
WC Insurance Pricing, Regulation and History of State Funds: An Overview

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WC Insurance Pricing, Regulation and History of State Funds – Briefing Outline

- How premiums are set (Insurance rate making)
 - How individual employer premiums are calculated
 - Alternative policy options
 - Underwriting
 - Market options in MT and comparator states
 - Public policy options for rate regulation
 - History and purpose of State Funds
 - Options for “market of last resort”
 - Current Montana insurance regulation
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WC Insurance Pricing: Manual Rates

CLASS CODE	DESCRIPTION	RATE
2812	Cabinet Mfg.	\$4.78
5183	Plumbing Installation. & Service	\$8.19
5190	Electrical Wiring	\$5.71
7380	Drivers NOC*	\$7.82
8742	Outside Sales	\$0.63
8810	Office Clerical	\$0.36

Job Classifications

Rate per \$100 of payroll

* Not Otherwise Classified

WC Insurance Pricing: Manual Premium Calculation

Rates
by classification
by state

X

Payroll
by classification
by state

\$100

Example for Office Clerks:

$$\begin{array}{r}
 \$0.36 \\
 \text{(for class 8810)}
 \end{array}
 \times
 \begin{array}{r}
 \$1,000,000 \\
 \$ 100
 \end{array}
 = \$3,600$$

WC Insurance Pricing: Experience Modification Factor

A Definition: **Your actual losses compared to the losses of other employers in your same business**

Timing

Years Included in the Calculations			Calculation Made	For Policy Period
2005	2006	2007	2008	2009

WC Insurance Pricing Pieces To The Pricing Puzzle

- Past premium history
- Incurred losses and IBNR
- Loss adjustment expenses
- Trend
- Reinsurance
- Taxes and assessments
- Marketing expenses
- Management expenses
- Profit
- The market (what is the competition charging?)
- Investment income (from reserves and surplus)

Premium Price Structure for a Specific State

- Varies by:
 - Degree of regulation
 - Underwriting decisions
 - The degree of competition
 - The assumptions accepted or used in the pricing model

Degree of Regulation

- Rate approval requirements dictate *when* an insurer is required to file its rates with the regulatory authority and *when and if* the proposed rates may be used.

Spectrum of Rate Approval Requirements					
Most Restrictive ←-----→Least Restrictive					
Prior Approval ("File and Wait")	Prior Approval with Deemer ("File and Wait a Certain Number of Days")	Ability to Disapprove Subsequent to Filing ("File and Use")	Ability to Disapprove Subsequent to Use ("Use and File")	Approval Required Only for Certain Percentage Change ("Flex Rating")	No Approval Required ("Filing for Information Purposes Only")

Montana's WC Insurance Rate Regulations

- Private Insurers are regulated by the Commissioner of Insurance's Office
 - NCCI loss costs filings are the basis for all rate regulation but insurers can file their own rates
 - If an insurer chooses to file their own rates, they will be considered file and use unless the filed loss cost multiplier is less than 1 or their filed rates are less than the NCCI filed loss costs, then "prior approval" is required
- State Fund files data with NCCI but is not regulated by the Commissioner of Insurance. They are subject to oversight by the Legislative Auditor and their own Board.

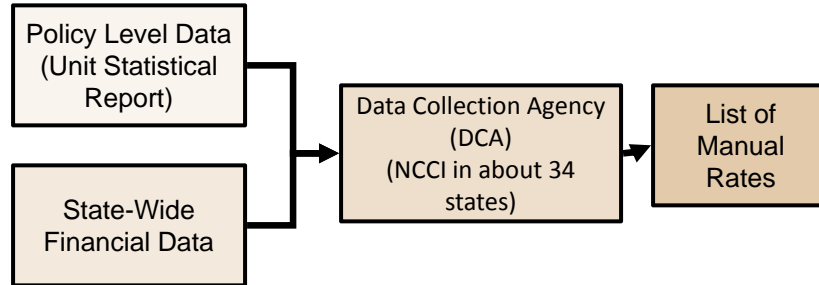
How Do States Regulate WC Rates?

Prior Approval (File and Wait)	Prior Approval with Deemer (File and Wait for a time period)	Ability to Disapprove Subsequent to Filing (File and Use)	Ability to Disapprove Subsequent to Use (Use and File)	Variation of Regulatory Strategies	No Approval Required (Filing For Information Purposes Only)
AK, AL, AR, CA, DC, FL, HI, IA, ID, LA, MA, MN, MT*, NH, NJ, NV, NY, OR, PA, VT, WI	AZ, CT, GA,	CO, DE, KS, MT, NE, NM, NC, RI, SD, TX, UT, WV	IL, MO	MD, MT, OK, TN, VA	SC

•MT is generally "file and use". However, if a company chooses to file their own rates and their loss cost multiplier is less than 1 or their rates are less than the NCCI filed loss costs, then "prior approval" is required. Plan 3 is not regulated by the Commissioner of Insurance.

