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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 offices of Duane Morris LLP, Conference Room 12K, 12th Floor, United Plaza Building, 30 South 17th Street, Philadelphia, Pennsylvania on Tuesday, December 3, 2013 at 10 a.m.

The following members were present:

Actuarial Committee

Mr. A. Iuliano	Amerihealth Casualty Insurance Company
Ms. M. Gaillard**	American Home Assurance Company
Ms. R. Reich	Donegal Mutual Insurance Company
Mr. A. Becker**	Harleysville Insurance Company
Mr. D. Savage	Hartford Accident & Indemnity Company
Ms. N. Treitel-Moore	Liberty Mutual Insurance Company
Mr. K. Brady	PMA Insurance Company
Mr. A. Becker	Selective Insurance Company
Mr. R. Willsey	Travelers Property and Casualty Company

Classification and Rating Committee

Ms. M. Gaillard**	American Home Assurance Company
Ms. M. Baumhauer	Graphic Arts Association
Mr. A. Becker**	Harleysville Insurance Company
Mr. K. VanElswyk	Insurance Company of North America
Mr. T. Mehaffie	Malt Beverage Distributors Association
Not Represented	National Federation of Independent Business
Not Represented	Pennsylvania Automotive Association
Not Represented	Pennsylvania Food Merchants Association
Ms. M. Melewsky	Pennsylvania Newspaper Association
Not Represented	Pennsylvania Retailers' Association
Mr. R. Edmunds	PMA Insurance Company
Not Represented	Westfield Insurance Company
Mr. J. Binkowski	XL Insurance Company
Mr. R. Duesberry	Zenith Insurance Company

Mr. T. Wisecarver	Chair - Ex Officio

Also present were:

Ms. L. Thorne	Berkley-MidAtlantic Insurance Group
Mr. C. Romberger	Coal Mine Compensation Rating Bureau of Pennsylvania
Mr. S. Cooley	Duane Morris LLP
Mr. S. Crossley*	Eastern Alliance Insurance Company
Mr. R. Irons*	Eastern Alliance Insurance Company
Mr. E. Faoller	Key Risk Insurance Company
Mr. J. Hanna	Mutual Benefit Insurance Company
Mr. M. McKenney	Pennsylvania Insurance Department
Mr. G. Zhou	Pennsylvania Insurance Department
Ms. F. Barton	PCRB Staff
Ms. D. Belfus	PCRB Staff
Mr. B. Decker	PCRB Staff
Mr. M. Doyle	PCRB Staff
Mr. D. Rawson*	PCRB Staff
Mr. P. Yoon	PCRB Staff

* - Present for part of meeting
** - Representative on both Committees

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

All Committee members and other attendees made self-introductions.

Background, recent events and considerations regarding the matter of planning and announcing PCRB committee meetings, including specifically this meeting, were addressed. Implications of extraordinary demands arising throughout 2013 on the PCRB's ability to address pending research topics were also discussed.

Forthcoming changes in staff at the PCRB were noted, with special acknowledgement of the distinguished career service provided by Michael Doyle, Chief Actuary, who would be retiring at the end of 2013.

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

ITEM (1) REVIEW OF APRIL 1, 2014 LOSS COST FILING

A discussion package of materials was provided to attendees for reference during the presentation of key findings from staff's work and to facilitate discussion. The meeting discussion proceeded to 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:

Overall Loss Cost Change Indication

The basis for the overall loss cost change was described as beginning with the evaluation of ultimate costs of prior policy years. The underlying data for that evaluation was obtained from aggregate financial calls as summarized in Exhibit 5. This data was presented on a consistent basis reflecting effects of Act 44 of 1993 (a law containing a variety of changes to the processes and parameters used to determine medical benefits for workers compensation cases in Pennsylvania) and Act 57 of 1996 (primarily consisting of changes to the system controlling indemnity benefits for workers compensation claims in Pennsylvania). Continuing practices of prior Pennsylvania filings, Exhibit 5 excluded data for policies written on a large deductible basis. Staff described procedures used to assemble reported data from consistent groups of companies for each age-to-age comparison supported by Exhibit 5, noting that some companies either did not report data at certain evaluations or reported data that was not used in the filing analysis for a variety of reasons related to data quality.

Exhibit 6 was noted as a key element of the PCRB's analyses of both loss development and trend. Premium development was presented on Page 6.1 of this exhibit. Loss development analyses for indemnity and medical benefits had been performed using both paid-loss and case-incurred loss methods. Calculations for indemnity benefits were shown on Pages 6.2 through 6.6, while the counterpart pages for medical benefits were 6.14 through 6.18. Tail factors for loss development calculations were derived using a methodology presented in Exhibit 7 of the agenda materials.

Exhibit 12 of the agenda materials was referenced. The second mailing's version of this exhibit was replicated as the first three pages of the discussion package for ease of access and reference.

Loss ratios selected for indemnity and medical benefits had been posted for each of the three most recent available completed policy years, i.e., 2009, 2010 and 2011. These loss ratios and the resultant average ratios were shown on Lines (1) through (4) on Page 12.1 of Exhibit 12, the first page of the discussion package.

Trended loss ratios based on each of the Policy Years 2009, 2010 and 2011 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 to derive time series of claim severity ratios.

Staff had applied an exponential trend model to claim severity ratios for the most recent seven years to derive claim severity trends for this filing. The annual indemnity severity trend thus obtained was noted on Page 12.2 of Exhibit 12, the second page of the discussion package, as +3.01 percent, and the counterpart annual medical severity trend was observed to be +4.45 percent.

Historical claim frequencies and the derivation of a prospective claim frequency trend (-4.8 percent) were presented on Page 12.3 of Exhibit 12, the third page of the discussion package.

The average trended on-level loss ratio obtained by applying the combined claim frequency and severity trends was shown on Line (9) of Page 12.1 of Exhibit 12, and at 0.9485 this ratio produced an indicated 5.15 percent decrease 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**: The claim frequency trend seems different from those reported for other states. Is the PCRB's frequency adjusted to a common wage? Does PCRB calculate average cost per case directly, as is published for other jurisdictions?*

***Answer**: The PCRB provides average cost per case data to the National Council on Compensation Insurance, Inc. (NCCI) for their Annual Statistical Bulletin. Those figures are based on unit statistical plan data.*

For ratemaking analyses, the PCRB does not calculate average claims from financial data as a basis for severity trends. Our frequency trends are derived from time series of first report indemnity claims compared to on-level expected losses. We use reported claim frequencies to adjust loss ratios to derive "severity ratios," which are the basis for our estimation of severity trends.

