

WORKERS COMPENSATION RATEMAKING

MONTANA LEGISLATIVE FINANCE COMMITTEE

March 6, 2008

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NCCI**

WC Ratemaking

- **Where to start**
- **Where does it come from**
- **What to do with it**
- **How can we be sure**
- **Bottom line to Joe Q. Public**

Technical & Actuarial Language

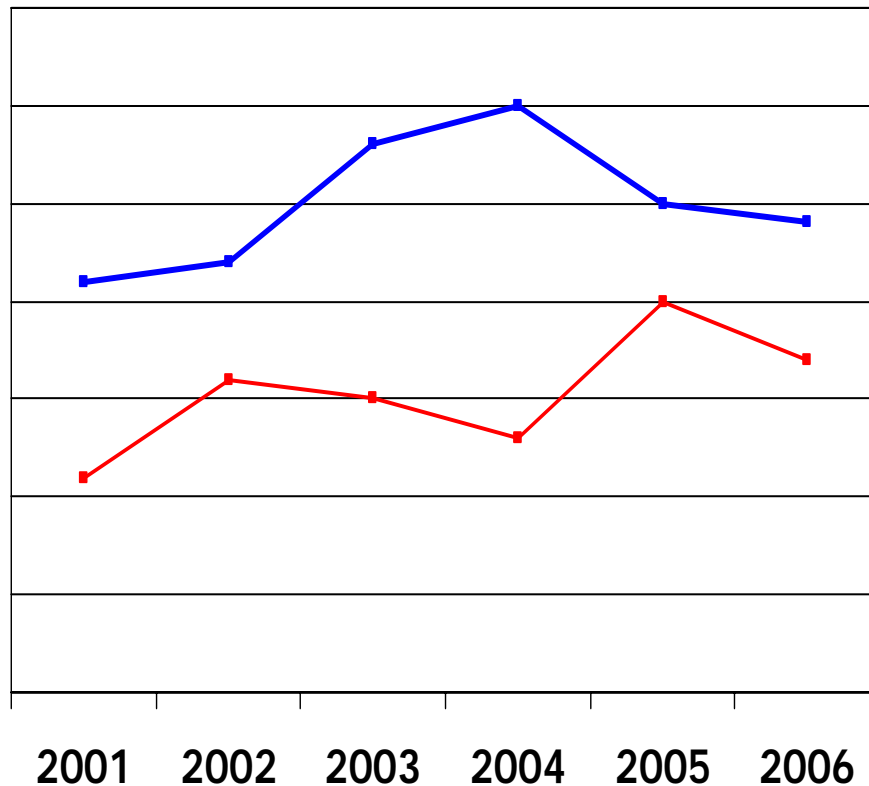
- Tail Factors
- Incurred But Not Reported
- On-Level Factor
- Exponential Trend Factors
- 18th to Ultimate Development
- Composite Adjustment Factor
- Off-Balance

Where to start?



- Look at where the state is
- Gather new and updated data
- Objectively analyze it
- Mix in other factors
- Spread it out

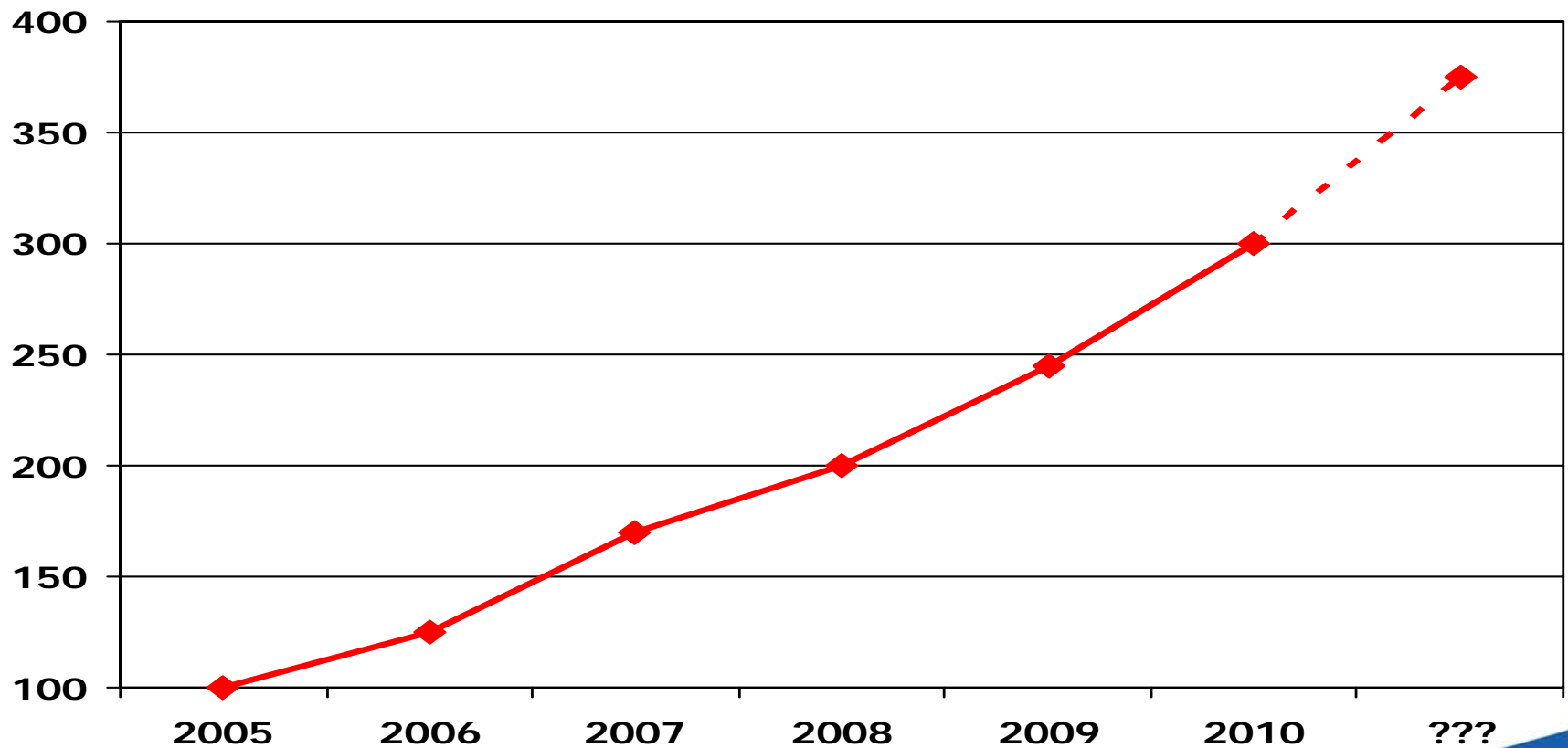
Where are we?



