

Understanding your premium

You control more than you may realize; here's where to look

An employer once said her work comp premium is like bread dough. It keeps rising until you poke it.

She took one poke at it by getting company managers to collaborate in finding light-duty jobs for recuperating employees who otherwise would sit home. She took another poke at it by assigning safety director duties to a supervisor whose work load had shrunk.

For many employers, workers' compensation premiums have been rising over the years. They're wondering why and what they can do to slow the ascent.

The answers lie in understanding, first, your premium and, second, your workplace.

The second item, understanding your workplace, relies mostly on your own management capabilities and any outside resources you enlist, such as loss prevention experts.

The first item, understanding your premium, starts with a look at your "premium description." That's the section of your policy's Information Page that lists and adds up the components of your annual workers' compensation premium billing.

Your "premium description" mirrors your business. Along with some constants are a lot of variables, including payroll, types of jobs, adjustments for your claim costs in the past, and adjustments for your risk of incurring claim costs in the future.

Changing things in your business will change things in your premium description. That's key.

The constants, of course, are parts of your premium you can't change. They respond to state and national trends, and some of those trends lately have been carrying high price tags.

An injury that happens today will cost considerably more than the same injury just a few years ago. Notable among the cost-drivers:

Steeply rising medical costs. New surgery techniques and more frequent major surgeries have raised medical costs but not necessarily outcomes, at least not in workers' compensation benefit cost savings. Prescription drugs costs have been rising at double-digit rates for many years, and the use of expensive pain management drugs continues to grow. Medical complications are on the rise, including higher rates of infection and diabetes. Hospital costs are high and, by law, workers' compensation pays at higher rates.

More pre-existing conditions. Especially obesity, diabetes and an aging workforce. These are contributing to the frequency and severity of injury and slowing recovery.

More social complications. Chemical dependency, mental health, family problems, and histories of violence are impacting and complicating a greater proportion of claims.

Side note: Though social complications and pre-existing conditions are mentioned here in the what-you-can't-control list, some employers are helping address these risks with innovative wellness and employee assistance programs.

State taxes and surcharges. The Minnesota Special Compensation Fund assessment is the largest single state surcharge on workers' compensation coverage, typically amounting to roughly 9 percent of an insured employer's annual premium.

These are some of the big factors driving workers' compensation costs and, hence, premiums—even for employers with good track records.

Except for the SCF assessment, most of these cost factors along with others are built into the workers' compensation rates applied to your payroll.

The 'rate' multiplier

A different rate is applied to each of the job classifications in your payroll, as you can see on your policy's Information Page. In the illustration on page 3, the rate for Automobile Service Or Repair employees is \$4.36 per \$100 of payroll. The rate for Clerical Office is \$0.26 per \$100 of payroll.

Each rate reflects the risk associated with the type of job. Determining the dollar values of each job's risk starts with the Minnesota Workers' Compensation Insurers Association.

The MWCIA collects statewide payroll and claims data from all workers' compensation insurers doing business in the state. Annually, it distills the data into dollar amounts for each of Minnesota's 300 or so job classifications. The dollar amount reflects an estimated average cost of medical and wage-replacement benefits for a worker in that job class.

Subject to Minnesota Commerce Department review and approval, each workers' compensation insurer

adjusts these dollar amounts to cover taxes, claims management and other operating costs not covered in the MWCIA data.

The rates produced annually through this process are the main multipliers for the first step in calculating your estimated premium.

But rates are only part of the picture. And it's the rest of the picture that holds a world of opportunities for you to lower your final premium cost—or raise it—depending on what you choose to do.

The rest of the picture will look the way you paint it: your successes in making good hiring choices, practicing good employee relations, preventing injuries, getting recuperating employees back to work early, doing what you can to help control your claim costs—or, conversely, your lack of attention to those.

Your e-mod

These successes or shortcomings are mostly wrapped up in your “experience modification factor.” Your e-mod is your greatest long-term opportunity to reduce your annual premium costs.

Your e-mod compares your organization's workers' compensation experience to the experience of other businesses similar in size and types of jobs. An e-mod of 1.00 is exactly average for your industry. If your e-mod is less than 1.00, then your losses are less than your industry's average.

Your e-mod is another key multiplier in calculating your premium, so the lower your e-mod, the better. A 0.80 e-mod compared to a 1.20 e-mod can make a substantial difference in your final premium cost. It also indicates you're doing better than your competitors.

Monitoring and improving your e-mod is usually well worth the effort. Consider two approaches.

