

State of Florida
Office of Insurance Regulation
Financial Services Commission

Actuarial Peer Review and Analysis of the
Ratemaking Processes of the National Council
on Compensation Insurance, Inc.

January 21, 2010



AMERICAN ACTUARIAL CONSULTING GROUP LLC

AMERICAN ACTUARIAL CONSULTING GROUP LLC
PROPERTY & CASUALTY INSURANCE CONSULTANTS

January 21, 2010

Mr. Kevin McCarty
Commissioner
Office of Insurance Regulation
200 East Gaines Street
Tallahassee, FL 32399

Dear Mr. McCarty:

American Actuarial Consulting Group LLC (“ACG”) is pleased to present the Florida Office of Insurance Regulation (“OIR”) with its report regarding the independent actuarial peer review and analysis of the ratemaking processes of the National Council on Compensation Insurance, Inc.

ACG appreciates the opportunity to be of service to OIR. Please do not hesitate to call us if you have any questions regarding our report.

Sincerely,



Charles Letourneau, FCAS, MAAA
President & Consulting Actuary



Joseph W. Pitts, FCAS, MAAA
Consulting Actuary

cc: Mr. James D. Watford, OIR

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■ EXECUTIVE SUMMARY

Introduction and Objectives

American Actuarial Consulting Group LLC (“AACG”) was retained by the Financial Services Commission (“Commission”) which oversees the Office of Insurance Regulation (“OIR”) of the State of Florida to perform an independent actuarial peer review and analysis of the ratemaking processes of the National Council on Compensation Insurance, Inc. (“NCCI”) in accordance with Section 627.285 of the Florida Statutes.

The specific objectives of this review, as outlined by the Commission, are as follows:

1. Conduct a peer review and analysis, in accordance with accepted actuarial practice and any standards for such analysis established by the Casualty Actuarial Society and/or the American Academy of Actuaries.
2. Status briefings, which may be conducted by teleconference, as requested by OIR.
3. Prepare a draft report which outlines the objectives and approach of the project; documents the data used, materials reviewed, assumptions and methodologies employed during the project including reference to any Actuarial Standards of Practice; and details of findings and recommendations, if any.
4. Prepare a final report, consistent with format and content described above.

The NCCI is the designated rating organization for workers’ compensation insurance in Florida. The NCCI collects data from Florida workers’ compensation insurance carriers through annual calls for experience and submits proposed rates to OIR for review and approval.

General Approach

In performing this study, AACG reviewed the methodology and assumptions used by the NCCI in the preparation of its recent workers’ compensation rate filings in Florida.

Specifically, the review and analysis procedure used by AACG can be summarized as follows:

1. Review the methodology and assumptions currently used by the NCCI.
2. Review the reasonableness of the methodology and assumptions and ensure compliance with actuarial standards and state laws.
3. Review recent changes in methodology and assumptions made by the NCCI.
4. Review the adjustments in methodology and assumptions made by the NCCI in order to incorporate savings generated by Senate Bill 50A (“SB 50A”).
5. Recommend changes in assumptions and methodology.

The methodology and assumptions used by the NCCI are discussed in the *Methodology Used by the NCCI* section of this report. AACG’s discussion and recommendations regarding certain aspects of the methodology and assumptions used by the NCCI are contained in the *Review and Recommendations* section of this report. In order to estimate the potential

remaining future savings associated with SB 50A, AACG adjusted the overall indicated rate change contained in the 2010 rate filing based on an alternate set of assumptions. AACG's analysis is contained in the *Impact on Overall Rate Change Indication* section of this report.

In performing its review and analysis, AACG requested and reviewed documentation and data from the NCCI and held teleconferences with OIR and the NCCI. The documentation and data which was relied upon by AACG is listed in the *Documentation and Data* section of this report.

Conclusions and Recommendations

Based on its peer review and analysis of the NCCI's ratemaking processes, AACG offers the following conclusions and recommendations:

1. The actuarial methodologies used by the NCCI are reasonable and comply with actuarial standards of practice. However, AACG believes that the assumptions made by the NCCI in connection with the selection of trends and loss development factors, starting with the 2005 rate filing through the 2008 rate filing, have led to indicated overall rate changes which have been excessive. For these rate filings, AACG found that the trends used by the NCCI have been consistently higher than the estimated trends and the loss development factors used by the NCCI have been consistently higher than the actual loss development factors. AACG found that the NCCI was slow in incorporating the savings generated by SB 50A in its assumptions.
2. The closure rate in Florida, defined as the ratio of the number of cumulative closed to reported claims, has increased significantly since SB 50A was passed in 2003. The NCCI did not make the appropriate adjustments to its loss development factor selection to reflect the faster closing of claims. This omission resulted in loss development factors which have been excessive, which in turn resulted in indicated trends which have been excessive. AACG believes that the loss development factors used by the NCCI should have been adjusted to directly reflect the higher closure rate, as recommended in the actuarial literature.
3. The calendar-accident year trends contained in the 2010 rate filing show a flattening of the frequency between 2007 and 2008. The exposure-accident year trends do not show such flattening. Based on information received from the NCCI, the calendar-accident year trends appear to be distorted by changes in the levels of audit premium, creating an artificial flattening of the frequency between 2007 and 2008. Since the exposure-accident year trends are not subject to such distortion, AACG believes that the exposure-accident year estimates provide a more appropriate basis from which trends should be selected.
4. The internal rate of return ("IRR") model used by the NCCI contains a weakness which may make the approach inappropriate for determining the profit and contingency provision in Florida. The weakness relates to the inclusion of a policyholder dividend in the IRR model. To the extent that some insurers do not pay a dividend, or pay a dividend which is lower than the provision used by the NCCI, the

profit and contingency provision estimated by the NCCI may be overstated for these insurers, resulting in rates which are excessive.

5. Based on information provided by the NCCI, Florida has the largest ratio of defense and cost containment expenses (“DCCE”) to losses in the country. Specifically, Florida had a calendar year ratio of paid DCCE to paid losses which was 44% higher and 56% higher, respectively for 2008 and 2007, than the countrywide ratio. AACG recommends that an independent study be performed to analyze the reasons and causes for the high ratio of DCCE to losses in Florida.
6. The NCCI currently relies on calendar-accident year data to calculate its overall rate change indication. Based on information presented by the NCCI, AACG believes that recent changes in the levels of audit premium adjustments may cause the overall rate change indication to be distorted. AACG recommends that the NCCI monitor the difference in overall rate change indications between the calendar-accident year approach and the policy year approach in future rate filings.
7. The NCCI has represented that, based on the lower levels of case reserves since SB 50A was passed, a decrease in case reserve adequacy has taken place. AACG believes that the lower levels of case reserves are not indicative of a decrease in case reserve adequacy but instead are the result of the faster closing of claims.

Report Distribution, Reliances, and Limitations

For this study, AACG relied on data and information compiled by the NCCI, without audit or independent verification.

This report was prepared on behalf of the Commission in order to fulfill the requirements of Section 627.285 of the Florida Statutes. This report should only be distributed in its entirety. The recipient of this report should place no reliance on the report, data, estimates, or conclusions contained herein that would result in the creation of any legal duty or obligation to the recipient or any other party.

The conclusions and estimates within this report are based on projections of the financial consequences of many future contingent events and are therefore subject to uncertainty. Future costs were developed from historical claim experience and covered exposure, with adjustments for anticipated changes. In addition to the assumptions stated in this report, numerous other assumptions underlie the calculations and results presented herein. There may have been abnormal statistical fluctuations in the past, and there may be such fluctuations in the future. In addition, economic, social, and legislative changes can have significant impacts on results. Because of these uncertainties inherent in the estimation of future costs, actual costs may vary significantly from the estimates.

This report is intended to express an opinion regarding AACG’s independent actuarial peer review and analysis of the ratemaking processes of the NCCI. This report is not intended to express an opinion regarding the adequacy of workers’ compensation insurance rates used by carriers in Florida, past or present.

■ METHODOLOGY USED BY THE NCCI

Overview

The methodology used by the NCCI to derive proposed rates for each occupational classification can be summarized in three major steps; Calculation of overall indicated rate change, allocation of overall indicated rate change to industry groups, and allocation of industry group indicated rate change to occupational classifications. The NCCI also calculates rating values which are used in the experience and retrospective rating plans.

Calculation of Overall Indicated Rate Change

Summary

The NCCI's methodology for calculating an overall rate change indication relies on the average of eight separate projections of indemnity losses, medical losses, and loss adjustment expenses. The eight separate projections are based on the projection of paid and paid plus case reserves ("paid+case") losses for two separate accident years, and separately for the standard and large deductible policies.

