

BOARD OF DIRECTORS MEETING (OPEN)

AGENDA ITEM 18a

ATTACHMENT 18a-I

WORKERS' COMPENSATION INSURANCE RATING BUREAU (WCIRB)  
PRESENTATION: CALIFORNIA EXPERIENCE RATING PLAN OVERVIEW

PRESENTED BY: Dave Bellusci, WCIRB

March 13, 2009

Workers' Compensation Insurance Rating Bureau of California

# **California Experience Rating Plan Overview**

Presented by:  
Dave Bellusci  
WCIRB of California

State Fund  
Board of Directors Meeting  
March 13, 2009

**WCIRB**California®

## California Experience Rating Plan Overview

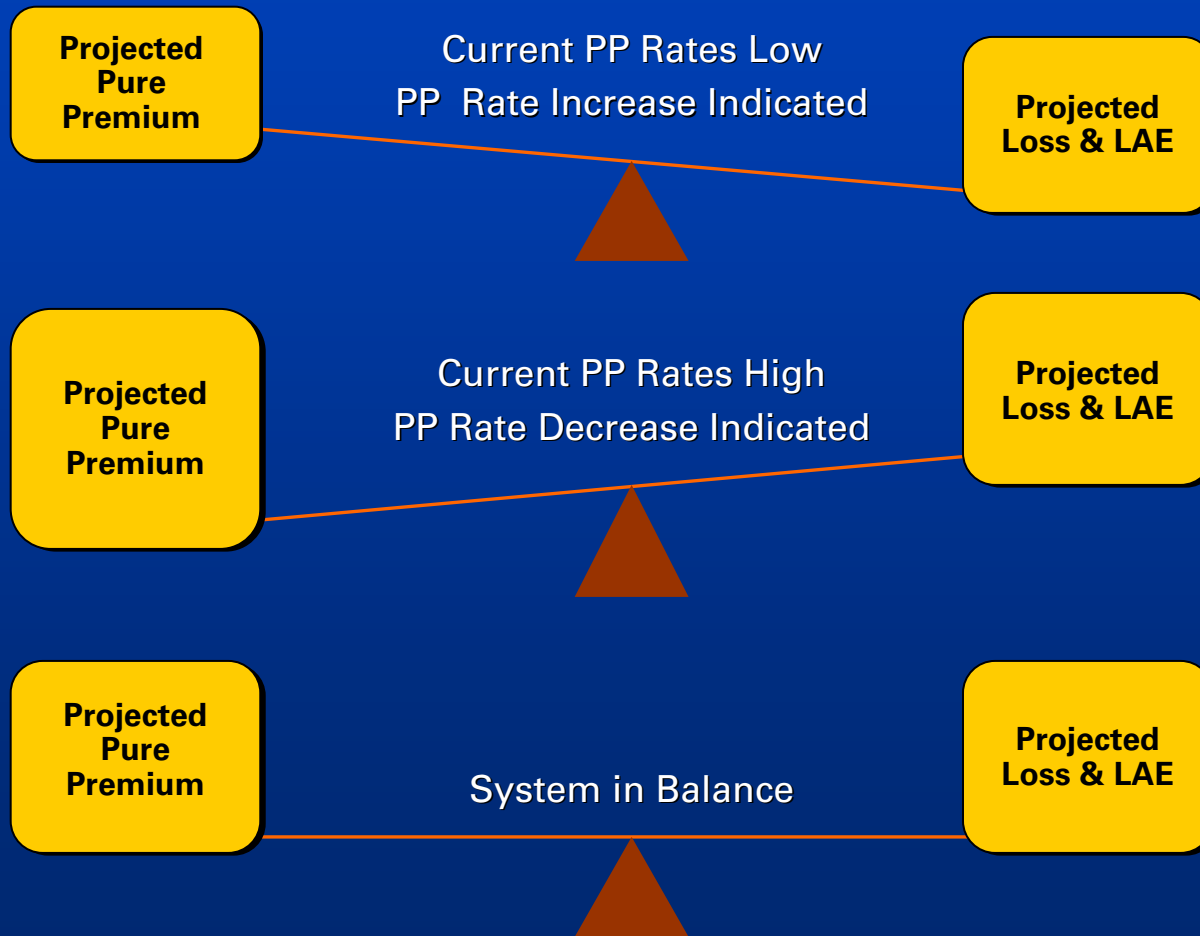
# WCIRB Ratemaking Process

- Overall Pure Premium Rate Level Change
- Classification Pure Premium (PP) Rates
- Experience Rating

