

# Workers Compensation State of the Market

WC - 3  
CAS Ratemaking Seminar  
March 17, 18, 2008

Jim Davis, ACAS, MAAA  
Chauncey Fleetwood, FCAS, MAAA  
Tony DiDonato, FCAS, MAAA

- Property/Casualty Results
- Workers Compensation Results
- WC Claim Frequency Research
- Concluding Remarks

# Property/Casualty Results

# P/C Industry Net Written Premium Continues Slow Growth

Private Carriers

Line of Business (LOB)	2004	2005	2006	2005– 2006 Change
Personal Auto	\$157.3 B	\$159.5 B	\$160.2 B	0.4%
Homeowners	\$51.6 B	\$54.5 B	\$54.5 B	0.1%
Other Liability (Incl Prod Liab)	\$43.0 B	\$42.7 B	\$42.0 B	-1.5%
<b>Workers Compensation</b>	<b>\$34.7 B</b>	<b>\$37.8 B</b>	<b>\$38.5 B</b>	<b>2.0%</b>
Commercial Multiple Peril	\$29.1 B	\$29.6 B	\$31.7 B	7.3%
Commercial Auto	\$26.6 B	\$26.5 B	\$26.7 B	0.5%
Fire & Allied Lines (Incl EQ)	\$17.6 B	\$17.4 B	\$17.1 B	-1.8%
All Other Lines	\$64.2 B	\$57.5 B	\$72.3 B	16.6%
<b>Total P/C Industry</b>	<b>\$424.1 B</b>	<b>\$425.5 B</b>	<b>\$441.9 B</b>	<b>3.8%</b>

Source: A.M. Best Aggregates & Averages

# Industry Underwriting Results Are Remarkably Good

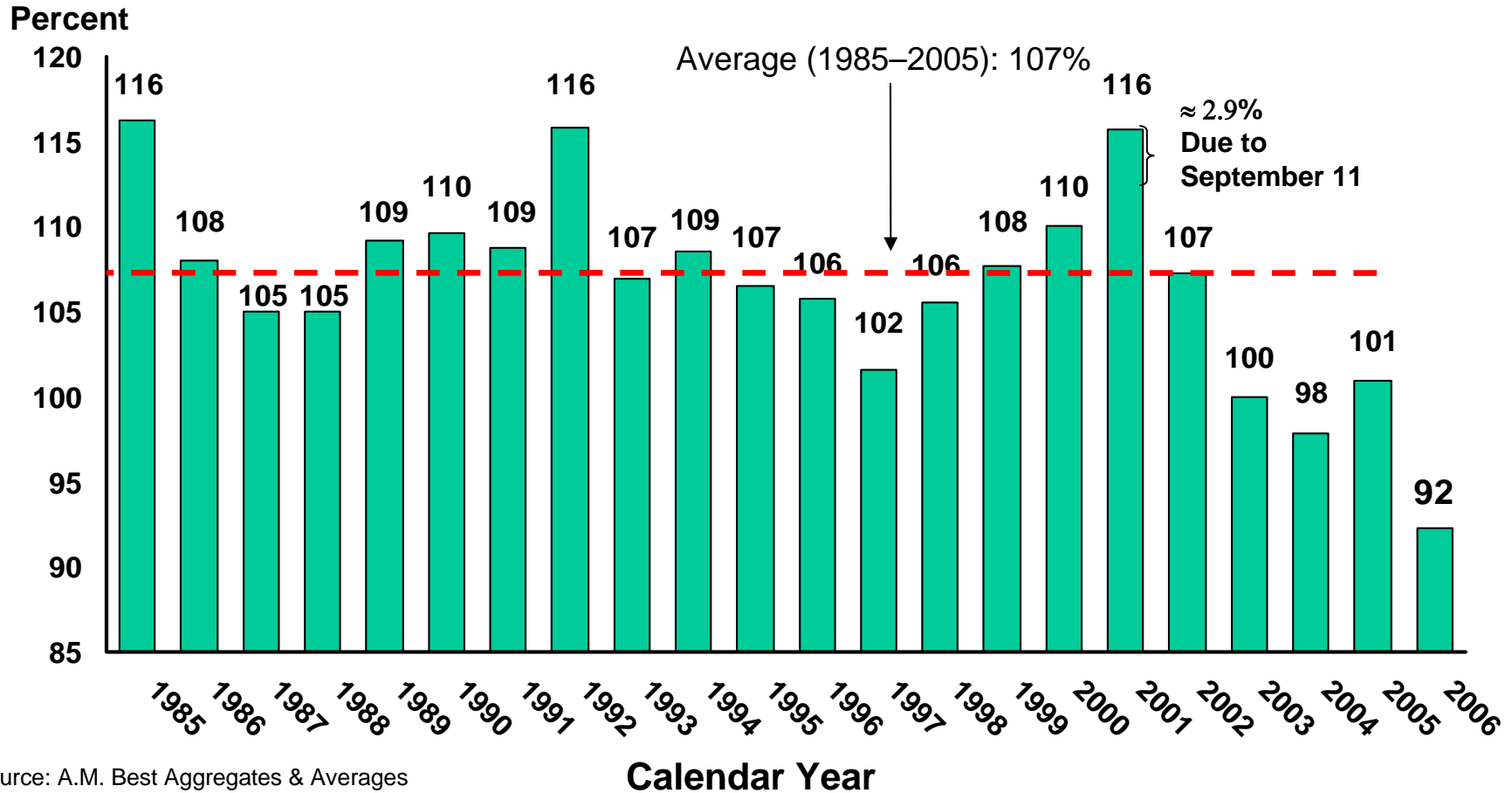
Net Combined Ratio—Private Carriers

Line of Business (LOB)	Calendar Year		
	2004	2005	2006
Personal Auto	94%	95%	97%
Homeowners	94%	100%	90%
Other Liability (Incl Prod Liab)	117%	113%	96%
<b>Workers Compensation</b>	<b>107%</b>	<b>103%</b>	<b>93.1%</b>
Commercial Multiple Peril	101%	97%	93%
Commercial Auto	93%	92%	91%
Fire & Allied Lines (Incl EQ)	87%	104%	81%
All Other Lines	99%	112%	86%
<b>Total P/C Industry</b>	<b>98%</b>	<b>101%</b>	<b>92%</b>

Source: A.M. Best Aggregates & Averages

# P/C Industry Calendar Year Net Combined Ratios

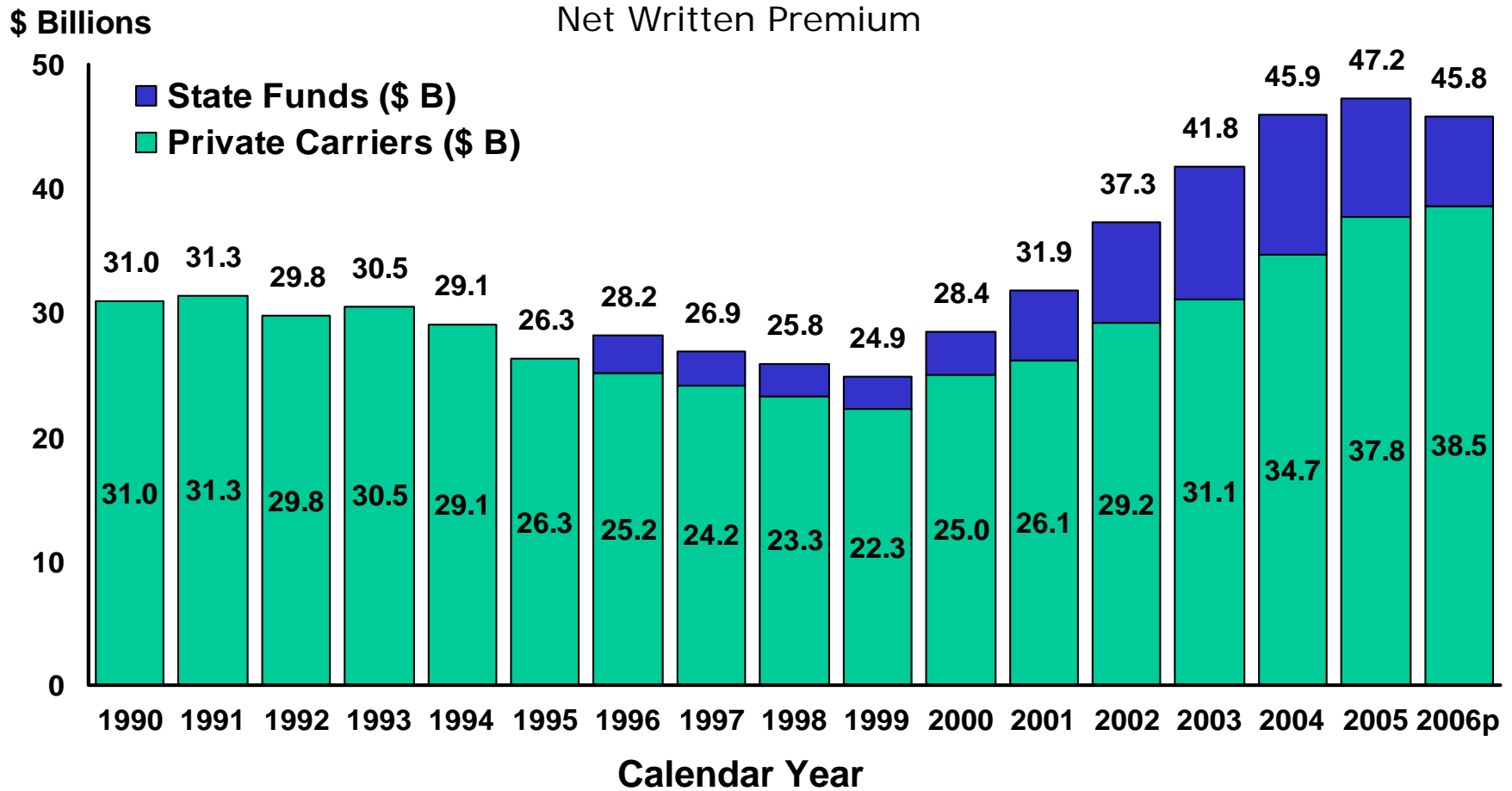
Private Carriers



Source: A.M. Best Aggregates & Averages

# Workers Compensation Results

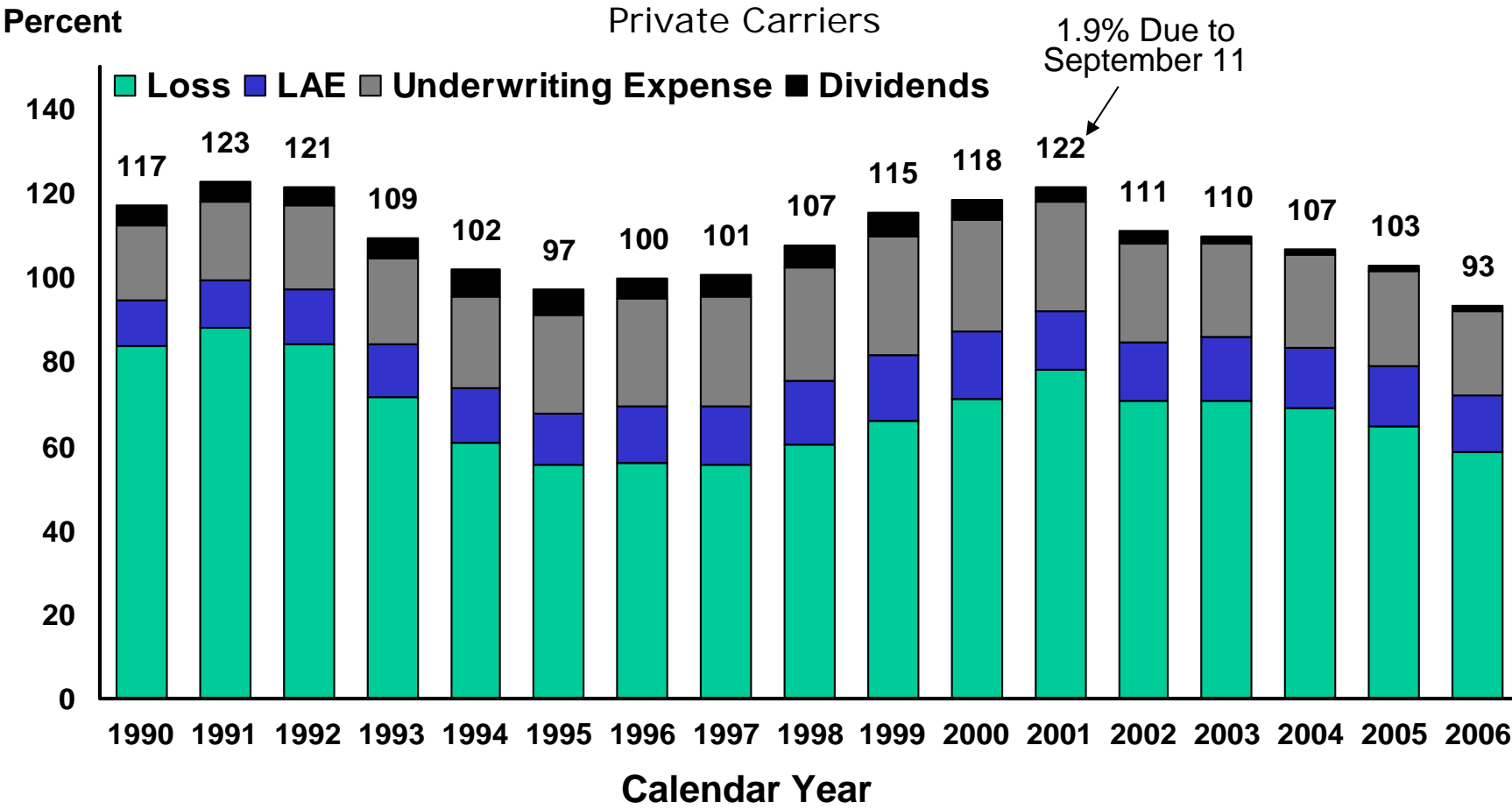
# Total Workers Compensation Premium Declined in 2006



Source: A.M. Best Aggregates & Averages  
 State Funds: AZ, CA, CO, HI, ID, KY, LA, MO, MT, NM, OR, RI, TX, UT Annual Statements  
 State Funds available for 1996 and subsequent

