Workers' Compensation Advisory Committee (WCAC) Meeting
Labor & Industries Tumwater, WA
Meeting Minutes
November 10, 2010

<u>Business Representatives</u>: Kris Tefft, Association of Washington Business; Rick Anderson, Sakuma Bros; Nancy Dicus, Vigilant; Rebecca Forrestor, Group Health

<u>Labor Representatives:</u> Rebecca Johnson, Washington State Labor Council; Owen Linch, Joint Council of Teamsters No. 28

<u>Labor & Industries:</u> Judy Schurke, Director; Bob Malooly, Assistant Director of Insurance Services

<u>Board of Industrial Appeals:</u> Dave Threedy

<u>Recorder:</u> Sharon Avery

<u>Guests:</u> Dave Kaplan, Mike Evans, Frank Romero, Carolyn Logue, Jim Brownell, John Meier, Brian Bishop, Dennis Kelley-Jones, Joan Elgee, Jeannie Gorrell, Ann Jarvis, Jerry Bonagofsky, Paulette Avalos, Lauren Gubbe, Clif Finch, Janice Camp, Art D'Alessandro, Lloyd Brooks, Rick Slunaker, Scott Dilley, Cody Arledge, Trish Leimbach, Holly Chisa, Beverly Simmons, Larry Stevens, Tammie Hetrick, Kim Hoff, James Paribello, Kathleen Collins, and Tonia Sorrell-Neal

<u>L&I Staff:</u> Vickie Kennedy, Tamara Jones, Elaine Fischer, Bill Vasek, Sharon Elias, Kirsta Glenn, Keri Smith, Joshua Ligosky, Rebecca Linville, Mark Mercier, and Mike Ratko

<u>Opening Comments and Safety Message</u>

The safety message was presented by Mr. Malooly. The meeting continued with an introduction of the attendees.

The June 23, 2010 minutes were approved with the correction to Nancy Dicus' contact information from Vigilant Counsel to Vigilant.

<u>Updates: Bob Malooly</u>

The packets include follow-up information from the June WCAC meeting.

Mr. Malooly provided an update on the Supplemental Pension Fund (SPF) loans which have been necessary due to the downturn in reported hours resulting in inadequate premiums to pay required cost-of-living adjustments for long-term claims (the SPF is statutorily a pay-as-you-go fund and the department cannot accumulate reserves as is done in the other funds). The first loan was for $15 million in April 2010. The second loan was for $25 million on July 13, 2010, and the third loan was for $25 million on October 13, 2010. The first two loans have been repaid and the third loan will be repaid in mid-November.

The Workers' Compensation Research Institute (WCRI) is conducting two studies: one to examine prescription patterns and one of shoulder and knee injuries. The WCRI conducts an extensive report for the states included in CompScope—this is a comprehensive comparison limited to 18 participating states. The draft report regarding pharmaceuticals is due January 29, 2011; the draft report on knee and shoulder conditions and medical practice patterns is due March 31, 2011, and final reports are due July 30, 2011.

<u>Board of Industrial Insurance Appeals (Board) Update: Dave Threedy</u>

The presentation was reviewed.

- *<u>Appeals Filed and Granted per Quarter:</u>* There were 3115 appeals filed and 1781 appeals granted last quarter.
- *<u>Department Reassumption Rate by Quarter:</u>* The reassumption rate is 26%. The number of appeals reassumed by the department has remained fairly constant over the fiscal year.
- *<u>Average Proposed Decision and Order (PD&O) Time-lag by Quarter for Hearing Judges:</u>* This is at 31 days, which is a slight increase from the last quarter. At the beginning of the calendar year, the Board hired several new judges. New judges take a little more time to get their decisions completed because the Board conducts intensive reviews of their decisions before they are issued.
- *<u>Decision and Order (D&O) Time-Lag by Quarter:</u>* It is taking a total of 63 days for the Board to issue a Decision and Order after a Petition for Review is filed. The Board members are taking about the same time to issue the orders; there is an increase for the judges. The review judges who draft the D&Os are seeing an increase in the time spent on stay motions. The number of stay motions received per month are up three from the same month in the previous year.

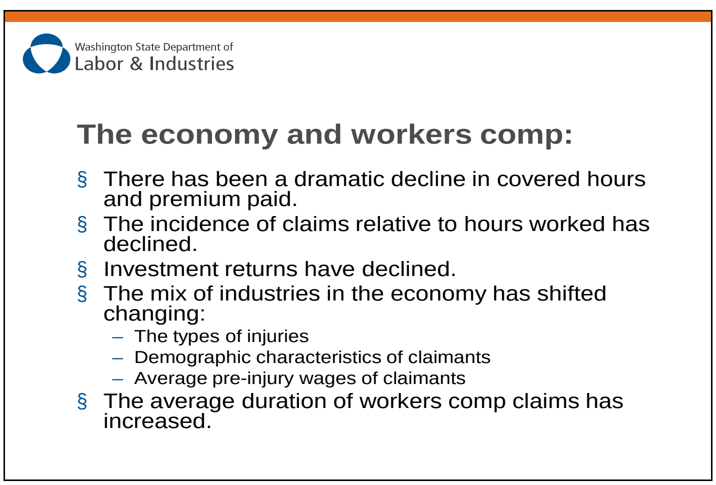
It was requested that Mr. Threedy provide a breakdown of the number of stays that are granted versus the number of stays being denied at the next WCAC meeting. Mr. Threedy agreed to provide these numbers at the next meeting.

- *<u>Quarterly Average Weeks to Completion</u>*: As of September 2010, the average weeks to completion is 32.5 weeks.
- *<u>Caseload at End of Quarter</u>*: The active appeals have decreased from last quarter to 4,533.

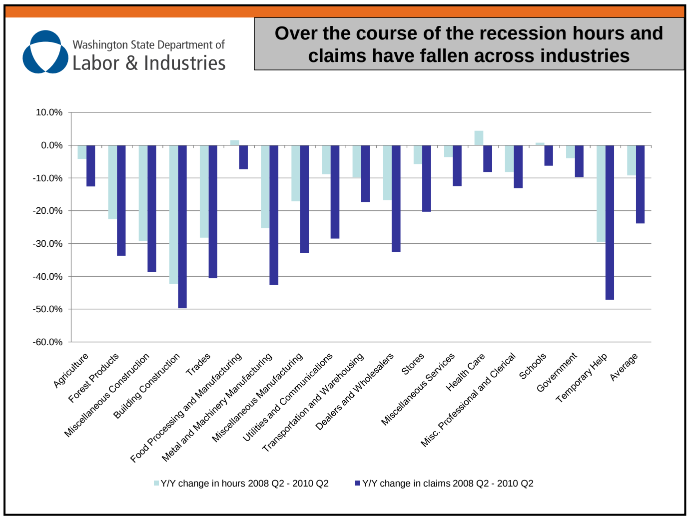
A question was asked regarding Report 411—is the settlement rate holding steady? Mr. Threedy answered yes; he has not noticed any change in the settlement rate.

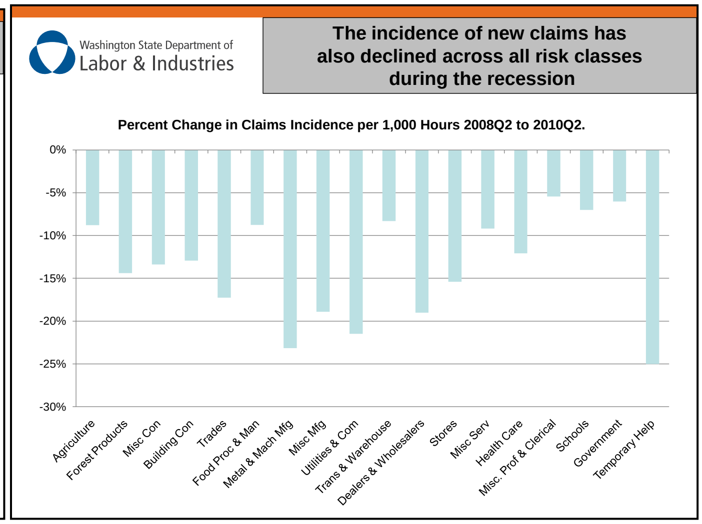
<u>Economic Update: Kirsta Glenn</u>

Ms. Glenn, Research and Data Services Program Manager, presented an economic update and how it relates to the workers' compensation system.

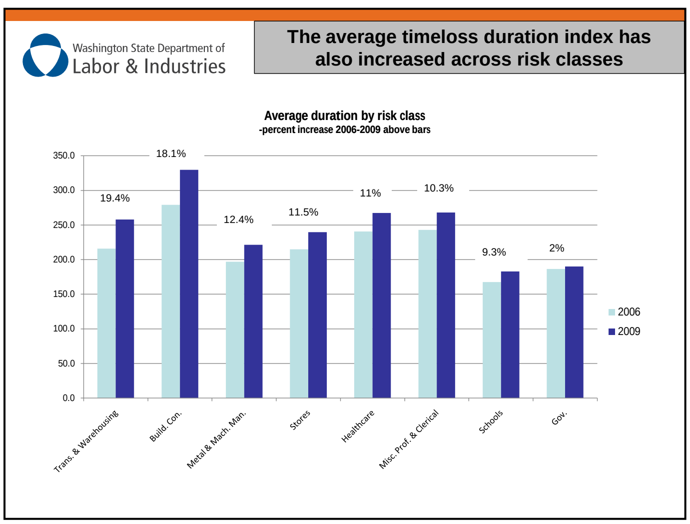


Slide 2 explains there is a definite effect of the economy on the operations of the workers' compensation system. The incidence of claims relative to hours worked has declined. This has been a national long-term trend. During the recession, we have seen the rate of the decline go down more quickly. This occurs because businesses tend to lay off their most inexperienced or younger workers who typically have higher rates of injuries. Research has also shown that workers may be hesitant to file claims during a recession because they are afraid their jobs could be eliminated.





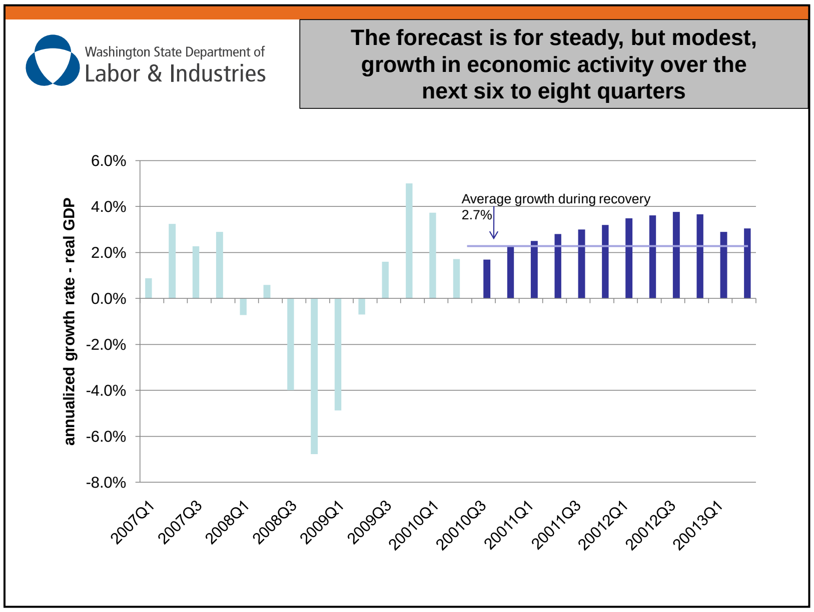
The charts on slides 3 and 4 show the experience of different risk classes from the 2nd quarter in 2008 to the 2nd quarter in 2010. These charts show that while both hours and claims filed have fallen across industries, claims have fallen by more than hours in all industries.



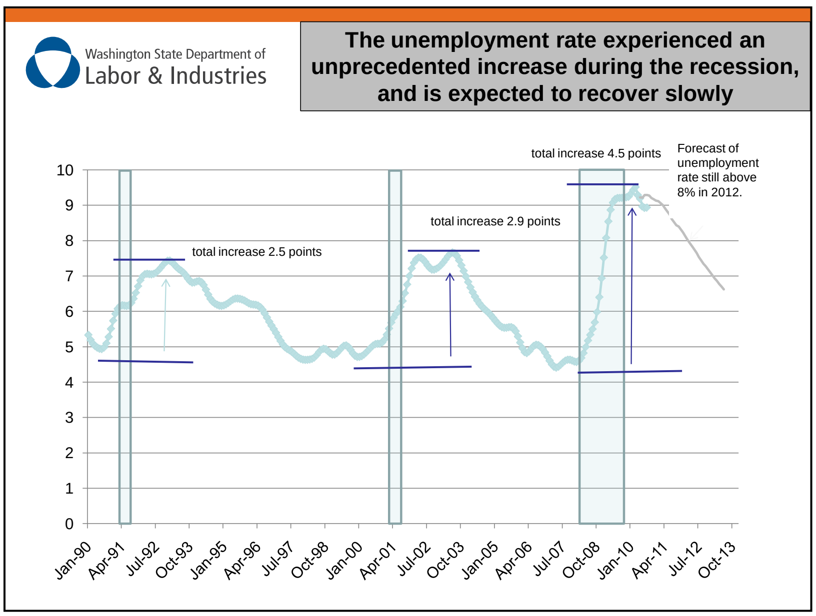
Slide 5 explains the average time-loss duration by industry for 2006 and 2009. The increase in duration has been systematic across all risk classes. However, the rate of increase differs for the various risk classes. Building construction duration increased by 18.1% between 2006 and 2009 while government duration increased 2%.

