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| In the Matter of<br>Workers' Compensation Insurance Rate<br>Application of the New York<br>Compensation Insurance Rating Board | : | **OPINION AND DECISION** |

On May 13, 2016, an application for an overall loss cost increase of 9.3% was submitted to the Department of Financial Services (Department) by the New York Compensation Insurance Rating Board (NYCIRB). In accordance with Insurance Law § 2305, which requires a hearing whenever a loss cost increase of 7% or more is proposed, and pursuant to notice in the State Register, a public hearing concerning NYCIRB's loss cost filing (Filing) was held on June 28, 2016, at the Department's State Street office in New York City (Hearing). The Superintendent of Financial Services (Superintendent), with assistance from certain of her staff, presided over the Hearing, which was convened for the purpose of determining whether to approve the Filing.

NYCIRB'S FILING

NYCIRB, licensed pursuant to Insurance Law § 2313, serves as the private rate service organization for New York State workers' compensation insurers. Consequently, all workers' compensation insurers that write business in New York report statistical information to NYCIRB. NYCIRB compiles and evaluates the data and proposes loss cost changes, which require the Superintendent's approval prior to implementation.

In the Filing, NYCIRB sought an overall loss cost increase of 9.3%. NYCIRB's request featured changes resulting in new values for certain multiplicative factors in its loss cost calculation: loss experience, as measured by two policy years of data, with a factor of 1.068; an overall trend factor valued at 1.016; the factor for loss adjustment expense valued at 1.005; and the factor for the impact of legislative and regulatory changes that raised the maximum weekly benefit amounts valued at 1.005. NYCIRB applied those factors in its loss cost calculation to arrive at its 9.3% figure.

PUBLIC HEARING

Nine people testified at the Hearing: Ziv Kimmel of NYCIRB; Kenneth Munnelly of the Workers' Compensation Board; Elizabeth Heck of the Greater New York Insurance Companies; Thomas Nowak of AIG Property Casualty Group; Robert Grey of the New York Workers' Compensation Alliance; Nadia Marin-Molina of the New York Committee for Occupational Safety and Health; Kelly McLaughlin of The Hartford Insurance Group; Nancy Treitel-Moore of Liberty Mutual; and Ken Pokalsky of the Business Council of New York.

Mr. Kimmel testified about the actuarial analysis NYCIRB performed in support of the Filing. He discussed the actuarial analysis underlying the Filing, the implementation of a new actuarial procedure to construct common rating modification factors for historical policy years to fit the current year environment and to better predict future costs, the rationale for using a five-year period to calculate the trend factor, and the impact of benefit level changes.

Mr. Kimmel testified that the proposed loss cost level increase is based on the latest data reported by the rating board member carriers and reflects the application of accepted actuarial principles and methodologies. He explained further that the experience used in the Filing reflects post-2007 reforms data as adjusted to reflect the impact on loss development by the revised benefits structure implemented as part of such reforms. Mr. Kimmel testified that such adjustments had been reviewed thoroughly by NYCIRB's Actuarial Committee. Mr. Kimmel explained further that NYCIRB conducts validation of the data provided by use of a rigorous testing and validation process. This is followed up with extensive communication between NYCIRB and its member carriers to ensure the data is reliable. As a result, NYCIRB determined that the 9.3% requested increase was necessary in order to balance the tension between fair rates for policyholders and maintaining a competitive workers' compensation system in which the premiums collected are adequate to satisfy accurately determined loss cost levels.

Mr. Kimmel also testified that schedule rating – whereby carriers are permitted to vary rates up to 5% – is a useful pricing tool that affords flexibility. He noted such flexibility is helpful to attract competition into the market.

Mr. Munnelly testified that the Workers' Compensation Board had solicited input from representatives from business, labor unions, workers, and carriers for the purpose of constructing the most valuable recommendations for improving the workers' compensation system. While some recommendations might be made possible through the Workers' Compensation Board enacting administrative changes, most require legislative action.

Mr. Munnelly testified that the Workers' Compensation Board supported approval of the Filing. He also explained that the Workers' Compensation Board had supported the Governor's reform package in the 2016/2017 Executive budget, which would have mitigated the rate increase proposed this year. He pointed out that such reform package would have provided significant changes to the claim process, and would have sped the provision of medical care and the return of financial benefits to workers. It would have also provided benefits to public and private employers by reducing assessments, eliminating mandatory deposits into the aggregate trust fund, improving municipalities' access to public self-insured pools, and freeing up $3 billion to self-insured employers throughout New York State.

