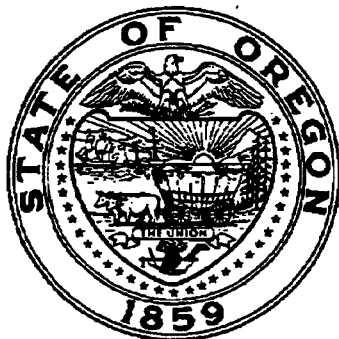




**HB 2033**  
**Report to the Sixty-Ninth**  
**Legislative Assembly**  
**Regarding SAIF**



*Prepared By:*

Department of Consumer  
& Business Services

January, 1997



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**Sixty-Ninth Legislative**  
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**Regarding SAIF**

**Department of Consumer & Business Services**

Director, Kerry Barnett

**January, 1997**

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# HB 2033 SAIF STUDY REPORT

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## A. Introduction

### a. Quotation of HB 2033

For many years--in fact, since shortly after the conversion of the Oregon Workers' Compensation market from a state-run monopoly to a three-way system which allowed private insurers to participate--there has been much public discussion and debate surrounding the role of SAIF Corporation. In the earlier years, issues tended to relate to the continued treatment of SAIF as a state agency, with the use of state-owned equipment (computers, vehicles, real estate, etc.) and favored regulatory treatment.

Through the intervening years, a variety of issues have been addressed through legislative action. Most recently, the Sixty-eighth Oregon Legislative Assembly directed the Department of Consumer and Business Services to conduct a study of the role of SAIF Corporation (SAIF) in the Oregon Workers' Compensation system. The specific instruction which led to the study and development of this report was embodied in HB 2033 and is recited here for reference:

***Section 10.** The Director of the Department of Consumer and Business Services shall conduct a study of the financial and other related regulatory status of the State Accident Insurance Fund Corporation and shall submit a report to the Sixty-ninth Legislative Assembly that describes any advantages or disadvantages of that status in comparison with other workers' compensation insurers.*

### b. General Issues

Perhaps due to the nature of workers' compensation, perhaps due to the nature of SAIF, there has been much discussion and debate concerning the status and operations of SAIF over the years. In preparing this report, we interviewed a variety of participants and stakeholders in Oregon's workers' compensation system. As expected, opinions and perspectives varied widely. Many feel strongly that Oregon's current system is working well and therefore does not need to be "fixed." They see a competitive marketplace, declining premium rates, and reasonable service. Some, however, believe that SAIF's status as a quasi-public entity offers it market advantages that cause short and long-term problems for the marketplace.

In the legislature and elsewhere, a variety of questions and issues have been raised over the years:

- Does SAIF's special status create an "uneven playing field" in the Oregon workers' compensation insurance market?
- Do SAIF's disadvantages stemming from its role as a quasi-public entity prevent it from competing effectively?
- Should Oregon reconsider opening its market to profit-seeking private insurers?
- Are there unreasonable barriers to entry for new carriers interested in participating in Oregon's market?
- Are small businesses treated fairly?

- Should SAIF--and other insurers--be required to offer appointments to transact business to any interested agent?
- In general, is pricing fair in Oregon? Are current rates sustainable?
- Should the state be in the "business" of providing workers' compensation insurance?
- Are injured workers' claims being handled properly? Are carriers' claims denial rates appropriate?
- Should SAIF be required to act as the market of last resort for Oregon employers?

It is important to note that SAIF and the workers' compensation system have both experienced remarkable change over the past ten years. The system has been reformed substantially through legislative action. SAIF itself has new management, a new business plan, and more stable finances. Undoubtedly, many of the issues that have been raised regarding SAIF are grounded in perceptions of SAIF from several years ago. Moreover, some of these issues have been raised by public policy decision-makers, while some other issues have been raised by participants in the Oregon workers' compensation market.

It is not the purpose of this report to set out to "answer" all of the questions that have been raised regarding SAIF. Many--if not all--of these questions involve public policy judgments that are within the province of the legislature. This report does, however, attempt to provide factual background necessary to fully understand SAIF and its role in Oregon's workers' compensation market.

### c. Purpose and Scope of the Report

In order to satisfy HB 2033, a comprehensive review of SAIF and the Oregon workers' compensation marketplace was conducted. In addition to interviews with many participants and interested parties in the workers' compensation system, the study included a review of various state regulatory and taxation issues as they relate to SAIF and private insurance companies, and multi-state comparisons of many elements of the system.

This report, which is the result of that extensive study, begins with an historical look at the three-way system (SAIF, private insurers and self-insurance) and the advent of the assigned risk plan. It then turns to workers' compensation markets in other states and compares Oregon to them with regard to market concentration; pricing, market entry and exit, and the competitive environment are also considered.

Attention is next given to the Department of Consumer and Business Services and its regulatory role relative to the workers' compensation system. In addition, both in terms of the Insurance Code and the Workers' Compensation Law, attention is directed to the differences in treatment of SAIF versus private insurers.

This report includes copies of a Financial Examination, a Market Conduct Examination, and a Secretary of State Audit of SAIF, as of December 31, 1995. It is worth noting that all insurers are subject to the first two types of examination, but SAIF alone is subject to audit by the Secretary of State.



Taxation issues are discussed at some length. Included in this section is an estimate of the effect on SAIF's financial condition and premium rates, if it were subjected to the same tax treatment as private insurers.

Various other issues constitute the balance of the report. Among them are SAIF's role in servicing Non-complying Employer Claims for the state, its role as the sole insurer of the captive state agency accounts, and its relationship to the Oregon Insurance Guaranty Association, a fund which exists to cover the claims of insolvent property and casualty insurers. Consideration is also given to possible regulatory efficiencies that could result from uniform application of the various statutes.

## **B. History of SAIF, the Three-Way System, and Assigned Risk Plan in Oregon**

For its first half century (1914-65), SAIF was the only insurer providing workers compensation coverage in Oregon. It was called the State Industrial Accident Commission (SIAC), and was governed by a commission appointed by the Governor. For the next 15 years (1966-80), it was a state agency (State Compensation Department, SCD and later State Accident Insurance Fund, SAIF) and a state-owned insurer that was initially freed from insurance regulatory oversight to assure it would be competitive to make certain that all employers could insure against compulsory liability and that they could do so at a minimum cost, and to guarantee prompt, fair, and humane adjustment of claims of the injured workmen and their dependents. For the last 16 years (1980-96), it has been a public corporation (State Accident Insurance Fund Corporation) governed by a board of directors that are appointed by the Governor.

Initially SAIF was not subject to insurance regulation. In 1972, SAIF came under the Insurance Code with the focus on ratemaking and trade practices. In the following two decades, a quiltwork of provisions was added without the apparent consideration of ancillary provisions for implementing these additions. A detailed chronology of SAIF's regulatory development follows later in this report.

The basic organization of the Oregon workers' compensation system has evolved over a long period of time. A brief summary of the history of SAIF, the three-way system, and the assigned risk plan is provided below.

February 1913 The Oregon's Workers' Compensation Law was enacted by nearly unanimous vote in both the House and Senate. The Legislature appropriated \$50,000 for the Industrial Accident Fund. The Referendum petition passed by a 2:1 margin in November, 1913.

July 1914 The new State Industrial Accident Commission (SIAC) began operation at this time. Three commissioners were appointed by the Governor.

Between 1914 and 1965, employers participated in the system on a voluntary basis, and SIAC acted as the exclusive workers' compensation insurer.

August 1965 The 1965 laws enacted, authorized Oregon's three-way system. The laws created the State Compensation Department (SCD), a state agency, to which SIAC's insurance functions were transferred. The manager of the SCD was appointed by the Governor. The Workmen Compensation Board was also created and had responsibility for regulating the system and closing claims. Mandatory coverage was required for most workers. Employers had the option of 1) insuring with the SCD; 2) insuring with a private insurer; or 3) qualifying as a self-insured employer. The laws also required the state and political subdivisions to insure with the SCD to ensure the stability of the Industrial Accident Fund.

In addition, the laws provided for activation, upon request by the SCD or private insurers, of an assigned risk plan to ensure that the State Compensation Department had a tool for remaining competitive with private insurers. Neither the State Compensation Department nor the private insurers ever requested activation of this mechanism.

January 1966 At this time the three-way system became effective and the State Compensation Department was operational.

July 1969 The State Compensation Department changed its name to the State Accident Insurance Fund (SAIF). The change was made to avoid public confusion between the insurer role of SAIF and the regulatory role of the Workmens' Compensation Board.

July 1979 The 1979 laws enacted authorized that SAIF no longer provide monopoly coverage of all political subdivisions, however, state government agencies remained a captive account.

October 1979 The 1979 Legislature repealed the insurer's authority to request an assigned risk plan and directed the Insurance Commissioner to promulgate a plan. Temporary rules for governing the plan were adopted in October.

January 1980 The Insurance Commissioner permanently adopted rules for governing the Assigned Risk Plan.

July 1980 SAIF was made an independent public corporation and its name was changed to the State Accident Insurance Fund Corporation. Also, SAIF became governed by a board of directors appointed by the Governor.

### **C. Workers' Compensation Market Models in Other States**

There are essentially three workers' compensation market models prevalent throughout the nation as of 1996. These market models may be described as follows. First, there are state markets that are populated only by private insurers and self-insurers; this market model will be referred to as

the non-state-fund model. Second, some state markets include only monopoly state funds and self-insurers (private insurers are excluded from participation in the market); this market model will be referred to as the monopolistic-state-fund model. Finally, some state workers' compensation markets include private insurers, self-insurers and a competitive state fund; this market model will be referred to as the competitive-state-fund model. Within the competitive-state-fund model, there is a secondary market distinction. For some competitive-state-fund states, the state fund serves as the market of last resort; there is no assigned risk plan within the state. For other competitive-state-fund states, the state includes an assigned risk plan which functions as the market of last resort. Oregon is an example of the latter competitive-state-fund model. Throughout this report these market model distinctions will be considered for various analyses. (In some cases the report makes a distinction between non-state-fund states, state-fund states, and monopolistic state-fund states; the labels are somewhat different, but the aforementioned distinctions are the same.) A brief historic summary of changes in workers' compensation market models for the nation is provided below.

In 1983, Minnesota established the first new workers' compensation state fund in 50 years. Prior to 1983, eighteen states had state funds, six of which were monopolistic funds and twelve of which were competitive state funds. Minnesota brought the total of competitive state funds to thirteen. Following is a list of state funds by type at that time:

Competitive State Fund: Arizona, California, Colorado, Idaho, Maryland, Michigan, Minnesota, Montana, New York, Oklahoma, Oregon, Pennsylvania, and Utah

Monopolistic State Fund: Nevada, North Dakota, Ohio, Washington, West Virginia, and Wyoming

By 1994, significant changes in the number of competitive-state-fund states had occurred. The Michigan State Fund was sold to Blue Cross/Blue Shield of Michigan, and five other states established new state funds. These states are: Louisiana, Rhode Island, New Mexico, Texas, and Maine.

Four other states had authority to create state funds by 1994, but were not operational during calendar year 1994, the last year for which financial information is currently available. However, by 1996, the following states were operational: Kentucky and Missouri. The remaining two states of Hawaii and Tennessee are still not operational.

South Carolina has a state fund that is generally not considered a true state fund because it only insures government entities; hence, the state is considered a non-state-fund market for the purposes of this report.

Generally, jurisdictions that have created state funds over the last several years have done so in response to problems in the voluntary market. Although the problems were not exactly the same in each state, they usually have involved the inability of the voluntary market to provide coverage to significant groups of employers. In Maine, for example, the voluntary market became almost non-existent and over ninety percent of all employers found themselves in the

assigned risk pool. The states of Texas, Rhode Island, Louisiana, and New Mexico had a similar problem, but not to the same degree as Maine. In almost all cases, creation of a state fund was part of a more comprehensive workers' compensation reform package. In most cases, these funds have been established as quasi-public, non-profit corporations. The states of Colorado, Oregon, Arizona and possibly other mature funds have also had their laws changed to acquire the same status within their states.

Overall the recent national market model trend has been toward the introduction of more state funds into the competitive-state-fund states model. Moreover, as of this writing, it appears that Nevada will abandon the monopolistic-state-fund model in favor of the competitive-state-fund model, and there are even discussions taking place in Washington for such a move. Interestingly, at the same time that the identified national trend toward the competitive-state-fund market model is occurring, Michigan has divested itself of its state fund, and there is public discussion about similar divestitures in California and Montana. Only time will tell if this movement is the beginning of a new national trend.

#### **D. Characteristics of Oregon's Workers' Compensation Marketplace**

There are a number of ways to characterize the Oregon workers' compensation marketplace. This section of the report discusses the issues of market concentration, pricing, market entry and exit, and other characteristics of Oregon's competitive environment.

##### a. Market Concentration in Oregon and Comparison With Other States

###### 1. Definition of Market Concentration Measures

There are two generally accepted measures of market concentration computed by economists:

- 1) the market concentration ratio (MCR), which equals the percentage of an industry's sales attributable to a particular number of the largest firms, usually the four and eight largest companies; and,
- 2) the Herfindahl-Hirschman Index (HHI), which equals the sum of the squared market shares for a particular number of the largest companies in an industry, usually the top 25 or 50 firms.

The rationale for the use of each of these measures is discussed in turn, along with a summary of how Oregon compares to other states<sup>1</sup>.

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<sup>1</sup> Much of the following discussion relies on information contained in a draft National Association of Insurance Commissioners (NAIC) Workers' Compensation Task Force draft monograph entitled "Market Conditions in Workers' Compensation, Interim Report," by Robert W. Klein, Eric C. Nordham, and Julienne L. Fritz, dated July 9, 1993. A final report was never issued.

Prior to 1984, public policy in the United States established by the Department of Justice (DOJ) applied the MCR standard that when four or fewer firms accounted for 40 percent (MCR) or more of the sales in a market, an undesirable market structure or excessive concentration existed. Briefly, the argument is that when a small number of firms account for a substantial percentage of the sales, the firms will recognize the interdependence of their actions on the market. This recognition may lead to actions taken by the firms that resemble collusion, irrespective of whether collusion occurs. If so, prices and profits of the firms may reflect monopoly characteristics. In evaluating proposed mergers, the Department of Justice would weigh the resulting MCR within the context of possible increased economies of scale and resulting efficiencies versus the effects of increased market concentration.

Subsequent to 1984, the Justice Department established post-merger guidelines using the Herfindahl-Hirschman Index (HHI). A post-merger market with an HHI exceeding 1,800 is considered highly concentrated; a post-merger market with an HHI between 1,000 and 1,800 is regarded as moderately concentrated. Either of these standards might motivate the DOJ to intervene in the proposed merger.

The rationale for using the HHI as a measure of market concentration is essentially the same as the rationale for the MCR, except that the HHI weights each firm's market share, and if one or more firms have relatively high market shares, this is of even greater concern than the share of the largest four firms (the MCR measure). The HHI provides an indication about inequality as well as degree of concentration.

## 2. Oregon's Market Concentration Measures and a Comparison With Other States

A summary of numerous workers' compensation market characteristics by state for 1991 through 1994 is provided in Table D.a.2-1. In 1991, the countrywide workers' compensation insurance four-firm MCR amounted to 22.6 percent. When the market is viewed on a state-by-state basis, in 1991 the state average four-firm MCR, excluding monopolistic state-fund states, was 45.3 percent. The state average excluding both monopolistic and competitive state-fund states was 40.4 percent. There was substantial variation in 1992 statewide MCR's, which ranged from a low of 25 percent in the state of Indiana, to a high of 94 percent in the state of Maine; Oregon's four-firm MCR was 71 percent. In 1994, Oregon's four-firm MCR was 74 percent, as compared to a national low of 23 percent of the market held by the top four firms in Indiana, and a national high MCR of 92 percent in Rhode Island. The state average MCR, excluding monopoly states, was 47 percent.

Eighty insurer groups and/or individual insurers participated in the Oregon market in 1992; ranking Oregon thirty-sixth highest of all states in the number of participating insurers. Eighty-two insurers operated in Oregon in 1994, making Oregon the state with the thirty-fourth highest count of insurers. In both 1992 and 1994, the national average was 95 insurers. The number of participating insurers in 1992 ranged from a low of 40 insurers in Maine to a high of 129 in Indiana. In 1994, the number of participating insurers ranged from 44 insurers, again in Maine, to 129 in Illinois.

On a countrywide basis in 1991, the HHI amounted to 285, well below the Justice Department threshold. Correspondingly, the 1991 state average HHI, including the effect of competitive state funds, was 1,031, and 693 when all state funds were excluded. In 1992, there was substantial variation in statewide HHI's including competitive state-fund states, ranging from a low of 309.9 for Indiana to a high of 4,821.5 for the state of Montana. The state average HHI, including both state-fund and non-state-fund states, for 1992 amounted to 1,097, while by 1994 the state average HHI had climbed to 1,326, a moderately concentrated level. In 1994 the range of HHI's ran from 286 in Indiana to 7,031 in Rhode Island.

Oregon's HHI amounted to 2,203.2 or 201 percent of the 1992 state average of 1,097, and increased to 2,450 or 185 percent of the 1994 state average of 1,326, both of which excluded monopolistic state funds (see Appendix Table D.a.2-1). Notice that generally the HHI values for those states with mature, competitive state funds exceed 2,000. For most of these states, the state fund has a market share equal to or greater than 40 percent, and is either a servicing carrier or functions as the market of last resort. However, two states, Rhode Island and Maine, are recent entrants to the competitive-state-fund market model.

In summary, Oregon's measures of market concentration are higher than the national averages. By both measures of market concentration, the market concentration ratio and Herfindahl-Hirschman Index, Oregon's workers' compensation market is considered highly concentrated. However, this fact should not be too surprising given that Oregon has a mature state fund. Specialists in workers' compensation markets assert that an HHI less than 2,000 should not be a great concern when evaluating individual state market concentrations because barriers to entry and exit are not regarded as severe. Note that when determining the competitiveness of a state's market structure, more than an HHI must be evaluated<sup>2</sup>. When evaluating proposed mergers, the Justice Department also investigates other factors in determining the desirability of the merger. Among other things, the Department considers barriers to industry entry and exit, and achievable economies of scale and the resulting economic efficiencies that inure to markets.

Economists recognize that the established critical values of both the MCR and HHI measures rest on neither underlying economic theory nor experiential assessments. Some economists maintain that whatever the measure of high market concentration, high concentration leads to some characteristics of monopoly markets. Other economists argue that increased market concentration results from aggressive competition, and that the innumerable business decisions which must be made simply make the opportunity for tacit collusion not feasible. Nevertheless, economists generally agree that at some point a single firm may grow so large as to control an excessive market share and either enjoy monopoly profits and/or become less than optimally efficient to comport with public policy.

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<sup>2</sup> Klein, Nordham and Fritz, pg. 19

### 3. Trends in the Distribution of Premium Volume and Number of Participants

From 1966 until 1978, SAIF wrote over 50 percent of the workers' compensation business in Oregon, including self-insured employers. Until 1982, SAIF had more earned premiums annually than all private insurers combined. Since 1983, SAIF's share of the market has fluctuated between 28 percent and 42 percent; private insurers' market share has been between 41 percent and 57 percent and self-insureds' between 12 percent and 18 percent (see chart D.a.3-1 and Table D.a.3-2). In 1995, including the servicing carrier portion of the assigned risk plan premium and estimated self-insurer premium, SAIF had a 33.2 percent market share, private insurers had 50.2 percent, and self-insured employers had 16.6 percent. SAIF's share of the 1994 market was 37.1 percent. The 1995 decline was the first time since 1990 that SAIF failed to gain at least 2 full percentage points of market share. In 1995, private carriers gained market share for the first time since 1990. In 1995, SAIF Corporation recorded \$244.5 million in premiums earned, private insurers had \$370.2 million, and self-insured employers had estimated premiums of \$122.6 million.

Although 375 private insurers were authorized by the insurance commissioner to write workers' compensation insurance in Oregon in 1995, only 193 had positive premiums. One firm, Liberty Northwest, accounted for 39 percent of the private insurers' premiums. The Liberty Mutual Companies together accounted for \$155 million in premiums, or 42 percent of the Oregon private-insurer total. Only four private insurers had more than \$10 million in premiums earned in 1995 (see attached Table D.a.3-3, Summary of Oregon Workers' Compensation Insurance Business By Type of Insurer, 1995).

In 1980, the commissioner adopted rules to establish the state's Assigned Risk Plan. The Plan makes workers' compensation insurance available to employers who are unable to obtain coverage in the voluntary market. The Plan is managed by the National Council on Compensation Insurance (NCCI). In Oregon, currently four insurance companies--SAIF, Employers Insurance of Wausau, A Mutual Company, Hartford Underwriters Insurance Company, and Liberty Northwest Insurance Corporation--act as service providers for the Assigned Risk Plan (ARP) under the provisions of the new servicing carrier bidding process.

Until 1985, very little business was written through the Assigned Risk Plan. From 1985 until 1989, premiums in the ARP grew from \$7.4 million to \$28.8 million. SAIF's 1990 Corporate Plan, implemented in late 1989, included a decision to eliminate coverage for about 10,000 small employers, and many of these employers entered the ARP in 1990. (By January 1, 1990, SAIF canceled or nonrenewed several thousand accounts -- fewer than half the total expected number -- and then reconsidered its decision before any subsequent quarterly renewal dates.) ARP premiums rose to an all-time high of \$71.9 million in 1990. The following year, the AOI Compwise program was created by Associated Oregon Industries and SAIF to provide coverage for employers with annual premiums between \$500 and \$2,500. This program, which groups small businesses together and provides risk management services, played a role in the 1991 drop in ARP risks. In addition, an NCCI Take-Out Credit Program was adopted on May 1, 1990, which rewards insurers for removing employers from the ARP. By 1993, the ARP premiums had dropped to \$48.6 million, but rose 9.2 percent in 1994 to \$53.1 million. The average

premium per risk fell for the third year in a row, to \$2,978 in 1994 for 17,821 policyholders. (See the attached Table D.a.3-4 for a summary of ARP operational characteristics.)

b. Pricing Characteristics

1. Oregon's Premium Rate Ranking

In 1986, Oregon ranked sixth highest in the nation in average workers' compensation premium rates, and had one of the nation's highest occupational injury and illness claims frequencies. At the same time, medical and permanent disability costs for injured workers in Oregon were among the highest in the nation, while benefits were among the lowest.

During the 1987 legislative session, major reform legislation, HB 2900, was enacted to reverse what seemed to be an ineffective workers' compensation system. Three years later, Oregon's premium rate ranking had improved a little to eighth position, but left much room for improvement. Workers' compensation costs were still considered an urgent problem and many small employer policies were being canceled. These conditions provided the impetus for further reform efforts by passage of SB 1197 and SB 1198 during a special session of the Oregon Legislature in May, 1990. Several refinements to the reforms were enacted during the 1991 legislative session, and additional major legislation was enacted in 1995. In addition, throughout this time period the Department of Consumer and Business Services implemented some administrative innovations, not explicitly provided for by legislation, that seem to have positively influenced the workers' compensation system. Moreover, insurers including SAIF responded effectively to both the legislative reforms and administrative innovations. All of these factors have contributed substantially to changes in Oregon's premium rates.

Oregon employs a "file-and-use" competitive rate-making system designed to increase price competition. Pure premium rates are filed by NCCI and are subject to the approval of the Insurance Commissioner. These pure premium rates cover only benefit costs and are based on claims from injuries in the current period. Insurers then apply an expense loading factor to cover administrative costs and profit margin. When comparing Oregon to other states, the calculated index rate represents as closely as possible the full cost to employers buying workers' compensation insurance in each state. Oregon's rate includes pure premium and an additional 24.1 percent which is the 1995 premium weighted average expense load factor used by the top 30 private insurers and SAIF.

Workers' compensation pure premium rates have decreased by over 37 percent from 1991 to 1996 (see chart D.b.1-1). Oregon was the only state in the nation with double-digit rate decreases for three consecutive years (1991-1993). In 1994 Oregon's rates declined 4.3 percent, 1995's rates dropped another 3.2 percent, 1996's rates fell 1.8 percent, and rates will drop another 10.5 percent for rates effective in 1997. Over the course of 1994, 14 states, including Oregon, filed rate reductions, four of those were in the double digits. In 1995, 27 states, including Oregon, had rate reductions, 11 of those were in double digits with the largest being a 20 percent decline in the state of Montana. In the first quarter of 1996, rate reductions became effective in



17 states, including Oregon. Seven states had double digit reductions; the largest was 24 percent in Minnesota.

Based on 1992 premium rates, Oregon's average workers' compensation premium rate ranked twenty-second highest in the nation; a significant improvement from sixth highest in 1986. By 1994 Oregon had dropped to 32nd highest, while preliminary 1996 estimates show Oregon dropping to 34th highest in the nation (See Table D.a.2-1-5). Preliminary premium rate indices range from a low of \$1.64 per \$100 of payroll in Indiana to \$6.08 in Kentucky. Oregon's index is \$3.13, down from \$3.70 in the 1994 study. Six jurisdictions have premium rates above \$5.00 per \$100 payroll; 13 are in the \$4.00 - \$4.99 range; 20 are in the \$3.00 - \$3.99 range; and 12 have rates under \$3.00. The premium rate indices are based on data from 51 jurisdictions for rates in effect as of January 1, 1996.

## 2. How Premium Rates Compare Between State-Fund and Non-State Fund States

Table D.a.2-3 summarizes average premium rates per \$100 of payroll for various aggregations of state categories for the years 1990 through 1996. Component data to compute technically correct state aggregations was not available. Instead, proxy measures of state aggregate weighted average premium rates were computed by weighting 1990 and 1992 estimated state manual rates by 1992 premiums; 1994 and 1996 premium index rates were weighted by 1994 premiums<sup>3</sup>.

For all state-fund states, the 1990, 1992, 1994, and preliminary 1996 premium weighted average premium index rates amounted to \$4.94, \$5.47, \$5.12, and \$4.52 respectively. In contrast, the non-state-fund states' premium index rates for the comparable periods amounted to \$3.73, \$4.18, \$4.25, and \$3.40. State-fund state aggregate average premiums were roughly 30 percent greater than non-state-fund states' average premiums in 1990, 1992, and 1996; the difference in 1994 was closer to 20 percent. Specific state premium ranks are displayed in Table D.a.2-1.

It is interesting to acknowledge that the state-fund, non-state-fund comparison of weighted average premium rates for 1990 through 1996 conforms on an aggregate basis with the results of one of the only available, credible studies on the differences in costs to employers for the aforementioned state aggregations. Krueger and Burton<sup>4</sup>, in a study conducted for the period 1972 through 1983, found indications that the presence of a state fund in a state leads to an average increase of nearly 20 percent in average insurance costs to employers when numerous other factors were controlled for such as benefit levels, injury rates, and the extent of unionization. The researchers hypothesized that, among other things, the result may have been

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<sup>3</sup> The rates used were developed and published in workers' compensation premium rate ranking studies by the Information Management Division, Department of Consumer and Business Services. The premium weighting procedure is imperfect yet provides meaningful, relative state aggregate premium rate indices for comparative purposes.

<sup>4</sup> Alan B. Krueger and John F. Burton, Jr., "The Employers' Costs of Workers' Compensation Insurance: Magnitudes, Determinants, and Public Policy," in The Review of Economics and Statistics, 1990.

due to possible inefficiency associated with a state bureaucracy, but the findings were inconclusive.

The Krueger and Burton findings were developed from state specific data using cross-sectional time series analysis, rather than using aggregate data in a manner similar to the development of the weighted average premium weight comparison. When a single period cross-sectional analysis of state specific data for 1992 is conducted relating the 1992 premium rate rank with the presence of a state fund and average benefit per covered employee (data in Table D.a.2-1), the statistical characteristics of the state fund variable is correct, but the variable is not statistically significant<sup>5</sup>. This means that the relationship indicates that states with state funds generally have a higher rank,--that is, higher premium rates--after controlling for benefit level in 1992, but one cannot statistically conclude that the presence of a state fund is a major determinant in premium rate ranks in 1992.

The period over which the Krueger and Burton study was conducted is substantially dated at this time. Moreover, the simple cross-sectional analysis for 1992 has numerous limitations. Important answers to the public policy issue concerning whether generally the presence of a state fund leads to higher premium rates will not be forthcoming until an update of the Krueger and Burton study, and other significant research is conducted. Even if an updated study found a general correlation between the presence of a state fund and higher premium rates, this would not mean that Oregon would necessarily follow this rule. For example, Oregon would appear to be an exception to this correlation today.

A review of the change in premium rate ranking for state-fund states (Table D.a.2-1) suggests that improvement in rate ranking-- that is, lower state relative premiums--is possible for state-fund states. Notice that for state-fund states with an assigned risk pool between 1990 and 1992, six of the eight states experienced improvement in their ranking. Conversely, none of the nine non-ARP state-fund states experienced improvement. Between 1992 and 1994 there were six state-fund states that had assigned risk pools. Of these, four showed improvement in their ranking. Of the eleven non-ARP state-fund states, only three improved. The preliminary data for 1996 shows improvement in five of the six ARP state-fund states, and in seven of the eleven non-ARP state-fund states.

Certainly the noted improvement is a result of much more than the simple presence of a state fund. For example, Oregon's improvement stems predominantly from the effects of legislative reform and concomitant premium rate decreases. Other state-fund states have enacted reform legislation as well. Also, some significant insurers in state-fund states may have redoubled efforts to be efficient and effective in claims cost containment. Clearly, there are many factors that affect insurance premiums in a given state.

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<sup>5</sup> In this analysis conducted by the Information Management Division of DCBS, the average benefit level factor was available for only 23 of the 45 states of interest. It may well be that the limited amount of data contributes to the finding that the presence of a state fund is not statistically significant in the relationship investigated. Nevertheless, the statistical relationship does explain over 57 percent of the state to state variability in the 1992 premium rate ranking.

### 3. Types of Pricing Plans in Oregon

The competitive rating environment in Oregon provides insurance-buying employers with a more multi-faceted pricing system than any single insurance company could be likely to design. Insurers independently devise rating plans and factors for modifying employers' premiums. Every insurer must file each plan or rating value with DCBS with appropriate supporting information for review prior to use.

"Pricing" is often understood to include policyholder dividends. Insurer dividend plans are subject to solvency and unfair discrimination standards, but except for some proposals to group employers for dividend calculations, they do not need to be filed with or reviewed by DCBS.

Premium rating begins with rates by classification for each insurer. Insurers assign payroll for an employer to one or more classifications appropriate for that employer. They then multiply the payroll for each class (in units of \$100) by the premium rate for that class. The total of these products for all classes is called "manual premium" simply because insurers usually publish class rates in a manual.

The next step is experience rating for any employer that has averaged over \$2500 in manual premium per year. DCBS rules mandate a uniform experience rating plan for all insurers. To the extent the previous experience for an employer differs from the averages expected for its classifications, the experience modification will adjust the manual premium accordingly. The result of this modification is called "standard premium" because it is the basis of most subsequent rating steps.

Insurer premium rates include provision for expenses, taxes, and profit. Because not all operating expenses vary in direct proportion to expected claim costs, insurers reduce premiums by a percentage that progressively increases with the amount of standard premium. This volume discount is called "premium discount." The discounts usually begin above \$5,000 standard premium. Nearly all insurers also charge an "expense constant" to cover fixed expenses common to all policies regardless of size. If standard premium is less than \$500, most insurers charge a minimum premium which sometimes varies by class and may be as high as \$500. SAIF charges a \$500 minimum premium, first approved by DCBS as part of a financial recovery plan late in 1989. The upper bounds on these minimum premiums filed by major private insurers range from \$250 (Fireman's Fund, Chubb, Grocers, Orion, Reliance, SAFECO) to \$450 (Industrial Indemnity, Hartford, Paula) for each policyholder. As of this writing, few have filed for \$500 (American Interstate, Lumbermen's Underwriting Alliance, Sentry).

Employers and insurers may agree in advance to use a "retrospective rating" plan whereby the insurer will adjust premium after the fact depending on the actual claim costs. These plans are usually available only to employers with more than \$25,000 standard premium. Eligibility is higher for some insurers. The adjusted premium may be greater or less than standard premium and will be subject to maximums and minimums and a fixed basic charge. The plan percentages are designed so that the expected retrospective premium will average the same as standard premium minus premium discount.

Some insurance companies offer further rating plan refinements. Some offer small credits or debits based on the timing of premium payment. Some offer credits for drug-free workplaces or in areas where they can refer injured workers to managed care organizations. Some insurers offer group rating plans whereby they calculate premiums of group members using the combined experience of the group. These plans usually supplement experience rating of the individual accounts or allow retrospective rating on a group basis.

One form of rating, known as "schedule rating" where an insurer can adjust employer premium based on the judgment of an underwriter, is used in some states but generally has been presumed unfairly discriminatory in Oregon. To overcome this presumption, all plans for modifying individual employers' premium must follow reasonably objective criteria and provide only specific credits or debits.

Some insurers have gained DCBS approval to use a few subclassifications. Oregon's competitive rating laws allow insurers to identify segments of standard classifications and to propose rate differentials for these. This was a common practice of several insurers from enactment of competitive rating in 1981 until the passage of SB 1197 in 1990 requiring all the subclasses in use by any insurer to be available in the assigned risk plan. That requirement led to many independent subclasses becoming standard statewide classifications.

The Oregon Workers' Compensation Insurance Plan, or the "assigned risk plan" (Plan) provides coverage to employers unable to find coverage from insurers voluntarily. The Plan features a modest premium discount up to as high as 7 percent and charges a minimum premium that varies by class to a maximum--since the beginning of 1996--of \$500. The Plan uses a few other rating modifications that are explained in Section G of this report.

#### 4. Competitiveness of Pricing Plans

Insurers are able to compete effectively in all stages of their pricing systems described in the previous section. This section contains references to several pricing terms explained in that section. Since premium rates by class in an insurer's rating manual are the first visible pricing component, insurers often begin with them when designing a pricing strategy.

Insurers base premium rates on loss cost rates filed with DCBS by the National Council on Compensation Insurance (NCCI), the licensed rating organization. These loss cost rates are prospective estimates of average claim costs only. The DCBS Insurance Division reviews these in great detail. ORS 737.320(3) prohibits NCCI from filing rating values that include provision for expenses, taxes, and profit. Each insurer must then file its own premium rates that include these provisions and must also give consideration to investment income (ORS 737.310(9)).

An insurer can also offer its own experience data or other supporting information to justify claim costs that differ from the averages NCCI computes by class from the total experience of all companies. The differences are usually uniform percentages for all classifications. The insurance industry, NCCI, DCBS Insurance Division actuaries and regulators in other states have focused much attention on refining the NCCI classification ratemaking procedure. Hence, very

few companies have attempted to bear the burden of justifying independent class rate differentials.

Insurance companies request different rate levels (relative to the NCCI advisory loss cost rates) based on several factors such as:

- Underwriting selection (claim costs expected to differ from statewide averages)
- Operating expenses
- Investment income opportunity
- Capital and profitability requirements

Clearly, the predominant factor driving rate levels is market competition. Nonetheless, the Insurance Division will not approve a rate unless the company demonstrates that the rate level is justified and sustainable. The marketplace simultaneously recognizes several different rate levels--or market sectors. The current range is from 1.075 times loss costs for SAIF, and a few others up to about 1.700. Rates effective January 1, 1997 for the Oregon Workers' Compensation Insurance Plan, are approved at 1.575 times loss costs and will be the effective ceiling.

A group of affiliated insurers will often file different rates for different insurance companies in order to participate in more market sectors. Since SAIF is only one company, DCBS has allowed it to use more than one rate level. It currently uses rates at 1.075, 1.15, 1.30, and 1.50 times approved loss cost rates. Liberty Northwest (LNW), a primary competitor, operates autonomously from its parent, Liberty Mutual, and DCBS has also allowed it to use multiple rate levels, currently at 1.08, 1.15, 1.30, and 1.475 times approved loss cost rates. A few other independent companies have similar multiple rate "tiers." Insurance Division Oregon Administrative Rules (OARs), require these insurers to use substantially objective rules for assigning employers to different rate levels. An underwriter cannot assign rate levels based solely on subjective judgment.

There is no official standard for premium discount percentages, but most insurers file discount tables identical to those designed by NCCI and used in other states. SAIF, LNW, Safeco, and a few other companies have supported using more aggressive discount schedules ranging up to 15 to 20 percent for the highest ranges of standard premium. By comparison, the latest NCCI table reaches 12.4 percent for the layer of standard premium over \$500,000.

Competition in retrospective rating plans is more sophisticated. Insurers usually include investment income in class premium rates by discounting claim reserves for the timing of claim payments. But for retrospective rating, claims costs are undiscounted so investment income must be an offset to expenses. SAIF, LNW, and a few other companies use an undiscounted "expected loss ratio" as the basis for their retrospective rating plan values. This tends to reduce the basic or fixed cost portion of retrospective rating premium.

Competitive rating allows--and thereby encourages--insurers to design innovative rating plans and file them independently with DCBS. The combination of all rating plans should offer Oregon employers greater opportunities for equitable savings than they could find from a single

monolithic rating system designed by NCCI or even DCBS. These innovative ideas must have statistical substantiation or other reasonable justification for DCBS approval.

Great American has an approved 5 percent credit for drug-free workplaces. SAIF and a few others have a 5 percent credit for employers in parts of the state where a DCBS-certified managed care organization is available. EBI Insurance Company has a sophisticated plan giving specific credits and debits for precisely-defined safety and cost-reducing measures adopted by individual members of its "partnership" groups.

Rating groups are a major means of competition for small- and medium-sized employers. These groups and the rating adjustments they offer are described in the previous section. The original concept may have been that a sponsoring association could provide safety and loss control services specific to similar employers. Legislative revisions to ORS 737.316 in 1983 and 1990, however, removed requirements for group members to be members of an organization formed for purposes other than buying insurance and that the members be in similar industries. Hence, several groups are artificially formed by insurers and are heterogeneous, or highly diverse.

Many insurers, primarily those operating countrywide, have proposed large deductible plans, more properly called "loss reimbursement" plans. With these plans, the insurer still administers and pays all claims, but the employer reimburses the insurer for claim costs up to an agreed limit in exchange for a substantial premium credit. Insurers describe these plans as an alternative to self-insurance and only offer them to very large employers. Because of some possible abuses, DCBS has carefully designed and adopted OARs to specify high standards for these plans. Only a few have been approved as of the writing of this report. Because the plans are similar to retrospective rating plans with substantial deferral of premium payment, SAIF and other insurers that primarily operate in Oregon and already use such comparable plans have shown less interest in large deductibles.

### c. Oregon's Market Entry and Exit Characteristics

Compared to other industries, most insurance markets have few entry barriers. Insurance companies do not have to build large factories or invest in years of research and development. Workers' compensation is a little more difficult because an insurer needs to find people who are familiar with the specific workers' compensation and insurance laws of this state. For initial market entry, an insurer can contract with independent firms for claim management, premium audit, and other services. Most insurers with substantial market shares have developed their own in-house staffs.

The minimum capital requirement for forming an Oregon domestic workers' compensation insurer is \$3.5 million (ORS 731.554). A company domiciled in another state and having a recent examination report from that state may not have an extensive wait for DCBS authorization. Thereafter, both domestic and foreign companies must maintain capital and surplus above risk-based capital regulatory action levels.

The more significant barrier to market entry is competition, as described in section D.b.4 of this report. A company with little or no previous Oregon experience has difficulty justifying a highly competitive premium rate level by demonstrating lower than average claims cost. A few companies with substantial business in other states have been able to provide convincing evidence of superior performance with underwriting strategies similar to those they propose to use in Oregon. Others have shown low expense or profitability requirements. Several regional or national insurers have entered Oregon when employers they insure in other states have operations here.

Table D.c.1.-1 shows 1995 market entrants and exits. Market entry was defined for this exhibit as having at least \$100,000 direct written premium for 1995 but less than that or none in 1994. If a company wrote more than \$100,000 in 1994 but less or none in 1995, it was counted as a market exit. Most of the exits and some of the entrants -- such as companies in the Allianz, CIGNA, CNA, and Zurich groups -- are due to corporate reorganizations and other reasons external to the Oregon workers' compensation market. The notable changes are the entrance of companies new to Oregon such as Business Insurance Company and Paula Insurance Company.

A company might be induced to leave the Oregon market either because DCBS revoked or suspended its certificate of authority to do business or because its management decided the prospects for future profitability were less than acceptable. Neither case has been common in recent years.

Several company managers have said that competing in Oregon with SAIF and Liberty Northwest is very difficult. At least part of the difficulty may arise from the dominance of these two organizations in the Oregon workers' compensation marketplace both in terms of market share and name recognition. Nevertheless, many new companies have expressed an interest in becoming authorized to transact workers' compensation insurance. The last occasion for many companies to exit the Oregon market was in the mid-1980s when workers' compensation insurance was unprofitable countrywide and claim costs may have been growing even more rapidly in Oregon than elsewhere. The inducements to leave the state appear related more to economic or system conditions than to the structure of the Oregon insurance market.

#### d. Other Characteristics of Oregon's Competitive Environment

Workers' compensation insurers compete in many different ways. Pricing competition is the most obvious, as described in Sections D.b.3 and D.b.4. This aspect of competition seems to focus on premium rate levels, retrospective rating parameters, and rating groups. Large deductible plans have been approved only this year and for only a few insurers. They may emerge as a competitive factor in the future.

Dividends had not been a substantial factor in the Oregon market since the advent of competitive rating in 1982 but have become more evident since the 1990 reforms. Workers' compensation insurance has been profitable in Oregon this decade. Claim costs may have decreased more than the department could objectively anticipate in 1990. Also, most insurers are conservative with investment income considerations in pricing. As described further in Section I.c, SAIF has

significant investment income advantages. However, insurers to some extent, return investment income margins to policyholders as dividends. Insurers are prohibited by Oregon law to promise any dividends, but are allowed to display historic dividend information. Further discussion of dividends is in Section I.b.

Insurers do compete on the basis of service, reputation, and financial strength. Most advertising is related to these factors. Several insurers enter the Oregon market in a particular segment for which they have expertise, such as agriculture, logging, hospitals, or auto dealers. Some will market through sponsorship of independent associations. SAIF advertising asserts its ability to provide quality service throughout the entire state.

Other aspects discussed in this report that particularly affect SAIF's ability to compete include its legal distinctions (Sections F and K), its relation to the assigned risk plan (Section G), its ability to discount loss reserves (Section H.b), tax advantages (Section N), and exemption from assessment by the guaranty association (Section O).

## **E. The Department's Role as Regulator of the Oregon Workers' Compensation System**

This section of the report outlines the DCBS's role as regulator of the Oregon Workers' Compensation System.

### **a. Insurance Division Statutes and Relevant Activities**

The Insurance Division is charged with protecting the insurance-buying public by ensuring the financial soundness of insurers, availability and affordability of insurance, and fair treatment of insureds and claimants. In carrying out this charge the Insurance Division performs a major balancing role for the state: Protecting the interests of the insured employers and their employees with the least amount of intrusion possible to the 374 insurance companies doing workers' compensation business in Oregon.

#### **(1) Relevant Statutes:**

There are numerous Insurance Division statutes that specify and authorize the regulatory role of the Division: ORS Chapters 656, 731, 732, 733, 734, 735, 737, 742, 744, and 746. The Division's statutory regulatory activities are discussed below.

#### **(2) Relevant Activities:**

(a) Administrative Services and Operations. In addition to providing administrative support to the Insurance Division, Administrative Services Operation Section, under ORS 744 Chapter, receives and reviews applications and appointments for agents, firms and corporations licensed to sell, counsel or adjust workers' compensation insurance in the state of Oregon. The section, under ORS Chapter 744, establishes licensing requirements for insurance agents and oversees the development and administration of licensing examinations. This Section, under ORS 737 Chapter, also conducts contested



case hearings and alternative dispute resolution processes for employers challenging their workers' compensation insurance audit billings and application of rating system. The Section is also responsible for Insurance Division rulemaking, legislative and budget matters.

(b) Rates and Forms Regulation. All workers' compensation insurer and rating organization policies, rates, rating plans and rating system are required by ORS Chapters 742, 737 and 746 to be submitted to the director for approval. The Rates and Forms Section oversees this approval process. The policies and rating systems are reviewed by the section for legality and fairness. The rating system review is in accordance with ORS Chapters 737 and 746 to ensure that the rates and rating plans are not inadequate, excessive, or unfairly discriminatory. In some cases, advertising and marketing practices are also reviewed by this section under ORS Chapters 742 and 746. Workers' compensation insurance safety dividend groups, rating groups and insurers' dividend practices are also overseen by this section for compliance with ORS Chapters 737 and 746. The section, under ORS 737 Chapter, monitors: (1) workers' compensation insurer maintenance of a premium audit program to aid in achieving equitable premium charges to Oregon employers and for the collection of creditable statewide data for ratemaking, (2) employer education of the premium audit reporting function of the rating system, and (3) a continuing premium test audit program providing for the auditing of all insurers including employer records. In addition, this section also conducts, or causes to be conducted, ratemaking examinations of insurers to assure compliance with ORS Chapters 737 and administrative rules for workers' compensation insurance.

The Director is required by ORS 656 Chapter to promulgate a workers' compensation insurance assigned risk plan for the equitable apportionment among SAIF and private workers' compensation insurers of subject employers whose coverage workers' compensation insurers including SAIF object to providing. The Rates and Forms Section oversees the operation of this assigned risk plan.

The Rates and Forms Section also oversees the ORS 737 Chapter licensing and examination requirements for workers' compensation rating organizations.

(c) Company Regulation. The Company Regulation Section is responsible for the licensing and examination of all domestic, foreign and alien insurers under ORS Chapters 731, 732 and 733. Company Regulation activities under ORS Chapter 731 include maintenance of files on approximately 374 licensed workers' compensation insurers; review under ORS Chapter 731 of annual financial statements; review under ORS Chapter 731 of applications to transact workers' compensation insurance business in Oregon; collection from these insurers of premium and retaliatory taxes under ORS Chapter 731; supervision under ORS Chapter 735 of all surplus lines business in Oregon (certain self-insured workers' compensation employers were grandfathered under ORS 656 Chapter for obtaining their excess workers' compensation insurance from the surplus lines market.); and, maintenance under ORS Chapter 731 of \$1.2 billion special security deposits required by licensed workers' compensation insurers.

Examination activities under ORS Chapter 731 include examination of the financial condition, market conduct, and insurance operations for all workers' compensation insurers domiciled in Oregon at least once every three years, as well as participation in the examination of other foreign and alien insurers. Additional responsibilities under ORS Chapter 731 include administration and review of filings for new company formations and applications for mergers and/or acquisitions of domestic workers' compensation insurers. The examinations staff also supervises the rehabilitation and liquidation activities involving domestic workers' compensation insurers under ORS Chapter 734 and ancillary receiverships on foreign and alien workers' compensation insurers.

(d) Employer/Employee and Insurer Protection. The Consumer Services and Enforcement Section responds to ORS Chapter 746 trade practice complaints and concerns brought to the attention of the Insurance Commissioner involving the transactions of workers' compensation insurance. Inquiries and complaints are received by phone, letter, and in person. When there is reason to believe that the insurance code or administrative rules there under have been violated by an individual, agent, agency, or insurer, under ORS Chapter 731, an investigation may be conducted and evidence may be presented at a formal hearing. Under the Insurance Code, hearing orders may sanction or in some instances provide remedial relief for the aggrieved employer, worker or competing insurer.

**b. Workers' Compensation Division Statutes and Relevant Activities**

The Workers' Compensation Division is charged with administering the workers' compensation laws; this includes, injured worker benefit assessment, regulation of insurer claims management, medical treatment and medical fee dispute resolution, and employer coverage regulation.

**(1) Relevant Statutes:**

(a) SAIF Corporation is subject to the statutes governing the payment of compensation and processing of workers' compensation claims as are all other workers' compensation carriers and self-insured employers; SAIF may avail itself of the same remedies as other insurers when its decisions are contested by claimants. See ORS 656.202 through 656.340.

(b) SAIF's claims examiners are subject to the same certification requirements as are claims examiners of private insurers, self-administered self-insured employers and third-party administrators. See ORS 656.780.

(c) SAIF, the director, and the Workers' Compensation Board may contract among themselves for such exchange or payment of services as will reduce the overall cost of administering ORS Chapter 656. Such arrangements are not subject to review by any court or administrative body. See ORS 656.726(6). Though this provision is used

infrequently, examples as such arrangements may include exchanges of information, providing access to databases and exchanging staff on job rotations.

(2) Relevant Activities. "Insurer" includes SAIF, self-insured employers and private carriers. All are subject to WCD's regulation.

(a) Compliance Audits. The Workers' Compensation Division regularly audits insurers to determine compliance with statutes and rules governing claims processing. This is a three-phase audit.

Phase I is a quarterly audit of five key performance measures based upon reports filed by insurers with the division. Three of the measures are currently used as a basis for penalties. Failure to timely accept or deny the claim, pay the first temporary disability payment, or report claims to the director timely at least 80% of the time results in civil penalties. The Workers' Compensation Research Institute reported in 1996 that Oregon has the highest rate of timely first payment of benefits of any state which it has surveyed. (See The Impact of Oregon's Cost Containment Reforms, Workers' Compensation Research Institute, 1996.) See Table E.b.2(a)-1 for SAIF's performance in relationship to private insurers and self-insured employers.

Phase II is a triennial audit of all 200 active self-insureds and approximately 250 insurers, including SAIF. The purpose of the audit is educational. A sample of claims is reviewed for compliance with statute and rules. The findings are given to the insurer together with information and technical assistance to help the insurer correct any problems. Training may also be provided, if requested. Such training is certified for continuing education credits for the certified claims examiners. Civil penalties are not assessed in connection with this audit. If the Phase I or Phase II audit reveals significant problems, the insurer will be scheduled for a full Phase III audit, in which WCD's auditors review a larger sample of the insurer's claims processing under the statute and rules. Substandard performance results in one or more of the following:

- civil penalties (all insurers);
- suspension or revocation of the insurer's authority to issue guaranty contracts (private insurers and SAIF);
- request that the director in his capacity as Insurance Commissioner revoke the insurer's authority to transact workers' compensation insurance (private insurers);
- revocation of the right to process claims out-of-state (self-insurers);
- revocation of an employer's authority to self-insure; or,
- a settlement in which the insurer agrees to come into compliance within a certain period (probation) or be subjected to a stronger sanction than originally contemplated.

(b) Special audits and investigations. Under ORS 656.726, the director has broad discretion supervising, enforcing and regulating all persons governed by ORS Chapter 656. That broad power was exercised most notably in late 1991 in WCD's investigation

of SAIF's exceptionally high rate of claims denials. A second audit of SAIF's practices in regard to claim denial was conducted in early 1993 to ensure SAIF's compliance with the director's expectation that its practices conformed to the legal opinion of the Attorney General in regard to certain of its claims investigation practices. The second audit revealed SAIF to be in compliance with the law, rules and opinion of the Attorney General.

## **F. Statutory and Regulatory Differences Between SAIF and Private Carriers**

There are numerous statutory and regulatory differences between the state's treatment of SAIF and its treatment of private carriers. These differences can be understood with the help of a chronology, outlining application of the state's Insurance Code to SAIF over the years, plus a description of ways in which the state currently applies the Insurance Code to SAIF differently than it does to private insurers. This section will also discuss differences with respect to the state's workers' compensation laws and regulation by the Workers' Compensation Division.

### **a. Insurance Division Regulation of SAIF**

#### **1. Evolution of SAIF's "Subjectivity" to the Insurance Code**

At its creation, SAIF was not subject to state insurance regulation. In 1972, the legislature changed this, making SAIF subject to the state Insurance Code with a focus on ratemaking and trade practices. In the following two decades, more provisions were added without any clearly-defined strategy to guide implementation of those provisions. What follows is a chronology of SAIF's regulatory development:

- |               |   |
|---------------|---|
| July, 1914    | SAIF's predecessor, the State Industrial Accident Commission (SIAC), began operation under a three member commission.   |
| January, 1966 | SIAC was succeeded by a newly-created state agency, initially called the State Compensation Department (SCD), with a governor-appointed manager. The department later changed its name to State Accident Insurance Fund (SAIF) to avoid public confusion with the Workers' Compensation Board, which was created at the same time. The state's "three way" system -- under which employers could insure their workers' compensation risk with the state, with a private insurer, or by qualifying as self-insured -- was established at this point. |
| January, 1972 | SAIF was made subject as a domestic insurer to rate making provisions and certain administrative, accounting, and trade practice provisions of the Insurance Code. However, SAIF was expressly exempted from the code's licensing requirements.   |
| October, 1977 | SAIF was made subject to the Insurance Code's trade practice provisions regarding dividends.  |

- July, 1979 SAIF was made subject to the Insurance Code's policy chapter, which describes requirements that must be fulfilled by any insurance policy.
- October, 1979 SAIF was made subject to a workers' compensation insurance assigned risk plan promulgated by the Insurance Commissioner.
- July, 1980 The legislature changed SAIF from a state agency into an independent public corporation, with a board of directors appointed by the governor. The new corporation was exempted from a variety of laws that govern most state agencies, but subject to certain enforcement powers of the state insurance commissioner and Insurance Code provisions dealing with agent licensing.
- January, 1988 SAIF was made subject to Insurance Code provisions regarding hearings for insureds who have grievances with application of the rating system.
- January, 1990 Application of the Insurance Code's chapter 744, which describes licensing requirements for insurance agents, adjusters and consultants, was limited to agent licensing in SAIF's case.
- September, 1991 SAIF was made subject to Insurance Code sections regarding unfair claim settlements and undefined trade practices.
- November, 1993 Insurance Code chapter 731 provisions regarding exchange of information by regulated carriers were enacted, and applied to SAIF as well as other subject insurers.
- September, 1995 SAIF was made subject to Insurance Code provisions regarding the effect of non-compliance with rating regulations.

