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STATE CORPORATION COMMISSION
BUREAU OF INSURANCE

June 3, 1991

**ADMINISTRATIVE LETTER
1991 - 10**

TO: **ALL INSURERS LICENSED TO WRITE WORKERS COMPENSATION INSURANCE**

RE: **VIRGINIA WORKERS COMPENSATION PROFITABILITY**

In April, 1991, William Hager, President of the National Council on Compensation Insurance (NCCI), issued a State of the Line Report detailing NCCI's view of the financial condition of workers compensation insurance on a countrywide basis. It is NCCI's opinion that the workers compensation line of business must be viewed as financially unsound and that this line will be in a negative surplus condition by 1992.

According to NCCI, the 1990 combined ratio is 118.2% on a countrywide basis. NCCI also advised that investment income on premiums and surplus has not been sufficient to offset underwriting losses and that surplus erosion is real. NCCI asserts that this situation has been created because the premium increases filed by NCCI have been granted at about 50% of the requested amount on a countrywide basis.

The purpose of this letter is to advise you that the Bureau of Insurance has further examined the premium level in Virginia using the NCCI methodologies and assumptions inherent in the countrywide analysis offered by NCCI's Mr. Hager. **As further explained below, our analysis shows that rates in Virginia will not force insurance companies into negative surplus situations by 1992, even with insurers continuing to give away profits in the form of dividends and deviations.** In fact, without dividends and deviations, insurer surplus has increased at an average annual rate of 22% for the years 1984-1990.

The Virginia operating results (including consideration of investment income on loss reserves and surplus) shown below compare profitability based on direct net earned premium with and without the inclusion of dividends and deviations.

	Column 1	Column 2
	*Virginia Only Operating Ratio as % of Premium **including** dividends and deviations actually granted to policyholders*	*Virginia Only Operating Ratio as % of Premium **excluding** dividends and deviations*
1984	105.8	87.6
1985	98.0	82.4
1986	98.9	86.1
1987	97.0	85.5
1988	97.9	85.8
1989	101.7	90.1
1990	103.4	91.7

As you can see, the figures in Column 1 are the direct result of insurers' insistence upon paying dividends and granting downward deviations, and not the result of inadequate rates.

Any deterioration of surplus attributable to Virginia is the direct result of dividend and deviation allowances. In fact, by excluding dividends and deviations, hindsight indicates that the rate of return on surplus for the period 1984-1990 has been more than adequate. There is a provision for a 14.5% rate of return underlying the current rate level.

The answer to NCCI's repetitive complaints that the State Corporation Commission does not include dividends and deviations in the premium level is for NCCI, if it so chooses, to approach the Virginia General Assembly and convince that body that dividends and deviations shall be included in the rate-making process and, therefore, that the law should be changed to accommodate that end. Without such a change, the Commission must continue as it has done and disallow dividends and deviations as a consideration in the rate-making process.

It is unassailable that overall the rates granted by the Commission during the period 1984-1990 have been more than adequate for insurers to pay claims, cover expenses and earn <u>at least</u> a reasonable rate of return, provided that insurers do not elect voluntarily, and recklessly in many instances, in the name of competition, real or perceived, to give away their profits in dividends and deviations.

We cannot address rate adequacy issues in other states, but we strongly object and disagree with the NCCI's insistence that there has been long-term rate inadequacy in Virginia. We are willing to discuss any legitimate concerns of NCCI, its member companies and their agents; however, scare tactics and misinformation have no place in this process.

For further information, copies of a paper outlining and discussing the various components underlying the current rate level are available from the Property and Casualty Consumer Services Section of the Bureau by calling 804-786-5185 or toll free in Virginia 1-800-552-7945.

Sincerely,

Steven T. Foster
Commissioner of Insurance

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