ABCs of Experience Rating

Introduction

This document is designed to further your understanding of experience rating and how it affects your workers compensation costs.

NCCI's ***Experience Rating Plan Manual for Workers Compensation and Employers Liability Insurance*** ("Plan") is an integral part of the final cost of workers compensation. It is a method for tailoring the cost of insurance to the characteristics of an employer or risk. It gives the employer the incentive to manage its own costs through measurable and meaningful cost-saving programs.

The Plan predicts whether a qualifying employer is likely to develop loss experience that is better or worse than that of the average risk in a particular classification. It modifies manual premium by a factor that is designed to more accurately price qualified employers. The Plan uses the employer's past experience to project future losses and provides added incentives for loss reduction.

While the underlying concepts are complex, this document will clarify the application of these concepts.

What Does Experience Rating Do?

Insurance spreads, or shares, the cost of a loss with members of a group that are likely to experience similar losses. While the cost and probability of injuries for the *whole* group can be predicted with a fair degree of accuracy, it is impossible to determine which member of the group will actually be responsible for these costs.

This is why insurance exists. If predictability were perfect, the members of the group that do not expect to experience a loss would have no incentive to purchase insurance, while the premium charge for the members that will experience the loss would need to include the value of the loss.

Historically, we know that serious individual injuries generally are rare and that the cost could vary from very minor amounts to millions of dollars.

The simplest rating method for workers compensation and employers liability insurance is "manual rating." Under manual rating, all employers are grouped according to their business operation or classification. The estimated losses of the group are added together, and an average cost is obtained. The rates determined for manual rating are averages reflecting the normal conditions found in each classification. An employer is assigned to a classification to ensure that the rates reflect the costs of all employers with similar characteristics. Although each classification contains "similar" risks, each individual risk in a class is different to some extent. Experience rating is designed to reflect these individual differences in loss potential.

If the rating system went no further than manual rating, insurance providers could seek employers with lower-than-expected costs and possibly avoid employers with higher-than-expected costs. To avoid this scenario, the rating system must be further refined. Experience rating is one such refinement.

In workers compensation experience rating, the actual payroll and loss data of the individual employer is analyzed over a period of time. Usually, the latest available three years of data is compared to similarly grouped risks to calculate the experience modification.

In general, an employer with better-than-average loss experience receives a credit, while an employer with worse-than-average experience carries a debit rating. Experience rating takes the average loss experience and modifies it based on the individual's own loss experience.

901 Peninsula Corporate Circle • Boca Raton, FL 33487-1362 • 800-**NCCI**-123 (800-622-4123)

The two primary benefits of experience rating are:

- It tailors the cost prediction and final net premium cost to the individual employer more closely than does manual rating alone
- It provides added incentives for loss reduction that are absent from manual rating alone

Why Have Experience Rating?

If workers compensation rates are designed to predict future losses, why use experience rating? How does experience rating benefit employers?

Experience rating represents a refinement in the premium determination process. It does so by comparing the industry average experience with an individual employer's own experience. It benefits employers by producing a net premium cost that is the best indicator of an individual employer's own potential for incurring claims. This means that the insurance premium will be appropriate for the coverage being provided by using sound insurance principles and an employer's own payroll and loss data.

Implicit in most risk-specific programs of experience rating is the prospect of both debits and credits. Since experience rating gives individual employers some influence over the final premium they pay, it provides an incentive for employers to develop loss prevention as well as incentives to have the injured employees return to work as soon as reasonably possible. In this way, experience rating benefits employers by promoting occupational health and safety.

Characteristics of Experience Rating

We have already mentioned the need to modify the premium based on manual rates, but what are the characteristics that the Plan recognizes?

A significant feature of experience rating is that it recognizes that the cost of a specific accident is often left to chance and is statistically less predictable than the fact that the accident *occurred*.

For example, the survivor benefits for a young worker in his 20s leaving a widow and three children would likely be considerably greater than the survivor benefits for a worker in his 50s leaving no dependents. The important fact is that the accident did occur, so *the Plan gives greater weight to accident frequency than to accident severity*.

