BEFORE THE NEW MEXICO SUPERINTENDENT OF INSURANCE
AS CUSTODIAN OF THE PATIENT COMPENSATION FUND

IN THE MATTER OF DETERMINING	**)**	
NEW PATIENT COMPENSATION FUND	**)**	
SURCHARGE RATES	**)**	**Docket No. 19-00004-PCF**
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RECOMMENDED DECISION

THIS MATTER comes before the Superintendent of the New Mexico Office of Superintendent of Insurance ("Superintendent" or "OSI") on the September 16, 2019 Order Scheduling Hearing to Determine New Patient Compensation Fund Surcharge Rates ("September 16 Order") and the September 30, 2019 Order Appointing Hearing Officer and Setting Initial Case Schedule ("September 30 Order") issued pursuant to NMSA 1978, Sections 41-5-1 to 41-5-29 (1976, as amended through 2015), the Medical Malpractice Act ("MMA"). The September 16 Order opened this docket for consideration of new patient compensation fund rates pursuant to NMSA 1978, Section 41-5-25 and appointed the undersigned as Hearing Officer.

On October 10, 2019, the Hearing Officer issued an order setting October 17, 2019 as the deadline for filing motions to intervene in this matter. No motions to intervene were filed.

On October 15, 2019, Notice of Public Hearing was published in the New Mexico Register and the *Albuquerque Journal*. The notice provided instruction for interested parties to participate in this matter by filing written comments and to attend the public hearing. OSI received the following written public comment: October 16, 2019 email from D J Letherer; and November 4, 2019 comments of the New Mexico Hospital Association submitted by Jeff Dye.

Mr. Letherer's written comment emphasized that a significant increase in the patient compensation fund surcharge rates could discourage health providers from participating in the fund and increase medical liability insurance premiums in the state. He urged the Superintendent to be moderate in any surcharge increase made as a result of this proceeding.

Appearing at the November 18, 2019 hearing on behalf of OSI was Todd S. Baran, Associate General Counsel. OSI presented two witnesses: Sandra Romero, manager of the Patient Compensation Fund for OSI; and Robert J. Walling III of Pinnacle Actuarial Resources, Inc. Bruce Whitmore and Richard Frese provided public comment on behalf of the New Mexico Hospital

Association and the New Mexico Hospital Risk Purchasing Group. OSI introduced Exhibits A through E that were admitted into the record.

At the hearing, Messrs. Whitmore and Frese made the following requests: 1) a phase in over two years of any surcharge rate increase; 2) application in the rate formula of an experience modification for hospitals as is currently done for physicians; and 3) clarification of how losses will be allocated between hospitals and physician providers.

The Patient Compensation Fund Surcharge

The MMA limits liability for health care providers qualifying under the terms of the Act, which, *inter alia*, includes required payment of an annual surcharge assessed by the Superintendent to fund the Patient Compensation Fund ("PCF"), a fund created by NMSA 1978, Section 41-5-25 and administered by the OSI. Subsection B states, in part: "The surcharge shall be determined by the superintendent based on sound actuarial principles, using data obtained from New Mexico if available." Subsection H of Section 41-5-25 states: "The superintendent shall contract for an independent actuarial study of the [PCF] to be performed not less than once every two years." The actuarial study is used to assist in the determination of the surcharge rates.

Chapter 21 of the NMAC governs the administration of the PCF including determinations of surcharges "… necessary and appropriate to ensure that [the PCF] is and remains financially and actuarially sound." 13.21.2.18 NMAC. In so doing, the Superintendent is to determine surcharges for health care providers, other than hospitals or outpatient care facilities, based on classifications and categories of medical malpractice liability risks with respect to the practice type or specialties as determined and specified in an actuarial study. For hospitals and outpatient care facilities the Superintendent is to determine surcharges considering the process or directions specified in an actuarial study. 13.21.2.19 NMAC. Surcharge rate proceedings are governed by 13.21.4 NMAC.

Based on the evidence presented at the November 18, 2019 hearing, the Hearing Officer makes the following:

FINDINGS OF FACT

1. The PCF is funded by annual premium surcharges collected from every qualified healthcare provider ("QHP") pursuant to NMSA 1978, Sections 41-5-5 and 41-5-25.

