The Liverside *e*-Letter

An *Executive Briefing* on Emerging Workplace Safety and Insurance Issues

June 23, 2005 An *Electronic Letter* for the Clients of L.A. Liversidge, LL.B. 4 pages

2006 Premium Rates:

There is a *Responsible* Alternative to Premium Rate Hikes

WSIB Administration poised to recommend higher employer premiums for 2006 and beyond

There is a "better way"

As described by one senior employer lobby group, the "***Recent history pertaining to Workplace Safety & Insurance Board premium rates is akin to an amusement park roller-coaster ride. Following a period of stability, of late we have been witness to wild dips and turns in WSIB funding plans that would be dizzying to any observer***".

Employer groups have been consulting with senior WSIB officials

Employer groups have recently been participating in a senior dialogue with WSIB officials on the Board's long-term funding strategy. This, of course, includes a key discussion on the level of the 2006 premium rates. Employers have long requested this dialogue (since at least the Fall of 2002), however, some employer groups have complained that even before the commencement of this essential exchange, the Board may have tipped its hand by declaring in a widely distributed senior letter last October that **it is the Board's "*strong belief that a rate increase will be required in 2006*"**. Some employer groups have worried that the real issue, in the eyes of the Board, is the *magnitude* of the rate hike. Throughout the extensive discussions during this past Winter and Spring, Board officials have not really wavered from this position.

There are responsible alternatives to a premium rate hike

The Board argues that cost pressures require a hike in premiums, perhaps as much as 3% per year over the next five (5) years, to keep pace and still retire the unfunded liability ["UFL"] (shortfall between the price of future liabilities and the value of the Board's accident fund) by 2014. Readers will recall that the retirement of the UFL by 2014 is a long-standing cornerstone of the Board's funding strategy, first developed in 1984. The Board remains firm that the objective of retiring the UFL by the year 2014 is unshakable, if it can be done "responsibly". In one scenario, the Board proposes that the average premium will increase from the current $2.19 up to $2.59 by 2010, a total hike of 18.3%, before it starts to decline.

Employers generally don't buy it, and counter that premium hikes should be a last resort (***Continued page 2***).

Client Executive Briefing

***An interactive executive briefing on leading workplace safety and insurance issues is scheduled for*:**

June 29, 2005

9:30 A.M. to 12:30 P.M.

As a follow-up to our June 7th executive briefing, L.A. Liversidge will provide an "*up-to-the-minute*" update on current developments flowing from the WSIB's recent consultation exercise, with a focus on 2006 premiums.

***The objective*: Advance the argument for a *responsible alternative* to rate hikes.**

Update and policy advocacy:

Following up on our in-depth policy forum of **June 7, 2005** which provided clients with an executive briefing of the Board's consultation outreach exercise, the June 29th meeting will be an ***interactive* policy advocacy** session. Clients will receive an "up-to-the-minute" update along with viable suggestions to *get the message out*.

Invitations will be e-mailed

This meeting will provide you with an opportunity to present comment, opinion, and feedback on the leading issues to the Board and Government.

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(*Continued from page 1*) Employers argue that there are responsible alternatives to *any* increase in premium rates, and demand that the Board seriously consider those alternatives before exploring any rate hike, even if that means moving off the 2014 target by a few years. In this issue of **The Liversidge *e*-Letter** I will address the issue of premium rate hikes and the long-term funding of the Ontario workplace safety and insurance ["WSI"] system.

A brief and relevant history

From 1995 to 2001, average employer premiums dropped

From 1995 to 2001, the average employer premium dropped 29%. During that same period, the UFL was cut almost in half.[1] In its 2001 Annual Report (released mid-2002), the WSIB noted that despite 9/11 affecting the Board's investment income, the Board made "*substantial progress towards its goals*" which included "*financial security*".[2]

By the Fall, 2002, the WSIB appealed for premium rate hikes

Yet, in the Fall of 2002, the then WSIB Acting Chair announced a need for a 7^{+}% average premium rate hike for 2003, and "settled" for a 3% rate hike, but not without warning that future rate hikes were imminent.[3]

One main reason for rate hikes in the Fall, 2002 – Collapse of world-wide equity markets following 9/11 (they have come back)

One of the principal reasons provided for the rate hike request was the downturn of the equity markets following 9/11, which of course, have since recovered. Interestingly, even amidst the investment uncertainty in the Fall of 2002, the Board was convinced that a "*new funding plan over two years*"[4] requiring a 3% hike for 2003 and another for 2004 "*will help make sure we remain on track for our goal of eliminating the unfunded liability by 2014*".[5]

Yet, even then the WSIB was convinced that a 6% hike – spread over two years – was enough

This suggests that the Board, at its most senior levels, in the Fall of 2002 when the investment future was most uncertain, was convinced that a modest premium hike spread over two (2) years would be sufficient to still adequately fund the system and "retire" the UFL by 2014.

