

Analysis of Loss Adjustment Expense Trends

Workers' Compensation Insurance Rating Bureau of California

Released: April 3, 2008

WCIRB California
525 Market Street, Suite 800
San Francisco, CA 94105-2767
Tel 415.777.0777
Fax 415.778.7007
wcirb@wcirbonline.org
www.wcirbonline.org

© 2008 Workers' Compensation Insurance Rating Bureau of California. All rights reserved.

No part of this work may be reproduced or transmitted in any form or by any means, electronic or mechanical, including, without limitation, photocopying and recording, or by any information storage or retrieval system without the prior written permission of the Workers' Compensation Insurance Rating Bureau of California (WCIRB), unless such copying is expressly permitted in this copyright notice or by federal copyright law.

Each WCIRB member company ("Company") is authorized to reproduce any part of this work solely for the following purposes in connection with the transaction of workers' compensation insurance: (1) as necessary in connection with Company's required filings with the California Department of Insurance; (2) to incorporate portions of this work, as necessary, into Company manuals distributed at no charge only to Company employees; and (3) to the extent reasonably necessary for the training of Company personnel. Each Company and all agents and brokers licensed to transact workers' compensation insurance in the state of California are authorized to physically reproduce any part of this work for issuance to a prospective or current policyholder upon request at no charge solely for the purpose of transacting workers' compensation insurance and for no other purpose. This reproduction right does not include the right to make any part of this work available on any Web site or through any computer or electronic means for any purpose.

Workers' Compensation Insurance Rating Bureau of California and WCIRB are registered trademarks of the WCIRB. The Workers' Compensation Insurance Rating Bureau of California logo, the WCIRB logo, WCIRB California, the WCIRB California logo, and WCIRB Online are service marks or trademarks of the WCIRB (collectively, the "WCIRB Marks").

WCIRB Marks may not be displayed or used in any manner without the WCIRB's prior written permission. Any permitted copying of this work must maintain any and all trademarks and/or service marks on all copies.

To seek permission to use any of the WCIRB Marks or any copyrighted material, please contact the Workers' Compensation Insurance Rating Bureau of California, 525 Market Street, Suite 800, San Francisco, California 94105-2767.

Table of Contents	Page
I. Executive Summary	1
II. Introduction and Background	4
III. Report Objectives	6
IV. Summary of Current LAE Trends	7
V. Impact of Recent Reform Legislation	13
VI. Analysis of Current LAE Projection Methodologies	20
VII. Alternatives to Current LAE Projection Methodologies	24
VIII. Conclusions and Recommendations	28
IX. Conditions and Limitations	30
X. Exhibits	31

I. Executive Summary

A. Introduction and Background

Recently, loss adjustment expense (LAE) ratios to loss have increased significantly, and the LAE projection has become a significantly greater component of the WCIRB's pure premium rate filing projections. Given (a) these post-reform increases in the ratios of LAE to loss, (b) historical differences in LAE trends relative to loss trends, (c) differences between the LAE projection methodologies in the WCIRB's pure premium rate filings and those used in California Department of Insurance (CDI) decisions, and (d) that it has been some time since the WCIRB has performed a comprehensive review of LAE projection methodologies, the WCIRB is undertaking an analysis of LAE trends and methodologies. This report summarizes the WCIRB's analysis.

B. Report Objectives

1. Compile, summarize and analyze the most current information available on statewide allocated loss adjustment expense (ALAE) and unallocated loss adjustment expense (ULAE) experience.
2. Identify and analyze the potential factors contributing to the recent post-reform sharp increases in the ratio of LAE to loss.
3. Assess the accuracy of current LAE projection methodologies.
4. As appropriate, recommend enhancements to the current LAE projection methodologies to improve the accuracy of future LAE projections.

C. Principal Conclusions and Recommendations

1. Summary of Current LAE Trends
 - a. Unlike losses, calendar year ALAE and ULAE incurred amounts have not declined subsequent to reform. As a result, both have increased significantly as a percentage of calendar year losses.
 - b. Given State Compensation Insurance Fund's (SCIF's) unique characteristics, the manner in which SCIF's defense costs are reported, and the rapid shifts in SCIF's market share, recent SCIF LAE experience has differed significantly from the average LAE experience of the private insurers. It is not clear that the circumstances which produced these differences will continue into the future and, as a result, excluding SCIF's historical LAE experience in projecting future overall LAE provisions may be appropriate.
 - c. Historical changes in calendar year incurred ALAE and ULAE have not been well correlated with changes in calendar year incurred losses.
 - d. Historical changes in calendar year incurred ALAE have not been well correlated with changes in ultimate indemnity claim counts, while changes in calendar year ULAE have been fairly well correlated.
 - e. The average statewide ALAE paid per reported indemnity claim has generally been increasing. However, the most recent increases in average ALAE per claim have been driven primarily by SCIF's experience. The average ALAE paid per reported

indemnity claim excluding SCIF's experience has declined moderately over the last several years.

- f. Statewide ratios of ULAE per claim have increased following the reforms. However, ULAE costs per weighted indemnity claim excluding SCIF's experience, after increasing immediately following the reforms, have recently begun to decline modestly.

2. Impact of Recent Reform Legislation

- a. Among the factors related to the recent reforms that would tend to reduce LAE costs are declining claim frequency, the elimination of vocational rehabilitation, and the reduction of Labor Code Section 5814 penalties.
- b. The recent reforms have provided insurers with new tools whose application have reduced the cost of losses. However, implementation of these tools has increased the cost of administering and adjusting claims as the reforms have added significant complexities to this process — potentially affecting both ALAE and ULAE costs.
- c. Among the reform-related factors that would tend to increase ALAE are increased disputes over medical treatment, disputes related to apportionment, issues related to the January 1, 2005 Permanent Disability Rating Schedule (PDRS), and litigation related to other reform issues.
- d. Among the reform-related factors that would tend to increase ULAE are the medical treatment review process, additional complexities related to the indemnity benefit process, and changes in average claim adjuster case loads.
- e. Some of the post-reform increases in the cost of LAE per claim are likely associated with resolving transitional reform issues that will not impact the cost of future injuries. In fact, paid LAE severities (excluding SCIF's experience) on the 2005 and 2006 years are less than those on the initial post-reform peaks in 2003 and 2004.
- f. LAE costs per claim could continue to decline in subsequent years as more of the legal challenges to the reform provisions are resolved and the remaining significant uncertainties surrounding the reforms are alleviated. However, it is also possible, depending on how various legal issues are resolved, that LAE costs could increase. LAE costs should continue to be closely monitored.

3. Analysis of the Historical Accuracy of Current LAE Projection Methodologies

- a. ULAE projections based on historical calendar year ratios to incurred losses are appropriate when the experience has been stable and there is no appreciable change expected for the projection year. However, during the recent turbulent periods where there have been dramatic and sudden changes in loss experience, historical calendar year ratios of ULAE to loss were not good predictors of future ULAE ratios.
- b. Current ALAE development projections based on either historical ALAE development or historical development in the ratios of paid ALAE to paid indemnity losses have accurately projected ALAE development.

- c. Since changes in ALAE levels by year have not correlated well with changes in loss levels by year, projecting future policy year ALAE levels based on historical estimates of the ratios of ultimate accident year ALAE to ultimate losses had mixed results.
4. Potential Alternative LAE Projection Methodologies
 - a. Inasmuch as the current method did not accurately predict future policy year ratios of ULAE to loss, alternative ULAE projection methodologies that attempt to relate ULAE incurred amounts to components other than calendar year incurred losses should be considered.
 - b. Alternative ALAE projection methodologies based on the relationship of ALAE amounts to estimated claim counts should be used to augment current ALAE projection methodologies.

II. Introduction and Background

LAE is incurred by insurers in investigating, administering and settling workers' compensation claims. There are two components of LAE. ALAE includes the costs associated with handling claims that can be directly allocated to a particular claim. ULAE includes the costs associated with handling claims that cannot be directly allocated to a particular claim.

Section 11730 of the California Insurance Code provides that the advisory pure premium rates include provision for LAE. As a result, pure premium rate filings have included a projection of the LAE anticipated to be incurred in the policy year for which pure premium rates are being proposed. The pure premium rate filings include separate projections for ALAE and ULAE.

Projections of ALAE have been based primarily on accident year paid ALAE amounts reported by insurers on a quarterly basis to the WCIRB. Additionally, insurers report ALAE amounts paid per claim on unit statistical submissions made in accordance with the *California Workers' Compensation Uniform Statistical Reporting Plan—1995* (USRP) as well as calendar year aggregate incurred ALAE to the WCIRB.

ULAE, by definition, is not available at a detailed, claim-specific basis. Projections of ULAE have been based on calendar year aggregate incurred ULAE reported annually by insurers in response to the WCIRB's annual call for expense information. ALAE and ULAE amounts are reported to the WCIRB in accordance with detailed definitions included in the USRP. The current USRP definitions of ALAE and ULAE are shown in Exhibit 1.

Generally, projections of the ALAE component of proposed pure premium rates have been derived by combining the results of separate projections based on (a) analysis of historical patterns of accident year paid ALAE development and (b) analysis of historical patterns of the ratio of accident year paid ALAE to accident year paid indemnity losses.¹ Projections of the ULAE component of proposed pure premium rates have been based on averages of historical statewide calendar year ratios of incurred ULAE to incurred losses.² For informational purposes, pure premium rate filings have also included a number of alternative LAE projections based on actuarial assumptions that differ from those upon which the proposed pure premium rate projection was predicated.

For a number of years, the LAE methodologies underlying the CDI's pure premium rate decisions have differed from those reflected in the pure premium rate filings.³ In the CDI's decision with respect to the proposed January 1, 2008 pure premium rates, the WCIRB was directed to continue its analysis of LAE projection methodologies.

LAE projections reflected in the proposed pure premium rates rely, to a large extent, on the relationship between LAE amounts and loss amounts paid or incurred over the same period. Chart 1 shows historical ratios of calendar year LAE incurred to calendar year incurred losses. As shown, in the early 1990s, the LAE ratio increased inasmuch as LAE amounts did not decline with the decline in loss amounts. Conversely, in the latter part of the 1990s when medical costs rose sharply, LAE did not increase commensurately, and the ratio of LAE to loss declined. Finally, in the last several years, post-reform losses declined dramatically while LAE

¹ In the WCIRB's January 1, 2008 pure premium rate filing, the ALAE provision was based on the average of these two methodologies, with projected age-to-age development factors predicated on the most recent historical factor.

² In the WCIRB's January 1, 2008 pure premium rate filing, the ULAE provision was set equal to the most recent (2006) calendar year ratio of incurred ULAE to incurred losses.

³ In the CDI's decision on the WCIRB's January 1, 2008 pure premium rate filing (File No. Reg-2007-00053), the CDI predicated the approved pure premium rates on an analysis excluding the experience of State Compensation Insurance Fund.

amounts were relatively constant. As a result, the ratio of LAE to loss increased sharply to more than twice the pre-reform level (29.4% versus 12.4%).

Chart 1. Historical LAE as a Percentage of Losses

Calendar Year	ALAE as % of Loss	ULAE as % of Loss	Total LAE as % of Loss	Year-to-Year Change
1987	N/A	N/A	14.0%	10.2%
1988	N/A	N/A	15.2%	8.6%
1989	N/A	N/A	15.5%	2.0%
1990	N/A	N/A	15.7%	1.3%
1991	N/A	N/A	15.8%	0.6%
1992	10.6%	9.3%	19.9%	25.9%
1993	10.8%	12.7%	23.5%	18.1%
1994	14.2%	16.7%	30.9%	31.5%
1995	8.7%	18.2%	26.9%	-12.9%
1996	9.5%	13.9%	23.4%	-13.0%
1997	8.9%	13.2%	22.1%	-5.6%
1998	8.4%	14.3%	22.7%	2.7%
1999	9.9%	9.1%	19.0%	-16.3%
2000	7.3%	9.0%	16.3%	-14.2%
2001	4.1%	8.3%	12.4%	-23.9%
2002	5.9%	6.5%	12.4%	0.0%
2003	6.2%	7.4%	13.6%	9.7%
2004	8.6%	8.8%	17.4%	27.9%
2005	9.7%	11.0%	20.7%	19.0%
2006	14.3%	15.1%	29.4%	42.0%

Major reform legislation was enacted in 2002, 2003, and 2004 — including Assembly Bill No. 749 (AB 749), Assembly Bill No. 227 (AB 227), Senate Bill No. 228 (SB 228) and Senate Bill No. 899 (SB 899). The WCIRB's cost evaluations of these bills projected significant reductions in loss levels in its prospective evaluations of the cost impact of these reforms that were reflected in pure premium rate filing submissions.⁴ In addition, these evaluations reflected the assumption that loss adjustment expenses would change proportionately with losses, implying an approximate 30% decline in LAE due to the series of legislative reforms. However, as shown in the WCIRB's 2007 Legislative Cost Monitoring Report,⁵ calendar year LAE incurred amounts have not declined at all despite sharp post-reform decline in claim frequency and claim severity. It is not clear to what extent this post-reform increase in the ratio of LAE to losses is the result of transitional issues impacting LAE incurred amounts that are related to the implementation of the reform measures, and to what extent they are related to permanent changes that will continue to impact future LAE costs.

Given (a) the post-reform increases in the ratios of LAE to loss, (b) historical differences in LAE trends relative to loss trends, (c) differences between the LAE projection methodologies used in the pure premium rate filings and those used in CDI decisions, and (d) that it has been many years since a comprehensive review of LAE projection methodologies has been conducted, the WCIRB has undertaken an analysis of LAE trends and methodologies. This report summarizes the WCIRB's analysis.

⁴ See the WCIRB's cost evaluation of AB 749 (published July 24, 2002), the WCIRB's amended January 1, 2004 pure premium rate filing submitted on November 3, 2003, and the WCIRB's amended July 1, 2004 pure premium rate filing submitted on May 13, 2004.

⁵ See the WCIRB's 2007 *Legislative Cost Monitoring Report*, published on October 9, 2007.

III. Report Objectives

1. Compile, summarize and analyze the most current information available on statewide ALAE and ULAE experience.
2. Identify and analyze the potential factors contributing to the recent post-reform sharp increases in the ratio of LAE to loss.
3. Assess the accuracy of current LAE projection methodologies.
4. As appropriate, recommend enhancements to the current LAE projection methodologies to improve the accuracy of future LAE projections.

