



**DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION**

P.O. Box 690, Jefferson City, Mo. 65102-0690

**In Re:** )  
 ) **DIFP Case No. 150330230C**  
**Travelers Rate Filing for the** )  
**Workers' Compensation Alternative** )  
**Residual Market** )

**FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER**

This matter concerns proposed changes to the rates and rating structure to be used in the Missouri Alternative Residual Market Plan ("A.R.M. Plan" or "Plan") beginning July 1, 2015. The A.R.M. Plan was created under the authority of § 287.896, RSMo, and 20 CSR 500-6.960 as a mechanism to provide workers' compensation and employer's liability insurance to applicants who are in good faith entitled to such coverage but who are unable to purchase such coverage by ordinary methods through the voluntary market. The A.R.M. Plan began operation on July 1, 1995, and is currently administered by Travelers Property Casualty Company of America ("Travelers"), which was selected by the Department of Insurance, Financial Institutions and Professional Registration ("Department") as the Contract Carrier following an Invitation For Bid issued in January 2015.

In accordance with the A.R.M. Plan, Travelers submitted its proposed rate filing ("Filing") with the Department on March 10, 2015, by which it sought rate changes for the new contract period beginning July 1, 2015. (Exhibit 1). Included within the Filing was Travelers' proposal for manual rates at the detail class code level. (Exhibit 2).

As required under § 287.896, RSMo, a public hearing was held concerning the Travelers' Filing. The hearing was conducted at the Department's Jefferson City offices on May 5, 2015. Travelers introduced the various documents that constituted its Filing into evidence and explained them through the testimony of Jonathan B. Hale, FCAS, Vice President and Actuary for Travelers. The Department's actuary, Julie Lederer, FCAS, MAAA, provided testimony regarding her review of the Travelers' Filing.

## FINDINGS OF FACT

**1. Effective Date:** If approved, the premium rate changes proposed in Travelers' Filing will go into effect on July 1, 2015.

**2. Expert Witnesses:** Both Mr. Hale and Ms. Lederer demonstrated that they are qualified to provide expert testimony regarding workers' compensation residual market rate matters.

**3. Indicated Premium Level Need:** At the 110% loss ratio retention level option authorized by 20 CSR 500-6.960, Travelers' Filing proposes changes to the existing A.R.M. Plan rates and rating structure which would result in an overall premium level change of -4.7%. This proposed premium level was determined by Travelers based on its analysis of the Plan's "premium level need" for the upcoming contract year of July 1, 2015 to June 30, 2016. This premium level need analysis compared the expenses likely to be incurred by the Plan during this upcoming period with the premium likely to be received during the same period (without any premium increase or decrease). This analysis revealed that the premium likely to be available to Travelers would exceed the likely expenses of the Plan. The various expense items included in this premium need analysis were summarized at Section II, page 2 of Travelers' Filing, which indicated the following:

<u>Cost Items</u>	<u>Estimated % of Premium</u>
1. Expected On-Level Loss & ALAE Ratio	69.7%
2. General Expenses (Excluding Commissions)	9.6%
3. Unallocated Loss Adjustment Expenses	4.5%
4. Agents' Commissions	3.6%
5. Loading for Taxes, Licenses & Fees	2.0%
6. Loading for Uncollectible Premiums	4.2%
7. Catastrophic Provision-Certified Terrorism	0.2%
8. Loading for Profit and Contingencies	2.0%

Using the item numbers from the Cost Items listed above and their corresponding premium percentages, the premium level need calculation is set forth below.

$$\frac{[(\text{Cost Item 1} + \text{Cost Item 2} + \text{Cost Item 3} + \text{Cost Item 7})}{(1 - \text{Cost Item 4} - \text{Cost Item 5} - \text{Cost Item 6} - \text{Cost Item 8})} - 1.00 = \text{Premium Level Need}$$

$$\frac{[(0.697 + 0.096 + 0.045 + 0.002)}{(1 - 0.036 - 0.02 - 0.042 - 0.02)]} - 1.00 = -0.047$$

Proposed premium level change = -4.7%

Findings of Fact 4 through 11, below, discuss in more detail Travelers' explanation for each of the eight Cost Items listed above.

