



Overview of the Proposed Florida Workers Compensation Rate Filing

Effective January 1, 2019

I. Summary

This document summarizes the proposed 13.4% rate decrease, effective January 1, 2019, that the National Council on Compensation Insurance (NCCI) filed with the Florida Office of Insurance Regulation (OIR) on August 27, 2018. NCCI is a licensed rating organization authorized to make rate filings on behalf of workers compensation insurance companies in Florida. NCCI's rate filing is objectively prepared, in compliance with actuarial standards. The proposed filing is submitted to the state insurance commissioner for review and approval.

The filing, based on experience data as of year-end 2017 from Policy Years 2015 and 2016, shows continued significant improvement in loss experience. This is consistent with prior experience filings in Florida and in line with most filings submitted thus far by NCCI in other states in 2018. In 2016, two separate Florida Supreme Court decisions resulted in changes to the Florida workers compensation landscape. Those cases, *Castellanos v. Next Door Company, et al.* and *Westphal v. City of St. Petersburg, et al.* brought about retroactive changes to claimant attorney fee and benefit levels. However, the favorable loss experience in Policy Years 2015 and 2016 has more than offset the combined cost increases that have emerged from those Court decisions.

For this filing, about 50% of the data analyzed relates to policies that became effective after the *Castellanos* and *Westphal* decisions. NCCI believes the *Castellanos* and *Westphal* decisions are now exerting upward pressure on system costs, and they will continue to influence Florida workers compensation insurance rates. Policy Year 2017 will be the first full policy year post-*Castellanos*; however, the full effects of that decision will not materialize for several years to come.

II. Background

Florida's last major workers compensation legislative reform, Senate Bill (SB) 50A, became effective in October 2003. Many stakeholders considered a primary component of the reform to be the changes that were made to attorney fees. Prior to the passage of SB 50A, there was an attorney fee schedule which was based on a percentage of benefits secured for the injured worker. However, the ability to deviate up from the fee schedule to hourly fees led to increased litigation activities resulting in cases remaining open longer, a higher average cost per case, and longer time for injured employees to return to work. SB 50A instituted caps on attorney fees. The fee schedule under SB 50A reduced litigation activities resulting in quicker settlements, a lower average cost per case, and faster return to work outcomes. However, changes to the

system can take time to show their full impact. By 2015, 13 years following the passage of SB 50A and including other system drivers, rates in Florida had decreased by approximately 60%.

In 2016, the Florida Supreme Court issued decisions in the *Castellanos* and *Westphal* cases. The mandatory claimant attorney fee schedule without regard to reasonableness of fees was found to violate the due process clause and was ruled unconstitutional in *Castellanos*. This decision effectively eliminated the statutory fee schedule cap on claimant attorney fees implemented with SB 50A. In the *Westphal* decision, the statutory limit of 104 weeks of temporary total disability benefits was ruled unconstitutional.

In response to these two court decisions, NCCI submitted a law-only filing to the OIR in July 2016. (A law-only filing occurs outside the normal rate filing schedule and is prompted by legal or legislative developments that are expected to impact workers compensation system costs). The OIR approved a rate increase of 14.5% effective December 1, 2016. The main driver behind the increase was the *Castellanos* decision (+10.1% of the total +14.5%), which essentially returned attorney fee awards in Florida back to the way they were prior to the passage of SB 50A.

In August 2017, NCCI made its first experience filing in Florida since the *Castellanos* and *Westphal* decisions. The two new policy years of data showed continued improvement in experience, driven primarily by a two-year decrease in Florida claim frequency of more than 8%. After reviewing NCCI's filing, the OIR approved a rate change of -9.5% effective January 1, 2018.

III. What is the Primary Driver Behind the Proposed Rate Decrease?

Consistent improvement in loss experience is the primary driver underlying the filing. More specifically, the long-term decline in claim frequency has continued to more than offset moderate increases in claim severity. This has resulted in continued downward pressure on the overall average rate level need and is consistent with trends across most NCCI states.

IV. Emerging Impact of the *Castellanos* Decision

An assessment of the emerging impact of the *Castellanos* decision on Florida's workers compensation marketplace was undertaken as part of this year's filing review pursuant to the *Order on Rate Filing* issued by OIR on October 31, 2017. Specifically, NCCI reviewed insurance company feedback, the change in claimant attorney fees, and the change in loss experience that has occurred since the *Castellanos* decision. To date, observed system changes in each of these areas are directionally consistent with NCCI's initial assessment of how the *Castellanos* decision would impact the Florida marketplace.

A. Insurance Company Feedback

NCCI obtained feedback from the state's largest workers compensation insurers who report financial data to NCCI. Most companies stated they have experienced claim cost increases after the *Castellanos* decision, while a minority of carriers have not been materially impacted. All

insurance companies stated they have experienced increases in claimant attorney fees. They also have observed that litigated claims tend to take longer to close and are costlier when compared with non-litigated claims. Additionally, some insurers reported that litigated claims now represent a relatively larger portion of their book of business. Most companies said that they have adjusted their case reserves in response to the *Castellanos* decision. Case reserves are amounts estimated by insurance company claim professionals that are set aside to cover the future payments on a claim.

