

MANAGING AND REDUCING COSTS

THE IMPORTANCE OF SHOPPING AROUND

With more than 300 insurance companies selling workers' compensation coverage in Michigan, it is imperative that employers shop around to find the most cost-effective coverage for the specific situations. There are not only a large number of carriers, but also the rates they charge cover a wide range. About 20 of the largest insurance groups account for over 75 percent of the dollars paid in workers' compensation insurance premiums. The rates charged, even among these large firms, vary so widely that it is not uncommon for the highest rate available to be twice as high as the lowest rate.

However, insurance purchasers must remember that price is NOT everything. Bad service from the insurance carrier or agent will result in higher net cost while good service can result in lower net cost.

WHAT TO LOOK FOR IN AN AGENT/AGENCY?

Workers' compensation coverage is the same with all carriers. The difference is in the cost and service provided by both the agent/agency and the insurance carrier.

The insurance agent is a person licensed by the state insurance bureau who solicits, negotiates or affects insurance contracts on behalf of one or more insurance companies, also known as insurance carriers.

The insurance agency is the insurance sales office directed by a general agent, manager, independent agent or insurance company manager. The actual insurance carrier provides the insurance coverage, not the agent or agency.

An important factor to keep in mind is that there are two kinds of insurance agents:

- **Captive Agents** represent only one insurance company.
- **Independent Agents** represent an average of five to ten insurance companies.

One agent/agency cannot represent all insurance companies. Agents are there to help. Any agent should be able to answer questions about insurance and provide an assessment of the company's needs and insurance products to meet those needs. Also, any insurance agent should

provide prompt, quality service in the case of a claim whether in direct dealing, or acting as a liaison, with the insurance carrier. Company officials should expect more than a yearly renewal contact from the agent and work toward building a continuing relationship.

What to look for and questions to ask: The insurance agent should be a licensed professional with strong customer and community ties. Get references. Independent agents should be asked how many insurance carriers his/her agency represents and should provide a list of the carriers' names.

Does the agency or agent specialize in commercial insurance or is it just written incidentally? Is the agency full service, meaning that they can handle all the insurance needs, including providing assistance with claims?

Who will handle the account on a daily basis? If not by the agent, will the account be handled by a customer service representative? What is their level of training and knowledge?

Ask what the agent perceives as his/her role in handling claims and helping to resolve claims disputes between the customer and the insurance company.

Does the insurance agent hold any professional designations? This means that they have invested considerable time into additional schooling.

The agency's experience in the industry from working in the past and matching up companies with insurers who know the industry is key. Insurers familiar with the industry can reduce the effect of claims on customers through good loss-control and claims departments.

Expect excellent service and competitive prices along with a thorough knowledge of special programs to reduce costs. Expect regular reports regarding your losses and the annual Michigan Experience Rating Form.

Expect periodic reviews of the insurance coverage to keep up with changing needs. Know that a professional is handling the account in coordination with the employer.

Finally, keep in mind that agents represent the insurance carrier. Unbiased advice and analysis may be obtained from certified insurance counselors.

BUYING WORKERS' COMPENSATION INSURANCE: IMPORTANT RIGHTS

Important rights included in Michigan's Workers' Compensation Act:

- An insurance company may not require that a business buy other forms of insurance from that company before it will sell workers' compensation coverage. However, a better package may be obtained using multi-line discounts with a specific carrier. Insurance agents can provide more information about discounts.
- After making a written request and paying a reasonable fee, a business is entitled to receive a copy of all information used for its classification and rating. The State of Michigan does not set the classifications.
- If a business disagrees with the way it has been classified or rated, it may request that the insurance company review its rating decision. If the disagreement persists, the business has the right to appeal to the Commissioner of Insurance.

Any workers' compensation agent can provide information on how to request a review. In addition, insurance companies provide an annual written notice regarding its client's classifications, including review procedures and rights to appeal. This is usually the last page of the policy, entitled Michigan Notice to Policyholders. Company officials should remember to keep detailed records and written documentation.