IV. Summary of Current LAE Trends

As shown in Chart 1, calendar year LAE amounts as a percentage of incurred losses have increased sharply following the reforms of 2003 and 2004. The impact of the recent reform legislation on these LAE trends is discussed in Section V. To better understand other factors that may be driving these increases in the ratio of LAE to incurred losses, a number of components and characteristics related to these LAE trends were reviewed. The principal findings and observations are summarized below.

A. Experience by Type of Insurer

Chart 2 summarizes recent calendar year ratios of ALAE to loss by type of insurer separately for SCIF, other California insurers, national or multi-state insurers, all insurers, and all insurers excluding SCIF.⁶

Chart 2. Ratio of Incurred ALAE to Incurred Loss

Calendar Year	SCIF	Other CA ⁷	National ⁸	Statewide	Statewide without SCIF
2002	4.1%	7.4%	7.6%	6.3%	7.6%
2003	4.3%	8.3%	7.1%	6.2%	7.2%
2004	5.6%	7.1%	11.0%	8.6%	10.6%
2005	5.3%	14.4%	12.4%	9.7%	12.7%
2006	3.7%	20.3%	20.0%	14.3% ⁹	20.0%
Average	4.6%	11.5%	11.6%	9.0%	11.6%

As shown in Chart 2, SCIF has markedly lower historical ratios of calendar year incurred ALAE to incurred loss than those of other California or national insurers—whose ratios were comparable. In addition, while other California and national insurers experienced significant increases in the ratio of calendar year incurred ALAE to incurred loss during the post-reform years, SCIF's ALAE ratio declined in 2006.

Chart 3 summarizes recent calendar year ratios of ULAE to loss for the same insurer groupings reflected in Chart 2.

Chart 3. Ratio of Incurred ULAE to Incurred Loss

Calendar Year	SCIF	Other CA	National	Statewide	Statewide without SCIF
2002	7.2%	10.1%	5.9%	6.6%	6.3%
2003	10.2%	7.9%	5.6%	7.4%	5.8%
2004	10.2%	12.3%	7.4%	8.8%	7.8%
2005	15.6%	11.8%	7.4%	11.0%	8.0%
2006	28.0%	20.9%	7.9%	15.1%	9.9%
Average	14.2%	12.6%	6.8%	9.8%	7.6%

⁶ In 2006, SCIF wrote 21% of the statewide market, insurers identified as "Other California" wrote 15%, and insurers identified as "National" wrote 64% of the market.

⁷ "Other CA" is defined as private insurer groups, other than State Compensation Insurance Fund, which underwrote at least 80% of their workers' compensation business in California in a particular calendar year.

⁸ National insurers are defined as private insurer groups, which underwrote less than 80% of their workers' compensation business in California for a particular calendar year.

⁹ Excludes experience of an insurer whose ALAE data for 2006 is known to be anomalous.

Chart 3 shows that, unlike for ALAE, SCIF's ratios of ULAE to losses are almost twice as high as the average for all other insurers, and have experienced a dramatic increase in recent years. Also, other California insurers' ratios of calendar year incurred ULAE to incurred loss have traditionally been higher than those of national insurers and have recently increased.

As shown in Chart 3, SCIF's ULAE as a percentage of losses has increased at a much more rapid rate than for other insurers. In fact, much of the sharp increase in statewide ULAE ratios is attributable to the inclusion of SCIF's ULAE experience. Additionally, as shown in Chart 2, SCIF's ratios of ALAE to loss are far lower than those incurred by other insurers and its 2006 ratio of ALAE to loss has declined while the analogous average 2006 ratio for the private insurers has increased significantly. In the CDI's decision with respect to the proposed January 1, 2008 pure premium rates, the CDI expressed concerns with respect to the rate at which SCIF has reduced claims staff in light of its declining market share and declining statewide claim frequency. As a result, the approved pure premium rates effective January 1, 2008 were computed by excluding SCIF's LAE experience.

Unlike many other insurers, SCIF makes extensive use of in-house defense counsel. Consistent with requirements of the USRP (see Exhibit 1), SCIF attempts to reassign the cost of in-house defense counsel to accident year and calendar year ALAE amounts. However, given SCIF's somewhat anomalous ALAE and ULAE ratios, it is not clear if the reassigned in-house defense counsel costs are consistent with the reported defense costs of insurers that rely primarily on outside defense counsel.

Given the unique characteristics of SCIF's operations as discussed in the most recent CDI pure premium rate decision, reporting issues related to in-house defense counsel costs, recent changes in SCIF's market share, and the current sharp increase in SCIF's ULAE ratios, it is not clear that the circumstances that produced the differences between SCIF's LAE experience and that of the private insurers will continue into the future. As a result, excluding SCIF's historical LAE experience in projecting future overall LAE provisions may be appropriate.

B. Changing Insurer Mix

The market share of many California workers' compensation insurers has dramatically changed over the last few years. With the widely divergent LAE ratios among the different types of insurers demonstrated in Charts 2 and 3 above, the statewide average LAE ratios can be significantly impacted by changes in the market share of various insurers for any given year.

Charts 4 and 5 below compare the actual statewide ratios with those for which the market share for each insurer for each year is held constant at the calendar year 2006 level for all years shown.

Chart 4. Ratio of Incurred ALAE to Incurred Loss

Calendar Year	Weighted Average ¹⁰	Controlled for Insurer Mix ¹¹
2002	6.3%	8.8%
2003	6.4%	9.5%
2004	8.5%	9.9%
2005	9.7%	9.4%
2006	14.3%	14.3%
Average	9.0%	10.4%

Chart 5. Ratio of Incurred ULAE to Incurred Loss

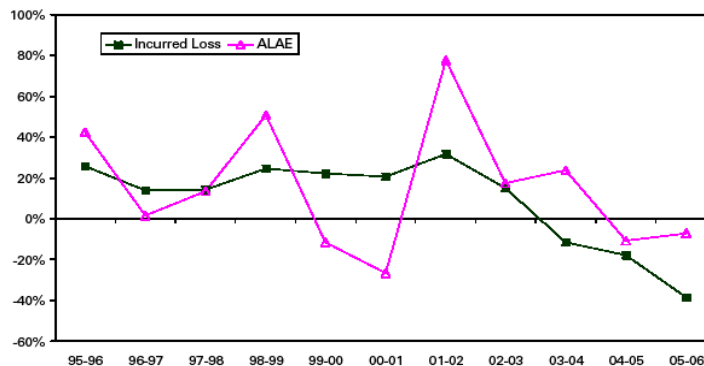
Calendar Year	Weighted Average ¹²	Controlled for Insurer Mix ¹³
2002	6.8%	4.6%
2003	7.5%	4.8%
2004	8.8%	8.6%
2005	11.2%	9.1%
2006	18.1%	18.1%
Average	10.5%	9.0%

As shown in Charts 4 and 5 above, controlling for recent changes in the market composition by insurer moderates the upward trend in the ratio of ALAE to loss but results in an acceleration of the trend in the growth of the ratio of ULAE to loss.

C. Relationship with Losses

The LAE projection methodologies have, to a large extent, been predicated on changes in the relationship between LAE and losses. Charts 6 and 7 below show the historical changes in calendar year incurred ALAE (Chart 6) and calendar year incurred ULAE (Chart 7) since 1995 as compared to changes in calendar year incurred losses.

Chart 6: Comparison of Year-to-Year Change between ALAE and Incurred Loss



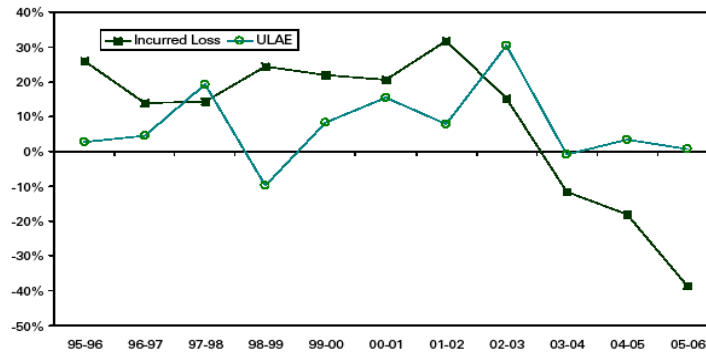
¹⁰ Excludes experience of an insurer whose LAE data for 2006 is known to be anomalous.

¹¹ Excludes experience of an insurer whose LAE data for 2006 is known to be anomalous.

¹² Excludes experience of an insurer whose LAE data for 2006 is known to be anomalous.

¹³ Excludes experience of an insurer whose LAE data for 2006 is known to be anomalous.

Chart 7: Comparison of Year-to-Year Changes between ULAE and Incurred Loss



As shown in Charts 6 and 7, over the last decade, changes in either calendar year ALAE or ULAE have not been well correlated with changes in incurred losses.

D. Relationship to Claim Counts

Charts 8 and 9 below show the historical changes in calendar year incurred ALAE (Chart 8) and ULAE (Chart 9) as compared to changes in ultimate claim counts since 1995.

Chart 8: Comparison of Year-to-Year Changes between ALAE and Ultimate Indemnity Counts

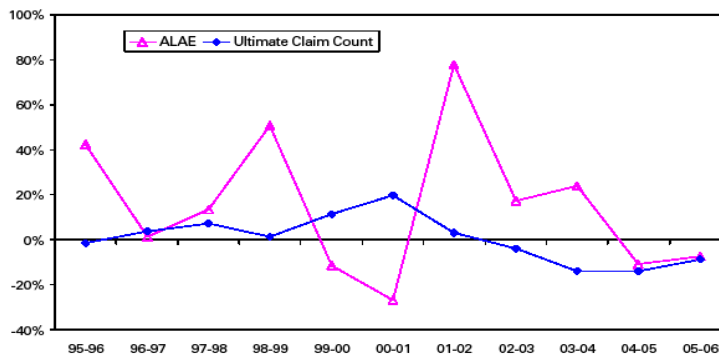
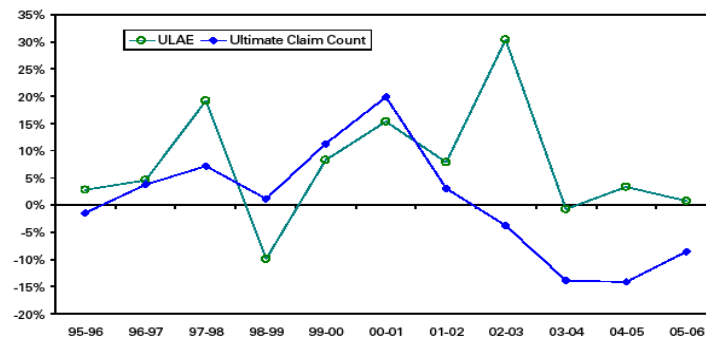


Chart 9: Comparison of Year-to-Year Changes between ULAE and Ultimate Indemnity Counts



As shown in Charts 8 and 9, while changes in calendar year incurred ALAE has not been well correlated with changes in ultimate claim counts (Chart 8), changes in calendar year incurred ULAE and changes in ultimate claim counts through 2002 were relatively well

correlated (Chart 9). Since 2002, however, ULAE has not declined commensurately with claim counts.

E. Average Cost per Indemnity Claim

Chart 10 shows the historical relationship of statewide accident year paid ALAE and reported accident year indemnity claim counts. Chart 11 shows the analogous information excluding the experience of SCIF.

Chart 10. Average Paid ALAE per Reported Indemnity Claim - Statewide

Accident Year	at 18 months	at 30 months	at 42 months	at 54 months
2000	594	1,145	1,636	2,012
2001	627	1,245	1,785	2,178
2002	718	1,538	2,181	2,651
2003	871	1,768	2,469	3,014
2004	928	1,833	2,606	
2005	952	1,877		
2006	1,070			

Chart 11. Average Paid ALAE per Reported Indemnity Claim – Excluding SCIF

Accident Year	at 18 months	at 30 months	at 42 months	at 54 months
2000	683	1,547	2,286	2,806
2001	950	2,280	3,312	4,029
2002	1,241	2,738	3,928	4,777
2003	1,430	3,056	4,326	5,275
2004	1,374	2,865	4,105	
2005	1,304	2,653		
2006	1,302			

As shown in Chart 10, the average statewide ALAE paid per reported indemnity claim has generally been increasing. However, as shown in Chart 11, the recent increases in average ALAE per claim have been driven primarily by SCIF's experience. After increasing sharply in 2002 and 2003, the average ALAE paid per reported indemnity claim excluding SCIF has generally been declining moderately over the last several years.

ULAE experience is not available on an accident year basis and, as a result, reported ULAE amounts do not correspond directly to reported accident year claim counts. Instead, Chart 12 compares the average calendar year incurred ULAE to a weighted indemnity claim count measure¹⁴ intended to reflect claims activity during the calendar year— both including and excluding SCIF's experience.

¹⁴“Weighted Indemnity Claim” is based on the sum of indemnity claims open at the beginning of the calendar year period and two times the newly-reported indemnity claims during that year.

Chart 12. Calendar Year ULAE per Weighted Indemnity Claim

Calendar Year	ULAE Per Weighted Indemnity Claim Statewide Experience	ULAE Per Weighted Indemnity Claim Excluding SCIF
2000	\$959	\$853
2001	\$1,036	\$801
2002	\$975	\$942
2003	\$1,376	\$1,210
2004	\$1,333	\$1,218
2005	\$1,417	\$1,027
2006	\$1,533	\$1,102

As shown in Chart 12, statewide ratios of ULAE per weighted claim have increased following reform. However, ULAE costs per weighted indemnity claim excluding SCIF's experience, after increasing immediately following the reforms, has recently begun to decline modestly.

V. Impact of Recent Reform Legislation

The reform legislation of 2002, 2003 and 2004 significantly reduced claim frequency as well as indemnity and medical loss severities. However, rather than declining with reduced claim and loss levels, post-reform calendar year ALAE and ULAE costs have remained relatively constant and the ratios of calendar year incurred ALAE and ULAE to incurred losses have increased. Chart 13 shows the history of calendar year incurred losses, ALAE and ULAE. Chart 14 shows the ratio of calendar year incurred LAE to incurred loss.