***Question**: What is the source of the first report indemnity claim counts?*

***Answer**: Those figures are taken from Unit Statistical Plan data.*

***Question**: Does the PCRB have claim counts also available from aggregate financial data?*

***Answer**: The financial data does include claim counts, but the exercise of matching sets of reporting companies at successive evaluations would complicate efforts to use that information for the purposes under discussion.*

***Comment**: It was noted that financial data would tend to be more current than unit statistical reports.*

***Answer**: For purposes of the claim frequency calculations, Policy Year 2011 information is currently available from statistical data. That is also the most recent complete policy year available from aggregate financial data for this filing.*

***Comment**: Perhaps the timing of the filing being made late in the year contributes to the availability of Policy Year 2011 from statistical data.*

***Question**: How is wage or payroll trend treated in the PCRB methodology?*

Answer: ***Payroll trend is included in the PCRB's calculation of frequency trend. Our methodology would result in an improvement in claim frequency if worker activity and numbers of claims were identical but wages were increasing. PCRB does not use an on-level adjustment for wages, but expected losses are put on a consistent loss cost level.***

Comment: ***NCCI uses an on-level wage adjusted premium in its claim frequency calculations. There would be advantages and more direct comparisons to be achieved by using a method comparable to that employed by NCCI.***

Question: ***Are the claim counts used for the PCRB's claim frequency calculations indemnity claim counts?***

Answer: ***Yes.***

Question: ***Would a claim be included as an indemnity claim if it had only indemnity payments, only an indemnity case reserve or both?***

Answer: ***Yes.***

Question: ***Has the PCRB adjusted expected losses to a common wage level?***

Answer: ***No, they are on a common loss cost level but are not wage-adjusted.***

Page 4 of the discussion package provided attribution of the effects of selected components of experience on the overall loss cost change indication. As illustrated on that exhibit, indemnity loss and trend experience each contributed improvement to the indication. Medical loss experience had also lowered the indication, while medical trend had caused an increase of approximately one percent.

Question: ***Are the first two bars on the chart experience changes?***

Answer: ***Yes, they represent the net effect of changes in the two most recent policy years from the previous filing to this one. The bars show that the loss levels for prior years are lower than they were a year ago.***

Comment: ***This comparison could include effects of a relatively adverse year dropping off the rate change calculation.***

Answer: ***Agreed, that would be the case.***

Question: ***Are there any law changes reflected in this filing?***

Answer: ***There are no law changes in Pennsylvania of a vintage to be part of this proposed loss cost change. The PCRB does not calculate and apply an on-level factor for routine changes in benefit minimums and maximums like many other states do. By order of the Insurance Department, such benefit changes are included as part of the severity trend.***

***Question*: Do the changes in indemnity and medical trend include wage changes?**

***Answer*: Yes, they do, because they are incorporated into the claim frequency component of the PCRB's trend.**

Staff described the PCRB's approach to loss development and the role of that analysis in the filing preparation. PCRB customarily used the average of the two most recent calendar years of development as a basis for deriving age-to-age factors in its filings. For each successive filing a new calendar year of data was added, and loss development factors from the older of the two years used in the previous filing were dropped from the analysis. This process effectively replaced the older of the two years used in the most recent previous filing with the newest available year. For the April 1, 2014 filing the newest available calendar year of loss development data available was that of Calendar Year 2012. The older of the two development periods relied upon in preparing the April 1, 2013 filing had been Calendar Year 2010. Calendar year 2011 had been included in the work supporting the 2013 filing and was retained for use in the 2014 filing.

Page 5 of the discussion package presented graphs of the Calendar Years 2012 and 2010 age-to-age factors less unity for paid indemnity losses, covering the five development maturities from 1st report (policy year at 24 months) to 6th report (policy year at 84 months). This comparison illustrated the change in loss development experience for paid indemnity losses for the 2014 filing in comparison to the filing underlying present loss costs, since the 2012 factors were replacing the 2010 factors with the 2011 factors having been used for the 2013 filing and being used again for the 2014 filing.

The comparisons on Page 5 showed improvement in paid indemnity loss development for the second-to-third, third-to-fourth and fourth-to-fifth maturities in 2014 filing, since the 2012 age-to-age factors were visibly lower than the comparable 2010 values at those maturities.

Page 6 of the discussion package presented graphical comparisons of the Calendar Years 2012 and 2010 age-to-age factors less unity for paid indemnity losses, covering development maturities subsequent to 6th report (policy year at 84 months). This separation of maturities from those reflected on Page 5 allowed the graph scale to be more informative of differences for later maturities, for which age-to-age factors become relatively small. As described with regard to Page 5 of the discussion package, the 2012 factors were replacing the 2010 factors with the 2011 factors having been used for the 2013 filing and being used again for the 2014 filing.

The comparisons on Page 6 continued to show a general improvement in paid indemnity loss development for the 2014 filing, since the 2012 age-to-age factors were lower than the comparable 2010 values for a majority of the development periods shown, with the exceptions being instances for which the 2012 and 2010 values were approximately equal.

Pages 7 and 8 of the discussion package presented comparative indemnity loss development factors less unity for case incurred losses. Page 7 included development to 6th report in annual increments, and Page 8 presented development after 6th report. Page 7 showed improvement

in indemnity incurred loss development after the first-to-second report. Page 8 showed alternating periods of development within which 2010 or 2012, respectively, had better indemnity incurred loss development experience, with a majority of the comparisons being in favor of 2010.

Pages 9 and 10 of the discussion package addressed paid medical loss development in the same fashion as Pages 5 and 6 had dealt with paid indemnity data. Page 9 showed only small differences between 2010 and 2012 development, with 2012 being slightly lower overall. The comparisons for maturities after 6th report shown on Page 10 showed 2012 as having better development over the first half of the periods shown, with subsequent comparisons being generally mixed.

Pages 11 and 12 of the discussion package addressed case-incurred medical loss development in the same fashion as Pages 7 and 8 had dealt with case-incurred indemnity data. Page 11 showed more almost identical development for the earliest two periods and then lower link ratios for 2012 over the remainder of the time shown. Page 12 showed lower case-incurred loss development for medical for 2012 over the initial few years with the subsequent periods being more balanced.

Pages 13 and 14 of the discussion package presented information also contained in part on Pages 10.1 and 10.2 of Exhibit 10 of the filing materials, that being comparisons of the estimated ultimate loss ratios derived using paid loss and case-incurred loss development approaches. Page 13 showed comparisons for indemnity loss in which newer policy year estimates were nominally lower using the case-incurred development method than the paid loss development method. These small differences became less significant for older policy years, and the two methods converged for the oldest policy years illustrated on Page 13.

Page 14 of the discussion package presented comparisons of the estimated ultimate loss ratios for medical derived from using paid loss and case-incurred loss development approaches. The pattern of comparisons was very similar to that observed for indemnity loss on Page 13, with newer policy years showing the case-incurred loss development method having nominally lower estimates than the paid loss development method and with the differences becoming less significant for older policy years.

The patterns illustrated on Pages 13 and 14 of the discussion package were noted as being similar to results from other recent PCRB filings.

