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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 Garden Room, 10th Floor of the Hilton Garden Inn Philadelphia Center City, 1100 Arch Street, Philadelphia, Pennsylvania on Friday, December 11, 2009 at 10 a.m.

The following members were present:

Actuarial Committee	
Mr. A. Kerin	Amguard Insurance Company
Mr. K. Rupert	Continental Casualty Company
Mr. C. Szczepanski	Donegal Mutual Insurance Company
Mr. A. Becker	Harleysville Mutual Insurance Company
Mr. J. Fratantaro	Insurance Company of North America
Mr. W. Herr	Liberty Mutual Insurance Company
Mr. K. Brady	PMA Insurance Company
Mr. A. Becker	Selective Insurance Company
Mr. J. Schmidt	Travelers Property & Casualty Company

Classification and Rating Committee	
Mr. I. Feuerlicht	American Home Assurance Company
Mr. S. Reaser	Amguard Insurance Company
Not Represented	Eastern Alliance Insurance Company
Not Represented	Graphic Arts Association
Ms. J. MacMullan	Harleysville Mutual Insurance Company
Mr. T. Mehaffie	Malt Beverage Distributors Association
Not Represented	National Federation of Independent Business
Mr. J. Devlin*	Pennsylvania Automotive Association
Not Represented	Pennsylvania Food Merchants Association
Ms. M. Melewsky	Pennsylvania Newspaper Association
Not Represented	Pennsylvania Retailers' Association
Mr. W. Carney	PMA Insurance Company
Mr. E. White	SeaBright Insurance Company
Mr. S. Zrebiec	Zurich Insurance company

Mr. T. Wisecarver	Chair - Ex Officio

Also present were:

Mr. R. Butera	AmeriHealth Casualty Company
Ms. M. Gaillard	Chartis Insurance Group
Mr. D. Broadwater	Coal Mine Compensation Rating Bureau of Pennsylvania
Ms. M. Innocenti*	Crum & Forster Insurance Company
Mr. S. Cooley	Duane Morris LLP
Ms. K. Ayres	National Council on Compensation Insurance, Inc.
Mr. K. Creighton	Pennsylvania Insurance Department
Mr. E. Zhou	Pennsylvania Insurance Department
Ms. L. Locust*	School Boards Insurance Company of Pennsylvania
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

***** Present for Part of Meeting

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 electronic distribution of agenda materials in advance of the meeting and encouraged all Committee members and other attendees to participate in the meeting by raising questions or posing suggestions as those arose during the course of discussion.

The meeting discussion proceeded to first address the loss cost change indication and its supporting materials. Questions were posed, responses were given and/or discussion ensued as indicated by the “Question,” “Answer,” “Discussion” and “Comment” entries inserted below:

<u>Overall Loss Cost Change Indication</u>

Staff outlined a format for this portion of the meeting discussion. General concepts and processes would first be outlined by reference to selected Preliminary Discussion Exhibits from the agenda materials. References would be made to agenda exhibits containing the counterpart analyses supporting the April 1, 2010 loss cost change indication. Selected agenda exhibits not included in the general overview would be described, and summary results of the PCRB’s analysis of the April 1, 2010 loss cost change indication would be presented for discussion.

The first Preliminary Discussion Exhibit, “Workers Compensation Data Development Illustration–Raw Data,” was introduced. Staff described the organization of information appearing on this exhibit, with policy years of experience appearing on separate rows and successively later evaluation points appearing in columns increasing in age from left to right on the page. The application of this form of data organization to various metrics of workers compensation experience, including premiums, expected losses, and losses or benefit costs was noted. For benefits, staff further described partitions of data into indemnity and medical components and noted the availability of paid and/or case incurred loss data.

The second Preliminary Discussion Exhibit, "Workers Compensation Data Development Illustration–Development Factor Analysis," was addressed next. Staff related the calculated factors displayed on this page to the raw data shown in the first Preliminary Discussion Exhibit. It was noted that data used by the PCRB in preparing its filing indications was provided by hundreds of different insurers and that, in the course of collecting this data, omissions, errors and/or questions pertaining to data quality were encountered. When those considerations precluded the PCRB from using a carrier's or carriers' submissions, data used for development analysis needed to be summarized such that the complement of insurers and insureds represented in each pair of data points used in computing development factors were the same. As a means of maximizing available data, the PCRB effectively constructed successive pairs of diagonals instead of a single triangle, as was used for illustrative purposes in the first two Preliminary Discussion Exhibits.

