SCOMM

33:4

NEW YORK STATE WORKER'S COMPENSATION FUND (000,000)

Year	Combined Ratio	Premiums	Investm. Inc.	Surplus
				23.5
1969	115 (Exp.: 19)	90	14.6	NA
1970	116	NA	16	NA
1971	110	NA	19	NA
1972	113	NA	20	NA
1973	123	116	24	±20
1974	125	NA	27	NA
1975	126	NA	32	7
1976	119	NA	45	NA
1977	108	NA	52	22
1978	99	NA	63	47
1979	82	NA	86	140
1980e	100	400	120e	260e

Source: Testimony of Donald Kramer, Kramer Capital Consultants, to Minnesota Workers' Compensation Study Commission, Sept. 3, 1980.

NA = not available on transcript; e = estimated

Kramer comments:

1969-73: "And even with a 123 combined ratio this surplus held constant in the $20 million range while they had modest growth in premiums from $90 million to $116 million."

1973-79: "First, it went through some periods where, by the way, it suffered some investment losses; it also went through periods where it suffered, as I say, 123 for three straight years -- '73, '74 and '75. And its surplus dropped to $7 million.... finally, it had a 99 and 82. The first two years it ever made so-called underwriting profit....With a 99, surplus went to $47 million. With an 82, surplus went to $140 million."

1969-81: "Between 1969 and 1981, this Fund will have accumulated approximately $380 million out of retained earnings. And during that period only two years did it have an underwriting profit: 1979 and 1978. And the result of that underwriting profit, by the way, was to foster a substantial reduction in rates in New York State....And again, I showed you the combined ratios were well over 100....In fact they have $400 million now. In fact, coming from $7 million of surplus less than ten years earlier, '73, to $400 million in '81 is almost an embarrassment of riches to the State Fund....And there is no incentive for the Fund to run -- it's not a stockholder-owned institution -- and there is no incentive for it to run to maximize reported profits. They take all the security lossses they can take...and take...conservative investment position."

I'm going into business. Somebody told me insurance was a good thing and I found Alaska was wide-open in workers' comp. Last frontier. Got a company, got the licenses and sold workers' comp. People have to have workers' comp; they bought it. At the end of the year I had sold $107 in premiums. That's my start -- my piece of the rock. If the risks were good, I might be making money; if not, I might be in trouble. In fact, insurance company net wealth leads me to believe that if I run with the pack my chances are pretty good that I'm going to come out all right, but let's see what happens to that $107.

First thing is, I had to buy a license, and I had to pay a premium tax. . . . . 3.5 %
Then I had general expenses. . . . . 6-plus %
Sales expenses. 7-plus%
When the claims came in, I had to adjust 'em:. . . . . 9-plus %
All those out-of-pocket expenses came to: . . . . . 26 %

The big variable, of course, is the losses. Mine came out at . . . . . 96 %
In the trade, that's called a combined ratio of 122 %
Workers' comp rates traditionally are regulated to hit a combined ration of 100%. Either I had a bad year, or the experience factor will kick the rates up again next year. Now, you're thinking, I am not going to have a next year: I only had $107 in premiums and I had a combined ration of 122.

But we've got two factors to consider:

1. I put that premium money in the bank and earned . . . 9%. In fact, the $107 I began with was actually $117 by the end of the year.

2. Some of those losses are going to be paid out over a long period of time. In fact, I actually paid out 60% of the incurred loss. (There's a lot of argument on the 60% figure -- some as low as 10%.)

Let's add it up: my total cash, remember, was $117. And I paid $28 in operating expenses, including loss adjustment (26% of $107) and I paid out 60% of the incurred losses (which were $102-plus -- so 60% =) $62.

What I had on hand, then, before taxes, at the end of the year, the product of my business (which I identify as change in surplus), was $27 ($117 minus $28, minus $62). Not a bad profit for a project

in which we invested no assets directly -- and operated with a killer loss ratio as bad as the one the carriers face in the Alaska comp market.

In fact, the figures on which this model was based are precisely the NAIC figures for workers' comp in Alaska in 1978 -- the exact same horrendous combined ratio that's keeping carriers out of the Alaska comp market.

But the NAIC figures show an underwriting loss in Alaska, don't they? Yes. Because the loss is reported as incurred loss. Incurred loss is not paid loss. The loss figure that goes into that horrible combined ratio is incurred loss. In other words, it's counted as paid, even though some of it -- perhaps 40%, perhaps even more -- won't be paid until some years down the pike.

(NOTE: If my understanding of the distinction between paid loss and incurred loss is faulty, I hope somebody will correct me on this point at once._

To understand the significance of the 1978 table I tried a second, third and fourth year with the same terrible loss ratio, watched my net surplus grow, then start to decline as the tail payments came due. I stopped writing in year four, recognizing the bubble had to burst. By the time I tried to work in tax losses, borrowing and such, I had cranked in too many assumptions to be comfortable; I was far away from the 1978 figures on workers' comp and I still didn't know whether workers' comp was a big money-maker, a giant loser, or somewhere in between. All I knew for certain was that if I had started from scratch in the year the carriers were hollering bloody murder, and had done precisely the business they had done, I would have had $25.7 million more in the bank at the end of the year than I had when the year began: from workers' comp premiums in Alaska.

For the next attempt to understand comp numbers, I looked around for a comp operation that wrote with a combined loss ratio well in excess of 100. Here are some figures on the New York State Worker's Compensation Fund. Let's start in 1969 with a premium of $90 million.

Hold on, you're saying: state funds have lower expenses. That's right. For 1969 we show expenses of 19 per cent and a combined ratio of 115. Let me lay out the figures for you.

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS 1978 PROFITABILITY RESULTS (000 OMITTED)

ALASKA 5/29/79 (p. 15)

LINE OF BUSINESS	PREMIUMS EARNED (= 100%)	INVST GAIN	LOSS INC	LOSS ADJ EXP	GEN EXP	SALES EXP	TAXES LIC & FEES	DIV TO PHDRS	FED INC TAX	UNDER WRITNT PRFT	OPER-ATING PRFT
	$	%	%	%	%	%	%	%	%	%	%
Workmens Comp	107,110	9.0	95.8	9.3	6.3	7.3	3.5	0.4	-8.4	-11.8	-5.3
	$	$	$	$	$	$	$	$	$	$	$
WC (Approx $ Value)[a]	107,000	9.6	102.5	10.0	7.7	7.8	3.7	0.4	-9.0	-12.6	-5.6
		116,600				-131,100			(9.0)		-6.5

Incurred loss is not paid loss: A review of paid-versus incurred losses for seven years in one state (Minnesota) showed 60% of incurred losses were paid, on the average, during the year in which the incurred loss was reported for all workers' comp written in the state, during those years. (The exact numbers are:

Total Incurred Losses $499,926,790 = 100%
Total Paid Losses $300,616,104 = 60.1%

(Indemn. pd. = $185,171,098)
(Med. pd. = $115,445,006)
(Total pd. = $300,616,104)
(Total unpd. = $199,310,686)

Some experts peg paid loss on a policy during the first policy year at 10% of incurred loss, the second year at 20-30 per cent. As the Minnesota Workers' Compensation Study Commission has observed, "A major failing in the present system of reporting loss stems from the inability to divide actual paid losses from incurred, but not paid, losses. Until this is done, it is impossible to judge with any certainty the accuracy or the judgements made by insurers about their future unpaid liability."

For the sake of simplicity, let's take the high pay-out ratio -- 60.1% of the incurred loss paid during the policy year -- and plug the paid loss number into the incurred loss column. The incurred loss -- reported on the NAIC form as approximately $102.5 million -- comes to a paid loss of $61.6 million. The paper loss of $15.5 million on the NAIC form is now a paper gain of $25.7 million. (Whether the reported federal income tax credit of $9.0 million should be added to the $25.7, giving a net profit of $34.7, I do not know.)

Notes: NAIC report distributed to Study Commission members 10/16/80.

Paid-versus-indemnity-loss figures from Minnesota from Minnesota Workers' Compensation Study Commission report, Feb. 1979 (on file with Study Commission), p. 148. Quote on failing of present system at p. 152.

W.O. 12- 0110
Amendment #1
Sofo

* Sec. ___. AS 23.30.005(k) is repealed.

* Sec. ___. AS 23.30.045(d) is amended to read:

(d) No contract may be awarded by the state or a home rule or other political subdivision of the state unless the person to whom the contract is to be awarded has submitted to the contracting agency proof, furnished by the insurance carrier, of current coverage by workers' compensation insurance from an insurance company or association authorized to transact the business of workers' compensation insurance in this state or proof, furnished by the insurance commissioner [BOARD], of a current certificate of self-insurance from the insurance commissioner [BOARD]. The person to whom the contract is awarded shall keep his workers' compensation insurance policy in effect during the life of the contract with the state or political subdivision. If the state or the political subdivision of the state fails to obtain proof of coverage or self-insurance or to protect itself under (e) of this section, and an employee of the contractor is injured during the term of the contract, the state or the political subdivision is liable for workers' compensation to the employee if the employee is unable to recover from the employer because of the employer's lack of financial assets. The state or the political subdivision is not liable, however, to the employee for workers' compensation if the employee can recover from the employer under (a) and (b) of this section.

* Sec. ___. AS 23.30.045(e) is amended to read:

(e) When a contracting agency of the state or a political subdivision receives notice that the workers' compensation insurance policy of an employer to whom the agency has awarded a contract has been cancelled due to nonpayment of a premium, without being replaced by a comparable policy, the agency may either terminate the contract with the employer or continue the premium payments on his behalf in order to

keep the policy in force during the life of the agency's contract. If the agency chooses to keep the policy in force, it may deduct its payments from the contract price or bring an action against the employer to recover the amount of the payments. When the contracting agency receives notice that the insurance commissioner [BOARD] has revoked a certificate of self-insurance held by a person to whom a contract has been awarded, the agency may terminate the contract. This subsection does not limit the causes of action or remedies which the state or political subdivision may have against the employer.

* Sec. ___. AS 23.30.075(a) is amended to read:

(a) An employer under this chapter, unless exempted, shall either [,] insure and keep insured for his liability under this chapter in an insurance company or association duly authorized to transact the business of workers' compensation insurance in this state, or shall furnish the insurance commissioner [BOARD] satisfactory proof of his financial ability to pay directly the compensation provided for. If an employer elects to pay directly, the insurance commissioner [BOARD] may, in his [ITS] discretion, require the deposit of an acceptable security, indemnity or bond to secure the payment of compensation liabilities as they are incurred.

* Sec. ___. AS 23.30.085(a) is amended to read:

(a) An employer subject to this chapter, unless exempted, shall initially file evidence of his compliance with the insurance provisions of this chapter with the board, in the form prescribed by it. The employer shall also give evidence of compliance within 10 days after the termination of his insurance by expiration or cancellation. These requirements do not apply to an employer who has certification from the insurance commissioner [BOARD] of his financial ability to pay compensation directly without insurance.

* Sec. ___. AS 23.30 is amended by adding a new section to read:

Sec. 23.30.087. GROUP SELF-INSURANCE. Two or more employers in the same rating classification may qualify as group self-insurers under regulations adopted by the insurance commissioner.

* Sec. ___. AS 23.30.090 is amended to read:

Sec. 23.30.090. SELF-INSURANCE CERTIFICATES. If an employer has complied with the provisions of this chapter relating to self-insurance, the insurance commissioner [BOARD] shall issue him a certificate which shall remain in force for a period fixed by the insurance commissioner [BOARD]. The insurance commissioner [BOARD] may, upon at least 10 days' notice and a hearing, revoke a self-insurance certificate upon satisfactory proof that an employer is no longer entitled to it. After revocation the insurance commissioner [BOARD] may grant a new certificate to an employer, upon his petition and satisfactory proof of his financial ability as provided in this chapter. The insurance commissioner shall notify the contracting agency of the state or of a political subdivision of the state when it revokes the self-insurance certificate of an employer holding a contract with the state or a political subdivision of the state. An employer authorized as a self-insurer shall provide claims facilities through its own staffed adjusting facilities located within the state, or independent, licensed, resident adjustors with power to effect settlement within the state.

* Sec. ___. AS 23.30.265(19) is amended to read:

(19) "self-insurer" means an employer who, instead of insuring his liability under this chapter as it provides, elects to pay directly the compensation provided for, and who has furnished to the insurance commissioner [BOARD] satisfactory proof of his financial ability to make the direct payments;

W.O. 12-0110
Amendment #2
Sofo

* Sec. ___. AS 21.36.190(d) is amended to read:

(d) This section does not apply to workers' compensation insurance when issued to an association of employers in the same rating classification [FORMED FOR PURPOSES OTHER THAN THE PURCHASE OF INSURANCE] and which as a group

[(1) HAS A CONSTITUTION AND BYLAWS;

(2) INCORPORATES A SAFETY PROGRAM;

(3) AS A GROUP HAS PREFERRED CHARACTERISTICS OVER SIMILAR RISKS WRITTEN ON AN INDIVIDUAL BASIS; AND

(4)] has filed and received approval from the director for the rating program to be applied to the group.

W.O. 12-0110
Amendment #3
Sofo

* Sec. ___. AS 23.30.025(b) is amended to read:

(b) All policies of insurance companies insuring the payment of compensation under this chapter are conclusively presumed to cover all the employees and the entire compensation liability of the insured employer employed at or in connection with the business of the employer carried on, maintained, or operated at the location or locations set out [FORTH] in that [SUCH] policy or agreement. A provision in a policy attempting to limit or modify the liability of the company issuing it is wholly void except as provided in (c) of this section.

* Sec. ___. AS 23.30.025 is amended by adding a new subsection to read:

(c) An insurer may issue a policy of insurance insuring the payment of compensation under this chapter which provides for a deductible amount to be paid by the employer. A policy with a deductible provision must be approved by the insurance commissioner and must provide that the deductible amount be paid by the insurer to the employee on behalf of the employer. After payment of the deductible by the insurer, the insurer may recover the deductible amount from the employer. The failure of an employer to reimburse an insurer for the deductible amount paid by the insurer on his behalf does not relieve the insurer from any other obligation it may have under the policy of insurance. An insurer is not required to apply for a deviation under AS 21.39.070 in order to issue a policy under this subsection.

W.O. 12-0110
Amendment #4
Sofo

* Sec. ___. AS 21.39.040(d) is amended to read:

(d) Subject to the exceptions [EXCEPTION] specified in (a) of this section and AS 21.39.045, each filing shall be on file for a waiting period of 15 days before it becomes effective, which period may be extended by the director for an additional period not to exceed 15 days if he gives written notice within the waiting period to the insurer or rating organization which made the filing stating that he needs additional time for the consideration of the filing. Upon written application by the insurer or rating organization, the director may authorize a filing which he has reviewed to become effective before the expiration of the waiting period. A filing shall be considered to meet the requirements of this chapter unless disapproved by the director within the waiting period.

* Sec. ___. AS 21.39 is amended by adding a new section to read:

Sec. 21.39.045. WORKERS' COMPENSATION RATE FILINGS. (a) Filings of workers' compensation rates by a rating organization shall be limited to provisions for claim payment and may not include allowances for expenses, taxes, or profit. The rating organization shall also file with the director the workers' compensation policy forms to be used by its members.

(b) If each rate in a schedule of workers' compensation rates for specific classifications of risks filed by an insurer is not lower than the rate provision for claim payment for each respective classification filed by a rating organization in accordance with (a) of this section and approved by the director, the schedule of rates filed by the insurer is not subject to AS 21.39.040(d) but becomes effective immediately.

W.O. 12-0110
Amendment #5
Sofo

* Sec. ___. AS 21.21 is amended by adding a new section to read:

Sec. 21.21.340. WORKERS' COMPENSATION INSURERS. Each foreign and domestic insurance carrier writing workers' compensation insurance coverage in the state shall include with its annual report required under AS 10.05.699 a report of income derived from the investment or deposit of insurance premiums and all forms of assets invested and held to cover reserves for workers' compensation liabilities resulting from its workers' compensation business in the state.

WORK DRAFT PAPER WORK DRAFT PAPER WORK DRAFT PAPER

W.O. 12-0110
Amendment #6
Sofo

* Sec. ___. AS 21.80.180(4) is amended to read:

(4) "covered claim" means an unpaid claim, including one of unearned premiums, which arises out of and is within the coverage and not in excess of the applicable limits of an insurance policy to which this chapter applies issued by an insurer, if the insurer becomes an insolvent insurer after August 6, 1970, and (A) the claimant or insured is a resident of this state at the time of the insured event; or (B) the property from which the claim arises is permanently located in this state; "covered claim" does not include any amount due a reinsurer, insurer, insurance pool, or underwriting association, as subrogation recoveries or otherwise and does not include any amount due under a policy of workers' compensation insurance based on rates effective under AS 21.39.045(b);

M E M O R A N D U M

TO: ALL COMMISSION MEMBERS

FROM: Licia Piceno

REF: Proposed legislation from the Division of Workers' Compensation

As per my telephone conservation with Jackie McClintock of November 13, 1980 she has requested that the following changes be made to your copies of their draft:

Section 2 (b) December 31, 1981, be deleted

Section 2 (i), be deleted, considered constitutionally invalid.