This reliance on accident frequency also measures risk differences. For example, compare two similarly sized employers from the same classification:

Employer A
1 loss totaling $50,000

Employer B
10 losses totaling $50,000

Which employer would you expect to incur the higher workers compensation costs in the future? Statistically, Employer A—with the one large claim—is more stable, particularly when you consider that any one of the 10 small accidents of Employer B could incur higher costs than the $50,000 amount given the proper combination of circumstances. In other words, for two similar risks, the one with the higher frequency of claims will generally have higher future workers compensation costs.

However, the fact that an employer may have a small number of very costly injuries should not be ignored. The final measure must be a blend of both the occurrence and the individual *cost* of each injury.

The Plan recognizes and measures both accident frequency and severity. Although severity of losses is recognized in experience rating, very large losses are less likely to occur and are seen as more fortuitous than smaller claims. In fact, very large losses are so infrequent that including the entire portion of the claim beyond a certain level in the experience period reduces the predictive ability of the Plan. One very large claim does not imply a pattern of claim frequency. So each individual claim is capped by a state accident limitation. The state accident limitation amount differs by state.

For example, let's use a state accident limitation amount of $150,000. Exhibit A shows that an individual loss of $500,000 would be capped at $150,000 for experience rating purposes. These limited losses used in the Plan are *ratable losses*. The amount of loss above the state accident limitation is excluded from the

calculation of the employer's experience rating modification and is a *nonratable loss*.

A *split rating* approach is used to reflect both the frequency and severity of losses. The split of individual ratable losses, as of January 1, 2015, in approved states, is made as follows:

- The amount of any ratable individual loss up to $15,500 is known as *primary loss*, which reflects frequency
- The amount in excess of $15,500 is known as *excess loss*, which reflects severity
- For individual claims below $15,500, the entire amount is primary loss and the excess loss is $0

See how this concept is applied in Exhibit A.

Under this split method, primary losses are given a greater weight in the formula than excess losses. Because of this, primary losses have a greater impact on the experience rating modification. Although excess losses have less weight, they're still relevant since total excess claim dollars can be high. The Plan includes an incentive for employers to reduce the frequency of claims, as well as an incentive to encourage injured employees to return to work as soon as reasonably possible. This type of involvement by the employer can reduce the severity of claims once they have occurred.

The weights or credibilities assigned to primary or excess losses are calibrated to ensure that the modification best reflects the loss history of the particular employer relative to its classification.

These credibilities vary by size of employer. The larger an employer, the more its experience rating calculation is influenced by its own experience. By contrast, a small employer may be covered for years without a claim and then incur an injury where the cost exceeds the total premium paid many times over. An equitable Plan must recognize this fact and temper the debit due to such a loss, as well as the credit for having no losses.

For example, an employer with 10 small losses of $5,000 each has a much larger primary loss total than an employer with a single loss of $50,000, even though each would have a loss total of $50,000. An employer with a single claim of $50,000 has $15,500 in primary loss, and the rest is excess. Because of the relative weightings, the 10-injury employer receives a much higher modification than the 1-injury employer, even though its total losses are the same.

Medical-only claims do not have as much of an impact on the experience modification because most states have approved Experience Rating Adjustment (ERA), which limits the amount of such claims in the experience modification calculation. This ERA change to the formula decreases the incentive for employers to pay medical-only claims without reporting them to the carrier.

Only 30% of the actual primary and excess portions of an individual medical-only claim are included in the calculation of the modification factor. As a result, medical-only claims are reduced by 70%. This reflects the impact of medical-only claims more appropriately.

For example, consider a single medical-only claim of $20,000. The primary portion of the loss is $15,500, and the excess portion is $4,500. After the adjustment, the primary portion of the loss included in the experience modification calculation is $4,650 (30% x $15,500), and the excess portion of this claim is $1,350 (30% x $4,500).

Exhibit A—Split Rating

Loss Amount	State Accident Limitation	Primary Loss (Frequency)	Excess Loss (Severity)
$500,000	$150,000	$15,500	$134,500
$500,000	$100,000	$15,500	$84,500
$5,000		$5,000	$0

How the Plan Operates

Experience rating is a *mandatory* plan, which applies to all employers that meet a state's premium eligibility criteria for the Plan. Experience rating calculations are computed by NCCI. As of this publication, **38** jurisdictions have approved and authorized the use of the Plan. In Minnesota, New York, Texas, and Wisconsin, the Plan applies on an interstate basis only. These four states participate in the Plan only if the risk has exposure in two or more participating states within the experience period.

