

MAINE STATE LEGISLATURE

The following document is provided by the
LAW AND LEGISLATIVE DIGITAL LIBRARY
at the Maine State Law and Legislative Reference Library
<http://legislature.maine.gov/lawlib>



Reproduced from scanned originals with text recognition applied
(searchable text may contain some errors and/or omissions)

REF
C-2



MAINE STATE LEGISLATURE
Augusta, Maine 04333

Report of
BLUE RIBBON COMMISSION
TO EXAMINE ALTERNATIVES TO THE
WORKERS' COMPENSATION SYSTEM AND TO
MAKE RECOMMENDATIONS CONCERNING
REPLACEMENT OF THE PRESENT SYSTEM

August 31, 1992

Members:

Richard B. Dalbeck
William D. Hathaway
Emilien A. Levesque
Harvey Picker

Augusta, Maine

STATE LAW LIBRARY
AUGUSTA, MAINE

AUG 31 1992

LIBRARY USE ONLY

FINDINGS OF THE MAJORITY OF THE BLUE RIBBON COMMISSION ON WORKERS' COMPENSATION

The Blue Ribbon Commission's review of the Maine worker's compensation system makes several points quite clear. The most important is that due to recent changes, the benefits provided are now coming closer to those found in other states. In the past Maine's workers' compensation law provided a benefit package that was significantly greater than those in other systems. Currently this is true in only two respects. Maine's maximum weekly benefit is higher than those in most states, in terms of its dollar amount and its relationship to the statewide average weekly wage. The duration of benefit entitlement in the majority of cases is also greater than in most but not all states, particularly for cases involving lower levels of impairment. Both the replacement rate for lost income and the benefit duration for very serious cases are similar to that used in the majority of states.

Procedurally the system is quite similar to the systems in the rest of the country, again with two exceptions. Employers are required to pay employees' attorneys' fees, and under some circumstances are required to obtain approval from the Commission before benefit payments can be modified or terminated. Both of these provisions can be found in a few other states, but not in most.

However, it is also clear that the Maine workers' compensation system is utilized in a different manner than virtually every other state's system. There is little question that Maine employees use the system more frequently than do employees in other states and stay in the system longer. The reasons for this are not clear.

Some believe that the problem springs from the failure of Maine employers to pay enough attention to safety and their lack of willingness to help return injured workers to the work force. Others blame the insurance industry for not handling claims properly. The Workers' Compensation Commission and the courts have been criticized for resolving disputed cases in a manner that increases utilization and costs. It is also argued that there exists in Maine what is described as a workers' compensation culture that leads people to use the system more often and longer than in other states, beyond that which is justified by the actual frequency and severity of the work-related injuries and diseases.

The information necessary to resolve these disagreements if not available and much of the debate is based on points of view rather than facts. This is unlikely to change, at least in the short term. More importantly, we do not find it helpful to belabor these issues. The future of

the Maine workers' compensation system lies with all of the people of Maine, employers and employees alike, and responsibility or blame cannot be left with any one segment of the community. What is needed is a major change in attitude, coupled with the adoption of a benefit structure and an administrative process that will permit the system to operate in a manner that meets the legitimate needs of the people of Maine.

The plan that is being offered places control of the system in the hands of a new labor-management board, which will have virtually total control over the operation of the system. The Board will have the ability and the responsibility to see to it that the system operates as intended, and that any problems that arise can be quickly and accurately identified and dealt with.

We expect that there are those who will believe that the proposal does not go far enough in cutting benefits, while others will complain that it goes too far. The fact is that the most significant benefit reduction, limiting the duration of benefits for those with permanent impairments that do not exceed 15% of the body, is matched with an increase in duration for those with impairments greater than 15%. We believe that the system can afford to provide greater benefits for those who are seriously injured, but that unless other aspects of the system, particularly utilization, are brought under control, it cannot afford long-duration benefits for most others.

This proposal will support the work of those who believe that cooperative efforts between employers and employees will reduce utilization of the system and its costs. If they are correct, costs to employers will be reduced far more than the actuarial predictions attributable to the proposal. In addition, benefit entitlement will increase, since the proposal provides for an automatic increase in duration should the Maine system be brought in line with those in other states. In the meantime, we have provided for the possibility that the 15% threshold may create a real hardship for some injured employees. The Board will have it within its power to extend benefit the duration in appropriate cases.

