

COMMONWEALTH OF VIRGINIA



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STATE CORPORATION COMMISSION BUREAU OF INSURANCE

May 2, 1990

Administrative Letter
1990-5

TO: ALL PROPERTY AND CASUALTY INSURERS AND RATE SERVICE ORGANIZATIONS LICENSED IN VIRGINIA

RE: PROSPECTIVE LOSS COSTS FILING PROCEDURES

The General Assembly of Virginia during the 1990 Session enacted and amended certain statutes regarding the rates and supplementary rating information filing requirements of rate service organizations. The effective date of these new or revised statutes is July 1, 1990.

Prospective Loss Costs Filing Procedures

This Administrative Letter specifies the framework under which rate service organizations and any member, subscriber or service purchaser of a rate service organization will operate in a loss costs system. Under this system, rate service organizations will no longer develop or file final rates, but instead will develop and file prospective loss costs and supporting actuarial and statistical data. Each insurer must individually determine and file the rates it will use as a result of its own independent company decision-making process. Rate service organizations will continue to develop and file rules and supplementary rating information on behalf of their members, subscribers and service purchasers.

Nothing in these procedures shall be construed to require rate service organizations or their members, subscribers and service purchasers to immediately refile rates previously implemented. Members, subscribers and service purchasers of a rate service organization are authorized to continue to use all rates and deviations filed for their use until such time as the insurer makes its own filing to change its rates, either by making an independent filing or by filing a Reference Filing Adoption Form (VA RFA-1 (7/90) copy attached) adopting the rate service organization's prospective loss costs, or modification thereof.

DEFINITIONS

For the purpose of loss costs filing procedures:

- A) "Advisory organization" means rate service organization.
- B) "Commission" means the Virginia State Corporation Commission.
- C) "Developed losses" means losses (including loss adjustment expenses) adjusted, using standard actuarial techniques, to eliminate the effect of differences between current payments or reserve estimates and those needed to provide actual ultimate loss (including loss adjustment expense) payments.
- D) "Effective date" shall mean the policy effective date that rates and supplementary rate information will be implemented.
- E) "Expenses" means that portion of a rate attributable to acquisition, field supervision, collection expenses, general expenses, taxes, licenses and fees.
- F) "Loss trending" means any procedure for projecting developed losses to the average date of loss for the period during which the policies are to be effective.
- G) "Minimum premium rule" means any formula or methodology used to calculate minimum premium for a given policy but does not include any manual rules that allow for the use of minimum premiums.
- H) "Prospective loss costs" are that portion of a rate that does not include provisions for expenses (other than loss adjustment expenses) or profit, and are based on historical aggregate losses and loss adjustment expenses adjusted through development to their ultimate value and projected through trending to a future point in time.
- I) "Rate" means the cost of insurance per exposure unit, whether expressed as a single number or as a prospective loss cost with an adjustment to account for the treatment of expenses, profit and variations in loss experience, prior to any application of individual risk variations based on loss or expense considerations, and does not include minimum premiums.
- J) "Supplementary rating information" includes any manual or plan of rates, classification, rating schedule, minimum premium or minimum premium rule, policy fee, rating rule, rate-related underwriting rule, experience rating plan, statistical plan and any other similar information needed to determine the applicable rate in effect or to be in effect.

SECTION I: RATES/LOSS COSTS

A) Rate Service Organization Action

- Rate service organizations will no longer develop or file final rates that contain provisions for expenses (other than loss adjustment expenses), and profit and contingencies. Instead, for all lines, rate service organizations will develop and file with the State Corporation Commission in accordance with Section 38.2-1906 of Title 38.2 of the Code of Virginia, a Reference Filing containing prospective loss costs and supporting actuarial and statistical data.
- The rate service organization may print and distribute manuals of prospective loss costs as well as rules and other supplementary rating information described in Section II A.
- With the initial prospective loss costs Reference Filing, rate service organizations will no longer develop or file any minimum premiums or minimum premium rules.

