

BWC Board of Directors

BOARD MEETING

Friday, January 22, 2010, 8:00 A.M.

William Green Building

30 West Spring St. 2nd Floor (Mezzanine)

Columbus, Ohio 43215

Members Present: William Lhota, Chair
James Harris, Vice Chair
Charles Bryan
David Caldwell
Alison Falls
Ken Haffey
James Hummel
Jim Matesich
Thomas Pitts
Larry Price
Robert Smith

Members Absent: None

Counsel Present: John Williams, Assistant Attorney General
Fiduciary Counsel Present: Ronald O'Keefe, Hahn, Loeser, & Parks, LLP

CALL TO ORDER

Mr. Lhota called the meeting to order at 8:00 a.m. and the roll call was taken.

MINUTES OF DECEMBER 17, 2009 MEETING

Mr. Bryan moved to approve the December 17, 2009, minutes. Mr. Haffey seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

AGENDA

Mr. Lhota added an action item to the Investment Committee report on the allocation of Disabled Workers Relief Fund (DWRP). He reserved the right to recess the meeting at an appropriate time, if needed.

Mr. Bryan moved to adopt the agenda as amended. Mr. Matesich seconded and the amended agenda was adopted by a roll call vote of eleven ayes and no nays.

CHAIRMAN'S COMMENTS

Mr. Lhota announced that the financial disclosure forms from the Ohio Ethics Commission have been mailed to all directors and must be filed on April 15. Anyone needing assistance should contact Don Berno, Board Liaison.

Mr. Lhota reported that there was excellent attendance by directors at the four committee meetings of January 21. Of forty-four opportunities for participation, there were forty-three directors in full or partial attendance, a participation rate of 98%. Mr. Lhota also reported that this is the thirtieth meeting of the Workers' Compensation Board. All 11 Directors have been present for 20 of those meetings; at just one Board meeting were ten directors were present and voting.

COMMITTEE REPORTS OF JANUARY 21

ACTUARIAL COMMITTEE

Mr. Bryan reported that there was one action item, the approval of the Large Deductible Program for deductibles of \$25,000 and higher. Employers will have more flexibility to structure their workers' compensation programs to assume more risk if they desire. BWC will handle all claims and the employer pays up to the deductible amount. Adoption of the large deductible program could affect BWC reserve levels. A change from the proposal as made in December is the addition of a stop-loss option so an employer will not be paying more than three times the chosen deductible level.

Upon the recommendation of the Actuarial Committee, Mr. Bryan moved that the Bureau of Workers' Compensation Board of Directors approve the Administrator's Recommendation to amend Rule 4123-17-72 of Administrative Code, "Deductible Rule," to create a Large Deductible Program. The motion consents to the Administrator amending Rule 4123-17-72 as presented at the Actuarial Committee. Mr. Caldwell seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

Mr. Bryan further reported there was a first reading on an amendment to the experience modifier cap rule. The presentation was from Terry Potts, Rates Supervisor, Actuarial Division. The proposal will have a second reading and possible vote at the February meeting. The amendment deletes reference to specific years for application of the cap and allows application in future years.

Among the discussion items was an education session on reserves by John Turnes, Actuarial Analysis Reserving Manager. The Committee now has completed a thorough review of the different methods and judgments involved in the development of reserves. There is a high interest in reserves because of the change of the BWC actuarial consultant from Oliver Wyman Consulting to Deloitte Consulting.

The Actuarial Committee also received a quarterly update from BWC staff on implementation of the HB100 Study. The Committee is monitoring the progress of implementing the recommendations, and believes we are moving at an acceptable pace.

Also, HB100 requires actuarial studies by the Actuarial Committee for proposed legislation, which raises several questions such as: What is “legislation proposing change”? “Will the legislation have a material impact?” “How much work is needed to prepare a study?” The CAO report noted a higher level of functioning for the Actuarial Division now that we have three credentialed actuaries on staff. Before HB100 there were no credentialed actuaries on staff.

Mr. Bryan indicated the report of the Actuarial Committee was concluded.