One is doing more to prevent injuries from happening in the first place. Generally the most productive place to start is analyzing your organization's recent history of work injuries. You want to find the patterns showing where you can get the most out of investing your injury prevention resources.

The second approach is reducing the costs of injuries that do happen. For example, you can work with a recuperating worker to return him to a lighter-duty, lesser-pay position as soon as medically possible rather than waiting until he's fully recovered. That can make a dramatic difference in the impact of the injury on your e-mod and, hence, on your premium.

Your successes today in reducing injuries and claim costs won't show up in your next policy year's e-mod. But they will show up in your e-mod the year after, and they'll stay there for three consecutive years. That's because by law your e-mod calculation includes three years of claim costs, excluding the most recent policy year.

The lingering effects of the three-year timeframe are painful for negligent employers who let loss prevention slide and whose claims run higher than they should be. On the other hand, by

monitoring your e-mod and diligently taking steps to improve it when needed, you can use the three-year timeframe to your continuing financial advantage, and it will soften the impact of an unusual major claim or even an unlucky year.

Improving your e-mod will also soften the impact of rates that, as mentioned earlier, are being driven up by factors outside your control.

What your underwriter looks at

While your efforts and successes today in reducing claim costs won't show up in next year's e-mod, they'll start having an impact on next year's premium anyway.

To see why, and to see how this mixes together with other activities and characteristics of your organization, look closer at what your SFM underwriter needs to gather up about you.

To determine the pricing for your next policy period, your underwriter gathers information about any anticipated changes in payroll, because that's a primary basis for your premium calculation. He also reads SFM's database files and talks with SFM staff and your insurance agent about you:

Losses and loss history: For instance, your frequency and severity of injuries. The causes of injuries and your role as employer, such as enforcement of rules. Whether the jobs in your organization have unusual characteristics that increase or decrease the risk of injury compared to other similar businesses SFM insures. Whether a claim is a rare occurrence for you. Whether you tend to have good years and bad years and how they average out. How your premium aligned with your claims costs in the past year, and whether your premium levels over time seem to be in line with your overall claims costs.

Claims resolution and return-to-work: Whether you do your part to resolve claims early on and work to get employees back on the job. Frequency of complications and litigation. Whether factors such as a slowdown in your business are negatively affecting claims costs and return-to-work, or might in the future. Whether you report claims on time. Improvements you've initiated, like a more aggressive return-to-work program.

Loss prevention: Your level of commitment and activity. The kind of “safety culture” you foster. Management approach. Whether you've followed through on recommendations by SFM loss prevention representatives. Whether any changes in your operations, such as automated processes or new equipment, reduce the risk of injury. Whether other new initiatives, such as safety measures, training programs and hiring practices, reduce the risk of injury.

Other: Whether you pay premium billings on time, thereby avoiding the administrative expense of processing and sending cancellation notices. Special problems, such as independent contractor issues.

That's a keyhole look at what your underwriter takes into account at renewal time. It includes any recent efforts you've undertaken to prevent injuries or reduce claim costs. Depending on how it all balances out, your underwriter may reduce your

What goes into your premium calculation

‘Classification description’ and ‘Class code’

Identifies the kind of work your employees do.

Where it comes from

The state of Minnesota has adopted more than 300 job classifications and corresponding classification codes. These classifications group workers with similar activities and risks.

‘Premium basis: total estimated annual remuneration’

Your payroll for each job classification is estimated, or projected, for the 12-month policy period ahead.

To be updated later

After your policy period has ended, an SFM auditor will ask for actual payroll amounts.

‘Rate per \$100’

The amount of premium for each \$100 of payroll.

Two components to ‘rate’

(1) “Pure premium” is calculated by the Minnesota Workers’ Compensation Insurers Association and reflects the risk of indemnity and medical losses based on statewide historical data. (2) A “load factor” is determined by each individual insurer for taxes and assessments, and claims administration and other operating expenses.

‘Estimated annual premium’

Your premium is estimated, or projected, at the beginning of the policy year. Actual premium is determined at the end of the policy year by an audit.

How it’s calculated

Simple math: Multiply “Total estimated annual remuneration” times “Rate,” then divide by 100.

‘Experience modification’

Compares your work comp experience to that of other businesses similar in size and types of jobs. A rating of 1.00 is exactly average for Minnesota businesses like yours. Below 1.00 is above average. It’s used here as a multiplier.

Where it comes from

The Minnesota Workers’ Compensation Insurers Association recalculates your e-mod annually about 90 days prior to your policy renewal date.