# California Experience Rating Plan Overview

## WCIRB Ratemaking Process

### Overall Pure Premium Rate Level Change



## California Experience Rating Plan Overview

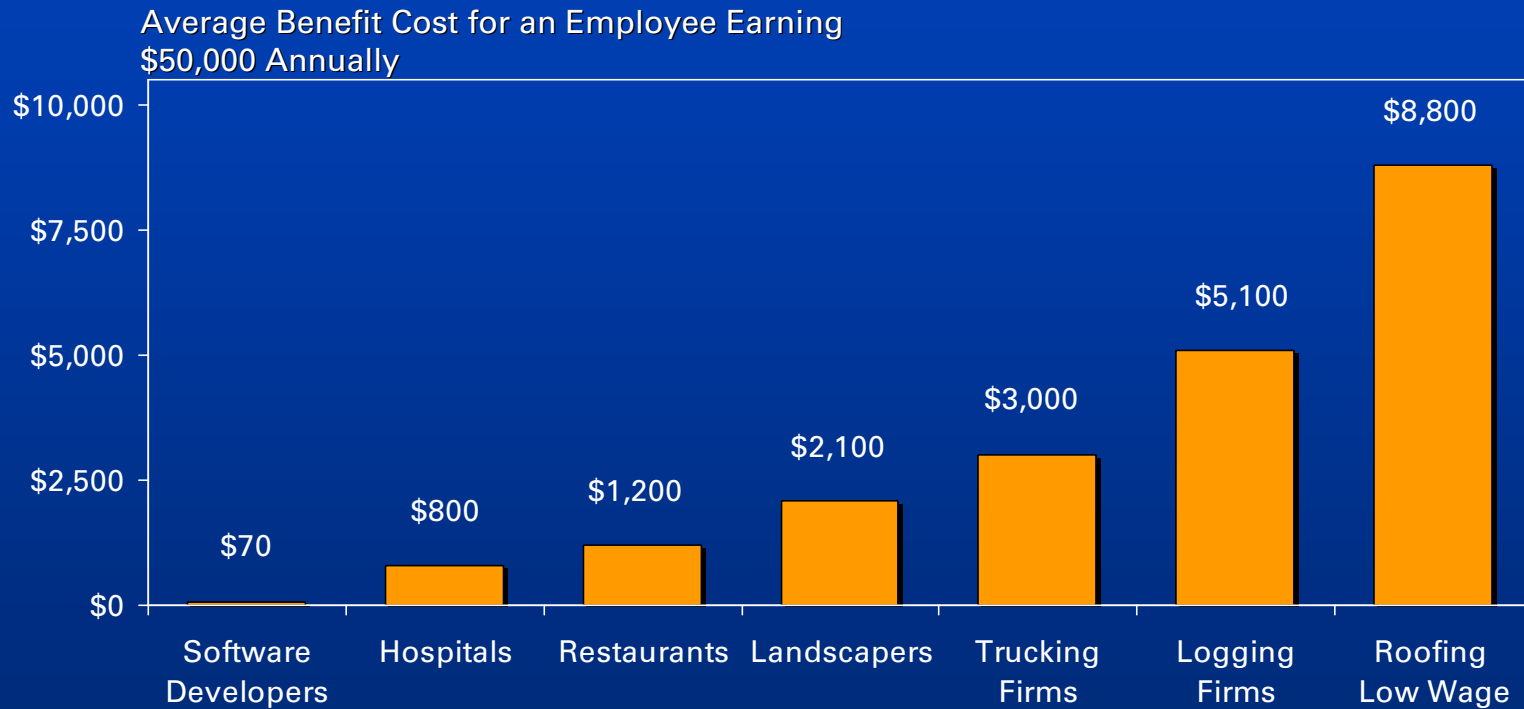
# WCIRB Ratemaking Process Standard Classification System

- Approved by Insurance Commissioner
- Approximately 500 Industry Classifications
- Mandatory for Data Reporting
- Advisory for Insurer Pricing
- Critical for Ratemaking Process
  - Many classifications with few large employers
  - Many small employers
  - Great cost variation by classification

# California Experience Rating Plan Overview

## WCIRB Ratemaking Process

### Classification Pure Premium Rates



## California Experience Rating Plan Overview

# Experience Rating Overview

## Statutory Objectives

- Contain Reasonable Eligibility Standards
- Provide Adequate Incentive for Loss Prevention
- Provide Sufficient Premium Differentials to Encourage Safety

