In this article, we’ll examine some of the current market trends and concerns, and review some of the reasons for (cautious) optimism.

Positive Industry Indicators

Let’s begin with a look at the industry premium and some relatively good news.

Written premium for private carriers is showing a second consecutive year of growth, continuing a turnaround from several years of declining premiums. Estimated premium increased to over $35 billion in 2012—a more than 10% rate of growth. The 2012 increase is likely due to slight growth in the economy, some increase in average wages, bureau loss cost increases, and carrier pricing actions.

The recent premium increases are notable. In contrast, industry watchers will recall the disturbing drop in premium from 2006 through 2010. This drop was caused by a confluence of factors:

- The general economic recession, which reduced total payroll
- The steep losses in manufacturing and construction jobs
- Generally declining bureau loss costs/rates
- A soft market in carrier pricing

Claims Frequency Returning to Expected Downward Trend?

After increasing in 2010 for the first time in 13 years, lost-time claim frequency declined once again in 2011, by 1%. Though modest in comparison with the annual rate of decline in prior years, this suggests that the 2010 uptick may have been the result of recession-related factors, such as an increase in new hires as the recovery began to take hold and an influx of small lost-time claims.

It remains to be seen whether frequency resumed its long-term rate of decline in 2012 (approximately 2% to 3% since 1926). But with the distorting effect of the recession behind us, the long-term downward trend is expected to outweigh any upward pressure from new, inexperienced workers.

Moderating Claim Costs

With the flattening of claim frequency, claim costs have also moderated.
After a slight decline in 2010, the average indemnity cost per claim increased by just 2% in 2011—less than the change in the average weekly wage and less than the change in most years since the reform era of the 1990s.

Changes in medical costs in 2011 also showed favorable results due to the shift in the mix of claims (i.e., the increase in small lost-time claims). The medical average cost per lost-time claim increased by almost 4% in 2011.

Despite the shift in the mix of claims, the underlying cost drivers for both indemnity—and particularly medical—are still present.

Still, we're seeing less development than expected. Some reasons include a flattening in the number of treatments per claim and continued focus on medical cost control on the part of public policy makers and carriers.

However, the increases remain slightly higher than both average wage increases and the medical Consumer Price Index (CPI). For NCCI states, medical losses are now approaching 60% of total losses.

As with general health, the workers compensation line continues to migrate to being a medical management business, with policy makers, employers, and carriers struggling to manage and control the costs of medical care.

Modest Economic Recovery
While a confident economic recovery still has not arrived, we expect modest growth in average weekly wages to continue in 2013. To date, most of the growth reflects increases in the number of hours worked per week; increases in hourly wage rates have barely kept up with the current modest pace of inflation.

This suggests that there will be limited growth in indemnity severity in 2013 since duration appears to be easing as the labor market strengthens.

At this point, however, strong job growth is not expected until 2015 at best. On the positive side, employment and payroll have increased modestly. This growth, combined with some firming in rates, has helped support the increase in workers compensation premium.

Reasons for Concern
While we are pleased to see the positive signs outlined above, there remain real concerns about the health of the workers compensation industry.

Calendar Year Combined Ratio
In 2011, for the third straight year, workers compensation held the distinction of having the highest combined ratio of all of the major commercial lines. Our preliminary analysis indicates that the combined ratio may come down slightly for 2012. However, we are not convinced that this will indicate a meaningful improvement in underlying results.

In May, we will report on the final calendar year combined ratio numbers and analysis at NCCI’s Annual Issues Symposium.

Operating Results
Combining the 2011 underwriting profit with investment gains results in a pretax operating loss of 1% for the industry. In other words, despite three years of favorable investment gain results, we have seen near zero operating gains. This is obviously not a desirable condition.

Accident Year Combined Ratio
NCCI’s current measure for Accident Year 2011 (the latest complete year) is 114%. The deterioration of the workers compensation insurance industry results appear to have moderated, with 2011 showing an ever-so-modest improvement in underwriting results on an accident-year basis.

It’s worth noting that, over the last few years, calendar year results are much more in line with accident year results—underscoring a degree of stability in the industry’s reserve position.

Reserve Deficiency
Our estimate of the industry’s reserve deficiency ticked up a bit in 2011 (up $1 billion in each of the last two years, beginning in 2009) to $11 billion. The net deficiency, after permissible discounting, is roughly $5.4 billion.

The $11 billion industry deficiency is roughly 10% of 2011 carried loss and loss adjustment expense (LAE) reserves—not alarming but worth monitoring. It remains a stark contrast to the 2001 peak, when the deficiency stood at 33% of carried reserves.

Rate and Loss Cost Changes
Although there are some states that have experienced significant loss cost and rate changes in the last few years, the bureau loss costs have been quite stable overall. Decreasing frequency and diminishing average wage increases have been acting to offset the impacts of rising indemnity and medical costs.

However, 2012 saw loss cost increases in 27 NCCI states—meaning that the overall environment may be changing. NCCI Senior Division Executive Peter Burton examines state-based issues and concerns in “2013 Legislative and Regulatory Outlook” in this Issues Report.
Residual Market Growth
Despite the first real increase in size since 2004, the residual market continues to perform well—largely self-funded, with a modest burden to the voluntary market. However, the market is showing a little bit of firming—something that will bear watching.

The combined ratio for the residual market in 2012 is estimated to be improved from 2011, although it’s important to remember that, as the pool grows significantly, the results tend to get a little better from a combined ratio perspective. A struggling economy has doubtlessly played a role in the number of accounts seeking coverage in the residual market today. Jim Nau, NCCI’s general manager of residual markets, examines the current state of residual market results in “What’s Up With the Residual Markets?” in this Issues Report.