Chart 13: Calendar Year Losses and LAE Incurred

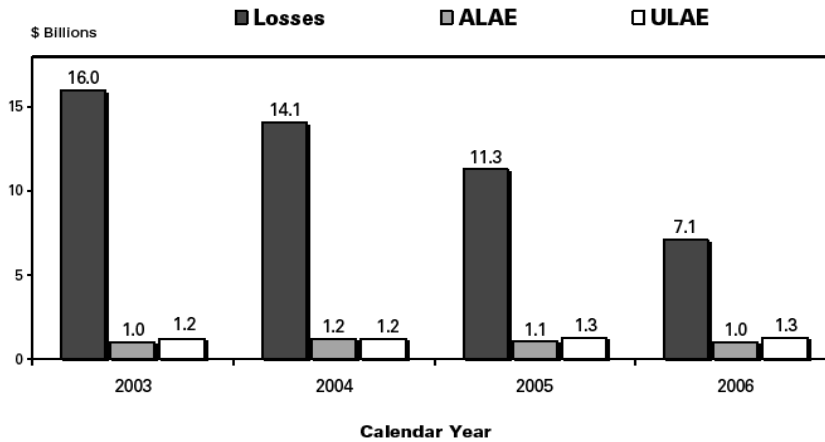
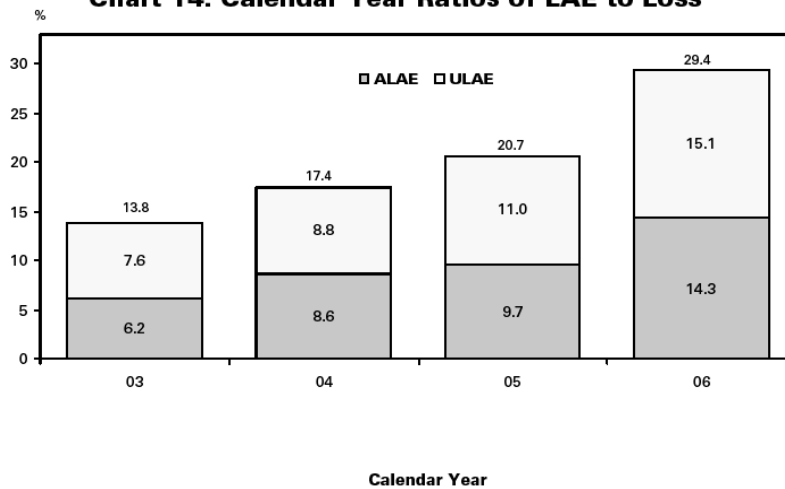


Chart 14: Calendar Year Ratios of LAE to Loss

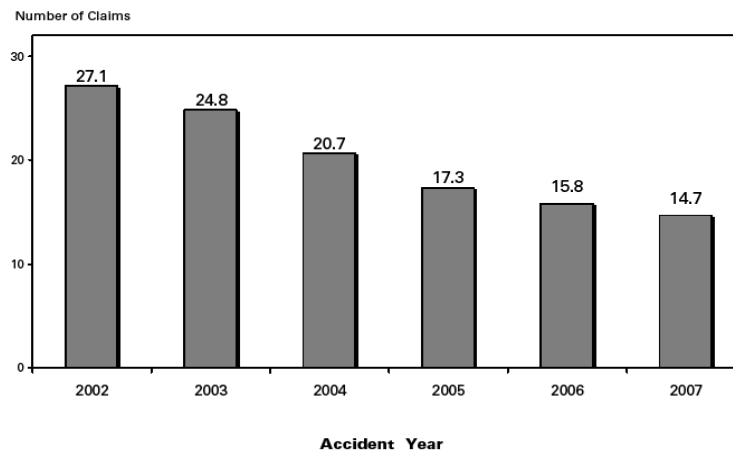


The reforms of 2002 through 2004 have radically changed the manner in which claims are adjusted and administered in California. While the cost of many loss components have been significantly reduced, it is not immediately evident how the reforms have impacted LAE. Some of the recent legislative reforms have tended to reduce LAE levels, while others have tended to increase LAE.

A. Recent Reform Factors Tending to Decrease LAE

1. Reduced Claim Frequency. As shown in Chart 15, claim frequency has dropped sharply subsequent to reform, which should, all else being equal, translate into reduced LAE.

Chart 15: Estimated Ultimate Indemnity Claims Per 1,000 Full-Time Employee Equivalents



2. Elimination of Vocational Rehabilitation Services. AB 227 and SB 228 have dramatically limited the scope of vocational rehabilitation services. The WCIRB's latest legislative cost monitoring report suggests a post-reform reduction in vocational rehabilitation costs of approximately 80%.¹⁵ In addition to impacting the cost of benefits, the vocational rehabilitation reforms also impacted the cost of administering claims.
3. Reduced Labor Code Section 5814 Penalties. SB 899 changes with respect to Labor Code Section 5814 penalties are likely to have also reduced claims administrative expenses.

B. Recent Reform Factors Tending to Increase ALAE

As shown in Charts 13 and 14, calendar year incurred ALAE amounts have remained constant. However, ALAE as a percentage of incurred losses has been increasing significantly, despite a reduction in claim frequency (see Chart 15). As shown in Chart 11 above, average accident year ALAE paid per claim, excluding SCIF's experience, increased sharply during the 2002 to 2004 reform period and then began to decline moderately. However, average paid amounts for the most recent post-reform accident years are still higher than during the pre-reform period.

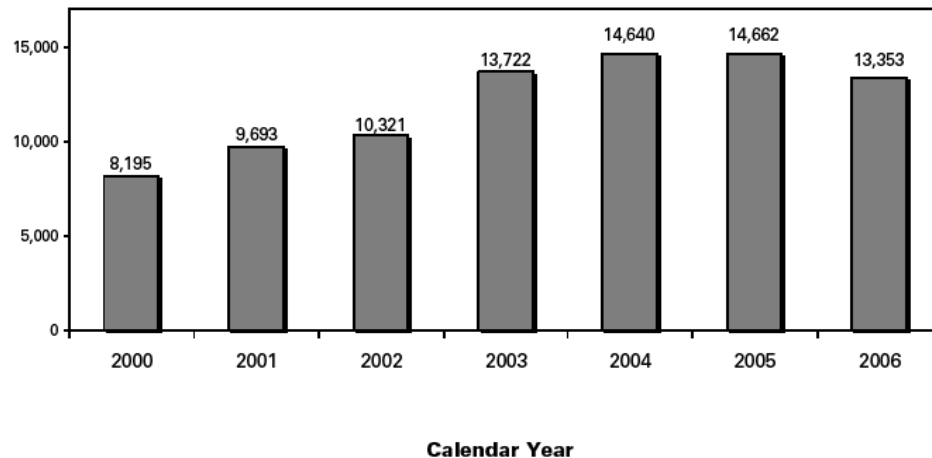
The considerations tending to increase the post-reform accident year paid ALAE include the following:

1. Resolution of Medical Treatment Disputes. SB 228 and SB 899 included a number of provisions related to the authorization of medical treatment. Prior to reform, a legal presumption was provided to the primary treating physician as to medical treatment issues. As a result, the insurer challenged the course of medical treatment only in relatively limited circumstances and, in many instances, the medical cost containment process consisted of reviewing and paying medical bills. The SB 228 and SB 899 reforms have provided insurers and employers with new tools to better manage

¹⁵ See the WCIRB's 2007 Legislative Cost Monitoring Report (pages 12 and 13), published on October 9, 2007.

medical costs through medical provider networks and utilization review. Use of these tools has reduced medical utilization and the medical losses in the system, but has increased what insurer claims departments must do to effectively manage medical costs. This impacts ALAE through additional hearings to resolve medical disputes. Most medical treatment issues are resolved through the WCAB's expedited hearing process. Chart 16 shows that despite significantly declining claim volume, expedited hearings increased every year through 2005 before declining somewhat in 2006.¹⁶

Chart 16: Number of Statewide Expedited Hearings



2. Apportionment. SB 899 allows for the apportionment of the permanent disability award to causation. Apportionment, which was not frequently used to reduce permanent disability awards prior to the reforms, has now become a significant issue and is frequently subject to litigation. Estimates of the proportion of post-reform permanent disability claims involving apportionment issues range from 8% to 10%.¹⁷
3. January 1, 2005 Permanent Disability Rating Schedule (PDRS). The January 1, 2005 PDRS, which was adopted pursuant to SB 899, significantly changed the manner in which permanent disability ratings are determined in California. The uncertainty arising from the new schedule has likely impacted ALAE costs through increased insurer referrals to outside counsel and litigation. In addition, the January 1, 2005 PDRS has been under a variety of administrative and legal challenges as to its constitutionality, its applicability to pre-January 1, 2005 injuries, and the impairment ratings generated under the new schedule.
4. Other Litigation. In addition to litigation over issues such as medical treatment, apportionment and permanent disability, many of the critical legislative changes and their implementation regulations have been the subject of multiple legal challenges as to their constitutionality or legality. In total, litigation in the system has appeared to increase. Chart 17 shows the number of Workers' Compensation Appeals Board (WCAB) hearings per calendar year.¹⁸ As shown in Chart 17, the number of Division of Workers' Compensation (DWC) hearings has continued to increase subsequent to the

¹⁶ Source: *Commission on Health and Safety and Workers' Compensation 2007 Annual Report* (page 213), published in December of 2007.

¹⁷ See the WCIRB's *2007 Legislative Cost Monitoring Report* (pages 13 and 14), published on October 9, 2007.

¹⁸ Source: *Commission on Health and Safety and Workers' Compensation 2007 Annual Report* (page 213), published in December of 2007.

reforms despite sharp reductions in claim frequency (see Chart 15). Similarly, Charts 18 and 19, which are compiled from aggregate calendar year information reported to the WCIRB, show that calendar year defense attorney expenses paid (Chart 18) and applicant attorney fees paid (Chart 19) have increased subsequent to the reforms.¹⁹

Chart 17: Number of Statewide WCAB Hearings

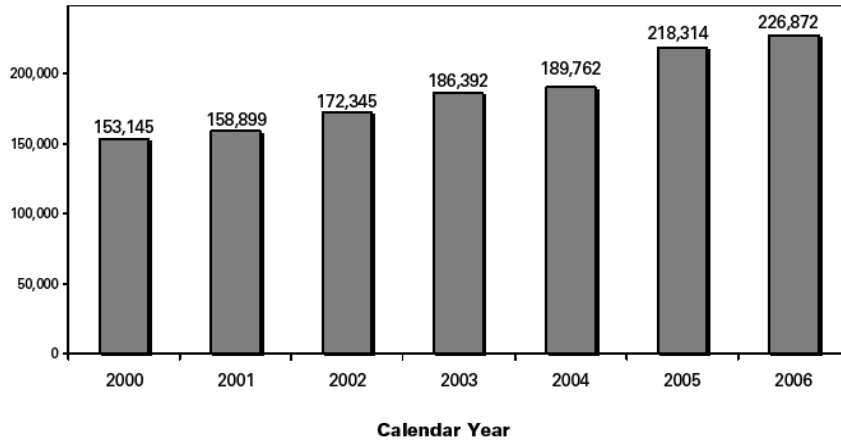
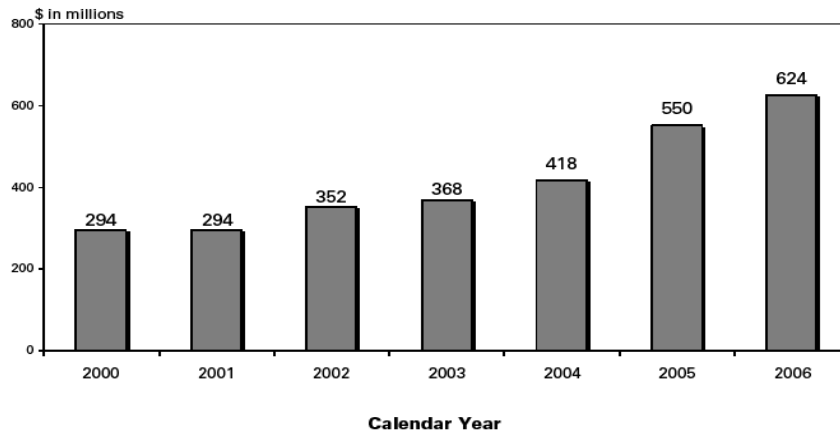
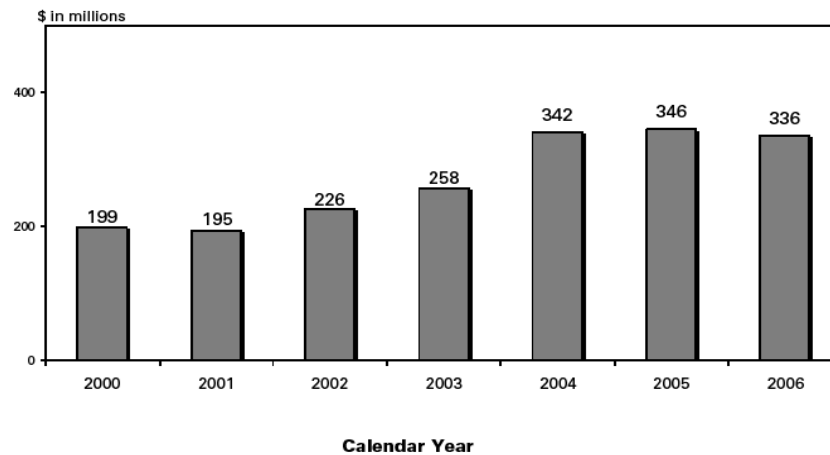


Chart 18: Reported Total Defense Expenses Paid



¹⁹ See the WCIRB's *Report on 2006 California Workers' Compensation Losses and Expenses*, published on June 18, 2007.

Chart 19: Reported Total Applicant Attorney Fees Paid

It is clear that some of the legal issues giving rise to increased litigation, such as the applicability of the January 1, 2005 PDRS or the medical provider network provisions of SB 899 to pre-January 1, 2005 injuries, will not impact the cost of later injuries. In addition, some of the legal questions related to the reforms, such as the apportionment formula, appear to be resolved. However, many other issues have not been resolved and will continue to impact litigation and ALAE costs. It is possible, depending on how certain issues are resolved, that ALAE costs per claim could again increase. For example, if additional expert testimony by economists and vocational rehabilitation experts as to the extent of loss of future earnings capacity becomes common in disputes related to permanent disability ratings,²⁰ ALAE costs per claim could increase.

The costs associated with resolving transitional reform issues did not impact the cost of injuries occurring in 2006 to the same extent as earlier injuries. As shown in Chart 11, paid ALAE per claim on 2005 and 2006 injuries, excluding SCIF's experience, is less than that on 2003 and 2004 injuries. ALAE costs per claim could continue to decline in subsequent years as more of the legal challenges to the reform provisions are resolved and the remaining significant uncertainties surrounding the reforms are alleviated. However, as noted above, depending on how various legal issues are resolved, ALAE costs could increase.²¹ It is recommended that ALAE costs continue to be closely monitored.

