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## BRIEFLY

*Washington's workers' compensation monopoly approaches insolvency, even as premium costs continue to escalate. At the same time, the system pays among the nation's highest benefits.*

*This year lawmakers have an opportunity to adopt reforms that will restore balance to the system. Proposed measures are generally consistent with previous Research Council recommendations.*

## THE TIME HAS COME TO FIX WORKERS' COMPENSATION

Recognizing that the workers' compensation system is in need of reform, Governor Chris Gregoire recommended a number of changes as part of her "Transforming Washington's Budget" effort.

Some of her proposals have moved forward in the legislature. The medical provider network and expanded Centers for Occupational Health and Education reforms have been passed by both houses and await the governor's signature. Additionally, last week a compromise was struck that enabled the Senate passage of ESB 5566. That bill would allow the choice of voluntary settlements for all injured workers, and it would provide wage subsidies to employers who provide light duty or transitional work to injured employees (return-to-work). Further, studies on the effectiveness of both the voluntary settlement and return-to-work provisions would be required, along with a study of occupational disease in the workers' compensation system.

The reforms in the compromise bill are generally consistent with recommendations made in previous Washington Research Council reports.

### High Benefits, High Costs

A 2010 study by the National Academy of Social Insurance found that Washington paid \$778.36 in benefits per covered worker in 2008. This was the nation's second highest benefit level. Moreover, benefits per covered worker increased 11 percent over 2007. Total benefits paid increased 9.9 percent (to \$2.2 billion). For comparison, total benefits paid in Oregon increased 2.6 percent and in all states went up 4.5 percent from 2007 to 2008.

Washington ranks third in the nation in benefits paid as a percent of covered wages (1.69 percent in 2008, behind only West Virginia and Montana). Benefit costs here are rising at a faster rate than in other states. Total workers' compensation benefits paid in Washington grew from \$1.3 billion in 1998 to \$2.2 billion in 2008. That's an increase of 70.4 percent, compared to 34.2 percent growth for all states.

These high and increasing benefits contribute to high employer costs in Washington. Every two years, the Oregon Department of Consumer and Business Services publishes a study comparing workers' compensation premium rates, state by state. The study notes that, because of the need to convert Washington's data from an hourly rate to a payroll rate measure, the comparison is not exact. (Washington is the only state that calculates premium rates in dollars per payroll hour. Every other state quotes rates as a percent of payroll.) The study weights the industry sample to replicate Oregon's own industrial mix, which—among other differences—includes a much smaller number of employers that self-insure.

Supporters of the workers' compensation status quo have often cited the Oregon report to support their contention that Washington provides high benefits at low cost. Putting aside questions about the accuracy of the study in Washington's case, the most recent edition shows that Washington's premiums are jumping up the rankings. In 2010, Washington ranked 26th in the country, meaning that its premiums were higher than 25 other states and the District of Columbia (Oregon ranked 41st, or 11th lowest in the country). In the 2008 report, Washington's premiums looked much better, at 38th in the nation (Oregon ranked 39th).

**Artificially Low Premium Rates**

The significant deterioration in 2010 of our position relative to other states, as estimated by the Oregon study, comes even as the Department of Labor and Industries (L&I) artificially holds premium rates below the actuarially-recommended level. To the extent the state ever did offer a "high-benefit, low-cost" model, which we have previously disputed, the answer can in part be found in the below-cost premiums imposed by L&I. In fact, a December 2010 audit showed that the Accident Account is insolvent, and there is a 94.1 percent chance that the Medical Aid Account will be insolvent within five years. Nonetheless, L&I proposed premium rates that the actuarial firm contracted by the state auditor found to be inadequate—but that were still a significant increase for business.

In 2011, L&I increased premium rates by 12 percent. If this 2011 increase were included in the Oregon study's 2010 rankings, Washington would rank 16th. The picture is even worse when using the actuarially-recommended premiums. We estimate, based on the December 2010 audit, L&I would have needed to increase rates by 22 percent to break even. With that rate increase, the Oregon report would show Washington as having the ninth highest costs in the nation.

In FY2010, the Accident Account's contingency reserve fell below zero (negative \$358 million). According to the December 2010 audit, this was due to the economic recession, the fact that loss and loss adjustment expense liabilities increased (to which "the growing duration of time loss claims and frequency of pension awards has contributed"), and the fact that "for the past three years premium rates have been insufficient to fund the system." L&I is required by law (RCW 51.16.035) to make premium rates "the lowest necessary to *maintain actuarial solvency* of the accident and medical aid funds in accordance with recognized insurance principles." (Emphasis added.)

