



**THE WORKERS' COMPENSATION
RATING AND INSPECTION BUREAU**

April 27, 2011

CIRCULAR LETTER NO. 2178

To All Members and Subscribers of the WCRIBMA:

**GUIDELINES FOR WORKERS' COMPENSATION RATE DEVIATION FILINGS
SEPTEMBER 1, 2011**

Attached are the updated Guidelines For Workers' Compensation Rate Deviation Filings Filed by Workers' Compensation Insurers and Self-Insurance Groups that were recently released by the Division of Insurance.

These guidelines indicate the required elements of deviation filings and other plans subject to review under the deviation statute and also provide the timeframes for filing or continuing individual carrier rate deviations, following the promulgation of workers' compensation rates, effective September 1, 2011.

Any questions regarding these guidelines should be directed to Walter Horn at the Division of Insurance, telephone number (617) 521-7335 or by e-mail Walter.Horn@state.ma.us.

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Vice President – Customer Services

Attachment

A. General

Massachusetts General Law Chapter 152, §§ 25O and 53A.
Classification of risks and premiums; distribution of premiums among employers.

1. Who May Insure Workers' Compensation Risks

- Any insurance company authorized to transact business in this Commonwealth under subclause (b) or (e) of 6th clause of M.G.L c. 175, §47, except as provided in clause (c) of M.G.L. c. 175, §54.
- Individual self-insurers authorized to transact business under M.G.L. c.152, §25A.
- Workers' compensation self-insurance groups authorized to transact business under M.G.L. c. 152, §25E-U.
- Municipal property-liability insurance groups authorized to transact business under M.G.L. c. 40M.

2. Authority for Rate Deviations

(a) The authority for workers' compensation insurance companies to make downward deviations in rates is provided in M.G.L. Chapter 152, §53A(9):

Any insurance company may make written application to the commissioner of insurance for permission to use, in place of premium rates approved pursuant to subsections (7) and (8), a percentage decrease from said premium rates which shall be uniform within any classification of risk in the commonwealth. The commissioner shall issue an order permitting the decrease for such insurance company unless he finds that the resulting premium would be inadequate or unfairly discriminatory.

(b) The authority for workers' compensation self-insurance groups ("SIGs") to make deviations in rates is provided in M.G.L. Chapter 152, §25O(3) and 211 CMR 67.09(4):

A group may apply to the Commissioner for authority to make its own rates. Such rates shall be filed with the Commissioner and shall be based upon at least two fund years, consisting of not less than twenty-four months, of the group's experience, to the extent actuarially credible. A public employer safety group in operation for at least two consecutive years before it applies for approval to operate as a public employer group, may apply to the Commissioner to make its own rates immediately. In no event shall a group determine members' premium contributions by any method other than that prescribed herein without the prior written approval of the Commissioner. In no event shall a group make a distribution to its members, other than dividends, without the prior written approval of the Commissioner.

(c) The authority for municipal property-liability groups to make deviations in rates is provided in M.G.L. c. 40M §11, subsection A:

“A group shall file with the commissioner its rating plan.”

3. DIA Assessments

Please note that, pursuant to M.G.L. Chapter 152, §65, Department of Industrial Accidents (DIA) assessments must be based on **standard premium** as defined by that agency (prior to the application of any ARAP [All Risk Adjustment Program] surcharge). Therefore, no deviation or schedule credit program will be approved that allows for any reduction in this assessment. In addition, all deviations or scheduled credits to premium shall be off Bureau manual rates, prior to the application of experience rating, merit rating, ARAP surcharges, construction credits, deductible credits, or premium discounts.

B. Guidelines for Workers' Compensation Rate Deviation Filings

1. Contents of Filings

New or renewal rate deviation filings must include the following elements:

- a) A demonstration that the filed rate deviation would not produce unfairly discriminatory rates. Insurance company groups must include the objective underwriting criteria used for every company within the group except that company writing at the level least favorable to employers. Insurance company groups should submit no more than one filing covering all of its member companies. Each insurance company group filing must include a summary document that sets forth the rate sought for each member company and the objective, non-overlapping eligibility criteria that will be used to determine which risks will be written by the various group members. Company groups must maintain detailed underwriting information supporting both the placement of each insured into a particular company and, if there is an approved schedule credit program (see below), the application of any schedule credit.
- b) A demonstration that such rate deviation will not threaten the filer's solvency. (SIG deviation filings must also include a rate review performed by a qualified actuary.)
- c) An estimate of the annual net premium to be written on an after-deviation basis by the filing company and the latest available three policy years of Massachusetts voluntary workers' compensation loss, expense, and premium experience. (SIGs are required to provide only two years of data and are expected to submit a pro-forma income statement showing that the rate will be adequate to pay all losses and expenses.)