Considerations encountered when performing development analyses on premiums, expected losses, and paid and/or incurred indemnity and medical losses were identified. Staff noted that the data supporting the April 1, 2010 Loss Cost Filing's loss development analyses was presented in Exhibit 5 of the agenda materials.

The third Preliminary Discussion Exhibit, "Workers Compensation Data Development Illustration–Ultimate Estimates from Development Analysis," was introduced. The mechanics and implications of the calculations shown were briefly described. Staff pointed out that portions of Exhibits 6 and 7 of the agenda materials provided details of the PCRB's estimates of ultimate expected losses and indemnity and medical loss amounts in support of the April 1, 2010 loss cost change indication.

The fourth Preliminary Discussion Exhibit, "Historical Changes in Workers' Compensation Experience," was used to provide background for the PCRB's trend analysis. The use of on-level adjustments in this process was described, and the implications of such adjustments on interpretation of historical data were noted. Staff observed that historical series were available for various metrics pertinent to its annual loss cost filing, including ratios of losses to expected losses and claim frequencies.

Exhibit 8 of the agenda materials was discussed. The importance of claim frequency as a factor in determining loss cost levels was emphasized, the PCRB's review of claim frequency experience was described, and the calculation of "severity ratios" from ratios of loss to expected losses was outlined.

Question: An attendee noted the selected claim frequency trend of -5.9 percent and asked about staff's perspective about using such an historical measure of frequency trend in light of current economic conditions.

Answer: Staff observed that previous PCRB filings had adopted a variety of approaches to trending claim frequency, with such approaches often predicated on the expectation and/or initial indication that claim frequency improvements would be affected by some

factor(s) in such a way as to change historical patterns. Such analyses had not generally been very successful in anticipating subsequent claim frequency changes. For this filing, staff had not applied any adjustments on account of economic conditions and/or other factors.

Comment: Analysis recently published by the National Council on Compensation Insurance, Inc. (NCCI) was referenced and was characterized as finding that claim frequency has historically fallen more rapidly during recessionary periods. It was observed that the approach used in the filing to trend claim frequency was not consistent with that behavior.

Answer: Staff indicated that the PCRB was aware of the NCCI study. The PCRB had reviewed claim frequency data in Pennsylvania since the late 1980s in the context of the recessionary periods that had been identified by NCCI with mixed results. Staff noted that Pennsylvania's economic cycles may not have coincided with the national cycles used by NCCI. Staff expressed the view that the extended period (over 20 years) during which claim frequency had been declining in Pennsylvania was a compelling trend and observed that forecasting changes in that pattern had proven a very difficult enterprise.

Comment: Staff's comments were interpreted as indicating that an average measure of claim frequency derived from a number of recent years was thought to be as good an estimate of future changes as any other approach.

Answer: Staff confirmed its agreement with the position stated.

Question: Inquiry was made as to whether staff had done a specific analysis of loss ratio trends.

Answer: Staff observed that, so long as the time periods used and trend function (linear or exponential) were common to the analysis of claim frequency and claim severity trend, the separate analyses of claim frequency and severity were approximately equivalent to a loss ratio trend analysis. Staff felt that treating the components of loss ratio trend separately was informative, observing the increased ability to fit severity ratios as compared to loss ratios using the same (exponential) model.

Question: An attendee asked whether the PCRB had studied the effect of recessionary periods on claim severity trend.

Answer: Staff answered that it had not undertaken this analysis and indicated that it was unaware of NCCI having done work in this area either. The availability of opposing anecdotal impressions about the likely effects of economic conditions on various components of loss experience was pointed out. This circumstance gave rise to considerable uncertainty when attempting to alter historical trends on account of anticipated economic conditions or changes in such conditions.

