The Ohio Manufacturers' Association
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THE POLICY POINT: *Workers' Comp Rate Reform*

On October 30, 2009, the Ohio Bureau of Workers' Compensation (BWC) Board of Directors approved rate reforms for the 2010–11 plan year designed to continue progress toward increasing the fairness of premiums paid by Ohio's employers.

These most recent reforms include (a) lowering the maximum group-rating discount from 77 percent to 65 percent and (b) modifying the "break even" factor so it applies to group-rated employers on a graduated scale that better aligns each employer's premium with the risk the company brings to the system.

As important as these changes are to the restructuring of Ohio's workers' compensation rate structure, additional improvements are needed. The OMA both applauds the BWC for the significant progress that has been achieved in recent years and challenges Bureau leadership to stay the course with continued reforms needed to enhance benefits for all participants.

An Imperative to Restore Ohioans' Confidence in the BWC

When the Ohio General Assembly passed House Bill 100 in May 2007, with bipartisan support, the message from lawmakers was crystal clear: No longer would "business as usual" be tolerated at Ohio's Bureau of Workers' Compensation. It was a new day with new expectations for how the BWC would go about serving the needs of Ohio's injured workers and their employers.

Among the changes provided for by House Bill 100 were the following:

- Abolishing the Workers' Compensation Oversight Commission and replacing it with a newly created Workers' Compensation Board of Directors
- Directing the Board to "safeguard and maintain" the solvency of the State Insurance Fund
- Directing the Board and the BWC Administrator to "fix and maintain" the lowest possible rate and premium consistent with maintaining a solvent fund and a reasonable surplus

House Bill 100 also required a thorough examination of the Bureau's governance, processes, programs and rates. In response to that directive, Deloitte Consulting Inc. was engaged in January 2008 to conduct a comprehensive review of BWC operations.

The Deloitte study, which was released in April 2009, identified fairness, equity and solvency problems with the BWC's group-rating program as priorities for reform. In particular, the report noted the following:

- A significant disparity existed in workers' compensation rates paid by group-rated employers and non-group-rated employers.
- Non-group-rated employers were subsidizing a portion of group-rated employers' premiums.
- Group-rated employers' large premium discounts (up to a maximum of 95 percent) had no actuarial justification.

The findings—and recommendations that the Bureau take action to address inequities in its experience-rating methodology—were consistent with those in a report issued by the Office the Inspector General of Ohio in August 2007 (which noted, among other things that the "staggering" savings enjoyed by group-rated employers had long been "unfairly subsidized" by non-group-rated employers), as well as a number of other third-party studies. **At least nine actuarial analyses during the past 20 years concluded that group-rating discounts have not generated adequate premiums to cover claims costs for group-rated employers and that non-group-rated employers have been paying higher rates than warranted in order to close that shortfall.**

It was within this context that the BWC developed a master plan in June 2008 that outlined a number of significant reforms designed to bring fairness and equity to group-rated and non-group-rated employers alike. The Deloitte Report, along with comprehensive actuarial data, has served as the blueprint for these reforms.

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A Closer Look at the Rationale for Rate Reform