- d) A description of how the filed deviation will be applied to the current rates, rating values, programs, and procedures. Such rating methodology must conform to the Premium Algorithm most recently promulgated by the Workers' Compensation Rating and Inspection Bureau of Massachusetts ("WCRIB").
- e) On an *individual company basis*, for each of *policy* years 2007, 2008, and 2009, the following dollar amounts:
 - 1) Massachusetts standard premium at bureau Designated Statistical Reporting level; 2) premium adjustments due to All Risks Adjustment Program premium; 3) cumulative paid indemnity losses; 4) case indemnity loss reserves; 5) cumulative paid medical losses; and 6) case medical loss reserves. The evaluation date should be the latest available year-end evaluation, and this date should be identified. All values should be defined consistent with the corresponding values reportable on Call #2 of the Massachusetts Workers' Compensation Statistical Plan (Part II).
- f) On a *reporting group basis*, dollar values and percentages of standard earned premium for each of *calendar* years 2007, 2008, and 2009:
 - 1) Commission and Brokerage Expense; 2) All Other acquisition expense; 3) Direct Written Premium; 4) Direct Standard Earned Premium; 5) Adjusting and Other Expenses; 6) Defense and Cost Containment Expenses; and 7) Direct Losses Net of Deductibles. All values should be defined consistent with the corresponding values reportable on Call # 6 of the Massachusetts Workers' Compensation Statistical Plan (Part II) and/or with statutory Page 14 Annual Statement filings.
- g) A completed Deviation Abstract form (referenced in the Division online checklist).
- h) If the filing includes a request for a -15% or greater deviation for any class,* an actuarial justification demonstrating that such a rate deviation will not result in inadequate premiums and a signed certification by an associate or fellow of the Casualty Actuarial Society indicating (i) that he or she has reviewed the material submitted to the Division; (ii) that this material is true and accurate to the best of his or her knowledge, information, and belief; and (iii) that it is his or her opinion that the premiums resulting from the proposed deviation will be adequate, and neither predatory nor likely to be destructive of competition in the Commonwealth.

A group wishing to apply different deviations to different 'classes' (i.e., workers' compensation industrial classifications currently approved by the Division for the entire industry) must provide all of above elements (a)-(h) for the relevant individual classes or groups of classes.

2. Schedule of Filings and Effective Dates

(a) Workers' Compensation Insurance Companies

Any WCRIB member wishing to retain any currently approved deviation without alteration beyond August 31, 2011, must inform the Division of this intent by email to the address below by July 29, 2011. Any member wishing to offer a new or altered rate deviation or schedule rating plan to be effective on September 1, 2011, must submit its filing in SERFF on or before August 5, 2011. If requested by the filer and approved by the Division, such timely filed program effective September 1, 2011 (or any later date requested), regardless of the date of its approval by the Division.

No deviation or schedule rating plan filing approved to be effective on or before August 31, 2011, may be used by any company beyond that date, unless (i) the currently approved deviation was made through SERFF; and (ii) the SRB has received written information on or before July 29, 2011 from the company group that includes such company, requesting that the group be allowed to continue its approved deviation or schedule rating program by applying it, without alteration, to risks written on or after September 1, 2011. For all new and renewal policies effective on or after September 1, 2011, WCRIB member companies shall use rates calculated in accordance with the Commissioner's order relative to such policies, but may apply any deviations or schedule rating plans that are newly approved or have been allowed to continue in effect as set forth in these guidelines.

The notification of intent to continue to use a previously approved deviation may be emailed to the State Rating Bureau care of walter.horn@state.ma.us

(b) Workers' Compensation Self-Insurance Groups

SIG deviations may be effective only on a fund-year basis, (generally, January 1 - December 31.) To permit the orderly implementation of the rates set forth in the Commissioner's order regarding rates effective September 1, 2011, and to avoid disruption in the market, all groups must continue to use the currently approved rates until the end of the current fund year.

