



Premium Rating Options for State-Fund Employers: “Making Sense of the Mess”

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In today's economic climate, employers must watch every dollar. This is especially true for smaller employers who may have less access to capital for operating their businesses. One potential budget-buster for a small business is the premium which must be paid to the State of Ohio for workers' compensation coverage. Thus, it is important to know what options are available to keep premiums as low as possible and allow a business to guard its financial bottom line. The purpose of this article is to lay out these options in a straightforward way and “make sense of the mess,” so that employers can determine what is in their own best interest when choosing among the programs offered by the Bureau of Workers' Compensation (BWC) that ultimately affect the amount of their premiums. Although most employers seek advice from third party administrators and others in making these choices, it is advisable that an employer have sufficient knowledge of the available options to verify the advice it is given and actively participate in the decision-making process.

Base Rating and Experience Rating

Premiums for all private state-fund employers are established using either “base rating” or “experience rating.” An employer cannot control the amount of its individual premium when it is base rated because it will pay the same premium regardless of its claims' experience. The term “experience” refers to the four-year window during which the compensation and medical benefits paid in all of the employer's claims are used to calculate its future premiums. The experience period is the oldest four

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of the last five years. Initially, premiums are base rated for two years after an employer obtains workers' compensation coverage, and the employer continues to remain based rated so long as it has less than \$8,000 in expected losses (paid compensation and medical benefits) during the four-year experience period. Beginning on July 1, 2010, an employer will need to have less than \$2,000 in expected losses to remain base rated. This will cause nearly 50,000 companies to lose base rating and become experience rated.

Based-rated premiums are established using occupational classifications and employer payroll. All occupations are divided into manual classifications based on their respective degrees of hazard, and each classification has its own base rate – the greater the degree of hazard, the higher the base rate. Premiums are then calculated by applying the base rate to each \$100 of an employer's payroll.

Unlike base rating, employers can control, to a certain extent, the amount of their premiums if they are experience rated through an emphasis on safety awareness and effective claims' management. Experience-rated premiums are based on an individual employer's claims' experience. Employers expected to incur \$8,000 or more in losses during the experience period (\$2,000 or more beginning on July 1, 2010) are experience rated. Employers with expected losses below this threshold are intentionally excluded from experience rating because a costly injury or occupational disease could result in an exorbitant increase in premiums for up to four years. Of course, employers who maintain below average claims' costs pay lower premiums than they would with base rating, but employers with above average claims' costs pay higher premiums. Currently, experience-rated premiums are based exclusively on total claims' costs without consideration of the number of claims. However, the BWC is in the process of developing a system for the 2011 policy year that sets premiums on the basis of both claim severity (costs) and claim frequency (number).

Group Experience Rating

An employer that is experience rated or base rated can join with other employers whose businesses are substantially similar to establish premium rates based on the claims' experience of the group as a whole. All members of a group must be in the same industry and cannot be a member of more than one group. Each group is sponsored by an organization like a local chamber of commerce or specific industry association, and there must be at least 100 individual employers in the group, or the combined premiums of the employers in the group must exceed \$150,000. The maximum premium discount an employer can receive by participating in a group for the July 1, 2010 policy year is 51%. The maximum discount was much higher in the past, but has been steadily decreasing over the last several years due to the BWC's desire to more equitably distribute premiums between group and non-group employers. Thus, group experience rating, while still attractive, is no longer as attractive an option as it once was.

BWC Programs Compatible with Group Experience Rating

1. The \$15,000 Medical-Only Program: An employer participating in this program pays up to \$15,000 in medical and pharmacy bills out of its own pocket. The employer cannot authorize or deny treatment, and its managed care organization (MCO), which is usually charged with the responsibility of paying these bills, cannot authorize treatment or pay the bills. As the name suggests, the program only applies to medical-only claims (claims with seven or less lost days from work), and once a claim becomes lost-time (eight or more lost days), it is no longer eligible for the program. By participating in the program, an employer can control the amount of its premium to a certain extent because the money paid out of pocket does not count toward the claims' costs in its experience for premium rating purposes. Participating employers have certain notice and recordkeeping requirements, and all bills must be paid within 30 days of receipt. Upon reaching the \$15,000 maximum, the MCO takes over processing the bills. The employer also has the option of removing a claim from the program, in which case the MCO assumes responsibility for bill payments. Of course, any bills paid by the MCO count toward the employer's claims' costs. An employer's participation in the program does not waive its right to contest a claim. However, there are a number of drawbacks to this program that do not make it a very attractive option, including the employer's inability to pay medical bills pursuant to the BWC's reduced fee schedule, additional recordkeeping responsibilities, and additional reporting responsibilities for Medicare purposes.

