

**DEPARTMENT OF LABOR****Employment Standards Administration****20 CFR Parts 701 and 703**

RIN 1215-AB38

**Regulations Implementing the Longshore and Harbor Workers' Compensation Act and Related Statutes****AGENCY:** Employment Standards Administration, Labor.**ACTION:** Final rule.

**SUMMARY:** This final rule requires each insurance carrier authorized to write insurance under the Longshore and Harbor Workers' Compensation Act and its extensions (the Defense Base Act; the Outer Continental Shelf Lands Act; the Nonappropriated Fund Instrumentalities Act; and the District of Columbia Workmen's Compensation Act) to demonstrate to the Office of Workers' Compensation Programs (OWCP) that its LHWCA obligations are sufficiently secured and, if necessary, to deposit security in an amount set by OWCP. This procedure will ensure the prompt and continued payment of compensation and medical benefits to injured workers and help protect the Longshore special fund's assets from consequences flowing from insurance carrier insolvencies. In addition, the rule conforms, where appropriate, the rules governing OWCP's authorization of employers as self-insurers to the provisions governing carrier security deposits.

**DATES:** This rule is effective August 25, 2005.

**FOR FURTHER INFORMATION CONTACT:** Michael Niss, Director, Division of Longshore and Harbor Workers' Compensation, Office of Workers' Compensation Programs, Employment Standards Administration, 202-693-0038. TTY/TDD callers may dial toll free (877) 889-5627 for further information.

**SUPPLEMENTARY INFORMATION:****I. Background of This Rulemaking**

On March 15, 2004, the Department issued a Notice of Proposed Rulemaking (NPRM) under the Longshore and Harbor Workers' Compensation Act, as amended (LHWCA), 33 U.S.C. 901 *et seq.*, proposing rules governing insurance carrier security deposits. 69 FR 12218-31 (March 15, 2004). As explained in the NPRM (69 FR 12218-19 (March 15, 2004)), since 1990 the Department has required insurance carriers it has authorized to write

Longshore coverage to deposit security in an amount sufficient to secure the payment of their LHWCA obligations in States without guaranty or analogous funds and in States whose funds do not fully secure such obligations. The Department waived the deposit requirement for carriers with financial security ratings of "A" or higher issued by the A.M. Best Company. Intervening changes in the insurance industry and related insurance rating systems, however, prompted the Department to re-examine and reformulate its security deposit policy. The NPRM embodied the Department's proposal to revamp this policy.

The NPRM proposed a process by which OWCP would determine: (1) The extent of an insurance carrier's unsecured LHWCA obligations; (2) the deposit amount necessary to secure those obligations in light of the guaranty or analogous funds in the State or States in which the carrier writes LHWCA insurance; (3) how such deposit will be held; and (4) when OWCP may seize or otherwise use deposited funds. 69 FR 12219 (March 15, 2004). The proposed rules also eliminated the Department's prior waiver policy so that all carriers, regardless of their financial strength, would be subject to the deposit requirements. 69 FR 12219 (March 15, 2004).

The Department has received five written comments in response to the NPRM: two from insurance carriers and one each from an insurance carrier association, a Longshore employer association, and a state insurance division. The Department has found these comments very helpful and, in several important respects, has revised the final rule in response.

**II. Explanation of Changes****A. Statutory Authority**

Congress granted the Department broad authority to "administer the provisions of [the LHWCA], and for such purpose the Secretary is authorized (1) to make such rules and regulations \* \* \* as may be necessary in the administration of the Act." 33 U.S.C. 939(a). Three commenters fully support the Department's efforts to ensure a financially sound Longshore program through the proposed rules. Two commenters, however, argue that the LHWCA does not grant the Department authority to require carriers to post security deposits. They contend that section 32 (33 U.S.C. 932, erroneously referenced by the commenters as 33 U.S.C. 939) allows the Department to require employers who seek to self-insure to deposit security

but does not allow imposition of a similar requirement on carriers. In these two commenters' view, the Department must instead rely on the various State regulators' supervision of carriers and those regulators' assessment of a carrier's financial strength to ensure solvency and the carrier's future ability to meet its obligations.

The Department disagrees with the commenters' construction of the statute and believes it has acted well within its rulemaking authority. Section 32 provides, in relevant part:

(a) Every employer shall secure the payment of compensation under this Act—

(1) By insuring and keeping insured the payment of such compensation with any stock company or mutual company or association, or with any other person or fund, which such person or fund is authorized (A) under the laws of the United States or of any State, to insure workmen's compensation, and (B) by the Secretary, to insure payment of compensation under this Act; or

(2) By furnishing satisfactory proof to the Secretary of his financial ability to pay such compensation and receiving an authorization from the Secretary to pay such compensation directly. The Secretary may, as a condition to such authorization, require such employer to deposit \* \* \* either an indemnity bond or securities \* \* \* in an amount determined by the Secretary, based on the employer's financial condition, the employer's previous record of payments, and other relevant factors. \* \* \*

(b) In granting authorization to any carrier to insure payment of compensation under this Act the Secretary may take into consideration the recommendation of any State authority having supervision over carriers or over workmen's compensation. \* \* \* The Secretary may suspend or revoke any such authorization for good cause shown. \* \* \*

33 U.S.C. 932.

Section 32 ensures that there is money available to pay compensation to an injured worker. *United Marine Mutual Indemnity Assn. v. Marshall*, 510 F.Supp. 34, 36 (N.D. Cal. 1981), *affm'd sub nom., United Marine Mutual Indemnity Assn. v. Donovan*, 701 F.2d 791 (9th Cir. 1983). The Act seeks "certain and absolute payment" of compensation, *United Marine*, 510 F.Supp. at 36, and the "major guarantee of the financial ability of the employer to compensate those injured or killed in the scope of employment is found in section 32." *Id.* at 793. As one court has noted, "[i]t is obvious from the language chosen that Congress wanted a central approval mechanism to support the fiscal soundness of the LHWCA system." *Id.*

To accomplish these goals, section 32(a)(1)(B) gives the Secretary discretion to authorize insurance carriers to write Longshore coverage. Apart from

requiring that the carrier be authorized by a State (or the United States) to insure workers' compensation, 33 U.S.C. 932(a)(1)(A), and permitting the Secretary to consider a State's recommendation as to the insurer's status, 33 U.S.C. 932(b), section 32 grants the Secretary the power to authorize carriers without any limitation, description, standards, or guidance. The power to authorize necessarily includes the power to refuse authorization as well; any other interpretation would render meaningless section 32(a)(1)(B)'s grant of authority to the Secretary to authorize carriers. Once granted, authorization may be suspended or revoked for "good cause." *Id.* By using broad, undefined terms such as "authorization" and "good cause," Congress afforded the Secretary wide discretion in deciding which carriers should be allowed to write Longshore insurance.

Requiring carriers to post security as a condition of authorization to write Longshore insurance is a proper exercise of the Secretary's authority under section 32. The deposits fulfill section 32's goal because they will prevent interruption in compensation payments and medical benefits to injured workers in the event the carrier defaults or becomes insolvent. Moreover, the statute does not compel the Secretary to authorize any carrier she believes may not be able to meet its LHWCA obligations. No conceivable legislative purpose would be served, however, by precluding authorization of a carrier who demonstrates actual reliability by posting security. In fact, permitting the Secretary to require insurance carriers whom she might not otherwise authorize to post security enlarges, rather than diminishes, the opportunities available to carriers.

One commenter points to section 32(b), 33 U.S.C. 932(b), and argues that Congress intended the Secretary to rely exclusively on the various States' supervision of carriers to assure a carrier's future ability to meet its LHWCA obligations. The plain terms of the statute, however, contradict this interpretation. First, Congress wrote section 32(b) in permissive language: "the Secretary *may*" consider a State supervisory authority's recommendation in making an authorization decision, but the statute does not require her to do so. Second, although State licensure is a condition to authorization, 33 U.S.C. 932(a)(1)(A), State approval is not sufficient alone because the statute also requires authorization by the Secretary to write Longshore insurance. 33 U.S.C. 932(a)(1)(B). Indeed, the commenter's view reads Section 32(a)(1)(B) out of the

statute. The sweeping language of the statute and the sparseness of its requisites, coupled with Congress' decision not to make State licensure sufficient alone, all suggest congressional intent to permit the Secretary to condition authorization on the terms the Secretary considers most appropriate.

One comment states that because the statute expressly permits the Secretary to impose a security deposit requirement on employers seeking authorization to self-insure, 33 U.S.C. 932(a)(2), but does not include the same provision for carriers, Congress intended to preclude the Secretary from imposing this condition on carriers. The Department disagrees. The statute's express security deposit provision for self-insurers is logical because Longshore employers, unlike insurers, would not have funds put aside to cover their liabilities under the statute. Thus, security deposits the Department requires from self-insurers under section 32(a)(2) may be the only source of payment available for an employer's LHWCA obligations. Insurers, on the other hand, may have additional sources for the payment of carrier obligations, such as State guaranty funds. The statute therefore appropriately gives the Secretary wide latitude to regulate within the carrier authorization arena.

The Secretary could have determined that the steps States take to ensure a carrier's fiscal soundness, including any coverage afforded by State insurance guaranty funds, were sufficient to fulfill section 32's goal of ensuring adequate funds to compensate injured workers. But experience has proved that wrong. *See generally* 69 FR 12218-19 (March 15, 2004). In 2003 and 2004, 23 carriers authorized to write Longshore insurance became insolvent. For one of these carriers, the Department has already exhausted the company's \$200,000 deposit (made under OWCP's existing policy) and is now paying the carrier's remaining obligations from the special fund. For two other carriers, whose security deposits total approximately \$11,000,000, the Department is currently meeting the carriers' obligations by using the deposited security. The Department anticipates that it will exhaust those funds and will have to pay all remaining obligations from the special fund. Had the security deposits not been available, the industry as a whole, through annual special fund assessments, would have borne the full brunt of these insurers' insolvency. *See* 33 U.S.C. 918(b), 944.

Moreover, the statute's structure does not reveal congressional intent to limit the Secretary's regulatory options by

negative implication. As already noted, section 32 contains virtually no limitations on the Secretary's right to authorize carriers to write Longshore coverage. And the Secretary may exercise her right to revoke authorization for "good cause," a term of broad compass. Given the broad general rulemaking authority conferred on the Secretary by section 39(a), and the sweeping authority section 32 gives the Secretary to grant or deny carrier authorization, it is counterintuitive to draw from Congress' silence a flat prohibition on the Secretary's ability to condition a carrier's authorization to write Longshore insurance on a deposit of security.

One comment contends that the proposed rules improperly create an "extra-statutory" funding and payment structure because the Secretary has no authority to put seized deposits into the special fund under the funding mechanism set out in section 44 of the Act (33 U.S.C. 944), and the statute gives the Secretary no obligation or authority to pay for insolvent employers or insurers except from the special fund under section 18(b) (33 U.S.C. 918(b)). In this same vein, the commenter also argues that the Secretary cannot set up a separate guaranty fund for Longshore benefits to protect employers from carrier insolvencies.