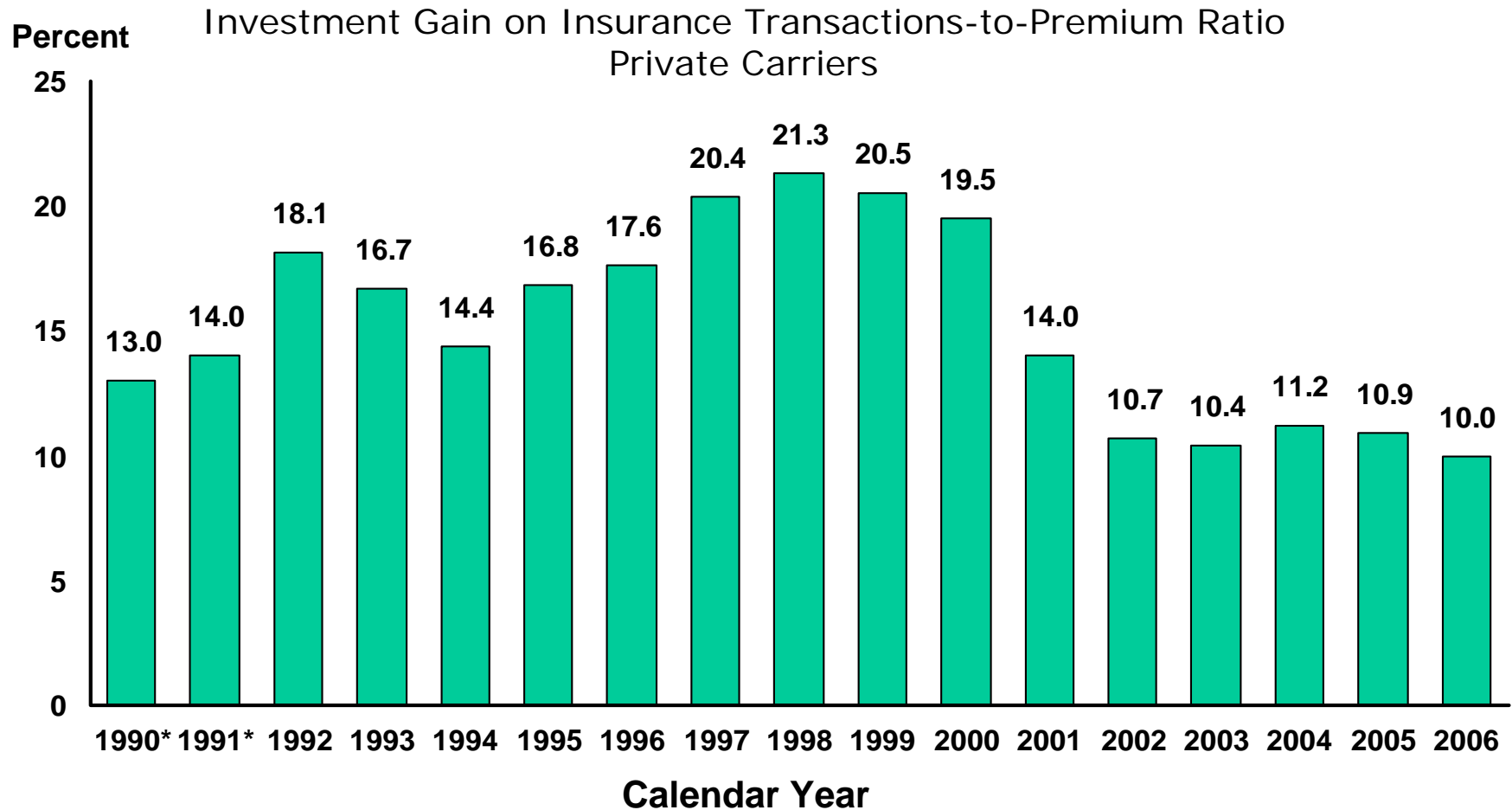


# WC Calendar Year Combined Ratio Best in at Least 30 Years



Source: A.M. Best Aggregates & Averages

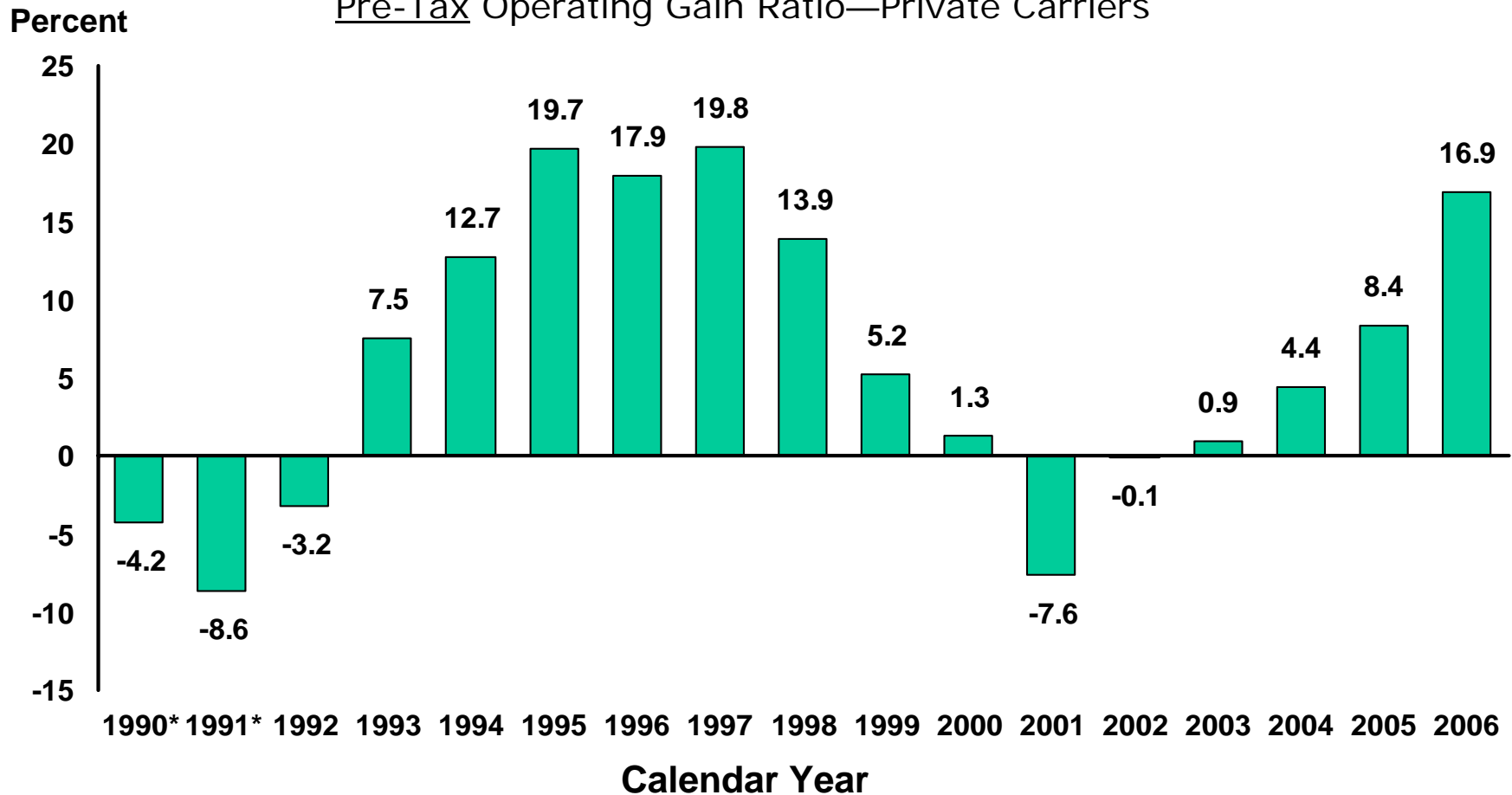
# Workers Compensation Investment Returns Show Little Change in 2006



\* Adjusted to include realized capital gains to be consistent with 1992 and after  
Investment Gain on Insurance Transactions includes Other Income  
Source: A.M. Best Aggregates & Averages

# Workers Compensation Results Continue to Improve

Pre-Tax Operating Gain Ratio—Private Carriers



\* Adjusted to include realized capital gains to be consistent with 1992 and after

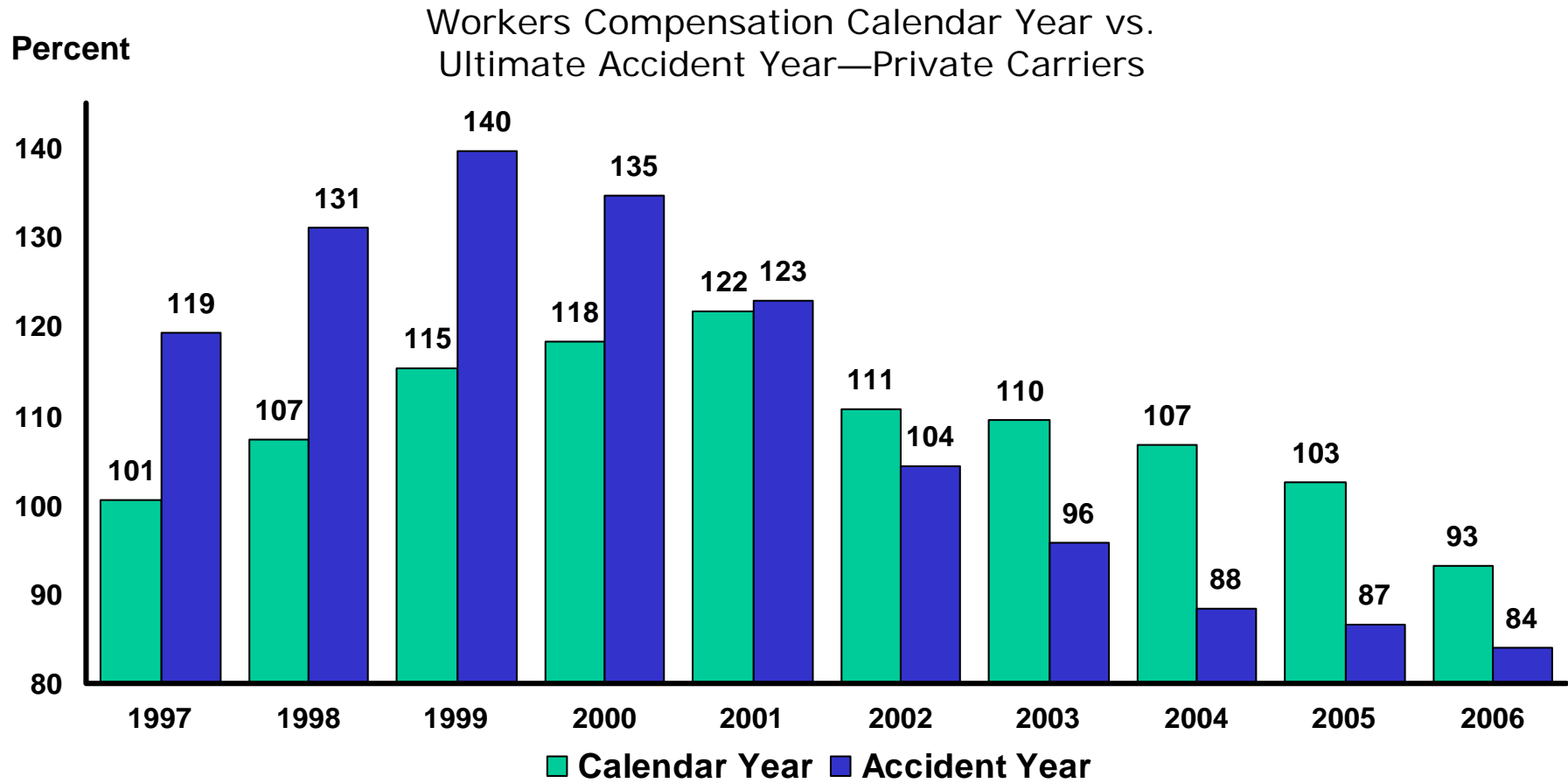
Operating Gain equals 1.00 minus (Combined Ratio less Investment Gain on Insurance Transactions and Other Income)

Source: A.M. Best Aggregates & Averages

# Workers Compensation

## Accident Year Results and Reserve Estimates

# Accident Year Combined Ratio— Another Underwriting Profit in 2006



p Preliminary

Accident Year data is evaluated as of 12/31/2006 and developed to ultimate

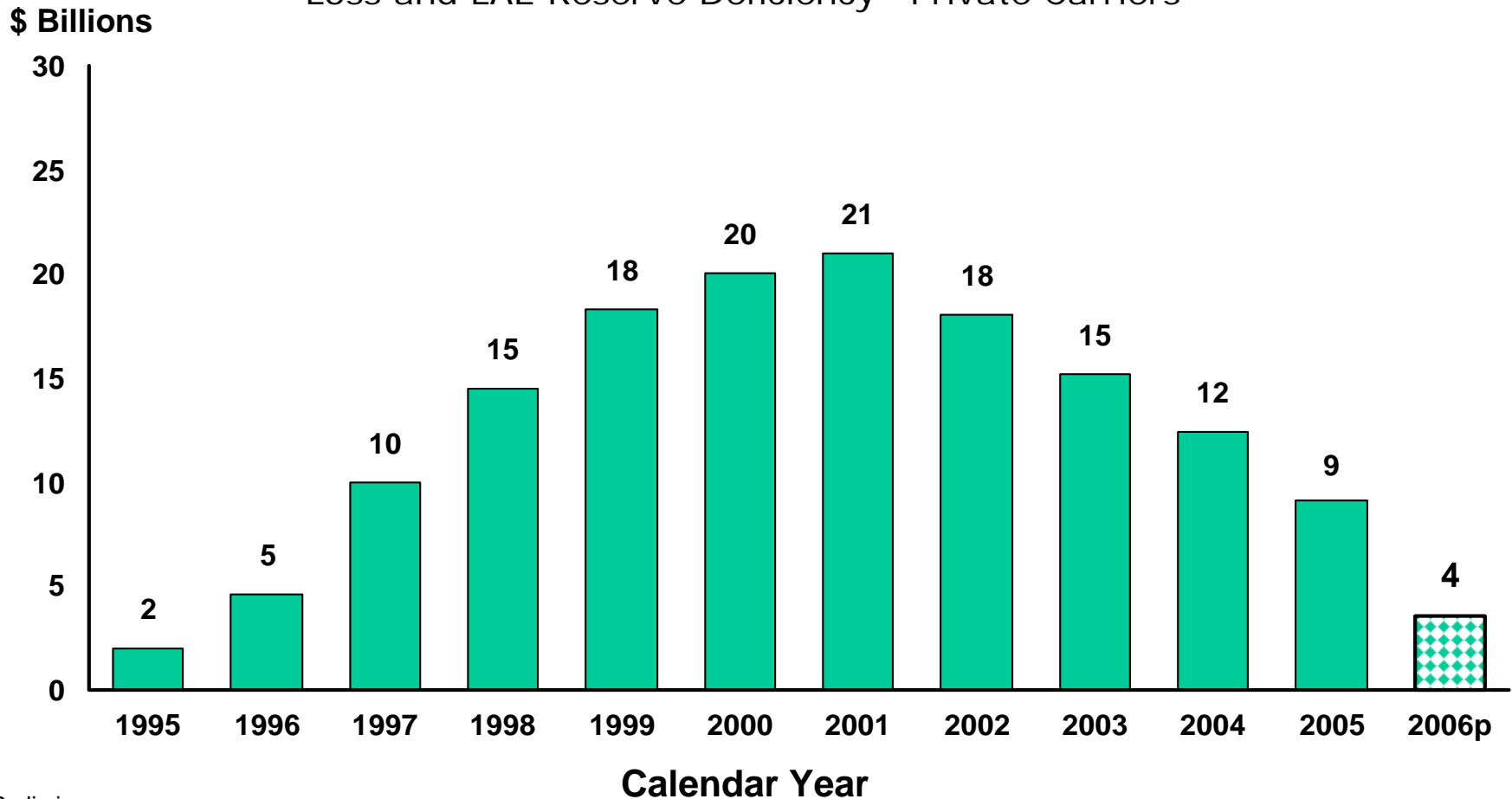
Source: Calendar Years 1997–2006, A.M. Best Aggregates & Averages