A question was asked if there is corresponding data from the 1990s or earlier recessions that could be reviewed. Ms. Glenn answered she was unable to go back to the 1990 recession data. She further explained that this recession was deeper than any other recession we have experienced and the change in the construction industry is unprecedented. Mr. Vasek will provide more details in his presentation.

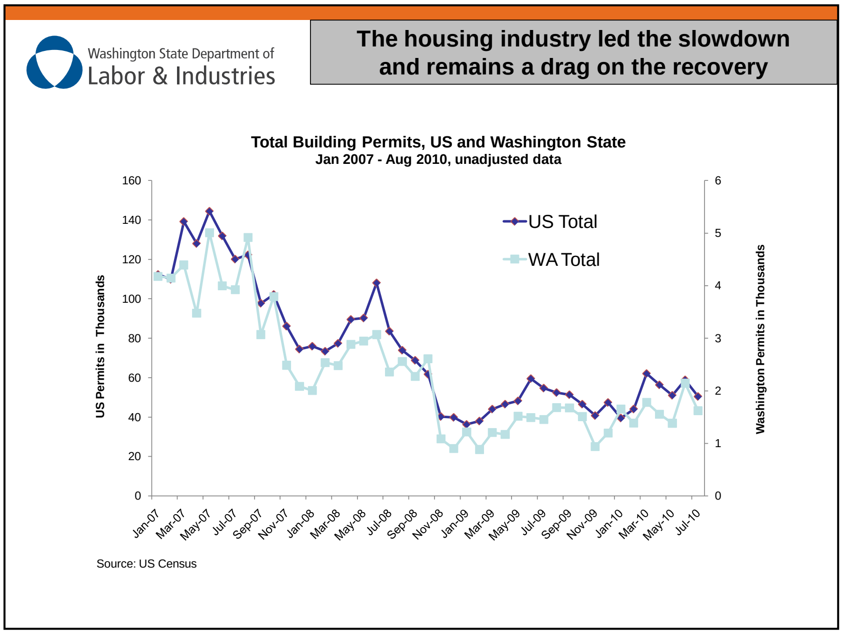
Mr. Malooly added an article from the Insurance Journal was provided in the packets that explained the problem with growing duration is a national issue, not exclusive to Washington State. This data was based on individual insurance company reports and NCCI studies.



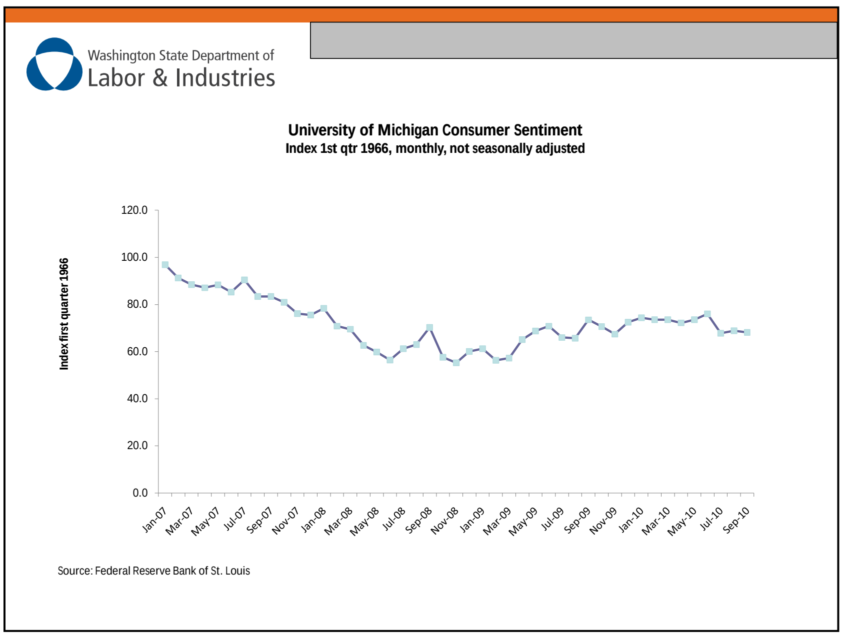
The chart on slide 6 shows the economic forecast. The economic recovery is expected to be steady, but slow. There is concern about the possibility of a double dip; the consensus economic forecast is still for a slow and steady recovery over the next six to eight quarters.



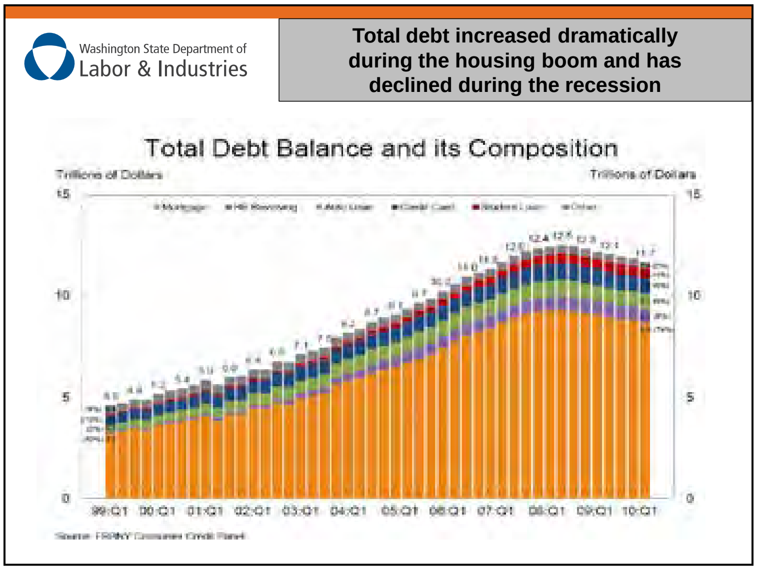
On slide 7, the highlighted boxes in the graph show the different recessions. This graph highlights how much longer this recession was than our previous recessions and it reflects the dramatic increase in the unemployment rate that occurred during the recession. In Washington State, the unemployment rate peaked at 9.5% in January 2010 and has slowing been decreasing. The current forecast of the unemployment rate is still above 8% in 2012. This forecast is higher than the peak unemployment rate in our previous recessions.



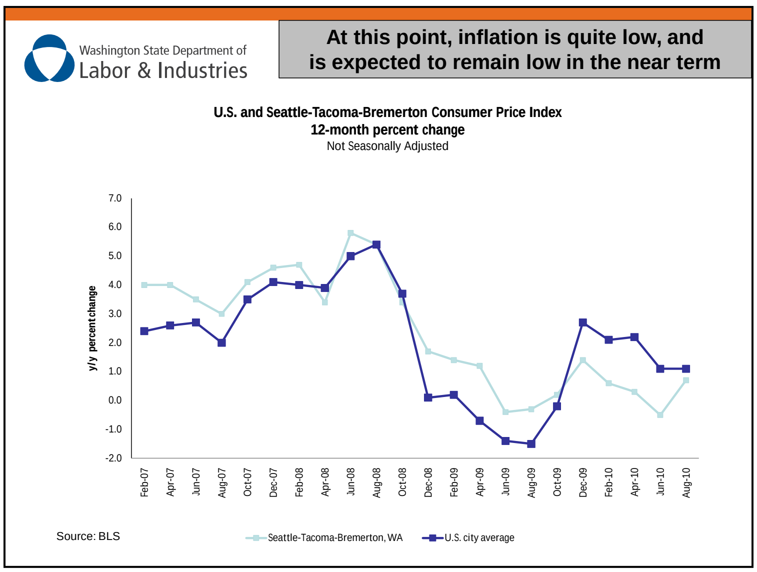
The chart on slide 8 shows that the housing industry led the slowdown and remains a drag on the recovery. Building permits are low, and it is estimated that from 2007 we have six years of housing inventory on the market. A report from last month noted that Seattle had the highest increase in foreclosure rates in the country. It is expected that the construction and housing industries will recover slowly.



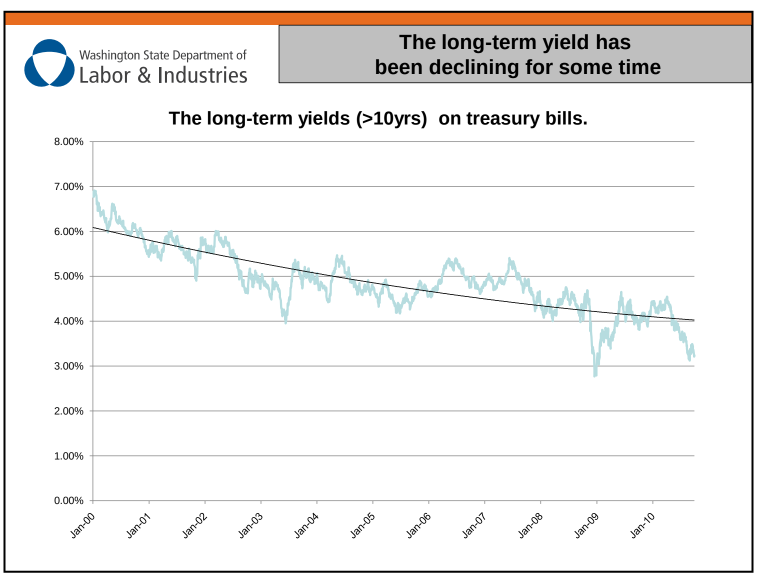
The graph on slide 9 reflects consumer confidence. It is relatively low at less than 80%. As long as consumer confidence is low, consumers will be hesitant to make purchases. Consumers are now saving more. Consumer spending is currently about 70% of the total demand in the economy.



Slide 10 shows the total debt increased dramatically during the housing boom and has declined during the recession. This is a reflection of consumer savings.



The chart on slide 11 shows the US and Seattle Consumer Price Index. Inflation is low and is expected to remain low in the near term. Low inflationary expectations and a decline in lending have allowed the Federal Reserve Board to put a lot of money into the economy without it affecting the inflation rate. There remains some possibility of either deflation or high inflation.



On slide 12, the chart explains the long-term yield on Treasury bills. The long term yield has been declining for some time. In January 2000, it was 6% and is currently at 3%. The Federal Fund rate is so low that the Federal Reserve Board cannot take it any lower. They are directly putting money into the economy to try to stimulate growth because inflation, at this point, is not a danger.

In conclusion:

- § The agency and all of its customers groups have been put under economic stress from the Great Recession.
- § We expect economic conditions to only slowly improve over the next two years.
- § One of our most important customer groups, construction firms and workers, will see a slower than average recovery.
- § Market returns are not expected to return to the rates of the mid-2000's.

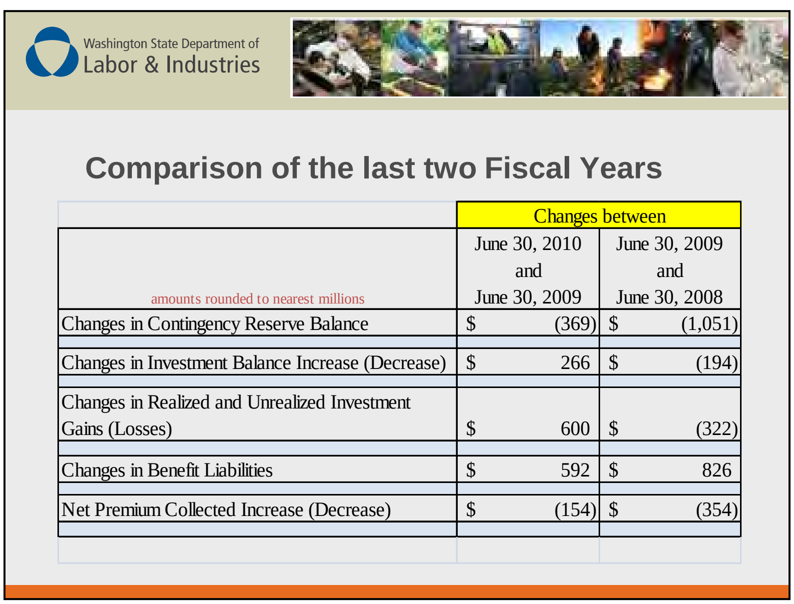
A question was asked referring to slide 2: what is the average duration of workers' compensation claims? An answer would be provided in the rates presentation. Mr. Malooly referred to additional material in the packet regarding the duration of time loss benefits in Washington State versus the nation.

Financial Update: Sharon Elias

The presentation *Industrial Insurance (State) Fund Unaudited Statutory Financial Information: Fiscal Year 2010- Fourth Quarter (As of June 30, 2010)* was reviewed.

The financial highlights for the fourth quarter include cumulative changes since June 30, 2009:

- The contingency reserve balance was $181 million as of June 30, 2010. The overall decrease of $369 million for the last four quarters was the result of better than expected investment and negative operating results.
- Total investments increased by $266.4 million as of June 30, 2010, compared to June 30, 2009.
- Total realized and unrealized gains on investments were $196.8 million.
- Benefit liabilities increased by $591.7 million since June 30, 2009. This is mainly due to injured workers staying on benefits longer, increasing number of pensions and increasing time-loss duration.
- The net premium collected during Fiscal Year (FY) 2010 decreased by $153.9 million compared to FY2009. Due to economic conditions, fewer people are working and we have a reduction in the number of hours and premium reported by employers.



amounts rounded to nearest millions	Changes between June 30, 2010 and June 30, 2009	Changes between June 30, 2009 and June 30, 2008
Changes in Contingency Reserve Balance	$ (369)	$ (1,051)
Changes in Investment Balance Increase (Decrease)	$ 266	$ (194)
Changes in Realized and Unrealized Investment Gains (Losses)	$ 600	$ (322)
Changes in Benefit Liabilities	$ 592	$ 826
Net Premium Collected Increase (Decrease)	$ (154)	$ (354)

Chart 4 is a comparison of the last two fiscal years. This table shows the continued negative effects from the economic downturn. The impact on FY 2010 was significantly less than it was in FY 2009. In FY 2009, the contingency reserve decreased $1.1 billion, while the decrease was less severe during FY 2010 with a $369 million decrease.

