Workers' Compensation Covid-19 Update

In recent history, workers' compensation insurance, as an overall line of business, has been rather profitable. In May 2019, NCCI reported a calendar year combined ratio of 83% for 2018, which was workers' compensation's most profitable year in modern history. Based on the information BMS has viewed, we expect that those tailwinds also flowed into last year. Another successful year gives us a reason to cheer during the upcoming NCCI Virtual Conference.

However, workers' compensation is one of the lines of business most impacted by COVID-19. Layoffs and furloughs are leading to dramatic payroll drops and climbing the unemployment rate. Reduction in payroll is greatly reducing premiums, and increases in unemployment have historically correlated with adverse claim results. We now have the issue of potential assumed workplace causation leading to loss compensability related to the coronavirus itself, which is now under debate within state legislatures. Depending on the legislative and ultimately judicial outcomes, worst case scenarios point to a workers' compensation "catastrophe" ranking as one of the largest disasters in insurance history.

In this report, we cover:

- BMS' expectations for NCCI's upcoming "State of the Line" results for 2019
- Presumption statutes watch
- Briefings on the two publicly traded pure-play WC specialists. What did we learn from their recent earnings reports?

Anticipating NCCI's 2019 State of the Line

Next week, NCCI will be releasing their view of 2019 workers' compensation results in its State of the Line presentation. Last year, NCCI surprised many within the industry by presenting profitable results for workers' compensation in 2018.

BMS research forecasts that the NCCI's published results will be similarly profitable for 2019. Calendar year results are expected to be somewhat close to last May's report, although, the combined ratio may rise due to fewer prior year loss reserves being released. Meanwhile, and somewhat surprisingly, expense ratios are holding steady year-over-year, despite nationwide rate/loss cost decreases. We expect the NCCI to report a slightly lower accident year combined ratio (2018 accident year was 97% versus the previously stated 83% calendar year combined, illustrating the significance of favorable prior year reserve development recognized in 2018) for 2019, likely in the mid-90s, confirming the continuing overall underwriting profitability of the workers' compensation line of business.

This news should be overwhelmingly positive for workers' compensation insurers; however, profitable State of the Line results have often been followed by loss cost and ultimately primary rate decreases in NCCI's member states. With the impact of COVID-19 looming, we would expect significant carrier reaction to any proposed downward loss cost revisions in 2020.

Presumption Statutes

While most acquired viruses (e.g. influenza or a cold) would not be compensable under workers' compensation, many states either have, or are contemplating the enactment of "presumption coverage" for front-line workers and other essential employees. These legal provisions would assume that for any qualifying employee diagnosed with COVID-19, it can presumed that the employee contracted the disease on the job, thus triggering workers' compensation coverage. A widely based presumption statute has already been adopted in Kentucky, and worker representative organizations like the AFL-CIO are pushing for many states to take the same approach.

Based on current estimates, fully transferring these costs from healthcare to workers' compensation would have a significant impact. For example, California's rating bureau (WCIRB) recently estimated a range of costs between \$2.2B and \$33.6B, with a midpoint of \$11.2B, should presumption become law. The wide range is dependent on:

- The level of presumption. Is the presumption "conclusive" or "rebuttable?"
- The scope of employees covered. Will the presumption cover first responders and healthcare workers only (ECI-1), or will it involve other "essential" employees (ECI-2)?

The scope of this legislation could significantly burden workers' compensation carriers.

UPDATE: California Governor Gavin Newson issues an executive order.

Last week, the NCCI also published its estimates on compensable COVID-19 claims. Like California, NCCI's estimates reflect a potentially ruinous outcome for the workers' compensation line, ranging from \$1B to \$80B in losses. FYI – The NCCI has put its COVID-19 scenario loss estimator online. **(Linked here)**

Most states are contemplating that "conclusive presumption" regulation will apply to first responders only, such as police, fire and emergency medical personnel. If this trend continues, the impact to private market workers' compensation carriers should be manageable, as many of these exposures are in self-insurance facilities. With that said, it is an issue worth watching carefully.

The Reinsurance Association of America is providing regular updates to regulation and legislation with respect to workers' compensation. **(Linked here)**

Results from Publicly Traded WC Specialists

On April 21, Employers Insurance Holdings (EIG) released its earnings for the first quarter of 2020. Amerisafe (AMSF) released their Q1 2020 earnings on April 29. Here are some highlights of those reports:

Employers Insurance Holdings (EIG)

EIG reported a modest loss, but it also did not take down any reserves for recent underwriting years (a major recent driver of WC profitability). The first half of April recorded \$6M in endorsed premium reductions, which roughly equates to a run-rate decrease in premium of 20%, should it persist. EIG targets small to mid-sized employers, with a heavy concentration in California.

EIG is not anticipating a great deal of COVID-19 claims. The classes written by EIG tend not to be the "essential" employee classes being considered in California's presumption legislation, however the premium income associated with the overall book is being negatively impacted by payroll decreases associated with workplace reductions. EIG is currently experiencing a noticeable drop in claims frequency, likely due to COVID-19. While EIG is maintaining a steady loss ratio for 2020, this has the potential to improve due to the ongoing frequency drop, depending on major states' position on the compensability of COVID-19 claims.

EIG noted that it does not anticipate a reinsurance recovery from its excess of loss reinsurance treaty (attaching at $10M per occurrence). It cited the "hours clause" in its reinsurance contract as a limitation to an excess of loss reinsurance recovery. This is in reference to the window of time in which an employer can combine claims, as they relate to occupational disease or cumulative trauma. BMS brokers, and its contract writing team are reviewing its clients' exposures and contract language to determine coverage implications related to COVID-19. We are also closely monitoring wording changes that have been proposed by the market, due to the pandemic.

Amerisafe (AMSF):

AMSF reported a profit for Q1 2020. Its combined ratio came in at 83.5%, largely driven by reserve take-downs for accident years 2012-2017. Gross premiums were down by 6% YoY, due largely to loss cost reductions hence premium reductions in its key classes/states. Their expense ratio rose 2% due to lower net earned premiums.

AMSF policyholders are small to mid-sized employers engaged in hazardous industries, principally; construction, trucking, logging and lumber, and manufacturing. Many of these are "essential," but not front-line exposures; therefore, its exposure to both payroll drops and COVID-19 claims should be manageable. Most of AMSF's insureds report payroll on a monthly basis; AMSF saw its March payroll reports coming in around 8% below original estimates. The company has also seen reduced claims frequency, though AMSF expressed concern about temporarily disabled workers (likely injured prior to COVID-19) not receiving access to in-person care; potentially leading to adverse injury outcomes and claims severity.

Key Takeaways:

- BMS expects the NCCI will report favorable results for 2019; however, resulting rate decreases are uncertain and perhaps unwise in a declining interest rate environment.
- Presumption statutes are an evolving issue that require considerable attention as they have the potential to deliver extraordinary losses to the workers' compensation market - depending on the level of presumption and scope of qualifying occupational classes.
- Publicly traded "pure play" workers' compensation insurers are reporting large payroll declines, but the underwriting results are holding steady. While presumption is a concern, reduced claims activity during the quarantine period could potentially lead to continued profitability, but the range of potential outcomes is extreme.

Meanwhile, the reinsurance market is in transition. While capacity remains available, reinsurance markets are becoming more selective in how they deploy their capacity to workers' compensation carriers.

BMS Re is staying on top of the constantly evolving issues affecting both insurers and reinsurers of workers' compensation business. Now more than ever, workers' compensation carriers need to be in regular contact with their reinsurance partners to attain optimal terms and flexibility.

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