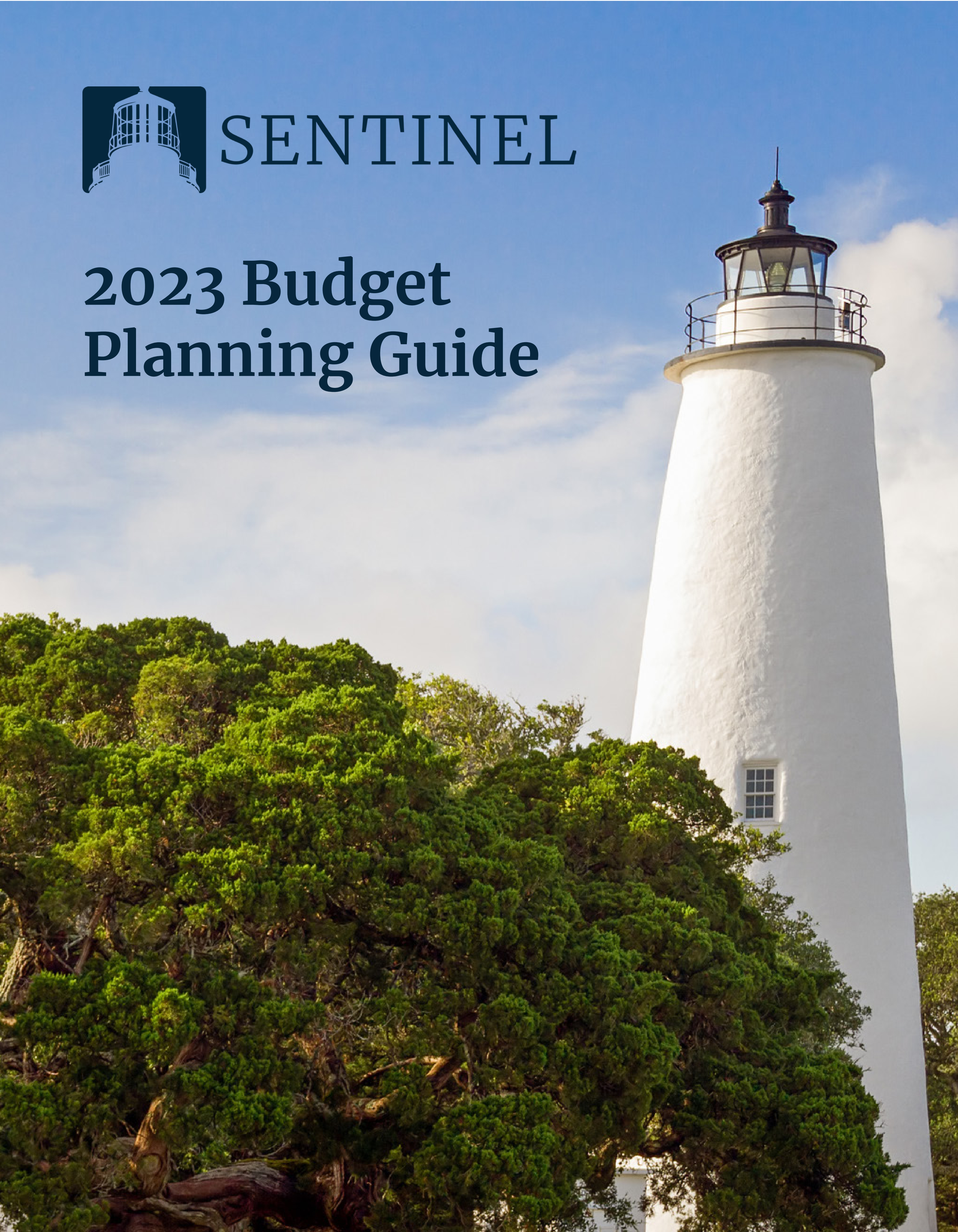
SENTINEL

2023 Budget Planning Guide



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Executive Summary

For several years, almost every line of insurance has been plagued by rising claims costs and resulting rate increases. The property and casualty industry faced profitability challenges pre-pandemic that have continued for the past two plus years. Add to that the rapid spikes in inflation and continued increased costs of goods and services and you get continued rising rate market expectations for 2023.

The COVID-19 pandemic has forever changed the manner for which healthcare is administered and delivered. When coupling the lingering effects of the pandemic with a very tight labor market, employers face challenges with finding a delicate balance between what they need to offer to attract and retain talent versus the challenges of the current inflationary economic environment.

The insurance landscape is complex and while our predictions contained within the 2023 Budget Planning Guide are based on expert research, they are subject to change. The team of risk and insurance professionals at Sentinel diligently monitors the insurance market throughout the year to keep you informed of conditions that may affect your operations.

James L. Holmes Jr., CPA
Managing Partner, Sentinel

Sentinel is the Carolina's Premier, Independent Risk Management Firm

Sentinel offers a broad scope of property, casualty, risk management, and employee benefit solutions for today's global marketplace. Founded in 2013 by an elite team of risk professionals, our Raleigh-based firm currently has offices in Charlotte and the Triad, with others in the development pipeline.

Sentinel represents clients nationwide and in numerous countries around the world. Our core business is risk mitigation and insurance services, but our greatest endeavor is investing in the success of our clients.

Our Mission

Our mission is to provide advice, guidance, and counsel to organizations and individuals who require a customized, high-touch service approach. Our commitment to remaining independently owned allows us to empower our team members to think dynamically about the unique characteristics of each client, while leveraging the resources and talents of a comprehensive technical and service platform.

Our Vision

Our vision is to protect and improve each client, personally and professionally, by elevating innovative solutions and resourceful services to unparalleled standards.

Innovative Solutions

Risk Management
Sentinel Benefits Consulting
Private Client Services
Surety Practice Group

Resourceful Services

Sentinel Risk Performance Group
Sentinel Connect
Health and Well-Being
Prepaid Legal Services

Sentinel Prepaid Legal Services Plan

In Partnership With

EXECUTIVE LEGAL SERVICES

The Prepaid Legal Services Plan encompasses Employment Law, Human Resources and Contractual Risk Transfer. This offering is designed to provide added depth and resource for your internal infrastructure.

Sentinel intentionally partnered with an independent, local, licensed North Carolina Attorney, Jacqueline C. Hawkins of Executive Legal Services, to serve clients in an engaged capacity for employment and contract related advice, guidance, and counsel.

The Prepaid Legal Services Plan is broken down into multiple tiers, billed on a prepaid, quarterly basis. Members may modify their plan selection at the end of each quarter with each incremental plan selection, requiring a minimum of 4 quarters participation before selecting a lower-tiered plan.

Any Sentinel client not yet a member of Prepaid Legal who would like to learn more about its offerings can contact their Sentinel Client Executive or Jacqueline C. Hawkins, Managing Partner at Executive Legal Services, at jhawkins@executive-legal.com.