The Plan applies in Indiana, Massachusetts, and North Carolina. However, the state bureaus in these three states are responsible for producing their own intrastate ratings.

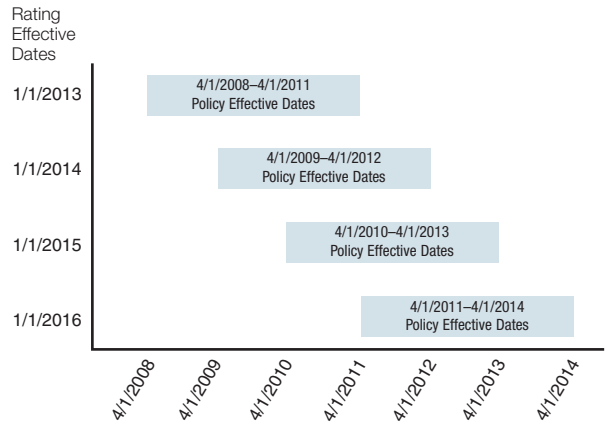
The Plan does not apply in California, Delaware, Michigan, New Jersey, and Pennsylvania. Nor does it apply in the four monopolistic states (North Dakota, Ohio, Washington, and Wyoming) that administer their own plans and rates.

Experience rating is a standard measure not impacted by individual insurance provider pricing programs. An employer qualifies for experience rating if the subject premium meets a premium eligibility point. (Eligibility criteria differ by state. Refer to the Plan for further details.) Because experience rating is based on past payroll and loss experience, each risk is evaluated based on its own experience period.

A risk's rating effective date determines the experience period. The experience period is generally based on three years of payroll and loss data, but could range from containing less than 12 months of data up to the inclusion of 45 months of data. The amount of policy data used on the experience rating may differ due to short-term policies, policies with different effective dates, or a new risk that qualifies to be experience rated with policy data from its first policy.

Data from each of a risk's policies is included in the experience period if the policy effective date is no less than 21 months before the rating effective date and no more than 57 months before the rating effective date. Since the modification is calculated during the term of the current policy—generally 60 to 90 days before the rating effective date—the current policy is not used in the calculation of the experience rating modification. Also, the insurer is not required to report data about the policy until 18 months after the policy inception date. This allows insurers time to value claims that may have occurred, and to prepare and submit the required reports to NCCI. Therefore, for a rating effective date of January 1, 2015, any policy with an effective date between 4/1/10 (1/1/15 less 57 months) and 4/1/13 (1/1/15 less 21 months) is included in the experience period. Exhibit B illustrates the policies that are included in a risk's experience period for each rating effective January 1.

Exhibit B—Experience Period



An employer with a policy that renews on January 1, 2015, will generally have an experience rating that uses the loss experience that occurred during policies that were effective 1/1/11–1/1/12, 1/1/12–1/1/13, and 1/1/13–1/1/14.

Because loss data for the 2014 policy period is not yet valued by the insurance provider or reported to NCCI, it is not used when the 2015 modification is being calculated. The next renewal, on January 1, 2016, will use the 2014 payroll and loss experience, while dropping the oldest policy of the three-year period mentioned above.

This constant updating ensures a stable historical record for the individual employer, while also using the most recent available reflection of operating characteristics. In this way, meaningful changes in safety programs or improved technology can be reflected in the costs paid by an employer.

Once the employer meets the qualifications for rating, the Plan formula is applied and a credit or debit modification is published by the rating organization (NCCI). The experience modification factor must be used by any insurance provider insuring the business. Generally, it applies for one year, and a new modification is calculated for the next year (as long as eligibility requirements are met).

A detailed explanation of the experience rating calculation is shown later in this document.

Qualification for Experience Rating

According to the Plan, if an employer meets the eligibility requirements, then experience rating is mandatory. The eligibility requirements are established and approved on a state-by-state basis. To qualify, the employer must achieve the established premium threshold by one of two methods:

1. Have enough premium subject to experience rating in the most recent 24 months

OR

2. Achieve the established premium threshold on average over the entire experience period

Example

The state of Florida requires $10,000 in audited premium subject to experience rating in the most recent two years of the experience period **OR** an average of $5,000 in the overall experience period. Exhibit C illustrates how the qualification requirement can be met for a 2015 experience rating.