The final Preliminary Discussion Exhibit, "Trending Workers' Compensation Data to Future Points in Time," was presented. The purpose of trend analysis and possible choices of methods and/or bases for deriving trend indications were illustrated. The interpretation of a future trended data point as a benchmark for loss cost change indications was described.

Staff observed that portions of Exhibit 6 and Exhibits 9a, 9b, 11a and 11b of the agenda materials addressed various aspects of the PCRB's trend analysis for the April 1, 2010 Loss Cost Filing.

Next staff discussed Exhibit 10 of the agenda materials. Pages 10.1 and 10.2 presented indemnity and medical ratios of loss to on-level expected losses derived using paid and case-incurred loss development methods, as well as the average of those separate indications. Pages 10.3 and 10.4 converted the ratios on Pages 10.1 and 10.2 to severity ratios by adjusting for known changes in claim frequency since 1996. Pages 10.5 and 10.6 presented historical loss ratios based on the average of paid and case-incurred loss development methods, claim frequency trend and claim severity trend with projections to the year beginning April 1, 2010. The significance of the projections to the last annual period reflected on Pages 10.5 and 10.6 was described.

Question:* *Clarification was sought as to whether the graphs under discussion were based on financial data.

Answer:* *Staff responded in the affirmative, with the clarification that the measure of claim frequency used in these graphs was based on unit statistical data excluding large deductible business.

Question:* *An attendee asked whether the PCRB kept claim frequency constant by injury type in the analysis being presented.

Answer:* *The answer indicated that, since financial data did not provide losses by injury type, the separation of loss ratios into claim frequency and claim severity components was accomplished using overall claim frequency rather than frequencies by injury type.

Question:* *Staff was asked how claim frequency experience and/or changes had been different by injury type and/or claim size. Mention was made of previous NCCI findings to the effect that claim frequency improvement had been concentrated in the areas of small claims.

Answer:* *Staff agreed that previous NCCI findings had supported the idea of claim frequency improvement being disproportionately concentrated in smaller, less serious claims but commented that, more recently, the PCRB understood that NCCI was seeing less effect of claim type or size on claim frequency changes. Staff also described a position taken in past reviews of PCRB filings that contended an inverse relationship between claim frequency and claim severity trends, particularly if and when the PCRB had attempted to modify observed historical trends in claim frequency for anticipated adverse effects in the future.

***Question:** The inclusion of payroll in the PCRB's calculation of claim frequencies was noted, and staff was asked whether payroll so applied had been adjusted for wage changes.*

***Answer:** Staff indicated that its claim frequency calculations had not included any wage level or "on-level" adjustment for payrolls. The implications of making such an adjustment were explored, with staff suggesting that, if wages were put on level for purposes of computing claim frequency, then a separate wage inflation value would be needed in the determination of any overall loss costs change indication.*

***Comment:** An attendee observed that the PCRB's claim frequency exhibit had included reference to and adjustment for the Statewide Average Weekly Wage (SAWW).*

***Answer:** Staff acknowledged that the claim frequency exhibit did show a time series of claim frequencies adjusted for the effects of wage inflation, in response to previous Committee questions from past meetings. However, staff indicated that the exhibit in question was used as a source for the claim frequency analysis presented prior to such adjustments and that the claim frequencies at constant wage levels were not incorporated into the analysis of the overall loss cost change indication.*

***Question:** The source of SAWW data shown on the claim frequency exhibit was sought.*

***Answer:** Staff indicated that the wage data in question was believed to have come from unemployment compensation insurance data collected by the Department of Labor and Industry and that this information was the source for annual updates to maximum indemnity benefit levels in Pennsylvania.*

***Question:** It was suggested that the PCRB's methodology was implicitly forecasting wage changes.*

***Answer:** Staff acknowledged that this was the case.*

***Comment:** Similar to the PCRB's treatment of claim frequency and claim severity, an attendee stated that, if wages were expected to change in a fashion differently from the past, then a separate, explicit projection of wage changes might be appropriate.*

***Answer:** Staff indicated that it did not have specific information concerning prospects for future wage changes.*

***Question:** A Committee member asked whether the PCRB could separate paid losses into those payments made on open claims and those made on closed cases.*

***Answer:** Staff replied that financial data did not support such a separation, although for many more recent policy periods unit statistical data did disclose this level of detail.*

Comment: The Committee member observed that their company had seen an increase in paid loss associated with open claims, leading to more development than had historically been the case.