B) Insurer Action

- If an insurer that is a member, subscriber or service purchaser of a rate service organization decides to use the prospective loss costs in a Reference Filing in support of its own filing, the insurer should make a filing using VA RFA-1 (7/90). The insurer's rates are the combination of the prospective loss costs and the loss cost adjustments contained in the VA RFA-1 (7/90).
- Insurers may file modifications of the prospective loss costs in a Reference Filing based on their own anticipated experience. Supporting documentation will be required for any modifications (upwards or downwards) of the prospective loss costs in the Reference Filing.
- Insurers may vary expense loads by individual classification, grouping, or subline of insurance. Insurers may use variable or fixed expense loads or a combination of these to establish their expense loadings.
- If an insurer wishes to use minimum premiums, it must file the minimum premiums and minimum premium rules it proposes to use.

- The insurer may request to have its loss costs adjustments remain on file and reference all subsequent prospective loss costs Reference Filings. Upon receipt of subsequent rate service organization loss costs Reference Filings, the insurer's rates will be the combination of the prospective loss costs and the loss cost adjustments contained in the VA RFA-1 (7/90) on file with the Commission, and will be applicable to new and renewal policies effective on or after the effective date of the prospective loss costs. The insurer need not file anything further.
- If an insurer that has filed to have its loss cost adjustments remain on file intends to delay, modify, or not adopt a particular rate service organization loss costs Reference Filing, the insurer must make an appropriate filing.
- The insurer's filed loss cost adjustments will remain in effect until the insurer withdraws them or files a revised VA RFA-1 (7/90).
- Insurers shall provide such other information as may be required by the Commission.
- To the extent that an insurer's final rates are determined solely by applying its loss cost adjustments, as proposed in the VA RFA-1 (7/90), to the prospective loss costs contained in a rate service organization's Reference Filing and printed in the rate service organization's rating manual, the insurer need not develop or file its final rate pages. If an insurer chooses to print and distribute final rate pages for its own use, based solely upon the application of its filed loss costs, the insurer need not file those pages with the Commission. If the rate service organization does not print the loss costs in its manual, the insurer must submit its rate pages.

For future Reference Filings filed by the rate service organization:

- If the insurer HAS filed to have its loss cost adjustments remain on file, applicable to subsequent Reference Filings, and a new Reference Filing is filed and

If....

Then....

- | | |
|---|--|
| 1. the insurer decides to use the revision of the prospective loss costs and effective date as filed... | 1. the insurer does NOT file anything with the Commission. Rates are the combination of the prospective loss costs and the on-file loss cost adjustments and become effective on the effective date of the loss costs. |
| 2. the insurer decides to use the prospective loss costs as filed BUT with a subsequent effective date... | 2. the insurer must file page one of VA RFA-1 (7/90) with the Commission before the effective date of the loss costs. |
| 3. the insurer decides to use the revision of the prospective loss costs, but wishes to change its loss cost adjustments... | 3. the insurer must file a revised VA RFA-1 (7/90) before the effective date of the loss costs. |
| 4. the insurer decides NOT to revise its rates using the prospective loss costs... | 4. the insurer must file page one of VA RFA-1 (7/90) with the Commission before the effective date of the loss costs. Page one of VA RFA-1 (7/90) should include in item 5 the loss cost reference filing number which immediately preceded the loss costs the insurer is not adopting and the second block of item 10 should be checked. Items 6 - 9 on page one need not be completed. |

- If an insurer has NOT elected to have its loss cost adjustments remain on file, applicable to future prospective loss costs reference filings, and a new Reference Filing is filed and

If...

Then...

1. the insurer decides to use the prospective loss costs to revise its rates...
2. the insurer decides NOT to use the revisions...

1. the insurer must file VA RFA-1 (7/90).
2. the insurer does not file anything.

SECTION II: SUPPLEMENTARY RATING INFORMATION

A) Advisory Organization Action

- Filings of rules and supplementary rating information are made by the rate service organization with the Commission on behalf of those insurers that have authorized the rate service organization to file rules, relativities and supplementary rate service information on their behalf. This includes policy-writing rules, rating plans, classification codes and descriptions, territory codes and descriptions and rules which include factors such as increased limits factors or similar factors but excludes minimum premiums and minimum premium rules.
- Rate service organizations may print and distribute manuals of rules and supplementary rating information excluding minimum premiums and minimum premium rules.

B) Insurer Action

- If an insurer has authorized a rate service organization to file on its behalf, and a new filing of rules and supplementary rating information is filed and

If...

Then...

1. the insurer decides to use the revisions and effective date as filed...
2. the insurer decides to use the revisions as filed BUT with a subsequent effective date...