Accident Years 1997–2006, NCCI analysis based on Annual Statement data

Includes dividends to policyholders

# Workers Compensation Reserve Deficiencies Continue to Decline

Loss and LAE Reserve Deficiency—Private Carriers



p Preliminary

Considers all reserve discounts as deficiencies

Tabular Discounts are approximately \$5–6 Billion from 1995 to 2006

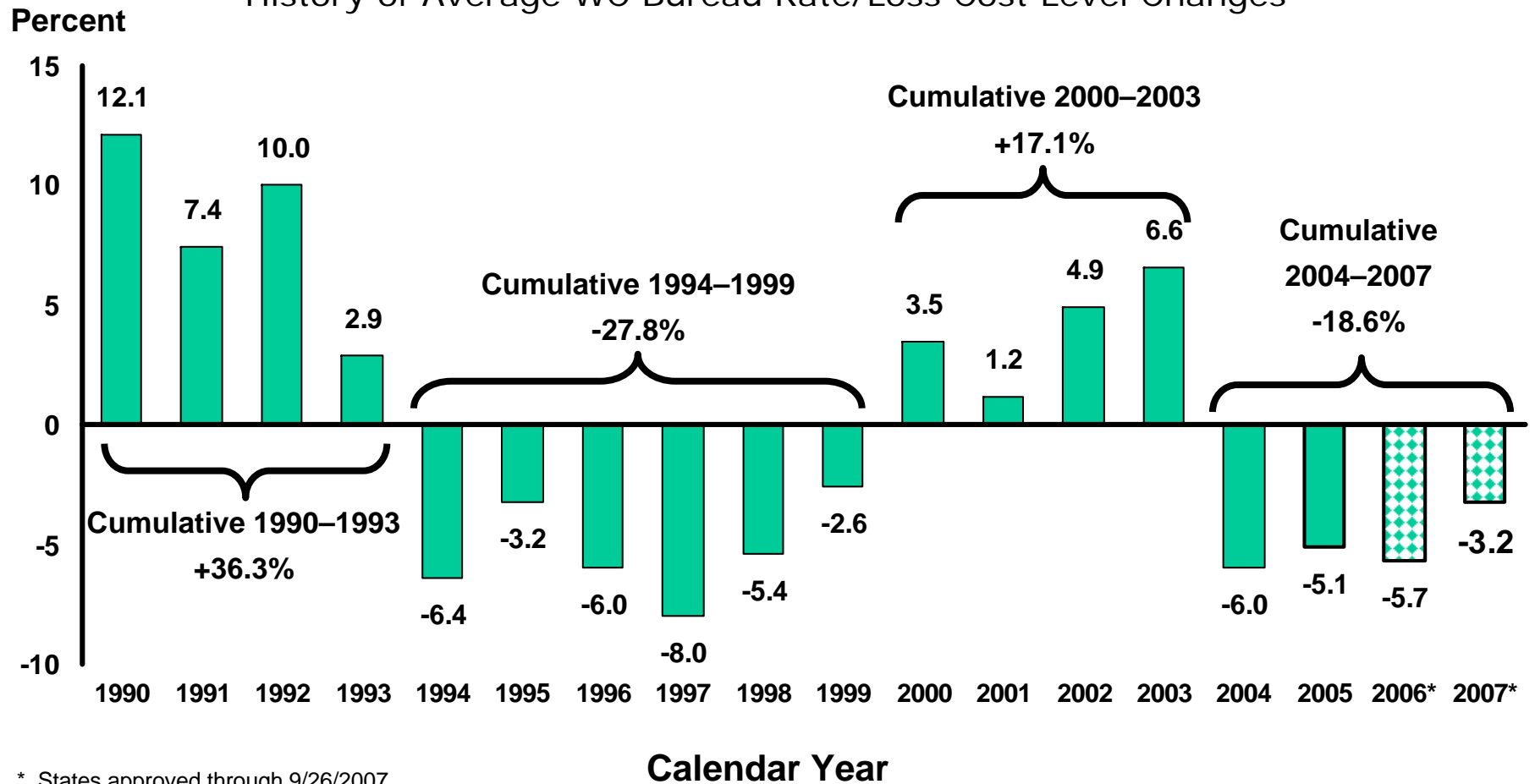
Loss and LAE figures are based on NAIC Annual Statement data for each valuation date and NCCI latest selections

Source: 1996–2006p, NCCI analysis

# Workers Compensation Premium Drivers

# Average Approved Bureau Rates/Loss Costs

History of Average WC Bureau Rate/Loss Cost Level Changes



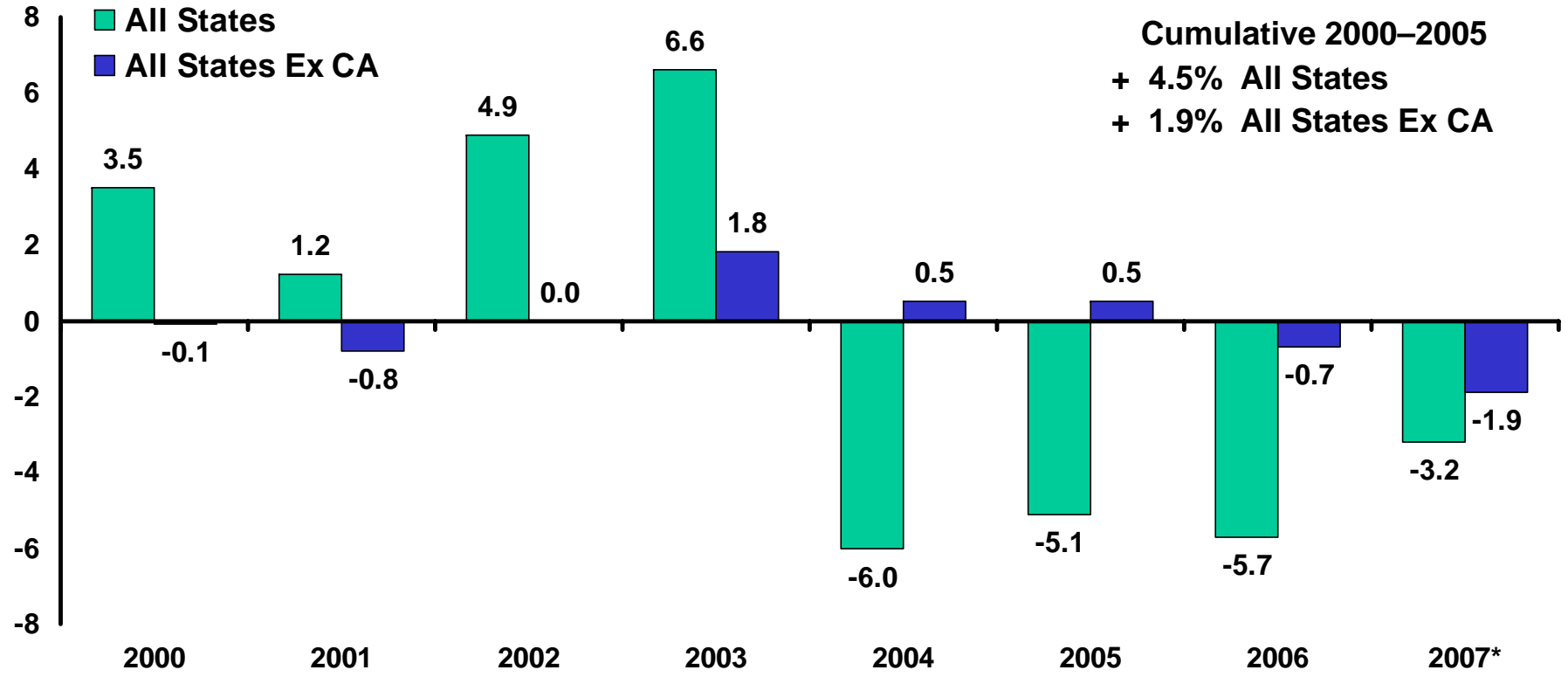
Countrywide approved changes in advisory rates, loss costs and assigned risk rates as filed by the applicable rating organization



# Average Approved Bureau Rates/Loss Costs

All States vs. All States Excluding California

Percent

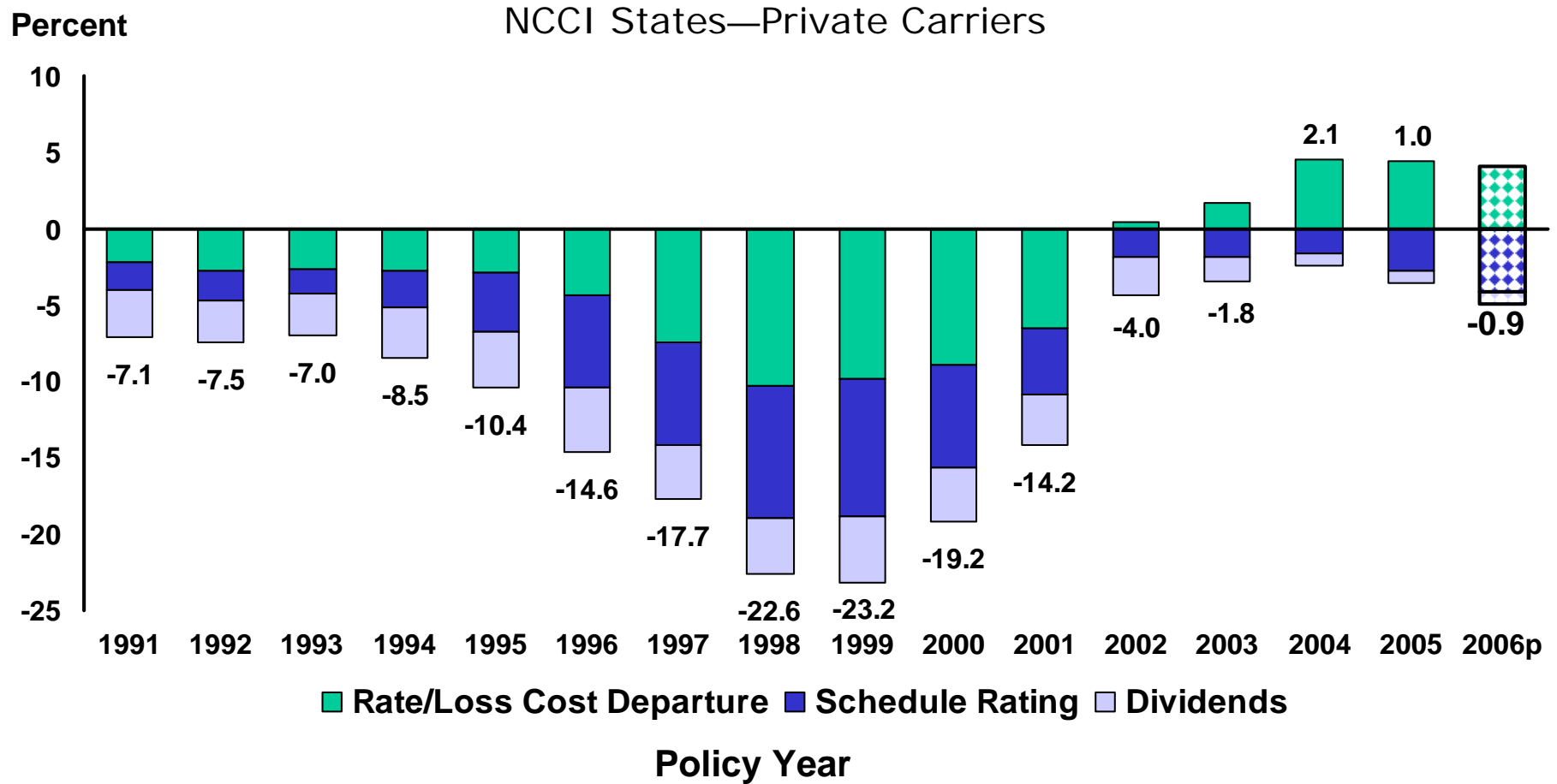


Calendar Year

\* States approved through 4/13/2007

Countrywide approved changes in advisory rates, loss costs and assigned risk rates as filed by the applicable rating organization