Answer: Staff stated that some time ago closure rates had been deteriorating persistently but that those statistics had been much more stable of late. As a counterpoint to the prospect of increasing payments on open claims, staff recalled previous assertions that payments on closed claims associated with expanded settlement activity could have been overstating estimates of ultimate loss based on paid loss development.

Exhibit 12 of the agenda materials was next offered. The second mailing version of this exhibit was utilized for this portion of the meeting discussion.

Loss ratios selected for indemnity and medical benefits had been posted for each of the three most recent available completed policy years, i.e., 2005, 2006 and 2007. 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 2005, 2006 and 2007 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.

Consistent with the approach in recent previous filings, trend procedures applied in the development of this filing had separated historical experience into frequency and severity components by adjusting policy year on-level loss ratios for actual changes in claim frequency. Historical claim frequencies and the derivation of a prospective claim frequency trend were presented on Page 12.3 of Exhibit 12.

Based on separate measures of policy year loss ratio trend and claim frequency trend, implied claim severity trends were derived. Review of the resulting claim severity ratios showed a notable increase in claim severities in the latest available policy year, Policy Year 2007. After attempts to learn about contributing factors to that increase, staff had applied exponential trend models to claim severity ratios for the most recent seven years (including Policy Year 2007) and for the oldest six of the most recent seven policy years (excluding Policy Year 2007) and had then averaged the results of those two calculations. This approach gave some weight to Policy Year 2007 but assigned less weight to that year than would have been the case using any single exponential model that included Policy Year 2007. The annual indemnity severity trend thus obtained was noted as +4.84 percent, and the counterpart annual medical severity trend was observed to be +5.72 percent.

The average trended on-level loss ratio obtained by applying the combined claim frequency and severity trends was shown on Line (9) of Exhibit 12, and at 1.0068 this ratio produced an indicated 0.68 percent increase in collectible loss costs.

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.

Question: A question was raised regarding the PCRBs treatment of benefit and law changes.

Answer: Staff indicated that the PCRB's compilation of financial data did account for the effects of the previous reforms enacted under Act 44 of 1993 and Act 57 of 1996. These adjustments were intended to remove the effects of those system changes on the data, leaving the intended phenomena of loss development to be assimilated into the PCRBs estimates of ultimate loss. Staff observed that the PCRB did not adjust for annual benefit changes (such as the updating of maximum benefit levels in accordance with changes in the SAWW) separately but rather included those changes in its measures of severity trend. In effect, the PCRB was accounting for those law or on-level changes implicitly rather than explicitly.

Question: An attendee asked what would happen if the change in wages became negative, whether the PCRB was taking this contingency into account and whether the PCRB might be projecting too aggressive a decrease in frequency.

Answer: Staff replied that it had not seen indications that wage growth was becoming negative but speculated that, if such an event were to occur, then carrier premiums would be reduced, and benefit levels for indemnity loss and price levels for medical loss would also be adjusted downward.

Comment: A Committee member noted that the PCRB's filing was trending from 2007 to early 2011. It was thought that some interim period of wage levels (since the end of the PCRB's experience but prior to the mid-point of the new schedule of loss costs) would be known. The suggestion was made to replace the historical rate of change with any known changes within the trend period.

Answer: Differences in the populations for which various wage indications were derived were noted (self-insured, commercially insured or all employers).

Comment: Another Committee member stated that, if wages per hour worked were going down, then trending using past experience (when wages were increasing) might underestimate future claim frequency. However, wage decreases were distinguished from employment levels' impacts on payroll. The speaker opined that workforce reductions were not necessarily attended with wage level reductions for those workers still employed. Reference was made to recent news items in this regard.

Answer: Staff observed that, in the context of discussion of the implications for wages behaving differently in the future than had been the case in the past, those concerns would be true for ratemaking with respect to any and all variables affecting experience data. <u>Any</u> parameter changing in a material and unpredictable fashion would present problems for ratemaking. It was noted that a history of Pennsylvania's SAWW was shown on the third page of Exhibit 8.

