



**Government of the District of Columbia**  
**Department of Insurance, Securities and Banking**

**Stephen C. Taylor**  
Commissioner

**BEFORE THE**  
**INSURANCE COMMISSIONER OF**  
**THE DISTRICT OF COLUMBIA**

Re: Report on Examination – **National Council on Compensation Insurance, Inc.**

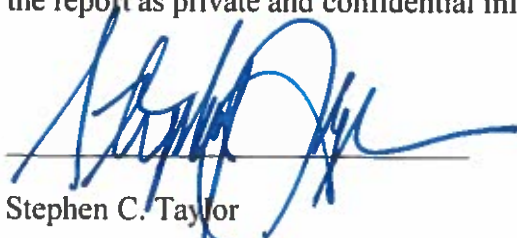
**ORDER**

In accordance with the authority established by D.C. Official Code § 31-2708(a)(1), a Market Conduct Examination of **National Council on Compensation Insurance, Inc.**, as of December 31, 2015 has been conducted by the District of Columbia Department of Insurance, Securities and Banking (“Department”) as a participating jurisdiction through the National Association of Insurance Commissioners’ Advisory Organization Examination Oversight (C) Working Group. The Department accepts the report in lieu of a single jurisdiction examination.

It is hereby ordered on this 2nd day of June 2017, that the attached Market Conduct Examination Report be adopted and filed as an official record of this Department.

Pursuant to D.C. Official Code § 31-1404(d)(1), this Order is considered a final administrative decision and may be appealed.

Pursuant to D.C. Official Code § 31-1404(e)(1), the Department will continue to hold the content of the report as private and confidential information for a period of 10 days from the date of this Order.

  
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Stephen C. Taylor  
Commissioner

**FINAL REPORT OF EXAMINATION**

**As of December 31, 2015**

**NATIONAL COUNCIL ON COMPENSATION INSURANCE, INC.**

**901 Peninsula Corporate Circle  
Boca Raton, Florida 33487**

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April 20, 2017

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Dear Commissioners and Superintendent:

Pursuant to your instructions, an examination has been conducted of the

**NATIONAL COUNCIL ON COMPENSATION INSURANCE, INC.  
901 Peninsula Corporate Circle  
Boca Raton, Florida 33487**

hereinafter referred to as (NCCI). The following report of the findings of this examination is herewith respectfully submitted.

## **I. PURPOSE AND SCOPE OF EXAMINATION**

The Advisory Organization Examination Oversight (C) Working Group of the National Association of Insurance Commissioners (NAIC) initiated a limited scope, targeted multi-state examination (examination) of the business practices of the National Council on Compensation Insurance (NCCI). The scope period of the Examination includes January 1, 2010, through December 31, 2015, (scope) and focused on process and procedural changes since the last examination. The last examination was for the period of January 1, 2006, through December 31, 2009, and was extended to December 31, 2010 for operations (prior examination).

The examination was conducted at the direction and overall management and control of the states of Florida (Managing Lead State), Georgia, Maine and Maryland (Lead States). Representatives from the firm of Risk & Regulatory Consulting, LLC (RRC) or (examiners) were engaged to complete examination procedures. The exam was conducted in accordance to the NAIC Market Regulation Handbook.

RRC personnel participated in this examination in their capacity as examiners. The examination team included actuaries, information technology (IT) specialists and market conduct examiners.

## **II. ORGANIZATION PROFILE**

NCCI Holdings, Inc. provides workers' compensation insurance information, tools, and services, including management of the nation's largest database of workers' compensation insurance information. NCCI operates as a not-for-profit entity, and is guided by a board of directors comprised of representatives of insurers that underwrite workers' compensation risks. NCCI's Board is responsible for establishing corporate strategy and acting as a resource for management on matters of planning and policy.

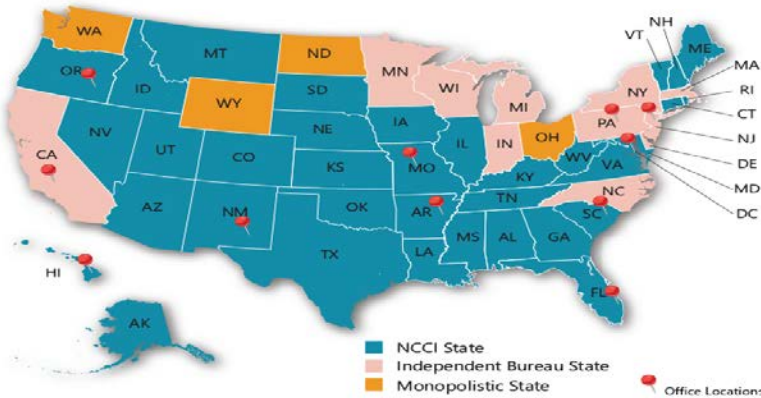
NCCI gathers data, analyzes industry trends, and prepares objective insurance rate and loss cost recommendations. This information is collected from insurers or NCCI-affiliated workers' compensation insurance companies (affiliates), related to policies, claims and overall financial results, which data is then maintained into a data repository. Additionally, NCCI studies workplace injuries and other national and state factors impacting workers' compensation. NCCI also analyzes industry trends, prepares workers' compensation insurance rate recommendations, assists in pricing proposed legislation, and provides a variety of data products to more than 900 insurance companies and 38 state governments. NCCI provides tools for circulars, excess loss factors, loss development exhibits, a manuals library, residual market expiration list, state insight, and training services. In addition, NCCI offers publications/reports, regulatory/legislative activities, underwriting resources, research, and residual market plan and reinsurance pool administration services. NCCI was founded in 1922 and is based in Boca Raton, Florida, with a work force of approximately 900 employees.

NCCI's core services include:

- Rate and advisory loss cost/rate filings;
- Cost analyses of proposed and enacted legislation;
- Residual market management;
- Production of experience ratings;
- Statistical and compliance services; and

- Maintenance of the workers' compensation infrastructure of classifications, rules, plans, and forms.

The following state map identifies states in which NCCI provides services as a licensed rating and/or statistical organization.



Source: NCCI Website.

### III. EXECUTIVE SUMMARY

The primary focus of the examination involved assessing any substantial process and procedural changes since the prior examination, including but not limited to loss cost/rate filings, rules and other regulated activities, operations, management, data receipt and controls, processing editing and compilation procedures, error handling, correspondence with reporting insurers and report submissions to regulators. The Lead States prepared a Target Examination Plan (examination plan) which served as the guide for the examiners in performing the examination. The examination plan identified 17 Market Regulation Handbook (Handbook) Standards which the examiners reviewed for compliance and to determine if there were any changes since the prior examination. Additionally, compliance with previous examination recommendations were also reviewed. The examiners collaborated closely with the Lead States throughout the course of the examination and had ongoing communication with NCCI.

Additionally, the NAIC solicited states and territories to serve as Participating States for the examination. Participating jurisdictions include 37 states and the District of Columbia as shown in the table below.

#### *NCCI Multi-State Examination – Scope: 2010 to 2015 - List of Participating States*

Alabama	Idaho	Montana	Tennessee
Alaska	Illinois	Nebraska	Texas
Arizona	Iowa	Nevada	Utah
Arkansas	Kansas	New Hampshire	Vermont
Colorado	Kentucky	New Mexico	Virginia
Connecticut	Louisiana	Oklahoma	Washington*
District of Columbia	Maine	Oregon	West Virginia
Florida	Maryland	Rhode Island	
Georgia	Mississippi	South Carolina	
Hawaii	Missouri	South Dakota	

\*Washington is a monopolistic state but signed on as a Participating State.  
Independent Bureau States -10 (CA, DE, IN, MA, MI, MN, NC, NJ, NY, PA)  
Monopolistic States-4 (OH, ND, WY, WA)

The examination was called on August 16, 2016, and NCCI was responsive throughout. All onsite work was completed at NCCI's corporate offices in Boca Raton, Florida. Field work was concluded on January 13, 2017.

#### **IV. GENERAL CONCLUSIONS AND OBSERVATIONS**

Based on the work completed, the examiners concluded the following. These matters are detailed further in the report under Examination Standards:

- The examiners determined that NCCI's processes and procedures related to its regulated operations adequately meet the Standards reviewed.
- NCCI's Internal Audit (IA) function is adequate and meets the needs of NCCI.
- The actuarial examiners concluded the following:
  - NCCI has credentialed and experienced actuaries.
  - NCCI has a robust process for the review of loss cost/rate filings including data gathering, analysis and peer review.
- The examiners confirmed that in addition to routine changes NCCI implemented during the scope three significant changes to its actuarial procedures:
  - Changes to three parameters used in the Experience Rating Plan (eligibility criteria, split point, and maximum debit);
  - Changes to NCCI's methodology for deriving excess loss factors, as published in NCCI's Retrospective Rating Plan; and
  - Changes to the NCCI's Internal Rate of Return Model, which is used by NCCI to derive profit provisions used in rate filings.

Each of these changes is discussed in further detail in this report.

- NCCI has an experienced team of IT professionals.
- NCCI's commitment to its IT processes has resulted in a stable, consistent and effective environment.
- IT examiners determined NCCI has in place strong IT General Controls (ITGC) that are effective on an overall basis.

#### **V. EXAMINATION METHODOLOGY**

The examiners primarily relied on the review of documentation and the testing of information maintained by NCCI. Also, the examiners were provided presentations by NCCI, which gave an overview of NCCI's operations. The examination included actuarial, IT and market conduct (MC) professionals, and in some instances, examiners from different functional areas participated in the review and investigation of a particular Standard, e.g., Standard 4 – Operations, Management and Governance.

RRC's actuarial examiners' work included reviewing NCCI's work product related to loss cost/rate filings (filings), with specific emphasis regarding NCCI's assumptions in preparing the filings as well as the completeness and accuracy of the information. The actuarial examiners also participated with RRC's IT examiners in reviewing certain areas of the examination, including but not limited to changes to NCCI's Experience Rating Plan. The actuarial examiners conducted interviews of NCCI's key actuarial resources, including the Chief Actuary. Similar to the IT work, the actuarial examiners also reviewed and discussed NCCI's IA reports specific to the scope.

Examiners' work focused primarily on addressing Standards from the examination plan related to residual market - administration, residual markets – reinsurance pool, anti-competitive practices, and NCCI's practices and procedures related to inspection services and classifications. Examiners accomplished their work by reviewing various documentation, including NCCI's practices and procedures, participating in interviews and leveraging the work of the actuarial and IT examiners to complete the review of specific Standards.

The IT examination of an advisory organization focuses on the critically important management of data and the controls in place to protect the data and information received from their members and reported to regulators. Consequently, the IT examiners approach and methodology was planned to gain a comprehensive understanding of NCCI's IT and data infrastructure operations. This included the IT examiners' review of the work of NCCI's IA group to determine if the quality and objectivity of the work was sufficient to place reliance on the IA's work. In addition, independent procedures were performed to enhance the IT examiners' understanding of certain controls. Further, IT examiners' procedures included a focus on gaining an understanding of the design, implementation and operating effectiveness of the NCCI's IT processes and associated IT General Controls.

RRC reviewed all IT-related information and determined that NCCI appeared to have taken a top-down approach to risk identification, control development and documentation. Supporting documentation and information was provided by NCCI, including network diagrams, policies and other related documents.

The specific systems and applications focused upon during the IT review included the following:

- Submission Tracking System (STS);
- Data Resource Center (DRC);
- Experience Rating System (ERC);
- Class Ratemaking System (CRS);
- Financial Data Collection Tool (FDC); and
- Aggregate Ratemaking (ARO).

