

# Review of Professional Employer Organizations and Workers' Compensation

Report 21-04

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# OPPAGA

Office of Program Policy Analysis and Government Accountability

# Review of Professional Employer Organizations and Workers' Compensation

## EXECUTIVE SUMMARY

Professional employer organizations (PEOs) are businesses that provide comprehensive human resources services, including workers' compensation coverage, to client companies. Florida statutes require all employers, with limited exceptions, to provide workers' compensation insurance for their employees.

The Department of Business and Professional Regulation licenses and regulates PEOs as employee leasing companies through the Board of Employee Leasing Companies. The board rarely finds that employee leasing companies have violated workers' compensation requirements.

The Office of Insurance Regulation regulates the state's workers' compensation policy coverage forms and rates, licensing and solvency of insurance carriers, market conduct, and policyholder disputes under s. 627.291, *Florida Statutes*, while the Department of Financial Services' Division of Workers' Compensation is responsible for enforcing employer compliance with coverage requirements.

Although PEOs offer workers' compensation coverage as a service, typically, the PEO itself is not providing the coverage; instead, the PEO obtains coverage from a workers' compensation insurance carrier. PEO arrangements can create differences in workers' compensation coverage, including which workers are covered, how experience modification factors are created, and how much notice a business receives before coverage is cancelled.

The relationship between a PEO and its client companies can lead to a workers' compensation coverage gap in several ways, which include reporting issues, employee/employer disputes, and financial issues.

### REPORT SCOPE

This report provides background information on professional employer organizations and Florida's workers' compensation requirements and answers six questions.

1. What is the relationship between PEOs and insurance carriers, and how might workers' compensation coverage differ for businesses that use PEOs?
2. How can the relationship between a PEO and its client companies lead to a workers' compensation coverage gap?
3. What has been the history of PEO-related workers' compensation insurance carrier insolvencies in Florida?
4. Can PEOs offering workers' compensation coverage have an effect on the workers' compensation insurance market, including premiums for other businesses?
5. How have other states addressed PEO regulation and PEO-related workers' compensation insurance coverage gaps?
6. What options could the Legislature consider to address PEO regulation and PEO-related workers' compensation insurance coverage gaps?

Since 2000, four insurance carrier insolvencies have occurred with Florida carriers that historically wrote large deductible workers' compensation policies for PEOs; only two of the four insolvencies were directly attributed to a PEO.<sup>1</sup> The Florida Workers' Compensation Insurance Guaranty Association identified 21 insurance carriers that, since 1997, had claims the association paid on behalf of policyholders involved in the employee leasing industry. Industry stakeholders report that PEO-related insurance carrier insolvencies can be a result of PEOs holding large deductible policies.

Some stakeholders reported that PEOs affect workers' compensation insurance rates, but OPPAGA was unable to find data to show that these factors have actually affected the Florida workers' compensation market. However, there are ways in which a PEO could pass on risk that could affect other businesses' premiums, including denying claims for subcontractors' employees or maintaining risk through large deductible policies.

OPPAGA reviewed 14 states' regulation of PEOs and whether they have adopted legislation that addresses PEO-related workers' compensation coverage gaps. Other states vary in how they regulate PEOs; most states we reviewed house PEO regulation in departments that regulate insurance or labor. Some of these states have enacted legislation or made policy changes to avoid PEO or insurer insolvencies, ensure uninterrupted payment of benefits to injured workers, address full workforce coverage, notify clients of termination of coverage, and/or address reporting issues.

To address the issues identified throughout this report, OPPAGA identified a number of options for legislative consideration. The options are grouped into three categories: options to minimize the risk of coverage gaps; options to enhance claim handling and insurance coverage; and options to modify state regulatory authority.

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<sup>1</sup> While an additional carrier that went insolvent may have issued large deductible policies, Department of Financial Services staff reported that information on this estate was very limited and therefore insufficient to determine if this insolvency occurred as a result of a PEO.

# BACKGROUND

## Professional employer organizations

**Professional employer organizations (PEOs) are businesses that provide comprehensive human resources services.** PEO clients are generally small and medium-sized businesses that want assistance with operational functions of employee management while retaining the direct supervision of the employees so that they may focus on the core mission of the business. These services may include payroll; insurance such as unemployment, disability, and workers' compensation; other employee benefits; and tax administration. PEOs offer regulatory expertise and cost savings through economies of scale.<sup>2</sup> (See Appendix A for a comprehensive list of services that PEOs may provide.)

The arrangement that PEOs provide to client businesses is called employee leasing. Under an employee leasing arrangement, an employer assigns its employees to a PEO for a fee and becomes a PEO client. It then leases back its employees from the PEO. Under this type of arrangement, the direction of and control over the leased employees are allocated to the client.

In Florida, PEOs are licensed and regulated as employee leasing companies (ELCs) under Ch. 468, Part XI, *Florida Statutes*.<sup>3</sup> Some state agencies refer to PEOs as ELCs. While we predominantly use the term PEO throughout this report, we also apply the term ELC where we discuss the particular entity that uses that term.

## Florida's workers' compensation requirements and benefits

**Florida statutes require all employers, with limited exceptions, to provide workers' compensation insurance for their employees.**<sup>4,5</sup> Requirements for workers' compensation coverage vary by industry type, number of employees, and organization type. (See Exhibit 1.) The goal of the Florida workers' compensation system is that the injured worker receives a portion of their lost wages and medical treatment immediately and in exchange, gives up their right to sue the employer for negligence and cannot receive compensation for pain and suffering.<sup>6</sup>

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<sup>2</sup> Goodner and Ramsey. "Certified Professional Employer Organizations and Tax Liability Shifting: Assessing the First Two Years of the IRS Certification Program." *Berkeley Business Law Journal* (2019): 571-601. <https://doi.org/10.15779/Z38QB9V61D>

<sup>3</sup> Chapter [468, Part XI](#), *F. S.*

<sup>4</sup> Sections [440.10](#) and [440.38](#), *F. S.*

<sup>5</sup> Exemptions in s. [440.05](#), *F.S.*, include business owners that opt out of the insurance coverage protections for themselves. Section [440.02](#), *F.S.*, maintains that employment requiring workers' compensation insurance does not include non-construction private employment when less than four employees are employed by the same employer; service performed by or as domestic servants in private homes; agricultural labor that employs five or fewer regular employees and that employs fewer than twelve other employees at one time for seasonal agricultural labor that is completed in less than 30 days but does not exceed 45 days in the same calendar year; professional athletes; labor under a sentence of a court to perform community services; and state prisoners or county inmates, except those performing services for private employers.

<sup>6</sup> Section [440.11](#), *F.S.*

## Exhibit 1

### Employer Workers' Compensation Coverage Requirements Vary by Type of Industry, Company, or Organization

Type of Industry, Company, or Organization	Number of Employees for Required Workers' Compensation Coverage	Additional Requirements
Agricultural	Six or more regular employees or 12 or more seasonal workers who work 30 days or more during a season and more than 45 days in a calendar year	N/A
Construction	One or more	N/A
Non-Construction	Four or more	N/A
Construction Contractor	N/A	Required to ensure that all sub-contractors have the required workers' compensation insurance before they begin to work on a project (r. 69L-6.032, F.A.C). If the subcontractor is not covered or is exempt and an injury occurs, the contractor becomes the statutory employer of the subcontractor's employees, and its insurance carrier is responsible for paying the benefits for the injury, illness, or fatality.
Employee Leasing Company (Professional Employer Organization)	N/A	If an employer enters into an employee leasing agreement with a licensed employee leasing company, the agreement entails workers' compensation coverage only for employees listed with the employee leasing company. The client company is responsible for coverage for all non-leased employees.
Out-of-State Employer	N/A	Must notify insurance carrier they are working in Florida. If the employer has no coverage, they are required to obtain a Florida workers' compensation insurance policy with a Florida-approved carrier.

Source: OPPAGA analysis of DFS Division of Workers' Compensation guidelines.

Businesses may secure workers' compensation coverage from several sources, including

- a Florida-licensed insurance agent in the voluntary market;
- the Florida Workers' Compensation Joint Underwriting Association if two non-affiliated workers' compensation insurers in the voluntary market have rejected the employer within the last 60 days (also known as the residual market); and
- a professional employer organization.<sup>7</sup>

In addition, an employer may become individually self-insured and secure the payment of workers' compensation by providing proof of financial strength necessary to ensure timely payments of current and future claims to the Division of Workers' Compensation pursuant to Ch. 440.38, *Florida Statutes*.

The *Florida Statutes* establish additional workers' compensation requirements specific to the construction industry. Section 440.10(1)(b), *Florida Statutes*, provides that if a general contractor sublets any part or parts of their contract work to a subcontractor or subcontractors, all of the

<sup>7</sup> The voluntary market consists of insurers that offer insurance in a competitive environment and thus retain the right to accept or reject business. The residual market is the market of last resort for those who cannot obtain coverage in the voluntary market. The Florida Workers' Compensation Joint Underwriting Association is the designated residual market for workers' compensation in Florida.

employees of such contractor and subcontractor(s) engaged on such contract work shall be deemed to be employed in one and the same business or establishment. The contractor is liable for, and shall secure, the payment of workers' compensation to all employees, except to employees of a subcontractor who has secured such payment. This requirement is often referred to as the 'up-the-chain' requirement.

Injured workers are eligible for compensation when they are unable to work for more than seven days. If a worker cannot work at all, they should receive compensation equaling about two-thirds of their regular wages, payable beginning on the eighth day they lose time from work.<sup>8</sup> For a critical injury, they may receive 80% of their regular wages for up to six months after the accident. An injured worker can receive up to a total of 260 weeks of temporary total disability and/or temporary partial disability benefits.<sup>9</sup>

## Regulation of PEOs in Florida

**The Department of Business and Professional Regulation (DBPR) licenses and regulates PEOs as employee leasing companies.** DBPR is responsible for licensing and regulating Florida businesses and professions. The department provides administrative support to 12 professional boards that represent various professions, including ELCs. The Board of ELCs licenses and regulates ELCs and promulgates rules to implement the provisions of Ch. 468, Part XI, *Florida Statutes* (s. 468.520 to 468.535, *Florida Statutes*). This includes reviewing applications for licensure and disciplinary cases and conducting informal hearings relating to licensure and discipline.

The board consists of seven members. Five board members are individuals already engaged in the employee leasing industry and two are Florida residents who have never had connections with the industry.<sup>10</sup> Board members are appointed by the Governor and confirmed by the Senate to four-year terms beginning upon appointment and continuing until their successors are appointed.

DBPR assigns several staff to support ELC oversight. The board is administratively supported by three employees from the DBPR's Division of Professions who split their time between providing administrative support to the Board of ELCs and other boards. In addition, one full-time equivalent position (FTE) in DPBR's Division of Regulations investigates complaints, audits ELCs' quarterly and annual financial reports, and reviews each ELC to determine if it has violated or is in danger of violating state law or department or board rule.<sup>11,12</sup> This includes verifying that each ELC has the required workers' compensation coverage. DBPR's Office of General Counsel prosecutes any violations confirmed by the investigator before the board, including unlicensed activities. (See Exhibit 2.)

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<sup>8</sup> The first 7 days lost from work are only paid if the worker loses more than 21 days from work.

<sup>9</sup> Although s. [440.15\(2\)\(a\)](#), *F.S.*, provides for a limit of 104 weeks for disability benefits, in *Westphal v. City of St. Petersburg*, 194 So. 3d 311 (Fla. 2016), the Florida Supreme Court found that this limit was unconstitutional. The court directed that the limit be returned to the statute in effect preceding 1994 amendments. This returned the limit to 260 weeks for disability benefits.

<sup>10</sup> Section [468.521](#), *F.S.*

<sup>11</sup> Chapter [455](#), *F.S.*

<sup>12</sup> Section 61G7-10.001 (1), *F.A.C.*

## Exhibit 2

### DBPR Assigns Several FTEs to ELC Oversight Activities

Unit	Staffing	Duties
Division of Professions	3 staff representing 1.5 FTE <ul style="list-style-type: none"><li>• 1 executive director</li><li>• 1 government analyst</li><li>• 1 administrative assistant</li></ul>	<b>Executive director</b> —liaison between the board and the department <b>Government analyst</b> —reviews ELC applications for completeness and manages the board activities, including setting meeting agendas, noticing meetings, recording meetings, completing minutes, and updating the department with meeting outcomes <b>Administrative assistant</b> —secures board meeting venues, arranges travel, and manages board expenses
Division of Regulation	1 FTE investigator	Investigates all employee leasing complaints
Office of General Counsel	1 FTE attorney	Prosecutes complaints for the board

Source: OPPAGA analysis of staffing information provided by DPBR.

The board's funding is provided through licensing and application fees.<sup>13</sup> Additionally, regulatory activities are supported by annual assessments from each ELC and ELC group.<sup>14</sup> For Fiscal Year 2019-20, the revenues and expenses related to DBPR's regulation of ELCs were approximately \$797,000 and \$536,000, respectively. (See Exhibit 3.)

## Exhibit 3

### Revenues and Expenses for DBPR Regulation of ELCs Fluctuated From Fiscal Year 2017-18 to Fiscal Year 2019-20

Fiscal Year	Board of ELCs		Unlicensed ELC Activity		Total Related to the Regulation of ELCs	
	Revenues	Expenses	Revenues	Expenses	Revenues	Expenses
2019-20	\$792,681	\$533,532	\$4,601	\$2,095	\$797,282	\$535,627
2018-19	\$248,495	\$504,148	\$1,273	\$508	\$249,768	\$504,657
2017-18	\$760,072	\$608,103	\$3,597	\$1,181	\$763,669	\$609,284

Source: OPPAGA analysis of revenue and expense data provided by DBPR.

**Since Fiscal Year 2010-11, the Board of ELCs had full membership during one fiscal year.** In 3 of the last 10 fiscal years, the board has lacked any resident member representation. During the 10-year period, the number of board members ranged from two to seven. DBPR staff report that the lack of full membership has not affected the board's ability to carry out its duties and achieve a quorum for meetings.

**The Board of ELCs rarely finds that ELCs have violated workers' compensation coverage requirements.** The board, under r. 61G7-7.001, *Florida Administrative Code*, may assess penalties to ELCs and controlling persons for noncompliance or violations that are confirmed by DBPR investigators and brought before the board. Since 2014, 713 unique complaints were brought before the board for violations of noncompliance. Eleven of the complaints (or 1.5% of the cases) were directly related to workers' compensation; the board found cause to assess fines or costs totaling \$12,035 (around 2.6% of all fines and assessments) for eight of these complaints.

<sup>13</sup> Section [455.219](#), *F.S.*

<sup>14</sup> Rule [61G7-10.001\(1\)](#), *F.A.C.*

## State agencies with oversight responsibility over workers' compensation insurance

**The Office of Insurance Regulation (OIR) and the Department of Financial Services (DFS) have workers' compensation regulation and oversight responsibilities.** As discussed above, DBPR verifies that PEOs have workers' compensation coverage. DFS' Division of Workers' Compensation is responsible for enforcing employer compliance with coverage requirements, and two additional units within DFS have roles in workers' compensation regulation. The Office of Insurance Regulation regulates the state's workers' compensation policy coverage forms and rates, licensing and solvency of insurance carriers, market conduct, and policyholder disputes under s. 627.291, *Florida Statutes*.

