BWC Board of Directors

ACTUARIAL COMMITTEE

Thursday, August 27, 2009, 2:00 P.M.
William Green Building
30 West Spring St.2nd Floor (Mezzanine)
Columbus, Ohio 43215

MEMBERS PRESENT:	Charles Bryan, Chair Jim Matesich, Vice Chair David Caldwell James Hummel Thomas Pitts William Lhota, ex officio
Members Absent:	None
Other Directors Present:	Alison Falls, Ken Haffey, James Harris, Larry Price, & Robert Smith
Counsel Present:	James Barnes, Chief Legal Counsel

CALL TO ORDER

Mr. Bryan called the meeting to order 2:00 p.m. and the roll call was taken. All members were present.

MINUTES OF JULY 29, 2009

Mr. Hummel moved to approve the minutes of July 29, 2009. Mr. Caldwell seconded the motion.

Mr. Matesich requested that the Actuarial Department provide an answer to his request on page 8 for reports on group performance and homogeneity proposals. John Pedrick, Chief Actuarial Officer, responded that his department could prepare such reports and has one in progress.

The minutes were approved by roll call vote of six ayes and no nays.

AGENDA
Mr. Caldwell moved to adopt the agenda as presented. Mr. Pitts seconded and the agenda was adopted by a roll call vote of six ayes and no nays.

ACTION ITEMS

RULES FOR FIRST READING

PUBLIC EMPLOYER TAXING DISTRICT RATE RECOMMENDATION FOR JANUARY 1, 2010, OHIO ADMINISTRATIVE CODE RULE 4123-17-34
Mr. Pedrick recommended a reduction of rates for Public Employer Taxing Districts (PECs) of 17% for the policy year January 1, 2010, to December 31, 2010. The recommendation is based upon the same desired outcomes that for private employers. BWC will reduce base rates to appropriate levels; achieve rate equity for all non-group employers, retrospectively rated employers, and group PEC entities; and improve PEC group-experience rating performance.

Oliver Wyman Actuarial Consulting, Inc. recommended a range of rate-changes, based on the 4.5% discount rate: -19.8%, baseline, -24.0% optimistic and -15.7% conservative. The rate indication table includes rate changes based on a 4.0% discount rate and shows that a 17% reduction baseline if that discount rate were used. This shows the sensitivity of investment assumptions to discount rate (expected investment return) changes.

For the January 1, 2009, rate, Oliver Wyman proposed a 14% reduction, but BWC adopted a 5% reduction. At that time, BWC had just experienced the end of a period of rising costs, so the change in the direction of cost trends was viewed as being somewhat ambiguous.

Mr. Bryan asked why the data was ambiguous. Mr. Pedrick replied that the date showed the same decrease in costs, but BWC was cautious in implementing change. In 2008, BWC did not implement the baseline indicated decrease. However, BWC now has another year of data and another year that confirms the baseline indicated change for 2008 was on target, so we conclude the decrease is appropriate. In retrospect, the 2009 rate decrease could have been 11%.

For 2010, the recommendation includes additional data, such as a decline in medical inflation. The report from Oliver Wyman shows calendar year expense, indemnity expense, medical expense, and total expense at discounted values.

If BWC were to set the pure premium at the recommended rate of $1.24 per $100, the baseline reduction would be -19.8%. The proposed overall rate is $1.29. First, the recommendation is close to the conservative end of the range, assuming the current trends. The decline in frequency is partly a result of economic decline. At the end of the recession, there may be an increase in costs, supporting our recommendation to target costs above the baseline indication. Oliver Wyman also sets forth data showing the actual costs, and uses a regression analysis to find a model and departures from the model. The standard deviation is .0645.

Ms. Falls asked: If given the rate decrease that had been left on the table, should not the Workers' Compensation Board expect a rate decrease of more than 20%. Mr. Pedrick replied the 2010 recommendation incorporates the actual change from last year as the starting point. Had BWC decreased rates by 14% in 2009, then the 2010 recommendation would be lower.

Mr. Harris asked if the Workers' Compensation Board had discussed last year's recommendation in terms of "leaving part of the recommended decrease on the table." Mr. Pedrick replied BWC did not present that recommendation with that intention. BWC conservatively reviewed the 2009 rate indications. In 2009, a 14% decrease seemed too large in light of the reasonable anticipation of an increase in costs. BWC saw a "large negative indication" and deemed it prudent not to fully implement it.

