



THE BEST INTERESTS OF WASHINGTON'S WORKERS' COMPENSATION SYSTEM

BRIEFLY

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Washington continues to have the nation's highest workers' compensation benefits. These high benefits are accompanied by high costs, which have been driven by structural issues in the system.

Washington's workers' compensation system is unusual among the states. The many elements that set Washington apart from other states combine to make it difficult to compare costs (and they can contribute to the costliness itself). One such element was the prohibition on compromise and release (C&R) agreements, through which the claimant and the insurer or employer agree to a compromise on benefits and there is a release of further liability for the injury. Since reforms were enacted in 2011, Washington has allowed a limited version of such voluntary agreements. (For more, see our report, "[New Reforms to Workers' Compensation](#).") In 2013, the Senate passed bills that would have expanded the option for more workers, but the bills failed to get hearings in the House. (See our report, "[More Reforms for Workers' Compensation](#).")

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Comparing Costs and Benefits

Workers' compensation is a factor in the business climate; high costs make Washington less competitive.

Complicating cost comparisons among states, Washington's system is unusual in several ways:

- It is a monopoly (like only three other states). The Department of Labor and

Industries (L&I) is the insurer and administers the state fund; no private insurers are allowed, but large companies are allowed to self-insure. In Washington 166,000 employers and 2.4 million employees are covered by the state fund, while 360 firms self-insure, covering 867,000 workers (L&I 2013a).

- Washington bases premium rate calculations on hours worked—every other state bases them on payroll. According to [L&I](#), "In Washington, premiums are based on the worker's exposure to risk (hours on the job), which employers and workers agreed to in the 1930s. The system has some advantages for employers and workers: premiums don't automatically go up each year as wages rise and it isn't influenced by whether employers pay higher wages to their workers" (L&I 2010).
- Washington is the only state in which employees are statutorily required to pay a portion of the premiums. Statutorily, employees are responsible for 50 percent of the Medical Aid Fund premiums, 50 percent of Supplemental Pension Fund premiums, and 50 percent of the Stay at Work premiums (but none of the Accident Fund premiums). In 2012, the average statutory employee contribution to the total premium rate was 23 percent. (The actual incidence of the premium is unclear, as we discuss below.)

Unfortunately, there is no good comparison of system costs in each state. The Oregon Department of Consumer and Business Services produces a [premium](#)

Table 1: Premium Rate Rankings in the Oregon Study

	WA	OR
2012	13	39
2010	26	41
2008	38	39
2006	37	42

Note: 1 = the highest premium rate

rate ranking study every two years. While it is considered to be the most comprehensive such study, it is not a good measure of Washington’s workers’ compensation system costs:

- The study is tailored to Oregon’s industry mix. The study incorporates 50 rate classes, selected due to their “importance as measured by share of losses in Oregon” (ODCBS 2013 5). Analysts note, “Because not all premium classes were included in the study, the actual average premium rate for a state will differ from the weighted premium rate index, which is based on the characteristics of Oregon’s economy” (ODCBS 2013 12).
- It does not include the costs of self-insured employers, of which Washington has many more than Oregon. In Washington, about 27 percent of workers are covered by self-insured employers; in Oregon, about 10 percent are.
- Washington’s rates have to be converted from an hourly to a payroll measure. According to the 2012 study, “The Washington payroll data included overtime pay that may overstate the average wage for purposes of premium computation, thus understating the effective average payroll rate” (ODCBS 2013 12).

Table 2: Average Workers’ Compensation Rates (%)

Year	Indicated Rate Increase	Adopted Rate Increase
2014	2.7	2.7
2013	0	0
2012	-0.3	0
2011	17.8	12
2010	19.4	7.6
2009	6.4	3.1
2008	6.1	3.2
2007	-1.3	-2
2006	5.2	0
2005	15.1	3.7
2004	19.4	9.8
2003	40.5	29
2002	26.3	1.8
2001	16.3	-2.2
2000	17.4	0

Nevertheless, the Oregon study is still used by some as a measure of Washington’s costs. In 2008, proponents of Washington’s system could point to the Oregon study as showing that Washington had low costs despite its high benefits. Since then, though, Washington has moved up in the rankings. As the Upjohn Institute writes, “there is an indication that costs in Washington are rising more rapidly than the average state. This is an important issue because of the potential economic development implications of high workers’ compensation costs” (Hollenbeck et al. 2012 113). This has happened even as L&I

kept premium rates artificially low, by adopting rates that were lower than the actuarially-recommended level for many years.

Since Washington’s recent rise in the Oregon study rankings, proponents of Washington’s system have argued that the Oregon study doesn’t account for the employee share of Washington’s premiums and have made back-of-the-envelope calculations purporting to show the actual cost to employers.

This is inappropriate, as it downplays the premium costs of the system as a whole.

