BWC Board of Directors

ACTUARIAL COMMITTEE

Thursday, August 26, 2010, 3:12 P.M.
William Green Building
30 West Spring St. 2nd Floor (Mezzanine)
Columbus, Ohio 43215

Members Present:	Charles Bryan, Chair David Caldwell James Hummel Thomas Pitts William Lhota, ex officio
Members Absent:	Jim Matesich
Other Directors Present:	Alison Falls, Kenneth Haffey, James Harris, Larry Price, and Bob Smith
Counsel present:	Thomas Sico, Associate General Counsel Ann Shannon, Legal Counsel

Staff present: John Pedrick, FCAS, MAAA, Chief Actuarial Officer (a number of other staff were present as well)

Consultant present:	Jan Lommele, FCAS, MAAA, FCA, Deloitte Consulting, LLP and additional Deloitte staff.
Scribe:	Larry Rhodebeck, Staff Counsel

CALL TO ORDER

Mr. Bryan called the meeting to order at 3:12 p.m. and the roll call was taken. Mr. Bryan reported that Mr. Matesich would not be present.

MINUTES OF JULY 26, 2010

Mr. Caldwell moved to approve the minutes of July 26, 2010. Mr. Pitts seconded and the minutes were approved by a roll call vote of five ayes and no nays.

AGENDA

Mr. Caldwell moved to adopt the agenda. Mr. Hummel seconded and the agenda was adopted by a roll call vote of five ayes and no nays.

NEW BUSINESS/ACTION ITEMS

SECOND READING: PUBLIC EMPLOYER TAXING DISTRICTS DEDUCTIBLE TABLES, OHIO ADMINISTRATIVE CODE RULE 4123-17-72

John Pedrick, Chief Actuarial Officer, recommended amendment of Ohio Administrative Code Rule 4123-17-72 to add revised deductible tables for public employer taxing districts (PEC) and to make editorial changes. Reference was made in the presentation to the executive summary, "Deductible Program Rule Changes," of August 26, 2010. Mr. Pedrick was assisted by John Turnes, Manager of Reserving; Joy Bush, Program Development Director; and Dave Heppen, Deloitte Consulting, LLP. Mr. Pedrick briefly described the proposed changes. The PEC large deductible table, Appendix F, incorporates the revised analysis by BWC with Deloitte's assistance. When BWC developed these PEC large deducible tables, it was also necessary to modify Appendix B, the PEC small deductible table. Appendix C displays the hazard groups assigned to each manual class and now incorporates changes made by the National Council on Compensation Insurance (NCCI) which were adopted by the board at a prior meeting. Based on comments from the last meeting, Appendix D tables include more explicit headings. Appendix F was also changed from the version shown last month with the addition of one decimal point for the deductible credits.

Mr. Bryan asked which of the actuaries who worked on the PEC large deductible tables can attest to its actuarial soundness. Mr. Turnes replied that because he had developed the tables, it was his opinion that the program was actuarially sound. Mr. Heppen replied that he had reviewed the process and discussed it at length with Mr. Pedrick and Mr. Turnes; it was his opinion that the program was actuarially sound.

Mr. Bryan requested that the words "Hazard Group" be added over the appropriate columns in Appendices A and B. Mr. Pedrick replied that he was submitting it to the Actuarial Committee with that change.

Mr. Bryan asked if the actuarial analysis was available to all Actuarial Committee members and Mr. Pedrick affirmed that it was. Further, Mr. Pedrick stated that the PEC tables must be approved this month so PEC employers may consider large deductibles during the two-month enrollment period which starts September 1. BWC would now start a three-year analytical cycle of program implementation, observing its performance, and proposing adjustments.

Mr. Hummel moved that the Actuarial Committee recommend that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendation to amend Rule 4123-17-72 of the Administrative Code, "Deductible Rule," to make changes to appendices to the rule. Mr. Caldwell seconded and the motion was approved by a roll call vote of five ayes and no nays.