Section 4, the date has been changed from January 1, 1982 to July 1, 1981.

Section 5, This Act takes effect January 1, 1982, be deleted and should read: Section One of this Act, takes effect immediately in accordance with AS 01.10.070 (c)

An addition of Section 6 to read: Section 2 through 4 of this Act takes effect on July 1, 1981

October 24, 1980

Licia Piceno

Attached is a copy of the only bill that I know of which relates to worker's compensation. And, a quick review of that bill indicates that it is not directly related to insurance. This is the bill that the Division of Worker's Compensation, Dept. of Labor has submitted to the Governor's office for introduction. At this point in time it is impossible to if the Governor will actually introduce it, but I suspect that he probably will.

Bob Williams

A BILL

For an Act entitled: "An Act relating to the Alaska Worker's Compensation Board, and the Second Injury Fund established under the Alaska Workers' Compensation Act; and providing an effective date."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

*Section 1 AS 23.30.005(a) is ammended to read:

(a) The Alaska Workers's Compensation Board shall consist of (SEVEN) nine members, including a Southern panel of three members sitting for the First Judicial District, a Northern panel of three members sitting for the Second and Fourth Judicial Districts, (AND) a Southcentral panel of three members sitting for the Third Judicial District (.), and one panel of three members sitting for all judicial districts. Each panel shall include the commissioner of labor or his designated representative, a representative of industry and a representative of labor. The latter two members of each panel shall be appointed by the governor. All panel members are subject to confirmation by a majority of the members of the legislature in joint session.

*Section 2 AS 23.30.040 is repealed and re-enacted to read:

Sec. 23.30.040. SECOND INJURY FUND. (a) There is created a second injury fund, administered by the commissioner of labor. Money in the second injury fund may only be paid for the benefit of those persons entitled to payment of benefits from the second injury fund under this chapter. Payments from the second injury fund must be made by the commissioner of labor in accordance with the orders and awards of the board.

(b) If an employee suffers a compensable injury after December 31, 1981, which results in temporary total disability, temporary partial disability, permanent partial disability, or permanent total disability,

the employer or insurance carrier shall pay into the second injury fund a sum equal to six percent of the compensation to which the employee is entitled for temporary total disability, temporary partial disability, permanent partial disability, permanent total disability, or for rehabilitation under AS 23.30.191.

(c) If an employee suffers a compensable injury which results in death and the employee is not survived by a widow, widower, child or dependent relative eligible to receive death benefits under AS 23.30.215, the emp' yer or insurance carrier shall pay $10,000 to the second injury fund.

(d) The board may refund a payment made into the second injury fund if the employer or insurance carrier shows that it made the payment by mistake or inadvertence, or if it shows there existed at the time of the death of the employee a beneficiary entitled to benefits under AS 23.30.215.

(e) The board may direct and provide the vocational retraining and vocational rehabilitation of a permanently disabled person whose condition is a result of an injury compensable under this chapter by making cooperative arrangements with insurance carriers, private organizations and institutions, or state or federal agencies. The person being retrained or rehabilitated is entitled to receive compensation from the second injury fund for maintenance during the period of retraining and rehabilitation in the sum which the board considers necessary, not to exceed $200 a month. The total expenditures for maintenance, retraining, rehabilitation, and necessary transportation may not exceed $10,000 for one person.

(f) All amounts collected as civil penalties under this chapter must be paid into the second injury fund.

(g) The attorney general may investigate claims and hire expert witnesses necessary to prevent fraudulent

or excessive claims for money in the second injury fund and, subject to an appropriation for this purpose, may be reimbursed from the second injury fund for the cost of investigating claims and defending against those claims.

(h) Administration expenses of the state under this section and AS 23.30.205 must be paid from an appropriation from the second injury fund.

(i) If there is not enough money in the second injury fund to provide a reasonable reserve for the payment of compensation to persons entitled to payment of benefits from the second injury fund, the commissioner of revenue may loan surplus money in the general fund to the second injury fund. The loan may be made only from an appropriation for that purpose. The commissioner of revenue and the commissioner of labor shall determine the conditions for repayment of the loan to the general fund.

*Section 3 AS 23.30.045 (c) is amended to read:

(c) For a person eligible for vocational rehabilitation service under AS 23.15.080 and who is placed with an employer for service (WITHOUT WAGES) at the request of the office of vocational rehabilitation to give him on the job training, work readiness or work therapy experience, or work sampling, the liability set out in (a) of this section applies to the state rather than to the employer.

*Section 4 AS 23.30.040 (b) enacted in Sec. 2 of this Act does not apply to an employer or insurance carrier required to make payments to the second injury fund for an injury to an employee which occurred before January 1, 1982. For those employers or insurance carriers the amount of a payment to the second injury fund and the conditions under which a payment is required must be in accordance with the version of AS 23.30.040 (b) in effect on the day that the

injury to the employee occurred.

*Section 5 This Act takes effect January 1, 1982.

JUSTIFICATION FOR PROPOSED LEGISLATION

Section 1

This provision adds an additional Statewide panel to the Alaska Workers' Compensation Board who will serve when regional members are not available. There are currently six members. Hearings must be postponed when a panel member is unavailable.

This change will insure that disputed claims are heard by a full board panel as expeditiously as possible and will allow for additional hearing rounds to be scheduled should a backlog of disputed claims requiring hearing occur.

Section 2

AS 23.30.040. The repeal and re-enactment of Sec. 040 is necessary if the second injury fund is to continue to meet its obligations as set out in Sec. 040 and 205 of the Alaska Workers' Compensation Act.

Present monetary demands on the fund exceed receipts and the fund is unable to reimburse carriers in full for payments made to injured workers as required by Sec. 205. It is forced to make reimbursements on a monthly installment basis. In the future, payments made on amounts owed in past years will combine with present debts to deplete the fund and the program will be unworkable.

The amendment allows a more realistic maintenance allowance of $200.00 a month and total maximum expenditures for retraining of $10,000. The present law's $100 allowance and $5,000 maximum has been in effect since the 1960's and does not meet current actual costs of vocational rehabilitation.

The amendment also provides that the commissioner of revenue may loan general fund surplus monies to the second injury fund if insufficient monies are available for payment of benefits from the fund.

Section 3

AS 23.30.045 (c) is in need of change to allow placement of disabled employees who are being rehabilitated for gainful employment into work situations where the employer is willing to pay some wages to the employee trainee but does not want the risk of new injury to the handicapped person and the consequent increase to the employer's compensation insurance just for the trainee.

Successful rehabilitation will result in getting the handicapped employee back to a self sustaining tax paying citizen of the state and worth the investment by the state in accepting the risk of his being re-injured while learning a new occupation. This amendment will also encourage employers to pay wages to the trainee and reduce costs to the rehabilitation agency sponsoring the trainee.

W.O. 12- 0110
Amendment #1
Sofo

* Sec. ___. AS 23.30.005(k) is repealed.

* Sec. ___. AS 23.30.045(d) is amended to read:

(d) No contract may be awarded by the state or a home rule or other political subdivision of the state unless the person to whom the contract is to be awarded has submitted to the contracting agency proof, furnished by the insurance carrier, of current coverage by workers' compensation insurance from an insurance company or association authorized to transact the business of workers' compensation insurance in this state or proof, furnished by the insurance commissioner [BOARD], of a current certificate of self-insurance from the insurance commissioner [BOARD]. The person to whom the contract is awarded shall keep his workers' compensation insurance policy in effect during the life of the contract with the state or political subdivision. If the state or the political subdivision of the state fails to obtain proof of coverage or self-insurance or to protect itself under (e) of this section, and an employee of the contractor is injured during the term of the contract, the state or the political subdivision is liable for workers' compensation to the employee if the employee is unable to recover from the employer because of the employer's lack of financial assets. The state or the political subdivision is not liable, however, to the employee for workers' compensation if the employee can recover from the employer under (a) and (b) of this section.

* Sec. ___. AS 23.30.045(e) is amended to read:

(e) When a contracting agency of the state or a political subdivision receives notice that the workers' compensation insurance policy of an employer to whom the agency has awarded a contract has been cancelled due to nonpayment of a premium, without being replaced by a comparable policy, the agency may either terminate the contract with the employer or continue the premium payments on his behalf in order to

keep the policy in force during the life of the agency's contract. If the agency chooses to keep the policy in force, it may deduct its payments from the contract price or bring an action against the employer to recover the amount of the payments. When the contracting agency receives notice that the ~~insurance commissioner~~ [BOARD] has revoked a certificate of self-insurance held by a person to whom a contract has been awarded, the agency may terminate the contract. This subsection does not limit the causes of action or remedies which the state or political subdivision may have against the employer.

* Sec. ___. AS 23.30.075(a) is amended to read:

(a) An employer under this chapter, unless exempted, shall either [,] insure and keep insured for his liability under this chapter in an insurance company or association duly authorized to transact the business of workers' compensation insurance in this state, or shall furnish the ~~insurance commissioner~~ [BOARD] satisfactory proof of his financial ability to pay directly the compensation provided for. If an employer elects to pay directly, the ~~insurance commissioner~~ [BOARD] may, in his [ITS] discretion, require the deposit of an acceptable security, indemnity or bond to secure the payment of compensation liabilities as they are incurred.

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Sec. 23.30.087. GROUP SELF-INSURANCE. Two or more employers in the same rating classification may qualify as group self-insurers under regulations adopted by the ~~insurance commissioner~~ DIR DIV INS.

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Sec. 23.30.090. SELF-INSURANCE CERTIFICATES. If an employer has complied with the provisions of this chapter relating to self-insurance, the ~~insurance commissioner~~ [BOARD] shall issue him a certificate which shall remain in force for a period fixed by the ~~insurance commissioner~~ [BOARD]. The ~~insurance commissioner~~ [BOARD] may, upon at least 10 days' notice and a hearing, revoke a self-insurance certificate upon satisfactory proof that an employer is no longer entitled to it. After revocation the ~~insurance commissioner~~ [BOARD] may grant a new certificate to an employer, upon his petition and satisfactory proof of his financial ability as provided in this chapter. ~~The insurance commissioner~~ shall notify the contracting agency of the state or of a political subdivision of the state when it revokes the self-insurance certificate of an employer holding a contract with the state or a political subdivision of the state. An employer authorized as a self-insurer shall provide claims facilities through its own staffed adjusting facilities located within the state, or independent, licensed, resident adjustors with power to effect settlement within the state.

* Sec. ___. AS 23.30.265(19) is amended to read:

(19) "self-insurer" means an employer who, instead of insuring his liability under this chapter as it provides, elects to pay directly the compensation provided for, and who has furnished to the ~~insurance commissioner~~ [BOARD] satisfactory proof of his financial ability to make the direct payments;

w/ Koch changes

W.O. 12-0110
Amendment #2
Sofo

* Sec. ___. AS 21.36.190(d) is amended to read:

(d) This section does not apply to workers' compensation insurance when issued to an association of employers in the same rating classification [FORMED FOR PURPOSES OTHER THAN THE PURCHASE OF INSURANCE] and which as a group

(1) HAS A CONSTITUTION AND BYLAWS;

(2) INCORPORATES A SAFETY PROGRAM;

~~(3) AS A GROUP HAS PREFERRED CHARACTERISTICS OVER SIMILAR RISKS WRITTEN ON AN INDIVIDUAL BASIS~~; AND

(3) has filed and received approval from the director for the rating program to be applied to the group.

LA-L 20A

W.O. 12-0110
Amendment #3
Sofo

* Sec. ___. AS 23.30.025(b) is amended to read:

(b) All policies of insurance companies insuring the payment of compensation under this chapter are conclusively presumed to cover all the employees and the entire compensation liability of the insured employer employed at or in connection with the business of the employer carried on, maintained, or operated at the location or locations set out [FORTH] in that [SUCH] policy or agreement. A provision in a policy attempting to limit or modify the liability of the company issuing it is wholly void except as provided in (c) of this section.

* Sec. ___. AS 23.30.025 is amended by adding a new subsection to read:

(c) An insurer may issue a policy of insurance insuring the payment of compensation under this chapter which provides for a deductible amount to be paid by the employer. A policy with a deductible provision must be approved by the insurance commissioner and must provide that the deductible amount be paid by the insurer to the employee on behalf of the employer. After payment of the deductible by the insurer, the insurer may recover the deductible amount from the employer. The failure of an employer to reimburse an insurer for the deductible amount paid by the insurer on his behalf does not relieve the insurer from any other obligation it may have under the policy of insurance. An insurer is not required to apply for a deviation under AS 21.39.070 in order to issue a policy under this subsection.

already div (ins-
promulgated
deductible policies
suggest tech amdt:
filing for deductible
is not deviation
Insurer apply
to exc

LA-L 20A

HOLD TO JANUARY

W.O. 12-0110
Amendment #4
Soño

* Sec. ___. AS 21.39.040(d) is amended to read:

(d) Subject to the exceptions [EXCEPTION] specified in (e) of this section and AS 21.39.045, each filing shall be on file for a waiting period of 15 days before it becomes effective, which period may be extended by the director for an additional period not to exceed 15 days if he gives written notice within the waiting period to the insurer or rating organization which made the filing stating that he needs additional time for the consideration of the filing. Upon written application by the insurer or rating organization, the director may authorize a filing which he has reviewed to become effective before the expiration of the waiting period. A filing shall be considered to meet the requirements of this chapter unless disapproved by the director within the waiting period.

* Sec. ___. AS 21.39 is amended by adding a new section to read:

Sec. 21.39.045. WORKERS' COMPENSATION RATE FILINGS. (a) Filings of workers' compensation rates by a rating organization shall be limited to provisions for claim payment and may not include allowances for expenses, taxes, or profit. The rating organization shall also file with the director the workers' compensation policy forms to be used by its members.

(b) If each rate in a schedule of workers' compensation rates for specific classifications of risks filed by an insurer is not lower than the rate provision for claim payment for each respective classification filed by a rating organization in accordance with (a) of this section and approved by the director, the schedule of rates filed by the insurer is not subject to AS 21.39.040(d) but becomes effective immediately.

Needs additional section (c) allow dir to reinstate prior approval if excess cost.

assigned risks Mahoney: pool who pays

delete years

W.O. 12-0110
Amendment #5
Sofo

HOLD TO JANUARY

* Sec. ___. AS 21.21 is amended by adding a new section to read:

Sec. 21.21.340. WORKERS' COMPENSATION INSURERS. Each foreign and domestic insurance carrier writing workers' compensation insurance coverage in the state shall include with its annual report required under AS 10.05.699 a report of income derived from the investment or deposit of insurance premiums and all forms of assets invested and held to cover reserves for workers' compensation liabilities resulting from its workers' compensation business in the state.

div ins

WORK DRAFT PAPER WORK DRAFT PAPER WORK DRAFT PAPER

W.O. 12-0110
Amendment #6
Sofo

HOLD TO JANUARY

* Sec. ___. AS 21.80.180(4) is amended to read:

(4) "covered claim" means an unpaid claim, including one of unearned premiums, which arises out of and is within the coverage and not in excess of the applicable limits of an insurance policy to which this chapter applies issued by an insurer, if the insurer becomes an insolvent insurer after August 6, 1970, and (A) the claimant or insured is a resident of this state at the time of the insured event; or (B) the property from which the claim arises is permanently located in this state; "covered claim" does not include any amount due a reinsurer, insurer, insurance pool, or underwriting association, as subrogation recoveries or otherwise and does not include any amount due under a policy of workers' compensation insurance based on rates effective under AS 21.39.045(b);

eliminates guaranty fund

* Sec. ___. AS 23.30.045(d) is amended to read:

(d) No contract may be awarded by the state or a home rule or other political subdivision of the state to an employer under this chapter unless the employer [PERSON] to whom the contract is to be awarded has submitted to the contracting agency proof, furnished by the insurance carrier, of current coverage by workers' compensation insurance from an insurance company or association authorized to transact the business of workers' compensation insurance in this state or proof, furnished by the board, of a current certificate of self-insurance from the board. The employer [PERSON] to whom the contract is awarded shall keep his workers' compensation insurance policy in effect during the life of the contract with the state or political subdivision. If the state or the political subdivision of the state fails to obtain proof of coverage or self-insurance or to protect itself under (e) of this section, and an employee of the contractor is injured during the term of the contract, the state or the political subdivision is liable for workers' compensation to the employee if the employee is unable to recover from the employer because of the employer's lack of financial assets. The state or the political subdivision is not liable, however, to the employee for workers' compensation if the employee can recover from the employer under (a) and (b) of this section.

12-0110 - Amend. #8
Sofo

* Sec. ___. AS 23.30.080 is amended by adding a new subsection to read:

(d) If an employer fails to insure or provide security as required by AS 23.30.075, the board may issue a stop order prohibiting the use of employee labor by the employer until the employer insures or provides security as required by AS 23.30.075. If an employer fails to comply with a stop order issued under this section, the board shall assess a civil penalty of ___.

