



**FILED**

OFFICE OF INSURANCE REGULATION

AUG 30 2012

KEVIN M. McCARTY  
COMMISSIONER

OFFICE OF  
INSURANCE REGULATION  
Deletated by QPS

IN THE MATTER OF:

CASE NO. 127610-12

2012 Profit and Contingency Factors

ORDER PUBLISHING OPTIONAL UNDERWRITING PROFIT AND CONTINGENCY FACTORS  
CALCULATED IN ACCORDANCE WITH RULE 69O-170.003, FLORIDA ADMINISTRATIVE CODE

Pursuant to Rule 69O-170.003, Florida Administrative Code, which requires the Office of Insurance Regulation (hereinafter the "OFFICE") to establish appropriate underwriting profit and contingency factors by annual statement lines or classes for insurers to use in calculating investment income, the OFFICE hereby finds as follows:

1. The OFFICE has jurisdiction over the subject matter of this Order and the affected parties.
2. Pursuant to Florida Statutes Section 627.062(2)(b)4., the commission has adopted by rule the manner in which investment income is used to calculate insurance rates. As required by this Section, the manner of calculation contemplates allowances for an underwriting profit and contingency factor and full consideration of investment income which produce a reasonable rate of return. (See exhibit "A" attached.)
3. Subsection (9) of Rule 69O-170.003 states that the OFFICE shall by Order establish appropriate underwriting profit and contingency factors that may be used in rate filings. Pursuant to Subsection (3) of Rule 69O-170.003, insurers may use the profit and contingency factors referenced below when they are unable to produce credible or appropriate profit and contingency factors from their own data. (See exhibit "B" attached).
4. The following profit and contingency factors were properly derived by the OFFICE using available and actuarially reasonable industry data:

LINE OF BUSINESS

2012 FACTOR

ALLIED LINES

3.5%

BOILER & MACHINERY

1.0%

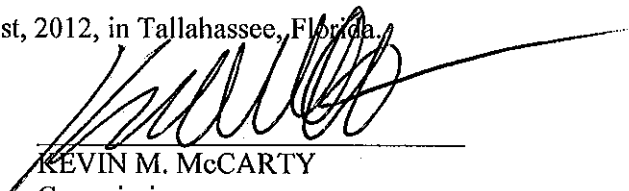
BURGLARY & THEFT	3.5%
COMMERCIAL AUTO LIABILITY	0.4%
COMMERCIAL AUTO PHYSICAL DAMAGE	4.9%
COMMERCIAL MULTIPLE PERIL (BUSINESS OWNERS)	1.2%
CREDIT	4.4%
EARTHQUAKE	3.4%
FARMOWNERS	4.1%
FIDELITY	2.3%
FINANCIAL GUARANTY	3.4%
FIRE	3.6%
HOMEOWNERS	4.1%
INLAND MARINE	3.5%
MEDICAL MALPRACTICE - CLAIMS MADE	-3.6%
MEDICAL MALPRACTICE - OCCURRENCE	-9.6%
MORTGAGE GUARANTY	0.9%
OTHER LIABILITY - CLAIMS MADE	-4.0%
OTHER LIABILITY - OCCURRENCE	-5.2%
PRODUCTS LIABILITY - CLAIMS MADE	-5.2%
PRODUCTS LIABILITY - OCCURRENCE	-8.4%
SURETY	3.2%

Pursuant to these findings, it is HEREBY ORDERED:

The profit and contingency factors set out specifically in paragraph 3 herein are determined to be the appropriate profit and contingency factors by annual line statement or class and may be used in all future rate filings submitted to the Office of Insurance Regulation. These factors replace any other factors previously in effect and will remain in effect until a future order supersedes them.

DONE and ORDERED this 30<sup>th</sup> day of August, 2012, in Tallahassee, Florida.



  
 KEVIN M. McCARTY  
 Commissioner

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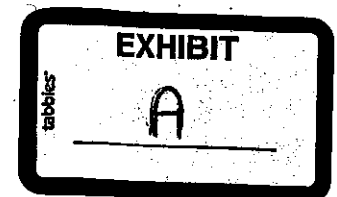
*All Property and Casualty Insurance Carriers*

**Florida Statutes §627.062, Rate standards--**

(2) As to all such classes of insurance:

(b) Upon receiving a rate filing, the office shall review the filing to determine if a rate is excessive, inadequate, or unfairly discriminatory. In making that determination, the office shall, in accordance with generally accepted and reasonable actuarial techniques, consider the following factors:

4. Investment income reasonably expected by the insurer, consistent with the insurer's investment practices, from investable premiums anticipated in the filing, plus any other expected income from currently invested assets representing the amount expected on unearned premium reserves and loss reserves. The commission may adopt rules using reasonable techniques of actuarial science and economics to specify the manner in which insurers calculate investment income attributable to classes of insurance written in this state and the manner in which investment income is used to calculate insurance rates. Such manner must contemplate allowances for an underwriting profit factor and full consideration of investment income which produce a reasonable rate of return; however, investment income from invested surplus may not be considered.



Rule 69O-170.003, F.A.C. Calculation of Investment Income.

(1) The purpose of this rule is to specify the manner in which insurers shall calculate investment income attributable to insurance policies written in Florida and the manner in which such investment income is used in the calculation of insurance rates by the development of an underwriting profit and contingency factor compatible with a reasonable rate of return.

(2) As used herein:

(a) "Insurance" means all classes of insurance subject to Section 627.062, F.S.

