BEFORE THE DEPARTMENT OF INSURANCE
STATE OF NEBRASKA

IN THE MATTER OF THE NEBRASKA HOSPITAL-MEDICAL LIABILITY ACT SURCHARGE FOR 2020	)))	SURCHARGE DETERMINATION FOR THE YEAR 2020

The Director of Insurance for the State of Nebraska, as Administrator of the Excess Liability Fund, conducted a public hearing on September 11, 2019, as required by Neb. Rev. Stat. § 44-2830, to consider adjusting the amount of the surcharge for the year 2020. Pursuant to § 44-2830, the Director is to adjust the amount of the surcharge provided for under § 44-2829 on January 1 of each succeeding year to maintain the Excess Liability Fund at a level which is sufficient to pay all anticipated claims for the next year and to maintain an adequate reserve for future claims. On the basis of the public hearing giving due regard to the size of the existing Fund, the number and size of potential claims against the Fund, the number of participating providers, change in the cost of living, and sound actuarial principles, the Director, hereby sets the surcharge for the year 2020, effective January 1, 2020, at fifty percent (50%) for all health care providers.

Dated this 16 day of September, 2019.

Bruce R. Ramge
BRUCE R. RAMGE
Director of Insurance for the State of
Nebraska and Administrator of the
Excess Liability Fund

Nebraska Department of Insurance
Medical-Hospital Excess Liability Fund

2019 Surcharge Rate Hearing – Actuarial Testimony

I am Gordon Hay, Senior Casualty Actuarial Examiner within the Department. I am a Fellow of the Casualty Actuarial Society, Member of the American Academy of Actuaries, and Chartered Property and Casualty Underwriter. I am qualified by education and experience to make and review rates for property/casualty insurance products, including the surcharge rate for the Excess Liability Fund (the Fund).

The surcharge rate is 45% for 2019. I recommend an increase for 2020 to the statutory 50% maximum. My actuarially indicated rate for 2020 is 62.9%, sharply up from last year's 53.2% and the previous year's 52%. Recall that my indicated rate was near 30% for 2015, 2016 and 2017, then 52% for 2018. The 2018 and 2020 increases were due to unexpectedly numerous newly reported claims and/re-evaluations of previously known claims during the fiscal years ending June 2017 and June 2019.

In late 2013, 2014, 2015 and 2016, I found expected annual revenue shortfalls between $0.6 Million and 2.4 Million (combined years ending June 2014-2017 near $6.5 Million) to be acceptable given the Fund's size combined with its potential for capital gains. However, the actual shortfall in the year ending June 2017 was much less sustainable at about $13 Million. Although the 2018 report year looked good at June 2018, subsequent adverse claims experience evaluated at June 2019 produced an additional $12 Million shortfall. Look below for more specifics.

The Fund's Recent Actual Costs exceeded the Fund's Revenue -- Exhibit II, Col. (18):

- Exhibit II shows underwriting costs under the current $500,000 underlying limit per occurrence, with totals for the most recent 4.5 years.
- Column (18) shows recent years' operating ratios. Costs in Col's. (6) and (10), minus investment income in Col. (14), are compared to Fund earned premium, net of ceded reinsurance, in Col. (17).
- Surcharge rates were in the 18% to 22% range during 2013-2016. The 2017 increase to 26% funded reinsurance. Increases to 40% in 2018 and 45% in 2019 followed adverse operating results as recognized in 2017. As of June 2017, the Fund's 4.5-year operating ratio was 184%.
- Despite rate increases that seemed aggressive at the time, as of June 2019, the 4.5-year operating ratio is 200.6%. Escalating costs have simply outpaced our rate increases.

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Indicated Surcharge Rate -- Exhibit II, Col. (16):

- To test the prospective adequacy of the current 45% surcharge rate, I estimated the Fund's expected costs for 2020 as a percent of the underlying primary earned premium. Col. (5) shows underlying primary earned premium, and the indicate surcharge rate for 2020 appears in Col. (16).
- In Column (8) note that the annual rate of change in severity is 5%, versus 6% last year and 5% the previous year.
- After 1/1/2015, the per-occurrence cap increased from $1.75 Million to $2.25 Million, causing an estimated 8.1% increase in the cost of Excess Fund coverage. The new cap applied to occurrences beginning 1/1/2015.
- The reinsurance cost in column (11) funds the Common Loss treaty covering $20 Million excess of a retained $4.5 Million per common loss. A common loss is a catastrophic mass tort with at least two plaintiffs and with costs to the Fund exceeding $4.5 Million. This treaty is renegotiated (and repriced) annually. At January 1, 2019, the $900,000 annual premium was unchanged from 2008.
- Column (16) shows my 2020 rate indication is 62.9% of underlying primary premium. My 2015-2018 indicated rates were respectively 28.8%, 30.0%, 52.0% and 53.2%.
- Please observe within Column (16) that my actuarially adjusted indication for <u>each</u> of the past six report years exceeds the statutory 50% maximum.

