

Management-Labor Advisory Committee Study SB 1558 (2014) and Workers' Benefit Fund Balance

REPORT TO THE LEGISLATURE

December 2018

Management-Labor Advisory Committee

Aida Aranda

Oregon & Southern Idaho Laborers-Employers Training Trust

Kevin Billman

UFCW Local 555

Tammy Bowers

May Trucking Company

Alan Hartley

Management representative

Lynn McNamara

CityCounty Insurance Services

Kathy Nishimoto

Duckwall-Pooley Fruit Company

Ateusa Salemi

Oregon Nurses Association

Diana Winther

IBEW Local 48

Kimberly Wood

Perlo Construction

Cameron Smith

Director, Oregon Department of Consumer & Business Services

Ex-Officio

Theresa Van Winkle

Committee Administrator

The committee extends thanks to Gary Helmer, Senior Economist, Information Technology and Research Section of the Department of Consumer and Business Services, for his expertise and technical support.

Contents

Executive summary4

Purpose of study.....5

SB 1558 background.....5

WBF assessment and fund balance6

WBF programs.....8

WBF long-term liability 12

Factors that affect the WBF fund balance..... 13

Tools to address risks 14

Alternative scenarios 16

Findings and recommendation..... 16

Appendix A - Fund balance scenarios 18

Appendix B – Suggested statutory language 20

Executive summary

Senate Bill 1558 (2014) reduced the required balance of the Workers' Benefit Fund in response to issues with the solvency of several self-insured employer groups. The bill required the Workers' Compensation Management-Labor Advisory Committee (MLAC) to review this change and report to the Legislative Assembly about whether to retain or change the fund balance requirement.

The Workers' Benefit Fund's revenue comes from a cents-per-hour payroll assessment. Employers and employees each pay half of the assessment, currently 2.4 cents per hour worked. The fund pays for a variety of programs that help injured workers and their employers. It provides benefit increases to permanently and totally disabled workers and to families of workers who died as the result of a workplace injury or disease. The fund supports Oregon's return-to-work programs that help injured workers return to work quickly, including financial assistance to employers that hire injured workers. This assistance includes wage subsidies, premium exemptions, and reimbursements for worksite modifications and equipment. As part of this study, MLAC reviewed the statutory programs and expenditures paid from the fund.

MLAC also studied historic fund balances and the effects of past and potential factors that can affect the stability of the fund, including economic downturns, fund transfers and new programs, and catastrophic events. The committee reviewed the agency's tools to address risks if the fund balance declines, including assessment rate changes and program and benefit reductions. To help determine an appropriate fund balance, the committee evaluated several scenarios based on the most recent recession.

MLAC concluded the fund balance should be about one year of expenditures to account for situations in which there is a large decline in revenue, such as a recession or a catastrophic event. At this level, the balance would cushion the impact of these events and allow time for the department and stakeholders to decide how to address expenditures and assessment rates. A larger fund balance enables action to be taken while minimizing volatility in the system.

MLAC unanimously approved the following recommendations:

1. Increase the minimum balance of the Workers' Benefit Fund to 12 months of projected expenditures and clarify that the balance is not entirely in cash.
2. Require the department to report to MLAC if projected expenditures could cause the fund balance to dip below the 12-month requirement. The department's report should include its action plan to address the fund balance situation.

These recommendations require a statutory change.

Purpose of study

The legislature passed Senate Bill 1558 during the 2014 legislative session. The bill was enacted in response to issues with the solvency of several self-insured employer groups. The bill included two provisions related to the required balance of the Workers' Benefit Fund.

- Section 7 of the bill changed the fund balance requirements of the Workers' Benefit Fund (WBF). The original language was:

ORS 656.506 (5) It is the intent of the Legislative Assembly that the department set rates for the collection of assessments ... in a manner so that at the end of the period for which the rates shall be effective, the cash balance shall be an amount **approximating 12 months** of projected expenditures from the Workers' Benefit Fund in regard to its functions and duties ... in a manner that minimizes the volatility of the rates assessed....

The bill changed the language to:

... the cash balance shall be an amount **of not less than six months** of projected expenditures from the Workers' Benefit Fund

- Section 9 of the bill stated:

No later than January 1, 2019, the Workers' Compensation Management-Labor Advisory Committee ... shall study the effects of the amendments to ORS 656.506 by section 7 of this 2014 Act and report to the Legislative Assembly the findings of the committee about the advisability of the continuation of the changes resulting from those amendments.

This report fulfills the legislative reporting requirement in SB 1558. It provides information about SB 1558, the WBF's revenue and funded programs, a history of the WBF's fund balance during the recession, tools used to manage the fund balance, and other considerations.