Question: ***In previous filings, the PCRB included exhibits showing settlement rates for claims. Have similar presentations been included for this proposal?***

Answer: ***When we make a filing, we prepare a discussion of the Casualty Actuarial Society's Statements of Principles for Ratemaking and Loss and Loss Adjustment Expense Reserving. That discussion includes an exhibit showing settlement rates based on unit statistical data. Except for the very early report levels, we generally see continuing improvement in settlement rates. (Note: Later in the meeting it was noted that Page 20 of the Discussion Package did, in fact, present open-to-reported indemnity claims.)***

Comment: ***Most of the closure or settlement activity occurs by 1st report.***

Answer: ***Most claims do close before the first report, although those that remain open for subsequent reports become material cost factors for overall policy year experience. After an early slowdown, the settlement rates appear to accelerate over time in Pennsylvania. Staff understood that compromise and release settlements take two-to-three years to begin to occur in significant numbers in the data.***

Comment: ***Because the plotted lines are based on incremental factors, it is difficult to envision the cumulative effect of observed differences. The overall change indication is based on the most recent three policy years.***

Answer: ***The PCRB derives trend rates from the most recent seven policy years, so more than the most recent three years contribute to the filing change indication.***

Question: ***Why are the ratios shown less unity?***

Answer: ***This approach allows a more detailed scale and makes the differences show up better. Notwithstanding that feature, when the incremental differences bounce around it, is hard to see the cumulative effect.***

Question: ***Could the PCRB add lines to the graphs showing comparisons of the cumulative development factors from the current and prior filing?***

Answer: ***Page 6.3 of Exhibit 6 shows the cumulative indemnity development factors from the current filing.***

Comment: ***It would still be helpful to see the cumulative differences on a graph.***

Answer: ***The value of showing cumulative differences was acknowledged.***

Question: ***Is settlement activity increasing in Pennsylvania?***

Answer: ***Compromise and release settlements were not allowed before Act 57 of 1996. Although the statute provides for the use of evaluations using AMA Guidelines to determine extent of disability, the compromise and release process is used almost exclusively in Pennsylvania.***

Question: ***Do you have detail on compromise and release activity?***

Answer: ***The PCRB receives reports of numbers of petitions by type. It was noted that, even if compromise and release petitions are level, that fact, in concert with fewer claims being incurred each year, would suggest increased penetration for the compromise and release process within the population of eligible claims.***

Comment: ***There is about a five point difference between loss ratios estimated using the paid method and the case incurred development method.***

***Answer:** Pages 6.6 and 6.18 of Exhibit 6 show the detail differences in loss ratios derived by those respective methods. Those differences were approximately five points at the extreme (most recent policy years) for both indemnity and medical.*

***Question:** Does the Delaware Compensation Rating Bureau, Inc. (DCRB) see the same pattern when comparing the result of loss development methods in Delaware?*

***Answer:** Staff recalled that case-incurred loss development gave higher results than paid loss development in Delaware. [Note: This was verified after the meeting for medical benefits. Indemnity results in Delaware were very similar for the paid and case-incurred loss development methods.]*

The indemnity/medical split percentages were about 30/70 in Delaware, while they were close to 50/50 in Pennsylvania.

In Delaware a review done many years ago showed very small amounts being involved in a vast majority of settlements. Contrary to Pennsylvania's experience, overall claims are staying open longer in Delaware than they used to.

Exhibit 8 of the agenda materials derived the filing's metric for claim frequency trend. Alternative data sets relevant to claim frequency experience and estimates were compared. The PCRB's derivation of claim frequency trend was described as using unit statistical data excluding large deductible policies. Pennsylvania's claim frequency had declined each year for the period shown, with a couple of very recent years showing relatively small changes. The basis of the draft filing's indication for claim frequency trend was noted as an exponential fit through the most recent available seven policy year points, giving an annual rate of claim frequency decrease of 4.8 percent. Page 15 of the discussion package illustrated the PCRB's long-term experience with regard to claim frequency with a line graph.

***Question:** Is wage inflation driving the observed claim frequency improvement?*

***Answer:** Staff referred attendees to Exhibit 8. Page 1 of this exhibit showed counts compiled by the Department of Labor & Industry. Injuries or illnesses in which the worker lost time outside the day or shift of occurrence were included in these time series. The PCRB had compared those counts to contemporaneous payroll data. Claim frequency was shown on both unadjusted and wage adjusted bases.*

Referring to the later portions of Exhibit 8 and looking at the unadjusted and wage-adjusted portions of exhibits, it was noted that the -4.8 percent claim frequency trend was -2.4 percent if the changes were adjusted for wage inflation.

***Comment:** An attendee recalled some recent NCCI presentations concerning claim frequency, derived from financial data, which had included discussion of calendar year distortions attributable to premium audits when economic conditions had been worsening.*

***Answer:** The PCRB computed its claim frequencies on a policy year basis using unit statistical data.*

***Comment:** An attendee suggested that claim frequency trend should not be reflecting wage changes. They expressed loss ratio trend as a result of three components, i.e., (Frequency) x (Severity) / (1 + Wage). This attendee also thought that claim severity in Pennsylvania was increasing more rapidly than the PCRB's approach showed.*

***Answer:** The PCRB's claim frequency trend, multiplied times its claim severity trend, did produce the appropriate loss ratio trend.*

***Comment:** The attendee expressed a preference for tying claim severity trend directly to the average cost per case.*

***Comment:** If claim frequency trend were adjusted by removing the effects of wage changes and loss ratio trends remained the product of claim frequency and claim severity trends, then claim frequency trend would be lower (less negative), and claim severity trend would be higher than the PCRB approach showed.*

Discussion was held concerning various alternative interpretations of approaches to analyzing trend. This led to a hypothetical discussion, as follows:

Suppose claim frequency trend was -5 percent and claim severity trend was +5 percent. If claim frequency trend was made less negative by virtue of putting the figures on a common wage level and if the product of the two trends was still supposed to produce a loss ratio trend, then claim severity trend would have to become less positive.

This led to the conclusion that, if claim frequency was stated on a common wage level, wage trend might be needed as a third component of loss ratio trend.

***Comment:** We would like PCRB's claim frequency to be consistent with values cited elsewhere. We also want to know what is happening to average costs per case.*

***Answer:** If, in the discussion example, the -5 percent claim frequency trend was expressed as a product of claim frequency trend on-level for wage changes and effective wage trend, the result might look like this:*

.975 (claim frequency on wage level) x 1.05 (claim severity) x .975 (wage trend).