C. Recent Reform Factors Tending to Increase ULAE

As shown in Charts 13 and 14, incurred ULAE amounts have remained relatively constant, but have increased significantly as a percentage of incurred losses. Chart 12 above shows the ratio of ULAE to weighted indemnity claims. As with ALAE, the average 2006 ULAE per claim, excluding SCIF's experience, increased during the 2002 to 2004 reform period and then began to decline moderately. However, the 2006 ULAE incurred per claim is still higher than during the pre-reform period.

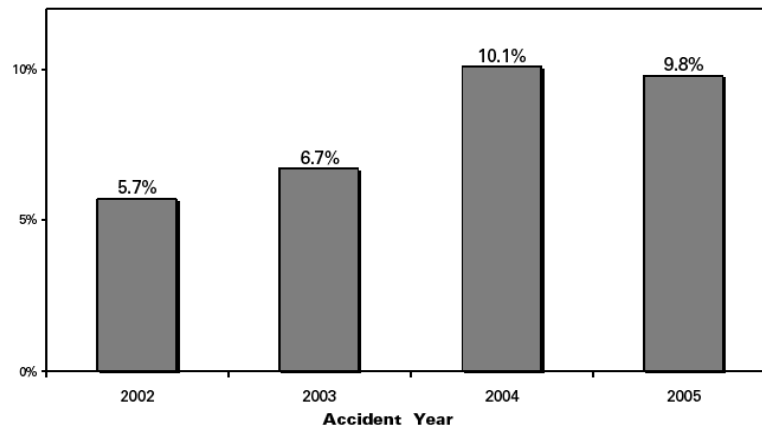
²⁰ In *Joey M. Costa v. Hardy Diagnostic and State Compensation Insurance Fund* (2006) 71 CCC 1797, the Appellate Court found that the Legislature intended to continue to allow the parties the opportunity to present rebuttal evidence to ratings under the new PDRS.

²¹ It should also be noted that depending on how various legal issues are resolved, medical and/or indemnity losses could also increase.

The considerations tending to increase the post-reform calendar year incurred ULAE include the following:

1. **Medical Review Process.** As previously discussed, SB 228 and SB 899 provided insurers with greater opportunities to review suggested courses of medical treatment and assess whether such treatment is appropriate. These legislative changes have significantly reduced the level of medical treatment in the system, but have increased the cost of the medical cost containment process. Many medical cost containment expenses (e.g., formal utilization review completed by a physician) are generally reported in California as medical loss. However, other costs that typically cannot be allocated to a claim file, such as an assessment of which medical treatments should be subject to formal utilization review by a claims adjuster or on-staff registered nurse, are reported as ULAE. Chart 20 shows the accident year ratio of paid medical cost containment to paid medical loss as compiled by the California Workers' Compensation Institute (CWCI). As shown, the ratio of medical cost containment to medical loss has increased significantly subsequent to reform.²²

Chart 20: Medical Cost Containment as a Percent of Paid Losses at 18 Months



2. **Indemnity Claim Process.** As with ALAE, ULAE has also been impacted by recent legislative reforms related to apportionment and permanent disability since the internal claims processes involved have become more complex as insurer claims adjusters must consider relatively new issues such as apportionment to non-work-related causation and adjustments to weekly permanent disability benefits based on return-to-work status. In addition, the immediate medical paid provisions of SB 899 (Labor Code Section 5402) have increased the burden on insurer claims departments to promptly investigate claims to determine compensability issues.
3. **Average Caseloads.** With the sharp decline in claim frequency, there is anecdotal evidence that the typical average caseload per claims adjuster has declined. However, given the increased complexity of the claims process and the common pre-reform perception that average caseloads may have been too high to ensure optimal claims handling, a decrease in average caseload may be appropriate.

²² See Attachment J of the WCIRB's 2007 *Legislative Cost Monitoring Report* (pages 13 and 14), published on October 9, 2007.

In summary, post-reform ULAE has been impacted by many of the same factors that have impacted post-reform ALAE. The largest component of ULAE is the cost of administering and adjusting claims. The reforms have provided insurers with new tools that have reduced the cost of losses. However, implementation of these tools has impacted the cost of administering and adjusting claims as the reforms have added significant complexities to this process. Some of these ULAE costs may be transitional and could decline in the future. In fact, on a per-claim basis (excluding SCIF's experience), there is evidence of a ULAE decline in 2005 and 2006. Conversely, other reform components, such as those related to the medical treatment process, are likely to be permanent components of the system. As with ALAE costs, it is recommended that ULAE costs continue to be closely monitored.

VI. Analysis of Current LAE Projection Methodologies

Historically, the ALAE and ULAE components reflected in the proposed pure premium rates were projected separately. ULAE was projected by averaging the most recent historical calendar year ratios to incurred losses. ALAE was projected by averaging the results of applying two accident year development methods: one based purely on paid ALAE development, and the other on development of the ratio of paid ALAE to paid indemnity loss.

To gauge the predictive accuracy of these methods, a retrospective analysis that compares projections based on these methods to actual emergence of ALAE and ULAE costs is presented below.

A. Accuracy of ULAE Projections

For a number of years, the future policy year ratio of ULAE to loss was projected by averaging the ratios of the latest two historical calendar year ratios. However, as the ratio of ULAE to losses increased significantly over the last several years, this approach understated ULAE levels. As a result, the proposed January 1, 2008 pure premium rates projected that the ratio of policy year 2008 ULAE to losses would be equal to the 2006 calendar year ratio – the latest available historical calendar year data.

Chart 21 compares actual policy year ratios of ULAE to incurred loss that emerged with projections based on a two-year average and the latest year of historical calendar year ULAE to incurred loss ratios.

Chart 21. ULAE to Loss Projections – Historical Accuracy

Policy Year	Actual ULAE as % of Losses	Projection Based on Average of Two Calendar Years	Two-Year Projection Pct. Point Error	Projection Based on Latest Calendar Year	Latest Year Projection Pct. Point Error
1992	11.0%	—	—	—	—
1993	14.7%	—	—	—	—
1994	17.5%	—	—	—	—
1995	16.1%	11.0%	-5.1	12.7%	-3.4
1996	13.6%	14.7%	+1.1	16.7%	+3.1
1997	13.8%	17.5%	+3.7	18.2%	+4.4
1998	11.7%	16.1%	+4.4	13.9%	+2.2
1999	9.1%	13.6%	+4.5	13.2%	+4.1
2000	8.7%	13.8%	+5.1	14.3%	+5.6
2001	7.4%	11.7%	+4.3	9.1%	+1.7
2002	7.0%	9.1%	+2.1	9.0%	+2.0
2003	8.1%	8.7%	+0.6	8.3%	+0.2
2004	9.9%	7.4%	-2.5	6.5%	-3.4
2005	13.1%	7.0%	-6.1	7.4%	-5.7

ULAE projections based on historical calendar year ratios of ULAE to incurred losses are generally believed to be appropriate when experience is relatively stable and there is no appreciable change expected for the future projection period. However, during turbulent periods, such as over the last decade, where there have been dramatic and sudden changes in loss experience that may not be reflected in commensurate changes in ULAE, historical calendar year ratios of ULAE to loss are not good predictors of future ULAE

ratios. In other words, since 1995, changes in calendar year losses have not been well correlated with changes in calendar year ULAE. (See Chart 7 above.)

B. Accuracy of ALAE Projections

For a number of years, the ALAE component of proposed pure premium rates was projected by averaging two separate projections—one based on accident year paid ALAE development and the second based on development of accident year paid ALAE to paid indemnity ratios. A retrospective analysis of the predictive accuracy of each of these two methods is presented below.

1. Paid ALAE Development Method

In recent pure premium rate filings, the most recent year's ALAE development factors have been selected to develop ALAE to an ultimate basis. Exhibit 2 presents a retrospective analysis of the accuracy of historical ALAE development factors as predictors of future development. This analysis shows that the most recent historical development factors were good predictors of actual development (average error was less than +/-1%).

While estimates of ultimate accident year ALAE based on paid ALAE development have been accurate, the ALAE provision in the proposed pure premium rates also depends upon projecting a future policy period's ratio of ALAE to loss based on these estimates of historical ultimate ALAE. In the most recent pure premium rate filing, this projection was based on the average of the latest three accident year estimates of ultimate ALAE to ultimate losses. In prior pure premium rate filings, other projection methodologies included the latest year ratio and applying a five-year exponential trend to the ratios of ultimate ALAE to ultimate losses. Chart 22 compares the ALAE projected using these three projection methods with the actual ratios to emerge in hindsight.

Chart 22. Paid ALAE Development Method Projections

Policy Year	Ultimate ALAE as % of On-Level Loss	Estimate Based on 3-Year Average ²³	3-Year Estimate Pct. Point Error	Estimate Based on Latest Year ²⁴	Latest Year Estimate Pct. Point Error	Trended Estimate ²⁵	Trended Estimate Pct. Point Error
1996	9.9	9.0	-0.9	7.9	-2.0	—	—
1997	10.7	8.4	-2.3	8.4	-2.3	—	—
1998	11.3	8.6	-2.7	9.4	-1.9	8.0	-3.3
1999	12.2	9.4	-2.8	10.4	-1.8	11.1	-1.1
2000	13.1	10.3	-2.8	11.0	-2.1	14.0	+0.9
2001	13.7	11.0	-2.7	11.5	-2.2	14.4	+0.7
2002	14.9	11.8	-3.1	13.0	-1.9	15.4	+0.5
2003	15.5	12.6	-2.9	13.2	-2.3	15.8	+0.3
2004	14.9	13.4	-1.5	14.1	-0.8	16.6	+1.7
2005	14.9	14.4	-0.5	15.8	+0.9	18.6	+3.7

²³ Projections were based on averaging the latest three historical ratios of ultimate ALAE to on-level losses available at the time. For example, the projection for policy year 1996 was based on averaging the policy year 1992 to 1994 ultimate ALAE ratios.

²⁴ Projections were based on the latest available historical ratio of ultimate ALAE to on-level losses available at the time. For example, the projection for policy year 1996 was based on the 1994 ultimate ALAE ratio.

²⁵ Projections were based on applying an exponential trend to the latest five historical ratios.

As shown in Chart 22, during the late 1990s and early 2000s when losses were deteriorating rapidly, ALAE did not increase commensurate with losses, and projections based on the three-year averages and latest year of historical accident year ultimate ratios understated ALAE. However, projections of ALAE as a percentage of losses based on the three-year average or latest year for the two post-reform years were relatively good predictors of actual emergence. By projecting historical growth in the ratio of ultimate ALAE to ultimate loss, the exponential trend projections accurately projected ALAE ratios in the early part of this decade, but overstated ALAE following the reform period.

2. Paid ALAE to Paid Indemnity Method

In recent pure premium rate filings, the most recent year's paid ALAE to paid indemnity ratio development factors were selected to develop an ultimate ratio of ALAE to indemnity. Exhibit 3 presents a retrospective analysis of the accuracy of these development factors. This analysis shows that the most recent historical development factors were also good predictors of actual development (average error was 1.1% or less).

While development projections based on the ratios of ultimate paid ALAE to paid indemnity were generally accurate, the accuracy of the ALAE provision in the proposed pure premium rates also depends upon projecting a future policy period's ratio of ALAE to loss based on these historical estimates of the ratios of ultimate ALAE to indemnity. In the most recent pure premium rate filings, this projection was based on the average of the latest three historically developed ratios. In prior pure premium rate filings, other projection methodologies included the latest year ratio and applying a five-year exponential trend to the historical ratios of ultimate ALAE to ultimate indemnity losses. Chart 23 compares policy year ALAE projected using these three methods with the actual ratios to emerge in hindsight.

Chart 23. Paid ALAE to Paid Indemnity Development Projections

Policy Year	Ultimate ALAE as % of On-Level Indemnity	Estimate Based on 3-Year Average ²⁶	3-Year Estimate Pct. Point Error	Estimate Based on Latest Year ²⁷	Latest Year Estimate Pct. Point Error	Trended Estimate ²⁸	Trended Estimate Pct. Point Error
1996	21.4	18.6	-2.8	16.5	-4.9	—	—
1997	24.6	17.5	-7.1	17.9	-6.7	—	—
1998	27.0	18.1	-8.9	20.0	-7.0	17.6	-9.4
1999	30.0	20.2	-9.8	22.8	-7.2	25.6	-4.4
2000	32.7	23.1	-9.6	26.4	-6.3	34.9	+2.2
2001	34.7	25.6	-9.1	27.6	-7.1	37.9	+3.2
2002	38.7	28.8	-9.9	32.3	-6.4	42.8	+4.1
2003	39.3	31.0	-8.3	33.1	-6.2	43.2	+3.9
2004	35.5	33.9	-1.6	36.2	+0.7	44.6	+9.1
2005	35.1	36.8	+1.7	41.1	+6.0	50.8	+15.7

²⁶ Projections were based on averaging the latest three historical ratios of ultimate ALAE to on-level indemnity losses available at the time. For example, the projection for policy year 1996 was based on averaging the policy year 1992 to 1994 ultimate ALAE ratios.

²⁷ Projections were based on the latest available historical ratio of ultimate ALAE to on-level indemnity losses available at the time. For example, the projection for policy year 1996 was based on the 1994 ultimate ALAE ratios.

²⁸ Projections were based on applying an exponential trend to the latest five historical ratios.

As shown in Chart 23, analogous to the paid ALAE development methodology as shown in Chart 22, during the late 1990s and early 2000s when losses were deteriorating rapidly, ALAE did not increase commensurate with indemnity losses. This resulted in the projections based on three-year averages and the latest year of historical accident year ultimate ratios understating ALAE. However, projections of ALAE as a percentage of indemnity losses based on the three-year average or latest year methodology for the two post-reform years were relatively good predictors of actual emergence. By projecting historical growth in the ratio of ultimate ALAE to ultimate loss, the exponential trend projections were better predictors of ALAE ratios in the early part of this decade, but overstated ALAE following the reform period.

VII. Alternatives to Current LAE Projection Methodologies

To improve upon the accuracy of the LAE component reflected in proposed pure premium rates, a number of alternative methodologies for projecting LAE were reviewed. The projection methodologies reviewed for ULAE and ALAE are presented separately below.

