

# Group Rating

## The Situation:

- Group rating allows employers of similar business types to be experience rated as if they were one employer.
- Combining experience allows small employers in a group who would otherwise be base rated or experience rated with minimal credibility to receive the maximum credibility available to an individual employer.
- There are over 500 groups in Ohio, and approximately 100,000 employers (private and public combined) participate in groups.

# Group Rating

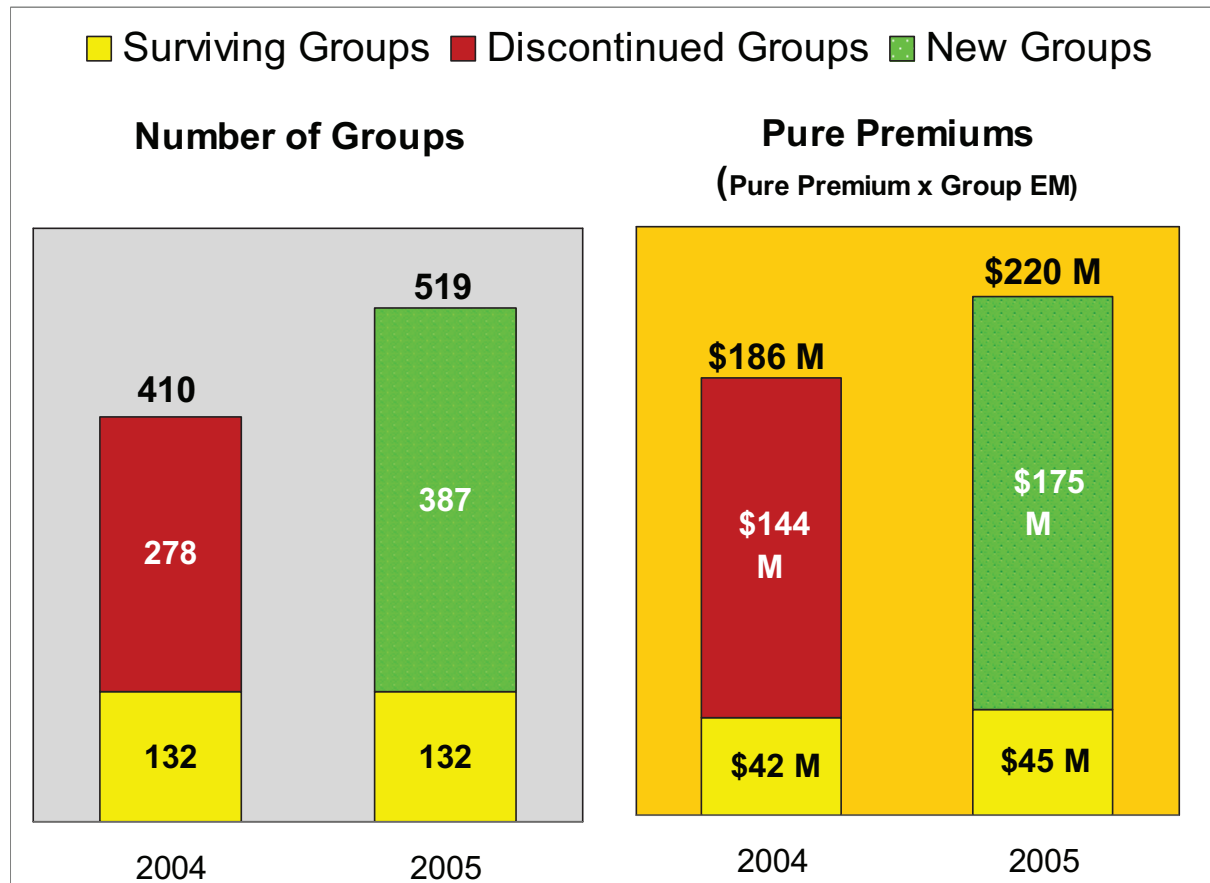
## Review & Analysis:

- The group experience rating process is inconsistent with two basic tenets of an experience rating plan:
  - 1) The plan should produce post experience rated loss ratios which are closer to the overall average than before experience rating; and
  - 2) The plan should balance stability of price with responsiveness.
- Group experience rating accomplishes neither and in fact exacerbates the post experience rated loss ratios so that there is more dispersion about the average loss ratio than less.
- Policyholders in the group experience rating process experience significant variability in their pricing as they move in to a group, to another group, or out of a group, which occurs frequently.
- We are unaware of any other state that has a program which functions similarly to group rating as it exists in Ohio.