Mr. Matesich stated that if recent years' rates are compared, most are minor percentage changes up or down. He asked should not BWC continue to be conservative. Mr. Pedrick replied that last year BWC was concerned about doing a large decrease, and then facing this year with a recommendation to make a large increase. A -17% decrease for 2010 means that BWC may adopt no change for 2011 if expenses increase. We had a similar discussion concerning private employers' rates.

Concerning historic data, Mr. Matesich asked were the prior years' analyses similar. Elizabeth Bravender, Actuarial Director, replied that she could affirm that a similar approach was taken under Administrators James Conrad and Bill Mabe. They always recommended a premium change within the indicated range.

Mr. Pitts asked since the rate indication trend shows a decrease, should not the recommendation for PEC be greater because of local government revenue concerns. Mr. Pedrick replied that this approach also considers the general state of the economy. The recommended change lowers the possibility of a need to increase rates next year.

Mr. Hummel asked to clarify the prediction that there will be no increase in 2011. Mr. Pedrick replied that at this time he expects 2011 to have an overall "no change" because the 19.8% indication for 2010 is based on reasonable, optimistic assumptions.

Mr. Pedrick reported further that non-group employers will benefit from the entirety of the rate reduction while the rate reduction for group rate employers will be limited by the break-even factor. The goal is to achieve rate equity by setting the rate structure to reach the relative rate levels of 1.10 for non-group and 0.70 for group and eliminate the impact of group discounts on base rates by establishing a uniform off-balance factor for all PEC manual classes at 1.01. Mr. Bryan clarified that the current off-balance factor is the multiplier to reach the equitable rate. Mr. Pedrick further reported that applying the break-even factors by discount level improved equity and allowed group formation at all levels. The impact of rate reform changes will be that: non-group will decline -24.6% and group by -4.7%. The PowerPoint chart on page 12 has errors on base rates and Directors should refer to the " DRAFT" hand-out distributed today for correct ones.

Mr. Bryan stated that questions on the presentation should be directed to Don Berno, Board Liaison, or Mr. Pedrick.

Mr. Harris agreed that BWC may want to consider a greater decrease for PECs because of current financial pressures, however, 2010 is an election year and there will be even greater political pressures on PECs to not raise taxes to pay for increased workers' compensation premiums.

ANNUITY FACTORS, OHIO ADMINISTRATIVE CODE RULE 4123-17-60

Mr. Pedrick recommended amending of Ohio Administrative Code Rule 4123-17-60 to revise the annuity tables to accommodate the change of the discount rate from 5% to 4.5%. The tables are based on a 2001 mortality study. Deloitte Consulting will undertake a new mortality study as the new actuarial consultant for BWC.

Mr. Bryan asked how the tables are used. Mr. Pedrick replied that they are used mostly for case reserving and MIRA 2. The tables are not determinative for lump-sum settlements, because lump-sum settlements use several other factors in assessing the amount of settlement to offer.

Mr. Pedrick stated that after approval by the Workers' Compensation Board, Fair Isaac will apply the amount from the new annuity tables to MIRA 2.

Marsha Ryan, BWC Administrator, added that each lump-sum settlement involves a standalone analysis of future costs and involves more than just the reserve.

Mr. Bryan asked if any member of the Actuarial Committee had any objections to waiving the procedure of a first and second reading of the proposal before taking action. Hearing none, he requested a motion.

Mr. Pitts moved that the Actuarial Committee recommend that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendation to amend Rule 4123-17-60 of the Administrative Code, Annuity Factors. The motion consents to the Administrator amending the rule as presented here today. Mr. Matesich seconded and the motion was approved by a roll call vote of six ayes and no nays.

PUBLIC EMPLOYER TAXING DISTRICT RETROSPECTIVE RATING, OHIO ADMINISTRATIVE CODE RULES 4123-17-42 AND 4123-17-42.1-FIRST READING

Tina Kielmeyer, Chief of Customer Service, presented a new rule setting forth different criteria for retrospective rating for PECs. The Deloitte Study found that only 400 employers had participated in retrospective rating policies in the past ten years, but of those 100 were PECs. Deloitte recommends changes to bring in more public sector employers and lower the minimum premium, which is higher than comparative states and insurers.

BWC recommends revising Ohio Administrative Code Rule 4123-17-42 to clean-up language and make it applicable only to private employers. The language is clarified requiring financial statements prepared in accordance with Generally Accepted Accounting Principles (GAAP) and a paragraph is stricken which applied to the program transition of 1997. BWC will look at all requirements of retrospective rating as part of a product review and bring all rules back to the Actuarial Committee and the Workers' Compensation Board at a later time.

