STATE OF FLORIDA
DIVISION OF ADMINISTRATIVE HEARINGS

JOHN DEERE INSURANCE COMPANY,	)	
	)	
Petitioner,	)	
	)	
vs.	)	Case No. 02-1657
	)	
DEPARTMENT OF INSURANCE,	)	
	)	
Respondent.	)	
	)	

RECOMMENDED ORDER

Administrative Law Judge Don W. Davis of the Division of Administrative Hearings conducted a final hearing in this case on July 31, 2002, in Tallahassee, Florida.

APPEARANCES

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For Respondent: Elenita Gomez, Esquire
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STATEMENT OF THE ISSUE

Whether the Department of Insurance (Respondent) properly determined that John Deere Insurance Company, now known as Sentry Select Insurance Company (Petitioner), realized excessive

profits pursuant to Section 627.215, Florida Statutes, for the calendar/accident years 1995, 1996 and 1997 in the amount of $571,197.00.

PRELIMINARY STATEMENT

On April 6, 2000 Respondent filed a Notice of Excessive Profits finding that Petitioner had realized excessive profits in the amount of $571,197.00 for calendar/accident years 1995-1997. Petitioner timely filed an Election of Rights with Respondent on February 2, 1999, requesting an informal hearing. Respondent received a Petition for Formal Administrative Hearing from Petitioner on April 19, 2000. Respondent filed the Petition with the Division of Administrative Hearings (DOAH) on April 26, 2002.

At the final hearing, Respondent presented testimony of one witness and 13 exhibits. Petitioner presented the testimony of two witnesses and 10 exhibits. A Transcript was filed with DOAH on August 19, 2002, and the parties were granted leave to file proposed recommended orders more than ten days following the receipt of transcript by DOAH. Proposed Recommended Orders were filed on October 28, 2002, and have been reviewed and considered in the preparation of this Recommended Order.

FINDINGS OF FACT

1. Petitioner, John Deere Insurance Company, is currently known as Sentry Select Insurance Company. It holds a

Certificate of Authority to do business in the State of Florida as a foreign property and casualty insurer and was so licensed at all material times.

2. Section 627.215, Florida Statutes, requires insurance companies writing workers' compensation and employer's liability insurance to file periodic reports with the Respondent. The reports are made using Respondent's Form DI4-15, which is adopted by Rule 4-189.007, Florida Administrative Code.

3. Section 627.215, Florida Statutes, was enacted by the 1979 Legislature and became effective July 1, 1979. Chapter 79-40, Laws of Florida. The statute was passed as part of a wage loss reform whose purpose was to change the benefits structure for workers' compensation insurance and to "pass-on" benefits of the reductions to the employers who purchase workers' compensation insurance.

4. From its inception, Section 627.215, Florida Statutes, has required insurers to file workers' compensation and employer's liability insurance data with Respondent prior to July 1 of each year. The data which is required includes "calendar year" earned premium, "accident year" incurred losses and loss adjustment expenses, administrative and selling expenses incurred in or allocated to Florida for the calendar year, and policyholder dividends applicable to the calendar year. Section 627.215(1), Florida Statutes.

5. Effective October 1, 1988, the Legislature amended Section 627.215, Florida Statutes, by adding commercial property and casualty insurance to the statute. Chapter 88-390, Laws of Florida. The operative terms of Section 627.215, Florida Statutes, which had previously applied only to workers' compensation and employer's liability insurance, were then applied to commercial property and casualty insurance as well. Under Section 627.215, Florida Statutes, as amended in 1988, commercial property and casualty experience was to be reported to Respondent on a rolling three-year basis in the same manner as workers' compensation and employer's liability insurance. Losses and loss adjustment expenses were also valued in the same manner for all four lines of business; that is, not at the end of the three-year compilation period, but one year after the conclusion of the three-year compilation period. Section 627.215(2) and (3), Florida Statutes (Supp. 1988). All four lines of insurance were then to be combined for determining whether there were excessive profits under the statute. Section 627.215(7), Florida Statutes (Supp. 1988).