Scan the QR Code above to learn more about the Prepaid Legal Services Plan or visit sentinelra.com/prepaid-legal-services.

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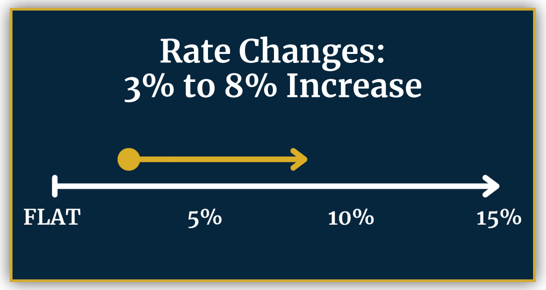
Commercial Property



The Commercial Property insurance market has hardened in recent years. Similar pricing trends occurred in the reinsurance markets during the same period through moderate, single-digit rate increases for most carriers.

Yet, it is important to note that some insureds may have encountered above-average rate increases, lowered available capacity, and certain coverage restrictions; especially those exposed to catastrophes (e.g., hurricanes and wildfires).

The Insurance Journal is forecasting an industry-wide 2022 combined ratio of 100.7%, which could signal a persistent hard market. However, Moody's reports that the Commercial P&C market had a Combined Ratio of 94.4% through June 2022, while also experiencing low double-digit written premium growth. Should these numbers hold for the remainder of the year, we would expect no industry-wide drastic changes in appetite or premiums in the coming year.

There are a few caveats to the 2023 outlook: Medical inflation, social inflation that gears up as courts resume post-Covid activity, wage inflation, continued supply chain issues, and a predicted economic recession are but a few items that could cause carriers to change strategies.

A recent report by Munich RE indicates that, "The first half of 2022 saw lower natural disaster losses than in the comparative period of 2021. Floods, earthquakes, and storms caused overall losses of some $65 billion compared with $105 billion in the loss-heavy previous year. At around $34 billion, insured losses were roughly in line with previous years. Early indications from Hurricane Ian estimate total insured losses near $63 billion. If that holds true, Ian may become one of the costliest hurricanes in U.S. History, eclipsed by only Hurricane Katrina in 2005.

While the US has had the total costliest losses from natural disasters, flooding in Australia and heatwaves and drought in the rest of the world will continue to keep the focus on climate change and upward pressure on property reinsurance prices. Even so, there are no industry-wide indications of drastic pricing changes on existing business and new account pricing looks to remain competitive on this line, as well.

Most carriers are indicating modest low-mid single digit price increases for the coming months. Also, many carriers had already tightened underwriting guidelines with regards to property valuation and condition and already restricted writing higher exposures/distressed property or in catastrophe-prone areas, so there are no major changes anticipated in the standard market appetite or terms for 2023.

2023 Outlook and Trends to Watch

Policyholders who conduct high-risk operations, have poor loss control practices, or are based in natural disaster-prone areas will likely remain vulnerable to ongoing rate increases and coverage limitations.

Interest Rates and Recession

Increasing interest rates can allow carriers more stable investment income, thereby decreasing the need to write to a pure underwriting profit. That along with an anticipated economic recession could lead to overall long-term market softening. However, economic inflation, social inflation, continued natural disasters, and other socioeconomic pressures will likely prevent a strong or prolonged soft market.

Natural Disasters

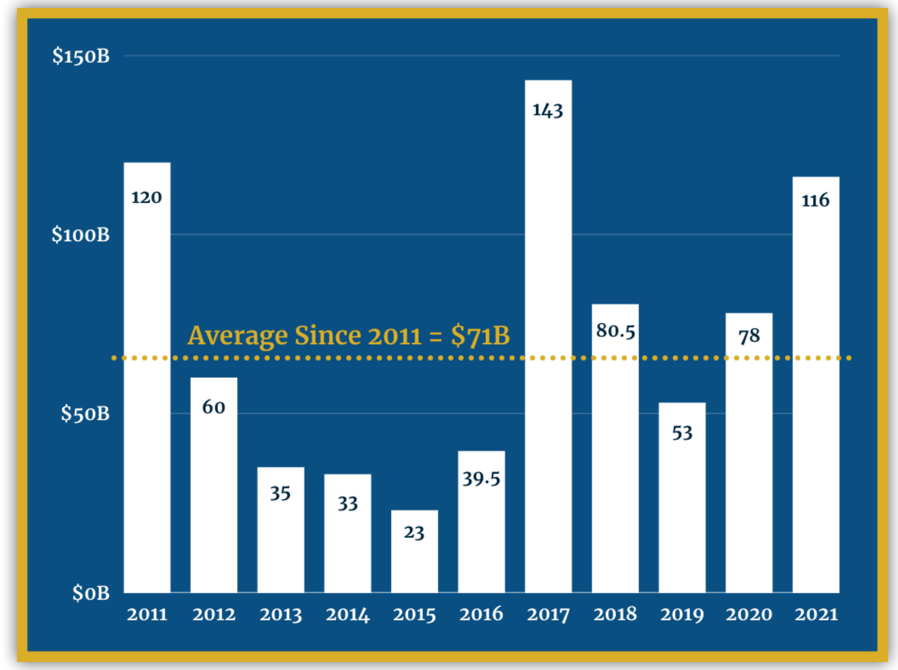
The growing frequency and severity of natural disasters have continued to pose concerns across the commercial property insurance market.

After all, these catastrophes often leave behind severe property damage and associated losses for affected establishments.

Insured losses from major natural catastrophes in 2021, excluding COVID-19 related losses, reached an estimated US$116 billion

This is the third largest total since 2011, and about 63% higher than the average loss of $71 billion since 2011, according to Gallagher Re. (Insurance Journal, 2/4/22).

Insured Losses From Natural Catastrophes



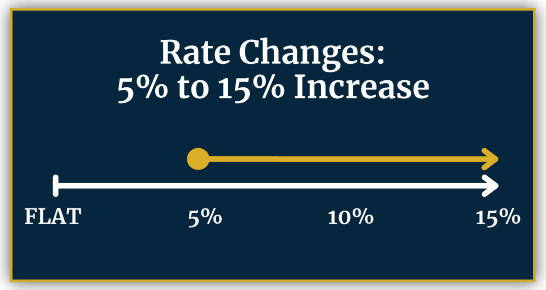
Supply Chain and Inflation Issues

The COVID-19 pandemic and various foreign disruptions have contributed to a range of material shortages (e.g., lumber and metal), supply chain issues, and inflation concerns within the past few years, thus impacting overall property construction and valuation costs.

Compounding concerns, ongoing worker shortages in the construction industry have led to elevated labor costs and project delays. Consequently, policyholders may face more claims severity and possible underinsurance issues if losses require them to rebuild structures or replace business personal property at higher costs.

Moving forward, overall inflation issues are expected to continue—potentially keeping property-related losses and subsequent claims costs high for years to come.

