The California Workers' Compensation Market in 2005
Reform, reorganization, rate reductions and some relief

By Dave Hock, Senior Vice President, ABD Insurance and Financial Services

With almost 8 months of 2005 “in the books” we thought it timely to offer a perspective on the evolving California Workers' Compensation Market and to again remind our clients and others of a simple truth: there is no “quick fix” when it comes to WC cost control. Regardless of market cycle, the legal and regulatory environment or any other variable, employers who develop, implement and sustain strong, effective risk control and claims management strategies will always capture the lowest net cost of workers’ compensation insurance. Success demands taking the long view. Before reviewing just what this entails, though, let’s recap mid-year 2005 market conditions.

CURRENT MARKET CONDITIONS

- A recent announcement by the California Department of Insurance (DOI) estimates that base rates of the state’s 25 largest workers’ compensation insurers have dropped an average of 25.7% since mid-2003 in the wake of reform legislation.

- The Workers’ Compensation Insurance Rating Bureau of California (WCIRB) notes that written premium reported for the first quarter of 2005 is $5.9 billion – 8% less that the first quarter of 2004.

- The WCIRB also reports that the average statewide insurer rate reported for the first quarter of 2005 is $5.21 per $100 of payroll – 18% less that the last six months of 2003.

- After estimating the impact of reform legislation on unpaid losses, the WCIRB further estimates that the ultimate 2004 accident year combined loss and expense ratio will be 64% - a sharp decline from the 1999 peak of 184%.

- The average cost of a 2005 indemnity claim will be approximately $48,000 (again, according to the WCIRB). This is 2% less than the 2003 indemnity claim average but still about 125% greater that the average cost of a 1994 indemnity claim.

- Capacity and competition are both increasing as improving conditions continue to attract new carriers to the market and improve the underwriting appetite of established carriers. There are more players to approach and consider.

- These improving market conditions are driving greater choice and, as noted, competition between the insurance companies for good risks. This has made alternative funding approaches (individual and group self-insurance and traditional group insurance programs) much less attractive options.
The market is going in the right direction, but when all is said and done, current conditions again place a premium on broad market knowledge and reach, having the respect and confidence of multiple underwriters and strategic, aggressive marketing and brokering.

INSIST ON A TOTAL BROKERING SOLUTION

It bears repeating: there is no “quick fix” when it comes to workers’ compensation cost control. This fundamental principal is the foundation of ABD’s consulting strategy and tactics. We offer a total workers’ compensation solution consisting of the people, expertise, relationships and advocacy that true cost control requires. Unfortunately, there’s always someone at the ready to offer the easy answer – something “new” to salve the wounds and save the day.

A tempting notion, but after 30 years in the business I can tell you that we’ve seen it all before. ABD continues to watch closely for any real opportunities to innovate and drive the market on behalf of our clients, but at the moment there just isn’t anything that’s new. Workers’ compensation cost control is all about a disciplined approach to the basics. It’s never been enough to focus on rates and a program’s financial characteristics and structure alone. For example:

- A 15% rate reduction means little if the rates being paid are 50% higher than they might otherwise be due to poor claims experience and an unattractive underwriting profile.

- An “exclusive” single carrier program approach may seem “unique” but eliminates important competitive dynamics (leveraging one carrier against another) and the value of broad market access and skillful brokering.

- Group programs touting “safety in numbers” and special rate reductions often result in quite the opposite: the best performers in any group will actually subsidize the poor performers and could do significantly better in an individual plan.

KEY ELEMENTS OF WORKERS’ COMPENSATION COST CONTROL

So let’s focus on the real answer and review the fundamentals – the basics found in all successful workers’ compensation programs. These are the key elements that ultimately drive rates and premium to the lowest possible level.

Safety and Loss Prevention

The best way to contain workers' compensation claims costs over time is to reduce the frequency and severity of claims. Well-conceived and aggressively managed safety and loss prevention programs not only reduce direct claims expense, they eliminate the indirect, or “hidden” costs of claims. This produces substantial savings over time, since these related expenses (e.g. lost productivity, temporary help, administrative expense) are often multiples of the direct claims costs incurred.

Working with a broker offering a total workers’ compensation solution can make a considerable difference in this area. Over time, most carriers have reduced or even eliminated loss prevention personnel and programs. Where services are available,
relatively inexperienced people are often the rule. What now passes for loss prevention service is frequently little more than a periodic “inspection”, based on underwriting requirements and guidelines.