Rate Change Comparison

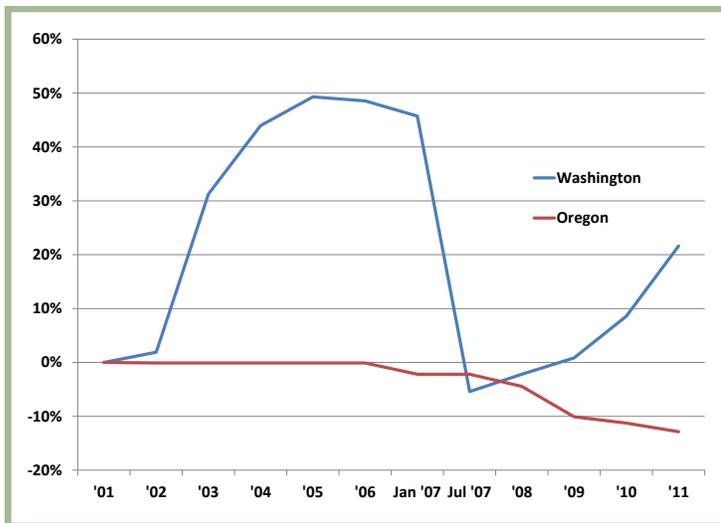
<b>Accident Account</b>		
	Actuary's Best Estimate of the Break-even Rate Change	L&I's Adopted Rate Change
2011	34.8%	29.8%
2010	33.0%	4.5%
<b>Medical Aid Account</b>		
	Actuary's Best Estimate of the Break-even Rate Change	L&I's Adopted Rate Change
2011	11.8%	-10.3%
2010	24.5%	8.4%

Although L&I has not increased rates to the actuary's recommended level, the rate changes' cumulative impact trends up (in 2007, stock market returns were used to subsidize premiums). Oregon, on the other hand, has steadily decreased its rates.

As presently operated, the Washington workers' compensation system has become insolvent and unsustainable. In order to balance the books without employment-depressing premium increases, significant changes will be required.

**Pensions and Voluntary Settlements**

First, workers' compensation pension costs must be brought under control. As Gov. Gregoire noted, "one of every 19 time-loss claims becomes a lifetime pension—a rate that has doubled in the past 10 years. And lifetime pension



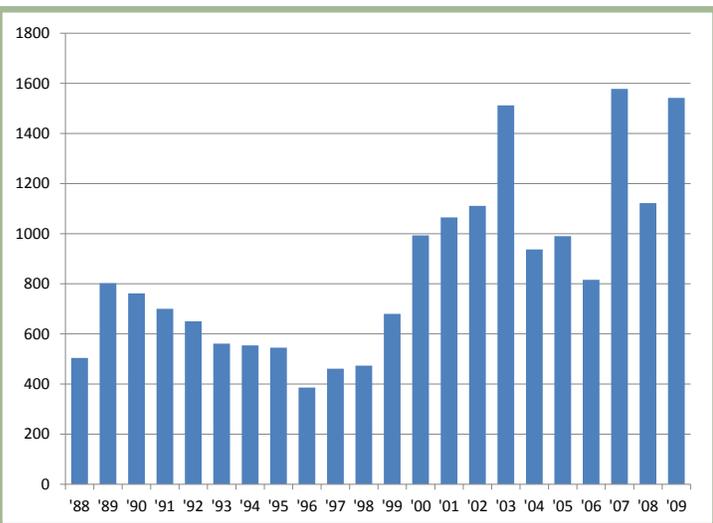
Cumulative Rate Changes, from 2001

claims comprise half of all workers compensation costs.” L&I awarded 1,542 total permanent disability (TPD) pensions in FY2009, compared with 13 pensions awarded by Oregon in CY2009. In 2008, the Upjohn Institute found that Washington has “two to four times the TPD incidence of the highest other states.”

Voluntary settlement agreements simply make good public policy sense. Washington is one of only six states that do not permit such settlements for cash benefits in order to close claims. (The other states are Delaware, Nevada, New Mexico, Texas and Wyoming). Voluntary settlements between the claimant and the insurer or employer generally include a lump sum payment (or structured settlement) and involve a release from further liability. Allowing these final settlement agreements would save costs and bring Washington into the mainstream nationally. It would give workers

and employers the option of a claims closure approach; give financial certainty to both workers and employers; allow for equitable settlements that can be cost-effectively assured by oversight, review, and approval by an appeals board judge; reduce legal costs and simplify administration; and reduce litigation, long-term claims costs, and the need for future rate increases.