## 2. Insurance Code Differences Between SAIF and Private Insurers

There are numerous Insurance Code regulatory differences between SAIF and private insurers:

- The director has authority under ORS 737.320 to set pure premium rates for all insurers if done in conjunction with the director's powers under ORS 731.216 regarding establishment of a rating bureau. SAIF is not subject to the director's rating bureau powers of ORS 731.216.
- Unlike private insurers, SAIF is limited under ORS 656.752(1) to write only workers' compensation insurance.
- Private insurers are entitled to set rates taking into account, among other things, the requirement for earning profits (see ORS 737.310(9) and 737.320(4)) which provides protection against insolvency, and to otherwise fairly underwrite the availability of their insurance. SAIF, on the other hand, is compelled by ORS 656.752(2), "To make insurance available to as many Oregon employers as inexpensively as may be consistent with the overall

integrity of the Industrial Accident Fund..." and by ORS 656.017, to provide workers' compensation insurance for agencies of the State of Oregon.

- Under ORS 731.146(2) private insurers can directly write workers' compensation insurance for Oregon employers' multi-state operations. This means that Oregon employers with not only operations in Oregon but also other states may have all of their operations (multi-state operations) covered by a private insurer. This can be a competitive advantage to private insurers. As an instrument of this state, SAIF is denied this multi-state advantage by sister state laws that prohibit foreign (out-of-state) governments from transacting insurance. (See ORS 731.390.) This means that SAIF is effectively prohibited from insuring Oregon employers with multi-state operations that desire multi-state coverage from a single insurer. Oregon's reciprocal agreements regarding ORS 731.454, which precludes domestic insurers from transacting business in jurisdictions where not authorized, further bar SAIF from issuing multi-state employer coverage.
- Unlike private insurers, SAIF is not subject to minimum capital requirements, and there is no statutory definition of solvency applicable to SAIF.
- Pursuant to ORS 731.240, insurers have access to a due process remedy for rate disapproval by the Insurance Division under ORS 737.320; however, ORS 731.240 is not available to SAIF, thus denying it access to that process.
- Complaints and investigations involving SAIF do not have the same confidentiality as those involving private insurers under ORS 731.264.
- Pursuant to Attorney General Opinion (OP-6176) and notwithstanding ORS 733.030, SAIF may discount its loss reserves. Private insurers are more restricted in their ability to discount reserves. (See Section H.b.4 for further explanation.)
- SAIF is exempt from provisions of the Oregon Guaranty Association laws (ORS 734.510 et seq.).
- The director has access to cease and desist remedies (ORS 737.045) to instantly address pending or in-use rate filings and accountability for any reasonable hearing expenses. These are applicable to private insurers, but not to SAIF.
- SAIF believes that the Insurance Code rate making chapter is subordinate to its rate making powers under the Workers' Compensation Law. SAIF testified this position to the House Labor Committee during the 1993 regular legislative session, and alluded to such a position again in a 1993 comparison publication. SAIF has never publicly retracted this position. Former DCBS Director Gary Weeks, when testifying before the House Labor Committee on SB 182, expressly rejected SAIF's position, noting that it is based upon an improper construction of subsection (2) of ORS 731.028.

- ORS 737.310 sets standards against unfair discrimination by insurance carriers. When reviewing insurers' class rate deviation filings to verify compliance with these standards, the director currently only has access to certain rating data regarding rate relativities of private insurers, pursuant to ORS 737.230. Because ORS 737.230 is not applicable to SAIF, the director lacks the ability to compel verification of the corporation's compliance with ORS 737.310.
- Pursuant to subsection (4) of ORS 731.028, ORS Chapter 744 only applies to SAIF concerning the regulation of agents.
- While SAIF is subject to the dividend trade practice provisions of ORS 746.145 and 746.150, it is not subject to the companion statutory rebate and inducement provisions of ORS 746.035 and 746.045, which underpin the OARs on dividend trade practices (OAR 836-80-145 et seq.).
- ORS 656.504 authorizes SAIF to utilize cents per hour in lieu of established \$100 units of payroll, and to set minimum premiums. This exposure base is currently inconsistent with that approved under ORS Chapter 737. Thus, if SAIF chose this base there would be two distinct rating and data systems for Oregon unless the licensed rating organization also filed and received approval for switching to such a system. Notwithstanding the "...sound principles of insurance" requirement of ORS 565.752(2)(B), this provision's authority for SAIF to prescribe minimum premiums also poses conflict of law issues with ORS 731.028(1) and (3).

b. Workers' Compensation Laws and Workers' Compensation Division (WCD) Regulation

Both the statutory and regulatory differences of the treatment of SAIF regarding workers' compensation law and WCD regulation are summarized below.

(1) Statutory Differences.

- Contracting for services. ORS 656.726(6) provides that the director, SAIF and the Workers' Compensation Board may contract and pay for such services among them as will reduce the overall costs of administering ORS chapter 656, without being subject to review by any court or other administrative body. This might include data sharing arrangements, providing for exchanges or rotation of staff for training purposes or special projects, etc.
- Representation of SAIF, WCD and the Insurance Division by the Attorney General. ORS 180.060(5) provides that "the attorney general shall...perform all legal services for the state or any department or officer of the state;" therefore, the Department of Justice provides legal counsel and representation to both the director and SAIF. While in most instances this serves the public interest well by preventing agencies from suing one another, this provision creates the potential for conflict on the part of the Department of Justice when it provides counsel to both DCBS and SAIF. The Attorney General has the authority and the duty to determine when it is not in the public interest or it would pose a

conflict to concurrently represent more than one agency or public officer, and to authorize agencies and officers to employ their own counsel. The Department of Justice (Industrial Accident Section of the Civil Enforcement Division, which advises SAIF Corporation) exercises this authority most commonly in cases where the responsibility for the claim is at issue between a SAIF-insured employer and a noncomplying employer (NCE). Since SAIF processes NCE claims on behalf of the director, retention of outside counsel minimizes the potential for conflict of interest inherent in such cases.

- SAIF as the state's insurer. Unlike other large public and private employers, under ORS 656.017(2) the State of Oregon cannot self-insure or insure with a private insurer: it must insure its workers' compensation risk with SAIF.
- SAIF processes all pre-1966 workers' compensation claims. SAIF continues to process all claims that occurred prior to 1966, as it was the only insurer allowed by statute preceding the passage of the "three way" law in 1966.

## (2) Regulatory Differences

WCD treats SAIF the same as private insurers in regard to enforcement of workers' compensation law. However, there are some differences in the relationship with SAIF based on the statutory provisions cited above. For example, SAIF is currently the sole processor of the claims of noncomplying employers on behalf of the director, which means SAIF is subjected to an additional audit in which WCD reviews 100% of such claims after closure. (Since the 1995 legislative session, the director has had the authority to contract with other claims processing agents in addition to SAIF, but no such contracts currently exist.) In its processing of claims and reporting to the department, SAIF has the same standards and obligations as other insurers, and suffers the same penalties for substandard performance.

## G. Assigned Risk Plan

### a. Characteristics of the Plan

The assigned risk plan (Plan) is a reinsurance pool mechanism created under ORS 656.730 and OAR 836-43-0001 et seq. These rules, adopted in 1979, utilized the existing National Workers' Compensation Reinsurance Pool. The National Pool is the non-profit unincorporated association of insurers that serves as a reinsurance facility for workers' compensation insurance in a number of states. The National Pool is administered by the National Council on Compensation Insurance, Oregon's licensed rating organization for workers' compensation insurance. Under the Plan, all Oregon workers' compensation insurers, including SAIF, are required to be members of the National Pool. The members of the National Pool enter into Reinsurance Agreements with Servicing Carriers for the purpose of sharing the claims costs of the Oregon assigned risks. These Reinsurance Agreements distribute risk, and define the obligations on a quota share basis among the parties.



The Servicing Carriers write and service the policies for a fee paid by the National Pool. Services include auditing and collecting premiums, paying all premium taxes, providing loss control services and paying claims. Insurers wishing to be Servicing Carriers must be nominated by the National Pool and approved by the Director. The National Pool, not the Servicing Carrier, is responsible for the gross liability of all losses for policies written under the Plan. Under the Plan, an insurer that terminates participation in the National Pool continues to be governed by the Reinsurance Agreement for risks subject to the agreement prior to midnight of the effective date of such termination.<sup>6</sup>

Plan financial results through the end of 1995 for the latest three policy years are stable (losses of \$1.9, \$3.0 and \$4.1 million for 1995, 1994 and 1993 respectively). A bid process to determine servicing carriers, implemented April 1, 1996, should help maintain a small operating loss for 1996 and forward. Plan premium for 18,046 policies at the end of 1995 was \$43,799,691. Over two-thirds of the policyholders are small employers with premiums under \$1,000.<sup>7</sup>

The Plan uses some rating rules not generally available in the voluntary market. Two of these were required by Chapter 1, Oregon Laws 1990 (Senate Bill 1198). First, all subclassifications approved by DCBS for any insurer must be available to employers in the Plan. As a result, many insurers ceased to view subclasses as an important competitive tool. The National Council on Compensation Insurance reviewed relative claims experience of subclasses that had been in use for a few years and found several that merited use as standard classes available to all insurers. Insurers withdrew other subclasses where rate differentials were not merited. Relatively few subclasses remain on file with DCBS for use by particular insurers and hence by the Plan. The second rating difference mandated by SB 1198 is a "non-rated" credit meant to give smaller employers that are not eligible for experience rating a benefit similar to rating tiers used by some insurers in the voluntary market. The credit is currently 11 percent, subject to a maximum credit amount of \$500.

The department has found that the voluntary market generally tends not to insure new small businesses due to underwriting and other business considerations. Because there often may be no other reason to decline a particular employer, the Plan requires the voluntary market to subsidize employers with no previous record of coverage and with Plan premium less than \$2,500. The subsidy is currently a 15 percent premium credit for the first two years in the Plan.

The voluntary market may deny some employers because of poor claims experience. The experience rating process used in the Plan includes an assigned risk adjustment program (ARAP) for employers in the Plan that are eligible for experience rating. The ARAP adjustment compounds the experience rating modification for employers with claims experience worse than average even after the normal experience rating formula. Premium for larger employers may increase by as much as 49 percent under ARAP.

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<sup>6</sup> Exhibit G.a.1. 1992 Articles of Agreement - National Workers' Compensation Reinsurance Pool.

<sup>7</sup> NCCI 1995 Residual Market Annual Report.

b. SAIF's Assigned Risk Plan Responsibilities

SAIF is a National Pool participant in the Plan. It is obligated to accept its quota share reinsurance of the Servicing Carrier's gross liability for losses under Oregon policies. Its five year average quota share assessments on a calendar year operating basis have been approximately \$3.8 million per annum. SAIF has also been a servicing carrier since the inception of the Plan. Under the current servicing carrier bidding system, SAIF has a 1996 quota of 25%. This means that, on average, one in every four risks in the Plan are assigned to SAIF. Previously SAIF's quota assignment was more representative of its market share (e.g., its quota in 1993 was 35.85%, and for 1994 it was 38.57%).<sup>8</sup> The 1996 quota will generate about \$11,000,000 in premiums for SAIF. At a servicing fee of 21%, this will produce about \$2,310,000 of revenue for SAIF.

c. How State Funds are Affected When the State Lacks an Assigned Risk Plan

Unfortunately, there is very little data and very few studies addressing the issue of how state funds are affected when the state lacks an ARP. Based on data for calendar year 1992 summarized in Table D.a.2-1, several facts are clear. Nine of the seventeen state-fund states in 1992 had no assigned risk pool. In addition, two of the eight state-fund states remaining, Maryland and Pennsylvania, had an ARP in 1992, but only for a small special segment of the workers' compensation market (for purposes of this discussion, these two states will be treated as if no ARP existed in 1992). In 1993, eleven of the seventeen competitive state-fund states did not have an ARP. Six assigned risk pools operated in the seventeen state fund states in 1994.

The state fund served as the market of last resort in ten states in 1992, in eleven states in 1993, and in twelve states in 1994. Because workers' compensation coverage is mandatory in virtually all states, if a state lacks an assigned risk plan, the state fund functions as the underwriter of last resort. It should also be noted that during 1993 both Rhode Island and Maine abolished assigned risk plans, and established state funds as markets of last resort. Texas established its Texas Workers' Compensation Insurance Fund as the insurer of last resort on January 1, 1994.

One financial measure which may provide information concerning the differences between state-fund states with and without ARP's is the combined ratio, defined as the sum of the loss ratio and expense ratio. The loss ratio is computed by dividing incurred losses, including loss adjustment expenses, by earned premium. The expense ratio is determined by dividing operating expenses by written premium. Hence the combined ratio provides information, albeit imperfect, about loss ratios and expense ratios, and also implicitly provides proxy information about rate adequacy. Combined ratios below a value of 100 percent are indicative of underwriting profits and rate adequacy, while values over 100 percent indicate that insurers are not earning enough premiums to cover losses and expenses.

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<sup>8</sup> NCCI Government, Consumer and Industry Affairs Director's June 26, 1996, advises of Oregon Licensing Servicing Carrier quotas.

Component data to compute aggregate combined ratios for categorized states was unavailable. Instead, a proxy measure for state aggregate combined ratios was developed by computing the premium weighted, state aggregate combined ratios<sup>9</sup>.

Table D.a.2-2 shows the results of premium weighted average combined ratios for various state aggregations. All of the premium weighted combined ratios exceeded 100 percent in 1991 and 1992, indicating that workers' compensation was an unprofitable line of insurance. The market has improved substantially since. Nevertheless, there are differences among the various state aggregations. For example, the premium weighted combined ratios for "non-ARP states," state-fund states where the fund operates as the market of last resort (including the states of Maryland and Pennsylvania), were 120.7% in 1991, and 121.1% in 1992. In 1993 the non-ARP states had a much improved combined ratio of 90.2% and in 1994 their ratio was 81.1%, indicating that premiums were easily covering both losses and profit. The corresponding ratios for state-fund states with an ARP (the state fund is not the market of last resort) were 114.6% in 1991, 107.5% in 1992, 104.8% in 1993, and 94.7% in 1994.

Oregon's combined ratios for 1991 through 1994 suggest rate adequacy, ranging from 84.3% to 98.4%. Only four states had combined ratios less than 100 percent in 1991, and of these only Oregon had a state-fund. Seven states were under 100% in 1992; only Louisiana and Oregon were state-fund states. In Louisiana the fund served as the market of last resort. By 1993, seventeen states had combined ratios under 100%, and thirty-one had adequate rates in 1994.

In summary, Oregon seems to be an anomaly when considering the results of insurance underwriting and the presence of a state fund. Only Oregon, which has an ARP, and state fund which does not serve as the market of last resort, has been able to achieve recently a combined ratio that suggests both rate adequacy and profitability for the market.

#### **H. Results of the Financial Examination of SAIF**

This section discusses the results of the recent financial examination of SAIF and also describes statutory accounting, various types of reserves, the differences in the way SAIF and private carriers discount loss reserves, and the effect of discounts on profit, capital and surplus.

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<sup>9</sup> This method of computing weighted combined ratios for various state aggregations is imperfect for a number of reasons. First, it would be best to compute the ratios using aggregated component data for each state for each year. Second, both the 1991 and 1992 combined ratios have not been computed by weighting with the corresponding 1991 and 1992 premiums; instead 1992 premiums were used as the weighting factors for both years because 1991 premiums were not readily available. Nevertheless, when one compares the premium weighted all states combined ratios for the two years to ratios computed by NCCI, the average error for the two years is around 2 percent, and year to year changes move in the proper direction.

a. Executive Summary of the Financial Examination

The entire written report of the recent financial examination of SAIF is attached as Appendix H. An executive summary of the examination findings is provided below.

- **FINANCIAL CONDITION:** No adjustments were made to the Company's December 31, 1995 financial statements as a result of this target financial examination. During the 2 year period since the last examination, assets have increased \$210,925,790 (now totaling \$2,117,052,335), liabilities have increased \$209,468,650 (now totaling \$1,687,124,647, and surplus has increased \$1,457,650 (now totaling \$429,927,688).
- **DIVIDENDS TO POLICYHOLDERS:** No instances were found in which the declaration and allocation of policyholder dividends were discriminatory as to risk size, risk location, and industry type. Management decisions in determining the level of total dividend distributions appeared to be reasonable and appropriate.
- **LOSS EXPERIENCE:** Loss ratios have fluctuated dramatically from 1988 through 1995 primarily due to changes in the basis and assumed rate of discount.
- **LIMITATIONS OF THE STATUTORY REGULATION OF SAIF:** SAIF is not subject to many Insurance Code requirements to which other similar insurers are subject. The biggest difference affecting underwriting results and financial condition between SAIF and the remainder of the Oregon insurance industry is SAIF's ability to discount its loss reserves. However, the magnitude of the amount of discount utilized has diminished each year since it was initiated. As a percentage of the amount that would have been required for all other workers' compensation carriers, SAIF's total reported loss reserves have increased from 69.7% in 1989 to 95.7% in 1995.
- **OTHER REQUIREMENTS APPLICABLE TO SAIF:** SAIF is subject to several requirements that do not apply to insurers and these requirements are detailed in the financial examination report.
- **RESERVES FOR LOSSES AND LOSS ADJUSTMENT EXPENSES:** Total reserves for losses and loss adjustment expenses, as of December 31, 1995, were estimated to be near the upper end of the range of reasonable actuarial estimates. No reduction is recommended due to the high level of uncertainty regarding their ultimate value.
- **RATING PLANS:** Risks are generally distributed among the various rating tiers using objective criteria. However, it was noted that small risks tend to end up in higher rating tiers while large risks end up in lower rating tiers. Two files (4% of those reviewed) contained insufficient documentation to determine if they were in the appropriate rating tier.
- **DEFERRED PREMIUM:** No exceptions were noted in which certain employers were given favorable treatment with respect to payment terms.

## b. Loss Reserves

### 1. Definition of Loss Reserves

"Loss reserves" means the liability of an insurance company for unpaid insurance claims. A workers' compensation insurer must recognize losses as incurred for occupational injuries or diseases that have occurred to-date, including all associated costs of future medical treatment, compensation benefits, and rehabilitation which might not be payable for several years. In insurance accounting, "reserve" means a liability while in general accounting a "reserve" usually means a segregated portion of capital and surplus.

### 2. The Purpose of Statutory Accounting

Loss reserves are calculated and reported in different ways for different purposes. Reports of the claims experience of a particular employer will include insurance company estimates of unpaid claims relating to an insurance policy of that employer. The financial statement of the same insurance company, however, must include its estimate of the ultimate cost of all claims, including those that have not yet even been reported to it. Insurance companies might prepare three financial statements. One is a general accounting statement for the SEC, shareholders, and prospective investors which is meant to describe the operating profitability of the company and other important information for investment decisions. Another statement is required for the IRS following tax laws for allowed expenses and for discounting loss reserves according to prescribed payment patterns and discount rates. The third statement (which might be the only financial report for a non-publicly-traded, tax-exempt insurer) is the statutory report required by insurance regulators.

The purpose of the statutory financial statement is to demonstrate the ability of the insurer to fulfill its contractual obligations to policyholders. The treatment of assets, liabilities, expenses, and income are generally more conservative than for the other types of reports. These loss reserves could only be considered "unnecessarily high" when examined for a different purpose. For instance, when determining future premium rates, loss reserves might be discounted to allow for the opportunity to invest corresponding premium income. Even for pricing, however, loss reserves are more often left undiscounted and a separate counter provision is included for investment income.

### 3. Distinction Between Tabular and Non-Tabular Reserves

A "tabular" reserve is one that can literally be looked up in a table. That is, when DCBS determines that a worker has become permanently and totally disabled and the insurer begins paying a lifetime pension or when a worker is fatally injured and the company begins pension payments to a widow, then the case has reached some finality. The future payments are completely determined except for such factors as mortality, remarriage, and escalation for cost of living adjustments. These factors are predictable enough that present values of future payments are published in actuarial tables. So, case reserve estimates for cases that have definitely reached fatal or permanent total disability (PTD) status are examples of tabular reserves.

All other reserve estimates must be "non-tabular." That is, one cannot determine the value of the reserves just by looking in a table. These other reserve values have varying degrees of unpredictability but for every case there is unresolved contingency. Each year, for instance, some cases that appeared to be straightforward temporary disability injuries emerge into permanent total disability cases. There is also every other possible status change. Temporary disability cases may receive permanent partial disability awards. A PTD claimant recovers sufficiently to find gainful employment. Injuries for closed cases become aggravated. Claimants that were totally unknown suddenly appear with permanent disabilities. The numbers of cases that will change status in these ways -- and which ones in particular -- are highly uncertain. Medical expense reserves and loss adjustment expense reserves are never tabular.

The distinction becomes important when we consider the extent to which DCBS can allow an insurer to discount loss reserves. The basic understanding is that an insurer can conservatively discount tabular reserves since they have a reasonable degree of predictability. The uncertainties in non-tabular reserves, however, outweigh the arguments for reporting discounted present values.

#### 4. Differences in the Way SAIF and Private Carriers Discount Loss Reserves

To reiterate, the purpose of the statutory financial statement is to demonstrate the ability of the insurer to fulfill its contractual obligations to policyholders. Future investment income is not assumed. The possible need to reinsure or to pay another insurer to assume the claim obligations allows no general assumption that reserves may be discounted. As regulator, DCBS normally permits insurers to discount only future wage loss compensation payments for cases known to have reached determination as fatal or permanent total disability cases. Future payments for those cases have then been determined except for duration, which is decided by mortality and remarriage factors. Since these factors are reasonably predictable, annuity or pension tables can be used. Hence, these are considered "tabular" reserves. For decades, the discount rate permitted has been 3.5 percent, allowing for no investment risk. DCBS does not normally allow any discounting of medical costs or loss adjustment expenses.

Original wording for ORS 656.636 suggested the same conservative discounting standards for SAIF. With the current wording, including mandated recognition of interest income, and an Attorney General opinion (OP#6176), the SAIF Board of Directors can adopt more liberal discounting assumptions. From 1988 through 1991, SAIF discounted all indemnity reserves at 7 percent and all medical costs at 3.5 percent. SAIF did not discount medical costs in 1992, but continued discounting all indemnity at 7 percent. Beginning in 1993, SAIF has been discounting all projected indemnity payments for fatal and permanent total disability cases at 4 percent and not discounting other indemnity or medical costs. Since these fatal and PTD payments are not restricted to cases which have reached final determination, this model remains more liberal than allowed for other insurers. On its own volition, until the end of 1995, SAIF also discounted corresponding portions of its loss adjustment expense reserves.

The December 1995 annual statement for SAIF shows \$154,337,000 discount of losses and \$0 discount of loss adjustment expenses. SAIF has estimated that the 1995 change in discounting

loss adjustment expenses increased its expense reserves by \$23,135,500. SAIF has advised DCBS that the stricter tabular discount of losses would only be approximately \$98.6 million. Hence, the difference would be about \$55.7 million. This difference between SAIF discounting and tabular discounting is much smaller than it once was. Prior to 1992, the difference exceeded \$300 million.

## 5. The Effect of Discounting on Profit, Capital and Surplus

"Losses incurred" is the major deduction from earned revenue in an insurer income statement. The accounting definition of losses incurred is losses paid during the year plus the change in losses unpaid (reserves) since the previous year end. Discounting reduces losses unpaid at both year ends, hence, it usually reduces the change in unpaid losses and increases net income. Capital and surplus, together considered "policyholders' surplus" in the statutory statement, is directly increased by the discount of current reserves. An increased surplus enables an insurer to take any number of actions including building the business, decreasing rates, and increasing dividends to policyholders.

If workers' compensation insurance becomes unprofitable in Oregon sometime in the future, SAIF management might again decide to discount loss reserves more liberally. Other parties might then request further legislative resolution or legal interpretation, but this does not appear urgent at the moment.

## I. Results of the Market Conduct Examination and Other Related Market Issues

Section I describes the results of the recent market conduct examination of SAIF and other related market issues including SAIF's dividend policy and the effect on the market, SAIF's investment income policy, underwriting and claims management practices, and SAIF's loss control efforts.

### a. Executive Summary of the Market Conduct Examination

The entire written report of the market conduct examination is attached as Appendix I.a.. An executive summary of the examination findings is provided below.

- **UNDERWRITING:** Policy files were reviewed on a random sample basis and subjected to nine different tests to determine compliance with Oregon laws and administrative rules, and proper treatment of policyholders. This included such areas as unfair discrimination, classification of occupations and rate levels, remittance of premium in accordance with contractual provisions, cancellation notices, disclosure, and file documentation. Compliance was found to be 100% on 7 tests, 99% on 1 test, and not in compliance on the remaining test. Companies are required to disclose the appeal process at or before policy issuance and SAIF made the disclosure at the time it later conducts the premium audit.
- **AGENT LICENSING/APPOINTMENTS:** Agents' records were reviewed on a random sample basis and reviewed for compliance with the various related Oregon laws and

administrative rules. Compliance was found in all respects except relating to the required provisions for notice of termination.

- **PREMIUM AUDIT:** Workers' compensation insurers are required to conduct an annual premium audit on each policy with an annual earned premium of \$10,000 or more. SAIF conducted such audits on only 29.5% of these policies in 1994 and 38.8% in 1995. The Company was in compliance with the remaining tests that were applied.
- **UNIT STATISTICAL DATA:** With the exception of system generated errors, the Company's unit statistical program appears to be operating with minimal errors. No recommendations are warranted at this time.

**b. SAIF's Dividend Policy**

Dividends had not been a substantial factor in the Oregon market since the advent of competitive rating in 1982, but have become more common since the 1990 reforms. Workers' compensation insurance has been profitable in Oregon this decade. Claim costs may have decreased more than could be objectively anticipated in 1990. Also, most insurers are conservative with investment income considerations in pricing. SAIF, and other insurers to some extent, have been returning these unexpected profits and investment income margins to policyholders as dividends to enhance their competitive image. Insurers are prohibited by Oregon law to promise any dividends, but are allowed to display historic dividend information. OAR 746.150(2).

SAIF dividends to policyholders by year from 1990 to 1996 are as follows<sup>10</sup>:

**DIVIDENDS TO POLICYHOLDERS**

<u>Year</u>	<u>Dividends</u>
1996	\$50,000,000 (est.) <sup>11</sup>
1995 <sup>12</sup>	\$80,188,951
1994	\$29,666,666
1993	\$32,672,940
1992	\$22,583,870
1991	\$17,728,354
1990	\$20,429,887

The examination of SAIF by Richard E. Sherman & Associates concluded with these observations:

1. SAIF does consider its surplus needs for various asset, liability, and investment risks before deciding how much to declare in dividends each year.

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<sup>10</sup> Source: SAIF annual statements.

<sup>11</sup> This dividend was declared at the April, 1996 SAIF Board of Directors meeting. Source: SAIF CORPORATION **Compnews**, June 1996.

<sup>12</sup> \$50 million of the \$80 million was a supplement dividend for coverage occurring between mid 1990 to 1994. Source: SAIF CORPORATION **Compnews**, June 1996.



2. SAIF dividend payments comply with Oregon law, specifically OAR 836-80-140.
3. SAIF dividend policies have recognized both premium size and profitability by product line (guaranteed cost, retrospective rating, various group plans, etc.) in order to satisfy various considerations regarding policyholder contribution to surplus. The result has been larger dividends to smaller accounts than would have been paid if SAIF had based dividends solely on premium size.
4. Although SAIF dividend plans should not be considered unfairly discriminatory, SAIF could possibly refine its dividend plans to place more emphasis on underwriting results by product line and perhaps use net premium as a basis rather than standard premium. (One apparent anomaly identified is that dividends for retrospectively rated policies based on standard premium may in some instances exceed the basic or fixed portion of final net premium.)

c. SAIF's Use of Investment Income

Three factors determine the impact of investment income in pricing:

- After-tax yield on invested assets
- Relative volume of invested assets and premiums
- Corporate profitability or surplus growth requirements

The attached Table I.c.-1 provides a summary of SAIF's investment income and total investment yield, and the corresponding yields for selected private insurers. The investment yields are computed according to profitability formulas used by the NAIC. Notice that SAIF's yields in the subject periods exceed the yields achieved by the private insurers in most instances. Table I.c.-2 shows a historic distribution of cash and invested assets for SAIF and the selected private insurers. A review of Table I.c.-2 and the insurers' annual statements suggests, in part, that SAIF's investment yields are somewhat higher because, unlike private insurers, SAIF does not invest in bonds exempt from U.S. taxes. However, a review of Table I.c.-2 also illustrates that there are significant differences in the distribution of cash and invested assets among the companies displayed over the historic period, and these differences in combination with the varying success in selecting individual investment instruments all come into play in explaining the differences in investment income and total investment yields achieved.

The difference in yield on invested assets for SAIF over the other selected insurers typically amounted to about two percentage points from 1993 through 1995. Because the investment earning figures taken from insurers' financial statements are pre-tax, the actual after-tax difference would be somewhat greater.

Most commercial insurers have invested assets amounting to some multiple of premiums. Because claims can take several years to resolve, these insurers must maintain assets to assure future payment of obligations incurred over several past years. Table I.c.-3 shows the comparison of invested assets with net premiums earned for SAIF and the other selected insurers. The ratios are considerably higher for SAIF than for the others. In comparison with Grocers and

Liberty Northwest, the difference is the longevity of SAIF. But the comparison is equally dramatic for the other two companies. Employers of Wausau, in particular, primarily insures workers' compensation and has existed since 1911. Growth patterns during the intervening decades may explain some of the difference. Also, Oregon experienced much higher frequencies of permanent total disabilities and other serious injury awards than other states through the late 1970s. Oregon premium rates were among the highest in the nation into the early 1980s. The influence of these factors on SAIF's investment leverage should diminish over the next few decades.

Finally, there is a definite difference in the profitability and growth requirements as determined by the management of each insurer. Most insurers will determine a total profitability goal -- usually as a return on surplus or net worth -- and translate that into an underwriting margin on premiums and then subtract an allowance for investment income. The total profitability goal will depend on corporate capital structure. These internal financial operating goals are not clearly stated in any regular reports but we can sometimes discern them from rate filings.

The most recent available information for SAIF and other selected insurers from rate filings shows these net provisions for profit and contingencies after offset for investment income:

Company	Net Profit & Contingencies Provision	Source
Employers Ins of Wausau	-3.7 %	Rate filing for 1/1/96
National Union Fire of PA	-3.5 %	Rate filing for 1/1/96
Grocers Insurance	-10.46%	Rate filing for 1/1/94
Liberty Northwest	-10.7 %	Rate filing for 10/1/94
SAIF	-30.0 %	Rate filing for 1/1/94

The examination of SAIF by Richard E. Sherman & Associates found that for 1994 and 1995, SAIF's pricing offsets for investment income exceeded anticipated investment income from prospective premium, claims, and expense flows by between 12 and 14 percent of earned premium. This "excess" has been funded by investment income on invested assets representing surplus. Although SAIF does not need profits to satisfy investors, it might still need to project long-term growth necessary to continue servicing a comparable share of the Oregon market in the future. SAIF has allocated all investment income to offsetting premiums for current policyholders, other than a portion needed for accrual of loss reserve discounts. The other insurers usually set profitability goals that translate to positive profit and contingency margins prior to investment income offsets. The rate filings referenced above show a 2.4 percent margin for Employers Insurance of Wausau prior to investment income offset, 2.5 percent for National Union Fire, and 0.3 percent for Liberty Northwest.

#### d. SAIF's Underwriting Practices

SAIF's pricing plans are described in earlier sections of this report, particularly sections D.b.3 and D.b.4. SAIF management, and underwriters for many other insurers, often believe that larger employers tend to have better claims experience and lower servicing costs. Underwriters also

consider many other factors, but generally they will compete more aggressively for larger accounts. Smaller employers often go many years without serious injury claims, so tend to disbelieve that large employers can be less costly to insure. This difference in perspective may be the basis of most cross-subsidy allegations.

DCBS has undertaken factual investigation of these allegations. The report of the recent financial and market conduct examination describes the findings of this investigation. The examination by Richard E. Sherman & Associates found that since 1990 SAIF has tended to place small employers in higher rate "tiers" while assigning larger employers to lower ones. (This is a standard insurer practice and is not by itself evidence of unfair discrimination.) Sherman also found some suggestion that premium discounts, retrospective rating, and other premium adjustments tended to change net premium loss ratios away from the average ratios more for large accounts than for small ones.

It was initially found that eight accounts were not in the appropriate rate tier for which there was insufficient evidence to justify the underwriter's decision. SAIF provided additional documentation that showed six of these files to be in the proper rate tier. Of the two remaining files, there was no documentation to show whether one account was still entitled to group rating and the underwriting decision to keep the other account in the 1.15 rate tier when it appeared to be eligible only for the 1.30 rate tier was not documented. These two files represent 4% of the selected audit sample. Therefore, 96% of the accounts passed the audit criteria. The timing of the Sherman investigation in conjunction with the seasonal workload around the four major policy renewal dates -- the first of each quarter -- incurred by SAIF, may be a contributing factor for this lack of file documentation. DCBS does not consider this as evidence of arbitrary or undisciplined pricing.

e. SAIF's Claims Management Practices

All self-insurers and workers' compensation insurers, including SAIF, must process claims and pay benefits in accordance with statute, administrative rules and case law. Workers and insurers have remedies before the Workers' Compensation Board and the director when either wishes to contest a matter relating to responsibility, compensability, medical treatment, vocational assistance and other matters.

The WCD Compliance Audit results and the percentage of denied claims appealed are the best indicators of SAIF claims management practices. Recent audit results and denial appeal rates are briefly discussed below.

- (1) WCD statistics from the Quarterly Claims Processing Performance system in four key timeliness categories indicate slightly higher performance by SAIF than other insurers as a whole. While timeliness for other insurers declined from 1994 to 1995 in three of four reported categories, SAIF's performance rose in two of four categories, fell in one and was unchanged in another. SAIF achieved 1995 timeliness of 87 percent or higher in all categories.

- (2) Since 1989, SAIF has denied a higher proportion of its claims than other insurers as a whole. This has not translated into consistently higher appeal rates, however. Denial appeal rates for SAIF, other insurers, and self-insurers have been comparable over the last five years (see exhibit I.e.1), with SAIF having a slightly lower appeal rate on 1994 and 1995 denials. These findings are based on periodic statistics produced by the DCBS Information Management Division which reflect the status of "originally denied" disabling claims. It should be noted that these statistics are based only on the existence of a hearing request (i.e., appeal) following the denial, and does not indicate the outcome of the case.

In addition, SAIF has a claims management philosophy embodied by the following quotation excerpted from a SAIF publication entitled Understanding SAIF Corporation.

"All claims employees strive to provide superior customer service by consulting with employers and by establishing rapport and trust relationships with workers and providers. Claims employees best serve SAIF and its customers when they reduce uncertainty by investigating questionable claims, promptly paying compensable claims, and communicating information to employers and their workers about issues that affect their interests."

f. SAIF's Loss Control Efforts

Oregon OSHA began auditing insurers in Oregon in 1989. The audits are conducted to determine if an insurer is providing loss control services to its insureds, and the adequacy of that service. The insurer is required by statute to provide loss control assistance at the request of the insured. In addition, Oregon OSHA identifies insureds with a high workers' compensation claims rate and notifies the insurer to provide mandatory loss control services within 90 days of notice.

All insurers, including SAIF, are audited to determine if loss control services are being offered and if services are timely and adequate. From 1990 through October 1995, OR-OSHA conducted 264 insurer audits and 99 self-insured audits issuing 348 violations, with aggregate penalties over \$200,000. Since 1990, SAIF has received three routine audits and two complaint generated audits resulting in two citations for violations of the OR-OSHA Administrative Rules, with a combined penalty of \$3,850. Citations and penalty amounts are comparable with other insurers and self-insureds. The average penalty amount for a violation is \$575 while SAIF's average penalty amounted to \$550.

SAIF's Risk Management Division has made an effort over the past two years to try innovative ways of improving loss control assistance to insureds. It has sent several proposals for OR-OSHA's review in an effort to improve upon its loss control plan. Very few insurers other than SAIF have proposed alternate loss control plans or met with OR-OSHA to discuss areas of potential improvement.

Over the years, some employers have suggested that SAIF and other large insurers do not provide loss control assistance to low premium insureds. The validity of this concern has not been established for SAIF or any other insurer. During inspections conducted by safety and health compliance officers, OR-OSHA does ask employers if their workers' compensation insurer is providing assistance. If not, they are encouraged to file a complaint. OR-OSHA has seen only seven complaints filed since 1989; two of these were filed against SAIF, a relatively small number given SAIF's substantial market share of Oregon's employers during the subject period.

Overall, OR-OSHA finds SAIF's loss control efforts comparable to the market and, in some areas, ahead of the market.

#### **J. Results of the Secretary of State Audit of SAIF**

Annually, the Secretary of State, Audits Division, conducts an audit of the SAIF Corporation. The purpose of the audit is to determine whether there is reasonable assurance that the Corporation's financial statements are free of material misstatement, to review the internal control structures, and to assess compliance with laws and regulations pertinent to Government Auditing Standards.

The entire written audit report for the period ending December 31, 1995, is attached as Appendix J. The audit results are consistent with the Department of Consumer and Business Services financial examination for the same subject period and which has already been summarized in Section H of this report. The Secretary of State audit concluded that the SAIF Corporation financial statements for the year ended December 31, 1995, were fairly presented. Significant details about the SAIF Corporation financial statements, accounting policies and other operational considerations are provided in the audit report.

It should be noted that the Secretary of State audit is conducted using generally accepted accounting principles while the Insurance Division financial audit uses statutory accounting principles. Generally accepted accounting principles differ in certain respects from the statutory accounting principles which are prescribed by insurance regulatory authorities. Hence, some quantitative findings of the audits conducted by the Secretary of State and DCBS may differ.

#### **K. State Attorney General Involvement With SAIF**

This section describes the State Attorney General's client relationship with SAIF and also briefly discusses some pertinent recent opinions.

##### **a. Description of the Client Relationship**

Under ORS Chapter 180, the Oregon Attorney General is counsel for executive branch agencies. SAIF is a part of the executive branch of state government. 46 Att'y Gen. 323 (1990). The Oregon Supreme Court has held that SAIF Corporation is among the entities required to use the Attorney General's services unless the Attorney General determines there is a conflict of interest and that it is appropriate and in the public interest to allow separate counsel. FROHNMAYER et

al v. STATE ACCIDENT INSURANCE FUND CORPORATION, 294 Or 570 (1983). Thus, the Oregon Attorney General represents both SAIF and the Department of Consumer and Business Services.

This role of dual counsel is proper as set forth in "THE ROLE OF THE DEPARTMENT OF JUSTICE" by James M. Mattis, Attorney Coordinator, Oregon DOJ, and Michael V. Reed, Assistant Attorney General, Oregon DOJ, STATE ADMINISTRATIVE LAW (Oregon CLE 1985). The treatise points out that the Oregon Attorney General, as chief legal office of the State and as part of the executive branch of Oregon government, has but one client, the State of Oregon. While the Attorney General represents individual agencies, he has an overriding duty to protect the interests of the State and public. The Attorney General is empowered to formulate and advance a consistent legal position on behalf of the State. Individual state agencies are precluded from fragmenting the State's legal policy by taking legal positions adverse to those developed by the Attorney General. Such integrated legal services ensures consistency in the legal policy advanced by the State. In short, as The Oregon Supreme Court stated, "all of the state's legal affairs...remain under the charge, control and supervision of the Department of Justice." Frohnmayer, *supra*, 557-578.

The agency, nonetheless, retains some discretion. It has the right of reasonable approval over assigned counsel, and the right under ORS 180.060(8) to forbid the Attorney General's appearance. It may employ its own general or special counsel, but only if the Attorney General authorizes it to do so under ORS 180.235(1). (See Letter of Advice to LeRoy Livermore, SAIF Corporation (May 12, 1983) (OP-5512) for the Attorney General's views on how and when ORS 180.235 is applicable.)

Finally, the Attorney General's charge is to represent the State -- to consider always the broader public interest. It succinctly states, "When the 'public interest' conflicts with an agency's desires in a particular situation, the Attorney General's higher duty is to the public interest. For example, the Attorney General will decline to assert a legal contention in court on behalf of a state agency if the Attorney General believes the contention has no legal merit. (See Letter of Advice to LeRoy Livermore, SAIF Corporation (May 12, 1983)(OP-5512).)"

Problems arise when the Director must resolve conflicts about the legal interpretation of specific statutes between SAIF and the Department. For example, conflict of law disputes have arisen over jurisdictional authority of the Insurance Code and the Workers' Compensation Law, ratemaking, and financial reserving issues. The conflicts can occur when SAIF's assistant attorney general has a different legal interpretation than the DCBS's assistant attorney general. When this occurs, the only way for a dispute to be resolved is to involve a higher ranking member of the Attorney General's Office to determine the legal interpretation that will prevail. Problems can also arise when the Director requires legal counsel from the Department of Justice to resolve conflicts between SAIF and another party when SAIF has already enlisted assistance from the Department of Justice regarding interpretation of the Insurance Code.

b. Discussion of Pertinent Recent Opinions

The following list summarizes some recent Oregon Attorney General opinions and letters of advice dealing with SAIF-related regulatory issues.

<u>Date</u>	<u>Topic</u>
2/27/86	SAIF of Oregon. State law authorizes SAIF to form and own a wholly owned subsidiary. OP-5931.
3/13/86	SAIF of Oregon. SAIF may not hold recoverable deposits for its wholly-owned subsidiary, SAIF Corporation of Oregon, nor provide a deposit on its own behalf to indemnify that subsidiary. As a domestic insurer, SAIF Corporation of Oregon must comply with the applicable provisions of the Insurance Code. OP-5830.
12/31/86	SAIF's reserves. Notwithstanding the Insurance Code (ORS 737.030), SAIF need not reserve the total amount of a permanent partial disability award, but can reserve that amount of money which, when combined with the interest it will earn, will equal the amount that must be paid out on an award. SAIF may not, however, in keeping with the Insurance Code, discount total disability benefits. OP-6020.
5/25/88	SAIF's reserves. The legislature has not specified the extent to which SAIF may discount its discretionary reserves. Thus, SAIF may reserve whatever amount it judges necessary. There is no statutory limit on the use of a discount rate, and SAIF is not subject to the same reserving requirements as private insurers. In addition, SAIF has special responsibilities as an instrumentality of the State of Oregon. Hence, the director's regulatory authority over SAIF reserves is limited. If the director finds the reserves insufficient, the director can require they be increased; however, the director cannot require that reserves be computed according to a certain formula. OP-6171.
4/9/90	SAIF's legal entity and government relationship. SAIF is an instrumentality of the state, organized to function through a corporate structure. It is governed by a board of directors, appointed by the governor. These directors establish policies to operate SAIF.  SAIF is part of the executive branch of state government, although as an independent public corporation the Legislative Assembly delegated policymaking responsibility to SAIF's board of directors and released the company from almost all aspects of legislative oversight. The legislature, however, can change its current relationship by changing the statutes that define SAIF.

Under Oregon's "three-way" workers' compensation system, private insurance carriers can compete with SAIF. At the same time, there are no restrictions on SAIF's legal authority to compete with private insurers.

SAIF is "owned" by the citizens of Oregon. Nearly all of SAIF's assets and liabilities are accounted for by the state as part of the Industrial Accident Fund (IAF). IAF is a separate entity from SAIF and not an asset of the corporation. Thus, the citizens do not necessarily own a marketable asset. OP-8212.

- 9/5/90 SAIF's reinsurance. SAIF has statutory authority to purchase reinsurance from an insurer admitted in Oregon or approved by DIF's director. OP-6392.
- 5/17/91 SAIF financial statements. DIF's director, rather than the secretary of state, has authority to instruct an insurer -- including SAIF -- to correct a previously filed statement. Unnumbered letter of advice, Jack L. Landau, deputy attorney general.
- 7/1/91 SAIF reinsurance. In this letter, DOJ stated that SAIF's reinsurance contract with a certain insurer constitutes a trade secret for purposes of ORS 192.501(2). Unnumbered letter of advice to Stanton F. Long.
- 2/5/92 Workers' compensation claims processing. Materials in this file include DOJ counsel to DIF on a number of questions regarding the obligations of workers' compensation insurers in processing claims, and on the role of the Workers' Compensation Division. Some questions specifically dealt with SAIF claims. DOJ file number 440-200-BA044-92.
- 3/19/92 SAIF reporting. While SAIF is not required by law to issue GAAP (generally accepted accounting principles) financial statements, the DIF's director could impose such a requirement under ORS 731.488. OP-6445.
- 4/24/92 SAIF's debts. No entity, including the State of Oregon, would be liable for the SAIF's debts if the Industrial Accident Fund became insolvent. OP-6418.
- 6/17/92 SAIF challenges DIF affirmation letter. This letter upheld DIF's authority to require insurers, and particularly SAIF, to submit a management affirmation letter, signed by the company chairperson, in connection with the insurer's regular biennial examination by the Insurance Division. The letter also recommended that DIF adopt rules on this requirement before enforcing it. Letter of Advice, Donald C. Arnold, chief general counsel division, DOJ.
- 6/26/92 SAIF challenges DIF OAR. Opinion validates the Department of Insurance and Finance's (DIF's) OAR 436-60-055(3) regarding the \$500 medical deductible and third party lien rights. OP-6191.



- 10/20/92 SAIF's contractual powers. SAIF has statutory power to contract out administration of its medical audit and provider reimbursement process for claims covered under one of its policies. OP-6468.
- 6/1/93 Reimbursement request for SAIF's board of directors. Relying on the statutory provision that reimbursable expenses must be "incurred in the performance of official duties," this opinion denies a request for reimbursement of SAIF's board members. OP-6489 (p.3).
- 6/3/93 Creation of corporations by special laws. SAIF is not the type of corporation referred to in Article XI of the Oregon Constitution, which prohibits creation of corporations by special laws. The AG's opinion on this cites *State ex re Eckles v. Wooley*, 302 OR 37, 726 p2d 918 (1986). OP-6478 (p.4) etc.
- 8/4/94 1994's Measure 5. This measure would not affect SAIF premiums, because premiums are monopolized by government and reflect individual adverse or favorable experience. OP-8229 (p.35)

#### **L. Non-Complying Employer Claims Processing**

Employers that are required to comply with Oregon workers' compensation laws but fail to do so are referred to as non-complying employers or NCE's. When claims arise from an NCE, the Director has the authority by virtue of ORS 656.054 to direct SAIF or an assigned claims processing agent to service the claim. Prior to 1995, SAIF was mandated by statute to function as the exclusive NCE servicing carrier. The 1995 amendments to ORS 656.054 gave the Director authority to appoint either SAIF or other carriers, if they expressed an interest, as NCE assigned claims agents. Since the effective date of the 1995 law amendments, SAIF remains the sole NCE assigned claims agent.

SAIF's NCE servicing carrier fee is recalculated annually with the new fee effective for the following fiscal year, July to June. The rate is determined by dividing the previous calendar year's direct paid loss adjustment expenses by the previous calendar year's direct paid losses. SAIF's figures are reviewed by the Department's actuary and the Director before a final decision is made. The current servicing carrier fee is 19.7 percent of direct paid losses.

#### **M. State Employee Captive Account**

State agencies are required under ORS 656.017(2) to provide workers' compensation coverage of state employees through SAIF. The Risk Management Division of the Department of Administrative Services (DAS) negotiates rates with SAIF and allocates the cost to each agency according to claims experience.

If the Legislative Assembly allowed state agencies to provide insurance through other insurers, the likely alternative would be self-insurance, perhaps with SAIF or another insurer providing

claims management services. The current pricing arrangement with SAIF is very close to a self-insurance arrangement.

SAIF renews the policy for state agencies effective July 1 each year. The estimated standard premium for the current year beginning July 1, 1996 is approximately \$35 million. SAIF actuaries determine an aggregate premium rate. The rate for the current year is \$1.78 per \$100 of payroll. Since state agencies have their own statistical classification, there is no experience rating.

The policy for July 1, 1996, through June 30, 1997, is a "paid loss" retrospectively rated policy. The basic premium factor, or fixed cost, is four percent of standard premium. The state will pay SAIF for actual claims costs paid each quarter plus 6.2 percent for claims administration expense. The maximum retrospective premium will be 200 percent of the standard premium. DAS will continue to pay SAIF periodically for the cost of claims incurred during this policy for ten years after it expires. At the end of that period, DAS will pay SAIF the remaining retrospective premium for unpaid losses.

Oregon Health Sciences University became a "public" corporation in 1995 and was then able to obtain workers' compensation insurance in the competitive market. Because OHSU had always been covered through SAIF under the DAS arrangement, there was no separate payroll and claims experience available to private insurers for pricing evaluation. SAIF explained that OHSU was unable to assign payroll to classifications or to recognize the required exclusions, such as vacations or bonuses. For this reason, DCBS guided SAIF and NCCI through properly establishing a special classification for OHSU. The same statistical data problems would prevent private insurers from competing for other state agencies if they were legally allowed to do so.

#### **N. Taxation of SAIF and Private Insurers.**

There are a number of important issues that arise with respect to the taxation of SAIF and private insurers generally. These issues are briefly discussed below.

##### **a. Tax Subjectivity of SAIF and Private Insurers**

SAIF pays the following taxes: (1) payroll taxes comprised of FICA taxes including Social Security, Oregon Unemployment Compensation, and the Tri-Met Tax for Portland based employees; (2) local ad valorem property taxes; (3) federal assessments on longshore and harbor workers premium; (4) WCD assessments and contributions, including the cents per hour tax; and (5) the WCD administrative assessment on Workers' Compensation (WC) direct earned premium. SAIF is exempt from state corporate excise taxes, the Gross Premium tax, the Fire Marshal tax, and Federal Income taxes.

Private property and casualty insurers pay all of the taxes SAIF is obligated to pay, and in addition pay Federal Income taxes (at an unadjusted rate of 34 percent prior to 1994 and 35 percent thereafter) and either the Gross Premium tax or the state corporate excise tax. Foreign insurers are subject to the Gross Premium tax (ORS 731.816), at a rate of 2.25 percent of

premiums received with a credit offset for workers' compensation assessments paid (ORS 731.832). Domestic insurers are subject to the state corporate excise tax amounting to a rate of 6.6 percent on taxable income in accordance with ORS 317.655, which does not permit an offset for workers' compensation assessments.

House Bill 2855, passed in 1995, provides that, beginning in 1997, foreign insurers will pay the state corporate excise tax, and the Gross Premium tax will be phased out over a five-year period. Foreign insurers will continue to be subject to a "retaliatory tax" (ORS 731.854) that guarantees that a foreign insurer's total taxes paid to Oregon will be at least as much as its home state would require an Oregon insurer to pay to do the same amount of business in that state. Both foreign and domestic insurers also pay a gross premium tax on pertinent fire insurance premiums, also known as the Fire Marshal tax, at a rate of one percent, according to ORS 731.820.

The attached Table N.a.-1 displays a summary of financial operations data for the SAIF Corporation and four selected private insurers. The three highest premium volume private workers' compensation underwriters in Oregon are Liberty Northwest Insurance Corporation, National Union Fire Insurance of Pittsburgh, and Employers Insurance of Wausau. All three companies are taxed as foreign insurers, and are not subject to the corporate excise tax. Oregon only has two domestic property and casualty insurers that underwrite workers' compensation coverage; the largest domestic underwriter is Grocers Insurance Company, formerly named United Employers Insurance. Data in Table N.a.-1 is reported on a consolidated basis according to information provided in annual statements filed with the Oregon Insurance Commissioner. Notice that there is no simple relationship between federal income taxes and net income. This fact arises from, among other things, differences in book and tax timing recognition, the ability to use tax loss carry-forwards accumulated in prior years, and changes in loss reserves. Hence, while Employers Insurance of Wausau earned net income of more than \$76 million in 1993, the insurer qualified for a tax credit of over \$5.5 million; the insurers also qualified for a credit in 1995. Notice that Grocers Insurance in 1993 and National Union Fire in 1994 had positive net income and yet qualified for tax credits as well. In addition, for Liberty Northwest, the federal and foreign income taxes as a percentage of net income were substantially different for the three years displayed. Finally, National Union Fire Insurance of Pittsburgh paid a federal and foreign income tax rate of 28.8 percent in 1993. These are just a few examples that illustrate the complexity of the relationship between taxes and income.