12-0110
AMEND. # 9
Sofo

* Sec. ___. AS 23.30.105(a) is amended to read:

(a) The right to compensation for disability under this chapter is barred unless a claim for it is filed within two years after the employee has knowledge of the nature of his disability and its relation to his employment and after disablement. The [HOWEVER, THE MAXIMUM TIME FOR FILING THE CLAIM IN ANY EVENT OTHER THAN ARISING OUT OF AN OCCUPATIONAL DISEASE SHALL BE FOUR YEARS FROM THE DATE OF INJURY, AND THE] right to compensation for death is barred unless a claim for compensation [THEREFORE] is filed within one year after the death, except that if payment of compensation has been made without an award on account of the injury or death, a claim may be filed within two years after the date of the last payment. It is additionally provided that, in the case of latent defects pertinent to and causing compensable disability, the injured employee has full right to claim as shall be determined by the board, time limitations notwithstanding.

12-0110 - Amend. #10
Sofo

* Sec. ___. AS 23.30.155 is amended by adding a new subsection to read:

(m) Compensation owed to an injured employee who is in the state shall be paid by certified check or by a check drawn on a bank authorized to do business and located in the state.

#12-0110 - Amend. #11
Sofo

* Sec. ___. AS 23.30.210(b) is amended to read:

(b) At any time after death, or after 30 days subsequent to the date of injury, the employer and the employee or the beneficiary or beneficiaries, as the case may be, have the right to reach an agreement in regard to a claim for injury or death under this chapter [HEREUNDER] in accordance with the applicable schedule [HEREOF], but a memorandum of the agreement in a form prescribed by the board shall be filed with the board. Otherwise, the agreement is void for any purpose. If approved by the board, the agreement is enforceable the same as an order or award of the board and discharges the liability of the employer for the compensation notwithstanding the provisions of [AS 23.30.130,] AS 23.30.160 [,] and AS 23.30.245(b) [AS 23.30.245]. The agreement shall be approved by the board only when the terms conform to the provisions of this chapter and, if it involves or is likely to involve permanent disability, the board may require an impartial medical examination and a hearing in order to determine whether or not to approve the agreement. The board may approve lump-sum settlements when it appears to be to the best interest of the employee or beneficiary or beneficiaries.

* Sec. ___. AS 23.30.215(a)(1) is amended to read:

(1) reasonable and necessary funeral expenses not exceeding ~~$2,000~~ [$1,000]; 2500 3000

$2500

condition - Bd may increase as needed

12-0110 - Amend. #13
Sofo

* Sec. ___. AS 23.30.095(a) is amended to read:

(a) The employer shall furnish medical, surgical, and other attendance or treatment, nurse and hospital service, medicine, crutches, and apparatus for the period which the nature of the injury or the process of recovery requires [, NOT EXCEEDING TWO YEARS FROM AND AFTER THE DATE OF INJURY TO THE EMPLOYEE. HOWEVER, IF THE CONDITION REQUIRING THE TREATMENT, APPARATUS, OR MEDICINE IS A LATENT ONE, THE TWO-YEAR PERIOD RUNS FROM THE TIME THE EMPLOYEE HAS KNOWLEDGE OF THE NATURE OF HIS DISABILITY AND ITS RELATIONSHIP TO HIS EMPLOYMENT AND AFTER-DISABLEMENT. IT SHALL BE ADDITIONALLY PROVIDED THAT, IF CONTINUED TREATMENT OR CARE OR BOTH BEYOND THE TWO-YEAR PERIOD IS INDICATED, THE INJURED EMPLOYEE HAS THE RIGHT OF REVIEW BY THE BOARD. THE BOARD MAY AUTHORIZE CONTINUED TREATMENT OR CARE OR BOTH AS THE PROCESS OF RECOVERY MAY REQUIRE]. When medical care is required, the injured employee may designate a licensed physician inside the state to render the care except in cases where, in the judgment of the board, care or treatment or both can best be administered by the selection of another <u>licensed</u> physician. Upon procuring the services of a <u>licensed</u> physician, the injured employee shall give proper notification of his selection to the employer within a reasonable time after first being treated. [IF FOR ANY REASON DURING THE PERIOD WHEN MEDICAL CARE IS REQUIRED THE EMPLOYEE WISHES TO CHANGE TO ANOTHER PHYSICIAN, HE MAY DO SO IN ACCORDANCE WITH RULES PRESCRIBED BY THE BOARD.]

* Sec. ___. AS 23.30.095(c) is amended to read:

(c) No claim for medical or surgical treatment is valid and enforceable as against the employer unless, within <u>20</u> [TWENTY] days following <u>each visit for</u> [THE FIRST] treatment, the physician giving the treatment or the employee receiving it furnishes to the employer and the board notice of the injury and treatment, preferably on a form

prescribed by the board. The board may, however, excuse the failure to furnish notice within 20 days when it finds it to be in the interest of justice to do so, and it may, upon application by a party in interest, make an award for the reasonable value of the medical or surgical treatment so obtained by the employee.

* Sec. ___. AS 23.30.095(e) is amended to read:

(e) The employee shall, after an injury, at reasonable times during the continuance of his disability if requested by his employer or, when ordered by the board, submit himself to an examination by a physician or surgeon authorized to practice medicine under the laws of the state in which the employee may be found, furnished and paid for by the employer. [THE EMPLOYEE HAS THE RIGHT TO HAVE A PHYSICIAN, PAID FOR BY THE EMPLOYER, PRESENT AT THE EXAMINATION OR EXAMINATIONS.] No fact relative to the injury or claim communicated to or otherwise learned by a physician or surgeon who may have attended or examined the employee, or who may have been present at an examination is privileged, either in the hearings provided for in this chapter or an action to recover damages against an employer who is subject to the compensation provisions of this chapter. If an employee refuses to submit himself to any examination provided for <u>in this section</u> [HEREIN], his rights to compensation shall be suspended until the obstruction or refusal ceases, and his compensation during the period of suspension may, in the discretion of the board or the court determining an action brought for the recovery of damages <u>under this chapter</u> [HEREUNDER], be forfeited. The board in any case of death may require an autopsy at the expense of the party requesting the autopsy. No autopsy may be held without notice first being given to the widow or widower or next of kin if they reside in the state or their whereabouts can be reasonably ascertained, of the time and place of the autopsy and reasonable time and opportunity

given the widow or widower or next of kin to have a representative present to witness the autopsy. If no adequate notice is given, the findings from the autopsy may be suppressed on motion made to the board or to the superior court, as the case may be.

* Sec. ___. AS 23.30.110(c) is amended to read:

(c) The board shall make the investigation which it considers necessary in respect of the claim, and upon application of an interested party shall order a hearing on it. If a hearing on a claim is ordered, the board shall give the claimant and other interested parties at least 20 [10] days' notice of the hearing, served personally upon the claimant and other interested parties or sent by registered mail, and shall, within 30 [20] days after the hearing is held [HAD], by order, reject the claim or make an award in respect to it. [IF NO HEARING IS ORDERED WITHIN 20 DAYS AFTER NOTICE IS GIVEN AS PROVIDED IN (b) OF THIS SECTION, THE BOARD SHALL BY ORDER REJECT THE CLAIM OR MAKE AN AWARD IN RESPECT TO IT.]

* Sec. ___. AS 23.30.155(c) is amended to read:

(c) Upon making the first payment, and upon an increase, reduction, termination, or suspension of payment for any cause, the employer or carrier shall [IMMEDIATELY] notify the board within 10 days, in accordance with a form prescribed by the board, that payment of compensation has begun or has been increased, reduced, stopped, or suspended, as the case may be. If the employer or carrier fails to so notify the board within 10 days, the board shall assess against the employer or carrier a civil penalty in the amount of $100 plus $25 for each day in excess of the 10 days that the employer or carrier fails to give the notice. Total penalties under this section may not exceed $2,500.

* Sec. __. AS 23.30.155(h) is amended to read:

(h) The board may upon its own initiative at any time in a case

in which payments are being made without an award, and shall in a case where right to compensation is controverted, or where payments of compensation have been reduced, stopped or suspended, upon receipt of notice from a person entitled to compensation, or from the employer, that the right to compensation is controverted, or that payments of compensation have been reduced, stopped or suspended, make the investigations, cause the medical examinations to be made, or hold the hearings, and take the further action which it considers will properly protect the rights of all parties.

* Sec. __. AS 23.30.175(b) is repealed and reenacted to read:

(b) After June 30 and before December 1 of each year, the commissioner shall adopt and publish the average weekly wage for the preceding calendar year as computed by the United States Secretary of Labor for the purposes of unemployment insurance. In determining the rate of compensation the commissioner shall use the average weekly wage figure for each jurisdiction, including Alaska, for which the Secretary of Labor computes an average weekly wage. These figures are the applicable average weekly wages for those jurisdictions for the following calendar year. The average weekly wage is the amount determined by dividing (1) the total wages paid by all employers covered for the purpose of computing unemployment insurance by (2) the average monthly employment reported by those employers for the same period and dividing the result by 52.

* Sec. __. AS 23.30.175(c) is repealed and reenacted to read:

(c) The following rules apply to recipients who do not reside in Alaska:

(1) The weekly rate of compensation must be calculated using the recipient's average weekly wage times the ratio of the average weekly wage of the jurisdiction in which the recipient resides to the

average weekly wage of Alaska.

(2) A calculation and reduction is not required by this subsection if the recipient's average weekly wage and resulting compensation rate is determined under the provisions of AS 23.30.220 by use of wages earned wholly in employment in jurisdictions other than Alaska or when the absence of the recipient is for medical or rehabilitation services that are not reasonably available in Alaska.

(3) Application of this subsection may not result in a reduction of the weekly compensation rate to less than the minimum weekly compensation payable under the workers' compensation system of the jurisdiction in which the recipient is residing. In no case may weekly compensation be less than $65 per week.

(4) Application of this subsection may not result in a weekly rate of compensation which is greater than 200 percent of the average weekly wage of the jurisdiction in which the recipient is residing.

* Sec. __. AS 23.30.191 is repealed and reenacted to read:

Sec. 23.30.191. EXPENSES FOR REHABILITATING INJURED EMPLOYEES. An employee, who, as a result of injury, is or may be expected to be totally or partially incapacitated for his normal occupation and who, under the direction of the Department of Labor, is being rehabilitated to engage in a remunerative occupation, may receive compensation necessary for his rehabilitation equal to 66-2/3 percent of his average weekly wage.

* Sec. __. AS 23.30.215(h) is amended to read:

(h) <u>If</u> [IN THE EVENT] a deceased worker is survived by children of a former marriage not living with the surviving widow or widower, [THEN] those children shall receive the amount being paid under a decree of child support<u>. The children may not receive benefits in</u>

excess of benefits to which they would have been entitled had there not been a decree of child support, unless there is no other beneficiary entitled to benefits; the difference between the amount payable under a decree of child support [THIS AMOUNT] and the maximum benefit payable under this section shall be distributed pro rata to the remainder of those entitled.

* Sec. __. AS 23.30.095(g), 23.30.125(b), 23.30.155(g), 23.30.175(d), (e), and (f) are repealed.

WO 12-0110
Amend. #14
Sofo

W

OK

* Sec.___. AS 23.30.250 is amended to read:

Sec. 23.30.250. PENALTY FOR MISREPRESENTATION. A person who wilfully makes a false or misleading statement or representation for the purpose of obtaining a benefit or payment under this chapter is guilty of theft as defined in AS 11.46.100(3) and is punishable as provided in AS 11.46.120 - 11.46.150 [A MISDEMEANOR, AND UPON CONVICTION IS PUNISHABLE BY A FINE OF NOT MORE THAN $1,000, OR BY IMPRISONMENT FOR NOT MORE THAN ONE YEAR, OR BY BOTH].

12-0110 - Amend. #15
Sofo

OK

*Sec. ___. AS 18.80.220(a)(4) is amended to read:

(4) an employer, labor organization or employment agency to discharge, expel or otherwise discriminate against a person because he has opposed any practices forbidden under AS 18.80.200 - 18.80.280, [OR BECAUSE HE] has filed a complaint, testified or assisted in a proceeding under this chapter, or has filed a claim for workers' compensation benefits under AS 23.30;

For an Act entitled: "An Act relating to the Alaska Workers' Compensation Board, and the Second Injury Fund established under the Alaska Workers' Compensation Act; and providing for an effective date."

BE ~~IT ENACTED~~ BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. AS 23.30.005(a) is amended to read:

(a) The Alaska Workers' [WORKMEN'S] Compensation Board shall consist of nine [SEVEN] members, including a southern panel of three members sitting for the first judicial district, a northern panel of three members sitting for the second and fourth judicial districts, [AND] a southcentral panel of three members sitting for the third judicial district, [.] and one panel of three members ~~sitting for all~~ which may sit in any judicial districts. Each panel shall include the commissioner of labor or his designated representative, a representative of industry and a representative of labor. The latter two members of each panel shall be appointed by the governor. All panel members are subject to confirmation by a majority of the members of the legislature in joint session.

* Sec. 2. AS 23.30.040 is repealed and re-enacted to read:

Sec. 23.30.040. SECOND INJURY FUND. (a) There is created a Second Injury Fund, administered by the commissioner of labor. Money in the Second Injury Fund may only be paid for the benefit of those persons entitled to payment of benefits from the Second Injury Fund under this chapter. Payments from the second injury fund must be made

by the commissioner of labor in accordance with the orders and awards of the board.

(b) If an employee suffers a compensable injury which results in temporary total disability, temporary partial disability, permanent partial disability, or permanent total disability, the employer or insurance carrier shall pay into the Second Injury Fund a sum equal to six percent of the compensation to which the employee is entitled for temporary total disability, temporary partial disability, permanent partial disability, permanent total disability, or for rehabilitation under AS 23.30.191.

(c) If an employee suffers a compensable injury which results in death and the employee is not survived by a widow, widower, child or dependent relative eligible to receive death benefits under AS 23.30.215, the employer or insurance carrier shall pay $10,000 to the Second Injury Fund.

(d) The board may refund a payment made into the Second Injury Fund if the employer or insurance carrier shows that it made the payment by mistake or inadvertence, or if it shows there existed at the time of the death of the employee a beneficiary entitled to benefits under AS 23.30.215.

(e) The board may direct and provide the vocational retraining and vocational rehabilitation of a permanently disabled person whose condition is a result of an injury compensable under this chapter by making cooperative arrangements with insurance carriers, private organizations and institutions, or state or federal agencies. The person being retained or rehabilitated is entitled to receive compensation from the Second Injury Fund for maintenance during the period of retaining and rehabilitation in the sum which the board considers necessary, not to exceed $200 a month. The total expendi-

tures for maintenance, retraining, rehabilitation, and necessary transportation may not exceed $10,000 for one person.

(f) All amounts collected as civil penalties under this chapter must be paid into the Second Injury Fund.

(g) The attorney general may investigate claims and hire expert witnesses necessary to prevent fraudulent or excessive claims for money in the Second Injury Fund and, subject to an appropriation for this purpose, may be reimbursed from the Second Injury Fund for the cost of investigating claims and defending against those claims.

(h) Administration expenses of the state under this section and AS 23.30.205 must be paid from an appropriation from the Second Injury Fund.

(i) The provisions of (b) and (c) of this section shall be waived in and during any calendar ~~year~~ Q when the unencumbered balance on ~~January 1~~ 1st day of Q in the Second Injury Fund is equal to or exceeds the sum of ~~$400,000~~ $600,000.

* Sec. 3. AS 23.30.045(c) is amended to read:

(c) For a person eligible for vocational rehabilitation service under AS 23.15.080 [AND] who is placed with an employer for service [WITHOUT WAGES] at the request of the office of vocational rehabilitation to give him on the job training, work readiness, [OR] work therapy experience[,] or work sampling, the liability set out in (a) of this section applies to the state rather than to the employer.

* Sec. 4. The amount of a payment to the Second Injury Fund and the conditions under which a payment is required of an employer or insurance carrier must be in accordance with the version of AS 23.30.040(b) in effect on the date that the injury to the employee occurred.

* Sec. 5. Section 1 of this Act takes effect immediately in accordance with AS 01.10.070(c).

* Sec. 6. Section 2-4 of this Act take effect on July 1, 1981.

A BILL

For an Act entitled: "An Act relating to the Alaska Worker's Compensation Board, and the Second Injury Fund established under the Alaska Workers' Compensation Act; and providing an effective date."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

*Section 1 AS 23.30.005(a) is ammended to read:

(a) The Alaska Workers's Compensation Board shall consist of (SEVEN) nine members, including a Southern panel of three members sitting for the First Judicial District, a Northern panel of three members sitting for the Second and Fourth Judicial Districts, (AND) a Southcentral panel of three members sitting for the Third Judicial District (.), and one panel of three members sitting for all judicial districts. Each panel shall include the commissioner of labor or his designated representative, a representative of industry and a representative of labor. The latter two members of each panel shall be appointed by the governor. All panel members are subject to confirmation by a majority of the members of the legislature in joint session.

