



Workers Compensation: Overview, Outlook and Review of Critical Issues

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■ Summary of P/C Financial Performance

- ◆ Profitability
- ◆ Underwriting Performance & Financial Strength
- ◆ Premium Growth
- ◆ Capital/Capacity
- ◆ Investments

■ Workers Compensation Operating Environment

- ◆ US and California Comparisons

■ Workers Compensation in the Aftermath of the “Great Recession”

- ◆ Economic Growth: US and CA
- ◆ Labor Market Analysis
- ◆ Impacts for Workers Compensation

■ Regulatory Update

- ◆ Dodd-Frank Implementation
- ◆ Federal Insurance Office: Status Update

■ Healthcare Reform: An Update and Implications for Workers Compensation

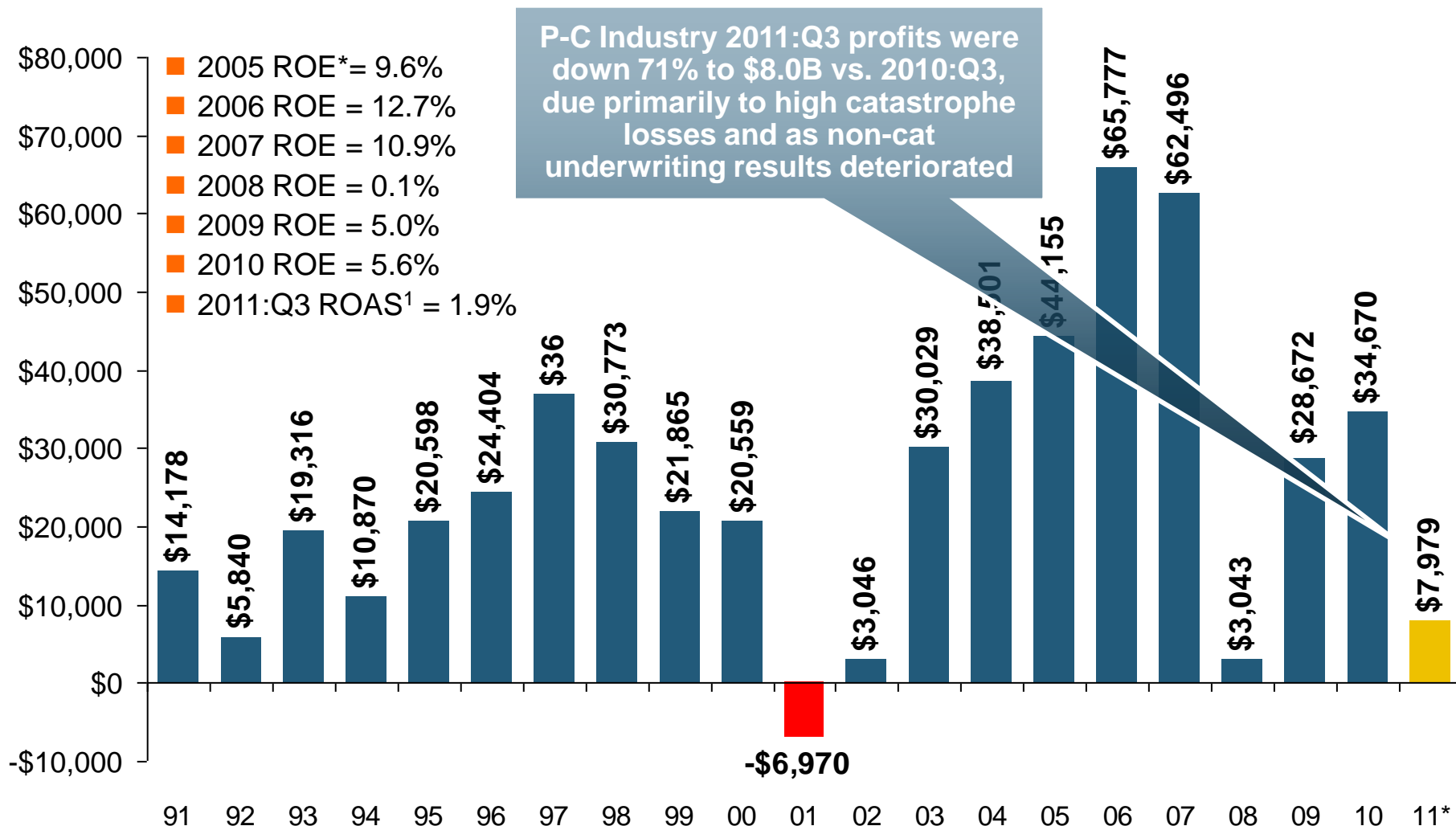
- ◆ Implementation Timetable for Key Provisions
- ◆ Medicare Issues
- ◆ Challenges to the PPACA (“ObamaCare”) & Supreme Court Hearings

■ Q&A

P/C Insurance Industry Financial Overview

**Profit Recovery Was Set Back
in 2011 by High Catastrophe
Loss & Other Factors**

P/C Net Income After Taxes 1991–2011:Q3 (\$ Millions)



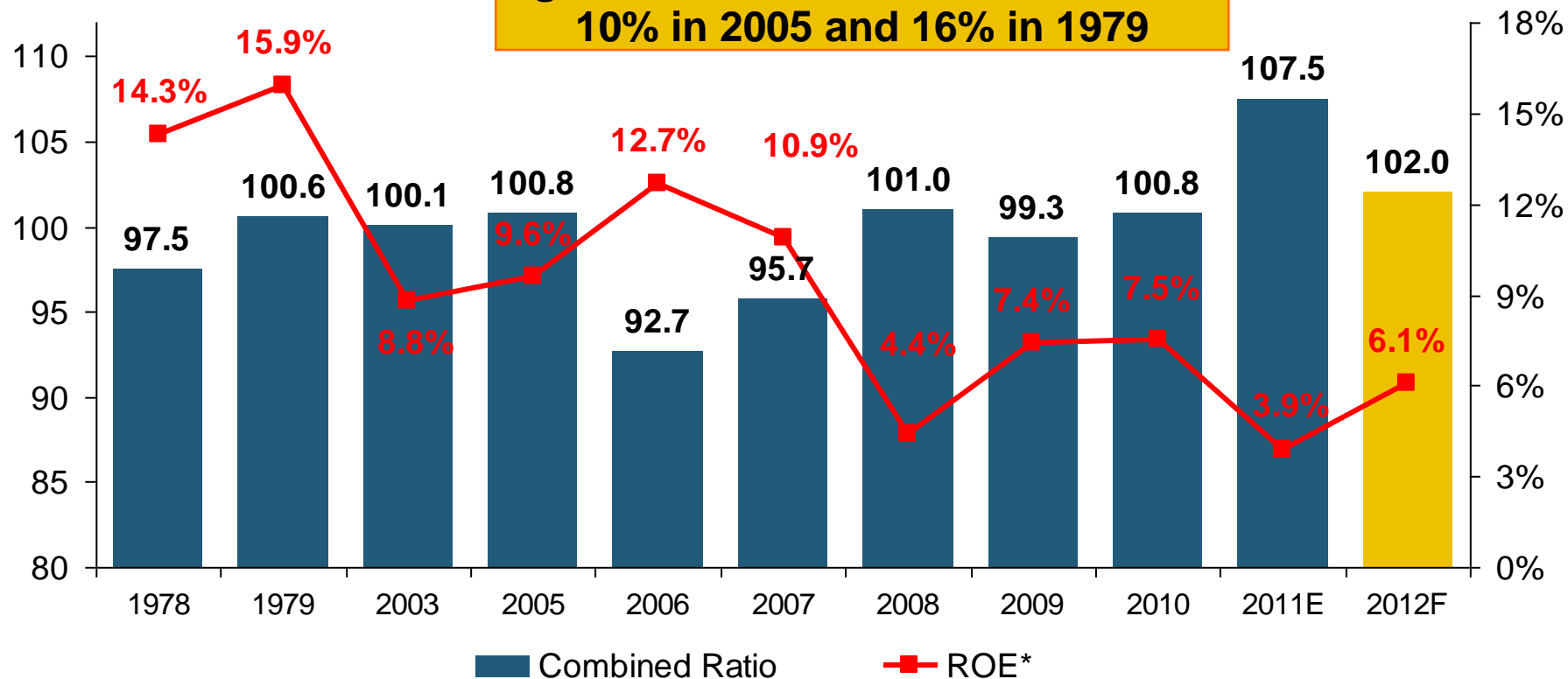
* ROE figures are GAAP; ¹Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields a 3.0% ROAS for 2011:Q3, 7.5% for 2010 and 7.4% for 2009.

Sources: A.M. Best, ISO, Insurance Information Institute

A 100 Combined Ratio Isn't What It Once Was: Investment Impact on ROEs

Combined Ratio / ROE

A combined ratio of about 100 generated ~7.5% ROE in 2009/10, 10% in 2005 and 16% in 1979

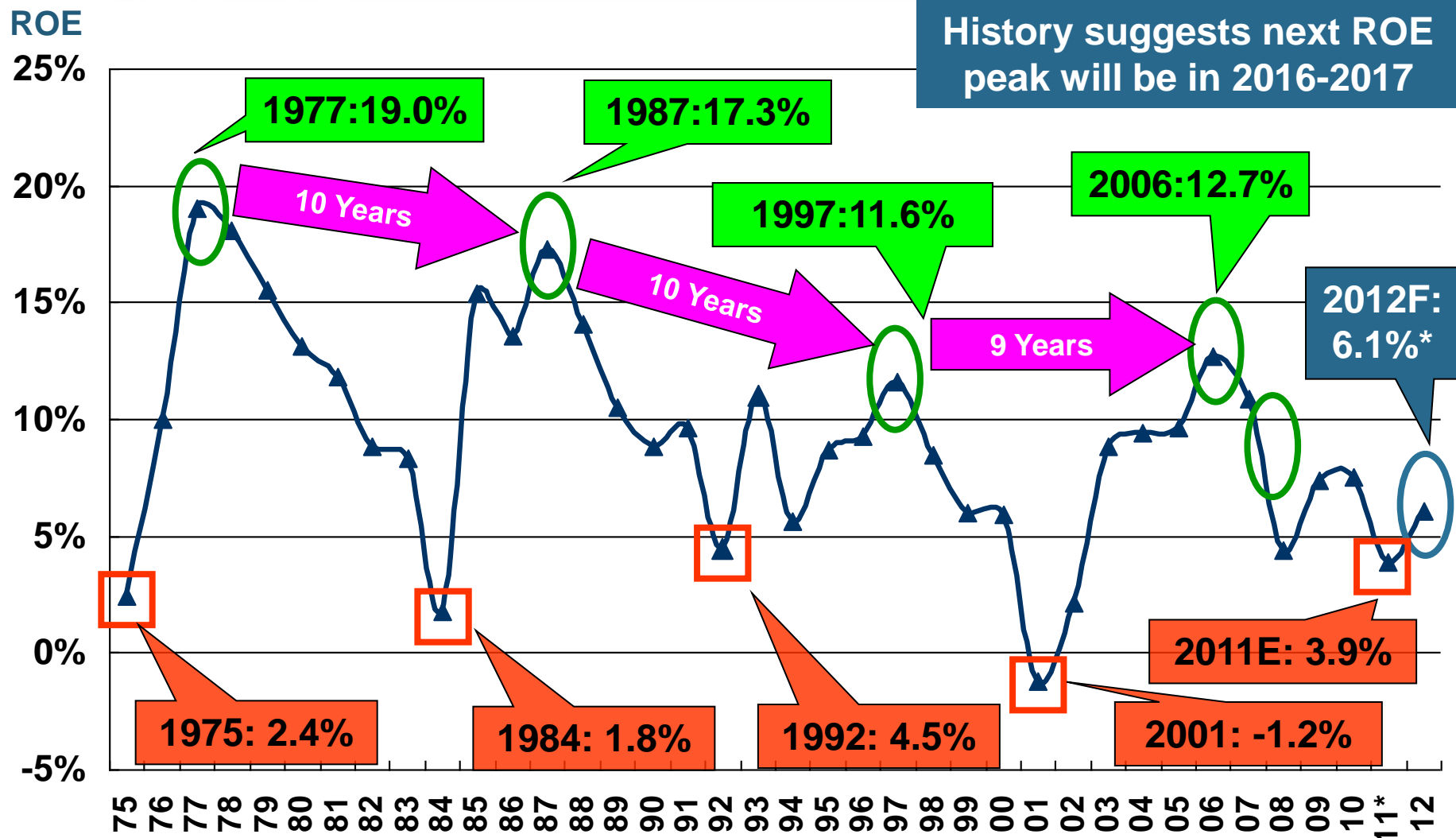


Combined Ratios Must Be Lower in Today's Depressed Investment Environment to Generate Risk Appropriate ROEs

* 2008 -2010 figures are return on average surplus and exclude mortgage and financial guaranty insurers. 2011-12 combined ratios are A.M. Best estimate excl. M&FG insurers.

Source: Insurance Information Institute from A.M. Best and ISO data.

Profitability Peaks & Troughs in the P/C Insurance Industry, 1975 – 2012F*

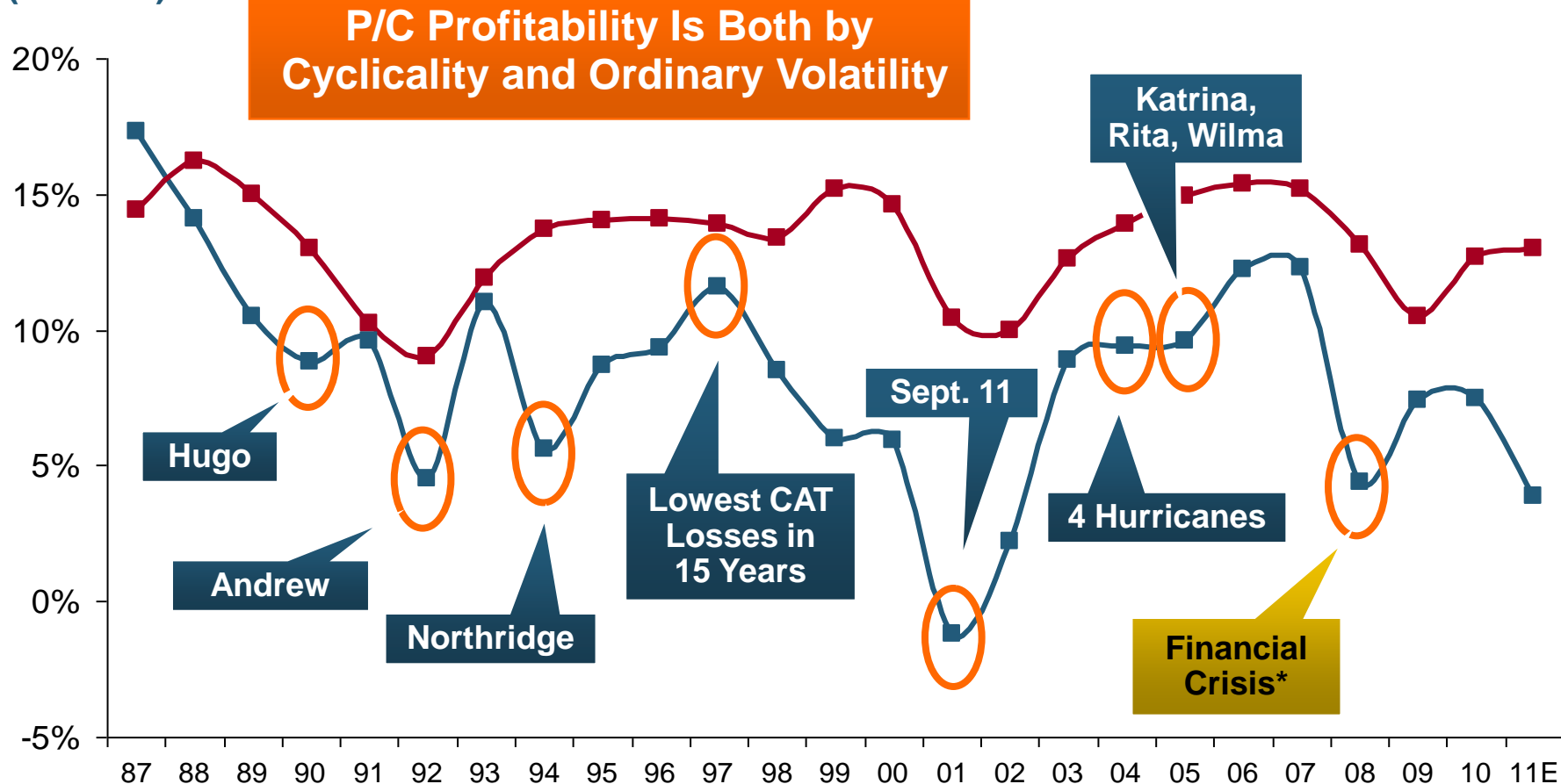


*Profitability = P/C insurer ROEs. 2011-12 figures are A.M. Best estimates. Note: Data for 2008-2012 exclude mortgage and financial guaranty insurers. For 2011:Q3 ROAS = 1.9% including M&FG.

Source: Insurance Information Institute; NAIC, ISO, A.M. Best.

ROE: Property/Casualty Insurance vs. Fortune 500, 1987–2011*

(Percent)



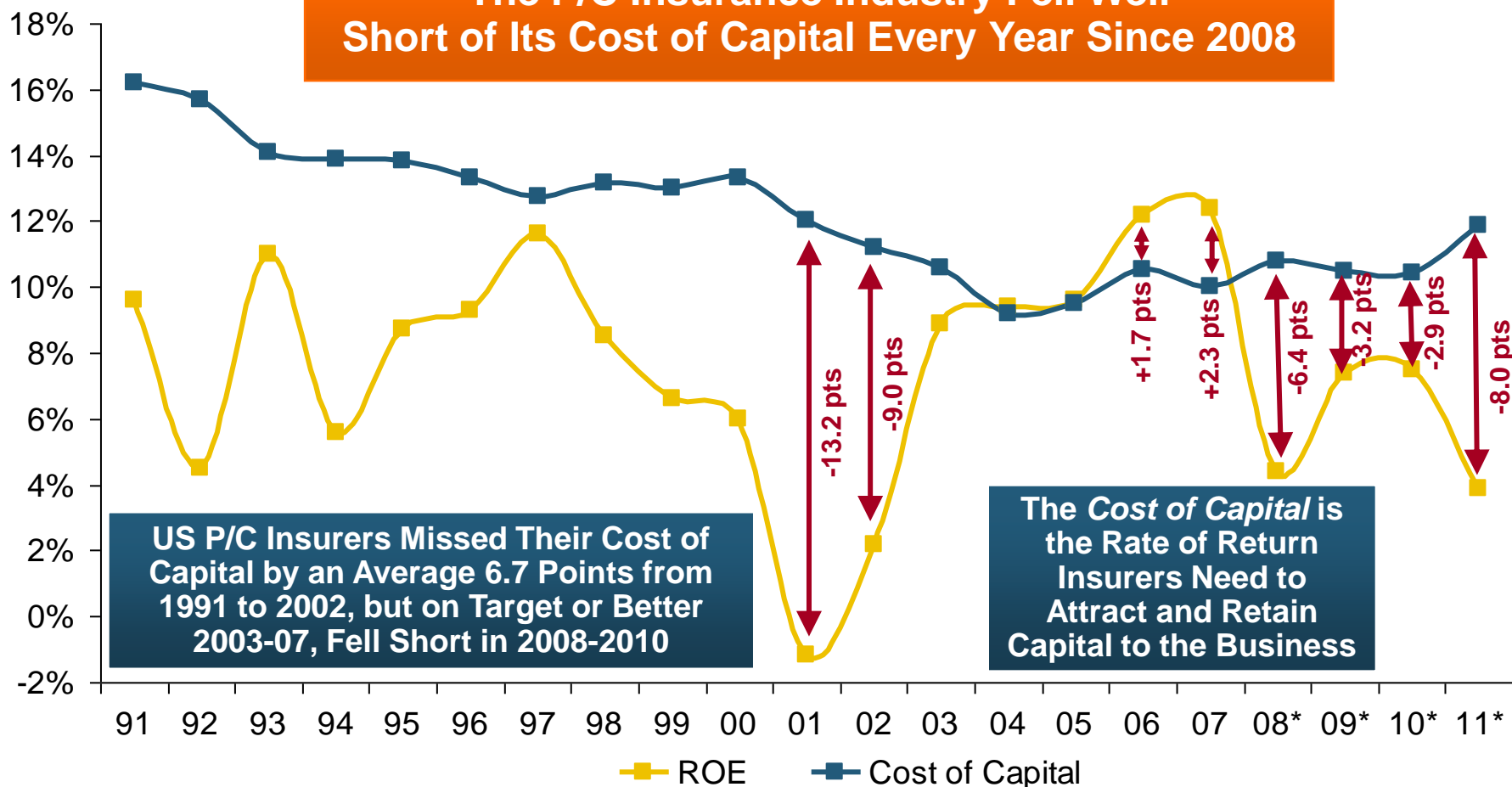
* Excludes Mortgage & Financial Guarantee in 2008 - 2011.

Sources: ISO, *Fortune*; A.M. Best (2011 P/C ROE); Insurance Information Institute (2011 Fortune 500 est.)

ROE vs. Equity Cost of Capital: U.S. P/C Insurance:1991-2011*

(Percent)

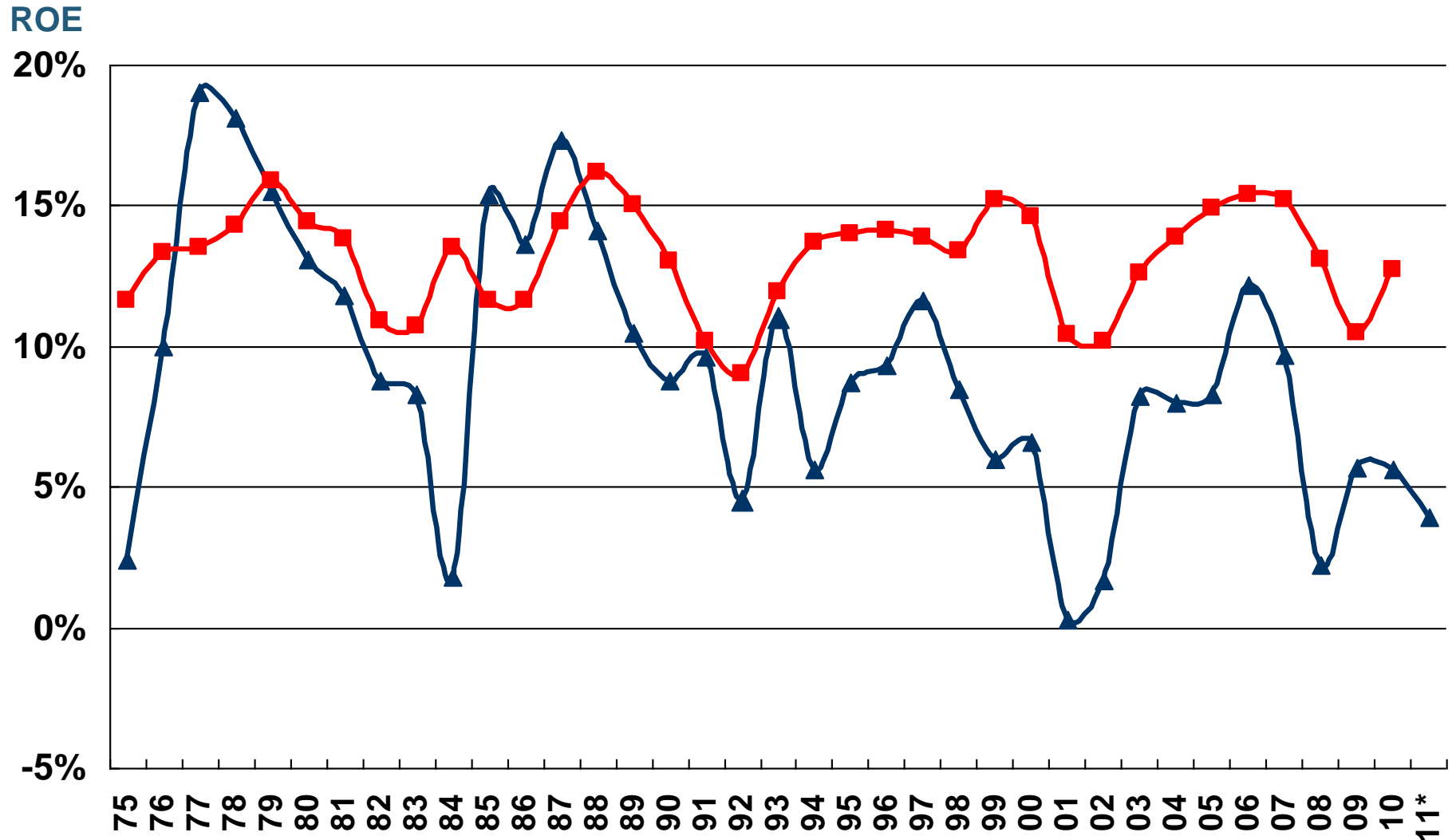
**The P/C Insurance Industry Fell Well
Short of Its Cost of Capital Every Year Since 2008**



* Return on average surplus used as proxy for ROE in 2008-2010 and excluding mortgage and financial guaranty insurers for these years. 2011 figure is A.M. Best ROE estimate. Change in model methodology in 2011 increased cost of capital by approximately 90 basis points.

Source: The Geneva Association, Insurance Information Institute

P/C Insurance Industry ROE vs. Fortune 500, 1975 – 2011*



*2011 is A.M. Best figure excl. mortgage and financial guaranty segments.

Source: Insurance Information Institute; NAIC, ISO.

The BIG Question: When Will the Market Turn?

Are Catastrophes and Other Factors Pressuring Insurance Markets?

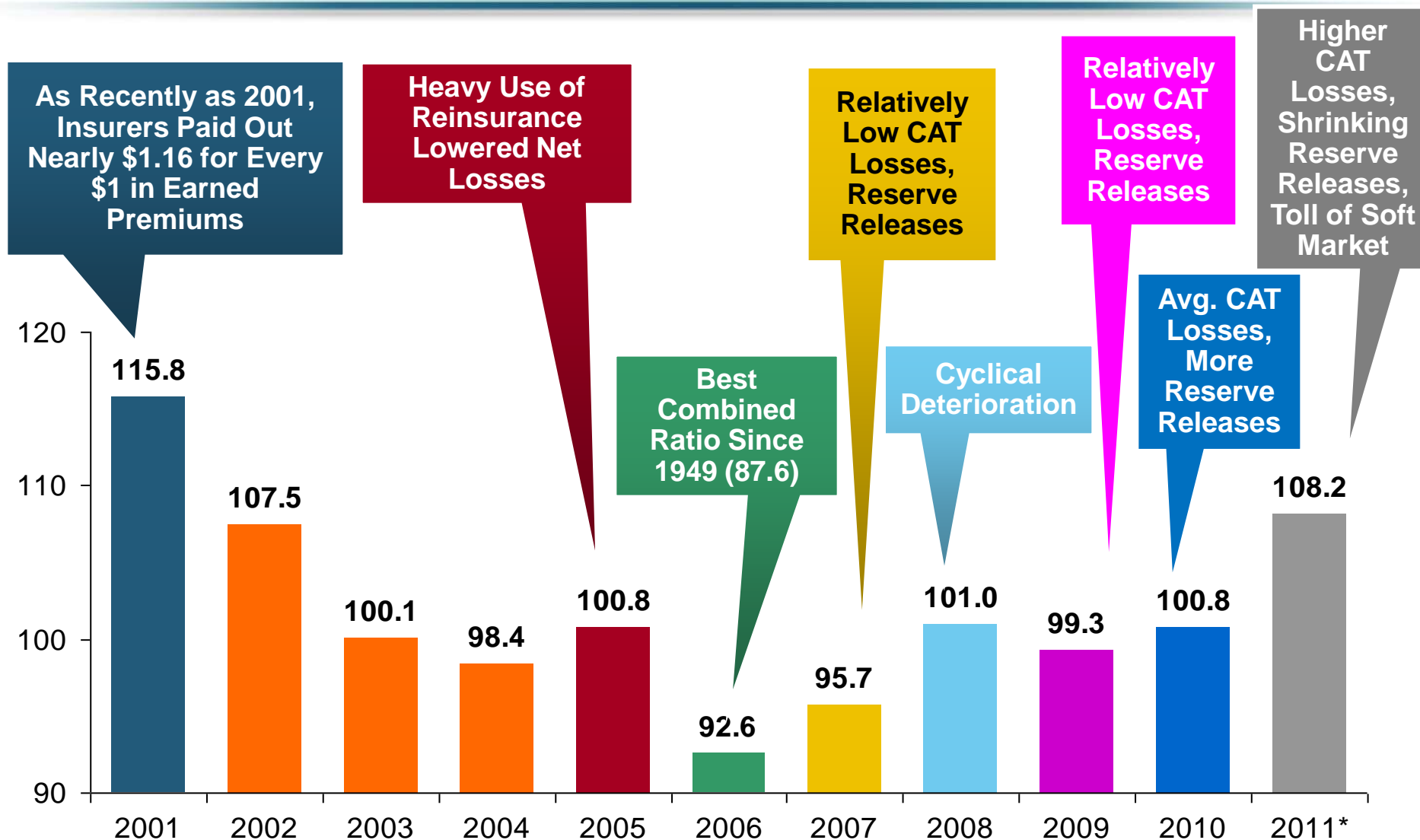
Criteria Necessary for a “Market Turn”: All Four Criteria Must Be Met

Criteria	Status	Comments
Sustained Period of Large Underwriting Losses	<i>Early Stage, Inevitable</i>	<ul style="list-style-type: none"> • Apart from 2011 CAT losses, overall p/c underwriting losses remain modest • Combined ratios (ex-CATs) still in low 100s (vs. 110+ at onset of last hard market) • Prior-year reserve releases continue to reduce u/w losses, boost ROEs, though more modestly
Material Decline in Surplus/ Capacity	<i>Entered 2011 At Record High; Since Fallen</i>	<ul style="list-style-type: none"> • Surplus hit a record \$565B as of 3/31/11 • Fell by 4.6% through 9/30/11 (latest available) • Little excess capacity remains in reinsurance markets • Weak growth in demand for insurance is insufficient to absorb much excess capacity
Tight Reinsurance Market	<i>Somewhat in Place</i>	<ul style="list-style-type: none"> • Much of the global “excess capacity” was eroded by cats • Higher prices in Asia/Pacific • Modestly higher pricing for US risks
Renewed Underwriting & Pricing Discipline	<i>Some Firming esp. in Property, WC</i>	<ul style="list-style-type: none"> • Commercial lines pricing trends have turned from negative to flat or up in some lines (property, WC); Casualty is flat. • Competition remains intense as many seek to maintain market share

P/C UNDERWRITING TRENDS

**Have Underwriting Losses
Been Large Enough for Long
Enough to Turn the Market?**

P/C Insurance Industry Combined Ratio, 2001–2011:Q3*

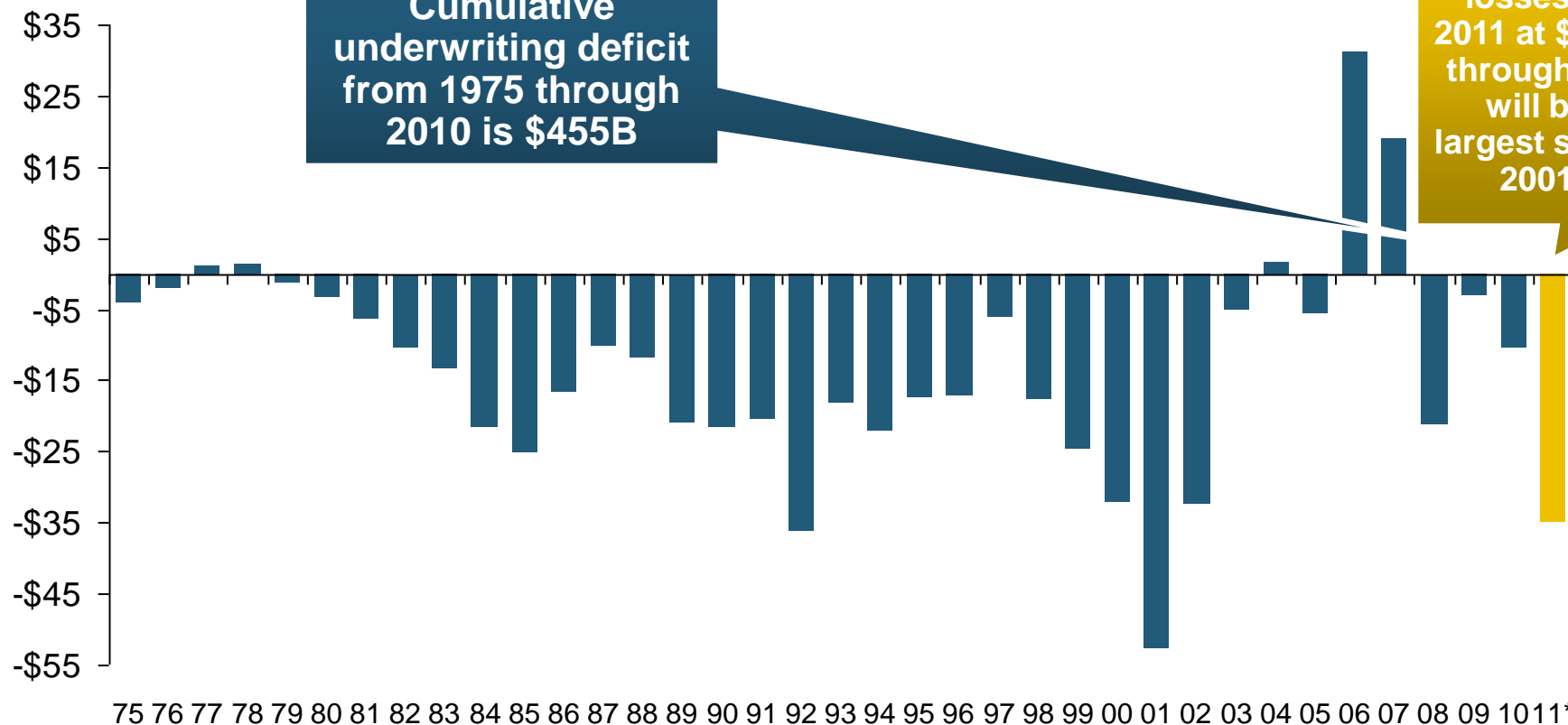


* Excludes Mortgage & Financial Guaranty insurers 2008--2011. Including M&FG, 2008=105.1, 2009=100.7, 2010=102.4, 2011=109.9

Sources: A.M. Best, ISO.

Underwriting Gain (Loss) 1975–2011*

(\$ Billions)



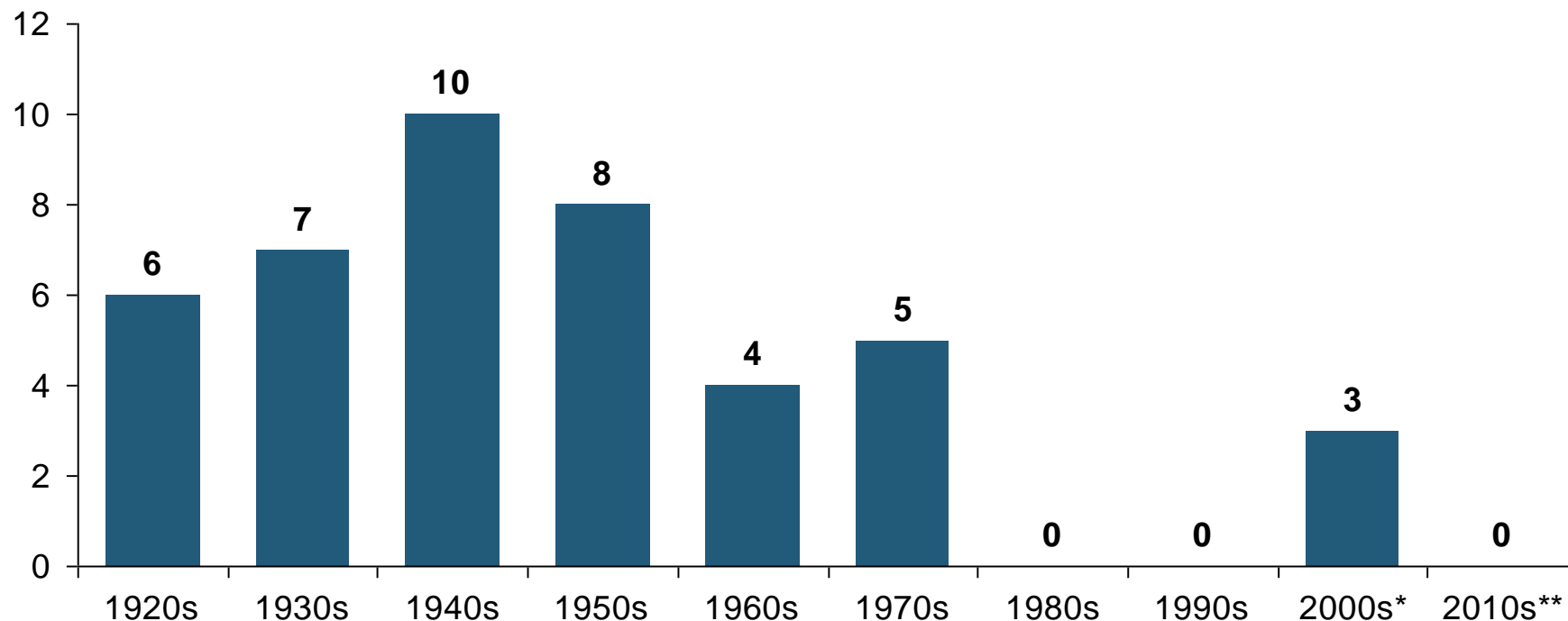
**Large Underwriting Losses Are *NOT* Sustainable
in Current Investment Environment**

* Includes mortgage and financial guaranty insurers in all years

Sources: A.M. Best, ISO; Insurance Information Institute.

Number of Years with Underwriting Profits by Decade, 1920s–2010s

Number of Years with Underwriting Profits



Underwriting Profits Were Common Before the 1980s (40 of the 60 Years Before 1980 Had Combined Ratios Below 100) – But Then They Vanished. Not a Single Underwriting Profit Was Recorded in the 25 Years from 1979 Through 2003

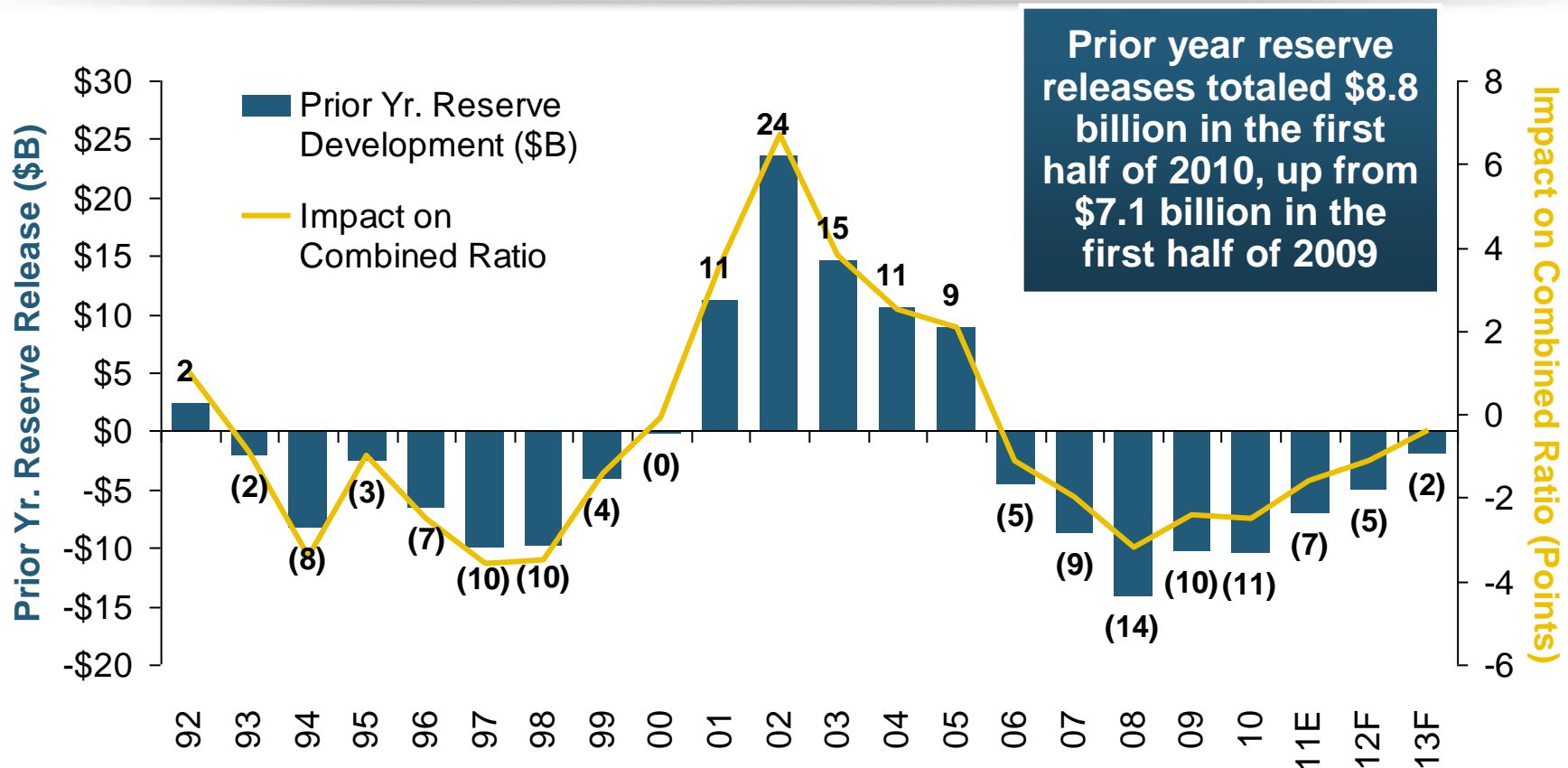
* 2009 combined ratio excl. mort. and finl. guar.anty insurers was 99.3, which would bring the 2000s total to 4 years with an u/w profit.

**Data for the 2010s includes 2010 and 2011.

Note: Data for 1920–1934 based on stock companies only.

Sources: Insurance Information Institute research from A.M. Best Data.

P/C Reserve Development, 1992–2013F



Reserve Releases Remained Strong in 2010 But Tapered Off in 2011. Releases Are Expected to Further Diminish in 2012 and 2103

Note: 2005 reserve development excludes a \$6 billion loss portfolio transfer between American Re and Munich Re. Including this transaction, total prior year adverse development in 2005 was \$7 billion. The data from 2000 and subsequent years excludes development from financial guaranty and mortgage insurance.

Sources: Barclays Capital; A.M. Best.

P/C Estimated Loss Reserve Deficiency/ (Redundancy), Excl. Statutory Discount

Line of Business	2011
Personal Auto Liability	-\$1.8B
Homeowners	-\$0.2
Other Liab (incl. Prod Liab)	\$4.0
Workers Compensation	\$8.2
Commercial Multi Peril	\$1.5
Commercial Auto Liability	\$0.0
Medical Malpractice	-\$4.0
Reinsurance—Nonprop Assumed	\$3.4
All Other Lines*	-\$2.2
Total Core Reserves	\$8.9
Asbestos & Environmental	\$7.4
Total P/C Industry	\$16.3B

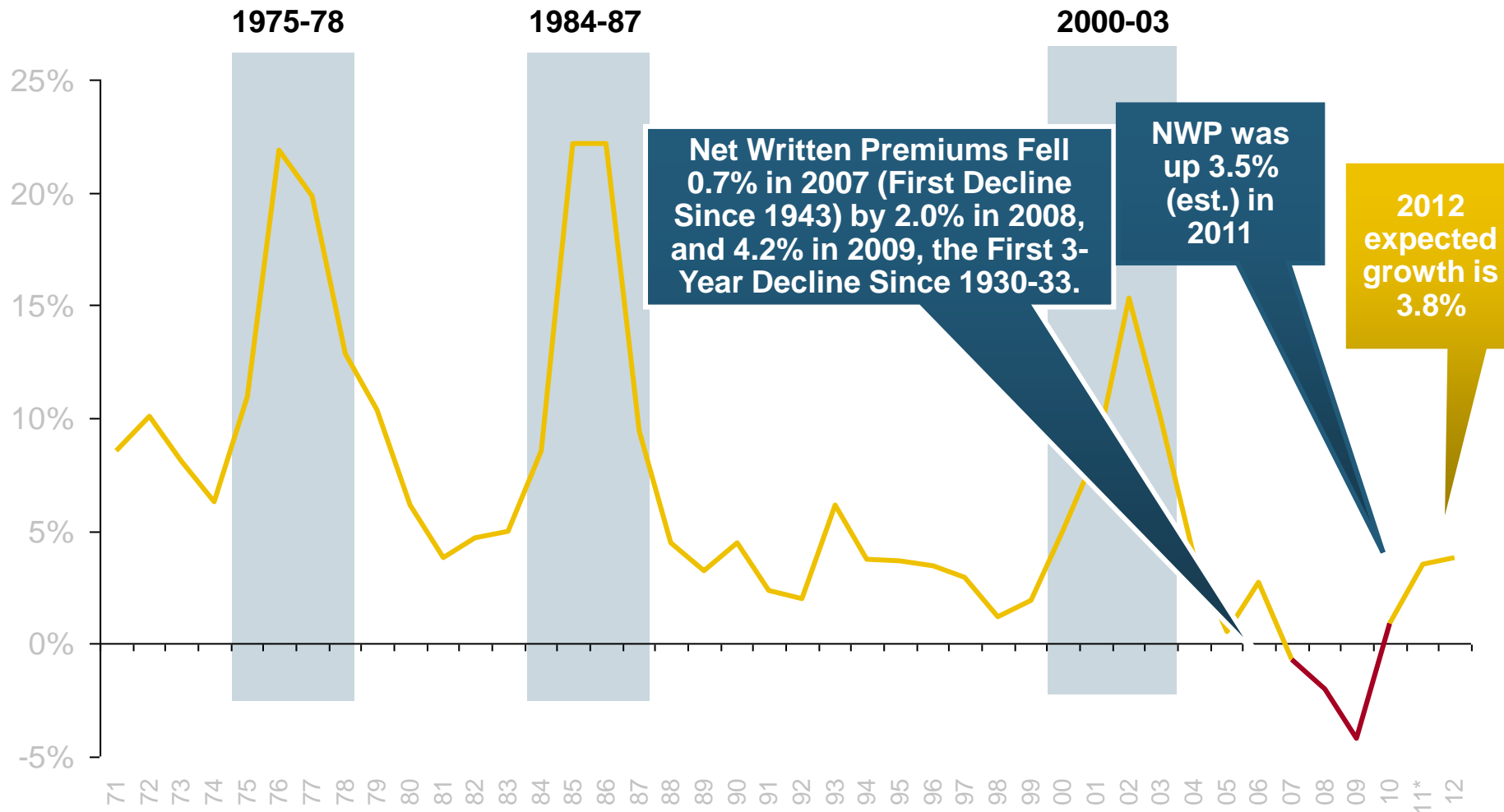
Workers Comp
has a significant
reserve
deficiency

RENEWED PRICING DISCIPLINE?

