Ohio Bureau of Workers' Compensation Board
Executive Summary: Comprehensive Study Group 4 Tasks
December 2008

This document briefly summarizes the results of Deloitte's Comprehensive Study on Group 4 tasks. The tasks included in Group 4 include: Actuarial Department Organization, NCCI classification plan; Experience Aggregation; Minimum Premium; Coal Workers Pneumoconiosis Fund; Marine Industry Fund; DWRF; Appeals; Out-of-State Employers; and Rehabilitation Program. Findings on the Group 4 task regarding the Handicap Reimbursement program were provided with the Group 3 results.

Actuarial Department Organization (Task # 36)

Situation: Current law requires that BWC contract with one or more actuarial firms to perform actuarial services for the actuarial audit reserve, rate adequacy, program pricing reviews, and other matters. In addition, House Bill 100 also required that BWC contract with one or more actuarial firms to assist in measuring the performance of Ohio's workers' compensation system and in comparing it to other state and private workers' compensation systems (the Comprehensive Study). There is limited internal capacity to analyze data, trends and findings relative to rates, programs pricing and reserving. As a result, there is almost a complete reliance on outside actuarial resources for all traditional actuarial functions, with limited internal review and analysis of findings.

BWC is interested in expanding its internal actuarial functions to include core actuarial functions. However, its status as a state agency could create some hiring challenges for actuarial talent; for example, providing a professional development program that is comparable to other actuarial positions or the ability to offer reimbursement of relocation expenses for newly hired actuaries.

Methodology: Our analysis included a review of the current actuarial organization at BWC, as well as a discussion of suggested actuarial organization functions which have been outlined by the BWC Chief Actuary. We also assessed the impact on actuarial workloads and requirements based on BWC's current capabilities and the recommendations for other tasks in the Comprehensive Study. We also researched relevant industry sources for comparison to the BWC, as well as to gain a better understanding of trends in the actuarial profession. Additionally, we incorporated our understanding and experiences with actuarial organizations from a variety of workers compensation providers across the country, including state funds, and used this information when inventorying prevailing practices and developing recommendations. Throughout our analysis and in the development of our recommendations, we considered the mission of the BWC and how the actuarial organization can and should support that mission.

Conclusions: We envision the BWC actuarial organization as having a mission to be a significant contributor to assess the effectiveness and efficiency of the Ohio workers' compensation system and to recommend and/or drive efforts to improve the financial security and stability of the system. Accordingly, their responsibilities would include:

- Analyzing and assessing loss reserves and net asset level needs.
- Establishing appropriate rate levels and pricing programs.

- Designing and analyzing programs that incent employer behavior and/or impact premium levels, such as the Safety Grant Program.
- Monitoring and assessing the impact of BWC cost control efforts such as MCOs.
- Analyzing system benefits relative to the intended application and BWC mission.
- Ensuring analysis performed by internal and external resources is based on appropriate data and assumptions.

In support of this mission, we recommend that BWC establish internal actuarial functions for rates, pricing, reserving and net asset analysis, as well as to obtain more data and information and to improve the analysis and integrity of such data and information. In addition, the actuarial function would work with other BWC areas such as the office of the COO and the CFO to assist them in achieving their missions. Focus should be put on building these core competencies and building the associated organization within the existing Actuarial Division, which would ultimately report to the Administrator. We recommend the future organization be organized around four functions each representing a team reporting to the chief actuary:

- <u>Rate Levels and Programs Pricing</u> - Establish a team and begin building in–house capability while expanding the capability to support the implementation of recommendations made in other Comprehensive Study task recommendations, such as performing rate level studies, designing and analyzing the performance of programs pricing, and conducting loss cost studies. This group would also liaise with external actuarial resources needed to perform independent reviews, as well as to provide additional expertise, specialized experience or additional capacity in this area. By focusing on these functions, BWC will be able to immediately advance the organization above the current capabilities level. Additionally, this would allow the BWC to build the capacity to address some of the task recommendations internally, while building necessary knowledge to manage this function more effectively on an ongoing basis.
- <u>Reserving & Net Asset Analyses</u> - Establish Director/Manager function and begin to build the capability and capacity to perform some of these analyses and to review the results of any outside studies. In doing so the organization would have primary responsibility for reserving and net asset level analyses, including reinsurance evaluation and coordination and analysis of external studies, as well as for support of the claim operations and development of claim diagnostics. This responsibility would include appropriate oversight of any outside assistance that is needed due to expertise, capacity or independent opinion. Initially, the BWC should focus on understanding and interpreting the current reserving and net asset analysis performed by outside actuarial resources, transitioning to additional secondary studies and variance analysis over time, and hiring staff to support these functions as they are built out. In the longer term, the BWC actuarial function should be expanded to perform much of the standard reserving and net asset analyses, and use external resources for a second opinion to determine reserve and net asset levels, to provide for the appropriate control and

independent support, and to meet state requirements for independent actuarial review.

- Data Management – Establish a function with the initial responsibility to improve the depth of data, data quality, and understanding of data, as well as to provide data needed for internal and external actuarial studies. This group would be responsible for the development of actuarial data bases and reporting tools to facilitate review and analysis by the actuarial resources. We also recommend that the Rate Adjustment Team transition to this group since much of the function surrounds data, including adjustment of employer and/or group claim experience and data management for MIRA, including the provision review and investigation of this data.
- Rating – Continue the current function performed by the private employer and public employer (taxing districts and state agencies) teams, focusing on calculation of rates and ensuring accuracy. However, the current support that these teams provide around data gathering should be transitioned to the data management function as noted above. Additionally, any support provided to the review and validation of actuarial studies should be transitioned to the function responsible for rate level and programs pricing or the function responsible for reserving & net analyses.

Once these functions have been established, external resources should be used to supplement BWC actuarial resources, perform special analysis or a deeper review, and to provide industry perspective and specific expertise. Additionally, we recommend external actuarial resources still be engaged to provide independent review of pricing and rate assumptions, as well as provide a second opinion on reserves and net asset levels on an annual basis, meeting both state and Board requirements while providing additional controls on the actuarial process.

In order to make this organizational expansion successful over time, we recommend that BWC take certain actions to enhance its ability to attract and retain actuarial talent.

- Create a job classification(s) for actuarial students which support professional requirements regarding exam passage and training by including the requirement to study and sit for exams, balanced with job performance and capabilities. (The term actuarial student does not mean that the employee is a college student, but rather that they are a studying to become a qualified actuary, including on-the-job time to study for the professional actuarial exams, etc.)
- Provide study materials and pay for exam fees.
- Foster an environment that exposes the actuarial student to different projects and functions to replace formal rotational program.
- Focus recruiting efforts to mitigate competition with large, established private employers that can provide enhanced programs and pay scale (e.g., small liberal arts schools with a strong math/science program but without a formal actuarial program).
- Emphasize benefits and quality of life aspects of BWC employment.

NCCI Classification System for Rating Calculations (Tasks #3)

Situation: Ohio (BWC) has adopted the National Council of Compensation Insurance ("NCCI") guidelines for the purposes of assigning classifications to employers. BWC has 28 classification codes that are state specials.

Methodology: We reviewed BWC's classification rules for rating calculations and compared these rules to common industry practice. In addition, we reviewed BWC's payroll distribution by class code to determine whether any apparent anomalies exist.

Analysis: BWC has largely adopted the NCCI classification system in a manner consistent with other states.