6. The 1995 Legislature then added Subsection (14) to Section 627.215, Florida Statutes. Section 627.215(14), Florida Statutes, became effective June 14, 1995. Chapter 95-276, Laws of Florida. Subsection (14) states that Section 627.215,

Florida Statutes, no longer applies to commercial property and casualty insurance as of January 1, 1997.

7. The Legislature made a further clarification in 1997, making clear that commercial umbrella liability was included as a part of commercial property and casualty. Subsequent to that legislative change, Respondent issued Bulletin 97-012 dated October 9, 1997, which advised insurance companies that the Legislature had passed Senate Bill 840. It stated that, by law, Respondent would not be able to use a profit and contingencies factor less than zero. It also clarified that commercial property and casualty insurance specifically included commercial umbrella liability insurance.

8. The terms "calendar year" and "accident year" are actuarial terms of art. A premium may be "written" (that is, collected) in one calendar year, but not fully "earned" until the succeeding calendar year, when the one-year period of the insurance policy is complete. A calendar year-earned premium, therefore, is the premium associated with a policy representing the portion of the policy expiring during a given year.

9. Because losses and loss adjustment expenses are not fully paid in the same calendar year in which the pertaining accidents are reported, losses and loss adjustment expenses are monitored on both a "paid" and estimated basis over time and attributed to the year in which the pertaining accidents are

reported--that is, the "accident year," which is January 1 through December 31. Losses and loss adjustment expenses are then valued as of December 31 of the first year following the latest accident year. Section 627.215(2), Florida Statutes.

10. A loss development factor is a factor that the company uses to take the losses as they exist today and project them into the future at what it ultimately expects to pay on a claim. Generally, a loss development factor is calculated based on historical data and historical patterns of development.

11. A company can project its own loss development factor, including its own workers' compensation data in Florida or it can use the factors published by the National Council on Compensation Insurance ("NCCI"), if it does not have sufficient experience to project losses. However, the company must be able to justify whatever loss development factors it chooses to use.

12. NCCI's circulars are provided to their affiliated companies and those circulars include its loss development factors, but NCCI advises the companies that whatever factors they use, they must be able to justify their use to Respondent. The choice of loss development factors directly affects the calculation of losses which affects what a company owes for excess profits. Petitioner was an affiliated company of NCCI.

13. The data which is filed on a yearly basis is for the three years prior to the most recent accident year.

Section 627.215(2), Florida Statutes. This results in the reporting of a "rolling" three-year experience period; for example, 1993-1995, followed by 1994-1996, followed by 1995-1997.

14. Applied to 1995-1997, which is the experience period at issue in this case, Section 627.215, Florida Statutes, therefore, operates to require calendar/accident years 1995-1997 be calculated as to losses and loss adjustment expenses as of December 31, 1998, and the filing of Form DI4-15 by July 1, 1999.

15. The six-month period between the valuation and the report being due to Respondent is to allow companies to gather data, do an evaluation, complete the form, and file it with Respondent. During the six-month period, the company also develops its losses and loss adjustment expenses to an ultimate basis.

16. Generally, excessive workers' compensation profits result where the insurance company's "underwriting gain" for workers' compensation exceeds its "anticipated underwriting profit" plus five percent. Section 627.215(7)(a), Florida Statutes.

17. Since January 1, 1997, Respondent has not taken commercial property and casualty experience into account when calculating a company's workers' compensation and employer's

liability excessive profits, nor has it combined commercial property and casualty with workers' compensation and employer's liability in making a determination of excessive profits.

18. During the time period when workers' compensation and employer's liability experience were combined with commercial property and casualty to determine if excessive profits were owed by an insurer, Respondent maintained two separate sections for review of the data. Workers' compensation had its own reporting forms, rule, analysis, and staff; and commercial lines had its own reporting forms, rule, analysis, and staff. Each section would conduct analysis of the data and make a determination as to whether excessive profits had been realized in the applicable line of insurance. Respondent then combined its work product to make an overall determination of whether excessive profits were owed.

19. At the time that Respondent reviewed commercial property and casualty excess profits reporting, such reports were required to be on Form DI4-358, adopted by rule of Respondent. That form is not used anymore because the law ceased to apply to commercial property and casualty experience as of January 1, 1997.