- What is the current status of the state?
- Any recent:
 - System Changes?
 - Benefit Changes?
 - Law Changes?
 - Other Changes?

WC – A long tail line

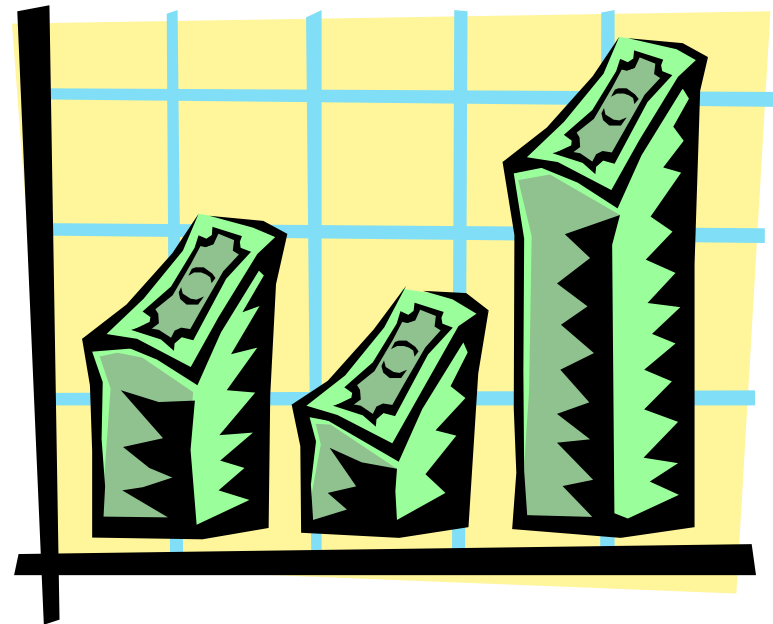
**\$100 spent on a claim in 2005 will
ultimately cost about \$375**



1ST Step: Determine Overall Rate Level

How much premium is needed:

- To fund the system?
- Only pay the anticipated indemnity and medical losses?



Data...

- **Financial Data**
 - Calendar Year Data
 - Policy Year Data

Answers the 1st question:

“How much was collected?”



...and more Data



- **Loss Data**

Answers the 2nd question:

“How much was paid out?”

- **Medical costs**
- **Wage Replacement**
- **Type of injuries**
- **Frequency**
- **Severity**