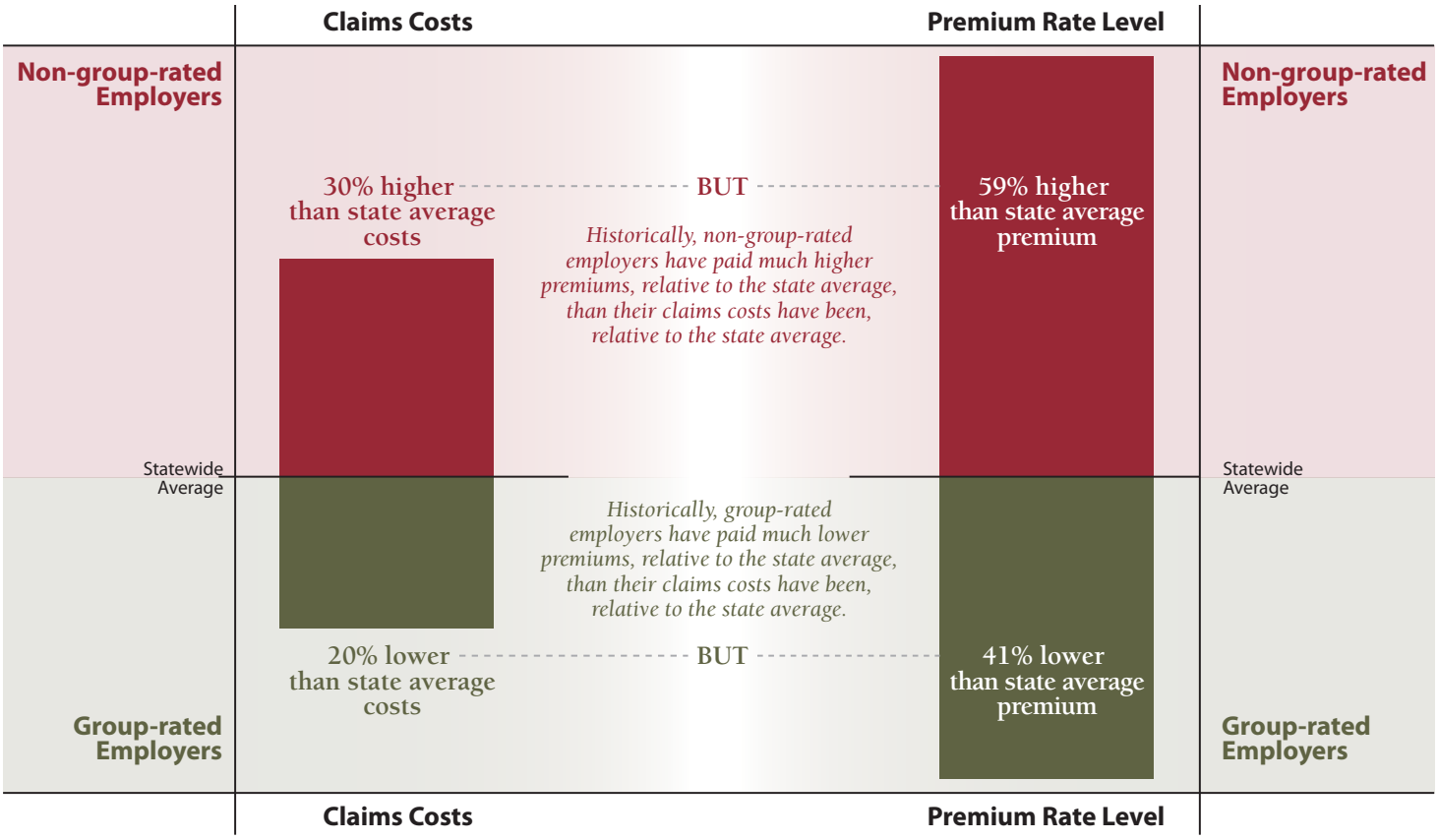
Group rating was introduced in 1991. It allows employers in similar industries to pool together for experience rating, a method of predicting an employer's potential for incurring claims losses, used to set its workers' compensation rates. Group rating has served a useful purpose in helping to improve workplace safety and in getting employers more actively involved in keeping their workers' compensation costs down. Currently, Ohio has about 90,000 group-rated employers and about 115,000 to 120,000 non-group-rated employers statewide.

The problem with group rating as it has functioned over the past 20 years is pretty straightforward: There has been a lack of alignment between the premiums individual employers pay for workers' compensation coverage and the cost of the claims they bring to the system. That problem has manifested itself in a number of ways, including a significant "gap" between the premiums paid by group-rated employers and the premiums paid by non-group-related employers. While it was never the intent or design of group rating to produce rate-making practices that would be unfair to any class of employers, that is exactly what evolved over time.

The disparity is clearly apparent, for example, when you look at loss ratio, which is a measure of the relationship between the cost of claims and the premium meant to cover those claims. Group-rated employers' loss ratios historically have been more than twice as high as those generated by non-group-rated employers. This tells us that group-rated employers have not been paying sufficient premium to cover the cost of their claims losses. And that has been due largely to the high discounts on premium the group-rating program historically has offered to employers—as high as 95 percent just four years ago before the BWC began to reduce the maximum allowable discount.

In the past, to offset the group-rating discounts, the BWC simply increased the base rate for all employers. Because the Bureau is a revenue neutral entity, the premium shortfall was made up by collecting additional premium from non-group-rated employers. The result was that group-rated employers' discounts essentially were being subsidized by non-group-rated employers—a subsidy that totaled nearly $300 million dollars in 2008.

