

Workers' Compensation Insurance Rating Bureau of California

California Regulatory Update Workers' Compensation

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WCIRB^{California}®

California Regulatory Update – Workers' Compensation

Overview of Presentation

- Pre-Reform Environment
- Reform Summary
- Post-Reform Experience
- Outlook For Future

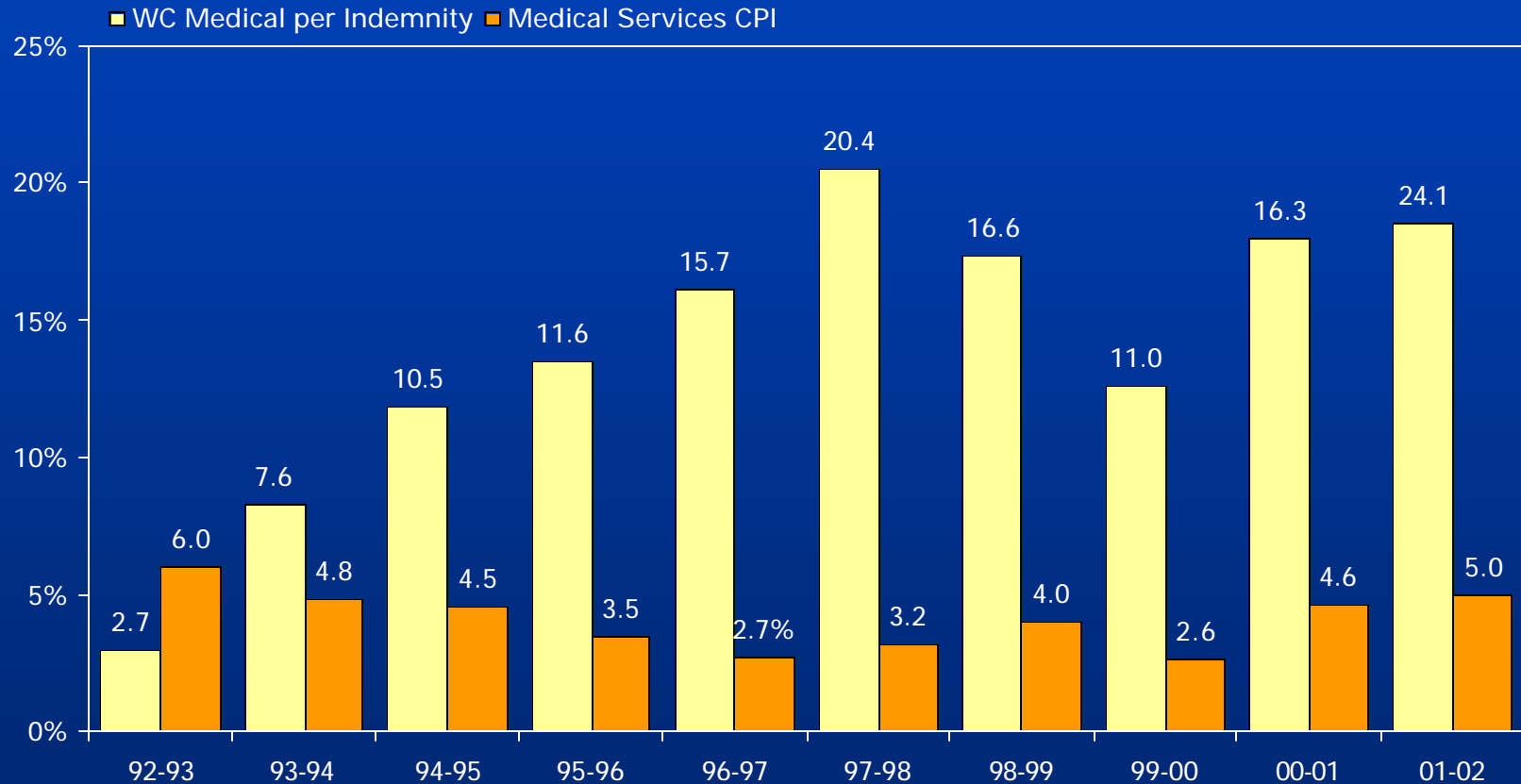
Pre-Reform Environment

- Injured Worker Perspective
 - Low weekly benefits
 - System riddled with delay and litigation
- Employer Perspective
 - Sharply rising premium rates
 - Limited markets
 - Businesses leaving state
- Insurer Perspective
 - Sharp medical inflation
 - High permanent disability costs
 - Record high loss and combined ratios
 - Huge reserve deficiencies
 - Many insurer insolvencies
 - State Fund market share growing

