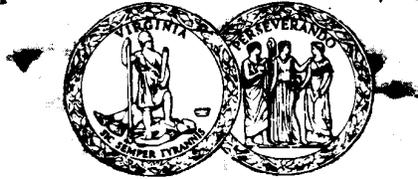


COMMONWEALTH OF VIRGINIA



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STATE CORPORATION COMMISSION BUREAU OF INSURANCE

April 16, 1991

Administrative Letter
1991-6

TO: All Insurers Licensed to Write Property and Casualty
Insurance in Virginia

RE: Workers' Compensation Insurance Rate Filings

It has become increasingly obvious to the Bureau of Insurance from comments made by insurers writing workers' compensation in the Commonwealth that there is considerable confusion and concern with respect to certain actions taken by the State Corporation Commission in the course of the last several workers' compensation rate filings.

While we understand that the National Council on Compensation Insurance (NCCI), the rate service organization which files rate requests on behalf of its member companies, does notify the members of its Virginia Classification and Rate Committee (C & R Committee) of the differences between what NCCI applied for and what the Commission granted in a rate proceeding, we are concerned that NCCI apparently does not adequately inform its member-insurers, who are not members of NCCI's C&R Committee, of the Commission's actions with respect to NCCI rate applications and the basis for such actions.

As a general matter, you should know that the State Corporation Commission is considered to be an expert rate-making body and conducts formal public hearings on NCCI's rate requests. In addition to insurance rate proceedings, the State Corporation Commission also conducts public hearings and sets rates in Virginia for electric, telephone and water public utilities. These hearings are conducted according to Virginia law and the Commission's published Rules of Practice and Procedure and are subject to the rules of evidence as used in the courts of record in the Commonwealth of Virginia. All testimony before the Commission is given under oath and is subject to cross-

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examination by counsel for participating parties. Transcripts of the hearings are available from the Commission's court reporters. Final orders of the State Corporation Commission are subject to appeal as a matter of right to the Virginia Supreme Court. Upon an appeal, the record of the proceeding, which includes, among other things, the Commission's written opinion stating the basis for its decision, its orders, the transcripts and evidentiary documents, is transmitted by the Clerk of the State Corporation Commission to the Clerk of the Virginia Supreme Court. Further proceedings before the Virginia Supreme Court are subject to the Supreme Court's Rules of Court.

In the 1990 rate filing by NCCI with the Commission, an increase of 27.7% in premium level was requested. Of this 27.7% requested increase, 15.4% was attributable to an increase in the factor for profit and contingencies. The Commission rejected this increase based on its previous rulings that dividends and deviations voluntarily paid and allowed must be excluded for the purpose of setting workers' compensation insurance rates in the Commonwealth of Virginia. Such payments and allowances, the Commission reasoned in its opinion filed in the record transmitted to the Supreme Court, should be funded out of better than expected experience and expense savings. NCCI has neither ever acceded to, nor ever perfected an appeal of right to the Virginia Supreme Court with respect to, the Commission's rulings concerning dividends and deviations.

In addition to the requested increase of 15.4% for profit and contingencies, which NCCI knew the Commission had not allowed in past rate proceedings, the balance of the NCCI 1990 premium level increase request was comprised of the following components: (i) 4.4% for experience; (ii) 4.2% for trend; (iii) 1.0% for general expense; (iv) 0.5% for loss adjustment expense; (v) 0.2% for benefits; and (vi) 0.1% for premium taxes.

At the hearings before the Commission, which lasted for three days in October, 1990, expert witnesses for the Attorney General, the Bureau of Insurance and other parties, as in past proceedings, opposed the inclusion of dividends and deviations in the rate-making process. These parties also opposed, in varying degrees, all of the remaining component increase requests with the exception of the requested increases for loss adjustment expense, benefits and taxes. These latter differences resulted principally from the use of economic and actuarial forecasting methodologies which differed from those employed by NCCI expert witnesses in the rate application before the Commission. In fact, NCCI admitted at the hearings that the methodology employed by the Bureau's expert actuarial witness with respect to the

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experience component of the requested premium level increase has also been utilized by NCCI in states other than Virginia. The Attorney General's experts recommended an overall increase of 0.4% and expert witnesses for the Bureau of Insurance recommended an overall increase in premium level of 2.0%. After considering NCCI's rate application together with all of the evidence offered in the hearings and the law applicable to the proceeding, the Commission granted an increase in premium level of 4.1% with a provision for a 14.5% rate of return on equity.

Within the period allowed by Virginia law and the Rules of the Virginia Supreme Court, NCCI filed an appeal of the Commission's decision with the Clerk of the State Corporation Commission. Subsequently, the Commission transmitted the record of the proceedings before the Commission to the Supreme Court in accordance with the Rules of that Court. The Virginia Supreme Court, among other actions, may reverse any decision of the State Corporation Commission whenever it finds that the Commission's decision is arbitrary and capricious, is not supported by the law or is contrary to the weight of the evidence contained in the record before the Commission. Nevertheless, notwithstanding NCCI's contrary position with respect to dividends and deviations in the making of workers' compensation insurance rates, shortly after the record was transmitted to the court, NCCI withdrew its appeal from the Supreme Court. Thus, NCCI's position with respect to dividends and deviations remains untested before the Virginia Supreme Court and the decision of the State Corporation Commission granting a 4.1% increase in workers' compensation insurance premium levels became final for new and renewal policies issued on and after November 1, 1990.

The Bureau of Insurance believes that insurers doing business in the Commonwealth of Virginia have every right to know and understand fully both the procedure to which rate applications are subject and the basis for the disposition of a particular rate application. The purpose of this letter has been to explain generally the manner in which the 1990 NCCI workers' compensation insurance rate application was handled before the State Corporation Commission. However, we are certain that there may be insurers who have additional and more specific questions which have not been answered in this letter. Accordingly, we invite any insurer who has any questions relating to the procedural or substantive manner in which any rate filing has been handled to contact the Bureau of Insurance in writing for an explanation. We will do our best to provide you with the answers to your questions.

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Questions regarding the contents of this letter should be directed to:

Robert A. Miller
Deputy Commissioner
Property & Casualty Division
Bureau of Insurance
P. O. Box 1157
Richmond, Virginia 23209

Yours truly,

A handwritten signature in black ink, appearing to read "Steven T. Foster", with a long horizontal line extending to the right.

Steven T. Foster
Commissioner of Insurance

STF/met