SB 1558 background

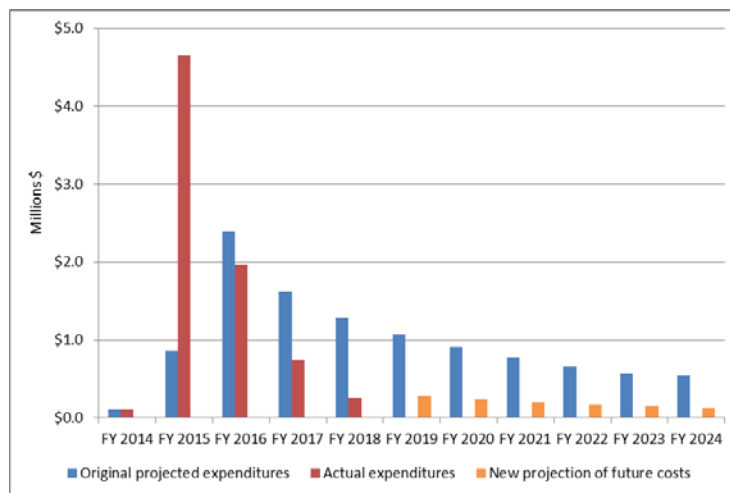
SB 1558¹ (2014) permitted the orderly dissolution of Oregon self-insured employer groups that wanted to disband as a result of financial instability caused by the Great Recession. Three of the seven self-insured groups chose to disband. These groups' reserves were inadequate to pay the claim costs of their injured workers. SB 1558 provided that the WBF would pay claim costs for the employees of members of the

¹ <https://olis.leg.state.or.us/liz/2014R1/Downloads/MeasureDocument/SB1558/Enrolled>

disbanded groups after their reserves were exhausted. It did not provide for the payment of the claim costs of future self-insurer group delinquencies.

The initial projection was that SB 1558-affected claims would cost the WBF about \$10.8 million over the first 10 years, with \$6.3 million being spent by the end of fiscal year (FY) 2018. The claim costs were initially higher, totaling about \$7.7 million by the end of FY 2018, but this was due to a higher-than-projected number of claim settlements in FY 2015, soon after the bill became effective. As a result of these settlements, the ongoing claim costs have been lower than forecast during the past three fiscal years and are expected to remain lower in future years. The SB 1558 costs to the WBF are now expected to be about \$8.9 million over the first 10 years.

Figure 1. WBF expenditures for SB 1558 claims, actual vs. projected expenditures



When the bill was introduced, the WBF’s balance was declining. This prompted the legislature to include the language that changed the fund balance requirement.

WBF assessment and fund balance

The fund’s primary revenue is a cents-per-hour payroll assessment. Employers and employees each pay half of the assessment. Employers send these funds when they file their combined quarterly tax report with the Department of Revenue. The fund also receives investment income and some other revenue, mainly money recovered as a result of audits by WBF compliance staff, fines and penalties, and interest paid on fines and penalties. In FY 2018, \$84.9 million was paid through the assessment.

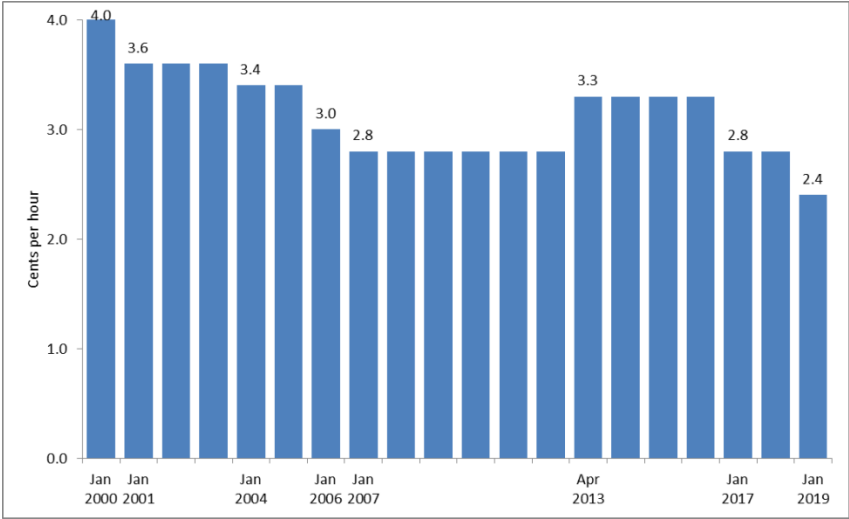
Table 1. WBF revenue, FY 2018 (\$ millions)

	Revenue
Assessments	\$84.9
Other revenue	\$4.5
Total	\$89.4

The DCBS director sets the cents-per-hour assessment rate each fall for the following calendar year. Figure 2 shows the assessment rates since 2000. The director lowered the assessment rate for 2006 and

2007 to reduce the fund balance. This lower rate, combined with the recession, resulted in a rapid decline in the fund balance. In April 2013, the director raised the assessment rate to 3.3 cents per hour to resume fully funding WBF expenditures. Because of declining expenditures, the rate was lowered to 2.8 cents per hour effective Jan. 1, 2017. The rate was lowered again to 2.4 cents per hour effective Jan. 1, 2019.

Figure 2. WBF rates since 2000



The term “equilibrium rate” denotes the assessment rate needed for revenue to equal expenditures. Figure 3 shows a comparison of the assessment rates with the equilibrium rates. When the assessment rate was lowered to 2.8 cents per hour in January 2007, the economic forecast implied the equilibrium rate would be about 3.0 or 3.1 cents per hour for the next five years. During the recession, however, there were fewer assessed hours, and the equilibrium rate rose to 3.5 cents per hour. With the economic recovery and declining Retroactive Program expenditures, the equilibrium rate fell to 2.5 cents per hour in FY 2018.