**Is There Evidence of a Broad
and Sustained Shift in Pricing?**

Soft Market Persisted into Early 2011 but Growth Returned: More in 2012?

(Percent)



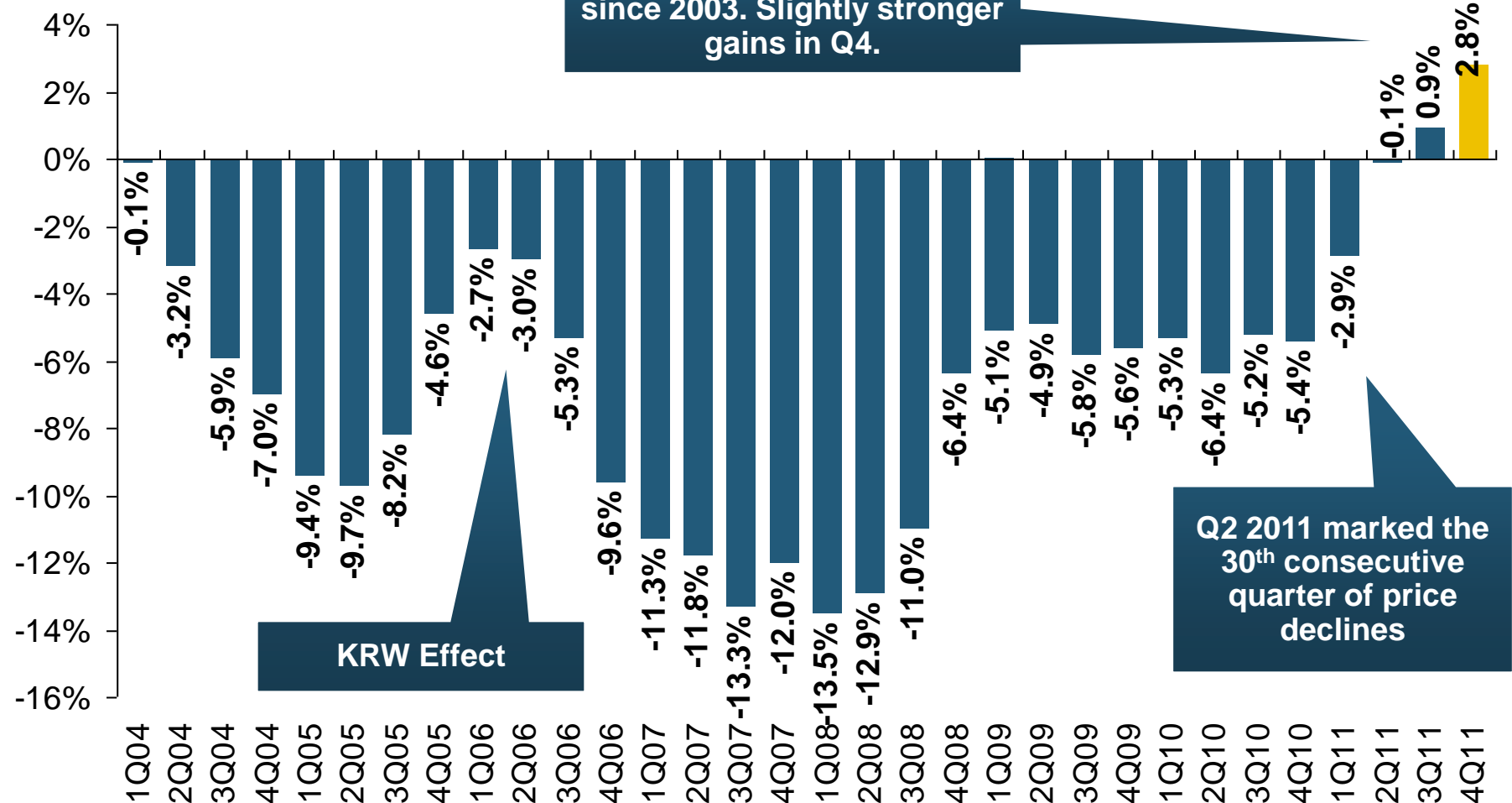
*2011 and 2012 figures are A.M. Best Estimates

Shaded areas denote "hard market" periods

Sources: A.M. Best (historical and forecast), ISO, Insurance Information Institute.

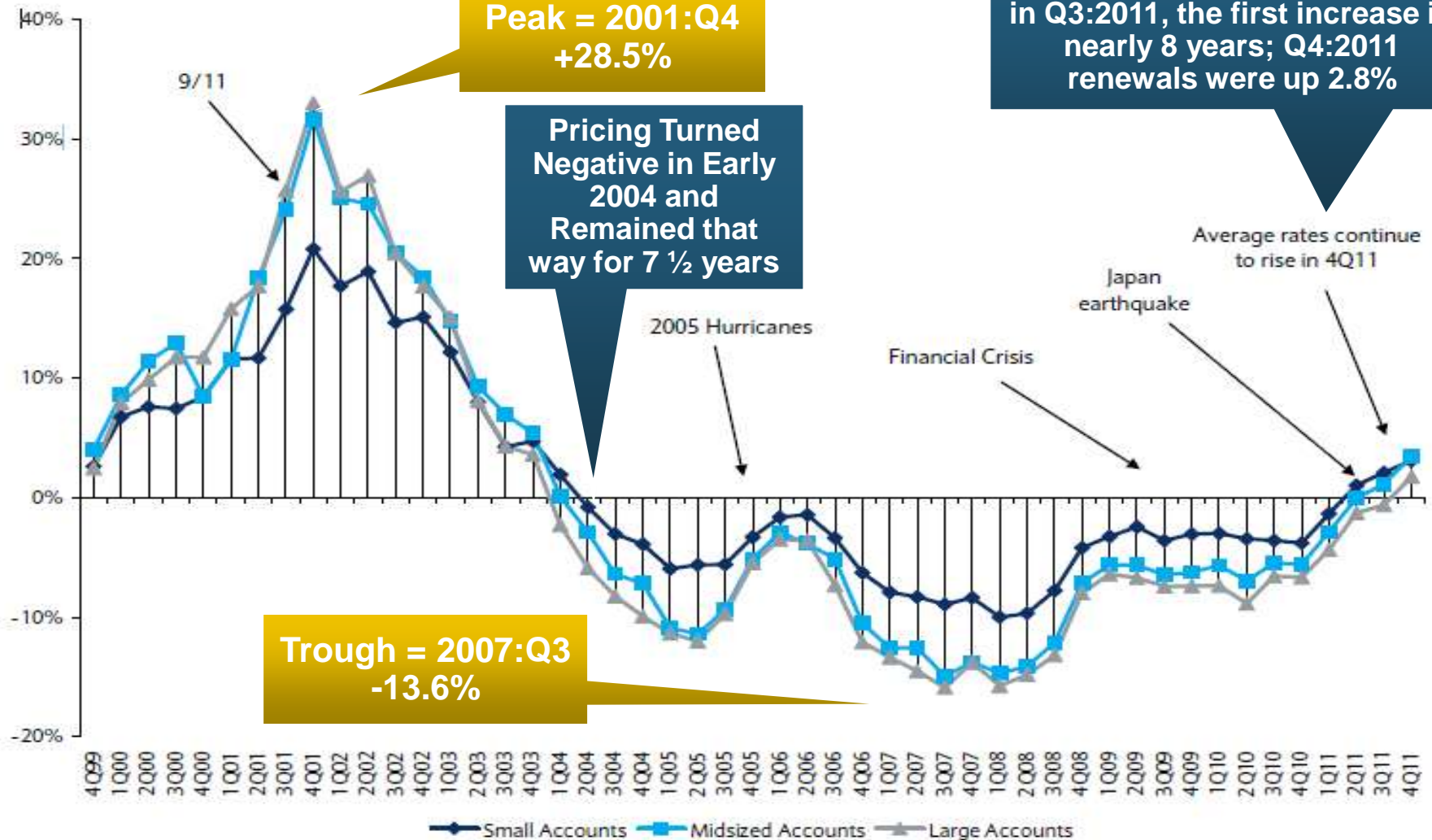
Average Commercial Rate Change, All Lines, (1Q:2004–4Q:2011)

(Percent)



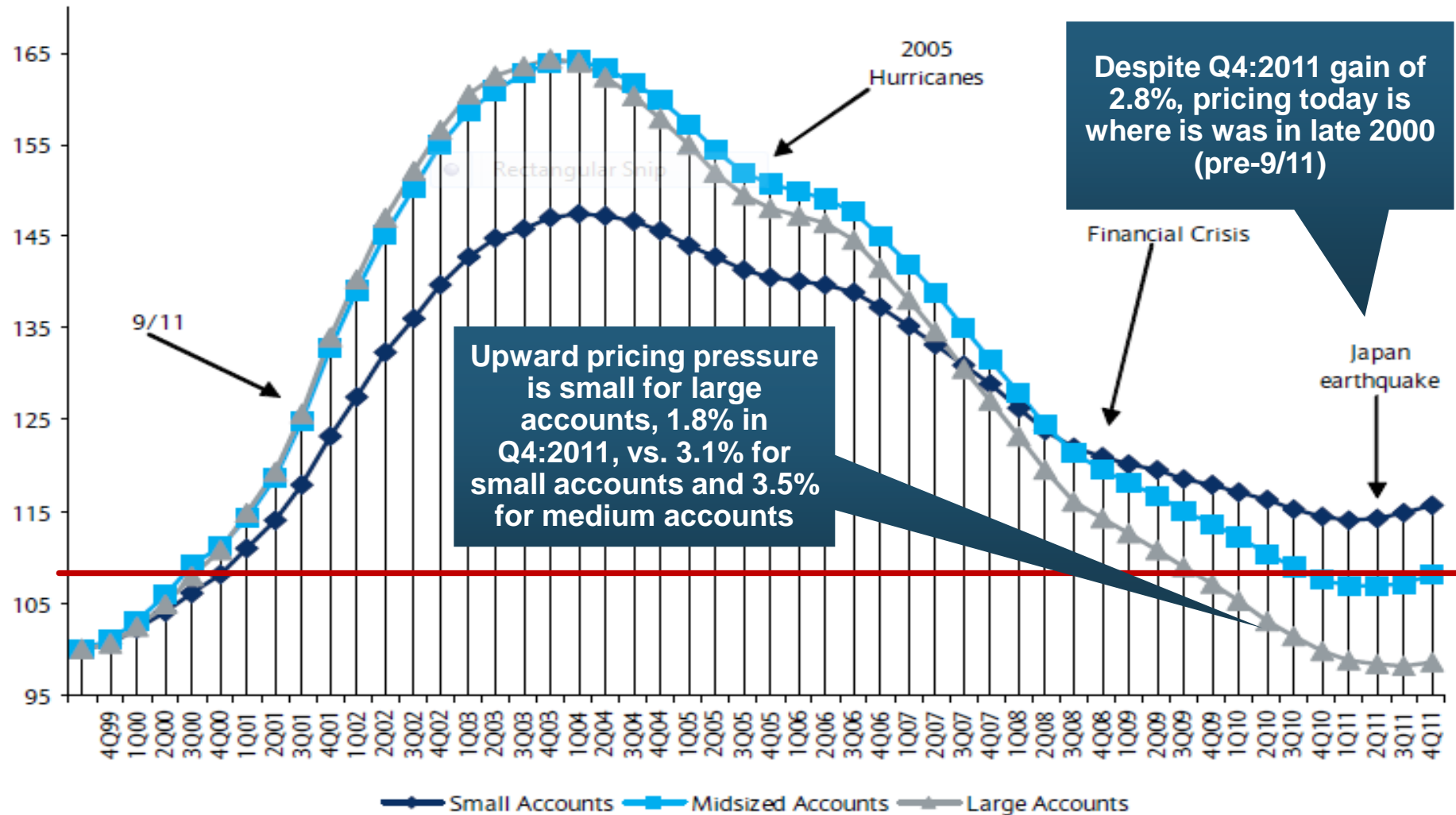
Change in Commercial Rate Renewals, by Account Size: 1999:Q4 to 2011:Q4

Percentage Change (%)



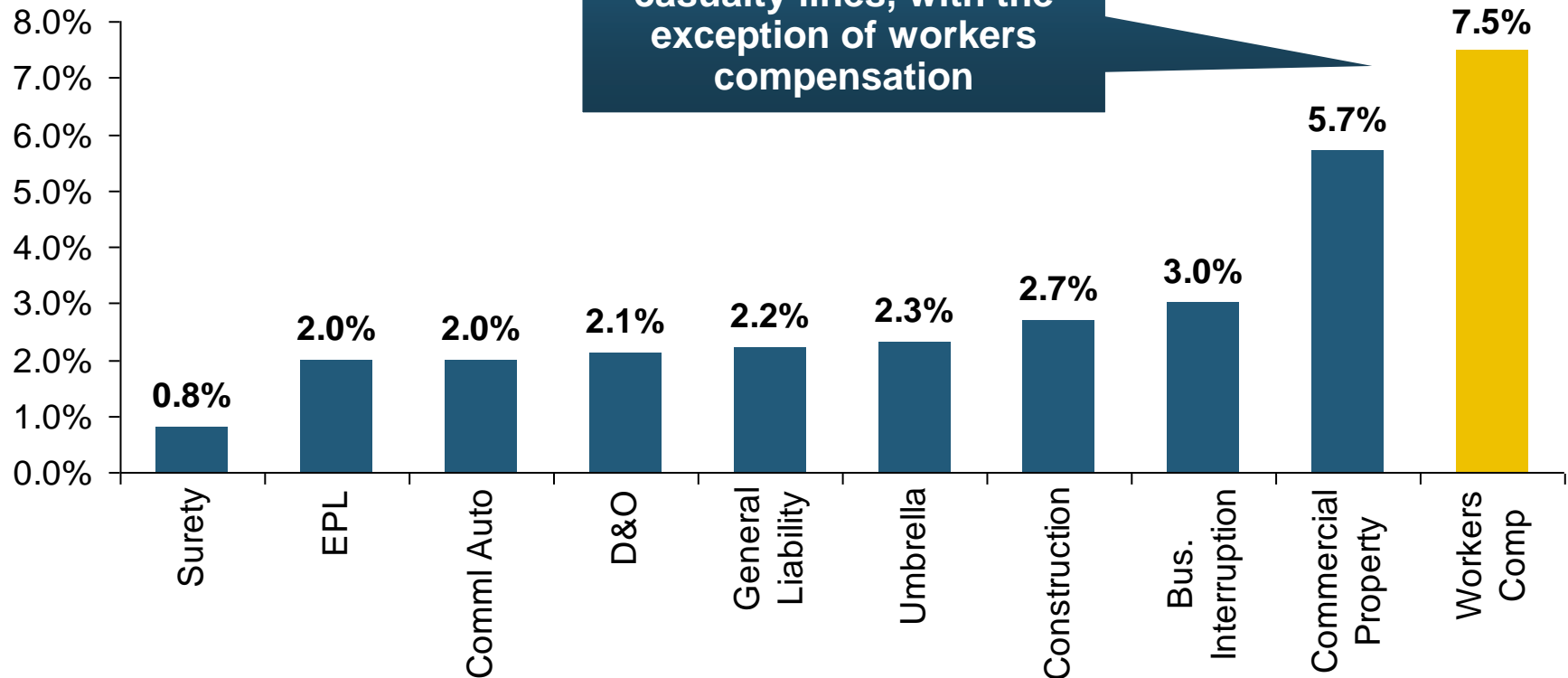
Cumulative Qtrly. Commercial Rate Changes, by Account Size: 1999:Q4 to 2011:Q4

1999:Q4 = 100



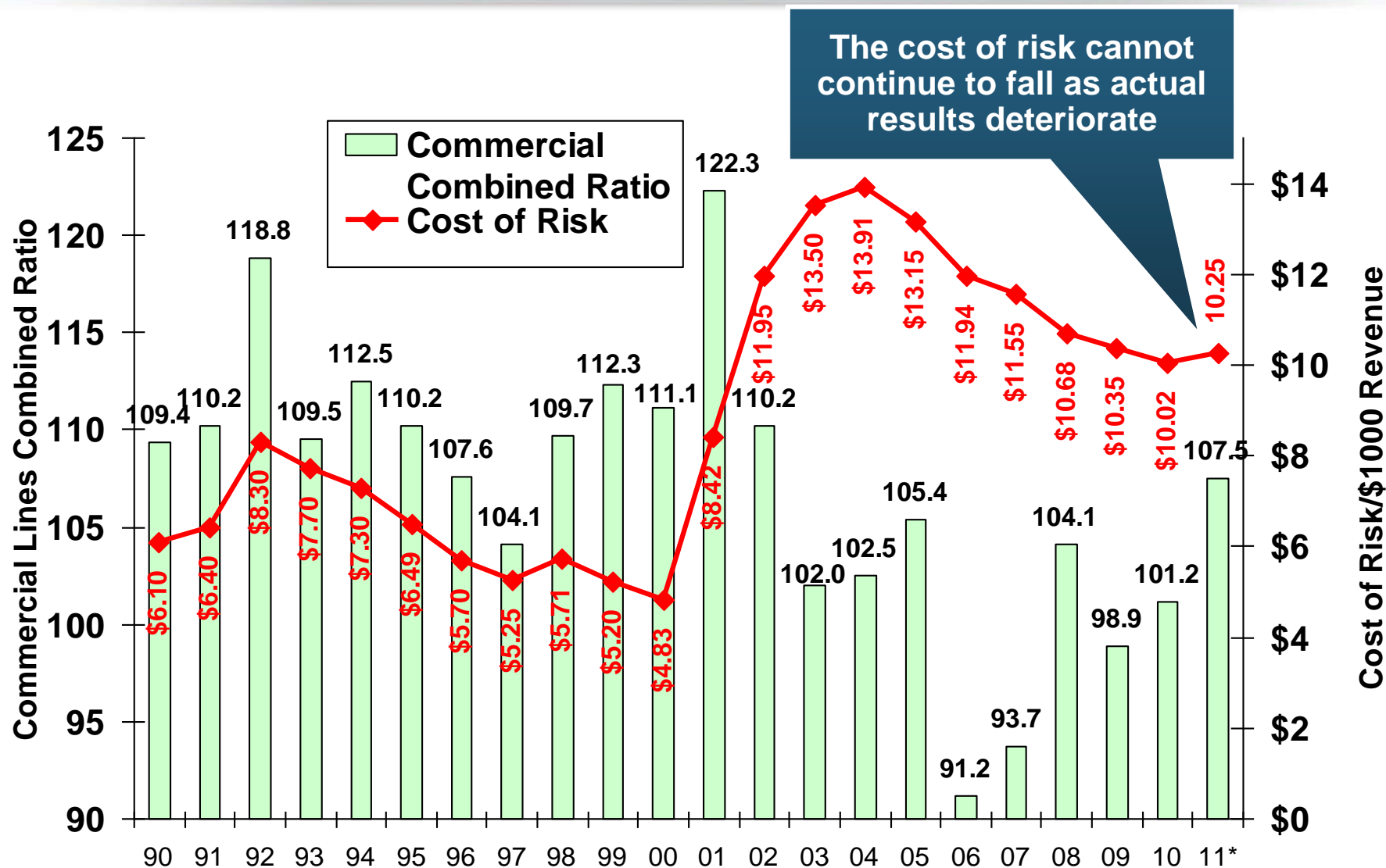
Change in Commercial Rate Renewals, by Line: 2011:Q4

Percentage Change (%)



Major Commercial Lines Renewed Uniformly Upward in Q4:2011 for Only the Second Time Since 2003; Property Lines & Workers Comp Leading the Way

Cost of Risk vs. Commercial Lines Combined Ratio



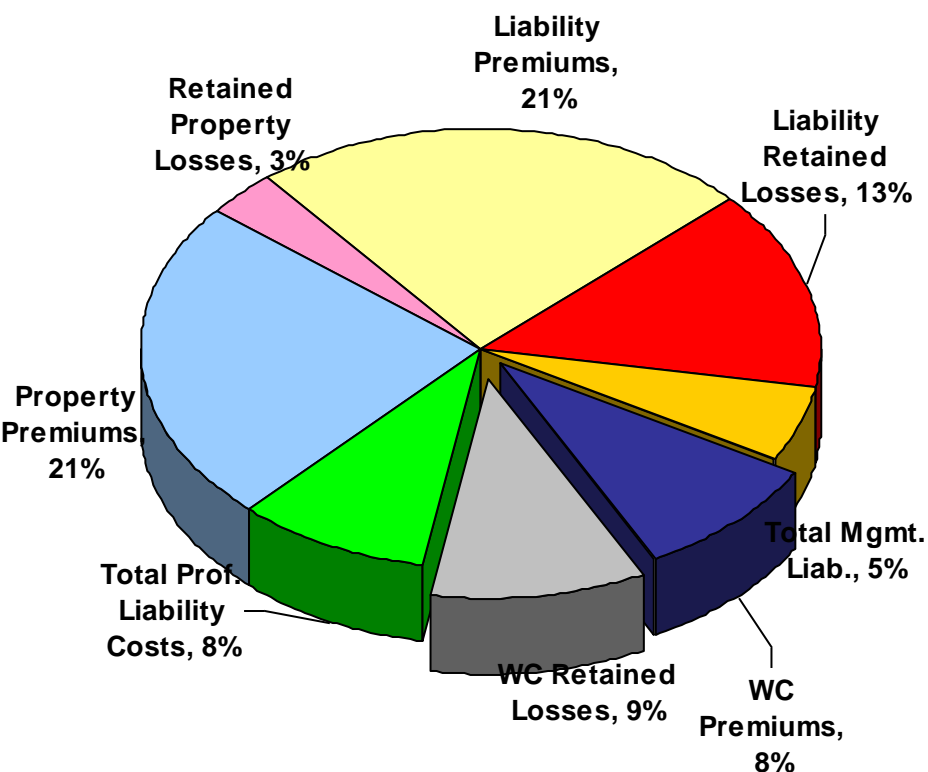
*Insurance Information Institute estimates for 2011.

Source: 2011 RIMS Benchmark Survey; A.M. Best; Insurance Information Institute

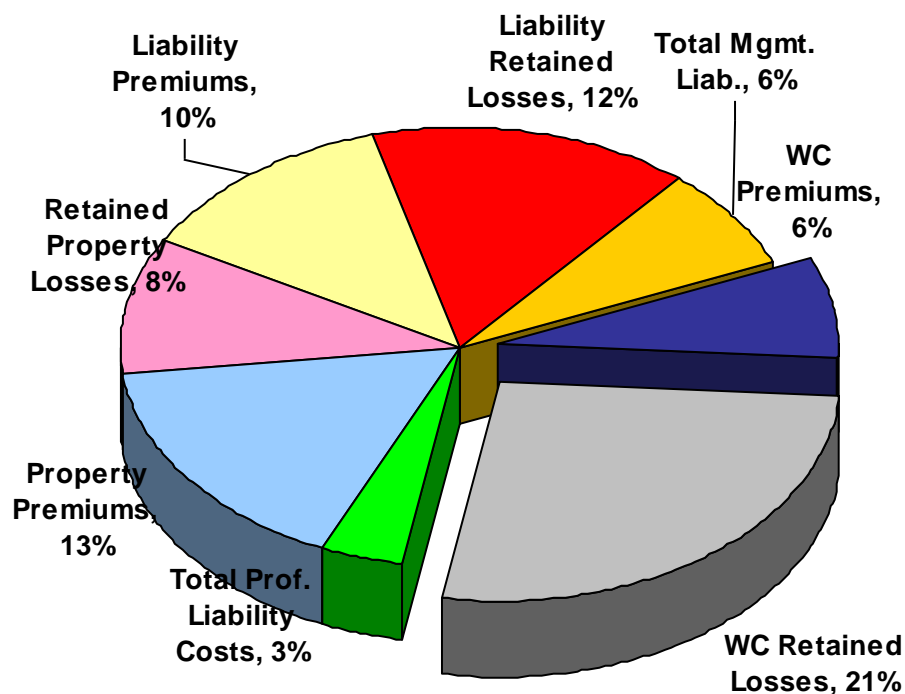
How the Risk Dollar is Spent (2011)

**Management & Professional Liability Costs Account for
17% - 27% of the Risk Dollar**

Firms w/Revenues < \$1 Billion

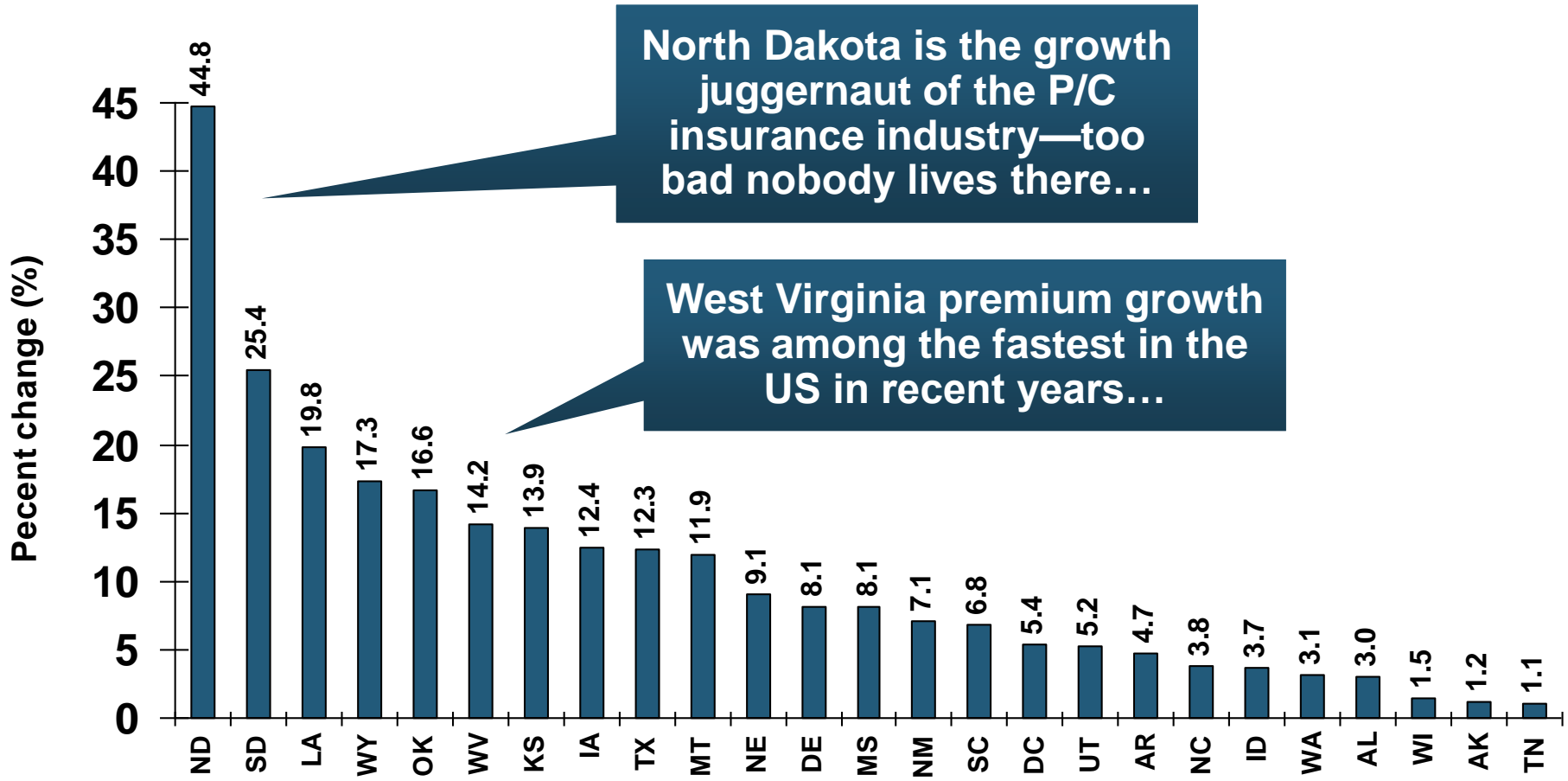


Firms w/Revenues > \$1 Billion



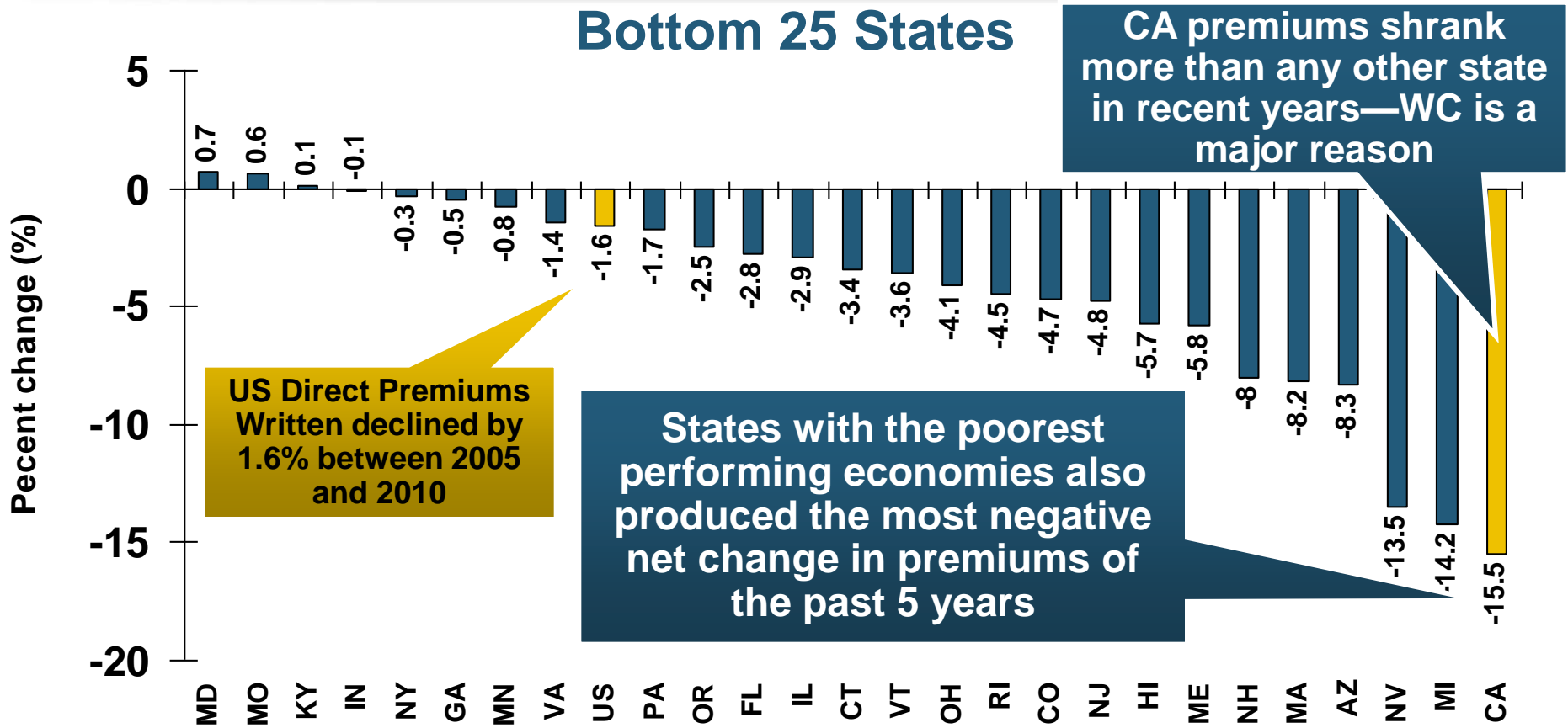
Direct Premiums Written: All P/C Lines Percent Change by State, 2005-2010

Top 25 States



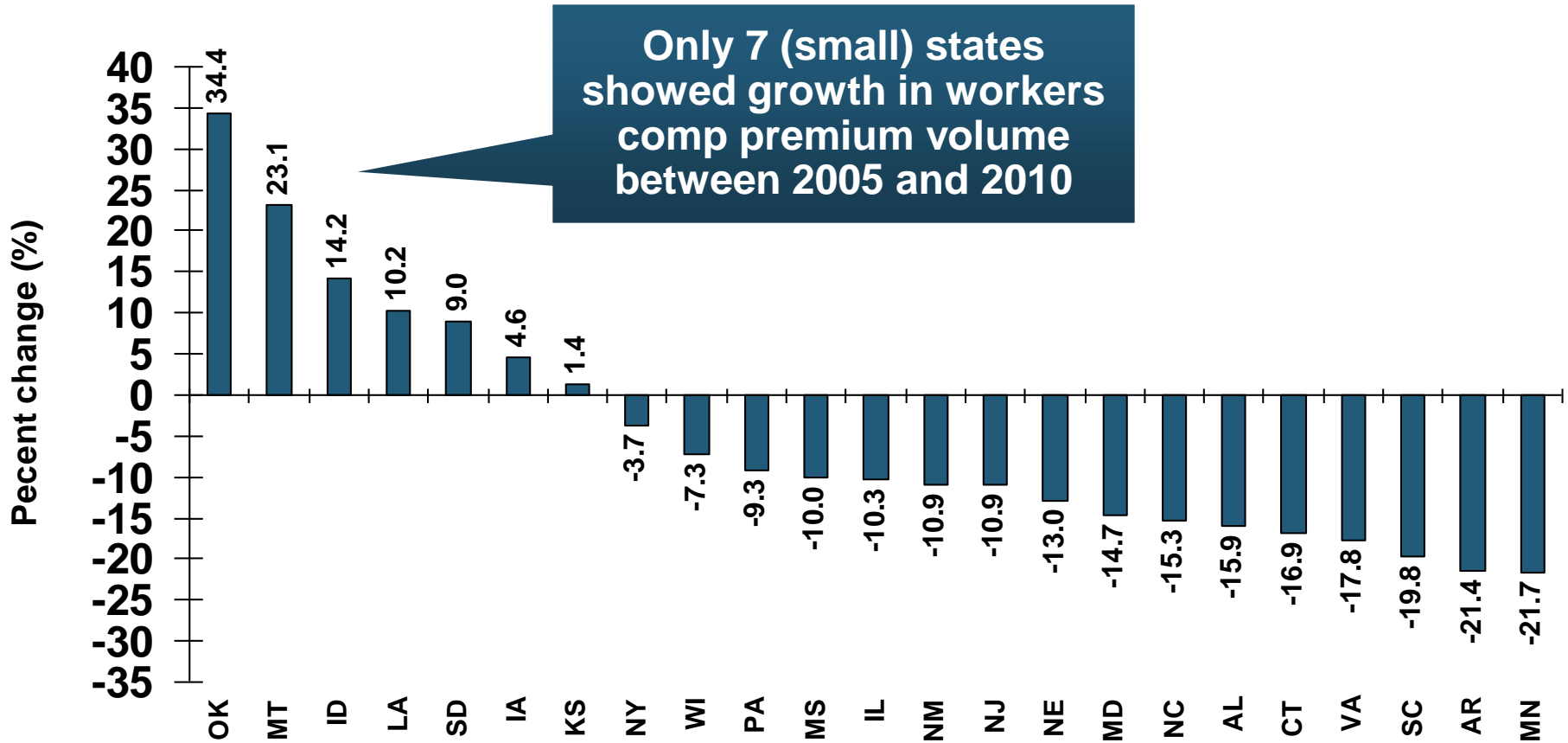
Sources: SNL Financial LC.; Insurance Information Institute.

Direct Premiums Written: All P/C Lines Percent Change by State, 2005-2010



Direct Premiums Written: Worker's Comp Percent Change by State, 2005-2010*

Top 25 States



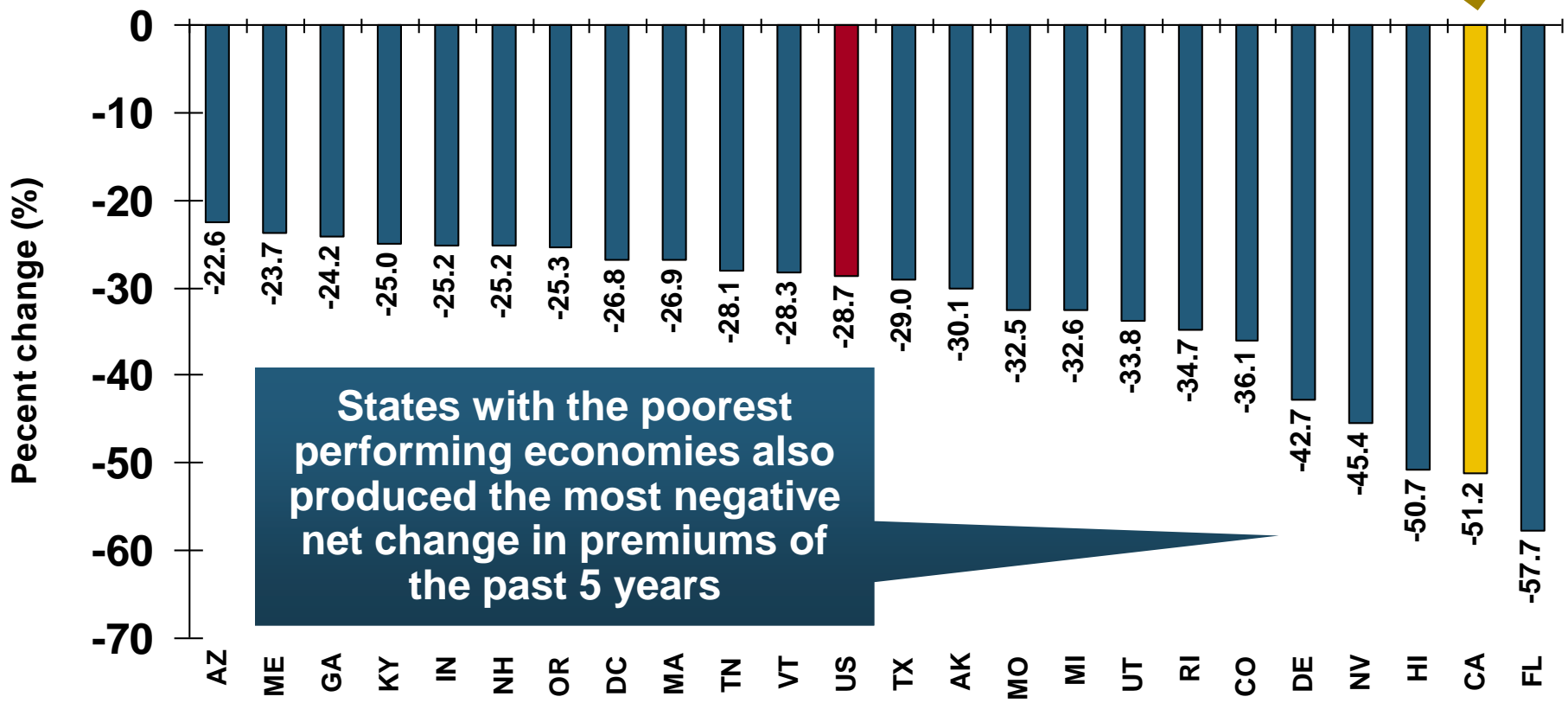
*Excludes monopolistic fund states: ND, OH, WA, WY as well as WV, which transitioned to a competitive structure during this period.

Sources: SNL Financial LC.; Insurance Information Institute.

Direct Premiums Written: Worker's Comp Percent Change by State, 2005-2010*

Bottom 25 States

CA Workers Comp
DPW plunged 51.2%
between 2005 and 2010



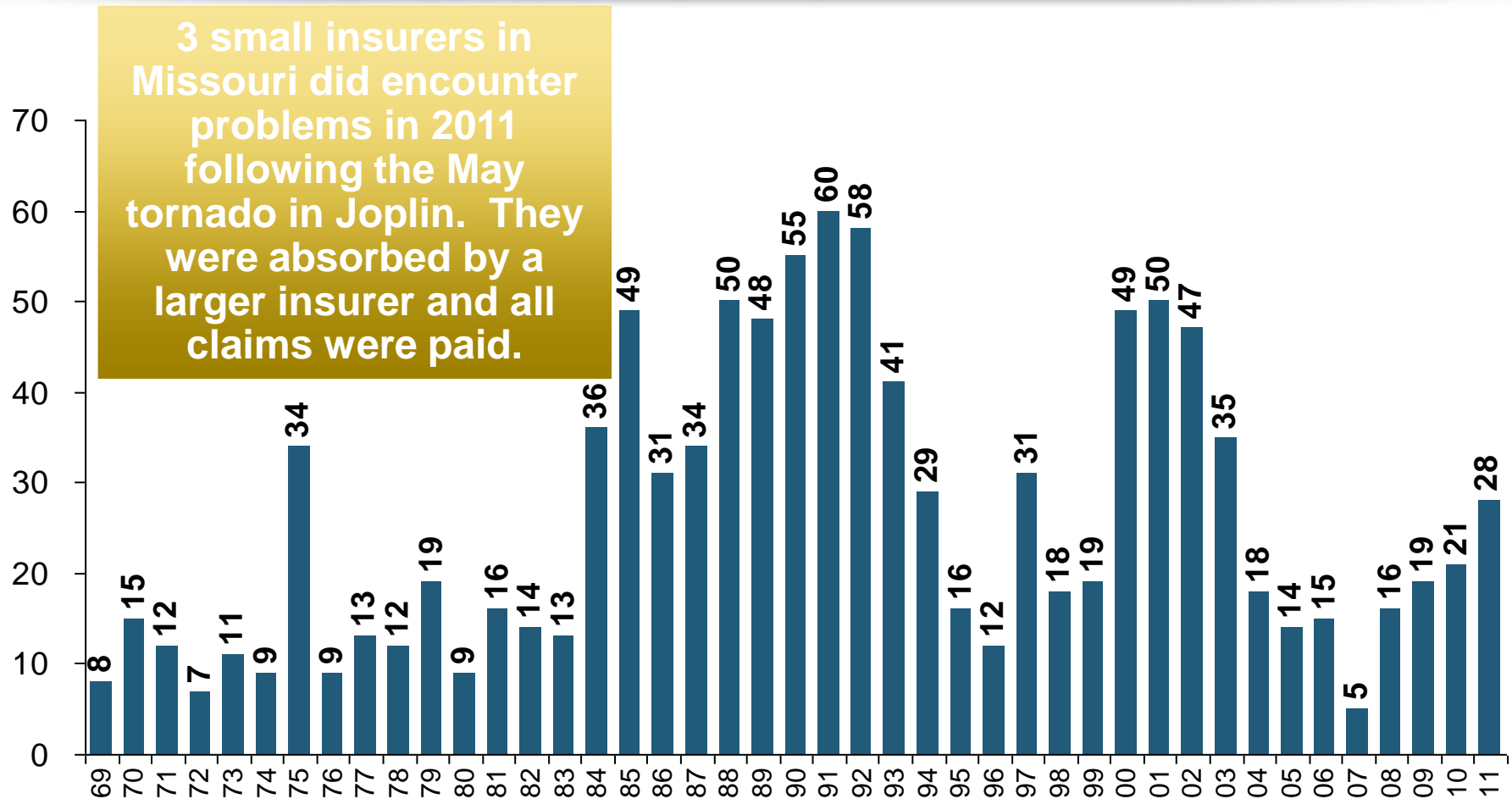
*Excludes monopolistic fund states: ND, OH, WA, WY as well as WV, which transitioned to a competitive structure during this period.

Sources: SNL Financial LC.; Insurance Information Institute.

