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March 15, 2016

Mr. Mike Shinnick  
Manager, Workers' Compensation  
Tennessee Department of Commerce & Insurance  
500 James Robertson Parkway  
Nashville, TN 37243

Re: National Council on Compensation Insurance ("NCCI")  
Law-Only Filing – Proposed Effective Date August 28, 2016

Dear Mr. Shinnick:

We have completed our review of the above-captioned filing. Our findings and conclusion follow.

**Summary of Filing**

This Tennessee law-only loss cost change, to be effective August 28, 2016, takes into account the effect of the changes due to:

- A. Adoption of a Closed Drug Formulary
- B. Medical Treatment Guidelines

NCCI estimates that the effect of (A) will be -2.7% of the overall loss costs. Regarding (B), the filing states, "NCCI is unable to estimate the potential cost impact from the adoption of the enacted rule regarding medical treatment guidelines due its optional nature (i.e., uncertainty as to how the guidelines would be implemented, administered and used in practice), as well as the lack of relevant statistical data upon which to predicate an estimate."

**Background:**

The Official Disability Guidelines ("ODG") Workers' Compensation Drug Formulary is a detailed list of prescription drugs that are frequently used in the treatment of injured workers. Within this list, there is a status indicator that identifies whether or not each drug requires preauthorization. Drugs with a status indicator of "N" (N-drugs) require preauthorization, while drugs with a status indicator of "Y," (Y-drugs) preferred drugs, do not require preauthorization, with the exception that initial prescriptions presented to a pharmacy for an alleged or accepted workers' compensation claim may be filled for a maximum of seven days, even if the drug status is "N". The list of preferred drugs, those that do not require preauthorization, defines the "closed formulary." With the implementation of a Closed Drug Formulary, three factors are considered:

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- The degree to which Y-drugs or other non-drug treatments would be substituted for N-drugs
- The degree of elimination of N-drugs
- The degree of authorization of N-drugs

The impact of these factors can be determined by analyzing the anticipated reduction in N-drug average costs per claim.

**Analysis:**

An audit of the NCCI data and verification of the detailed calculation was beyond the scope of our review. We did, however, review the summary calculation of the final impact.

Based on NCCI's Tennessee data, the relevant statistics were:

- (a) Medical Benefits Loss Cost = 70.9% of total loss costs
- (b) Prescription Drug Payments = 18.0% of all medical benefits
- (c) N-drug Prescription Drug Payments = 27.8% of all prescription drug payments
- (d) N-drug Cost reduction = [*delta*%]

The overall loss cost impact is the product of all four quantities above [ $0.709 * 0.180 * 0.278 * \textit{delta}$ ].

To determine *delta*%, NCCI relied on three observed statistics:

- NCCI estimates a -92% difference in N-drug average cost per claim for Accident Year (AY) 2014 (\$1.61) relative to AY 2010 (\$19.58) at 12-month maturity in Texas<sup>1</sup>
- Texas experience shows that the average N-Drug cost per claim in Service Year 2014 (\$35) is 75% lower than the average for Service Year 2010 (\$140)
- The Texas Department of Insurance has calculated an 83% reduction in the total N-drug costs from Fiscal-Accident Year 2011 (ending August 30, 2011) to Fiscal-Accident Year 2012

NCCI selected the N-drug cost reduction, *delta*%, to be -75%. The overall loss cost reduction =  $0.709 * 0.180 * 0.278 * -0.75 = -0.027$  (-2.7%).

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<sup>1</sup>Both the Texas and the Tennessee implementations have the first seven days exception for the initial prescriptions. In addition, both implementations apply to all claims, new and legacy claims alike, though with staggered effective dates.

**Findings:**

We are of the opinion that the analysis was performed in accordance with applicable Actuarial Standards of Practice, and we concur with NCCI's stated opinion that the effect of the Medical Treatment Guidelines is not quantifiable at the present time. We have no objection to the requested loss cost changes.

Sincerely,



Christopher J. Burkhalter, FCAS, MAAA  
President & Principal

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