Source: NCCI and Montana Insurance Commissioner's Office

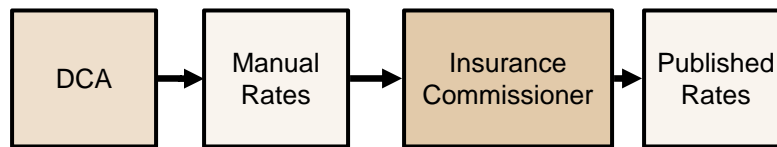
Data Collection (It's Legal)



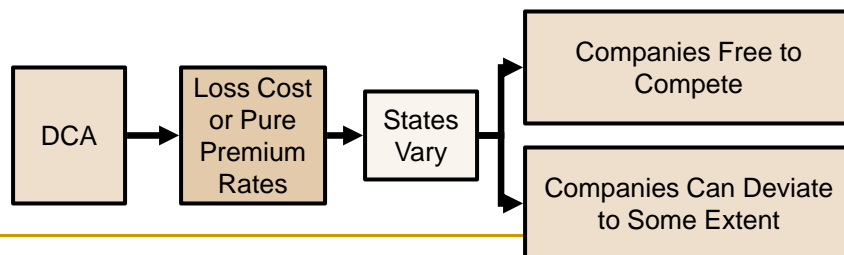
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Competition and Regulation

Administered Pricing



Competitive Pricing



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Rate Variation Methods:

- “Techniques permitted by a state which allow insurers to charge a rate that is different from the approved rate.”
 - Deviations
 - Schedule rating
 - Retrospective rating
 - Fixed credits
 - Dividends
 - Negotiated experience modifications
 - Deductibles

WC Insurance Pricing: A Guaranteed Policy Example

1. Obtain deviation of rates (if any)
2. Compute Manual Premium \$25,179
3. Adjust for Experience modification
 $(.80) \times \$25,179 =$
 Adjusted Manual Premium \$20,143

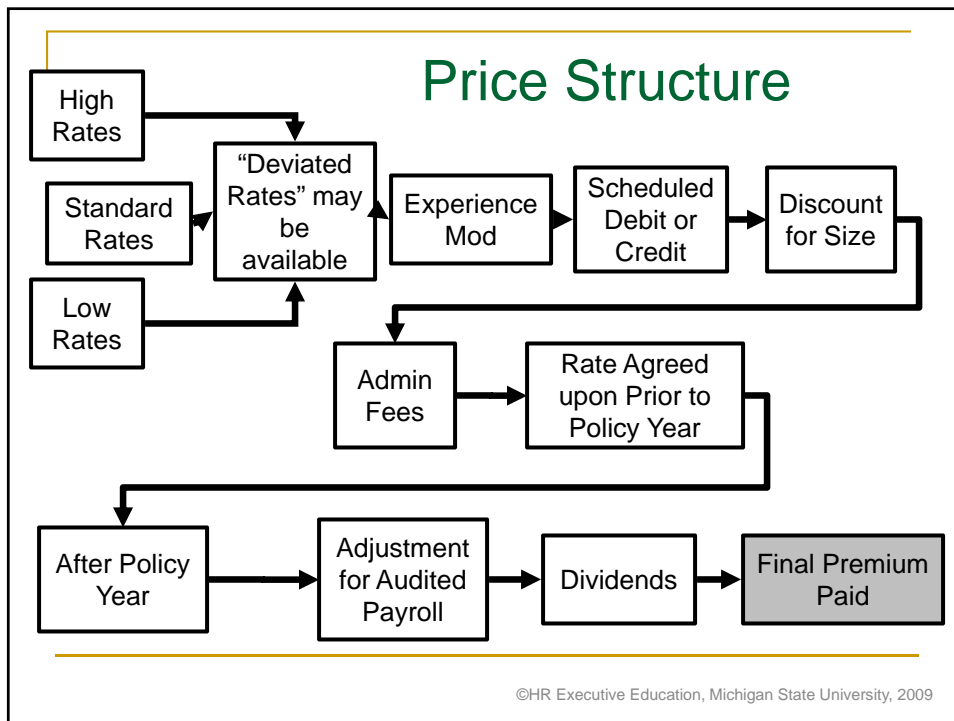
CC	2812	8742	8810
Est. Payroll	\$500,000	\$65,000	\$185,000
Divide by \$100	\$5,000	\$650	\$1,850
X Rates	\$4.78	\$.80	\$.41
	\$23,900	\$520	\$758.50
		Total MP	\$25,179
		X Mod	.80

WC Insurance Pricing: A Guaranteed Policy Example

4. Apply Scheduled Credit or Debit (if available)
5. Reduce by Premium Discount
6. Add Expense Constant

Result is ESTIMATED
annual premium of
\$18,579

Adjusted Manual Prem.	\$ 20,143
Apply schedule debit or credit	X .95
Adjusted Manual Prem.	\$19,136
Premium Discount	(\$5000) X .95 + \$5000
Adjusted Manual Prem.	\$18,429
Expense Constant	+ 150



WC Insurance Pricing: A Guaranteed Policy Example

- Final ACTUAL premium will be calculated *AFTER* the policy period when actual payroll is reported and/or audited. At that time, premium could go up or down if you expanded or reduced the size of your business
- Final ACTUAL premium may also be reduced if carrier issues a “dividend” or refund

Hence an employer’s actual premium will be based on many factors some of which they have control over (prevention, return to work, labor management relations, etc.) and some of which they do not (market competition, interest rates, quality of claims management, cost and quality of medical care, statutory benefits required to be paid, etc.)