## California Experience Rating Plan Overview

# Experience Rating Overview

## Other Supporting Objectives

- Distribute Costs of System Equitably Among Employers in an Industry Classification
- Simplicity
- Predictability
- No Impact on Overall Statewide Premium
- Consistency Across Jurisdiction

## California Experience Rating Plan Overview

# Experience Rating Overview

## Statutory Definition

- Contained in Section 11730 of the California Insurance Code

*“rating procedure utilizing **past insurance experience** of the individual policyholder to **forecast future losses** by measuring the policyholder’s loss experience against the loss experience of **policyholders in the same classification** to produce a prospective premium credit, debit or unity modification.”*

## California Experience Rating Plan Overview

# Experience Rating Overview

## Statutory Definition

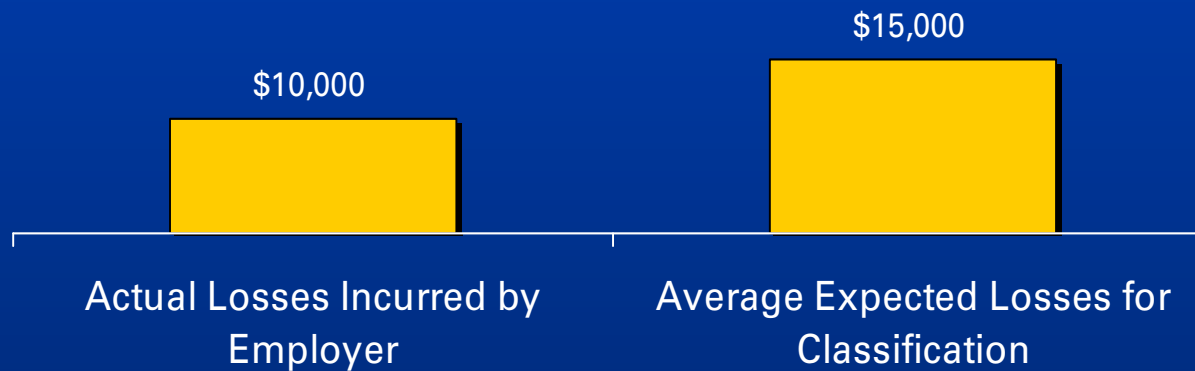
- Measuring Policyholders' Past Experience Against the Experience of Policyholders in the Same Classification
- Produce a Prospective Premium Credit, Debit or Unity Modification

# California Experience Rating Plan Overview

## Experience Rating Overview

### Actual Losses Vs. Expected Losses

Actual Losses < Expected Losses : X-Mod <100%

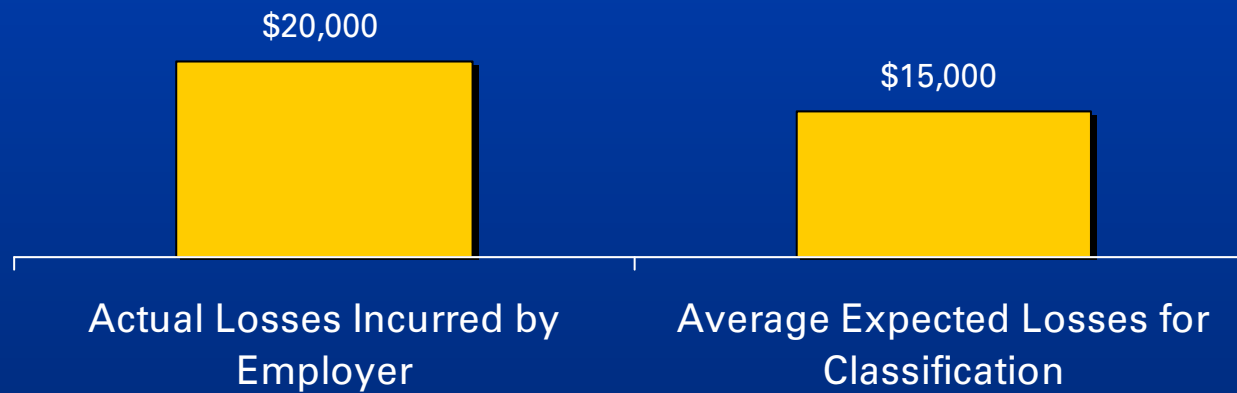


# California Experience Rating Plan Overview

## Experience Rating Overview

### Actual Losses Vs. Expected Losses

Actual Losses > Expected Losses : X-Mod >100%



## California Experience Rating Plan Overview

# Experience Rating Overview

## Statutory Definition

- Measuring Policyholders' Past Experience Against the Experience of Policyholders in the Same Classification
- Refinement of Classification System
- Classifications Fairly Homogeneous but With Differences
  - Operations (level of mechanization)
  - Safety practices
  - Salary levels
  - Employee relations (e.g. degree of unionization)
  - Availability of other benefits
  - Other characteristics (e.g. location)