The Fall, 2002 employer response – short-term investment losses should not drive long-term funding strategy

In response to the "investment loss argument", a senior and leading employer trade association coalition, the Employers' Council of Ontario ["ECO"] noted that the long-term funding strategy, first struck in 1984, had "*survived the often rough seas of economic uncertainty, intact*".[6]

The ECO suggested that "short term" economic uncertainty should not drive long-term policy.[7] As it turned out, this was sage advice – the equity markets have returned to Fall, 2000 levels. This is a policy position still adhered to by most employer groups.

In Summer of 2003, WSIB executive held rates level – the UFL was still to be zero at 2014

In the Summer of 2003, notwithstanding the continuation of similar financial pressures, following an extensive consultation with employer stakeholders in July, the WSIB executive, including the Board's current Chief Actuary, recommended to the WSIB Board of Directors that the average 2004 premium level not be increased.[8] Notwithstanding that the premium rate was to remain at $2.19, the UFL was still expected to be zero by the year 2014 (though expected to rise slightly in the short-term).[9]

Employers supported this move and suggested that WSIB focus on "cost drivers"

Employers were of the view this was a prudent and responsible plan, and strongly suggested that WSIB attention must be channelled towards containing administrative costs[10] and examining the increase in health care costs, noting that central to the 1999 "*Health Care Model*" ["HCM"] was a commitment to measure "quality and success" of health care expenditures.[11]

Yet, WSIB has progressed little to understand drivers behind cost increases

Many employer representatives were shocked to discover during the WSIB "*Health Care Session*" of March 2, 2005, that not only were WSIB officials no further along in their understanding of the effectiveness of the HCM than they were when it was introduced in 1999, Board officials are now "only close" to even *begin* to analyze health care costs.

Effectiveness of labour market re-entry has not been evaluated

On a related theme, the Board also advised that they have not measured the effectiveness of the outsourcing of labour market re-entry ["LMR"], even though LMR has been a legislative, policy and operational fixture since 1998. Surprisingly, the Board does not know if LMR has been as effective, more effective, or less effective than the regime it replaced, notwithstanding that hundreds of millions of dollars are channelled through LMR each year.

Effectiveness of Nurse Case Managers not known

Similarly, Nurse Case Managers ["NCM"], in place since 1997 and once heralded as a critical component to monitoring

[1] WSIB Annual Report 2000, page 4.
[2] WSIB 2001 Annual Report, page 2. The Board reported that the unfunded liability was down to $5.657 billion, from its peak of $11.532 billion in 1993.
[3] November 19, 2002 letter from Acting Chair Hikel,.
[4] *Ibid.*
[5] *Ibid.*
[6] November 8, 2002 ECO letter to WSIB Acting Chair Hikel, at page 4.
[7] *Ibid.*
[8] August 26, 2003 letter from WSIB Chair.
[9] See July 8, 2003 WSIB Presentation, "*Funding Strategy, Employer Consultations*", Slide 56, "Premium Rates Projection, Scenario 4 – No Increase ($2.19)".
[10] Since that time, an audit on the WSIB ordered by the Minister was completed.
[11] March 1999 WSIB Health Care Model, "Measurement of Quality and Success", at page 4.

health care and ensuring early and safe return to work,[12] are a complete unknown in the effectiveness equation. Board officials admitted they have no idea whether or not these positions have been effectual. There has been no effort to measure whether NCMs have reduced recovery, have prolonged recovery, or have had no effect on recovery and return to work.

WSIB advises it is becoming more accountable

Yet, session after session, while the Board was building its case for higher premiums, participants were told the Board is, just now, getting on top of these programs, and WSIB management will be more accountable. Many have suggested that ***accountability, aptly demonstrated, must precede any request for higher premiums***.

WSIB 2003 commitment to hold rates level quickly evaporates

Notwithstanding the decisions taken following the July 2003 consultations, the commitment to hold rates level quickly evaporated. Last August, the Board again rolled out an argument for higher premium rates. The Board clearly was back-peddling on the July 2003 decision, now suggesting that the July 2003 decision was nothing more than a "premium hike deferral", even though by this time, the Board's investment fortunes were improving.

