

**STATE OF CALIFORNIA
DEPARTMENT OF INSURANCE**
45 Fremont Street, 21st Floor
San Francisco, CA 94105

June 5, 2002

File No. RH01018851

**NOTICE OF WORKSHOP
AND GENERIC DETERMINATIONS HEARING**

The Insurance Commissioner of the State of California (“Commissioner”) hereby gives notice that, pursuant to the provisions of Title 10, California Code of Regulations, Section 2646.3, he proposes to make findings and determinations concerning the following generic factors:

- Catastrophe Adjustment** (Cal.Code Regs, Tit. 10, § 2644.5)
- Loss Development** (Cal.Code Regs., Tit. 10, § 2644.6)
- Loss Trend** (Cal.Code Regs., Tit. 10, § 2644.7)
- Trending Of Allocated Loss Adjustment Expenses** (Cal.Code Regs., Tit. 10, § 2644.8)
- Executive Compensation** (Cal.Code Regs., Tit. 10, § 2644.10(b))
- Expense Trend** (Cal.Code Regs., Tit. 10, § 2644.11)
- Efficiency Standard** (Cal.Code Regs., Tit. 10, § 2644.12)
- Rate Of Return** (Cal.Code Regs., Tit. 10, § 2644.16)
- Leverage Factors** (Cal.Code Regs., Tit. 10, § 2644.17) and
- Credibility Adjustment** (Cal.Code Regs., Tit. 10, § 2644.23).

The proposed generic determinations largely adopt the factors the Department historically has been using to review rate applications on a case-by-case basis. As such, it is expected that adoption of generic factor regulations will have no significant material impact on the process by which the Department reviews individual company rate applications.

HEARING DATE, LOCATION, AND TIME

The hearing is scheduled for two days beginning as follows:

Thursday, July 18, 2002 – 8:30 a.m.
California Department of Insurance
45 Fremont Street, 22nd Floor Hearing Room
San Francisco, CA 94105

PROCEDURE

These proceedings are part of the rulemaking process and involve findings of general applicability relating to insurance ratemaking (also known as “generic determinations”). Additionally, pursuant to California Government Code Section 11346.45(a), these proceedings are designed to involve parties who would be subject to or interested in the proposed regulations in a public workshop and discussion regarding the proposed regulations.

The Commissioner recognizes that input from the public and the insurance industry, including input from actuaries, economists and other experts in the field of rate regulation makes for a balanced approach and benefits all those involved. He is also aware that the hearing must be kept to a manageable size. With that in mind, the Commissioner herein provides the following specific timelines and procedures by which the hearing is to be conducted:

1) Any person may submit written comments relating to the subject matter of this hearing, subject to certain limitations explained in detail below. Persons who wish to provide oral comments at the hearing must file those comments with the Department in writing no later than **Monday, July 1, 2002**, at 5:00 p.m. Any person desiring to provide written comments only, without providing oral comments at the hearing, must file those comments with the Department in writing no later than **Friday, July 17, 2002**, at 5:00 p.m.

The Commissioner will accept comments relating only to the values presented in the specific generic determinations, the reasonableness of the methodology employed to arrive at those values, the data used to make those determinations and, only where applicable, the soundness of the actual calculations.

While the Commissioner recognizes that not every aspect of the regulations was specifically ruled on in *20th Century Ins. Co. v. Garamendi* (1994) 8 Cal.4th 216, 32 Cal.Rptr.2d 807; 878 P.2d 566, the case makes clear the Commissioner’s power to promulgate regulations of general applicability. As such, any challenge to the overall regulatory plan as set forth in Title 10, California Code of Regulations, Sections 2641.1 through 2646.5 serves no constructive purpose, but rather, takes away from the efficacy of these proceedings.

Accordingly, the Commissioner will not accept, or respond to, any comment or statement relating to any aspect of regulations already promulgated.

2) Written comments shall be directed to:

Donald P. Hilla, Senior Staff Counsel
California Department of Insurance
45 Fremont Street, 21st Floor
San Francisco, CA 94105
Telephone: (415) 538-4108

Written comments may also be sent as a Microsoft Word attachment via e-mail to hillad@insurance.ca.gov.

