



Rate Framework Reform

Paper 1:

Executive Summary – An Overview of the Proposed Preliminary Rate Framework

MESSAGE FROM THE CHAIR AND PRESIDENT & CEO

In recent years, stakeholders, experts and the WSIB have identified a number of fundamental challenges to the WSIB's current classification and premium rate setting approach.

Following the recent engagement with stakeholders, Mr. Douglas Stanley released his final *Pricing Fairness* report, in which he recommends that the WSIB develop an Integrated Rate Framework that would change the way employers are classified and the way premium rates are set.

After a careful review of Stanley's recommendations, consideration of stakeholder perspectives and challenges, the WSIB's own analysis and advice from a team of actuarial experts from the firm Morneau Shepell, the WSIB committed to bring forward a proposed preliminary Rate Framework for discussion with stakeholders.

The WSIB's objectives are to consider reforms that ensure that everyone pays their fair share for workplace coverage, to ensure that there is a reasonable balance between premium rate stability and responsiveness, and to make it easier for stakeholders to understand and engage in the process.

The proposed preliminary Rate Framework described in these technical papers builds upon Stanley's recommendations and proposes a plausible working model - a way forward for the WSIB to distribute the costs of the system in a fair and transparent manner.

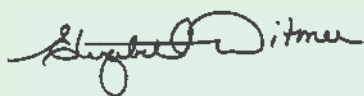
Its key features are:

- A simplified, transparent and modernized classification system, aligned to an accepted national standard;
- A fair process that prospectively sets premium rates, reflecting individual employers' claims experience relative to their industry; and
- Considerations for a reasonable transition path to ensure employers can gradually adjust to the new premium rate setting process.

Although the WSIB is proposing a plausible working model, there are a number of options and key questions for further consideration. The WSIB understands that it is only with stakeholders' varied and unique perspectives that it will be able to make informed decisions on the issues currently faced by the system.

The WSIB is thankful for the support and thoughtful engagement of stakeholders in the Rate Framework Reform initiative and looks forward to further opportunities to hear the diverse perspectives as we consider potential reforms to the current approaches for employer classification and premium rate setting.

Yours truly,



Elizabeth Witmer
Chair



I. David Marshall
President & CEO

March 31, 2015



THE RATE FRAMEWORK REFORM ANALYSIS

The Rate Framework Reform Package consists of five papers. Each paper can be read independently, however in order to gain a better understanding of the proposed preliminary Rate Framework, each paper should be read sequentially.

The Rate Framework Reform Package includes:

Paper 1: Executive Summary - An Overview of the Proposed Preliminary Rate Framework

A paper that provides the reader with a sound overview to aid in the general understanding of the proposed preliminary Rate Framework.

Paper 2: Current State Analysis

An overview of the Rate Framework Reform Consultation that describes, at a high-level, the *Pricing Fairness* report's conceptual Integrated Rate Framework, and sets the stage for this engagement with stakeholders. This paper also highlights some of the fundamental issues with the Workplace Safety and Insurance Board (WSIB)'s current classification and premium rate setting process, which includes experience rating.

Paper 3: The Proposed Preliminary Rate Framework

A three step approach outlining the WSIB's recommendations on a proposed preliminary Rate Framework. This paper describes a workable model the WSIB is proposing to replace the current employer classification, premium rate setting and experience rating systems. Each section within this paper includes an overview and analysis of the WSIB's current system, a set of recommendations, and Douglas Stanley's recommendation as applicable.

Paper 4: The Unfunded Liability

An outline of the proposed preliminary Rate Framework's recommendation on how the unfunded liability could be reasonably apportioned to specific classes.

Paper 5: A Path Forward

An overview of the key considerations for a gradual transition towards a new Rate Framework, and how stakeholders can provide comments on the proposed preliminary Rate Framework.

Throughout the consultation period, the WSIB will be accepting written submissions on the proposed preliminary Rate Framework. Please visit www.wsibratereform.com for more information and opportunities to participate in the discussion, and email your written submissions to consultation_secretariat@wsib.on.ca.