SECOND READING, PRIVATE EMPLOYER CREDIBILITY TABLE EFFECTIVE JULY 1, 2011, OHIO ADMINISTRATIVE CODE RULE 4123-17-05.1

Mr. Pedrick, Mr. Turnes, and Mr. Heppen recommended amendment of Ohio Administrative Code Rule 4123-17-05.1, the private employer credibility table, to be effective July 1, 2011. Reference is made to the executive summary, "Private Employers Credibility Table Used for Experience Rating" of July 13, 2010. Mr. Pedrick stated that adoption would bring certainty concerning the factors to be used for the policy year beginning July 1, 2011 to third party administrators, group sponsors, and employers contemplating group rating. The rule retains the 65% maximum credibility rate used for the policy year beginning July 1, 2010.

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 4123-17-05.1 of the Administrative Code, "Private Employer Credibility Table Used for Experience Rating." The motion consents to the amendment of Rule 4123-17-05.1 effective July 1, 2011, as presented here today.

SECOND READING, GROUP BREAK EVEN FACTOR, OHIO ADMINISTRATIVE CODE RULE 4123-17-64.1

Mr. Pedrick recommended approval of Administrative Code Rule 4123-17-64.1 regarding break-even factors for private employers, also effective July 1, 2011. Reference was made to the executive summary, "Private Employer Break-Even Factor" of July 13, 2010.

Mr. Caldwell moved that the Actuarial Committee recommend that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendations to adopt Rule 4123-17-64.1 of the Administrative Code, "Private Employer Group Experience Break Even factors." The rule establishes break even factors to be applied to group rating experience modifications for private employers effective July 1, 2011. 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 five ayes and no nays.

FIRST READING, PROGRAM COMPATIBILITY RULE CHANGES AND RULE CLEAN-UP, OHIO ADMINISTRATIVE CODE RULE CHAPTER 4123-17 AND RULE 4123-17-74

Tom Prunte, Executive Director, Employer Management Services and Ron Suttles, Supervisor of Employer Programs recommended amendment of several rules of Ohio Administrative Code Chapter 4123-17 and enactment of new rule 4123-17-74. Reference was made to the executive summary, " OAC Chapter 4123-17 Employer Program Rule Revisions," of August 12, 2010. Mr. Prunte stated that this was a first reading. The changes are proposed to enhance simplicity and ease of use. The changes are made with the goal of achieving clarification and standardization. Stakeholder input has been sought and continues to be submitted. So far, comments have been favorable. A complete report of stakeholder input will be submitted at the second reading. The table at the front of the executive summary sets forth the changes.

Mr. Suttles reported on specific changes. Rule 4123-17-41 adds language that Rules 4123-17-41 to 4123-17-54 apply to individual employer retrospective rating.
BWC added language to Rule 4123-17-42 to include eligibility requirements for PECs; requiring that the employer's policy be in active status as of the application deadline, rather than on the first day of the policy year; allowing BWC to remove the employer from the program if the employer fails to implement the ten-step business program for safety; and to remove current language requiring employers to meet with representatives quarterly. The latter was removed because many employers in the ten-step safety program meet more frequently with BWC representatives.

Mr. Bryan asked if the Division of Safety and Hygiene supported the change and Mr. Suttles responded that it did.

Rule 4123-17-42.1 is rescinded because the requirements for PECs have been combined into Rule 4123-17-41. BWC removed language from Rule 4123-17-43 that a retro rating program is optional and adds language requiring that all information must be filed by the application deadline. Rule 4123-17-67 concerns representation for group experience rating and has a typographical correction to reflect the employer is to submit form AC-24. Rule 4123-1-71 concerns the one-claim program and changes the requirement to attend Workers' Compensation University to six hours of BWC approved training. WCU is no longer a program and its instruction has been rolled into the Ohio Safety Congress & Expo.

Mr. Bryan asked if the one-claim program is important now that rate stability has improved. Mr. Suttles replied that 1,860 employers currently participate in the program. Mr. Pedrick added that the one-claim program applies an experience modifier of 0.60 for a 40% discount, which made sense when group experience modifiers were as low as 0.95. With the maximum group discount now at 51%, the one-claim discount structure and rationale requires a review.