- 3) Persons who submit comments by 5:00 p.m. on July 1, 2002, will be given the opportunity to provide an oral presentation to the hearing panel. Persons providing oral comments at the hearing shall be prepared to answer questions and/or otherwise provide further information at the hearing panel's request. Persons wishing to give oral presentations at the hearing will be subject to a time limit of a maximum of five minutes per hearing topic. The Commissioner will modify this time limit at the hearing if warranted.
- 4) Persons wishing to provide oral comments may present a brief synopsis of their written comments at the hearing. However, the purpose in addressing the hearing panel will be to allow the panel to ask questions related to the submitted comments. Reading verbatim from previously submitted written comments will not be permitted.
- 5) The hearing has been scheduled to take no more than two (2) business days.
- 6) Persons or groups representing the interests of consumers may be entitled to reasonable advocacy fees, witness fees, and other reasonable expenses, in accordance with the provisions of subchapter 4.5, title 10, of the California Code of Regulations, in connection with their participation in this matter. Persons interested in inquiring about the appropriate procedures should contact the Office of the Public Advisor at the following address:

California Department of Insurance
Office of the Public Advisor
300 Capitol Mall, 17th Floor
Sacramento, CA 95814
(916) 492-3559

A copy of any written materials submitted to the Public Advisor regarding this proceeding must also be submitted to the contact person listed above. Please contact the Office of the Public Advisor for further information.

- 7) Persons desiring to become parties, and thus on the mailing list for this proceeding, shall submit a written request to that effect to:

Donald P. Hilla, Senior Staff Counsel
California Department of Insurance
45 Fremont Street, 21st Floor
San Francisco, CA 94105

SCHEDULE

The following schedule shall be observed.

PLEASE NOTE: In the event certain issues take less time to address than contemplated by the schedule, the panel will proceed to the next scheduled issue.

July 1, 2002

For those wishing to provide oral comments at the hearing, written comments must be submitted to the Department by 5:00 p.m. on this date.

July 18, 2002

8:30 a.m. – 10:15 p.m.

Comments relating to the Department's formulation and calculation of rate of return (Cal.Code Regs., tit. 10, § 2644.16) will be entertained.

10:15 a.m. – 10:30 a.m.

Morning Break.

10:30 a.m. – 11:30 a.m.

Continuation of comments relating to the Department's formulation and calculation of rate of return (Cal.Code Regs., tit. 10, § 2644.16) will be entertained.

11:30 p.m. – 12:00 noon.

Comments relating to the Department's formulation and calculation of leverage factors (Cal.Code Regs., tit. 10, § 2644.17) will be entertained.

12:00 noon – 1:00 p.m.

Lunch Break

1:00 p.m. – 2:30 p.m.

Continuation of comments relating to the Department's formulation and calculation of leverage factors (Cal.Code Regs., tit. 10, § 2644.17) will be entertained.

2:30 p.m. – 3:30 p.m.

Comments relating to the number of years for catastrophe losses to be averaged (Cal.Code Regs, tit. 10, § 2644.5) will be entertained.

3:30 p.m. -- 3:45 p.m.

Afternoon Break.

3:45 p.m. – 5:00 p.m.

Comments relating to the number of intervals specified for loss development factors (Cal.Code Regs., tit. 10, § 2644.6) will be entertained.

July 19, 2002

8:30 a.m. – 10:00 a.m.

Comments relating to the Department's formulation and calculation of loss trend factors (Cal.Code Regs., tit. 10, § 2644.7) will be entertained.

10:00 a.m. -- 10:15 a.m.

Morning Break.

10:15 a.m. – 11:30 a.m.

Comments relating to the Department's formulation and calculation of allocated loss adjustment expense trends (Cal.Code Regs., tit. 10, § 2644.8) will be entertained.

11:30 a.m. – 12:00 noon

Comments relating to the Department's proposed executive compensation factor (Cal.Code Regs., tit. 10, § 2644.10(b)) will be entertained.

12:00 noon – 1:00 p.m.

Lunch Break.

1:00 p.m. – 1:30 p.m.