Comment: It was suggested that the PCRB consider wage growth projections made by the Federal Reserve Bank or other external sources. This member felt that a constant rate of wage inflation could not be assumed.

Answer: Staff noted that in Pennsylvania SAWW was the benchmark for both maximum indemnity benefits and medical prices.

Comment: One attendee stated that both frequency and severity might require adjustment for anticipated wage changes.

Answer: Staff speculated that such adjustments would tend to offset each other, with the adjustment to claim frequency raising the indication and adjustments to severity reducing the indication.

Question: Staff was asked what the cap was on indemnity benefits.

Answer: Staff indicated that the maximum indemnity benefit was set at 100 percent of the SAWW in Pennsylvania.

Question: An inquiry was made about the procedures that the PCRB used to derive measures of claim severity.

Answer: Staff noted that the overall loss cost change indication was based on aggregate financial data. Initially, ultimate losses and on-level expected losses were used to derive loss ratios, and then known changes in claim frequency (taken from unit statistical data) were used to convert loss ratios into implied severity ratios.

Question: An attendee asked whether the PCRB analyzed severity by type of claim.

Answer: Staff reiterated that financial data was not partitioned by type of claim.

Question: A Committee member observed that claim frequency changes seemed to be moderating. They asked whether staff had given recognition to that moderation.

Answer: Staff noted that Policy Year 2006 had shown an unusually low drop in claim frequency but felt that making use of the most recent seven policy year data points for claim frequency was reasonably responsive to current conditions.

Discussion next proceeded to selected agenda exhibits pertaining to pricing programs as identified following.

<u>Loss-Based Assessments and Employer Assessment Factor</u>

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 PCRB loss costs, had been removed from those loss costs. Consistent with requirements of HB 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 PCRB loss costs under provisions of this law.

With the enactment of HB 2738, an Uninsured Employers Guaranty Fund had been established, with initial funding granted by legislative appropriation and authority given to the Bureau of Workers' Compensation to issue assessments to insurers and self-insurers for additional funding as the need might arise. Consistent with past practice, the PCRB continued to include offset provisions for merit rating and credits granted under the Certified Safety Committee Program in published and proposed PCRB loss costs.

Exhibit 13 provided parameters used to compute the proposed employer assessment factor effective April 1, 2010 (0.0207) and the proposed loading to PCRB 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, 2010 (0.0142). Staff noted that the proposed employer assessment factor was lower than the current level (0.0241) due to declines in budgetary provisions for Administration Fund and Supersedeas Fund expenses and a higher Employer Assessment Premium Base compared to last year. With respect to the Employer Assessment Premium Base, staff was proposing a procedural change which substituted deductible credits at company level instead of PCRB level as had been applied in previous years.

The loading in PCRB loss costs for the remaining factors listed above was noted as being down nominally from 0.0144 due to decreased credit activity in the Certified Safety Committee Credit Program.

<u>Pennsylvania Construction Classification Premium Adjustment Program (PCCPAP)</u>

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 higher than that currently in effect (3.56 percent proposed vs. 3.42 percent current). This was attributed to the effects of increases 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.

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 (0.29 percent), the same level as was currently in effect.

Question: An attendee asked whether the PCRB had studied the loss experience of employers eligible for merit rating credits and whether it was sufficiently better than average to warrant the merit rating credits being applied.

Answer: Staff responded in the negative but noted that an analytical construct suitable for such a review was already being applied to various other pricing programs, such as PCCPAP and for the Certified Safety Committee Program.

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 – 2007 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 and 2000 some employers began to reach the limit of five years' of credit application under current law. In 2002 new legislation (Senate Bill 813) was passed that removed the limit on the number of times an employer could receive such credits. Based on a monitoring of ongoing certification activity, staff proposed a nominal change in the loading to offset ongoing credits from 1.14 percent to 1.12 percent.

