The Liverside e-Letter

An *Executive Briefing* on Emerging Workplace Safety and Insurance Issues

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The WSIB 2014 Funding Plan
Why it Failed

A generation later – we appear to be no further ahead

As the WSIB is about to tackle the state of the Board's financial health in earnest, a question that must be addressed front and center is simply this: ***Why is it that after almost 30 years of tackling the unfunded liability ["UFL"] the UFL appears to be as much a problem today as it was in 1984?***

At the Queen's Park **Standing Committee on Public Accounts** on February 24, 2010, the Committee's Chair, long-time serving MPP Norm Sterling (Carleton-Mississippi Mills), put it this way: "*I was in Bill Davis's cabinet in 1984 when we had this 30-year plan to solve it (the UFL) in 2014, and we appear to be no further ahead now.*"

The need for a *Funding Summit*

I have been pushing for what I have termed a "*Funding Summit*" for about a year and a half now. I first raised the suggestion in the November 21, 2008 issue of **The Liversidge *e*-Letter**, "**WSIB Funding Crisis: *Everything Old is New Again***", when I said:

> **The WSIB must organize an urgent Funding Summit**
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> By no later than mid-January, 2009, the WSIB should facilitate an urgent funding summit with Ontario's business leaders and senior government officials, to develop a new long-term funding strategy - a newly conceived 20 or 30 year plan. The Board should make this announcement right away, propose an agenda, develop alternatives, and commit to a process to be completed no later than the end of the 1st quarter of 2009. ***A new era must start today***.

17 months have passed since that suggestion and while I fully expect that the Board *eventually* will journey down that road (they really have no choice), much valuable time has been lost.

The world-wide financial melt-down is only a contributing factor – things were slipping before

Of late of course, the recent financial crisis has shouldered a disproportionate amount of the blame for the Board's current financial woes. I have been advancing an alternate theory, one that in my view is more realistic and factual – things were slipping long before the Fall of 2008.

The Board's finances were slipping before last year's market melt-down

In the October 18, 2008 issue of **The Liversidge *e*-Letter**, ***"Stay the Course or Change Direction" Tough Times. Tough Choices***", I said this:

> **Beginning in 2007 things started to dip**
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> For 2007, the excess of expenses over revenues increased to $1.13 billion **[WSIB 2007 Annual Report, p. 18]**, with $720 million of that driven by the ***Budget Reforms***. In 2007, while noting that the 2007 funding ratio had declined 6.8 percentage points to 66.4% (mainly due to falling investment returns), "*the WSIB believes that elimination of the unfunded liability by 2014 is still possible, provided improved outcomes consistent with the targets in the WSIB's Five-Year Strategic Plan, 2008-2012*" **[WSIB 2007 Annual Report, p. 21]**.
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> **LOE benefits up 12.3% 2006 to 2007**
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> Loss of earnings ["LOE"] benefits were up almost $100 million, an increase of 12.3% (from $807 million in 2006 to $906 million in 2007) **[WSIB 2007 Annual Report, p. 23]** even though injury rates continued a steady decline, in spite of more money being "invested" in labour market re-entry ["LMR"] programs. LMR costs increased 14.1% to $283 million **[WSIB 2007 Annual Report, p. 24]**. Health care costs jumped 6.7% to $527 million. Benefit liabilities increased $702 million due to the net growth in LOE claims inventory **[WSIB 2007 Annual Report, p. 24]**.

In 2006, the Board announced it had "*turned the financial corner*" – I said it was "*playing a long-shot*"

A full year before the melt-down, just after the Board announced it was "*starting to turn the financial corner*" (see the September 19, 2007 issue of **The Liversidge *e*-Letter**), I noted expenses still outpaced revenues, and other than its investment performance, the Board wasn't doing too well at all.

Until last year the Board was bullish on its finances

While the Board was being quite bullish on its state of affairs, I suggested that retiring the UFL by 2014 was a long-shot at best. Two and a half years ago, in the September 24, 2007 issue of **The Liversidge *e*-Letter - *Is the Board playing a long-shot*?** I said this:

The Board's goals are possible but unlikely

The Board just might pull it off:

- *if* there are mainly financially "fair weather days" for the next seven years (certainly *possible* but likely?);
- *if* the equity markets don't falter and continue to deliver phenomenal returns (*possible* but likely?);
- *if* there are not continued major job losses Ontario's manufacturing and particularly the automotive sector (*unlikely*) [As recently as September 8, 2007 the Toronto Star reported that Ontario has lost 200,000 manufacturing jobs over the last three years, and the Ontario jobless rate exceeds the national average for the first time in history];
- *if* injuries continue to decline (*likely*);
- and, *if* time on claim is substantially reduced (*unlikely*).