Different Data For Different Needs

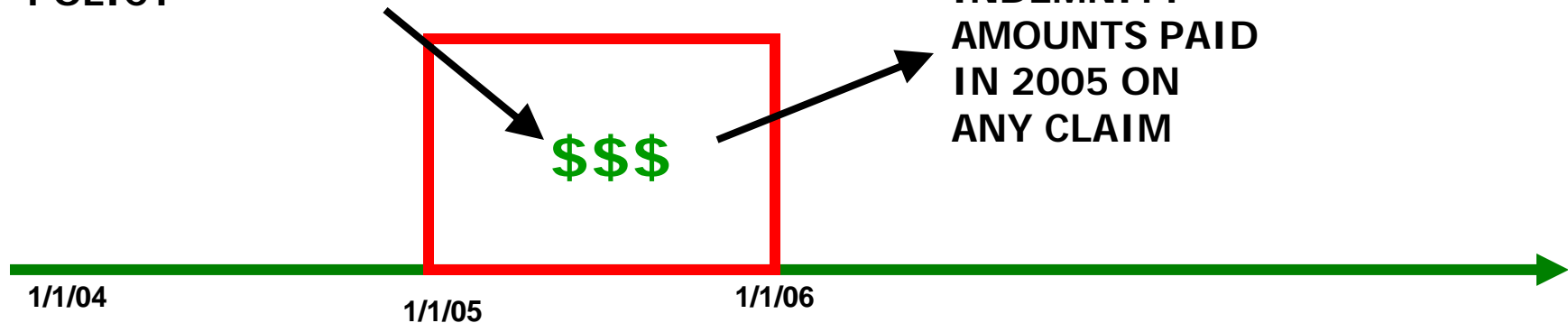


- Calendar Year Data
- Policy Year Data
- Individual Policy Data

Calendar Year 2005

**PREMIUM COLLECTED
IN 2005 FROM ANY
POLICY**

**MEDICAL AND
INDEMNITY
AMOUNTS PAID
IN 2005 ON
ANY CLAIM**



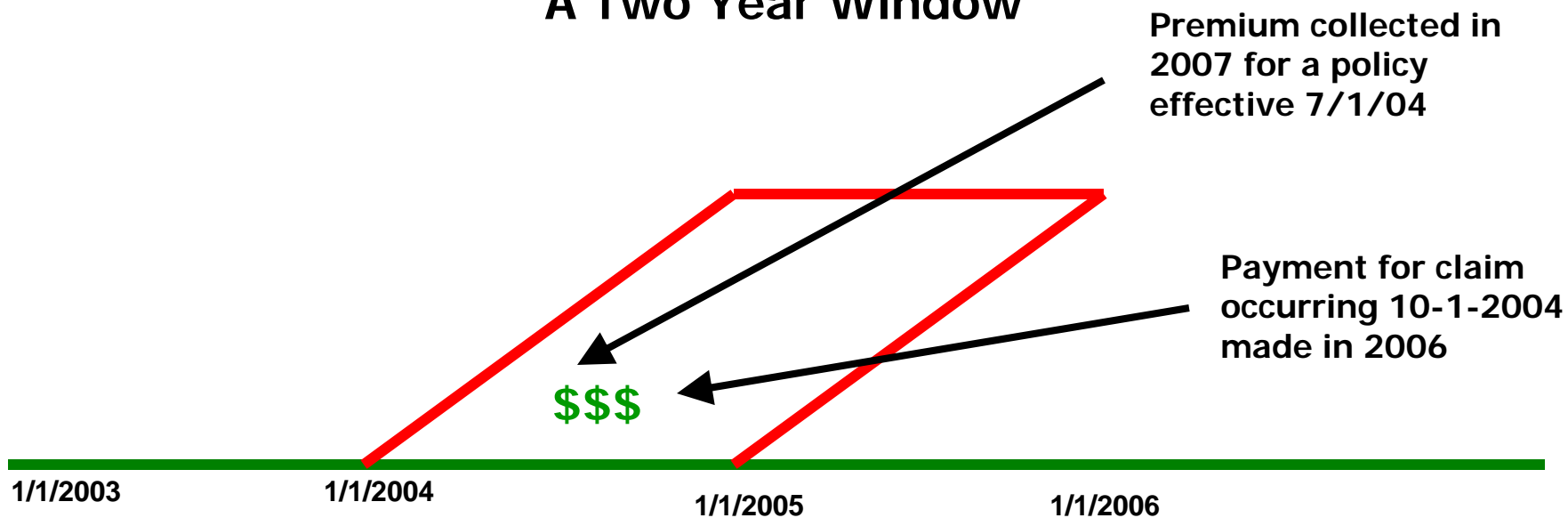
Consists of all transactions reported in 2005, regardless of the years which generated them.

Premium in – losses paid out

Sources: NAIC, Annual Statements or AM Best

Policy Year 2004

A Two Year Window



All policies with effective dates from 1/1/2003 through 12/31/2003 and expiration dates from 12/31/2003 through 12/31/2004

Data is organized by matching premiums and losses to policies issued during a given year, regardless of when it's reported to insurer

