

STATE OF NEW JERSEY
DEPARTMENT OF BANKING AND INSURANCE

IN THE MATTER OF:

Proceedings by the Commissioner of Banking)	ORDER TO SHOW CAUSE
and Insurance, State of New Jersey, to have Applied)	
Underwriters, Inc., Applied Underwriters Captive Risk)	
Assurance Company, Inc., Applied Risk Services, Inc., Ref.)	
No. 0091510, and Continental Indemnity Company, NAIC)	
Code 28258, cease and desist from selling the EquityComp,)	
SolutionOne, and PremierExclusive workers' compensation)	
programs, unwind the programs, and pay restitution; to)	
suspend the authority of Continental Indemnity Company to)	
write workers' compensation insurance; and to fine, suspend,)	
and/or revoke the insurance producer license of)	
Applied Risk Services, Inc.)	

TO:

Applied Underwriters, Inc.
c/o Jeffrey A. Silver, Esq., Registered Agent
10805 Old Mill Road
Omaha, Nebraska 68154

Applied Risk Services, Inc.
c/o Jeffrey A. Silver, Esq., Registered Agent
10805 Old Mill Road
Omaha, Nebraska 68154

Applied Underwriters Captive Risk Assurance Company, Inc.
c/o C T Corporation System, Registered Agent
400 E Court Ave.
Des Moines, Iowa 50309

Continental Indemnity Company
c/o Jeffrey A. Silver, Esq., Registered Agent
10805 Old Mill Road
Omaha, Nebraska 68154

This matter, having been opened by the Commissioner of Banking and Insurance (“Commissioner”), State of New Jersey, upon information that Applied Underwriters, Inc. (“Applied”), Applied Risk Services, Inc. (“ARS”), Applied Underwriters Captive Risk Assurance Company, Inc. (“AUCRA”), and Continental Indemnity Company (“Continental”) (collectively, “Respondents”) may have violated various provisions of the insurance laws of the State of New Jersey; and

WHEREAS, Respondents are subject to the provisions of the New Jersey Insurance Producer Licensing Act of 2001, N.J.S.A. 17:22A-26 to -48 (“Producer Act”), the general penalty provision of N.J.S.A. 17:33-2, and the Employers’ Liability Insurance Law, N.J.S.A. 34:15-70 to -95.5; and

WHEREAS, pursuant to N.J.S.A. 17:22A-40(a)(2), an insurance producer shall not violate any insurance laws, or violate any regulation, subpoena or order of the Commissioner or of another state’s insurance regulator; and

WHEREAS, pursuant to N.J.S.A. 17:22A-40(a)(5), an insurance producer shall not intentionally misrepresent the terms of an actual or proposed insurance contract, policy, or application for insurance; and

WHEREAS, pursuant to N.J.S.A. 17:22A-40(a)(8), an insurance producer shall not use fraudulent, coercive or dishonest practices, or demonstrate incompetence, untrustworthiness or financial irresponsibility in the conduct of insurance business; and

WHEREAS, pursuant to N.J.S.A. 17:22A-40(a)(16), an insurance producer shall not commit any fraudulent act; and

WHEREAS, pursuant to N.J.S.A. 17:22A-40(a)(17), an insurance producer shall not knowingly facilitate or assist another person in violating any insurance laws; and

WHEREAS, pursuant to N.J.S.A. 17:33-2, the penalty for any violation of N.J.S.A. 17:17-1 to 17:51B-4, other than the failure of an insurance company to file an annual statement, shall be a penalty not exceeding \$1,000 for the first offense and not exceeding \$2,000 for each subsequent offense; and

WHEREAS, pursuant to N.J.S.A. 34:15-88, every insurance company or mutual association which insures employers against liability either under the Employers' Liability Insurance Law or for damages imposed by law arising out of any other liability to employees because of personal injuries including death at any time resulting therefrom, or both, shall file with the Commissioner its classification of risks and premiums and rules pertaining thereto, together with the basis rates and system of merit or schedule rating applicable to such insurance; and

WHEREAS, N.J.S.A. 34:15-88 further provides that no insurance company or mutual association writing workmen's compensation or employer's liability insurance in this state shall issue, renew, or carry any insurance against the liability of an employer either for compensation or for damages imposed by law, because of personal injuries, including death at any time resulting therefrom, sustained by his employees, or for both, except in accordance with the classifications, rules, basis rates, and system of merit or schedule rating approved by the Commissioner as aforesaid and applied by the New Jersey Compensation Rating and Inspection Bureau ("CRIB"); and