Exhibit C—Qualification for Experience Rating

Employer 1	Employer 2
2013—$6,500	2013—$4,100
2012—$5,500	2012—$5,200
2011—$2,000	2011—$6,000
Qualification requirement met in the most recent two years	Qualification requirement met when premium is averaged over three years

The premium qualification thresholds by state can be found in the Premium Eligibility table in the Plan.

If Employer 2 continues to experience declining premium amounts in subsequent years, it may no longer qualify to be experience rated. If this were to occur, the insurance provider would be notified by NCCI that the employer no longer qualifies to be experience rated.

Types of Experience Rating

There are two types of experience modifications developed by NCCI: intrastate and interstate. An *intrastate* modification factor is issued when the employer has exposure in only one state that participates in the Plan. An *interstate* modification is issued when the employer has exposure in two or more states that participate in the Plan.

Intrastate Modification

Take, for example, an employer that has exposure in Florida only. Florida participates in the Plan; therefore, if the employer meets the qualifications established, NCCI will develop and publish an *intrastate* modification for Florida.

If an employer has exposure in Florida and Pennsylvania (Pennsylvania does not participate in the Plan) and meets the qualifications in both states, NCCI will develop and publish an *intrastate* modification that includes the payroll and loss experience for Florida only. The Pennsylvania bureau will develop an *intrastate* modification that includes the payroll and loss experience for Pennsylvania only.

Interstate Modification

If an employer has exposure in Florida and New York (both states participate in the Plan), and meets the qualifications established for at least one of those states, NCCI will develop and publish an *interstate* modification for the employer. The modification will include payroll and loss experience from both Florida and New York.

Status of Experience Rating

The status of an experience modification is important because it is used to determine what state-approved rating values are being used to calculate the experience rating modification. There are three statuses:

1. Preliminary
2. Final
3. Contingent

If the status is *preliminary*, it means that NCCI does not have the final approved rating values for the state(s). A modification will be calculated using the prior approved rating values. Once the state's final approved rating values have been

received by NCCI, the modification will then be revised to indicate a status of *final*.

Note: NCCI cannot indicate that an interstate modification is in a *final* status until all of the states' final approved values are used in the calculation. Using the previous interstate example, if Florida and New York are both being calculated, and NCCI has Florida's final approved rating values but not New York's, the interstate modification will have a status of *preliminary* until NCCI receives the New York final approved rating values for use. The worksheet will define which states are outstanding.

Lastly, another status used in experience rating is *contingent*. A *contingent* modification is issued when NCCI is expecting audited payroll and loss information but has not received the information from the insurance provider by the time the rating is produced. Once the audited payroll and loss information is received by NCCI, the modification will be revised to add the newly received experience data.

Experience Rating Modification Factor

The modification factor applied to an employer's policy is either a unity (1.00) factor, a credit modification, or a debit modification.

An employer will receive a unity factor against the premium if any of the following apply:

- It does not meet eligibility requirements for experience rating
- It does not meet the minimum data requirements
- It is a new business with no data available for production of an experience rating modification
- It qualifies for experience rating, and the calculation results in a 1.00 modification
- Data could not be provided as a result of an ownership change

A credit modification is a modification lower than 1.00. If an employer runs a safe workplace, which includes implementing safety programs, the employer will be in a better position to receive a credit experience rating modification factor against their premium.

A debit modification is a modification higher than 1.00. If an employer receives a debit experience rating modification factor against its premium, it may benefit from a review of its workplace safety programs.

Application of Experience Rating

Exhibit D illustrates the impact that various experience modification factors can have on the final premium an employer pays. In these examples, the premium prior to the application of the modification factor is $100,000.

Now let's examine a more detailed example that illustrates how both the rates and the experience modification factor are used to determine the premium an employer pays. The information displayed in Exhibit E is for a single roofing company with employees in two classifications. The rate, which is approved by the state for each classification, is applied per $100 of payroll. The roofer's rate is higher than the clerical rate because it has greater exposure to injuries. Each $100 of payroll is multiplied by the rate to arrive at the premium for each classification. Summing the premium for these two classifications yields the initial total premium. The modification factor is then applied to arrive at the modified premium.

