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ACTUARIAL AND CLASSIFICATION & RATING COMMITTEES - RECORD OF JOINT MEETING

A meeting of the Actuarial and Classification & Rating Committees of the Pennsylvania Compensation Rating Bureau was held in the Board (Blue) Room, 7th Floor, One South Broad Building, One South Broad Street, Philadelphia, Pennsylvania on Wednesday, November 5, 2003 at 10 a.m.

The following members were present:

Actuarial Committee

Ms. M. Gaillard*	American Home Assurance Company
Mr. L. White	AmeriHealth Casualty Company
Mr. G. Busche	Continental Casualty Company
Ms. M. Sperduto	Harleysville Mutual Insurance Company
Ms. P. Sealand-Reale	Hartford Accident & Indemnity Company
Mr. P. DeMallie*	Liberty Mutual Insurance Company
Mr. D. Miller	Penn National Insurance Company
Mr. J. Fratatoro	PMA Insurance Company
Mr. M. Yingling	Travelers Insurance Company

Classification and Rating Committee

Ms. M. Gaillard*	American Home Assurance Company
Mr. J. McGuire	Amguard Insurance Company
Mr. J. Binkowski	Insurance Company of North America
Mr. P. DeMallie*	Liberty Mutual Insurance Company
Not represented	Manufacturers Assn. of South Central Pennsylvania
Not represented	National Federation of Independent Business
Not represented	Pennsylvania Chamber of Business & Industry
Mr. F. Preis	Pennsylvania Food Merchants Association
Ms. B. Flaherty	PMA Insurance Company
Not represented	Pennsylvania Retailers' Association
Not represented	Security Insurance of Hartford
Mr. J. Gilbert	Westport Insurance Company

Mr. T. Wisecarver	Chair - Ex Officio

Also present were:

Mr. D. Broadwater	Coal Mine Compensation Rating Bureau of Pennsylvania
Mr. J. Potts	Duane Morris, LLP
Mr. J. Hohman	Erie Insurance Company
Mr. W. Wilkins	Insurance Company of North America

Mr. J. Zhang	Mercer Risk Finance & Insurance Consulting (Office of Small Business Advocate)
Ms. K. Ayres	National Council on Compensation Insurance, Inc.
Ms. C. Pennington	Office of Small Business Advocate
Mr. K. Creighton	Pennsylvania Insurance Department
Mr. C. Romberger	Pennsylvania Insurance Department
Mr. B. Krick	Selective Insurance Company
Mr. M. Pozaic	State Workers' Insurance Fund
Ms. F. Barton	Bureau Staff
Ms. D. Belfus	Bureau Staff
Mr. B. Decker	Bureau Staff
Mr. M. Doyle	Bureau Staff
Mr. P. Yoon	Bureau Staff

* Member of both committees

The Antitrust Preamble was read at the beginning of the meeting for the benefit of all participants.

All Committee members and other attendees made self-introductions.

Staff noted the meeting agenda materials provided in advance of the meeting and indicated that the Committee discussion would be organized so as to first address specific subject areas incorporated in those materials. All Committee members and other attendees were encouraged to participate in the meeting by raising questions or posing suggestions as those arose during the course of discussion.

The meeting discussion proceeded to address the overall loss cost indication, with questions posed and responses given as offset by inserted italicized "Question" and "Response" entries below:

<u>Trended Ultimate Loss Ratios - Indemnity</u>

Exhibit 5 was identified as providing historical financial data upon which the proposed filing's analysis was based. Participants were reminded that for recent loss cost filings the Bureau had adopted an approach of adjusting financial data to "post-law" levels, as respects the medical provisions of Act 44 of 1993 (Act 44) and the indemnity provisions of Act 57 of 1996 (Act 57). It was noted that the limited indemnity provisions of Act 44 had been accounted for in those previous filings by way of a "savings factor" applied to loss ratios initially established on a "pre-law change" basis. Staff indicated that these techniques continued to be used for this proposed filing. This methodology, which offered efficiencies in the overall filing analysis, precluded on-going revisions of prior estimates of the separate and specific effects of the more substantial components of those law changes on Pennsylvania workers compensation system costs.

Page 1 of Exhibit 5 provided the two most recent calendar years of premium development data, which staff noted was supplemented by additional older experience taken from previous filings' documentation for the analysis supporting this proposed filing.

Reported indemnity losses were identified as appearing on Page 3 (case-incurred indemnity loss) and Page 5 (paid indemnity loss) of Exhibit 5. Pages 7 through 17 of Exhibit 5 were noted as presenting details of the adjustment of indemnity experience to a post-Act 57 basis. Adjustments for calendar years prior to 1999 reflected factors derived in previous Bureau filings. The original such adjustments had been prepared using data from the April 1, 1999 Loss Cost Filing. Those adjustments had been balanced so that indications obtained using historical data adjusted to a "post-law" level were comparable to alternative indications derived using historical data stated on a "pre-law" level in combination with savings factors related to legislation. The adjustment for Calendar Year 2002 was used for the first time in this proposed filing. Staff distributed a revised Page 17 of Exhibit 5 correcting an inadvertent duplication of the adjustment of indemnity losses for Calendar Year 2001 instead of the intended and appropriate adjustment for Calendar Year 2002. The correct adjustment had been carried forward to subsequent parts of the filing, the error in compiling Exhibit 5 pages notwithstanding. The Calendar Year 2002 adjustment had been performed in a manner similar to adjustments for prior years and used parameters consistent with those prior adjustments and/or ongoing assumptions about the extent to which data had responded to the effects of the law change.

The adjusted indemnity financial data, stated on a post-Act 57 basis, was shown on Pages 31 (incurred loss) and 33 (paid loss) of Exhibit 5.