It should also be noted that for foreign insurers, the WCD Administrative assessment will amount to a total offset to the gross premium taxes due on Oregon workers' compensation direct written premium. The WCD Administrative assessment is currently set at 4.5 percent of earned premium, far exceeding the 2.25 percent gross premium tax rate. Table N.a.-2 demonstrates the result of applying the WCD Administrative assessment offset to Liberty Northwest's gross premium tax obligation; the net result is that no gross premium taxes were paid in 1992 and 1993 on Oregon workers' compensation premiums written.

b. Estimated SAIF Tax Obligations if Subject to Tax

If SAIF paid the same taxes as private insurers, what would its tax obligation be? In order to answer this question numerous assumptions must be made. For the purposes of this analysis we assume no change in SAIF's investment asset mix, book of business, loss reserving practices, or any other operations reflected in SAIF's annual financial statements. For computing SAIF's estimated corporate excise taxes for 1992 through 1995, a method essentially consistent with the provisions of ORS 317.655 was employed. The corporate excise taxes that SAIF would have paid are estimated at \$17,973,556 for 1992; \$7,426,954 for 1993; \$5,289,291 for 1994; and \$22,173 for 1995 (see Tables N.b.-1 and N.b.-2).

To compute SAIF's estimated federal income tax liability for the four subject years, a method consistent with National Association of Insurance Commissioners (NAIC) formulas was employed (see "Report on Profitability by Line by State 1994," NAIC, October 1995 and corresponding publications for 1992 and 1993). SAIF's estimated federal tax liabilities would have amounted to \$86,103,202 for 1992; \$35,033,549 for 1993; \$24,956,077 for 1994; and -\$1,166,758 for 1995 (see Tables N.b.-1 and N.b.-2).

It is important to note, however, that we cannot accurately compare SAIF's estimated taxes with the tax obligations of the insurers displayed in Table N.a.-1. This is because the analysis is static for SAIF. On a going-forward basis, SAIF might generate tax loss carry-forwards that would reduce future tax liabilities. In addition, as a private carrier SAIF would likely use tax optimizing strategies to maximize its after-tax return. An optimizing tax strategy might involve changes in reserving practices, dividend policy, or investment asset mix. Therefore, it is quite likely that the taxes estimated above are upper bound estimates; actual future tax obligations would likely be much lower for comparable business volume.

c. Estimated Impact on SAIF's Capital and Surplus, and Rates if Subject to Taxation

Estimates of the state corporate excise and federal income taxes that SAIF would have paid for the years 1992 through 1995 are displayed in the tax worksheet, Table N.b.-1. Data which underlie these calculations are shown in Table N.b.-2. As of December 31, 1991, SAIF's surplus as regards policyholders amounted to \$218,397,903. Had SAIF paid the estimated upper bound corporate excise taxes and federal income taxes for the period 1992 through 1995, SAIF would have paid a combined estimated \$30,157,977 in corporate excise tax, and a combined estimated \$144,926,070 in federal income tax. Table N.c.-1 shows the estimated tax effects on SAIF's financial condition for the subject period. Among other things, the table shows an estimate of SAIF's year end adjusted surplus after the tax effects, and two important ratios: (1) net premium written to adjusted surplus; and, (2) adjusted surplus to risk based capital control level. SAIF's actual book surplus for the subject period would have been reduced by the amount of taxes paid. However, based on both of the aforementioned ratios for each year, the adjusted surplus balances would have been sufficient for actuarial purposes to permit SAIF to participate in the Oregon market at its actual premium volume while charging the rates it actually charged and remitting actual dividends paid to policyholders. Whether SAIF's management would have made these same decisions had it been subject to tax is a question that only SAIF's management can answer.

can answer. If a tax on income were to reduce SAIF's surplus growth to a level that is insufficient to service its current share of the market, then SAIF would have to consider increasing rates. Whether SAIF would do this would likely be determined by other market considerations. If SAIF's surplus were less than half of premium writings, or SAIF's surplus dropped below its minimum risk based capital requirement, then the Department would require SAIF to file a plan of action that might include an increase in rates. Generally, the requirement to pay taxes has the effect of reducing the amount by which capital and surplus may grow during periods of positive financial operations.

The department has also attempted to model the tax impact assuming SAIF had efficiently shifted its cash and invested assets to a portfolio paralleling private insurers on January 1, 1992, and subsequently realized investment returns and effective tax rates similar to private insurers. Table N.c.-2 displays our calculations of apparent yield rates and tax rates on investment income for the selected insurers. These rates are carried into Table N.c.-3 to model results for SAIF during the years 1992 through 1995.

Since invested assets include cumulative amounts of unrealized capital gains, the reported amounts of unrealized gains were included in the apparent investment yield rates. However, unrealized gains were excluded from the apparent tax rate calculation. Hence, taxes for SAIF in Table N.c.-3 include tax on unrealized gains which SAIF would actually defer. The model thus slightly understates invested assets and surplus by the amount of this tax payment deferral.

Insurers must discount unpaid losses for tax calculations. This discount was included in both tables. As SAIF realizes the accrual of its tax-calculation discount, future tax payments will be correspondingly reduced. Statutory insurance accounting does not allow insurers to recognize this prospective recovery. General accounting theory, however, might allow SAIF to capitalize these prepaid taxes. The amount would be approximately the change in unpaid losses and loss adjustment expenses since the end of 1991 times both the nominal tax rate and the complement of the discount factor. In the context of the model, the amount is about \$19 million.

As in Table N.c.-1, ratios of net written premium to the model surplus and of the model surplus to risk-based capital control levels were calculated. The invested assets and surplus for SAIF in this model in Table N.c.-3 are somewhat less than in Table N.c.-1 but, again, the model surplus balance would have been sufficient for SAIF to participate in the Oregon market at its actual premium volume, charging the rates it actually charged and paying the dividends it actually paid. If the estimated prepaid taxes mentioned above were included, the ratios in Table N.c.-3 would be nearly identical to those in Table N.c.-1.

It must be emphasized that the estimates of SAIF's potential tax obligations presented herein have been developed within the context of numerous assumptions, perhaps most important of which is that SAIF would be subject to taxation at its current income levels. Were SAIF subject to taxation, SAIF's management, like any business, would have numerous ways available to minimize its actual tax obligations. However, it serves no useful purpose to speculate here about exactly what steps SAIF's management might take.

In addition, it should be noted that in evaluating proposed premium rates, future taxes are prospectively modeled, as opposed to using actual historic data because of the lack of a clear relationship between operating income and tax liabilities. Were SAIF subject to incremental tax expenses, it would have the same economic incentives to provide its current array of programs and services. Future decisions to continue the programs and services would be influenced by cost-benefit considerations and market competition.

## **O. The Oregon Insurance Guaranty Association**

This section describes the Oregon Guaranty Association, the fact that SAIF does not participate in the Association, SAIF's estimated incremental expenses if it did participate, and a brief description of Association member credits.

### **a. The OIGA and its Operations**

The Oregon Insurance Guaranty Association (OIGA) functions as an insurer to pay claims of property and casualty insurers that become insolvent. The OIGA is governed by ORS 734.510-710. With the sole exception of SAIF, these laws apply to all foreign and domestic insurers, that write all kinds of direct insurance except life, health, title, surety, credit, mortgage guaranty, home protection insurance, and wet marine and transportation insurance. The purpose of the OIGA is specified in ORS 734.520:

"The purpose...is to provide for the payment of covered claims under certain insurance policies to avoid excessive delay in payment and to avoid financial loss to claimants or policyholders because of the insolvency of an insurer, to assist in the detection and prevention of insurer insolvencies, to provide an association to assess the cost of such protection among insurers and to assist in the liquidation of insurers as provided..."

The OIGA has the authority to assess all member insurers for the funds necessary to carry out its responsibilities. The assessments of each member insurer are in proportion to net direct premiums written by the member insurer compared to the net direct premium written by all member insurers for the preceding calendar year.

A summary of the OIGA activities for the period 1982 through 1995 is provided in Table O.a.-1. The table shows the number of insolvency claim files pending by type, the number of insolvencies currently administered, the number of new insolvencies, assessments made, total revenues of the OIGA, net claims payments made, administrative expenses, and the ending Association fund balance. The data has been summarized from OIGA annual reports.

### **b. OIGA Member Assessment Credits**

Member insurers are entitled to offset the OIGA assessment first against the insurer's corporate excise tax (ORS 734.570(3)), next against its gross premium tax imposed under ORS 731.816, and third against its fire insurance gross premium tax imposed under ORS 731.820. The offset

may be applied at a rate of 20 percent of the amount of the assessment for each of the five calendar years following the assessment (ORS 734.575).

c. SAIF's Expenses if Subject to the OIGA

We have attempted to calculate SAIF's additional expenses if it were subject to the OIGA assessment. In calendar years 1992, 1994, and 1995, SAIF would not have incurred additional expenses because the Association did not levy assessments in those years. In 1993, the OIGA levied a total assessment of \$1,497,899 (see Table O.a-1). SAIF's 1992 direct premiums written amounted to \$257,369,899, or 9.576 percent of all property and casualty premiums written, which totaled \$2,687,775,000. Therefore, as shown in Table O.b.-1, it is estimated that SAIF would have paid an assessment of \$143,798 in calendar year 1993. Estimated future expenses to SAIF would be a function of required OIGA assessments and SAIF's share of the subject total net direct premiums written.

The 1993 assessment would have entitled SAIF to potential offsets against corporate excise tax of an estimated \$28,760 per year for 1994 through 1998. Four other assessments prior to 1992 would also have resulted in offsets during 1992-1995. SAIF would have been assessed an estimated \$397,575 in 1987, \$325,874 in 1988, \$284,807 in 1989, and \$203,859 in 1991. Including the 1992 amount, these assessments would have entitled SAIF to offsets totaling \$242,423 in 1992, \$162,908 in 1993, \$126,493 in 1994, and \$69,532 in 1995 (see Table O.b.-1). Any impact on the State's General Fund revenues due to shifting a share of assessments to SAIF would depend upon how SAIF's usable offsets compare with usable offsets lost to other member insurers because of the redistribution. As Table O.b.-1 indicates, SAIF could have used its full offset each year from 1992 through 1994 and an estimated \$22,173 in 1995, for a total of \$553,997 (92.1 percent) usable out of \$601,356 potential offsets over the four years. In recent years, property and casualty insurance companies have averaged close to 90 percent utilization of their potential offsets. Furthermore, if their potential offsets had been reduced, their utilization percent would have been higher. This suggests that the effects on General Fund revenues of shifting a share of OIGA assessments to SAIF would be negligible.

Currently, Oregon law does not provide for specific action if SAIF were to become financially impaired. Essentially, the Legislature would have to decide what action to take in order to protect claimants.

**P. Potential Regulatory Efficiencies From Uniform Application of the Insurance Code**

Six years after the enactment of the "three-way" system in 1965, individual provisions of the Insurance Code began to be applied to SAIF on a piecemeal basis. As a result, some portions of the code apply to SAIF explicitly, some portions apply to SAIF only implicitly, and other portions still do not apply to SAIF. At times, this situation has led to confusion, conflict and frustration among the public, the Department of Consumer and Business Services, and SAIF. Accommodation, compromise and resolution have been achieved on an issue-by-issue basis, but not without a price: substantial Attorney General fees and countless hours of debate. A variety of issues continue to be unresolved to this day.

To illustrate the problem, note the conflicting provisions of Chapter 737 of the Insurance Code and Chapter 656 of the Workers' Compensation Law. ORS 737.205 requires every insurer--including SAIF--to file rates with the Director for approval. ORS 656.508, however, provides that SAIF may adjust its premium rates whenever it chooses, "effective on such dates as SAIF may determine." This type of obvious, direct conflict leads to unnecessary uncertainty in the relationship between DCBS and SAIF.

The Department of Consumer and Business Services proposed Senate Bill 182 in the 1993 legislative session to clarify the regulatory relationship between SAIF and DCBS, but that measure failed.

Uniform application of the Insurance Code to SAIF and other workers' compensation insurers would achieve two things: clarity and parity. This would clear up any confusion that exists regarding how SAIF is regulated, and enable DCBS to regulate the workers' compensation market with greater fairness and efficiency. With clear lines of statutory authority, both DCBS and SAIF could avoid expensive, protracted disagreement.

In considering whether SAIF should be subject to the same regulations and control as other insurers, there are three categories of regulation that need to be considered. The first involves the regulatory relationship between DCBS and SAIF. These include capital and surplus requirements, ratemaking authority, and a variety of financial oversight issues.

The second category of statutory differences involves financial advantage for SAIF. For example, SAIF is allowed to discount its reserves, unlike other workers' compensation insurers; and SAIF is not subject to Guaranty Fund assessments. These factors, perhaps more than any others, lead to complaints by competitors of an "uneven playing field."

Uniform application of the Insurance Code to SAIF would afford SAIF the regulatory protections enjoyed by other workers' compensation insurers. SAIF could avoid possible legal costs and damages if it had the protection of the Code's confidentiality provisions regarding complaints and investigations (ORS 731.264). Judicial and other legal expenses might similarly be avoided if SAIF had a right to a contested case hearing for rate disapproval (ORS 731.240), and the hearing procedures under ORS 737.342.

Regulatory efficiencies would be achieved by harmonizing application of the Insurance Code to SAIF and other workers' compensation insurers. Such uniformity would reduce demands on legal and other staff resources for both SAIF and DCBS which are often needed to devise alternative regulatory treatment for SAIF. Commonality should also conserve actuarial resources from both SAIF and DCBS. For instance, consistency of loss reserve discounting should result in more stable and predictable loss development factors, eliminating the opportunity for disagreements which would save some regulatory resources. Although these regulatory efficiencies are important, the magnitude of potential efficiencies is small compared to the total costs of the workers' compensation system, and would have minimal effect on the conduct of the workers' compensation market.



The third category of statutory difference involves the attributes of a public corporation rather than the statutory application of the Insurance Code or workers' compensation laws. These include:

- SAIF has a five-member public board of directors appointed by the Governor and confirmed by the Senate.
- SAIF's records must be accessible to the public (with the exception of account records and claimant files).
- SAIF's board of directors' meetings are subject to the public meetings law.
- SAIF is required to use the Oregon Attorney General for legal counsel.
- SAIF is required to be the state's workers' compensation insurer.
- SAIF employees are covered under the PERS system.
- SAIF and its officers and employees enjoy qualified immunity and limitations on tort liability under the Oregon Tort Claims Act.
- SAIF's investments are managed by the State Treasurer.
- SAIF is not subject to state or federal income taxes.

Some of these requirements (tort liability protections and the state as a large captive customer) are clear advantages for SAIF. Other requirements (use of the Attorney General for legal counsel and the State Treasurer for managing investments) may limit the choices that SAIF can make. Still others (the public meetings law and the public records law) impose requirements on SAIF with which other insurers need not comply. Finally, state and federal tax exempt status provides SAIF with a competitive advantage.

The legislature would need to carefully consider which of the attributes of a public corporation it wishes to leave in place. Any advantages left in place diminish the "level playing field" objective. Any disadvantages left intact might hinder SAIF's ability to effectively compete. As any of these requirements are removed, public control of SAIF is diluted. All of these tradeoffs need to be carefully balanced.

#### **Q. Agent Operations in the Oregon Workers' Compensation Market**

Insurance agents must be licensed by the Insurance Division to transact all lines of insurance, including workers' compensation. In order to handle business for a particular insurance company, the agent must be appointed by that company, and is considered by law to be the agent of the company in all matters related to the insurance transaction. Agents solicit accounts, advise customers on their exposure to various risks, and quote prices for the appropriate coverage. Once coverage is secured, they may provide assistance with claims reporting and premium collection.

Currently, there are roughly 6,600 individuals licensed as Property and Casualty agents in Oregon. SAIF uses both full appointments and partial appointments with its agents. The difference between the two classes of appointment is that the "full" agent has a regular, ongoing working relationship with SAIF, whereas the "partial" agent deals with SAIF on an account-by-account basis. SAIF has 75 full appointments and 33 partial appointments. These numbers, however, include both agencies as well as individual agents; an actual count of the

number of appointed individual agents is not available. Perhaps a better indicator of the level of independent agent involvement with SAIF is that these agents, both full and partial, handle approximately 55% of SAIF's total business.

#### **R. Issues Relating to SAIF as a Monoline Insurer**

By statute, SAIF is limited to writing only workers' compensation and related coverages. In addition, it is able to provide this insurance only to cover Oregon workers. These factors tend to inhibit SAIF's ability to compete in certain cases. For example, if an employer has operations in several states, SAIF could only cover the Oregon portion of the business, while a private insurer licensed in all the states involved could insure the entire business under a single policy. Also, a private insurer might provide coverage for several lines of insurance and by "packaging" a marginal workers' compensation exposure with other desirable coverages, make the "package" more attractive to insure. SAIF is unable to do this, thus having to evaluate only the marginal workers' compensation exposure without collateral support. In addition, because of SAIF's status as a monoline insurer it cannot accomplish the following: issue twenty-four hour coverage without entering into a partnership with a health insurer; diversify its business risk into other lines of property and casualty insurance; and, achieve administrative economies of scale associated with issuing multiple lines of insurance coverage.

#### **S. Miscellaneous Issues**

The Department contracted with Richard E. Sherman & Associates, Inc., an actuarial firm, to conduct a Special Scope Examination of SAIF which included various subject matter areas not regularly included in either financial or market conduct examinations. Many of the earlier sections of this report incorporate the findings of the special examination such as the discussions of SAIF's tax status and dividend policy. This section includes a summary of the special examination findings for subject matter areas not previously discussed.

##### **a. Lobbyist Expenditures**

From 1986 through 1995, SAIF expended \$236,928 on outside lobbyists (see Appendix S.a.). Of this amount, approximately half was paid to the Public Affairs Council; however, not all work performed by the Council can be considered lobbying. As for in-house lobbying expenses, SAIF does not maintain accounting records that would permit the identification of lobbying activities and corresponding expense for SAIF personnel. SAIF management advised that there has been only limited lobbying activity by employees, and that salary expense is not allocated to lobby expense. Comparable data for other insurers is not readily available. However, we do not believe SAIF's expenditure to be atypical.

##### **b. Real Estate Activities**

The attached Appendix S.b. summarizes the properties owned by SAIF for the period from January 1, 1980 through December 31, 1995. The table shows the acquisition date, the actual cost, the book value, the market value, and if applicable, the date of sale, the sale price and gain

or loss on the sale. As of December 31, 1995 the market value of real estate owned amounted to \$30,599,590 compared to the actual cost of the properties amounting to \$29,832,359. During the subject period, SAIF disposed of eight properties for a combined gain of \$258,293.

c. Competitive Bidding and Purchasing Processes

SAIF's purchasing of goods and services is accomplished by using its own purchasing system and processes instead of the system and processes used by other state agencies. SAIF's purchasing system is generally similar to the state system. The most significant difference is that SAIF does not advertise for bids as is required for other state agencies. Instead, SAIF invites vendors to submit bids (see Appendix S.c.). Although SAIF has access to the state purchasing system, SAIF uses the system on a selective basis. SAIF management believes that its competitive bidding and purchasing processes provide for more flexibility, and therefore cost savings.

d. Administrative Expense Analysis

The attached Appendix S.d. displays the results of one method for developing an industry comparison of administrative expenses for SAIF, Liberty Northwest and three other state funds for the period 1992 through 1995. For each organization, the table displays total administrative expenses, direct premiums earned, and the ratio of administrative expenses to premium earned. For SAIF only, the table also displays the number of employees at year end and the ratio of SAIF employees per million dollars of premium for each year. Notice that SAIF's administrative expense ratio (ADRATE) has climbed from 35.6 percent in 1992 to 47.2 percent in 1995. The ADRATE for all other organizations has trended upward as well with the exception of the Idaho State Insurance Fund. Generally, the increase in the ADRATE can be explained by a combination of increases in administrative expenses coupled with decreases in direct earned premium volume over the subject period.

This industry comparison of administrative expenses shows that SAIF's expenses are a greater percentage of earned premium than for the other entities. However, there may be a number of factors that explain this situation. First, SAIF operates similarly to a private carrier. Comparisons with state funds that do not aggressively solicit business or are insurers of last resort may not be appropriate. Second, SAIF operates only in Oregon. Perhaps the business climate and Oregon specific workers' compensation law may cause differences in administrative or operating expenses. Third, SAIF may spend more on loss consultation services to reduce claims frequency, or spend more on managed care to reduce the medical cost of claims. Finally, SAIF is a monoline insurer. Perhaps the administrative expense basis is different for a multiple line insurer that also sells other property and casualty coverage.

e. Premium Collection

Premiums are due directly from the insured employers. For employers that remit premium monthly, at the end of each month the employer fills out a payroll report for all covered employees. The report, along with the applicable premium, is due to SAIF by the 15th of the

following month. For a limited number of policies, quarterly payments are received, in which case the premium due is payable on the 15th of the month following the end of the quarter. No exceptions were noted in which certain employers were given differential payment treatment.

SAIF maintains reports for premiums over and under 90 days past due. Premiums due over 90 days are properly treated as non-admitted assets. Premiums over 90 days past due at year end as a proportion of premiums in the course of collection grew substantially from 1990 through 1992. However, this situation began to reverse in 1993 and has continued to improve through 1995.

Finally, it should be noted that the examination of SAIF's uncollected premium accounts as of December 31, 1995, did not reveal violations of ORS 656.504.

**f. Expropriation of \$81 Million From the Industrial Accident Fund**

In June of 1983, the State of Oregon expropriated \$81 million from the Industrial Accident Fund and transferred the moneys to the State General Fund. Litigation concerning the expropriation ensued, and on November 18, 1993, the Oregon Supreme Court ruled the transfer inappropriate. See Alsea Veneer, Inc. v. State of Oregon. The Court ruled that the State must repay the moneys, including interest, to the Industrial Accident Fund (IAF), and also ordered that a lower court decide what SAIF should do with the money remitted to the IAF.

During 1994, the State paid a \$5 million installment to the IAF. An additional \$60 million was paid to the IAF during 1995. Settlement negotiations occurred among the parties and a settlement agreement for an additional \$160 million of payments was reached and approved by the Marion County District Court on February 26, 1996. The funds are to be disbursed to the plaintiffs and the IAF. However, legislative appropriation is required before the moneys may be paid by the State. Details about these events are provided in the attached Appendix J, pages 26 and 27.

**T. Conclusion**

Throughout this report, we have provided myriad facts and analyses regarding SAIF and Oregon's workers' compensation system. We will leave sweeping policy conclusions to the legislature and others. There are, however, some significant observations that may be made. These observations are briefly summarized below.

1. Oregon's workers' compensation system is an example of a competitive-state-fund model, and the recent national trend has been toward this same model.
2. Oregon's measures of market concentration are higher than the national averages, and Oregon's market is considered highly concentrated; however, this fact should not be surprising given that Oregon has a mature state fund, which in 1995 insured nearly half of Oregon employers required to purchase workers' compensation insurance and accounted for one-third of total premium volume.

3. Oregon's workers' compensation premium rate ranking for 1996 is 34th highest in the nation, a significant improvement since 1990.
4. Studies suggest that the presence of a state fund correlates significantly with higher premium rates, but in recent times Oregon is an exception to this generalization most likely because of the enactment of legislative reforms, effective responses to reforms by SAIF and private insurers, and concomitant premium rate decreases.
5. Compared to other industries, Oregon's workers' compensation market has few barriers to entry, and market exit is induced primarily by economic or systems conditions rather than by the structure of the Oregon market. Many new companies have expressed an interest in transacting business in the Oregon market.
6. The Department's role as regulator of Oregon's workers' compensation market is extensive and includes activities of both the Insurance and Workers' Compensation Divisions.
7. There are numerous statutory and regulatory differences between the State's treatment of SAIF and its treatment of private carriers. Some of these differences confer competitive advantage upon SAIF; some confer a competitive disadvantage.
8. The voluntary market tends not to insure new small businesses due to underwriting and other business considerations; nevertheless, the Oregon Assigned Risk Plan (ARP) insures only 7.9 percent of the total voluntary market premium. This is well below the national average of over 25 percent.
9. Oregon seems to be an anomaly when considering the results of insurance underwriting and the presence of a state fund. Oregon is the only state with a state fund that does not serve as the market of last resort, that has been able to achieve results that suggest both rate adequacy and profitability for the market. Both SAIF and private insurers have contributed to this result.
10. The financial examinations by both the Secretary of State and Insurance Division of SAIF concluded that there were no overall material misstatements of SAIF's financial results.
11. Historically there have been differences in the way SAIF and private carriers discount loss reserves. However, recently SAIF's discounting practices have been tending more toward standard private carriers' practices. Prior to 1992 the difference in SAIF's discounting practice and private carrier tabular reserve discounting exceeded \$300 million; in 1995 that difference would be about \$55.7 million.
12. The recent market conduct examination of SAIF did not identify significant problem areas with respect to statutory or administrative rule requirements.
13. SAIF generates substantial investment income which it uses to set rates at very competitive levels.

14. SAIF's claims management practices are consistent with statutory and administrative rule requirements.
15. Overall, OR-OSHA finds SAIF's loss control efforts comparable to the market and, in some areas, ahead of the market.
16. Both the Department and SAIF are generally provided legal counsel by the State Attorney General. At times, problems arise with this arrangement when the Director must resolve conflicts between SAIF and the Department.
17. State agencies are required to provide workers' compensation coverage of state employees through SAIF exclusively.
18. SAIF is exempt from numerous taxes including state corporate excise tax and federal income tax; the tax savings may be substantial.
19. SAIF is not a member of the Oregon Guaranty Association. Currently, Oregon law does not provide for specific action if SAIF were to become financially impaired.
20. There is the potential for regulatory efficiencies by a more uniform application of the Insurance Code with respect to SAIF.
21. Industry comparisons of administrative expenses show that SAIF's expenses are a greater percentage of earned premium than for other insuring entities, a fact that may be due, at least in part, to SAIF's unique status and its claims management practices.
22. SAIF's financial condition has improved substantially since 1989; today, SAIF's financial condition is sound.

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**APPENDICES,  
EXHIBITS, TABLES  
&  
CHARTS**





Table D.a.2-1-2

## Summary of Workers' Compensation Market Characteristics by State for 1992

1992 STATE FUND STATES	Average Benefits paid per Covered Employee 12/				WC Premium Rate Ranking 13/				Premium Weighted Index Rate		Resid Mkt. Undwrtng Burden 14/	Herfindahl Inde Excluding Monopoly 15/	Number of Ins 16/	Rank	Mkt. Conc. Ratio 4 Firm 17/
	1991	Rank	1992	Rank	1990	Index Rate	1992	Index Rate	1990	1992					
ARIZONA	71.5%	36	67.1%	36	22	3.93	25	4.34	2,261,943	2,497,922	-1.6%	2,422.0	99	21	60.4
IDAHO	78.8%	29	71.3%	32	26	3.80	29	3.90	772,023	792,340	-1.0%	2,545.8	76	38	67.0
MICHIGAN	88.6%	25	85.9%	23	19	4.00	18	4.75	4,957,332	5,886,832	-3.3%	559.6	109	12	39.9
MINNESOTA 2/	80.8%	27	80.4%	28	1	6.72	7	6.18	4,019,944	3,696,913	NA	372.2	99	21	28.5
NEW MEXICO 6/	114.6%	18	91.5%	19	14	4.82	19	4.63	1,075,053	1,032,675	-11.6%	1,469.8	83	33	63.1
OREGON	121.2%	13	85.7%	24	8	5.65	22	4.41	3,703,846	2,890,967	-2.9%	2,203.2	80	36	71.0
TEXAS 7/	164.8%	3	118.8%	11	2	6.46	2	6.51	16,095,865	16,220,446		509.9	108	15	34.1
CALIFORNIA	139.7%	8	140.2%	6	9	5.61	8	5.96	48,403,400	51,423,220		648.8	110	9	36.0
COLORADO 8/	124.9%	12	117.2%	12	5	5.94	1	6.60	4,239,402	4,710,446		2,513.4	104	18	67.3
LOUISIANA 1/	116.9%	15	94.7%	18	16	4.50	16	4.96	2,166,633	2,388,111	-173.3%	922.2	81	35	54.4
MARYLAND 5/	73.7%	33	71.1%	33	42	2.61	45	2.86	1,330,784	1,458,254	5/	867.2	110	9	43.3
MONTANA 3/	150.5%	7	197.6%	1	3	6.43	3	6.34	1,181,217	1,164,683		4,821.5	71	41	82.4
NEW YORK	71.2%	37	74.1%	30	30	3.46	11	5.36	11,819,395	18,309,814		2,022.2	113	8	59.3
OKLAHOMA	116.0%	17	110.7%	15	28	3.55	26	4.11	1,734,775	2,008,430		2,073.2	91	28	47.8
PENNSYLVANIA 5/	119.4%	14	114.9%	13	20	3.98	21	4.60	10,518,658	12,157,243	5/	462.8	125	3	35.1
UTAH 3/	63.7%	44	65.3%	37	46	2.34	42	3.00	530,534	680,172		3,315.4	78	37	67.2
RHODE ISLAND 18/	156.6%	5	172.5%	4	7	5.77	6	6.19	888,649	953,334		2,158.7	56	43	87.1
NON STATE FUND STATES															
ALABAMA	91.6%	24	80.8%	27	31	3.41	13	5.04	1,317,126	1,946,719	-27.2%	591.7	96	24	37.4
ALASKA	152.3%	6	135.6%	7	15	4.78	24	4.35	914,681	832,398	-3.0%	1,440.1	60	42	64.6
ARKANSAS	77.4%	31	64.4%	40	29	3.48	28	4.04	1,116,113	1,295,718	-36.3%	579.5	94	25	36.2
CONNECTICUT	135.8%	9	124.6%	10	10	5.50	5	6.21	3,380,177	3,816,527	-5.8%	608.9	83	33	41.6
DELAWARE	76.3%	32	74.9%	29	33	3.26	36	3.35	309,744	318,296	-12.4%	514.8	90	29	34.2
DIST. OF COL.	48.9%	49	61.0%	42	11	5.46	15	4.99	646,409	590,766	-5.6%	618.5	73	39	40.2
FLORIDA	108.7%	21	90.1%	21	4	6.39	4	6.22	6,774,577	6,594,346	-29.1%	693.4	109	12	41.8
GEORGIA	80.4%	28	88.5%	22	27	3.57	17	4.77	3,196,070	4,270,379	-17.2%	340.3	120	4	25.9
HAWAII	125.1%	11	127.5%	8	6	5.87	9	5.52	1,632,167	1,534,849	-7.0%	851.1	53	44	47.6
ILLINOIS	92.2%	23	82.0%	26	17	4.30	14	5.03	8,587,975	10,045,934	-2.5%	501.5	127	2	37.6
INDIANA	44.3%	51	38.0%	51	50	2.03	48	2.29	1,070,235	1,207,310	-3.4%	309.9	129	1	24.6
IOWA	50.5%	46	47.3%	48	36	3.06	35	3.37	1,068,708	1,176,976	-4.7%	421.6	105	17	31.0
KANSAS	73.7%	33	64.6%	38	45	2.43	40	3.10	896,383	1,143,533	-18.6%	441.8	99	21	30.5
KENTUCKY	88.1%	26	83.6%	25	34	3.24	27	4.04	1,294,482	1,614,107	-44.6%	599.4	102	19	41.2
MAINE 4/, 18/	204.6%	1	185.9%	3	12	5.45	12	5.05	1,179,598	1,093,022		3,081.1	40	47	93.7
MASSACHUSETTS	132.9%	10	111.9%	14	13	5.14	10	5.40	6,828,701	7,174,122	-38.4%	1,012.6	86	31	50.3
MISSISSIPPI	66.7%	40	69.9%	34	39	2.94	34	3.41	647,089	750,535	-28.7%	697.8	93	27	45.2
MISSOURI	66.9%	39	73.3%	31	41	2.65	31	3.63	1,975,098	2,705,512	-18.1%	485.7	109	12	32.7
NEBRASKA	50.2%	47	47.1%	49	47	2.31	44	2.92	562,650	711,229	-6.9%	427.3	100	20	31.9
NEW HAMPSHIRE	113.0%	19	100.2%	17	18	4.18	23	4.40	786,004	827,373	-45.2%	805.8	87	30	46.3
NEW JERSEY	69.2%	38	64.6%	38	43	2.48	38	3.13	2,879,338	3,634,003	-16.6%	789.6	110	9	43.9
NORTH CAROLINA	47.5%	50	53.1%	47	51	1.53	47	2.56	929,027	1,554,450	-10.2%	481.3	107	16	33.6
SOUTH CAROLINA	56.6%	45	59.8%	44	35	3.22	46	2.71	1,060,962	892,921	-15.3%	682.1	94	25	43.1
SOUTH DAKOTA	64.8%	43	59.2%	45	37	3.06	33	3.42	291,621	325,929	-14.7%	376.1	85	32	30.4
TENNESSEE	78.1%	30	67.9%	35	32	3.34	37	3.33	2,111,828	2,105,505	-36.4%	587.2	119	5	38.0
VERMONT	65.8%	41	62.8%	41	40	2.88	39	3.11	254,908	275,265	-22.4%	690.8	72	40	40.5
VIRGINIA	50.0%	48	43.6%	50	49	2.19	49	2.28	1,201,713	1,251,099	-22.2%	463.2	115	7	32.2
WISCONSIN	65.5%	42	53.9%	46	38	2.99	41	3.02	2,979,373	3,009,266	NA	404.0	119	5	28.5
MONOPOLY STATES															
NEVADA	164.6%	4	194.1%	2	24	3.88	20	4.61	1,353,417	1,608,054			27	51	74.3
NORTH DAKOTA	73.1%	35	60.8%	43	21	3.94	51	1.97	332,735	166,368			28	50	75.9
OHIO	116.7%	16	110.7%	15	25	3.81	30	3.83	8,912,414	8,959,198			52	45	58.7
WASHINGTON *	111.0%	20	127.3%	9	23	3.92	32	3.54	3,316,856	2,995,324			43	46	63.9
WEST VIRGINIA *	175.3%	2	166.9%	5	48	2.30	43	2.99	783,984	1,019,179			35	48	69.2
WYOMING *	93.4%	22	91.5%	19	44	2.47	50	2.12	181,937	156,157			34	49	67.0

(Excluding Monopoly  
States)Minimum  
Maximum  
Average310  
4,822  
1,097  
201%40  
128  
95  
84%25  
94  
46  
154%

Oregon as a % of Avg

Table D.a.2-1-3

## Summary of Workers' Compensation Market Characteristics by State for 1993

1993 STATE FUND STATES	Premium Written (000's) CY 1993			State Fund Market Share %	State Fund is Servicing Carrier? %	Assigned Risk Plan? %	S.F. is Mkt of Last Resort? %	Residual Market Share %	Direct Combined Ratio %	Premium Weighted Direct Combined Ratio	Avg. Benefit Per Covered Empl. 10/	Rank 11/
	State Fund %	Privates %	Total Premium %									
ARIZONA	315,369	311,090	626,459	50.3%	Y	Y	N	3.3%	102.9%	644,626	68.7%	36
IDAHO	116,491	126,037	242,528	48.0%	N	Y	N	2.6%	102.9%	249,561	73.2%	32
MINNESOTA 1/	44,783	647,078	691,861	6.5%	N	Y	N	NA	121.9%	843,379	82.0%	24
NEW MEXICO	14,887	191,096	205,983	7.2%	Y	Y	N	46.9%	66.4%	136,773	78.3%	28
OREGON 3/	256,830	355,580	612,410	41.9%	Y	Y	N	8.0%	98.4%	602,611	86.3%	20
TEXAS	316,151	1,773,199	2,089,350	15.1%	N	N	N	NA	105.6%	2,206,354	97.0%	17
CALIFORNIA	1,705,363	7,335,513	9,040,876	18.9%	N	N	Y	NA	100.7%	9,104,162	145.9%	6
COLORADO	373,234	385,322	758,556	49.2%	N	N	Y	NA	110.6%	838,963	107.3%	15
LOUISIANA	205,740	189,582	395,322	52.0%	N	N	Y	NA	91.9%	363,301	76.8%	29
MARYLAND 2/	134,945	378,277	513,222	26.3%	N	N	Y	NA	110.4%	566,597	72.3%	33
MONTANA	169,993	62,831	232,824	73.0%	N	N	Y	NA	100.0%	232,824	164.4%	3
NEW YORK 5/	1,614,463	1,946,319	3,560,782	45.3%	N	N	Y	NA	127.2%	716,878	80.3%	26
OKLAHOMA	254,202	309,381	563,583	45.1%	N	N	Y	NA	109.6%	617,687	119.1%	12
PENNSYLVANIA 2/	450,880	2,410,149	2,861,029	15.8%	N	Y	Y	NA	129.8%	3,713,616	122.1%	11
UTAH	151,850	128,414	280,264	54.2%	N	N	Y	NA	96.1%	269,334	73.8%	31
MAINE 4/	68,431	101,331	169,762	40.3%	N	N	Y	NA	104.9%	178,080	154.1%	4
RHODE ISLAND	61,507	59,297	120,804	50.9%	N	N	Y	NA	68.9%	83,234	126.0%	10
NON STATE FUND STATES												
MICHIGAN	0	1,025,308	1,025,308	0.0%	N	Y	N	14.4%	98.5%	1,009,928	89.7%	19
ALABAMA	0	337,267	337,267	0.0%	N	Y	N	40.5%	124.6%	420,235	79.8%	27
ALASKA	0	181,846	181,846	0.0%	N	Y	N	16.3%	90.9%	165,298	134.5%	8
ARKANSAS	0	308,947	308,947	0.0%	N	Y	N	51.4%	86.2%	266,312	60.7%	43
CONNECTICUT	0	626,691	626,691	0.0%	N	Y	N	11.6%	105.6%	661,786	134.1%	9
DELAWARE	0	87,080	87,080	0.0%	N	Y	N	17.4%	127.8%	111,288	74.5%	30
DIST. OF COL.	0	108,959	108,959	0.0%	N	Y	N	18.6%	108.8%	118,547	63.1%	41
FLORIDA	0	1,161,829	1,161,829	0.0%	N	Y	N	34.2%	133.3%	1,548,718	83.9%	21
GEORGIA	0	831,975	831,975	0.0%	N	Y	N	28.7%	107.4%	893,541	83.5%	22
HAWAII	0	340,413	340,413	0.0%	N	Y	N	20.3%	130.2%	443,218	153.9%	5
ILLINOIS	0	2,069,997	2,069,997	0.0%	N	Y	N	12.6%	103.0%	2,132,097	81.3%	25
INDIANA	0	618,877	618,877	0.0%	N	Y	N	14.7%	92.8%	574,318	38.0%	51
IOWA	0	382,630	382,630	0.0%	N	Y	N	18.6%	87.3%	334,036	45.5%	49
KANSAS	0	371,390	371,390	0.0%	N	Y	N	38.6%	95.7%	355,420	69.5%	35
KENTUCKY	0	437,260	437,260	0.0%	N	Y	N	44.1%	111.6%	487,982	82.6%	23
MASSACHUSETTS	0	1,396,817	1,396,817	0.0%	N	Y	N	61.0%	81.2%	1,134,215	94.8%	18
MISSISSIPPI	0	222,166	222,166	0.0%	N	Y	N	41.6%	90.5%	201,060	60.9%	42
MISSOURI 6/	0	731,113	731,113	0.0%	N	Y	N	35.0%	95.8%	700,406	71.2%	34
NEBRASKA	0	263,023	263,023	0.0%	N	Y	N	19.7%	95.1%	250,135	49.8%	48
NEW HAMPSHIRE	0	222,331	222,331	0.0%	N	Y	N	38.4%	117.1%	260,350	97.9%	16
NEW JERSEY	0	1,327,998	1,327,998	0.0%	N	Y	N	21.3%	123.2%	1,636,094	68.5%	37
NORTH CAROLINA	0	667,878	667,878	0.0%	N	Y	N	28.4%	109.4%	730,659	51.9%	47
SOUTH CAROLINA 12/	44,011	348,316	392,327	11.2%	N	Y	N	46.2%	98.4%	386,050	60.7%	43
SOUTH DAKOTA	0	109,951	109,951	0.0%	N	Y	N	23.5%	117.5%	129,192	63.7%	40
TENNESSEE	0	649,075	649,075	0.0%	N	Y	N	55.0%	106.9%	693,861	64.8%	38
VERMONT	0	109,772	109,772	0.0%	N	Y	N	41.8%	124.1%	136,227	64.6%	39
VIRGINIA	0	567,172	567,172	0.0%	N	Y	N	32.6%	117.2%	664,726	44.8%	50
WISCONSIN	0	1,154,921	1,154,921	0.0%	N	Y	N	NA	92.9%	1,072,922	56.9%	45
MONOPOLY STATES												
NEVADA	378,146	0	378,146	100%	N	N	Y	NA	NA		204.1%	1
NORTH DAKOTA	91,512	0	91,512	100%	N	N	Y	NA	NA		53.4%	46
OHIO	2,202,310	0	2,202,310	100%	N	N	Y	NA	NA		114.6%	13
WASHINGTON 7/	877,605	0	877,605	100%	N	N	Y	NA	NA		142.3%	7
WEST VIRGINIA 7/	389,139	0	389,139	100%	N	N	Y	NA	NA		180.9%	2
WYOMING	80,535	0	80,535	100%	N	N	Y	NA	NA		109.0%	14

## Notes:

- 1/ Includes both State Fund and Reinsurance Association.  
2/ Fund is market of last resort. Assigned Risk Plan for coverage which State Fund can't write e.g. Certain Federal Coverage.  
3/ Premium Written for SAIF Corporation is from the 1993 Annual Statement.  
4/ The Maine state fund Employers' Mutual Insurance Company was created in 1992.  
5/ The premium earned is unaudited.  
6/ Missouri Employers' Mutual Insurance Company (MEM) was established on 6/21/93 and issued its first policy on 2/2/95.  
7/ Premium earned is for the fiscal year ending 6/30/93.

8/ All data is for calendar year 1994.

Reference sources: State Fund States: 1. NCCI Quick Facts of Workers' Compensation for 1993 from the 1995 Issues Report.  
2. 1995 Fact Book, American Association of State Compensation Insurance Funds (AASCF).  
Non State Fund States: NCCI Quick Facts of Workers' Compensation 1995 Issues Report.  
Monopoly State Fund States: 1995 AASCF Fact Book. Private insurer data represents non specific coverage not covered by the state fund.  
NCCI Quick Facts of Workers' Compensation 1995 Issues Report.

9/ Reference source:

- 10/ Average benefits per covered employees in 1993 as a percentage of the U.S. Average. Source: John Burton's 1996 Workers' Compensation Year Book.  
11/ State with the highest average benefit per covered employee has a rank value of 1.  
12/ The state fund in South Carolina insures only state employees and is not a competitive fund.  
13. Earned Premium earned, from the 1995 AASCF Fact Book, is used for all the state funds (except SAIF Corp. of Oregon.)

Table D.a.2-1-4

Summary of Workers' Compensation Market Characteristics by State for 1994 and 1996

1994-1996 STATE FUND STATES	Premium Written (000's) CY 1994			State Fund Market Share %	State Fund is Servicing Carrier? #/	Assigned Risk Plan? #/	S.F. is Mkt of Last Resort? #/	Residual Market Share %	Direct combined Ratio %	Premium Weighted Direct Combined Ratio	Avg. Benefit Per Covered Empl. 10/	Rank 11/
	State Fund #/	Privates #/	Total Premium #/									
ARIZONA *	338,420	378,391	716,811	47.2%	Y	Y	N	1.3%	97.7%	700,325	68.7%	36
IDAHO *	139,986	116,752	256,738	54.5%	N	Y	N	2.6%	91.5%	234,915	73.2%	32
MINNESOTA * 1/	55,855	631,876	687,731	8.1%	N	Y	N	NA	99.0%	680,854	82.0%	24
NEW MEXICO *	57,599	161,503	219,102	26.3%	Y	Y	N	34.5%	65.8%	144,169	78.3%	28
OREGON *	262,928	352,258	615,186	42.7%	Y	Y	N	8.7%	97.9%	602,267	86.3%	20
CALIFORNIA *	1,449,033	6,184,757	7,633,790	19.0%	N	N	Y	NA	99.1%	7,565,085	145.9%	6
COLORADO 2/	370,454	340,576	711,030	52.1%	N	N	Y	NA	87.9%	624,995	107.3%	15
LOUISIANA	246,941	182,969	429,910	57.4%	N	N	Y	NA	104.1%	447,536	76.8%	29
MARYLAND 3/	148,125	415,882	564,007	26.3%	N	N	Y	NA	97.9%	552,163	72.3%	33
MONTANA	181,626	90,281	271,907	66.8%	N	N	Y	NA	75.2%	204,474	164.4%	3
NEW YORK 4/	1,735,301	2,049,406	3,784,707	45.9%	N	N	Y	NA	119.8%	694,248	80.3%	26
OKLAHOMA	289,920	289,586	579,506	50.0%	N	N	Y	NA	103.4%	599,209	119.1%	12
PENNSYLVANIA * 3/	474,480	2,270,072	2,744,552	17.3%	N	Y	Y	NA	108.9%	2,988,817	122.1%	11
TEXAS * 19/	623,433	1,357,952	1,981,385	31.5%	N	N	Y	NA	68.5%	1,357,249	97.0%	17
UTAH	159,050	131,144	290,194	54.8%	N	N	Y	NA	89.5%	259,724	73.8%	31
MAINE	138530	69,890	208,420	66.5%	N	N	Y	NA	119.6%	249,270	154.1%	4
RHODE ISLAND *	112,714	22,606	135,320	83.3%	N	N	Y	NA	105.4%	142,628	126.0%	10
NON STATE FUND STATES												
MICHIGAN	0	1,021,379	1,021,379	0.0%	N	Y	N	10.4%	91.5%	934,562	89.7%	19
ALABAMA	0	313,417	313,417	0.0%	N	Y	N	39.4%	88.3%	276,748	79.8%	27
ALASKA	0	178,218	178,218	0.0%	N	Y	N	16.4%	74.8%	133,307	134.5%	8
ARKANSAS	0	294,476	294,476	0.0%	N	Y	N	39.2%	82.5%	242,943	60.7%	43
CONNECTICUT	0	514,732	514,732	0.0%	N	Y	N	11.4%	115.0%	591,941	134.1%	9
DELAWARE	0	89,968	89,968	0.0%	N	Y	N	22.3%	129.5%	116,509	74.5%	30
DIST. OF COL.	0	103,296	103,296	0.0%	N	Y	N	14.5%	81.7%	84,393	63.1%	41
FLORIDA	0	738,752	738,752	0.0%	N	Y	N	NA	124.2%	917,530	83.9%	21
GEORGIA	0	684,773	684,773	0.0%	N	Y	N	30.7%	94.5%	647,111	83.5%	22
HAWAII	0	363,096	363,096	0.0%	N	Y	N	35.3%	101.7%	369,268	153.9%	5
ILLINOIS	0	2,054,276	2,054,276	0.0%	N	Y	N	10.8%	93.9%	1,928,965	81.3%	25
INDIANA	0	619,910	619,910	0.0%	N	Y	N	11.6%	91.0%	564,118	38.0%	51
IOWA	0	374,175	374,175	0.0%	N	Y	N	13.9%	81.6%	305,327	45.5%	49
KANSAS	0	341,633	341,633	0.0%	N	Y	N	35.4%	104.8%	358,032	69.5%	35
KENTUCKY 5/	0	395,557	395,557	0.0%	N	Y	N	49.1%	121.3%	479,811	82.6%	23
MASSACHUSETTS	0	1,170,652	1,170,652	0.0%	N	Y	N	47.0%	78.6%	920,133	94.8%	18
MISSISSIPPI	0	215,210	215,210	0.0%	N	Y	N	38.6%	80.0%	172,168	60.9%	42
MISSOURI 6/	0	659,587	659,587	0.0%	N	Y	N	37.0%	90.1%	594,288	71.2%	34
NEBRASKA	0	251,040	251,040	0.0%	N	Y	N	15.6%	83.1%	208,614	49.8%	48
NEW HAMPSHIRE	0	211,585	211,585	0.0%	N	Y	N	41.8%	71.5%	151,283	97.9%	16
NEW JERSEY	0	1,278,614	1,278,614	0.0%	N	Y	N	26.6%	113.0%	1,444,834	68.5%	37
NORTH CAROLINA	0	610,502	610,502	0.0%	N	Y	N	23.7%	88.8%	542,126	51.9%	47
SOUTH CAROLINA	31,593	328,115	359,708	8.8%	N	Y	N	42.7%	98.5%	354,312	60.7%	43
SOUTH DAKOTA	0	117,071	117,071	0.0%	N	Y	N	20.4%	94.4%	110,515	63.7%	40
TENNESSEE	0	691,403	691,403	0.0%	N	Y	N	52.3%	102.5%	708,688	64.8%	38
VERMONT	0	110,998	110,998	0.0%	N	Y	N	36.4%	85.1%	94,459	64.6%	39
VIRGINIA	0	625,486	625,486	0.0%	N	Y	N	29.1%	99.0%	619,231	44.8%	50
WISCONSIN	0	1,144,420	1,144,420	0.0%	N	Y	N	8.1%	89.8%	1,027,689	56.9%	45
MONOPOLY STATES												
NEVADA	419,103	7,081	426,184	100%	N	N	Y	NA	NA		204.1%	1
NORTH DAKOTA	104,623	4,026	108,649	100%	N	N	Y	NA	NA		53.4%	46
OHIO	12,905,374	41,517	12,946,891	100%	N	N	Y	NA	NA		114.6%	13
WASHINGTON	920,077	40,317	960,394	100%	N	N	Y	NA	NA		142.3%	7
WEST VIRGINIA 7/	386,371	4,396	390,767	100%	N	N	Y	NA	NA		180.9%	2
WYOMING	101,139	6,520	107,659	100%	N	N	Y	NA	NA		109.0%	14

\* Premium written is used for these state funds. For remaining state funds, premium earned is used.

Notes:

- 1/ Includes both State Fund and Reinsurance Association.
- 2/ Market of last resort. The data was taken from Best Database Services-Experience by State (by Line), Property and Casualty 1995 Edition.
- 3/ Fund is market of last resort. Assigned Risk Plan for coverage which State Fund can't write e.g. Certain Federal Coverage.
- 4/ Written Premium for New York State Insurance Fund from the 1994 Annual Statement was obtained by calling them.
- 5/ Employers' Mutual Insurance Authority (EMIA) was created on 4/4/94. The EMIA started to issue policies and provide coverage on 9/1/95 and the Assigned Risk Pool will cease to exist on the same date.
- 6/ Missouri Employers' Mutual Insurance Company (MEM) was established on 6/21/93 and its first policy on 2/3/95.
- 7/ Premium earned is for fiscal year ending 6/30/94.
- 8/ All data is for calendar year 1994.
- Reference sources: State Fund States: 1. Best Data Base Service - Experience by State (by Line), Property & Casualty 1995 Edition.  
 Non State Fund States: 2. 1995 Fact Book, American Association of State Compensation Insurance Funds (AASCIF).  
 Monopoly State Fund States: 1. Data extracted from NAIC financial statement database by NCCI.  
 NCCI Quick Facts of Workers' Compensation for 1994 from the 1995 Issues Report.
- 9/ Reference source: NCCI Quick Facts of Workers' Compensation for 1994 from the 1995 Issues Report.
- 10/ Average benefits per covered employee in 1993 as a percentage of the U.S. Average. Source: John Burton's 1996 Workers' Compensation Year Book.
- 11/ State with the highest average benefit per covered employee has a rank value of 1.
- 12/ Reference Source: Premium Rate Ranking Report for years 1994 and 1995 published by IMD, Department of Consumer and Business Services.
- 13/ Reference source: NCCI Management Summary 1992. Policy Year Underwriting Results by State (1986 - 1992). Residual Market burden percentage is for policy year 1992.
- 14/ Premium figures and herfindahl index by company, by state for 1994 provided by NCCI. Data derived from the NAIC financial statement database for calendar year 1994.
- 15/ State with the highest herfindahl index value has a rank value of 1.
- 16/ This count of insurers consists of all groups writing in the state and any insurers who are not part of a group. This figure will be less than or equal to the actual number of insurers writing premium in the state.
- 17/ State with the most insurers has a rank value of 1.
- 18/ The market concentration ratios for the monopoly fund states represent private carrier business volume for non-state fund business such as longshore and harbor workers'.
- 19/ Texas Workers' Compensation Insurance Fund became the insurer of last resort on 1/1/94.
- 20/ The state fund insures only state employees and is not a competitive fund.