COSTS OF WORKERS' COMPENSATION COVERAGE IN MICHIGAN

Michigan is one of 36 states with some form of open competition rating law. The state has had this type of competitive open market since 1983. Michigan's law has outpaced all other states in driving down and holding down workers' compensation costs. In most cases, our rates are lower than they were in 1983.

Prior to 1983, virtually all insurance companies used the same rates. Some states still use this type of rate setting, where the insurance companies hold the power over prices and use dividends and rebates to mask the real costs of workers' compensation coverage. Five of these states have monopolistic state funds.

WAYS TO CUT COSTS

As with most insurance, Michigan's workers' compensation rates reflect a company's experience, its commitment to safe practices and its determination to holding down costs. The formula for reducing workers' compensation costs is simple:

$$\begin{array}{l}
 \text{INJURY PREVENTION} \\
 \text{Loss control} \\
 + \text{Lowest cost insurance program} \\
 = \text{Lower workers' compensation costs}
 \end{array}$$

But, those employers who have successfully cut their workers' compensation costs report that the reality of cost reduction is very challenging and requires the attention and commitment of the highest levels of management.

A study of 5,568 employers in 29 different industries conducted by Michigan State University and the W.E. Upjohn Institute for Employment Research gives some insight regarding injury prevention and loss control. The study findings, issued in 1993, show that employers with the best records (fewest workers' compensation claims) had these common qualities:

- Placed great emphasis on safety and prevention practices;
- Were more inclined to have open managerial styles that encourage shared decision making; and
- Had consciously developed disability prevention and management strategies.

Employers are encouraged to look at their individual operations with a critical eye toward identifying ways to further reduce injuries and illness, thus improving working environments while cutting workers' compensation claims cost. Michigan companies that have successfully reduced workers' compensation costs have offered the following cost-saving suggestions:

- Set safety goals.
- Create an employee incentive program.
- Improve accident reporting and investigating.
- Make review of injury reports part of the job of top managers.
- Review injury reports promptly.
- Have front-line supervisors and employees design injury prevention programs.
- Establish training programs in safe lifting techniques, hand safety and hazard recognition.

- Purchase appropriate equipment along with making other ergonomic changes.
- Develop return-to-work programs in which injured employees are allowed to return gradually, from simulated work settings to meaningful transitional or part-time assignments to full-time duty.
- Write job descriptions that include physical capability requirements.

By making an effort to improve the safety of the workplace, companies can reduce their workers' compensation insurance costs in two ways:

- They can reduce the dollar value of business losses by limiting the severity of accidents or by eliminating them altogether.
- They may make the business eligible for schedule rating credits, premium credits and other incentive programs offered by carriers.

Nearly all insurance companies provide safety inspection services and loss prevention/control programs to help clients keep costs under control. These are services that businesses should inquire about before choosing an insurance carrier.

In addition, the Consultation Education and Training (CET) Division of the Michigan Department of Energy, Labor & Economic Growth assists employers and employees to eliminate safety hazards and reduce work injuries through education programs, training and consultation with staff specialists. Professional consultants combine their talents with the latest safety information to offer a variety of programs with proven effectiveness in reducing the frequency and severity of injuries.

CET also offers an on-site consultation program to promote voluntary compliance with Michigan's safety standards. This program provides a workplace inspection that is identical to the Michigan Occupational Safety and Health Act (MIOSHA) inspection, but without citations and monetary penalties if corrections are made within a reasonable period of time (usually six months).

For a free workplace consultation on accident prevention, safety training and other services, contact:

Consultation Education and Training Division
Michigan Department of Energy,
Labor & Economic Growth
P.O. Box 30643
Lansing, MI 48909-8143
Phone: 517.322.1809
Web site: www.michigan.gov/cis/0,1607,7-154-11407_15317---,00.html

DIFFERENCES IN WORKERS' COMPENSATION AND OTHER LINES OF INSURANCE:

Short-term penalty rates are charged to firms that switch insurance carriers in the middle of a workers' compensation policy year. This is the only line of insurance that carries such a penalty and shoppers should be careful when contemplating a switch during a policy year.

