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Midwest Employers Casualty | a Berkley Company

Evaluating Self-Insurance in Washington State

Finance, Risk Management, and Excess Insurance

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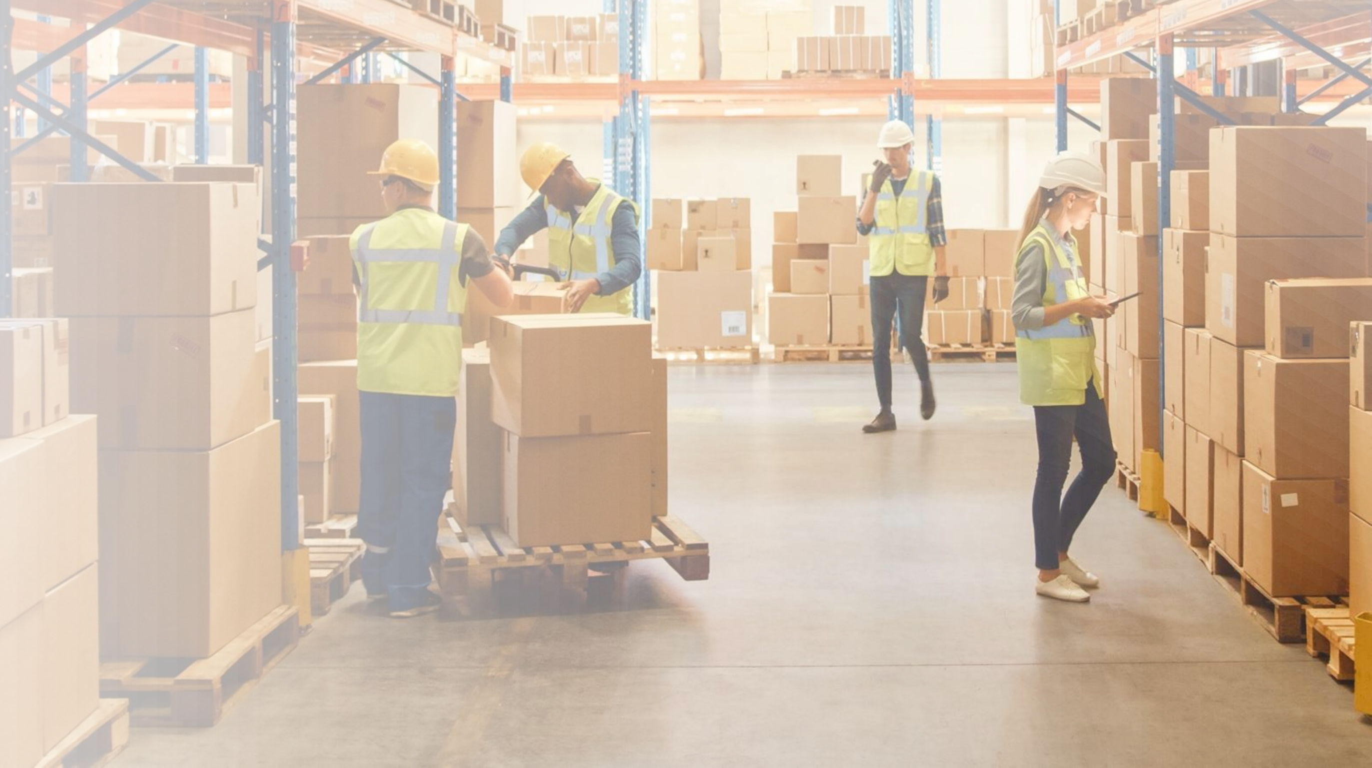


Agenda

- Why Self-Insure?
- Total Cost of Risk
- Does Self-Insurance Make Sense for You?
- Pursuing Self-Insurance
- Excess Insurance
- Long Term Commitment

Why Self-Insure?

Why Self-Insure?