A5  
Table D.a.2-1-5

Summary of Workers' Compensation Market Characteristics by State

WC Premium Rate Ranking 12/				Premium Weighted Index Rate		Residual Market Net Operating Gain/(Loss) and Written Premium Policy year underwriting results as of December 31, of that year						Herfindahl Index 1994		Number of	Rank	Mkt. Conc. Ratio
1994	Index Rat	1996	Index Rat	1994	1996	1992 Net oper	1992 Prem	1993 Net oper	1993 Prem	1994 Net oper	1994 Prem	Monopoly 14/	Rank 15	Ins 16/	17/	4 Firm 18/
28	4.18	29	3.38	2,996,271	2,422,822	(8,570)	19,702	(8,551)	22,608	(2,933)	7,639	2,361.1	10	94	26	62.02
30	3.88	39	3.00	996,144	770,215	(2,024)	6,814	(1,450)	6,513	(1,595)	6,354	3,005.0	6	76	37	72.70
13	5.29	22	3.68	3,638,097	2,530,850	NA	NA	NA	NA	NA	NA	329.8	42	106	14	27.56
7	5.75	26	3.55	1,259,835	777,811	(28,077)	116,986	(4,513)	101,320	3,318	63,815	1,208.6	14	82	34	60.50
32	3.70	34	3.13	2,276,188	1,925,532	(16,125)	46,071	(3,047)	46,436	(7,626)	55,667	2,450.1	8	82	34	73.78
15	5.04	7	4.89	38,474,299	37,329,231	NA	NA	NA	NA	NA	NA	581.8	27	127	2	36.58
14	5.28	15	4.19	3,754,238	2,979,216	NA	NA	NA	NA	NA	NA	1,769.6	12	85	32	68.77
1	6.98	3	5.47	3,000,772	2,351,608	(76,340)	340,803	NA	NA	NA	NA	3,478.1	4	90	29	71.72
45	3.08	44	2.46	1,737,142	1,387,457	NA	NA	NA	NA	NA	NA	908.8	17	108	13	45.35
2	6.91	4	5.26	1,878,877	1,430,231	NA	NA	NA	NA	NA	NA	4,662.7	2	68	41	82.85
11	5.38	6	5.13	20,361,724	19,415,547	NA	NA	NA	NA	NA	NA	2,273.6	11	112	10	62.34
18	4.86	11	4.65	2,748,399	2,694,703	NA	NA	NA	NA	NA	NA	2,676.2	7	92	28	68.25
16	5.02	12	4.41	13,777,652	12,103,475	NA	NA	NA	NA	NA	NA	540.8	30	125	3	35.15
4	5.91	15	4.19	11,709,984	8,302,002	NA	NA	NA	NA	NA	NA	1,157.8	15	109	12	48.37
35	3.62	42	2.64	1,050,502	766,112	NA	NA	NA	NA	NA	NA	3,131.9	5	83	33	70.77
5	5.87	20	3.91	1,223,425	814,922	(90,049)	195,333	NA	NA	NA	NA	4,376.6	3	44	47	85.08
6	5.75	8	4.81	778,093	650,891	(107,067)	123,349	NA	NA	NA	NA	7,030.9	1	60	43	92.21
23	4.54	36	3.05	4,637,062	3,115,207	(34,874)	151,626	(30,385)	191,133	(4,160)	138,668	389.3	38	105	16	30.5
20	4.78	20	3.91	1,498,136	1,225,462	(54,146)	147,135	(40,340)	113,962	(12,727)	72,936	777.5	19	96	25	47.40
29	3.92	28	3.41	698,614	607,723	(3,830)	29,237	(7,258)	31,069	(2,994)	28,246	1,474.8	13	65	42	66.68
34	3.69	38	3.04	1,086,617	895,207	(49,100)	165,879	(5,197)	152,177	9,389	103,177	448.0	32	97	23	32.47
12	5.34	10	4.66	2,748,667	2,398,649	(29,825)	84,490	(19,730)	68,044	(16,854)	48,488	646.7	24	74	39	41.45
43	3.18	35	3.08	286,099	277,102	(9,054)	12,953	(9,508)	15,783	(10,836)	18,242	571.0	28	90	29	35.46
19	4.83	9	4.68	498,919	483,425	(5,090)	18,051	(2,978)	21,515	(1,435)	15,772	681.8	22	75	38	43.92
8	5.72	4	5.26	4,225,661	3,885,835	(185,180)	266,064	(131,860)	289,826	NA	NA	610.2	26	102	18	38.35
24	4.52	14	4.38	3,095,175	2,999,307	(102,839)	200,857	(86,011)	195,111	(53,912)	151,013	347.2	40	118	6	29.51
3	6.06	2	5.75	2,200,361	2,087,801	(18,566)	39,419	(57,621)	81,225	(93,954)	155,553	733.8	20	52	44	43.55
9	5.48	31	3.21	11,257,431	6,594,225	(42,312)	264,452	(27,975)	252,534	(6,834)	189,845	447.3	33	129	1	34.06
51	2.26	51	1.64	1,400,997	1,016,653	(14,556)	93,306	(3,278)	87,758	972	64,781	286.1	45	125	3	22.70
39	3.47	48	2.17	1,298,387	811,959	(12,506)	60,416	(661)	70,595	2,185	42,018	322.1	44	114	8	25.87
38	3.49	42	2.64	1,192,300	901,912	(40,510)	119,499	(18,612)	140,218	432	107,922	420.2	36	97	23	31.45
10	5.46	1	6.08	2,159,741	2,404,986	(99,930)	170,239	(102,736)	188,545	(92,407)	160,151	680.7	23	103	17	43.47
17	4.98	19	4.03	5,829,848	4,717,729	(134,315)	790,086	(26,203)	831,663	(30,782)	513,037	782.2	18	79	36	44.42
33	3.70	24	3.59	796,278	772,605	(25,355)	103,490	NA	NA	NA	NA	721.1	21	93	27	47.14
26	4.35	27	3.45	2,869,205	2,275,576	(82,014)	233,658	(39,258)	243,234	(30,810)	200,067	424.7	34	106	14	30.75
42	3.31	49	2.04	830,941	512,121	(12,407)	49,431	(1,699)	51,228	3,307	33,476	332.4	41	101	20	25.19
21	4.73	17	4.13	1,000,797	873,846	(49,992)	74,616	(30,839)	84,594	(21,855)	84,892	2,425.8	9	89	31	61.16
37	3.58	32	3.20	4,577,438	4,091,564	(115,748)	128,324	(127,189)	218,235	(109,420)	243,696	933.4	16	110	11	45.26
40	3.41	36	3.05	2,081,812	1,862,032	(43,074)	131,726	(31,826)	177,050	(2,039)	119,935	424.7	34	102	18	32.67
47	2.91	46	2.38	1,046,750	856,105	(25,429)	124,044	(16,217)	146,393	2,270	102,708	563.1	29	100	21	38.14
31	3.88	32	3.20	454,234	374,626	(10,063)	22,312	(8,329)	26,440	(6,163)	20,542	323.5	43	98	22	25.10
36	3.60	24	3.59	2,489,052	2,482,138	(125,106)	270,792	(124,702)	347,994	(51,978)	303,524	531.2	31	114	8	34.32
27	4.21	23	3.60	467,300	399,591	(11,655)	34,790	(9,500)	46,182	(3,355)	36,872	636.6	25	70	40	38.30
49	2.76	50	1.91	1,726,341	1,194,678	(80,918)	135,088	(71,470)	162,911	(27,065)	138,797	414.8	37	117	7	30.70
44	3.17	47	2.34	3,627,812	2,677,943	NA	NA	NA	NA	NA	NA	373.3	39	119	5	26.78
22	4.55	12	4.41	1,939,136	1,879,471	NA	NA	NA	NA	NA	NA			37	48	99.54
50	2.53	45	2.45	274,881	266,189	NA	NA	NA	NA	NA	NA			31	51	99.45
25	4.42	18	4.12	57,225,260	53,341,192	NA	NA	NA	NA	NA	NA			51	45	99.86
41	3.33	30	3.23	3,198,112	3,102,072	NA	NA	NA	NA	NA	NA			46	46	97.84
46	2.93	40	2.84	1,144,948	1,109,779	NA	NA	NA	NA	NA	NA			33	50	99.54
48	2.84	41	2.75	305,752	296,063	NA	NA	NA	NA	NA	NA			34	49	97.54

(Excluding Monopoly States)  
Oregon as a % of Avg

Minimum Maximum Average

286  
7,031  
1,326  
185%

44  
129  
95  
86%

23  
92  
47  
157%

Table D.a.2-2

Premium Weighted Avg. Combined Ratios *	1991	1992	1993	1994	1996
All State Fund States	119.2%	117.6%	93.0%	82.7%	NA
All Non State Fund States	123.3%	118.7%	104.9%	95.9%	NA
State Fund is Market of Last Resort **	120.7%	121.1%	90.2%	81.1%	NA
State Fund is not Market of Last Resort	114.6%	107.5%	104.8%	94.7%	NA
All States	120.8%	118.0%	98.0%	88.2%	NA

\* Does not include monopoly state fund states, since combined ratio data for these states is unavailable.

\*\*The combined ratios for State Fund as the market of last resort treats Maryland and Pennsylvania as non-ARP states.

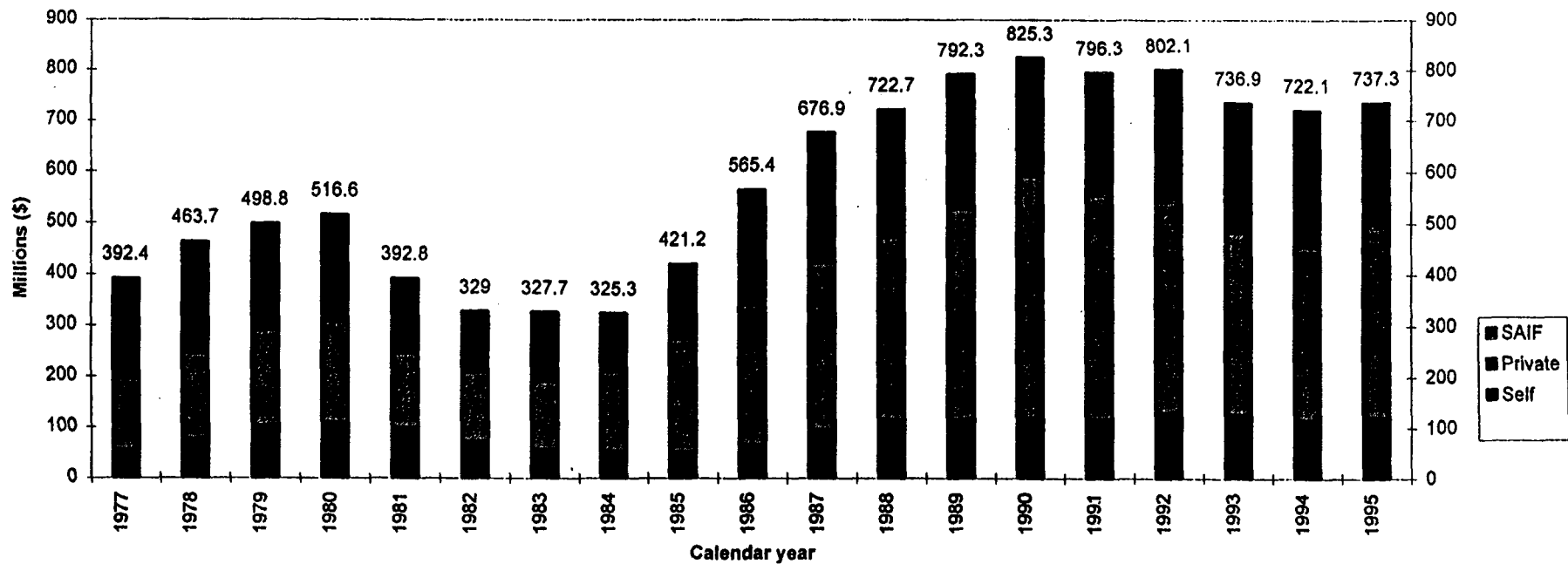
Table D.a.2-3

Premium Weighted Average Premium Rate Index *	1990	1992	1993	1994	1996
All State Fund States	4.94	5.47	NA	5.12	4.52
All Non State Fund States	3.73	4.18	NA	4.25	3.40
State Fund is Market of Last Resort **	4.75	5.46	NA	5.20	4.67
State Fund is not Market of Last Resort	5.49	5.52	NA	4.47	3.38
All States	4.46	4.97	NA	4.76	4.05

\* Does not include monopoly state fund states

\*\*The average premium rate index for State Fund as the market of last resort treats Maryland and Pennsylvania as non-ARP states.

**Chart D.a.3-1**  
**Direct premiums earned and market share by type of insurer, Oregon, 1977-1995\***



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\* Excludes premium assessment. Direct premium earned is shown for self-insurers. Premium total for the file and use transition year of 1982 is estimated.  
 \*\*Includes SAIF Corporation premium adjustment transfer of \$30 million from 1990 to 1989.

**Table D.a.3-2**  
**Direct premiums earned**  
**and market share by type of insurer,**  
**Oregon, 1977-1995**

	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	
Self	14.50	16.90	21.10	21.50	25.60	22.70	17.50	16.60	12.70	11.80	14.40	16.20	14.80	14.60	14.80	16.40	17.31	16.15	16.62	
Private	35.30	36.10	37.30	38.00	37.20	40.80	40.60	48.10	52.40	48.40	48.10	49.10	51.60	57.00	54.80	51.20	48.03	46.77	50.21	
SAIF	50.20	47.00	41.60	40.50	37.20	36.50	41.90	35.30	34.90	39.80	37.50	34.70	33.60	28.40	30.40	32.40	34.67	37.09	33.16	
TOTAL	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	
<b>Premium by Type of Insurer (\$ million):</b>																				
Self	56.898	78.3653	105.2468	111.069	100.5668	74.683	57.3475	53.9998	63.4924	66.7172	97.4736	117.0774	117.2604	120.4938	117.8524	131.5444	127.53663	116.8044	122.5693	
Private	138.5172	167.3957	189.0524	196.308	148.1216	134.232	133.0462	156.4693	220.7088	273.6536	325.6889	354.8457	408.8268	470.421	436.3724	410.6752	353.92307	337.7646	370.2338	
SAIF	198.9848	217.939	207.5008	209.223	146.1216	120.085	137.3063	114.8309	146.9988	225.0292	253.8375	250.7769	266.2128	234.3852	242.0732	259.8804	255.48056	267.7729	244.5044	
	392.4	463.7	498.8	516.6	392.8	329	327.7	325.3	421.2	565.4	676.9	722.7	792.3	825.3	796.3	802.1	736.9	722.1	737.3	
Chk Tol	0	5.684E-14	-5.68E-14	0	-5.7E-14	0	0	0	5.684E-14	0	0	0	0	0	0	0	0	0	0	
* Excludes premium assessment. Direct premium earned is shown for private insurers and SAIF Corporation, estimated simulated net premium is shown for self-insurers. Premium total for the file and use transition year of 1982 is estimated.																				
* Includes SAIF Corporation premium adjustment: transfer of \$30 million from 1990 to 1989.																				
Note: Due to rounding, sum of percents may not equal 100 percent.																				
Source: Private and SAIF Corporation data from Annual Statements filed with the Oregon Department of Consumer and Business Services. Self-insurer data from quarterly Payroll and Assessment Reports to Fiscal Services Section. Data compiled by the Research & Analysis Section, Oregon Department of Consumer and Business Services.																				

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Table D.a.3-3

Summary of Oregon workers' compensation insurance business  
by type of insurer, calendar year 1995  
(excludes workers' compensation premium assessment)  
(\$)

Name of Insurer (Top 30 private Insurers listed by direct premium earned)	Direct premiums written (a)	Direct premiums earned (b)	Dividends paid or credited (c)	Direct unearned premium reserves (d)	Direct losses paid (e)	Direct losses incurred (f)	Direct losses unpaid (g)	Loss ratio ((f/b)*100)	Expense loading factor
1 Liberty Northwest Insurance Corporation	142,559,959	142,566,361	0	1,721,359	104,567,192	126,948,889	392,028,941	89.0	1.202
2 National Union Fire Insurance Company Of Pittsburg	14,202,869	16,629,471	0	6,837,736	5,231,580	4,214,746	20,179,770	25.3	1.488
3 Liberty Mutual Fire Insurance Company	14,433,115	10,823,145	75,309	(3,472,297)	9,475,513	8,042,086	25,806,200	74.3	1.200
4 Employers Insurance Of Wausau, A Mutual Company	10,296,709	10,498,248	372,671	(666,179)	8,362,952	1,814,691	31,737,405	17.3	1.466
5 General Insurance Company Of America	8,802,921	8,675,113	1,080,695	833,699	4,133,293	4,639,872	10,360,220	53.5	1.150
6 Connecticut Indemnity Company (The)	9,395,161	8,466,781	156,228	2,066,605	3,276,006	4,066,677	4,993,908	48.0	1.190
7 Reliance National Indemnity Company	5,574,949	7,600,689	0	(902,682)	2,000,032	1,485,121	9,907,009	19.5	1.500
8 Zurich Insurance Company (Switzerland)	7,327,012	7,469,843	0	315,578	1,256,637	1,939,414	6,165,616	26.0	1.492
9 Industrial Indemnity Company	7,051,050	7,337,463	61,251	1,121,775	3,752,631	2,939,569	18,935,486	40.1	1.465
10 Pacific Employers Insurance Company (Ca)	8,014,557	6,807,167	1,376,942	(2,193,842)	5,331,904	6,402,477	12,156,032	94.1	1.510
11 American Manufacturers Mutual Insurance Company	7,019,245	6,576,984	874,643	1,084,235	2,092,918	171,282	5,098,303	2.6	1.275
12 Grocers Insurance Company	6,168,830	6,168,830	1,973	0	3,739,000	3,583,042	7,032,302	58.1	1.119
13 Argonaut-Southwest Insurance Company (La)	3,496,916	6,137,421	0	(2,215,407)	545,318	1,802,459	2,064,993	29.4	1.075
14 Lumbermens Mutual Casualty Company	5,600,770	5,268,436	1,796,152	2,504,438	2,274,701	81,656	4,429,121	1.5	1.500
15 Travelers Indemnity Company Of Illinois	7,998,377	5,210,145	0	(3,215,970)	2,643,552	13,956,381	20,304,192	267.9	1.518
16 Transportation Insurance Company	4,383,518	4,925,469	2,929,512	(13,605,546)	2,985,431	(1,525,942)	12,189,113	(31.0)	1.270
17 Reliance Insurance Company	3,535,026	4,921,772	278	(487,031)	1,923,179	892,075	5,588,033	18.1	1.190
18 Birmingham Fire Insurance Company Of Pennsylvania	4,780,166	4,761,521	0	1,642,992	2,008,757	1,954,103	5,620,823	41.0	1.488
19 Cigna Insurance Company (Ca)	4,626,717	4,578,385	0	48,629	406,462	3,200,956	2,994,728	69.9	1.472
20 Paula Insurance Company Dba Agri-Comp Insurance	4,637,581	4,526,189	0	111,392	466,243	2,248,235	1,781,992	49.7	1.220
21 Safeco Insurance Company Of America	4,370,180	4,399,011	0	396,430	3,155,241	3,930,955	12,733,648	89.4	1.250
22 Truck Insurance Exchange	4,292,342	4,335,879	36,164	823,418	1,811,539	6,362,708	12,258,543	146.7	1.300
23 Tig Insurance Company	4,673,122	4,060,024	176,255	1,249,937	1,478,917	1,893,773	3,539,725	46.6	1.495
24 American Motorists Insurance Company	4,026,632	3,803,622	915,208	1,301,232	1,973,594	1,894,747	5,558,564	49.8	1.500
25 New Hampshire Insurance Company	4,971,115	3,671,571	0	2,731,502	877,674	2,200,996	2,301,363	59.9	1.150
26 Prudential Property and Casualty Insurance Company	3,723,496	3,585,197	601,216	1,522,521	1,635,737	1,071,459	2,879,918	29.9	1.510
27 Mid-Century Insurance Company	2,240,354	3,201,431	357,218	114,518	3,210,800	2,995,241	9,240,359	93.6	1.150
28 Twin City Fire Insurance Company (In)	2,991,005	3,173,437	297,447	454,770	1,562,118	1,163,668	2,332,857	36.7	1.381
29 Tig Premier Insurance Company	2,168,473	3,009,736	(4,433)	233,836	903,550	1,358,633	1,747,085	45.1	1.170
30 Hartford Underwriters Insurance Company	3,199,276	3,007,153	129	568,791	1,067,300	1,123,223	1,910,616	37.4	1.381
Subtotal of Top 30 Private	316,541,443	316,196,594	11,104,858	926,439	184,199,771	212,853,182	653,876,865	67.3	1.269
Subtotal of All Other Private	61,634,192	54,037,157	1,412,541	11,145,885	44,381,301	39,699,781	224,388,325	73.5	N/A
A. TOTAL, All Private Insurers	378,375,635	370,233,751	12,517,399	12,072,324	228,581,072	252,552,973	878,265,190	68.2	N/A
B. SAIF Corporation	249,347,835	244,504,398	80,188,951	33,657,153	159,607,005	201,575,195	1,377,939,063	82.4	1.206
Subtotal A + B	627,723,470	614,738,149	92,706,350	45,729,477	388,188,077	454,128,168	2,256,204,253	73.9	1.241
C. TOTAL, Self-Insurers	NA	122,569,300	NA	NA	NA	NA	NA	NA	NA
GRAND TOTAL, A + B + C	N/A	737,307,449	N/A	N/A	N/A	N/A	N/A	N/A	N/A

Note: Data from Annual Statements filed by insurance companies is shown for private insurers and SAIF. Data includes assigned risk business. Loss ratios were calculated from columns b and f. Net premium shown for self-insured employers is based on the experience modification rate and, for insurers on Retrospective Plan, estimated at 80% of the Standard Premium. Premium totals shown include Longshore and Harbor Workers Compensation Act, Jones Act, and excess coverage for self-insured employers. Figures may include adjustments for prior years and are subject to future retrospective adjustments. Expense loading factors shown are companies' weighted average factors in effect during 1994. Expense loading factor for SAIF and privates combined is calculated using only the top 30 private insurers. (See narrative for explanation of expense loading factors.) N/A = Not available.

Sources: Annual Statements filed by insurance companies with the Oregon Insurance Division. Data on self-insurers from Quarterly Payroll and Assessment Reports from Oregon self-insurers to the Fiscal Services Section. Data compiled by Research & Analysis Section, Department of Consumer and Business Services.



**Table D.a.3-4  
Assigned Risk Pool  
Oregon, 1985 - 1995**

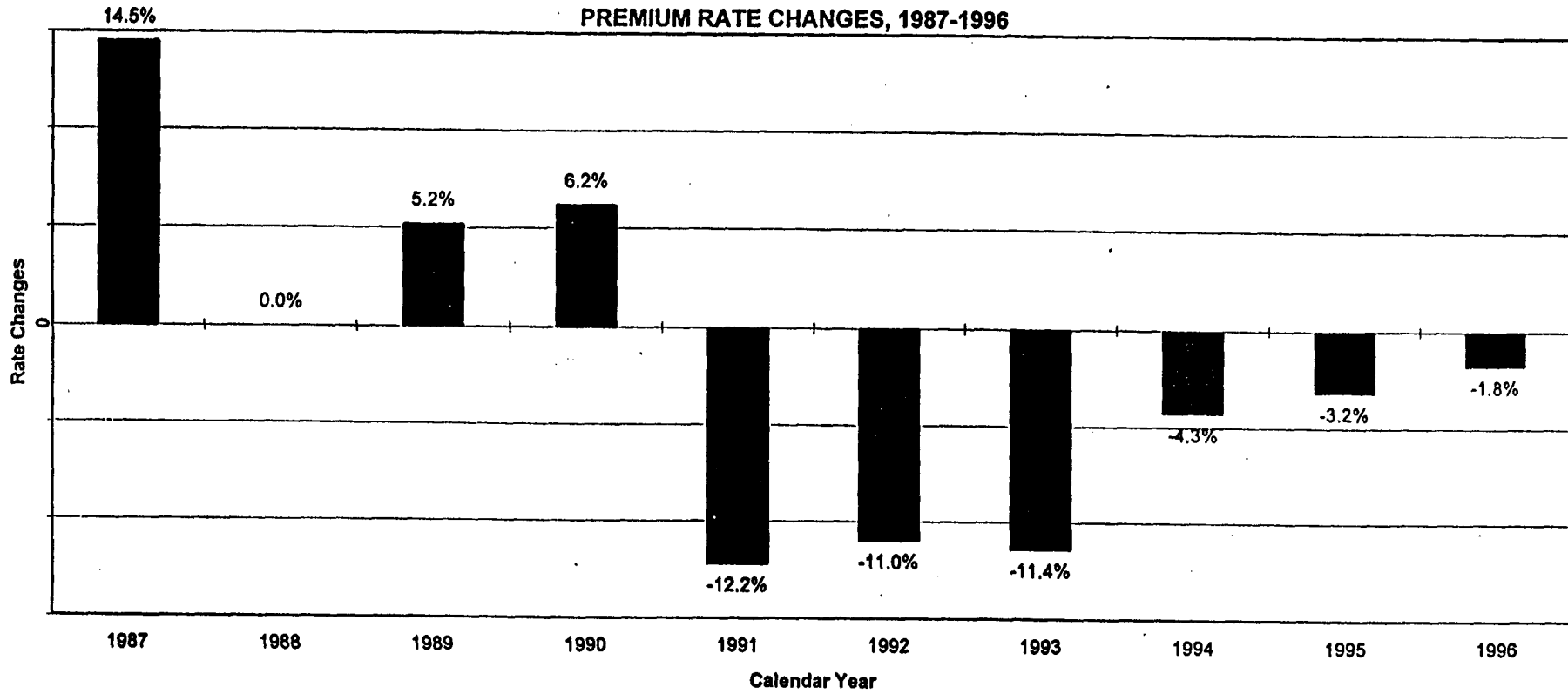
	<u>1985</u>	<u>1986</u>	<u>1987</u>	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>1995</u>
ARP Total Net Premium (millions)	\$7.4	\$18.3	\$19.4	\$20.1	\$28.8	\$71.9	\$71.7	\$50.2	\$48.6	\$53.1	\$49.1
Avg Premium per Employer	\$3,770	\$7,522	\$10,026	\$10,737	\$7,873	\$5,633	\$5,990	\$4,135	\$3,027	\$2,949	\$2,731
ARP Covered Employers	1,963	2,433	1,935	1,872	3,658	12,765	11,970	12,140	16,056	18,008	17,982
ARP as % of Total Premium <sup>1</sup>	2.0%	3.6%	3.4%	3.3%	4.2%	9.8%	11.4%	7.7%	8.0%	8.7%	7.9%
ARP as % of Systemwide Tot. Prem. <sup>2</sup>	1.8%	3.2%	2.9%	2.8%	3.6%	8.7%	9.0%	6.3%	6.6%	7.4%	6.7%

Source: Based on data from Management Summary 1995, "Back to the Future: a Healthy, Stable Market of Last Resort", published by NCCI, 1996.

<sup>1</sup> Total Premium as reported to NCCI does not include estimated self-insurer premium.

<sup>2</sup> Systemwide Total Premium as reported in Oregon's Workers' Compensation Premium Report includes Private Insurers, SAIF, and estimated Self-Insurer premiums for both the voluntary market and the assigned risk pool.

Chart D.b.1-1  
PREMIUM RATE CHANGES, 1987-1996



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**1995 Insurance Market Entrants**

NAIC CODE COMPANY NAME	GROUP NAME	1995	1994
		Direct Premiums Written	Direct Premiums Written
35300 Allianz Ins Co	Allianz Ins Grp	282	-199
16691 Great American Ins Co	American Fncl Ins Grp	182	13
23396 Michigan Mutual Ins Co	Amerisure Companies	173	12
19895 Atlantic Mutual Ins Co	Atlantic Companies	249	70
34649 Business Insurance Company	Calcomp Group	1716	0
22667 Cigna Ins Co	Cigna Group	4627	2
43575 Indemnity Ins Co of North America	Cigna Group	104	0
21105 North River Ins Co	Crum & Forster I C	241	62
21652 Farmers Ins Exchange	Farmers Ins Grp	1646	0
13978 Florists Mutual Ins Co	Florists Mutual	117	87
37478 Hartford Ins Co of the Midwest	Hartford F & C Grp	165	-7
33588 First Liberty Ins Corp	Liberty Mutual Ins Co	145	4
20362 Sumitomo Mar & Fire Ins Co Ltd Us Br	N/A	127	86
32115 Paula Ins Co	Paula Ins Grp	4638	0
24600 Globe Indemnity Co	Royal Grp	139	75
18023 Star Ins Co	Star Ins Grp	111	51
35386 Fidelity & Guaranty Ins Co	Us Fid & Gty Grp	235	0
25879 Fidelity & Guaranty Ins Underwriters	Us Fid & Gty Grp	127	-44

**1995 Insurance Market Exits**

NAIC CODE COMPANY NAME	GROUP NAME	1995	1994
		Direct Premiums Written	Direct Premiums Written
19070 Standard Fire Ins Co	Aetna Life & Casualty	-20	866
21881 National Surety Corp	Allianz Ins Grp	67	260
36463 Northbrook National Ins Co	Allstate Ins Grp	35	249
31089 Republic Western Ins Co	Amerco Corp	-120	554
19399 Aiu Insurance Company	American International Gr	-4	254
19909 Centennial Ins Co	Atlantic Companies	63	165
20699 Cigna Property & Casualty Ins Co	Cigna Group	74	607
22713 Insurance Co of North America	Cigna Group	-505	4219
20850 Firemens Ins Co of Newark Nj	Cna Insurance Group	35	389
11207 Fremont Indemnity Co	Continental Corp	47	570
21113 United States Fire Ins Co	Crum & Forster I C	12	142
11126 Yasuda Fire & Marine Ins Co of Amer	N/A	89	120
12416 Protective Ins Co	Protective Ins Grp	62	295
26247 American Guarantee & Liability Ins	Zurich Amn Ins Cos Grp	66	143
22527 Home Ins Co	Zurich Amn Ins Cos Grp	-3379	2030
19356 Maryland Casualty Co	Zurich Amn Ins Cos Grp	38	126
19372 Northern Ins Co of Ny	Zurich Amn Ins Cos Grp	78	560

**Table E.b.2(a)-1**  
**Quarterly Claims Processing Performance Audit**  
**Yearly Overall Industry Average**  
**Compared to SAIF Corporation and all Other Insurers in the Sample**

YEAR	<u>REPORT OF CLAIM</u>			<u>1ST PMT OF TIMELOSS</u>			<u>SUBMISSION OF 1503</u>			<u>ACCEPTANCE/DENIAL</u>		
	REPORTED	TIMELY	PERCENT TIMELY	REPORTED	TIMELY	PERCENT TIMELY	REPORTED	TIMELY	PERCENT TIMELY	REPORTED	TIMELY	PERCENT TIMELY
<b>1995</b>												
<b>OVERALL</b>	29,979	25,352	<b>85%</b>	25,716	22,683	<b>88%</b>	13,979	11,749	<b>84%</b>	38,089	36,218	<b>95%</b>
<b>SAIF</b>	9,901	8,585	<b>87%</b>	8,085	7,369	<b>91%</b>	2,741	2,440	<b>89%</b>	12,258	11,856	<b>97%</b>
<b>OTHERS</b>	20,078	16,767	<b>84%</b>	17,631	15,314	<b>87%</b>	11,238	9,309	<b>83%</b>	25,831	24,362	<b>94%</b>
<b>1994</b>												
<b>OVERALL</b>	31,507	26,706	<b>85%</b>	27,340	24,106	<b>88%</b>	13,637	11,942	<b>88%</b>	39,510	37,968	<b>96%</b>
<b>SAIF</b>	15,442	13,154	<b>85%</b>	13,183	11,677	<b>89%</b>	5,329	4,785	<b>90%</b>	19,278	18,648	<b>97%</b>
<b>OTHERS</b>	16,065	13,552	<b>84%</b>	14,157	12,429	<b>88%</b>	8,308	7,157	<b>86%</b>	20,232	19,320	<b>95%</b>



EXHIBIT G.a.1  
ARTICLES OF AGREEMENT

Adopted January 1, 1970  
Amended May 20, 1970  
Amended May 19, 1971  
Amended March 2, 1972  
Amended May 18, 1973  
Amended March 7, 1974  
Amended May 15, 1974  
Amended May 21, 1975  
Amended March 29, 1977  
Amended May 20, 1981  
Amended May 19, 1982  
Amended June 15, 1983  
Amended June 20, 1984  
Amended June 19, 1985  
Amended January 1, 1991

Amended July 1, 1992

Reprinted \_\_\_\_\_

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## ARTICLES OF AGREEMENT

Adopted January 1, 1970  
As Amended Effective July 1, 1992

Whereas, the undersigned parties hereto (hereafter also referred to as companies or members), are engaged in the business of insuring against liability under workers compensation acts of the United States of America, of the various states, territories thereof and of the District of Columbia (hereinafter referred to generally as State or States, as the context may require); and

Whereas, policies of workers compensation insurance have been or will be issued by one or more of the companies to certain employers whose risks have been assigned to and accepted by such companies under certain plans (hereinafter referred to as Insurance Plans) in force or to be in force in certain States, the principal purpose of which is to procure insurance which might otherwise be unavailable, with which Insurance Plans and the purposes and scope thereof the said companies are familiar; and

Whereas, it is desired that by the distribution of losses arising out of the risks so assigned or to be assigned undue loss to any one of the companies, parties hereto, may be avoided and that the underwriting results, expenses and administration costs can be accounted for in a cost effective and consistent manner;

Now, therefore, for the purpose of distributing such or any such losses among such companies, and for the protection of each such company from extraordinary hazards incident to the issuance of policies covering such risks, the undersigned companies hereby join in, become parties to, and adopt these Articles of Agreement.

## ARTICLE I

## NAME

Name. The Agreement embodied in these Articles of Agreement may be referred to as the National Workers Compensation Reinsurance Pool ("Pool").

## ARTICLE II

## PURPOSE AND LIMITATIONS

1. Purpose. The Pool is for the purpose of permitting the members to share in the

both administrative costs and the annual fluctuation in assigned risk liability. Risks are assigned by way of the various State Insurance Plans. Carriers appointed pursuant to these Articles (known as "Servicing Carriers") write and service the policies and file reports with the Pool Administrator. Service includes auditing and collection premiums, paying all premium taxes, providing loss control and paying claims.

The members of the Pool enter into Reinsurance Agreements with Servicing Carriers ("Reinsurance Agreements") for the purpose of sharing the experience of these assigned risks. These Reinsurance Agreements distribute risk and define the obligations among the parties. This Agreement facilitates the reinsurance by establishing uniform rules and procedures and providing a framework which permits the members to agree upon such rules and procedures in the future. This Agreement also provides for the appointment of a Pool Administrator by the members for the purpose of administering the terms and conditions of the Agreement.

The Pool is administered by the Pool Administrator. The duties and obligations of the Pool Administrator are established under a separate administration agreement, (herein referred to as "Administration Agreement"). The Pool Administrator, as agent for the members of the Pool, undertakes such services as the apportionment of the operating results of the Pool to each member in a state in proportion to its respective share of workers compensation insurance premiums in such state, providing information to members, settling accounts among members as it further set forth in the Administration Agreement.

2. Limitations. No Insurance Plan for any state shall be brought within the scope of these Articles of Agreement and the rules and procedures adopted hereunder unless all members of the Pool writing workers compensation insurance in such State have subscribed to such Plan, nor until such Plan shall have been specifically approved for inclusion hereunder, as of a stated effective date not prior



the entire membership of the Board of Governors. Thereafter, any proposal to withdraw such Plan shall be submitted to the members of the Pool writing workers compensation insurance in such State. Such Plan shall be withdrawn upon affirmative vote by members writing no less than 51% of the total net workers compensation premiums written by all members during the latest available calendar year in such State.

These Articles of Agreement shall apply only to workers compensation policies including any one or more of the following coverages provided under such policies (or such other policies deemed in compliance with the workers compensation statute of a state);

- (a) Statutory workers compensation and occupational disease including liability under the Longshore and Harbor Workers' Compensation Act as amended and the Federal Coal Mine Health and Safety Act of 1969, as amended.
- (b) Employers Liability.
- (c) Such other coverages as the Board of Governors, by resolution, may authorize.

These Articles of Agreement shall apply to policies issued to employers whose risks have been assigned to and accepted by members of the Pool in accordance herewith, and to become effective on or after 12:01 a.m. of the effective date, as specified by the Board of Governors, of the inclusion within the scope hereof of the Insurance Plan under which such risk is assigned, and, in addition, such workers compensation policies issued to such employers covered in States in which no workers compensation Insurance Plan, voluntary or otherwise, is in effect, as the Board of Governors, by resolution, may authorize.

### ARTICLE III

#### PARTICIPATION

1. Participation. Any company licensed to write workers compensation insurance in any state that has an approved Insurance Plan that embodies these Articles of Agreement may become a participating company by subscribing to these Articles of Agreement. Any State Workers Compensation Insurance Fund established by law also may become a participant by subscribing to

these Articles of Agreement. The Board of Governors may permit participation at its sole discretion to any group, organization, association or other entity it deems appropriate, subject to such entity subscribing to these Articles of Agreement.

A company that elects to become a participating company need not participate in the reinsurance in all states where the Articles of Agreement apply. If, however, a participating company is part of a group or affiliation, its election as to which states it will participate in the reinsurance pursuant to these Articles of Agreement must be the same for all companies affiliated in the group. At the time an Insurance Plan member becomes a participant, it must identify all affiliated companies and notify the Administrator which states it will participate in the reinsurance provided under these Articles of Agreement. Thereafter, any participating company may withdraw from providing reinsurance in any state by giving notice as required in paragraph 2 below subject to the withdrawal of all affiliated companies from such state or states.

2. Withdrawal. Any participating company may withdraw as a participating company with respect to the reinsurance in a given state or states only on December 31 of any year and must give ninety (90) calendar days' advance written notice to the Administrator. Any withdrawal must be made by all companies affiliated within a group.
3. Expulsion. The Board of Governors, by affirmative vote of at least nine members then holding office and eligible to vote, may at any time expel from membership in the Pool any member which in the opinion of the Board shall have violated any of the provisions of these Articles of Agreement or of the Rules forming a part hereof as then constituted or shall have failed to comply therewith. Prior to any such action by the Board, the member shall have the opportunity to present any relevant evidence to the Board concerning any such alleged violation after notice of no less than ten (10) calendar days by the Board which specifies the alleged violation. If, after the member has presented evidence to the Board, the Board determines that a violation has occurred, the Board shall send the member a notice of expulsion by mail, facsimile transmission, or delivery to such member at its latest home office address appearing on the records of the Pool. If the violation is not cured within fifteen (15) calendar

days following the mailing, transmission, or delivery of such notice, the expulsion shall become effective at the end of the fifteen (15) day period. No member of the Board of Governors may vote in a proceeding to expel itself or any of its affiliates.

An appeal to the membership may be made in regard to the action of the Board of Governors with respect to any such expulsion if requested within ten (10) calendar days of the receipt of such notice of expulsion. The only basis upon which such an appeal can lie is that the Board acted arbitrarily and capriciously. No expelled member shall resume membership except with Board approval and upon such conditions as the Board may prescribe.

4. **Obligations After Termination.** Any participating company which terminates participation by withdrawal or by expulsion or has withdrawn from providing reinsurance in a certain state or states shall, nevertheless, with respect to risks subject to these Articles of Agreement prior to midnight of the effective date of such termination or withdrawal, continue to be governed by these Articles of Agreement, the Reinsurance Agreements, and the rules and procedures promulgated thereunder.

5. **Insolvency.**

(a) In the event any participating company shall become insolvent, as hereinafter defined, participation by such company under these Articles of Agreement and the Reinsurance Agreements shall be deemed terminated at the time such company becomes insolvent subject to the further provisions of Section 5(f). As used herein, "insolvent" means being the subject of receivership, conservatorship, rehabilitation, liquidation, or similar proceedings, whether voluntary or involuntary, in any jurisdiction.

(b) In the event a Servicing Carrier becomes insolvent, the Administrator, acting on behalf of each of the participating companies as directed by the Board of Governors, shall have the option to:

(i) pay to the receiver, conservator, rehabilitator, liquidator or other appropriate representative all losses and expenses for which such insolvent Servicing Carrier shall have come

liable upon risks to which these Articles of Agreement apply; or

(ii) subject to the approval of the receiver, conservator, rehabilitator, liquidator or other representative, and subject to the approval of any court having jurisdiction over the proceedings, terminate the obligation of the participating companies to such insolvent Servicing Carrier to reinsure such insolvent Servicing Carrier for losses, costs and expenses for which the insolvent Servicing Carrier shall have become liable upon risks to which these Articles of Agreement apply. If this option is exercised, the Administrator shall make arrangements to have all risks that have been assigned to and are being serviced by such insolvent Servicing Carrier reassigned to another Servicing Carrier for servicing. Such successor Servicing Carrier shall assume all the duties and obligations of the insolvent Servicing Carrier and shall be entitled to the reinsurance provided by the participating companies. Payment made on account of such risks, including expenses for the servicing thereof, shall be apportioned ratably among the remaining participating companies in accordance with the method provided for the apportioning of assessments.

(c) The outstanding liability to the participating companies of any insolvent participant, whether in its capacity as a Servicing Carrier or a participating company or both, and except for the portion unexpended of any amount of premium retained for servicing by such insolvent participating company (if a Servicing Carrier), shall, in event of such insolvency, and subject to any other or further provision with respect thereto which may be from time to time embodied in the rules and procedures adopted hereunder, be assumed by and apportioned among the remaining participating companies in the same manner in which liability for assessments is apportioned. No refund shall be made to such insolvent participating company until all of its liabilities to the participating

participating companies by virtue of the provisions in this section shall have been fully settled and satisfied.

The participating companies shall have all the rights allowed by law against the estate or funds of such insolvent Servicing Carrier for recovery of funds disbursed (including the payment of losses, costs, expenses and unearned Servicing Carrier allowance) to insolvent Servicing Carriers which have been absorbed by the participating companies as herein provided. The Administrator may assert and enforce such rights on behalf of the remaining participating companies.

Upon the insolvency of a Servicing Carrier, all amounts due to such insolvent Servicing Carrier from the participating companies as a result of the reinsurance provided to such Servicing Carrier and all amounts due from the insolvent Servicing Carrier as a participating company to other Servicing Carriers it reinsures shall be merged into one account and deemed mutual debts and credits which solvent participating companies and Servicing Carriers may offset.

- (d) Any participating company that fails or has failed to make timely payment of its reinsurance obligations or any assessment made under these Articles of Agreement shall become immediately liable as of the earliest date on which such failure to pay occurs, for all current assessments and reinsurance obligations and an additional amount equal to the commuted value on such date of all outstanding reinsurance obligations that such participating company may have. For the purposes hereof, such commuted value shall total the amount of unearned premium reserves and loss reserves then allocated to such participating company hereunder, as determined by the Administrator and approved by the Board of Governors. The liability of the insolvent participating company for such commuted value under this provision shall be deemed fixed, liquidated, and non-contingent as of the date of such failure to pay. The Administrator may assert and enforce such liability on behalf of the participating companies.

- (e) The Board of Governors shall have the discretion to terminate participation of any or all affiliated companies of the insolvent participating company. The termination of an insolvent participating company or any or all companies described in this section shall not be deemed a violation of the requirement contained in Article III, Section 1 relating to all insurers in a group becoming participating companies. A decision to terminate an affiliate of an insolvent participating company is reviewable under the applicable Insurance Plans.

- (f) Anything in this Section to the contrary notwithstanding, the Board of Governors may, in the event such action is in its judgment feasible and desirable, and in a manner equitable to all participating companies, elect not to terminate the participation of such insolvent participating company, and permit such participating company to continue its participation under these Articles of Agreement upon such conditions as it may prescribe and subject in all respects to these Articles of Agreement and the rules and procedures hereunder as then constituted.

- (g) No member of the Board of Governors that is either an insolvent participating company or affiliate thereof may vote in any proceeding under this Section.

6. **Member Obligations.** Any or all member companies shall, at the discretion of the Board of Governors, be required to periodically provide, at intervals to be determined by the Board of Governors, information on the ability to pay return premiums, losses and expenses which may be assessed pursuant to Article XI, Section 7 for all risks which are subject to these Articles of Agreement. Member companies shall provide all further information necessary for the Board of Governors to determine a company's ability to pay its obligations to the Pool members, and for the Board of Governors to determine if there is any significant likelihood that the company's reserves are not adequate to meet its obligations to the Pool members, or that there is a significant likelihood that future reserves will be inadequate to meet future obligations, or should the Board of Governors determine that the member company has not cooperated to the extent necessary to make these

determinations, the Board of Governors shall have the authority to ensure that the member company has reserves adequate to protect the other members of the Pool by taking actions which may include, but need not be limited to, any or all of the following:

- (a) Ordering that all premium distributions or refunds due the member company be paid into escrow or trust with the Pool Administrator to secure the member's obligations.
- (b) Ordering that all premium distributions or refunds due the member company be paid in trust with a third party to secure the member's obligations.
- (c) Order that the member company obtain a letter of credit approved by the Board of Governors to secure the company's future liabilities.

Compliance with any such order within the time specified therein shall be an obligation of membership.

#### ARTICLE IV

##### MEETINGS AND VOTING RIGHTS

1. **Regular Meetings.** The participating companies shall meet annually on the third Wednesday of June, or on such other date as the Board of Governors may determine, and at such place as the Board of Governors may determine.
2. **Special Meetings.** Special meetings of the participating companies may be called at any time by the Chair of the Board of Governors and shall be called by the Chair upon the written request of three (3) non-affiliated participating companies.
3. **Notice of Meetings.** Except as otherwise provided in Article IX, notice of all annual and special meetings shall be given or caused to be given by the Chair, in writing, mailed or delivered to, or by facsimile transmission direct to, each participating company at the latest address appearing upon the records of the Administrator, or by telephone communication to any executive officer of such participating company. If notice is given by writing and mailed to the participating company, such notice shall be placed in the mail not less than ten (10)

calendar days prior to the date of the meeting. If given by facsimile transmission or telephone communication, it shall be so given not less than five (5) calendar days prior to the meeting.

4. **Quorum.** A quorum at any annual or special meeting shall consist of participating companies that write not less than 50.1% of the total net workers compensation premiums written by all participating companies during the latest calendar year for which information is available in all states where these Articles of Agreement are operative. For purposes of determining a quorum and any vote taken hereunder, the net workers compensation premium written for each participating company shall only include those states where such participating company is providing reinsurance under these Articles.
5. **Powers.** The purpose of any special meeting shall be stated in the notice thereof; but at all such meetings and at annual meetings, participating companies may consider and act upon all matters brought before them, except where otherwise specifically provided in these Articles of Agreement.
6. **Voting Rights.** Except where otherwise provided in these Articles of Agreement, at all meetings action may be taken only upon affirmative vote of participating companies that write not less than 50.1% of the total net workers compensation premiums written by all participating companies during the latest calendar year for which information is available in all States where these Articles of Agreement are operative. If such meeting is limited to matters involving one State by the terms of the notice of meeting, no action may be taken unless there has been an affirmative vote of participating companies which that not less than 50.1% of the total net workers compensation premiums written by all participating companies providing reinsurance in such State during the latest calendar year for which information is available in such State. Action may also be taken without meeting by mail or telephone upon affirmative vote of participating companies which write not less than 50.1% of the total net workers compensation premiums written by all participating companies during the latest calendar year for which information is available in all States where these Articles of Agreement are operative provided that all participating companies are polled.

7. **Proxies and Mail Votes.** Participating companies may be represented at any meeting by proxy. Participating companies may record their votes by mail on written propositions, and such votes shall have the same standing as if cast by such participating companies in person or by proxy.
8. **Minutes of Meetings.** Minutes of all meetings of the participating companies and of the Board of Governors shall be recorded by the Administrator and provided to all participating companies.
2. **Conditions.** The Board may fix the conditions upon which assigned risks may be afforded coverage beyond that required by the applicable Insurance Plans, and the conditions upon which claims shall be handled by Servicing Carriers. All risks shall be insured by Servicing Carriers and all claims on risks shall be handled by Servicing Carriers in accordance with such conditions.
3. **Vacancies.** A vacancy occurring in the Board of Governors shall be filled by vote of the members of the class of companies on the Board in which the vacancy occurs. Such election shall be for the unexpired term of the replaced member.

## ARTICLE V

### BOARD OF GOVERNORS

1. **Number and Term of Office.** The operation, business and affairs of the Agreement shall be managed and controlled by a Board of Governors composed of twelve (12) members of the Pool and the chief executive officer of the Pool Administrator, who shall serve as an ex-officio member without vote.
 

The Board shall be elected by the membership at the annual meetings of the members of the Pool. Board elections shall be made for staggered terms. Four (4) members shall be elected annually for a term of three (3) years. No member for a full term shall succeed itself, except:

  - (a) Due to an inability to satisfy the required minimum on the Board of 30% from the stock and non-stock classes of members; or
  - (b) Where a sufficient number of non-succeeding companies cannot be induced to serve on the Board.
5. **Quorum and Voting Rights.** A majority of the Board of Governors shall constitute a quorum. Each member of the Board shall be entitled to one vote. A member's vote may be cast only by its representative, or in his or her absence, by its alternate. Proxy voting shall not be permitted. Any Board action requires that there be at least one affirmative vote of a stock insurer and one affirmative vote of a non-stock insurer. If such votes are not cast, the matter fails adoption except as provided for elsewhere in these Articles of Agreement. In the absence of a quorum, the Board, subject, however, to the provisions of Section 3 of the Article relative to filling vacancies on the Board, shall have no power except that a majority of the members in attendance may adjourn the meeting from time to time until a quorum shall attend. Action may also be taken without meeting by mail or telephone upon affirmative vote of a majority of the members, provided that all members of the Board are polled and no member demands a meeting.

In the event of a tie vote, the matter fails adoption.

The Board of Governors shall have a mixture of members from the non-stock class and from the stock class with a minimum participation of 30% from each class. The non-stock class shall consist of capital stock companies and corporations. No more than eight (8) of the twelve (12) members of the Board of Governors shall be Servicing Carriers.

Each Board membership shall be in the name of the member company. All members elected to the Board shall designate knowledgeable representatives of suitable senior standing and may select two (2) alternates of similar standing

6. **Meetings.** The Board shall meet within thirty (30) calendar days next following the annual election of the Board for the purpose of electing officers to serve for the next ensuing year and for the transaction of all other business within the powers of the Board. Other regular meetings of the Board of Governors shall be held at such places and on such dates as the Board may from time to time determine. Special meetings of the Board may be called at any time by the Chair and shall be called by him

- or her upon written request of three (3) non-affiliated members of the Pool. Such notice of regular and special meetings of the Board shall be given as may be determined by the Board or, in the event the period of notice shall not have been prescribed, as the Chair shall deem reasonable.
7. **Organization and Procedure.** The members of the Board of Governors shall elect a Chair and Vice-Chair from among their number. The Chairship and Vice-Chairship of the Board shall be rotated annually as between the non-stock and the stock class members. The Chair, or in his or her absence the Vice-Chair, or in the absence of both, a Chair pro-tem elected by the members present, shall act as a Chair of every meeting of the Board; and the General Manager-Secretary, or in his or her absence a person appointed by the Chair, shall act as a Secretary of the meeting and shall keep a record of its proceedings. The order of business at all meetings of the Board shall be determined by the Chair. If any member of the Board of Governors is absent from the meeting of the Board, such absent member, or the member of the Pool that he or she represents, may designate in writing any other member of the Board to act, but not to vote, in the place and stead of such absent member at such meeting.
8. **Disputes and Appeals.** In addition to the powers elsewhere conferred upon it by these Articles of Agreement the Board of Governors shall constitute a committee with full authority to pass upon all disputes arising with respect to these Articles of Agreement, including without limitation any questions as to the application, scope and effect of these Articles of Agreement; and the ruling of a majority of the Board as then constituted on any such dispute or question following reasonable notice and an opportunity for a hearing shall be final, unless within thirty (30) calendar days after notice of such ruling is mailed to the membership, except in the case of expulsion, three (3) non-affiliated members of the Pool shall in writing request the Board of Governors to submit such ruling to a special meeting of the members of the Pool. Such request shall specify the ruling appealed from, and such special meeting shall be called by the Chair for a date not later than forty-five (45) calendar days from the date of said ruling. The action of the special meeting of the members of the Pool so called, upon such ruling, shall be final.
9. **Servicing Carriers.** The Board of Governors may select one or more members of the Pool to act as Servicing Carriers, subject to qualifications and such other conditions as may be established by the Board of Governors.
10. **Audit and Inspections.** The Board of Governors shall have the right, in person or through representatives, at all reasonable times during the business day, to audit and inspect the books and records of any Servicing Carrier with respect to any policy or policies and claims thereunder coming within the purview of these Articles of Agreement.
11. **Rules and Procedures.** The Board of Governors shall have the right to promulgate and adopt rules and procedures for the purpose of implementing the terms of this Agreement.
12. **Authority of Pool Administrator.** The Pool Administrator is authorized to enter into agreements on behalf of the members of the Pool to carry out the purposes of this Agreement, including but not limited to reinsurance agreements. Upon direction by the Board of Governors, the Pool Administrator is empowered to act as attorney-in-fact for each member of the Pool to prosecute, to defend, to submit to arbitration, to settle and to propose or to accept a compromise with respect to, any claim existing in favor of, or against, such member based on or involving any matter relating to this Agreement or to intervene in any action or proceeding related thereto.