Figure 3. Assessment rates and equilibrium rates, FY 2006 - FY 2018

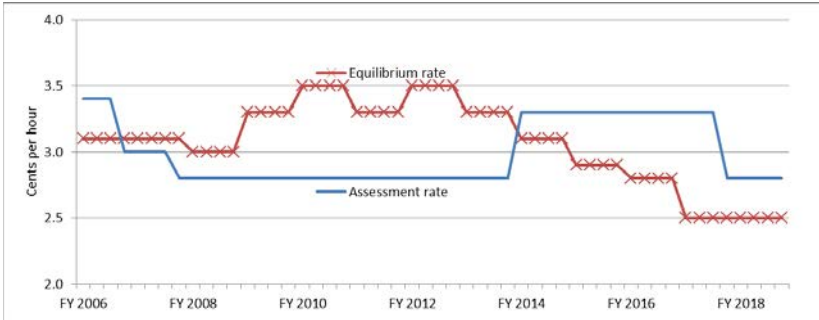


Figure 4 shows the fund balance from the beginning of FY 2006 through FY 2018. The balance was \$168.9 million at the end of FY 2006. The two other lines show 12 months of expenditures (the fund balance requirement before 2014) and six months of expenditures (the requirement since 2014). With the recession and the 2.8 cents-per-hour assessment rate, the fund balance dropped by about \$92 million over

a seven-year period to \$77.0 million at the end of FY 2013. The fund balance was the equivalent of 10 months of expenditures at this point, which led the legislature to lower the fund balance requirement in SB 1558, as Figure 4 illustrates.

The assessment rate was raised to 3.3 cents per hour in April 2013. With the higher assessment rate and the economic recovery, the balance has grown again, reaching \$137.2 million at the end of FY 2018. This is equivalent to 23 months of expenditures.

Figure 4. WBF balance, FY 2006 – FY 2018



This figure illustrates that DCBS went through the Great Recession without increasing the WBF assessment rate or cutting benefits, because the fund entered the recession with a large fund balance. The fund balance was drawn down by 13 months of expenditures over a seven-year period. The appendix includes a discussion of two scenarios that illustrate the decisions that would have been necessary if the fund balance had been lower before the recession.

WBF programs

About 90 percent of the fund's expenditures pay for programs authorized by law. Table 2 shows the program expenditures for the past three fiscal years. Program descriptions follow the table.

Table 2. WBF program expenditures, FY 2016 – FY 2018 (\$ millions)

WBF Program Expenditures:	FY 2016	FY 2017	FY 2018
Retroactive Program	\$41,412	\$39,628	\$38,820
Reemp. Assistance Program (RAP)	26,507	24,992	27,181
RAP: EAIP	19,824	18,040	19,389
RAP: PWP wage subsidy, workiste mod.	4,342	4,436	5,531
RAP: PWP claims costs	2,339	2,513	2,260
RAP: Other programs	0,002	0,004	0,000
Reopened Claims Program	3,809	3,635	3,328
Workers with Disabilities Program	0,321	0,222	0,215
SB 485 Supplemental Disability	0,870	0,888	0,944
SB 1558 Claim Payments	1,960	0,744	0,254
Total WBF Program Expenditures	\$74,879	\$70,109	\$70,741

Retroactive Program

The Retroactive Program pays for benefit increases to workers and their beneficiaries. Insurers and self-insured employers pay the adjusted benefits and then request reimbursement from the division. In HB 2337 and HB 2338, the 2017 legislature increased permanent total disability (PTD) and death benefits, which will increase the amount of reimbursement requests for benefit adjustments. In FY 2018, the program had \$38.8 million in expenditures, which accounted for 55 percent of WBF program expenditures.

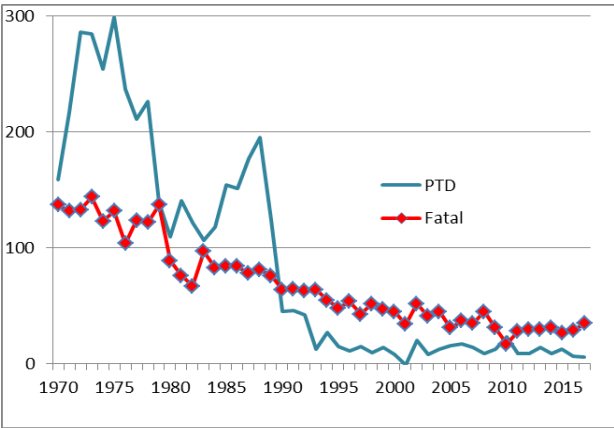
Table 3 shows an example of the program's WBF costs. Suppose a claim had an initial benefit of \$1,000, and average wages increase 2 percent a year. In the first year, the insurer would pay the entire \$1,000. In the second year, the benefit paid would be \$1,020; the insurer would be responsible for \$1,000 and the WBF would reimburse the insurer for the \$20 adjustment. In each subsequent year, the WBF responsibility increases and, after 20 years, the WBF would reimburse \$457 of the \$1,457 benefit.

