

# **Worker's Compensation Insurance in Wisconsin**

## **THE SYSTEM, THE BENEFITS, THE COSTS A REFERENCE GUIDE FOR EMPLOYERS**

This guide is intended to provide a general, non-technical explanation to help employers understand the basic principles of the worker's compensation system in Wisconsin. The sections that follow cover administration of the system, the benefits payable to injured employees and pricing that will help employers understand how their costs are determined.

### **WORKER'S COMPENSATION - WHAT IS IT?**

Wisconsin law provides that (most) employers have an obligation to pay certain specified benefits to any employee who is injured while working for the employer, regardless of fault. The most common method of satisfying this compulsory obligation is to purchase a Worker's Compensation and Employers Liability Insurance Policy from a licensed insurance company. Worker's compensation as a system, however, is much more than one employer buying an insurance policy from an insurer.

The Worker's Compensation system, when viewed in its entirety, is a mechanism under which virtually all Wisconsin employers contribute an equitable share of the estimated total dollars that will be needed to pay benefits to all injured Wisconsin employees in the coming year, plus the costs of administering this system. Each employer's contribution is determined and collected as a premium they pay for their insurance policy each year.

Obviously, all employers are not a part of this mechanism, as some are self-insured and others may not be subject to the law during a particular period of time. This guide will not address these exceptions, as it is designed for use only by those employers who are a part of the insurance system.

## ADMINISTRATION OF THE SYSTEM

### A. THE LAWS

The following two laws enacted by the Wisconsin Legislature control the entire worker's compensation system in our state.

- Chapter 102, Wis. Stats., which is commonly called the "Worker's Compensation Act of Wisconsin", establishes which employers and employees are subject to the law, provides enforcement procedures for non-compliance, and sets forth all benefits payable in Wisconsin.
- Chapter 626, Wis. Stats. is part of the Wisconsin Insurance Laws. It licenses the Wisconsin Compensation Rating Bureau (WCRB) and sets forth all of the rules, regulations and procedures relating to the classification of employers, worker's compensation rates, rating plans, appeal procedure, etc. In a very real sense, this law specifies how each employer's contribution (i.e., premium) is to be determined.

These two laws are obviously related, even though each law has a clearly defined responsibility and authority. Because of this relationship, there are provisions in each law that refer to the other law and the manner in which the laws complement each other.

### B. STATE OF WISCONSIN, DEPARTMENT OF WORKFORCE DEVELOPMENT - WORKER'S COMPENSATION DIVISION (DWD)

This State Agency is responsible for the administration of the Worker's Compensation Act of Wisconsin. It administers Chapter 102 with respect to enforcement, payment of claims, violations, and a host of other related duties under the system. Disputed worker's compensation

claims are adjudicated by this agency. It is also where claims involving loss of time from work must be reported by employers.

#### C. THE WISCONSIN COMPENSATION RATING BUREAU (WCRB)

The Wisconsin Compensation Rating Bureau (WCRB) is a licensed rate service organization for worker's compensation insurance in Wisconsin. It was created by Wisconsin law, and while it is regulated by OCI and works very closely with the Worker's Compensation Division, the WCRB is not a State agency. The WCRB is an unincorporated association of insurers who, by law, must be members of the WCRB.

The WCRB is responsible for the classification of employers, the rates and rating plans used, all policy forms and endorsements, and the collection and analysis of all statistical and other data needed to meet its responsibilities. All rates, rating plans, forms, etc. must be filed with and approved by OCI before insurers can use them. Deviations are not permitted.

The WCRB assists the Worker's Compensation Division in its enforcement activities. By law, the WCRB receives required information on every worker's compensation policy issued to every employer with operations in Wisconsin and every termination thereof, and transmits this information via computer to the Worker's Compensation Division. The WCRB also administers the Wisconsin Worker's Compensation Insurance Pool.

#### D. STATE OF WISCONSIN, OFFICE OF THE COMMISSIONER OF INSURANCE (OCI)

The Wisconsin Insurance Commissioner's Office licenses not only the WCRB, but also all insurance companies who transact worker's compensation business and all agents or intermediaries who sell worker's

compensation insurance in Wisconsin. It regularly examines the WCRB and insurers to make certain that all are meeting their obligations under the law. As previously noted, all worker's compensation rules, rates, and forms developed by the Bureau must be approved by OCI before insurers can use them.

## BENEFITS

Under the worker's compensation insurance system, insurers contractually agree to fulfill the legal obligation of employers to provide worker's compensation benefits to injured workers. A worker can be injured by an on-the-job accident or by disease or other impairment, which was contracted by on-the-job exposure. There are several kinds of benefits payable to injured employees or in some cases, their families, and the principal benefits in Wisconsin are:

- Medical Benefits - There is full, complete and unlimited coverage of all bills for medical treatment and for hospital services provided to injured workers.
- Indemnity Benefits - These are weekly cash payments to workers intended to partially replace lost income. In Wisconsin, there are several different kinds of payments that make up indemnity benefits. The principal kinds are:
  - ◇ Temporary Total - Currently, two-thirds of an employee's earnings, subject to a maximum, are paid to injured workers until they recover from work-related injuries and return to work.
  - ◇ Permanent Total - Injured workers who are 100% disabled due to a work-related injury are entitled to receive two-thirds of their earnings, subject to a maximum weekly amount for the remainder of their lives.

