R.C. 2325

To: The Members of the Board

RE: Carrier Test Audit Performance Program
    Administrative Procedures Update
    Audit Year Commencing October 1, 2013

The Underwriting Committee of the New York Compensation Insurance Rating Board has authorized a change to the procedures under the Board’s Carrier Test Audit Performance Program.

The program, as currently constituted, reviews carrier, or carrier group, audit performance on a quarterly basis in order to ascertain if carriers are meeting the minimum error standard of twenty-five percent (25%) on their physical audits. Should a carrier, or carrier group, have error ratios in excess of twenty-five percent (25%), for four consecutive calendar quarters, they must meet with the Audit Staff of the Field Services Department in order to address the issues and submit a written plan of action to correct any deficiencies in their performance. The current procedures are attached as Exhibit I.

The newly revised procedures are outlined in Exhibit II, also attached. These new procedures will maintain many aspects of the current program (quota, policy selection, carrier notification, etc.). However, the primary difference, under the new procedure, is in the method of fining carriers having deficient audit results. While the prior procedures mandated a quarterly review, on a revolving basis, the new procedure will be based upon an annual review of audit results. Carriers will be fined based not only on their error ratios but also on the number of audits found in error. This approach is further explained and illustrated by a sliding scale chart as shown on Exhibit II.

The revised audit procedures will be effective beginning with the Board’s next “Audit Year” commencing on October 1, 2013. Any actions will, therefore, not be applicable until the end of the Board’s “Audit Year” which is September 30, 2014. This lead time will allow all carriers ample time to assess any deficiencies in order to institute whatever corrective measures are necessary to avoid the issuance of fines.
In addition to the Exhibits noted above, the new procedures will be available on the Rating Board’s website at: www.nycirb.org, via the ‘NY Programs’ tab, and by choosing the ‘Test Audit Performance’ selection.

Very truly yours,

Monte Almer

President

WVT:tg
Encl.
How the Test Audit Program Works

Each carrier or carrier group has a predetermined quota for policies to be audited which is established on a yearly basis. This quota is based upon a formula that encompasses the total number of policies written and the amount of premium written by the carrier in New York State. The quota is adjusted based upon a review of the carrier's last four years of audit results. The quota will increase if the carrier's results are worse than the industry as a whole or decrease if the results are better than the industry. The selection of policies includes Physical Audits, Policyholder Statements, Estimates, Telephone Audits and Electronic Data Interface Audits. It also includes all industry groups, such as Manufacturing, Contracting and Stores, etc. Policies written on a Per Capita or any other basis of premium other than payroll are excluded from the program. The total payroll for the policies selected is generally not more than $1,000,000 or less than $50,000. Carriers will be notified on a monthly basis of the policies selected and are required to respond to the request within thirty (30) days.

Audit Differences

Any audit producing a premium difference of more than $500 is considered rebillable. An audit that produces a premium difference of $500 or less will be considered rebillable if 5% of the carrier premium is less than the premium difference determined by the audit. It is non-rebillable if 5% of the carrier premium is more than the premium determined by the audit. For all rebillable audits the carrier has thirty (30) days to respond either by submitting a revised premium billing or by submitting a letter explaining the reason the carrier does not agree with the Rating Board audit results. Failure to respond will result in the carrier being assessed fines for non-compliance. A revised unit statistical report must also be submitted to the Rating Board along with any revised premium billing.

Carriers must refund premium when an audit determines that an insured is entitled to a return premium due to a carrier overcharge. However, carriers cannot collect additional premium when an audit determines that the carrier undercharged an insured. In either instance a revised premium billing is required.

Compliance With The Carrier Test Audit Performance Program

Carrier performance will be reviewed on a quarterly basis and will be based upon four (4) consecutive quarters of results. Any carrier that exceeds the minimum standard audit ratio of 25% for four consecutive quarters will be subject to the provisions of the program. Any carrier that achieves a performance standard of less than 15% for four consecutive quarters will be exempt from the Program for eight consecutive quarters.

Administration Of The Program

The Rating Board will administer the program. An Audit Review Committee, established by the Governing Committee and consisting of three (3) member carriers, is empowered to discuss a carrier's audit results, the carrier's audit program and any remedial actions necessary to improve the carrier's performance.

The Rating Board will:

1. Notify carriers, on a monthly basis, which policies are subject to audit.
2. Report individual audit results, quarterly reports and annual reports to the carrier.

If the test audit performance of a carrier has exceeded the minimum standard for four (4) consecutive quarters the following steps are followed:

The carrier is required to meet with the Manager of Field Services and the Vice President of Underwriting and Field Services to discuss the carriers audit proficiency. At this meeting the carrier is to provide a detailed explanation of any remedial measures it has or proposes to implement in the future to improve its audit proficiency.

Any carrier who meets with the Board will be advised that continued failure to meet the minimum standard for audit proficiency will have additional policies selected for audit, beyond their established quota, at a cost of $1,000 each. Following the meeting with the Board the carrier's performance will be measured again after three quarters. If the carrier has failed to achieve the minimum standard an officer of the carrier will be required to meet with the Audit Review Committee to present the carrier's plan to achieve audit proficiency. The Committee will establish the number of additional audits to be performed in the next two quarters and inform the carrier that $1,000 per audit will be charged to offset the cost of performing the additional audits. Any carrier that fails to meet the minimum standards after the additional audits are performed will be reported to the Governing Committee for further action. An officer of the carrier will then have to meet with the Governing Committee to explain its plan to improve proficiency. The Governing Committee may then impose additional fines or report the carrier to the Insurance Department. The Rating Board President will inform the carrier of any action taken by the Governing Committee.
**Excluded from the Calculation of the Error Ratio**

- Special audits performed by the Rating Board that fall outside the parameters of the Test Audit Program.
- Carrier final premium billings that were based on policyholder statements.
- Carrier final premium billings that were based upon estimates in situations such as if the insured was uncooperative in complying with carrier requests for a payroll statement or refused the carrier access to conduct a physical audit. In these cases, the carrier is required to provide documentation to the Rating Board to show that the carrier made a reasonable effort to obtain an audit.

