



POLICY BRIEF

Reforming Washington's Workers' Compensation System

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I. Introduction

The phrase "workers' compensation insurance" often elicits vacant stares if not wrinkled brows and frowns from those who hear it. This complex and important social program, which replaces employer liability for workplace injuries with a public system of financial support to sick and injured workers, is often confusing and tedious for employers, workers, citizens and policymakers alike. In addition, workers' compensation programs are, by their very nature, fraught with negative emotions: workers interact with them only when they have had the worst of luck and been injured on the job, and policymakers are presented with the unenviable task of striking a cost/benefit balance that is palatable to the employers who fund the system and the workers who are its beneficiaries. Rarely does either side register much satisfaction.

While it can be tempting to dismiss the insurance program as one that only business owners need worry about, such a reaction is imprudent. Increasing insurance costs have been linked to large-scale job losses, layoffs and wage cuts, and poor compensation systems have a harmful effect on the economic vitality and business climate of a region. Any citizen who is concerned with the overall economic well-being of Washington state should regard workers’ compensation insurance as a topic of prime importance.

II. The burden of rising rates and inefficient systems

Although workers’ compensation has received much attention in “crisis” states such as Florida and California, it has only recently become a topic of significance in Washington. This

is partially a result of the recent sharp rate increases adopted after many years of stable or even declining rates. The Department of Labor and Industries, the state government agency which runs the workers' compensation program, adopted a 29.4% rate increase in 2003, a 9.8% increase in 2004, and will likely impose a third consecutive increase in 2005.¹ Annual inflation for these years is around 2%. Since each year's rate increase compounds previous ones, the average employer's costs in 2004 are 42% higher than his 2002 costs. This is a heavy increase for employers to shoulder in a weak economy and when health care and liability insurance costs are rising rapidly.

Employers, industry groups and workers have all raised concerns surrounding the increasing rates and the efficacy of the current program. Some employers, for instance, feel they are losing ever increasing amounts of business to "black-market" employers who operate without workers' compensation insurance. Although illegal, failing to purchase insurance allows an employer to significantly cut his operational costs and offer customers lower prices than his law-abiding competitors. Employers also point out that they cannot hire new workers when the combined costs of salaries and insurance is too much to bear, and they are worried about being forced out of the state to operate in more competitive business environments such as Idaho or the South. Industry groups have spoken out strongly against the state's administration of the program, insisting that it be reformed for greater efficiency before any further rate increases are imposed. Even workers have wondered whether the increasing percentage of their paychecks that goes to fund the program is being spent wisely.²

III. The burden affects almost all employers

With very few exceptions, workers' compensation insurance is a mandatory purchase for every business in the state. While a few large, cash-rich companies may qualify for self-insurance, all others must purchase insurance from an external source. And since Washington is one of only five states that forbids private insurers from underwriting policies, most employers are forced to purchase insurance from the sole provider: the Department of Labor and Industries. The Department is therefore in both the government regulatory business (it oversees the safety of workplaces, among other things) and the insurance business. The Department of Labor and Industries is the third largest agency in state government, with more than 2,600 full-time staff and an annual budget of almost half a billion dollars.³ Since the Department is the sole insurer for all businesses, the insurance program it administers is also extremely large: the program

¹ "L&I adopts 9.8 percent rate increase for 2004; state workers' compensation premiums still among lowest in country," Washington Department of Labor and Industries news release, December 1, 2003, at www.lni.wa.gov/news/2003.

² Washington is the only state which requires workers to pay a portion of premiums. Worker paycheck deductions account for about 23% of total premium dollars collected. Anecdotal evidence suggests that many employers do not pass on any costs to employees, simply paying the full premiums themselves.

³ "All Budgeted Funds - Employment, FTE Staff Years by Function, Activity, and Agency," 2003 Budget Summary, Table 19, Office of Financial Management, at www.ofm.wa.gov/budget03/summary/table19.htm, and "2003 - 2005 Proposed Budget: Agency Detail, Department of Labor and Industries," Office of Financial Management, at www.ofm.wa.gov/budget03/detail/default.htm.

provides insurance to over 160,000 employers, covers roughly 1.9 million workers, and collected about \$1.2 billion in premiums in 2003.⁴

The cost of purchasing the mandatory compensation insurance is a serious concern for many businesses. A recent survey by the Washington chapter of the National Federation of Independent Business (conducted before the 2004 rate increase was announced), found that worker's compensation costs were one of the top three "most serious problems" for small business owners, trailing only the cost and availability of liability and health insurance.⁵

Worker's compensation insurance costs were identified by these business owners as being significantly more problematic than Business and Occupation taxes, environmental regulations, unemployment insurance taxes, transportation for moving goods and services and hiring quality employees.⁶

IV. An overview of workers' compensation systems

One of the problems in assessing the adequacy of a particular workers' compensation program is the lack of agreement on what a "good" system looks like. In fact, debates over how an "ideal" compensation insurance system should be constituted have existed since the inception of such programs at the beginning of the 20th century. Rarely do all sides agree on even the most fundamental components of a system, such as the "right" level of cost and benefits. However, assessment of five main criteria – cost affordability, benefit adequacy, system efficiency and efficacy, customer satisfaction, and injury prevention – give some indication of how a system performs and compares to others of similar nature.

1. The History and Role of "No-Fault" Workers' Compensation Programs

Each state has its own laws and regulations regarding the administration of its workers' compensation program. Despite the many differences, all state programs share a fundamental feature – they are "no-fault," meaning that workers are financially compensated and employers are protected from lawsuits regardless of who is at fault for an injury or illness. This is also known as the "exclusive remedy" provision: workers are statutorily guaranteed compensation as a remedy, but are supposed to be unable to seek additional indemnity benefits through lawsuits brought against their employers.⁷

⁴ "About L&I Today: Regionally Delivered Customer Service," Department of Labor and Industries, at www.lni.wa.gov/IPUB/101-041-01-000.htm, and "L&I adopts 29 percent rate increase; proposes reforms to the workers' comp system," Department of Labor and Industries news release, Nov 27, 2002, at www.lni.wa.gov/news/2002/pr021127b.htm.

⁵ "NFIB/Washington 2003 Member Ballot Results," *Small Business News and Issues*, National Federation of Independent Business, Washington state, February 20, 2003, at www.nfib.com/cgi-bin/NFIB.dll/jsp/issues/state.

⁶ *ibid.*

⁷ Many states, including Washington, do allow workers to file suit for additional benefits if the employer had a "deliberate intention" to produce an injury or illness (Revised Code of Washington 51.24.020). Washington's Supreme Court has interpreted this phrase to mean "the employer had actual knowledge that an injury was certain to occur and willfully disregarded that knowledge," see ruling in *Birkliid v. Boeing*, 1995.

The “no-fault” provision was created during the social reform period of the early 20th century. Organized labor groups began pushing for mandates, and workplace injuries received much attention since they could be financially devastating for workers who faced two types of costs: medical bills and lost wages. Employers at the time had no legal obligation to compensate workers for either of these monetary losses, and so a worker’s only recourse in the event of an injury was to sue his employer for negligence – an expensive, time-consuming effort that usually resulted in a favorable ruling for the employer.⁸

This does not mean the situation was rosy for employers, though. Although lawsuits were often decided in their favor, the outcome could not be guaranteed, and employers found negligent by the courts were directed to recompense workers. Thus, employers existed in a constant state of risk and uncertainty, subject to unpredictable and potentially significant payouts to workers who were successful in court.

A key intent of workers’ compensation systems, then, was to reduce risk and dissatisfaction for both parties, and many states moved quickly to adopt relevant laws. Wisconsin was the first state to adopt such laws in 1911, and by 1949 all states had enacted similar legislation.⁹ Washington was among the leaders in this movement, adopting its workers’ compensation laws beginning in 1911.

2. States use one of three different insurance models

Workers’ Compensation Insurance (also called “Industrial Insurance” in Washington state) uses the same basic model as other insurance industries. In this model people or companies exposed to similar types of risk band together to spread the risk and resulting exposure costs across the group as a whole. A well-known example is the auto insurance industry, in which all drivers pay a premium to insure themselves against the potentially much larger costs that an accident might produce.

Workers’ compensation insurance in Washington operates the same way. Employers are required to pay a premium to insure their workers against the costs of on-the-job injuries and illnesses. The state uses the collected sums to cover the medical costs and lost wages of the small number of workers who sustain an injury in any given year. As a result, the cost of worker injuries is spread throughout the system, and no one company or worker should be financially devastated by a single accident. All states except Texas require employers to provide workers’ compensation insurance for their employees.¹⁰

⁸ “Workers Compensation,” *Hot Topics & Insurance Issues*, Insurance Information Institute, July 2003, at www.iii.org/media/hottopics/insurance/workerscomp.

⁹ “Workers’ Compensation: Benefits, Costs and Safety under Alternative Insurance Arrangements,” by Terry Thomason, Timothy P. Schmidle and John F. Burton Jr., W.E. Upjohn Institute for Employment Research, 2001. States, rather than the federal government, wrote the laws since the Supreme Court’s interpretation of the U.S. Constitution at the time precluded federal legislation from covering private-sector workers.

¹⁰ “Type of Law and Insurance Requirements for Private Employment,” Benefit Tables, Table 1, U.S. Department of Labor, January 2003, available at www.workerscompresources.com.

Each state has its own specific set of laws and manages its own workers' compensation system.¹¹ States employ different insurance models, and three distinct types exist in the United States: a fully private model, a fully public model, and a "hybrid" model in which private insurers and a publicly-run program operate in the same state.

The fully private and hybrid public/private models are by far the most common. Forty-five states use one of the two, meaning that employers in these states have many insurers from which to choose. Twenty-six of these 45 states have totally private systems in which insurance companies compete against each other for the business of employers. The remaining nineteen of the forty-five use the "hybrid", or "three-way" system, in which the state operates a program (often called a "competitive state fund") that competes with the private insurers in the state. Both models result in a large number of choices for employers. Oregon, for instance, has authorized more than 430 insurance providers, and more than 200 of them underwrote policies in 2001.¹² Washington's other neighbor, Idaho, has more than 200 active workers' compensation insurance providers.¹³

The remaining five states, including Washington, use the totally public model. This model renders private insurance illegal and forces employers to purchase insurance from a state-run monopoly fund.

The table on the next page shows the type of workers' compensation model used in each state, based on United States Department of Labor information as of January 1, 2003.

¹¹ Also, the U.S. Department of Labor operates four specific workers' compensation programs that pertain to workers in select industries. These federally administered programs are: The Energy Employees Occupational Illness Compensation Program, the Federal Employees' Compensation Program, the Longshore and Harbor Workers' Compensation Program, and the Black Lung Benefits Program. See the U.S. Department of Labor Workers' Compensation website at www.dol.gov/dol/topic/workcomp/index.htm.