## California Experience Rating Plan Overview

# Experience Rating Overview

## Statutory Definition

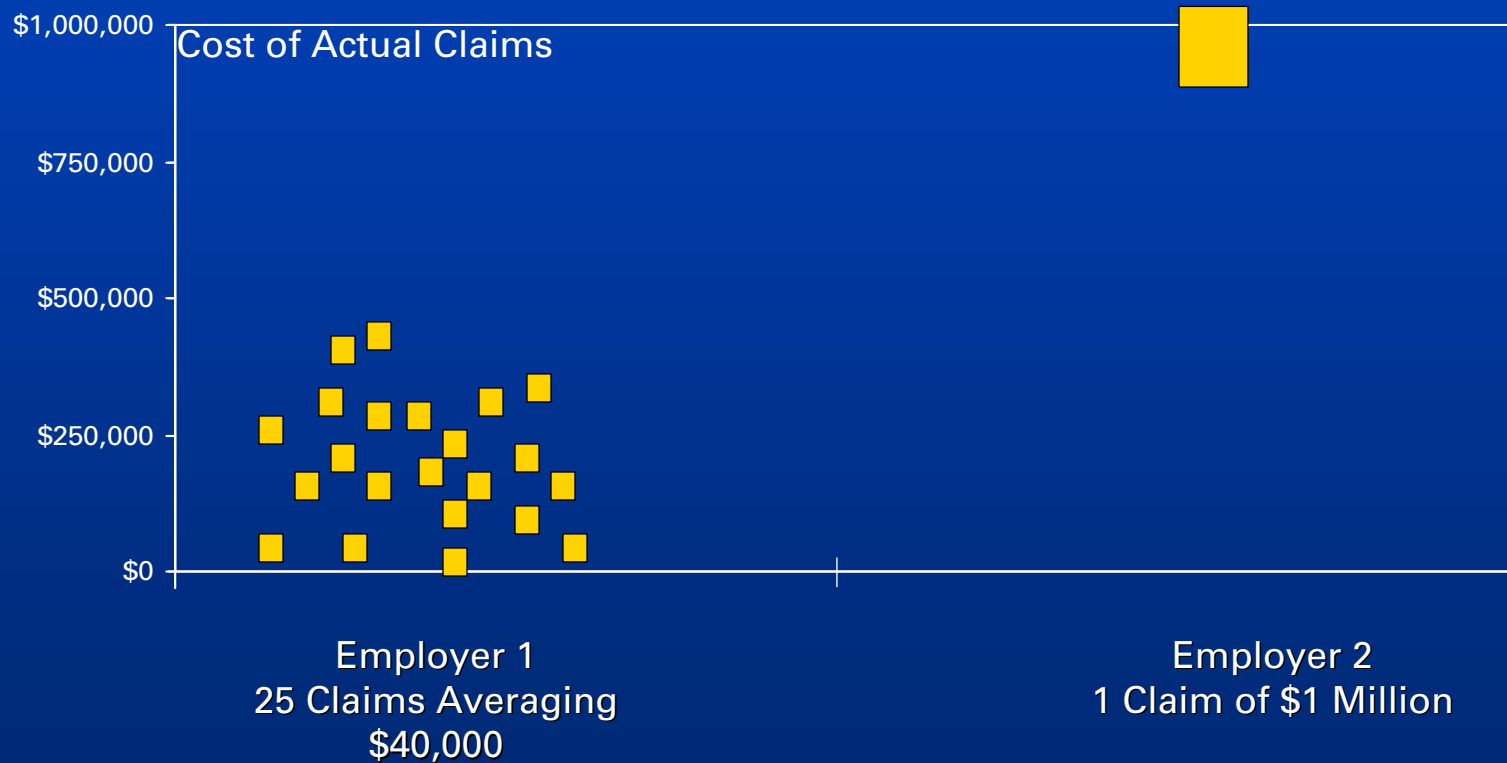
- Forecast of Future Losses
- Not a Proxy for Safety
- Past Experience Used to Extent it is Predictive of Future Losses
  - Greater reliance on claim frequency than severity
  - Predictive value depends on size of employers
  - Very small employers not eligible for experience rating