The IT examiners also conducted walkthroughs of these systems and applications with NCCI's IT and data resources staff to gain a comprehensive understanding of their scope and purpose to NCCI. Additionally, interviews and process walkthroughs with representatives of NCCI were also conducted. Targeted testing was performed consistent with examination processes and sampling methodologies prescribed in the Handbook.



The IT examiners leveraged work reported in relevant audits and, following an appropriate level of validating the information, concluded:

- The scope of the work performed was appropriate;
- The sampling procedures used were appropriate;
- Test plans are designed to adequately test the control and tests are executed in accordance with the test plans;
- The work was properly documented, including evidence of supervision and review; and
- The conclusions reached were consistent with the results of the work performed.

The IT examiner was also able to leverage other work and projects, such as the Experience Rating Plan Project, to assist in addressing some of the Standards associated with the examination plan. This information is detailed in the individual Standards addressed by the IT examiners.

## **VI. EXAMINATION RESULTS**

### **Prior Examination Observations and Recommendations Follow-up**

In addition to addressing the examination plan, the examiners reviewed observations documented during the prior examination, which was a key aspect of the scope. Although the prior observations and recommendations include two non-IT related matters, the observations were substantially related to NCCI's IT and data related infrastructure. As such, RRC's IT examiners reviewed the observations and performed the follow-up to determine NCCI's response to the observations and the current status relative to NCCI's IT environment.

The information gathered and documented under "Current Status" in the table below confirms that NCCI has effectively addressed each of the observations noted in the prior examination.

<b>Issue(s) Noted</b>	<b>Recommendation or Observation from Prior Examination</b>	<b>Current Status</b>
<p>NCCI does not use the Flesch test or other readability tests/tools. Based on a review of state statutes, some states require the use of the Flesch test or some comparable test.</p>	<p>It is recommended that NCCI comply with the readability requirements as set forth in applicable state statutes.</p>	<p>At the conclusion of the prior examination, NCCI responded to the examiners recommendation by noting: "NCCI believes that its plain language approach promotes the readability of its forms and rules and that this approach underlies the forms and endorsements which have been approved by the respective state regulators. NCCI will review with the respective state regulators all instances where statutory requirements may prescribe specific readability tests and will take appropriate action."</p>

Issue(s) Noted	Recommendation or Observation from Prior Examination	Current Status
		<p>In discussing this matter with NCCI for the examination, the examiners confirmed the following:</p> <ol style="list-style-type: none"> <li>1. NCCI’s plain language approach promotes the readability of its forms and rules and this approach underlies the forms and endorsements which have been approved by the respective state regulators.</li> <li>2. NCCI has not made any changes to its readability requirements and continues to comply with those requirements as set forth in applicable state statutes.</li> </ol>
<p>It is noted that a 2008 internal audit of accounts payable included a review of 15 employee reimbursement requests. There were no significant findings related to these requests. The internal audit function has not performed an audit of the travel and entertainment expenses for proper review, authorization and compliance with related policies and procedures since 2008.</p>	<p>It is recommended that NCCI’s internal auditor perform an audit of travel and entertainment expenses to determine if the expenses are reviewed, authorized and comply with related policies and procedures, that it periodically perform subsequent audits of the travel and entertainment expenses and that it report its finding to the board of directors.</p>	<p>In 2013, NCCI performed a ground up risk assessment to set the 2013 plan year in place. Given the risk profile of “Employee Expenses” being low relative to its peers, a cycle of every four or five years was agreed to by the Senior team &amp; CEO at the time; as recommended by Internal Audit. During 2015, a dedicated Employee Expense audit was performed and completed by December 8, 2015. It was presented to the Audit Committee in January 2016. The audit received a “good.”</p>
<p>Access to the data center is by badge access, which is a single factor authentication. The recommended control level is for two-factor authentication.</p>	<p>It is suggested that NCCI consider implementing an additional factor of authentication for access to the data center.</p>	<p>Datacenter access is restricted through the use of key cards and a PIN code. Access to the datacenter is restricted to infrastructure personnel and limited additional resources (security, etc.).</p>

Issue(s) Noted	Recommendation or Observation from Prior Examination	Current Status
<p>The use of sign-in sheets for visitors to the data center provides a record of who has gained access to this sensitive area. There are cameras located at strategic locations, which is a mitigating control. However, a sign-in sheet would provide a record that can easily be reviewed and maintained.</p>	<p>It is suggested that a sign-in sheet be provided and sign-ins be required for all visitors to the computer room.</p>	<p>During the Examiner's datacenter tour on September 16, 2016, the IT examination team observed various controls in use for the datacenter including the sign in sheet for visitors to the datacenter.</p>
<p>The security system utilized at the company has the ability to sound an alarm when specific doors are open for longer than a specified period of time. This feature is enabled for loading dock doors but is not enabled for the doors to the computer room.</p>	<p>It is suggested that the alarm feature be enabled on the security system to alert the guards if the computer room door is open for more than a specified time.</p>	<p>During the datacenter tour on September 16, 2016, the IT examination team confirmed the operation of the datacenter doors and noted that the alarms for the computer room door activate security response.</p>
<p>Backups are created of the security data and systems but are not taken offsite for storage.</p>	<p>It is suggested that NCCI consider requiring offsite storage of the security systems and backup to be recovered in the event of a fire in the security computer room or other catastrophic event.</p>	<p>Data backups are performed on a daily basis to a virtual tape library. The backups are performed to the local library in the Boca Raton datacenter and then replicated to the disaster recovery (DR) site.</p>
<p>Due to technological limitations with other NCCI systems, complex passwords are not enforced in Active Directory. NCCI currently requires more</p>	<p>It is suggested that the technological limitations be resolved to accommodate the enforcement of more complex passwords.</p>	<p>Users authenticate to the Windows Active Directory which grants them access to the network and the associated resources. Users are required to provide a unique username and complex password in order to authenticate.</p>

Issue(s) Noted	Recommendation or Observation from Prior Examination	Current Status
frequent password changes to compensate for weak passwords.		
Evidence of consistent and complete documentation of security incidents or responses to such incidents to support legal action was not observed.	It is suggested that NCCI develop consistent and complete documentation of security incidents to support follow-up activity and/or legal action.	NCCI employs a “defense in depth” strategy to protect its network. An Incident Response plan has been developed to address cybersecurity threats.
Internal audit findings currently drop off the list of open items when they are addressed. Having a list of resolved items with the date that each finding is addressed; including a brief summary of the resolution approach would be helpful for verification that all findings are resolved in a timely manner.	It is suggested that NCCI implement a process to easily identify the resolution to all internal audits findings.	During the course of the examination, the examiners reviewed Internal Audit reports, which included details concerning testing, findings and NCCI’s remediation efforts as may be necessary. Examiners observed that Internal Audit findings and related recommendations are reported quarterly to the Audit Committee for tracking and to aid in audit planning for subsequent audits.

**VII. REVIEW OF EXAMINATION STANDARDS AND RESULTS**

The examiners reviewed and tested where applicable, the Standards included in the examination plan and Chapter 25 of the Handbook. Additionally, aspects of Appendix F of Chapter 25 of the Handbook were also referenced during the Examination.

**a. Operations, Management and Governance**

**Standard 1** - The advisory organization has implemented written policies and procedures to prevent anti-competitive practices in the insurance marketplace, as related to the advisory organization's services and communications to insurers.

**Results: Pass**

**Observations:** The examiners confirmed through the review of documentation provided by NCCI that since the prior examination, NCCI continues to maintain anti-competitive policies

and procedures, which are updated where necessary, and to ensure compliance with antitrust laws and requirements.

NCCI has in place Antitrust Compliance Guidelines for both employees and its Board of Directors/Committees (Directors), both of which were updated in 2015 and again in 2016, respectively. On an annual basis, employees and Directors are required to sign annual acknowledgements of NCCI's Antitrust Compliance Guidelines. Directors are also required to sign an acknowledgement of the Code of Business Conduct and Ethics of Directors, which were updated in 2016. Further, NCCI provides regular training on antitrust compliance for all employees. The last compliance trainings were completed in 2011 and 2015.

*Based on the review of NCCI's documentation, as well as interviews conducted with NCCI representatives, the examiners have concluded that the advisory organization has implemented written policies and procedures to prevent anti-competitive practices in the insurance marketplace, as related to the advisory organization's services and communications to insurers.*

**Recommendations: None**

**Standard 2** - The advisory organization uses sound actuarial principles for the development of prospective loss costs.

**Results: Pass**

**Observations:** The actuarial examiners performed a procedural review and testing to address the scope of Standard 2, which included a review of a sample of loss cost/rate filings. Each sample was tested against certain actuarial guidelines set forth in the Actuarial Standards of Practice (ASOP), and identified below for reference:

- ASOP #12: Risk Classification (*Please see comment below*);
- ASOP #13: Trending Procedures in Property/Casualty Insurance;
- ASOP #23: Data Quality;
- ASOP #25: Credibility Procedures;
- ASOP #29: Expense Provisions in Property/Casualty Insurance Ratemaking;
- ASOP #30: Treatment of Profit and Contingency Provisions and the Cost of Capital in Property/Casualty Insurance Ratemaking;
- ASOP #38: Using Models Outside the Actuary's Area of Expertise (Property and Casualty);
- ASOP #39: Treatment of Catastrophe Losses in Property/Casualty Ratemaking; and
- ASOP #41: Actuarial Communications.

The actuarial examiners did not directly review NCCI's adherence to ASOP #12, Risk Classification (for all practice areas), as these filings were only tangentially cited in the loss cost/rate filing sample. NCCI confirmed to the examiners the following: "*they (NCCI) adhere to ASOP (#) 12 during the ratemaking process. It is imperative to consider the elements outlined in ASOP (#) 12 in order for NCCI to derive rates that are reasonable for individual risks.*" NCCI

also provided a brief synopsis of one of its classification filing to further support its adherence to ASOP #12.

The examiners' testing included a sample of calculations performed by NCCI, which were used to support the derivation of certain loss costs/rate including:

- Loss Development Factors;
- Premium Development Factors;
- Premium On-level Factors;
- Trend Factors;
- Benefit Level Changes;
- Credibility Procedures;
- Loss Adjustment Expenses;
- Classification Relativity Analysis; and
- Use of Models.

Using Automated Command Language, the examiners selected a sample of filings from a list of filings provided by NCCI for the scope. The following table identifies the specific 11 separate experience loss cost/rate filings tested.