DFS' Division of Workers' Compensation is responsible for enforcing employer compliance with the coverage requirements of the workers' compensation law.<sup>15</sup> All insurers are required to report proof of coverage information to the division; this information becomes part of the data the division makes publically available on proof of coverage. The division's compliance investigators can enter and inspect any place of business to ensure employer compliance with workers' compensation law and request an employer's business records. During the inspection, if compliance investigators determine that the company is a PEO client, they will match each employee on the job site with the PEO's employee roster. If an employee is not on the roster, investigators will issue a stop-work order.

In addition, the DFS Division of Rehabilitation and Liquidation resolves insurance carriers' liabilities when carriers are placed in receivership or liquidation. The DFS Division of Investigative and Forensic Services, Bureau of Workers' Compensation Fraud, working jointly with DBPR, federal agencies (the Internal Revenue Service, the Department of Homeland Security, and the Department of Labor), and multiple local law enforcement agencies, investigates suspected criminal violations of Florida's workers' compensation laws. This bureau's activities include preventing and prosecuting unlicensed contractors, businesses employing workers without appropriate workers' compensation coverage, employees who file false on-the-job injuries or exaggerate their injuries, and employees working other jobs while receiving workers' compensation benefits.

OIR is responsible for all activities concerning insurers and other risk bearing entities, which includes ensuring that insurance carriers licensed to do business in Florida are financially viable, operate within the laws and regulations governing the industry, and offer insurance policy products at fair and adequate rates that do not unfairly discriminate against the public. Although OIR is within the Financial Services Commission, which is administratively housed within DFS, OIR is not subject to control, supervision, or direction by the department. OIR licenses insurance carriers, including property and casualty insurers, monitors insurance operations in terms of market conduct, and reviews and approves policy coverage forms and rates for insurance carriers. It licenses and processes carriers that want to write workers' compensation insurance in Florida. OIR also conducts financial examinations and ongoing financial analysis of workers' compensation insurance carriers and self-insurance funds. Further, it reviews insurance carriers' solvency to ensure compliance with minimum surplus requirements and ensure that companies have competent management.

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<sup>15</sup> The division also audits insurers for the timely and accurate payment of benefits for injured workers and the timely and accurate reporting of workers' compensation claims information to the division. In addition, it assists employees with questions or concerns about workers' compensation claims, works on behalf of workers to resolve issues, and educates the public on their rights and responsibilities regarding workers' compensation. The division assesses the workers' compensation trust fund rates and special disability trust fund rates against all insurers that are writing workers' compensation and collects these assessments to fund the division and numerous other workers' compensation activities. The division is further responsible for authorizing and regulating individual self-insurers in accordance with recommendations provided by the Florida Self-Insurers Guaranty Association.



DBPR, DFS, and OIR each have different responsibilities with respect to workers' compensation regulation and oversight. The roles of DFS and OIR regarding workers' compensation coverage are relevant to all Florida businesses, while DBPR is the only regulatory entity in this context with a role that is specific to PEOs. (See Exhibit 4 for more detail and side-by-side comparison of the various roles of these entities that apply to the regulation of workers' compensation coverage.)

#### Exhibit 4

#### Multiple State Agencies Have Roles in the Oversight and Regulation of Workers' Compensation Coverage for Florida Businesses; DBPR's Role is Specific to PEOs

Workers' Compensation Oversight Roles and Activities			
Function	DBPR	DFS	OIR
General workers' compensation insurance regulation	N/A	<ul style="list-style-type: none"> <li>Processes applications for workers' compensation exemptions.</li> <li>Provides information on employer workers' compensation compliance and employee claims.</li> <li>Authorizes businesses that want to self-insure.</li> <li>Serves as the receiver of insurers placed into receivership in Florida and resolves insurance carriers' liabilities.</li> <li>Prevents and prosecutes workers' compensation fraud.</li> </ul>	<ul style="list-style-type: none"> <li>Ensures licensed insurance carriers, including property and casualty, are financially viable; monitors operations in terms of market conduct; and reviews and approves policy coverage forms and rates for insurance carriers.</li> <li>Processes carrier applications that want to write workers' compensation insurance.</li> </ul>
Inspecting licensee operations	<ul style="list-style-type: none"> <li>Verifies employee leasing company (PEO) workers' compensation coverage.</li> </ul>	<ul style="list-style-type: none"> <li>Actively monitors businesses' workers' compensation coverage, including PEO and individual businesses.</li> <li>Regulates businesses that want to self-insure and monitors purchase of reinsurance policies.</li> </ul>	<ul style="list-style-type: none"> <li>Monitors insurance carriers' operations in terms of market conduct.</li> </ul>
Examining/auditing financial condition of licensees	<ul style="list-style-type: none"> <li>Audits and reviews ELCs' quarterly and annual financial statements for positive net worth and working capital.</li> </ul>	<ul style="list-style-type: none"> <li>Audits timely reporting and payment of workers' compensation claims.</li> </ul>	<ul style="list-style-type: none"> <li>Conducts financial examinations and ongoing financial analysis of workers' compensation carriers and self-insurance funds.</li> <li>Reviews insurance carriers' solvency to ensure compliance with minimum surplus requirements and ensure that the company has competent management.</li> </ul>
Investigating complaints against licensees	<ul style="list-style-type: none"> <li>Investigates complaints against ELCs, ELC groups, ELC group members, controlling persons, de minimus ELCs, etc.</li> </ul>	<ul style="list-style-type: none"> <li>Investigates and inspects jobs sites for workers' compensation compliance.</li> <li>Investigates suspected criminal violations of Florida's workers' compensation laws.</li> </ul>	<ul style="list-style-type: none"> <li>Monitors complaints of insurance carriers' operations in terms of market conduct.</li> </ul>
Disciplinary authority	<ul style="list-style-type: none"> <li>The Board of ELCs may discipline, including assessing costs for violations of Ch. 455, <i>F.S.</i>, Ch. 468, Part XI, <i>F.S.</i>, or rules promulgated. These reasons for discipline include failing</li> </ul>	<ul style="list-style-type: none"> <li>Enforces employer compliance, in accordance with s. 440.107(3), <i>F.S.</i>, including (1) conducting investigations and inspections, (2) issuing stop work orders, and (3) imposing financial penalties.</li> <li>Prosecutes unlicensed contractors, businesses that employ workers</li> </ul>	<ul style="list-style-type: none"> <li>Enforces the provisions of Chs. 624 and 625, <i>F.S.</i>, and applicable rules as they relate to the review of property and casualty insurer solvency.</li> <li>Enforces the provisions of Chs. 627 and 626, <i>F.S.</i>, and</li> </ul>

Workers' Compensation Oversight Roles and Activities			
Function	DPBR	DFS	OIR
	to maintain workers' compensation or misclassification of employees for workers' compensation.	without appropriate workers' compensation coverage, employees who file false on-the-job injuries or exaggerate their injuries, and employees that work other jobs while receiving workers' compensation benefits, in accordance with s. 440.107(8), F.S.	applicable rules as they relate to the review of property and casualty contracts and associated rates.
Oversees licensees through a board	• Yes	• No	• No
FTEs dedicated to workers' compensation monitoring, oversight, and investigation	• 1 FTE examining/auditing licensees' financial documents and investigating complaints.	• 41 FTEs monitor and audit workers' compensation insurers to ensure benefit payments. • 146 FTEs verify that employers comply with workers' compensation laws.	• 248 FTEs dedicated to ensuring proper function of insurers, including reviewing the solvency and working capital of insurers. • 3 FTEs specifically dedicated to reviewing rates and forms that the workers' compensation insurance carriers use.

Source: OPPAGA analysis of information provided by DBPR, DFS, and OIR; interviews with agency officials; and review of agency websites.

## Size of the PEO industry and types of businesses they serve

**The size of Florida's PEO industry has increased during the past several fiscal years.** The Department of Economic Opportunity (DEO) collects employment data from all employers based on their reporting and payment of reemployment taxes to the Department of Revenue. PEOs are statutorily required to report employment data to the state on a quarterly basis; however, not all PEOs report data broken out by individual client companies.<sup>16</sup> OPPAGA received information on trends in PEO employment and wages for Fiscal Year 2016-17 through Fiscal Year 2018-19, and because complete data was not available for Fiscal Year 2019-20 at the time of this review, we analyzed DEO employment and wage data from the first quarter of 2020.

The number of PEOs in the state has increased from 677 in Fiscal Year 2016-17 to 760 as of March 2020. The average fiscal year employment increased from 537,930 in Fiscal Year 2016-17 to 572,798 in Fiscal Year 2018-19, and fiscal year average wages increased from \$39,636 in Fiscal Year 2016-17 to \$42,995 in Fiscal Year 2018-19. (See Exhibit 5.)

### Exhibit 5

#### The Size of Florida's PEO Industry Increased From Fiscal Year 2016-17 Through Fiscal Year 2018-19

Fiscal Year	Number of PEOs in June	Total Fiscal Year Wages	Fiscal Year Average Employment	Fiscal Year Average Wage
2016-17	677	\$21.3 billion	537,930	\$39,636
2017-18	679	\$22.5 billion	549,211	\$41,032
2018-19	726	\$24.6 billion	572,798	\$42,995

Source: Department of Economic Opportunity.

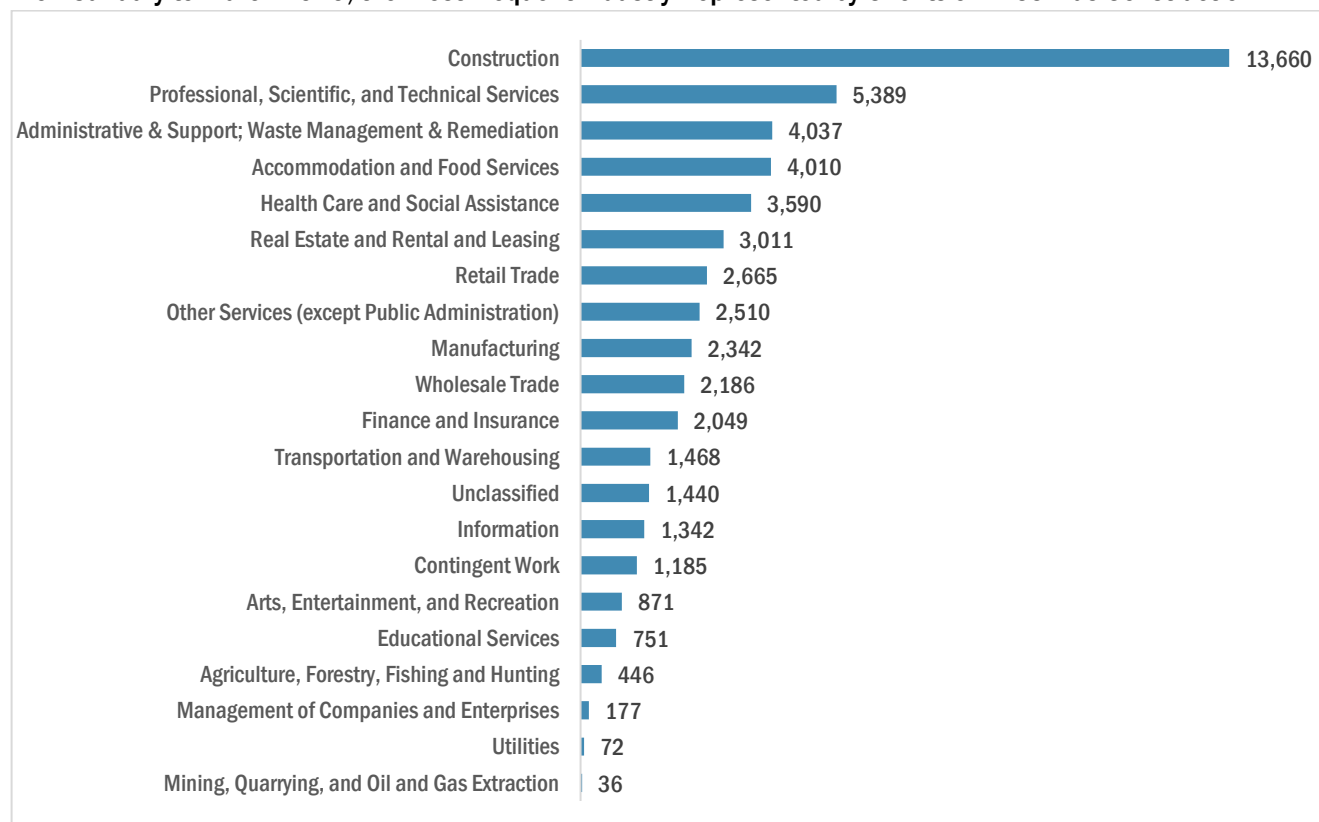
<sup>16</sup> Section [443.036\(18\)](#), F.S.

While PEOs are required to report employment data broken out by individual clients, most PEOs report aggregate data to the state. In the data OPPAGA analyzed for January through March 2020, 332 of 760 PEOs reported employment data broken out at the client level. These PEOs reported 53,237 total client companies with \$6.3 billion in payroll, representing an average employment of 562,469 and an average wage of \$11,194. The remaining 428 PEOs reported aggregate employment data not broken out at the client level, totaling \$111 million in payroll, representing an average employment of 9,118 and an average wage of \$12,146. DEO staff report that these PEOs are more likely to be smaller and have fewer than 10 clients each. This is supported by the fact that they account for approximately 1% of all PEO wages during the first quarter of 2020.

OPPAGA also analyzed the industries of PEO clients for those that reported their client company information to the state for the first quarter of 2020. Because we were not able to identify the industries of the clients of the 428 PEOs that did not report client-level employment data, the following analysis is based on the industries of the clients of the 332 PEOs that reported client-level employment data. The most frequent industry represented by PEO client companies, of those that reported to the state, was the construction industry (26%). The next most frequently represented industries included professional, scientific, and technical services (such as computer services, consulting services, and lawyers' offices) at 10%; management of companies and enterprises (including office workers) at 8%; accommodation and food services at 8%; and health care and social assistance at 7%.<sup>17</sup> (See Exhibit 6.)

## Exhibit 6

### From January to March 2020, the Most Frequent Industry Represented by Clients of PEOs Was Construction



Source: OPPAGA analysis of Department of Economic Opportunity data.

<sup>17</sup> Professional, technical, and scientific services includes a wide variety of industries, including, but not limited to, computer programming services, administrative management and general management consulting services, computer systems design, lawyers' offices, marketing consulting, engineering services, veterinary services, other scientific and technical consulting, certified public accounting offices, and advertising agencies.

# QUESTIONS AND ANSWERS

## What is the relationship between PEOs and insurance carriers, and how might workers' compensation coverage differ for businesses that use PEOs?