Another example is the change in benefit liabilities. From FY 2008-FY 2009, benefit liabilities increased $836 million; From FY2009-FY 2010, the increase was a more moderate $592 million.

Total Investments:

- Total investments increased by $266 million to $11.075 billion from $10.809 billion.
- In FY 2010, we had realized gains of $17.7 million compared to $41.5 million realized losses in FY 2009.
- Total unrealized gains in FY 2010 was $179 million compared to $361.7 million total unrealized losses during FY 2009.

Benefit liabilities:

- Compared to June 30, 2009, benefit liabilities increased by $591.7 million to $10.748 billion in the last four quarters.
- The benefit liabilities increased mainly due to injured workers' increasing number of pensions, increased time-loss duration and the increase in medical costs.

At the last WCAC meeting, questions were asked if we have enough money to pay benefits. Most money for the state fund is invested by the Washington State Investment Board to pay for the future costs of current claims. As of June 30, 2010, we have $11.076 billion to pay for $10.748 billion in benefit liabilities. The difference between these two numbers is the contingency reserve and other liabilities. If needed, we are able to sell investments to pay benefits. There are no cash flow issues related to our future benefit payments.

Tobin v. L&I was resolved by the Supreme Court in favor of the plaintiff. As a result of this decision, the net benefit liabilities increased by $41.2 million for the state fund and for the unfunded liability of the Supplemental Pension Fund increased $124.5 million.

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Fiscal Year to Date Change in Benefit Liabilities
As of 6/30/10 (in thousands)

	Accident Fund	Medical Aid Fund	Pension Reserve Fund	Totals
Benefit Liability as of June 30, 2009	$ 3,940,013	$ 3,168,101	$ 3,048,607	$ 10,156,721
New Benefits incurred since June 30, 2009	860,833	682,631	2,893	1,546,357
Development on prior liabilities as of June 30, 2010:				
Discount accretion	88,910	73,919	187,814	350,643
Other development on prior liabilities	276,783	(117,045)	38,443	198,181
Claim payments	(615,528)	(604,795)	(323,843)	(1,544,166)
Establishing state fund pension awards	(241,368)	-	241,368	-
Establishing SI 2nd Injury pension awards	-	-	40,693	40,693
Change in Benefit Liability	369,630	34,710	187,368	591,708
Benefit Liability as of June 30, 2010	$ 4,309,643	$ 3,202,811	$ 3,235,975	$ 10,748,429

This table summarized the benefit liabilities.

We ended the last fiscal year (June 30, 2009) with a total benefit liability of $10.157 billion.

- We had new liabilities of $1.546 billion.
- There was unfavorable development of $548.8 million due to discount accretion and other development.
- The total claims paid during the year was $1.544 billion.
- The net changes in liability was $591.7 million.
- The total benefit liability as of June 30, 2010 was $10.748 billion.

<u>Contingency reserve balances:</u>

- The contingency reserve balance as Of June 30, 2010 was $181 million.
  - The Accident Fund and Pension Reserve portion of the balance is negative $358 million. The Medical Aid Fund portion is positive $539 million.

Ms. Elias provided a summary of the results for Fiscal Year (FY) 2010:

- We started the fiscal year (July 1, 2009) with a Contingency Reserve balance of $550.2 million.
- We had actual realized and unrealized investment gains of $196.8 million. (Our actuaries expected investment gains of $98.5 million.)
- For insurance operating results we had:
  - Unfavorable prior year loss of $223.7 million.
  - Increase in loss liabilities for Tobin Case -- $41.2 million.
  - Current FY operating loss of $223.7 million.
  - The change in the Contingency Reserve was $369 million. As of June 30, 2010, the Contingency Reserve balance is $181.2 million.

It was asked for the department to provide further details of the Tobin decision. Mr. Malooly answered that an extensive presentation will be provided at the next WCAC meeting.

<u>Supplemental Pension Fund: Pay-as-you-go versus Prefunding- Bill Vasek</u>

The *Supplemental Pension Fund pay-as-you-go vs. prefunding* presentation was reviewed.

This presentation explains the consequences of converting the current pay-as-you-go approach to a pre-funding approach (which is used for the Accident and Medical Aid Funds).

Some History

- Original funding of COLA on timeloss and pension benefits came from the state's General Fund – pay-as-you-go
- Legislature transferred the funding obligation to the Supplemental Pension Fund (SPF) in early 1970s – remains pay-as-you-go (RCW 51.32.073)
- Insurance liability of past liabilities recognized when the obligation shifted to the SPF in the early 1970s
- Because this is not a normal insurance funding scheme,
  - a flat rate per hour is charged all business,
  - half of the funding comes from workers
- Oregon also has a similar funding scheme for COLAs

Slide 2 provided the history of the Supplemental Pension Fund (SPF).

A question was asked if workers in Oregon pay half of the funding scheme as well. Mr. Vasek confirmed that Oregon workers do pay half of the funding scheme—they pay a flat rate per hour worked as well. Mr. Malooly added the obligations are much lower in Oregon.

Pay-as-you-go	vs	Prefunding
Premiums less than New costs incurred. Virtually no investment income.		Premiums Equal to New costs incurred offset by investment income
If funding stops, no money left to pay benefits		If funding stops, the reserves set aside adequate to pay for future benefits
Big Unfunded Liability		Assets larger than liabilities to maintain solvency

Slide 3 provided contrasts of the Pay-as-you-go scheme versus the Prefunding scheme.

Mr. Vasek reviewed slide 4—as of June 30, 2009, the SPF benefit liability was $11.386 billion; discounted to present value at 2.5%.

Changing over to a prefunded scheme

- Would require a law change
- The old liabilities have not been fully funded – would need to continue pay-as-you-go scheme to fund old liabilities
- New SPF rates expected to fully fund new liabilities on future insurance claims
- Cost of new liabilities being incurred are higher than the current payments on old liabilities
- Normal insurance funding schemes would base rates on the past experience of the businesses being charged
- So two SPF charges:
  - Pay-as-you-go flat rate: to pay for old liabilities
  - New experience-rated rate: to pay for new liabilities

Slide 5 provided an overview of the changes that would need to occur to change to a prefunded scheme.
This would require two SPF charges to be instituted. First, the pay-as-you-go scheme would continue because we cannot stop paying benefits to workers who have already been injured; we would need to continue to pay for old liabilities. Secondly, we would need new liabilities to be experience rated. This would be higher than the pay-as-you-go approach and would cause rates to double.
Regarding the 5th bullet, Mr. Vasek further explained that different base rates per class would be used.

The costs for Fiscal Year 2009

(estimates as of 6/30/2009)

- New SPF liabilities for injuries/illness during FY 2009
  - $471 Million discounted to present value at 2.5%
- SPF Payments during FY 2009
  - $375 Million
- Straight change over to prefunding would have cost
  - $471 + $375 = $846 Million
  - Increase of $471 Million

Slide 6 provided an example of the costs for FY 2009 for both state fund and self-insured claims in this new scheme. Premiums would more than double going from $375 to $846 million.

Effect on State fund employers

of new prefunding scheme if effective 2010

- Funding Old liabilities
  - Current SPF rate of $0.097 per hour split 50-50 with workers
- Funding New liabilities
  - State fund portion of new liabilities is $390 M
  - Would have been an additional 27% rate increase
  - 2 Options to experience rate:
    - Addition to accident fund rate in order to pick up these new liabilities – NOT split with workers
    - Addition to SPF rate in order to pick up these new liabilities – SPLIT with workers

Effect on State fund employers

(cont.)

- Impact by rate class would vary considerably to fund the new COLA liabilities
  - Would need to charge the expected future COLA usage per class
  - Based on the serious claim portion of the accident fund rate per class
  - Examples of the additional rate (in $ per hour and %):

•Clerical office:	$0.012 or 8%
•Restaurant	$0.055 or 13%
•Wood frame construction	$1.01 or 31%
•Logging, NOC	$5.39 or 42%

Slides 7 and 8 explain the effects on state fund employers using the prefunding approach.

A question was asked regarding the bullet "Would have been an additional 27% rate increase". Would the 27% be added to the overall average rate or is the 27% an increase in the SPF rate? Mr. Vasek answered this would be an overall increase—instead of 7.6% rate increase we recently had, it would be 27% on top of that. This is based on a funding scheme change.

A comment was made that based on this data, the state fund would be responsible for $390 million and self-insured employers would be responsible for $80 million. It was asked whether this is due to the difference in utilization and pensions. Mr. Vasek answered that self-insured employers have fewer workers and their costs are less per hour for workers who are self-insured versus state fund.

A question was asked if the department is proposing legislation for this next year. Director Schurke answered this presentation was for the department to follow up on a question asked at a previous WCAC meeting. At this point, the department is not planning proposed legislation. Overall, we need to understand the socialized costs of the system, even if the decision is to leave it the way it is.

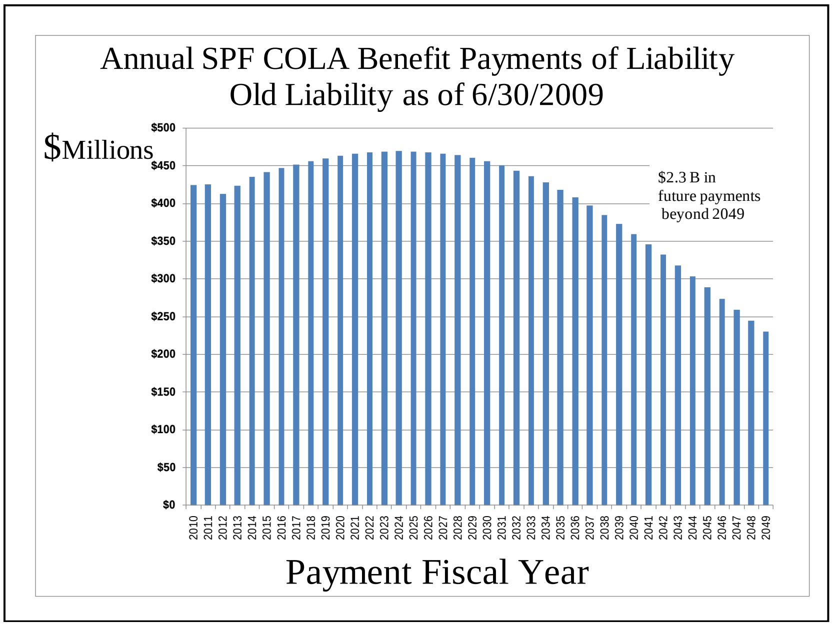
A question was asked if there is a way to have the fund bifurcated to have the current fund continue with state fund claims and have the self-insured portion of SPF liabilities handled differently. Director Schurke answered there is a way, though it brings in the question about the discount rate. The department would like to have further discussions with the self-insured community. Director Schurke added that she hopes the WCAC would weigh in and come to an agreement on this before any legislation.

A comment was made regarding the concerns of the self-insured community regarding:

- Paying disproportionate share into the fund relative to the liabilities for the fund. The self-insured employers are paying more than would be attributed to self-insured claims.
- Concerns have been expressed about the impacts on different industries.
- In most other states, they are prefunded as part pension costs.
- Self-insured members are interested in bifurcating the fund. They would like to look at various methodologies for either assessing self-insurers or looking at self-insurers paying their own benefits.

A comment was made that this is a joint problem for both labor and business groups.

A question was asked regarding the pension discount rate—we use 6.5% for the pension fund and we are using 2.5% on the SPF—why the difference? Mr. Malooly answered we should be using a discount rate based on the risk-free interest rate tied to 10-20 year treasury bills. For the Accident and Medical Aid Funds, we use a discount rate two percentage points lower than this risk-free rate. If we were to lower our discount rate to one based on this risk-free rate in the Pension Fund, self-insurers would have to pay additional money. Because of the potential additional funding, it was decided we did not want to change the Pension Fund discount rate of 6.5%. Ultimately, the self-insurers pay the difference between the actual investment income and the anticipated investment income each year through the "experting" of pensions. We should be changing the Pension discount rate especially given the decline in investment yield. (This is an issue that warrants further discussion. Mr. Vasek added that the SPF has no invested assets.)