A. Alternative ULAE Projection Methodologies

Currently, future ULAE levels are projected based on recent historical calendar year ratios of incurred ULAE to incurred losses. As discussed above, during periods of stable loss and LAE experience, historical calendar year statistics are generally believed to be acceptable proxies for projecting future policy year ULAE emergence. However, during the late 1990s and early 2000s when the volume and development of losses (especially medical) were at unprecedented levels and ULAE amounts did not change commensurately with losses, basing projections on historical ratios of ULAE to loss did not accurately predict future ULAE levels. Several alternative ULAE projection methodologies that attempt to relate ULAE incurred amounts to components other than calendar year losses are presented below.

1. Claim Count by Calendar Year Method

The majority of ULAE cost is associated with the salary cost of claims adjusters. Based on a ULAE projection methodology described in the Casualty Actuarial Society Proceedings,²⁹ an analysis of a methodology which attempts to relate the incurred cost of ULAE to claim processing activities was undertaken. The methodology is predicated on the assumption that ULAE costs are incurred in the establishment of new claims as well as in the “maintenance” of existing open claims. Specifically, it was assumed that in a given year, a new claim incurs twice as much ULAE costs as a “maintenance” claim. In this way, historical calendar year ULAE severities based on these weighted average claim counts can be used as a basis for projecting future ULAE costs.

Exhibit 4.1 shows the derivation of historical calendar year statewide ULAE incurred severities based on these weighted open claim counts. Exhibit 4.2 shows the claim reporting and claim closure patterns that are used to estimate future calendar year count activity by accident year. The projection of future accident year claims is needed to estimate future calendar year counts, and is based on applying annual indemnity claim frequency trends from the WCIRB’s latest indemnity claim frequency forecast³⁰ to the historical claim counts. By assigning twice the weight on newly-opened claims as maintenance claims, a weighted projection of claim counts for each future calendar year is estimated as shown on the lower portion of Exhibit 4.3.

Exhibit 4.4 presents the historical as well as estimated future calendar year weighted claim counts. The ULAE severities in Exhibit 4.4 are also projected to future calendar years based on the California average annual wage level changes published by UCLA Anderson School of Business. Applying the projected ULAE severities to the projected weighted claim counts results in projected calendar year ULAE incurred dollars, which are then converted into a ratio to losses for the projected policy year.³¹

²⁹ Johnson, Wendy A., *Determination of Outstanding Liabilities for Unallocated Loss Adjustment Expenses*, Proceedings of the Casualty Actuarial Society, Volume LXXVI (1988).

³⁰ See Part A, Section B, Appendix C, Exhibit 4, of the WCIRB’s January 1, 2008 pure premium rate filing submitted on September 20, 2007.

³¹ While this method is relatively straightforward in its application based on available data, it does require the use of calendar year data as a proxy for policy year, and assumes the same claim reporting and closure pattern for every accident year (which may not be appropriate—especially in a rapidly changing claims environment).

2. Claim Count by Accident Year Method

This method is very similar to the Claim Count by Calendar Year Method discussed above. In this method, future accident year weighted claim counts (instead of calendar year weighted claim counts) are derived.³²

Exhibit 5.1 presents the weighted claim counts by calendar year for each of the future accident years needed for the policy year projection. Exhibit 5.2 shows the calendar year ULAE per weighted claim for the remaining duration of the future accident years—projected based on annual wage level changes derived from information published by the UCLA Anderson School of Business. Applying these future weighted counts to the future ULAE severity estimated for the remaining duration of the open claims results in projected ULAE incurred dollars for each future accident year. This is then converted into a ratio to losses for the policy year to be projected.

3. Weighted Loss by Calendar Year Method

The claim count methodologies described above implicitly assume that the cost of adjusting a smaller indemnity claim is comparable to that of a larger indemnity claim. To reflect potential ULAE differences based on the size of the claim, an alternative ULAE projection based on a ULAE projection methodology described in Casualty Actuarial Society Forum³³ was developed. This approach varies from the claim count-based methodologies described above in that in lieu of using newly-reported and maintenance claim counts to quantify claims handling activities, it relates ULAE expenditures to the dollars of loss on the claims being adjusted. Specifically, the methodology is predicated on the following assumptions:

- ULAE amounts spent opening claims are proportional to the ultimate cost of claims being reported;
- ULAE amounts spent maintaining claims are proportional to payments made, and
- ULAE amounts spent closing claims are proportional to the ultimate cost of claims being closed.³⁴

Exhibit 6 presents an alternative ULAE projection based on this methodology. (For ease of presentation, all figures in this exhibit are shown as percentages of premiums.) In this method, accident year ultimate losses are used as a proxy for the cost of ULAE in handling claims newly reported in a calendar year. (Calendar year ultimate losses are difficult to obtain; therefore, accident year ultimate losses are used instead, thereby ignoring any calendar year changes to ultimate losses for prior accident years.) Calendar year paid losses are used as a proxy for the cost of ULAE in handling open claims in a calendar year. (No additional cost related to closing an existing claim is used.) Based on actual ULAE data referenced in the actuarial study upon which this methodology was presented, a 60% weight was applied to accident year ultimate losses and a 40% weight was applied to calendar year paid losses.

³² While this method uses future accident years that should be a better predictor of policy year experience than calendar year experience, it requires projections of claim and inflation patterns many years into the future, which can be problematic and subject to significant error.

³³ Conger, Robert F. and Nolibos, Alejandra, *Estimating ULAE Liabilities: Rediscovering and Expanding Kittel's Approach*, Casualty Actuarial Society Forum, Fall 2003.

³⁴ Conger, Robert F. and Nolibos, Alejandra, *Estimating ULAE Liabilities: Rediscovering and Expanding Kittel's Approach*, Casualty Actuarial Society Forum, Fall 2003, page 110.

The resultant weighted losses, referred to as "loss basis", for each historical calendar year are used as the "normalizer" for the corresponding historical incurred ULAE by deriving ratios of calendar year incurred ULAE to its loss basis. Future calendar year ratios of ULAE to loss basis are then projected.

Ultimate losses for future accident years are based on the estimates reflected in the January 1, 2008 pure premium rate filing. Paid losses for future calendar years are derived based on the selected year-end development factors from the July 1, 2007 pure premium rate filing. The loss basis for the future calendar years can then be computed by applying a 60% weight to ultimate losses and a 40% weight to paid losses. Incurred ULAE for a future calendar year is derived by multiplying the corresponding loss basis by the selected ratio of ULAE to loss basis.

In Exhibit 6, ULAE for policy year 2008 is computed based on averaging the projected incurred ULAE for calendar years 2008 and 2009. This ULAE projection is then converted into a percentage of losses.

B. Alternative ALAE Projection Methodologies

Currently, the future ratio of ALAE to loss is projected based on two different accident year development methods: one based purely on paid ALAE, and the other based on the ratio of paid ALAE to paid indemnity. Estimates of ultimate ALAE by accident year using these methodologies have been shown to be relatively accurate. However, the projections of future policy year levels of ALAE based on historically-developed accident year ALAE ratios using these methodologies have, at times, been somewhat divergent and, in hindsight, not consistently accurate. Several alternative ALAE projection methodologies are presented below.

1. Claim Count by Calendar Year Method

Defense attorney costs are commonly believed to be the largest component of ALAE. Like ULAE costs, these costs are incurred on both newly-reported claims as well as on existing open claims. Assuming that a claim incurs the same ALAE expenses in the year it is opened as in every subsequent year through the year it is closed, a modification of the calendar year claim count method for projecting ULAE discussed above can be used to project ALAE costs.

Exhibit 7.1 shows the derivation of historical calendar year ALAE incurred severities based on these weighted open claim counts. The ultimate ALAE shown in Exhibit 7.1 is projected based on the latest historical paid ALAE development factor. Exhibit 7.2 presents a calendar year ALAE projection method analogous to the ULAE claim count-based method previously presented, except that it is based on historical calendar year incurred ALAE normalized to a claim count base that places equal weight on newly-reported claim counts and existing open claim counts. The projection of the weighted number of claims for future calendar years (see lower portion of Exhibit 4.3) is based on current claim reporting and closure patterns. The projection of the calendar year ALAE severity for future years is based on the average annual wage level change from the Professional and Technical component of the Consumer Price Index furnished by Global Insight, Inc. Applying the projected ALAE severities to the projected weighted claim counts results in projected calendar year ALAE incurred dollars, which are then converted into a ratio to losses for the projected policy year.

2. Claim Count by Accident Year Method

ALAE can also be projected based on future accident year incurred ALAE normalized to a claim count base that places equal weight on newly-reported claim counts and existing open claim counts. Exhibit 8.1 presents the weighted claim counts by calendar year for each of the future accident years needed for the future policy year projection. Exhibit 8.2 shows the calendar year ALAE per weighted claim for the remaining duration of the future accident years—projected based on using annual wage level changes derived from the Professional and Technical component of the Consumer Price Index furnished by Global Insight, Inc. Applying these future weighted counts to the future ALAE severity estimated for the remaining duration of the open claims results in projected ALAE incurred dollars for each future accident year. This is then converted into a ratio to losses for the policy year to be projected.

3. Accident Year Frequency-Severity Method

In this method, historical accident year paid ALAE and indemnity claim counts are separately developed to ultimate based on the latest historical development factors. The resultant historical accident year ultimate ALAE severity is derived by dividing the ultimate paid ALAE by the ultimate indemnity claim count.

Exhibit 9 includes an ALAE projection based on separate projections of frequency and ALAE severity. The ultimate ALAE amounts shown in Exhibit 9 are developed based on the latest year ALAE development factors. The ALAE severity for the future policy year is projected based on an exponential trend of the ALAE severities from the historical post-reform years (2003 to 2006). The frequency for the future policy year is estimated using projected frequency trends reflected in the January 1, 2008 pure premium rate filing.³⁵ Ultimate ALAE incurred dollars is then derived and converted into a ratio to loss for the future policy year.

³⁵ See Part A, Section B, Appendix C, Exhibit 4, of the WCIRB's January 1, 2008 pure premium rate filing submitted on September 20, 2007.

VIII. Conclusions and Recommendations

A. Summary of Current LAE Trends

1. Unlike losses, calendar year ALAE and ULAE incurred amounts have not declined subsequent to reform. As a result, both have increased significantly as a percentage of calendar year losses.
2. Given SCIF's unique characteristics, the manner in which SCIF's defense costs are reported, and the rapid shifts in SCIF's market share, recent SCIF LAE experience has differed significantly from the average LAE experience of the private insurers. It is not clear that the circumstances which produced these differences will continue into the future and, as a result, excluding SCIF's historical LAE experience in projecting future overall LAE provisions may be appropriate.
3. Historical changes in calendar year incurred ALAE and ULAE have not been well correlated with changes in calendar year incurred losses.
4. Historical changes in calendar year incurred ALAE have not been well correlated with changes in ultimate indemnity claim counts, while changes in calendar year ULAE have been fairly well correlated.
5. The average statewide ALAE paid per reported indemnity claim has generally been increasing. However, the most recent increases in average ALAE per claim have been driven primarily by SCIF's experience. The average ALAE paid per reported indemnity claim excluding SCIF's experience has declined moderately over the last several years.
6. Statewide ratios of ULAE per claim have increased following the reforms. However, ULAE costs per weighted indemnity claim excluding SCIF's experience, after increasing immediately following the reforms, have recently begun to decline modestly.

B. Impact of Recent Reform Legislation

1. Among the factors related to the recent reforms that would tend to reduce LAE costs are declining claim frequency, the elimination of vocational rehabilitation, and the reduction of Labor Code Section 5814 penalties.
2. The recent reforms have provided insurers with new tools whose application have reduced the cost of losses. However, implementation of these tools has increased the cost of administering and adjusting claims as the reforms have added significant complexities to this process—potentially affecting both ALAE and ULAE costs.
3. Among the reform-related factors that would tend to increase ALAE are increased disputes over medical treatment, disputes related to apportionment, issues related to the January 1, 2005 Permanent Disability Rating Schedule (PDRS), and litigation related to other reform issues.
4. Among the reform-related factors that would tend to increase ULAE are the medical treatment review process, additional complexities related to the indemnity benefit process, and changes in average claim adjuster case loads.
5. Some of the post-reform increases in the cost of LAE per claim are likely associated with resolving transitional reform issues that will not impact the cost of future injuries.

In fact, paid LAE severities (excluding SCIF's experience) on the 2005 and 2006 years are less than those on the initial post-reform peaks in 2003 and 2004.

6. LAE costs per claim could continue to decline in subsequent years as more of the legal challenges to the reform provisions are resolved and the remaining significant uncertainties surrounding the reforms are alleviated. However, it is also possible, depending on how various legal issues are resolved, that LAE costs could increase. LAE costs should continue to be closely monitored.

C. Accuracy of Current LAE Projection Methodologies

1. ULAE projections based on historical calendar year ratios to incurred losses can be appropriate when the experience has been stable and there is no appreciable change expected for the projection year. However, during the recent turbulent periods where there have been dramatic and sudden changes in loss experience, historical calendar year ratios of ULAE to loss were not good predictors of future ULAE ratios.
2. Current ALAE development projections based on either historical ALAE development or historical development in the ratios of paid ALAE to paid indemnity losses have accurately projected ALAE development.
3. Since changes in ALAE levels by year have not correlated well with changes in loss levels by year, projecting future policy year ALAE levels based on historical estimates of the ratios of ultimate accident year ALAE to ultimate losses had mixed results.

D. Potential Alternative LAE Projection Methodologies

1. Inasmuch as the current method did not accurately predict future policy year ratios of ULAE to loss, alternative ULAE projection methodologies that attempt to relate ULAE incurred amounts to components other than calendar year incurred losses should be considered.
2. Alternative ALAE projection methodologies based on the relationship of ALAE amounts to estimated claim counts should be used to augment current ALAE projection methodologies.