Although PEOs offer workers' compensation coverage as one of their services, typically, the PEO itself is not providing the coverage; instead, the PEO obtains coverage from a workers' compensation insurance carrier.<sup>18</sup> A PEO arrangement can create differences in workers' compensation coverage, including which workers are covered, how experience modifiers are created, and how much notice a business receives before coverage is cancelled. To address these issues, OPPAGA analyzed data provided by the Department of Financial Services and Office of Insurance Regulation; interviewed state agency officials; interviewed other stakeholders, including the National Council on Compensation Insurance (NCCI), National Association of Insurance Commissioners (NAIC), Florida Workers' Compensation Insurance Guaranty Association (FWCIGA), representatives of the PEO industry, and representatives of the insurance industry and professional and trade associations; reviewed Florida statutes; and reviewed literature.

### Relationship between PEOs and insurance carriers

PEOs provide workers' compensation to client businesses through three primary products. (See Exhibit 7.) OIR authorizes Florida insurance carriers to write policies for workers' compensation that PEOs can secure in the voluntary market.<sup>19</sup>

#### Exhibit 7

##### Three Primary Types of Workers' Compensation Policies Are Written for PEOs

Policy Features	Master Policies	Multiple Coordinated Policies	Direct Client Purchase Policies
Policyholders	PEO	PEO and client companies	Client companies
Covered employees	The PEO's direct and its leased client company employees.	The PEO's direct and its leased client company employees.	All client company employees
Additional features	Certificates of liability insurance can show proof of coverage for PEO client companies.	The PEO has its own standard policy covering only its direct employees. Generally, if there are no direct employees, the policy is issued on an "if any" basis. Each client company has its own standard policy covering its leased workers in the name and under the Federal Employer Identification Number of each client individually. Endorsements, or amendments to existing contracts, are used to coordinate coverage between the client companies and PEO.	

Source: National Council on Compensation Insurance, National Association of Insurance Commissioners, and DFS rules.

<sup>18</sup> According to DFS, only one Florida PEO self-insures its workers' compensation coverage.

<sup>19</sup> The voluntary market consists of insurers that offer insurance in a competitive environment and thus retain the right to accept or reject business. The residual market is the market of last resort for those who cannot obtain coverage in the voluntary market. The Florida Workers' Compensation Joint Underwriting Association is the designated residual market for workers' compensation in Florida. The association offers coverage to PEOs but only on a multiple coordinated policy basis.

According to NCCI, while 67% of PEO workers' compensation policies in Florida from October 2017 to September 2020 were multiple coordinated policies (based on the number of policies), 90% of premiums paid were for master policies. Research indicates there are limitations to issuing master policies, which include collecting individual client data, linking claims experience to specific employers, and pricing for policies.<sup>20</sup> However, some PEOs may prefer master policies because the PEO has more control over the policy and has the ability to screen in employees that are covered under their company. PEOs may further prefer master policies because they have a smaller administrative expense for the insurance carrier and the PEO as compared to, for example, multiple coordinated policies (MCPs). In addition, master policies could financially benefit PEOs, and the amount they are able to charge for workers' compensation is not regulated. Because PEOs establish client fees for services, they could assess fees that are higher than the premiums they pay to workers' compensation carriers.

## Trends in workers' compensation insurance carriers that cover PEOs

Of the 267 insurance carriers that wrote workers' compensation policies in Florida in 2019, 33 (12%) wrote policies for PEOs. From 2010 to 2019, a range of 29 to 40 carriers wrote PEO policies in each year, and overall, those carriers wrote more PEO policies over time. During this period, the percentage of these carriers' client base represented by PEOs ranged from less than 5% for most carriers to a high of 86%.<sup>21</sup> Only one carrier consistently wrote more than 40% of its policies with PEOs during the nine-year period. One carrier wrote exclusively for PEOs during this time but closed its operations within the same year.<sup>22</sup> On average, PEO policies comprised 7% of the client base for carriers with PEOs in their client base in a given year. Due to the small number of observations and potential for other important explanatory factors, OPPAGA did not attempt to determine whether there was a statistically significant relationship between the loss ratios of carriers writing policies for PEOs and the percentage of their policies that were for PEOs.<sup>23</sup> (See Appendix B for more detail on the loss ratios of carriers that wrote PEO policies.)

## How workers' compensation coverage differs for businesses that obtain coverage through a PEO

A typical workers' compensation policy covers all employees on an employer's job site, regardless of how they are paid. However, a PEO arrangement can create differences in workers' compensation coverage in three primary areas: which workers are covered, how experience modifiers are created, and how much notice a business receives before coverage is cancelled.

First, when a PEO uses a master or multiple coordinated policy, the insurance carrier covers only those client company workers the PEO has processed through its payroll system and/or accepted as its employees. As a result, some employees paid by the PEO's client companies may not be covered.

Second, PEO master policies can cause differences in how experience modifiers are created. The NCCI collects data to establish an experience modifier based upon a company's payroll, industry

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<sup>20</sup> Foley et al. "Contingent Workers: Workers' Compensation Data Analysis Strategies and Limitations." *American Journal of Industrial Medicine* 57 (2014):764-775; Torrey, David B. "[Professional Employer Organizations: Background, Issues in Workers' Compensation, and Recent Court Cases.](#)" Prepared for and Presented at the IAABC Workers' Compensation College (2006): 1-29.

<sup>21</sup> This range excludes the one carrier that wrote exclusively to PEOs.

<sup>22</sup> This carrier was not domiciled in Florida.

<sup>23</sup> The loss ratio is the ratio of claims paid to premiums collected. A loss ratio of less than 100% indicates that the insurer collected more in premiums than it paid in claims, whereas a loss ratio of greater than 100% indicates that the insurer paid more in claims than it collected in premiums.

classification, and number and amount of claims for three prior years.<sup>24</sup> An experience rating is an adjustment of an employer's premium for workers' compensation coverage based on the losses the insurer has experienced from that employer, as compared to similarly classified employers. The more losses, the higher the experience modifier and the higher the premium the business must pay.<sup>25</sup> A PEO master policy aggregates payroll, premium, and losses for the PEO and its client companies to apply one experience modification to a single policy. In this way, a business with a poor experience modifier could join a PEO and pay premiums based on the PEO's better experience modifier. In contrast, with a multiple coordinated policy, each client maintains separate classifications, payroll, and losses and reports client-level experience for experience rating. Similarly, with a direct client purchase policy, the PEO and client maintain separate experience modification factors.

The third way that workers' compensation policies differ under PEO arrangements is that, while workers' compensation insurance carriers are required to give advance notice to businesses for cancelling coverage, there are no requirements for PEOs to notify client companies in advance if they are cancelling their contract and thus cancelling their workers' compensation coverage. (See Exhibit 8.)

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<sup>24</sup> Industry classification is identified through classification codes, which are the risk factors associated with an individual company that are used to calculate the premium. The classification codes categorize groupings of employers with similar types of businesses that have similar exposures to risk. NCCI establishes the system of classification codes used in Florida.

<sup>25</sup> A neutral experience modification factor for a policy would be a 1.0; anything less than 1.0 would reflect a discount on premium, and a factor above a 1.0 would reflect an additional charge on premium.

## Exhibit 8

### Workers' Compensation Coverage Provided Through a PEO Differs From Direct Insurer Workers' Compensation Coverage

Component of Workers' Compensation Coverage	Terms of Workers' Compensation Coverage for a Business With a Direct Policy With an Insurer	Terms of Workers' Compensation Coverage for a Business With Insurance Through a PEO
Policy Owner	Individual Employer/Company	PEO for master policy; PEO and each client for multiple coordinated policy.
Coverage	All employees (as defined by s. 440.02, 15(a), <i>F.S.</i> ) that are paid by an employer for work or service, whether lawfully or unlawfully employed, including those of a construction subcontractor or independent contractor, are covered. Exceptions may exist for undocumented workers who provide false information per ss. 440.09(4)(a) and 440.105(4)(b)1, <i>F.S.</i>	Only those employees processed through PEO payroll system. Examples of the types of employees that may not be covered include <ul style="list-style-type: none"> <li>• Day laborers who are paid cash</li> <li>• New hires not yet processed through payroll</li> <li>• Uninsured or underinsured subcontractors</li> <li>• Employees falsely claimed as independent contractors</li> <li>• Owner of company working outside their authorized workers' compensation exemption</li> <li>• Undocumented workers who provide false information per ss. 440.09(4)(a) and 440.105(4)(b)1, <i>F.S.</i></li> </ul>
NCCI's establishment of experience modifier	Based on company's payroll, classification of industry, and number and amount of claims for the latest available three years of data; higher premium if higher experience modifier.	For a PEO with a master policy, based on all of the PEO's clients' collective payroll, classification of industry, and number and amount of claims for the latest available three years of data; higher premium if higher experience modifier.
How risk of employer is established	The insurance carrier can use a claims activity report from each company's prior insurer.	Section 627.192(4), <i>F.S.</i> , states that PEOs are required to keep information on individual company loss run but does not require them to provide it to the next insurance carrier when ending the PEO relationship. <sup>1</sup>
Requirements for cancelling coverage	Insurance carrier must provide advance notice: Notice for nonpayment, 10 days; Notice for any other reason, 45 days, s. 627.4133(1)(b), <i>F.S.</i>	PEOs can cancel contract with client company with no notice, thereby canceling workers' compensation coverage. PEOs must notify the insurer of their intent to terminate the client prior to termination when feasible; when not feasible, within five working days following termination.

<sup>1</sup> Representatives from the insurance industry report that it can be difficult to obtain these claims activity reports from PEOs.

Source: OPPAGA analysis of Florida Statutes, NCCI documents, DFS Division of Workers' Compensation guidelines, and stakeholder interviews.

## How can the relationship between a PEO and its client companies lead to a workers' compensation insurance coverage gap?

The relationship between a PEO and its client companies can lead to a workers' compensation coverage gap in several ways. These can be grouped into reporting issues, employee/employer disputes, and financial issues. To identify how coverage gaps can occur, OPPAGA reviewed literature; interviewed state agency officials; and interviewed other stakeholders, including the National Council on Compensation Insurance, National Association of Insurance Commissioners, Florida Workers' Compensation Insurance Guaranty Association, representatives of the PEO industry, and



representatives of the insurance industry and professional and trade associations. These coverage gaps have been identified by multiple sources and may affect PEOs at both the national and state level.

## Reporting issues

Reporting issues occur when a client company does not report all of its employees to the PEO or does not report them in a timely manner. This might be intentional, such as a construction subcontractor paying someone cash for day labor, or unintentional, such as when the contractor has submitted the paperwork, but the employee has not been processed by the PEO. For example, in *Crum Services v. Lopez*, the court found that a contractor, and not the contractor's PEO, was responsible for providing workers' compensation coverage to the injured worker. The concurring opinion on the case expressed concern that such coverage gaps can occur under employee leasing arrangements in Florida. In this case, a contractor failed to provide notice of a new employee to their PEO, the employee was injured on the job, and the contractor did not have adequate workers' compensation coverage for the employee's injury. While an injured worker could bring a civil action against their employer in such a circumstance, the concurring opinion further noted that it is unrealistic to expect that this would result in a viable remedy, particularly for situations like this that involve small businesses such as the contractor that may fail to appear in court proceedings.<sup>26</sup>

Intentional non-reporting can particularly affect undocumented immigrants due to their overrepresentation in the construction industry.<sup>27</sup> Additionally, academic research has found that immigrants are overrepresented in occupations and industries with higher injury and fatality rates.<sup>28,29</sup>

Unintentional reporting issues occur when an employee's start date occurs prior to a PEO verifying the employee's identifying information. Although handled differently by each PEO, generally the client fills out a new employee packet and sends it electronically to the PEO. Once in the system, the PEO will determine that the employee is one of its leased employees, and thus covered by the PEO's workers' compensation insurance. However, there can be a time lag between the employee's actual start date and the PEO verifying the employee's information. This time difference between when a client notifies the PEO of an employee and when the PEO approves an employee may cause a client company to unintentionally have a non-reported employee on their jobsite.

Another reporting issue can occur with a split-workforce arrangement, which is when a client company uses a PEO for only a specified segment of its workforce.<sup>30</sup> This can create confusion as to who is a covered employee and who is not, as workers' compensation must be secured separately for all employees not covered under the PEO.

## Employee/employer disputes

One example of an employee/employer dispute is when a PEO does not accept an injured laborer who works for a construction subcontractor as being its leased employee, and the injury ends up being covered by a general contractor's insurance. As previously discussed, in Florida, construction contractors are statutorily responsible for all subcontractors and workers on their job sites unless

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<sup>26</sup> *Crum Services v. Lopez*, 975 So. 2d 1184 (Fla. 1st DCA 2008).

<sup>27</sup> Passel, Jeffrey S., and D'Vera Cohn. A Portrait of Unauthorized Immigrants in the United States. Washington, DC: Pew Hispanic Center, April 2009.

<sup>28</sup> Orrenius, Pia M., and Madeline Zavodny. "DO IMMIGRANTS WORK IN RISKIER JOBS?" *Demography* 46, no. 3 (2009): 535–51.

<sup>29</sup> Nicholson, Valerie J., Terry L. Bunn, and Julia F. Costich. "[Disparities in Work-Related Injuries Associated with Worker Compensation Coverage Status](#)." *American Journal of Industrial Medicine* 51, no. 6 (June 2008): 393–98.

<sup>30</sup> NAIC Model Law, Regulation, Guidelines and Other Resources: Guidelines for Regulations and Legislation on Workers' Compensation Coverage for Professional Employer Organization Arrangements (2010).



these workers have other coverage.<sup>31</sup> However, PEOs are only responsible for their recognized leased employees, regardless of whether their client is a contractor or subcontractor. As a result, disputes may occur as to who is responsible for covering the injury of a subcontractor's worker who is not on the PEO's payroll, either intentionally or unintentionally. Construction contractors doing business with subcontractors using PEOs may not be aware of the risk they are taking on since PEOs can deny liability as a statutory employer by stating that they are only the employer for their leased employees.

Employee/employer disputes may occur because the PEO is still processing a new employee for payroll, and as a result, disputes that an injured worker is one of its leased employees. Also, if the paperwork sent to the PEO is incomplete, the PEO will be unable to accept the new employee. In addition, according to the PEO association, sometimes clients will fraudulently submit the paperwork to enroll an existing employee directly after the employee has been injured. However, research has shown that injuries can occur on the first day of work because the worker is unfamiliar with work tasks and the job site, often has limited safety training, and tends to be younger.<sup>32</sup> Lags in processing a new employee can leave a workers' compensation coverage gap when the PEO's insurer denies the claim because the PEO has not yet accepted the new employee.

## Financial issues

PEO and insurer insolvency are the main financial issues that could lead to a coverage gap. According to NAIC, after a PEO becomes insolvent, its insurer might use the PEO's failure to pay as a basis for denying claims made by injured workers.<sup>33</sup> Further, because the PEO rather than the client is the policyholder, when a PEO or its insurer becomes insolvent, the client may not be notified immediately that it no longer has coverage.<sup>34</sup>

In addition, a study commissioned by the National Conference of Insurance Guaranty Associations identified several potential coverage gaps that can occur when a PEO takes on a high deductible workers' compensation policy and subsequently becomes insolvent, resulting in unpaid or delayed claims for injured workers.<sup>35</sup>

- The insurer may not have access to the claim information needed to pay the claims, especially when a third-party administrator was under the control of the now defunct PEO.
- The PEO stops paying the third-party administrator that handles the claims, and thus claim payments stop.
- The PEO stops funding the account used to pay claims, and benefits checks may bounce.
- Access to the PEO's collateral to pay the claims may require litigation.
- Even if the workers' compensation policy requires that the insurer pay claims directly, there may be side agreements between the insurer and the PEO, contradicting policy wording, that allow the PEO to direct all claims administration without insurer involvement, more like a self-insurance plan.