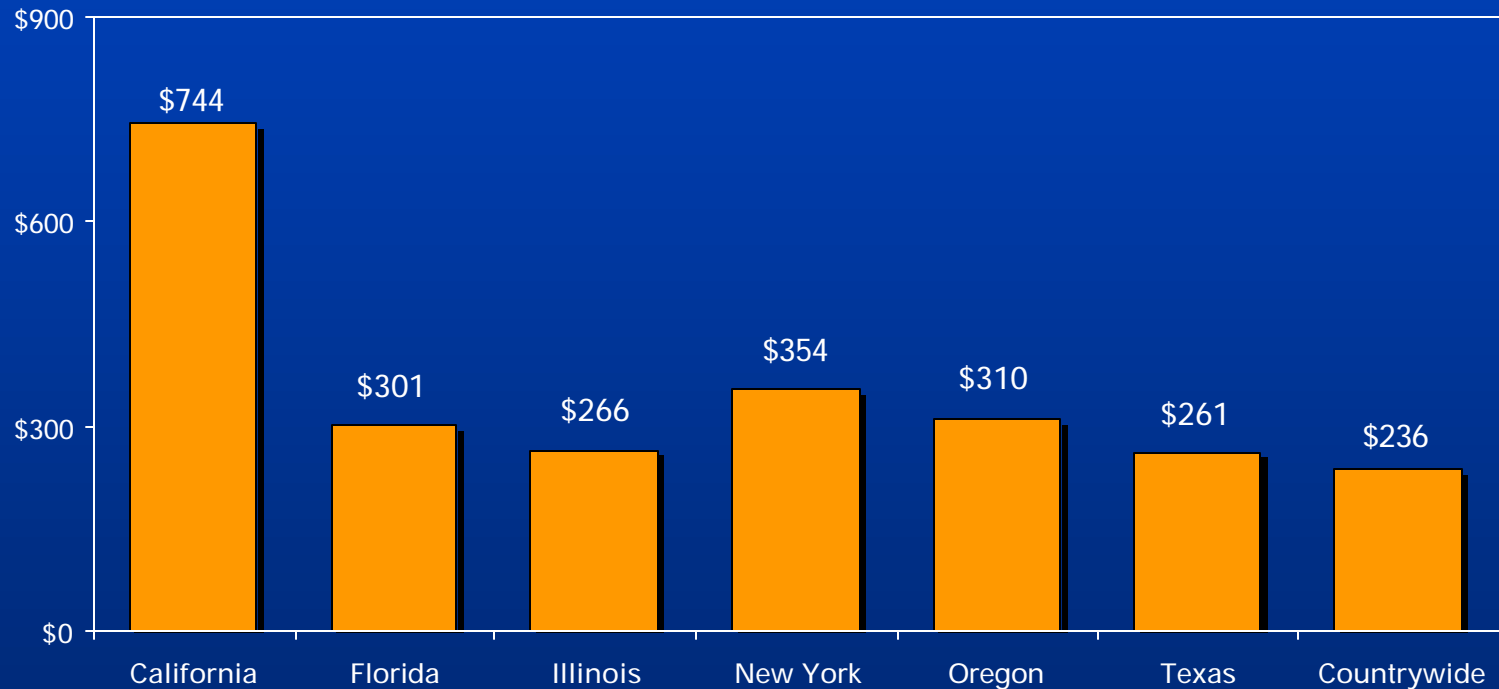
Average Insurer Rate Per \$100 of Payroll



Growth in Average WC Medical Per Claim vs. National Medical CPI



Permanent Partial Disability Claim Cost Per Worker (Based on 2003 NCCI Annual Statistical Bulletin)



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California Regulatory Update – Workers' Compensation Provisions of AB 749

- Enacted in February 2002
- 4-Year Phase-in of Benefit Increases
- TTD / PTD Increases
 - Max: \$490 to \$840 by 2005 (indexed to SAWW)
- PPD Increases
 - Max: Increases range from 20% to 65% by 2005
 - PD Award (10% rating at max): \$9,200 vs. \$4,200
- Death / Life Pension Benefits Doubled in 2006
- PTD & LP Benefits Adjusted Annually
- Primary Treating Physician Presumption Repealed
- Total WCIRB Estimated Annual Effect: +18% (+\$3.2 Billion)
by 2006

California Regulatory Update – Workers' Compensation Provisions of AB 227 & SB 228

- Enacted in September 2003
- Fee Schedule Changes
 - Physicians, inpatient, pharmaceuticals, outpatient
- Medical Utilization
 - Caps on physical therapy & chiropractic visits
 - Adoption of utilization standards (ACOEM)
 - Presumption given to decisions based on standards
 - Second opinions for spinal surgeries
- Vocational Rehabilitation Repealed
- Provides for Non-transferable Educational Vouchers
- Total WCIRB Estimated Annual Effect: -13% to -16%
(-\$4 Billion to -\$5 Billion)

California Regulatory Update – Workers' Compensation Provisions of SB 899

- Enacted in April 2004
- Major Provisions Include
 - 2-year caps on temporary disability benefit duration
 - Multiple changes to permanent disability
 - Definition of medical necessity / utilization standards
 - Medical provider networks / independent medical review
 - Employers' liability for immediate medical care
 - Medical-legal evaluation process
 - Penalties reduced
- Total WCIRB Estimated Annual Effect (Excluding January 2005 PD Schedule): -18% (-\$4 Billion)
- Impact of January 2005 PD Schedule: 38% Reduction in PD, -12% Overall Cost Reduction (-\$2 Billion)

Combined Impact of 2003-2004 Reforms

- WCIRB Combined Estimated Annual Impact of All Reforms: Approximately -40% (-\$10 Billion)
- Major Effect on Loss Development (WCIRB 3/06 Study)
- Impact on Size of Loss Distribution Being Studied
- Bickmore & Associates 2006 Study for DWC
 - Estimated annual savings: \$8 billion to \$15 billion
 - Estimated savings on pre-1/1/04 claim reserves: \$6 billion to \$11 billion

