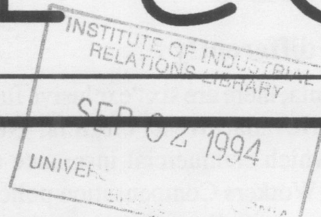


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THE DOMINANCE OF CALIFORNIA WORKERS' COMPENSATION SYSTEM BY COMMERCIAL INSURANCE CARRIERS

by Bruce Poyer

The originators of California's Workers' Compensation system (in the Progressive era of the early 1900s) intended to create a social insurance system. But they permitted employers to insure for Work Comp liabilities by buying policies from commercial insurance companies. Unfortunately, our system over the years has become dominated by these companies, whose economic interests have come to be much better protected than those of injured workers.

Today, some 300 commercial insurance carriers sell Work Comp policies to California employers, covering about 57% of all workers subject to state compensation law. In addition, the State Fund (a public agency offering similar Workers Compensation insurance policies) covers about 23% of such workers. About 20% of workers are covered by large employers who can meet the requirements of self-insurance. Thus, we have at least 350 different "administrators" of California's comp laws, making decisions about workplace accidents and injuries affecting the lives of more than a million workers who present claims each year. The state agencies (Division of Workers' Compensation, and Workers' Compensation Appeals Board) act as referees in trying to settle an incredible number of disputes that begin to arise in the first steps of the claims process. The more carriers we have seeking to improve their profits in the lucrative Workers Compensation market, the more disputes we get.

It is in the rate-making process, however, that the commercial insurance companies achieve real dominance of the state's Workers' Compensation system. Rates that may be charged to employers, by both the commercial companies and the State Fund (covering 80% of all workers subject to compensation law), are subject to final approval by the State Insurance Commissioner (previously Roxane Gillespie, an appointed of-

ficial, now John Garamendi, an elected official). The Commissioner acts on recommendations of the Workers' Compensation Insurance Rating Bureau (WCIRB). This agency is funded and operated by the commercial insurance carriers, and it is the only rating agency recognized under state law. The rates which the Bureau recommends, when approved by the Insurance Commissioner, are the minimum rates that can be charged for Workers Compensation insurance in California. The State Fund must also charge these rates, and cannot compete with the private carriers on rates. (The private carriers, obviously, have lobbied this provision into state law.)

WCIRB has recently recommended a 12.5% increase in all Workers Compensation rates for next year, and Garamendi will soon act on this recommendation. (Commissioners like Gillespie have routinely approved such recommendations in the past.) The Insurance Commissioner can increase rates once or even twice each year. But workers' benefits, which are uniform for everyone covered by state comp law, are set by the legislature, which tends to make important benefit changes only in three to five year intervals. Thus rates inflate, and benefits lag, year after year. The elected Insurance Commissioner may help to change this situation by holding down rate increases. But the legislature will have to do its part by making benefit improvements easier to achieve (by indexing, for ex-

ample). Otherwise, California will always be a high rate/low benefit state, because of an inherent imbalance in its rate making and benefit setting procedures.

We could do it all quite differently . . .

In sharp contrast to California, there are six "exclusive fund" states (Ohio, Washington, Nevada, West Virginia, North Dakota, and Wyoming), in which commercial insurance carriers are not allowed to write Workers Compensation policies. The exclusive state agency covers all workers, sets benefit levels, determines insurance rates, handles all workers' claims, and pays all operating costs from premiums charged to employers. There are no general fund appropriations for Workers Compensation in these six states. Insurance rates in these states are uniformly much lower than in California, while the most important worker benefit levels are uniformly much higher.

I gathered the annual reports of the Workers Compensation programs from the six exclusive fund states, for 1988, and combined their operating data (as if they were one state, with eight million covered workers, compared to 11 million covered in California). Then, I compared their results with 1988 California data reported by WCIRB (the commercial carriers' own source of data). I wanted to measure the difference in "total administrative costs," which I defined to include profits and dividend distributions. That is a broad definition of "administrative costs." None of the six exclusive fund states makes profits or pays dividends, so California's insurance companies do not like to have their operations compared with the exclusive fund states.

Profits and dividends, however, are built into both the financial and the administrative structure of California's Workers' Compensation system, and have become an inherent part of it. They have become, in fact, more important than benefits and services that the system is supposed to make available to injured workers. A comparison which omits profits and dividends would therefore be pointless, in my opinion.

Here are some conclusions from my study:

(1) The weighted average administrative cost of the six exclusive fund states in 1988 was 9.3%. The comparable figure for California was 36.2%. If California had achieved a 9.3% rate in 1988, the savings would have been \$2,169,000,000.

