GROUP RATING STAKEHOLDER MEETING

Executive summary

On July 11, 2007, the Ohio Bureau of Workers' Compensation (BWC) hosted its third stakeholder meeting to further consider improvements to Ohio's group rating program. The primary focus of this meeting was the concept of group continuity.

Jeffery Scholl and Bill Hansen, both with the Oliver Wyman consulting firm, led the discussion by reviewing the principles of group continuity, illustrating how group continuity impacts experience rating and comparing options for group continuity.

Mr. Scholl explained that group continuity yields a more accurate and equitable distribution of premium rates. He added that frequent changes in group composition create situations that do not accurately reflect a group's risk-management and safety efforts in experience rating calculations because the time frame covers several years.

Mr. Scholl and Mr. Hansen said large groups, ideally, should look like large employers when it comes to rate making. Much like a large employer, a large group's actuarial experience should be reflected in the rate level. However, this can only be achieved when risk composition remains stable over time — in other words, through group continuity.

Mr. Scholl also provided a comparison of various models for group continuity. These models included: the current group rating program that allows employers to move freely in and out of groups; a uniform group program that does not allow members to be removed; and a limited flexibility program that allows limited removal of group members.

The presentation slides provided a side-by-side comparison of how each model impacts the experience modification (EM) for group members. Mr. Scholl also explained that in an ideal situation EMs should center around 1.00 with a majority of debits/credits falling between 0.75 and 1.25.

He added that any changes regarding group continuity should be phased in to ease the transition for employers. He also reiterated that groups that want to be rated for insurance purposes like large employers should function like a large employer.

In conclusion, Oliver Wyman believes it is important to adopt group rating rules that promote group continuity and controllability of risk factors. Experience rating formulas that balance stability and responsiveness as well adopting credibility levels that recognize correct predictive values of past experience are also keys to a successful program. Finally, any changes made to group rating should balance simplicity and ease of use with equity and fairness for all employers.

GROUP RATING STAKEHOLDER MEETING RECAP REPORT

Meeting Minutes

Attendees

- Rep. Steven Driehaus, Denny Davis, Lauri Cochran, Rep. William Batchelder, Jean Krum, Todd Spence, Joy Bush, Liz Bravender, John Pedrick, William Hansen, Jeff Scholl, Keary McCarthy, Jeremy Jackson, Rep. Chris Widener, Bob Schmitz, Ty Pine, Steve Millard, George Haenszel, Stuart Garson, Phil Fulton, Jack Fisher, Tony Fiore

Agenda

Welcome

- Jeremy Jackson welcomed attendees, said everyone should have received executive summary and meeting minutes from the previous meeting. He said BWC was still working on records requests – putting together data on medical only and lost-time claims with comparisons to other states. He said a list of outstanding data requests would be compiled. Finally, he introduced John Pedrick, BWC's Chief Actuary.
- John Pedrick introduced himself and explained his background in rate making.
- Rates need to be actuarially sound, high enough to cover costs but not too high, identify different risks where possible.
- Group rating concept is good.
- Wants to achieve accurate and equitable rates, build financial strength of BWC.
- Jeremy Jackson gave agenda.
- Group continuity – why it is important and how different decisions will affect experience modifications (EMs).
- Jeff Scholl, of Oliver Wyman, gave his presentation.
- Risk classification principles and considerations
- Statistical considerations
- Homogeneity
- Credibility
- Predictive stability
- Operational considerations
- Expense
- Expenses should be as low as possible, while effectively permitting the system to minimize adverse selection and maximize equity.
- Constancy
- It is desirable that the characteristics used in any risk classification system should be constant in their relationship to a particular risk. This constancy should prevail over the period covered by the insurance contract or, alternatively, over the period for which a class is assigned.

