Actuarial Committee

Meeting Minutes

Date	Time	Location	Staff Contact
June 14, 2019	9:30 AM	WCIRB California 1221 Broadway, Suite 900 Oakland, CA	David M. Bellusci

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Members	**Representing**
Jim Gebhard	Farmers Insurance Group of Companies
Joanne Ottone	Berkshire Hathaway Homestate Companies
Jill Petker	Liberty Mutual Group
Mark Priven	Public Members of Governing Committee
Kate Smith	State Compensation Insurance Fund
Bryan Ware	AmTrust
Chris Westermeyer	Travelers
Doug Zearfoss	Employers Insurance Group

California Department of Insurance
Mitra Sanandajifar*

WCIRB
Bill Mudge
David Bellusci
Tony Milano
Shane Steele
Julia Zhang

* Participated via teleconference

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The meeting of the Actuarial Committee was called to order at 9:30 AM following a reminder of applicable antitrust restrictions, with Mr. David Bellusci, Executive Vice President and Chief Actuary, presiding.

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Approval of Minutes
The Minutes of the meetings held on March 18, 2019 and April 2, 2019, were distributed to the Committee members in advance of the meeting for review. As there were no corrections to the Minutes, a motion was made, seconded and unanimously approved to adopt the Minutes as written.

Notice

The information in these Minutes was developed by the Workers' Compensation Insurance Rating Bureau of California (WCIRB) for the purpose of assisting the WCIRB Actuarial Committee. The WCIRB cannot make any guarantees if this information is used for any other purpose and the WCIRB shall not be liable for any damages, of any kind, whether direct, indirect, incidental, punitive or consequential, arising from the use of or reliance upon this information for any other purpose.

Item II
Working Group Meeting Summaries

The summaries of the Claims Working Group meeting held on March 28, 2019 and Actuarial Research Working Group meeting held April 22, 2019 were included in the Agenda for the Committee's review. Staff presented a summary of the enhancements to the retrospective rating plan claim simulation based on paid loss development that were discussed at the April 22, 2019 Actuarial Research Working Group meeting. It was noted that staff plans to implement this enhancement in future retrospective rating plan claim simulations. After discussion, the meeting summaries were accepted by the Committee.

Item AC16-06-05
Update on Medical Severity Trends by Component

Staff presented an updated analysis on medical severity trends by medical component using medical transaction information through December 31, 2018 (service year (SY) 2018). The updated analysis included changes in the share of total medical payments by different fee schedules, changes in paid per transaction, paid transactions per claim, and cost per claim by service type, as well as cumulative percentage changes in selected components of physician services.

The Committee was advised that the share of total medical payments for pharmaceuticals decreased by about 74%, from 16% in SY2012 to 4% in SY2018, while with the dramatic reduction of pharmaceutical cost, the share of all other service categories increased by 2-3%. Staff noted that the sharp decline in the pharmaceutical payment share was driven by a number of intersecting factors, including (1) legislative and policy changes intended to monitor and regulate prescription drug utilization such as independent medical review and the drug formulary, (2) reduced overall prescribing and opioid prescribing in particular, (3) public awareness of the adverse effects of opioids, (4) reduced fee schedules for generic drugs (also known as the “Average Federal Upper Limit”) implemented in 2016, and (5) indictments of providers for fraud.

Staff noted that, the total medical payments per claim started to stabilize after 2015, yet because of the continuous reduction in utilization of medical services in the earlier years, on a cumulative basis the paid per claim declined by 23% between SY2012 and SY2018. The cumulative reduction was largely attributable to the impact of Senate Bill No. 863, subsequent legislation, the overall decline in pharmaceutical costs and anti-fraud efforts.

The Committee was advised of the following trends and patterns of medical services utilization and costs by different fee schedule:

- <u>Physician Services:</u>
  - Staff noted that physical therapy, the leading category of physician services, experienced an increase in paid per transaction in 2018. However, staff observed no change in its utilization per claim, which differs with the 9% increase shown in the analysis results using only 1st half of SY2018 data. A member suggested that staff further explore if changes in the speed of the payments to physical therapy contributed to the changes in the utilization pattern.
- <u>Pharmaceuticals:</u>
  - Staff presented additional breakdowns for pharmaceuticals on opioids and non-opioids costs. The Committee was advised that pharmaceutical paid per claim decreased by 80% from 2012 to 2018, and the decline in opioid paid per claim was even more pronounced (89%). Staff noted that the impact of the sharp decline in pharmaceutical costs on loss development patterns is currently being studied (See Agenda Item AC19-06-03.)
- <u>Inpatient:</u>
  - Staff summarized the percentage changes in inpatient costs at both the transaction and episode levels. Staff noted a continued reduction in transactions per claim from SY2015 to SY2018, while the paid per transaction increased. This was likely in part attributable to a shift of minor inpatient procedures to outpatient settings, leaving more intensive (and more expensive) care to dominate the remaining inpatient procedures.
  - When summarizing the inpatient costs based on episodes, staff noted that for the first time the paid per episode decreased by 17% while the number of episodes per claim increased in SY2018. A Committee member suggested seeking input from the Claims Working Group on the potential reasons for the unexpected patterns, and staff agreed to present and discuss this issue at the July Claims Working Group meeting.