## ARTICLE VI

### OFFICERS AND COMMITTEES

*Former Sections 1-4 and 7-15 repealed*

5. **Chair.** The Chair shall be chief executive officer of the Pool and shall have overall control of and responsibility for all activities subject to this Agreement and other powers incidental to the office.
6. **Vice-Chairs.** The Vice-Chairs shall have immediate charge, subject to the direction and control of the Chair, of such matters as may be assigned to them respectively by the Chair. In the Chair's absence or inability for any reason to act as the Chair, his or her executive duties and powers in the management of the Pool may, with

like effect, be performed and exercised by the Executive Vice-Chair or, if the latter also be absent or unable to act, by any of the Vice-Chairs.

16. Other Committees. The Chair may from time to time appoint such other committees, with such duties and subject to such rules, not inconsistent herewith, as the chair may deem desirable.

#### ARTICLE VII

##### FISCAL MATTERS

1. Fiscal Year. The fiscal year for the purpose of administering this Agreement shall be the calendar year unless otherwise established by the Board of Governors.
2. Deposits. Funds held temporarily for the benefit of members by the Pool Administrator, with the approval of the Board of Governors, may be kept on deposit in such banks, trust companies or other depositories as may from time to time be designated and prescribed by the resolution of the Board of Governors; and such designation shall be evidenced by an instrument signed by the Chair or the Vice-Chair, and countersigned by the General Manager-Secretary or the Treasurer. Accurate records shall be kept to identify the funds so deposited.
3. Withdrawals. Any two (2) of the officers of the Pool duly authorized by the Board of Governors shall have power to sign and countersign all checks, drafts or other orders for payment of money and to cause the endorsement of all commercial paper payable under this Agreement, or to delegate such authority to the Pool Administrator.
4. Special Accounts. Funds temporarily held for the benefit of members also may be kept on deposit with any authorized depository, but in a special account designated as such, subject to withdrawal upon check signed by any two (2) of the officers of the Pool duly authorized by the Board of Governors if authorized by, and subject to, the terms and conditions contained in a written instrument signed by any two (2) of the officers of the Pool authorized by the Board of Governors. Accurate records shall be kept to identify the funds so deposited. This authority may be delegated to the Pool Administrator.

5. Safe Deposit. Access may be had to any safe deposit box, hired vault, or like place of safekeeping, standing in the name of the Pool, by the General Manager-Secretary or the Treasurer, when accompanied by the Chair or any Vice-Chair. This authority may be delegated to the Pool Administrator.
6. Investment Income. All income on the funds held for the benefit of members of the Pool shall, upon receipt thereof, become subject to all the appropriate provisions to this Agreement.

#### ARTICLE VIII

##### INDEMNIFICATION

1. Indemnification. Any person or insurer made, or threatened to be made, a party to any action, suit or proceeding, because such person or insurer was a member, or a Servicing Carrier, or served as a member or representative of a member of the Board of Governors or other committee, or was an officer or employee of the Pool or of the Pool Administrator acting on behalf of the Pool shall be indemnified against all judgments, fines, amounts paid in settlement, reasonable costs and expenses including attorney's fees, and any other liabilities that may be incurred as a result of such action, suit or proceeding, or threatened action, suit or proceeding, except in relation to matters as to which he, she or it shall be adjudged in such action, suit or proceeding to be liable by reason of willful misconduct in the performance of his, her or its duties or obligations to the Pool and, with respect to any criminal actions or proceedings, except when such person or insurer had reasonable cause to believe that his, her or its conduct was unlawful. Such indemnification shall be provided whether or not such person or insurer is a member, or a Servicing Carrier, or is holding office, or is employed at the time of such action, suit or proceeding, and whether or not any such liability is incurred prior to the adoption of this Article. Such indemnification shall not be exclusive of other rights such person or insurer may have, and shall pass to the successors, heirs, executors or administrators of such person or insurer. The termination of any such civil or criminal action, suit or proceeding by judgment, settlement, conviction or upon a plea of nolo contendere, or its equivalent, shall not in itself create a presumption that any such person or insurer was liable by reason of willful

cause to believe that his, her or its conduct was unlawful. If any such action, suit or proceeding is compromised, it must be with the approval of the Board of Governors of the Pool; provided, however, the Board of Governors of the Pool may delegate to the General Manager-Secretary of the Pool the authority to approve any such compromise of financial liability requiring payment by the Pool which is less than an amount as may be fixed from time to time by the Board of Governors of the Pool.

2. In each instance in which a question of indemnification arises, entitlement thereto, pursuant to the conditions set forth in Section 1 of this Article, shall be determined by the Board of Governors which shall also determine the time and manner of payment of such indemnification; provided, however, that a person or insurer who or which has been wholly successful, on the merits or otherwise, in the defense of a civil or criminal action, suit or proceeding of the character described in Section 1 of this Article shall be entitled to indemnification as authorized in such section. The Board of Governors of the Pool may delegate to the General Manager-Secretary of the Pool the authority to determine, in a manner consistent with this Article, entitlement to indemnification, and the time and manner of payment of such indemnification, for any indemnification requiring payment by the Pool which is less than an amount as may be fixed from time to time by the Board of Governors of the Pool. Nothing herein shall be deemed to bind a person or insurer who or which the Board of Governors has determined not to be entitled to indemnification, or to preclude such person or insurer from asserting the right to such indemnification by legal proceedings. Such indemnification as is herein provided shall be apportioned among all members, including any named in any such action, suit or proceeding pursuant to Article XI of the Articles of Agreement.

#### ARTICLE IX

#### AMENDMENTS

Amendments. Any and all provisions of these Articles of Agreement and any amendments hereto shall be subject to amendment, alteration, repeal or re-enactment at any annual meeting of the members of the Pool, or at any special meeting called for the purpose, by the affirmative vote of two-thirds (2/3) of

the members present at such meeting and such members shall write not less than 50.1% of the total net workers compensation premiums written by all members during the latest available calendar year for which information is available in all states where the Pool is operative. Not less than fifteen (15) calendar days' written notice of any such meeting shall be given, or caused to be given, by the Chair, in which notice the action proposed to be taken shall be fully set forth.

#### ARTICLE X

#### EFFECTIVE DATE

Effective Date. These Articles of Agreement shall become effective upon signature and applicable to the signatory for any state where an Insurance Plan is operative so long as members writing not less than 85% of the total net workers compensation insurance premiums written by all companies have subscribed.

#### ARTICLE XI

#### ASSESSMENTS AND EXPENSES

1. Application. This Article shall apply to all risks processed under any Insurance Plan subject to these Articles of Agreement.
2. Assignment of Risks. A member of the Pool which is providing insurance on a risk assigned to it under an Insurance Plan shall be referred to herein as a Servicing Carrier.

The Pool shall endeavor to consummate arrangements with the Administrators of all Insurance Plans subject to these Articles of Agreement, whereby such Administrators will equitably reassign to a Servicing Carrier those risks which, in the normal course of the Insurance Plans' operation, would have been assigned to a member not a Servicing Carrier. To that end the Pool Administrator, when the Articles of Agreement shall have become effective, shall advise the Administrators of such Insurance Plans of the fact and shall furnish such Administrators a complete roster of the Pool membership and Servicing Carriers (which roster shall be corrected from time to time to reflect changes in membership and Servicing Carriers). If such arrangements cannot be consummated with an Administrator of an Insurance Plan, the Board of Governors at their discretion may make other appropriate arrangements with the



Administrator to effectuate these Articles of Agreement.

Any Servicing Carrier to which a risk has been assigned by the Administrator of any Insurance Plan shall (subject to the further provisions hereof) continue as the Servicing Carrier as provided in the applicable Reinsurance Agreement.

3. **Premiums.** The Pool Administrator shall distribute the premiums received from Servicing Carriers to the members of the Pool in proportion to their workers compensation premiums written in each state on a calendar year basis, or as otherwise determined by the Board of Governors.
4. **Expenses and Payments.** Expenses incurred by the Pool in the administration of the affairs subject to these Articles of Agreement, and not allocable directly to any assigned risk, shall be a proper charge against, and shall be paid from, the general funds held on behalf of the members of the Pool. A record shall be kept of all such expenses, and the amount thereof shall be apportioned to the members of the Pool in the ratio of their interest in such funds, and when at the discretion of the Board of Governors, deemed necessary, shall be included in any assessment levied under Section 6 of this Article. Except with respect to claims, the cost of the interpretation of physical and X-ray examinations of employees in assigned dust hazard risks, provided the employer pays for the making of such examinations, shall be a proper charge against, and shall be paid from, the general funds held on behalf of the members of the Pool. Except as the Board of Governors shall otherwise direct:
  - (a) payments to or in behalf of members shall be limited to administration expenses, reimbursement for losses paid under policies to which these Articles apply, and for return premiums on such policies and the payment of such refunds as may be allowed under these Articles of Agreement;
  - (b) except for costs of premium collection as provided in the Reinsurance Agreement, the Pool shall not assume for payment, and shall not be liable to pay, any expenses of any nature whatsoever incurred by members;

5. **Transactions, Accounts and Financial Statements.** Separate accounts shall be maintained by the Pool Administrator covering transactions for each policy year in each state. The Pool Administrator shall prepare and deliver to the members a financial statement showing the apportionment of the expense of administration provided for herein and the condition of each account.
6. **Assessments and Refunds.** Assessments shall be levied or refunds allowed by the Board of Governors as they may from time to time deem reasonable and necessary. Except as otherwise determined by the Board, assessments or refunds for account of a specified policy year and State shall be levied upon or allowed to all members who were such during the calendar year corresponding to such policy year, and each member shall pay such proportion of such assessment, and shall receive a proportionate share of such refund, as is determined by the relation which the net workers compensation insurance premiums, written in such State during such calendar year by such member, shall bear to the total net workers compensation insurance premiums written in such State during such calendar year by all members.

The amount of net workers compensation premiums written, which shall serve as the basis of all computations in this Section or elsewhere in the Articles of Agreement and the rules and procedures hereunder, and in the applicable Reinsurance Agreement, shall be that shown by the records of the Pool Administrator. If the amount of net workers compensation premiums written for a specified calendar year is not available at the time of the levying of any assessment or the distribution of any refund, net premiums written for the preceding calendar year shall be used as the basis for a preliminary assessment or refund, but such preliminary assessment or refund shall be adjusted as soon as the new premiums written for the specified calendar become available.

The amount of any assessment levied shall be paid within, and the amount of any refund allowed shall be distributed within, such time following the submission of the quarterly, or other statement referred to herein, as may be determined at their sound discretion by the Board of Governors.

Anything in this Article to the contrary notwithstanding, a carrier becoming a member as of an effective date other than January 1 shall, during its first calendar year of membership, participate in the Pool, with respect to assessments and refunds, on a prorated basis the ratio of which recognizes the number of months as a member in relationship to the 12 month period.

When levying assessments, due consideration shall be given to membership by any members of the Pool in any other similar workers compensation reinsurance pool in a particular state or states.

7. **Distribution Upon Termination of the Pool.** Upon termination of the Pool in any State, distribution by way of refund (if any) shall be made to the members of the Pool in such state entitled to participate therein, subject to provisions of Section 6 of Article III of the Articles of Agreement, within such reasonable period of time as the Board of Governors at its sound discretion shall determine; and all provisions of these Articles of Agreement and the rules and procedures adopted hereunder relative to administration of the Pool shall remain in full force and effect until final distribution shall have been made.

## ARTICLE XII

### DEFINITIONS AND RULES OF CONSTRUCTION

1. **Construction.** Wherever in the Articles of Agreement there appear such phrases as "subject to the further provisions hereof" or "as herein provided" or "as limited herein," or phrases or words of like or similar import, references is thereby intended to be made to such provisions or limitations wherever appearing in the Articles of Agreement, and not merely to those appearing only in the Section in which such phrase or word is used, unless a contrary intent is expressly indicated.

The terms "net premiums written," "net workers compensation insurance premiums written," "workers compensation premiums written" and "workers compensation insurance premiums," wherever used in these Articles of Agreement, shall mean the gross direct premiums charged less all premiums (except dividends and savings refunded under participating policies) returned

to policyholders for all Workers Compensation and Occupational Disease Insurance, exclusive of premiums for risks subject to these Articles of Agreement, and for risks written under Special National Defense Comprehensive Rating or Special National Defense Premium Discount Plans and under excess policies.

"Insurance Plans" of "State Plans" wherever used herein shall include any insurance program organized to write Workers Compensation and Employers Liability when it is not otherwise available in the voluntary market by members of the Pool subject to these Articles of Agreement.

A member of the Pool referred to herein as a "Servicing Carrier" shall include any member company servicing coverage written by such member company servicing coverage written by such member and subject to these Articles of Agreement.

The terms "affiliate" or "affiliated," whenever used herein, refer to companies controlling, controlled by, or under common control with other companies.

The term "Workers Compensation" and the word "Workers" wherever used within these Articles of Agreement means Workers or Workmen's as applicable.

2. **Workers Compensation Insurance Premium.** The term "Workers Compensation Insurance premium" shall also include all premium received by non-admitted carriers on policies issued by such carriers for coverage in any state where such policies are deemed to meet employer obligations under the workers compensation statutes of such state.

## ARTICLE XIII

### ACCEPTANCE OF ARTICLES OF AGREEMENT BY MEMBERS

THE ARTICLES OF AGREEMENT may be simultaneously executed by the subscribing members in any number of counterparts, written or printed or both, and each counterpart so executed shall be deemed to be an original and all such counterparts shall constitute one and the same document.

IN WITNESS WHEREOF the undersigned have respectively caused their corporate names to be

Vice-President and their corporate seals to be hereto  
affixed, attested by a duly authorized officer.

\_\_\_\_\_  
Company

By: \_\_\_\_\_

Title: \_\_\_\_\_

Attest: \_\_\_\_\_

SEAL

Date Subscribed:

\_\_\_\_\_

## EXHIBIT G.a.2

## SERVICING CARRIER AGREEMENT

THIS AGREEMENT is made and entered into effective as of the \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, by and between the National Council on Compensation Insurance, acting in its capacity as Administrator of the \_\_\_\_\_ Workers Compensation Insurance Plan (hereinafter the "Plan Administrator") and \_\_\_\_\_ (hereinafter the "Servicing Carrier").

WHEREAS, The Plan Administrator is authorized by the provisions of the Workers Compensation Insurance Plan ("WCIP") to appoint Servicing Carriers; and

WHEREAS, The Plan Administrator wishes to contract with the Servicing Carrier for the purpose of providing workers compensation insurance to risks, which coverage is reinsured pursuant to the Articles of Agreement; and

WHEREAS, The Servicing Carrier is willing to accept such contract and to provide full workers compensation insurance services, including coverage, underwriting, claims, loss control, auditing, supervision of litigation and other defense duties, and other services, subject to the terms and conditions hereinafter specified.

NOW, THEREFORE, In consideration of the mutual promises contained hereinafter, the Plan Administrator and the Servicing Carrier agree as follows:

## I. TERM

This agreement shall become effective on the day and year first above written and shall continue in force until such time as it may be amended or terminated pursuant to the provisions hereinbelow set forth.

## II. POWER AND DUTIES OF SERVICING CARRIER

The Servicing Carrier shall make available such of its own staff, office space, facilities and equipment as are necessary for the performance of its duties. The Servicing Carrier shall perform its services, exercise its powers, and perform all of its duties in accordance with the attached Servicing Carrier Performance Standards, which are incorporated herein, and as from time to time amended by the Plan Administrator.

The Servicing Carrier shall process, adjust, settle, compromise, defend, litigate and pay covered compensable loss claims arising out of or in connection with all claims reinsured by the Pool, including with respect thereto, the unlimited right to hire and discharge attorneys and to hire independent adjusters in those circumstances in which the use of adjusters regularly employed by the Servicing Carrier is imprudent or impractical as determined solely by the Servicing Carrier. The Servicing Carrier shall establish and maintain reported claim reserves in accordance with the Quota Share Reinsurance Agreement. It shall also maintain complete, orderly and accurate claim files, records and accounts in accordance with generally accepted insurance principles and as directed by the Plan Administrator.

The Servicing Carrier shall comply with all reporting requirements and procedures required by the Plan Administrator.

The Servicing Carrier shall file quarterly reports of premiums written, losses paid and known outstanding losses with the Pool on a quarterly basis in accord with such procedures and format as established by the Plan Administrator.

All reporting requirements and procedures contained in the "Servicing Carrier Reference Book", and/or as may be hereinafter amended, are applicable and incorporated herein by reference.

The Servicing Carrier may act generally in its capacity as a Servicing Carrier under the Plan to bring and defend lawsuits in the ordinary course of business unless otherwise instructed by the Plan Administrator.

The Servicing Carrier shall remain in compliance with all servicing carrier eligibility criteria during the term of this contract, and shall abide by such servicing carrier performance standards as may be established from time to time by the Plan Administrator.

The Servicing Carrier shall receive as compensation an allowance as established by the Plan Administrator and in accordance with the WCIP, which may be amended in writing from time to time by the Plan Administrator, at its discretion. The Servicing Carrier also agrees that its compensation may be increased or decreased pursuant to the application of such performance based incentive/disincentive programs as the Plan Administrator may from time to time adopt.

### III. POWERS AND DUTIES OF THE PLAN ADMINISTRATOR

The Plan Administrator shall have the right at all reasonable time to inspect the books, records and files of the Servicing Carrier so far as they pertain to the operations of the Plan, and shall have the right to copy or abstract such books, records and files at its expense.

If an additional claims examination is deemed necessary by the Plan Administrator as a result of advice received from a general audit or examination, such audit or examination shall also be performed at its expense. However, the Servicing Carrier shall bear all expenses of any state insurance department audit or examination.

### IV. STATUS OF PARTIES

Nothing contained herein shall be deemed to create the relationship of employer and employee between the Plan Administrator and the Servicing Carrier. It is understood and agreed that the Servicing Carrier is an independent contractor whose rights and obligations are established by this agreement. Employees of the Servicing Carrier are not employees of the Plan Administrator. Such employees shall at all times be under the sole direction and control of the Servicing Carrier.

V. NOTICE

Whenever written notice is required to be given under any provision of this Agreement, such notice shall be sufficient if sent by certified mail, return receipt requested, to the following addresses:

(a) Plan Administrator The National Council on Compensation Insurance  
750 Park of Commerce Drive  
Boca Raton, Florida 33487  
  
Attention: William F. Vieweg

(b) Servicing Carrier \_\_\_\_\_  
Name of Officer \_\_\_\_\_  
Home Office Address \_\_\_\_\_  
\_\_\_\_\_

VI. AMENDMENT

This Agreement may be modified, altered or amended only by a writing signed by an authorized representative of the Servicing Carrier and of the Plan Administrator.

This writing constitutes the entire agreement of the parties and no agent or employee of either party has authority to change this agreement or to waive any of its provisions except as otherwise expressly provided herein.

VII. TERMINATION

This Agreement may be terminated at any time by mutual agreement between the Plan Administrator and the Servicing Carrier.

Either party may terminate this Agreement without cause by giving notice to the other party at least ninety (90) days prior to the end of the then current fiscal year of the Pool stating that this Agreement shall terminate as of midnight on December 31, of the same year. If the Plan Administrator determines that the Servicing Carrier is not in compliance with any provision of this Agreement, it shall notify the Servicing Carrier of such non-compliance, and shall set a time period for the Servicing Carrier to bring itself into compliance. If the Plan Administrator determines, in its discretion, that the Servicing Carrier has failed to bring itself into compliance within the specified time, it shall have the right to immediately terminate this Agreement by notifying the Servicing Carrier as to the date of such termination. Notwithstanding the foregoing, non-compliance based upon the Servicing Carrier's failure to meet such performance standards as may be established in accordance

with the Plan shall be remedied pursuant to the provisions of the Remediation Program, a copy of which is attached hereto.

#### VIII. CHANGE IN LAW

If changes in any state or federal law, governmental agency rule or regulation, or the by-laws, rules or regulations, procedural handbook or performance standards established pursuant to the Plan increase substantially the Service Carrier's cost of servicing claims, the Servicing Carrier may terminate this Agreement by giving notice to the Plan Administrator within a reasonable period of time after being notified of such changes. Such termination shall be effective as of midnight on December 31 of the same year in which notification was given, or at an earlier date upon mutual agreement.

#### IX. ACTIONS UPON TERMINATION

- A. Except as provided in B. below the Servicing Carrier, promptly upon termination of this Agreement, but no later than 30 calendar days after notice, shall deliver the following to any person or organization designated in writing by the Plan Administrator: all policy records or copies thereof, claim files, reports and other documents relating to claim files and accounting and statistical reports or any other records required to be maintained pursuant to the Articles, or maintained relating to the Policies.
- B. Upon termination, the Plan Administrator will have the option of requiring the Servicing Carrier to retain and handle all servicing and claims arising under the Policies. If the Plan Administrator elects such option, the Servicing Carrier shall be responsible for the expense of adjusting to conclusion without further expense reimbursement all such claims except for those loss adjustment expenses not covered by the servicing carrier allowance provided for in Article X below, but normally reimbursed to Servicing Carriers pursuant to the Articles.

If the Administrator elects said option, the Servicing Carrier will handle all such servicing and claims in accordance with the terms of this Agreement until the claims have been terminated or assigned to the Reinsurers or some third party under mutually agreed upon terms.

#### X. WAIVER

The failure or delay of any party at any time to require performance by another party of any provision of this Agreement shall not affect the right of such party at a later date to require performance of such provision or to exercise any right, power, or remedy provided for hereunder. The waiver by any party of any breach of any provision of this Agreement shall not be construed as continuing or as a bar to or waiver of any right or remedy as to any subsequent event. No notice to or demand on any party, in any case, shall of itself entitle such party to any other or further notice or demand in similar or other circumstances.

Appendix H

STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF TARGET FINANCIAL EXAMINATION

OF

STATE ACCIDENT INSURANCE FUND CORPORATION  
SALEM, OREGON

NAIC COMPANY CODE 36196

AS OF

DECEMBER 31, 1995





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August 8, 1996

Honorable Kerry Barnett, Director  
Department of Consumer and Business Services  
State of Oregon  
350 Winter Street NE, Room 440-4  
Salem, Oregon 97310

Dear Director:

In accordance with your instructions and pursuant to ORS 731.300, we have examined the business affairs and financial condition of

**State Accident Insurance Fund Corporation**  
**400 High Street SE**  
**Salem, Oregon 97312**

**NAIC Company Code 36196**

hereinafter referred to as "SAIF" or the "Company." The following report is respectfully submitted.

**SCOPE OF EXAMINATION**

The purpose of this examination is to conduct a target examination pursuant to the requirements of B-Engrossed House Bill 2033 (HB 2033). The target examination is part of a study of the financial and other related regulatory status of the State Accident Insurance Fund Corporation.

The target examination involved a limited review of the financial condition for the 2 years ended December 31, 1995. This examination focused on the certain lines reported in the 1995 Annual Statement. The annual statement lines examined are indicated on the financial statements included as part of this report. The limited scope financial examination also involved a review of: general internal controls, information systems internal controls, reinsurance, pension plans and corporate records.

The target examination was conducted pursuant to the provisions of ORS 731.300 and in accordance with procedures and guidelines prescribed by the National Association of Insurance Commissioners (NAIC) for the purpose of determining the Company's financial condition, ability to fulfill and the manner of fulfillment of its obligations, the nature of its operations, and compliance with the Insurance Code. Accounting methods, internal control procedures, records, and other supporting evidence were examined or tested by appropriate methods to the extent deemed necessary and appropriate for the type, volume, and complexity of the accounting system and operations utilized by the Company. The record testing included, but was not limited to, assets, liabilities, income, and expense related items.

In conjunction with this target financial examination, a target market conduct examination was performed by insurance examiners from the Department of Consumer and Business Services, State of Oregon. A separate report was issued for the target market conduct examination of the Company.

The Oregon Department of Consumer and Business Services contracted with the actuarial firm of Richard E. Sherman & Associates (Sherman) to evaluate the Company's losses, loss adjustment expenses, rating, and a portion of dividends. The results of their analyses are found under the relevant sections and appendices in this report.

### COMPANY HISTORY

The State Accident Insurance Fund Corporation was created as an independent public corporation by passage of Senate Bill 255 in 1979. By this enactment, SAIF is the successor to the State Accident Insurance Fund (the Fund), which was created for the purpose of transacting workers' compensation business formerly transacted by the State Industrial Accident Commission. The latter operated as the exclusive state workers' compensation agency from 1914 through 1965.

Passage of ORS 731.028 made SAIF a domestic insurer subject to limited provisions of the Oregon Insurance Code covering rate filings, accounting methods, annual statement filings and examinations.

Passage of Senate Bill 255 in 1979 converted the Fund to its present structure as an independent public corporation governed by a board of 5 directors appointed by the Governor. This bill exempted SAIF from a number of statutes which control the administration and fiscal activities of state agencies, and made SAIF subject to limited Insurance Code provisions.

In 1982 the Legislature amended ORS 656.526 and 656.634 to permit the State of Oregon to direct legislatively the disposition of SAIF's surplus in excess of reserves and surplus deemed actuarially necessary according to recognized insurance principles. The Oregon Legislature directed the State Treasurer to transfer \$81,000,000 from the Industrial Accident Fund to the General Fund of the State of Oregon on June 3, 1983.

Effective January 1, 1989, the Company merged its subsidiaries, SAIF Corporation of Oregon and Loggers' Assurance Company, into its own operations.

On November 18, 1993, the Supreme Court of the State of Oregon handed down an opinion (Alsea Veneer, Inc. v. State of Oregon case) which indicated that the expropriation of \$81,000,000 from SAIF in June 1983, by the State of Oregon, was inappropriate. The Supreme Court ruled that the State of Oregon must repay the \$81,000,000, with interest, to SAIF. During 1994, the State of Oregon made a first installment of \$5 million and an additional payment of \$60 million in 1995 to SAIF. On February 26, 1996, the Marion County District Court approved a settlement agreement which calls for the State of Oregon to pay an additional \$160 million to the plaintiffs and SAIF.

### MANAGEMENT AND CONTROL

#### Board of Directors

SAIF is governed by a 5 member Board of Directors appointed by the Governor and subject to confirmation by the Oregon Senate. Directors are appointed to 4 year terms, but serve at the pleasure of the Governor. Two members of the Board are chosen to represent the public and, of the 3 remaining members, 1 must be a contributing employer at the time of appointment and for 1 year prior to appointment, or an employee of such an employer.

Members of the Board of Directors, duly appointed and serving as of December 31, 1995, were:

<u>Name and Address</u>	<u>Principal Affiliation</u>	<u>Director Since</u>
William D. Thorndike, Jr.* 2875 David Lane Medford, OR 97504	President, Medford Fabrication	7/01/94
Jon A. Egge PO Box 393 Clackamas, OR 97015	Owner, MP Plumbing	9/11/95
Marjorie M. Cross 1704 NW First Street Bend, OR 97701	Self-employed broker/dealer of collector cars	4/19/93
Howard M. Shapiro 2621 NW Cornell Road Portland, OR 97210	Non-profit business consultant	9/18/93
Gregory A. Teeple 11402 SE Flavel Portland, OR 97266	Labor Representative	1/23/93

\*Chairman of the Board of Directors

### Officers

Operating management of SAIF as of December 31, 1995, was under the direction of the following principal officers:

<u>Name</u>	<u>Office</u>
Katherine L. Keene	President and Chief Executive Officer
Brian M. Steffel	Senior Vice President of Operations
Corlet Graff	Vice President, Claims Operations
Charles E. Graham	Vice President of Policyholder Service
Harlan Jones	Vice President of Legal Affairs
Pamela Jordan	Vice President of Information System
J. David Thurber	Vice President of Personnel Service
Cecil Tibbetts	Vice President of External Affairs



MANAGEMENT AFFIRMATION

To the Attention of Patrick Huth, CFE, Examiner-In-Charge for the Oregon Insurance Division in connection with the examination of the State Accident Insurance Fund Corporation, for the period of January 1, 1994 to December 31, 1995.

Pursuant to the provisions of ORS 731.300 and 731.308 and to the best of my knowledge and belief, I, William D. Thorndike, do hereby certify for the period covered by this examination that:

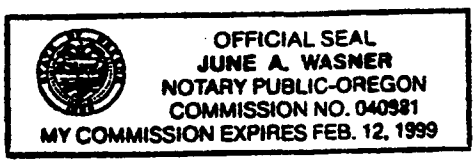
- the transactions and business affairs of State Accident Insurance Fund Corporation are conducted in compliance with the [applicable] statutes, rules and procedures of the Oregon Insurance Division;
- for the period under review, all operations of the Company were conducted in such a manner as not to be hazardous to the insurance buying public or in violation of the [applicable provisions of the] Oregon Insurance Code;
- all books, records, accounts, papers, documents and computer and other recordings in the Company's possession and relating to its assets, accounts, transactions and affairs, to its treatment of policyholders, compliance with the Insurance Code, and to all matters relating to the period under examination, are kept in accordance with ORS 733.170 and have been made available to the examiners in their entirety pursuant to ORS 731.308; and
- all corporate powers are exercised by or under the authority of the duly qualified and constituted Board of Directors of the Company and the business affairs and transactions of the Company are managed under the direction of such Board of Directors, all in accordance with the duties and responsibilities conferred upon the Board of Directors by the Articles of Incorporation\*, Bylaws, and Oregon Law.

Dated this 7 day of June 1996.

William D. Thorndike  
William D. Thorndike - Chairman of the Board

Subscribed and sworn before me this 7<sup>th</sup> day of June 1996.

June A. Wasner  
Notary Public in and for the State of Oregon



[\*Note that, as a creation of statute, State Accident Insurance Fund Corporation has no Articles of Incorporation.]

**CONFLICT OF INTEREST**

The Company has an established policy for disclosure of any material interest or affiliation on the part of any of its directors, officers and key employees which is in, or is likely to, conflict with official duties. Officers and key employees are required to sign a conflict interest statement annually. However, each director is only required to sign a conflict of interest statement upon appointment by the Governor. No exceptions were noted in a review of such forms for the period under the examination.

**CORPORATE RECORDS****Board Minutes**

Minutes of the Board of Directors meetings were reviewed for the period under examination. Meetings were held in accordance with the Company's Bylaws and a quorum was achieved at all meetings. The minutes supported the transactions of the Company and the actions taken by its officers.

**Bylaws**

There were no amendments to the Bylaws for the period under examination.

**Holding Company Registration**

The Company is not required to file a holding Company registration with the Oregon Insurance Division.

**Statutory Deposit**

The Company is not required to maintain a deposit with the Oregon Insurance Division, Department of Consumer and Business Services.

**FIDELITY BONDS AND OTHER INSURANCE**

The Company is insured up to \$20,000,000 per occurrence, with \$250,000 deductible, against losses from acts of dishonesty and fraud by its employees, under "the Oregon State Public Employees Dishonesty Bond" coverage. Fidelity bond coverage was found to exceed the minimum coverage recommended by the NAIC.

All other insurance coverages, provided by the State of Oregon are as follows:

- Commercial general liability
- Automobile liability
- Fire

The Company insures its own employees for workers' compensation.

The above coverages were found to be adequate as of December 31, 1995.

**PENSION PLANS AND OTHER POST-RETIREMENT BENEFITS**

The Company employees participate in the Oregon Public Employee's Retirement System (PERS), which includes a cost sharing, multiple employer, defined benefit public employee retirement system for state agencies. All SAIF employees are eligible to participate in the system after completing 6 months of service. The covered employees are required by state statutes to contribute 6% of their salary to the system. SAIF's employee contributions are paid for by the employer. The Company is required by statute to contribute actuarially computed amounts as determined by PERS.

The Company does not provide any other post-retirement benefits (other than pension) to its employees.

**DIVIDENDS TO POLICYHOLDERS**

The Company's Board of Directors approved the payment of policyholder dividends during the prior 3 year period as follows:

1993 - \$32,672,940  
1994 - \$29,666,666  
1995 - \$80,188,951

Sherman reviewed every dividend declaration for these years (1993 to 1995) and did not find any instances in which those declarations did not comply with the provisions of Oregon Administrative Rule (OAR) 836-80-140. This administrative rule prohibits an insurer from discrimination in the allocation of dividends and permits dividends to be based on a percentage of premiums with variations for risk size, risk location, and industry type. SAIF, in accordance with OAR 836-80-140, bases its dividends on product line, premium size, and loss ratio. SAIF does not utilize industry type or geographic location to determine dividends.

In addition to the requirements of OAR 836-80-140, Sherman noted:

We have reviewed all of the key steps taken by SAIF management in determining the level of its total dividend distributions and are of the opinion that those decisions were reasonable and appropriate.

**TERRITORY AND PLAN OF OPERATION**

The Company transacts workers' compensation and surety insurance only in the State of Oregon. SAIF is not required to hold a Certificate of Authority to write workers' compensation insurance. Also, the Company was originally issued a Certificate of Authority to write surety insurance as it relates to self-insured employers. The Company has written no surety insurance in the past several years. Based upon a previous examination recommendation the Company surrendered this Certificate of Authority effective July 1994.

The Company offers workers' compensation coverage under distinct rate tiers based on an employer's loss experience. These rate classes are select, preferred, standard, and non-standard. Rates are composed of a base rate, determined by the National Council on Compensation Insurance (NCCI) and approved by the Department of Consumer and Business Services, and then multiplied by a risk factor determined by SAIF. If an employer is unable to obtain a coverage from SAIF or another insurer, then the employer must obtain coverage through the State of Oregon's Workers' Compensation Insurance Plan (WCIP). The Company participates as a servicing carrier of the WCIP residual market and pays its proportionate share of pool losses in excess of pooled premiums.

In addition to different rate classes, the Company offers various forms of premium payment plans under premium calculation methods such as the standard and retrospective plans. Under the standard plan, coverage is provided for a fixed premium paid on a monthly, quarterly, or yearly basis.

SAIF's retrospective premium plans (Retro) are generally offered to larger employers. For Retros, premiums are determined on a retrospective basis, based on the employer's actual loss experience. The Retro premiums are subject to maximum and minimum amounts. An employer's losses are evaluated at fixed periods following the end of a policy period.

Risks with premiums of \$2,500 or less are placed through AOI Compwise (AOI), a division of SAIF. AOI is located in a Portland office where it maintains policy records on a separate computer system.

#### **GROWTH OF THE COMPANY**

The following exhibit reflects the growth of the Company since 1986. The stated amounts were compiled from copies of the Company's filed annual statements and, where indicated, from the previous examination reports.

<u>Year</u>	<u>Assets</u>	<u>Liabilities</u>	<u>Surplus as regards Policyholders</u>	<u>Net Income</u>
1986	\$1,098,439,688	\$1,053,593,248	\$ 44,846,440	\$ (6,633,483)
1987*	1,202,619,477	1,170,614,184	32,005,293	8,348,683
1988	1,334,132,479	1,180,786,390	153,346,089	(49,911,101)
1989	1,441,649,785	1,297,310,307	144,339,478	(10,373,335)
1990*	1,495,925,705	1,283,253,165	212,672,540	110,407,052
1991	1,585,689,046	1,257,291,143	328,397,903	87,868,939
1992	1,710,660,435	1,332,273,731	378,386,704	261,792,729
1993*	1,906,126,545	1,477,655,997	428,470,548	(26,642,691)
1994	2,006,828,916	1,532,072,616	474,756,300	73,578,081
1995	2,117,052,335	1,687,124,647	429,927,688	(8,516,524)

\*Per examination

### LOSS EXPERIENCE

The following exhibit reflects the annual underwriting results of the Company since 1988. The amounts were compiled from copies of the Company's filed annual statements and, where indicated, from the previous examination reports.

#### Income Statement - Loss Ratios On A Calendar Year Basis

<u>Year</u>	(1) <u>Premium Earned</u>	(2) <u>Loss and Loss Adjustment Expenses</u>	(2/1) <u>Ratio</u>
1988	\$247,521,792	\$367,654,578	148.53%
1989	230,101,194	305,348,334	132.70
1990*	250,278,708	191,677,439	76.59
1991	220,629,138	206,060,496	93.40
1992	242,667,330	40,176,385	16.56
1993*	243,116,851	326,664,491	134.37
1994	273,996,168	238,686,201	87.11
1995	250,560,246	257,430,279	102.74

\*Per examination

The chart shown above indicates a loss ratio of 16.56% for 1992. This resulted from the fact that significant changes were made to loss reserves during 1992. One of the changes in loss reserves had come from the downward development of prior year reserves. On a discounted basis, the downward development of prior year reserves was approximately \$225 million (88% of 1992 surplus). As a result, instead of reporting

incurred losses and loss adjustment expense of approximately \$265 million, the Company reported incurred losses and loss adjustment expenses of \$40.2 million in the income statement. This explains the low losses and loss adjustment expenses reported for 1992 and the resultant increase in net income.

Before 1992, loss reserves had been discounted at a rate of 3.5% on medical accounts. The Company opted to eliminate this discount on medical reserves in 1992. The change in discounting on medical reserves was treated as a change in accounting principal. Therefore, the cumulative increase of \$236,392,434 million (88% of 1992 surplus) in reserves were recorded as a direct reduction to surplus. The net effect of these 2 transactions reduced surplus approximately \$11,392,434.

A ratio of 134.37% in 1993 resulted from the fact that the Company opted to reduce the discount rate from 7% to 4% on fatal and permanent total disability claims and discontinued discounting all other indemnity claims previously discounted at 7%. The effect of this change in discounting increased losses and loss adjustment expenses by approximately \$125.7 million.

### **REINSURANCE**

The Company's reinsurance coverages are obtained through a reinsurance broker, Aon Re, Inc.

#### **Per Occurrence Excess of Loss**

Per Occurrence Excess of Loss reinsurance is provided through 2 reinsurance contracts with 7 layers of coverage. The limits and retentions for the Per Occurrence contracts are as follows:

<u>Treaty Layer</u>	<u>Limit</u>	<u>Retention or Underlying Limit</u>
First	75% of \$3,000,000 per occurrence 75% of \$1,000,000 per occurrence (employers liability)	\$2,000,000
Second	\$5,000,000 per occurrence with an aggregate limit of \$10,000,000.	\$5,000,000
Third	\$20,000,000 per occurrence with an aggregate limit of \$40,000,000.	\$10,000,00
Fourth	\$20,000,000 per occurrence with an aggregate limit of \$40,000,000.	\$30,000,000
Fifth	\$25,000,000 per occurrence with an aggregate limit of \$50,000,000.	\$50,000,000
Sixth	\$25,000,000 per occurrence with an aggregate limit of \$50,000,000.	\$75,000,000
Seventh	\$50,000,000 per occurrence with an aggregate limit of \$100,000,000.	\$100,000,000

#### Per Claimant Excess of Loss

The Company's excess of loss layers are supplemented by per claimant coverage for losses that exceed \$2,000,000 up to \$10,000,000 per claimant. The retentions and limits per treaty layer are as follows:

<u>Treaty Layer</u>	<u>Limit</u>	<u>Retention or Underlying Limit</u>
First	60% of \$3,000,000 per occurrence with an aggregate limit of \$10,000,000.	\$2,000,000
Second	\$5,000,000 per occurrence with an aggregate limit of \$10,000,000.	\$5,000,000

#### Regulatory Limitations Pertaining to Reinsurance

Under the provisions of ORS 731.028, the Company is not subject to the Oregon Revised Statutes relevant to reinsurance which include:



731.504	Limit of risk
731.508	Approved reinsurance
731.509	Criteria for allowing credit for reinsurance
731.510	Criteria for allowing reduction from liability for reinsurance.
731.511	Criteria to be met by assuming insurer in order to be accredited as reinsurer.
731.512	Withdrawal of insurer.
731.516	Mortgage insurance limitation.

Although the Company is not subject to these reinsurance statutes, its reinsurance practices are consistent with the provisions of these statutes in the areas of risk retention and insolvency clause.

### **Risk Retention**

The Company's retention on its policies is \$2,000,000 per individual (per claimant) risk. Reinsurance covers the next \$10,000,000 of risk per claimant. The Company does not retain risk on any one subject in excess of 10% of its surplus to policyholders.

### **Insolvency Clauses**

All reinsurance agreements contained Insolvency Clauses which specified payments would be made to a statutory successor without diminution in the event of an insolvency.

### **Unlicensed Reinsurers**

For a 1 month period covering January 1, 1995, to January 31, 1995, the Company's Per Claimant Excess of Loss and Per Occurrence Excess of Loss agreements contained participating reinsurance companies that were not licensed to transact the business of workers compensation in the State of Oregon. The provisions of ORS 731.508(1) prohibit an insurer from accepting risks of which it is not authorized to insure. However, effective February 1, 1995, these agreements were terminated. On this same date, the Company entered into new agreements, providing the same coverage, in

which all participating reinsurers were authorized to transact the business of workers compensation in the State of Oregon.

### **LIMITATIONS ON THE STATUTORY REGULATION OF SAIF**

Under ORS 731.028, the Company is not subject to many Insurance Code requirements, to which other insurers are subject. By way of example, SAIF is not subject to several of the provisions which limit insurer investments, such as the limitations ordinarily imposed on investments in mortgage loans (ORS 733.600), real property (ORS 733.610), stocks of corporations (ORS 733.620), stocks or obligations of subsidiaries (ORS 733.630), data processing systems (ORS 733.660), non-investment grade securities (733.695), and many other such items. SAIF is exempt from the "prudent investor" and prohibited investments standards. See ORS 733.670; 733.780. SAIF is not legally empowered to control its own investments or investment decisions. SAIF's investments are subject to the control of the Oregon State Treasurer. See ORS 293.701 through 293.820.

Additionally, in the event of an impairment or insolvency, SAIF is not subject to the statutory requirements of minimum required capital or surplus (ORS 731.554), or supervision, rehabilitation or liquidation. See ORS 734.043; 734.150; 734.170. Ordinarily, the claims of an insolvent workers' compensation insurer are protected by the Oregon Insurance Guaranty Association. See ORS 734.550. These provisions are not applicable to SAIF. See ORS 731.028.

Certain rating practices do not apply to SAIF. See ORS 737.230 (data must include certain information). Many trade practice requirements also do not cover SAIF. See for example ORS 746.035 (inducements); 746.045 (rebates); 746.120 (illegal dealing in premiums); 746.160 (practices injurious to free competition).

Because of these, and many other nonapplicable sections of the Insurance Code, this report of examination is limited in its scope. The lack of comment in a variety of areas

should not be read as approval or acquiescence with the practices of the Company. These, and other areas, simply were not examined or commented upon.

One difference affecting underwriting results and financial condition between SAIF and the remainder of the Oregon insurance industry is SAIF's ability to discount its loss reserves. [This is according to a Letter of Advice to Theodore R. Kulongoski (OP-6176), dated May 25, 1988 by the Department of Justice].

Under statutory accounting principles, all workers' compensation insurers are permitted to discount "tabular" reserves. See ORS 656.636. This is limited to the "indemnity portion" of fatal and permanent total disability claims after a final determination or settlement has been reached. The discount on tabular reserves is calculated by using an assumed interest rate and the use of mortality tables to determine the present value of estimated future indemnity payments to permanently disabled workers or to the survivors of deceased workers. The amount of reserves required for these claims is generally a small segment of the total required reserves for all unpaid losses and loss adjustment expenses. The total required reserves included all known or "reported" losses and loss adjustment expenses (LAE) plus an additional amount for "incurred but not reported" (IBNR) for both losses and LAE. Based on each company's historical experience, the IBNR portion is the estimated amount of losses, as of the financial statement date, that have actually been incurred at that point in time but will not be reported to the company until after that date.

SAIF assumes an interest rate of 4% to calculate its tabular discount while the Insurance Division permits all other workers' compensation carriers to use a rate of only 3.5%. A larger interest rate results in a larger discount and ultimately a smaller

reported reserve. This difference is roughly estimated to be \$12,300,000 as of December 31, 1995.

SAIF also calculates a discount on both the tabular reserves estimated in its provision for IBNR and for its reported claims that are estimated to become fatal or permanent total disability cases but which have not yet reached final determination or settlement. No other workers' compensation insurers are permitted to do this. This difference was \$55,835,000 as of December 31, 1995.

The Company began discounting all reserves for losses and LAE in 1989 under the provisions contained in OP-6176. Of the total \$633,605,000 discount reported for 1989, \$126,739,000 was attributable to tabular reserves and would have been permitted by other workers' compensation insurers. The remaining balance of \$506,866,000 would not have been permitted by other workers' compensation insurers. SAIF reported total 1989 reserves for losses and LAE in the amount of \$1,168,055,016 which was 69.7% of the amount that would have been required for other insurers. Subsequently, the amount of discount has diminished each year and currently SAIF reported total 1995 reserves for losses and LAE in the amount of \$1,526,642,289 which was \$68,135,000 ( $\$12,300,000 + 55,835,000$ ) less than or 95.7% of the amount required for all other workers' compensation insurers.

Appendix A attached (from Sherman's report) displays the extent and magnitude of SAIF's historical discounting practices on required reserves for losses and LAE.

#### **OTHER REQUIREMENTS APPLICABLE TO SAIF**

The Company is subject to several other requirements which are not applicable to other insurers. Some of these differences include: SAIF's Board of Directors is appointed by the Governor, SAIF's investment officer is the Oregon State Treasurer, SAIF's auditor is the Secretary of State, SAIF's legal firm is the Department of Justice, and SAIF must

insure state agencies. In addition, the meetings of SAIF's governing body are subject to public meeting rules (see ORS 192.630(1)), and its records, excepting employer account records and claimant files, shall be open to public inspection (see ORS 656.702).

### ACCOUNTS AND RECORDS

In general, the Company's records and source documentation supported the amounts presented in the December 31, 1995, annual statement and were maintained in a manner by which the financial condition was readily verifiable as required by ORS 733.170. No material exceptions were noted from a review of the Company's internal controls. In addition, the Company filed the required report for unclaimed property to the State of Oregon in accordance with the requirements of ORS 98.352 to 98.436.

### Losses and Loss Adjustment Expenses

The loss reserves and loss adjustment expense reserves, as reported in the December 31, 1995 annual statement, were determined by Sherman to be near the upper end of his range of reasonable actuarial estimates. A portion of his comments are as follows:

The following table presents a comparison of our estimates with the loss and LAE reserves carried by SAIF as of December 31, 1995:

<u>Reserve Component</u>	(000's omitted) <u>Carried by SAIF</u>	<u>Per Examination</u>	<u>Redundancy (+) or Deficiency (-)</u>
Total loss & LAE	\$1,517,486	\$1,376,008	\$141,478

Although the above comparison indicates a redundancy of \$141.5 million in SAIF's total loss and LAE reserves, we are not recommending that SAIF take down its reserves by that amount. In our opinion, the range of variability around our best estimate is on the order of \$200 million plus or minus our total indication. As noted in the immediately preceding section of this report, there are an unusual number of reasons why there is a high level of uncertainty regarding the ultimate value of loss and LAE reserves as of 12/31/95. In our opinion, it would not be inappropriate for SAIF to continue to maintain reserves at a similar margin above our best estimate. Again, such a continuation would be the result of recognizing the possible magnitude of variations which could easily occur around our best estimate.

### Real Estate

SAIF's real estate holdings are comprised solely of properties used to conduct its business operations. Appendix B reflects the history of the Company's real estate portfolio.

### Rating Plans

Sherman reviewed SAIF's rating plans and programs (excluding assigned risk accounts) with particular attention to differences related to premium size, geographic location, or industry. In addition, Sherman examined whether employers are assigned to rating tiers and rating group programs, according to their approved filed rating plans.

Sherman's examination revealed the Company generally distributes risks among various rating tiers using objective criteria such as experience rating, expected loss ratio, premium size, eligibility for experience rating, and/or eligibility for a claim rating plan. It was noted that small risks tend to end up in higher rating tiers while large risks end up in lower rating tiers. Sherman's comments in regard to this finding are as follows:

It could be argued that this is appropriate because of the greater expenses associated with the underwriting and servicing of small accounts. It could also be argued that this is appropriate because small risks might have worse loss experience.

In addition, Sherman sampled 50 policy files to determine if each account was in the appropriate rate tier based on SAIF's underwriting criteria. In 2 files there was no documentation to support the underwriting decision. In one case there was a question whether the account was still entitled to group rating. In the other, the underwriting decision to keep the account in the 1.15 rate tier when it appeared to be eligible only for

the 1.30 rate tier was not documented. These files represent 4% of the selected audit sample and 96% passed the audit criteria. In view of this observation, I recommend the Company establish procedures to assure documentation of underwriting decisions that have resulted in assignment to an alternative rate tier. Documentation should be uniform and used consistently by all underwriters. This recommendation is made pursuant to the provisions of ORS 733.170.

### Deferred Premium

An examination of the Company's uncollected premium accounts, as of December 31, 1995, determined the Company collects premiums in accordance with the provisions of ORS 656.504. With respect to uncollected premiums, the examiners noted the following:

- Premiums in collection are due directly from the insured employers. At the end of each month the employer fills out the payroll report for all the covered employees for the month just ended. This report along with the applicable premium is due into SAIF's offices by the 15th of the following month. For a limited number of policies, quarterly payments are applicable, in which case the premium due is payable on the 15th of the month following the quarter just ended. No exceptions were noted in which certain employers were given favorable treatment with respect to the cited payment terms.
- The Company maintains reports for premiums over and under 90 days. Those over 90 days are properly nonadmitted. Premiums over 90 days due at year end, as a proportion of premiums in the course of collection, grew dramatically from 1990 through 1992. This trend reversed in 1993 and has continued to improve through 1995.

**FINANCIAL STATEMENTS**

The limited scope of this target financial examination involved a review of only select annual statement accounts primarily limited to premium accounts, dividends, and loss reserves. These examined items are denoted on the following financial statements by an asterisk. In addition to the DCBS examination, the Oregon Secretary of State, Division of Audits, conducted a statutory audit of the Company's financial statements as of December 31, 1995. The results of their audit was the issuance of a "clean" opinion. Based on this opinion and the fact that no significant adjustments were made to the majority of the accounts previously examined, the balances reported in the December 31, 1995 annual statement have been accepted for purposes of this target financial examination.