Over the past 20 years a service evolution has taken place with leading brokers (and their Risk Control Departments) assuming primary responsibility for safety program design, implementation and management. Many of the industry’s most experienced and capable engineers and consultant now work for brokers (ABD, for example, has a group of six). But regardless of where you find the support and resources, it all starts here: you must establish results-oriented, objective-driven programs that identify and address your most frequent and costly claims exposures.

**Initial Claims Investigation and Reporting**

Actions immediately after an injury occurs have a major impact on the ultimate disposition of a claim. The role of supervisors and department managers, therefore, is critical since they are frequently the first to know of claims and have the initial opportunity to investigate, direct and control events. To avoid relinquishing medical control, creating an adversarial employee relations situation, increasing litigation, incurring fines and penalties and failing to preserve necessary evidence, your supervisors must be properly trained in workers’ compensation claims investigation and reporting procedures.

Supervisors also play a key role in preventing future claims and must understand the importance of thoroughly investigating the causes of injuries and taking appropriate corrective action to eliminate any unsafe conditions and acts that produce claims. And it is frequently your supervisors who play a pivotal role in the opportunity for, and success of, modified duty / transitional work programs.

Again, you can’t rely exclusively on your insurance carrier for necessary direction and supervisory training. There is a real difference between aggressive claims management and simple claims processing and, unfortunately, the insurance industry has increasingly moved toward the latter, utilizing “inside adjusters” and relying on outside resources when more than basic claims handling is required.

On the other hand, brokers offering a total workers’ compensation solution have built their own teams of experienced claims and program management consultants who will inform, educate and train their clients' claims management groups. We are particularly proud of the expertise, advocacy and results produced by our own claims consulting teams here at ABD.

**Medical Control / Provider Selection and Management**

Proper selection and management of workers’ compensation medical providers can significantly reduce claims expense. Physicians must understand your operations and human resource philosophy, specialize in occupational medicine and be willing to work closely with your insurer and broker. If initial medical control is not assumed, employees can seek their own care - usually from their family physician. Attempting to manage treatment and the nature and extent of disability with a physician who does not understand the workers’ compensation system can be a challenge, at best. Treatment from an
employee’s personal physician invariably leads to a longer recovery period; increasing indemnity expense and total claims costs.

**Return-to-work / Transitional Duty Programs**

Workers’ compensation is ultimately a disability management system. Programs that focus on managing temporary disability, permanent disability and vocational rehabilitation will have the greatest impact on reducing claims expense.

There are differing approaches to return-to-work programs, based on each employer’s culture, interest and individual needs. They range from simple “modified duty” plans to fully integrated absence management programs using the same practices and protocols to manage all time off work, regardless of the reason (non-industrial illness, occupational injury, etc.). If you don’t have a formal return-to-work program of some kind, I strongly recommend implementing one. ABD has structured a partnership with AtWork Resources, offering our clients a range of tools, resources and consulting support.

**The Right Insurance Broker / Consultant**

Here are some of the key capabilities you should insist on when selecting an insurance broker to design, implement and manage your workers’ compensation program:

- **Broad Market Access** – your broker must have strong relationships with the major national underwriter of workers’ compensation coverage as well as any regional specialty carriers in your market. Bigger is not always better, but a certain amount of market reach and leverage is extremely important. Beware of any approach that involves approaching a single carrier (frequently the case with group programs).

- **Experience and Expertise** – does your broker really understand and can they demonstrated specific expertise in workers’ compensation insurance? Ask for current client references and evaluate whether their programs contain the key cost control elements discussed above. Is the broker close to and respected by the underwriting community and do they know how to best present and position the clients they represent? Keeping the key cost control elements in mind, how would they “sell” your company to an underwriter and why would they recommend this strategy?

- **Resources and Infrastructure** – brokers who have developed workers’ compensation as an area of specialty and strength have built their own teams of Risk Control and Claims Management professionals to support their clients. Identify these people and ask for an opportunity to meet with them personally to assess their qualification. In the right situation, you shouldn’t even have to ask. The best brokers will usually approach you as a team and involve their Claims and Risk Control professionals early in the process.

- **Needs Assessment and Communication** – how much time does a broker spend evaluating and understanding your current program (or lack of one). Do they ask questions related to the key cost control elements or do they simply ask for payroll and loss information and call it a day? What can they tell you about workers’ compensation market trends, emerging areas of risk, cost containment
strategies, etc? Do they regularly communicate on these issues with their clients and, if so, ask to see some examples of how it’s done.

Workers’ Compensation is ultimately an employer’s most controllable insurance expense. But assuming and maintaining this financial control requires knowledge, discipline and attention to the fundamentals. You have to understand and practice the basics – the long-standing, key elements of workers’ compensation cost control. All that “glitters” in the marketplace is definitely not workers’ compensation “gold.”

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