The commenter misapprehends the nature of carrier security deposits. Security posted by a carrier under OWCP's current policy and these final rules is neither allocable to, nor payable from, the special fund established by section 44. Instead, the Department treats carrier security deposits in the same manner as security deposits made by authorized self-insurers, which are not placed in the special fund. *See* 33 U.S.C. 932(a)(2) (as a condition to self-insurer authorization, the Secretary may "require such employer to deposit in a depository designated by the Secretary either an indemnity bond or securities \* \* \*"). Accordingly, negotiable securities posted by carriers are deposited in a Department of Labor Federal Reserve Bank account (now in St. Louis, Missouri) and held under sub-accounts the Bank creates in the name of each carrier and self-insurer. The Bank pays the carrier interest on the deposited securities as it accrues. The Department has no authority to disperse funds from these accounts. Letters of credit and indemnity bonds posted by carriers are held by OWCP in its Washington, DC office.

In the event the Department redeems the posted security, and the security is in the form of a surety bond, the surety will pay claims directly. If, however, the

security is in the form of a letter of credit or negotiable securities, OWCP deposits the proceeds of the security in an OWCP agency account, established by the Treasury Department, so that OWCP may disperse the funds when necessary. This agency account also contains, *inter alia*, monies that constitute the section 44 special fund, proceeds of seized self-insurer security deposits, and monies payable under the District of Columbia Workmen's Compensation Act. The carriers' security proceeds are neither part of the section 44 special fund nor pooled to form a separate insurance carrier guaranty fund. Instead, like the Federal Reserve Bank, OWCP creates sub-accounts for each carrier so that both interest on, and payments from, the security deposit proceeds are allocated to the individual carrier.

Security deposits simply provide some measure of assurance that a carrier will meet its *own* payment obligations. These obligations are separate from the increased assessment costs the carrier may also bear for another carrier's or employer's insolvency when the special fund makes payments under Section 18(b). Because OWCP uses a carrier's security deposit solely to satisfy the carrier's own liabilities, OWCP pays claims from the deposits in the same manner the carrier would. Accordingly, OWCP does not require claimants to follow the procedure set forth in section 18(b) for payments made from the special fund. If, for example, the employer is bankrupt and the carrier was voluntarily paying compensation to an injured worker prior to becoming insolvent, OWCP will continue those payments on the carrier's behalf if that carrier deposited security and continued payments are appropriate. Once the security deposit is exhausted, however, the claimant must obtain a compensation order before OWCP will make payments from the special fund under section 18(b).

Thus, rather than imposing an independent obligation on the United States or seeking to alter the role of the special fund, as the commenter suggests, security deposits provide a separate mechanism through which a carrier's liabilities may be satisfied. If the carrier fully discharges its payment obligations, then OWCP never uses the carrier's security deposit and returns it (or any unused portion) to the carrier (or its successor in interest) when the carrier ceases writing Longshore insurance or becomes insolvent. See §§ 703.209(c) and 703.211(c). For instance, one of the 23 insolvent carriers mentioned above had posted a \$400,000 deposit in the form of negotiable securities. Because

the carrier had no remaining LHWCA obligations, OWCP returned the deposited securities to the State office handling the carrier's liquidation.

Finally, nothing in the proposed or final rules relieves an employer from its payment obligations if its insurer is financially incapable of meeting those obligations. See generally 33 U.S.C. 904(a); *B.S. Costello v. Meagher*, 867 F.2d 722 (1st Cir. 1989). In these circumstances, OWCP routinely seeks payment from the employer before turning to any deposited security. Only if the employer is also unable to pay due to insolvency does OWCP use the carrier's deposited security. OWCP intends to continue this practice under these rules.

#### *B. Changes Made Between Proposed and Final Rule To Allow Exemption From the Deposit Requirements for Certain Carriers*

The proposed rule eliminated OWCP's current practice of exempting those carriers who have an "A" or higher A.M. Best rating. See 69 FR 12218–19 (March 15, 2004). Instead, the proposal required all carriers authorized to write Longshore insurance, regardless of their financial strength, to deposit security based on the amount of their outstanding Longshore obligations not otherwise secured by State guaranty funds. Two comments generally support this approach. Two other comments, however, object to eliminating the exemption and propose alternatives.

Commenters lodging objections point out that eliminating the exemption increases operating costs for the financially strongest companies who are exempt under OWCP's current policy. These companies pose the least risk to the special fund. The commenters also argue against moving away from private insurance carrier rating systems to a new system of OWCP's creation because the private rating systems provide an objective, verifiable standard for determining whether a particular company is financially fit. Thus, rather than eliminating the exemption altogether, the commenters recommend that OWCP elevate the standard for exempting companies, and they offer a variety of suggestions for accomplishing this goal: Raise the required rating above the current A.M. Best "A" rating; consider ratings from multiple recognized carrier rating systems; factor in the carrier's overall size, as well as the size of its Longshore exposure; and consider the carrier's longevity in the workers' compensation insurance market.

The Department agrees that the strongest carriers should be exempt from the security deposit requirements. In implementing this decision, the Department has adopted the commenters' suggestion to strengthen the criteria for exemption. Under the final rule, carriers awarded the highest rating by each of three private insurance carrier rating services designated on OWCP's web site—currently, A.M. Best, Standard & Poor's, and Weiss Research—for the current rating year and the immediately preceding year will be exempt from the security deposit requirements. This change is reflected in revisions the Department has made to §§ 703.203(a) and 703.204(c)(1). The Department estimates that 10% of currently authorized carriers will meet the new exemption requirements.

The Department's decision to exempt certain carriers remains faithful to the measured approach the Department advocated in the NPRM. 69 FR 12219 (March 15, 2004). Although exempting even one carrier necessarily entails some degree of additional risk for the special fund, the Department believes that it has substantially reduced that risk by adopting a more stringent financial test for exemption than currently used so that only the strongest carriers—those least likely to run into financial difficulties—are granted an exemption. Moreover, by looking at ratings from three private systems and requiring sustained superior financial ratings over a two-year period, the Department believes it has minimized the impact of flaws inherent in any one static rating scheme for predicting future financial performance.

Granting an exemption to the strongest carriers has additional benefits. First, very strong carriers will not be discouraged from participating in the Longshore insurance market by the added costs the security deposit requirement would impose. Second, OWCP's administrative burden will be lessened because it will not have to determine security deposit amounts for exempt carriers.

The Department has responded to the remaining comments in the following section-by-section discussion.

#### *C. Section-by-Section Explanation*

The Department received two comments addressing specific sections of the proposed rule. The following discussion responds to those comments and explains any changes the Department has made in the final rules. The Department received no comments concerning, and has made no changes to, proposed rule sections not discussed

here; these sections appear in the final rule as proposed.

20 CFR 701.301(a)(7)

(a) The Department proposed revising the definition of "District Director" by adding a sentence stating that "[a]ny action taken by a person under the authority of a district director will be considered the action of a deputy commissioner." 69 FR 12225 (March 15, 2004). The Department added this sentence to clarify that substitution of the title "district director" for "deputy commissioner" did not in any way alter OWCP staff members' authority to act.

(b) One comment states that this sentence should be removed in order to avoid any implication that OWCP claims examiners have the same scope of authority as district directors. The Department agrees with this comment and has deleted the last sentence from the final rule. The Department did not intend to change the scope of authority of either district directors or claims examiners. Deleting the last sentence removes any implication to the contrary.

20 CFR 703.201

(a) Section 703.201 provides a general overview of security deposits and their purpose. As proposed, it states, in part: "Security deposits secure the payment of benefits when an insurance carrier defaults on any of its obligations under the LHWCA, regardless of the date such obligations arose." 69 FR 12226 (March 15, 2004).

(b) One comment states that the phrase "obligations under the LHWCA" is unclear and should be revised. The Department agrees that this phrase in the proposed rule could be misconstrued. Accordingly, the Department has revised this section in the final rule by including specific language clarifying that the phrase "obligations under the LHWCA" means a carrier's liability for both compensation payments and medical benefits, and that such meaning applies to the entire subpart.

(c) The same comment states that the word "default" is unclear because it could include situations where a solvent insurer simply disputes a claim. The comment suggests that default be expressly limited to a carrier's failure "to timely pay a final judgment against the carrier for its obligation to pay benefits under the LHWCA and against which there is a right of execution."

In both legal and everyday parlance, the term "default" is commonly understood to mean a failure to meet a legal or contractual duty. *See, e.g., Black's Law Dictionary* (8th Ed. 2004); *The New Shorter Oxford English*

*Dictionary* (1993). Such duty does not arise simply because an employer or insurance carrier contests a claim. Instead, it arises when a valid compensation order is entered. Under the Longshore Act's comprehensive adjudication scheme, claims are initially considered by an OWCP district director. 33 U.S.C. 919(c); 20 CFR 702.311–.317. If the district director is unable to resolve all disputed issues to the parties' satisfaction, an administrative law judge holds a *de novo* hearing and issues a compensation order. 33 U.S.C. 919(d), (e); 20 CFR 702.301, 702.332. Once filed by the district director, the administrative law judge's order becomes effective and imposes a legal obligation on the employer or carrier to pay any compensation awarded, notwithstanding any appeal from the order. 33 U.S.C. 919(e), 921(a), 921(b)(3); 20 CFR 702.350. Failure to comply with this effective order within the statutory 10-day time period constitutes a default. 33 U.S.C. 914(f); 20 CFR 702.350.

To the extent this comment implies that OWCP should be allowed to use the posted security only when a carrier fails to satisfy a district court order enforcing an underlying compensation order (or, as put by the commenter, a "final judgment \* \* \* against which there is a right of execution") issued under section 18 of the statute, 33 U.S.C. 918, the Department rejects the comment. Requiring claimants or the Director to go to district court in every case in which a financially troubled carrier defaults runs counter to the primary purpose of the security deposit requirement: the uninterrupted and prompt payment of compensation and medical benefits when a carrier is no longer capable of paying. Accordingly, the Department has not changed this portion of the rule.

(d) The Department has also revised the third sentence of this regulation for stylistic and grammatical purposes. As proposed, this sentence stated that security deposits "also secure the payment of compensation and medical benefits when a carrier with LHWCA obligations becomes insolvent in States with no insurance guaranty funds, or with guaranty funds that do not fully secure such obligations." The final rule states more simply and clearly that security deposits "secure the payment of compensation and medical benefits when a carrier becomes insolvent and such obligations are not otherwise fully secured by a State guaranty fund."

20 CFR 703.202

(a) Section 703.202 discusses how the Department will determine gaps in State

guaranty fund coverage and how it will convey those determinations to the public. Specifically, the rule: (1) Outlines factors OWCP will consider in determining each State's guaranty fund coverage of Longshore obligations; (2) requires OWCP to post its findings on the agency's web site, where they will be open for public inspection and comment; (3) provides that OWCP will deem 33 % of a carrier's Longshore obligations unsecured if the amount of State fund coverage cannot be determined or is ambiguous; and (4) states that OWCP will revise its findings in response to substantiated public comments or for any other relevant reason. 69 FR 12226 (March 15, 2004).