Financial Strength & Underwriting

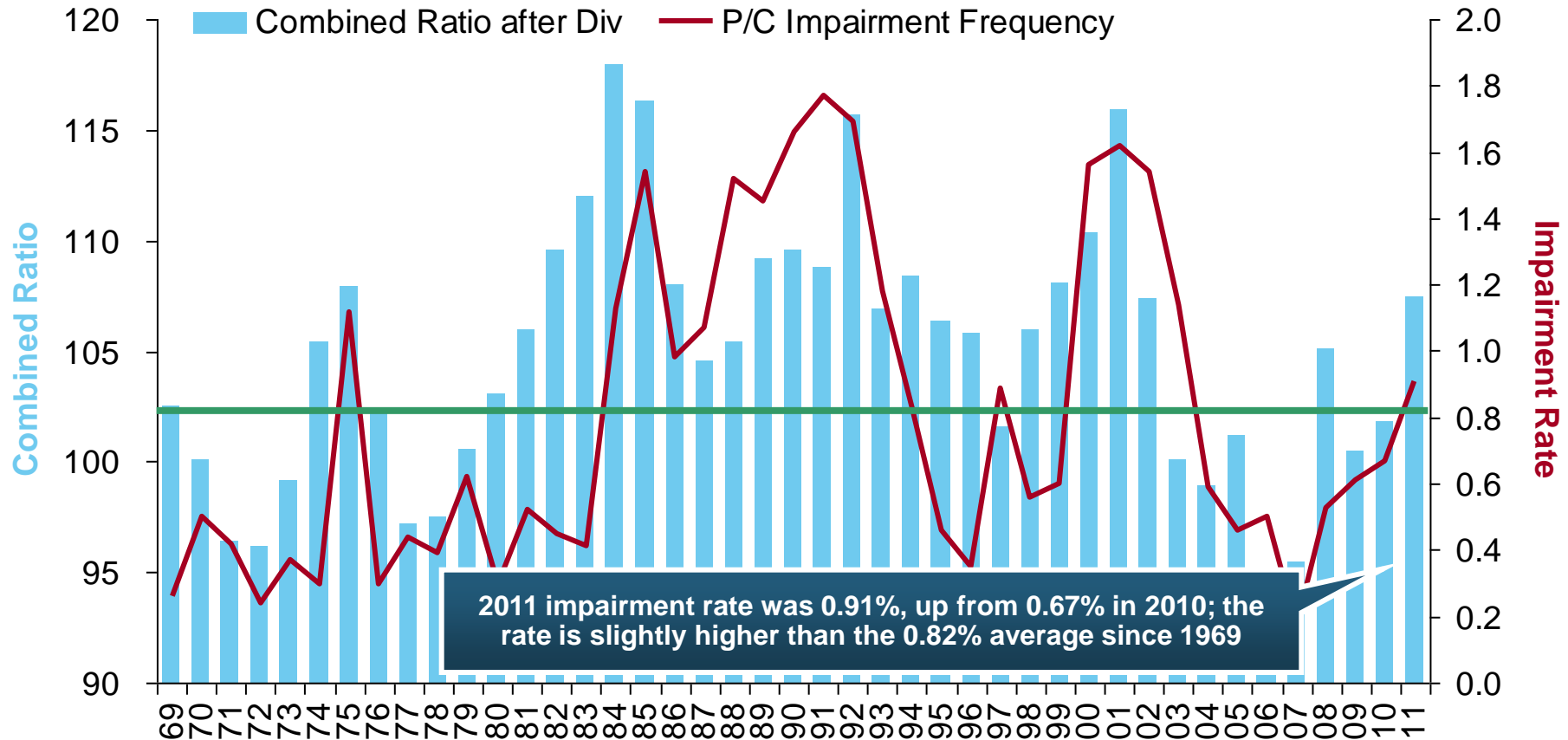
**Cyclical Pattern is P-C Impairment
History is Directly Tied to
Underwriting, Reserving & Pricing**

P/C Insurer Impairments, 1969–2011



The Number of Impairments Varies Significantly Over the P/C Insurance Cycle, With Peaks Occurring Well into Hard Markets

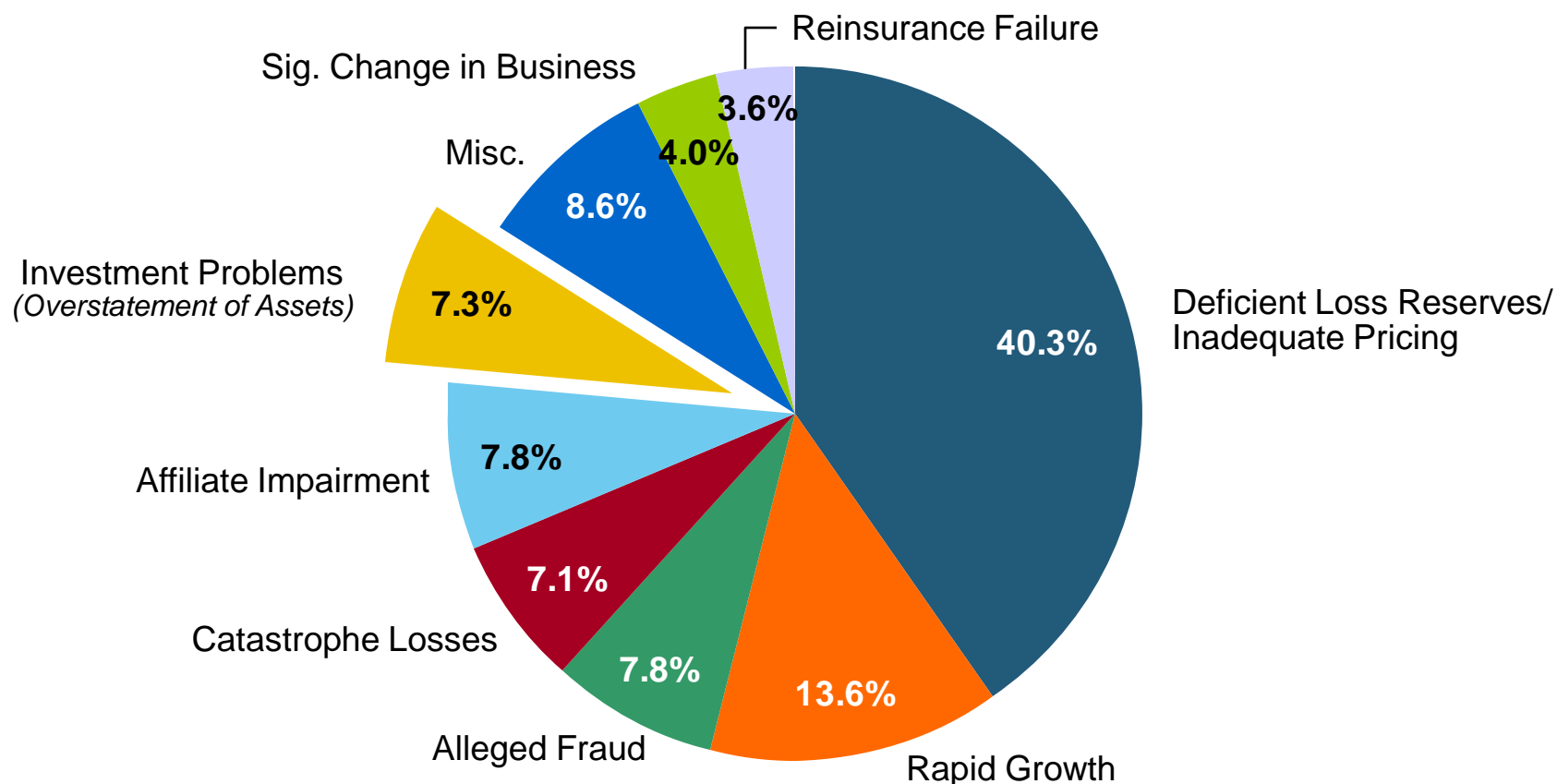
P/C Insurer Impairment Frequency vs. Combined Ratio, 1969-2011



Impairment Rates Are Highly Correlated With Underwriting Performance and Reached Record Lows in 2007; Recent Increase Was Associated Primarily With Mortgage and Financial Guaranty Insurers and Not Representative of the Industry Overall

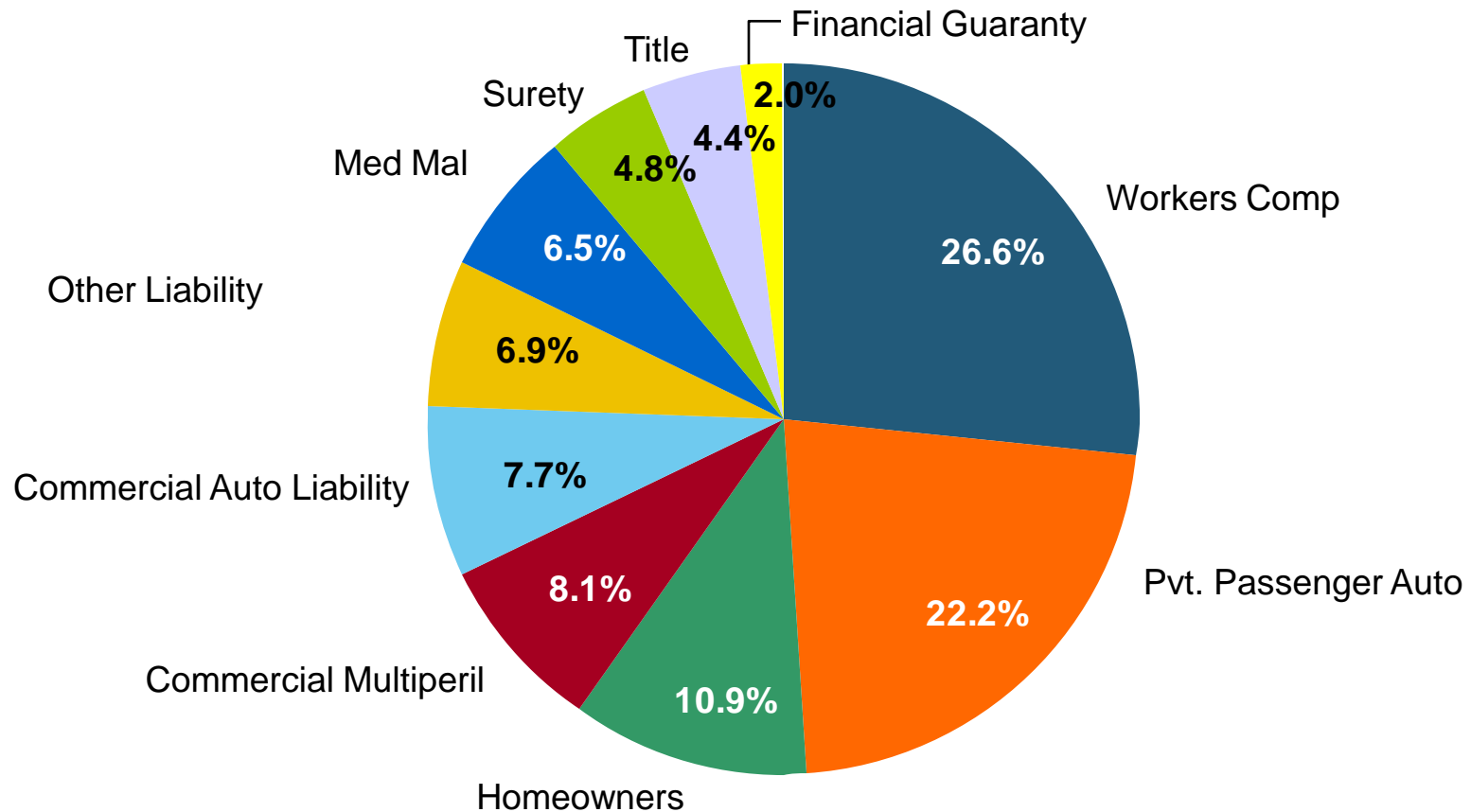
Reasons for US P/C Insurer Impairments, 1969–2010

Historically, Deficient Loss Reserves and Inadequate Pricing Are By Far the Leading Cause of P-C Insurer Impairments. Investment and Catastrophe Losses Play a Much Smaller Role



Top 10 Lines of Business for US P/C Impaired Insurers, 2000–2010

Workers Comp and Pvt. Passenger Auto Account for Nearly Half of the Premium Volume of Impaired Insurers Over the Past Decade



SURPLUS/CAPITAL/CAPACITY

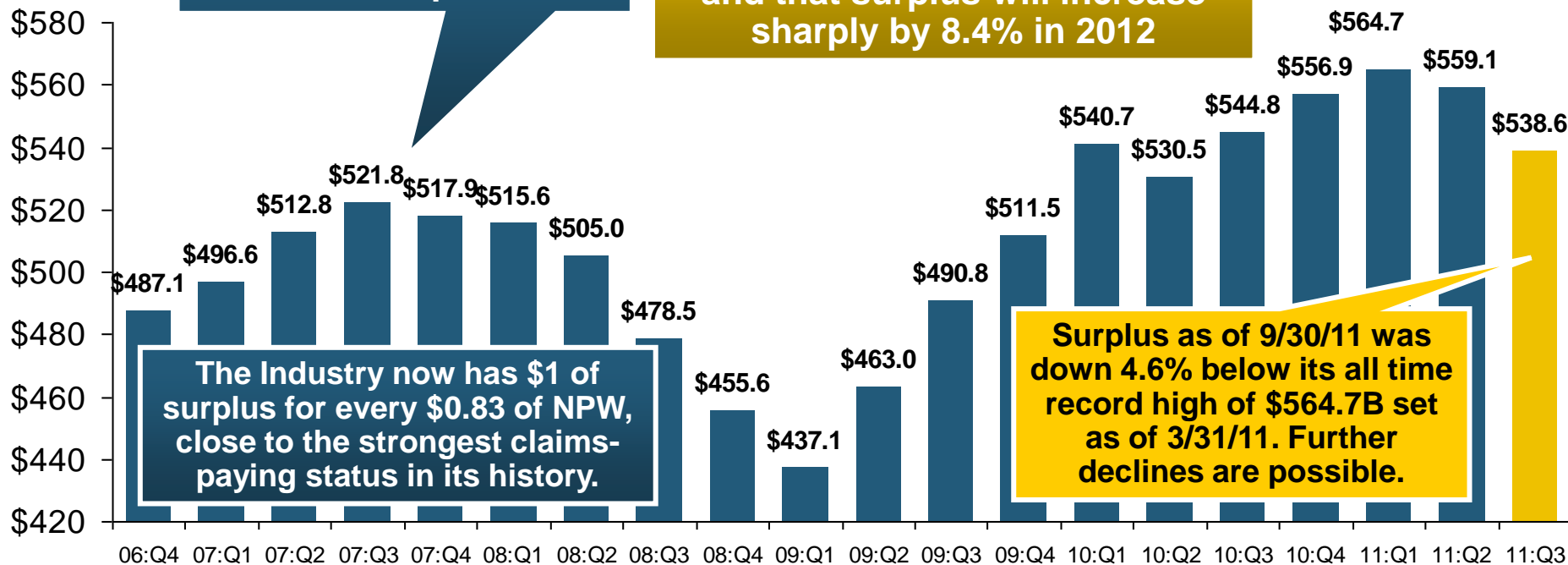
**Have Large Global Losses Reduced
Capacity in the Industry, Setting
the Stage for a Market Turn?**

Policyholder Surplus, 2006:Q4–2011:Q3

(\$ Billions)

2007:Q3
Previous Surplus Peak

A.M. Best is predicting year-end 2011 surplus was down just 1.7% and that surplus will increase sharply by 8.4% in 2012



The Industry now has \$1 of surplus for every \$0.83 of NPW, close to the strongest claims-paying status in its history.

Surplus as of 9/30/11 was down 4.6% below its all time record high of \$564.7B set as of 3/31/11. Further declines are possible.

Quarterly Surplus Changes Since 2011:Q1 Peak

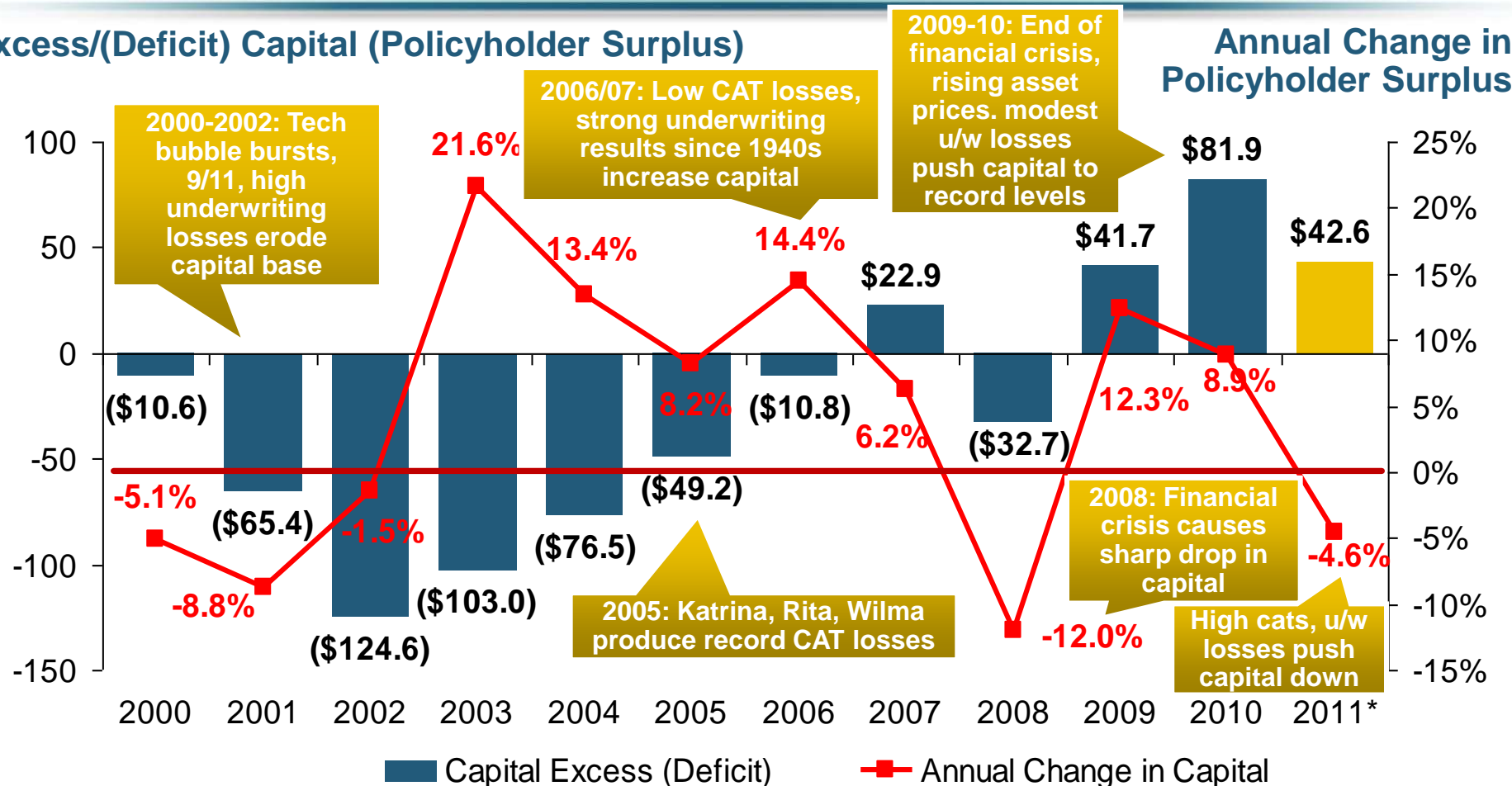
11:Q2: **-\$5.6B (-1.0%)**

11:Q3: **-\$26.1B (-4.6%)**

*Includes \$22.5B of paid-in capital from a holding company parent for one insurer's investment in a non-insurance business in early 2010.

Implied Excess (Deficit) Capital Assuming Premium/Surplus Ratio = 0.9:1

Excess/(Deficit) Capital (Policyholder Surplus)



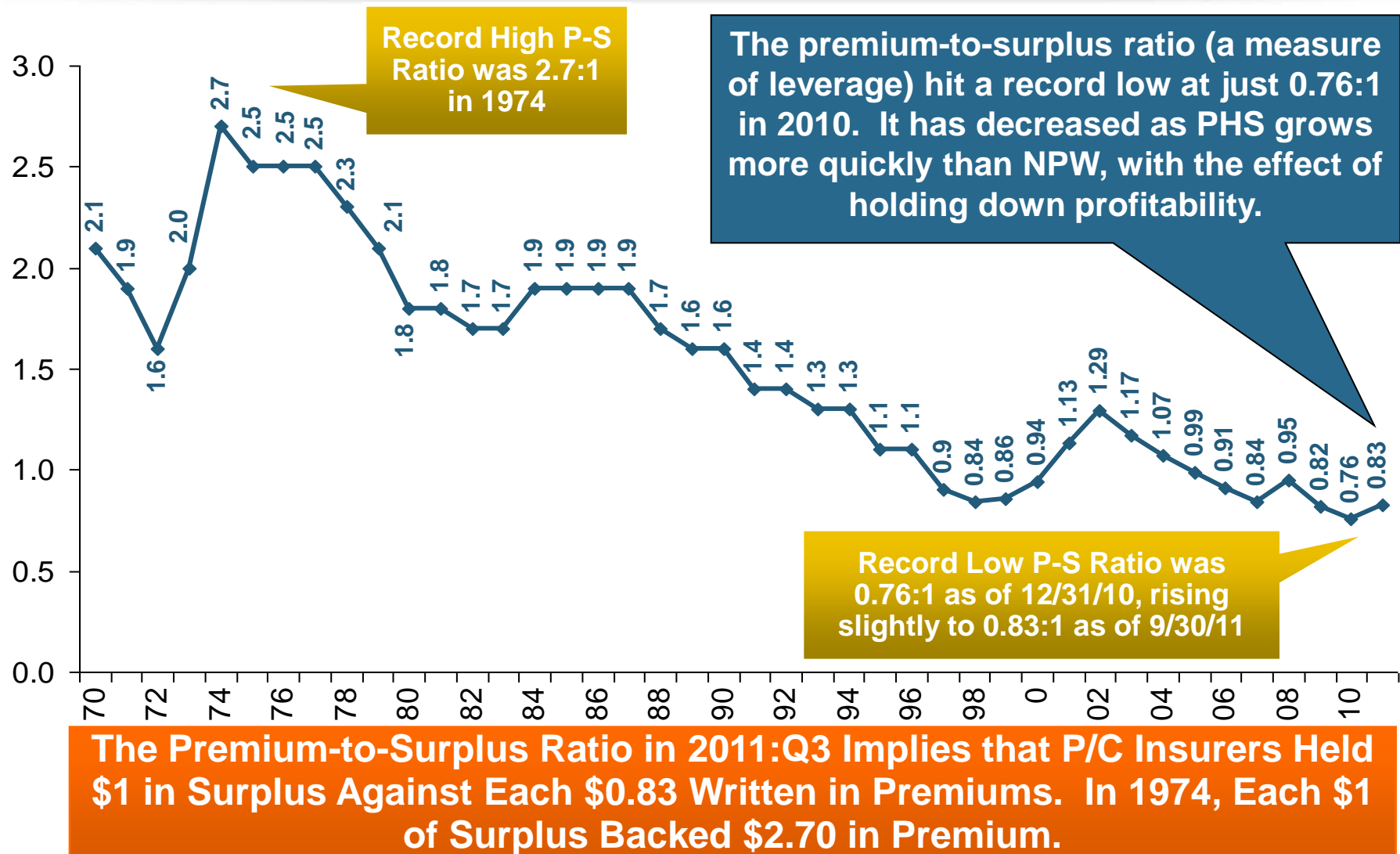
Record Policyholder Surplus (Capital) Resulted in Significant Excess Capital in the P/C Insurance Sector in 2010. Deteriorating Underwriting Losses, Higher CAT Activity, More Modest Market Returns Shrank Excess Capital in 2011 by Nearly Half.

Note: The assumption of a 0.9:1 P/S ratio is derived from a Feb. 2011 announcement by Advisen, Ltd., that the US P/C insurance industry has \$74 billion in excess capital. The implied P/S ratio (calculated by III) is 0.88:1, which was rounded to 0.9:1.

Source: Insurance Information Institute calculations from A.M. Best and ISO data.

* Net Premiums Written 37

Ratio of Net Premiums Written to Policyholder Surplus, 1970-2011*



*2011 data are as of 9/30/11.

Sources: Insurance Information Institute calculations from A.M. Best data.

INVESTMENTS: THE NEW REALITY

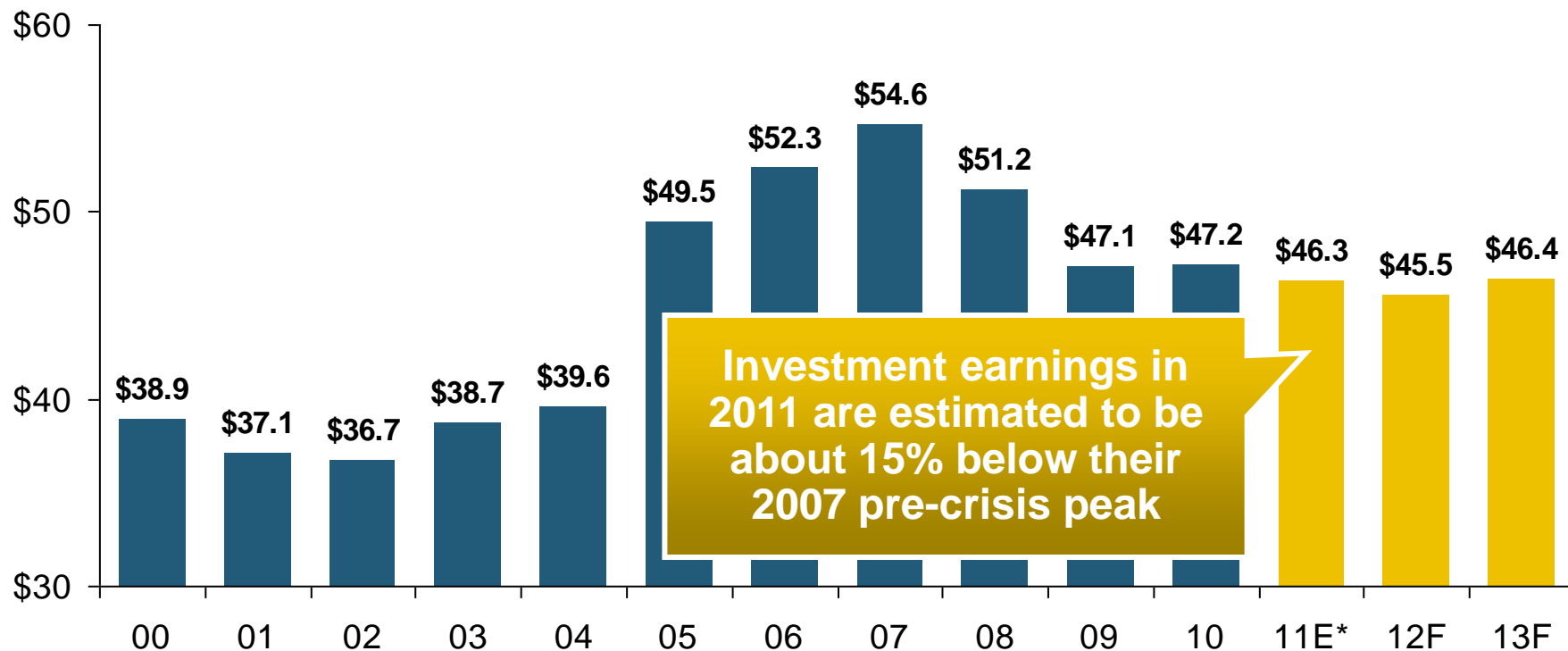
**Investment Performance is a
Key Driver of Profitability
*Does It Influence
Underwriting or Cyclicalities?***

Insurers Have Not Yet Fully Adapted to a Persistently Low Interest Rate Environment

- **No Expectation that Rates Would Be:**
 - ◆ **Pushed to Such Low Levels**
 - ◆ **Pushed Down so Rapidly**
 - ◆ **Held to Such Low Levels for So Long**
 - ◆ **Suppressed via Unprecedented Aggressiveness of the Federal Reserve**
 - **Use of traditional and unconventional tools (QE)**
 - **Unconventional 's policies couldn't be anticipated, esp. QE1, 2 (3?)**
- **Competitive Pressure→Protracted Soft Market**
- **Ability to Release Prior Reserves Eases Urgency**
- **Realization of Capital Gains**

Property/Casualty Insurance Industry Investment Income: 2000–2013F¹

(\$ Billions)



Investment Income in 2011 Was Surprisingly Strong, Though Investment Income Is Likely to Weaken in 2012 Due to Persistently Low Interest Rates

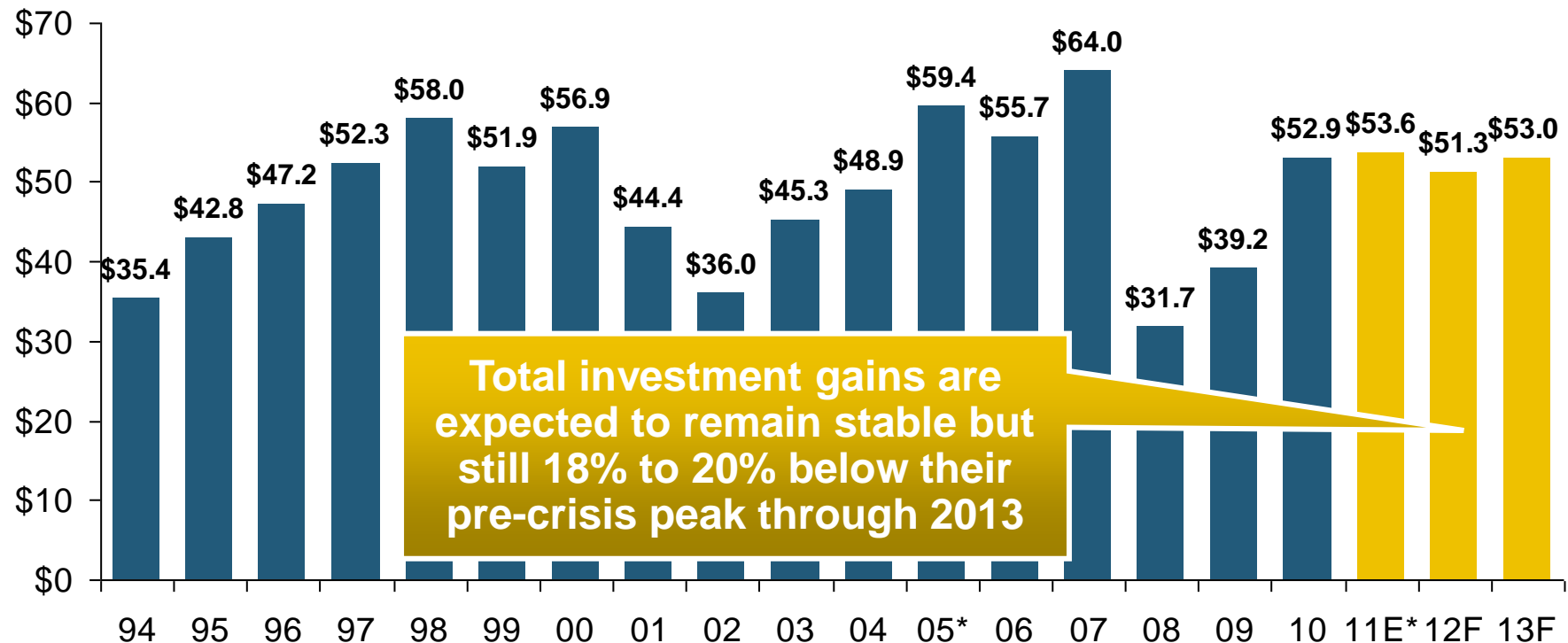
¹ Investment gains consist primarily of interest and stock dividends.

*2011E figure is annualized based on actual investment income through 2011:Q3; 2012F-2013F based on Conning projections.

Sources: ISO; Conning Research & Consulting; Insurance Information Institute.

Property/Casualty Insurance Industry Investment Gain: 1994–2013F¹

(\$ Billions)



Investment Gains in 2011 Were Surprisingly Robust. Investment Gains Recovered Significantly Due to Realized Investment Gains; The Financial Crisis Caused Investment Gains to Fall by 50% in 2008

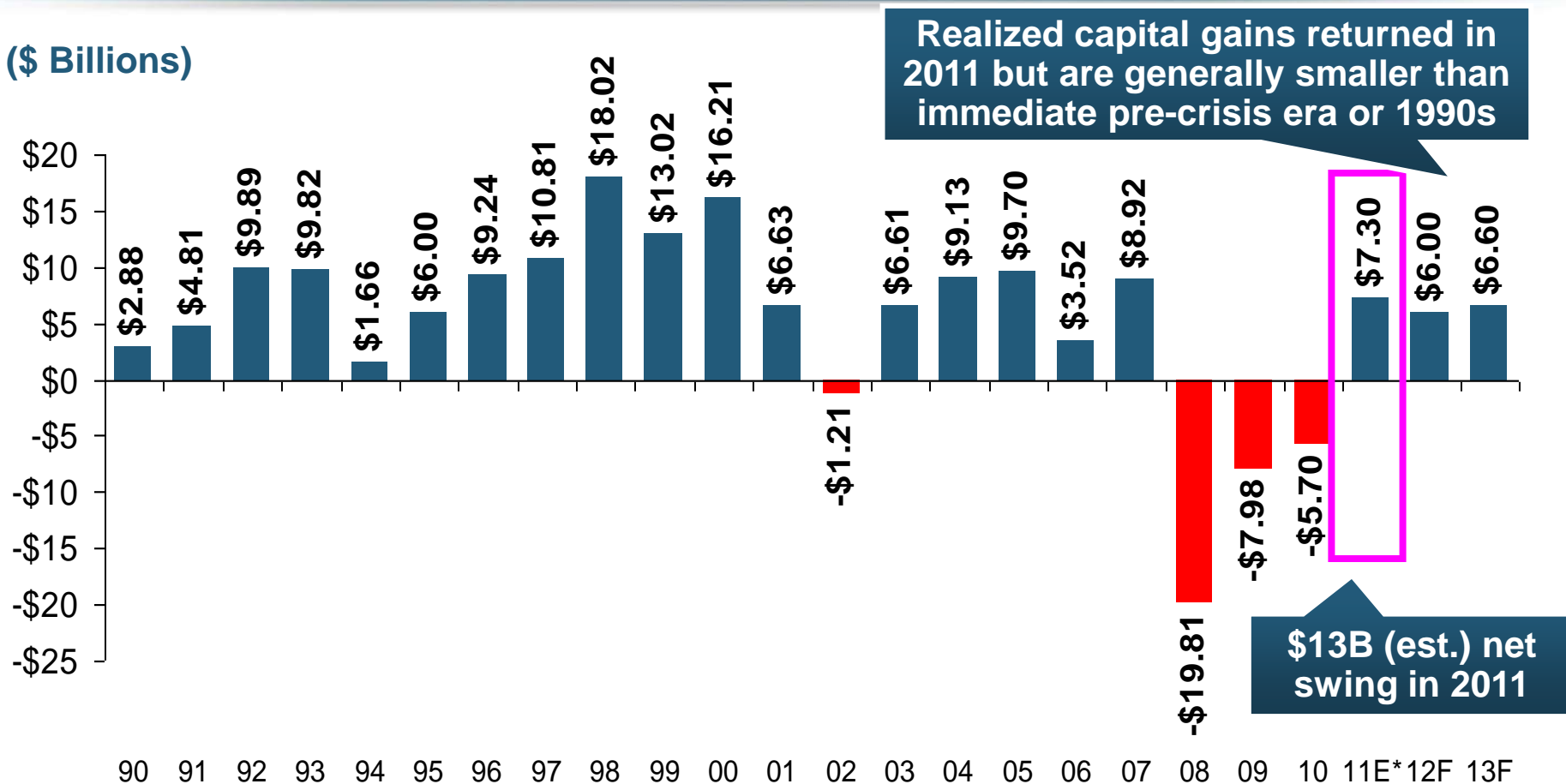
¹ Investment gains consist primarily of interest, stock dividends and realized capital gains and losses.

* 2005 figure includes special one-time dividend of \$3.2B; 2011 figure is annualized based 2011:Q3 actual; 2012-13F derived from Conning forecast data.

Sources: ISO; Conning; Insurance Information Institute.

P/C Insurer Net Realized Capital Gains/Losses, 1990-2013F

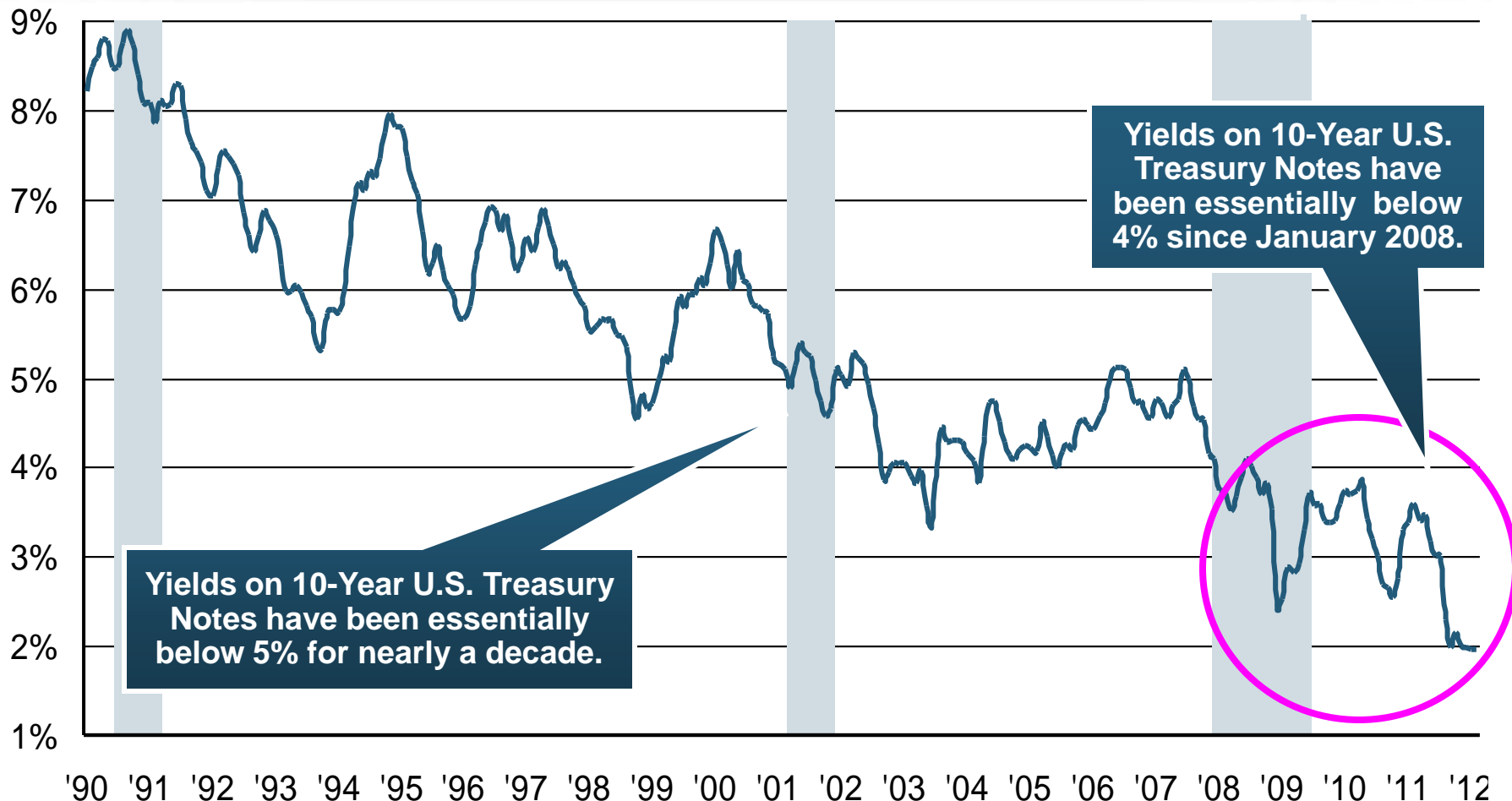
(\$ Billions)



Insurers Posted Net Realized Capital Gains in 2011 for the First Time Since 2007. Realized Capital Losses Were a Primary Cause of 2008/2009's Large Drop in Profits and ROE

*2011 is an estimate based on annualized actual 2011 9-month figure of \$5.5B; 2012F and 2013F are Conning estimates.
Sources: A.M. Best, ISO, Conning; Insurance Information Institute.

U.S. 10-Year Treasury Note Yields: A Long Downward Trend, 1990–2012*



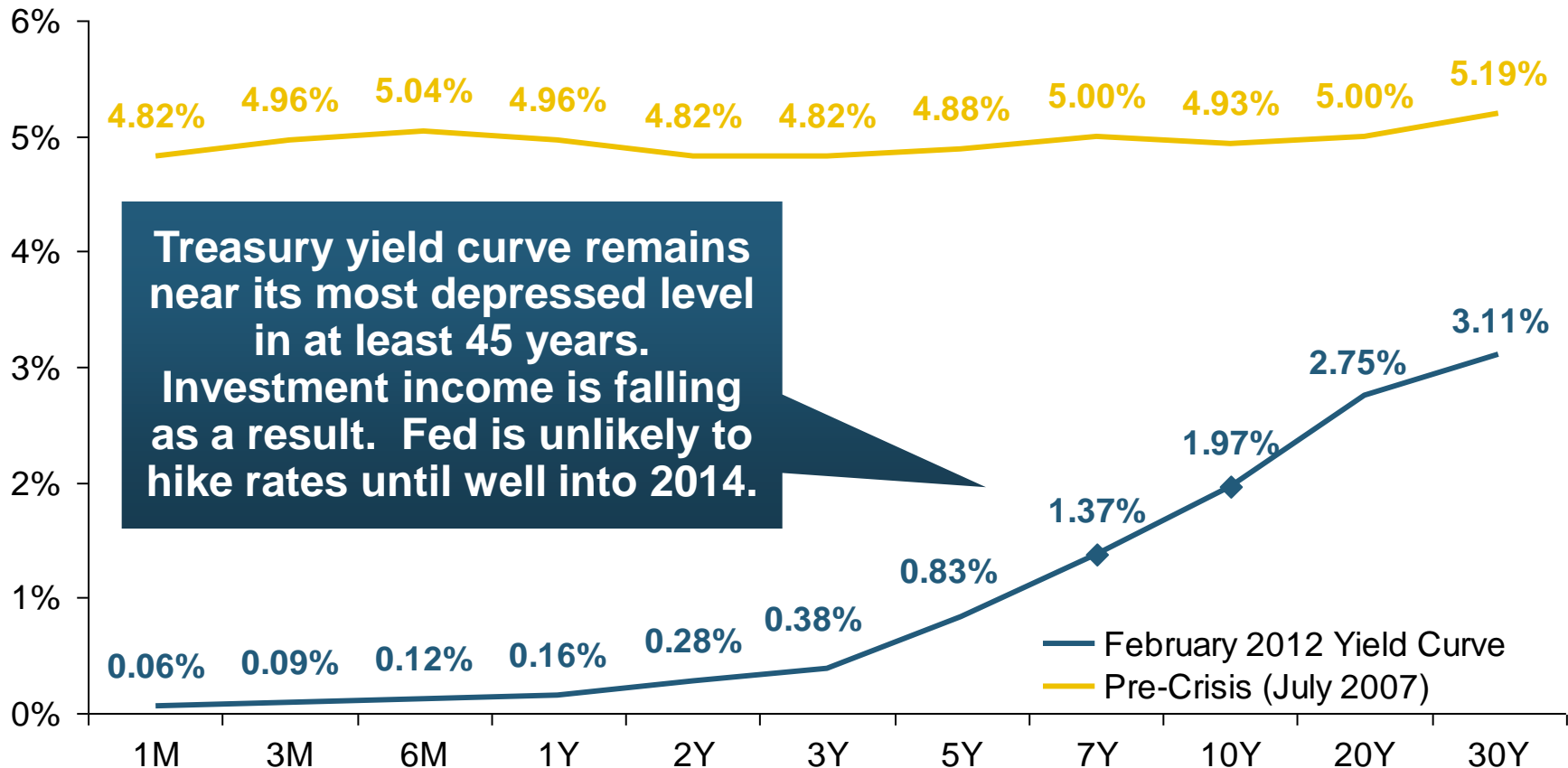
Since roughly 80% of P/C bond/cash investments are in 10-year or shorter durations, most P/C insurer portfolios will have low-yielding bonds for years to come.

*Monthly, through February 2012.

Note: Recessions indicated by gray shaded columns.

Sources: Federal Reserve Bank at http://www.federalreserve.gov/releases/h15/data/Monthly/H15_TCMNOM_Y10.txt
National Bureau of Economic Research (recession dates); Insurance Information Institutes.

Treasury Yield Curves: Pre-Crisis (July 2007) vs. Feb. 2012



The Fed Is Actively Signaling that it Is Determined to Keep Rates Low Through Late 2014

Reduction in Combined Ratio Necessary to Offset 1% Decline in Investment Yield to Maintain Constant ROE, by Line*



Lower Investment Earnings Place a Greater Burden on Underwriting and Pricing Discipline

*Based on 2008 Invested Assets and Earned Premiums

**US domestic reinsurance only

Source: A.M. Best; Insurance Information Institute.