- ◇ Permanent Partial - Workers who sustain permanent partial disability receive supplementary compensation in addition to two-thirds of earnings, subject to a current maximum for a specified number of weeks related to the degree of disability. For example, a worker who suffers the loss of a leg at the hip joint receives 500 weeks of permanent partial payments. Correspondingly, if the worker loses a little toe at the second or distal joint, only 4 weeks of permanent partial payments are received.
- ◇ Death Benefit - there are several benefits payable when an employee is fatally injured dependent upon the worker's family status at the time of death. A maximum burial expense is also payable.
- Vocational Rehabilitation - The cost of rehabilitation is fully covered and the injured worker is also entitled to weekly indemnity payments during the rehabilitation period.

For a list of benefits, select the Maximum Wage and Rate Chart link located in the [Miscellaneous Values Table](#).

## COSTS

### A. FUNDING THE SYSTEM

The funding needed to pay both benefits to injured workers and the expenses of operating the system is primarily provided by the premiums employers pay for worker's compensation insurance. Because the system is prefunded and premiums are paid before benefits have to be paid, insurers are able to invest a portion of the premium. Therefore, investment income or loss on this premium could also add or subtract from the system's funding to some extent.

## B. PREMIUM DETERMINATION OR PRICING

1. Pricing Objectives - Worker's compensation pricing is designed to meet the following objectives:

- To generate funding needed to meet the cost of providing indemnity and medical benefits to injured workers and cost-effective services to insured employers.
- To equitably distribute the cost of the insurance system among employers, keeping in mind that the risk of injury to employees varies widely by industry.
- To provide incentives to insured employers to maintain safe working environments, thereby reducing the volume of worker's compensation injuries.
- To provide insurers an opportunity to earn a fair profit.
- To produce a stable insurance market and pricing structure that reflects changes in costs of the insurance system.

2. Unusual Characteristics of Worker's Compensation - The worker's compensation insurance system is quite unique when compared to other lines of insurance. When the actuaries review the statistical data to determine funding levels, some recognition must be given to the following:

- Unlike other lines of insurance, standard worker's compensation coverage and rates are non-negotiable.

- Worker's Compensation premiums are determined by multiplying a manual rate times the amount of payroll remuneration, measured in \$100 components, times any experience rating modification applicable. The premium collected from the employer when the policy is issued is only an estimated premium and the final premium is determined after the policy is expired and the actual remuneration is known.
  - Although employers pay the premiums, the injured workers and their families are the receiver of the benefits.
  - Even though the worker receives the benefits if injured, the named insured is the employer who is classified according to the business the employer is in and not necessarily according to the work being done by any employee. It should be noted that the risk of injury to employees doing similar work could still vary widely by business or industry.
  - Because worker's compensation insurance is mandatory for most employers, the magnitude of the system requires that pricing be as accurate as possible. Overpricing can impose a severe burden on employers, which is certainly not desirable. Underpricing could impact the solvency of insurers potentially affecting claim paying ability, which is also undesirable.
3. Wisconsin Expense Provisions - The accumulated premium dollars collected by all insurers from all employers in Wisconsin is intended to pay for:
- a. Loss Costs - All indemnity and medical expenses paid for or to injured employees or their dependents.

b. Operating Expenses of Insurers - including:

- Benefit & Loss Adjustment Expenses - which are the insurer's costs of administering and settling worker's compensation claims,
- Production Expenses - which include agents' commissions, advertising costs, etc.
- General Expenses - which include general administrative expenses, loss control services, and similar costs.
- Taxes - including federal, state, and any payroll or premium taxes.
- Profit and Contingency.

### C. WISCONSIN PRICING PROCESS

The amount of premium an employer pays for worker's compensation insurance in Wisconsin may be subject to several components defined as follows:

- Statewide Benefit Rate Changes - Whenever the Wisconsin Legislature enacts a change in benefits payable to injured workers, all rates are adjusted a specific percentage amount to reflect this change. This percentage applies uniformly to all employers regardless of the business or industry in which they operate.
- Statewide Average Rate Change - Since the worker's compensation insurance system is a prefunded system, historical loss information is used to project the costs anticipated during the future policy year. These anticipated or expected costs are compared with anticipated or expected income at current levels, and the rates will then be adjusted to reflect the result. Whenever expected costs for the upcoming policy year are higher than expected income, then rates, on average, will increase. If, however, expected costs are lower than expected income, then rates, on average, will decrease.



- **Manual Rates** - Since losses vary widely by business or industry of employers, charging the statewide average rates would result in some employers paying too high a premium, while employers in other businesses or industries would pay less than their fair share. Accordingly, employers are classified by the business or industry in which they operate to reflect this variation in loss costs. There are more than 600 classifications of employers in Wisconsin, each of which contains groups of employers engaged in the same business or industry, and each of which is large enough to develop sufficient loss data to produce an accurate projection for future losses.
- **Experience Rating** - If all employers in the same business or industry had identical operations, the same experience and skill level of employees, and the same safety commitment, the manual rate would be appropriate for every employer in determining price. However, we know that employers often differ significantly in these areas, and to take these differences into account, a method of adjusting the price paid by many employers called experience rating is used.