Advantages to Your Program

Self-Insuring in WA

Business Growth and Contraction

- Mergers & Acquisitions – **new structure** supports business need
- Major expansion and growth – **increasing liabilities**
- Financial advantage to **the bottom line**
- **Alignment** with other states

Cash Flow Advantage

- **“Pay as you go”** rather than premium in arrears
- More **control** over financials

Program Control

- Claim management **oversight**
- Ability to **issue claim decisions and orders**
- Increased **influence** in claim process
- **Flexibility** around participating vendors

Employee Advocacy

- Increased ability to **assist employees** through the process
- **Greater control** in communicating with employee – ensuring understanding of available resources
- **Reduced litigation**

Vendor Partnerships

- Litigation management
- Nurse case management
- Utilization review
- Pharmacy management
- Subro/investigation
- Vocational rehabilitation

Total Cost of Risk

Establishing a Casualty Framework

Positioning you to make informed risk decisions that support your organizational strategies and goals

Prevent accidents — Deploying effective safety management strategies to reduce illness and injuries

Optimize structure — Achieving the right balance between risk transfer and retained risk

Protect balance sheet — Enhancing limits and coverage

Maximize liquidity — Executing creative risk financing solutions

Mitigate claims severity — Implementing innovative cost containment strategies

Enablers

- Industry focus
- Data and analytics
- Specialists
- Service
- Partnerships
- Contractual risk management

Results

- Safe work environment
- Expense reduction
- Volatility management
- Maximize contract certainty
- Lower claim costs

Engagement Framework | **Digital Enablement** | **Service "365"**

Components of Your Total Cost of Risk

Self-Insured program rather than guarantee cost (State Fund)

DEFINE RISK

Be fully aware of cost of risk drivers

DESIGN SOLUTIONS

Design solutions to address these costs

DELIVER RESULTS

Execute on strategies and measure performance

Total Cost of Risk

Loss Costs

- Post injury response protocol
- Medical provider networks (Same)
- RTW programs
- Claim oversight & advocacy

Risk Prevention Costs

- Evaluate trends for intervention
- Design/implement safety plans
- Assess/provide ergo environment

Claims Management Costs

- TPA and managed care costs
- Detailed Client Svc Instructions
- Regular claim review and audits

Admin Costs

- Excess and surety purchase
- Second Injury Fund usage
- Self-Insurance Admin
- Insolvency Trust
- Supplemental Pension & Asbestos

Implied Risk Charge

- Manage financial volatility
- Settlement strategy and closing philosophy

Savings Opportunity

Optimized Total Cost of Risk

Prioritize new cost savings opportunities

Does Self-Insurance Make Sense for You?

Is Self-Insurance the Right Choice?

Evaluating the commitment

Organizational Responsibilities

- Maintain **excess insurance** and **surety**
- Claims **administration** and safety/loss **prevention**
- **Notification** to employees
- **Quarterly and annual filing** of claim costs and worker hours
- Annual **audited financial statements**

Financial Perspective

- Annual loss spend of appropriate zine (**min. surety = $1M**)
- Financial capability to manage **fluctuating costs**
- Ability to pay for **required administration** (internal and external)
- Capability to pay **assessments and pensions**
- Escrow account for **~2.5 months of loss payments**

Parental Guarantee

- Parent must obligate or **additional surcharge** may apply
- Typical surcharge ~**25% of surety** requirement
- Regardless of M&A – self-insurance liabilities **remain with the self-insurer** (i.e., do not transfer to purchaser)

Pursuing Self-Insurance

Once the Decision is Made

Pursuing self-insurance certification

01 Meet Qualifications

- Be in business in State of WA for three (3) years
- Assets of at least $25M, or $50M in annual revenue, or annual WC premium or loss payments of at least $1M (verified by audited financial statements)
- Meet financial standards
- Have an L&I approved written accident prevention program in place 6 months prior to application
- Designation of individual or third party administrator

02 Application Process

- Process takes three months to complete and coincides with natural quarters
- Failing application process – must wait 6 months to reapply

03 Application Requirements

- Complete Self-Insurance Certification Questionnaire
- 3 years audited financial statements (most current)
- Check for $250
- Copy of written accident prevention program
- List of all subsidiaries/divisions in WA and demographic information
- Description of organization administering claim program
- Name and qualification of contact person (claim and safety)