Exhibit 6 presented the Bureau's loss development analysis in support of the filing, as well as significant portions of the special trend procedure proposed for use therein. Staff reviewed the pertinent portions of Exhibit 6 and related supporting documentation for indemnity benefits as follows.

Page 6.1 of Exhibit 6 provided premium and/or expected loss development history and estimated ultimate, on-level expected losses for use in computing loss ratios. Pages 6.2 through 6.6 provided steps in the application of incurred and/or paid loss development approaches to indemnity benefits. One of the approaches shown used a case-incurred loss development method to estimate ultimate indemnity losses. A series of additional alternative estimates had been constructed using a combination of paid loss development and case-incurred loss development methods. By applying a paid loss development method to indemnity benefits for varying periods of initial development, then converting cumulative paid losses to equivalent case-incurred losses and applying case-incurred loss development for the remaining development period(s) to ultimate, the Bureau had constructed a series of ultimate indemnity loss estimates. Finally, the Bureau had derived estimates using the average of a case-incurred loss development method and the paid loss development method that relied on the longest available period of paid loss experience (in this case, a paid loss development method applied to 20th report).

Exhibit 7 presented the Bureau's derivation of "tail factors" for use in its array of possible loss development methods. The methodology applied had been used in prior PCRB filings in response to recommendations in regulatory examinations. Pages 2, 4, 6 and 8 of this exhibit each provided a tail factor estimate for indemnity benefits based on a different calendar year of development experience. An indemnity tail factor for the proposed filing had been selected as the average of these four separate indications, as summarized on Page 1 of Exhibit 7.

Exhibit 8 provided claim frequency experience that the Bureau had used in support of its trend analysis for the proposed filing.

Staff had obtained counts of indemnity claims and exposures (measured by expected losses at a constant set of Bureau loss costs) from unit statistical reports. This data was available by policy year from 1987 through 2001, with the last year having a mid-point of January 1, 2001. Compilations of this experience were provided separately for non-deductible business (Pages 3 and 4 of Exhibit 8) and for all business including deductible coverages (Pages 5 and 6 of Exhibit 8.) Staff had also reviewed trends in claim frequency by industry group, and indications for that review were provided on Pages 8 and 9 of Exhibit 8.

Recent PCRB filings had included reference to data provided by the Department of Labor and Industry (L&I) regarding counts of injuries and illnesses reported in the Commonwealth, together with non-Federal payrolls. The work injuries and illnesses shown in those reports were incidents resulting in lost time beyond the day or shift of occurrence. For this filing, updates had been received from the L&I through June 30, 2003. The history of these injury reports and payrolls was thus available on a calendar year basis from 1985 through 2002 and for the 12-month period ending June 30, 2003.

Staff noted that, in providing its more recent data for counts of injuries and illnesses, L&I had cautioned the Bureau that this data had been influenced to an unknown extent by changes in reporting practices by some of their data sources. In the main, the changes so noted were thought by L&I representatives to have involved changing from a practice of reporting only indemnity claims to the intended procedure of included injury and illness reports for any case having lost time beyond the date or shift of occurrence.

Given the caveats applicable to the more recent data from L&I, staff had not made adjustments to its analysis of claim frequency as reflected in Bureau data based on the L&I information. For reference purposes, however, the historical data from L&I was provided on Pages 1 and 2 of Exhibit 8, and a graphical comparison of the claim frequency trends inherent in that data to those reflected in the PCRB data was set forth on Page 7 of Exhibit 8.

Question: How quickly were the changes in reporting practices for the L&I data assimilated into their ongoing reports?

Response: The PCRB suspects that this transition is not yet complete, as the trends in claim counts and frequencies continue to diverge somewhat from those reflected in PCRB data for common periods of time. The PCRB would expect reporting practices to stabilize at some point and intends to continue to monitor the L&I data for possible utility in future filings.

Question: Did L&I approach all of the reporting entities to alert them to the discovered reporting problems at the same time?

Response: The PCRB's understanding was that reporting entities had been informed on a case-by-case basis about necessary changes as the discrepancies in prior practices came to light. The PCRB was not certain what processes had been used to canvas or identify potential reporting problems or the entire timeframe over which that activity had take or was taking place.

Comment: A Committee member observed that on the Exhibit 8 prepared for the April 1, 2003 filing the one-year claim frequency change for Policy Year 2000 showed a decline of 7.5 percent, while in the current Exhibit 8 the one-year change for Policy Year 2000 was shown as a decline of only 6.0 percent.

Response: Staff noted that all of the claim frequency reports from PCRB data in Exhibit 8 reflected first report statistical data. Changes in claim frequency could and did occur in recent years as correction reports and/or previously missing reports were filed. Generally, staff would expect claim counts to increase for relatively recent policy years because of corrections and new reports. However, with new reports, exposures and thus expected losses would also increase, so that the implications of such revisions on claim frequency were not clearly preordained. It was further noted that in using a mid- to long-term average change in claim frequency the effect of changes in an isolated year would be limited.

Question: As a result of the process as described, would staff expect to see even more of a decline in claim frequency for Policy Year 2000 when data is assembled a year from now than the 6.0 percent figure shown this year?

Response: While staff would expect claim counts to increase for the most recent policy year or years, the combined effects of those changes and revisions in exposure reports on claim frequency might either reduce or increase frequency. The changes to first report data would be expected to become very small after a year or two of additional reporting.