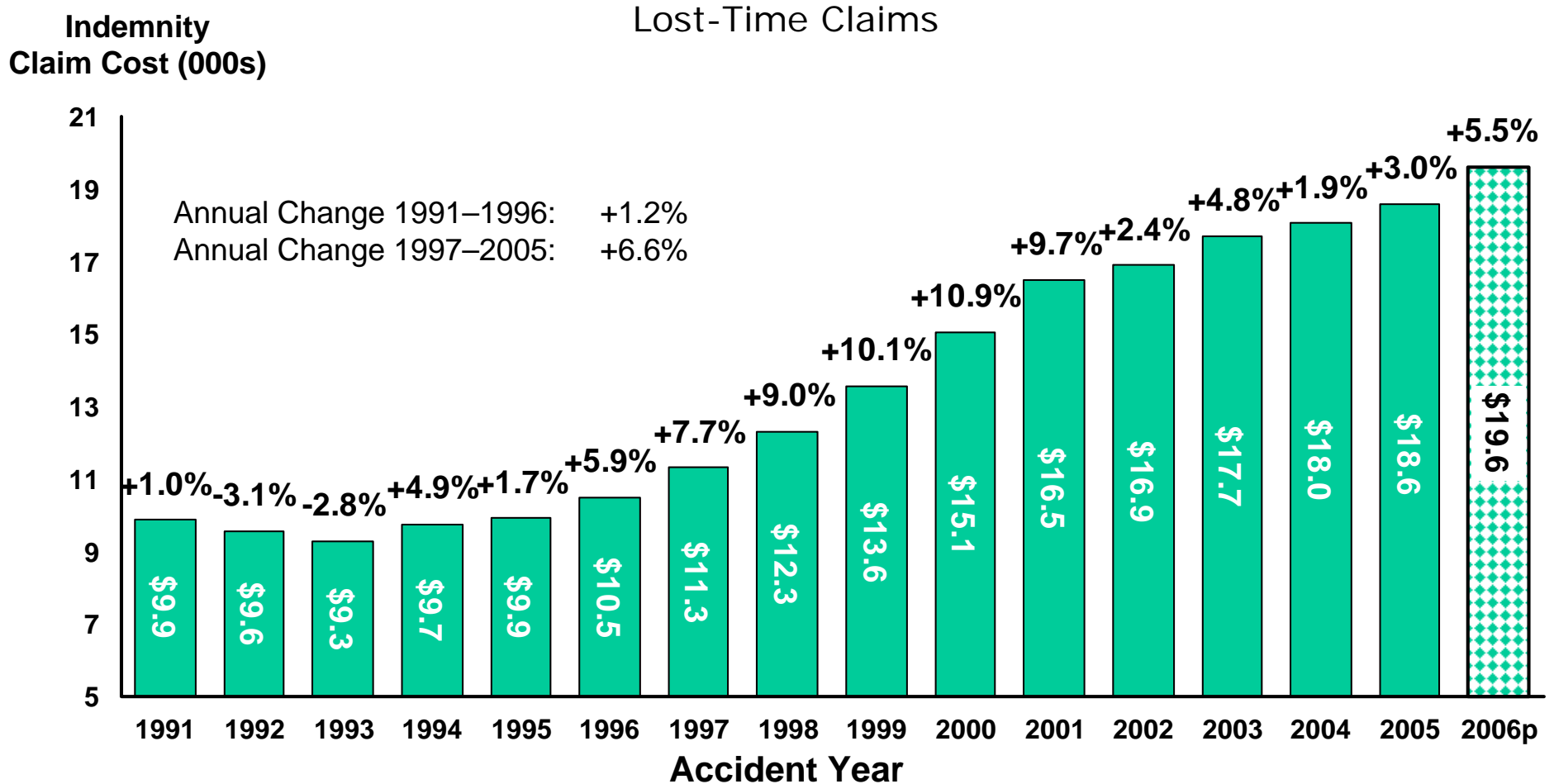
# Impact of Discounting on Workers Compensation Premium



p Preliminary  
 NCCI benchmark level does not include an underwriting contingency provision  
 Dividend ratios are based on calendar year statistics  
 Based on data through 12/31/2006 for the states where NCCI provides ratemaking services

# Workers Compensation Loss Drivers

# Workers Compensation Indemnity Claim Costs

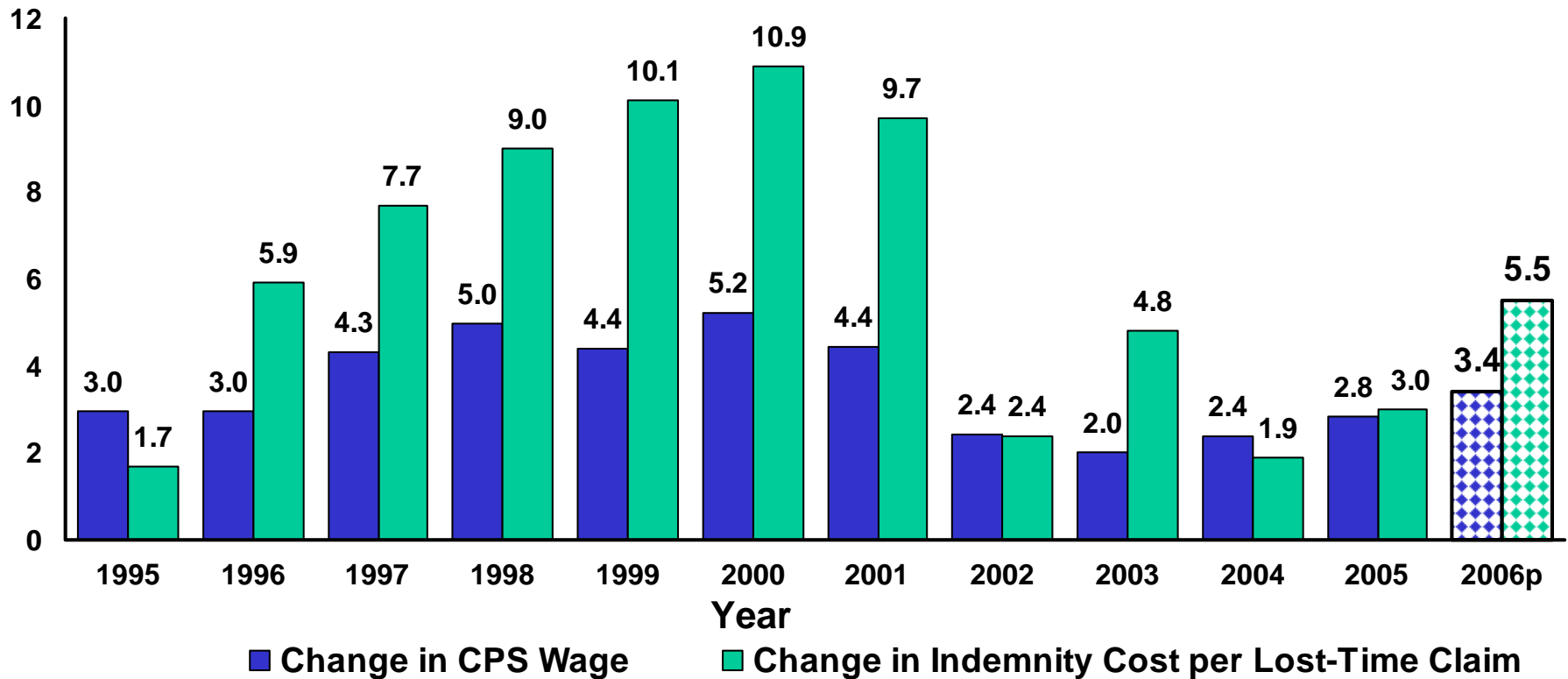


2006p: Preliminary based on data valued as of 12/31/2006  
 1991–2005: Based on data through 12/31/2005, developed to ultimate  
 Based on the states where NCCI provides ratemaking services  
 Excludes the effects of deductible policies

# WC Indemnity Severity Outpacing Wage Inflation in 2006

Lost-Time Claims

Percent Change

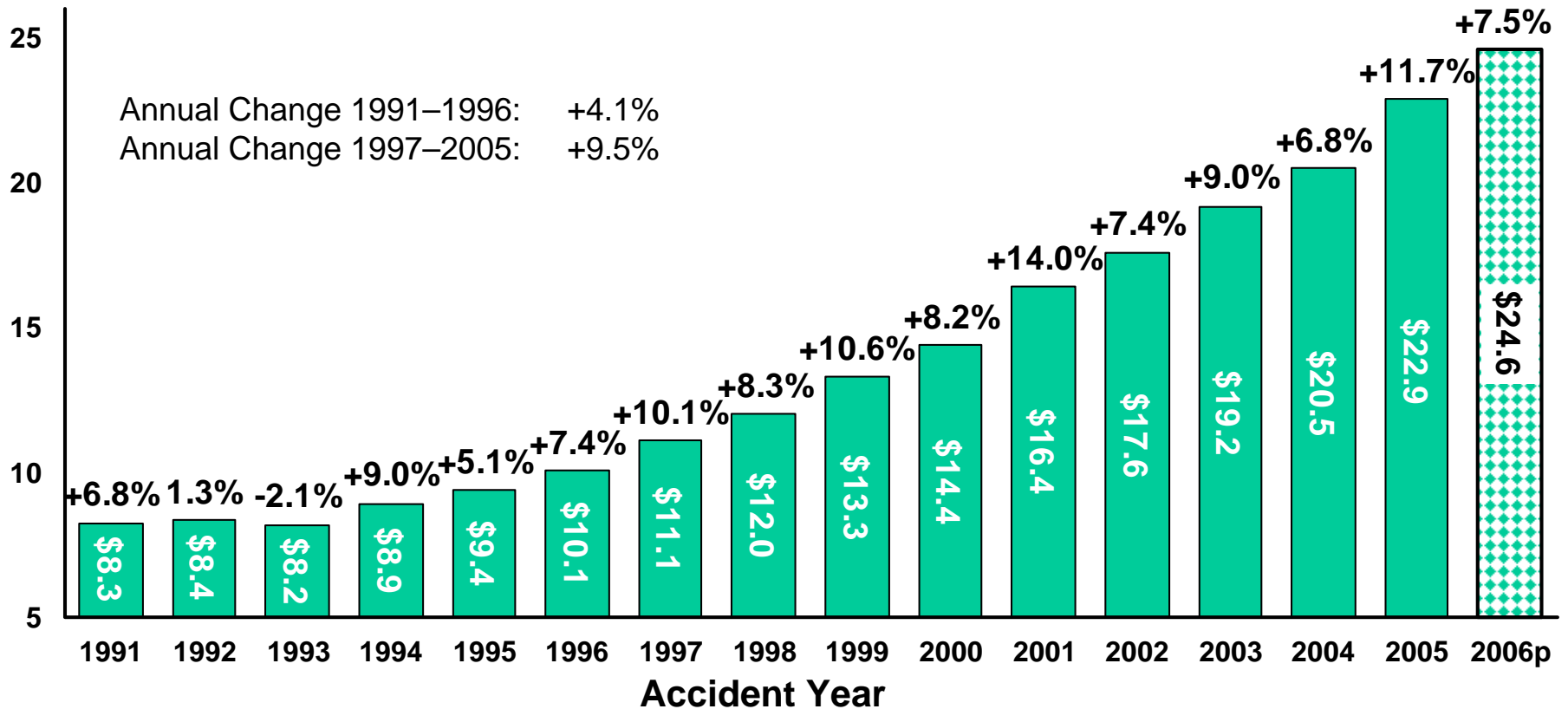


Indemnity severity 2006p: Preliminary based on data valued as of 12/31/2006  
 Indemnity severity 1995–2005: Based on data through 12/31/2005, developed to ultimate  
 Based on the states where NCCI provides ratemaking services, excludes the effects of deductible policies  
 Source: CPS Wage—All states (Current Population Survey), Economy.com;  
 Accident year indemnity severity—NCCI states, NCCI

# WC Medical Claim Cost Trends— Growth Continues in 2006

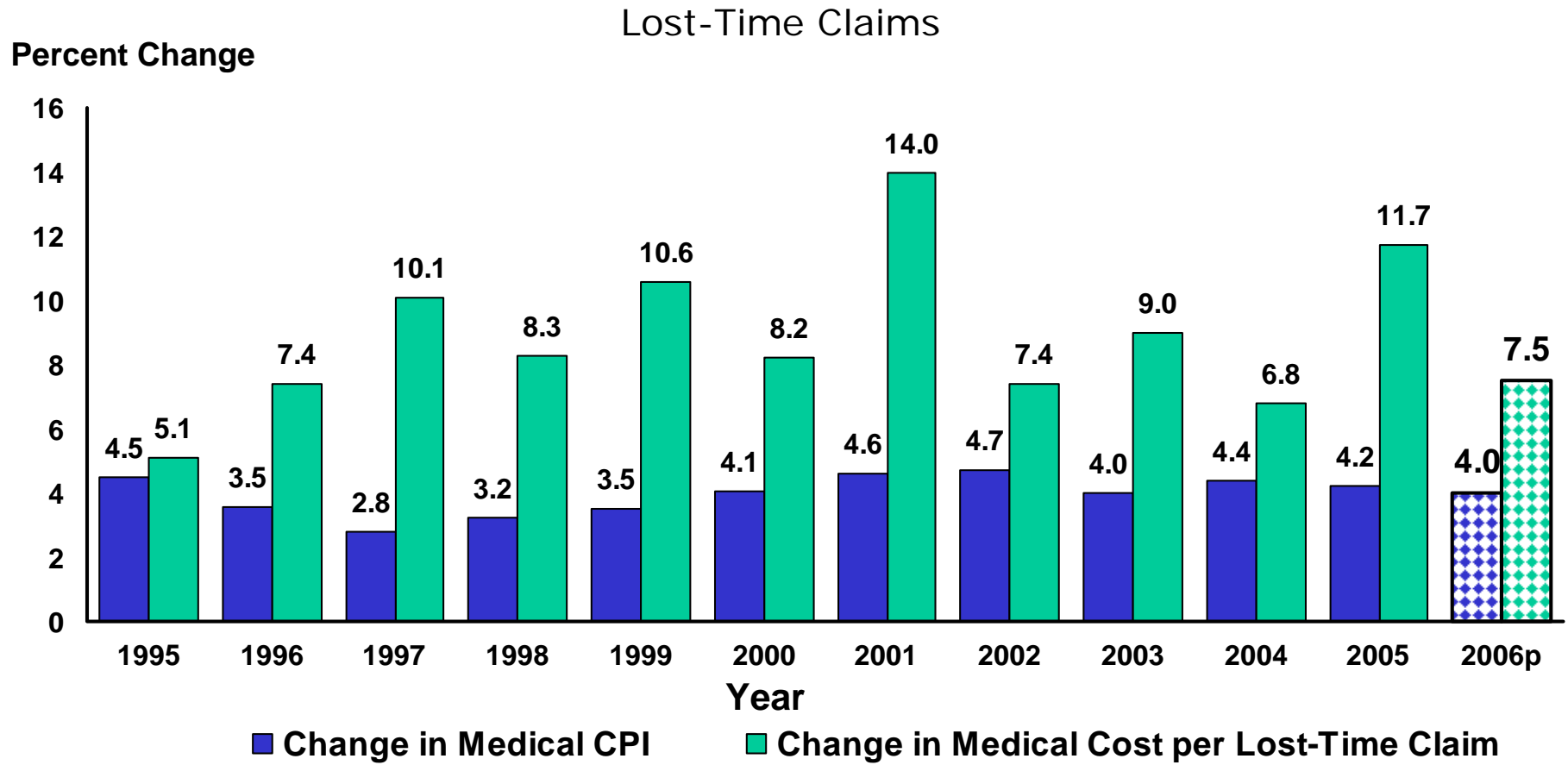
Medical  
Claim Cost (000s)

