

2016 Annual Report from Pinnacol Assurance

To Governor John Hickenlooper
and the Colorado General Assembly

Dec. 5, 2017



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Introduction

For more than 100 years, Pinnacol has provided workers' compensation insurance to all Colorado employers that seek it. This coverage ensures workers injured on the job receive benefits covering lost wages and medical costs and employers are protected from potentially catastrophic losses. Without Pinnacol, many companies would be unable to secure workers' compensation coverage for their employees. In 2016, we provided workers' compensation insurance to nearly 56,000 employers in the state, and protected the lives of almost 900,000 Colorado workers.

The last century has seen a lot of change, but our world has never moved as fast as it is now. Ensuring our customers are able to protect their employees and remain competitive in this dynamic environment means changing to meet their evolving needs. In 2016, we set out to do just that.

A new vision and mission

We started at the most fundamental level: updating our vision and mission statements. Our previous vision was to be the best workers' compensation insurance company in the nation and the most respected company in Colorado, and our mission was to provide assured protection to Colorado employers and their greatest asset — their employees. But they didn't capture what Pinnacol is and aspires to be. So we brought together a group of employees from all levels of the organization to think about a vision and mission that would better capture who we are and where we want to go. Already known for our caring culture and drive to keep people safe and productive, we needed something to represent our focus on innovation.

This effort produced a new mission: *To provide caring protection for Colorado employers and their employees.* And our vision became: *To lead a revolution in caring for people, businesses and our community.* The caring component has always been integral to Pinnacol; the reference to "revolution" reflects our belief that we can and must innovate to do still more for the injured workers, businesses and communities we serve.

For us, central to a revolution in caring is ensuring that the "Voice of the Customer" informs our actions. Listening to them. Hearing what they want, what they like and what they don't like about interacting with us — and then acting on what they've told us. In almost every case, this means increased speed, ease, user control, and lower costs.

Innovating to add value

This kind of improvement doesn't happen overnight, but rather through many small and intentional changes. That's why we're reimagining every aspect of what we do and using Toyota Lean methods to reduce waste and improve the experience for all the customers we serve.

For example: last year, our business service representatives examined a process that included moving thousands of pages from one part of the building to another, multiple handoffs and duplication every day. Multiple departments came together to strip the process down to only those tasks that added value. The results are impressive: 80 percent reduction in time spent, nearly 80 percent decrease in distance traveled around the building, and 100 percent on-time completion rate.

We also began a full-scale reinvention of our customers' digital experience in 2016. It started with a new policyholder portal featuring online payments and enhanced payroll reporting. These improvements hit the mark, increasing registered users by 475% to 19,000 in just one year.

We will always work to innovate and care for customers, but Pinnacol continues to labor under statutory constraints that haven't kept pace with our fast-changing world. The statute that governs Pinnacol, written more than 100 years ago, dictates that Pinnacol write only in Colorado and offer only workers' compensation. But many Colorado businesses are seeking bundled business insurance that follows them even if they expand outside Colorado. Other carriers — including state workers' comp funds, big national carriers and online start-ups — have been successful in attracting these employers with more flexible products. Our focus remains on

developing the kind of service our evolving customers need, but the statute continues to hinder our ability to be the best Pinnacol we can be.

Serving Colorado employers

We knew that if we achieved our new mission to provide caring protection for Colorado employers and their employees, they would see the difference. Improving how we help keep employees safe, ensuring they get the care they need, and contributing to our community are all ways we would demonstrate our commitment to their wellbeing.

Customer satisfaction: Three key metrics from 2016 show our stakeholders have taken notice:

- Policyholder satisfaction score was 8.42 out of 10 points for overall service quality
- Policyholder retention rate, based on written premium, was 89 percent
- Injured worker satisfaction score was 3.87 on a 5-point scale. The average score for all other carriers in Colorado was 3.52.

Safety services: Every Colorado employee deserves a safe workplace, and Pinnacol is doing its part to make that a reality. We have the largest, most experienced team of safety consultants in the state, and they invest more than **35,000 hours every year** helping our policyholders across the state keep their worksites safe. Pinnacol's team includes experts in areas like industrial hygiene and ergonomics, and industries like construction and oil and gas. We also offer hundreds of safety resources to our policyholders at no cost, including webinars, posters and sample documents. Many of these materials are available for download whenever an employer needs them.