***Comment:** The PCRB's method did not require a separate wage trend.*

***Comment:** It was concluded that using the PCRB's method, claim severity trend was a true severity change.*

Staff provided a brief overview of the PCRB's customary trending procedures, which separated loss ratio trends into claim frequency and claim severity components. The calculation of "severity ratios" by adjusting loss ratios for observed changes in claim frequency was outlined,

with reference to Pages 6.6 and 6.18 of Exhibit 6. Estimation of severity trends was accomplished in Exhibit 6 (Pages 6.6 through 6.10 for indemnity severity ratios and Pages 6.18 through 6.22 for medical severity ratios). Pages 10.3 and 10.4 of Exhibit 10 displayed time series of severity ratios thus derived.

Pages 16 and 17 of the discussion package showed graphs of historical severity ratios and trend lines projecting future severity ratios based on prior policy years. Page 16 addressed indemnity severity ratios, with historical ratios being based on the average of the paid loss and case-incurred loss development methods and shown connected by a solid line and trended ratios based on a seven-point exponential trend line fit through Policy Years 2005 through 2011 and represented by a dotted line on the discussion package page.

Page 17 addressed medical severity ratios, with historical ratios being based on the average of the paid loss and case-incurred loss development methods and shown connected by a solid line and trended ratios based on a seven-point exponential trend line fit through Policy Years 2005 through 2011 and represented by a dotted line on the discussion package page.

In evaluating the filing proposal's treatment of trend the PCRB had replicated prior filings' tests of the goodness-of-fit of various trend methods and experience periods applied to loss ratios and severity ratios, respectively, and those tests were presented in Exhibit 9a (loss ratios) and Exhibit 9b (severity ratios). R-squares for fits using seven or more points for indemnity were comparable for loss ratios and severity ratios, and r-squares for medical were universally better for severity ratios. Residuals based on seven-point exponential fits compared more favorably for loss ratio fits for indemnity, but were more favorable for severity ratio fits for medical.

In addition, PCRB had reviewed the efficacy of alternative trend methods and experience periods in forecasting subsequent policy year loss ratios and severity ratios, with the results of those reviews contained in Exhibit 11a (for loss ratios) and Exhibit 11b (for severity ratios). Although application of a common trend method (i.e., exponential fit) through the same number of points (for example, seen) separately to claim frequency and claim severity is equivalent to using those same methods applied to loss ratios, the limited number of tests available for seven-point exponential projections were somewhat skewed in favor of loss ratio and against severity ratios.

Page 18 of the discussion package presented graphs of historical and projected indemnity loss ratios, claim frequency and claim severity derived in accordance with the procedures and methods previously discussed. This presentation replicated Page 10.5 of Exhibit 10 and illustrated gradually declining indemnity loss ratios which resulted from claim severity increasing more slowly than claim frequency had declined.

Page 19 of the discussion package presented graphs of historical and projected medical loss ratios, claim frequency and claim severity derived in accordance with the procedures and methods previously discussed. This presentation replicated Page 10.6 of Exhibit 10 and illustrated slightly higher severity ratios for medical than for indemnity loss but with loss ratios still declining modestly over time due to the net favorable effects of claim frequency improvement.

In the context of Pennsylvania system outcomes, Page 20 of the discussion package illustrated settlement rates derived from unit statistical data. This page contained a set of line graphs tracking the portions of reported indemnity claims that remained open at various report levels for a series of prior policy years. These graphs generally showed a pattern of stable or slowly improving settlement rates over the past three to four years.

Question: Do the medical loss dollars used to derive medical severity ratios include losses for medical-only claims.

Answer: Yes, all medical loss dollars are included in the analysis.

Question: Is there a medical fee schedule in Pennsylvania?

Answer: In 1993 a medical fee schedule was introduced. In the beginning this fee schedule was established at 113 percent of the Medicare fee schedule. In late 1994 or 1995, the fee relativities in the existing fee schedule were frozen, and in subsequent years medical fees had been adjusted based on changes in the Statewide Average Weekly Wage (SAWW). As new medical services are developed, they are added to Pennsylvania's fee schedule at 113 percent of Medicare but then indexed to changes in the SAWW for subsequent years.

WCRI reports have shown that Pennsylvania's overall fee schedule now falls in the mid-to-upper 120 percent range compared to Medicare. However, since 1994-95, Medicare has revised the comparative reimbursements that they provide for specialists and primary care physicians. There has been discussion of adopting some percentage of the current and ongoing Medicare fee schedule in Pennsylvania in order to maintain fee relationships applicable under that broad-based reimbursement system.

It was noted that Page 20 of the discussion package addressed a prior question concerning settlement rates.

Comment: The ratios shown on Page 20 were ratios of open claims to total reported claims.

Answer: That was correct, so the interpretation of the lines was for settlement rates to be improving when the lines were trending downward.

Question: Isn't this a possible explanation for why the paid loss development method produces higher estimates than the case-incurred loss development method? Acceleration of settlements might be impacting the results.

Answer: An increase and/or acceleration of settlements could cause the methods to behave this way, but the differences observed have persisted for many years.

Question: Is this data shown on the same basis as the other graphs, i.e., excluding large deductible business?

Answer: No, this graph is taken from unit statistical plan data and includes all large deductible business.

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

Loss-Based Assessments and Employer Assessment Factor

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

Effective October 1, 1999, the provisions for the Administration Fund, Subsequent Injury Fund and Supersedeas Fund, previously included in published 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, 2014 (0.0195) 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, 2014 (0.0143).

Staff noted that the proposed employer assessment factor was lower than the current level (0.0262) due to reduced budgetary provisions for the Administration Fund and Supersedeas Fund.

The loading in PCRB loss costs for the remaining factors listed above was noted as being down nominally from 0.0150 due to lower anticipated activity in the Certified Safety Committee Credit Program.

Question: Does the assessment factor bounce around from year-to-year?

Answer: There has been some volatility in the assessment factor, generally attributable to changes in budgetary amounts for the Administration and Supersedeas Funds.

Question: What kind of premium is shown on this exhibit – standard or net?

Answer: It is standard premium.

Question: Where does the premium shown come from?

Answer: It is taken from Pennsylvania Special Schedule W.

Pennsylvania Construction Classification Premium Adjustment Program (PCCPAP)

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

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

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

Staff noted that the average PCCPAP loading indicated, based on the most recent available data, was nominally lower than that currently in effect (2.42 percent proposed vs. 2.50 percent current). This was attributed to the effects of continuing small declines in participation in the program.

Question: Does the PCCPAP loading vary by risk classification?

Answer: Yes, it does.

Question: How is an employer who does construction work that spans multiple class codes treated under this program?

Answer: One overall premium credit is computed on a weighted basis to be applied to the entire policy. That credit is the composite result of the employer's application that tells us the average wage for their operations in each risk classification.

Question: An attendee reported that they had heard of instances in which employers would apply for these credits but then not use them or have them applied to their policies. Does the PCRB check for this condition?

Answer: When an employer applies for and receives a credit, the PCRB records that in the employer's file, and policies subsequently issued are checked for the credit.

