

BIG DECISION: Travelers Loses Unfiled Side Agreements Case

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Ryan Salsig

“The big takeaway from this is that under Insurance Code section 11737, the Commissioner has the authority to review pretty much anything that affects what the insured pays for insurance,” says attorney Ryan Salsig with the firm Roxborough, Pomerance, Nye & Adreani.

The California Insurance Commissioner's authority to require carriers to file key policy documents for pre-approval and – more importantly – to void those agreements that were not filed was reaffirmed and reinforced by a Los Angeles Superior Court.

The court rejected a challenge to that authority by The Travelers (NYSE: TRV) that sought to overturn a precedential decision by former Insurance Commissioner Dave Jones that invalidated its workers' comp large deductible side agreement.

Salsig argued the case for the successful employer– Davidson Hotel. "It's not just what is technically insurance premium, but also the other fees, other costs, other charges – anything that sums up to the money paid by the insured for the insurance appears to be within the Commissioner's jurisdiction."

The case stems from the four-year-old dispute between Travelers and Davidson over the legality of the large deductible program agreements. The agreements defined how premium would be calculated, established a collateral requirement, required mandatory arbitration of all disputes, and supplanted the cancellation terms of the guaranteed cost workers' comp policy attached to the program.

Former Commissioner Jones held the agreements were void and unenforceable as they had not been filed before use as required by Insurance Code section 11658/11735 and California Code of Regulations Title 10, Section 2268. The decision held that the side agreements "misapplied Travelers' filed rating plan."

Jones' decision equated the side agreements with endorsements that must be filed and approved before use. The Commissioner also found that the agreements constitute collateral agreements that must be filed, attached, and made part of the workers' comp policy. They were not.

Davidson is a national hotel chain based in Tennessee, but about 10% of its workforce is in California. It paid Travelers roughly \$20 million a year from 2009 through 2012 for workers' comp coverage for all its employees.

As a remedy, Commissioner Jones ordered Travelers to refund any premium that was paid in excess of what would have been required by the guaranteed cost policy absent the large deductible program agreements (For past coverage see [Travelers' Unfiled...](#), [Travelers Sues...](#), and [Travelers, CDI...](#)).

The decision could have significant implications for the myriad disputes pending between Applied Underwriters and employers over its unfiled and unapproved reinsurance participation agreements in its EquityComp program, according to sources. Those cases, however, are currently enjoined due to California Insurance Company's conservation status. Applied's arguments have mirrored many of those raised by Travelers that the court rejected. Attorneys in the EquityComp cases also note that Applied wanted the Davidson case to proceed first.

Commissioner's Jurisdiction

Travelers argued in its petition that the Commissioner's decision was "riddled with factual errors and factual assertions." Additionally, it maintained that the Commissioner lacked jurisdiction under Insurance Code section 11737 to hear Davidson's appeal in the first place as Travelers asserted that the dispute was a form filing one, not a rate dispute.

The court was not persuaded. "While the court agrees that the pure premium rate is not used to calculate premium for a deductible plan, Travelers fails to rebut the point in the Commissioner's decision that the side agreement contained supplementary rating information because it alters the [Allocated Loss Adjustment Expense's Medical Cost Containment] expense obligation from actual expenses to a 27% charge on resulting savings. This is a change in Davidson's insurance cost, which is part of the rating system," the court held.

“Travelers’ witnesses admitted that the Side Agreement governed premium, billing, risk of loss, cancellation, and indemnification.” -- Los Angeles Superior Court

“Travelers also fails to address the Decision’s finding that the Side Agreement materially altered Davidson’s financial obligations under the program,” the court said, noting that the agreement added an initial collateral requirement and a cash collateral adjustment formula. Additionally, the agreements permitted Travelers to require a letter of credit, unilaterally adjust the cash collateral amount, deplete the cash collateral, and apply loss development factors. “Travelers’ witnesses admitted that the Side Agreement governed premium, billing, risk of loss, cancellation, and indemnification,” the court pointed out

Applies Retroactively

The court also held that the Commissioner has the authority to retroactively void side agreements/endorsements that were not filed as required. Travelers attempted to argue that Insurance Code section 11658(b) only allows for the prospective disapproval of a form or endorsement, such as the side agreements.

The court notes that this argument misses a crucial point – the prospective limitation is for the disapproval of filed forms and endorsements, not ones that were never filed. “[A]n interpretation of section 11658 that limited the Commissioner to a prospective prohibition on the issuance of unfiled forms and endorsements would lead to an absurd result,” the court wrote. “An insurer could fail to file the required document with impunity until it is caught, and then slightly change the document in order to continue using it.”

The court’s findings parallel those in recent actions against Applied Underwriters and its unfiled, unapproved reinsurance participation agreement in its EquityComp program. The Los Angeles Court noted the recent appellate decisions in the *Nielsen*, *Luxor*, and *Jackpot Harvesting* cases that dealt with the unfiled arbitration clauses that Applied used in the program. Each appellate court held that the failure to file the endorsement containing this clause would render the endorsement unlawful and void – the same conclusion reached in the Davidson case.

In denying the petition, the court ordered counsel for the Department to draw up a proposed judgment order. Parties are due back in court later this month to finalize the judgment.