Paid losses include the cumulative losses paid through the valuation date. Paid+case losses add the case reserves set by claim adjusters as of the valuation date to the paid losses. Therefore, projections based on paid losses rely on higher age to ultimate loss development factors than projections based on paid+case losses since paid losses are lower than paid+case losses.

The NCCI uses the two most recent accident years of data to calculate the overall indicated change in loss costs. Indicated changes in the loss and the loss adjustment expense components are separately estimated and then combined in order to obtain the overall indicated change in rates.

The basic methodology used to obtain the overall indicated change in rates is to divide the developed and trended losses adjusted for changes in benefit levels by the adjusted and on-level standard earned premium. This ratio is then compared to the targeted loss ratio to determine the overall indicated rate change.

Premium Adjustments

The premium used in the overall rate change indication is the calendar year standard earned premium for all policies in the state. The standard premium is adjusted to the current rate level, adjusted to remove the expense constant, and adjusted to reflect the average experience modifier in the state.

Loss Adjustments

Loss Development Factors

The indemnity and medical losses are developed to ultimate by applying loss development factors to the amounts valued as of the latest valuation date. The purpose of the loss development factors is to bring the losses for a specific accident year from the current amount to the amount which will have been paid once all claims for that accident year have been reported and closed. The loss development factors are separately estimated for the indemnity and medical losses, for the paid and paid+case amounts, and for standard and large deductible policies. The loss development factors are selected based on an average of the last two years of data. The tail factor, which is used to bring the losses from the last valuation point to ultimate, is estimated primarily based on the review of changes in calendar year carried ultimates.

Changes in Benefits

The indemnity and medical losses are separately adjusted for historical changes in benefit levels. An adjustment factor is estimated by dividing the current benefit level by the average benefit level for each accident year. The indemnity and medical losses for each accident year are brought to current benefit levels through the application of the adjustment factor.

Loss Based Expenses

Loss adjustment expenses are those expenses which are incurred in connection with the adjustment of losses. The two major components are DCCE and adjusting and other expenses ("AOE"). A ratio of DCCE and AOE to losses is selected by reviewing the countrywide experience over multiple years. The countrywide ratio of DCCE to losses is increased to reflect the actual ratio of DCCE to losses in Florida. A loss adjustment expense factor is calculated by adding the DCCE and AOE provisions and is separately applied to the indemnity and medical losses.

Trends

Trend factors are used to adjust for year-to-year changes in indemnity and medical costs, other than changes in benefit levels. The trend factors are calculated net of wage inflation levels, since workers' compensation premiums are calculated by applying rates to payroll amounts which usually grow over time. The trend factors are estimated separately for the indemnity and medical losses by reviewing the historical changes in ultimate ratios of losses to on-leveled premium. The trend factors reflect changes in claim frequency (number of claims per unit of exposure) as well as changes in claim severity (cost of a claim). The trend factors are selected by the NCCI based in part on a review of historical calendar-accident year and exposure-accident year loss ratios based on the projection of paid and paid+case indemnity and medical losses. The trends are applied to the indemnity and medical losses to reflect the changes in costs between the experience period to the average date of loss of the new policy period.

Indicated Loss Ratio

Indicated loss ratios are calculated separately for the standard and large deductible policies, and for the last two accident years using the paid and paid+case development methods, resulting in eight separate indicated loss ratios. Each indicated loss ratio is calculated by dividing the developed and trended indemnity and medical losses, adjusted for benefit changes and including loss adjustment expenses, by the on-level and adjusted earned premium. An average loss ratio is calculated for the standard and large deductible policies by taking a simple average of the four indicated loss ratios from the paid and paid+case development methods from the last two accident years. An overall indicated loss ratio is then calculated by taking a weighted average of the indicated loss ratio of the standard and large deductible policies. The weights are based on the net premium in each category.

Targeted Loss Ratio

The targeted loss ratio is used as a comparison basis with the indicated loss ratio to determine if current rates need to be increased or decreased. It is calculated by estimating the proportion of each premium dollar which is used for indemnity losses, medical losses, and loss adjustment expenses as compared to the proportion which is used for other insurance company expenses, including the provision for profit and contingency.

The expense provision provides for the following four categories of expenses:

- Production expenses
- General expenses
- Taxes, licenses, and fees
- Profit and contingency

The production expenses are composed primarily of commission and brokerage fees, and other acquisition expenses. The provision for production expenses is calculated based on countrywide data contained in the Insurance Expense Exhibit. The provision is based on a three year average of production expenses incurred to direct written premium.

The general expenses include all expenses incurred by insurance companies, other than production expenses, loss adjustment expenses, and taxes, licenses, and fees. The provision for general expenses is calculated based on countrywide data contained in the Insurance Expense Exhibit. The provision is based on a three year average of general expenses incurred to direct earned premium.

The provision for taxes, licenses, and fees is composed primarily of the premium tax and the Special Disability Trust Fund provision, and excludes federal income taxes. The provision for taxes, licenses, and fees is based on actual costs.

The profit and contingency provision is based on an internal rate of return model which is discussed below.

The targeted loss ratio is calculated as follows:

- 1 - Production Expenses Provision
- General Expenses Provision
- Taxes, Licenses, and Fees Provision
- Profit and Contingency Provision
- = Targeted Loss Ratio

Proposed Overall Rate Change Indication

The proposed overall rate change indication is calculated by dividing the overall indicated loss ratio by the targeted loss ratio. A ratio of more than 1.0 indicates that rates should be increased while a ratio of less than 1.0 indicates that rates should be decreased.

Profit and Contingency Provision

The NCCI uses an internal rate of return methodology to estimate its profit and contingency provision.

The IRR methodology used by the NCCI models all cash flows associated with a set of insurance transactions and discounts them to the present in order to assess the profit and contingency provision. The modeled cash flows originate with the purchase of a hypothetical insurance policy. The premium and operating expenses associated with the hypothetical policy are modeled based on the anticipated timing of premium collections and expense payments. The future expected loss and loss adjustment expense payments are modeled based on an expected payout pattern of future expected loss occurrences originating from the hypothetical policy. Investment income from the loss reserves and unearned premium reserves associated with the hypothetical policy are reflected in the IRR methodology. The model does not, however, include the impact from investment income related to loss and unearned premium reserves as they relate to prior written policies. The model also does not include investment income earned on the existing policyholder surplus.

The anticipated insurance cash flows contained within the IRR methodology are based on several assumptions. Expense provisions and investment return assumptions based on a hypothetical insurer were included in the model. The model also includes a provision for expected dividend payment to policyholders.

Allocation of Overall Indicated Rate Change to Industry Groups

The NCCI uses a methodology which relies primarily on losses in order to allocate the proposed overall rate change to each of the five industry groups; Manufacturing, contracting, office & clerical, goods & services, and miscellaneous. The methodology relies on a comparison of actual to expected losses for each industry group in order to obtain industry group differentials. This methodology uses five years of loss experience in Florida and no weight is given to out of state experience.

The NCCI made a few minor changes to the industry group allocation methodology starting with the 2010 rate filing. Specifically, the new methodology includes the following changes:

- Large claims are limited to \$500 thousand for each single claim occurrence and \$1.5 million for each multiple claim occurrence.
- The losses are developed to ultimate by applying limited loss development factors and an excess factor.
- The full credibility standard was increased from a range of 7,000 to 11,000 lost time claims to 12,000 lost time claims for each industry group.

Allocation of Industry Group Indicated Rate Change to Occupational Classifications

The methodology used to allocate the indicated rate change of each industry group to the underlying occupational classifications relies on a three-way credibility weighting approach. The following three sets of pure premiums are weighted in order to obtain a formula pure premium for each classification:

- Indicated pure premium
- Present on-level pure premium
- National pure premium

The indicated pure premium is calculated by using five years of loss experience in Florida. The present on-level pure premium is based on the adjusted pure premium component underlying the current rates, adjusted for the proposed rate change. The national pure premium is adjusted to Florida's state conditions.

An iterative process, called the test correction factor, is used in order to balance the rates by classification to the overall indicated rate change. The ratio of manual to standard premium by industry group is applied and the pure premiums are then loaded for expenses, profits, and disease loading in order to obtain the rate for each classification.

The NCCI applies swing limits to the proposed changes in rates for each classification. The proposed change in rates for each classification is limited to a range of 20% around the underlying rate change for the industry group.

The NCCI implemented changes to its class ratemaking methodology, starting with the 2010 rate filing. Some of the most important changes are as follows:

- The loss development factors are selected separately for the "likely to develop" and "not likely to develop" categories instead of the former "serious" and "non-serious" categories.
- Large claims are limited to \$500 thousand for each single claim occurrence and \$1.5 million for each multiple claim occurrence.
- "Serious" and "non-serious" pure premium components no longer exist and have been replaced by the indemnity and medical components.
- The full credibility standards for the indicated and national pure premiums have been modified.