Continuation of comments relating to the Department's proposed executive compensation factor (Cal.Code Regs., tit. 10, § 2644.10(b)) will be entertained.

1:30 p.m. – 2:30 p.m.

Comments relating to the Department's formulation and calculation of expense trend (Cal.Code Regs., tit. 10, § 2644.11) will be entertained.

2:30 p.m. – 2:45 p.m.

Afternoon Break

2:45 p.m. -- 4:00 p.m.

Comments relating to the Department's formulation and calculation of the efficiency standard (Cal.Code Regs., tit. 10, § 2644.12) will be entertained.

4:00 p.m. – 5:00 p.m..

Comments relating to the Department’s formulation and calculation of credibility adjustment (Cal.Code Regs., tit. 10, § 2644.23) will be entertained.

BACKGROUND

Proposition 103, an initiative approved by the citizens of California on November 8, 1988, established, among other things, a system of prior approval rate regulation for property-casualty insurance in California.

California Insurance Code Section 1861.01(c) provides that commencing November 8, 1989, insurance rates must be approved by the Commissioner prior to their use.

California Insurance Code Sections 1861.05(a) and (b) provide:

(a) No rate shall be approved or remain in effect which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter. In considering whether a rate is excessive, inadequate or unfairly discriminatory, no consideration shall be given to the degree of competition and the commissioner shall consider whether the rate mathematically reflects the insurance company's investment income.

(b) Every insurer which desires to change any rate shall file a complete rate application with the commissioner. A complete rate application shall include all data referred to in Sections 1857.7, 1857.9, and 1864 and such other information as the commissioner may require. The applicant shall have the burden of proving that the requested rate change is justified and meets the requirements of this article.

In *Calfarm Insurance Company v. Deukmejian* (1989) 48 Cal.3d 805, the California Supreme court unequivocally affirmed the constitutionality of Insurance Code section 1861.05 which, according to the court, “requires rates within that range which can be described as fair and reasonable and prohibits approval or maintenance of confiscatory rates.”

In *20th Century Ins. Co. v. Garamendi* (1994) 8 Cal.4th 216, 32 Cal.Rptr.2d 807; 878 P.2d 566, the Supreme Court upheld the Commissioner’s regulations implementing the rate approval provisions of Proposition 103. Those regulations are found at Title 10, California Code of Regulations, Sections 2641.1 through 2646.5. As set forth in this notice, various sections of those regulations require the Commissioner to adopt certain numeric factors to be inserted into the ratemaking formula. Section 2646.3 sets forth the procedure for the adoption of those factors. Therefore, the Commissioner is holding the required “generic hearings” to seek input and guidance from the public and the insurance industry regarding the generic determinations.

ISSUES / PROPOSED GENERIC DETERMINATIONS

The purpose of this hearing is to receive comments from those entities directly affected, as well as from insurance consumers and citizens, in order to select a series of generic determinations relating to the prior approval of insurance rates. Following this hearing, the Commissioner

intends to promulgate regulations adopting the generic determinations.

Where the Commissioner has not promulgated a numerical value for a generic factor in a given line, values submitted by insurers in rate filings will be evaluated using generally accepted actuarial principles and standards of reasonableness to ensure that the resulting rates are not excessive, inadequate, unfairly discriminatory, or otherwise in violation of law.

Where a specific generic factor is not proposed in this notice, the Commissioner requests comment and supporting data regarding which number he should adopt.

These hearings are convened for the purpose of gathering public input in the following areas:

1) **2644.5 Catastrophe Adjustment**

This section requires the commissioner to set, by line, the number of years to be used to average, or “smooth,” catastrophe losses. The chart below contains the minimum number of years to be used in smoothing catastrophe losses.

The number of years used to smooth catastrophe losses are from the latest approved ISO loss cost filing for each line of business.