General Liability



The General Liability market has consistently underperformed for insurance carriers in recent years. As claims have increased in frequency and severity, insurance carriers have responded by tightening underwriting standards, deploying less capacity and seeking rate increases. Despite recent trends, carriers have begun to see some improvement in General Liability results. In 2023 it's predicted that most policyholders will encounter another year of modest rate increases for General Liability coverage.

Policyholders who operate in sectors with elevated General Liability exposures (e.g., real estate, construction, manufacturing, retail, and hospitality) may be more prone to double-digit rate increases and restrictive underwriting standards and may experience difficulties securing higher coverage limits. Rising interest rates may dampen some of the rate needed on this line of coverage.

2023 Outlook and Trends to Watch

Firming rates and capacity constraints are likely to continue for the remainder of this year and into 2023. Insurers continued to watch loss trends as the impact of courts being closed during earlier stages of the pandemic diminishes.

Social Inflation Concerns

Social inflation refers to the heightened frequency and severity of insurance claims. These rising costs result from societal trends and views toward increased litigation, broader contract interpretations, plaintiff-friendly legal decisions, and large jury awards.

Together, these factors can raise the cost of insurance. Currently, the primary factor influencing social inflation within the liability market is nuclear verdicts; especially in the case of commercial auto accidents and class-action lawsuits.

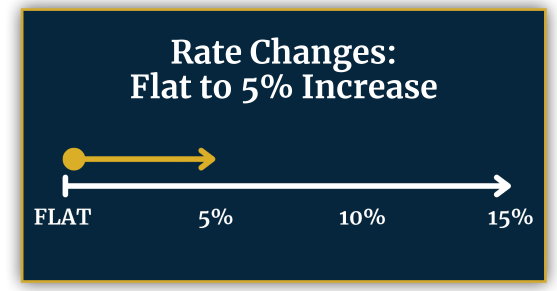
Surging Single-Fatality Expenses

Single-fatality losses have become an increasingly prevalent concern within the liability insurance space over the past decade. Such losses can stem from various scenarios (e.g., on-site accidents, product defects and commercial auto crashes) in which organizations are held liable for the resulting fatalities.

According to Advisen loss data, the median cost of a single-fatality loss spiked 67% between 2010 and 2020, jumping from $2.3 million to $3.7 million. Although these losses have occurred across industry lines, the manufacturing and construction sectors collectively contribute to more than one-third (35%) of overall single-fatality losses, primarily due to their high-risk operations.

The increasing cost of such losses is attributed to a rise in fatal incidents, social inflation, and surging medical expenses. When single-fatality events arise, they are generally followed by wrongful death lawsuits. These lawsuits may result in a range of awarded damages including medical costs, funeral expenses, and lost wages, among others, leading to costly liability claims.

Workers' Compensation



The Workers' Compensation insurance market has stayed resilient in recent years. Although the COVID-19 pandemic contributed to some fluctuations in the number of Workers' Compensation claims and associated costs, insurance experts predict claim frequency will continually decline while claim severity will see moderate changes, thus maintaining the market's robust reserves.

2023 Outlook and Trends to Watch

The Workers' Compensation Insurance segment should remain stable, with most policyholders experiencing rate decreases and others seeing minimal rate increases.

Labor Shifts

Over the past year, many employees have begun leaving their jobs in search of positions that offer greater work-life balance, flexibility, and benefits; coining a new employment trend known as the "Great Reshuffle."

The Great Reshuffle has led to a rise in short-tenured employees and increased labor shifts between industries.

Such changes present several Workers' Compensation implications. According to the NCCI, short-tenured employees have significantly higher injury frequency rates than their long-tenured counterparts. This potentially contributes to additional Workers' Compensation claims, especially in the construction, manufacturing, and wholesale trade sectors.

Wage Inflation Issues

Due to the Great Reshuffle, many businesses have increased their workers' pay to attract and retain employees. According to NCCI, this trend has been most prevalent in industry sectors with a large proportion of lower-wage positions (e.g., hospitality).

Since payroll is leveraged as an exposure base to calculate Workers' Compensation premiums, wage inflation could prompt increased rates. Higher wages are tied to greater benefits, and it's important for benefits and premiums to remain in balance.

NCCI also reported that the surge in employees receiving raises and moving from lower-wage positions to higher-paying roles could create short-term disconnects between wages, benefits, and Workers' Compensation premiums.

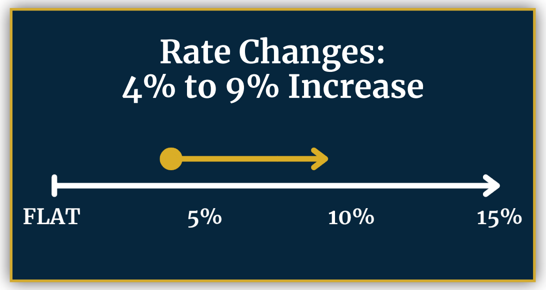
Gig Economy Challenges

Gig workers are individuals who work on demand and at will by performing short-term jobs or tasks for multiple clients. As the gig economy expands, businesses that utilize such workers have encountered various challenges. Some states have developed legislation regarding whether gig workers should be classified as employees or independent contractors. Making this distinction is critical, as it determines the Workers' Compensation benefits each type of worker is entitled to.

Generally, an employee would be protected by a business's Workers' Compensation program and receive certain benefits following a job-related illness or injury (e.g., covered treatment costs, reimbursement for lost wages and return-to-work resources), whereas an independent contractor would not.

Commercial Automobile

The Commercial Automobile space has been largely unprofitable for insurance carriers over the past decade, with underwriters experiencing significant losses despite deploying consistent rate increases. While this segment continues to face difficult market conditions, rate increases have started to decelerate in recent months. This deceleration can be attributed to a reemergence of insurers that had previously been inactive in the segment as well as the growing implementation of telematics among usage-based insurers to help collect additional driving data and ensure more accurate premium pricing.



Yet, certain cost-driving trends remain pressing concerns across the market, pushing claims frequency to pre-pandemic levels and increasing overall loss severity. Additionally, cars are significantly more sophisticated and expensive, a trend that shows no sign of dissipating.

2023 Outlook and Trends to Watch

Looking ahead, policyholders with poor loss history may be vulnerable to ongoing rate increases.

Driver Shortages

Amid the nation's driver shortage, many companies have had to lower their driver applicant standards to fill open positions. These drivers often have fewer years of experience and shorter driving records. Such factors can make these new employees more likely to be involved in accidents on the road, contributing to an increase in Commercial Automobile claims. Although the latest industry data suggests that the driver shortage may have peaked last year and will likely diminish going forward, this trend is still expected to exacerbate overall trucking sector costs for months and years to come.

Distracted Driving Issues

The National Highway Traffic Safety Administration estimates that every year, up to 391,000 people are injured and 3,450 people are killed in crashes involving distracted drivers.