Experience Rating Plan

Experience rating is used to adjust the premium paid by an employer based on a comparison of historical claim experience with other employers in the same industry group. Experience rating provides an incentive for loss prevention and loss mitigation as the premium adjustments are based on an employer's own loss experience. In Florida, participation in the experience rating plan is mandatory for employers with an annual premium of \$10,000 within the last two years or an average of \$5,000 for more than two years.

Experience rating is applied in the calculation of an employer's premium through the use of an experience modification factor. For an employer, the experience modification factor is calculated by dividing the adjusted actual losses by the adjusted expected losses. The adjusted actual losses consist of the sum of actual primary losses, weighted average of actual and expected excess losses, and ballast. The adjusted expected losses consist of the sum of total expected losses and ballast. The actual and expected losses are calculated based on three years of experience for that employer. The weight and ballast used in the calculation of the experience modification factor are based on, and increase with, the level of total expected losses.

The expected losses are calculated by applying an expected loss rate to the payroll in each classification code. Expected primary losses are then calculated by applying the discount ratio to the expected losses in each classification code. Actual losses are based on the incurred value of an employer's claims. Actual primary losses are calculated based on the first \$5,000 of each claim.

AACG's review of the experience rating plan was limited to a review of changes in rating values over the last three years.

Retrospective Rating Plan

The premium for a policy written under the retrospective rating plan is adjusted based on the amount of losses incurred during the policy premium. The retrospectively adjusted premium is usually subject to a minimum and maximum amount. An excess loss factor is used to limit the amount of losses from a single occurrence which are used in the calculation of the adjusted premium. Excess loss factors vary by limit and by hazard group.

AACG's review of the retrospective rating plan was limited to a review of changes in rating values over the last three years.

■ REVIEW AND RECOMMENDATIONS

Overview

Based on AACG's peer review and analysis of the ratemaking processes used by the NCCI, AACG believes that the actuarial methodologies used by the NCCI to calculate the overall indicated rate change, the allocation of overall indicated rate change to industry groups, and the allocation of industry group indicated rate change to occupational classifications are appropriate, reasonable, and comply with actuarial standards of practice. Also, AACG did not find abnormal changes in the rating values used in the experience and retrospective rating plans.

However, AACG believes that the assumptions made by the NCCI in connection with the selection of trends and loss development factors have led to overall indicated rate changes in Florida which have been excessive. AACG found that, starting with the 2005 rate filing through the 2008 rate filing, the trends used by the NCCI have been consistently higher than the estimated trends and the loss development factors used by the NCCI have been consistently higher than the actual loss development factors. AACG found that the NCCI was slow in incorporating the savings generated by SB 50A in its assumptions.

Data regarding the closure rate in Florida shows that the closing of claims accelerated after SB 50A was passed. This acceleration in the closing of claims resulted in loss development factors which have gradually declined. However, the NCCI did not make the appropriate adjustments to its selected loss development factors to reflect the faster closing of claims. This omission also resulted in indemnity and medical trends which are overstated, since the loss development factors are applied to the losses before the trends are selected by the NCCI. The result is a double impact on the overall rate indication as both the trends and loss development factors became overstated.

In addition to a discussion of loss development factors and trends, this section also includes a discussion of the NCCI's profit and contingency provision, defense and cost containment expense ratio, and policy year data.

Loss Development Factors

Since SB 50A was passed in 2003, the Florida paid and paid+case indemnity and medical loss development factors have experienced a gradual decline while the closure rate, defined as the ratio of the cumulative number of closed to reported claims, has steadily increased. The increase in the closure rate indicates that SB 50A has shortened the average period of time required to close a claim. AACG believes that the increase in the closure rate is in large part due to the limits on attorney fees which were introduced through SB 50A.

Loss development factors are used by the NCCI to develop the indemnity and medical losses from an immature status to a mature status in the overall rate change indication and also in the analysis of trends.

The table below displays the historical closure rate in Florida for lost time claims only.

Historical Closure Rate (# of closed claims / # of reported claims)

Accident Year	Valuation Period				
	<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>
1996			84.1%	93.0%	94.8%
1997		69.3%	85.6%	90.8%	95.8%
1998	33.8%	68.0%	80.7%	91.4%	95.6%
1999	33.1%	66.1%	84.9%	92.6%	95.6%
2000	32.3%	68.0%	84.8%	91.9%	94.8%
2001	34.4%	69.8%	85.5%	91.8%	95.2%
2002	31.6%	70.1%	84.8%	92.2%	95.4%
2003	31.8%	71.0%	86.2%	92.7%	96.2%
2004	32.6%	74.1%	88.0%	94.4%	97.0%
2005	34.0%	75.7%	90.2%	95.2%	
2006	35.9%	79.2%	91.1%		
2007	36.8%	78.5%			
2008	36.8%				

An observation of each column in the above table shows that the closure rate has gradually increased since 2003. For example, 31.8% of reported claims were at a closed status as of the first valuation period in accident year 2003 and that closure rate now stands at 36.8% for accident year 2008. A review of accident years 2007 and 2008 shows that the closure rate appears to be stabilizing. This may be due to the closure rate having reached its natural maximum or may be due to the temporary impact of the Florida Supreme Court's decision in *Emma Murray vs. Mariner Health Inc. and ACE USA* which resulted in the elimination of the caps on attorney fees which were placed by SB 50A.

The increase in the closure rate has resulted in a decline in loss development factors. The tables below display the paid and paid+case indemnity and medical historical loss development factors, separately for the standard and large deductible policies.

Historical Loss Development Factors – Standard Policies

Accident Year	<u>Paid Indemnity</u>				Accident Year	<u>Paid Medical</u>			
	Development Period					Development Period			
	<u>1-2</u>	<u>2-3</u>	<u>3-4</u>	<u>4-5</u>		<u>1-2</u>	<u>2-3</u>	<u>3-4</u>	<u>4-5</u>
1996				1.100	1996				1.063
1997			1.197	1.092	1997			1.130	1.065
1998		1.496	1.206	1.096	1998		1.276	1.142	1.069
1999	2.901	1.520	1.219	1.092	1999	2.261	1.294	1.139	1.066
2000	2.974	1.514	1.186	1.087	2000	2.237	1.286	1.119	1.060
2001	3.018	1.481	1.171	1.093	2001	2.244	1.263	1.109	1.062
2002	2.886	1.436	1.184	1.086	2002	2.142	1.239	1.115	1.059
2003	2.619	1.402	1.163	1.085	2003	1.976	1.235	1.102	1.048
2004	2.487	1.377	1.153	1.072	2004	1.966	1.191	1.077	1.050
2005	2.433	1.332	1.131		2005	1.858	1.173	1.079	
2006	2.397	1.317			2006	1.776	1.167		
2007	2.461				2007	1.857			

Historical Loss Development Factors – Standard Policies

<u>Paid+Case Indemnity</u>					<u>Paid+Case Medical</u>				
Accident	Development Period				Accident	Development Period			
Year	1-2	2-3	3-4	4-5	Year	1-2	2-3	3-4	4-5
1996				1.028	1996				1.024
1997			1.073	1.030	1997			1.042	1.021
1998		1.204	1.066	1.044	1998		1.096	1.054	1.033
1999	1.638	1.230	1.102	1.032	1999	1.372	1.120	1.060	1.029
2000	1.629	1.200	1.084	1.035	2000	1.345	1.096	1.046	1.030
2001	1.559	1.192	1.089	1.031	2001	1.309	1.082	1.058	1.047
2002	1.463	1.193	1.077	1.033	2002	1.327	1.088	1.054	1.018
2003	1.425	1.175	1.057	1.027	2003	1.237	1.098	1.028	1.023
2004	1.356	1.129	1.055	1.005	2004	1.295	1.056	1.032	1.008
2005	1.308	1.102	1.045		2005	1.221	1.049	1.011	
2006	1.294	1.106			2006	1.156	1.036		
2007	1.343				2007	1.180			

Historical Loss Development Factors – Large Deductible Policies

<u>Paid Indemnity</u>					<u>Paid Medical</u>				
Accident	Development Period				Accident	Development Period			
Year	1-2	2-3	3-4	4-5	Year	1-2	2-3	3-4	4-5
1996				1.138	1996				1.097
1997			1.330	1.156	1997			1.201	1.106
1998		1.618	1.337	1.119	1998		1.312	1.229	1.088
1999	2.899	1.676	1.241	1.135	1999	2.321	1.361	1.133	1.071
2000	3.110	1.579	1.293	1.119	2000	2.404	1.337	1.138	1.081
2001	3.223	1.618	1.220	1.109	2001	2.460	1.312	1.142	1.067
2002	3.246	1.522	1.217	1.103	2002	2.324	1.259	1.113	1.075
2003	3.081	1.461	1.196	1.103	2003	2.247	1.230	1.116	1.058
2004	2.608	1.413	1.166	1.083	2004	2.071	1.225	1.084	1.043
2005	2.692	1.379	1.137		2005	2.051	1.175	1.064	
2006	2.623	1.327			2006	1.955	1.145		
2007	2.563				2007	1.932			