Individual Policy Data

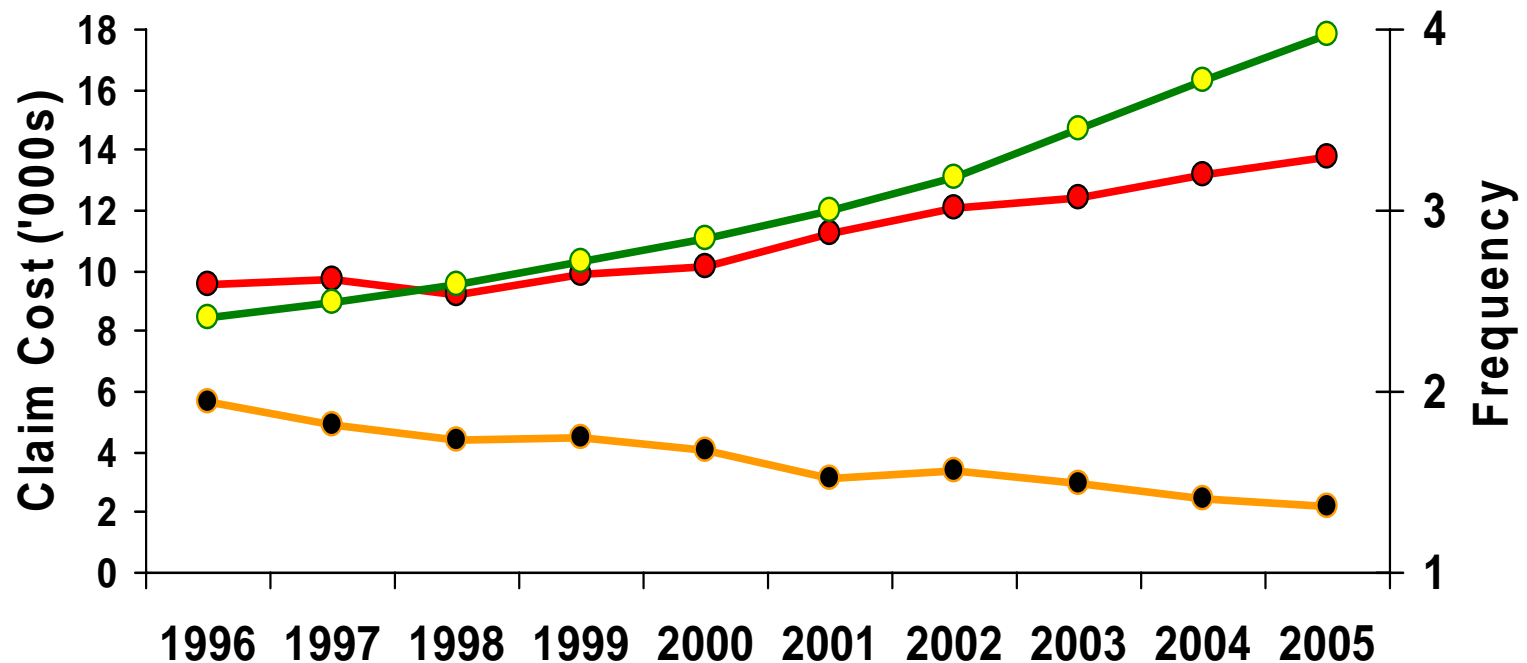
- **Payroll and Loss Data by Classification and Policy**
 - **Used in individual class ratemaking**
 - **What was the overall experience of different industries?**
 - **Used for individual employer experience rating**
 - **Measurement of employer's own losses**

2nd Step: Trend

- Getting from Point **A**
Where we are today
- to Point **B**
Where we need to go
- Measure the changes in the growth/decline of wages and losses

