



STATE OF ARIZONA

DEPARTMENT OF INSURANCE

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Circular Letter 1998-9

TO: All Rate Service Organizations, Property & Casualty Insurers, Insurance Trade Associations, And Other Interested Parties

FROM: John A. Greene
Director of Insurance

DATE: August 28, 1998

RE: **Senate Bill 1024; Loss Cost Filings**

Senate Bill 1024, effective August 21, 1998, amended the Arizona Revised Statutes, Title 20, Chapter 2, Article 4.1 (Article 4.1). Article 4.1 applies to the rates of all property and casualty lines of insurance except workers' compensation and related employers' liability, title, and mortgage guaranty.

The purpose of this circular letter is to describe the most significant amendments to Article 4.1. However, this description is not intended to be exhaustive. Enclosed is a copy of the new law, and we strongly encourage those impacted to review the amendments carefully.

The most significant changes made to Article 4.1 are:

1. A rate service organization may file "prospective loss costs" instead of final rates on behalf of its member insurers. A.R.S. § 20-385(A).
2. If a rate service organization files prospective loss costs, each member insurer shall file, on a form approved by the Director, the "loss cost adjustment" and "loss cost modification factors" applicable to the prospective loss costs. A.R.S. § 20-385(A). The form approved by the Director is attached and represents no substantive changes from that which has previously

been used by insurers and rate service organizations to make such filings in Arizona. A.R.S. § 20-385(A).

3. An insurer is not required to file with the Director the insurer's final rate pages that combine the prospective loss costs separately filed by the rate service organization with the loss cost adjustment and the loss cost modification factors filed by the insurer. A.R.S. § 20-385(C) and (D).

A.R.S. § 20-387(B) provides that an insurer may discharge its obligations pursuant to A.R.S. § 20-385 by giving notice to the Director that the insurer uses rates and supplementary rate information prepared by a designated rate service organization. The insurer's rates and supplementary rate information are those filed by the rate service organization, including any amendments to the rate as filed, subject to the modifications filed by the insurer. A.R.S. § 20-385 still requires every authorized insurer and every rate service organization which has been designated by any insurer for the filing of rates pursuant to A.R.S. § 20-387(B) to file with the Director all rates and supplementary rate information and all changes and amendments to those rates within 30 days after the rates become effective.

Therefore, if an insurer's designated rate service organization files prospective loss costs the insurer must initially file its corresponding loss cost adjustment and loss cost modification factors within 30 days after the prospective loss costs become effective. Insurers may request to have their loss cost adjustments remain on file and reference all subsequent rate service organization prospective loss cost filings. Upon receipt of subsequent rate service organization prospective loss costs filings, the insurers' rates shall be a combination of the prospective loss costs and the adjustments contained in the insurers' reference filing on file with the Director and will be effective on the effective date of the prospective loss costs. No further filings need to be made by the insurer if the insurer has requested its loss cost adjustments to remain on file.

Insurers are reminded that notwithstanding these changes final rates are prohibited from being excessive, inadequate or unfairly discriminatory, and insurers are required to adhere to rates based on their current filings. A.R.S. §§ 20-383 and 20-385.

Should you have questions relative to this circular letter, please direct them to Dean Ehler, Supervisor, Property and Casualty Section, Rates and Regulations Division at (602) 912-8461.

Senate Engrossed

State of Arizona
Senate
Forty-third Legislature
Second Regular Session
1998

FILED

Betsey Bayless
Secretary of State

CHAPTER 42

SENATE BILL 1024

AN ACT

AMENDING SECTIONS 20-381, 20-382 AND 20-385, ARIZONA REVISED STATUTES;
RELATING TO OPEN COMPETITION RATES AND RATING ORGANIZATIONS.

1 Be it enacted by the Legislature of the State of Arizona:

2 Section 1. Section 20-381, Arizona Revised Statutes, is amended to
3 read:

4 20-381. Definitions

5 In this article, unless the context otherwise requires:

6 1. "Advisory organization" means any person other than a single
7 insurer who assists insurers or rate service organizations in the making of
8 rates by compiling and furnishing loss or expense statistics or other
9 statistical information and data, or by the submission of recommendations as
10 to rates, forms or supplementary rate information. Advisory organization does
11 not include a joint underwriting association, any actuarial or legal
12 consultant, any employee of an insurer or insurers under common control or
13 management or their employees or manager.