*Section 2 AS 23.30.040 is repealed and re-enacted to read:

Sec. 23.30.040. SECOND INJURY FUND. (a) There is created a second injury fund, administered by the commissioner of labor. Money in the second injury fund may only be paid for the benefit of those persons entitled to payment of benefits from the second injury fund under this chapter. Payments from the second injury fund must be made by the commissioner of labor in accordance with the orders and awards of the board.

(b) If an employee suffers a compensable injury after December 31, 1981, which results in temporary total disability, temporary partial disability, permanent partial disability, or permanent total disability,

th[redacted]mployer or insurance car[redacted]r shall pay into the second injury fund a sum equal to six percent of the compensation to which the employee is entitled for temporary total disability, temporary partial disability, permanent partial disability, permanent total disability, or for rehabilitation under AS 23.30.191.

(c) If an employee suffers a compensable injury which results in death and the employee is not survived by a widow, widower, child or dependent relative eligible to receive death benefits under AS 23.30.215, the employer or insurance carrier shall pay $10,000 to the second injury fund.

(d) The board may refund a payment made into the second injury fund if the employer or insurance carrier shows that it made the payment by mistake or inadvertence, or if it shows there existed at the time of the death of the employee a beneficiary entitled to benefits under AS 23.30.215.

(e) The board may direct and provide the vocational retraining and vocational rehabilitation of a permanently disabled person whose condition is a result of an injury compensable under this chapter by making cooperative arrangements with insurance carriers, private organizations and institutions, or state or federal agencies. The person being retrained or rehabilitated is entitled to receive compensation from the second injury fund for maintenance during the period of retraining and rehabilitation in the sum which the board considers necessary, not to exceed $200 a month. The total expenditures for maintenance, retraining, rehabilitation, and necessary transportation may not exceed $10,000 for one person.

(f) All amounts collected as civil penalties under this chapter must be paid into the second injury fund.

(g) The attorney general may investigate claims and hire expert witnesses necessary to prevent fraudulent

excessive claims for money in the second injury fund and, subject to an appropriation for this purpose, may be reimbursed from the second injury fund for the cost of investigating claims and defending against those claims.

(h) Administration expenses of the state under this section and AS 23.30.205 must be paid from an appropriation from the second injury fund.

(i) If there is not enough money in the second injury fund to provide a reasonable reserve for the payment of compensation to persons entitled to payment of benefits from the second injury fund, the commissioner of revenue may loan surplus money in the general fund to the second injury fund. The loan may be made only from an appropriation for that purpose. The commissioner of revenue and the commissioner of labor shall determine the conditions for repayment of the loan to the general fund.

*Section 3 AS 23.30.045 (c) is amended to read:

(c) For a person eligible for vocational rehabilitation service under AS 23.15.080 and who is placed with an employer for service (WITHOUT WAGES) at the request of the office of vocational rehabilitation to give him on the job training, work readiness or work therapy experience, or work sampling, the liability set out in (a) of this section applies to the state rather than to the employer.

*Section 4 AS 23.30.040 (b) enacted in Sec. 2 of this Act does not apply to an employer or insurance carrier required to make payments to the second injury fund for an injury to an employee which occurred before January 1, 1982. For those employers or insurance carriers the amount of a payment to the second injury fund and the conditions under which a payment is required must be in accordance with the version of AS 23.30.040 (b) in effect on the day that the

injury to the employee occurred.

*Section 5 This Act takes effect January 1, 1982.

JUSTIFICATION FOR PROPOSED LEGISLATION

Section 1

This provision adds an additional Statewide panel to the Alaska Workers' Compensation Board who will serve when regional members are not available. There are currently six members. Hearings must be postponed when a panel member is unavailable.

This change will insure that disputed claims are heard by a full board panel as expeditiously as possible and will allow for additional hearing rounds to be scheduled should a backlog of disputed claims requiring hearing occur.

Section 2

AS 23.30.040. The repeal and re-enactment of Sec. 040 is necessary if the second injury fund is to continue to meet its obligations as set out in Sec. 040 and 205 of the Alaska Workers' Compensation Act.

Present monetary demands on the fund exceed receipts and the fund is unable to reimburse carriers in full for payments made to injured workers as required by Sec. 205. It is forced to make reimbursements on a monthly installment basis. In the future, payments made on amounts owed in past years will combine with present debts to deplete the fund and the program will be unworkable.

The amendment allows a more realistic maintenance allowance of $200.00 a month and total maximum expenditures for retraining of $10,000. The present law's $100 allowance and $5,000 maximum has been in effect since the 1960's and does not meet current actual costs of vocational rehabilitation.

The amendment also provides that the commissioner of revenue may loan general fund surplus monies to the second injury fund if insufficient monies are available for payment of benefits from the fund.

Section 3

AS 23.30.045 (c) is in need of change to allow placement of disabled employees who are being rehabilitated for gainful employment into work situations where the employer is willing to pay some wages to the employee trainee but does not want the risk of new injury to the handicapped person and the consequent increase to the employer's compensation insurance just for the trainee.

Successful rehabilitation will result in getting the handicapped employee back to a self sustaining tax paying citizen of the state and worth the investment by the state in accepting the risk of his being re-injured while learning a new occupation. This amendment will also encourage employers to pay wages to the trainee and reduce costs to the rehabilitation agency sponsoring the trainee.

Open Competitive Rates for Workers' Compensation

by Albert J. Millus * President
Albert J. Millus & Associates, New York

We are witnessing history being made in the recent trends toward substituting market place competition for state regulation of rates for Workers' Compensation premium. The movement is really much broader in that its supporters advocate open competitive rates for all personal and commercial property and casualty insurance coverage, and the arguments advanced for and against it exemplify the historic differences in approach by certain elements in the industry to a problem that has gone full circle over the past century.

A Bit of History

As long ago as 1869, the United States Supreme Court in the case of Paul v. Virginia[1] held that insurance was not commerce under the commerce clause of the Constitution. As a result of that decision, states were left free to regulate insurance and if states did not do so, the insurance industry was free to set up its own mechanisms to control the business. Fire insurance was an important line of coverage and the competition for this business became very widespread. At the same time the agency system for procuring business was developing rapidly and before long insurance carriers began to devote more time and energy to building up a strong agency system than to direct competition for the fire insurance business. Soon rate wars began to threaten the solvency of some of the insurance companies. As a means of protecting their interests the companies began to "fix" rates by agreement among themselves. Many insurers refused to adhere to such practices and some states began to enact anti-trust laws. States realized that insurance required regulation and their laws began to recognize the need for rating bureaus where the insurers could collectively submit their loss experience and where an objective base could be found for fair rates. By the early 1940's most states had authorized rate bureaus and in effect the business of rate fixing was largely in the control of the insurance industry,

* Albert J. Millus heads a firm specializing in the reduction of workers' compensation cost. He is the former Executive Director of the State Insurance Fund (New York) and author and lecturer on Workers' Compensation.

(1) 8 Wall. 168, 19L.6Ed.357.

although "regulated" by the Insurance Commissioners in the several states. The situation that brought about the McCarran-Ferguson Act - Public Law 15 - developed when one of the groups of fire rating organizations - the Southeastern Underwriters Association - promulgated rates for fire coverage and the United States brought suit against the Association and its members. The United States Supreme Court (1944)(2) held such activity subject to federal anti-trust laws. Congress thereafter passed Public Law 15, which, in substance, declared that historically states had the right to regulate insurance and that the federal law would be applied only if the states failed to do so. However, agreements to boycott, coerce or intimidate would continue to be subject to the federal law. This law gave the states the incentive to pass regulatory laws and most did so, using a model law proposed by the National Association of Insurance Commissioners (NAIC). Each state varied its laws to some extent from the model law to suit its own situations but most provided for rate organizations to collect loss data by classification and promulgate rates for the approval of the State Industrial Commissioner. Practically al_ state laws required that rates so calculated may not be excessive, inadequate or unfairly discriminatory. With the development of multiperil policies the historic gap between fire insurance companies and other personal lines began to narrow. Now there is hardly any distinction and as many of the independent, non-bureau insurance companies grew into national operations the tendency toward reliance on open market competition to regulate rates became more widespread. State laws were changed to make bureaus advisory only and various forms of file & use and other forms of non prior approval changes became prevalent. Thus we see a full circle from the position of the insurance industry demanding the right to fix rates by agreement to one where many are advocating complete open competition with the market place determining the rate. This latter position is most strongly advocated by the large, national

(2) 322 U.S. 533

direct writers, although the old line bureau companies are reluctantly joining the demand even though they may have some serious reservations about the ultimate effect on themselves and the public.

Workers' Compensation

While this trend to open competitive rates is directed at all property and casualty lines, large segments of the industry do not agree that it should apply to Workers' Compensation. The author claims no expertise in the area of rate making in property and casualty insurance generally and so will limit this article to the area of Workers' Compensation rate making, where he does claim knowledge and understanding of the subject.

NAIC - Report of the Advisory Committee on Competitive Rating

The National Association of Insurance Commissioners appointed a subcommittee to consider competitive rating as the primary means of regulating rates in the personal and commercial property and casualty markets. In August, 1979, the subcommittee appointed a widely based Advisory Committee to assist the subcommittee. This Advisory Committee submitted its Report at the 109th Annual Meeting of the NAIC held in June, 1980. The report is comprehensive, clear and reasonably concise. However, the divergence of opinions as expressed by particular members of the Advisory Committee shows that there is little basic agreement in what should be done or how it should be done. In the area of Workers' Compensation the report of the Advisory Committee made three recommendations:

1. "that workers' compensation be included in the competitive rating law and not be separately regulated in a law which requires mandatory rating organization membership and/or permits members or subscribers to depart from bureau rates only by a 'deviation';

2." workers' compensation insurance rates be subject to a prior filing pro-

cedure before they become effective, but not subject to specific prior approval; and

3." statistical data for workers' compensation insurance be collected on a uniform basis."(3)

The report alleges that workers' compensation does not now qualify for open competitive pricing and precisely because of the laws which now regulate rates in the several states, plus the requirement that insurers must belong to and adhere to bureau rates. The report further points out that workers' compensation is not currently regulated by a competitive rating law in any state;(4) that six states have exclusive State Funds, and that fifteen other states have special laws regulating workers' compensation exclusive of other more general laws regulating property and casualty rates. The other states subject workers' compensation to some form of prior approval or to a waiting period of some kind.

The report states "[t]he present system works well in terms of availability, affordability and the quality of services."(5)

While the Advisory Committee was composed of the heads of the largest nationwide insurance companies as well as representatives of agents, bureaus, consumers and academia, their varied special interests were such that several felt the need to file their own "minority" reports. They were not, of course, called that, but that is what they are. Several of them are worthy of noting both as an indication of the difficulty of obtaining agreement on this subject and as an example of the wide range of thought that leaders in the industry hold on this basic problem of regulation. Let us take a closer look at a few of them.

"Minority" Reports

John S. Trees, Group Vice President Personal Lines, represented Mr. Archie R. Boe, Chairman of the Board of Allstate Insurance Company, who was appointed as a Committee member. In its separate comments(6) Allstate pointed out:

(3) Report of the Advisory Committee on Competitive Rating (NAIC) page 44-45

(4) This statement is questionable in view of the rating laws of Illinois and California (discussed below).

(5) Id. page 43

(6) Id. page 124 et seq.

"While the Advisory Committee seems clearly to endorse the goal of enhanced competition in insurance markets - a goal we ardently share - it is our view that implementation of certain specific recommendations of the report could, in practical application, tend to frustrate rather than further that goal. It is for this reason that we felt it necessary to submit these separate views.

"Initially, we regret that the Committee chose to adopt a regulatory approach more restrictive even than that which has existed for more than 20 years in the State of California - a state frequently cited as a model for competitive improvements. In this connection, we note that we have also reviewed the views of the State Farm Insurance Companies, and, while we cannot endorse at this time any of the technical details of the State Farm proposal, we believe such is in concept more faithful to the goal of advancing competition than is the Advisory Committee report."

A group of Advisory Committee members filed a separate paper specifically directed to Workers' Compensation(7). The group consisted of:

Melvin B. Bradshaw, President, Liberty Mutual Insurance Company

Samuel Fortunato, President, Metropolitan Property and Liability Insurance Company

John W. Joanis, Chairman, Sentry Insurance, A Mutual Company

Robb B. Kelley, President, Employers Mutual Casualty Company

Paul S. Wise, President, Alliance of American Insurers

In their comments they say:(8) "The system of Administered Pricing for workers' compensation has a proven track record of success and service to the public.... The public policy considerations appropriate to workers' compensation insurance differ substantially from those applicable to other property/casualty lines, and warrant broader study and consideration....

"In order to maintain the integrity of the data base, the administered pricing system encourages the use of rating bureau services by insurers, subject in most states to statutory right of deviation. Without the volume of quality statistical

(7) Id. page 128 et seq.
(8) Id. page 129 et seq.

detail now required by rating bureaus and obtained from all insurers, sound actuarial analysis of benefit changes and the determination of creditable rate levels would not be possible. Without uniform input of statistical data to the bureaus, the data base would be diluted and eroded. As the quality of the data deteriorates, there will be a declining incentive for larger insurers with their own sophisticated data processing equipment to submit data. This, in turn, will accelerate the detriment to smaller insurance carriers, which are absolutely dependant on broadly based statistical support. Thus, we believe that in addition to the steps recommended by the committee, it is also necessary to preserve manual rules, rating plans and the classification system, in application; this will require some degree of adherence, now rejected in the committee report.

"Further, we take issue with the committee's decision to eliminate rate service organization adherence requirements. We do not think this is appropriate for workers' compensation. We believe a workers' compensation rate service organization should be able to require adherence to manual rules, classifications, and rating plans."

Perhaps the most incisive "minority" viewpoint was filed by State Farm Insurance Companies, represented on the Advisory Committee by Edward R. Rust, President, State Farm Mutual Automobile Insurance Company. State Farm's comments were thoughtful, extensive, of deep probative value and marked with an objectivity born of conviction in the merit of the viewpoint expressed. While the author does not necessarily agree with the concept that open competitive pricing is desirable for workers' compensation rate making, he recognizes a worthy adversary in State Farm's presentation of the case for market place rate making. State Farm places maximum reliance on competitive forces and presents convincing arguments for that viewpoint. State Farm went so far as to draft a model competitive rating law embodying their concepts of what such a law should contain. Their model

law excludes workers' compensation with the note: "Workers' Compensation insurance is excluded.... primarily because it may be regulated in a separate Article. It is possible that many of the provisions of this Article would be appropriately applied to Workers' Compensation insurance."(9) Since this article is primarily concerned with Workers' Compensation no further comment will be made on State Farm's presentation but the author earnestly recommends a thorough perusal of it by anyone interested in open competitive pricing as a general approach to property and casualty insurance rate regulation.

Several other Advisory Committee members filed papers expressing their views. The consumer advocates, Robert Sable, Executive Director, National Consumer Law Center, Inc., and Sandra L. Willett, Executive Vice President, National Consumers League, generally felt the report did not go far enough in favor of the consumer; Berry L. Griffin, Jr., President, Risk and Insurance Management Society, representing some 3300 corporate members, disagreed with the Advisory Committee's conclusions on Workers' Compensation and argues for even broader open competitive activity in all lines including Workers' Compensation' and Arthur C. Mertz, President, National Association of Independent Insurers also argued that the Advisory Committee's position on Workers' Compensation was too restrictive and that Workers' Compensation should be subject to the same rules as all other insurance lines.

Comments on Advisory Committee Report

As one can see from the above summary of the many viewpoints expressed in the report and in the comments by several Committee members, there is a wide divergence of opinion on the role for market pricing especially as it applies to Workers' Compensation. Historically the large independent carriers are in favor of free and open competition and the old line bureau members generally want to hold onto what they are accustomed to and feel comfortable with. It will not be easy for these two powerful and divergent groups to find a common ground on

(9) Id. Page 176.

which they can agree. The present trend in federal circles to repeal McCarran-Ferguson and substitute a mandatory open competitive law makes a resolution of these basic conflicts not only desirable but as a practical matter, almost imperative if the insurance industry is to present a united front on what to many appears to be a life and death matter. This necessity focuses on the solutions reached in at least two states - California and Illinois. Allstate referred to the California system in its comments on the Advisory Committee report, and State Farm mentioned the Illinois statute as a rebuttal to the Advisory Committee's position that there is no experience available in Workers' Compensation outside the rating bureau experience. What then can we learn from the experience in these two states.