CATASTROPHE ADJUSTMENT	No. of Years
Fire	
* Personal Dwelling Fire	22 Years
* Personal Dwelling Extended Coverage	39 Years
* Commercial Property Fire Basic Group I	10 Years
* Commercial Property Fire Basic Group II	50 Years
* Commercial Property Fire Special Causes of Losses	14 Years
Allied Lines	See Fire
Multiple Peril Crop	
Farmowners Multiple Peril:	
* Farm Property	48 Years
Homeowners Multiple Peril:	
* Fire	21 Years
* Wind	39 Years
Commercial Multiple Peril (non-liability)	
* Fire	5 Years
* Extended Coverage / Business Group II	48 Years
* Special Causes of Loss	12 Years
Inland Marine	
Medical Malpractice	
Earthquake	
Other Liability	
Private Passenger Auto Liability	
Commercial Auto Liability	

Private Passenger Auto Physical Damage	34 Years
Commercial Auto Physical Damage	
* Excess Wind and Water Other Than Collision – Commercial Cars and Private Passenger Types	12 Years
Aircraft (all perils)	
Fidelity	
Surety	
Burglary and Theft	
Boiler and Machinery	
Credit	

2) 2644.6 Loss Development

This section provides that the Commissioner prescribe the number of reporting intervals to be used in determining the company specific loss development factor. The chart below contains the minimum number of reporting intervals to be used in determining the loss development factor.

The number of loss reporting intervals are from the latest approved ISO loss cost filing for each line of business.

LOSS DEVELOPMENT	Reporting Interval
Personal Fire	6 Reporting Intervals
* Commercial Property Basic Group I, II and Special Causes of Loss	4 Reporting Intervals
Allied Lines	
Multiple Peril Crop	
Farmowners Multiple Peril	
* Liability	18 Reporting Intervals
Homeowners Multiple Peril	6 Reporting Intervals
Commercial Multiple Peril	9 Reporting Intervals
Inland Marine	
Medical Malpractice	19 Reporting Intervals
Earthquake	
Other Liability	
* Premises and Operations: M&C and OL&T – Bodily Injury and Property Damage	18 Reporting Intervals
M&C and OL&T – Fringe	12 Reporting Intervals
* Products/Completed Operations: Bodily Injury and Property Damage	19 Reporting Intervals
Private Passenger Auto Liability	
* Bodily Injury Liability and Uninsured Motorist Liability * Property Damage Liability and Medical	6 Reporting Intervals

Payments	2 Reporting Intervals
Commercial Auto Liability	
* Commercial Cars and Private Passenger Types Bodily Injury	9 Reporting Intervals
* Commercial Cars and Private Passenger Types Property Damage	8 Reporting Intervals
* Garage Dealers and Services Bodily Injury	8 Reporting Intervals
* Garage Dealers and Services Property Damage	7 Reporting Intervals
Private Passenger Auto Physical Damage	
Commercial Auto Physical Damage	
* Commercial Cars and Private Passenger Types OTC & Collision	9 Reporting Intervals
Aircraft (all perils)	
Fidelity	8 Reporting Intervals
Surety	
Burglary and Theft	8 Reporting Intervals
Boiler and Machinery	
Credit	

3) **2644.7 Loss Trend**

This section requires that the Commissioner adopt loss trend factors for those lines of insurance subject to prior approval. The chart below contains the loss trend factors, by line of insurance.

The loss trend factors are from the latest approved ISO loss cost file for each line of insurance, with the exception of private passenger automobile, where Fast Track data was used. .

LOSS TREND	Factor
Fire	
* Personal Dwelling Fire and Extended Coverage:	4.7%
* Commercial Property:	
Building Annual Rate of Change	1.8%
Content Annual Rate of Change	4.6%
Time Element Annual Rate of Change	0.8%
Allied Lines	
Multiple Peril Crop	
Farmowners Multiple Peril	
* Property Annual Rate of Change	1.60%
* Inland Marine Livestock Annual Rate of Change	2.00%
* Inland Marine Machinery and Equipment Annual Rate of Change	0.90%