Ensuring injured workers get the care they need

Pinnacol covers workers across Colorado, and in 2016 we paid for medical care and provided wage replacement benefits to **nearly 44,000 injured workers**. Just three percent of claims were contested (denied) in 2016, most often because the injury was not work-related.

Investing in our community

As a large employer that touches a majority of Colorado employers, we understand the impact we have on the state. Pinnacol plays an outsized role in Colorado's economy, providing stable coverage that employers can count on year after year. But our mission to provide caring protection extends beyond our employers and their employees. We designed our community investments to positively impact all Coloradans in three main areas:

- Helping injured workers get better. In 2016 we helped fund organizations such as Craig Hospital, the Brain Injury Alliance of Colorado, and the Spinal Cord Recovery Project.
- Keeping worksites safe. Our grants and sponsorships here include the Colorado Safety Association and the Colorado School of Public Health.
- Ensuring that Colorado has a robust business climate and our policyholders have the workforce they need. Here, we fund workforce development projects with groups such as the Associated General Contractors of Colorado, Sedgwick County Economic Development, and the Colorado Advanced Manufacturing Alliance.

Our Pinnacol in Action volunteering program focuses employee energy where they can make the most impact. Last year, nearly 80 percent of Pinnacol employees volunteered with a local nonprofit, contributing 5,321 hours of community service.

In addition to opening their hearts, we encourage Pinnacol employees to open their wallets to support Colorado charities. In 2016, more than 80 percent of our employees donated at total of \$117,000. Along with Pinnacol's match, we shared nearly \$230,000 with more than 250 community organizations.

In 2016 the Pinnacol Foundation provided 109 scholarships totaling almost \$400,000 to the children of workers who were severely injured or killed in a workplace accident. Last year's scholarship brought the Foundation's total to more than \$4 million in scholarships to more than 450 students since 2000, whether or not Pinnacol was the parent's workers' compensation carrier. Many of these are first-generation college students.

Maintaining financial stability

After another solid year, our board made the decision in 2016 to decrease rates and issue a general dividend to our policyholders for the second year in a row. To maintain our financial stability and guarantee the payment of benefits to injured workers and their dependents that may span years or even decades, we manage expenses, carefully steward our financial resources, apply disciplined underwriting practices, and focus on managing risks to our investment portfolio. We are committed to maintaining the funds required to fulfill our commitment to policyholders and injured workers. These efforts have helped us retain an A- (Excellent) rating from insurance rating agency A.M. Best and a BBB+ rating from Standard & Poor's.

In 2016, Pinnacol received a clean audit of its financial statements, as conducted by independent auditors (KPMG) contracted by the Colorado Office of the State Auditor. The full audit report is attached in Appendix B.

Required reporting per C.R.S. §8-45-122 - All data as of Dec. 31, 2016

A. Policy Count: 55,969

Pinnacol's policies-in-force (active) as of Dec. 31, 2016 increased by less than 1 percent over year-end 2015.

B. Total (Admitted) Assets: \$2,632,859,069

Pinnacol's total assets grew by 6.88 percent over year-end 2015. The change was driven primarily by positive net income resulting in an increase in invested assets. Pinnacol's investment portfolio emphasizes high quality, taxable bonds, supplemented by a smaller portfolio of equities, high-yield debt and alternative investments. It is overseen by an investment committee including outside professionals as well as members of Pinnacol's board.

C. Reserves: \$935,713,000

Our reserves represent the financial obligations of Pinnacol to pay injured workers' expected future benefits and related claims expenses, as determined by a contracted third-party actuarial firm (Milliman). Pinnacol's total reserves decreased by less than 1 percent over year-end 2015, primarily due to fewer claims per premium dollar.

D. Surplus: \$1,086,348,605

Our surplus is equity to cover unexpected claims/losses and economic fluctuations, as well as other risks. It is, essentially, our rainy day fund.

Colorado's strong economy helped drive positive net income, which is consistently the biggest driver of surplus growth for Pinnacol, and resulted in a 16.15 percent surplus increase in 2016. Even more significantly, the number of claims decreased in 2016 due to a variety of factors, including improved worksite safety.

E. Claims filed in 2016: 43,965

F. Claims required by statute to be admitted or denied within 20 days and notice provided to the Colorado Division of Workers' Compensation (DOWC): 5,732

Contested claims that are medical-only: 1,360

Contested claims that are indemnity claims: 112

The number of claims Pinnacol admitted or contested (denied) within 20 days decreased by .14 percent in 2016 compared to 2015. The percent of claims we provide notice of to the DOWC has held steady at 12-14 percent of total claims filed for a number of years.