Once the Decision is Made

Additional considerations during and after certification

01 Surety Amount

- May consider **actuarial evaluation** of losses if surety level above $1,000,000
- **Annual premium** would have paid to state industrial insurance fund
- Average of **last five years'** developed incurred costs
- Minimum surety (average cost of **one total permanent disability award)**

02 TPA Evaluation

- Licensed by LNI
- Knowledgeable in WA claim adjudication
- Capable of timely distribution of employee benefits and claim/vendor payments
- Appropriate management information systems to account for losses and complete required reporting

03 Excess Insurance Placement

- Retention level
- Policy limits – specified or statutory

04 Best Practices

- High performing claim management practices (e.g., compliance, employee satisfaction, effective cost containment practices)
- Effective medical cost containment strategies and programs
- Capability to integrate WA data/loss information with other state programs
- Regular and effective stewardship

05 Safety Evaluation

- Partnership with DOSH to enable approval of accident prevention program

06 Monitor Program Performance

- Frequency Rate/Severity (Claims per workhours)
- Percent Expense for Lost Time claims
- Percent Medical Cost for Lost Time claims
- Reporting lag time
- Claim closure performance

07 Funding Mechanism

- Need to establish a bank account or other funding mechanism to issue payment and benefits
- Typically ~2.5 months of average loss payments

