

G99G00
Injured Workers' Insurance Fund

Operating Budget Data

(\$ in Thousands)

	<u>CY 2001</u> <u>Actual</u>	<u>CY 2002</u> <u>Actual</u>	<u>CY 2003</u> <u>Budget</u>	<u>Change</u>	<u>% Change</u> <u>Prior Year</u>
Nonbudgeted Fund	\$33,147	\$33,679	\$43,787	\$10,108	30.0%
Total Funds	\$33,147	\$33,679	\$43,787	\$10,108	30.0%

- A total of \$75.0 million will be transferred in fiscal 2003 from the State's unfunded liability account to the general fund under the 2003 session Budget Reconciliation and Financing Act.
- The \$20.0 million budgeted annually since fiscal 1999 for the State's unfunded liability account is not included in the fiscal 2004 allowance.

Personnel Data

	<u>CY 2002</u> <u>Actual</u>	<u>CY 2003</u> <u>Budget</u>	<u>Change</u>
Regular Positions	389.00	406.00	17.00
Total Personnel	389.00	406.00	17.00

Note: Numbers may not sum to total due to rounding.

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Analysis in Brief

Major Trends

IWIF Improves Productivity but Investment Earnings Are Down: The Injured Workers' Insurance Fund (IWIF) has shown significant increases in business volumes between calendar 1999 and 2003. It has improved performance in terms of claims handled, premiums written, and number of policies per staff member, while per-staff operating expenses have increased marginally. In contrast, large losses in investment earnings between calendar 2001 and 2002 have contributed to an overall loss by the company of \$25.9 million in calendar 2002.

Issues

\$75.0 Million Is Transferred from Long-term Liability Account in Fiscal 2003: The Governor has proposed transferring \$75.0 million from the State's long-term liability account to the general fund in fiscal 2003, through the Budget Reconciliation and Financing Act. **IWIF and the Department of Budget and Management are asked to discuss the implications of this transfer.**

Agency Assessments Show Large Decrease in Fiscal 2004: The Board of Public Works decided in November 2001 that the State should be required to maintain accounts separate from other IWIF clients. This decision resulted in a need for the State to more fully cover its operating account, which eventually resulted in a larger operating account balance than will be necessary at the end of fiscal 2003. This balance, coupled with the decision by the administration to not require a \$20.0 million appropriation into the long-term liability account results in a much lower agency assessment in fiscal 2004 than is the case in fiscal 2003.

Recommended Actions

1. Nonbudgeted.

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Operating Budget Analysis

Program Description

The Injured Worker's Insurance Fund (IWIF) is a nonbudgeted, independent entity. IWIF is governed by a Board of nine directors (appointed by the Governor to five-year terms), which approves the operating and capital budgets. By law, IWIF's calendar 2003 budget is submitted to the General Assembly for informational purposes only. The primary purpose of IWIF is to provide workers' compensation insurance to Maryland-based businesses. IWIF provides workers' compensation insurance to employers who do not wish, or are not allowed, to self-insure. The goal of IWIF is to provide insurance coverage and to pay benefits promptly to injured workers and dependents. Financing for IWIF is derived solely from its premium and investment income.

Performance Analysis

As an independently chartered company, IWIF does not participate in the Managing for Results program. However, it tracks its performance through productivity and financial indicators and has provided those data to the Department of Legislative Services.

Productivity Indicators

IWIF has shown significant increases in business volumes between calendar 1999 and 2003. The size of the staff employed by IWIF has increased 6% since 1999, from 384 to 406 employees. In the same time period, the number of "FROIs" or first report of injuries and the number of policies per employee have increased 72% and 31%, respectively. Further, while operating expenditures per employee have increased by 20% since calendar 1999, premiums paid per employee have increased 190%, while claims paid per employee have increased 95%. All indicators are demonstrated in **Exhibit 1**. Please note that these data do not include activity from the State; if they did, activity per employee would increase substantially.