Staff believed that reluctance to apply PCCPAP credits might have been attributable to the impacts of such credits on experience modification factors. When the PCCPAP program first started, an employer would apply for credits and, as a result of the credit being applied, their experience modification could increase. For many construction businesses, having an experience modification above 1.000 precluded them from bidding on many desirable contracts.

In 2002, Pennsylvania stopped adjusting the experience modification for the credit and instead applied the adjustment to the PCCPAP credit itself. That step helped reduce the number of people applying for the credit but not using it.

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

Certified Safety Committee Credit Program

Exhibit 16 of the agenda materials addressed recent experience under the Certified Safety Committee Credit Program. Experience was presented for Policy Years 1997–2011 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 1.19 percent to 1.12 percent.

Question: Noting the maximum program credit of five percent, staff was asked how the average credits for participating risks shown in the exhibit could exceed that amount by nominal margins.

Answer: This was described as the result of credits being applied to a different base than had been used in preparing the exhibit.

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 be expected to improve the accuracy of the modifications thus issued.

Illustration of effects of the Experience Rating Plan was provided by reference to Pages 21 and 22 of the discussion package, which replicated materials included in Exhibit 18a.

Page 21 (credit risks) showed a pattern that might suggest that the Experience Rating Plan gave insufficient credibility to larger risks. Page 22 (debit risks) was consistent with the Experience Rating Plan having too low credibility across the spectrum of risk sizes.

Staff noted observations provided by a member carrier that had attempted to compare experience modifications for sample risks using the PCRB and NCCI plans. Issues of classification differences were noted, but, based on an attempted mapping between the two systems, the results had been characterized as follows:

For credit modifications the results were extremely close together.

For debit risks the NCCI modifications were consistently higher than the PCRB alternatives.

Aspirations to refresh and extend testing of the PCRB Experience Rating Plan previously shared with the Committees were affirmed, with a caveat for the potential usurpation of otherwise available time for work dictated by outside forces and influences.

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.

***Question**: An attendee wondered whether experience rating credibility wasn't a potential issue based on the exhibits. If more credibility was given to experience where a debit experience modification was produced, it seemed that some of the features of the comparisons would improve.*

***Answer**: Staff observed a possible area of improvement for credit risks if larger accounts were assigned greater credibility but had not seen separate credibility scales being established for credit and debit experience modifications. Other alternatives, such as applying a multiple and/or different split point, might be appropriate.*

***Comment**: An attendee observed a concentration of experience modifications in the mid- to upper-80 percent range and encouraged staff to look into this.*

***Answer**: Staff had reviewed the report details and was not surprised to find a concentration of experience modifications at the point where loss-free employers just became eligible for experience rating.*

***Comment:** The attendee insisted that more attention should be given to this subject and expressed concern about rating adjustments being given in the absence of any losses.*

***Answer:** Staff acknowledged an interest in reviewing and improving the Experience Rating Plan.*

***Comment:** It appeared that many risks were getting credits at levels for which assigned debits could not offset the adjustments. This was exacerbated by the presence of many loss-free risks.*

***Answer:** The numbers of accounts were, and probably always would be, weighted toward the credit side. It is hard to balance out credits and debits assigned in most size groups due to the skewed nature of the workers compensation loss distributions.*

Discussion ensued concerning the interpretation of discussion package pages, and the prevailing credits assigned to small loss-free accounts.

***Question:** Are there caps or limitations on the level or movement of experience modifications in the plan?*

***Answer:** Yes, there were swing limits of +/- 25 percent of the prior experience modification. There was a special procedure in place when the capped experience modification and the calculated experience modification were on opposite sides of the manual rate.*

***Comment:** If a risk had a maximum upward cap of 0.85 on their experience modification but calculated an indicated experience modification of 1.15, would that employer be assigned the manual rate (an experience modification of 1.000)?*

***Answer:** No, if you are capped moving down from a debit rating but have a calculated credit experience modification, then you are moved to 1.000. Experience ratings above 1.000 were particularly problematic for construction employers.*

***Question:** How were the graphs on Pages 21 and 22 of the discussion package prepared?*

***Answer:** Those graphs showed results of the Experience Rating Plan on an uncapped basis. Exhibit 18b showed summary results of the plan with the swing limits taken into account.*

***Comment:** An attendee expressed interest in seeing Pages 21 and 22 prepared on a capped basis.*

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.

Question: Noting the different results of off-balances by industry group, an attendee asked whether the PCRB knew why those disparities were in place.

Answer: While the relative results of the Experience Rating Plan have been consistent over time, the cause(s) for those differences had not been identified.

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 included rating values pertinent to various rating plans affected by the size of loss for individual claims or occurrences insured thereunder. Some such plans provided limitations applicable to the amount(s) of loss that could be used in computing a retrospective premium. Other portions of this analysis facilitated 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 varied by hazard group and that the hazard groups had been 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. The PCRB continued to publish information based on both seven and four hazard groups during a three-year transition period. Beginning with the April 1, 2012 filing, the transition program had ended, and this filing was proposing to continue to support analysis for the seven hazard groups (A-G) only.

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. Separate analyses of claim frequency and loss severity had been performed. For loss severity a single parameter Pareto distribution for all injury types combined has been used since the initial analysis was performed. For claim frequency a Pareto distribution is used for each separate type of injury, except permanent total (PT)
where a lognormal distribution was chosen. 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.

Staff then described analysis conducted for the April 1, 2014 filing to support hazard groups and excess loss factors applicable thereto. The methods and distributions employed were similar to the approach first introduced with the April 1, 2008 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 had been trended to the midpoint of the prospective rating period. The exhibit also included 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. As with the April 1, 2013 filing, separate medical-only data had been included in the analysis. Medical-only claim distributions had not been fitted and actual excess ratios for those claims had been used in the analysis.

Question: Have you used a distribution of development factors in deriving the size-of-loss distributions?

Answer: No, small claims have the same development factor applied to them as larger ones. The size-of-loss distributions were more critical in ratemaking in Delaware than was the case in Pennsylvania.

Comment: It was suggested that consideration be given to the results of a dispersion model(s).

Answer: Staff agreed, adding that Pennsylvania would be the logical starting point for such a review.

Exhibit 23 derived proposed excess loss (pure premium) factors computed using results in Exhibit 22. The process for calculating excess factors in Exhibit 23 was unchanged from prior years, although the loss distributions on which the analysis relies had been updated, and the average costs and weights by type of injury and hazard group reflected the most recent data.

Size of loss considerations also applied to the determination of state and hazard group relativities that allowed 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. But for the April 1, 2009 filing, where the revision and expansion of hazard groups required a special treatment, the procedure had been used consistently since the April 1, 2003 filing. The complement of credibility was assigned to prior year relativities adjusted for overall changes in Pennsylvania and countrywide (NCCI states) average severities.