WC Pricing: Alternative Policy Options

- Guaranteed cost insurance policies
- Small deductibles
- Retrospectively rated insurance policies
- Large deductibles
- Captives
- Wrap Up Policies
- Self Insurance
 - Individual
 - Group

Market Options in Comparator States

	State Fund	Private Ins.	Ind. SI	Group SI
AK	No	Yes	Yes	No
ID	Yes	Yes	Yes	No
MT	Yes	Yes	Yes	Yes
NM	Yes	Yes	Yes	Yes
ND	Yes	No	No	No
OR	Yes	Yes	Yes	Yes
SD	No	Yes	Yes	No
WA	Yes	No	Yes	No
WY	Yes	No	Non-haz	Non-haz

WC Insurance Overview: Underwriting

- Underwriting is the process of evaluating the profit or loss potential associated with the risks of an individual employer *
- Underwriters are charged with making the following decision on each employer:
 - Do we want to assume this risk or decline it?
 - If we want to assume it, what price should we charge in order to make an underwriting profit for the company

*Edward Welch, *Insurance and Self-Insurance*, Michigan State University CWCP

WC Regulation: Markets of Last Resort

- What happens if no insurer wants to write a wc policy for an employer?
 - In Montana, the Montana State Fund Must provide coverage
 - In other states, they use:
 - A State Fund
 - Assigned risk plans
 - A Joint Underwriting Authority
 - Assigned risk “pools”
- And they may be required to be self-funded or they may be subsidized by the rest of the insurers and employers
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History of State Funds

- Been around since Washington State enacted their fund (monopolistic) in 1911
 - Today only the states of North Dakota, Ohio, Washington and Wyoming still have monopolistic state funds
 - All other state funds (22) exist as the market of last resort, to ensure a competitive market, or to do both
 - Not all state funds are the markets of last resort
 - Some were initially created as a result of a lack of trust of private insurers. Regulators expected State Funds would provide a opportunity to obtain information they could not otherwise obtain from the private market and ensure insurers would not reap unfair profits.
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State Funds – Rapidly Changing

- Nevada and West Virginia have gone from monopolistic state funds to competitive markets
 - The wc state fund in MI became a private insurer and discussions continue about the same happening in CO and OK
 - Many wc state funds are seeking authority to write policies in other states (ME, CO, OK are a few)
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Public Policy Issues In WC Regulation

- WC insurance is regulated to protect employers, injured workers, and the public.
 - Employers need protection from excess profits of insurers; they must be able to get wc coverage; they want fair competition and rates; and they need protection from insurers becoming insolvent
 - Workers need protection from employers and insurers who may become insolvent and need government to ensure they are paid the benefits to which they are entitled under the law
 - In some states, like Montana, when a State Fund does not collect enough premium to pay benefits, all the citizens of the state pay a tax to fund; in others, the employer policyholders of the State Fund are assessed, much like a mutual insurer.
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Who Pays Benefits to Injured Workers if a Payer Goes Bankrupt in Montana?

- **Plan 1- Self-Insured Employers** – Self Insurance Guaranty Association (not true for public self-insured entities)
 - **Plan 2 – Private Insurers** – Insurer's Guaranty Association
 - **Plan 3 – Montana State Fund** – All Montana taxpayers
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What Happens In Other States?

- Private Insurers usually are members of an Insurance Guaranty Fund within individual states
 - Individual Self Insurers have self insurance guaranty funds in some but not all states
 - Group self insurance arrangements are usually first joint and severally liable and then if all of the companies are bankrupt or out of business, the self insurance guaranty fund would pay claims if there were members
 - State Funds vary, some are mutuals, some are members of their state's insurance guaranty fund and some would depend on public money in cases of bankruptcy.
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Sources for this presentation:

- www.naic.org *Risk Based Capital*
- www.ncci.org – State rate and form filing requirements
- www.iii.org/Issues_Updates/Workers-Compensation.html
- www.aascif.org *State Funds: Their role in Workers' Compensation*
- *Workers' Compensation State Laws: Second Edition*, 2009, Workers Compensation Research Institute, Cambridge, MA
- *Insurance and Self-Insurance* – Michigan State University, School of Labor and Industrial Relations – Certified Workers' Compensation Professional course material
- *Deregulation of Workers' Compensation Pricing*, prepared by the staff of the Florida House of Representatives, October 30, 1998
- *Rate Regulation of Workers' Compensation Insurance*, Danson and Harrington, 1998, The AEI Press, Washington, D.C.

Questions?

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