Sample	State	Filing Designation
LC and Rate Filing 01	Kansas	KS-2010-04
LC Filing 02	Montana	MT-2012-01
Rate Filing 03	Illinois	IL-2012-02
Rate Filing 04	Arizona	AZ-2013-02
LC and Rates Filing 05	New Hampshire	NH-2013-01
LC Filing 06	Oklahoma	OK-2013-01
Rate Filing 07	Georgia	GA-2014-05
LC Filing 08	Hawaii	HI-2014-01
LC and Rate Filing 09	Illinois	IL-2014-03
LC Filing 10	Oklahoma	OK-2014-02
LC and Rate Filing 11	Virginia	VA-2014-01

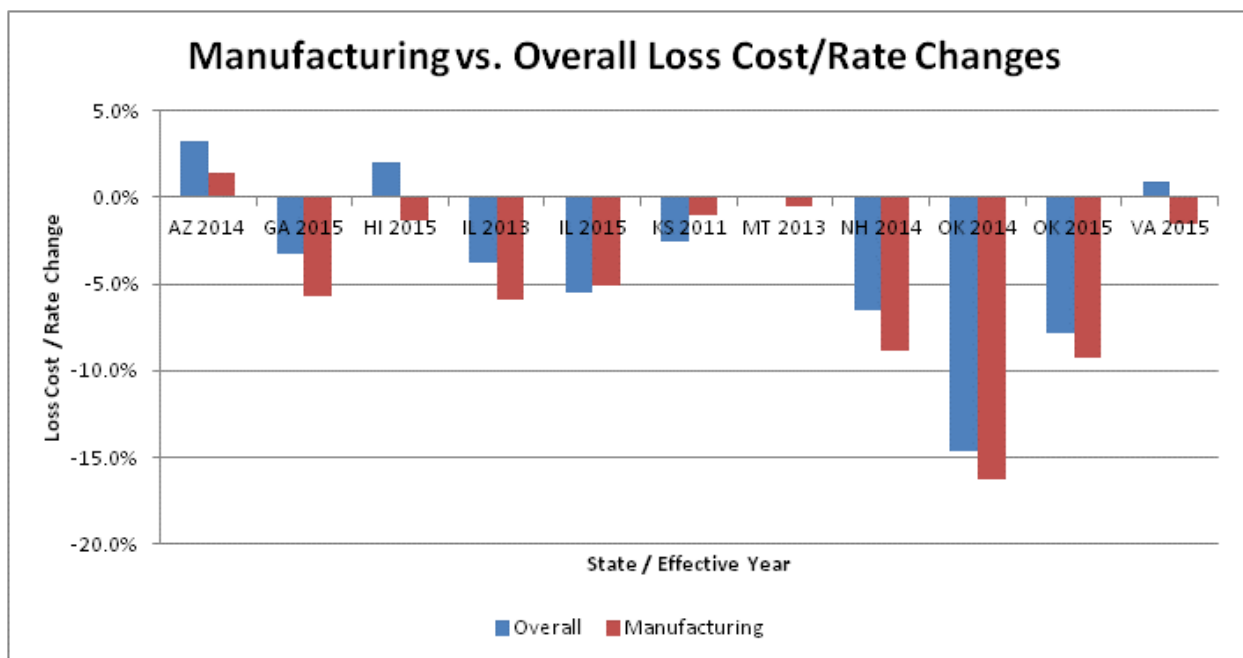
The review of the loss cost/rate filings included specific attributes, which are included below for reference.

- Overall change by industry group as defined by NCCI;
  - Manufacturers;
  - Contractors;
  - Officer & Clerical;
  - Goods & Services;
  - Miscellaneous;
- Key actuarial assumptions underlying loss cost/rate change; and
- Key expense assumptions underlying rate change.

The actuarial examiner’s impressions for each of the attributes, based on the summaries of the sample for the scope, are discussed below.

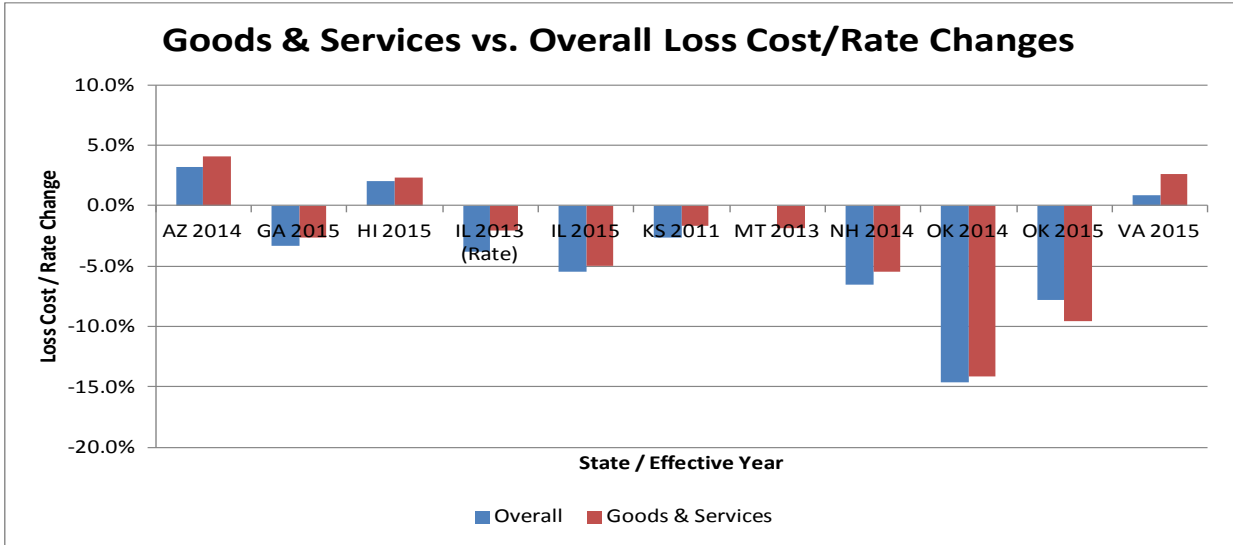
*Overall Loss Cost/Rate Change and Change by Industry Group*

The chart below illustrates the overall change in the state along with the change in the manufacturing group.



There is a range of overall loss cost/rate changes. Of the 11 filings reviewed, there are three increases, seven decreases and one filing with no change (Montana 2013). The changes for manufacturers are less than the overall change in the state in nine of 11 cases (with the exception of the Kansas 2011 and Illinois 2015 filings).

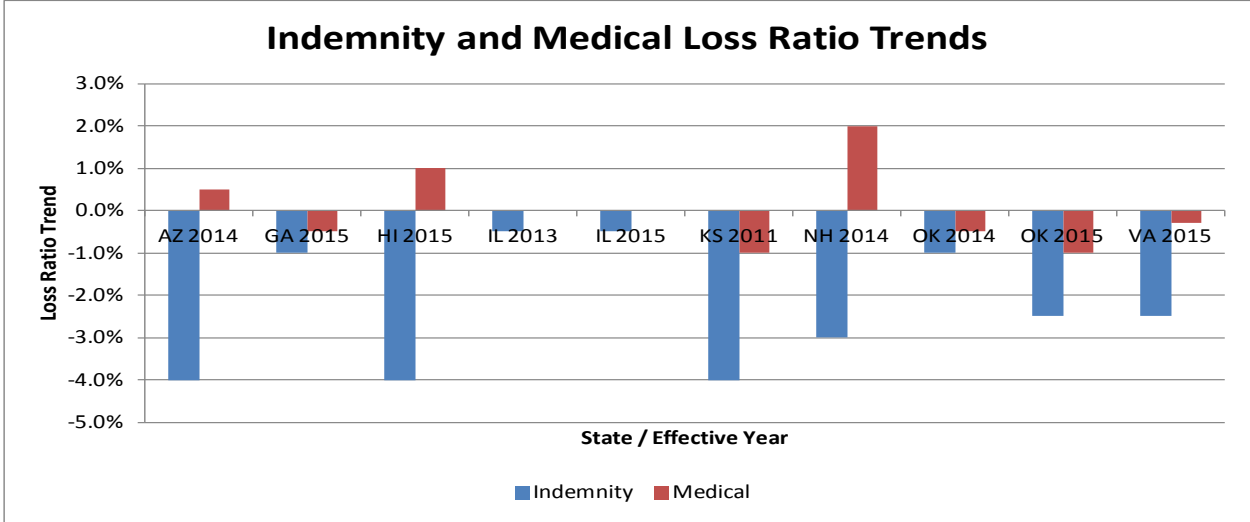
The chart below illustrates the overall change in the state along with the change in the Goods & Services group.



In this case, nine of the 11 states have a higher change for the Goods & Services group as compared to the overall change for the state. Only Montana 2013 and Oklahoma 2015 have lower changes for Goods & Services.

**Key Assumptions Underlying Loss Cost/Rate Change**

One of the most important assumptions underlying the loss cost/rate change is the trend in indemnity and medical costs. The chart below illustrates NCCI’s trend assumptions in the filings reviewed (excluding Montana 2013, which did not include trend assumptions):



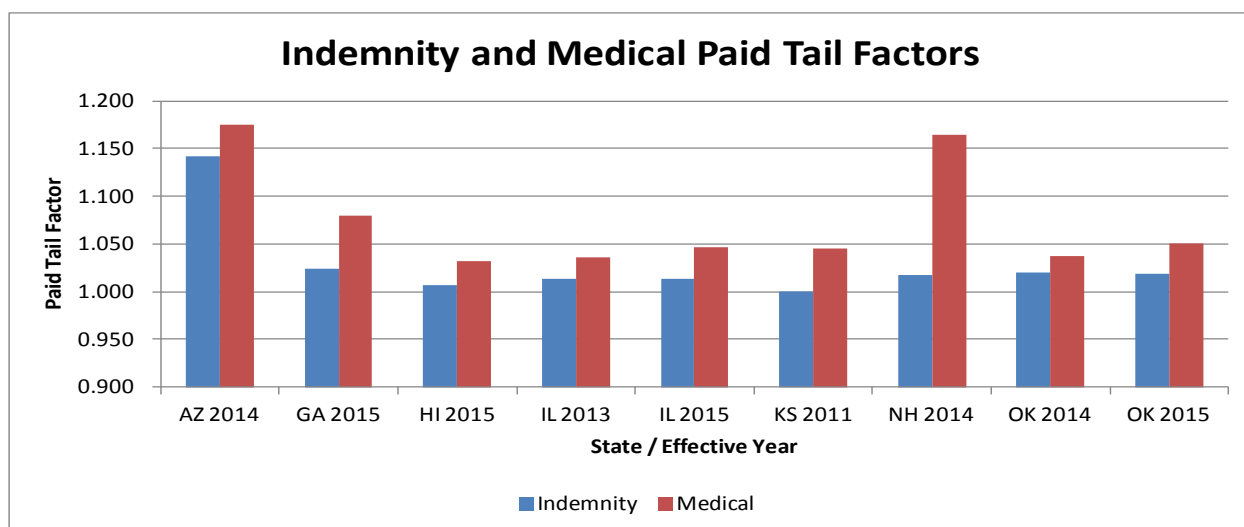
Medical trend is higher than indemnity trend in all cases. This is expected, given the fact that the key driver of medical trend, medical inflation, has been in excess of the key driver of indemnity trend, wage inflation. For clarification, indemnity benefits are for lost wages as opposed to medical benefits, as usually there is a link between the indemnity benefits and the average state weekly wage.



Trend assumptions are contained within a relatively narrow band, with indemnity trend varying between -4% and 0%, and medical trend varying between -1% and +2%. Because of the fact that trend has a significant impact on the indications, we see this relative consistency in trend factors as a positive aspect of NCCI filings, and an indication that the workers' compensation system is functioning smoothly.

**Loss Development Tail Factors**

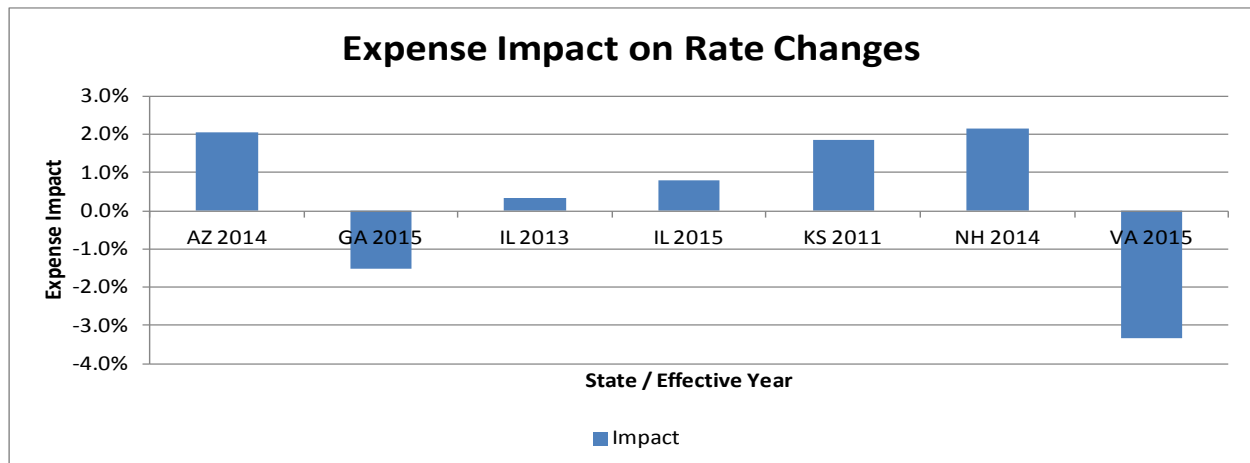
Due to the fact that workers' compensation is a very long tail line, loss development factors are necessary even for periods beyond which data is shown. These factors are termed "tail" factors. Tail factors are another important element of the actuarial analysis for workers' compensation. The chart below illustrates NCCI's tail factor selections for paid indemnity and medical losses, after nineteen years. Montana 2013 and Virginia 2015 are not shown, as these filings did not include paid tail factors.