Lost-Time Claims



2006p: Preliminary based on data valued as of 12/31/2006  
 1991–2005: Based on data through 12/31/2005, developed to ultimate  
 Based on the states where NCCI provides ratemaking services  
 Excludes the effects of deductible policies

# WC Medical Severity Still Growing Much Faster Than the Medical CPI

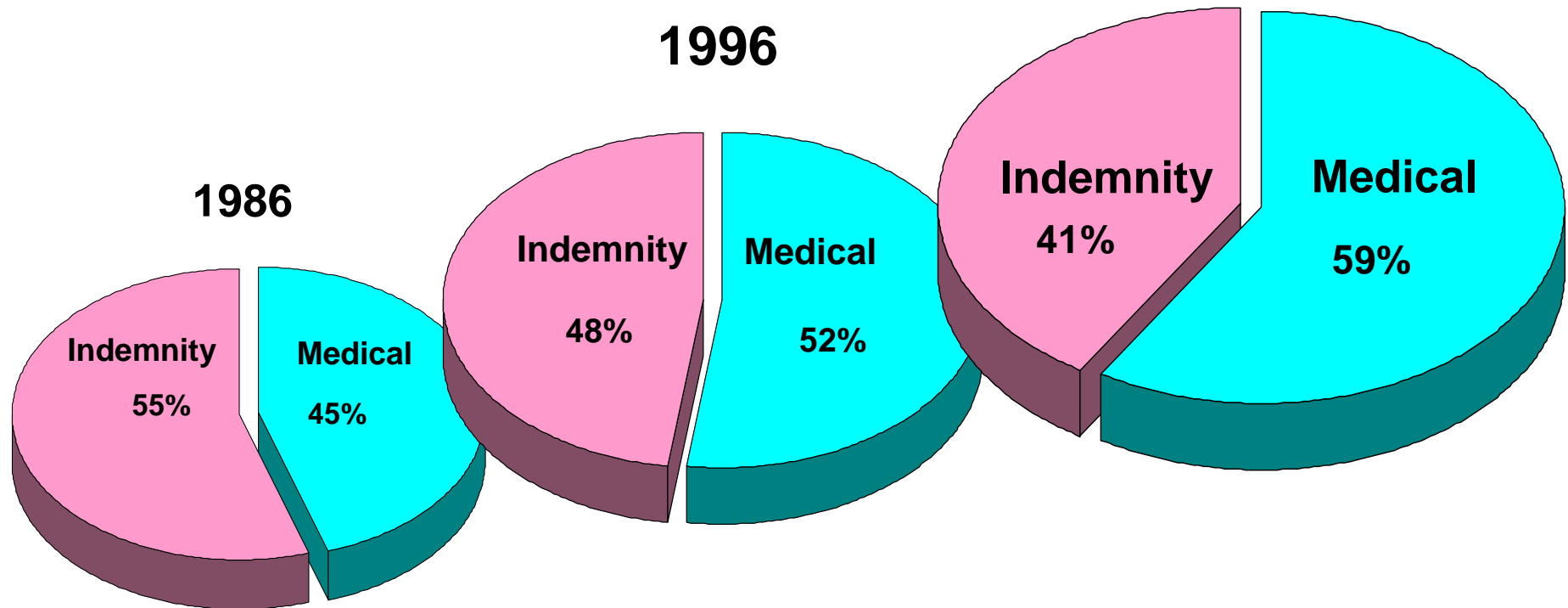


Medical severity 2006p: Preliminary based on data valued as of 12/31/2006  
 Medical severity 1995–2005: Based on data through 12/31/2005, developed to ultimate  
 Based on the states where NCCI provides ratemaking services, excludes the effects of deductible policies  
 Source: Medical CPI—All states, Economy.com; Accident year medical severity—NCCI states, NCCI

# Workers Compensation Medical Losses Are More Than Half of Total Losses

All Claims—NCCI States

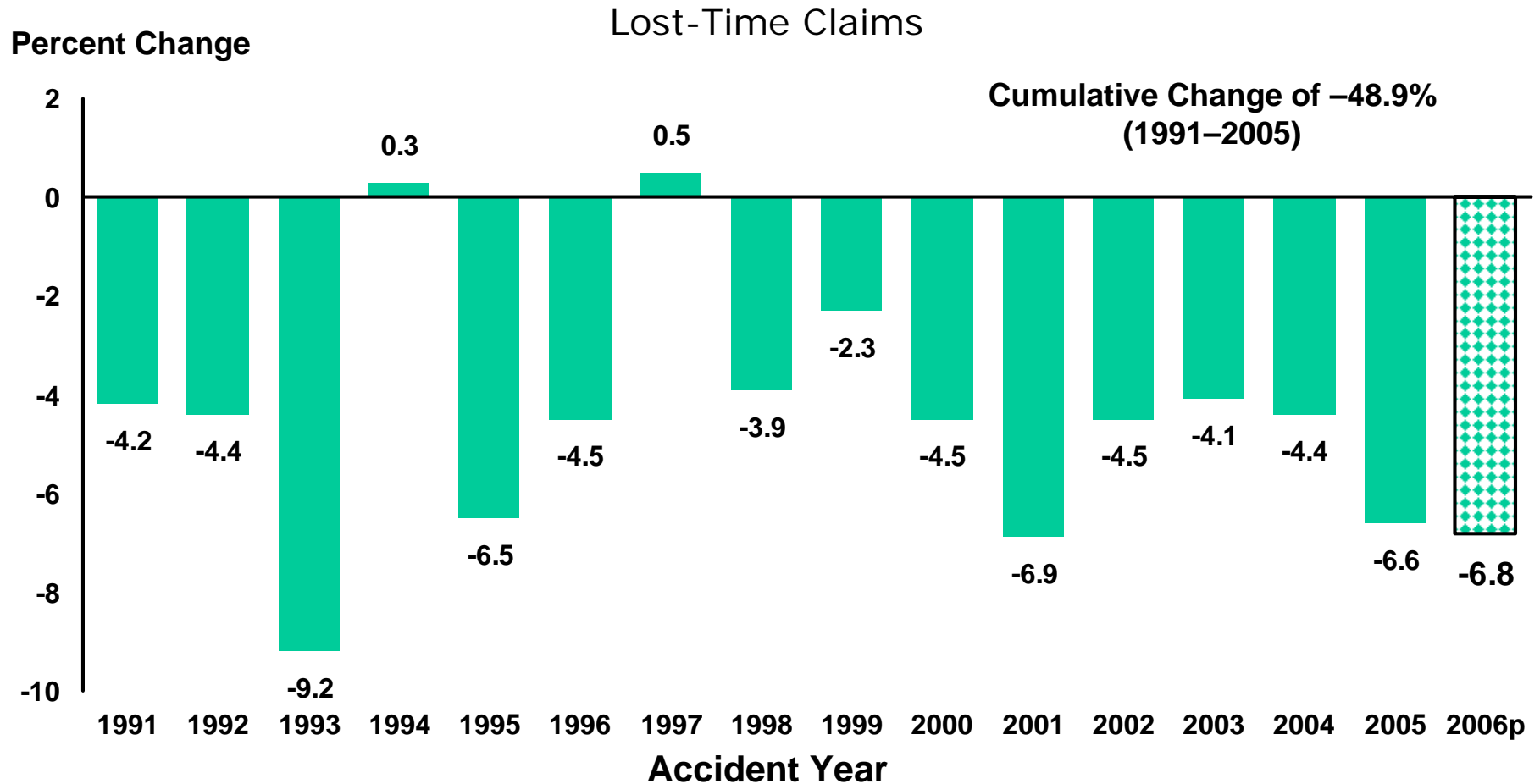
**2006p**



2006p: Preliminary based on data valued as of 12/31/2006  
1986, 1996: Based on data through 12/31/2005, developed to ultimate  
Based on the states where NCCI provides ratemaking services  
Excludes the effects of deductible policies

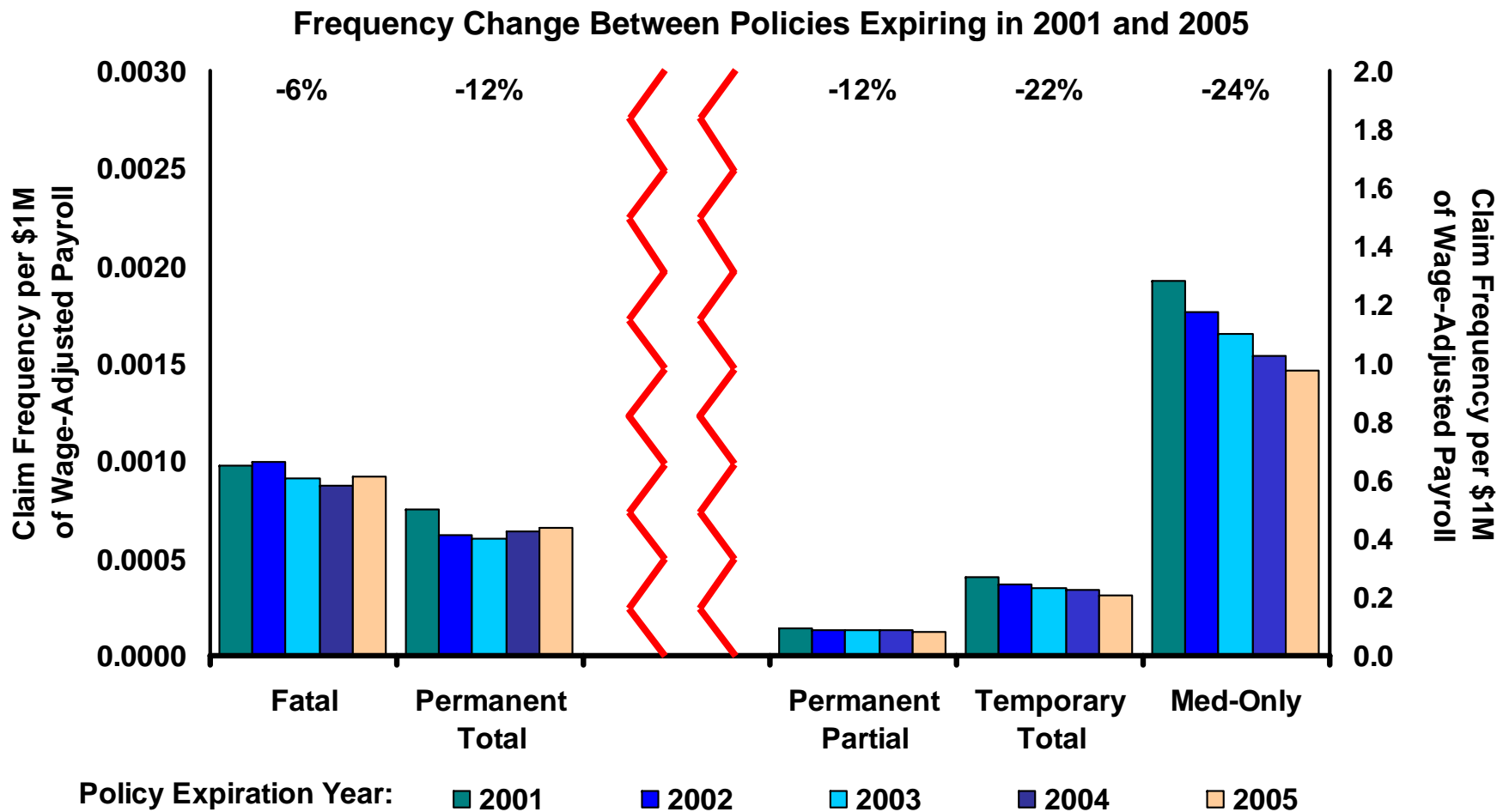


# Workers Compensation Lost-Time Claim Frequency Continues to Decline



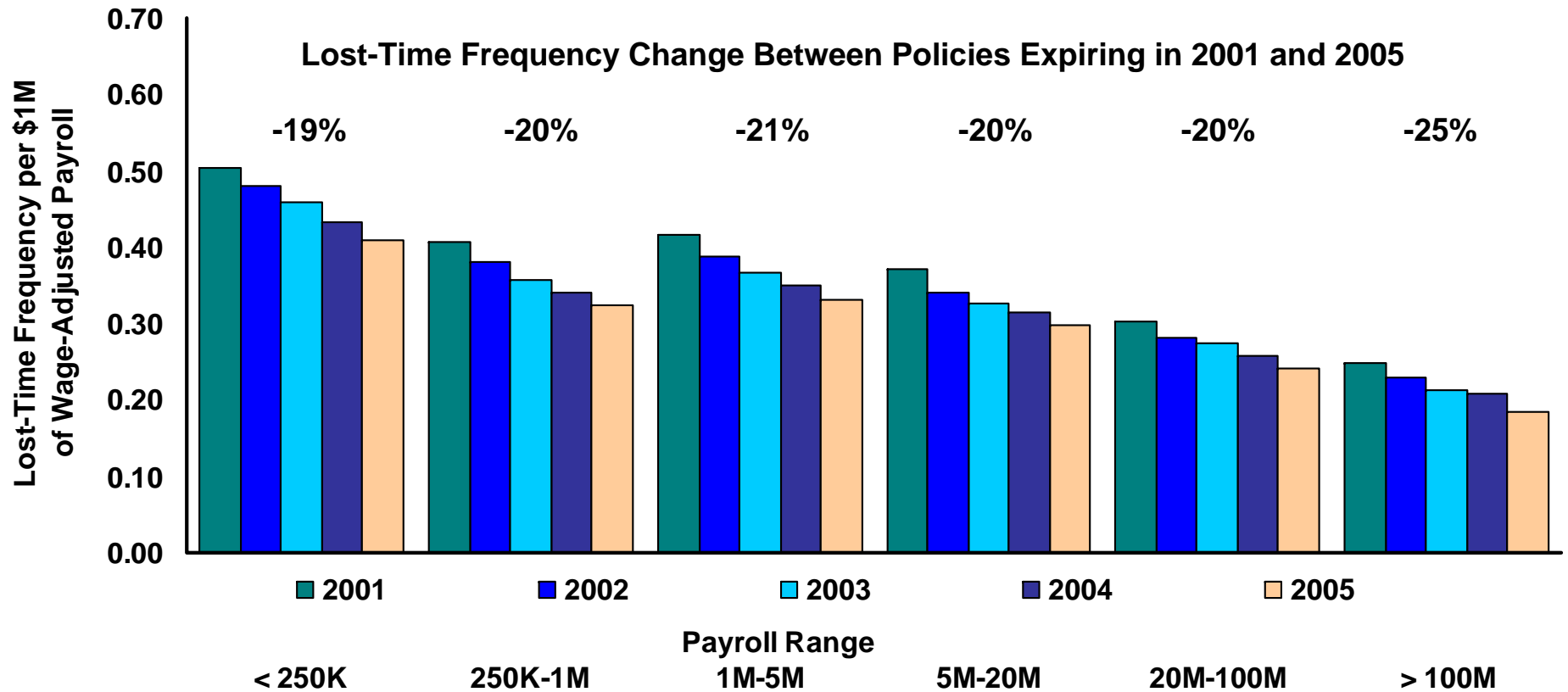
2006p: Preliminary based on data valued as of 12/31/2006  
 1991-2005: Based on data through 12/31/2005, developed to ultimate  
 Based on the states where NCCI provides ratemaking services  
 Excludes the effects of deductible policies