Lastly, staff summarized the cumulative share changes in the leading physician service categories from the second half of SY2012 and noted a significant increase in the paid per transaction for Evaluation & Management, Physical Therapy and Other Medicine, and a large reduction in the paid per transaction for major Surgery, Radiology and Anesthesia services. The Committee was reminded that these changes were expected with the completion of the four-year transition to RBRVS in 2017.

Item AC17-12-04
Earthquake Study

Staff advised that, at the December 6, 2017 and December 5, 2018 meetings, the Committee reviewed studies of earthquake and terrorism exposure in California completed by Risk Management Solutions (RMS) on behalf of the WCIRB. In the studies, RMS projected that the long-term average earthquake loss per year was $29 million, with an average loss rate per $100 of payroll of $0.005 and the long-term average net-insured retained terrorism loss per year was $21 million, with an average loss rate per $100 of payroll of $0.0039.

The Committee was also reminded that the WCIRB had included a provision for earthquake exposure in proposed January 1, 2004 pure premium rates and that the California Department of Insurance (CDI) had rejected that provision due to concerns over (a) the magnitude of the model estimates due to the limited volume of historical earthquake workers' compensation losses in California and (b) the lack of a long-term funding mechanism for earthquake losses. However, it was noted that since 2004 refinements to the earthquake models have significantly moderated the loss estimates, the WCIRB has developed a refined model of statewide insured exposures by location and that most jurisdictions include some catastrophe load in loss costs.

Staff advised the Committee that in other states these catastrophe loadings are generally not part of the manual rate but are separate loadings generally not subject to experience rating and most other rating plan adjustments. Based on review of insurer rate filings with the CDI as well as feedback from several insurer representatives, staff advised that some insurers file a similar structure for application of such charges in California. Staff noted that by statute the WCIRB proposes advisory pure premium rates to the Insurance Commissioner but not other risk rating plans beyond experience rating and including a loading for average earthquake and terrorism exposure in advisory pure premium rates could create administrative issues for insurers who do not include such charges in their manual rates.

Given the CDI's concerns in prior decisions and that including a long-term average provision for earthquake and terrorism exposure in advisory pure premium rates may create administrative issues for some insurers, the consensus of the Committee was that the WCIRB's proposed advisory pure premium rates should not reflect a provision for earthquake and terrorism losses at this time. However, several Committee members suggested that published information on the potential statewide exposure of these events is of value and should be updated on a regular basis.

Item AC18-06-03
Classification Payroll Limitations

The Committee was reminded that in the Decision on the January 1, 2019 Regulatory Filing, the Insurance Commissioner approved annual payroll limitations to be applied to employees in five additional classifications, effective January 1, 2020. The Agenda included staff's proposed methodology to develop appropriate advisory pure premium rate adjustments for January 1, 2020 advisory pure premium rates for these classifications to reflect the new payroll limitation in the data used for classification ratemaking. Staff summarized the approach for the Committee and noted that the approach and resulting adjustments were also reviewed and adopted by the Classification and Rating Committee at the May 30, 2019 meeting.

During the discussion, a Committee member noted that the level of the executive officers' maximum annual payroll (to which the payroll limitation for these five classifications is set) while inflation adjusted each year has not been reviewed for some time. The member also noted that wage inflation for employees at the annual payroll limitation may differ from statewide averages and suggested these issues be reviewed in the future.

After discussion, the consensus of the Committee was that staff's recommend approach for adjusting these classifications' advisory pure premium rates was appropriate and should be reflected in the classification relativities to be included in the January 1, 2020 Regulatory Filing.

Item AC19-06-01
3/31/2019 Experience – Review of Methodologies

Staff presented a summary of the preliminary analysis of statewide accident year experience evaluated as of March 31, 2019 that was included in the Agenda. It was noted that the decrease in the projected loss ratio since the analysis of December 31, 2018 experience reviewed at the April 2, 2019 meeting was primarily attributable to an extended trending period in that the projected overall loss trend was somewhat lower than the projected wage trend, while changes in the loss development projection were modest.

Staff noted that the recent decreases in both paid and incurred indemnity and medical development moderated in the first quarter of 2019. It was noted that the modest decreases in the projected loss ratios based on March 31, 2019 experience compared to those based on December 31, 2018 experience were approximately one-quarter of the decrease from the similar period a year ago. It was also noted that claim settlement rates continued to increase while indemnity claim count development has moderated.