Lack of Alignment of Claims Costs with Premium Rate Level



Historically, employers' workers' compensation premiums have not aligned with the risk and costs they bring to the system.

The solution was clear and simple: The BWC needed to collect its premium in an equitable manner. And the Bureau needed to set rates for both group-rated and non-group-rated employers at levels that are actuarially sounds—i.e., at levels commensurate with the risk these employers present to the system.

The problem with group rating as it has functioned over the past 20 years is that there has been a lack of alignment between the premiums individual employers pay for workers' compensation coverage and the cost of the claims they bring to the system.

Phased-in Reductions in Group Rating's Maximum Discount

Plan Year	Maximum Group Discount
2005-06	95%
2006-07	93%
2007-08	90%
2008-09	85%
2009-10	77%
2010-11	65%

As a result of these reductions in the maximum group-rating discount—spread out over a number of years to soften the impact on group-rated employers—the historical cost shifting among employers has been reduced.

Saying goodbye to politically driven rate-setting

Unfortunately, politics have had a hand in workers' compensation rates. Despite clear actuarial evidence that reducing group-rating's maximum discount was needed to ensure fairness and equity, certain groups have been resisting these and other reforms. The historical group-rating methodology and experience-rating system have created substantial income and political influence for "third-party administrators" (TPAs) and group-rating sponsors. Not surprisingly, those constituencies have been reluctant to give up either in the interest of moving Ohio forward.

And yet, despite strong opposition and vigorous lobbying by some TPAs and group-rating sponsors, progress is being made.

Over the past two years, the BWC has approved and implemented a number of welcome reforms to the policies and formulas used to set employers' workers' compensation rates. The desired outcomes of these reforms have been to (a) treat all employers fairly and equitably by ensuring that every employer pays a premium based on the risk it brings to the system, (b) protect the stability and solvency of the State Insurance Fund to ensure that the needs of injured workers' are met, and (c) position Ohio with a competitively priced workers' compensation system that will support the state's continuing ability to attract economic development.

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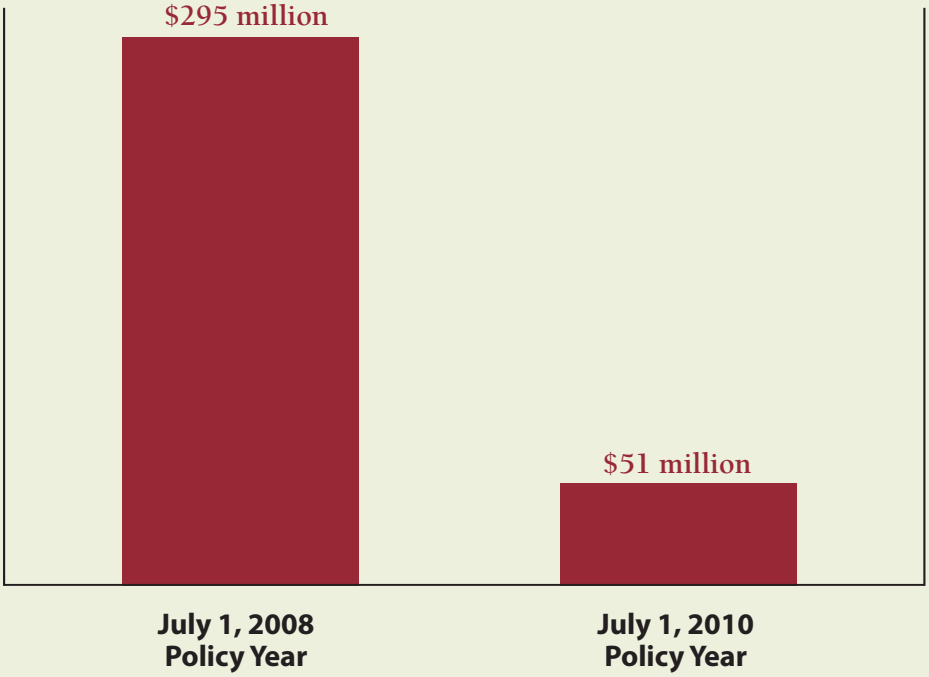
Two major focal points for the BWC's reform efforts have been (a) gradual reductions in the maximum group-rating discount and (b) closing the gap between what group-rated employers and non-group-rated employers pay for workers' compensation premiums.