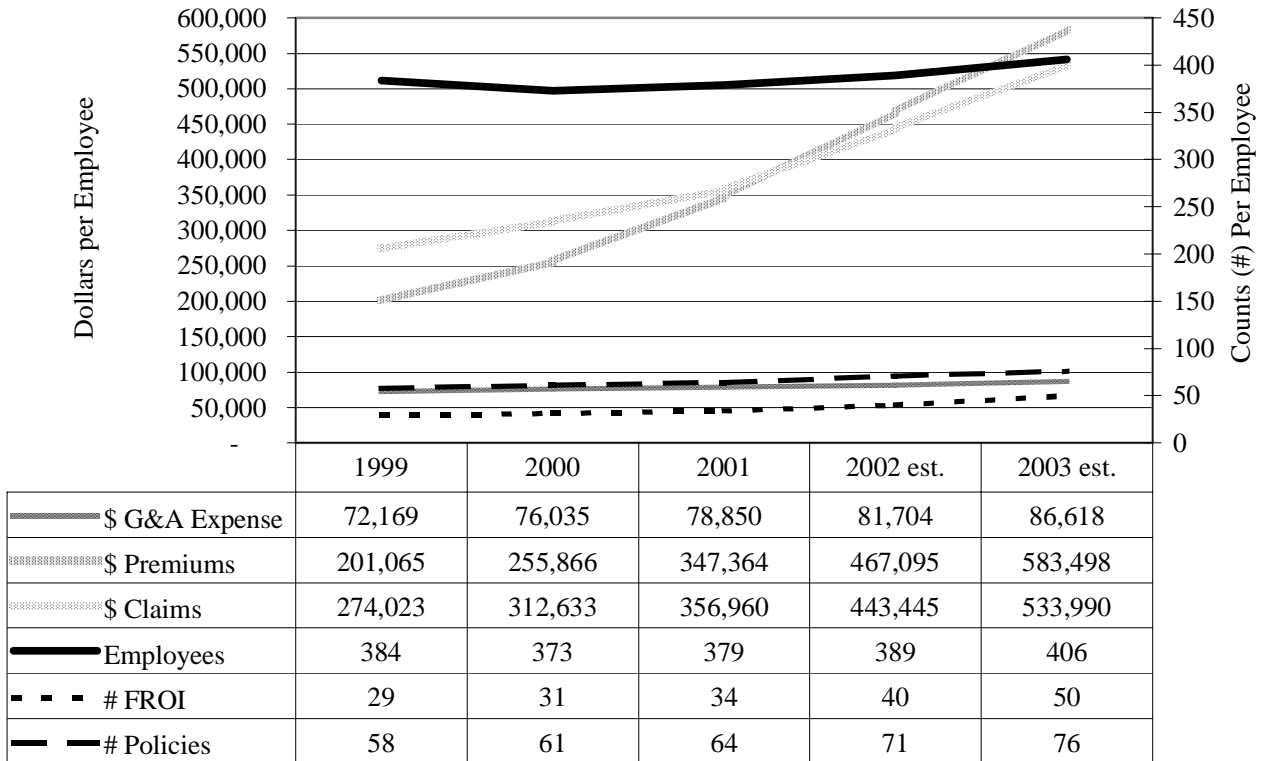
Financial Indicators

Although business volumes have increased steadily and operating performance has improved since calendar 1999, the net income of IWIF is negative in calendar 2002, as indicated in **Exhibit 2**. Assets have risen to \$946.2 million, or a 5.4% increase in the most recent full year of business. Total income on those assets has increased 5.9%, which is somewhat restrained due to a significant drop in investment income. Another positive note in 2002 is that premiums earned exceeded claim expenses by \$8.9 million. In each of the two previous years, claims expenses surpassed premiums.