20. For the workers' compensation calendar/accident years 1995-1997 at issue in this case, Petitioner timely submitted its Form DI4-15 to Respondent along with the required certification,

explanations, and supporting data dated June 16, 1999. The form appropriately contained only data for workers' compensation and employer's liability experience. No commercial property and casualty data was submitted to Respondent at that time.

21. By letter dated November 19, 1999, Respondent was notified by Petitioner of the acquisition of John Deere Insurance Company and the name change to Sentry Select Insurance Company. John Deere Insurance Company was headquartered in Moline, Illinois, prior to its acquisition.

22. The John Deere operations in Moline, Illinois, were discontinued. Accounting records were transferred to Stevens Point, Wisconsin. Actuarial records were also transferred to Stevens Point, Wisconsin, in 2000.

23. Using the data submitted, Respondent generated a report dated January 3, 2000, indicating a total of $571,197.00 in workers' compensation and employer's liability excessive profits for 1995-1997. Respondent then issued a Notice to Petitioner dated April 6, 2000, alleging the sum of $571,197.00 was owed to Petitioner's policyholders in excessive profits.

24. On May 4, 2000, Respondent received a fax from Petitioner's employee Diane Huber advising that the Petitioner had left off some numbers for its residual market. These numbers should have been included in the DI4-15 report which was due by July 1, 1999; however, Respondent was willing to consider

these numbers because it appeared that the omission of the data was a clerical oversight, and such data is routinely considered by Respondent. By including the residual market data, Petitioner's excess profits would be reduced to $488,150.

25. By cover letter dated June 14, 2002, Petitioner submitted what was represented as the company's commercial and property casualty experience for 1995 and 1996 to Respondent, on Form DI4-358, along with revised workers' compensation data. This was the first commercial documentation submitted to Respondent.

26. Neither the workers' compensation nor the commercial data were accompanied by a certification, explanations, or supporting data. Form DI4-15 is adopted by reference, along with its instructions, by Rule 4-189.007, Florida Administrative Code.

27. The revised workers' compensation data proposed two changes to the excess profits calculation: The first was to change the loss development factors and the ultimate losses for each of the accident years, and the second was the proposal to include the residual market data. The net effect of those two changes is that Petitioner's excess profits increase to $672,488.00.

28. Ms. Patricia Ferguson, a statistical manager with Sentry Insurance Group, made the modifications to the workers'

compensation data and compiled the commercial property and casualty data, which was not an original submission of John Deere. Ferguson agrees that using the revised loss development factors and the direct method of calculation raises Petitioner's workers' compensation excess profits to $672,488.00. The method of loss development used by Ferguson was the "incurred including IBNR." IBNR stands for "incurred but not reported."

29. Upon review of the commercial data submitted by Petitioner, it was determined that Petitioner only submitted data for calendar/accident years 1995 and 1996 and nothing for 1997, which should have been included in the calculation, assuming that commercial property and casualty data were still being collected. Ferguson concedes that she did not include the 1997 data because per the statute, commercial data could not be included to calculate excess profits for that year.

30. If Respondent were to apply the excess profits statute as it once functioned to the commercial data for years 1995-1997, the situation is worse than for the prior years 1994-1996, because the valuation date for 1995-1997 is two years after the law ceased to apply to commercial property and casualty experience and the filing date is two and a half years beyond when the law ceased to apply.

31. The June 14, 2002, commercial data does not include any numbers for countrywide data, although Petitioner did do

business in states other than Florida. The form on its face requires a derivation of IBNR loss reserves which was not provided (Line 7). Also on its face, the form requires that a derivation be attached for the profit and contingencies factor (Line 17). None was provided. Unlike the workers' compensation experience submission, the commercial lines filing does not contain a certification or any explanations or supporting documents.

32. On July 12, 2002, Petitioner submitted a revised Form DI4-358, also prepared by Ferguson. Assuming that the commercial portion of the law was still in effect, the revised Form DI4-358 would have been late because it would have been due July 1, 1999. Even with the revisions to countrywide data and expense numbers in the Florida line, the company is still only reporting data for 1995 and 1996. There was still no derivation included for the profit and contingencies factor.