Question: Staff was asked how consistent this method was.

Answer: There is movement observed from year-to-year. PCRB tries to temper that movement to some extent by smoothing out average costs.

Question: Do you always do that or just when things look odd?

Answer: We always do this. We don't interrupt the movement, but we do try to mitigate changes that are unexpected and significant.

Question: Where are the excess ratios by type of loss on Exhibit 23, Page 2 coming from?

Answer: ***They come from results derived in Exhibit 22. Exhibit 22 is based on experience for all hazard groups combined. Excess ratios in Exhibit 23 adjust Exhibit 22 excess ratios for differences in average costs between each hazard group and the composite of all hazard groups combined.***

Exhibit 24 presented the derivation of state and hazard group relativities for the proposed filing.

Exhibit 25 - Offering of small deducible coverages at certain specified amounts was noted as being mandatory in Pennsylvania. PCRB filings thus provided updated loss elimination ratios computed consistent with the mandatory deductible levels of $1,000, $5,000 and $10,000. 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. Beginning with the April 1, 2013 filing, PCRB had segregated individually-reported small claims from small claims reported on a grouped basis, which allowed for a more refined treatment of the distribution of medical-only losses by loss size. Exhibit 25 showed the results of the updated analysis.

Retrospective Rating Plan Optional Loss Development Factors

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

Proposed Loss Cost Relativities by Classification

Exhibits 17, 20a, 20b, 20c, 28, 29, 30, 31, 33 and 34 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.

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 shifted from better to worse than average or vice-versa between successive filings.

A Class Book providing detail of historical experience and derivation of proposed rating values had been distributed with agenda materials 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.

PCRB Filing No. 240 had introduced a new procedure for mapping direct employment classes into temporary staffing classes. Effective December 1, 2010 temporary staffing classification Codes 544, 682, 929, 937 and 947 had been discontinued and were replaced with ten new temporary staffing exposure groups, Classes 520-529. The exposures and losses for the risks in the discontinued classifications could not be accurately reassigned to other approved classifications. While no new business would be written using these discontinued classifications, the Experience Rating Plan still required reference to expected loss factors (ELFs) associated with prior periods of exposure in computing experience modifications. Exhibit 31 included ELFs for the discontinued classes for use in calculating experience modification factors for affected risks.

The temporary staffing procedures adopted in 2010 mapped direct employment classes with similar rating values into a common temporary staffing exposure group. As part of PCRB Filing No. 240, it had been observed that classification rating value relativities would shift over time and that the rating values of the direct employment classes mapping into the proposed temporary staffing exposure groups might subsequently move outside the bounds of originally-constructed ranges. With that phenomenon in mind, the PCRB had intended to review the composition of direct business classes defining the temporary staffing exposure groups periodically.

Subsequent to the approval of the April 1, 2013 filing, PCRB had reviewed the direct employment mappings defined by Filing No. 240 and had updated those mappings to reflect shifts in rating values that had occurred since December 1, 2010. Exhibit 34 updated that analysis by reviewing rating value relativities based on approved April 1, 2013 loss costs. The methodology for calculating rating values for temporary staffing Classes 520-529 remained unchanged.

<u>Comment from PCRB Counsel</u>: There was an appeal by the American Staffing Association on behalf of the temporary staffing industry challenging the separate classification and pricing of temporary staffing businesses. After the PCRB approaches had been upheld by the Classification & Rating Committee and the Pennsylvania Insurance Department, the appellant had not pursued a further appeal in the matter.

Exhibit 35 and Staff Memorandum Dated November 15, 2013 Pertaining to Aircraft Seat Surcharge

The per passenger seat surcharge currently used in conjunction with the transportation of employees by aircraft or helicopter was being proposed for elimination effective January 1, 2015 by NCCI. The PCRB was proposing to mirror such discontinuation effective April 1, 2014, and the cited agenda materials provided a copy of NCCI's Filing Memorandum B-1426 and the requisite Manual changes to accomplish this discontinuation in Pennsylvania. With rating values customarily changed each April 1, staff invited commentary as to the respective merits of discontinuing this surcharge effective April 1, 2014 or April 1, 2015 in Pennsylvania.

Comment: Eliminating Class 9108 effective April 1, 2014 could present programming and system problems for PCRB members.

Comment: We agree with that and would like more lead time.

Answer: Staff agreed to develop a loss cost for Code 9108 in the April 1, 2014 filing and will wait until April 1, 2015 to eliminate it.

Exhibit 33 – Attendant Care Analysis

Exhibit 33 updated a procedure for rating attendant care workers that had first been introduced in the April 1, 2013 filing. The procedure combined the experience for attendant care workers that had previously been reported in Class Codes 0908, 0913 and 973 into Class Code 972.

Where the client was considered to be the employer, attendant care services had been assigned to Classes 0908 and 0913, depending upon whether the workers were engaged full- or part-time. Classes 0908 and 0913 used per capita exposure bases. Where the fiscal agent was considered to be the employer, Class 943 was the applicable Pennsylvania classification. Class 943 was a payroll-based classification.

A survey of fiscal agents provided payroll data for a complement of attendant care workers that were rated on a per capita basis. Based on observed relationships between payrolls and per capita units, staff had estimated aggregate payrolls for the attendant care exposures reported under Codes 0908 and 0913 for the Policy Years 2003 through 2007. Payrolls for Policy Years 2008, 2009 and 2010 had been projected based on reported per capita exposures and known changes in the Statewide Average Weekly Wage (SAWW).

Estimated payrolls associated with attendant care exposures previously reported in Codes 0908 and 0913 had been combined with attendant care payrolls from Code 943, and loss experience for all attendant care services for use in a 2014 Class Book page for attendant care services. Codes 0908, 0913 and 943 had been addressed by removing the historical attendant care exposures and losses from their data and producing revised Class Book pages.

Auditable Payroll Values Indexed to the Statewide Average Weekly Wage

Staff noted that the Manual designated various auditable weekly or annual payrolls, including the weekly maximum musicians' or entertainers' payrolls, the weekly minimum and maximum corporate officer payrolls, the annual taxicab operator payroll and the annual minimum auxiliary or special school police payroll.

A staff memorandum dated October 15, 2013 outlining appropriate revisions to the currently-approved parameters in these cases was presented for discussion. Continuing a transitional program begun with the April 1, 2013 filing, the minimum corporate officer auditable payroll was proposed to be computed as 70 percent of the SAWW effective January 1, 2013. As the January 1, 2013 SAWW was $917, the resulting minimum auditable corporate officer payroll was $650 per week.

The maximum individual payroll for executive officers was proposed to change from $2,200 to $2,300 per week.

The annual payroll applicable to taxicab operators in the absence of payroll records was proposed to change from $44,400 to $45,850, and the minimum payroll for auxiliary police or special school police appointed by municipalities or townships was proposed to increase from $4,450 to $4,600 per year. Each of these parameters was maintained annually by reference to Pennsylvania's SAWW, with the convention of rounding results to the nearest $50 applied.

