Workers' Compensation Advisory Committee (WCAC) Meeting
Labor & Industries Tumwater, WA
Meeting Minutes
April 29, 2009

Business Representatives

Jon Warling, Mar-Jon Orchards; Nancy Dicus, TOC Management Services; Kris Tefft, Association of Washington Business; Rebecca Forrestor, Group Health.

Labor Representatives

Karen Gude, United Food & Commercial Workers Union Local 1439; Dave Johnson, Washington State Building & Construction Trades Council; Jeff Johnson, Washington State Labor Council; Owen Linch, Joint Council of Teamsters No. 28.

Labor & Industries

Judy Schurke, Director; Bob Malooly, Assistant Director of Insurance Services.

Recorder

Sharon Avery.

Guests

Holly Chisa, Beverly Simmons, Dan Fazio, Joan Elgee, Dave Kaplan, Jan Gee, Rob Evans, Vicky Smith, Rebecca Johnson, Diana Will, Theresa Whitmarsh, Janice Camp, Terry Tilton, Craig Scukas, Scott Daniels, Kevin Sheehy, Ann Jarvis, Veronica Shakotko.

L&I Staff

Rebecca Linville, Julie Black, Jean Vanek, Josh Ligosky, Ron Moore, Mark Mercier, Denise McKay, Les Hargrave, Cara Hsieh, Dick Bredeson, Karen Peterson, Cheri Ward, Chris Freed, Tiffany Scheer, Brenda Heilman, Diane Doherty, Russ Redding, Roy Plaeger-Brockway, Vickie Kennedy.

Absent

Tom Egan, Board of Industrial Insurance Appeals

Opening Comments and Safety Message:

Ms. Schurke presented a safety message to the committee. The meeting continued with an introduction of the attendees.

The December 8, 2008 meeting minutes were approved.

Updates

Director Schurke provided updates on department personnel changes which included the announcement of Roy Plaeger-Brockway as the Assistant Director of Management Consulting Services (MCS). The new focus for MCS is Business Process Management, which includes "Lean" concepts. Mr. Malooly added that Dr. Mecklenburg, Virginia Mason Hospital's Chief of Medicine, recently presented to the executive management team how they applied lean concepts at the hospital.

Director Schurke noted that Jean Vanek, Self-Insurance Program Manager, has announced that she will be retiring in August, 2009. The department will begin recruiting for her position in the near future.

Denise McKay was introduced as the new Self-Insurance Ombudsman.

Tom Egan was unable to attend this meeting, but was pleased to announce that the Governor has appointed Larry Dittman to serve as the employer member for the term ending June 17, 2011. Copies of the handouts, *WCAC- April 29, 2009* and *State of Washington BIIA Monthly Statistical Report for March 2009*, were distributed.

A *2008 Annual Report for Washington State Fund* was distributed to the committee members.

Mr. Malooly commented on a bill before the US Congress that would establish a National Commission on workers' compensation. If it moves forward, it will be the first evaluation from a national perspective since the National Commission in 1970. It is sponsored by Representative Baca, House Resolution 935.

Financial Reports: Sharon Elias

The presentation, *Summary of Fiscal Year 2008- Workers' Compensation Program Comprehensive Annual Financial Report and Industrial Insurance Fund- Statutory Financial Information Report*, was reviewed.

The financial reports were delivered to the Governor's office, legislators, and OFM. For the third consecutive year, the State Auditor's Office hired Peterson Sullivan and Towers Perrin Tillinghast to conduct the GAAP audit and actuary reviews and both issued clean opinions. The department elected to have the SAP financial information audit for 2008 and also received a clean opinion.

Financial highlights since June, 2007 include:

- The Medical Aid rate holiday from July to December 2007 reduced revenues by $310 million.
- Dividend checks were issued to non-retro employers the last week of June, totaling $36.5 million.
- A new asset allocation was implemented by purchasing international equities and treasury inflation-protected securities (TIPS).
- Retrospective rating adjustments decreased by $36 million.
- Benefit liabilities increased by $536 million.
- Changes in the Washington State average annual wage increased outlays from the Supplemental Pension Fund.
- The downturn in the stock market did not impact us as severely as it might have because the new asset allocation reduced our equity exposure; we gained $13 million from 2007-2008 (from $10,989 billion to $11,003 billion).