In addition to injuries and fatalities, these crashes can result in substantial costs for impacted businesses.

According to Advisen's loss database, the average distracted driving loss ranges from $1.2 million to $2 million among top industries. The manufacturing industry holds the highest median cost for such losses. The chart aside shows the distracted driving losses by industry and median severity.

Regardless, the growing prevalence of distracted driving incidents has played a role in climbing Commercial Automobile insurance costs for policyholders across industry lines.

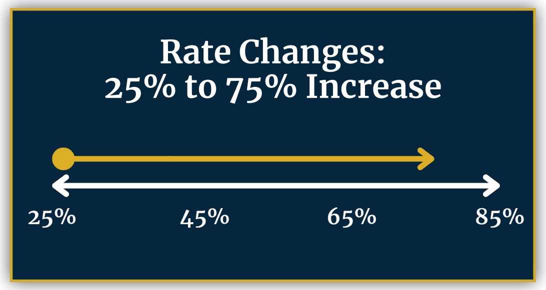
Increased Claim Costs

There are several factors contributing to surging accident costs and associated Commercial Automobile claim expenses. Primarily, rising accident frequency, greater crash severity, increased road violations, and a subsequent jump in related litigation have led to elevated social inflation issues across the segment. Social inflation, which refers to the growing costs of legal settlements and jury verdicts, has worsened the market's existing profitability concerns, creating continued challenges for insurers and policyholders alike. Such social inflation issues have been evident through a higher frequency in attorney representation for Commercial Automobile claims, prolonged claim resolution processes and increased legal defense costs.

Additionally, certain technological advancements have made vehicles increasingly expensive to repair following accidents, further driving up claim costs. Industry research shows that electronics now make up more than 40% of the cost of a new vehicle, highlighting the economic concerns associated with repairing or replacing modern vehicle parts. Compounding concerns, supply chain issues brought on by the pandemic and various international disruptions have made some vehicle parts harder to obtain. This issue, coupled with rising labor expenses, has led to extended vehicle repair times and elevated claim costs.

Cyber Liability

The past several years have seen a rapidly hardening Cyber insurance market as cyberattacks have surged in both cost and frequency. This increase in attacks has, in turn, resulted in a rise in Cyber insurance claims and subsequent underwriting losses.



Amid these market conditions, most policyholders experienced higher Cyber insurance rates at their 2022 renewals, with many insureds seeing double-digit rate increases.

In fact, industry data shows that rates rose by as much as 50%- 100% throughout the year, depending on policyholders' specific exposures, loss history and risk management measures.

Insureds have also begun encountering coverage restrictions, further scrutiny from underwriters regarding cybersecurity practices, and exclusions for losses stemming from certain types of cyber incidents—namely, acts of cyberwarfare related to international conflicts and other increasingly prevalent cyberattack methods (e.g., ransomware).

2023 Outlook and Trends to Watch

Policyholders who fail to adopt proper cybersecurity protocols or experience a rise in cyber-related losses may continue to face rate increases and coverage limitations for the foreseeable future.

Increased Nation-State Threats and Coverage Exclusions

Nation-state cyberattacks have become a growing concern over the past year, especially as the ongoing Russia-Ukraine conflict contributes to global cyberwarfare worries. Earlier in 2022, the White House issued a statement warning U.S. organizations that nation-state cybersecurity exposures stemming from Russian attackers would likely increase in the coming months. The federal government also introduced new initiatives to harden the nation's cyber defenses against foreign threats and urged businesses to follow suit.

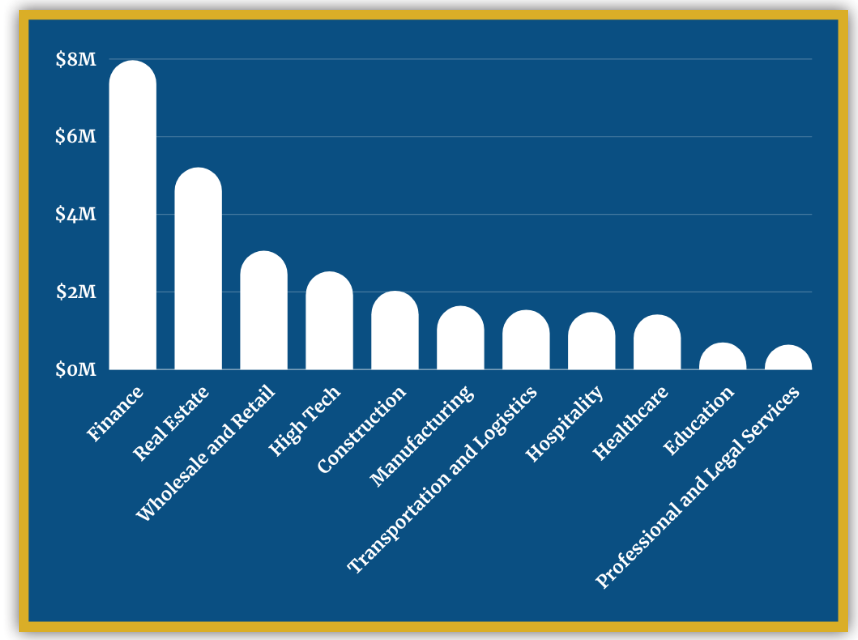
Apart from elevating their cyber defenses, some insureds have sought coverage for emerging cyberwarfare risks. But these policyholders have likely faced challenges obtaining such coverage, primarily due to war exclusions, which generally state that damages from "hostile or warlike actions" by a nation-state or its agents won't receive coverage. Cyber insurance policies are not immune to war exclusions. However, recent court cases and insurance industry shifts have both broadened and narrowed aspects of the scope of war exclusions as they pertain to cyberwarfare, creating confusion and posing potential insurance gaps among policyholders.

Elevated Ransomware Concerns

Ransomware attacks have skyrocketed in recent years, affecting many businesses but especially small- and medium-sized establishments.

According to industry data, ransomware activity decreased in 2022 compared to the fourth quarter of 2021. Presumably due to international law enforcement operations disrupting several high-profile ransomware groups since the beginning of the year.

Nevertheless, industry data confirmed that ransomware attacks still contributed over 30% of overall cyber-related losses. Further, costs stemming from ransomware attacks remain on the rise. According to data from cybersecurity company Palo Alto Networks, the average ransom payment reached almost $1,000,0000 in 2022; up over 70% from last year. The chart aside shows the average ransom demand by industry in 2022.