Medical paid tail factors are larger than indemnity, since medical losses tend to pay over a longer period than indemnity. The chart also reflects the wide range of medical paid tail factors, ranging from approximately 1.030 in Hawaii 2015 and Illinois 2013 to 1.170 in Arizona 2014 and New Hampshire 2014. Larger tail factors are associated with greater uncertainty in ultimate costs to the workers' compensation system. The disparity in medical paid tail factors across the filings reviewed is an indication that some states may have more effective measures for controlling medical costs than others.

**Expense Assumptions**

The chart below illustrates the impact of changes in NCCI's expense assumptions on the overall rate changes for the reviewed filings that include rate changes.



The chart reflects changes in the provision for expenses for the filings reviewed have been contained within a fairly narrow band, ranging from approximately -3% to +2%. This is a positive characteristic, as changes in expenses unrelated to losses would not be expected to drive significant changes in the rates charged for workers' compensation insurance.

**Other Changes During the Examination Period:**

The examiners also reviewed the following additional changes NCCI utilized in producing loss cost/rate:

**A. Internal Rate of Return Model**

The examiners reviewed the study of the internal rate of return model and interviewed the economist who led the study. The motivation of the study was to determine more consistent ways of analyzing the cost of capital and the return on investment, which are core inputs to the model. The cost of capital and the return on investment are really related questions regarding forward looking market rates of return. The model itself was not changed, but rather the manner of analyzing inputs to the model. The results of these changes produce profit and contingency loads that are generally lower than those of the previous version of the model. This is due to the moderating of the bias with respect to the linkage of the cost of capital versus the return on investment and the low interest rate environment.

*Based on the actuarial examiners' review, these changes appear reasonable.*

**B. Establishment of the Thresholds for Escalating Errors**

The examiners reviewed material related to three instances which exceeded the threshold for escalating errors occurring during the scope. The actuarial examiners also conducted an interview with the NCCI Legislative Practice Leader, about the escalation process for communication of errors when they may occur. When an issue rises to the level of materiality, NCCI's Chief Actuary discusses the matter with the "Triage Group", which is a group of senior staff members, to decide on the best course of action. This process has been in effect since 2005. The materiality standards, which were agreed to at the NAIC by the states, are as follows:

- +/- 1% impact on the statewide loss cost, or
- +/- 10% impact on a single class, or
- More than 20% of the classes are impacted by +/-5%.

If an issue does occur, NCCI's escalation process requires affiliates to be informed on a timely basis, and following the agreement with the affected state regulators, take appropriate remedial action.

Since the prior examination, the examiners confirmed with NCCI that three errors occurred, which were identified internally, communicated to affiliates and regulators and remediated successfully, consistent with NCCI's escalation process. These errors are discussed in greater detail as follows:

- **National Pure Premium (2015)**

A data error was discovered during a research project related to small classes. Over time, some classes are discontinued, but may not be discontinued in all states. NCCI actuarial staff found that in some of these cases, NCCI incorrectly aggregated exposure related to the discontinued classes for all states. Losses for the discontinued classes were correctly aggregated for the states in which the class was still active (not all states). This led to a mismatch in exposure and loss with the exposure overstated. In turn, the loss costs associated with the classes for the states in which the classes were still active were understated. Once NCCI recognized this error, it communicated the issue to the states affected via phone calls and communicated with all states by letter. The error was corrected and loss costs for these classes rose to the appropriate level in subsequent loss cost/rate filings subject to caps on the amount by which the loss cost for a class can increase each year.

In addition, NCCI's IA was asked to validate the correction, and also to ensure that the issue could not arise in the future. IA validated the correction by independently extracting and testing the relevant data. IA also tested a new control that the actuarial group created to prevent the error from occurring in the future. This control was a manual check included in a spreadsheet used to compute the national pure premiums. NCCI's IA validated the issue had been properly resolved. The actuarial examiners agreed with IA's conclusions based on the review.

- **Kansas Assigned Risk Expense Loading (2011)**

Assigned risk rate filings include a provision for expenses. In the Kansas 2011, assigned risk filing, NCCI discovered that it had inadvertently "double-counted" two components of the expenses. These components included the Administrative Fund Assessment and the Second Injury Fund Assessment, which are loss based assessments. Essentially, these are "pass through" items. As a result, the provision for expenses was overstated by 1.07%. The data used for these expenses is not a calculation but information provided by NCCI's Residual Market Plan Administration group. In order to prevent this error from occurring in the future, NCCI's Actuarial Department implemented an enhanced validation process. This process is described below:

NCCI Reserving Team annually creates a Residual Market Expense Exhibit for the Aggregate Ratemaking Team to use in the preparation of filings for those jurisdictions

in which assigned risk rates are filed. This exhibit separately provides the NCCI Plan Administration Expense, National Pool Administration Expense, and Servicing Carrier Other Expense categories. Each year before the Exhibit is prepared, NCCI's Reserving Team requests a list of all pass-through expenses from the Residual Market Finance Department. The Reserving Team then separately identifies and excludes all pass-through-related expenses from the exhibit's Servicing Carrier Other Expense category. The Residual Market Expense Exhibit is thoroughly quality reviewed by two members of the Reserving Team prior to it being provided to the Aggregate Ratemaking Team. This enhanced process ensures the expenses are corrected identified as a pass-through category.

- **Arkansas Excess Loss Pure Premium Factors (2013)**

Excess loss pure premiums factors (ELPPFs) measure the percentage of losses expected to be above particular limits. A manual effort to enter these factors in one state, resulted in errors for 26 class codes. The ELPPFs were misstated by +/-0.001 for 24 class codes and +/-0.002 for two additional class codes. Though the impacts are small, NCCI refiled with the corrected ELPPFs after discovering the error.

### **C. Revisions to Retrospective Rating Plan**

The examiners also identified a change to the Retrospective Rating Plan (RRP). The underlying RRP is scheduled to be reviewed once every ten years, although the values in the RRP are updated annually to reflect changing economic conditions. A new RRP was implemented at the end of 2014. NCCI's focus was on revising the methodology of calculating the ELPPFs. While the old methodology was based on empirical state data, the revised methodology focuses on countrywide data using five years of unit statistical plan data at 6<sup>th</sup>, 7<sup>th</sup>, 8<sup>th</sup>, 9<sup>th</sup> and 10<sup>th</sup> evaluations and modeling the data using two lognormal curves. The purpose is to produce Excess Loss Factors (ELFs) that are more stable and consistent over time. Once the countrywide curves were established, modifications were made to adjust up or down for state-specific conditions. Each state curve maintains the shape of countrywide curve.

In order to communicate and gather consensus for the new process, quarterly presentations were made to the Individual Risk Rating Working Group (IRRWG) which is a subgroup of NCCI's Actuarial Committee. IRRWG members include affiliate actuaries that, as explained to the examiners by NCCI, "have a more technical focus." In addition, a peer review was performed by an internal NCCI actuary. NCCI performed an analysis to compare the results of the revised procedure, and which was completed for each state. States that indicated large changes were examined to make sure that the results were reasonable.

The examiners reviewed NCCI's Filing Memorandum, ITEM R-1408 as well as the ELFs Manual dated January 1, 2015. In addition, the examiners participated in a conference call describing the changes to the retrospective rating plan, which was led by an NCCI actuary. The NCCI actuary led the research initiative for the revised plan and was also the chair of the IRRWG. The examiners also reviewed the relevant agendas and minutes for the IRRWG quarterly meetings.

*Based on this review the actuarial examiners believe that these changes were reasonable. Further, based on the review and testing of the sample of NCCI's filings as well as a review of the changes to the retrospective rating plan discussed above, the examiners concluded that NCCI uses sound actuarial principles for the development of prospective loss costs.*

**Recommendations: None**

<b>Standard 4</b> - Experience rating factors are developed in a correct and timely manner.
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**Results: Pass**

**Observations:** Members of RRC's actuarial and IT teams investigated this Standard and learned that NCCI's data quality approach starts with the recommended Data Quality best practices workflow which is intended to improve the overall timeliness and quality of data reported. NCCI provides a Data Reports Guide that is accessible on the Data Reporting page on NCCI's website. NCCI also provides a guidebook for each of the data types, which details the data elements required for a particular data type and the edits which will be performed by NCCI in order to confirm the integrity of the data used to develop the experience rating factors. NCCI's editing process is a series of front-end quality checks performed by NCCI, which verifies the validity, accuracy, and completeness of the data submitted by data providers. Editing is critical to ensuring the submitted data is consistent with reporting requirements and meets quality standards. In the Data Collection and Handling section, the IT examiners reviewed the edit matrix for each data type and determined that the edits were appropriate based on the edits listed in the Statistical Handbook of Data Available to Insurance Regulators.

In addressing this Standard from an IT perspective, the examiners confirmed that an updated version of the Experience Rating System (ERS) had been implemented which represented a major change since the prior examination. The IT examiners determined that testing for the ERS had been performed by a third party (PricewaterhouseCoopers, LLP (PwC) and an investigation into the background, goals and objectives and testing of PwC's work (Project) would be relevant to the Examination. Consequently, the IT examiners reviewed copies of the PwC's work papers, which included a PwC's report (Report) which described the procedures performed by PwC prior to NCCI's implementing the ERS application.

Based on the review of the Report, the IT examiner noted that the overall objective of the Project was to perform an assessment of the ERS including the data migration from the current legacy (mainframe) system to the new system and the functionality of the new application.

The IT examiner noted that during the Project, PwC's performed functional testing, the objective of which was to assess the in-scope components of the ERS for the selected business requirements and corresponding functionality in the new ERS. PwC's work involved five functional areas, including: Rating Calculation, Rating Effective Date, Edits, Triggers, and Distribution. Three findings were identified by the Functional

Testing, which were resolved prior to the ERS “going live.” Based on the review of the work performed by PwC and follow-up performed by the IT examiners to confirm that any findings were resolved, the work was determined to be relevant to this review and adequate to confirm that the functionality of the ERS is appropriate and the information provided by the system is accurate.

*Based on the edits noted in the matrices and the review of the work for the Experience Rating project, it was confirmed that NCCI uses data integrity checks to ensure the quality of the data upon which experience rating factors are based.*

**Recommendations: None**

### **Actuarial Review of Experience Rating Plan**

In addition to the IT examiners’ review, members of the actuarial examiner team also reviewed this Standard, specifically with regard to the changes to NCCI’s Experience Rating Plan (ERP) occurring during the Scope. As a result, several revisions were confirmed, including the following:

#### **Premium Eligibility**

- Premium eligibility refers to the threshold to qualify for the ERP based on premium for a given employer. The existing methodology for determining premium eligibility had been unchanged for approximately twenty years. This had the effect of allowing an increasing number of employers to be eligible for experience rating over time as a result of inflation, due to the fact that the threshold was a fixed dollar amount. Smaller employers are not considered eligible for experience rating since their losses are unpredictable and should not impact the premium charged for this risk.

