for Workers' Compensation Insurance" (C.A.C. Title 10, Section 2350), provides that the entire contract of insurance, including any agreement with respect to participation thereunder, shall be set forth in the policy, including endorsements, and specifies that no agreement which is not set forth in such policy shall be valid or enforceable.~~

~~Rebate: Section 751 provides that an insurer, insurance agent, broker or solicitor, personally or otherwise, shall not offer or pay, directly or indirectly, as an inducement to enter into an insurance contract any valuable consideration which is not clearly specified, promised or provided for in the policy, or application for the insurance, and any such consideration not appearing in the policy is an unlawful rebate. Section 752 makes it a misdemeanor for the insured or any agent or representative of the insured to knowingly accept or receive any unlawful rebate. Section 763 provides that the payment of a dividend on a participating policy after expiration of the term covered by the policy is not an unlawful rebate.~~

~~Misrepresentation: Under Section 780 and Business and Professions Code Section 17500 it is unlawful for an insurance agent, broker or solicitor to misrepresent the terms or effect of an insurance policy or contract. Sections 780 and 782 make it a misdemeanor for any insurer or agent thereof, or an insurance broker or solicitor, to issue or permit to be issued, circulated or used, any misrepresentation of the terms of a policy, the benefits or privileges thereunder or the future dividends payable thereunder. Under Sections 783 and 783.5, an agent, broker or solicitor's license or an insurer's certificate of authority may be suspended, after hearing, for knowingly violating Section 780.~~

~~Unfair Practices: Section 790.03 prohibits the making, issuing, circulating or causing to be made, issued or circulated, any estimate, illustration, circular or statement misrepresenting the terms of any policy issued or to be issued or the benefits or advantages promised thereby or the dividends or share of surplus to be received thereon, or making any false or misleading statement as to the dividends or share of surplus previously paid on similar policies, or making any misleading representation or any misrepresentation as to the financial condition of any insurer. Section 790.10 empowers the Commissioner to promulgate, after notice and public hearing, reasonable rules and regulations necessary to administer the provisions of the Insurance Code dealing with unfair practices.~~

~~Rating Bureaus: Section 11751.1 provides that the California Inspection Rating Bureau shall not adopt any rule or exact any agreement the effect of which would be to prohibit or regulate the payment of dividends, savings, or unabsorbed premium deposits allowed or returned by insurers to their policyholders or members.~~

~~Group Policies: Section 11656.6 provides that an insurer may issue a workers' compensation policy insuring an organization or association of employers as a group if such organization or association complies with certain conditions. One of the conditions specified in Section 11656.6 requires the organization or association to file certified copies of its articles of incorporation, by-laws or agreements of association and its rules and regulations governing the conduct of its business. Such documents must be filed with the Commissioner or a licensed workers' compensation rating organization designated by him. Section 11656.7 states that each member of an organization insured under a group policy shall be treated as a single and separate entity as respects rates, classifications and rating plan.~~

### **§ 2503. Participating Workers' Compensation Policies -Required Provisions and Notice of Intent to Issue.**

~~Every prospective policyholder, including policyholders renewing existing policies, shall be entitled, on request, to written advice prior to the issuance of each policy, whether the policy is being issued on a participating or nonparticipating basis. Any such written advice shall be subject to the provisions of this article.~~ (a) Every workers' compensation policy issued on a participating basis shall include a participating provision or endorsement indicating that it is a participating policy. All workers' compensation policy forms, including any participating provisions or endorsements, ~~must~~ shall be approved as to substance and form by filed with the Commissioner prior to use.

(b) If a policy is issued on a participating basis, the participating provision or endorsement ~~must~~ shall be designated "Participating Provision" and contain the following language:

"Under California Law it is unlawful for an insurer [us] to promise the future payment of dividends under an unexpired workers' compensation policy or to misrepresent the conditions for dividend payment. Dividends are payable only pursuant to conditions determined by the [our] Board of Directors or other governing board [of the Company] following policy expiration. ~~Forfeiture of a right to, reduction in the amount of, or delay in the payment of, a policyholder's dividend due to the policyholder's failure to accept renewal of the policy or subsequent policies issued by the same insurer is illegal and constitutes an unfair practice.~~"

(c) A workers' compensation insurer may advise a prospective policyholder, directly or through its agent or an insurance broker or solicitor, of the provisions and factors, or the arrangement thereof, that shall be set forth in the participating provision, provided that such advice or provisions and factors shall not set forth or imply, directly or indirectly, the amount of dividend or percentage of premium which will be paid as dividend, or amount or percentage of premium to be retained by the insurer after payment of dividend.