# Claim Frequency by Injury Type



Claim count determined at first report  
 Frequency = claims / payroll; Payroll adjusted for inflation  
 All NCCI states; excludes NV & TX

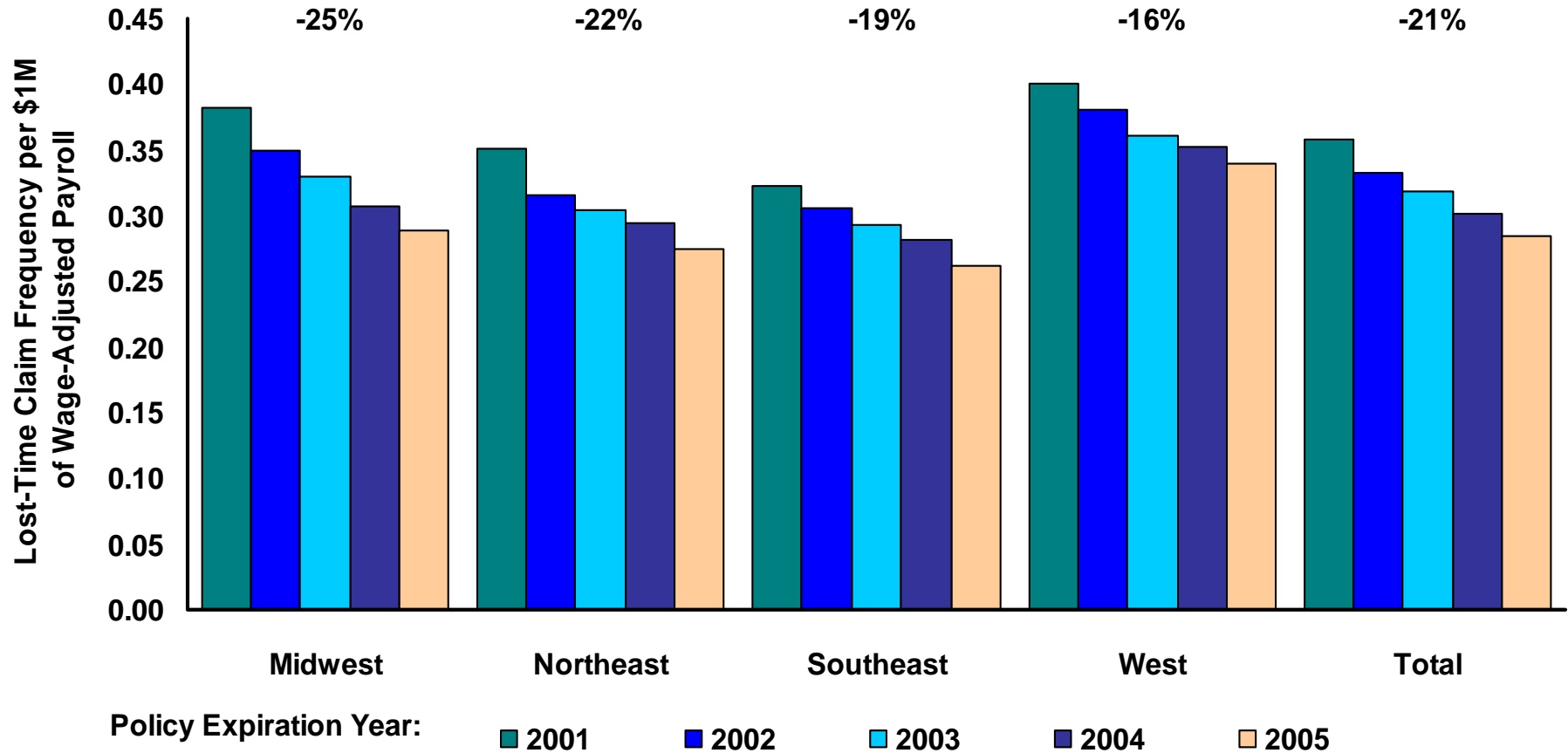
# Lost-Time Claim Frequency by Size of Payroll



Frequency = Lost-time claims/payroll. Payroll adjusted for inflation  
 Claim count determined at first report  
 NCCI states only

# Lost-Time Claim Frequency by Region

Lost-Time Frequency Change Between Policies Expiring in 2001 and 2005



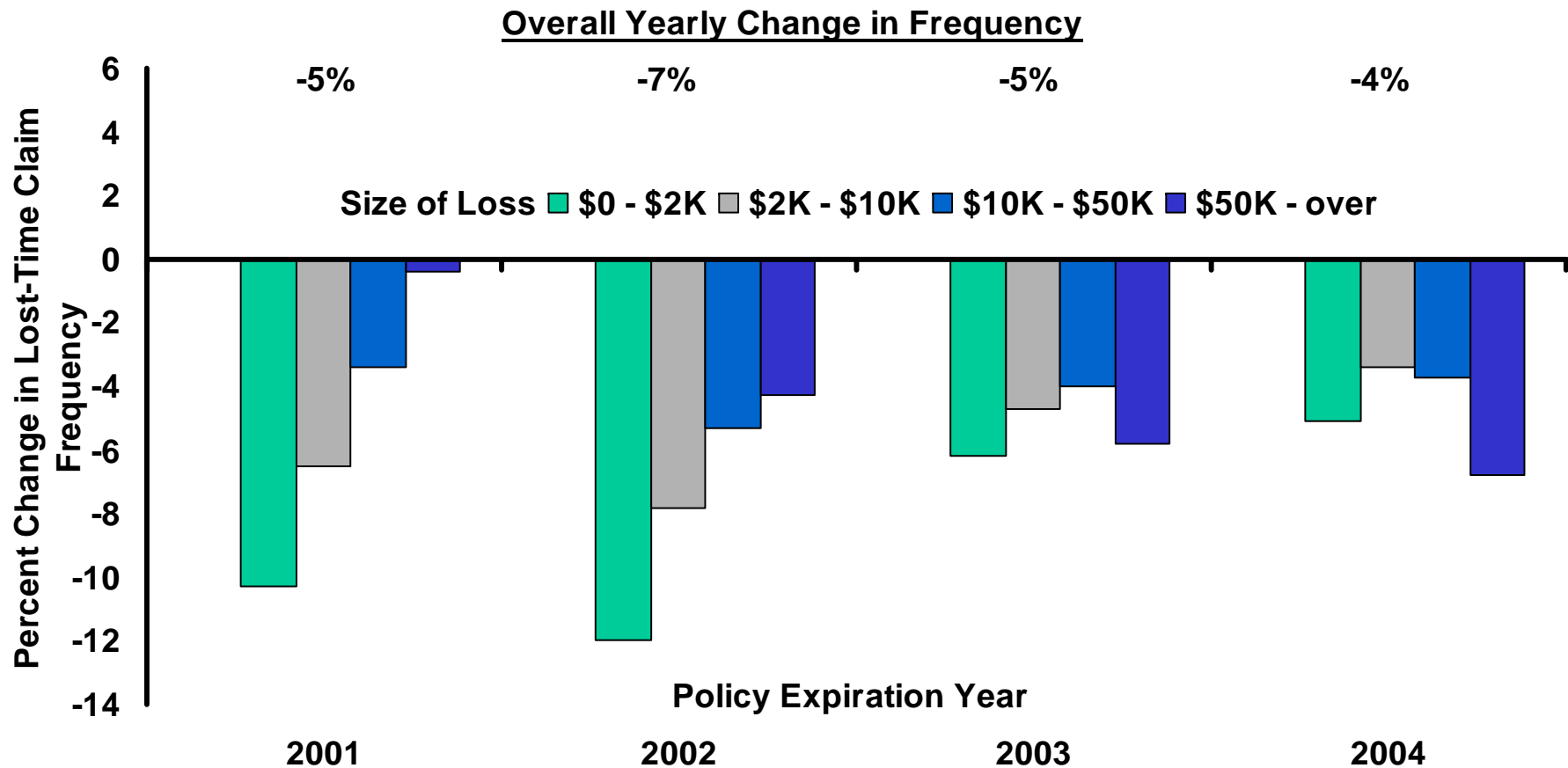
Claim count determined at first report  
 Frequency = Lost-time claims / payroll; Payroll adjusted for inflation  
 All NCCI states; excludes NV & TX

# Lost-Time Claim Frequency for Largest Classes

Countrywide Classes	Policies Expiring in 2005			Policies Expiring in 2001			Frequency Change
	Wage-Adjusted Payroll (\$M)	Lost Time # Claims	Lost Time Frequency	Lost Time # Claims	Lost Time Frequency		
<b>1. Manufacturing</b>							
Television/Radio	\$ 7,360	2,035	0.276	3,860	0.341	-19%	
Machine Shop	\$ 7,707	4,919	0.638	6,838	0.791	-19%	
Plastics Manufacturing	\$ 6,538	3,837	0.587	4,867	0.711	-17%	
<b>2. Contracting</b>							
Electrical Wiring	\$ 12,379	6,726	0.543	9,126	0.674	-19%	
Contractor-Supervisor	\$ 12,819	2,257	0.176	2,898	0.259	-32%	
Plumbing	\$ 10,244	6,533	0.638	8,178	0.752	-15%	
<b>3. Office and Clerical</b>							
Clerical	\$ 596,101	27,489	0.046	32,388	0.055	-17%	
Salesperson-Outside	\$ 138,180	8,634	0.062	10,591	0.079	-21%	
College Professional	\$ 69,034	5,752	0.083	8,172	0.105	-21%	
<b>4. Goods and Services</b>							
Store-Retail	\$ 39,324	16,898	0.430	17,518	0.492	-13%	
Restaurant/Caterer	\$ 30,608	16,836	0.550	22,665	0.752	-27%	
Auto Service/Repair	\$ 23,076	12,267	0.532	15,698	0.654	-19%	
<b>5. Miscellaneous</b>							
Trucking (NOC, Local, Long-Distance)	\$ 19,347	21,011	1.086	28,002	1.415	-23%	
Drivers/Chauffeurs	\$ 10,113	8,416	0.832	12,227	1.068	-22%	
Police Officers	\$ 8,932	4,375	0.490	5,533	0.622	-21%	
<b>Total All classes</b>	<b>\$ 1,768,682</b>	<b>501,221</b>	<b>0.283</b>	<b>627,258</b>	<b>0.358</b>	<b>-21%</b>	
<b>Mixed-Adjusted Total</b>						<b>-18%</b>	

Claim count determined at first report  
 Frequency = Lost-time claims / payroll; Payroll adjusted for inflation  
 All NCCI states; excludes NV

# Year to Year Change in Lost-Time Frequency By Size of Loss Group

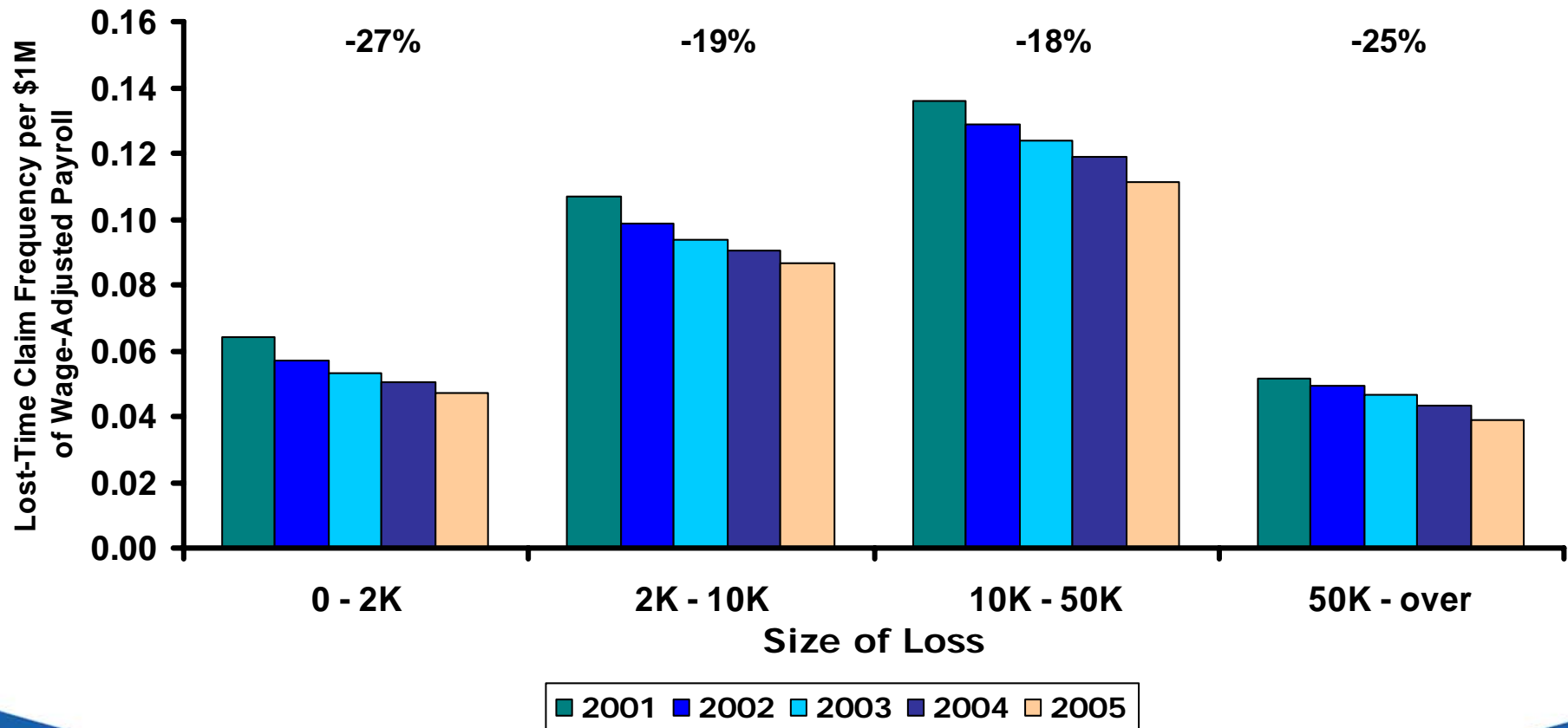


Claim count determined at first report  
 Loss size adjustments vary by year, averaging 3.8% indemnity and 7.4% medical  
 Frequency Loss = (time claims / payroll); Payroll adjusted for inflation  
 AIA, NCCI States and TX, excludes NV