Historical Loss Development Factors – Large Deductible Policies

<u>Paid+Case Indemnity</u>					<u>Paid+Case Medical</u>				
Accident	Development Period				Accident	Development Period			
Year	1-2	2-3	3-4	4-5	Year	1-2	2-3	3-4	4-5
1996				1.062	1996				1.091
1997			1.180	1.091	1997			1.104	1.067
1998		1.366	1.134	1.066	1998		1.165	1.139	1.044
1999	1.899	1.321	1.143	1.081	1999	1.492	1.172	1.077	1.049
2000	1.896	1.369	1.149	1.064	2000	1.560	1.199	1.047	1.050
2001	1.946	1.341	1.121	1.079	2001	1.659	1.171	1.077	1.055
2002	1.890	1.306	1.122	1.069	2002	1.535	1.143	1.056	1.076
2003	1.884	1.241	1.122	1.053	2003	1.488	1.097	1.075	1.034
2004	1.605	1.232	1.085	1.032	2004	1.367	1.123	1.038	1.024
2005	1.679	1.182	1.075		2005	1.366	1.074	1.034	
2006	1.630	1.154			2006	1.306	1.058		
2007	1.623				2007	1.291			

The above tables clearly show a significant decline in indemnity and medical loss development factors since SB 50A was passed.

The NCCI did not appropriately adjust its loss development factor selection to reflect the faster closing of claims. This adjustment is required to reflect the fact that lower loss development factors should be used since a higher proportion of claims are closed, and, hence, less development should be expected in the future. This omission introduced a bias in the NCCI's loss development factor selection.

To illustrate the bias in the NCCI's loss development factor selection, the tables below compare the loss development factors selected by the NCCI in the 2007 and 2008 rate filings for the standard coverage with the actual loss development factors which emerged two years later, for the first four periods of development. The two year lag in comparison is to approximately account for the period between the accident year data used in the rate filings and the proposed policy periods.

Paid Indemnity – Standard	1-2	2-3	3-4	4-5
NCCI Selected 2007 Filing:	2.552	1.419	1.178	1.090
Actual with 2 Year Lag:	2.397	1.332	1.153	1.085

Paid Indemnity – Standard	1-2	2-3	3-4	4-5
NCCI Selected 2008 Filing:	2.461	1.390	1.174	1.089
Actual with 2 Year Lag:	2.461	1.317	1.131	1.072

Paid Medical – Standard	1-2	2-3	3-4	4-5
NCCI Selected 2007 Filing:	1.971	1.237	1.112	1.061
Actual with 2 Year Lag:	1.776	1.173	1.077	1.048

Paid Medical – Standard	1-2	2-3	3-4	4-5
NCCI Selected 2008 Filing:	1.912	1.214	1.109	1.061
Actual with 2 Year Lag:	1.857	1.167	1.079	1.050

Paid+Case Indemnity – Standard	1-2	2-3	3-4	4-5
NCCI Selected 2007 Filing:	1.369	1.177	1.082	1.033
Actual with 2 Year Lag:	1.294	1.102	1.055	1.027

Paid+Case Indemnity – Standard	1-2	2-3	3-4	4-5
NCCI Selected 2008 Filing:	1.333	1.153	1.067	1.032
Actual with 2 Year Lag:	1.343	1.106	1.045	1.005

Paid+Case Medical – Standard	1-2	2-3	3-4	4-5
NCCI Selected 2007 Filing:	1.248	1.088	1.056	1.039
Actual with 2 Year Lag:	1.156	1.049	1.032	1.023

Paid+Case Medical – Standard	1-2	2-3	3-4	4-5
NCCI Selected 2008 Filing:	1.259	1.078	1.041	1.033
Actual with 2 Year Lag:	1.180	1.036	1.011	1.008

Projections made by the NCCI consistently show paid projections which are higher than the paid+case projections. The NCCI believes that the difference is due to a weakening of the case reserves in Florida and that therefore the projections based on paid+case data will tend to understate actual costs. The NCCI bases its opinion on a review of various diagnostic ratios. AACG believes that the difference between the paid and the paid+case

projections is due to the NCCI's overstated loss development factor selection combined with the higher leverage associated with paid loss development factors, since the paid loss development factors are higher than the paid+case loss development factors. The data reviewed by AACG shows no evidence of weakening of the case reserves in Florida.

AACG believes that the NCCI did not make the appropriate adjustments to its selected loss development patterns to account for the increasing closure rate and declining loss development factors. Such adjustments are commonly used by actuaries and are widely discussed in the actuarial literature. The loss development factors selected by the NCCI since SB 50A was passed have contributed to the overstatement of overall indicated rate changes in Florida.

Trends

In order to reflect the impact of annual changes in claim frequency and claim severity, the NCCI selects trend factors which are used to adjust the loss data in the last two accident years to the level of losses expected in the new policy year.

The table below compares the exposure-accident year loss ratio trends which were estimated by the NCCI in the 2010 rate filing to the loss ratio trends selected by the NCCI in the rate filing for each year.

Indemnity Loss Ratio Trends						
	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
NCCI Estimated	-14.0%	-11.2%	-11.0%	-8.9%		
NCCI Selected	-2.0%	-2.0%	-4.0%	-6.5%	-8.2%	-7.0%

Medical Loss Ratio Trends						
	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
NCCI Estimated	-7.6%	-8.3%	-10.7%	-7.3%		
NCCI Selected	1.0%	0.5%	0.5%	-1.5%	-4.0%	-4.0%

The above table does not provide an exact match of estimated to selected trends since the estimated trends represent a one year change in loss ratios while the selected trends are applied by the NCCI over multiple years. For instance, the -14.0% estimated indemnity trend for 2005 represents the change in loss ratios between exposure-accident years 2004 and 2005 while the selected trend of -2.0% is the annual trend applied to the losses in accident years 2003 and 2002 in order to be adjusted to a policy year 2005 level.

A more appropriate approach for comparing the trends used by the NCCI to the estimated trends may be to compare trends which subsequently emerged to the trends used by the NCCI. The table below compares the trends used by the NCCI in its 2008, 2007, 2006, and 2005 rate filings to the loss ratio trends which were subsequently estimated by the NCCI.

1/1/2008 Rate Filing							
Accident	Indemnity			Accident	Medical		
<u>Year</u>	<u>Selected</u>	<u>Est. Yr+1</u>	<u>Est. Yr+2</u>	<u>Year</u>	<u>Selected</u>	<u>Est. Yr+1</u>	<u>Est. Yr+2</u>
2006	-6.5%	-11.0%	-8.9%	2006	-1.5%	-10.7%	-7.3%
2005	-6.5%	-11.2%	-11.0%	2005	-1.5%	-8.3%	-10.7%

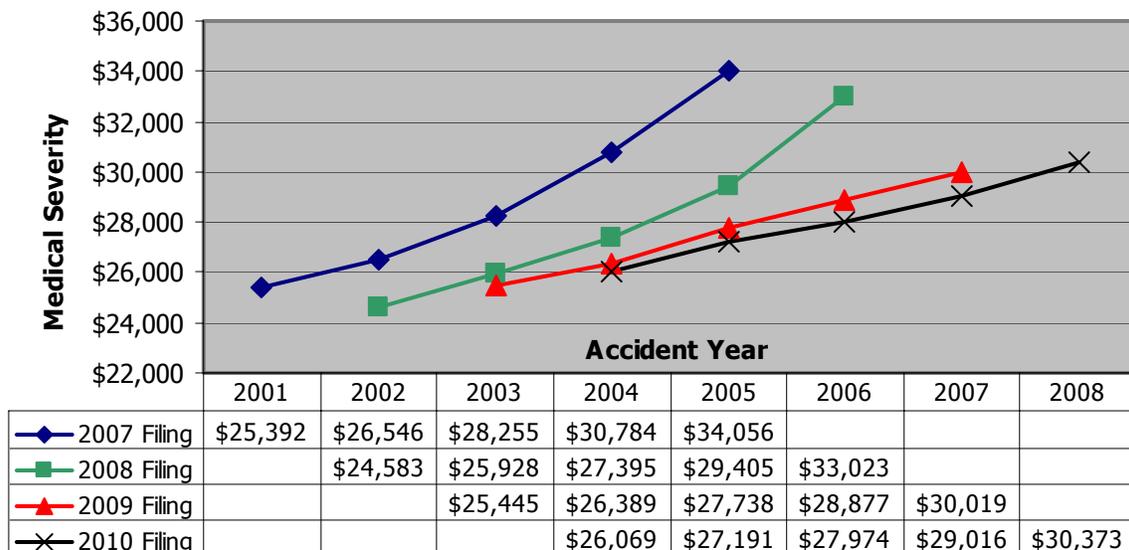
1/1/2007 Rate Filing							
Accident				Medical			
Year	Selected	Est. Yr+1	Est. Yr+2	Year	Selected	Est. Yr+1	Est. Yr+2
2005	-4.0%	-11.2%	-11.0%	2005	0.5%	-8.3%	-10.7%
2004	-4.0%	-14.0%	-11.2%	2004	0.5%	-7.6%	-8.3%