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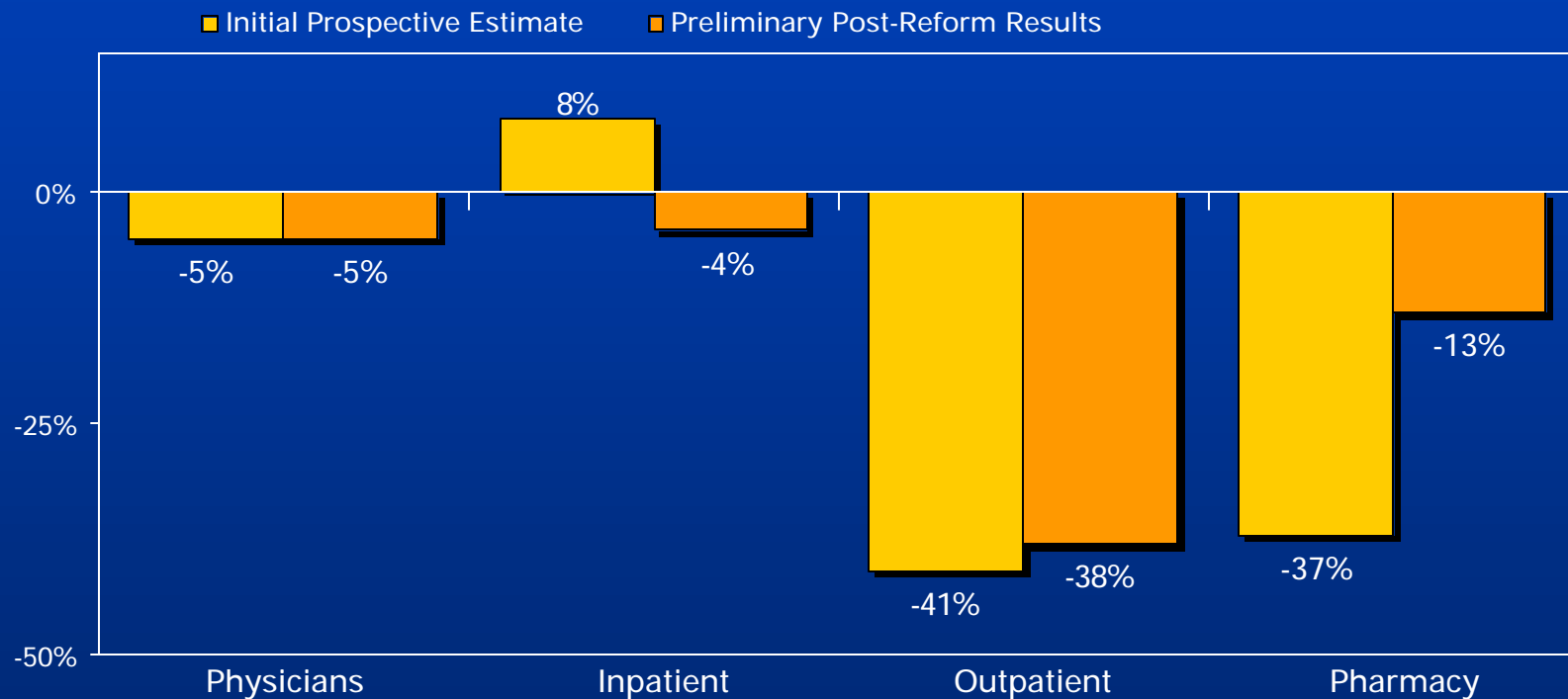
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- Summary of Reforms
- Post-Reform Experience

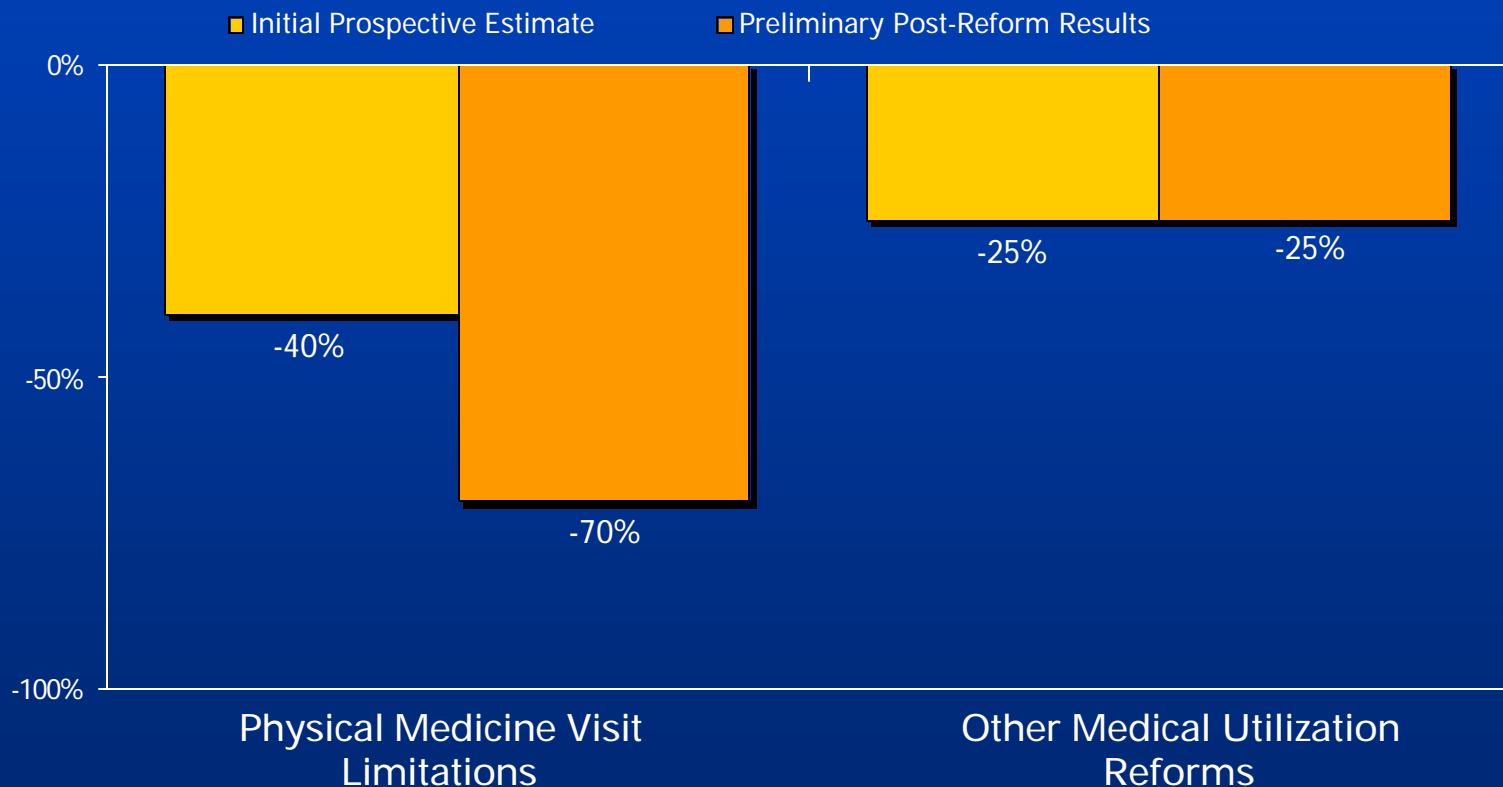
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Effect of Fee Schedule Changes

