

BWC BOARD OF DIRECTORS
BOARD MEETING
FRIDAY, March 25, 2011, 8:00 A.M.
WILLIAM GREEN BUILDING
30 WEST SPRING ST. 2ND FLOOR (MEZZANINE)
COLUMBUS, Ohio 43215

MEMBERS PRESENT: Nicholas Zuk, Chair
David Caldwell
Ken Haffey
James Hummel
Steve Lehecka
Jim Matesich
Mark Palmer
Thomas Pitts
Larry Price
Robert Smith
Dewey Stokes

Members Absent: None
Counsel Present: Janyce Katz, Assistant Attorney General
BWC Counsel Ann Shannon, Legal Counsel
Staff present: Steve Buehrer, Administrator
Tracy Valentino, Chief, Fiscal & Planning
Scribe: Larry Rhodebeck, Staff Counsel

CALL TO ORDER

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

MINUTES OF MARCH 24, 2011

Mr. Price moved to amend the Board minutes to reflect that the governance Board vote on the Governance Committee added Director Palmer as a member. Mr. Smith seconded the motion.

Mr. Matesich moved to approve the minutes of March 24, 2011, as amended. Mr. Hummel seconded the motion to approve the amended minutes. The motion to amend the minutes and the motion to approve the amended minutes were approved by a combined roll call vote of eleven ayes and no nays.

AGENDA

Mr. Haffey moved to approve the agenda as submitted. Mr. Palmer seconded and the agenda was approved by a roll call vote of eleven ayes and no nays.

COMMITTEE REPORTS

Mr. Zuk commended the committees and BWC staff for the level of detail provided at the committee meetings of March 24.

ACTUARIAL COMMITTEE

Mr. Lehecka reported that the Actuarial Committee held an education session on March 23. John Pedrick, Chief Actuarial Officer, and Tracy Valentino, Chief Fiscal & Planning Officer, discussed balance sheet concepts including assets, liabilities, net assets and relative risks, and stresses. Dave Heppen and Jan Lommele from Deloitte Consulting LLP walked the committee through the actuarial process and methodologies of determining unpaid claim liabilities or reserves. Elizabeth Bravender, Actuarial Operations Director, addressed rating concepts, which included the individual groups and funds, and the ratemaking process and considerations. Mr. Pedrick led a discussion regarding premium equity within the Private Employer Fund, specifically relative to group and non-group rates and results.

Mr. Lehecka further reported that the regular meeting of the Actuarial Committee was held March 24. The agenda for the meeting was modified to move the rate change recommendation from a first reading to a discussion item. Tom Prunte, Executive Director, Actuarial Services, and Michael Glass, Director of Underwriting and Premium Audit, presented the second reading of the 2011 NCCI Classification changes which were approved by the Actuarial Committee.

Upon the recommendation of the Actuarial Committee, Mr. Lehecka moved that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendation to amend Rule 4123-17-04 of the Administrative Code, "Classification of Occupations or Industries," to adopt new NCCI classifications. The motion consents to the Administrator amending Rule 4123-17-04 as presented at the Actuarial Committee meeting. Mr. Stokes seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

Mr. Lehecka also reported that Joy Bush, Program Development Director, presented the second reading of the Deductible Program Rule 4123-17-172, which also was approved by the Actuarial Committee.

Upon the recommendation of the Actuarial Committee, Mr. Lehecka moved 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," related to the aggregate stop loss of an employers' premium in the program. The motion consents to the Administrator amending Rule 4123-17-72 as presented at the Actuarial Committee meeting. Mr. Hummel seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

As discussion items, Mr. Lehecka reported that Mr. Heppen of Deloitte addressed the private employer rate indication. The reasonable expectation indication for the July 1, 2011, policy year is a range from -5.4% reduction to a +7.4% increase, with a baseline increase of +1.3%. The committee conducted a robust discussion on the comparison of indemnity and medical average costs which shows costs of Ohio significantly higher than

the 35 states included in the NCCI annual survey. Many on the committee expressed the need to maintain focus on and potentially addressing these cost differences without hindering the required remedies to injured workers. Mr. Pedrick also summarized the potential public employer state agency rate activity.