Staff described the proposed filling's approach to trend analysis in the following fashion. Estimated ultimate on-level loss ratios derived in Exhibit 6 had been adjusted for the effects of changes in claim frequency presented in the Bureau data from Exhibit 8. The results of these adjustments were referred to as "severity ratios" and were presented on Page 6.6 of Exhibit 6. The Bureau had then applied its customary linear and exponential trend models to the severity ratios so derived over numbers of data points ranging from four to ten. For each trend model and loss development method in combination, severity trend factors were calculated for each of the three most recent policy years. This severity trend analysis was shown on Pages 6.7 through 6.10 of Exhibit 6.

Question: Is the selected methodology for measuring indemnity severity trend different from that applied in the PCRB's filing a year ago?

Response: Last year the PCRB had presented a five-point linear trend model for indemnity severity to the Committees. Based on discussion, however, the April 1, 2003 filing had used a five-point exponential trend for indemnity severity. This year's materials for Committee review used a six-point exponential model for indemnity severity.

In Exhibits 9a and 9b, goodness-of-fit tests had been applied to trend models applied to loss ratios (Exhibit 9a) and severity ratios (Exhibit 9b). Exhibits 11a and 11b, respectively, provided further examinations of the effectiveness of trend models by testing predictive abilities of the respective models and trend periods prepared in support of this proposed filing.

For use in conjunction with the indemnity severity trend factors, the Bureau had selected from Exhibit 8 a prospective frequency trend based on non-deductible business over the Policy Years 1996 – 2001 inclusive, resulting in a frequency trend of –6.0 percent which had been used in trending claim frequency through the mid-point of the prospective rating period (April 1, 2005). The frequency trend factors consistent with this procedure were set forth on Page 6.6 of Exhibit 6.

Indemnity loss ratio trend factors computed as the product of the indemnity severity trend factors and frequency trend factors describe above were shown on Page 6.11 of Exhibit 6. The resulting trended indemnity loss ratios were presented on Pages 6.12 (linear trend model) and 6.13 (exponential trend model).

Exhibit 10 provided graphs of indemnity loss ratios (Page 10.1) and indemnity severity ratios (Page 10.3). In addition, Exhibit 10 provided a graph of indemnity loss ratios, indemnity severity ratios and claim frequency on Page 10.5, each indexed to a common starting point (January 1, 1990). These graphs illustrated the point that, since Policy Year 1996 indemnity claim severity in Pennsylvania had been generally increasing at a rate more than offsetting continuing improvements in claim frequency.

Question: An attendee observed that indemnity loss ratios as graphed on Exhibit 10 showed significantly different patterns in the separate periods before Policy Year 1996 and after Policy Year 1995. Since Act 57 had gone into effect in 1996, this observer questioned whether the graphs might suggest that the adjustments made for Act 57 were playing some part in the observed discontinuity.

Response: The PCRB had developed the adjustments applied to financial data to account for prior legislation only after some years of experience under the new laws had become available and held significant confidence about those adjustments in general.

It was observed that the 1995-1996 inflection point in Exhibit 10 was evident for medical benefits as well as for indemnity, but that the statutory changes being adjusted for in medical loss ratios had become effective in 1993.

The Coal Mine Compensation Rating Bureau representative noted that that organization's data was presenting similar patterns to those seen in the PCRB data.

Staff then observed that claim severity ratios were much smoother and more consistent year-to-year than were loss ratios and pointed to very large drops in claim frequency that had occurred over the five successive policy years for 1991 through 1995 inclusive. Staff thought that the pattern of severity ratios was generally supportive of the law adjustments being applied to financial data.

Question: Staff was asked whether employment levels might be affecting claim frequency.

Response: Staff commented that employment levels would impact the absolute number of claims but observed that fewer workers would not only produce fewer claims but also lower expected losses, and, as a consequence, claim frequency would not inherently be made better as a statistical matter by virtue of lower employment.

Comment: It was noted that in the mid-1990s many states had enacted various kinds of reforms and changes to their workers compensation laws, including a variety of changes in claim practices. It was theorized that such changes might have affected claim reporting and/or claim frequency.

Response: Other attendees stated that even states that have not had reforms had seen declines in claim frequency over time. Staff concurred with this observation with respect to Delaware. It was noted that the change in claim frequency for Policy Year 2001 was not particularly remarkable in the context of other recent annual changes.

Pages 6.12 and 6.13 of Exhibit 6 showed arrays of possible trended indemnity loss ratios produced by the methods described above, with the Bureau's selected result highlighted with a border on Page 6.13. The selected result was produced using the average of a case-incurred loss development approach and the paid loss development method to 20th report loss development. An exponential six-point severity trend was used in combination with the selection of an annual claim frequency trend rate of –6.0 percent to trend selected policy year results forward through the mid-point of the prospective rating period, April 1, 2005.

Trended Ultimate Loss Ratios - Medical

Staff indicated that the analysis done for medical losses paralleled that described above for indemnity losses in most important respects. The pertinent exhibit and page references were provided as follow:

Exhibit	Content	Page(s)
5	Medical financial data - Table I Reported data	4 (case incurred), 6 (paid)
	Adjustment of medical financial data to Post-Act 44 basis	18 through 28
	Adjusted medical financial data	32 (case incurred), 34 (paid)
6	Medical loss development	6.14 through 6.18
	Trending of medical Severity ratios	6.19 through 6.22
	Medical loss ratio trend factors	6.23
	Trended medical loss ratios	6.24 (linear), 6.25 (exponential)
7	Medical loss development tail factors	Summary on Page 1, detail on Pages 3, 5, 7 and 9
8	Claim frequency	Per indemnity discussion

Exhibit	Content	Page(s)
9a, 9b	Goodness of fit tests 9a for loss ratios, 9b for severity ratios	9a1, 9a4, 9a5, 9a8 and 9a9 9b1, 9b4, 9b5, 9b8 and 9b9
11a, 11b	Retrospective tests of prediction 11a for loss ratios, 11b for severity ratios	11a6 – 11a10 and 11b6 – 11b10
10	Graphs of medical loss ratios Graphs of medical severity ratios Graph of indexed medical loss ratios, Severity ratios and frequency trends combined	10.2 10.4 10.6

Staff provided a replacement Page 6.18 of Exhibit 6 that included a matrix of estimated loss ratios by policy year and loss development method that had been inadvertently omitted from the original agenda material printing.