- GAAP Financial Highlights:
  - The total deficit in fiscal year 2007 was $8.186 billion. This increased to $10.160 billion in 2008.
    - The deficits are related to the Supplemental Pension Fund. The fund operates on a current payment basis. No assets accumulate.
    - At the last WCAC meeting, it was noted that some adjustments were needed for the 2007 financial statement. This was done on page 26 of the report. $7,688,324 was

redistributed to all other funds. There was no impact to the workers' compensation funds as a whole.

- SAP Financial Highlights:
    - SAP financial statements are for state fund only and include Accident, Medical Aid, and Pension Funds.
    - The contingency reserve decreased from $2,094 billion to $1,602 billion. This was due to the rate holiday, dividend checks, and increases in benefit liabilities.

Both GAAP and SAP annual financial reports are available at the Labor and Industries website at: www.Lni.wa.gov/ClaimsIns/Insurance/Learn/StateFund/Reports/.

The presentation, *Statutory Financial Information Industrial Insurance (State) Fund 2nd Quarter Fiscal Year 2009 As of December 31, 2008*, was reviewed.

Financial Highlights of Fiscal Impact include:

- Due to market turmoil, the agency lost $446 million in realized and unrealized investments.
- The department received $17 million from the Enron settlement which was re-invested.
- The retro rating adjustment liability was reduced $14.6 million due to recent changes. (**Note: there was a typographical error on the presentation handout. It is listed as **$46 million** and should be corrected to **$14.6 million**).
- Benefit liabilities increased $262 million to total $9.6 billion.
- The state fund continues to weather the market turmoil with relatively small losses due to an excellent investment strategy.
- In comparison to fiscal year 2008, investments dropped $276 million to total $10.7 billion.
- Benefit liabilities increased from $9.3 billion to $9.6 billion.
- The contingency reserve continues to decrease but stays within the policy range. The entire state fund contingency reserve balance was $1.6 billion as of June 30, 2008. That is a $532 million decrease from the prior year. $963 million is considered the bottom of the range.
- The Accident and Pension Fund contingency, as of December 31, 2008, is 7.3%--slightly lower than the low-end of the policy range of 7.4%.
- The Medical Aid Fund, as of December 31, 2008, is 17%; between the mid- and lower points of the range.

Mr. Malooly added that at the June 22, 2009 WCAC meeting, a review of the rate indications for 2010 using first calendar quarter results will be on the agenda.

Copies of the handouts were distributed:

- *Industrial Insurance (State) Fund Interim Statutory Financial Information for the Second Quarter of Fiscal Year 2009 December 31, 2008, Industrial Insurance Fund Statutory Financial Information Report for fiscal year ended June 30, 2008*
- *Workers' Compensation Program – Comprehensive Annual Financial Report for the fiscal year ended June 30, 2008*

State Investment Board Presentation: Theresa Whitmarsh and Diana Will

Copies of the presentation, *Workers' Compensation Advisory Board: Labor and Industries' Funds Portfolio Review, April 29, 2009*, were distributed.

Ms. Whitmarsh began the presentation with an introduction of herself and Diana Will. The Washington State Investment Board (WSIB) was created in 1981 to manage the long term assets of the state. The WSIB is comprised of 15 members, ten voting members and five non-voting members. The WSIB invests for 39 funds including 17 retirement funds, 4 state insurance funds for injured workers, and 18 other trust funds. L&I is the single largest client for WSIB. The presentation focused on an overview of the WSIB, Labor and Industries' funds investment policy, and the March 31, 2009 portfolio data.

On slide 6, it was asked to clarify the term 'your peers'. Ms. Whitmarsh explained it includes other institutional investors including Calpers [California Public Employees Retirement System], Calsters [California State Teachers Retirement System], Canadian funds, European funds and other public retirement funds.

