

Depression in the workforce • Coalitions simplify health care • Bare bones plans
Flu shot delays • Aetna's RICO victory • Domestic partner benefits • Politics trumping policy

SEPTEMBER 2000

Business & Health

KEYS TO WORKFORCE PRODUCTIVITY

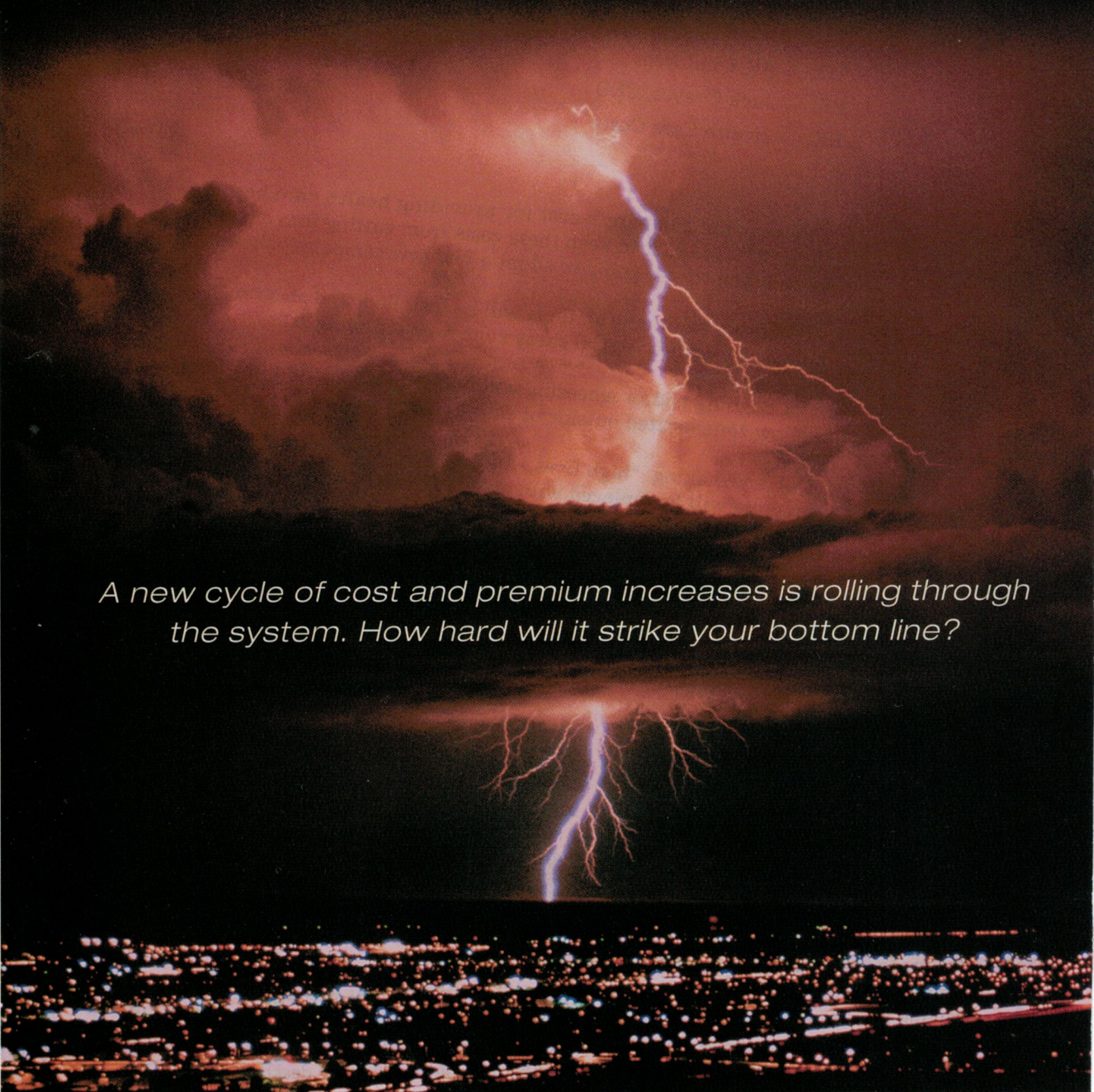
www.businessandhealth.com



**The gathering storm
in workers' comp**

The gathering storm in workers' comp

BY ANNMARIE GEDDES LIPOLD



A new cycle of cost and premium increases is rolling through the system. How hard will it strike your bottom line?

