

Watching Your Barometer— Getting the Most from Your Data



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Key Characteristics of a Risk Retention Group

- Intense focus on a particular group or class
- Recognition of changes in exposure
- Intimate understanding of the risk drivers
- Contact with clients
 - Size enables quick response to change in risk
 - Data base is very specific with identifiers not often collected on an industry basis

Thinking in Terms of Frequency and Severity

- Most underwriters think frequency
 - It is what they see the most
 - It is more concrete. Can be counted
 - Insureds and Agents respond to frequency
- Severity is often partially ignored
 - Disregarded as a “shock loss”
 - It belongs to the reinsurer
 - What do you do with one or two claims
- Thinking in terms of frequency and severity
 - Enables us to begin to visualize loss curves
 - Keeps pricing more accurate
 - Begins to correlate our thinking to real risk

Frequency and Severity

Higher frequency, lower severity risks:

- Show up as a higher loss ratio renewal
- Are viewed often as marginal accounts
- Get more underwriting attention due to claims
- More likely to have a “bad” year

Frequency and Severity

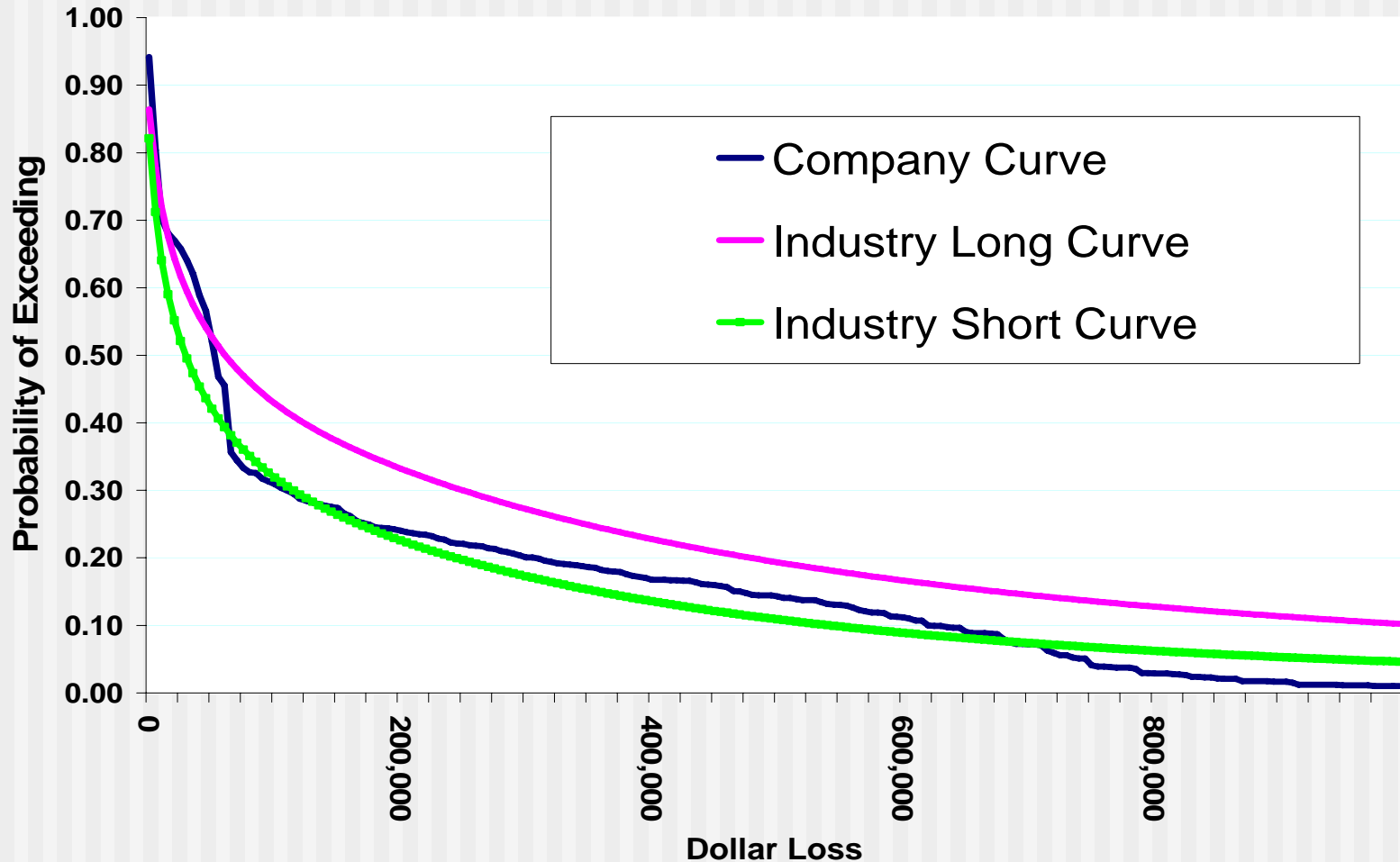
Lower frequency, higher severity risks:

- Almost always have lower renewal loss ratios, or a very high loss ratio that gets “discounted” as a shock loss
- Often get better experience credits in the underwriting process
- Are usually the driver of reinsurance cost
- Difficult to credit for deductibles

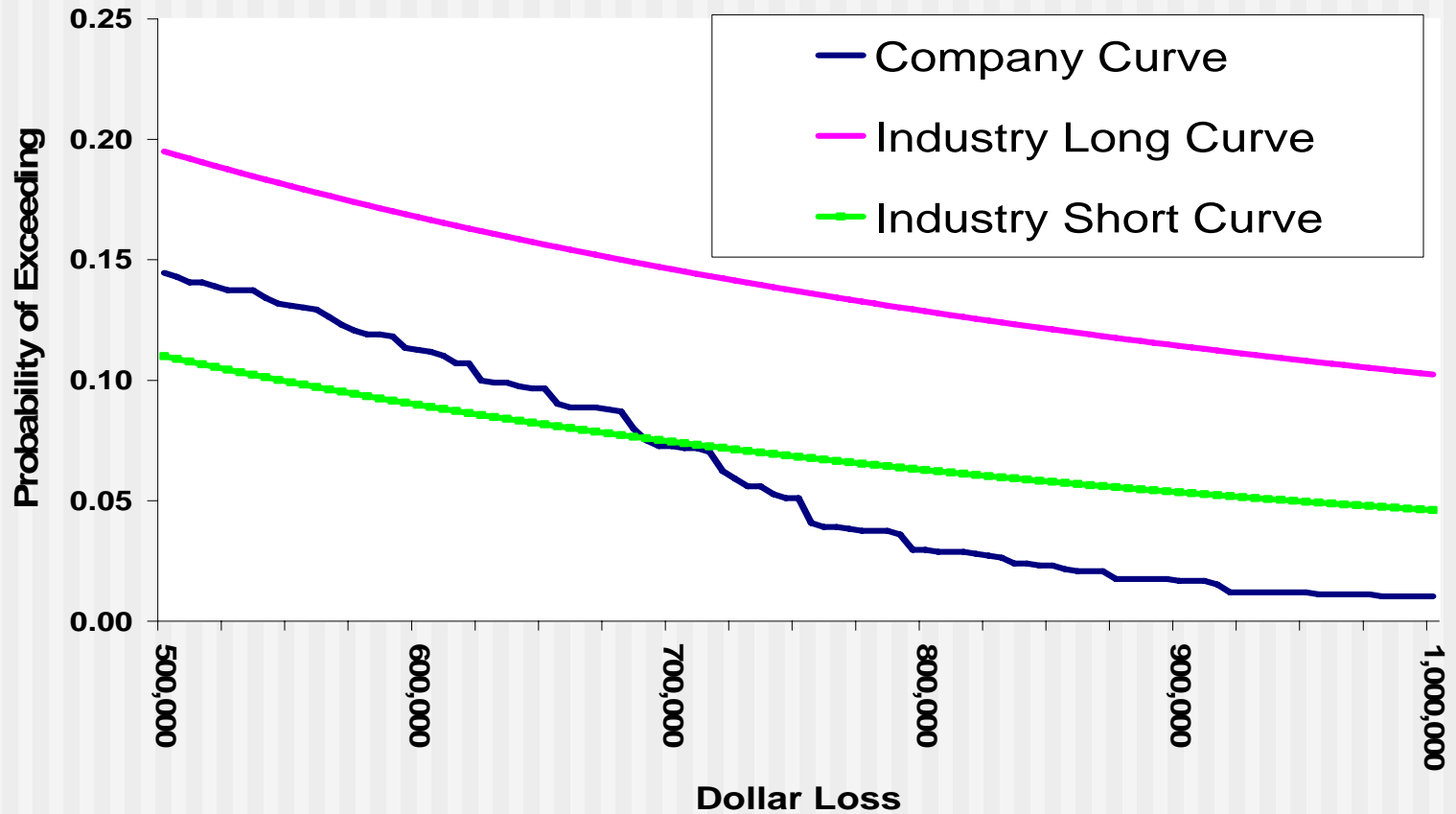
Rate and Reserve Reviews

- Are inexpensive and really great reading
- Reviews without insight are only “crunched numbers”
- Reviews that never get taken off the shelf are only useful as very expensive paperweights
- Often fall back on industry data due to “credibility” issues
- Should be one of the best guides to your underwriting