Closed Claims and Closed Claim Severity Trend -- Exhibit III:

- The first graph shows that closed claim counts since 2000 would have been more stable if the current underlying $500,000 per occurrence requirement applied from the Fund's inception – especially, almost all the mass tort claims reported in 2002 and closed in 2005 were smaller than the new threshold. At the current $500,000 threshold, we should expect between 10 and 20 Fund cases annually to close with payment.
- The second graph shows average closed-with-payment severities for calendar years 2000-2018. The actual history (simple line) is comparable to values adjusted to reflect the current $500,000 threshold (dashes). My 5.0% annual severity trend selection is an amount that roughly accounts for the "slope" over time in the adjusted averages.
- This 5.0% trend contributes to the indicated surcharge rate – see Exhibit II Col. (8).

The Size of the Existing Fund:

- The Fund's operating reserve has decreased about $27.7 Million since June 2015.
- In some detail, assets at 6/30/2015 were $94.0 Million, estimated liabilities were $20.5 Million and the operating reserve was $73.5 Million. At 6/30/2016, the Fund's assets were $90.4 Million, estimated liabilities were $20.5 Million and the operating reserve was $69.9 Million. At 6/30/2017, assets were $92.3 Million and estimated liabilities were $35.4 Million, so the operating reserve decreased to $56.9 Million. At 6/30/2018, assets were $87.0 Million and estimated liabilities were $28.8 Million, and the $58.2 Million operating reserve increased a bit from 2017. At 6/30/2019, assets are $85.2 Million, estimated liabilities are $39.4 Million and the operating reserve is $45.8 Million.

- Of the $27.7 Million total decrease, fiscal years ending June 2017 and June 2019 respectively contributed $13 Million and $12 Million, and the primary reason in each case was actual claims costs greater than previous forecasts.
- The Fund invests in long-term bonds. Realized and unrealized gains/losses were relatively insignificant prior to 2008, when a $3.0 Million loss was followed by gains totaling $18.4 Million through 2012 -- Exhibit II Column (13). Since then, results have varied. Generally, bonds' market value rose (declined) as interest rates decreased (increased), and 2013-2019 has netted a contribution of $4 Million to the Fund's assets. As always, future interest rates are relevant, but unpredictable.
- 2013-2018 investment income was consistently between $1.5 Million and $1.7 Million, except for $1.25 Million in 2017.
- Given the Fund's current size and the current investment conditions, there is no reason for the Fund to expect investment activity to mitigate inadequate rates.
- To the nearest million, I expect $20 Million of 2020 underlying annual premium, which is similar to 2017-2019 but down from previous years. Contributing factors are a highly competitive (unprofitable) market for primary coverage and continuing consolidation among health care providers.

Number of Participating Providers – Exhibit IV:

- The residual market wrote one provider in YTD 2019, five in 2018, 9 in 2017, 12 in 2016, 16 in 2015, 20 in 2014 and 16 in 2013. Small numbers are evidence of a competitive voluntary market.
- In the past five years, the numbers of providers participating in the Excess Fund has been stable except for a 6% drop in 2016. Despite the 2017, 2018 and 2019 surcharge rate increases to 26%, 40% and 45%, participating provider counts have held close to 4,740.

Summary and Recommendation:

Assuming 2020 underlying earned premium near $20 Million, the Fund's expected costs net of investment income are 62.9% of that, or $12.58 Million. This excludes any provision for risk or profit to the Fund, future interest rate increases, faster decline in primary premium volume if the primary market softens further, or increased pressure on the health care system due to the Affordable Care Act and Medicaid Expansion. The Fund's reinsurance for catastrophic mass torts costs $900,000 in 2019, subject to renegotiation on renewal at January 1, 2020.

At the proposed 50% rate, the Fund's expected $10.0 Million revenue is about 20% less than its expected $12.58 Million net costs. At the 50% maximum rate, I expect 2020 to produce a $2.58 Million operating deficit.

