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Understanding Worker's Compensation

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Agenda

- What is an Experience Rating
- Experience Rating Eligibility
- Purpose & Benefits of Experience Rating
- Basic Promulgation of an Experience Modification Rating
- Modification Changes – When & Why
- Implications of Return to Work Programs and Lost Time Incidents
- Is There Really a Benefit in not Reporting Claims?

Experience Rating Defined

- Experience Rating: A method in which the actual loss experience of the business is compared to the loss experience that is normally expected by other companies in the businesses rating class. The resulting experience modification factor is then applied to the premium.

- There are two types of NCCI modifications
  - Intrastate – When there is payroll is only in one participating state
  - Interstate – When payroll is in two or more participating states

NCCI Experience Rating Plan - Eligibility

- Mandatory for all employers that meet a premium eligibility criteria which varies by state*
- Computed by the NCCI for all states authorized to use the NCCI plan
- The NCCI Plan does not apply in CA, DE, MI, NJ, PA – nor the 4 monopolistic states of ND, OH, WA, WY. These states administer their own plans and rates**

**(For state specific info, refer to the premium eligibility table in the NCCI Plan Manual. https://www.ncci.com/ServicesTools/Pages/ER2003.aspx)*

***(Refer to state's insurance website for details related to rating plan)*

Purpose & Benefits of Experience Rating

- The NCCI's Experience Rating Plan is an integral part of the final cost of workers compensation
- Tailors the cost of insurance to fit each risk
- Modifies manual premium by a factor designed to more accurately price each risk
- Predicts loss experience
- Provides incentives for employers to manage costs & reduce losses with measurable & meaningful cost savings programs

Time Period used in Calculation

- The experience period is generally based on 3 years of payroll and loss data
  - This could range between 12 months and 45 months of data.
- The modification is calculated during the current policy term
  - Typically 60-90 days before the rating effective date
- The insurer is not required to report data about a policy to the state until 18 months after the policy inception date
- The current policy is not used in the calculation

Time Period used in Calculation

- NCCI Unit Stat Date – It's important!
  - Claim data is reported to NCCI by the Carrier electronically
  - 6 Months after expiration
  - Reduce unwarranted reserves
  - Close out open claims if possible

Time Period used in Calculation

- Example: An employers policy renews on January 1, 2018, the rating uses loss experience from the following policies:
  - 1/1/14 – 1/1/15
  - 1/1/15 – 1/1/16
  - 1/1/16 – 1/1/17
- Because the 17-18 policy period is not yet valued by the carrier or reported to NCCI, it is not used when the 18-19 modification is calculated

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Elements of Experience Rating

- Recognizes and measures both claim frequency and severity
- Each individual claim will be capped by an accident limitation, which differs by state
- In most states*, an Experience Rating Adjustment (ERA) is then applied.
- The ERA reduces medical only claims by 70%
  - Acts to reduce the incentive for employers to pay medical only claims without reporting them to the carrier.

*States that have not adopted the ERA include: MA, NY, CO, NJ

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Status of Experience Rating

- The status of an experience modification determines what state approved rating values are used to calculate the experience rating modification
- There are three statuses:
  - Preliminary
  - Final
  - Contingent

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Status of Experience Rating

- Preliminary – When the NCCI doesn't have the final approved rating values for all the state(s) that apply. The Modification will be calculated using the prior approved rating values, while a new rate filing is pending.

Status of Experience Rating

- Final - The mod uses current rating values that have been approved for use in a specific state. Interstate mods can have states with both preliminary and final rating values. Only when all states are final is the mod considered final.

Status of Experience Rating

- Contingent – is issued when NCCI is expecting audited payroll and loss information but has not received the information from the insurance provider by the time the rating is produced.

Experience Rating Mod Factor

- The modification factor applied to an employer's policy/premium is one of three factors:
- Unity factor = 1.00
- Credit Mod = mod lower than 1.00 (e.g, 0.75)
- Debit Mod = mod higher than 1.00 (e.g, 1.25)

Application of Experience Rating

- How the experience rating modification (mod) affects premium paid for workers compensation:

Premium		Modification Factor		Modified Premium
$100,000	X	0.75	=	$75,000
$100,000	X	1.00	=	$100,000
$100,000	X	1.25	=	$125,000

Application of Experience Rating

- Illustration of how rates and the experience modification factor are used to determine premium.
- Rates for each classification code are approved by state.
- Example includes a single employer with employees in 2 classifications.

Classification	Payroll	Divided by 100	Rate per $100 of Payroll	Premium
Clerical	$70,000	700	$0.75	$525
Roofer	$200,000	2,000	$63.17	$126,340

Total Premium	=$126,865
Modification Factor	=1.25
Modified Premium	=$158,581

Summary of Plan

- Mandatory for all risks that meet the premium eligibility requirement
- Measures how the performance of an employer differs predictably from similarly classified employers
- Tailors the cost of coverage to a particular employer

Experience Rating Basic Formula

$$\frac{\text{Actual Losses}}{\text{Expected Losses}} = \text{Experience Modification}$$

- The Formula:
  - Determines the modification factor for eligible risks
  - Includes data for individual risks

Expected Losses

- Expected Losses = Payroll X ELR/100
  - Expected Loss Rate (ELR) vary by classification (determined by state)
- Expected Losses are separated into primary (reflects frequency) and excess (reflects severity)
  - Expected Primary Losses = Expected Losses X discount ratio (ratio is established by the state)
  - Excess Losses = Expected Losses – Primary Losses

