

## CONCISE EXPLANATORY STATEMENT

### *Chapter 296-17 WAC General Reporting Rules, Audit and Recordkeeping, Rates and Rating System for Washington Workers' Compensation Insurance)*

The purpose of this rulemaking is to adopt a reduction in the Medical Aid premium base rates for work performed during the six months beginning July 1, 2007, which will ultimately reduce the Medical Aid contingency reserve. During this time period, Medical Aid premiums will not be assessed for employers and workers and therefore it is anticipated that this will reduce the balance of the Medical Aid fund by approximately \$315 million.

The intended date of Adoption for this rule is March 12, 2007.

The intended Effective date for this rule is July 1, 2007.

The purpose of this document is to respond to the oral and written comments received through the public comment period and public hearing.

The public comment period for this rulemaking began December 13, 2006 and ended January 17, 2007.

Public hearings were held on: December 13, 2006 in Tukwila with 38 people attending; December 14, 2006 in Spokane with 32 people attending; December 15, 2006 in Tumwater with 28 people attending; and December 18, 2006 in Yakima with 15 people attending.

The proposed rule would reduce a surplus in the medical aid fund by temporarily eliminating worker and employer payments into the fund – a rate holiday.

Comments received from workers and worker representatives were supportive of the proposal because they felt that a rate holiday is the best way to ensure that half the surplus is distributed to workers.

Employers and employer representatives were generally supportive of the idea of reducing a surplus, but many expressed a preference for leaving rates steady and distributing the surplus via a dividend.

Several participating employers and retrospective rating group sponsors expressed concern about the reduced retrospective rating group refunds that would result from a rate holiday.

Insurance principles require that any surplus be distributed to those who contributed to the surplus in proportion to their relative contributions. Insurance principles also require that the design of any surplus distribution take into account practical considerations so

that resources used in distributing the surplus are minimized and the amount distributed is maximized.

By law, workers contribute half of the premiums paid into the medical aid fund. Therefore, the principle of contribution requires that the department return half of the surplus to workers.

The department considered three possible mechanisms for distributing the surplus to workers. The rule as proposed would distribute the surplus by eliminating worker premium payments in the second half of 2007. The department also considered making direct dividend payments to workers, and making payments to employers that employers would be required to pass on to workers.

Making direct dividend payments to workers is problematic because employers do not report workers to the department individually. The department considered whether it could overcome this obstacle by obtaining information on individual workers from the Employment Security Department. Because coverage under Title 50 is not identical to coverage under Title 51, the department determined the administrative cost of this approach would be high.

The department considered making payments to employers that employers would be required to pass on to workers. However, this approach would impose on employers a significant cost: it would require employers to identify workers and determine each workers' share of the surplus distribution.

Workers and worker representatives commenting on the rule supported a rate holiday. Given the relative efficiency of this approach, the department has decided that workers will receive their half of the medical aid surplus by the department eliminating medical aid premiums for the second half of 2007, thereby eliminating worker contributions to those premiums.

Employers want to receive a surplus distribution from the medical aid fund, but also prefer a dividend, and are concerned about the effect of lowering rates for six months only to raise them for 2008.

The department considered distributing the employers' share of the surplus via dividends while eliminating premium contributions for workers. However, RCW 51.16.140 will not allow this as it requires employers to deduct from worker pay half of any medical aid premiums they are required to pay.

The department considered the concerns expressed about rate stability. In 1996, the department distributed a surplus by reducing rates. The department announced this rate reduction as being for a set time period, and no employers reported to the Department that this temporary rate reduction caused any problems. In the late 1990s and early 2000s the department distributed a surplus in the medical aid fund by setting rates low. This was not publicized as being for a limited duration. When the surplus was dissipated and

rates were returned to normal levels, the abrupt rate change did cause problems for employers.

In light of these experiences, the department has concluded that employers will not experience trouble if medical aid premiums are eliminated for the second half of 2007 because employers will know that this is a temporary measure.

The department has decided that the benefits of distributing the worker share of the surplus to workers via a temporary elimination of medical aid premiums outweigh employers' concerns about rate instability and their stated preference for dividends.

There were concerns expressed that those receiving the benefit of the rate holiday in 2007 will not be the same as those who contributed to the surplus by paying premiums in prior years. Whenever a surplus is distributed, the goal of distributing the surplus proportionately to those who contributed to the surplus must be tempered by practical considerations so that the surplus is not consumed by the cost of distributing the surplus. The rate holiday approach does not perfectly distribute the surplus to those who contributed to the surplus. Employers and workers who otherwise would be paying more in 2007 than in prior years will receive more than they would using other approaches, and employers and workers who otherwise would be paying less in 2007 will receive less. However, the cost of distribution is far lower using the rate holiday approach which leaves more surplus to be distributed. The rate holiday approach does quite accurately distribute the surplus to employers as a class and workers as a class in proportion to their contributions, and will accurately distribute the surplus to the vast majority of employers and workers whose employment pattern in 2007 will be comparable to prior years. Considering the costs and benefits of the rate holiday and other distribution approaches, the department has concluded that the efficiency of the rate holiday distribution method outweighs concerns about its imprecision.

Retrospective rating adjustments are calculated so that retro employers pay the same percentage of the cost of claims as non-retro employers. A consequence of eliminating medical aid premiums for the second half of 2007 would be a reduction in total net retrospective rating refunds. Retrospective rating adjustments are paid out of the accident fund. Consequently, this anticipated reduction in refunds led to the reduced accident fund rates in the proposed rule.

Employers and retrospective rating group sponsors expressed concern about the reduction in retro refunds. In light of these concerns, the department has decided to use a different mechanism to maintain the actuarial balance between retro and other employers. The rule being adopted will not reduce total net retrospective rating refunds, and so does not reduce accident fund premiums. Instead, the department will pay dividends to non-retro employers in 2008. This approach will maintain the actuarial balance between retro and other employers while eliminating the reduction in retro refunds.