* Liability Annual Rate of Change	-1.00%
Homeowners Multiple Peril	
* Policy Form 2, 3, 3w/15: Annual Rate of Change	2%
* Policy Form 4 and 6: Annual Rate of Change	-0.3%
Commercial Multiple Peril (non-liability)	
* Buildings Annual Trend	2.0%
* Contents Annual Trend	-1.7%
* All Other Property Losses – Use fire	
* Extended Coverage Losses - Use fire	
Commercial Multiple Peril (liability)	
* OL&T Bodily Injury: Selected Annual Severity Trend	5.5%
* OL&T Property Damage: Selected Annual Severity Trend	4.0%
* Combined OL&T BI / PD Annual Severity Trend (Calculated using weights of 88% BI and 12% PD)	5.3%
* Products Bodily Injury: Selected Annual Severity Trend	7.0%
* Products Property Damage: Selected Annual Severity Trend	8.5%
* Combined Products BI / PD Annual Severity Trend (Calculated using weights of 51% BI and 49% PD)	7.7%
* Combined OL&T and Products BI / PD Annual Severity Trend (Calculated using weights of 96% BI and 4% PD)	5.4%
* Burglary & Theft:	-0.01%
Inland Marine	.09%
Medical Malpractice	
* Physicians, Surgeons and Dentists: Selected Annual Trend	5.5%
* Hospital and Health Related Facilities:	9.0%
Earthquake	
Other Liability	
* Frequency Trend	0%
Severity Trend:	
*M & C Bodily Injury:	4.5%
*M & C Property Damage:	7.0%
*M & C Fringe:	9.0%
*OL&T Bodily Injury:	3.0%
*OL&T Property Damage:	6.0%
* OL&T Fringe:	7.0%

*LP/CO Bodily Injury:	1.0%
*LP/CO Property Damage:	9.0%
*Products Bodily Injury:	3.0%
*Products Property Damage	5.5%
Private Passenger Auto Liability	0.52%
** Bodily Injury	-1.86%
** Property Damage	3.61%
Commercial Auto Liability	
* Frequency Trend	0%
* Comm. Cars, Private Passenger Types, & Garage Dealers Bodily Injury:	1.8%
* Comm. Cars, Private Passenger Types, & Garage Dealers Property Damage:	3.6%
* Garage Services Bodily Injury:	1.0%
* Garage Services Property Damages:	7.5%
Private Passenger Auto Physical Damage	6.38%
** Comprehensive	1.25%
** Collision	8.12%
Commercial Auto Physical Damage	
* Frequency Trend	0%
* Commercial Cars Other Than Collision: Selected Annual Severity Trend	4.5%
* Commercial Cars Collision: Selected Annual Severity Trend	4.5%
* Private Passenger Type Other Than Collision: Selected Annual Severity Trend	1.5%
* Private Passenger Collision: Selected Annual Severity Trend	3.0%
Aircraft (all perils)	
Fidelity	
* Annual Severity Trend	5.8%
Surety	
Burglary and Theft	6.3%
Boiler and Machinery	
Credit	

4) **2644.8 ALAE Trend**

This section requires that the Commissioner adopt ALAE trend factors for those lines of insurance subject to prior approval. The chart below contains the ALAE trend factors, by line of insurance.

The ALAE trend factors are from the latest approved ISO loss cost file for each line of insurance, with the exception of private passenger automobile, where Fast Track data was used. .

ALAE TREND	Factor
Fire	
* Personal Dwelling Fire and Extended Coverage:	4.7%
* Commercial Property:	
Building Annual Rate of Change	1.8%
Content Annual Rate of Change	4.6%
Time Element Annual Rate of Change	0.8%
Allied Lines	
Multiple Peril Crop	
Farmowners Multiple Peril	
* Property Annual Rate of Change	1.60%
* Inland Marine Livestock Annual Rate of Change	2.00%
* Inland Marine Machinery and Equipment Annual Rate of Change	0.90%
* Liability Annual Rate of Change	-1.00%
Homeowners Multiple Peril	
* Policy Form 2, 3, 3w/15: Annual Rate of Change	2%
* Policy Form 4 and 6: Annual Rate of Change	-0.3%
Commercial Multiple Peril (non-liability)	
* Buildings Annual Trend	2.0%
* Contents Annual Trend	-1.7%
* All Other Property Losses – Use fire	
* Extended Coverage Losses - Use fire	
Commercial Multiple Peril (liability)	
* OL&T Bodily Injury: Selected Annual Severity Trend	5.5%
* OL&T Property Damage: Selected Annual Severity Trend	4.0%
* Combined OL&T BI / PD Annual Severity Trend (Calculated using weights of 88% BI and 12% PD)	5.3%
* Products Bodily Injury: Selected Annual Severity Trend	7.0%
* Products Property Damage: Selected Annual Severity Trend	8.5%
* Combined Products BI / PD Annual	