The total number of claims Pinnacol contested (denied) and reported to the DOWC increased in 2016 from 2015 by 4.1 percent. The number of contested indemnity claims was down 10 while the number of contested medical-only claims was up 68. Pinnacol's most common basis for contesting claims in 2015 was due to an injury not being work-related or the need for further investigation.

Here is a more complete picture of key data elements for 2016 with explanations to follow.

1. Claims processed with no filing required with DOWC	= 38,233 (87 percent)
2. Claims admitted within 20 days with DOWC	= 4,260 (9.7 percent)
3. Claims contested (denied) within 20 days with DOWC	= <u>1,472</u> (3.3 percent)
Subtotal of items 2 and 3	= 5,732
Total claims in fiscal year 2015	= 43,965 (100 percent)

Item 1: No Filing Required: Claims that are minor in nature; the injured worker has not sustained a permanent disability, disfigurement, or lost time from work in excess of three calendar days/shifts. These claims are processed by Pinnacol and do not require a filing of admission or contest with the DOWC. These claims represent 87 percent of all claims received by Pinnacol in 2016.

Items 2 and 3: Admitted or Contested within 20 days: Claims that are more complex in nature require a formal filing with the DOWC of “contested” or “admitted.” It should be noted that not all contested claims are ultimately denied; as many may initially be contested based on the need for more information within the 20 day window, the time in which compensability must be determined.

Claims where the injured worker has sustained one of the following require a formal filing of “contested” or “admitted” with the DOWC:

- The injured employee contracted an occupational disease
- The injured employee was found to have a permanent disability due to the injury
- The injury or occupational disease resulted in lost time from work for the injured employee in excess of three shifts or calendar days

As noted above, the number of claims that fall into these two categories has stayed between 12–14 percent of total claims filed for the last few years.

Item 3: Contested Claims:

The 1,472 contested claims (3.3 percent of total claims in 2016) stemmed from one or more of the following reasons:

- Injury or illness was not work-related – 785 (53 percent)
- Pending further investigation or information – 374 (26 percent)
- Other – 313 (21 percent) This category includes such things as no insurance policy or the injured worker is covered by another carrier.

Pinnacol’s percentage of claims contested remained at 3.3 percent in 2016, slightly higher than 2015.

G. Medical procedures denied: 2,743

Pinnacol’s percentage of medical procedures denied compared to total bills received was .42 percent for 2016. This metric has remained relatively stable over the past few years. The most common reason for denying medical procedures that require prior approval from Pinnacol is the procedure was found not to be medically necessary.

Medical procedures denied are in accordance with Rule 16 of the Colorado Division of Workers’ Compensation’s Rules of Procedure. Some medical procedures require prior approval from the insurance company. Once a request for prior authorization is received, Pinnacol has seven business days to inform the medical provider and the injured worker that we will pay or deny payment for the procedure.

H. Amount of total compensation each executive officer or staff member receives, including bonuses or deferred compensation

Title	2016 Total Compensation
President and CEO	\$534,874
Vice President, General Counsel and Corporate Secretary	\$394,719
Vice President, Chief Investment Officer	\$348,912
Vice President, Strategic Development	\$363,646
Senior Vice President, Insurance Operations	\$386,689
Vice President, Chief Information Officer	\$229,319
Chief Financial Officer	\$324,070
Vice President, Agency Relations and Safety Services	\$285,859
Vice President, Human Resources	\$322,817
Vice President, Communications and Public Affairs	\$284,035
Average total compensation for 7 Associate Vice Presidents	\$184,054

- I. Amount spent on commissions: \$77,479,432**
- J. Amount paid to trade associations for marketing fees: \$251,061**
- K. Information related to bonus programs**
See Appendix A
- L. Other information the CEO deems relevant to the report**
See Appendix B

Note: Sources for all items except H and the Appendices are the 2016 Pinnacol Annual Statement, the Pinnacol Assurance Key Factor Report, the General Ledger Account (60511-100 — Advertising Expenses — Association Marketing) and other internal reports.

Appendix A

Information related to bonus programs

Appendix B

Other information the CEO deems relevant to the report:

Annual financial statement audit report

Rule 16 of the Colorado Division of Workers' Compensation
Rules of Procedure