(b) One comment suggests that OWCP should complete State fund reviews and receive public comments before calculating and requiring security deposits. The commenter states that this would give State legislators and regulators an opportunity to remedy any State guaranty fund coverage deficiencies OWCP identifies, thus implying that the need for certain security deposits would be eliminated.

While the Department agrees that public comment on OWCP's State guaranty fund evaluations will be helpful, it has not incorporated the commenter's proposal in the final rule. The procedure § 703.202 adopts is a dynamic one: OWCP will revisit its determinations regarding State guaranty fund coverage when public comment or other relevant information makes a re-determination useful. This can happen before, during, or after calculating deposits for insurers on an individual basis. At a minimum, though, OWCP will consider each insurer's comments prior to setting the required security deposit amount for that company. Section 703.203(b) explicitly gives each insurer who disagrees with OWCP's assessment of State fund coverage the opportunity to submit evidence and/or argument on the question with its security deposit application. Thus, although OWCP might make a security deposit determination before all public comments are received, it is unlikely that general public comments will be more enlightening than information offered by insurers with a direct financial stake in the determination.

Moreover, the regulation's dynamic process is designed to take into account actions States may take in response to OWCP's evaluation of their guaranty funds' coverage for Longshore claims. The legislative process is often protracted, outcomes are uncertain, and OWCP has no control over that process in any event. If and when a State alters its guaranty fund coverage, that

alteration will be considered in the security deposit calculation process.

20 CFR 703.203

(a) Section 703.203 requires carriers to apply annually for a security deposit determination and prescribes the information the application must include. In addition to reporting its outstanding Longshore Act liabilities, the subsection (a)(2) of the proposed rule required each carrier to include a statement either “[o]f the deposit amount it believes will fully secure its obligations” or “[t]hat it has sufficient assets or other means to fully secure its obligations.” 69 FR 12227 (March 15, 2004).

(b) One commenter states that the proposed rule does not clearly explain: (1) How an insurance carrier “fully secures” its obligations; (2) what factors a carrier should consider in suggesting a security deposit amount that will fully secure its liability; and (3) how a carrier determines whether it has sufficient assets to secure its obligations. The Department has reconsidered proposed subsection (a)(2) and determined that a carrier should not be required either to suggest a security deposit amount or to state that it has sufficient assets to fully secure its obligations. The statement the proposed rule describes is superfluous and unnecessary to the security deposit determination process set forth in the final rules. Accordingly, the Department has deleted these requirements. This change will make the application process simpler because the carrier need only supply very limited, clearly defined information: (1) A statement of its outstanding liabilities on a state-by-state basis; (2) other specific information OWCP requests; and (3) if the carrier wishes, evidence and/or argument regarding OWCP’s evaluation of relevant State guaranty funds. Moreover, given the changes the Department has made to § 703.204 (*see* discussion below), a carrier generally will not be asked to submit voluminous financial information because it will no longer be necessary.

(c) The final version of § 703.203 adds a new subsection (a)(1) to implement the Department’s decision to exempt the financially strongest carriers from the security deposit requirement. In order to obtain this exemption, a carrier must submit, as part of its annual application, documentation from three OWCP-designated private insurance rating organizations demonstrating the rating each service awarded the carrier for both the current year and the immediately preceding year. The carrier must receive the highest rating each service awards for both years in order to

qualify for the exemption. OWCP will make an exemption decision each year. Thus, an exempt carrier whose rating is downgraded by any one of the rating services the following year will be required to deposit security. The carrier may again qualify for an exemption, but only after it has demonstrated sustained superior financial performance by receiving the highest ratings from the three designated rating organizations for two consecutive years.

Currently, OWCP has designated A.M. Best, Standard & Poor’s, and Weiss Research as the three private rating services it will use. The rule does not name these rating services; instead, the rule requires OWCP to publish the services it selects by posting their names on the agency’s web site. This procedure will give OWCP the option of selecting different rating services from time to time without having to engage in a new rulemaking. A variety of factors may lead OWCP to change its selections. For instance, a selected service could change its name or corporate form, or even go out of business. By the same token, new rating services that prove to be reliable may enter the market. The procedure the rule adopts allows OWCP the flexibility to make changes as the agency deems necessary. Subsection (a)(2) of the final rule also clarifies that a carrier seeking an exemption based on its financial standing need not include a statement of its outstanding LHWCA liabilities with its application unless OWCP denies its exemption request.

20 CFR 703.204

(a) This section sets forth the process OWCP will follow in determining the security deposit amount for each carrier.

(b) Proposed § 703.204(b) lists a variety of factors, most financial in nature, that OWCP could evaluate and consider in making its determination. These factors include the carrier’s: (1) Financial strength; (2) insureds’ strength; (3) reinsurance protection; (4) surplus and recent settlements; (5) amount of business written through the National Reinsurance Pool; (6) deductibles secured by letters of credit; (7) reduced exposure; (8) increases in capitalization; (9) State guaranty fund coverage for its LHWCA obligations; and (10) expansion of business into States without guaranty fund coverage for Longshore obligations. 69 FR 12227 (March 15, 2004).

One comment states that evaluation of these factors requires highly technical expertise in both insurance company and general financial analysis. The factors encompass voluminous information that is often confidential and difficult, if not impossible, to

present in a meaningful way. The commenter contends that private insurance rating organizations are in a better position to conduct this analysis. In addition, the commenter notes that it is unclear whether OWCP intends to consider these factors as they pertain only to the carrier’s Longshore business or its business as a whole.

The Department agrees with this comment. Accordingly, it has made substantial revisions in the final rule. OWCP has insufficient resources to conduct a financial evaluation of each carrier that matches the breadth and depth of recognized private rating organizations’ evaluations. Moreover, a survey of private organizations’ rating methodology documents verifies that they consider many of the same financial factors listed in the proposed rule.

Thus, the Department agrees that it should rely on insurance rating organizations for a picture of each carrier’s financial health and has eliminated those factors already considered by the rating organizations from the list in § 703.204(b). There is one exception. The final rule retains consideration of the strength of a carrier’s insureds in the Longshore industry. Because a carrier’s insolvency does not absolve an employer of its own liabilities under the LHWCA, the size and financial strength of the employers a carrier insures is an important consideration in determining the special fund’s risk in the event the carrier becomes insolvent. If the employer is financially capable of meeting its LHWCA obligations, notwithstanding its carrier’s insolvency, the risk to the special fund is diminished. In some instances, the strength of a carrier’s insureds is also relevant to the amount of coverage a State guaranty fund affords. For example, some State guaranty funds will not pay any of an insolvent carrier’s obligations where the insured employer is insolvent as well; as a result, the special fund’s risk increases.

The final rule also adds a variety of Longshore-insurance-related factors that fall within OWCP’s particular expertise as administrator of the program. The Department drew two of these factors—a carrier’s longevity in the Longshore insurance market and Longshore claim-payment history—from the comments discussing criteria for exempting carriers from the security deposit requirements. While a reliable payment history of significant duration does not guarantee future performance, this information is nevertheless a helpful indicator for OWCP in setting the

security deposit amount for a particular carrier.

The Department has also deleted from § 703.204(b) language regarding the deposit amount suggested by the insurance carrier. See 69 FR 12227 (March 15, 2004). This language is no longer necessary in light of the Department's revisions to proposed § 703.203 explained above.

(c) Proposed § 703.204(c) provides that OWCP will require all carriers that write LHWCA insurance in States without complete guaranty fund coverage identified under § 703.202(b) to deposit security for their unsecured LHWCA obligations. For each carrier who writes more than an insignificant or incidental amount of LHWCA insurance, OWCP will fix a security deposit amount between 33⅓% and 100% of the carrier's outstanding LHWCA obligations in each State. 69 FR 12227 (March 15, 2004).

One comment states that § 703.204(c) is unclear. The commenter suggests that the rule be revised to clarify that: (1) OWCP will require a security deposit for only those obligations not covered by State guaranty funds; (2) the 33⅓% minimum deposit applies only to that portion of a carrier's Longshore obligations not covered by State guaranty funds; and (3) OWCP will consider the factors set forth in § 703.204(b) in making its security deposit determination. The commenter's first two points have merit. Accordingly, the Department has revised the final rule by breaking § 703.204(c) into three subparts. Subpart (1) implements the Department's decision to exempt from the security deposit requirements those carriers awarded the highest financial ratings for both the current rating year and the immediately preceding year from the three rating organizations selected by OWCP. Subpart (2) clarifies that carriers whose LHWCA obligations are fully secured by State guaranty funds will not be required to deposit security. Subpart (3) contains language similar to proposed § 703.204(c), but specifically qualifies the phrase "outstanding LHWCA obligations" by adding "not secured by a State guaranty fund." The Department does not believe any change to the proposed rule is necessary in response to the commenter's third point because § 703.204(b) makes clear that OWCP may consider the factors listed in that subsection in rendering a security deposit determination (*i.e.*, "The Branch may consider a number of factors in setting the security deposit amount, including. \* \* \* § 703.204(b).").

One comment asks whether a carrier must make a pledge or other assurance

that it will meet its payment obligations in addition to the security deposit if that deposit is less than 100% of its outstanding obligations. The Department does not believe an additional pledge or other guaranty is necessary. The statute already requires each carrier to meet its payment obligations, regardless of the amount of security a carrier deposits.

#### 20 CFR 703.205

(a) Section 703.205(a) requires each carrier to execute an Agreement and Undertaking containing terms set forth in the regulation. As proposed, these terms give OWCP authority to act upon any deposited security when "[t]he carrier fails to renew any deposited letter of credit or substitute acceptable securities in their place" or "[t]he carrier fails to renew any deposited negotiable securities at maturity or substitute acceptable securities in their place." 69 FR 12227 (March 15, 2004) (proposed § 703.205(a)(2)(ii), (iii)).

One comment suggests that proposed § 703.205(a)(2)(ii) be rewritten to clarify that a carrier may substitute a new letter of credit or a bond, in addition to negotiable securities, in lieu of renewing any deposited letter of credit. This comment has merit. As proposed, § 703.205(a)(2)(ii) could be read to foreclose a carrier's ability to use a new letter of credit or an indemnity bond to secure its obligations. Proposed § 703.205(a)(2)(iii) similarly could be read to preclude a carrier from substituting a letter of credit or an indemnity bond for matured securities. The Department does not wish to restrict a carrier's ability to shift among approved forms of security as the carrier deems necessary. Accordingly, the Department has revised both § 703.205(a)(2)(ii) and (iii) to make clear that a carrier may substitute approved forms of security for others that have reached maturity or expired. As set forth below, the Department has also revised several other regulations that contain the same language as proposed §§ 703.205(a)(2)(ii) and (iii).

(b) Proposed § 703.205(a)(2)(iii) requires that the carrier either renew matured negotiable securities or substitute acceptable securities in their place. 69 FR 12227 (March 15, 2004). One commenter contends this provision is unnecessary because the Treasury Department's regulations, which govern the conduct of the custodian of the deposited securities (*e.g.* the Federal Reserve Bank), prohibit release of the principal to the carrier unless OWCP consents or the carrier provides substitute securities. The commenter misconstrues this provision's point. The

rule requires that carriers authorize OWCP to take possession of their security deposits under certain conditions. Thus, unlike the Treasury Department's rule, which governs the custodian's conduct, § 703.205(a)(2)(iii) governs the carrier's obligations and OWCP's rights with respect to the deposited security. The regulation is therefore appropriate and necessary.