Table 3. Retroactive Program example

Year	Insurer paid	WBF reimbursed	Beneficiary total
1	\$1,000	\$0	\$1,000
2	\$1,000	\$20	\$1,020
3	\$1,000	\$40	\$1,040
4	\$1,000	\$61	\$1,061
5	\$1,000	\$82	\$1,082
10	\$1,000	\$195	\$1,195
20	\$1,000	\$457	\$1,457

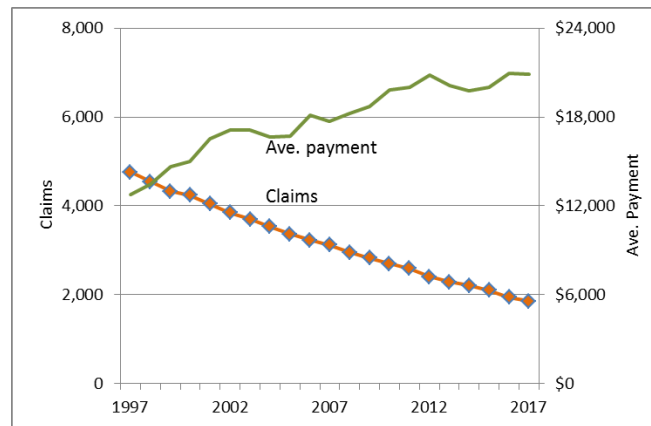
The next two figures illustrate the Retroactive Program's trends. Few new claims are entering the program. During the 1970s, there was, on average, one new fatal or PTD claim each day; over the past decade, there was fewer than one new fatal or PTD claim each week.

Figure 5. New fatal and PTD claims, 1970-2017



In 2017, WBF payments were made on 1,848 claims. About two-thirds of these claims and 85 percent of the expenditures were for injuries that occurred before 1990. The number of claims for which payments were made has been declining by 5 percent per year. The average payment on the remaining claims has been increasing by just 1 percent per year. The combination of these two trends means that Retroactive Program expenditures should continue to decline.

Figure 6. Retroactive Program claims and average annual payment, 1997-2017



Reemployment Assistance Program

The Reemployment Assistance Program provides incentives for returning injured workers to jobs. The major programs are the Employer-at-Injury Program (EAIP) and the Preferred Worker Program (PWP); there are also other smaller programs paid in this category.² In FY 2018, the program's expenditures were 38 percent of WBF program expenditures.

EAIP provides incentives to return workers to regular work before claim closure. The program is managed by insurers and self-insured employers. Benefits available to employers and their injured workers include wage subsidy, worksite modifications, and work-related purchases. Since 2008, about 25 percent of claimants with an accepted disabling claim have participated in EAIP. In addition, about 3,000 workers with nondisabling claims use the program each year. The program has been shown to return workers to their jobs more quickly than they would otherwise. This lowers the amount of temporary disability paid by insurers.

PWP is designed to assist injured workers who suffer a permanent disability and who are unable to return to regular work. The program is managed by the Workers' Compensation Division. PWP pays for wage subsidies, direct employment purchases, and worksite modifications. Also, if a worker hired through PWP has a new injury during the first three years of re-employment, the WBF pays the costs, including administrative costs, of this new claim.

² The accounting system includes payments to the Oregon Institute for Occupational Health Sciences (OIOHS) in this expenditure category. These payments are removed from Table 2; they are included in Table 4.

Reopened Claims Program

This program provides reimbursement to insurers and self-insured employers for costs arising from certain claim costs associated with the Workers' Compensation Board's Own Motion (BOM) orders. A BOM order may authorize benefits in three circumstances:

- For claims with a date of injury before Jan. 1, 1966, medical benefits can be authorized.
- For all claims, temporary disability benefit payments can be authorized when, five years after claim closure, the worsening of a compensable injury requires inpatient surgery, outpatient surgery, or any treatment requiring hospitalization.
- For claims with new or omitted medical conditions, SB 485 (2001) authorized the Workers' Compensation Board to grant permanent partial disability (PPD) benefits.

Reopened Claims Program expenditures were about \$3.3 million in FY 2018. More than 70 percent of expenditures were for temporary disability benefits, and 20 percent were for PPD benefits. Because medical benefits are limited to injuries before January 1966, few claims received medical payments; individual medical payments can be large.

Workers with Disabilities Program

This program was created by the legislature in 1981. Senate Bill 1197 (1990) restricted the program to claims for which the application for reimbursement had been made before May 1, 1990. The program provides reimbursement to employers or insurers for costs in excess of \$1,000 for injuries suffered or caused by previously disabled workers. About \$215,000 was paid in FY 2018, and the program expenditures will continue to decline.

Senate Bill 485 – Supplemental Disability Benefits

In 2001, Senate Bill 485 added a new component to the WBF. SB 485 allowed wages from multiple jobs (called supplemental disability benefits) to be considered in temporary disability computations. Previously, only the wages from the job at injury could be used in these calculations. This provision was effective for claims on injuries that occurred on or after Jan. 1, 2002. The insurers' payments for the jobs other than the job at injury are reimbursed from the WBF.