For PECs, BWC proposes Rule 4123-17-42.1, which creates a two-tier program in which applicants for both tiers are required to have active coverage, current premiums and audit findings, less than fifteen days of lapse in the previous five years, and a minimum premium size. Tier 1 employers must have greater financial strength, while Tier 2 employers must be able to cover claims losses and remain financially viable. Financial statements for Tier 1 must be GAAP financial statements, whereas Tier 2 financial statements should be GAAP, but BWC will accept financials that comply with the Auditor of State minimum requirements. An employer in Tier 1 cannot be under a fiscal watch or emergency, but Tier 2 employers under fiscal watch or emergency are eligible. Tier 1 employers must have an "approved program of choice" for safety; Tier 2 employers must follow the Ten-Step Business Program. A Tier 1 employer cannot have a part-pay agreement within three years, but a Tier 2 employer remains eligible.

Mr. Bryan asked if the Ten-Step Program must be implemented over two years. Ms. Kielmeyer replied that it will have similar implementation requirements as the prior policy.

Ms. Kielmeyer further reported that BWC has taken the proposal to stakeholders and received three comments. First, stakeholders objected because the lapses for applicants are shorter than for other programs. BWC is currently evaluating this objection. Second, stakeholders objected that employers in Tier 1 cannot be under a fiscal watch or emergency. However, again, employers would still be eligible for Tier 2. Third, employers cannot be in Tier 1 if they entered into a part-pay agreement for the past three years. However, they may still be in Tier 2.

Mr. Matesich observed that the requirements for Tier 1 are stronger than Tier 2, yet BWC is asking for GAAP financial statements. This seems counter-intuitive. Ms. Kielmeyer replied that the greatest reason for denial of PEC applicants was lack of GAAP financial statements. Mr. Haffey added that the distinction lies in the additional cost of a GAAP audit, although smaller entities should probably have greater scrutiny.

PUBLIC EMPLOYER GROUP RETROSPECTIVE RATING—APPLICATION DEADLINE CHANGE, OHIO ADMINISTRATIVE CODE RULE 4123-17-73

Joy Bush, Product Development Director, recommended amendment of Ohio Administrative Code Rule 4123-17-73 to change group retrospective rating application deadlines for PECs from the last Friday in September to December 31. The Workers' Compensation Board is still discussing the application of the break-even factors. Market acceptance for the product is strong.

Mr. Pitts asked to verify the changes are for only one year and Ms. Bush confirmed that they were just for this year.

Mr. Bryan asked if there were any objections to waiving the first-reading and approving the recommendation of BWC. Hearing none, he requested a motion.

Mr. Matesich moved that the Actuarial Committee recommend that the Bureau of Workers' Compensation Board of Directors approve the Administrator’s recommendations to amend Rule 4123-17-73 of the Administrative Code, Group Retrospective Rating, to change the application deadline for public employer group retrospective rating. The motion consents to the Administrator amending the rule as presented here today. Mr. Hummel seconded and the motion was approved by a roll call vote of six ayes and no nays.

PEC APPLICATION FOR GROUP EXPERIENCE RATING, OHIO ADMINISTRATIVE CODE RULE 4123-17-62

Mr. Pedrick recommended amendment of Ohio Administrative Code Rule 4123-17-62 based on feedback from sponsors. The rule had been approved by the Workers' Compensation Board in July for deadlines of August 14 and August 28 for group sponsor notification to members and group roster filing with BWC, respectively. BWC now requests change to September 28 and October 9. Rate reform has resulted in many changes; some affect some stakeholders in ways not anticipated when enacted. Ms. Falls asked what does this teach us about the rule development process. Mr. Pedrick responded that while we seek to address reasonable concerns from interested parties, we need to cross check changes to ensure there are not unintended consequences in other rules.

Mr. Price commended BWC for being responsive to stakeholder comments.

Mr. Bryan asked if there were any objections to waiving the first-reading and approving the recommendation of BWC for presentation to the Board. Hearing none, he requested a motion.

Mr. Hummel moved that the Actuarial Committee recommend that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendations to amend Rule 4123-17-62 of the Administrative Code, "Application for Group Experience Rating." The motion consents to the Administrator amending the Rule as presented here today. Mr. Pitts seconded and the motion was approved by a roll call vote of six ayes and no nays.