In my opinion the WSIB is playing a long shot

These are a lot of "ifs". The Board just might pull it off. *I hope they do*. Frankly, in my estimate, the Board is playing a long shot. I hope they beat the odds.

Well, the Board gambled on a long-shot and lost. That preceding narrative was not intended to give some *bona fides* to an "*I told you so*" spin, but to hit home the point that the Board's financial woes are endemic, long-standing and systemic. The Auditor General said as much in his 2009 Annual Report when he noted significant structural changes are called for:

> **However, in addition to improved investment returns and further cost reduction measures, *more significant structural changes, including legislative reforms, may be needed to ensure that the Board continues to have the ability to meet future financial obligations*. (Auditor General 2009 Annual Report at p. 317)**

So, when the Board does get around to arranging a "*Funding Summit*", and I am confident it will, the purpose of the Summit must be linked to the real, pressing issues.

Purpose of the Funding Summit

Unquestionably, the 2008/9 world-wide financial crisis layered over an already stressed workplace safety and insurance ["WSI"] system created a "perfect storm" culminating in a loss of investment capital, investment income, employer premium revenue stream, and increasing claims costs.

While the "*statement of the problem*" was addressed in recent WSIB financial statements it was confronted head-on in the **2009 Annual Report of the Ontario Auditor General** ["AG"], and received recent focus before the **Standing Committee on Public Accounts**.

The 2014 target for retiring the UFL will not be achieved. Some (LAL) have suggested that the target was unattainable before the "meltdown" whereas others (WSIB) suggested that the primary culprit was the "meltdown". *Nonetheless, there is no discord that full funding or anything close will be realized by 2014.*

A new funding strategy is required

While the WSIB possesses the legal authority to proceed unilaterally to develop a funding strategy and approach of its sole design, it would prove imprudent to do so. Because employers as a class assume final and direct responsibility for the WSIB's funding needs, employer support and ratification of the WSIB funding strategy advances a spirit of partnership and buy-in. Moreover, a joint WSIB/employer plan augments the spirit of the original 30 year funding plan linking the exercise of the Board's taxing powers to the health of the Ontario economy, aptly summarized in the WCB 1983 Annual Report:

> **"…the ultimate health of the workers' compensation system depends on the continued strength of the province's economy"**

The purpose of the Funding Summit is multi-faceted

***Objective one*:** To trigger and cultivate a renewed partnership with Ontario's employers generating a revitalized spirit of cooperation and support, sharing ownership of the both the problem and the solution.

***Objective two*:** To mutually define new objectives with clear deliverables based on new fundamentals, all of which is to be built on a common knowledge base, all the while respecting prescribed legislative expectations.

***Objective three*:** To translate the objectives into a workable business model that will endure regime change and respect inter-generational equity.

***Objective four*:** To structure a meaningful review methodology that allows for a structured mechanism to assess progress and adjust the plan if warranted.

Why the 1984 thirty year plan failed

The "1984 thirty year funding plan" ["1984 Plan"] was not an outright failure. It succeeded in creating an awareness of the funding frailties of the Ontario WSI system for a generation. Other than that, it never came close to achieving a policy objective of full funding. *Why?*

***Reason No. 1*: The plan was not a serious commitment – the founding objective was not funding**

The 1984 Plan never represented a serious commitment to retire the UFL by 2014. The 1984 Plan was more crisis management (curtailing premium hikes) than funding policy. The Board was clumsy in its lead-up to the 1984 Plan, and instead of embarking on a pre-emptive thoughtful consultation with Ontario's employers; it responded to a looming funding crisis (miniscule by today's standards) and reacted with proposed rate hikes in excess of 20-30%.

This triggered an explosive employer backlash politicizing the issue. ***The "crisis" solved by the 1984 Plan was not funding but rather employer discontent.*** Once employer discontent was effectively managed through a longer term vision reinforced and with acceptance of six years of premium rate hikes, urgency cooled. From 1984's vista, 2014 was far enough out to be a problem deferred to another generation and close enough not to be ruled irresponsible.

***Reason No. 2*: Competing priorities**

From the early 1970s (Aird Task Force) to the early 1990s (post-Weiler), the primary policy worry of the WSI system was worker equity not funding or system costs. ***This policy focus was reasonable and objectively based***. Prior to the 1985 (Bill 101: Representative Board of Directors; independent

Appeals Tribunal) and 1990 (Bill 162: Wage loss and reemployment obligations/rights) reforms, which congregated on a myriad of worker equity issues, the system *was* systemically unfair to workers ("Meat chart" pensions; an insensitive administration; inadequate benefits; lack of reemployment opportunity and rights; etc.).