Conclusions and Recommendations:

- **Assignment of Classifications:** We recommend the BWC continue to use the NCCI classification system with respect to basic classifications, standard exception classifications, and other classification rules.
- **Public Taxing Districts Classification System:** BWC has created 14 state specials (9400 codes) for public employees which serve only to segment out standard exception class employees for organizations such as Public Libraries & Local School Districts. Ohio has more state specials for public employees than all other states. The current state specials add unneeded complexity and, more importantly, reduce the credibility of the loss experience of each class. As a comparison, Oregon has four state specials for public employees, and Utah has three compared to 14 in Ohio. It is our recommendation that Ohio consider using the NCCI classification system for public taxing districts and consolidate the number of state special class codes for these employers. We believe that this will allow BWC to better reflect the relative hazard level by employee job class for the public taxing districts.
- **Construction Classification System:** We find that BWC's use of class code 5605 (construction estimators) is not necessary. A review of state loss costs shows that code 5605 matches the other low loss cost code in the construction industry; 5606: Contractor – Project Manager, Construction Executive, Construction Manager, or Construction Superintendent. Approximately 14% of payroll for all construction classes is coded to 5605, compared with approximately 5% coded to 5606. The payroll in 5605 appears to be disproportionately high given the class definition. This is potentially a payroll audit issue for the misallocation of payrolls by construction employers to a lower rated class. Adherence to the NCCI Scopes Manual should alleviate the potential problems. We recommend that BWC monitor the procedures in place to ensure that only appropriate payroll is coded to both 5605 and 5606.

- **Process of employer's reporting payroll, premium auditing process and the procedures for non-reporting of payroll:** BWC's policy and procedures for premium auditing are well documented based on a comparison to industry and other state funds. We recommend no change to the policies and procedures currently in place. However, we understand that BWC has audited approximately 30,000 employers since April, 2006 compared to approximately 300,000 employers in Ohio. This is a far below common industry practice. We recommend that BWC establish specific audit objectives, including developing an expanded approach that will audit most employers every three to five years and possibly more frequently (every one to two years) for large employers and certain other types of employers. We also recommend increasing the scope of the premium audit function to introduce different levels of audits and more focused or targeted audits. We recommend that BWC consider an audit scoring system as a tool to prioritize potential premium audits by employer and to improve the effectiveness and efficiency of BWC's premium audit resources.

Experience Aggregation Approach (Task #32)

Situation: BWC does not apply the common majority ownership principle in calculating individual employer experience modification factors. Entities are "tracked" and assigned experience based upon federal tax identification numbers. Although BWC may decline to issue a new policy for what is essentially the same business as an existing policy, they do not blend the experience of commonly owned but separate businesses. In cases of partial or whole succession, BWC does transfer experience to the succeeding or acquiring entity.

Methodology: We reviewed BWC's approach to experience aggregation for experience rating and compared it to common industry practice.

Analysis: The industry standard (NCCI) uses an approach that captures ownership. Applications are not typically finalized until 100% of a business's ownership is accounted for. The *ACORD 130- W*orkers Compensation Application is used by almost all private carriers and many state funds. In the Individuals Included/Excluded section, the form requests names, birth dates, titles, and ownership percentages for partners, officers, and relatives.

A potential issue that is created by grouping entities by tax identification numbers rather than common majority ownership is that employers with historical experience that would result in debits from the experience rating process are provided an opportunity to create new entities in order to be base rated.

Conclusions: It is our recommendation that BWC adopt the NCCI approach of capturing common majority ownership in the aggregation for experience rating, to be more consistent with industry practice. This would require discontinuing BWC's practice of relying on the federal tax identification number to identify separate employers.

Minimum Premium Review (Task #5)

Situation: For accounts that do not report payroll, a minimum premium of $50 is charged for each six months of coverage. Similarly, for those accounts that do report payroll, but for which calculated premium is less than $50, the minimum premium of $50 is charged for each six months of coverage.

Methodology: We reviewed information provided by BWC on the number of accounts which had minimum premiums for each six month policy period from January 1 – June 30, 2003 through July 1 – December 31, 2007. We also compared BWC's minimum premium amount to those typically seen in the industry.

Review and Analysis: As shown in the table below, minimum premium accounts have experienced high loss ratios since 2003, when the minimum premium was $10 per six months of coverage.