AUDIT COMMITTEE

Mr. Haffey reported that there were three presentations and one action item and at the Audit Committee meeting. Tom Croyle, Chief Information Officer, provided the annual report on the disaster recovery plan. In the event of disaster, BWC will move its command center to Plain City and back-up operations center to New York. Tracy Valentino, Chief, Fiscal & Planning, reviewed comments by the external auditor in its management letter. The letter made nine comments, eight of which are minor deficiencies and of which all but one or two are currently resolved. There was also a discussion on audits of Managed Care Organizations (MCOs). Finally, Ms. Valentino reported on what the Fiscal and Planning Division does to address these comments until the external auditors return in June for the next audit.

Ray Mazzotta, Chief Operating Officer, and Ms. Valentino led a discussion on reinsurance. This included a report on the use of reinsurance by other states and a Deloitte evaluation of the proposal. The next step is to obtain terms and prices.

Mr. Haffey moved that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendation per the Memorandum dated December 21, 2009, from the Chief Operating Officer and the Chief Financial Officer to obtain reinsurance coverage for the State Insurance Fund at terms favorable to the Bureau, as recommended by the Audit Committee and with the approval of the Board Chair and Chair of the Audit Committee.

Mr. Haffey further reported that Caren Murdock, Chief of Internal Audit, provided the monthly update on current internal audit projects. There was also a discussion on the requirement for performance audits required by SB4 and conducted by the Auditor of State or external auditors. The February meeting will include updates and a report from Joe Bell, Office of Budget and Management, on the IT audit.

Mr. Haffey indicated the report of the Audit Committee was concluded.

INVESTMENT COMMITTEE

Mr. Smith reported that the investments of the Bureau State Insurance Fund stood at \$18.8 billion in market value as of January 20 and consisted of 68.6% in fixed income investments, 30.4% in equities, and 1% in cash. The portfolio's bonds and stocks increased in market value by 1.9% or \$353 million during January as of January 20. For the calendar year 2009, the total portfolio return was 8.6%, and constituted very strong returns; for the fiscal year-to-date ended December 31, 2009, the total portfolio return was 9.1%.

Mr. Smith reported that the Investment Committee had received a presentation from Mellon Capital Management as a new manager of the Russell 3000 index investments. Mellon is head-quartered in San Francisco and its representatives offered insights on their passive equity strategy in managing funds to the Russell 3000 index.

Mr. Smith moved that the Workers' Compensation Board of Directors adopt the recommendation of the Investment Committee to approve Mellon Capital Management as a U.S. Equities Passive Index manager for the State Insurance Fund, representing a targeted six percent (6%) of the total State Insurance Fund invested assets, for the reasons set forth in the presentation of the Passive Index Manager RFP Evaluation Committee dated January 21, 2010, and the Memorandum prepared by Mercer Investment Consultants dated January 6, 2010, and upon such terms as are outlined in Mellon Capital Management's Response to the Request for Proposals issued July 2, 2009, and such other terms as are favorable to the Bureau. Ms. Falls seconded and the motion was approved by a vote of eleven ayes and no nays.

Mr. Smith remarked that this is the fifth consecutive month in which there has been a presentation and recommendation of passive investment managers for in the State Insurance Fund. Each time, there has been an excellent presentation by Bruce Dunn, Chief Investment Officer, on behalf of the RFP Evaluation Committee. Mr. Smith also commented that the asset class transitions have been planned and executed with effectiveness and efficiency.

Mr. Smith continued by summarizing the report on the asset allocation for the Disabled Workers' Relief Fund (DWRF) by Mercer Investment Consulting, Inc.. DWRF constitutes \$1.25 billion of the portfolio and has only \$200 million in liabilities. The Investment Committee discussed if DWRF should be merged into the State Insurance Fund (SIF) and the statutory changes that would be required to combine it. In the end, the Investment Committee recommended an asset allocation strategy similar to the SIF (70/30 fixed income/equity) for the DWRF portfolio. The recommended DWRF allocation would have a lower standard

deviation of return risk because of the much shorter average duration of the fixed income allocation.

Mr. Smith moved that the Workers' Compensation Board of Directors adopt the recommendation of the Investment Committee to approve revision of the Asset Allocation Mix for the Disabled Workers' Relief Fund to conform with "Mix D" as discussed in the Mercer Strategic Asset Allocation Analysis Report dated January 21, 2010, and the Memorandum of the Chief Investment Officer dated January 13, 2010, and also to adopt relevant revisions to BWC's Statement of Investment Policy and Guidelines as they are set forth in the attachments to the Chief Investment Officer's Memorandum of January 13, 2010. Mr. Haffey seconded and the motion was approved by a vote of eleven ayes and no nays.