¹² "Workers' Compensation Premium Report, 2001," Research and Analysis section, Oregon Department of Consumer and Business Services, April 2003.

¹³ "A Guide for Employers," Idaho Industrial Commission, revised June 20, 2002, at www2.state.id.us/iic/guide_for_employers.htm, and "How to Buy Insurance," Oregon Workers' Compensation Division, December 2003, at www.cbs.state.or.us/external/wcd/communications/howto.htm.

Workers' Compensation Systems by State

| State | Coverage Required? | Private Carriers Allowed? | State Fund Available? | Self-Insurance Allowed for: | |
|---------------|--------------------|---------------------------|-----------------------|-----------------------------|--------|
| | | | | Individuals | Groups |
| Alabama | Yes | Yes | No | Yes | Yes |
| Alaska | Yes | Yes | No | Yes | No |
| Arizona | Yes | Yes | Yes | Yes | Yes |
| Arkansas | Yes | Yes | No | Yes | Yes |
| California | Yes | Yes | Yes | Yes | No |
| Colorado | Yes | Yes | Yes | Yes | Yes |
| Connecticut | Yes | Yes | No | Yes | Yes |
| Delaware | Yes | Yes | No | Yes | No |
| Florida | Yes | Yes | No | Yes | Yes |
| Georgia | Yes | Yes | No | Yes | Yes |
| Hawaii | Yes | Yes | Yes | Yes | Yes |
| Idaho | Yes | Yes | Yes | Yes | No |
| Illinois | Yes | Yes | No | Yes | Yes |
| Indiana | Yes | Yes | No | Yes | No |
| Iowa | Yes | Yes | No | Yes | Yes |
| Kansas | Yes | Yes | No | Yes | Yes |
| Kentucky | Yes | Yes | Yes | Yes | Yes |
| Louisiana | Yes | Yes | Yes | Yes | Yes |
| Maine | Yes | Yes | No | Yes | Yes |
| Maryland | Yes | Yes | Yes | Yes | Yes |
| Massachusetts | Yes | Yes | No | Yes | Yes |
| Michigan | Yes | Yes | Yes | Yes | Yes |
| Minnesota | Yes | Yes | Yes | Yes | Yes |
| Mississippi | Yes | Yes | No | Yes | Yes |
| Missouri | Yes | Yes | Yes | Yes | Yes |
| Montana | Yes | Yes | Yes | Yes | Yes |
| Nebraska | Yes | Yes | No | Yes | No |
| Nevada | Yes | Yes | No | Yes | Yes |
| N. Hampshire | Yes | Yes | No | Yes | Yes |
| New Jersey | No | Yes | No | Yes | No |
| New Mexico | Yes | Yes | Yes | Yes | Yes |
| New York | Yes | Yes | Yes | Yes | Yes |
| N. Carolina | Yes | Yes | No | Yes | Yes |
| N. Dakota | | No | Yes (Monopoly) | No | No |
| Ohio | Yes | No | Yes (Monopoly) | Yes | No |
| Oklahoma | Yes | Yes | Yes | Yes | Yes |
| Oregon | Yes | Yes | Yes | Yes | Yes |
| Pennsylvania | Yes | Yes | Yes | Yes | Yes |
| Rhode Island | Yes | Yes | Yes | Yes | Yes |
| S. Carolina | Yes | Yes | No | Yes | Yes |
| S. Dakota | Yes | Yes | No | Yes | Yes |
| Tennessee | Yes | Yes | No | Yes | Yes |
| Texas | No | Yes | Yes | Yes | No |
| Utah | Yes | Yes | Yes | Yes | No |
| Vermont | Yes | Yes | No | Yes | No |
| Virginia | Yes | Yes | No | Yes | Yes |
| Washington | Yes | No | Yes (Monopoly) | Yes | No |
| W. Virginia | Yes | No | Yes (Monopoly) | Yes | No |
| Wisconsin | Yes | Yes | No | Yes | No |
| Wyoming | Yes | No | Yes (Monopoly) | No | No |

3. Current research does not conclusively point to a “best” model

Before embarking on an in-depth analysis of the Washington state system, it is worth noting that current research does not yield conclusive answers as to which of the three insurance models most consistently achieves all defined objectives. Few researchers have focused on creating equitable comparisons between states, and fewer still have attempted to do so for states using different insurance models. In what is probably the most academic and thorough research study spanning all 50 states, three national experts in workers’ compensation, Terry Thomason, Timothy Schmidle and John Burton, Jr., noted that a recurrent theme of their study was that programs are complex and achieving the defined objectives is inherently “counter-productive: achieving one objective often interferes with reaching one or more of the remaining goals.”¹⁴ This is especially true for the interplay of cost and benefits, for instance, because any increase in benefits must be supported and paid for by a proportional increase in costs to employers and workers.

Furthermore, the authors of that study concluded that it is “likely that no empirical study will ever surmount all of these problems and completely dispose of the issue once and for all.”¹⁵ Policymakers must therefore carefully examine the system in place in their own states and encourage reforms that contain costs, promote choice for employers and improve service for injured workers.

4. Self-insurance only allowed for government and large companies

Many states, including Washington, allow qualified employers to opt out of the traditional risk-sharing programs. These companies are referred to as “self-insurers,” and they pay injured employees the legally-required workers’ compensation benefits directly from their own financial resources. These employers bear, therefore, the full risk and cost of injuries occurring in their workplaces.

In Washington only about 400 employers, out of more than 200,000, are able to qualify for self-insurance.¹⁶ Although about 30% of the workforce in Washington (some 800,000 workers) is covered by a self-insurance plan instead of the state’s risk-sharing plan, this figure is misleading since it includes federal and local public workers whose employers take advantage of special provisions not available to private-sector employers.¹⁷ All non-public employers in Washington wishing to self-insure must first apply to and be approved by the Department of Labor and Industries. This is no small undertaking. Generally, employers must fulfill five main requirements to be considered eligible for self-insurance. They must:¹⁸

¹⁴ “Workers’ Compensation: Benefits, Costs and Safety under Alternative Insurance Arrangements,” by Terry Thomason, Timothy P. Schmidle, and John F. Burton Jr., W.E. Upjohn Institute for Employment Research, 2001.

¹⁵ Ibid.

¹⁶ “The Why of L&I,” by Myke Folger, *The Everett Business Journal*, February 2003, at www.businessjournal.org/ejb/articles/0302/the_why_of_li.htm.

¹⁷ “L&I proposes 19.4 percent workers’ compensation rate increase in 2004, bringing premiums in line with benefits,” Washington Department of Labor and Industries news release, September 3, 2003, at www.lni.wa.gov/news.2003/pr030903a.htm.

¹⁸ The requirements are provided under Revised Code of Washington 51.14.020.

- Convince the assigned Labor and Industries representative that they have sufficient liquid assets to pay injured workers statutorily-guaranteed benefits.¹⁹
- Have a net worth of \$5,000,000 or more.
- Demonstrate the existence of a safety program with a proven record of accident prevention.
- Establish a qualified administrative organization to manage all industrial insurance matters and ensure an adequate claims management process.
- Be able to provide three years of historical financial data.

Self-insurance is clearly not a practical option for most employers. Dave Kaplan, executive director of the Washington Self Insurers Association, has said that self-insurance really doesn't become a viable option for businesses until they pay \$150,000 a year in premiums, far more than most small businesses owe.²⁰ As the state acknowledges, self-insurance is a program for only "the largest, most financially secure companies in the state and governmental entities."²¹

Thirty-five states allow employers to take advantage of the self-insurance option by allowing small enterprises to self-insure as a group. Washington is not one of them. In Washington group self-insurance is so limited as to be of no practical use for businesses. Only a few governmental entities, such as hospital districts, school districts, and educational districts, are allowed to form self-insurance groups.²² It is particularly ironic that the Department defends the existing restrictive system for private employers while supporting special exceptions which allow government organizations to opt out of the program.

5. Who is covered

Almost all workers in Washington state, from clerical workers and bank executives to baristas and retail salespeople, are covered by industrial insurance laws through either the state fund or a self-insurance program.²³ Overall, it is estimated that 90 to 97 percent of the American workforce is covered by a workers' compensation program.²⁴ In Washington and most other states, people who "employ" others temporarily for services such as house cleaning, garden work, appliance repair and newspaper delivery are not required to provide compensation insurance for the workers they hire.²⁵ But almost every other type of worker who sustains an injury or occupational illness "in the course of employment"²⁶ is covered and eligible to receive

¹⁹ The Labor and Industries representative may also require the employer to deposit a minimum of \$100,000 in an escrow account to cover worker's compensation costs. The amount deposited must also be at least equal to the employer's annual expected costs of worker's compensation claims.

²⁰ "The Why of L&I," by Myke Folger, *The Everett Business Journal*, February 2003.

²¹ "Employers' Guide to Industrial Insurance," Washington Department of Labor and Industries, January 2003, at www.lni.wa.gov/IPUB/101-002-000.pdf.

²² Revised Code of Washington 51.14.150 (2)(a).

²³ As mentioned, a few select job types are covered by one of four federal programs rather than a state program.

²⁴ "Workers' Compensation," in *Industry Issues*, American Insurance Association, Washington, D.C., 2003, at www.aiadc.org/IndustryIssues/?Nav=1.33, and "Workers Compensation," *Hot Topics and Insurance Issues*, Insurance Information Institute, March 2004, at www.iii.org/media/hottopics/insurance/workerscomp.

²⁵ Revised Code of Washington 51.12.020.

²⁶ Revised Code of Washington 51.08.013.

benefits.²⁷ Moreover, the injury or illness need not be solely the result of work, since job-related aggravation of a pre-existing condition is compensable in Washington.²⁸

In fact, Washington has more inclusive coverage laws than many other states, which often exempt key groups to help reduce business costs to employers. Fourteen states, for instance, exempt employers with fewer than 3 or 5 employees from purchasing insurance, and more than half have some special exemptions for agricultural workers. Washington does not have any numerical exemptions and the only agricultural exemption is for dependents under age 21 who live and work on a family farm.²⁹

6. Types of benefits provided under workers' compensation programs

The benefits provided to injured workers are laid out in each state's law and fall into two main categories:

- 1) Payment of all medical care and rehabilitation fees;³⁰
- 2) Disability or "time-loss" compensation (includes death or "fatal" compensation).

Medical care and rehabilitation benefits pay the fees assessed by medical service providers for treating a worker and returning him to full health. Generally, workers' compensation programs cover all costs that result from treating injuries, including hospital costs, surgical costs and pharmaceutical expenses. Rehabilitation benefits are not allowed in all cases. In Washington, the Department of Labor and Industries determines which claimants should receive rehabilitation services. The second type of benefit, disability compensation, is a cash benefit paid to workers who lose their wages for more than three days as a result of injury. The benefit levels for this type of compensation are set by each state government, and, as a result, vary widely.