**Note:** Carrier final premium billings based upon policyholder statements or estimates will be excluded from the error ratio calculation if the audit difference between the Rating Board audit and the carrier final premium billing is based solely upon differences in remuneration or the assignment of a classification to an individual employee.

Premium differences based upon other factors such as the incorrect classification of the business, experience modifications, deviations, New York State Assessment, etc., will be considered errors.

These situations will be reviewed by the Rating Board on a case-by-case basis.
How the Test Audit Program Works

Each carrier or carrier group has a predetermined quota for policies to be audited which is established on a yearly basis. This quota is based upon a formula that encompasses the total number of policies written and the amount of premium written by the carrier in New York State. The quota is adjusted based upon a review of the carrier's last four years of audit results. The quota will increase if the carrier's results are worse than the industry as a whole or decrease if the results are better than the industry. The selection of policies includes Physical Audits, Policyholder Statements, Estimates, Telephone Audits and Electronic Data Interface Audits. It also includes all industry groups, such as Manufacturing, Contracting and Stores, etc. Policies written on a Per Capita or any other basis of premium other than payroll are excluded from the program. The total payroll for the policies selected is generally not more than $1,000,000 or less than $50,000. Carriers will be notified on a monthly basis of the policies selected and are required to respond to the request within thirty (30) days.

Audit Differences

Any audit producing a premium difference of more than $500 is considered rebillable. An audit that produces a premium difference of $500 or less will be considered rebillable if 5% of the carrier premium is less than the premium difference determined by the audit. It is non-rebillable if 5% of the carrier premium is more than the premium determined by the audit. For all rebillable audits the carrier has thirty (30) days to respond either by submitting a revised premium billing or by submitting a letter explaining the reason the carrier does not agree with the Rating Board audit results. Failure to respond will result in the carrier being assessed fines for non-compliance. A revised unit statistical report must also be submitted to the Rating Board along with any revised premium billing.

Carriers must refund premium when an audit determines that an insured is entitled to a return premium due to a carrier overcharge. However, carriers cannot collect additional premium when an audit determines that the carrier undercharged an insured. In either instance a revised premium billing is required.

Compliance with the Carrier Test Audit Performance Program

Fining: The fining process will be based upon an annual review of carrier performance. With this approach, carriers whose annual error ratios for physical audits, that are greater than the standard error ratio of 25% would be fined. The annual period is for each completed Audit year (October 1st through September 30th) of the following year. This carrier evaluation approach would make allowance for small (25 closed audits or less), medium (from 26 to 99 closed audits) and large carriers (100 or more closed audits).

The following further specifies this method:

For carriers or carrier groups with 100 audits or more (large carrier) the fines would be as follows:

- An error ratio of 25% or less is deemed as meeting requirements
- An error ratio between 26% and 40% will require a fine of $10,000
- An error ratio between 41% and 50% will require a fine of $25,000
- An error ratio of 51% or more will require a fine of $50,000

For carriers or carrier groups from 26 to 99 audits (medium carrier) the fines would be as follows:

- An error ratio of 25% or less is deemed as meeting requirements
- An error ratio between 26% and 40% will require a fine of $5,000
- An error ratio between 41% and 50% will require a fine of $12,500
- An error ratio of 51% or more will require a fine of $25,000

For carriers or carrier groups with 25 audits or less the fines (small carrier) would be as follows:

- An error ratio of 25% or less is deemed as meeting requirements
- An error ratio between 26% and 40% will require a fine of $2,500
- An error ratio between 41% and 50% will require a fine of $6,250
- An error ratio of 51% or more will require a fine of $12,500

For all carrier categories, if the error ratio exceeds 25%, there also will be a fine of $100 for every audit that produces a premium difference greater than 25% of the carrier premium.

Administration of the Program

The Board will:

1. Notify carriers, on a monthly basis, which policies are subject to audit.
2. Report individual audit results, quarterly reports and annual reports to the carrier.
Excluded from the Calculation of the Error Ratio

- Special audits performed by the Rating Board that fall outside the parameters of the Test Audit Program.
- Carrier final premium billings that were based on policyholder statements.
- Carrier final premium billings that were based upon estimates in situations such as if the insured was uncooperative in complying with carrier requests for a payroll statement or refused the carrier access to conduct a physical audit. In these cases, the carrier is required to provide documentation to the Rating Board to show that the carrier made a reasonable effort to obtain an audit.

Note: Carrier final premium billings based upon policyholder statements or estimates will be excluded from the error ratio calculation if the audit difference between the Rating Board audit and the carrier final premium billing is based solely upon differences in remuneration or the assignment of a classification to an individual employee. Premium differences based upon other factors such as the incorrect classification of the business, experience modifications, deviations, New York State Assessment, etc., will be considered errors. These situations will be reviewed by the Rating Board on a case-by-case basis.