There is another unresolved disagreement that is of significance: the cost of the system with regard to insurance rates and the residual market mechanism deficit. Rates are alleged by some to be inadequate, while others argue that insurance carriers are making money in Maine. Residual market deficits are blamed on inadequate rates or on poor claims handling practices. Once again, we cannot resolve these issues with certainty and find no reason to do so at this time.

The proposal gives all of the workers' compensation system's participants a chance to demonstrate where the truth lies. Insurance carriers will be given great latitude in setting their rates, which should eliminate

excuses for not writing more voluntary business in Maine. The residual market mechanism will become self-supporting, and will be run by the same policyholders who will have to pay its costs. It will be up to the self-insured groups and the new mutual insurance organization to provide a competitive market, to insure that the rates charged by private carriers are not excessive. Since self-insurance and the residual market mechanism now provide coverage for the overwhelming majority of employers, the self-insured employers and the new mutual company are in a position to significantly influence rates in the entire market.

What this Commission has done is to put the new Workers' Compensation Board, and through it the entire community, in a position to deliver a system that will provide substantial protection for workers who have suffered work-related injuries and diseases, at an affordable cost to employers. What we cannot do is guarantee that anyone will take advantage of this opportunity. If the parties so desire, the system can be operated in a manner that will provide injured workers with high-quality medical care, prompt delivery of benefits, and the income support that they require as the result of their injuries. This can be done at a cost no greater than the median cost among states. Both objectives are equally important. How well they are achieved is dependent on those who carry out the law.

In preparing these findings and the proposal we have relied upon an actuarial analysis from Milliman and Robertson. Summary of the actuarial report is attached as part of these findings.

REPORT TO THE MAINE BLUE RIBBON COMMISSION

Prepared By: John Herzfeld, FCAS, MAAA

Date: August 27, 1992

BACKGROUND

The Maine Blue Ribbon Commission (the "Commission") was created by an act of the Maine legislature in 1992. Their mission was to propose changes to the Maine Workers Compensation system to reduce costs and to allow the system to function more efficiently. Milliman & Robertson, Inc. ("M&R") was retained to assist the Commission and help with estimating the cost impact of the proposed legislation.

SCOPE

The Commission has developed a bill that adopts many of the key features of the Michigan Workers Compensation system. A number of the Michigan provisions were revised in order to reflect considerations particular to the state of Maine.

The Commission has asked M&R to assist their consultant, John Lewis, by providing cost estimates of the changes proposed to the Maine system. M&R's primary role was to focus on changes that are measurable using statistics available from various sources including historical workers compensation costs in Maine.

This report will discuss our findings and our approach to estimating the cost impact of the Commission's bill. In addition, we will discuss the major assumptions behind our analysis. Due to the limited time frame between the drafting of the bill and the date of this report, we were unable to analyze all of the features of the proposed bill.

LIMITATIONS

A complete rewrite of a workers compensation statute is particularly difficult to price. As direct and indirect participants in the system i.e., claimants, attorneys, employers, medical providers, administrators, insurers, and others, adapt to the new system, their behavior will change. Behavioral changes are likely to take place over a number of years and are difficult to identify and project. This adds to the uncertainty of our estimates.

Any major legislative change brings with it a large number of changes that cannot be readily quantified, due to the lack of available data. These include changes in administration, i.e., will claims be resolved faster, will fewer claims be disputed, changes in legal interpretations, i.e., will provisions of the new law be litigated, changes in behavior, i.e., will injured workers return to work faster, etc. This report quantifies those changes where statistical data is available to support our actuarial estimates. Actuarial projections are normally based on historical data which are projected to the future under the proposed system. Those areas where we cannot perform an actuarial analysis are commonly referred to as "soft costs". This is not to imply that they will have no impact, or that given more time and data, a reasonable range of their estimated impact could not be developed. To price many of these items would involve obtaining additional data from various sources, including surveys of administrators, attorneys, claims handlers, employers, and other parties. Time did not permit such extensive research. Instead, this report will focus on the issues that can be quantified in a relatively accurate manner using data and

information readily available from the insurance industry, the state of Maine, and internal to M&R.