IX. Conditions and Limitations

In reviewing the results of this analysis of LAE trends and projection methodologies, the following should be noted:

1. This evaluation is based largely on compilations of individual insurer reports of accident year and calendar year premium, loss and LAE experience. While the individual insurer data submissions are regularly checked for consistency and comparability with other data submitted by the insurer, as well as with data submitted by other insurers, the source information underlying each insurer's data submission is not audited by the WCIRB.
2. In addition to using information collected by the WCIRB, this report relies on analysis and information compiled by other public and private sources of data. While this information was evaluated for reasonableness, the WCIRB did not audit the underlying data provided by other entities.
3. Some of the figures and ratios shown are based on WCIRB actuarial projections of future claim and LAE payments, using information reported by insurers. Although the actuarial methodologies upon which these projections are predicated are comprehensively and regularly tested and the underlying assumptions verified, the actual costs that will ultimately emerge could differ from the amounts projected.
4. The amounts and ratios shown represent statewide totals based on the amounts reported by all insurers writing workers' compensation insurance in California. The results for any individual insurer can differ significantly from the statewide average.
5. The California workers' compensation benefit delivery system is a complex, multi-dimensional system, impacted by many economic, demographic, societal and claims-related factors, including legislative changes. In many cases, it can be very difficult to distinguish the specific effect of various claims phenomena on LAE from other influences.
6. In many instances, insurers that have become insolvent have discontinued reporting credible statistical information to the WCIRB. As a result, the experience summarized in this report may not be fully reflective of the entire market in each of the historical years. Similarly, other significant shifts in the composition in the California marketplace can affect indicated results.

X. Exhibits

Part 4 – Unit Statistical Report Filing Requirements
Section II – Definitions**19. Loss Adjustment Expense(s)**

Loss adjustment expense(s) are comprised of two components, **Allocated Loss Adjustment Expense(s)** and **Unallocated Loss Adjustment Expense(s)**, each of which is defined below:

a. Allocated Loss Adjustment Expense(s)

Allocated loss adjustment expenses shall be comprised of the following costs:

- (1) Fees, salary and overhead (including support staff) of individuals whose primary or predominant job function is to perform representation before the Workers' Compensation Appeals Board or other legal services. This shall include costs incurred by outside or in-house counsel, non-attorney hearing representatives and their related support personnel.

EXCEPTION: Costs associated with occasional or incidental legal work performed by individuals hired primarily or predominantly to perform the function of claim operations shall be considered as Unallocated Loss Adjustment Expenses (see Subrule 19b, below).

- (2) The cost of legal services incurred in pursuing subrogation recoveries.

EXCEPTION: If a subrogation reimbursement is obtained, the reported cost of legal services incurred in pursuing the recovery shall be reduced by the amount reimbursed. If the reimbursement exceeds the cost of such legal services, the excess shall be applied to reduce the reported incurred losses.

- (3) Court, alternate dispute resolution and other specific costs listed below that are not included in the award to or incurred on behalf of the claimant:

(If any costs listed below are included in the award to or incurred on behalf of the claimant, they shall be reported as incurred indemnity.)

- (a) Expert testimony.

EXCEPTION: The cost of all expert testimony related to medical-legal shall be reported as incurred medical.

- (b) Witnesses and summonses.

- (c) Copies of documents such as birth and death certificates.

EXCEPTION: The cost of procuring copies of medical treatment records shall be reported as incurred medical.

- (d) Alternate dispute resolution fees, such as arbitration fees.

- (e) Surveillance, including activity checks, performed by either in-house personnel or outside services.

EXCEPTION: The cost of incidental surveillance or activity checks performed by individuals hired primarily or predominantly to perform the function of claim operations shall be considered as unallocated loss adjustment expenses (see Subrule 19b, below).

- (f) The cost of field investigations related to the compensability of claims, potential fraud or the potential for future subrogation, performed by either dedicated in-house personnel or outside services.

EXCEPTION: The cost of incidental field investigations performed by individuals hired primarily or predominantly to perform the function of claim operations shall be considered as unallocated loss adjustment expenses (see Subrule 19b, below).

Part 4 – Unit Statistical Report Filing Requirements
Section II – Definitions

(g) Court costs, such as appeal bond costs and appeal filing fees.

(h) Interpreter fees.

EXCEPTION: Interpreter fees related to medical-legal or medical treatment shall be reported as incurred medical. Interpreter fees related to vocational rehabilitation or included in the award to, or incurred on behalf of, the claimant, other than those related to medical-legal or medical treatment, shall be reported as incurred indemnity.

b. Unallocated Loss Adjustment Expense(s)

The costs of an insurer, in connection with the handling of claims, which are not defined as allocated loss adjustment expenses, incurred indemnity or incurred medical. These include, but are not limited to:

(1) Fees, salary and overhead (including support staff) of individuals hired primarily or predominantly to perform the function of claim operations. This includes costs incurred by in-house personnel or outside services.

EXCEPTION: Costs related to individuals whose primary or predominant function is to perform legal services or field investigations related to the compensability of claims, potential fraud or the potential for future subrogation shall be considered as allocated loss adjustment expenses (see Subrule 19a, above).

(2) The costs of medical cost containment programs that cannot be allocated to a particular claim. (The costs of medical cost containment programs that can be allocated to a particular claim shall be reported as incurred medical.)

(3) The cost of benefit increases or penalty awards made pursuant to California Labor Code Sections 4650, 5814, 4603.2 and 4622.

**Evaluation of the Use of Latest Year for Projecting Paid ALAE Development Factors
Paid ALAE Development Method**

Paid ALAE Development Factors:

<u>Accident Year</u>	<u>18-30</u>	<u>30-42</u>	<u>42-54</u>	<u>54-66</u>	<u>66-78</u>
1991					1.057
1992				1.091	1.064
1993			1.181	1.111	1.065
1994		1.383	1.187	1.104	1.074
1995	2.133	1.443	1.199	1.115	1.072
1996	2.063	1.380	1.199	1.104	1.065
1997	1.909	1.373	1.169	1.096	1.073
1998	1.950	1.370	1.179	1.108	1.089
1999	2.143	1.410	1.197	1.136	1.102
2000	2.099	1.442	1.226	1.158	1.109
2001	2.179	1.467	1.243	1.143	1.103
2002	2.218	1.449	1.216	1.141	
2003	2.120	1.407	1.218		
2004	1.992	1.419			
2005	2.003				

Projected Paid ALAE Development Factors Based on Selecting Latest Year:

<u>Accident Year</u>	<u>18-30</u>	<u>30-42</u>	<u>42-54</u>	<u>54-66</u>	<u>66-78</u>
1992					1.057
1993				1.091	1.064
1994			1.181	1.111	1.065
1995		1.383	1.187	1.104	1.074
1996	2.133	1.443	1.199	1.115	1.072
1997	2.063	1.380	1.199	1.104	1.065
1998	1.909	1.373	1.169	1.096	1.073
1999	1.950	1.370	1.179	1.108	1.089
2000	2.143	1.410	1.197	1.136	1.102
2001	2.099	1.442	1.226	1.158	1.109
2002	2.179	1.467	1.243	1.143	
2003	2.218	1.449	1.216		
2004	2.120	1.407			
2005	1.992				

Projection Errors:

<u>Accident Year</u>	<u>18-30</u>	<u>30-42</u>	<u>42-54</u>	<u>54-66</u>	<u>66-78</u>
1992					-0.7%
1993				-1.8%	-0.1%
1994			-0.5%	+0.6%	-0.8%
1995		-4.2%	-1.0%	-1.0%	+0.2%
1996	+3.4%	+4.6%	0.0%	+1.0%	+0.7%
1997	+8.1%	+0.5%	+2.6%	+0.7%	-0.7%
1998	-2.1%	+0.2%	-0.8%	-1.1%	-1.5%
1999	-9.0%	-2.8%	-1.5%	-2.5%	-1.2%
2000	+2.1%	-2.2%	-2.4%	-1.9%	-0.6%
2001	-3.7%	-1.7%	-1.4%	+1.3%	+0.5%
2002	-1.8%	+1.2%	+2.2%	+0.2%	
2003	+4.6%	+3.0%	-0.2%		
2004	+6.4%	-0.8%			
2005	-0.5%				
Average	+0.8%	-0.2%	-0.3%	-0.4%	-0.4%
Standard Dev.	+4.9%	+2.5%	+1.5%	+1.3%	+0.7%

**Evaluation of the Use of Latest Year for Projecting Paid ALAE/Paid Indemnity Development Factors
Paid ALAE to Paid Indemnity Development Method**

Paid ALAE to Indemnity Development Factors:

<u>Accident Year</u>	<u>18-30</u>	<u>30-42</u>	<u>42-54</u>	<u>54-66</u>	<u>66-78</u>
1991					1.004
1992				0.998	1.013
1993			0.999	1.022	1.013
1994		0.975	1.019	1.011	1.019
1995	0.965	1.039	1.026	1.021	1.014
1996	0.930	0.979	1.016	1.002	1.008
1997	0.841	0.977	0.997	0.993	1.010
1998	0.856	0.969	0.989	1.005	1.020
1999	0.944	0.981	1.004	1.018	1.031
2000	0.916	0.991	1.011	1.039	1.039
2001	0.937	0.978	1.025	1.038	1.038
2002	0.951	0.984	1.027	1.041	
2003	0.955	1.001	1.037		
2004	1.060	1.053			
2005	1.093				

Projected Paid ALAE to Paid Indemnity Development Factors Based on Selecting Latest Year:

<u>Accident Year</u>	<u>18-30</u>	<u>30-42</u>	<u>42-54</u>	<u>54-66</u>	<u>66-78</u>
1992					1.004
1993				0.998	1.013
1994			0.999	1.022	1.013
1995		0.975	1.019	1.011	1.019
1996	0.965	1.039	1.026	1.021	1.014
1997	0.930	0.979	1.016	1.002	1.008
1998	0.841	0.977	0.997	0.993	1.010
1999	0.856	0.969	0.989	1.005	1.020
2000	0.944	0.981	1.004	1.018	1.031
2001	0.916	0.991	1.011	1.039	1.039
2002	0.937	0.978	1.025	1.038	
2003	0.951	0.984	1.027		
2004	0.955	1.001			
2005	1.060				

Projection Errors:

<u>Accident Year</u>	<u>18-30</u>	<u>30-42</u>	<u>42-54</u>	<u>54-66</u>	<u>66-78</u>
1992					-0.9%
1993				-2.3%	0.0%
1994			-2.0%	+1.1%	-0.6%
1995		-6.2%	-0.7%	-1.0%	+0.5%
1996	+3.8%	+6.1%	+1.0%	+1.9%	+0.6%
1997	+10.6%	+0.2%	+1.9%	+0.9%	-0.2%
1998	-1.8%	+0.8%	+0.8%	-1.2%	-1.0%
1999	-9.3%	-1.2%	-1.5%	-1.3%	-1.1%
2000	+3.1%	-1.0%	-0.7%	-2.0%	-0.8%
2001	-2.2%	+1.3%	-1.4%	+0.1%	+0.1%
2002	-1.5%	-0.6%	-0.2%	-0.3%	
2003	-0.4%	-1.7%	-1.0%		
2004	-9.9%	-4.9%			
2005	-3.0%				
Average	-1.1%	-0.7%	-0.4%	-0.4%	-0.3%
Standard Dev.	+5.7%	+3.2%	+1.2%	+1.3%	+0.6%

Calendar Year ULAE Incurred Per Open Claim

Calendar Year	(a) ULAE Incurred	(b) Number of Open Indemnity Claims at Beginning of the Year	(c) Number of Indemnity Claims Opened During Year	(d) Weighted Number of Open Claims	(e) ULAE Per Open Claim
2000	566,309,754	267,027	161,741	590,509	959
2001	681,413,646	251,668	203,146	657,960	1,036
2002	780,554,042	347,829	226,429	800,687	975
2003	1,159,283,960	386,335	228,160	842,655	1,376
2004	1,141,623,669	453,886	201,395	856,676	1,333
2005	1,130,421,884	471,134	163,287	797,708	1,417
2006	1,137,080,992	443,444	149,265	741,974	1,533

Notes:

- (a) Calendar year ULAE incurred is based on WCIRB expense calls. All figures in each calendar year contain information from the same combination of insurers that submitted both the ULAE and claim count data for that calendar year.
- (b), (c) Based on WCIRB accident year experience calls.
- (d) $(b) + [2.0 \times (c)]$. The assumption is that a claim incurs twice as much ULAE costs in the year it is opened than it does in each subsequent year that it remains open
- (e) $(a)/(d)$

Selected Ultimate Indemnity Claim Reporting and Closure Patterns

As of December 31, 2006

Selected Indemnity Claim Reporting and Closure Patterns - As of 12/31/2006				Cumulative Indemnity Claim Counts					
Year	Percent	Percent	Percent	AY	Year	Reported	Open	Estimated	Annual
	Reported	Closed	Open			@12/31/06	@12/31/06	Ultimate(a)	
				(1)	(2)	(3)	(4)	(5)	(6)
1	83.2%	25.4%	57.8%	1989	18	242,676	1,824	242,725	----
2	94.8%	53.3%	41.5%	1990	17	268,180	2,525	268,260	10.5%
3	97.1%	65.1%	32.0%	1991	16	272,881	3,123	272,990	1.8%
4	98.3%	74.5%	23.8%	1992	15	212,709	2,830	212,815	-22.0%
5	98.9%	81.9%	17.0%	1993	14	169,232	2,800	169,334	-20.4%
6	99.3%	86.5%	12.8%	1994	13	156,620	3,496	156,730	-7.4%
7	99.5%	90.9%	8.6%	1995	12	146,381	4,643	146,498	-6.5%
8	99.7%	93.6%	6.1%	1996	11	143,904	6,231	144,034	-1.7%
9	99.8%	95.1%	4.7%	1997	10	149,394	7,153	149,544	3.8%
10	99.9%	96.2%	3.7%	1998	9	160,571	8,871	160,893	7.6%
11	99.9%	97.0%	2.9%	1999	8	163,136	11,548	163,627	1.7%
12	99.9%	97.7%	2.2%	2000	7	184,721	17,690	185,649	13.5%
13	99.9%	98.4%	1.5%	2001	6	216,648	30,105	218,175	17.5%
14	99.9%	98.9%	1.0%	2002	5	226,152	41,062	228,667	4.8%
15	100.0%	99.2%	0.7%	2003	4	212,306	53,992	215,978	-5.5%
16	100.0%	99.4%	0.6%	2004	3	180,407	62,075	185,795	-14.0%
17	100.0%	99.4%	0.6%	2005	2	152,611	69,855	160,982	-13.4%
18	100.0%	99.4%	0.6%	2006	1	119,609	84,640	143,761	-10.7%
19	100.0%	99.9%	0.1%					<u>Projected(b)</u>	
20	100.0%	100.0%	0.0%	2007				140,023	-2.6%
				2008				135,962	-2.9%
				2009				134,059	-1.4%
				Total		3,378,138	414,463		

Notes:

- (a) Estimated based on number of reported indemnity claims as of December 31, 2006 and selected reporting pattern.
- (b) Estimated based on projected frequency trends of -2.6%, -2.9% and -1.4% for accident years 2007 to 2009. The estimated frequency changes are based on the WCIRB's econometric claim frequency model, which projects changes in claim frequency based on a number of economic, demographic, and claims-related variables—including changes in indemnity benefit levels.

