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**OFFICE OF  
INSURANCE REGULATION**  
Docketed by: \_\_\_\_\_

**OFFICE OF INSURANCE REGULATION**

**DAVID ALTMAIER**  
COMMISSIONER

Revised Workers' Compensation Rates and  
Rating Values as Filed by the  
NATIONAL COUNCIL ON  
COMPENSATION INSURANCE, INC.

CASE NO.: 232557-18

ORDER ON RATE FILING

On August 27, 2018, the NATIONAL COUNCIL ON COMPENSATION INSURANCE, INC. ("NCCI") filed, pursuant to Section 627.091, Florida Statutes, revised Workers' Compensation Rates and Rating Values ("Filing") for consideration and review by the FLORIDA OFFICE OF INSURANCE REGULATION ("OFFICE"). The Filing proposed a 13.4% decrease in the overall rate level, to be effective January 1, 2019, on new and renewal policies.

This experience-based Filing proposes a decrease in rate level based on data from Policy Years 2015 and 2016 valued as of year-end 2017. While some of the experience used as the basis for this Filing occurred before the 2016 Florida Supreme Court decisions [Marvin Castellanos v. Next Door Company, et al. ("*Castellanos*"), Case No. SC13-2082, and Bradley Westphal v. City of St. Petersburg, etc., et al. ("*Westphal*"), Case No. SC13-1930], a portion of the experience period includes claims that occurred after the decisions. Even after considering the impact of the *Castellanos* and *Westphal* decisions, other factors at work in the marketplace combined to contribute to the indicated decrease, which included reduced assessments, increases in investment income, and declines in claim frequency.

The OFFICE provided an opportunity for members of the public to comment on the Filing, but did not hold a public hearing due to Hurricane Michael.

Following a complete review of the entire record, and upon consideration of the Filing and additional information provided by NCCI, the supporting data, public comments received, and the analysis by the staff of the OFFICE, and being otherwise fully advised in the premises the OFFICE finds as follows:

1. The OFFICE has jurisdiction over the parties and the subject matter of these proceedings.

2. NCCI is a licensed rating organization authorized to make rate filings on behalf of workers' compensation insurance companies in Florida pursuant to Section 627.091(4), Florida Statutes. Any insurer may make a filing to deviate from the NCCI rate level pursuant to Section 627.211, Florida Statutes, and Rule 690-189.004, Florida Administrative Code.

3. NCCI provided on-level developed loss ratio data in the Filing that is the basis for the proposed annual indemnity and medical trend selections. NCCI also provided claim frequency (number of workplace injuries) and claim severity (average cost per injury) data but did not specifically select trends based on this data. An analysis of the data reveals there is a significant downward trend in the loss ratios from policy year 2002 to 2006. During this timeframe the indemnity loss ratio declined by 42.4% and the medical loss ratio declined by 34.9%. From 2007 to 2010, the loss ratios primarily increased. The total increase in loss ratios during this period was 4.7% for indemnity and 9.1% for medical. The most recent policy years, 2011 to 2016, show a declining trend in the loss ratios, but the decline is much less substantial than that exhibited from 2001 to 2006. From 2011 to 2016, the cumulative decreases in the indemnity and medical loss ratios were 29.1% and 22.8%, respectively. The primary reason for the declining loss ratios is a significant reduction in the lost-time claim frequency, which declined by 47.2% from 2002 to 2016

with over 11% of the decline occurring in 2015 and 2016. NCCI provided testimony at a prior hearing that claim frequency decline for workers' compensation is not unique to Florida and that for a number of years frequency has been declining countrywide similar to Florida. NCCI also testified that claim frequency decline is due, in part, to safer workplaces, enhanced efficiencies in the workplace, and increased use of automation and innovative technologies. According to NCCI's testimony the decline is expected to continue in the future.

4. Fitting the historical data provided in the Filing to an exponential curve allows for an analysis of the loss ratio trends, but the trend data in the Filing reflects losses that have been adjusted to the current level using the NCCI initial estimate of the effect of the 2003 reforms. If the actual impact of the 2003 reforms is greater than the initial estimate (as is commonly believed), then the use of the longer-term data in the Filing could produce trends that are too low. Excluding data prior to the 2003 reforms, the loss ratio trend data in the Filing provides a range of trend values for indemnity from -4.7% to -2.7% and for medical from -4.3% to -1.2% using various exponential trend fits (13-point through 5-point) to the latest 13 years of policy year data for Standard Coverage. It is also apparent that nonrecurring events, such as the Great Recession and subsequent recovery, are likely impacting the data provided by NCCI for the trend analysis. In a trending procedure, it is proper to consider the impact of any events that may be influencing the data and determine if the observed trends affected by these events will continue into the projected period when the rates will be effective. Recognizing that the 2003 reforms have affected the data in ways that will not be repeated in the future and other considerations such as the economic events impacting the data used for the trend analysis, the NCCI selected annual indemnity trend of -3.5% and the selected annual medical trend of -2.0% appear to be reasonable.