Reducing group-rating's maximum discount

Multiple actuarial studies have shown that reducing group-rating's maximum discount would better align premium with claims costs of individual employers—and improve pricing equity among employers. The BWC began phasing in a reduction of group rating's maximum discount in the 2006-07 plan year, gradually cutting it from 95 percent to the current maximum of 77 percent (for plan year 2009–10). On October 30, 2009, the BWC Board approved an additional reduction, from 77 percent to 65 percent, effective in the 2010–11 plan year.

As a result of these reductions—spread out over a number of years to soften the impact on group-rated employers—the historical cost shifting among employers has been reduced (though not totally eliminated).

Estimated Subsidization of Group-Rated Employers by Non-Group-Rated Employers



Rate reforms implemented by the BWC have helped reduce, but not totally eliminate, the unfair subsidization of group-rated employers by non-group-rated employers.

Applying a "break-even factor" to further narrow the premium gap

Lowering group rating's maximum discount has helped to restore a large measure of balance and fairness to worker's compensation rates, but it has not been enough to completely close the gap between group-rated employers' premiums and non-group-rated employers' premiums. Nor has it produced premium rates that are completely aligned with the risk each employer brings to the system.

To better understand the gap, consider that historical claims costs for group-rated employers are about 20 percent lower than the statewide average, and claims costs for non-group-rated employers are about 30 percent higher than the statewide average. In a properly aligned and actuarially sound system, you would expect to see premium rates that reflect the two groups' respective impact on system costs.

To better align premium with risk, the BWC created a so-called "break-even factor"—a mechanism for applying an assessment to group-rated employers to ensure adequate premium is collected from them and to further reduce the unfair subsidization of group-rated employers by non-group-rated employers.

However, that is not the case in Ohio. In 2008, group-rated employers' rate level was 41 percent lower than the statewide average rate level (compared to claims costs that were just 20 percent lower than average). Non-group-rated employers' rate level was 59 percent higher than the average statewide rate level (compared to claims costs that were just 30 percent higher than average). These discrepancies clearly illustrate the problem of group-rated employers being subsidized by non-group-related employers.

To help close this gap and achieve better alignment of premium with risk, the BWC created a so-called "break-even factor"—a mechanism for applying an assessment to every group-rated employer to ensure that adequate premium is collected from those employers and to further reduce the unfair subsidization of group-rated employers by non-group-rated employers.

For the 2009–10 plan year, the BWC applied a flat break-even factor across the board on premium rates for all group-rated employers. This, in combination with the reduction of the group-rating maximum discount from 85 percent to 77 percent and other adjustments to the rate-setting methodology, resulted in the following changes:

- Nearly a 25 percent reduction in premium for non-group-rated employers
- A 9.6 percent increase in premium for group-rated employers
- An overall, system-wide reduction in base rates of about 12 percent

For the 2010–11 plan year, the BWC Board approved an important modification to the break-even factor. Instead of a flat assessment applied evenly across the board to all group-related employers regardless of an individual employer's premium discounts or claims experience, in 2010 the break-even factor will be assessed in a graduated fashion. Employer groups with higher discounts (i.e., those contributing

more to the off balance) will be assessed a higher break-even factor, and groups with lower discounts will be assessed a lower break-even factor.

Overall, the break-even factor for 2010 will be slightly lower, on average, than it is for 2009. More importantly, it will be applied more fairly and equitably. Some TPAs and group sponsors lobbied hard to have the break-even factor abolished, but actuarial analysis indicated that base rates likely would have increased for all employers under such a scenario.

While it's too early to know for certain the precise impact on rates that the BWC Board's October 2009 actions will have, overall the change will be revenue neutral.

Restoring fairness and equity to rate-setting

With these latest rate reforms, the BWC has achieved a number of important objectives:

- A rate structure in which premium costs are applied more fairly and equitably among all employers in the system
- A rate structure in which employers pay premiums more closely aligned with the risk and costs they bring to the system
- A system that fully pays for itself
- A system that is more stable and solvent
- Lower base rates that enhance Ohio's competitive position in the Midwest

Just as critically, Ohio now has a workers' compensation rate structure that will serve as a solid foundation for additional reforms that will further strengthen the system, better serve injured workers and employers, and make Ohio even more attractive for economic expansion and development.