As most clearly delineated by Prof. Weiler in his seminal 1980 report (**Ontario, Reshaping Workers' Compensation for Ontario, November, 1980**) the system of the late 1970s and early 1980s was not responsive to contemporary worker needs. *Change was demanded, required and delivered.*

The early 1980 funding considerations were little more than a transitory distraction, resolved with the 1984 Plan. After that, until the mid-1990s, design and administrative focus was almost exclusively set towards establishing a higher standard of worker equity.

That the Board's funding ratio immediately dipped from its 1983 level of 49% to a floating 30-40% range until 1996 ought to be no surprise. ***While a higher level of funding was no doubt desired, it was not sought.***

The system was not responsive to the efficacy of the 2014 Plan until the introduction of the Friedland formula (1994) and modified Friedland (1997). Yet, even at these two junctures, a strong commitment to full funding never materialized. With the introduction of Friedland, retroactive increases to worker benefits were implemented. In 1997, premium rates commenced a decline.

In short, a full funding policy was supplanted in the 1980s and early 1990s by a policy preference towards increased benefits and in the late 1990s by a policy preference towards lower premiums. Achieving 100% funding has itself never been a policy priority.

I am not saying that the policy objectives that trumped a priority of full funding were not sound policy. They may well have been. I am simply suggesting that a goal of full funding, spin and rhetoric aside, has never been a significant priority of the Ontario WSI scheme. The last 26 years has proved that.

***Reason No. 3*: A design flaw – a serious policy realignment was not possible**

The 1984 Plan was defeated in part by its simplicity that full funding was to be achieved over a thirty year period with the combined power of serial and cumulative achievements: injury reduction; persistency reduction; cumulated investment performance; and a stable or increasing economy (See **WSIB Funding Framework, May 2008**, pp. 7-8 for a summary of the most current presumptions.)

While in recent years the Board developed multi-year funding strategies, the fundamentals of the 1984 Plan (100% funding level by 2014) was always accepted as the target ("*The target full funding date is 2014, which is the original 30-year funding target date established in 1984*", **WSIB Funding Framework, May 2008**, p. 6. "*The WSIB is committed to a planned and disciplined approach to achieving full funding by the target full funding date*", p.7)

There was never any real serious capacity to objectively move off that target. ***Yet, the target itself was not taken seriously***. One need look no further than the WSIB's Q&A informational document which accompanied the announcement on 2008 premium rates, released in mid-2007, for evidence that supports the proposition that *the target was driving the presumptions rather than the presumptions driving the target*.

That year's announcement followed the government's amendments increasing worker benefits beyond the legislative prescribed levels, triggering close to $1 billion in unanticipated cash outflows. *Yet, premiums did not increase*. The reason behind stable premiums was not founded on objective evidence of past and actual performance, but rather on the "hopes" that "*all partners in Ontario's workplace safety and insurance system continue to achieve breakthroughs in health and safety and return to work.*"

Absent from the plan was a serious incremental review and assessment mechanism, other than the yearly premium rate setting process. In response to the inevitable attraction of "*toe-the-line*" on yearly premiums, the presumptions tended to become rather "*rose coloured*" over time.

To avoid the "*tail wagging the dog*" the policy choice of low premiums was achieved not by an honest recalibration of the 1984 Plan, but instead by an overly optimistic and over time unrealistic and unattainable series of presumptions.

That the Board still held to the expectation that the WSIB would "*reduce the number of workers still on benefits at various claim durations by 10 to 20 per cent by 2012*" (**WSIB Funding Framework, May 2008**, p. 7) when all objective evidence showed a systemic trend in the opposite direction, colours the true depth of commitment to the 1984 Plan. Even *before* the significant increases arising from the amendments introduced in the 2007 Budget, the Board attributed a 11.5% increase in benefits (2006 over 2005) to "*persistency of claims over 12 months old, natural growth of locked-in claims each year, and indexing*" (**WSIB 2006 Annual Report**, p. 26).

So, what seemed to have evolved is simply this – a priority of full funding was usurped by a priority of premium stability. Again, I am not suggesting that this was not a more appropriate policy goal of the time – it may well have been. In fact, the vast majority of employers supported this approach. I am simply suggesting that a goal of full funding was not the pressing priority.

