National
Council on
Compensation
Insurance, Inc.

NCCI Response to the Report of Mercer Oliver Wyman Actuarial Consulting Inc.: Actuarial Review of the Ratemaking Process of NCCI

NCCI appreciates the opportunity to comment on the report compiled by Mercer Oliver Wyman Actuarial Consulting Inc. ("Mercer"), regarding the ratemaking process of the National Council on Compensation Insurance ("NCCI") in the State of Florida. In general, we believe the report to be thorough and comprehensive in nature. With regard to some of the more specific points in the Mercer review, NCCI offers the following comments:

Regarding Mercer's comments on NCCI's investigation of behavioral changes in key data elements that impacted the actuarial decision making process

Mercer suggests that NCCI should have done further investigation to determine whether it might have been appropriate to change methodologies in the most recent rate filing and give more weight to the paid plus case methodology.

NCCI employs a number of techniques to produce possible indications and then uses actuarial judgment to select the best methods. These methods typically do not vary from year to year in a particular state, unless conditions in the state under review are changing and a new methodology is warranted.

Every year, NCCI examines the results of the two most commonly accepted ratemaking methodologies (the paid methodology and the paid plus case methodology) and for the last four years in Florida, NCCI has averaged the two. While NCCI might choose to implement a "standard method", NCCI recognizes that the option must exist to deviate from that method – providing that a full explanation is made to the regulator – when conditions require. In developing the 1/1/06 Florida rate indication, NCCI added a reform-related downward adjustment to the paid methodology, which was producing the higher indication of the two methodologies, prior to calculating the final average. This resulted in a lower overall indication. With this downward adjustment, NCCI believes it was appropriate to continue to give some weight to the paid methodology.

NCCI accepts that the additional investigation into case reserves suggested by Mercer could be useful, and perhaps as Mercer suggests, might help NCCI better support its position. We would however like to point out that NCCI does a variety of analyses and that NCCI's position was supported by these analyses as well as by the analysis and testimony of an independent and well-regarded consulting actuary. For those reasons, we do not believe, nor does Mercer suggest, that NCCI's final position was in any way flawed.

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Mercer's opinion regarding the lag in the distribution of expected SB 50A savings to individual classes

Mercer notes that NCCI did not distribute the 14% rate reduction effective October 1, 2003 using NCCI's standard classification ratemaking procedure. Rather than permitting some classes to achieve the rate level change indicated by class which could mean that an individual employer's rates might change by more or less than 14%, NCCI applied the "flat factor approach" which means every employer received a 14% rate reduction. In addition, Mercer notes that Florida has a procedure called "swing limits" which limits changes to individual classification rates to a range around the statewide change. Mercer states that the combined impact of these two factors is delaying savings to certain classes.

As Mercer notes, the "flat factor approach" is not NCCI's standard classification ratemaking procedure. It was a unique solution that was implemented with regulatory approval because of practical considerations at the time. In 2003, there was volatility and confusion in the Florida marketplace due to several rate changes which occurred during a short period of time (the 10/1/03 rate change as a result of Senate Bill 50A was the third in a 14 month period). The "flat factor approach", which resulted in a 14% savings to all Florida employers on 10/1/03, expedited the implementation of this change and allowed for employer verification of the savings.

It is important to note that adjustments to individual classifications are revenue neutral. Any delayed savings to certain classes noted by Mercer, to the extent that they are deserved, would be savings which are being redistributed to all other classes. Additionally, the impact of the "flat factor approach" and "swing limits" is only temporary. These methodologies prevent volatility in rates and, over time, each class achieves its appropriate level.

As Mercer notes in its final report, NCCI's ratemaking process in Florida is based on commonly applied actuarial methodologies that are supported in actuarial literature as well as frequency of usage by credentialed actuaries. In addition, Mercer notes that the NCCI ratemaking process is based on data that is appropriate as respects the actuarial methodologies used in the ratemaking process.

NCCI would add that it regularly seeks the opinions of outside consulting actuaries as to whether its actuarial conclusions in the Florida ratemaking process are appropriate. Those consulting actuaries typically present their findings to the Office of Insurance Regulation ("OIR") as part of the ratemaking process. On any NCCI rate filing, the OIR typically has before it additional opinions submitted by outside actuaries including actuaries retained by the Consumer Advocate and the Florida Workers Advocate. Based upon a thorough vetting of all the information that is available from various sources – including NCCI – the OIR issues a decision as to the appropriate rate level for Florida.

NCCI is pleased to have participated in the review process conducted under the leadership of Scott Lefkowitz and Mercer. In its final report on NCCI's ratemaking process, Mercer notes several areas where additional investigation might be valuable in the ratemaking arena. As we examine and adopt suggestions for improvement, NCCI will continue to support Florida's legislators and regulators as they seek to achieve a stable and healthy workers compensation system.

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