Disability compensation is classified according to the severity and duration of the injury. There are three main categories: total temporary disability (TTD), permanent partial disability (PPD), and total permanent disability (TPD, also called a "pension benefit"). A fourth type of benefit called fatal or "death" compensation is paid to the dependents of a worker killed on the job. TTD benefits are the most common, although PPD benefits account for the greatest share of benefit costs. TPD and fatal compensation cases are not very common.

²⁷ Mental health conditions arising from stress on the job are specifically excluded from the "occupational disease" definition in Revised Code of Washington 51.08.142.

²⁸ "Workers' Compensation System Performance Audit," Appendix B, Washington Joint Legislative Audit and Review Committee, December 1998.

²⁹ "Coverage of Agricultural Workers," State Workers' Compensation Laws, Table 3, U.S. Department of Labor, January 1, 2003, at www.dol.gov/esa/regs/statutes/owcp/stwclaw/tables-htm. The exemption is the result of a lawsuit.

³⁰ Forty-four states, including Washington, place no limits on this benefit. The remaining six have some special provisions. See the U.S. Department of Labor's "State Workers' Compensation Laws Benefit Tables," Table 5, published by the Office of Workers' Compensation Programs.

The duration of benefit payments is quite standard throughout the country. Washington pays Total Disability benefits, both permanent and temporary, for the duration of the disability. About 30 other states have the same policy. Approximately 20 states apply some sort of time limit, generally ranging from 100 to 500 weeks, on the receipt of benefits.

The amount of benefits paid, on the other hand, varies greatly depending on the state. Benefits are usually a percentage of a worker's pre-injury wages. Washington uses this system for TTD and PTD benefits, but the state's PPD benefits are lump sum payments that correspond to the type and severity of a particular injury. Complete loss of hearing in both ears, for example, is compensated with a single \$43,200 payment and the amputation of a little finger is compensated with a \$2,430 payment.³¹ Although Washington's PPD calculations differ in method from other states, the overall level of Washington's PPD benefits appears to be relatively in line with those in the rest of the country.

V. Benefits under the Washington workers' compensation system

1. Generosity of benefits in Washington state

As mentioned, benefits fall into two main categories: medical and time-loss. Since medical costs are generally fully covered in all states, the question of generosity pertains mainly to the time-loss portion of benefit payments that have been established by state legislatures.

Time-loss benefits differ markedly among states, and by several measures. Washington has one of the most generous programs in the nation. A 1998 audit commissioned by the Joint Legislative Audit and Review Committee (JLARC) – a bipartisan committee composed of senators and representatives – found that benefits received by Washington claimants were “substantially above the average.”³² Workers in other jurisdictions received an average of \$10,988 per claim, but workers in Washington received on average 21% more at \$13,109 per claim.³³

Moreover, the gap between the level of benefits in Washington and other states is growing. The following chart illustrates the high growth rate of Washington's cash benefits compared to that of other states. Washington's benefits surpassed the nationwide 75% percentile mark during the late 1980s and have remained there since. The “sawtooth” pattern (see chart) reflects legislative enactments that have steadily raised PPD benefit levels.³⁴

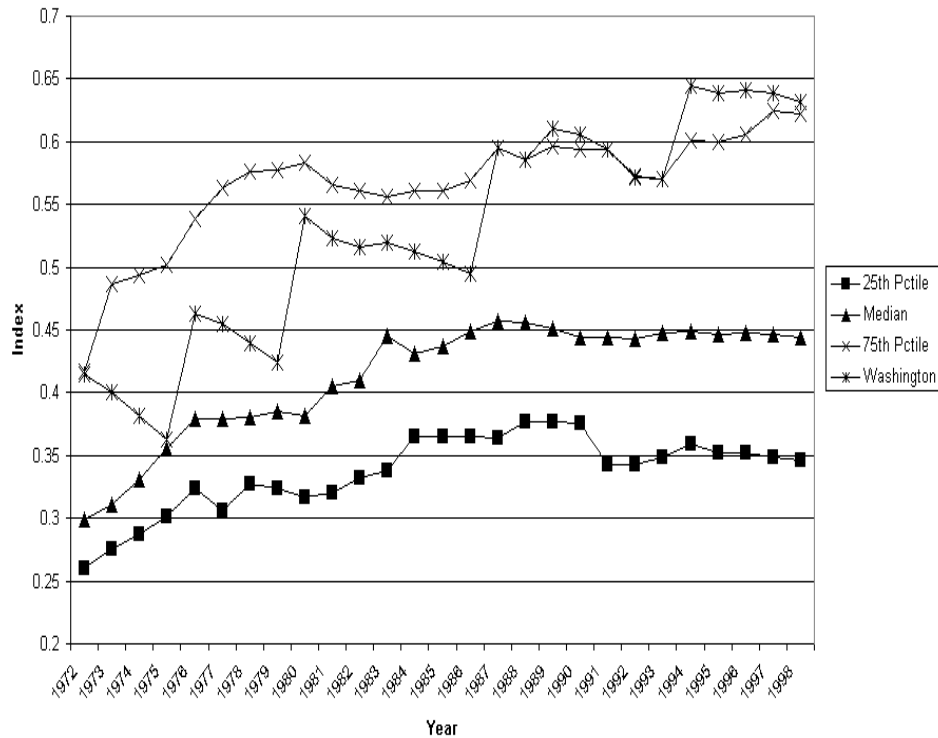
³¹ Revised Code of Washington 51.32.080.

³² “Workers’ Compensation System Performance Audit,” Washington Joint Legislative Audit and Review Committee, December 1998.

³³ Ibid, Appendix C.

³⁴ Ibid.

Total Benefits in Washington Compared to Other U.S. Jurisdictions



Source: "Workers' Compensation Benefits in Washington and the Nation," T. Thomason and J. Burton.

Permanent and temporary total disability payments are calculated as a percentage of a worker's pre-injury wages. The reasons for this are two-fold. First, replacing wages in full would add extraordinary cost to the system. Sustainable workers' compensation systems must keep rates affordable, a standard generally taken to mean that costs are not so high as to bring about "serious adverse consequences such as loss of jobs."³⁵ Second, common sense indicates that reduced pay provides workers with an incentive to participate actively in their own recovery and re-enter the workforce without unnecessary delays. Replacing wages at 100% of pre-injury levels would almost certainly cause the number and average length of claims to rise sharply: under such a system, workers would receive the same amount of money whether they worked or not. Also, workers' compensation benefits are not subject to federal income, Social Security or Medicare taxes.³⁶

Time-loss benefits paid to injured workers in Washington range from 60% to 75% of the worker's pre-injury wages, depending on the worker's marital status and number of dependent

³⁵ Thomason et al.

³⁶ See Internal Revenue Service publication 525.

children. This calculation of benefits is unique and very complex. Every other state simply uses a flat replacement rate, generally 66 2/3%, that applies to all workers, regardless of family status.

Washington’s workers’ compensation system replaces injured lost wages in the following percentages:

Wage Replacement Rates in Washington

| <i>Worker Status</i> ³⁷ | <i>Wage Replacement Rate, PTD & TTD benefits</i> |
|------------------------------------|--|
| Single, no children | 60% |
| Married, no children | 65% |
| Married, 1 child | 67% |
| Married, 2 children | 69% |
| Married, 3 children | 71% |
| Married, 4 children | 73% |
| Married, 5+ children | 75% |

As the table illustrates, replacement rates in Washington often exceed the 66 2/3% flat rate used in other states.

Benefits are also capped to ensure that workers with higher than average salaries do not receive more in benefits than most people in the state receive in wages. Most states set maximum benefits equal to 100% of the average weekly wage for the state. Washington, however, allows benefits to run as high as 122% of the state’s average wage as a result of cap increases adopted in the mid-1990s.³⁸

The following table shows: 1) how each state’s maximum benefit level compares to the average worker’s wage, and 2) the dollar amount of maximum weekly time-loss benefits receivable in each state.

³⁷ Workers who are unmarried but have children are compensated at a 5% lower rate than their married counterparts, Revised Code of Washington 51.32.060.

³⁸ “Workers comp benefits increase 5.25% July 1,” Department of Labor and Industries press release, June 18, 1997, at www.lni.wa.gov/news/1997/pr970618a.asp.

Average Weekly Wage and Maximum Benefit Percentages by State

| State | 1999 State Avg. Weekly Wage | TTD Maximum | PTD Maximum | Death Maximum |
|-------------------------|-----------------------------|-------------|-------------|---------------|
| Alabama | \$558 | 102% | 102% | 102% |
| Alaska | \$676 | 130% | 130% | 130% |
| Arizona | \$627 | 60% | 60% | 59% |
| Arkansas | \$506 | 87% | 87% | 87% |
| California | \$792 | 76% | 76% | 76% |
| Colorado | \$715 | 92% | 90% | 90% |
| Connecticut | \$875 | 104% | 104% | 104% |
| Delaware | \$703 | 70% | 70% | 70% |
| District of Columbia | \$1,019 | 100% | 100% | 100% |
| Florida | \$588 | 103% | 103% | 103% |
| Georgia | \$658 | 61% | 61% | 61% |
| Hawaii | \$589 | 98% | 98% | 98% |
| Idaho | \$533 | 89% | 89% | 59% |
| Illinois | \$732 | 136% | 136% | 136% |
| Indiana | \$596 | 99% | 99% | 99% |
| Iowa | \$537 | 205% | 205% | 205% |
| Kansas | \$565 | 76% | 76% | 76% |
| Kentucky | \$554 | 103% | 103% | 52% |
| Louisiana | \$536 | 78% | 78% | 78% |
| Maine | \$532 | 92% | 92% | 92% |
| Maryland | \$700 | 103% | 103% | 103% |
| Massachusetts | \$852 | 104% | 104% | 104% |
| Michigan | \$712 | 92% | 92% | 92% |
| Minnesota | \$682 | 110% | 110% | 110% |
| Montana | \$467 | 101% | 101% | 101% |
| Nebraska | \$533 | 102% | 102% | 102% |
| Nevada | \$621 | 94% | 94% | 94% |
| New Hampshire | \$668 | 152% | 152% | 152% |
| New Jersey | \$840 | 76% | 76% | 76% |
| New Mexico | \$529 | 102% | 102% | 102% |
| New York | \$872 | 46% | 46% | 46% |
| N. Carolina | \$597 | 113% | 113% | 113% |
| N. Dakota | \$475 | 113% | 113% | 113% |
| Ohio | \$625 | 103% | 103% | 103% |
| Oklahoma | \$519 | 102% | 102% | 102% |
| Oregon | \$594 | 146% | 110% | 146% |
| Pennsylvania | \$654 | 103% | 103% | 103% |
| Rhode Island | \$627 | 112% | 112% | 112% |
| S. Carolina | \$542 | 104% | 104% | 104% |
| S. Dakota | \$477 | 101% | 101% | 101% |
| Tennessee | \$588 | 102% | 102% | 102% |
| Texas | \$672 | 80% | 80% | 80% |
| Utah | \$562 | 100% | 85% | 85% |
| Vermont | \$556 | 156% | 156% | 156% |
| Virginia | \$676 | 101% | 101% | 101% |
| Washington | \$713 | 122% | 122% | 122% |
| West Virginia | \$517 | 102% | 102% | 102% |
| Wisconsin | \$590 | 113% | 113% | 113% |
| Wyoming | \$516 | 102% | 71% | 71% |
| National Average | \$648 | 106% | 104% | 103% |

Source: "State workers' compensation laws in effect on January 1, 2002 compared with the 19 essential recommendations of the national commission on state workmen's compensation laws," U.S. Department of Labor Standards Employment Administration, Office of Workers' Compensation Programs, Division of Planning, Policies and Standards, Branch of Planning, Policy and Review, data as of January 1, 2003.