5. In this Filing, the internal rate of return model used by NCCI in selecting the profit and contingencies provision of -0.5% does not include anticipated policyholder dividends. Florida

workers' compensation rates have not previously included an explicit policyholder dividends provision greater than zero. Further, the failure to explicitly load an amount for policyholder dividends into the rates has not precluded insurers from paying policyholder dividends in Florida. Thus, policyholders in Florida have received substantial dividends without the explicit inclusion of a provision for policyholder dividends greater than zero.

6. Policyholder dividends are, by definition, a non-guaranteed return of profits, which means the payment of policyholder dividends is left strictly to the discretion of the insurers. In order for a policyholder to be eligible for a policyholder dividend, the insurance carrier files a participating endorsement that is attached to and becomes part of the policy. Many insurance carriers do not intend to pay policyholder dividends and have not filed such endorsements. Of the 245 insurance carriers actively writing workers' compensation in Florida in calendar year 2017, only 97 carriers paid policyholder dividends. Thus, if the rates are explicitly loaded for policyholder dividends, some employers will pay higher rates without any possibility of receiving a dividend, so that other employers can receive a policyholder dividend. This loading would likely result in unfairly discriminatory rates.

7. Pursuant to Actuarial Standards of Practice 29, "[w]hen the actuary determines that policyholder dividends are a reasonably expected expense and are associated with the risk transfer, the actuary may include a provision in the rate for the expected amount of policyholder dividends." NCCI has not demonstrated that for Florida workers' compensation policyholder dividends are a reasonably expected expense and are associated with the risk transfer. Nor has NCCI demonstrated that, in accordance with Actuarial Standards of Practice 29, they have considered the following: the companies' dividend payment history, the current dividend policy or practice, whether dividends are related to loss experience, the capitalization of the companies, and other

considerations affecting the payment of dividends. Further, NCCI did not address these factors in the Filing.

8. NCCI estimated the “static” investment yield at +3.2%, a yield near historic long-term lows. This estimate is below the average representative portfolio yields over the recent past, and below expected yields in the near future, as economic performance continues to improve. NCCI has estimated the “dynamic” investment yield to range from +4.14% to +4.62%. The “dynamic” yields are forecasted, forward-looking estimates and are more likely to capture general market trends than the “static” investment yield, which assumes that the return on investments does not change over time. A common belief among economists is that interest rates are mean-reverting, suggesting that the “static” estimate is very likely underestimating any reasonable estimation of investment yields looking forward.

9. Based on paragraphs 5 through 8 above, the -0.5% profit and contingencies provision is excessive. The use of a -0.5% profit and contingencies provision in the Filing does not adequately reflect investment income on unearned premium and loss reserves as required by Section 627.072, Florida Statutes. Investment yields have increased since the profit and contingencies provision of +0.5% underlying the current rates was approved, and it is appropriate to decrease the profit and contingencies factor to less than a -0.5% to reflect this change.

10. Classification code rates are derived using a three-way credibility weighting of the indicated, the present on rate level, and national pure premiums. In this Filing, NCCI proposes to not include a national pure premium component in the derivation of the classification code ratemaking process for those codes that are a state special in less than seven states so that the experience in one state or a few states does not unduly impact the derivation of the rate in Florida. This change affects twelve classification codes in Florida.

11. NCCI has not supported that the exclusion of the similar experience for the twelve state-special classification codes outside of Florida is appropriate and complies with Section 627.072(1)(a), Florida Statutes.

12. The OFFICE received testimony in prior hearings regarding the uncertainties associated with the recent Florida Supreme Court decision, *Castellanos*. To ensure workers' compensation rates are not excessive, inadequate, or unfairly discriminatory in violation of Section 627.062, Florida Statutes, it is imperative that additional quantitative analysis be conducted to determine the effect the *Castellanos* decision is having on the Florida workers' compensation market and the data used to support future rate filings. The analysis may include alternative data sources and should examine changes to the Florida workers' compensation market that are attributed to or observed as a result of the recent court decision. These changes include, but are not limited to, reopening of claims from older years, changes in reserves or payment patterns, changes to claim closure or settlement rates, changes to claim frequency and severities, increasing attorney involvement, and fees paid to attorneys.

WHEREFORE, in consideration of the foregoing, and being otherwise duly advised in the premises, it is hereby ORDERED:

The Filing by NCCI is hereby DISAPPROVED. The Filing will be approved provided that the Filing is amended to comply with all of the following and that such amendments to the Filing are filed as soon as practicable.

A. Effective January 1, 2019, for new and renewal policies for other than the "F" classifications, the statewide overall rate level change shall be -13.8% for the Filing.