1. the insurer does NOT file anything.
2. the insurer must file with the Commission its effective date before the rate service organization's effective date.

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|---|--|
| 3. the insurer decides not to use the revision... | 3. the insurer must advise the Commission in writing before the rate service organization's effective date. |
| 4. the insurer decides to use the revision with modifications on or after the effective date as filed ... | 4. the insurer must file the modifications with the Commission, specifying the basis for the modifications, and the insurer's effective date, if different from the effective date filed by the rate service organization. |

If you have any questions regarding the content of this letter, please call the:

Property and Casualty Division
Rates and Forms Section
(804) 786-3665

In addition, the attached VA RFA-1 (7/90) should be reproduced for your future use.

Sincerely,



Steven T. Foster
Commissioner of Insurance

STF:krm
Attachments

Space Reserved for Bureau of Insurance Use

Date: _____

INSURER RATE FILING
ADOPTION OF ADVISORY ORGANIZATION
PROSPECTIVE LOSS COSTS
REFERENCE FILING ADOPTION FORM

1. INSURER NAME _____
ADDRESS _____

PERSON RESPONSIBLE FOR FILING _____
TITLE _____

2. INSURER NAIC # _____ TELEPHONE # _____

3. LINE OF INSURANCE _____

4. ADVISORY ORGANIZATION _____

5. ADVISORY ORGANIZATION REFERENCE FILING # _____

6. The above insurer hereby declares that it is a member, subscriber or service purchaser of the named advisory organization for this line of insurance. The insurer hereby files to be deemed to have independently submitted as its own filing the prospective loss costs in the captioned Reference Filing.

The insurer's rates will be the combination of the prospective loss costs and the loss costs multipliers and, if utilized, the expense constants specified in the attachments.

7. PROPOSED RATE LEVEL CHANGE _____% EFFECTIVE DATE _____

8. PRIOR RATE LEVEL CHANGE _____% EFFECTIVE DATE _____

9. ATTACH "SUMMARY OF SUPPORTING INFORMATION FORM"
(Use a separate Summary for each insurer-selected loss costs multiplier.)

10. CHECK ONE OF THE FOLLOWING:

The insurer hereby files to have its loss costs multipliers and, if utilized, expense constants be applicable to future revisions of the advisory organization's prospective loss costs for this line of insurance. The insurer's rates will be the combination of the advisory organization's prospective loss costs and the insurer's loss costs multipliers and, if utilized, expense constants specified in the attachments. The rates will apply to policies written on or after the effective date of the advisory organization's prospective loss costs. This authorization is effective until disapproved by the Commissioner, or amended or withdrawn by the insurer.

The insurer hereby files to have its loss costs multipliers and, if utilized, expense constants be applicable only to the above Advisory Organization Reference Filing.

Insurer Name _____

NAIC Number _____

Date _____

INSURER RATE FILING
ADOPTION OF ADVISORY ORGANIZATION PROSPECTIVE LOSS COSTS
SUMMARY OF SUPPORTING INFORMATION FORM
CALCULATION OF COMPANY LOSS COSTS MULTIPLIER

1. Line, Subline, Coverage, Territory, Class, etc. combination to which this page applies: _____

2. Loss Costs Modification:
A. The insurer hereby files to adopt the prospective loss costs in the captioned reference filing:

(CHECK ONE)

Without modification. (factor = 1.000)

With the following modification(s). (Cite the nature and percent modification, and attach supporting data and/or rationale for the modification.)

B. Loss Costs Modification Expressed as a Factor: _____
(See examples below.)

NOTE: IF EXPENSE CONSTANTS ARE UTILIZED, ATTACH "EXPENSE CONSTANT SUPPLEMENT" OR OTHER SUPPORTING INFORMATION. DO NOT COMPLETE ITEMS 3 - 7 BELOW.

3. Development of Expected Loss Ratio. (Attach exhibit detailing insurer expense data and/or other supporting information.)