Mr. Bryan then requested that BWC develop a recommendation on the one-claim program even if there is a statutory change required. Mr. Prunte added that removal of the one-claim program was part of the Deloitte HB100 Report and on the schedule for review in 2011.
Mr. Suttles concluded that the number of allowed lapse days is changed from 59 within an 18 month period to 40 days within a 12 month period.

Mr. Prunte reported that Ohio Administrative Code Rule 4123-17-74 was being proposed to capture all deadlines and compatibility information of six chapter 4123-17 rules. These are summarized on page 52 of the executive summary. The rule itself incorporates three appendices. Appendices A and B consolidate private and public employer program application deadlines while Appendix C is the compatibility table.
Mr. Harris remarked that Rule 4123-17-74 will be helpful to employers with stacking of programs. Mr. Pedrick added that Employer Management and Customer Services staff, along with all those who develop and manage these various programs, put a significant effort into proposing the revisions that are straight-forward and easy to use.

DISCUSSION ITEMS

FINAL RESERVE AUDIT AS OF JUNE 30, 2010, AND QUARTERLY RESERVE TRUE-UP FOR FINANCIAL REPORTING FOR FISCAL YEAR ENDING JUNE 30, 2010 AND UPDATED ESTIMATE FOR FISCAL YEAR ENDING JUNE 30, 2011, BASED ON DATA AS OF JUNE 30, 2010

Bill Van Dyke, Dave Heppen, Jan Lommele, and Bob Miccolis, Deloitte Consulting LLP, presented the final reserve audit for June 30, 2010. Reference was made to the report, "Ohio Bureau of Workers' Compensation June 30, 2010, Reserve Analysis" of August 26, 2010. Also participating were Mr. Pedrick and Mr. Turnes.
Mr. Van Dyke reported that the presentation included the purpose and scope of the report; the process; the updated unpaid estimates as of June 30, 2010; changes in unpaid estimates from fiscal year 2009 recorded reserve; changes in unpaid estimates from March 31, 2010 evaluation; and the funding ratio.

Mr. Van Dyke reported that Deloitte Consulting has been retained by BWC to determine an actuarial analysis of a central estimate of the unpaid loss and loss adjustment expense as of June 30, 2010, using data as of that date. The determination concerns both nominal and discounted losses for the State Insurance Fund, the Disabled Workers' Relief Fund (DWRF), Coal-Workers Pneumoconiosis Fund (CWPF), Self-Insuring Employers' Guaranty Fund (SIEGF), Marine Industry Fund (MIF), Public Work-Relief Employees Compensation Fund (PWREF); and Administrative Cost Fund (ACF). The actuarial process to estimate discounted unpaid loss involves calculation of ultimate loss estimates based on actuarial methodologies. Ultimate loss equals paid loss, plus MIRA case reserves plus incurred but not reported (IBNR) reserves. The nominal unpaid loss estimate as of June 30, 2010 equals estimated ultimate losses less payments through June 30. The discounted unpaid loss estimate is the nominal unpaid loss estimate, less estimated future investment income on the reserves at a 4% discount rate.

The June 30, 2010, estimate of unpaid loss and loss adjustment expense (LAE) is based on the estimate using data through March 31, 2010, incorporating additional data evaluated as of June 30, 2010, and considering actual versus expected payments during the fourth quarter of fiscal year 2010. There are no changes in methodology from the March 31, 2010, evaluation. There are updated parameters for new fiscal year 2010 estimates which use fourth quarter experience data. The prior report used nine months of data, whereas the current report uses twelve months of data. The nominal unpaid loss and LAE for all funds is $32.2 billion and the discounted unpaid loss and LAE at a 4% discount rate is $19.8 billion dollars. The three largest of the funds responsible for the unpaid loss and LAE are the State Insurance Fund (79.16%), DWRF (10.32%), and the ACF (5.61%). The discounted unpaid estimates anticipate $12.4 billion of future income earned on invested funds or collected in premium assessments for unfunded liabilities in order to provide sufficient funds to make all future claim payments associated with claims occurring on or before June 30, 2010.