On slide 7, Ms. Will continued the presentation with a review of Labor and Industries funds strategic goals. They are:

- Maintain the solvency of the funds.
- Maintain premium rate stability.
- Ensure sufficient assets are available to fund the expected liability payments.
- Subject to those above, achieve a maximum return at a prudent level of risk.

On slide 8, the policy guidelines were reviewed:

	Fixed Income	TIPS	Equity
Accident Fund	80%	10%	10%
Pension Reserve Fund	80%	10%	10%
Medical Aid Fund	65%	20%	15%
Supplemental Pension Fund	100%	0%	0%

Department asset allocation as of March 31, 2009:

	Fixed Income	TIPS	Equity	TOTAL
Accident Fund	80.8%	11.3%	7.9%	$4,084 million
Pension Reserve Fund	81.8%	10.4%	7.8%	$2,735 million
Medical Aid Fund	66.4%	22.1%	11.5%	$3,616 million
Supplemental Pension Fund	100%	0%	0%	$66 million

Rebalancing occurs when assets fall outside of the policy ranges; however, the timing of rebalancing is based on market opportunities, cash flows, and consideration of transaction costs. The WSIB has been slow to rebalance due to the volatility of the market and the high transaction costs.

On slide 9, Ms. Will explained that each asset class managed has policy guidelines: fixed income sector allocations, duration targets, and actual duration. As of March 31, 2009, L&I's combined funds are mostly invested in corporate bonds.

On slide 10, the TIPS portfolio is managed against the Barclays Capital US TIPS index. TIPS are purchased and held until they mature and are then replaced with a new issuance. These bonds are purchased to give the funds inflation protection. The only concern for TIPS is they are inflation adjusted against the CPI, which is the total U.S. inflation index. Over the past seven years, the CPI has increased 2.5% and medical inflation is over 4% annually. The inflation bonds do not match the inflation of the costs, but it does provide some protection.

On slide 11, the data shows the equity allocation as of March 31, 2009. The US equities are targeted to be 60% while international equities are 40%. This changed in February, 2008 as international equities used to be 15%.

It was decided that the international equities provided more diversification and, in the long run, would be a more stable portfolio.

On slide 12, Ms. Will remarked that the data reflects a bad year for the one-year returns:

- Accident Fund--down 4.05%
- Medical Aid Fund--down 6.3%
- Pension Reserve Fund--down 4.79%
- Supplemental Pension Fund--up 1.66%

However, a comparable market index (CMI) was significantly lower than our portfolios. The difference was:

- L&I's portfolio reflects that we did not rebalance quite as fast as others.
- We were "underweight" in the low performing asset classes, which helped our returns. The overall TIPS index return was down 2%, while L&I's portfolio was only down 1.2%.
- The main portion of returns came from the fixed income active management. Long-term financial credits were down 25%. L&I did not own any of these.
- Thirty-year treasuries were up 17.94% for the quarter while long financials were down 25.45%, which is an incredible difference in return for fixed income securities. You would typically expect this in equities, but not bonds. Being in the right types of securities this quarter is what helped the fixed income portfolio to outperform their index.

Contact Information for additional questions:
Website: www.sib.wa.gov
Phone: (360) 956-4600

Mr. Malooly remarked that the WSIB does an excellent job for the department. The quality of investments is outstanding. Although last year's performance was negative given the market turmoil, the funds out performed the benchmarks by 3.0-3.5%. This is unheard of in fixed income portfolios.

Trends in Property Casualty and Workers' Compensation: Scott Daniels, Conning

Copies of the presentation, *Workers' Compensation Advisory Committee: Insurance Trends*, and the handout, *Workers' Compensation Advisory Committee, April 29, 2009*, were distributed. Mr. Daniels began with an introduction of himself. He echoed Mr. Malooly's comments regarding the WSIB's performance.

On slide 8, it was clarified that Conning is forecasting a recovery in premium growth to 3.8% in 2010, assuming the economy turns around.

On slide 12, Mr. Malooly commented that the rates referenced are per $100.00 of wages paid. Our rates are based on hours worked, so an adjustment would need to be made for an accurate comparison. When a jurisdiction has a zero rate increase but the rates are based on salary, they automatically receive more premium dollars due to wage inflation. For Washington, if there is wage inflation, we need a rate increase to cover the wage inflation costs. Insurers in other states can claim no increase in these cases, when in fact they did see an increase in premiums.