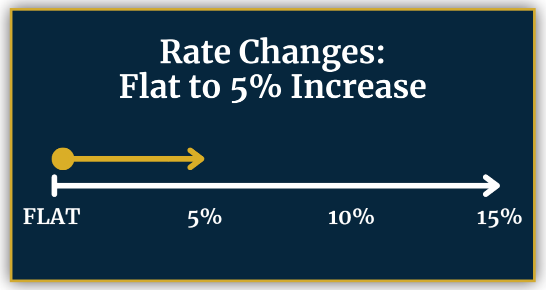


Heightened Business Email Compromise Risks (BEC)

BEC scams entail a cybercriminal impersonating a legitimate source within an organization to trick their victim into wiring money, sharing sensitive data or engaging in other compromising activities. These scams are among the most expensive types of social engineering losses, and they have emerged as a major threat. According to the FBI, BEC scams caused more than $43 billion in losses since 2016, with such losses increasing by 65% between 2019 and 2022 alone.

Directors and Officers (D&O) Liability

Although the last few years have seen double-digit rate increases and lowered capacity within the Directors and Officers Liability (D&O) insurance segment, market conditions have shifted in recent months. Rate increases have moderated, especially for publicly traded companies. According to industry data, rates increased by an average of 3-5% in 2022. It is likely this trend will continue in 2023.



2023 Outlook and Trends to Watch

Taking a closer look at these trends, renewal pricing for primary and lower excess layers of D&O coverage has ranged from flat to single digit increases in 2022. In contrast, pricing for mid-excess and high-excess layers has mostly decreased. Furthermore, capacity for higher-excess layers has been on the rise, resulting in increasingly competitive market dynamics.

While the D&O segment has also started to stabilize for private and nonprofit companies, these companies are still deemed high risk by insurers compared to their publicly traded counterparts. Thus, rates for these companies have increased by an average of 5% in 2022 and this trend is expected into 2023, according to industry data.

Even as market conditions change, it's important to note that policyholders operating within challenging industries, possessing poor loss history, or utilizing insufficient risk management measures could face ongoing coverage difficulties.

New Market Entrants

Amid increasing capacity and decelerating rates, insurers' overall sentiment toward the D&O market has shifted. Looking ahead, insurers are poised to fuel further segment growth, as evidenced by several new entrants in the market (e.g., IQUW, Rising Edge and Inigo) and, subsequently, greater competition. To secure market shares, some D&O insurers have broadened their underwriting appetites by quoting additional layers of coverage and undercutting competitors to attract new business.

Cybersecurity Concerns

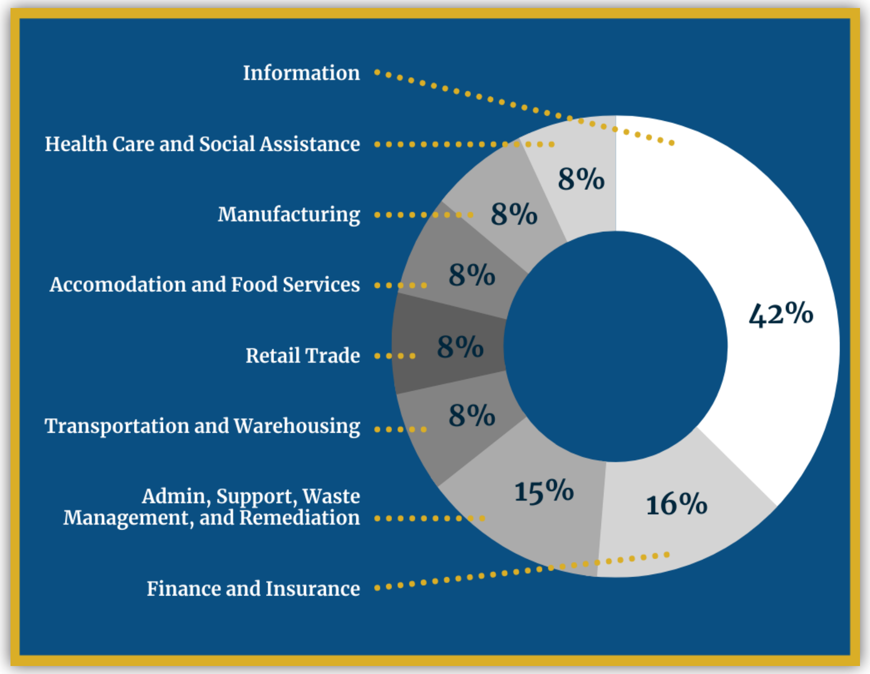
Cyberattacks continue to increase in both cost and frequency, sometimes leading to litigation and related D&O claims. After all, the decisions made by companies' senior leaders are often intensely scrutinized following cyberattacks. Potential D&O losses can arise from allegations such as senior leaders failing to take reasonable steps to detect and prevent cyberattacks, report these incidents, or notify the appropriate parties.

Compounding D&O risks stemming from cyberattacks, the U.S. Securities and Exchange Commission (SEC) proposed changes to its existing cybersecurity disclosure requirements for publicly traded companies earlier in 2022.

These changes include enhanced and standardized rules regarding cybersecurity governance, strategy, risk management, and incident reporting.

Going forward, the adoption of these changes could result in further litigation and associated D&O losses for affected companies.

The chart on the right, from Advisen, shows data breach-related D&O losses by industry since 2010.



Environmental, Social, and Governance Issues (ESG)

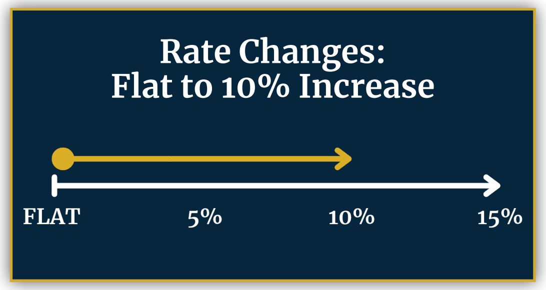
ESG activism has also made a noticeable impact on the D&O market. Specifically, extreme weather events have contributed to a surge in climate change litigation, with many allegations claiming companies and their senior leaders have failed to adequately disclose the material risks of climate change or take action to ensure eco-friendly operations.

Adding to these concerns, the SEC proposed changes to its climate change disclosure rules for publicly traded companies earlier in 2022. Such changes include requiring companies to share further information on their climate-related risks, associated mitigation measures and greenhouse gas emissions.

Changes could contribute to increased climate change litigation and subsequent D&O claims for impacted companies. This proposal was met with intense scrutiny of the SECs authority. Significant legislation is expected to follow but it may take years to work through federal courts.

Employment Practices Liability (EPL)

The EPL insurance market has hardened and most insureds have experienced rate increases in 2022. Experts predict this trend to continue in 2023. The extent of these rate increases varied based on sector, location, potential exposures, and prior losses.



Most policyholders with good claims history encountered moderate rate increases, ranging between 5%–15%, according to industry data. Further, retention increases have become common across the board, with added pressure on primary retentions.

2023 Outlook and Trends to Watch

As new insurers emerge for excess layers of EPL coverage, market capacity has somewhat stabilized. Yet, a lack of competition among primary and lower excess layers—particularly as it pertains to riskier industries (e.g., health care, retail, hospitality, and leisure) and states (e.g., California, Illinois, Florida, New York, and Texas) has created ongoing capacity challenges for some insureds.

