

The True Mover

Workers' compensation in the U.S. is becoming an underwriters' nightmare and perhaps the trigger for the oft-predicted hard market.

By DAN REYNOLDS, senior editor of Risk & Insurance®



Oft has it been speculated, mused upon and pontificated: What will turn the soft market? What catastrophic event, what superquake, or murderous Caribbean storm, will do it?

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What if it is the quiet but merciless degradation in [workers' compensation](#) losses and corresponding reserve inadequacies?

Figures released last week indicate that this is indeed where the new hard market could begin.

Researchers with [A.M. Best & Co.](#) think that the combined ratio for workers' comp among the 40 or so companies in its workers' comp composite will strike 116 when full-year figures for 2010 are available. That's a big underwriting loss in anybody's book. And things stand to look much worse in 2011.

"Our expectations are that things will erode, things will get worse before they get better," said Michelle Baurkot, an assistant vice president for A.M. Best based in Oldwick, N.J.

The ongoing march of medical costs is one big driver, with pharmaceutical costs a big part of that. Another factor is that prior-year reserve releases to buck up many financial reports have left carriers thin in facing the vagaries of the largest stand-alone commercial line in the property/casualty world.

High unemployment rates in the United States have lowered workers' comp exposures, to be sure. But there was still \$32.6 billion in net written premium in 2009. In 2008, before the credit crunch had yet to wreak its full effects, net written premium in workers' compensation was \$39.4 billion, according to Baurkot. At its peak in 2005, the market saw \$48.6 billion in net written premium.

So how much worse will it get? Could that 116 combined ratio crest at 120 and head toward 130? It will go higher in 2011, A.M. Best researchers believe, and possibly again in 2012.

"That is the big uncertainty for 2012, is how quickly companies will start to recognize if they are deficient in their reservings, which could potentially drive the combined ratio even higher," Baurkot said.

[Chartis Inc.](#) is one company that is getting away from workers' compensation with all due haste, according to published comments from its president and CEO, Kristian Moor. The company has exited \$2 billion in business in workers' comp in the past couple of years, Moor said.

Chartis' parent company, AIG, had \$3.55 billion in direct written premiums in the line in 2009, according to researchers with A.M. Best., down from \$6.7 billion in 2006. The company will continue that trend in 2011 due to unfavorable pricing, according to Moor.

No one expects the economy to turn around quickly, which means premium volume will remain relatively low. Medical costs continue to rise, however, which means carriers will continue to pay out even more for workers receiving compensation.

"This is the line that is most impacted by the economy," Baurkot said.

As insurers released reserves that covered prior-year underwriting adventures, something has to give in this largest of the property/casualty sector. Must it not be price?

"You would hope," Baurkot said.

In California, companies are starting to ask for sizable rate increases, she added.

"But in other states, you are still seeing more erosion," Baurkot said.

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