# California Experience Rating Plan Overview

## Experience Rating Overview

### Past Experience as a Predictor of Future Losses

#### Frequency Vs. Severity

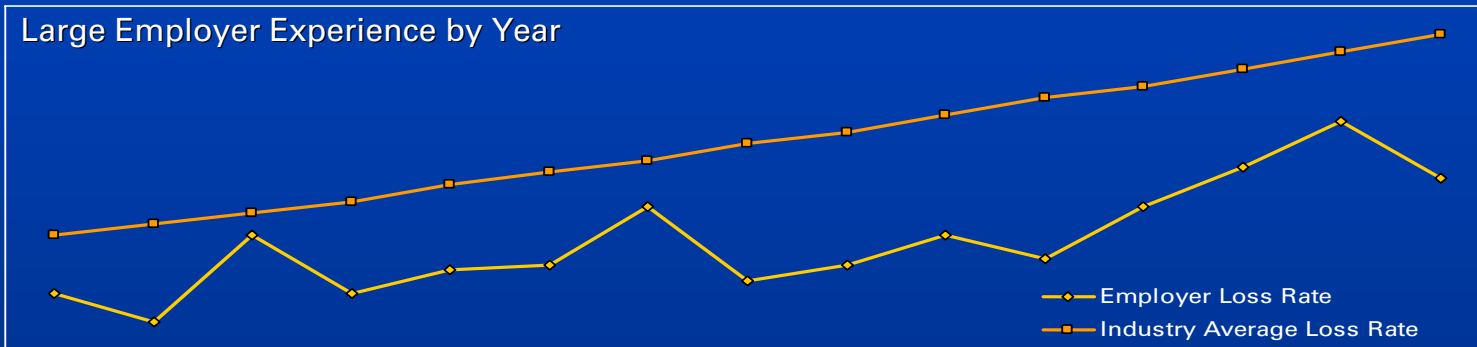


# California Experience Rating Plan Overview

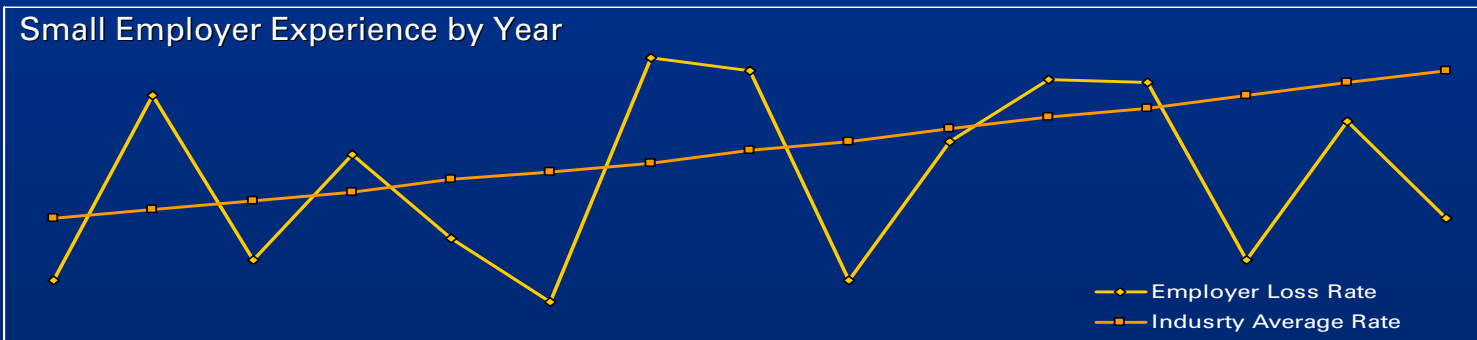
## Experience Rating Overview

### Past Experience as a Predictor of Future Losses

#### Role of Employer Size



X  
Predicted  
Loss Rate



X  
Predicted  
Loss  
Rate

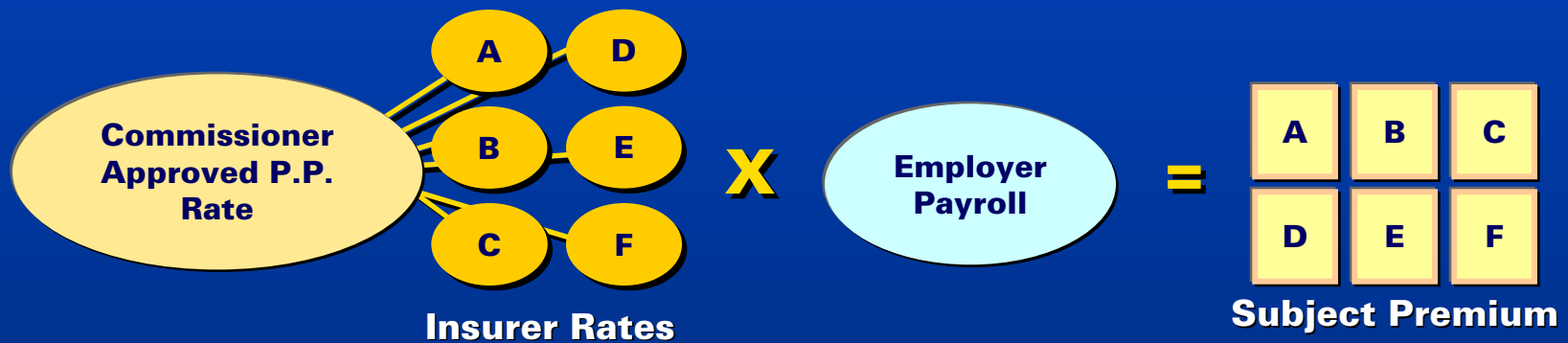
## California Experience Rating Plan Overview

# California Experience Rating Plan Summary

- Introduced in California in 1921
- Approved by the Insurance Commissioner
- Comparison of 3-Year Actual Incurred Loss History to Average Expected for Classification
- Application of Published X-Mod is Mandatory Under Insurance Code 11734