Bill Van Dyke of Deloitte presented the Quarterly Reserve Analysis for the fiscal year ending June 30, 2011, based on data as of December 31, 2010. On a discounted basis, the total liability estimate of \$20.045 billion for all funds is a decrease of \$20 million from the previous quarterly evaluation. Mr. Pedrick outlined the calendar for the next few months relative to potential rate action.

Mr. Zuk noted that all members of the Workers' Compensation Board were present for the meeting and contributed to the discussion.

AUDIT COMMITTEE

Mr. Haffey reported that the Audit Committee met on March 23 and had one action item. Tom Sico, Assistant General Counsel, recommended approval of the five-year rule review for the rule on electronic submission of documents.

Upon the recommendation of the Audit Committee, Mr. Haffey moved that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendation on the five-year rule review of Rule 4125-1-02 of the Administrative Code, "Electronic Submission and Acceptance of Documents." The motion consents to the Administrator retaining without change Rule 4125-1-02 as presented at the Audit Committee, and to filing the rule jointly with the Industrial Commission upon the approval of the Industrial Commission. Mr. Smith seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

Mr. Haffey further reported that Ms. Valentino held discussions on the discount rate and financial metrics. The discount rate is set in accordance with BWC historic practices, industry standards, BWC investment returns, investment trends, and anticipated changes in financial markets. In her discussion of performance metrics, Ms. Valentino discussed the funding ratio, the net leverage ratio, the net loss ratio, the expense ratio, the combined ratio, and the operating ratio.

Mr. Prunte held an education session on Professional Employer Organizations (PEOs). PEOs manage payrolls, pay payroll taxes, workers' compensation premiums, and are employers of record. BWC is undertaking changes in regulation, based on a recent audit of PEOs led by Caren Murdock, Chief of Internal Audit. Recommendations include tracking of data to calculate individual experience modification of clients; require PEOs to provide workers' compensation to clients; require quarterly reporting of clients and workforces; and require securitization of PEOs.

Ms. Murdock provided the Second Quarter Executive Summary Report for Fiscal Year 2011. The report included management comments and management acceptance of risks of not taking action on one audit. Three projects are in planning, six in field work, and three in final phases. Eight projects are to be completed in the next three months. There was also a discussion on Internal Audit Division staff and its qualifications. The Audit

committee went into executive session with Joe Bell, Chief Audit Executive, Office of Budget and Management, Office of Internal Audit, to discuss an Information Technology audit.

INVESTMENT COMMITTEE

Mr. Smith reported that as of March 23, the BWC investments totaled \$20.744 billion, consisting of 66% in fixed income, 32% in equities, and 2% cash. All distributions are within the range of the Investment Policy guidelines. For fiscal year to date ended February 2011, the BWC investment portfolio has returned 9.8%, with reported investment income of almost \$1.9 billion. However, there has been a 0.3% fall in market value of its stock and bond assets in March as of March 23 because of declines in equities.

The internal audit of the Investment Division process for Requests for Proposal (RFP) yielded no items of material weakness.

Mercer Consulting is terminating its public fund investment clients, so BWC has been in search of another consultant. The RFP was issued in November 2010; responses were received in January 2011. The RFP Evaluation Committee then immediately began its review. The Evaluation Committee consists of Mr. Smith, Mr. Palmer, Bruce Dunn, Chief Investment Officer, and Lee Damsel, Director of Investments. The Evaluation Committee interviewed four final candidates on February 24 and 25 at the William Green Building. R.V. Kuhns & Associates, Inc., was selected as the finalist and the Evaluation Committee did its due diligence visit to R.V. Kuhns' headquarters in Portland, Oregon.