	Selected Provisions
A. Total Production Expense	_____ %
B. General Expense	_____ %
C. Taxes, Licenses & Fees	_____ %
D. Underwriting Profit & Contingencies	_____ %
E. Other (explain)	_____ %
F. TOTAL	_____ %

4A. Expected Loss Ratio: ELR=100% - 3F = _____ %

4B. ELR in decimal form = _____

5. Company Formula Loss Costs Multiplier: (2B / 4B) = _____

6. Company Selected Loss Costs Multiplier = _____
Explain any differences between 5 and 6:

7. Rate level change for the coverages to which this page applies _____ %

Example 1: Loss costs modification factor: If your company's loss costs modification is -10%, a factor of .90 (1.000 - .100) should be used.

Example 2: Loss costs modification factor: If your company's loss costs modification is +15%, a factor of 1.15 (1.000 + .150) should be used.

Insurer Name _____

NAIC Number _____

Date _____

EXPENSE CONSTANT SUPPLEMENT

CALCULATION OF COMPANY LOSS COSTS MULTIPLIER WITH EXPENSE CONSTANTS

3. Development of Expected Loss Ratio. (Attach exhibit detailing insurer expense data and/or other supporting information.)

	Selected Provisions		
	Overall	Variable	Fixed
A. Total Production Expense	_____	_____	_____
B. General Expense	_____	_____	_____
C. Taxes, Licenses & Fees	_____	_____	_____
D. Underwriting Profit & Contingencies	_____	_____	_____
E. Other (explain)	_____	_____	_____
F. TOTAL	_____	_____	_____

4. A. Expected Loss Ratio: ELR=100% - Overall 3F = _____

B. ELR expressed in decimal form = _____

C. Variable Expected Loss Ratio VELR=100% - Variable 3F = _____

D. VELR in decimal form = _____

5. Formula Expense Constant:
[(1.00 / 4B) - (1.00 / 4D)] x Average Underlying Loss Costs = _____

Formula Variable Loss Costs Multiplier: (2B / 4D) = _____

6. Selected Expense Constant = _____

Selected Variable Loss Costs Multiplier = _____

7. Explain any differences between 5 and 6:

8. Rate level change for the coverages to which this page applies _____%

REFERENCE FILING ADOPTION
VIRGINIA SUPPLEMENT

- . In item 10. on page 1 the phrase "policies written" is replaced with "policies effective". Please refer to Administrative Letter 1990-3, dated January 26, 1990. In addition, the word "Commissioner" is replaced with "Commission".
- . In item 5 on page 3, "average underlying loss costs" means the insurer's statewide per policy (or coverage) loss cost, averaged across all policy limits, deductibles, territories, classifications, etc. One simple method of determining your statewide underlying loss costs per policy would entail first calculating your average premium per policy for a prior period. Then multiply the average premium by your expected overall loss ratio (e.g., line 4.A.) to get an average underlying loss cost for that prior period. Finally, apply a trend factor to place the average loss cost at the level anticipated for the prospective period for which the rates will be used. Other methods for determining statewide underlying loss costs per policy are left to individual company discretion.
- . Insurers should review Administrative Letters 1987-11 and 1989-10 for certification and data requirements. The certification forms contained in these letters shall not be utilized by rate service organizations.
- . Administrative Letter 1988-17 should be reviewed as respects delayed effect of rate filings.
- . Rates are "file and use" for Chapter 19, except those lines and subclassifications designated by the Commission to be subject to §38.2-1912 of the Code of Virginia.
- . Filings must be filed separately by line of insurance, and by program.
- . A CP-12 (4-83) is required for any homeowner's rule and rate filing affecting premium levels.
- . A CP-19 (7-89) is required for rate filings affecting premiums for special package auto policies.
- . A CP-20 (7-89) is required for rate filings affecting premiums for family auto policies.

This check list is not all inclusive. You need to review current Administrative Orders and Letters for additional requirements.

DEFINITIONS

The following are commonly accepted definitions for use with this form.

- A. **"Total Production Expense"**: Commission and brokerage and other expenses associated with production, sales, field supervision, advertising and collection.
- B. **"General Expense"**: Payroll, rent, board and bureau fees, pensions and employee benefits.
- C. **"Taxes, Licenses and Fees"**: Premium taxes, fire programs fund assessment, maintenance assessment of the Bureau of Insurance, payroll taxes, and guaranty fund assessments, etc.
- D. **"Underwriting Profit and Contingencies"**: Investment income, riskiness, cost of capital, surplus, competitive considerations.
- E. **"Other"**: for expenses not included above.