Mr. Smith reported that the Investment Committee is required to review the custodial relationship with JPMorgan Chase. There was report from Lee Damsel, Director of Investments, and Doug Walouke and Dan Blevins, Senior Investment Managers, on the activities of the custodian over the past year. The sub-custodian is selected by the Treasurer of State. The current contract will expire in June, 2010, and the Treasurer has issued an RFP. The Investment Division staff is satisfied with the performance of the current sub-custodian.

Mr. Smith indicated the report of the Investment Committee was concluded.

MEDICAL SERVICES AND SAFETY COMMITTEE

Mr. Harris reported that the Medical Services and Safety Committee had three presentations and two action items.

The committee had a second reading from Freddie Johnson, Director of Managed Care Services, and Anne Casto, Consultant, Medical Services, on the out-patient hospital fee. During the December meeting, the Committee raised several questions for staff to answer. Also, the Committee had received a letter of comment from the Ohio Hospital Association. The result is a recommendation to implement the fee schedule over three years rather than two.

Upon the recommendation of the Medical Services and Safety Committee, Mr. Harris moved that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendation to rescind current Rule 4123-6-37.2 and adopt new Rule 4123-6-37.2 of the Administrative Code, "Payment of Hospital Outpatient Services." The motion consents to the Administrator rescinding and adopting new Rule 4123-6-37.2 as presented at the Medical Services and Safety Committee. Mr. Hummel seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

Mr. Harris reported Michael Rea, Public Employment Risk Reduction Program, gave a presentation on the new acetylene standards of OSHA. These standards will be embodied in a rule amendment.

Upon the recommendation of the Medical Services and Safety Committee, Mr. Harris moved that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendation to amend Public Employment Risk Reduction Program Rule 4167-3-04.2 of the Administrative Code, "Amending of Standards." The motion consents to the Administrator amending Rule 4167-3-04.2 as presented at the Medical Services and Safety Committee. Mr. Pitts seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

Mr. Harris reported that Abe Al-Tarawneh, Superintendent of Safety and Hygiene, gave a presentation on new standards for the Drug Free Safety Program. The pricing of this program will be discussed with the Actuarial Committee. There will be a first reading of the rules for this new program in February.

Mr. Price commented that BWC staff is doing an outstanding job of outreach to stakeholders. Nevertheless, in light of a comment on the out-patient fee rules received on January 22, he emphasized that BWC needs to give the stakeholders enough time to respond to its proposals.

Mr. Harris indicated the report of the Medical Services and Safety Committee was concluded.

GOVERNANCE COMMITTEE

Mr. Lhota announced that there is no Governance Committee report this month because the Committee meeting is scheduled immediately after the Workers' Compensation Board meeting.

MONTHLY ENTERPRISE REPORT

Ms. Valentino provided the enterprise report. Net assets declined by \$202 million, from \$4.2 billion in November 2009 to \$3.95 billion as of December 31. The first reason for the decrease was an adjustment in premium and assessment income. In December, private employer premium accruals were adjusted to reflect the impact of reduced employer payroll noted in the most recent collection period. Premium payments in July and August were lower than expected, leading to a decision to reduce the recognition of premium income. The adjustment was made in December and led to a \$60 million (8%) reduction. The second reason was the provision for uncollectible receivables was being impacted by adjustments to outstanding receivables. The two factors led to recognition of \$159 million in operating revenue. Also, premium and assessment income was reduced in December because of \$10.5 million in rebates for employers participating in safety

councils. The benefits and compensation adjustment expense of \$188 million and other expense of \$7 million resulted in \$195 million in operating expense. December expenses were less than November because of the quarterly MCO performance payments of \$6 million and one less payroll in December. There was a \$222 million decrease in the market value of the portfolio.

December premium and assessment income was \$90 million because the second 50/50 payment was due December 1. BWC redeemed \$58 million from investment managers to support operations, an amount significantly lower than past years. In the fiscal year-to-date, net assets increased by \$1.4 billion. Premium and assessment income for fiscal year to date is \$1.1 billion, compared to \$1.2 billion for the same period last year. Decreases in premium rates for private and state agency employers effective July 1, 2009, are off-set by increased unbilled receivables for DWRP and the Self-Insuring Employers' Guaranty Fund (SIEGF). Reserves for compensation and compensation adjustment expenses for DWRP and SIEGF have increased by \$35 million. Lump sum settlements are \$53 million less for fiscal year to date compared to the same period last year.