After the $13 Million drawdown in the Fund's operating balance two years ago, we have another $12 Million drawdown. The actuarially indicated rate has exceeded the 50% maximum for three years now. I recommend exploring ways to restore the Fund's financial strength. Meanwhile I recommend increasing the surcharge rate to the 50% maximum.

Exhibit II

Nebraska Department of Insurance
Nebraska Medical-Hospital Liability Act
Historical Costs to the Fund (000's)
With Forecast for 2020 Based on Data as of June 30, 2019

	Excess Fund and Underlying Primary Premium					Fund Costs Net of Investment Income Related to Underlying Primary Earned Premium													Fund Claims Made Net Operating Ratio	
	Direct Written Premium			Direct Earned Premium		Projected Underwriting Cost Ratio							Investment Income Considered							
Report Year	Excess Fund Claims Made Written Premium (1)	Historical Surcharge Factor (2)	Underlying Primary Claims Made Written Premium (3) = (1) / (2)	Earned Premium at Actual Surcharge Rate (4)	Estimated Underlying Primary Earned Premium (5)	Report Year Ultimate Loss and ALAE (Claims Made, Net of Reins) (6)	Ratio to Underlying Direct Earned Premium (7) = (6) / (5)	With 5% Annual Severity Trend, to 2020 (8)	Cost of Increasing Cap from \$1.75M to \$2.25M Effective 1/1/2015 (9) 8.1% from Study as of June 2013	Admin-istrative Expenses (10)	Reins-urance Cost (See Note) (11)	Projected Under-writing Cost Ratio (12) = [(8) + (9) + (10) + (11)] / (5)	Investment Activity Total (12)	Realized & Unrealized Gain/Loss on Long-Term Investments (13)	Investment Income (Minus Investment Expenses) (14) = (12) - (13)	Ratio to Primary Earned Premium (15) = (14) / (5)	Projected Underwriting Cost Ratio Minus Investment Income Ratio (16) = (11) - (15)	Fund's Claims Made Net Earned Premium (17)	Operating Ratio = [Fund Costs minus Investment Income] / [Net Earned Premium] (18) = [(6) + (10) - (14)] / (17)
2002	5,357	35%	15,305	4,214	14,256	13,069	91.7%												
2003	8,867	50%	17,733	6,919	15,442	7,278	47.1%												
2004	9,287	50%	18,575	9,321	17,951	8,002	44.6%												
2005	11,692	50%	23,384	10,679	19,508	12,163	62.3%												
2006	11,326	45%	25,170	11,461	22,784	11,100	48.7%												
2007	10,040	40%	25,101	10,513	23,914	7,276	30.4%	14,062	1,139	352	900	68.8%	2,581	674	1,907	8.0%	60.8%	10,513	54.4%
2008	8,534	35%	24,384	9,446	24,145	3,870	16.0%	7,123	577	289	900	36.8%	(498)	(3,023)	2,525	10.5%	26.4%	9,446	17.3%
2009	8,706	35%	24,874	8,638	23,268	4,574	19.7%	8,018	649	280	900	42.3%	9,682	7,832	1,850	8.0%	34.4%	8,638	34.8%
2010	8,890	35%	25,401	8,783	24,008	5,620	23.4%	9,383	760	302	900	47.3%	8,341	5,754	2,587	10.8%	36.5%	8,783	38.0%
2011	4,961	20%	24,807	6,878	23,854	9,818	41.2%	15,611	1,264	216	900	75.4%	2,868	910	1,959	8.2%	67.2%	6,878	117.4%
2012	4,880	20%	24,402	4,917	22,552	5,613	24.9%	8,499	688	180	900	45.5%	5,961	3,866	2,095	9.3%	36.2%	4,917	75.2%
2013	4,560	18%	25,335	4,627	21,973	6,851	31.2%	9,881	800	258	900	53.9%	7	(1,674)	1,682	7.7%	46.2%	4,627	117.3%
2014	4,340	18%	24,110	4,338	22,340	10,621	47.5%	14,588	1,182	262	900	75.8%	4,032	2,460	1,572	7.0%	68.8%	4,338	214.6%
2015	4,352	20%	21,761	4,408	21,925	9,578	**43.7%**	12,530	609	390	900	65.8%	1,186	(481)	1,668	7.6%	**58.2%**	4,408	**188.3%**
2016	4,738	22%	21,534	4,415	19,740	11,735	**59.4%**	14,619	-	377	900	80.5%	3,742	2,247	1,496	7.6%	**73.0%**	3,721	**285.3%**
2017	5,217	26%	20,064	4,972	19,833	9,083	**45.8%**	10,777	-	428	900	61.0%	1,561	315	1,246	6.3%	**54.8%**	4,092	**202.0%**
2018	7,959	40%	19,899	6,533	18,465	9,550	**51.7%**	10,791	-	391	900	65.4%	814	(772)	1,586	8.6%	**56.8%**	5,333	**156.7%**
2019	3,279	45%	7,287	3,952	9,184	7,324	**79.7%**	7,979	-	173	450	93.7%	2,940	1,869	1,071	11.7%	**82.0%**	3,362	**191.1%**
4.5 Yrs	25,545		90,544	24,280	89,147	47,270	**53.0%**	56,696	609	1,760	4,050	**70.8%**	10,244	3,177	7,067	7.9%	**62.9%**	20,917	**200.6%**