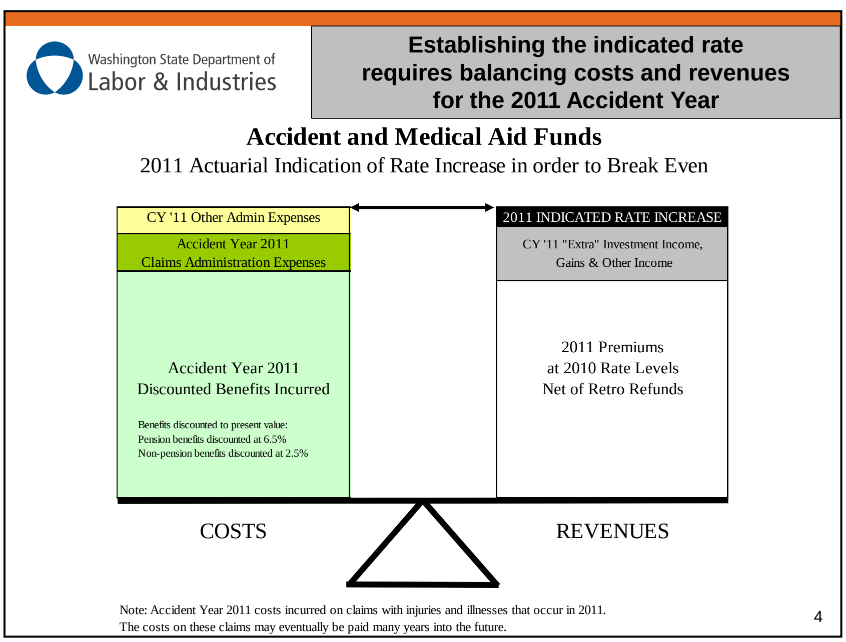
The chart on slide 9 reflects the estimate of the pay out of liabilities as of June 30, 2009. For 40 years we would continue to sustain the 2 rate scheme and by 2049 we would still have $2.3 billion in future payments beyond 2049 for the old pre-2009 liabilities. A decision to make this change would obviously have long term consequences.

An additional comment was made that this presentation helped to reinforce that change is needed due to the pension trends.

<u>2011 Rate Indication and Proposal: Judy Schurke, Bob Malooly, Bill Vasek and Kirsta Glenn</u>

The *2011 Rate Indication and Proposal* presentation was reviewed. Mr. Malooly provided an overview of the discussion and advised the committee that the 2011 proposed rate and the strategies to restore the contingency reserve will be announced at the end of the presentation.

Mr. Vasek began the presentation with a review of actuarial considerations in determining the indicated rate including balancing costs and revenues, fund trends and investment income.



This chart explains that establishing the indicated rate requires balancing costs and revenues for the 2011 Accident Year. The indicated rate is the break-even rate. Break-even means that we earn zero net income as we balance the cost with the revenues.

The costs are the benefits, claims administrative expenses and other administrative expenses.

The revenues are the premiums, extra investment income and the rate increase.

Washington State Department of Labor & Industries

Cost components explained

- Discounted benefits incurred
  - Estimated benefit liabilities <u>for the lifetime cost</u> of the claims that occur in 2011, discounted at the following rates:
    - Pension benefits (6.5%)
    - Non-pension benefits (2.5%)
- Claims Administration Expenses
  - <u>Variable</u> costs associated with the lifetime provision of benefits (claims management, medical cost and policy management, vocational rehabilitation services, etc.)
- Other Administration Expenses
  - <u>Fixed</u> costs for 2011 associated with other services including premium collection (account management), fraud prevention services, DOSH, SHARP, UW, etc.

5

Mr. Vasek explained the cost components. The discounted benefits incurred are the estimated lifetime costs of the claims. These are not the costs paid during the year; they are the costs for the claims that occurred during the accident year. The estimated benefit liabilities for the lifetime cost of the claims that occur in 2011 are discounted at the following rates: pension benefits at 6.5% and non-pension benefits at 2.5%.

To administer these claims, we incur claims administrative expenses. These are costs associated with administering claims that occurred during the year. The department must administer these claims until the provision of the benefits has ended. These are variable costs that are estimated as a percentage of the benefits.

A question was asked if Specialty Compliance Division was included in the "other administrative expenses". Mr. Vasek confirmed they were included.

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Revenue components explained

- 2011 premiums (estimated at 2010 rate levels)
  - Estimated premiums assessed based on 2010 rate levels
- Less Net retro refunds
  - Expected 2011 net retro refunds based on new Retro program, reduces premium revenue
- Extra investment income, gains and other income
  - Investment yield in excess of discount rates because benefits are already discounted for anticipated investment income
- 2011 indicated break-even rate
  - The rate change necessary to balance costs and revenues

6

The department estimates what premiums would be earned in 2011 if no changes were made to the rates. The department adjusts for net expected retro refunds based on 2010 rate levels. The extra investment income is the income in excess of what is anticipated by the discount rate. The final component is the indicsted break-even rate for 2011.

Mr. Vasek provided details of the cost items. The biggest cost component is benefits. He explained how the actuaries consider everything as a ratio to or percentage of premiums.

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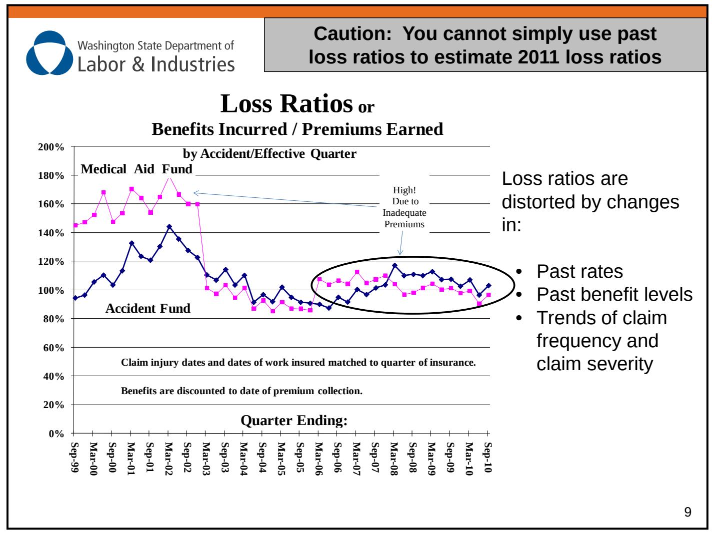
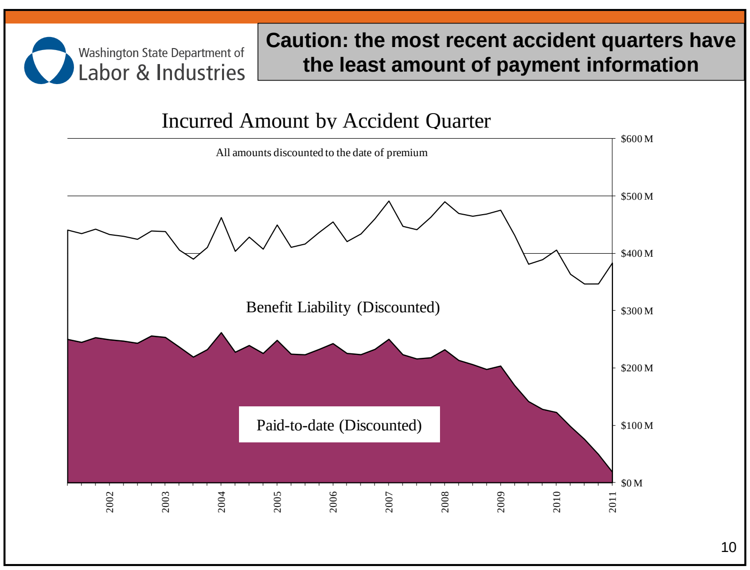
Loss ratios are critical to understanding our ratemaking process

- Loss ratio is the ratio of incurred benefits to premiums assessed
- Loss is another term for benefits
- Used in the insurance industry as a measure of profitability
- Rough measure of how adequate premiums were for a given year
- Past loss ratios are used to estimate future loss ratios after some adjustments are made

8



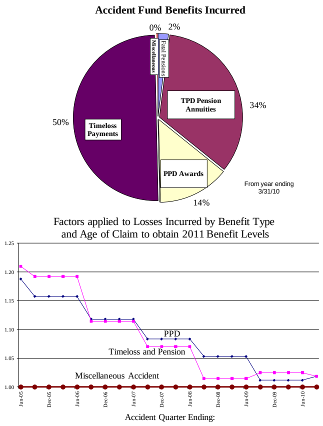
"Loss ratio" is the ratio of the incurred benefits to the premiums. The chart on slide 9 shows what the loss ratios look like with no adjustments made. It is difficult to predict future loss ratios without making adjustments because of known historical changes on trends of premium rates, claims frequency and claim severity. One cannot simply use past loss ratios to estimate 2011 loss ratios.



This chart is by accident quarters—the top portion shows how much discounted losses have been incurred. The lower portion shows how much has actually been paid to date on a discounted basis. (Note: There is little payment information for the most recent quarters.)

How much would past claims cost in 2011?

Washington State Department of Labor & Industries

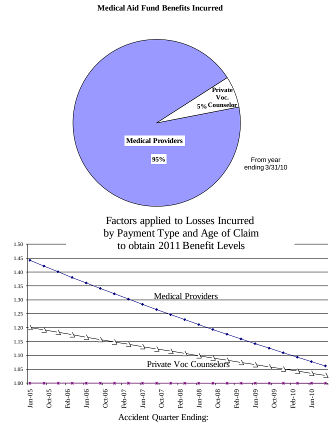


- In order to estimate 2011 accident fund benefits we determine how much past claims would cost if they occurred in 2011
- Factors adjust past benefits so that we have an estimate of the costs to be incurred in 2011
- The two most recent quarters are not used as they are immature

11

How much would past claim cost in 2011?

Washington State Department of Labor & Industries



- In order to estimate 2011 Medical Aid benefits we determine how much past claims would cost if they occurred in 2011
- Factors adjust past benefits to 2011 benefit levels
- The two most recent quarters are not used as they are immature

12

In the Accident Fund, we first look at benefits by type: 50% are time-loss, 34% are total permanent disability (TPD) pensions, 14% are permanent partial disability (PPD), and 2% accounts for fatal pensions. As past benefit levels have changed differently by type of benefit, the past benefit levels are adjusted to levels expected in 2011. For example, for time-loss and pension awards, we have an estimate of the average monthly benefit today, and a projection of what it will be in 2011 along with historical information of what the average monthly benefits were.

In the Medical Aid Fund, the two benefit components are for medical providers which account for 95% and private vocational counselors who make up 5%. We apply factors to these benefits to bring them to 2011 rate levels; we are applying a 5.5% annual inflation trend for medical providers and a 2.5% trend for private vocational counselors.

Washington State Department of Labor & Industries

Claims Administration Expenses

- These variable costs are a percentage of the estimated benefit cost
- Costs associated with services provided by the following programs that support the provision of benefits for the life of the claim
  - Claims & Claims Support Units
  - Health Service Analysis and the Office of the Medical Director
  - Legal Services & AAGs (Claims)
  - Vocational Rehabilitation

Note: Groupings are consistent with statutory accounting principles

Other Administrative Expenses

- Fixed costs for 2011 associated with other services

Premium Administration
Employer Services
Collections
Field Audit
Field Services
Retro
Legal Services & AAG (Firms)

General Insurance
SHARP
DOSH Consultation
Risk Management

Non-Insurance
Board of Industrial Insurance Appeals
DOSH Compliance
UW Department of Environ & Occ Health Sciences
Apprenticeship
Employment Standards

15

Administrative costs are broken into two categories: claims administrative expenses and other administrative expenses. The claims administrative expenses are for the lifetime of a claim and vary with frequency and severity of the claims. If benefit costs increase, then the claims administrative expenses also increase.

The other administrative expense costs incurred during 2011 are fixed costs. We are using groupings listed here that are consistent with statutory accounting principles allowing us to compare to other insurance companies and state funds.

Washington State Department of
Labor & Industries

Accident + Medical Aid Combined

Appropriated Administrative Expenses Paid

	FIXED		VARIABLE		TOTAL		
	Prem. Related, General, & Other		Claims Administrative				
	as of 6/2009	as of 9/2010	as of 6/2009	as of 9/2010	as of 6/2009	as of 9/2010	as of 9/2010
FY Yr. 2008	$ 98 M	$ 99 M	$ 124 M	$ 124 M	$ 222 M	$ 223 M	Actual
FY Yr. 2009	$ 108 M	$ 108 M	$ 130 M	$ 130 M	$ 238 M	$ 238 M	Budgeted
FY Yr. 2010	$ 113 M	$ 111 M	$ 136 M	$ 132 M	$ 249 M	$ 243 M	Budgeted
Cal. Yr. 2008	$ 108 M	$ 109 M	$ 133 M	$ 133 M	$ 241 M	$ 242 M	Actual
Cal. Yr. 2009	$ 110 M	$ 110 M	$ 131 M	$ 129 M	$ 241 M	$ 240 M	Estimated
Cal. Yr. 2010	$ 115 M	$ 112 M	$ 139 M	$ 129 M	$ 254 M	$ 240 M	Estimated
Cal. Yr. 2011		$ 116 M		$ 131 M		$ 247 M	Estimated
2011 Standard Premiums		**$ 1,414 M**	Estimated at 2010 rate levels				
2011 Fixed Expenses /Std. Premiums		**8.2%**					
2011 Claim Payments				**$ 1,598 M**			
2011 Claims Admin /Claim Payments				**8.2%**			

16

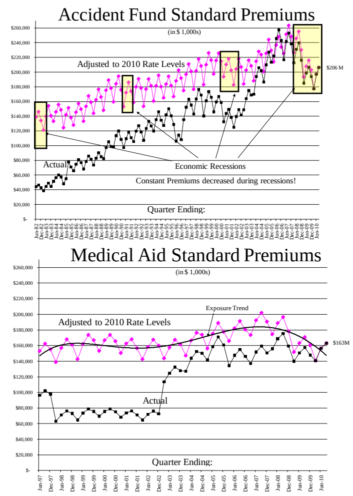
This table shows both the past and projected administrative expenses for the Accident and Medical Aid Funds combined. The current data is as of September 2010. The biggest change was the estimate for calendar year 2010 which is $3 million lower for fixed expenses and $10 million lower for claims administrative expenses. We are estimating $247 million to be paid during 2011.