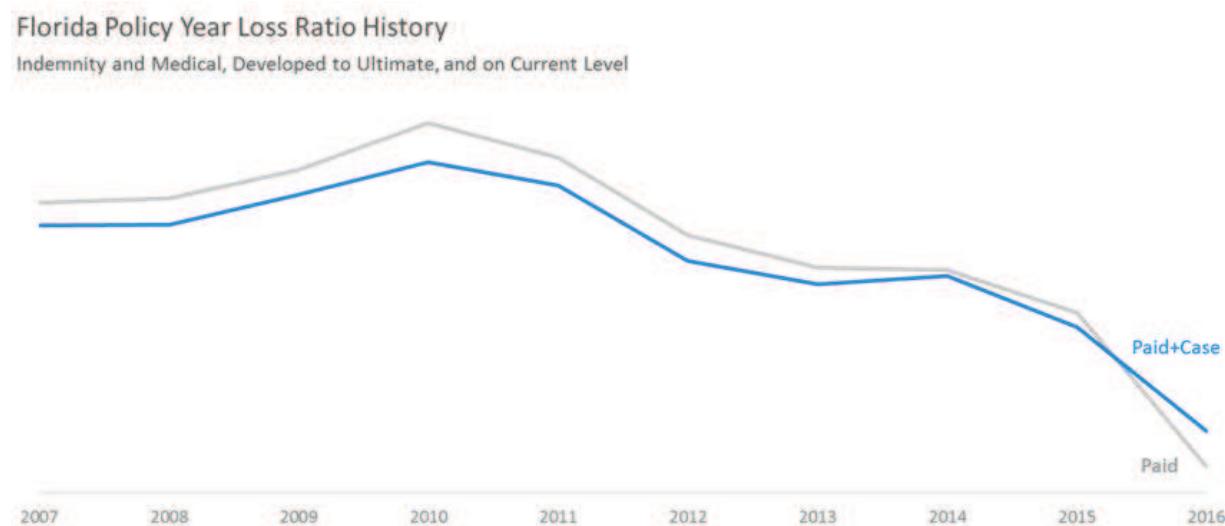
B. Claimant Attorney Fees

The increase in claimant attorney fees observed by insurance companies is supported by data obtained from the Florida Division of Administrative Hearings (DOAH). DOAH data received through June 2018 has shown a marked increase in the ratio of claimant attorney fees to benefit and settlement amounts. In 2014 and 2015, the ratio of claimant attorney fees to benefit and settlement amounts was approximately 13%. There was a slight uptick in 2016 to more than 15%. By 2017, the ratio had increased to more than 19%. Through June 2018, claimant attorney fees have continued to rise and now represent almost 22% of benefit and settlement amounts.

C. Loss Experience

NCCI's proposed rate filing utilizes two different approaches to analyze emerging loss experience. The Paid method relies exclusively on paid losses, while the Paid+Case method relies on the combination of paid losses and case reserves. Consistent with historical rate filings in Florida, equal weight is given to the results of both the Paid and Paid+Case methodologies.

Historically, Florida's Paid loss ratios have exceeded those based on the Paid+Case methodology. As illustrated below, this longstanding pattern notably reversed itself for the first time in 2016. This reversal is consistent with insurance company feedback indicating that they have increased case reserves and are observing a slowing down in the payout of workers compensation claims in Florida's post-*Castellanos* environment.



V. Data Sources That Will Be Used to Analyze the Future Impact of the *Castellanos* Decision

There are three main data sources that will assist NCCI in analyzing the future impact of the *Castellanos* decision. These include Unit Statistical Data, Supplemental Financial Data and a future Indemnity Data Call.

A. Unit Statistical Data

Unit Statistical Data is used for the Class Ratemaking portion of NCCI's rate filing. In addition to audited exposure, premium, and losses, it also includes both claimant and employer attorney fee data for Florida. Since a Unit Report is first valued six months after the policy expires, it takes about two years to develop a complete policy year. This means that Unit Statistical Data for 2016 will be included for the first time in Florida's rate filing effective January 1, 2020.

B. Supplemental Financial Data

In 2017, NCCI requested supplemental Financial Data from insurers in Florida. This voluntary request for information asked for a further breakdown of financial data already being reported to NCCI based on the status of claims before and after the *Castellanos* decision. Specifically, the number of claims along with the associated claim payments and reserves were collected for years 2009 and subsequent at both year-end 2016 and year-end 2017. At this time, NCCI only has a single calendar year of information based on this data. The data's usefulness in providing insight into how the *Castellanos* decision is affecting Florida's workers compensation environment may increase over time as additional valuations of data are collected.

C. Indemnity Data Call

NCCI is in the process of creating a future Indemnity Data Call to insurers. This Call will provide more current, comprehensive, transactional indemnity data that will be used to support NCCI's legislative pricing and research related to indemnity benefits. Indemnity claim activity for all workers compensation claims for which an indemnity payment has been made or reserved will be reported. This includes attorney fee information for both employers and claimants. NCCI will start to collect indemnity data in mid-2020, once carriers have completed the infrastructure changes and testing necessary to report this information.

VI. Conclusion

NCCI's workers compensation rate filing proposed a 13.4% decrease. The filing shows continued improvement in loss experience and is in step with prior experience filings in Florida along with most filings submitted by NCCI in other states this year. The primary driver behind the recommended rate decrease is the long-term decline in claim frequency offsetting increases in claim severity and cost increases from the *Castellanos* and *Westphal* court cases. Policy Year 2017 will be the first full policy year post-*Castellanos*, but the full effects of that Court decision will not materialize for several years to come.