Staff noted that the trend model used for medical severity ratios was an exponential fit through the most recent six policy year data points, estimated based on the average of the case incurred and paid to 20th report development methods. In combination with the selected claim frequency trend previously described with the analysis of indemnity experience, this approach gave the trended medical loss ratio highlighted with a border on page 6.25 of Exhibit 6.

Indicated Overall Change in Loss Costs

Exhibit 12 of the agenda materials supported this section of the meeting discussion. Staff described the construction and interpretation of Exhibit 12 as follows.

Loss ratios selected for indemnity and medical benefits had been posted for each of the three most recent available completed policy years, i.e., 1999, 2000 and 2001. These loss ratios and the resultant average ratios were shown on Lines (1) through (4) on Page 12.1 of Exhibit 12.

Trended loss ratios based on each of the Policy Years 1999, 2000 and 2001 were presented on Lines (5) through (7) on Page 12.1 of Exhibit 12, with the resultant average trended loss ratio shown on Line (8) of that same page.

The appropriate savings factors for the indemnity provisions of Act 44 of 1993 previously described were shown on Line (9) on Page 12.1 and had been applied to produce Line (12) of that exhibit. This analysis produced an overall collectible loss cost increase of approximately 3.32 percent.

Staff noted that nominal changes in Experience Rating Plan off-balances, measured using the currently approved Experience Rating Plan and differing by industry group, had been applied to produce the indicated average changes in manual loss costs by industry group shown on Line (15), Page 12.1 of Exhibit 12. Two handout pages were provided that supplemented the original materials for Exhibit 12. The first handout page added an overall manual loss cost

change consistent with the currently-approved Experience Rating Plan (a result not available when the original agenda materials were produced). The second handout page presented comparable values for manual loss cost change indications by industry group and in total consistent with the proposed Experience Rating Plan that had been filed with the Pennsylvania Insurance Department in June 2003 and remained pending before the Department as of the date of this meeting.

Question: What effective date was proposed for the revisions to the Experience Rating Plan?

Response: The proposed revisions to the Experience Rating Plan had been filed with the Insurance Department in June 2003 and had included a proposed effective date of April 1, 2004.

Question: What would the likely timing of a forthcoming filing be?

Response: In general staff aspired to present annual loss cost filings to the regulator as soon as possible, toward the goal of providing as much advance notice as possible to the market-place of approved changes in rating values. In the present case it was noted that some time and effort would be devoted to reviewing and evaluating the Caso case and potentially other recent case decisions. Staff opined that actual presentation of a filing would take a couple of weeks, if not longer.

Question: On Line 11 of Exhibit 12, how did the PCRB derive the value shown of "0.9970"?

Response: The value in question, the overall impact of Act 44 changes on loss costs not incorporated into the adjustments of financial data in the PCRB's filings, was a weighted average of the separate factors shown of "0.9943" for indemnity and "1.0000" for medical. As a result of Act 44, the absolute minimum benefit was eliminated, and the maximum burial award for death cases had been increased, and these were the changes reflected in the values under discussion.

Question: What is the average experience modification?

*Response: The average experience modification, including the effects of risks not subject to experience rating, would be derived as the reciprocal of the "collectible premium ratio." The proposed Experience Rating Plan included a proposal to limit year-to-year swings in experience modifications to a range of +/-25 percent from the expiring modification. Staff noted that that provision pushed the collectible premium ratio under the proposed Experience Rating Plan closer to that of the current plan than would have been the case absent the limitation of modification changes***.**

Question: Do all of the PCRB's medical loss development methods use the same tail factor?

Response: Yes. All medical loss development methods use the same tail factor, derived from a four-year average analysis presented in Exhibit 7. Similarly, all indemnity loss development methods use a common tail factor similarly derived and much smaller than the tail factor applied to medical losses.

Following the discussion of the overall loss cost change indication, the Committees continued discussion of additional topics related to staff analysis or potential areas for additional review as outlined below.

Terrorism Provisions in Pricing

Staff noted that the PCRB had implemented a loss cost rating value related to terrorism effective April 1, 2003. That implementation had been supported by terrorism modeling analysis done by and/or for the National Council on Compensation Insurance, Inc. (NCCI). The PCRB had subsequently been advised by NCCI that further analysis had resulted in some changes in the original modeling that essentially offset the scheduled changes in company retentions under the Terrorism Risk Insurance Act of 2002 (TRIA), and that, as a result, NCCI was generally holding rating values related to TRIA level in their current filing cycle. The PCRB felt that under these circumstances it was appropriate to retain the existing loss cost rating value for terrorism in Pennsylvania and, thus, was not proposing a change in that value at this time.

Recognition of Recent Case Law Precedents and Related Influences on Loss Cost Levels

Staff provided a brief and general background of issues pertinent to the *Caso* decision and described previous and ongoing staff work intended to develop estimates of the effect of that precedent on prospective loss costs in Pennsylvania. Excerpts from legal discussions of the Caso case that had been obtained by the Bureau were read to illustrate the range of views that appeared to exist with respect to the implications of this case on system costs.