Exhibit 1

G99G00 - Injured Workers' Insurance Fund

Productivity Per Employee



G&A = General and Administrative
 FROI = First Report of Injuries

Source: Injured Workers' Insurance Fund

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Exhibit 2

Injured Workers' Insurance Fund Status
Calendar 2000 through 2002
(\$ in Thousands)

	<u>2000</u>	<u>2001</u>	<u>2002</u>	% Change 01 to 02
Balance Sheet Data				
<i>Assets:</i>				
Total investments (market value)	\$920,190	\$845,800	\$832,000	-1.6%
Cash and equivalents	29,436	16,092	74,400	362.3%
Subtotal Cash and Investments	949,626	861,892	906,400	5.2%
Other assets	\$34,205	\$35,819	\$39,800	11.1%
Total Assets	\$983,831	\$897,711	\$946,200	5.4%
<i>Liabilities:</i>				
Accrual unpaid claims and related expense	\$649,000	\$710,000	\$766,000	7.9%
Dividends payable	629	789	1,600	102.8%
Other liabilities	153,916	46,746	62,800	34.3%
Total Liabilities	\$803,545	\$757,535	\$830,400	9.6%
Total fund equity	\$180,286	\$140,176	\$115,800	-17.4%
Total Liabilities and Fund Equity	\$983,831	\$897,711	\$946,200	5.4%
Income Statement Data				
<i>Income:</i>				
Net premiums earned	\$95,438	\$131,651	\$181,700	38.0%
Other income	256	572	600	4.9%
Investment income and gains	67,906	50,146	10,800	-78.5%
Total Income	\$163,600	\$182,369	\$193,100	5.9%
Net claim expenses	\$116,612	\$135,288	\$172,800	27.7%
Net operating expenses	34,067	37,061	46,200	24.7%
Total Expenses	\$150,679	\$172,349	\$219,000	27.1%
Income	\$12,921	\$10,020	-\$25,900	
Change in Accounting Principle		-\$51,246		
Net Income/Loss After Change in Accounting Principle	\$12,921	-\$41,226	-\$25,900	-37.2%

¹ IWIF moved under the jurisdiction of the Maryland Insurance Administration at the beginning of calendar 2001 and was required to change its basis of accounting. The \$51.2 million loss at the end of calendar 2001 was the result of no longer being able to recognize the time value of money for medical claims payments.

Source: Injured Workers' Insurance Fund

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Calendar 2003 Budget

The IWIF budget for calendar 2003 is demonstrated in **Exhibit 3**, below. IWIF's budget increases \$10.1 million between expenditures for calendar 2002 and those budgeted for calendar 2003. Operating, or general and administrative, expenditures have increased \$3.4 million, or 10.6%, while capital expenditures have increased \$6.7 million, for an overall increase of 30.0%.

Exhibit 3

**Governor's Proposed Budget
Injured Workers' Insurance Fund
(\$ in Thousands)**

How Much It Grows:	Nonbudgeted <u>Fund</u>	<u>Total</u>
CY 2002 Actual	\$33,679	\$33,679
CY 2003 Budget	43,787	43,787
Amount Change	\$10,108	\$10,108
Percent Change	30.0%	30.0%

Where It Goes:

Personnel Expenses

New positions (salary & fringes)	\$550
Salary increase of 4%	800
Employee health insurance.....	350
Other fringe benefits (Social Security, etc.).....	144
Consulting and contractual services.....	319

Other Changes

Training, travel, and other staff costs	242
Advertising, promotion, and printing.....	187
Facility costs, postage, telecommunications, and supplies.....	432
Legal expenses	279
Other operating costs	81

Capital

Building upgrades and parking lot	5,450
New furniture	1,000
New vehicles	80
Other capital expenditures	194

Total **\$10,108**

Note: Numbers may not sum to total due to rounding.

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Capital Increases

The largest increases in calendar 2003 are attributable to capital expenditures, some of which the State would refer to as operating or PAYGO expenditures. The largest single expenditure is a planned \$5.5 million renovation of IWIF's building and the acquisition of a new parking lot at 8722 Loch Raven Boulevard in Towson. IWIF had planned these changes in prior years but postponed them until the current budget year. The IWIF building was erected 12 years ago and has not had any significant renovations since. IWIF also plans to spend approximately \$1.0 million on new furniture for the renovated building.