2. Three classes of QHPs currently fund the PCF: a) individual QHPs; b) legal entities such as corporations, partnerships or limited liability companies that are comprised of one or more

QHPs ("QHP Entity" or "QHP Entities"); and hospitals and outpatient health care facilities ("QHP Hospitals"). TR 8; 89; 116

3. The risks and funding requirements relating to a QHP Entity are included with those relating to individual QHPs that make up the entity. TR 62-63

4. The PCF surcharge payable by an individual QHP is determined through a formula. The foundation of the formula is the base surcharge that applies to the rate classification for the provider practice specialty. TR 6-8. Each specialty is assigned to a rate classification. TR 17. The rate classifications are based on the risk exposure presented by each practice specialty relative to every other practice specialty. TR 17-18. The annual base surcharge will increase from 25 to 75 percent depending on the number of past malpractice claims paid on behalf of the provider. TR 12-21. The base surcharge will decrease if the provider works less than full time or seeks QHP status for less than an annual term. TR 10-12

5. PCF surcharges for individual physicians are currently based on the risk presented by the exposure of the particular physician specialty, to which an experience rating surcharge enhancement is applied for past claims of the specific physician QHP. TR 10-22; 115. This type of rating process is used by commercial medical malpractice liability insurers to determine rates. TR 115.

6. To determine the actual surcharge due, the QHP, or the provider's representative, will transmit to the PCF pertinent information concerning the provider's practice specialty, coverage term, time status, and claims experience. TR 14-15. The PCF uses an automated process to generate an actual surcharge amount, using the base annual surcharge as the foundation for the calculation. *Id.*

7. The PCF surcharge payable by a QHP Entity is currently determined by assessing a $341.00 fixed fee for the first physician in the entity and an additional $86.00 fee for each additional physician who practices in the entity. Ex. A, p. 77; TR 89-90. As more individual physicians have been employed by QHP Entities, the malpractice claim risks presented by such groups have increased. TR 110-112. The current PCF surcharge rate formula that applies to QHP Entities is inadequate to account for the risks to the PCF attributable to those groups. TR 90.

8. The Superintendent contracted with Pinnacle Actuarial Resources, Inc. ("Pinnacle") to conduct an actuarial study of the PCF as of December 31, 2018. Ex. A, p. 5. Pinnacle was contracted to determine: (a) loss and loss reserves for unpaid claims obligations of the PCF as of

December 31, 2018; (b) the PCF fund balance as of December 31, 2018, based on the projected loss reserves; (c) the overall indicated percentage change indicated for surcharge levels applicable to QHPs; (d) PCF surcharge relativities by class for individual QHPs; (e) PCF surcharges for QHP Entities; and (f) the overall indicated percentage change for surcharge levels applicable to QHP Hospitals. Pinnacle was also contracted to develop an actuarially sound rating plan for determining surcharges for QHP Hospitals. *Id.* Pinnacle's actuarial study was published on October 7, 2019, and admitted into the record as Ex. A.

9. Based on the application of sound actuarial principals, the projected losses to be paid for all PCF claims occurring prior to December 31, 2018, is reasonably projected to be $131.5 million on a nominal basis, $119.0 million on a discounted basis using a 3.5% discount rate, and $143.5 million when discounted reserves reflect a risk margin to increase the statistical confidence to 90%. Ex. A, p. 6.

10. Based on the application of sound actuarial principals, the PCF balance as of December 31, 2018, is a deficit of $44.4 million when unpaid claim reserves are stated on a nominal basis. This deficit is reduced to $31.9 million when unpaid claims reserves are discounted at an annual rate of 3.5%. When discounted reserves are stated at a 90% level of statistical confidence, the PCF deficit is $56.4 million. Ex. A, p. 6.

11. Based on the application of sound actuarial principals, the projected 2019-2020 undiscounted losses attributable to individual QHPs and QHP Entities is $26,211,763.00. The projected 2019-2020 income requirements to fund those losses, at the currently used central confidence level standard, *i.e.*, 55 percent, is $24,945,200.00, after adjusting for expenses, discount rates, and reinsurance expenses. TR 81; Ex. A, p. 58.