1/1/2006 Rate Filing							
Accident				Medical			
Year	Selected	Est. Yr+1	Est. Yr+2	Year	Selected	Est. Yr+1	Est. Yr+2
2004	-2.0%	-14.0%	-11.2%	2004	0.5%	-7.6%	-8.3%
2003	-2.0%	-12.5%	-14.0%	2003	0.5%	-10.8%	-7.6%

1/1/2005 Rate Filing							
Accident				Medical			
Year	Selected	Est. Yr+1	Est. Yr+2	Year	Selected	Est. Yr+1	Est. Yr+2
2003	-2.0%	-12.5%	-14.0%	2003	1.0%	-10.8%	-7.6%
2002	-2.0%	-8.4%	-12.5%	2002	1.0%	-2.6%	-10.8%

The above tables show that, on average, the trends used by the NCCI have been significantly higher than the estimated trends. For instance, the above table shows that the NCCI used an indemnity trend of -2.0% in its 2005 rate filing in order to bring losses from accident years 2003 and 2002 to a policy year 2005 level. The estimated trends, as compiled by the NCCI, show that for accident year 2003, the trend was -12.5% between 2003 and 2004 and -14.0% between 2004 and 2005.

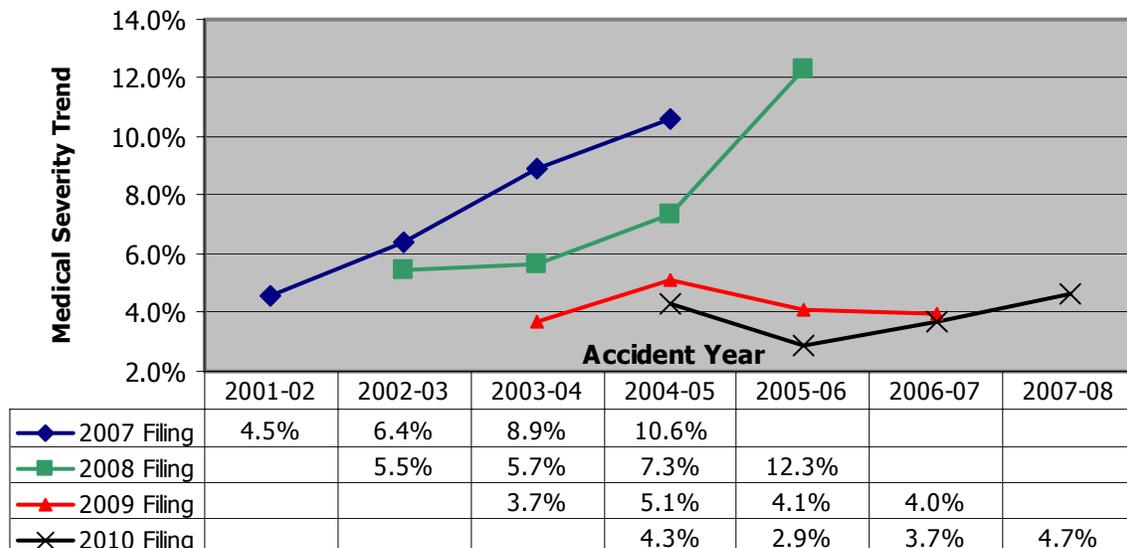
The chart below compares the NCCI's selection of ultimate medical severity in its 2007, 2008, 2009, and 2010 rate filings.



The above chart shows that the medical claim severities selected by the NCCI have consistently declined over time. For instance, the medical severity for accident year 2004

was estimated to be \$30,784 in the 2007 rate filing and is now estimated to be \$26,069 in the 2010 rate filing. The indemnity severities also show a similar decline. AACG attributes this decline in estimated indemnity and medical severities to the overstated loss development factor selection, as discussed in the previous section.

The decline in indemnity and medical severities also impacted severity trend levels since the severity curves have become flatter over time. The chart below compares the NCCI's estimated medical severity trends in its 2007, 2008, 2009, and 2010 rate filings.



The above chart shows that the medical severity trends estimated by the NCCI have consistently declined over time. For instance, the medical severity trend between accident years 2004 and 2005 was estimated to be 10.6% in the 2007 rate filing and is now estimated to be 4.3% in the 2010 rate filing. The decline in indemnity and medical severity trends similarly impacted the indemnity and medical loss ratio trends.

Since SB 50A was passed, the NCCI has selected indemnity and medical loss ratio trends which have consistently been higher than the estimated trends. This bias appears to have been impacted by the decline in loss development factors which have gradually lowered the estimated trends.

The consistent difference between the trends used by the NCCI and the estimated trends has contributed to the overstatement of indicated overall rate changes in Florida.

Profit and Contingency Provision

AACG believes that the IRR model used by the NCCI contains a weakness which may make the approach inappropriate for determining the profit and contingency provision in Florida. The weakness relates to the inclusion of a policyholder dividend in the IRR model. In its 2010 rate filing, the NCCI assumed that 5.6% of the premium would be paid to policyholders as a dividend. To the extent that some insurers do not pay a dividend, or pay a dividend

which is lower than the provision used by the NCCI, the profit and contingency provision estimated by the NCCI may be overstated for these insurers, resulting in rates which are excessive.

Notwithstanding the above weakness of the IRR model, in its 2010 rate filing, the NCCI selected a profit and contingency provision of 2.5% while the indicated provision based on its model was 10.99%.

Defense and Cost Containment Expense Ratio

Defense and cost containment expenses generally include payments related to defense, litigation, and medical cost containment. In its 2010 rate filing, the NCCI applied factors to the countrywide ratio of DCCE to losses in order to select its ratio of DCCE to losses for Florida. The application of factors to the countrywide ratio resulted in one year and two year Florida average ratios of 17.6% and 18.3%, which compare with a two year average countrywide ratio of 12.2%.

Based on information provided by the NCCI, Florida has the largest ratio of DCCE to losses in the country. Specifically, Florida had a calendar year ratio of paid DCCE to paid losses which was 44% higher and 56% higher, respectively for 2008 and 2007, than the countrywide ratio. AACG recommends that an independent study be performed to analyze the reasons and causes for the high ratio of DCCE to losses in Florida.

Policy Year vs. Calendar-Accident Year Data

The NCCI currently relies on calendar-accident year data to estimate its overall rate change indication. Under this approach, the premium used is on a calendar year basis while the losses are on an accident year basis. The calendar year premium is subject to distortions caused by changes in audit premium adjustments since the adjustments recorded in a specific year are generally from policies which were written in the prior year. To the extent that the level of audit premium adjustments fluctuates from year to year, a distortion is introduced in the ratemaking formula. Policy year premium is not subject to such distortion since the audit premium adjustments are recorded in the same year the policy was written.

Based on information provided by the NCCI, such distortion may be present in the calendar year premium for 2008. According to the NCCI, the economic downturn has caused the payroll in Florida to drop, resulting in lower audit premium adjustments which in turn results in lower calendar year earned premium. AACG believes that the varying levels of audit premium adjustments could cause the overall rate change indications to be distorted.

AACG recommends that the NCCI monitor the difference in overall rate change indications between the calendar-accident year approach and the policy year approach in future rate filings.

IMPACT ON OVERALL RATE CHANGE INDICATION

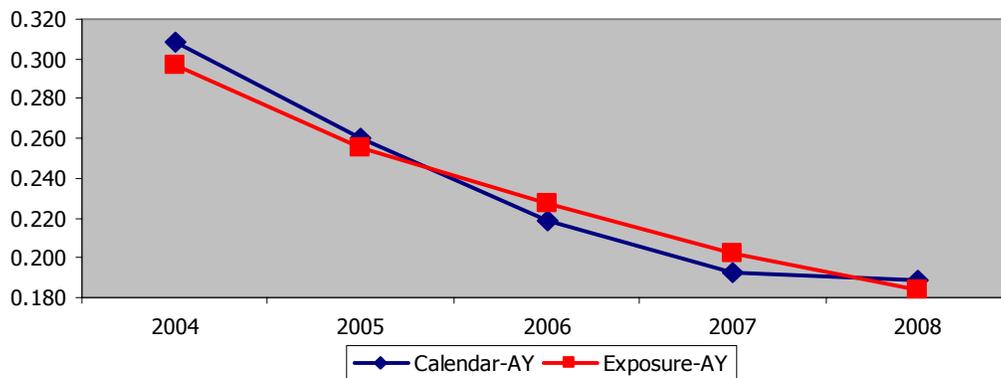
Summary

In order to estimate the potential remaining future savings associated with SB 50A, AACG adjusted the calculation of the overall rate change indication contained in the NCCI's 2010 rate filing. Specifically, AACG selected indemnity and medical trends as well as loss development factors which are lower than those used by the NCCI. All other aspects of the NCCI's methodology and assumptions were kept. Based on AACG's assumptions, the rate change indication was lowered from -6.8% to -23.2%, showing the potential for future rate decreases. AACG's estimated rate change should not be viewed as the basis for a recommended rate adjustment, but instead as an attempt to quantify the remaining impact of SB 50A on rates, should the observed trends for the period from 2003 to 2008 carry through policy year 2010.