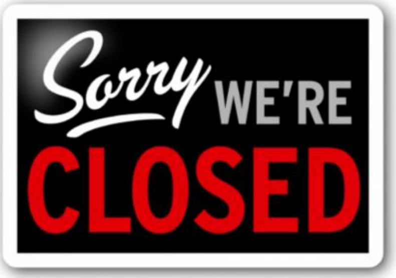
Excess Insurance

Excess Workers' Comp Carriers

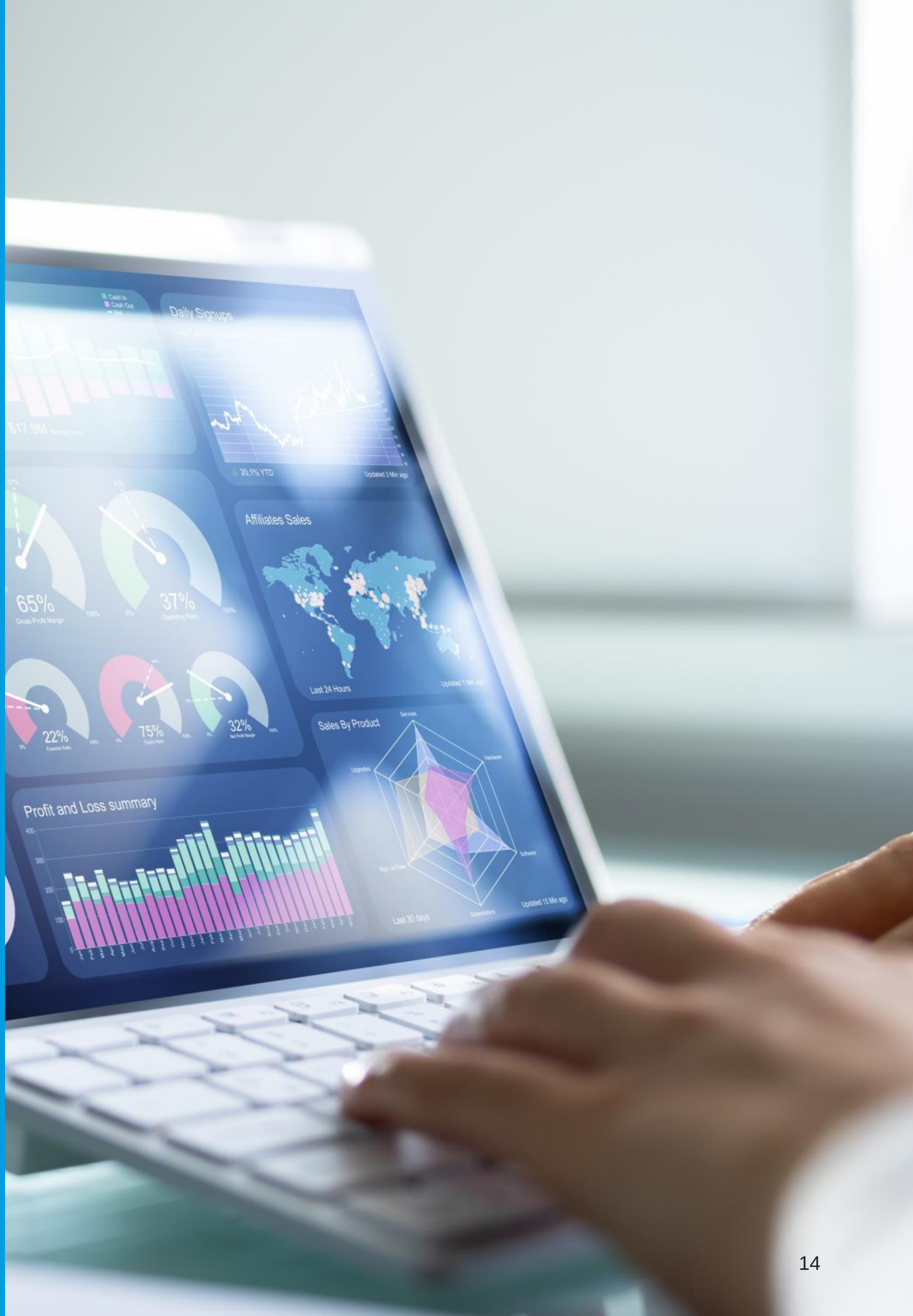
Past performance limits current market

- In the last soft market, there were numerous "A" (+/-) carriers writing Excess WC

- Those carriers are no longer in business or no longer writing Excess WC. (AIG, ERC, Frontier)