Noncomplying Employers (NCE) Program

The NCE program revenue flows through the WBF. The revenue includes NCE recoveries, NCE fines and penalties, and NCE interest. The expenditures are payments to the NCE claims administrator. The NCE expenditures totaled \$4.2 million in FY 2018. In the event that expenditures exceed revenue, there is a transfer from the Premium Assessment Operating Account (PAOA) to cover the difference; when revenues exceed expenditures, the excess is transferred to PAOA. Although the NCE funds are housed in the WBF, the program is not funded by the WBF assessment. Also, NCE expenditures are excluded from the calculation of the number of months that the WBF covers.

WBF administrative expenditures

In FY 2018, state agency administrative expenditures were \$5.7 million. Of this amount, about \$3.0 million were Department of Consumer and Business Services (DCBS) expenditures, and about \$2.7 million were paid to other state agencies as authorized by law. This is shown in Table 4.

By statute, DCBS makes payments of 1/16th of a cent per hour worked from the WBF to the Oregon Institute of Occupational Health Sciences (OIOHS) at Oregon Health & Science University. These amounts are matched by equal payments from PAOA and fund OIOHS's operations. The Employment Department and the Department of Revenue receive funds to cover the costs of collecting the WBF assessment. The Bureau of Labor and Industries (BOLI) receives payments for the enforcement of anti-discrimination laws.

Table 4. WBF administrative expenditures, FY 2016 – FY 2018 (\$ millions)

WBF Administrative Expenditures	FY 2016	FY 2017	FY 2018
DCBS expenditures	\$5.217	\$5.182	\$2.974
OIOHS (formerly CROET)	1.782	1.918	1.793
Employment & Revenue collection costs	0.633	0.659	0.682
BOLI costs	0.382	0.382	0.250
Total WBF Admin. Expenditures, exc. NCE	\$8.014	\$8.141	\$5.698

WBF long-term liability

DCBS is required to estimate the future viability of the WBF. The figure shows the estimated present value of forecast WBF payments³ for claims with injuries that have occurred as of June 30, 2018. If the current programs and benefits were retained, the estimated present value of the WBF reserve liabilities was almost \$830 million. This long-term liability is declining by about 3 percent per year as the number of Retroactive Program claims declines.

Table 5. WBF long-term liability as of 6/30/2018 (\$ millions)

Retroactive Program	\$760.1
Reemployment Assistance	45.3
Reopened Claims	22.5
Workers with Disabilities	1.5
SB 1558 Self-Insured Group Claims	0.5
Total (\$ millions)	\$829.9

As mentioned earlier, the WBF had a fund balance of \$137 million at the end of June 2018. This table illustrates that while the fund balance is large, it has a large long-term liability that is not funded. The current statutory language does not account for this liability.

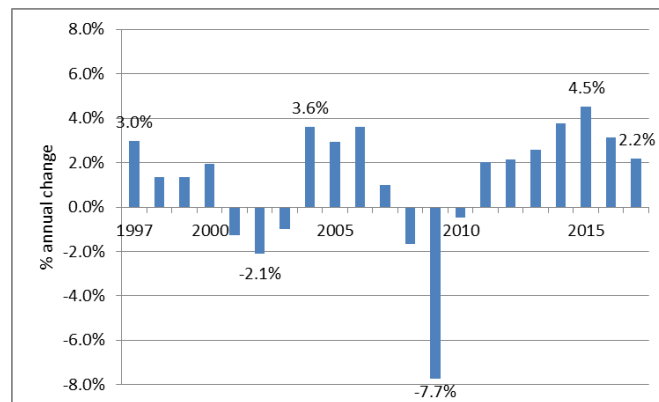
³ The table excludes the Non-complying Employer Program liability.

Factors that affect the WBF fund balance

Economic downturns

Because the WBF is funded by a per-hour assessment, changes in work hours due to changes in total employment quickly affect the fund balance. A drop in employment in one quarter will result in a revenue drop the next quarter. Figure 7 shows the annual percentage change in the work hours covered by the WBF assessment.

Figure 7. Percentage change in WBF assessable hours, 1997-2017



The department's forecast of WBF assessment revenue is based on the employment forecasts from the Oregon Office of Economic Analysis and the department's hours-per-employee forecasts. The one-year-ahead assessment revenue forecasts are generally accurate. The assessment revenue has been within 1 percent of the forecast in nine of the past 19 years and has been within 3 percent of the forecast every year except FY 2009. Longer range forecasts are less accurate because small differences compound over time.

Fund transfers and new programs

The legislature can change the statutory uses of WBF revenue. In FY 2004, the legislature transferred about \$250,000 from the WBF to the General Fund to reduce a deficit. The legislature has also added programs and modified benefits. Changes have included:

- 1999 – HB 2022 modified PTD and death benefits
- 2001 – SB 485 allowed for payment of temporary disability payments for secondary jobs and for PPD payments included in Board Own Motion orders
- 2009 – SB 110 modified PTD and death benefits
- 2014 – SB 1558 allowed for the payment of claim costs for dissolved self-insured employer groups
- 2017 – HB 2337 and HB 2338 expanded PTD and death benefits

Catastrophic events

The following is from the Oregon Office of Emergency Management.