The objective of full funding by 2014 had evolved into a belief system, not a business plan. 2014 became the "Holy Grail" of WSIB economic policy.

***Reason No. 4*: The spectre of unintended consequences**

The 1990 amendments (Bill 162) and the 1997 amendments (Bill 99) redefined the terms of the "*insurance contract*" prescribing benefits based on actual wage loss. *The premise was based on sound policy* – an individual's earning capacity is influenced as much, or more, by socio-economic elements as it is by degrees of actual impairment.

Coupled with these giant reform steps was a structural shift towards improving individual earning capacity through early rehabilitation intervention, with the expectation that even the seriously injured individual would be able to return to gainful employment and re-establish an earnings profile, which overall should result in lower aggregate claims costs.

The initial wage loss model was slightly modified in the 1997 amendments but the essential features remained.

"*Locking in*" benefits by the end of the 6th year post-injury was introduced as a mechanism to curtail unnecessary administrative activity on established cases predicated on the presumption that within 72 months the injured worker would have achieved maximum earnings potential. At least that was the (unproven) theory. *I didn't buy it then and I certainly don't now.*

Concurrent with these initiatives was the introduction of experience rating ["ER"], a program designed, in part, to encourage employers to re-employ disabled workers early in the course of the claim.

Ironically, the "lock-in" feature and certain elements of ER policy ("three year window") diminished the capacity of the Board to affect the desired outcome in the most serious of cases. For the seriously injured, after a period of protracted medical rehabilitation which may consume the initial several years in the lifespan of the claim, the focus would turn towards vocational rehabilitation, another lengthy process. Often, by the time of the lock-in a worker may not have achieved maximum earnings capacity.

In addition, in the serious case with no return to work within the first three years, an employer lost financial motivation to permanently rehire workers.

Moreover, adding to this, worker motivation would understandably abate in the few years leading up to the "lock-in". *Why trade certainty for uncertainty?*

In short, critical system design elements are at odds with system objectives and expectations.

Reason No. 5: A lack of policy discipline – the tarnishing of an objective

In an unprecedented move, just as the funding fortunes of the Board were improving (as a result of investment gains, not performance gains), the **2007 Ontario Budget** included amendments to the *Workplace Safety & Insurance Act* to increase worker benefits beyond the prescribed statutory inflation adjustments, adding $750 million in immediate expenditures. For the record, and as I have repeatedly set out in these pages, I support full indexing. But, as I noted in the September 12, 2007 issue of **The Liversidge *e*-Letter:**

> Full benefit indexing *is* a good idea. Worker benefits should not be eroded over time by inflation. But, indexing must be responsible, and achieved in a way that does not risk pushing the Ontario WSI system back into yesterday's malaise, where expedient political decisions to increase benefits without the requisite funding almost bankrupted the system. *But, raising taxes carries its own prevailing risks.*

A year ago, in the Spring of 2009, the Board announced that the 1984 Plan was dead. Yet, in December 2009 a further $200-$300 million was expended by similar legislative amendments at a time concurrent with the Board's public declaration that it was facing an unprecedented financial crisis.

These moves rendered the 1984 Plan moot and in my opinion stamped out the moral authority of the Board to achieve full funding through premium rate hikes.

OK, so where from here? The timing and duration of the Funding Summit

First the "Funding Summit" I envision is a long-term project, a "roll-up-your-sleeves" type of exercise, with the Board forging a dynamic partnership with Ontario's employers. I expect that the desired WSIB/employer consensus will take no less than 9-12 months to be achieved, and another 1-3 months to codify into a workable and durable policy. The process must start immediately, and should be the first order of business after the employer Advisory Committees ["AC"], (as recommended by WSIB Chair Mahoney) are struck. I offer the following as a guide.

I suggest that a series of meetings be scheduled at regular intervals commencing in May, 2010. This schedule should be flexible to allow for the striking of select *ad hoc* sub-committees to address specific issues as considered appropriate. The **Funding Summit** will then re-group after twelve (12) meetings have been held to assess the future and continuing agenda.

Structure of the Funding Summit Committee

The members of the Funding Summit should be drawn from each of the ACs (except the Schedule 2 AC). Each AC will elect a set number of delegates. The WSIB will resource the Funding Summit in a similar manner to the administration of the ACs ensuring sufficient dedicated resources.

The agenda

While Funding Summit participants will define the agenda, at a minimum, the following issues and approaches are suggested as a rough guide.

