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Exploitation of Workers' Compensation in California

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The commercial insurance industry in California is the source of about 60% of the benefit payments made to injured workers. The state Workers' Compensation Insurance Fund, which functions like a commercial carrier, is the source of another 13% of benefit payments, and self-insured employers pay the remaining 27% of total benefits. For employers who insure, Workers' Compensation premium rates are set by the State Insurance Commissioner. The Commissioner usually sets the rates recommended by an agency funded by the commercial carriers, called the Workers' Compensation Insurance Rating Bureau (WCIRB). The Bureau has requested and received from the Insurance Commissioner six premium rate increases in the last three years, and a seventh rate increase is pending. In contrast, injured workers covered either by insurance policies or by self-insured employers have and no adjustment in their benefit levels for the past four years.

What the commercial insurance carriers have developed over the years, through the WCIRB and the Insurance Commissioner, is a process of Workers' Compensation premium rate setting which allocates about 60% of premium income to administration, employer dividends, profits, and future loss reserves, and leaves only about 40% to pay benefits to injured workers. Whether intentional or not, this allocation process exploits the state's Workers' Compensation system and the state's injured workers. This process is also a primary reason why California's Workers'

Compensation system remains high in costs, low in benefits, and very slow in service to injured workers.

Administrative Costs Average 27.7% of Premiums

WCIRB data presented to the Insurance Commissioner to justify another premium rate increase on January 1 of this year indicates that annual administrative costs of about 300 private Workers' Compensation insurers in California averaged 27.7% of their premium rates (1982-1986). This rate of administrative cost is exorbitant. In comparison, the costs of administering employer-employee health and welfare plans average in the range of 12-16% of annual premium income, on a national basis. The cost of administering Social Security averages 1.5% of that system's contributions. Since the administrative costs of workers' Compensation carriers are covered by frequent increases in premium rates, the carriers obviously have no incentive to hold them down.

Administrative costs of the carriers are only a part of the total administrative cost of Workers' Compensation in California. The state has an essential role in supervising the Workers' Compensation system, particularly in the adjudication of disputes between injured workers and the carriers, who represent the employers in such disputes. The state budget, for example, funds the Workers' Compensation Appeals board, which employs 130 administrative law judges in 22 locations in California. The Appeals Board has had a steadily increasing work load in the past decade, particularly in disputed claims for permanent disabilities and for rehabilitation. However, the Appeals Board has had no comparable increase in staffing or funding in the past decade, while the Insurance Commissioner has allowed the carriers to allocate more than one of every four premium dollars to their administrative representation of the employers. The result is an administrative system heavily weighted against the claims of injured workers, in all but routine cases. A recent staff report of the state's Joint Study Committee on Workers' Compensation found that delays in cases before the Appeals Board were so excessive that the Board, in effect, cannot actually adjudicate, but instead must seek "to prod the parties into settlement whenever possible," to avoid even greater delays in the administrative process. Such delays are devastating to workers, whose primary source of income is cut off because of job-connected injury or illness.

Annual Dividends Returned to Employers Average 17.3% of Premiums

Annual employer dividends as a percent of the premium rates set by the Insurance Commissioner averaged 17.3% (1972-1986). These dividends supposedly reflect both size and experience differences of employers. But critics argue that in practice, the lion's share of dividends goes back to the larger employers or to those who might be inclined to switch carriers, and dividends are not utilized to give employers an incentive to introduce more effective health and safety practices. Any such incentive must also overcome the basic disincentive inherent in the protection from employee lawsuits, which Workers' Compensation gives to employers. Asbestos diseases are a case in point. They were not covered by Workers' Compensation in most states two decades ago. As court settlements became more and more costly to employers and carriers, their opposition to coverage of these diseases by state Workers' Compensation programs disappeared.

Annual Profits of the Carriers Average 10.8% and Annual Returns to the Carriers from Investment Income Average 11%

WCIRB reports both of these returns (1972-1986) on the basis of earned premium, rather than the premium rate set by the Insurance Commissioner. Thus the accounting basis is different than that used for administrative costs and employer dividends. The subtleties of accounting, however, should not obscure the total allocation of approximately 60% of carrier income to administration, employer dividends, profits, and investment returns, leaving only about 40% of such income for benefits.

Carrier investment income is primarily from a huge loss

reserve for claims incurred but not reported; i.e., injury or illness known to have occurred already in the workplace, but not expected to result in a worker's claim until later, possibly many years later. This loss reserve by the end of 1986 totalled \$7.1 billion, which was more than the total of \$5 billion in premiums which the carriers required for their operations in 1986.

Many questions should be raised about the use and the regulation of carrier loss reserves. Neither WCIRB nor the Insurance Commissioner reports what workplace hazards or threats are included in the list of those which require reserves for future claims nor do they report how a hazard is added to the list. We have little information about what standards of accounting and reporting and fiduciary responsibility are required for the handling and investment of these reserve funds. Such standards should at least be equal to those required of pension trustees, who hold and manage the funds set aside to meet future retirement benefits. Such standards should also extend to policies of the carriers and the employers which would control health and safety hazards in the workplace and thus reduce the amounts required for huge reserve funds for future claims.

Conclusion

Workers' Compensation benefits in California are among the lowest in the nation while the costs of California's program are among the highest in the nation. Proposals to improve California's program, however, have been stalemated in the legislature for the past four years. Both labor and the legislature should focus greater attention on inefficiencies in the administration of Workers' Compensation. The insurance carriers clearly play a leading role not only in creating high costs, but also in administrative problems which lead to psychologically frustrating and financially damaging delays in the handling of claims of injured workers.

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