On slide 14, a question was asked about Mr. Daniels' thoughts regarding AIG's formation of a new company, AIU, and what effect that may have on the insurance market. Mr. Daniels remarked their property/casualty lines tend to be profitable and it is large enough to be a stand-alone entity, so they are expected to remain a competitive force.

On slide 15, it was asked if stimulus money is taken into consideration for the underlying assumptions. Mr. Daniels responded that stimulus money will take 6-12 months to have an impact on the market. Overall, it is anticipated that by 2010 the market should improve and become more stable.

Mr. Malooly had a question regarding the long-term view of investments and if the yield on investments is going down over time. This would mean that more of the cost of insurance would be borne by the premiums if this is a long-term trend, which Mr. Daniels felt that it is. Conning's equity expectations are for an 8.5% return, which is lower than the historical 10-11% annual return. Mr. Malooly added that Washington is compared to other states on the cost of workers' compensation insurance. The insurance cycle goes from "boom to bust." For instance, during the "boom," private carriers would often greatly reduce coverage costs to gain market share and the resulting, artificially low prices make Washington coverage look expensive. During the "bust," private carriers retreat from the market or raise prices significantly, which can make coverage so expensive that small businesses cannot afford insurance. Such a cycle was seen in California in the 1990s and early 2000s. A large number of California workers' compensation companies went out of business in this period, and the California state fund's premium volume quintupled. Washington's goal is to have smaller variations in rates, taking rate increases only when necessary. We want to keep rates as stable as possible so we have a predictable business climate.

Regarding the discussion on small businesses struggling to access insurance in some states, it was asked how large businesses compared. Mr. Daniels answered that larger businesses generally had an easier time, since they have more bargaining power, greater sophistication, and are able to deal with national workers' compensation players.

It was asked whether, in the private market, small employer groups are treated the same as big businesses because of the amount of premium. Mr. Daniels remarked yes, that is the attraction of forming different groups to get more leverage and be able to offer insurers a larger block of premiums.

Experience-rating of the Second Injury Fund Assessment for Self Insured Employers: Jean Vanek

Copies of the handouts, *Experience Rating of the Self Insurance Second Injury Fund Effective July 1, 2009* and *Draft Proposed Rules*, were distributed.

Ms. Vanek informed the committee regarding the implementation of experience rating the Second Injury Fund for self-insurers as required by legislation passed in 2005. This legislation directed the department to experience rate 50% of the second injury assessments. Determining the experience rates requires three years of data on the individual employers' use of the fund. This change is effective July 1, 2009, and will use data for fiscal years 07-09. The CR-102 is being filed this week. There is a public hearing scheduled at the Town Center on May 26, 2009 at 9:00am.

The Second Injury Fund was established statewide shortly after World War II and was primarily focused on veterans returning to the workforce. Some of the veterans had disabling conditions that may have limited their employment opportunities. When an employer hires someone with a pre-existing disabling condition, work-related or not, and the worker sustains a second injury, if the worker is permanently totally disabled, a decision is made about whether the pension is due to the combined effects of the new injury and the earlier disabling condition. When it is, the employer is eligible for second injury fund relief. Eighty-five percent of all self-insured pensions receive some second injury relief. This is a significant impact to the self-insured community as a whole.

Regarding the assessing of inactive accounts discussed in the handout, it was asked if employers are paying into the insolvency trust as well. Ms. Vanek answered that those employers pay certain assessments for three years following their inactive status, but it is on a declining basis. They have never been assessed for the Second Injury Fund. To clarify, this was not specifically directed by the legislation; the department reviewed this and is proposing the addition of this assessment of inactive accounts as part of the new rule. Once these employers have no claim costs to report, their assessment rates will drop.

Ms. Vanek reviewed the "Experience Rating of Second Injury Fund: Active Self-Insureds" pie chart. It was asked if the department knows the employers who will pay more than 150-200% of their current assessment and if those employers have been informed. The department confirmed that the employers have been identified, but have not been alerted yet. Employers who use the fund extensively should be aware. However, there will be a specific mailing for the inactive accounts because this is probably not on their radar.