Experience rating uses the historical loss experience of the individual employer as a predictor of future losses to adjust the premium the employer pays. Employers whose business is too small to rely on past losses as statistically reliable predictors of future losses are not subject to experience rating. For current eligibility, view the [Miscellaneous Values Table](#).

Under experience rating, the premium of individual employers will be adjusted upward or downward by an experience modification factor. If an employer's actual past losses are greater than the expected average losses for all employers in the same business or industry, then an experience rating surcharge (or debit) will be applied to the policy and the employer's overall premium will be increased. If the converse is true and the employer's actual losses are lower than the expected average employer's losses, a rating credit is assigned and the employer will pay a lower overall cost.

In addition to making the pricing process more equitable by reflecting differences in an employer's loss experience from the average for the classification, experience rating provides a strong financial incentive for employers to reduce injuries.

- Expense Constant - This flat charge is added to every policy to reflect the overall expense of issuing a policy, billing, setting up an internal file for the policyholder, and other initial start-up expenses. For current expense constant charges, see the [Miscellaneous Values Table](#).
- Premium Discount - A portion of every dollar in premium paid by an employer is intended to cover general expenses of the insurer in servicing the policyholder. These expenses are not incurred in direct proportion to a premium regardless of premium size. Accordingly, a discount is given to employers having annual premiums over \$10,000 to reflect expense reduction. The larger the premium, the greater the discount. (NOTE: This discount does not apply to risks insured through the Wisconsin Worker's Compensation Insurance Pool.)

- Standard Premium - The initial premium utilizing estimated payrolls or remuneration, the manual rate, and the experience rating modification, if applicable, is called the estimated Standard Premium. Premium Discount has never been included in the determination of standard premium.

#### D. POSSIBLE RETROSPECTIVE ADJUSTMENTS TO PRICE

Retrospective Rating Plan - This plan is available only to employers generating \$25,000 or more of standard premium. The plan permits an employer and an insurer, by advance mutual agreement, to adjust the standard premium upward or downward based on the actual losses which arise during the policy period.

For those employers who elect this plan, each dollar of savings in reduced claim costs will reduce the price the employer pays, subject to a minimum premium. However, unlike policyholder dividends, which can only reduce the price, under this plan each dollar of cost which exceeds the expected claim costs will increase the price above the standard premium, subject to a maximum premium.

Policyholder Dividends - The payment of policyholder dividends to insured employers is the method most frequently used in Wisconsin to adjust the price of insurance after the policy expires. The amount of the dividend is typically based on the losses that arise during the policy period, the size of the premium, or both.

In addition to making the pricing process more equitable by reflecting the actual cost of benefits and creating a financial incentive to promote safety, policyholder dividends are one of the major means by which insurers compete in the Wisconsin marketplace. For most employers it is the final step in the pricing process.

Dividend calculation methods vary considerably among insurers. For example, one insurer's type of business and its policyholders may be served best by a relatively level or flat dividend rate. Others are better suited to dividend variations according to the level of losses, the type of business in which the policyholder is engaged, or the amount of premium involved.

Sometimes small employers engaged in the same business will join a so-called "safety group" program through membership in a business association. These employers all purchase individual worker's compensation insurance policies from the same insurer, but the loss experience of the entire "safety group" is used to determine the dividend amounts for all member employers. Often, these dividends are larger than what an employer might earn individually because:

- They participate in an association safety program which can reduce claim costs overall;
- The insurer often saves expense dollars as safety engineering and
- The greater volume of business represented by the group provides for greater predictability of losses.

The payment of policyholder dividends is contingent upon a declaration by the board of directors of the insuring company. By law, a dividend can be declared only if the insuring company has retained profits generated by its Wisconsin worker's compensation insurance operations; therefore, dividends cannot be guaranteed. To ensure fairness and equity in the payment of dividends, dividend disclosure statements must be presented to policyholders in accordance with regulations promulgated by the OCI.

## CONCLUSION

The WCRB recognizes the growing awareness and heightened interest in the determination of the price of worker's compensation insurance. This guide is intended to provide a better understanding of how the cost of the worker's compensation insurance system is translated into the price paid by employers for insurance coverage.

The Wisconsin pricing process, which establishes rates at a level adequate to fund the cost of the insurance system and thereby safeguard the payment of benefits, equitably allocates the price of insurance and provides strong incentives for safety.

Manual rates and experience rating produce an equitable price at the time the insurance is purchased, while the payment of policyholder dividends after the policy expires and the losses are known, produces the "right" final price to the employer. In addition, since insurers compete for business based in part on their record of paying policyholder dividends, they are compelled to minimize losses and expenses to help ensure the payment of future dividends. This competitive pressure promotes efficiency and the lowest net price for insurance, consistent with the overall objectives of the worker's compensation pricing process.