14 2. "LOSS COST ADJUSTMENT" MEANS THAT PORTION OF A RATE FILED BY AN
15 INSURER WITH THE DIRECTOR THAT INCLUDES THE INSURER'S GENERAL EXPENSES, TOTAL
16 PRODUCT EXPENSES, TAXES, LICENSES AND FEE EXPENSES AND UNDERWRITING PROFIT
17 AND CONTINGENCIES. LOSS COST ADJUSTMENT DOES NOT INCLUDE LOSS ADJUSTMENT
18 EXPENSES OR PROSPECTIVE LOSS COSTS.

19 3. "LOSS COST MODIFICATION FACTOR" MEANS THAT RATING FACTOR FILED BY
20 AN INSURER WITH THE DIRECTOR FOR THE PURPOSE OF MODIFYING THE RATE SERVICE
21 ORGANIZATION'S PROSPECTIVE LOSS COST FILING.

22 4. "PROSPECTIVE LOSS COSTS" MEANS THE HISTORICAL AGGREGATE LOSSES AND
23 LOSS ADJUSTMENT EXPENSES FILED BY A RATE SERVICE ORGANIZATION WITH THE

1 DIRECTOR ON WHICH A PORTION OF A RATE IS BASED, ADJUSTED THROUGH ACTUARIAL
2 TRENDING TO A FUTURE POINT IN TIME AND DEVELOPED TO THEIR ULTIMATE VALUES.

3 5. "RATE" MEANS THAT COST OF INSURANCE PER EXPOSURE UNIT WHETHER
4 EXPRESSED AS A SINGLE NUMBER OR AS A PROSPECTIVE LOSS COST WITH AN ADJUSTMENT
5 TO ACCOUNT FOR THE TREATMENT OF EXPENSES, PROFIT AND INDIVIDUAL INSURER
6 VARIATION IN LOSS EXPERIENCE BEFORE ANY APPLICATION OF INDIVIDUAL RISK
7 VARIATIONS BASED ON LOSS OR EXPENSE CONSIDERATIONS. RATE DOES NOT INCLUDE
8 THE MINIMUM PREMIUM.

9 6. "Rate service organization" means any person other than a
10 single insurer who assists insurers by compiling and furnishing loss or
11 expense statistics and recommending, making or filing rates, forms or
12 supplementary rate information. Rate service organization does not include
13 a joint underwriting association, any actuarial or legal consultant, any
14 employee of an insurer or insurers under common control or management, or
15 their employees or manager.

16 7. "Supplementary rate information" means any manual or plan of
17 rates, statistical plan, classification, rating schedule, minimum premium,
18 policy fee, rating rule, rate related underwriting rule and any other
19 information used by an insurer in making rates. SUPPLEMENTARY RATE
20 INFORMATION DOES NOT INCLUDE THE FINAL RATE PAGES THAT COMBINE THE
21 PROSPECTIVE LOSS COSTS WITH THE LOSS COST ADJUSTMENTS.

22 Sec. 2. Section 20-382, Arizona Revised Statutes, is amended to read:
23 20-382. Scope of application

24 A. This article applies to all insurance on risks or on operations in
25 this state, except:

26 1. Reinsurance, other than joint reinsurance to the extent stated in
27 section 20-391.

28 2. Any policy of insurance against loss or damage to or legal
29 liability in connection with property located outside this state, any motor
30 vehicle or aircraft principally garaged and used outside this state or any
31 activity wholly carried on outside this state.

32 3. Insurance of vessels or craft, their cargoes, marine builders'
33 risks, marine protection and indemnity or other risks commonly insured under
34 marine, as distinguished from inland marine, insurance policies.

35 4. Disability or life insurance.

36 5. Annuities.

37 6. Mortgage guaranty insurance.

38 7. Workers' compensation and employers' liability insurance written
39 in connection with workers' compensation.

40 8. Risks subject to section 20-360.

41 9. Title insurance.