General and Administrative Expenditures

The largest share of general and administrative, or operating expenditure, increases is attributable to personnel. IWIF has budgeted funds for ten new "floating" positions to handle increased workload where needed. It also plans to replace seven people who departed in calendar 2002, so is showing a gain of seven positions in calendar 2003. IWIF does not fully fund positions, as does the State, nor does it count in its total workforce positions that are not filled. Another significant departure from the way the State does business is that IWIF has budgeted \$0.8 million for an average salary increase of 4% in calendar 2003. Other fringe benefit increases include funds for health, prescription, and dental plan cost increases and for increases in other fringes such as Social Security. Total increases in consulting and contractual services include increased expenditures for the implementation of a disaster recovery system and the outsourcing of policy audits.

Other calendar 2003 operating expenditure increases include advertising, promotion, and printing related to the acquisition and support of increased business volumes. This includes a substantial increase in fees paid to Weber Shandwick for a retainer for Maryland professional and college athletic team-related advertising. Rising legal expenditures are primarily attributable to the increased use of outside legal support.

Issues

1. \$75.0 Million Is Transferred from Long-term Liability Account in Fiscal 2003

The State of Maryland is self-insured for workers' compensation claims. The State contracts with IWIF for claims processing and maintains two accounts with the fund. The operating account is utilized to pay annual claims against the State and cover administrative costs. The long-term liability account provides a reserve against the State's future workers' compensation liabilities.

Governor Ehrlich has proposed transferring \$75 million from the long-term liability account to the general fund in fiscal 2003 through the 2003 Budget Reconciliation and Financing Act (BRFA). The long-term liability fund is commonly called the "Unfunded Liability" account, which refers to the difference between what the actuaries have determined is adequate to cover future liability and what the State has deposited in the account. Coupled with the \$75.0 million transfer from the balance of the unfunded liability account is the administration's decision not to appropriate \$20.0 million to the account, as has been the practice since fiscal 1999. These decisions will leave the long-term liability account with a balance of \$4.8 million at the end of 2003, and \$5.5 million at the end of 2004. The State's resulting unfunded long-term liability is \$173.5 million at the end of 2003, and \$206.4 million at the end of fiscal 2004. Both balances are demonstrated in **Exhibit 4. IWIF and the Department of Budget and Management are asked to comment on the implications for the State of the increase in the unfunded liability balances.**

Exhibit 4

Maryland's IWIF Long-term Liability Account Fiscal 2002 through 2004

	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>
Estimated Reserves Needed (June 30)	\$194,802,000	\$206,000,000	\$218,000,000
Estimated Long-term Liability Account Balance			
Beginning Balance	\$107,518,959	\$97,542,503	\$4,849,934
Transfer to IWIF operating account to cover deficit (12/31/01)	-34,000,000		
State's contribution (June 30)	20,000,000	20,000,000	0
Transfer – 2002 BRFA (June 30)		-39,200,000	
Transfer – 2003 BRFA (June 30)		-75,000,000	
Interest	4,023,544	1,507,431	650,747
Total Balances at IWIF (June 30)	\$97,542,503	\$4,849,934	\$5,500,681
Balance of operating account ¹	9,077,550	27,687,402	6,115,743
Unfunded Long-term Liability (June 30)	\$88,380,655	\$173,462,664	\$206,383,577

¹ The balance of the operating account offsets the long-term liability of the State.

Source: Injured Workers' Insurance Fund

2. Agency Assessments Show Large Decrease in Fiscal 2004

Agency assessments have fluctuated greatly over the last three years, increasing 27.6% in fiscal 2003, and decreasing 68.5% in fiscal 2004, as demonstrated in **Exhibit 5**.

Exhibit 5

IWIF Assessments of State Agencies Fiscal 2002 through 2004 (\$ in Thousands)

	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>
Claims Paid ¹	\$33,741.8	\$42,756.4	\$41,087.3
Administration Costs ²	7,495.5	9,094.2	8,968.9
Adjustment for Operating Cash Shortfall/(Surplus)	8,054.6	16,542.9	(22,200.0)
Subtotal	\$49,291.9	\$68,393.4	\$27,856.1
Contribution to Reduce Future Liability ³	\$20,000.0	\$20,000.0	\$0.0
Total Agency Assessment/Appropriation	\$69,291.9	\$88,393.4	\$27,856.1
Change in Total Assessments/Appropriations		\$19,101.5	(\$60,537.3)
Percent Change in Total Assessments/Appropriations		27.6%	-68.5%

¹ Estimated to equal the claims paid in the most recent fiscal year for which actual data is available (two years prior).