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<sup>31</sup> Section 440.10(1)(b), F.S.

<sup>32</sup> Foley et al. "Contingent Workers: Workers' Compensation Data Analysis Strategies and Limitations." *American Journal of Industrial Medicine* 57 (2014): 764-775.

<sup>33</sup> NAIC Model Law, Regulation, Guidelines and Other Resources: Guidelines for Regulations and Legislation on Workers' Compensation Coverage for Professional Employer Organization Arrangements (2010).

<sup>34</sup> IBID.

<sup>35</sup> Jones, James R. "The Role of Large Deductible Policies for PEO's in the Failures of Small Workers' Compensation Insurers." Insights at Katie, Insurance Industry White Papers and Consulting Services, 2015.

#### PEO INSOLVENCY EXAMPLE

An insurer issued a high deductible master policy to a PEO policyholder, but the PEO defaulted on funding premiums and deductibles. This led the insurer into insolvency and cost the guaranty association \$190,500. The PEO filed for bankruptcy with only a fraction of its assets paid into the estate.

- If the insurer is small and a significant part of its income comes from a PEO with a large deductible plan, then the insurer itself may become insolvent and unable to pay the claims.

Another financial issue leading to a coverage gap is when a PEO cancels its contract with the client company, such as when a client has not fulfilled its payroll obligations. The contract cancellation terminates the client company's workers' compensation coverage. As a result, the client company must quickly find a replacement policy to cover its workers, and there may be a lapse in coverage.

## What has been the history of PEO-related workers' compensation insurance carrier insolvencies in Florida?

Since 2000, four insurance carrier insolvencies have occurred with Florida insurance carriers that historically wrote large deductible workers' compensation policies for PEOs; only two of the four insolvencies were directly attributed to a PEO. The Florida Workers' Compensation Insurance Guaranty Association identified 21 insurance carriers that, since 1997, had claims the association paid on behalf of policyholders involved in the employee leasing industry. Industry stakeholders report that PEO-related insurance carrier insolvencies can be a result of PEOs holding large deductible policies. To identify the history of PEO-related workers' compensation insurance carrier insolvencies, OPPAGA interviewed officials from the Office of Insurance Regulation, Department of Financial Services Division of Rehabilitation and Liquidation, and FWCIGA and reviewed documentation and data from these entities.

**DFS and FWCIGA have roles in the workers' compensation insurance company insolvency process.** If a workers' compensation insurance company becomes insolvent, the company is liquidated and its assets transferred to a receiver. The receiver verifies the liabilities of the company, such as claim payments and bills. Florida Statutes name DFS as the receiver in the liquidation process of insolvent estates for domestic insurance carriers.<sup>36</sup> Because most estates will not yield sufficient assets to pay all claims in full, states have created insurance guaranty associations to cover certain claims in different types of insurance markets. Florida's guaranty association for workers' compensation insurance is the FWCIGA, which was created to provide a mechanism for the payment of covered claims, to avoid excessive delays in payment, and to avoid financial losses to claimants in the event of member insurer insolvency.

**A small number of insurance carrier insolvencies in Florida were the direct result of writing workers' compensation policies for PEOs.** The FWCIGA reports that since 1997, it has incurred \$119 million in claims for 21 insolvent insurance carriers that wrote policies for business entities that lease workers.<sup>37,38</sup> FWCIGA paid a total of \$52.1 million in employee leasing-related claims for six carriers domiciled in Florida since 2009, which accounted for approximately 22% of all claims for those

<sup>36</sup> Section [631.111](#), F.S.

<sup>37</sup> Due to data limitations, the guaranty association used key words to search its data and identify any entity that could be a PEO (including temp agencies, leasing agencies, etc.) as well as PEOs known to the association.

<sup>38</sup> The guaranty association covers claims for Florida citizens by taking over as the insurer. Each state has a guaranty association that will pay the claims when an insurer goes insolvent.

companies. Of the total claims paid by FWCIGA for these six companies, less than 2% were related to employee leasing-type businesses for three companies, between 15% and 25% were related to employee leasing-type businesses for two companies, and over 99% were related to employee leasing-type businesses for one company.

According to information provided by DFS, four of these six carriers had large deductible PEO policies. Two of these four insurers entered insolvency as a direct result of affiliated PEOs defaulting on their financial obligations.<sup>39,40,41,42</sup> In the third case, while the insolvency was not a direct result of PEO affiliation, a large deductible policy with a PEO was a contributing factor to the insolvency. In the fourth case reported by DFS staff, a PEO went bankrupt and was unable to pay into the estate, but the insurance carrier's business practices were the primary reason for the carrier's insolvency. DFS staff reported that it was common for them to see the same PEOs come through the liquidation process, as only a few workers' compensation insurers will write large deductible policies for PEOs.<sup>43</sup> One stakeholder reported that the type of insurer that enters insolvency is typically a small, regional company that has not collected adequate collateral.

**Large deductible policies are a contributing factor in PEO-related workers' compensation insurer insolvencies.** Insurance carriers are the designated first dollar payer for workers' compensation claims and are therefore liable for any claim that is brought against their policy. When large deductibles are involved, risk is transferred to the policyholder. However, if these policies are issued to a company that defaults on financing its premiums or collateral, this unfunded risk contributes to insurance carrier insolvency. This was a contributing factor for three of the four Florida-domiciled carrier cases reported by DFS because the carriers lacked the assets to carry out their obligations for claim payments. Industry research has also identified large deductible policies as one of several factors that have the potential to cause the insolvency of an insurance carrier.

Although there are industry standards and state protocol for assessing risk before writing a large deductible policy, state law does not establish additional financial requirements for policyholders.<sup>44</sup> Ultimately, the decision lies with the insurance carrier, which enters an agreement with the policyholder for coverage and any collateral. The minimum deductible allowed for a workers' compensation large deductible program is \$100,000, but stakeholders noted that it is not uncommon to see deductibles as high as \$1.0 million. Although large deductible policies for PEOs can function similar to self-insurance, the requirements for qualifying as a self-insurer are not the same as for a large deductible policy. (See Appendix C for a comparison of Florida's requirements for self-insurance and large deductible policies.) One stakeholder reported that some PEOs that obtain large deductible policies might not qualify for self-insurance. To govern the financial requirements for insurance carriers, the National Conference of Insurance Guaranty Funds prepared language that recommends limiting the size of policyholders' obligations under a large deductible policy to a percentage of their net worth. In consideration of regulating large deductibles, other states have set criteria or determined

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<sup>39</sup> While an additional carrier that went insolvent may have issued large deductible policies, Department of Financial Services staff reported that information on this estate was very limited and therefore insufficient to determine if this insolvency occurred as a result of a PEO.

<sup>40</sup> Review of insolvency reports showed that all four Florida carriers had financial problems that ultimately contributed to the carriers' insolvency. Those contributing factors included the comingling of assets and fraudulent reporting of finances.

<sup>41</sup> Analysis of the individual PEO financial statements at time of bankruptcy was not part of this review.

<sup>42</sup> In 2003 and 2006, OIR recorded findings of insufficient collateral leading to risk exposure and unfiled side agreements related to a PEO high deductible policy.

<sup>43</sup> Records for this are not readily available, however, due to the requirement in s. [631.141\(12\)](#), F.S., to dispose of records in accordance with the order of the court at such time as the receiver determines that the records are not needed for the administration of the estate.

<sup>44</sup> The insurance carrier, under s. [627.192](#) F.S., has the authority to take all reasonable steps to ascertain exposure under the policy and collect the appropriate premium by collecting documentation and conducting audits.

that such policies cannot be issued. For example, Oregon allows large deductibles, but policyholders have to meet the same criteria as self-insurance.

## **Can PEOs offering workers' compensation coverage have an effect on the workers' compensation insurance market, including premiums for other businesses?**

While some stakeholders reported that PEOs affect workers' compensation insurance rates, we were unable to find data to support that these factors have actually affected Florida's workers' compensation market. However, there are ways in which a PEO could pass on risk that could affect other businesses' premiums, including denying claims for subcontractors' employees or maintaining risk through large deductible policies. To analyze the effect on the workers' compensation market of PEOs offering workers' compensation coverage, OPPAGA interviewed state agency officials and other stakeholders, including the National Council on Compensation Insurance, National Association of Insurance Commissioners, Florida Workers' Compensation Insurance Guaranty Association, representatives of the PEO industry, and representatives of the insurance industry and professional and trade associations; reviewed documentation and data provided by stakeholders; and reviewed documentation provided by state agencies.

Although stakeholders have raised concerns with PEOs using master policies to provide workers' compensation coverage, evidence of how this practice could affect the overall market is limited. As the entity that receives and maintains data from Florida insurance carriers for setting rates for Florida's workers' compensation market, the National Council on Compensation Insurance reported that they are able to collect the necessary data from insurance companies. However, NCCI did note that there are data reporting challenges with master policies. Over the past three years, master policies have comprised no more than 12% of total PEO policies, but they account for approximately 90% of all premiums written. The NCCI reported that it receives the data needed to set industry rates and did not have evidence of PEO arrangements affecting factors involved with rate making in the workers' compensation market in Florida. OPPAGA did not find sufficient data to support that PEO policies are inflating or concealing the risk or rates in the market.

### **How PEO arrangements could influence market risk**

Stakeholders reported three factors that could cause PEO arrangements to influence market risk. While we were unable to find data to support that these three factors have actually affected Florida's workers' compensation market, we provide descriptive information about how these factors could influence market risk.

The first factor is uncollected premium due to unreported workers. Workers' compensation insurers calculate policy premiums based on an employer's payroll, experience modification factors, and classification codes assigned to the policy. In a PEO arrangement, payroll is determined by client companies reporting their employees to the PEO. However, in such an arrangement, if the PEO is not aware of all of a client's employees, then there are unknown risks to the policy and uncollected premium. Should an unreported employee become injured and the PEO's insurer denies the claim but the claim is picked up by another insurance policy in a subcontractor-contractor relationship, the

premium paid on the contractor's policy would not have reflected the cost of that employee.<sup>45</sup> The insurance carrier would later adjust the contractor's premium at the time of audit to reflect the actual payroll, including that of any uninsured workers of the subcontractors. Comparatively, under a non-PEO arrangement, all of the resulting loss and audited premium would stay with the same insurer.

The second factor is called 'mod washing.' As discussed earlier, experience rating modification factors are an indicator of each individual company's risk based upon prior experience and loss cost on former policies, up to three years prior on the policies. Under a PEO arrangement, only two types of policies utilized in Florida account for the client's individual modification factor—multiple coordinated and client direct.<sup>46</sup> In Florida, when a PEO brings a client company under a master policy, the client company no longer needs to pay premiums based on its own modification factor or client-level loss data because it is covered by a policy in the PEO's name and therefore utilizes the PEO's modification factor for all associated premium payments.<sup>47</sup> The premium ultimately paid by the PEO on that policy would be due to payroll but may not accurately reflect the past or current risk of clients on the payroll. Although the risk of those clients would remain the same, ultimately, premium reflecting less risk might be collected. This is known in the industry as mod washing and can become an issue during the client's policy term and when a client leaves a PEO arrangement, as future underwriting would have limited understanding of the company's risk. Comparatively, a company insured under its own policy would have its risk factored into its premium. NCCI reported that mod washing is a possibility under a PEO arrangement but did not provide data to support its occurrence.

The third factor cited by stakeholders is misclassifying the type of worker covered on a policy. Classification codes are the risk factor associated with an individual company that is used to calculate the premium. The classification codes categorize groupings of employers with similar types of businesses that have similar exposures to risk. Under a workers' compensation policy, an employer is assigned classification codes for their policy term. While there is speculation that a misclassification could occur under a Florida PEO arrangement, we did not identify any evidence to support that this is actually a practice in Florida's PEO industry.

## How PEO arrangements can pass on risk and increase another business's premiums

Stakeholders reported that there are two examples of ways in which PEOs are able to pass on the risk of their unleased employees to other businesses. The first example occurs when a PEO disputes its status as the employer when receiving an injury claim for an employee that the PEO does not identify as one of its leased employees. Two stakeholders reported that the cost and resultant risk of a denied PEO claim has been passed along to another insurance carrier's policyholder that was not the direct employer of the injured worker. PEOs are able to limit their coverage to only those employees that they confirm as leased and therefore exclude any worker that is unknown or unrecognized by the PEO. If a PEO denies a claim for a subcontractor's employee, and that employee's injury ends up having to be covered by a contractor's workers' compensation insurance due to Florida's statutory requirement for general contractors, it goes on the general contractor's record and will be picked up in the carrier's

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<sup>45</sup> According to s. [440.381](#), F.S., audits may be conducted by insurance carriers and employers. Employers in the construction industry who are experience rated are audited annually, while all other employers are audited biennially (though more frequent audits are allowed). Payroll verification audits utilize state and federal reports of employee income, payroll, and other accounting records; certificates of insurance maintained by subcontractors; and duties of employees.

<sup>46</sup> Florida utilizes NCCI's experience rating plan, though some states have chosen to set their own.

<sup>47</sup> NCCI maintains an optional form for PEO insurers to submit individual client-level data when a company is terminated for NCCI to determine if an individual company is eligible for an experience modification factor.

end-of-year audit.<sup>48</sup> This in turn will factor into the contractor's loss ratio and could increase future premiums for the contractor.

To assess the extent to which this may be occurring, OPPAGA requested data from DFS on workers' compensation claim denials that can be definitively linked to PEOs. DFS staff reported that two denial categories can be tied to PEO-related claims: (1) no employee-employer relationship and (2) employee not reported to PEO. Because other businesses can also deny claims under the first category, it is not possible to isolate PEO-specific claims in that category. DFS provided data for the remaining category, which showed 86 of 60,014 total claims denied by insurers with PEO policyholders between 2014 and 2019. Of the 86 denials, 11 were eventually paid by another company. Of these 11, 7 were from the same carrier and appear to be examples of a claims administrator disputing an insurance carrier's relationship to the client. All seven claims were paid out by another insurance company for a total of \$65,294 over a four-year period. All of the claims were from the construction industry, and the same named employer was on five of those claims.