PAPER 1 | EXECUTIVE SUMMARY – AN OVERVIEW OF THE PROPOSED PRELIMINARY RATE FRAMEWORK

The WSIB is undertaking a comprehensive review of its current employer classification structure, as well as the premium rate setting process, which includes the current experience rating programs. Further to previous discussions with stakeholders, led by Professor Harry Arthurs and Mr. Douglas Stanley, the WSIB's on-going Rate Framework Reform Consultation will provide a range of opportunities for stakeholders to have their views heard, ensuring that any significant reform would be implemented gradually and in a manner that fosters stability.

Considering the input from these previous undertakings and the WSIB's own analysis across other comparable jurisdictions in the context of the workers' compensation system in Ontario, the WSIB is bringing forward a proposed preliminary Rate Framework for discussion with stakeholders.

This proposed preliminary Rate Framework represents a plausible working model that aims to address fundamental issues raised by stakeholders, partners and the WSIB itself, with the current employer classification structure and premium rate setting processes.

The WSIB has been working with a team of external actuarial advisors from the firm Morneau Shepell to develop a proposed preliminary Rate Framework. This model includes a number of variations, options and questions to be discussed and considered in the accompanying Rate Framework Reform Papers. In addition, other perspectives and ideas that stakeholders are interested in putting forward as improvements will be considered.

As you read the Executive Summary and the subsequent papers and begin to consider the merits, potential variations and implications, it is important to reflect on the Key Goals of the proposed preliminary Rate Framework identified below for the workers' compensation system as a whole.

Preliminary Rate Framework Key Goals:

1. **Clear and Consistent:** A new streamlined and simpler classification structure that is clear and consistent in its application as a foundation.
2. **Fairly Allocated Premiums:** An approach that ensures a fair premium for workplace coverage, based on each employer's risk and claims experience to ensure occupational health and safety is top of mind for employers as it relates to their premiums.
3. **Balanced Rate Responsiveness:** A reasonable consideration for premium rate stability, while also ensuring responsiveness to risk and claims experience attained through occupational health and safety efforts to reduce workplace injuries and return workers to productive work.
4. **Transparent and Understandable:** A Rate Framework that stakeholders can easily understand, and promotes active and informed participation.

5. **Collective Liability:** A risk sharing arrangement exists among employers who collectively pay premiums to maintain the insurance fund.
6. **Ease of Administration:** Efficient and effective for the employer community and for the WSIB to administer and maintain.

Revenue Neutrality as a Foundation

The adoption of a new classification structure and prospective Risk Adjusted Premium Rate process would not affect the total amount of premium dollars collected by the WSIB, thereby remaining revenue neutral. However, a new system would, in a reasonable and gradual manner, shift the distribution of premiums among individual employers based on their claims experience, while ensuring that employers are paying their fair share of workplace coverage.

Proactive Occupational Health and Safety Interventions – Return to Work and Prevention

The proposed preliminary Rate Framework would act as an early warning for employers by providing target premium rates allowing employers to; better identify the future projected path of their premium costs; and take proactive health and safety actions (e.g. prevention; and return to work (RTW) to address the risks).

Employers could see premium rate implications as a result of:

- A transition to a more responsive Rate Framework;
- A significant gap between their historical rates in the current system and their new Target Premium Rate;
- A sustained performance trend leading to a significant increase in their risk profile; and
- A risk profile that is disproportionate to their respective industry performance.

New and enhanced risk reduction support services (focusing on RTW and Prevention) are delivered by the WSIB's Workplace Health and Safety Services function and other Occupational Health and Safety partners (including the Ministry of Labour, the Chief Prevention Officer and Health and Safety Associations).

These services would be most helpful in assisting employers who have a particular interest in reducing their claims experience performance trends that have led to high premium rates.

The design of the proposed preliminary Rate Framework could accommodate other health and safety initiatives or programs (Ministry of Labour/Chief Prevention Office).

Helping You Understand What is Being Proposed

As employers familiarize themselves with the proposed preliminary Rate Framework, it is important to understand that it may not be easy for them to compare what they may recognize as their premium rate, that is the premium rate associated with the rate group (RG) in the current system, with the proposed approach.