(c) The Department has also corrected a typographical error that appeared in the proposed rule. As proposed, § 703.205's introductory paragraph cross-referenced § 703.203 when referring to OWCP's decision fixing a carrier's required security deposit amount. 69 FR 12227 (March 15, 2004). The regulation governing OWCP's decision, however, is § 703.204. Accordingly, the final rule contains the correct cross-reference to § 703.204.

#### 20 CFR 703.207

(a) Proposed § 703.207 cross-references the Treasury Department's regulations to define the types of negotiable securities a carrier may post. The rule states that if a carrier elects to use negotiable securities, the carrier "shall deposit any negotiable securities acceptable as security for the deposit of public monies of the United States under regulations issued by the Secretary of the Treasury. (See 31 CFR part 225.)" 69 FR 12228 (March 15, 2004).

(b) One comment objects to this provision on the ground that the Treasury Department's regulations appear inapplicable. The commenter states that those regulations define "bond" as a written instrument that guarantees fulfillment of an obligation to the United States. From this premise, the commenter contends that because the statute does not place any financial obligations on the United States, the Treasury Department's rules are not applicable. The Department disagrees. As the statutorily designated administrator of the LHWCA invested with broad rulemaking authority, 33 U.S.C. 939(a), 944(a), the Secretary (and, thus, the United States) has a direct interest in ensuring that the statute's primary goal is met. That goal is the prompt and certain payment of compensation and medical benefits to injured workers and their families. Taking steps to safeguard the Longshore program's fiscal vitality by requiring insurers to deposit security furthers that goal. The Treasury Department rule referred to by the commenter does not lead to a different conclusion. That rule specifically pertains to obligations to the United States—the sort of obligation these rules impose on insurance

carriers—as opposed to obligations of the United States—those duties the United States owes to other entities. Obligations to the United States—the kind governed by this regulation—squarely fall within the Treasury Department’s rules. See 31 CFR 225.2 (“Bond means an executed written instrument, which guarantees the fulfillment of an obligation to the United States and sets forth the terms, conditions, and stipulations of the obligation.”)

To the extent this comment relates to the Department’s authority to require carriers to post security deposits, the Department has responded fully in the Statutory Authority discussion above. Accordingly, the Department rejects this comment and has made no changes in the final rule.

#### 20 CFR 703.208

(a) This section provides that a carrier who chooses to secure its Longshore obligations with negotiable securities must deposit the securities with a Federal Reserve bank or the Treasurer of the United States. As proposed, this rule also sets forth OWCP’s discretionary authority to authorize the securities’ custodian to pay interest accrued on the deposited securities to the carrier. 69 FR 12228 (March 15, 2004).

(b) One comment states that the rule should be revised to require OWCP to direct interest payments to the carrier unless the carrier has defaulted on its Longshore obligations. OWCP currently directs the Federal Reserve bank to pay accrued interest on deposited negotiable securities to the carrier absent other specific instructions. OWCP does not plan to depart from its current practice under the new rules. The Department has therefore revised § 703.208 to reflect that interest accruing on deposited negotiable securities will be paid to the carrier unless any of the conditions set forth in § 703.211(a) occur (*i.e.* the conditions that allow OWCP to seize a carrier’s security deposit and/or use its proceeds).

#### 20 CFR 703.209

(a) Proposed § 703.209 proscribes substitution of “an indemnity bond, letters of credit or negotiable securities deposited by an insurance carrier under the regulations in this part” without OWCP authorization. This regulation also explains how carriers may apply to withdraw their security deposits when they have ceased writing Longshore insurance. 69 FR 12228 (March 15, 2004).

(b) One comment suggests that for carriers who secure their obligations with negotiable securities, the

Department should include in the rule a list of acceptable securities that a carrier could substitute without OWCP’s consent. The commenter notes that this would reduce the administrative burden on OWCP and carriers alike.

The Department agrees in principal with this comment. Section 703.207 limits the types of negotiable securities a carrier may use to those approved by the Treasury Department. Because the approved list of securities and their valuations change over time, the Treasury Department has eliminated from its regulations all mention of acceptable classes of securities. It has opted instead to put this information in other documents (*e.g.* Treasury Department circulars) and to post it on the Treasury Department’s Web site. Thus, it would not be advisable for the Department to promulgate a rule containing a list of acceptable substitute securities.

Nevertheless, the Treasury Department’s regulations governing the conduct of the custodian (*e.g.* a Federal Reserve Bank holding the carrier’s deposited securities) allow the custodian to release proceeds from matured securities to the depositor without specific instructions from the agency, but only if the depositor substitutes Treasury Department-approved securities in their place. 31 CFR 225.7(c). Because the custodian will allow substitution only with approved negotiable securities, a carrier need not seek the Department’s approval in those circumstances. To implement this change in the final rule, the Department has: (1) Limited § 703.209(a) to requirements regarding substitution of security; (2) added language to § 703.209(a) to allow different treatment for substitution of negotiable securities; (3) moved language regarding withdrawal of security from proposed § 703.209(a) to § 703.209(b); and (4) renumbered proposed § 703.209(b) as § 703.209(c).

#### 20 CFR 703.211

For the reasons set forth in paragraph (a) of the discussion of comments received regarding § 703.205(a)(2)(ii) and (iii), the Department has revised §§ 703.211(a)(2) and (3) in the same manner.

#### 20 CFR 703.301

(a) Section 703.301 discusses the Department’s authority to authorize employers to self-insure. As proposed, the rule allows the Department to authorize any employer who furnishes “satisfactory proof of its ability to pay compensation directly, and who agrees to immediately cancel any existing

insurance policy when OWCP approves the employer’s application to be self-insured.”

(b) Although the Department received no comments on this section, the Department realized in finalizing the rule that the phrase “immediately cancel any existing insurance policy” could be construed more broadly than intended. For instance, the phrase could be read as requiring an employer to cancel any excess or catastrophic insurance it may have to cover its Longshore obligations, a reading that would be contrary to other regulations authorizing the Department to require a self-insurer to carry catastrophic coverage. See, *e.g.*, § 703.304(a)(6). To avoid confusion, the Department has added language to § 703.301 clarifying that an approved self-insurer must agree to cancel existing insurance policies covering its Longshore obligations but may continue to carry excess or catastrophic coverage it chooses (or is required by the Department) to purchase.

#### 20 CFR 703.304

For the reasons set forth in paragraph (a) of the discussion of comments received regarding § 703.205(a)(2)(ii) and (iii), the Department has revised § 703.304(a)(4)(ii) and (iii) in the same manner. The Department has also added a comma after the phrase “in a form prescribed and provided by OWCP” in § 703.304(a) for grammatical purposes.

#### 20 CFR 703.307

For the reasons set forth in the discussion of comments received regarding § 703.208, the Department has revised § 703.307 in the same manner.

#### 20 CFR 703.308

For the reasons set forth in the discussion of comments received regarding § 703.209, the Department has revised § 703.308 in the same manner.

#### 20 CFR 703.310

For the reasons set forth in paragraph (a) of the discussion of comments received regarding § 703.205(a)(2)(ii) and (iii), the Department has revised §§ 703.310(a)(2) and (3) in the same manner.

### III. Executive Order 12866 (Regulatory Planning and Review)

The Office of Management and Budget (OMB) has determined that this rule is a “significant regulatory action” under section 3(f)(4) of Executive Order 12866. Under that section, a “significant regulatory action” includes one that “raise[s] novel legal or policy issues arising out of legal mandates, the President’s priorities, or the principles



set forth in this Executive order.” Accordingly, OMB has reviewed this rule.

In adopting this final rule, the Department considered several alternatives set forth in the NPRM. 69 FR 12219 (March 15, 2004). The Department considered requiring all carriers to fully secure their LHWCA obligations. This approach would place the risk of insolvency on the failed insurer rather than the surviving, healthy members of the insurance industry and self-insured employers through special fund assessments. 33 U.S.C. 944(c)(2). The Department rejected this approach, however, because it might lead some insurance carriers to leave the market and would duplicate, at least to some extent, the reserve requirements imposed by State insurance regulators.

Another alternative the Department considered but rejected was to use the existing special fund as an overall guaranty fund for all LHWCA claims. Although easy to administer, this approach would likely create negative incentives for prudent fiscal responsibility in the insurance industry.

Thus, the Department proposed a third approach in the NPRM. The proposed rules required all authorized insurance carriers to post security deposits, but only where there was no adequate State guaranty fund and only in amounts that reflected the actual risk of loss to the special fund. 69 FR 12226–12228 (March 15, 2004). As discussed in detail above, the Department has adopted this approach in the final rule, with the addition of an exemption from the security deposit requirements for the financially strongest carriers.

The benefits of this rule are numerous. First, security deposits will ensure that the Longshore Act’s primary purpose—the prompt payment of compensation and medical benefits to injured workers and their survivors—is fulfilled, notwithstanding an insurance carrier’s insolvency.

Second, security deposits protect both healthy members of the insurance industry and the special fund. The special fund’s costs, which are calculated and assessed against authorized Longshore insurance carriers and self-insured employers each year, are primarily incurred for compensation payments in two circumstances: (1) When a carrier (and the employer it insured) or a self-insurer is insolvent; and (2) when a carrier or employer is entitled to relief under 33 U.S.C. 908(f) (second-injury fund). Security deposits will avoid draining the special fund’s available resources in the event a carrier becomes insolvent. Moreover, as many

industry members recognized in responding to the Department’s request for information published in the **Federal Register** on February 22, 2002 (67 FR 8450), requiring authorized carriers to fully secure their LHWCA obligations obviates the need to collect annual special fund assessments from healthy carriers to pay for the insolvency of weaker carriers. See 69 FR 12219 (March 15, 2004). Because the requirement that liabilities be fully secured should decrease the fund’s costs for benefits paid on behalf of insolvent carriers, the special fund assessments levied against carriers and self-insured employers are expected to decrease commensurately.

Third, security deposits protect the special fund from the unpredictable future, including the inherent inability of any static rating scheme to accurately predict the future financial stability of an insurance carrier, and the potential for catastrophic losses beyond the carrier’s control (e.g. natural disasters, acts of terrorism) in the shipping and shipbuilding industries. See 69 FR 12219 (March 15, 2004).

By providing three methods for meeting the security deposit requirements, the final rules allow carriers to manage the direct costs associated with posting security by choosing an appropriate financial instrument. A carrier who deposits negotiable securities, for instance, continues to own the negotiable securities (subject to OWCP’s security interest) and receive the income generated by them. See § 703.208. The majority of carriers have chosen this method for securing their LHWCA obligations under OWCP’s current policy. A carrier may also elect to purchase an indemnity bond or letter of credit to meet its security deposit obligation. As noted in the NPRM, the Department estimates a \$400,000 bond would require only a small initial cash outlay of approximately \$6,000–\$8,000 at typical current rates. See 69 FR 12223 (March 15, 2004).

