

Workers Compensation Pricing Perspectives: Factors Affecting Workers Compensation Insurance Efficiency and Cost

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Declining claim frequency and moderate per claim cost trends have led to significant rate reductions in every New England state as well as countrywide during the past three years.

Exhibit one (on page 12) compares annual changes in claim frequency with changes in medical and indemnity (wage replacement) costs per claim and changes in average wages for 34 states served by the National Council on Compensation Insurance (NCCI). Together, the decrease in frequency and increase in revenue proportional to wages have outpaced increases in claim costs. However, frequency cannot decrease indefinitely; it will not reach zero. (This exhibit contains data from the NCCI publication: "2018 State of the Line Guide.") Looking forward, attempts should be made to reduce transactional costs and thereby increase the efficiency of the workers compensation system.

Workers compensation insurance is a form of no-fault insurance for employee injury and occupational illness, required in every state except Texas, where it is optional. The key feature of workers compensation insurance is its

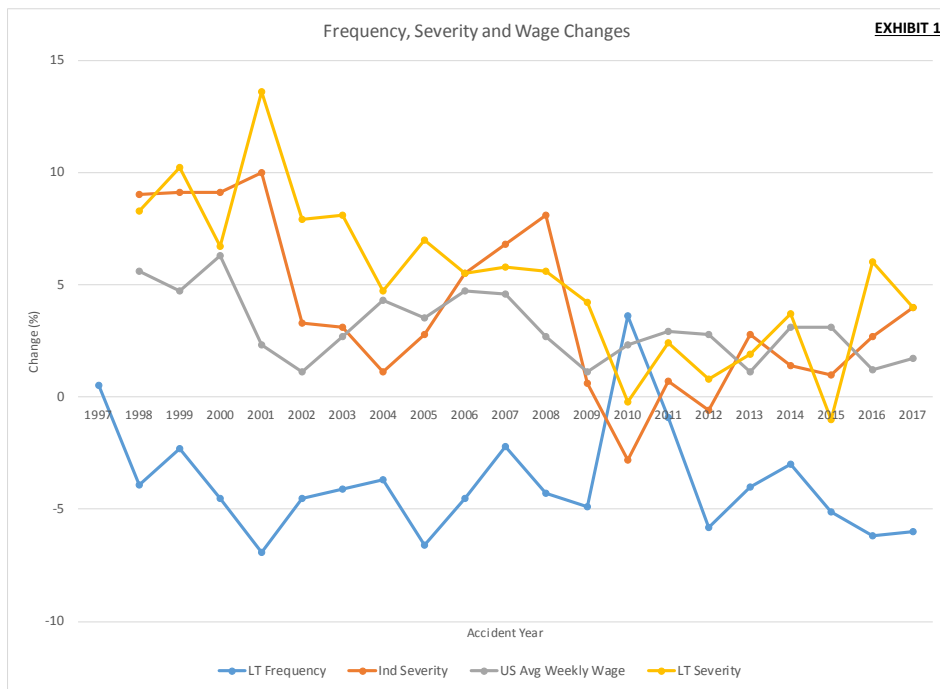
role as sole remedy for employee injury. In exchange for specified medical, wage replacement and survivors' benefits, provided without the need to establish negligence on the employer's part, the employee loses his/her right to sue the employer for negligence allegedly causing injury or occupational illness. Hence the employee cannot try to recover economic or noneconomic (e.g. pain and suffering) damages from the employer beyond those provided by the workers compensation policy.

Workers compensation insurance is a highly regulated form of insurance, where the state government mandates the coverages, benefit schedules and policy language. Workers compensation insurance rates are also regulated, allowing insurers a degree of flexibility within a rating structure established by each state's insurance department. The no-fault nature of this coverage is a key virtue in providing certainty of coverage and promoting efficiency, since resources are not used establishing degrees of negligence among the employer, the injured employee and other employees. However, hearings and attorney involvement are sometimes required to

determine whether an injury or illness is work related, what the degree and duration of disability are and what the scope of treatment should be. The degree of attorney involvement in the system varies by state and is a factor in determining the efficiency and cost of the system.

Exhibit two (bottom of page 12) displays the ratio of defense and cost containment expense (DCCE) to loss for each New England state and countrywide. These expenses include litigation and other cost containment expenses associated with adjusting losses. Note that the ratios for all six New England states are lower than the countrywide average. This suggests that the New England states enjoy above average efficiency in at least some aspects of workers compensation administration, and it is a highly positive feature.

In North Dakota, Ohio, Washington, Wyoming and Puerto Rico, workers compensation insurance can only be purchased from a state-owned monopolistic carrier. In the other 46 states and the District of Columbia, this coverage is available from private carriers. For private carriers, rates can be determined in



Source: NCCI publication: "2018 State of the Line Guide"

one of two ways depending on the state.