2. The Deductible Program: The BWC's Deductible Program is compatible with group experience rating (as well as the new Drug-Free Safety Program discussed below) only if the employer selects a deductible level of \$25,000 or more. Employers that are not group experience rated can participate in the program at any deductible level. An employer is responsible for claim costs up to its chosen deductible level for any claim that occurs during the policy year. Deductible levels range from \$500 up to \$200,000, but different levels have different requirements. Deductible levels between \$500 and \$10,000 cannot exceed 25% of the employer's annual premium, and levels between \$25,000 and \$200,000 cannot exceed 40% of the annual premium. Deductible levels of \$25,000 and \$50,000 require the employer to provide reviewed or audited financial statements for the three most recent fiscal years and, for the \$100,000 and \$200,000 levels, the employer only can provide audited financial statements. The BWC requires the financial statements because it must ensure that the employer has the financial ability to pay claim costs up to the chosen level. Employers participating in the program receive premium discounts depending on the deductible level – the greater the level, the higher the discount. Employers cannot participate in both the Deductible Program and the \$15,000 Medical-Only Program (or in the Group Retrospective Rating and Individual Retrospective Rating programs which will be discussed later).

3. The Drug-Free Safety Program (DFSP): On July 1, 2010, the BWC is rolling out its DFSP which is replacing its Drug-Free Workplace Program (DFWP) and Drug-Free EZ (DFEZ) program (which are currently in effect and will be discussed later). Unlike the DFWP and the DFEZ program, the DFSP is compatible with group experience rating. Thus, participating employers can receive both the DFSP premium discount and the discount for participating in the group program. While the DFSP retains many of the same elements as the DFWP, there are significant differences. Probably the most significant difference is the reduction in the percentage of available premium discounts. The range of discounts has been reduced from 10% to 20% down to 3% to 7%. Under the DFSP, employers that are not group experience rated will receive a 4% premium discount for participating in the program's basic level and a 7% discount for participating in its advanced level. Employers that are group experience rated will be able to receive a 3% premium discount in addition to their group discount if they participate in the advanced level. No additional discount is available for these employers for participating in the basic level.

Employers participating in either level of the DFSP must meet most of the same requirements which were part of the DFWP. In addition, the DFSP requires employers to conduct a safety review, provide accident analysis training for supervisors, submit timely accident reports and perform follow-up alcohol and/or drug testing for employees who are allowed to retain their jobs after a positive test (in addition to the other types of alcohol and drug testing required under the DFWP). To participate in the advanced level, an employer also must design and implement a safety action plan based on the results of the completed safety review, perform random drug testing of 15% of its average annual total workforce and pre-establish a working relationship with an employee assistance professional to whom employees can be referred for substance abuse assessments. The employer must pay for the assessment and, except in limited circumstances, cannot terminate an employee for a first positive alcohol or drug test.

Although the premium discounts are lower in the DFSP than in the DFWP, this is somewhat offset by the fact that participation in the DFSP is of unlimited duration. Unlike the DFWP, participation is not limited to five years. Thus, employers that have previously exhausted their eligibility to participate in the DFWP will now be able to participate in the DFSP.

BWC Programs Incompatible with Group Experience Rating

1. The One Claim Program: The One Claim Program is only available to state-fund employers who are being removed from group experience rating. To be eligible, an employer must have one significant claim enter its experience for the first time from what is called the "green year," which is the calendar year prior to a premium rate's July 1st effective date. (January 1, 2009 to December 31, 2009, would be the green year for a rate effective on July 1, 2010.) A significant claim has total costs which exceed the employer's individual expected losses for the policy year. The employer only can designate one claim as being a significant claim every four years and can remain in the program for this length of time. To maintain eligibility, the employer only can have up to three minor medical-only claims in its experience at the same time as the one significant claim. By participating in the program, the employer receives a 40% discount off its premium, but it must meet annual participation requirements, including attending two BWC-approved, all-day training courses.

2. Group Retrospective Rating: Employers participating in group retrospective rating pay their own individual premiums and then have the opportunity to later receive premium adjustments based on the combined claims' experience of the group. Depending on the group's performance, an employer can receive a premium refund or an additional premium assessment. Theoretically, this encourages employers within the group to practice effective workplace safety and claims' management so that each individual employer can pay lower premiums. However, the amount of an individual employer's premium is at the mercy of the safety record of other group members whose safety and claim practices may be less than desirable. Thus, group retrospective rating only makes sense for companies that are closely affiliated and share common safety and claim practices, thereby creating a level of accountability among the employers in the group.

Under this program, employers pay their usual experience-rated or base-rated premiums, and the premiums for all of the employers in the group are totaled. At the end of the policy year and for two consecutive years thereafter, the total of the group's premiums is recalculated based on the claims' costs, including reserves, incurred by the group during the policy year. If the recalculated total is lower than the original total, employers in the group receive a premium refund. If the recalculated total is higher than the original, employers in the group are charged an additional assessment. The amount of an individual employer's refund or assessment is determined by its percentage of the original total. A group can choose to cap the amount of additional premium its employers may have to pay, but this reduces the amount of any potential premium refund (the higher the chosen cap, the greater the potential refund and vice versa). Employers cannot participate in group retrospective rating and also participate in the One Claim Program, \$15,000 Medical-Only Program, Deductible Program or DFWP (or in individual retrospective rating which is discussed below).