Estimated Number of Weighted Open Claims

Based on Selected Reporting and Closure Patterns - As of December 31, 2006

AY	Estimated Number of Reported Indemnity Claims (a)			Estimated Number of Open Indemnity Claims (b)			Estimated Number of Indemnity Claims Opened During Calendar Year (c)		
	@12/31/07	@12/31/08	@12/31/09	@12/31/07	@12/31/08	@12/31/09	2007	2008	2009
1989	242,700	242,725	242,725	218	0	0	24	24	0
1990	268,207	268,234	268,260	1,556	241	0	27	27	27
1991	272,908	272,936	272,963	1,556	1,583	246	27	27	27
1992	212,730	212,752	212,773	1,192	1,213	1,234	21	21	21
1993	169,249	169,266	169,283	1,270	948	965	17	17	17
1994	156,636	156,651	156,667	1,630	1,175	878	16	16	16
1995	146,396	146,410	146,425	2,241	1,524	1,099	15	15	15
1996	143,918	143,933	143,947	3,198	2,204	1,498	14	14	14
1997	149,409	149,424	149,439	4,352	3,320	2,288	15	15	15
1998	160,732	160,748	160,764	5,953	4,682	3,572	161	16	16
1999	163,300	163,463	163,480	7,690	6,054	4,762	164	164	16
2000	185,092	185,278	185,464	11,325	8,726	6,869	371	186	186
2001	217,084	217,521	217,739	18,763	13,309	10,254	436	436	218
2002	227,067	227,524	227,981	29,269	19,665	13,949	915	457	457
2003	213,602	214,466	214,898	36,716	27,645	18,574	1,296	864	432
2004	182,637	183,751	184,494	44,219	31,585	23,782	2,230	1,115	743
2005	156,314	158,245	159,211	51,514	38,314	27,367	3,703	1,932	966
2006	136,285	139,592	141,317	59,661	46,003	34,215	16,676	3,306	1,725
<u>Projected</u>									
2007	116,499	132,742	135,962	80,933	58,110	44,807	116,499	16,243	3,221
2008		113,121	128,892		78,586	56,424		113,121	15,772
2009			111,537			77,486			111,537
Total	3,520,765	3,658,780	3,794,221	363,257	344,888	330,269	142,627	138,016	135,441
(d) Open Claims at Beginning of the Year:							414,463	363,257	344,888
(e) "Weighted" Open Claims Used in ULAE Projection:							699,716	639,289	615,770
(f) "Weighted" Open Claims Used in ALAE Projection:							557,090	501,273	480,329

Notes:

- (a), (b) Estimated based on projected number of indemnity claims (see Exhibit 4.2) and selected reporting and closure patterns as of December 31, 2006.
- (c) Based on the difference between estimated numbers of reported and open indemnity claims.
- (d) Based on number of indemnity claims still open as of the previous year-end. For example, the number of open indemnity claims at the beginning of calendar year 2007 is the total number of indemnity claims from all accident years that were open as of December 31, 2006 (see column (4) total on Exhibit 4.2).
- (e) The "weighted" number of open claims is the sum of the number of open claims at the beginning of the year and two times the number of claims opened during the year.
- (f) The "weighted" number of open claims is the sum of the number of open claims at the beginning of the year and the number of claims opened during the year.

Projected Ratio of ULAE to Loss for Policy Year 2008
(Based on Estimated ULAE Incurred by Calendar Year)

Calendar Year	(a) Weighted Number of Open Claims	(b) ULAE Per Open Claim	(c) ULAE Incurred (\$000)
2000	590,509	959	566,310
2001	657,960	1,036	681,414
2002	800,687	975	780,554
2003	842,655	1,376	1,159,284
2004	856,676	1,333	1,141,624
2005	797,708	1,417	1,130,422
2006	741,974	1,533	1,137,081
Projected:			
2007	699,716	1,539	1,077,085
2008	639,289	1,578	1,008,571
2009	615,770	1,622	998,668
(d) Projected Policy Year 2008 ULAE (\$000):			1,003,620
(e) Calendar Year 2006 Earned Premium (\$000):			16,703,422
(f) Projected Loss to Pure Premium Ratio for Policy Year 2008:			0.821
(g) Factor to Adjust CY2006 Premium to Policy Year 2008 Level:			0.447
(h) Projected Losses (\$000) for Policy Year 2008: (e) x (f) x (g)			6,129,939
(i) Projected Ratio of ULAE to Losses for Policy Year 2008: (d)/(h)			16.4%

Notes:

- (a) Calendar years 2000 to 2006 are from Exhibit 6.1, and 2007 to 2009 are from Line (e), Exhibit 6.3.
- (b) ULAE per open claim for calendar years 2000 to 2006 are from Column (e), Exhibit 6.1. Calendar years 2007 to 2009 are projected based on applying the California average annual wage level changes of 3.53%, 2.58%, 2.49% and 2.80% for 2006 to 2009, derived from information published by the UCLA Anderson School of Business, to the average of the 2005 and 2006's ULAE per open claim.
- (c) Column (a) x Column (b)
- (d) Average of calendar years 2008 and 2009.
- (e) Based on the reported earned premium from the same group of insurers that reported the number of open indemnity claims for calendar year 2006.
- (f) Based on the projected loss to pure premium ratio from the WCIRB's January 1, 2008 pure premium rate filing as amended on October 19, 2007.
- (g) See Part A, Section B, Appendix A, Exhibit 5.2 of the WCIRB's January 1, 2008 pure premium rate filing.

Projected Ratio of ULAE to Loss for Policy Year 2008
Weighted Number of Open Claims for Accident Years 2007 to 2009

Valuation Date	Estimated Number of Reported Indemnity Claims for Accident Year(a)			Estimated Number of Open Indemnity Claims for Accident Year(b)			Weighted Number of Open Claims for Accident Year(c)		
	2007	2008	2009	2007	2008	2009	2007	2008	2009
@12/31/07	116,499			80,933			232,998		
@12/31/08	132,742	113,121		58,110	78,586		113,419	226,241	
@12/31/09	135,962	128,892	111,537	44,807	56,424	77,486	64,551	110,130	223,074
@12/31/10	137,643	132,019	127,088	33,325	43,508	55,634	48,168	62,679	108,588
@12/31/11	138,483	133,651	130,171	23,804	32,359	42,899	35,006	46,771	61,801
@12/31/12	139,043	134,467	131,780	17,923	23,114	31,906	24,924	33,991	46,116
@12/31/13	139,323	135,011	132,584	12,042	17,403	22,790	18,483	24,201	33,515
@12/31/14	139,603	135,283	133,120	8,541	11,693	17,160	12,602	17,947	23,862
@12/31/15	139,743	135,554	133,389	6,581	8,294	11,529	8,821	12,237	17,696
@12/31/16	139,883	135,690	133,657	5,181	6,390	8,178	6,861	8,566	12,065
@12/31/17	139,897	135,826	133,791	4,075	5,031	6,301	5,209	6,662	8,446
@12/31/18	139,911	135,840	133,925	3,109	3,957	4,960	4,103	5,058	6,569
@12/31/19	139,925	135,854	133,938	2,142	3,018	3,901	3,137	3,984	4,987
@12/31/20	139,939	135,867	133,952	1,456	2,080	2,976	2,170	3,046	3,928
@12/31/21	139,953	135,881	133,965	1,050	1,414	2,051	1,484	2,107	3,003
@12/31/22	139,967	135,894	133,978	784	1,020	1,394	1,078	1,441	2,078
@12/31/23	139,981	135,908	133,992	798	761	1,005	812	1,047	1,421
@12/31/24	139,995	135,922	134,005	812	775	751	826	789	1,032
@12/31/25	140,009	135,935	134,019	126	789	764	840	802	778
@12/31/26	140,023	135,949	134,032	0	122	778	154	816	791
@12/31/27	140,023	135,962	134,045	0	0	121	0	150	804
@12/31/28	140,023	135,962	134,059	0	0	0	0	0	147
@12/31/29	140,023	135,962	134,059	0	0	0	0	0	0
@12/31/30	140,023	135,962	134,059	0	0	0	0	0	0

Notes:

(a), (b) Estimated based on projected number of ultimate indemnity claims for accident years 2007 to 2009 and selected reporting and closure patterns in Exhibit 4.2.

(c) The "weighted" number of open claims is the sum of the number of open claims at the beginning of the year and two times the number of claims opened during the year.

Projected Ratio of ULAE to Loss for Policy Year 2008

(Based on Estimated Ultimate ULAE by Accident Year)

Calendar Year	Weighted Number of Open Claims for Accident Year(a)			ULAE Per Open(b)	Indicated ULAE Incurred for Accident Year (\$000)(c)		
	2007 (1)	2008 (2)	2009 (3)		2007 (5)	2008 (6)	2009 (7)
2007	232,998	0	0	1,539	358,658	0	0
2008	113,419	226,241	0	1,578	178,935	356,929	0
2009	64,551	110,130	223,074	1,622	104,690	178,610	361,786
2010	48,168	62,679	108,588	1,659	79,901	103,971	180,125
2011	35,006	46,771	61,801	1,697	59,391	79,353	104,853
2012	24,924	33,991	46,116	1,735	43,251	58,984	80,026
2013	18,483	24,201	33,515	1,775	32,805	42,954	59,484
2014	12,602	17,947	23,862	1,815	22,877	32,580	43,318
2015	8,821	12,237	17,696	1,857	16,379	22,720	32,856
2016	6,861	8,566	12,065	1,899	13,030	16,267	22,913
2017	5,209	6,662	8,446	1,942	10,117	12,940	16,405
2018	4,103	5,058	6,569	1,987	8,151	10,048	13,050
2019	3,137	3,984	4,987	2,032	6,373	8,095	10,133
2020	2,170	3,046	3,928	2,078	4,511	6,329	8,163
2021	1,484	2,107	3,003	2,126	3,155	4,480	6,383
2022	1,078	1,441	2,078	2,174	2,344	3,133	4,518
2023	812	1,047	1,421	2,224	1,806	2,328	3,160
2024	826	789	1,032	2,274	1,879	1,794	2,348
2025	840	802	778	2,326	1,954	1,866	1,809
2026	154	816	791	2,379	366	1,941	1,882
2027	0	150	804	2,434	0	364	1,957
2028	0	0	147	2,489	0	0	367
2029	0	0	0	2,546	0	0	0

Total Estimated ULAE (\$000) by Accident Year: 950,573 945,685 955,536

(d) Projected Policy Year 2008 ULAE (\$000): 950,611

(e) Calendar Year 2006 Earned Premium (\$000): 16,703,422

(f) Projected Loss to Pure Premium Ratio for Policy Year 2008: 0.821

(g) Factor to Adjust CY2006 Premium to Policy Year 2008 Level: 0.447

(h) Projected Losses (\$000) for Policy Year 2008: (e) x (f) x (g) 6,129,939

(i) Projected ULAE to Losses for Policy Year 2008: (d)/(h) 15.5%

Note:

(a) Based on Exhibit 5.1.

(b) ULAE per open claim for calendar years 2007 to 2029 are projected by applying the California average annual wage level changes of 3.53%, 2.58%, 2.49% for 2006 to 2008 and 2.80% for years 2009 to 2029. The annual wage level change is derived from information published by the UCLA Anderson School of Business.

(c) (a) x (b)

(d) Average of accident years 2008 (Column (6) total) and 2009 (Column (7) total).

(e) Based on the reported earned premium from the same group of insurers that reported the number of open indemnity claims and the incurred ULAE for calendar year 2006.

(f) Based on the projected loss to pure premium ratio from the WCIRB's January 1, 2008 pure premium rate filing as amended on October 19, 2007.

(g) See Part A, Section B, Appendix A, Exhibit 5.2 of the WCIRB's January 1, 2008 pure premium rate filing.

Projected Ratio of ULAE to Loss for Policy Year 2008
Based on Ratio to Weighted Losses¹

Calendar Year	Calendar Year (% to EP)		Accident Year	Loss Basis ²	ULAE Ratio ³
	Incurred	Paid	Ultimate		
	<u>ULAE</u>	<u>Losses</u>	Loss Ratio		
	(a)	(b)	<u>@6/30/07</u>	(d)	(e)
2000	9.1%	74.8%	125.2%	105.0%	0.087
2001	7.7%	59.5%	105.9%	87.3%	0.088
2002	6.2%	54.5%	82.3%	71.2%	0.087
2003	5.9%	43.4%	52.6%	48.9%	0.121
2004	5.2%	37.6%	32.1%	34.3%	0.152
2005	5.7%	36.1%	28.2%	31.4%	0.182
2006	6.8%	40.8%	35.4%	37.6%	0.181
Projected					
2007	6.6% ⁷	37.6% ⁶	35.7% ⁵	36.5%	0.181 ⁴
2008	6.4%	34.0%	35.8%	35.1%	0.181
2009	6.2%	31.6%	35.8%	34.1%	0.181

(f) Projected PY2008 ULAE Incurred to CY2006 Earned Premium Ratio: (Average of calendar years 2008 and 2009 in Column (a))	6.3%
(g) Projected Loss to Pure Premium Ratio for Policy Year 2008 ⁸ :	0.821
(h) Factor to Adjust CY2006 Premium to Policy Year 2008 Level ⁹ :	0.447
(i) Projected Ratio of ULAE to Losses for Policy Year 2008: (f) x (g) x (h)	17.1%

Notes:

¹ Conger, Robert F. and Nolibos, Alejandra, "Estimating ULAE Liabilities: Rediscovering and Expanding Kittel's Approach", Casualty Actuarial Society Forum, Fall 2003.

² Loss basis for a time period is defined as a weighted average of the ultimate cost of claims reported, claims closed and losses paid during that particular time period. The ultimate losses for an accident year is used as a proxy for ultimate cost of claims reported in the calendar year. The assumption is that 60% of ULAE on a claim is incurred at the time the claim is reported, and the remaining 40% of ULAE is spread over the remaining life of the claim. No additional cost related to closing an existing claim is included. Loss basis on this exhibit equals 60% x (c) + 40% x (b).

^{3,4} (e) = (a) / (d). Ratios for calendar years 2007 to 2009 are judgmentally selected.

⁵ Based on the estimated ultimate loss ratios from the WCIRB's January 1, 2008 pure premium rate filing.