SIGs wishing to deviate from the September 1, 2011 rates may continue to use their currently approved rates or may use September 1, 2011 rates as provisional rates for the subsequent fund year, however, any provisional rates must be adjusted as soon as a new rate is approved.

SIGs must file deviation requests no later than 45 days after the due date of their Annual Statement. All deviations expire at the end of the SIG's fund year, but, if there has been no change in the approved overall rates, the deviation may be extended for a subsequent year by a written request to the Division, in conjunction with a review of the SIG's Annual Statement to assure that the rate is adequate.

(c) Municipal Property-Liability Groups

— A “40M” group is not required to obtain the approval of the Commissioner for its rates or rating plan., but must file such rates with the Commissioner before they may be used.

3. FILING PROCEDURES

- **All filings must be made via SERFF along with the appropriate filing fee.**

Failure to provide all material required by these guidelines will result, at a minimum, in delays in the processing of applications and may result in the disapproval of requested rates, effective dates or other plan parameters.

C. PLANS SUBJECT TO REVIEW UNDER RATE DEVIATION STATUTES

Workers' compensation insurance companies should be aware that the Division of Insurance regards certain rating plans, including some plans referred to as "dividend plans," "retention plans," "installment plans," "retrospective rating plans," or "deferred payment plans," as operating, at least in part, as rate deviations, and as therefore being subject to prior approval by the Division. *In particular, any program guaranteeing or otherwise promising premium reductions at any time, and any program allowing for the return of, or reduction in, premium during the policy period, is viewed by the Division as a rate deviation that must be submitted for approval prior to use.* Furthermore, premium installment plans with terms allowing for the payment of any installment after the end of the policy period will also be considered deviations. Unless otherwise permitted by the Division in writing, retrospective rating plans must be in compliance with the Retrospective Rating Plan Manual and must use rating factors approved for use by the Commissioner during the applicable period.

IT SHOULD BE NOTED THAT ALTHOUGH SCHEDULE RATING PLANS MAY BE APPROVED FOR WORKERS' COMPENSATION INSURANCE COMPANIES, THEY ARE PROHIBITED FOR WORKERS' COMPENSATION SELF-INSURANCE GROUPS.

Within SIGs, premium installment plans with terms allowing the member to pay less than 25% of the premium on the effective date of the policy and the balance in equal monthly or quarterly installments within the first eight months of the fund year are prohibited (211 CMR 67.06(2)(b)(8)+. The only dividend plan permitted is that described in the regulation (211 CMR 67.08 (2)(d)(4)+.

Schedule rating-type plans for traditionally insured workers' compensation risks are allowed only pursuant to the above-quoted deviation statute and these guidelines, and are subject to prior approval by the Division. Such plans, regardless of the magnitude of the credits offered, may not provide for "upward deviations," non-uniformity of rates within any class, or unfairly discriminatory rating. In addition

to all of the requirements set forth for deviation applications above, schedule credit programs will be approved only if:

- (i) They contain no schedule debits;
- (ii) They are retrospective in nature (i.e., all credits are earned during the relevant policy period, and not *guaranteed* at policy inception), and the insurer, subsequent to the policy period, actually determines the appropriate credit and adjusts the premium accordingly;
- (iii) Each employer written in any company that is offering such a plan is, at policy inception, capable of earning the maximum credit available to any risk in that industrial classification written by that company;
- (iv) All schedule credits offered are determinable by objective, unambiguous, and non-discriminatory criteria approved by the Division;
- (v) The company's filing for such plan provides the estimated percentage and dollar impact of the requested schedule rating plan credits. This shall be accomplished by filling out the following table for the period the schedule credits are expected to be in effect;

Time Period Covered in Following Estimate of Impact:

| Range of Projected Credit Percentage | Number of Policies | Earned Premium* | Average Estimated Percent Credit ** | Incurred Losses *** | Loss Ratio |
|--------------------------------------|--------------------|-----------------|-------------------------------------|---------------------|------------|
| 0%**** | | | | | |
| -1% to -5% | | | | | |
| -6% to -15% | | | | | |
| -16% to -25% | | | | | |
| Bigger than -25% | | | | | |
| Total / Average | | | | | |

- * Premium is the standard earned premium at the company rate level after experience rating, deviations and **estimated** schedule credits, but before premium discount and retrospective rating.
- ** The average credit expected to be received by all policyholders in each "Credit Percentage" range. This should be used to calculate earned premium and loss ratios.
- *** Incurred losses are the case incurred losses consisting of paid plus case reserves. Do not include incurred but not reported losses (IBNR).
- **** Exclude any servicing carrier or VDAC business.