As a percentage of claims payments, the claims administrative expenses are 8.2%, the fixed expenses are also 8.2%. The level of overhead is about 15.5%, very low when compared to the industry.

A question was asked why 15 months was used instead of a year—could the three months distort the data? Mr. Vasek answered the previous presentation made to the committee was based on June 2009 figures, which was 15 months ago.

Mr. Vasek continued with an explanation of revenues.

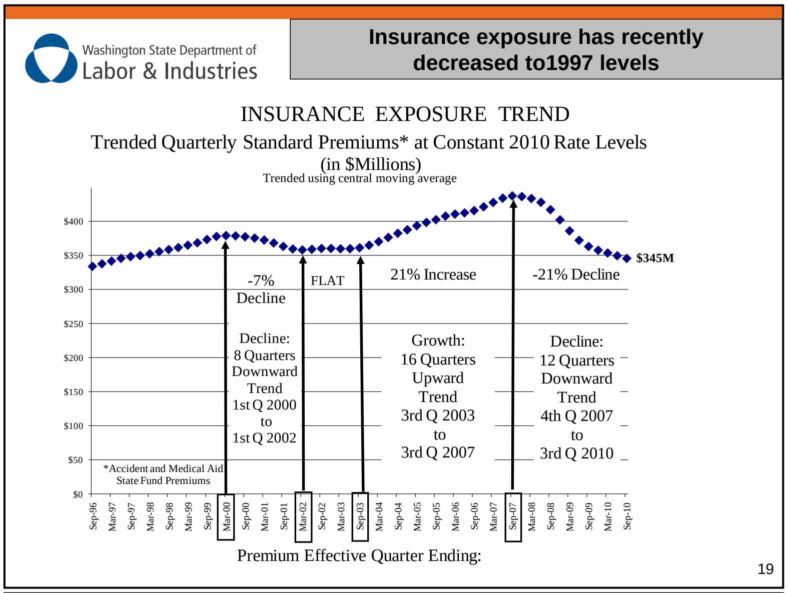
Washington State Department of
Labor & Industries



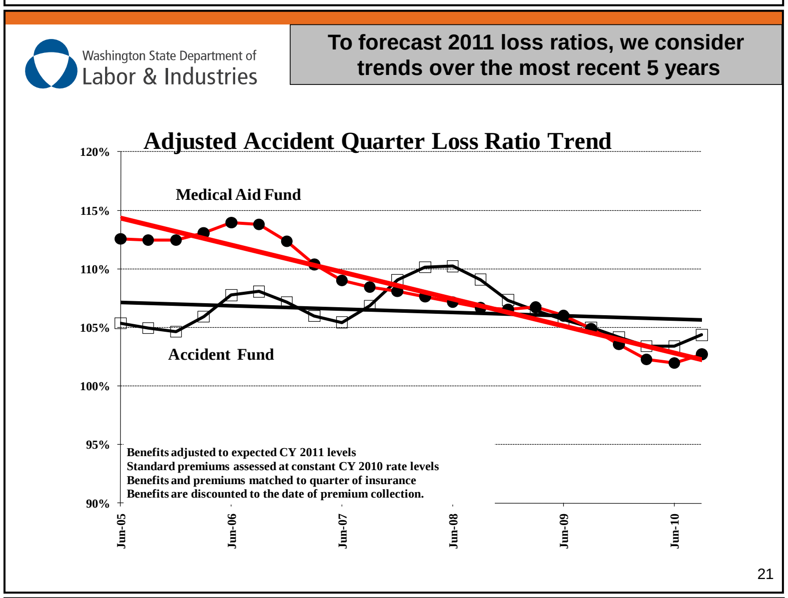
- In order to estimate 2011 premiums we adjust past premiums to 2010 rate levels
- The insurance exposure is the premiums at 2010 rate levels
- The adjusted premium trends look similar for both funds

18

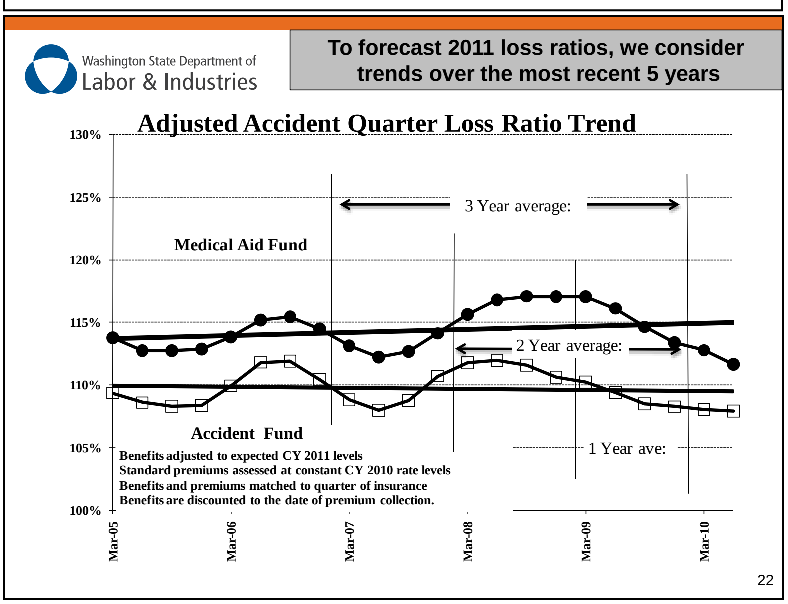
To forecast the rate indication, the department must forecast 2011 premiums at the 2010 rate levels. This is called insurance exposure and is shown here on the same scale for the Accident and Medical Aid Funds in purple. The black lines are the standard premiums assessed up-front.



This chart shows the effects of the economy on the insurance exposure. Insurance exposure peaked in the third quarter of 2007; we had a 21% increase from the third quarter of 2003 to this peak. Since the peak, we have declined 21%. Currently, the level of exposure is similar to the levels from 1997.

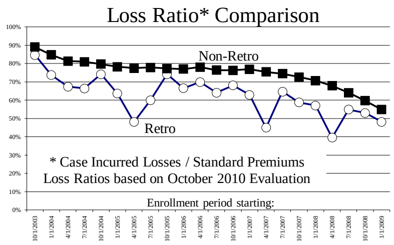


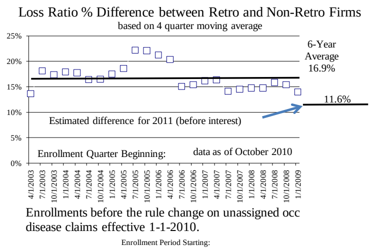
These charts show the adjusted accident quarter loss ratios over the last five years. Slide 22 depicts the various possible averages of loss ratios to project the 2011 loss ratio. There is a downward trend in the Medical Aid Fund. The Accident Fund does not have a consistent upwards or downwards trend over the five years; instead the loss ratio increased until the peak; once the recession occurred the loss ratio declined.



Washington State Department of Labor & Industries

Past performance is used to estimate future retro refunds





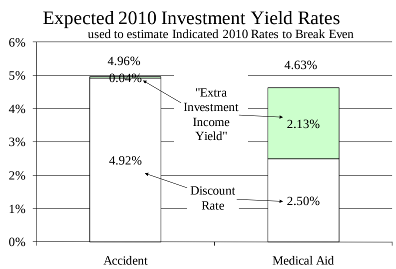
- We look at the loss ratios for retro and non-retro employers to determine the average loss ratio difference
- The loss ratio difference determines the size of the retro refund pool
- The difference in loss ratios is estimated at 16.9% for enrollments using previous rules
- For 2011 the estimated differences = 11.6% due to implementation of study recommendations

25

Mr. Vasek continued with an explanation of retro refunds. The department uses past performance to estimate future retro refunds. The average percentage difference in loss ratios between non-retro and retro firms over the last six plan years is 16.9%. The chart reflects enrollments prior to the law change effective January 1, 2010. When the percentage is adjusted for changes to rules in January 2010 and 2011, we expect the percent difference to be 11.6%.

Washington State Department of Labor & Industries

Actuaries estimate the excess of 2011 investment income yield rates above liability discount rates



Extra Investment Income
(as a % of Premiums)

Extra Investment Income from:	Accident Fund*	Medical Aid Fund
Invested Assets in excess of Loss Liability	-2.9%	1.7%
Yield in excess of Discount**	0.2%	13.6%
TOTAL	-2.7%	15.3%
*includes the Pension Fund		
**highly leveraged by ratio of Invested Assets/Premiums	5.70	6.39

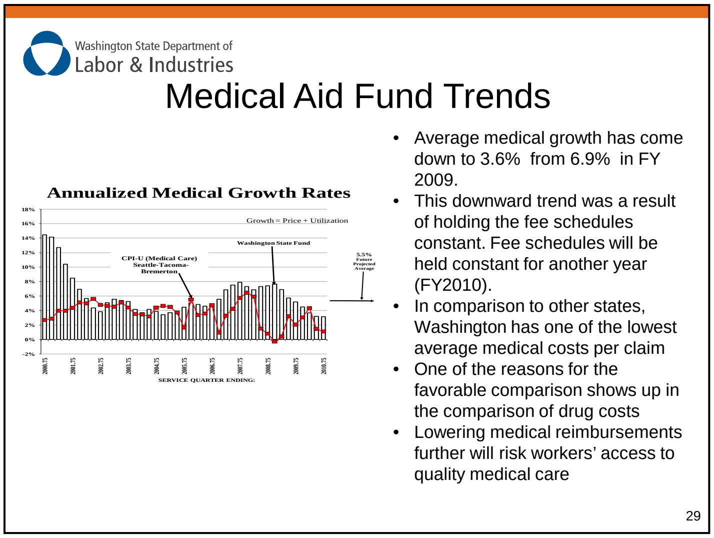
- Investment income yield rates will be above liability discount rates by 0.04% in the Accident Fund and 2.13% in the Medical Aid Fund (as percentage of invested assets)
- Excess yield rates are restated as percentages of premium to determine how much premiums can be offset by investment income
- Excess yields are -2.7% for the Accident Fund and 15.3% for the Medical Aid Fund (as a percentage of premiums)
- The Accident Fund excess yield is negative because liabilities are greater than invested assets. So it is estimated that investment income will be below the level anticipated by liability discounts.

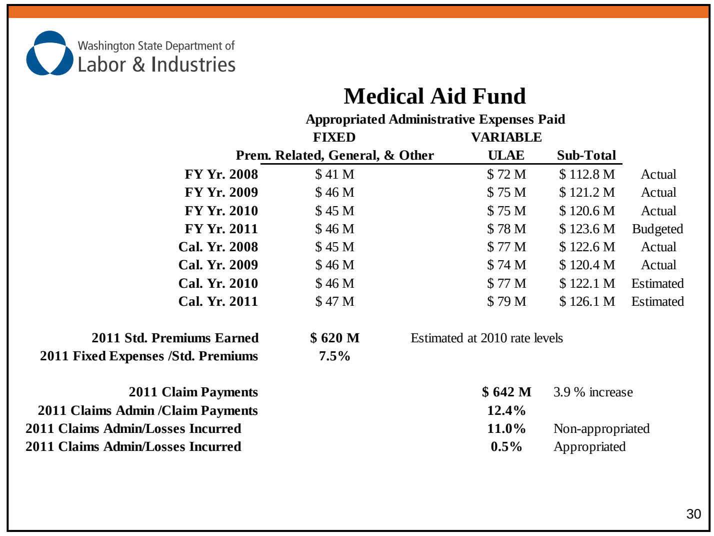
27

The extra investment income usually helps offset the rate increase.

The extra investment income is (negative) -2.7% in the Accident Fund and (positive) 15.3% in the Medical Aid Fund as a percentage of premiums. This negative percentage in the Accident Fund is an estimate that investment income will be below the level anticipated by the discount rate.

Medical Aid Trends





Medical Aid Fund

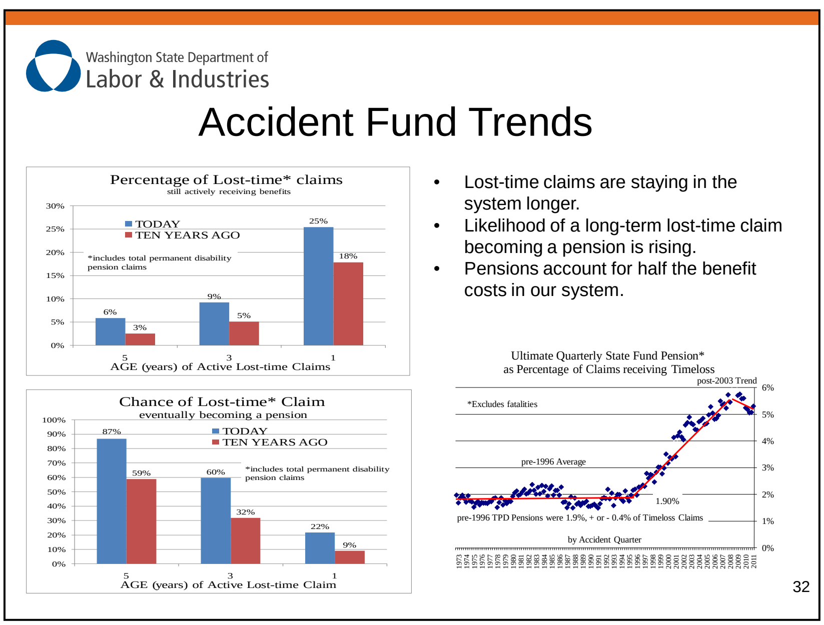
Appropriated Administrative Expenses Paid

	FIXED Prem. Related, General, & Other	VARIABLE ULAE	Sub-Total	
FY Yr. 2008	$ 41 M	$ 72 M	$ 112.8 M	Actual
FY Yr. 2009	$ 46 M	$ 75 M	$ 121.2 M	Actual
FY Yr. 2010	$ 45 M	$ 75 M	$ 120.6 M	Actual
FY Yr. 2011	$ 46 M	$ 78 M	$ 123.6 M	Budgeted
Cal. Yr. 2008	$ 45 M	$ 77 M	$ 122.6 M	Actual
Cal. Yr. 2009	$ 46 M	$ 74 M	$ 120.4 M	Actual
Cal. Yr. 2010	$ 46 M	$ 77 M	$ 122.1 M	Estimated
Cal. Yr. 2011	$ 47 M	$ 79 M	$ 126.1 M	Estimated
2011 Std. Premiums Earned	$ 620 M	Estimated at 2010 rate levels		
2011 Fixed Expenses /Std. Premiums	7.5%			
2011 Claim Payments		$ 642 M	3.9 % increase	
2011 Claims Admin /Claim Payments		12.4%		
2011 Claims Admin/Losses Incurred		11.0%	Non-appropriated	
2011 Claims Admin/Losses Incurred		0.5%	Appropriated	

Medical growth, which is the annualized change in the average cost of medical services provided during the quarter, has come down to an average of 5.6%. For claims with injuries during accident year ending June 30, 2002, the state fund average medical cost per lost-time claim is one of the lowest in the country when compared to average costs using data from the National Council on Compensation Insurance.