Looking forward, first-time EPL insurance buyers may experience greater capacity difficulties as insurers focus on maintaining profitability among their existing customers. Overall, rate increases, and coverage limitations will likely persist for high-risk policyholders for the foreseeable future.

Pandemic-Related Claims

The COVID-19 pandemic forced many businesses to make workplace changes. With these changes, legal action against employers and related EPL claims followed. According to law firm Littler Mendelson, more than 5,400 pandemic-related employment lawsuits were filed between March 2020 and March 2022

Common concerns listed in these lawsuits included claims that employers failed to make reasonable accommodations for employees amid return-to-office plans, as well as allegations that employees faced workplace discrimination and adverse employment outcomes after opting out of COVID-19 vaccination requirements for health or religious reasons. As the pandemic continues, these issues are expected to remain top of mind for both employers and EPL underwriters.

Biometric Privacy Exclusions

A growing number of employers are using technology that retains biometric identifiers from their employees (e.g., fingerprints and facial geometry) for identification and access control purposes.

However, without proper precautions in place, collecting such identifiers could threaten employees' privacy, potentially leading to employment litigation and associated EPL claims.

Compounding concerns, EPL insurers are increasingly excluding or capping their exposure to claims involving biometric privacy.

Social Movements

The #MeToo movement has empowered employees to call out inappropriate workplace conduct, contributing to a substantial rise in sexual assault and sexual harassment lawsuits against employers since 2017, according to the U.S. Equal Employment Opportunity Commission (EEOC). Amid this trend, the Biden administration signed the Ending Forced Arbitration of Sexual Assault and Sexual Harassment Act into law on March 3, 2022, and employers are still determining next steps as a result.

This legislation permits employees who come forward with sexual assault or sexual harassment allegations the option to take such claims to court, even if they had previously agreed to arbitrate these disputes before the claims arose. Such legislation has the potential to prompt further employment litigation and related EPL claims as employees are empowered to come forward and speak up.

Retaliation Concerns

Retaliation is defined as an employer taking inappropriate actions against an employee for exercising their workplace rights. According to the EEOC, retaliation has repeatedly reigned as the top cause of employment litigation and associated EPL claims in the past few years. In fact, more than half of all employment charges filed with the EEOC involve retaliation.

Taking a closer look at these charges, Advisen's loss database shows that allegations of retaliation associated with racial discrimination and harassment claims have the highest median severity at $185,000. While all industries are at risk of experiencing retaliation losses, the public administration sector accounts for more than one-third (37%) of such losses, contributing to increased climate change litigation and subsequent D&O claims for impacted companies.

Medical and Recreational Marijuana

With the confirmation of legalized recreational marijuana in 15 states and medical marijuana in 37 states, Human Resources Managers are faced with a conundrum with employees scattered across the country. It is increasingly difficult to manage the differing state laws affecting employment.

Quiet Quitting

A new phrase has emerged in 2022: Quiet Quitting. Some liken it to "checking out" of their job and performing just the bare minimum to get by. Post-pandemic, many workers evaluated their job satisfaction and ended up setting boundaries in the workplace or decided to "search for something better."

This has resulted in a battle for talent in numerous industry segments. Employees don't announce they are quietly quitting, but managers need to be extremely aware of changes in work productivity or attitudes and engage in conversations with their associates when major differences are noted.

Many frontline managers and supervisors could use additional training to tackle this emerging trend. In addition, if an employee is now filling multiple roles due to lack of proper resources that leads to an entirely different discussion altogether. Many managers share a hesitation to tackle these subjects with their employees leading to additional turnover and employee morale concerns. Anytime these factors are present, EPL issues are soon to follow.

The job market is still dealing with the aftereffects of the COVID-19 pandemic. Workers are taking stock of their circumstances and considering which employment perks matter the most. Specifically, employees are increasingly more concerned about their physical and mental health, financial security, and work-life balance than before the pandemic. Many employers have responded by enhancing benefits offerings to support employees.

According to a recent study by Mercer's U.S Health Care Policy, employers are focused on improving healthcare affordability for employees in 2023.

Medical plan option with a low deductible or even no deductible:

- 41% of employers surveyed currently offer
- 11% of employers considering it

Free Employee-Only Coverage (no paycheck deductions) with at least one medical plan option:

- 11% of employers will offer
- 11% of employers considering it

Further results indicate that while free coverage historically has been relatively common among small employers (29% currently offer it), it is a newer strategy for large employers.

2023 Outlook and Trends to Watch

As employers map out employee benefit strategies for 2023 and beyond, there are several factors and trends that are having a major impact on those decisions. Employers will have to strike a delicate balance of offering attractive benefits and affordable cost while considering the following trends that could impact healthcare spending in a profound way over the next several years.

Health Care Deferred During Pandemic

Care and treatment for chronic medical issues that have been deferred since the beginning of the pandemic will inflate medical costs in 2023. In some geographic areas, expenditures for routine health care, preventative care, elective surgeries, etc. have been down by as much as 30%. Health issues and severe diseases resulting from deferred care over the past two years will inflate health care spending in 2023 and beyond.

COVID-19 and Behavioral Health

There has been an alarming increase in depression and other related mental illnesses which will have a direct impact on increased health care spending. Adding or expanding programs to increase access to behavioral health care is a top-three priority for all employers with 500 or more employees (74% rated it is important or very important); and it's the number one priority for employers with 20,000 or more employees (86% rated it important or very important).

Prescription Drugs

Higher drug cost trends will accelerate overall health care cost increases. The research into, and introduction of expensive "Specialty" drugs will continue to contribute to double-digit inflationary trends. While medical cost trend increases remain in mid-single digits, pharmacy cost trends range from 10%-15%. Pharmacy claims account for approximately 30% of employers' total healthcare cost.

The recently passed "Inflation Reduction Act" allows, for the first time, Medicare to negotiate directly with pharmaceutical companies. While Medicare recipients should realize significant savings in drug prices, the savings from Medicare will inevitably result in increases in cost being passed along to private insurance payors, resulting in higher premiums for individual and employer sponsored benefit plans.

Telehealth and Virtual Healthcare

Telehealth usage grew more than 7,000% during the first two years of the pandemic. FAIR Health's annual report studies health care indicators, prices, and utilization trends. The biggest changes occurred during the first year of the pandemic. In 2020, the utilization of traditional health care services dropped, while new models (e.g., telehealth) increased dramatically. Telehealth utilization increased 41,919% from 2015 to 2020—and national growth was 7,060% from 2019 to 2020. The growth of virtual health care will continue to grow, with companies introducing innovative telehealth & virtual care models into most of the healthcare space segments. Telehealth, specifically drug prescriptions, will grow exponentially over the next few years.