Summary of To-Date Loss Ratios for Minimum Premium Policies (excludes PEO's)

Policy Period	Minimum Premium Amount	Policy Count	Premium	Claim Count	Incurred Loss	Loss Ratio
1/1/2003	10	65,825	658,250	343	9,011,609	1369.0%
7/1/2003	10	64,406	644,060	351	8,997,300	1397.0%
1/1/2004	10	69,743	697,430	380	7,437,931	1066.5%
7/1/2004	10	67,210	672,100	303	4,788,673	712.5%
1/1/2005	10	71,012	710,120	274	5,049,070	711.0%
7/1/2005	10	68,177	681,770	310	5,048,506	740.5%
1/1/2006	10	70,273	702,730	319	4,518,260	643.0%
7/1/2006	50	79,555	3,977,750	357	6,664,485	167.5%
1/1/2007	50	78,424	3,921,200	377	4,891,822	124.8%
7/1/2007	50	72,245	3,612,250	380	5,572,541	154.3%
Totals			16,277,660		61,980,197	380.8%

Note: Incurred losses are undeveloped.

Conclusions: It appears from the chart above that BWC needs to charge minimum premium of approximately $75 - $100 per 6 month period in order to cover the losses associated with minimum premium accounts. BWC's minimum premium level is significantly lower than industry levels, which generally range from $500 - $750 per year. Given that the current minimum premium appears to be insufficient to cover losses, and the disparity between BWC's minimum premium and industry levels, we recommend that BWC examine the feasibility of raising the minimum premium to a level that is more likely to be in line with the expected losses. Some phase-in of increases in minimum premiums might be appropriate.

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In addition, we recommend that BWC increase the involvement of the premium audit function with respect to accounts that report no payroll but experience claims. There are typically 200 to 300 such accounts in each 6 month period. Since April, 2006, 292 payroll audits have been performed on these accounts. We recommend that BWC perform some level of audit of most of these accounts in order to evaluate the possibility of fraud and to help determine whether the minimum premium is appropriate. We also recommend that BWC consider the use of a per capita exposure base rather than payroll for certain classes such as domestic workers. This is consistent with NCCI practice for these classes where payroll is not readily available. This NCCI approach should prevent or mitigate issues regarding how minimum premiums are applied to employers in these classes.

Rating – Disabled Workers Relief Fund (DWRF I and DWRF II), Marine Industry Fund (MIF), and Coal Workers Pneumoconiosis Fund (CWPF) (Task # 7, 10, 13)

Situation: Oliver Wyman (OW) prepares annual rate recommendations for the DWRF, MIF, and CWPF. The DWRF provides supplementary payments to workers whose combined PTD plus Social Security Disability benefits are lower than a specified entitlement amount, which is indexed to the CPI each year. The MIF insures maritime employers from exposure arising from federal USL&H. The CWPF insures employers with mining operations from exposure to black lung claims subject to federal benefits.

Methodology: We were provided with the rate reviews for the July 1, 2003 year through the July 1, 2007 year. We reviewed OW's rate reviews, supporting reserve reviews, and supplemental schedule of revenues, expenses, changes in net assets, and balance sheet related to these funds in BWC's financial statements.

DWRF

Review and Analysis: DWRF revenue is derived from assessments on employers' payrolls or premiums. Two separate assessments are applied to employers, one related to accidents occurring prior to 1987 ("DWRF I") and another for accidents occurring in 1987 and subsequent ("DWRF II"). DWRF I assessments are based on a rate applied to the employer's payroll. This rate is limited by current law to no more than $0.10 per $100 of payroll. DWRF II assessments are based on a rate applied to the employer's base-rated premium.