**STATE ACCIDENT INSURANCE FUND CORPORATION**  
**STATEMENT OF ASSETS, LIABILITIES, SURPLUS & OTHER FUNDS**  
**As of December 31, 1995**

<u>ASSETS</u>	<u>Ledger Assets</u>	<u>Nonadmitted/ Non-ledger Assets</u>	<u>Net Admitted Assets</u>
Bonds	\$1,541,452,544	\$ (2,664,662)	\$1,538,787,882
Preferred stock	46,941,742	1,828,153	48,769,894
Common stock	61,072,902	24,713,245	85,786,147
Mortgage loan	9,722,988		9,722,988
Real estate*	25,768,686		25,768,686
Cash	20,809,922		20,809,922
Other invested assets	18,833,194	(1,506,000)	17,327,194
Premiums and agents balances in the course of collection*	12,057,690	(3,860,031)	8,197,659
Premiums, agents balances deferred and not yet due*	176,304,520	(5,148,415)	171,156,106
Accrued retrospective premiums*	46,759,265	(4,675,927)	42,083,338
Reinsurance recoverable	418,010		418,010
EDP equipment*	4,838,110	(352,762)	4,485,349
Interest & investment income due and accrued	31,410,610		31,410,610
Equities and deposits in pools and associations	719,088		719,088
Equipment and furniture	2,152,875	(2,152,875)	0
Aggregate write-ins for other than invested assets	<u>115,530,721</u>	<u>(3,921,258)</u>	<u>111,609,463</u>
<b>TOTAL ASSETS</b>	<b><u>\$2,114,792,867</u></b>	<b><u>\$ 2,259,468</u></b>	<b><u>\$2,117,052,335</u></b>

\*Examined as of December 31, 1995

**STATE ACCIDENT INSURANCE FUND CORPORATION**  
**STATEMENT OF ASSETS, LIABILITIES, SURPLUS & OTHER FUNDS**  
**As of December 31, 1995**

(CONTINUED)

**LIABILITIES**

Losses*	\$1,320,978,734
Loss adjustment expenses*	205,663,555
Other expenses due or accrued	9,211,720
Taxes licenses & fees	21,961,842
Unearned premium*	33,443,180
Funds held by Company under reinsurance treaties	356,196
Amounts withheld for the accounts of others	14,546,987
Aggregate write-ins for liabilities	<u>80,962,433</u>

<b>TOTAL LIABILITIES</b>	<b><u>1,687,124,647</u></b>
--------------------------	-----------------------------

**SURPLUS AND OTHER FUNDS**

Unassigned funds*	<u>429,927,688</u>
<b>TOTAL SURPLUS AND OTHER FUNDS</b>	<b><u>429,927,688</u></b>
<b>TOTAL LIABILITIES, SURPLUS, AND OTHER FUNDS</b>	<b><u>\$2,117,052,335</u></b>

\* Examined as of December 31, 1995

**STATE ACCIDENT INSURANCE FUND CORPORATION**  
**STATEMENT OF UNDERWRITING AND INVESTMENT EXHIBITS**  
**INCOME STATEMENT**  
**For the Year Ended December 31, 1995**

**UNDERWRITING INCOME**

Premiums earned	\$250,560,246
Losses incurred	198,763,243
Loss adjustment expenses incurred	58,667,036
Other underwriting expenses incurred	<u>54,845,803</u>
Total Underwriting Deductions	<u>312,276,082</u>
Net Underwriting Loss	(61,715,836)

**INVESTMENT INCOME**

Net investment income earned	119,877,379
Net realized capital gains	<u>20,323,849</u>
Net Investment Gain	140,201,228

**OTHER INCOME**

Net loss from premium balances charged off	(6,795,542)
Aggregate write-ins for miscellaneous income	<u>(17,423)</u>
Total other income	(6,812,965)
Net income before Federal taxes and dividends to policyholders	71,672,427
Dividends to policyholders*	<u>80,188,951</u>
Net income after dividends to policyholders but before Federal taxes	(8,516,524)
Federal income taxes incurred	<u>0</u>
Net Income	<u>\$ (8,516,524)</u>

**CAPITAL AND SURPLUS ACCOUNT**

Surplus as regards policyholders, December 31, 1994	474,756,300
Net income	(8,516,524)
Net unrealized capital gain	20,036,627
Change in nonadmitted assets	47,786,786
Aggregate write-in for losses in surplus	<u>(104,135,500)</u>
Change in surplus as regards policyholders for the year	<u>(44,828,611)</u>
Surplus as regards policyholders, December 31, 1995	<u>\$429,927,688</u>

\* Examined as of December 31, 1995

**COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS**

Several of the comments and recommendations made in the December 31, 1993 examination were made with respect to annual statement accounts which were not reviewed under the limited scope of this target financial examination. As a result, compliance with these prior examination recommendations have been addressed through correspondence with the Oregon Insurance Division and will be reported in the next regular scheduled examination. With respect to items examined, the Company has not complied with the following recommendation made in the December 31, 1993 report of examination:

Because of major shifts in the definition of injury types over time, the degree of uncertainty surrounding the Company's loss reserves is larger than would otherwise be the case. This shift has been most notable between permanent total and permanent partial claims. While the Company's consulting actuary, Milliman & Robertson, Inc. (M&R), has made a substantial effort to reflect the effects of this shift in their estimation of loss reserves, Mr. Sherman believed that the Company might benefit from an analysis of the medical loss reserves for both of these injury types on a combined basis. In his opinion this combined analysis might reduce some of the uncertainty surrounding the magnitude of the medical loss reserves for these two injury types.

Sherman noted the following pertaining to the compliance with this former recommendation:

This recommendation has not been adopted. Reasons cited include concerns regarding the reliability of the indications which might result from such a combined analysis. That reliability has been questioned because of concerns regarding changes in the homogeneity of types of claims included in the combined grouping. We agree that such concerns are valid, but would point out that the existing approach to analyzing the reserves for permanent total and permanent partial claims also suffers from the same problem of a lack of homogeneity. In our opinion, this problem exists to a greater extent for the current analysis than for the type of analysis we proposed two years ago. In view of all of these concerns, we believe that both approaches should be taken and their results compared and analyzed.

It is again recommended the Company perform an analysis of the medical loss reserves for both permanent total and permanent partial claims on a combined basis.

### SUMMARY OF COMMENTS AND RECOMMENDATIONS

Page

- 22 I recommend the Company establish procedures to assure documentation of underwriting decisions that have resulted in assignment to an alternative rate tier. Documentation should be uniform and used consistently by all underwriters. This recommendation is made pursuant to the provisions of ORS 733.170.

### CONCLUSION

There were no adjustments made to the Company's financial statements as a result of this target financial examination. During the 2 year period covered by this target financial examination, the surplus of the Company has increased from \$428,470,548 as presented in the December 31, 1993, report of examination, to \$429,927,688 as shown in this report of target financial examination. The comparative assets and liabilities are shown below:

	December 31,		
	<u>1995</u>	<u>1993</u>	<u>Change</u>
Assets	\$2,117,052,335	\$1,906,126,545	\$210,925,790
Liabilities	<u>1,687,124,647</u>	<u>1,477,655,997</u>	<u>209,468,650</u>
Surplus	<u>\$ 429,927,688</u>	<u>\$ 428,470,548</u>	<u>\$ 1,457,140</u>

**ACKNOWLEDGMENT**

The cooperation and assistance extended by the officers and employees of the Company during the examination process are gratefully acknowledged.

In addition to the undersigned, Thomas T. Farrelly, CFE, David Daulton, AFE, and Michael P. Phillips, CFE, CPA, insurance examiners for the State of Oregon, Department of Consumer and Business Services, Insurance Division, and Richard E. Sherman, FCAS, MAAA, and Richard Fallquist, FCAS, MAAA, consulting actuaries, participated in the examination.

Respectfully submitted,

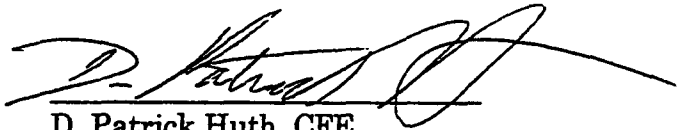


D. Patrick Huth, CFE  
Supervising Insurance Examiner  
Insurance Division  
Department of Consumer and Business Services  
State of Oregon

**AFFIDAVIT**

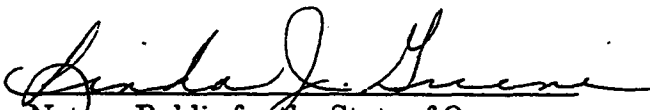
STATE OF OREGON       )  
  ) ss  
County of Marion       )

D. Patrick Huth, CFE, being duly sworn, deposes and says the preceding report of target financial examination as of December 31, 1995, of the State Accident Insurance Fund Corporation, Salem, Oregon, subscribed by him is true and correct to the best of his knowledge and belief.



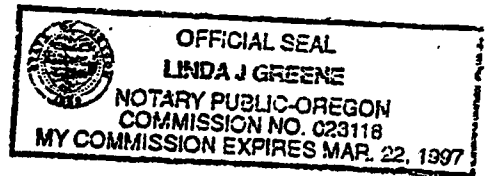
D. Patrick Huth, CFE  
Supervising Insurance Examiner  
Insurance Division  
Department of Consumer and Business Services  
State of Oregon

Subscribed and sworn to before me this 22<sup>nd</sup> day of October, 1996.



Notary Public for the State of Oregon

My Commission Expires: 3/22/97



**SAIF CORPORATION**  
**HISTORY OF RESERVE DISCOUNTS**  
(S000)

As of	(1) Total Discount on Loss Reserves	(2) Total Discount on LAE Reserves	(3) Total Amount of Discount (1) + (2)	(4) Estimated Amount of Tabular Discount * Included In (3)	
12/31/89	593,735	39,870	633,605	126,739	(e)
12/31/90	596,518	42,820	639,338	112,511	(e)
12/31/91	591,354	50,819	642,173	106,456	(e)
12/31/92	331,346	31,409	362,755	108,951	(e)
12/31/93	171,580	15,056	186,636	119,910	(e)
12/31/94	158,453	23,135	181,588	104,341	(e)
12/31/95	154,337	0	154,337	98,502	(a)

\* Tabular Discount = Discount on Indemnity Fatalis and PTD reserves at 3.5%

(a) = Actual, (e) = Estimated

**Source :**

Col (1) and Col (2) from various year of the Annual Statement, Schedule P summary Col (31) and Col (32).

	<u>Discount Rate</u> <u>For Medical</u>	<u>Discount Rate</u> <u>For Indemnity</u>
@12/31/89	3.5%	7.0%
@12/31/90	3.5%	7.0%
@12/31/91	3.5%	7.0%
@12/31/92	0.0%	7.0%
@12/31/93	0.0%	4% for Fatal and PTD
@12/31/94	0.0%	4% for Fatal and PTD
@12/31/95	0.0%	4% for Fatal and PTD



## HISTORY OF DISCOUNTING ASSUMPTIONS

<u>KEY DATES</u>	<u>MEDICAL</u>	<u>INDEMNITY</u>
Before December 31, 1985	0%	3.5% on awarded PTD's and fatalities 0% on all other indemnity claims
Since December 31, 1985	0%	3.5% on all PTD's and fatalities 0% on all other indemnity claims
Since December 31, 1986	0%	3.5% to date of award on PTD's, PPD's and fatalities 0% on all other indemnity claims
Since December 31, 1987	3.5% on all medical claims	7% on all indemnity claims
Since September 30, 1992	0%	7% on all indemnity claims
Since September 30, 1993	0%	4% on all PTD's and fatalities 0% on all other indemnity claims

**PROPERTIES OWNED BY SAIF CORPORATION  
FOR THE PERIOD FROM 1/1/80 TO 12/31/95**

This worksheet summarizes real estate holdings from its acquisition to the later of its disposition or 12/31/95. Included is all property owned as of 12/31/95 as well as all other property with buy or sell transactions since 1/1/80.

Source: Annual Statements filed by Saif with the Oregon Insurance Division.

Property	Date Acquired	Date Sold	Actual Cost	Book Value	Market Value	Sale Price	Gain (loss) on sale
<b>Real Estate Owned As Of 12/31/95</b>							
400 High St, SE, Salem, OR	1972		5,581,375	3,151,466	6,318,600		
2862 State St., Medford, OR (Glenmont)	1980		1,983,122	1,297,657	1,616,380		
3080 Broadway, North Bend, OR	1982		125,155	89,690	178,225		
115 SE 8th, Pendleton, OR	1975		118,850	61,601	87,580		
555 13th St, NE, Salem, OR	1989		1,832,940	1,552,399	2,650,000		
440 Church St, SE, Salem, OR	10/93		13,874,702	13,579,693	13,579,693		
480 Church St, SE, Salem, OR	10/93		1,257,751	1,226,571	1,226,571		
655 Bellevue St., SE, Salem, OR	1994		5,058,464	4,942,541	4,942,541		
<b>Real Estate Disposed of Prior to 12/31/95</b>							
Clark & Lawrence St Land, Eugene, OR	1988	12/90	15,000	15,000	18,510	20,000	5,000
79 Centennial Loop, Eugene, OR	1975	1983	240,995	198,228	322,200	308,500	110,272
999 Spring St, Medford, OR	1975	1982	123,508	106,854	208,400	215,000	108,146
355 NE Lafayette, Bend, OR	1975	11/85	74,230	58,648	88,000	78,000	19,352
Land - Boyd's Addition, Baker, OR	1976	9/84	20,229	20,229	12,060	15,000	(5,229)
600 Country Club Rd, Eugene, OR (lot 3100)	1981	12/89	2,378,777	1,969,857	1,757,410	2,021,077	51,220
Parcel 2608, Gateway Loop, Springfield, OR	6/86	11/87	120,800	120,800	106,400	90,000	(30,800)
Gateway St. tax lot 2300 Springfield, OR	1989	5/90	327,500	314,852	359,890	315,184	332

A68

A69

Appendix I.a.

STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF TARGET MARKET CONDUCT EXAMINATION

OF

STATE ACCIDENT INSURANCE FUND CORPORATION  
SALEM, OREGON

NAIC COMPANY CODE 36196

AS OF

DECEMBER 31, 1995



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July 23, 1996

Honorable Kerry Barnett, Director  
Department of Consumer and Business Services  
State of Oregon  
350 Winter Street NE, Room 440-4  
Salem, Oregon 97310

Dear Director:

In accordance with your instructions and pursuant to ORS 731.300, we have examined the business affairs of

**STATE ACCIDENT INSURANCE FUND CORPORATION**  
**400 High Street SE**  
**Salem, Oregon 97312**

**NAIC Company Code 39196**

hereinafter referred to as the "Company" or "SAIF." The following report of examination is respectfully submitted.



**SCOPE OF EXAMINATION**

The market conduct examination of the Company was conducted as of December 31, 1995, covering the two-year period then ended, and included a review of material transactions or events which occurred subsequent to the examination cut-off date and were noted during the examination.

The last market conduct examination of the Company was as of December 31, 1993.

The examination of the Company was conducted pursuant to ORS 731.300 and in accordance with procedures and guidelines outlined in the Market Conduct Examination Handbook as adopted by the National Association of Insurance Commissioners (NAIC) and/or the market conduct program established by the Oregon Insurance Division. The purpose was to conduct a limited scope target examination pursuant to the requirements of B-Engrossed House Bill 2033 (B-Eng.HB 2033). In addition, the examination will determine the Company's ability to fulfill and manner of fulfillment of its obligations, the nature of its operations, whether it has given proper treatment to policyholders, and its compliance with the Oregon Insurance Code and Administrative Rules.

In order to determine the practices and procedures of the Company's operations, one or more of the following procedures was performed in each phase:

1. A sample of files was selected from listings provided by the Company. Each file was then reviewed by the examiner.
2. The procedure manuals and/or memorandum were evaluated.
3. The Company responded to a series of questions regarding the phase being examined.

The examination was comprised of the following 4 phases:

Agent Licensing/Appointments

Underwriting

Premium Audit

Unit Statistical

### DESCRIPTION OF COMPANY

The State Accident Insurance Fund Corporation (the Fund) was created in 1979 as an independent non profit public corporation by passage of Senate Bill 255. The Company is the successor to the Fund which was created for the purpose of transacting workers' compensation business formerly transacted by the State Industrial Accident Commission. The latter operated as an exclusive state workers' compensation agency from 1914 through 1965.

In 1965, private insurance companies were permitted to compete with the Fund. Simultaneously, large businesses were allowed to self-insure. This resulted in the three-way workers' compensation insurance system found in Oregon today.

Passage of ORS 731.028 made SAIF a domestic insurer subject to the limited provisions of the Oregon Insurance Code covering rate filings, accounting methods, annual statement filings and examinations.

Passage of Senate Bill 255 in 1979 converted the Fund to its present structure as an independent public corporation governed by a board of 5 directors appointed by the Governor. This bill exempted the Company from a number of statutes which control the administration and fiscal activities of state agencies, and made the Company subject to limited Insurance Code provisions.

### UNDERWRITING

Applications received from agents are first checked to confirm duplicate submissions were not made. Agency records are reviewed to verify the agent is appointed to represent the Company and a corporation check is run through the State of Oregon. If

prior coverage history with this Company exists, the data is extracted and provided with the file for the underwriter's review.

A confirmation letter also referred to as a "release letter" is mailed to the agent. An application number is assigned, the case is entered into the computer system and forwarded to an assistant underwriter.

The assistant underwriter collects all information the underwriter will need to make a decision on the application and enters the case into the Company's RAPID (Risk Analysis Policy Issuance Design) application system.

The RAPID application is a windows-based SAIF developed facility that provides a set of windows to input or view policy information, evaluate that information, produce a proposal for coverage, and issue and maintain a policy of insurance.

The underwriter then reviews all materials compiled regarding the risk to determine the appropriate action necessary.

Applications made directly to the Company without agent involvement are handled by the branch account representatives who work with regional support specialists to develop the data needed for the underwriter to make a decision. The branch account representatives do have limited authority for approving coverage up to certain levels without consulting an underwriter.

The Company also receives applications from the National Council on Compensation Insurance, Inc. (NCCI) for participants in the assigned risk program. These are routed to a Company cashier who handles the initial premium received with the applications and then forwards them to the customer policy services area. The customer service

representative sets up the file, assigns a policy number, enters the case in the computer system and issues the policy. The customer service representative checks the data received from the NCCI and generates any changes needed such as a classification code designation or endorsement required for coverage. The customer service representatives hold the same responsibility as an underwriter except they are not responsible for pricing decisions.

A Coverage Request Form is sent when an agent or employer makes an inquiry regarding coverage through the AOI Compwise program. After this form is received, Company records are checked to confirm duplicate submissions were not made. Agency records are reviewed to verify the agent is appointed to represent the Company and a corporation check is run through the State of Oregon. If prior coverage history with this Company exists, the data is extracted and provided with the file for review. A preliminary underwriting review by a customer service representative is made and a quote along with an application for insurance is mailed to the agent or applicant. Completed applications with initial premium are routed to the accounting department. The case is once again reviewed by underwriting and if the risk is approved, the policy is issued.

AOI Compwise began as a pilot project in April, 1991 between Associated Oregon Industries, SAIF and JBL & K of Portland as the general agent in charge of sales and policy issue. In 1994, the Company assumed responsibility for the policy issuance side of the program from JBL & K..

The program was created to cover nonexperience rated business with annual premium up to \$2,500. Its challenge was to focus on the unique issues facing small business, to simplify procedures and to find ways to reduce its high claims exposure.

AOI Compwise policyholders are a diverse group with no particular business type dominating the mix. Dentists, doctors, lawyers, churches, research labs and nonprofit organizations comprise the largest business segments, but each represents only 2% to 5% of the program participants.

As of March, 1996 there were over 15,000 active accounts in the AOI Compwise program representing a premium volume of \$17 million. Approximately 32% of the businesses in the AOI Compwise program have a premium value of \$1,000 or less and another 68% have a premium value of above \$1,000. The AOI Compwise program accounts for about 40% of SAIF policyholders and 6% of its annual premium.

The AOI Compwise program utilizes a simplified billing process by collecting premium due in advance of coverage. Minimum premium accounts pay their full premium at the inception of the policy. Larger accounts whose estimated premium exceeds the minimum amount are allowed to use installment payment plans. This premium collection method has reduced the administrative costs related to premium collection. Uncollected premium represents .02% of the current level of active premium.

This method of premium collection differs from larger accounts which are often allowed to pay premiums retrospectively in whole or in part.

The AOI Compwise program also follows separate underwriting guidelines than the larger accounts. The listing of hazardous operations which the Company will not write

in AOI Compwise differs from the SAIF Corporation hazardous operations listing. A separate Underwriting Authority has been established for AOI Compwise.

The computer system currently being used for the AOI Compwise program contains limitations which do not allow the Company to service experience rated business. AOI Compwise insureds received their first dividends in 1994 and 2 additional dividends in 1995. The dividends for AOI Compwise are computed differently than dividends for other SAIF insureds.

Employers who do not qualify for coverage through the AOI Compwise program either due to system limitations or premium levels may be referred to SAIF Corporation for coverage.

### Findings

The Company provided master listings of policies issued and policies canceled or rejected during the examination period.

Two computer systems are operated by the Company. The AOI Compwise program computer system is based in the Portland, Oregon office and is used for small businesses which meet certain underwriting criteria. All other SAIF policies are maintained in the Salem, Oregon computer system. For this reason, samples were selected from each of the systems to produce a total random sample of 100 records. From the AOI Compwise master listing of 6,602 policies issued, a random sample of 50 (.76%) policies was selected. From the other SAIF master listing of 7,287 policies issued, a random sample of 50 (.69%) was selected.

A similar process was used to develop the samples for rejected or canceled business. A random sample of 50 rejected or canceled cases was reviewed. From the AOI Compwise

master listing of 1,907 rejections or cancellations, a random sample of 25 (1.31%) was selected. From the other SAIF master listing of 1,882 rejections or cancellations, a random sample of 25 (1.33%) was selected.

The samples were tested for compliance with the following standards based on Oregon Revised Statutes and/or Oregon Administrative Rules. The text of the laws and administrative rules which form the basis of each standard may be found in Appendix 1 following the report.

Underwriting - Issued Business Standard #1 - The Company does not make or permit any unfair discrimination. See ORS 746.015, page A-8 and OAR 836-81-010, page A-13.

**Findings**

100% compliance.

Underwriting - Issued Business Standard #2 - Classifications of occupations and rate levels are correct. See ORS 656.508, page A-3.

**Findings**

99% compliance. An incorrect classification code was assigned to 1 of the policies reviewed. The Company file documentation is not adequate enough to determine which classification should have been applied. The customer is no longer insured and it appears reclassification would not result in a premium refund. The Company was unable to explain how it arrived at the incorrect code.

The examiner performed a rating review of 21 assigned risk policies for which no errors were noted. An additional review of rating to determine if employers were assigned to rating tiers and rating group programs, particularly small employers, according to their

approved filed rating plans was performed by Richard E. Sherman & Associates, Inc. and is addressed in the corresponding financial examination for the same period.

Since a failure rate of 1% does not appear to constitute a pattern, no recommendation is made.

Underwriting - Issued Business Standard #3 - Every insured employer remits premium to the Company in accordance with the payment plan established for that employer. See ORS 656.504, page A-2.

**Findings**

100% compliance.

Underwriting - Issued Business Standard #4 - Rate changes made on renewed policies are appropriate. See OAR 836-85-225, page A-14.

**Findings**

100% compliance.

Underwriting - Policies Rejected/Nonrenewed Standard # 1- The Company does not make or permit any unfair discrimination. See ORS 746.015, page A-8 and OAR 836-81-010, page A-13.

**Findings**

100% compliance.

Underwriting - Policies Rejected/Nonrenewed Standard #2 - The Company sends copies of cancellation notices it receives from insured employers to the Oregon Department of



Consumer and Business Services within 10 days following receipt of such notices. See ORS 656.423(4), page A-1.

**Findings**

100% of the records reviewed to which this standard applies are in compliance. Only 1 of the policies included in this sample was canceled by the insured employer.

**Underwriting - Policies Rejected/Nonrenewed Standard #3** - The Company provides written notice of termination of guaranty contracts to the employer and to the Oregon Department of Consumer and Business Services 30 days prior to the effective date of termination. If the reason for termination is based on the Company's decision not to offer insurance to employers within a specific premium category, 90 days prior notice is provided to the employer and to the Oregon Department of Consumer and Business Services. See ORS 656.427(1)(2), page A-1

**Findings**

100% of the records reviewed to which this standard applies are in compliance. Five of the policies included in this sample were guaranty contracts canceled by the Company.

**Underwriting - Policies Rejected/Nonrenewed Standard #4** - The Company maintains its records in such a manner that the Oregon Department of Consumer and Business Services may readily ascertain whether proper treatment has been given to policyholders and that the Company has complied with the Insurance Code. See ORS 733.170, page A-4.

**Findings**

100% compliance.

Underwriting Global Standard #1 - Confirmation of Compliance with OAR 836-43-120 Minimum Standards of Employer Education Program. See OAR 836-43-120, page A-12.

### Findings

Not in compliance. The provisions of OAR 836-43-120(1)(e) require the Company to disclose to the employer the appeal process afforded employers by ORS 737.505 at or before policy issuance. From the information provided, it appears the Company notifies employers of this appeal process at the time the premium audit is conducted rather than at or prior to policy issue.

I recommend the Company notify employers of the appeal process available to employers by ORS 737.505 at or before policy issuance in accordance with the provisions of OAR 836-43-120(1)(e).

### Summary of Rejection/Nonrenewal Reasons

<u>Reason</u>	<u>Number</u>	<u>% To Total</u>
Adverse loss projection	8	16%
Applicant rejected offer	1	2
Company data entry error-Not a true rejection	1	2
Claims experience	7	14
Have not been insured-Non-compliance	1	2
Hazardous operation	4	8
Inquiry only-No formal application submitted	2	4
Lack of information from applicant	1	2
Lack of management experience	5	10
Management reason	1	2
New business	2	4
Not an employer	4	8
Not experience rated	1	2
Poor credit	2	4
Premium too large for AOI Compwise program	9	18
Type of business not acceptable	<u>1</u>	<u>2</u>
Total	<u>50</u>	<u>100%</u>

**Additional Procedures and Findings**

One of the policies in the rejected/nonrenewed portion of this phase of the examination was canceled 1-1-95. A premium audit was performed in November, 1995 which resulted in a premium credit. The \$90.65 refund due the employer was not mailed until this outstanding credit was noticed by the examiner and an inquiry sent to the Company for response.

The provisions of ORS 731.028, exempt the Company from compliance with ORS 746.650 which requires the Company to provide written notification to the applicant of the specific reason(s) for adverse underwriting decisions. Therefore, compliance with this statute was not considered in this examination.

**AGENT/AGENCY LICENSING/APPOINTMENTS**

The Company appoints licensed independent agents and/or agencies to market its products.

A support specialist in the underwriting division screens applications received to verify the writing agent is appointed to represent the Company..

Appointed agents are notified of new products and changes in insurance law through "competitive updates" which are mailed from the agency division and the Company's compquotes publication which is distributed on a bi-monthly basis. The updates typically contain new product information, dividend information, competitive carrier filings and changes to group programs. All communication sent from the agency division is maintained in a central file. The Company also offers training courses to its appointed agents to assist them in understanding the technical elements of selling workers' compensation insurance.

The Company is not under any obligation to appoint every agent who requests an appointment.

**Findings**

Agent and agency information was captured in the underwriting phase and a report containing the agent/agency names for the 100 records reviewed was produced. From this report, 10 records (10%) were chosen. Beginning with unit number 10, each 10th record was selected. If the policy identified for review was not written by an agent, the next unit listed on the report containing an agent or agency name was selected for this sample.

The sample was tested for compliance with the following standards based on Oregon Revised Statutes and/or Oregon Administrative Rules. The text of the laws and administrative rules which form the basis of each standard may be found in Appendix 1 following the report.

Agent Licensing Standard #1 - Agents must be properly appointed. See ORS 744.155(1), page A-7.

**Findings**

100% compliance.

Agent Licensing Standard #2 - Agents must be properly licensed at the time of appointment. See ORS 744.051, page A-5, ORS 744.054, page A-6, and ORS 744.057, page A-6.

**Findings**

100% compliance.

Agent Licensing Global Standard #1 - Agent contracts must contain 90 day notice of termination by the Company. See ORS 744.175(1)&(2), page A-7.

### Findings

Not in compliance. The Company provided 2 specimen contracts for review. Although these documents do provide a 90 day notice of termination, the reasons listed in the contracts for immediate termination include 4 causes which are not grounds for immediate termination pursuant to the provisions of ORS 744.175(2).

I recommend the Company revise its agency agreements by removing the 4 causes for immediate termination which are not included as grounds for immediate termination pursuant to the provisions of ORS 744.175(2).

### Subsequent Events

During the course of this examination the Company acknowledged the agent contracts do contain improper language. Although the contracts have been used in their present form for a number of years, no agency termination has been based upon the 4 causes for immediate termination referenced above. The Company indicates no agency agreement will be terminated without 90 days notice unless the grounds for such termination are cited in ORS 744.175. Additionally, the Company will modify the agent contracts on their renewal dates, going forward, in order to comply with the provisions of ORS 744.175.

### PREMIUM AUDIT

The Company is required to conduct periodic audits of businesses based on premium size. These audits help protect the Company's financial position and allow a periodic

monitoring of the payrolls to help maintain the accuracy of statistics used to determine workers' compensation insurance rates.

The Company maintains a home office premium audit department which reviews the data submitted by businesses on monthly self audits. This department also supports several field auditors positioned by risk concentration throughout the state.

The field auditors perform periodic physical audits of the employers' books and records for determining overall final premium based on payroll assigned to the correct risk classifications unique to the business and to verify payroll amounts submitted by those businesses in the previous policy year. It is important that payroll records be accurate because they are a key element in determining the final premium.

### **Findings**

The Company provided listings of completed premium audits. The examiner used this information to develop the following information for the examination period.

#### **1994**

<b><u>Premium Category</u></b>	<b><u># of Audits per Category</u></b>	<b><u>Total # of Policies per Category</u></b>	<b><u>% of Audits to Total</u></b>
\$1,000 - \$9,999	1,678	18,217	9.2
≥ \$10,000	1,601	5,436	29.5

#### **1995**

<b><u>Premium Category</u></b>	<b><u># of Audits per Category</u></b>	<b><u>Total # of Policies per Category</u></b>	<b><u>% of Audits to Total</u></b>
\$1,000 - \$9,999	1,482	18,109	8.2
≥ \$10,000	2,162	5,574	38.8

The results were tested for compliance with the following standards based on Oregon Revised Statutes and/or Oregon Administrative Rules. The text of the laws and administrative rules which form the basis of each standard may be found in Appendix 1 following the report.

Global Premium Audit Standard #1 - The Company audits each policy producing an annual earned premium of \$10,000 or more at least annually. See OAR 836-43-110(1)(a), A-10.

### Findings

Not in compliance. The Company audited 29.5% of the policies with \$10,000 or greater in earned premiums in 1994 and 38.8% in 1995. The Company changed its procedures in 1991 in anticipation of a proposed amendment to OAR 836-43-110. The amendment would have changed the required audit period for policies earning \$10,000 or greater in earned premium from annually to once every three years. The rule change was never implemented. However, the Company continued to operate under the proposed rules. The Company believed the Insurance Division had placed a moratorium on the old rules.

During the course of the examination, written evidence from the Insurance Division of such a moratorium was not provided.

I recommend the Company audit annually each policy producing an earned premium of \$10,000 or more in accordance with the provisions of OAR 836-43-110(1)(a).

Global Premium Audit Standard #2 - The Company audits 5% of the policies earning less than \$10,000 in annual earned premium but more than \$1,000. See OAR 836-43-110(1)(b), page A-10.

**Findings**

The Company is in compliance.

Global Premium Audit Standard #3 - The Company receives a signed payroll statement for each year not audited from policies with earned premiums of less \$10,000 but more than \$1,000. See OAR 836-43-110(1)(b), page A-10.

**Findings**

The Company is in compliance.

Global Premium Audit Standard #4 - The Company follows the requirements for the Final Premium Audit Billing. See OAR 836-43-110(2), page A-11.

**Findings**

The Company is in compliance.

**Additional Procedures and Findings**

The examiner reviewed the premium audit of 20 files selected through interval sampling to verify the accuracy of the data provided by the Company. No exceptions were noted.

**UNIT STATISTICAL**

The unit statistical phase includes a review of final premiums, modifications, and claims incurred loss data attributed to each policy according to evaluation guidelines in the Unit Statistical Plan Manual and sent to the NCCI.



Data quality submission by the Company in the unit statistical reporting is important for ratemaking and the promulgation of reliable individual experience modifications for each business operation.

During the previous market conduct examination the Company was in the final phases of a project which integrated all internal computer systems so the information in these systems would download and interface properly with the unit statistical system. This project is now complete. The transmission of data electronically resulted in system errors as opposed to manual errors experienced under the former "unit stat card" program. The Company worked with the NCCI and the Insurance Division to minimize the impact of system errors on its insureds.

The focus of this examination was to determine if the current unit statistical system is operating correctly and error free. The review consisted of three steps:

1. Samples from the last report filed with the NCCI were drawn and compared to source documents to verify the accuracy of the data transmitted to the NCCI.
2. A review of the quality and timeliness reports received from NCCI was completed.
3. An actuarial study of the unit statistical reporting was performed by Richard E. Sherman & Associates, Inc., a consulting actuary contracted by the Department of Consumer and Business Services (DCBS). The results of the study are incorporated in the following section.

### **Findings**

Accuracy of data transmitted to NCCI from SAIF:

Two samples were drawn from the unit statistical report transmitted to NCCI in May of 1996. The May 1996 report consisted of data extracted from policies with an inception date of November 1994 or earlier.

The first sample was selected at a policy level. From a total population of 673 policies, the last digit 2 was randomly selected and the first 25( 3.7%) policies ending in the digit 2 were selected for sample.

The examiner was provided with a print out for each policy selected displaying the information sent to the NCCI. The examiner compared the data sent to the NCCI against the source documents. Specific attention was given to the following areas: class codes, exposure, premium and rate. No discrepancies were noted.

The second sample was drawn only from policies with claims data. A total of 68 files with 1 or more claims were identified from the May 1996 tape. A total of 88 claims were counted.

Every other policy was selected for review resulting in a total of 38 (43%) claims.

Once again the examiner was provided with a print out for each policy selected displaying the information transmitted to the NCCI. Specific attention was given to the class codes and loss data. No discrepancies were noted.

Review of quality and timeliness reports from NCCI:

The NCCI provides feedback on the Company's unit statistical data in the form of quality and timeliness reports. The NCCI reports lag 1 to 3 months behind the unit statistical transmissions.

The quality report ("Carrier Performance Report-Quality") contains unit reports processed through NCCI's system which failed one or more of the quality edits and/or which failed to match a policy in NCCI's system.

The quality report indicated 8,843 first report, 4,311 subsequent report and 1,990 corrections were reviewed from the April unit statistical reports. From the total of 15,144 reports, 2138 (14%) default errors were shown. The majority of these errors were tied to a system problem regarding standard premium and the Oregon exceptions. The Company has been working with the NCCI and the Insurance Division to resolve this error. This error is a system error and does not impact the policyholder.

Additionally there were 72 suspect errors and 1 priority error. Suspect errors are notification by the NCCI of potential error. A priority error is a true error which must be corrected by the Company.

There are 2 reports addressing timeliness. The first, "Delinquent Unit Report Policy List" is issued 1 month after the initial unit statistical transmission is due for a specific reporting period. The examiner reviewed the "Delinquent Unit Report Policy List" for the reporting period representing policies with an inception date of August 1994 and the 4 previous annual reporting periods.

Out of a total of 942 reports due, 15 (1.6%) were delinquent.

The second timeliness report, the "Fine List," arrives one month after the Delinquent Unit Report Policy List. It is a listing of delinquent reports for every prior reporting period. The last report received from the Company at the time of the examination was

for policies with an inception date of July 1994 and every reporting period prior. From a total of 65,914 reports expected by the NCCI, 27 (.04%) were delinquent.

Results of actuarial study:

The DCBS consulting actuary reviewed listings produced by the NCCI and contacted NCCI officials to obtain information regarding the nature and extent of problems in SAIF's unit statistical reporting.

The actuary's observations and findings are as follows:

In 1995, SAIF received a less than optimal grade for timeliness of newly issued policies and any endorsements. This was primarily due to an Assigned Risk related issue, and should not be considered reflective of SAIF's voluntary business.

The one area where SAIF received a lower than optimum grade in 1994 was the average quality of aggregate financial data. The measure used was the average fine per submission. That average fine (\$200) corresponds to a letter grade of "C". It is noted that SAIF has openly acknowledged the existence of these problems with its 1994 submissions but has stated these areas are no longer a problem. This is confirmed by the fact that SAIF's 1995 letter grade for this same category has improved to an "A" with average fines per submission of \$0.

With the exception of system generated errors, the Company's unit statistical program appears to be operating with minimal errors. No recommendations are warranted at this time.

#### **COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS**

The prior market conduct examination produced 4 recommendations. Two recommendations concerned the handling of complaints. The complaint handling phase was waived due to the limited scope of this examination. Therefore, the Company's actions regarding the prior complaint recommendations were not verified.

As of December 31, 1995, the Company appeared to have complied with the 2 remaining recommendations made in the report as of December 31, 1993.

CONCLUSION/RECOMMENDATIONS

Page

- 13 I recommend the Company notify employers of the appeal process available to employers by ORS 737.505 at or before policy issuance in accordance with the provisions of OAR 836-43-120(1)(e).
- 16 I recommend the Company revise its agency agreements by removing the 4 causes for immediate termination which are not included as grounds for immediate termination pursuant to the provisions of ORS 744.175(2).
- 18 I recommend the Company audit annually each policy producing an earned premium of \$10,000 or more in accordance with the provisions of OAR 836-43-110(1)(a).

MANAGEMENT AFFIRMATION

To the Attention of Jann Goodpaster, CIE, CPCU, Examiner-In-Charge for the Oregon Insurance Division in connection with the examination of the State Accident Insurance Fund Corporation, for the period of January 1, 1994 to December 31, 1995.

Pursuant to the provisions of ORS 731.300 and 731.308 and to the best of my knowledge and belief, I, William D. Thorndike, do hereby certify for the period covered by this examination that:

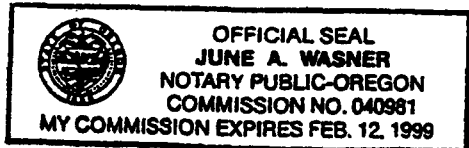
- the transactions and business affairs of State Accident Insurance Fund Corporation are conducted in compliance with the [applicable] statutes, rules and procedures of the Oregon Insurance Division;
- for the period under review, all operations of the Company were conducted in such a manner as not to be hazardous to the insurance buying public or in violation of the [applicable provisions of the] Oregon Insurance Code;
- all books, records, accounts, papers, documents and computer and other recordings in the Company's possession and relating to its assets, accounts, transactions and affairs, to its treatment of policyholders, compliance with the Insurance Code, and to all matters relating to the period under examination, are kept in accordance with ORS 733.170 and have been made available to the examiners in their entirety pursuant to ORS 731.308; and
- all corporate powers are exercised by or under the authority of the duly qualified and constituted Board of Directors of the Company and the business affairs and transactions of the Company are managed under the direction of such Board of Directors, all in accordance with the duties and responsibilities conferred upon the Board of Directors by the Articles of Incorporation\*, Bylaws, and Oregon Law.

Dated this 7 day of June 1996.

William D. Thorndike  
William D. Thorndike - Chairman of the Board

Subscribed and sworn before me this 7<sup>th</sup> day of June 1996.

June A. Wasner  
Notary Public in and for the State of Oregon



[\*Note that, as a creation of statute, State Accident Insurance Fund Corporation has no Articles of Incorporation.]

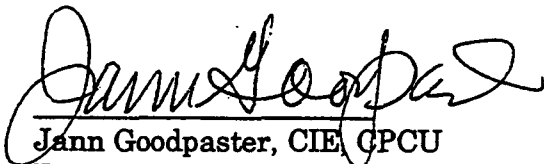
**ACKNOWLEDGMENT**

The cooperation and assistance rendered by the officers and employees of the Company during this examination is hereby acknowledged and appreciated.

A special thanks is extended to the examination coordinator for his courtesy, assistance, and promptness in providing, correlating, or coordinating all requested documents and statistics necessary to ensure a smooth transition during the overall examination process. The responsibilities that were undertaken during this examination were in addition to the scope of his regular assigned duties.

In addition to the undersigned, Gayle L. Woods, market conduct examiner, for the State of Oregon, Department of Consumer and Business Services, Insurance Division, and Richard E. Sherman, FCAS, MAAA, consulting actuary, participated in this examination.

Respectfully submitted,

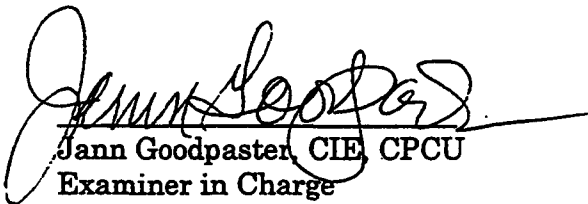


Jann Goodpaster, CIE, GPCU  
Examiner in Charge  
Market Conduct Section  
Department of Consumer and Business Services  
Insurance Division  
State of Oregon

AFFIDAVIT

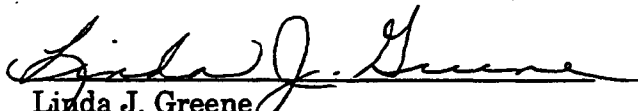
STATE OF OREGON        }  
                                  }  
County of Marion        } ss

Jann Goodpaster, being duly sworn, deposes and says that the foregoing market conduct report of examination as of December 31, 1995, subscribed by her is true to the best of her knowledge and belief.

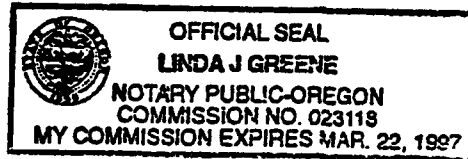


Jann Goodpaster, CIE, CPCU  
Examiner in Charge  
Market Conduct Section  
Department of Consumer and Business Services  
Insurance Division  
State of Oregon

Subscribed and sworn to before me on the 3rd day of September, 1996.



Linda J. Greene  
Notary Public for the State of Oregon  
My Commission Expires: March 22, 1997





APPENDIX 1  
APPLICABLE OREGON REVISED STATUTES  
AND OREGON ADMINISTRATIVE RULES

**ORS 656.423 Cancellation of coverage by employer; notice required; exception.**

(1) An insured employer may cancel coverage with the insurer by giving the insurer at least 30 days' written notice, unless a shorter period is permitted by subsection (3) of this section.

(2) Cancellation of coverage is effective at 12 midnight 30 days after the date the cancellation notice is received by an authorized representative of the insurer, unless a later date is specified.

(3) An employer may cancel coverage effective less than 30 days after written notice is received by an agent of the insurer by providing other coverage or by becoming a self-insured employer. A cancellation under this subsection is effective immediately upon the effective date of the other coverage or the effective date of certification as a self-insured employer.

(4) The insurer shall, within 10 days after receipt of a notice of cancellation under this section, send a copy of the notice to the director.

**ORS 656.427 Termination of guaranty contract or surety bond liability by insurer.**

(1) An insurer that issues a guaranty contract or a surety bond to an employer under this chapter may terminate liability on its contract or bond, as the case may be, by giving the employer and the director written notice of termination. A notice of termination shall state the effective date and hour of termination.

(2) An insurer may terminate liability under this section as follows:

(a) If the termination is for reasons other than those set forth in paragraph (b) of this subsection, it is effective at 12 midnight not less than 30 days after the date the notice is received by the director.

(b) If the termination is based on the insurer's decision not to offer insurance to employers within a specific premium category, it is effective not sooner than 90 days after the date the notice is received by the director.

(3) Notice under this section shall be given by mail, addressed to the employer at the last-known address of the employer. If the employer is a partnership, notice may be given to any of the partners. If the employer is a limited liability company, notice may be given to any manager, or in a member managed limited liability company, to any of the members.

If the employer is a corporation, notice may be given to any agent or officer of the corporation under whom legal process may be served.

(4) Termination shall in no way limit liability that was incurred under the guaranty contract or surety bond prior to the effective date of the termination.

(5) If, before the effective date of a termination under this section, the employer gives notice to the insurer that it has not obtained coverage from another insurer and intends to become insured under the assigned risk plan established under ORS 656.730, the insurer shall insure that continuing coverage is provided to the employer under the plan without further application by the employer, transferring the risk to the plan as of the effective date of termination. If the insurer is a servicing carrier under the plan, it shall continue to provide coverage for the employer as a servicing carrier, at least until another servicing carrier is provided for the employer in the normal course of administering the plan. If the insurer is not a servicing carrier, it shall apply to the plan for coverage on the employer's behalf. Nothing in this section is intended to limit the authority of administrators of the plan to require the employer to provide deposits or to make payments consistent with plan requirements. However, the rules of the plan shall allow any deposit requirements imposed by the plan to be deferred for as long as one year.

#### **ORS 656.504 Rates, charges, fees and reports by employers insured by SAIF Corporation.**

(1) Every employer insured by the State Accident Insurance Fund Corporation shall pay to the State Accident Insurance Fund Corporation on or before the 15th day of each month, for insurance coverage, a percentage of the employer's total payroll for the preceding calendar month of subject workers according to and at the rates promulgated by the State Accident Insurance Fund Corporation under ORS 656.508 and shall forward to the State Accident Insurance Fund Corporation on or before the 15th day of each month a signed statement showing the employer's total payroll for the preceding calendar month, the kind of work performed, the number of workers and the number of days worked. The State Accident Insurance Fund Corporation may establish other reporting periods and payment-due dates and in lieu of payment based upon a percentage of total payroll may promulgate rates to be paid by employers insured with the State Accident Insurance Fund Corporation utilizing a certain number of cents for each work-hour worked by workers in such employer's employ. Each such employer shall also pay an annual fee, deposit and minimum premium in such amount and at such time as the State Accident Insurance Fund Corporation shall prescribe, to the Industrial Accident Fund for each calendar year. Each such employer may be required to pay a registration fee in such amount and at such time as the State Accident Insurance Fund Corporation shall prescribe. The State Accident Insurance Fund Corporation may vary the amount of these fees and minimum premium by employer groupings, accept them in lieu of the other premiums which are based on the employer's payroll, and may adjust the period of application from a calendar year to a fiscal year.

(2) The State Accident Insurance Fund Corporation may provide for a short rate premium applicable to employers who cancel their coverage with the State Accident Insurance Fund Corporation prior to the expiration of the coverage period using a standard short rate table.

**ORS 656.508 Authority to fix premium rates for employers.**

(1) The State Accident Insurance Fund Corporation shall classify occupations or industries with respect to their degree of hazard and fix premium rates upon each of the occupations or industries sufficient to provide adequate funds to carry out the purposes of this chapter and the duties of the State Accident Insurance Fund Corporation.

(2) The State Accident Insurance Fund Corporation may annually, and at such other times as it deems necessary, readjust, increase or decrease the premium rates of employers insured with the State Accident Insurance Fund Corporation. Any such readjustment, increase or decrease shall be made and become effective on such dates as the State Accident Insurance Fund Corporation may determine. The State Accident Insurance Fund Corporation shall notify the employer of the rate.

(3) The State Accident Insurance Fund Corporation may establish a uniform system of rate modification conforming to recognized insurance principles including schedule rating and experience rating, premium discount and retrospective rating.

**ORS 731.028 Applicability of certain Insurance Code provisions to State Accident Insurance Fund Corporation.**

The State Accident Insurance Fund Corporation is subject as a domestic insurer to ORS 731.248, 731.252, 731.256, 731.258, 731.260, 731.296 to 731.316, 731.488, 731.574, 731.730, 731.731, 731.735, 731.737, 731.988, 731.992, 733.010 to 733.060, 733.140 to 733.170, 733.210, 737.205, 737.215, 737.225, 737.235 to 737.340, 737.505, 737.560, ORS chapters 742, 743 and 744, ORS 746.015, 746.075, 746.110, 746.145 to 746.155, 746.230 and 746.240 to the extent that such provisions are not inconsistent with the express provisions of ORS chapter 656. However:

- (1) The requirements of the Director of the Department of Consumer and Business Services under ORS 733.010 to 733.060, 733.140 to 733.170 and 733.210 govern in the case of a conflict between those requirements and the requirements of any accounting system prescribed by the Oregon Department of Administrative Services.
- (2) The filing requirements of ORS 737.205 to 737.340, 737.505 and 737.560 are in lieu of any similar filing requirements prescribed by any other law of this state.
- (3) The requirements of ORS chapter 743 are applicable only with respect to excess workers' compensation insurance furnished by the corporation.
- (4) The provisions of ORS chapter 744 apply only with respect to the regulation of agents.

(5) For each year that the Secretary of State conducts an audit of the State Accident Insurance Fund Corporation under ORS 297.210, the director may accept the audit and a copy of the Secretary of State's audit report in lieu of the requirements of ORS 731.488 if the director determines that the purposes of ORS 731.488 are adequately served by the Secretary of State's audit and report. The Secretary of State shall file a copy of its audit report of the State Accident Insurance Fund Corporation with the director.

**ORS 731.300 Examination of insurers; when required.**

(1) The director shall examine every authorized insurer, including an audit of the financial affairs of such insurer, as often as the director determines an examination to be necessary but at least once every five years. An examination shall be conducted for the purpose of determining the financial condition of the insurer, its ability to fulfill its obligations and its manner of fulfillment, the nature of its operations and its compliance with the Insurance Code. The director may also make such an examination of any surplus line agent or any person holding the capital stock of an authorized insurer or surplus lines agent for the purpose of controlling the management thereof as a voting trustee or otherwise, or both.

Subsections (2) and (3) do not apply and are omitted here.

**ORS 733.170 Accounts and records.**

An insurer shall keep its books, records, accounts and transaction source data in such manner that the director may readily verify its statements of financial condition and ascertain whether the insurer is unimpaired, has given proper treatment to policyholders and has complied with the Insurance Code.

**ORS 737.505 Insured entitled to rate information; remedies of aggrieved persons.**

(1) Every rating organization and every insurer which makes its own rates, within a reasonable time after receiving written request therefor and upon payment of such reasonable charge as it may make, shall furnish to any insured affected by a rate made by it, or to the authorized representative of such insured, all pertinent information as to such rate.

(2) Every rating organization and every insurer which makes its own rates shall provide within this state reasonable means whereby any person aggrieved by the application of its rating system may be heard, in person or by the authorized representative, on written request by the person or authorized representative to review the manner in which such rating system has been applied in connection with the insurance afforded the person. If the

rating organization or insurer fails to grant or reject such request within 30 days after it is made, the applicant may proceed in the same manner as if the application had been rejected.

(3) Any party affected by the action of such rating organization or such insurer on such request, within 30 days after written notice of such action, may appeal to the director, who, after a hearing held at a place designated by the director upon not less than 10 days' written notice to the appellant and to such rating organization or insurer, shall affirm or reverse such action.

(4) Appeals to the director pursuant to ORS 737.318 with regard to a final premium audit billing must be made within 60 days after receipt of the billing.

(5) The director may, upon a showing of good cause, stay any workers' compensation insurer's collection effort on a final premium audit billing during the pendency of an appeal authorized by subsection (4) of this section.

**ORS 744.051 Requirements for acting as agent; permissible activities; rules.**

(1) Except as otherwise provided in this section, a person shall not act as an agent in this state with respect to a domestic risk unless the person:

- (a) Holds a valid license or a temporary license issued by the director that authorizes the person to act as an agent; and
- (b) Is appointed by the insurer for whom the agent acts as an agent.

(2) An agent may act as an agent only with respect to those classes of insurance indorsed on the license of the agent.

(3) The director by rule may establish conditions and limitations:

- (a) Under which an agent may transact insurance that is otherwise authorized by the license of the agent with an insurer with whom the agent does not hold an appointment.
- (b) Under which a person may transact insurance on a domestic risk without a license as an agent in this state.

(4) An agent who is a surplus lines licensee may place insurance with an eligible surplus lines insurer as provided in ORS 735.400 to 735.495 without being appointed by the insurer.

(5) The provision of this section are subject to exemptions stated in ORS 744.057.

**ORS 744.054 Prohibition on appointing unlicensed person to be agent.**

- (1) An insurer or agent, with respect to domestic risks, shall not authorize or appoint a person to act as an agent for the insurer or agent if the person, while transacting insurance, does not hold a valid license as agent issued by the director.
- (2) The provisions of this section are subject to exemptions stated in ORS 744.057.

**ORS 744.057 Exemptions from agent licensing requirements.**

The following persons are exempt from the provisions of ORS 744.051 and 744.054:

- (1) Employees or representatives of insurers or agents, not receiving a commission, who perform administrative, clerical or technical services and who do not solicit insurance.
- (2) Salaried employees of insurers who solicit, negotiate or effect insurance only through licensed resident agents.
- (3) An attorney in fact of an authorized reciprocal insurer, or the salaried representatives of the insurer or attorney who receive no commissions.
- (4) Salaried employees of the holder of a master group insurance policy or salaried employees of a participant in an institutional retirement program, who, in the performance of ministerial duties on behalf of such holder or participant, secure and forward information for the purpose of group life and health insurance or institutional retirement programs or for enrolling individuals under such group coverages or issuing certificates thereunder, when no commission is paid for such services and the compensation, if any, paid is reasonably related to the services performed.
- (5) A person engaging in the lawful transaction of reinsurance.
- (6) Salaried employees of title insurance agents or insurers, except for the individual or individuals designated as exercising the powers conferred by a title insurance agent's license.
- (7) Any agent or representative of persons exempt from the Insurance Code under ORS 731.032 and 731.036, with respect to the exempted transactions.
- (8) Any agent or representative of a fraternal benefit society who devotes, or intends to devote, less than 50 percent of the agent's or representative's time to the solicitation and procurement of insurance policies for such society. Any person who in the preceding calendar year has solicited and procured life insurance policies on behalf of any society in an amount of insurance in excess of \$50,000 or, in the case of any other class or classes of

insurance which the society might write, on the persons of more than 25 individuals, and who has received or will receive a commission or other compensation therefor, shall be presumed to be devoting, or intending to devote, 50 percent of the person's time to the solicitation or procurement of insurance policies for such society.