Severity Trend (Calculated using weights of 51% BI and 49% PD)	7.7%
* Combined OL&T and Products BI / PD Annual Severity Trend (Calculated using weights of 96% BI and 4% PD)	5.4%
* Burglary & Theft:	-0.01%
Inland Marine	.09%
Medical Malpractice	
* Physicians, Surgeons and Dentists: Selected Annual Trend	5.5%
* Hospital and Health Related Facilities:	9.0%
Earthquake	
Other Liability	
* Frequency Trend	0%
Severity Trend:	
*M & C Bodily Injury:	4.5%
*M & C Property Damage:	7.0%
*M & C Fringe:	9.0%
*OL&T Bodily Injury:	3.0%
*OL&T Property Damage:	6.0%
* OL&T Fringe:	7.0%
*LP/CO Bodily Injury:	1.0%
*LP/CO Property Damage:	9.0%
*Products Bodily Injury:	3.0%
*Products Property Damage	5.5%
Private Passenger Auto Liability	0.52%
** Bodily Injury	-1.86%
** Property Damage	3.61%
Commercial Auto Liability	
* Frequency Trend	0%
* Comm. Cars, Private Passenger Types, & Garage Dealers Bodily Injury:	1.8%
* Comm. Cars, Private Passenger Types, & Garage Dealers Property Damage:	3.6%
* Garage Services Bodily Injury:	1.0%
* Garage Services Property Damages:	7.5%
Private Passenger Auto Physical Damage	6.38%
** Comprehensive	1.25%
** Collision	8.12%
Commercial Auto Physical Damage	
* Frequency Trend	0%
* Commercial Cars Other Than Collision: Selected Annual Severity Trend	4.5%

* Commercial Cars Collision: Selected Annual Severity Trend	4.5%
* Private Passenger Type Other Than Collision: Selected Annual Severity Trend	1.5%
* Private Passenger Collision: Selected Annual Severity Trend	3.0%
Aircraft (all perils)	
Fidelity	
* Annual Severity Trend	5.8%
Surety	
Burglary and Theft	6.3%
Boiler and Machinery	
Credit	

5) **2644.10(b) Executive Compensation**

Section 2644.10 provides that certain expenses shall be not allowed for ratemaking purposes. Subsection 2644.10(b) specifies that executive compensation that exceeds the reasonable amount for such compensation shall be excluded from expenses allowed for ratemaking purposes. This subsection also requires that the Commissioner determine what constitutes excessive executive compensation.

It is recommended that the prior approval regulations adopt the same approach as that used in C.C.R. section 2645.5(a) for determining excessive executive compensation (but with current, not 1989, data).

6) **2644.11 Expense Trend**

This section requires that the Commissioner set expense trend factors for those lines of insurance subject to prior approval. The chart below contains the expense trend factors by line of insurance.

The expense trend factor was obtained from the Bureau of Labor Statistics, U.S. Department of Labor. The factor represents the 12 month total compensation change for the insurance industry.

EXPENSE TREND	Factor
Fire	4%
Allied Lines	4%
Multiple Peril Crop	4%
Farmowners Multiple Peril	4%
Homeowners Multiple Peril	4%
Commercial Multiple Peril (non-liability)	4%

Commercial Multiple Peril (liability)	4%
Inland Marine	4%
Financial Guaranty	4%
Medical Malpractice	4%
Earthquake	4%
Other Liability	4%
Private Passenger Auto Liability	4%
Commercial Auto Liability	4%
Private Passenger Auto Physical Damage	4%
Commercial Auto Physical Damage	4%
Aircraft (all perils)	4%
Fidelity	4%
Surety	4%
Burglary and Theft	4%
Boiler and Machinery	4%
Credit	4%

7) **2644.12 Efficiency Standard (factor)**

This section requires that the Commissioner adopt efficiency standard values for those lines of insurance subject to prior approval. The chart below contains the efficiency standard values, by line of insurance.