(d) A participatory provision shall set forth any time schedule during which the insurer intends to consider, compute or pay any dividend, if applicable.

Note: Authority cited: Sections 790.10, 10191 and 11739 11659, Insurance Code. Reference: Sections 780 through 784, 790.03, 790.035, 790.04 through 790.07, 11657, 10191, 11658 and 11739 11659, Insurance Code.

#### **§ 2504. Representations Regarding Future Payment of Dividends.**

No workers' compensation insurer or officer or agent thereof or insurance broker or solicitor shall represent, either orally or in writing, as an inducement either to insure or to continue or to renew insurance, that the insurer has agreed or will agree (a) to pay a specified policyholder's dividend or (b) upon a formula, criteria or factors which set forth or can be used to determine the amount of dividend, or percentage of premium to be paid as dividend, or amount or percentage of premium to be retained by the insurer after payment of dividend or (c) to pay a dividend by any plan which is unfairly discriminatory.

Note: Authority cited: Sections 790.10 and 11739, Insurance Code. Reference: Sections 780 through 784, 790.03, 790.035, 790.04 through 790.07, and 11739, Insurance Code.

#### **§ 2505. Policyholder Dividend Statements.**

~~(a) The employment of a "Policyholder Dividend Disclosure Statement" as hereinafter defined shall be mandatory in every circumstance that the annual premium, based upon the best information available, which will be earned during the policy period (the Estimated Annual Premium) shall equal or exceed the sum of \$10,000. In all other circumstances, the employment of such "Dividend Statement" shall be optional at the discretion of the insurer. A workers' compensation insurer may advise a prospective policyholder, directly or through its agent or an insurance broker or solicitor, of the general provisions and factors, or the arrangement thereof, which are expected to be taken into consideration in regard to dividends on a given policy; provided that such provisions and factors shall not set forth or imply, directly or indirectly, the amount of dividend or percentage of premium which will be paid as dividend, or amount or percentage of premium to be retained by the insurer after payment of dividend. Any such advice or statement, whether issued directly to a prospective or current policyholder or issued by an insurer to its agent or a broker, shall be deemed a "Dividend Statement" and shall be subject to the rules set forth in this section.~~

~~(1) A Dividend Statement shall be upon a format prescribed by the Insurance Commissioner and available upon request from his San Francisco and Los Angeles offices. A Dividend Statement shall be in writing and shall include the mandatory language set forth in Section 2503 above. The mandatory language shall appear prior to, and have equal prominence as, any advice regarding such general provisions and factors set forth in the statement. Such Dividend Statement shall also contain, with equal prominence, the following language: "It is a misdemeanor for any insurer or officer or agent thereof, or any insurance broker or solicitor, to promise the payment of future workers' compensation dividends."~~

(2) A Dividend Statement shall include the rate or amount of dividend previously declared or paid on a similar policy or policies or the scale or schedule previously used to determine the amount or rate of dividends. In any such case, however, the Dividend Statement shall also set forth the period covered by policies on which such dividends were paid and that past dividend performance is no guarantee of an insurer's future dividend performance.

(3) A Dividend Statement shall set forth a time schedule during which the insurer intends to consider, compute or pay any dividend.

(4) A Dividend Statement shall include a statement in compliance with Section 2507.2 that forfeiture of a right to, reduction in the amount of, or delay in the payment of, a policyholder's dividend due to the policyholder's failure to accept renewal of the policy or subsequent policies issued by the same insurer is coercive and illegal and constitutes an unfair practice. This statement shall have equal prominence as any advice regarding such general provisions and factors set forth in the Dividend Statement.

(5) A Dividend Statement shall include a statement that, in every situation where the policy develops an annual premium equal to or in excess of the amount of \$10,000 as finally audited and adjusted, a "Policyholder Dividend Result Disclosure Statement," which will provide all essential data employed to compute the dividend result, and which also will compare the factors actually employed in calculation of the dividend result to the factors presented to the policyholder in the Dividend Statement, shall accompany the dividend paid or, where no dividend is paid, shall be provided in place of a dividend.

(a) (b) Whenever a dividend is paid on a workers' compensation policy has developed an annual premium equal to or in excess of the sum of \$10,000 as finally audited and adjusted, a written form captioned "Policyholder Dividend Result Disclosure Statement" shall accompany the dividend paid or, where no dividend is paid, shall be provided in place of a dividend. This statement shall be upon a format prescribed by the Insurance Commissioner and available upon request from his San Francisco or Los Angeles office.

(1) The Policyholder Dividend Result Disclosure Statement must shall identify the policyholder and the insurer, the policy to which the statement applies, and the term of said policy.