42 10. Rates developed by an insurer to be applied individually to the
43 insurance policies of risks, other than medical malpractice risks, for which
44 no rate service organization has published a rate or loss costs in this or

any other state and for which insufficient similar exposure units and loss experience data exist to develop statistically credible rates for the risk and no homogeneous rating class exists in which the risk could reasonably be placed. With respect to each type of risk covered by this subsection, the insurer shall annually certify by January 30 to the director for the preceding ~~twelve month period ending December 31~~ CALENDAR YEAR, on a form acceptable to the director, that the insurer did not have when the risks were written credible experience to establish a rating class for the specific types of risks. The insurer or rate service organization on the insurer's behalf shall file a rate for the specific risks with the director pursuant to section 20-385 when either of the following occurs:

(a) The insurer's written premiums for any specific risk covered by this subsection exceed twenty-five per cent of the insurer's total annual written premium in this state and the insurer has issued contracts for five or more homogeneous risks covered by this subsection in this state in any consecutive three year period, unless an insurer demonstrates to the director that its experience under this subsection does not produce sufficient data to satisfy the requirements of ~~subsection B~~ SUBDIVISION (b) of this ~~section~~ PARAGRAPH.

(b) The number of specific risks covered by this subsection written by the insurer in a specific class meet the standards set forth in the actuarial standard of practice 25 applying to credibility for rate making purposes as adopted by the actuarial standards board as of January 1, 1997.

B. This article does not apply to hospital service or medical service corporations, investment companies, mutual benefit associations or fraternal beneficiary associations.

Sec. 3. Section 20-385, Arizona Revised Statutes, is amended to read:
20-385. Filing of rates

A. Except as to marine, inland marine and transportation risks, which by general custom of the business are not written according to manual rates and rating plans, every authorized insurer and every rate service organization which has been designated by any insurer for the filing of rates pursuant to section 20-387, subsection B shall file with the director all rates and supplementary rate information and all changes and amendments to those rates made by it for use in this state within thirty days after they become effective. IF A RATE SERVICE ORGANIZATION FILES PROSPECTIVE LOSS COSTS ON BEHALF OF ITS MEMBER INSURERS WITH THE DIRECTOR, EACH MEMBER INSURER SHALL FILE, ON A FORM APPROVED BY THE DIRECTOR, THE LOSS COST ADJUSTMENT AND LOSS COST MODIFICATION FACTORS APPLICABLE TO THE PROSPECTIVE LOSS COSTS FILED BY THE RATE SERVICE ORGANIZATION.

B. FOR ANY FILING MADE PURSUANT TO SUBSECTION A OF THIS SECTION, the director may require the filing of supporting data including:

1. The experience and judgment of the filer.

1 2. The experience and judgment of other insurers or rate service
2 organizations.

3 3. The filer's interpretation of any statistical data relied upon.

4 4. A description of the methods used in making the rates.

5 5. A DESCRIPTION OF THE METHODS USED AND STATISTICS RELIED ON BY THE
6 INSURER IN DEVELOPING ITS LOSS COST MODIFICATION FACTOR AND PROVIDING ITS
7 LOSS COST ADJUSTMENT.

8 6. A DESCRIPTION OF THE METHODS USED AND STATISTICS RELIED ON BY THE
9 RATE SERVICE ORGANIZATION IN DEVELOPING ITS PROSPECTIVE LOSS COSTS FILING.

10 C. AN INSURER IS NOT REQUIRED TO FILE WITH THE DIRECTOR THE INSURER'S
11 FINAL RATE PAGES THAT COMBINE THE PROSPECTIVE LOSS COSTS SEPARATELY FILED BY
12 THE RATE SERVICE ORGANIZATION WITH THE LOSS COST MODIFICATION FACTOR FILED
13 BY THE INSURER.

14 D. FOR THE PURPOSES OF THIS SECTION, AN INSURER DOES NOT NEED TO FILE
15 WITH THE DIRECTOR THE INSURER'S FINAL RATE PAGES THAT COMBINE THE PROSPECTIVE
16 LOSS COSTS WITH THE LOSS COST ADJUSTMENTS.

17 E. Upon written consent of the insured, stating the insured's
18 reasons, a rate in excess of that provided by an otherwise applicable filing
19 may be used on a specific risk, if such rate is filed with the director
20 pursuant to subsection A of this section.

21 F. If, after a hearing, the director finds that a particular
22 market is noncompetitive, ~~he~~ THE DIRECTOR shall order that all rates or rate
23 changes and all supplementary rate information in such noncompetitive market
24 be filed with the director at least thirty days before the effective date.
25 The order remains in effect until the director determines that a competitive
26 market has been restored.

