



JUDICIAL COUNCIL OF CALIFORNIA

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REPORT TO THE JUDICIAL COUNCIL

For business meeting on November 16–17, 2017

Title	Agenda Item Type
Judicial Branch Administration: Judicial Branch Workers' Compensation Program	Action Required
Rules, Forms, Standards, or Statutes Affected	Effective Date
N/A	November 17, 2017
Recommended by	Date of Report
Judicial Branch Workers' Compensation Program Advisory Committee	October 30, 2017
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Executive Summary

The Judicial Branch Workers' Compensation Program Advisory Committee recommends approval to revise the workers' compensation premium methodology for fiscal year 2018–2019. This change will result in stabilizing program administrative costs.

Recommendation

The Judicial Branch Workers' Compensation Program (JBWCP) Advisory Committee recommends that the Judicial Council, effective November 17, 2017:

1. Approve the revised premium formula for calculating:
 - a. **Claims handling fees**
Allocate based on 80 percent of losses and 20 percent of percent of payroll to trial courts and the state judiciary, with trial court judges now included with the state judiciary.

b. Brokerage and consulting fees

Allocated based on percentage of payroll to trial courts and state judiciary, with trial court judges now included with the state judiciary.

Previous Council Action

In fiscal year 2015–2016, the JBWCP Advisory Committee recommended and the Judicial Council approved a change from the “cash flow” annual premium to an “ultimate cost” basis premium. The reasons for the change were:

- To prevent further erosion of the program’s financial position;
- To bring the program into conformity with the financial practices of other public entity risk pools in California; and
- To bring the program into compliance with generally accepted accounting principles.

Once the change was approved, committee members noted that other aspects of the premium formula should be updated to reflect the change in funding philosophy. In fiscal year 2016–2017, the JBWCP Advisory Committee formally requested Judicial Council staff to develop options for updating the premium formula.

Rationale for Recommendation

In the actuarial report provided to the Judicial Council on May 19, the JBWCP’s total claims handling¹ and brokerage fees² were initially allocated to the trial courts, state judiciary, and trial court judges based on 80 percent of losses and 20 percent of payroll. This was created to ensure that a portion of these expenses was incurred regardless of claims activity and to add a component of exposure in the premium calculation. However, this also created significant volatility for entities that have very few losses.

The proposal changes two aspects of the formula:

Claims handling fees

Under the proposed method, the JBWCP’s claims handling fees will be initially allocated based on 80 percent of losses and 20 percent of payroll to trial courts and the state judiciary, with trial court judges now included with the state judiciary. This will reduce volatility in the claims handling fees for trial court judges. In addition, each member’s claims handling fees will be based on their percentage of total weighted adjusted loss and allocated loss adjustment expenses

¹ The claims handling fees represent the cost of administering workers’ compensation claims and primarily fund the program’s agreement with its third party administrator, AIMS.

² The brokerage and consulting fees represent the cost of the program’s actuarial consulting firm, Bickmore. Bickmore is responsible for calculating the total liability of the program’s workers’ compensation claims.

(ALAE)³ premium, on the theory that each member's claims handling expenses are proportional to their total estimated loss and ALAE costs.

Brokerage and consulting costs

Under the proposed method, the JBWCP's total brokerage and consulting fees will be allocated between the state judiciary and trial courts based on the distribution and percentage of payroll, with trial court judges included with the state judiciary. By excluding losses from the formula, members benefit from a more stable distribution of costs since payroll growth trends are not subject to significant fluctuation as are workers' compensation loss trends. Furthermore, there is no meaningful correlation between brokerage and consulting services and losses. The primary scope of services involves actuarial analysis and committee support, which occur regardless of members' losses.

Comments, Alternatives Considered, and Policy Implications

External comments

On July 10, 2017, the committee convened a public meeting to discuss the change to the premium calculation. The committee did not receive any comments from the public.

Internal comments

The committee had requested confirmation that the proposed changes to the formula would not impact the overall program deficit as it was determined that members are not in a position to afford any premium increases to address growing liabilities. JBWCP staff acknowledged this and confirmed that the changes are not intended to address the deficit, and it will result in a net zero impact to the program's fund balance.

Trial Court Presiding Judges Advisory Committee (TCPJAC) and Court Executives Advisory Committee (CEAC)

This report was submitted to TCPJAC and CEAC at their August 2017 joint meeting. The JBWCP Advisory Committee did not receive any comments from those committees.

Litigation Management Committee

The Litigation Management Committee approved the report at its October 2017 meeting.

Appellate Court Executive Officer Conference

The Supreme Court and Appellate Court Executive Officers reviewed the report at its meeting in October 2017. They did not have additional questions.

Alternatives

Maintaining the premium calculation formula in its current state does little to address the volatile nature of members' claims experience.