Fixed expenses are estimated to be 7.5% of premiums and claims administration expenses are estimated to be 11.5% of losses incurred.

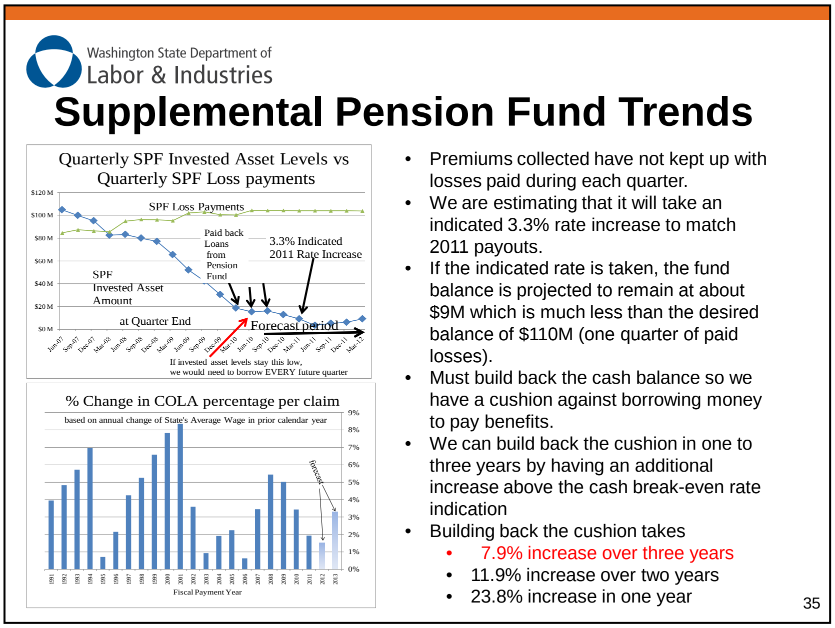
Accident Fund Trends



The following three trends are significant:
1) Duration is up for lost-time claims.
2) Claims that become one, three, or five years old all have an increased likelihood of becoming a pension.
3) Pensions, which account for half the benefit costs in the system, have increased from 1.9% of time-loss claims to over 5% of time-loss claims.

It has been noticed that the department is receiving more claims from lower hazard industries than higher hazard because of the shift in mix of business recently. Because higher hazard industries tend to have more pensions, there is a slight decline in pensions.

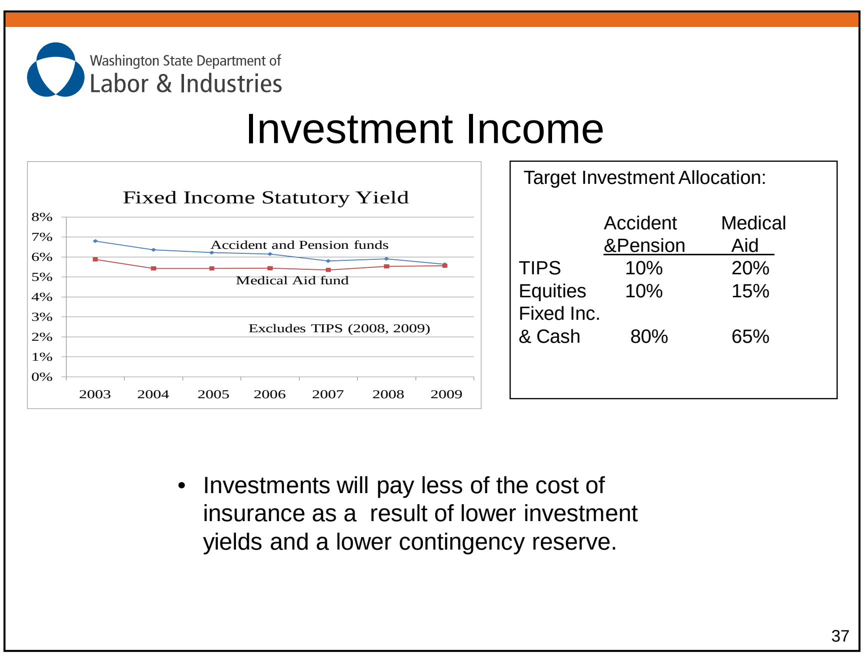
Supplemental Pension Fund Trends



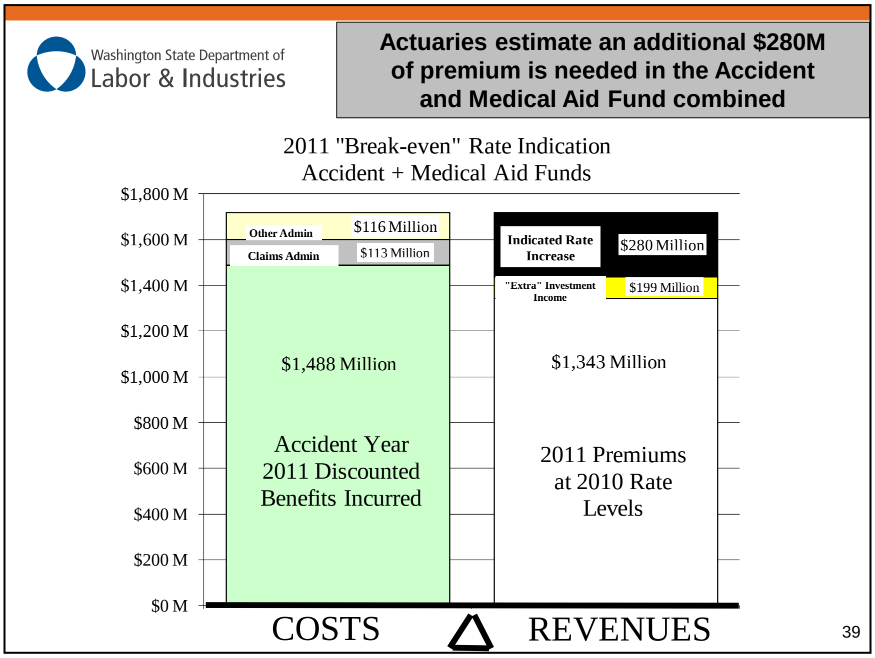
The Supplemental Pension Fund (SPF) is funded on a pay-as-you-go basis and is not prefunded. When hours decline in the system, the level of cash in the SPF declines as well. Our break-even indicated rate increase, to keep the cash level constant, is 3.3%. At this level, we will have to continue to borrow money.

Slide 35 explains we can build a cushion in one to three years by having additional increases above the cash break-even rate indication. We have chosen to build back a one-quarter cushion (about $110 million) over three years—this would be a 7.9% increase on top of the 3.3% increase to total 11.2% increase for SPF.

A question was asked how we can accurately discuss this based on the earlier *Pay-as-you-go versus Prefunding* presentation: what is the difference between a contingency reserve and a cushion? Also, is the money invested? Mr. Malooly answered the money is invested in relatively short-term assets because it gets drawn out in the course of a quarter. It is not a contingency reserve which is the difference between assets and liabilities if we were prefunding. The SPF has an unfunded liability of $11 billion. The $110 million compared to $11 billion is relatively small; just enough to maintain current payment obligations.



Investment yield rates have been decreasing in the Accident, Pension, and Medical Aid Funds.



This slide was corrected at the meeting. When the Accident and Medical Aid Funds are combined, there is a need for $290 (instead of $280) million additional premiums.

Washington State Department of
Labor & Industries

AY 2011 Break-Even Premium Rate Change*

Based on 3rd Q 2010 Analysis

	Average 2010 Rate**	Indicated Break-even Change	Indicated 2011 Rate**
Accident	$0.261	**29.8%**	$0.339
Medical Aid	$0.206	**9.4%**	$0.225
Supp. Pension	$0.097	**3.3%**	$0.100
Overall	**$0.564**	**17.8%**	**$0.664**

	2011 premiums at 2010 rate levels	Increase:	2011 premiums at Break-even
Accident	$ 792 Million	$ 236 Million	$ 1,028 Million
Medical Aid	$ 623 Million	$ 59 Million	$ 681 Million
Supp. Pension	$ 293 Million	$ 10 Million	$ 303 Million
Overall Premiums	$ 1,707 Million	$ 304 Million	$ 2,012 Million
Less Net Retro Refunds	-$ 71 Million	-$ 15 Million	-$ 86 Million
'11 Net Premiums	**$ 1,636 Million**	**$ 290 Million**	**$ 1,926 Million**
Employee portion	$ 458 Million	$ 34 Million	$ 492 Million
Net Employer portion	$ 1,178 Million	$ 255 Million	$ 1,434 Million
Employee percentage	28.0%		25.5%

40

This shows the indicated rate increases based on the actuarial analysis as of September 30, 2010. The increases are 29.8% in the Accident Fund, 9.4% in the Medical Aid Fund, and 3.3% in the Supplemental Pension Fund, for a combined increase of 17.8%.

Washington State Department of
Labor & Industries

AY 2011 Break-Even Premium Rate Change*

Based on 2nd Q 2010 Analysis

	Average 2010 Rate**	per Loss Ratio Projection			
		Selected 1-Yr Average	**2-Yr Average**	**3-Yr Average**	**1-Yr Average Reserve**
Accident	$0.267	**35.2%**	37.4%	36.3%	37.9%
Medical Aid	$0.208	**22.0%**	23.1%	21.4%	29.3%
Supp. Pension	$0.097	**0.9%**	0.9%	0.9%	0.9%
Overall	**$0.572**	**24.6%**	**26.0%**	**24.9%**	**28.5%**

41

Slide 41 presented what the rate indication would have been three months ago; the Accident Fund was 35.2%, Medical Aid Fund was 22% and the SPF was 0.9%.

When combined, the total indicated rate increase was 24.6%.

Washington State Department of
Labor & Industries

What changed from the 2nd to 3rd quarter?

- More claims were filed from low-wage jobs and less claims were filed from high-wage jobs due to a shift in industry mix
- Changes in medical cost assumptions related to payments made early in the life of a claim

42

Slide 42 explained the significant changes that occurred between the 2nd and 3rd quarter.

Washington State Department of Labor & Industries

Factors impacting the indicated rate

How did we get here?

Indicated 2011 Overall Rate Change*

as of September 30, 2010

	2Q 2009 Indication 2010 Change	Adopted Average 2010 Change	Rate Level not Taken	Expected 2011 Benefit Inflation	Other* Stuff	Indicated Average 2011 Change
Accident	**18.9%**	4.5%	13.8%	2.5%	11.3%	**29.8%**
Medical Aid	**21.5%**	8.4%	12.1%	4.3%	-6.4%	**9.4%**
Supp.Pension	**16.0%**	16.0%	0.0%	1.2%	2.1%	**3.3%**
	19.4%	7.6%	10.8%	2.9%	3.3%	**17.8%**

*Other stuff explanation	Accident	Medical Aid	SPF
AF 4.18% to 4.92% discount rate assumption	8.2%		
Lower "Extra" Investment Income	1.8%	1.8%	
Lower LTD claim frequency AY09	0.69%	0.61%	
Timeloss duration	6.7%	5.6%	
Medical growth latest year vs expected		3.1%	
Lower fixed admin expenses	0.0%	-1.4%	
Lower Retro Refunds	-1.6%		
Fewer hours			2.1%
Modeling change:			
more responsive to recent trends	-3.3%	-9.3%	
Other	-1.2%	-6.1%	
TOTAL	11.3%	-6.4%	2.1%

43

Correction on slide: *Lower* LTD claim frequency AY09 should be corrected to *Higher* LTD claim frequency AY09.

This slide shows how we got from last year's rates to this year's rate indication: last year the indication was 19.4%. The department adopted a 7.6% rate increase. The amount of rate not taken in the Accident Fund was 13.8%, Medical Aid Fund was 12.1%, and SPF was 0%, averaging a 10.8% rate increase that was not taken in 2010. During the year, there was benefit inflation for 2011 of 2.9% and other circumstances that accounted for 3.3%.

This totals an indicated rate of 17.8%.

Ms. Glenn continued the presentation by discussing: 1) Effect of the economy on workers' compensation and industry mix; and 2) Conning Inflation Analysis. Bob Malooly then went on to discuss cost drivers and contingency reserves.