- Six, seven, or eight years are necessary in the Ohio system.
- Avoidance of extreme discontinuities
- Don't want extreme swing in rates.
- Manipulation
- The system should minimize the ability to manipulate or misrepresent a risk's characteristics so as to affect the class to which it is assigned.
- Measurability
- Controllability
- Controllability refers to the ability of a risk to control its own characteristics as used in the risk classification system. While controllability is in many cases a desirable quality for a characteristic in a risk classification system to have, because of its close association with an effort to reduce hazards and the resulting general acceptability by the public, it can easily be associated with undesirable qualities, such as manipulation, impracticality and irrelevance to predictability of future costs.
- Experience rating plans – options and comparisons
- Why is controllability a group-rating issue?
- Participants in group plans today can predetermine a key rating component, the experience modification [EM], before the actual group is formed. This allows for the creation of groups that minimize incurred losses and, thus, the EM for the next policy year. This process is repeated as each new year of experience develops.
- One can think of this system using an analogy to the fantasy sports leagues that are popular among fans today. Fantasy league participants "draft" team members at the beginning of the season with their team results based on the individual performance of the players they select. The team results are based only on what the players do in the future, with no recognition of past statistics.
- Group insurers also select employers who can participate in their respective group-rating plan with the overall loss results based on the performance of each group member. However, unlike the fantasy league example, future results do not matter, as only individual past results feed the rating modifications. In essence, because they already know the loss results of the members they are choosing, it is more like having a fantasy league where the players are chosen after the season has ended.
- Amount of group experience in rating calculation
- It takes seven years before entire group experience is in the rating calculation.
- Group plans and large employers should be identical in that their actual experience is reflected in the rate level, but that can only be achieved when risk composition remains stable over time.
- If group composition changes frequently, there is not a true reflection of the risk management and safety efforts of the group in the experience rating calculation because the time frame extends over many years.
- Rep. William Batchelder asked what the difference was between Ohio and other plans – don't have employers jumping in and out of plans.
- Jeff Scholl said yes you don't have 20 percent of members rejected every year.
- Rep. William Batchelder pointed out that private insurance has cancellations.
- Jeff Scholl said that was true.

- William Hansen said that in private insurance, when an employer switches carriers between AIG and Chubb, for example, the employer would keep his experience when he moves.
- Rep. William Batchelder pointed out that Company A might know something that Company B may not know.
- John Pedrick said that safety will come through in the experience and risk management. If a carrier has a better way of doing it, they will attract more customers.
- Jeff Scholl discussed the next slide which showed groups of employers with their original EM at July 1, 2000, their 60 percent credibility EM at July 1, 2002, and their 60 percent credibility EM at July 1, 2004, using the current rating rules, uniform group-rating rules, and limited flexibility rating rules. Uniform group rules do not allow for members to be removed; limited flexibility allows for removal of one member per year.
- Changing the credibility standard to 60 percent does not correct the rate imbalance among group and non-group employers.
- EMs should center around 1.00 with a majority of debits/credits falling between 0.75 and 1.25.
- For experience rating purposes, 12.5 percent of group losses are in the 2002 EM, while 62.5 percent of group losses are in the 2004 EM.
- Liz made a clarification on the slide to point out what uniform group-rating rules were and what limited flexibility rating rules were.
- Considerations and conclusions
- Considerations
- Desirable to phase in changes to minimize disruption by employing one of several possible implementation strategies.
- Groups that want to be rated for insurance purposes like large employers should function like large employers.
- Conclusions
- Achieve rate equity across all employers by:
- Adopting credibility levels that recognize the correct predictive value of past experience.
- Adopting experience-rating formulas that balance stability and responsiveness.
- Adopting group-rating rules that promote constancy and the desirable qualities of controllability.
- Working towards balance of simplicity and ease of use with equity and fairness.
- Want risks to be able to implement strategies.
- Steve Millard asked how we would handle small groups that simply disappear from year to year
- Jeff Scholl said Oliver Wyman didn't look at those scenarios.
- Stuart Garson asked if a member could be expelled by the sponsor.
- Todd Spence said group membership is for one year.
- Stuart Garson asked how a manufacturing company and a donut shop could be in the same group.
- Todd Spence said that groups are split into 10 industries. A sponsor can have groups in each industry. Concerns have been raised about dissimilar employers in the same group – that is not the case.