First, economists assume that even the statutory employer share of payroll taxes is borne by employees. As the Upjohn Institute notes in discussing Washington’s employee portion, “economists will maintain that workers always share in the costs of workers’ compensation through indirect wage tradeoffs” (Barth et al. 2008 3-9).

Second, the law is not perfectly clear on the employee portion. Employers are required to remit the full premium amount to L&I. They may deduct the statutory employee portion from employee paychecks, but it is not clear how often that occurs. (L&I notes that “some businesses choose not to make employee payroll deductions” (L&I 2013b).) Indeed, the statutory employee portion is likely factored into compensation or included in collective bargaining agreements. See, for example, the 2013–15 collective bargaining agreement between Washington and SEIU Healthcare 775NW:

The home care worker premium share for worker’s compensation insurance shall be paid by the Employer. If applicable laws or rules prevent the Employer from paying the premium share at any time during the life of this Agreement, the Employer shall adjust each step of the wage scale established under Article 9 (Compensation) of this Agreement upward by an amount equivalent to the home care worker premium share for worker’s compensation insurance. (WA 2013 15)

Cost rankings like the Oregon study may use the term “employer costs,” but that is interchangeable with “system costs” because for every other state they are statutorily the same. The anomalies of Washington’s system make it possible for proponents to claim that costs to employers are low, as if that makes the system inexpensive.

Because of the lack of a good cost comparison, we use benefits paid as a proxy. The benefits paid approach requires no data conversions, doesn’t exclude self-insurers, and is not based on a particular industry mix. And, as the National Academy of Social Insurance has written, “several studies . . . demonstrate that the level of statutory benefits is a major determinant of the costs of workers’ compensation in a state” (Sengupta et al. 2012 35).

Cost Drivers

Washington’s workers’ compensation program has the highest benefits in the nation, at \$855.78 per covered worker. Alaska and West Virginia follow, at \$782.99 and \$765.99, respectively. Washington has the third-highest benefits as a percent of covered wages, at 1.72 percent (preceded by West Virginia at 2.01 percent and Montana at 1.78 percent).

Additionally, in Washington, medical as a percent of total benefits paid is the lowest in the country (32.4 percent). This suggests that Washington pays an inordinate amount of benefits in the form of cash (medical benefits account for about half of total benefits nationally). Washington pays the highest cash benefits in the nation (\$578.63 per covered worker) and the 9th highest medical benefits (\$277.15 per covered worker).

Structural issues that set Washington apart from other states have been a significant factor in these high benefits. As the Upjohn Institute wrote in 2008,

In Washington, temporary disability benefits can continue for extended periods of time; but unlike most wage-loss jurisdictions, Washington’s statute

does not place a time limit on such wage (earnings) losses before benefits are terminated, nor are compromise and release agreements allowed” (Barth et al. 2008 3-4).

Also, in Washington (almost singularly among the states),

Even where a work-related injury causes a severe economic hardship, the law requires that only the degree of (medically determined) impairment be considered in the awarding of permanent partial disability benefits. However, the impairment benefit may bear very little relationship to the actual degree of work disability. If it appears evident that the permanent partial disability benefit inadequately compensates for the work disability that the worker has experienced, the system has no flexibility to remedy this. The result of this combination of factors places the worker and the state fund or the self-insured employer in a position where the only possible source of additional compensation is the TPD [total permanent disability] pension. (Barth et al. 2008 xi-xiii)

Further, Upjohn concluded that “Washington has two to four times the TPD incidence of the highest other states” (Barth et al. 2008 6-3 – 6-4). One reason for that is that “in Washington it has not been unusual for claims to remain open and active for more than 10 years before they are resolved with the award of a pension” (Barth et al. 2008 xi). And, “the longer a time-loss claim is open in Washington, the greater the odds that a pension will result” (Barth et al. 2008 2-39).

A voluntary settlement option allows for flexibility in the system, and can thus lower the number of pensions. Forty-four other states allow claims to be closed through compromise and release agreements, thereby allowing both the company and the worker to move on. Washington did not allow such voluntary settlements until 2011. Still, as enacted and implemented, Washington’s settlement option is narrow.

Claims Management. When a workable settlement option is not present, claims can linger open. As Pennsylvania’s Judge David Torrey wrote of a 2002 conversation he had with Judge James W. Sherry of the Board of Industrial Insurance Appeals (BIIA) regarding Washington’s prohibition on compromise and release, “This prohibition, he stated, can make it difficult to resolve cases” (Torrey 2007 227).

In such an environment, efficient claims management is important: “Most persons familiar with workers’ compensation issues recognize the central role that claim management plays in determining the outcome of a claim. . . . If an insurer can shorten the duration of the claim, then the costs are likely to be lower” (Barth et al. 2008 2-38). But, as the Upjohn Institute noted regarding claims management in 2008, “. . . it is clear that Washington claims are slower to develop than in most other states” (Barth et al. 2008 3-24).