Currently, the RG premium rate represents the collective claims experience of all employers in the group and has little to do with the individual claims experience of any one employer. Even when the current experience rating programs are added (which excludes 60% of employers and could lead to surcharges and rebates nearly 2 years later), this system leads to a lack of fairness in setting premium rates, particularly for those employers with good health and safety performance.

The proposed preliminary Rate Framework uses a methodology that is seeking to set employer centric premium rates that considers an employer's claims experience in setting a premium rate for the upcoming year, and gradually moving employers towards a rate that is truly reflective of their own experience.

Simply explained, the proposed preliminary Rate Framework would see individual employers more fairly assessed based on their own claims experience, moving away from the current system where, regardless of their own experience, all employers pay the same premium rate within their rate group.

As part of this phase of Rate Framework Reform consultation, the WSIB has prepared a series of technical papers. These papers and accompanying questions can be technical in nature, and provide varying level of depth of analysis and detail. For those stakeholders who would like a higher level overview of what is being presented in these technical papers, the WSIB has developed a number of products that could be helpful, such as this Executive Summary, and other products that summarize the current state, and the proposed preliminary Rate Framework, which can be found on the website below.

The WSIB appreciates that you may have questions about what is being proposed - it works differently than the current system. Our aim is to ensure that you understand, at the level that you believe is necessary, and have every opportunity to ask the important questions that matter to you. At any point in this conversation, the WSIB is prepared to provide you with additional support to help individual stakeholders or representative groups or associations better understand what is being proposed. Simply reach out to us at the consultation_secretariat@wsib.on.ca, and we will be happy to provide any required support.

In addition, as part of stakeholder outreach, the WSIB has scheduled technical and working group sessions in April and May to provide stakeholders with a better understanding of the proposed preliminary Rate Framework. Please visit the www.wsibraterateframeworkreform.com for more information and a list of meetings and opportunities where you can join in the discussion.