Issues That Bear Watching in 2013
In addition to both the positive and cautionary industry metrics described above, there are also a number of other issues that bear watching in 2013.

Near the top of the list remains the Patient Protection and Affordable Care Act (PPACA). With most of the law’s provisions taking effect over the next couple of years, the ultimate consequences to workers compensation stakeholders remain to be seen.

Other federal initiatives that market leaders are watching include the anticipated 2014 expiration of federally backed terrorism insurance (TRIA/TRIPRA). There are passionate voices on both sides of the renewal debate, and this should be monitored in the months ahead as Congressional hearings continue. Former NCCI executive Barry Llewellyn examines the current state of the law and some of the competing viewpoints in “Terrorism Insurance to End?” in this Issues Report.

Beyond TRIA renewal debates, it will be interesting to see if the President’s reelection results in a more visible Federal Insurance Office (FIO) presence in the months ahead.

At the state level, we do not anticipate many major legislative efforts during 2013, aside from Oklahoma and Tennessee. Peter Burton, NCCI’s senior division executive for state relations, examines the full regulatory landscape in “2013 Legislative and Regulatory Outlook” in this Issues Report.

However, among the issues that have captured significant legislative and regulatory attention are drugs (both repackaging and opioid abuse) and ongoing efforts in Oklahoma to create an opt-out program for workers compensation insurance.

The prescribing of opioids in workers compensation cases has garnered tremendous attention—both in terms of system costs and the long-term effects on patients—as part of the larger national debate on healthcare issues. Several states are examining the impact of narcotics on claims, and legislation addressing drug monitoring programs and reforms may be introduced this year. At the same time, some states continue to work to reduce the additional costs that repackaged drugs introduce to workers compensation claims.

Also of interest is the ongoing effort to create a workers compensation opt-out system in Oklahoma. This effort failed in 2012, but it has come up again in 2013. Writer Nancy Grover examines the issues surrounding opt-out in “The Future of Opt-Out” in this Issues Report.

Summing Up
I’ve relayed a great deal of information about the trends, metrics, and initiatives affecting the workers compensation market at the start of 2013. Let me conclude by summarizing some of the general trends we’re seeing in the market today.

Under the heading “positive trends,” we have:
• Economic recovery continuing (albeit too slowly)
• Premium growing
• Modest indemnity and medical severity changes
• Firming underwriting cycle

At the same time, we are monitoring several areas of concern:
• Combined ratio remains too high
• Claim frequency not yet returned to historic rates of decline
• Residual market growth
• Political uncertainty, particularly at the federal level involving fiscal and regulatory issues
• Impact of implementing Patient Protection and Affordable Care Act remains uncertain

As always, NCCI will continue to monitor and report on all of the above issues, including our traditional State of the Line analysis to be presented at our Annual Issues Symposium in May. In the meantime, we invite you to visit ncci.com for our continually updated research, legislative analysis, and economic forecasts.

Stephen J. Klingel, CPCU, WCP, was appointed president and chief executive officer of NCCI in 2002. Before joining NCCI, Mr. Klingel was a leader with the St. Paul Companies for more than 25 years.
Every day, NCCI partners with some 900 companies representing 350 carrier groups from across the country, as well as dozens of state regulators.

We engage with our customers through a wide range of events, from in-person visits to *State Advisory Forums*, from open houses and data workshops to our *Annual Issues Symposium*. All of these events allow us to share information, but more important, to receive feedback from our constituents. Another way that NCCI receives feedback on the services we provide our customers is through a series of annual surveys of carriers and regulators. We dig deep to monitor the quality of support and information we provide and the value we bring to the industry. And we get an honest assessment from our key constituents of how we are doing.

Our most recent survey revealed that many customers remain concerned about rate adequacy; the economic environment; medical cost inflation; and regulatory, legislative, and political stability. The importance of NCCI’s knowledge and expertise, the need for consistent provision of our core services, and the importance of our positive working relationships were also noted.

Obviously, clear communication and the development of effective customer tools are vital to meeting the demands of our diverse customer base. Throughout the year, NCCI conducts many conferences, training sessions, and one-on-one meetings. We also work very hard to provide an array of effective Web-based tools and services that enhance the functioning of the workers compensation system.

Some of the most popular products and tools are those that underwriting staff, data reporters, and actuaries at our carrier partners use every day to execute their work.

For example, our *RiskWorkstation* tool is used by underwriters and agents to evaluate risk information, analyze financial data, and get experience mod and worksheet information all in one place. And *WorkComp Workstation* can be used to complete a comparative analysis of a company’s results to those of the aggregated market by state or by class of business.

We also have tools to provide proof of coverage (POC) information, to report and correct data submissions, and to facilitate the smooth functioning of the residual market. And we are working to improve the access to and functionality of our circulars and manuals for all users.

We recognize that there is extensive content on ncci.com, so improvements to our search tools are under way to allow users to find the right information easily and quickly.

As always, our ASEs (affiliate services executives) and SREs (state relations executives) are available to all of our constituents to help them get the information they need.

Finally, I want to note the tremendous success of the webinars that NCCI has offered on our website over the last few years. Carriers and other industry stakeholders are using them for new hire training, for ongoing development and refresher courses for existing staff, and as tools for agent engagement. A link to a webinar can easily be attached to an email and forwarded as part of regular communication.

Today, NCCI offers more than 60 webinars that are accessible to all—a password is not necessary—and they are reasonably short, about 20 minutes in length. They cover powerful topics, ranging from details on the workings of the experience rating and classification systems to how the ratemaking process works to the impact of last year’s split point change, and much, much more.

Effective customer communication and engagement remain a top NCCI priority. As 2013 progresses, we are committed to growing and improving the tools, resources, and information our customers require to ensure a smoothly functioning workers compensation system.