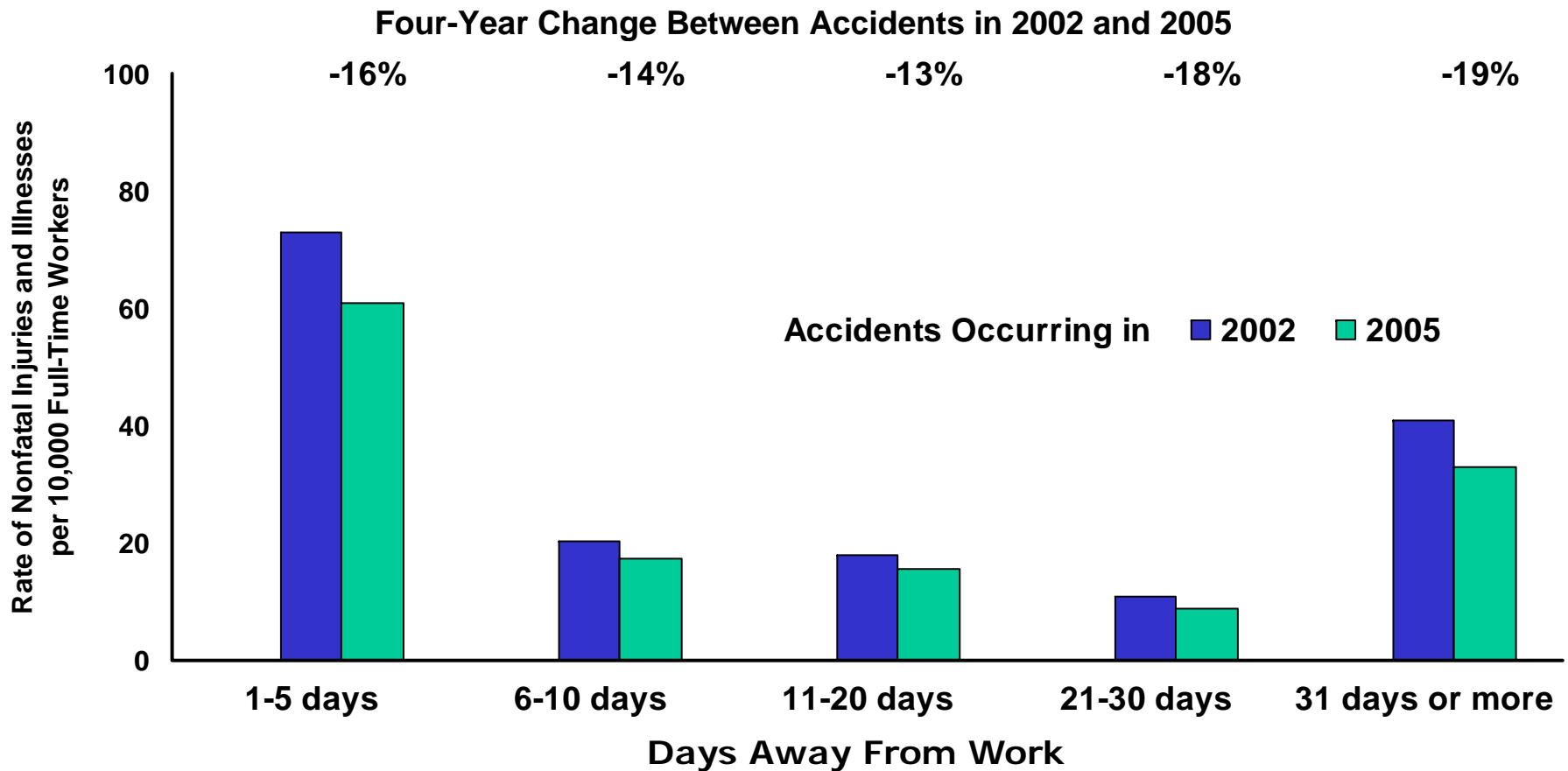
# Lost-Time Claim Frequency by Size of Loss

Frequency at First Report

Lost-Time Frequency Change Between Policies Expiring in 2001 and 2005



# Claim Frequency by Days Away From Work

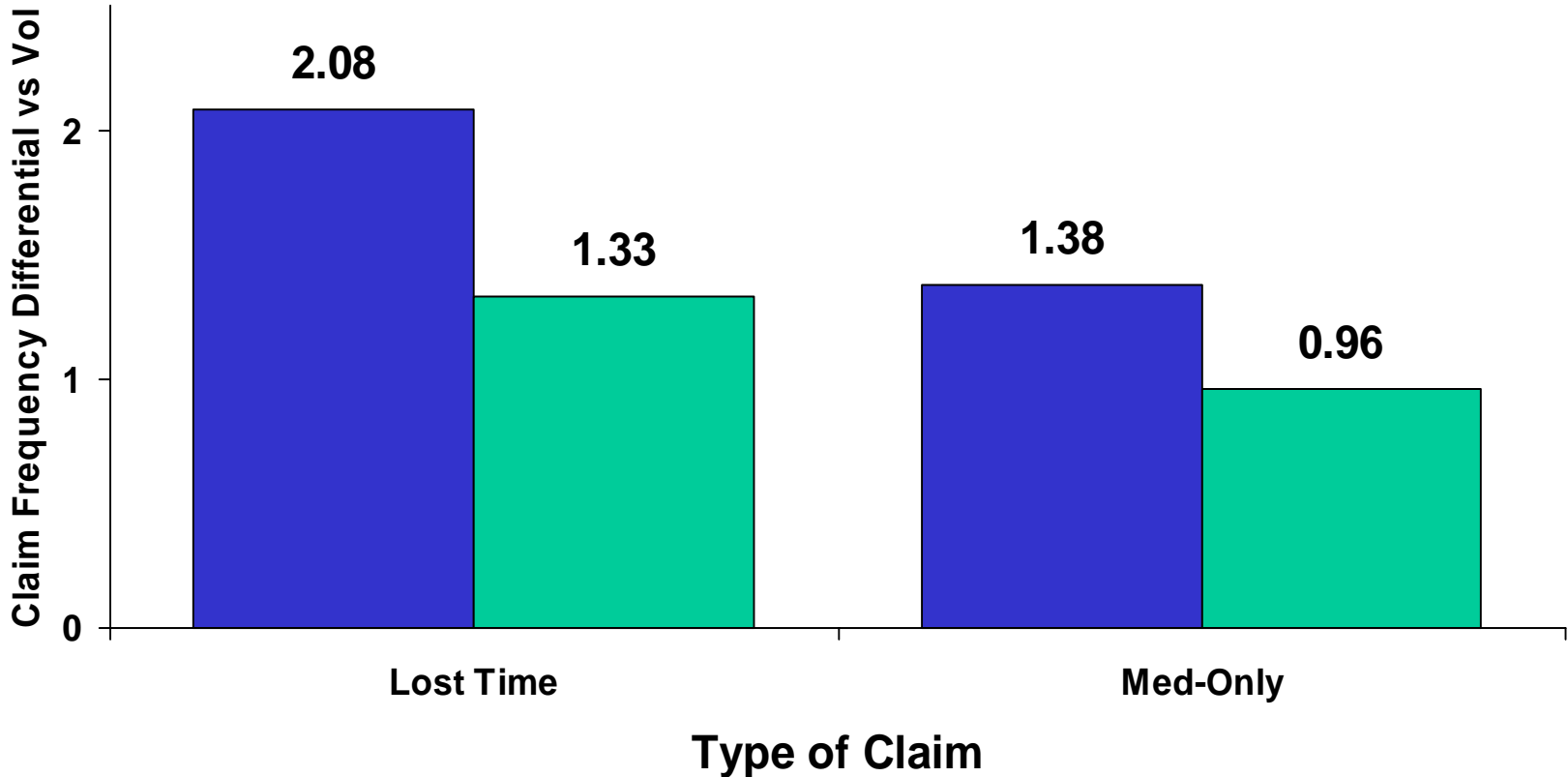


Source: Bureau of Labor Statistics



# Assigned Risk Claim Frequency Expressed Relative to Voluntary Market = 1.00

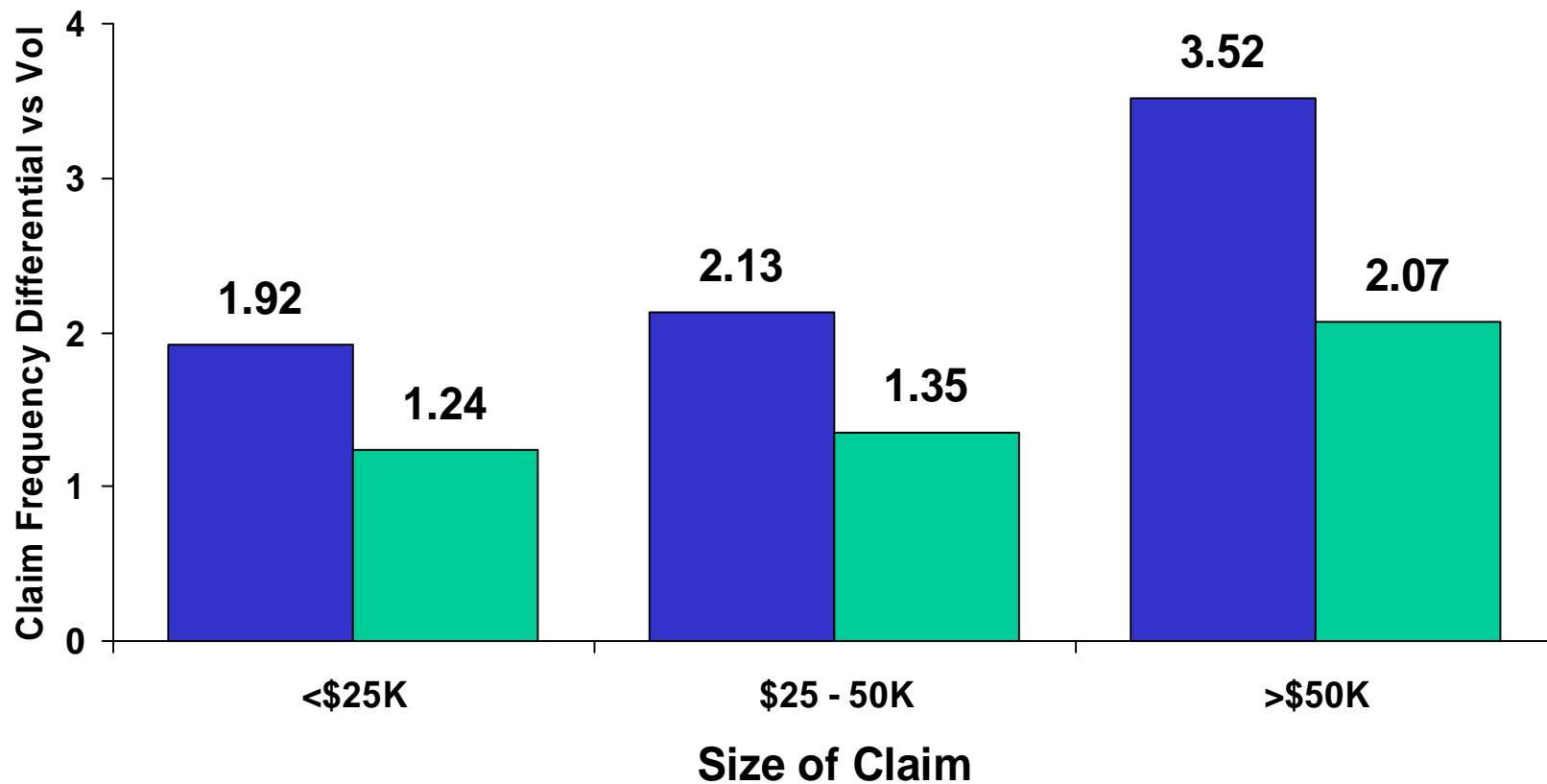
Frequency at First Report



Actual Class-Mix-Controlled

# Assigned Risk Claim Frequency Expressed Relative to Voluntary Market = 1.00

Lost-Time Frequency and Severity at First Report, Undeveloped



Actual Class-Mix-Controlled

# Claim Frequency Study Summary

- Over the last several years, the claim frequency decline appears to be just as strong for the medium and large claims as for the small lost-time claims.
- The above is corroborated by BLS data showing claim frequency by days away from work.
- Because the relative increase in larger claims (caused by the uneven frequency decline) has subsided in the past several years, there is less upward pressure on severity. This is particularly true for indemnity.