OVERVIEW | PAPER 3: THE PROPOSED PRELIMINARY RATE FRAMEWORK

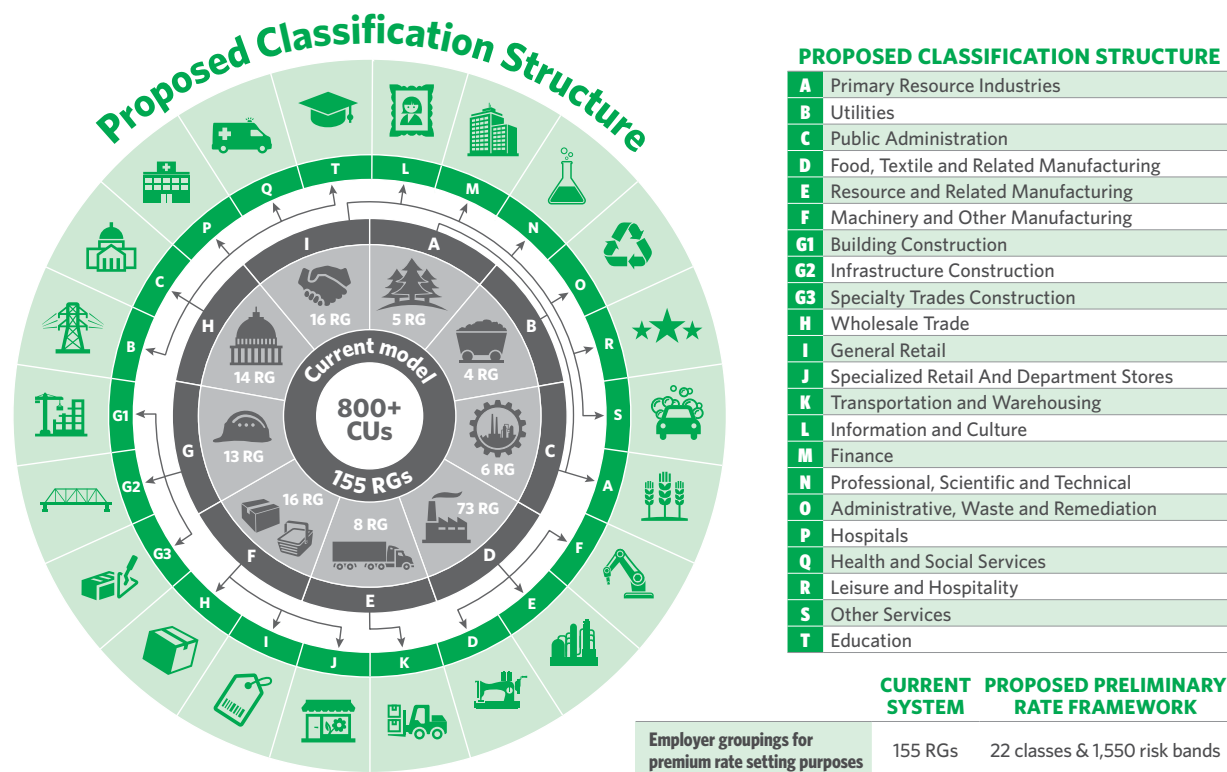
Step 1 - Employer Classification

North American Industry Classification System

The proposed preliminary Rate Framework seeks to replace the WSIB’s current employer classification system with a 22 class structure adapted from the 2012 North American Industry Classification System (NAICS), the most recent version of the NAICS, which is updated every five years. The proposed classification structure is based on significantly fewer employer groupings for the purpose of setting premium rates, compared to the current 155 RG and 840 CU structure. It is intended to create a structure that is simple and understandable.

The WSIB assessed the actuarial predictability of each two-digit NAICS sector and determined that \$2 billion in insurable earnings per year for each sector provided a level of predictability that can be relied upon to predict future outcomes and therefore fairly and accurately set premium rates.

Figure 1: SIC to NAICS-based Classification Structure



This diagram is intended to show the broad mapping of the current RGs to the proposed preliminary Rate Framework classes. It is not intended to show where each individual employer or business activity would be assigned in the proposed preliminary Rate Framework.

The proposed new structure recognizes certain industry groupings that are similar to the current structure, such as Manufacturing, Construction, and Transportation and Storage. As a result, many employers would remain in a similar employer grouping at the class level to the one they are in the current system. However, it would also group industries into new, separate categories, like Information and Culture and Professional, Scientific and Technical. Further details on employer classification are provided in Paper 3: The Proposed Preliminary Rate Framework.

Multiple Business Activities

The proposed preliminary Rate Framework's classification structure would group employers with multiple business activities in a single class according to their predominant class. The WSIB is proposing to define the "predominant class" as the class that represents the largest percentage of the employer's annual insurable earnings.

Under the proposed classification structure, the WSIB would continue to classify employers according to an employer's business activities (when registering, an employer must provide the WSIB with a description of their business activities). As in today's structure, the employer would be required to report any changes to their business activities or to their insurable earnings.

The classification of employers according to their predominant class would require changes to Ontario Regulation 175/98 of the *Workplace Safety and Insurance Act, 1997*, as well as to related policies.

Step 2 & 3 - Risk Adjusted Premium Rate Setting

Paper 3: The Proposed Preliminary Rate Framework will detail for stakeholders how an employer's premium rate would be calculated under the proposed preliminary Rate Framework, based on the following steps:

- **Step 2: Class Level Premium Rate Setting** would create an average premium rate for each individual class ("Class Target Premium Rate") based on the valuation of collective liabilities of new claim costs for employers within their respective classes, their allocation of administrative costs and the apportionment of the past claim costs for a particular class; and
- **Step 3: Employer Level Premium Rate Adjustment** would adjust the Class Target Premium Rate for individual employers based on their risk, represented by their own claims experience and insurable earnings relative to their Class Target Premium Rate, to arrive at their individual risk band position and corresponding Employer Actual and Target Premium Rates.