Under current law, DWRF is funded on a pay-as-you-go basis. Assessments are typically based on projected payments for the next 12 months. House Bill 100 permits BWC to assess employers in future periods for amounts needed to fund DWRF. As a result, BWC reflects an asset for unbilled assessments receivable in both the June 30, 2007 and June 30, 2008 financial statement. The amount of the unbilled assessments receivable is approximately $1.6 billion as of June 30, 2007 and $1.5 billion as of June 30, 2008. The net assets of DWRF are $800 million as of June 30, 2007 and $849 million as of June 30,

2008. Consequently, without the accrual for the unbilled assessments receivable, DWRF would be in a significant deficit position of $650 million as of June 30, 2008.

The table below displays the assessment income reflected in BWC's financial statements for the past four fiscal years:

Fiscal Year ending	DWRF Assessment Income ($ Thousands)
June 30, 2005	115,933
June 30, 2006	130,644
June 30, 2007	130,790
June 30, 2008	23,389

For the past several fiscal years, receipts from assessment income have exceeded disbursements related to DWRF benefits. As a result, Oliver Wyman has recommended reductions in the assessment rate for DWRF I. For DWRF II, where the indicated assessment rate (0.7% of base premium) is higher than the actual rate (0.1% of base premium), Oliver Wyman recommends no change in the rate level.

Conclusions and Recommendations: The asset of $1.5 billion on BWC's balance sheet for unbilled assessments is based on BWC's statutory right to assess employers in future periods for DWRF funding. It is our understanding that there is no corresponding liability reflected on the balance sheet of employers who will be subject to these assessments. Therefore, considering the state of Ohio as a whole, there is an unrecognized obligation of employers for their collective potential future premium liability related to this Fund equal to $1.5 billion. For BWC, the unbilled assessment receivable for this accrual represents 177% of the DWRF net assets as of June 30, 2008

We believe it is inappropriate to reduce the DWRF assessment rates to a level which produced less income for the year than the expected payment level. This will cause the unfunded liability for DWRF to increase, creating a larger burden for employers to bear in future periods. We recommend that BWC set the DWRF assessment rates at a level sufficient to absorb expected payments for the upcoming year.

In general, the methodology used by OW to estimate expected payments appears to be appropriate. However, the statute that requires DWRF to fund on a pay-as-you-go basis is inconsistent with the concept of actuarial soundness, as indicated in actuarial principles and standards, which state that a premium rate should be sufficient to fund for the expected costs incurred during the period, rather than those costs expected to be paid during the period. At a minimum, we recommend setting the level of assessments equal to the expected payments in the next year in order to prevent increasing the unfunded amount in the DWRF.

We recognize that any change to the funding basis of the DWRF would require legislative change. We recommend a change in legislation, considering the large amount of unfunded and unrecognized obligations, the lack of a good, clear, and long term public policy rationale for pay-as-you-go funding for these benefits. The policy rationale should also address the need to have a separate fund rather than being funded through the SIF, and the issues of fairness and equity between past, current and future employers, who pay the assessments for the DWRF benefits. Separate funds creates an obligation for the BWC to manage them, creating duplicative processes and inefficiencies. It also creates additional risks for each fund, and additional responsibilities to maintain each fund's financial strength and stability, which could be better accomplished under a combined fund. BWC does not have a process for evaluating the continued need and relevance of separate funds or for combining or closing a fund. Therefore, we recommend further research to support possible legislative change to combine the funds of BWC. As a separate fund, we recommend the development of a funding policy for DWRF, similar to our recommendations for the SIF.

MIF

Review and Analysis: The MIF is fully funded. The premium and loss experience of the MIF is presented below:

Marine Industry Fund - Results as of 12/31/07
Dollars in Thousands

Accident Year	Earned Premium	Earned Premium at 7/1/07 Rates	Discounted Incurred Losses as of 12/31/07
1995	1,439	1,025	1,104
1996	986	703	777
1997	777	583	390
1998	732	579	180
1999	762	604	297
2000	719	570	138
2001	701	555	17
2002	752	595	3
2003	825	653	108
2004	819	690	952
2005	799	719	-
2006	677	641	337

It can be observed that as of 12/31/07, premium has exceeded discounted incurred loss in all years from 1995 to 2006 with the exception of 2004. Rates have been reduced several times during the period displayed above, including a 10% rate decrease effective 7/1/97, a 12% rate decrease effective 7/1/05, and a 10% rate decrease effective 7/1/07.