PEOs maintaining large deductible policies is another way in which PEOs might pass risk on to other businesses. Large deductible policies allow PEOs to maintain more risk in a policy and decrease their premiums, allowing the PEO to potentially offer small businesses lower premiums. Often, insurers' books do not include the risk from large deductibles, and that is an unknown risk in the market. If a PEO takes out a large deductible policy and contributes to an insurance carrier's insolvency due to issues such as insufficient collateralization or comingled assets, and the state's guaranty association has to increase its assessment on other insurance carriers, this can increase premiums if the carriers pass it on to their policyholders. However, while OIR approves the guaranty association to assess member insurers and self-insurance funds at a rate not to exceed 2%, the association has rarely needed to levy an additional assessment to cover costs. Although it recently imposed an additional assessment of 1%, it had not done so since 2005. However, we understand from the guaranty association that this recent assessment had PEO involvement.<sup>49</sup>

## How have other states addressed PEO regulation and PEO-related workers' compensation insurance coverage gaps?

OPPAGA reviewed a sample of 14 states to determine how they regulate PEOs and to identify the extent to which other states have addressed PEO-related workers' compensation coverage gaps.<sup>50</sup> We surveyed each state, interviewed and/or corresponded with officials in 11 states, and analyzed each state's laws and rules.<sup>51</sup> States' regulation of the PEO industry varied. Some states have taken steps to address gaps in coverage that can occur under PEO arrangements, such as adopting policies recommended by the 2010 National Association of Insurance Commissioners' *Guidelines for Regulations and Legislation on Workers' Compensation Coverage for Professional Employer Organizations Arrangements*.

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<sup>48</sup> Section 440.10 F.S., requires contractors to cover any uncovered risks of their subcontractor's employees.

<sup>49</sup> The liquidation of Guaratee Insurance Company resulted in over \$129 million in liabilities to the association, 24% of which were attributable to employee leasing claims.

<sup>50</sup> The states we reviewed were Alabama, Georgia, Illinois, Indiana, Louisiana, Mississippi, Nebraska, North Carolina, Oregon, Pennsylvania, South Carolina, Tennessee, Texas, and Utah. These states were selected because they were either identified by stakeholders as being a model state for the regulation of PEO workers' compensation arrangements and/or because they are located in the southeast.

<sup>51</sup> We were able to contact officials in Alabama, Georgia, Indiana, Mississippi, Nebraska, North Carolina, Oregon, South Carolina, Tennessee, Texas, and Utah.



**Other states vary in how they regulate PEOs; most states we reviewed house PEO regulation in departments that regulate insurance or labor.** Of the 14 states that OPPAGA reviewed, 11 require PEOs to be licensed or registered; 6 license PEOs and 5 register PEOs. However, the term license does not necessarily mean more stringent requirements than register. States' requirements for licensing or registering differ, with elements of some states' registration being more stringent than elements of other states' licensing, and vice versa.

As in Florida, nine of the states we reviewed allow multiple coordinated, master, or direct policy models. With respect to financial requirements for PEOs, several states have a requirement for PEO net worth or working capital of at least \$50,000 to \$100,000, and several require a surety bond or other proof of financial standing. Two states are similar to Florida in only requiring positive working capital with no specified threshold, and five have no financial requirement.

Responsibility for PEO oversight varies in the states reviewed, with 6 of the 14 states housing it within their Department of Insurance (or equivalent) and 4 within their Department of Labor (or equivalent). Only Texas houses PEO regulation in a licensing and regulatory agency similar to DBPR. Like Florida, nine states split responsibility for regulating PEOs and workers' compensation between two state agencies. In four states (Alabama, Oregon, Pennsylvania, and Utah), PEOs are regulated within the same department that regulates workers' compensation. (See Appendix D, Exhibit D-1.)

**Recognition of the coverage gap was limited among other states we reviewed, but several states have implemented policies that can help prevent or minimize the potential for a coverage gap.** OPPAGA corresponded and/or conducted interviews with officials in 11 of the states in our sample regarding PEO-related workers' compensation policies and any policies to address PEO-related workers' compensation coverage gaps. States generally require PEOs that provide workers' compensation to their client companies to only cover the PEO's leased employees. However, in South Carolina if a client company is found to be out of compliance, a PEO is required to provide coverage to all of the client company's employees. Oregon requires PEOs to cover all of its clients' employees (i.e., it does not allow split workforce arrangements).

We did not find widespread recognition of the coverage gap as a significant issue of concern in the other states we reviewed. Officials in eight states reported no knowledge of an existing coverage gap issue and officials in two states reported that they had experienced such issues in the past but were only aware of a single case in their respective states. This lack of awareness does not necessarily mean that there are no ongoing issues among other states; a 2002 NAIC and International Association of Industrial Accident Boards and Commissions report stated that "potential gaps in coverage may not be apparent to the client or to the state regulatory authorities charged with maintaining proof of insurance coverage."<sup>52</sup>

Although reported knowledge of coverage gap issues from these state agencies may be limited, OPPAGA found that several of the states reviewed have adopted legislation and/or regulation that could help prevent or minimize potential coverage gap issues. As shown in Exhibit 9, we grouped state legislative and regulatory actions into five areas, which are

- preventing PEO and insurer insolvency, which safeguards against the litigation and delays associated with a PEO insolvency and against the state guaranty association paying the claims;

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<sup>52</sup> *Report on Employee Leasing and Professional Employer Organizations* by the NAIC/IAIABC Joint Working Group, June 2002.

- ensuring uninterrupted payment of benefits to injured workers, which safeguards against delays in paying the injured worker while disputes are resolved;
- providing full workforce coverage, which helps ensure that disputes do not happen because of reporting issues or construction general contractors being unaware that their subcontractors do not have full coverage;
- ensuring client notice of termination of workers' compensation coverage, which safeguards against the PEO cancelling the contract with the client company and the client company being unable to immediately find a replacement insurer for workers' compensation coverage; and
- addressing reporting issues, which includes legislation that generally reduces the risk of "mod washing."

## Exhibit 9

### Other States' Policy Actions Related to the Coverage Gap Fall Across Several Policy Issue Categories

Policy Issue	Specific Policy	Number of Reviewed States That Adopted Policy
Preventing PEO and Insurer Insolvency	Prohibition against PEO's self-insuring	3
	Prohibition on master policies in the voluntary market	1
	Limitations on large deductible policies	5
	Prohibition on splitting a client's risk between the residual and voluntary market	1
Ensuring Uninterrupted Payment of Benefits to Injured Worker	Uninsured Employers Fund	5
	Uninterrupted payment of benefits if the insurers dispute who is responsible for a claim	1
Providing Full Workforce Coverage	If the PEO agreement is not a full workforce PEO agreement, the policy may exclude coverage for direct hire employees and may specify that only those employees acknowledged in writing by the PEO as one of the PEO's leased employees shall be covered if the PEO obtains satisfactory evidence of coverage for the client's other workers' compensation liabilities	2
	The PEO agreement with a covered client is a full workforce PEO agreement; the policy or certificate shall cover all PEO leased employees and shall also cover any other obligations of the client to the same extent as if the client had obtained a direct purchase policy	1
	If the services that a PEO offers to a client do not include securing workers' compensation coverage on a master policy or multiple coordinated policy basis, the PEO shall provide the client with clear and conspicuous written notice, before entering into a PEO agreement with the client, that the client will remain responsible for obtaining its own workers' compensation coverage for both PEO leased employees and direct hire employees, and the written PEO agreement shall also clearly set forth that responsibility	2
Ensuring Client Notice of Termination of Workers' Compensation Coverage	Prohibits PEOs and/or insurers from terminating the contractual relationship with the client without advanced notice	10
	The PEO insurance carrier becomes liable for full workforce coverage if it does not promptly issue notice of termination after learning that the client's coverage has been cancelled	3
Addressing Reporting Issues	All loss and payroll data reporting must identify both the PEO and the client and enable the calculation of experience modification factors at the client level	5
	Master policies must have client-specific requirements	2

Source: OPPAGA analysis of states' laws and rules and interviews with state administrators.

Each of the 14 states adopted at least one policy recommended by the NAIC Guidelines. (See Appendix D, Exhibit D-2 for policies states adopted that are similar to the NAIC Guidelines and other policies that



could address coverage gaps. See Appendix D, Exhibit D-3 for details on selected states' policies that could address coverage gaps.)

## What options could the Legislature consider to address PEO regulation and PEO-related workers' compensation insurance coverage gaps?

There are a variety of potential causes and consequences of the workers' compensation coverage gap that may occur under PEO arrangements. OPPAGA specified scenarios under which such a coverage gap could occur, including circumstances in which there are reporting issues, employer disputes, and financial issues. Additionally, we identified areas of financial and regulatory vulnerabilities of PEOs and insurers, including the potential for PEOs to pass risk on in the market or to cancel workers' compensation coverage without notice as well as the risks introduced by large deductible policies, among others.

To address these and other issues, OPPAGA identified a number of options for legislative consideration. The options are grouped into three categories: options to minimize the risk of coverage gaps; options to enhance claim handling and insurance coverage; and options to modify state regulation. (See Appendix E for a table of the advantages and disadvantages of each option.)

### Options to minimize the risk of a coverage gap

#### PEO Policy Models

- Amend ss. 468.529 and 627.192, *Florida Statutes*, to
  - require that an insurance carrier providing coverage to a PEO issue multiple coordinated policies;
  - require that an insurance carrier providing coverage to a PEO issue direct client policies; or
  - enhance master policies to require that clients be tracked at the individual level (including through data reporting and experience ratings).

#### Uninsured Employers Fund

- Amend Ch. 440, *Florida Statutes*, to create an uninsured employers fund to cover worksite injuries similar to other states; this would require a penalty to be assessed on all non-compliant workers' compensation employers.

#### PEO Coverage Arrangement

- Amend s. 468.529, *Florida Statutes*, to require PEO contracts to name the liable party depending upon when the employee is hired and reported.
- Amend ss. 468.529 and 627.192, *Florida Statutes*, to specify that if the PEO agreement with a covered client is a full workforce PEO agreement, the policy shall cover all PEO leased employees and any other obligations of the client to the same extent as if the client had obtained a direct purchase policy.
- Amend ss. 468.529 and 627.192, *Florida Statutes*, to specify that if the PEO agreement is not a full workforce PEO agreement, the client company must maintain a separate "if-any" policy that would

cover any workers not covered by the PEO policy. The client company would need to have a separate policy or the PEO would need to take responsibility for everyone on the job site.

### Regulation and Documentation

- Require a principal of a client company to provide their personal signature attesting that they have reviewed, understand, and acknowledge responsibility to report the names of workers to their employee leasing company or PEO as well as understanding the potential for the Division of Workers' Compensation to impose stop work orders and/or financial penalties for not providing coverage for all employees.
- DBPR could amend r. 61G7-7, *Florida Administrative Code*, to make underreporting employees for workers' compensation a violation of s. 440.381(6)(a), *Florida Statutes*, a violation for which the board imposes licensing and financial penalties, and to authorize employee leasing companies to pass along any financial penalties to their client companies if the underreporting is due to client negligence. The Division of Workers' Compensation could coordinate with DBPR by informing it of all stop work orders and other penalties issued for client companies of employee leasing companies (PEOs) for having employees on their job sites that are not on an employee leasing company (PEO) employee roster.

## Options to enhance claim handling and insurance coverage

### Large Deductible Policies

- Revise Ch. 468, *Florida Statutes*, to require PEOs seeking workers' compensation large deductible policies to meet the same requirements as self-insured businesses in s. 440.38, *Florida Statutes*, including meeting collateralization requirements and keeping security deposits separate from the company's own assets.<sup>53</sup>
- Clarify the financial requirements of PEO policyholders for large deductible policies by strengthening the initial net working capital required to obtain such a policy and requiring insurance carriers to report these deductible policies consistently.
- Prohibit PEOs from taking out large deductible policies.

### Insolvent Insurers Reporting

- In ss. 627.914 and 627.331, *Florida Statutes*, require insurers in the insolvency process to continue reporting data on experience and losses from policies for the purpose of ratemaking and experience modification factors; and in s. 627.072, *Florida Statutes*, require the rate making process to obtain data from the receiver of insolvent estates.

### Claim Disputes

- Amend ss. 468.529 and 627.192, *Florida Statutes*, to provide clarification on which insurer will cover an injured workers' claim under a PEO arrangement. If there is a dispute as to whether the employee is a direct hire employee or an employee covered by a PEO, require the client's insurer to pay the benefits, subject to reimbursement of claims costs and loss adjustment expenses by the PEO's insurer if it is determined that the claimant is an employee covered by a PEO.

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<sup>53</sup> Statute and Division of Workers' Compensation rules address what companies must have to be self-insured. The division does not regulate large deductible policies.

## Regulation and Documentation

Currently, statutes identify a PEO/ELC as a business entity and employer. As these businesses can maintain risk during their role of securing workers' compensation coverage insurance for leased employees, the Legislature could regulate that part of the ELC business similar to insurance carriers.

- In s. 627.192, *Florida Statutes*, enact timeframes for PEOs reporting to their clients if they are cancelling their coverage.
- In Ch. 468, *Florida Statutes*, require greater disclosure and financial reporting for PEOs affiliated with their workers' compensation insurance carrier and claims administrator.
- In s. 468.525, *Florida Statutes*, strengthen PEO financial minimum requirements based on the size of the PEO.

## Options to modify state agency regulation

- Adjust the current makeup of the Board of Employee Leasing Companies to include other representation, such as individuals experienced in insurance and/or the business community, while retaining the two consumer members, as required by s. 20.165(6), *Florida Statutes*.
- Move the regulation of PEOs to the DFS Division of Workers' Compensation.
- Only move the regulation of PEO workers' compensation coverage to the DFS Division of Workers' Compensation.

# APPENDIX A

## Services That PEO's May Provide to Client Companies

Professional employer organizations (PEOs) offer a wide variety of services to client companies. These services fall into five categories: state, local, and federal law compliance; human resources; payroll administration, technology, and tax administration; employee benefits management; and workers' compensation and risk management. Exhibit A-1 summarizes the types of services that PEOs may provide to their client companies.

### Exhibit A-1

#### PEOs Provide Many Different Types of Services to Client Companies

State, Local and Federal Law Compliance Services	Human Resource Services
Age Discrimination in Employment Act	Employer counseling
Americans with Disabilities Act	Employer assistance with the act, equal employment opportunity laws, wage and hour laws, and other employment regulations
Title VII of the Civil Rights Act of 1964 as amended (Equal Employment Opportunity laws)	Hiring and recruitment procedural guidance
Equal Pay Act	Employee training
Consumer Credit Protection Act	Performance management
Fair Credit Reporting Act	Unemployment claims administration
Consolidated Omnibus Budget Reconciliation Act	Compliance and job description audits
Employee Retirement Income Security Act	Employment verification
Family and Medical Leave Act	Governmental and census reporting
Genetic Information Nondiscrimination Act	Equal Employment Opportunity Commission claims administration
Patient Protection and Affordable Care Act	Employment practices liability insurance
Fair Labor Standards Act	Employee assistance program administration
Immigration Reform and Control Act	Drug testing assistance and background checks
Occupational Safety and Health Act	
Uniform Services Employment and Reemployment Rights Act	
Worker Adjustment and Retraining Notification Act	
State and local laws and regulations	
Payroll Administration, Technology, and Tax Administration	Employee Benefits Management
Full payroll processing, including overnight delivery	Major and mini medical insurance
Web payroll access, including employee self-service	Group vision and dental insurance
Employee maintenance	Life insurance
Time and attendance system integration	Long and short-term disability insurance
W-2 processing, including electronic distribution	Individual insurance programs
New hire reporting	Benefit administration consulting services, including claims dispute assistance
A full suite of payroll reports, including on-line access	Open enrollment processing
Garnishment administration	Billing and reconciliation
Benefits and deduction processing	Administration of 401(k)/retirement options, including coordination of mid-year and year-end 401(k) compliance testing
Direct deposit processing	Administration of Section 125 Plan
Paid time off benefit accruals	Coordination of employee notifications, annual orientations, enrollments, and terminations
Federal, state, and local payroll tax filing and remittance	COBRA administration: administer notifications, payments, benefits, regulation compliance, and reporting
	Benefits package administration to new hires and on-going employee orientation, including new hires, terminations, and option changes
	Coordination of benefits renewals

#### Workers' Compensation and Risk Management

Workers' compensation insurance options from A-rated workers' compensation insurance carrier partners

Field-based safety services

Loss control safety consulting services, including training materials and inspections and field-based assistance

OSHA compliance assistance

Risk analysis and safety recommendations

Review/analysis of claims, losses, reserves, and classification codes

Internal employee advocate staff

Administration assistance with drug-free workplace programs

Return-to-work programs

Source: A Lens into the Future of Insurance, Understanding the Acquisition, Valuation and Ongoing Management of a Business, Insurance Transaction. September 4, 2014. RiskMD, Informed Risk Management Decision Making.