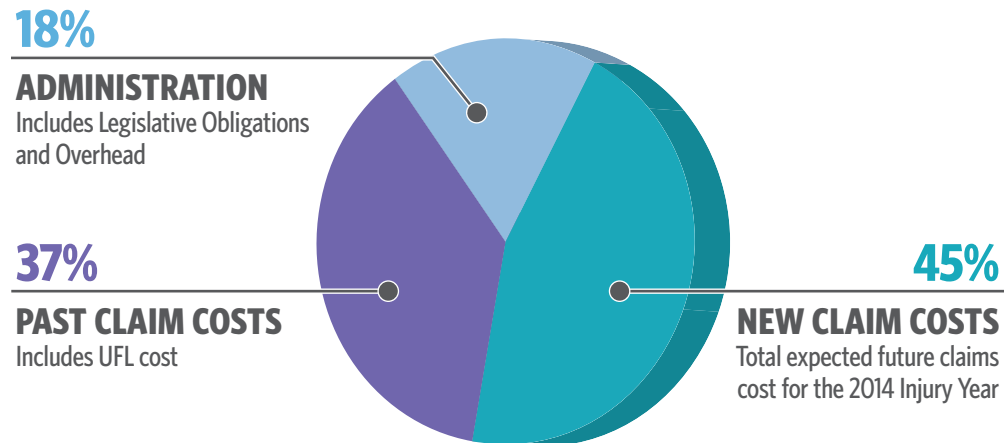
In order to ensure that the proposed preliminary Rate Framework could improve workplace health and safety and create outcomes that are reasonable and fair to all employers, the WSIB developed a working model that utilized enough data to determine the premium rate impacts to employers.

In the coming sections, the WSIB presents information on a working model that is based on 13 years of claims and insurable earnings experience. Using the proposed preliminary Rate Framework methodology, the WSIB generated 2014 employer premium rates so that employers would be able to relate to the premium rates that were created at the class level.

Step 2 – Class Level Premium Rate Setting

In a manner similar to the current premium rate setting process, this step of the proposed preliminary Rate Framework derives a premium rate to cover expected costs relating to the upcoming premium year. The 2014 premium rates are made up of three parts.

Figure 2: 2014 Premium Rate Components - Schedule 1



The proposed preliminary Rate Framework would use the current methodology for estimating the new claim costs amount required at the Schedule 1 level and incorporate a graduated per claim limit. However, some changes would be needed as a result of the proposed classification structure, where a 22 class structure would replace the existing classification structure.

As a result, some classes may experience an increase or decrease in the new claim costs component of their Class Target Premium Rate. This may occur because the risk profile (determined by looking at an employer’s claim costs and their insurable earnings) of the nine classes may be different than the risk profile of the 22 classes.

In addition, the proposed preliminary Rate Framework intends that each class stand on its own, with no pooling of costs from other classes or from Schedule 1.

To support this new premium rate setting method, the WSIB would need to develop a:

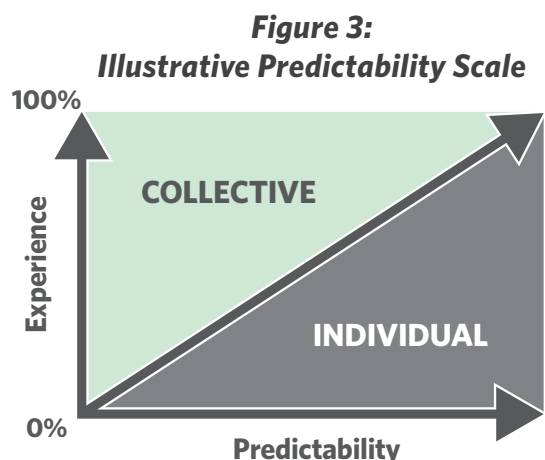
- Premium Rate Setting Policy to:
 - Identify a set of governing principles on the setting of premium rates;
 - Guide the processes undertaken by the WSIB;
 - Provide parameters for the processes that would be used; and a
- Transition plan that would guide the process from the current to a future state.

Step 3 – Employer Level Premium Rate Adjustments

The proposed preliminary Rate Framework would eliminate the current experience rating programs: New Experimental Experience Rating Plan (NEER), Construction Industry Plan (CAD 7) and Merit Adjustment Program (MAP). In its place, Employer Level Premium Rate Adjustments would prospectively assess Schedule 1 employers. In order to determine an employer’s premium rate, the WSIB would look at two main factors – an employer’s *risk profile* and *actuarial predictability*, which are further defined below.

