



*A Partnership of the Association
of Bay Area Governments
and the Bay Area Council*

Bay Area Economic Forum Core Recommendations for Workers' Compensation Reform

A Dysfunctional System

California's Workers' Compensation system is broken, and is threatening California's economy and the ability of businesses to generate the jobs needed for full economic recovery. The dysfunctionality of California's system is evident in the disparity between its high employer costs - California employers pay the highest Workers Compensation premiums in the nation - and its relatively low level of worker satisfaction and benefits.

Today large and small businesses alike are unable to predict their insurance costs, adding instability and uncertainty to an already weak business climate. Onerous rates effectively operate as a tax on employment. As a result, Bay Area and California companies are deferring new hiring, cutting payrolls, and limiting or reducing benefits and salary increases. Higher rates that cannot be absorbed are being passed on to consumers, raising the cost of a wide range of goods and services.

The State Compensation Insurance Fund

Due to the closing or withdrawal from the market of many insurance carriers and the insolvency of others (27 Workers' Compensation insurance companies have either gone bankrupt or have been placed in receivership by the Department of Insurance) the State Compensation Insurance Fund, as the insurer of last resort, has seen its market share increase from 18% to more than 50% in only a few years. This deprives employers of competitive options and threatens the viability of the Fund itself.

Two Core Problems: Utilization and Medical Costs

Since 1995, annual Workers Compensation costs have increased from \$10 billion to \$25 billion (2002). Medical costs have risen at a rate of 17.5% per year. In the last two years alone, premiums have increased by more than \$6 billion, an amount paid for by all employers including large companies, small business, non-profits and local government. In many cases costs in California are 4 to 5 times higher than in surrounding states.

Two of the primary causes of this rapid escalation are 1) the over-utilization of medical services, and 2) surging medical costs.

The Bay Area Economic Forum was founded in 1988 to promote the economic vitality of the Bay Area. It is governed by the leaders in business, government, labor, higher education and the community

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UTILIZATION: The volume of services supplied to claimants has escalated rapidly, with the average number of visits per claim growing by 90% in the last five years. The current level of visits per claim is more than 70% higher than the average for other major states (30 vs. 17). Nationwide the average number of visits an injured worker makes to a chiropractor, for example, is 15; in California it's 34.

Workers Compensation lacks controls against the over-utilization of medical services that are common to other third-party payer systems, such as co-payments and deductibles. It is even more important, therefore, that the system provide necessary checks and balances to avoid unnecessary and ineffective medical treatments.

MEDICAL COSTS: Workers compensation costs fall principally into the categories of 1) indemnity payments, which are paid to injured workers for their time lost from work and for permanent disability, and 2) payments for medical services provided to injured workers. While indemnity payments to injured workers for lost work time have seen relatively modest growth, the average cost of medical services has more than tripled in the last ten years, from approximately \$9000 per worker to over \$31,000 (2002), with most of that growth occurring in the last five years. Increases in the cost of medical services in California have far outpaced the rate of increase in the medical benefits arena nationally.

The absence of comprehensive, up-to-date fee schedules has enabled this escalation. Notably, the average reimbursement level for one unit of outpatient facility use is substantially higher than for the comparable reimbursement under Medicare. Costs are between 50% and 100% higher for patients' treatment under workers compensation than for the treatment of comparable conditions under non-occupational health insurance programs.

Core Solutions

There are many elements of Workers' Compensation system that need reform. However, given the urgency of the situation, State leaders must immediately address its two most serious causes: utilization rates and medical costs.

REINING IN UTILIZATION: To determine what is a reasonable volume of services, an accepted standard-of-care based on clinical evidence or evidence-based medical protocols should be adopted. This should be coupled with an Independent Medical Review process to determine the appropriateness of proposed procedures and to approve services exceeding the standard-of-care where medically justified. The Independent Medical Review process should be conducted by qualified medical practitioners independent of insurance companies or other parties of interest. Adoption of an agreed standard-of-care and Independent Medical Review will help to ensure expedited, clinically-based consideration of claims for service, and to reduce administrative, legal and medical costs.

CONTROLLING MEDICAL COSTS: To establish a fair market price for services, comprehensive medical fee schedules for all providers, including outpatient surgery centers, should be adopted, linked and indexed to the fee schedule used by Medicare, and at a level that is effective in achieving meaningful cost control.

Consideration should also be given to the establishment of a pilot program that would allow employers to provide Workers Compensation insurance through HMOs already providing non-occupational health insurance, to test whether this framework can be effective in reducing administrative, medical and legal costs.

RECOMMENDATIONS:

As a matter of priority, the Bay Area Economic Forum recommends the inclusion of Medicare-indexed medical fee schedules, standardized protocols for medical treatment and Independent Medical Review in omnibus legislation to reform the state's Workers Compensation system. Immediate implementation of these measures is required to stabilize the Workers Compensation system and to stop the further erosion of jobs and business confidence in the state. This must happen now, without linkage to other issues not directly related to Workers Compensation.

The Bay Area Economic Forum also recommends:

Adoption of a requirement to use generic drugs in hospitals for workers compensation treatments, as a further means to reduce medical costs,

A stricter requirement that to be eligible for benefits workers compensation injuries must be predominantly caused by employment-related activity;

Adoption of independent dispute resolution mechanisms and other measures to restrain excessive litigation;

More aggressive treatment of fraud; and

Reforms to assure greater fairness in assessing employer penalties for benefit delays.

The Bay Area Economic Forum is an organization of civic leaders representing business, government, higher education, labor and the community. Sponsored by the Bay Area Council and the Association of Bay Area Governments, its activities address the vitality and competitiveness of the Bay Area's economy and the quality of life of its residents.