Exhibit D—Application of Experience Rating

Premium		Modification Factor		Modified Premium
$100,000	x	0.75	=	$75,000
$100,000	x	1.00	=	$100,000
$100,000	x	1.25	=	$125,000

Exhibit E—Application of Experience Rating

Classification	Payroll	Divided by 100	Rate per $100 of Payroll	Premium
Clerical	$70,000	700	$0.75	$525
Roofer	$200,000	2,000	$63.17	$126,340

Total Premium = $126,865
Modification Factor = 1.25
Modified Premium = $158,581

Data Used on the Experience Rating Worksheet

The payroll and claim/loss information used in experience rating comes from unit statistical reports. Insurance providers are required to file a unit report with NCCI for each policy they issue in accordance with NCCI's ***Statistical Plan for Workers Compensation and Employers Liability Insurance***. Other factors or rates on the worksheet are actuarially derived and are updated with each change in rates approved on a state-by-state basis.

The **first step** in the experience rating process is to transfer the payroll and loss information from the unit report to the experience rating worksheet. Let's take a look at an NCCI experience rating worksheet for "Any Insured" in Exhibit F.

Risk Information

The top section of Exhibit F contains the basic identifying information, such as the name of the employer **(1)**, the state in which the employer is located **(2)**, and the risk identification number **(3)**. In addition, it shows when the experience modification was calculated **(4)** and that it will be used for the policy that becomes effective January 1, 2015 **(5)**.

The payroll and loss information is shown separately for each of the three policies included in the calculation, with the oldest audited policy information toward the top of the page and the most current audited policy information toward the bottom of the page. Starting on the left-hand side, we have the payroll (exposure) **(6)** for each classification code **(7)**.

Expected Losses

The ELR **(8)** is the Expected Loss Rate. It is the amount of expected losses for the classification for each $100 of payroll. Therefore, to obtain the expected losses, multiply the ELR by the payroll divided by $100.

Taking the first line of the worksheet as an example, with an ELR of **1.46** and payroll of **$3,325,338**, the calculation is **1.46 x ($3,325,338 ÷ 100) = $48,550**. The **$48,550** is entered in the Expected Losses column **(9)**.

The D Ratio **(10)** is the Discount Ratio. It represents the portion of the expected losses that are expected *primary* losses **(11)**. Multiply the expected losses by the D Ratio to get the expected primary losses. The calculation is **$48,550 x 0.31 = $15,051**.

Claim Information

On the right-hand side is the reported claim information for each policy. Note that each loss is not directly attributable to the payroll information on the corresponding line. The claim data column **(12)** indicates claim numbers for losses more than $2,000. Individual claims of $2,000 or less may be grouped together by injury type **(13)**. The number of claims grouped will be indicated in the claim data column **(12)** by "NO." In addition, there is an indicator that shows whether the claim is open (O) or final/closed (F) **(14)** and the actual incurred losses **(15)**.

Note that in transferring the losses from the unit report to the experience rating worksheet, the indemnity and medical amounts are combined because we are only concerned with the total amount of the claim.

For example, claim number **1200001 (16)** has an indemnity cost of $11,200 and a medical cost of $5,559 for a total of **$16,759 (17)**. Medical-only claims (Injury Type 6) are reduced by 70%. The reduced losses are shown in the summary only; the claim detail shows the entire actual amounts **(18)**.

The **second step** is to separate the actual losses into primary and excess components. The actual primary losses are shown in the last column **(19)**. For losses less than $15,500, the whole amount is taken as the primary value. For losses greater than $15,500, only the first $15,500 is primary.

Exhibit F—Page 2 of the Experience Rating Worksheet (DETAILED)

WORKERS COMPENSATION EXPERIENCE RATING

Risk Name: ANY INSURED **Risk ID:** 990123456

Rating Effective Date: 01/01/2015 **Production Date:** 09/02/2014 **State:** ANY STATE

00-ANY STATE **Firm ID:** **Firm Name:** ANY INSURED

Carrier: 00000 **Policy No:** 2011UNIT **Eff Date:** 01/01/2011 **Exp Date:** 01/01/2012