(2) The Policyholder Dividend Result Disclosure Statement shall present the calculation of the dividend result, and shall provide the policyholder with all essential data provided to compute the dividend result. In the event that the insurer has also issued a Dividend Statement to the policyholder or his agent, broker, or solicitor in conjunction with the policy term for which the dividend is to be calculated and to which the Policyholder Dividend Result Disclosure Statement applies, then and in such event the Policyholder Dividend Result Disclosure Statement must also compare the factors employed in calculation of the actual dividend result to the factors presented to the policyholder when the policy was issued.

(3) When no dividend is paid, the Policyholder Dividend Statement shall state the reason or reasons for non-issuance of a dividend for that participating policy.

(b) In presentation of the calculation of any dividend result, the Policyholder Dividend ~~Result Disclosure Statement~~ shall show such calculation in columnar form in both actual dollars and percentage of earned premium, and shall present such figures and percentages for the earned premiums, the incurred losses, the Incurred But Not Reported losses (IBNR), if any, the ~~Loss Development Factor (LDF)~~, if any, the insurer retention, and any other factors pertinent to the actual dividend result. Within the context of this paragraph, the ~~IBNR Incurred But Not Reported losses and the LDF Loss Development Factor~~ are deemed pertinent factors sufficient to warrant separate identification and disclosure, if applicable. ~~In the event that the insurer has issued a Dividend Statement in conjunction with the policy term, the Policyholder Dividend Result Disclosure Statement shall also repeat these factors in actual dollars and percentages of estimated premium for comparison purposes and disclose any differences for the benefit of the policyholder.~~

(c) A ~~Dividend Statement and~~ Policyholder Dividend ~~Result Disclosure Statement~~ prepared in compliance with these sections shall be delivered to the organization or association or the administrator thereof in the event that the insurer will issue a workers' compensation policy insuring an organization or association of employers as a group in compliance with Section 11656.6 of the Insurance Code, in addition to being issued to each employer of the organization or association.

(d) If a policy of insurance is issued, continued or renewed and a ~~Policyholder Dividend Disclosure Statement or~~ Policyholder Dividend ~~Result Disclosure Statement~~ is issued in connection therewith by the insurer, a copy of such Dividend Statements shall be retained by the insurer with a copy of the policy, and shall be available for audit by the Insurance Department. Where the Dividend Statements ~~are~~ provided to the policyholder through an agent, broker or solicitor, such agent, broker or solicitor shall also retain a copy of the Dividend Statements with a copy of the policy.

(e) ~~The provisions of this section relating to the mandatory form, content, delivery or retention of a Policyholder Dividend Disclosure Statement shall be applicable to workers' compensation policies incepting or renewing on and after April 1, 1985. The provisions of this section relating to the mandatory form, content, delivery or retention of a Policyholder Dividend Result Disclosure Statement shall be applicable to dividend results arising from a workers' compensation policy expiring on or after January 1, 1985.~~

Note: Authority cited: Sections 790.10, 1727, 1857, 10191 and 11739 11734, Insurance Code.  
Reference: Sections 750, 763, 780, 790.02 10191, 11656.6, 1165 8, 11739 and 11752.6 11738, Insurance Code.

## **§ 2506. Sanctions for Unfair Practices or Misrepresentations Regarding Workers' Compensation Dividends.**

Any representation as to future dividends, or statements as to prior dividends declared or paid, issued by any insurer, agent, broker, or solicitor to induce a prospective policyholder to accept a policy, or to induce a policyholder to retain or renew a policy, failing to conform to this article

shall be deemed an unfair practice or misrepresentation, subject to sanctions set forth in Insurance Code Sections 782, 783, 783.5 and 790.04 et seq.

Note: Authority cited: Section 790.10 and 10191, Insurance Code. Reference: Sections 780-784, 790 through 790.03, 790.034(a), 790.035, 790.036, 790.04 through 790.10, 10191 and 11658, Insurance Code.

### **§ 2507. Declaration by Board of Directors or Other Governing Board.**

No right to a policyholder's dividend under a workers' compensation insurance policy, or to the application or use of any plan, scale, table, formula or schedule to determine whether any dividends shall be paid or allowed or the amount thereof, shall accrue unless and until the Board of Directors or other governing body of the insurer shall have determined that the insurer has a surplus from which dividends may lawfully be paid and shall have declared such dividends by resolution adopted after the expiration of the term covered by the policy.