Committee members and other attendees were invited to offer insights, suggested references or sources, or results of independent efforts focused on such an evaluation for the consideration of staff in its preparation of the April 1, 2004 Loss Cost Filing.

Comment: One Committee member reported that their claims department did not think that this decision would have much of an impact on system costs.

Comment: Another Committee member expressed the opposite view, stating that their claims department was very concerned about the Caso precedent. While acknowledging that the company's defense work continued to try to accomplish desired results despite this decision, the company firmly believed that Caso would increase both settlement costs and duration of claims.

Question: Staff was asked whether aggressive claims adjusters might respond to the Caso decision by using techniques such as settlements.

Response: Staff thought that the Caso case could, in fact, impact settlement opportunities, practices and ultimately values. The dynamic in which a case law precedent might serve to impair settlement processes and opportunities was thought to make the decision both more important (given the historical significance of compromise and release settlements in Pennsylvania) and harder to objectively quantify.

Question: Staff was asked whether attendees should direct data pertaining to the Caso decision to the PCRB for attention.

Response: Staff encouraged all attendees to provide any subsequent comments or information to the PCRB. It was noted that efforts were in progress to obtain data from L&I and from the Workers' Compensation Research Institute (WCRI) in addition to individual PCRB members and other constituencies.

Comment: A Committee member stated that their claims department monitored case law on an ongoing basis but that their company had the impression and expectation that parties don't generally embrace and apply such findings unless and until a matter is finally resolved at a final level. Given that Caso now was on appeal before the Supreme Court in Pennsylvania, this member felt that its impact would not have been substantial as yet.

Response: Staff observed that references to Caso in some other decisions provided evidence that the administrative system has already taken at least some notice of this case.

Comment: The opinion was expressed that, given the present uncertainty regarding the ultimate decision in Caso, activity on many outstanding claims would in effect be in a holding pattern until a decision was finalized. This commenter thought that, even if the Supreme Court were to ultimately decide Caso in the industry's favor, a temporary flurry of activity and an attendant spike in costs would likely occur.

Response: Staff noted that the financial data applied to the development of the proposed filing ended December 31, 2002, so effects of Caso are not reflected at all in much of the available data and are not fully reflected in any of the PCRB's data.

Comment: Staff was cautioned that, in the event that a filing was made specific to Caso or if specific provisions for this decision were included in another filing(s), care would be needed to avoid subsequent "double counting" as the data reported also began to reflect the decision.

Comment: It was noted that a legislative hearing on H.B. 88, a proposed statutory measure to address Caso, was expected in mid-November.

Response: Staff reiterated its need to obtain insurer perspectives on this case, in particular with respect to how the decision was perceived as affecting claim costs and resolution processes, and what the typical impact on costs for representative claims at issue might be.

Question/Comment: If the 2003 legislative session ends without action of H.B. 88, would the legislation carry over to next year or would it expire and require reintroduction?

Response: Neither PCRB staff nor other attendees were certain about the legislative calendar with respect to this question.

Question: Staff was asked if it knew why L&I had not established, and apparently did not intend to establish, a list of approved vocational rehabilitation experts in order to overcome the Caso decision.

Response: Staff emphasized that the PCRB had not been informed about the reasons for L&I's actions and/or position in this regard by any means other than isolated public statements and comments. Staff's impression was that L&I perceived the processes of developing a list, maintaining it and providing access to it could entail large amounts of work and that many other issues were competing for limited resources within and about that agency. An attendee added that the size and considerations pertinent to the composition of the contemplated lists would be very different from location to location and stated that these types of lists might well be very difficult to maintain.

Comment: It was stated that an Insurance Federation of Pennsylvania conference call was planned for the following week on the subject of H B. 88, which the commenter felt evidenced prospects for significant progress on that legislation.

Staff reiterated the PCRB's interest in obtaining carrier and other constituent input that might assist in performing an objective evaluation of the impacts of Caso on the Pennsylvania workers compensation system if the present decision were to be left in effect undisturbed by either court decision or legislation. Some Committee members indicated that they would attempt to obtain such information within their companies and would share any results of that effort with the PCRB.

Question: Recalling that the PCRB had expressed interest in notable cases in addition to Caso, a Committee member asked about the PCRB's understanding of the Gardner case. Staff indicated that the PCRB was aware of the case but did not have instant recollection of the issues involved. For the benefit of all in attendance, the questioner described the decision in general terms as going to the proposition that evaluations of claimants using the American Medical Association Guides to Permanent Impairment could only be done at the point of 104 weeks of total temporary disability benefits, contrary to previously prevailing practice and interpretation that such evaluations could not be done sooner than 104 weeks of total temporary disability benefits but could be done at later dates depending upon the worker's medical condition and other considerations.

Response: Staff noted prior indications that the AMA Guide evaluations were used infrequently, apparently being supplanted in many cases by operation of the compromise and release features of the system. It was noted that the settlement procedure itself might have been advanced by the prospect of potential evaluations of impairment, even in cases where the evaluations were not actually done.

Comment: It was noted that the Gardner case was thought to be on appeal in the Pennsylvania Supreme Court. The potential cost implications of this case include the cost of additional impairment evaluations invoked to comply with the new deadline and developments on cases formerly thought to be eligible for such evaluations beyond the 104 week threshold.

Staff indicated that as a rough starting point for evaluation of the Gardner case, unit statistical reports would provide an authoritative measure of the portion of claims that remain open at 2nd report (a roughly comparable point to the 104-week standard under consideration in Gardner). With respect to insights about how the Gardner decision might influence costs on specific claim scenarios and for loss cost overall, the PCRB invited follow-up comment and/or suggestion.