The procedure used to calculate these values is the weighted average of companies in each marketing system, using reported premium and expense data. The data was derived from the NAIC database for premium data from state, annual statement expense data from the Insurance Expense Exhibit (IEE).

2000 EFFICIENCY STANDARD (%)	CAPTIVE AGENT	DIRECT WRITER	INDEPENDENT AGENCY
Fire	34.95	25.34	29.47
Allied Lines ¹	39.21	36.62	40.98
Multiple Peril Crop ²	15.12	15.12	15.12
Farmowners Multiple Peril	44.77	38.25	28.99
Homeowners Multiple Peril	36.70	34.72	36.04
Commercial Multiple Peril (non-liability)	41.86	35.63	37.03
Commercial Multiple Peril (liability)	32.11	34.30	38.03
<i>*Com'l Multi-Peril (liability & non-liability)</i>	38.42	35.02	37.51
Inland Marine	36.42	25.55	35.25
Financial Guaranty ³	32.04	32.04	32.04
Medical Malpractice	26.64	26.58	28.80

Earthquake	34.75	27.16	23.95
Other Liability	35.55	32.90	30.90
Private Passenger Auto Liability	35.26	30.48	32.29
Commercial Auto Liability	37.67	32.90	34.34
Private Passenger Auto Physical Damage	34.57	33.83	34.15
Commercial Auto Physical Damage	36.69	34.79	37.42
Aircraft (all perils)	29.69	30.66	28.63
Fidelity	33.40	39.77	40.17
Surety ⁴	49.66	42.16	49.02
Burglary and Theft ⁵	36.99	26.92	38.20
Boiler and Machinery ⁶	33.55	33.12	39.02
Credit	44.73	49.72	37.59

Note:

1. Allied Lines: use Captive/Direct/Independent (C/D/I) weighted average of 36.62% for Direct Writer.
2. Multiple Peril Crop: use Captive standard of 15.12% for Direct Writer and Independent.
3. Financial Guaranty: use Direct Writer standard of 32.04% for Captive and Independent.
4. Surety: use C/D/I weighted average of 49.66% for Captive.
5. Burglary & Theft: use C/D/I weighted average of 36.99% for Captive.
6. Boiler and Machinery: use C/D/I weighted average of 33.12% for Direct Writer

8) **2644.16 Rate of Return**

This section requires that the Commissioner set the maximum and minimum permitted after-tax rate of return.

Insurer solvency, and hence, adequacy of rates, is of paramount concern to the Commissioner. The Commissioner believes that appropriate weight and consideration should be given actual historical data. For the fifteen-year period from 1985 through 2000, the annual property/casualty return on equity has ranged from 4.0% -- 17.3%. For the ten year period from 1990 through 2000, the annual property/casualty return on equity has ranged from 4.5% -- 11.6%. With this in mind, the Commissioner requests comment and supporting justification for the maximum and minimum permitted rate of return. In the past, the Commissioner has allowed a maximum rate of return for ratemaking purposes of up to 15%. The Commissioner does not intend to set a maximum above that amount in this proceeding, and therefore requests that public comment not advocate a process or model which would result in a maximum rate of return higher than 15%.

9) **2644.17 Leverage Factors**

This section requires that the Commissioner set leverage factors for those lines of insurance subject to prior approval. The chart below contains the leverage factors, by line of insurance.

The data was derived from A.M. Best's Aggregate and Averages. For the homeowners and earthquake lines, the factors are consistent with prior decisions of the Commissioner.