- Approximately 20% of Policies are Experience Rated, Representing Approximately 85% of the Premium
- Approximately 120,000 X-Mods issued annually

## California Experience Rating Plan Overview

# California Experience Rating Plan Application of X-Mod



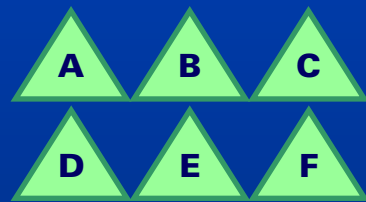
## California Experience Rating Plan Overview

# California Experience Rating Plan Application of X-Mod



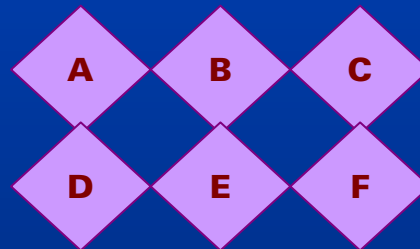
## California Experience Rating Plan Overview

# California Experience Rating Plan Application of X-Mod



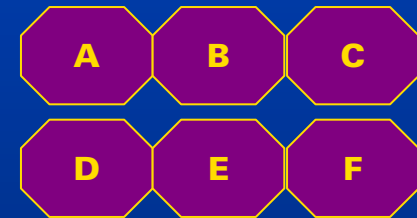
**Modified Premium**

**X**



**Individual Insurer Rating  
Plan Adjustments**

**=**



**FINAL PREMIUM**

## California Experience Rating Plan Overview

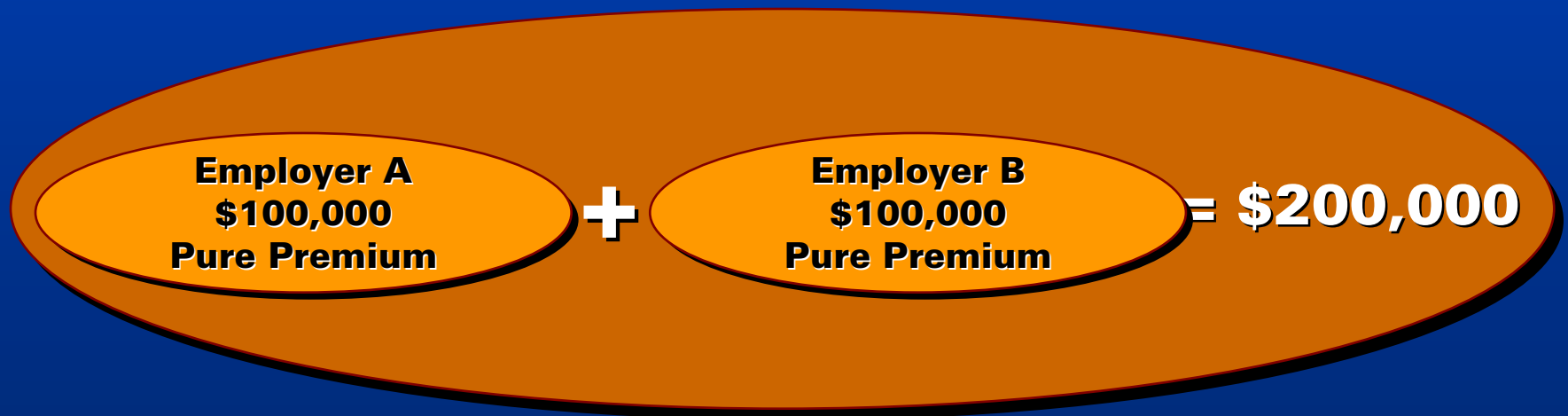
# California Experience Rating Plan General Purpose