Washington's use of a high allowable percentage means injured workers receive more money per week here than they would in all but five or six other states. In 1999, the cap yielded a maximum weekly time-loss payout of \$870 a week, or more than \$45,000 a year, in comparison to the national average of \$688 a week. Certainly, a portion of this difference is attributable to the higher-than-average cost of living in Washington as suggested by the average weekly wages in the table above. But were Washington simply to reinstate a 100% cap to be more in line with other states, the system would save approximately \$157 per week per claimant receiving benefits at the maximum level. The Department has estimated that approximately one to two percent of the annual 25,000 claimants are granted benefits at the maximum level,

meaning that total savings to the system would be approximately \$59,000 per week.³⁹ And, as noted, every workers' compensation dollar is more valuable than a regular wage dollar because state benefits are not subject to federal income, Social Security and Medicare taxes.

State benefit levels are sometimes compared to "ideal" benefit levels recommended by various organizations, such as the National Commission on State Workmen's Compensation Laws and the Council of State Governments. Activists who believe injured workers are not receiving enough benefits say that few, if any, states are living up to the recommendations in these reports. While this is technically true, Washington's high level of benefits approaches, and in some cases exceeds, the "ideal" level promoted by activists. Also, it is important to remember that in practice, adding benefits equates to adding costs. And these higher incremental costs may be impractical for businesses to sustain.

The National Commission's publication in 1972, for example, originally caused a "flurry of activity...which resulted in higher benefits," but by the early 1990s, "an almost inevitable backlash against higher costs" occurred, causing widespread reforms to be enacted.⁴⁰ The Thomason study estimated that adoption of the National Council's "essential recommendations" would raise rates by 15% to 20%, and that implementing the Council of State Government's revised Model Act, published in 1974, would be even more damaging. The researchers found that implementation of the Model Act would likely raise rates by 60% to 75% while simultaneously widening the cost differences among states.⁴¹ This latter result, they noted, was particularly troubling due to its implications for firm location decisions. As the "gap between high and low-cost states" grows, there are "adverse consequences for employment in those high-cost states."⁴²

2. Recent judicial decisions have expanded benefits and increased costs of Washington's system

Several recent state court cases have re-interpreted statutory guidelines for calculating benefits, thereby increasing benefit payouts and threatening to drastically increase employers' premiums to support these payouts. Court decisions that imposed some of the highest costs are:

- *Cockle v. The Department of Labor and Industries* (2001) in which the state Supreme Court reversed 30 years of benefit law by ruling that benefits such as health insurance must be included in the calculation of a worker's benefits.⁴³ The decision leaves unanswered many questions regarding which other benefits must be included in wage calculations and resulted in the Department requesting a \$2.4 million budget increase simply to administer the complex and ambiguous

³⁹ Provided by the Washington Department of Labor & Industries, Planning & Research Services, January 2004.

⁴⁰ Thomason et al.

⁴¹ Ibid.

⁴² Ibid.

⁴³ *Cockle v. Labor and Industries*, 142 Wn.2d 801 (2001). The altered state law is Revised Code of Washington 51.08.178. This section of the code describes the formula for calculating benefits. Washington Administrative Code 296-14-522 through 296-14-530 are newly-adopted rules that provide for the incorporation of "core benefits" to the formula. See www.lni.wa.gov/rules/WorkersCompensation/default.htm.

decision.⁴⁴ It has been estimated that this decision costs employers \$40 million annually in workers' compensation funds.⁴⁵

- *Avundes v. Department of Labor and Industries* (2000) in which the state Supreme Court decided that the earnings of a seasonal worker could be based on the worker's earnings at the time of injury instead of his historic annual earnings.⁴⁶ This decision could greatly increase the benefits paid to workers in seasonal industries and discourage their return to work. Senator Jim Honeyford (R-Sunnyside) pointed out that the “*Avundes* decision requires employers to pay many seasonal workers far more in benefits than they ever earned working.”⁴⁷
- *Birkliid v. The Boeing Company* (1995) which increased the potential liability of employers by expanding the definition of “deliberate intention to injure” in a way that makes it easier for workers to sue their employers. The decision undermines the social purpose of workers' compensation by eroding the protection employers are supposed to have against costly lawsuits in return for paying into a state-mandated fund.⁴⁸

Even before many of these cases were decided in the courts, the Joint Legislative Audit and Review Committee (JLARC) recommended that the state find a way to “clarify and simplify” the calculation of benefits to reduce costs in the system.⁴⁹ Unfortunately, recent court decisions have only *added* to the system's complexity and cost. Legislation to clarify wage calculation was introduced in both the 2003 and 2004 sessions, but the issue remains unresolved.

3. Costs in the Washington workers' compensation system

Cost is one of the most difficult aspects of workers' compensation systems to assess. First, involved parties rarely agree on a definition of “acceptable” costs. Second, each state has a unique industrial composition that drives underlying costs in a unique way, so meaningful comparisons between states are difficult. Third, the theoretical and empirical research conducted to date is “limited, inconsistent and inconclusive” and does not provide any specific conclusions regarding the costs of public versus private systems.⁵⁰ Finally, comprehensive studies tend to focus on average costs across all industrial classifications within a state, but employers are really only concerned about the rates that apply to their particular business. Averages will continue to be developed as a measure of a state's overall competitiveness, but their usefulness in this regard is dubious and they should not be invoked to describe a specific employer's true circumstances.

⁴⁴ “Worker's Compensation System Reform,” *Washington 2003 Agenda*, National Federation of Independent Business, Washington state chapter, 2003, at www.nfib.com/cgi-bin/NFIB.dll/public/advocacy.

⁴⁵ “The Why of L&I,” by Myke Folger, *The Everett Business Journal*, February 2003.

⁴⁶ *Avundes v. Department of Labor and Industries*, 140 Wn.2d 282 (2000).

⁴⁷ “Senate Passes Bill Simplifying Workers' Compensation Benefits,” news release, Senate Republican Caucus, March 12, 2003, at www.src.wa.gov/News2003/HoneyfordPR031203.htm.

⁴⁸ *Birkliid v. The Boeing Company*, 127 Wn.2d 853 (1995).

⁴⁹ “Workers' Compensation System Performance Audit,” Washington Joint Legislative Audit and Review Committee, December, 1998. Other areas recommended for clarification were: the concept of “employability,” criteria for stopping time-loss benefits, criteria for vocational rehab payments and the effect of losing a claim.

⁵⁰ Thomason et al.

On the theoretical front, arguments on both sides of the private versus public debate abound. Proponents of state monopoly workers' compensation say public systems are cheaper because they eliminate some costs associated with the private sector such as marketing expenses and profits. Proponents of free market systems, on the other hand, assert that the lack of competition and profit discipline in public monopoly systems creates top-heavy bureaucracy, administrative inefficiency and over usage of benefits because the eligibility and duration of claims are not stringently evaluated. One indicator that points to greater efficiency among private companies is that Washington firms that self-insure experience lower claims costs than the state fund when managing similar cases.

Furthermore, researchers have pointed out that many of the well-exposed costs in private systems are simply hidden and unaccounted for in public systems.⁵¹ States with private insurance systems receive income tax revenue and other state and local tax revenue from insurance carriers, while states with monopoly funds do not. Monopoly-fund states must therefore increase the tax burden on the remaining employer base to support the same overall level of government services. Prominent researchers have concluded that the existence of hidden costs means rates for monopoly state funds are "probably under-stated relative to private-carrier rates," but that ascertaining and quantifying these hidden costs is "extremely problematic."⁵²

The lack of conclusive answers on the theoretical front is matched by a paucity of reliable data on the empirical front. Most empirical cost analyses attempt to calculate an average rate that spans all industrial classifications for each state and then rank the states accordingly in a single list to determine which are "relatively expensive" and which are "relatively cheap" or "competitive." Calculating comparable averages is inherently problematic, though, because each state is a closed system with its own unique set of several variables. These variables include:

- Industrial composition (states with a high percentage of jobs in "dangerous" industries, such as mining, necessarily have higher rates than states with a preponderance of jobs in "safe" industries, even if all other factors are equal).
- Statutory provisions (benefit levels and limitations).
- Wage levels and distribution systems.
- Health care delivery systems and costs.
- Attorney activity and lawsuits.
- Rate setting practices.

All of these factors and many more can influence costs in unpredictable and immeasurable ways, making it extremely difficult to find a common basis for rate calculation that allows for valid comparisons among states. The difficulty of comparing Washington's rates with those of other states has also been exacerbated by the fact that Washington is the only state

⁵¹ Ibid.

⁵² Ibid.

in the country that bases premium rates on hours worked instead of payroll. The reliability of all published rankings is lessened by this idiosyncrasy.⁵³

This is not to say that attempts have not been made. They have, and several analyses enjoy a significant amount of popularity and press coverage, so it is worth looking at a few of these in brief. One of the longest running analyses is conducted yearly by the National Foundation for Unemployment Compensation and Workers' Compensation (UWC). This analysis ranks states by two separate statistics: "Cost per Covered Employee" and "Cost per \$100 of Payroll." In the 2003 report (data from 2001), Washington was ranked as the fourth most expensive state in both measures, with an average cost of \$625 per worker per year (almost twice the national average of \$350 per worker per year) and an average cost of \$1.68 for every \$100 of payroll covered by the system (compared to the national average of \$1.08 per \$100 of payroll).⁵⁴

There are, however, many inadequacies that limit the usefulness of these calculations and rankings.⁵⁵

- The calculations include only the portion of benefit payments made in a calendar year. In reality, benefit payments for a single injury may be paid over several years.
- The data do not control for differences in states' industrial compositions.
- The data are based on benefits paid to workers rather than the cost to employers, and so some costs, such as administrative expenses, are not captured by the analysis.