3. Individual Retrospective Rating: Individual retrospective rating is a blend of experience rating and self-insurance. The program allows an employer to earn a possible premium reduction in exchange for assuming a portion of its claims' risk – the greater the risk taken, the greater the possible reduction. To qualify for the program, the employer must submit audited financial statements and meet stringent financial requirements, and meet BWC-mandated safety requirements. The employer also must have an estimated annual experience-rated premium of at least \$25,000 to be eligible, but the program may be better suited to larger employers that pay over \$100,000 in annual premiums.

When applying for the program, the employer selects a claim limit of \$100,000, \$125,000, \$200,000, \$300,000, \$400,000 or no claim limit and also selects a maximum premium percentage of 150% or 200%. Based on these selections and the employer's estimated annual premium, a minimum premium percentage is assigned. The employer pays its premium to the BWC just as it would have paid its experience-rated premium, but the premium is reduced by the minimum premium percentage. Upon completion of the policy year and annually throughout a 10 year evaluation period, claim costs for claims incurred during the policy year are tracked and billed to the employer up to the maximum limits selected (claim limit and maximum premium percentage). At the end of the 10 year evaluation period the BWC submits a final invoice to the employer that can include any outstanding reserves.

To illustrate, an employer with a \$300,000 experience-rated premium chooses the \$100,000 claim limit and the 150% maximum premium percentage. These choices result in a minimum premium percentage of 50%. The employer would initially pay a premium of \$150,000 based on the 50% minimum premium percentage. The BWC would then bill the employer for claim costs incurred for the next ten years, but could not bill the employer more than \$100,000 for any claim, or more than \$450,000 for the policy year. If the employer incurred \$50,000 in claim costs for the year, it would save \$100,000. If it incurred \$200,000 in claim costs, it would lose \$50,000.

4. The Drug-Free Workplace Program (DFWP): As noted above, the DFWP is being phased out as of July 1, 2010, but many of its elements will be required for the new DFSP. The DFWP requires participating employers to develop a written substance policy describing their DFWP program, including provisions on employee education, supervisor training, drug and alcohol testing, and employee assistance. Employers also must perform pre-employment drug testing, reasonable suspicion drug and/or alcohol testing, post-accident drug and/or alcohol testing of involved employees, and return-to-work testing. Employers could participate in the program at one of three levels. In addition to the Level I requirements just noted, Level II required random drug testing of 10% of an employer's average annual total workforce, and Level III required 25% random drug testing. Employers participating in Level I received a 10% discount on their premiums, Level II participants

received a 15% discount, and Level III a 20% discount. However, while premium savings for participating employers could be substantial, eligibility was limited to five years. Employers could participate in the DFWP and group experience rating, group retrospective rating or individual retrospective rating, but in these circumstances the DFWP did not result in any additional discount over and above the benefits of the specific rating program.

The BWC also offered the Drug-Free EZ (DFEZ) program to companies with no more than 25 employees. The same premium discounts were available depending on the level of participation. The DFEZ program had fewer requirements than the DFWP, but like the DFWP, the DFEZ program is being phased out as of July 1, 2010.

5. The Safety Council Rebate Program: Through this program, employers can receive a 2% premium rebate for meeting all participation eligibility requirements, and also can receive a 2% performance bonus for reducing either claim frequency or claim severity. Employers with no claims also can receive the 2% performance bonus. To receive the 2% rebate, an employer must attend 10 safety meetings or events during the program year, at least eight of which must be safety council meetings, the employer’s CEO must attend at least one safety council meeting or function, and the employer must submit semi-annual reports detailing its claim activity. Employers can earn the additional 2% performance bonus by demonstrating a reduction in claim frequency or severity of 10% or more below the previous year’s frequency or severity.

Conclusion

In the past, if an employer qualified for group experience rating, it was usually a no-brainer. Premium discounts for being group rated were usually substantial, and the employer could “stack” other discounts, like the DFWP discount and safety council rebate and performance bonus, on top of its group discount resulting in significant savings. Thus, for most employers, it made no sense to not be in a group, and it took little analysis of the BWC’s various options to make that determination. However, times have changed. Group discounts are no longer at the levels that they once were and may continue to decline, and the BWC stopped permitting the stacking of certain discounts on top of an employer’s group discount. Thus, while inclusion in a group generally is still the best way for employers to save on their premiums, it is no longer as universally so, and more investigation is needed before the decision to join a group is made. Employers that are not able to qualify for higher group discounts may find they are better off being experience rated as an individual employer with the ability to obtain discounts which are not available to group-rated employers.



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