The revised methodology defines the eligibility threshold as a function of the average weekly wage. This statistic is produced by the U.S. Department of Labor. The use of this statistic will allow for the value of the threshold to be indexed on an annual basis. The revised premium eligibility threshold is due to be implemented starting on January 1, 2017.

- **Primary/Excess Split Point**

The Split Point in the ERP determines which portions of an employer’s historical losses are considered primary versus excess. The distinction is an important component of the plan, as the primary losses are given more credibility than excess losses in determining the experience rating modification factor. Over time inflation increases the size of losses and therefore the split point of primary versus excess should increase as well. NCCI conducted diagnostic tests (quintile tests) to demonstrate that there is improvement in the performance of the ERP by revising the split point. The split point is scheduled to increase in stages over a multi-year period.



- **Revised Maximum Debit Formula**

Formerly, under the ERP, experience rate modifications were subject to a risk specific cap based on the following formula:  $1+[0.00005 \times (E+2/G)]$ , where “E” refers to the expected losses for an individual risk, and the value of “G” is the statewide average cost of a claim per \$1,000. This formula has a minimum value of one (1), when E is zero. The revised formula is  $1.1+ (.0004 \times E/G)$ . This new formula has a minimum of 1.1 rather than 1. A maximum debit that approached 10% is more reasonable than a 0% debit. In addition, the new formula more fully accounts for differences across states in claim severities, such that two identical employers in two different states would be subject to the same experience rating modification cap because the expected losses would be directly correlated with the state average severity. We concluded that the changes to the maximum debit formula appear reasonable.

The actuarial examiners reviewed NCCI’s countrywide circular CIF-2011-14, dated August 3, 2011, announcing the change to the Experience Rating Plan Primary/Excess Split Point Value and Maximum Debit Modification Formula, as well as the NCCI countrywide circular CIF-2015-61 dated December 7, 2015 announcing the establishment of a methodology to calculate experience rating premium eligibility amounts. The examiners also interviewed an NCCI actuary to discuss these topics. It is important to note that the basic formula for the ERP itself is not being modified.

*The actuarial examiners believe that based on the review of the ERP and the changes discussed above, the Organization develops experienced rating factors in a correct and timely manner.*

<p><b>Standard 5</b> - The advisory organization performs thorough and meaningful inspections and research when required for individual insured rating classification.</p>
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**Results: Pass**

**Observations:** NCCI’s Inspections Services are supported by a 25-page comprehensive guideline document, which includes workflows. The document is identified as NCCI’s *Classification Quality Assurance (CQA) – CQA 03.013 – Inspector Procedures (Procedures)*. The procedures were developed to document the NCCI’s requirements related to performing onsite inspections, specifically providing guidance to NCCI’s inspectors in conducting any type of physical inspections. The inspection process is critically important in supporting NCCI’s classification process. Ensuring classifications are correct and accurately reflect a risk profile is the foundation in ensuring the correct determination of rates, or premiums, for filings.

NCCI’s procedures address both CQA/Selected as well as Special Inspections. Selected Inspections are defined as physical classification inspections performed as part of the Selected Inspection Program and are applicable only in Florida. Special Inspections are those, which have been requested by an employer, agent, insurance carrier, regulator, the NAIC or another system participant.

NCCI's inspection process is supported by an automated system identified as the Regulatory Assurance Information System (RAIS). This system affords access for online classification inspections using a specific online form. The form requires relevant information to be entered including identifying the type of inspection being requested (*Selected or Special*). The inspector is required to enter certain information into RAIS as part of the inspection request process. For Special Inspections, a Regulatory Services Coordinator reviews the requests and will address any missing information with the requestor. All inspection documentation is entered and maintained into an Inspection Project Folder and added to the Inspector's Documentum Inbox.

Inspection timelines are also established in RAIS and include the following:

- A minimum of two good faith attempts to schedule an inspection appointment must be made within 30 days of the initial inspector assignment.
- Within ten days of receiving an inspection assignment, inspectors must make one good faith effort by mail to schedule an appointment. If an inspection appointment is not scheduled on the initial attempt, the inspector must make a second attempt within 30 days of the assignment by telephone.
- If an appointment is not successfully scheduled after the second attempt, the inspector may close the assignment and notify the Regulatory Services Coordinator or Inspection Team Leader at which time the Inspector and Team Leader will agree on next steps, which are enumerated in the CQA.
- Inspection reports should be completed within 11 days of completing the on-site inspection.
- Inspections should *be completed* within 55 days of assignment.

Similar timelines are established for Special Inspections; however, inspection reports should be completed within nine days of an assignment and the inspection should be fully completed within 47 days.

Inspections are monitored and managed through the use of Microsoft Outlook and a Work in Process Inventory.

The above is a general summary of the inspection assignment process; however, the procedures include guidance related to special instructions, inspection preparation, on-site gathering requirements and documentation requirements.

Based on the examiners' review of the procedures and related documentation, the examiners determined that NCCI's Inspection process is thorough and appropriate. NCCI's practices and procedures are maintained and kept updated as necessary, as evidenced by NCCI's confirmation that there were changes regarding the procedures during the scope. However, the changes are minor in nature and did not affect NCCI's core inspection process. The specific changes include the following:



Date of Change	Procedures Section	Change
07/01/2014	All	Revised and reformatted document
05/28/2015	1.4.2.1, 1.4.3, 1.4.4.2, 1.4.7.4, 1.4.7.8, 1.4.10.2	Clarification wording/grammar, minor revisions related to appt. letter automation, comment for additional information in the email notification
08/25/15	All	Minor clarifications to wording/grammar, format, order

Source: The NCCI Procedure Guidelines – Revision date 08/24/2015

*Based on the examiners review of NCCI’s documentation and related information related to their classification services, the examiners concluded that NCCI performs thorough and meaningful inspections and research when required for individual insured rating classifications.*

**Recommendations: None**

**Standard 9** - The advisory organization uses objective and established procedures when administering residual market or pool assessments.

**Results: Pass**

**Observations:** NCCI does not perform pool assessments but rather, NCCI’s process involves the allocation and distribution of financial results related to residual market policies, reinsured through a pooling mechanism by participating insurance companies. The pooling mechanism involves quota share reinsurance with the participating insurance companies collectively providing 100% reinsurance. Each participating company’s quota share is based on their voluntary market share in the respective state and relevant year.

The examiners observed during the investigation of Standard 9 that NCCI’s process for pool assessments and allocation of plan administration expenses has changed since the prior examination. This change occurred in 2015, when NCCI implemented a new standard pricing allocation methodology for plan administration expenses that uses a five year rolling average of policy and/or premium to reduce pricing volatility for the carriers participating in each state’s assigned risk plan.

To ensure this change was properly communicated, NCCI provides a quarterly communication to all companies that participate in the allocation and distribution of reinsurance pool financial results. The examiners also confirmed that there were no changes to the Service Carrier Report Procedures and there was no communication required or made to any State Insurance

Department regarding payment problems on balances due from reinsurance pool financial result distributions.

With respect to NCCI's data quality approach, the IT examiners found that NCCI utilizes a consistent process relative to the handling of data. In order to test the quality of the data NCCI uses for the allocation and distribution of financial results related to residual market policies, the IT examiners determined the process is detailed within NCCI's data quality best practices workflow. The IT examiners confirmed that pool data is submitted both at the detail and summary levels. NCCI's Pool Data Reporting Guidebook (Guidebook) provides the rules and requirements for reporting Residual Market data to NCCI, and it contains coding values, record layouts, and examples.

Servicing carriers are responsible for collecting, storing, and reporting Residual Market data to comply with the requirements as set forth in the quota share reinsurance agreements and articles of agreement and bylaws. Residual Market Data consists of the following financial and actuarial data; Financial (NP-1 and NP-4 data elements) and actuarial (NPX, Loss Sensitive Rating Plan—LSR, and Residual Market Large Loss—LGL data elements) data and are reported on a quarterly basis. Each of these data elements are reported on one or more forms, and will also be reported either at a summary and/or detail level. Residual Market data experience (premiums, losses, and expenses) for a given policy should be reported for the same state as the corresponding policy exposure, i.e., the state to which the corresponding policy premium was generated. Losses are reported based on the exposure state and not the jurisdiction state.

The IT examiners reviewed the Guidebook and confirmed that it details the process for receiving and reviewing Residual Market data. In addition, the IT examiners confirmed that the data edits performed for other data types (Financial, Unit Statistical, etc.) are applicable for Residual Market data. Also, the IT examiners performed a walkthrough with NCCI, who demonstrated the Residual Market application to Assigned Risk Policy process and confirmed the assignment. The IT examiners reviewed data in the RMAPS (Residual Market) and PDC (Policy Data) systems and confirmed that the data was consistent from the financial data collection through to the Residual Market systems.

*Based on the edits found in the matrices and the sample edits observed, the IT examiners determined that NCCI effectively uses data integrity checks to test the quality of the data upon which calculation of pool assessments is based, and also NCCI relies on objective and established procedures when administering residual market or pool assessments.*

**Recommendations: None**

<p><b>Standard 10</b> - The advisory organization uses objective and established procedures when administering assigned risks.</p>
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**Results: Pass**

**Observations:** The primary goal related to administering assigned risks is ultimately to depopulate the residual market and transition risks to the voluntary market. NCCI's processes in administering assigned risks focuses on this ultimate goal. In addressing Standard 10, the

examiners met with NCCI's representative regarding incentive programs used in hopes to achieve this goal. The premium and losses related to assign risk are included in NCCI's data call, and in the ratemaking process. Therefore, the same data controls which are discussed in the Data Collection and Handling standard, apply to assigned risks data to ensure the data quality. NCCI's changes to the process for administering assigned risks remains to be an objective and established process.

***Recommendations: None***

<p><b><i>Standard 13</i></b> - The advisory organization has appropriate controls, safeguards and procedures for protecting the integrity of computer information.</p>
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***Results: Pass***

***Observations:*** The IT examiners found NCCI's computer/communication facilities (computer room, network operations center, wiring closets, etc.) are secure and protected from hazards. Additionally, access to the computer/communication facilities is restricted to only authorized personnel at all times. NCCI uses firewall technology to protect its internal network from unauthorized external access, including scanning inbound messages and files for malicious content. Further, NCCI encrypts all sensitive data files when transmitting data outside the physical premises. Access to NCCI's network and computer systems is protected with layered security measures including unique user IDs and complex passwords, based upon the sensitivity of the information and the requirements of the individuals. Computer programs/databases/files impacted by user change requests are properly monitored, modified, tested and migrated to the secure production libraries. Changes to the application portfolio are authorized, controlled and documented by NCCI.

There are sufficient controls in place for the movement of new application components to a production environment, which guarantee accuracy and completeness. Based on the IT examiners' observations, the physical access controls and environmental controls are adequately designed.

***In summary, based on the IT examination team's observations, the advisory organization has appropriate controls, safeguards and procedures for protecting the integrity of computer information.***

During the walkthrough of the firewall operations, the IT examiners also discussed the automated scanning of email attachments. NCCI provided screenshots to the IT examiner confirming the operation of its automated solution for scanning email attachments.

