Fiscal Note & Local Impact Statement

127 th General Assembly of Ohio

Ohio Legislative Service Commission
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BILL: **H.B. 79** DATE: **May 8, 2007**

STATUS: **As Introduced** SPONSOR: **Rep. Batchelder**

LOCAL IMPACT STATEMENT REQUIRED: **No — No local cost**

CONTENTS: **Bureau of Workers' Compensation investment policy changes**

State Fiscal Highlights

STATE FUND	FY 2008	FY 2009	FUTURE YEARS
State Insurance Fund			
Revenues	Possible gain or loss	Possible gain or loss	Possible gain or loss
Expenditures	Decrease, possibly in the $25 million range	Decrease, possibly in the $25 million range	Decrease, possibly in the $25 million range
Administrative Cost Fund (Fund 023)			
Revenues	- 0 -	- 0 -	- 0 -
Expenditures	Increase, possibly in the millions	Increase, possibly in the millions	Increase, possibly in the millions

Note: The state fiscal year is July 1 through June 30. For example, FY 2007 is July 1, 2006 – June 30, 2007.

- Investment returns into the surplus and reserve of the State Insurance Fund could increase or decrease as a result of the bill limiting investments of the State Insurance Fund to a "white list" of permitted investments and removing prohibitions on certain investment classes under current law, depending on the classes in which funds are invested and the state of the markets.

- Expenditures from the State Insurance Fund could decrease with the bill's provision prohibiting the Administrator of Workers' Compensation from contracting with an investment manager, investment information services, consulting services, and other like services.

- A decrease in contract expenditures from the State Insurance Fund would likely be at least partially offset by an increase in expenditures from the Administrative Cost Fund in order to pay for investment managers and consultants to join the Bureau's staff.

Local Fiscal Highlights

- No direct fiscal effect on political subdivisions.

Detailed Fiscal Analysis

Permitted investments

House Bill 79 removes the current statutory requirement that the Administrator of Workers' Compensation make investments and manage the various workers' compensation funds in a manner that a prudent person acting in a like capacity and familiar with such matters would use in an enterprise with like character and like aims, including diversification of investments to minimize risk unless circumstances render it not prudent to do so. The removal of this requirement opens the potential for the Bureau of Workers' Compensation (BWC) to invest moneys in the surplus and reserve of the State Insurance Fund (SIF) in investments with high returns, but also high risk. However, in place of the "prudent person" standard and in order to provide some investment limitations, the bill also enumerates the classes in which the Bureau is permitted to invest and places additional restrictions on how much of the SIF may be invested in certain classes, thereby serving to mitigate the effect of removing the prudent person standard from the law.

Under the bill, the Bureau (acting through the authority of the Administrator) is required to invest funds of the State Insurance Fund in any of 28 investment classes specifically identified in division (A) of section 4123.442 of the Revised Code. These are described in detail in the LSC bill analysis. This "white list" limits the classes the Bureau can invest in only to those specifically named. The bill also removes a list of current prohibited investments and places restrictions on the list of permitted investments that prevents the SIF from containing investments in large portions of single companies or investing large fractions of the fund's surplus and reserves in a single type of asset class, such as real estate or railroad holdings.

The bill could have either a positive or negative effect on investment returns into the surplus and reserves of the State Insurance Fund as a result of these changes, depending on the allocation of assets in the Bureau's investment portfolio and the state of the markets for those various assets.

Contracting with investment managers and consultants

The bill prohibits the Administrator from entering into contracts with outside investment managers, consultants, information services, and other like services. Under current law, such contracts must be paid for out of the State Insurance Fund. According to the Bureau of Workers' Compensation, the current contract for investment consulting services with Wilshire Associates is approximately $650,000 per year and the current contracts for investment management services with State Street Global Advisors and Barclays Global Advisors are estimated at a total of $3 million per year for a portfolio that is invested *100% in passive assets.* The Bureau is currently engaged in an effort to transition its investments into a portfolio that would have 40% of all investments managed actively, which would require increased costs. Current BWC estimates place total annual costs for a portfolio with outside investment management that is *60% passive and 40% active* at approximately $20 million to $25 million. It should be noted that these are estimated costs for managing a total portfolio of approximately $17 billion and that, logically, one would expect that returns on these investments will more than compensate for any management fees the Bureau may incur.

Under the provisions in the bill, these contract expenditures would no longer be paid from the SIF, opening up additional moneys in the fund for further investment or to pay compensation and benefits for injured workers. Alternatively, a corresponding minor reduction in employer premiums could result if funds are no longer needed in the SIF to pay contracting expenses for investment managers and consultants. It is possible, however, that any decrease in expenditures from the SIF as a result of the prohibition on contracting would at least partially be offset by a corresponding increase in expenditures from the Administrative Cost Fund (Fund 023).

Possible increase in BWC investment staff costs

If the Bureau is unable to contract with outside investment managers and consulting services, such services would likely have to be provided for in-house, requiring the staff of the BWC Investments Division to expand to include investment experts paid via Fund 023. At current pay rates for the "Investments Officer" employment classification as defined by the Department of Administrative Services, these staff members would earn between $54,246 and $71,032 per year for an Assistant Investments Officer and between $65,686 and $86,174 per year for a senior level Investments Officer. This could result in an increase in the rates charged to employers for assessments on workers' compensation premiums that go into Fund 023 in order to cover the additional payroll costs and any additional administrative costs associated with managing BWC's investments in accordance with the policies laid out in current law, the BWC investment policy, and under the provisions of this bill.

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