Calculation of Expected Losses

- Comparison of Operations
  - The higher rated the class code, the larger the ELR
  - The larger the ELR, the greater the expected losses
- Payroll (Exposure Base)
  - The larger the exposure, the greater the expected losses

Frequency vs. Severity

- Claim frequency has a greater weight than claim severity
  - The specific cost of an accident is statistically less predictable than the fact that an accident will occur

	Claims	Cost per Claim	Total Losses
Employer 1	1	$50,000	$50,000
Employer 2	10	$5,000	$50,000

- Risks with higher claim frequency will generally have higher future workers compensation costs
  - Statistically, Employer 1 is considered more stable, when you consider that any one of the small 10 accidents of Employer 2 could incur higher costs under the right (or wrong) circumstances

Primary vs. Excess Loss

- Primary Loss = the first $17,000* of a claim
- Excess Loss = Any ratable individual loss greater than $17,000*
  - Ratable loss is that portion of a claim that falls within the loss cap established by the state's accident limitation amount

	Total Loss Amount	Ratable Loss	Primary Loss	Excess Loss
Employer 1	$9,000	$9,000	$9,000	$0
Employer 2	$100,000	$100,000	$17,000	$83,000

- Note: The primary loss amount becomes effective concurrently with each state's approved rate/loss cost filing

*In most states effective with rate filing on or after 1/1/19

Primary vs. Excess Loss

- Primary losses (frequency) are given a greater weight than excess losses (severity)

	Number of Losses		Total Loss Amount	Total Primary Loss	Total Excess Loss
Employer 1	1	X	$50,000	$17,000	$33,000
Employer 2	10	X	$5,000	$50,000	$0

Weight Factor

- The Weight Factor is the weight given to excess and expected losses
- The Weight Factor determines the portion of excess losses used in the calculation
- The Weight Factor acts as a stabilizing value to prevent the mod from shifting too far above or below unity (1.0)
- The Weight Factor is a small percentage for small employers and increases with the size of the employer

Total Expected Losses	Weight Factor	Total Loss Amount	Excess Loss	Ratable Excess Loss
$250,000	0.25	$50,000	$33,000	$8,250

The state primary loss threshold or split point amount used in this calculation is $17,000

Characteristics of Experience Rating

- Including very large losses would reduce the predictive ability of the plan
- One very large claim does not imply a pattern of claim frequency
- Standardized weights are assigned to losses and are calibrated to ensure the mod best reflects the loss history of the particular employer relative to its classification

Per-Claim Accident Limitation

- Claims are limited by the state per-claim accident limitation to prevent large one-off claims from reducing the predictive ability of the plan
- Limitations vary by state and by rate filing

	Total Loss Amount	Ratable Loss	Ratable Primary Loss	Non-Ratable Loss
Florida	$500,000	$240,000	$17,000	$260,000
Georgia	$500,000	$319,500	$17,000	$180,500

Ratable loss is that portion of a claim that falls within the per-claim accident limitation established by the state

State per-claim accident limits and split points for FL & GA listed are effective 1/1/19

Types of Deductible Programs

- A **gross** deductible program prescribes that the gross reported incurred amounts are to be used in the experience rating calculation. The entire gross loss (incurred indemnity & medical) is used to promulgate the experience rating modification
- A **net** deductible program prescribes that losses net of any deductible reimbursement are used in the experience rating calculation

Deductible Type	Total Loss Amount	Deductible Reimbursement	Claim Value in Mod
Gross	$5,000	$2,500	$5,000
Net	$5,000	$2,500	$2,500

- States vary on whether they use a gross or net deductible program

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When Will Mod Factor Be Revised?

- Changes from preliminary to final status
- Receipt of payroll or loss correction reports
- Receipt of missing data for a previously contingent modification
- Changes in Ownership
- Reclassification of a risk
- Transfer of experience from a Professional Employer Organization's (PEO's) mod to stand alone workers compensation coverage

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Why Experience Rating Mod Factors Change

- Changes in the employer's loss experience
- Changes in payroll amounts (increase or decrease)
- Changes in the Experience Rating Plan – such as ERA
- Changes in the average benchmark industry experience:

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Summary

- The larger the premium size, the more reliable the actual record is in predicting future losses (premium eligibility threshold)
- The cost of an injury may vary over a very large range
- The cost is less predictable than the fact than an injury occurred (addressed with the use of primary and excess loss components)

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Why Does Your Mod Matter?

- Poor performance equates to a debit modifier, resulting in higher premium
- A higher mod may limit insurability in the voluntary market leaving the assigned risk pool as the only option
- A higher mod may prevent bidding eligibility and opportunities
- A higher mod may limit profits and potential growth

Why Does Your Mod Matter?

- Good performance equates to a credit modifier, and results in lower premium
- A lower mod results in lower premium
- A lower mod = more profit, ability to be more competitive and more opportunity to grow the business
- A lower mod may result in more bidding opportunities
- A lower mod presents a better risk, inclining more markets to compete for the business

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Questions?

Implications of Return To Work Programs

- Reduce future premium increases
- Reduce claim costs more than 50%
- Return injured workers to their regular jobs faster
- Faster recovery
- Reduce fraud

Implications of Return To Work Programs

- Reduce litigation
- Limit personnel costs
- Maintain efficiency and productivity
- Increase employee morale

Is There a Benefit to Not Reporting Claims?

- No.
- Timely reporting of claims gives you;
  - The ability to control the claim
  - Reduce unnecessary treatment
  - Avoid fines and penalties
  - Decrease overall costs
  - Avoid litigation expense
  - Enhances possible subrogation

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Questions?

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When It’s Over and It’s Time to Tailgate!

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