***Based on the settings noted in the screenshot, the IT examiners found that NCCI appears to be properly scanning all incoming email for malicious content.***

To examine NCCI's process for transmitting secure information across the network, the IT examiners requested a screenshot showing the use of encryption for file submissions and email transfers. NCCI responded that file submissions from the carrier only come through its Data Transfer via the Internet tool and do not receive submission files by email. NCCI provided

screenshots that demonstrate the extent of security regarding the transfers including certificate information for the SFTP site, HTTPS information, and encryption information.

***The IT examiners observed that NCCI has the proper protocols in place to ensure information is securely transmitted across the Internet.***

The IT examiners noted NCCI enforces passwords with an application to create/remove/modify user accounts across all applications. This provisioning solution allows for password synchronization across platforms; therefore, NCCI does not set the password policy in Active Directory.

Based on information gathered during this walkthrough, the IT examination team requested additional details regarding NCCI's IT password processes and NCCI provided a copy of its Information Security Policy. The IT examiners observed that all Electronic Resources that store NCCI information, or that are permanently or intermittently connected to internal computer networks, must have a password-based access control system approved by NCCI's Enterprise Information Systems group. Also, to appropriately secure access to NCCI's electronic resources, users must follow the acceptable password management protocols.

The examiners reviewed NCCI's password policy and account lock out policy and found it to be reasonable.

***NCCI's information and supporting documentation provided indicates that NCCI appears to properly maintain effective management of passwords in order to access systems.***

In addition to the Information Security controls, the IT examiners also reviewed the controls around change management. From a change management perspective, the IT examiners leveraged IA's work related to these control areas:

- Change Management policies and procedures;
- Change initiation;
- Change testing;
- End-user documentation;
- Emergency changes;
- Change management system security; and
- General controls including: segregation of duties, access controls, and business continuity.

Additionally, the IT examiners reviewed NCCI's IA's work around System Development Life Cycle (SDLC) as relevant, including:

- Project Management Office (PMO) Methodology / Governance;
- Change initiation and testing;
- End-user documentation;
- Emergency changes;
- Project Implementation and review; and

- Confirming that findings from the prior audit have been resolved.

*In summary, based on the IT examination team's observations, the controls around changes to the application portfolio are authorized, controlled and documented. In addition, the IT examination team found that the controls relative to computer programs/databases/files impacted by user change requests are properly monitored, modified, tested and migrated to the secure production libraries and are adequately designed.*

**Recommendations: None**

<b>Standard 14</b> - The advisory organization has a valid disaster recovery plan.
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**Results: Pass**

**Observations:** The IT examiners reviewed documentation to ensure that critical business applications, databases and files are regularly backed up and stored off-site. Additionally, the IT examiners reviewed the disaster recovery plan and procedures to determine the following:

- Confirm the recovery procedures are current, detailed and repeatable;
- Confirm the inventory of critical business applications, databases and files is current and is defined and prioritized in the recovery process; and
- Confirm critical business areas developed manual recovery testing (off-site retrieval through restoration of a fully operational computing environment) on a regular basis.

The IT examiners reviewed copies of the IA work papers, the Business Continuity Plan (BCP) and Disaster Recovery Plan (DRP) Audit from 2014. The scope of the audit included a review of the BCP and DRP as well as DRP test documentation. In addition, the backup processes were reviewed for appropriate frequency, retentions, and failure management of the UNIX and Windows Environments. The audit included an evaluation of the adequacy and effectiveness of internal controls in place to ensure compliance with policies, plans, procedures, and laws and regulations which could have a significant effect on operations and reports. Additionally, the following included the following Processes/ IT Components:

- DRP testing;
- IT infrastructure and configuration; and
- Application backup.

The IT examiners found that data received by NCCI is replicated to the Disaster Recovery site on a near-real time basis and requested evidence of the replication schedule which was provided by NCCI. The screenshots demonstrated the continuous replication of the production data to the Disaster Recovery site and also provided evidence as to instances in which the data is consistent and up to date. The replication frequency is scheduled based on the criticality of the data with the most critical data being replicated on a near-real time basis. The replication schedule is configured through the console and replication is operating 24 hours a day. NCCI indicated that the only time there is an interruption in the replication connection is when Disaster Recovery testing is conducted twice a year, and that the schedule is reactivated through the console when the test is complete.

The replication activity is written to a journal log as a tracking mechanism and to help with troubleshooting issues should they arise. NCCI provided a screenshot of the log reflecting the results of the replication activity.

*Based on a review of the information provided, it appears NCCI ensures its data is routinely backed up and replicated off-site.*

Upon review of the Disaster Recovery and BCP, the IT examiners determined that the BCP was current as of January 2016. Also, the IT examiners confirmed key changes since the prior examination provided by NCCI. The key changes were:

- Inclusion of the updated Experience Rating System and
- Replication of backup data to the Disaster Recovery site.

The DRP defines the rules and processes required to ensure that the critical business functions can resume/continue normal processing within timeframes specified in the BCP. The plans are well documented to describe the steps NCCI would take when it cannot operate normally because of a natural or man-made disaster. The BCP is properly based on the Business Impact Analysis that classifies the functions as Immediate, Critical, Essential, and Deferred and defines the associated recovery timeframes.

Along with the BCP and DRP, NCCI also provided evidence of testing both plans. The IT examiners reviewed results from the NCCI's January 2016 post review of issues identified from the latest testing for application data, customer operations, and infrastructure. During the review, the IT examiners found the issues identified are clearly documented, with a resolution and recommendations for the future.

*As such, NCCI appears to be properly testing the Disaster Recovery Plan and Business Continuity Plan and addressing issues discovered during the testing.*

The BCP and DRP extend to the use of NCCI's IT Emergency Team to ensure adequate coverage in the event of a hurricane or similar natural disaster. NCCI IT has implemented guidelines, which addresses the availability of senior management during these events. The BCP and DRP outline the roles of the Emergency Team Leader and senior staff as well as the individuals assigned these roles during an emergency. Section six of the DRP specifically addresses the Declaration Procedures that identify the persons who are authorized to declare an emergency and the general process they should follow.

The BCP and DRP also identifies all key business functions and a list of programs, etc. A contact person (and alternate) is included for each function. This information also includes any vendors relied upon and the recovery time option of manual, critical, or deferred. The plan identifies the contact person in each department for manual processes used.

In response to the ITGC data requests, NCCI provided screenshot evidence of the Off-site Disaster Recovery directory where the Disaster Recovery policy/procedures documents are stored and maintained.



The IT examiners requested the Service Organization Control (SOC) report for the disaster recovery site. In response, NCCI stated that NCCI's Disaster Recovery vendor for the Disaster Recovery site does not currently subscribe to SOC certification/reporting. After further discussion, it was determined that NCCI needed to modify its contract with the vendor in order to receive the SOC reports. Upon the contract update, the current report was provided and reviewed by the IT examiners who found no issues in the report. Upon further inquiry with NCCI, the IT examiners found that NCCI has been using the same company as its Disaster Recovery vendor for over ten years. Prior to the contract renewal, NCCI had performed a review of the security procedures during semi-annual Disaster Recovery test. In the past two years, NCCI has enhanced its contract process to include the review of vendor SOC reports prior to committing to the contract.

*Based on the IT examiners' review of the Plans as discussed above, the examiners conclude that NCCI has in place a valid and effective DRP.*

*Recommendations: Yes. Please see the Examination Summary on page 39 and 40 of this Report.*

***b. Data Collection and Handling***

<p><b><i>Standard 1</i></b> - The statistical agent's series of edits are sufficient to catch material errors in data submitted by a company.</p>
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***Results: Pass***

***Observations:*** The IT examiners requested that NCCI provide evidence of edits performed for the various data types, which NCCI receives. NCCI provided matrices depicting the edits for each of the following data types:

- Policy Data;
- Detailed Claim Data;
- Medical Call Data;
- Financial Call Data; and
- Unit Statistical Data.

***The IT examiners reviewed the matrices and determined that the edits appeared to be appropriate for the various data types.***

In addition to reviewing the testing performed for the previously discussed ERS and the matrices of data edits, the IT examiners performed a walkthrough of the data edits performed using the Financial Data Collection and Aggregate Ratemaking (ARO) applications. With the assistance of NCCI's IT resources, the IT examiners walked through the edits to the data from the various carriers. A total of eleven sample filings was selected by the actuarial examiners and the IT examiners selected a sample of six of those filings to walkthrough. The IT examiners selected the following filings for review:

- New Hampshire - Report year 2014;
- Hawaii - Report year 2015;
- Virginia - Report year 2015;
- Illinois - Report year 2013;
- Oklahoma - Report year 2015; and
- Georgia - Report year 2015.

The IT examiners observed screens within the Financial Data Collection application that showed the edits which were performed for the New Hampshire Financial Call data. The IT examiners found that two edits were identified and were resolved. The IT examiners also observed the edits for the remaining samples, acknowledging that any edits identified were resolved. Additionally, the IT examiners observed the monitoring of the Financial Call data for completeness and found that the percentage of reporters expected is monitored for each call. Finally, the IT examiners observed the data for each sample and confirmed that 100% of the expected respondents had reported.

In addition to the examiners' review discussed above, the IT examiners also reviewed copies of the previously discussed Experience Rating Migration Project Results documentation and determined the review would be relevant to this Standard. The report regarding the project describes the procedures performed by PwC in reference to the project undertaken by NCCI in 2014. The IT examiners performed a review of the report in the online system at NCCI on November 7, 2016. Based on the review of PwC's Experience Rating Migration Project Results report, the IT examiners found that the scope of the procedures covered the entirety of the ERS including the application (calculation, rating effective date, edits, triggers, rating distribution) and database (data accuracy, data validity). The project involved five functional areas, including: Rating Calculation, Rating Effective Date, Edits, Triggers, and Distribution. The IT examiners reviewed the testing for the project and confirmed that the data edits included in the scope of the project were successfully performed.

*As a result of the work performed, the IT examiners concluded based on the review and investigation of Standard 1 that NCCI's series of edits are sufficient to catch material errors in data submitted by a company.*

***Recommendations: None***

***Standard 2*** - All data that is collected pursuant to the statistical plan is run through the editing process.

***Results: Pass***

***Observations:*** Please refer to Standard 1, under Data Collection and Handling "*The statistical agent's series of edits are sufficient to catch material errors in data submitted by a company*" for relevant testing, as these standards were tested in conjunction with each other.

***As such, the examiners have concluded that NCCI runs all data that is collected pursuant to the statistical plan, through the Organization's editing process. The process has been determined to be effective and comprehensive in addressing any data issues.***



## *Recommendations: None*

**Standard 4** - Determine that statistical data is reconciled to the State Page - Exhibit of Premiums and Losses, Statutory Page 14, of the NAIC annual statement on an annual basis.

## *Results: Pass*

To address Standard 4, the IT examiners investigated NCCI's Financial/Statistical Analysis (analysis), which compares data from the Policy Year Call (Call #3) to Unit Statistical data. The reconciliation process of financial data to page 14 of the carrier's annual statement is performed as part of the overall Financial Data Call validation and notification process. The Reconciliation Report (Call #8) is used to reconcile calendar year premium, losses, and expenses by state from the Calendar-Accident Year Call to the Exhibit of Premiums and Losses (Statutory Page 14) of a company's National Association of Insurance Commissioners (NAIC) Annual Statement. NCCI collects detailed data on work-related injuries and prepares state insurance rate recommendations, prices state legislative proposals, and delivers data services and products for use by insurance companies and state government entities. The type of data and the frequency/timing, which it is provided is termed a "call". The analysis is typically performed for the most current and complete policy years. Financial/Statistical analyses are prepared after the submission of the Financial Calls for a given reporting season. This analysis is also refreshed later in NCCI's validation season to account for additional Unit Statistical reports received after the Financial Calls primary due date.