Mr. Smith asked what would happen to these estimates if Ohio were to adopt a competitive State Insurance Fund. Mr. Van Dyke replied that if a competitive State Insurance Fund were not allowed to discount, it would need $8 to $9 billion in additional funding. Mr. Miccolis added that some states permit their state insurance funds to discount their reserves by statute. Mr. Bryan stated that if BWC were to enter a run-off process, it would still need assets. Mr. Pedrick explained that BWC would need to post reserves close in value to the undiscounted estimate of $32.2 billion, to collect the full amount of accrued premiums of approximately $4.6 billion and to collect funds to cover the ACF reserve estimate of $1.1 billion which is not offset by a premium receivable in our financial statement. In addition BWC could be required to meet risk based capital requirements under statutory accounting standards. The magnitude of the additional funds that would be needed by the system could be $20 billion or more. Mr. Lommele stated that the State of Maryland made changes to its State Insurance Fund and collected additional premiums from employers. Mr. Pedrick stated that BWC collects $2 billion per year now, and while the $20 billion figure is not based on thorough analysis and is very rough, it represents ten years premiums. Mr. Bryan cautioned participants about discussing specific percentages and dollar amounts without significant actuarial analysis since these types of numbers include complex assumptions.

Mr. Van Dyke further reported on the changes in the unpaid loss and LAE reserve estimates. The recorded reserves for all funds as of June 30, 2010, are $19.8 billion dollars; as of June 30, 2009, the comparable figure was $19.2 billion. The 2010 estimated reserves are approximately $559 million, or 2.9% higher than the 2009 recorded reserves. The difference is the result of $1.7 billion in new claims, plus $843 million in interest accretion, less $627 million in estimated prior year's loss and LAE change, plus $934 million due to the change in the discount rate, and less fiscal year 2010 loss and LAE payments.

Mr. Bryan asked if the $19.8 billion reserve will be carried on the fiscal year 2010 balance sheet presented to the Board by Tracy Valentino and Mr. Van Dyke confirmed it would be. Mr. Heppen commented that the change of the discount rate from 4.5% to 4% made a large impact on the reserve. Otherwise, the reserve would have declined, based on the other factors in its calculation.

Mr. Van Dyke continued that the retrospective unpaid loss and LAE reserve estimate using data through June 30, 2010 of $18.6 billion is $627 million or 3% lower than the fiscal year ending 2009 recorded reserves of $19.2 billion.

Mr. Bryan asked if fiscal year 2009 reserves may be considered overstated. Mr. Van Dyke replied they were not overstated because it is the reduction in claims which also drives the increase. Mr. Van Dyke continued that most of the change is driven by the State Insurance Fund, with the retrospective estimates of four of the remaining funds being similar to the fiscal year ending 2009 recorded reserves. The SIEGF increase of $42 million is a result of a higher SIEGF DWRF estimate, partially offset by a lower SIEGF loss estimate. Also, the ACF decrease of $52 million is driven by lower employer estimates and a reduction in the paid LAE to paid loss ratio used in the estimate of loss adjustment expense reserves embedded in the ACF.

With respect to a retrospective comparison of unpaid loss and LAE specific to the State Insurance Fund, the combined effect of private employers (-$378 million), public employer taxing districts (-$239 million), and public employer state agencies (PES) (-$140 million) decreased by $757 million primarily due to lower medical estimates. This reduction in medical estimates is based on continuation of lower frequency in recent injury years and reliance on historical BWC medical inflation. The self-insured surplus fund decrease of $26 million is primarily from an increase in the expected recovery rate from surety bonds from 15% to 35%. The Health Partnership Program (HPP) increase of $146 million is from an increase in the paid LAE to paid loss ratio in the fourth quarter, based on fiscal year 2010 experience and from an increase from 0% to 15% for the assumed HPP expense

associated with unreported claims. The Private employer and the PEC decreases were also driven by the decrease in the inflation assumption, using historical rates.
Mr. Bryan asked what if there was an increase in medical inflation. Mr. Van Dyke replied that Deloitte would only change its recommended inflation factor if there were a sustained increase.

Mr. Smith added that the prior consultant used a medical inflation rate from 8% to 9%, which the Actuarial Committee questioned. Mr. Van Dyke added that the NCCI sees 3-4%; recent Consumer Price Index inflation is 3-5%. A 9% medical inflation assumption is warranted only if there is high general inflation and there are higher interest rates. Mr. Lommele commented there are many moving parts. Mr. Miccolis added that this also impacts consideration of the funding ratio.

