



## Coverage Insights

### Understanding Your Workers' Compensation Experience Modification Factor

Are you interested in learning about how your workers' compensation insurance premium is calculated? You should be—your experience modification factor, or mod, is an important component used in calculating your workers' compensation premium. Understanding the mod factor calculation and the data utilized provides you with the information necessary to determine how to control your mod to reduce your workers' compensation premium.

#### Who calculates the mod factor?

Most states use the National Council on Compensation Insurance (NCCI) to collect data and calculate the experience modification factor. NCCI is a private corporation funded by member insurance companies. The following states have their own government-run rating bureaus that are separate from the NCCI: California, Delaware, Indiana, Massachusetts, Michigan, Minnesota, New Jersey, New York, North Carolina, Pennsylvania, Texas and Wisconsin.

#### How is a mod calculated?

Calculating the experience modification factor is complex, but the underlying theory and purpose of the formula is straightforward. Your company's actual losses are compared to its expected losses by industry type. The formula incorporates factors that take into account company size, unexpected large losses and the difference between loss frequency and loss severity to achieve a balance between fairness and accountability

#### What is a credit vs. a debit mod?

The mod factor represents either a credit or debit that is applied to your workers' compensation premium. A mod factor greater than 1.0, a debit mod, means that losses are worse than expected and a surcharge will be added to your premium. A mod factor less than 1.0, a credit mod, means the losses are better than expected, resulting in a discounted premium.

#### What is the experience rating period?

The mod is calculated using loss and payroll data for an experience rating period. The experience rating period typically includes data for three policy years, excluding the most recently completed year. For example, for a mod factor calculated on January 1, 2008, data would be used for the January 1, 2004-2005, January 1, 2005-2006 and January 1, 2006-2007 policy periods. The data for the January 1, 2007-2008 would be excluded.

*Time period used in Workers' Compensation Experience Rating*

Experience Rating Period			Data Excluded	Rating Year
1/1/2004	1/1/2005	1/1/2006	1/1/2007	1/1/2008
<ul style="list-style-type: none"> <li>• Claims Costs For Each Policy Period</li> <li>• Payroll data by state and class code</li> </ul>			Mod Calculated	Mod Applied

Three years of data is used to provide a more accurate reflection of the losses, smoothing out the impact of any bad or good year of losses.

The actual loss data is separated into primary and excess pools. Primary losses—the first \$5,000 of every loss—measure frequency. Excess losses—amounts in excess of \$5,000—measure severity. The formula penalizes loss frequency by including all loss amounts in the calculation. The reason for this is that these types of claims can be controlled through proactive loss control programs. Losses in excess of \$5,000 are capped at levels that vary by state. This minimizes the impact of any single large claim. In approved states, medical-only claims figures are reduced by 70 percent.

Expected losses are then calculated by utilizing your payroll data by state and class code, and applying the Expected Loss Ratio (ELR). The ELR is provided by each state rating bureau. These figures are also broken down into expected primary losses and expected excess losses.

#### **How do your losses compare?**

The final mod calculation compares your actual primary and excess loss figures to those expected for a company of the same size and industry type. To understand how workers' compensation losses to your business compare to state industry averages, contact us to review your experience modification worksheet.

#### **How can you control your mod?**

Your mod factor has a direct impact on your workers' compensation premium. The key to controlling your insurance costs is through accident prevention.

- The mod is calculated based on data reported to the rating bureau by past insurers. Incorrect or incomplete data can cause incorrect mod factors. Review the loss and payroll data to make sure the calculation is complete and accurate.
- Losses remain in the experience rating formula for three years. The experience modification factor is influenced more by small, frequent losses than by large, infrequent ones.
- Develop a sound safety program, Return to Work program, and loss prevention procedures to reduce loss frequency.
- An effective self-inspection and accident investigation program are critical to managing claim frequency.
- Implement an active claims management program to manage outstanding reserves and focus on efficiently resolving open claims.
- Report all claims to carrier immediately.
- Take an aggressive approach to providing light duty to all injured employees upon their release from treatment.
- Set safety performance goals for supervisory roles. Success in achieving safety goals should be used as one measure during performance appraisals.
- Train employees in their responsibilities for safety and enforce conformance with these responsibilities.
- Frequently communicate with employees, on a formal and informal basis, regarding the importance of safety.

#### **How can your experience rating save you money?**

Establishing a proactive safety program is an effective way to reduce losses, which impacts your mod and workers' compensation premium. Contact us today at 319-365-8611. We have the loss control experience to help you advance safety and control your workers' compensation premium.

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