APPROVED BY THE GOVERNOR MAY 4, 1998

FILED IN THE OFFICE OF THE SECRETARY OF STATE MAY 4, 1998

Date: _____

**ARIZONA
INSURER RATE FILING
ADOPTION OF RATE SERVICE ORGANIZATION
PROSPECTIVE LOSS COSTS
REFERENCE FILING ADOPTION FORM**

1. INSURER NAME _____

ADDRESS _____

PERSON RESPONSIBLE FOR FILING _____

TITLE _____ TELEPHONE # _____

2. INSURER NAIC # _____

3. LINE OF INSURANCE _____

4. RATE SERVICE ORGANIZATION _____

5. RATE SERVICE ORGANIZATION REFERENCE FILING # _____

6. The insurer named in number 1 above hereby declares that it is a member of the rate service organization, named in number 4, for this line of insurance. The rate service organization has filed prospective loss costs (PLC) on behalf of its member insurers in Arizona with the Director of the Arizona Department of Insurance (ADOI). Therefore, the insurer hereby files, pursuant to A.R.S. § 20-385(A), its lost cost adjustment (LCA) and lost cost modification factors (LCMF) to be used in the development of the loss cost multiplier (LCM) to be applied to the PLCs filed on the insurer's behalf by the rate service organization. The insurer's rates will be the product of the PLC and the LCM(s) as developed from the insurer's LCA and LCMF.

7. PROPOSED RATE LEVEL CHANGE _____ % EFFECTIVE DATE _____

8. PRIOR RATE LEVEL CHANGE _____ % EFFECTIVE DATE _____

9. ATTACH "SUMMARY OF SUPPORTING INFORMATION FORM," FORM 1024B

(Use a separate FORM 1024B for each insurer-selected LCM.)

10. CHECK ONE OF THE FOLLOWING:

Pursuant to A.R.S. § 20-385(A), the insurer hereby files to have its LCA and LCMF and any applicable expense constant apply to future PLC revisions of the rate service organization for this line of insurance if the insurer's LCA and LCMF do not change. (If the LCA and LCMF change, the insurer is required to file the new LCA and LCMF.) The insurer's rates will be the product of the rate service organization's PLC and the insurer's LCM as developed from the insurer's LCA and LCMF. The rates that result from the insurer's LCM and the rate service organization's PLC will apply to policies written on and after the effective date specified by the rate service organization in its filing with the ADOI.

The insurer hereby files to have its LCM as developed from its LCA and LCM apply only to the current rate service organization's filing referenced above in number 5.

Insurer Name: _____
NAIC Number: _____

Date: _____

**INSURER RATE FILING
ADOPTION OF RATE SERVICE ORGANIZATION PROSPECTIVE LOSS COSTS
SUMMARY OF SUPPORTING INFORMATION FORM**

CALCULATION OF COMPANY LOSS COST MULTIPLIER

1. Line, Subline, Coverage, Territory, Class, etc. combination to which this page applies:

2. LOSS COST MODIFICATION FACTOR:

A. The insurer hereby files to adopt the prospective loss costs in the captioned reference filing:
(CHECK ONE)

- Without modification. (factor = 1.000)
- With the modification(s) factor shown below in 2(B). Please describe the nature (e.g., applies only to certain classifications) below and attach supporting data for the modification.
-
-

B. Loss Cost Modification Expressed as a Factor (LCMF): _____ (See examples below)

Example 1: If insurer's loss cost modification is -10%, then the LCMF is .90 (1.000 - .100).

Example 2: If insurer's loss cost modification is +15%, then the LCMF is 1.15 (1.000 + 150).

3. LOSS COST ADJUSTMENT: Development of Expected Loss Ratio. (Attach exhibit detailing insurer expense data and/or other supporting information.)

- A. Total Production Expense
B. General Expense
C. Taxes, Licenses & Fees
D. Underwriting Profit & Contingencies
E. Other (explain)
F. Total

Selected Provisions	% _____
B. General Expense	% _____
C. Taxes, Licenses & Fees	% _____
D. Underwriting Profit & Contingencies	% _____
E. Other (explain)	% _____
F. Total	% _____

4. DEVELOPMENT OF LOSS COST MULTIPLIER:

4A. Expected Loss Ratio: ELR=100% - 3F =

4B. ELR in decimal form =

4C. Company Formula Loss Cost Multiplier: (2B ÷ 4B) =

5. Company Selected Loss Cost Multiplier =

Explain any differences between 4C and 5:

6. Rate level change for the coverages to which this page applies

%