Tiered and Narrow Network Benefit Plans

Insurance carriers have been developing tiered and narrow networks. These networks are used to direct enrollees to more cost-effective providers, and are restricted to a limited number of providers that agree to meet stringent cost and/or quality objectives. These plans have significantly lower premiums and overall spending without necessarily harming access to care, even though fewer providers are covered. Narrow network plans have been common in the individual and large group self-funded market. Small and midsize employers have been reluctant to adopt this strategy, however, as limited networks have increased usage flexibility, while maintaining lower cost, expectations are that enrollment will increase by 15-20%.

On-Site Health Care

On-site health care refers to employers bringing medical services directly to their employees by establishing health care centers at or near the workplace. On-site health care can provide a full range of services, including advanced primary care, chronic condition management, physical therapy, wellness coaching and behavioral and mental health support. It can also provide increased efficiency for routine services, such as wellness visits and blood draws, by reducing travel and wait times.

Many organizations, especially smaller ones, are unable to provide full-range on-site health care. These organizations, however, are making on-site health care services available to their employees by providing access to telehealth and offering routine or tailored services within the workplace. This allows even smaller organizations to better and more efficiently focus on employee well-being while addressing their rising health care expenses.

Benefits of On-Site Care

- Convenient access to health care
- Talent attraction and retention
- Improved understanding of employees' health needs

2023 Projected Employee Benefits Costs

Despite the decreases in health care utilization during the height of the pandemic, medical care price inflation is expected to continue to increase for the near future. While many employers may not currently be feeling the full impact of the consumer price inflation in their current health care plans, that may soon change. Employers should act now to reign in rising health care expenses and better position themselves to address future increases within their health care plans.

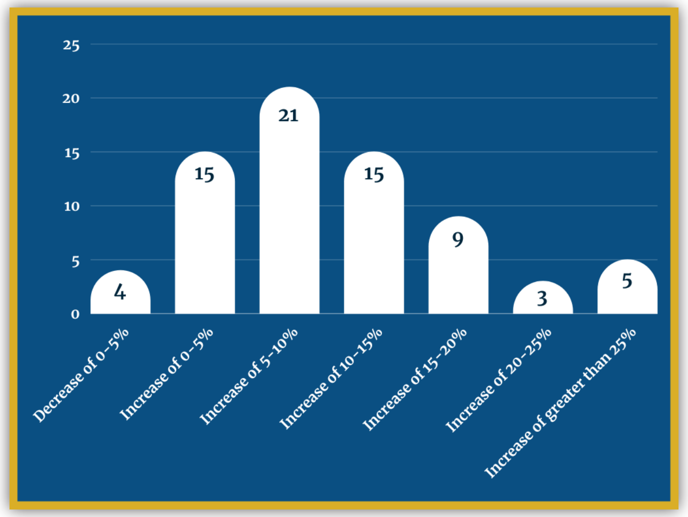
Distribution of Rate Changes Among 72 Reviewed ACA Marketplace Insurers

The average health benefit cost per U.S. employee is expected to increase by 5.6% in 2023, according to early results from Mercer's National Survey of Employer-sponsored Health Plans 2022. This is significantly higher than the 4.4% projected increase for 2022 but is still lower than overall inflation. The chart below shows the distribution of rate changes among 72 reviewed ACA marketplace insurers.

The expected 5.6% increase accounts for changes that employers plan to implement to reduce their overall health care expenses.

5.6% is higher than the 4.4% average in 2022, however employers are not yet experiencing the full impact of the current consumer price inflation with their health care plans because of the multiyear nature of health care provider contracts.

Employers should expect price inflation to be factored into the costs of health plans over the next few years as carriers' provider reimbursement contracts expire and providers negotiate higher reimbursement rates.



Employer Sponsored Health Insurance

Initial North Carolina insurers' rate filings suggest deferred care will be a contributing driver of health care spending in 2023. Health care spending for chronic and other medical illnesses that have been deferral due to Covid-19 between 2020-2022 will return.

- Small Group ACA Marketplace: Depending on the insurance carrier and geographic region the range of base rate adjustments will range from -7% to +7%.
- Mid and large employer, fully insured: average base rate increase of 7%
- Self-insured employers: Administration cost will increase due to external inflationary pressures. Stop loss claims more than doubled over the past 2 years due to Covid-19 related illnesses. Medical claims cost increased between 5 to 6.5% annually. Reinsurance Stop Loss coverage is forecasted to increase by an average of 8%.

Individual ACA Marketplace

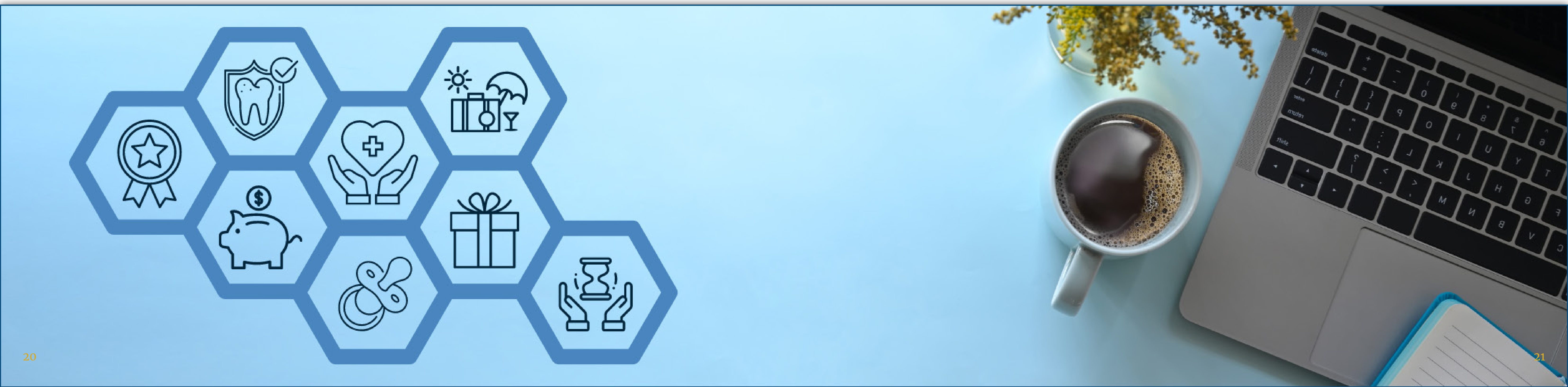
Depending on insurance carrier and geographic region the range of increases nationally will range from -5% to 20% with some increases as high as 50%

Employee Sponsored Group Term Life Insurance

Group Term Life Insurance plans will experience minimal premium increases in 2023 averaging 0-5%.

Employee Sponsored Dental Insurance

Dental PPO plans are now the norm in the market with most employees enrolled in PPO or Passive PPO Plans. Indemnity dental plans account for about 25% enrollment. Dental PPO cost trend projections for 2023 is an average of 4.5%. Dental indemnity plans are trending at just above the Dental PPO plans at 6%.