In Massachusetts, the Workers' Compensation Rating and Inspection Bureau of Massachusetts (WCRIBMA) files rates for each class (type of business) on behalf of all insurers within the state. Individual insurers must use these rates subject to optional downward deviations (discounts) that they may include in their own company filings.

In the other five New England states, the National Council on Compensation Insurance (NCCI) files loss costs for each class on behalf of all insurers. Loss costs are rates that exclude underwriting expenses, which are built back in by each carrier's filing of loss cost multipliers. Risks above a specified size have experience modification factors, based on their claims history, applied to their rates. These factors are tempered to reflect the fact that loss history for all but the largest risks will contain an element of randomness. In New England states other than Massachusetts, carriers may apply schedule credits or debits to filed rates for specific insureds with documented favorable or unfavorable risk characteristics not fully reflected in their loss experience, to adjust their premium within specified limits to reflect the risk's true loss potential. The underwriting file for each risk documents

the reasons for any schedule debits or credits for review, upon request, by regulators. Hence, we see that among New England states Massachusetts allows the least rating flexibility to reflect individual risk characteristics.

Key factors that affect the comparative cost of workers compensation insurance among states are the efficiency of the system and the generosity of the benefits provided. As noted, greater

procedural costs, such as higher legal fees due to greater attorney involvement can increase costs. Additionally a system that limits unnecessary (and possibly even harmful) treatment, such as unnecessary levels of pain medication, will be more efficient. State mandated provider fee schedules and enforcement of professional standards for providers promote the most efficient and effective care. Wage replacement benefits vary among states.

Among the New England states, Connecticut has the most generous benefits, with a maximum benefit equal to 75% of the statewide average weekly wage, compared to levels of 60% to 67% in the other five New England states. (See Exhibit three on page 14: Summary of Specific Benefit Levels by State.) In an empirical comparison of loss costs for a sample of classes, we found that Massachusetts had the lowest rate level and Connecticut and Vermont the highest among New England states. This is an interesting result, since Connecticut and Massachusetts have similar economic environments, including high average wages. (See Average Weekly Wage by State.) The generous wage replacement benefits in Connecticut contribute to this result.

The socially most beneficial way to limit workers compensation costs is to lim-

EXHIBIT 2

Defense and Cost Containment Expense Provisions from Recent Rate and Loss Cost Filings

State	DCCE/Loss
Connecticut	10.0%
Maine	6.5%
Massachusetts	9.4%
New Hampshire	8.1%
Rhode Island	12.9%
Vermont	7.4%
Countrywide	13.2%

The source of this data for Massachusetts is the most recent rate filing, submitted by the Workers Compensation Rating and Inspection Bureau of Massachusetts (WCRIBMA) on December 22, 2017. The sources for the other states and Countrywide are the most recent NCCI loss cost filings for these states, submitted during 2018.

Summary of Specific Benefit Levels by State

EXHIBIT 3

	MA	CT	ME	NH	RI	VT
Temporary Total Disability (TTD)	60% of AWW - Max 156 weeks	75% of after tax and Social security AWW. No cap on # of weeks.	2/3 rd s of AWW - No durational cap on total disability benefits.	60% of the AWW up to 150% of the SAWW, no limit.	Find AWW & tax filing status in Spendable Wage Table & multiply that by 75%. Also entitled to \$15/per dependent.	2/3 rd s of AWW, can not be more than 90% of AWW.
Temporary Partial Disability (TPD)	60% of the difference between TTD CR and current earning capacity not to exceed 75% of TTD CR. Max 260 weeks. TTD and TPD combination max no to exceed 364 weeks.	75% of the difference between AWW and current earning capacity. No cap.	2/3rds of the difference between AWW and actual or imputed earnings - 520 week durational cap.	60% of the difference between the AWW and gross wages up to 260 weeks	Same as TTD but no dependency benefit - 312 wk max - TTD does not count towards the cap	2/3 of difference between AWW and gross wage for week.
Permanent Partial Disability (PPD)	Permanent loss of function scheduled by chart set by state - Permanent scarring set by state limited to face neck and hands.	Scheduled by state perm loss of function charts. Also scarring which is limited to face, head and neck.	2/3rds of the difference between AWW and actual or imputed earnings - 520 week durational cap with possibility of long term PPD beyond cap if PI is over 18%, EE is working and wages are 65% or less than AWW.	Scheduled body part for PPD set by the state. No scarring.	\$90 Scarring & \$180 LOF - Scarring is discretionary and loss of function is scheduled by chart set by the state. Max for both benefits is 500 weeks combined.	According to AMA Guides, 5th Edition
Permanent Total Disability (PTD)	66.67% of AWW for life, no cap. We can always file to contest ongoing perm total at any time if we obtain appropriate supporting evidence.	75% of after tax and Social security AWW. For life or until no longer consider perm total.	2/3rds of AWW - No durational cap on total disability benefits	60% of the AWW up to 150% of the SAWW, no limit.	TTD rate For life - Classified as "Odd Lot" applies to those who are medically partial, but because of the age, education, & skills are unemployable. Those receiving TTD beyond 312 wks receive COLA after collecting TTD benefits for 52 weeks, and yearly thereafter.	Initial 330 week award paid at 2/3 of AWW, weekly benefits after 330 weeks for life unless evidence shows no longer PTD, COLA each year.
Death	66.67% of AWW for life or until remarriage of surviving spouse. Dependent children also entitled to an equal share until age 18 or no longer a full time student.	75% of after tax and Social security AWW until death or remarriage of surviving spouse.	2/3rds of AWW - 500 weeks or until the spouse becomes a dependent of another person. Benefits for dependent children continue until age 18 or to 23 if child is a full-time student.	60% of the AWW, benefits due spouse unless remarried, benefits to dependents until age 18, can be extended if full time college student.	TTD rate For life for spouse, but do terminate if the spouse remarries. For the children, they terminate when they reach 18 yrs or 23 yrs if they are enrolled FT in an accredited college. They also receive COLA adjustments each year.	21 VSA 632 - percentages depend on spouse, number of children, parents if no spouse or children.
Voc Rehab	Clmt must be found suitable for Voc Rehab by state agency, Office of Education and Vocational Rehabilitation (OEVR).	Yes. This is provided and paid for the Rehabilitation Services branch of the CT Workers Comp Commission.	Claimant can seek an evaluation for voc rehab services and Board can then order voc rehab over employer objection. If EE completes voc rehab over employer objection and finds work, ER must pay 180% of plan cost.	Full time work capacity necessary, Each case is reviewed by the DOL and determined if eligible.	Not required, rarely done, but it is available at Arrigan Center which is a non-profit outpatient rehab facility under the purview of the RI DOL.	After on TTD 90 days must be referred for screening and entitlement assessment.