In sum, the final rule balances the interests of insurance carriers, Longshore Act claimants, and the Department. The rule exempts from the deposit requirements those insurance carriers with the highest financial ratings who demonstrate solid financial strength, and limits the number of remaining carriers who must post deposits to those carriers operating in States with inadequate guaranty funds. At the same time, the rule meets the Department’s objectives of protecting the special fund from insurance carrier insolvency and ensuring the prompt and

continued payment of compensation and medical benefits to injured workers.

#### **IV. Information Collection Requirements (Subject to the Paperwork Reduction Act)**

As explained in the NPRM, the Department submitted several new collections of information contained in the proposed rules to the Office of Management and Budget (OMB) for review in accordance with the Paperwork Reduction Act of 1995, 44 U.S.C. 3501 *et seq.*, and its implementing regulations at 5 CFR part 1320. 69 FR 12221–22 (March 15, 2004). The new information collection requirements are found in §§ 703.2, 703.203, 703.204, 703.205, 703.209, 703.210, 703.212, 703.303 and 703.304.

With the exception of §§ 703.303 and 703.304, these collections relate to information insurance carriers are required to submit as part of the authorization process for writing LHWCA insurance, and as part of the process by which OWCP decides both the extent of an authorized insurance carrier’s unsecured LHWCA obligations and the amount of the required security deposit. To implement these new collections, the Department proposed creating two new forms for insurance carriers (LS–276 and LS–275 IC). 69 FR 12221 (March 15, 2004). The information collections established in §§ 703.303 and 703.304 relate to the security a self-insured employer deposits to secure its payment of compensation under the LHWCA and its extensions. To implement these collections, the Department proposed one new form for self-insurers (Form LS–275 SI). 69 FR 12221 (March 15, 2004).

*Burden estimates.* (1) Form LS–276, Application for Security Deposit Determination. As fully explained in the NPRM, approximately 385 insurance carriers annually will file Form LS–276. The Department estimates that on average, it will take a carrier one hour to collect the information, complete Form LS–276 and mail it. Thus, the total annual hour burden is estimated to be 385 hours. The Department also estimates respondents’ total annual operating and maintenance (printing and mailing) costs to be \$163.80. 69 FR 12221 (March 15, 2004).

(2) LS–275 IC, Agreement and Undertaking (Insurance Carrier); LS–276 SI, Agreement and Undertaking (Self-Insured Employer). As fully explained in the NPRM, the Department estimates that approximately 343 (or 50%) of all authorized insurance carriers and self-insurers annually will complete and file Form LS–275 IC or LS–275 SI. The



Department estimates that on average, it will take a respondent 15 minutes to locate the information, complete form LS-275 IC or LS-275 SI and mail it. Thus, the total annual hour burden is estimated to be 85.75 hours. The Department also estimates respondents' total annual operating and maintenance (printing and mailing) costs to be \$145.60. 69 FR 12222 (March 15, 2004).

The Department invited public comment on the new information collection requirements. 69 FR 12218, 12221 (March 15, 2004). No comments were received. OMB subsequently approved the use of the three new forms under OMB No. 1215-0204 until June 30, 2007, provided that the Department reports on the viability of developing criteria to exempt financially secure carriers from making a security deposit when it renews these collections of information in 2007.

Changes made between the proposed and final rules in response to public comment require a minor revision to Form LS-276, Application for Security Deposit Determination. Under the final rules, any carrier seeking an exemption from the security deposit requirements must submit documentation establishing its current rating and its rating for the immediately preceding year from each of three private insurance rating services designated by the Department. The Department intends to revise Form LS-276 to: (1) Allow a carrier to indicate that it is seeking an exemption; and (2) notify the carrier that it must submit the required ratings from private insurance rating services with its application. The Department believes this new reporting requirement will result in only de minimus increases in the cost and time burdens estimated for completing Form LS-276 that the Department set forth in the NPRM's preamble. 69 FR 12221 (March 15, 2004).

#### V. Regulatory Flexibility Act and Executive Order 13272 (Proper Consideration of Small Entities in Agency Rulemaking)

The Regulatory Flexibility Act of 1980, as amended (5 U.S.C. 601 *et seq.*), requires an agency to prepare regulatory flexibility analyses when it proposes regulations that will have "a significant economic impact on a substantial number of small entities," or to certify that the proposed regulations will have no such impact, and to make the analyses or certification available for public comment. For the reasons set forth in the NPRM, the Department determined that a complete regulatory flexibility analysis was not necessary, and certified that the proposed rules

would not have a significant economic impact on a substantial number of small entities. 69 FR 12222-23. The Department invited public comment on the certification and delivered a copy of the NPRM to the Chief Counsel for Advocacy of the Small Business Administration.

The Department has received no comments responding to the certification or its underlying factual basis. Accordingly, for the reasons stated in the NPRM, the Assistant Secretary of Labor for Employment Standards again certifies that this rule will not have a significant economic impact on a substantial number of small entities. As a result, no regulatory impact analysis is required.

#### List of Subjects

##### 20 CFR Part 701

Longshore and harbor workers, Organization and functions (government agencies), Workers' compensation.

##### 20 CFR Part 703

Bonds, Insurance companies, Longshore and harbor workers, Reporting and recordkeeping requirements, Securities, Workers' compensation.

■ For the reasons set forth in the preamble, title 20, Chapter VI, Subchapter A of the Code of Federal Regulations is amended to read as follows:

#### PART 701—GENERAL PROVISIONS, DEFINITIONS AND USE OF TERMS

■ 1. The authority citation for Part 701 is revised to read as follows: Authority: 5 U.S.C. 301 and 8171 *et seq.*; 33 U.S.C. 939; 36 D.C. Code 501 *et seq.*; 42 U.S.C. 1651 *et seq.*; 43 U.S.C. 1331; Reorganization Plan No. 6 of 1950, 15 FR 3174, 3 CFR, 1949-1953 Comp., p. 1004, 64 Stat. 1263.

■ 2. Revise § 701.101 to read as follows:

##### § 701.101 Scope of this subchapter and subchapter B.

(a) This subchapter contains the regulations governing the administration of the Longshore and Harbor Workers' Compensation Act, as amended (LHWCA), 33 U.S.C. 901 *et seq.*, except activities, pursuant to 33 U.S.C. 941, assigned to the Assistant Secretary of Labor for Occupational Safety and Health. It also contains the regulations governing the administration of the direct extensions of the LHWCA: the Defense Base Act (DBA), 42 U.S.C. 1651 *et seq.*; the Outer Continental Shelf Lands Act (OCSLA), 43 U.S.C. 1331; and the Nonappropriated Fund

Instrumentalities Act (NFIA), 5 U.S.C. 8171 *et seq.*

(b) The regulations in this subchapter also apply to claims filed under the District of Columbia Workmen's Compensation Act (DCCA), 36 D.C. Code 501 *et seq.* That law applies to all claims for injuries or deaths based on employment events that occurred prior to July 26, 1982, the effective date of the District of Columbia Workers' Compensation Act, as amended (D.C. Code 32-1501 *et seq.*).

(c) The regulations governing the administration of the Black Lung Benefits Program are in subchapter B of this chapter.

■ 3. Revise § 701.102 to read as follows:

##### § 701.102 Organization of this subchapter.

Part 701 provides a general description of the regulations in this subchapter; sets forth information regarding the persons and agencies within the Department of Labor authorized by the Secretary of Labor to administer the Longshore and Harbor Workers' Compensation Act, its extensions and the regulations in this subchapter; and defines and clarifies use of specific terms in the several parts of this subchapter. Part 702 of this subchapter contains the general administrative regulations governing claims filed under the LHWCA. Part 703 of this subchapter contains the regulations governing insurance carrier authorizations, insurance carrier security deposits, self-insurer authorizations, and certificates of compliance with the insurance regulations, as required by sections 32 and 37 of the LHWCA (33 U.S.C. 932, 937). Because the extensions of the LHWCA (*see* § 701.101) incorporate by reference nearly all the provisions of the LHWCA, the regulations in parts 701, 702 and 703 also apply to the administration of the extensions (DBA, DCCA, OCSLA, and NFIA), unless otherwise noted. Part 704 of this subchapter contains the exceptions to the general applicability of parts 702 and 703 for the DBA, the DCCA, the OCSLA, and the NFIA.

■ 4. Revise § 701.201 to read as follows:

##### § 701.201 Office of Workers' Compensation Programs.

The Office of Workers' Compensation Programs (OWCP) is responsible for administering the LHWCA and its extensions (*see* 20 CFR 1.2(e)). The regulations in subchapter A of chapter I of this title (20 CFR part 1) describe OWCP's establishment within the Employment Standards Administration, the functions assigned to it by the Assistant Secretary of Labor for

Employment Standards, and how those functions were performed before OWCP's establishment.

**§ 701.202 [Reserved]**

**§ 701.203 [Reserved]**

■ 5. Remove and reserve §§ 701.202 and 701.203.

■ 6. Amend § 701.301 by revising paragraphs (a)(1), (a)(5), (a)(6), (a)(7), (a)(8), (a)(9), (a)(10), (a)(12)(i)(B), (a)(12)(ii)(A) and (a)(12)(iii)(E) to read as follows:

**§ 701.301 Definitions and use of terms.**

(a) \* \* \*  
 (1) *Act* or *LHWCA* means the Longshore and Harbor Workers' Compensation Act, as amended (33 U.S.C. 901 *et seq.*), and includes the provisions of any statutory extension of such Act (*see* § 701.101(a) and (b)) pursuant to which compensation on account of an injury is sought.

(5) *Office of Workers' Compensation Programs* or *OWCP* or *the Office* means the Office of Workers' Compensation Programs within the Employment Standards Administration, referred to in § 701.201 and described more fully in part 1 of this title. The term *Office of Workmen's Compensation Programs* shall have the same meaning as *Office of Workers' Compensation Programs* (*see* 20 CFR 1.6(b)).

(6) *Director* means the Director of OWCP, or his or her authorized representative.

(7) *District Director* means a person appointed as provided in sections 39 and 40 of the LHWCA or his or her designee, authorized to perform functions with respect to the processing and determination of claims for compensation under the LHWCA and its extensions as provided therein and under this subchapter. The term District Director is substituted for the term *Deputy Commissioner* used in the statute. This substitution is for administrative purposes only and in no way affects the power or authority of the position as established in the statute.

(8) *Administrative Law Judge* means a person appointed as provided in 5 U.S.C. 3105 and subpart B of 5 CFR part 930, who is qualified to preside at hearings under 5 U.S.C. 557 and is empowered by the Secretary to conduct formal hearings whenever necessary in respect of any claim for compensation arising under the LHWCA and its extensions.

(9) *Chief Administrative Law Judge* means the Chief Judge of the Office of Administrative Law Judges, United States Department of Labor, whose

office is at the location set forth in 29 CFR 18.3(a).

(10) *Board or Benefits Review Board* means the Benefits Review Board established by section 21 of the LHWCA (33 U.S.C. 921) as amended and constituted and functioning pursuant to the provisions of chapter VII of this title and Secretary of Labor's Order No. 38-72 (38 FR 90), whose office is at the location set forth in 20 CFR 802.204.