Code	ELR	D-Ratio	Payroll	Expected Losses	Exp Prim Losses	Claim Data	IJ	OF	Act Inc Losses	Act Prim Losses
8380	1.46	.31	3,325,338	48,550	15,051	1100001	05	F	7,317	7,317
8748	.36	.31	2,145,647	7,724	2,394	1100002	05	F	28,985	15,500
8810	.07	.35	1,579,999	1,106	387	NO. 14	06	*	18,365	18,365
Policy Total:			**7,050,984**	**Subject Premium:**	**195,190**	**Total Act Inc Losses:**			**54,667**	

00-ANY STATE **Firm ID:** **Firm Name:** ANY INSURED

Carrier: 00000 **Policy No:** 2012UNIT **Eff Date:** 01/01/2012 **Exp Date:** 01/01/2013

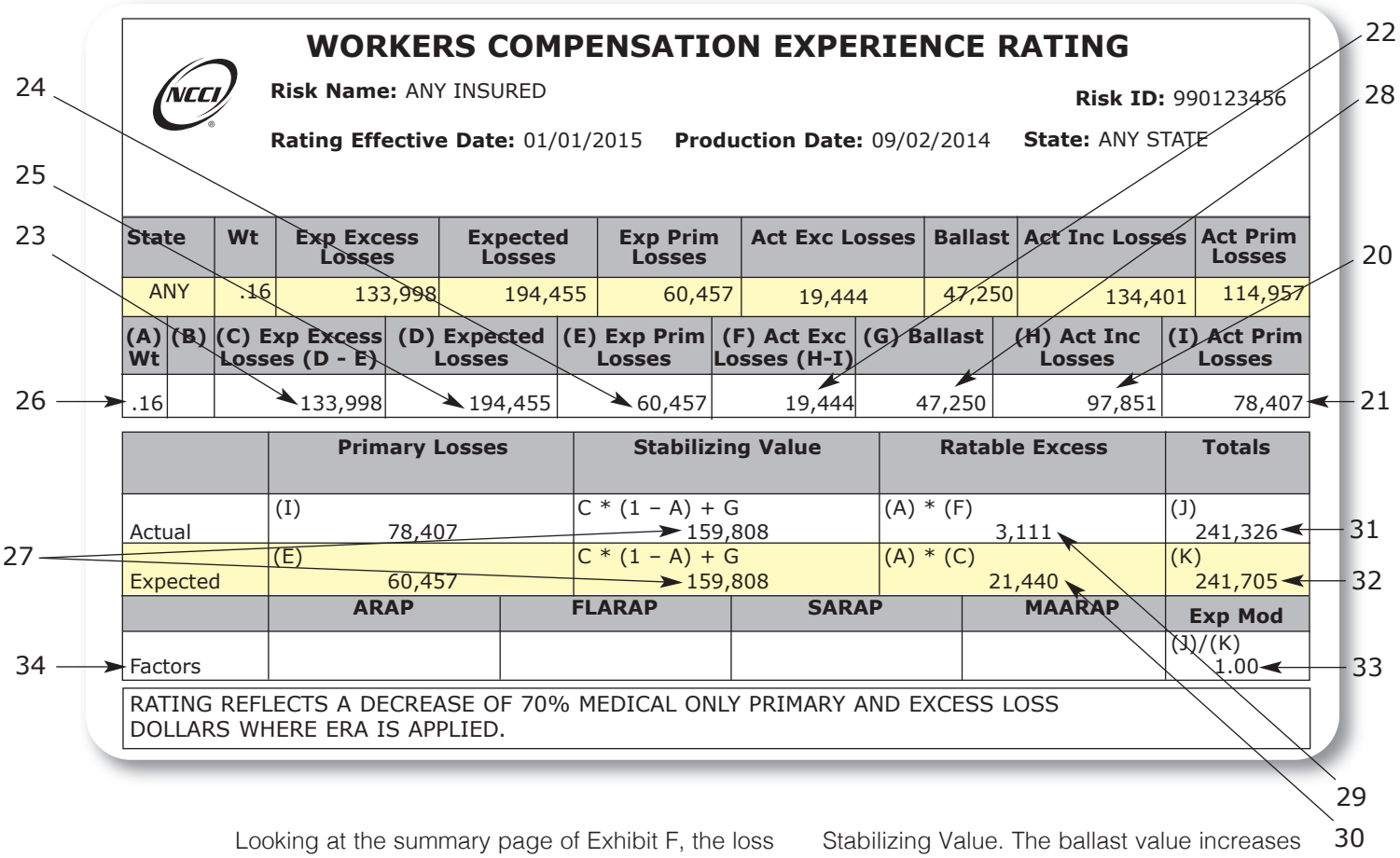
Code	ELR	D-Ratio	Payroll	Expected Losses	Exp Prim Losses	Claim Data	IJ	OF	Act Inc Losses	Act Prim Losses
8380	1.46	.31	3,486,050	50,896	15,778	1200001	05	F	16,759	15,500
8748	.36	.31	2,398,429	8,634	2,677	1200002	06	F	2,250	2,250
8810	.07	.35	1,897,869	1,329	465	NO. 19	06	*	28,453	28,453
Policy Total:			**7,782,348**	**Subject Premium:**	**230,125**	**Total Act Inc Losses:**			**47,462**	