(2) The major elements of higher costs in California in 1988 were:

a. Taxes	\$ 357,250
b. Profits and Return on Surplus	885,980,000
c. Allocation for Dividends	792,000,000
d. Private carriers expense for commissions, loss adjustment, other acquisition costs, and general administrative expense	1,445,606,000

(State Fund expenses in this category were only half of these private carrier expenses)

(3) Compared to the exclusive fund states, California's much higher operating costs (including profits and dividends) clearly do not result in better service to injured workers. The carriers' expenses for "loss adjustment" (which are excessive even compared to the California State Fund) result in endless adversarial hassles for injured workers, who must overcome well-financed carrier efforts to reduce claims expense, and thus increase profits, and return on surplus, and dividends.

(4) The California state agencies (Division of Workers Compensation, and WCAB) were funded with an additional general fund appropriation of \$50 million in 1988. (There were no similar general fund appropriations in the exclusive fund states.) But these agencies are underfunded and understaffed in California, and do not keep up with their workloads, or help to reach timely and just settlements. This increases the economic pressure, especially on more seriously injured workers, the majority of whom are forced to "compromise and release" their claims (i.e., settle for a cash amount essential for immediate self or family survival). We have begun to lose the basic function of WCAB, which should be to reach adjudicated settlements in an administrative process not burdened with the long delays of complex legal procedures.

We should do it all quite differently . . .

With respect to the profits and dividends in California's system, we should raise these basic questions:

First, why should anyone be making any profits or paying any dividends on the basis of injuries and illnesses that occur to workers on the job — especially in a no-fault system that is supposed to be based on social insurance, not commercial insurance, principles?

Second, to what extent do the dividends paid by the commercial insurance carriers go to large employers — including those who may happen to be on the Boards of Directors of the insurance companies? In other words, to what extent are subsidies extracted from small employers for the benefit of large employers in California's system? WCIRB data does not answer this question. Hopefully, we will get more insight when the current Rate-Study Commission reports next year on its study of this and other interesting questions. If not, the elected insurance commissioner should demand more public information to answer this question.

Third, what remains in California's Workers Compensation system of the original concept of social insurance, which is alive and doing well in the six exclusive fund states? I believe that's the most interesting question of all.

It would clearly be possible for California to reduce costs and improve benefits by returning to some of our original social insurance concepts. We have the right precedents to follow, in the exclusive fund states (one, Nevada, being just across our

common border). It will not be possible, however, unless we can eliminate or at least control some prevailing commercial insurance concepts — like the right to make huge profits and distribute huge dividends, and also the right to make political contributions to legislators. These contributions now flow freely from lucrative, state-protected, monopolistic insurance operations, and make change more difficult.

These issues won't disappear; they will be raised again and again. They should, but probably *will not* be raised because of poor service and adversarial pressure put on injured workers, in a system designed by and for the interests of the commercial insurance carriers. But they *will* be raised if only because of

\$2 billion or more that we waste every year, in support of an inefficient commercial insurance system that is simply indifferent to the problems of injured workers. At some point, we will be obliged to notice the lower costs, the higher benefits, and the better service rendered through social insurance in the exclusive fund states.

Copies of Bruce Poyer's study from which he has quoted above are available from the Labor Center, 2521 Channing Way, Berkeley, CA 94720. The price is \$4.50 and the title is Labor Education Review: A Class on Workers' Compensation Insurance in California — Rates and Rate-Setting Procedures.

BOOKS ON CALIFORNIA WORKERS COMPENSATION Available from the Labor Center

Basic Stuff: A Survival Guide

by Dorsey Hamilton

\$ 9.95 / 125 pp.

The first complete book written about California Workers' Compensation without legalese. It is a survival guide not just for the injured worker. All business agents and every shop steward in every union and worker association in California should get a copy and keep it handy for reference.

A Class on Workers' Compensation Insurance in California: Rates and Rate-Setting Procedures

by Bruce Poyer

\$ 4.50 / 32 pp.

This booklet explains how insurance rates are set in California, how California's administrative "expense loading" factor compares to six states with "exclusive" state funds and programs, and how private insurance carriers in the state are guaranteed by law to enormous financial returns.

Workers' Compensation: A Worker's Guide to the California System

by Bruce Poyer

\$ 5.00 / 32 pp.

Published in July 1990, this guide is a plain language description of benefits and administrative changes effective in California in 1990 and 1991 as a result of legislation passed late in 1989. It gives the new benefit levels and outlines the basic rights of injured workers pursuing a Workers' Compensation claim.

To order: Send pre-payment to Labor Center / 2521 Channing Way, Rm 300 / Berkeley, CA 94720. A 20% bulk rate discount is given to orders of 21 or more books per title. The costs include postage and handling. Please make checks payable to "U.C. Regents."

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