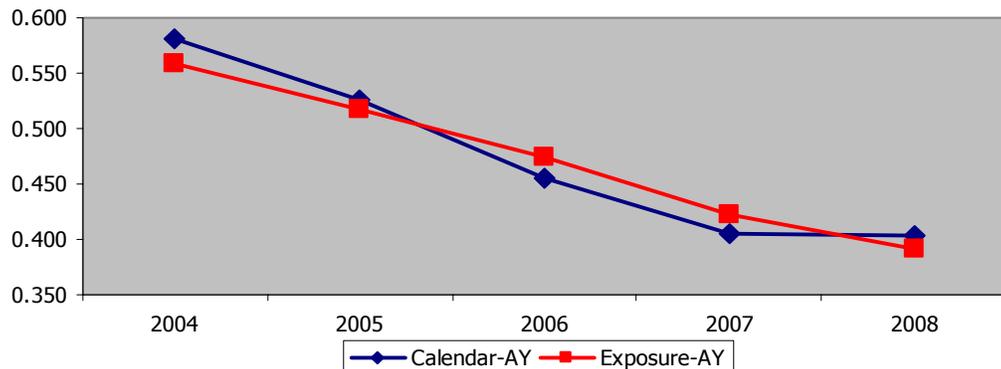
Trends

The NCCI selects its indemnity and medical loss ratio trends based in part on the review of historical loss ratio trends by calendar-accident year and exposure-accident year. The charts below compare the two sets of loss ratios for the indemnity and medical components.

Comparison of NCCI Indemnity Loss Ratio Estimates



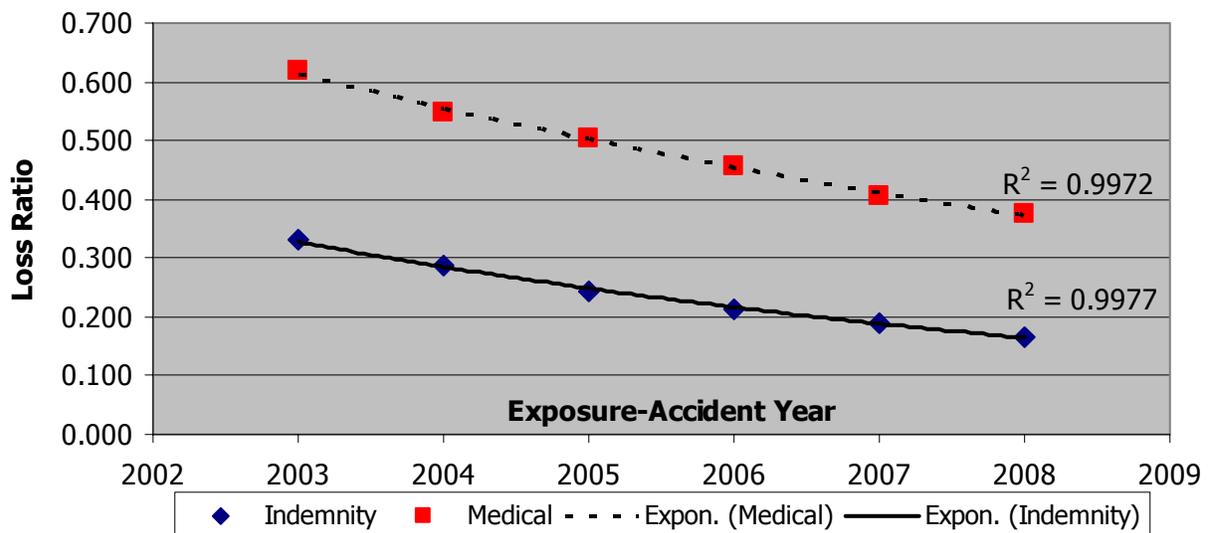
Comparison of NCCI Medical Loss Ratio Estimates



The above charts show that the indemnity and medical loss ratios appear to be flattening between 2007 and 2008 under the calendar-accident year approach, but show a continued decline under the exposure-accident year approach.

The calendar-accident year loss ratios are calculated by dividing the accident year adjusted ultimate indemnity and medical losses by the on-level calendar year earned premium. The exposure-accident year loss ratios rely on the same accident year losses, but use on-level exposure year earned premium instead of on-level calendar year earned premium. The exposure year earned premium is calculated by the NCCI by taking a weighted average of the policy year premium from the current and prior year. The exposure-accident year approach provides a better matching of the premium and losses for trending purposes. Also, based on information provided by the NCCI, the loss ratio trend on a calendar-accident year basis between 2007 and 2008 appears to be artificially distorted by changes in audit premium levels. Based on these considerations, AACG believes that the exposure-accident year approach provides a better basis from which trends should be selected.

In order to select indemnity and medical loss ratio trends, AACG plotted the historical exposure-accident year loss ratios from 2003 through 2008, as estimated by the NCCI in the 2010 rate filing. The loss ratio estimates used are based solely on the results of the paid+case loss ratio projections. AACG then fitted an exponential curve to the loss ratios. The chart and table below display the historical loss ratios as well as the results of the exponential curve fit.



Year	NCCI Estimated Loss Ratios				Fitted Loss Ratios - Exponential Curve Fit			
	Indemnity	% Change	Medical	% Change	Indemnity	% Change	Medical	% Change
2003	0.331		0.619		0.328		0.613	
2004	0.287	-13.3%	0.548	-11.5%	0.285	-12.9%	0.555	-9.5%
2005	0.245	-14.6%	0.505	-7.8%	0.249	-12.9%	0.502	-9.5%
2006	0.214	-12.7%	0.455	-9.9%	0.217	-12.9%	0.455	-9.5%
2007	0.188	-12.1%	0.407	-10.5%	0.189	-12.9%	0.412	-9.5%
2008	0.167	-11.2%	0.376	-7.6%	0.164	-12.9%	0.373	-9.5%

AACG only relied on the NCCI's estimated loss ratios based on the results of the paid+case projections because it believes that the NCCI's paid projections are more overstated than the paid+case projections. However, even if less overstated than their paid counterparts, AACG believes that the NCCI's paid+case estimated exposure-accident year loss ratios also probably overstate the loss ratio trends for the period 2003 through 2008. AACG is however using the fitted trends of -12.9% for indemnity and -9.5% for medical while considering this caveat.

Loss Development Factors

As previously discussed, AACG believes that the NCCI did not give full consideration to the long term decline experienced in the loss development factors since SB 50A was passed. In order to account for the decline, AACG applied decay factors to the last diagonal of loss development factors for the period of development 2-3, 3-4, and 4-5 in order to calculate expected loss development factors for accident year 2007. The historical loss development factors reviewed by AACG were compiled from the NCCI's 2006 through 2010 rate filings. The selected loss development factors for accident year 2007 were then used to develop the losses for accident years 2007 and 2008. The selected decay factors and resulting loss development factors are displayed in the tables below.