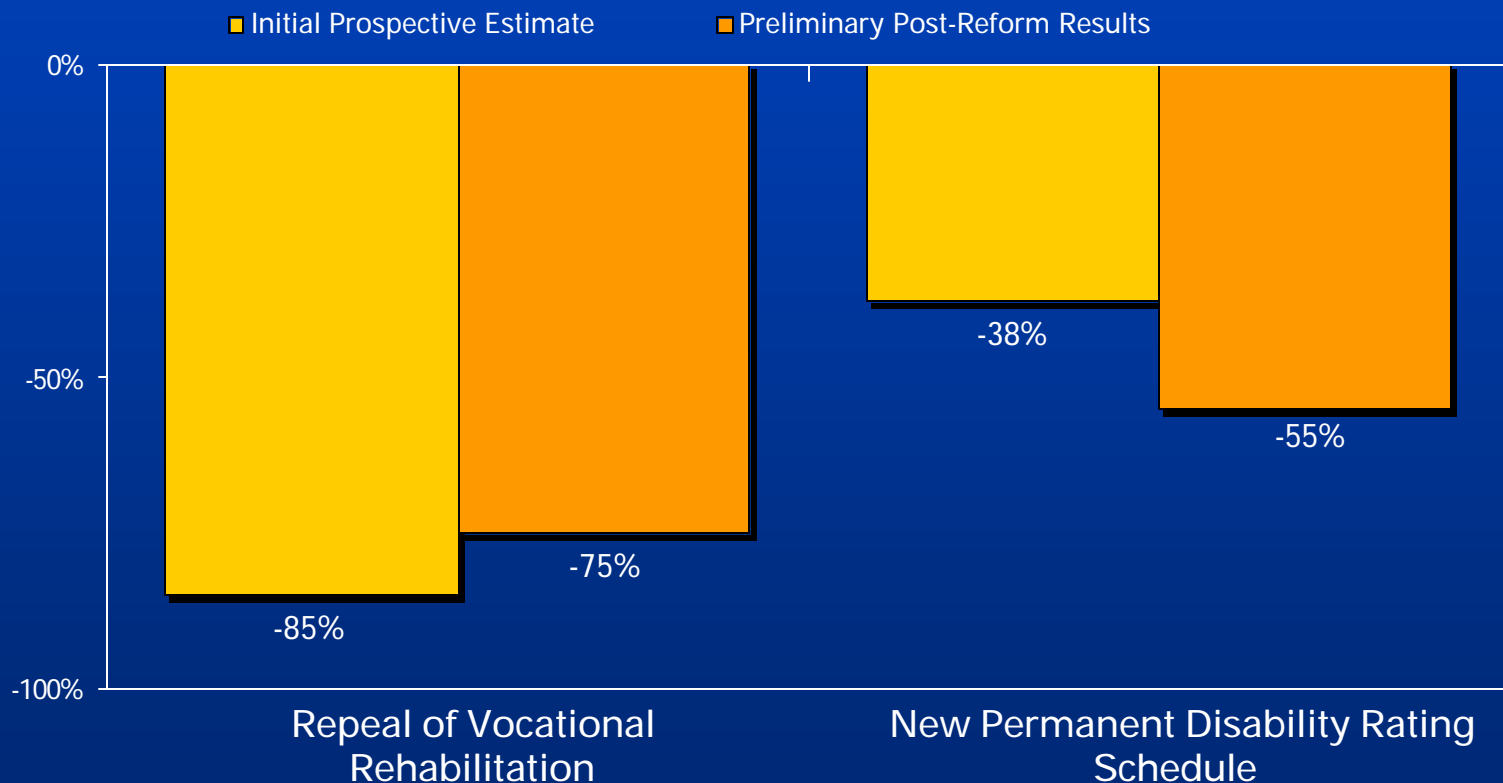
Initial Estimate vs. Prelim. Post-Reform Results