Performance by Segment: Commercial Lines

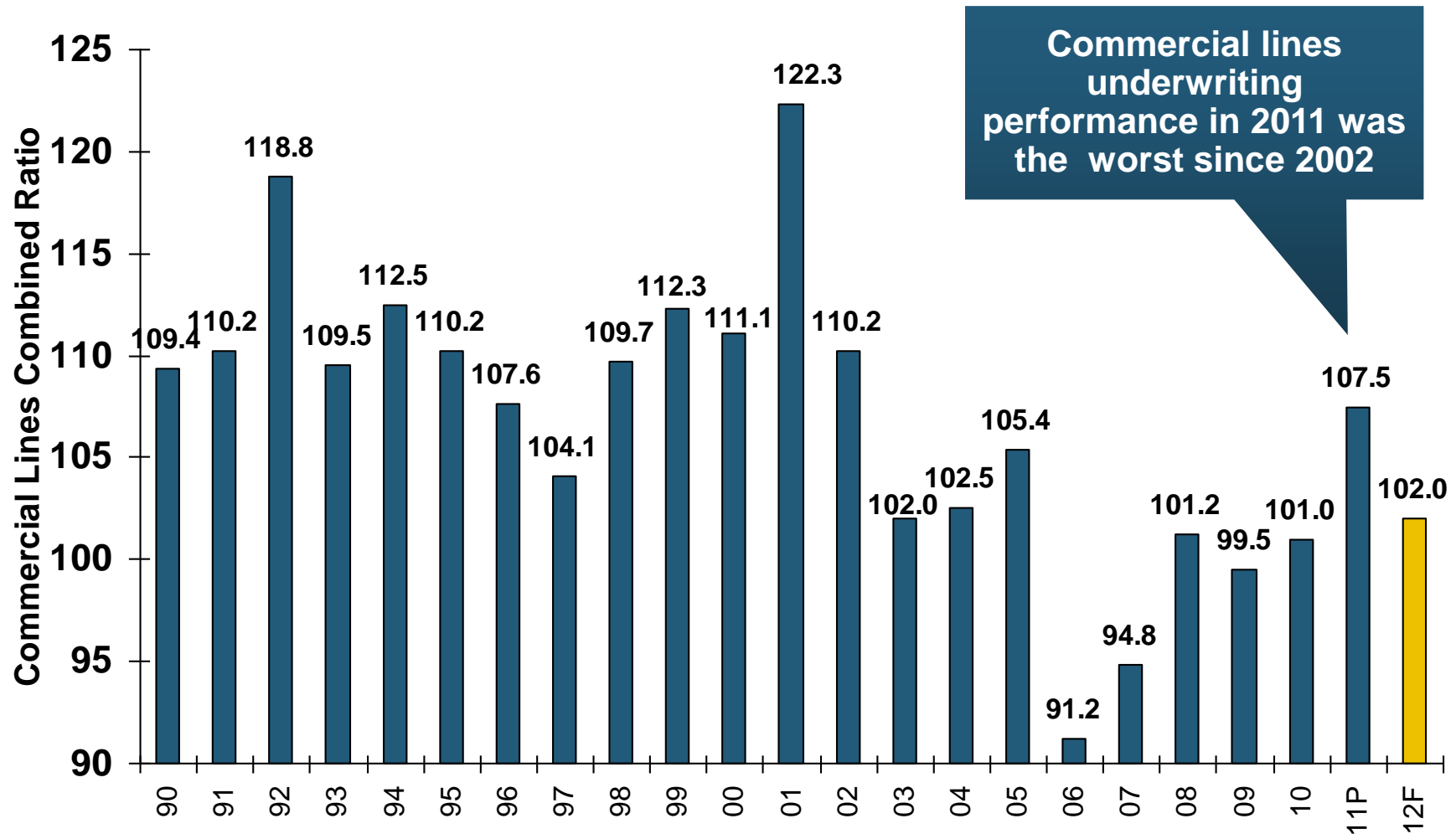
A.M. Best Commercial Lines Outlook: Negative (as of January 2012)

- **Underwriting Margins Pressured**
 - ◆ Will recent rate increases hold?
- **Loss Reserve Redundancies Fade**
- **Historically Low Investment Yields**

OFFSETTING FACTORS

- **Capitalization Still Solid**
- **Emergence of Sophisticated Price Monitoring and Underwriting Tools**

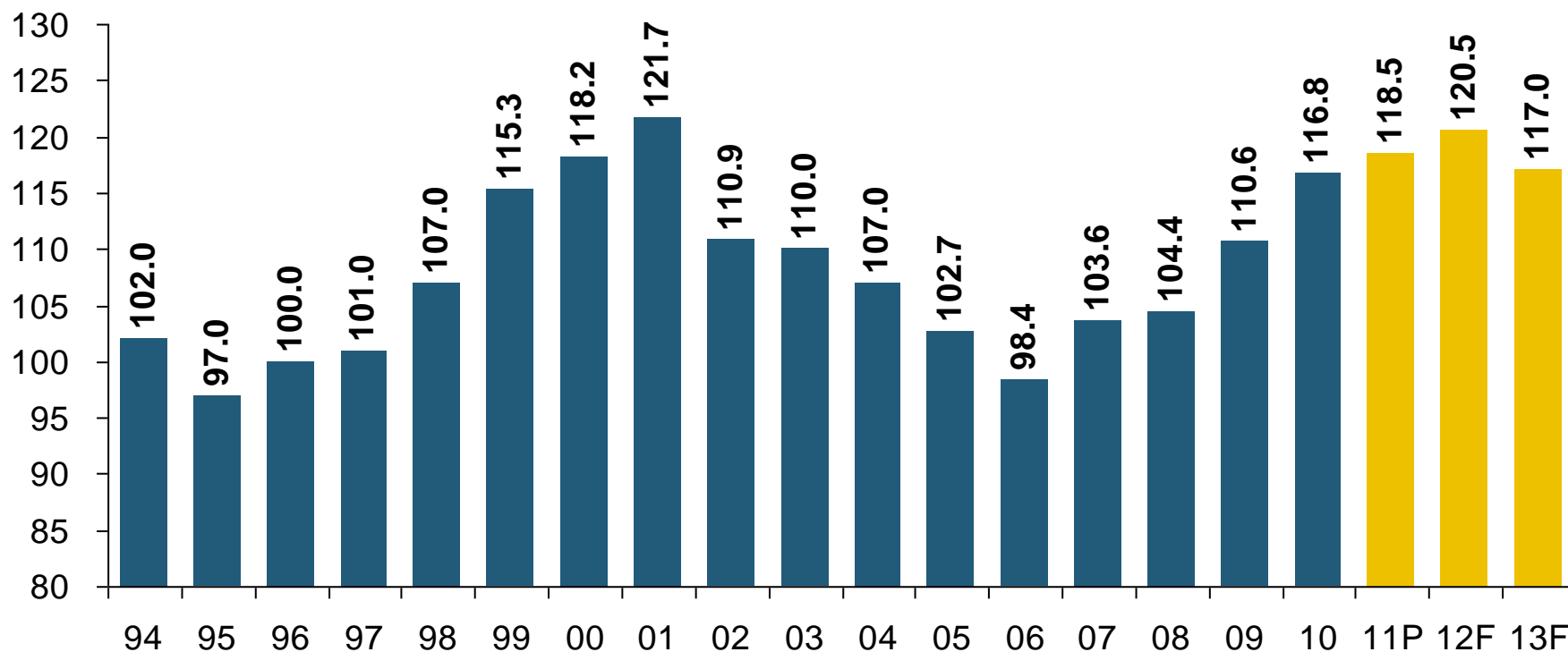
Commercial Lines Combined Ratio, 1990-2012F*



*2007-2012 figures exclude mortgage and financial guaranty segments.

Source: A.M. Best; Insurance Information Institute

Workers Compensation Combined Ratio: 1994–2013F

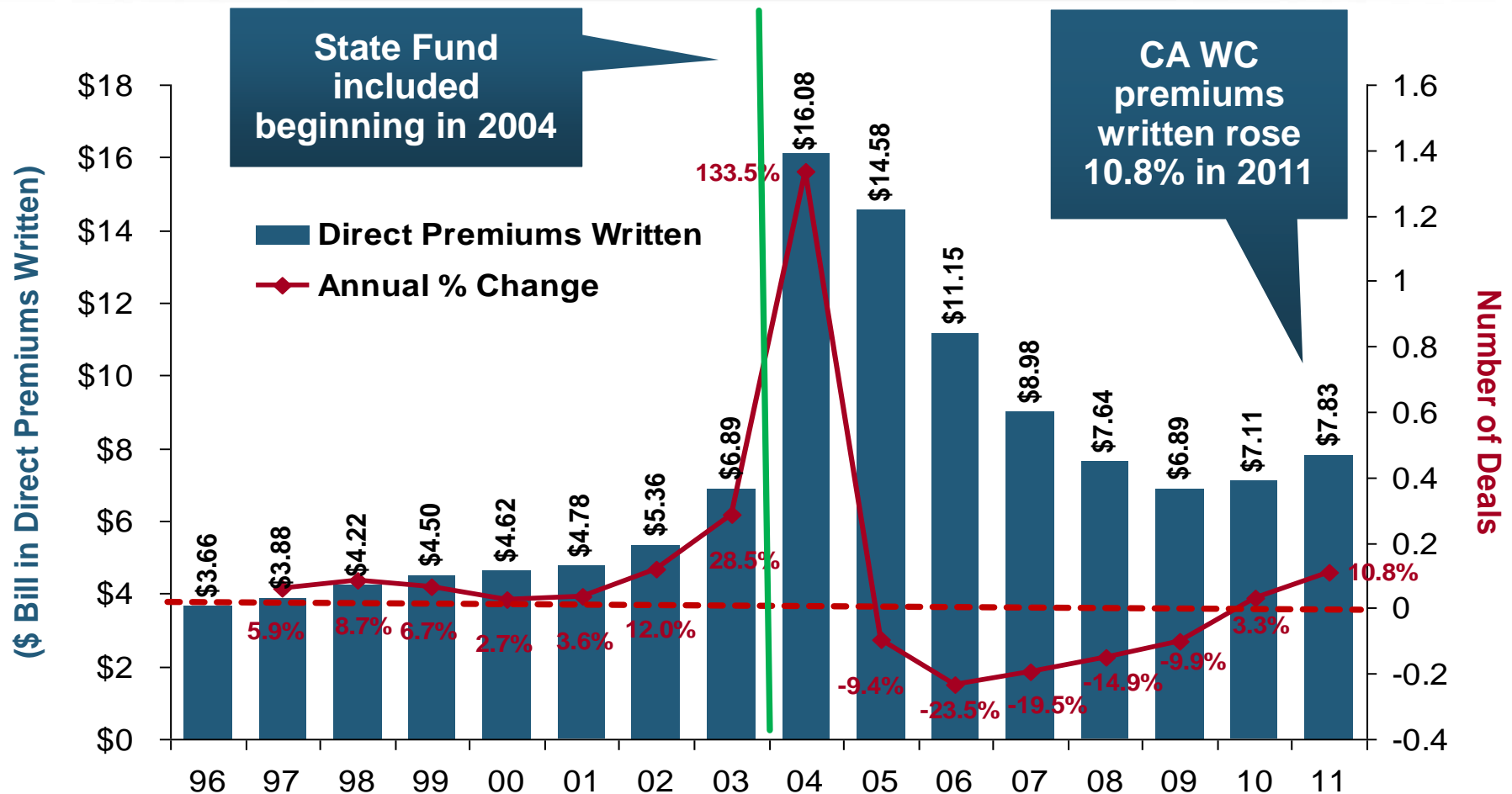


Workers Comp Underwriting Results Are Deteriorating Markedly and the Worst They Have Been in a Decade

Workers Compensation Operating Environment

**The Weak Economy and Soft Market Have
Made the Workers Comp Operating
Increasingly Challenging**

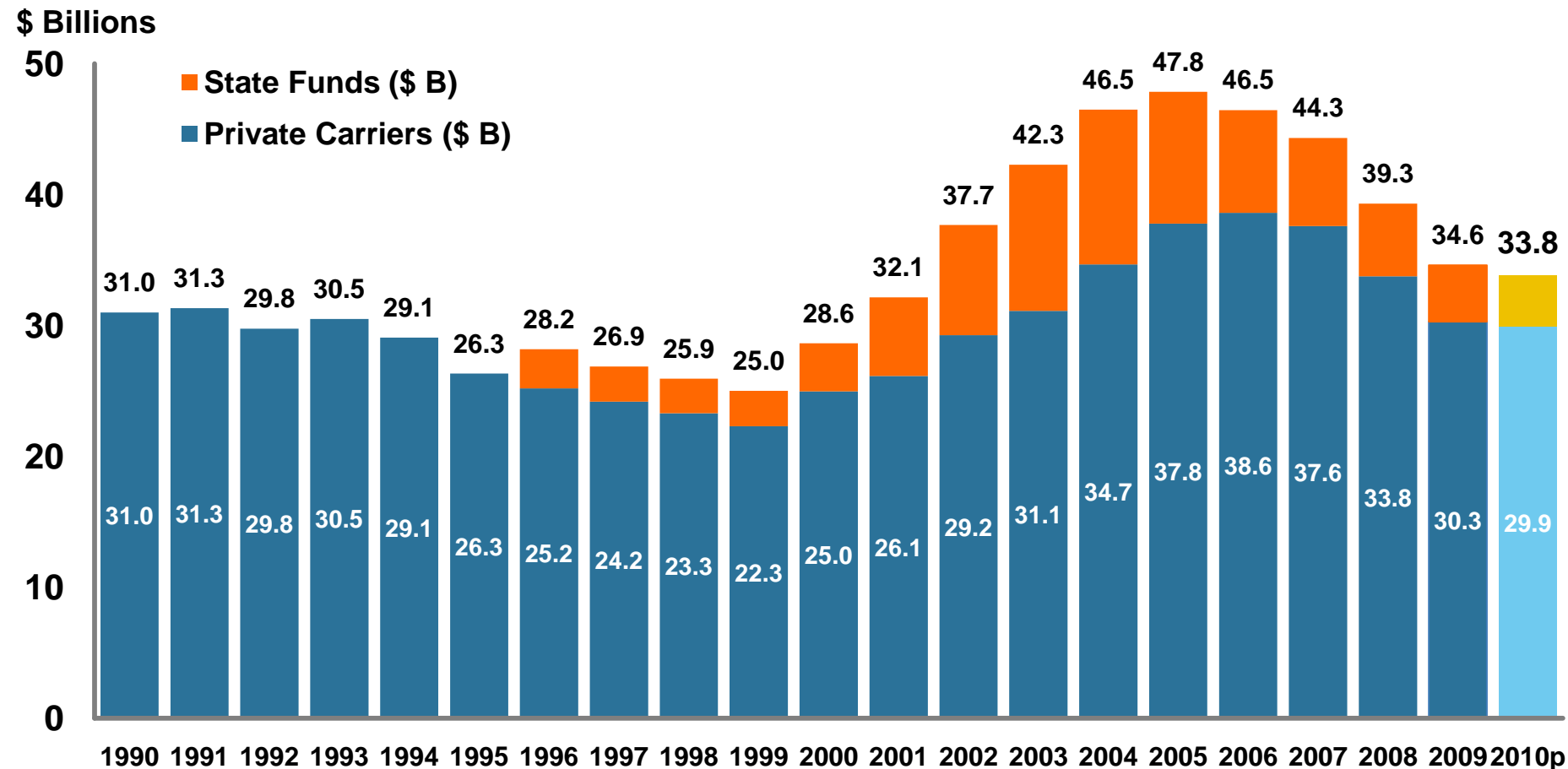
WC: Direct Premiums Written in California, 1996-2011(Incl. SCIF 2004-2011)



The Precipitous Decline in WC Premiums Written Has Ended With Growth Now Being Driven by Rate Actions and Improved Payroll Exposure Growth

Workers Compensation Premium Continues Its Sharp Decline

Net Written Premium



p Preliminary

Source: 1990–2009 Private Carriers, *Best's Aggregates & Averages*; 2010p, NCCI

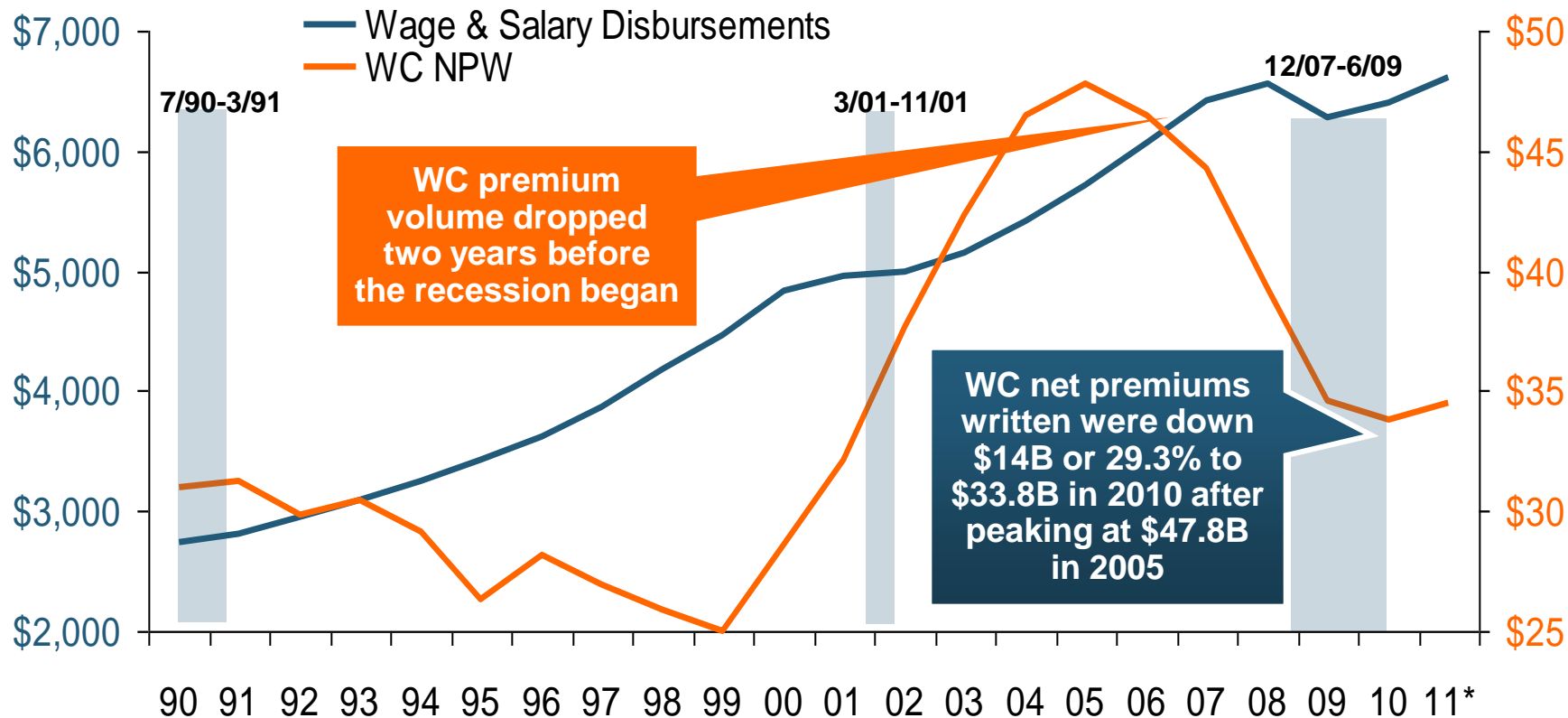
1996–2010p State Funds: AZ, CA, CO, HI, ID, KY, LA, MD, MO, MT, NM, OK, OR, RI, TX, UT Annual Statements

State Funds available for 1996 and subsequent

Payroll vs. Workers Comp Net Written Premiums, 1990-2011

Payroll Base*
\$Billions

WC NWP
\$Billions

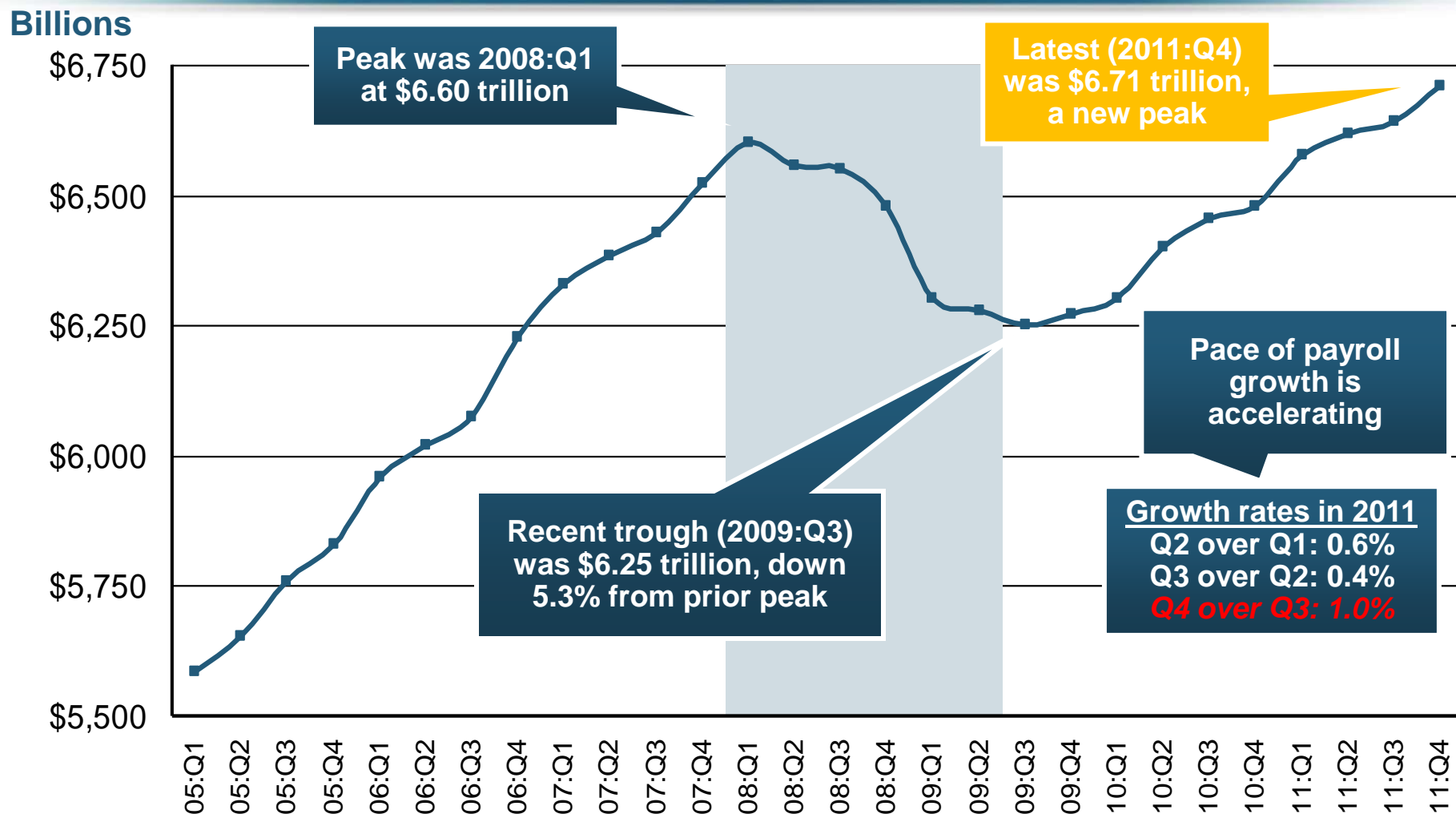


Resumption of payroll growth and rate increases suggests WC NWP will grow again in 2012

*Private employment; Shaded areas indicate recessions. Payroll and WC premiums for 2011 is I.I.I. estimate

Sources: NBER (recessions); Federal Reserve Bank of St. Louis at <http://research.stlouisfed.org/fred2/series/WASCUR> ; NCCI; I.I.I.

Nonfarm Payroll (Wages and Salaries): Quarterly, 2005–2011:Q4

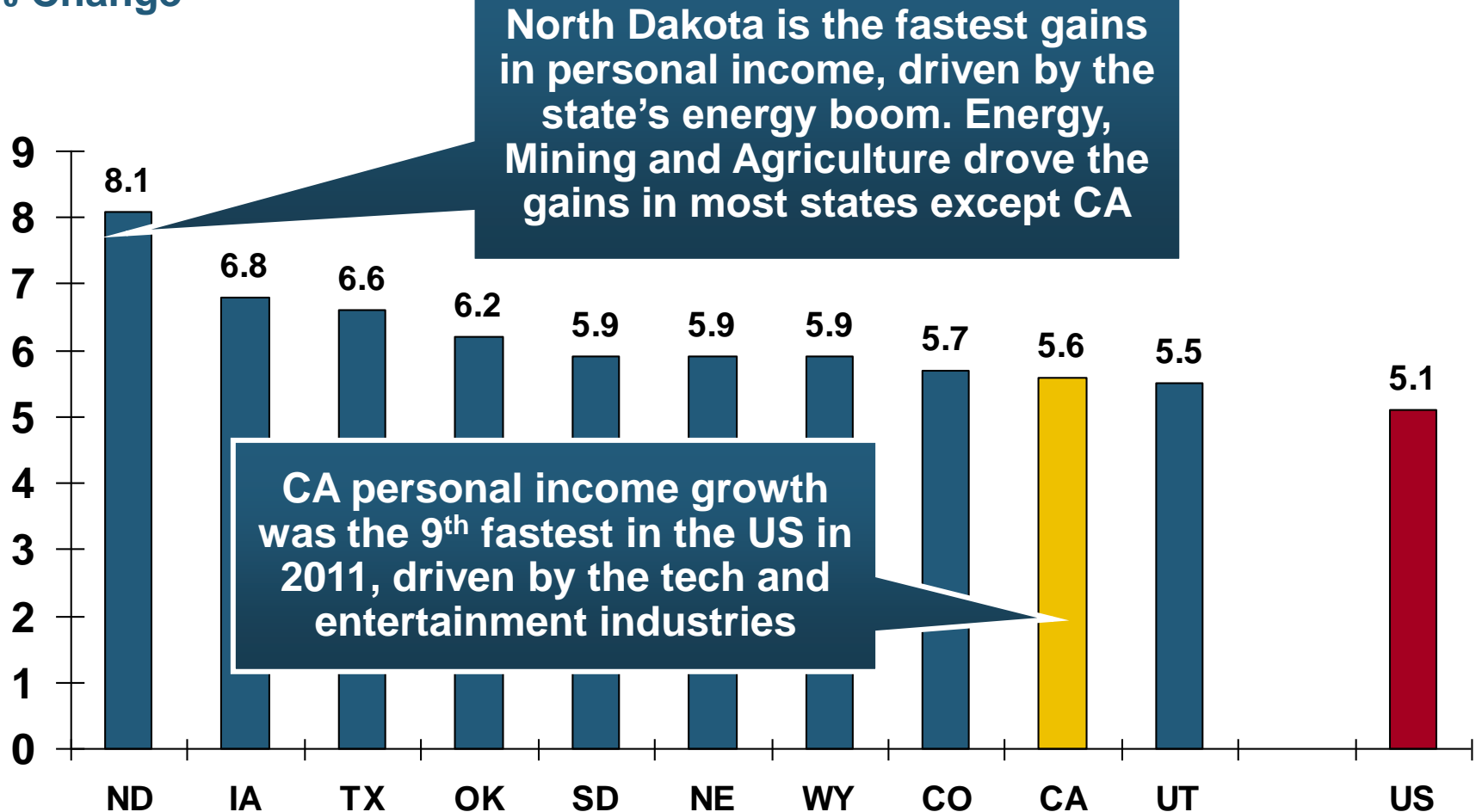


Note: Recession indicated by gray shaded column. Data are seasonally adjusted annual rates.

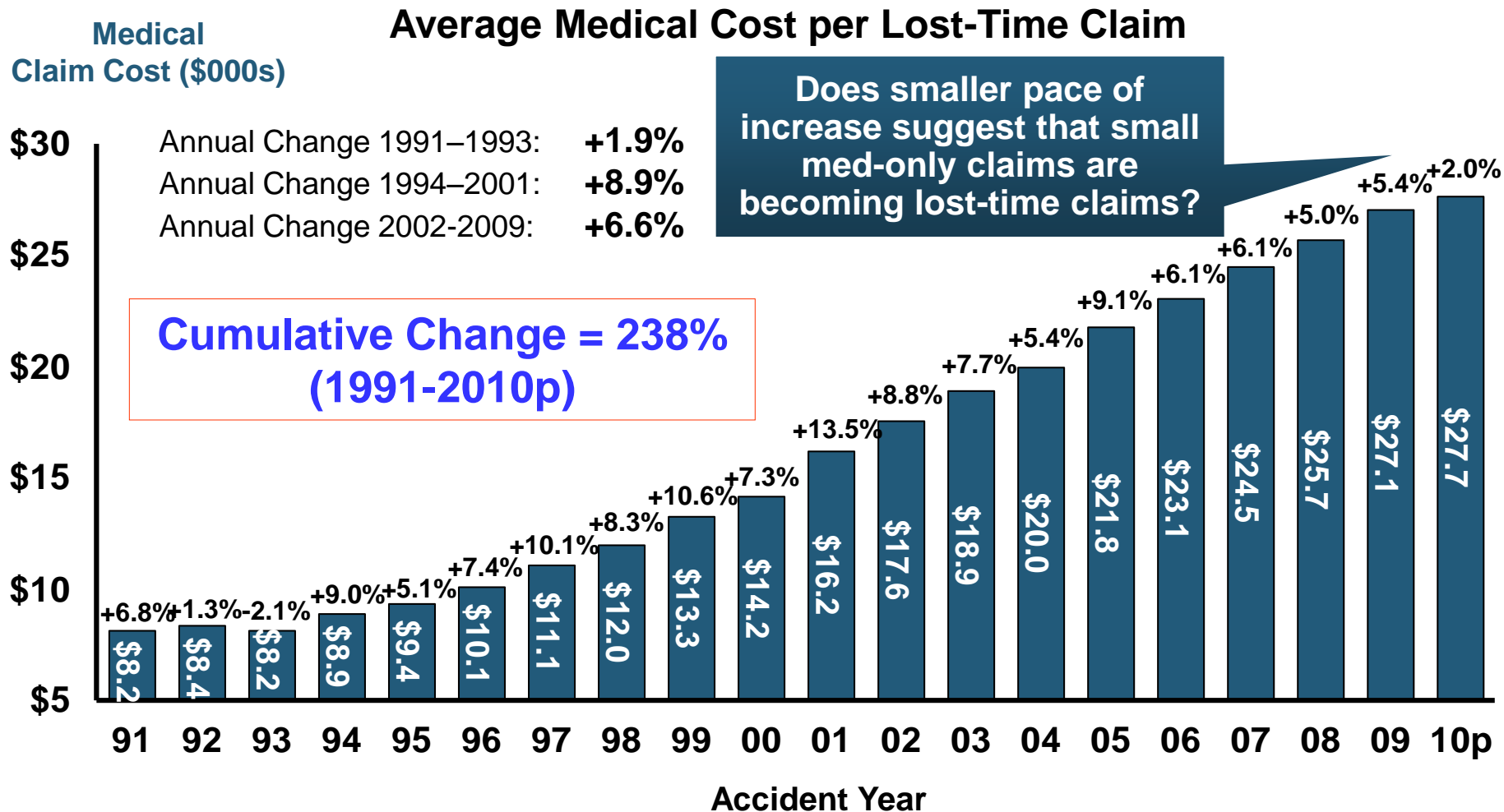
Sources: <http://research.stlouisfed.org/fred2/series/WASCUR>; National Bureau of Economic Research (recession dates); Insurance Information Institute.

Personal Income Growth in 2011: Top 10 States

% Change



Workers Comp Medical Claim Costs Continue to Rise



2010p: Preliminary based on data valued as of 12/31/2010

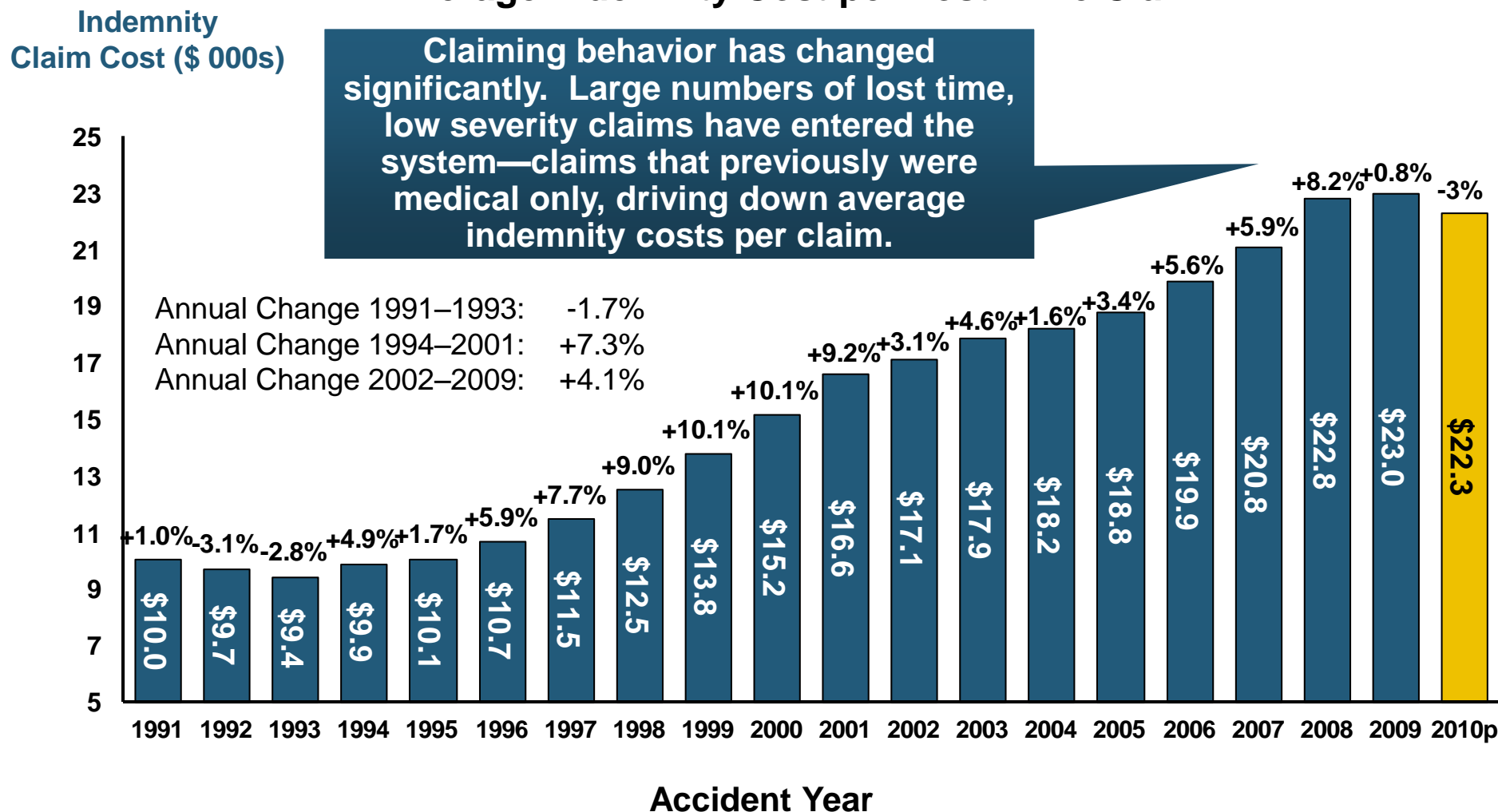
1991–2008: Based on data through 12/31/2008, developed to ultimate

Based on the states where NCCI provides ratemaking services; Excludes the effects of deductible policies

Workers Comp Indemnity Claim Costs Decline in 2010

Average Indemnity Cost per Lost-Time Claim

Claiming behavior has changed significantly. Large numbers of lost time, low severity claims have entered the system—claims that previously were medical only, driving down average indemnity costs per claim.



2010p: Preliminary based on data valued as of 12/31/2010

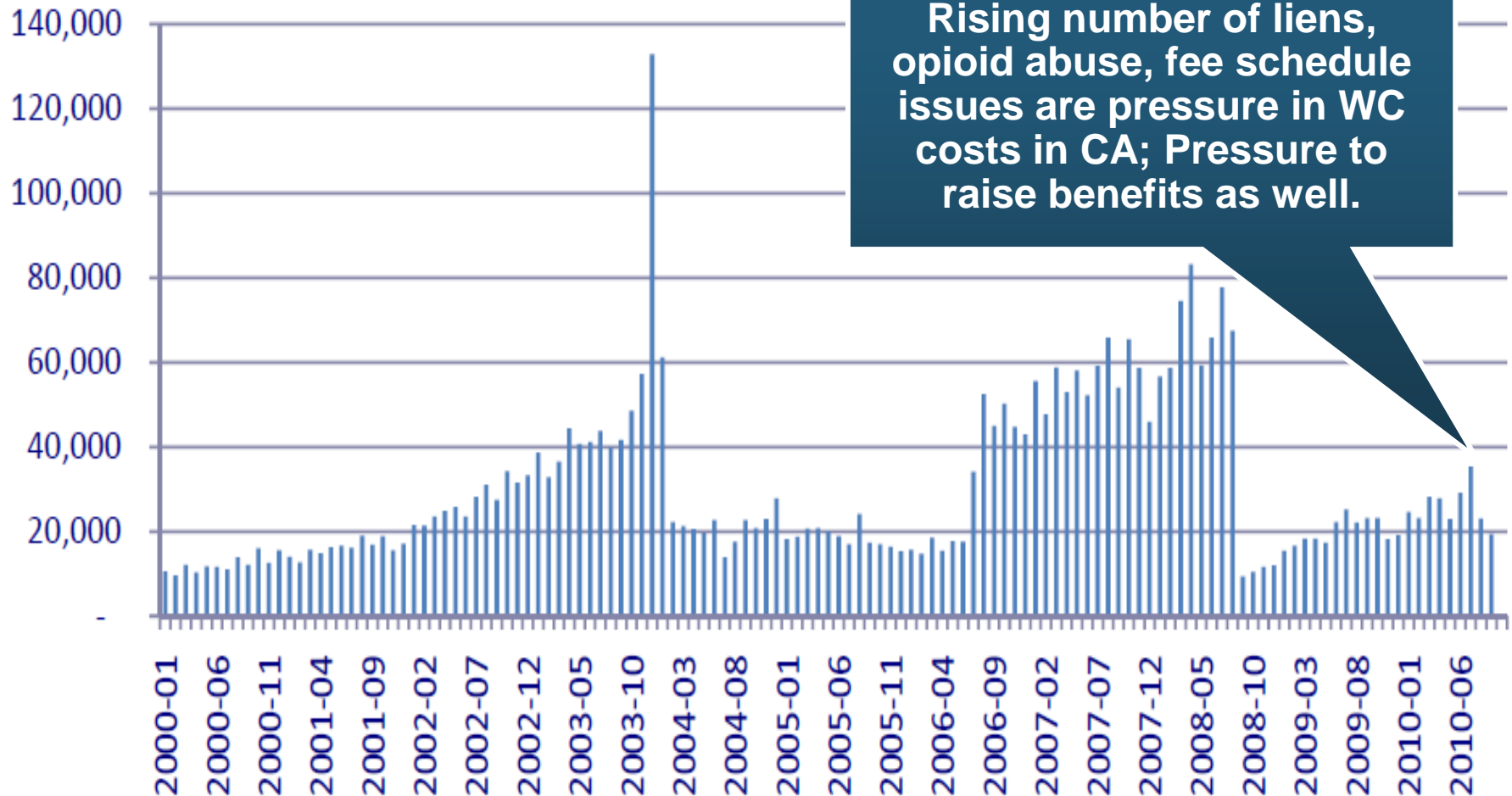
1991–2008: Based on data through 12/31/2008, developed to ultimate

Based on the states where NCCI provides ratemaking services

Excludes the effects of deductible policies

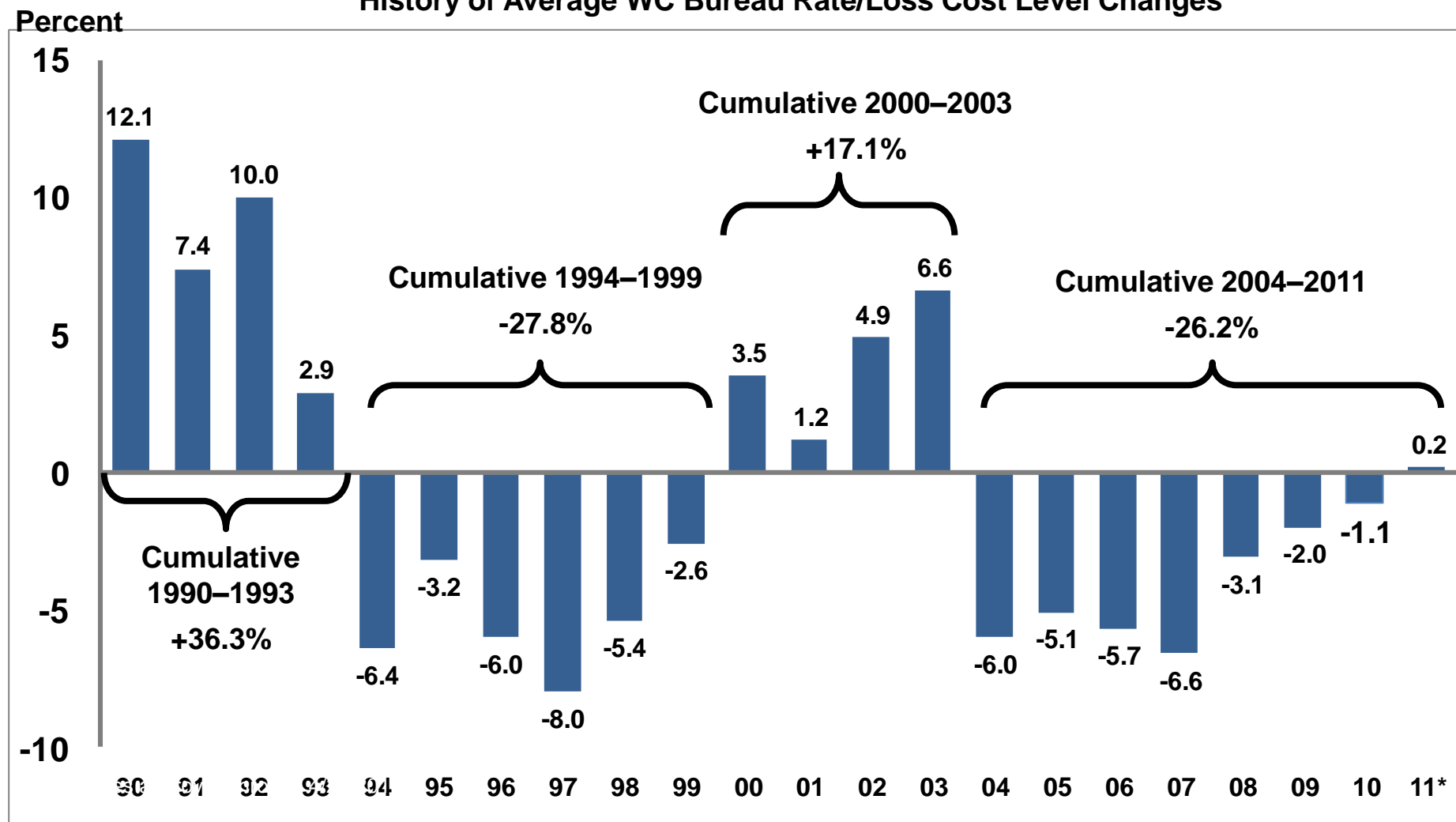
Number of Liens Filed per Month, Jan. 2000—Oct. 2010

The most recent months shown here have not been completely counted.



Average Approved Bureau Rates/Loss Costs

History of Average WC Bureau Rate/Loss Cost Level Changes



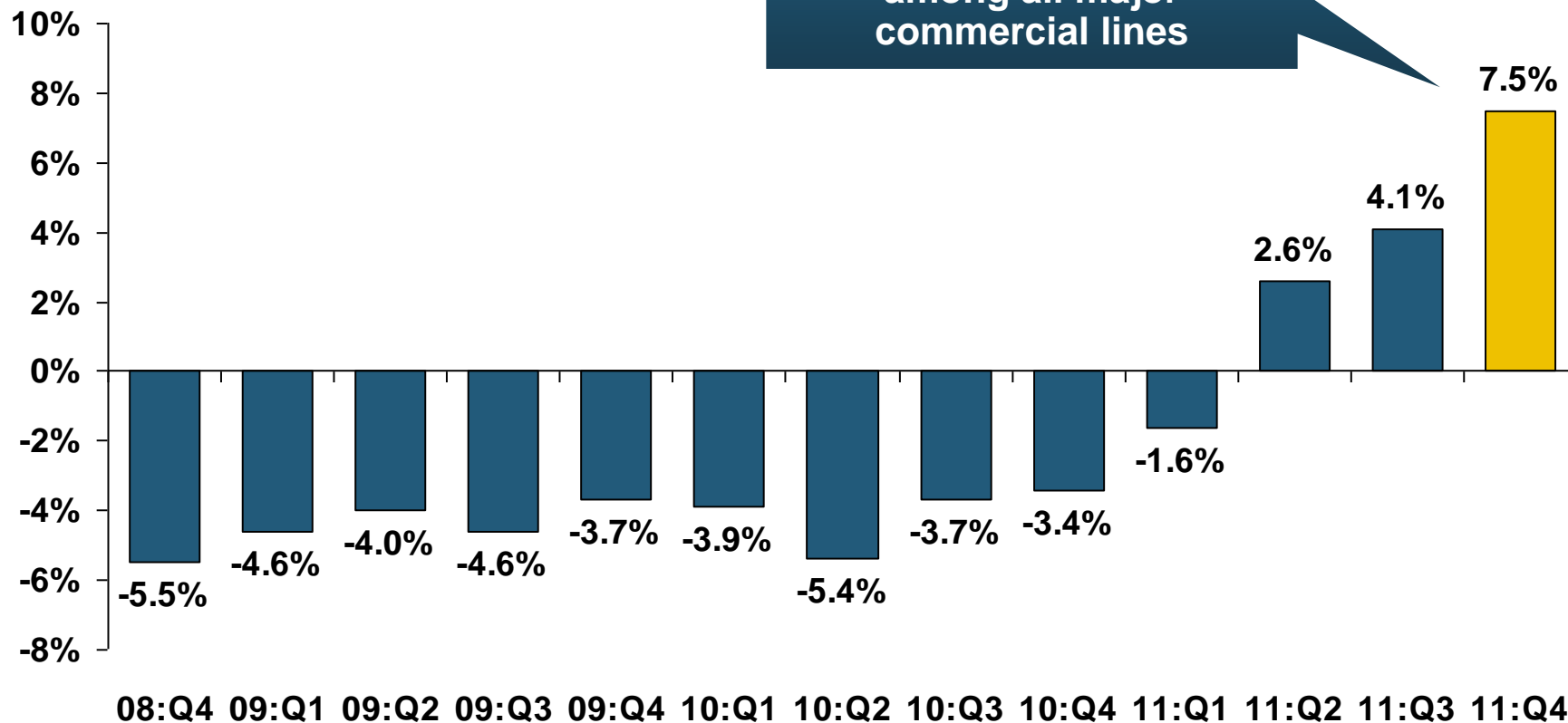
*States approved through 4/8/11.