In Oliver Wyman's 7/1/08 rate analysis for the MIF, two scenarios are presented. The first is based on the results above, using accident years 1996 to 2005. The indicated rate change using this approach is approximately -27%. A second scenario is based on accident years 2002 to 2005. This scenario results in an indicated rate change of -48%.

As a result of this analysis, Oliver Wyman notes the variability of results from year to year and recommends a rate change of 0% to -20%.

Conclusions and Recommendations: The MIF is a small fund, which presents challenges in providing rate recommendations as losses can vary significantly from year to year. Despite indications that rates have been redundant for the past several years with the exception of 2004, BWC is subject to large claims in the MIF. We believe it is appropriate to exercise prudence in reducing rates that may appear to have a degree of redundancy, given the potential for large claims relative to the annual premium volume. Thus, we believe that OW's methodology and rate recommendations for the MIF are appropriate.

The net assets of the MIF appear to be more than sufficient to meet the obligations of that fund. However, separate funds creates an obligation for the BWC to manage them, creating duplicative processes and inefficiencies. It also creates additional risks for each fund, and additional responsibilities to maintain each fund's financial strength and stability, which could be better accomplished under a combined fund. BWC does not have a process for evaluating the continued need and relevance of separate funds or for combining or closing a fund. Therefore, we recommend further research to support possible legislative change to combine the funds of BWC.

As a separate fund, we recommend the development of a funding policy for MIF, similar to our recommendations for the SIF, in particular to address the most appropriate approach to deal with a net asset level that appears to be excessive.

CWPF

Review and Analysis: The history of the CWPF is displayed below:

Coal Workers Pneumoconiosis Fund
Dollars in Thousands

Year	Assets	Liabilities	Fund Balance	Loss+LAE Reserves	Premiums
1997	141,647	43,357	98,290	34,500	264
1998	149,317	35,858	113,459	35,600	260
1999	148,102	37,043	111,059	36,782	(16)
2000	152,326	38,249	114,077	38,021	3
2001	187,512	53,271	134,241	37,026	-
2002	186,115	50,758	135,257	50,190	1,232
2003	211,290	63,398	147,891	52,600	267
2004	220,527	68,809	151,718	55,700	256
2005	224,739	63,320	161,419	57,500	824
2006	221,894	61,756	160,138	61,100	921

It can be seen that the net assets of the CWPF are generally increasing over time. This is despite the fact that the BWC has collected premium only for new employers seeking coverage from the CWPF for the past several years, and for a period of time collected no premium at all.

Oliver Wyman recommends a continuation of the practice of charging premium only to new employers, due to the relatively large net assets in the CWPF. As a result of this practice, BWC has been collecting premium that is less than the expected losses for the past several years. Estimated discounted ultimate losses for the CWPF average approximately $1.5 million each year, and as can be seen above, annual premiums are less than this. Net assets have grown despite this fact due to the investment income generated by the existing asset base, which exceeds the shortfall in annual premium accumulated over the past several years.

Recommendations and Conclusions: The OW recommendation to charge premiums less than expected losses appears to be a result of the relatively high level of net assets and associated investment income in the CWPF. We believe that this practice is understandable from the perspective of its convenience. However, while the net assets of the CWPF appear to be more than sufficient to meet the obligations of that fund, the current practice of only charging premium to new employers can create issues of equity and fairness among past current and future employers who need this coverage.

Separate funds creates an obligation for the BWC to manage them, creating duplicative processes and inefficiencies. It also creates additional risks for each fund, and additional responsibilities to maintain each fund's financial strength and stability, which could be better accomplished under a combined fund. BWC does not have a process for evaluating the continued need and relevance of separate funds or for combining or closing a fund. Therefore, we recommend further research to support possible legislative change to combine the funds of BWC.

