Packaging Your Account to Be Underwritten for Insurance

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Packaging Your Account to be Underwritten for Insurance

As a former Underwriter, it is my opinion that the time spent to prepare your account to become a submission (a request for an insurance quote) is an investment in potentially lower insurance cost and possibly more carriers/quotes to choose from. This information is focused on the underwriting of Workers' Compensation insurance, but the principles can be applied to all lines of coverage. When your account is submitted to an insurance company it is usually in the form of a submission prepared by your insurance agent(s). That submission 'paints a picture' for the underwriters who decides what is a fair rate to charge for the risk of loss your account creates from business operations. The more 'brush strokes' in the picture, in the form of information, the clearer the picture and the better the chance of an informed decision by the underwriter.

Employers should spend a little time developing their account just as if they were going to sell their products or services to a potential client. When you think about it the Underwriter and insurance company will be your partner for the next year and hopefully many years. They need to know who they are getting into bed with. They need information that will lead a reasonable person to believe that based on the submitted information the insurance company will make a profit on this account. This is called an underwriting profit and is an absolute necessity for an insurance company to survive.

The first main idea to understand is that underwriters are human creatures that have a job to do. They base their decisions on information. Secondly, insurance companies are for- profit entitles and, just like all other companies, if they do not make a profit they will not be in business for long. Regardless of the legal form such as stock carrier, mutual or self-insured fund, if a carrier does not make an Underwriting Profit, they will not be able to stay in business bearing risk. As a general rule an account is considered “profitable” if the Loss Ratio is below 65%. The Loss Ratio is Your Losses divided by Your premium. The lower the loss ratio is, the happier the underwriter because your account generates profit to the insurance company.

Understand that the Premium dollar is allocated as such:

Your Account Losses: 65% of the premium
Carrier Expenses: 30% of the premium
Profit: 5%
Total Premium: 100%

Understand that the base or beginning rate before modification comes from the historical losses of your industry. That rate is modified up or down based on your individual claims experience. The expense portion of the rate goes to cover payroll of employees, office expenses, state assessment to fund rating bodies, Second Injury Fun tax, premium tax, and to buy Reinsurance. The profit is not guaranteed because before the policy year underwriters do not know what the actual cost of losses will be. They are using actuarial information to charge a rate adequate premium, yet remain competitive to write the account, if quoted. I know of no other business where “the cost of goods”, in this case the losses, are priced before they are known.

Now you might say; ‘Wait a minute, I know those insurance companies put their money into the stock market and make Investment Income.’ That is true and needs to be clarified. Insurance company investments are highly regulated by state laws so carriers cannot invest in highly speculative instruments. Therefore, the rate of return is lower than other investments. Another key point is that the investment market is down so returns are down. In fact, my 401K turned into a 201K! Suffice to say that in past years investment income was more heavily relied on to augment underwriting profit but that is a limited case these days.

Underwriters seek information to make informed decisions about an account.

The first three choices an Underwriter has is:

1) Quote
2) Do not quote, called a Declination
3) Need more information to make a decision, called a Request for Information.

The first step in understanding insurance pricing is in how rates are calculated.

Rates for insurance come from three general ingredients:
1) the cost of injuries (claims) in your industry

2) carrier expenses

3) a load for profit

Rates can be modified with Schedule Rating and Experience Rating.
Experience Rating, as the name implies, looks at the historical loss experience of the account and compares that experience to the whole population of your industry. If you have losses that have cost more than the average, then your account is giving a Debit Rating and your coverage may cost more. If you have had a loss experience that is above average that is your company had fewer losses that the total population of your industry, you earn an experience Credit. Knowing your Experience Modification Factor is the second step in understanding pricing.

The third step is Schedule Rating which is Underwriter Discretion. This is the judgment part of the pricing. An Underwriter will need to know what exactly the employer is doing to prevent and manage losses. The Schedule Rating portion of underwriting is just like Experience Modifiers, in the forms of rate credits and debits. Usually, Underwriters have Schedule Rating ability up to +/- 25 %. For the best accounts, those with credit Mods, evidence of written safety programs and evidence of injury management procedures, will get the most credits. That is because Underwriters know that this account, based on the management loss control programs, will generate a higher probability of generating an Underwriting Profit.

An Underwriter should be provided, and if not may ask for, the following:

► What is the description of operations? Do not leave this up to your agent to develop. Instead, you may want to develop a one-time “Description of Operations” and only change when your operations change.