Mr. Smith moved that the Board of Directors of the Bureau of Workers' Compensation approve and adopt the recommendation of the Investment Committee to approve and adopt the RFP Evaluation Committee's suggestion to authorize the Administrator of the Bureau of Workers' Compensation to contract with R.V. Kuhns & Associates, Inc., to serve the Board of Directors and the BWC staff as a full service investment consultant, upon such terms as are outlined in the Request for Proposals issued November 16, 2010, by the Bureau of Workers' Compensation and in R.V. Kuhns & Associates, Inc.'s response to the Request for Proposals issued November 16, 2010. Mr. Caldwell seconded the motion.

Mr. Stokes commended Mr. Smith, the Investment Committee, and BWC on the thoroughness of the reports on selection of the consultant. Mr. Zuk agreed with Mr. Stokes' comments.

The motion was passed by a roll call vote of eleven ayes and no nays.

Mr. Smith also reported that the Investment Committee undertook as a second action item the renewal of contracts for the three transition managers currently serving the Bureau.

Mr. Smith moved that the Bureau of Workers' Compensation Board of Directors approve and adopt the recommendation of the Investment Committee to renew the respective Optional Use Contracts of the BWC transition managers, for the reasons set forth in the memorandum of BWC's Chief Investment Officer dated March 15, 2011, for BlackRock

Institutional Trust Company, N.A.; Russell Implementation Services, Inc.; and State Street Bank & Trust Company. Mr. Haffey seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

Mr. Smith reported the third action item was approval of an amendment to the Investment Policy Statement regarding the long duration credit active management portion of the portfolio. The BWC Chief Investment Officer recommended in his memorandum dated January 12, 2011 that a targeted 20% of the State Insurance Fund investment portfolio be allocated to the active management of its long duration credit fixed income mandate with the remaining 8% of this mandate remaining passively managed.

Mr. Smith moved that the Bureau of Workers' Compensation Board of Directors approve and adopt the recommendation of the Investment Committee to amend those provisions of the *Statement of Investment Policy and Guidelines* regarding long duration credit active management, for the reasons set forth in the Memorandum the BWC Chief investment Officer dated January 12, 2011. The recommended amendments to the IPS are shown in the red-lined version of the IPS prepared by the BWC Chief Investment Officer and Mercer Investment Consulting and will be incorporated by reference into the minutes of this meeting. Mr. Caldwell seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

Mr. Smith finally reported that the Investment Committee meeting in April will undertake discussion on real estate investments with a goal of investing up to 5% of the State Insurance Fund portfolio.

Mr. Price commended Mr. Dunn, Ms. Damsel, Mr. Smith, and Mr. Palmer on the thoroughness of their investment consultant selection presentation. The hiring of Mercer Consulting in 2008 was a very thorough RFP process and this process was continued in the new investment consultant RFP to address the concerns of the Workers' Compensation Board.

MEDICAL SERVICES AND SAFETY COMMITTEE

Mr. Hummel reported that the Medical Services and Safety Committee met on March 24 with all members present and approved one action item. The Medical Services and Safety Committee completed the second reading on the claimant reimbursement rule, 4123-6-26. The rule change would allow BWC to reimburse an injured worker for his out-of-pocket co-pays paid prior to the allowance of a claim. The stakeholder feedback was supportive of the change.

Upon the recommendation of the Medical Services and Safety Committee, Mr. Hummel moved that the Bureau of Workers' Compensation Board of Directors approve the Administrator's recommendation to amend Rule 4123-6-26 of the Administrative Code, "Claimant Reimbursement," to reimburse injured workers for certain co-payments for medical services. The motion consents to the Administrator amending Rule 4123-6-26 as presented at the Medical Services and Safety Committee. Mr. Caldwell seconded and the motion was approved by a roll call vote of eleven ayes and no nays.

Mr. Hummel also reported that there were four first readings on other action items. Freddie Johnson, Interim Chief of Medical Services and Compliance, and Karen Fitzsimmons, Manager, Rehabilitation Policy, presented the Vocational Rehabilitation Fee Schedule. The fee schedule has been presented to a broad range of stakeholders. The major changes include: an overall increase of 1.36% to all established fees for service; adding local codes for training, counseling and job development; and changes in several definitions.