(9) A person engaging in the lawful transaction of home protection insurance if the person is a real estate licensee as defined by ORS 696.010, and if the transaction of this insurance by the person is subject to a written contract, to which the insurer is a party, governing the person's activities in the transaction.

(10) Salaried employees of a banking institution or a national bank as defined in ORS 706.005, a savings association or a federal association as defined in ORS 722.004, a state credit union as defined in ORS 723.006 or a federal credit union, who, in the regular course of business with the customers of the banking institution, national bank, savings association, federal association or federal or state credit union, present the customers with written information about savings account annuities issued by an authorized insurer. Any person who purchases such an annuity may rescind the transaction within 10 days after the issuance of the contract. For purposes of this subsection, savings account annuities are annuities purchased with the proceeds of a savings account, certificate or share in a banking institution, national bank, savings association, federal association or federal or state credit union.

#### **ORS 744.155 Appointment of agents.**

(1) Each insurer appointing an agent in the state shall file written notice of the appointment with the director not later than the 30th day after the effective date of the appointment. The notice shall include the name and address of the agent and the class or classes of insurance or subclasses thereof to be transacted by the agent for the insurer. The insurer also shall pay the applicable fee established by the director.

(2) If the appointment includes any class of insurance, other than surety insurance, that is transacted under the general lines insurance class as provided in ORS 744.155, the insurer shall state thereon, with respect to such class, that the agent so appointed has authority to solicit, negotiate and effect policies of insurance on behalf of the insurer.

Subsections (3), and (4) are not applicable and have been omitted here.

#### **ORS 744.175 Termination of appointment.**

(1) An insurer may terminate an agency appointment at any time as provided in this section. Termination shall be without prejudice to the contracts rights, if any, of the agent so terminated. The insurer shall give written notice of the termination and the date thereof to the agent at least 90 days prior to the effective date of the termination. The notice must

specify the reasons for the termination. The insurer shall deliver the notice either in person or by mail at the address last provided by the agent to the insurer. The agent shall not have a cause of action against the insurer as a result of any statement in the notice unless the statement is false and the insurer knew the statement was false when made. The insurer shall also notify the director of the termination not later than the 30th day after the effective date of the termination. The director may require of the insurer reasonable proof that the insurer has given such notice to the agent.

(2) An insurer may terminate an agency appointment without giving the notice required by subsection (1) of this section on any of the grounds specified in this subsection. The insurer shall notify the director of any termination under this subsection and the date thereof not later than the 30th day after the effective date of the termination and shall notify the agent when reasonably possible. The director may require the insurer to give proof that the insurer has notified the agent. The following are grounds for termination under this subsection:

- (a) The agent's insurance license is denied, restricted, revoked, suspended or canceled by any public authority;
- (b) The agent's business is sold, transferred or merged and the insured has not appointed the successor;
- (c) The agent is insolvent or fails to remit balances to the insurer in accordance with the agreement;
- (d) The agent commits fraud or engages in intentional misconduct;
- (e) The insurer amends its certificate of authority in order to discontinue a line of insurance;
- (f) The insurer ceases selling insurance in this state; or
- (g) The insurer and agent mutually agree to terminate the agency appointment.

Subsection (3) is not applicable and has been omitted here.

#### **ORS 746.015 Discrimination; noncompliance; hearing.**

(1) No person shall make or permit any unfair discrimination between individuals of the same class and equal expectation of life, or between risks of essentially the same degree of hazard, in the availability of insurance, in the application of rates for insurance, in the dividends or other benefits payable under insurance policies, or in any other terms or conditions of insurance policies.

(2) Discrimination by an insurer in the application of its underwriting standards or rates based solely on an individual's physical handicap is prohibited, unless such action is based on sound actuarial principles or is related to actual or reasonably anticipated experience. For purposes of this subsection, "physical handicap" shall include, but not be limited to, blindness, deafness, hearing or speaking impairment or loss, or partial loss, of function of one or more of the upper or lower extremities.



(3) Discrimination by an insurer in the application of its underwriting standards or rates based solely upon an insured's or applicant's attaining or exceeding 65 years of age is prohibited, unless such discrimination is clearly based on sound actuarial principles or is related to actual or reasonably anticipated experience.

(4) If the director has reason to believe that an insurer in the application of its underwriting standards or rates is not complying with the requirements of this section, the director shall, unless the director has reason to believe the noncompliance is willful, give notice in writing to the insurer stating in what manner such noncompliance is alleged to exist and specifying a reasonable time, not less than 10 days after the date of mailing, in which the noncompliance may be corrected.

(5)(a) If the director has reason to believe that noncompliance by an insurer with the requirements of this section is willful, or if, within the period prescribed by the director in the notice required by subsection (3) of this section, the insurer does not make the changes necessary to correct the noncompliance specified by the director or establish to the satisfaction of the director that such specified noncompliance does not exist, the director may hold a hearing in connection therewith. Not less than 10 days before the date of such hearing the director shall mail to the insurer written notice of the hearing, specifying the matters to be considered.

(b) If, after the hearing, the director finds that the insurer's application of its underwriting standards or rates violates the requirements of this section, the director may issue an order specifying in what respects such violation exists and stating when, within a reasonable period of time, further such application shall be prohibited. If the director finds that the violation was willful, the director may suspend or revoke the certificate of authority of the insurer.

(6) Affiliated workers' compensation insurers having reinsurance agreements which result in one carrier ceding 80 percent or more of its workers' compensation premium to the other, while utilizing different workers' compensation rate levels without objective evidence to support such differences, shall be presumed to be engaging in unfair discrimination.

#### **ORS 746.650 Reasons for adverse underwriting decisions.**

(1) In the event of an adverse underwriting decision the insurer or agent responsible for the decision shall:

- (a) Either provide the applicant, policyholder or individual proposed for coverage with the specific reason or reasons for the adverse underwriting decision in writing or advise the person that upon written request the person may receive the specific reason or reasons in writing; and
- (b) Provide the applicant, policyholder or individual proposed for coverage with a summary of the rights established under subsection (2) of this section and ORS 746.640 and 746.645.

(2) Upon receipt of a written request within 90 business days from the date of the mailing of notice or other communication of an adverse underwriting decision to an applicant, policyholder or individual proposed for coverage, the insurer or agent shall furnish to the person within 21 business days from the date of receipt of the written request:

(a) The specific reason or reasons for the adverse underwriting decision, in writing, if this information was not initially furnished in writing pursuant to subsection (1) of this section;

(b) The specific items of personal information and privileged information that support these reasons, subject, however, to the following:

(A) The insurer or agent shall not be required to furnish specific items of privileged information if it has a reasonable suspicion, based upon specific information available for review by the director, that the applicant, policyholder or individual proposed for coverage has engaged in criminal activity, fraud, material misrepresentation or material nondisclosure.

(B) Specific items of medical record information supplied by a medical care institution or medical professional shall be disclosed either directly to the individual about whom the information relates or to a medical professional designated by the individual and licensed to provide medical care with respect to the condition to which the information relates, whichever the insurer or agent prefers; and

(c) The names and addresses of the institutional sources which supplied the specific items of information described in paragraph (b) of this subsection. However, the identity of any medical care institution or medical professional shall be disclosed either directly to the individual or to the designated medical professional, whichever the insurer or agent prefers.

(3) The obligations imposed by this section upon an insurer or agent may be satisfied by another insurer or agent authorized to act on its behalf.

(4) When an adverse underwriting decision results solely from an oral request or inquiry, the explanation of reasons and summary of rights required by subsection (1) of this section may be given orally.

#### **OAR 836-43-110 Insurer Premium Audit Program**

(1) The rates, rating plans and rating systems approved by and on file with the Insurance Division shall govern the audited payroll and the adjustment of premiums, subject to the provisions of this rule. An insurer shall make an actual audit of an employer's records for the purpose of determining the premium as follows:

(a) An insurer shall audit each policy producing an annual earned premium of \$10,000 or more at least once annually;

(b) An insurer shall audit five percent of all policies that are issued by the insurer and produce an annual earned premium of less than \$10,000 but more than \$1,000. In each year when such a policy is not audited, the insurer shall obtain a signed payroll statement from the employer. If neither an audit nor a signed

statement of payroll is obtained, the insurer shall give satisfactory reason therefore to the Division. Of the policies described in this subsection, the insurer shall first select such policies that show multiple classifications, high rates or indications of contract labor, or any combination of such criteria.

(2) When an insurer increases premium for an employer based on a premium audit the insurer shall include in the final premium audit billing a notice to the employer:

- (a) That the employer may appeal to the Director, as allowed by ORS 737.505; and
- (b) That the written request required to initiate the appeal must be received by the Director not later than the 60th day after the employer receives the final premium audit billing.

(3) The final premium audit billing must be entitled "Final Premium Audit Billing" at the top of the front page. The notice required in section (2) of this rule shall include the following wording, or substantially equivalent wording approved by the Director, that is prominently displayed and in not less than 12-point type.:

Notice: You, the employer, may appeal this final premium audit billing. You must initiate your appeal by submitting a written request for a hearing to the Director of the Department of Insurance and Finance, State of Oregon. Your request must be received by the Director not later than the 60th day after you received this billing.

Who may submit an employer's request?

1. If the employer is a sole proprietor, the employer or an attorney for the employer may submit the request.
2. If the employer is a partnership, an attorney for the partnership or any member of the partnership may submit the request.
3. If the employer is a corporation, association or organized group, an attorney for the corporation, association or organized group or an authorized officer or regular employee of the corporation, association or organized group may submit the request.
4. If the employer is a governmental authority other than a state agency, an attorney for the governmental agency or an authorized officer or employee of the governmental authority may submit the request.

Please state in your request the date on which you received your final premium audit billing.

The request for hearing must be sent to the following address:

Director, Department of Insurance and Finance  
c/o Hearings Unit  
Insurance Division  
440 Labor and Industries Building  
Salem, OR 97310

After you submit your request for hearing, the Insurance Division will provide you a petition form. In the petition, you must state the reasons you believe your insurer billed you incorrectly and describe the actions you wish the Director to take to correct the matter.

You are entitled to a hearing only if the Director has received your completed petition and has determined that the Director has jurisdiction over the matter.

You may send a copy of your request for hearing to your insurer so that you may attempt to resolve the dispute with your insurer prior to a hearing. You may seek resolution up to the time set for the hearing, but please remember:

1. The 60-day period for initiating your request continues to run even though you may be negotiating with your insurer.
2. Your request must be received at the address above not later than the 60th day after you received this billing.

You may wish to consult with an attorney about your case.

(4) In addition to the requirements of section (2) of this rule, if the premium audit billing is based in whole or part on a determination by the insurer that one or more persons are employees rather than an independent contractor, the insurer must also include in the notice with respect to each such person, an explanation of that determination. The explanation must name the person, designate or describe the position or tasks for which the person is determined to be an employee and give reasons for the determination.

(5) For purposes of this rule, the term "final premium audit billing" has the meaning given that term in OAR 836-43-170.

#### **OAR 836-43-120 Minimum Standard of Employer Education Program**

(1) At or before policy issuance, an insurer shall provide written reference materials to the employer-insured covering the following matters:

- (a) Which workers are subject to the Workers' Compensation Law for whom premiums must be paid;
- (b) What remuneration (or pay) is subject to premium charges;
- (c) How to divide payroll between assigned classifications;
- (d) The requirements for verifiable records;
- (e) The existence and nature of premium audits and the appeal process afforded employers by ORS 737.505;
- (f) The employer's responsibility to notify the insurer of changes in the business structure and operations;
- (g) The classification notice requirements prescribed by OAR 836-43-175 to 836-43-185.

(2) When the insurer becomes aware of changes in the employer's business that affect the reporting of payroll or other exposure basis, the insurer shall provide additional appropriate instruction to the employer.

(3) When changes in statute, rules or rating system occur that affect reporting of payroll or other exposure basis, the insurer shall provide notification of such changes to employers as soon as reasonably possible.

(4) The Bureau shall conduct seminars for insured employers covering the audit fundamentals of section (1) of this rule. Such seminars shall be held at least semi-annually in Portland, Salem, Eugene, Medford, Coos Bay, Bend and Pendleton.

(5) The Bureau shall continuously disseminate to its member insurers beneficial information relevant to auditing procedures, training and materials.

#### **OAR 836-81-010 Unfair Discrimination--Insurance Other Than Life or Health Insurance**

(1) Insurer decisions on the availability of insurance for individuals, other than life or health insurance, that are based on one of the following characteristics will be regarded as unfair discrimination:

- (a) Age of individuals;
- (b) Sex;
- (c) Marital status (i.e., single, married, separated, divorced);
- (d) Race or color;
- (e) Creed;
- (f) National origin;
- (g) Ancestry;
- (h) Occupation, if lawful, unless the occupation significantly increase (sic) the degree of hazard. This paragraph does not apply in the case of an insurer that limits its market to one occupation or several related occupations;
- (i) Change of occupation, unless the frequency of change is significant;
- (j) Change of domicile, unless the frequency of change is significant or the change significantly increases the degree of hazard or the expense of administering policy benefits;
- (k) Previous rejection, cancellation or nonrenewal of insurance by another insurer;
- (l) Change of insurer;
- (m) Lack of previous insurance, unless such was after August 31, 1978 and was in violation of law.

(2) A combination of several such characteristics may be the basis for such decisions only if the combination significantly increases the degree of hazard.

**OAR 836-85-225 Unfair Trade Practices**

(1) Retroactive application of experience rating modification factors in any manner other than provided for in OAR 836-85-215 constitutes an unfair trade practice under ORS 746.240.

(2) Failure of an insurer or rating organization to comply with the statistical reporting requirements of OAR 836-85-220 constitutes an unfair trade practice under ORS 746.240.



Table I.c.-1  
INVESTMENT INCOME YIELD AND TOTAL INVESTMENT YIELD

	Employers Ins. of Wausau			National Union Fire Ins. of PA			Grocers Insurance		
	1993	1994	1995	1993	1994	1995	1993	1994	1995
A Subtotal Cash & Invested Assets, Current Year	\$2,616,615,653	\$2,698,484,490	\$2,781,648,932	\$5,366,844,549	\$7,337,534,787	\$8,267,935,281	\$40,913,381	\$42,357,556	\$47,119,584
B Subtotal Cash & Invested Assets, Previous Year	2,637,121,133	2,616,615,653	2,698,484,490	5,052,646,341	5,366,844,549	7,337,534,787	35,780,989	40,913,381	42,357,556
C Accrued Interest, Dividends & Real Estate Income Du	34,969,905	35,451,093	38,279,745	94,213,461	87,099,467	93,208,787	733,784	824,981	843,361
D Accrued Interest, Dividends & Real Estate Income Du	36,628,704	34,969,905	35,451,093	93,185,315	94,213,461	87,099,467	640,544	733,784	824,981
E Borrowed Money, Current Year	0	0	0	0	0	0	0	0	0
F Borrowed Money, Previous Year	0	0	0	0	0	0	0	0	0
G Net Investment Income Earned, Current Year	164,892,053	160,662,481	297,080,599	309,626,237	292,470,395	329,670,664	2,669,894	2,669,583	2,951,998
Investment Yield (2*G)/(A+B+C+D-E-F-G) /1	6.39%	6.15%	11.30%	6.01%	4.84%	4.27%	7.08%	6.50%	6.69%
H Realized Gains	12,819,077	2,669,651	10,930,219	151,118,364	(25,400,684)	109,266,898	1,500	28,757	161,687
Total Investment Yield (2*(G+H))/(A+B+C+D-E-F-G)	6.89%	6.25%	11.72%	8.95%	4.24%	5.68%	7.09%	6.57%	7.06%

	Liberty Northwest				SAIF			
	1992	1993	1994	1995	1992	1993	1994	1995
A Subtotal Cash & Invested Assets, Current Year	\$487,098,248	\$523,107,697	\$566,368,377	\$609,160,362	\$1,480,989,264	\$1,597,907,411	\$1,683,112,177	\$1,746,972,713
B Subtotal Cash & Invested Assets, Previous Year	442,816,836	487,098,248	523,107,697	566,368,377	1,357,512,358	1,480,989,264	1,597,907,411	1,683,112,177
C Accrued Interest, Dividends & Real Estate Income Du	9,764,277	9,761,900	11,001,328	10,813,485	30,457,062	30,501,443	33,425,056	31,410,610
D Accrued Interest, Dividends & Real Estate Income Du	9,678,762	9,764,277	9,761,900	11,001,326	26,577,262	30,457,062	30,501,443	33,425,056
E Borrowed Money, Current Year	0	0	0	0	0	0	0	0
F Borrowed Money, Previous Year	0	0	0	0	0	0	0	0
G Net Investment Income Earned, Current Year	34,553,138	36,032,750	37,121,328	39,652,110	111,279,252	112,647,166	115,250,569	119,877,379
Investment Yield (2*G)/(A+B+C+D-E-F-G) /1	7.55%	7.25%	6.92%	6.85%	7.99%	7.44%	7.14%	7.10%
H Realized Gains	2,172,000	973,597	468,712	2,482,920	15,815,000	33,423,000	13,421,219	20,323,849
Total Investment Yield (2*(G+H))/(A+B+C+D-E-F-G)	8.03%	7.45%	7.01%	7.28%	9.13%	9.65%	7.97%	8.31%

Note:

1. Investment income yield is computed according to the NAIC Insurance Regulatory Information System accepted formulas.
2. Data for A, B, C & D from page 2, data for E & F from page 3 and data for G & H from page 4 of Annual Statements.
3. Data is reported on a consolidated basis, and does not necessarily reflect only Oregon Business.

Source: Department of Consumer and Business Services, Information Management Division, May 1994.



**Table I.c.-2  
DISTRIBUTION OF CASH AND INVESTED ASSETS - 5 YEAR HISTORICAL DATA**

	Employers Ins. of Wausau							National Union Fire Ins. of PA							Grocers Insurance Company						
	1995	1994	1993	1992	1991	1990	1989	1995	1994	1993	1992	1991	1990	1989	1995	1994	1993	1992	1991	1990	1989
Bonds	90.4%	84.7%	86.2%	87.7%	87.1%	84.4%	83.3%	49.7%	48.6%	69.0%	69.7%	70.4%	70.2%	64.4%	81.7%	88.1%	84.9%	86.1%	79.8%	71.8%	68.9%
Stocks	6.3%	10.9%	8.6%	7.7%	8.1%	8.0%	7.7%	43.5%	44.0%	18.9%	19.2%	19.9%	20.6%	21.7%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Mortgage Loans on Real Estate	0.1%	0.3%	0.3%	0.4%	0.4%	0.3%	0.3%	0.0%	0.0%	0.0%	0.4%	0.4%	0.0%	0.0%	0.0%	0.0%	1.2%	1.3%	1.5%	2.1%	2.6%
Real Estate	1.5%	1.6%	1.6%	1.6%	1.5%	1.6%	1.7%	0.0%	0.1%	0.1%	0.1%	0.1%	0.0%	0.1%	1.1%	1.2%	1.3%	1.6%	1.9%	2.7%	3.3%
Collateral Loans	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Cash & Short Term Investments	1.3%	2.4%	2.8%	2.2%	2.1%	4.6%	5.5%	1.3%	3.4%	6.4%	5.5%	3.4%	7.0%	12.4%	17.2%	10.6%	12.6%	11.0%	16.9%	23.4%	25.2%
Other Invested Assets	0.3%	0.2%	0.5%	0.5%	0.8%	1.1%	1.4%	5.5%	4.0%	5.6%	5.1%	5.8%	2.1%	1.4%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Aggregate Write-ins for Invested Assets	0.1%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
<b>Cash &amp; Invested Assets</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

	Liberty Northwest								SAIF							
	1995	1994	1993	1992	1991	1990	1989	1988	1995	1994	1993	1992	1991	1990	1989	1988
Bonds	94.5%	99.8%	98.5%	98.2%	96.5%	94.6%	92.0%	97.0%	88.1%	86.1%	87.9%	88.3%	83.5%	86.4%	84.8%	82.5%
Stocks	3.5%	0.2%	0.2%	1.8%	2.1%	1.4%	0.8%	0.0%	7.7%	6.2%	6.5%	6.1%	6.2%	5.8%	5.8%	5.1%
Mortgage Loans on Real Estate	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.6%	0.9%	1.6%	2.6%	3.8%	4.9%	5.6%	7.2%
Real Estate	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.5%	1.2%	0.6%	0.4%	0.4%	0.5%	0.5%	0.6%
Collateral Loans	0.0%	0.0%	1.3%	0.0%	1.4%	4.0%	7.2%	3.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Cash & Short Term Investments	2.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.2%	4.3%	3.4%	2.6%	6.0%	2.5%	3.3%	4.6%
Other Invested Assets	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.0%	1.3%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Aggregate Write-ins for Invested Assets	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
<b>Cash &amp; Invested Assets</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

Note:

1. Data from page 20 of Annual Statement
2. Data is reported on a consolidated basis.

Source: Department of Consumer and Business Services, Information Management Division, May 1994.

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Table I.c.-3 Comparison of Invested Assets and Premiums

	Gross Premiums Written	Net Premiums Earned	Ratio of Mean Cash and Invested Assets	
			to GPW	to NPE
<b>Employers Insurance of Wausau</b>				
1993	3,492,058,817	1,344,824,004	0.75	1.95
1994	2,922,529,525	1,354,532,236	0.91	1.96
1995	2,642,383,235	1,415,727,786	1.04	1.94
<b>National Union Fire Ins of PA</b>				
1993	9,745,933,283	2,151,548,113	0.53	2.42
1994	10,629,466,729	2,284,862,272	0.60	2.78
1995	11,165,222,302	2,387,789,812	0.70	3.27
<b>Grocers Insurance</b>				
1993	25,910,069	18,583,922	1.48	2.06
1994	24,534,597	18,592,908	1.70	2.24
1995	27,729,217	20,434,057	1.61	2.19
<b>Liberty Northwest Ins Corp</b>				
1993	161,406,829	142,611,425	3.13	3.54
1994	189,044,547	168,906,850	2.88	3.23
1995	196,972,952	179,067,026	2.98	3.28
<b>SAIF</b>				
1993	277,026,465	353,116,151	5.56	4.36
1994	284,674,237	273,996,168	5.76	5.99
1995	269,684,360	250,560,246	6.36	6.84

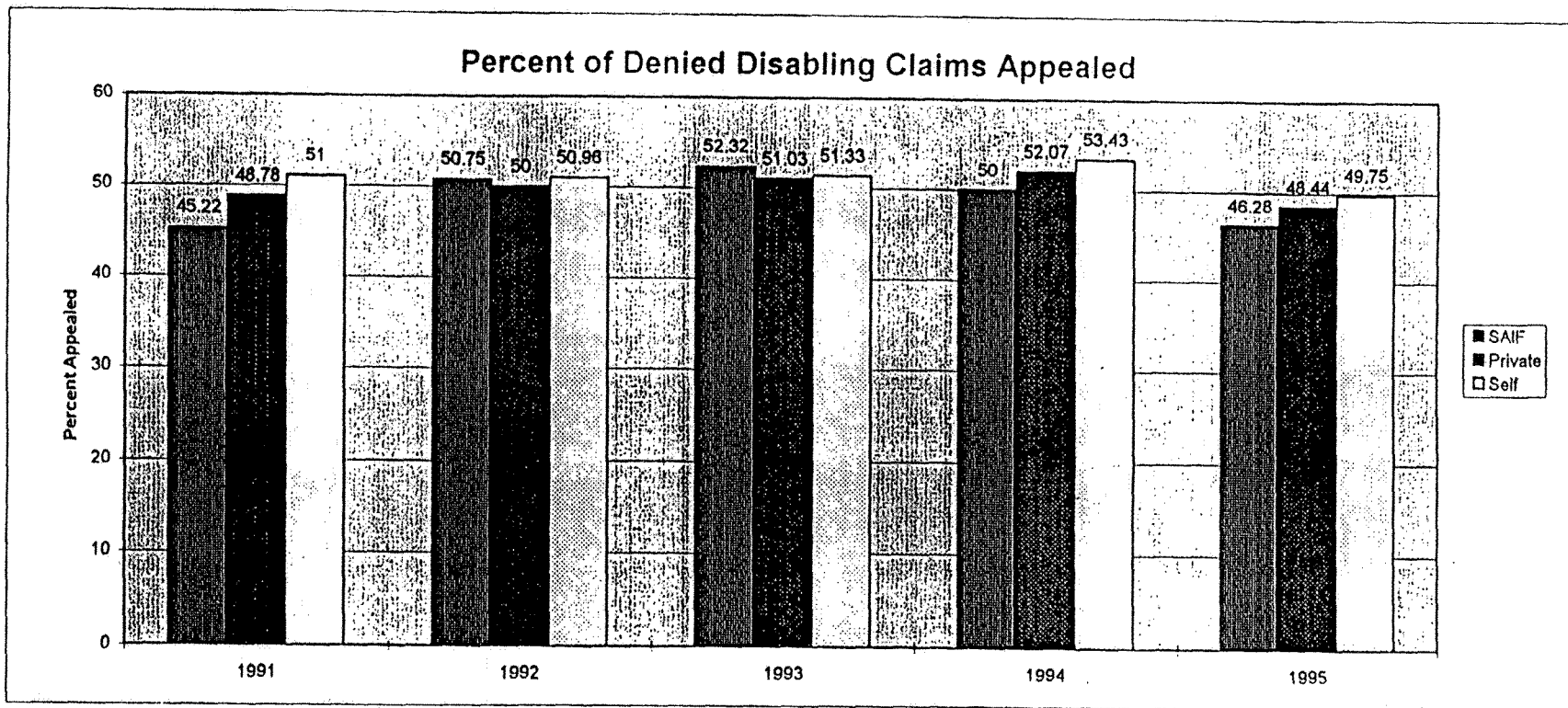
**Notes:**

1. Gross premiums written from Five-Year Summary, Page 22, 1995 Annual Statement
2. Net Earned Premium from Statement of Income, Page 4, Annual Statement
3. Invested Assets from Table I.c.-2

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Hearing Request Percentage Rates on Denied Disabling Claims

Year	SAIF	Private	Self
1991	45.22	48.78	51
1992	50.75	50	50.96
1993	52.32	51.03	51.33
1994	50	52.07	53.43
1995	46.28	48.44	49.75



Source: Information Management Division, Department of Consumer and Business Services, October, 1996.

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Secretary of State

State of Oregon

SAIF CORPORATION

Salem, Oregon

For the Year Ended December 31, 1995



Audits Division

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Secretary of State

State of Oregon

**SAIF CORPORATION**

Salem, Oregon

For the Year Ended December 31, 1995



**Audits Division**

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Secretary of State

Audits Division

*Auditing for a Better Oregon*

The Honorable John Kitzhaber  
Governor of Oregon  
State Capitol  
Salem, Oregon 97310

Katherine Keene, President & CEO  
SAIF Corporation  
400 High Street SE  
Salem, Oregon 97312

This audit was conducted for the purpose of reporting on SAIF Corporation's financial statements as of and for the year ended December 31, 1995, and on the internal control structure and compliance with applicable laws and regulations.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

As also required by those standards, we reviewed the internal control structure of SAIF Corporation in order to determine the audit procedures necessary to gather sufficient competent evidence in support of our opinion on the financial statements. We also performed tests of SAIF's compliance with applicable laws and regulations. Our comments regarding internal controls and compliance with legal requirements are presented in the Audit Results section of this report.

OREGON AUDITS DIVISION

Don Waggoner, CPA  
State Auditor

Fieldwork Completion Date:  
July 8, 1996



## INTRODUCTION

### ORGANIZATION AND FUNCTIONS

SAIF Corporation is an independent public corporation created by an act of the 1979 Oregon Legislature. It is governed by a board of five directors appointed by the Governor. The function of the board of directors is to establish policies for the operation of SAIF. The board also appoints a president and chief executive officer, a position held by Katherine Keene since September 1992.

SAIF Corporation was created for the purpose of transacting workers' compensation insurance and reinsurance business. It is the largest workers' compensation insurer in the state of Oregon. SAIF furnishes employers with complete coverage and promotes safety programs for the benefit of employers as well as employees.

Oregon has a "three-way" workers' compensation system: employers may choose to purchase coverage from SAIF, to purchase coverage from a private insurer, or to self insure. The Attorney General has indicated that a central reason for SAIF's existence is to act as a competitive force in the workers' compensation marketplace.

### FINANCIAL ACTIVITIES

SAIF's operating revenues are obtained primarily from workers' compensation insurance premiums and from investment income. These revenues provide the resources needed to pay claim losses incurred. All transactions arising from these activities are recorded in the Industrial Accident Fund. As of December 31, 1995, SAIF had total assets of approximately \$2.1 billion, including \$1.9 billion in cash and investments. Liabilities at that date totaled \$1.7 billion, \$1.5 billion of which consists of the reserve for future payments on losses and loss adjustment expenses that have been incurred.

In past years, we have audited SAIF's financial statements for fiscal years ending June 30. Beginning with this audit report, we will audit SAIF's statements for the calendar years ending December 31.

**AUDIT RESULTS****REPORT ON THE  
INTERNAL CONTROL  
STRUCTURE**

We have audited the financial statements of SAIF Corporation (SAIF) as of and for the year ended December 31, 1995, and have issued our report thereon dated July 8, 1996.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of SAIF is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audits of the financial statements of SAIF, for the year ended December 31, 1995, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in

operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operations that we consider to be material weaknesses as defined above.

#### **REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS**

Compliance with laws and regulations applicable to SAIF is the responsibility of SAIF's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of SAIF's compliance with certain provisions of laws and regulations. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under *Government Auditing Standards*.

## FOLLOW-UP ON PRIOR AUDIT FINDING

### LOSS RESERVE ESTIMATES ARE CONSERVATIVE

As with any insurer, SAIF's largest liability consists of the reserve for future payments on losses that have been incurred. SAIF engages an actuarial firm to estimate most of this liability. Reserves are reevaluated and adjusted each calendar quarter. Increases or decreases in the reserve are reflected in claims expense for that quarter.

In our last audit report, for the year ending June 30, 1995, we commented that the conservative assumptions and methodologies adopted by SAIF resulted in establishing its total reserve at the high end of a range of possible results. SAIF has not made changes to its assumptions and methodologies for the current evaluation; thus the reserves are still estimated conservatively.

SAIF management is currently performing a review of its reserving assumptions and methodologies in connection with the estimation of reserves for June 30, 1996. Changes will be considered at the August 1996 Board of Directors meeting.

## **REPORT DISTRIBUTION**

This report is a public record and is intended for the information of SAIF Corporation management, the governor of the state of Oregon, the Oregon Legislative Assembly, and all other interested parties.

## **COMMENDATION**

The courtesies and cooperation extended by officials and employees of SAIF Corporation during the course of the audit were very commendable and are sincerely appreciated.

## **AUDIT TEAM**

Joel Leming, CPA, Audit Administrator  
Sheila Orton, CPA  
Margaret Kane, CPA  
Anne Lawrence





Secretary of State

Audits Division

*Auditing for a Better Oregon*

The Honorable John Kitzhaber  
Governor of Oregon  
State Capitol  
Salem, Oregon 97310

Katherine Keene, President & CEO  
SAIF Corporation  
400 High Street SE  
Salem, Oregon 97312

## INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying balance sheet of SAIF Corporation as of December 31, 1995, and the related statements of income, retained earnings, and cash flows for the year then ended. These financial statements are the responsibility of SAIF management. Our responsibility is to express an opinion on the statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of SAIF Corporation as of December 31, 1995, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

The financial statements at December 31, 1995, include loss reserves valued at \$1,320,979,000 and loss adjustment expense reserves valued at \$205,664,000. Together, these accounts comprise 87.7 percent of SAIF's total liabilities. As discussed in Note (2), these values were estimated by SAIF management. The loss reserve estimates are based primarily on evaluations prepared by loss reserve specialists. We have reviewed the

procedures used by management in estimating reserves and have inspected documentation prepared by SAIF's loss reserve specialists. We believe that SAIF's estimates are conservative. However, given the degree of uncertainty inherent in the evaluation process, a wide range of estimates is acceptable. It should be noted that actual results may differ significantly from estimated values depending on the actuarial methods and assumptions used in estimating loss reserves, and the differences could be material.

## OREGON AUDITS DIVISION



Don Waggoner, CPA  
State Auditor

July 8, 1996

## SAIF CORPORATION

## Balance Sheet

December 31, 1995

(Expressed in thousands)

Assets	
Investments:	
Bonds, at Amortized Cost	\$1,541,440
Equity Securities, Principally at Market (Cost \$108,015)	134,556
Other Invested Assets	17,327
Deferred Compensation	13,786
Mortgage Loans on Real Estate, at Amortized Unpaid Balance	9,723
Deposit With Reinsurer	127,843
Cash	20,812
Restricted Cash	66,805
Accrued Investment Income	37,258
Premiums in Course of Collection (Net of Allowance for Uncollectibility of \$5,435)	106,680
Reinsurance Recoverable	418
Due from Workers' Compensation Division	25,349
Other Assets (Net of Allowance for Uncollectibility of \$1,125)	9,527
Property and Equipment (Net of Accumulated Depreciation of \$20,684)	32,760
<b>Total Assets</b>	<b>\$2,144,284</b>
Liabilities and Retained Earnings	
Policy Liabilities and Accruals:	
Loss Reserves	\$1,320,979
Loss Adjustment Expense Reserves	205,664
Unearned Premiums	33,443
Due to Reinsurers	3,212
Other Policyholders' Funds:	
Premium Deposits	10,660
Dividends	50,000
Due to Policyholders for Settlement against State of Oregon	66,805
Deferred Compensation Payable	13,786
Due to Workers' Compensation Division	13
Premium Taxes Payable	25,579
Accounts Payable and Other Liabilities	10,196
<b>Total Liabilities</b>	<b>\$1,740,337</b>
Retained Earnings:	
Net Income Retained	377,453
Unrealized Appreciation of Equity Securities	26,494
<b>Total Retained Earnings</b>	<b>\$ 403,947</b>
<b>Total Liabilities and Retained Earnings</b>	<b>\$2,144,284</b>

The accompanying notes are an integral part of the financial statements.

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**SAIF CORPORATION**  
**Statement of Income**  
Year ended December 31, 1995  
(Expressed in thousands)

Premiums and Other Revenues:

Net Premiums Earned	\$ 241,847
Net Investment Income	128,904
Net Realized Capital Gains	20,654
Other Income (Expenses)	(1,336)

Total Operating Revenues 390,069

Losses and Expenses:

Incurred Losses	198,763
Loss Adjustment Expense	58,228
Policyholder Dividends	130,189
Underwriting Expenses	57,242

Total Losses and Expenses 444,422

Income Before Extraordinary Items and Cumulative  
Effect of a Change in Accounting Principle \$ (54,353)

Extraordinary Loss from Recognition of Liability (81,000)

Cumulative Effect of a Change in Accounting Principle (23,136)

Net Income \$(158,489)

The accompanying notes are an integral part of the financial statements.

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**SAIF CORPORATION**  
**Statement of Retained Earnings**  
Year ended December 31, 1995  
(Expressed in thousands)

Balance Beginning of Year	\$ 539,806
Adjustment for the Cumulative Effect on Prior Years of Change in Method of Accounting for Deposit with Reinsurer (Note 11)	8,778
Restated Beginning Retained Earnings	<u>\$ 548,584</u>
Net Income (Loss)	(158,489)
Increase (Decrease) in Unrealized Appreciation of Equity Securities	<u>13,853</u>
Retained Earnings End of Year	<u><u>\$ 403,948</u></u>

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The accompanying notes are an integral part of the financial statements.

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**SAIF CORPORATION**  
**Statement of Cash Flows**  
Year ended December 31, 1995  
(Expressed in thousands)

<b>Operating Activities</b>	
Net Income	\$(158,489)
Adjustments to Reconcile Net Income to	
Net Cash Provided by Operating Activities:	
Change in Premiums Receivable, Unearned	
Premiums, and Policyholders' Funds	59,237
Increase in Accrued Investment Income	300
Amortization of Bond and Mortgage Premium	
and Discount (Net)	(2,053)
Change in Accrued Loss and Loss Adjustment	
Expense Reserves	89,747
Change in Other Assets, Other Liabilities	
and Accrued Premium Taxes	119,702
Provision for Depreciation	5,510
Net Realized Gains on Investments	(20,654)
	<hr/>
Net Cash Provided by Operating Activities	\$ 93,300
<b>Investing Activities</b>	
Purchases of Investments and Loans Made	\$(671,494)
Sales or Maturities of Investments and	
Receipts from Repayment of Loans	597,823
	<hr/>
Net Cash Used by Investing Activities	\$ (73,671)
<b>Capital Financing Activities</b>	
Purchase of Property and Equipment	\$ (4,578)
	<hr/>
Increase in Cash	\$ 15,051
Cash at Beginning of Year	72,566
	<hr/>
Cash at End of Year	<u>\$ 87,617</u>

The accompanying notes are an integral part of the financial statements.



**SAIF CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 1995**

(1)

**ORGANIZATION**

The Company is a public corporation created by an act of the Oregon Legislature. It traces its origins to 1914 when its predecessor organization commenced business.

SAIF is an insurance company authorized to write workers' compensation coverage in Oregon and certain other jurisdictions. The Corporation's Board of Directors is appointed by the Governor of the State and consists of prominent Oregon business and community leaders, not otherwise in the employ of the Company.

(2)

**SUMMARY OF SIGNIFICANT  
ACCOUNTING POLICIES**

**A. Basis of Accounting**

SAIF Corporation prepares financial statements in conformity with statutory accounting practices which are prescribed for use in reporting accounting transactions for insurance companies. These practices arise from state laws and from rules adopted by the State Insurance Commissioner and, for Oregon, are usually the practices promulgated by the National Association of Insurance Commissioners. Statutory accounting practices are very conservative in nature and are designed to protect policyholders to ensure that in the event of liquidation, sufficient amounts will have been set aside to provide for policyholder benefits. See Note (9).

At the request of the Secretary of State's Audits Division, SAIF Corporation has prepared the accompanying financial statements on the basis of generally accepted accounting principles. As a component unit of the State of Oregon, generally accepted accounting principles are applied in a manner consistent with the State of Oregon. In accordance with Statement 20 of the Governmental Accounting Standards Board, SAIF Corporation has determined that only Statements of the Financial Accounting Standards Board issued prior to November 30, 1989 are applicable to its financial statements. Generally accepted accounting principles differ in some respects from the statutory accounting practices noted above in that generally accepted accounting principles are based on the going-concern concept and place more emphasis on assigning income and expenses to their proper period.

The following is a description of the significant accounting policies and practices employed by the Company:

## (2)-Continued

## B. Loss and Loss Adjustment Expense Reserves

The liability for claims and claim adjustment expenses is generally based on past experience, except for certain awarded claims which are determined on a case basis. The liability includes provisions for reported claims, claims incurred but not reported, and claims that are currently closed but which experience indicates will be reopened.

The reserves for claim and claim adjustment expenses are considered adequate to cover the discounted present value of the ultimate net cost of losses incurred through the respective dates. However, the provision is necessarily predicated on estimates of actual future costs and investment earnings, which may vary from the amounts that are ultimately paid and received. Estimates for the reserves are continually under review, and adjustments are reflected in the income of the period they are made.

The discount rate that SAIF Corporation uses should reflect the anticipated rate of return on investments taking into consideration the uncertainty inherent in long pay-out patterns (see Attorney General Opinion Number 6176). Annually, the Board of Directors reviews the actuarial assumptions and discount rates utilized in determining loss reserve liabilities.

Currently, the Company discounts the liability for unpaid fatal and permanent total disability losses at 4 percent per annum. The discount reflected in the claim reserves at December 31, 1995 totaled \$154.3 million.

As part of the ongoing review of loss reserves, a number of assumptions were revised and methods for developing reserves were refined. The most significant change resulted from the passage of Senate Bill 369. This bill reversed the erosion of workers' compensation reforms which were put in place with earlier legislation. Therefore, the Company was able to eliminate approximately \$42.3 million in supplemental reserves which had been previously established for erosion of workers' compensation reforms. These changes were considered to be part of the normal estimation process and the changes from such adjustments are included as part of incurred losses for the current year.

Another significant change in loss reserves has come from the downward development of prior year reserves. On a discounted basis, the downward development of prior year reserves was approximately \$45.8 million for 1995. This downward development is in addition to the supplemental reserves reduction mentioned above, for a total of \$88.1 million downward development.

The Company does not discount unpaid loss adjustment expenses which is a change from previous years. Had these unpaid loss adjustment expenses been discounted at December 31, 1995, the amount of discounted loss adjustment expense reserves would have been \$181.3 million. The change in discounting on loss adjustment expense reserves has been treated as a change in accounting principle. Therefore, the cumulative effect of this change

Notes to Financial Statements (continued)  
December 31, 1995

(2)-Continued

has been recorded as an extraordinary item on the Statement of Income. The effect of this change reduced income \$23.1 million.

C. Policyholder Dividends

Dividends to policyholders are charged against income as declared by the Board of Directors. The liability at December 31, 1995 consists of estimated unpaid policyholder dividends. See Note (5).

D. Taxes and Assessments

The Company, in common with all other carriers licensed to write workers' compensation insurance in Oregon, is subject to levies by the Oregon Workers' Compensation Division of the Department of Consumer and Business Services. Such assessments constitute an in-lieu-of-tax relative to premiums.

E. Property and Equipment

Depreciation of real estate owned and occupied by the Company, automobiles, furniture and equipment, is provided over their estimated useful lives on the straight-line method. Maintenance and repairs are charged to income as incurred. Upon retirement or sale, any resulting gain or loss is credited or charged to income.

The following schedule summarizes the fixed assets of the Company at December 31, 1995, (expressed in thousands):

Land	\$ 3,392
Buildings	26,300
Equipment and Machinery	21,131
Data Processing Software	2,621
Less Allowance for Depreciation	<u>(20,684)</u>
	<u>\$32,760</u>

F. Investments

Bonds and short-term investments are carried primarily at amortized cost with discount and premium amortizations calculated on the effective-yield basis. Mortgage loans on real estate are stated at their amortized unpaid balances. Equity securities are carried at market value.

Realized investment gains and losses are determined on the basis of specific identification and are included in the income statement as a component of net income. Unrealized gains and losses on securities carried at market are reflected as direct increases or decreases in the Company's equity accounts. See Note (3).

(2)-Continued

G. Premium Revenue Recognition

Workers' compensation insurance premiums are recognized as income over the period for which coverage is provided. Collection of certain premiums included in income is deferred until subsequent to the policy year as set forth in Note (4).

A number of the insurance contracts issued by the Company contain a provision for a retroactive premium adjustment predicated on the loss experience of the policyholder. With respect to these loss-sensitive policies, retrospective rating valuations are performed on a periodic basis with the resulting premium amounts charged or credited to operations through adjustments to earned premiums. An estimate of the ultimate amounts payable to or receivable from policyholders for retrospective ratings not yet perfected is made for reporting purposes. Estimated amounts due policyholders are shown as a liability and charged as a reduction of earned premiums, while estimated amounts the Company are included in earned premiums and in premiums in course of collection.

(3)

CASH AND INVESTMENTS

The State Treasurer is the Company's investment officer, investing in an instrument in which persons of prudence, discretion and intelligence would invest for their own accounts. The Oregon Investment Council is responsible for establishing investment policy. On stock acquisitions are limited to 50 percent of the moneys contributed. The State Treasurer is prohibited from investing in common stock. Oregon Investment Council common stock investments are made by independent investment managers selected and evaluated by the Council.

The investments are categorized to provide an indication of the level of risk the company assumed at year end. Categories are:

1. Insured or registered, or securities held by the entity or its agent in the entity's name.
2. Uninsured and unregistered, with securities held by the counter-part department or agent in the entity's name.
3. Uninsured and unregistered, with securities held by the counter-part's own trust department or agent, but not in the entity's name.

A summary of risk categories, carrying values and market values as of December 31, 1995, (expressed in thousands):

Notes to Financial Statements (continued)  
December 31, 1995

(3)-Continued

	CATEGORY			Carrying Value	Market Value
	1	2	3		
<b><u>Classified as to Risk</u></b>					
Bonds					
Governments	\$ 836,199			\$ 836,199	\$ 862,994
Public Utilities	369,288			369,288	375,764
Industrials	<u>328,298</u>			<u>328,298</u>	<u>343,197</u>
Total Bonds	\$1,533,785	\$0	\$0	\$1,533,785	\$1,581,955
Equity Securities	<u>51,149</u>			<u>51,149</u>	<u>52,151</u>
Investments Classified as to Risk	<u>\$1,584,934</u>	<u>\$0</u>	<u>\$0</u>	<u>\$1,584,934</u>	<u>\$1,634,106</u>

	Carrying Value	Market Value
<b><u>Unclassified as to Risk</u></b>		
Bonds	\$ 7,655	\$ 7,367
Equity Securities	83,407	83,407
Other Invested Assets	17,327	20,621
Deferred Compensation	13,786	13,786
Real Estate Mortgage Loans	<u>9,723</u>	<u>9,723</u>
Risk Unclassified Investments	<u>\$ 131,898</u>	<u>\$ 134,904</u>
Total Investments	<u>\$1,716,832</u>	<u>\$1,769,010</u>

The aggregate cost and market value of common stock and other equity participations at December 31, 1995 are set forth below (expressed in thousands):

	Cost	Market Value
Well Fargo Industrial Fund	\$ 60,830	\$ 83,407
Other Equity Securities	47,185	52,151
Other Invested Assets	<u>18,833</u>	<u>20,621</u>
Total	<u>\$126,848</u>	<u>\$156,179</u>

(3)-Continued

Investment income of SAIF as of December 31, 1995 is summarized as follows  
 (expressed in thousands):

Bonds	\$107,335
Equity Securities	8,562
Real Estate Mortgage Loans	1,211
Interest on Deposit with Reinsurer	7,407
Interest on Cash Balances	4,511
Other Investment Income	998
Real Estate Income	<u>314</u>
Total	\$130,338
Investment Expense	<u>(1,434)</u>
Investment Income Earned	<u>\$128,904</u>

Realized gains and losses on sales or other dispositions of investments, as determined on a specific identification basis at December 31, 1995, are as follows (expressed in thousands):

Bonds	\$15,086
Equity Securities	5,658
Real Estate Mortgage Loans	<u>(90)</u>
Total	<u>\$20,654</u>

SAIF participates in securities lending agreements whereby securities are loaned to a broker/dealer for a fee. The borrowing broker/dealer pledges and maintains collateral. The collateral for loaned debt securities and loaned equity securities is held by the trustee, First Interstate Bank Portfolio Lending Services. At December 31, 1995, the market value for the securities loaned was \$9.2 million and the related collateral was \$9.5 million.

Cash equivalents are defined as cash held in the State Treasury and cash on deposit outside the State Treasury. At December 31, 1995, the total of cash on deposit and short term investments with the State Treasurer was \$13.5 million, and the book balance was \$2.6 million. The difference between book balance and State Treasury balance consists primarily of deposits in transit and outstanding checks. Additionally, \$66.8 million on deposit with the State Treasury is restricted to distributions in settlement of Alsea Veneer, Inc. v. State of Oregon as directed by the Marion County Court. The portion of these funds which consists of cash on deposit in state banks is covered by federal deposit insurance or is secured by the State Treasury at a minimum of 25 percent as required by statutes. The portion which consists of short-term investments is insured or secured with securities held by the State Treasurer or by its agent in the Treasurer's name.



## (3)-Continued

Investment managers' deposits with a custodian bank consist of cash and cash equivalents that represent buying reserves. The amount on deposit with First Interstate Bank of Oregon was \$16.2 million and the book balance was \$18.2 million as of December 31, 1995. Although the deposit is in an interest bearing account, the deposits are neither collateralized nor insured. However, these deposits are backed by the faith and credit of First Interstate Bank.

At December 31, 1995, the Company has on deposit with a reinsurer \$127.8 million, which is not insured or collateralized. While ORS Chapter 656 requires that all moneys received by SAIF be deposited with the State Treasurer, the Company followed the advice of the Attorney General at the time it entered into this transaction.

Petty cash funds for the Company are maintained at commercial banks. At year-end, the total of the accounts was approximately \$16 thousand, all of which was covered by federal deposit insurance.

## (4)

**PREMIUMS IN COURSE  
OF COLLECTION**

As permitted by Oregon law, the majority of SAIF's premiums are determined and billed only after completion of the modal premium period. Accordingly, to properly recognize premiums as income earned during the coverage period, a receivable for premiums earned but not billed is established based on historical experience with respect to premiums collected subsequent to the coverage period.

The Company also offers plans of insurance wherein the collection of a portion of the earned premium, representing the estimated future claims cost, is deferred for a valuation period extending up to 4½ years subsequent to the close of the policy year. Such premium deferrals are adjusted monthly for the cost of claims. At the close of the evaluation period, the Company settles with the policyholder with regard to any premium amounts that may be due or returnable.

## (5)

**POLICYHOLDER  
DIVIDENDS**

A portion of the Company's business is written under various participating plans wherein a dividend may be returned to the policyholder. The determination of the dividend as well as the amount is predicated upon the Company's overall experience. A dividend of approximately \$30.1 million was declared in June 1995 and paid shortly thereafter. As a result of continued positive financial performance and because of the passage of Senate Bill 369, which allowed the Company to release supplemental loss reserves, the Board declared a supplemental dividend of approximately \$50.1 million which was distributed to policyholders who had coverage with the

(5)-Continued

Company over the previous four and one half years. Subsequent to December 31, 1995, the Board of Directors declared a policyholder dividend of approximately \$50 million. The dividend was declared at the April, 1996 meeting of the Board of Directors. It is the intent of the Company to share the benefits of the Company's positive financial results with policyholders in the form of rate reductions, when prudent to do so, and dividends.

(6)

**REINSURANCE**

The Company maintains reinsurance agreements with other insurance companies. The agreements generally provide for recovery by SAIF of selected per-occurrence or per claim losses to the extent that such losses exceed \$2 million and are incurred during the reinsurance coverage period or in the event that certain adverse loss reserve development occurs. Amounts so recoverable are subject to limitations. As of December 31, 1995, recoveries of \$32.7 million were recoverable to SAIF under the terms of these agreements.

(7)

**RETIREMENT PLAN**

SAIF Corporation employees participate in the Oregon Public Employee's Retirement System (PERS), which includes a cost sharing, multiple employer, defined benefit public employee retirement system for state agencies. The payroll for employees covered by PERS for the year ended December 31, 1995, was \$38.4 million and the total payroll for that period was \$40.0 million. All SAIF Corporation employees are eligible to participate in the system after completing six months of service. The PERS retirement allowance, payable monthly for life, may be selected from 12 retirement benefit options. Options include survivorship benefits and lump sum refunds. The basic benefit formula is 1.67 percent of a member's final average salary, multiplied by the member's number of years of service. Benefits may also be calculated under either a money match or an annuity-plus-pension computation if a greater benefit results. PERS also provides death and disability benefits. Benefits are established by state statutes.

An employee member will be eligible at minimum retirement age for a service retirement allowance if he or she has had a contribution in each of five calendar years or has reached at least 50 years of age before ceasing employment with a participating employer. Employee members may retire with unreduced benefits at age 58 or at any age with 30 or more years of service. A member with less than 30 years of service who is between the ages of 55 and 58 may retire with reduced benefits.

(7)-Continued

Covered employees are required by state statutes to contribute 6 percent of their salary to the plan. The employee contributions are currently paid by the Company for employees hired prior to January 1, 1995. SAIF Corporation is required by statute to contribute actuarially computed amounts as determined by PERS. (Currently, the contribution rate is 8.46 percent.) For the year ended December 31, 1995, the total amount paid by SAIF was \$5.8 million, which consisted of \$3.5 million for the employer contribution and \$2.3 million for the employee contribution. For the calendar year ending December 31, 1994, SAIF's contribution represents 2.30 percent of the total contribution required of all state agencies.

The "pension benefit obligation" is a standardized way to measure the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among PERS and employers. The System does not make separate measurements of assets and pension benefit obligations for individual employers.

The most recent actuarial valuation update of the pension benefit obligation for all state agencies was made as of December 31, 1994. The actuarial rate of return used was 8 percent. The total pension benefit obligation amount was \$4,279.5 million. The System's net assets available for state agency benefits on that date were \$4,066.8 million.

Historical trend information showing the System's progress in accumulating sufficient assets to pay benefits when due may be found in the June 30, 1995, Oregon Public Employees Retirement System annual financial report.