When, not if, the next great Cascadia subduction zone earthquake strikes the Pacific Northwest, Oregon will face the greatest challenge in its history. Oregon's buildings, transportation network, utilities, and population are simply not prepared for such an event. Were it to occur today, thousands of Oregonians would die, and economic losses would be at least \$32 billion. In their current state, our buildings and lifelines (transportation, energy, telecommunications, and water/wastewater systems) would be damaged so severely that it would take three months to a year to restore full service in the western valleys, more than a year in the hardest-hit coastal areas, and many years in the coastal communities inundated by the tsunami. Experience from past disasters has shown that businesses will move or fail if services cannot be restored in one month; so Oregon faces a very real threat of permanent population loss and long-term economic decline.⁴

The report estimated 650 to 5,000 deaths caused by the earthquake, with another 600 to 5,000 deaths due to the tsunami. People who die at work during an earthquake, other natural disasters, or acts of terrorism, would have compensable claims, creating a new, long-term liability on the WBF. An earthquake could also significantly reduce revenue due to the job loss.

It is beyond the scope of this report to estimate the effect on the WBF from a major earthquake. WBF costs would depend not only on the number of worker deaths, but also on the survival of their dependents. However, in the latest valuation of the Retroactive Program, it was estimated that the WBF case reserves for fatal claims with CY 2011 – 2015 dates of injury was \$32.4 million. There were 146 compensable fatalities during that period. This suggests that if the earthquake would occur in the near future, the WBF would have a liability of about \$20 million for every 100 compensable fatalities. This is another liability for which there is no current reserve.

Tools to address risks

DCBS is funded through a large number of fees and assessments, and it manages many dedicated accounts. The department has established a policy to handle these accounts and to set assessment rates. When setting rates, DCBS strives to:

- Meet the cash flow needs of the program
- Accommodate the timing of receipts and expenditures
- Ensure stable funding for legislatively approved programs and services during uncertain economic times
- Minimize the volatility of fees and assessments on regulated industries and the consumers they serve.

⁴ https://www.oregon.gov/oem/Documents/01_ORP_Cascadia.pdf, The Oregon Resilience Plan, 2013, downloaded, July 9, 2018

The goals of stable funding and minimal fee volatility can be somewhat contradictory. Earlier, Figure 3 showed the equilibrium and assessed rates. The equilibrium rates have changed every year. A policy that focuses on fund stability would necessitate a change in the assessment rate nearly every year. This can cause confusion for employers. Department assessment staff members note that many employers have difficulty reporting correctly when the assessment rate changes.

There are several tools for addressing fund balance issues. For the WBF, these include:

- Drawing down the fund balance
- Increasing assessments to generate more revenue
- Decreasing administrative expenditures
- Reducing benefits

Because one of the department's goals is to minimize rate volatility, the window for planning assessment rates spans a five-year period. In doing so, it is common to draw down fund balances for a period of time. This is done most often when it appears future economic growth will be strong enough to overcome a short-term deficit.

The department used two of the other tools in 2013 to reverse the decline in the WBF fund balance. First, the department raised the assessment rate from 2.8 cents per hour to 3.3 cents per hour in April 2013. This raised about \$14 million a year in additional revenue. Second, the division reduced EAIP benefits. Following stakeholder meetings and a public hearing, the division changed its administrative rules and reduced the EAIP wage subsidy from 50 percent to 45 percent of wages for programs starting after July 1, 2013. This reduced expenditures by about \$1.7 million per year.

ORS 656.506 (7), which defines the Retroactive Program, also provides a mechanism for reducing benefits. (The language is bolded for emphasis):

Notwithstanding the formulas for computing benefits provided in ORS 656.204, 656.206, 656.208 and 656.210⁵, the increased benefits payable under this subsection shall be in such amount as the director considers appropriate. The director annually shall compute the amount which may be available during the succeeding year for payment of such increased benefits and determine the level of benefits to be paid during such year. **If, during such year, it is determined by the director that there are insufficient funds to increase benefits to the level fixed by the director, the director may reduce the level of benefits payable under this subsection.**

The last sentence gives the director the authority to reduce benefits if needed to keep the fund solvent. ORS 656.625 has similar language covering the reopened claims program.

One of the constraints on the department's ability to manage the WBF fund balance is the length of time it takes to implement changes. According to ORS 656.506(4), the assessment rate can be changed once a year. The assessment rate is set based on the August economic forecast, takes effect in January of the

⁵ These sections cover death benefits, PTD benefits, PTD benefits following death, and supplemental disability wage benefits.

following year, and the affected revenue is paid beginning in May. Therefore, there is a nine-month period between the assessment rate decision and the resulting revenue.

To control expenditures, DCBS can make some WBF administrative cuts fairly quickly. The first step is to freeze hiring and stop the purchase of supplies. The next step is to move staff members from WBF-funded positions or to begin layoffs. There are more constraints on the other administrative expenditures. The OIOHS expenditures are statutory requirements, and the payments to other agencies are contractual obligations that would require time to change.