WHEREAS, N.J.S.A. 34:15-88 further provides that if any insurance company or mutual association authorized to write workmen's compensation or employer's liability insurance in this state shall violate any of the provisions of the Employers' Liability Insurance Law, the Commissioner, may, in her discretion, after public hearing, suspend the

authority of said insurance company or mutual association to transact workmen's compensation or employer's liability insurance in this state for such period as said Commissioner shall fix; and

WHEREAS, pursuant to N.J.S.A. 34:15-90.2(f), CRIB shall have authority to establish and maintain rules, regulations and premium rates for workers' compensation and employers' liability insurance and equitably adjust the same; and

WHEREAS, pursuant to N.J.S.A. 34:15-90.2(i), CRIB shall have authority to prepare and file, for the approval of the Commissioner, and for the use by all of its members, any amendments to its policy forms and its system of classification of risks and premiums thereto, together with the basis rates and system of merit or schedule rating applicable to such insurance, as currently set forth in the New Jersey Workers' Compensation and Employers' Liability Insurance Manual; and

WHEREAS, pursuant to the New Jersey Workers' Compensation and Employers' Liability Insurance Manual, Part Three, Section 3, Page 1, Paragraph 9, no endorsement shall be issued or attached to any Workers Compensation or Employers Liability Policy which purports to construe, alter, limit, waive or extend any of the provisions of the policy or the applicable provisions of the Employers' Liability Insurance Law, except as otherwise provided by the Manual; and

FACTUAL ALLEGATIONS

IT APPEARING, that Applied is an indirect subsidiary of Berkshire Hathaway Inc. and is the parent company of AUCRA and ARS. Applied is a Nebraska financial service corporation that provides payroll processing services and underwrites workers' compensation insurance through its affiliated insurance companies to small and medium-

sized employers. Applied's address is 10805 Old Mill Road, Omaha, Nebraska 68154. Applied is not an authorized or admitted insurer and is not permitted to enter into insurance contracts or engage in the business of insurance in New Jersey; and

IT FURTHER APPEARING, that ARS is currently licensed as a non-resident business entity insurance producer in the State of New Jersey, pursuant to N.J.S.A. 17:22A-34, with an address of 10805 Old Mill Road, Omaha, Nebraska 68154. ARS is a subsidiary of Applied and also acts as a billing agent; and

IT FURTHER APPEARING, that AUCRA is an insurance company organized and existing under the laws of Iowa with its principal place of business in Omaha, Nebraska, with an address of 10805 Old Mill Road, Omaha, Nebraska 68154. AUCRA is a subsidiary of Applied, and its purpose is to serve as a reinsurance arm for Applied. AUCRA is not an authorized or admitted insurer and is not permitted to enter into insurance contracts or engage in the business of insurance in New Jersey; and

IT FURTHER APPEARING, that Continental is a foreign insurer domiciled in Iowa, with an address of 10805 Old Mill Road, Omaha, Nebraska 68154. Continental is licensed in the State of New Jersey to issue accident and health, property, and casualty, and workers' compensation insurance policies. Continental is an indirect subsidiary of Applied; and

IT FURTHER APPEARING, that the Boards of Directors for Applied, ARS, AUCRA, and Continental are identical in composition. Jeffrey A. Silver, Esq., Applied's General Counsel, serves on each of these Boards; and

IT FURTHER APPEARING, that from 2008 to present, Respondents marketed and sold workers' compensation programs called EquityComp, SolutionOne, and/or PremierExclusive (collectively, the "programs") to at least 300 New Jersey employers; and

IT FURTHER APPEARING, that these programs combine issuance of a guaranteed cost workers' compensation policy¹ sold by Continental and a "reinsurance participation agreement" ("RPA") with AUCRA; and

IT FURTHER APPEARING, that the guaranteed cost workers' compensation component of the programs uses forms and rates that were filed with CRIB and approved by the Commissioner, but that the RPA and the programs were never filed with CRIB nor approved by the Commissioner; and

IT FURTHER APPEARING, that Applied has patented the RPA. The patent states that the purpose of the RPA is to allow small and medium sized employers to utilize retrospective rating plans,² a practice which is only permitted in New Jersey under certain circumstances not applicable to the RPA, including but not limited to filing and compliance with CRIB's parameters for retrospective rating plans as approved by the Commissioner.³

¹ A guaranteed cost policy essentially fixes an employer's insurance premiums, meaning that the actual cost of claims against the policy will not cause premiums to fluctuate during the life of the policy. Nat'l Convention Servs., LLC v. Applied Underwriters Captive Risk Assur. Co., 239 F. Supp. 3d 761, 769 (S.D.N.Y. Mar. 9, 2017).