The July, 2003 decision not to increase rates *was not* a rate hike deferral

To employer representatives participating in the process, the July 2003 decision was not a premium hike deferral – it was a responsible and prudent decision with a long-term focus. This point was again pressed on the Board, and with the commitment to participate in a series of significant discussions to address leading funding and expenditure issues (held February – May, 2005), the Board did not increase the average 2005 premium rate.

WSIB holds series of employer consultation meetings February to May, 2005

While the Board agreed to hold meetings, and was very open with its information, many employer participants were disappointed that prior to the commencement of these discussions, the Board's CEO announced that it is the Board's "*strong belief that a rate increase will be required in 2006*",[13] leading some to worry that the Board had pre-determined the result.

The Board's case for a premium increase

Given its preferences, it is clear that the Board is set on increasing premium levels - the only issue is the magnitude of the rate hike. Throughout the extensive discussions during this past Winter and Spring, Board officials have not wavered from this position.

[12] WSIB 1997 Annual Report, at page 14: Nurse Case Managers were brought into the Board's disability management model to facilitate early, effective treatment to result in a safe, early return to work.

[13] October 15, 2004 widely distributed letter from WSIB CEO.

WSIB advises cost pressures force a premium hike

The Board continues to press the case that cost and economic pressures require a rate hike if the UFL is to be retired, on plan, by 2014. Most employers take no quarrel with the Board's analysis, taking the advocacy position that little is gained through quibbling over the Board's financial projections.

Board convinced it must increase premiums as much as 3% per year over the next 5 years

Essentially, the Board is proposing a renewed funding strategy, which at its core, will call for successive premium rate hikes, likely as much as 3% per year for five (5) years. The average premium is expected to peak at $2.59 in 2010 ($18^{+}$% increase over 2005 premiums), and the UFL is retired, as planned, by 2014.[14]

Accident rates have declined by 60% since late 1980s

The Board's plan will likely extract over $2.0 billion from the Ontario economy over the next seven (7) years,[15] even though from the late 1980s to the early 2000s, the LTI rate *declined by over 60%*,[16] and is projected to drop another 20% over the next few years.

There is an alternative to higher premiums

Employer groups unanimously call for no rate hikes

In a WSIB "wrap up meeting" held June 23rd, to a participant, while thanking Board officials for their time and openness, that Board was advised that there is a responsible alternative to increasing premium rates. *In fact, this advice was based on the Board's own analysis*.

The viewpoint was unanimous – the WSIB must not increase premiums for 2006 (and beyond), and instead, simply extend the amortization of the UFL out a couple of years, and focus energies on understanding and dealing with cost drivers.

"*The system is not in crisis – it is very manageable*" [WSIB Chief Actuary, WSIB Funding Session, March 24, 2005].

Noting that the Board's Chief Actuary unequivocally declared that the "*system is not in crisis*" and is "*very manageable*", employers pressed upon Board officials that there is a responsible alternative to increasing premium rates. During the 2005 consultations, at the outset, employers had requested that the Board analyze the system implications if there are no rate hikes, and the average premium is held at $2.19.

If rates remain stable, the "sky does not fall" – the UFL is still reduced to zero – it will just take 2 to 4 more years

If rates remain at current levels, just as was discovered in July 2003, not only does the system not implode, but after rising slightly in 2006, the UFL begins a downward slope and

[14] See March 24, 2005 WSIB Presentation, *Funding Framework Working Session #2*, Slide 35, "Mitigation Scenario – Smoothed Rates, Premium Rates and UFL".

[15] Presuming that every $0.01 in the average premium rate equates to approximately $14 million in collected premiums.

[16] March 30, 2005 WSIB Presentation, *Prevention in Ontario*, Slide No. 76.

declines to zero just a few years after the planned target of 2014.[17]

The bottom line – a "zero percent increase" responsibly respects the essence of the long-term funding strategy, without resorting needlessly to premium rate hikes.