The IT examiner confirmed that NCCI's analysis considers the following:

- Company Standard Premium;
- Total Paid and Case Losses (indemnity paid, plus medical paid, plus case losses); and
- Indemnity Incurred Claim Counts

The analysis excludes certain experience from the Unit Statistical data to mirror the reporting requirements for Financial Call data. The *Financial Call Reporting Guidebook* outlines specific experience that should be included and excluded for Financial Call reporting for both Calls #3 and #20. If discrepancies are identified, an exhibit is created that will show the reported Financial Call data and aggregated Unit Statistical data amounts by data component with the differences and the percentage differences displayed by state and policy year. The discrepancies of concern are highlighted. In addition, Call #8 – Reconciliation Report provides the means for NCCI to reconcile Financial Call data to page 14 of a carrier's annual NAIC statement. When a carrier reports Call 8 to NCCI they must provide detailed explanations for any differences. NCCI validates Call 8 through a series of edits that compare reported values across other Financial Calls reported to NCCI, and against page 14 data obtained from the NAIC. The IT examiner reviewed the edits/validations defined in the Financial Call Reporting Matrix and confirmed that edits/validation are performed to reconcile the Financial Call data to the page 14 of the NAIC statement.

NCCI groups are aligned with one of the following four categories based on Company Standard Premium:

- Small (\$500,000);
- Medium (\$750,000);
- Large (\$1,000,000); and

- Extra-Large (1,500,000).

Premium and loss differences between the corresponding Financial and Unit data are considered out of tolerance when the difference meets the state category threshold and is  $\geq 10\%$ , or  $\geq \$3,000,000$  (regardless of the percentage difference). Claim count differences are considered out of tolerance when they are  $\geq 20$  and  $\geq 10\%$ , or the count difference is  $\geq 40$  (regardless of the percentage difference). The data provider's Financial Call data contact will receive the exhibit and supporting information that describes the analysis. This includes the policy list of the Unit Statistical data that was used to create the Unit Statistical side of the analysis.

The IT examiners performed a walkthrough of the analysis process with NCCI on January 16, 2017. The examiners confirmed the following updates to the process during the review period:

- In April 2015, NCCI implemented the All Carrier Financial/Statistical, which identifies discrepancies for all data providers that report financial calls and unit statistical data. These results are used to determine which carriers will be selected for more detailed analysis.
- In 2014 NCCI, expanded the Financial Call to Unit Statistical comparisons to include analysis between filing cycles after unit statistical data has been received for an entire policy year, as the means to provide support to carriers ahead of the next reporting cycle. This analysis is run September through October.
- The Designated Statistical Reporting analysis, and Large Loss review, were formally introduced when the Data Quality Guidebook was first published in 2015, and also compare Financial Call and Unit Statistical data.

The IT examiners obtained a listing of financial reconciliation reports from NCCI which were separated into three categories:

- Designated Statistical Reporting – 148 reports;
- Financial Call to Unit Statistical Comparison – 293 reports; and
- Large Loss Review – 158 reports.

A sample of five reports of each type of financial reconciliation report was selected for review. Using a pivot table, the IT examiners determined the five groups which had the greatest number of reports and judgmentally selected one report from each group including for the period 2013, and two each from 2014 and 2015. The IT examiners obtained the sampled reports and reviewed the associated documentation. The IT examiners found that the analysis is a comparison between a carrier's financial and unit statistical information with the primary goal being to evaluate the consistency of data reporting between the two sources. There is also a difference in the timing of the reporting and valuation for the financial and unit data; however, NCCI makes adjustments to eliminate this issue as much as possible. Although there still may be nominal timing discrepancies, it is reasonable to expect that the more mature years will move comparably closer between the two data sources. The IT examiners found that the issues documented in the analysis were resolved by either sufficient explanations for the discrepancy or updated information.

The IT examiners also performed a walkthrough with the NCCI of the Analysis process using three of the samples. The samples included multiple carriers of varying sizes and an accompanying sample of financial reports, including: Designated Statistical Reporting, Financial Call to Unit Statistical Comparison and Large Loss Review. The walkthrough included a review of NCCI's process for identifying the reconciliation matters, NCCI's processes used to communicate the matters to the affiliates involved and confirmation that reconciliation issues are resolved. For each of the samples reviewed during the walkthrough, updated data was required to demonstrate how the reconciliation issue was resolved. The IT examiner's reviewed the additional information and confirmed that the reconciliation issue was resolved and the corrected data was utilized.

*Based on the work discussed above by the IT examiners, it was determined that statistical data is reconciled to the State Page Exhibit of Premiums and Losses, Statutory Page 14, of the annual NAIC Statement on an Annual Basis.*

*Recommendations: None*

*c. Correspondence with Insurers and States*

<p><i>Standard 2</i> - The statistical agent has established procedures for notifying companies (and regulators, as requested or required) of material errors and for correcting those errors (also reference Standard 2, Operations/Management/Governance).</p>
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*Results: Pass*

*Observations:* NCCI communicates any errors to its affiliates and regulators through an Escalation Process and Data Quality Remediation Program to resolve significant data issues. Please reference Standard 2 – Operations/Management and Governance for a detailed overview of NCCI's Escalation Process.

Since the prior examination, NCCI has established materiality thresholds for escalating data errors to affiliates and regulators. NCCI worked with regulators and the NAIC to validate that the proposed thresholds are appropriate and developed the Regulator Service Commitments that include details of the steps NCCI takes to escalate reporting errors. In addition to investigating and discussing NCCI's Escalation Process, a review of a sample of communications to affiliates and regulators discussing the process was performed.

*Based on the review of information and documentation related to this Standard 2 and the investigation of NCCI's Escalation Process described under Standard 2 – Operations/Management and Governance, the examiners have concluded that NCCI has an established and robust process in place for notifying companies (and regulators, as requested or required) of material errors and for correcting those errors (also reference Standard 2, Operations/Management/Governance).*

*Recommendations: None*

**Standard 4** - Review any additional data quality programs maintained by the statistical agent pertaining to data collected pursuant to the statistical plan.

**Results: Pass**

**Observations:** Please refer to Data Collection and Handling Standard 1, “The statistical agent’s series of edits are sufficient to catch material errors in data submitted by a company” and, Standard 2, “All data that is collected pursuant to the statistical plan is run through the editing process” for all IT testing performed related to this Standard.

**Recommendations: None**

**d. Reports, Report Systems and Other Data Requests**

**Standard 2** - The statistical agent has accurately extracted the appropriate information from the statistical database.

**Results: Pass**

**Observations:** The IT examiners reviewed the sample of filings selected by the actuarial examiners using the Financial Data Collection and Aggregate Ratemaking applications. With the assistance of the IT examiners selected various data elements in the reports and tied the values back to the data in the Aggregate Ratemaking and the Financial Data Collection. This tie-out confirmed that the data was consistent and accurate from receipt through processing to the final report. A total of eleven sample filings was selected by the actuarial examiners, and the IT examiners selected the following sample of five filings to walkthrough:

- New Hampshire - Report year 2014;
- Hawaii - Report year 2015;
- Virginia - Report year 2015;
- Illinois - Report year 2013;
- Oklahoma - Report year 2015; and
- Georgia - Report year 2015.

The IT examiners observed screens within the Financial Data Collection and Aggregate Ratemaking applications which reconciled with the values in each of the sampled filings. The IT examiners observed the values for the sampled filings and confirmed that the data in the reports was consistent with the data contained in the applications and was extracted from the databases correctly.

The IT examiners previously discussed the examiners’ scope of work regarding Standard 1 – Data Collection and Handling. The IT examiners reviewed the previously discussed project (Experience Rating Migration Project) documentation and determined the review would be relevant to this Standard. The report from the project describes the procedures performed by PwC in reference to the ERP undertaken by NCCI in 2014. The IT examiners performed a review of the report in the online system at NCCI on November 7, 2016. The IT examiners

found that the scope of the procedures covered the entirety of the ERS including the application and database. The IT examiners reviewed the testing for the project and confirmed that the reports generated from the ERS, included data which was extracted from the applicable databases and was correctly displayed on the reports.

*As a result, the IT examiners concluded based on the review and investigation of Standard 4 that the data for NCCI reports is extracted correctly.*

***Recommendations: None***

***e. Inspection Services***

***Standard 1*** - The advisory organization conducts inspection services in accordance with applicable statutes, rules and regulations, and written procedures.

***Results: Pass***

***Observations:*** NCCI's Inspections Services are supported by a 25-page comprehensive guideline document, which includes workflows. The document is identified as NCCI's *Classification Quality Assurance (CQA) – CQA 03.013 – Inspector Procedures (Procedures)*. The procedures were developed to document the NCCI's requirements related to performing onsite inspections, specifically providing guidance to NCCI's inspectors in conducting any type of physical inspections. The inspection process is critically important in supporting the NCCI's classification process. Ensuring classifications are correct and accurately reflect a risk profile is the foundation in ensuring the correct determination of rates, or premiums, for filings.

NCCI's procedures address both CQA/Selected as well as Special Inspections. Selected Inspections are defined as physical classification inspections performed as part of the Selected Inspection Program and are applicable only in Florida. Special Inspections are those, which have been requested by an employer, agent, insurance carrier, regulator, the NAIC or another system participant.

NCCI's inspection process is supported by an automated system identified as the Regulatory Assurance Information System (RAIS). This system affords access for online classification inspections using a specific online form. The form requires relevant information to be entered including identifying the type of inspection being requested (*Selected or Special*). The inspector is required to enter certain information into RAIS as part of the inspection request process. For Special Inspections, a Regulatory Services Coordinator reviews the requests and will address any missing information with the requestor. All inspection documentation is entered and maintained into an Inspection Project Folder and added to the Inspector's Documentum Inbox.

Inspection timelines are also established in RAIS and include the following:

- A minimum of two good faith attempts to schedule an inspection appointment must be made within 30 days of the initial inspector assignment.
- Within ten days of receiving an inspection assignment, inspectors must make one good faith effort by mail to schedule an appointment. If an inspection appointment

is not scheduled on the initial attempt, the inspector must make a second attempt within 30 days of the assignment by telephone.

- If an appointment is not successfully scheduled after the second attempt, the inspector may close the assignment and notify the Regulatory Services Coordinator or Inspection Team Leader at which time the Inspector and Team Leader will agree on next steps, which are enumerated in the CQA.
- Inspection reports should be completed within 11 days of completing the on-site inspection.
- Inspections should *be completed* within 55 days of assignment.

*Based on the examiners' review of the procedures and related documentation, the examiners determined that NCCI conducts inspection services in accordance with applicable statutes, rules and regulations, and written procedures. Further, NCCI's practices and procedures, including, the inspection timelines and documentation requirements, facilitate timely communication with carriers, insured's and regulators.*

*Recommendations: None*

*f. Residual Market Functions- Plan Administration*

<p><i>Standard 1-</i> The advisory organization uses objective and established procedures when administering assigned risk plans.</p>
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**Results: Pass**

**Observations:** NCCI provides a variety of Residual Market Services for 31 states. These services include but are not limited to the administration of NCCI's Workers' Compensation Insurance Plan (WCIP) and the National Workers' Compensation Reinsurance Pooling Mechanism (NWCPR). Additionally, NCCI provides financial, actuarial and insurer oversight for clients. NCCI provided Residual Market Plan Administration Services in 22 states during the scope.

NCCI has an established process for the management of Assigned Risk plans, which starts with an application process, which is in place to ensure all applications are compliant with state and eligibility requirements. The application process is supported by an online application, referred to as RMAPS, a proprietary NCCI system which leverages NCCI's data systems to assist in validating applications. RMAPS provides NCCI's clients a number of benefits including expedited processing where an application, the ACORD 130 Workers' Compensation Application, will be reviewed within 48 hours of receipt.