Experience Rating Plan

Staff reminded the Committees that substantial revisions to the existing Experience Rating Plan had been approved by the Insurance Department effective April 1, 2004. Attendees were advised that the Experience Rating Plan exhibits provided for discussion at this meeting had been constructed by applying the revised Experience Rating Plan to rating periods occurring prior to the actual implementation of the new plan.

Staff referred to Exhibits 18a, 18b, 19 and 27 of the agenda materials.

Exhibit 18a 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. It was noted that Exhibit 18a presented Experience Rating Plan results prior to the effects of capping, recognizing that the selected capping procedures were intended to mitigate year-to-year movement in experience modifications but would not improve the accuracy of the modifications thus issued. An illustration of some of the effects of the new Experience Rating Plan was provided by reference to Exhibit 18a.

Question: An attendee asked under what circumstances the PCRB would revisit the performance and parameters of the Experience Rating Plan. This person questioned the adjustments applied on the credit side of the rating plan.

Answer: Staff acknowledged some variation in results for credit-rated risks but expressed the view that overall the Experience Rating Plan seemed to be performing well for credit-rated risks. Staff foresaw some problems in attempting to adjust the plan for debit-rated risks, including the impacts of large loses on individual accounts which would overwhelm even large debit experience modifications. The Experience Rating Plan had been substantially revised in 2004. An updated review was expected to be undertaken in the not-too-distant future.

Exhibit 18b was referenced as a summary page formatted identically to Exhibit 18a but reflecting the impacts of capping procedures adopted incrementally with initial swing limits adopted in 2004 and additional transition capping procedures added effective April 1, 2006.

Exhibit 19 presented derivation of selected parameters within the current Experience Rating Plan. It was 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.

Size-of-Loss Analyses

Staff noted that PCRB loss cost filings typically include rating values pertinent to various rating plans affected by the size of loss for individual claims or occurrences insured there under. Some such plans provide limitations applicable to the amount(s) of loss that can be used in computing a retrospective premium. Other portions of this analysis facilitate the application of standard tables to Pennsylvania business.

Staff further noted that many of the size-of-loss studies and rating values proposed in the filing vary by hazard group and that the hazard groups were modified and expanded from four (designated I, II, III and IV) to seven (designated A, B, C, D, E, F and G) hazard groups as part of the April 1, 2009 filing. Those seven can also be combined to form four new hazard groups (A&B = 1, C&D = 2, E&F = 3, and G = 4) for use by carriers during a transition period that will provide time for carrier system changes to be made.

Staff briefly noted that the April 1, 2008 filing analysis had determined that actual loss experience could be used over a significant portion of the size-of-loss range for each type of injury. Various commonly-used distributions had been considered in fitting the empirical size-of-loss distributions, including Single Parameter Pareto, Generalized Pareto, Lognormal, Gamma, Weibull and Exponential. Separate analyses of claim frequency and loss severity were performed. In generating final loss distributions and excess loss factors, actual data (claim counts and dollars of loss) for limits below $500,000 had been combined with fitted counts and dollars above $500,000 and re-accumulated.

Staff then described analysis conducted in support of the April 1, 2010 filing to support expanded hazard groups and excess loss factors applicable thereto. The methods and distributions employed are similar to the approach introduced with the April 1, 2008 filing and repeated for the April 1, 2009 filing.

Exhibit 22 presented the most recent available Pennsylvania size-of-loss distribution, derived by tabulating reported loss amounts and developing open claims, so as to produce ultimate loss estimates on a case-by-case basis consistent with the PCRB's analysis of aggregate financial data. Losses were trended to the midpoint of the prospective rating period. The exhibit also includes actual excess loss factors based on empirical loss distributions by type of injury (death, permanent total, permanent partial, and temporary total), along with excess loss ratios tied to fitted curves for loss limitations of $500,000 and higher.

Exhibit 23 derives proposed excess loss (pure premium) factors computed using results in Exhibit 22 and based on the proposed new hazard group assignments. Note that the process for calculating excess factors in Exhibit 23 is unchanged from prior years, although the loss distributions on which the analysis relies have been updated, and the average costs and weights by type-of-injury and hazard group reflect the most recent data.

Question: Staff was asked why the average severities were consistently increasing across the hazard groups for each given injury type.