- (vi) The filer has submitted a signed certification by an Associate or Fellow of the Casualty Actuarial Society indicating that he or she has reviewed the material submitted to the Division; that this material is true and accurate to the best of his or her knowledge, information, and belief; and that it is his or her opinion that, based on company-specific or other relevant information, the proposed schedule credits are actuarially justified in the sense that reductions in losses that are commensurate with the credits offered can reasonably be expected to result from the various credited activities, and that the premiums resulting from the proposed schedule rating plan will be adequate and not unfairly discriminatory, and will not threaten the solvency of the company. The filer should include all supporting documentation and analysis for the opinion of the actuary that the plan is actuarially justified; and
- (vii) Any insurer for whom workers' compensation schedule rating is not new in Massachusetts must also include in its filing a grid that indicates how much premium volume has received the various available credits, as well as the loss ratios obtained by each group of risks. This grid must be of the following form and must include data from all policies written in the company between 1/1/08 and 12/31/09.

Actual Historical Impact of Schedule Rating Plan

| Range of Actual Credit Percentage Granted | Number of Policies | Earned Premium* | Average Estimated % Cred. at Incep.** | Incurred Losses *** | Loss Ratio |
|---|--------------------|-----------------|---------------------------------------|---------------------|------------|
| 0%**** | | | | | |
| -1% to -5% | | | | | |
| -6% to -15% | | | | | |
| -16% to -25% | | | | | |
| Bigger than -25% | | | | | |
| Total / Average | | | | | |

* Premium is the standard earned premium at the company rate level after experience rating, deviations and **actual** schedule credits, but before premium discount and retrospective rating.

** The average credit estimated at policy inception for all policyholders in each "Credit Percentage" range. This value may be different from the average credit actually received as specified in the left-most column above. **[NB: This differs from the 4th column in the projection grid by containing the average percentage credit**

actually applied to policyholder premiums prior to recalculation at audit. This percent should *not* be used to calculate earned premiums or loss ratios unless the credits actually received after audit matched those estimated at policy inception.]

*** Incurred losses are the case incurred losses consisting of paid plus case reserves. Do not include incurred but not reported losses (IBNR).

**** Exclude any servicing carrier or VDAC business.

3. Large Deductible Policies

211 CMR 115.00: Requirements Applicable to Large Deductible Policies

(1) The following features must be included in all large deductible policies:

- _____ (a) Only those Massachusetts insureds whose workers' compensation full coverage standard premium plus ARAP would otherwise exceed \$375,000 of Massachusetts premium are eligible, provided, however, that insureds with either (i) at least \$50,000 of annual non-Massachusetts workers' compensation premium or (ii) at least \$10,000 of annual non-Massachusetts workers' compensation premium and payroll in at least two states other than Massachusetts, need have only \$100,000 or more in countrywide workers' compensation premium to be eligible to be written on large deductible plans.
- _____ (b) The policies may not provide cancellation provisions that differ in any respect from those contained in the standard Massachusetts workers' compensation policy.
- _____ (c) A reasonable aggregate deductible limit must be included. For insureds having less than \$500,000 in countrywide worker's compensation premium, such aggregate limit may not exceed three times standard premium.
- _____ (d) The per claim deductible must be at least \$75,000.
- _____ (e) Rates, policy forms and deductible endorsements must be filed with and approved by the Division of Insurance. An example of an acceptable rating formula is set forth on the following pages.

**Example of Approvable Rating Formula for
Workers' Compensation Large Deductible Policies Pursuant to 211 CMR 115**

Parameters

Per Claim Deductible. The per claim loss (and allocated loss adjustment expense –“ALAE”– amount, if elected) that will be paid by the insured. This amount is agreed upon by insurer and insured and is subject to the minimum amount listed in 211 CMR 115.05(2)(d).

Aggregate Deductible. The aggregate loss (and ALAE amount, if elected) that will be paid by the insured. This amount is agreed upon by insurer and insured and is subject to the maximum amount listed in 211 CMR 115.05(2)(c). All large deductible policies are required to include an aggregate deductible in accordance with 211 CMR 115.05(2)(c).