The 2008 Upjohn report lists administrative and structural issues at L&I that were barriers to claim closure; some could be alleviated by new claims management pilot projects. L&I recently introduced several projects it developed “to improve outcomes and reduce costs” (L&I 2013c). In all, L&I’s goal is to reduce claims costs by \$35–70 million (L&I 2013d). They include safety initiatives and projects to help injured workers return to work, to improve claims processes, to improve medical care, and to make it easier to work with L&I. Some of these are:

- Claims Processor Pilot: Processors were brought in to three units to relieve “claim managers of day-to-day administrative tasks, allowing them to spend time adjudicating claims” (L&I 2013c). The processors have saved so much time that L&I plans to fully implement this project. The governor’s proposed 2014 supplemental budget includes funding for seven claims processors, and L&I plans to use existing funds to add 20 more.
- Knowledge Management System: This is a technical package that will “give

claims staff modern search capability and improved electronic access to resources . . . freeing up time to assist customers and reducing overall costs” (L&I 2013c). It is just getting underway.

- First 100 Days of a Claim: “L&I mapped the first 100 days of a time-loss claim to identify where it can eliminate unnecessary tasks and reduce delays for workers and employers” (L&I 2013c).
- Stay at Work: The goal of this program is to keep injured workers “active and connected to the workforce, reducing time-loss costs” (L&I 2013c). It is funded by employer premiums.
- Job Assistance Service Pilots: One of these is attempting to predict early indicators of not returning to work so as to get workers specialized services when needed.
- Medical Management Project: The 2013–15 budget provided funding to increase the ratio of occupational nurse consultants to claim managers. The idea is to be better able to identify clinical problems earlier. (According to the budget, L&I must report on the impact of this pilot by December 2014.)

In addition to the administrative barriers listed by the Upjohn report, another was that “Claims in Washington State never close absolutely” (Barth et al. 2008 2-6).

Voluntary Settlements. In 2011, the Legislature enacted EHB 2123, which allows voluntary claim resolution structured settlements for workers 55 or older. (The age floor drops to 53 on Jan. 1, 2015 and to 50 on Jan. 1, 2016.) Under the bill, Washington workers can only receive periodic payments that total 25 to 150 percent of the average monthly wage (\$4,299.58 in 2013), but the first payment may be up to six times the average monthly wage. Medical benefits cannot be settled, and all agreements must be approved by the BIIA.

While this is an improvement on the sta-

tus quo ante, it is very limited. Based on a review of the laws of the states that allow compromise and release settlements, Washington appears to be the only state that limits them to workers of a certain age and the only state that doesn't allow the settlements to be in the form of a lump sum.

Additionally, the review process has turned out to be problematic. The bill specifies that if a worker is not represented by an attorney, an industrial appeals judge must conference with the parties involved to review the agreement. According to the bill, "Before approving the agreement, the industrial appeals judge shall ensure the worker has an adequate understanding of the agreement and its consequences to the worker." Further, "the industrial appeals judge may approve a claim resolution structured settlement agreement only if the judge finds that the agreement is in the best interest of the worker." After the conference, if the judge decides to allow the agreement, it is submitted to the BIIA.

The BIIA must approve the agreement unless it has not been entered into "knowingly and willingly," it "does not meet the requirements of a claim resolution structured settlement agreement," it "is the result of a material misrepresentation of law or fact," it "is the result of harassment or coercion," or it "is unreasonable as a matter of law." Later the bill notes that if a worker is represented by an attorney, there is no need for the conference and the agreement must be submitted directly to the BIIA.

In practice, the BIIA believes it is bound to determine whether every agreement is "in the best interest of the worker" whether or not the worker has an attorney. This has resulted in numerous rejections:

The BIIA has rejected 11 self-insured and 5 State Fund proposed settlement agreements involving represented workers, based, at least in part, on the agreement not containing sufficient information to prove that the agreement was in the best interest of the worker. (L&I 2013e)

The practice is being litigated in the Zimmerman case. In that case, the BIIA rejected an agreement, saying, "we believe we must evaluate whether the agreement is in the best interest of the worker" (Zimmerman). This was reversed by the Superior Court, and the case is now at the Court of Appeals.

Since implementing the program in Jan. 2012, 800 applications for settlements have been received and 51 state fund agreements approved. Nineteen self-insured agreements have been approved by the BIIA. L&I estimates that total savings from the program are \$100 million (L&I 2013e). Most of these settlements are of time-loss claims, some of which could have become permanent partial disability awards or TPD pensions in the future.

