



STATE OF ARIZONA
DEPARTMENT OF INSURANCE

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JOHN A. GREENE
Director of Insurance

TO: Insurance Rating Organizations, Insurance Industry Representatives, Insurance Trade Associations, Property & Casualty Insurers, And Other Interested Parties

**FROM: John A. Greene
Director of Insurance**

DATE: June 3, 1998

RE: Administration of Workers' Compensation Laws; Arizona Revised Statutes, Title 20, Chapter 2, Article 4

The Arizona Department of Insurance (the Department) administers the Arizona Revised Statutes, Title 20, Chapter 2, Article 4, which governs workers' compensation (WC) rate filings made by rating organizations.

An insurer may satisfy its obligation to make rate filings by authorizing the Department to accept on the insurer's behalf filings made by the licensed rating organization of which the insurer is a member. A.R.S. §§ 20-357(A), (B). The law requires every insurer that writes WC insurance in Arizona, including the Arizona State Compensation Fund, to be a member of a WC rating organization. The law also restricts each insurer to membership in one WC rating organization at a time. A.R.S. § 20-363(E).

Arizona law does not limit the number of WC rating organizations that may be licensed in this state. Since 1969, only one licensed WC rating organization has operated in Arizona. Consequently, all authorized WC insurers have been, and are at this date, members of that rating organization. That WC rating organization has been, and remains, the repository for all loss and expense data arising out of the transaction of WC insurance in this state. However, in 1997, the Department issued WC rating organization licenses to three other entities. At this time, none of the three entities licensed in 1997 have satisfied all prerequisites to act as a rating organization in this state. However, in anticipation of that eventuality, I must now exercise my authority to designate a Statistical Agent pursuant to A.R.S. § 20-371 to assist in gathering and compiling loss

and expense data used to make WC rates in this state and to make compilations of that data available to licensed WC rating organizations.

The insurance laws plainly contemplate a competitive market for rating organization services. However, multiple operational rating organizations without a designated Statistical Agent will fracture the Arizona loss and expense database, impair the credibility of each portion of that database, and impair the credibility of the resultant rates. The role of a designated Statistical Agent is crucial in a multiple rating organization scenario to maintain the integrity and credibility of the Arizona loss and expense database upon which WC rates in Arizona are based. Further, designating a Statistical Agent resolves the issue under A.R.S. § 20-363(F) as to what degree of combined experience of a rating organization's members is "reasonably adequate for rate-making purposes" because all licensed rating organizations will have access to the combined loss and expense data for the entire state.

The Department, with the assistance of members of the WC insurance industry and the Arizona Industrial Commission, developed a Request for Proposals (RFP) for Statistical Agent services, which will be issued shortly by the State Procurement Office. The recipient of this contract award will be the Department's sole Statistical Agent during the term of its agreement. The Statistical Agent shall develop and administer a statistical plan which meets the specifications of the RFP, and in accordance with which all licensed WC rating organizations shall report the loss and expense statistics of their member insurers to the Statistical Agent. The law and the RFP provide that the Statistical Agent shall give due consideration to the rating systems on file with the Director and to the form of statistical plans used for rating systems in other states in order that the statistical plans may be as uniform as is practicable among the several states. A.R.S. § 20-371. The law and RFP also provide that no insurer shall be required to record or report its loss experience on a classification basis that is inconsistent with the rating system filed for it. The RFP also provides for comprehensive data security procedures to protect the privacy rights of individual insureds, the property rights of individual insurers in underlying data and information concerning their insureds, and the property rights of the Department to the compiled loss and expense data and related work product.

The Statistical Agent and the licensed WC rating organizations will interact as follows:

1. Each licensed Arizona WC rating organization will report the loss and expense statistics of its member insurers to the Statistical Agent in accordance with the statistical plan developed by the Statistical Agent.
2. The Statistical Agent, in conformance with acceptable actuarial and statistical standards, will compile the loss and expense data reported by the rating organizations to **produce one state-wide compilation** that includes the loss and expense experience of every insurer writing WC insurance in Arizona.
3. After compiling the data, the Statistical Agent will provide the compilation to the Department and to every licensed rating organization in Arizona.

4. Each rating organization will thereafter use the compilation as a basis upon which to promulgate its base or starting rates to be used by its respective member insurers to calculate WC premiums for policyholders.

5. The rating organizations will then file the rates they have made with the Department in accordance with A.R.S. § 20-357.

6. The Statistical Agent will also provide rating organizations with experience rating data regarding insureds who move from one WC insurer to another.

The RFP provides that the Statistical Agent shall bid a total annual calendar year fee for all services as the designated Statistical Agent. The fee shall be allocated among all Arizona licensed rating organizations on a pro-rata basis according to net written Arizona premium of the rating organizations' members for the immediate preceding calendar year, subject to a minimum charge to each licensed rating organization in the amount of five per cent of the Statistical Agent's total annual fee. The fee shall be billed and collected quarterly during the calendar year to which it applies, with installments due January 1, April 1, July 1, and October 1 of each year.

The Department contemplates that the contract will take effect on January 1, 1999. After being issued, copies of the RFP may be obtained by faxing requests to the State Procurement Office at (602) 542-5508, referencing RFP No. A8-0106.

Should you have questions about this circular letter, please direct them to Deloris Williamson at (602) 912-8461.