The department conducted two studies: one was internal and the other conducted by Conning Research Analysis. Conning conducted an analysis of the risk of different recovery scenarios on the financials of the agency.

Industry Mix and Cost

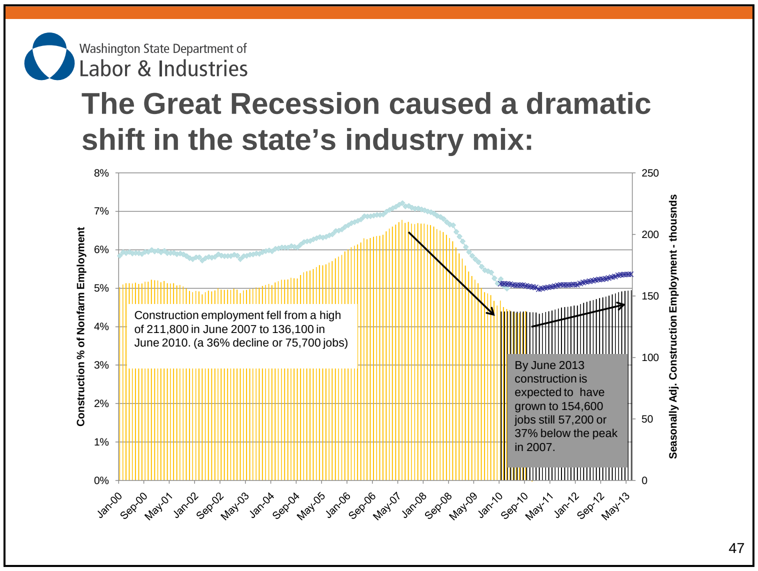
Washington State Department of Labor & Industries

Industry mix and cost:

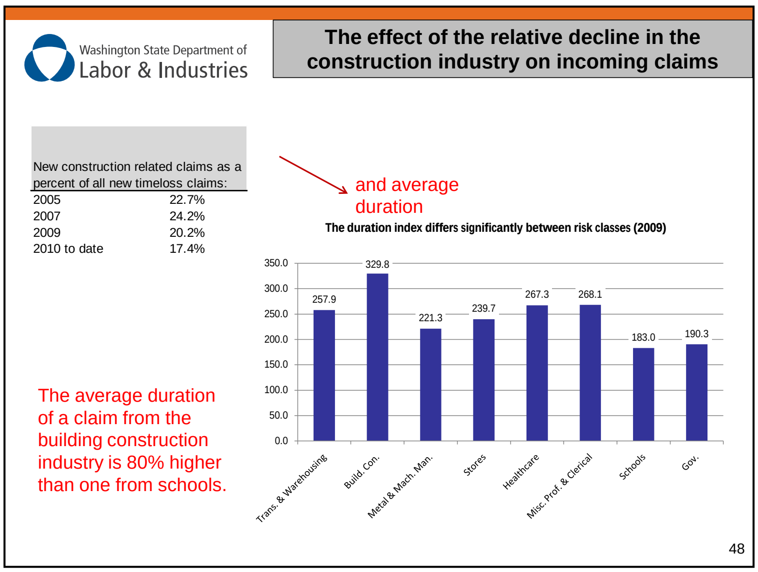
- Claims from different industries have different characteristics likely to impact severity.
  - Demographic
  - Nature of injury
  - Return to work possibilities
- Rates for each risk class versus average rates.
- Rates are based on historic and current attributes of claims.

46

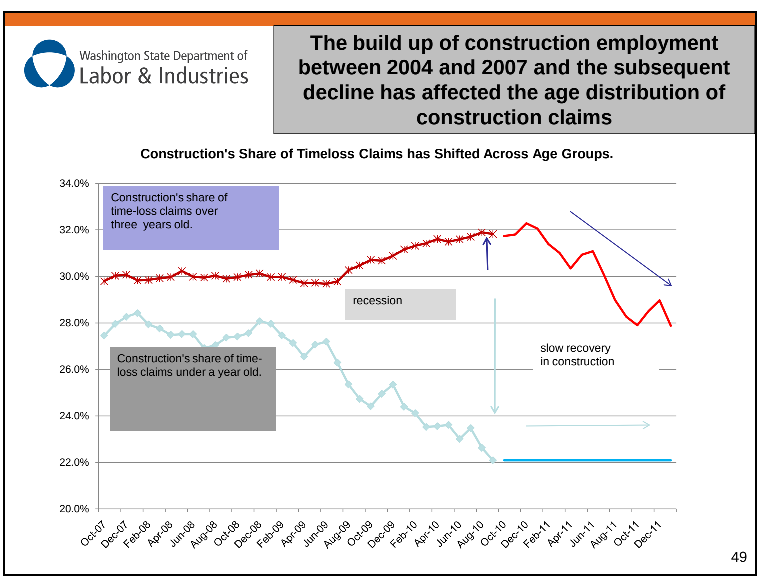
The change in industry mix impacts workers' compensation because it changes the nature of the claims coming into the system.



The bars on this chart represent the employment in construction and the line is the percent of total employment that comes from the construction industry. During the economic recovery, construction employment will remain far below where it was during the height of the construction boom. The expectation is construction will come back slowly—we are not expecting a return to the boom levels.



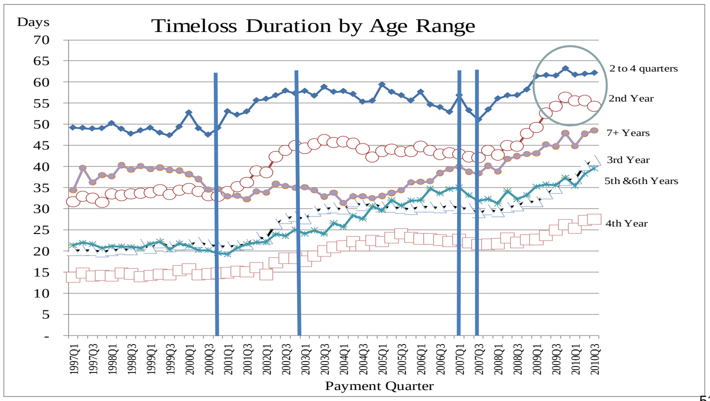
Construction claims accounted for 24% of claims in 2007. As of 2010 to date, it is down 17.4%. This has a significant impact on our system because construction claims tend to have higher average duration than claims from other industries.



The percentage of construction claims that have been in the system for three years or longer is still rising. These claims came into our system three years ago during the construction boom. As claims age, our expectation is that a lower percentage of older claims will be construction claims.

Washington State Department of Labor & Industries

Average duration rose from 2007 to 2009 among all ages of claims -- Since 2009, the duration among the youngest claims has begun to level off



51

Since the recession started, we have seen a general increase in the average duration of claims at different ages. They all increased during the early part of the recession. We are starting to see the duration of claims less than a year old is beginning to level off and may be coming down.

Washington State Department of Labor & Industries

High Severity Analysis:

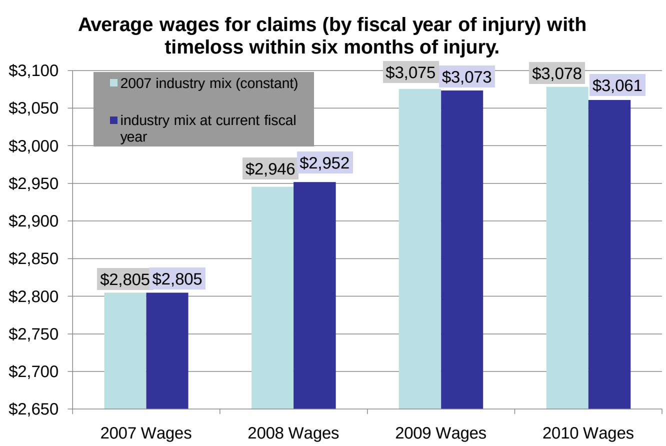
- Risk classes were categorized into 9 groups (from low severity to high severity) based on average claim costs.
- High severity groups were examined as a share of premium and by average duration.
- Results:
  - Premium collected from high severity industries, as a share of all premium, has fallen.
  - Average duration has risen among all severity groups.

52

An analysis based on groups of claims ranked by likely ultimate duration was done to compensate for the possibility that the decline in some high hazard risk classes such as construction might have been offset by increases in other high hazard industries. This analysis yielded the same result: that there has been a relative decline in claims from high-risk industries.

Washington State Department of Labor & Industries

Industry mix also seems to have affected average wages



55

While construction claims tend to be higher severity, they also tend to be higher wage jobs. As fewer construction claims are received in the system, the average wage has fallen.

Washington State Department of Labor & Industries

Conclusions:

- Claims from construction related risk classes have fallen dramatically and the small incoming cohort is working its way through the system.
- The fall in incoming claims from high average severity risk classes has put downward pressure on average claim duration.
- There has been a systemic increase in average duration that has, to this point, outweighed the duration lowering effects of the change in industry mix.
- We are beginning to see the effect of the decline in high severity claims on the average duration of newer claims.
- The change in the industry mix has also put downward pressure on average wages.

56

Washington State Department of Labor & Industries

Conning Inflation Analysis

The impact of different economic recovery scenarios on Washington's workers comp system.

- The Great Recession had major impacts on Washington's workers comp system.
- The path of the recovery is still uncertain, and there are unusually high risks of very different recovery paths.
  - Deflation
  - Inflation
  - Double Dip recession or slow growth

57

The second study was conducted by Conning Research and Associates. At the beginning of the recovery, there was a high risk of different scenarios: specifically deflation, inflation, double dip, or slow growth.

The department wanted an assessment of the risk to the financial health of the agency of each of the recovery scenarios.

Washington State Department of Labor & Industries

Conning Research and Consulting evaluated the impact of different economic recovery scenarios on financial indicators of workers comp system.

Scenarios:

1. Baseline –
   1. Steady low inflation (2-3%)
   2. Medical inflation almost twice as high as US CPI inflation
   3. Real GDP growth above 3% in 2011 and 2012
2. Higher inflation – both persistent and temporary
3. Double dip recession
4. Persistent slow growth
5. Deflation – both persistent and temporary

58

The department asked Conning to set up a model to evaluate the risks.

Washington State Department of
Labor & Industries

Results of scenarios on L&I financials:

- Estimated impact both on accident and medical aid funds.
- Indicators included:
  - Net combined ratio
  - Net investment gain/(loss)
  - Total net income/(loss)
  - Contingency reserves
  - Operating cash flow

59

In conducting this analysis, Conning did not include any effects of different recovery scenarios on claim duration or industry mix. They looked only at the impact of the scenarios on investment income and liabilities.

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Results compared to baseline 2012:

Accident Fund

	Combined Ratio	Net Investment	Total Net Income/(Loss)	Contingency Reserve	Operating Cash Flow
Inflation	Up (worst)	Down (worst)	Lower (worst)	Lower (worst)	Lower
Deflation	Down	Up	Higher	Higher	Higher
Double Dip	Up	Down	Lower	Lower	Lower (worst)
Slow Growth	Up	Down	Lower	Lower	Lower

Medical Aid Fund

	Combined Ratio	Net Investment	Total Net Income/(Loss)	Contingency Reserve	Operating Cash Flow
Inflation	Much worse	Down (worst)	Much worse	Much worse	Lower(worst)
Deflation	Down	Up	Much better	Higher	Higher
Double Dip	Up	Down	Lower	Lower	Lower
Slow Growth	Up	Down	Lower	Lower	Lower

60

These are the results of each of the scenarios in the Accident and Medical Aid Funds. The basic result was inflation, double dip recession, or slow growth would all put the agency in a worse position. Deflation puts us in a better position because the model assumes deflation would be associated with high growth.

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Conclusions:

- The baseline scenario is fairly robust to changes in assumptions about the pace of the economic recovery.
- The main avenues of influence are through returns on investments and changes in the value of liabilities due to medical inflation.
- In none of these scenarios is the US stock market expected to consistently produce returns at pre-recession levels.
- The most likely scenario for 2011 now appears to be continued slow economic growth with low inflation. This is close to Conning's baseline scenario.

61

The committee will be sent the Conning report.

Mr. Malooly continued the presentation.

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Workers' Comp Outlook for 2011

- Economic conditions are expected to improve very slowly, so workers will continue to face a tough job market, while employers struggle with costs.
- L&I's medical costs growth rates are lower than the national average.
- L&I continues to face financial challenges as average indemnity costs per claim rise. This year L&I has undertaken coordinated strategies to target appropriate services both to new claims and to long-term claims.

62

The frequency of injuries is declining; however, incoming claims are now costing more. This is happening in Washington and throughout the nation. Some states' statutes have benefit structures that constrain growth and duration.

We are seeing more of an effect of duration and pensions in Washington.

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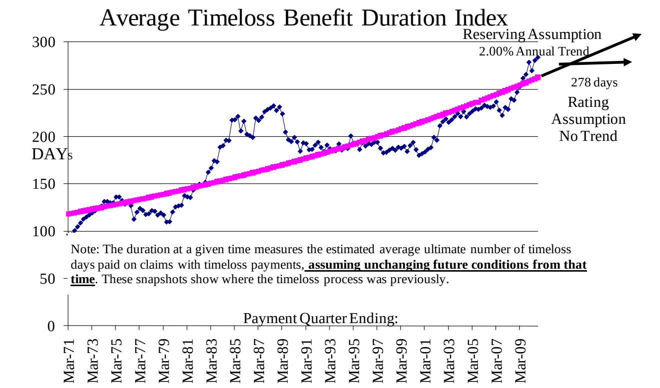
Time-loss duration index has continued to increase



As of September 30, 2010

63

This graph shows the time-loss duration index has continued to increase. For purposes of rate making we are assuming it will hold level. It is currently at 284 days.