Risk Profile and Actuarial Predictability

An employer’s risk profile is determined by looking at an employer’s claim costs, insurable earnings, and actuarial predictability (based on insurable earnings or total claims). In other words, the WSIB would look at an employer’s risk profile and actuarial predictability to determine the extent to which their premium rate should be affected by their own individual claims experience versus the collective experience of their respective class.



Based on the application of actuarial predictability, the chart below represents the various levels that describe the mix of individual and collective experience that would support the Employer Level Premium Rate Adjustments.

Figure 4: Proposed Actuarial Predictability Scale

Predictability Scale (%)	<= 2.5	2.5 - 5.0	5.0 - 10	10 - 20	20 - 30	30 - 40	40 - 50	50 - 60	60 - 70	70 - 80	80 - 90	90 +
Individual Experience for Premium Rate Setting (%)	2.5	5.0	10.0	20.0	30.0	40.0	50.0	60.0	70.0	80.0	90.0	100.0
Collective Experience for Premium Rate Setting (%)	97.5	95.0	90.0	80.0	70.0	60.0	50.0	40.0	30.0	20.0	10.0	0.0

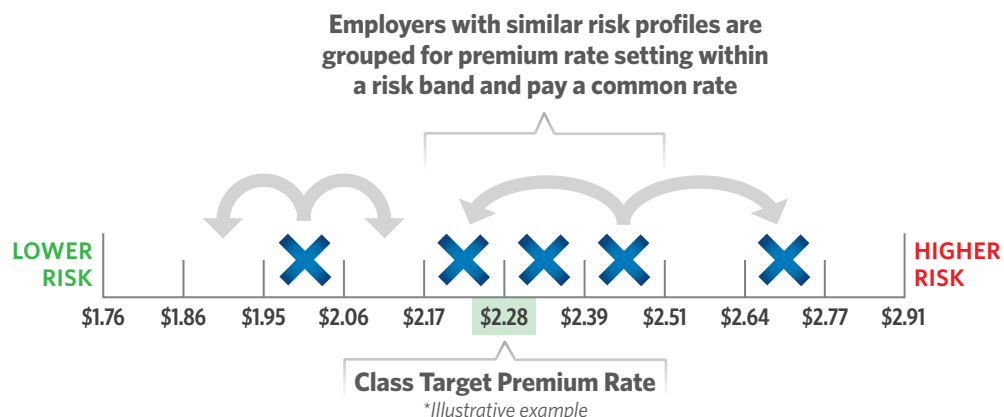
For example, if an employer’s actuarial predictability is calculated as anywhere between 40% and 50%, then half (50%) of their premium rate will be based on their individual experience, and half (50%) will be based on the collective experience of the class. This ensures that collective liability to protect employers from sudden cost changes is balanced by accountability for an individual employer’s workers’ compensation claim costs.

Risk Banding

The proposed preliminary Rate Framework recommends replacing the current experience rating programs with Employer Level Premium Rate Adjustments for all Schedule 1 employers. Each employer would see adjustments from their Class Target Premium Rate based on the risk that they specifically bring to the system (after taking into consideration each employer’s historical claims experience and actuarial predictability).

Risk bands are hierarchical series of divisions within each class. Each division represents a different level of risk where employers would be placed relative to the Class Target Premium Rate. In each class, risk bands are subject to limitations, such as the premium rate of the minimum risk band (\$0.20), and the maximum risk band, which will not exceed about three times the Class Target Premium Rate. Each risk band represents approximately 5% increments in premium rate.

Figure 5: Illustrative Risk Banding Scale



New Employers

The proposed preliminary Rate Framework seeks to ensure that all new employers are taking part in the Risk Adjusted Premium Rate Setting process as soon as possible when compared to current experience rating programs.

A minimum of 12 months of claims experience would be necessary to obtain sufficient information to determine the level of accident cost and insurable earnings information required to calculate an employer’s risk profile, so that Employer Level Premium Rate Adjustments relative to the Class Target Premium Rate can be calculated. To calculate an employer’s risk profile, the WSIB would obtain the employer’s claim costs and insurable earnings.