² A retrospective rating plan is a loss sensitive insurance policy, meaning that premiums can fluctuate during the life of the policy depending on the actual cost of the claims. Ibid.

³ In New Jersey, retrospective rating plans are available on a one or three year rating period to any insured with estimated annual standard premium of at least \$25,000. The Large Risk Alternative Rating Option, another optional form of Retrospective Rating, is available to any insured with estimated annual workers compensation and employers liability standard premium of \$100,000 of New Jersey or countrywide premium, or in any combination with any other commercial casualty line of insurance for the rating term. New

One of the challenges of introducing a fundamentally new premium structure into the marketplace is that the structure must be approved by the respective insurance departments regulating the sale of insurance in the states in which the insureds operate.

In the United States, each state has its own insurance department and each insurance department must give its approval to sell insurance with a given premium plan in its respective jurisdiction. Getting approval can be extremely time consuming and expensive, particularly with novel approaches that a department hasn't had experience with before. Also, many states require insurance companies to only offer small sized and medium sized companies a Guaranteed Cost plan, without the option of a retrospective plan. In part, this is because of governmental rules and laws that regulate the insurance industry.

Disclosed herein is a reinsurance based approach to providing non-linear retrospective premium plans to insureds that may not have the option of such a plan directly.

[Reinsurance Participation Plan, US Patent No. 7,908,157 B1 (issued Mar. 15, 2011), at col. 6, lines 22-40.]

IT FURTHER APPEARING, that the patent continues to describe how Respondents attempt to evade regulatory oversight of their programs:

[C]ompliance with regulatory requirements that do not make specific provision for these plans . . . is based on the fact that an insurance carrier can cede a certain portion of an insurance risk to a reinsurance company. Said reinsurance company can, in turn, enter into a separate Participation Agreement with the insured whereby a credit or debit is assessed on the insured as a function of the losses experienced by each insured.

An admitted insurance carrier . . . has a license from a state insurance department . . . to sell Guaranteed Cost workers' compensation insurance in a given state. The insurance carrier obtains approval by using an industry standard Guaranteed Cost policy and filing premium rate requests

Jersey Workers Compensation Employers Liability Insurance Manual (2018), Part Three, Sec. 12, p. 1.

with the insurance department The insurance department, already familiar with the policy, approves the rates. . . .

The insurance carrier then contractually arranges with a broker . . . to sell said standard policies to a targeted class of companies. These targeted classes include small sized . . . and medium sized . . . companies.

[Id. at col. 6, lines 45-63.]

IT FURTHER APPEARING, that the patent explains how an employer's use of the RPA results in an employer obtaining a retrospective rating plan:

The reinsurance company . . . can now provide funds to implement a non-linear retrospective rating plan as a "participation plan." The reinsurance company does this by entering into a separate contractual arrangement with the insured. If the insured has lower than average losses in the next year, then the reinsurance company can provide a premium reduction . . . according to the participation plan. If the insurance has higher than average losses in a given year, then the reinsurance company will assess additional premium . . . accordingly. The insured can now, in effect, have a retrospective rating plan because of the arrangement among the insurance carrier . . . , the reinsurance company . . . , and the insured, even though, in fact, the insured has Guaranteed Cost insurance coverage with the insurance carrier

[Id. at col. 7, lines 41-54.]

IT FURTHER APPEARING, that the RPA potentially leads to higher and unpredictable assessments against an employer should a certain level of claims occur; and

IT FURTHER APPEARING, that the RPA causes the ultimate cost and other key contractual terms of the guaranteed-cost workers' compensation policy to be materially different than those filed with CRIB and approved by the Commissioner; and

IT FURTHER APPEARING, that the state insurance departments of California, Vermont, and Wisconsin have concluded that the programs do not comply with their states'

insurance laws, because the RPA is a collateral agreement that modifies the underlying guaranteed cost policy, and that the RPA was required to be filed with and approved by the insurance departments of those states; and

IT FURTHER APPEARING, that the Supreme Court of Nebraska, Respondents' home state, in Citizens of Humanity, LLC v. Applied Underwriters Captive Risk Assur. Co., 909 N.W. 2d 614, 620-21, 632-33 (Neb. 2018), found that the RPA was a retrospective rating plan and that it was not a reinsurance contract; and