DISCUSSION ITEMS

RESERVE AUDIT UPDATE

Jeffery Scholl, Principal, Oliver Wyman, and Zia Rehman, Director of Actuarial Analysis, reported on the actuarial reserve audit. Mr. Scholl reported that the original audit used data as of March 31. Since then, Oliver Wyman has used data from June 30 to true-up the audit. In March, the discounted unpaid liability was calculated at $19,289 million; as of June 30, it is $19,245 million. Medical payments and lump-sum settlements are the two biggest factors in the change. Noteworthy among re-estimates of past years, the 2002 year was originally estimated at $13,572 million, but is now estimated at $11,174 million at the same time period. After removal of the discount rate, the re-estimate for 2002 is $19,384 million.

The three highlights of the audit are as follows. First, the State Insurance Fund liability estimate is slightly lower. The principal reason is the decline in the medical inflation assumptions and the decrease in the discount rate from 5% to 4.5%. Second, there is lower medical liability. Third, the lump sum settlement payments were lower in the fourth quarter than in recent prior years.

Mr. Scholl further reported that the peak in medical payments occurred in 2002. After some decline, the payments have been flat for the last seven quarters. Claims losses have been in decline. Lump-sum settlements peaked in 2007. Mr.

Bryan commented there has been a separate lump-sum settlement reserve to segregate its effects and evaluate later injuries. Mr. Scholl further reported when comparing BWC with country-wide performance, the annual trend on medical severity is similar.

Mr. Pitts asked if the countrywide trend comparison includes lump-sum settlements. Mr. Scholl replied that he believed it did, but would research that issue. Country-wide the BWC indemnity payments show greater severity, but the trend is similar. There is a decrease in lost-time frequency country-wide.

Mr. Pedrick reported that the material includes an opinion letter from Mr. Scholl and Jeffery Scott, Principal, Oliver Wyman, and a letter from Mr. Pedrick of August 25. In addition, the Enterprise Report will continue to use the figures already reported for June 30 until the external audit is finished.

Mr. Rehman reported on the reserve reconciliation from June 30, 2008, to June 30, 2009. The report excludes the Health Partnership Program (HPP) and pre-1987 self-insured claims expense. The total as of 2008 was $14,838 million. Adjustments were made for one year's reserve release, investment income, the impact of medical inflation and loss development changes, the impact of the discount rate change, and an additional accident year's reserves. The total has decreased to $14,584 million. Mr. Bryan asked what the effect of the reconciliation for case reserves is. Mr. Rehman replied there was no affect.

MIRA 2 UPDATE

Mr. Bryan tabled the MIRA 2 update to the September meeting.

UPDATE ON COMPREHENSIVE RATE REFORM

Mr. Pedrick reported on progress in comprehensive rate reform. Reform included substantial outreach to stakeholders and was more challenging than originally thought. First, there were unplanned interruptions. Second, there were challenges to development of realistic solutions.

An example of unplanned interruptions was the construction contractor rate modification. Also, based on incomplete information, there were some calls to action going to the General Assembly before BWC was contacted to clarify its actions and proposals. An example of an unplanned good interruption was the PEC break-even factor. It became necessary to change our approach from computing a factor for each manual to a stratified table of factors that apply to group experience modifiers, which helps to achieve greater equity.

Examples of challenges to develop programs were the two group rating options, with a new one for group retrospective rating. These are meant to be sustainable group programs. With respect to reform of group rating, BWC would like to formulate a proposal in September, but it may not be ready. Proposals under consideration would provide for a bigger credit if group sponsors maintained membership continuity. Working out details has delayed formulation because a credit for continuity would require maintaining the break-even factors. Another proposal is that members of a group get a fixed discount, applied to their individually determined rates, so that the experience rating change of one employer does not affect the others. Group sponsors would then no longer need to move participants in and out of the group. The BWC is sometimes meeting twice per week with interested parties to work on proposals.

CHIEF ACTUARY REPORT

Mr. Pedrick reported there was a new hire in the Actuarial Division: Jon Turnes, Reserving Actuary, who is a Fellow in the Casualty Actuarial Society and a Member of the American Academy of Actuaries. He formerly worked for Swiss Re as a reserving actuary. He has a Bachelor of Science degree in mathematics and a Bachelor of Arts degree in economics from the University of Maryland.

Mr. Matesich stated that he was eager to discuss group changes in September. Mr. Pedrick replied that he was optimistic that proposals would be available for a first reading.

COMMITTEE CALENDAR

There was no discussion of the Actuarial Committee calendar.

EXECUTIVE SESSION—LITIGATION UPDATE

There was no litigation update and no executive session.

ADJOURNMENT

Mr. Matesich moved to adjourn. Mr. Hummel seconded and Mr. Bryan adjourned the meeting at 4:02 pm after the motion was approved by roll call vote of six ayes and no nays.

Prepared by: Larry Rhodebeck, Staff Counsel
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September 2, 2009