Mr. Munnelly further explained that the Workers' Compensation Board is pressing forward with administrative improvements. These include a medical portal to speed treatment requests, virtual hearings, and a redesigned claim information system. He expects the effects of these efforts to be seen by the end of 2016 or early 2017. Because the cost of operating the workers' compensation system is borne ultimately by employers, such improvements might provide some much needed relief to those employers. Notwithstanding such efforts, Mr. Munnelly noted that administrative improvements would only provide limited benefits and legislative solutions are still very necessary.

The next two witnesses, representing private carriers writing New York workers' compensation business, also testified in support of the Filing. Ms. Heck testified that rising claim and medical costs, combined with an extended period of low interest rates, require a loss cost increase. The essence of her testimony was that the proposed rate increases are necessary to make the market competitive by attracting insurers, which would benefit policyholders as they shop for the best coverage available at fair rates. She testified further, as did other insurers, that the failure to match premiums to loss costs would harden the market as insurers retreated from writing workers' compensation coverage. That would leave only the State Insurance Fund (SIF) available to satisfy a disproportionate share of the market. Mr. Nowak testified that the Filing is supported by standard actuarial analysis and is essential for maintaining a vibrant, innovative and competitive marketplace in which the participating carriers' solvency is preserved.

Mr. Grey and Ms. Marin-Molina testified in opposition to NYCIRB's application. Mr. Grey questioned the validity of the data and assumptions underlying the Filing, but acknowledged that he is not an actuary. As an attorney who represents claimants, he expressed concerns about his clients having to enter unfavorable settlements. Ms. Marin-Molina spoke about misclassification of low wage earners and employer abuses in the workers' compensation system, and asserted that an increase in loss costs might encourage employers to continue dishonest practices.

The final three witnesses, Mr. McLaughlin, Ms. Treitel-Moore and Mr. Pokalsky, provided testimony in support of the Filing. Mr. McLaughlin testified that he sits on NYCIRB's Underwriting Committee and its Board of Governors. He stated that NYCIRB is comprised of a number of differing constituents, including insurance, labor and business members. He explained that, after a full discussion of the issues, each of NYCIRB's Underwriting Committee and Board of Governors approved the rate increase with limited opposition. He also expressed The Hartford's support for the proposed rate increase. Ms. Treitel-Moore stated that Liberty Mutual chose to reduce its New York writings in part due to inadequate loss costs. Ms. Treitel-Moore also testified that having actuarially sound loss costs is a particularly important condition for having a competitive marketplace in states, like New York, with less pricing flexibility. Ms. Treitel-Moore discussed a number of market practices that have driven up loss costs in the workers' compensation system. While she made those points to explain why an increase is necessary to match loss costs, such points also argue for the legislative reforms necessary to adjust the current loss cost environment.

Mr. Pokalsky testified that costs of the workers' compensation system should be accurately reflected in the loss costs, and that these systemic costs should be reduced legislatively and administratively. He stated that it would be better to wait until legislative changes affect the experience than to estimate what savings might be achieved in the future. While noting his institution is not pleased with the need for increased loss cost levels, he acknowledged that the Business Council of New York believes firmly these numbers must reflect the true cost of the workers' compensation system and supports NYCIRB's application for a rate increase. Mr. Pokalsky also noted the need to consider reforms so that New York's workers' compensation system will not be in a perpetual state of deficit. He expressed his organization's ultimate wish to see a workers' compensation system that will support a healthy competitive environment for the growth of business in New York State.

None of the witnesses provided an actuarial analysis refuting NYCIRB's request in the Filing. In addition, no witness testified in favor of an increase of any percentage other than the percent increase included in the Filing.

## WRITTEN SUBMISSIONS

In addition to the public testimony presented at the Hearing, the Department received written submissions in connection with the Hearing. Mr. Grey, Ms. Marin-Molina, Ms. Heck, and Mr. Nowak provided written submissions in connection with their testimony. In addition, Lev Ginsburg of the Business Council of New York provided a written submission supporting Mr. Pokalsky's testimony, and Mr. Kimmel provided a written submission in further support of the Filing and to address Mr. Grey's testimony regarding NYCIRB's actuarial assumptions and expertise.