# Claim Frequency Study Summary

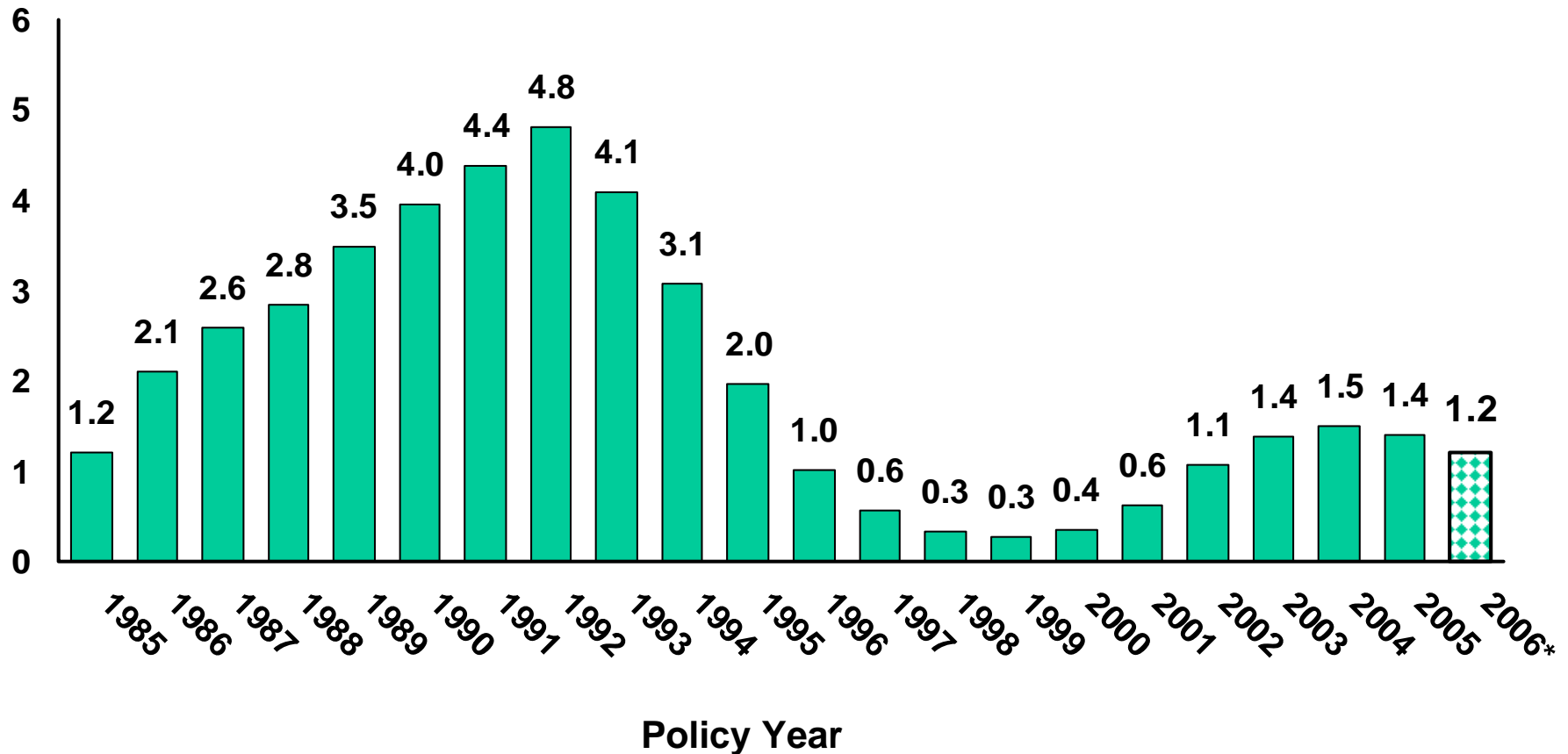
- The decline in the frequency of workers compensation claims spanned all injury types, geographic regions and almost all occupations.
- A shift in occupational mix is a minor contributor to the decline in claim frequency.
- The assigned risk market has a higher frequency of lost-time claims than the voluntary market, especially for the larger claims. This is true even after controlling for class-mix differences between the two markets.

# Workers Compensation Residual Market

# Workers Compensation Residual Market Premium Volume Declines

NCCI-Serviced Workers Compensation Residual Market Pools  
as of June 30, 2007

\$ Billions

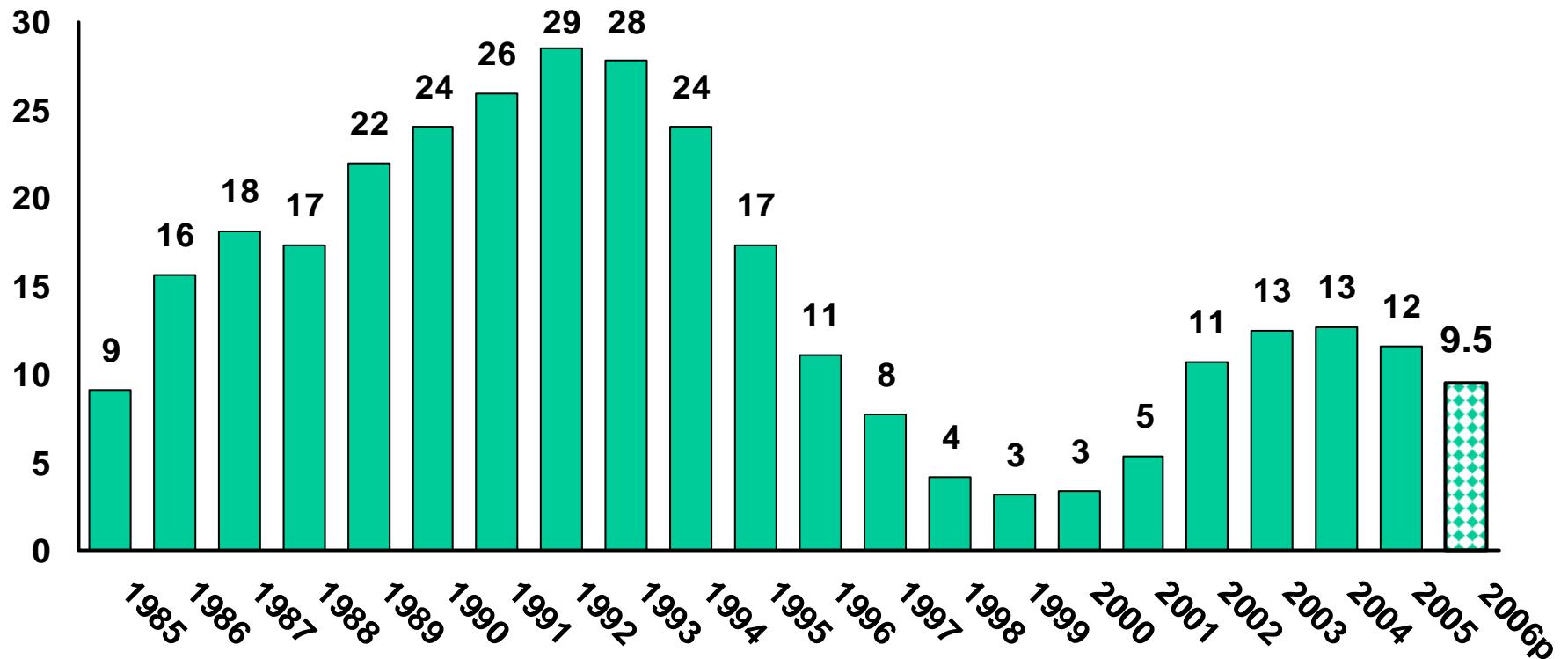


\* Incomplete Policy Year Projected to Ultimate

# Workers Compensation Residual Market Shares Continue to Decline

Workers Compensation Insurance Plan States\*  
Premium as a Percentage of Direct Written Premium

Percent



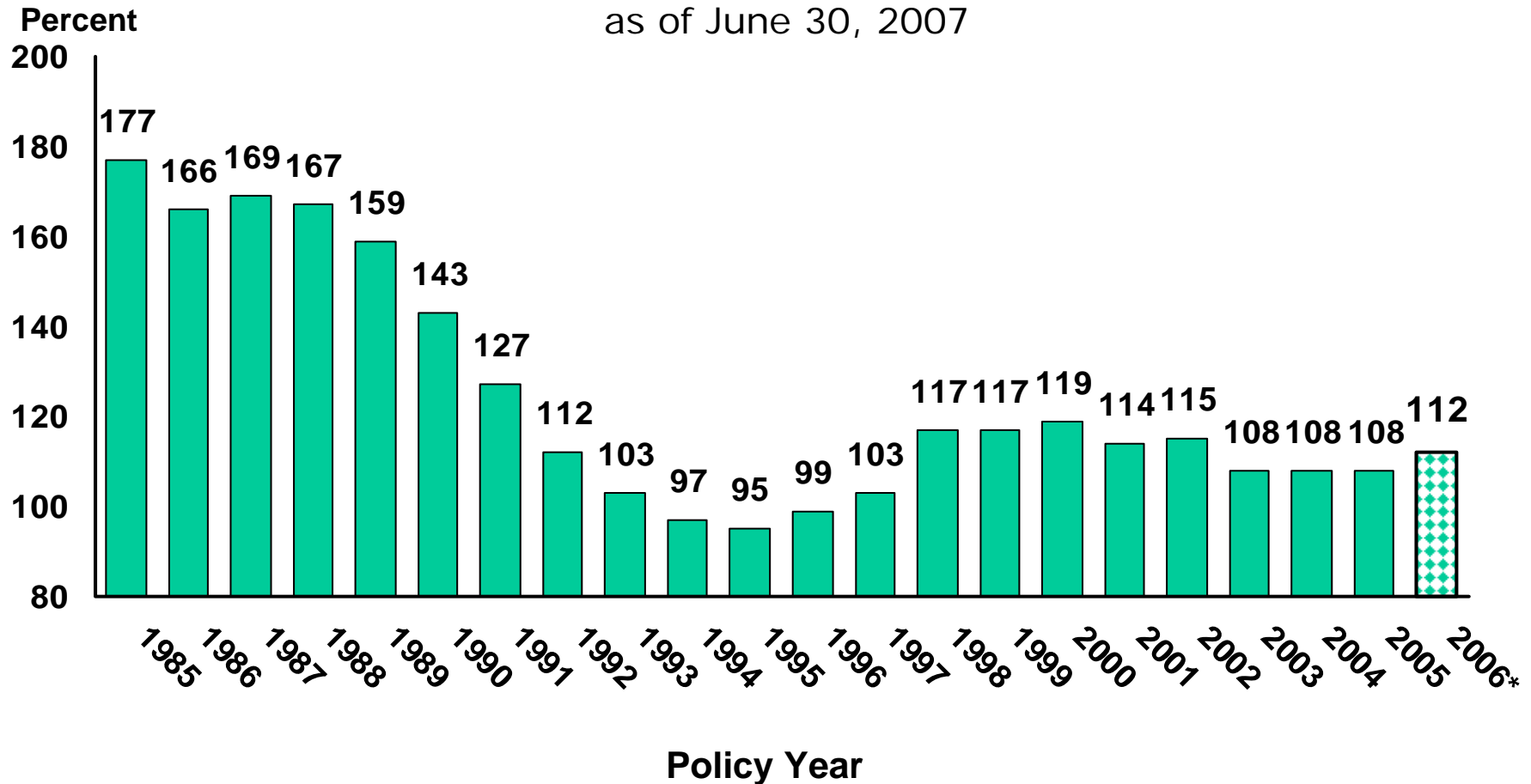
Calendar Year

p Preliminary

\* NCCI Plan states plus DE, IN, MA, MI, NJ, NC

# Workers Compensation Residual Market Combined Ratios

NCCI-Serviced Workers Compensation Residual Market Pools  
as of June 30, 2007



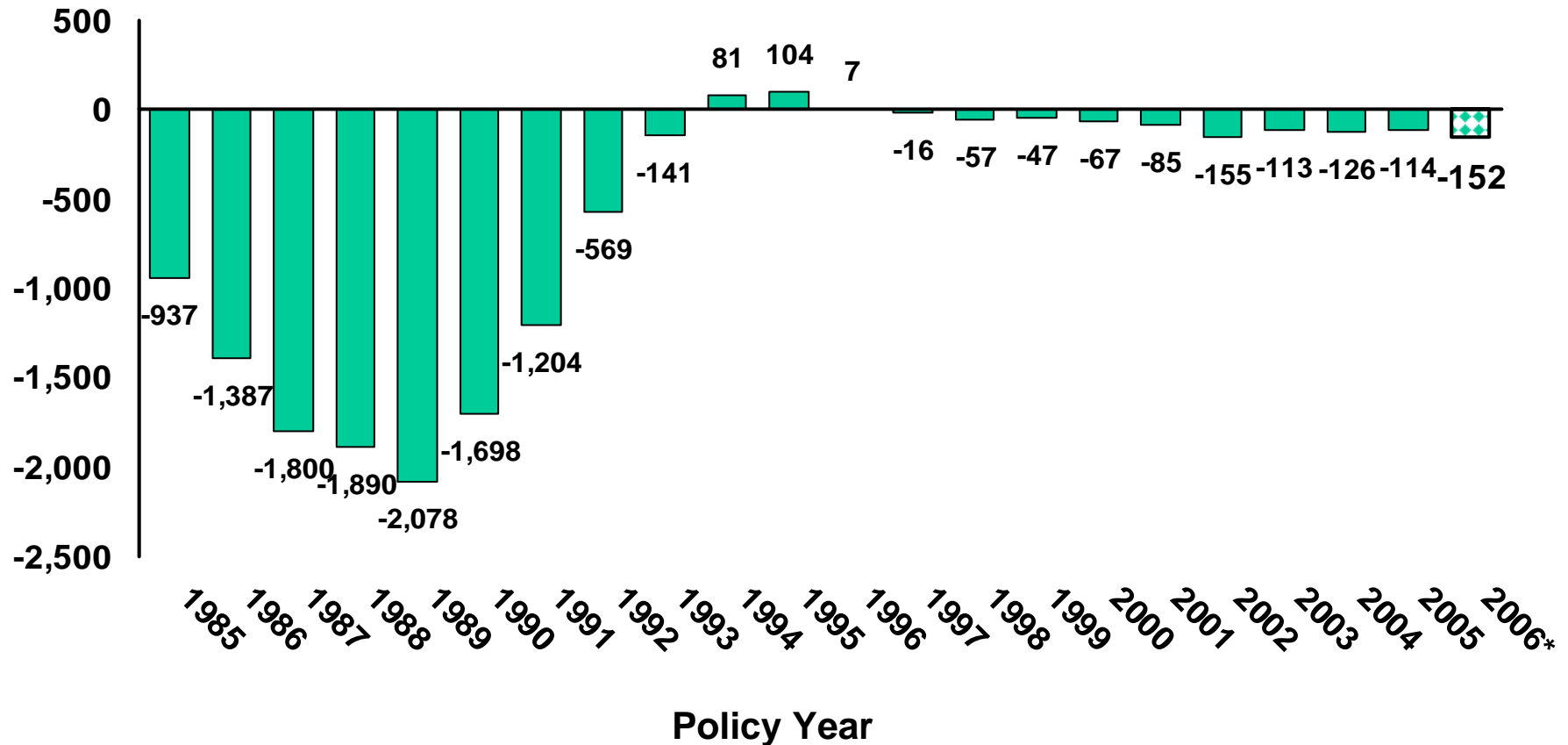
\* Incomplete Policy Year Projected to Ultimate



# Workers Compensation Residual Market Underwriting Results

NCCI-Serviced Workers Compensation Residual Market Pools  
as of June 30, 2007

\$ Millions



\* Incomplete Policy Year Projected to Ultimate

# Concluding Remarks

## Positives

- Underwriting results best in more than 30 years
- Frequency continues to decline
- Strongest reserve position in over two decades
- Residual Market depopulation continues

## Negatives

- Low investment returns continue to put pressure on underwriting results
- Medical costs still well above inflation
- Underwriting cycle

Q & A