The director does have the statutory authority to not make payments for programs such as retroactive benefit payments. However, program cuts would normally go through stakeholder meetings and the rulemaking process, which normally takes three to six months.

While the director can change the administrative rules for return-to-work programs, the effect would not be immediate. For example, the 2013 EAIP wage subsidy rule change applied to new EAIP usage. However, insurers have one year and 30 days from claim closure to request reimbursement from the WBF. Therefore, the rule change did not result in an immediate expenditure reduction. This would be true for most return-to-work program changes.

Alternative scenarios

Earlier, it was shown that the department went through the Great Recession without raising the assessment or cutting program benefits. This was possible only because the WBF had a large fund balance, equal to 23 months of expenditures, before the recession. We modeled two scenarios in which the fund balance was lower before the recession. See Appendix A for the scenarios. They show the decisions that would have been needed in these situations. The department would have had to make large program cuts or increase assessment rates during the recession.

Findings and recommendation

This study has shown that the Workers' Benefit Fund needs to have a sufficient fund balance in situations where there is a large decline in revenue. The fund needs a sufficient balance to last for a year, during which the fund balance is drawn down, while the department and stakeholders make decisions about the balance. A larger fund balance enables action to be taken while minimizing volatility in the system. Following is a list of the benefits of having a large fund balance:

- It allows the continuation of benefits during recessions
- It will cushion the impact of a catastrophic event
- It allows for the minimal changes in assessment rates
- It allows the funding of new workers' compensation programs or increased benefits without an immediate increase in assessment rates
- It allows the legislature to redirect the money to fund non-workers' compensation programs that are not a part of the WBF, as was done in FY 2004

There is one important argument against having a large fund balance:

- Because the purposes for which the money can be used are limited by the legislature, there is a limit on how much can be spent in a given period. Therefore, a large balance represents unused capital taken from employers and workers.

On balance, the original statutory language worked well until the end of the recession and the dissolution of the self-insured employer groups. It is reasonable, therefore, to return to the original requirement.

The committee unanimously approved the following recommendation:

1. Increase the minimum balance of the Workers' Benefit Fund to 12 months of projected expenditures and clarify that the balance is not entirely in cash.
2. Require the department to report to MLAC if projected expenditures could cause the fund balance to dip below the 12-month requirement. The department's report should include its action plan to address the fund balance situation.

These recommendations require statutory changes. Suggested language is included in Appendix B.

Appendix A - Fund balance scenarios

To illustrate the department's tools for managing the WBF fund balance, we can use recent experience to model what might have happened to the fund had it been at different levels before the recession. Two scenarios are shown.

Scenario 1

The scenario is:

- The assessment rate is 3.0 cents per hour.
- We enter the recession with a fund balance equal to nine months of expenditures.
- We draw down the fund balance to six months and then begin cutting expenditures.

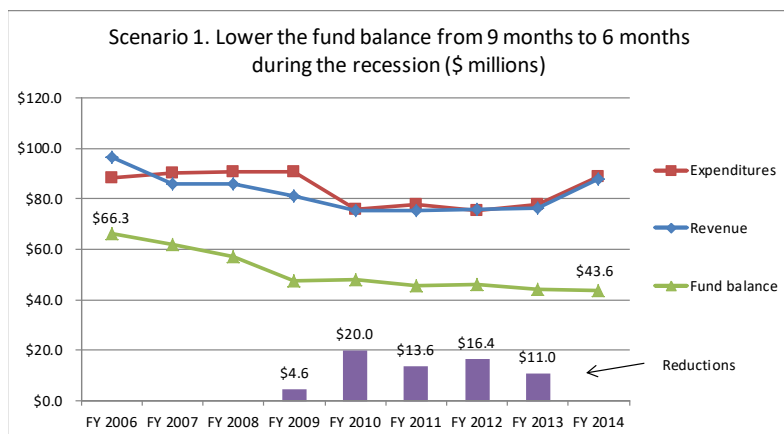
Under this scenario, the WBF would have had a fund balance of \$66.3 million as of June 2006. With the lower fund balance, the assessment rate probably would not have been lowered to 2.8 cents per hour in January 2007, so we assume it is 3.0 cents per hour.

Moving forward, the fund balance would have declined during FY 2008 and FY 2009, and DCBS would have had to begin taking measures. The figure below assumes the department began making expenditure cuts to ensure that the fund balance remained about six months of expenditures. The needed cuts would have been \$4.6 million in FY 2009, \$20.0 million in FY 2010, and smaller amounts in later years. These cuts would have totaled \$65.6 million over a five-year period.

The table below illustrates the expenditures during this time. Over the five-year period, the program expenditures were \$247 million and the expenditures for the four state agencies and OIOHS were \$35.6 million. The needed cuts would have been 14 percent of these expenditures.

The table illustrates the decisions that would have been needed. The needed cuts are equivalent to 25 percent of the Retroactive Program benefits paid or half of the state agency expenditures plus the entire Preferred Worker Program and 10 percent of the Employer-at-Injury Program.

An alternative would have been to raise the assessment rate. The assessment rate could have been raised to 3.5 cents per hour in January 2009 to maintain the fund balance at six months without cuts.