All projections of future costs are subject to uncertainty. This uncertainty can arise from unexpected changes in economic conditions, rates of inflation, claimant behavior, employer behavior, and changes to the legal system, and other sources. We relied on data provided by the National Council on Compensation Insurance ("NCCI"), the Maine Bureau of Insurance, and other sources. We did not audit this data.

FINDINGS

Based on an analysis of those areas where actuarial data and statistical information is available, we project that the Commission's proposed bill will reduce costs approximately 12%. This 12% value is a preliminary estimate and may move upwards or downwards as continued analysis is undertaken.

Our estimated cost impact by type of injury is shown below:

<u>Injury Type</u>	<u>Estimated Percentage Change in Losses</u>	<u>Estimated Total System Impact</u>
Fatal	-50%	-1%
Permanent Total	-50%	-1%
Permanent Partial	-12%	-5%
Temporary Total	- 7%	-1%
Medical	- 7%	-3%
Total Loss Savings	-11%	-11%
Loss Expense Savings		- 1%
Grand Total		-12%

These savings are estimates of the reduction in losses expected from the proposed legislation. They are not premium reductions. These are factors to be applied to an otherwise adequate rate level. In other words, if current rates are exactly adequate,

then this -12% savings would lead to a -12% rate reduction. However, if current rates were inadequate by, for example 20%, then the combined effect of the rate level inadequacy and the proposed legislation would lead to a rate change of +5.6% ($.88 \times 1.20 = 1.056$)

The following are the key components of the bill that we have analyzed:

1. The basis of compensation is changed from 66 2/3% of gross wage loss to 80% of "spendable" wage loss, also called net wage loss. We estimate that this change accounts for approximately a 2% total cost decrease, out of the 12% total cost decrease figure cited above.
2. The maximum weekly benefit amount is changed to \$441 or 90% of the statewide average weekly wage, whichever is greater.
3. The durational limit for permanent partial cases is changed to 260 weeks of total benefits, unless the impairment, measured relative to the whole body is greater than 15%, in which case lifetime benefits (actually, benefits for the duration of wage loss) are allowed. In hardship cases, the 260 week limit can be extended.
4. The periodic escalation of benefits for permanent total disability and death cases is removed.
5. Death benefits are generally limited in duration to 500 weeks.

6. The waiting period for total benefits was changed from 3 days to 7 days. The retroactive period (i.e., the required duration before the worker can recoup the benefits lost from the waiting period) will remain unchanged at 14 days.

7. Under the proposed legislation, the claimant's attorney must now be paid by the claimant, whereas under current law, the claimant's attorney was paid by the employer (insurer).

8. Provisions regarding Independent Medical Examiners are changed.

9. The dispute resolution mechanisms are changed.

APPROACH

The pricing of workers compensation benefit changes always starts with a distribution of how benefit dollars are currently being spent. Then, various models are constructed for each injury type which measure the average costs under the current law and under the proposed law.

The current distribution of losses that we used is shown below:

<u>Injury Type</u>	<u>Percentage of Losses</u>
Fatal	1.6%
Permanent Total	2.7%
Permanent Partial	44.8%
Temporary Total	10.9%
Medical	40.0%

This distribution is based on information from the NCCI and reflects estimates based on the current Maine benefit structure.

We note that the injury types listed above are based on the way NCCI categorizes claims and may not exactly reflect the names of the benefit categories as classified in the statute. However, this classification scheme is practical and it allows interstate cost comparisons to be made.

In the following sections we will discuss each of the injury types and how we estimated the expected impact of the proposed legislation.

Medical

Currently both Michigan and Maine have medical fee schedules in effect. The purpose of a medical fee schedule is to limit the charges for certain medical procedures. The proposed legislation intends to replace Maine's current medical fee schedule with a fee schedule similar to that currently in place in Michigan. In order to price a medical fee schedule change, it is necessary to have a very detailed and credible data base which contains the frequency with which the most common medical procedures are performed. Given such a data base, it is basically a mechanical task to estimate the cost change of moving from one medical fee schedule to another.