A second oft-cited report is the "Oregon Workers' Compensation Premium Rate Ranking" published bi-annually by the Oregon State Department of Consumer and Business Services. While the UWC report ranks Washington among the five most expensive states, the 2002 Oregon report ranks Washington among the five cheapest, making it especially popular with Washington state officials. The Oregon report attempts to improve on the UWC data in several ways and has gained a level of acceptance within the industry, but its methodologies create a similar set of problems:

- All states' average rates are calculated using the Oregon economy as a base, and the 50 code classes used (of 450 total) represent only 67% of Oregon's payroll and only 62% of losses.⁵⁶ The more a state's industrial composition and loss profile differs from Oregon's, the more its calculated rate misrepresents true costs in that state.

⁵³ Senate Bill 5461 would have required the Department of Labor and Industries to report on the advantages and disadvantages of basing employer premiums on hours worked rather than total payroll. In the 2004 legislative session the bill passed the Senate, but failed to gain passage in the House.

⁵⁴ "Research Bulletin, Fiscal Data for State Workers' Compensation Systems 1991-2001," UWC-Strategic Services on Unemployment & Workers' Compensation, the National Foundation for Unemployment Compensation and Workers' Compensation, Washington DC, August 2003.

⁵⁵ Thomason et al.

⁵⁶ "Oregon Workers' Compensation Premium Rate Ranking Calendar Year 2002," Research and Analysis Section, Department of Consumer and Business Services, Salem, OR, March 2003.

- The calculated “average” rates do not include many rate-modifying factors such as experience ratings, deductibles, premium discounts, dividends and participation in retrospective rating programs.
- The Washington rate may be understated as a result of the method used to convert Washington’s “hourly rates” into the “payroll rates” used by all other states.⁵⁷

Thus, rankings that compare states provide only limited insight into cost affordability. An alternative way to evaluate costs is to examine what those who pay get for their dollars. Just about any system could lower costs by dropping services to a minimum level, but this would not benefit employers or workers or fulfill the objectives of the program. Successful workers’ compensation programs must fulfill the objectives its funders expect within a price range they feel is affordable.

In summary, many employers feel the cost of workers’ compensation in Washington is no longer affordable, and statistics also suggest that Washingtonians may receive a lower level of service from their government-run program than residents in other states receive from programs based on private competition. While “service” can be a difficult concept to quantify, the historically low (though improving) rates of customer satisfaction and disproportionately high injury rates in our state suggest that Washington’s monopoly program may be providing an insufficient level of service for the fees it charges.⁵⁸

4. Cost differentials between states

This is not to say Washington should raise rates even higher to make more money available for services, rather policymakers should ensure that current funds are being spent wisely. In addition, it is in the state’s best interest to ensure that Washington’s rates do not greatly exceed those in other states: large cost differentials between states can produce strong disincentives for businesses to locate in the more expensive states. Policymakers in California, for example, are struggling to keep businesses in their state, after several years of skyrocketing rates.

The extent of cost differentials is well highlighted in The Costco Wholesale Corporation’s 2003 financial report. On March 5, 2003, the company announced that its second-quarter earnings results had been hurt by the need to set aside \$26 million to pay for increased workers’ compensation costs, particularly in California. Richard Galanti, Costco Wholesale’s Chief Financial Officer, called the rising cost trend in California “alarming,” stating that even though only one-third of the company’s workforce is employed in California, two-thirds of the

⁵⁷ Washington is the only state that does not publish rates as a function of payroll, which further increases the difficulty of making comparisons among state systems.

⁵⁸ The rate of injury and illness for private sector workers in Washington is 37% higher than it is for workers in other states. Since injury prevention is a key objective of workers’ compensation systems, the issue is discussed more fully in a later section of this report.

company's compensation costs are generated there.⁵⁹ Costco spends an average of \$26,000 per claim nationwide, but it spends an astounding \$70,000 per claim in California.⁶⁰

The California workers' compensation system is generally regarded as one of the most expensive in the nation. As costs have risen in recent years, the issue has moved to the forefront of the state's political agenda. The cost increases are due in part to an expansion of benefits: in 2002, the legislature adopted a benefit increase that raised maximum benefits from \$490 a week to \$602 a week.⁶¹ (Washington's maximum benefit, in comparison, is even higher.) California's high costs have also been attributed in part to the prevalence of litigation – in 2002 California employers and insurers needed to hire lawyers to handle 29% of claims involving employees who missed a week of work, and California lawyers pocketed \$226 million in fees that year from workers' compensation cases.⁶² These are, indeed, alarmingly high additional costs for a system that is supposed to have the elimination of litigious court battles and the standardization of benefits at its core. While Washington is not yet facing the same level of crisis, California's experience serves as a warning for states like Washington that have seen a broad expansion of benefits and increased court involvement.

VI. Cost trends and drivers across the nation and in Washington

Nationally, the real cost of worker's compensation to employers has oscillated over time, although the overall trend has been upward. In the mid-1950s, private sector employees paid an average 0.5% of payroll for workers' compensation. By 1970, the figure was 1%, by 1987 it was 2%, and in 1994 it was 2.9%. The figure dropped to 2.0% in 2000, but has been rising again since then.⁶³ It is particularly interesting that costs have continued to rise even while injury and illness rates have declined, as the following chart indicates.⁶⁴ The American workplace is safer today than it ever has been, yet the cost of workers' compensation is still going up.

⁵⁹ "Costco Wholesale Corporation Reports Second Quarter and Year-to-Date Operating Results for Fiscal 2003 and February Sales Results," news release on earnings, Costco Wholesale Corporation, March 05, 2003, at www.corporate.ir.net/ireye/ir.

⁶⁰ "Workers' compensation costs dip into Costco's profits," by Christine Frey, *Seattle Post-Intelligencer*, Seattle, WA, March 6, 2003. In April 2004 the California legislature approved reforms which will reduce the costs the state's workers' compensation system imposes on employers.

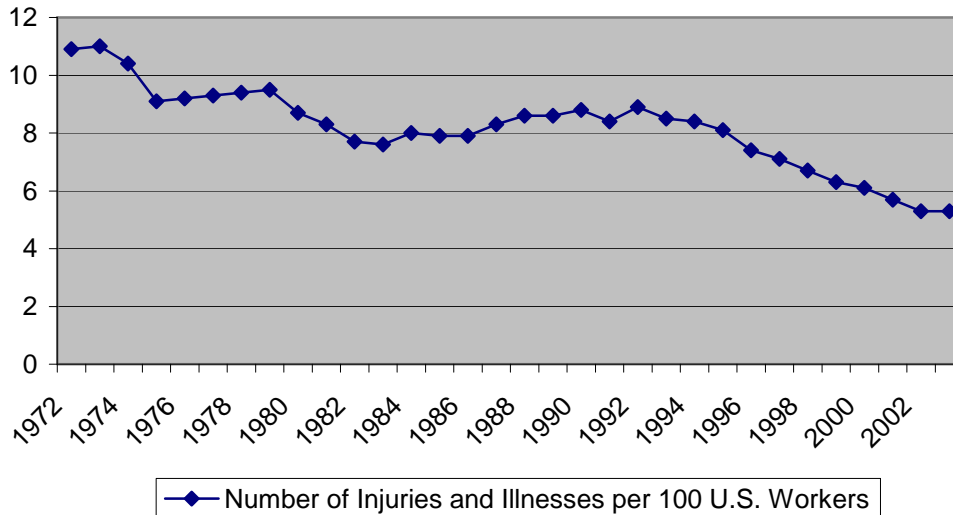
⁶¹ "Changes in Workers' Compensation Laws, 2002," by Glenn Whittington, *Monthly Labor Review Online*, Volume 126, No. 1, Bureau of Labor Statistics, U.S. Department of Labor, January 2003, at www.bls.gov/opub/mlr/2003/01/art2exc.htm.

⁶² "Workers' Comp Crisis," Review and Outlook Section, *The Wall Street Journal Online*, July 28, 2003.

⁶³ "Workers' Compensation," *Hot Topics and Insurance Issues*, Insurance Information Institute, New York, NY, March 2004.

⁶⁴ "Occupational Injuries and Illness Since the Passage of OSHA," Bureau of Labor Statistics, U.S. Department of Labor, 2002. This is also the source for the accompanying chart.

Rate of Occupational Injuries and Illnesses Among U.S. Workers, 1972 - 2002

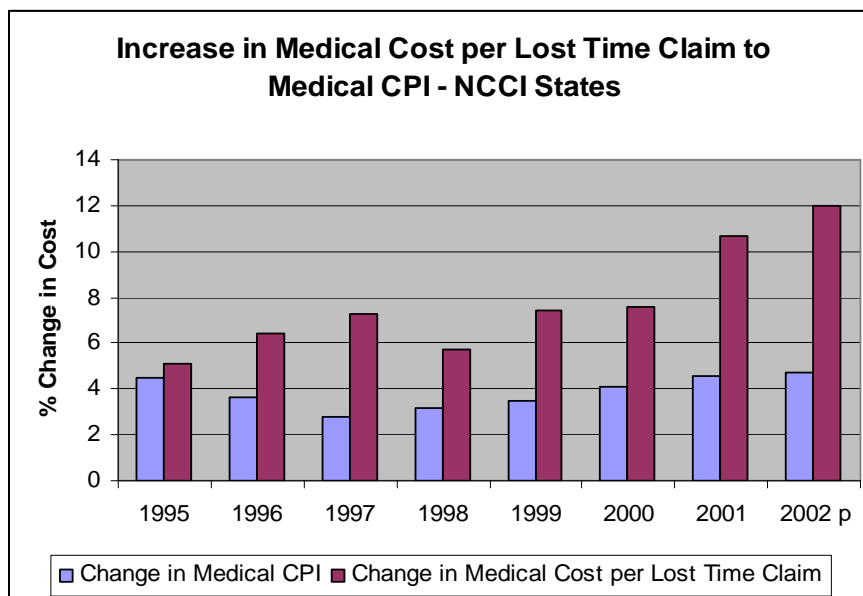


Several factors are contributing to workers' compensation premium increases across the nation: 1) rising medical costs; 2) an increasing number of claimants using the courts and 3) falling investment returns.

Rising medical costs are a result of several key factors:⁶⁵

- A broader definition of "workplace injury."
- An increased number of medical visits made per claimant. Although the frequency of claims has fallen almost 40% since 1990 and 27% since 1997, the number of medical visits per claim has increased steadily.
- Rising prescription drug costs.
- Increasing medical treatment costs. The chart below illustrates how the medical costs of workers' compensation claims have grown much more rapidly than medical costs in general as measured by the medical Consumer Price Index (CPI). For the period 1995 - 2002, lost-time-claim medical costs increased 82%, while the medical CPI increased just 36%.