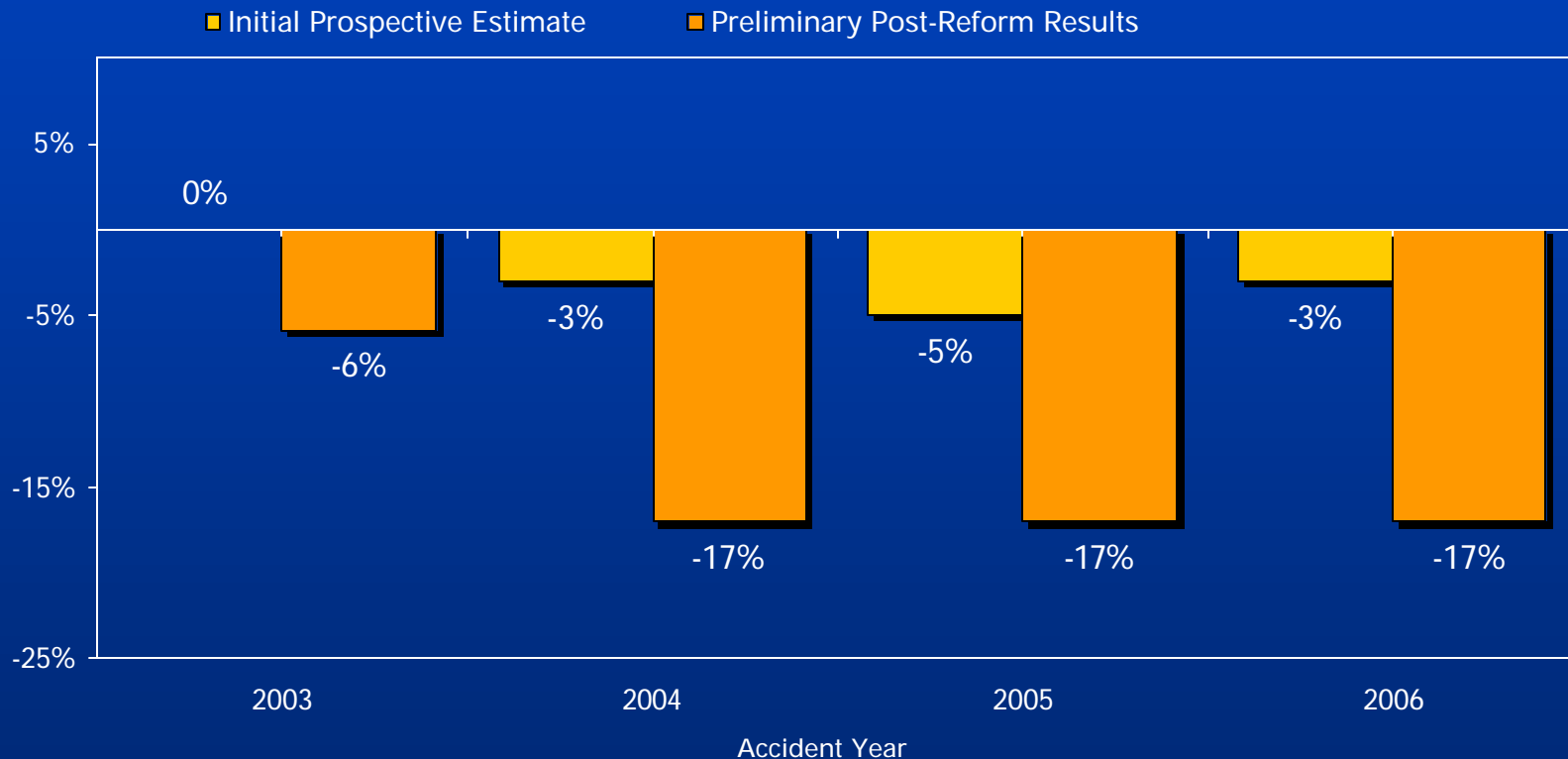
Effect of SB 228/SB 899 Indemnity Reforms Initial Estimate vs. Prelim. Post-Reform Results