As a separate fund, we recommend the development of a funding policy for CWPF, similar to our recommendations for the SIF, in particular to address the most appropriate approach to deal with a net asset level that appears to be excessive.

Changing of Individual Employer Rates due to Administrative Appeals or Clerical Errors by the BWC (Task #14)

Situation: BWC equates the term "employer rate" to an employer's experience modification factor, or the premium rate after the application of the experience modification factor. The industry standard for "employer rate", however, refers to the dollars of premium charged per exposure for a given classification.

Some of the adjustments that BWC's makes to an employer's experience modification factor have no time constraint or have an overly extended reporting period. This adds to the administrative burden required of the BWC staff in order to process multiple changes to employer experience.

Other monopolistic states do not make as many mid-term adjustments to experience modification; nor do the NCCI guidelines permit such practice. A significant amount of claim updates are communicated from the Claims department to the Employer Rate Adjustments Department manually rather than via BWC's IT systems.

Methodology: Given the fundamental difference in interpretation of "employer rate", we have focused its research and conclusions on events that would "trigger" the recalculation of an experience modification and ultimate premium.

Our research focuses on how BWC defines "employer rate" relative to the industry standard and the types of triggers that cause an insurer (state fund or private company as per NCCI standards) to recalculate an experience modification and ultimate premium.

In addition to researching other monopolistic states' practices and NCCI conventions, we utilized information obtained from the BWC State Fund Manual and interviews with BWC staff. We also reviewed process documentation provided in response to data requests.

Conclusions: Our major recommendations in this area are:

- Redefine the criteria for allowing mid-term experience adjustments so that the majority of such adjustments take place only once a year.
- For adjustment requests that currently have no time constraint or have an overly extended reporting period, establish shorter and clearly defined time constraints.
- Adopt the industry standard definitions for "employer rate".
- Enhance the interface between BWC's Claims system and Policy/Rating system to better automate updates to employers' experience.

Calculation of Experience Modifications for Out-of-State Employers Who Wish to Enter Ohio (Task #16)

Situation: Current language in the State Fund Manual is vague about the payroll requirements for experience rating – the current interpretation is that a company's non-Ohio payroll can qualify it for experience rating in Ohio even if the Ohio-only payroll would not ordinarily qualify the company for experience rating.

The other monopolistic states and NCCI have a premium level requirement, time in business requirement, or a combination of these two to qualify for experience rating. Ohio is the only state that uses expected losses as a requirement to qualify for experience rating.

As compared to the other monopolistic states, Ohio is the only state to use out of state payrolls and exposures to calculate an experience modification for an in-state employer.

Methodology: As part of industry benchmarking, we surveyed how the other monopolistic states calculate experience modification for Ohio risks with out of state exposure. We also surveyed the NCCI standard as that is used in many competitive states.

In addition to researching other monopolistic states' practices and NCCI conventions, we utilized information obtained from the BWC State Fund Manual and interviews with BWC staff. We also reviewed process documentation provided in response to data requests.

Conclusions: Our major recommendations in this area are:

- Utilize only the Ohio based information to determine eligibility for experience rating in Ohio (i.e., does the Ohio exposure alone qualify for experience rating).
- Adopt the industry standard of using premium level instead of expected losses as the eligibility criteria for experience rating and retain the time frame requirement. Document in the State Fund Manual the specific amount of premium required to qualify.
- Consider specific checks and balances to experience rating similar to those used in other monopolistic states such as Wyoming.

Vocational Rehabilitation Program (Task #28)

Situation: BWC offers vocational rehabilitation ("voc rehab") to workers in order to accelerate the return-to-work process and reduce lost time claim costs. Injured workers who have stabilized are referred to a field case manager. The case manager is overseen by two parties: a disability management coordinator ("DMC") from BWC, and an MCO. The DMC and MCO have the ability to authorize rehabilitation services. The role of the DMC is to oversee both the field case manager and the MCO.