LEVERAGE FACTOR	Factor
Fire	3.50 : 1
Allied Lines	3.50 : 1
Multiple Peril Crop	
Farmowners Multiple Peril	2.50 : 1
Homeowners Multiple Peril	2.00 : 1
Commercial Multiple Peril (non-liability)	
Commercial Multiple Peril (liability)	
* Commercial Multi-Peril (combined)	1.75 : 1
Inland Marine	3.50 : 1
Medical Malpractice	1.00 : 1
Earthquake	1.00 : 1
Other Liability	1.00 : 1
Private Passenger Auto Liability	2.00 : 1
Commercial Auto Liability	2.00 : 1
Private Passenger Auto Physical Damage	5.50 : 1
Commercial Auto Physical Damage	5.50 : 1
Aircraft (all perils)	1.00 : 1
Fidelity	2.00 : 1
Surety	2.00 : 1
<i>Glass (no longer an Annual Statement Line)</i>	5.50 : 1
Burglary and Theft	4.00 : 1
Boiler and Machinery	2.50 : 1
Credit	

10) **2644.23 Credibility Adjustment**

This section requires that the Commissioner promulgate a credibility adjustment for those lines of insurance subject to prior approval. The chart below contains the credibility standards, by line of insurance.

The credibility factors are from the latest approved ISO loss cost filings for each line of insurance.

Line of Insurance	Full Credibility Standard	Partial Credibility Formula
Personal Fire Fire Extended Coverages	K = 500,000 house years K = 330,000 house years	$(\text{earned house years} / K)^{0.5}$
Commercial Fire	K = 18,206	$(\# \text{ of claims in experience period} /$

Basic Group I		$K)^{0.5}$
Basic Group II	K = 30,000	$(\# \text{ of claims in experience period} / K)^{0.5}$
Special Causes of Loss	K = 25,000	$(\# \text{ of claims in experience period} / K)^{0.5}$
Allied Lines	See fire	
Multiple Peril Crop		
Farmowners Multiple Peril Property -- Dwellings and HPP -- Outbuildings -- Farm Personal Property Inland Marine	K = 439,116 K = 231,021 K = 1,023,294 K = 373,895 K = 250,000 Earned risks	$(\text{Statewide earned risks} / K)^{0.5}$
Farmowners Multiple Peril Liability	K = 2,500 Claims	$(\# \text{ of claims in experience period} / K)^{0.5}$
Homeowners Multiple Peril -- Forms 2, 3, 3 w/ 15 -- Form 4 -- Form 6	K = 240,000 K = 285,000 K = 190,000	$(\# \text{ of earned house years in experience period} / K)^{0.5}$
Commercial Multiple Peril (non-liability)	K = 9,231	$(\# \text{ of claims in experience period} / K)^{0.5}$
Commercial Multiple Peril (liability)	K = 9,231	$(\# \text{ of claims in experience period} / K)^{0.5}$
Inland Marine	K = 6,187	$Z = (\# \text{ of claims in experience period} / K)^{0.5}$
Medical Malpractice Hospitals Physicians, Surgeons & Dentists	K = 900 K = 700	$Z = (\# \text{ of claims in experience period} / K)^{0.5}$
Earthquake		
Other Liability -- Manufacturers and Contractors -- Owners, Landlords & Tenants -- Products / Completed Operations	K = 8,000 claims K = 6,000 claims K = 7,000 claims	$Z = (\# \text{ of claims in experience period} / K)^{0.5}$
Private Passenger Auto Liability	K = 4,000 claims	$Z = (\# \text{ of claims in experience period} / K)^{0.5}$
Commercial Auto Liability Commercial Cars Private Passenger Types Garages	K = 14,326 Claims K = 6,512 Claims K = 3,743	$(\# \text{ of claims in experience period} / K)^{0.5}$
Private Passenger Auto Physical Damage	K = 4,000 claims	$(\# \text{ of claims in experience period} / K)^{0.5}$
Commercial Auto Physical Damage OTC Commercial Cars	K = 10,414	$(\# \text{ of claims in experience period} / K)^{0.5}$

Private Passenger Types Collision	K= 9,615	
Commercial Cars	K = 4,025	
Private Passenger Types	K = 3,202	
Aircraft (all perils)		
Fidelity	K= 348	Z= (# of claims in experience period/ K)^0.5
Surety		
Burglary and Theft	K= 300	Z= # of claims in experience period / (# of claims in experience period + K)
Boiler and Machinery	K = 10,000	(# of claims in experience period/ K)^0.5
Credit		

HARRY LOW
Insurance Commissioner

By _____/s/_____
Donald P. Hilla
Senior Staff Counsel