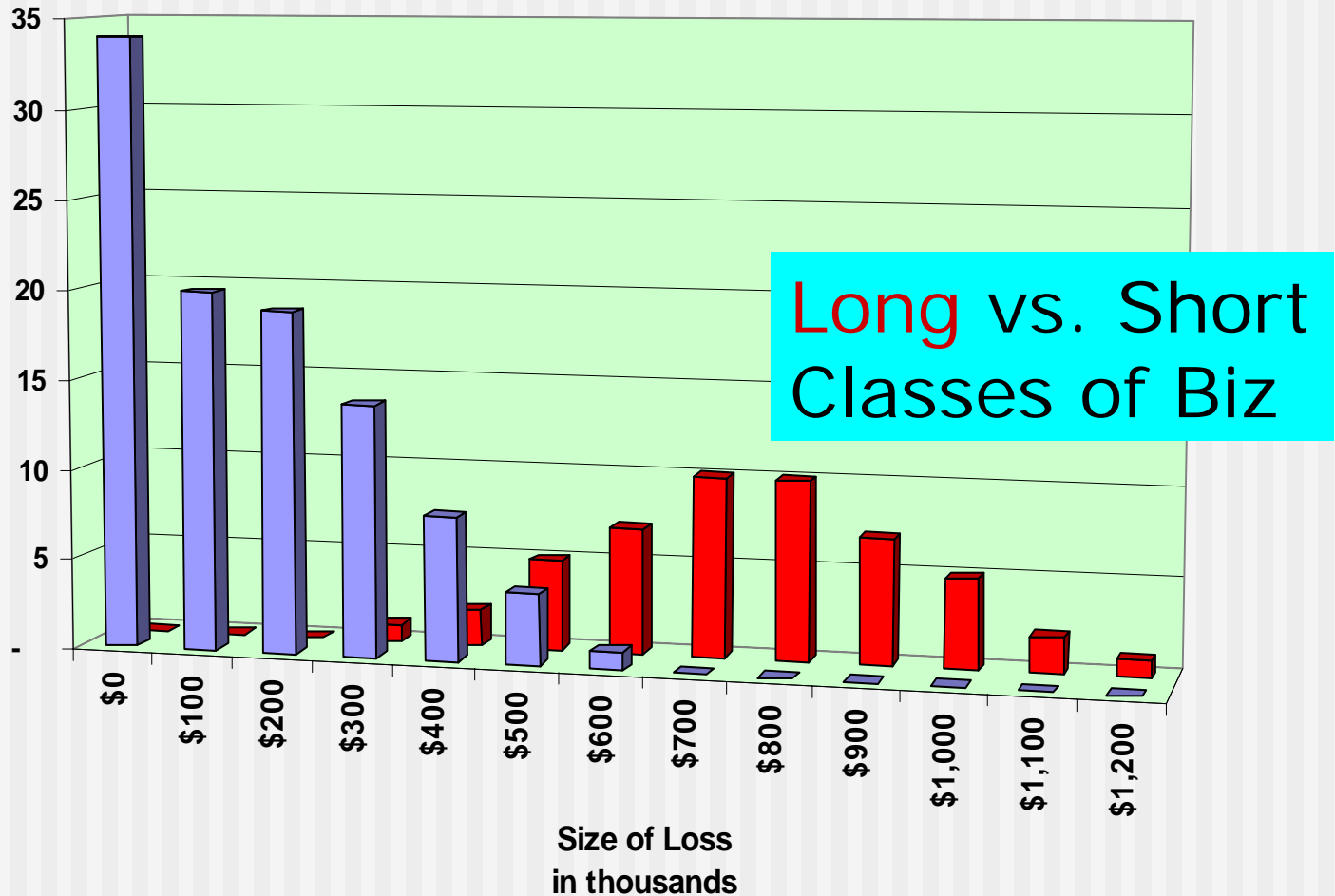
Severity Curves: Ground-up



Severity Curves: Excess



Comparison of Frequency & Severity Characteristics



A Change in Thinking – ABC Mutual pre-2004

- Un-mined claims database
- Looked at 5-year loss run as primary evaluative tool for underwriting risk
- Rewarded existing members with lowest rates – highest rates to new prospects
- Never changed our base rates, deductible credits or underwriting adjustment factors
- Applied adjustment factors somewhat arbitrarily