The core of the long-term funding strategy – reducing premiums *along with* reducing the UFL

Ontario business is a "founding partner" to the Board's funding strategy

In its 1983 Annual Report, the Board noted that:

> **In 1983 . . . it was hoped that, together, the Board and employers could determine the most appropriate methods of reducing the unfunded liability without, in any way, hampering the ability of Ontario's employers to carry on business. *After all, the ultimate health of the workers' compensation system depends on the continued strength of the province's economy.***

Employers substantially increased premiums in the 1980s and 1990s with the expectation that premiums would fall along with accident rates

More than two decades later, these comments remain fitting. As part of the 1984 strategy, Ontario business accepted substantial premium rate hikes of 15% per year for three years followed by 10% each year for another three years. A large portion of employer premiums was dedicated to increase reserves to eliminate the UFL in a planned, responsible *and gradual manner*.

From the late 1980s, the Board reported, through its Annual Reports, that the strategy was on track. In 1987, the unfunded liability was expected to peak in 1988-89 and decline gradually to zero by 2014. In 1990, the Board reported that the strategy remained on track, despite the current year's decline in revenues. In 1997, the Board reported that despite the severe recession in the early 1990s, the outlook was positive to retire the unfunded by 2014. In 1998 a new Funding Strategy was adopted to allocate a larger portion of the employer premium to pay down the unfunded liability, while premiums were themselves declining.

The tail should not be wagging the dog

In short, declining premiums was just as significant a building block to WSIB funding as was retiring the UFL by 2014. While it is clear that employers would prefer to see the system fully funded by 2014, it would be imprudent and inconsistent with the principles of the long-term funding strategy to achieve that objective at any cost. 2014 was selected as a reasonable terminal date more than twenty years ago. It was not an unreasonable target – but it was simply that – a target. *The tail should not be wagging the dog* – the 2014 date should not determine funding policy – funding policy should determine the termination date.

[17] See March 24, 2005 WSIB Presentation, *Funding Framework Working Session* #2, Slide 14, "Requested Scenario 3.

The Board is correct to focus on contemporary challenges. The Board has convincingly set the stage to address the several risks facing the Board, and by consequence, workers and employers. In the past, premiums were increased when there were no other viable options. Today, even the Board's Chief Actuary admits "*the system is not in crisis*". Employers have reminded the Board as late as June 23rd that there are alternatives. Keep rates as they are, while channelling resources to resolve the drivers behind the call for rate hikes.

In reality, the WSIB has already put in place a *de facto* 3% premium rate hike through experience rating changes – with more yet to come

All the while the Board is pressing its case for rate hikes, in reality, the WSIB has already put in place a "back door" premium hike through "administrative changes" to the Board's NEER experience rating plan ["ER"] **[see the May 16 and June 2 issues of The Liversidge *e*-Letter]**. It is noteworthy that most employers are not familiar with these changes, since the first "transaction" for Accident Year 2004 will not take place until December 2005.

These "administrative changes" adjusted several elements of the ER formulae which has had the effect of reducing rebates while increasing surcharges. Even though employers are under the impression premiums did not increase for 2004, in actuality, net-premiums will rise by at least 3%.[18]

For some sectors, the impact will be more dramatic. Automotive assembly will see a 20% increase, automotive parts a 5.1% increase, hospitals a 6.3% increase, food sales, a 6.6% increase, to illustrate just a few examples.

Many employers, while acknowledging their discord with the Board's recent approaches to ER reform, have suggested that layering additional premium hikes on top of an already implemented *de facto* rate hike is unconscionable.

The bottom line

In the past, when premium rate hikes were required, Ontario's employers stepped up to the plate and significantly increased contributions. Increases in premium levels must be a last resort.

Maintaining premium rates at present levels is not only prudent, it remains consistent with the tenets of the long-term funding principles first developed over twenty years ago. The UFL is still reduced to zero. It will simply take a few extra years. Employers suggest that this is not at all an unreasonable state of affairs in light of the claimed effect of 9/11 on the Board's investment fortunes, and the significant room for improvement in the Board's administrative capacity.

[18] Since the 2004 Accident Year will not receive its first ER transaction until December, 2005 (with data as at September 30, 2005), one must use Accident Year 2001 as a representative year (since 2001 is the most recent year that is "closed"). In 2001, on premiums of $1.438 billion, the net rebate was close to $60 million (surcharges - $83.8 million; rebates - $143.4). The 2004 changes, *already implemented*, if applied to Accident Year 2001, would *increase surcharges* to $118.8 million (+42%), and *decrease rebates* to $133.5 (-7%). The net result is a reduction in the net rebate to $14.8 million, a reduction of $44.8 million. ***This has the effect of increasing the net premium by 3.1%***. This means that, in effect, there was no freeze in the average premium for 2004.