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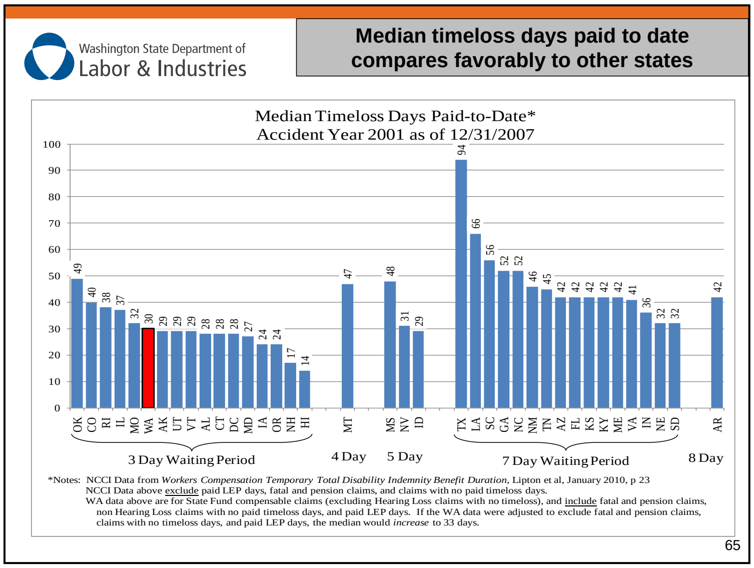
The increasing probability of active time-loss claims becoming a pension has lead to more estimated pensions

Probability of active claim becoming a pension

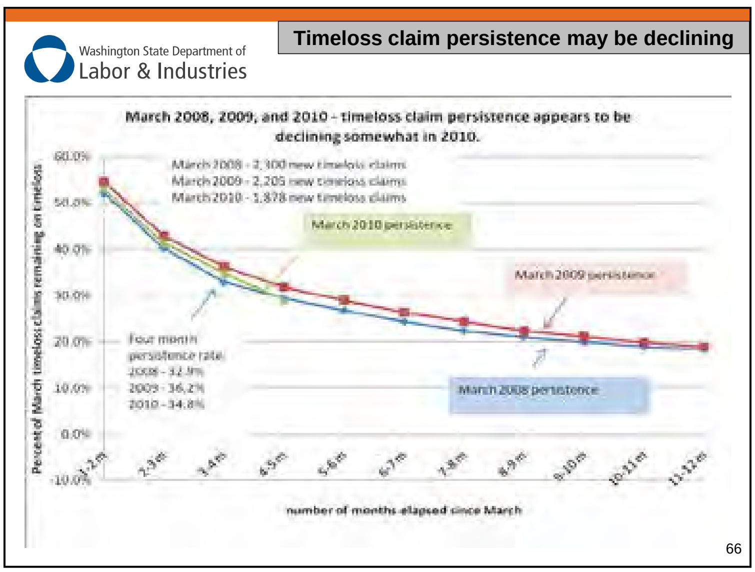
Age (Years)	6/30/2008	6/30/2009	6/30/2010
0 to 0.99	11%	13%	14%
1 to 1.99	29%	32%	32%
2 to 2.99	44%	48%	48%
3 to 3.99	58%	62%	63%
4 to 4.99	68%	74%	74%
5 to 5.99	77%	80%	83%
6 to 6.99	82%	84%	88%
7 to 7.99	88%	88%	93%
8 to 8.99	88%	89%	94%
9 to 9.99	93%	91%	96%
10 to 10.99	96%	95%	99%
11 to 11.99	99%	97%	100%
12 to 12.99	99%	98%	99%
13 and over	100%	100%	100%

64

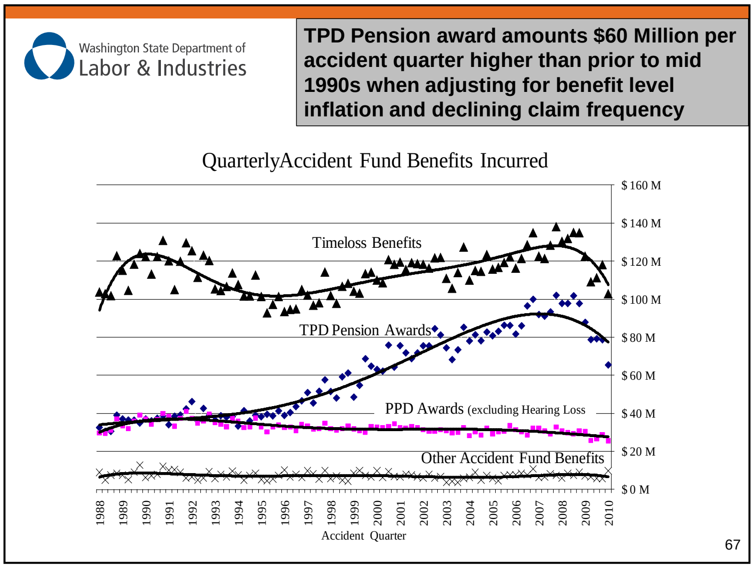
The department is concerned about the increasing probability of active time-loss claims becoming pensions. Comparing the percentages in 2008 with 2010 shows a significant increased probability of pensions for younger claims. We know a growing percentage of claims become long duration claims.

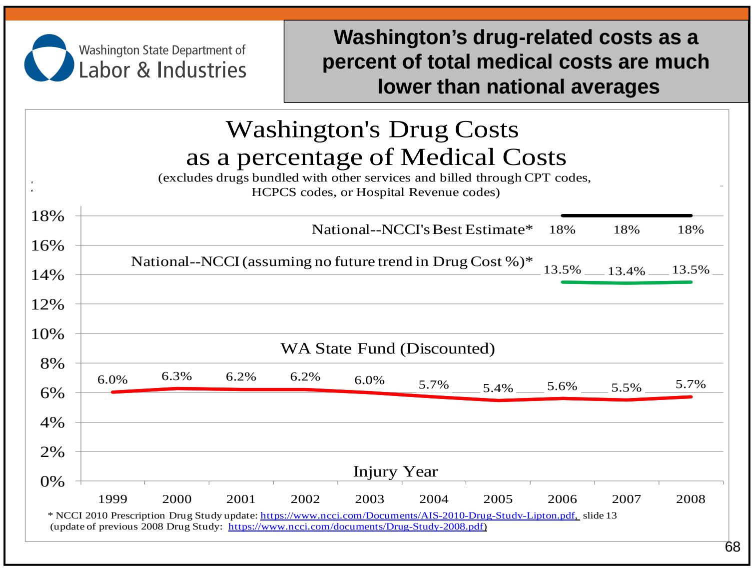


This chart compares the median time-loss days paid to date of states with three-day waiting periods.



This graph shows the persistence of a claim (what percentage of them stay in the system). From 2008-2009, the persistence increased in all age groups; recently, we have begun to see early indications that this may be improving.





NCCI's estimates of drug-related costs are 18% of the total medical costs. Washington State is at a much smaller percentage (between 5.5% and 5.7%). The department has been successful in getting physicians to use generic drugs and this has produced positive results.

Washington's medical costs on time-loss claims are low compared to the other states. The average ultimate medical cost per time-loss claim is $12,698 for Washington versus the nation's average of $19,237.

How we are addressing timeloss duration and pension costs

Claims Operations

- Data indicates that Early Claim Solutions claims are being processed more quickly, returned to work more quickly and costing less.

Early Return to Work

- L&I staff intensified efforts to help workers return to their employer of injury in FY09. In spite of the recession, in FY10, staff returned 2,500 workers to their employer of injury.

Vocational Services

- Approximately 73% of retraining job goals are in "demand" or "balanced demand" occupations.

Medical Management

- We increased the percent of injured workers treated by COHE doctors from 25% to 30%; and we are planning two new COHEs by 2013.

Lean Initiatives

- 9 workers' compensation lean initiatives are underway.

Legislative Changes

- Business, Labor and the Department are engaged in "interim" discussions regarding statutory changes to reduce costs and improve outcomes.

70

Ongoing L&I Cost Containment Initiatives (Over $200 Million)
Operational

- Emphasis on fraud and collections returns money to the trust funds
- Vocational Improvement Project
- Agency fiscal variance (salary, travel and equipment freeze)
- Early return to work assistance by L&I staff saves time-loss and professional fees
- Reduced postage

Medical Management

- Centers for Occupational Health Education (COHE) savings
- Management of physical/occupational therapy
- Held medical professional fee schedule at 2009 level
- Fee schedule for generic drugs
- Utilization review of medical treatment
- Financial incentives to encourage doctors to use preferred drug list
- Interpreting initiatives (including telephonic interpretation)
- Injured worker travel reimbursement revision
- Evidence-based coverage policies (Health Technology Assessments)
- Magnetic Resonant Imaging (MRI)
- Class A Surgeons
- Massage therapy cap
- Medical bill audits

71

The department has a number of efforts to address time-loss duration and pension costs as shown on slide 70.

The list on slide 71 provides cost containment initiatives. Mr. Malooly provided details regarding "Class A Surgeons" which was developed by Tom Wickizer and Gary Franklin. Class A Surgeons allows doctors who always pass utilization review (UR) to not request review and authorization for outpatient surgeries (complicated surgeries still go through the UR process). This has shortened the time before an injured worker gets surgery and has reduced costs.

Contingency Reserve

Mr. Malooly reviewed the contingency reserve slides. Upper and lower limits for the contingency reserve for each fund were established in the draft policy developed with the finance committee.

As of fiscal year end, the Medical Aid contingency reserve remains above the lower policy limit with $542 million.

As of fiscal year end, the Accident and Pension Funds were well below the lower policy limit at negative $360 million.

As of fiscal year end, the overall contingency reserve was below the lower policy limit with a combined total of $182 million.

2011 Proposed Rate

Director Schurke explained the 2011 proposed rate.

Regarding indications, the department wanted to set rates that were relatively stable and to keep funds in the contingency reserve to provide additional investment income.

We will use $117 million of the contingency reserve this year to absorb a portion of the increase.

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2011 Proposed Rate

Based on 3rd Q 2010 Analysis

					Proposal 2011 Rates		
Fund	2009 Hourly Rate	2010 Change	2010 Hourly Rate	Indicated 2011 Change	w/o SPF Cushion 2011 Change	w/SPF Cushion 2011 Change	Proposed 2011 Hourly Rate
Accident	$0.250	4.5%	$0.261	29.8%	29.8%	29.8%	$0.339
Medical Aid	$0.190	8.4%	$0.206	9.4%	-10.3%	-10.3%	$0.184
Supp. Pension	$0.083	16.0%	$0.097	3.3%	3.3%	11.2%	$0.108
Overall	**$0.523**	**7.6%**	**$0.564**	**17.8%**	**10.6%**	**12.0%**	**$0.631**

77

The 2011 proposed rate the department is considering before the additional funding for the SPF is 10.6%. An additional 7.9% in the SPF, or 1.4% overall, is needed to build the cushion for the SPF.

Director Schurke is proposing an overall rate increase of 12%.

Director Schurke advised the committee that Deloitte is working with the State's Auditor's Office this year. In late December 2010, they will distribute an opinion on the effect of the proposed rate on the solvency of the funds. Deloitte is also working with the department on estimated liabilities and these reports will be available.

Director Schurke commented that the department is not anticipating the high levels of investment incomes to offset premiums as we had in the past.

<u>Going Forward</u>

Director Schurke talked about next steps and strategies for re-establishing the fund balances. Mr. Vasek has been asked for a recommendation that will be reviewed by the Director and Deloitte. These recommendations will be discussed with the WCAC committee members.

Director Schurke also discussed statutory changes. Changes might alter the long-term duration of claims and reduce the probability of workers going on pension. In the wake of the initiative, she expressed it is not business as usual for the department. We have exciting changes occurring in the claims department that will have tremendous impact for workers and employers. This will entail further discussion with the committee. The department is committed to improving service.

The public hearings on the proposed rate are scheduled for January 4, 2011, in Tacoma and Spokane.

Washington State Department of Labor & Industries

2011 Proposed Rate

Based on 3rd Q 2010 Analysis

Fund	2010 Hourly Rate	Proposed 2011 Change	Proposed 2011 Hourly Rate
Accident	$0.261	29.8%	$0.339
Medical Aid	$0.206	-10.3%	$0.184
Supp. Pension	$0.097	11.2%	$0.108
Overall	**$0.564**	**12.0%**	**$0.631**

	2011 at 2010 Rate Levels	Increase /(Decrease)	Proposed 2011
Employee rate	$0.151	($0.005)	$0.146
Employer rate	$0.413	$0.073	$0.485
(Net Retro rate)	($0.023)	($0.003)	($0.026)
Employer rate net of Retro	$0.389	$0.070	$0.459
Total rate net of Retro	$0.540	$0.065	$0.605
Employee portion	$ 458 Million	($ 16) Million	$ 442 Million
Employer portion	$ 1,178 Million	$ 212 Million	$ 1,390 Million
'11 premiums net of Retro	$ 1,636 Million	$ 196 Million	$ 1,832 Million
Employee percentage	28.0%		24.1%

79

A question was asked regarding slide 79: why was the employee portion reduced? Mr. Malooly answered that this is the consequence of reducing the Medical Aid rate, which produced an overall decrease in the percentage paid by workers.

Meeting adjourned.