(b) "Subline" means a type of insurance uniquely identified for purposes of establishing rates under Section 627.062, F.S.

(c) "Property insurance subline" means insurance as defined in Section 624.604, F.S.

(d) Insurer includes rating organizations licensed in Florida.

(e) An underwriting profit and contingency factor can be positive or negative.

(3) Each insurer shall determine separately for each subline of insurance the expected patterns of loss payments over time associated with insurance written in Florida. The determination shall be made using Florida accident year or policy year loss payment patterns, and must fairly represent the insurance loss transaction of the insurer. If Florida data is not credible or is inappropriate, the insurer may exercise reasonable actuarial judgment in utilizing other relevant data or procedures or may use the underwriting profit and contingency factors referred to in subsection (9) of this rule.

(4) Each insurer shall determine  $Y_A$ , the expected investment income yield on invested assets representing unearned premium and loss reserves. The expected investment income yield,  $Y_A$ , shall be calculated using the quantities and formula below:

$$Y_A = Y_N W_N + Y_O W_O$$

Where:

$Y_N$  = Expected investment income yield on assets newly invested or reinvested during the time the new rates are expected to be in effect.

$Y_O$  = Expected investment income yield on assets invested prior to the time the new rates are expected to be in effect.

$W_N$  = Proportion of assets, held during the time the new rates are expected to be in effect, that is expected to be newly invested or reinvested.

$$W_O = 1 - W_N$$

The above expected investment income yield,  $Y_A$ , shall be used for purposes of this rule unless evidence is presented that this quantity is not the investment income yield reasonably expected by the insurer.

(5) Separately for each subline, each insurer shall, using the average date of premium remittance by the insured, determine the discounted value of the expected loss payment pattern determined in subsection (3) using the expected investment income yield,  $Y_A$ , calculated in subsection (4). The undiscounted pattern minus the discounted pattern for each subline is to be expressed as a percent of the expected subline premium that is associated with the series of loss payments over time. This difference is the investment income opportunity associated with the subline.

(6) The investment income opportunities calculated in subsection (5) shall be used as follows to develop the underwriting profit allowance, to be used in rate filings:

(a) Select and specify the underwriting profit and contingency factor to be used in rate filings for the property insurance subline with the smallest investment income opportunity as calculated in subsection (5). If an insurer does not write property insurance in Florida, it shall use relevant data for such property insurance subline from areas other than Florida or shall use industry data, as determined by reasonable



actuarial judgment. The selected underwriting profit and contingency factor is presumed to give due recognition to property insurance investment income. An underwriting profit and contingency factor greater than the quantity five percent is prima facie evidence of an excessive expected rate of return and unacceptable, unless supporting evidence is presented demonstrating that an underwriting profit and contingency factor included in the filing that is greater than this quantity is necessary for the insurer to earn a reasonable expected rate of return. In such case, the criteria presented in subsection (7) shall be used by the Office of Insurance Regulation in evaluating this supporting evidence.

(b) Determine the investment income differential between the property insurance subline and any other subline by subtracting the investment income opportunity for the property insurance subline as calculated in subsection (5) from the investment income opportunity for any other subline as calculated in subsection (5).

(c) The underwriting profit and contingency factor for any subline other than that specified in paragraph (6)(a) shall be the underwriting profit and contingency factor for the subline from paragraph (6)(a), minus the investment income differential from paragraph (6)(b). An underwriting profit and contingency factor greater than this quantity is prima facie evidence of an excessive expected rate of return and unacceptable, unless supporting evidence is presented demonstrating that an underwriting profit and contingency factor included in the filings that is greater than this quantity is necessary for the insurer to earn a reasonable rate of return. In such cases, the criteria presented in subsection (7) shall be used by the Office in evaluating this supporting evidence.

(7) An underwriting profit and contingency factor calculated in accordance with this rule is considered to be compatible with a reasonable expected rate of return on net worth. If a determination must be made as to whether an expected rate of return is reasonable, the following criteria shall be used in that determination:

(a) An expected rate of return for Florida business is to be considered reasonable if, when sustained by the insurer for its business during the period for which the rates under scrutiny are in effect, it neither threatens the insurer's solvency nor makes the insurer more attractive to policyholders or investors from a corporate financial perspective than the same insurer would be had this rule not been implemented, all other variables being equal; or

(b) Alternatively, the expected rate of return for Florida business is to be considered reasonable if it is commensurate with the rate of return anticipated for other industries having corresponding risk and it is sufficient to assure confidence in the financial integrity of the insurer so as to maintain its credit and, if a stock insurer, to attract capital, or if a mutual or reciprocal insurer, to accumulate surplus reasonably necessary to support growth in Florida premium volume reasonably expected during the time the rates under scrutiny are in effect.

(8) Each insurer filing insurance rates in Florida shall use an underwriting profit and contingency factor for each subline that is developed in accordance with this rule. The combined profit and contingency factor shall be quantified and stated as a single percentage factor. The entire factor and the component parts of the factors shall be justified by the insurer proposing to use the factor.

(9) For use as permitted in subsection (3) of this rule, the Office shall annually establish appropriate underwriting profit and contingency factors by annual statement lines or classes subject to this rule. Such factors shall be derived by using available and actuarially reasonable industry data. The factors shall be established by order and provided to all affected insurers prior to the date their use is required. Factors distributed for the previous year shall remain in effect until new factors are published.