NCCI's process also includes procedures and established timelines regarding notification of declinations for worker's compensation coverage as well as a process for Investigative Review of an application for situations in which an application may be identified for a more in-depth review. Finally, NCCI's process includes a Quality Program, wherein samples of applications are reviewed by NCCI's Quality Analysts on a weekly basis.

NCCI administers assignments using a quota mechanism, wherein NCCI's primary goal is to *"distribute residual market risks randomly and equitably among servicing carriers writing residual market business on behalf of the participants in the reinsurance pooling mechanism and direct assignment carriers."* The assignment process is supported by NCCI's Plan and Pool Membership System (PPM), which is a sub-system of RMAPS. PPM helps to ensure carriers secure their agreed upon quota percentage during the relevant contract term and are meeting their statutory duty to participate.

PPM considers a number of variables when assigning a residual market application to an assigned carrier. These variables include the following:

- **Reassignment** – PPM aligns the employer with the prior assigned risk carrier, which limits movement of risks from one carrier to another and better enhances provided services such as claims handling and fraud prevention.
- **Multistate Assignments** – Assignments are made consistent with an established reciprocal agreement and adds flexibility for risk with multistate locations.
- **Special Coverage** – Considers special coverage needs such as United States Longshore and Harbor Workers (USL&HW), Maritime, Coal Mining and increased limits.
- **Increased Limits of Liability** – Assignments with employers' liability limits up to \$1,000,000/\$1,000,000/\$1,000,000.
- **Distance from Quota** – PPM considers insurance carriers with available capacity and weighted by each carrier's distance from expected quota.

PPM also provides carriers and regulators with access to quota reports and related information to enhance communication and to ensure stakeholders to the process have availability to key plan information.

The actuarial examiners reviewed filings, which included assigned risk rate changes for the following States and Effective Year:

1. Arizona – 2014;
2. Georgia – 2015;
3. Illinois – 2013;
4. Illinois – 2015;
5. Kansas - 2011
6. New Hampshire – 2014; and
7. Virginia - 2015

There were no findings resulting from the review.

NCCI discussed with the examiners that the over-arching goal is to depopulate the residual market. The two primary programs NCCI has in place to accomplish this goal are:

- 1) Take-Out Credit
- 2) Voluntary Coverage Assistance Program (VCAP)



The Take-Out Credit program provides an incentive for carriers to take risks out of the residual market into the voluntary market. This is accomplished by providing a credit to the carrier based on the amount of premium moved out of the residual market by the carrier when it writes the risk on a voluntary basis. The carrier needs to keep the risk on the books for a reasonable period of time to qualify for the credit.

VCAP is a program whereby NCCI offers risks that are unable to find a voluntary market through its agent. NCCI opens the risk to additional national markets in an attempt to secure voluntary coverage. NCCI typically observes savings of approximately 20% for the risk, which are able to secure voluntary coverage.

A third program created by NCCI is known as Program Expiration. This program allows NCCI to make information on the risk available to the market in advance of program expiration, so that there is more time for a carrier to consider writing the risk on a voluntary basis in the upcoming year.

### *Other Incentives*

NCCI has created additional incentives for risks to manage losses in the residual market. One such program is the Assigned Risk Adjustment Program, which builds a surcharge for prior claim experience into the assigned risk rate structure. This incentivizes residual market risks to improve safety programs and achieve claim-free experience. Some residual market risks are also eligible for a retrospective program, which allows for lower premium if claim experience is favorable during the policy period.

Additionally, the examiners confirmed that effective January 1, 2015, NCCI implemented a standard pricing allocation methodology for Residual Market Plan Administration Expenses. The new methodology relies on a five year rolling average of policy and/or premium to reduce pricing volatility.

The key changes regarding the new methodology include the following:

- Implemented a state flat fee, which includes expenses, which are not driven by state volume.
- Variable/Volume driven expenses, which are variable in nature and are driven by application processing volume, carrier audits, and direct costs. Allocated to each state relying on a five year rolling average of each states annual assigned risk policy volume.
- Bank & Credit Card Fees, which are allocated to each state using the five year rolling average of each state's annual assigned risk premium volume.
- The NCCI eliminated a customer service flat fee.

NCCI advised the examiners, that NCCI previously relied on an approach that was based on a combination of application, policies and premium to allocate a targeted revenue budget to the states. NCCI believes this previous approach was more inherently volatile based on changing market conditions and servicing carrier "bid results," which will be addressed through the implementation of the new standard pricing allocation methodology.



The examiners considered the new standard pricing allocation methodology, and agree that in context to the prior methodology, the new standard pricing methodology appears to be a reasonable approach and one, which should mitigate the potential volatility associated with the previous approach.

***Based on the work conducted by the examiners and the supporting documentation provided by NCCI, the examiners have concluded that NCCI uses objective and established procedures when administering assigned risk plans. Further, the standard pricing allocation methodology implemented in 2015 for Residual Market Plan Administration Expenses, appears to be justifiable and is consistent with the plan rules and procedures.***

***Recommendations: Yes. Please refer to the Examination Summary on pages 39 and 40 of this Report.***

**g. Residual Market Functions - Reinsurance Administration**

<p><b><i>Standard 1</i></b> - The advisory organization uses established procedures when administering residual market pool assessments or reinsurance pooling mechanisms.</p>
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***Results: Pass***

***Observations:*** Standard 1 acknowledges the following Documents and Procedures to be reviewed in addressing the scope of the Standard. The examination is recommended to include:

- Manuals, procedures and information prepared or published by the advisory organization that relate to residual market pool assessment or reinsurance;
- Reporting of financial information;
- Financial and accounting responsibilities;
- Reserving Practices;
- Deficit/Surplus administration; and
- Review of the implementation and performance results of the enhanced carrier audit system.

In discussing NCCI's Reinsurance Administration program, NCCI advised the examiners that aspects of this Standard were waived from review during the prior examination and NCCI requested this approach be adopted again for the Examination. NCCI advised the following:

*“Pool financial data, pool results, actuarial reserve analysis and individual carrier pooling allocations are conducted under separate contracts and subject to independent audits overseen by the governing bodies of the various pools serviced by NCCI and the information is confidential in accordance with those agreements.”*

NCCI further advised that their financial role as the Reinsurance Pool Administrator is largely limited to serving as a “pass through.” They do not become involved, as stated above with the various financial components, which again, are overseen by governing bodies of the various pools.

The Examiner-In-Charge (EIC) discussed this matter with the Lead States who agreed with NCCI that the financial aspects, e.g. Financial and accounting responsibilities of Standard 1 would not be subject to the Examination.

NCCI’s Reinsurance Administrator process does not result in pool assessments, but rather there is an allocation and distribution of financial results regarding residual market policies reinsured through the pooling mechanisms by their participating insurance companies. The applicable pooling mechanisms are quota share reinsurance mechanisms, with the participating insurance companies collectively providing 100% reinsurance, with each participating company’s quota share based on their voluntary market share in the respective state and relevant year.

Financial operating results for the reinsurance mechanisms are distributed on a quarterly basis for cash flow as well as incurred basis activities. Results of cash flow transactions are either paid or billed to the participating companies, dependent upon whether there is a positive or negative cash flow position.

To assist the participating companies in preparing their financial statements, NCCI also provides the incurred losses, which would include charges in unearned premium and loss reserves. NCCI advises that *“all of the reporting and settlement differs from a true “assessment” process, since the financial result could be either positive or negative to the participants.”*

The examiners also confirmed that there were no instances in which communication was required or made to any State Insurance Department regarding assigned risk deficits or surplus results. Further, NCCI reported that during the scope, there were no payment problems on balances due from reinsurance pool financial result distributions.

*Based on the scope of work performed to address this Standard, including interviews and discussions with the NCCI and a review of the Organization’s policies and procedures related to Reinsurance Administration, the examiners concluded that NCCI uses established procedures when administering residual market pool assessments or reinsurance pooling mechanisms.*

## **VIII. EXAMINATION SUMMARY**

In addition to the General Conclusions and Observations included on pages 6-9 of the Report, the following are specific observations made as a result of the Examination:

<b>OBSERVATION</b>	<b>RECOMMENDATION</b>
NCCI’s actuarial team appears to be well organized with well-defined roles and responsibilities. However, they do not appear to produce regularly scheduled management reports related to on-going activities.	NCCI should begin the practice of producing monthly and/or quarterly management reports that assists NCCI in monitoring actuarial related tasks, timelines and overall status.

<b>OBSERVATION</b>	<b>RECOMMENDATION</b>
NCCI should disclose how they utilize accident year data in making their informed decisions regarding the loss costs/rate filings.	NCCI should include sufficient documentation in the loss cost/rate filings to allow regulators, members and other interested parties to understand the methods applied and the selection process relied upon, as per the observation.
NCCI should provide additional information as to how the separate calculation of frequency and severity trends contributes to the selection of the loss ratio trend.	NCCI should include sufficient documentation in the loss cost/rate filings to allow regulators, members and other interested parties to understand the methods applied and the selection process relied upon, as per the observation.
NCCI should document within the loss cost/rate filing how the trend is selected from the various results similar to the process used in the Technical Peer Review.	NCCI should include sufficient documentation in the loss cost/rate filings to allow regulators, members and other interested parties to understand the methods applied and the selection process relied upon, as per the observation.
NCCI should provide a description of the methods used to calculate the various trend factors especially those methods that are based on economic modeling.	NCCI should include sufficient documentation in the loss cost/rate filings to allow regulators, members and other interested parties to understand the methods applied and the selection process relied upon, as per the observation.
NCCI relies solely on paid and reported loss development methods in its projection of ultimate losses underlying indicated loss cost/rate changes.	NCCI should consider using additional actuarial methodologies, such as Bornhuetter-Ferguson approaches, in projecting ultimate losses.
NCCI should find a practical method of including more information with respect to the filings other than loss cost/rate filings that are approved separately and then referenced in the loss cost/rate filing. For example, the actuarial examiners noted references to changes in the experience and retrospective rating plans and in class definitions in the loss cost/rate filing but there is no additional information provided in the loss cost/rate filings.	NCCI should include sufficient documentation in the loss cost/rate filings to allow regulators, members and other interested parties to understand the methods applied and the selection process relied upon, as per the observation.
NCCI should provide additional information for the determination of the full credibility standard for classification ratemaking.	NCCI should include sufficient documentation in the loss cost/rate filings to allow regulators, members and other interested parties to understand the methods applied and the selection process relied upon, as per the observation.
NCCI's rate filings should provide support for the selected profit and contingencies provision.	NCCI should include sufficient documentation in the loss cost/rate filings to

OBSERVATION	RECOMMENDATION
	allow regulators, members and other interested parties to understand the methods applied and the selection process relied upon, as per the observation.
NCCI should make it a practice to obtain the annual SOC report from the Disaster Recovery vendor in a timely manner and review the report to confirm controls at the Disaster Recovery site are adequate, effective and meet the objectives of NCCI.	NCCI’s review of the report should be formally documented and available for inspection by regulators in a timely manner.
NCCI should consider providing regulators an interim report regarding NCCI’s new standard pricing allocation methodology related to its residual market – plan administration and reinsurance pool services	Understanding the new methodology relies on a five year rolling average, NCCI should consider submitting an ad hoc report at the conclusion of the examination, discussing the new standard pricing allocation methodology to cover calendar years 2015 and 2016. The report would serve as a “status check” regarding NCCI’s anticipated expectations for the new methodology.

**EXAMINATION FINAL REPORT SUBMISSION**

The Office hereby issues this Final Report based upon information from the examiner’s draft report, additional research conducted by the Office, and additional information provided by the Company.