B. The -0.5% allowance for profit and contingencies for the proposed rates in the Filing and identified in Exhibit II of the Filing is disapproved. Exhibit II of the Filing shall be re-filed

containing a profit and contingencies provision no greater than -0.8%. The -0.8% profit and contingencies provision shall also apply to the “F” classifications.

C. The exclusion of national pure premium information in the derivation of the classification code rate for state specials in which the classification code only exists in seven states or less is disapproved.

D. In future rate filings, NCCI shall provide a detailed explanatory memo and quantitative analysis regarding the effect the recent Florida Supreme Court decision of *Castellanos* is having on the Florida workers’ compensation market and the data used to support future rate filings.

E. For any filing submitted to the OFFICE, NCCI shall list and explain each and every change in the proposed manual pages, including but not limited to, the rating plan manual, the experience rating plan manual, and the retrospective rating plan manual. These shall be shown in the summary exhibit and described by an explanatory memorandum.

F. NCCI shall provide a monthly report to the OFFICE of the average intrastate experience modification factors for the policies effective during the month. This monthly report shall be filed with the OFFICE within 7 days of the end of the month. Thus, the January 2019 report will be due no later than February 7, 2019.

G. Section 627.4133, Florida Statutes, requires insurers to give at least 45 days’ notice of renewal premium. Therefore, to meet statutory timeframes for a January 1, 2019, effective date, NCCI shall file the necessary amendments to the Filing as may be required to implement the terms of this Order as soon as practicable but no later than November 7, 2018. No rate change shall be implemented until such amendments are properly filed and final approval is issued by the OFFICE. If NCCI fails to file the necessary amendments to the Filing to implement the terms of this Order, the OFFICE will initiate proceedings under Section 627.141, Florida Statutes, to disapprove the current rates.

H. By making a filing to comply with this order, NCCI waives any right to any further proceedings and authorizes the OFFICE to enter a final order on the Filing.

DONE and ORDERED this 2<sup>nd</sup> day of November, 2018.



*David Altmaier*  
David Altmaier, Commissioner  
Office of Insurance Regulation



COPIES FURNISHED TO:

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## NOTICE OF RIGHTS

Pursuant to Sections 120.569 and 120.57, Florida Statutes and Rule Chapter 28-106, Florida Administrative Code (F.A.C.), you may have a right to request a proceeding to contest this action by the Office of Insurance Regulation (hereinafter the "Office"). You may request a proceeding by filing a Petition. Your Petition for a proceeding must be in writing and must be filed with the General Counsel acting as the Agency Clerk, Office of Insurance Regulation. If served by U.S. Mail, the Petition should be addressed to the Florida Office of Insurance Regulation at 612 Larson Building, Tallahassee, Florida 32399-4206. If Express Mail or hand-delivery is utilized, the Petition should be delivered to 612 Larson Building, 200 East Gaines Street, Tallahassee, Florida 32399-0300. The written Petition must be received by, and filed in the Office no later than 5:00 p.m. on the twenty-first (21) day after your receipt of this notice. Unless your Petition challenging this action is received by the Office within twenty-one (21) days from the date of the receipt of this notice, the right to a proceeding shall be deemed waived. Mailing the response on the twenty-first day will not preserve your right to a hearing.

If a proceeding is requested and there is no dispute of material fact the provisions of Section 120.57(2), Florida Statutes may apply. In this regard you may submit oral or written evidence in opposition to the action taken by this agency or a written statement challenging the grounds upon which the agency has relied. While a hearing is normally not required in the absence of a dispute of fact, if you feel that a hearing is necessary one will be conducted in Tallahassee, Florida or by telephonic conference call upon your request.

If you dispute material facts which are the basis for this agency's action you may request a formal adversarial proceeding pursuant to Sections 120.569 and 120.57(1), Florida Statutes. If you request this type of proceeding, the request must comply with all of the requirements of Rule Chapter 28-106.201, F.A.C., must demonstrate that your substantial interests have been affected by this agency's action, and contain:

- a) A statement of all disputed issues of material fact. If there are none, the petition must so indicate;
- b) A concise statement of the ultimate facts alleged, including the specific facts the petitioner contends warrant reversal or modification of the agency's proposed action;
- c) A statement of the specific rules or statutes the petitioner contends require reversal or modification of the agency's proposed action; and
- d) A statement of the relief sought by the petitioner, stating precisely the action petitioner wishes the agency to take with respect to the agency's proposed action.

In some instances you may have additional statutory rights than the ones described herein.

Failure to follow the procedure outlined with regard to your response to this notice may result in the request being denied. Any request for an administrative proceeding received prior to the date of this notice shall be deemed abandoned unless timely renewed in compliance with the guidelines as set out above.

Revised 9/4/2008