\* \* \* \* \*

(12) \* \* \*

(i) \* \* \*

(B) Any harbor worker, including a ship repairer, shipbuilder and shipbreaker; and

\* \* \* \* \*

(ii) \* \* \*

(A) A master or member of a crew of any vessel; or

\* \* \* \* \*

(iii) \* \* \*

(E) Aquaculture workers, meaning those employed by commercial enterprises involved in the controlled cultivation and harvest of aquatic plants and animals, including the cleaning, processing or canning of fish and fish products, the cultivation and harvesting of shellfish, and the controlled growing and harvesting of other aquatic species; or

\* \* \* \* \*

**PART 703—INSURANCE REGULATIONS**

■ 7. The authority citation for Part 703 is revised to read as follows:

**Authority:** 5 U.S.C. 301 and 8171 *et seq.*; 31 U.S.C. 9701; 33 U.S.C. 932 and 939; 36 D.C. Code 501 *et seq.*; 42 U.S.C. 1651 *et seq.*; 43 U.S.C. 1331; Reorganization Plan No. 6 of 1950, 15 FR 3174, 3 CFR, 1949-1953 Comp., p. 1004, 64 Stat. 1263; Secretary's Order 4-2001, 66 FR 29656.

■ 8. Amend Part 703 by redesignating §§ 703.001 through 703.003 as §§ 703.1 through 703.3 and designating them as new "Subpart A—General," by designating center heading "Authorization of Insurance Carriers" as "Subpart B—Authorization of Insurance Carriers," and revising newly designated subpart A to read as follows:

**Subpart A—General**

- Sec.
- 703.1 Scope of part.
- 703.2 Forms.
- 703.3 Failure to secure coverage; penalties.

**Subpart B—Authorization of Insurance Carriers**

\* \* \* \* \*

**Subpart A—General**

**§ 703.1 Scope of part.**

Part 703 governs insurance carrier authorizations, insurance carrier security deposits, self-insurer authorizations, and certificates of compliance with the insurance regulations. These provisions are required by the LHWCA and apply to the extensions of the LHWCA except as otherwise provided in part 704 of this subchapter.

**§ 703.2 Forms.**

(a) Any information required by the regulations in this part to be submitted to OWCP must be submitted on forms the Director authorizes from time to time for such purpose. Persons submitting forms may not modify the forms or use substitute forms without OWCP's approval.

Form No.	Title
(1) LS-271 ...	Application for Self-Insurance.
(2) LS-274 ...	Report of Injury Experience.
(3) LS-275 SI	Self-Insurer's Agreement and Undertaking.
(4) LS-275 IC	Insurance Carrier's Agreement and Undertaking.
(5) LS-276 ...	Application for Security Deposit Determination.
(6) LS-405 ...	Indemnity Bond.
(7) LS-570 ...	Card Report of Insurance.

(b) Copies of the forms listed in this section are available for public inspection at the Office of Workers' Compensation Programs, Employment Standards Administration, U.S. Department of Labor, Washington, D.C. 20210. They may also be obtained from OWCP district offices and on the Internet at <http://www.dol.gov/esa/owcp/dlhwcp/liforms.htm>.

**§ 703.3 Failure to secure coverage; penalties.**

(a) Each employer must secure the payment of compensation under the Act either through an authorized insurance carrier or by becoming an authorized self-insurer under section 32(a)(1) or (2) of the Act (33 U.S.C. 932(a)(1) or (2)). An employer who fails to comply with these provisions is subject, upon conviction, to a fine of not more than \$10,000, or by imprisonment for not more than one year, or both. Where the employer is a corporation, the president, secretary and treasurer each will also be subject to this fine and/or imprisonment, in addition to the fine against the corporation, and each is severally personally liable, jointly with the corporation, for all compensation or other benefits payable under the Act while the corporation fails to secure the payment of compensation.

(b) Any employer who willingly and knowingly transfers, sells, encumbers, assigns or in any manner disposes of, conceals, secretes, or destroys any property belonging to the employer after an employee sustains an injury covered by the Act, with the intent to avoid payment of compensation under the Act to that employee or his/her dependents, shall be guilty of a misdemeanor and punished, upon conviction, by a fine of not more than \$10,000 and/or imprisonment for one year. Where the employer is a corporation, the president, secretary and treasurer are also severally liable to imprisonment and, along with the corporation, jointly liable for the fine.

■ 9. Amend Part 703 by adding new "Subpart C—Insurance Carrier Security Deposit Requirements" (consisting of §§ 703.201 through 703.213), designating the center heading "Authorization of Self-Insurers" as "Subpart D—Authorization of Self-Insurers," designating center heading "Issuance of Certificates of Compliance," as "Subpart E—Issuance of Certificates of Compliance," and revising new Subpart D.

The addition and revision read as follows:

**Subpart C—Insurance Carrier Security Deposit Requirements**

Sec.

- 703.201 Deposits of security by insurance carriers.
- 703.202 Identification of significant gaps in State guaranty fund coverage for LHWCA obligations.
- 703.203 Application for security deposit determination; information to be submitted; other requirements.
- 703.204 Decision on insurance carrier's application; minimum amount of deposit.
- 703.205 Filing of Agreement and Undertaking; deposit of security.
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**Subpart E—Issuance of Certificates of Compliance**

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**Subpart C—Insurance Carrier Security Deposit Requirements**

**§ 703.201 Deposits of security by insurance carriers.**

The regulations in this subpart require certain insurance carriers to deposit security in the form of indemnity bonds, letters of credit or negotiable securities (chosen at the option of the carrier) of a kind and in an amount determined by the Office, and prescribe the conditions under which deposits must be made. Security deposits secure the payment of compensation and medical benefits when an insurance carrier defaults on any of its obligations under the LHWCA, regardless of the date such obligations arose. They also secure the payment of compensation and medical benefits when a carrier becomes insolvent and such obligations are not otherwise fully secured by a State guaranty fund. Any gap in State guaranty fund coverage will have a direct effect on the amount of security the Office will require a carrier to post. As used in this subpart, the terms "obligations under the Act" and "LHWCA obligations" mean a carrier's liability for compensation payments and medical benefits arising under the Longshore and Harbor Workers' Compensation Act and any of its extensions.

**§ 703.202 Identification of significant gaps in State guaranty fund coverage for LHWCA obligations.**

(a) In determining the amount of a carrier's required security deposit, the Office will consider the extent to which a State guaranty fund secures the insurance carrier's LHWCA obligations in that State. When evaluating State guaranty funds, the Office may consider a number of factors including, but not limited to—

- (1) Limits on weekly benefit amounts;
- (2) Limits on aggregate maximum benefit amounts;
- (3) Time limits on coverage;
- (4) Ocean marine exclusions;
- (5) Employer size and viability provisions; and
- (6) Financial strength of the State guaranty fund itself.

(b) OWCP will identify States without guaranty funds and States with guaranty funds that do not fully and immediately secure LHWCA obligations and will post its findings on the Internet at <http://www.dol.gov/esa/owcp/dlhwc/lstable.htm>. These findings will indicate the extent of any partial or total gap in coverage provided by a State guaranty fund, and they will be open for inspection and comment by all interested parties. If the extent of coverage a particular State guaranty fund provides either cannot be determined or is ambiguous, OWCP will deem one third (33 1/3 percent) of a carrier's LHWCA obligations in that State to be unsecured. OWCP will revise its findings from time to time, in response to substantiated public comments it receives or for any other reasons it considers relevant.

**§ 703.203 Application for security deposit determination; information to be submitted; other requirements.**

(a) Each insurance carrier authorized by OWCP to write insurance under the LHWCA or any of its extensions, and each insurance carrier seeking initial authorization to write such insurance, must apply annually, on a schedule set by OWCP, for a determination of the extent of its unsecured obligations and the security deposit required. The application must be addressed to the Branch of Financial Management and Insurance (Branch) within OWCP's Division of Longshore and Harbor Workers' Compensation, and be made on a form provided by OWCP. The application must contain the following:

- (1) Any carrier seeking an exemption from the security deposit requirements based on its financial standing (*see* § 703.204(c)(1)) must submit documentation establishing the carrier's current rating and its rating for the

immediately preceding year from each insurance rating service designated by the Branch and posted on the Internet at <http://www.dol.gov/esa/owcp/dlhwc/lstable.htm>.

(2) All other carriers, and any carrier whose exemption request under paragraph (a)(1) of this section has been denied, must provide—

(i) A statement of the carrier's outstanding liabilities under the LHWCA or any of its extensions for its LHWCA obligations for each State in which the obligations arise; and

(ii) Any other information the Branch requests to enable it to give the application adequate consideration including, but not limited to, the reports set forth at § 703.212.

(b) If the carrier disagrees with any of OWCP's findings regarding State guaranty funds made under § 703.202(b) as they exist when it submits its application, the carrier may submit a statement of its unsecured obligations based on a different conclusion regarding the extent of coverage afforded by one or more State guaranty funds. The carrier must submit evidence and/or argument with its application sufficient to establish that such conclusion is correct.

(c) The carrier must sign and swear to the application. If the carrier is not an individual, the carrier's duly authorized officer must sign and swear to the application and list his or her official designation. If the carrier is a corporation, the officer must also affix the corporate seal.

(d) At any time after filing an application, the carrier must inform the Branch immediately of any material changes that may have rendered its application incomplete, inaccurate or misleading.

(e) By filing an application, the carrier consents to be bound by and to comply with the regulations and requirements in this part.

**§ 703.204 Decision on insurance carrier's application; minimum amount of deposit.**

(a) The Branch will issue a decision on the application determining the extent of an insurance carrier's unsecured LHWCA obligations and fixing the amount of security the carrier must deposit to fully secure payment of its unsecured obligations. The Branch will transmit its decision to the applicant in a way it considers appropriate.

(b) The Branch may consider a number of factors in setting the security deposit amount including, but not limited to, the—

(1) Financial strength of the carrier as determined by private insurance rating organizations;

(2) Financial strength of the carrier's insureds in the Longshore industry;

(3) Extent to which State guaranty funds secure the carrier's LHWCA obligations in the event the carrier defaults on its obligations or becomes insolvent;

(4) Carrier's longevity in writing LHWCA or other workers' compensation coverage;

(5) Extent of carrier's exposure for LHWCA coverage; and

(6) Carrier's payment history in satisfying its LHWCA obligations.

(c) In setting the security deposit amount, the Branch will follow these criteria:

(1) Carriers who hold the highest rating awarded by each of the three insurance rating services designated by the Branch and posted on the Internet at <http://www.dol.gov/esa/owcp/dlhwc/lstable.htm> for both the current rating year and the immediately preceding year will not be required to deposit security.

(2) Carriers whose LHWCA obligations are fully secured by one or more State guaranty funds, as evaluated by OWCP under § 703.202 of this subpart, will not be required to deposit security.

(3) The Branch will require all carriers not meeting the requirements of paragraphs (c)(1) or (2) of this section to deposit security for their LHWCA obligations not secured by a State guaranty fund, as evaluated by OWCP under § 703.202 of this subpart. For carriers that write only an insignificant or incidental amount of LHWCA insurance, the Branch will require a deposit in an amount determined by the Branch from time to time. For all other carriers, the Branch will require a minimum deposit of one third (33 $\frac{1}{3}$  percent) of a carrier's outstanding LHWCA obligations not secured by a State guaranty fund, but may require a deposit up to an amount equal to the carrier's total outstanding LHWCA obligations (100 percent) not secured by a State guaranty fund.