The above changes were proposed to become effective on a new and renewal basis April 1, 2014.

Current Manual provisions for minimum and maximum annual payrolls for professional or semiprofessional athletes, coaches or managers were presented. The existing parameters had been in effect since the early 1980s. A proposal to raise the maximum through a transitional series of step increases to a level 2.5 times the SAWW was presented, with staff inviting comments from Committee members and attendees. Staff expressed some uncertainty about the potential impact of this change on some risk(s) engaged in the businesses in question and proposed a review of such accounts prior to submitting the changes under discussion to the regulator.

Question: ***Had the PCRB reviewed minor league sports other than baseball?***

Answer: ***Yes, staff had looked at minor league hockey as well. The impact will be selective. Also, the Philadelphia 76ers basketball team had established an instructional league team in Wilmington with an average salary of about $20,000 per year.***

Comment: ***Most professional athletes' salaries were either far above or far below the current $60,000 maximum.***

Answer: ***For the most part, Major League Baseball and other major leagues were not affected, as they were exempt from the Workers Compensation Act.***

Comment: ***There were a limited number of minor league sports teams in Pennsylvania, and most of them pay salaries under the $60,000 maximum.***

Answer: ***Only a limited number of people will be affected. Many team policies are only for office staff or scouts.***

Question: ***What is the next step?***

Answer: ***PCRB staff would further review the population of the affected risk classification(s) to better understand the potential impacts, if any, of this change.***

Staff Memorandum Dated November 21, 2013 Pertaining to Codes 955 and 607 Study

A classification study precipitated by a 2012 appeal and described in the captioned memorandum was summarized. The resulting proposal was to discontinue the payroll division between Codes 955 and 607 when drilling was performed incident to an employer's Code 955 business. Manual changes were set forth in the descriptive memorandum.

Comment: ***Technology is a big part of the discussion.***

Answer: ***The proposed change is based on whether drilling was incidental or non-incidental to the employers' Code 955 business. Some geo-probes are larger, more expensive and more dangerous than others if used incorrectly and could lead to significant losses.***

Staff Memorandum Dated November 8, 2013 Pertaining to Manual Housekeeping Changes

Language changes intended to make the Manual clearer and current with prevailing business practices were ongoing, and staff reviewed the nature of such changes being proposed for implementation effective April 1, 2014.

Question: ***An attendee sought clarification on the proposal regarding Code 7428.***

Answer: ***The PCRB was proposing to change the Underwriting Guide entry to delete the word "remanufacturing."***

Question: ***Would the various memos being referred to in the meeting be included in the filing?***

Answer: ***The memoranda or materials derived from them will be included in the filing.***

Question: ***Would that specifically include the November 8th and 21st memoranda?***

Answer: ***Yes.***

Question: ***The inquirer asked whether the PCRB didn't more commonly submit a separate filing for proposals of the types addressed in the memoranda being discussed.***

Answer: Staff acknowledged that such was a common approach for the PCRB.

Question: If these proposals are included in the filing, would the PCRB notify affected employers?

Answer: Generally, housekeeping revisions did not precipitate notices to employers. For more substantive changes, the PCRB sent out two levels of notice. The first level was a mass mailing sent to affected employers; the second also informed their insurers-of-record about approved changes.

Comment: The "housekeeping" changes under discussion seemed to have more impact on employers than most such revisions in the past.

Answer: Staff agreed to consider the posture of various components of the revisions that had been shared with the Committees in light of the discussion.

Comment: In the past, it was noted, significant volumes of comments had sometimes been received from employers.

Staff Memorandum Dated November 25, 2013 Pertaining to Department of Labor & Industry Forms

Two forms pertaining to executive officer coverage declarations were published for reference in the PCRB Manual. These forms had been revised by the Department of Labor & Industry, and it was proposed to reflect the current versions of the forms in the April 1, 2014 Manual.

ITEM (2) REVIEW OF APRIL 1, 2014 F-CLASSIFICATION FILING

Staff introduced the topic of rating value filings for federal classifications, noting that changes to Pennsylvania's rating laws in 1993 had not revised the pricing system applicable to these classifications to a loss-cost approach. Due to the paucity of available experience data, F-Class filings were customarily prepared and submitted in alternating years, but the most recent change to F-Class rates had been adopted effective April 1, 2011.

F-Class filing exhibits had often been circulated to the Committees as e-mail advisories, but, given the opportunity for discussion afforded by this meeting, agenda materials had been included in the first mailing distributed for the meeting.

The Discussion of Exhibits narrative in the agenda materials was pointed out. Selected highlights were noted as follows:

Indicated Change in Rate Level

Exhibit 1 attached showed the derivation of a decrease of 1.84 percent in collectible premium for Pennsylvania F-Class business. On a manual basis, the indicated change was a decrease of 2.14 percent.

The procedure for developing the indicated change in Exhibit 1 was the same as that used in the 2011 Pennsylvania F-Class filing.

Losses

Derivation of the trended loss ratios based on a review of F-Class experience, as reported under the Unit Statistical Plan, was described in Exhibit 5.

Experience for the most recent available years through 2010 was newly extracted from the current revision database. This recent data had been supplemented by prior experience included in the PCRB's F-Class filings since and including 1997. Page 1 of Exhibit 5 shows reported standard earned premiums (1992 to 2007) and indemnity incurred losses (1992 to 2007). The step-shaped lines separated successive evaluations for a given policy period on the basis of which filing evaluation was the source for the information shown.

Page 2 showed similar detail for F-Class medical experience.

Page 3 showed age-to-age incurred loss development factors for indemnity losses from 1st through 10th report. The cells denoted with asterisks (****) represented points where an inconsistency in data between successive extracts for a given report year and maturity had been observed. The bottom section of Page 3 showed indemnity-incurred loss development factors to an ultimate reporting level. The selected age-to-age factors for indemnity were derived on Page 5 and were the result of fitting the age-top-age factors using seven years averages to a curve and also projecting a tail factor (10th-to-ultimate) based on that curve.

Page 5 showed the derivation of selected indemnity age-to-age development factors. Residuals (LDF-1) of average age-to-age loss development factors are fitted to a curve of the form $y = a * (1+x)^{\wedge b}$. An average factor of 1.0000 was chosen for the 14th to 15th development stage to improve the fit and shape of the resulting curve. A tail factor was selected by compounding the age-to-age factors for successive stages beyond 10th report.

Page 4 provided age-to-age incurred loss development factors for medical losses. Medical incurred loss development factors were not susceptible to satisfactory curve-fitting and so seven-year average age-to-age factors were employed to estimate ultimate medical losses.