- Experience Rating Benchmarks a Business Against Others in its Industry
  - It provides a direct financial incentive for employers to reduce accidents
  - It is intended to distribute the cost of workers' compensation insurance equitably among employers in an industry classification

## California Experience Rating Plan Overview

# California Experience Rating Plan General Purpose

- Distributing the Cost of Workers' Compensation
  - Two employers in the same classification code
  - Each develops \$100,000 in pure premium

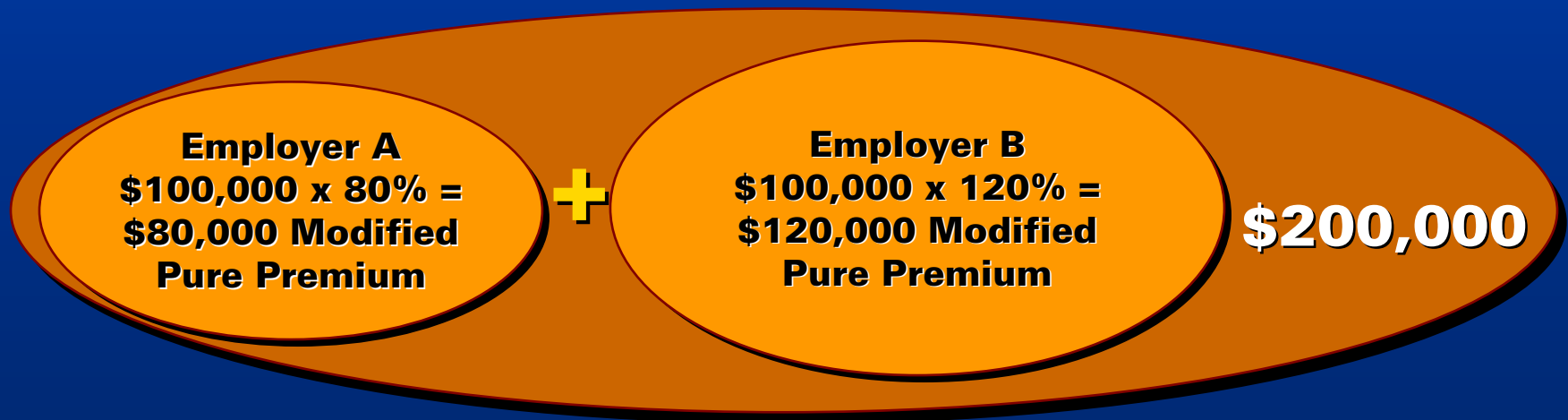


**Pool of Workers' Compensation Insurance Pure Premium**

## California Experience Rating Plan Overview

# California Experience Rating Plan General Purpose

- Distributing the Cost of Workers' Compensation
  - If Employer A has a favorable loss history compared to Employer B, Employer B's X-Mod would increase to offset the decrease in Employer A's so that the industry modified pure premium remains the same or "premium neutral."



**Pool of Workers' Compensation Insurance Pure Premium**

## California Experience Rating Plan Overview

# California Experience Rating Plan Eligibility

- All California Insured Employers with Minimum Qualifying Premium (Approximately 120,000)
- Qualifying Premium Based on Payroll During the Experience Period and Current Pure Premium Rates
- For Average Classification, Eligibility is 6 Full-Time Employees Over 3 Year Experience Period
  - Varies depending on the classification pure premium

# California Experience Rating Plan Overview

## California Experience Rating Plan Eligibility

### Experience Rating Eligibility

Number of Full-Time Employees (Earning \$50,000 Annually)  
Needed to Meet Experience Rating Eligibility