³ Allocated loss adjustment expenses can include fees paid to outside attorneys, experts, and investigators used to defend claims.

When the premiums for fiscal year 2017–2018 were calculated, approximately half of the members experienced an increase in costs due to negative claims development and increasing administrative expenses. Those courts—with little or no historical claims activity—faced significant premium increases when they were suddenly burdened with new claims. The current premium formula is sensitive to large swings in claim frequency. As a result, JBWCP staff modified the formula to address two areas:

- Volatility
- Administrative costs

Under the new premium formula, members would experience less volatility in member premiums from year to year. Percentage of payroll is typically less volatile than claims activity since payroll calculations are relatively stable from one year to the next. The formula also allows for a more equitable distribution of costs to the individual members since trial court judges would now be treated the same as all other state judiciary members and claims handling fees would be more closely aligned with actual expenses.

The premium formula uses a combination of a three-year loss distribution and a three-year payroll distribution for calculating the annual charge to each member using a weighting formula. JBWCP staff received one recommendation to expand the experience period from three years to five years. This approach stabilizes premiums for the member and reduces the impact of large cost spikes. However, this will also increase overall premiums as volatile experience periods will remain with the member for at least five years, extending the time from which the court may be able to recover from a particularly bad experience year.

Implementation Requirements, Costs, and Operational Impacts

JBWCP staff used existing claims data to project cost impacts for select JBWCP members. The data is hypothetical in the sense that JBWCP staff based its figures on existing information; the actual fiscal year 2018–2019 figures will have to account for any changes in loss developments, possible changes in administrative costs, and payroll. When applied, JBWCP staff noticed the following impacts to member premiums:

1. Actual year-to-year premium changes ranged from a low of –53 percent to a high of +126 percent. When the revised premium formula was applied, the year-to-year premium changes ranged from –34 percent to +87 percent.
2. Under the revised formula, members that experienced large increases in their premium would receive smaller increases (e.g., Del Norte and Madera Counties; the Supreme Court; the Courts of Appeal; and the Fourth Appellate District).
3. Members that experienced large decreases in their premium would receive small decreases (e.g., Butte, El Dorado, Inyo and Trinity Counties; the Courts of Appeal; and the Fifth Appellate District).

Court	Actual	Revised	Actual	Revised	2016-2017 Actual to 2017-2018 Actual	2016-2017 Revised to 2017-2018 Revised
	2016-2017	2016-2017	2017-2018	2017-2018		
Del Norte	\$26,954	\$29,960	\$60,903	\$52,886	126%	77%
El Dorado	101,036	100,416	77,020	83,014	-24%	-17%
Orange	1,420,673	1,432,323	1,616,295	1,624,114	14%	13%
Supreme Court	34,867	43,267	75,014	80,827	115%	87%
Trinity	30,763	26,302	15,336	17,281	-50%	-34%
Judicial Council	237,267	252,320	372,261	408,240	57%	62%
6th District Court	11,073	14,768	12,443	17,240	12%	17%

4. State judiciary members would receive a larger portion of the brokerage and consulting fees since they are approximately 36 percent of the payroll, but only about 3 percent of the losses.
5. In general, the revised formula will alter how the claims handling and brokerage and consulting costs will be distributed, as shown below:

Division	2013-14 to 2015-16 Payroll (\$000)	Percent Payroll	2013-14 to 2015-16 Incurred Limited to \$75K	Percent Limited Losses	2017-18 Claims Handling	2017-18 Program Admin.	2017-18 Brokerage / Consulting
Current Methodology							
Trial Courts	\$2,463,770	63.65%	\$20,849,252	96.78%	\$2,490,966	\$0	\$514,017
Judiciary	523,532	13.52%	570,792	2.65%	133,304	0	27,508
Trial Court Judges	883,637	22.83%	122,657	0.57%	138,730	0	28,627
Total	\$3,870,938	100.00%	\$21,542,701	100.00%	\$2,763,000	\$0	\$570,152
Alternative Methodology							
Trial Courts	\$2,463,770	63.65%	\$20,849,252	96.78%	\$2,490,966	\$0	\$362,890
State Judiciary	1,407,168	36.35%	693,449	3.22%	272,034	0	207,262
Total	\$3,870,938	100.00%	\$21,542,701	100.00%	\$2,763,000	\$0	\$570,152

Attachments and Links

1. Attachment A: Judicial Branch Workers' Compensation Program Advisory Committee Meeting Materials, July 10, 2017

Judicial Branch Workers' Compensation Program

Advisory Committee Meeting
July 10, 2017



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Current Premium Calculation Methodology

STEP 1:

- Determine the Total Trial Court and State Judiciary Program Costs
 - Loss and ALAE claim costs from actuarial study
 - Claims Handling Fees (TPA Fees) – The total JBWCP TPA Fees allocated to Trial Courts, State Judiciary and Trial Court Judges separately based on:
 - 80% of % Capped Losses
 - 20% of % of Payroll
 - Excess Insurance Premiums – Provided by JBWCP
 - Brokerage/Consulting Fees – The total JBWCP Brokerage/Consulting Fees allocated to Trial Courts, State Judiciary and Trial Court Judges based on
 - 80% of % Capped Losses
 - 20% of % of Payroll



Revised Premium Calculation Methodology

STEP 1:

- Determine the Total Trial Court and State Judiciary Program Costs
 - Loss and ALAE claim costs from actuarial study
 - Claims Handling Fees (TPA Fees) – The total JBWCP TPA Fees allocated to **Trial Courts and State Judiciary (including Trial Court Judges)** based on:
 - 80% of % Capped Losses
 - 20% of % of Payroll
 - Excess Insurance Premiums – Provided by JBWCP
 - Brokerage/Consulting Fees – The total JBWCP Brokerage/Consulting Fees allocated to **Trial Courts and State Judiciary (including Trial Court Judges)** based on
 - % of Payroll



Current Premium Calculation Methodology

STEP 2:

- Determine the Member Premiums:
 - 3 year experience period
 - \$75,000 loss cap
 - The total Trial Court and State Judiciary Loss and ALAE claim costs from actuarial study allocated to members based on weighted average of:
 - Estimated Loss and ALAE Costs based on % of Payroll
 - Estimated Loss and ALAE Costs based on % of Capped Losses
 - Weights based on 3 Year Payroll with largest member receiving 80% weight
 - Claims Handling Fees (TPA Fees) based on 80% of % Capped Losses, and 20% of % Payroll
 - Excess Insurance Premiums based on % of Payroll
 - Brokerage/Consulting Fees based on 80% of % Capped Losses, and 20% of % Payroll



Revised Premium Calculation Methodology

STEP 2:

- Determine the Member Premiums:
 - 3 year experience period
 - \$75,000 loss cap
 - The total Trial Court and State Judiciary Loss and ALAE claim costs from actuarial study allocated to members based on weighted average of:
 - Estimated Loss and ALAE Costs based on % of Payroll
 - Estimated Loss and ALAE Costs based on % of Capped Losses
 - Weights based on 3 Year Payroll with largest member receiving 80% weight
 - Claims Handling Fees (TPA Fees) based on % of Loss and ALAE claim costs
 - Excess Insurance Premiums based on % of Payroll
 - Brokerage/Consulting Fees based on % of Payroll



Summary

Pros of Revised Methodology:

- More equitable distribution of the costs to the individual members
 - Trial Court Judges treated same as all other State Judiciary members
 - TPA fees based on estimated Loss and ALAE costs which the TPA fees support
 - Brokerage/Consulting Fees based on % of payroll since these costs are less based on claims activity
- Less volatility in the member premiums from year to year
 - Brokerage/Consulting Fees based on % of payroll which is less volatile than claims activity
 - Actual 16/17 to 17/18 premium change ranged from -53% to +126%
 - Revised 16/17 to 17/18 premium change would range from -34% to +87%
- Members that experience large increases in their premium would receive smaller increases (ex: Del Norte, Madera, Supreme Court, 4th District)



Summary

Cons of Revised Methodology:

- State Judiciary would receive a larger portion of the brokerage & consulting fees since they are approximately 36% of the payroll, but only about 3% of the losses
- Members that experience large decreases in their premium would receive smaller decreases (ex: Butte, El Dorado, Inyo, Trinity, 5th District)



Impact of TPA and Brokerage/Consulting Change

Division	2013-14 to 2015-16 Payroll (\$000)	Percent Payroll	2013-14 to 2015-16 Incurred Limited to \$75K	Percent Limited Losses	2017-18 Claims Handling	2017-18 Program Admin.	2017-18 Brokerage / Consulting
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Impact to Premiums

<u>Court</u>	2016-2017		2017-2018		2016-2017	2016-2017
	Actual	Revised	Actual	Revised	Actual	Revised
	<u>2016-2017</u>	<u>2016-2017</u>	<u>2017-2018</u>	<u>2017-2018</u>	to	to
					2017-2018	2017-2018
					<u>Actual</u>	<u>Revised</u>
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Requested Action

Approve the revised premium methodology for calculating:

- **Claims Handling Fees**

- Allocate based on 80% of percent of losses and 20% of percent of payroll to Trial Courts and State Judiciary, with Trial Court Judges now included with State Judiciary.

- **Brokerage & Consulting Fees**

- Allocate based on percentage of payroll to Trial Courts and State Judiciary, with Trial Court Judges now included with State Judiciary.