33. An Explanation of Methodology was included, but it was a carbon copy of the one prepared by John Deere for the prior filing and did not have sufficient details to evaluate the reasonableness of the IBNR calculation. Ferguson concedes that she does not know who wrote the explanation and that neither the claims reporting patterns nor the historical data was provided to Respondent. Further, the development triangles referenced in the explanation and the historical patterns to develop case

reserves were not provided either. Loss development triangles are helpful to actuaries in that they assist the actuary in evaluating the appropriateness of the IBNR number.

34. Petitioner's allocated loss adjustment expense reserves were not determined by adding up a series of numbers by accident year, but were instead "spread" across the accident years using a ratio of countrywide split by accident year, which is contrary to the appropriate method of calculating those reserves.

35. Petitioner's countrywide commercial auto liability unallocated loss adjustment expenses are greater than the countrywide numbers shown in Petitioner's Schedule P of their annual statement. For calendar/accident year 1995, the number on the revised DI4-358 form is $657,000.00 greater than what is on the company's Schedule P. For calendar/accident year 1996 the number on the revised DI4-358 form is $916,000.00 greater than what is on the company's Schedule P. Schedule P is the countrywide all-inclusive total for the company. This is an audited number; therefore, it is not possible or appropriate for the countrywide number on the revised DI4-358 form to be greater than what appears on the company's Schedule P.

36. Petitioner's countrywide commercial auto liability allocated loss adjustment expense reserve for calendar/accident year 1996, is $836,000.00 greater than what is found on

Schedule P of the company's annual statement. The countrywide number on the revised DI4-358 form should not be greater than what appears on the company's audited Schedule P.

37. Much of the documentation supplied by Petitioner included computer-generated numbers which were then crossed out and replaced by hand-written numbers, with no explanation being provided for the changes.

38. The paid losses for Florida for calendar/accident years 1995, 1996, and 1997 do not have the appropriate level of detail or underlying documentation (as there is for 1998) to show the source of those numbers.

39. Regarding how the numbers for Florida paid loss, paid allocated expense, and loss reserves to case outstanding and IBNR outstanding were derived in the four-page document entitled, Summary of Data Used in P&C Florida John Deere Excessive Profits Filing as of 12/31/98, statements are made that indicate that there is an unknown problem with the source of the documents from which to get the information to fill out the DI4-358 form. In some instances, Ferguson did not have the data and had to estimate to get the accident year numbers to put on the form. ("However, the paid loss and paid ALE were off in total to page 15. The difference is with the transportation part. One thing is that the fiche for JDTSI included the outside adjusters for the ALE paid, and the page 15 data does

not. Not sure what causes the paid loss difference. We had total numbers for optional and floaters, but did not have accident year data, so had to estimate that split.")

40. On July 15, 2002, Petitioner submitted another revised version of its workers' compensation data which proposed adjustments to reflect reinsurance calculations. Reinsurance was not a factor in the submission received by Respondent on June 14, 2002. These revisions have the effect of reducing the company's excess profits to $467,846.00. Such a result is not possible because Petitioner is not ceding the amount of premium for reinsurance to a non-affiliated company. Petitioner is ceding it to affiliated companies, Rock River Insurance Company and John Deere Casualty Company, under an intercompany pooling arrangement. Under circumstances where Respondent has allowed credit to be taken for reinsurance, such reinsurance has been purchased from a company that is not affiliated or within the company's group.

41. Respondent has never knowingly allowed a company to cede premiums to an affiliate and thereby exclude that amount from its excess profits. Reporting for excess profits net of reinsurance has only been allowed for non-affiliated companies and the credits are only proper in those instances because the money leaves the company.

42. Neither the pooling arrangement nor reinsurance contracts have been provided to Respondent, and Petitioner's pooling arrangement affects prior years' losses because the agreement was entered into in 1997, yet it affects losses for prior years. Further, Petitioner in this revised version, while adding reinsurance, is still using the loss development factors based on direct losses, so there is a "mismatch" between the loss development factor and how it is calculated and the losses to which it is applied.

43. Reinsurance contracts must be reviewed to confirm the existence of reinsurance, the time period for that reinsurance, and the amounts available to the insurer.