California Workers' Compensation Law

Over 20 years ago California adopted what can be described as a minimum rate law for Workers' Compensation. Under that law, as amended to date, "[t]he Commissioner shall approve or issue, as adequate for all workers' compensation insurers, a classification of risks and premium rates relating to California workers' compensation insurance. He may also approve or issue a system of merit rating,"(10) which must be adhered to by all California workers' compensation insurance carriers, including the State Fund. Merit rating is restricted to California experience and may not be combined with the risks experience in any other state. Any expense provisions included in the classification of risks and premium rates approved by the Commissioner shall be uniform as to all insurers and insured affected thereby. "An insurer shall not issue, renew or continue in force any workers' compensation insurance.... at premium rates which are less than the rates approved or issued by the Commissioner"(11)

The law recognizes and approves rating organizations to collect data helpful in making adequate minimum rates for workers' compensation and employer's liability

(10) Workers' Compensation Law of the State of California, Sec. 11732
(11) Id. Sec. 11736.

coverage and to submit such rates to the Commissioner for issuance or approval. The law authorizes the existence and cooperation of qualified rating organizations and requires every insurer to belong to one such rating organization. Under the law, a [r]ating organization means any organization which has as its primary object or purpose, the collecting of rating information, the making of rates, rating plans and rating systems for workers' compensation insurance and employer's liability insurance incidental thereto and written in connection therewith and presenting them to the Commissioner for issuance or approval."(12)

Rating organizations are given authority to inspect risks to determine proper classification, to make test audits of employer's payrolls and generally to do all the things rating organizations have historically been permitted to do.

In view of the foregoing it is difficult to understand how Allstate would seem to be saying that the California system is closer to an open competitive pricing plan than that proposed by the Advisory Committee. In any event, the California plan has been working for over twenty years so it is at least a workable plan and appears to enjoy the reputation of being, as Allstate says: "a model for competitive improvements."(13)

Illinois Workers' Compensation Law

Illinois has an Article in its law covering Workers' Compensation and Employers' Liability Rates, separate from its rules and regulations applying to Property and Casualty Rates other than Workers' Compensation. A comprehensive policy statement as to Workers' Compensation rates is found in the law under the title - "Purpose of Article":(14)

"The purpose of this Article is to promote the public welfare by regulating workers' compensation and employer's liability insurance rates to the end that they shall not be excessive, inadequate or unfairly discriminatory, and to authorize and regulate co-operative action among companies in rate making and in other

(12) Id. Sec. 11750. 1b
(13) Advisory Committee Report (NAIC) page 124
(14) Illinois Workers' Compensation Law - Sec. 1065.1

matters within the scope of this Article. Nothing in this Article is intended (1) to prohibit or discourage reasonable competition, or (2) to prohibit, or encourage except to the extent necessary to accomplish the aforementioned purpose, uniformity in insurance rates, rating systems, rating plans or practices. This Article shall be liberally interpreted to carry into effect the provisions of this Section."

The law spells out the factors that shall be used in making rates and provides that:

"(1) Every company shall file with the Director every manual of classifications, every manual of rules and rates, every rating plan and every modification of any of the foregoing which it proposes to use."(15)

"(2) A company may satisfy its obligation to make such filings either by making an individual filing or by becoming a member of, or a subscriber to, a licensed rating organization which makes such filings, and by authorizing the Director to accept such filings on its behalf; provided, that nothing contained in this Article shall be construed as requiring any company to become a member of or a subscriber to any rating organization."(16)

"(6) Upon the written application of the insured, stating his reasons therefor, filed with and approved by the Director, a rate in excess of that provided by a filing otherwise applicable may be used on any specific risk.

"(7) No company shall make or issue a contract or policy except in accordance with filings which are in effect for said company as provided in this Article or in accordance with Subsection (6) of this Section."(17)

"Deviations. Every member of or subscriber to a rating organization shall adhere to the filings made on its behalf by such organization except that any such company may make written application to the Director for permission to file a

(15) Id. Sec. 1065.4
(16) Id. Sec. 1065.4
(17) Id. Sec. 1064.4

deviation from the class rates, schedules, rating plans or rules thereof."(18)

Thus the Illinois law breaks with the past at least by recognizing competition as a means of rate regulation and by its provision for filing by individual companies of their rates and by providing specifically that premium rates need not be uniform. This was a substantial variance from any other State law enacted at the time(19) and the reasons for the development of the law along these lines offers an interesting bit of history. For many years the concerted action on rates sanctioned by the approval of mandatory membership in a rating organization by the insurance companies bothered regulators and some members of the insurance industry as being tainted with anti-trust implications. Efforts to make rating organizations advisory only had not really removed the stigma. Further, under open competitive rate laws the insurance industry agrees that certain anti-competitive actions of rating bureaus, especially the right to make rates and file them with regulatory authorities for approval, could not be reconciled with the concept of free and open competition. The NAIC Advisory Committee recognized this conflict but apparently was unable to solve the dilemma. This brings us to the Illinois situation in 1971 & 1972. When the Illinois law that was in effect in 1970 expired, the insurance industry were operating without any rate regulation and were thereby open to anti-trust action under the Illinois equivalent of the Sherman Act. Fearful of the situation it faced the industry prevailed upon the Insurance Commissioner to issue regulations permitting concerted action by the industry. Before doing so, the discussions focused on what essential concerted action was essential and what other areas of concerted action, which had been permitted to authorized rating bureaus, were not essential. Thereupon the Commissioner issued regulations which were later reinforced by the statute passed in 1972 and the reissue of regulations under that statute.

(18) Id. Sec. 1065.7
(19) 1972

As a result of several years' experience under the Illinois "open competitive" rating system, those industry members who advocate this approach claim there is ample proof of benefits to the public without a need for concerted action by the industry regarding rate filing data. Others do not feel there is a sufficiently broad base from the experience of one state to claim success over a long period of time. Those not convinced by the Illinois situation point out that insurance companies have the experience of other large industrial states to use in formulating rates for Illinois and that regardless, the smaller insurance carriers could not operate successfully without the benefit of reliable statistical data that is only available under the present rating organization system of concerted action.

There is no apparent or obvious solution to this fundamental difference in approach and none is likely to be found unless and until some extraneous situation developes, as it did in Illinois, to force an agreement with which neither group would be entirely satisfied. Such an extraneous situation could well be the repeal of McCarran-Ferguson with a distinct possibility of a law requiring open competition. Because of all these uncertainties the efforts of the NAIC to reach some sort of accomodation among insurers is both understandable and praiseworthy. It is this author's private opinion that short of the happening of some compelling event, the liklihood of agreement among the industry giants is quite remote.

Typical of the relevancy of this topic in the minds of the insurance industry leaders, were the remarks of John A. Schoneman, President, Wausau Insurance Companies, at the 4th Annual National symposium on Workers' Compensation held in July 1980 at the University of Maine. He discussed the problem generally and made several points regarding the specific problems involving Workers' Compensation coverage which sum up the position of those who advocate a continuance of the present rating bureau system as far as Workers' Compensation is concerned. Mr. Schoneman pointed

out that as far as competition is concerned that the good and desirable large risks (over $100,000. annual premium) are very competitive[20], pricewise, and will continue to be so under any rate system. However, this cannot be said for the smaller risks which comprise by far the larger number of risks (perhaps as much as 75% of all risks in number) but account together for only a small percentage of total premium, (perhaps only 10% of total premium). He pointed out further that there are many competitive factors built into the present rate structure such as premium discount, dividends, retrospective rating, loss limit and excess loss factors and others. It was also Mr. Schoneman's opinion that the basis for the continued success of the present system over such a long period of time was the sound statistical base used to project losses and expenses. This has resulted in a stability not found in other lines of insurance and this stability encourages new insurance companies to enter the market and thus makes coverage more accessable. Since workers' compensation is a government mandated social program with definite goals, great care must be exercised to make certain any changes made will not adversely affect those goals. Mr. Schoneman does not believe we can say that open competitive pricing will do as good a job as the tried and proven system we presently have. Again since we are dealing with long term loss payments involving human beings we dare not experiment with the rights of injured workers or their dependents without assurance that what we change will result in a better situation - legislators will demand assurances on this point as well as upon the cost effectiveness of any proposed changes. Mr. Schoneman repeats the argument so often made that any dilution of the data base will adversely affect smaller carriers and once lost the reliability of the data base cannot be reestablished. The discussion by Mr. Schoneman was equally as effective in favor of the present system of administered rate making or pricing as was State Farm's "minority" views as expressed in the Advisory Committee (NAIC) Report, in favor of open competitive pricing.

(20) Risks subject to the Longshoremen's and Harbor Workers' Compensation Act are excluded. Generally such risks are not "competitive" except as to how much the charge will be over and above standard rates through various insurance plans.

New York and New Jersey

Amid all the discussion that is going on throughout the country on the question of open competitive rating for Workers' Compensation, it is interesting to note that New York and New Jersey, which are both heavy industrial and manufacturing States, have thus far elected to stay with regulated rating bureau rates for this important line of insurance.

A bill was introduced in the New York legislature (1980 session) (S.4240-A.6210) to amend Section 184 of the Insurance Law which would eliminate the need for approval of the Superintendant of Insurance prior to making effective rates filed by a rating organization or an insurer and which provided that insurers could establish rating schedules which would allow for a reduction of not to exceed fifty percent or a surcharge not to exceed one hundred percent of the rates recommended by the workers' compensation rating board. While neither bill passed this year, their introduction indicates the trend toward unregulated rates that is gaining ground all over the country. However, the idea of a discount and differential limit, while still using rating bureau rates, would be novel were it not for the fact that it is the way the New York State Insurance Fund has operated for over sixty years.

In New York the law established the State Insurance Fund as a competitive carrier to which employers could turn to insure their liability under the law. Since the private insurance industry demanded and retained their right to refuse to insure any risk it did not want, the legislation provided for a State Fund rather than an assigned risk pool or some such other technique. So that the State Fund would not need to be subsidized, the law permitted the fund to establish its own rates which were not under the supervision of the Superintendant of Insurance. It is interesting to note that during the first few years of its existence the State Insurance Fund (New York) did establish its own rates which were different

from those used by the private insurance companies. However, the Fund's representatives soon discovered that the employers were too confused by the different rates being quoted to be able to decide where their coverage could be had at the lowest cost. The Fund then joined the rating board and used the identical rates the private carriers were using but established a fixed advance discount from these rates which averaged 20% and were thus able to quote on identical rates with a definite discount over the private industry. The 20% was arrived at by taking the agents' commission (at that time 15%) and adding the profit allowance built into the rate - 2½% (since by law the Fund had to operate without profit) and 2½% less than the expense allowance in the rates, since the fund was operating in one State with one line of insurance. On the other side of the coin, the Fund established a range of "differentials" or higher rates which it applied to risks with bad experience, generally on a retrospective basis, so that by close attention to accident prevention thereby establishing an average or better experience, the specific risk could "earn" back the extra charge the differential rate created. This system of advance discounts and differentials has been maintained for the sixty odd years the Fund has operated in New York State. In retrospect you might say that the New York State Fund has operated on an open competitive basis for all these years.

The experience of the author as Executive Director of The State Insurance Fund (New York) for over six years (1972-1978) convinces him that regardless of what form regulation of rates takes, as far as the large risks are concerned (21) whether in manufacturing, retailing, construction or whatever, the competition to write these risks is always intense, innovative (e.g. paid loss retros) and often times self-destructive in its intensity. The State Fund over the years was involved in this competition and witnessed first hand the lengths to which one or more of the large carriers would go to cover some of these risks. Typical examples were the several water tunnel

(21) Risks subject to the Longshoremen's and Harbor Workers' Act excepted

jobs carrying water from upstate New York to New York City, the Brooklyn-Battery tunnel, the World Trade Center buildings, the subway tunnel jobs to name but a few. Without a doubt this type of work could not be more competitive no matter what sort of law the carriers operate under.

But of course these jobs represent only a drop in the bucket as far as the number of businesses which need coverage is concerned. At the other end of the scale there are literally thousands of risks whose annual premium is less than $750. These risks designated as small risks are the type the large carriers do not want. The State Fund has over 70,000 such small risks and because it has such a volume of them it was able to computerize this segment of its business so as to minimize the expense factor in handling them and control the loss factor as far as that was possible. While the Fund wrote most of these risks at Board rates, or the rates the private industry used, as their experience justified it they were extended the discount offered to larger risks.

These examples are mentioned to demonstrate that there is a great deal more competition in fact even under regulated bureau rates, or administrated pricing, as some proponents of the present system describe it, than a casual reading of the rules would indicate. True there is concerted action among carriers in membership in and adherence to rating bureau calculated rates, but offsetting this, to a degree not generally admitted by regulators, is the review, delay and often the arbitrary reduction in the request for rate increases that the Superintendants' office makes in the proposals of the rating bureaus.

New Jersey does not have a State Fund but it does have a really independant rate bureau.

Most states use the National Council on Compensation Insurance to collect loss and expense data and file rates for approval by the State Insurance Department. Not so in New Jersey. Its rating bureau under the direction of a Deputy Insurance

Commissioner collects its own data and compiles its own statistics using them to establish rates for use within the State. Among all the discussion about rating bureaus and the need to have reliable statistics little reference is ever made to the detailed and complicated system followed by the bureaus, and which individual companies would have to follow for each company to establish rates independently of rating bureaus. It is not the purpose of this article to get into the details of how workers' compensation rates are established.(22) Suffice it to say it is a technical and special business requiring not only acturial expertise but also sophisticated equipment, a knowledge of underwriting principles and the ability to make judgmental decisions - skills not possessed by the average man on the street, and surely not generally available to small insurance carriers. Businesses in both New York and New Jersey are fortunate to have workers' compensation available from a number of large and small insurance carriers with flexible plans of insurance, suited to a variety of situations and conditions, whose presence is encouraged by an alert, forward looking administration of the State Workers' Compensation laws in these two States The administration of the law is as good or better than that found in many States and the regulation of rates has produced a stable, steady, strong and growing insurance industry that is fully capable of discharging its responsibilities to its policyholders, their injured employees and their dependents.

Conclusions

The report of the NAIC Advisory Committee has been filed and the Subcommittee expects to make its recommendations on the draft model open competitive rating bill before the end of 1980. The industry is faced with a decision that will give direction to the development of workers' compensation coverage over the next several

(22) The author published an article "How Workers' Compensation Rates are Formulated," which appeared in Risk Management, January 1979, and which outlines the various elements involved in this very specialized work.

years. There is a substantial segment of the insurance industry as well as others outside the industry that want a change toward more free and open competition. This uneasiness with the present system is evident even in a monopolistic State Fund State like Ohio. There a Committee has been formed to amend the Ohio law to permit the private insurance companies to compete with the State Fund and also to permit self-insurance. This will require an amendment to the Constitution of Ohio but the Committee feels it has a good chance of success. Since New York State started over 60 years ago with justwhat the Ohio Committee now seeks, their approach seems mild in the light of other demands for open competition.

Whichever way the NAIC's decision goes, whether to take the moderate way included in the Advisory Committee's model law, or go all the way to open, unregulated rates for workers' compensation as State Farm and Illinois Insurance Director Philip R. O'Connor, Chairman of the Subcommittee charged with drafting the model law, prefer, it is the author's opinion that regardless of the type of rating laws that are enacted the good, large and desirable risks will be intensely competed for and the small, less desirable risks will be avoided as far as possible. The medium size risk will be sought after or avoided depending on how near average or better its experience is. In the last analysis the insurer's underwriting judgment, whether it can make a profit on the risk or not, will determine how competitive its bid will be. One thing is fairly certain - the lack of reliable loss statistics will drive business to the large carriers and to the State Fund in New York and will have a tendency to push rates for the undesirable risk with less than average experience to a point that may well adversely affect such a risk's ability to stay in business. This same effect will probably result in other jurisdictions since the same competitive factors exist in all states. Such a result would be a repetition of the experience which followed the general adoption of the multiperil policy. The better business was packaged and the whole bundle was priced as competitively as possible. But the poorer business continued in single

policy coverage and rates increased because the experience of the better business multiperil policies did not get into the data on which the rates for the single line policies were based. Without reliable, complete and extensive data to produce quality statistics, a similar deterioration can be expected in the area of Workers' Compensation rates with a similar result to the less than average and poor risks, especially smaller risks.

For certain, it will take many years to see the full effect of any major change in regulation of rates - just as it will probably take many years for any kind of a model law to be acted upon by a majority of the States. The proposals for changes in rating techniques has started something that will be around for a long time - for the simple but unassailable reason that the topic has no single or correct answer.

Edited Version approved in 11/80 Boston Revision

CORRESPONDENCE/MEMORANDUM

STATE OF WISCONSIN

Date: July 21, 1980 *File Ref:*

To: Insurance Carriers and Self Insurers

From: John R. Byrnes, Administrator, Worker's Compensation Division
State of Wisconsin Department of Industry, Labor and Human Relations

Subject: Promptness of First Indemnity Payments in 1979 Under Worker's Compensation Act of Wisconsin

The 1979 percent of prompt first indemnity payments is at the highest level since 1975. The promptness record for the five year period 1975 -1979 is:

	1979	1978	1977	1976	1975
All Cases	82.7%	78.1%	78.8%	80.6%	80.0%
Insurance Carriers	82.8	77.2	78.2	79.9	79.8
Self Insurers	81.8	84.0	82.9	85.8	80.8
Private	78.6	81.9	80.9	83.0	80.1
Public*	94.9	91.0	87.9	91.8	84.1

My congratulations to the insurance carriers and self insurers who maintained or significantly improved their 1979 rating.

