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NCCI Split Point

How the 2013 NCCI Primary-Excess Split Point Change Affects Your Construction Company

The National Council on Compensation Insurance (NCCI) recently announced its plan to increase the primary-excess split point over a three-year transition period.

The first stage of the transition will take effect with each state's approved rate and loss cost filing on or after January 1, 2013.

Due to the split mod, a contractor's mods can result in a 1.0 or higher mod. The impact is that a mod over 1.0, many contractors will not be allowed to work on numerous public and private jobs. The questions are what is the split mod and what are the available options to contractors whose mods are now over 1.0?

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Upcoming Changes

The split point will also be indexed for claim inflation in the third and subsequent years of this transition. These changes will directly affect the 34 states of which New Mexico is one, and the District of Columbia currently using the NCCI's rating system, and may cause the independent rating bureaus of Indiana, Massachusetts, Michigan, Minnesota, New York, Texas and Wisconsin to re-evaluate their split points as well. North Carolina, which has an independent rating bureau, will be enacting the changes. The rating methods used by California, Delaware, New Jersey and Pennsylvania differ widely from NCCI's approach, so similar changes in those states may not occur.

Proposed Plan

•**Year 1:** The split point will initially be increased to $10,000 to become effective with each state's approved rate/loss cost filing on or after January 1, 2013

•**Year 2:** A state's next effective year filing will further increase the split point to $13,500

•**Year 3:** A state's third effective filing year will further increase the split point to $15,000 plus two years of inflation adjustment (rounded to the nearest $500)

UNDERSTANDING THE PRIMARY-EXCESS SPLIT

In the experience rating process, each loss is divided into a primary and excess portion. Currently, the first $5,000 of every loss is allocated as a primary loss with everything over and above considered an excess loss. For example, a $3,000 loss has no excess value. On the other hand, a loss of $15,000 would have $5,000 in primary losses, as well as $10,000 in excess losses. Primary losses are used as an indicator of frequency and are counted in full as part of the mod calculation. Conversely, excess losses receive partial weight in the mod calculation. This means that primary losses affect the mod more than excess losses do.

The rationale behind assessing primary and excess loss amounts is that "severity follows frequency," or in other words, an organization that displays a continual pattern of loss has an increased chance of a severe loss in the future. Thus, a contractor with a large number of primary losses will have a higher mod than a contractor with the same amount of losses split between primary and excess.

Reasoning: NCCI has announced a proposal to raise the split point from $5,000 to $15,000 over a three-year period to better correlate with claim inflation, which has almost tripled since the last split point change nearly two decades ago. Because of this, the portion of each claim that flows into the experience rating formula at full value (primary loss amount) is much smaller than 20 years ago giving less weight to each contractor's actual experience. Consequently, the Plan formula has become less responsive and individual risk experience rating modifications have gravitated toward the all-risk average over time.

Three Myths of the Split Point:

Myth #1 - As a result of the change, every experience mod will increase.

Reality: NCCI reports that 18 percent of mods will increase more than 2 points in the first year of the change. The spit point isn't the only thing that will change in the new formula. The D-Ratio, which determines the portion of expected losses for a class code that is expected to be primary loss, will also be increasing. Other rating values may also change, but we don't know about those things yet. This increase in the D-Ratio is going to also have an impact on:

Myth #2 - The split point change is bad for employers.

Reality: Let's be clear, for the 7 percent whose mods are going to increase 11+ points, the change will be a bad thing. However, 46 percent of employers will see a drop of between 2 and 10 points. More importantly, because of the increase in the D-Ratio, the minimum experience mod that each contractor can reach will be dropping. This means that EVERY contractor, no matter what the first year impact of the change is on their mod, will have greater control over the workers' compensation costs than they do now.

For contractors who take action to take advantage of this opportunity, not only is the split point change not a bad thing, it is an incredible positive that will allow them to free up more of the capital that is locked up in their experience mod.

Myth #3 - The split point change is a "shadow rate increase."

Reality: There is a consistent fear that insurance companies are always trying to find creative ways to collect more money without having to do the unpleasant raising of rates. The reality of the split point change is that insurance companies will be in a position to more accurately charge contractors for the actual exposures that they present.

It is important to remember that the mod is a "predictive indicator of future losses." That is, it helps the insurance company determine how much money they should expect to pay for employee injuries for any given contractor during that policy period. The split point change allows insurance companies to have a clearer

How can your experience rating save you money?

Establishing a proactive safety program is an effective way to reduce losses, positively impacting your mod and workers' compensation premium. Contact us today at 575.524.2222 or info@burke-insurance.com. We have the loss control experience to help you promote safety and control your workers' compensation premium.

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