IT FURTHER APPEARING, that on June 4, 2012, Applied's General Counsel met with representatives of CRIB and spoke about the programs, but the conversation did not constitute approval of the program by the Commissioner; and

IT FURTHER APPEARING, that the RPA is a de facto Retrospective Rating Plan Endorsement that materially modifies the guaranteed-cost workers' compensation policy of the programs; therefore, the RPA and the programs must be filed with CRIB and approved by the Commissioner; and

VIOLATIONS OF LAW

COUNT 1

IT FURTHER APPEARING, that from 2008 to present, Respondents marketed and sold an unfiled and unapproved workers' compensation program with impermissible retrospective rating to at least 300 New Jersey employers that, based on a sampling, resulted in approximately 85% of those employers owing approximately \$18.9 million to Respondents, often in excess of CRIB's approved premium rates, in violation of N.J.S.A. 17:22A-40(a)(2), (5), (8), (16), and (17); and N.J.S.A. 34:15-88;

NOW, THEREFORE, IT IS on this 6th day of March, 2019;

ORDERED, Respondent Continental appear and show cause why its authority to transact workmen's compensation or employer's liability insurance should not be suspended, pursuant to N.J.S.A. 34:15-88; and

IT IS FURTHER ORDERED, that Respondents appear and show cause why they should not be ordered to unwind the programs, pursuant to N.J.S.A. 34:15-88; and

IT IS FURTHER ORDERED, that Respondents appear and show cause why they should not be ordered to cease and desist from collecting additional premiums from insured New Jersey businesses that may have paid less than they would have under their Continental policy including voiding all contracts, liens or promissory notes entered into by New Jersey businesses with the Respondents regarding payment of the additional premium due under the retrospective rating, pursuant to N.J.S.A. 34:15-88; and

IT IS FURTHER ORDERED, that Respondent ARS appear and show cause why its insurance producer license shall not be revoked by the Commissioner, pursuant to N.J.S.A. 17:22A-40a; and

IT IS FURTHER ORDERED, that Respondents appear and show cause why the Commissioner should not assess a fine of up to \$5,000 for the first violation, and \$10,000 for each subsequent violation of the Producer Act, and/or \$1,000 for the first offense and not exceeding \$2,000 for each subsequent offense as applicable under N.J.S.A. 17:33-2, and order Respondents to pay restitution of moneys owed to any person, pursuant to N.J.S.A. 17:22A-45c. Restitution shall include return of all insurance premiums in excess of the premiums that should have been charged by Continental in accordance with the approved CRIB rating system, after any applicable payroll audits, and excluding specified

fees for non-insurance services under the RPA, such as those for payroll processing, with interest; and

IT IS FURTHER ORDERED, that Respondents appear and show cause why they should not be required to reimburse the Department of Banking and Insurance for the costs of the investigation and prosecution authorized pursuant to N.J.S.A. 17:22A-45c; and

IT IS PROVIDED, that Respondents have the right to request an administrative hearing, to be represented by counsel or other qualified representative, at their own expense, to take testimony, to call or cross-examine witnesses, to have subpoenas issued, and to present evidence or argument if a hearing is requested; and

IT IS FURTHER PROVIDED, that, unless a request for a hearing is received within twenty (20) days of the service of this Order to Show Cause, the right to a hearing in this matter shall be deemed to have been waived by Respondents, and the Commissioner shall dispose of this matter in accordance with law. A hearing may be requested by mailing the request to Virgil Downtin, Chief of Investigations, Department of Banking and Insurance, P.O. Box 329, Trenton, New Jersey 08625, or by faxing the hearing request to the Department at (609) 292-5337. A copy shall also be sent to Deputy Attorney General Adam B. Masef, R.J. Hughes Justice Complex, 25 Market Street, P.O. Box 117, Trenton, New Jersey 08625. The request shall contain the following:

- (a) Respondent's full name, address and daytime telephone number;
- (b) A statement referring to each charge alleged in this Order to Show Cause and identifying any defense intended to be asserted in response to each charge. Where the defense relies on facts not contained in the Order to Show Cause, those specific facts must be stated;
- (c) A specific admission or denial of each fact alleged in this Order to Show Cause. Where the Respondent has no specific knowledge regarding a fact alleged in the Order to Show Cause, a statement to that effect must be

contained in the hearing request. Allegations of this Order to Show Cause not answered in the manner set forth above shall be deemed to have been admitted; and

- (d) A statement requesting the hearing.



Marlene Caride
Commissioner