Insurance carriers scoring 90.1 and above by size group (excluding the companies with only 1-3 cases tabulated) are:

Carriers with 50 or more cases

West Bend Mutual Insurance Company	98.9%
Mid Century Insurance Company	94.5
American Guarantee and Liability Insurance Co.	92.9
Regent Insurance Company	92.6
Employers Insurance of Wausau	92.1
General Accident, Fire & Life Assurance Corporation, Ltd.	91.3
Twin City Fire Insurance Company	91.1
General Casualty Company of Wisconsin	90.9
Hartford Accident & Indemnity Company	90.4
Reliance Insurance Company	90.2

Carriers with 25 to 49 cases

Employers Reinsurance Corporation	92.9%
Master Plumbers' Limited Mutual Liability Co.	91.1

* Excluding State of Wisconsin

Carriers with 4 to 24 cases

Assurance Company of America	100.0%
Foremost Insurance Company	100.0
Highlands Insurance Company	100.0
North American Company for Property and Casualty Insurance	100.0
Security National Insurance Company	100.0
The Travelers Indemnity Company of Rhode Island	100.0
Transport Indemnity Company	95.2
American Employers' Insurance Company	94.4
Security Insurance Company of Hartford	90.9

Please refer to attached tables for additional information.

Private self-insured employers scoring 90.1 and above by size groups (excluding the employers with only 1-3 cases tabulated) are:

Employers with 50 or more cases

K-Mart Corporation	100.0%
Wisconsin Gas Company	100.0
Oscar Mayer & Company	95.0
Mirro Aluminum Company	94.1
Milwaukee Transport Services, Inc.	93.8
Evans Products Company	93.3
Pabst Brewing Company	93.2
J. I. Case Company	92.0
Cutler-Hammer, Inc.	91.0
Beatrice Foods Company	90.8
Allis-Chalmers Corporation	90.6
General Motors Corporation	90.4

Employers with 25 to 49 cases

Caterpillar Tractor Company	96.4%
Colt Industries Operating Corp.	91.7

Employers with 4 to 24 cases

Amoco Foam Products Company	100.0
Eaton Corporation	100.0
Envirex, Inc.	100.0
Foremost McKesson, Inc.	100.0
International Harvester Company	100.0
Madison Gas & Electric Company	100.0
Northern States Power Company	100.0
Ryder Truck Lines, Inc.	100.0
Scott Paper Company	100.0
Seven-Up Bottling Company of Oshkosh, Inc.	100.0
Western Electric Company, Inc.	100.0
Aunt Nellie's Foods, Inc.	95.2
Chrysler Outboard Corporation	92.5
Dresser Industries, Inc.	90.5

Public exempt employers scoring 90.1% and above are:

Employers with 50 or more cases

City of Madison	100.0%
Milwaukee Public Schools	100.0
City of Milwaukee	99.7
Milwaukee County	93.7

Employers with 25 to 49 cases

Dane County	100.0%

Employers with 4 to 24 cases

Chippewa County	100.0%
Waupaca County	100.0

Insurance carriers which had a poor promptness record in 1979 will receive a claims handling checklist with this memo to help them assess their claims handling procedures. I would like these companies to comment on the questions asked and to let me know what problems they encountered and how they plan to alleviate them. My address is P. O. Box 7901, Madison, Wi 53707.

I have sent the claims handling checklist to the self insurers which experienced poor promptness records in 1979 in previous correspondence.

A prompt first payment is one in which the time lag between the last day on which the injured or ill employee worked and the date on which the insurance carrier or the self-insured employer sent or delivered the first indemnity payment to the injured or ill employee was 14 days or less. Cases in which salary was continued are also considered prompt. Some of the larger public self insurers continue salary payments during temporary disability. This practice brings up the promptness ratio. because salary payments are considered prompt first payments.
A self-insured employer is a subject employer exempt from insuring all or part of his liability as provided by the Worker's Compensation Act of Wisconsin. Injury cases protected by excess insurance are classified with self-insured employers.

The attachments to this memo are:

Tables 1A and 1B which rank insurance carriers and self-insurers by promptness record by size of company in terms of number of cases tabulated.

The Index is an alphabetic list of the insurance carriers and self insurers and their percent of promptness for 1979.

Promptness checklist for insurance companies which had more than three cases tabulated and had less than 80.0% prompt first payments.

In 1977, the former administrator of the Worker's Compensation Division asked 66 insurance conpanies and 13 self-insurers which had pay lag rates of between 3.0% and 77.3% to report on their claims handling procedures and to find ways to improve their performance. The acceptable level of performance is 80.0%.

Sixteen of the 66 insurers and ten of the 13 self-insurers raised their performance levels in 1979 into the 80.0% to 96.4% range. All of these carriers and employers are to be commended on their improved payment delivery systems. They are:

Insurance Carriers	1979	1977
American Employers Insurance Company	94.4%	65.8%
Master Plumbers' Limited Mutual Liability Co.	91.1	62.9
Twin City Fire Insurance Company	91.1	69.4
Security Insurance Company of Hartford	90.9	51.7
Liberty Mutual Insurance Company	86.2	77.3
Vigiland Insurance Company	85.7	72.4
The Ohio Casualty Insurance Company	84.6	59.7
Continental Insurance Company	84.0	74.2
Tower Insurance Company. Inc.	83.7	70.6
Threshermen's Mutual Insurance Company	83.5	70.3
Maryland Casualty Company	82.3	71.9
Atlantic Mutual Insurance Company	81.5	69.9
American Universal Insurance Company	80.9	76.6
St Paul Fire & Marine Insurance Company	80.3	65.1
Transport Insurance Company	80.2	76.3
The North River Insurance Company	80.0	72.6
Self Insured Employers		
Caterpillar Tractor Company	96.4%	77.1%
J. I. Case Company	92.0	72.0
Colt Industries Operating Corp.	91.7	69.1
General Motors Corporation	90.4	50.3
A. O. Smith Corporation	87.2	70.4
Sears, Roebuck & Company	84.4	76.3
Borden, Inc.	84.4	76.3
Armour & Company	82.5	67.1
American Hospital Supply Corp.	81.7	71.8
Consolidated Freightways Corp. of Delaware	80.0	76.6

The following insurance carriers have improved their performance measurement significantly in the last half of 1979 and are expected to continue the upward trend in 1980.

	Last Half 1979	1977
Bituminous Fire and Marine Insurance Company	90.4%	69.6%
Aetna Insurance Company	83.7	69.4
Shelby Mutual Insurance Company of Shelby, Ohio	82.1	78.6
United States Fidelity & Guaranty Company	83.8	70.8
Fireman's Fund Insurance Company	80.0	74.0
Lumbermen's Underwriters Alliance	85.0	40.8
Universal Underwriters Insurance Company	38.9	54.3
Milwaukee Mutual Insurance Company	80.1	54.2
Transcontinental Insurance Company	83.3	71.8
West American Insurance Company	84.2	75.0
National Surety Corp.	81.3	65.6

The remaining 40 insurance carriers did not achieve a noteworthy improvement. However, several of these insurers have been making efforts to improve their systems of payment deliveries. Their efforts should become more apparent in 1980.

The department's monitoring program for carriers and exempt employers will be continued on a quarterly basis. However, individual reports to companies will be discontinued. Companies which continue to have poor records will be contacted. Performance rates will be available on request. If profiles of your injury claims could help isolate problems that are hampering your efforts to improve your benefit delivery systems, they are available under certain circumstances. Please direct specific data requests to Ruth Wilson, P. O. Box 7946, Madison, Wi 53707. Telephone No. 608-266-0317.

Attach.

Insurance Bills May Rise for Many Firms As Poor Profits Force Insurers to Lift Rates

By CYNTHIA SALTZMAN
Staff Reporter of THE WALL STREET JOURNAL

From the trenches of the insurance industry, Donald E. Bell looks out on fighting of an intensity he has never seen before.

An insurance broker in the Melville, N.Y., office of Alexander & Alexander Services Inc., Mr. Bell watches property-and-casualty companies battling for commercial insurance business by slashing premiums as much as 70%. Recently, he looked around for quotes on renewing insurance on a fleet of trucks—a policy that last year cost $450,000—and found a company offering the insurance for as little as $180,000.

"That's insane," Mr. Bell says. "The losses were higher than that."

Insane or not, there isn't any question that the largely unregulated commercial insurance market is in turmoil. And the cutthroat competition, some observers say, is setting the stage for a backlash in the industry—a backlash that may lead to higher premiums for businesses and thus higher prices of products and services for consumers.

Boom-and-bust cycles have whipped the property-and-casualty insurers around for decades. But observers say the current turmoil differs from seemingly similar periods in the past. For one thing, there are more players — among them foreign insurance companies that are based in countries with strong currencies and are stepping up their U.S. operations.

Too Much Capacity

"There's too much capacity chasing too few premiums," says John H. Bretherick, executive vice president of Continental Corp., an insurance holding company based in New York.

But perhaps the most important force aggravating the competition is the huge income being reaped by property-and-casualty companies from their investments. Traditionally, insurers have split their business into, on the one hand, the operation of taking in premiums and paying out claims and, on the other, investing premium dollars in stocks, bonds and real estate.

In recent times, high returns on investments seem to have made many insurers willing to write money-losing policies just to get more cash to invest. Last year, for example, stockholder-owned insurers lost $1.4 billion on underwriting but posted net income exceeding $5 billion—thanks to the $6.7 billion earned by investing capital, surpluses and reserves set aside to cover insured losses by policyholders.

This "cash-flow game" is played primarily for the high stakes involved in insuring corporate giants whose six- and seven-figure premiums, cut-rate or not, are eagerly sought as investment fodder. By contrast, the relatively small premiums paid by individuals for property-and-liability insurance have remained immune to rate-cutting; indeed, they have been rising.

Auto-Policy Problems

But not enough to satisfy the insurers. Auto coverage, which makes up 25% of the business of stockholder-owned insurers, and homeowners' insurance are state-regulated, and premiums for both haven't kept up with inflation's effect on claims. For example, the cost of automobile claims—in line with the surging cost of health care, auto parts, legal fees and labor—has climbed 16% this year, while auto-policy rates have risen less than 10%.

Because of that disparity and the fierce competition for commercial insurance business, the industry's earnings are beginning to suffer. In this year's second quarter, overall profits of stockholder-owned companies were flat, and operating income fell 9% at Aetna Life & Casualty Co., 14% at Safeco Corp. and 30% at Ohio Casualty Corp. Profits are expected to deteriorate further.

"The accumulated ravages of exceptional rate-cutting and inflation will show most Cushman, insurance-stock analyst at Morgan Stanley & Co.

For 1981, some analysts are predicting at least a 10% drop in insurance-company earnings. Robert Brian of Conning & Co., a Hartford, Conn., firm specializing in insurance-stock analysis, sees the industry's "combined ratio"—the bench-mark statistic measuring claims losses and operating expenses against premiums—climbing to 104% of premiums by year-end and to about 109% in 1981.

Some Optimists

However, many insurance executives and securities analysts expect a turnaround in 1982. One such optimist is B.P. Russell, chairman of Crum & Forster, an insurance holding company based in New York. "We'll really see action to harden prices next spring after insurance-company boards review the 1980 underwriting results," he says.

Mr. Russell adds: "Once you lower underwriting standards, you can't accurately predict where loss ratios will top out. If you don't keep the pressure on to have profitable underwriting, you wish to hell you had." At Crum & Forster, such pressure is applied by means of cash bonuses paid to individual underwriters on the basis of the company's underwriting results alone, apart from its investment income.

But others expect the rate-cutting to extend into 1982—with an increasingly devastating effect. Inflation, the pessimists argue, will keep pushing up claims costs while competition and a lag in rate increases will slow the growth of premiums; and the smaller cash inflow, combined with interest rates considerably below those last spring, will retard gains in investment income. For example, Donald Franz, a securities analyst at Smith Barney, Harris Upham & Co., predicts that the insurance industry's after-tax investment income will grow only 13.6% this year, down from the 1979 record of 26%.

Danger Ahead?

Conning's Mr. Brian says inflation and some large catastrophes next year could throw some small insurers into financial trouble. Companies may continue to lose money on underwriting, he says, until they see return on equity falling to "an unacceptable level" such as 10%.

In fact, Mr. Brian observes, the industry may be accepting underwriting losses as normal. "The big question is whether cycles will be the same in the future," he says. "Will the industry return to making money on insurance or breaking even, or will it accept a whole new level of underwriting loss?"

That question can't be answered readily by looking at history. In past cycles, investment income was much smaller in absolute dollars and less of a cushion for underwriting losses. "This time," says James J. Meenaghan, executive vice president of American Express Co.'s Fireman's Fund Cos. in San Francisco, "investment income may be clouding some people's view."

What worries Mr. Meenaghan and others is the persistence of intense competition. Indeed, without an outside shock such as a stock-market collapse, says Barbara D. Stewart, a Chubb Corp. economist, the current downturn "will be like a bad toothache. It will stretch out for a long time—longer than the last downturn," which went on for three years.

Trouble in 1975

That underwriting plunge, which reached bottom five years ago, is remembered with a shudder by insurance executives as the worst period in the industry's history. In 1975, the stockholder-owned firms posted a $3.2 billion loss on underwriting, and earnings fell to $100 million. The combined ratio hit 109%, the highest since 1906, the year of the San Francisco earthquake.

But, Ms. Stewart says, "it wasn't simply bad financial results" that prompted the industry's plunge. "Inflation soared, the stock market went down the tubes, and the surpluses were disappearing. Geico (a large insurance company) almost went bust, and insurers saw exotic liabilities losing money. A number of companies said, 'Stop the music!' "

The result: Many insurers became more selective in writing policies and in some cases bailed out of unprofitable lines. Moreover, rates for certain types of insurance, such as medical malpractice and some product-liability lines, jumped as much as 200% to 300%.

In reaction, many corporations, unable to get coverage, began to set up their own insurance operations to self-insure plants, employes and products—a move that has continued. (Such captive insurers, by later seeking outside business, have intensified the current competition among commercial insurers.)

A Boom Begins

Nevertheless, the insurance industry's tougher policies set the stage for the boom that began in 1977. Because of increased premium rates and the growing demand for coverage, revenues from premiums soared 21% in 1976 and 19% in 1977. Once again, the industry was making money on insurance; at the same time, it was raking in sharply higher investment income.

But it was the desire to fuel that investment income, of course, that led to today's frenzied rate-cutting. The lure of sizable amounts of money to invest, along with an increasing number of people seeking insurance to protect themselves against a surge in lawsuits involving allegedly faulty products and professional negligence, has also contributed to the industry's gradual switch away from property coverage toward more liability insurance. With such "long tail" insurance, companies can hold liability premiums for many years and thereby maximize investment income; a product-liability claim may take five or six years to settle, while a claim for, say, a damaged fence is paid relatively promptly.

By taking on more liability insurance, some observers say, companies are accepting a higher level of risk. And Ernest G. Jacob, an analyst at Alex. Brown & Sons, a Baltimore-based securities firm, says it is difficult to estimate the cost of claims five or six years into the future even without trying to guess the rate of inflation. Consequently, he says, "Loss-reserve adequacy is more critical than it was in the past." He adds that today insurers on the average maintain loss reserves amounting to 99% of earned premiums, a big jump from 65% in 1969.

More Reinsurance

And to reduce their risks in certain lines, insurers are turning more and more frequently to the reinsurance market. Today, for example, with reinsurance cheap and easily available, a small insurer can take on a $1 million policy and "lay off" as much as $900,000 of it on reinsurers—and thus spread far more of the risk among other companies than it could in the past. By, in effect, splitting up insurance policies in this way, insurers can take on risks that they ordinarily would have avoided. The current oversupply of reinsurance contributes to the competitiveness of the primary-insurance market because it enables insurers to write larger policies.

Given the insurance industry's cyclical nature, the currently soft insurance market undoubtedly will harden eventually, despite the increased reliance on investment income.

"I think these cycles are healthy for the business and the economy and certainly for the consumer," says Crum & Forster's Mr. Russell, whose views may be colored by the fact that his company's profits recently have been among the best in the industry. "A well-managed firm can manage in down cycles," he adds. "If it can't, it ought to get

SOME OBSERVATIONS ON PROFITABILITY

1. Any insurance can be written at an underwriting loss and still show a profit. In fact, nationwide all lines (aggregate) and comp did precisely that for the past two years. (Note Wall Street Journal, Sept. 23, 1980).