⁶⁵ Ibid, July 2003.



Source: National Council on Compensation Insurance (NCCI), *Issues Report 2003*

The investment climate is a final factor worth highlighting because it has been implicated in Washington’s rate increases. Insurance companies often rely on investment returns for profitability. The premiums collected can amount to sums slightly less than the amounts that must be paid out in benefits, and investment income from assets can make up the difference. Assets in Washington’s monopoly workers’ compensation fund, for instance, generated about \$500 million in both 1999 and 2000, an amount equivalent to about half the amount of premiums collected from employers in each of those years.⁶⁶

While the Department of Labor and Industries’ financial statements do not show precipitous drops in investment income for the two-year period ending June 2002, they do record some impressive capital losses. Whereas the fund yielded about \$330 million in net realized equity gains for the two year period ending June 2000, it recorded over \$400 million in equity losses for the two year period ending June 2002.⁶⁷

Investment returns are separate from many of the other issues at hand, however, such as the adequacy of benefits and the efficiency of the system. While it is true that investment losses have altered the Department’s financial earnings in recent years, this phenomenon is not a substantive reason for employers and workers to blindly accept rate increases handed down by the Department. The extraordinary investment earnings of the late 1990s may simply have masked the underlying financial weaknesses in the system. The recent steep rate increases must be assessed in the context of actual services and benefits provided, not on how poorly the Department’s investment portfolio has performed.

⁶⁶ “State of Washington, Department of Labor and Industries, Industrial Insurance Fund, Financial Information (Unaudited) as of June 30, 2000,” Insurance Services Division, Department of Labor and Industries, at www.lni.wa.gov/ClaimsInsurance/RatePremium/About/FinInfo/Files/FinInfo20020630.pdf.

⁶⁷ Ibid, and the same report “as of June 30, 2002.”

VII. Injury Prevention under Washington Workers' Compensation System

One key measure of workers' compensation systems is how well they keep accidents and injuries from happening in the first place. A reduced number of injuries benefits everyone. Fewer injuries mean less physical, emotional and financial stress for workers and lower costs and improved productivity for employers. Of course, injuries and illnesses can never be completely eliminated, but this fact should not diminish the importance of a system's ability to reduce injuries to a minimum.

The Department of Labor and Industries has historically done a very poor job of reducing injuries in comparison to other states. Only three other states have higher overall injury rates. While some of this could be due to a higher-than-average concentration of "dangerous" jobs in Washington, the incidence rate of occupational injuries and illnesses is actually higher across every industrial category. In other words, any type of worker in any job is more likely on average to be injured on the job in Washington than in most other states. Recent research also suggests that Washington is not an anomaly. States with monopoly funds have on average more injuries than states which allow private insurers to sell workers' compensation coverage.⁶⁸

The table below illustrates how Washington workers are getting injured more often than their counterparts in other states. Injuries in Washington are more prevalent in every major industrial category. Washington workers sustained, on average, 37% more injuries than the average U.S. worker in 2001 and 38% more injuries in 2002.

Rate of non-fatal injuries in Washington compared to the national average, 2001

| Job Category | Total Non-Fatal Injuries & Illnesses per 100 workers | | Percent Difference |
|------------------------------------|--|------------|--------------------|
| | National | Washington | |
| Private Industry Overall | 5.7 | 7.8 | 37% |
| Agriculture, forestry, and fishing | 7.3 | 9.9 | 36% |
| Mining | 4 | 6.1 | 53% |
| Construction | 7.9 | 13.2 | 67% |
| Manufacturing | 8.1 | 10.4 | 28% |
| Transportation & public utilities | 6.9 | 8.9 | 29% |
| Wholesale and retail trade | 5.6 | 7.7 | 38% |
| Finance, insurance, real estate | 1.8 | 2 | 11% |
| Services | 4.6 | 5.7 | 24% |

Source: U.S. Department of Labor, Bureau of Labor Statistics. Data shown is for 2001.

⁶⁸ Thomason et al.

This phenomenon is a troubling one. The high injury rates are almost certainly a function of two factors: insufficient safety services and/or a high number of fraudulent claims. As mentioned, the Department's safety consulting and compliance units may be too closely linked to be effective. In addition, the Department has a much weaker incentive than private insurers to work cooperatively with employers to improve safety. The Department can raise rates at will to cover costs, but private insurers must contain costs to keep their premiums competitive with the rest of the market. As a result, private insurers are extremely vigilant about tracking down the causes of injuries and working with employers to improve dangerous environments. Private insurers are in the business of mitigating risk, and the best way to reduce risk is to improve safety.

It is important to note that Washington's high injury rates do *not* signify the need for expanding burdensome safety regulations. Rather, they suggest that Washington would benefit from the kind of competitive system in place and working effectively in other states. States that have reduced injuries to equal or below the national average do not have expansive sets of regulations: they simply allow normal market forces and economic incentives to shape the safety improvement efforts of insurers and employers.

VIII. Efficiency and effectiveness of Washington workers' compensation system

A third key measure by which workers' compensation systems can be evaluated is efficiency: How well does a particular system process claims, resolve disputes and dispense benefits compared to other systems? Does the system appear to do a good job of managing administrative costs? Does it provide an equivalent level of service to other, comparable systems for the costs it incurs? Is it focused on the right goals and outcomes?

This aspect of workers' compensation systems is difficult to measure since there are qualitative as well as quantitative components, but some key data points and the testimonies from the audit team and employers suggest that the Washington state system is "not as effective nor as efficient" as that found in other states.⁶⁹ In fact, the (Joint Legislative Audit and Review Committee (JLARC) audit team which reviewed the system found that "everything in the Washington state system is more formal and more process oriented" than in private systems.⁷⁰ The team's assessment of the Department's efficiency in fulfilling some of its key roles is disheartening:

1. Premium rate setting creates cross-subsidies and raises problems of fairness within the system

Workers' compensation systems strive to set fair rates for employers that correlate premiums with expected (and, where possible) historical losses. Two processes are employed to achieve this goal. First, employers are classified into one of over 300 main and 1200 sub

⁶⁹ "Workers' Compensation System Performance Audit," Appendix I, Washington Joint Legislative Audit and Review Committee (JLARC), December 1998.

⁷⁰ Ibid.

classification codes (or SICs, Standard Industrial Classifications) that express the expected “hazard” and consequent losses of employers engaged in a particular industry. All employers in a given code thus share the same “base rate” premium, or workers’ compensation tax. This first classification step results in a vastly differentiated spectrum of premiums. In 2003, for instance, some logging jobs carried a rate of more than \$10.00 an hour, but the rate for clerical workers and executive officers was 11 cents an hour.⁷¹

The second classification step applies to medium and large employers with three years of history and further differentiates rates for employers by adjusting the “base rate” with an “experience rating” which expresses the employers’ actual average loss experience compared to others in the same classification. Employers with a relatively high loss experience for their code pay higher tax rates while those with less loss experience are rewarded with lower rates. The experience rating is thus also meant to function as an incentive for employers to continuously improve workplace safety.

The audit team determined that the classification and experience rating practices used by the state system do not function as well as they should. In a free market environment, the rigors of competition require insurers to determine the most accurate rates for each classification since employers will seek out the lowest rates. The discipline of the market provides managers with current, accurate and detailed information about how to set rates within the system. Managers in the Department of Labor and Industries, though, are not necessarily concerned with fairness or accuracy since employers have no practical choice but to accept the rates ordained by the Department. As a result, administrative ease triumphs over fairness and accuracy, allowing several types of cross-subsidies within the program. Cross-subsidies involve revenue from one program activity being used to pay for another. They are clearly unfair to employers, and they undermine the public policy goals of the system by weakening the direct relationship between losses and rates, which in turn weakens safety incentives.

The audit team identified many different cross-subsidies in the Washington system. One such subsidy results from the arbitrary division of serious and non-serious claims for the purpose of rate assignment. Since the basis for these decisions had “no statistical foundation,” the team felt there was no certainty that costs were fairly distributed.⁷²

2. Consulting services create a conflict of interest

An inherent conflict of interest exists as a result of the Department’s oversight of two worker safety services that are normally separated: consultation and compliance. Consultation services are supposed to be a confidential, voluntary means for employers to get help making their workplaces safer without fear of retribution from regulators. Compliance and enforcement services are meant to enforce the worker safety and health law and penalize employers who do not comply.

⁷¹ “2003 Premium Rates,” Department of Labor & Industries, at www.lni.wa.gov/insurance/Rates/Files/2003RatesByIndustryType.pdf.

⁷² “Workers’ Compensation System Performance Audit,” Washington Joint Legislative Audit and Review Committee (JLARC), December 1998.

In Washington, both safety consulting and compliance functions are carried out by the Department of Labor and Industries under the oversight of the same director, and many employers worry that asking for consultation services will immediately initiate a full code review and costly citations against them.⁷³ By law information from the consultation service is not supposed to be shared with the compliance division. Still, as one employer noted in a focus group, “to ask a consultant is like asking the IRS to balance your checkbook.”⁷⁴ The Department recently stated that almost all employers who used the consultation services were satisfied, but it is important to note that only about 2,000 consultations are performed each year, meaning only about one in every 80 employers annually is asking for a consultation.⁷⁵

In other states, private insurers generally provide consultation services while a state department oversees compliance with occupational safety rules. This arrangement makes sense. Insurers want safer workplaces because it helps make them profitable, and employers want safer workplaces because they will save money and attract and retain the best employees. In fact, some private insurers require a company to be up to date in meeting injury prevention standards before it can be considered for workers’ compensation coverage. Importantly, employers do not worry that their use of consultation services will get them into trouble because the insurance companies which provide the consultation services are in no way connected to, and have no incentive to associate with, the government oversight agencies responsible for enforcement. This clear division allows each party to concentrate on and excel at its exclusive duties.

A competitive market environment also encourages private insurers to develop customized, company-specific loss prevention programs. Liberty Northwest, one of the region’s largest private workers’ compensation insurers, has its consultants “customize the product to fit a company’s culture, rather than impose a one-size-fits all approach.”⁷⁶ Liberty’s flexible service model is working well for employers. One year after implementing Liberty’s new product, the safety director of Superior Lumber in Glendale, Oregon noted that the number of workplace accidents had dropped by nearly half and claims costs have dropped 75%. Just as importantly, he added that “morale in the plant has gone way up and the need for supervision has gone way down.”⁷⁷

3. Delays in injury reporting and claims initiation

The whole purpose of workers’ compensation systems is to ensure prompt, reliable payment to injured workers – to provide “sure and certain relief” to workers and their families in the event of an injury.⁷⁸ But an astounding number of Washington workers do not receive benefits quickly because of the process followed by the Department.