Ultimate on-level loss ratios are calculated on Page 6 for indemnity, medical and in total. Page 7 shows a graph of the resulting projected ultimate loss ratios.

An analysis of loss ratio trend was summarized on Page 8. Linear and exponential trend lines were used to project trended loss ratios for indemnity and medical, using combinations of policy years ranging from three-to-ten points. Seven-year average loss ratios and zero percent annual trends were selected for both indemnity and medical losses. The resulting trended loss ratios of 37.63 percent for indemnity and 14.66 percent for medical were carried to Line (1) of Exhibit 1.

Expenses

Expense provisions were presented in Exhibit 2 and were broadly categorized as loss and loss adjustment, fixed expenses, and variable expenses. Variable expenses are expected to remain a constant percentage of premium regardless of the overall premium level or premium charge. Fixed expenses (Security Fund, General Expenses and Other Acquisition Expenses) are considered to be a function of changes in payroll levels and/or expense costs independent of changes in premium levels. Fixed expenses are, therefore, separately trended.

The fixed expense trend factor of 2.37 percent was based on a review of countrywide workers compensation dollars of expense for general and other acquisition expenses for the period 2003 through 2011, as compiled by A. M. Best Company. The payroll trend factor of 4.07 percent was based on insured payrolls from Unit Statistical Plan data for the 11 years 1998 to 2009 (excluding 2001). Loss adjustment expenses and the federal assessment were functions of losses, with LAE derived in Exhibit 3 and the federal assessment based on the latest available assessment rate.

The provisions for profit (+0.07 percent) and the combined provision for loss and loss-related expenses (78.98 percent) were derived from an internal rate of return model, as described in Exhibit 4.

The combined provision for loss and loss-related expenses of 78.98 percent was split into the loss, loss adjustment expense and the federal assessment components by maintaining a ratio of loss adjustment expense to loss of 14.62 percent and a ratio of federal assessment expense to loss of 16.74 percent.

A variety of expense provisions used in the proposal were derived from the expense study, as presented in Exhibit 3.

Page 3.1 of Exhibit 3 derived provisions for commission, other acquisition, and general expense exclusive of expense constant dollars. Commissions were related to premium, including large deductible business on a net (as reported) basis. Other acquisition and general expense were related to premiums, including large deductible business, on a gross (before deductible credits) basis. An average factor over three years, 2009 through 2011, was used. Experience for all companies was included.

Loss adjustment expenses for Calendar Years 2009 through 2011 were related to incurred losses, including large deductible business on a gross (before reimbursement) basis. Experience for all companies is included.

An average premium discount figure was derived based on the total Pennsylvania premium for all policies including those with F-Class exposure. The figure included an adjustment to account for multi-state risks.

Based on data from the Delaware (Assigned Risk) Insurance Plan, an average uncollectible premium rate of approximately 1.0 percent was observed. An uncollectible premium provision of 0.50 percent was selected for Pennsylvania F-Class business.

***Question:** It was observed that Page 3.9 of Exhibit 3 had "Delaware" in the title. Staff was asked if the intended reference was to "Pennsylvania."*

***Answer:** Uncollectible premium experience from the Delaware Assigned Risk Plan had been used as the basis for selecting the uncollectible premium ratio.*

***Comment:** An attendee suggested that NCCI Management Reports showed uncollectible premium ratios for other states, which might provide a broader source for this metric than Delaware alone.*

Exhibit 4, the Internal Rate of Return Model presented an internal rate of return model which tracked the premium, loss and expense cash flows of Pennsylvania workers compensation F-Class business for the prospective rating period. The model combined expense assumptions from Exhibit 2, a premium collection pattern, loss and expense payout patterns, and a base standard premium of $1 million to model the net cash flows for F-Class business.

The cost of capital (8.86 percent) was derived in Exhibit 4. A profit loading (0.07 percent) was chosen so that the net cash flows, when discounted to present value, provided a return on equity equal to the projected target rate of return or cost of capital. A loss ratio, including provision for loss, loss adjustment and the federal assessment, and consistent with the other expense values used in the model, was also derived and that ratio was 78.98 percent.

***Question:** Staff was asked what interest rate had been used in the Internal Rate of Return modelling work.*

***Answer:** Exhibit 4 showed a post-tax return on assets of 3.43 percent.*

***Question:** What was the source of the 4.33 percent pre-tax return on assets?*

***Answer:** Both the 4.33 percent pre-tax rate of return and the 3.43 percent post-tax rate of return were derived from distributions shown in Exhibit 4.*

Classification Analysis and Exhibits

The methodology for the derivation of F-Class rates was unchanged from the process used for developing F-Class rates in each Pennsylvania F-Class filing since and including 1997 and was similar to the process used in the calculation of State Act loss costs.

Exhibit 10, Rate Formulae, described the steps used in the classification ratemaking process.

Exhibit 9, Derivation of F-Class Rates, showed current and proposed rates by class and the respective percentage changes. No classes were subject to capping at the upper or lower allowable ranges.

Expected loss rate factors for use in calculating expected losses for experience rating were derived in Exhibit 11, Calculation of Expected Loss Rate Factors.

Proposed rating values were shown in Exhibit 12, Manual Rates and Expected Loss Rates.

F-Classification Exhibits, Exhibit 14, and the F-Class Book were noted. The F-Class Class Book showed the reported and projected experience for each class and the derivation of proposed rates. The F-Classification Exhibits showed various factors used in the class ratemaking process. The per-claim and per-accident loss limits and the credibility table were the same as had been used in the April 1, 2013 Pennsylvania State Act Loss Cost Filing.

Question: ***Staff was asked whether F-Class rates were separately published and announced.***

Answer: ***Two separate filings were made, one (larger) for Pennsylvania State Act business and the other for Pennsylvania F-Class business. The F-Class rates and the regular loss costs were published in two separate places in the Manual.***

U. S. Longshore & Harbor Workers Coverage Factor

Exhibit 6 showed the derivation of a USL&HW factor which, when applied to State Act class rating values, provided for the pricing of risks with USL&HW exposure. The USL&HW factor was based on a comparison of average benefit levels by type of injury under the USL&HW Act and the Pennsylvania Workers Compensation Act.

It was proposed that the USL&HW factor be decreased from 1.781 to 1.775, representing a 77.5 percent load to State Act rating values.

Other Exhibits

Exhibit 7, Table II, presented a summary of Unit Statistical Plan experience on a reported and projected basis for F-Class business by type of injury.

Exhibit 8***,*** Tax Multiplier, provided a tax multiplier factor applicable to F-Class exposures for use in retrospective rating. It was proposed that the factor decrease from 1.2736 to 1.1729.

Other Items:

Question: ***Staff was asked when filings based on the materials discussed at the meeting would be made.***

Answer: ***Staff expressed the hope to make the State Act filing before the close of the week after the meeting and to submit the F-Class filing soon thereafter.***

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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