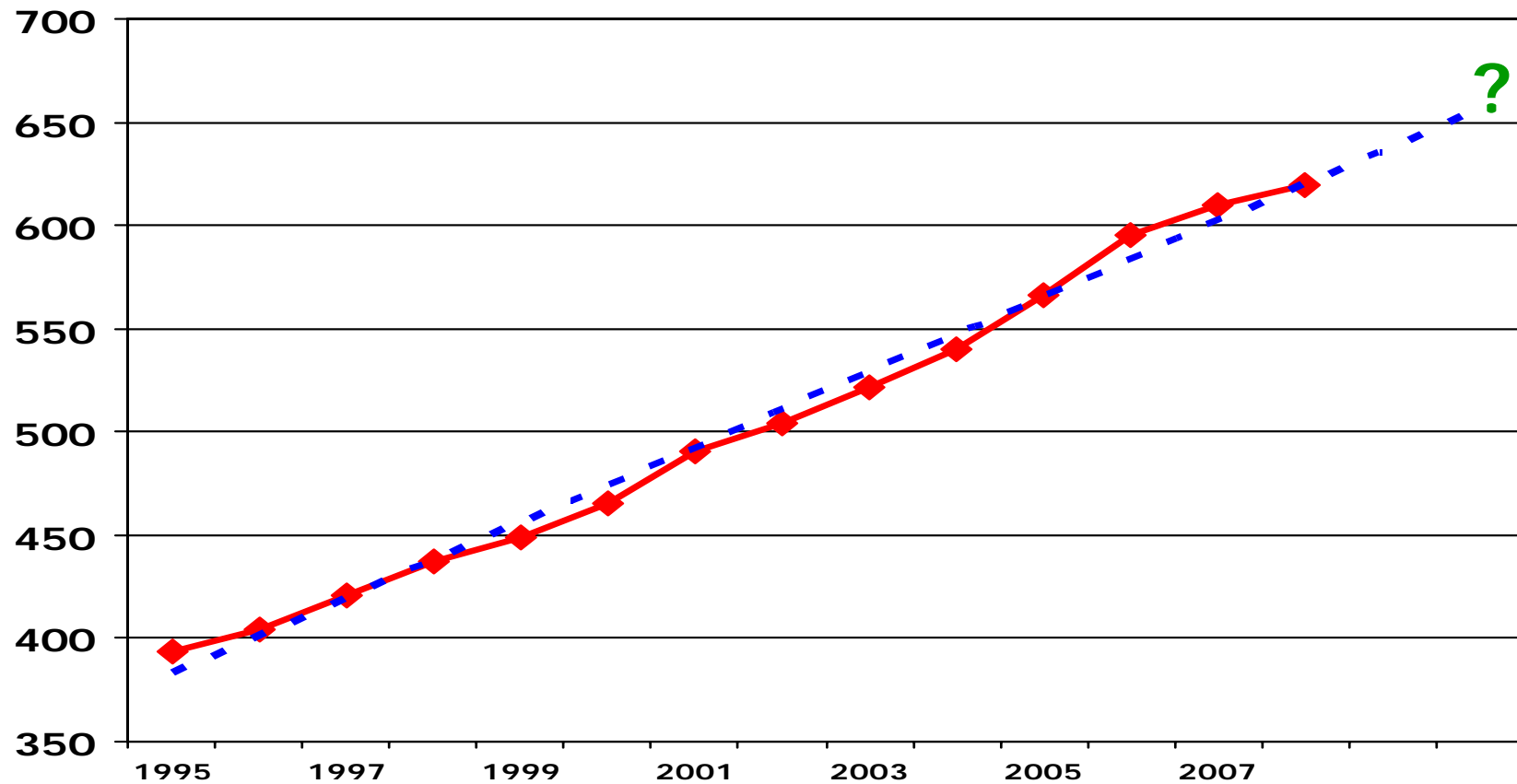
Differences indicate trend

Cost Per Claim Going Up, Number of Claims Going Down



● Indem Claim Cost ● Med Claim Cost ● Freq per 100 Workers

Wages Are Expected To Grow



Montana Average Weekly Wage & Trend - Source: US BLS

Negative Trend

Wages Grow Faster Than Losses