⁷³ Ibid.

⁷⁴ Ibid, Appendix H.

⁷⁵ “L&I gets high marks for safety and health inspections, consultations,” Department of Labor and Industries news release, September 25, 2003, at www.lni.wa.gov/news/2003/pr030925a.asp.

⁷⁶ “Customized Programs Focus on Specific Customer Needs,” Liberty Northwest Insurance Corporation news release, May 12, 2000, at www.libertynorthwest.com/about/news/news000512b.asp.

⁷⁷ Ibid.

⁷⁸ Revised Code of Washington 51.04.010.

Many states have set and achieved goals to pay the vast majority of claims within 14 days of a worker submitting a claim. This is an important goal for the many families living paycheck to paycheck. Needless delays may make it impossible for a family to pay its monthly bills. In 1998, many states achieved this commonsense objective: 88% of injured workers in Oregon and 82% of injured workers in Wisconsin, for instance, received their first workers' compensation checks within two weeks of making a claim. In contrast, most injured workers in Washington must wait much longer to receive their first check.⁷⁹

This payment delay is largely the result of the Department upholding a “highly unusual if not unique” feature of the system.⁸⁰ Workers in Washington report their injuries through their doctors instead of their employers, as is common in other states. Doctors can take days or weeks to complete and return the forms to the Department, but the Department does not begin the required 14-day countdown until the necessary paperwork is in hand. The audit team identified this characteristic as a “very serious weakness in the Washington system” and stated that no new legislation would be needed to change it, but the Department has not yet streamlined the process.⁸¹ Additionally, self-insured employers report the Department requires them to begin the 14-day countdown from the date of the injury, without applying this same standard to itself.

The claims process does not improve much once the Department finally receives the paperwork from a doctor. The audit team found that the claims-initiation process requires claims to be passed through an unusually high number of departments and that it takes “more than six days to accomplish” what is just “90 minutes of actual work.”⁸²

4. Claims management process excludes employers

The members of the audit team identified several claims management features they believe need changing. Almost across the board, the team found that private insurers do a better job of measuring the right data points and using resources to consistently improve the claims management process.

A Key Claims Management Indicator Shows Deterioration in the Process

At the time of the audit, the Department rejected claims management recommendations, asserting that they had implemented a “long-term strategy” that “ha[d] set the groundwork for significant improvement” in the process.⁸³ Yet the Department’s actual performance has been moving in the opposite direction. The key outcome measure, the “change in the duration of time-loss benefits,” actually shows an *increase* in time-loss benefit duration every year since

⁷⁹ “Workers’ Compensation System Performance Audit,” Washington Joint Legislative Audit and Review Committee (JLARC), December 1998.

⁸⁰ *Ibid.*

⁸¹ *Ibid.*

⁸² “Workers’ Compensation System Performance Audit, Appendix I,” Washington Joint Legislative Audit and Review Committee, December 1998.

⁸³ “Workers’ Compensation System Performance Audit,” State of Washington Joint Legislative Audit and Review Committee (JLARC), December 1998.

1999. There was a 1.1% increase in 2000, a .01% increase in 2001, and an astounding 16% increase in 2002.⁸⁴

Early and Sustained Employer Involvement is Needed

Almost all private insurers carefully monitor a best practice standard for the industry, the speed with which, once an injury occurs, “three-party contact” among employer, attending physician and injured employee is established.⁸⁵ Managers at private firms have learned that early and continued employer involvement is critical to keeping claim costs low and reducing litigation. Washington’s workers’ compensation managers, however, do not even measure this performance standard, and employers are much less involved than they are in other states. Perhaps most disturbing, though, is that Washington employers actually want to be more involved, but they feel that the current process excludes them.⁸⁶

Focus Should be on “Return to Work,” not “Employability”

Most private insurers focus on getting an injured person back to work as the ultimate goal of claims management. Washington’s program, however, focuses mainly on “employability.” This standard does not have much meaning for injured workers who need a secure source of income more than having a state agency consider them “employable.” A member of the audit team with years of experience in the insurance business stated that many resources in the Washington state system are wasted on assessing employability. The audit team member said these resources would be used more effectively if they were devoted to helping workers find and obtain actual jobs.⁸⁷

5. The Department has not used resources effectively

The Department made a “significant investment” in expensive document scanning and imaging technology in an attempt to improve operating costs in the Insurance Services section of the Department of Labor and Industries. A thorough analysis revealed that the overall effect of the investment was negligible to negative. Operating costs increased, productivity decreased, and neither claims managers nor customers benefited in any identifiable way.⁸⁸

The Department also uses premiums to fund a “substantial amount” of research, but there is little public discussion or involvement regarding the research agenda or whether it produces anything of value for the workers and employers who pay for it.⁸⁹ The Department also funds a

⁸⁴ “Agency Mission,” Department of Labor and Industries, report to Office of Financial Management, 2003.

⁸⁵ “Workers’ Compensation System Performance Audit,” Appendix I, Washington Joint Legislative Audit and Review Committee (JLARC), December 1998.

⁸⁶ See *ibid* Appendix I. See also “Agenda for Reform: Priority Solutions for Improving Washington Small Business Climate, Results of the 2003 Statewide Small Business Conference,” Washington Policy Center Policy Brief, January 2004.

⁸⁷ “Workers’ Compensation System Performance Audit,” Appendix I, Washington Joint Legislative Audit and Review Committee (JLARC), December 1998.

⁸⁸ *Ibid*.

⁸⁹ “Workers’ Compensation System Performance Audit,” State Joint Legislative Audit and Review Committee, (JLARC), Olympia, Washington, December 1998. A bill considered in the 2004 legislative session, SB 6391, would

number of program activities that are not related to collecting workers compensation premiums or managing claims. Enforcing safety standards (WISHA⁹⁰), wage and hour rules, extraneous legal and administrative work and overseeing employment standards all draw time, energy and budget away from the program's core mission. For example, the Department charges 99% of central administration costs for its five Divisions to the workers' compensation accounts.⁹¹ These functions should be funded through general revenue appropriated for the purpose, not with money drawn from the workers' compensation trust fund.

Finally, the Department may be significantly overstuffed in some areas. For example, claims from self-insured employers are highly regulated by the state and the Department checks all complex self-insured claims for accuracy. While Michigan oversees its complex claims with a staff of six, the Department of Labor and Industries employs a staff of 70 to perform the same task.⁹²

6. Appeals process is lengthy and costly

The Washington workers' compensation system has many levels of dispute resolution that eat up time and resources. In most states, the appeals process is composed of just four steps, but in Washington, an appeal is subject to as many as nine steps. If the additional steps helped create improved outcomes they might be warranted, but the audit team found no evidence that this was the case.⁹³ In fact, the team suggested that the large number of steps may cause claims managers to be less diligent in the initial review process since they feel they have a "second chance to correct errors."⁹⁴

7. Service management suffers from lack of continuity

The service side of the current workers' compensation system also suffers from several problems. First, the fund has had limited continuity because a new director is appointed almost every time a new governor is elected, and there is no requirement that the appointee have experience in the insurance industry. Private insurance companies, in contrast, are generally headed by individuals with a wealth of experience.

Second, the exclusive fund does not publish the standardized reports used by most of the industry. Even the government's own audit team found it "very difficult" to determine in the current documentation which services were being funded by premiums, and which "should" be funded by premiums.⁹⁵

have set research priorities for the Department. The bill was approved by the Senate but failed to gain passage in the House.

⁹⁰ "Washington Industrial Safety and Health Act," Washington state's version of the federal OSHA law.

⁹¹ "2003 State of Washington Accountability Report, 2003," Office of the State Auditor, p.213, released March 23, 2004.

⁹² "The Why of L&I," by Myke Folger, *The Everett Business Journal*, February 2003. SB 6317, a bill to expand the role of self-insurers, passed the Senate in 2004 but failed to gain passage in the House.

⁹³ "Workers' Compensation System Performance Audit," Washington Joint Legislative Audit and Review Committee (JLARC), December 1998.

⁹⁴ Ibid.

⁹⁵ Ibid.

Third, the Department has no accountability to its key stakeholders: workers and employers. The Department answers first and foremost to the governor and legislature who necessarily have a less direct interest in the system's efficiency than the program's clients. To help fix this problem, the audit team recommended the creation of a board, composed of employers, workers and members of the public, that would resemble the boards used by other exclusive fund states and the boards of directors that oversee private insurers.⁹⁶ The Department issued a formal "non-concur" statement in response to this recommendation, saying such a board would make state government "less accountable to the voters of the state."⁹⁷

8. Customer satisfaction has significantly improved

Customer satisfaction can be a difficult concept to measure, but it should not be overlooked in a performance assessment of a workers' compensation system. The Department has a duty to provide an "acceptable" level of customer service. But what, and who, should define "acceptable"? This is not an easy question to answer.

Without doubt, the Department's customer satisfaction ratings were *unacceptable* in the late 1990s. After questioning and surveying injured workers who had interacted with the system, the audit team found that an almost unbelievable 30% of workers felt they had not been treated with dignity and respect by claims managers, and 40% felt that claims managers had not behaved ethically towards them. Ratings for the Board of Industrial Insurance Appeals were even lower.⁹⁸

The Department embarked on a campaign to improve its customer service, and it made good strides with workers, according to surveys conducted by the Gilmore Research Group, a Seattle-based firm hired by the Department from 1999 to 2003. The surveys indicate customer service towards workers has improved substantially over the last five years. Among the positive developments are:⁹⁹

- An increase in the number of time-loss benefit recipients who were satisfied with the claims experience. In 1998, 56% reported being satisfied, in 2003 that figure was 74%.
- A decrease in workers who were "very dissatisfied" with the overall claims experience. In 1998, 22% of workers reported being very dissatisfied, in 2003 only 11% did.
- In 2000, 57% of workers said that it was either "very easy" or "somewhat easy" to get medical bills paid. In 2003 that figure was 68%.

The Department has clearly made strong improvements in its relations with workers. At the same time, it must be noted that parallel improvements in relations with employers have not materialized. Employers have recorded little or no improvement in their assessment of service

⁹⁶ Ibid.

⁹⁷ Ibid.

⁹⁸ Ibid, Appendix G.