Policy dates are also important. Many employers get into problems because of changing their policy dates and causing experience to carry over for a longer than normal period.

Employers that change carriers must know that open claims will continue to be controlled by the old carrier.

These are all important issues employers must discuss fully with their insurance agent.

Below is a sample timetable involved in calculating a modification factor, and, thus the premium—each employer needs to insert his/her own policy anniversary date:

- Policy January 1, 2007–January 1, 2008 (experience and payroll covering years 2003, 2004 and 2005)
- Policy January 1, 2008–January 1, 2009 (experience and payroll covering years 2004, 2005 and 2006)
- Policy January 1, 2009–January 1, 2010 (experience and payroll covering years 2005, 2006 and 2007)

YOUR RIGHTS REGARDING WORKERS' COMPENSATION

Audits and Refunds

A workers' compensation insurance policy, like all other insurance, is a legal contract. The policyholder agrees to pay a certain amount of money each year and the insurance company is required to adhere to the provisions stated in the policy. As with any legal contract, an insurance policy must be maintained. The ongoing requirement of a workers' compensation policy is the audit.

An initial premium is based on a company's own estimates of its payroll and job classifications. The audit compares those estimates against the actual payroll and job classification figures for the year the policy was in force. Any difference between estimates and actual payroll figures is reflected in the adjusted premium.

Audits are done as soon as possible after coverage is concluded or after the job policy is renewed. Since premium costs are based partly on a company's job classifications, the auditor also reviews the business to be certain the workers' compensation premium being charged is accurate.

The Process

The auditor will contact the business and make an appointment to review the payroll records and job classifications. Company officials should take this opportunity to also discuss any concerns about the insurance coverage. To save time for all concerned, the firm should have the following records available: Federal Income Tax Return Form 941, the general ledger and payroll records.

Know Your Rights

The following information is excerpted from the Michigan Notice to Policyholders, a notice that appears as the last page of the policy as required by Michigan law. The actual notice should be reviewed for further information.

Company officials may request a payroll audit once each calendar year. The request must be in writing to the carrier and must state the payroll expenditures that have changed by 20 percent or more and must state the reasons for that change. The carrier will complete the audit within 120 days of receipt of the request if provided all the information needed to perform the audit.

Company officials may request reserve and redemption information that relates to the premium for this policy. The request must be in writing and the carrier must respond with that information within 30 days of receipt of the request. The company may submit a written request for a meeting if it believes the premiums are excessive because of unreasonable reserves or the unreasonable redemption of a claim.

Insurance companies can reserve a portion of a client's premium to cover the projected cost of paying for claims against a specific client. These reserves may be held for:

- A. Claims that have been made but not yet closed; or
- B. The cost of injuries or illnesses that have occurred but have not yet had claims filed.

Also, a written request may be submitted to the carrier for a review of the method by which the carrier's rates and premiums are determined. A written appeal may be made to the Commissioner of Insurance if the results of the review are unsatisfactory.

An insurance company must make payments it owes in a timely manner—generally on or before the date specified in the policy or, if no date is specified, within 60 days after the policy expires. It must pay a 12 percent per annum simple interest penalty on any late payments. Specifically, dividend payments must be made within 60 days of the policy's expiration; premium refunds resulting from payroll audits are due within 60 days of the audit's completion; and premium refunds resulting from a retrospective rating plan are due within nine months of the policy's expiration.

Agents can provide information on how to request an audit, a meeting with management or information on premium factors.

Premiums Based On Remuneration

Policy premiums paid by companies are based on remuneration to employees. Payroll is the most common component of remuneration, but it is not the only one. Generally, remuneration includes: regular salary and hourly pay; commissions; bonuses; overtime pay, less the premium portion; holiday, vacation and sick pay; piecework, incentive plans and profit-sharing plans; payments to employees for hand or power tools; value of rent, housing and meals provided to employees; value of store certificates, merchandise or credits given to employ-

ees; and payments of contributions required by law to statutory insurance or pension plans.