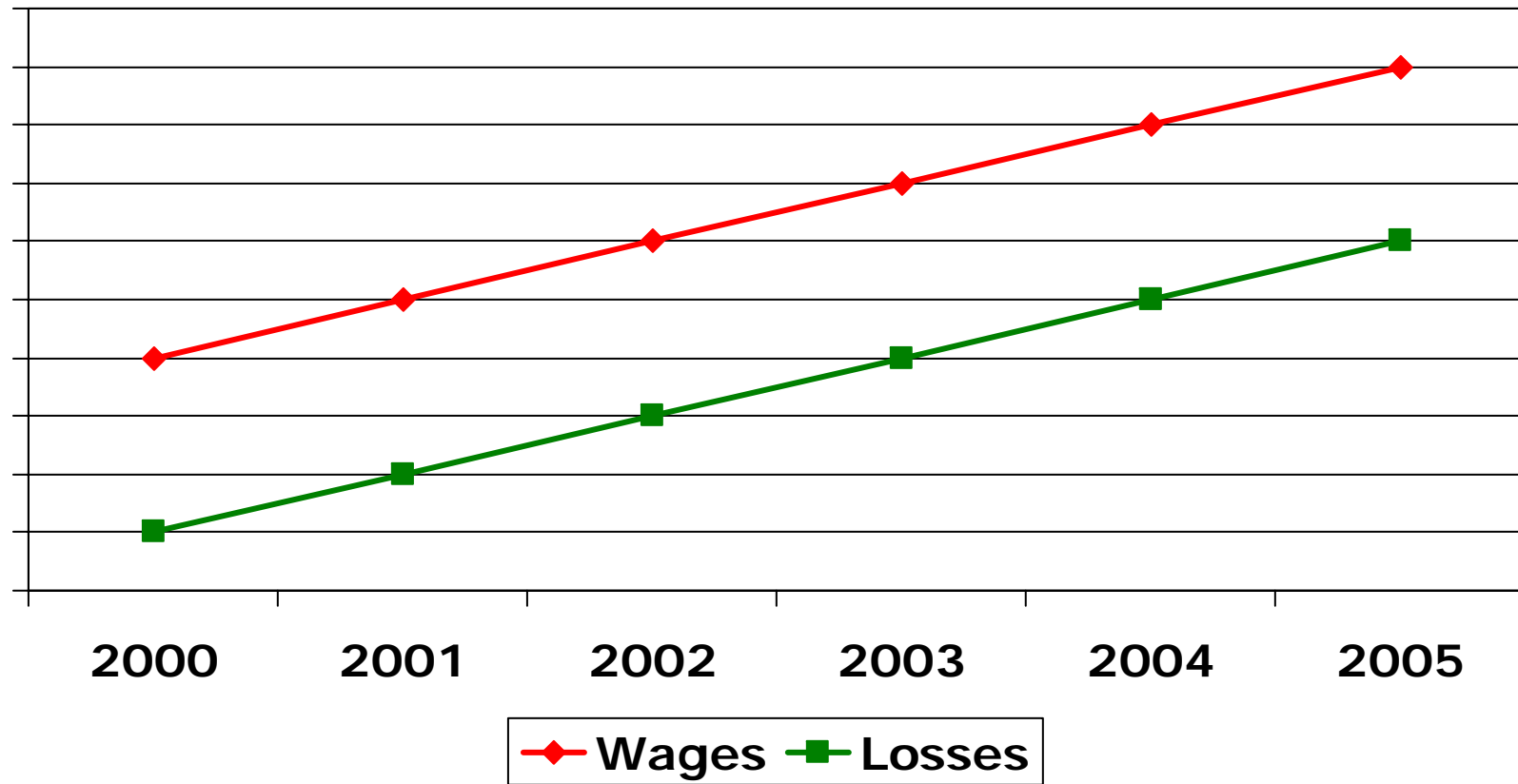


Positive Trend

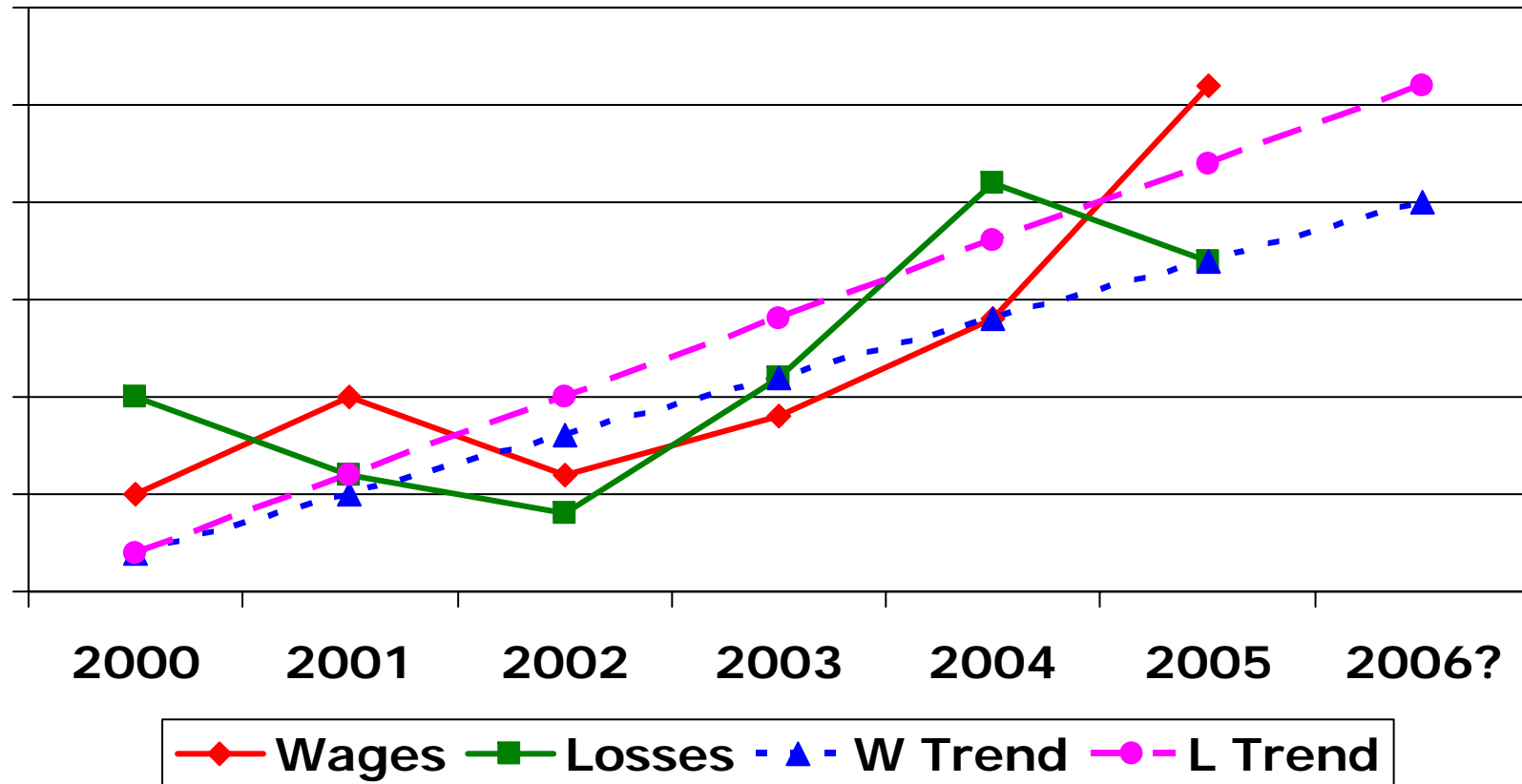
Losses Grow Faster Than Wages



Flat Trend



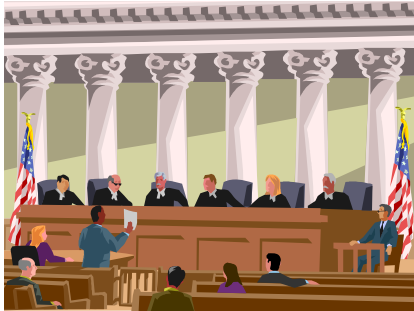
Real World



3rd Step: Analyze & Include Any Changes



- Legislation



- Court Decisions



- Regulations

Source:

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Impact of changes

- **Legislative Changes** –Can have an immediate impact on premiums by instituting higher or lower wage loss payments, definitions of accidents, etc.
- **Court Decisions** – Alter laws on compensability, coverages or benefits. Impact can be retroactive, immediate or in future
- **Regulations** – Generally more long term in nature (safety requirements) but can have immediate effect (assessments)

If we continue at the same level...

- Will things balance out?
- Will there be enough money to pay claims?
- Will there be more than needed?



4th Step: Sanity Check



**Check outside sources
for independent
verification:**

- DOL
- WCD
- OSHA
- BLS
- Carriers
- Guy on the street

5th Step: Determine Overall Premium Level

Add everything up to determine what the overall premium level needs to do:

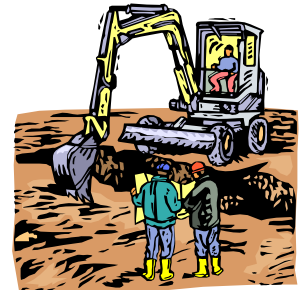
- Up?
- Down?
- No change?



6th Step: Spread Out The Changes

Not equitable to apply the rate change unilaterally to all employers

- Distribute to 5 Industry groups based on their experience**
- Distribute to individual classifications based on their experience**



Source:

© 2005 National Council on Compensation Insurance, Inc.



Final WC Rate

What Goes Into A Loss Cost Multiplier

- **Developed and Trended Losses –**
The underlying cost of losses – medical and indemnity payments - projected to ultimate amount.
- **Loss Adjustment Expense –** What does it take to settle claims. Includes evaluations, claims examiners, legal fees, etc.
- **Production and General Expense –** The cost of issuing a policy. Includes agents commissions, underwriting costs, loss control reports, auditing etc. as well as expenses for operation of offices and staff costs, advertising, training, etc
- **Taxes, Licenses and Fees –** Includes such items as property taxes, state or federal taxes, certification fees, etc,
- **Profit and Contingencies –** An amount put aside to address unknown or unexpected expenses such as change to benefits, larger than expected losses, court decisions, etc.

Final Manual Rate

Full Rate

- A provision for each expense item is added by the insurer to the final loss cost to produce a full manual rate
- Carrier rates expressed as a Loss Cost Multiplier

Loss cost X LCM = Final Rate

Profit & Contingencies
Taxes, Licens & Fees
Production & General Expense
Loss Adjustment Expense
Developed and Trended Losses

Final Premium Impact



- What does this mean to the average employer?
- Are there other factors involved?
 - Growth
 - Change in exposure
 - Losses
- Bottom Line:
"How much will this cost me?"

Policyholder Pricing Programs

Programs "tailor" the final premium to better match the characteristics of each insured

- Experience rating
- Contractors Premium Credit Program
- Schedule Rating
- Premium discounts by size of policy
- Retrospective Rating
- Etc.

Dirt Diggers, Inc

- **Dirt Diggers, Inc Payroll:**

- 6217 \$100,473
- 8810 \$ 25,716

- **Loss Cost Rates:**

- 6217 = \$17.56
- 8810 = \$.79

- **Mega Mutual Insurance Company**

- Loss Cost Multiplier = 1.25

- **MMIC Rates:**

- Class 6217 = \$21.95 /\$100
- Class 8810 = \$0.99/\$100

Dirt Diggers, Inc

Code 6217	\$100,473	x \$21.95/\$100	=	\$22,054
Code 8810	\$25,716	x \$.99/\$100	=	\$ 255

Manual Premium	=	\$22,309
Experience Mod	x	.95
Modified Premium	=	\$21,193
MCCPAP		.95
Standard Premium		\$20,134
Premium Discount (10%)	x	.90

Estimated Annual Premium **\$18,121**

Base Premium = **\$22309** Actual Premium = **\$18,121**

DIFFERENCE = **<\$4,188>** **@18% Savings**

Dig & Go, Inc.