Oregon reformed its workers’ compensation program in 1990. The reforms included allowing voluntary settlements. The number of TPD awards fell 95 percent from 1988 to 1998, and the number of voluntary settlements went



TPD Pensions Awarded by State Fund

from zero to about 3,000 annually. The Workers Compensation Research Institute, according to the Upjohn Institute, studied the reforms and found that “the share of lost-time claims that received PPD or lump-sum payments dropped from 44 percent in 1989 to 38 percent in 1991, and with less litigation, attorney costs were reduced as well.”

The bill passed by the Senate would allow this option for all workers. Under the bill, settlements would have to be approved by the board of industrial insurance appeals and there would be a mandatory 30 day waiting period before an agreement becomes binding. If a worker is not represented by an attorney, a settlement officer would ensure that the worker understands the consequences of the settlement, and the settlement officer “may approve a settlement agreement only if the officer finds that the settlement is in the best interest of the worker.” A claim closed through a voluntary settlement

could be reopened, for medical treatment only, if the related medical conditions worsen.

**Occupational Disease**

SB 5566 would also require an independent study of “the nature, incidence, and cost of occupational disease claims in the Washington workers’ compensation system.” The study would, among other things, consider the definition of occupational disease and the statute of limitation for filing claims. The study needs to lead to concrete recommendations.

This is important because Washington’s occupational disease definition is vague when compared to other states. For example, Virginia sets out specific circumstances under which a disease arises out of employment and excludes common illnesses.

As we outlined in a policy brief last year (Mainstreaming Workers' Compensation: Reforms for 2010), lack of clarity increases costs. Direct costs rise because the current state definition allows for diseases to be covered that may not necessarily be directly caused by workplace exposure. Indirect costs are high because administrative costs and time and legal fees are higher when more clarification is required over which situations should be covered.

Also, currently, the statute of limitations for filing an occupational disease claim is set at two years following the date the worker had written notice from a doctor that he has an occupational disease. In application, this means two years from the date that the worker knew or should have known about the disease. Effectively, the time period is wide open because it can take years for an occupational disease to manifest.

### **Medical Provider Networks**

Business and labor groups endorsed the governor's plan to institute a medical provider network in Washington, and it has passed both houses in a separate bill (SB 5801). The bill would establish a health care provider network to treat injured workers, and the providers would have to meet minimum standards established by L&I. Additionally, the Centers for Occupational Health and Education would be expanded, to provide access to all injured workers by December 2015. Designed by L&I and the Workers' Compensation Advisory Committee, these centers promote best practices and prevention, with the goals of expanding occupational health care expertise, improving health care delivery, and providing better outcomes for injured workers.

Such networks, common nationally, have demonstrated success in controlling costs and improving patient outcomes. The Workers' Compensation Research Institute (WCRI) found in 2001 that "medical networks are generally associated with much lower medical costs: 16 to 46 percent lower if the injured worker is treated by network providers and up to 11 percent lower if the worker is treated predominately, but not exclusively by network providers."

### **Discussion**

In all, the reforms currently before the legislature would go a long way in reducing the costs of the workers' compensation system. The system has serious funding problems, yet increasing burdens on business by continually raising premium rates is not a sustainable solution. Instead, costs need to be controlled; reforms like these would help.

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## Resources

- Governor's Policy Brief: Strengthening Washington's Economy and Creating Jobs. January 2011. [http://www.governor.wa.gov/priorities/budget/creating\\_sustaining\\_jobs.pdf](http://www.governor.wa.gov/priorities/budget/creating_sustaining_jobs.pdf)
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- Oregon Department of Consumer and Business Services. 2010 Report on the Oregon Workers' Compensation System. December 2010. [http://www4.cbs.state.or.us/ex/imd/reports/rpt/index.cfm?fuseaction=version\\_view&version\\_tk=184782&ProgID=FEARA006](http://www4.cbs.state.or.us/ex/imd/reports/rpt/index.cfm?fuseaction=version_view&version_tk=184782&ProgID=FEARA006)
- Washington State Auditor's Office. Worker's Compensation Program, July 1, 2009 through June 30, 2010. December 2010. <http://www.sao.wa.gov/auditreports/auditreportfiles/ar1004886.pdf>
- Upjohn Institute. Washington Pension System Review. November 2008. <http://www.upjohninst.org/publications/tr/tr08-025.pdf>
- Washington Research Council. Mainstreaming Workers' Compensation: Reforms for 2010. January 2010. <http://www.researchcouncil.org/docs/PDF/WRCBusinessClimate/MainstreamingWorkersComp2010.pdf>
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