Mr. Van Dyke also reported regarding the change in unpaid estimates from March 31, 2010. The nominal unpaid loss and LAE as of June 30 is a $49 million decline compared to using March data. The discounted unpaid estimate of $19.8 billion is $43 million or 0.2% lower than the prior discounted unpaid estimate based on data as of March 31, which is driven by change in the State Insurance Fund. There is little change in the other funds. The change in the State Insurance Fund unpaid estimate is driven by a reduction in private employers of $75 million partially offset by an increase of $37 million for the HPP. The HPP increase is from an increase in the paid LAE to paid LSS ratio based on recent experience.

The total resulting from the drivers of the change in the State Insurance Fund is a $79 million decline. This is a decrease of $39 million in the ultimate losses from lower 2010 payroll projections. There is a decrease of $35 million in the ultimate losses from actual payments lower than expected for the fourth quarter of fiscal year 2010. Updates of certain parameters led to a further decrease of $70 million in the ultimate losses. This was mostly due to declines in payments for temporary total disability (TTD) and permanent total disability (PTD). Offsetting the $144 million decrease in the ultimate losses is an increase of $38 million due to fewer payments than anticipated in the March 31 analysis and $27 million in discount since the ultimate losses decreased.

For DWRF, CWPF, SIEGF, and ACF funds, the current June 30, 2010, discounted unpaid estimate of approximately $4.1 billion decreased by only $1 million from the March 31, 2010, evaluation based on new experience data in the fourth quarter of fiscal year 2010. There are no changes in methodology or significant changes in assumptions since the March 31, 2010, evaluation for these funds.

The BWC funding ratio guidelines are a range between 1.15 and 1.35. For fiscal year 2009, the BWC funding ratio was 1.15 and the draft for fiscal year 2010 is 1.22 and in the recommended range. In the HB100 Comprehensive Study, Deloitte recommended a funding ratio between 1.2 and 1.5; the Deloitte estimate for fiscal year 2010 is 1.

Mr. Van Dyke concluded the presentation by mentioning that the full supporting report is in five volumes available to the Workers' Compensation Board on disk or in hard copy. Each of the Board members was given a disk.

Mr. Bryan stated that in 2009, the Workers' Compensation Board received an actuarial opinion from the BWC consultant. Mr. Lommele responded that Deloitte has begun discussion on a statutory opinion format, although one is not required for BWC.

Ms. Falls asked why the Deloitte HB100 had recommended a funding ratio of 1.5, versus the 1.35 upper range adopted by the Workers' Compensation Board. Mr. Lommele responded that Deloitte believed 1.5 was a better number based on stochastic analysis and the historic variability of the insurance industry. Ms. Falls further asked if reinsurance would change that recommendation. Mr. Lommele responded that reinsurance is not significant enough to make a material change. Mr. Miccolis added that there would need to be a three year experience to reach materiality.

LEGISLATIVE DISCUSSION AND ANALYSIS

There was no discussion of pending legislation.

CHIEF ACTUARY REPORT

Mr. Pedrick reported that page 1 of his report summarized the activities presented today. Page 4 added the base rate analysis and PEC rates. He added that in the earlier conversation regarding the changes required if BWC were to adopt statutory accounting, he mentioned broad estimated figures and that a careful and full analysis would be needed.

COMMITTEE CALENDAR

Mr. Bryan asked where the rate stability study is on the calendar. Mr. Pedrick replied it would be presented in early 2011, but is not yet on the calendar. BWC is looking at plans to recommend short-term changes and long-term (system) changes. Mr. Bryan requested that the issue be placed on the agenda of the January meeting.

EXECUTIVE SESSION

Mr. Bryan reported there was an executive session during the Audit Committee meeting, so there would be none needed for the Actuarial Committee.

ADJOURNMENT

Mr. Hummel moved to adjourn. Mr. Caldwell seconded and Mr. Bryan adjourned the meeting after a unanimous roll call vote.

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August 31, 2010