⁶ Estimated based on selected age-to-age development factors from the WCIRB's July 1, 2007 pure premium rate filing.

⁷ (d) x (e)

⁸ Based on the projected loss to pure premium ratio from the WCIRB's January 1, 2008 pure premium rate filing as amended on October 19, 2007.

⁹ See Part A, Section B, Appendix A, Exhibit 5.2 of the WCIRB's January 1, 2008 pure premium rate filing.

Calendar Year ALAE Incurred Per Open Claim

Calendar Year	(a) ALAE Incurred	(b) Number of Open Indemnity Claims at Beginning of the Year	(c) Number of Indemnity Claims Opened During Year	(d) Weighted Number of Open Claims	(e) ALAE Per Open Claim
2000	382,282,159	267,027	161,741	428,768	892
2001	462,597,897	251,668	203,146	454,814	1,017
2002	726,862,954	347,829	226,429	574,258	1,266
2003	882,617,835	386,335	228,160	614,495	1,436
2004	1,125,464,160	453,886	201,395	655,281	1,718
2005	985,420,910	471,134	163,287	634,421	1,553
2006	738,059,076	443,444	149,265	592,709	1,245

Notes:

- (a) Calendar year ALAE incurred is based on WCIRB expense calls. All figures in each calendar year contain information from the same combination of insurers that submitted both the ALAE and claim count data for that calendar year.
- (b), (c) Based on WCIRB accident year experience calls.
- (d) (b) + (c). The assumption is that a claim incurs the same ALAE costs in the year it is opened as it does in each subsequent year that it remains open.
- (e) (a)/(d)

Projected Ratio of ALAE to Loss for Policy Year 2008
(Based on Estimated ALAE Incurred by Calendar Year)

Calendar Year	(a) Weighted Number of Open Claims	(b) ALAE Per Open Claim	(c) ALAE Incurred (\$000)
2000	428,768	892	382,282
2001	454,814	1,017	462,598
2002	574,258	1,266	726,863
2003	614,495	1,436	882,618
2004	655,281	1,718	1,125,464
2005	634,421	1,553	985,421
2006	592,709	1,245	738,059
Projected:			
2007	557,090	1,478	823,161
2008	501,273	1,520	762,165
2009	480,329	1,562	750,039
(d) Projected Policy Year 2008 ALAE (\$000):			756,102
(e) Calendar Year 2006 Earned Premium (\$000):			16,703,422
(f) Projected Loss to Pure Premium Ratio for Policy Year 2008:			0.821
(g) Factor to Adjust CY2006 Premium to Policy Year 2008 Level:			0.447
(h) Projected Losses (\$000) for Policy Year 2008: (e) x (f) x (g)			6,129,939
(i) Projected Ratio of ALAE to Losses for Policy Year 2008: (d)/(h)			12.3%

Notes:

- (a) Calendar years 2000 to 2006 are from Exhibit 7.1, and 2007 to 2009 are from Line (f), Exhibit 4.3.
- (b) ALAE per open claim for calendar years 2000 to 2006 are from Exhibit 7.1. Calendar years 2007 to 2009 are projected by applying the average annual wage level change of 3.3%, 3.9%, 2.9% and 2.7% for 2006 to 2009, which are derived from the Professional & Technical component of the Consumer Price index furnished by Global Insight, Inc., to the average of 2005 and 2006's ALAE per open claim.
- (c) Column (a) x Column (b)
- (d) Average of calendar years 2008 and 2009.
- (e) Based on the reported earned premium from the same group of insurers that reported the number of open indemnity claims for calendar year 2006.
- (f) Based on the projected loss to pure premium ratio from the WCIRB's January 1, 2008 pure premium rate filing as amended on October 19, 2007.
- (g) See Section B, Appendix A, Exhibit 5.2 of the WCIRB's January 1, 2008 pure premium rate filing.

Projected Ratio of ALAE to Loss for Policy Year 2008
Weighted Number of Open Claims for Accident Years 2007 to 2009

Valuation Date	Estimated Number of Reported Indemnity Claims for Accident Year(a)			Estimated Number of Open Indemnity Claims for Accident Year(b)			Weighted Number of Open Claims for Accident Year(c)		
	2007	2008	2009	2007	2008	2009	2007	2008	2009
@12/31/07	116,499			80,933			116,499	0	0
@12/31/08	132,742	113,121		58,110	78,586		97,176	113,121	0
@12/31/09	135,962	128,892	111,537	44,807	56,424	77,486	61,330	94,358	111,537
@12/31/10	137,643	132,019	127,088	33,325	43,508	55,634	46,488	59,552	93,037
@12/31/11	138,483	133,651	130,171	23,804	32,359	42,899	34,166	45,140	58,718
@12/31/12	139,043	134,467	131,780	17,923	23,114	31,906	24,364	33,175	44,508
@12/31/13	139,323	135,011	132,584	12,042	17,403	22,790	18,203	23,657	32,710
@12/31/14	139,603	135,283	133,120	8,541	11,693	17,160	12,322	17,675	23,326
@12/31/15	139,743	135,554	133,389	6,581	8,294	11,529	8,681	11,965	17,428
@12/31/16	139,883	135,690	133,657	5,181	6,390	8,178	6,721	8,430	11,797
@12/31/17	139,897	135,826	133,791	4,075	5,031	6,301	5,195	6,526	8,312
@12/31/18	139,911	135,840	133,925	3,109	3,957	4,960	4,089	5,044	6,435
@12/31/19	139,925	135,854	133,938	2,142	3,018	3,901	3,123	3,970	4,974
@12/31/20	139,939	135,867	133,952	1,456	2,080	2,976	2,156	3,032	3,915
@12/31/21	139,953	135,881	133,965	1,050	1,414	2,051	1,470	2,094	2,990
@12/31/22	139,967	135,894	133,978	784	1,020	1,394	1,064	1,428	2,065
@12/31/23	139,981	135,908	133,992	798	761	1,005	798	1,033	1,408
@12/31/24	139,995	135,922	134,005	812	775	751	812	775	1,019
@12/31/25	140,009	135,935	134,019	126	789	764	826	789	764
@12/31/26	140,023	135,949	134,032	0	122	778	140	802	778
@12/31/27	140,023	135,962	134,045	0	0	121	0	136	791
@12/31/28	140,023	135,962	134,059	0	0	0	0	0	134
@12/31/29	140,023	135,962	134,059	0	0	0	0	0	0
@12/31/30	140,023	135,962	134,059	0	0	0	0	0	0

Notes:

(a), (b) Estimated based on projected number of ultimate indemnity claims for accident years 2007 to 2009 and selected reporting and closure patterns in Exhibit 4.2.

(c) The "weighted" number of open claims is the sum of the number of open claims at the beginning of the year and the number of claims opened during the year.

Projected Ratio of ALAE to Loss for Policy Year 2008
(Based on Estimated Ultimate ALAE by Accident Year)

Calendar Year	(a) Weighted Number of Open Claims for Accident Year			(b) ALAE Per Open (4)	(c) Indicated ALAE Incurred for Accident Year (\$000)		
	2007	2008	2009		2007	2008	2009
	(1)	(2)	(3)		(5)	(6)	(7)
2007	116,499	0	0	1,478	172,140	0	0
2008	97,176	113,121	0	1,520	147,752	171,995	0
2009	61,330	94,358	111,537	1,562	95,768	147,341	174,166
2010	46,488	59,552	93,037	1,604	74,551	95,501	149,201
2011	34,166	45,140	58,718	1,647	56,270	74,344	96,707
2012	24,364	33,175	44,508	1,691	41,210	56,113	75,282
2013	18,203	23,657	32,710	1,737	31,621	41,096	56,821
2014	12,322	17,675	23,326	1,784	21,983	31,533	41,614
2015	8,681	11,965	17,428	1,832	15,906	21,921	31,931
2016	6,721	8,430	11,797	1,882	12,647	15,862	22,198
2017	5,195	6,526	8,312	1,932	10,039	12,612	16,062
2018	4,089	5,044	6,435	1,985	8,114	10,011	12,771
2019	3,123	3,970	4,974	2,038	6,364	8,092	10,137
2020	2,156	3,032	3,915	2,093	4,514	6,347	8,194
2021	1,470	2,094	2,990	2,150	3,161	4,501	6,427
2022	1,064	1,428	2,065	2,208	2,349	3,152	4,558
2023	798	1,033	1,408	2,267	1,810	2,343	3,192
2024	812	775	1,019	2,329	1,891	1,805	2,373
2025	826	789	764	2,392	1,976	1,886	1,827
2026	140	802	778	2,456	344	1,970	1,910
2027	0	136	791	2,522	0	343	1,995
2028	0	0	134	2,591	0	0	347
2029	0	0	0	2,660	0	0	0
Total Estimated ALAE (\$000) by Accident Year:					710,409	708,766	717,712
(d) Projected Policy Year 2008 ALAE (\$000):							713,239
(e) Calendar Year 2006 Earned Premium (\$000):							16,703,422
(f) Projected Loss to Pure Premium Ratio for Policy Year 2008:							0.821
(g) Factor to Adjust CY2006 Premium to Policy Year 2008 Level:							0.447
(h) Projected Losses (\$000) for Policy Year 2008: (e) x (f) x (g)							6,129,939
(i) Projected ALAE to Losses for Policy Year 2008: (d)/(h)							11.6%

Note:

- (a) Based on Exhibit 8.1.
- (b) ALAE per open claim for calendar years 2007 to 2029 are projected by applying the average annual wage level changes of 3.3%, 3.9%, 2.9% for 2006 to 2008 and 2.7% for 2009 to 2029, which are derived from the Professional & Technical component of the Consumer Price Index furnished by Global Insight, Inc., to the average of 2005 and 2006's ALAE per open claim.
- (c) (a) x (b)
- (d) Average of accident years 2008 (Column (6) total) and 2009 (Column (7) total).
- (e) Based on the reported earned premium from the same group of insurers that reported the number of open indemnity claims for calendar year 2006.
- (f) Based on the projected loss to pure premium ratio from the WCIRB's January 1, 2008 pure premium rate filing as amended on October 19, 2007.
- (g) See Part A, Section B, Appendix A, Exhibit 5.2 of the WCIRB's January 1, 2008 pure premium rate filing.

Projected Ratio of ALAE to Losses for Policy Year 2008
(Based on Estimated Accident Year Indemnity Claim Frequency and ALAE Severity)

Acc. Year.	Paid ALAE @ 6/30/07 (1)	Cumulative Development Factors (2)	Estimated Ultimate ALAE (3)=(1)x(2)	Number of Indemnity Claim Counts @ 6/30/07 (4)	Cumulative Count Development Factors (5)	Estimated Ultimate Ind. Counts (6)=(4)x(5)	Estimated Ultimated ALAE Per Count (7)=(3)/(6)
1991	433,609,309	1.078	467,430,835	275,078	1.002	275,628	1,696
1992	335,252,971	1.085	363,749,474	214,267	1.002	214,696	1,694
1993	237,289,161	1.092	259,119,764	170,505	1.003	171,017	1,515
1994	219,859,180	1.104	242,724,535	157,851	1.003	158,325	1,533
1995	235,543,733	1.123	264,515,612	147,553	1.004	148,143	1,786
1996	277,707,898	1.144	317,697,835	144,901	1.005	145,626	2,182
1997	350,717,154	1.172	411,040,504	150,805	1.006	151,710	2,709
1998	502,177,854	1.207	606,128,670	162,340	1.008	163,639	3,704
1999	535,598,156	1.254	671,640,088	164,708	1.009	166,190	4,041
2000	664,938,250	1.321	878,383,428	186,680	1.010	188,547	4,659
2001	787,254,039	1.416	1,114,751,719	218,853	1.011	221,260	5,038
2002	785,275,065	1.561	1,225,814,376	228,650	1.014	231,851	5,287
2003	708,466,314	1.781	1,261,778,505	215,792	1.016	219,245	5,755
2004	490,136,400	2.169	1,063,105,852	184,405	1.023	188,646	5,635
2005	294,946,558	3.078	907,845,506	157,152	1.036	162,809	5,576
2006	146,773,871	6.167	905,154,462	137,667	1.079	148,543	6,094

Projected Based on 2-Year Average of 2005 and 2006:

	(c)	(a)	(b)
2007	898,559,046	145,832	6,162
2008	897,803,358	141,603	6,340
1/1/2009	903,451,628	140,608	6,425

(d) Projected ALAE Incurred for Policy Year 2008 (\$000):	903,452
(e) Calendar Year 2006 Earned Premium (\$000):	17,147,784
(f) Projected Loss to Pure Premium Ratio for Policy Year 2008:	0.821
(g) Factor to Adjust CY2006 Premum to Policy Year 2008 Level:	0.447
(h) Projected Losses (\$000) for Policy Year 2008: (e) x (f) x (g)	6,293,014
(i) Projected ALAE to Losses for Policy Year 2008: (d)/(h)	14.4%

Notes:

- (a) Frequency is projected using annual frequency trends of -7.5%, -2.6%, -2.9% and -1.4% for accident years 2006, 2007, 2008 and 2009, respectively. The estimated frequency changes are based on the WCIRB's econometric claim frequency model, which projects changes in claim frequency based on a number of economic, demographic, and claims-related variables—including changes in indemnity benefit levels. These frequency trends were then applied to the ultimate indemnity claim count estimated from averaging 2005 and 2006.
- (b) Severity is projected by applying the average annual wage level change of 3.3%, 3.9%, 2.9% and 2.7% for 2006 to 2009, which are derived from the Professional & Technical component of the Consumer Price Index furnished by Global Insight, Inc., to the ultimate severity estimated from averaging 2005 and 2006.
- (c) (a) x (b)
- (d) 1/1/2009 projection of ultimate ALAE from Column (c).
- (e) Based on the reported earned premium for calendar year 2006 from the same group of insurers that reported the paid ALAE in Column (1) and the number of indemnity claims in Column (4) by accident year as of June 30, 2007.
- (f) Based on the projected loss to pure premium ratio from the WCIRB's January 1, 2008 pure premium rate filing as amended on October 19, 2007.
- (g) See Part A, Section B, Appendix A, Exhibit 5.2 of the WCIRB's January 1, 2008 pure premium rate filing.

WCIRBCalifornia®

525 Market Street, Suite 800
San Francisco, CA 94105-2767

Voice 415.777.0777
Fax 415.778.7007

www.wcirbonline.org
wcirb@wcirbonline.org
wcirb@wcirbonline.org