ALTERNATIVE FORMS OF WORKERS' COMPENSATION COVERAGE

Self-Insured Programs

To self-insure, either individually or as a group of employers, all applicants must first apply for approval to the Self-Insured Programs Division of the Workers' Compensation Agency, Department of Energy, Labor & Economic Growth. The agency may be contacted by accessing its Web site at www.michigan.gov/wca.

Individual Self-Insured Programs

The Workers' Disability Compensation Act allows some financially secure companies to carry their own workers' compensation risk rather than contracting with an insurance carrier. Today, more than 450 employers are individually self-insured in Michigan.

Generally, employers applying for individual self-insured status are paying premiums over \$100,000 in the traditional market. Some of the advantages of being individually self-insured include the potential for:

- Lower cost as compared to commercial rates;
- Improvement in cash flow; and
- Greater control over the claims process.

Major factors the Workers' Compensation Agency considers in granting self-insured authority are:

- Demonstration of a good financial position;
- Claims history; and
- The ability to secure favorable excess insurance. Excess insurance covers losses—either single losses or combined (aggregate) losses—beyond specified dollar amounts.

Employers seeking self-insured authority must reapply annually. Self-insured authority is based on the agency assessment of the employer's financial ability to assume the workers' compensation liability and make compensation payments directly as they become due.

All self-insured employers are required to post a surety bond or a letter of credit. The minimum security is \$100,000. The actual surety or letter of credit amount for each self-insurer is based on the financial position of the employer, the liability to be assumed and the compensation loss history.

Self-insurers are also required to secure specific excess insurance and may be required to purchase aggregate excess insurance. Generally, employers with a net worth of less than \$20 million are required to secure aggregate excess insurance in addition to specific excess insurance.

Format and language of bonds, letters of credit, and excess insurance policies must be approved by the agency. Each self-insurer must contract with a agency-approved service company for claims handling unless the employer can demonstrate an in-house capability to administer claims. Multiple entities under one approval are required to execute a workers' compensation payment guaranty. The format of these guaranties is determined by the agency, based on the facts of each situation.

Group Self-Insured Programs

Any two or more employers in the same industry may join to form a self-insured group fund. Group members must have combined assets of at least \$1 million and be able to generate a gross annual premium of at least \$500,000, as well as meet other requirements.

There are more than 30 active self-insured groups in Michigan, providing workers' compensation coverage for 6,880 employer members. These groups have been very successful in saving money for the employer members. Certain groups have realized significant savings over commercial market rates. Other advantages of belonging to a group include:

- The ability to recover surplus premiums through state-approved distributions or discounts or credits on future coverage periods based upon surplus assets available.
- Self-government through an elected board of trustees.
- The ability to have greater control over the claims process.

For example, the 840 local governmental agencies of the non-profit Michigan Municipal League Workers' Compensation Fund receive underwriting profit and investment income in the form of a dividend. Dividends have been returned every year since 1979. Dividends amount to 20 to 30 percent of members' premiums, and rates continue to be very competitive with insurance company rates.

For more information on self-insured programs, contact:

Self-Insured Programs Division
 Workers' Compensation Agency
 Michigan Department of Energy,
 Labor & Economic Growth
 P.O. Box 30016, Lansing, MI 48909
 Phone: 517.322.1868
 Web site: www.michigan.gov/wca

RETROSPECTIVE RATING POLICIES: A DIFFERENT APPROACH

Under a retrospective rating plan, an employer's final premium is based on its actual loss experience during the policy period. The firm pays a basic premium upfront and agrees to pay a final premium somewhere between a previously agreed-upon range of minimum and maximum premium. The final premium will be within this range and will be based on the firm's actual losses for that policy period. It generally takes three years or more to determine the extent of actual losses and, therefore, the final cost of the policy.