The investment income for fiscal year-to-date 2010 totaled \$1.6 billion, consisting of \$596 million in net realized losses and \$1.777 billion in net unrealized gains and \$376 million of interest and dividend income, net of \$3 million in investment expenses. Fiscal year-to-date premium collections are \$77 million less because of an 8% decrease in private employer premium payments. Declines in private employer payroll and last year's 5% decrease in private employer premium rates have contributed to premium collections being \$97 million less than the prior fiscal year-to-date collections.

Mr. Bryan asked, in light of payment in arrears, does BWC offer discounts for prepayment of premiums. Ms. Valentino replied that employers may make flex pay payment on a monthly basis. Also, Public Employer Taxing Districts pay twelve months in arrears. Barb Ingram, Director of accounting, reported that the discount offered in the flex pay program is tied to a U.S. Treasury interest rate. Ms. Valentino reported that BWC will provide the Workers' Compensation Board more information on rates and explanations of discounts.

Mr. Harris asked if the December adjustments occur each year. Ms. Valentino replied that BWC makes this adjustment in each year, usually in the third and first quarter. The adjustment was in the second quarter this year because of greater unemployment in Ohio and BWC had the data and decided to apply it.

Marsha Ryan, BWC Administrator, stated that the decline in payroll is shown on page 17 of the Enterprise Report. The Department of Taxation saw the decline earlier, and is now seen in payments to BWC. Payrolls are similar to those reported in 2006.

Mr. Smith remarked that when the Ohio Senate undertakes a study of private insurance, it should be impressed that Ohio employers have the benefit of BWC premium payments in arrears.

Mr. Haffey stated that as an accountant he appreciates the booking of the reduction of income at the earliest time. This reflects sound fiscal practice.

Mr. Price requested a report on the impact of those who participate in pre-payment programs on total collections.

Ms. Valentino further reported that, in looking forward, the payroll reports were mailed in January and have a February 28, 2010 due date. Those electing the 50/50 option have a second payment due on June 1, 2010. Employers now have the option of paying online or by mail. We will monitor trends. The bulk of the payments occur during the last two weeks of February.

The combined financial statements show \$3.9 billion in net assets, of which \$3.5 billion is in the State Insurance Fund.

Concerning the Administrative Cost Fund (ACF) budget, BWC has begun the process for the FY 2011 ACF budget, which will be the basis of the ACF assessment. The Audit Committee will review the ACF budget at the April and May meetings. After completion, BWC will begin the 2012—2013 biennial budget, which is usually due to OBM in September.

Year-to-date, operating expense is 12% less than the budget. There was a decrease in payroll because of hiring freeze and one less health insurance payment in July. BWC personnel are taking cost savings days (CSDs). Through December, they took 123,000 hours, which is 66% of the available CSDs of 189,000, for \$3.6 million in savings. Usage continued to increase through the December holidays, increasing the hours taken to 147,000 (80%), for a savings of \$4.4 million. BWC conducts continuous evaluation of personnel service contracts, licenses, and equipment. Some projects for 2010 will be delayed. Further, the budget is 11% than the legislative appropriation.

Ms. Valentino reported that the funding ratio and net leverage ratio of 1.24 and 4.62, respectively, are both within the policy range. Performance measures show that new claims filed continues to decrease. Ms. Valentino asked the Directors for suggestions additions or refinements to the metrics contained in the Enterprise Report.

Mr. Haffey asked about the cost to the employer for using the 50/50 program. Ms. Valentino replied there was no cost. Mr. Haffey observed that if compared to commercial insurance, not only do employers pay in arrears, but the employer can delay payment.

Mr. Harris noted that the Department of Administrative Services had sent a notice on a missed health insurance payment and asked about the effect. Ms. Valentino replied that recovery of the payment will be pro-rated over future payrolls.

Ms. Falls noted that maintaining premium stability is one of the duties of the Workers' Compensation Board. She requested the Administrator provide a review of this topic to the Board during the year.

