Report on Workers Compensation Rates

as required by MN Stat 79.55, Subd. 10.

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SUMMARY AND CONCLUSION

Minnesota Statute 79.55, Subdivision 10, states: "The commissioner shall issue a report by March 1 of each year, comparing the average rates charged by workers' compensation insurers in the state to the pure premium base rates filed by the association, as reviewed by the rate oversight commission." This is the third report required by that statute.

The pure premium base rates filed by the association (the MWCIA) decreased by 2.8% on January 1, 1999. Insurers' average rates decreased by 9.7% between January 1, 1998, and January 1, 1999. The Commissioner concludes that the insurance marketplace is responding adequately to reductions in loss costs.

DISCUSSION AND ANALYSIS

Measurement of the Insurer Rate Level

The Commerce Department has rate filings from every insurer doing business in Minnesota. Insurers must file an explanation of any rate change, and the vast majority of them file a multiplier which they apply to the MWCIA loss costs to produce their rates. For this report, we compared the average multiplier filed as of January 1, 1998, to the average multiplier filed as of January 1, 1999. We adjusted the average multipliers so that both were on the same level, namely the level of the 1999 MWCIA loss costs. The average multiplier on January 1, 1998, was 1.720. The average on January 1, 1999, was 1.554. That represents a decrease of 9.7%.

Companies Compared

The average multipliers calculated in this report do not use all the companies that wrote workers compensation premium during 1997 and 1998. For 1997 the calculation uses insurers that wrote 96.8% of the total market; for 1998 the calculation uses insurers that wrote 96.6% of the market. We excluded insurers whose rate calculation required additional steps beyond applying a multiplier to the MWCIA loss costs. In some cases the excluded insurers do not base their premiums on the MWCIA loss costs, but rather calculate their own loss costs, consequently they had no multiplier. In theory we could individually correct the data of the missing insurers, and refine the estimated multipliers. These few insurers' results could not materially change the estimates. We have percentage changes for the excluded insurers; the average is a decrease of 11.3%, which does not change the other estimates in this report by even one-tenth of a percentage point.

Shifts in Market Share

The insurance marketplace is constantly changing in Minnesota. New employers and insurers come into the market; old insurers and employers leave the market; existing employers change insurers. Even if no insurer ever changed its rates, this continuing flux would have a big effect on the average premiums that employers pay. Consider the extreme example where one insurer writes the entire market at a rate of $2 in 1998, and a different insurer writes the entire market at a rate of $1 in 1999. Premiums would drop by 50% even if neither company changed its rates. For this report we took this flux into account in order to accurately measure how the market is responding to changing underlying loss costs. We used 1996 market shares for averaging the old rates and 1997 market shares for averaging the new rates. The market shares for 1997 and 1998 would have been better, but 1998 premiums are not available until after March 1, 1999. Using a one year lag introduces a possible error, but it is much better than ignoring the shifts in market share, which would introduce an even larger error. The error caused by the lag becomes immaterial over time, but the error caused by ignoring the shifts would compound over time and could become truly enormous.

Timing

Insurers do not all change their rates at the same time. Furthermore, a particular insurer does not necessarily change rates at the same time every year. As a result, one can never measure an annual change in multipliers with total precision. One needs to look at an analysis such as this one over a period of years before reaching a firm conclusion. Insurers are currently in the midst of filings, most of which are rate reductions. At the end of another month or two, the average multiplier of 1.554 will probably have decreased further.

Schedule Rating

The multipliers estimated in this report do not present the entire rate picture. Insurers also give "schedule" credits or debits based on an insurer's individual risk characteristics. For the majority of insurers, that can mean adjustments to rates of up to ±40%. We do not now have a good way to measure the overall effect of schedule credits and debits. In the long run their use can not materially affect the cumulative changes in rates, but changes in their use can have a large impact in a shorter time span. Companies are giving more credits now than a few years ago, but we are seeing less requests for new credits now than we saw prior to 1998. The use of credits has probably leveled off, in which case they are probably not distorting the current analysis to any significant extent.

Other Credits

Schedule credits are not the only possible rate modifications. Some insurers, for example, give rate reductions to employers that participate in managed care programs. Most such programs are still relatively new, and their increased use may contribute to rates that are lower than otherwise indicated by this analysis. Insurers also give experience rating modifications to many insureds, and at a time when experience is improving, the balance of such modifications becomes more favorable to insureds than in the past. The same thing applies to policyholder dividends.

Assigned Risk Plan

Changes in the Assigned Risk Plan market share can have the same result as shifts in other companies' market shares. The Assigned Risk Plan is currently losing market share, which generally means that its former customers have found coverage at lower rates in the voluntary market. We did not measure the effect of that price reduction in this report. Even if the 1997 and 1998 multipliers were exactly equal, the movement from the Assigned Risk Plan would mean that the overall average rate for employers decreased. The Assigned Risk Plan has gotten small enough now that its depopulation is probably not distorting the current analysis, but one should be aware that movement in or out of the Plan has an effect on the average premium that employers pay for workers' compensation coverage.