For example, the insurer would calculate a standard premium. He/she then sets the minimum premium at 50 percent of that amount and the maximum premium at 125 percent. This means that the employer would pay at least the minimum premium, plus any actual losses beyond that amount, up to the amount of the maximum premium. If the actual claims surpass the maximum premium figure, the employer would have no liability for the excess amount.

If the employer's total losses are less than the standard premium, a refund is issued for the difference between the minimum premium and the standard premium. Obviously, this type of plan offers a strong financial incentive to minimize one's losses.

In a sense, a retrospective rating is a sort of hybrid between a traditional insurance policy and the self-insured program. In fact, some employers try a retrospective rating policy for a transitional period before deciding whether to self-insure. Retrospective plans offer larger businesses more cash-flow protection against big losses than a self-insured program. A retrospective plan is generally an option only for a business with an estimated annual premium of at least \$5,000.

This type of plan could have a very negative effect if the employer has a poor loss experience.

DEDUCTIBLE POLICIES

Deductible policies are becoming increasingly popular in workers' compensation insurance. Simply put, the policyholder (employer) takes on the portion of the risk below the deductible with the amount exceeding it to be paid by the insurer. In the event the employer fails to reimburse the carrier for the deductible amount, the carrier is responsible in full for the claims.

Policies in Michigan are written so that the insurance company pays and administers all claims, even those under the deductible amount. The employer then reimburses the insurer for all losses up to an agreed-upon deductible amount. This may be on a per accident (usually for small deductible policies) or aggregate basis (total of all losses in a policy year).

To qualify for these programs, an employer may be required to pay a substantial premium and demonstrate financial stability in order to cover the risk of the deductible amount. The carrier will often require security from the employer covering the deductible amount. This may be in the form of a cash deposit, surety bond or letter of credit.

THE WORKERS' COMPENSATION PLACEMENT FACILITY

Some employers are not able to obtain workers' compensation coverage from the open market. These employers usually involve hazardous or rarely occurring occupations, have a history of accidents, a measurable adverse loss ratio over a period of years or have demonstrated an attitude of non-compliance with safety requirements.

Since workers' compensation is mandatory, the state has established an insurance pool in which all the state's workers' compensation carriers share a portion of the cost of underwriting higher-risk clients. In 2008, Michigan's pool premium of \$52 million represented 5.1 percent of the total statewide workers' compensation market. This indicates a commitment on the part of Michigan's employers, employees and insurance providers to health and safety on the job.

Companies covered by the pool—known as the Workers' Compensation Placement Facility—usually pay substantially higher rates than the standard voluntary market. The Placement Facility is the market of last resort for employers who cannot obtain coverage through the voluntary market. In 2008, more than 16,000 employers bought coverage through the facility.

It is a popular misconception that only poor risk employers with negative loss histories are forced to buy coverage in the Facility. This is not true.

Only a small fraction of the Placement Facility policyholders are assessed a surcharge because they have a demonstrated accident frequency problem, have a measurably adverse loss ratio over a number of years or have demonstrated an attitude of non-compliance with safety requirements. The rest are usually new employers or companies that can benefit from a quick, generic premium formula, even if it is higher than they might be able to negotiate under other circumstances. The Placement Facility is an expensive alternative, however, and most employers will benefit significantly by insisting that their agents try to place them with the voluntary market.

For more information on the Placement Facility, see the Web site www.caom.com.

RIGHTS AS A MEMBER OF, OR APPLICANT TO, THE PLACEMENT FACILITY

Companies insured through the Placement Facility retain their rights to fair treatment. They have the right to request a formal hearing before the Facility's Board of Governors for either of the following:

1. Any alleged violation of the Facility's plan of operation.
2. Any alleged improper act or ruling of the Facility affecting premiums, assessments or the coverage furnished.

If a company disagrees with the Board's response, it may appeal its ruling to the State Insurance Commissioner who can either reverse or uphold the Board's ruling.