The NCCI has estimated the cost impact of adopting the Michigan medical fee schedule in Maine to be a savings in medical costs of approximately 5-10%. Their analysis indicated that Maine's medical fees are approximately 7% higher than Michigan's. Therefore, the estimated cost reduction is approximately $1/1.07 = .935$ or a 6.5% savings. We have selected a 6.5% savings to

reflect the revised medical fee schedule. Since medical costs are approximately 40% of total costs, the 6.5% savings on medical translates to approximately a 3% reduction in overall costs. However, the exact impact of the revised medical fee schedule depends on the cost limits that eventually are implemented. In addition, we have not adjusted for any impact of changes in programs aimed at controlling or monitoring medical utilization.

Temporary Total

Temporary total injuries are those cases where the injured worker is out of work for a short period of time, but on his/her return to work there is no permanent impairment and no wage loss. The cost of temporary total injuries is impacted by the dollar amount of the wage loss and the duration of the wage loss.

The average weekly benefit will change due to the change in the basis of compensation (66 2/3% of gross wages versus 80% of net wages), and the change in the maximum weekly benefit. We estimate that the change in the average weekly benefit will reduce temporary total costs approximately 2.7%.

The change in waiting period will impact the frequency and the average duration of temporary total claims. We estimate that the change in waiting period will reduce temporary total costs approximately 4.7%. Therefore, the overall impact on temporary total is estimated as $.973 \times .953 = .927$ or a reduction of approximately 7%. Since temporary total costs are approximately 10% of total injury costs, the 7% savings on temporary translates to approximately a 1% reduction in overall costs.

Fatal

Fatal benefits consist of a flat sum for burial expenses and a set of annuities to the various survivors. Under the proposed legislation, the cost of fatal benefits will be impacted by some changes in eligibility for fatal annuities, the duration of the annuities, and the average weekly benefit (discussed above in temporary total). Briefly, the current Maine system allows lifetime benefits to spouses (who do not remarry) while the proposed Michigan system generally limits these benefits to 500 weeks. In addition, there are various changes in presumptions of dependency. We have estimated the impact of these provisions and also, we have reviewed calculations performed by NCCI. Based on this analysis, we have selected an estimated cost reduction on fatal cases of -50%, which corresponds to a reduction in overall costs of -1%.

Permanent Total

The cost of permanent total benefits is impacted by the duration of the benefits and the cost of the benefits. Currently, in Maine, permanent total cases have lifetime benefits and are eligible for escalation on the third anniversary of the date of injury. In the proposed legislation, escalation of permanent total benefits would be eliminated. The presumption of permanent and total incapacity in the proposed legislation will last for 800 weeks. In addition, the average weekly benefit (discussed above in temporary total) will also change. We have estimated the impact of these provisions and also, we have reviewed calculations performed by NCCI. Based on this analysis, we have selected an estimated cost reduction on permanent total cases of

-50%, which corresponds to a reduction in overall costs of -1%.

Permanent Partial

These cases form the single biggest dollar block of benefits in the current Maine system. As noted above, we estimate that approximately 45% of benefit dollars are expended for permanent partial injuries. Therefore, changes to permanent partial benefits can have a large impact on overall system costs.

Permanent partial injuries are typically analyzed separately for major permanent partial injuries and minor permanent partial injuries. In Maine, most of the interest and focus is on major permanent partial injuries, since these account for approximately 95% of all permanent partial costs and 42% of all benefit costs.

The model for evaluating permanent partial benefits consists of three major components. These are the healing period, the impairment benefit, and the partial wage loss benefit. These three components are financially the most significant. Other adjustments are made to reflect vocational rehabilitation benefits and other offsets, but these adjustments are not as significant as the first three components.

We will discuss our analysis of the healing period, the impairment benefit, the partial wage loss benefit, and other adjustments in the sections below.

Healing Period

The healing period represents the length of time that the injured worker is out of work completely and is receiving total wage loss benefits. Healing periods in Maine have historically been rather long, much longer than average healing periods observed in other states. Recent NCCI data showed that the average healing period in Maine for major permanent partial injuries was over 160 weeks. The NCCI's countrywide model for major permanent partial injuries is based on a healing period of 36 weeks. The current rate level in Maine is based on an assumed 120 week healing period for major permanent partial injuries. These assumed reductions in healing period are based on the legislative changes enacted in 1987 and 1991.