## APPENDIX B

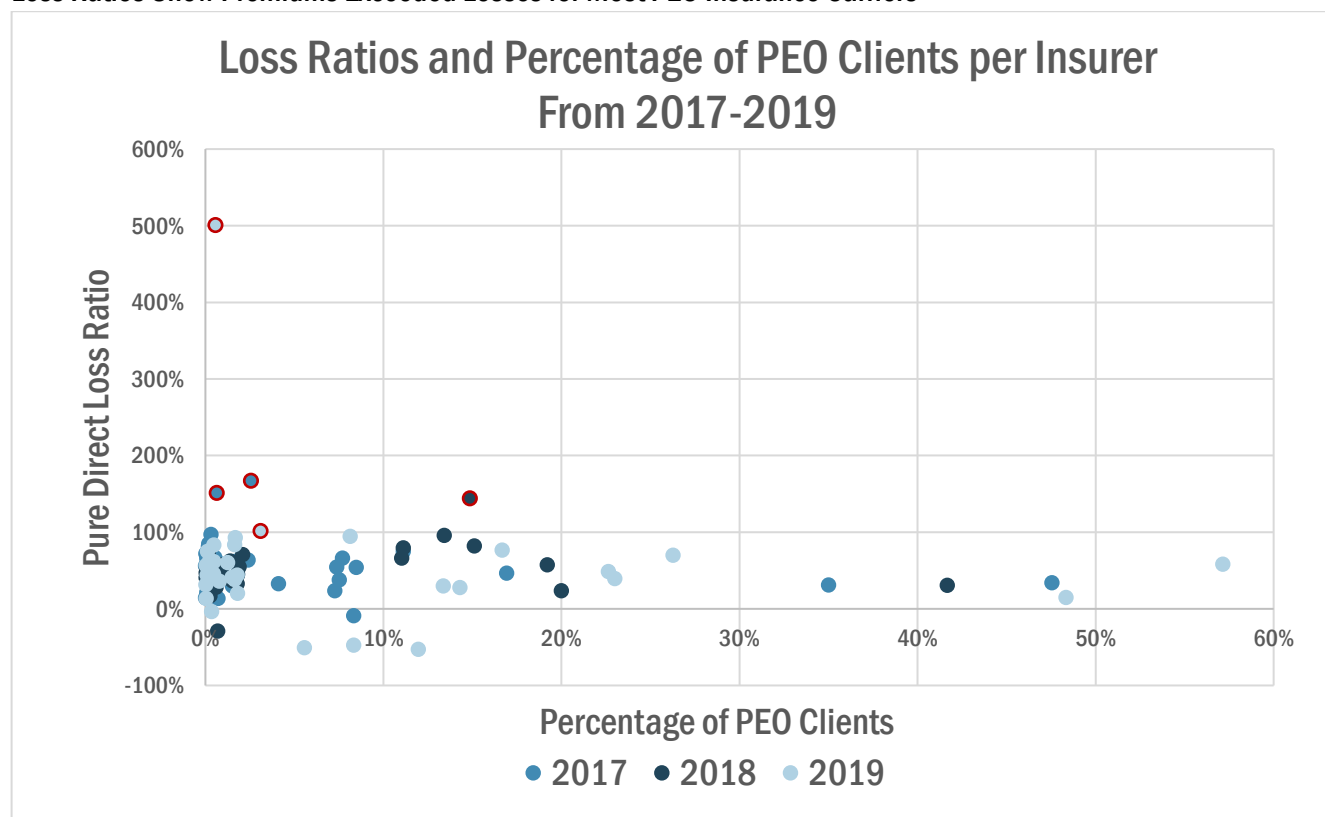
### Loss Ratios of Insurance Carriers That Wrote PEO Policies

OPPAGA analyzed Department of Financial Services and Office of Insurance Regulation data to determine whether loss ratios differ depending on the percentage of policies insurance carriers write for professional employer organizations (PEOs). The loss ratio of a carrier indicates the losses paid out over premiums earned. A loss ratio of less than 100% indicates that the insurer collected more in premiums than it paid in claims, whereas a loss ratio of greater than 100% indicates that the insurer paid more in claims than it collected in premiums.

Exhibit B-1 shows the loss ratios of insurance carriers that issued workers' compensation policies to PEOs over a three-year period from 2017 to 2019.<sup>54</sup> The exhibit includes data from 42 carriers and shows that only a small percentage of these carriers' client base was from PEO policies. Due to the small number of PEO insurers, OPPAGA could not determine if there was a significant difference between the loss ratios of carriers writing policies for PEOs. Loss ratios for PEO insurers were typically below 100% over the period analyzed and on average were 56% for 2017, 51% for 2018, and 56% for 2019. While most carriers had loss ratios below 100%, two carriers in 2017, one in 2018, and two in 2019 had loss ratios above 100%.

#### Exhibit B-1

##### Loss Ratios Show Premiums Exceeded Losses for Most PEO Insurance Carriers<sup>1</sup>



<sup>1</sup> Loss ratios circled in red represent ratios greater than 100%.

Source: OPPAGA analysis of data provided by the Department of Financial Services and the Office of Insurance Regulation.

<sup>54</sup> Two carriers reported by DFS are not shown in this chart due to the absence of carrier data to calculate a loss ratio.

# APPENDIX C

## Comparison of Workers' Compensation Large Deductible Policy Requirements to Self-Insurance Requirements

Florida's requirements for professional employer organizations (PEOs) that hold large deductible policies differ significantly from requirements for self-insurance. Exhibit C-1 compares Florida's requirements for employee leasing companies or professional employer organizations holding large deductible workers' compensation policies to requirements for self-insurance. When compared to requirements for self-insurance, PEOs with large deductible policies have lower capital requirements and do not need to meet requirements for security deposits. Requirements also differ for specific workers' compensation provisions, financial reporting, and oversight such as examinations and audits.

### Exhibit C- 1

#### Florida's Workers' Compensation Large Deductible Policy Requirements Compared to Its Self-Insurance Requirements

Subject	Employee Leasing (PEO) Large Deductible Policyholders	Individual Self-Insurers
<b>Regulator</b>	Board of Employee Leasing Companies within the Department of Business and Professional Regulation	Department of Financial Services – Division of Workers' Compensation
<b>Statutes</b>	Chapter 468, Part XI, <i>Florida Statutes</i>	Chapter 440, <i>Florida Statutes</i>
<b>Rules</b>	Department of Business and Professional Regulation r. 61G7, <i>F.A.C.</i>	Division of Workers' Compensation r. 69L5, <i>F.A.C.</i>
<b>Capital Requirements</b>	<p>\$50,000 initial and greater than \$0 ongoing</p> <p>No distinction is made for risk-bearing (large deductible) and non-risk bearing entities.</p> <p>An applicant for an initial employee leasing company (ELC) license shall have a tangible accounting net worth of not less than \$50,000. An applicant for initial or renewal license of an employee leasing company group shall have an accounting net worth or shall have guaranties, letters of credit, or other security acceptable to the board in sufficient amounts to offset any deficiency. Each employee leasing company shall maintain an accounting net worth and positive working capital, as determined by generally accepted accounting principles, or shall have guaranties, letters of credit, or other security sufficient to offset any deficiency. In determining the amount of working capital, a licensee shall include adequate reserves for all taxes and insurance, including plans of self-insurance or partial self-insurance for claims incurred but not paid and for claims incurred but not reported. (s. 468.525(3)(b), (c) &amp; (d), <i>F.S.</i>)</p> <p>Initial application, accounting net worth, or working capital deficiencies can be offset with an</p>	<p>Greater of \$10 million or three times standard premium Most recent audited financial statements shall show a net worth of the greater of \$10 million or three times the standard premium. (r. 69L-5.225, <i>F.A.C.</i>)</p> <p>Current self-insurers that no longer meet the net worth requirements must post a qualifying security deposit in an amount equal to 150% of the actuarially determined outstanding loss reserves, discounted to present value, using a 4% discount rate. (s. 440.38(1)(b)2, <i>F.S.</i>)</p>

Subject	Employee Leasing (PEO) Large Deductible Policyholders	Individual Self-Insurers
	irrevocable guaranty until such time that the deficiency causing the guaranty has been corrected. (r. 61G7-5.005, <i>F.A.C.</i> )	
<b>Security Deposit</b>	None	<p>Current investment grade credit rating - Minimum \$100,000; Less than investment grade credit rating – amount equal to the greater of the actuarially determined outstanding loss reserves discounted to present value, using a 4% discount rate, or the actuarially determined outstanding loss reserves forecasted to a date one year in the future, discounted to such forecasted date using 4% discount rate as calculated in its actuarial report.</p> <p>To be maintained until there is no remaining value to its workers’ compensation claims and the statute of limitations has run out on closed claims. To be held by the Florida Self-Insurers Guaranty Association or DFS exclusively for the benefit of workers’ compensation claimants. Security deposit to consist of either (1) surety bond or (2) irrevocable letter of credit.(r. 69L-5.218, <i>F.A.C.</i>)</p>
<b>Workers' Compensation Insurance</b>	<p>Guaranteed cost or large deductible policies per occurrence retention limit: None [No distinction is made for risk bearing (large deductible) and non-risk bearing entities.]</p> <p>Claim Adjusting: Insurer adjusters or qualified servicing entities approved by DFS, contracted and managed by the insurer.</p> <p>Required to file with board a full description of workers’ compensation self-insurance benefit plan and incorporate all assets and liabilities of any trust established for funding in its financial statements. (r. 61G7-9.001, <i>F.A.C.</i>)</p>	<p>Specific excess workers’ compensation insurance policy</p> <p>Per occurrence retention limit: No more than \$600,000 or 1.5% of the self-insurer’s net worth as shown on latest audited financial statements, whichever is greater (rounded to the nearest \$50,000). Higher retention must be approved by DFS.</p> <p>Excess insurance carriers must be subject to the protection afforded by the Florida Workers’ Compensation Insurance Guaranty Association, or DFS may accept policies issued by insurance carriers that have current financial strength and size ratings from A.M. Best Company of not less than “A-” and “VII,” respectively. (r. 69L-5.219(1)(a) &amp; (b)&amp; (c), <i>F.A.C.</i>)</p> <p>Claim adjusting: Qualified servicing entities approved by DFS or in-house servicing approved by the department. (r. 69L-5.216, <i>F.A.C.</i>)</p>
<b>Financial Statement Reporting Requirements</b>	<p>Required for ELC or ELC Group with gross payroll of \$2.5 million or more, no later than 120 days from fiscal year end. (s. 468.525(3)(e), <i>F.S.</i>, and r. 61G7-5.0031, <i>F.A.C.</i> )</p> <p>Regulatory requirement: Generally accepted accounting principles (GAAP) statements audited using generally accepted accounting standards (GAAS)</p> <p>No later than 75 days after end of each calendar quarter, statement affirming that it is maintaining positive working capital and accounting net worth and has adequate reserves to pay, when due, all payroll taxes, workers’</p>	<p>Required for all self-insurers no later than 120 days from fiscal year end. (r. 69L-5.209, <i>F.A.C.</i>)</p> <p>Regulatory requirement: Audited using GAAS unless exempted before 1/1/1997 to ensure the timely payment of all current and future claims, financial statements shall show net worth of the greater of \$10 million or three times standard premium. (r. 69L-5.209, <i>F.A.C.</i> and r. 69L-5225, <i>F.A.C.</i>)</p>



Subject	Employee Leasing (PEO) Large Deductible Policyholders	Individual Self-Insurers
	compensation and health insurance premiums, and amounts due under any plan of self-insurance or partial self-insurance along with balance sheet and income statement for the quarter. (s. 468.525(3)(d), <i>F.S.</i> , and r. 61G7-10.001, <i>F.A.C.</i> )	
<b>Workers' Compensation Claim Liability Reporting</b>	Each audited or reviewed financial statement shall include Form EL-4516 disclosing no additional claim liabilities for guaranteed cost policies or the actuarial methodology used to calculate claim reserves, including incurred but not reported (IBNR). (r. 61G7-10.0012, <i>F.A.C.</i> )	<p>Workers' Compensation Liabilities: Form DFS-F2-SI-20 due no later than 120 days from fiscal year end. (r. 69L-5.207, <i>F.A.C.</i>)</p> <p>If credit rating is less than investment grade, an actuarial report is due within 120 days of fiscal year end or within 90 days from date requested. Shall include a forecast of loss reserves to a future date. (r. 69L-5.210, <i>F.A.C.</i>)</p>
<b>Workers' Compensation Classification Oversight</b>	The ELC and its assigns may conduct an annual onsite physical examination and audits of the client who is or was subject to an applicable employee leasing contractual relationship to determine proper workers' compensation classifications of leased employees and to aid in the determination of payroll amounts paid to such leased employees. (r. 61G7-12.001, <i>F.A.C.</i> )	<p>Section 440.525, <i>F.S.</i>, authorizes the department and office to examine or investigate any insurance carrier, third-party administrator, servicing agent, or other claims-handling entity as often as is warranted to ensure that it is fulfilling its obligations under Ch. 440. If the department finds any self-insurer in violation of this chapter, it may take action pursuant to s. 440.38(3), <i>F.S.</i></p> <p>Self-insurers are required to maintain loss records that reflect a true and accurate division by the classification codes, status type, and injury codes contained in the NCCI Workers' Compensation Statistical Plan Manual and the NCCI Basic Manual for Workers' Compensation and Employers Liability Insurance so the proper classification code, status type, and injury code for each accident may be determined. The records shall be retained for five years from the last date the claims data was used for calculation of the experience modification to ensure their availability for audit purposes. The location of these records shall be provided to the department upon submission of the application for self-insurance and updated within fifteen days of any relocation. (r. 69L-5.206 (1), <i>F.A.C.</i>)</p>

Source: OPPAGA statutory update of Appendix B of the KATIE School of Insurance and Financial Services at the University of Illinois, The Role of Large Deductible Policies for PEOs in the Failures of Small Workers' Compensation Insurers, August 2015.