Why ? | Claims caught up with these carriers and they lost money



Excess Workers' Comp Carriers

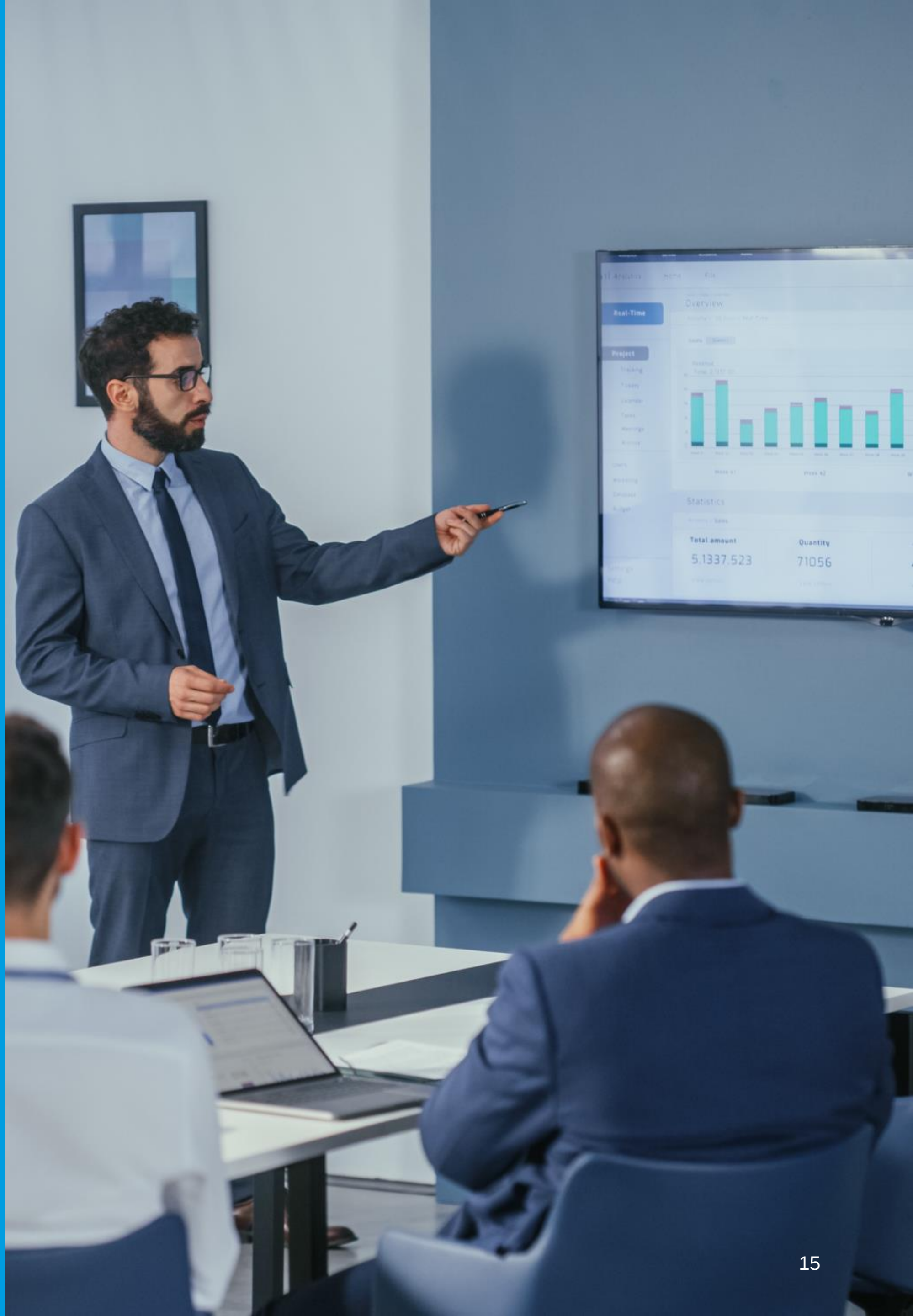
Current market

Carriers Exiting the Market

At an industry event in January 2011, Kristian P. Moor, president and CEO of Chartis, said "workers' compensation is underpriced and the company will continue to exit the market".

Current Market

- 3100 P&C Insurers Operating in the U.S
- 6 to 8 Currently Provide Excess Coverage for Self Insured Employers
- 2 are Specialists



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Excess Workers' Comp Market

Common misconceptions

All Excess Workers' Compensation carriers are the SAME

"We've never had a loss above our SIR . . ."

Focus is centered on PREMIUM rather than LOSSES

Primary Workers' Compensation = **Excess** Workers' Compensation

Excess Workers' Comp

Characteristics of excess v. primary

Excess WC	Primary WC
Low Frequency	High Frequency
High severity	Low severity
Unpredictable	Very predictable
50 year pay out	5 to 7 year payout
Small % of normal premium collected (Premium is not cost/plus)	100% normal premium collected (Premium is cost/plus)
Greatly impacted by medical inflation	Moderately impacted by medical inflation Reinsurance Purchased
Significant exposure to changes in medical technology	Minor exposure to changes in medical technology
Excess Premium – one of the least expensive insurance costs for client	Primary WC Premium is 40-60% of total insurance cost

Excess Workers’ Comp

Underwriting process

Information Required

- Description of operations, safety processes, claims administration
- Ten years’ prior losses, including experience modification worksheets
  - Detailed loss information for any claim over $50,000
- Ten years prior payroll/workhour data
- Budgeted payroll/workhours for coming year by class code (may require by location)

Program Considerations

- Determine appropriate retention level
  - Per occurrence retention
  - Aggregate retention might be available
- Evaluate policy limit
  - Specific excess limit
  - Statutory excess limit

Excess Workers’ Comp

Economic environment

- Declining investment income and low interest rates have placed additional pressure on underwriting results. Medical inflation is an additional complication.

- The historically low interest rate environment has put substantial pressure on excess rates. Interest rates have an effect on how much carriers can discount expected losses. This effects the level of pricing flexibility

Excess Workers' Comp

Emerging cost trends

- Obesity Epidemic
- Aging Workforce
- Medical Costs
- Economic Environment

It’s a Long Term Commitment

Self-Insuring in Washington State

Long term commitment

Considerations

- Engage in partnerships to take advantage of opportunities and maximize the benefits of self-insuring
- Leverage your broker to guide you through the process and during self-insurance
- LNI is a great business partner as well as a regulator

Evaluate

- Ensure your excess insurance and surety purchases are competitive
- Manage third party administrator and other medical management components to appropriately contain costs and deliver benefits
- Make sure safety programs are preventing accidents and your experience modification factor is at or above industry average

Thank You!