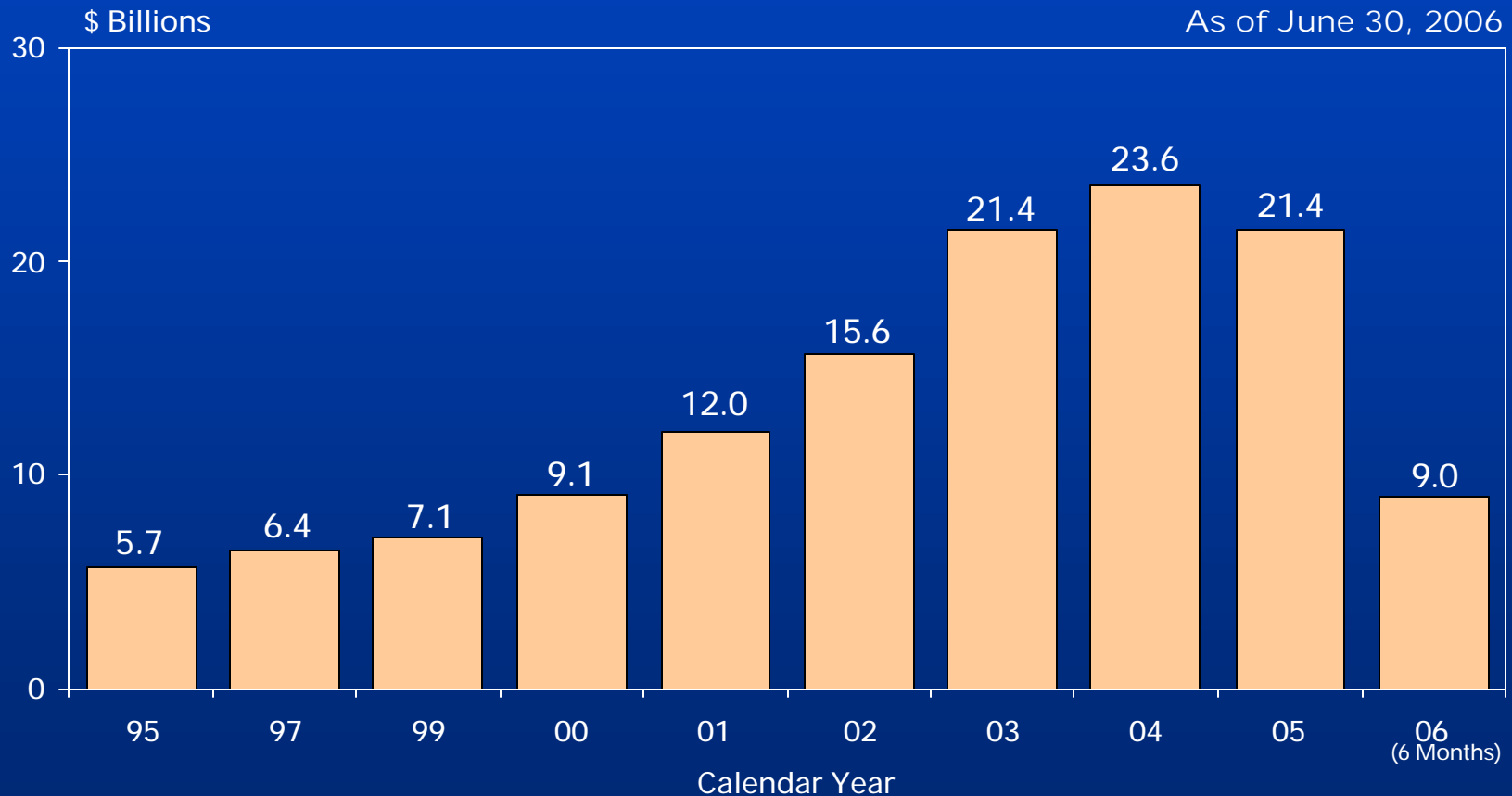
Effect of SB 228/SB 899 Indemnity Reforms Initial Estimate vs. Prelim. Post-Reform Results



California Regulatory Update – Workers' Compensation Indemnity Claim Frequency Change Initial Estimate vs. Prelim. Post-Reform Results