Answer: Some possible factors and/or explanations were offered, including the possibility that less hazardous classes might tend to have less serious claims within an injury type(s).

Comment: It was observed that in some situations, even for common types of injuries, the work demands on injured employees might be such that workers in less hazardous classifications would return to work sooner, the residual effects of their injuries notwithstanding, than could other employees whose jobs were more physically active.

Question: The questioner asked why this tendency would hold for fatalities.

Comment: There could be a wage component to this, e.g., more hazardous occupations could command higher wages.

Answer: Notwithstanding the availability of explanatory features, staff observed that the trends under discussion were clearly illustrated in the actual data that had been reviewed and used in the derivation of size-of-loss parameters for the filing.

Question: An attendee noted that excess loss factors for relatively high limits showed large percentage decreases, and asked why this would occur. The question was posed in the context of large changes in the opposite direction having been implemented last year.

Answer: The Committees were reminded that in 2009 the PCRB had changed the way it handled medical losses and that those changes had been a factor in the previous years' revisions. Staff also reported that it had separated losses into those above and below $250,000 in cost. The average costs for claims below this threshold were up from the previous year, while the average costs for losses greater than 250,000 were down. There was effectively a squeezing in on the loss distribution from the ends toward the middle. The average cost for temporary total claims was up 14 percent. Permanent Partial and Permanent Total cases combined were flat. Death claims, because of their limited numbers, do not have much of an impact on the loss distribution or excess loss factors. At the lower ends of the loss distribution, average costs are up more than at higher levels. Thus, at the lower loss limits the PCRB's data does not exhibit the growth it did a year ago. In closing, staff stated that, regardless of whether excess factors were moving upward or downward, higher limits tended to see larger proportional changes.

The 2009 filing had shown increases in the excess loss factors at high limits. The PCRB had changed the way it developed and trended medical losses, previously doing these in the aggregate but more recently doing this analysis by type of injury. Staff also observed that there are only a handful of classes in Hazard Group A, a group that shows large swings in excess loss factors.

Question: Staff was asked if the PCRB had used the same methodology as NCCI in determining its seven new hazard groups.

Answer: Staff indicated that the procedures had been similar, but that, recognizing the many differences in classification procedure between NCCI states and Pennsylvania, the Technical Director of the PCRB's Classification Department had mapped classes and hazard groups between the Pennsylvania and NCCI systems as a starting point for our transition to the new sets of hazard groups.

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. The proposed filing continued a procedure first implemented for the April 1, 2003 filing, which assigned credibility weights by hazard group rather than on a statewide basis. For the April 1, 2009 filing the revision and expansion of hazard groups were without historical (prior year) indicated relativities, to which the compliment of credibility was assigned, so the complement of credibility was assigned to NCCI countrywide average severities. For the April 1, 2010 filing, staff is returning to a procedure consistent with pre-April 1, 2009 filings, and the compliment of credibility can be assigned to prior year relativities adjusted for overall changes in Pennsylvania and countrywide (NCCI states) average severities. Exhibit 24 presented the derivation of state and hazard group relativities for the proposed filing.

Offering of small deducible coverages at certain specified amounts is mandatory in Pennsylvania. PCRB filings thus provide loss elimination ratios computed consistent with the mandatory deductible levels. Exhibit 25 presented the derivation of loss elimination ratios as the complements of excess loss (pure premium) factors. Staff noted the fact that the mandatory $1,000 deductible offer fell below the threshold for required individual claim reporting under the approved Statistical Plan, requiring some special treatment and consideration in the course of the analysis of loss elimination ratios. The revised loss distributions of Exhibit 22 have been incorporated in the derivation of values for limits of $5,000 and $10,000.

Question: An attendee asked whether Pennsylvania was a "gross reporting state" (meaning that in its Statistical Plan losses on deductible policies were reported on a first-dollar basis).

Answer: Staff replied affirmatively that unit statistical loss data was all to be reported on a first-dollar basis in Pennsylvania.

<u>Retrospective Rating Plan Optional Loss Development Factors</u>

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.

<u>Proposed Loss Cost Relativities by Classification</u>

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.