(d) If a carrier believes that a lesser deposit would fully secure its LHWCA obligations, the carrier may request a hearing before the Director of the Division of Longshore and Harbor Workers' Compensation (Longshore Director) or the Longshore Director's representative. Requests for hearing must be in writing and sent to the Branch within 10 days of the date of the Branch's decision. The carrier may submit new evidence and/or argument in support of its challenge to the

Branch's decision and must provide any additional documentation OWCP requests. The Longshore Director or his representative will notify the carrier of the hearing date within 10 days of receiving the request. The Longshore Director or his representative will issue the final agency decision on the application within 60 days of the hearing date, or, where evidence is submitted after the hearing, within 60 days of the receipt of such evidence, but no later than 180 days after receiving the carrier's request for a hearing.

**§ 703.205 Filing of Agreement and Undertaking; deposit of security.**

Within 45 days of the date on which the insurance carrier receives the Branch's decision (or, if the carrier requests a hearing, a period set by the Longshore Director or the Longshore Director's representative) determining the extent of its unsecured LHWCA obligations and fixing the required security deposit amount (*see* § 703.204), the carrier must:

(a) Execute and file with the Branch an Agreement and Undertaking, in a form prescribed and provided by OWCP, in which the carrier shall agree to—

(1) Deposit with the Branch indemnity bonds or letters of credit in the amount fixed by the Office, or deposit negotiable securities under §§ 703.207 and 703.208 in that amount;

(2) Authorize the Branch, at its discretion, to bring suit under any deposited indemnity bond or to draw upon any deposited letters of credit, as appropriate under the terms of the security instrument, or to collect the interest and principal as they become due on any deposited negotiable securities and to sell or otherwise liquidate such negotiable securities or any part thereof when—

(i) The carrier defaults on any of its LHWCA obligations;

(ii) The carrier fails to renew any deposited letter of credit or substitute a new letter of credit, indemnity bond or acceptable negotiable securities in its place;

(iii) The carrier fails to renew any deposited negotiable securities at maturity or substitute a letter of credit, indemnity bond or acceptable negotiable securities in their place;

(iv) State insolvency proceedings are initiated against the carrier; or

(v) The carrier fails to comply with any of the terms of the Agreement and Undertaking; and

(3) Authorize the Branch, at its discretion, to pay such ongoing claims of the carrier as it may find to be due

and payable from the proceeds of the deposited security;

(b) Give security in the amount fixed in the Office's decision:

(1) In the form of an indemnity bond with sureties satisfactory to the Branch and in such form, and containing such provisions, as the Branch may prescribe: *Provided*, That only surety companies approved by the United States Treasury Department under the laws of the United States and the rules and regulations governing bonding companies may act as sureties on such indemnity bonds (*see* Department of Treasury's Circular-570), and that a surety company that is a corporate subsidiary of an insurance carrier may not act as surety on such carrier's indemnity bond;

(2) In the form of letters of credit issued by a financial institution satisfactory to the Branch and upon which the Branch may draw; or

(3) By a deposit of negotiable securities with a Federal Reserve Bank or the Treasurer of the United States in compliance with §§ 703.207 and 703.208.

**§ 703.206 [Reserved]**

**§ 703.207 Kinds of negotiable securities that may be deposited; conditions of deposit; acceptance of deposits.**

An insurance carrier electing to deposit negotiable securities to secure its obligations under the Act in the amount fixed by the Office under the regulations in this part shall deposit any negotiable securities acceptable as security for the deposit of public monies of the United States under regulations issued by the Secretary of the Treasury. (*See* 31 CFR part 225.) The approval, valuation, acceptance, and custody of such securities is hereby committed to the several Federal Reserve Banks and the Treasurer of the United States.

**§ 703.208 Deposits of negotiable securities with Federal Reserve banks or the Treasurer of the United States; interest thereon.**

Deposits of negotiable securities provided for by the regulations in this part must be made with any Federal Reserve bank or any branch of a Federal Reserve bank designated by the Branch, or the Treasurer of the United States, and must be held subject to the order of the Branch. The Branch will authorize the insurance carrier to collect interest on the securities it deposits unless any of the conditions set forth at § 703.211(a) occur.

**§ 703.209 Substitution and withdrawal of indemnity bond, letters of credit or negotiable securities.**

(a) A carrier may not substitute other security for any indemnity bond or letters of credit deposited under the regulations in this part except when authorized by the Branch. A carrier may, however, substitute negotiable securities acceptable under the regulations in this part for previously-deposited negotiable securities without the Branch's prior approval.

(b) A carrier that has ceased to write insurance under the Act may apply to the Branch for withdrawal of its security deposit. The carrier must file with its application a sworn statement setting forth—

(1) A list of all cases in each State in which the carrier is paying compensation, together with the names of the employees and other beneficiaries, a description of causes of injury or death, and a statement of the amount of compensation paid;

(2) A similar list of all pending cases in which the carrier has not yet paid compensation; and

(3) A similar list of all cases in which injury or death has occurred within one year before such application or in which the last payment of compensation was made within one year before such application.

(c) The Branch may authorize withdrawal of previously-deposited indemnity bonds, letters of credit and negotiable securities that, in the opinion of the Branch, are not necessary to provide adequate security for the payment of the carrier's outstanding and potential LHWCA liabilities. No withdrawals will be authorized unless there has been no claim activity involving the carrier for a minimum of five years, and the Branch is reasonably certain that no further claims will arise.

**§ 703.210 Increase or reduction in security deposit amount.**

(a) Whenever the Office considers the security deposited by an insurance carrier insufficient to fully secure the carrier's LHWCA obligations, the carrier must, upon demand by the Branch, deposit additional security in accordance with the regulations in this part in an amount fixed by the Branch. The Branch will issue its decision requiring additional security in accordance with § 703.204, and the procedures set forth at §§ 703.204(d) and 703.205 for requesting a hearing and complying with the Office's decision will apply as appropriate.

(b) The Branch may reduce the required security at any time on its own initiative, or upon application of a

carrier, when in the Branch's opinion the facts warrant a reduction. A carrier seeking a reduction must furnish any information the Office requests regarding its outstanding LHWCA obligations for any State in which it does business, its obligations not secured by a State guaranty fund in each of these States, and any other evidence as the Branch considers necessary.

**§ 703.211 Authority to seize security deposit; use and/or return of proceeds.**

(a) The Office may take any of the actions set forth in paragraph (b) of this section when an insurance carrier—

(1) Defaults on any of its LHWCA obligations;

(2) Fails to renew any deposited letter of credit or substitute a new letter of credit, indemnity bond or acceptable negotiable securities in its place;

(3) Fails to renew any deposited negotiable securities at maturity or substitute a letter of credit, indemnity bond or acceptable negotiable securities in their place;

(4) Has State insolvency proceedings initiated against it; or

(5) Fails to comply with any of the terms of the Agreement and Undertaking.

(b) When any of the conditions set forth in paragraph (a) of this section occur, the Office may, within its discretion and as appropriate to the security instrument—

(1) Bring suit under any indemnity bond;

(2) Draw upon any letters of credit;

(3) Seize any negotiable securities, collect the interest and principal as they may become due, and sell or otherwise liquidate the negotiable securities or any part thereof.

(c) When the Office, within its discretion, determines that it no longer needs to collect the interest and principal of any negotiable securities seized pursuant to paragraphs (a) and (b) of this section, or to retain the proceeds of their sale, it must return any of the carrier's negotiable securities still in its possession and any remaining proceeds of their sale.

**§ 703.212 Required reports; examination of insurance carrier accounts.**

(a) Upon the Office's request, each insurance carrier must submit the following reports:

(1) A certified financial statement of the carrier's assets and liabilities, or a balance sheet.

(2) A sworn statement showing the extent of the carrier's unsecured LHWCA obligations for each State in which it is authorized to write insurance under the LHWCA or any of its extensions.

(3) A sworn statement reporting the carrier's open cases as of the date of such report, listing by State all death and injury cases, together with a report of the status of all outstanding claims.

(b) Whenever it considers necessary, the Office may inspect or examine a carrier's books of account, records, and other papers to verify any financial statement or other information the carrier furnished to the Office in any statement or report required by this section, or any other section of the regulations in this part. The carrier must permit the Office or its duly authorized representative to make the inspection or examination. Alternatively, the Office may accept an adequate independent audit by a certified public accountant.

#### **§ 703.213 Failure to comply.**

The Office may suspend or revoke a carrier's certificate of authority to write LHWCA insurance under § 703.106 when the carrier fails to comply with any of the requirements of this part.

#### **Subpart D—Authorization of Self-Insurers**

##### **§ 703.301 Employers who may be authorized as self-insurers.**

The regulations in this subpart set forth procedures for authorizing employers to self-insure the payment of compensation under the Longshore and Harbor Workers' Compensation Act, or its extensions. The Office may authorize any employer to self-insure who, pursuant to the regulations in this part, furnishes to the Office satisfactory proof of its ability to pay compensation directly, and who agrees to immediately cancel any existing insurance policy covering its Longshore obligations (except for excess or catastrophic workers' compensation insurance, *see* §§ 703.302(a)(6), 703.304(a)(6)) when OWCP approves the employer's application to be self-insured. The regulations require self-insurers to deposit security in the form of an indemnity bond, letters of credit or negotiable securities (at the option of the employer) of a kind and in an amount determined by the Office, and prescribe the conditions under which such deposits shall be made. The term "self-insurer" as used in these regulations means any employer securing the payment of compensation under the LHWCA or its extensions in accordance with the provisions of 33 U.S.C. 932(a)(2) and these regulations.

##### **§ 703.302 Application for authority to become a self-insurer; how filed; information to be submitted; other requirements.**

(a) Any employer may apply to become an authorized self-insurer. The application must be addressed to the Branch of Financial Management and Insurance (Branch) within OWCP's Division of Longshore and Harbor Workers' Compensation, and be made on a form provided by OWCP. The application must contain—

(1) A statement of the employer's total payroll for the 12 months before the application date;

(2) A statement of the average number of employees engaged in employment within the purview of the LHWCA or any of its extensions for the 12 months before the application date;

(3) A statement of the number of injuries to such employees resulting in disability of more than 7 days' duration, or in death, during each of the 5 years before the application date;

(4) A certified financial report for each of the three years before the application date;

(5) A description of the facilities maintained or the arrangements made for the medical and hospital care of injured employees;

(6) A statement describing the provisions and maximum amount of any excess or catastrophic insurance; and

(7) Any other information the Branch requests to enable it to give the application adequate consideration including, but not limited to, the reports set forth at § 703.310.

(b) The employer must sign and swear to the application. If the employer is not an individual, the employer's duly authorized officer must sign and swear to the application and list his or her official designation. If the employer is a corporation, the officer must also affix the corporate seal.

(c) At any time after filing an application, the employer must inform the Branch immediately of any material changes that may have rendered its application incomplete, inaccurate or misleading.