Scott Lefkowitz, a partner at Oliver Wyman Actuarial Consulting, Inc., and a fully credentialed actuary, provided a written submission noting that following the 2007 reforms loss costs increased significantly and stressed that the Filing pertained to meeting actual loss costs. The critical points of that submission are that the Filing seeks an increase that reflects actual workers' compensation costs in New York and that initiatives should be undertaken to address the level of loss costs in the workers' compensation system.

The Business and Labor Coalition of New York and the New York State AFL-CIO each provided a brief written submission opposing the Filing because of the potential impact the rate increase might have on employers and workers. Neither commented on the loss cost calculations.

None of the written submissions provided an actuarial analysis refuting NYCIRB's request in the Filing. In addition, none of the written submissions argued in favor of an increase of any percentage other than the percent increase included in the Filing.

## DISCUSSION

Careful analysis of the technical aspects of the Filing was conducted by Department staff, which consisted of actuaries and market experts. Results of that analysis are set out below as they correspond to the various sections of the Filing.

### A. Loss Experience by Policy Year

In this revision, NYCIRB has submitted case basis loss experience for Policy Years 2013 and 2014. The submission shows a loss cost indication for Policy Year 2013 of +4.9% and a loss cost indication for Policy Year 2014 of +8.7%. Both indications rely on premium and loss development factors and on-level factors to project data to ultimate values and adjust data to the current loss cost level, respectively. Such factors must be evaluated each year to assure that they are reasonable projections of past development patterns, and appropriate to apply to the current data.

This task has been complicated by the gradual inclusion of reserves reflecting the reforms implemented in 2007. Among other changes, those reforms imposed duration caps on non-scheduled permanent partial disability (PPD) cases, closed the Special Disability Fund (SDF) to claims occurring on or after July 1, 2007, required the implementation of medical treatment guidelines, and allowed employers and carriers to establish mandatory networks for pharmacy and diagnostic testing. Subsequent changes that should also be considered include the January 2012 implementation of Loss-of-Earning-Capacity Guidelines by the Workers' Compensation Board and the closure of the Reopened Case Fund (RCF) to new claims as of January 1, 2014.

For the portion of PPD losses estimated to reflect caps limiting the duration of an award, the indemnity loss development pattern was accelerated to reflect the lower anticipated development for these claims. Conversely, reflection of the closure of the SDF and the RCF require an increase to the projected ultimate losses to reflect the shift of losses that previously could be ceded to these funds back to insurers. NYCIRB adjusted losses by 6.2% to account for its current estimate of the impact of the elimination of the RCF. This differs from the 4.5% provision approved in the 2013 and 2015 loss cost filings, which were based upon data through 2012. The Department considered the difference and, based upon data since last year, encompassing the period 2013 through 2015, determined that the increase to 6.2% is a reasonable adjustment at this time.

B. Loss and Wage Trend Factor

The trend factor is based on a review of exponential regression lines of claim costs and frequencies fit to the latest five available policy years of data. Wage data are analyzed separately, and the severity trends are shown separately for indemnity and medical claims. The indemnity and medical claim frequencies are identical, as only lost time claims are considered in the claim frequency analysis. The indemnity and medical indications are combined using a weighted average based on Policy Year 2014 ultimate on-level losses.

Loss trend data comes from policy year financial data valued as of December 31, 2015 submitted to NYCIRB. Data from private carriers (excluding large deductible experience) and the

SIF are separately adjusted to an ultimate settlement basis, and brought to current levels. Regression lines are fit to the combined private carrier and SIF data.

The wage factor accounts for rising payrolls, which exceed the corresponding increase in exposure to loss. The wage factor is based on published annual Department of Labor statistics from the historical experience period, as well as projections made in the New York State Assembly's 2016 Economic Report to trend from the historical to the prospective experience periods. Finally, the wages in the prospective period were increased by 1.15% to account for the increase in the minimum wage effective December 31, 2016.

The filed indemnity severity trend has significantly increased from the indication from last year's filing, while the medical claim cost trend has moderated somewhat when compared to last year's indication. The filed claim frequency trend is identical to the indication from the 2015 loss cost filing.

C. Loss Adjustment Expense

The loss adjustment expense (LAE) provision was based on developing an ultimate ratio of paid Defense and Cost Containment Expense (DCCE) to paid losses, and on a review of historical calendar year ratios of paid Adjusting and Other Expense (AOE) to paid losses. Private carrier financial data excluding large deductible experience on both policy year and accident year bases were used to determine the DCCE provision, while the AOE provision was based on a review of Insurance Expense Exhibit data. The selected DCCE provision of 0.093 was based on an average of the latest three years of policy year and accident year ultimate ratios of paid DCCE to paid loss. A five year average of calendar year ratios of AOE to paid losses of 0.061 was selected as the AOE provision.