Note: Countrywide approved changes in advisory rates, loss costs and assigned risk rates as filed by applicable rating organization.

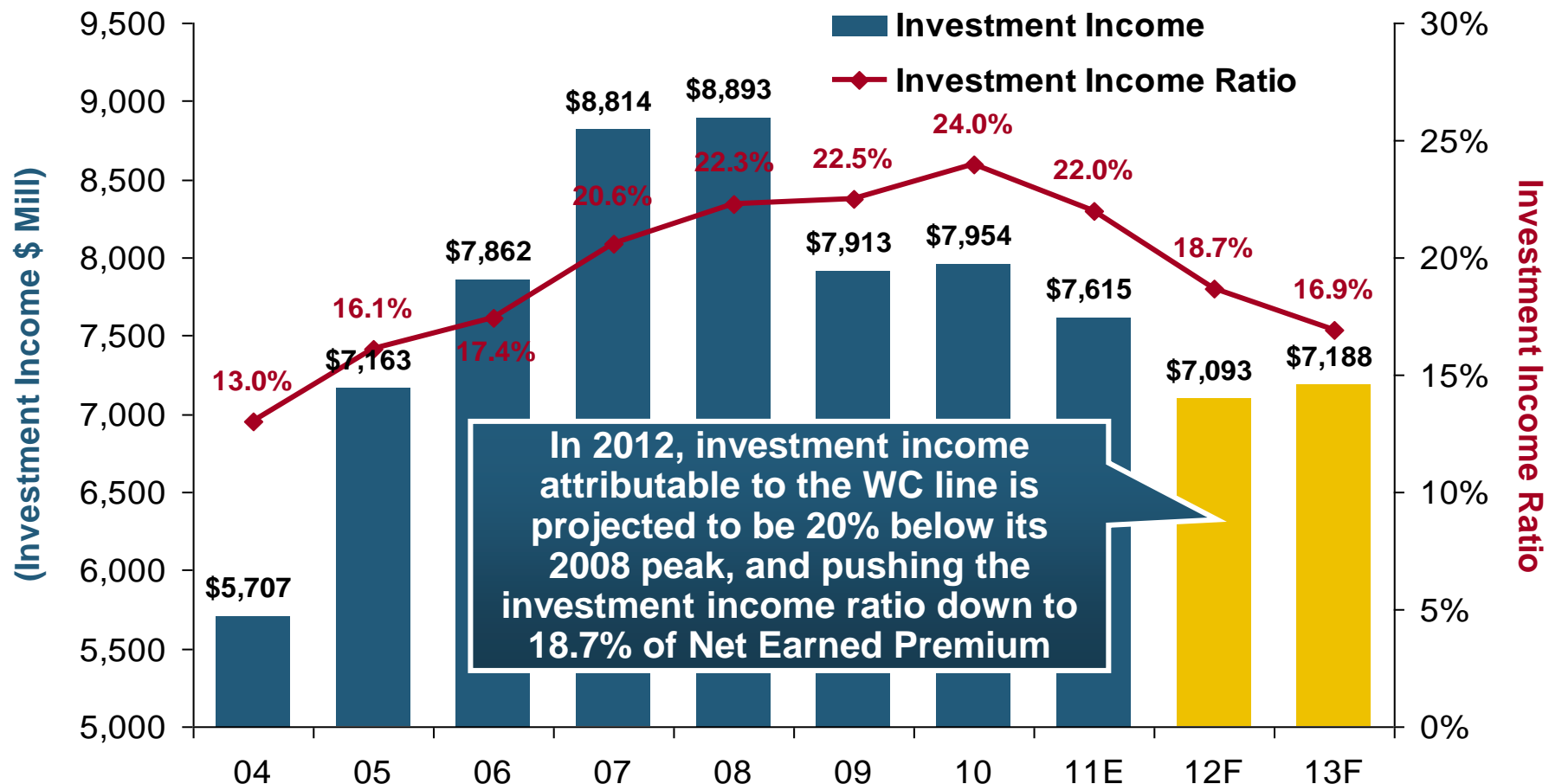
Source: NCCI.

Workers Comp Rate Changes, 2008:Q4 – 2011:Q4

(Percent
Change)



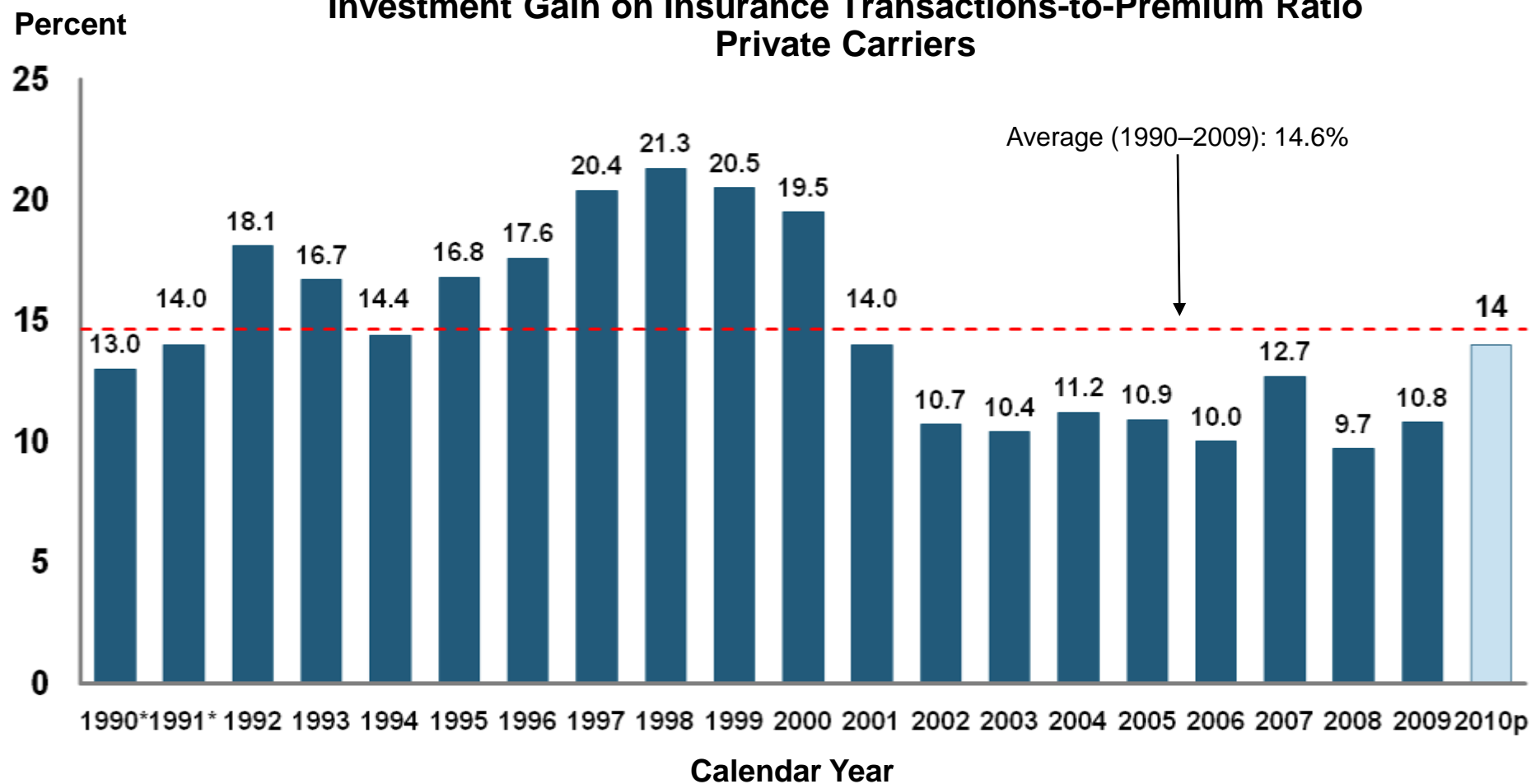
Workers Comp Investment Income Earned and Investment Income Ratio, 2004-2013F



Restoring the Workers Comp Line to Profitability Will Be Made More Difficult Because Investments Will Provide Little Lift, Requiring More of an Emphasis on Underwriting Profitability

Workers Compensation Investment Returns

**Investment Gain on Insurance Transactions-to-Premium Ratio
Private Carriers**



p=Preliminary

Source: 1990–2009, Annual Statement Data; 2010p, NCCI

Investment Gain on Insurance Transactions includes Other Income

•Adjusted to include realized capital gains to be consistent with 1992 and after

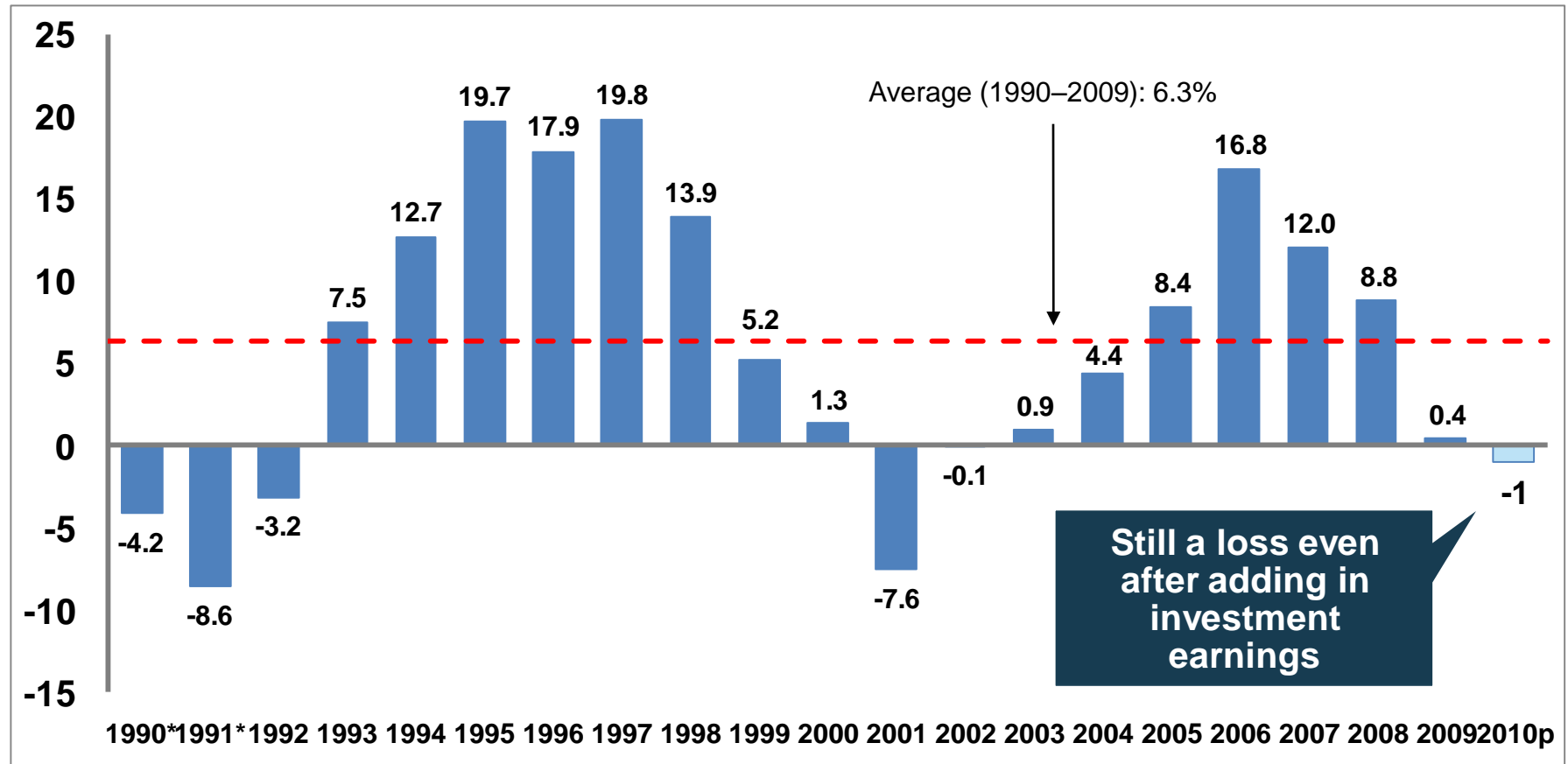
Source: NCCI

Workers Compensation Results

Modest Operating Loss

Pre-Tax Operating Gain Ratio Private Carriers

Percent



p Preliminary

Source: 1990–2009, Annual Statement Data; 2010p, NCCI

Operating Gain Equals 1.00 minus (Combined Ratio Less Investment Gain on Insurance Transactions and Other Income)

*Adjusted to include realized capital gains to be consistent with 1992 and after

Source: NCCI

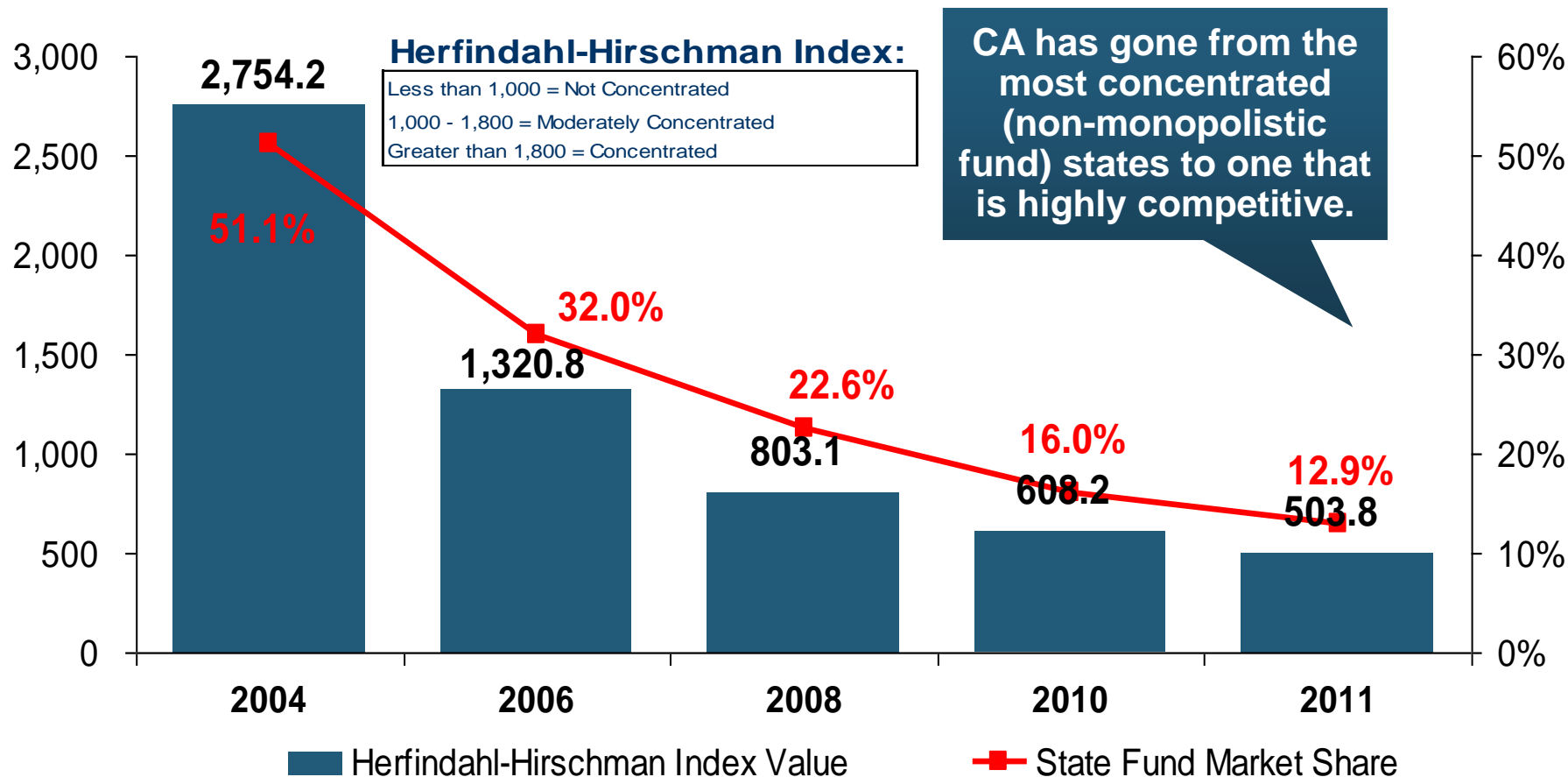
Competition, Profitability and Growth in California P/C and WC Insurance Markets vs. US

Analysis by Line and Nearby State Comparisons

Market Concentration in CA WC Market Has Dropped Precipitously: HHI Index, 2004-2011

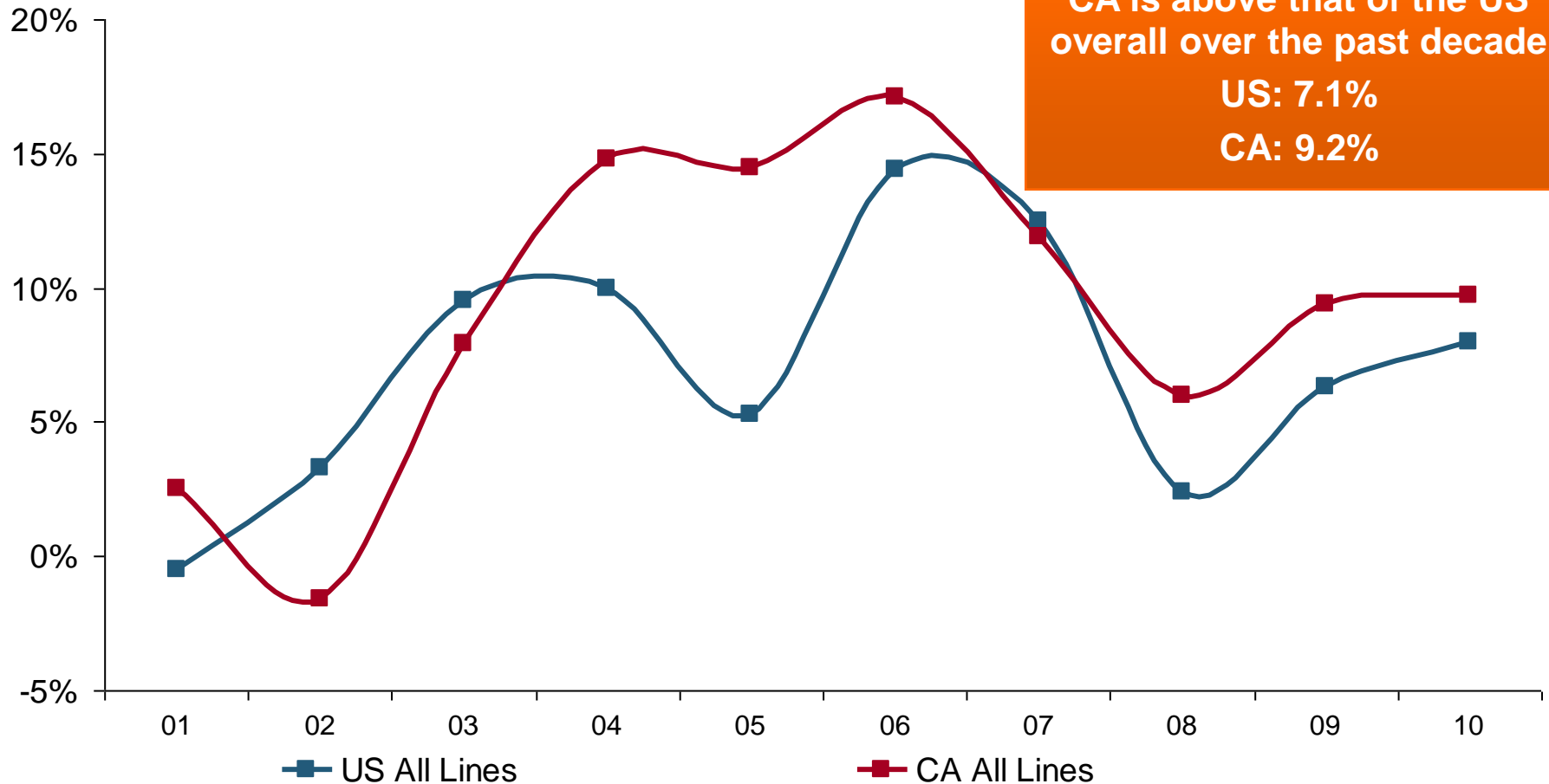
HHI Index Value

CA State Fund Market Share



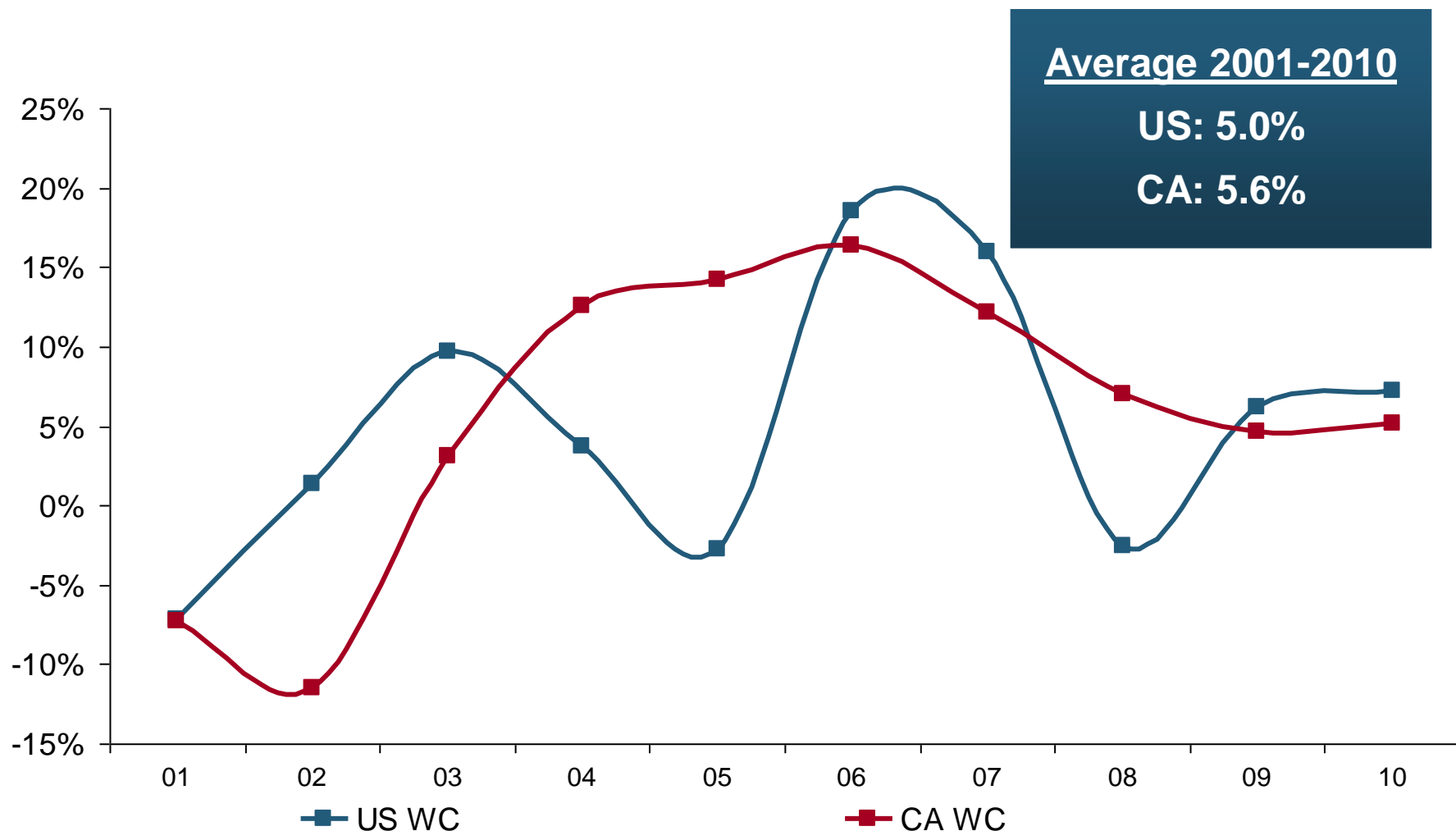
RNW All Lines: CA vs. U.S., 2001-2010

(Percent)



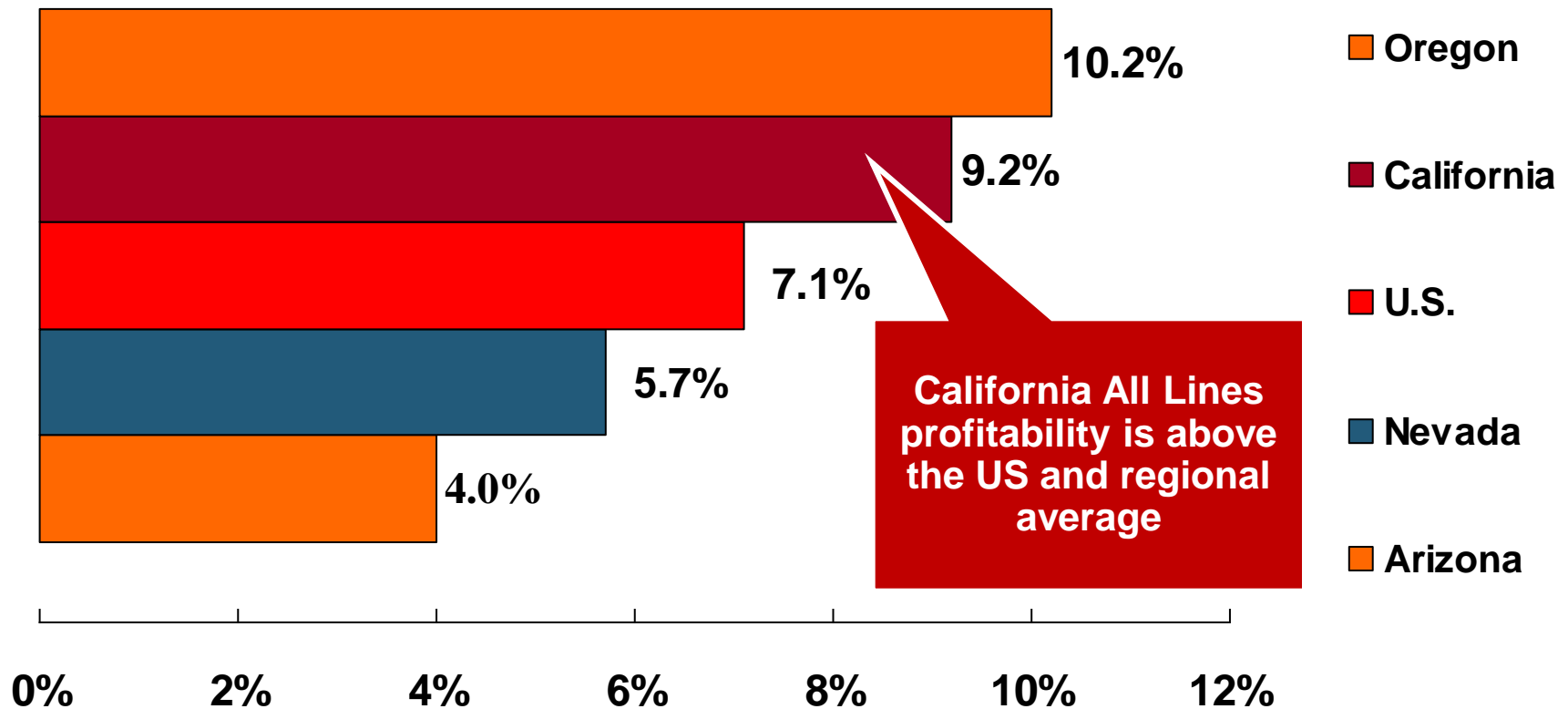
RNW Workers Comp: CA vs. U.S., 2001-2010

(Percent)



All Lines: 10-Year Average RNW CA & Nearby States

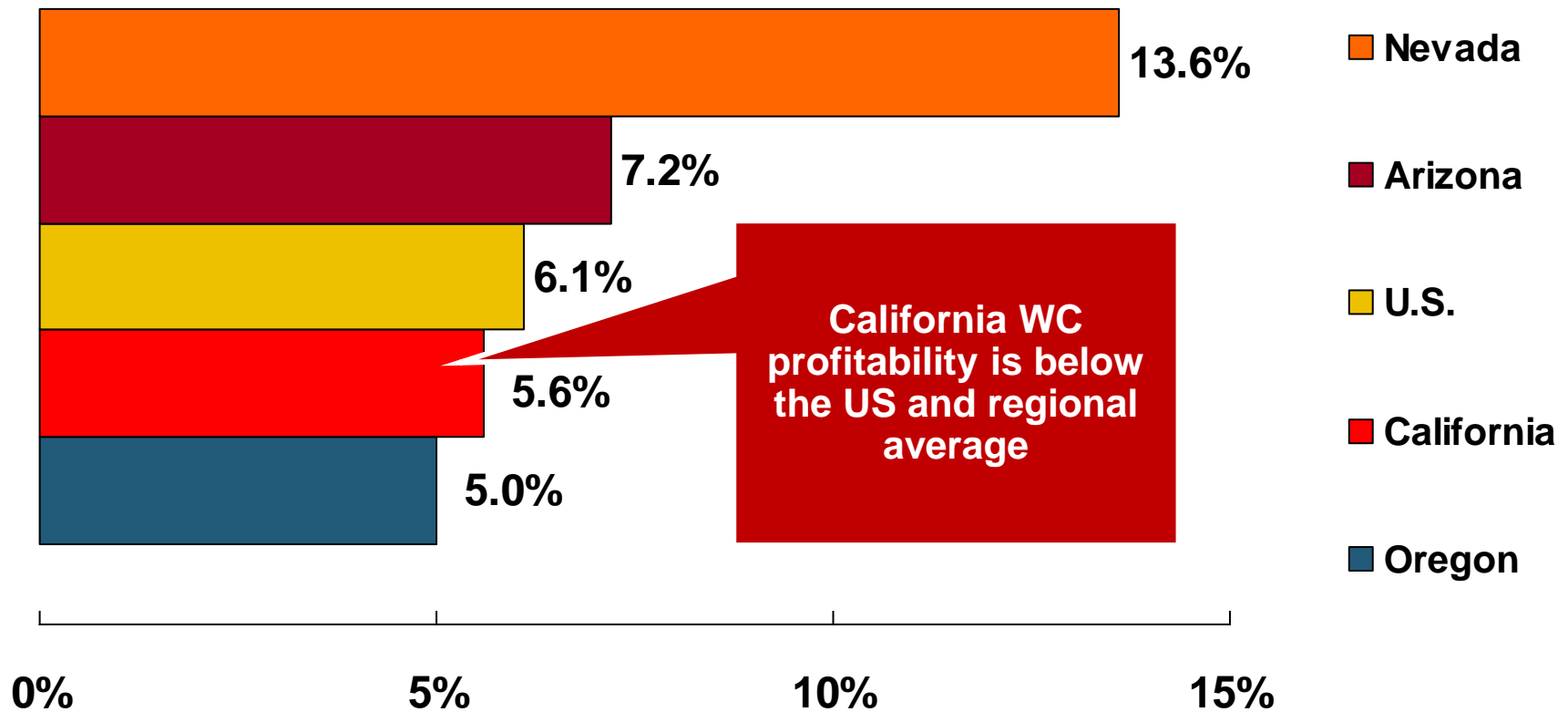
2001-2010



Source: NAIC, Insurance Information Institute.

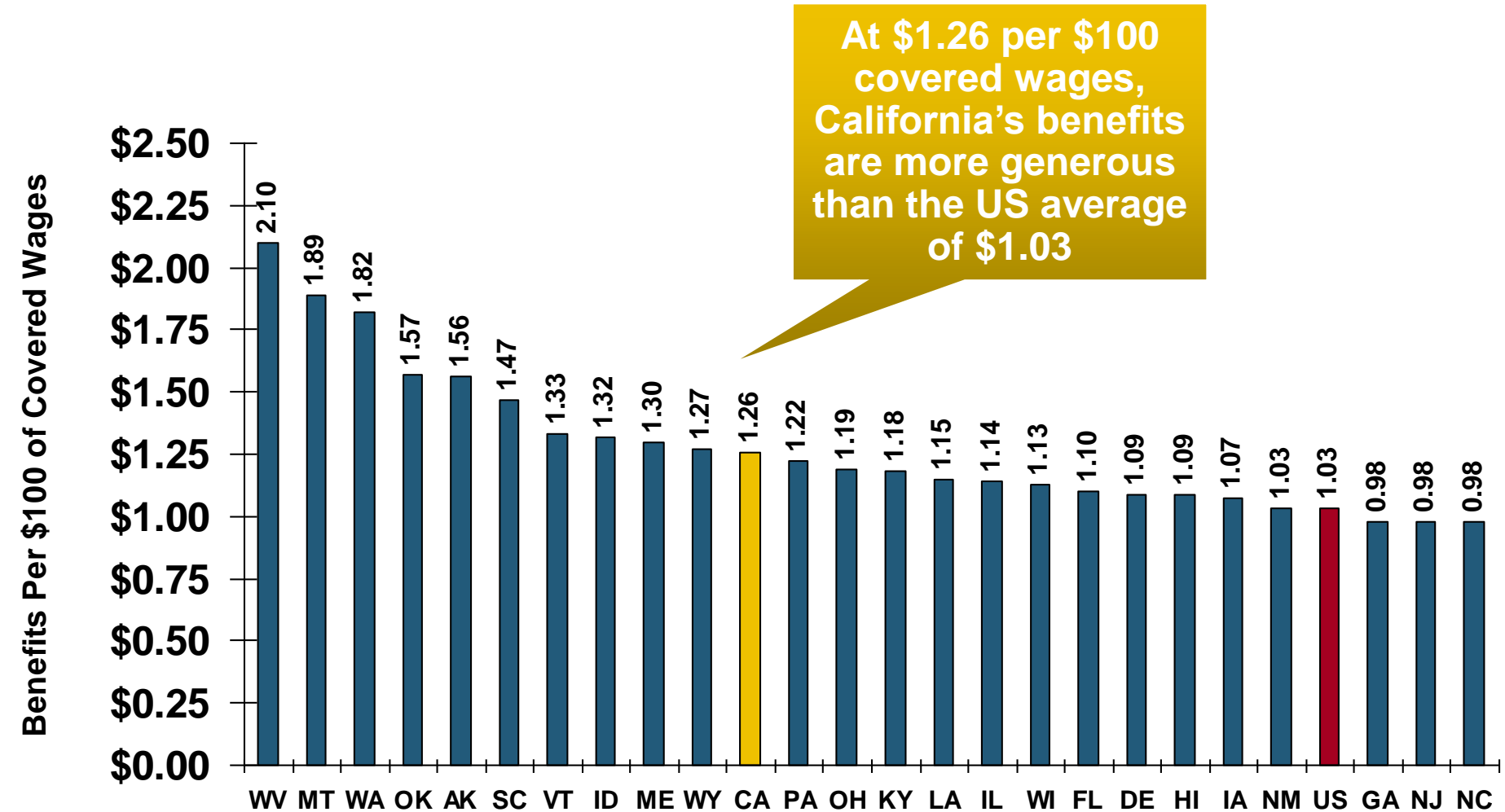
Workers Comp: 10-Year Average RNW CA & Nearby States

2001-2010

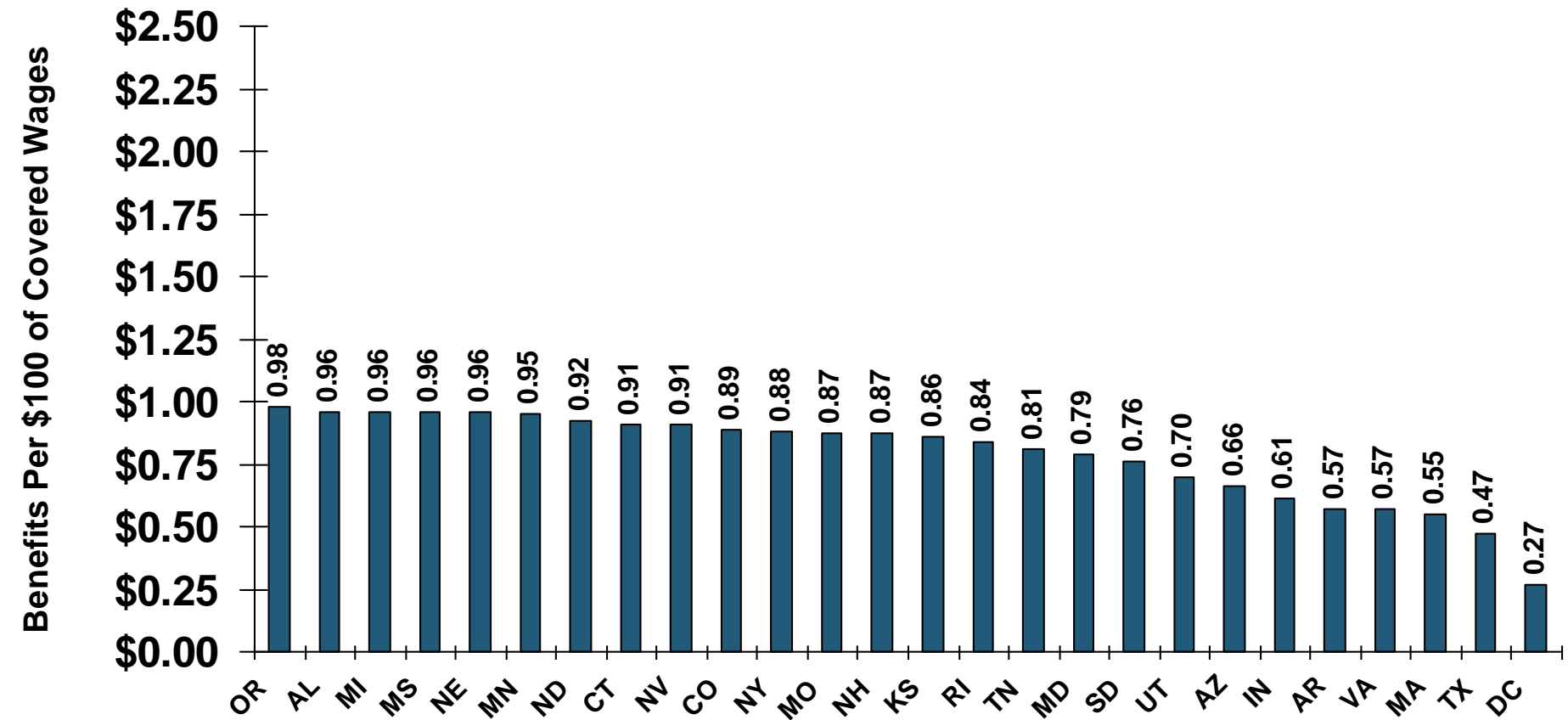


Source: NAIC, Insurance Information Institute

WC Benefits Per \$100 of Covered Wages by State, 2009: Highest 25 States



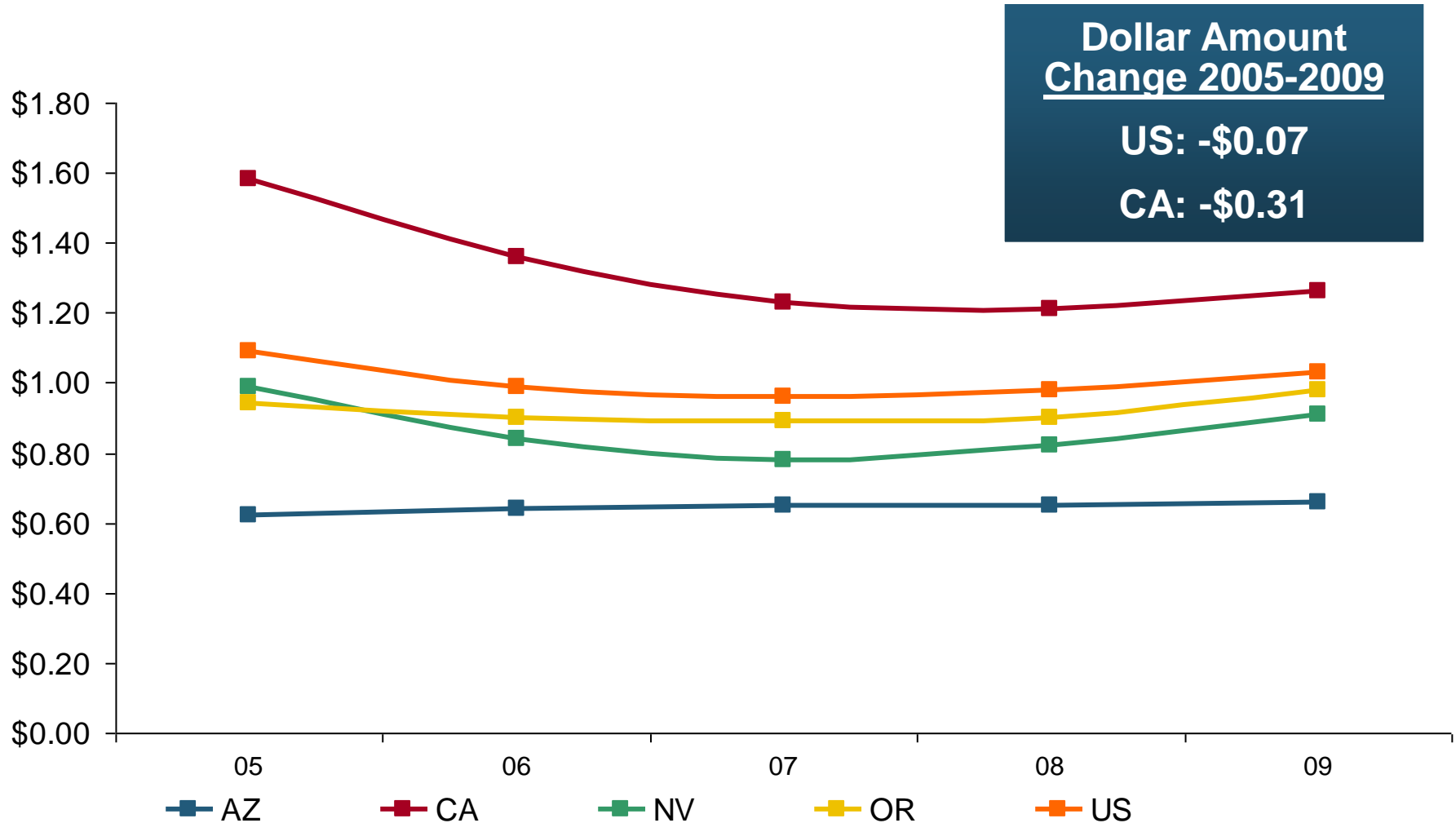
WC Benefits Per \$100 of Covered Wages by State, 2009: Lowest 25 States



WC Benefits Per \$100 of Covered Wages by State

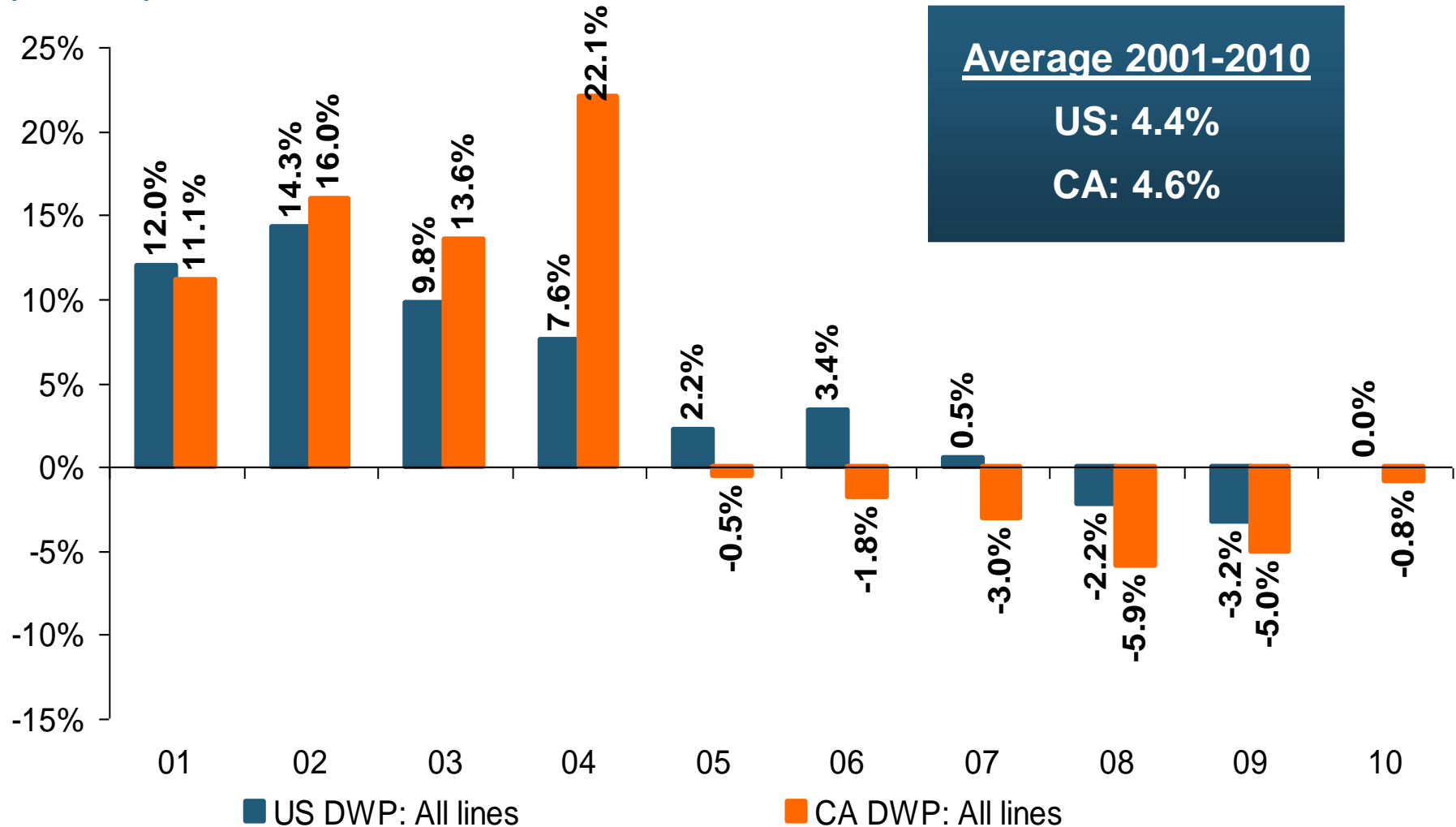
2005-2009: CA & Nearby States

(Percent)



All Lines DWP Growth: CA vs. U.S., 2001-2010

(Percent)

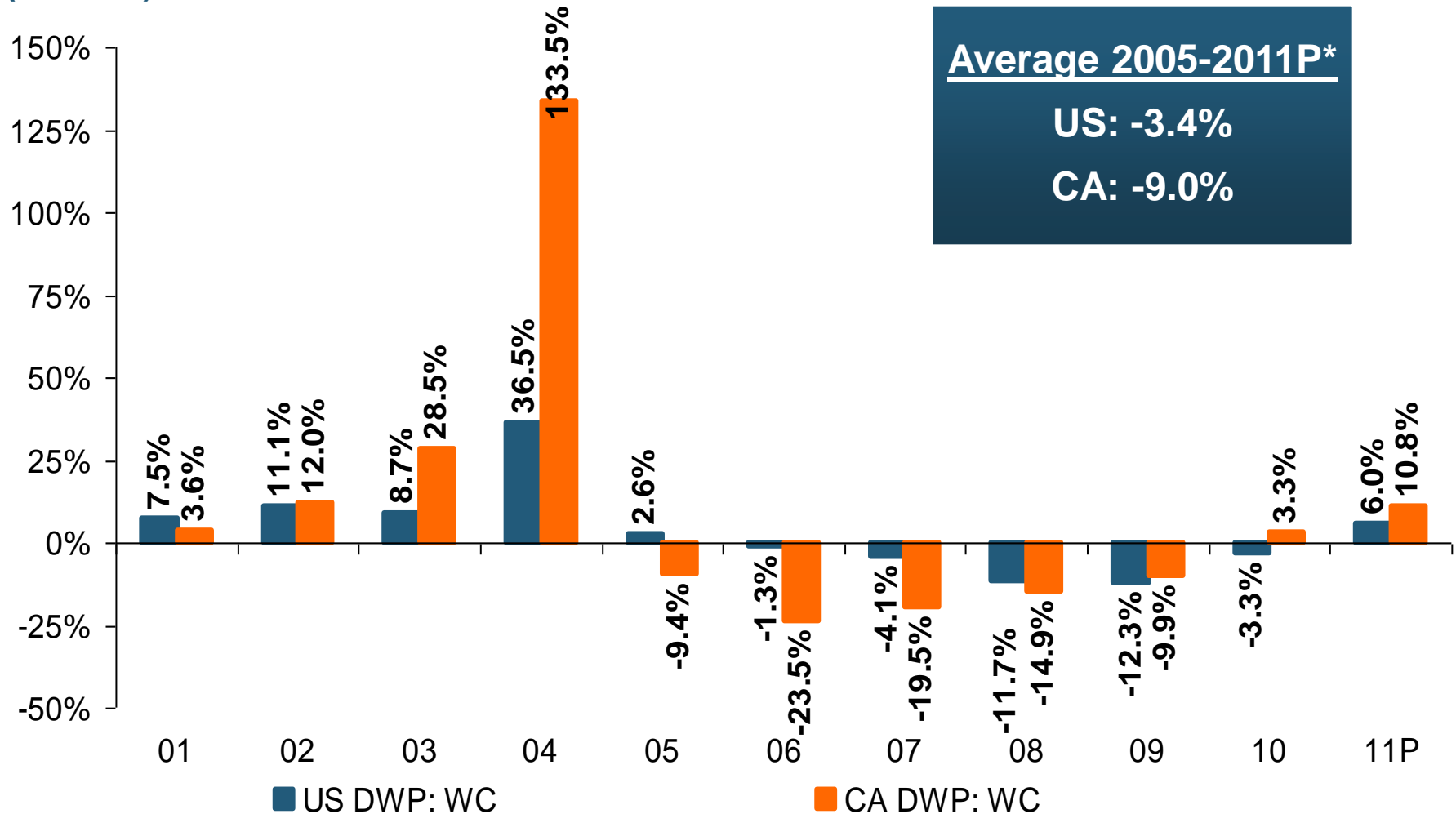


*2004 and onward includes major state funds.