(8)

**DEFERRED COMPENSATION PLAN**

A deferred compensation plan (plan) was authorized under Internal Revenue Code Section 457 and ORS 243.400 to 243.495. The plan is a benefit available to all Company employees wherein they may execute an individual agreement with the Company for amounts earned by them to be paid at a future date. Participants in the plan are not required to pay federal and state income taxes on the deferred earnings until these earnings are received.

Participants cannot receive the funds until certain circumstances are met. Moneys accumulated by the Company under its plan have been invested with various financial institutions and insurance companies.

All amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are (until

## (8)-Continued

paid or made available to the employee or other beneficiary) solely the property and rights of the Company (without being restricted to provisions of benefits of the plan), subject only to the claims of the Company's general creditors. Participants' rights under the plan are equal to those of general creditors of the Company in an amount equal to the fair market value of the deferred account for each participant.

The Company has no liability for losses under the plan but does have the duty of due care that would be required of an ordinary prudent investor. The Company believes that it is unlikely that it will use the assets to satisfy the claims of general creditors in the future.

The investments are valued at market and totaled approximately \$13.8 million as of December 31, 1995.

## (9)

**STATUTORY NET INCOME AND  
POLICYHOLDER SURPLUS**

Generally accepted accounting principles differ in certain respects from the accounting practices prescribed or permitted by insurance regulatory authorities (statutory basis). Statutory net loss was approximately \$8.5 million for the year ended December 31, 1995 and statutory surplus was approximately \$429.9 million at December 31, 1995.

## (10)

**CONTINGENCIES**

On November 18, 1993, the Supreme Court of the State of Oregon handed down an opinion on Alsea Veneer, Inc. v. State of Oregon, which indicated that the expropriation of \$81.0 million from the Industrial Accident Fund in June, 1983 by the State of Oregon was inappropriate. The Supreme Court ruled that the State of Oregon must repay the \$81.0 million, with interest to the State Industrial Accident Fund. The Supreme Court's decision also directed the lower court to decide what the Company should do with the funds returned to the Industrial Accident Fund.

In 1993, the Company recorded a receivable from the State of Oregon for the \$81.0 million expropriation and restricted \$81.0 million of retained earnings. The Supreme Court decision created the potential for a loss contingency, however, it was not necessarily probable, nor could the amount be reasonably estimated at that time. Therefore, the Company did not accrue the \$81.0 million as a liability.

During 1994, the State of Oregon made a first installment of \$5.0 million and an additional payment of \$60.0 million in 1995 to the State Industrial Accident Fund. Settlement negotiations

## (10)-Continued

between the State of Oregon and the plaintiffs in this case progressed and it became probable that the Company would be ordered by the Court to distribute these funds. Therefore, the Company has eliminated the amount due from the State of Oregon, eliminated the amount set aside as reserved retained earnings, and recorded \$65.0 million as an asset and corresponding liability. In accordance with generally accepted accounting principles, this transaction is considered an extraordinary item and has been recorded as such on the Statement of Income.

The settlement agreement reached between the parties involved, which was approved by the Marion County District Court on February 26, 1996, calls for additional payments from the State of Oregon of \$160 million during the next two biennium. These funds are to be distributed to the plaintiffs and the State Industrial Accident Fund. However, the Oregon Constitution requires a legislative appropriation of funds before funds may be paid by the State. Therefore, the Company has not recorded any additional contingencies related to the Alsea Veneer, Inc. v. State of Oregon settlement.

The Company has committed no other reserves to cover any contingent liabilities. Various lawsuits against the Company have arisen in the course of the Company's business. Contingent liabilities arising from litigation were not considered material in relation to the financial position of the Company.

## (11)

**CHANGE IN ACCOUNTING FOR DEPOSIT WITH REINSURER**

The Company has changed the method of accounting for the deposit with reinsurer. The deposit is carried on the balance sheet at the cash value. Interest accrued on the deposit is recorded as Accrued Investment Income. Losses recoverable from the reinsurer are estimated to be \$7.5 million. Loss reserves are reduced by the estimated losses recoverable from the deposit with reinsurer.

## (12)

**SUBSEQUENT EVENTS**

Subsequent to December 31, 1995, the Board of Directors declared a policyholder dividend of approximately \$50 million. The dividend was declared at the April, 1996 meeting of the Board of Directors.



Table N.a.-1  
SUMMARY FINANCIAL OPERATION DATA FOR SELECTED INSURERS

	Employers Ins. of Wausau			National Union Fire Ins. of PA			Grocers Insurance		
	1993	1994	1995	1993	1994	1995	1993	1994	1995
Premiums Earned /1	\$1,344,824,004	\$1,354,532,236	\$1,415,727,786	\$2,151,548,113	\$2,284,862,272	\$2,387,279,812	\$18,583,922	\$18,592,908	\$20,434,057
Net Underwriting Gain /1	(83,191,718)	(64,896,723)	(181,964,572)	(99,704,322)	(132,861,365)	(19,104,955)	(525,398)	(27,057)	(1,021,281)
Net Investment Gain /1	177,711,130	163,332,132	307,990,818	462,744,601	267,069,711	438,937,362	2,671,394	2,698,340	3,113,685
Net Income /1	76,002,094	70,884,924	110,840,771	274,344,631	132,622,239	331,035,067	2,859,373	2,460,685	1,947,400
Federal & Foreign Income Taxes Incurred /1	(5,519,900)	681,205	(856,365)	78,991,987	(9,198,712)	67,544,799	(453,093)	173,714	166,362
Payroll Taxes /2	11,796,579	12,599,000	12,124,718	4,364,239	4,650,000	6,562,066	131,204	250,488	267,390
State & Local Insurance Taxes, Deducting Guaranty Association Credits /2	52,830,855	47,986,000	48,854,430	57,805,158	64,310,000	54,950,197	482,035	447,706	499,676
Gross Guaranty Association Assessments /2	(289,753)	1,899,000	(136,289)	0	0	0	0	0	0
Total Taxes, Licenses & Fees /2	56,901,301	54,388,000	52,452,031	80,489,956	71,968,000	72,512,013	652,571	557,679	570,407
Real Estate Taxes /2	1,981,103	2,024,000	2,014,852	217,083	636,000	423,465	14,702	13,053	10,631
Oregon Workers' Compensation Premiums Earned	12,343,751	12,696,686	10,488,248	17,151,671	15,352,712	16,629,471	5,506,480	5,006,092	6,168,830

	Liberty Northwest				SAIF			
	1992	1993	1994	1995	1992	1993	1994	1995
Premiums Earned /1	\$158,891,065	\$142,811,425	\$168,906,850	\$179,067,026	\$242,867,330	\$353,116,851	\$273,996,168	\$250,560,246
Net Underwriting Gain /1	1,953,156	3,786,697	(1,529,334)	(4,623,252)	158,339,254	(31,118,448)	(23,377,408)	(61,715,836)
Net Investment Gain /1	36,725,269	37,006,347	37,590,040	42,135,030	127,094,876	146,069,922	128,671,788	140,201,228
Net Income /1	24,756,641	28,485,101	25,867,494	26,840,070	261,792,729	83,357,309	73,578,081	(8,516,524)
Federal & Foreign Income Taxes Incurred /1	10,184,658	8,962,266	5,918,915	6,753,192	0	0	0	0
Payroll Taxes /2	1,519,154	1,291,386	1,602,105	1,890,224	3,215,643	3,520,555	3,952,749	4,189,480
State & Local Insurance Taxes, Deducting Guaranty Association Credits /2	342,582	741,649	989,854	1,004,229	2,373,139 /3	5,664,493 /3	1,195,629 /3	133,281
Gross Guaranty Association Assessments /2	16,635	96,871	25,514	(12,868)	0	0	0	0
Total Taxes, Licenses & Fees /2	871,962	1,285,075	1,251,757	1,575,512	2,411,469	5,682,876	1,386,578	155,698
Real Estate Taxes /2	0	0	0	0	238,940	300,397	293,866	375,868
Oregon Workers' Compensation Premiums Earned	151,751,714	130,635,441	138,308,318	142,566,361	259,977,660	255,480,563	267,772,916	244,504,398

Notes:

1. Data from page 4 of Annual Statements-- Underwriting and Investment Exhibit Statement of Income
2. Data from page 11 of Annual Statements -- Underwriting and Investment Exhibit Part 4 - Expenses
3. SAIF does not pay state or local income taxes. However, SAIF reports assessments paid to the Federal Government on premium received for coverage provided to Longshore and Harbor Workers' and Jones Act Insureds.
4. Data is reported on a consolidated basis, and does not necessarily reflect only Oregon Business.





**Table N.a.-2 .  
LIBERTY NORTHWEST PREMIUM AND PREMIUM TAX INFORMATION 1992-1995**

	Workers' Compensation				Other Lines			
	1992	1993	1994	1995	1992	1993	1994	1995
Total Oregon Gross Direct Premium Written	\$152,055,601.00	\$130,559,488.00	\$138,576,933.00	\$142,559,959.00	\$76,451.00	\$52,039.00	\$0.00	\$0.00
Premium Tax on Federal Workers' Compensation Premium	17,355.92	31,207.86	165,101.81	86,494.14	0.00	0.00	0.00	0.00
Premium Tax on Stateside Workers' Compensation Premium	3,403,895.11	2,906,380.57	2,952,879.19	3,121,104.94	0.00	0.00	0.00	0.00
Premium Tax on Non-Workers' Compensation Premium	0.00	0.00	0.00	0.00	1,720.14	1,170.88	0.00	0.00
Total Gross Taxes Prior to Fire Marshal Tax	3,421,251.03	2,937,588.43	3,117,981.00	3,207,599.08	1,720.14	1,170.88	0.00	0.00
Less Offset for WCD Assessments Paid on Workers' Comp Premium	(6,748,042.89)	(6,141,532.10)	(5,788,205.60)	(6,221,935.71)	0.00	0.00	0.00	0.00
Less Offset for Oregon Insurance Guarantee Association Assessments	(97,596.45)	(100,804.82)	(66,271.53)	(54,055.93)	(1,720.14)	(1,170.88)	0.00	0.00
Net Tax Prior to Fire Marshal Tax	0.00	0.00	98,830.28	32,438.21	0.00	0.00	0.00	0.00
State Fire Marshal Tax Not Available to be Offset	39.18	0.13	0.00	0.00	0.00	0.00	0.00	0.00
Federal Taxes on Income	10,241,347.00	8,608,654.00	5,955,447.00	6,873,312.00	0.00	0.00	0.00	0.00
Total Net Tax	10,241,386.18	8,608,654.13	6,054,277.28	6,905,750.21	0.00	0.00	0.00	0.00

Note: WCD Assessment may be used only to offset tax on stateside workers' compensation premium. Guarantee Association Assessments may offset tax on federal workers' compensation and non workers' compensation premiums.

Data Source: Liberty Northwest Insurance, June 1996.

Source: Department of Consumer and Business Services, Information Management Division

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Table N.b.-1  
SAIF TAX WORKSHEET FOR 1992 THROUGH 1995

	1995	1994	1993	1992
<b>Summary of Total Investment Gain</b>				
A Unpaid Losses (p3,I1,c1&2 / 2)	1,301,309,965	1,267,409,746	1,192,572,157	1,108,955,712
B Ratio of Unpaid Loss Adjustment Expenses to Losses (Grand Average) (p3,I2,c1&2 / p3,I1,c1&2)	0.1387	0.1138	0.1047	0.0919
C Loss Adjustment Expense Reserve (A x B)	180,491,692	144,231,229	124,862,305	101,913,030
D Average Unearned Premium Reserve (p3,I9,c1&2) / 2	31,103,052	31,264,392	32,331,648	31,688,617
E Agent Balances Factor ((p2,I9.1&9.2,c1&2) / 2) / p4,I1)	0.7122	0.6293	0.3187	0.2427
F Agents' Balances (p4, I1 x E)	178,449,007	172,425,789	112,538,340	58,895,361
G Premiums Earned (p4, I1)	250,560,246	273,996,168	353,116,851	242,667,330
H Surplus Ratio: (((SAF)(p4,I32,c1&2) / 2) / ((p3,I1&2&5,c1&2) / 2) + p4,I1))	0.2162	0.2210	0.1721	0.1346
I Investment Gain Ratio: [p4,I9a / (SAF(p33,I25,c1&2)+p3,I1&2&9,c1&2 -p2,I9.1&9.2,c1&2) / 2]	0.0818	0.0780	0.0955	0.0919
J Estimated Investment Gain I x (H(A+C+D+G) + A+C+D-F)	140,345,636	128,693,356	146,143,070	127,150,381
K Other Income Ratio (p4,I13 / p4,I1)	(0.0272)	(0.0075)	0.0031	(0.0044)
L Estimated Other Income (K x G)	(6,815,239)	(2,054,971)	1,094,662	(1,067,736)
M Est Investment Gain & Other Inc (J + L)	133,530,398	126,638,384	147,237,732	126,082,644
<b>Summary of Underwriting Experience</b>				
N Premium Earned (p4, I1)	250,560,246	273,996,168	353,116,851	242,667,330
O Losses Incurred (p4, I2)	198,763,243	185,171,672	279,425,462	(1,368,957)
P Loss Expenses Incurred (p4, I3)	58,667,036	53,514,529	46,398,230	41,549,461
Q Other Underwriting Exp (p4, I4)	54,845,803	58,687,375	57,570,808	44,151,691
R Dividends to Policyholders (p4, I14a)	80,188,951	29,666,666	32,672,940	22,583,870
S Underwriting Profit (1-2-3-4-7)	(141,904,787)	(53,044,074)	(62,950,589)	135,751,265
<b>Estimated State Corporate Excise Tax</b>				
T Taxable Income (Underwr Profit + Total Invest Gain + (1-RDF) x Change in Tot Losses)	673,244	80,140,777	112,529,604	272,326,609
U Gross Excise Tax (Taxable Inc x ETR)	44,434	5,289,291	7,426,954	17,973,556
Ua Adj Excise Tax (Gr Tax x (1-SRRF))	22,173	5,289,291	7,426,954	17,973,556
Ub Available OIGA Offsets	69,532	126,493	162,908	242,423
Uc Adj Excise Tax after Offsets (Ua - Ub)	-	5,162,798	7,264,046	17,731,133
<b>Estimated Federal Income Tax</b>				
V Adjusted Underwriting Profit (S + Loss Reserve Discount Adjustment)	(132,857,153)	(46,497,607)	(34,708,128)	146,243,964
W Total Investment Gain (T - V)	133,530,398	126,638,384	147,237,732	126,082,644
X Adjusted Underwriting Profit net of excise tax relating to underwriting (S - (S x Adj ETR))	(128,481,636)	(43,428,765)	(32,417,392)	136,591,862
Y Adjusted Total Investment Gain net of corp excise tax relating to investments (M - (M x Adj ETR))	129,132,707	118,280,251	137,520,042	117,761,190
Z Other Components:				
ZA Net Realized Capital Gain + Net Investment Inc Earned (p4,I9 + p4,I8)	140,201,228	128,671,788	146,069,922	127,094,676
ZB Bonds Exempt from US Tax (none)	-	-	-	-
ZC Unaffiliated Stocks (p6, Part 1, col 8, lines 2.1 & 2.2)	7,072,849	6,237,482	3,450,364	1,889,990
ZZ (((Fed Tax Rate x (ZA - (ZB x Factor B) - (ZC x Factor C))) / ZA)	0.3392	0.3395	0.3349	0.3368
AA Federal Income Tax (FTR x X)+(ZZ x Y)	(1,166,758)	24,956,077	35,033,549	86,103,202

Source: Information Management Division, Department of Consumer & Business Services

**Table N.b.-2**  
**Data Used in SAIF Tax Worksheet for 1992 through 1995**

<b>From Annual Statements</b>	<b>1995</b>	<b>1994</b>	<b>1993</b>	<b>1992</b>
Page 2:				
Line 9.1	8,197,659	8,324,811	8,278,457	2,279,030
Line 9.2	171,156,106	169,194,964	159,031,153	55,485,604
Page 3:				
Line 1	1,320,978,734	1,281,641,195	1,253,178,296	1,131,966,017
Line 2	205,663,555	155,253,777	133,163,815	116,553,391
Line 5	21,961,842	23,504,225	33,760,766	30,704,570
Line 9	33,443,180	28,762,923	33,765,861	30,897,435
Line 25	429,927,688	474,756,300	428,470,548	268,386,704
Page 4:				
Line 1	250,560,246	273,996,168	353,116,851	242,667,330
Line 2	198,763,243	185,171,672	280,266,261	(1,373,076)
Line 3	58,667,036	53,514,529	46,398,230	41,549,461
Line 4	54,845,803	58,687,375	57,570,808	44,151,691
Line 8	119,877,379	115,250,569	112,647,166	111,279,252
Line 9	20,323,849	13,421,219	33,422,756	15,815,424
Line 9a	140,201,228	128,671,788	146,069,922	127,094,676
Line 13	(6,812,965)	(2,049,633)	1,078,775	(1,057,331)
Line 14a	80,188,951	29,666,666	32,672,940	22,583,870
Line 32	429,927,688	474,756,300	428,470,548	268,386,704
Page 6				
Line 2.1	2,952,962	1,243,642	-	-
Line 2.2	4,119,887	4,993,840	3,450,364	1,889,990
<b>From Other Sources</b>	<b>1995</b>	<b>1994</b>	<b>1993</b>	<b>1992</b>
Surplus Adjustment Factor (SAF)	0.839	0.839	0.841	0.820
Recovery & Subrogation Factor (RSF)	1.000	1.000	0.997	0.997
Reserve Discount Factor (RDF)	0.770	0.770	0.767	0.772
OR Corporate Excise Tax Rate (ETR)	0.066	0.066	0.066	0.066
State Revenue Refund Factor (SRRF)	0.501	0.000	0.000	0.000
Adjusted ETR (Rate x (1- SRRF))	0.033	0.066	0.066	0.066
Federal Tax Rate (FTR)	0.35	0.35	0.34	0.34
Factor for "B" in Federal Tax Formula	0.90	0.91	0.92	0.93
Factor for "C" in Federal Tax Formula	0.61	0.62	0.63	0.64

Note: SAF, RSF, RDF, Federal Tax Rate, and factors for B & C are from NAIC's *Report on Profitability By Line By State in 19yy*. 1995

SAF and RDF were not available, so 1994 factors were used for 1995 as well. Factors for B and C were not available for 1995, so we assumed continuation of trends. ETR and SRRF are from Form 20, Oregon Corporation Excise Tax Return.

Table N.c.-1  
 Estimated Tax Effects on SAIF Financial Condition

	1992	1993	1994	1995
Surplus -- Beginning of Year	218,397,903	164,552,369	282,338,618	298,505,495
Reported Change in Surplus	49,988,801	160,083,844	46,285,752	(44,828,611)
Corporate Excise Tax	17,731,133	7,264,046	5,162,798	0
Federal Income Tax	86,103,202	35,033,549	24,956,077	(1,166,758)
Adjusted Surplus -- Year End	164,552,369	282,338,618	298,505,495	254,843,642
Net Premium Written	241,084,967	355,985,277	268,993,230	255,240,504
Risk-based Authorized Control Level			51,548,186	54,809,262
RATIOS:				
Net Premium Written to Adjusted Surplus	1.465	1.261	0.901	1.002
Adjusted Surplus to Control Level			5.791	4.650

Source: Department of Consumer and Business Services, July, 1996.

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Table N.c.-2  
Apparent Tax Rate and Yield on Invested Assets

	Employers Insurance of Wausau				National Union Fire Ins Co of Pittsburgh			
	1992	1993	1994	1995	1992	1993	1994	1995
1 Net Underwriting Gain/Loss	-163,564,375	-83,191,718	-64,896,723	-181,964,572	-77,788,414	-99,704,322	-132,861,365	-19,104,955
2 Net Investment Gain/Loss	215,649,669	177,711,130	163,332,132	307,990,818	336,785,971	462,744,601	267,069,711	438,937,362
3 Total Other Income	-7,866,580	-15,324,267	-8,807,959	-7,723,021	-9,244,040	-8,761,243	-8,913,284	-14,949,615
4 Dividends to Policyholders	6,581,624	8,712,951	18,061,321	8,318,819	2,244,510	942,438	1,871,535	6,302,926
5 Fed/Foreign Income Tax Incrd	-3,555,133	-5,519,900	681,205	-856,365	71,231,838	78,991,967	-9,198,712	67,544,799
6 Net Income	41,192,223	76,002,094	70,884,924	110,840,771	176,277,169	274,344,631	132,622,239	331,035,067
7 Losses Unpaid @ Prior YrEnd	1,524,885,484	1,671,699,120	1,468,023,585	1,475,231,794	3,828,700,669	4,091,027,522	4,284,819,077	4,616,031,420
8 Losses Unpaid @ Year End	1,671,699,120	1,468,023,585	1,475,231,794	1,555,730,579	4,091,027,522	4,284,819,077	4,616,031,420	4,663,249,411
9 Avg Reserve Discount Factor	0.807	0.813	0.819	0.820	0.775	0.776	0.786	0.784
10 Apparent Tax Rate on Investment Income (5)-TxRate(1+3-4+(1.0-9)(8-7)) (2)	21.95%	24.68%	19.80%	20.58%	24.21%	21.93%	6.09%	17.79%
11 Surplus from Prior Year-End	428,800,158	420,567,543	456,902,267	590,215,413	1,420,948,632	1,401,263,930	1,401,450,399	3,492,858,212
12 Unrealized Capital Gains	8,818,906	24,260,332	66,809,244	-109,525,475	44,576,552	63,644,067	117,414,048	388,931,188
13 Other Changes to Surplus	-17,051,521	12,074,392	66,503,902	68,816,927	-64,261,254	-63,457,598	1,973,993,765	167,653,911
14 Total Changes to Surplus	-8,232,615	36,334,724	133,313,146	-40,708,548	-19,684,702	186,469	2,091,407,813	556,585,099
15 Surplus at Year-End	420,567,543	456,902,267	590,215,413	549,506,865	1,401,263,930	1,401,450,399	3,492,858,212	4,049,443,311
Cash and Invested Assets								
16 From Prior Year-End	2,429,529,983	2,637,121,133	2,616,615,653	2,698,484,490	4,649,076,310	5,052,646,341	5,366,844,549	7,337,534,787
17 From Year-End	2,637,121,133	2,616,615,653	2,698,484,490	2,781,676,932	5,052,646,341	5,366,844,549	7,337,534,787	8,267,935,281
18 Apparent Yield on Invested Assets $\frac{2.0 \times (2) + (12)}{(16) + (17) - (2) - (12)}$	9.27%	8.00%	9.05%	7.52%	8.18%	10.64%	6.24%	11.20%

	Grocers Insurance				Liberty Northwest Insurance Corp.			
	1992	1993	1994	1995	1992	1993	1994	1995
1 Net Underwriting Gain/Loss	-187,645	-525,398	-27,057	-1,021,281	1,953,158	3,786,897	-1,529,334	-4,623,252
2 Net Investment Gain/Loss	2,287,786	2,671,394	2,698,340	-3,113,685	36,725,269	37,006,347	37,590,040	42,135,030
3 Total Other Income	320,846	329,436	150,537	154,922	-2,301,745	-1,480,097	-1,245,341	-522,100
4 Dividends to Policyholders	0	69,152	187,421	133,564	1,435,383	1,865,780	3,028,956	3,396,416
5 Fed/Foreign Income Tax Incrd	746,812	-453,093	173,714	166,362	10,184,658	8,962,266	5,918,915	6,753,192
6 Net Income	1,674,175	2,859,373	2,460,685	1,947,400	24,756,641	28,485,101	25,867,494	26,840,070
7 Losses Unpaid @ Prior YrEnd	19,141,286	21,191,291	22,812,496	23,612,429	340,807,728	355,556,614	358,534,089	374,702,957
8 Losses Unpaid @ Year End	21,191,291	22,812,496	23,612,429	24,539,398	355,556,614	358,534,089	374,702,957	391,399,103
9 Avg Reserve Discount Factor	0.808	0.802	0.804	0.802	0.772	0.767	0.770	0.770
10 Apparent Tax Rate on Investment Income (5)-TxRate(1+3-4+(1.0-9)(8-7)) (2)	24.82%	-17.67%	5.24%	14.52%	26.27%	23.18%	17.69%	19.94%
11 Surplus from Prior Year-End	6,507,069	9,167,486	11,848,105	13,971,375	84,811,119	110,066,521	141,056,483	159,422,293
12 Unrealized Capital Gains	-158,391	-230,477	-282,265	-166,448	-1,821	13,601	29,129	1,340,957
13 Other Changes to Surplus	2,818,808	2,911,096	2,405,535	1,873,799	25,257,223	30,976,361	18,336,681	16,852,330
14 Total Changes to Surplus	2,660,417	2,680,619	2,123,270	1,707,351	25,255,402	30,989,962	18,365,810	18,193,287
15 Surplus at Year-End	9,167,486	11,848,105	13,971,375	15,678,726	110,066,521	141,056,483	159,422,293	177,615,580
Cash and Invested Assets								
16 From Prior Year-End	31,966,904	35,780,989	40,913,381	42,357,556	442,816,836	487,098,248	523,107,697	566,368,377
17 From Year-End	35,780,989	40,913,381	42,357,556	47,119,584	487,098,248	523,107,697	566,368,377	609,160,362
18 Apparent Yield on Invested Assets $\frac{2.0 \times (2) + (12)}{(16) + (17) - (2) - (12)}$	6.49%	6.57%	5.98%	6.81%	8.22%	7.61%	7.15%	7.68%

SELECTED AVERAGES	1992	1993	1994	1995
Tax Rate on Investment Income	24.31%	23.26%	18.75%	18.21%
Yield on Invested Assets	8.04%	8.21%	7.11%	8.30%

## Notes:

- 1 Company data from pages 2 and 4 of annual statements for 1992 through 1995
- 2 Nominal tax rate in (7) is 34% for 1992 and 1993 and 35% for 1994 and 1995.
- 3 Excluded from the selected averages for tax rates: Grocers (1993,1994), Nat'l Union Fire (1994).

**Estimated Tax Effects on SAIF Financial Condition**  
**Assuming Investment Yields and Tax Rates Comparable to Private Insurers**

Actual Data	1992	1993	1994	1995
1 Surplus @ Prior Year-End	218,397,903	268,386,704	428,470,548	474,756,300
2 Net Income	261,792,729	83,357,309	73,578,081	(8,516,524)
3 Unrealized Capital Gains	9,449,680	3,927,796	(12,953,224)	20,036,627
4 Other Changes to Surplus	(221,253,608)	72,798,739	(14,339,105)	(56,348,714)
5 Total Changes to Surplus	49,988,801	160,083,844	46,285,752	(44,828,611)
6 Surplus @ Year-End	268,386,704	428,470,548	474,756,300	429,927,688
7 Cash/Inv Assets @ Prior YrEnd	1,357,512,358	1,480,969,264	1,597,907,411	1,683,112,177
8 Cash/Inv Assets @ Year End	1,480,969,264	1,597,907,411	1,683,112,177	1,746,972,713
9 Net Investment Income [excl.(3)]	127,094,676	146,069,922	128,671,788	140,201,228
10 Change in InvAssts O/T InvIncom	(13,087,450)	(33,059,571)	(30,513,798)	(96,377,319)
11 Losses Unpaid @ Prior YrEnd	1,085,945,406	1,131,966,017	1,253,178,296	1,281,641,195
12 Losses Unpaid @ Year End	1,131,966,017	1,253,178,296	1,281,641,195	1,320,978,734
13 Reserve Discount Factor	0.772	0.767	0.770	0.770
<b>Model Data</b>	<b>1992</b>	<b>1993</b>	<b>1994</b>	<b>1995</b>
14 Surplus @ Prior Year-End	218,397,903	159,177,876	262,972,400	290,116,236
15 Cash/Inv Assets @ Prior YrEnd	1,357,512,358	1,371,760,436	1,432,409,263	1,498,472,113
16 Selected Yield on Inv Assets	8.04%	8.21%	7.11%	8.30%
17 Estimated Investment Gain = (16)((15)+.5(10))	108,644,927	111,197,179	100,698,428	120,419,065
18 Underwriting Income/Loss	158,339,254	(31,118,448)	(23,377,408)	(61,715,836)
19 Other Income/Loss	(1,057,331)	1,078,775	(2,049,633)	(6,812,965)
20 Policyholder Dividends	22,583,870	32,672,940	29,666,666	80,188,951
21 Selected Tax Rate on Inv Income	24.31%	23.26%	18.75%	18.21%
22 Nominal Tax Rate	34.00%	34.00%	35.00%	35.00%
23 Adjusted Oregon Excise Tax Rate	3.3%	6.6%	6.6%	6.6%
24 Oregon Excise Tax = ((17)+(18)+(19)-(20)+[1-(13)]((12)-(11)))(23)	8,376,577	5,063,984	3,441,978	(1,270,569)
25 Income Taxes = (21)(17)+(22)((18)+(19)-(20)-(24)-(25))+[1-(13)]((12)-(11))	72,932,821	12,424,797	679,801	(26,514,664)
26 Net Income (incl all cap gains) = (17)+(18)+(19)-(20)-(24)-(25)	162,033,581	30,995,784	41,482,941	(513,454)
27 Other Changes to Surplus: (4)	(221,253,608)	72,798,739	(14,339,105)	(56,348,714)
28 Surplus @ Year End	159,177,876	262,972,400	290,116,236	233,254,068
29 Cash/Inv Assets @ Year End = (28)-(6)+(8)	1,371,760,436	1,432,409,263	1,498,472,113	1,550,299,093
Net Premium Written	241,084,697	355,985,277	268,993,230	255,240,504
Risk-based Authorized Control Level			51,548,186	54,809,262
<b>RATIOS:</b>				
Net Premium Written to Model Surplus	1.515	1.354	0.927	1.094
Model Surplus to Auth Control Level			5.628	4.256

## Notes:

1 Actual data from SAIF annual statements for December 31, 1992 through 1995

2 Model Data: Initial assets and surplus are actual data for December 31, 1991.

Adjusted excise tax rates (18) are from Table N.b.-2.

Selected yield rates and tax rates on invested assets are from Table N.c.-2.

Underwriting gain, other income, and policyholder dividends are actual.

3 The model assumes SAIF efficiently shifted cash & invested assets to a portfolio parallel to private insurers on January 1, 1992, and subsequently also realized returns and effective tax rates similar to private insurers. Taxes include accrual of tax on unrealized capital gains at the same effective rate as apparent from realized capital gains and investment income. The model may slightly understate invested assets by the net amount of this tax payment deferral.

**Table O.a.-1  
SUMMARY OF OREGON INSURANCE GUARANTY ASSOCIATION ACTIVITIES 1982-95**

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Insolvency Claims 1/ Workers' Compensation Liability 2/ Subrogation Total	37 30 - 67	NA NA NA NA	37 19,038 1 19,076	NA NA NA NA	72 775 - 847	236 623 - 859	115 314 - 429	134 204 - 338	146 154 - 300	252 211 - 463	143 311 - 454	105 199 - 304	118 182 - 280	102 83 - 185
Number of Insolvencies Administered 3/ New Insolvencies 4/	10 -	10 -	10 3	13 6	19 7	26 5	31 2	33 4	37 -	37 5	42 1	43 1	44 5	49 -
Assessments 5/ Total Revenues 6/ Net Claims Paid 7/ Administrative Expenses 8/ Ending Fund Balance	\$ 851,247 \$ 1,132,982 \$ 553,984 \$ 47,944 \$ 570,843	NA NA NA NA \$ 526,675	\$ 9,990,700 \$ 10,160,533 \$ 1,132,772 \$ 67,999 \$ 9,486,437	\$ 809,984 \$ 2,270,782 \$ 6,241,557 \$ 813,065 \$ 4,702,597	\$ 4,146,770 \$ 5,050,258 \$ 5,602,011 \$ 256,373 \$ 3,923,147	\$ 3,487,499 \$ 6,315,204 \$ 5,907,641 \$ 290,108 \$ 4,125,082	\$ 2,809,261 \$ 4,357,343 \$ 5,547,189 \$ 208,251 \$ 2,746,755	\$ 2,393,339 \$ 4,176,362 \$ 3,249,128 \$ 181,459 \$ 3,492,530	\$ - \$ 1,355,343 \$ 2,525,517 \$ 151,736 \$ 2,170,620	\$ 1,998,621 \$ 3,516,268 \$ 2,233,806 \$ 170,097 \$ 3,282,985	\$ - \$ 1,530,634 \$ 1,195,171 \$ 163,227 \$ 3,455,221	\$ 1,497,899 \$ 2,505,859 \$ 3,550,042 \$ 175,801 \$ 2,235,237	\$ - \$ 621,077 \$(3,746,724) \$ 204,144 \$ 6,398,894	\$ - \$ 967,200 \$(490,313) \$ 173,912 \$ 4,373,955

Notes:

1. Files pending as of December 31, 19xx, by type of claim.
2. Liability claims also include unearned premium claims for 1982, 1984, and 1986.
3. Number of insolvent firms to date, not including any firms becoming insolvent during current year.
4. Number of firms becoming insolvent during current year.
5. Assessments collected by the Oregon Insurance Guaranty Association during the year.
6. Includes assessments, security deposits, interest income, and miscellaneous income.
7. Includes claims paid, claims expenses, unearned premiums paid, recoveries from receivers, and salvage and subrogation received.
8. Includes salaries, rent, legal services, office expenses, taxes, SEP contributions, depreciation, and other expenses.

Data Source: Oregon Insurance Guaranty Association Annual Reports 1982 - 1995.

Source: Department of Consumer and Business Services, Information Management Division, May 1996.

**Table O.b.-1  
SAIF'S SIMULATED SHARE OF OIGA ASSESSMENTS AND OFFSETS FOR 1992-95**

**SAIF's Share of Assessment Base Premiums Written**

Year	Non-A&H P&C	Ocean Marine	Surety	Credit	Mortgage, etc	Total Assess-able Premiums	SAIF's Premiums	SAIF's Share
1986	2,093,971,000	15,601,000	19,411,000	6,181,000	-	2,052,778,000	233,406,000	11.4%
1987	2,261,588,000	15,930,000	22,218,000	4,973,000	10,252,000	2,208,215,000	256,254,000	11.6%
1988	2,346,683,000	12,846,000	24,870,000	5,593,000	12,928,000	2,290,446,000	272,155,000	11.9%
1990	2,677,585,000	14,728,000	33,759,000	5,136,000	22,715,000	2,601,247,000	265,411,000	10.2%
1992	2,763,115,000	17,493,000	31,352,000	4,230,000	22,265,000	2,687,775,000	257,370,000	9.6%

**SAIF's Share of Assessments and Offsets, and Percent of Available Offsets that are Usable**

Assessment Year	Assessment	SAIF's Share	1992 Offsets	1993 Offsets	1994 Offsets	1995 Offsets	Total, 1992-95
1987 (used 1986 prem)	3,487,499	397,575	79,515				79,515
1988 (used 1987 prem)	2,809,261	325,874	65,175	65,175			130,350
1989 (used 1988 prem)	2,393,339	284,807	56,961	56,961	56,961		170,883
1991 (used 1990 prem)	1,998,621	203,859	40,772	40,772	40,772	40,772	163,088
1993 (used 1992 prem)	1,497,899	143,798			28,760	28,760	57,520
Offsets Available			242,423	162,908	126,493	69,532	601,356
Offsets Used			242,423	162,908	126,493	22,173	553,997
Percent of Offsets Used			100.0%	100.0%	100.0%	31.9%	92.1%

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## Exhibit "P"

**I. REGULATORY DIFFERENCES BETWEEN SAIF and OTHER INSURERS****A. Under the Insurance Code:**

1. ORS Chapter 732 addresses the organization and corporate procedures of domestic insurers, but does not apply to SAIF.
2. ORS Chapter 734 provides for the rehabilitation and liquidation of domestic insurers. This Chapter also establishes the Oregon Insurance Guaranty Association requiring participation by all property and casualty insurers in covering losses to claimants of insolvent property or casualty insurers. SAIF is not subject to these provisions.
3. ORS 733.510 to 733.780 imposes limitations and other safeguards upon insurers' investments. SAIF's investments, which are handled by the State Treasurer, are not subject to these provisions.
4. ORS 731.554 prescribes capital and surplus requirements of not less than \$3 million for workers' compensation insurers. SAIF is not subject to this provision.
5. ORS 731.028(5) allows a copy of the Secretary of State's audit to be submitted to the director in lieu of an annual audit conducted by an independent certified public accountant.
6. ORS 733.060 governs claim reserving and precludes the discounting of workers' compensation death and permanent disability reserves. While SAIF is subject to this provision pursuant to ORS 731.028 and sets reserves in the Industrial Accident Fund under ORS 656.636, the Attorney General has opined that SAIF may nevertheless discount these reserves (AG OP-6176).

**B. Under the Workers' Compensation Law:**

1. ORS 656.752(8) requires SAIF to be the State's insurer.
2. ORS 656.751 requires SAIF but no other insurer to have a five member public board of directors appointed by the Governor and confirmed by the Senate.
3. ORS 656.702 requires the records of SAIF (with the exception of employer account records and claimant files) to be accessible to the public. No other insurer is subject to this requirement.
4. ORS 656.758 statutorily binds SAIF insured employers to make full disclosure to SAIF Corporation regarding all information relevant to all risks insured by the

fund. These obligations of SAIF's insureds are enforceable by resort to civil and criminal penalties.

C. Under Other Law:

1. ORS 192.610 to 192.690, under the opinion of the Oregon Attorney General (No. 2862 of 5/25/88), subjects SAIF's Board of Director's meetings to the Public Meetings Law.
2. ORS 317.080 exempts SAIF from state income taxation.
3. 26 U.S.C. 115 of the Internal Revenue Code exempts SAIF from federal income taxation.
4. Frohnmayer v. SAIF, 294 OR 570, 660 P2d 1061 (1983) held that SAIF's legal counsel must be the Oregon Attorney General.
5. ORS 30.260 et. seq., the Oregon Tort Claims Act, confers upon the State Accident Insurance Fund Corporation and its officers, employees and agents qualified immunity and limitations on liability.
6. Chapter 237 et. seq. requires the employees of the State Accident Insurance Fund Corporation to participate in the Public Employees Retirement System.

**REGULATORY PROVISIONS THAT REQUIRE CLARIFICATION WITH RESPECT TO SAIF**

The following provisions have been the subject of some discussion or disagreement between SAIF and DCBS. Interpretations of the Code provisions may or may not vary. In any case, greater clarity would result if these provisions were explicitly related to SAIF.

A. Under the Insurance Code:

1. ORS 731.216 empowers the director to establish a rating bureau for prescribing loss cost rates which may require insurers to use pursuant to ORS 737.320(7).
2. ORS 731.240 provides due process of contested case hearings for rate filing disapproval's under ORS 737.320.
3. ORS 737.045 provides the director with cease and desist remedies for immediately addressing pending or in force filings that contravene rate making provisions of the Insurance Code.

4. ORS 737.230 grants the director access to certain rating data regarding rate relativity of an insurer's classification rates. Such data is necessary for applying the statutory rate making standards for fair discrimination.
5. ORS 737.346 prohibits fictitious groupings for rating purposes. This statute is one of the enforcement provisions utilized in the Insurance Division's Administrative rules regulating unfair trade practices regarding policyholder dividends (OAR 836-80-105 et. seq.).
6. ORS 746.035 prohibits inducements not specified in the insurance policy.
7. ORS 746.045 prohibits rebates as an inducement for insurance.
8. ORS 746.160 prohibits practices injurious to free competition.
9. ORS 746.600 to 746.691 is the Code's Privacy Act that: (a) establishes standards for the collection, use and disclosure of insurance transaction information, (b) balances insurer's business needs and the public's need for fairness in insurance information practices, (c) establishes a regulatory mechanism to enable a natural person to ascertain what information is being collected, (d) limits disclosure of insurance information, and (e) enables insurance applicants and policyholders to obtain reasons for any adverse underwriting decision.
10. ORS 744.505 to 744.575, 744.605 to 744.700 to 744.740 and 744.800 to 744.820 regulate adjusters, insurance consultants and third party administrators.
11. ORS 731.028(2) states that "The filing requirements of...(the Insurance Code rating laws)...are in lieu of any similar filing requirements prescribed by any other law of this state." There is a difference of opinion as to whether the Code's rating laws control if inconsistent with the W.C. Law provisions regarding SAIF's rate making capabilities. SAIF has viewed the Code's provisions as merely procedural and non-binding in substance while the Insurance Division sees the subsection as substantive with the Code controlling.
12. ORS 731.028 provides that certain provisions of the Insurance Code are applicable to SAIF. Inexplicably, this statute leaves out a number of harmonizing and operational provisions of the Insurance Code that logically should—even must—apply to SAIF. The statute should be changed to make SAIF explicitly subject to these provisions. These include:
  - a. ORS 731.004 to 731.016 which provides the Short Title, Purpose and Construction of the Code.
  - b. ORS 731.022, 731.026, and 731.028 that deal with jurisdiction regarding application of the Code.

- c. ORS 731.052 to 731.146 that provide general definition under the Code.
- d. ORS 731.158 and 731.186 that define Classes of Insurance.
- e. ORS 731.232 and 731.236 that empower the director with subpoena and general powers.
- f. ORS 731.244 which empowers the director with rule making authority.
- g. ORS 731.264 which makes complaints and investigations confidential.
- h. ORS 731.475 that requires records retention by workers' compensation insurers.
- i. ORS 731.480 that requires safety services by workers' compensation insurers.
- j. ORS 737.007 to 737.035 that deal with definitions, purpose and application of the Code's chapter on rates and rating organizations.
- k. ORS 737.342 that provides hearing procedures on rate grievances.
- l. ORS 737.360 which affords insurers rights to participate in a rating organization.
- m. ORS 737.365 which authorizes insurers and rating organizations to engage in certain cooperative activities otherwise prohibited by anti-trust laws.
- n. ORS 737.526 that allows for the interchange of data between the director, insurers and rating organizations in the furtherance of uniform administration of rate regulatory laws.

**B. Under the Workers Compensation Law:**

- 1. ORS 656.508 authorizes SAIF to fix premium classification rates annually or at other times it deems necessary.
- 2. ORS 656.504 authorizes SAIF to prescribe minimum premiums. Such currently are \$500 whereas other insurers are limited to \$400 allowed in the Oregon Workers' Compensation Insurance Plan (assigned risk). This statute also authorizes SAIF to utilize cents per hour in lieu of established \$100 units of payroll. Such exposure base is currently inconsistent with that approval under ORS Chapter 737.

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APPENDIX S.a.

SAIF CORPORATION  
EXTERNAL LOBBY EXPENSE  
1986-1995

Year	Name	Address	Amount Paid	Matter, Measure Proceeding
1995	Public Affairs Council	867 Liberty St. NE Salem, OR	52,800	Workers' Comp issues before the Oregon State Legislature
1994	Public Affairs Council	867 Liberty St. NE Salem, OR	6,600	Workers' Comp issues before the Oregon State Legislature
1993	Public Affairs Council	867 Liberty St. NE Salem, OR	60,000	Workers' Comp issues before the Oregon State Legislature
1992			0.00	
1991	C. J. T. Davie	Salem, OR	11,648	Legislative representation January through June, 1991
1990	Senator Ron Grensky	Medford, OR	158	All matters affecting Workers' Comp insurance and/or SAIF Corp. during the 1990 session of the OR legislature and subcommittees.
1989	Stanton F. Long Katherine Keene Stephanie Kelly	Salem, OR Salem, OR Salem, OR	282 9,474 2,959 <u>12,715</u>	All matters affecting Workers' Comp insurance and/or SAIF Corp. during the 1989 session of the OR legislature and subcommittees.
1988			0.00	
1987	Susan Brown Thomas Evans Ken Johnson Richard Lang John Gilkey Pat Lord Susan Deschler	Salem, OR Salem, OR Salem, OR Salem, OR Salem, OR Salem, OR Salem, OR	24,020 16,250 9,831 6,000 4,860 1,663 1,787 <u>64,411</u>	All matters affecting Workers' Comp insurance and/or SAIF Corp. during the 1987 session of the OR legislature and subcommittees.
1986	Stephen Beckham	Salem, OR	28,596	All matters affecting Workers' Comp insurance and/or SAIF Corp. during the 1986 session of the OR legislature and subcommittees.
Total			<u>236,928</u>	

The following information was extracted from Schedule M-1 of the 1986 through 1995 Annual Statements filed by SAIF Corp.

Source: Table provided by Richard E. Sherman & Associates Inc.

APPENDIX S.b.

PROPERTIES OWNED BY SAIF CORPORATION  
FOR THE PERIOD FROM 1/1/80 TO 12/31/95

This worksheet summarizes real estate holdings from its acquisition to the later of its disposition or 12/31/95. Included is all property owned as of 12/31/95 as well as all other property with buy or sell transactions since 1/1/80.

Source: Annual Statements filed by Saif with the Oregon Insurance Division.

Property	Date Acquired	Date Sold	Actual Cost	Book Value	Market Value	Sale Price	Gain (loss) on sale
<b>Real Estate Owned As Of 12/31/95</b>							
400 High St, SE, Salem, OR	1972		5,581,375	3,151,466	6,318,600		
2862 State St., Medford, OR (Glenmont)	1980		1,983,122	1,297,657	1,616,380		
3080 Broadway, North Bend, OR	1982		125,155	89,690	178,225		
115 SE 8th, Pendleton, OR	1975		118,850	61,601	87,580		
555 13th St, NE, Salem, OR	1989		1,832,940	1,552,399	2,650,000		
440 Church St, SE, Salem, OR	10/93		13,874,702	13,579,693	13,579,693		
480 Church St, SE, Salem, OR	10/93		1,257,751	1,226,571	1,226,571		
655 Bellevue St., SE, Salem, OR	1994		5,058,464	4,942,541	4,942,541		
<b>Real Estate Disposed of Prior to 12/31/95</b>							
Clark & Lawrence St Land, Eugene, OR	1988	12/90	15,000	15,000	18,510	20,000	5,000
79 Centennial Loop, Eugene, OR	1975	1983	240,995	198,228	322,200	308,500	110,272
999 Spring St, Medford, OR	1975	1982	123,508	106,854	208,400	215,000	108,146
355 NE Lafayette, Bend, OR	1975	11/85	74,230	58,648	88,000	78,000	19,352
Land - Boyd's Addition, Baker, OR	1976	9/84	20,229	20,229	12,060	15,000	(5,229)
600 Country Club Rd, Eugene, OR (lot 3100)	1981	12/89	2,378,777	1,969,857	1,757,410	2,021,077	51,220
Parcel 2608, Gateway Loop, Springfield, OR	6/86	11/87	120,800	120,800	106,400	90,000	(30,800)
Gateway St. tax lot 2300 Springfield, OR	1989	5/90	327,500	314,852	359,890	315,184	332

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Source: Table provided by Richard E. Sherman & Associates Inc.

**CORPORATE STANDARDS MANUAL**  
**Administrative Services Standards**  
**CSM 103 - Purchasing Policy**

- (i) Purchasing
- (i) Expendable Goods
- (i) Capital Equipment
- (i) Furnishings
- (i) Surplus Property
- (i) Service Contracts)
- (i) Purchase Orders
- (i) Purchase Requisitions
- (i) Central Stores
- (i) Surplus Dispositions
- (i) Receiving
- (i) Authorization
- (i) Office Supplies
- (i) Equipment
- (i) Approved Expenditures
- (i) Budget

The objective of SAIF Corporation's purchasing policy is to satisfy the company's requirements for materials, parts, services and supplies through the prudent expenditure of funds while contributing to the company's position as a positive member of the Oregon business community.

The Purchasing Section of the Administrative Services Division and chief financial officer (CFO) are the only authorized agents to negotiate and make commitments to vendors, unless the Purchasing Section specifies otherwise.

The Purchasing Section's responsibilities include:

- o Establishing and administrating purchasing policies
- o Communicating purchasing principles and practices
- o Negotiating and selecting vendors
- o Committing SAIF funds
- o Issuing binding legal purchasing documents
- o Maintaining good vendor relations

Each purchase must be covered by a SAIF purchase order, contract or agreement. While the Purchasing Section will make final purchasing commitments, various divisions may be called upon to help establish specifications, select vendors, negotiate and consult on services.

All purchases between \$1,000 and \$15,000 require price quotes, if a price agreement (contract to hold pricing for one year) is not in place. Purchases over \$15,000 not subject to price agreements will go through a formal bid process. Personal services are subject to the CSM Contracts Policy 245. (attached).

SAIF solicits bids from selected, qualified vendors. All solicited vendors are given equal opportunity for submitting their bids. Selection is based on the vendor's ability to satisfy SAIF's requirements, which include quality, price, continuity of supply and service. SAIF wishes to maintain relationships with proven vendors. SAIF also continuously seeks

CORPORATE STANDARDS MANUAL A174  
Administrative Services Standards  
CSM 103 - Purchasing Policy  
new and improved sources.

SAIF deals with vendors fairly and impartially by extending equal opportunity to all vendors to present products and services. SAIF wishes to be recognized as a good customer and insures prompt, courteous treatment of vendors. SAIF solicits as few samples as possible.

Purchasing at SAIF is conducted in accordance with all applicable government regulations. SAIF encourages procurement from small businesses when they are technically and financially qualified. We seek and develop purchasing relationships with minorities and the handicapped.

SAIF personnel dealing with vendors will conduct themselves ethically. SAIF's Purchasing Section will at all times avoid fraud, waste and abuse. Purchasing will require documentation from specifiers to insure they also avoid fraud, waste and abuse. SAIF's Purchasing Section and division specifiers will be free of personal interests that conflict or appear to conflict with the best interests of SAIF as determined by chief financial officer. SAIF employees and family members will not receive gifts or gratuities of any type from vendors.

If promotional premiums are offered, the SAIF representative will attempt to obtain a cash discount for SAIF instead, or decline the offer if a discount is not available.

Reciprocity is not a factor in SAIF procurement. We give all vendors equal consideration. Buying is based on the merits of the purchased item, such as quality and price, and the vendor's performance. Reciprocal buying would limit supply sources and be detrimental to improving quality and price of our products. The aforementioned does not prohibit SAIF from purchasing from SAIF insureds - every thing else being equal.

References:

- ACC 516 - Capital Equipment Policy
- ASD 414 - Receiving Procedure
- CSM 070 - Administrative Expense Disbursements Policy
- CSM 104 - Central Stores Supply Request Procedure
- CSM 105 - Expendable Goods Procedure
- CSM 106 - Capital Equipment Procedure
- CSM 108 - Request for External Services Procedure
- CSM 109 - Permanent Property Control Procedure
- CSM 110 - Surplus Property Disposition Procedure

Effective Date: August 13, 1987

Revised Date: March 21, 1991

Review Date: April 1, 1992

CSMAS103



**INDUSTRY COMPARISON BASED UPON DIRECT EXPENSES INCURRED**

	1992	1993	1994	1995
<b>SAIF</b>				
Total expenses	92,568,280	106,712,815	113,582,819	115,475,099
Direct premiums earned	259,977,660	255,480,563	267,772,916	244,504,398
Ratio of total expenses to premium	0.356	0.418	0.424	0.472
Number of employees as of 12/31	1,149	1,142	1,152	1,092
No. of employ.per \$1 mil. prem.	4.4	4.5	4.3	4.5
<hr/>				
<b>Liberty Northwest Insurance Company</b>				
Total expenses	35,369,124	30,672,526	36,630,770	42,726,823
Direct premiums earned	166,339,734	148,704,579	165,230,805	174,011,630
Ratio of total expenses to premium	0.213	0.206	0.222	0.246
Number of employees not available				
<hr/>				
<b>California State Compensation Insurance Fund</b>				
Total expenses	392,879,413	435,316,444	450,631,451	433,629,150
Direct premiums earned	1,755,372,216	1,705,362,553	1,455,870,432	1,072,672,421
Ratio of total expenses to premium	0.224	0.255	0.310	0.404
Number of employees not available				
<hr/>				
<b>Idaho State Insurance Fund</b>				
Total expenses	14,719,673	20,054,197	18,995,888	17,767,367
Direct premiums earned	97,709,211	116,490,665	134,867,335	132,275,179
Ratio of total expenses to premium	0.151	0.172	0.141	0.134
Number of employees not available				
<hr/>				
<b>Worker Compensation Fund of Utah</b>				
Total expenses	Not available	28,780,500	39,407,540	39,359,153
Direct premiums earned	127,112,000	151,850,000	159,050,000	144,635,225
Ratio of total expenses to premium		0.190	0.248	0.272
Number of employees not available				

The Kennemer Letter asked for a comparison of SAIF with state funds in California, Idaho and Montana. Montana does not file an Annual Statement with the NAIC. Therefore, no data was available. Utah was included in the place of Montana.

Data on California, Idaho and Utah state funds was obtained from the NAIC database which only has information for 5 years.

Data for SAIF and Liberty Northwest Insurance Company was obtained from filed Annual Statements.

Source: Table provided by Richard E. Sherman & Associates Inc.

