

Economic Affairs Interim Committee

SJR 27 Subcommittee Meeting

OFFICE OF MONTANA STATE AUDITOR,
COMMISSIONER OF SECURITIES AND INSURANCE

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Role of the Commissioner of Securities and Insurance in Worker's Compensation

The following presentation will provide an overall summary:

- The Role of the Commissioner of Securities and Insurance (CSI) in Regulation of Workers' Compensation
- How Regulation Protects the Insurance Consumer

Workers' Compensation Insurance

Montana employers and businesses are required to buy workers' compensation insurance

It is a reasonable expectation when purchasing a policy - that the insurer will be financially able to pay claims as they come due

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Role of CSI in Workers' Compensation

CSI's Role:

- Protect Insurance Consumers

This responsibility includes:

- Review of Premium Rates
- Review of Insurer Reserves
- Review of Insurer Surplus
- Taking preventive and corrective action to reduce insurer insolvencies

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Rates

NCCI annually files “loss costs” for private insurers and state fund

“Loss costs” = benefits and claim related expenses

Once the “loss costs” are approved by CSI - insurers file their Rates

Rates = “loss costs” + insurer expenses + may include reasonable profit, contingencies, contribution to surplus

CSI Role- Rates may be disapproved if found to be excessive, inadequate, or unfairly discriminatory

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Reserves

Insurer Reserves:

- Are the funds set aside to cover the estimated cost of paying benefits on claims?
- Requires projection of future amounts needed to pay claims
- Actual cost to pay claims can turn out higher or lower than projected

CSI Role:

- CSI examinations staff review Annual Reports and the Insurers Actuarial Opinion on Reserves each year
- CSI obtains an Actuarial Review of Reserves as part of Financial Examinations
- Reserves must be Reasonable and Adequate

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Policyholder Surplus

Surplus funds aid in assuring a company will be able to pay its claims and help protect a company from insolvency

Adequate surplus is critical in Workers' Compensation-purposes include:

- Needed to pay for the future cost of claims if such costs turn out to be more than the estimated reserves
- Needed to cover premium deficits if future costs on current year policies turn out to be more than what was included in the rates
- Needed to absorb unexpected downturns in the value of invested assets held to fund future claim payments

CSI Role:

- Monitor and Regulate Insurer Solvency

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Solvency - Risk Based Capital (RBC)

RBC is one tool used to measure the minimum amount of capital (or policyholder surplus) an insurance company needs

Regulators use the RBC system to require a company to make preventive or corrective measures to improve financial solvency

Steve Matthews, head of our Financial Examination Bureau will be up soon to explain our approach in reviewing the financial solvency of a company.

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Risk Based Capital (RBC)

Montana State Fund (MSF) has a higher RBC requirement than private insurers.

Factors supporting the higher RBC:

- MSF incurs a higher risk as the Guaranteed Market for MT
- MSF does not have the ability to access additional capital
- MSF is not a member of the MT Guaranty Association
- MSF writes one line of insurance in one state

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Rates - Reserves - Surplus

Reserves and Surplus: “What they mean to rates”

Restated: What do Rates mean to Reserves and Surplus?

Rates must be set:

- ✓ To cover the cost of claims to closure (adequate reserves)
- ✓ To cover expenses of the insurer
- ✓ To maintain appropriate surplus

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Rates - Reserves - Surplus

There is a balance:

- If surplus was determined to be too high and in response rates were set artificially low-
 - Competition is impacted

- Or if surplus is maintained too low and preventative or corrective action is necessary by the regulator-
 - Policyholders can be hit with steep rate increases
 - Insolvency of the company can occur

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Insolvency

Montana, like others states, has been impacted by insolvent Workers' Compensation Insurers. The Montana Guaranty Association has covered claims from 14 insolvent Workers' Compensation Insurers since approximately 1985

96.4% of 139 open claims in the Guaranty Association are Workers' Compensation:

Total claim reserves are \$25,776,570 as of 4-9-18

Covered claims are paid in full-no cap on payments

There is a similar concern with Long Term Care Insurers- inadequate rates and surplus have led to rate hikes and even insurer insolvency

Workers' Compensation and Long Term Care are both long tail lines of insurance- the losses are not fully known for a long period

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Rates - Reserves - Surplus

Financially strong Insurers are key to protecting consumers
– we want insurers to be able to pay claims as they come due

Steve Matthews will be up next to provide some additional information on Solvency Regulation

Questions?

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Solvency Regulation

SURPLUS PROVIDES A CUSHION AGAINST INSOLVENCY RISK

ASSETS – LIABILITIES = SURPLUS / CAPITAL / TOTAL CAPITAL AND SURPLUS / POLICYHOLDER SURPLUS / POLICYHOLDER EQUITY

MSF: \$1,684,538,074 - \$1,129,836,991 = \$554,701,083

MSF: UNPAID LOSS RESERVE \$919.7 MILLION

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Statutory Tool Box

Financial Reporting

- Annual and Quarterly Statutory Financial Statements
- Annual Actuarial Opinion
- Annual Independent Auditor Reports

Investment Laws

Risk Based Capital (RBC)

Hazardous Financial Condition Determination (Regulation)

Credit for Reinsurance

Holding Company

Examination

Supervision, Rehabilitation, and Liquidation Laws (not applicable to MSF)

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Risk Based Capital (RBC)

Establishes a minimum capital (surplus) requirement (authorized control level) based on risk.

- Asset Risk
- Underwriting Risk

Functions as a “Tripwire” system. Alerts regulators to undercapitalized companies while there’s still time for corrective action.

Triggers regulatory action based on comparison of actual capital to the authorized capital level.

- > 200% No Action (MSF 400%)
- 200% - 150% Company Action Level (RBC Plan)
- 150% - 100% Regulatory Action Level (corrective action order)
- 100% - 70% Authorized Control Level
- < 70% Mandatory Control Level

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Montana State Fund

RBC at 12/31/2017 918%

- Authorized Control Level \$60.4 million
- Company Action level \$161.6 million
- Actual Capital \$554.7 million

Commercial work comp insurers had RBC levels ranging from 261% to 887%.

Other State Funds: -441% to 3,517%. (Average 1,090%)

What's the right RBC level...what level of risk are you willing to take?