Notes: Earned premium for each half-year reflects 1/4th weight on current, 1/2 weight on previous and 1/4th weight on second previous half-year's written premium.

Column (16): The surcharge rate equals the ratio of Fund revenue to Underlying Primary Premium. Column (16) is the indicated surcharge rate for policies effective in 2019. Assuming anticipated 2019 cost levels and investment activity similar to recent years, the indicated surcharge rate is 53.2%, which (like 52% last year) would exceed the 50% statutory maximum.

Column (18) compares the Fund's historical costs in (6) and (10), minus investment income in (15) to the Fund's net earned premium in (17). The 2015 - 2019 net operating ratio is 200.6%. The main difference between net earned premium in (17) and direct earned premium in (4) is ceded reinsurance, which was new in 2016.

Written Premium is based on coverage effective in the period. Primary carrier written premium is estimated above from Excess Fund written premium and then-current surcharge rates.

In column (8), the trend period is from the year's average earned date (i.e. June 30, except March 31st for YTD 2019), to average earning date for coverage effective in 2020 (i.e. Dec. 31, 2020).

The Fund purchased a Common Loss reinsurance treaty effective May 1, 2016. The treaty provides \$20 Million of limit excess of a \$4.5 Million retention for situations involving multiple plaintiffs whose claims arise from shared underlying circumstances. The annual cost was initially \$800,000, but increased to \$900,000 effective 1/1/2018. The treaty renews again on 1/1/2019, but I have built no change into my 2019 indicated surcharge rate.

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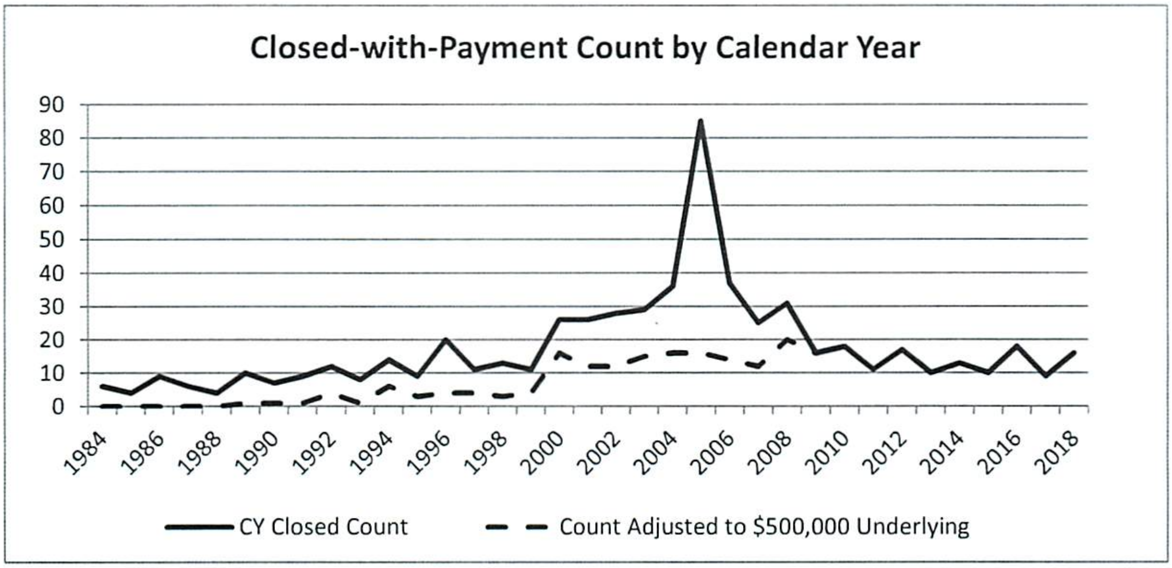
Exhibit III