Each declaration of policyholder's dividends for workers' compensation insurance policies by the Board of Directors or other governing board of the insurer shall identify by policy inception or expiration dates the body of policies to which such declaration is applicable and shall specify the dividend plans, scales, tables, formulas or schedules applied or to be applied to determine whether any dividends shall be paid or allowed or the amounts thereof to be allocated to separate policies pursuant to such declaration.

Note: Authority cited: Sections 790.10, 11735 and 11739, Insurance Code. Reference: Sections 1420, 4050-4052, 11739, 11775 through 11777, Insurance Code.

#### **§ 2507.1. Prohibition Against Unfair Discrimination.**

Allocation of dividends shall not be unfairly discriminatory. The dividend plans, scales, tables, formulas or schedules specified in the declaration may provide for allocation of dividends as a flat percentage of premiums or may provide for variations in the amounts of dividends or the percentages of premium paid as dividends based upon loss or expense factors or any other reasonable considerations, such as size, location, hazard, industry or trade classification, which have a probable effect on losses or expenses. Failure to apply in a consistent manner the plans, scales, tables, formulas or schedules adopted and specified in a declaration of dividends shall be prima facie evidence of unfair discrimination except that any variation from such adopted procedures set forth in ~~the policy or endorsement thereto a dividend statement~~, pursuant to Section 2505 hereof, which has been provided to the policyholder prior to inception of his policy shall not be deemed to be unfairly discriminatory.

Note: Authority cited: Sections 790.10 and 11739, Insurance Code. Reference: Sections 790.03 and 11739, Insurance Code.

## **§ 2507.2. Prohibition Against Unfair Forfeiture of Dividend for Failure to Renew.**

- (a) Forfeiture of a right to, reduction in the amount of, or delay in the payment of, a policyholder's dividend due to the policyholder's failure to accept renewal of the policy or subsequent policies offered by the same insurer is coercive and illegal and shall constitute an unfair practice.
- (b) This section shall not be deemed to prohibit a reasonable reduction in the amount of a policyholder dividend if
- (1) the policyholder has elected to be considered for policyholder dividends under a plan which utilizes the premium and loss experience of the policyholder for two or more policy years, and
  - (2) the nature of the adjustment is set forth in ~~a Dividend Statement which the policy or by an endorsement has been provided attached~~ to the policyholder within thirty days after the inception of the first policy year for which such election has been made, and
  - (3) the policyholder does not remain insured by the same insurer during the complete term of the multi-year dividend plan. In the context of this paragraph, a "reasonable reduction" in the amount of policyholder dividends is defined as and specifically limited to the application of that most favorable dividend plan for which the policyholder then qualifies under the dividend procedures of the insurer unless some alternative dividend plan has been set forth in the ~~policy or an endorsement thereto~~ Dividend Statement provided the policyholder.
- (e) Paragraphs (a) and (b) herein are effective with respect to all workers' compensation dividends declared or payable after the effective date hereof.

Note: Authority cited: Sections 790.10 and 11739 ~~11734~~, Insurance Code. Reference: Sections 750, 763, 780, 790.02, 790.03, 790.035, 790.04, 790.05, 790.06, 790.07, 11739, and 11776 ~~11738~~, Insurance Code.

## **§ 2508. Group Policies -Reduction or Forfeiture of Member's Right to Distribution of Dividend Funds.**

To avoid any coercion or possible misrepresentation of dividends ~~which that~~ may be paid to members of organizations or associations of employers insured under group workers' compensation policies, no group policy shall be issued ~~to become effective on and after July 1, 1976~~, unless the articles of incorporation, by-laws, agreements of association, or rules and regulations filed pursuant to Insurance Code Section 11656.6 shall provide that (1) any distribution of funds to any member, derived from a dividend, shall not be reduced or forfeited except for reasons set forth in the articles of incorporation, by-laws, agreements of association, or rules and regulations, and (2) no such reduction or forfeiture shall be made effective unless the reasons for such reductions or forfeiture have been made known by written communication to the member prior to inception of his insurance coverage during the policy period for which such dividend adjustment is made.

Note: Authority cited: Sections 790.10 and 12921, Insurance Code. Reference: Sections 790.03, 11656.6 and 11739, Insurance Code.

**§ 2509. False or Deceptive Documents.**

No workers' compensation insurer or officer or agent thereof, or other insurance broker or solicitor shall adopt or cause or permit to be issued, circulated or used any representation, plan, schedule, letter or advertising material of any kind stating or implying that any insurer has acted or will in the future act in any manner at variance with this article.

Note: Authority cited: Sections 790.10 and 12921, Insurance Code. Reference: Sections 780 through 784, 790.03 and 11739, Insurance Code.