If the WSIB does not have 12 months of claims experience for an employer at the time of premium rate setting, an employer would be charged the Class Actual Premium Rate. This contrasts with the current MAP program’s requirements that the employer have three years of claims experience before receiving premium rate decreases.

Surcharging

As part of the proposed preliminary Rate Framework, the WSIB would cap Employer Level Premium Rate Adjustments up to about three times the Class Target Premium Rate. This measure would limit an employer’s risk band movement each year, and protect an employer from unexpected catastrophic claim costs in a specific year.

However, there may be employers who have high and disproportionate claim costs relative to their class, year over year. Additionally, the gap between what they are actually paying in premium rates and what they should be charged is of such a significant difference. As such, it may make sense to assign these employers some additional accountability for their consistently poor behavior.

The proposed preliminary Rate Framework seeks to consider the application of a surcharge mechanism that would be applied against the Risk Adjusted Premium Rate Setting process. Without such a mechanism, the WSIB would consider having employers within each class collectively subsidizing the sustained poor claims experience of these employers. The WSIB would like to receive stakeholder input on the merits of surcharging and the proposed approach that should be considered.

CONCLUSION

The WSIB is recommending the proposed preliminary Rate Framework replace its current classification structure, premium rate setting process, and experience rating programs. The new model aims to address some of the fundamental issues raised by stakeholders, partners and the WSIB itself, with the current framework and its associated business processes. The WSIB has done extensive technical analysis and modeling of design features to ensure the proposed preliminary Rate Framework is aligned with the Rate Framework's Key Goals.

The WSIB's objectives are to consider reforms that ensure that everyone pays their fair share for workplace coverage, to ensure that there is a reasonable balance between premium rate stability and responsiveness, and to make it easier for stakeholders to understand and engage in the process.

NEXT STEPS

The WSIB is seeking input from stakeholders on the proposed preliminary Rate Framework. Input can be provided at consultation meetings, and/or in writing at the following email address consultation_secretariat@wsib.on.ca.

Please visit www.wsibratereform.com for more information and opportunities to participate in the discussion.

GLOSSARY

Actuarial Predictability is a process where the WSIB determines the degree to which past claims costs can be relied upon to predict future outcomes and therefore fairly and accurately set premium rates. Also referred to as actuarial credibility.

Class Actual Premium Rate is the premium rate that would be set by the WSIB, taking into consideration risk band limitations, previous year(s) premium rates, as well as the collective experience of all employers in that class.

Class Target Premium Rate is a premium rate based on the valuation of collective liabilities of new claim costs for the employers within a respective class, their allocation of administrative costs, and apportionment of the past claims costs for a particular class.

Employer Actual Premium Rate is an adjusted premium rate that represents how much each employer would pay taking into consideration risk band limitations, previous year(s) premium rates, minimum premium rate, as well as the collective experience of all employers in that class.

Employer Level Premium Rate Adjustment is a process where the Class Target Premium Rate is adjusted for an individual employer based on their risk relative to the Class Target Premium Rate, to arrive at their individual risk band position and corresponding Employer Target and Actual Premium Rates.

Employer Target Premium Rate is an adjusted premium rate that represents how much an employer needs to pay in order to fund their fair share of costs, as well as the collective costs of their class.

Net Premium Rate represents the premium rate, for a class, rate group or individual employer, comprised of the published premium rate combined with any premium adjustments resulting from the existing experience rating programs, as applicable.

Predominant Class is the class that represents the largest percentage of the employer's annual insurable earnings.

Risk Adjusted Premium Rate Setting is a two-step process that includes setting the Class Target Premium Rate and Employer Level Premium Rate Adjustments.

Risk Bands are hierarchical series of divisions within each class. Each division represents a different level of risk where employers would be placed relative to the Class Target Premium Rate. In each class, risk bands are subject to limitations, such as the premium rate of the minimum risk band (\$0.20), and the maximum risk band will not exceed about three times the Class Target Premium Rate. Each risk band represents approximately 5% increments in premium rate.

Risk Disparity is when claims experience or premium rates vary significantly from the average experience of the class.

Risk Profile is a step in determining the allocation of the costs to the system between the classes and/or individual employers, and is based on an employer's (or a class') claims costs relative to their insurable earnings.