**4. Expected On-Level Loss & ALAE Ratio:** Travelers used the frequency/severity method in its rate request, developing separate projections of the estimated claim counts (the frequency) and the average loss and allocated loss adjustment expenses (“ALAE”) (the severity) for the upcoming contract year. The bulk of the spreadsheets contained in the Filing represent the steps needed to arrive at this estimate of loss and ALAE. Travelers ties all these steps together to produce the loss and ALAE ratio to premium of 69.7% for the upcoming year used in Travelers’ premium level need calculation. (See Filing Section III, page 2.)

**5. General Expenses (Excluding Commissions):** Many of the remaining elements of Travelers’ premium level need calculation are related to the expenses associated with administering the Plan. Cost Item 2 of the calculation concerns General Expenses (Excluding Commissions). Page 2 of Section IX of Travelers’ Filing sets forth the various anticipated expense levels contemplated by General Expenses for the upcoming contract period:

	<b>2015 Filing</b>
Estimated Premium (2015 Contract Year):	\$31,378,000
Estimated No. of Insureds (2015 Contract Year):	3,692

<u>Category of General Expense</u>	<u>Amount</u> <u>(,000)</u>	<u>% of</u> <u>Premium</u>
Underwriting, Policy Issuance & Rating/Billing	\$706	2.2%
Missouri Injury Management Program	\$90	0.3%
Data Processing	\$787	2.5%
Premium Audit	\$310	1.0%
Loss Control and Prevention	\$471	1.5%
Actuarial, Finance, and Human Resources	\$277	0.9%
Other Overhead	<u>\$385</u>	<u>1.2%</u>
Total	\$3,026	9.6%

On April 3, 2015, Mr. Hale informed the Department that there was an error in the Filing’s general expense provision. The general expense percentage increases from 9.6% of premium to 9.9% of premium when this error is corrected, and the overall premium level change increases from -4.7% to -4.4%. Travelers did not submit a revised filing to correct the error. This issue is discussed in Ms. Lederer’s Report (Exhibit A) on page 18, third paragraph. Ms. Lederer used the corrected general expense provision when developing her range of reasonable premium level changes. Whether Travelers utilized the original general expense of 9.6% or the corrected general expense of 9.9%, the resulting overall rate change would still fall within the actuarially reasonable range. Further, because this error benefits consumers while still not being inadequate to Travelers, it is not necessary for it to be modified.

**6. Unallocated Loss Adjustment Expense:** Travelers based the A.R.M. Plan’s ULAE calculation on the ULAE-to-loss percentage filed with the Department by the National Council on Compensation Insurance, Inc. (“NCCI”) in its Missouri Loss Cost Filing, effective 1/1/2015; that number was 7.3%. From that number, Travelers calculated the A.R.M. Plan’s ULAE for medical and indemnity claims as 4.5% of premium (Filing Section IX, p. 4) for the upcoming contract year.

**7. Loading for Taxes, Licenses & Fees:** Travelers anticipated paying taxes, licenses and fees at the equivalent of 2.0% of premium. The amount includes premium to pay the current Missouri Workers' Compensation Administrative Tax, the Missouri Property and Casualty Guaranty Fund assessment, and miscellaneous taxes such as personal property taxes, National Association of Insurance Commissioners (NAIC) zone examinations, and agent license fees. (See Filing Section IX, p. 5)

**8. Agents' Commissions:** Travelers compared its A.R.M. premium for nineteen previous contract periods with the agent commissions it paid in those periods, and then calculated the corresponding commission "rates." Travelers selected 3.6% for the upcoming contract period based on historical commissions. (See Filing Section IX, p. 6.)