Mr. Johnson also recommended changes in the prior-approval process of the Managed Care Organizations (MCO) for all non-emergency medical treatment on the form fondly known as C-9. Again, the rule has had a thorough vetting with interested parties. The substantive changes include adding a definition of “eligible treating provider” to the rule; requiring providers to use HCPCS codes in effect at the time of the treatment; and requests from physical or occupational therapists must be accompanied by a prescription. Finally, an MCO can dismiss the request without prejudice if the claim has been disallowed, dismissed, or is the result of a pre-existing condition; the treatment or services are “never covered” by BWC; or the provider has not submitted supporting medical documentation to the MCO.

The final two rules address outpatient medication practices. Ohio Administrative Code Rule 4123-6-21 applies to state fund employers and Rule 4123-6-21.1 applies to self-insured employers. These rules update reimbursement practices and clinical guidelines for the BWC Pharmacy Department and self-insuring employers and introduce a clinical perspective to the BWC outpatient medication rules that is intended to improve outcomes for injured workers. The rules have been reviewed by the Pharmacy and Therapeutics Committee, and distributed to stakeholders for further comment with a requested response date of April 6. The major changes include: prohibiting reimbursement for noncertified providers unless one of three exceptions are met; allow a \$3.50 dispensing fee to a pharmacy; prohibit reimbursement to third party pharmacy billers; allow injured worker reimbursement for brand-name drug where it has been demonstrated that generics have caused allergic reactions or adverse events, and allow BWC to deny refills requested before 90% of any published days’ supply limit has been utilized, with overrides for documented exceptions.

Also, Dr. Kort Gronbach, a member of BWC’s Pharmacy and Therapeutics Committee, discussed best practices of pain management. His comments were well-received and will be helpful as the Workers’ Compensation Board and BWC continue to make improvements to the pharmacy program for the safety of injured workers.

Tina Kielmeyer, Chief, Customer Services, reported on the Customer Services Division focused on permanent total disability (PTD) and death claim transfers. In order to ensure proficiency and consistency of claims management and better service to customers, BWC recently centralized and regionalized certain complex claim types. Effective January 21, 2011, 4,300 death claims (with active dependent benefits) are centralized and managed by the Columbus Service Office and 24,500 PTD claims are regionalized and managed by the Dayton and Youngstown Service Offices. Specialized teams have been assigned these more complex claims types.

Finally, Abe Al-Tarawneh, Superintendent, Safety and Hygiene, reported about the upcoming Ohio Safety Congress and a BWC-NIOSH workshop that was held March 15. At the workshop, BWC and NIOSH staff shared results of recently completed studies, and exchanged ideas for future potential joint projects involving trucking, wholesale trade and retail, agriculture, and manufacturing.

Mr. Pitts commended Dr. Gronbach's written report. If an injured worker has a legitimate need for pain relief, he should get the medication. If the medication is not needed, BWC should help with any addiction and abuse assistance. Mr. Pitts believes it is important to "stay ahead of the curve" to protect the system and injured workers.

ENTERPRISE REPORT

Ms. Valentino presented the March 2011 *Enterprise Report*. BWC's net assets increased by \$310 million in February resulting in net assets of \$5.3 billion at February 28, 2011 compared to \$5.0 billion at January 31, 2011. This includes the impact of a 4.0% discount rate on future liabilities. Premium and assessment income net of the provision for uncollectible accounts receivable and ceded reinsurance premiums resulted in operating revenues of \$147 million in February. Benefits and compensation adjustment expenses of \$190 million along with other expenses of \$9 million resulted in operating expenses of \$199 million.

A decrease of \$6 million in medical benefits along with a \$2.6 million decline in settlements contributed to decreased net benefit payments in February. Medical payments of \$61.5 million issued in February are the third lowest monthly total issued in the last 24 months. The previous monthly lows for medical payments were January 2010 and February 2010 with \$60.2 million and \$60.7 million, respectively. February payments include \$5 million in quarterly performance payments made to Managed Care Organizations.