Audrey King was expecting to pay more when she renewed her workers' compensation policy last June. Her company, the Walker Corporation, had been getting a pretty good deal, but she'd heard premiums were going up. "I expected an increase, but not an 86 percent increase," recalls King, human resources manager for the 135-employee metal and fabricated products manufacturer in Ontario, Calif. Thanks to a better-than-average injury record—no lost-time accidents in 1998 and 1999—she was able to procure coverage a bit cheaper from another insurance company. But the premium was still 50 percent higher than what she paid the year before.

Employers around the country are beginning to feel the same pinch of rising premiums and costs after a half decade of relief, but observers of the workers' comp industry are not sure if employers will go through the same degree of financial trauma they experienced during the last crisis. Back in the late 1980s and early 1990s, the mandated state-based social insurance program made headlines for being too costly.

Like other forms of insurance, workers' comp goes through cycles that are felt first by reinsurers and insurers and then by purchasers. Observers agree that premiums and costs are on the rise, but this cycle looks different and the extent of the impact on employers is unclear.

"(Workers' comp is) in crisis, not yet for employers, but certainly for insurance companies, based on the financial numbers," notes Richard W. Palczynski, group senior vice president and chief actuary for The Hartford Financial Services Group Inc. The Hartford, Conn.-based company posted \$13.5 billion in revenues for 1999 and wrote \$1.07 billion in direct workers' comp premiums in 1999.

A key financial indicator points to trouble for the industry, according to Barry Llewellyn, senior divisional executive of regulatory services for The National Council on Compensation Insurance Inc., which collects workers' comp and recommends rates and loss costs in 39 states. The combined ratio, which measures the relationship of premium to loss and administrative expenses, has been growing the past four years. For accident year 1999, the combined ratio is 134.6, according to Boca Raton, Fla.-based NCCI. This means that insurers pay \$1.35 in expenses for every \$1 they collect. NCCI's figures measure lost-time claims, which represent over 90 percent of claim expenses.

Raising premiums

"We are losing so much money that drastic measures have to be taken," warns Kevin Ryan, vice president of

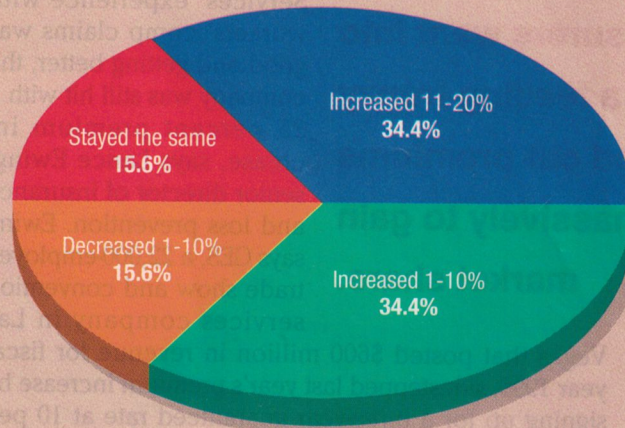
Princeton, N.J.-based Munich American Risk Partners, which reinsures workers' comp for insurance companies and self-insured employers. "We've got to raise prices and review the business we are writing," he adds, "with an eye to not renewing some portions of our business." Munich American is projecting a written premium volume of \$3.5 billion for fiscal year 2000 with approximately \$1.1 billion for workers' compensation. Workers' comp premiums started going up at the beginning of the year, he says, but some employers have not seen it yet because they have not renewed their policies.

The Hartford is increasing premiums about 10 to

Storm clouds

About a third of the workers' compensation insurance companies recently surveyed by Conning & Company raised rates by as much as 20 percent this year. Another third planned smaller increases.

% of insurers whose 2000 rates:



Source: Conning 2000 Workers' Compensation Survey.