A Change in Thinking – ABC Mutual post-2004

- Analysis of claims data produced interesting results:
 - New understanding and appreciation of low frequency/high severity nature of business
 - Vindicated our thinking about rate relativity

A Change in Thinking – ABC Mutual post-2004

- Prospects are not necessarily more risky than existing members
 - In fact, they are usually less risky given our existing members' large quantity of historical exposures
 - We unfairly penalized new risks resulting in stagnant growth
 - Desiring slow, measured growth is not a bad thing – just understand the reasoning behind it

A Change in Thinking – ABC Mutual post-2004

- Pared down our underwriting factors to those that really mattered
 - Quality Control Score
 - Owner Factor
 - Business Mix
 - Tail Exposure
 - Loss Ratio
 - Market Driven (Business Decision)

A Change in Thinking – ABC Mutual post-2004

- Revised our deductible credit schedule to better match historical claims data
 - We had been giving too much credit for lower deductibles and not enough credit for high deductibles

Deductible Credit Analysis

Claim	Total Paid	Deductibles								
		\$ 1,000	\$ 2,500	\$ 5,000	\$ 10,000	\$ 25,000	\$ 50,000	\$ 100,000	\$ 150,000	
A	\$ 1,250	\$ 250	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
B	\$ 1,500	\$ 500	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
C	\$ 3,500	\$ 2,500	\$ 1,000	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
D	\$ 3,600	\$ 2,600	\$ 1,100	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
E	\$ 4,200	\$ 3,200	\$ 1,700	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
F	\$ 4,600	\$ 3,600	\$ 2,100	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
G	\$ 5,500	\$ 4,500	\$ 3,000	\$ 500	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
H	\$ 9,500	\$ 8,500	\$ 7,000	\$ 4,500	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
I	\$ 11,000	\$ 10,000	\$ 8,500	\$ 6,000	\$ 1,000	\$ -	\$ -	\$ -	\$ -	\$ -
J	\$ 15,000	\$ 14,000	\$ 12,500	\$ 10,000	\$ 5,000	\$ -	\$ -	\$ -	\$ -	\$ -
K	\$ 18,000	\$ 17,000	\$ 15,500	\$ 13,000	\$ 8,000	\$ -	\$ -	\$ -	\$ -	\$ -
L	\$ 26,000	\$ 25,000	\$ 23,500	\$ 21,000	\$ 16,000	\$ 1,000	\$ -	\$ -	\$ -	\$ -
M	\$ 54,000	\$ 53,000	\$ 51,500	\$ 49,000	\$ 44,000	\$ 29,000	\$ 4,000	\$ -	\$ -	\$ -
N	\$ 110,000	\$ 109,000	\$ 107,500	\$ 105,000	\$ 100,000	\$ 85,000	\$ 60,000	\$ 10,000	\$ -	\$ -
O	\$ 450,000	\$ 449,000	\$ 447,500	\$ 445,000	\$ 440,000	\$ 425,000	\$ 400,000	\$ 350,000	\$ 300,000	\$ -
Total	\$ 717,650	\$ 702,650	\$ 682,400	\$ 654,000	\$ 614,000	\$ 540,000	\$ 464,000	\$ 360,000	\$ 300,000	\$ -
Deductible Credit		0.98	0.95	0.91	0.86	0.75	0.65	0.50	0.42	

Steps to be Taken - Summary

1. Match qualitative thoughts to quantitative data
2. Consider true exposure base
3. Review deductible credits
4. Review reinsurance cost allocation
5. Review underwriting process vis-à-vis claims data
6. Reformat underwriting documentation
7. Perform ongoing audit of the accuracy of claims data

Steps to be Taken

Review your database from a claims and underwriting perspective

1. At least once a year, set aside a day for matching your qualitative thoughts to the quantitative numbers.
2. Consider your true exposure base, be it:
 - Vehicles or miles driven
 - Units manufactured or sales
 - Relationship of units to sales drives the underwriting credits and dividend policy

Steps to be Taken

3. Review your deductible credits and how they match your data and risks, not just the industry.
4. Review your allocation of reinsurance cost, making sure they correspond to severity potential rather than premium.

Steps to be Taken

5. Consider each underwriting process and how it reacts to the claims data
 - Do you overly credit loss-free/higher severity risks?
 - Are loss ratio renewal standards set to reflect frequency and severity?

Steps to be Taken

6. Reformat underwriting documentation
 - Must match thought process
 - Let thought process guide the underwriting not vice versa
7. Perform ongoing audit of the accuracy of claims data
 - Data is only as good as its accuracy – Garbage in, garbage out
 - Knowing how you will ultimately use data should drive what information is collected and entered

Q & A



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