Source: SNL Financial.

Workers Comp DWP Growth: CA vs. U.S., 2001-2011P*

(Percent)

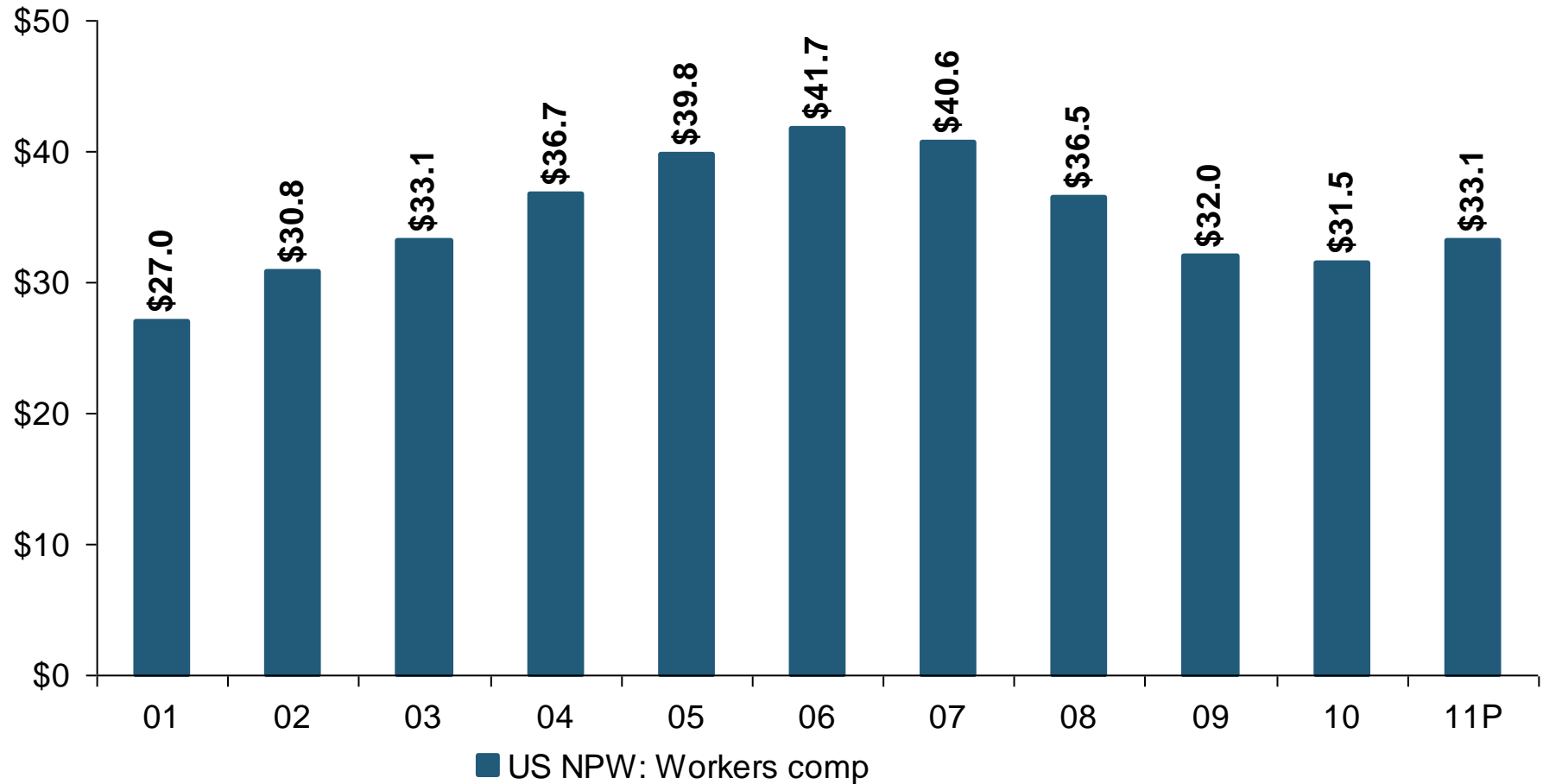


*2004 and onward includes state funds.

Source: SNL Financial.

Workers Comp NPW: 2001-2010

(\$ billions)

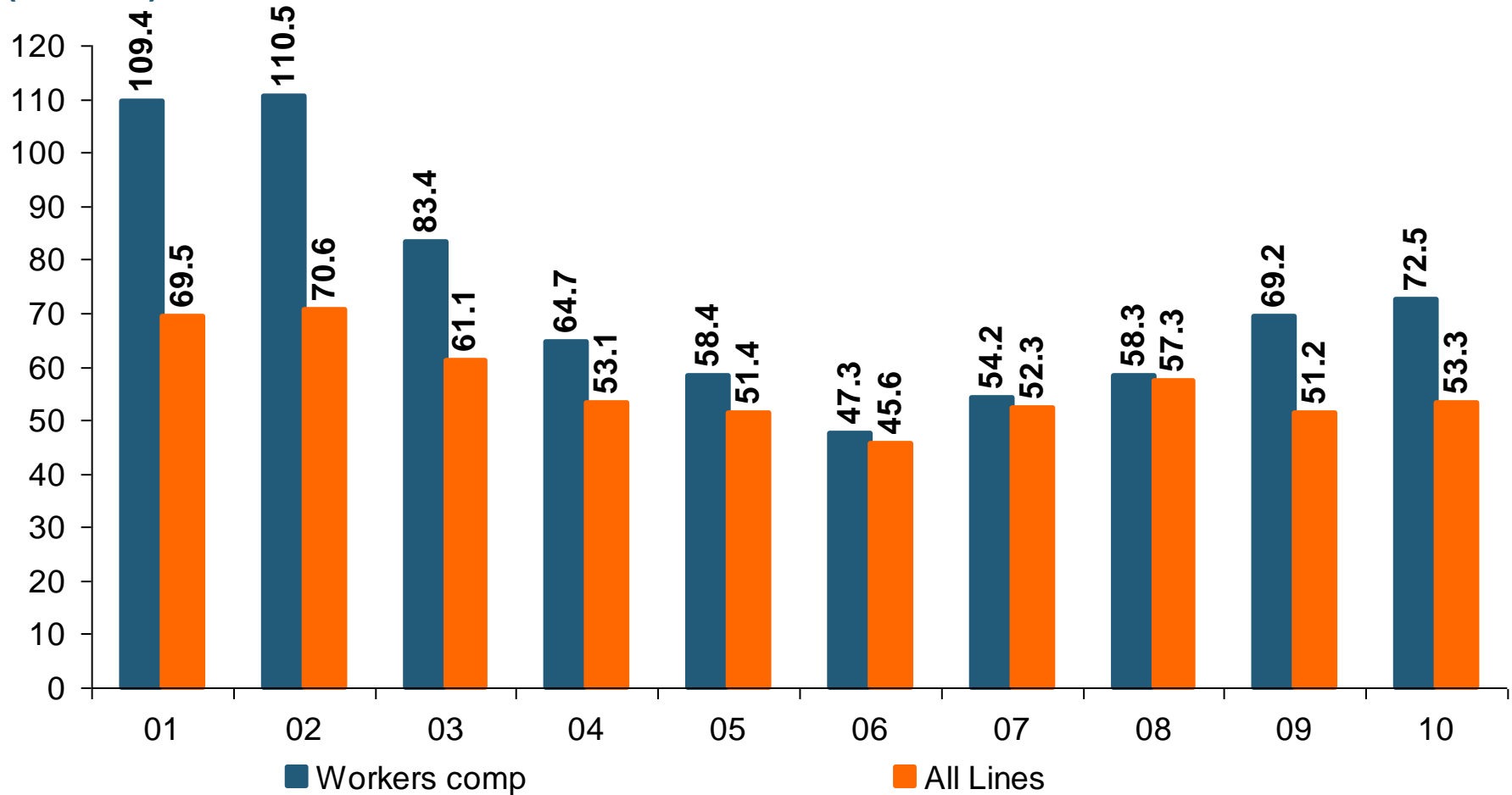


*Does not include state funds.

Source: SNL Financial.

Direct Incurred Loss Ratio: WC & All Lines CA, 2001-2010

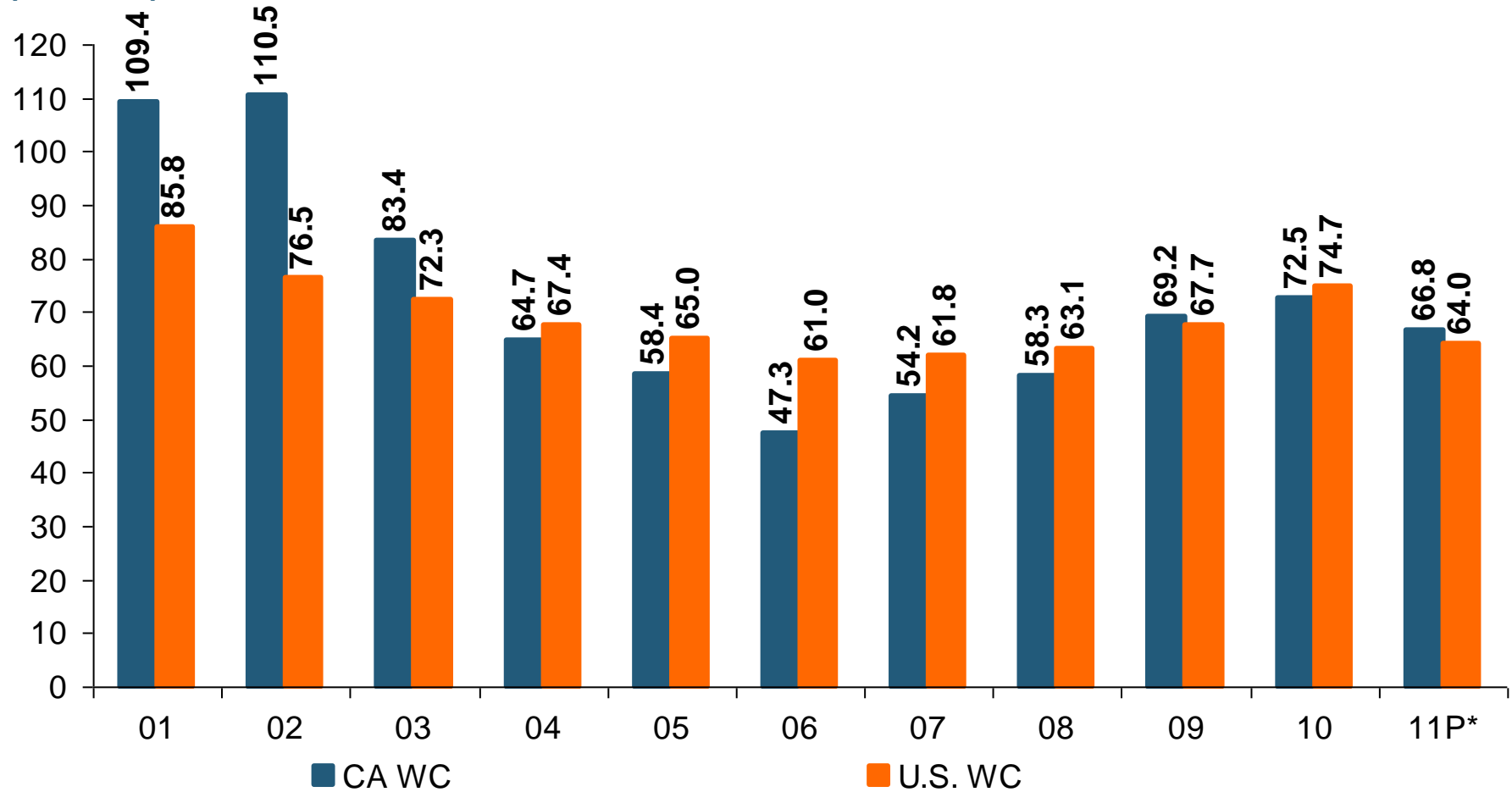
(Percent)



*2004-2010 includes major state funds;
Source: SNL Financial.

Workers Comp Direct Incurred Loss Ratio: CA vs. U.S., 2001-2011P*

(Percent)



*2004-2010 includes major state funds; Preliminary data for 2011 do not include state funds.

Source: SNL Financial.



Economics 2012:

Workers Comp in the Aftermath of the Great Recession

**2012 Is the First Year Since 2005
Where Economic Perceptions and
Reality in the US Will Be Positive**

***Potentially Enormous Benefits for
Workers Comp Insurers***

- **Economic Growth Will Accelerate Modestly in 2012/13, Beating Expectations**
 - ◆ No Double Dip Recession
 - ◆ Economy remains more resilient than most pundits presume
- **Consumer Confidence Will Continue to Improve**
- **Consumer Spending/Investment Will Continue to Expand**
- **Consumer and Business Lending Continue to Expand**
- **Housing Market Remains Weak, but Some Improvement Expected in 2012**
- **Inflation Remains Tame**
 - ◆ Runaway inflation highly unlikely but energy spike possible; Fed has things under control
- **Private Sector Hiring Remains Consistently Positive, Exceeds Expectations**
 - ◆ Unemployment dips below 8% by year's end
- **Sovereign Debt, Euro Currency/Economy, Muni Bond "Crises" Overblown**
- **European Recession is Milder than Commonly Presumed**
- **Soft Landing in China**
- ***Higher Oil Prices and Current Middle East Turmoil Pose Greater Risk to US Economy than in 2011***
- **Interest Rates Remain Low by Historical Standards; Edge Up by Year's End**
- **Stock and Bond Markets More Stable, Less Volatile**
- **Political Environment Is More Hospitable to Business Interests**
- **Obama Wins Re-Election Based on Improving Economy**

■ P/C Insurance Exposures Grow Robustly

- ◆ Personal and commercial exposure growth is certain in 2012; Strongest since 2004
- ◆ But restoration of destroyed exposure will take until mid-decade

■ P/C Industry Growth in 2012 Will Be Strongest Since 2004

- ◆ Growth likely to exceed A.M. Best projection of +3.8% for 2012
- ◆ No traditional “hard market” emerges in 2012

■ Underwriting Fundamentals Deteriorate Modestly

- ◆ Some pressure from claim frequency, in some severity in key lines

■ Increasing Private Sector Hiring Will Drive Payrolls/WC Exposures

- ◆ Wage growth is also positive and could modestly accelerate
- ◆ WC will prove to be tough to fix from an underwriting perspective

■ Increase in Demand for Commercial Insurance Will Accelerate in 2012

- ◆ Includes **workers comp**, property, marine, many liability coverages
- ◆ Laggards: inland marine, aviation, commercial auto, surety
- ◆ Personal Lines: Auto leads, homeowners lags (*though HO leads in NPW growth due to rates*)

■ Investment Environment Is/Remains Much More Favorable

- ◆ Return of realized capital gains as a profit driver
- ◆ Interest rates remain low; Some upward pressured if economic strength surprises

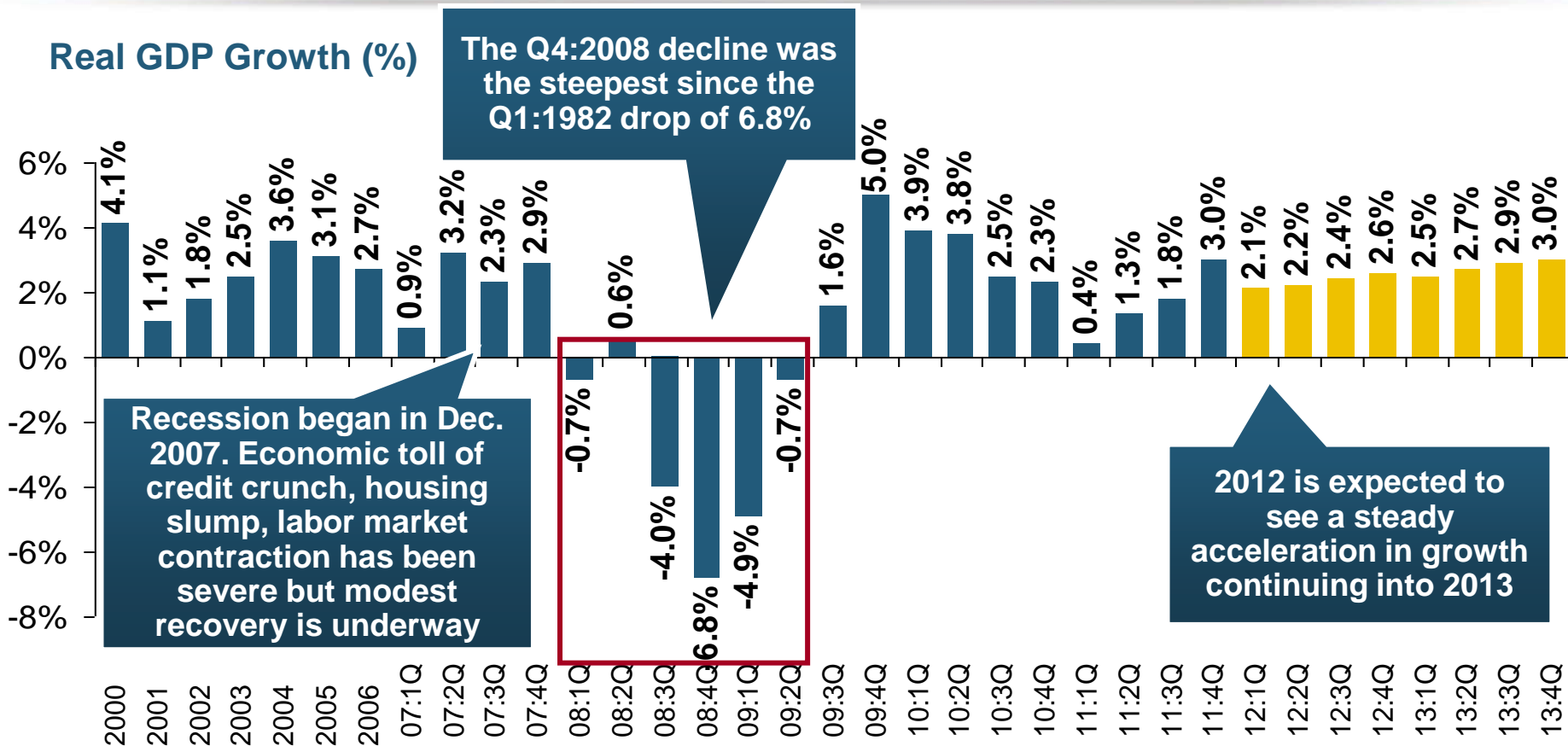
■ Industry Capacity Hits a New Record by Year-End 2012 (Barring Mega-CAT)



The Strength of the Economy Will Influence WC Insurer Growth Opportunities

**Growth Will Expand Insurable Exposures
Including WC Payroll Exposures**

US Real GDP Growth*



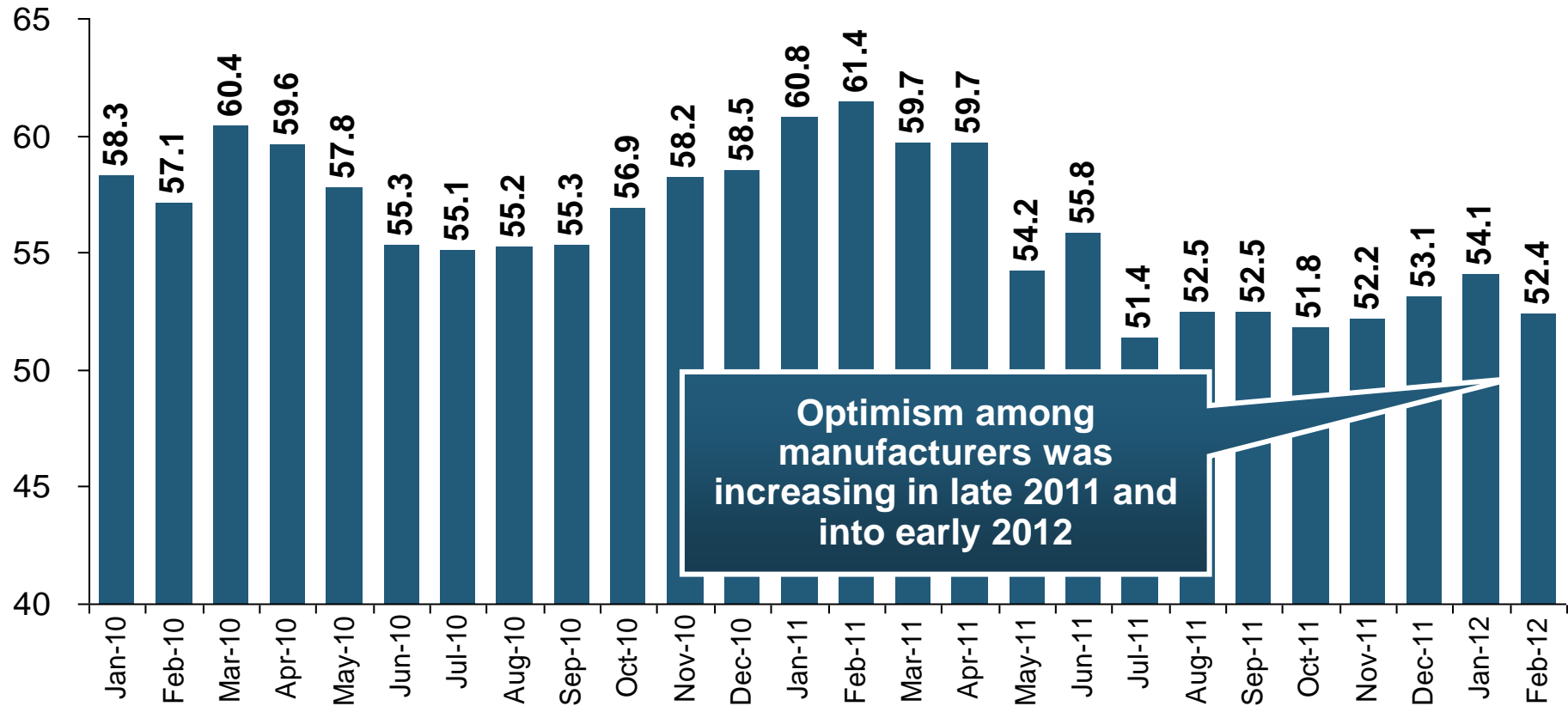
Demand for Insurance Continues To Be Impacted by Sluggish Economic Conditions, but the Benefits of Even Slow Growth Will Compound and Gradually Benefit the Economy Broadly

* Estimates/Forecasts from Blue Chip Economic Indicators.

Source: US Department of Commerce, Blue Economic Indicators 3/12; Insurance Information Institute.

ISM Manufacturing Index (Values > 50 Indicate Expansion)

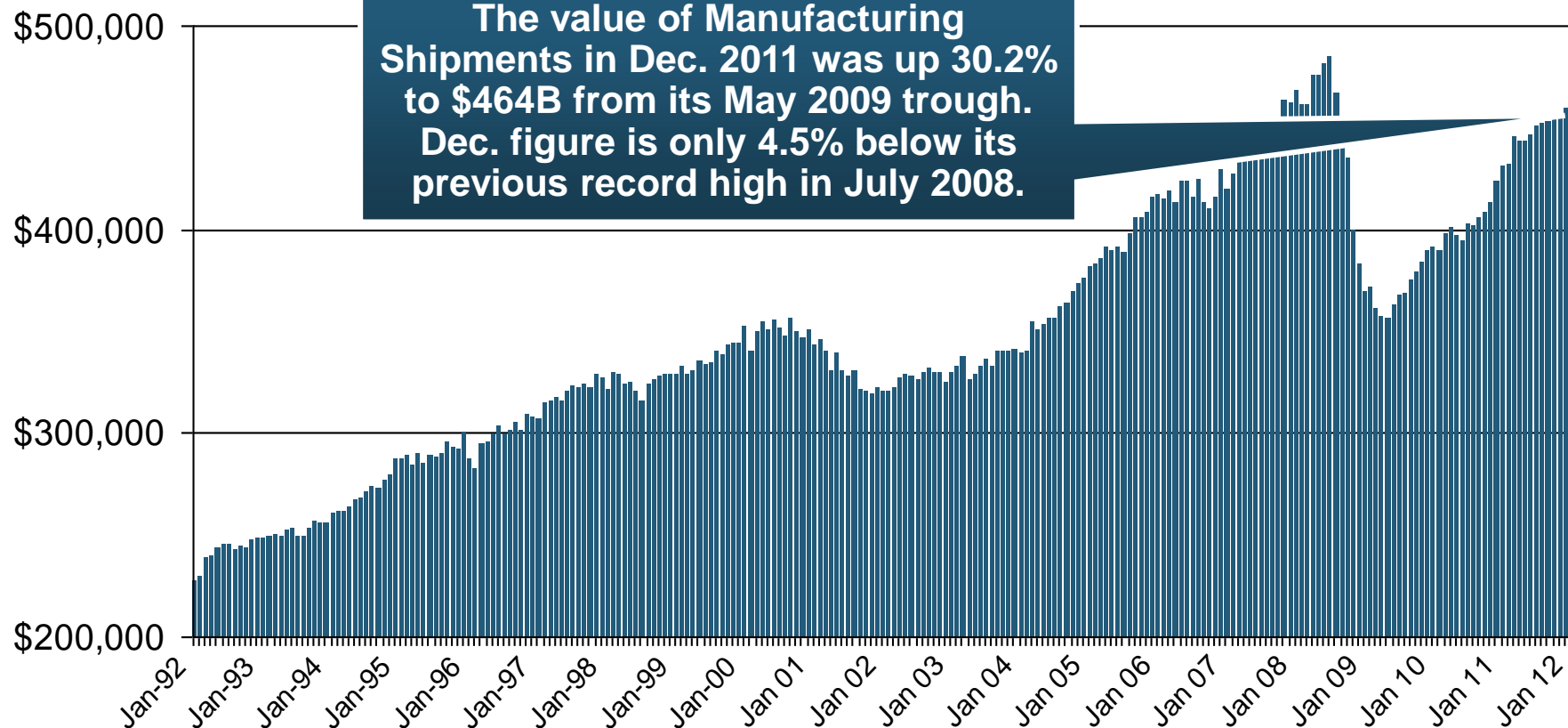
January 2010 through February 2012



**The manufacturing sector has been expanding and adding jobs.
The question is whether this will continue.**

Dollar Value* of Manufacturers' Shipments Monthly, Jan. 1992—Jan. 2012

\$ Millions



Monthly shipments are nearly back to peak (in July 2008, 8 months into the recession). Trough in May 2009. Growth from trough to December 2011 was 30.2%. This growth leads to gains in many commercial exposures: WC, Commercial Auto, Property and Various Liability Coverages

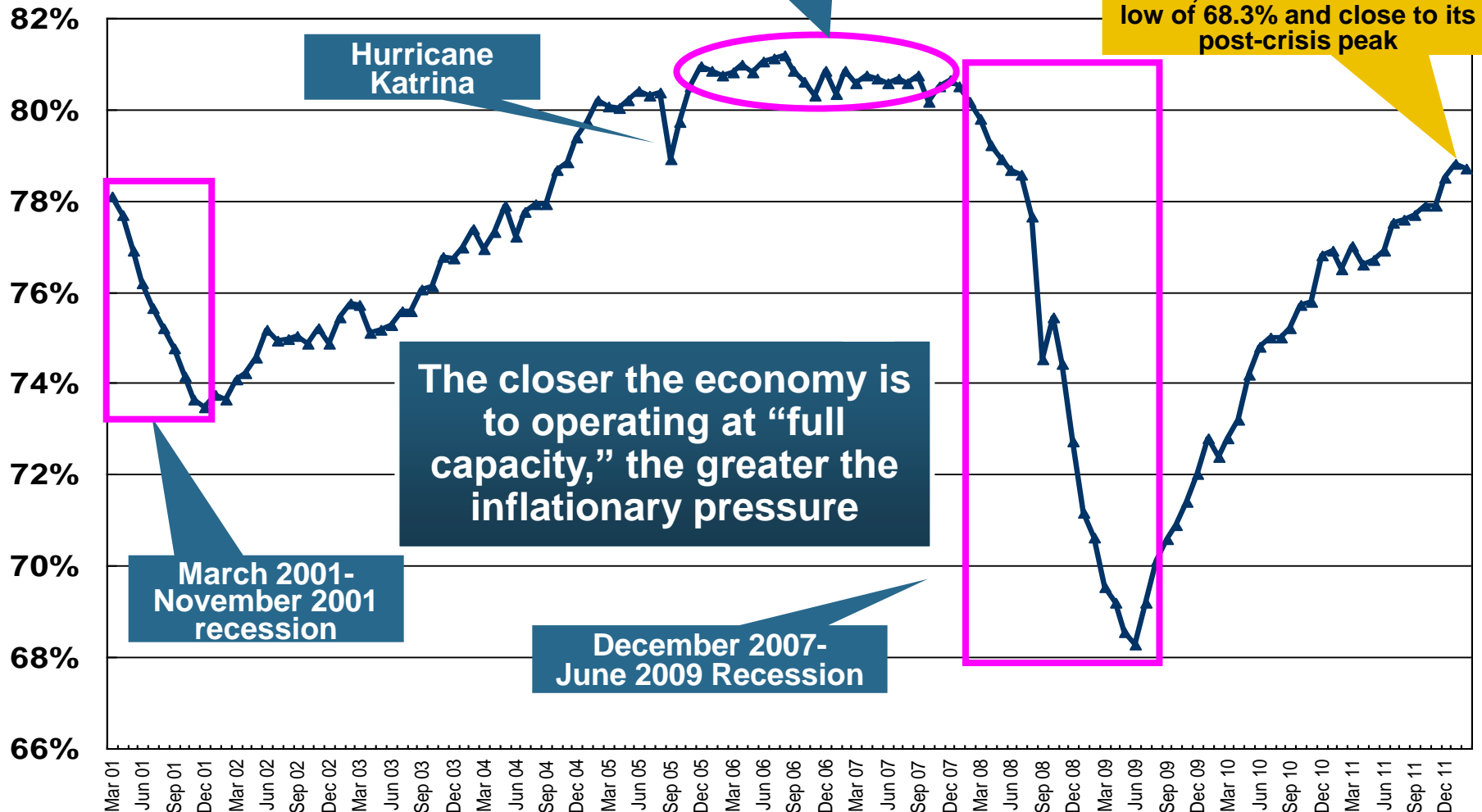
*seasonally adjusted

Source: U.S. Census Bureau, *Full Report on Manufacturers' Shipments, Inventories, and Orders*, <http://www.census.gov/manufacturing/m3/>

Recovery in Capacity Utilization is a Positive Sign for Commercial Exposures

March 2001 through February 2012

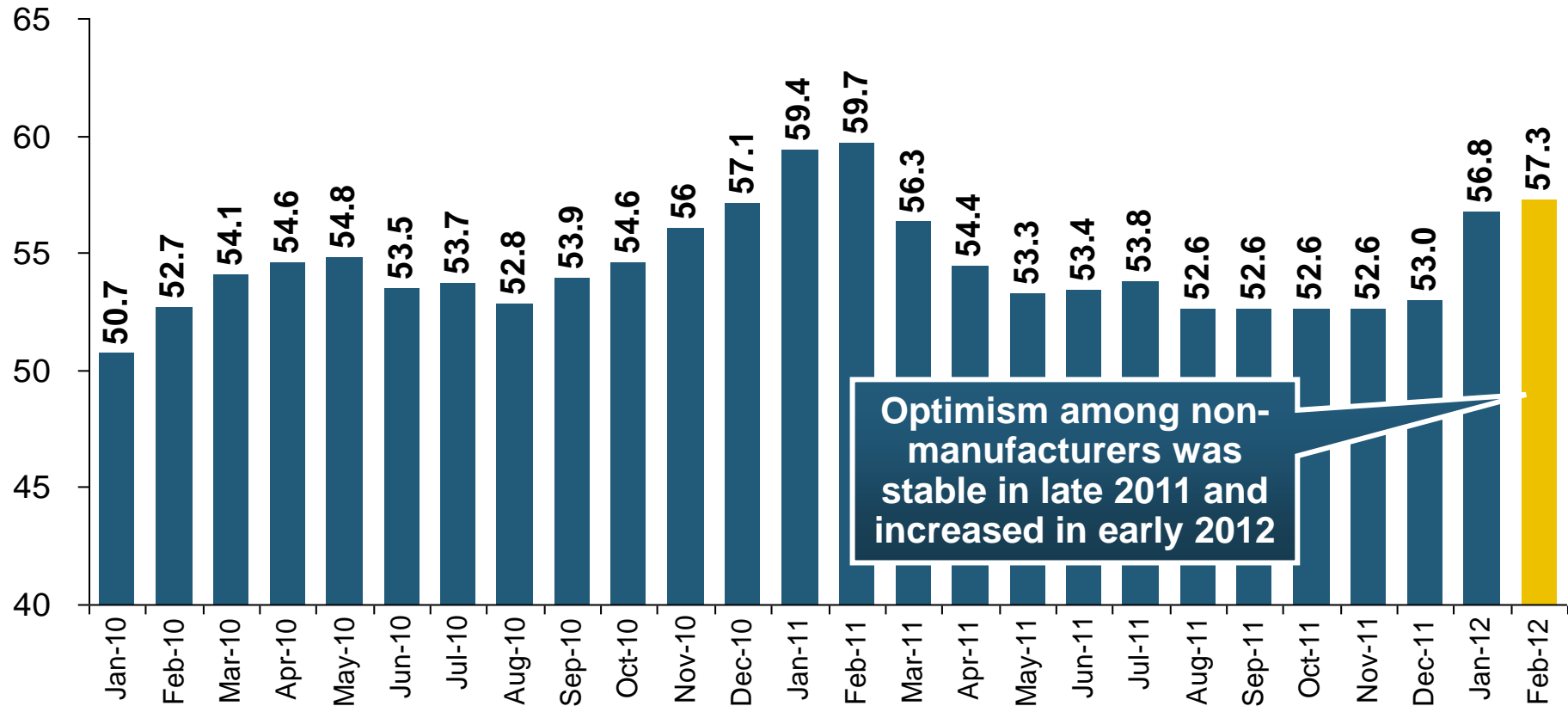
Percent of Industrial Capacity



Source: Federal Reserve Board statistical releases at <http://www.federalreserve.gov/releases/g17/Current/default.htm>.

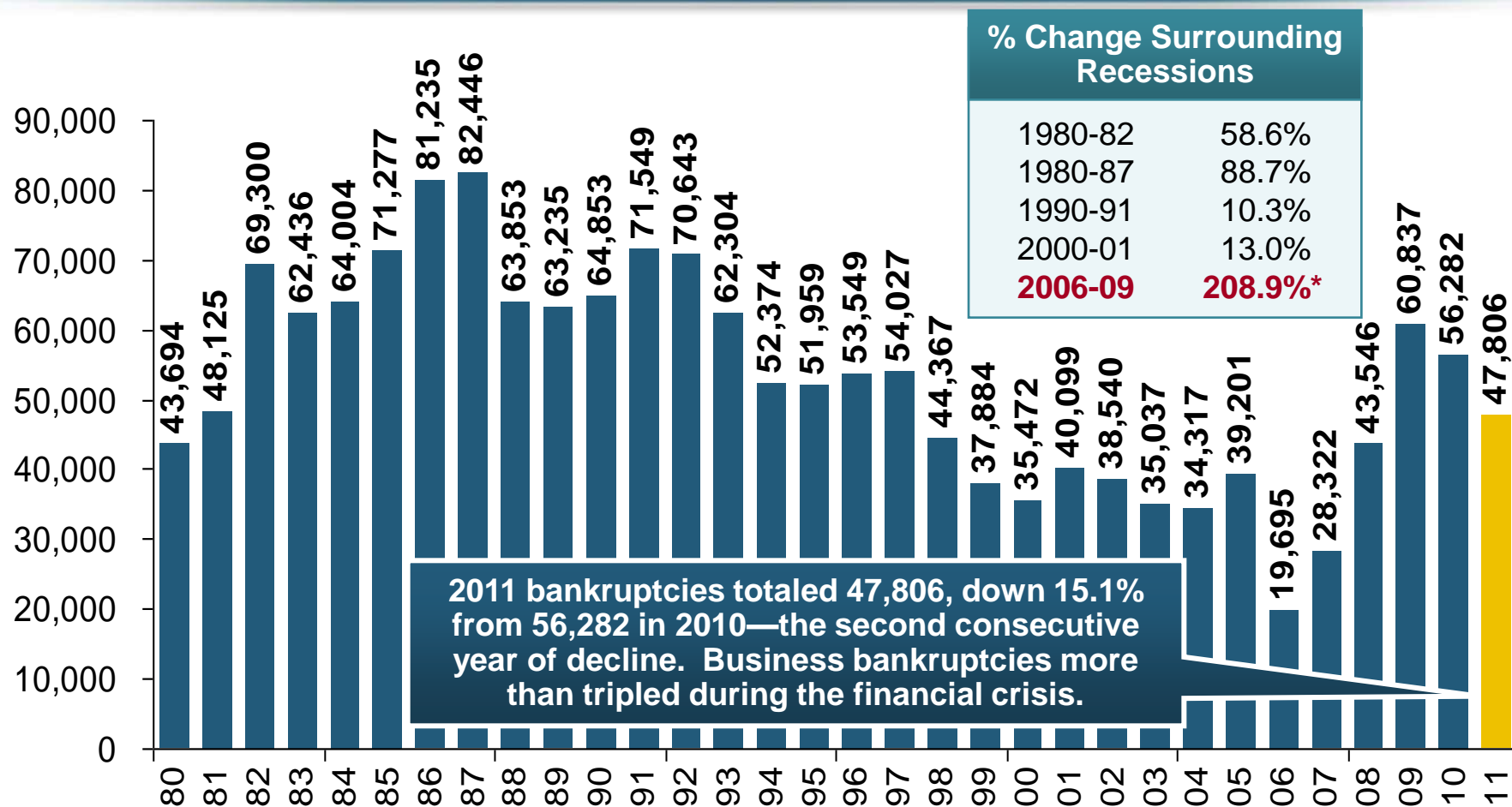
ISM Non-Manufacturing Index (Values > 50 Indicate Expansion)

January 2010 through February 2012



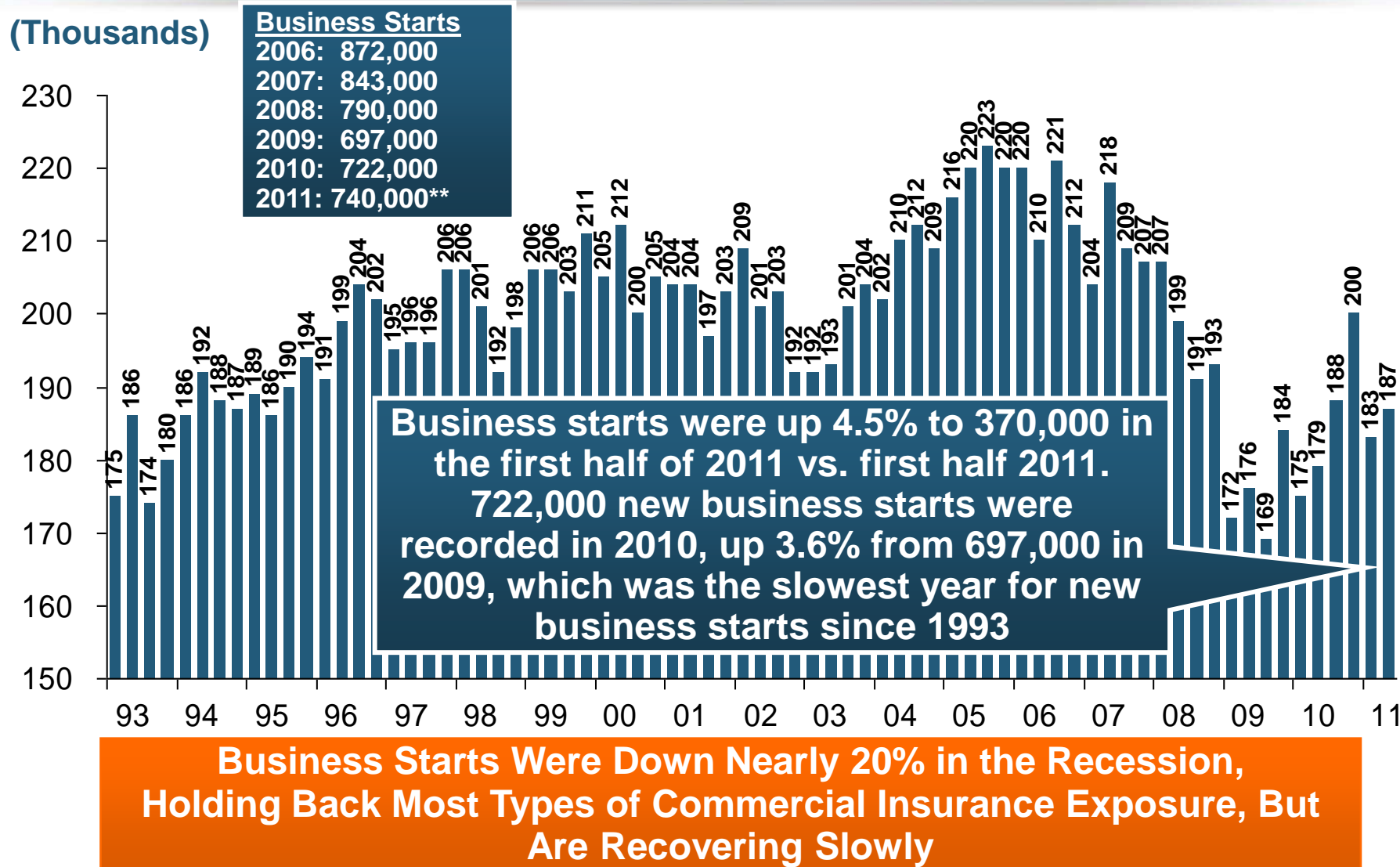
Non-manufacturing industries have been expanding and adding jobs. The question is whether this will continue.