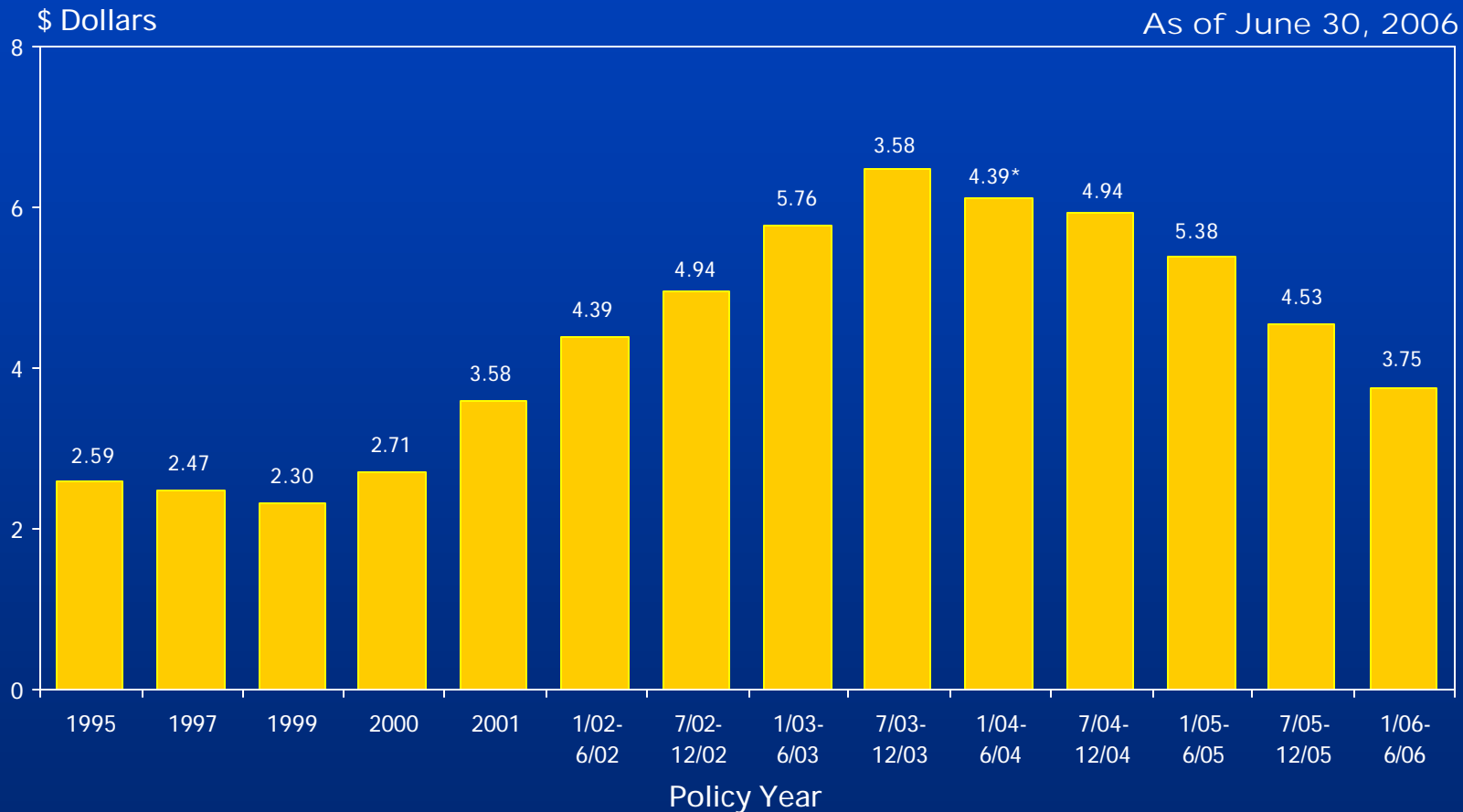


Written Premium Gross of Deductible Credits



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Average Insurer Rate per \$100 of Payroll



Ultimate Indemnity Claim Counts Per Estimated 1,000 Full-Time Employee Equivalents



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Recent Claim Frequency Declines

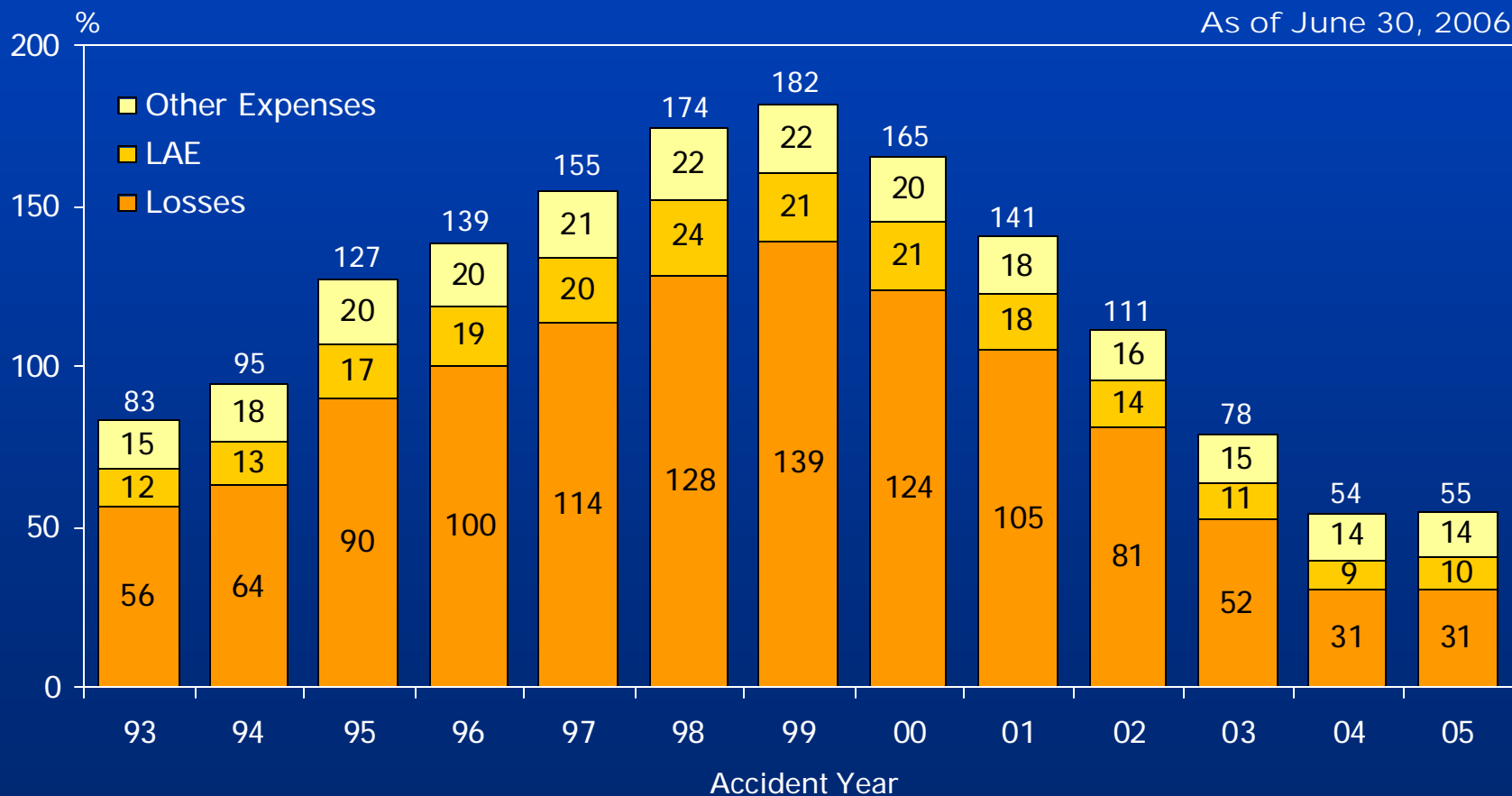
- Principal Cause of Recent Rate Decreases
- Key Considerations
 - Little in recent reform directly impact frequency
 - Decline much greater than in other states
 - Impact on severities not yet fully understood
- WCIRB 2005 & 2006 Studies
 - Broad-based frequency decline
 - Not explained by economic or demographic variables
 - Timing of decline, substantiating evidence, elimination of alternative hypotheses all suggest frequency decline is an indirect impact of reforms