Ms. Vanek added that the legislation requires a study of impacts of experience rating. There was significant concern on behalf of labor that this change could potentially cause an employer not to move claims to pension if their costs would increase. The research study methodology will be ready to present to the committee by the August meeting.

Ms. Vanek was asked for her thoughts on bankruptcy rates for self-insurers. Ms. Vanek has seen an increase in defaulting self-insured employers. Last week, the program received a notice of default from the Associated Grocers, a company that has been self-insured since 1979.

Ms. Forrestor commented that she participated in groups that researched the Second Injury Fund and looked at alternatives. The 85% of self-insured claims with Second Injury Fund is down from 96% in the late 1990s. When alternatives were reviewed from the complete socialization to assuming the full value of pensions, this new methodology was in the middle. Even with the use of experience rating, most employers would be paying less than if they fully funded the pension. The employers in the higher-use categories probably have significant claim costs and are considered extreme. The group was optimistic about this approach and based on three-quarters of employers expected to pay either the same assessment or less, it appears the goal of the legislation is being achieved.

Legislative/Budget Update: Vickie Kennedy

Copies of the following handouts were distributed:

- *2009 L&I Legislative Summary.*
- *Key 2009-11 Workers' Compensation Budget Items.*
- *Ongoing Implementation and Follow-Up Items.*
- *Department of Labor and Industries 2009-2011 Budget Passed Legislature April 26, 2009.*

Ms. Kennedy remarked that the department fared well in the final budget given the current circumstances, partly due to the department prioritizing what was important to make significant improvements in how we do business.

The *2009 L&I Legislative Summary* handout was reviewed.

A concern was raised regarding the various legislation concerning medical costs and utilization and the legislators' interest in uniformity in policy and procedures. It was expressed that they hope the department has a strong presence in various groups created by the bills. The goal of workers' compensation is different than other healthcare delivery systems and our goals should not be modified for conformity. Ms. Kennedy indicated the legislative staff expects the department to take an important role and carry the message of what works for the system and recognize the efficiencies where we can gain from a consistent process.

On SSB 5613 (authorizing L&I to issue stop work orders to contractors that do not have any industrial insurance coverage), it was asked to clarify that this was for unregistered contractors, not for a company that had an account with disputes on uncovered workers. Ms. Kennedy confirmed that it pertains to contractors without an account as opposed to under-reporting.

It was asked what happens if the general contractor is self-insured. Does the Supreme Court decision in the Stute case have any application? Ms. Kennedy answered that the general contractor should be confirming that their subcontractors are in "good standing" with the department and have an active account. (The Stute decision discussed the responsibility of the self-insured/prime contractor for worker safety of employees of a subcontractor.) This did not come up as a question or concern during the legislative session. It is assumed this is because the legislative discussion focused on unregistered contractors who have no account. These unregistered employers are considered the underground economy.

Regarding E2SSB 5688 (expanding the rights and responsibilities of state-registered domestic partners), it was asked if this only applies to same-sex domestic partners. Ms. Kennedy clarified it does not apply to opposite-sex couples, except those where one partner is age 62 or over.

On SSB 6158 (delaying the implementation of the Family Leave Insurance program), it was asked if any money had been loaned from this fund. Ms. Kennedy answered $29,000 had been loaned to the Employment Security Department (ESD) and has since been re-paid.

The *Key 2009-11 Workers' Compensation Budget Items* handout was reviewed.

Retrospective Rating: a question was asked about the $500,000 allotted for the department to contract with independent consultants for the retro program. Director Schurke answered that as the department moves forward implementing any recommendations that come from the retro proviso study, we will need to continue to have independent actuarial oversight.

It was commented that one of the improvements in retro that stakeholders have asked for concerns the ability to conduct trending analysis for individual groups, although this can be done for individual employers. Mr. Malooly remarked that one issue with the retro program is to the lack of accessibility for people who do not understand the fundamentals involved with retro. We need more user friendly explanations so people can take better advantage of the program.