Paid Indemnity - Standard Policies					Paid+Case Indemnity - Standard Policies				
Accident	Development Period				Accident	Development Period			
Year	1-2	2-3	3-4	4-5	Year	1-2	2-3	3-4	4-5
1999	2.901	1.520	1.219	1.092	1999	1.638	1.230	1.102	1.032
2000	2.974	1.514	1.186	1.087	2000	1.629	1.200	1.084	1.035
2001	3.018	1.481	1.171	1.093	2001	1.559	1.192	1.089	1.031
2002	2.886	1.436	1.184	1.086	2002	1.463	1.193	1.077	1.033
2003	2.619	1.402	1.163	1.085	2003	1.425	1.175	1.057	1.027
2004	2.487	1.377	1.153	1.072	2004	1.356	1.129	1.055	1.005
2005	2.433	1.332	1.131	1.067	2005	1.308	1.102	1.045	1.016
2006	2.397	1.317	1.120	1.061	2006	1.294	1.106	1.045	1.016
2007	2.461	1.317	1.120	1.061	2007	1.343	1.106	1.045	1.016
		Decay Factors					Decay Factors		
2000		0.9961	0.9729	0.9954	2000		0.9756	0.9837	1.0029
2001		0.9782	0.9874	1.0055	2001		0.9933	1.0046	0.9961
2002		0.9696	1.0111	0.9936	2002		1.0008	0.9890	1.0019
2003		0.9763	0.9823	0.9991	2003		0.9849	0.9814	0.9942
2004		0.9822	0.9914	0.9880	2004		0.9609	0.9981	0.9786
2005		0.9673	0.9809	0.9950	2005		0.9761	0.9905	1.0000
2006		0.9887	0.9900	0.9950	2006		1.0036	1.0000	1.0000
2007		1.0000	1.0000	1.0000	2007		1.0000	1.0000	1.0000

Paid Medical - Standard Policies				
Accident	Development Period			
Year	1-2	2-3	3-4	4-5
1999	2.261	1.294	1.139	1.066
2000	2.237	1.286	1.119	1.060
2001	2.244	1.263	1.109	1.062
2002	2.142	1.239	1.115	1.059
2003	1.976	1.235	1.102	1.048
2004	1.966	1.191	1.077	1.050
2005	1.858	1.173	1.079	1.045
2006	1.776	1.167	1.068	1.040
2007	1.857	1.167	1.068	1.040

Paid+Case Medical - Standard Policies				
Accident	Development Period			
Year	1-2	2-3	3-4	4-5
1999	1.372	1.120	1.060	1.029
2000	1.345	1.096	1.046	1.030
2001	1.309	1.082	1.058	1.047
2002	1.327	1.088	1.054	1.018
2003	1.237	1.098	1.028	1.023
2004	1.295	1.056	1.032	1.008
2005	1.221	1.049	1.011	1.016
2006	1.156	1.036	1.011	1.016
2007	1.180	1.036	1.011	1.016

Accident	Decay Factors		
Year	1-2	2-3	3-4
2000	0.9938	0.9824	0.9944
2001	0.9821	0.9911	1.0019
2002	0.9810	1.0054	0.9972
2003	0.9968	0.9883	0.9896
2004	0.9644	0.9773	1.0019
2005	0.9849	1.0019	0.9950
2006	0.9949	0.9900	0.9950
2007	1.0000	1.0000	1.0000

Accident	Decay Factors		
Year	1-2	2-3	3-4
2000	0.9786	0.9868	1.0010
2001	0.9872	1.0115	1.0165
2002	1.0055	0.9962	0.9723
2003	1.0092	0.9753	1.0049
2004	0.9617	1.0039	0.9853
2005	0.9934	0.9797	1.0000
2006	0.9876	1.0000	1.0000
2007	1.0000	1.0000	1.0000

Paid Indemnity - Large Deductible				
Accident	Development Period			
Year	1-2	2-3	3-4	4-5
1999	2.899	1.676	1.241	1.135
2000	3.110	1.579	1.293	1.119
2001	3.223	1.618	1.220	1.109
2002	3.246	1.522	1.217	1.103
2003	3.081	1.461	1.196	1.103
2004	2.608	1.413	1.166	1.083
2005	2.692	1.379	1.137	1.078
2006	2.623	1.327	1.126	1.072
2007	2.563	1.300	1.114	1.067

Paid+Case Indemnity - Large Deductible				
Accident	Development Period			
Year	1-2	2-3	3-4	4-5
1999	1.899	1.321	1.143	1.081
2000	1.896	1.369	1.149	1.064
2001	1.946	1.341	1.121	1.079
2002	1.890	1.306	1.122	1.069
2003	1.884	1.241	1.122	1.053
2004	1.605	1.232	1.085	1.032
2005	1.679	1.182	1.075	1.030
2006	1.630	1.154	1.070	1.028
2007	1.623	1.142	1.064	1.026

Accident	Decay Factors		
Year	1-2	2-3	3-4
2000	0.9421	1.0419	0.9859
2001	1.0247	0.9435	0.9911
2002	0.9407	0.9975	0.9946
2003	0.9599	0.9827	1.0000
2004	0.9671	0.9749	0.9819
2005	0.9759	0.9751	0.9950
2006	0.9623	0.9900	0.9950
2007	0.9800	0.9900	0.9950

Accident	Decay Factors		
Year	1-2	2-3	3-4
2000	1.0363	1.0052	0.9843
2001	0.9795	0.9756	1.0141
2002	0.9739	1.0009	0.9907
2003	0.9502	1.0000	0.9850
2004	0.9927	0.9670	0.9801
2005	0.9594	0.9908	0.9980
2006	0.9763	0.9950	0.9980
2007	0.9900	0.9950	0.9980

Paid Medical - Large Deductible					Paid+Case Medical - Large Deductible				
Accident	Development Period				Accident	Development Period			
Year	1-2	2-3	3-4	4-5	Year	1-2	2-3	3-4	4-5
1999	2.321	1.361	1.133	1.071	1999	1.492	1.172	1.077	1.049
2000	2.404	1.337	1.138	1.081	2000	1.560	1.199	1.047	1.050
2001	2.460	1.312	1.142	1.067	2001	1.659	1.171	1.077	1.055
2002	2.324	1.259	1.113	1.075	2002	1.535	1.143	1.056	1.076
2003	2.247	1.230	1.116	1.058	2003	1.488	1.097	1.075	1.034
2004	2.071	1.225	1.084	1.043	2004	1.367	1.123	1.038	1.024
2005	2.051	1.175	1.064	1.038	2005	1.366	1.074	1.034	1.022
2006	1.955	1.145	1.053	1.033	2006	1.306	1.058	1.029	1.020
2007	1.932	1.122	1.043	1.027	2007	1.291	1.047	1.024	1.018

Decay Factors				Decay Factors			
2000	0.9824	1.0044	1.0093	2000	1.0230	0.9721	1.0010
2001	0.9813	1.0035	0.9870	2001	0.9766	1.0287	1.0048
2002	0.9596	0.9746	1.0075	2002	0.9761	0.9805	1.0199
2003	0.9770	1.0027	0.9842	2003	0.9598	1.0180	0.9610
2004	0.9959	0.9713	0.9858	2004	1.0237	0.9656	0.9903
2005	0.9592	0.9815	0.9950	2005	0.9564	0.9961	0.9980
2006	0.9745	0.9900	0.9950	2006	0.9851	0.9950	0.9980
2007	0.9800	0.9900	0.9950	2007	0.9900	0.9950	0.9980

ACCG Estimated Loss Development Factors

Paid - Standard - Age-to-Age						Paid - Standard - Age-to-Ultimate					
	1-2	2-3	3-4	4-5	5-ult		1-2	2-3	3-4	4-5	5-ult
Indemnity	2.461	1.317	1.120	1.061	1.285	Indemnity	4.949	2.011	1.527	1.364	1.285
Medical	1.857	1.167	1.068	1.040	1.307	Medical	3.145	1.694	1.451	1.359	1.307

Paid+Case - Standard - Age-to-Age						Paid+Case - Standard - Age-to-Ultimate					
	1-2	2-3	3-4	4-5	5-ult		1-2	2-3	3-4	4-5	5-ult
Indemnity	1.343	1.106	1.045	1.016	1.107	Indemnity	1.746	1.300	1.175	1.125	1.107
Medical	1.180	1.036	1.011	1.016	1.177	Medical	1.477	1.252	1.208	1.195	1.177

Paid - Large Ded. - Age-to-Age						Paid - Large Ded. - Age-to-Ultimate					
	1-2	2-3	3-4	4-5	5-ult		1-2	2-3	3-4	4-5	5-ult
Indemnity	2.563	1.300	1.114	1.067	1.414	Indemnity	5.603	2.186	1.681	1.509	1.414
Medical	1.932	1.122	1.043	1.027	1.404	Medical	3.261	1.688	1.504	1.443	1.404

Paid+Case - Large Ded. - Age-to-Age						Paid+Case - Large Ded. - Age-to-Ultimate					
	1-2	2-3	3-4	4-5	5-ult		1-2	2-3	3-4	4-5	5-ult
Indemnity	1.623	1.142	1.064	1.026	1.149	Indemnity	2.326	1.433	1.254	1.179	1.149
Medical	1.291	1.047	1.024	1.018	1.228	Medical	1.730	1.340	1.280	1.250	1.228

ACCG's selected loss development factors were used for the first four periods of development. The loss development factors for the fifth period of development to ultimate are from the NCCI's 2010 rate filing. ACCG believes that a complete adjustment of the loss development factors would involve adjusting all periods of development, rather than only the first four periods of development. Therefore, the above adjustments are meant to analyze the potential impact of adjusting the loss development factors and are not meant to form the requisite for a specific adjustment methodology nor are they meant to represent the full potential impact that such adjustment could have on overall indicated rate changes.