Formulas

$$\begin{aligned} \text{Deductible Premium} &= \{ \text{Per Claim Deductible Charge} + \text{Aggregate Deductible Charge} + \text{Expense Provision} + \text{Residual Market Provision} + \text{Insolvency Fund Provision} \} \times \text{Adjusted Tax Multiplier} \\ \text{Deductible Credit} &= 1 - \{ \text{Deductible Premium} / \text{Standard Premium} \} \end{aligned}$$

Values

Per Claim Deductible Charge. This is the premium charge associated with the portion of losses (and ALAE, if subject to the deductible) expected above the per claim deductible amount. It is equal to the excess loss factor (or the excess loss and allocated expense factor, if ALAE is subject to the deductible) associated with the agreed upon per claim deductible amount, as found on the current approved Retrospective Rating Plan Manual Massachusetts Special Rating Values pages times the standard premium.

Aggregate Deductible Charge. This is the premium charge associated with the portion of losses (and ALAE if subject to the deductible) expected above the aggregate deductible amount. It is equal to the insurance charge for the entry ratio associated with the selected aggregate deductible amount, found in the state approved Retrospective Rating Plan, times the expected limited losses (and ALAE, if subject to the deductible). The expected limited losses are equal to standard premium times the difference between the expected loss ratio and the excess loss factor, associated with the per claim deductible amount, found on the current approved Retrospective Rating Plan Manual Massachusetts Special Rating Values pages (or equal to standard premium times the difference between the expected loss and allocated expense ratio and the excess loss and allocated expense factor, if ALAE is subject to the deductible) as shown below.

$$\text{Aggregate Deductible Charge} = \text{Standard Premium} \times \text{Insurance Charge} \times \{ \text{Expected Loss Ratio} - \text{Excess Loss Factor} \}$$

The insurance charge is derived from Table M of the Retrospective Rating Plan Manual. It is a function of the entry ratio and the expected loss group.

The entry ratio is calculated by dividing the aggregate deductible amount by the product of standard premium and the expected limited loss ratio (or expected limited loss an allocated expense ratio, if ALAE is subject to the deductible).

The expected loss group is based on the product of the expected unlimited losses, the hazard group differential, and the loss group adjustment factor (LGAF). The loss group adjustment factor is calculated as shown below:

$$LGAF = \left\{ 1 + \left[\frac{(.8 \times LER)}{(1.0 - LER)} \right] \right\}$$

$$LER = \frac{\text{Excess Loss Factor}}{\text{Expected Loss Ratio}}$$

Expense Provision. This is the premium charge that covers expenses, profit and contingencies associated with the large deductible policy. The expense provision is equal to the standard premium times the expense factor found in the Table of Expense Ratios – Excluding Taxes and Including Profit and Contingencies table in the state approved Retrospective Rating Plan. (If ALAE is subject to the deductible, the expense ratio found on the Table of expense Ratios – Excluding Allocated Loss Adjustment Expense and Taxes and Including Profit and Contingencies should be referenced instead.)

Residual Market Provision. This is the premium charge that covers the residual market subsidy, which is applicable to full coverage premium for large deductible policies. The residual market provision is equal to the residual market subsidy provision shown on the current approved Retrospective Rating Plan Manual Massachusetts Special Rating Values pages multiplied by standard premium.

Insolvency Fund Provision. This is the premium charge that covers the insurers' insolvency fund assessment, which is applicable to full coverage premium for large deductible policies. The insolvency fund provision is equal to the insolvency fund provision shown on the current approved Retrospective Rating Plan Manual Massachusetts Special Rating Values pages multiplied by standard premium.

Adjusted Tax Multiplier. The adjusted tax multiplier is applied in order to cover taxes associated with the large deductible policy. Since the residual market subsidy and the insurer's insolvency fund assessment is separately accounted for in the calculation, the tax multiplier found on the current approved Retrospective Rating Plan Manual Massachusetts Special Rating Values pages must be adjusted to remove the residual market subsidy and the insurer's insolvency fund assessment before being applied. The following formula is used to calculate the adjusted tax multiplier.

$$\text{Adjusted Tax Multiplier} = 1 / \left\{ (1 / \text{Tax Multiplier}) + \frac{\text{Residual Market Subsidy}}{\text{Insolvency Fund Assessment}} \right\}$$

Standard Premium. The standard premium referred to in the large deductible calculations includes any All Risk Adjustment Program ("ARAP") Surcharge.