The Committee discussed the projected frequency and severity trends. It was noted that the estimated accident year 2018 on-level indemnity severity increase moderated somewhat from that reviewed at the April 2, 2019 meeting based on December 31, 2018 experience, but remains a significant change from the last several years of on-level indemnity severity decreases. The Committee recommended staff perform a follow-up analysis to the estimated impact of the Senate Bill No. 863 reforms to overall indemnity severities for the next meeting.

The Committee reviewed the projected medical claim severity trends and noted that the estimated on-level medical severity change for accident year 2018 based on March 31, 2019 experience is only modestly lower than that projected from December 31, 2018 experience. It was also noted that incremental paid medical per open indemnity claim severities over the last 12 months showed increases across maturities compared to earlier periods which showed mostly declines. The Committee was reminded that diagnostic information on medical severities will be reviewed at the next meeting as part of the Committee’s semi-annual review of system diagnostics.

Item AC19-06-02
1/1/2020 Regulatory Filing – Experience Rating Plan Values

Staff presented a draft analysis of the indicated policy year 2020 experience rating off-balance correction factor. The Committee was advised that the preliminary indicated off-balance factor using the same methodology as in the January 1, 2019 Regulatory Filing was 1.019. The consensus of the Committee was that this methodology was appropriate and should be used to compute the final 2019 off-balance factor.[1]

Staff also presented a draft analysis of the factors used to generate the proposed policy year 2020 expected loss rates, which used the same methodology as in the January 1, 2019 Regulatory Filing. (As with the 2019 expected loss rates, the indicated 2020 expected loss rates reflect the impact of the $250 loss exclusion that was adopted to be used in 2019 and later experience modification computations.) Staff noted that the preliminary expected loss rate changes in several industry sectors appeared volatile. The Committee was advised that, as during similar periods of volatility, staff will be reviewing the analysis to assess if there are any data anomalies and may moderate preliminarily indicated industrial sector development or trend factors in the final analysis to the extent appropriate. Staff also noted that since the payroll amounts used in the experience rating period for 2020 experience modifications will not be impacted by the new payroll limitations adopted for 2020 policies in five classifications, no adjustment to 2020 expected loss rates for these classifications is needed.

After discussion, the consensus of the Committee was that the proposed 2020 expected loss rates should reflect the methodologies summarized at the meeting. During the discussion, several Committee members noted that a significant number of classifications are impacted by the 15% swing limit in expected loss rates, which differs from the 25% swing limit in classification relativities, and suggested this issue be reviewed in the future.

[1] After the meeting, staff updated the preliminary values used to produce the indicated off-balance factor. The indicated off-balance factor after the update and using the same methodologies as the January 1, 2019 Regulatory Filing and the Committee's recommendation was 1.014, which is 0.3% lower than the 2019 off-balance factor.

Item AC19-06-03
Impact of Pharmaceutical Cost Reductions on Loss Development

The Committee was reminded that at prior meetings the Committee noted that since the pharmaceutical share of medical payments varies significantly by maturity level, the sharp reductions in pharmaceutical costs since 2012 could significantly affect medical loss development projections. Staff summarized its analysis of the impact of the recent reduction in pharmaceutical costs on medical loss development which was included in the Agenda.

Staff noted that the recent pharmaceutical cost decreases have been significant and disproportionally impact paid medical development at later maturities. It was also noted that, if these shifts are not adjusted for in the medical loss development projection, age-to-age loss development factors may be distorted in that more recent incremental payments which include a lower proportion of pharmaceutical costs will be compared to pre-reform cumulative payments for the accident year which include significantly higher pharmaceutical costs. Staff summarized its recommended approach to adjust for these distortions in the paid medical loss development factors. Staff noted that the adjustment is similar to the WCIRB's standard approach for adjusting for other one-time shifts in payment patterns resulting from reforms but refined to compute the adjustments by accident year, maturity, and type of medical service (i.e., pharmaceuticals) using WCIRB medical transaction data. Staff noted that these adjustments would have a moderate impact on the medical loss development projection.

After discussion, the consensus of the Committee was that staff's proposed adjustments are appropriate and should be reflected in the updated summary of March 31, 2019 experience to be reviewed at the next meeting. Staff noted that adjustments to the medical paid-to-date ratio and medical on-level factors will also be reviewed at the next meeting so that the loss development adjustments are applied consistently and the impact of the pharmaceutical cost reductions are not double counted.

The meeting was adjourned at 12:25 PM.

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Note to Committee Members: These Minutes, as written, have not been approved. Please refer to the meeting scheduled for August 1, 2019 for approval and/or modification.