

**APPENDIX TO THE
MASSACHUSETTS ASSIGNED RISK POOL
PLAN OF OPERATION**

**MASSACHUSETTS WORKERS' COMPENSATION
ASSIGNED RISK POOL
PAID LOSS RATIO INCENTIVE PROGRAM**

The following incentive program for servicing carriers in Massachusetts has been developed based on paid loss ratio relativities. For each servicing carrier, paid loss ratio relativities will be calculated by policy year for Massachusetts assigned risks by dividing the servicing carriers' paid loss ratio (to written minus uncollectible premium) by the average paid loss ratio for all servicing carriers in the Massachusetts Pool.

Program Applicability

A servicing carrier with premium less than \$2.5 million in the Massachusetts Pool is not subject to any incentive or disincentive in this Commonwealth. This is meant to reduce the administration cost in dealing with a relatively small servicing carrier.

This program will be effective beginning with policy year 1993. In other words, the first year of paid loss ratios evaluated will be policy year 1993.

Calculation of Incentives and Disincentives

There is an aggregate limit on incentives/disincentives of 9% of premium subject to the program. The formulas for calculating the incentives and disincentives are in Exhibit 1.

Annual Evaluation of Paid Loss Ratios

Each policy year will have five annual evaluations. The first evaluation will be at the completion of the policy year (policy year 1993 at 12/31/94, etc.). The final evaluation for policy year 1993 will be based on experience reported as of 12/31/98.

Incentives/disincentives will be calculated on an annual basis in accordance with the page entitled "Determining the Servicing Carrier Fee." To avoid the back and forth transfer of funds and to consider the fact that more immature data is less reliable, not all of the calculated incentive/disincentive will be dispensed/billed for preliminary adjustments. The portion of the incentive/disincentive dispensed will depend upon the evaluation number. See the chart below as an example for policy year 1993.

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Evaluation Number	Date	Portion of Incentive/Disincentive Dispensed
1	December 31, 1994	20%
2	December 31, 1995	40%
3	December 31, 1996	60%
4	December 31, 1997	80%
5 (Final)	December 31, 1998	100%

Each evaluation for a policy year considers losses paid since the beginning of the policy year. Because of this, the incentive/disincentive calculated on a subsequent evaluation will net out any payments made or received from earlier evaluations.

Experience Used

The experience data referred to is the assigned risk portion of business for servicing carriers. The data used for calculating incentives will be servicing carrier paid losses, written premium, and uncollectible premium as reported quarterly.

Loss ratios will be calculated to written premium minus uncollectible premium. However, to the extent that Massachusetts Pool rules for a given policy year allow appeals, any uncollectible premium which the servicing carrier appeals to obtain servicing carrier allowance and wins, will be included.

Medical Cost Containment Expenses/Allocated Loss Adjustment Expense

To the extent Massachusetts pool rules for a given policy year provide for reimbursements of servicing carriers for medical cost containment, allocated loss adjustment expenses, etc., reimbursed expenses will be added to paid losses to calculate the relativities. Since such expenses should serve to lower losses, the addition of any such reimbursed expenses should not adversely impact a servicing carrier. The average pool paid loss ratios would also be adjusted to include any such reimbursed expenses. The purpose of including reimbursed expenses would be to discourage servicing carriers from requesting reimbursement of costs which are not effective in reducing losses. The statewide average servicing carrier fee will be adjusted to the extent that any reimbursements are made for such expenses. [See items 1 and 2 on the page entitled "Determining the Servicing Carrier Fee."]

Capping of Losses

In order to limit the impact of very large losses, paid losses will be capped at \$250,000 per claim/\$500,000 per occurrence. Losses will be capped at \$100,000 per claim/\$200,000 per occurrence for preliminary adjustments at the first and second evaluations.

For several reasons, the limit on large losses used in the calculation is lower for earlier evaluations of a policy year. Very large losses are not considered in earlier evaluations to avoid discouraging servicing carriers from making lump sum payments. Additionally, a very large paid loss could have a bigger impact on a servicing carrier's paid loss ratio when the policy year is immature.

Since cumulative paid loss amounts are not reported by claim, this would require servicing carriers to report losses which should be capped. The loss cap was selected large enough so that the administrative burden of reporting individual large paid loss amounts is not burdensome.

Carriers

This program will be applied on a group basis. The definition of a group is to be found in the Pool Plan of Operation.

Formula for Calculating Incentives and Disincentives

Definition of Variables

MR	=	Maximum Relativity Factor
mR	=	Minimum Relativity Factor
P	=	Carrier written premium minus uncollected premium
SLR	=	State average paid plus case loss ratio
Carrier Rel	=	Carrier paid loss relativity
	=	Carrier paid loss ratio/ state average paid loss ratio

Disincentive

$$\begin{array}{l} \text{If } MR < \text{Carrier Rel,} \\ \qquad \qquad \qquad = \end{array} \quad P \times SLR \times (\text{Carrier Rel} - MR)$$

Incentive

$$\begin{array}{l} \text{If } mR > \text{Carrier Rel,} \\ \qquad \qquad \qquad = \end{array} \quad P \times SLR \times (mR - \text{Carrier Rel})$$

Note: The maximum Incentive/Disincentive is capped at 9% of premium subject to this program.