Question: An attendee asked if the PCRB was considering changing Pennsylvania's classification ratemaking procedures to be more consistent with those of NCCI.

Answer: Staff briefly mentioned some of the features of the recent NCCI changes to classification ratemaking. It was noted that the existing Pennsylvania procedures were significantly different from those previously employed by NCCI. Pennsylvania's loss development approach for classification ratemaking measures movement between loss types at each level for ten reports. The process that Pennsylvania uses offers substantial stability. Staff believed that any review of possible merits of elements of the NCCI changes would be done incrementally over time.

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 PCRB 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.

Staff noted legislation enacting a presumption of work-related causality for Hepatitis C incurred by selected sets of workers (HB 1633) that was passed in 2001. As a result of that legislation, the PCRB had introduced a procedure to calculate surcharges applicable to the affected classifications for each subsequent filing through April 1, 2009. The April 1, 2010 filing includes Unit Statistical Plan data for Policy Years 2002 through 2006, and the experience for the HCV claims will have been fully incorporated into the data base. Staff is therefore no longer proposing surcharges to cover exposure initially introduced with HB 1633.

Question: It was suggested that Hepatitis C claims remained open, and staff was asked how the suspension of the surcharges would comport with that circumstance.

Answer: It was agreed that many losses used in classification pricing remained open and subject to valuation changes. Such changes would work their way into loss development over time, whether for disease or traumatic cases. Staff indicated that within the commercial market a review of classification losses for the surcharged classes had not disclosed any claims associated with this exposure.

A Class Book providing detail of historical experience and derivation of proposed rating values had been distributed with agenda materials 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. An exhibit labeled “Index and Supporting Classification Exhibits” was provided for use in conjunction with the Class Book.

Question: Staff was asked whether the PCRB had considered using Delaware experience to supplement the pricing system for non-credible Pennsylvania classifications.

Answer: Staff felt that this approach would not help Pennsylvania to any meaningful extent, due to the very limited amount of exposure available in Delaware. It was further noted that in Delaware “non-reviewed” classes (classifications having less than five percent credibility) were actually priced in part by reference to Pennsylvania classification relativities.

Staff Memorandum Dated November 1, 2009

Professional Employer Organization (PEO) – Executive Officer Salaries
Withdrawal of Endorsement WC 00 01 10 Migrant and Seasonal Agricultural Worker Protection Act Exclusion Endorsement
Addition of New Endorsement WC 00 01 11 Migrant and Seasonal Agricultural Worker Protection Act Coverage Endorsement
Withdrawal of Endorsement WC 00 03 18 – Amendatory Endorsement

Manual language is proposed to clarify that executive officers employed under the provisions of an agreement with a Professional Employer Organization are not subject to the executive officer payroll limitation provisions of the Manual. This interpretation is consistent with practices in most jurisdictions and arises because the individuals in question are not executive officers of the entity under which the workers compensation insurance coverage is being obtained.

The withdrawal of Endorsement WC 00 01 10 and addition of a new endorsement, WC 00 01 11, will correct a previous oversight in the maintenance of PCRB endorsement forms, since this withdrawal and adoption should have been done effective July 1, 1992.

The withdrawal of Endorsement WC 00 03 18 removes a form originally approved for short-term use while existing supplies of forms were used up and was intended to have been accomplished as of March 31, 1994.

The above changes, described in the referenced staff memorandum, are proposed to be effective April 1, 2010.

Staff Memorandum Dated October 21, 2009

Auditable Payroll Values Indexed to the Statewide Average Weekly Wage

Staff noted that maximum remunerations for premium computation purposes with respect to 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 was similarly derived. A staff memorandum outlining appropriate revisions to the currently-approved parameters in these cases was presented for discussion. Changes proposed would move the maximum individual payroll for an executive officer from $2,000 per week to $2,100 per week, increase the annual payroll applicable to taxicab operators in the absence of payroll records from $40,350 to $41,800 and revise the minimum payroll for auxiliary police or special school police appointed by municipalities or townships from $4,050 to $4,200 per year.

The Manual changes set forth in the staff memorandum dated October 21, 2009 are proposed effective on a new and renewal basis April 1, 2010.

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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