We have assumed no change in the healing period in Maine for the proposed legislation. While we can optimistically hope that reductions will be achieved, based on our approach to "soft costs", it seems to be appropriately conservative to wait and see. If such reductions are attained, then losses will decrease, and the improved experience should be reflected in future rates.

We have reflected a change in the average weekly benefit for the healing period, but we have assumed that the healing period duration would remain unchanged.

Impairment Benefit

The impairment benefit is typically a scheduled benefit based on the type of injury. In Maine, an impairment benefit is currently available based on a percentage rating developed from the AMA Guides. However, since 1991, these impairment dollars are offset by other benefit dollars. The net effect is that the impairment benefits are reduced significantly for the vast majority of claimants. Under the proposed system, impairment benefits would only be available in a small percentage of the cases where there was loss of a limb, or finger, etc. We have reflected these changes in our model.

Partial Wage Loss Benefits.

Currently, in Maine, permanent partial benefits are limited to a total duration of 520 weeks (including healing period). The proposed legislation encompasses a 260 week limit for injuries that result in an impairment, measured as part of the whole man, of 15% or less, and an unlimited duration for cases with an impairment of greater than 15%. For some special cases with less than 15% rating, the duration can be extended.

The pricing of these wage loss benefits involves estimating the average weekly benefit under the current and revised

benefit structures, and estimating the current and revised average duration (discounted for mortality, interest, and improvement in earning capacity). In our model, we assume that approximately 35% of the major permanent partial cases would have impairment rating of over 15%.

Other Adjustments

Under the proposed legislation, permanent partial benefits will be offset by social security retirement benefits and various other disability and retirement benefits. Our model also reflects adjustments for vocational rehabilitation benefits and various other offsets to the permanent partial benefits.

Permanent Partial results

Based on our model, we have estimated that the overall impact on permanent partial cases will be approximately -12%. Since permanent partial costs are approximately 45% of total injury costs, the -12% savings on permanent partial translates to approximately a 5% reduction in overall costs.

Attorneys Fees

Currently, in Maine, the claimant's attorney is paid by the employer (insurer) in a workers compensation case. Under the proposed system, the employee pays for the cost of his/her attorney. The ultimate impact of this change is difficult to estimate. First of all, Maine data on the expenses due to

employees' attorneys is difficult to obtain in a proper format for ratemaking. Secondly, if these costs are shifted, there may be a whole change in which cases are aggressively pursued and how negotiated settlements are reached. One possibility is that the employees' attorney's costs will be eliminated from the system. However, we feel that this is an oversimplification. A second possibility is that some smaller cases will drop out of the system, and for slightly larger cases, the employee will pay his attorney out of the proceeds; but the larger cases will be pursued more aggressively by the injured workers and their attorneys so that each participant obtains similar benefits under the new system as under the old system. In other words, claimants may try to obtain a larger gross settlement, so that after paying their attorney, their net remaining benefit is similar to that obtained under the current law. After reviewing some Maine data on the percentage of dollars paid to claimants attorneys, we have selected a -1% rate impact for this change.

Other Issues

The proposed legislation contains many other changes that we have not explicitly evaluated. For example, there is a change regarding the compensability of preexisting conditions. In addition, there is revised language regarding the use of Independent Medical Examiners. We also assumed that the possibility of extending Permanent Partial benefits past 260 weeks would not occur frequently enough to effect overall costs. The impact of these three items, as well as many others fall into the area of "soft costs". As discussed above, we have not evaluated the impact of these kinds of items.

The actual outcome of the proposed legislation may produce

greater or lesser savings than the estimated -12% depending on what happens in all of the areas that we did not analyze.

In addition, available data appears to indicate that Maine has a claim frequency rate substantially greater than that in Michigan. If Maine's claim frequency could be reduced to levels observed in Michigan, then the savings in workers compensation costs could be reduced an additional 10 to 30 percent.

Overall Pricing Impact

The overall impact of the proposed legislation is calculated by multiplying the percentage impact for each injury type by the percentage of losses attributable to that injury type. Finally, an adjustment is made for the estimated impact of the change in employee's attorneys fees.