Ms. Ryan replied that this discussion is best presented as an effect of rate reform in premiums.

ADMINISTRATOR BRIEFING

Ms. Ryan first provided an update on legislative affairs. SB249 concerns redefinition of "journalist" to permit access to bulk lists of claimant contact information. The Senate Committee on Insurance, Commerce, and Labor recently held a hearing with proponent testimony. BWC has no information on future hearings or the opportunity to present opponent testimony. The staff of the Workers' Compensation Council issued its report on HB213 on January 20. This bill would create a two-year moratorium on rate reform. BWC will evaluate it after today's meeting. At first glance, the report is thorough and comprehensive. The bill on PEOs, HB216, is subject to ongoing discussion. Mr. Mazzotta and the Legal Division are providing input to strengthen the ability of BWC to assess accurate premiums. SR118 concerns study of the feasibility of privatization of workers' compensation. The Senate has now made appointments of taskforce members and a list is available. By the express terms of the resolution, members include Mary Jo Hudson, Director, Ohio Department of Insurance, Mr. Lhota, and Administrator Ryan. Now that the appointments are finished, meetings can be scheduled. Governor Strickland's State of the State address will be given on January 26.

Ms. Ryan reported that she continues to attend local round-tables as an opportunity to meet with chambers of commerce and local businesses. She recently attended a session in Cincinnati with twenty local participants. BWC was able to report \$18 million in premium reductions locally. The next roundtable is on January 29 in Marietta.

Human Resources Chief Tony Brokaw is returning to BWC after being loaned to the Department of Administrative Services HR. Ms. Ryan thanked Brian Walton, Director of Labor Relations for heading human resources in her absence. Peggy Concilla will now serve as Director of Communication and Legislation. Christine Madriguera will return to the Office of the Governor. Mr. Mazzotta and Tom Prunte, Director of Employer Management Services, are making changes in that division. Mr. Prunte has reorganized the Self-Insured Department, with the input

of the self-insured community. The Self-Insured Bankruptcy Claims Unit will be merged with Claims Management. The split-plan will be discussed at a February 10, 2010 meeting and BWC will take comments from stakeholders.

Ms. Falls asked if the Workers' Compensation Council analysis of SB213 was factual, or did it include recommendations. She also asked for an executive summary of the report. Ms. Ryan further stated she would be sharing the Workers' Compensation Council analysis and BWC comments with the Workers' Compensation Board. The SB213 report is very analytical and sets forth consequences without advocacy.

Mr. Smith added he thought it would be a two-step process: The Workers' Compensation Council staff would do an analysis. Then the Workers' Compensation Council would make a recommendation on the bill. Mr. Smith asked if the chair of the Workers' Compensation Council would recuse himself as the sponsor of the bill.

Mr. Bryan stated that one goal of the Workers' Compensation Board was in preparing an index of rates to compare Ohio with other states. This is needed before comparison with private insurers can be made. He asked how that index is progressing. Ms. Ryan replied that this is difficult study, especially in obtaining information from Michigan. BWC has discussed this with the National Council on Compensation Insurance, but this was not a fertile field of information. BWC does have some data for a basis of comparison, but it is usually several years old. "Real time" or current rate comparisons are expensive to develop.

Mr. Pitts commented that BWC needs to make an effort to compare systems. There are constitutional barriers to privatization; however, Senator Grendell is reported to believe there are ways around the constitution. The committee appointed under SR118 is expected to explore these issues.

EXECUTIVE SESSION

There was no executive session.

CHAIRMAN'S COMMENTS

Mr. Lhota suggested that the Governance Committee be convened immediately after the adjournment of the Workers' Compensation Board meeting. Further, he suggested that the Governance Committee recess during its executive session to excuse Mr. Pitts, who is appointed to the Board as a representative of injured workers, from the meeting. Pursuant to an opinion of the Ohio Ethics Commission, a Director who is an attorney representing clients before the BWC may not participate in an Administrator's evaluation.

ADJOURNMENT

Mr. Smith moved to adjourn the meeting. Mr. Caldwell seconded and Mr. Lhota adjourned the meeting at 9:15 a.m. after the motion was approved by a roll call vote of eleven ayes and no nays.

Prepared by: Larry Rhodebeck, Staff Counsel
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January 28, 2010