Loss-Based Assessments and Employer Assessment Factor

Exhibit 13 of the agenda material addressed the above referenced items.

Effective October 1, 1999, the provisions for the Administration Fund, Subsequent Injury Fund and Supersedeas Fund previously included in published Bureau loss costs had been removed from those loss costs. Consistent with requirements of H.B. 1027, these amounts were now treated as a separate charge to insured employers collected through insurers. Loss-based assessments applicable to funding for the Office of the Small Business Advocate remained part of published Bureau loss costs under provisions of this law. Also consistent with past practice, the Bureau continued to include offset provisions for merit rating and credits granted under the Certified Safety Committee Program in published and proposed Bureau loss costs.

Exhibit 13 provided parameters used to compute the proposed employer assessment factor effective April 1, 2004 (0.0236) and the proposed loading to Bureau loss costs to provide for Merit Rating Plan credit offset, Certified Safety Committee Program credit offset and the Office of Small Business Advocate funding effective April 1, 2004 (0.0092). Staff noted that the proposed employer assessment factor was reduced from the current level (0.0280) largely due to increasing premium volume in Pennsylvania. The loading in Bureau loss costs for the remaining factors indicated above was noted as being down nominally from 0.0101, reflecting somewhat lower than expected early response to the 2002 legislative amendment removing the limitation of five years from this program.

Question: Staff was asked if there was a guarantee fund mechanism for workers compensation in Pennsylvania.

Response: The Workers' Compensation Security Fund pays workers compensation benefits for failed carriers in Pennsylvania. Statutory triggers apply to when and in what amount assessments in support of this fund are invoked. Since the adoption of loss cost pricing in Pennsylvania, the PCRB has not accounted for Workers Compensation Security Fund assessments in its loss cost filings.

Question: Is the Security Fund assessment used as an offset to premium taxes?

Response: Comparable assessments ARE used to offset premium taxes in Delaware, but, to the best of staff's knowledge, this was not the case in Pennsylvania.

Pennsylvania Construction Classification Premium Adjustment Program (PCCPAP)

Exhibit 14 of the agenda materials was reviewed with all attendees.

The purpose of the PCCPAP program was described as responding to wage differentials within the construction industry, providing a program of premium credits to higher-wage employers. These credits were offset by loadings applied to construction classifications, reflecting the portion of employers participating in the program and the average premium credit obtained by those participating businesses, thus maintaining the required premium level in each classification.

The table of qualifying wages applicable to the PCCPAP was regularly amended based on actual changes on statewide average wage levels, with such filings subject to review and approval by the Insurance Department and typically effective each July 1.

Staff noted that the average PCCPAP loading indicated, based on the most recent available data, was nominally lower than that currently in effect (3.06 percent proposed vs. 3.23 percent current). This was attributed to the effects of nominal decreases in participation in the program and/or average credits being generated by participating employers.

Staff noted that the PCCPAP program had been revised effective January 1, 2002 to eliminate adjustment of experience modifications in recognition of the effects of PCCPAP credits as the approved means of avoiding providing redundant credits. The adjustment of experience modifications had been seen as a potential impediment to participation on the program. The revised plan made adjustment within the computation of the credits themselves for the effect of high wages on experience modifications. During the interim period in which available historical data reflected the prior plan and proposed new plan parameters were needed consistent with the revised plan, staff was assuming that the alternative forms of adjustment to coordinate experience rating adjustments with PCCPAP credits were equivalent calculations, the intent of the change approved effective January 1, 2002.

Merit Rating Plan

Exhibit 15 of the agenda materials was used as the basis for this discussion.

The Merit Rating Plan was noted as a statutory requirement intended to provide incentive for the maintenance of safe workplaces for businesses too small to qualify for the uniform Experience Rating Plan. Exhibit 15 presented the offset to manual loss costs required to compensate for the net credit received by all eligible employers under this plan, which was shown to have changed only nominally from the level currently in effect (0.36 percent proposed as compared to 0.35 percent currently in effect).

Certified Safety Committee Credit Program

Exhibit 16 of the agenda materials addressed recent experience under the Certified Safety Committee Credit Program. Experience was available for Policy Years 1994 - 2001 inclusive.

Staff noted that until mid- to late-1996 this program did not allow employers to qualify for credit in more than one policy period. As a result, 1995, 1996 and 1997 data were expected to understate the prospective experience under this program after Act 57 had provided for up to five annual credit periods for qualifying employers. Subsequently, in 1999 or 2000 some employers began to reach the limit of five years' of credit application under current law. In 2002 new legislation (S.B. 813) was passed that removed the limit on the number of times an employer could receive such credits. Based on monitoring of ongoing certification activity, staff perceived the early response to this legislation to have been somewhat more muted than had originally been estimated, and the loading to offset ongoing credits was proposed to be reduced from 0.65 percent to 0.55 percent.

Question: Has the PCRB tracked the subsequent experience of employers who left the Certified Safety Committee program?

Response: The PCRB had analyzed the experience of Pennsylvania risks before and during the first four years of participation in the Certified Safety Committee Program. Thus far no work had been done to check experience after participation in the program had ended. It had been seen that of the experience reviewed the best results generally occurred in the year prior to first certification, with the first year of certification being closely comparable to the previous year. In subsequent periods the results were recalled as having deteriorated somewhat.

Comment: An attendee expressed the expectation that the experience of small employers would be too random and variable to support a meaningful analysis of this type.

Response: Staff noted that historically participating employers in the Certified Safety Committee Credit Program have not been particularly "small" and that the PCRB program truly focused on small risks was merit rating.