California Regulatory Update – Workers' Compensation Estimated Ultimate Total Loss per Indemnity Claim

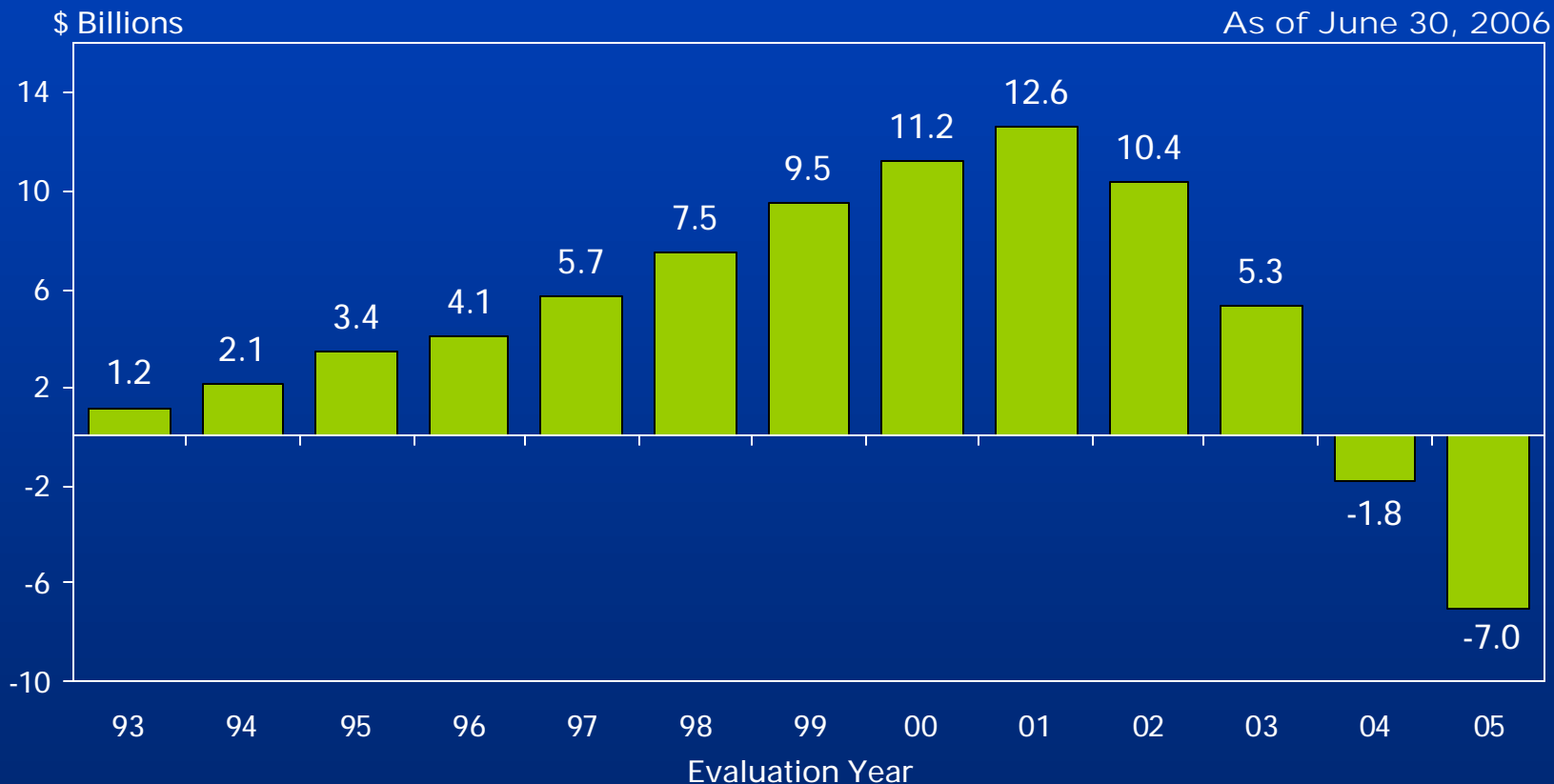


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Accident Year Combined Loss and Expense Ratios



Estimated Ultimate Losses Less Reported Losses at Successive December 31 Evaluations



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Future Outlook

■ Pricing & Premiums

- Rates already down 42% through June 30
- Further 16.4% (7/1/06) & 9.5% (1/1/07) pure premium rate decreases
- Anecdotal evidence of further market pricing declines
- 2006 rate level almost 30% below 2005
- 2007 premiums likely to continue to decline

■ Claim Costs

- Frequency – significant declines in 2003 to 2006
- Severity – 2005 estimate up over 2004
- Post-reform data supporting reform savings

California Regulatory Update – Workers' Compensation Future Outlook (Continued)

■ Insurance Market

- 2004 to 2006 very favorable results
- Follows long period of record losses
- Better results attracting more entrants
- State Fund market share moving toward its historical norm
- Will cutthroat pricing of 1990s return?

■ Legislation/Regulation

- Potential reform rollback
- Legal challenges to law and regulations
- Rate regulation concerns lessening
- Key regulations subject to change