Rate Reform Just One Dimension of Effort to Build Operational Excellence Into the BWC

The OMA has long believed that a professionally and efficiently operating Bureau of Workers' Compensation is critical to retaining and creating jobs in Ohio. That's why the OMA was an advocate for House Bill 100, legislation passed in 2007 establishing new models for governance, transparency and accountability at the BWC and also requiring the use of sound actuarial science in the Bureau's rate-setting. Among other things, HB 100 created a new Board of Directors to serve as the BWC's governing body and, along with the BWC Administrator, to share fiduciary responsibility for Ohio's workers' compensation system.

Under the leadership of the new Board and Administrator, rate reform has been a major focus of work at the Bureau during the last two-plus years, and the number-one accomplishment at the BWC during this time has been bringing greater parity to both group-rated and non-group-rated employer premium rates (the primary focus of this edition of *Retooling Ohio*). However, the BWC and the Industrial Commission of Ohio (the claims adjudication arm of Ohio's workers' compensation system) have been working on multiple additional reforms. Following are selected improvements since 2008.

Selected BWC Improvements

- Launching of MIRA II reserving system that provides more responsive, accurate claims reserves
- Back-to-back rate decreases for private employers (5 percent in 2008, 12 percent in 2009—the first average decreases since 2001)
- An average 25.3 percent rate decrease for non-group-rated private employers
- Two rate decreases for state agencies, universities and university hospitals (10 percent in 2008, 3.75 percent in 2009—their first average decreases since 1999)
- A 5 percent premium rate decrease for public employers
- A 100 percent cap option on premium increases due to an employer's claims history, to limit extreme cost swings for affected employers
- Beginning a transition to a multi-split experience-rating plan that will take into account the frequency as well as the severity of an employer's claims, thus improving experience rating accuracy
- Two new insurance options—deductible and group retrospective—designed to lower out-of-pocket costs for employers and improve safety for workers
- Updated inpatient hospital fee schedules for physicians and other medical professionals who provide care for injured workers
- Elimination of redundancies in the alternative dispute resolution process to ensure timely, quality care for injured workers
- Monthly Enterprise Report to provide a transparent record of agency-wide financial and operational performance metrics
- New investment policy statement to strengthen investment returns
- New implementation strategy for diversifying State Insurance Fund fixed-income and equity investments

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Selected Industrial Commission (IC) Improvements

- Continued IC's long history of minimal budget increases that have averaged just six-tenths of one percent annually
- Decreased IC workforce by more than 150 employees (over the last several years) while continuing to meet and exceed statutory requirements for timely service
  - For example, from the date an appeal was filed to the date of the hearing, first-level hearings averaged 29.5 days, and second-level hearings averaged 27.5 days, both well within the statutorily mandated 45-day time frame.
- Implemented a variety of cost-saving measures that are expected to save IC more than $15 million over the next five years
  - Consolidated several district offices (Springfield/Dayton, Canton/Akron, Bridgeport/Zanesville/Cambridge, Hamilton/Cincinnati)
  - Consolidated office space in IC's Columbus office, which will save $800,000 annually
  - Converted standard telephone service to Voice-Over Internet Protocol telephone service, which is expected to save $865,000 over five years
  - Reduced employee overtime and overnight delivery, saving more than $58,000 annually
  - Consolidated and streamlined IC's supply ordering process, which has reduced supply purchases by more than $60,000 annually
- Launched a new Web site that enhances and accelerates customer service
- Implemented technological advances that have made it easier to file appeals on the Web and to submit questions to IC's Customer Service Department
- Implemented a new automated tracking system for customer service
- Implemented new Customer Service and Word Processing Pools to provide a more flexible, efficient way of doing business and managing changing workloads

There is much more to be done, but these many improvements to Ohio's workers' compensation system are helping to ensure more equitable and accurate rates and improved services, which in turn will aid Ohio's efforts to retain existing jobs and attract new investment and additional jobs.

Why The OMA Supports Rate Reform

The OMA is a provider of workers' compensation group-rating services. Yet, unlike many other group-rating sponsors, we fully support the BWC's recent rate reforms. Many have asked why this is so.

The OMA's mission is to protect and grow manufacturing in Ohio, and we support public policy that improves Ohio's manufacturing competitiveness. We are fundamentally opposed to government policies in any area that pick winners and losers, or that punish one class of manufacturers to benefit another. Unfortunately, however unintentional, that has been the case with workers' compensation group rating in our state.