- George Haenszel said there is a lot of confusion among employers.
- Todd Spence explained the application process where groups are to submit rosters. There are a number of eligibility requirements that each employer must meet. If employers don't meet those criteria, they get rejected.
- Rep. William Batchelder asked if homogeneity is determined by NCCI.
- Todd Spence said yes. The manual classification system and industries that we used are determined by NCCI.
- George Haenszel said we keep comparing to private industry. There are fundamental differences between private industry and Ohio's workers' compensation system. There are competitive market pressures, need volume. If there is a bad business, they will write it, but they can change deductibles and coverages. Not sure how that factors in.
- Jeff Scholl said there are differences, but the underlying principles are the same. Equity and fairness in rates is necessary in private industry and at BWC.
- William Hansen said that large employers and groups should behave the same. Private insurers will write a bad business at the correct rate.
- George Haenszel said the marketplace has an effect.
- Bob Schmitz talked about return on investments and the trade combined ratio. There are peaks and valleys in the casualty insurance business. If there is a 10-percent return, you can cut rates, get more business and get a return.
- Rep. William Batchelder said in Ohio there is a single line of business. Private industry has many lines. A carrier can juggle rates among the many lines, become competitive, underbid, and drive some out of business. Some carriers made mistakes in what decisions they made. Adverse selection can cause a carrier to go out of business. Comparables don't exist.
- John Pedrick said there are similarities and differences. All companies are in the same spot at the same time. AIG won't write a policy on someone they will lose money on. Home Depot is a large company – national. Roush Hardware is a small hardware store. They may form a group with other small hardware stores to get better as one entity for insurance purposes. Lowes – you would expect they would get charged more if they have a bad experience. The two would balance each other out.
- Rep. William Batchelder talked about rates of return and costs of investment.
- Ty Pine highlighted that we are looking at Ohio only. We want to attract everyone.
- Rep. William Batchelder asked if anyone paid their rate.
- Liz Bravender said base-rated employers.
- Rep. William Batchelder compared Indiana to Ohio, and said that we are at a disadvantage because of higher base rates.
- Joy Bush pointed out the discussion from the first meeting when credibility percents and off balances were talked about. Base rates would come down 20 to 25 percent if the maximum credibility percent were lowered to 60 percent.
- William Hansen said 20 percent.
- Rep. William Batchelder said there should be a footnote every time Ohio is listed in a study because we are a monopoly.
- Joy Bush said that the higher base rates don't help us competitively.
- John Pedrick pointed out that if he had a company that was paying at a rate twice as much as it should be, he would want to know why.

- Liz Bravender referenced the handouts that were distributed at the last meeting and mentioned a manual class with a 333 percent off balance factor. Everyone is paying more for group. It is a barrier to entering Ohio.
- Rep. William Batchelder mentioned his past discussions with NCCI and recalled that Ohio has a much higher permanent total disability (PTD) rate than other states.
- Liz Bravender said that information is in the packet of information that Jeremy Jackson is putting together.
- Phil Fulton pointed out that Ohio has different settlement practices.
- Liz Bravender said that Ohio is very paternalistic in dealing with its claims.
- Rep. William Batchelder asked if that would lead to a 300-percent difference.
- Phil Fulton thought it very well could. We have to pay workers.
- Tony Fiore said Ohio does a good job of paying workers when they are injured. Incentives need to be factored in. As long as safety is factored in, an employer can get these rates. He asked if any consideration has been given for shortening the four-year tail (experience period). Shortening the period would give an incentive for providing a safe work environment. We should give a quicker incentive to be safe so employers will immediately address issues.
- Rep. William Batchelder said that raises a good question between people who are safe and where stuff just happens. A bee could fly in the window and someone could get into an accident. It is different in a foundry than in a fast food restaurant.
- John Pedrick said that any discounts should be self-sustaining. Show there is true value in any safety programs that are implemented. He talked about car discounts for anti-lock breaks when they first came on the market. Discounts should reflect the true loss experience.
- William Hansen said that when the experience period is four years, each year contributes 25 percent toward the rate. When the experience period is only three years, each year contributes 33 percent to the rate. There is a disadvantage of dropping off good years.
- Jeff Scholl said there would be a benefit to switching to an NCCI split plan.
- Ty Pine asked if the numbers assume status quo when it comes to reserving methodology.
- Jeff Scholl said that the same reserves are used across the board, so it is the same for everyone.
- William Hansen said the numbers would be the same if MIRA II were used.
- Jeff Scholl said the numbers would be the same if paid losses were used.
- Stuart Garson said he was here to represent small businesses. He had an example where an employer paid $12,000 in premium one year and $123,000 the next year after getting kicked out of a group-rating program. He had several other similar examples. Employers didn't know they were vulnerable for such large premium swings by being in a group-rating plan. How can they budget for such a large premium change? They know how to run their business. It's all about solving the problem. All of us have a horse in that race. Employers don't expect coverage for nothing, but they can't budget for wild spikes. We can't have a system where employers are at the throat of injured workers. Because of the imbalances in the system, employers try to cost shift, hide injuries or have injured workers file under private insurance. We need to send workers back to work to grow the economy.