Business Bankruptcy Filings, 1980-2011



Significant Exposure Implications for All Commercial Lines as Business Bankruptcies Begin to Decline

Private Sector Business Starts, 1993:Q2 – 2011:Q2*



* Data through June 30, 2011 are the latest available as of March 7, 2012; Seasonally adjusted.

Source: Bureau of Labor Statistics, <http://www.bls.gov/news.release/cewbd.t08.htm>.

12 Industries for the Next 10 Years: Insurance Solutions Needed

Health Care
Health Sciences
Energy (Traditional)
Alternative Energy
Petrochemical
Agriculture
Natural Resources
Technology (incl. Biotechnology)
Light Manufacturing
Insourced Manufacturing
Export-Oriented Industries
Shipping (Rail, Marine, Trucking)

Many industries are poised for growth, though insurers' ability to capitalize on these industries varies widely

12 Fastest Growing Industries in 2011, by Sales Growth*

1. Metal & Mineral Wholesalers	+28.1%
2. Forging & Stamping	+26.2%
3. Resins, Synthetic Rubber/Fiber/Filaments	+24.5%
4. Cattle Ranching & Farming	+22.8%
5. Coating, Engraving, Heat Testing & Allied Act.	+22.4%
6. Motor Vehicle Parts Mfg.	+21.7%
7. Machine Shops	+21.0%
8. Petroleum & Petro. Merchant Wholesaling	+19.9%
9. Freight Transportation	+19.3%
10. Rubber Product Manufacturing	+18.7%
11. Wholesale Electronic Markets	+18.6%
12. Foundries	+17.7%

*12-months ending Oct. 2011. Total of 184 industries.

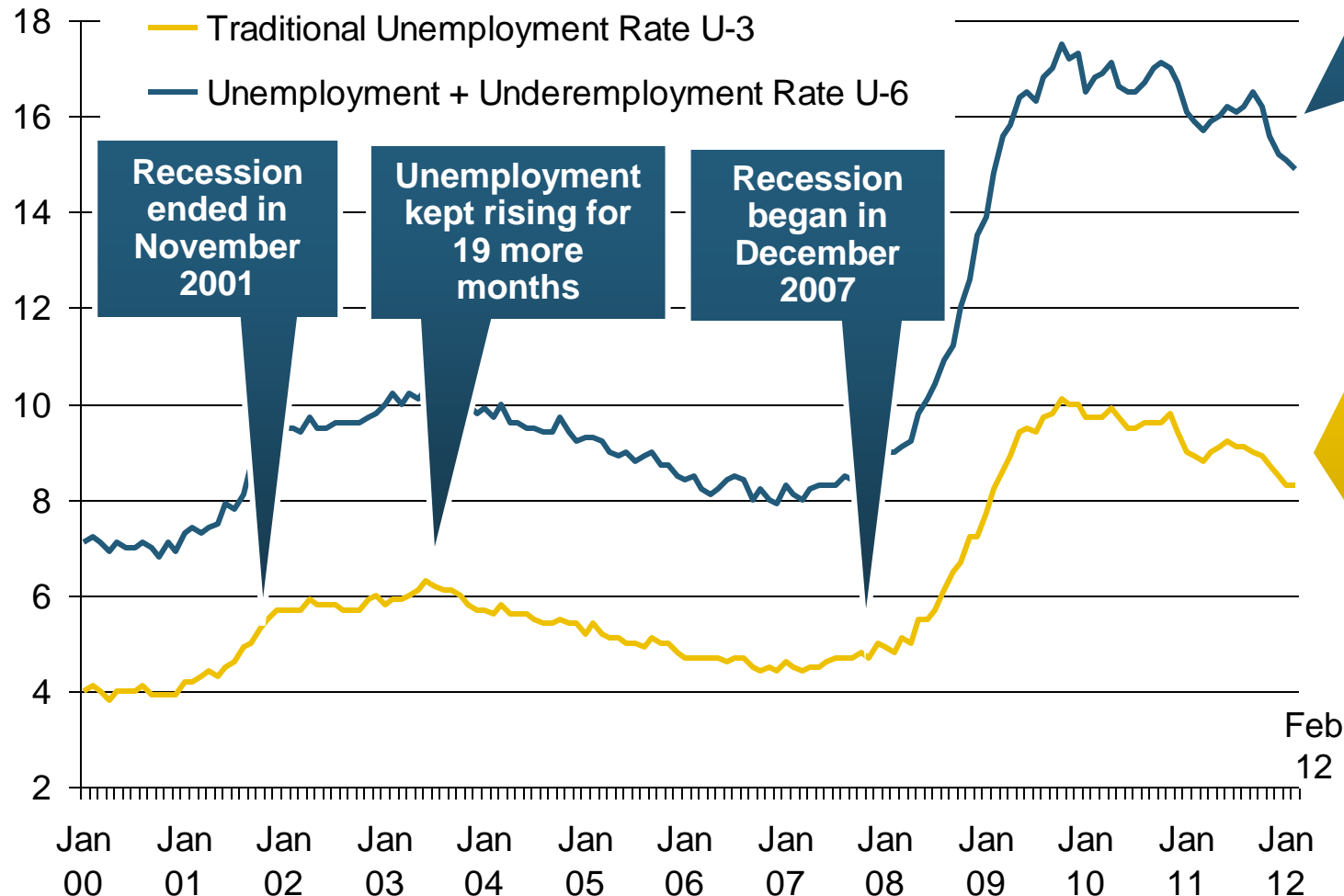
Source: Sageworks Consulting from US Census Bureau data as published in BusinessInsider.com (Oct. 5, 2011); Insurance Information Inst. 91

Labor Market Trends

**Massive Job Losses Sapped the
Economy and Commercial/Personal
Lines Exposure, But Trend is
Improving**

Unemployment and Underemployment Rates: Stubbornly High in 2012, But Falling

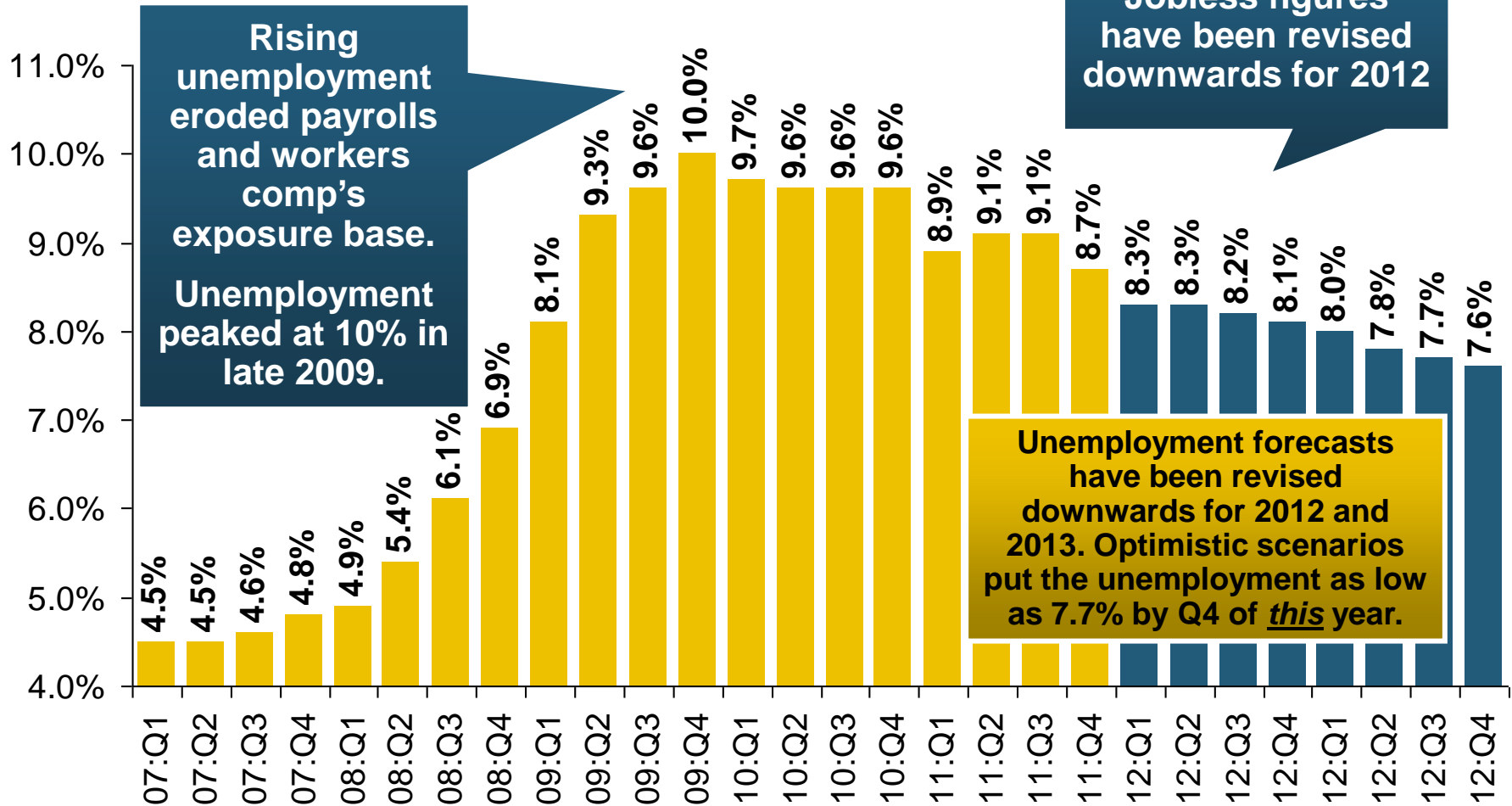
January 2000 through February 2012, Seasonally Adjusted (%)



Stubbornly high unemployment and underemployment constrain overall economic growth, but the job market is now clearly improving

US Unemployment Rate

2007:Q1 to 2013:Q4F*

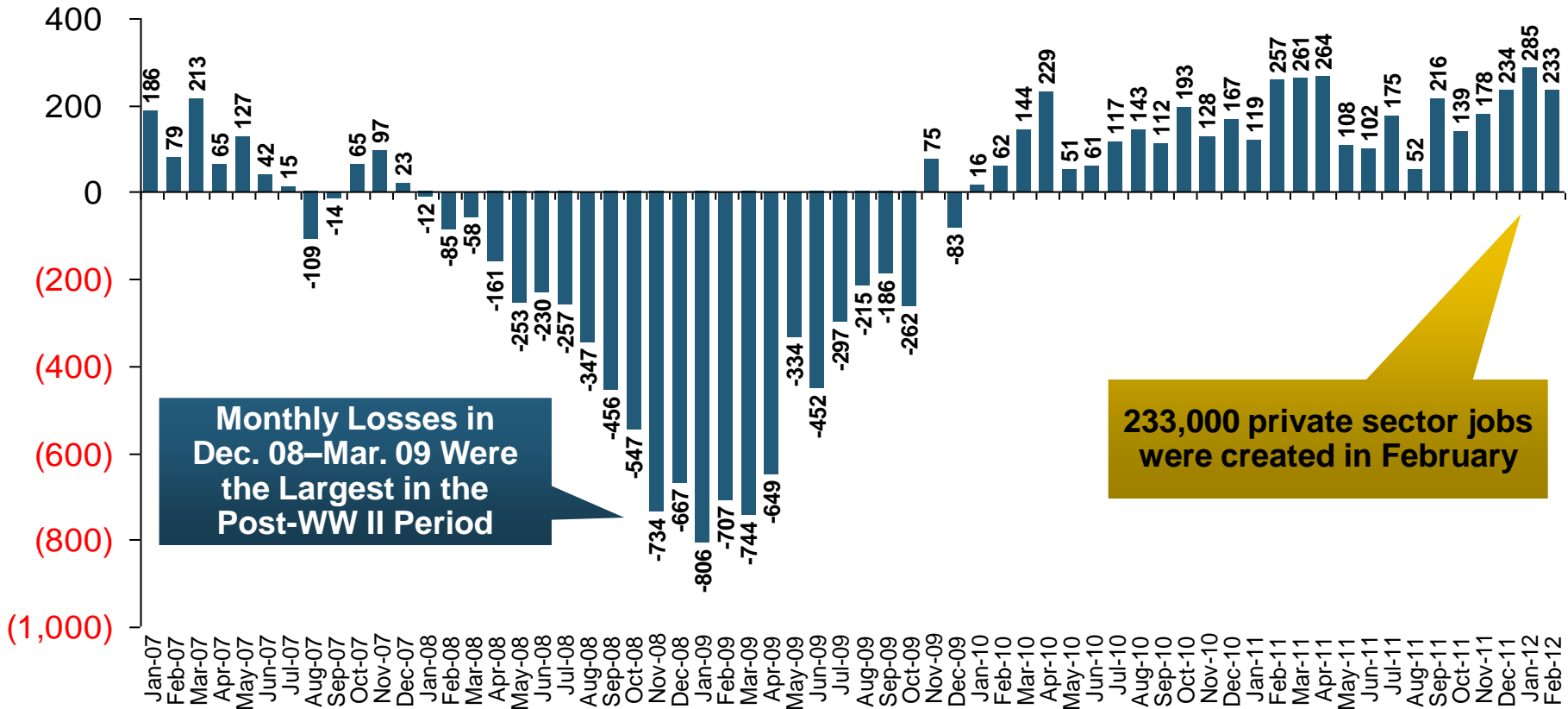


* ■ = actual; ■ = forecasts

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (3/12 edition); Insurance Information Institute.

Monthly Change in Private Employment

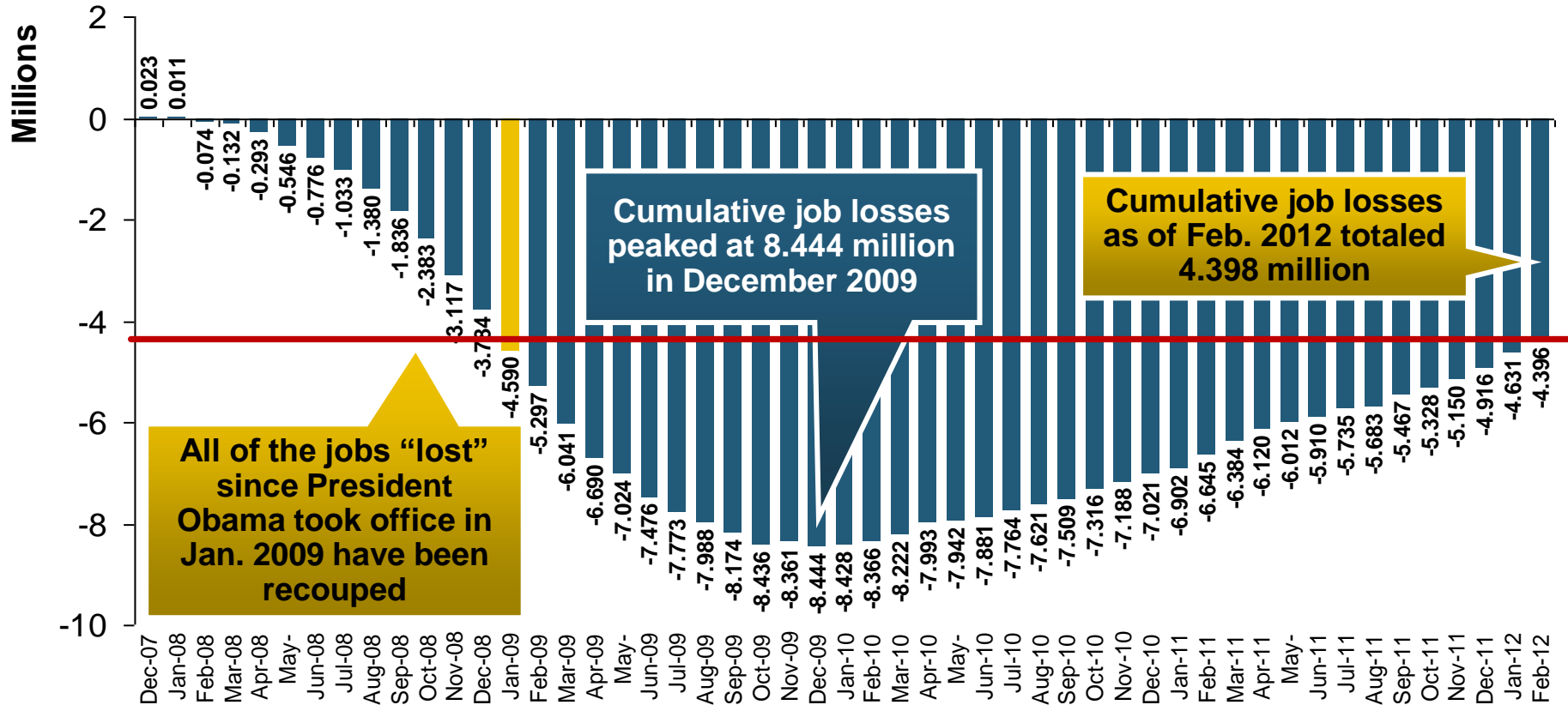
January 2008 through February 2012* (Thousands)



Private Employers Added 4.046 million Jobs Since Jan. 2010 After Having Shed 4.66 Million Jobs in 2009 and 3.81 Million in 2008 (State and Local Governments Have Shed Hundreds of Thousands of Jobs)

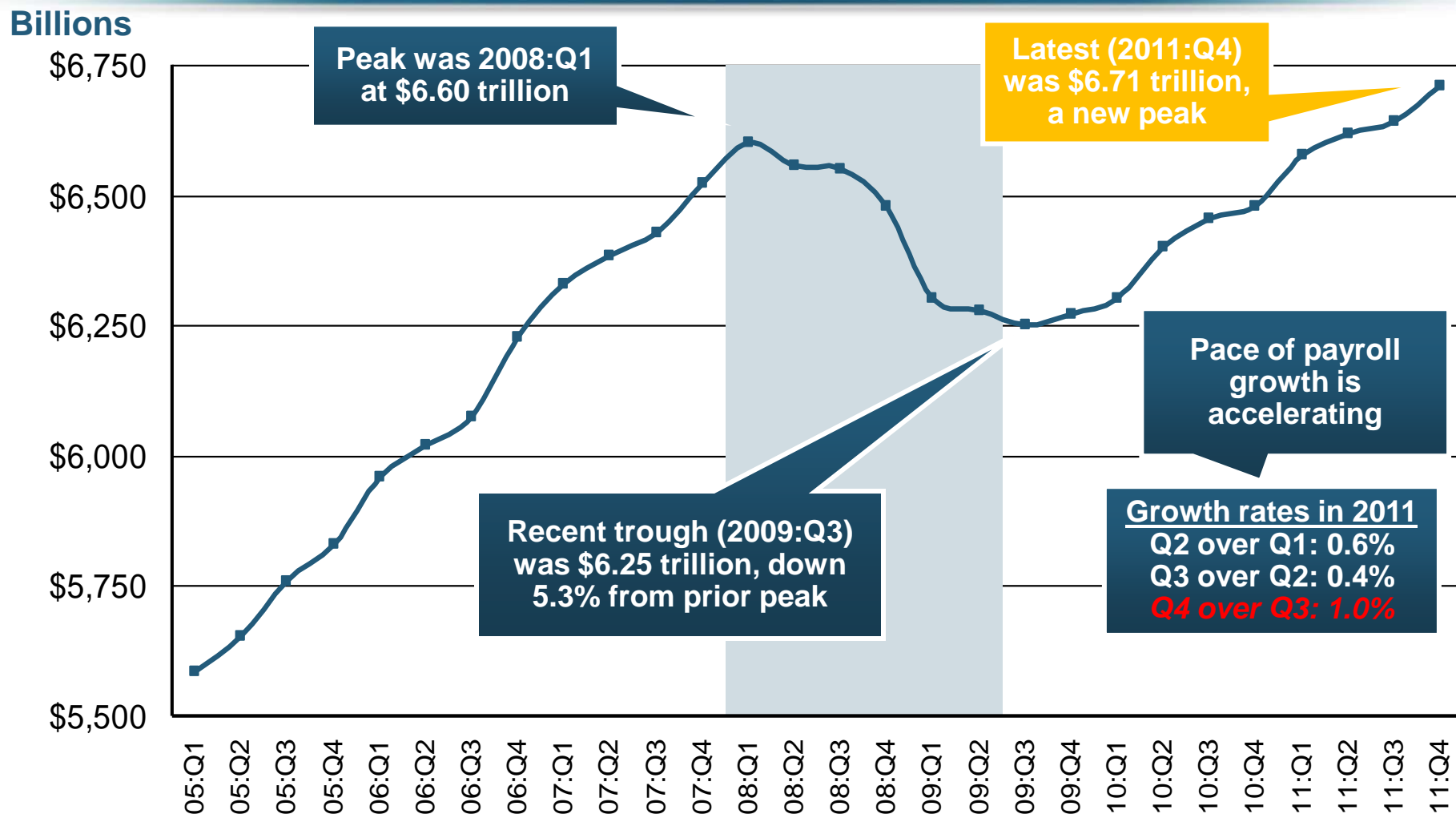
Cumulative Change in Private Employment: Dec. 2007—Feb. 2012

December 2007 through February 2012* (Millions)



Private Employers Added 4.046 million Jobs Since Jan. 2010 After Having Shed 4.66 Million Jobs in 2009 and 3.81 Million in 2008 (State and Local Governments Have Shed Hundreds of Thousands of Jobs)

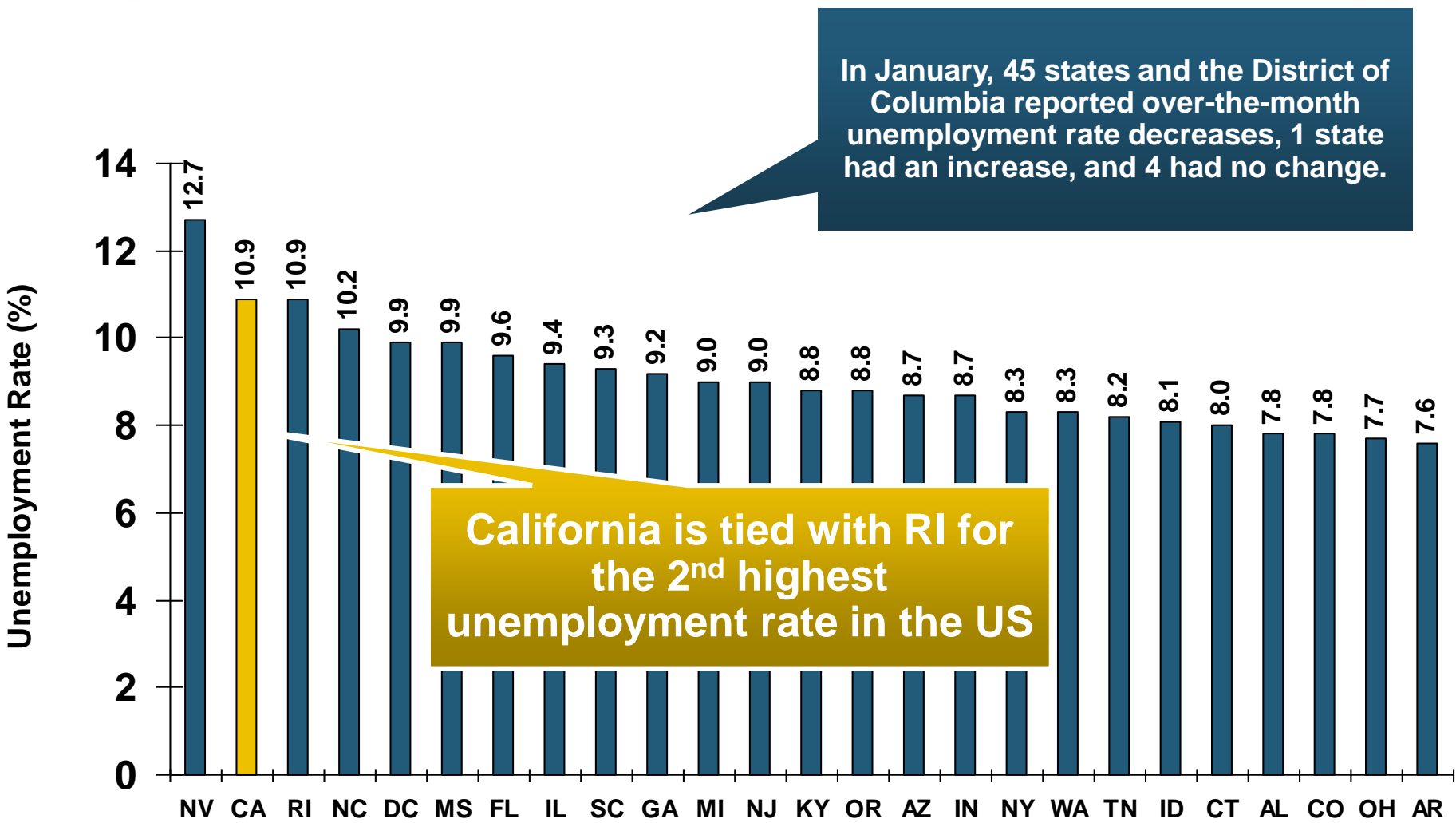
Nonfarm Payroll (Wages and Salaries): Quarterly, 2005–2011:Q4



Note: Recession indicated by gray shaded column. Data are seasonally adjusted annual rates.

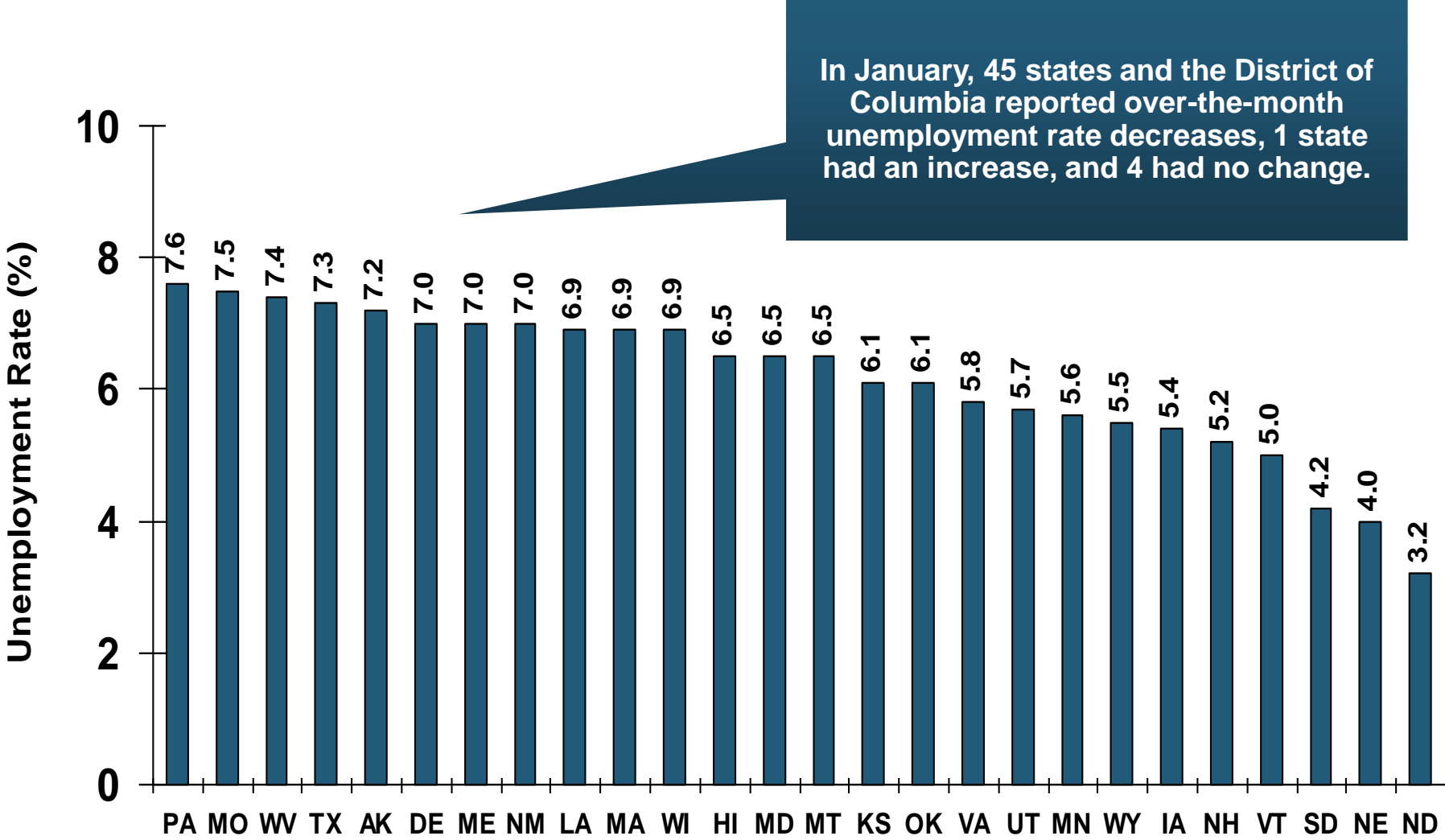
Sources: <http://research.stlouisfed.org/fred2/series/WASCUR>; National Bureau of Economic Research (recession dates); Insurance Information Institute.

Unemployment Rates by State, January 2012: Highest 25 States*



*Provisional figures for January 2012, seasonally adjusted.
Sources: US Bureau of Labor Statistics; Insurance Information Institute.

Unemployment Rates By State, January 2012: Lowest 25 States*



*Provisional figures for January 2012, seasonally adjusted.
Sources: US Bureau of Labor Statistics; Insurance Information Institute.

Inflation

**Is it a Threat to Claim Cost
Severities**

Annual Inflation Rates, (CPI-U, %), 1990–2017F

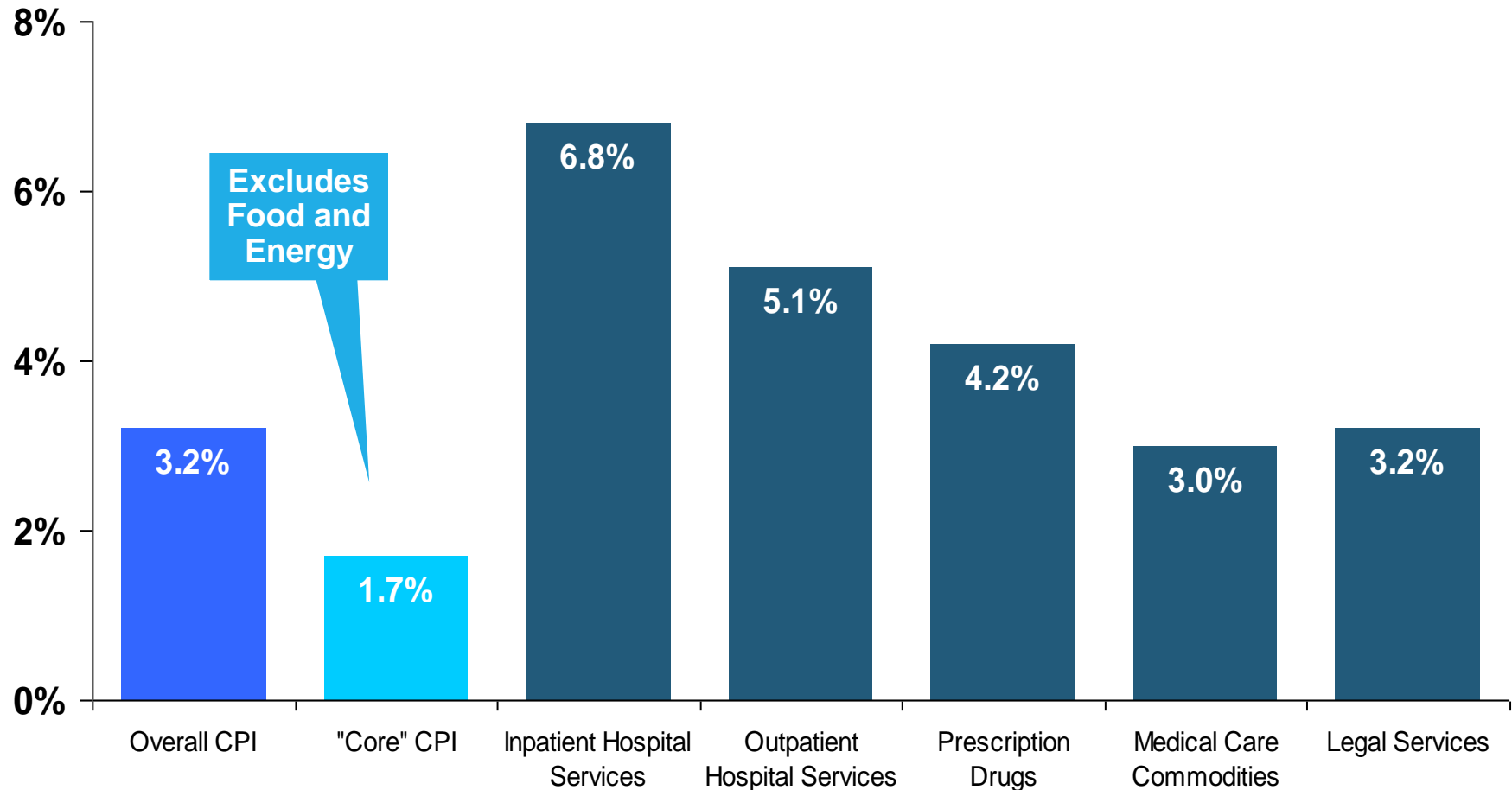
Annual Inflation Rates (%)



The slack in the U.S. economy suggests that inflationary pressures should remain subdued for an extended period of times. Energy, health care and commodity prices, plus U.S. debt burden, remain longer-run concerns

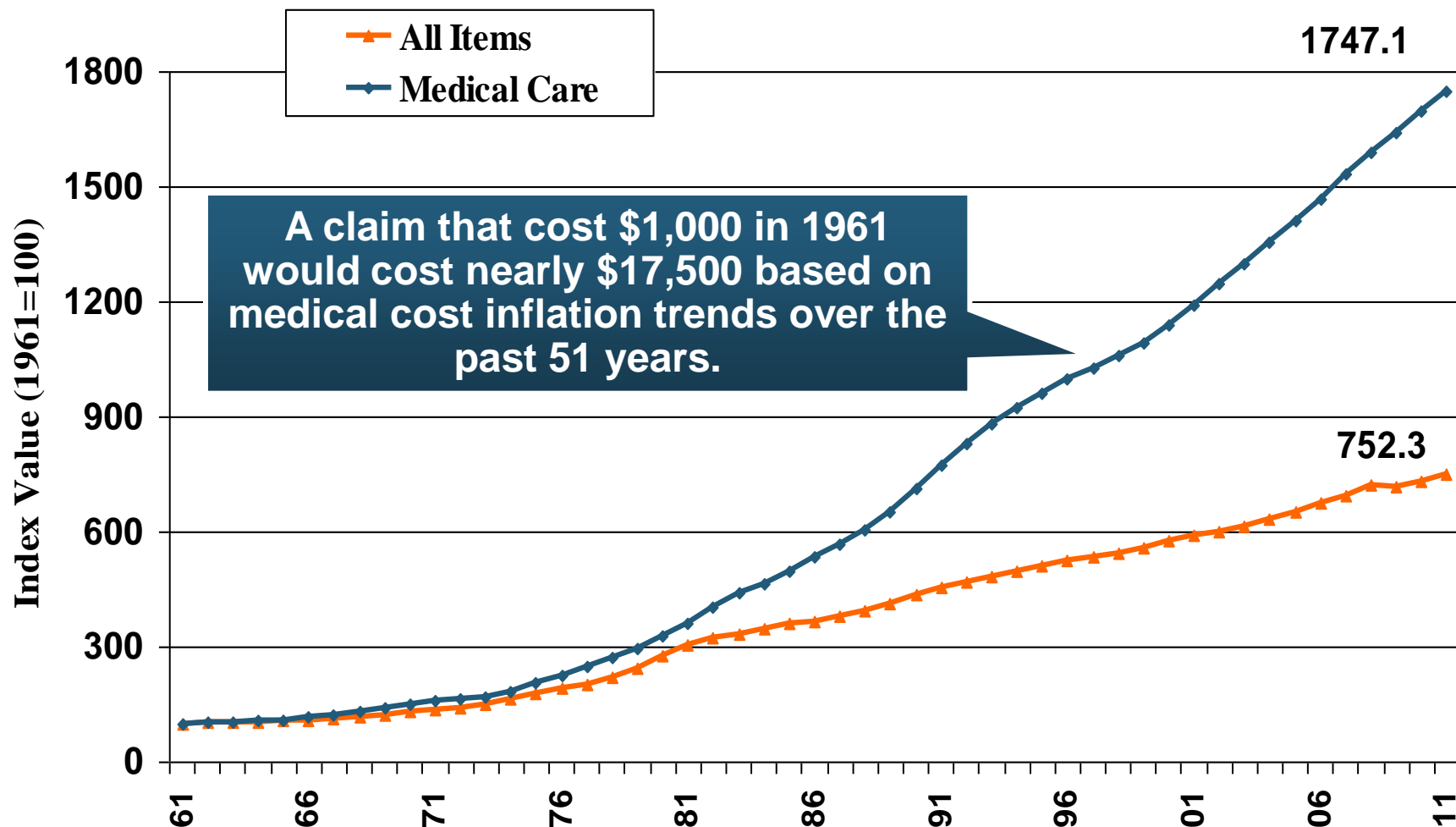
P/C Personal Insurance Claim Cost Drivers Grow Faster Than the Core CPI Suggests

Price Level Change: 2011 vs. 2010



Healthcare costs are a major liability, med pay, and PIP claim cost driver. They are likely to grow faster than the CPI for the next few years, at least

Medical Cost Inflation Has Outpaced Overall Inflation For Over 50 Years



Source: Department of Labor (Bureau of Labor Statistics)



Federal Regulatory Update: ***Dodd-Frank Implementation*** ***Health Care Reform***

A Brief Summary of Implications for Insurers



Dodd-Frank Financial Services Reform & Consumer Protection Act

A Brief Summary of Implications for Insurers

Financial Services Reform: *What does it mean for insurers?*

The Dodd-Frank Wall Street Reform and Consumer Protection Act

■ Systemic Risk and Resolution Authority

- Creates the Financial Stability Oversight Council and the Office of Financial Research
- Imposes heightened federal regulation on large bank holding companies and “systemically risky” nonbank financial companies, including insurers

■ Federal Insurance Office (FIO)

- Establishes the FIO (while maintaining state regulation of insurance) within the Department of Treasury, headed by a Director appointed by the Secretary of Treasury
- FIO will have authority to monitor the insurance industry, identify regulatory gaps that could contribute to systemic crisis
- **CONCERN: FIO morphs into quasi/shadow or actual regulator**

■ Surplus Lines/Reinsurance

- Title V of the Dodd-Frank bill includes, as a separate subtitle, the Nonadmitted and Reinsurance Reform Act (NRRA), which eliminates regulatory inefficiencies associated with surplus lines insurance and reinsurance

Systemic Risk: Oversight & Resolution Authority

Issues Related to Systemic Risk & Resolution Authority

- **Financial Stability Oversight Council created to oversee systemic risk of large financial holding companies) [a.k.a. TOO BIG TOO FAIL]**
 - P/C insurers potentially could be determined to present systemic risk to the financial system and thus be supervised by the Federal Reserve.
 - Such supervision would subject such insurers to prudential standards, if the Council determines that financial distress at the company would pose a threat to the U.S. financial system.
- **Orderly Liquidation**
 - The legislation provides an “Orderly Liquidation Authority” mechanism whereby the FDIC would have enhance powers to resolve distress at financial institutions.
 - Insurance holding companies and any non-insurance subsidiaries of insurers may be subject to this authority.