## APPENDIX D

### Other States' Regulation of PEOs and Policies to Address Workers' Compensation Coverage Gaps

OPPAGA reviewed 14 states' regulation of professional employer organizations (PEOs) and whether any of them addressed PEO-related workers' compensation coverage gaps.<sup>55</sup> States differed in how they regulate the PEO industry. (See Exhibit D-1.) Some of the 14 states have taken steps to address gaps in coverage that can occur under PEO arrangements, such as adopting policies recommended by the 2010 National Association of Insurance Commissioners' (NAIC) *Guidelines for Regulations and Legislation on Workers' Compensation Coverage for Professional Employer Organizations Arrangements*. Exhibit D-2 shows the policies states adopted that are similar to the NAIC *Guidelines* and other policies that could address coverage gaps. Policies that are part of the *Guidelines* are indicated by an asterisk (\*) in the policy column. Exhibit D-3 provides detailed examples of selected states' policies that could address coverage gaps.

#### Exhibit D-1

##### States Regulate PEOs and Workers' Compensation in Various Ways

State	Agency Responsible for Administering/Regulating Workers' Compensation	Agency Responsible for Overseeing PEOs/ELCs	Are PEOs Required to be Licensed or Registered?	Policy Models in Voluntary Market (Multiple Coordinated Policy or MCP, Master, Direct)	Working Capital or Other Financial Requirement <sup>1</sup>
Alabama	Department of Labor, Workers' Compensation Division	Department of Labor	Registered	MCP, Master, Direct	\$100,000 Net Worth <sup>2</sup>
Florida	Department of Financial Services, Division of Workers' Compensation	Department of Business and Professional Regulation	Licensed	MCP, Master, Direct	Positive Working Capital <sup>3</sup>
Georgia	State Board of Workers' Compensation	Department of Labor	Neither	MCP, Master	\$10,000 or 2.7% of taxable payroll surety bond <sup>4</sup>
Illinois	Workers' Compensation Commission	Department of Insurance	Registered	MCP, Master, Direct	None
Indiana	Workers' Compensation Board of Indiana	Department of Insurance	Registered	MPC, Master, Direct	Positive Working Capital <sup>5</sup>
Louisiana	Department of Labor, Workforce Commission, Office of Workers' Compensation Administration	Department of Insurance	Registered	MCP, Direct	\$100,000 Surety Bond
Mississippi	Workers' Compensation Commission	N/A	Neither	MPC, Master, Direct	N/A
Nebraska	Department of Insurance	Department of Labor	Registered	MCP, Master, Direct	\$100,000 Working Capital <sup>6</sup>

<sup>55</sup> The states we reviewed were Alabama, Georgia, Illinois, Indiana, Louisiana, Mississippi, Nebraska, North Carolina, Oregon, Pennsylvania, South Carolina, Tennessee, Texas, and Utah. These states were selected because they were either identified by stakeholders as being a model state for the regulation of PEO workers' compensation arrangements and/or because, similar to Florida, they are located in the southeast.

State	Agency Responsible for Administering/Regulating Workers' Compensation	Agency Responsible for Overseeing PEOs/ELCs	Are PEOs Required to be Licensed or Registered?	Policy Models in Voluntary Market (Multiple Coordinated Policy or MCP, Master, Direct)	Working Capital or Other Financial Requirement <sup>1</sup>
North Carolina	North Carolina Industrial Commission	Department of Insurance	Licensed	MCP, Master, Direct	\$100,000 surety bond <sup>7</sup>
Oregon	Workers' Compensation Division	Workers' Compensation Division	Licensed	Master, Direct	Verification of state and federal tax compliance
Pennsylvania	Department of Labor and Industry, Workers' Compensation Services	Department of Labor and Industry, State Workers' Insurance Fund	Neither	MCP, Master, Direct	N/A
South Carolina	Workers' Compensation Commission	Department of Consumer Affairs	Licensed	MCP, Master, Direct	None <sup>8</sup>
Tennessee	Department of Labor and Workforce Development, Bureau of Workers' Compensation	Department of Commerce & Insurance	Licensed	MCP, Master, Direct	Positive Working Capital <sup>9</sup>
Texas	Texas Department of Insurance, Division of Workers' Compensation	Texas Department of Licensing and Regulation	Licensed	Master, Direct	Working Capital of \$50,000 to \$100,000 <sup>10</sup>
Utah	Utah Insurance Department	Utah Insurance Department	Licensed	Master, Direct	Working Capital of at least \$100,000 <sup>11</sup>

<sup>1</sup> "None" means licensing/registration requirements do not have any working capital or financial requirements, and "N/A" means there is no licensing/registration or regulatory agency.

<sup>2</sup> Or audited financial statements, additional securities, or a cash deposit with the Alabama State Treasury or other securities subject to the approval of the Director of Industrial Relations or the director's official designee.

<sup>3</sup> Or shall have guaranties, letters of credit, or other security acceptable to the board in sufficient amounts to offset any deficiency.

<sup>4</sup> Or a cash deposit, irrevocable letter of credit, or equivalent financial security equal to or greater than \$10,000 or 2.7% of taxable payroll. A surety bond, irrevocable letter of credit, or cash deposit equaling \$5,000 may also be acceptable if meeting the conditions of Georgia Department of Labor Rule 300-2-7.07.

<sup>5</sup> Or a surety bond, an irrevocable letter of credit, cash, or combination of the preceding with a minimum aggregate value in an amount that is at least sufficient to eliminate the PEO's or PEO group's negative working capital plus \$100,000.

<sup>6</sup> Or a bond, certificate of deposit, escrow account, or irrevocable letter of credit in an amount of not less than \$100,000, or, if negative working capital, a bond, certificate of deposit, escrow account, and irrevocable letter of credit in an amount that is not less than \$100,000, and an amount that is sufficient to cover the deficit.

<sup>7</sup> Or an irrevocable letter of credit in a form acceptable to the Commissioner of Insurance.

<sup>8</sup> Biennial assessment fee ranging from \$500 to \$4,000. Exact figure dependent on amount of gross South Carolina payroll.

<sup>9</sup> Or a bond, irrevocable letter of credit, or securities with a minimum market value equaling the deficiency plus \$100,000.

<sup>10</sup> \$50,000 if applicant employs fewer than 250 covered employees, \$75,000 if applicant employs at least 250 but not more than 750 employees, \$100,000 if applicant employs more than 750 employees. An applicant may satisfy any deficiencies in the working capital requirement through guarantees, letters of credit, or a bond in an amount that demonstrates compliance with the amounts specified.

<sup>11</sup> Or provide to the Commissioner of Insurance in an amount equal or greater than an amount calculated by subtracting the amount of working capital of the PEO or PEO group from \$100,000 in a bond, an irrevocable letter of credit, one or more credits or securities as determined by the market value of the credits or securities, or in a combination of the preceding.

Source: OPPAGA analysis of states' laws and rules, and interviews with state administrators.

## Exhibit D-2

### States Have Enacted Various Policies to Regulate PEOs and Address Potential PEO-Related Workers' Compensation Coverage Gaps

Policy	AL	FL	GA	IL	IN	LA	MS	NC	NE	OR	PA	SC	TN	TX	UT
<b>Administrative</b>															
PEOs must be licensed or registered*	✓	✓		✓	✓	✓		✓	✓	✓		✓	✓	✓	✓
Standardization of language*1	✓				✓	✓		✓	✓		✓	✓	✓	✓	✓
<b>Preventing PEO and Insurer Insolvency</b>															
Prohibition on master policies in voluntary market						✓									
Prohibition on PEOs self-insuring			✓						✓						✓
Prohibition on splitting a client's risk between the residual and voluntary market*									✓						
Prohibition or limits on large deductible policies							✓		✓	✓				✓	✓
Insurer may not seek recourse from the client in the event of PEO default*															
Limit coverage of a master policy to one PEO or one PEO group*															
<b>Ensuring Uninterrupted Payment of Benefits to Injured Worker</b>															
Uninsured Employers Fund				✓							✓	✓	✓		✓
Uninterrupted payment of benefits if the insurers dispute who is responsible for a claim*											✓				
Uninterrupted payment of benefits where there are two insurers and one becomes insolvent*															
<b>Providing Full Workforce Coverage</b>															
Option 1*2									✓			✓			
Option 2*3										✓					
Option 3*4									✓		✓				
<b>Ensuring Client Notice of Termination of Coverage</b>															

Policy	AL	FL	GA	IL	IN	LA	MS	NC	NE	OR	PA	SC	TN	TX	UT
Coverage cannot be terminated by the insurer and/or PEO without reasonable advance notice*	✓	✓	✓				✓			✓	✓	✓	✓	✓	✓
PEO carrier becomes liable for full workforce coverage if it does not promptly issue notice of termination after learning that the client's coverage has been cancelled*			✓					✓							✓
Certificate of Coverage mechanism that ensures each client's coverage has a clearly established inception and termination date*															
Addressing Reporting Issues															
All loss and payroll data reporting must identify both the PEO and the client and enable the calculation of experience modification factors at the client level*	✓							✓			✓			✓	✓
Master policies must have client-specific requirements*										✓	✓				

\* Indicates policy option is recommended by the 2010 NAIC *Guidelines for Regulations and Legislation on Workers' Compensation Coverage for Professional Employer Organizations Arrangements*.

<sup>1</sup> Use of "PEO" rather than "employee leasing company" or other terminology.

<sup>2</sup> Option 1: If the PEO agreement is not a full workforce PEO agreement, the policy may exclude coverage for direct hire employees and may specify that only those employees acknowledged in writing by the PEO as PEO leased employees shall be covered if the PEO obtains satisfactory evidence of coverage for the client's other workers' compensation liabilities.

<sup>3</sup> Option 2: The PEO agreement with a covered client is a full workforce PEO agreement; the policy or certificate shall cover all PEO leased employees and shall also cover any other obligations of the client to the same extent as if the client had obtained a direct purchase policy.

<sup>4</sup> Option 3: If the services that a PEO offers to a client do not include securing workers' compensation coverage on a master policy or multiple coordinated policy basis, the PEO shall provide the client with clear and conspicuous written notice, before entering into a PEO agreement with the client, that the client will remain responsible for obtaining its own workers' compensation coverage for both PEO leased employees and direct hire employees, and the written PEO agreement shall also clearly set forth that responsibility.

Source: OPPAGA analysis of states' laws and rules and interviews with state administrators.

### Exhibit D-3

#### Selected Examples Show How Policies in Other States Have Addressed Potential Coverage Gaps

State/Policy Type	Details
<b>Georgia</b> PEO is included in the definition of a statutory employer	Georgia encountered a contested coverage gap issue involving a PEO that was heard through its court system in 2018. The court found that the PEO was not liable for coverage, as the employee was not one of the PEO's leased employees nor did the PEO have statutory liability as an employer. When the case was appealed, the appellate court sustained that the injured worker was not an employee of the PEO. However, the appellate court concluded that the PEO was liable for workers' compensation benefits as a statutory employer because of interpretation of state law. <sup>1,2</sup>
<b>Nebraska</b> Full workforce coverage	<p>If the PEO limits coverage to its leased employees, then the client shall obtain an additional workers' compensation insurance policy. The policy shall be written to cover any and all employees not covered by the PEO's policy, including any new or unknown employees.</p> <p>If all employees of the client are covered employees under the PEO agreement, then a workers' compensation insurance policy obtained by the PEO to cover employees of the client must be written to cover any and all employees of the client, including potential new or unknown employees that may not be covered employees under the agreement.</p>
<b>Nebraska</b> Prohibition against splitting coverage between policies or between the voluntary and the assigned risk market	<p>A PEO shall not split coverage that it obtains for a client between two or more policies.</p> <p>If workers' compensation coverage for a client's employees covered by the PEO agreement and for other employees of the client is not entirely available in the voluntary market, then assigned risk workers' compensation coverage may only be written on a single policy that covers all employees and leased employees of the client.</p>
<b>Nebraska</b> Requirement that a PEO give notice before imposing a fee increase	A PEO shall not impose any fee increase on a client based on the actual or anticipated cost of workers' compensation coverage without giving the client at least thirty days' advance notice and an opportunity to withdraw from the PEO agreement without penalty.
<b>Oregon</b> Full workforce coverage	When a worker leasing company provides workers to a client, the worker leasing company shall provide workers' compensation coverage for those workers and any subject workers employed by the client unless during the term of the lease arrangement the client has proof of coverage on file with the director that extends coverage to subject workers employed by the client and any workers leased by the client.
<b>Oregon</b> Notice for termination of coverage	A worker leasing company may terminate its obligation to provide workers' compensation coverage for workers provided to the client by giving to the client and the director written notice of the termination. A notice of termination shall state the effective date and hour of the termination, but the termination shall be effective not less than 30 days after the notice is received by the director.
<b>Pennsylvania</b> Uninterrupted payment of benefits if the insurers dispute who is responsible for a claim	If there is a dispute as to if the injured worker is an employee of the client company or the PEO, it defaults to the client company (or their insurer) to pay for the claim, and if it is later determined that the injured worker was a covered leased employee of the PEO, then the PEO (or their insurer) will have to reimburse the client company. If the client company does not have a workers' compensation insurance policy and is not self-insured, the PEO (or their insurer) will have to pay for the claim unless and until it is determined that the client company was responsible, and then the client company will have to reimburse the PEO (or their insurer).
<b>Tennessee</b> Uninsured Employers Fund	<p>Businesses who illegally fail to maintain workers' compensation insurance or who illegally misclassify employees as "independent contractors" or "subcontractors" are subject to financial penalties.</p> <p>These fines are collected by the state and are used to provide workers' compensation benefits to any eligible employee who is injured while working for an illegally uninsured employer.</p> <p>Businesses may be assessed a financial penalty equal to 1.5 times the employer's total estimated annual premium.</p> <p>In Fiscal Year 2018-19, Tennessee collected over \$1 million and assessed over \$2 million in new penalties for employers who did not have workers' compensation coverage or who had a lapse in coverage. During the same year, Tennessee collected over \$0.5 million and assessed businesses over \$2.7 million in new penalties for construction service providers who misclassify either the amount of payroll, number of employees, or employee's duties.</p>

State/Policy Type	Details
<b>Utah</b> Regulation of master policies	The client is shown as an insured by means of an endorsement for each individual client, the experience modification of a client is used, and the insurer files the endorsement.
<b>Utah</b> Requirement for the availability of client records at the termination of the PEO agreement	If requested by the client, the insurer shall provide the client records regarding the loss experience related to workers' compensation insurance provided to a covered employee pursuant to the professional employer agreement.

<sup>1</sup> See O.C.G.A. § 34-9-1(3) and § 34-9-11.

<sup>2</sup> Under the exclusive rights and remedies granted to employers, O.C.G.A. § 34-9-11 states that "[a] temporary help contracting firm or an employee leasing company shall be deemed to be a statutory employer."

Source: OPPAGA analysis of states' laws and rules and interviews with state administrators.

# APPENDIX E

## Advantages and Disadvantages of Options for Legislative Consideration

Based on concerns over workers' compensation coverage under a professional employer organization (PEO) arrangement, including the coverage gap for workers and the financial vulnerabilities of PEOs and insurers, OPPAGA identified a number of options for legislative consideration. The options are grouped into three categories: options to hold individuals accountable and minimize the risk of coverage gaps on job sites; options to increase the accountability for proper handling of insurance coverage and claims; and options to modify state agency regulation. Exhibit E-1 summarizes the advantages and disadvantages of each option.