‘Premium discount’

Recognizes that the expense of servicing larger-premium policies is less, relatively, than for smaller-premium policies.

How it’s calculated

Figured on a sliding scale and applied to premium in excess of the \$5,000.

Classification Description	Class Code	Premium Basis Total Estimated Annual Remuneration	Rate per \$100 of Remuneration	Estimated Annual Premium
Automobile Service Or Repair	8380	188,000	4.36	8,197
Clerical Office Employees Noc	8810	20,000	0.26	52
Experience Modification	9898		0.99	-82
Premium Discount	0063			-288
Expense Constant	0900			180
Total estimated annual premium				\$8,059
State of Minnesota Special Comp Fund Assessment	0174			605
Total estimated cost				\$8,664

‘Expense constant’

A set charge applied to every policy. Covers expenses common to all work comp policies regardless of premium size, such as as issuing, recording and auditing.

‘State of Minnesota Special Compensation Fund assessment’

Used to be built into the “Rate per \$100.” Now itemized separately, per state law. The amount is calculated based on your “pure premium.”

What does it pay for?

Administered by the state Department of Labor and Industry. Pays for benefits to injured workers of uninsured employers and certain low-wage workers. Also pays for operating the state’s work comp system, including judicial and regulatory costs.

Other adjustments may go into customizing the premium

- **Schedule credit.** Premium reduction that recognizes things that reduce risk, like new safety initiatives.
- **Schedule debit.** Premium surcharge that recognizes such things as jobs with unique characteristics making them more hazardous than average for their classification group.
- **MCPAP credit.** The Minnesota Contractors’ Premium Adjustment Program reduces the premium of a contractor paying above-average wages in certain job classifications. Applications for the MCPAP credit are mailed in January to eligible contractors.

premium accordingly by allowing a “schedule credit” of, say, 5 to 10 percent.

Over the months ahead, your efforts will take hold and begin producing fewer injuries or lower claim costs. By the time your policy renewal comes around a year later, those results will be showing up in your e-mod. The initial up-front credit will go away since it’s no longer needed in order for your premium to reflect your good work.

For some employers, the considerations taken into account by the underwriter balance out to an overall negative, and a “schedule debit” is assigned raising the premium. Some overriding factor is often the cause: atypical risks inherent in your operations, for instance, or unexpectedly large claims costs during the past policy year.

If your premium description shows a schedule debit, regard it as a red flag. You need to find out why and what, if anything, you can do to reduce or even eliminate it in future years.

Bottom line

Your premium is a level of pricing that reflects your risk. SFM generally looks at pricing and risk not just one year at a time, but over the long term. That makes long-term relationships important, whether for the employer with several claims a year or the employer with but one big claim in 20 years.

Your pricing is determined by a recipe of factors. Some you can’t alter and, in times like this, they’ll push pricing up. Others you can do a whole lot to alter and, if you make the committed effort, you’ll help offset the upward pricing push.

Two other resources to read are the “E-mods” and “Understanding your losses” CompTalks containing more extensive explanations and best practices. Order or download them from the “Resource catalog” on SFM’s website, www.sfmic.com.

Five best practices to control your premium

1. Build injury prevention into everything you do.

Whenever making changes in any aspects of your business’ operations, keep injury prevention in mind. Buying equipment or office furniture? Be sure it is ergonomically adjustable. Building a new facility? Find out what safety advances you should be incorporating, and apply what you should have learned from your own business’ past experience.

2. Take specific steps to control workers’ compensation costs.

Focus on transitional or lighter-duty jobs to improve the results of your return-to-work efforts, keeping lost-time claims within the waiting period whenever possible. Report claims right away.

Figure out what your best lost-control opportunities are by using the same loss history runs your SFM underwriter uses, available from your SFM loss prevention representative or through CompOnline. Fire up your loss prevention program by firing up your safety committee, educating your employees and evaluating their workspaces.

Learn from past accidents and injuries. Develop a wellness program.

Be especially vigilant in tougher economic times to things that might increase the frequency or severity of reported injuries.

3. Monitor your e-mod.

It’s your biggest opportunity to gauge your long-term performance and control your premium. Your e-mod should never be greater than 1.00.

4. Talk to your agent.

Be sure your agent understands your organization, your efforts to control losses, and what you anticipate in the months ahead. Your agent is an important source of information for your SFM underwriter.

5. Make good employee practices a priority.

Tune in to employee concerns. Deal with performance problems promptly and separately from workers’ compensation issues.