15 percent this year for midsize employers, which pay out \$50,000 to \$1 million annually, Palczynski says. Munich American and The Hartford are not alone. In a Conning & Company survey released in August, nearly 35 percent of insurers said they are raising premiums by 11 to 20 percent this year, says Geri Riley, assistant vice president for the Hartford-based insurance research firm.

Base rates, used as the basis for premium, have gone up 3.5 percent in the year 2000, according to

Annmarie Geddes Lipold is a freelance writer based in Arlington, Va., who has spent nearly a decade covering workers' compensation and other human resource issues.

Llewellyn. Riley predicts they will go up another 5 percent in 2001, "and that's probably conservative." She notes that premium and base rate increases are varying drastically across states. While some states, Connecticut for example, have not been hit yet, California employers are seeing premium increases of 20 to 30 percent or more and Texas is getting hit hard.

Houston-based Friedkin Companies Inc., a 3,000-employee distributor for the automotive industry, was confronted by a workers' comp premium increase last March, reports Mary Isbell, the company's director of risk management. "We entered into a three-year agreement because we believe that the market is turning and this is a good time to lock in the rates," she says. The company has a \$250,000 deductible plan and has

Just as losses were coming under control, insurers went into a feeding frenzy and cut premiums massively to gain market share.

not filed a claim with its insurer, says Isbell, and that was good leverage in maintaining the same coverage at the same price.

Although GES Exposition Services' experience with workers' comp claims was good and getting better, the company was still hit with a 25 percent premium increase, says Lance Ewing, senior director of insurance and loss prevention. Ewing says GES, a 22,000-employee trade show and convention services company in Las

Vegas that posted \$600 million in revenue for fiscal year 1999, sidestepped last year's premium increase by signing up for a three-year guaranteed rate at 10 percent less with a new insurer.

Other employers, like Papa John's International Inc., are getting ready for the hardening workers' comp market. "I have heard that I need to be prepared," says Tom Thompson, the company's vice president for risk management. Premiums for the Louisville-based restaurant chain have not gone up for five years, but Thompson is actively scanning the marketplace to be ready for renewals this October. Papa John's has 17,000 employees and posted \$805 million in revenues for fiscal year 1999.

Changing rules

Employers can scramble for better deals, but they are becoming harder and harder to find. "It is going to be more difficult for the insured than the previous (cycle), because there aren't as many alternatives

available anymore," says Ryan of Munich American. There used to be more insurance companies offering workers' comp coverage, he explains, but they have either dropped from the market or been acquired by other carriers.

That's not the only reason why this workers' comp cycle upturn is different than the last one. "In the last workers' compensation crisis, regulators exercised the authority to suppress rates," says Eric J. Oxfeld, president of UWC-Strategic Services on Unemployment & Workers' Compensation. "When the rate needs became impossible to ignore, the magnitude of the necessary increase was enormous, and regulators were put in the politically impossible position," he recalls. Based in Washington, D.C., UWC represents business on workers' compensation and unemployment compensation issues.

But this time around, pricing regulations are more relaxed in many states thanks to major reform measures made in the late 1980s and early 1990s. By the mid-1990s, just as losses were coming under control, insurers went into a competitive "feeding frenzy" and discounted workers' comp insurance prices massively to gain market share, says Richard Hofmann, president of Sigma Consulting Group, a workers' compensation actuarial firm in St. Louis.

NCCI data support Hofmann's assertion. According to the most recent figures available, carriers were charging about 35 percent less in 1998 than in 1993, says NCCI's Llewellyn, explaining that the combined effect of the decline in base rates and discounts made this possible. Palczynski of The Hartford also says employers in the middle market have enjoyed significant price reductions during the past three to four years.

The price competition, however, has put insurers in a difficult place financially. Matters could get much worse if losses, which had stabilized in the mid-1990s, continue to increase, and there are signs that losses are beginning to climb.

Dissecting costs

The average cost per claim has been increasing the past five years, but this has been offset by a declining number of claims per 100 workers, Llewellyn says. So far, claims frequency remains lower than it was in the 1980s, but the extent of the decrease is tapering off, he adds.