44. Ferguson is not familiar with the reinsurance arrangements and has never seen the contracts to verify their existence or terms. She was just told to do it that way.

45. John Deere Insurance Company was acquired in October 1999, by Sentry Insurance Group and then renamed Sentry Select Insurance Company. The former officers of John Deere Insurance Company were replaced, as were certain operating personnel. The individual who is responsible for the content of supporting documentation for the DI4-358 form submitted on June 14, 2002, is not known.

46. The sum of Petitioner's evidence in support of its 1995 and 1996 commercial property and casualty experience is the

DI4-358 form submitted on June 14, 2002, by Ferguson who states that she never worked for John Deere Insurance Company, is not an actuary, that none of the people in the Sentry Select Insurance Company accounting department worked for John Deere Insurance Company, and that she can’t say the records were directly transferred from John Deere Insurance Company to Sentry Select Insurance Company.

47. Holly Lauer is an assistant comptroller with Sentry Select Insurance Company. She has worked with the company for 22 years and has never been employed by anyone else. Lauer was never employed or worked for John Deere Insurance Company. She is licensed as a CPA in Wisconsin, not in Florida, and she is not an actuary. Further, Lauer was not involved and had nothing to do with the transfer of the actuarial work product of John Deere Insurance Company. Lauer did, however, agree that there could be documentation (that is, accident year loss data and documentation) kept by an insurance company’s actuarial department that would not be included in that same insurance company’s accounting department and that that could have been the case with John Deere Insurance Company.

48. Even assuming that the law currently applies to commercial property and casualty excess profits, Petitioner's supporting documentation is insufficient to allow an actuarial

determination of what the correct numbers would be for underwriting profit or underwriting loss.

49. Pursuant to the information supplied by Petitioner (taking into account the residual market and allowing for the change in NCCI loss development factors to the correct years), the company owes workers' compensation excessive profits in the amount of $672,488.00.

CONCLUSIONS OF LAW

50. The Division of Administrative Hearings has jurisdiction over the parties and the subject matter of this cause, pursuant to Sections 120.569(1) and 120.57(1), Florida Statutes.

51. The burden of proof in this case is on Respondent, Florida Department of Insurance. The party seeking to prove the affirmative of an issue has the burden of proof. Florida Department of Transportation v. J.W.C. Company, Inc., 896 So. 2d 778 (Fla. 1st DCA 1981); and Balino v. Department of Health and Rehabilitating Services, 348 So. 2d 349 (Fla. 1st DCA 1977). Pursuant to Section 627.215, Florida Statutes, Respondent has jurisdiction over workers compensation excessive profits in the State of Florida.

52. Section 627.215, Florida Statutes, is the casualty insurance excess profits law. Chapter 95-276, Laws of Florida,

added Subsection (14) to Section 627.215, Florida Statutes, effective June 14, 1995. Subsection 14 provides:

> The application of this law to commercial property and commercial casualty insurance, which includes commercial umbrella liability insurance, ceases on January 1, 1997.

53. The excessive profits experience in this cause covers calendar/accident years 1995, 1996 and 1997. Subsection (14) removed the authority under Section 627.215, Florida Statutes, for Respondent to consider commercial property and casualty experience for the purpose of determining excess profits for the filing for calendar/accident years 1995, 1996 and 1997. Respondent has correctly determined that Petitioner has realized excessive profits in the amount of $672,488.00.

RECOMMENDATION

Based on the foregoing Findings of Fact and Conclusions of Law, it is

RECOMMENDED that Respondent enter a final order finding that Petitioner has realized excessive profits for calendar/accident years 1995, 1996 and 1997 in the amount of $672,488.00.

DONE AND ENTERED this 15th day of November, 2002, in Tallahassee, Leon County, Florida.

DON W. DAVIS
Administrative Law Judge
Division of Administrative Hearings
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Filed with the Clerk of the
Division of Administrative Hearings
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NOTICE OF RIGHT TO SUBMIT EXCEPTIONS

All parties have the right to submit written exceptions within 15 days from the date of this Recommended Order. Any exceptions to this Recommended Order should be filed with the agency that will issue the final order in this case.