² Estimated to equal the administration costs from two years prior.

³ Transferred to the unfunded liability account.

Source: Injured Workers' Insurance Fund

These fluctuations began with a fiscal 2002 Board of Public Works (BPW) decision. On November 14, 2001, BPW approved an amendment to the State's contract with IWIF that included the requirement that IWIF maintain separate accounts for the State's funds. These funds had previously been commingled with other workers' compensation funds managed by IWIF.

As of December 31, 2001, IWIF established the separate accounts for the State's operating funds and future liability funds, and at the same time allocated to the operating account a portion of the total State funds on hand that would ensure a positive balance. Prior to that time, the State consistently ran a "deficit" in the operating portion, sometimes for as long as six months; IWIF would record a receivable (due from the State to IWIF) for the amount of the deficit. This deficit in the operating fund was covered by moving funds from the IWIF long-term liability account as of December 31, 2001, (fiscal 2002) to the operating account.

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When fiscal 2003 agency assessment levels were determined in August 2001, this transfer of funds from the long-term liability account to the operating account had not yet been required, and assessments were based on the then existing deficit situation in the operating fund. Then, in fiscal 2003, both the fiscal 2002 transfer had been made and assessments were higher than they needed to be – the deficit was addressed twice, in effect.

In the fiscal 2004 allowance, an adjustment is made to reflect the resulting necessary decrease in agency assessments due to the over-large agency assessment in fiscal 2003. The Governor has also chosen not to make an appropriation to the unfunded liability account, which had been made in the amount of \$20.0 million over the last few years. This decision contributed to the drop in agency assessments from \$88.4 to \$27.9 million. DBM has not assumed in its long-term forecast that the \$20.0 million appropriation to the long-term liability account will resume in fiscal 2005. This, however, is not a policy decision, so it is possible that appropriations may resume at this or another level in the future.

Recommended Actions

1. Nonbudgeted.

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Appendix 1

**Object/Fund Differences Report
Injured Workers' Insurance Fund
(\$ in Thousands)**

	CY 2001 <u>Actual</u>	CY 2002 <u>Actual</u>	CY 2003 <u>Budget</u>	CY02 - CY03 <u>Change</u>	<u>% Change</u>
Positions					
Regular Positions	379.0	389.0	406.0	17.0	4.4%
Objects					
Salaries and Fringe Benefits	\$23,669	\$26,091	\$27,935	\$1,844	7.1%
Training	133	230	327	97	42.2%
Travel	94	164	219	55	33.5%
Facility Costs	599	511	737	226	44.2%
Postage Costs	399	438	557	119	27.2%
Telecommunications	427	428	480	52	12.1%
Advertising/Promotion	958	896	1,046	150	16.7%
Staff Costs	159	187	277	90	48.1%
Printing	146	152	189	37	24.3%
Contractual Services	593	237	499	262	110.5%
Consulting Services	791	540	597	57	10.6%
Legal Expenses	266	291	570	279	95.9%
Automobile Expense	61	84	64	-20	-23.8%
Supplies	435	521	556	35	6.7%
Computer Maintenance	321	353	222	-131	-37.1%
Equipment Rental	136	0	20	20	n/a
Other Operating Costs	697	660	872	212	32.1%
Total G&A Objects	\$29,884	\$31,783	\$35,167	\$3,384	10.6%
Capital Budget	\$3,263	\$1,896¹	\$8,620	\$6,724	354.6%
Total Operating	\$33,147	\$33,679	\$43,787	\$10,108	30.0%
Funds					
Nonbudgeted Fund	\$33,147	\$33,679	\$43,787	\$10,108	30.0%

¹ The calendar 2002 capital expenditures are actuals. IWIF has not completed closeout for calendar 2002 operating (general and administrative) expenditures.