2. This is particularly true of workers' comp because it is a long-tail line.

> ...on a longer-tail line of business, then, your underwriting tends to be skewed negatively. You tend to have an underwriting combined ratio in excess of 100. You tend to lose money in underwriting (a) because you've got much bigger investment income subsidy, and (b) because you're pricing your product further away from the event. . .
>
> (on a short-tail line)...your underwriting tends to be skewed positively....you're not making very much money on investments so you better be making it on the difference on underwriting or why are you in the business in the first place....
>
> -- Donald Kramer, Kramer Capital Consultants, to Minnesota Workers' Compensation Study Commission, Sept. 3, 1980

3. It has been asserted that reserves go up in good years, masking profits. . . . and that for nationwide companies, over-reserving in one locale could be masked by a poor showing in other areas.

> -- Comments of one insurance executive to this writer during fact-finding mission

4. Companies claim they don't make money on workers' comp and they're going to leave the state. Yet the remain and continue to compete for business in the Lower 48.

> The insurance industry is so anxious to get into Washington state to write workers' comp that some companies -- including one of the major comp writers in Alaska -- have retained the former Director of Labor & Industries and Special Assistant to the Gov. of Washington to lobby for a law permitting entry.

5. Between 1955 and 1974 the nationwide ratio between reserves and premiums changed little, but there was a pronounced shift from unearned premium reserves to loss reserves. Over the same time ratemaking in a number of states began to consider unearned premium reserves. Marine insurance -- not regulated -- showed no such trend.

> -- Bell Journal of Economics, 1979(10):1, p. 189.

ALASKA EXPERIENCE WITH WORKERS' COMP -- GENERAL OBSERVATION

1. Carriers claim they're losing their shirts on comp in Alaska.
2. Although the last two years appear to have been bad ones for Alaska comp carriers (if one accepts the confusing best available figures), workers' comp in Alaska has shown an operating profit in four of the last seven years. In three of those years (1973, 1975, 1977) the carriers' operating profit exceeded the loss recorded in the worst year (1978).
3. Although the carriers did not complain publicly when they pocketed a 10% operating profit on the money employers paid them for underwriting workers' comp -- nor did the carriers offer to share their gains -- they were far less willing to absorb a much smaller operating loss in 1978-79.
4. During the 1970's the state's largest comp carrier grew rapidly, increased its domination of the comp market and, fuelled by a pipeline contract its controller called "profitable," opened offices in Seattle, Boise and Portland, moved into California and was at one time reported opening in Alaska. During the same period claims service lagged and the state administrative structure was innundated with boom-generated cases.

(3.) • FINDINGS / PROFITABILITY
Dec. 13, 1980

Recommendations

1. Institute a viable profits-tracking system for workers' comp in Alaska. Such a system might incorporate elements of Minnesota's Form I-57 ("Workers' Compensation Experience Exhibit") and/or the Florida 1980 Excess Profits Test.

   Comment: Despite its importance (in this writer's estimation), Amendment #5 of "Work Draft Paper" submitted to this Study Commission (a general sentence requiring an undefined profits report) was not placed on today's agenda by the Insurance Subcommittee.

   In view of carrier resistance to providing the information sought in Minnesota (it's too soon to tell in Florida), and given the lack of staffing in the Division of Insurance to closely monitor such a report, the Legislature should consider (1) refining Amendment #5 to close loopholes, and (2) adding a staff person in the Division of Insurance to study workers; comp profitability. (Note: Such a study could be required by the Division and the cost plowed back into the rate structure, as is the custom.)

2. This Study Commission should look closely at reserving practices of Alaska workers' comp carriers, and at the question of profitability.

   Comment: If it is found that workers' comp is in fact profitable in Alaska, this fact should be widely publicized to encourage carriers to compete in this market.

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS REPORT ON PROFITABILITY

LINE / YR	ALASKA PREMIUMS EARNED (= 100%) $	INVST GAIN %	LOSS INC %	LOSS ADJ EXP %	GEN EXP %	SALES EXP %	TAXES LIC & FEES %	DIV TO PHDRS %	FED INC TAX %	UNDER WRITNT PRFT %	OPER-ATING PRFT %	U.S. OPER-ATING PRFT %
WC / 79	73,994	9.4	86.7	11.7	6.8	8.8	3.9	0.8	-6.1	-10.1	-3.3	5.3
WC / 78	107,110	9.0	95.8	9.3	6.3	7.3	3.5	0.4	-8.4	-11.8	-5.3	3.3
WC / 77		8.8								1.5	7.4	1.2
WC / 76		7.8								-2.1	3.4	1.7
WC / 75		7.								---	10.	3.
WC / 74		2.								---	-2.	2.
WC / 73		5.								---	8.	3.

Source: NAIC Data in reports on file at NAIC, Milwaukee, Wis.

Compiled by R.A. Fineberg
Alaska Workers' Compensation Study Commission

Fineberg / Comp Profitability Analysis
Dec. 13, 1980

(4)

A. Background: Litigation Costs, Patterns

The percentage of the comp premium bill directly attributable to litigation is not readily available. There are, however, some interesting statistical ways to back into the subject:

1. Loss Adjustment Expenses as % of Premium[1]

	Workers' Comp	All Lines
Countrywide	8.6%	9.4%
Alaska	9.3%	8.6%

Comment: These figures could mean many things, but it seems probable that Alaska's higher rate of loss adjustment expense than both the national average for workers' comp and the statewide average for all lines is a result of litigation: The difference isn't overhead and the most likely variable appears to be litigation.

2. Legal Costs in Litigated Cases: California

The case in which an Application for Adjudication was settled in 1978 in California cost $1941 in legal fees, compared to $6102 in average total awards.[2]

3. Controverted Cases in Alaska

1,323 controverted cases were resolved in Alaska during FY 1979.[3]

4. For ballpark purposes, let's assume the California legal costs apply to Alaska and multiply:

1,323
(x) 1,941
$2,567,943

Comment: This figure (25.7% of the loss adjustment expenses, according to the NAIC report) may be hig -- or it may be low. If I had to guess, I'd say give or take a million dollars, giving a SWAG of $1.5 to $3.5 million for legal expenses arising DIRECTLY from comp appeals procedures per year.

This figure -- however inadequate it is -- is only part of the picture on litigation costs. The state bears the administrative costs of the appeals procedure. It is generally accepted that litigation works against the claimant's healing process, thereby adding to maintenance, medical and rehabilitation costs while prolonging the period in which the claimant is not doing whatever it is he/she did before the accident.

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1 NAIC Report on Profitability By Line and By State for the Year 1978 (National Assoc. of Insurance Commissioners, 1979), pp. 12-15.

2 1978 Legal Cost Study (Caligornia Workers' Compensation Institute, April 1979, mimeographed tabulation of forms on 2642 cases filled out by 28 insurer groups)

3 Figures from State of Alaska, Workers' Compensation Division.

It may not be appropriate to look at litigation in terms of the admittedly modest reduction in premium prices that would appear to result from reduced litigation (if the crude estimates on the preceding page are an accurate reflection of reality): Workers' comp is a system of service delivery and a high degree of litigation indicates that delivery is not going smoothly. Who litigates, and what are the effects?

(1) It has been reported that a major carrier once instructed its adjustors to controvert every major claim, regardless of merit.[1]

(2) Documented reports of apparent patterns in carrier controversion on permanent partial disability cases have been reported.[2]

(3) In addition to controversion, the Division of Workers' Compensation estimates that carriers informally resist as many cases as they controvert.[3] Informal resistance may contribute to the number of late first payments, reported by the Division as totalling 72% of 3,889 first payments in a 1978 tally.[4]

Comment: In contrast with Alaska, which ignores both the spirit and the letter of AS 23.30.155(b) and (e), which require prompt payment and prescribe penalties for carrier failure in this area, some states actively enforce this aspect of their comp law. The Wisconsin Worker's Compensation Division tabulates first payments by carrier, ranks the carriers and publishes the tabulation in a memo to all carriers congratulating the firms that both head the list and show improvement. In 1979 82.7% of all first payments were made promptly, in Wisconsin -- and the five-year average for all carriers was 80%.(The corresponding figure in the Alaska tally was 28%.) [5] New Hampshire is similarly conscientious in penalizing delays and rewarding good performance: the leading carriers are honored at a banquet at which the Governor makes an award. [6]

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1 Statement of a senior claims adjustor with that carrier to the author in November 1979.

2 See author's report to House Labor & Management Committee, Jan. 21, 1980.

3 Report to Alaska Workers' Compensation Study Commission by Diane Simonson (summarized in memo to Sen. Terry Stimson, Sept. 16, 1980).

4 Alaska Workers' Compensation Division 1978 IAIABC tally.

5 "State of Wisconsin, Correspondence/Memorandum To Insurance Carriers and Self Insurers," July 21, 1980.

6 Interview with June Robinson, Assoc. Dir. for State Workers' Compensation Standards, USDL Office of Workers' Compensation Programs (Washington, DC, Nov. 10, 1980).

(4) A 1974 study by the California Workers' Compensation Institute[1] discovered that:

-- 92% of all litigated cases were first injuries; most were unfamiliar with the comp system.

-- unions encouraged 80% of their claimants to get a lawyer;

-- most frequent lawyer contact took place after the first contact with employer, physician, insurer -- and first payment.

The report described a characteristic litigation scenario:

> A low-paid, relatively uneducated employee with a dependent personality (and a one in four chance of having an English language handicap) has an accident at work and receives what he believes is a serious injury. His employer, for whatever reasons, does not reduce his anxiety by assuring him his medical bills will be paid and that he'll receive wage-replacement benefits until he's able to return to work. His treating physician doesn't explain what is happening and what will happen. He may be contacted by the insurance company but the representative is defensive and seems unwilling to answer questions. Finally, he receives a check, less than his usual wages, attached to a legalistic form he can't understand but which does tell him he has the right to consult an attorney.

The California report on legal costs contains another interesting piece in the litigation puzzle: 41.9% of all litigated cases involve back injuries.

(5) To summarize, Alaska's carriers have an abysmal record on prompt payments. To date no entity with resources and authority to investigate reports that such payments may constitute a trade practice has seen fit to do so. On the other side of the fence, the claimant litigates when he/she is uncertain about how to cope with the workers' comp problem.

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[1] "Litigation in Workers' Compensation: A Report to the Industry," California Workers' Compensation Institute (n.d.).

B. Recommendations

One of the basic legal premises from which the workers' compensation system has evolved is that the worker gives up the right to bring suit against his/her employer for negligence in exchange for prompt and efficient payment for wag loss and medical treatment. From this widely-accepted starting-point the high degree of litigation in the workers' compensation system is contradictory. Alaska's workers' comp system may have a higher litigation rate than average -- and there are some indications that a portion of that litigation may be induced by carrier trade practices. This overview leads the author to the following recommendations:

1. AS 23.30.155 provisions requiring a 20 per cent penalty for carrier failure to make first payment by 14th day (b), notify board of suspension of payment (c), failure to pay award within 14 days (f) should be enforced.

   Because the Workers' Compensation Division is not able to process claims in an expedited manner, a form letter advising claimants of this and other relevant provisions of the law should be sent to each claimant when injured. This procedure should be implemented immediately and should be picked up by the computerized system when it comes on line.

2. The Workers' Compensation Division should tabulate carrier payment records and honor prompt payment and improvement in the manner of Wisconsin and New Hampshire, described above.

   Comment: Reward of prompt claims payment would be a selling point for carriers competing for workers' comp business. Additionally, prompt payment would reduce claimant tendency to litigate, saving the carrier loss adjustment expenses.

3. California and Florida have added staff specifically assigned to give claimants information, facilitate their claim problems, on the theory that the outreach program will reduce time-consuming and costly litigation. Author does not recommend this approach. Wisconsin accomplishes the same goal through form letters, dispatched almost automatically when claims-handling norms are not met.

   Note: If brochures advising claimants of their rights cannot change the claims-handling climate before the computer system comes on line, perhaps a program of public service announcements could fill the gap. In any event, the Wisconsin experience demonstrates that it is not necessary to hire bunches of people to inform claimants and encourage carriers to make prompt payments.

4. In view of (a) the long delays involved in the hearing schedule, (b) the cost and logistical difficulties associated with the three-person hearing system, and (c) the complex nature of the controverted cases, which require medical and legal expertise, as well as attention to the detail of each particular case, the Legislature should consider repealing AS 23.30.005(f) ("Two members of a panel constitute a quorum for hearing claims") and other statutory legal barriers (if any) to the replacement of the initial hearing by a three-person panel with a hearing by a lone hearing examiner whose decision could be appealed to the three-person board.

   Comment: The Division of Workers' Compensation could promulgate the appropriate regulations once the necessary deletion(s) in the law was effected, thereby streamlining still further the litigation process.

5. In view of the high litigation over back injuries and the difficulty determining degree of disability, Alaska litigative experience should be examined -- by study of specific cases with interviews of all parties -- to determine the best way(s) to make this process more efficient. I have not done sufficient interviewing and observation of the process in Alaska to be confident of the best changes to adopt, but it is my impression[1] that specific goals of proccedure revisions might be:

   (a) Doctor rates impairment, or specific loss of function (note: this is a medical term, established by fixed criteria such as A.M.A. guidelines, i.e., 6-degree motion of limb = X% impairment)

   (b) Carrier/claimant determine disability (effect on earnings, based on a range of non-medical factors such as age, occupation, change in job, etc.).

   The guiding principle here is to have the doctor perform as a technical specialist within his field of competence, not as an adversary or social/legal expert.

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[1] Guideline was introduced to me by Alan Tebb, General Manager, Calif. Workers' Compensation Institute (interview 11/7/80), re-inforced by Sen. Steve Keefe, Chair, Minnesota Workers; Compensation Study Commission (interview 11/10/80). See also "Promptness of Payment in Workers' Compensation," Bernard N. Samers and Dorothy I. Kelly, (Research Report of the Interdepartmental Workers' Compensation Task Force, Vol. 3: Washington, D.C., Government Printing Office, 1979).

GOODGUY INSURANCE COMPANY: A COMPETITIVE COMPANY[1] (BACKGROUND, INTERVIEW NOTES)

How the good little guy beats the big insurance companies on workers' comp by running a tight ship.

I. Introduction: From the Annual Report for 1979

"It's always a pleasure to report on another successful year . . . . Our budgeted goals were exceeded, both in premiums written and in patronage dividends declared. For the fifteenth consecutive year, substantial dividends have been returned to the policyholders as additional savings on their insurance premiums. This past year's dividend of 18.9% was the largest ever paid. . . .

"Goodguy probably could have grown faster than it has, although we are very pleased with the growth level that has been achieved. However, it was decided long ago to match the company's growth with its ability to serve. . . .Carefully conceived, and slowly expanded, we have earned a reputation for providing quality insurance . . . at the lowest possible cost -- in a difficult marketplace."

II. Background

Goodguy has carved a place for itself writing in relatively isolated rural areas, where it has undercut the large carriers -- and earned a handsome profit in the process. About 40 per cent of Goodguy's business is workers' comp. Goodguy serves a limited market: its customers are shareholders who started the company when they became dissatisfied with the rates and services of the dominant carrier(s).

III. Q.: How do you beat the big guys? A.: "Keep expenses down."

(Note: It is not clear from Goodguy's experience what effect -- if any -- deregulation would have had; it is clear that Goodguy undercut the big guys in a standard, regulated comp market.)

A. Don't live in marble mansions.
   1. We don't have big sales commissions -- we have employees make the sales. We're a direct writer. (Note: With the exception of Ohio, Alaska and Hawaii are the only two states where direct writers account for less than 10% of the business. Western states are generally in the teens, with a national average of 25.7% direct writing.)
   2. I think big companies have become accustomed to a different style. Executives with 7-room suites, company jets fly several hundred miles to pick up the executive's wife's purse (I actually saw this happen myself).

B. Don't hide money in reserves.
   1. Reserving is the major diference. You can only fatten expenses so much.
   2. We began writing at a $3.67 manual rate. Within six years we were down to $1.28 -- returning an automatic 10% on the policy every year, plus the year-end dividend. A part of that cost cut was due to our honest reserving of claims.

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[1] Name changed. Company president is willing to be identified if necessary but prefers anonymity.

III. "Keep Expenses Down" (cont.)

B. Don't hide money in reserves (cont.)

3. I don't know that big companies can do anything else -- they insist it averages out -- but I am of the opinion that they over-reserve. That gives them more investment income but it also moves the rates up. When you don't have a lot of competition it's a lot easier to raise rates. For a company that's having a good year, you pass the word down the line in relatively soft terms -- and pretty soon those reserves are going up. And who can say what IBNRs are supposed to be?
4. Where you hide profit is by reserving high across-the-board. IRS watches reserves, but IRS has to wait ten years -- you've got to let all those claims pay out, then take a look at it to find the redundancy. And for a company operating in Alaska, you could be over-reserved in Alaska and under-reserved in Pennsylvania and it would balance out.
5. I'm not sure the actuaries aren't throwing in some figures they don't need to. The last 2-3 years have been good years, despite the (pay-out) rates going up faster than (policy) costs. Either we've been terribly lucky or . . . I don't quite know why; I can't put my finger on it. (Maybe our bubble is going to burst, but our competition has been saying that while we've been beating them for every year one of the past 20 years.)