- Rep. William Batchelder mentioned a case where an injured worker went to a hearing with the employer. The process took so long that the claimant ended up getting a PTD award when it shouldn't have been needed.
- Ty Pine said that 95,000 employers have been enjoying the group-rating program. He believed that we need to make sure the program is actuarially sound, but he disagreed on the policy to get there.
- Denny Davis asked how restrictive are we talking about. If EMs need to be centered around 1.00, a group won't exist after four years. The employers will abandon ship.
- Jeff Scholl said that Oliver Wyman looked at the extremes to see where the boundaries would be.
- Jack Fisher asked if employers are required to stay in the same group for four years. He mentioned a small farmer and group continuity. Employers don't like eminent domain.
- John Pedrick said that loss ratios are too high. If he had seen a system where the loss ratios were three to four times normal, he would call that dysfunctional. In a system that is working, an employer would not see a 10-fold premium increase in one year. There would be a premium increase. More weight should be placed on frequency instead of severity. A small operation with a permanent disability claim won't have such a great impact. This is what we are trying to do.
- Steve Millard agreed with Stuart Garson not so much Ty Pine because they represent small businesses. Small businesses are one step away from being in the same position. A system with real value should get the benefit.
- C. Luther Heckman said that in dealing with constituent complaints, not one that they looked at was accurate. Small employers aren't ignorant. If they are getting an 80-percent discount, they should assume that their rates will go up. They get a hell of a deal. They need to budget for hard times. Constituents make decisions and should be accountable for them.
- C. Luther Heckman said that when an employer no longer qualifies for group rating, they don't want to lose them as a customer. They do remedial work until they get back to a place where they will qualify for group rating again.
- Jeremy Jackson said that we need to do a better job of informing people of group and what can happen when they are in a group-rating program. Everyone knows of the inequities overall.
- Tony Fiore said that we can agree we need to move in some direction. Even if we switch to NCCI, the $7,000 premium amount goes to $50,000 instead of $70,000. There isn't as quick of an incentive to be safe. Referring to George's point, how much have they been saving, and what is their frequency and severity.
- Jeremy Jackson said that we couldn't quantify that in terms of dollars. Frequency of claims is focus in the NCCI system. One claim won't hurt as much. It isn't as crippling. There is an incentive to be safe.
- Tony Fiore said there are a lot of different factors to look at, not just group rating. Look at loss ratios; there are so many more factors to examine.
- William Hansen asked a question of Denny Davis from his comments. How can you expect from random nature to always have EMs less than 1.00?
- Denny Davis said that employers won't stay in a group-rating plan if they have better rates on their own.
- William Hansen said that the rates should be expected to fluctuate up and down.

- Bob Schmitz said that employers aren't joined together by family so they don't have a reason to stay in a group together.
- John Pedrick said that groups should reflect doing something together. We need to have an accurate picture of what the future losses are going to be and what the group is going to be. How long should employers be kept together? He made an analogy to car insurance. Teenage kids have a higher risk for car accidents. Carriers estimate the best rate for insurance. When group members come in and out of the program, they see huge changes. You can't measure the true risk.
- Tony Fiore said that even in private insurance, that state fund is the high-risk pool so it doesn't drag down people who aren't high risk. In Ohio, the groups take on that roll.
- Joy Bush said she was really enjoying the macro-level conversation, but she wanted some discussion on stickiness and the limited flexibility plan.
- Steve Millard said there needs to be a benefit from group. He needs more details about the proposed changes. Right now employers worry about the administrative fees, sponsor fees, and group discount. How do you keep groups together?
- Tony Fiore asked if stricter rules would make more pressure on employers and claimants.
- Rep. William Batchelder asked where the 100-percent discount came from. Moses didn't bring it.
- Liz Bravender said that before group rating, there weren't that many 100-percent credible employers, or they were self-insured. NCCI had a similar model. In the 1980s they pulled the credibility percent back. Employers needed to be much larger to still be 100 percent credible. Ohio didn't adjust.
- Rep. William Batchelder asked what the barrier was to becoming self-insured.
- A few people responded that the statute was the barrier.
- Stuart Garson asked if the stickiness rule would apply in reverse. Do employers have to stay out of the group program for a couple of years?
- John Pedrick said that those employers have stickiness inherently by being in existence.
- Denny Davis remembered the early days of group rating when groups kept the experience of employers when they left the group, but it was manipulated. He quipped he had spent half of the last hour trying to figure out how to manipulate the stickiness rule.
- Keary McCarthy made a comparison between one small employer not in group with the same small employer in a group-rating program. In the group-rating program, if there is one claim, the risk will be dispersed across the entire group. This is inherent in a group program. The employer not in group doesn't have this benefit. It is important to recognize the benefits of group.
- George Haenszel said that he thinks everyone clearly understands the concerns of group. But in the insurance business, if you can't get a divorce, will I marry you? If the bar gets raised, employers will be more selective. There are insurance cycles. He mentioned drafting a letter to send to an employer who was going to be removed from group. Pretty soon all group employers were getting the same letter. The marketplace finds ways to do what it wants to do.