The change in the LAE factor from 1.148 to 1.154 results in an increase of 0.5% to the loss cost level.

D. Legislative and Regulatory Changes

The only legislative change considered in the Filing is the increase in maximum weekly indemnity benefits. As of July 1, 2010, the maximum weekly benefit for injured workers was set to two-thirds of the statewide average weekly wage (SAWW) with additional annual revisions effective July 1 of each subsequent year tied to the change in the SAWW. The statewide average weekly wage is determined by the New York State Department of Labor. The maximum weekly benefit will increase from $844.81 to $864.32 for accidents occurring on or after July 1, 2016, and is assumed to increase by 2.5% on July 1, 2017 and by 4.1% on July 1, 2018. NYCIRB estimates the loss cost impact of these actual and anticipated indemnity benefit changes from October 1, 2015 to average +0.5% over the prospective experience period.

E. Catastrophes

In January 2015, the Terrorism Risk Insurance Program Reauthorization Act of 2015 (TRIPRA) extended the federal backstop for terrorism through December 31, 2020. The loss cost provision for terrorism was increased to $0.045 per $100 of payroll as part of the October 1, 2015 loss cost filing. The current loss costs for natural disasters and catastrophic industrial accidents is $0.008 per $100 of payroll. For these hazards, payroll is a better reflection of risk than premium, as the exposure to these hazards appears to be independent of the inherent risk of a given employment.

Despite the increased carrier retentions required by TRIPRA, NYCIRB did not file for any changes in these factors.

## DECISION

A healthy, balanced workers' compensation system is important for the health of New York's economy and is necessary to provide an efficient process for employers and employees alike to have an effective resolution method for accidents that occur in the workplace. This process requires funding, which is not infinite. The Department recognizes the costs of increased funding on employers in this state as well as the strain that inadequate funding places on carriers writing workers' compensation insurance. We must ensure that all stakeholders in the workers' compensation insurance system are treated equitably, and that efforts are undertaken to improve the process.

Witnesses who appeared at the Hearing testified that approval of the Filing is necessary to maintain the balance of the workers' compensation system. However, other testimony opposed the Filing for a variety of reasons. The Department's experts carefully considered the matter, including the Filing, testimony and written submissions.

The testimony at the Hearing was illuminating in several respects. First, the Business Council of New York State, which is New York State's largest statewide employer association, whose members will bear the burden of increased premium levels, supports an increase. Second, several witnesses explained that reforms implemented in 2007 have been met with practices that have driven up loss costs in the workers' compensation system. It is clear that legislative reforms are necessary, at a minimum, to address such practices and mitigate the current loss cost environment. Third, several insurers confirmed in their testimony the simple economic principle that carriers will withdraw from the market when faced with unprofitable business, which limits consumers' options. Finally, two witnesses testified about alleged abuses within the workers' compensation system, which are concerning and may merit attention as a matter of enforcement, but do not undermine the bases for the Filing.

In 2007, legislative reforms were enacted with the intent to make the workers' compensation system more efficient and decrease the funding that it requires to be effective. As part of the 2007 reforms, the New York State Legislature updated benefits, and promulgated into law initiatives that were intended to create efficiencies. Those initiatives require adjustments over time as the workers' compensation system adjusts to the significant changes made. Those necessary adjustments came into focus with the passage of time.

Governor Cuomo has proposed statutory changes to the workers' compensation system, which would mitigate the loss cost increases presented at the Hearing. However, the Legislature declined to enact those necessary adjustments such that workers' compensation insurance rates must increase without the benefit of the Governor's proposed adjustments. Accordingly, with the benefit of the Department's analysis, as well as the testimony of the witnesses at the hearing, the Department concludes that legislation should be considered in order to limit the possibility of additional significant workers' compensation insurance rate increases in the future.

Based on the Department's review of relevant information, which included the Filing, the testimony provided at the Hearing, and the related written submissions, we find that NYCIRB's application should be approved as requested, with an effective date of October 1, 2016.

SUBMITTED AND RECOMMENDED:

Alexander Vajda
Principal Casualty Actuary

Maurice Morgenstern
Deputy Bureau Chief

ACCEPTED AND DETERMINED:

Maria T. Vullo
Superintendent