(d) By filing an application, the employer consents to be bound by and to comply with the regulations and requirements in this part.

##### **§ 703.303 Decision on employer's application.**

(a) The Branch will issue a decision granting or denying the employer's application to be an authorized self-insurer. If the Branch grants the application, the decision will fix the amount of security the employer must deposit. The Branch will transmit its

decision to the employer in a way it considers appropriate.

(b) The employer is authorized to self-insure beginning with the date of the Branch's decision. Each grant of authority to self-insure is conditioned, however, upon the employer's execution and filing of an Agreement and Undertaking and deposit of the security fixed in the decision in the form and within the time limits required by § 703.304. In the event the employer fails to comply with the requirements set forth in § 703.304, its authorization to self-insure will be considered never to have been effective, and the employer will be subject to appropriate penalties for failure to secure its LHWCA obligations.

(c) The Branch will require security in the amount it considers necessary to fully secure the employer's LHWCA obligations. When fixing the amount of security, the Branch may consider a number of factors including, but not limited to, the—

(1) Employer's overall financial standing;

(2) Nature of the employer's work;

(3) Hazard of the work in which the employees are employed;

(4) Employer's payroll amount for employees engaged in employment within the purview of the Act; and

(5) Employer's accident record as shown in the application and the Office's records.

(d) If an employer believes that the Branch incorrectly denied its application to self-insure, or that a lesser security deposit would fully secure its LHWCA obligations, the employer may request a hearing before the Director of the Division of Longshore and Harbor Workers' Compensation (Longshore Director) or the Longshore Director's representative. Requests for hearing must be in writing and sent to the Branch within ten days of the date of the Branch's decision. The employer may submit new evidence and/or argument in support of its challenge to the Branch's decision and must provide any additional documentation OWCP requests. The Longshore Director or his representative will notify the employer of the hearing date within 10 days of receiving the request. The Longshore Director or his representative will issue the final agency decision on the application within 60 days of the hearing date, or, where evidence is submitted after the hearing, within 60 days of the receipt of such evidence, but no later than 180 days after receiving the employer's request for a hearing.

**§ 703.304 Filing of Agreement and Undertaking; deposit of security.**

Within 45 days of the date on which the employer receives the Branch's decision (or, if the employer requests a hearing, a period set by the Longshore Director or the Longshore Director's representative) granting its application to self-insure and fixing the required security deposit amount (see § 703.303), the employer must:

(a) Execute and file with the Branch an Agreement and Undertaking, in a form prescribed and provided by OWCP, in which the employer shall agree to:

(1) Pay when due, as required by the provisions of the Act, all compensation payable on account of injury or death of any of its employees injured within the purview of the Act;

(2) Furnish medical, surgical, hospital, and other attendance, treatment and care as required by the Act;

(3) Deposit with the Branch indemnity bonds or letters of credit in the amount fixed by the Office, or deposit negotiable securities under §§ 703.306 and 703.307 in that amount;

(4) Authorize the Branch, at its discretion, to bring suit under any deposited indemnity bond or to draw upon any deposited letters of credit, as appropriate under the terms of the security instrument, or to collect the interest and principal as they become due on any deposited negotiable securities and to seize and sell or otherwise liquidate such negotiable securities or any part thereof when the employer:

(i) Defaults on any of its LHWCA obligations;

(ii) Fails to renew any deposited letter of credit or substitute a new letter of credit, indemnity bond or acceptable negotiable securities in its place;

(iii) Fails to renew any deposited negotiable securities at maturity or substitute a letter of credit, indemnity bond or acceptable negotiable securities in their place; or

(iv) Fails to comply with any of the terms of the Agreement and Undertaking;

(5) Authorize the Branch, at its discretion, to pay such compensation, medical, and other expenses and any accrued penalties imposed by law as it may find to be due and payable from the proceeds of the deposited security; and

(6) Obtain and maintain, if required by the Office, excess or catastrophic insurance in amounts to be determined by the Office.

(b) Give security in the amount fixed in the Office's decision:

(1) In the form of an indemnity bond with sureties satisfactory to the Office, and in such form and containing such provisions as the Office may prescribe: *Provided*, That only surety companies approved by the United States Treasury Department under the laws of the United States and the rules and regulations governing bonding companies may act as sureties on such indemnity bonds (see Department of Treasury's Circular-570);

(2) In the form of letters of credit issued by a financial institution satisfactory to the Branch and upon which the Branch may draw; or,

(3) By a deposit of negotiable securities with a Federal Reserve Bank or the Treasurer of the United States in compliance with §§ 703.306 and 703.307.

**§ 703.305 [Reserved]****§ 703.306 Kinds of negotiable securities that may be deposited; conditions of deposit; acceptance of deposits.**

A self-insurer or a self-insurer applicant electing to deposit negotiable securities to secure its obligations under the Act in the amount fixed by the Office under the regulations in this part shall deposit any negotiable securities acceptable as security for the deposit of public monies of the United States under regulations issued by the Secretary of the Treasury. (See 31 CFR part 225.) The approval, valuation, acceptance, and custody of such securities is hereby committed to the several Federal Reserve Banks and the Treasurer of the United States.

**§ 703.307 Deposits of negotiable securities with Federal Reserve banks or the Treasurer of the United States; interest thereon.**

Deposits of negotiable securities provided for by the regulations in this part shall be made with any Federal Reserve bank or any branch of a Federal Reserve bank designated by the Office, or the Treasurer of the United States, and shall be held subject to the order of the Office. The Office will authorize the self-insurer to collect interest on the securities deposited by it unless any of the conditions set forth at § 703.304(a)(4) occur.

**§ 703.308 Substitution and withdrawal of indemnity bond, letters of credit or negotiable securities.**

(a) A self-insurer may not substitute other security for any indemnity bond or letters of credit deposited under the regulations in this part except when authorized by the Office. A self-insurer may, however, substitute negotiable securities acceptable under the

regulations in this part for previously-deposited negotiable securities without the Office's prior approval.

(b) A self-insurer discontinuing business, discontinuing operations within the purview of the Act, or securing the payment of compensation by commercial insurance under the provisions of the Act may apply to the Office for the withdrawal of the security it provided under the regulations in this part. The self-insurer must file with its application a sworn statement setting forth—

(1) A list of all cases in each compensation district in which the self-insurer is paying compensation, together with the names of the employees and other beneficiaries, a description of causes of injury or death, and a statement of the amount of compensation paid;

(2) A similar list of all pending cases in which the self-insurer has not yet paid compensation; and

(3) A similar list of all cases in which injury or death has occurred within one year before such application or in which the last payment of compensation was made within one year before such application.

(c) The Office may authorize withdrawal of previously-deposited indemnity bonds, letters of credit and negotiable securities that, in the opinion of the Office, are not necessary to provide adequate security for the payment of the self-insurer's outstanding and potential LHWCA obligations. No withdrawals will be authorized unless there has been no claim activity involving the self-insurer for a minimum of five years, and the Office is reasonably certain no further claims will arise.

**§ 703.309 Increase or reduction in the amount of indemnity bond, letters of credit or negotiable securities.**

(a) Whenever the Office considers the principal sum of the indemnity bond or letters of credit filed or the amount of the negotiable securities deposited by a self-insurer insufficient to fully secure the self-insurer's LHWCA obligations, the self-insurer must, upon demand by the Office, deposit additional security in accordance with the regulations in this part in an amount fixed by the Branch. The Branch will issue its decision requiring additional security in accordance with § 703.303, and the procedures set forth at §§ 703.303(d) and 703.304 for requesting a hearing and complying with the Office's decision will apply as appropriate.

(b) The Office may reduce the required security at any time on its own initiative, or upon application of a self-



insurer, when in the Office's opinion the facts warrant a reduction. A self-insurer seeking a reduction must furnish any information the Office requests regarding its current affairs, the nature and hazard of the work of its employees, the amount of its payroll for employees engaged in maritime employment within the purview of the Act, its financial condition, its accident experience, a record of compensation payments it has made, and any other evidence the Branch considers necessary.

**§ 703.310 Authority to seize security deposit; use and/or return of proceeds.**

(a) The Office may take any of the actions set forth in paragraph (b) of this section when a self-insurer—

- (1) Defaults on any of its LHWCA obligations;
- (2) Fails to renew any deposited letter of credit or substitute a new letter of credit, indemnity bond or acceptable negotiable securities in its place;
- (3) Fails to renew any deposited negotiable securities at maturity or substitute a letter of credit, indemnity bond or acceptable negotiable securities in their place; or
- (4) Fails to comply with any of the terms of the Agreement and Undertaking.

(b) When any of the conditions set forth in paragraph (a) of this section occur, the Office may, within its discretion and as appropriate to the security instrument—

- (1) Bring suit under any indemnity bond;
- (2) Draw upon any letters of credit;
- (3) Seize any negotiable securities, collect the interest and principal as they may become due, and sell or otherwise

liquidate the negotiable securities or any part thereof.

(c) When the Office, within its discretion, determines that it no longer needs to collect the interest and principal of any negotiable securities seized pursuant to paragraphs (a) and (b) of this section, or to retain the proceeds of their sale, it must return any of the employer's negotiable securities still in its possession and any remaining proceeds of their sale.

**§ 703.311 Required reports; examination of self-insurer accounts.**

(a) Upon the Office's request, each self-insurer must submit the following reports:

- (1) A certified financial statement of the self-insurer's assets and liabilities, or a balance sheet.
- (2) A sworn statement showing by classifications the payroll of employees of the self-insurer who are engaged in employment within the purview of the LHWCA or any of its extensions.
- (3) A sworn statement covering the six-month period preceding the date of such report, listing by compensation districts all death and injury cases which have occurred during such period, together with a report of the status of all outstanding claims showing the particulars of each case.

(b) Whenever it considers necessary, the Office may inspect or examine a self-insurer's books of account, records, and other papers to verify any financial statement or other information the self-insurer furnished to the Office in any report required by this section, or any other section of the regulations in this part. The self-insurer must permit the Office or its duly authorized representative to make the inspection or

examination. Alternatively, the Office may accept an adequate report of a certified public accountant.

**§ 703.312 Period of authorization as self-insurer.**

(a) Self-insurance authorizations will remain in effect for so long as the self-insurer complies with the requirements of the Act, the regulations in this part, and OWCP.

(b) A self-insurer who has secured its liability by depositing an indemnity bond with the Office will, on or about May 10 of each year, receive from the Office a form for executing a bond that will continue its self-insurance authorization. The submission of such bond, duly executed in the amount indicated by the Office, will be deemed a condition of the continuing authorization.

**§ 703.313 Revocation of authorization to self-insure.**

The Office may for good cause shown suspend or revoke the authorization of any self-insurer. Failure by a self-insurer to comply with any provision or requirement of law or of the regulations in this part, or with any lawful order or communication of the Office, or the failure or insolvency of the surety on its indemnity bond, or impairment of financial responsibility of such self-insurer, shall be deemed good cause for suspension or revocation.

Signed at Washington, DC, this 18th day of July, 2005.

**Victoria A. Lipnic,**

*Assistant Secretary for Employment Standards.*

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