Nebraska Medical-Hospital Liability Act
Closed Claims and Closed Claim Severity Trend

Claim Counts More Stable After Underlying Coverage Increased to $500K Per Occurrence:



Paid/Closed Claims Severity Trend Is Approximately 3.0 Percent Annually:

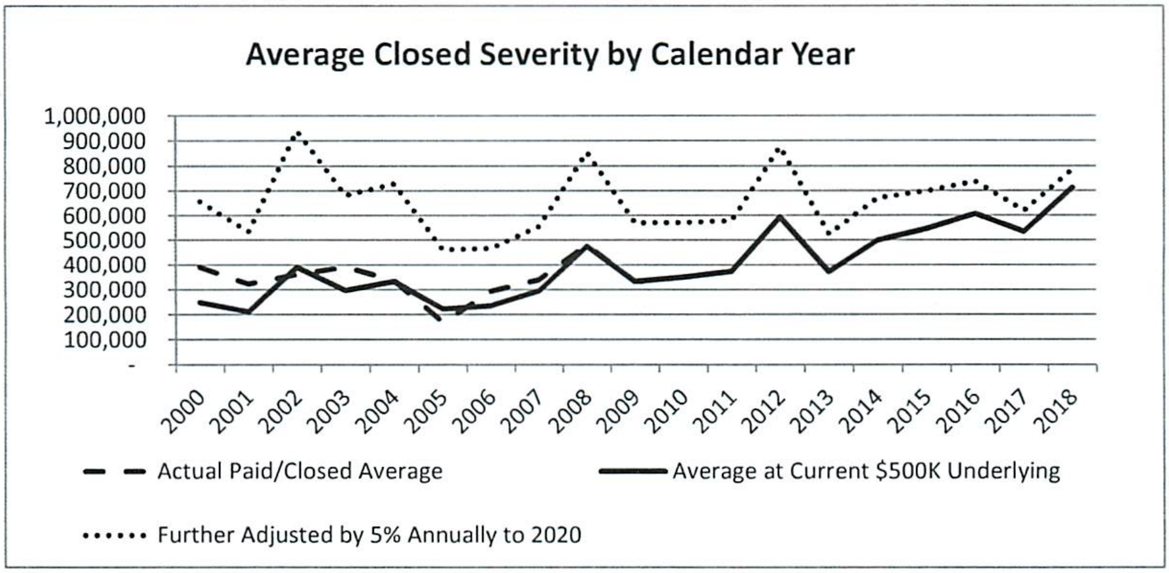


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Exhibit IV

Nebraska Department of Insurance
Nebraska Medical-Hospital Liability Act
History through June 30, 2019
Number of Participating Providers

Cal. Year	CRNA	Osteopath	Hospital	Intern	MD	PC	Total
2015	384	190	171	1	3,846	464	5,059
2016	363	179	144	1	3,593	457	4,737
2017	351	178	142	1	3,602	459	4,733
2018	356	150	145	2	3,639	453	4,745
2019	232	92	64	1	1,732	249	2,370

Excess Fund Written Premium

Cal. Year	CRNA	Osteopath	Hospital	Intern	MD	PC	Total
2015	71,158	105,071	1,199,562	278	2,454,636	253,956	4,084,660
2016	85,588	110,596	1,178,338	351	2,538,923	537,462	4,451,258
2017	101,545	123,385	1,411,842	1,006	2,825,621	489,353	4,952,752
2018	103,092	210,251	2,043,404	2,173	4,251,520	742,113	7,352,552
2019	59,921	99,703	559,441	-	2,208,980	158,200	3,086,534

Average Annual Excess Fund Surcharge

Cal. Year	CRNA	Osteopath	Hospital	Intern	MD	PC	Total
2015	185	553	7,015	278	638	547	807
2016	236	618	8,183	351	707	1,176	940
2017	289	693	9,943	1,006	784	1,066	1,046
2018	290	1,402	14,092	1,087	1,168	1,638	1,550
2019	258	1,084	8,741	-	1,275	635	1,302

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