Question: In Exhibit 13, Line 13, is the factor "0.0092" attributed to the offsets for merit rating, Certified Safety Committee credits and funding for the Office of the Small Business Advocate included in manual loss costs?

Response: Yes. The indicated load factor is included in manual loss costs. As a point of further clarification, staff noted that the effects of changes to the offsets for merit rating, Certified Safety Committee credits and funding for the Office of the Small Business Advocate are not reflected in the overall loss cost changes (on either a collectible or manual basis) in Exhibit 12. The indicated changes shown on Exhibit 12 are developed from experience without consideration of the various surcharges and offsets addressed in Exhibit 13. Finally, it was noted that the Merit Rating Plan and the Certified Safety Committee Credit Program were revenue-neutral programs for which the offsets in manual loss costs were intended only to recover credits given under those respective plans.

Size-of-Loss Analyses

PCRB loss cost filings include rating values pertinent to various rating plans affected by the size of loss for individual claims or occurrences insured thereunder. Some such plans provide limitations applicable to the amount(s) of loss that can be used in computing a retrospective premium. A series of handout exhibits were distributed to attendees and discussed as noted below.

Exhibit 21 presented results of a methodology previously supplied to the PCRB by the NCCI. This method had been used to calculate excess loss (pure premium) factors in some previous PCRB filings. More recent filings had relied heavily on empirical Pennsylvania data as the basis for these values; however, staff had continued to apply the NCCI methodology in order to review its results, as compared to the empirical indications, and in order to be able to use relativities established by the NCCI methods for selected loss values where historical Pennsylvania data was either unavailable or of very limited volume and statistical credibility.

Exhibit 22 presented the most recent available Pennsylvania size-of-loss distribution, derived by tabulating reported loss amounts and developing open claim values so as to produce ultimate loss estimates on a case-by-case basis consistent with the PCRB's analysis of aggregate financial data.

Exhibit 23 showed current and proposed excess loss (pure premium) factors computed using results from Exhibits 21 and 22, together with the indicated percentage changes therein by loss limitation and hazard group.

Size of loss considerations also applied to the determination of state and hazard group relativities that allow a single table of insurance charges and savings to be used in different jurisdictions where benefit levels and statutory provisions may vary significantly. But for some technical differences pertaining to the date to which various calculations are trended, the procedure used to establish these state and hazard group relativities has the same as that used in the NCCI excess loss (pure premium) factor calculation. For the April 1, 2003 filing staff had proposed a revision to the NCCI credibility-weighting process to recognize the volumes of data available in each hazard group, as opposed to the state as a whole. This refinement imparted some additional stability in the indicated state and hazard group relativities for smaller hazard groups (notably Hazard Groups I and IV). This proposed filing would continue that approach. Exhibit 24 presented the derivation of state and hazard group relativities for the proposed filing.

Offering of small deductible coverages at certain specified amounts is mandatory in Pennsylvania. PCRB filings provide loss elimination ratios computed consistent with the mandatory deductible levels. A special consideration arose when computing these loss elimination ratios because Pennsylvania's Statistical Plan does not require separate reporting of losses below $2,000, but a loss elimination ratio is required at a $1,000 deductible. With appropriate adjustment, the needed loss elimination ratios were derived as the complements of per-claim excess loss factors at the specified deductible levels of $1,000, $5,000 and $10,000, as shown on Exhibit 25.

Question: On Exhibit 25, since we are dealing with loss elimination ratios, shouldn't we calculate and show percentage changes based on a formula of 1.0 minus the loss elimination ratio in order to be comparable with procedures used for excess loss pure premium factors?

Response: If the intent of percentage changes is always and only to show affects of premium, the suggested approach would be correct since declining loss elimination ratios do mean that the premium is increasing. However, in the context of credits given for selection of specified deductible options, the available credits are, in fact, decreasing in the proposed filing. Regardless of how one expresses the percentage change, readers must be aware of what is changing and how those changes will affect rating values in order to be properly interpreted.

Retrospective Rating Plan Optional Loss Development Factors

Carriers may apply loss development factors to early evaluations in order to include a provision for maturation of loss values at subsequent reports. Exhibit 26 of the agenda materials provided such development factors applicable without limitation of losses, as well as a procedure that could be used to apply excess loss factors to compute appropriate loss development factors for various loss limitations and hazard groups.

NCCI Filing Memorandum (Item R-1385-2003 - Update to Retrospective Rating Plan Parameters)

Staff directed attention to Exhibit 32, a copy of NCCI's captioned item filing. The PCRB proposed filing the Table of Expected Loss Ranges shown as Exhibit 2 on Page 4 of that filing memorandum for use in Pennsylvania effective April 1, 2004.

Hepatitis C Surcharges for Selected Classifications

Staff noted legislation enacting a presumption of work-related casualty for Hepatitis C incurred by selected sets of workers (H.B. 1633) that was passed in 2002. For its April 1, 2003 Loss Cost Filing the Bureau had conducted an analysis based on available statistics concerning incidence of HCV in the general population in concert with projections of costs made for Hepatitis C cases in healthcare workers under various scenarios by an independent consulting group (Milliman U.S.A., formerly Milliman & Robertson, Inc.). These projections had been compared with existing loss cost estimates for affected classifications, and indicated surcharges had been derived. The Insurance Department's review of the April 1, 2003 filing had suggested that the incidence of HCV in the affected classifications could arguably be comparable to those of the general U.S. population and thus lower than those originally proposed by the Bureau. Ultimately, the Bureau had adjusted the applicable surcharges to be consistent with the incidence of HCV in the general U.S. population. This filing proposed to continue maintaining surcharges at the approved levels.

Question: Is the HCV loading to be treated as a surcharge?