Employee Sponsored Group Short-Term/Long-Term Disability Insurance

The COVID pandemic has shed new light on the importance of disability insurance products, an employee benefit that often flies under the radar. Representatives from a leading national disability insurance company, believes disability insurance will become a more sought-after employee benefit due to Covid There will increases in both Employer Sponsored Short-Term (STD) & Long-Term Disability (LTD) in 2023. Industry experts expect STD & LTD premiums to increase by 5-7% due to more employees filing claims due to time away from work during the height of the pandemic.

Voluntary Benefits

Voluntary benefits are products such as: life, disability, critical-illness and accident insurance, as well as pet coverage, ID theft protection, legal services, and financial counseling offered through an employer but paid for partially or solely by workers through payroll deferral.

In 2019, only 36% of employers predicted voluntary benefits would be a key component of their employee benefits offering. Many employers earlier this year considered offering unsubsidized benefits. Of those employers considering offering Voluntary Benefits as part of their benefits package, the following list illustrates the types and possibility of offering these programs.

- Identity Theft: 78%
- Hospital Indemnity: 65%
- Pet Insurance: 69%
- Critical Illness: 76%
- Group Prepaid Legal: 75%

Newer Voluntary "family friendly" programs have recently been introduced to the market. Employers, to retain employees, are now considering financial planning or counseling, tuition reimbursement programs, nanny stipends, and subsidized childcare/tutoring and enhanced mental health benefits.

Individual Long-Term Care Insurance

Individual Long-Term Care (ILTC) premiums have been increasing at double digit rates for the past several years. Baby boomers who bought policies in the 1990s have continued to pay premiums and keep policies in-force at a far greater percentage that had been forecast. Most long-term care insurers had anticipated a 10% policy lapse rate, however the lapse rate for many has only been 1%. The average premium rate increase filing for 2023 was approximately 35%, depending on the state. A ILTC policy purchased in the 1990s will have increased in premium by approximately 300% by 2023. Even with the dramatic premium increases most ILTC polices are of great benefit. The average cost of a private room in a standard long-term nursing facility will average more than $125,000 annually

Employer Sponsored Group Long-Term Care Insurance

Employer Sponsored Group Long Term Care (GLTC) insurance is a great benefit to offer employees. GLTC has less restrictive underwriting and can be offered as employer paid or voluntary employee paid. Premiums are far more affordable than individual policies and can be underwritten with a base amount and allow employees to buy up to greater daily benefit amounts. These policies are typically portable and can be converted to an individual policy if employment is terminated.

Risk and Insurance

The Property and Casualty market remains in a state of flux as we look to 2023 and beyond. Where and when the market will stabilize and settle for a consistent period of time is still anyone's guess. The most important part of any risk and insurance program is your risk management partner. When contemplating your Total Cost of Risk, you need to think broadly about your overall risk and strategy rather than just focusing on your existing insurance placement and policies.

The following are five key components of a successful risk management strategy:

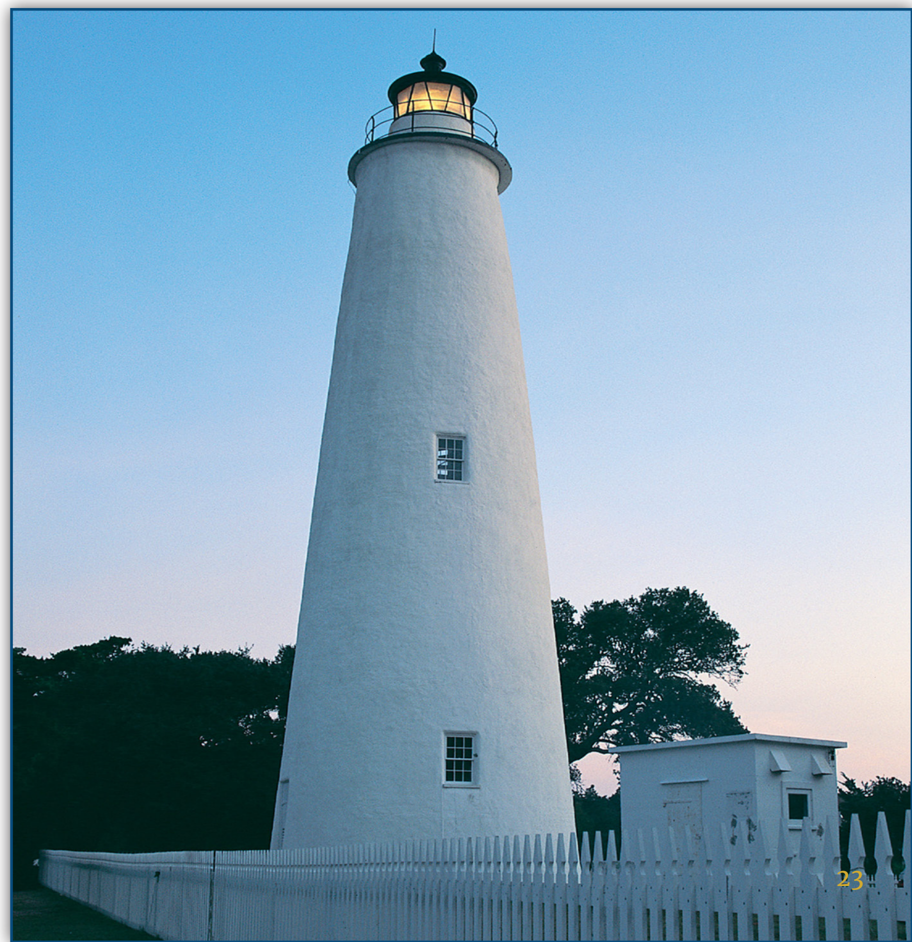
1. **Pinpoint your exposures and cost drivers**
2. **Identity the best loss control solutions to address your unique risks**
3. **Create a solid business continuity plan to account for disasters and other unpredictable risks**
4. **Build a company culture focused on safety**
5. **Manage claims efficiently to keep costs down**

In addition to implementing sound risk management strategies, working alongside an experienced insurance professional is equally crucial. At Sentinel, we focus on assisting clients to analyze their business, understand their exposures, and establish a suite of customized insurance solutions that act as a last line of defense against losses.

Employee Benefits

With respect to the everchanging Employee Benefit arena, how 2023 rates and structures will differ form 2022 depends on many factors. Carriers are looking to project claims under multiple scenarios as we move out of the pandemic into a phase where costs may be more predictable in the short and long term. However, uncertainty with current vaccine effectiveness as variants continue to migrate have experts wondering about a resumption of increasing rates and serious complications down the road.

The expectation of continued rate pressures is expected at higher averages than 2022 and 2021 for similar plan designs. As new information continues to emerge, there is still a wide range of potential effects on benefits programs and rates in 2023; historically high inflation, increased mental health services, workforce shortages and provider payment lags to name a few.



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