

DEPARTMENT OF INSURANCE
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ADMINISTRATIVE LAW
BUREAU

BEFORE THE INSURANCE COMMISSIONER
OF THE STATE OF CALIFORNIA

Appeal of GARY E. MILNE,)	
)	
Appellant,)	FILE NO. ALB-WCA-97-11
)	
of Rating Decisions of)	PROPOSED DECISION
STATE COMPENSATION INSURANCE FUND and)	
THE WORKERS' COMPENSATION INSURANCE)	
RATING BUREAU OF CALIFORNIA,)	
)	
Respondents.)	
)	

Administrative Law Judge: Michael D. Jacobs

Counsel:

For appellant Gary E. Milne: Gary E. Milne, Esq.

For respondent State Compensation Insurance Fund: Margorie Rasmussen, Esq.

For respondent Workers' Compensation Insurance Rating Bureau: Brenda Keys, Esq.

SUMMARY

Gary E. Milne, an attorney and insured employer, appeals State Compensation Insurance Fund's (SCIF) rejection of his objection to an increase in premium charges for his 1997 workers' compensation insurance policy. For the reasons detailed below, we affirm SCIF's action.

Uniform Rating System

Workers' compensation insurance rates prior to January, 1, 1995, were determined under a uniform system of classifications and minimum rates approved by the Insurance Commissioner. Under the uniform rating scheme, the Bureau developed minimum adequate rates, rating plans, and risk classifications from information and statistics collected from insurers and presented the rates, plans, and classifications to the Commissioner for approval. (Former Ins. Code, § 11750.1, subd. (b), amended by Stats. 1993, ch. 228, § 3, eff. Jan. 1, 1995; Stats. 1993, ch. 1242, § 9, eff. Jan. 1, 1995.) The approved classifications and rates applied to all admitted insurers (former Ins. Code, § 11732, repealed by Stats. 1993, ch. 228, § 1, eff. Jan. 1, 1995). Insurers were prohibited from using rates that were less than those approved. (Former Ins. Code, § 11736, repealed by Stats. 1993, ch. 228, § 1, eff. Jan. 1, 1995.)

The uniform system was criticized for perpetuating market inefficiency and imposing heavy economic burdens on employer policyholders. (See, e.g., Commissioner's decision in Department of Insurance File No. RH-322 (Ruling 282).) Efforts to improve the rating system culminated in the Legislature's historic deregulation of worker's compensation insurance uniform pricing controls effective on January 1, 1995.

Current Competitive Rating System

Effective January 1, 1995, the Legislature repealed the uniform system and replaced it with a system of "open rating" that allows insurers greater competitive autonomy in setting workers' compensation insurance rates. The change from uniform rating to open rating represents a greater reliance on competitive market mechanisms to promote efficiency, innovation, and economy in the insurance market.

Under the open rating system, the Bureau develops a risk classification system and pure premium rates⁵ for approval by the Commissioner. (Ins. Code, §§ 11734, subd. (b); 11750, subd. (b).) Insurers may choose to adopt the approved classification system and approved pure premium rates or they may develop their own. (Ins. Code, § 11734, subd. (b); tit. 10, Cal. Code Regs., § 2509.32, subd. (I).)

Bureau Vice President Murray's October 8, 1997, letter to Mr. Milne accurately describes the components of pure premium rates and the significance of those rates under open rating.

"[T]he pure premium rates approved by the Commissioner reflect the expected average cost of losses and loss adjustment expenses in a particular year. They do not reflect the cost of commissions, other acquisition expenses, general expenses, taxes,

⁵ Pure premium rate means "[t]hat portion of the rate which represents the loss cost per unit of exposure, including loss adjustment expense." (Ins. Code, § 11730, subd. (f).)

policyholder dividends and profit. Also, these pure premium rates are advisory only. Insurers are not required to utilize these pure premium rates in any way. An insurer may develop its rate for a particular classification of employers by (1) simply applying a loading onto the pure premium rates to reflect expenses and other cost components not contemplated in the pure premium rates, (2) deviating from the pure premium rates to reflect differences in its own book of business from the average represented in pure premium rates and then applying a loading for expenses, or (3) developing their own rates independently from pure premium rates. However, if an insurer establishes a rate for a particular classification, the final price charged depends on those rates, the plan adjustments (schedule rating, premium discounts, etc.) applicable in accordance with the insurer's filed rating plans...."

Since open rating has been in effect, SCIF has based its rating plans on the classification system and pure premium rate for Code 8820 developed by the Bureau and approved by the Commissioner.

We turn next to Mr. Milne's contention that SCIF has unlimited discretion to develop its rating plan for classification 8820.

Current Statutory and Regulatory Rate Controls

Contrary to Mr. Milne's contention, insurers do not have unrestricted discretion to set workers' compensation insurance rate levels under open rating. The open rating system contemplates competitive pricing consistent with the public interest in fair and adequate insurance. Rates that tend to

impair an insurer's solvency or create a monopoly are prohibited (Ins. Code, § 11732). Rates shall not be unfairly discriminatory (Ins. Code, § 11732.5). Rates and classification systems shall not violate laws against invidious and arbitrary discrimination (Ins. Code, § 11735, subd. (d)). The open rating laws did not affect existing statutes that require SCIF to establish fair and adequate rates. (Ins. Code, §§ 11821 and 11822.)

Workers' compensation insurance rates are subject also to the Insurance Commissioner's regulatory supervision and statutory enforcement powers. Insurers must file their rates and rating plans with the Commissioner at least 30 days prior to using the rates (Ins. Code, § 11735, subd. (a)), and upon filing, the rates and all supporting information are open to public inspection (Ins. Code, § 11735, subd. (b)). The rate filing must include an actuary's statement of opinion attesting to the reasonableness of the rates as the insurer's expected loss and expense estimates for the anticipated risks for the period the rates will be used (tit. 10, Cal Code Regs., § 2509.32, subd. (j)). If the Commissioner believes the rates violate any statute the insurer shall be called to a hearing to determine whether the rates should be disapproved (Ins. Code, § 11737, subd. (b)).