For accident year 1998, the average cost per workers' compensation claim was \$21,173 compared to \$18,183 for accident year 1993, according to NCCI, an increase of just over 16 percent. The cost per claim is increasing mostly because medical costs are going up, sources say. "The average cost per claim for medical

Your to-do list for workers' compensation

Employers needn't be caught off-guard by premium and cost increases for workers' comp, but they do need to prepare. Any or all of the following will help you weather a storm.

1. Research and document your company's experience since the last time workers' comp costs began to increase. The last cycle can give you a good indication of what to expect.

2. Find out what strategies were used to contain costs and improve efficiency and re-evaluate them. Establish internal benchmarks, and get comparable benchmarks from other companies.

3. Consider how your company has changed since the last crisis. With less-experienced workers, new jobs and possible changes to the manner of work, your company's risk exposure might have changed. Telecommuting, for example, requires a different loss control strategy, because the employer has little control over the safety of the home workplace and how work there is performed.

4. Make sure your safety program is effective and up-to-date. Safety consultants can be hired or obtained through your insurance company.

5. Coordinate management of workers' comp and nonoccupational disability claims to eliminate duplicate claims and assure employees receive timely assistance.

6. Update your claims reporting systems to reduce administrative costs.

7. Monitor claims performance at least monthly to get an early warning of cost increases.

8. Consider charging workers' comp costs to departments so managers understand that they have a direct impact on the bottom line.

9. Train your managers to know how to respond when an employee sustains a work-related injury. Workers are more likely to return to work promptly when they know their bosses care, so managers should stay in touch with their injured employees. This also reduces the likelihood that routine claims will turn into costly "problem" claims.

10. Treat your employees well. Besides boosting productivity, this is the best way to control workers' comp costs. Satisfied workers are less likely to malingering after job injuries or to file phony claims.

11. Get involved when new legislation and regulations threaten to make workers' comp more expensive.

12. Talk to your insurance company or broker and make sure the insurance arrangement you have is best suited to your company's current needs.

Source: UWC—Strategic Services on Unemployment & Workers' Compensation.

benefits is increasing at a faster rate than over the past five years," notes Hofmann. Indeed, wage replacement increased 12 percent while medical costs rose nearly 22 percent in that period.

Hofmann adds that his company's research indicates the cost of treating an injured worker rose 5 to 8 percent from 1998 to 1999, depending on the state. NCCI estimates that workers' comp medical costs increased 6 to 7 percent in 1998, Llewellyn says. "There are others that think it has gone up more than that," he added.

Self-insured employers are seeing similar trends. For Tricon Global Restaurants, medical costs have increased by 30 to 40 percent in 1999 compared to 1998, reports Chris Mandel, director of global risk management for the parent company of restaurants including Pizza Hut, Taco Bell and KFC. Tricon has 130,000 employees and posted \$7.8 billion in sales for FY 1999. The Louisville-based company's average claim cost has increased by 53 percent since 1996, but medical makes up 50 of that 53 percent, Mandel says.

Insurers confirm the increases. Palczynski says The Hartford paid 10 percent more for hospital bills, 5 percent more for doctors, and 20 to 25 percent more for prescription drugs in 1999 compared to 1998. Medical

costs are increasing partly because the maximum impact of the managed care programs has been reached in comp, says Hofmann of Sigma. Mandel reports that managed care cost Tricon Company more than it saved starting in 1998.

While wage replacement costs are not rising as quickly, they are still a cause of some concern. To Palczynski, The Hartford's 10 to 15 percent premium increase shows a slow turn in the workers' comp insurance market. But loss inflation is the "wild card" that could intensify the inflationary trend. "The issue is how quickly will the market address the financial problems," Palczynski says, adding that "We may very well see a knee-jerk reaction in the marketplace but that is not yet evident." Competitive rating should mean prices will rise more gradually, which will not be as painful for policyholders, says Oxfeld of UWC.

But Ryan of Munich American does not agree. "The pricing has to be increased substantially more than the last crisis," Ryan says, because the last crisis did not see such a deep valley of depressed prices. "The adjustment is going to have to be greater than last time . . . because they have the ability to move prices without getting regulatory approval," he concludes. □