Average Weekly Wage By State

EXHIBIT 4

State	Average Weekly Wages 2017	Rank
District of Columbia	1,645	1
Massachusetts	1,359	3
Connecticut	1,294	4
New Hampshire	1,074	14
Rhode Island	979	20
Vermont	869	38
Maine	836	44
Mississippi	729	51
United States	1,064	

Source: NCCI 2019 Annual Statistical Bulletin, which cites the U.S. Bureau of Labor Statistics, Quarterly Census of Employment and Wages (www.bls.gov/cew)

it the probability of accidents through the promotion of safe workplaces. Workers compensation insurers make a significant contribution to this effort by providing their insureds with loss control information and services.

In addition, the experience modification factor component of the rating calculation not only promotes equity among insureds, but also provides a significant incentive for insureds to follow safe practices.

Equity in workers compensation pricing also depends on accurate reporting of payroll by insureds. When insureds under report payroll or misclassify workers, inadequate premium is collected by insurers and inadequate payroll reported to the WCIRBMA and NCCI. The result of inadequate reporting is an increase in filed rates and loss costs. Hence, honest and careful insureds end up subsidizing

dishonest or careless insureds. Insurers audit the payroll records of insureds, but if the records are inaccurate, the insurer may not be able to detect and correct the inadequate reported payroll. Employers who do not maintain accurate payroll records may deny society adequate taxes, their employees promised benefits and the workers compensation system funds and accurate information. Priority should be given to encouraging accurate reporting and, when appropriate, prosecuting payroll fraud.

Since workers compensation insurance, like auto liability insurance, is required by law, most states provide a mechanism for businesses that, due to their risk characteristics, find it hard to purchase insurance. Two common mechanisms are competitive state funds and reinsurance pools. Competitive state funds are state-owned insurers that compete with private insurers and provide a market

of last resort for employers who find it difficult to secure coverage from other insurers.

Reinsurance pools are a mechanism that reinsures servicing carriers. Servicing carriers are insurers, which agree to provide coverage to employers that cannot secure coverage from other insurers in exchange for an administrative fee. The underwriting profit or loss is assumed from the servicing carrier by the pool through the reinsurance mechanism. Reinsurance pools are found in a number of states, including Connecticut, Massachusetts, New Hampshire and Vermont. Per the NCCI 2018 “Annual Statistical Bulletin,” the Massachusetts pool contains the highest percentage of workers compensation premium, 22.1% in 2017, of any pool in the country.

In recent years, claim frequency — even after adjusting for a change in class distribution reflecting the continuing shift from industrial to office and service employment — has decreased significantly in New England, as well as country-wide. In the past three years, all six New England states have experienced double-digit rate decreases. At the same time, workers compensation has remained a profitable line of business.

For more than a century, the workers compensation system in the New England states has provided reliable medical, wage replacement and other benefits to injured workers. Through education and the incentive experience modification system, it promotes worker safety. Actions that reduce transactional costs will improve the efficiency of the system. Sanctions on employers that misreport payroll protect workers, responsible employers and the ability of insurers to efficiently provide this vital insurance coverage. ■

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