00-ANY STATE **Firm ID:** **Firm Name:** ANY INSURED

Carrier: 00000 **Policy No:** 2013UNIT **Eff Date:** 01/01/2013 **Exp Date:** 01/01/2014

Code	ELR	D-Ratio	Payroll	Expected Losses	Exp Prim Losses	Claim Data	IJ	OF	Act Inc Losses	Act Prim Losses
8380	1.46	.31	4,075,500	59,502	18,446	NO. 8	05	*	8,925	8,925
8748	.36	.31	4,104,329	14,776	4,581	1300001	05	O	20,200	15,500
8810	.07	.35	2,768,163	1,938	678	1300002	06	F	3,147	3,147
Policy Total:			**10,947,992**	**Subject Premium:**	**256,050**	**Total Act Inc Losses:**			**32,272**	

Exhibit F—Page 1 of the Experience Rating Worksheet (SUMMARY)



WORKERS COMPENSATION EXPERIENCE RATING

Risk Name: ANY INSURED **Risk ID:** 990123456

Rating Effective Date: 01/01/2015 **Production Date:** 09/02/2014 **State:** ANY STATE

State	Wt	Exp Excess Losses	Expected Losses	Exp Prim Losses	Act Exc Losses	Ballast	Act Inc Losses	Act Prim Losses
ANY	.16	133,998	194,455	60,457	19,444	47,250	134,401	114,957

(A) Wt	(B)	(C) Exp Excess Losses (D - E)	(D) Expected Losses	(E) Exp Prim Losses	(F) Act Exc Losses (H-I)	(G) Ballast	(H) Act Inc Losses	(I) Act Prim Losses
.16		133,998	194,455	60,457	19,444	47,250	97,851	78,407

	Primary Losses	Stabilizing Value	Ratable Excess	Totals
Actual	(I) 78,407	C * (1 – A) + G 159,808	(A) * (F) 3,111	(J) 241,326
Expected	(E) 60,457	C * (1 – A) + G 159,808	(A) * (C) 21,440	(K) 241,705

	ARAP	FLARAP	SARAP	MAARAP	Exp Mod
Factors					(J)/(K) 1.00

RATING REFLECTS A DECREASE OF 70% MEDICAL ONLY PRIMARY AND EXCESS LOSS DOLLARS WHERE ERA IS APPLIED.

Looking at the summary page of Exhibit F, the loss amounts used in the calculation are total losses of **$97,851 (20)** and primary losses of **$78,407 (21)**. By subtracting the primary from the total losses, we obtain excess losses of **$19,444 (22)**.

Now that primary and excess losses have been determined, the next step is to calculate the expected losses for the employer. The actual losses will be compared with the expected losses to determine whether a credit (decrease) or debit (increase) modification is in order.

After totaling the expected losses, the expected *excess* losses **(23)** are obtained by subtracting the total expected primary losses **(24)** from the total expected losses **(25)**. The calculation is $**194,455 – $60,457 = $133,998**.

Experience Rating Modification Factor

The **final step** is to calculate the experience modification factor. The term "ballast" is defined as something that gives stability, such as heavy material in the hold of a ship to keep it from shifting too far one way or the other. Similarly, the ballast factor in the experience rating formula helps prevent the experience modification from shifting too far above or below unity. It is part of the Stabilizing Value. The ballast value increases as expected losses increase.