Meeting No. 1 (May, 2010): Defining and understanding the scope of problem

The WSIB will "open its books" and fully disclose the scope of the problem. The Board will present alternative scenarios to project the likely future realities facing the WSI system. ***The key questions*:**

- Where will the system be if the current presumptions hold true 5, 10, 15 and 20 years out?
- Are the presumptions realistic?
- What if frequency targets are not met or rate of injury reduction slows?
- What if claims persistency continues current upwards trends? Slows but no decline?
- What if investment targets are not met? Or, inflation projections exceed expectations?

- What are the premium rate pressures to attain full-funding status, under a variety of mitigation scenarios?
- How do premium rate pressures abate with a funding target reduction to 90%, 85%, 80% or 75%?
- What are the most likely scenarios?

The purpose of the first meeting is to ensure that all participants fully understand the scope and depth of the challenges of the WSIB, and understand that change in one form or another is essential.

***Meeting No. 2 (June, 2010):* A closer look at the drivers**

An examination of contemporary trends and an informed and open exploratory discussion on potential causes.

- *A look at the "claims inventory":* 1-6 years duration cases and 6 years+ (locked-in) duration cases
- *Medical costs:* An assessment of medical costs against a theoretical construct – WSIB versus universal social health care
- *An introductory discussion:* What are the primary policy objectives of the Ontario WSIB?
- *Administrative costs:* Value for money and channelling resources towards objectives

***Meeting No. 3 (July, 2010):* Comparing Ontario**

Much can be gleaned from experiences in other jurisdictions. A "*made in Ontario*" solution is not necessarily essential.

- *How does Ontario stack up*: With comparable Canadian provinces? With comparable American jurisdictions (size and proximity) With comparable world systems? (Australia; Europe)
- Contrasting Ontario with relevant world wide trends

***Meeting No. 4 (August, 2010):* An Economist's perspective**

The viewpoints of a leading, world renowned economist with a solid reputation contributing to tax related public policy to address:

- The economic and competitive truths arising from WSIB funding realities and challenges;
- The implications of standing still and the cost of moving forward
- A review of the overarching public policy role of a modern WSI system
- Roundtable discussion

***Meeting No. 5 (September, 2010):* Where is the system succeeding? Where is the system failing?**

An objective assessment of the system's attributes (positives and negatives):

- What can the Board do without? What does the Board need more of?
- A discussion of the role of government
- Is the WSIB in reality an "arms-length" public body? Should it be?
- The broad implications of premiums as a payroll tax to the overall taxation burden of Ontario business
- What is the actual current role and influence of government? What should it be?
- What should government directly decide?
- Since indexation levels beyond prescribed amounts are now the purview of the Executive Council, should employer premiums be afforded similar treatment?
- Accounting for the unfunded liability and assessing the Auditor General's suggestions as set in the 2009 Annual Report of the Auditor General

***Meeting No. 6 (October, 2010):* The funding policy options**

A realistic discussion on the burdens and benefits of a target of full or better funding.

- A full and open discussion of new approaches to modern WSI administration
- Is full funding a necessary target in the medium term?
- A nuts and bolts analysis of the various funding options available

***Meeting No. 7 (November, 2010):* Deciding on a policy**

Developing a consensus on a new funding policy

- A Funding Framework that will be welcomed by tomorrow's generations

***Meeting No. 8 (December, 2010):* Identifying related policy initiatives**

Is a renewed funding policy enough?

- An assessment of the expenditure side
- Controlling controllable costs
- Assessing the challenge of increasing time on claim
- What is within the Board's role – what is not?
- The WSIB as policy adviser to the government - *Is the Board an agent of reform or an administrator of the status quo?*
- An assessment of the current benefit delivery model: *After two decades of experience with a wage loss system, what are the lessons?*
- What is the ideal benefit delivery model? Is Ontario there? If not, define the road to perfection
- Reducing/eliminating the risk of legislative "wild cards"

***Meeting No. 9 (January, 2011):* Setting the benchmarks**

Planning to monitor and monitoring the plan

- The development of specific funding targets to be achieved within specific timelines

***Meeting No. 10 (February, 2011):* Setting the review mechanism**

Reviewing progress – the mechanism

- The implications of worse than expected performance
- The implications of better than expected performance

***Meeting No. 11 (March, 2011):* The communication of the plan**

Developing support:

- The Board's role
- Employer associations
- Developing a communications plan

***Meeting No. 12 (April, 2011):* Regrouping and assessing next steps**

- A look back at the year
- A look ahead at the decade

The most important next step is the decision to proceed. As I said in the December 18, 2009 issue of **The Liversidge *e*-Letter**, "*I may forever be an optimist, but I see opportunity around the corner*". But, there's no time to lose.