## California Experience Rating Plan Overview

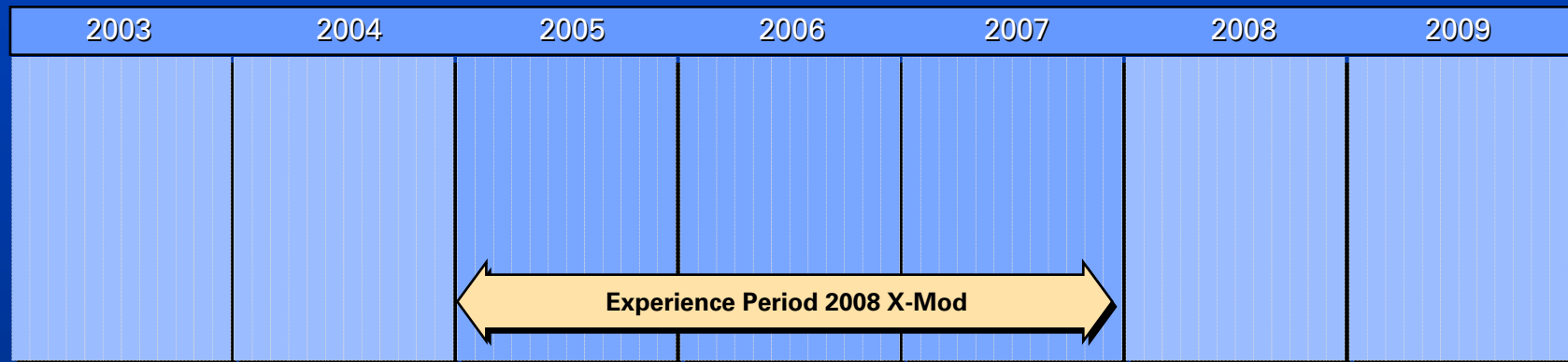
# California Experience Rating Plan Experience Period

- Typically 3 Year Experience Period
- Typically Most Current Policy in Experience Period Expired 12 months Prior to the X-Mod Effective Date
  - 2009 ratings reflect 2005, 2006 and 2007 policies

# California Experience Rating Plan Overview

## California Experience Rating Plan Experience Period

### Experience Used



Experience period losses valued

January 1, 2009 X-Mod Published by WCIRB

January 1, 2009 X-Mod Effective Date

## California Experience Rating Plan Overview

# California Experience Rating Plan Loss and Payroll Experience Used

- Uses Data Submitted Under Uniform Statistical Reporting Plan (USRP) approved by the Insurance Commissioner
- Audited Payroll by Classification
- Loss Amounts Reflect Incurred Loss Estimates as of Most Current USRP Valuation
- Individual Claims Limited to \$175,000

## California Experience Rating Plan Overview

# California Experience Rating Plan Expected Losses

- Based on Audited USRP Payroll and Expected Loss Rates by Classification Approved by Insurance Commissioner
- Expected Loss Rates Reflect Average Losses by Classification for Period Used in Calculation
  - 2009 expected loss rates reflect average losses estimated by class for 2007 policies (valued at 18 months), 2006 policies (valued at 30 months) and 2005 policies (valued at 42 months)

## California Experience Rating Plan Overview

# California Experience Rating Plan X-Mod Calculation Formula

- X-Mod Based on the Ratio of Actual Losses to Expected Losses for Experience Period
- Formula Reflects Actuarial Adjustment for Predictive Value Based on Size of Claim and Size of Employer
- Individual Losses Segregated into “Primary” and “Excess” Components
- X-Mods are Corrected for Erroneous Unit Statistical Data or Changes in Claim Activity (E.G. Subrogation)
  - Re-rates if claims in aggregate close for 60% or less of value used in x-mod computation
  - Approximately 18,000 re-rates annually

## California Experience Rating Plan Overview

# Experience Rating Task Force

- Created at Directive of Insurance Commissioner
- Objective to Review How Well Experience Rating Plan Meets its Principal Objectives
- Includes Representatives of Insurers, Employers, Labor, Producers, CDI & WCIRB
- Reviewed Principal Aspects of Experience Rating System
- Report Submitted to CDI in July 2008

## California Experience Rating Plan Overview

# Experience Rating Task Force

## Principal Recommendations

- Single Primary/Excess Loss Split Plan
- Update Rating Values with Most Current Available Data
- Simplify Plan Formula
- Enhanced Expected Loss Rate Projection Methodology
- New Experience Rating Worksheet
- Broad Educational Outreach Program
- Implementation Plan
  - Substantive calculation changes to be proposed effective 1/1/10
  - Worksheet changes to be proposed effective 1/1/11
  - Broad outreach program to be undertaken

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