In 2013, additional reforms were passed by the state Senate (but not the House). [ESSB 5127](#) would have reduced the age at which a worker could agree to a structured settlement to 40. It also would have specified that if a worker has attorney representation, a determination of the best interest of the worker is not one of the requirements of a structured settlement agreement, so the BIIA would not be able to reject one on those grounds. The Senate also passed the much broader [ESSB 5128](#), which would have allowed all workers the option of a voluntary settlement agreement which could include lump sums.

Settlements Bring Closure

As noted above, Washington's workers' compensation system is a monopoly. Because L&I is the insurer and the administrator of the system, the need of the insurer to close claims and the desire of the administrator to provide social insurance are at odds. This has manifested in the debate over voluntary settlements. A 2013 [paper](#) from the Minnesota Department of Labor & Industry lays out the problem:

The arguments for and against the use of settlements are based on two contrasting philosophical views. The first approach posits that workers' compen-

sation systems are a form of social insurance and the state government's role is to look out for the best interests of injured workers. In this view, society as a whole has an interest in seeing that injured workers are properly compensated so that they and their families do not require relief from other government benefit programs and that workers are provided with support to return to work.

The second approach considers workers and employers to be free agents who have the right to determine the outcome of the workers' compensation claims process. In this view, workers' compensation is an insurance program that provides benefits in exchange for the exclusion of common law defenses, such as contributory negligence. An injured worker, with adequate information about the claim, the available benefits and their circumstances, and who is not coerced, is in the best position to decide whether to settle the claim. (Zaidman et al. 2013 4)

Indeed, "To date, no empirical evidence exists that workers routinely dissipate C&R lump sums and turn to charity or the state" (Torrey 2007 438). There also isn't much information on how workers use lump sum settlements. In 1961, economist Earl Cheit looked at workers who had agreed to compromise and release settlements and found that

They generally used the settlement money to pay debts or meet living expenses (38 percent), for home improvements or mortgage payments (6 percent), or to start a business, buy income property or invest (14 percent). However, Cheit observed that when the worker was (1) offered a choice, (2) chose the C&R voluntarily, and (3) had a plan for use of the settlement, the plan was usually successful. (Hunt and Barth 2010 10-11)

Of Torrey's cases over a few years, "The vast majority of workers would not admit to any plan to utilize the lump sum on retraining or opening a business." There were exceptions; e.g., to start a business selling tools; to help pay tuition; to re-

train as a home inspector; to purchase property and become a landlord; to buy and manage storage units (Torrey 2007 430-1). However, "a sizeable group of claimants, many of whom were quite vocal, stated that their motive was relief from the claims adjustment process and/or the stress of litigation. . . . The majority of claimants expressed their reason for settling in a simple fashion: 'to get on with my life'" (Torrey 2007 431-2).

That last is termed the closure effect. In 2010, economist Henry Hyatt found that, contrary to the idea that lump-sum settlements discourage work,

California Workers' Compensation claimants who settle their claim through Compromise and Release, an irreversible lump-sum settlement, clearly have an immediate increase in labor force participation. I have demonstrated this phenomenon in a descriptive analysis, and, in summary, the short-term effect of receiving a lump-sum payment is a 5% increase in the quarterly labor force re-entry rate and an 8% decline in the quarterly labor force exit rate. . . .

In order to provide some theoretical context in which to interpret this surprising result, I documented the small psychological literature on the subject of "closure," and I maintain that the emotional state of the claimants may be key to understanding their labor supply. Once a claim is settled, the injured worker may experience what is commonly called "closure," which could lead to an easier resumption of one life's major activities, finding, or maintaining, employment. (Hyatt 2010 16-17)

Further, in 2012, a Workers Compensation Research Institute paper found a "7 percentage point increase in average employment after a lump-sum settlement. . . . This evidence in Michigan reveals the greater importance of the closure effect that workers may experience—closing out a claim helps workers restart their careers which may have been stopped due to a disabling injury" (Savych 2012 8).

Washington's current system is firmly in the social insurance camp, but it has made some movement toward allowing workers more freedom to decide what works for them. Workers have already made positive use of the limited settlements. As L&I reported, settlements have

empowered a worker to receive dental care he otherwise could not have afforded; assisted a worker to relocate and retire in his extended family's small, rural hometown; allowed a worker to avoid the cost and uncertainty of litigation and acquire the peace of mind of predictable, adequate income. (L&I 2012)

Comment

The 2011 reforms that allowed structured settlements were philosophically significant, but practically narrow. The Legislature should build on this step and broaden the availability of settlements so that workers may have more choices.

Settlements can bring workers closure and reduce long-duration time-loss claims, which are costly and—given that they often lead to pensions—contribute to Washington's costliness compared with other states. More effective claims management can also help reduce costs, and L&I has shown good initiative there. Allowing more settlements and continuing to improve claims processes can reduce the high costs of Washington's workers' compensation system and provide better outcomes for injured workers.

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