

# *TerranearPMC Safety Share*

## **Week of November 4, 2013 – Changes in the Experience Modification Rate**

During our modern times, where everyone is trying to reduce risk, many businesses in the US will request to review a potential contractor's experience modification rate or EMR. The EMR is a number established in the insurance industry through the National Council on Compensation Insurance (NCCI) and is used by insurance companies to gauge both past cost of injuries and future chances of risk. The lower the EMR, the lower worker compensation insurance premiums will be. An EMR of 1.0 is considered the industry average, or what the insurance company predicts your losses should be when compared to similar businesses (business type, size, operations, etc.). In other words, your insurance workers compensation carrier is expecting a certain amount of accidents (equated into dollars) that it plans to set aside for payments towards accidents your company is likely to sustain. When your business has an EMR greater than 1.0, it is because there has been a history of accidents greater than anticipated and therefore, through a calculated EMR the worker compensation premium is adjusted.

The EMR is based on a three-year period, omitting the most recent year and going back from there. For instance, EMRs for 2013 include workplace incidents for 2011, 2010 and 2009. That means any injuries/illnesses during 2013 will not be considered until two years, in 2015, while injuries/illnesses in 2012 will cease being calculated into the EMR in 2017.

Frankly, calculating the EMR is a lot more involved than the calculations used for OSHA incident rates. The base premium is calculated by dividing a company's payroll in a given job classification by 100, and then by a 'class rate' determined by the NCCI that reflects the inherent risk in that job classification. For example, structural ironworkers have an inherently higher risk of injury than receptionists, so their class rate is significantly higher.

NCCI has developed a complicated formula that considers the ratio between expected losses in your industry and what your company actually incurred, as well as both the frequency of losses and the severity of those losses. A company with one big loss is going to be 'penalized' less severely than a company with many smaller losses, because having many small losses is seen as a sign that you'll face larger ones in the future (hence the term, "frequency breeds severity"). The result of that formula is your EMR, which is then multiplied against the manual premium rate to determine your actual premium (before any special discounts or credits from your insurer). Essentially, if your EMR is higher than 1.00, your premium will be higher than average; if it's 0.99 or lower, your premium will be less.

An EMR of 1.2 would mean that insurance premiums could be as high as 20% more than a company with an EMR of 1.0. That 20% difference must be passed on to clients in the form of increased bids for work. A company with a lower EMR has a competitive advantage because they pay less for insurance.

In the beginning of 2013, the NCCI announced its plan to increase the primary-excess split point over a three-year period. The first stage of the changes will take effect with each state's approved rate and loss cost filing on or after January 1, 2013.

Split point?! What's that?! Well, in the experience rating process each loss is divided into primary and excess categories. Currently, the first \$5,000 of every loss is considered "primary" with everything

over \$5,000 considered an “excess” loss. Primary losses are an indicator of frequency and are counted in full as part of the EMR calculation. Conversely, excess losses are given partial weight in the EMR calculation. This means that primary losses affect the EMR more than excess losses do. Consequently, a company that has a large number of primary losses will have a higher EMR than a company with the same amount of losses split between primary and excess. The NCCI intends to raise the split point between primary and excess losses from \$5,000 to \$15,000 over a three-year period. According to the NCCI, this change is necessary due to claim inflation which has nearly tripled since the last change almost 20 years ago. In order to better reflect the cost of claims, the amount of the loss considered “primary” is being increased.

In the first year, the split point will be increased from \$5,000 to \$10,000 effective with each state’s approved rate/loss cost filing on or after January 1, 2013. (New York State is on target for changes effective October 1, 2013). In year 2, the split point will be increased from \$10,000 to \$13,500 effective with approved filing on or after January 1, 2014. Next, year 3, the split point will be increased from \$13,500 to \$15,000 plus two years of inflation adjustment effective with approved filing on or after January 1, 2015.

The potential for an EMR increase or decrease will depend on whether the company has an above or below average number of losses under the split point. If most of the losses are under \$5,000 there will likely be a decrease in the EMR. If most of the losses exceed \$5,000 there will likely be an increase in the EMR.

There are 38 states that participate in the NCCI plan; all have approved the updated experience rating formula. While the majority of NCCI states will update their rate filings on January 1, 2013, not all will do so. A number of other states have rate filing effective dates later in the year, so depending on an employer’s state of operations, the potential impact may not be realized until after the initial effective date of the changes.

Not only does the EMR have a direct monetary impact on a company through increased insurance premiums, but, similar to OSHA recordable rates, potential and existing customers rely on these numbers to judge a company’s commitment to safety and therefore, serve as an indication of whether that organization will be able to perform the assigned scope of work without jeopardizing the safety and health of the workers. Looking at a company’s safety records through OSHA recordables and EMRs has become a primary consideration to determine if a company is allowed to even bid on work. Depending on the potential customer, an EMR greater than of 1.0 (and in some cases 0.90!) will automatically disqualify a company to participate in the bidding process. This is just one more indication that an organization needs to be diligent with regards to providing an effective safety and health process. Otherwise, a contractor’s ability to ensure a healthy and successful future may be in jeopardy.

**A man cannot be comfortable without his own approval**

Mark Twain