**9. Loading for Uncollectible Premium:** The Filing provides the history of uncollectible premiums for the A.R.M. Plan on Page 7 of Section IX. Travelers calculated several different averages, and finally selected -4.2% for contract year 2015.

**10. Catastrophic Provision – Certified Terrorism Losses:** Since 2003, Travelers has included a catastrophe provision for foreign terrorism losses. The Filing uses a load of 0.01 per \$100 of payroll, which is consistent with the most recent NCCI loss cost filing that became effective 1/1/2015. This amount of terrorism funding is estimated to represent 0.2% of the premium in the A.R.M. Plan. (See Filing Section X, p. 2.)

**11. Profit & Contingency:** The Filing includes Cost Item 8 ("Loading for Profit and Contingencies"), with a profit load of 2.0% of premium. Ms. Lederer testified that the profits were reasonable for the assigned risk pool.

**12. Proposed Allocation of a Rate Increase Among Class Codes:** Travelers' Filing included a proposal for manual rates at the detail class code level. The proposal attempts to better align the overall rates with the voluntary market loss costs filed by the NCCI that became effective on 1/1/2015.

According to Travelers, the rates will align with NCCI loss costs except in instances where they have deemed the premium impact to be too severe to be taken at once. To avoid large rate increases to employers, Travelers proposes that increases be capped at 15%, plus one-quarter of the difference between the indicated rate change and +15%. In addition, decreases are capped at -15% plus one-quarter of the difference between the indicated rate change and -15%. (Exhibit 2, letter titled: Enclosed Manual Rate Proposal for the Missouri Workers Comp Alternative Residual Market –Effective 7/1/2015)

**13. The Department's Actuarial Analysis of Premium Level Need:** Travelers' actuary, Mr. Hale, testified that the proposed rates were neither excessive nor inadequate, nor were they unfairly discriminatory. The Department's actuary, Ms. Lederer, also reviewed the Filing and testified that the rates were not inadequate, excessive, or unfairly discriminatory.

**CONCLUSIONS OF LAW**

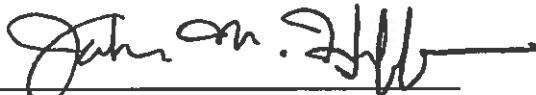
Based on the substantial and competent evidence provided by Travelers and the Department and presented at the May 5, 2015 hearing in the matter, and upon the record as a whole, the Director concludes as follows:

1. The subject matter of Travelers' Filing and the hearing held by the Department of Insurance, Financial Institutions and Professional Registration on said Filing on May 5, 2015 are within the jurisdiction of the Director under § 287.896, RSMo.
2. July 1, 2015 is a reasonable date for new premium rates and rating structures authorized pursuant to this Order for new and renewal business in the Missouri residual market.
3. Travelers' proposed -4.7% premium level change at the proposed 110% loss ratio retention level option, together with its proposed rate relativity capping methodology, will produce a level of premium, investment income and final premium rates which are not excessive, inadequate, or unfairly discriminatory and which will be actuarially sufficient to cover the claims, losses, and reasonable operating expenses of the Missouri residual market under the A.R.M. Plan.

**ORDER**

IT IS THEREFORE ORDERED that the rates and supplemental rate information, as proposed by Travelers, for use in the A.R.M. Plan beginning July 1, 2015, as set forth above, are hereby approved.

SO ORDERED, SIGNED AND OFFICIAL SEAL AFFIXED THIS 19 DAY OF  
May, 2015.

  
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John M. Huff, Director  
Missouri Department of Insurance,  
Financial Institutions and  
Professional Registration



**CERTIFICATE OF SERVICE**

The undersigned hereby certifies that a true and correct copy of the foregoing was served by certified mail, postage prepaid, No. 7014 1820 0002 0484 3323, and by electronic mail, on this 19<sup>th</sup> day of May, 2015 to:

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