# Group Rating

## Review & Analysis (continued):

- The turnover of groups is very high at 75-80%.
- This lack of stability is indicative that groups are functioning poorly.

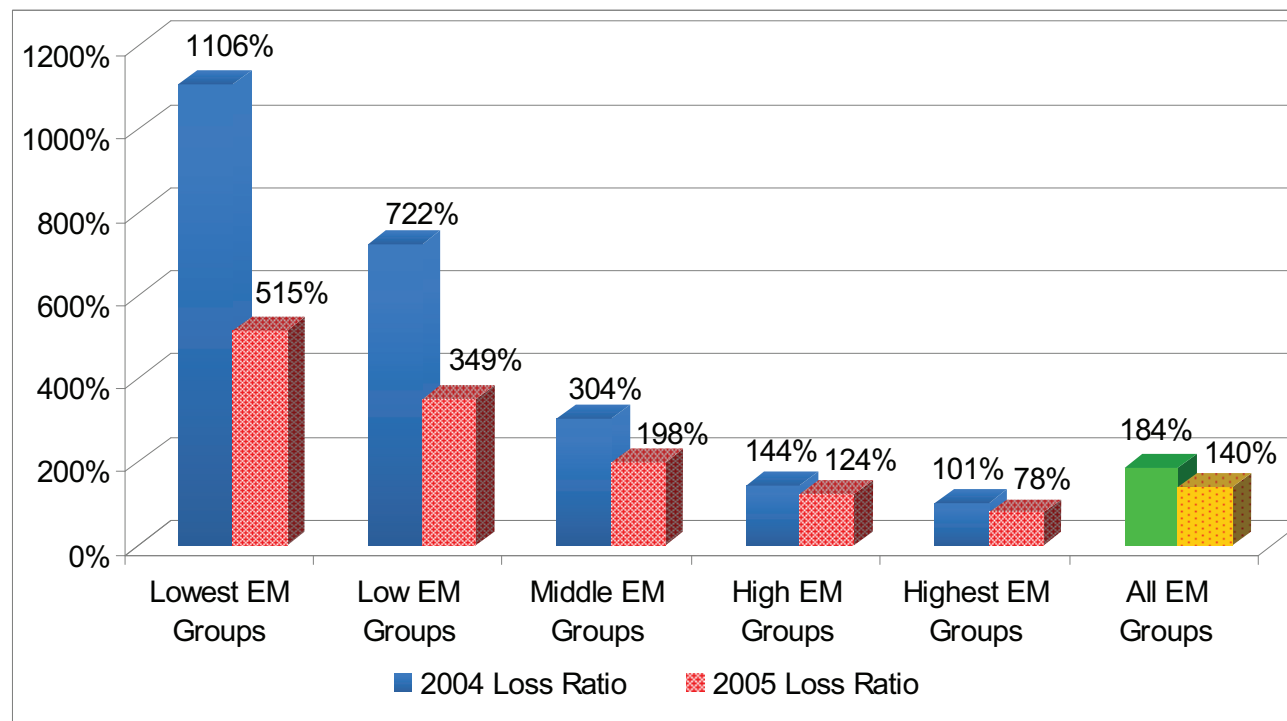


88% to 91% of group policies stayed in some group for 2004 to 2005.  
For group pure premiums, 68% to 80% of the premiums stayed in some group.

# Group Rating

## Review & Analysis (continued):

- Graph shows Group Loss Ratio Patterns by Low to High Group EM.
- Loss Ratios should be roughly equal if EMs are equitable.
- Such large dispersions indicate that group rating needs to be discontinued in its present form.