Ms. Valentino also reported that a \$305 million increase in the fair value of the investment portfolio in February, along with interest and dividend income of \$58 million for the month, resulted in net investment income of \$362 million for the month after investment expenses of \$0.7 million. The increase in the fair value of the portfolio is comprised of \$0.6 million in net realized gains and \$304 million in net unrealized gains. Cash and cash equivalents include \$162 million in money market holdings in the outside investment manager accounts. These funds are committed to covering a \$105 million net investment trade payable for transactions that will settle in March.

Premium and assessment receipts of \$501 million were collected in February compared to \$460 million in February 2010 when the last day of the month was Sunday. Approximately 212,000 or 85% of private employers timely filed their payroll report for the July through December 2010 policy period compared to 84% for the same period last year.

BWC's total net assets have increased by \$1.5 billion for fiscal year-to-date 2011 resulting in net assets of \$5.3 billion at February 28, 2011 compared to \$4.0 billion at February 28, 2010. BWC's premium and assessment income for fiscal year-to-date 2011 is \$1.3 billion compared to \$1.4 billion for fiscal year-to-date 2010 reflecting decreased payroll and

premium rates for private and state agency employers effective July 1, 2010 and January 1, 2010 and 2011 for public employer taxing districts.

Ms. Valentino additionally reported that benefit and compensation adjustment expenses increased by \$60 million for fiscal year-to-date 2011 compared to prior fiscal year-to-date expenses. BWC's net investment income for fiscal year-to-date 2011 totaled \$1,877 million comprised primarily of \$1,219 million in net unrealized gains and \$206 million in net realized gains, along with \$457 million of interest and dividend income, net of \$5 million in investment expenses. Declines in private employer and public employer taxing district premium rates have contributed to premium collections being \$33 million less than prior fiscal year-to-date collections.

Approximately 21,400 employers participating in the 50/50 payment plan will be paying \$151 million in premiums by June 1, 2011 to maintain active coverage. These numbers are up from the 20,200 employers that participated last year that owed \$146 million for the second installment. Coverage was lapsed March 1, 2011 for almost 38,000 private employers that failed to report payroll and pay premium by the February 28th due date. As of March 11th, coverage remained in a lapsed status for over 29,000 private employers who owe an estimated \$31.3 million in premiums. Estimated premium will be billed to employers that are still in a lapsed status the weekend of March 19th. BWC will follow-up after lapse with phone calls to large employers. Most lapsing employers are not in business not aware of the need to cancel coverage or new employers.

Mr. Smith asked if the employer lapses, is the injured worker still covered. Ms. Valentino replied that the injured workers are still covered and employers are liable dollar for dollar for the cost of the claim.

Ms. Valentino further reported that based upon the quarterly reserve analysis completed by Deloitte, reserves for compensation and compensation adjustment expenses will be reduced by approximately \$14 million through February 28th. This reduction in estimated reserves is primarily a result of lower than expected benefit payments.

BWC Administrative Cost Fund expenses through fiscal year to date (FYTD) February 2011 are approximately \$11.7 million (6.7%) less than budgeted and 2% less than last fiscal year to date. Decreases in payroll through FYTD February 2011 are a result of decreases in staffing due to retirements and hiring controls. As of February 2011, there were approximately 170 less full time equivalent positions compared to the same time last year. Payroll changes within the Fiscal and Planning and Information Technology divisions are the result of Office Services and Facilities departments moving between divisions. Through February 2011 journal entries, BWC staff have taken 148,700 (88%) of the available 169,000 hours of cost savings days for a savings of approximately \$4.4 million, which is about the same as last fiscal year.

Mr. Hummel asked how much longer cost-savings days will be used. Ms. Valentino replied this is the last year for them and effective July 1, will not be in use.

Ms. Valentino also reported that the timing of the receipt of invoices for payment in fiscal year 2011 contributed to actual expenditures being less than the amount budgeted

through February. Purchase orders have been completed in the Personal Services and Maintenance categories to encumber the FYTD 2011 budget. BWC's current fiscal year 2011 budget is approximately \$65 million (19.8%) less than appropriated by the General Assembly.