12. The assessment level required to fund the projected losses attributable to individual QHPs and QHP Entities will be impacted by PCF revenue increases or decreases attributable to any changes in physician specialty rating classifications. TR 93-96. Based on the application of sound actuarial principals, the ratings for these physician specialties should be changed as indicated:

A. Radiation Therapy and Shock Therapy (ISO 80163, 80165 and 80431) Move from class 1 to class 2.

B. Otorhinolaryngology – Minor Surgery (ISO 80291) – Move from class 2 to class 3.

C. Gynecology – Minor Surgery (ISO 80277) – Move from class 3 to class 4.

D. Intensive Care Medicine (ISO 80283) – Move from class 3 to class 4.

E. Nephrology – No surgery (ISO 80260) – Move from class 3 to class 2.

F. Podiatrists/Chiropodists – No surgery (ISO 80993-N) – Move from class 5 to class 4.

G. Cardiac Surgery (ISO 80141) – Move from class 6 to class 8.

H. Nephrology – Including Child – Minor Surgery (ISO 80288) – Move from class 6 to class 4.

I. Obstetrics Surgery (c-sections only) (ISO 80168) – Move from class 6 to class 8.

J. Pediatrics – Minor Surgery (ISO 80293) – Move from class 6 to class 4.

Ex. A, pp. 75-76.

13. The assessment level required to fund the projected losses attributable to individual QHPs and QHP Entities will also be impacted by PCF revenue increases or decreases attributable to any changes in class relativities. Based on the application of sound actuarial principals, these class relativities should be changed as indicated:

A. Class 5A – Increase from 1.60 to 1.70.

B. Class 7 – Reduce from 4.00 to 3.50.

C. Class 10 – Increase from 6.25 to 6.5.

D. CRNA – Increase from 0.20 to 0.25. Ex. A, p. 76.

14. The class and relativity changes identified in the preceding two paragraphs will result in a net PCF revenue increase of $229,411.00 at the central confidence level, and an increase of $259,371.00 at the 80 percent confidence level. TR 87; Ex. A, p. 105.

15. The assessment level required to fund the projected losses attributable to individual QHPs and QHP Entities will also be impacted by revenue generated from QHP Entities. TR 87-91. Based on the application of sound actuarial principals, QHP Entities should be assessed 10 percent of the individual QHP surcharge for each physician who practices in the entity. Ex. A, p. 77. This assessment more accurately accounts for the loss risk attributable to the entity form of practice. TR 110-112. Assessing QHP Entities at 10 percent of the cumulative surcharge assessed to the individual QHPs that practice in the entity will generate $1,570,142.00 of additional surcharge at the central confidence level, and $1,775,192.00 of additional surcharge at the 80 percent confidence level. TR 107-109; Ex. A, p. 105.

16. After offsetting additional income to be derived from class changes and QHP Entity surcharge increases, the projected 2019-2020 income requirements for individual QHPs, at

the central confidence level is $23,145,646.00, and $26,168,310.00 at the 80 percent confidence level. Ex. A, p. 105. The indicated individual QHP base surcharge level change required to meet the PCF income requirement at the central confidence level is 5.5 percent, and 19.3 percent at the 80 percent confidence level. Ex. A, p. 105.

17. Based on the application of sound actuarial principals, the projected 2019-2020 undiscounted losses attributable to QHP Hospitals is $22,176,471.00. Ex. A, p. 64. The projected 2019-2020 income requirements to fund those losses, at the central confidence level, is $21,104,895.00, and $23,861,051.00 at the 80 percent confidence level, after adjusting for expenses, discount rates, and reinsurance expenses. Ex. A, pp. 64 & 106. The indicated QHP Hospital base surcharge level change required to meet the PCF income requirement at the central confidence level is -4.5 percent, and 8.0 percent at the 80 percent confidence level. Ex. A, p. 106.

18. NMSA 1978, Section 41-5-5(B), requires the Superintendent to determine the PCF surcharge for a QHP Hospital based on a risk assessment.

19. Historically, the PCF surcharge payable by a hospital or hospital group has been determined by independent actuarial studies that utilized experience (claim history) ratings. TR 115-116. This process, which is used by commercial malpractice liability insurers, resulted in a virtual dollar-for-dollar (100.4), or break-even, loss ratio for the hospitals. TR 120. PCF staff cannot independently determine surcharges for the hospitals using an experienced based rating methodology. TR 116.

20. The PCF currently does not have a process for determining the surcharge payable by an outpatient facility. TR 133. Because of the limited claims experience of smaller outpatient facilities, it is not practical or accurate to determine a PCF surcharge for an outpatient facility using an experience rating-based risk assessment. TR 133.

21. To comply with the mandate of NMSA 1978, Section 41-5-5(B) to provide a rating methodology for outpatient facilities, and to enable PCF staff to perform a risk assessment that will generate an actuarially sound surcharge for a QHP Hospital, Pinnacle generated a hospital/outpatient facility rating plan. TR 116; Ex. A, p. 18.