Methodology: BWC provided us with the following information related to the voc rehab program:

- BWC Internal Audit report on the voc rehab program, dated October, 2007
- Monthly and rolling 12 month summary of voc rehab utilization for periods from December, 2003 to October, 2008
- A 2007 study on the impact of voc rehab on claim costs
- A description of the rules associated with the inclusion (or exclusion) of costs associated with voc rehab, such as living maintenance payments, on an employer's experience rating
- A study of the impact of these rules on the amount of losses excluded from the experience rating process

Review and Analysis: As discussed in BWC's Internal Audit report, the structure of the voc rehab program potentially creates a conflict of interest for MCO's, due to the fact that there is no restriction against MCO's referring cases to affiliated companies. This is categorized as a material weakness in the Internal Audit report.

Incentives are provided to employers to place injured employees in the voc rehab program. The rules associated with the treatment of living maintenance ("LM") payments in experience rating are shown below. LM represents payments made to an injured worker in a voc rehab program. LM payments are generally equivalent to the temporary total indemnity that the worker would receive.

Living Maintenance Reserve Reduction: Any claim where living maintenance or living maintenance wage loss is the latest type of indemnity paid, with the exception of Permanent Total Disability or Death benefits, will have its reserve reduced by half (50%).

Salary Continuation followed by Living Maintenance: Any claim where salary continuation is immediately followed by living maintenance or living maintenance wage loss, and only these two types of indemnity have been paid in the claim, will have their reserves suppressed.

Based on a study conducted by BWC in September 2007, the impact of these rules is to exclude approximately $30 million per year from the experience rating process. This amount is effectively spread to all employers through the class rating process. Thus the cost of providing incentives to employers to have their injured employees enroll in the voc rehab program is borne by all employers in the state.

BWC conducted another study in 2007 to gauge the effectiveness of the voc rehab program. Results are shown below:

CY	# Claims		Avg Med Cost/Claim		Avg Comp Amt Post Rehab	
	Successful RTW	Unsuccessful RTW	Successful RTW	Unsuccessful RTW	Successful RTW	Unsuccessful RTW
2006	1,467	2,205	$3,847	$2,190	$2,149	$6,367
2005	1,785	2,247	$5,179	$3,462	$5,066	$10,080
2004	1,913	2,095	$5,231	$3,670	$7,036	$12,763
2003	1,987	2,632	$5,099	$3,708	$7,798	$14,301
2002	3,268	4,157	$4,674	$3,636	$7,526	$17,736
2001	3,679	4,630	$4,119	$3,589	$7,959	$19,274

These results suggest that the voc rehab program has the intended effect of reducing future lost time claim costs when an employee successfully returns to work after participating in the program.

Conclusions and Recommendations: We agree with the recommendation to have sole authority for recommended rehabilitation services rest with BWC rather than the MCO's. This will mitigate conflict of interest concerns expressed by system stakeholders. In addition, it will afford BWC an opportunity to manage, track and rate voc rehab service provider performance, and leverage existing BWC voc rehab staff to eliminate existing redundancies in the authorization and referral processes between MCOs and the BWC.

We believe that offering incentives to employers to encourage their injured employees to participate in voc rehab is a reasonable practice. The incentives provided by BWC are in the form of rules related to the reduction or suppression of reserves for experience rating purposes when injured workers are receiving living maintenance in lieu of temporary total benefits. This effectively socializes the cost of this program to all employers in the state. We believe this is acceptable, particularly for a program such as voc rehab which is intended to improve the outcome for both injured workers and employers. However, we recommend that BWC make certain that the cost of this socialization is made clear to employers throughout the state, as it does not appear to be transparent based on our review of the ratemaking process.

In addition, we have previously recommended the discontinuation of the salary continuation program. To the extent that this recommendation is adopted, BWC will need to reconsider the rules associated with the treatment of living maintenance losses following salary continuation in experience rating.