⁹⁹ "Customer Satisfaction Study 2003", Gilmore Research Group, Seattle, August 2003.

over the last five years. In fact, employers are less likely to “strongly agree” with positive statements about the Department’s performance than they were in earlier years. Some of the most significant findings include:¹⁰⁰

- Overall employer satisfaction with the Department is fair and has held steady for the last six years. Seventy-five percent of employers were satisfied with their experience, although only 33% were “very satisfied” and 42% were “somewhat satisfied.”
- The number of employers who “strongly agreed” with the statement that “L&I claims staff were courteous and professional in their dealings with me” dropped from 66% in 2000 to 54% in 2003.
- In 2000, 59% of employers “strongly agreed” that their questions to the Department were answered in a way they could understand. In 2003, only 46% “strongly agreed.”
- In both 2000 and 2003, only 58% of employers agreed that “L&I protects the interests of employers.” The rest disagreed or had no opinion.
- Forty-five percent of employers who were “dissatisfied” with claims disbursement said the Department fails to investigate enough before disbursing benefits. This number has doubled since 2000 when only 22% of such employers gave that reason and is way up from 1998 when only 2% gave it. Fraudulent claims were also a recurrent complaint in employer focus groups conducted in the late 1990s.

These customer satisfaction statistics are problematic because employers pay for the majority of the almost \$2 billion of benefits disbursed each year, and they should feel reasonably satisfied with the system they are required to fund.

In contrast, satisfaction rates for other state systems are higher. Wyoming and Ohio, for instance (two other states using the monopoly state-fund insurance model) have much higher satisfaction rates: 88% of injured workers in Wyoming were satisfied with their states’ service,¹⁰¹ and over 90% of injured workers in Ohio are satisfied.¹⁰² Similarly, the Canadian province of Saskatchewan (which also uses an exclusive, government-run system) has consistently tracked both worker and employer satisfaction ratings in the 86% to 96% range for the period 1997-2001.¹⁰³

¹⁰⁰ Ibid.

¹⁰¹ “Wyoming State Government 2003 Annual Report”, Wyoming Department of Employment, at <http://www-wsl.state.wy.us/slpub/reports/>

¹⁰² “Ohio Workers’ Compensation Benchmarks,” Customer Trend Analysis Department, Ohio Bureau of Workers’ Compensation, at www.ohiobwc.com/home/current/FactFigLnks.asp.

¹⁰³ “2001 Customer Satisfaction Survey Results and Five-Year Comparison, 1997 – 2001,” Saskatchewan Workers’ Compensation Board, 2002.

IX. Policy recommendations

As the preceding discussion indicates, Washington's workers' compensation system would benefit from a number of reforms, ranging from streamlining existing procedures to allowing employers a choice of insurers. Key policy changes that would improve the quality and cost-effectiveness of the system are presented below.

1. Make sure workers' compensation trust funds are used only for workers' compensation administration and benefits.

As time passes government programs tend to accumulate functions that do not relate to their original mission. The Department of Labor and Industries uses money from the workers' compensation trust fund to pay for a number of functions that bear little or no relation to collecting premiums or paying out benefits to injured workers. Enforcing safety standards, wage and hour rules, general legal and administrative work and overseeing employment standards, while important in themselves, all place added financial pressure on the workers' compensation program. It is unfair to workers and employers when money intended for workers' compensation purposes is re-directed to pay for other activities.

Naturally it is easier for an agency to pay for additional functions with an existing funding stream, like workers' compensation premiums, than to argue every two years for specific appropriations from the legislature. While this might be an attractive solution for a state agency, it deprives tax-paying citizens of an essential safeguard against the mis-use of public money. When there is no biennial review through the normal budget process, elected officials have little opportunity to judge whether the Department's activities continue to justify the money being spent on them.

The State Auditor estimates that in 2003 more than \$3.4 million in general administration costs were charged to the workers' compensation accounts. All activities of the Department of Labor and Industries not directly related to managing the workers' compensation program should be funded through general revenues appropriated in the regular state budget. This reform would maintain faith with employers and workers, re-focus the program on its central mission and provide better claims service to injured workers.

2. Require annual financial audits of workers compensation accounts.

Currently the state workers' compensation system is not subject to regular financial audits. In fact, the state sets far less stringent fiscal audit and reporting requirements for itself than it does for the insurance companies it regulates. To eliminate waste, identify financial weakness and assist program managers, the Department should use the State Auditor or hire an outside accounting firm to conduct thorough annual audits. The results would build greater transparency and accountability into the system, help build public trust and allow employers to determine whether the premiums they pay are being managed wisely. Regular audits would provide the public with a clear financial standard by which to compare Washington's workers'

compensation program with those of other states. It would also provide a reliable guide to policymakers as they consider possible reforms in the current system.

3. Allow small groups of similar employers to self-insure

Thirty-five states allow small groups of employers in related businesses to self-insure as a group. This practice gives small businesses with limited financial resources access to the same self-insurance as their larger competitors and the capability to reject broader public or private insurance options. Additionally, such groups can help spur the sharing of best practices and improve safety because each employer has an incentive to help lower the injury costs of other group members.

Washington law currently bars small groups of private employers from self-insuring, reserving that choice to large companies and a few public entities. There is no reason to limit this alternative to government. Citizens in the private sector should be allowed equal access to group insurance. It is important to realize that this action would not in any way compromise protections for workers: injured workers are entitled to their statutory protections regardless of how their employers choose to insure, and all self-insured entities must pass the legal standard of financial fitness before they are allowed to leave the state program.

4. Legalize private insurance

Washington is one of only five states that make it illegal to buy private workers' compensation insurance. The ban forces all employers not large enough to afford self-insurance to purchase coverage from the state monopoly. While supporters of the current system frequently cite Washington's "low costs" as a reason to shun change, national level research does not support a demonstrable connection between public insurance and lower costs. Moreover, Washington's use of non-standard reporting methods and metrics means comparisons among states are difficult and fraught with uncertainty. Finally, costs can only be assessed as a factor of the services to which they are related, and there is evidence that Washington's current system provides inefficient service to employers and workers for the cost incurred.

Allowing private insurers to compete for workers' compensation insurance business would bring market discipline to the industry. To be successful, insurers must provide fast, effective service at low rates. They do not perform endless rounds of surveys and analyses to become efficient, simply because they do not have the luxury of doing so. Insurance carriers also need to be ever-vigilant in determining the causes of accidents and improving workplace safety to keep rates competitive; a characteristic from which all Washington employers and workers would benefit. Finally, allowing private insurers to manage the insurance side of workers' compensation would free the professionals at the Department of Labor and Industries to concentrate on their core function: the regulation, oversight and promotion of safe workplaces.

As part of legalizing private workers' compensation insurance, the state could maintain its own program and provide an additional choice in the marketplace. In addition, the state could

serve as the “insurer of last resort” for firms that have difficulty getting the required level of coverage from private insurers.

5. Bring benefit levels more in line with those in other states

Washington is one of only a few states that allows benefits to run significantly higher than the state’s average annual wage.¹⁰⁴ Reducing the cap by 10% to 20% to match the national average would save money because payments to higher income workers would be set so they did not exceed the state’s average wage. Injured workers who earn the same or less than the average wage would not be affected by this change.

6. Consultation services should be separated from enforcement and regulatory services

The fact that the Department of Labor and Industries enforces regulations while at the same time offering voluntary consultation services on how to comply creates an inherent conflict of interest. Private insurers have a better history of success in improving the safety of their clients’ workplaces. Natural economic incentive spurs the energies and eventual success of these companies. Preventing injuries from happening in the first place is the best possible outcome for employers and workers, and its importance to a workers’ compensation system should not be overlooked. Policymakers should consider assigning workplace safety consultation services to another state agency or, better yet, grant a premium discount to companies that hire private consultants to provide these services. An alternative would be to allow private choice in purchasing workers’ compensation insurance. Any of these approaches would allow the Department to concentrate its efforts on regulatory enforcement and claims management.

7. Workers should report injuries through their employers rather than doctors

There are many reasons to adopt this practice, which is used by almost every other state. First, early and active employer involvement is widely considered paramount in reducing costs, rehabilitating workers and improving workplace safety. Under the current system, employers have little or no involvement in claims. Second, doctors have little vested interest in the quick and thorough processing of claims, and any delays in the completion of paperwork on their end translates into payment delays for injured workers. Injured workers should not have to wait more than the standard 14 days from the date of their injury to receive their first compensation check. The Department’s measure of time elapsed between when it receives a claim from a doctor and when it sends a check to an injured worker is of little real-world value to workers. Reporting injuries through employers would make the workers’ compensation system more efficient, would promote workplace safety, and would provide better service to workers.

¹⁰⁴ As mentioned previously, Washington actually uses the average monthly wage to calculate maximum benefits, but the end result is basically the same.

8. Efforts should be geared towards “job placement” rather than “employability”

The current practice based on “employability” is an agency-focused rather than a worker-focused standard. Workers do not really care whether or not a government agency considers them conceptually employable; they care whether or not they have a source of income. The agency should re-focus its efforts by concentrating on helping workers return to their jobs or find new ones suited to their skills and physical condition.

9. Clarify and simplify the calculation of benefits

A key policy goal of “no-fault” insurance is to keep costs low by eliminating the need for judicial involvement. More and more frequently, though, Washington workers are seeking decisions in the courts, partially as a result of unclear legislation. Policymakers should resolve the calculation of benefits quickly to avoid a patchwork of judicial decisions. One simple reform would be to authorize the state to “compromise and release” certain claims as most other states do. This would allow the Department and an injured worker to agree to a lump sum settlement to resolve an outstanding claim, without resorting to costly litigation and appeals. Another would be to replace the system’s cumbersome time-loss and pension benefits calculation, which now involves marital status and number of dependents, with a single flat-rate calculation.

X. Conclusion

The original purpose of workers’ compensation was to provide sure and certain relief for workers in the event of an on-the-job injury. In return for joining a legally-mandated program, employers gained protection against individual lawsuits brought against them by injured employees. For employers and workers the system is intended to provide security, financial predictability and fair treatment.

Yet the “exclusive remedy” aspect of workers’ compensation has been eroded. Workers routinely sue the Department in court to gain a higher level of benefits, and, while they are not suing employers directly, employers must bear the full cost of lawsuits and any resulting awards through higher workers’ compensation premiums. In addition, employers must pay the long-term cost of litigation when court decisions result in a permanent higher level of benefits for all claimants. Injured workers and their attorneys who sue and win realize an immediate economic gain, while the system as a whole is undermined and risks becoming fiscally unsustainable, to the ultimate detriment of employers and workers.

The research and policy changes presented in this study point to concrete proposals for strengthening the system, and can serve as an essential guide for the state’s policy leaders. Future studies will examine the impact of high workers’ compensation costs on job losses, a worsening business climate, lower economic growth and reduced personal incomes. Yet even current research indicates that systematic reform is urgently needed to bring the workers’ compensation program back to its original purpose; a true insurance plan which mitigates risk for employers, provides fair and reliable benefits for injured workers and contributes to a stable business environment for all Washington citizens.

About the Author

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