The OMA believes workers' compensation rates should be driven by actuarial data. And we agree with the many actuarial studies that have concluded that historical group-rating discounts are too high and cause non-group-rated employers to pay too much premium. That's why the OMA has supported the BWC's reengineering of its rate structure—in particular the continued, phased-in reduction of the maximum group-rating discount and the application of a graduated break-even factor to eliminate the continued subsidizing of group-rated employers by non-group-rated employers.

These changes will help ensure that each Ohio employer will pay the right premium for the risk the company brings to the system. They will lower base rates across the whole workers' compensation system and distribute them more fairly among employers based on actuarial experience. Employers with low claims will enjoy lower rates, while employers will higher claims (and thus greater costs to the system) will pay higher rates. This will bring not just fairness but also stability to the system.

Our bottom line? The OMA is committed to helping to ensure that all businesses pay fair workers' compensation rates commensurate with the risk they bring to the system, that injured workers receive fair and timely benefits and the support they need for getting back to productive work quickly and safely, and that the state's workers' compensation insurance fund remains actuarially sound. Those are good outcomes for Ohio manufacturers,—and good outcomes for Ohio's overall economy.

These changes will help ensure that each Ohio employer will pay the right premium for the risk the company brings to the system. This will bring not just fairness but also stability to the system.

Next Steps in Workers' Compensation Reform

Rate reform was the necessary prelude to additional structural reforms at the BWC that are needed to eliminate unnecessary costs within the system and provide enhanced benefits to all Ohio employers and injured workers. We know additional reforms are needed, and there is no reason to delay action on other critical fronts.

The OMA intends to work with its member companies, the BWC and the legislature to enact reforms that will improve processes for injured workers and employers and continue to drive system costs down.

The Deloitte study released in January 2009 included a large inventory of recommended system improvements, including a number that will require statutory changes that the Ohio General Assembly will need to take up. The OMA intends to work with its member companies, the BWC and the legislature to enact those reforms that will improve processes for injured workers and employers and continue to drive system costs down. Among the next-phase reform concepts for consideration are the following:

- **Rebuttable presumption drug statute:** Eliminate the "reasonable suspicion" standard and incorporate the Louisiana Pacific standard of "voluntary abandonment" for benefits.
- **Self-Insured Employers' Guaranty Fund:** Solve securitization, claims management and accountability problems.
- **Industrial Commission hearing inconsistencies:** Require hearings to be recorded for improved consistency in outcomes.
- **BWC claims management problems:** Improve consistency in delivery against claims management performance standards.
- **Rate-making transparency:** Develop data and reporting on component costs within premium rates.
- **Permanent total disability as retirement benefit:** Establish retirement benefit offsets and/or age or number-of-weeks capping.
- **Permanent total disability (PTD) multiple applications:** Require claimants to show new and changed circumstances when filing for PTD benefits more than once.
- **Permanent partial disability transaction costs:** Lower transaction costs by allowing telephonic hearings.
- **Permanent partial disability impairment standard:** Establish impairment standard (no consideration of non-medical factors).
- **Permanent partial disability (PPD) multiple applications:** Require claimants to show new and changed circumstances when filing for PPD benefits more than once.
- **Temporary total disability (TTD):** Terminate the compensation paid for TTD as of the date established by the medical evidence establishing maximum medical improvement.
- **Temporary total disability:** If a claim for workers' compensation is suspended due to a claimant's refusal to provide a signed medical release or attend the employer's medical examination, the claimant forfeits his or her right to benefits during the period of suspension.
- **Payment without prejudice:** Allow employers to pay compensation and medical bills without losing the right to contest a claim.
- **Actuarial integrity:** Eliminate BWC programs that have no actuarial foundation.
- **Managed Care Organization reforms:** Study the effectiveness of the Managed Care Organization system in Ohio, including possibly requiring MCOs to unbundle their services and compete on price.

The mission of The Ohio Manufacturers' Association is to protect and grow Ohio manufacturing. Through the OMA, manufacturers and manufacturing stakeholders work directly with the members of the Ohio General Assembly, state regulatory agencies, the judiciary community and statewide media with the sole focus of improving business conditions for manufacturers in Ohio.

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