Workers' Compensation Practice Group
SPOTLIGHT on Workers' Comp

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# NCCI Describes State of Workers' Compensation as 'Balanced.'

## What are the positive developments and challenges for the line?

The National Council of Compensation Insurance (NCCI) operating on a not-for-profit basis provides data and a variety of other services to more than 900 insurance companies and nearly 40 state governments.

NCCI held its Annual Issues Symposium (AIS) in Orlando, Fla., May 8 - 9, 2014. In opening remarks, NCCI President and CEO Steve Klingel described the current state of the workers' compensation marketplace as "balanced." Mr. Klingel's observed that "today, industry costs are largely contained, at present there is a reasonable expectation for some level of profit, claims frequency continues to decline, and the system in most states is operating effectively and efficiently." Click here to view the opening AIS 2014 presentation. To watch the presentation, click here.

The 2014 State of the Line report was presented by new NCCI chief actuary, Kathy Antonello. She said, "Overall, the workers compensation line showed a number of positive results in 2013." Click here to view the complete State of the Line presentation. Click here to watch a video of the presentation.

**Positive Developments in 2013**

According to NCCI, the workers' compensation calendar year combined ratio for private carriers decreased to 101 for the first time since 2007. The accident year results also showed notable improvement in 2013, falling eight points to a combined ratio of 99.

The combined ratio measures underwriting profit. This ratio is calculated by dividing the sum of incurred losses and expenses by earned premium. For example, a combined ratio of 101 percent means that an insurer is underwriting at a loss because for every $1 in premiums received, $1.01 in claims and expenses are paid. However, even if the combined ratio is above 100 percent, a company can still potentially make a profit from income received from investments.

NCCI reported that investment income remained surprisingly robust in 2013. Based on carrier annual statement data, the ratio of investment gains on insurance transactions to net earned premium was 15 percent. This investment gain outcome, combined with the underwriting results, produced a workers' compensation pre-tax operating gain of 14 percent for 2013, which represents a significant increase over 2012, and the industry's first double-digit return since 2007.

The report contained additional causes for optimism:

- Net written premiums increased for the third consecutive year. Net written premiums countrywide increased 5.4 percent to $37 billion in 2013 for private carriers and state funds. This increase was primarily driven by a growth in wages and payroll and carrier discounting
- Lost-time claim frequency maintained a path of decline in 2013, down 2 percent, on average, in NCCI states. Using statistical plan data, NCCI indicates that since the end of the recession most of the decline in frequency occurred due to a decrease in the number of large claims defined as $50,001 or greater.
- The average indemnity cost per lost-time claim in 2013 was $22,700. The indemnity claim severity increase was only 2 percent, which equaled the U.S. average weekly wage increase in 2013 as reported by Moody's Economy.com.
- In 2013, the average medical cost per lost-time claim increased a modest 3 percent to $28,800. This change was just 1 percent greater than the 2013 U.S. Bureau of Labor Statistics (BLS) medical consumer price index (CPI). These results are evidence that the industry's investment in cost containment has been effective.

**Challenges to the Workers' Compensation Line**

Even with the improvements, workers' compensation is faced with some ongoing challenges:

- Current investment returns are likely not sustainable if the historic low-interest-rate environment continues.
- The continued slow growth in employment, particularly in the manufacturing and construction industries, is impeding additional premium growth. Manufacturing and construction remain below pre-recession levels, and these jobs generate approximately 35 percent of workers' compensation premium.
- Physician dispensing, opioid abuse and the potential impact of the Patient Protection and Affordable Care Act (PPACA) may adversely impact medical severity.
- Uncertainty regarding the extension of the Terrorism Risk Insurance Act (TRIA) is a major concern for the workers' compensation line.

**Impact of TRIA Expiration on Workers' Compensation**

In 2002, Congress enacted TRIA following the terrorist attacks of September 11, 2001, in response to terrorism insurance becoming unavailable or, when offered, extremely costly. Extended first in 2005 and again in 2007, TRIA is set to expire December 31, 2014. *TRIA Renewal: Why Risk Managers Care* by Chris Mandel, Sedgwick senior vice president, strategic solutions, explains the history of the act and its importance.

Often, discussions regarding TRIA are primarily focused on commercial real estate property insurance; however, TRIA impacts other lines of insurance including workers' compensation. On May 7, 2014, the Rand Corporation announced the release of a new study, "The Impact of Eliminating the Terrorism Risk Insurance Act on Workers' Compensation Insurance Markets."

The study notes that losses in workers' compensation could be "more than $10 billion from a large conventional attack (10-ton truck bomb) and more than $300 billion from a nuclear attack." The study notes that the workers' compensation losses caused by the 9/11 attacks were "approximately $2.6 billion (in 2013 dollars)."

This study points out that because workers' compensation coverage is mandatory for most employers and defined by each state's statute, strategies available for other lines of insurance such as changing the insurance contract; imposing policy limits; excluding coverage of terrorism; or excluding losses from nuclear, biological, chemical or radiological (NBCR) attacks are generally not an option.

According to this report, some of the possible effects of TRIA expiration on workers' compensation absent a dramatic increase in the provision of affordable reinsurance include:

- A reduction in the amount of workers' compensation capacity provided by the insurance industry, thus making it harder for businesses to obtain coverage. It is anticipated that this impact would likely be most pronounced for large employers, landmark buildings, and businesses in dense urban areas.
- Redistribution of risk such that the burden of catastrophic losses is confined within the state that is attacked to a greater extent, whereas TRIA currently spreads those losses across the country. This result would add to the challenge of rebuilding in the affected state.
- High-risk businesses paying more for their workers' compensation coverage may pass some of the cost to workers in the form of reduced wages and/or benefits, thereby reducing labor income and economic growth.

On April 10, 2014, a bi-partisan bill was introduced to reauthorize TRIA for seven more years. Senate Bill 2244 is currently pending before the Senate Committee on Banking, Housing, and Urban Affairs. The Senate Banking Committee is scheduled to vote June 3 on legislation to renew the Terrorism Risk Insurance Act. In the House, the Terrorism Risk Insurance Program Reauthorization Act of 2013, House Bill 2146, was introduced May 23, 2013 and referred to the House Finance Committee.

Urging prompt congressional action on TRIA renewal to protect employers, their injured employees, insurers, and our economy may be a way to make a difference in 2014.