\* Losses valued as of 12/07; 2005 Loss Ratios are 1 year less mature than 2004 Loss Ratios

# Group Rating

## Review & Analysis (continued):

### GROUP RATING USING AN INDIVIDUAL EXPERIENCE RATING FORMULA

- Differences in the loss experience of individual employers are largely driven by the differences in the behavior of the management and employees of each employer, in terms of employee selection and training, safety programs, operating procedures, accident prevention, risk controls, etc.
- Such behaviors directly affect the frequency and severity of work injuries.
- Experience rating is a good predictor of future losses for an employer, because prior loss experience reflects an employer's oversight of such behaviors.

# Group Rating

## Review & Analysis (continued):

### GROUP RATING USING AN INDIVIDUAL EXPERIENCE RATING FORMULA

- A group of employers will not have the same management influencing such behavior, and therefore an individual experience rating formula applied to a group is not generally predictive of future losses for that group, regardless of similarities in type of business and prior loss experience of the group members.
- Studies of BWC's group rating program have consistently demonstrated that applying the individual experience rating formula to group experience has resulted in significant under-prediction of losses for groups.
- The poor performance of the individual experience rating formula when applied to groups is evidence of the flaws in the current approach to group rating, and indicates a need for a different approach to group rating.

# Group Rating

## Review & Analysis (continued):

### CONVERSION TO NCCI-TYPE SPLIT PLAN

- A split experience rating plan, with lower credibility assigned to group experience compared to the current plan, will mitigate some of the inequity currently produced by group rating.
- However, a split plan shares the same basic flaw as the current plan in that it applies a formula designed for an individual employer to a group of employers.
- The opportunity to manipulate the composition of a group in order to maximize discount will still be present under such a structure, and inequity will persist.

# Group Rating

## Performance Assessment



### Peers and Industry Standards Considered

NCCI, Other State Funds, Actuarial Standards of Practice.

# Group Rating

## Deloitte Conclusions:

A group rating program should have a primary focus on safety, preventing injuries, and mitigating severity of work injuries. However, the current group rating formula has led to:

- Behaviors focused on achieving the maximum group credit
- Retaining “Loss-free” employers in groups
- Excluding employers from groups if their losses impact the group credit
- Churning of employers to different groups, new groups, or out of groups, driven by group rating impact
- Programs such as \$15,000 Medical Only and Salary Continuation, to keep claims out of group rating
- The One Claim Program, driven by reducing the premium impact between group and non-group status

# Group Rating

## Deloitte Conclusions (continued):

- Change the structure of group rating to mitigate the present inequities.
- Provide appropriate incentives for groups to focus primarily on accident prevention and loss mitigation activities.
- Eliminate the use of the individual e-mod formula for group rating.
- Determine group rating through the use of a group discount factor.
- Establish a minimum number of years of experience for a group to qualify for a discount factor, e.g. 3 years.

# Group Rating

## Deloitte Conclusions (continued):

- Develop a group discount formula based on the past performance of each group, with the goal of achieving equity between group rated and non-group rated employers, and equity between different groups.
- Apply a separate group rating off-balance adjustment to the group discount factors, rather than applying an overall off-balance adjustment to all employers through class rating.
- Develop the group discount factor based on the actual past performance of each specific group.
- In determining the group discount factor, include the experience of all group members only during the period when they were in the group, including members who leave the group.

# Group Rating

## Deloitte Conclusions (continued):

- Apply the group discount factor to the individual e-mod adjusted premium of each member of the group.
- Develop a group discount formula simpler than an e-mod formula, based on a loss ratio or loss rating approach.
- Vary the maximum discount factor with the premium size of the group, reflecting the credibility of the group size, but without a credibility formula.
- Apply a phase-in period of at least two years to new group members prior to receiving the full group discount, e.g. 1<sup>st</sup> year 25%, 2<sup>nd</sup> year 50% .

# Group Rating

## Deloitte Conclusions (continued):

Evaluate possible alternatives for group rating:

- **Group dividend plan**, in which dividends are credited to group members based on the actual profits generated by the group. Both new and established groups could be eligible for such a program.
- **Group retro plan**, in which premiums are adjusted upward or downward within certain limits depending on the actual loss experience of the group.
- **Per accident loss limitations (optional at different amounts)** for any group rating program, in which large losses are capped before being used in group rating.
- **Tiering** within a single group, with varying discounts by tier, where the average discount over all tiers equals the total discount for the group.