FY 2009-2013	
Additional revenue or reduced expenditures	\$65.6
Percentage of expenditures	14%
Expenditures	
Retroactive Program	\$260.7
EAIIP	95.4
PWP	24.4
PWP claims	12.6
Reopened Claims Program	24.7
Workers with Disabilities Program	3.8
Supplemental Disability	4.6
Program expenditures	\$427.3
State agency expenditures	\$35.6
Assessment rate modeled	0.030
Assessment rate needed to offset the deficit	0.035

Scenario 2

The scenario is:

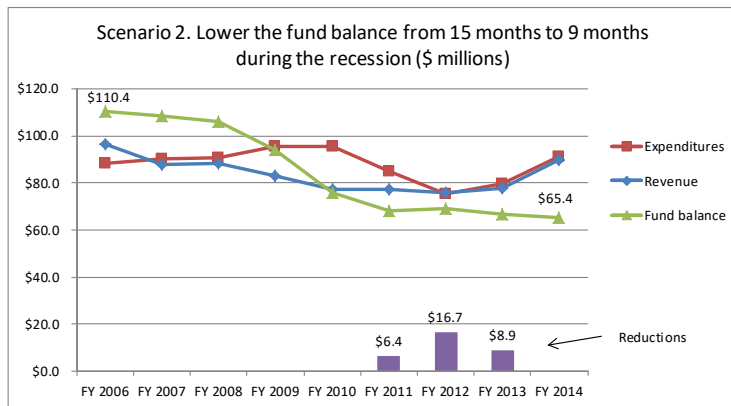
- We enter the recession with a fund balance equal to 15 months of expenditures.
- The assessment rate is 3.0 cents per hour.
- We draw down the fund balance to nine months and then begin cutting expenditures. We assume that this satisfies the statutory requirement if there is a long-term plan to raise the balance back to 12 months.
- We see the decline early enough that we can begin making expenditure cuts in FY 2010, a year before they are needed.

Under this scenario, the WBF would have had a fund balance of \$110.4 million as of June 2006. The figure below assumes the department began making expenditure cuts to ensure that the fund balance remained about nine months of expenditures. The needed cuts would have totaled \$32.0 million.

The table below illustrates the expenditures during this time. We assume that an action would take one year to be fully implemented, so we show expenditures over a four-year period, FY 2010 – FY 2013.

Over the four years, program expenditures were \$338.9 million, and agency expenditures were \$28.6 million. Without an assessment change, these expenditures would have needed to be cut by 9 percent to cover the \$32 million required to maintain the fund balance. While various choices could have been made, the scale of the cuts would have been equal to the elimination of the Preferred Worker Program and the staff positions involved in its administration.

The alternative would have been to raise the assessment rate. The assessment rate could have been raised to 3.3 cents per hour in January 2009 to maintain the fund balance at nine months without cuts.⁶ Or, a mix of rate increases and program cuts could have been implemented.



FY 2010-2013	
Additional revenue or reduced expenditures	\$32.0
Percentage of expenditures	9%
Expenditures	
Retroactive Program	\$207.0
EAIIP	\$76.2
PWP	\$18.3
PWP claims	\$10.3
Reopened Claims Program	\$20.1
Workers with Disabilities Program	\$3.4
Supplemental Benefits	\$3.6
Program expenditures	\$338.9
State agency expenditures	\$28.6
Assessment rate modeled	0.030
Assessment rate needed to offset the deficit	0.033

⁶ Given the timing of the decisions, perhaps an increase to 3.4 cents per hour in January 2010 would have been more likely.

Appendix B – Suggested statutory language

656.506 Assessments for programs

(5) It is the intent of the Legislative Assembly that the department set rates for the collection of assessments pursuant to subsections (2) and (3) of this section in a manner so that at the end of the period for which the rates shall be effective, the ~~cash~~ **fund** balance shall be an amount of not less than ~~six~~ **12** months of projected expenditures from the Workers' Benefit Fund in regard to its functions and duties under subsection (7) of this section and ORS 656.445, 656.622, 656.625, 656.628 and 656.630, in a manner that minimizes the volatility of the rates assessed. **In the event the department projects the fund balance will be less than twelve months, the department shall report its plan to meet the balance requirement to the committee referred to in ORS 656.790.** The department may set the assessment rate at a higher level if the department determines that a higher rate is necessary to avoid unintentional program or benefit reductions in the time period immediately following the period for which the rate is being set.

656.790 Workers' Compensation Management-Labor Advisory Committee; membership; duties; expenses.

(2) The director may recommend areas of the law which the director desires to have studied or the committee may study such aspects of the law as the committee shall determine require their consideration. The committee shall biennially review the standards for evaluation of permanent disability adopted under ORS 656.726 and shall recommend to the director factors to be included or such other modification of application of the standards as the committee considers appropriate. The committee shall biennially review and make recommendations about permanent partial disability benefits. The committee shall advise the director regarding any proposed changes in the operation of programs funded by the Workers' Benefit Fund **and review plans to address the fund balance under 656.506(5).** The committee shall report its findings to the director for such action as the director deems appropriate.