Overall Rate Change Indication

AACG computed an overall indicated rate change, based on the methodology used by the NCCI in its 2010 rate filing, but by substituting lower indemnity and medical trends and loss development factors. The results of this updated projection are displayed in the table below.

Comparison of Overall Indicated Rate Change
 Based on the 2010 NCCI Florida Rate Filing

	<u>NCCI Selected</u>	<u>AACG Estimated</u>
(1) Standard Coverage Adjusted Cost Ratio	0.646	0.537
(2) Large Deductible Adjusted Cost Ratio	0.674	0.528
(3) Average Cost Ratio, Weighted by Net Premium	0.650	0.535
(4) Current Target Loss Ratio	0.7143	0.7143
(5) Indicated Change - Experience, Trend, and Benefits [(3)/(4)-1]	0.909	0.749
(6) Effect of Change in Production and General Expenses	1.003	1.003
(7) Effect of Change in Taxes	1.000	1.000
(8) Effect of Change in Loss Based Expenses	1.000	1.000
(9) Effect of Change in Profit and Contingency Provision	1.022	1.022
(10) Indicated Rate Change [(5)x(6)x(7)x(8)x(9)-1]	-6.8%	-23.2%

The detailed projections supporting the above estimates are contained in the appendix of this report.

The above table shows that the lower indemnity and medical trends and loss development factors selected by AACG result in an overall indicated rate change of -23.2% instead of the NCCI's overall indicated rate change of -6.8%. This difference in estimates shows the potential for future savings and future rate decreases that may emerge as a result of SB 50A.

AACG's overall indicated rate change assumes that the trends observed between 2003 and 2008 will carry through policy year 2010.

■ DOCUMENTATION AND DATA

For this review, AACG relied on the following documentation and data received from the NCCI:

- NCCI Florida Rate Filings with proposed effective dates of January 1, 2010, 2009, 2008, 2007, 2006, and 2005.
- Support regarding the calculation of experience rating values.
- Support regarding the internal rate of return model.
- Support regarding the calculation of trending periods.
- Data regarding the distribution of claim counts by hazard group and year.
- Support regarding the calculation of severity, frequency, and loss ratio trends.
- Support regarding the calculation of exposure-accident year earned premium.
- Support regarding the calculation of the Florida DCCE relativities.
- Data regarding the historical closure rate in Florida.
- 2009 Reporting Guidebook for the Annual Calls for Experience.

AACG also relied on the following additional documentation:

- Transcript of the workers' compensation rate hearing held on October 6, 2009 in Tallahassee, Florida, including the pre-filed testimonies.
- Senate Bill 50A Summary, prepared by the Department of Financial Services.
- 2008 Workers' Compensation Annual Report, prepared by OIR.
- 2008 Independent Actuarial Review, prepared by Oliver Wyman Actuarial Consulting, Inc.
- 2006 Independent Actuarial Review, prepared by Oliver Wyman Actuarial Consulting, Inc.
- Supreme Court of Florida, Emma Murray vs. Mariner Health Inc. and ACE USA, October 23, 2008.

■ APPENDIX

- Projection of 2010 Adjusted Cost Ratio – Standard Policies
- Projection of 2010 Adjusted Cost Ratio – Large Deductible Policies

Projection of Adjusted Cost Ratio
Based on 2010 NCCI Rate Filing

Standard Policies

Premium	Accident Year 2008		Accident Year 2007	
	Paid	Paid+Case	Paid	Paid+Case
(1) Standard Earned Premium	2,443,399,682	2,443,399,682	3,214,603,823	3,214,603,823
(2) Factor to Adjust Prem. to Current Level	0.750	0.750	0.613	0.613
(3) Premium Adjusted to Current Level	1,832,549,762	1,832,549,762	1,970,552,143	1,970,552,143

Indemnity Benefit and LAE Cost:

(4) Indemnity Cost Valued as of 12/31/2008	75,137,974	184,934,096	193,523,540	271,856,626
(5) Factor to Develop Indemnity Benefit Cost	4.949	1.746	2.011	1.300
(6) Developed Indemnity Benefit Cost	371,876,507	322,853,685	389,189,799	353,388,709
(7) Factor to Adjust to Current Benefit Level	0.988	0.988	1.000	1.000
(8) Factor to Include Loss Based Expenses	1.255	1.255	1.255	1.255
(9) Composite Adjustment Factor	1.240	1.240	1.255	1.255
(10) Adjusted Indemnity Cost	461,104,556	400,319,198	488,433,198	443,502,829
(11) Indemnity Cost Ratio	0.252	0.218	0.248	0.225
(12) Trend Length	2.355	2.355	3.355	3.355
(13) Application of Indemnity Trend Factor	0.722	0.722	0.629	0.629
(14) Projected Indemnity Cost Ratio	0.182	0.158	0.156	0.142

Medical Benefit and LAE Cost:

(15) Medical Cost Valued as of 12/31/2008	246,871,334	480,570,228	480,848,728	604,505,596
(16) Factor to Develop Medical Benefit Cost	3.145	1.477	1.694	1.252
(17) Developed Medical Benefit Cost	776,463,618	709,914,703	814,417,346	756,776,482
(18) Factor to Adjust to Current Benefit Level	0.990	0.990	0.995	0.995
(19) Factor to Include Loss Based Expenses	1.255	1.255	1.255	1.255
(20) Composite Adjustment Factor	1.242	1.242	1.249	1.249
(21) Adjusted Medical Cost	964,717,222	882,033,523	1,016,983,300	945,005,712
(22) Medical Cost Ratio	0.526	0.481	0.516	0.480
(23) Trend Length	2.355	2.355	3.355	3.355
(24) Application of Medical Trend Factor	0.791	0.791	0.715	0.715
(25) Projected Medical Cost Ratio	0.416	0.380	0.369	0.343

Total Benefit and LAE Cost

(26) Adjusted Cost Ratio [(14)+(25)]	0.598	0.538	0.525	0.485
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Projection of Adjusted Cost Ratio
Based on 2010 NCCI Rate Filing

Large Deductible Policies

Premium	Accident Year 2008		Accident Year 2007	
	Paid	Paid+Case	Paid	Paid+Case
(1) Standard Earned Premium	2,061,431,997	2,061,431,997	2,720,071,696	2,720,071,696
(2) Factor to Adjust Prem. to Current Level	0.750	0.750	0.613	0.613
(3) Premium Adjusted to Current Level	1,546,073,998	1,546,073,998	1,667,403,950	1,667,403,950

Indemnity Benefit and LAE Cost:

(4) Indemnity Cost Valued as of 12/31/2008	54,156,555	114,899,067	162,008,005	220,199,216
(5) Factor to Develop Indemnity Benefit Cost	5.603	2.326	2.186	1.433
(6) Developed Indemnity Benefit Cost	303,441,235	267,252,638	354,169,725	315,575,114
(7) Factor to Adjust to Current Benefit Level	0.988	0.988	1.000	1.000
(8) Factor to Include Loss Based Expenses	1.255	1.255	1.255	1.255
(9) Composite Adjustment Factor	1.240	1.240	1.255	1.255
(10) Adjusted Indemnity Cost	376,248,925	331,377,236	444,483,005	396,046,768
(11) Indemnity Cost Ratio	0.243	0.214	0.267	0.238
(12) Trend Length	2.355	2.355	3.355	3.355
(13) Application of Indemnity Trend Factor	0.722	0.722	0.629	0.629
(14) Projected Indemnity Cost Ratio	0.176	0.155	0.168	0.149

Medical Benefit and LAE Cost:

(15) Medical Cost Valued as of 12/31/2008	181,612,033	341,513,359	392,621,586	496,652,906
(16) Factor to Develop Medical Benefit Cost	3.261	1.730	1.688	1.340
(17) Developed Medical Benefit Cost	592,264,879	590,896,542	662,732,717	665,626,327
(18) Factor to Adjust to Current Benefit Level	0.990	0.990	0.995	0.995
(19) Factor to Include Loss Based Expenses	1.255	1.255	1.255	1.255
(20) Composite Adjustment Factor	1.242	1.242	1.249	1.249
(21) Adjusted Medical Cost	735,859,499	734,159,409	827,570,912	831,184,235
(22) Medical Cost Ratio	0.476	0.475	0.496	0.498
(23) Trend Length	2.355	2.355	3.355	3.355
(24) Application of Medical Trend Factor	0.791	0.791	0.715	0.715
(25) Projected Medical Cost Ratio	0.376	0.375	0.355	0.357

Total Benefit and LAE Cost

(26) Adjusted Cost Ratio [(14)+(25)]	0.552	0.530	0.523	0.506
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