22. The rating plan incorporates an exposure model that uses rates based on unit of exposure. Ex. A, p. 18. The ratable exposures are commonly used by hospital professional liability insurers and reflect the relative loss potential of the exposures. The surcharges by exposure were selected so that the targeted overall surcharge would generate cumulative

surcharges from the hospitals consistent with the 80 percent confidence level, or $23,861,051.00. Ex. A, pp. 18; 99-104.

23. The hospital/outpatient facility rating plan incorporates an experience rating that modifies the surcharges of larger hospitals. The experience rating is based on a comparison of the number of PCF layer claims during a five-year period compared to the expected number of PCF layer claims for the risk given the ratable exposures for the hospital or outpatient facility. The approach will be responsive to larger hospitals and outpatient facilities whose PCF claims frequency is better or worse than expected, but will also provide surcharges that do not overreact to a single large PCF claim. Ex. A, p. 18.

24. PCF staff will be able to implement the Pinnacle QHP Hospital rating plan to generate actuarially sound surcharges for QHP Hospitals without the need for an independent actuarial study for each facility. TR 128-130.

25. The term "confidence level" refers to the probability that rates will generate sufficient income to cover projected losses. TR 83. Historically, the Superintendent has set surcharge rates at the central confidence level or below. TR 102. The central confidence level is approximately 55 percent. TR 85. The PCF currently has a deficit of $31,858,505.00 in discounted reserves. Ex. A, p. 44. This deficit reflects unfunded future payment obligations. TR 100. Setting surcharges at the central confidence level or below has contributed to the deficit. TR 103.

26. Setting surcharges at the 80 percent confidence level produces an actuarially sound result and an adequate risk margin that will be less likely to add to the current PCF deficit and is more appropriate for a government insurance fund. TR 86; 100.

27. Actuarial standard of practice number 4 directs that rates/surcharges should be reasonable, not excessive, adequate and not discriminatory. Ex. A, p. 12. A rate/surcharge is discriminatory if it is priced in a way that requires one insured to subsidize the risk of another insured. TR 66-67. Applying different confidence levels to the determination of surcharge assessments for individual physicians and hospitals/outpatient facilities would result in a discriminatory rate/surcharge. TR 66-68.

28. It would be reasonable to defer the effective date of any rate increase by at least 60 days. TR 155.

CONCLUSIONS OF LAW

1. The Superintendent has authority and jurisdiction over the subject matter herein pursuant to the Medical Malpractice Act, NMSA 1978, Sections 41-5-1 to 41-5-29 (the "Act").

2. The Superintendent has complied with the Act and 13.21.2.4 NMAC in this surcharge rate proceeding.

3. The Superintendent is charged with maintaining the PCF and ensuring that it is financially and actuarially sound. NMSA 1978, Section 41-5-25; 13.21.2.18 NMAC.

4. Based on the evidence, the PCF surcharge rates should be assessed at the 80 percent confidence level for all QHPs.

5. The cumulative surcharges to be collected from all QHPs for the 2020 PCF plan year total $50,029,361 at the 80 percent confidence level: $26,168,310 of this surcharge amount is allocable to individual QHPs and QHP Entities; the remaining $23,861,051 is allocable to QHP Hospitals.

6. The risk classifications for individual providers set out on pages 79 through 81 of Exhibit A are actuarially sound and should be adopted for used by the PCF.

7. The classification factors by assigned class that appear on page 85 of Exhibit A are actuarially sound and should be adopted for used by the PCF.

8. Current individual QHP surcharges should be increased 19.3 percent by class.

9. QHP Entity surcharges should be assessed at 10 percent of the cumulative individual QHP surcharges for the individual QHPs who practice within the QHP Entity.

10. QHP Hospital surcharges should be assessed according to the rating plan on pages 99 through 104 of Exhibit A.

11. There is no evidence to support the imposition of a special assessment, and no such assessment should be imposed.

12. The increases and methodologies recommended herein should be effective 60 days from entry of an order adopting these findings of fact and conclusions of law.

Wherefore, based on the above, the Hearing Officer recommends the Superintendent adopt these findings of fact and conclusions of law.

DONE this 19th day of December, 2019.

MARILYN S. HEBERT
Hearing Officer

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing *Recommended Decision* was sent by email to the following individuals, as indicated below, on this 19th day of December, 2019.

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