More robust audit system for Self-Insurance: clarification was requested on what "targeted audit approach" and "changes in audit elements" were. Ms. Kennedy answered it may change how we approach an audit and who we audit. Director Schurke added that this refers to the strategic plan. The department is working toward not having self-insured employers on a regular cycle for an audit, but to be able to categorize employers who have consistently had positive results on their audits to come up on a less-frequent basis. In addition, the department will be able to have a focused approach toward what we audit.

It was commented that more consistency is needed in terms of how audits are conducted.

Ms. Vanek added that the package is a technology package. The technology will enable the Self-Insurance program to revisit the premise to which we audit, the components of the audits, and what data should be focused on during an audit. The goal is to increase compliance and that every self-insured worker receives the benefits they are entitled to.

In a future meeting, the department plans to link the budget items to the strategic plan for further discussion with the committee.

SHIP grants: it was asked if this was funded. The original grant was for $8 million and the funds that were unspent will carry over to the next biennium.

Community Agricultural Safety: a question was asked of the division of the $500,000 from 608/609 funds. It is 85% Accident Fund and 15% Medical Aid Fund.

Director Schurke added that she had a conversation with the director of the Agriculture Department and has committed to sending a letter that explains the oversight of our SHIP grant program and how return on investments is determined.

Lastly, a question was asked if the policy-level budget items would be implemented with the hiring freeze. Ms. Kennedy clarified that the hiring freeze legislation bill is only through the current biennium. Each agency will have individual budgets to work within as of July1, 2009.

Sector Analysis: Felix D'Allesandro

Mr. D'Allesandro, Research and Data Services Program Manager, presented an industry sector study. Claims received are trending down and the department wants to analyze which industries are accounting for this decline. This analysis is in the beginning stages of data gathering. The handout is a drill down of the construction sector. The data reflected is the most current data available.

On slide 2, Mr. D'Allesandro reviewed the Industrial Sector Analysis table:

- Establishment: Data is from ESD.
- Safety Inspections 2008: Data from DOSH.
- Employers Offering Health Insurance: Data from ESD survey.
- Employment (Workers Share): Distribution of workers across industry.
- Unemployment Exhaustion Rate: Data from ESD.
- Injury Claims Received: Total of both medical and compensation claims. All Reports of Accident (ROA) are counted.
- Active Time-Loss: How many people are on active time-loss at any given time?
- Time-Loss, Return-to-Work: Injured workers who were on active time-loss are cross-matched with ESD wage data. This measures the percentage of workers who returned to work within a year of their date of injury.

It was noted that, over the last year, the construction sector accounted for 17.20% of all injury claims received. Mr. Malooly added that construction is a very high hazard industry, especially home/residential construction.

On slide 13, a dramatic drop in claims received is observed. Mr. D'Allesandro remarked that the construction sector has recently shed many jobs and there are many fewer hours of exposure. Mr. Malooly added that the economic downturn is causing less claims to be submitted to the department. We expect that when the economy recovers, and workers return to work, injury rates may rise significantly.

On slide 14, data show that the number of workers on active time-loss is increasing. This increase may be due to workers not having positions to return to. This may ultimately affect the Supplemental Pension Fund.

A comment was made regarding the observed decrease in new claims received. The source of increasing time-loss claims may reflect an observed increase in complex claims. Mr. Malooly confirmed that the incoming claims are down; however, the duration of claims may be rising due to the complexity of the claim and more claims with multiple diagnoses.

Next Meetings:

The next WCAC meeting is scheduled for June 1, 2009 in Tumwater. This is a special meeting focused on Centers of Occupational Health and Education. The next regular WCAC meeting is scheduled for June 22, 2009 in Tumwater.

Handouts included:

- *L&I- Industrial Insurance Only: Rulemaking Activities.*
- *Employer Services' Rules Filings Memo.*
- *Employer Services' Classification Plan Maintenance Model Memo.*
- *Office of the Medical Director's Proposed Rule-making on Psychiatric ARNPs.*
- *Office of the Medical Director's Proposed amendments to the Medical Aid Rules.*

Meeting adjourned.