Administrative expenses paid from the State Insurance Fund include the investment administration expenses, actuarial expenses, reinsurance expenses, and the Ohio Rehabilitation Services. Operating transfers have been made to the Ohio department of Natural Resources for the Mine Safety Fund and Strip Mining Administration Fund and the Ohio Inspector General. Premium and Assessment receipts for February totaled \$501 million and reflected the payroll reporting and premium payment. The statement of net assets shows a balance of \$5,321 billion and continuing the upward trend for fiscal years 2010 and 2011. The combined reserve for compensation and compensation adjustment expense is \$19.978 billion. The undiscounted reserve is \$32.474 billion. The funding ratio is 1.31 and the net leverage ratio is 3.61. Both fall within the policy guidelines. There will be a March discussion on metrics and guidelines.

Mr. Price stated that he had attended the budget hearings in the House of Representatives and listened to the testimony of Mr. Buehrer. He requested an explanation on how three different numbers are all described as "assets." The numbers are \$20 billion, \$5.3 billion, and \$32 billion. Ms. Valentino responded that the \$20 billion "asset" is the investment portfolio, which is distinct from accounts receivable and real estate. Mr. Smith added that each month's expense report always is more than income because some portion of investment earnings are used to pay claims. Mr. Price stated that there is some confusion at the Statehouse on where the \$5 billion in assets is. Mr. Haffey replied that this is the difference between the discounted liability of the State Insurance Fund, and the invested assets.

Mr. Pitts noted that the severity chart on page 17 should include expenses in medical-only claims. He also requested information comparing data from the NCCI.

ADMINISTRATOR'S REPORT

Steve Buehrer, Administrator, congratulated Mr. Zuk, Mr. Lehecka, Mr. Palmer, and Mr. Stokes on being confirmed as directors by the Ohio Senate.

Mr. Buehrer reported that he continued to meet during the month with staff on floors of the William Green Building. On March 1, BWC held a town hall meeting and received hundreds of comments on improvements and suggested changes. When the comments are combined and collated, they will be posted for all to read. There is real employee enthusiasm with the opportunity to be involved in this process.

Mr. Buehrer met with additional stakeholders such as the Ohio Manufacturers Association, the County Commissioners Association, the NCCI, and agricultural interests gathered at the Ohio Department of Agriculture for a conference.

The BWC budget was approved by the House of Representatives. Hearings will begin in the Senate Insurance, Commerce, and Labor Committee on March 30. BWC will continue to monitor the general budget which will contain provisions on personnel.

Governor Kasich has given a high priority to closing pill mills. The Medical Services and Safety Committee held a session on prescription drug addiction and abuse. BWC spearheaded a task force to close the clinics of Dr. James Lundeen. His Portsmouth clinic is responsible for 61% of prescriptions in Scioto County and is second in the state. BWC executed warrants on the Portsmouth and Plymouth Clinics and the residence of his ex-wife. Dr. Lundeen had seen forty patients during the morning of the raid. BWC pulled the doctor's certification two days later. The Special Investigations Division is a great resource for BWC. For every dollar it spends, BWC saves \$6 in fraud. The bad news is that more doctors will need to be investigated in the future.

The Ohio Safety Congress and Expo will be held March 29 to 31 at the Columbus Convention Center. Governor Kasich will speak at 3:45 p.m. on March 30. All directors of the Workers' Compensation Board have been registered.

Mr. Hummel asked the status of the Workers' Compensation Council. Mr. Buehrer replied that he did not know. Neither the House nor Senate of the new General Assembly has named their representatives to the Workers' Compensation Council. The staff of the House Finance and Appropriations had questions, but not the House Committee on Insurance. The Workers' Compensation Council probably has no staff beyond the executive director.

ADJOURN

Mr. Zuk announced that the next meetings will be held April 28 and 29. The Workers' Compensation Board meeting will start at 10:00 a.m. on April 29 because of a scheduling conflict.

Mr. Hummel moved to adjourn. Mr. Palmer seconded and Mr. Zuk adjourned the meeting at 9:10 am after a roll call vote of eleven ayes and no nays.