- Ty Pine said that he needs details on the proposed changes, so that is why they are talking at a macro level. We need to go back to the process in 1995 where they have their actuaries review the information that has been presented to understand the information and provide responses.
- Jeremy Jackson said that everyone needs to talk to whoever they need to for feedback. Submit questions in writing. The goal of these meetings was to get feedback. Over the next couple of weeks, get your questions together.
- Bob Schmitz said that no one has resources. You can't find an actuary in two weeks. RFPs need to be submitted. It would be a very difficult task, almost impossible. They didn't have Oliver Wyman and Pinnacle to review information. We need to consider the legislature and I am sure that Rep. William Batchelder has something to say about that.
- Rep. William Batchelder said there is some pending investment language on rates of return. There is potential legislature about MCOs and TPAs. He has no idea how long those hearings will take. He is baffled how no one knows where large discounts come from.
- Bob Schmitz says that the legislation requires a study of our rating systems and reserving. Is an RFP in process?
- John Pedrick said that the board is the first thing. The Workers' Compensation Council is the next thing. I am your actuary. I am new, have fresh eyes, and can provide factual insight and the transparency needed to move forward on a business decision. I am here to help make the system fundamentally sound.
- Jeremy Jackson said this process isn't meant to make a decision and never talk about the issues again. We are not going to try to slam something in without legislative and board approval, but everyone knows something needs to be done.
- George Haenszel asked why there was urgency now to fix the problems. Small employers have subsidized large employers for years.
- Jeremy Jackson said that we wouldn't go from A to Z immediately. It will be over a period of time.
- Rep. William Batchelder said it needs to be a short-term problem. We need to do something for small employers now.
- Phil Fulton said we need to do something.
- Jean Krum said we have an obligation to act.
- Keary McCarthy said we have tried to move methodically and judiciously at the same time.
- Bob Schmitz said the entire discussion has been from an actuarial perspective.
- George Haenszel asked what the process is going to be for developing an agenda and moving forward.
- Jeremy Jackson said the next meeting would be on rule changes. We want to have people submit rule changes to Todd Spence to include in discussions at the next meeting.
- Bob Schmitz expressed concern about the time frame for rule changes.
- Jeremy said that any changes would be submitted to the group to review.
- George Haenszel asked if the rules were subject to JCAR approval.
- Bob Schmitz said no.
- Jeremy Jackson said they would be subject to board approval.
- Ty Pine asked if all rules would be open for discussion at the next meeting.

- Jeremy Jackson and Joy Bush said that only the group-rating eligibility rules would be discussed.
- Ty Pine said that other rules were discussed.
- Joy Bush said we are trying to focus on group rules.
- Rep. William Batchelder asked if the governor had been given names for the board.
- Bob Schmitz said yes, 44 names.
- Lauri Cochran asked if we would be able to see the proposals before the next meeting so we can provide feedback. They have employers who get kicked out of group rating, but they won't follow their suggestions to get eligible again.
- Jean Krum said the type of thing we are looking for might be out of the box.
- John Pedrick said in regard to the question of urgency, that it is a business development issue.
- George Haenszel said he could see that, but moving the maximum credibility from 95 percent to 90 percent was a doubling of premium.
- John Pedrick said that what we are doing today is setting the goal.
- Stuart Garson asked if we would be addressing people who are paying too much.
- Phil Fulton asked if we had data on the people in group, their movement, and on other discount programs.
- Todd Spence said that in 2004 there were 91,000 members – 5,100 were in group the previous year, but not the current year, and would have met the eligibility requirements; in 2005, there were 93,000 members – 6,100 were in group the previous year, but not the current year, and would have met the eligibility requirements; in 2006, there were 98,000 members – 4,500 were in group the previous year, but not the current year, and would have met the eligibility requirements.
- Jean Krum said that we are trying to help everyone.
- Joy Bush said that the 5,100 employers weren't the only ones disadvantaged. The other 280,000 employers paid higher base rates and premiums. The inequities need to be addressed for the bulk of employers.

Next Steps

- Jeremy Jackson asked attendees to send proposed rule changes to Todd Spence.
- Next meeting is scheduled from 9 a.m. to noon Wednesday, July 18, in the William Green Building (Level 2, Room 1).
- Next meeting agenda:
- Reviewing group eligibility requirements.