Federal Insurance Office (FIO): *What Would it Do?*

Duties of the Federal Insurance Office

- **Establishes office within US Treasury headed by a Director appointed by Treasury Secretary, and charged with:**
 - Monitor the insurance industry to gain expertise (oversight extends to all lines of insurance except health insurance, long-term care and federal crop insurance).
 - Identify regulatory gaps that could contribute to a systemic crisis in the insurance industry or the U.S. financial system.
 - Gather information from the insurance industry in order to analyze such data and issue reports. May require insurers, with exception of small insurers which are exempt, to submit data and FIO director can issue subpoenas to gain such info.
 - Deal with international insurance matters.
 - Monitor the extent to which underserved communities have access to affordable insurance products.
 - Assist in administration of the Terrorism Risk Insurance Program (expires end of 2014)

Dodd-Frank Almost 2 Years On: *Status Report*

Expectations vs. Reality



Dodd-Frank Implementation

Status Report for Insurers: Slow Start

The Dodd-Frank Wall Street Reform and Consumer Protection Act

■ Financial Stability Oversight Council—*Slow to Consider Insurer Concerns*

- FSOC deliberates largely behind closed doors
- Criteria and process for designation of Systemically Important Financial Institutions (SIFIs) were not announced until October 12, 2011
 - ***Likely that a small number of US insurers will be designated as SIFIs***
- Operated/deliberated until late September 2011 without a voting member representing the insurance industry
 - ***Roy Woodall, approved by Senate in Sept. 27, 2011, is the sole voting representative for the entire p/c and life insurance industry (was Kentucky Ins. Comm. 1966-1967; Worked in other insurance trade posts, Treasury)***
- Two non-voting FSOC members represent insurance interests:
 - ***FIO Director Michael McRaith (started June 1, 2011)***
 - ***Missouri Insurance Director John Huff (started in Sept. 2010)***
 - ***Not allowed to brief fellow regulators on FSOC discussions***

Dodd-Frank Implementation: *SYSTEMIC RISK CRITERIA*

The Dodd-Frank Act and Systemic Importance

- All Banks with Assets > \$50B Considered Systemically Important
- Non-Bank Financial Groups with Global Consolidated Assets > \$50B Will Be Examined for Systemic Riskiness, But Not Automatically Labeled as a Systemically Important Financial Institution (SIFI)
 - Foreign firms with assets in the US exceeding \$50 billion will also fall under review
- If Firm Exceeds the \$50B Threshold, a 3-Stage Test Applies
- **STAGE 1:** Non-Banks Financial Groups with \$50B+ Assets Will Be Evaluated on Five “Uniform Quantitative Thresholds,” at Least One of Which Will Have to Be Met to Trigger a Further (Stage 2) Review Potentially Leading to a SIFI Designation
 - **Leverage:** Would have to be leveraged more than 15:1 (insurers unlikely to trigger)
 - **ST Debt-to-Assets:** Would have to a ratio of ST debt (less than 12 months to maturity) to consolidate assets exceeding 10%
 - **Debt:** Have total debt exceeding \$20 billion (i.e., loans borrowed and bond issues)
 - **Derivative Liabilities:** Have derivative liabilities exceeding \$3.5 billion
 - **Credit Default Swaps:** Have more than \$30 billion CDS outstanding for which the nonbank financial firm is the reference entity (i.e., CDS written against firm’s failure)
- **Thresholds Considered to Be Guideposts**
 - Not all companies that breach a barrier will be deemed systemically important
 - Regulators retain right to include firms that do meet any of the criteria

Dodd-Frank Implementation: *SYSTEMIC RISK CRITERIA (continued)*

The Dodd-Frank Act and Systemic Importance

- **STAGE 2: Analysis of Firms Triggering Uniform Quantitative Thresholds**
 - Firms triggering one or more of the quantitative thresholds in Stage 1 will be analyzed using publicly available information in order to conduct a more thorough review
 - No data call will be required at this stage
 - Firms viewed as potentially systemically important (candidate SIFIs) will subject to a Stage 3 analysis
- **STAGE 3: Analysis of Candidate Systemically Important Financial Institutions**
 - Firms deemed in Stage 2 to be potentially systemically important will be subjected to more detailed analysis including data not available during the Stage 2 analysis
 - Stage 3 firms will be notified by the FSOC that they are under consideration and will have the opportunity to contest their consideration
- **SIFI DESIGNATION PROCEDURE: 2-Stage Voting Procedure by FSOC is Required Before a Final SIFI Designation is Made**
 - At the conclusion of the Stage 3, FSOC has the authority to propose a firm be designated as a SIFI
 - Requires 2/3 majority vote of FSOC members, including affirmation of the Chair (Treasury Secretary)
 - Potential SIFI firm will be given written explanation for the determination
 - Firm can request a hearing to contest the determination
 - Final determination requires another 2/3 majority of FSOC members and affirmation of the Chair

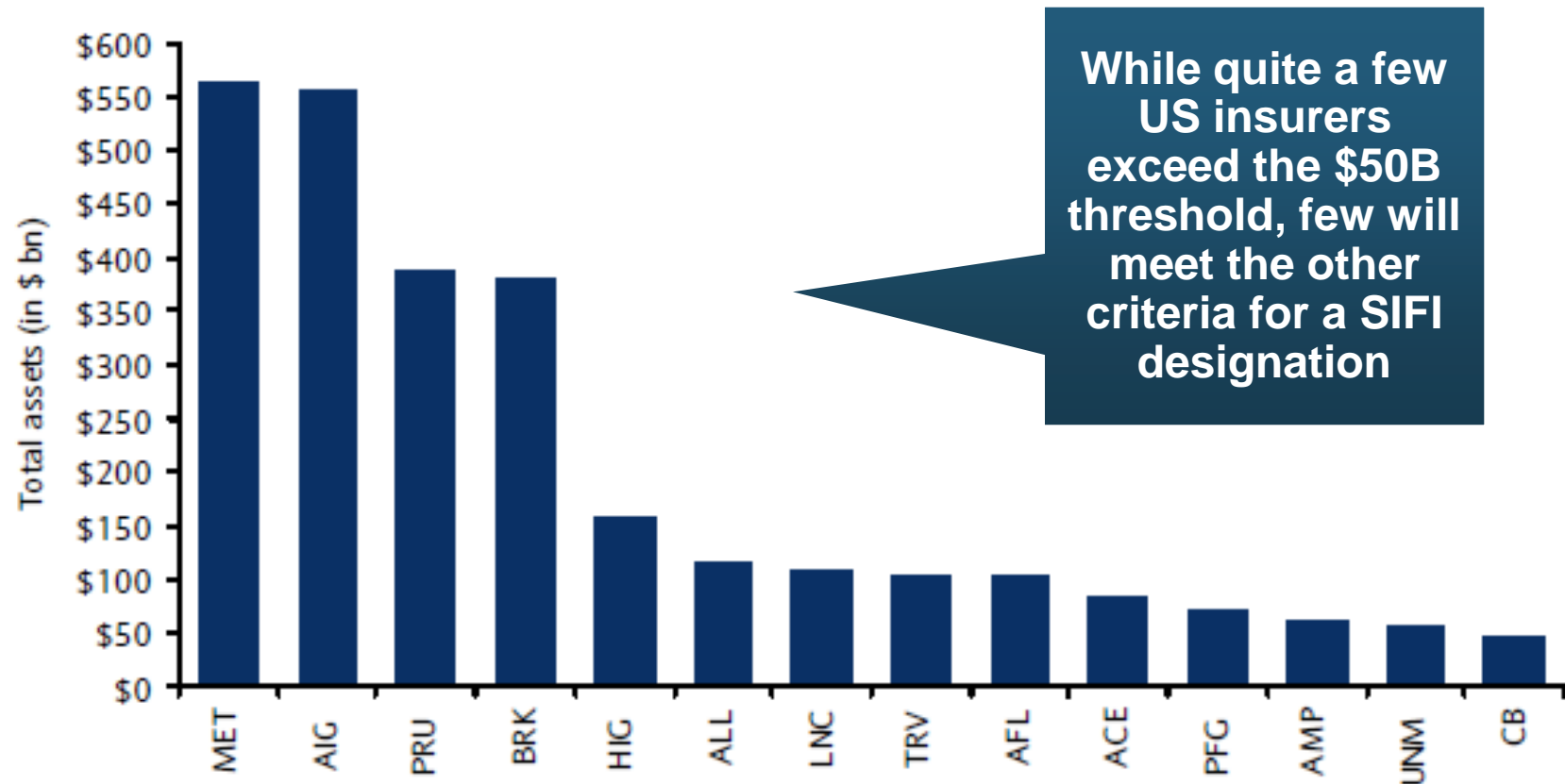
Dodd-Frank Implementation: *FSOC MEMBERS*

The Dodd-Frank Act and Systemic Importance

Members of the Financial Stability Oversight Council

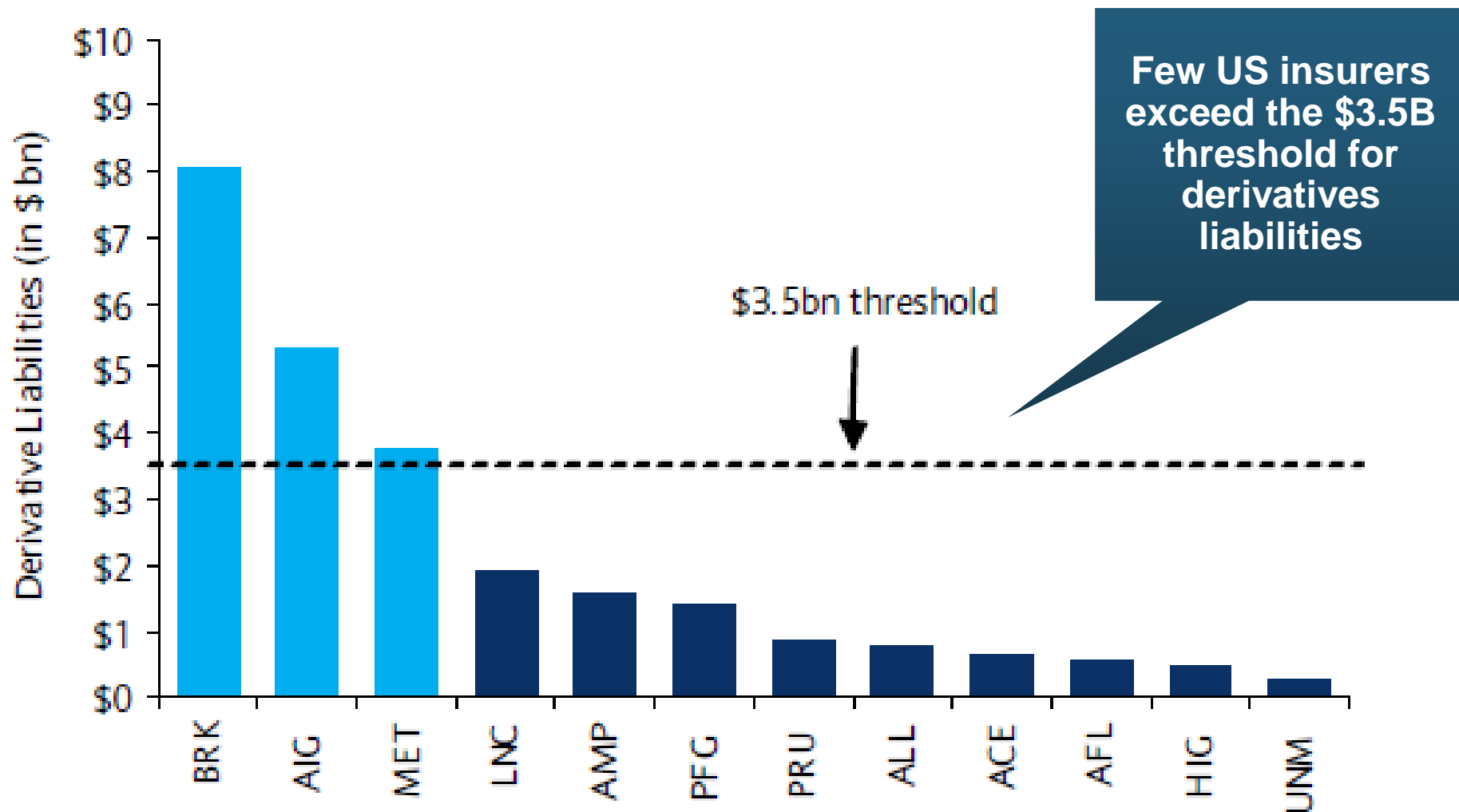
- There are 10 voting members of the FSCO
- **Treasury Secretary and FSOC Chair: Timothy Geithner**
- **Federal Reserve Chairman: Ben Bernanke**
- **Securities & Exchange Commission Chairman: Mary Shapiro**
- **Commodities Futures Trading Commission Chairman: Gary Gensler**
- **National Credit Union Administration Chairman: Debbie Matz**
- **(Acting) Comptroller of the Currency: John Walsh**
- **Federal Housing Finance Agency (Acting) Director: Edward DeMarco**
- **Consumer Financial Protection Bureau Director: Richard Cordray**
- ***Independent Insurance Expert: Roy Woodall***
 - There are 2 nonvoting members of the FSOC representing insurance interests
 - Federal Insurance Office Director Mike McGraith
 - John Huff, Director of the Missouri Insurance Department

Total Assets Greater than \$50 Billion: Publically Traded US Insurers

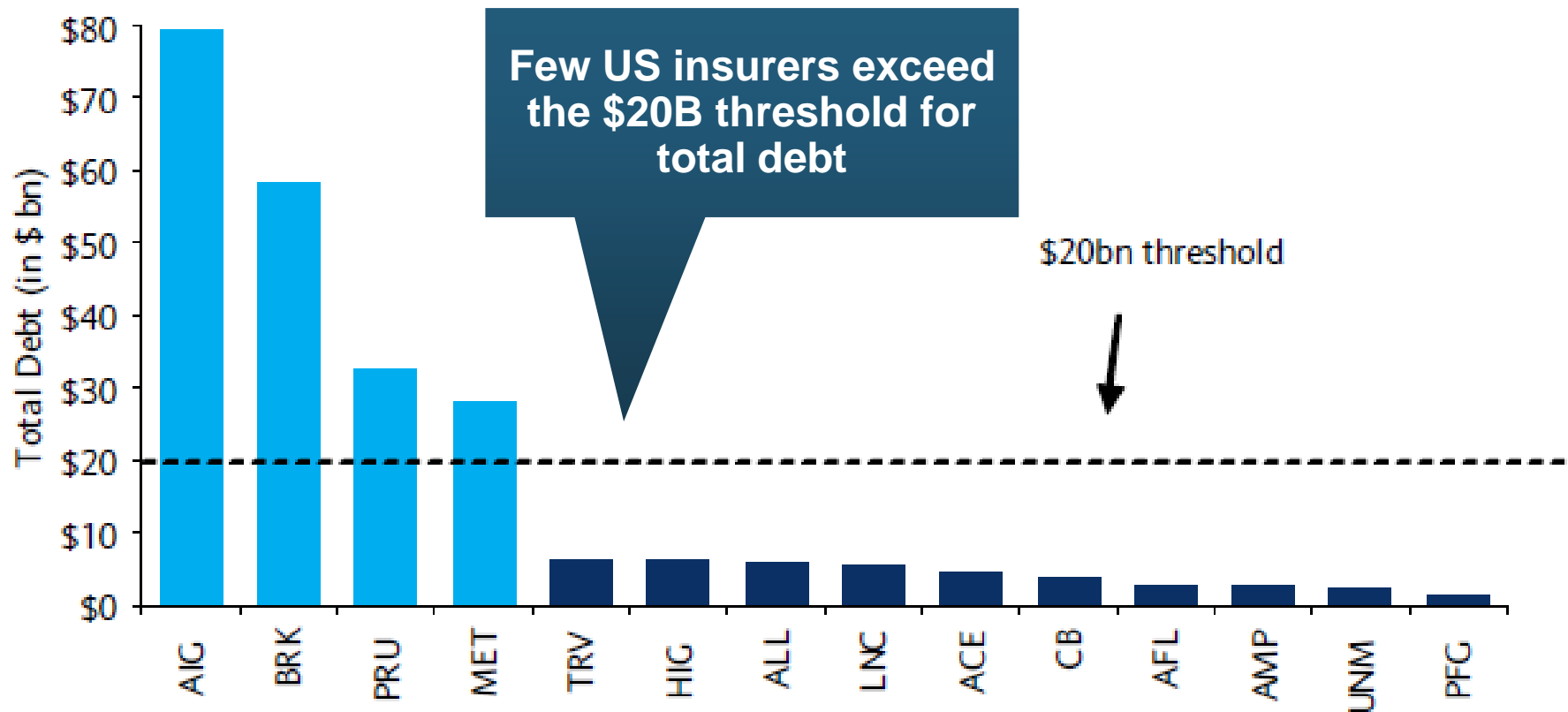


Note: Total assets excluding separate accounts as of 2Q11.

Derivative Liabilities: Publically Traded US Insurers

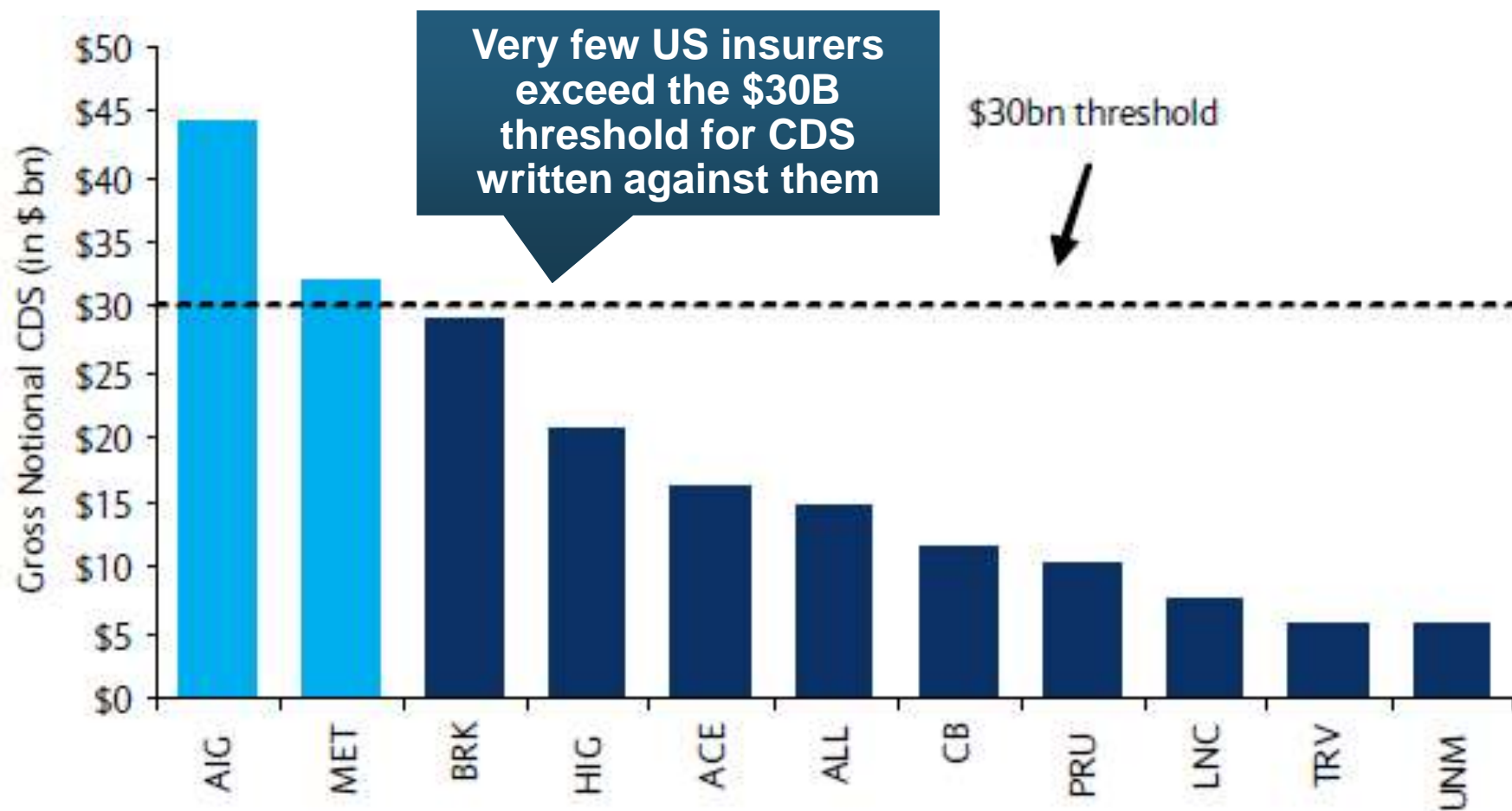


Total Debt: Publically Traded US Insurers



Note: Includes short-term and long-term debt outstanding.

Gross Notional Credit Default Swaps: Publically Traded US Insurers



Note: Gross notional CDS outstanding as of October 7 2011.

Dodd-Frank Implementation: *Federal Insurance Office: Very Quiet*

Federal Insurance Office Update: *Activity Update*

■ FIO's First Director Did Not Assume Office Until June 1, 2011

- Former Illinois Insurance Director Michael McRaith
- Small staff (10-12) and modest budget; Trying to staff up
- McRaith has made relatively few appearances or public comments
- FIO held small conference at Treasury on Dec. 9



■ Study on State of Insurance Regulation Was Due Jan. 2012

- Delayed—April release likely
- Report will likely review previously identified inefficiencies and strengths of current regulatory system with an eye toward modernization.
- Consumer protection could play a larger-than-expected role

■ Treasury Will Exert Heavy Influence on the Report

**Former President of P/C
Insurance at The Hartford**



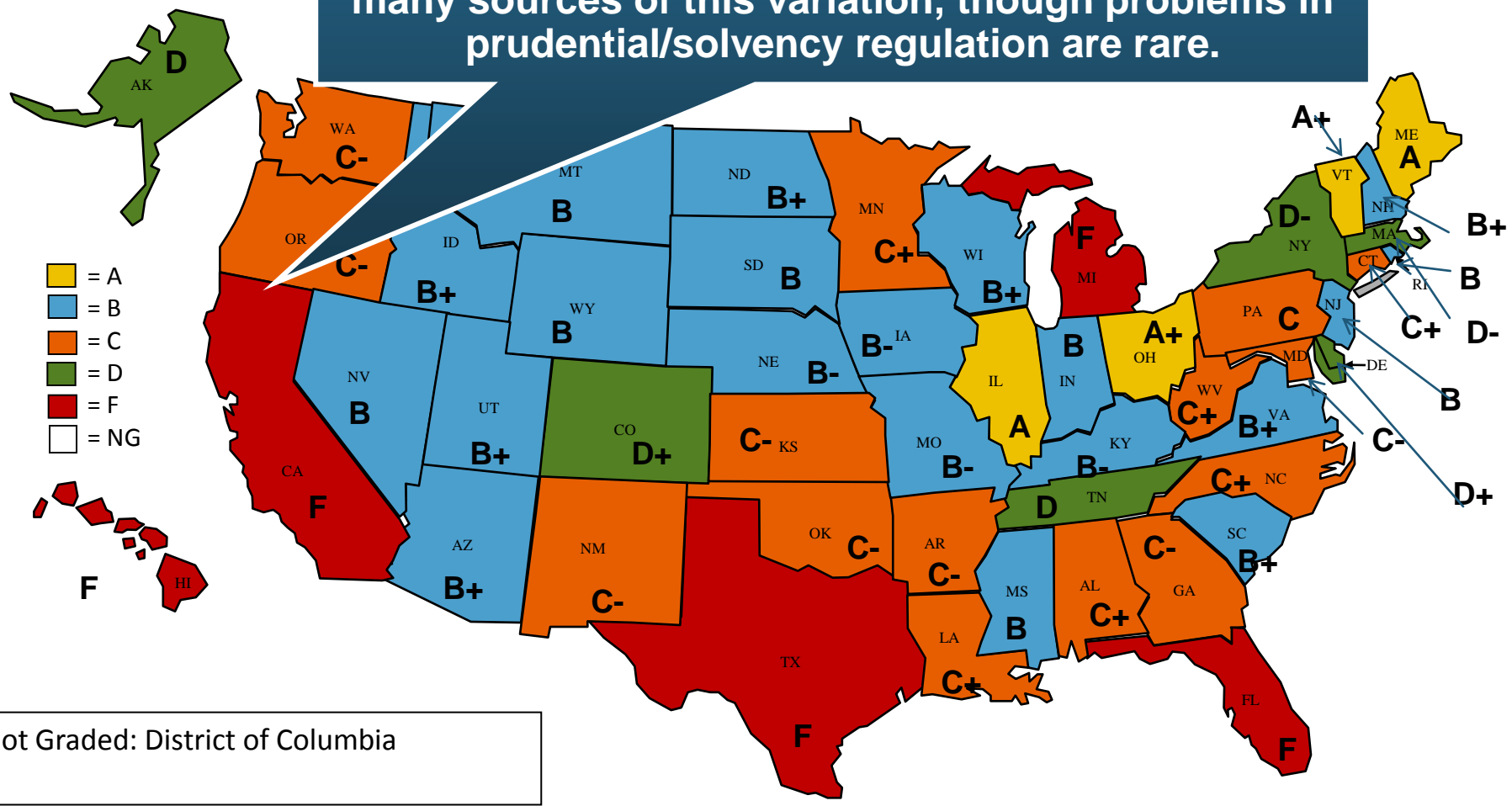
“The states remain the functional regulators, [but] the federal government will work toward modernizing and improving our system of insurance regulation.”

Neal Wolin, Deputy Secretary
Treasury Department

2010 Property & Casualty Insurance Regulatory Report Card: Enormous Variation

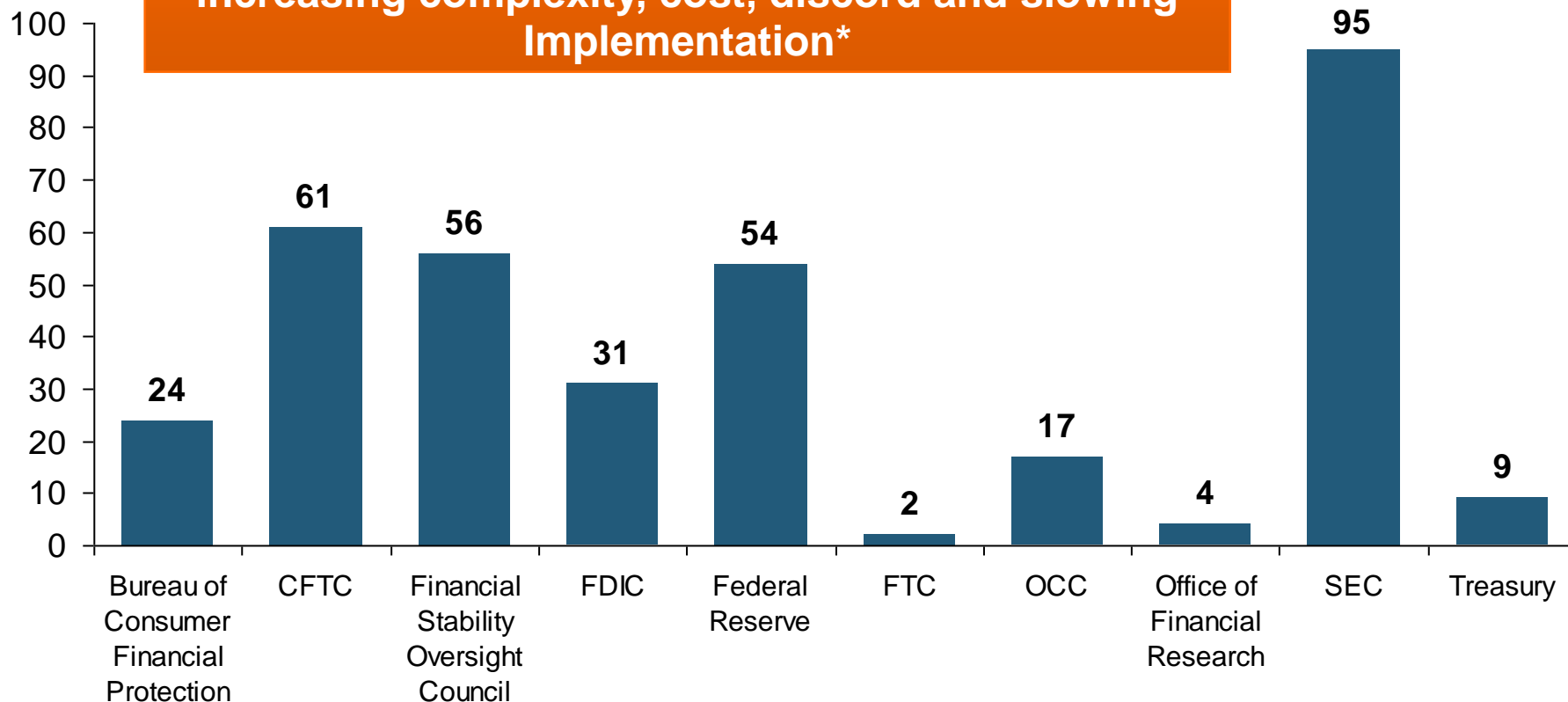


There is enormous variation in the quality of insurance regulation in the United States. There are many sources of this variation, though problems in prudential/solvency regulation are rare.



New Rulemakings Under The Dodd Frank Wall Street Reform and Consumer Protection Act

A total of at least 250-300 new rulemakings are expected under the Dodd-Frank financial reform, increasing complexity, cost, discord and slowing Implementation*



* Total eliminates double counting for joint rule-makings and this estimate only includes explicit rule-makings in the bill, and thus likely represents a significant underestimate.

Source: Wall Street Journal, July 14, 2010; Davis Polk & Wardwell.



Dodd-Frank and Insurance: *The Years Ahead*

**Outlook for Its Medium and Long-
Term Viability & Global Influence**

Dodd-Frank:

What does the future hold for insurers?

Insurance Issues Timeline for Dodd-Frank

■ Short-to-Mid-Term Uncertainty

- Outcome of 250-300 rules across many federal agencies (ETA: months to years)
- Legal challenges to the Dodd-Frank (ETA: Years)
- Outcome of 2012 election (US Senate could fall under Republican control, Republican presidential candidates vow to repeal/revisit reforms) (ETA: 9-21 months)

■ Mid-Term Issues for Insurers

- FIO report in 2012: Will there be renewed effort for federal chartering in the US?
- Federal chartering will reopen a large scale battle within the US insurance industry
- Systemic Risk Designations: Will affect very few US insurers (3-5)
- **CONCERN: FIO morphs into quasi/shadow or actual regulator; CFPB too.**

■ Mid-to-Long-Term Issues for Insurers

- SIFI: Do enhanced capital requirements put them at a competitive disadvantage or is the “Too Big To Fail” designation viewed as an advantage?
- Solvency II: Tough sell in the US right now (Solvency II = Basel III = European Banks)

Dodd-Frank: *Long-term Issues for Insurers & the Dodd-Frank Blueprint*

Insurance Issues Timeline for Dodd-Frank

■ Longer-Term Issues for Insurers

- **Streamlining of Regulation:** Dodd-Frank does little to directly address the inefficiencies of the US insurance regulatory system. (ETA: Many Years, Never)
 - 2012 FIO study will address some of these issues, but likelihood of timely, uniform implementation of recommendations is remote (FIO has no regulatory power; Treasury/Fed powers very limited)
 - Begs questions of regulatory authority: States vs. Federal Government
- **Ultimate Resolution of Regulatory Authority:** (ETA: Years)
 - Possible outcomes: OFC, status quo or bifurcation (life = federal, nonlife = OFC)

■ Can Dodd-Frank Serve as a Blueprint for International Reforms?

- The US is and will remain in a greatly weakened position in terms of its credibility to offer regulatory or policy solutions internationally
- Elements of Dodd-Frank (e.g., derivatives regulation) could prove useful; Systemic risk criteria
- Dodd-Frank provides little guidance on international insurance issues, though FIO will define its role (albeit a narrow one) on this issue



Healthcare Reform & Implications for Workers Compensation

A Status Report

Outline of Discussion Items

- **Summary of the Major Provisions of the Patient Protection and Affordable Care Act (PPACA) of 2010 – popularly known as ObamaCare**
- **Implementation Timetable for Key Provisions of PPACA**
- **Challenges to the Act**
- **Possible Effects on Workers Compensation Benefits/Insurance**

Summary of the Major Provisions of the Patient Protection and Affordable Care Act (PPACA)

**The PPACA (aka “ObamaCare”)
Faces Many Challenges**

1. Provides Access to a Minimum Standard of Private Health Insurance for the Vast Majority of Americans

- No denial of coverage for applicants with pre-existing-conditions
- Young adults can stay on their parents' plan until age 26
- Subsidies for people who cannot afford private insurance
 - Not eligible for subsidies are people who are eligible for Medicare or Medicaid and people who are covered by an employer's plan
- Creates “insurance exchanges”—interstate markets for health insurance policies for individuals and families, and separate exchanges for small businesses
 - Aim is to promote more competition among carriers
 - But federal creation and (where states don't) operation of exchanges, including specifying minimum policy features, is a big step on states' regulatory toes

Major Provisions of the PPACA

2. Expands Eligibility for Medicaid and CHIP (Children's Health Insurance Program)

- These programs are for those too poor to buy private insurance

3. Creates New Apparatus That Might be Activated to Reduce the Projected Rate of Growth in Medicare Payments (and Health Care Expenditures Generally)

4. Creates New Markets for Health Insurance

- Might be operated by the federal government if the states don't want to
- New federal standards for prices and features of some health insurance policies

PPACA: Implementation Timetable for Key Provisions

**Provisions of the PPACA Have
Already Been Enacted Even as the
Act is Challenged in the Courts**

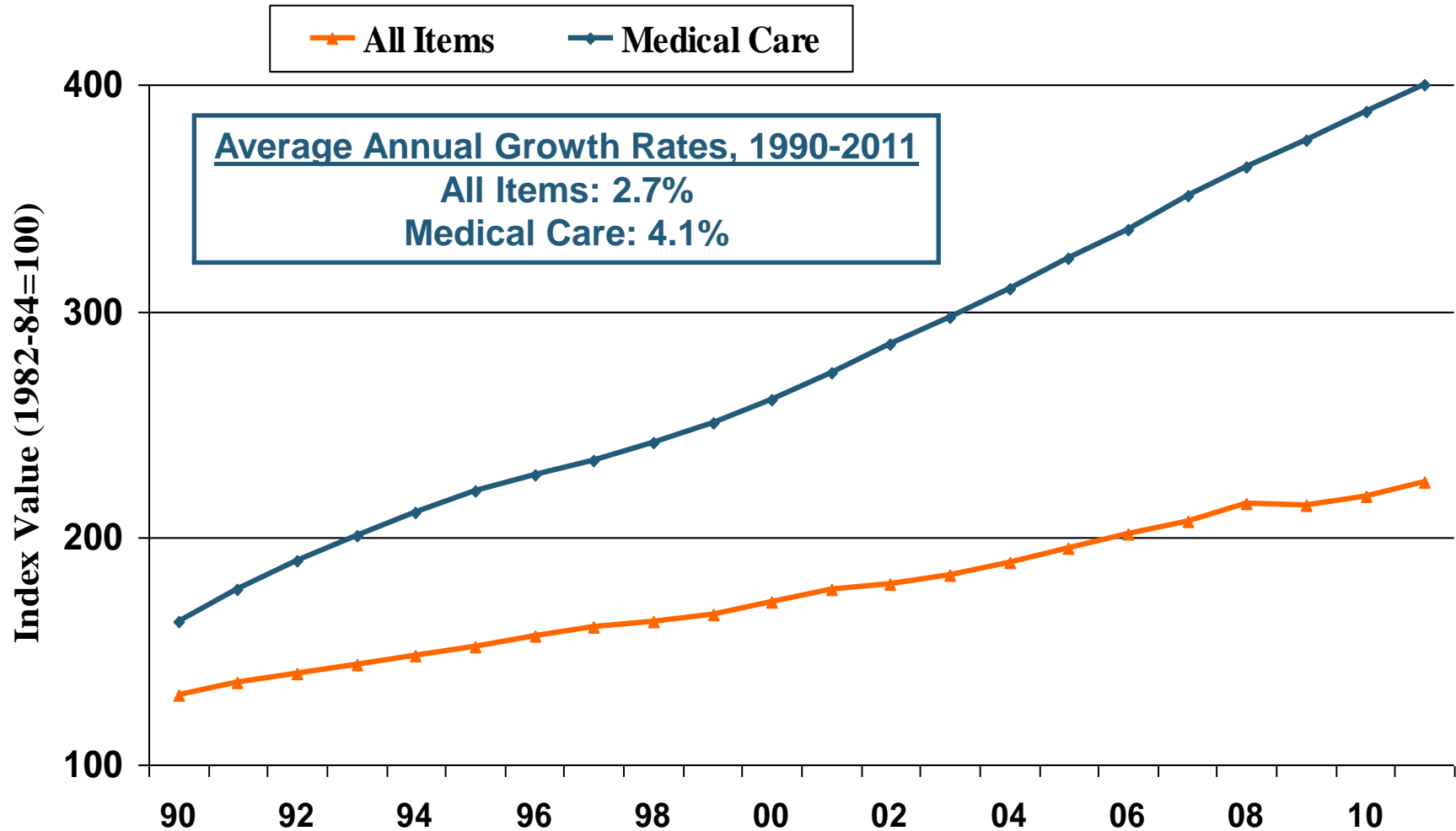
Selected PPACA Provisions that are Already in Effect

1. Independent Payment Advisory Board established

- IPAB makes “recommendations” to trim Medicare spending growth that ***take effect automatically*** if
 - Medicare’s Chief Actuary projects that Medicare per-capita spending growth for the next 5 years will exceed PPACA targets* (determination due by April 30 each year, starting in 2013) and
 - Congress doesn’t vote to achieve same goal by different means
 - First set of IPAB recommendations could be due in January 2014 for implementation in 2015 (depends on Chief Actuary projection)
 - IPAB recommendations can’t
 - ❖ Ration care
 - ❖ Increase taxes or beneficiary premiums and cost-sharing requirements
 - ❖ Change Medicare benefits or eligibility
 - ❖ Reduce low-income subsidies under Part D

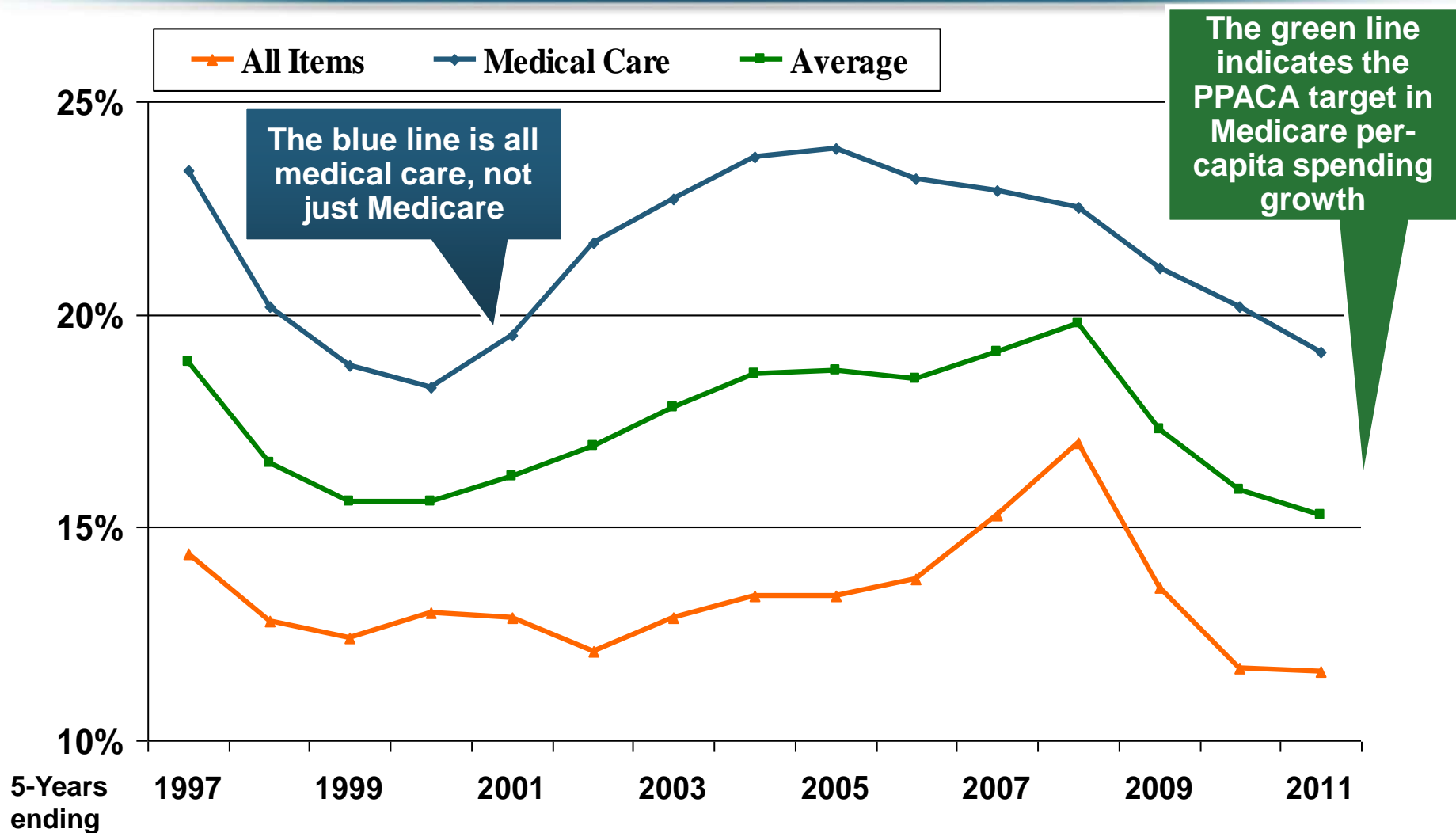
*The target for determinations prior to 2018 is the average of the projected 5-year growth in the CPI-U and the projected 5-year growth in the CPI-M (medical care inflation). In 2018 and beyond, the target is the projected 5-year average growth in nominal per-capita GDP plus 1 percentage point.

Medical Care Prices Have Risen Faster Than Overall Inflation For Many Years



Source: Department of Labor (Bureau of Labor Statistics); Insurance Information Institute.

5-Year Price Growth Rates, Medical Care vs. All Items, 1992-2011



Source: Department of Labor (Bureau of Labor Statistics)

Selected PPACA Provisions that are Already in Effect (cont'd)

- 2. Created State High-Risk Pools for People with Pre-Existing Conditions**
- 3. Insurers' Ability to Enforce Annual Spending Caps is Restricted (completely prohibited by 2014)**
- 4. Children Can Continue Under Parents' Health Insurance Until Age 26**
- 5. Prohibited out-of-pocket costs for preventive services**
- 6. Medicare Expanded to Rural Hospitals and Facilities**
- 7. Medical Loss Ratio Requirements**
 - Policies for individuals and small businesses must be structured to pay out at least specified percentages of premium as benefits

Selected PPACA Provisions that are Already in Effect (cont'd)

8. Patient-Centered Outcomes Research Institute established

- PCORI studies different medical treatments, compares outcomes, effectiveness

9. Health Insurance Cost Disclosure to Employees

- W-2s must report the value of health insurance benefits

10. Enhanced Fraud Detection Programs

Coming Soon: Effective Dates for Selected PPACA Provisions

1. August 1, 2012,

- All new plans must cover certain preventive services without charging a deductible, co-pay, or coinsurance.

2. January 1, 2013, new taxes

- On some “unearned” income, an additional 3.8% on the lesser of (i) net investment income or (ii) the amount of AGI over \$200,000 (\$250,000 for married filing jointly)
- An additional tax of 0.9% on income from self-employment and wages of single individuals in excess of \$200,000 (\$250,000 for married filing jointly).

PPACA Provisions That Take Effect on January 1, 2014

1. Penalty for Not Buying Insurance: 1% of Income

- On individual adults, but at least \$95
- At least \$190 for 2 adults, at least \$285 for 3 or more adults

2. Penalty for Not Providing Insurance (if at least one employee qualifies for a health-tax credit, at employers of 50 or more employees):

- \$2,000 per employee

3. New Excise Taxes

- Tax on health insurance companies, based on their market share
 - Tax rate rises after 2014 to 2018 and then grows with inflation
- 2.3% tax on medical devices (collected at purchase)
- Tax on pharmaceutical companies, based on their market share

4. State Insurance Exchanges Begin Operating

Possible Effects of Affordable Care Act on Workers Compensation

1. Changes in Medicare Reimbursement Levels

- If CMS-authorized Medicare reimbursement levels are modified there could be impacts on states that used Medicare as a basis for reimbursement in their fee schedules. This could affect Physician Fee Schedules, Hospital Fee Schedules (inpatient, outpatient and ambulatory surgical centers)
 - Magnitude of impact depends on (i) when feds make changes to Medicare reimbursements
 - How (if?) states adopt new Medicare reimbursement formula for their own WC fee schedules

2. Reduced Cost Shifting into Workers Comp

- If health care coverage is expanded, presumably the incentive to cost shift is diminished

Possible Effects on Workers Comp (cont'd)

3. Wellness Initiatives

- Affordable Care Act promotes wellness programs which could, over the long run, reduce the incidence and duration of workers comp claims

4. Protecting Consumer Access to Generic Drugs

- One provision of the Act facilitates early entry of generic drugs, which could have a favorable incremental effect on WC pharmaceutical costs

5. New Taxes

- Act calls for new taxes on medical devices, drug manufacturers and health insurance companies

6. Reduction in Fraud and Abuse

- Broad reach of Affordable Care Act combined with enforcement and penalty provisions could reduce fraud and abuse

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4. State Insurance Exchanges Begin Operating

1. Could slow the growth in WC medical care costs

- IPAB recommendations and PCORI reports, plus Medicare changes, could have beneficial effects on cost and treatment effectiveness
- Could reduce cost shifting into workers comp

2. Could be first step in federal regulation of insurance products and markets

- Will regulation like that requiring products to be priced to meet Medical Loss Ratios be applied to WC?
- Will cost-control mechanisms such as the Independent Payment Advisory Board be developed for WC?
- Will WC insurers lose their limited exemption from anti-trust laws that they have had under McCarran-Ferguson since 1945?

Challenges to “ObamaCare”

**Few Acts of Congress Have
Generated Such Intense Debate
and Aroused Such Passions
Among the Public and Politicians**

1. U.S. Supreme Court

- Heard arguments on constitutionality of PPACA on Monday-Wednesday, March 26-28 in rare 3 sessions totaling 6 hours
 - Longest block of time for arguments in 40 years
- Decision expected in June at end of Supreme Court session

2. U.S. Congress

- H.R. 5, the Protecting Access to Healthcare Act,
 - Repeals the Independent Payment Advisory Board
 - An amendment to H.R. 5 repeals, for health insurers, the limited exemption from anti-trust laws that they have had under McCarran-Ferguson since 1945
- All candidates for the Republican presidential nomination and many GOP party leaders have repeatedly stated their intention to repeal the PPACA next year.

- 1. The Obama Administration has already cancelled CLASS**
 - This was to be a major new long-term care insurance program, but the administration concluded that it wasn't "sustainable"

Summary of Supreme Court Hearings on Affordable Care Act

1. Day 1: Anti-Injunction Act

- Anti-Injunction Act dates to an 1867 law asserting that a tax cannot be challenged before it is paid. Court seemed unpersuaded by idea that it could not hear challenges to the Act now even though “penalty” for not complying with the mandate does begin until 2014

2. Day 2: The Mandate to Purchase Coverage

- Court seemed to believe that such a mandate represented an overreach of Congressional authority
- It appears (highly) likely that the mandate will be ruled unconstitutional

3. Day 3: Severing the Mandate & Viability of the ACA

- Unclear that the Act can survive if the mandate is severed. Two issues are inextricably linked to the mandate:
- **Guarantee Issue:** Can't deny coverage due to pre-existing conditions
- **Community Rating:** Everyone charged the same

4. What's Next: Ruling Likely in June

- Will the Court rule to invalidate the entire ACA or rule narrowly on the mandate
- Does that mortally wound the Act: Death by Adverse Selection?
- Will states develop a Plan B?

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