The "Wt" factor **(26)** is the weight given to the excess losses and expected losses. "Wt" is a small percentage for small employers and increases with the size of the employer. The complement of "Wt" or "1 – Wt" is assigned to the expected excess losses to produce another part of the Stabilizing Value.

The Stabilizing Value **(27)** is calculated by multiplying the expected excess losses **(23)** by **(1 – Wt)**, then adding the ballast value **(28)**. The calculation is **$133,998 x (1 – 0.16) + $47,250 = $159,808**. The weighted ratable excess losses entering the formula are obtained by multiplying the excess by the "Wt" value:

(29) Weighted Actual Excess = **$19,444 x 0.16 = $3,111**

(30) Weighted Expected Excess = **$133,998 x 0.16 = $21,440**

Adjusted actual losses (the numerator of the fraction) used in the calculation are obtained by adding

across and are equal in this case to **$241,326 (31)**. The adjusted expected losses are **$241,705 (32)**.

The experience modification **(33)** is derived by dividing adjusted actual losses by the adjusted expected losses, or **$241,326 ÷ $241,705 = 1.00**. This **1.00** is applied to the employer's manual premium at the policy's renewal, effective January 1, 2015.

Notification of experience rating modification completion for each employer is sent by NCCI to the insurance provider on file, and in some states, to the employer. The experience rating modification and worksheet are also made available on **ncci.com** through ***Riskworkstation***™.

Additional Factors

The last row of the summary page **(34)** may include some or all of the following additional factors: Assigned Risk Adjustment Program (ARAP), Florida Assigned Risk Adjustment Program (FLARAP), Simplified Assigned Risk Adjustment Program (SARAP), and Massachusetts All Risk Adjustment Program (MAARAP). These factors are calculated using the same data used in the experience rating calculation and are filed and approved programs. Most surcharge factors are applied to assigned risk policies and are only for those risks with a debit modification.

Ownership Changes and Combination of Entities

Another component that may affect the experience modification is a change in the ownership of an individual risk. When a change in ownership occurs, the insurance provider must be notified in writing within 90 days of the date of the change. The best method of notifying the insurance provider of these ownership changes is to complete an ERM-14 Form—Confidential Request for Ownership Information. Upon receipt of this form, the insurance provider will forward this information to NCCI.

If a change in ownership occurs, recalculation of experience modifications may be required. Changes in ownership may affect the use of an individual risk's experience in past, current, and future calculations of experience ratings. NCCI may issue, retract, and/or revise the current modification and up to two preceding modifications due to ownership or combination changes. Generally, the past experience of the business will be transferred to the new owner. These changes may also result in a change in the rating effective date.

In addition, the experience of businesses with more than 50% common majority ownership is combined into one experience modification. Combinability of the experience of entities with the same ownership is based on the premise that the owner is responsible for safety and loss prevention programs within the businesses.

For additional information on the impact of ownership changes to the modification factor, please refer to the Plan and the Basics of Experience Rating Ownership Webinar on Demand.

Summary of the Plan

The essentials of experience rating are:

- It is mandatory for all employers that meet a state's premium eligibility requirements
- The formula measures how the performance of an employer differs predictably from similarly classified employers
- The formula is designed to tailor the cost of coverage to a particular employer

Two basic statistical principles underlie the formula:

1. The larger the premium size, the more reliable the actual record is in predicting future losses. Integral to the Plan is a credibility scale so that the actual historical record is given more weight/credibility as the size of the employer increases. Even the smallest risks have some credibility, but for practical purposes, it is necessary to have a premium threshold, or a minimum point, for eligibility.
2. The cost of an injury may vary over a very large range. Therefore, cost is less predictable than the fact that an injury occurred; this is accomplished through the use of the primary and excess loss components.

Additional Resources to Reference

To complement this document, there is a suite of experience rating Webinars on Demand—located on **ncci.com**—that cover some of the topics reviewed in more detail. The webinars can each be viewed in 30 minutes or less. They are:

- Basics of Experience Rating
- Advanced Experience Rating
- How to Understand Your Experience Rating Worksheet
- Basics of Experience Rating Ownership
- How to Complete the ERM-14 Form
- ***Riskworkstation***™
- The New Online Manuals Library

Click here to view the experience rating webinars.