It does not need to be elaborate but should cover:

The basic mission of your company
The task to achieve that mission
Your experience in this industry
The experience of your key staff, include resumes’ and biography’s
The number of employees (full and part time)
Where employees are located they are located
Turn Over of employees (less is better)
Your Hiring Procedures
What is the pay for your industry (low, moderate, high)
Is there a Drug Free Work Place
New Worker Orientation- do you do it
Is there a benefit program (health, dental, life coverage, and 401K) all of these items
indicate desirability of employment.

►Regarding your ability to prevent and control losses the Underwriter will want to know:

Is top management committed to a safe workplace?
Does the account have a written safety program?
Do you have safety responsibility assigned to a single person?
What is their name?
Can the agent send evidence of Safety Meetings?

Does this account know what the hazards are in their industry and what are they doing to control those hazards?

Make a written statement on your letterhead that it is your intent to work with the insurance company staff in the areas of Loss Control and Claims Management. That may be expected but to have it in writing validates the expected. Provide your marketing literature so the Underwriter can get a view and feel for your operations. Provide your website address so Underwriters can see you message to the world. Educate the underwriter on your operations. For example, if your account uses chemicals then explain the type, usage, control, and exposed employees. Indicate if the chemical is potentially explosive, reactive, non-reactive, etc. Provide evidence of documentation and the Material Safety Data Sheet; the technical bulletin that explains the chemicals hazards and controls.

ACORD Forms are the standard application submitted by agents. (ACORD stands for: Agency Communications On Research and Development).

This basic information should be supplemented with:

►An executive summary of your organization

►General and physical information account your account

►Safety or industrial certifications, e.g., ISO 9001, and their value

►Coverage Specifications

►Complete loss data and explanations of large claims

►Include Photographs of your operations

►Include financial statements, this shows you are viable and will remain in business.

Employers can prepare their accounts for review by an underwriter by taking some time to develop the information that underwriters will need to make an informed decision. Once the Underwriter understands that you know the insurance company has to make a profit the underwriter will feel that you are on the same page. In fact, I recall during a presentation to a large prospective client that the President of the Company said, “Chris I want you to make as much on my account as you can”. Wow, that guy understood the program. We did get the account and did make an underwriting profit.

I suspect that employers often feel that they are at the mercy of the insurance industry. Perhaps they feel that there is some grand scheme where carriers collude to make sure they make a profit. Well, that is not the case. In fact, the insurance industry has lost money for 5 years in a row. Now you might say that is their fault for pricing accounts to low or that is the nature of competition. Perhaps you are right but understand that the insurance industry has bled enough money and now is seeking price increases to cover past losses and poor market returns.

The Combined Ratio is the combination of carrier expenses and loss ratio for the industry. So, if the Combined Ratio exceeds 100% then carrier has spent all of the premiums collected on losses, expenses, and no profit to enjoy.

So, for 5 years in a row the industry paid out more than it took in. No industry can stay in business for long with those types of

results. So, the solution is to take more in, hence increased rates, and therefore premium increases. Underwriters need to write
business to attempt to generate an underwriting profit. The underwriting standards have gotten much tougher, and underwriters are asking more questions and demanding high levels of performance from accounts to prevent and manage losses. Add to the equation the Coward Attacks of September 11, 2001 and you can see the insurance industry has some ground to make up as it is projected, they will pay out $40 Billion due to these unexpected events. The actuarial models of past losses did NOT contemplate these events and therefore reasonable premium was not charged. Rates are going up now but where would we be if the insurance industry was not in place to bear this huge financial burden?

I say we should look at the insurance industry with pride and say that have weathered the storm. In evidence of just how much of a blow the 9/11 attacks where we can look to the number of companies downgraded by A.M. Best. Best rates insurance companies based on financial strength and the ability to pay current and future claims. In 2002 Best lowered the Financial Rating of 648 companies. To contrast that number in 2001 Best lowered the rating of only 380, 421 the year before and 314 the year before that. (Source A.M. Best).

The downgrades were due to poor financial strength for three reasons:

1) Years of predatory pricing- accepting accounts for too little premium to cover previously mentioned expenses
2) Poor investment returns
3) September 11, 2001 coward attacks

So, the insurance industry has been hammered by losses exceeding premium. To recover carriers are increasing prices across the board. To improve your pricing and gain a competitive advantage you may want to evaluate your risk from the viewpoint of an underwriter so you will have a better understanding from their side of the desk. Once that is in perspective you may want to evaluate how your account is presented to underwriters because in doing so you increase the probability of obtaining competitive pricing.

It is a new day in the way risk is analyzed and priced. By partnering with a carrier and focusing on workplace safety and injury management employers can earn pricing better than their industry competitors and enjoy a bid advantage.