C. Policy selection

1. We don't have a lot of little policies. Our premiums range from $5,000 to $200,000. It costs no more to type the policy for $100,000 than for $5,000. But you have to have a raft of people to write any policy.
2. We are stock-owned and we insure the owner companies (as indicated above). We know our people and they know this is a cooperative venture, so they don't try to cheat us.

IV. Q.: What would it take to get companies like yours in Alaska?

A. Make it easy to apply for a license. We began writing in State X this year. The state said it was too busy to get out license processed, but clients in-state began hollering. When they put the pressure on, <u>then</u> we got our license.

B. It's my guess that you could attract a company that's big in workers' comp if you could promise a certain percentage of the market.

C. One of our competit[illegible] says they're losing their shirt on comp in Alaska, and they'd like us to take it off their hands. I'd like to try; we've been doing things the industry said couldn't be done for 20 years -- and beating them. I almost wish I had the time to do it (but) other expansion keeps us tied up.

V. Miscellaneous Points

A. We can't back out our by-state costs for you (but) I think the big companies could. Branch offices would have their own balance sheet, probably by branch office and by line; it would surprise me that if they wanted to break it out they couldn't.

B. (Mentioned two states with very different court stances on workers' comp; cited litigation and benefit increases as reason one state is much higher than the other; then said Goodguy reserved similar cases in the two states identically. When I questioned this, he called in his reserving specialist -- and found out he was wrong. Second state may be reserved 5-10% higher in some cases in the expectation of a higher pay-out on a big claim.)

C. (Assigned risk pool: Higher premium and lower commission. A big co. that dropped a risk would get it back -- with higher premium to make up for the commission, and the risk spread to other carriers in the pool.)

SOME QUESTIONS CONCERNING OPEN RATING OF WORKERS' COMPENSATION IN ALASKA

Prepared by Richard A. Fineberg, based on information gathered during a fact-finding mission conducted for the Alaska Workers' Compensation Study Commission, Oct. 31 - Nov. 26, 1980

Presented to the Alaska Workers' Compensation Study Commission, Dec. 13, 1980

I. General Premises

A. Taking Risks [1]

Insurance involves the assumption of risk by the carrier.

1. Known Risks

When risks are known and all other factors are equal, if the risk on insuring Employer A is higher than for Employer B, carriers will seek Employer B's business. This translates into higher premium rates for Employer A.

2. Unknown Risks

Uncertainty equates with increased risk. Anything that makes it more difficult to assess the risk on a policy tends to increase the premium rate.

B. Making Money: Long-Tail and Short-Tail Lines [2]

1. The carrier assumes risks to make money.
2. The carrier makes money in two ways: (a) profit on the policy and (b) profit on investment income.
3. Workers' compensation is what the industry calls a Long-Tail Line. This means the carrier holds relatively large portions of the premium for relatively long periods of time. The resulting investment income from these reserves is a more significant economic consideration in workers' comp than it is for Short-Tail Lines, such as a home-owner's policy on which the major portion of a claim is paid during (or shortly after) the period the policy is in force. The profit on investment income is one reason why workers' comp traditionally has a lower profit factor in its rate base than a short-tail line.

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[1] For concise statement of the concepts of risk and uncertainty, see Fred Collingnon, "Estimating and Financing the Costs of State Workers' Compensation" (Research Report of the Interdepartmental Workers' Compensation Task Force, Vol. 3, 1979), fn. p. 45.

[2] For introduction to short- and long-tail lines, and their significance to workers' comp, see presentation to Minn. Workers' Compensation Study Commission by Donald Kramer, Kramer Capital Consultants, Sept. 3, 1980.

II. Application of General Premises to the Alaska Workers' Comp Market

A. Risks

1. Known Risks

From the carrier's point of view, it can be assumed that, all other things being equal for known risks, a small employer is less desirable than a larger employer. Two reasons for this are (a) the possibility of the big accident and (b) the cost of procuring/processing the policy. Even when the risks are known, the small policy is inherently riskier. But often the small policy risks take on characteristics of unknown risks.

2. Unknown Risks

Because of its small aggregate data base and its geographical isolation, Alaska's risks tend to be more difficult to assess than similar risks in the Lower 48. (A measure of the difficulty in assessing Alaska risks is that experience from other states must be used to calculate various Alaska manual rates. States with an adequate data base for all industries, such as California, allow no dilution of their statistics with data from other states.)

B. Making Money

If the risks are so great in Alaska, why would any carrier want to write workers' comp? To make money. Where does most of that money come from? Investment income. Carriers will compete -- even write policies at a paper loss -- to obtain investment income. Note the following from a recent Wall Street Journal article:[1]

> In recent times, high returns on investments seem to have made many insurers willing to write money-losing policies just to get more cash to invest. Last year, for example, stockholder-owned insurers lost $1.4 billion on underwriting but posted net income exceeding $5 billion -- thanks to the $6.7 billion earned by investing capital, surpluses and reserves set aside to cover insured losses by policyholders.

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[1] "Costlier Coverage: Insurance Bills May Rise for Many Firms as Poor Profits Force Insurers to Lift Rates," Wall Street Journal, Sept. 23, 1980

> This "cash-flow game" is played primarily for the high stakes involved in insuring corporate giants whose six- and seven-figure premiums, cut-rate or not, are eagerly sought as investment fodder. By contrast, the relatively small premiums paid by individuals for property-and-liability insurance have remained immune to rate-cutting; indeed, they have been rising.

Competition for big policies while the small customer goes begging is a well-known phenomenon in workers' comp. John A. Schoneman, President, Wausau Insurance Companies, told a national symp on workers' comp last summer that as far as competition is concerned, the good and desirable large risks are very competetive price-wise, and will continue to be under any rate system. However, he continued, this cannot be said for the smaller risks which comprise by far the larger number of policies but account for only a small percentage of the total premium. Mr. Schoneman's definition of the "good and desirable large risks": over $100,000 annual premium.[1]

Albert J. Millus, former executive director of the State Insurance Fund of New York and now a consultant who heads a firm specializing in reduction of workers' comp costs, shares Mr. Schoneman's view. Millus:

> The experience of the author as Executive Director of the State Insurance Fund (New York) for over six years (1972-1978) convinces him that regardless of what form regulation of rates takes, as far as the large risks are concerned whether in manufacturing, retailing, construction or whatever, the competition to write these risks is always intense, innovative (e.g. paid loss retros) and often times self-destructive in its intensity. The State Fund over the years was involved in this competition and witnessed first hand the lengths to which one or more of the large carriers would go to cover some of these risks. Typical examples were the several water tunnel jobs . . . the Brooklyn-Battery tunnel, the World Trade Center buildings, the subway tunnel jobs to name but a few. . . .
>
> At the other end of the scale there are literally thousands of risks whose annual premium is less than $750. These risks designated as small risks are the type the large carriers do not want. The State Fund has over 70,000 such small risks and because it has such a volume of them it was able to computerize this segment of its business so as to minimize the expense factor in handling them and control the loss factor as far as that was possible. . . .the Fund wrote most of these risks at . . . the rates the private industry used, as their experience justified it they were extended the discount offered to larger risks.

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[1] Quoted in Albert J. Millus, "Open Competitive Rates for Workers' Compensation," undated manuscript (shorter version appears in Best's Review, November 1980).

III. Some Observations on Competition and Open Rating

A. National Association of Insurance Commissioners (NAIC)

Open rating is being considered by the NAIC. The Insurance Subcommittee of this Study Commission considered the NAIC's Advisory Committee draft on open rating at an earlier meeting. The premises of the NAIC Advisory Committee that recommended open rating are worth noting. The NAIC Advisory Committee states, "(t)he present system works well in terms of availability, affordability and the quality of services."[1] It is precisely the lack of availability and affordability of workers' comp in Alaska, if I read the reports correctly, that led the Insurance Subcommittee of this Study Commission to consider an open rating system modelled after the NAIC subcommittee's recommendations. If the Alaska Workers' Compensation Study Commission is not addressing the same problem the NAIC is addressing, is there any reason to assume the NAIC recommendations are appropriate to Alaska?

B. W.W. Fritz, Commissioner of Insurance, State of Oregon

Oregon Commissioner Fritz explained his enthusiasm for open rating at the October 16 Study Commission meeting in Achorage. The situation in Oregon differs from Alaska in several respects that may be relevant:

1. Oregon's total payroll is approximately four times that of Alaska, giving comp carriers a much larger volume of business ($126,618,000 additional premium dollars in 1979) to aim for.
2. Oregon has a number of large industries that might lure carriers;
3. Comp carriers are so eager to get into neighboring Washington State (where comp is provided by state fund) that some carriers have retained lobbyists in Olympia to seek a statute change permitting private carriers to write comp there. In sum, Oregon has an existing competition structure that may not exist for Alaska at this time -- and it is not clear that open rating will create that competition.

C. Michael Markman, Commissioner of Insurance, State of Minnesota

Generally regarded as consumer-oriented and progressive, Markman is a recent convert to open rating for Minnesota. In recent testimony before the Minnesota Workers' Compensation Study Commission, Markman described the merits of open rating. Among his major points :

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[1] See NAIC Advisory Committee report, p. 43. (NAIC Advisory Committee report presented to Insurance Subcommittee in October . The recommendations were quoted in the Subcommittee's Progress Report, Nov. 14, 1980.)

> (1) . . . companies are going to be forced to be making their own decisions naturally, and I think that's positive . . . . As a result you are going to have the insurance industry itself getting much more thorough in their understanding of workers' compensation. . . .
>
> (2) I think that if the average employer could go out and shop for a better price that it would be of significant benefit for everyone.[1]

The theory sounds good; does it apply to Alaska? With regard to Markman's first point, it takes a large volume of business to make it worth a carrier's time to do the complicated statistical work necessary to gauge comp risks independently from the NCCI. With this in mind, let's compare Minnesota's comp market to Alaska's:

1. Minnesota has five times Alaska's payroll and five times Alaska's comp premium.
2. In 1976 (the last year for which I have statistics at my desk) Alaska had eight comp carriers writing $1 million or more in premiums; if I'm not mistaken, in 1979 a second carrier broke the $10-million mark. By comparison, in 1979 Minnesota had nine carriers that wrote over $10 million in premiums, AND had over $200 million worth of comp business left over for the remaining carriers interested in competing.[2]

With regard to Markman's second point, note the following anecdote from Albert Millus, who found that employers lacked information for analysis of comp premiums at varying prices:[3]

> It is interesting to note that during the first few years of its existence the State Insurance Fund (New York) did establish its own rates which were different from those used by the private insurance companies. However, the Fund's representatives soon discovered that the employers were too confused by the different rates being quoted to be able to decide where their coverage could be had at the lowest cost. The Fund then joined the rating board and used the identical rates the private carriers were using but established a fixed advance discount from these rates which averaged 20%. . . .

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[1] Transcript of Markman testimony provided by Minnesota Workers' Compensation Study Commission (undated).

[2] It is not this writer's assertion that either $1 million or $10 million are the levels at which it would be worthwhile for a carrier to do its own figuring in Alaska.

[3] Millus, "Open Competitive Rates for Workers' Compensation" (manuscript version of article appearing in Best's Review, Nov. 1980), pp. 14-15.

D. James M. Stone, Former Commissioner of Insurance, Massachusetts[1]

1. Stone is in favor of competetive markets where the prerequisites for competition exist. He is not optimistic that they exist for workers' comp. Two of the things Stone feels are needed to make a competetive market work are:
   a. lots of competitors
   b. well-informed clientele
2. A move to open rating is "a major economic decision" that may change the economics of doing business. In Stone's view, open rating implies that each business carry its own weight -- and some businesses may not be able to do that for a socially-mandated insurance policy.
3. Stone feels that a move to open rating is risky at best -- even for a large state with many competing carriers.
4. Stone also notes that workers' comp has many subsidies built into the system and therefore may not be handled in all ways as a purely economic system.
5. Stone observed that if pricing is done properly, the residual market (e.g., an assigned risk pool) ought to have 40 to 50 per cent of the business because the carriers should be backing off from the risks they consider worse than average.

E. Dr. Harold Wilde, Former Commissioner of Insurance, Wisconsin[2]

1. With regard to the notion that deregulation guarantees competition, Dr. Wilde observed that Wisconsin had totally open markets in home-owners, auto and malpractice -- and even with effective deregulation for those lines carriers were reluctant to write.
2. Dr. Wilde said he would not favor deregulating workers' comp -- or any insurance line -- without two mechanisms in place:
   a. State fund to keep the market place honest (probably not feasible for political reasons, he noted, but essential to keep prices down by offering competition).
   b. Good pooling mechanism to insure that all risks can get coverage (could be the assigned risk pool if it is a true risk-sharing pool, rated and based on pool experience).

[1] Now Commissioner, Commodities Futures Trading Commission, Washington, D.C.; interviewed 11/21/80.

[2] Now Vice-President, University of Wisconsin; interviewed 11/14/80.

IV. Some Questions Concerning Open Rating

The open rating proposal the Study Commission is considering has two key elements: (1) rate filing on claim payment only, deleting expense allowance (profit, tax and expenses); and (2) automatic acceptance of all rates except those below the rating organization's minimal filing. (A third ingredient -- the Director of Insurance's involvement if the plan does not work -- does not appear in the draft legislation of Nov. 12, 1980.) Before recommending major revision of the complicated rate-making system, this Study Commission might wish to explore the following questions:[1]

1. Could the proposed changes pose a barrier to entry -- rather than the desired inducement -- by deteriorating trending data and information on operating expenses?

   Comment: If changes in the filing base would make the data carriers use for trending and other analyses more difficult to use, such a change might keep new carriers out of the Alaska comp market, rather than bringing them in. As Schoneman of Wausau points out, small carriers rely on the data generated by larger carriers (and the rating organization) to write workers' comp. Will we draw them in if we dilute the data base? There's a similar question on operating expenses, however suspect they may be to some. Most liable to suffer in this scenario are the small businesses. Millus points out that lack of reliable loss statistics "will have a tendency to push rates for the undesirable risk with less than average experience to a point that may well adversely affect such a risk's ability to stay in business."[2] Keeping in mind that the vast majority of Alaska comp purchasers are, in national terms, relatively small businesses, the Study Commission might wish to insure that the six lines of proposed legislation styled Sec. 21.39.045(a) will not create changes in the system that will make it more difficult, rather than easier, for a carrier to assess the risks in writing workers' comp in Alaska.

2. Is it possible that under the proposed system carriers might tend to structure their rates to attract only big policies, offering little or no improvement in the comp market for the vast majority of small businesses?

   Comment: See Wall Street Journal and Millus articles quoted on page three of this report.

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[1] If any or all of these matters have been considered in subcommittee or full Study Commission deliberations, I beg the Commission's indulgence: These comments are based on materials gathered during a month out of state, travelling on Study Commission assignment. In the course of my travels I may have missed discussion of these matters.

[2] Millus, op. cit., pp. 12-13, 18.

3. Might the chaos in the comp market resulting from variable rate filings operate to the detriment of the employer/purchaser, who already suffers from too little information about his/her options for workers' comp?

   Comment: See Millus, pp. 14-15, quoted above at p. 5.

4. In view of the Division of Insurance's acknowledged difficulties handling its statutory responsibilities for workers' comp,[1] has the Study Commission considered what legislative actions -- if any -- are necessary to assure that the Director would be able to protect the public interest by responding promptly to potential problems that might arise from the new system?

   Comment: Although it is not evident from the "Work Draft Paper" (Amendment #4 of Nov. 12, 1980) before the Study Commission, a key provision of the proposal is a trigger mechanism to bring the Insurance Division into action if rates are either (a) inadequate, excessive or discriminatory, or (b) non-competitive. Since filings would be approved automatically, it is highly unlikely that the small and ostensibly overworked Division of Insurance staff would have the staff capability and information to respond to potential problems in a timely manner.

5. How many policies over $100,000 are written each year in Alaska? How does this number compare to other states considering open rating?

   Comment: That's just a first-cut question to get a handle on distribution of Alaska comp policies by premium amount, which is necessary background to ask the question raised by Millus and the Wall Street Journal article: at what point will the premium be large enough to generate competition?

6. Has the Study Commission fully explored other ways to cut comp premium costs without taking risks inherent in radical revision of this complicated system?

   Comment: While open rating is a subject of much debate nationally, it is not known what the effects might be, or whether those effects would hold in the Alaska market, which may be unique by virtue of size and isolation. On the other hand, it is clear that attention to areas such as loss-prevention and litigation can reduce comp premiums -- and both these areas offer social benefits outside the comp premium structure, as well as premium savings. If new competition is desired, the Study Commission might consider other ways to reduce barriers, such as speeding Division of Insurance licensing, establishing a toll-free line for inquiries from prospective carriers in the Lower 48, etc.

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[1] See author's Jan. 21, 1980 report to the House Labor & Management Committee,