- **Dig & Go, Inc Payroll**

- 6217 \$100,473
 - 8810 \$ 25,716

- **Loss Cost Rates:**

- 6217 = \$17.56
 - 8810 = \$.79

- **Fairly Equitable Insurance Company**

- Loss Cost Multiplier = 1.50

- **FEIC Rates:**

- Class 6217 = \$26.34/\$100
 - Class 8810 = \$ 1.19/\$100

Dig & Go, Inc.

$$\begin{array}{rclcl} 6217 & \$100,473 & \times & \$26.34/\$100 & = & \$ 26,465 \\ 8810 & \$25,716 & \times & \$ 1.19/\$100 & = & \$ 306 \end{array}$$

$$\text{Manual Premium} = \$ 26,771$$

$$\text{Experience Mod} \quad \times \quad 1.25$$

$$\text{Modified Premium} = \$ 33,463$$

$$\text{MCCPAP} \quad \times \quad .95$$

$$\text{Standard Premium} = \$31,791$$

$$\text{Premium Discount (7\%)} \quad \times \quad .93$$

$$\text{Estimated Annual Premium} \quad \$29,565$$

$$\text{Base Premium} = \$26,771 \quad \text{Actual Premium} = \$29,565$$

$$\text{DIFFERENCE} = \$2,794 \quad @ 8\% \text{ Increase}$$

Differences

- **Dirt Diggers, Inc**
 - **Safety conscientious**
 - **controlled losses**
 - **better training**

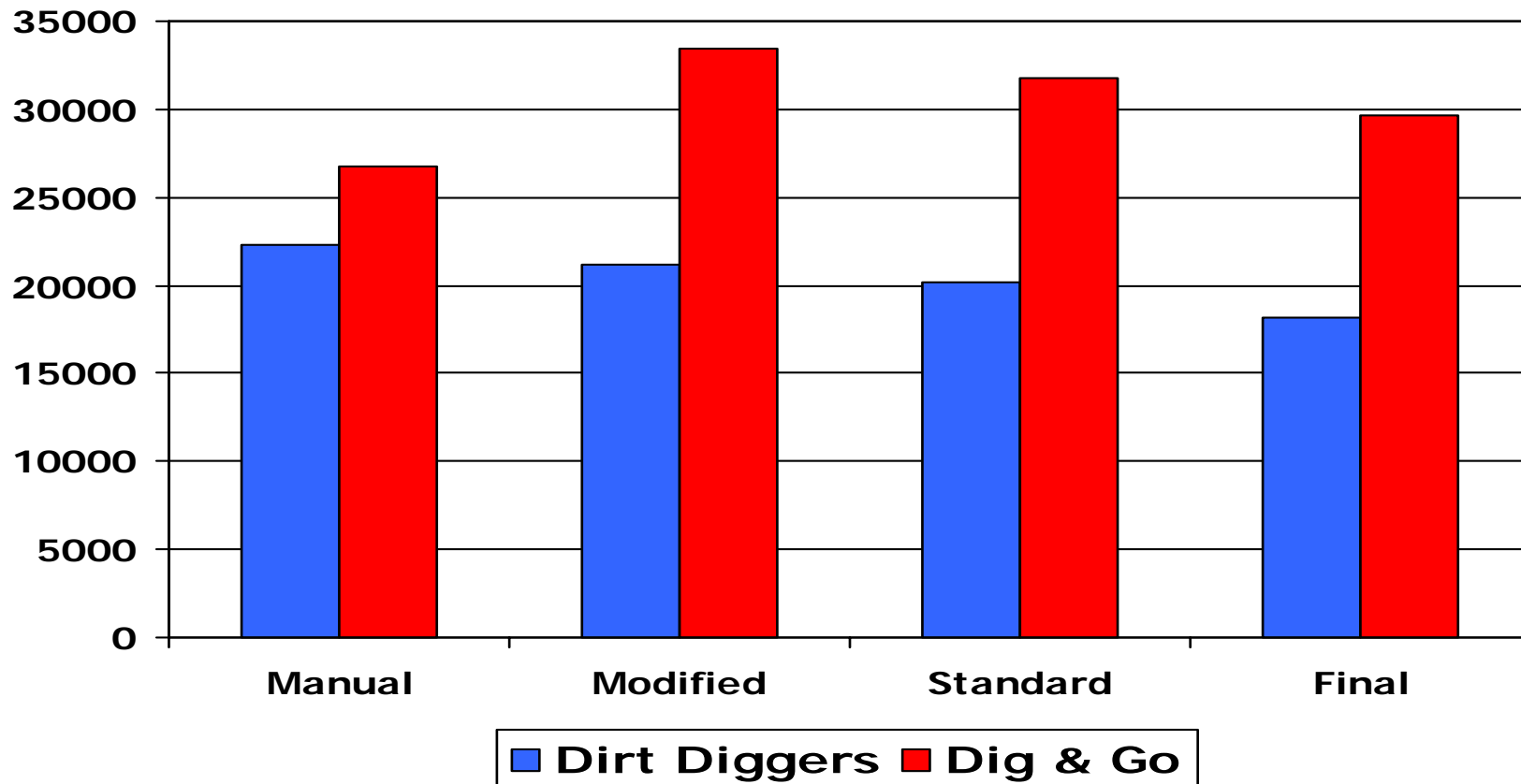
Provides more carrier choices, options for premium savings via lower ex-mod MCCPAP, etc.

- **Dig & Go, Inc**
 - **Multiple losses**
 - **less emphasis on safety**
 - **spotty training**

Results in less options for coverage, higher ex mod, lower premium discount, etc.

\$18,121	vs	\$29,565
\$11,444	or	63% higher

Premium Differences



Questions?

Comments?

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