### Exhibit E-1

#### Options for Legislative Consideration

Option	Statute/Rule	Advantages	Disadvantages
<b>Minimize the Risk of a Coverage Gap</b>			
<b>PEO Policy Models</b> Require insurers to issue workers' compensation policies to each client as multiple coordinated policies.	s. 468.529, F.S. s. 627.192, F.S.	<ul style="list-style-type: none"> <li>Client businesses would hold their own policies in their name, and this could reduce the risk of the coverage gap.</li> <li>Eases state's need to monitor compliance.</li> </ul>	<ul style="list-style-type: none"> <li>Affordability of coverage could push businesses into the residual market.</li> <li>There is still an opportunity for a split workforce for non-leased employees, leaving potential for a coverage gap.</li> <li>Creates more administrative requirements for insurers and PEOs.</li> <li>Feasibility of the option relies on client companies reporting required information.</li> </ul>
Require insurers to issue workers' compensation policies to each client as a direct client policy.	s. 468.529, F.S. s. 627.192, F.S.	<ul style="list-style-type: none"> <li>Coverage gap would be reduced, and there would not be a possibility of a split workforce.</li> </ul>	<ul style="list-style-type: none"> <li>Affordability of coverage could push businesses into the residual market.</li> <li>Most policies currently utilized are either master or multiple coordinated policies.</li> </ul>
Regulate master policies by requiring separate reporting of client businesses.	s. 468.529, F.S. s. 627.192, F.S.	<ul style="list-style-type: none"> <li>Client-level data would be available for regulatory and ratemaking purposes.</li> <li>Client businesses would receive notification on the termination of a policy with sufficient time to find new coverage.</li> </ul>	<ul style="list-style-type: none"> <li>There is no current system established for reporting client-level data from a single policy.</li> <li>Costs associated with collecting, maintaining, and verifying additional data.</li> <li>Feasibility of the option relies on client companies reporting required information.</li> </ul>
<b>Uninsured Employers Fund</b> Create a fund to cover any uninsured worksite injuries by assessing financial penalties on businesses that fail to maintain workers' compensation insurance or that illegally misclassify employees as "independent contractors" or "subcontractors."	Ch. 440, F.S.	<ul style="list-style-type: none"> <li>Instead of an assessment against the entire industry, uninsured workers are compensated by those who do not adhere to workers' compensation laws.</li> <li>Financial penalties could deter potential bad actors.</li> <li>All employees would have access to getting their claim paid.</li> <li>Could be used to help general contractors avoid having to pay claims for subcontractors' employees.</li> </ul>	<ul style="list-style-type: none"> <li>Financial penalties must be sufficient to avoid <ul style="list-style-type: none"> <li>encouraging noncompliance with maintaining coverage and</li> <li>depleting the fund due to the fluctuating nature and size of workers' compensation claims.</li> </ul> </li> <li>Initial establishment of the fund and staff would require a legislative appropriation.</li> </ul>



Option	Statute/Rule	Advantages	Disadvantages
<b>PEO Coverage Arrangement</b> Require PEO contracts to name the liable party depending upon when the employee is hired and reported.	s. 468.529, F.S.	<ul style="list-style-type: none"> <li>All employees would have a liable employer for injury claims.</li> <li>May help contractors avoid having to cover claims for unreported employees of subcontractors who use PEOs to provide their workers' compensation coverage.</li> </ul>	<ul style="list-style-type: none"> <li>PEO loses discretion over who is an employee.</li> <li>PEO might not know its full liability if a client company neglected to initiate reporting newly hired employees.</li> </ul>
Require the PEO to provide full coverage for employees of the client companies, regardless of leased status on their policy.	s. 468.529, F.S. s. 627.192, F.S.	<ul style="list-style-type: none"> <li>Eliminates the coverage gap for non-leased employees.</li> <li>Encourages PEOs to verify payroll and exposure.</li> </ul>	<ul style="list-style-type: none"> <li>PEOs would be required to cover all employees regardless of their contractual relationship, which would increase their costs.</li> <li>If a client company was delayed in reporting, the PEO would be unaware of the uninsured risks until a claim was filed.</li> </ul>
If client companies do not have full coverage for their entire workforce, they must have coverage on an "if any" basis, meaning that anyone not on a PEO's coverage is covered.	s. 468.529, F.S. s. 627.192, F.S.	<ul style="list-style-type: none"> <li>All employees would have a liable employer for injury claims.</li> </ul>	<ul style="list-style-type: none"> <li>Costs associated with issuing separate policies could lead to unaffordable coverage for the client business.</li> <li>Client businesses could be dissuaded from using PEOs to obtain coverage.</li> <li>Client businesses may not be able to find an insurance carrier that will issue this type of policy.</li> </ul>
<b>Regulation and Documentation</b> Require a principal or client business to attest to their reporting duties to PEOs for hired employees and acknowledge the potential legal and financial repercussions of not properly fulfilling requirements to obtain workers' compensation coverage for all employees.	s. 440.107, F.S.	<ul style="list-style-type: none"> <li>Principals would become informed of their legal responsibility and sign off on their understanding.</li> <li>Principals would be informed of the enforcement actions the Division of Workers' Compensation is authorized to conduct for non-compliant employers.</li> <li>PEOs would maintain the documentation should any coverage disputes arise.</li> </ul>	<ul style="list-style-type: none"> <li>Does not fully address the coverage gap.</li> </ul>
Authorize the Department of Business and Professional Regulation (DBPR) to assess penalties to PEOs for incomplete or inaccurate employee data, and allow PEOs to pass on financial penalties to client businesses.	s. 468.532, F.S.	<ul style="list-style-type: none"> <li>PEOs would be held to the same standard as all other employers under s. 440.381(6)(a), F.S.</li> <li>Client companies and PEOs would have a vested interest in reporting all employees covered under a workers' compensation policy.</li> </ul>	<ul style="list-style-type: none"> <li>Does not fully address the coverage gap.</li> <li>Reporting requirements may differ by PEO contract.</li> <li>PEOs would incur the penalty and would then pass it along to the client company.</li> </ul>
<b>Enhance Claim Handling and Insurance Coverage</b>			
<b>Large Deductible Policies</b> Require PEO large deductible policyholders to meet the requirements for self-insurance.	Ch. 468, F.S.	<ul style="list-style-type: none"> <li>As the entities incurring risk, PEOs would be required to demonstrate working capital and collateral.</li> </ul>	<ul style="list-style-type: none"> <li>PEOs with current large deductible policies that are unable to meet these requirements would need to secure a new policy.</li> </ul>
Improve reporting of PEO large deductible arrangements and associated collateral.	Ch. 468, F.S. s. 627.192, F.S.	<ul style="list-style-type: none"> <li>Financial vulnerabilities would be disclosed and the Office of Insurance Regulation (OIR) would be able to monitor any risk to the market.</li> </ul>	<ul style="list-style-type: none"> <li>Adds more regulatory burden to businesses.</li> </ul>

Option	Statute/Rule	Advantages	Disadvantages
Adjust Office of Insurance Regulation rule to prevent large deductible policies for PEO workers' compensation arrangements.	r. 690-189.006, <i>F.A.C.</i>	<ul style="list-style-type: none"> <li>Reduces the potential for insurer insolvency due to PEOs maintaining uncollateralized risk.</li> </ul>	<ul style="list-style-type: none"> <li>Premiums for businesses covered by these large deductible policies will increase.</li> </ul>
<b>Insolvent Insurers Reporting</b> Modify requirements of insolvent insurers to continue reporting data for the ratemaking process.	s. 627.912, <i>F.S.</i> s. 627.331, <i>F.S.</i> s. 627.072, <i>F.S.</i>	<ul style="list-style-type: none"> <li>Information that is attached to an insolvent estate would factor into the ratemaking process.</li> <li>The impact of a PEO insolvency could be quantified.</li> </ul>	<ul style="list-style-type: none"> <li>Coordination and reporting between the insolvent estate and the claims administrator would be required.</li> <li>New reporting procedures would need to be identified for claims under the receivership process.</li> <li>Costs associated with tracking and compiling information may require additional funds to support reporting activities.</li> </ul>
<b>Claim Disputes</b> In a dispute over a worker's employment status, require the client's insurer to pay the benefits, subject to reimbursement of claims costs and loss adjustment expenses by the PEO's insurer if it is determined that the claimant is a PEO leased employee.	Ch. 468, <i>F.S.</i> s. 627.192, <i>F.S.</i>	<ul style="list-style-type: none"> <li>The Legislature would define in statute who the first payer for all workers' compensation claims would be instead of leaving it up to individual contractual arrangements between leasing companies and clients.</li> </ul>	<ul style="list-style-type: none"> <li>The possibility of a PEO claim being passed on to a third-party payer remains, but the claim is covered upfront.</li> </ul>
<b>Regulation and Documentation</b> Regulate PEOs' administration of workers' compensation similar to insurance carriers by requiring PEOs to notify client companies of coverage termination within certain timeframes.	s. 627.192, <i>F.S.</i>	<ul style="list-style-type: none"> <li>PEOs would have the same requirements as insurance carriers for notifying clients of termination of workers' compensation insurance coverage.</li> </ul>	<ul style="list-style-type: none"> <li>PEOs are employers and provide more services than just workers' compensation.</li> </ul>
Require disclosure and financial reporting from PEOs affiliated with insurance carriers and claims administrators.	Ch. 468, <i>F.S.</i>	<ul style="list-style-type: none"> <li>Financial vulnerabilities would be disclosed, and OIR would be able to monitor any risk to the market.</li> </ul>	<ul style="list-style-type: none"> <li>DBPR does not currently have a way to utilize this information for regulatory practices.</li> </ul>
Strengthen PEO financial minimum requirements based on the size of the PEO.	s. 468.525, <i>F.S.</i>	<ul style="list-style-type: none"> <li>Requirements would provide more assurance that PEOs offering workers' compensation are financially viable.</li> </ul>	<ul style="list-style-type: none"> <li>Increasing requirements could lead to a less competitive PEO market.</li> </ul>
<b>Modify State Agency Regulation</b>			
Change the makeup of the Board of Employee Leasing Companies to include one individual experienced in insurance and/or one individual representing a small business, while retaining the two consumer members, as required by s. 20.165(6), <i>F.S.</i>	s. 468.521, <i>F.S.</i>	<ul style="list-style-type: none"> <li>Better representation of individuals who have knowledge of the industry.</li> </ul>	<ul style="list-style-type: none"> <li>If the board not having full membership is due to lack of interest, there might be difficulty finding additional individuals interested in board appointment.</li> </ul>
Move the regulation of PEOs to the Department of Financial Services' (DFS) Division of Workers' Compensation.	Ch. 468, <i>F.S.</i>	<ul style="list-style-type: none"> <li>The division already monitors PEO compliance with workers' compensation requirements.</li> <li>The division has more personnel than DBPR and is authorized to handle workers' compensation</li> </ul>	<ul style="list-style-type: none"> <li>The division is specialized to focus on workers' compensation, not business regulation.</li> <li>The division lacks the structure and expertise of a professional board to handle responsibilities such as licensing and reporting.</li> </ul>

Option	Statute/Rule	Advantages	Disadvantages
		<p>enforcement and compliance under Ch. 440, F.S.</p> <ul style="list-style-type: none"> <li>• The division has investigatory processes and compliance tools including stop work orders and penalties.</li> </ul>	<ul style="list-style-type: none"> <li>• Costs associated with agency transfer and additional FTE.</li> </ul>
Move the regulation of PEO workers' compensation coverage to DFS' Division of Workers' Compensation.	Ch. 468, F.S.	<ul style="list-style-type: none"> <li>• The division already monitors PEO compliance with workers' compensation requirements.</li> <li>• The division has more personnel than DBPR and is authorized to handle workers' compensation enforcement and compliance under Ch. 440, F.S.</li> <li>• The division has authority to monitor and audit insurance carrier performance.</li> <li>• The division has databases that collect information on proof of coverage and claims administration.</li> <li>• The division has investigatory processes and compliance tools, including stop work orders and penalties.</li> <li>• The division could increase coordination with the DBPR board to ensure proper conduct within the industry.</li> <li>• The department has a fraud unit that could handle any cases of criminal violations with a PEO providing workers' compensation.</li> </ul>	<ul style="list-style-type: none"> <li>• The division would have limited oversight over the remainder of the PEO's operation.</li> <li>• Costs associated with agency transfer and additional FTE.</li> </ul>

Source: OPPAGA analysis of the *Florida Statutes*, National Association of Insurance Commissioners (NAIC) model legislation, stakeholder input, and literature review.

# AGENCY RESPONSES



Office of the Secretary  
Thomas R. Philpot, Chief of Staff  
2601 Blair Stone Road  
Tallahassee, Florida 32399-1000  
Phone: 850.413.0755 • Fax: 850.921.4094

**Ron DeSantis, Governor**

February 15, 2021

R. Philip Twogood, Coordinator  
Office of Program Policy Analysis and Government Accountability  
111 West Madison Street  
Tallahassee, Florida 32399-1475

Dear Dr. Twogood,

Thank you for sharing the preliminary findings and recommendations of the report on the Review of Professional Employer Organizations and Workers' Compensation as prepared by your office. The Department of Business and Professional Regulation appreciates the efforts of the Office of Program Policy Analysis and Government Accountability (OPPAGA) in reviewing and analyzing information relative to workers' compensation insurance and employee leasing companies. This correspondence shall serve as the department's response pursuant to Section 11.51(2), Florida Statutes.

The department will provide a copy of the final OPPAGA report, once issued, to the Board of Employee Leasing Companies for review and consideration of the findings and recommendations. The department reserves comment in regard to the report's legislative recommendations. However, options for the modification of board member positions or the transfer of regulatory responsibilities between state departments should be subjected to additional study and review to determine if alternative measures would be more effective.

Again, thank you and the staff of OPPAGA for preparing this preliminary analysis of issues related to workers' compensation coverage and Florida's employee leasing companies. Please contact the Department's Office of Inspector General at (850) 414-6700 if our team can be of further assistance to OPPAGA in this review.

Respectfully,

A handwritten signature in blue ink, appearing to read "Tom Philpot", is written over a horizontal line.

Thomas R. Philpot  
Chief of Staff

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# OPPAGA

Office of Program Policy Analysis and Government Accountability

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OPPAGA supports the Florida Legislature by providing data, evaluative research, and objective analyses that assist legislative budget and policy deliberations. This project was conducted in accordance with applicable evaluation standards. Copies of this report in print or alternate accessible format may be obtained by telephone (850/488-0021), by FAX (850/487-3804), in person, or by mail (OPPAGA Report Production, Claude Pepper Building, Room 312, 111 W. Madison St., Tallahassee, FL 32399-1475).

Project supervised by Becky Vickers (850/717-0515)

Project conducted by Ryan Bastek, Anne Cooper, Becca Greene, Daphne Holden, Kim Shafer, and  
Shane Whitney

Laila Racevskis, Health and Human Services Staff Director (850/717-0524)

R. Philip Twogood, Coordinator