Response: No. Rather than being separate surcharges, the provisions for increased potential for HCV claims are increases to loss costs in the affected classifications. It was noted that the proposed provisions for this exposure provide only nominal increases to the underlying loss costs.

Question: What happens if and when employees in other classifications contract HCV? Is this a compensable disease?

Response: Hepatitis C has always been potentially compensable in Pennsylvania in any classification. At present a worker in a classification other than those included in Exhibit 31 would have to prove that their HCV was work-related, but claims by workers in those classifications included in Exhibit 31 would be compensable unless their employers could prove a lack of work relationship.

Experience Rating Plan

Staff reminded the Committees that a filing that proposed substantial revisions to the existing Experience Rating Plan had been submitted to the Insurance Department in June of 2003. When agenda materials were needed for this meeting, the Bureau had not be advised of the results of the Insurance Department's review of that filing, and so, for the sake of discussion,

several affected exhibits had been compiled and prepared on two alternative bases; one consistent with continuation of the existing Experience Rating Plan (and thus also consistent with a disapproval of the proposed revisions to that plan) and another contemplating adoption of the proposed Experience Rating Plan.

Staff indicated that, apart from the parameters of the Experience Rating Plan itself, nominal changes in indicated off-balance calculations, relativities between classification loss costs and manual level changes in loss costs would also be affected in the event the existing Experience Rating Plan were to be revised but that the overall loss cost change indication was independent of those matters. Staff referred to Exhibits 18, 19 and 27 of the agenda materials as appearing on different bases depending on the resolution of the pending Experience Rating Plan filing.

Exhibit 18 showed historical results of applying the Experience Rating Plan over a period of five successive years organized by year, industry group, and premium size and modification range. As had been noted in previous exhibits of this type, risks in excess of $250,000 in premium across all years and industry groups appeared to have collectively received more responsive adjustments based on their observed favorable or unfavorable historical experience than would have been appropriate to balance these employers' loss ratios with those of all risks as a whole.

Exhibit 19 presented derivation of selected parameters within the current Experience Rating Plan. It was further noted that the collectible premium ratios derived on Page 19.1 of Exhibit 19 were the basis for the relativities by industry group of manual changes in loss costs previously discussed in Exhibit 12.

Exhibit 27 provided the proposed Table B or credibility table for the current Experience Rating Plan, consistent with parameters developed in Exhibit 19.

A handout page providing a summary comparison of the performance of the current and proposed Experience Rating Plans was provided to all attendees. This page compared the extent to which each plan would have been successful in normalizing loss ratios for groups of employers having similar size and receiving either credit or debit modifications, respectively. The analysis showed that the proposed Experience Rating Plan achieved more desirable results in that respect substantially more often than did the current plan.

Question: Are all the risks whose experience is included in Exhibit 18 experience rated?

Response: No. Risks not eligible for experience rating are included in Exhibit 18 (at effective modifications of 1.000) as well. In order to be eligible for experience rating in Pennsylvania, a risk has to have expected losses within the applicable rating experience period at current Bureau loss costs of $10,000.

Proposed Loss Cost Relativities by Classification

Exhibits 17, 20A, 20B, 20C, 28, 29 and 30 of the agenda materials and the Class Book were reviewed with the attendees as follows:

Exhibit 17 presented a narrative discussion of the procedures applied to derive classification loss cost relativities. Staff noted that these procedures were generally unchanged from those

of the most recent previous loss cost filing. With respect to certain "test correction factors" which had historically been applied as matrices of factors differing by type of loss and industry group, the Bureau's April 1, 2003 Loss Cost Filing had completed a transition begun with the April 1, 2001 filing to implement a process of applying test correction factors uniformly across all types of loss and industry groups. The proposed filing would maintain and continue the procedure first used in final form with last year's loss cost filing.

Exhibits 20A, 20B and 20C of the agenda materials were offered as summary tabulations based on unit statistical data used to derive certain parameters applied in the determination of classification loss cost relativities.

Exhibit 28 showed proposed classification loss costs and expected loss factors by classification consistent with the proposed overall change in loss cost level. Exhibit 29 provided insight into the derivation of the proposed classification rating values by showing a test of indicated and selected classification rating values, including effects of capping and application of loadings for the various assessments which would remain a part of published Bureau loss costs.

Exhibit 30 showed a histogram of proposed classification rating value changes based on the proposed overall change in loss cost levels. Staff noted that desirable features of classification loss cost changes included relatively narrow distribution around the average change and few, if any, classifications which materially shift from better to worse than average or vice-versa between successive filings.

A Class Book providing detail of historical experience and derivation of proposed rating values had been distributed with agenda materials mailed prior to the meeting. This exhibit contained tabulations of prior experience data by classification together with the detail of the derivation of individual loss cost proposals in the draft filing. Staff noted that the Class Book as provided was consistent with the current Experience Rating Plan and that a second version compatible with the proposed Experience Rating Plan had not been prepared in recognition of the volume of materials at issue and the fact that the vast majority of data and information that would be shown in such a publication would have been duplicative of the first Class Book.

<u>Auditable Payroll Values Indexed to the Statewide Average Weekly Wage</u>

Staff noted that minimum and/or maximum remunerations for premium computation purposes with respect to some musicians, executive officers and salaried police or firefighters were maintained in specified relationships to the Statewide Average Weekly Wage. In addition, presumed remuneration for premium computation purposes for some taxicab operators were similarly derived. A staff memorandum outlining appropriate revisions to the currently-approved parameters in these cases was presented for discussion.

There being no further business for the Committees to consider, the meeting was adjourned.

Respectfully submitted,

Timothy L. Wisecarver
Chair - Ex Officio

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