

***New York Compensation Insurance Rating Board
Response to Report of Fiscal Policy Institute***

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The Fiscal Policy Institute recently issued a report entitled *New York State Workers' Compensation: How Big is The Coverage Shortfall?*, which purportedly identifies a \$25 - \$50 B payroll shortfall within the workers compensation system. A review of that document reveals a number of false, inaccurate, unsubstantiated or misleading statements, which, if not addressed, might result in a very distorted view of both the workers compensation system, and the insurance industry that provides this critical insurance protection.

To begin with, the report's Executive Summary states that "many employers do not provide this coverage for their workers". In one way or another, every eligible worker receives coverage for workers compensation. First, a workers' compensation policy, once in effect, covers all of the employer's employees at the covered employment regardless of whether they were reported to the carrier when the policy was issued. Second, it is believed that, throughout history, only a small percentage of employers have failed to provide coverage to their workers. Finally, if coverage is lacking for an insured who files a claim, the Uninsured Employers' Fund, (Section 26-a WCL), which the article's author obviously has no familiarity with, takes over and is specifically designed to provide benefits to injured employees, while penalizing the employer who must then pay the benefits into the system and face fines and other legal actions.

More importantly, the report emphatically states, with no stated basis in fact or knowledge, that "the quality of workers' compensation payroll data is not what it should be". The author and others who make similar unsubstantiated statements clearly are not aware of, or recognize, the detailed editing and review of all workers compensation data that is reported to the Rating Board. Furthermore, this data is also reviewed annually by the New York State Insurance Department in conjunction with the Board's annual rate filing. In addition, every three years, the Department conducts an examination of the Board's operations and procedures, which includes a review of the data handling processes that are being used. At no time, during either an annual review or a detailed examination, has the integrity of the payroll data ever been questioned or criticized.

A substantial portion of the Institute’s argument regarding missing payroll is based on what is purported to be total 2003 payroll figures for workers compensation vs. the payroll amounts for unemployment insurance. We do not understand the basis for this comparison. First, it must be understood that different time periods are being used. The 2003 payroll information relates to policies first written in 2003, whereas the unemployment figures are those reported to the state in a particular calendar year. The 2003 New York payroll figures used in the comparison are on a first report basis which means that these figures are generally lower than the final payroll figures which have been audited and verified by the carriers as the final payrolls and premiums. Incidentally, in response to the Report’s questioning as to why the Rating Board’s latest numbers are from 2003, it is necessary to state that the Rating Board collects data, not as a means for determining coverage (responsibility of the Workers’ Compensation Board), but rather as a tool to develop individual insured’s experience rating factors and classification rate relativities. In order to properly do this, it is necessary to develop matching claim experience for each of these policy periods which necessarily and essentially results in the lag time between experience period and the latest calendar year period.

The report notes that “there are several categories of workers excluded from coverage under the NYS worker’s compensation law.” One item, however, not included in the WC payroll base, but which is in the UI base, and not mentioned in the Report, is the payroll of part-time domestic workers (under forty hours per week) which can be quite substantial and, by law, is excluded from the workers compensation system. There are many other such categories not considered in the report. In addition, although payroll limitation was mentioned as a consideration, we are unsure how much credit was given to this amount or where the numbers are extrapolated from. Furthermore, the paper fails to take into consideration that the payroll for employment classifications such as athletic teams, radio and television broadcasting, racing stables, theatrical productions, executive officers, sole proprietors and partners are also substantially reduced prior to their inclusion for reporting to the Rating Board. For example, consider the fact that Executive Officers payroll is limited to just four times the average weekly wage for workers compensation reporting. Considering the number of highly paid executives, this limitation can have a severe impact on the total payroll dollars reported to UI versus that reported for workers compensation. Finally, consider as well, items such as overtime and severance

pay that are excluded items from workers compensation payroll reporting which further erodes any perceived differences between the workers compensation and UI payroll base.

A good portion of the report is devoted to the premise that employers intentionally report their workers as independent contractors to avoid paying premiums. Outside of one example which indicates that this situation can occur, most of the report's conclusions are based on "anecdotal" experience which are not supported. The Rating Board has found that, in many instances, given the lack of a clear and uniform definition of Independent Contractor in the state, determination of status at policy writing may be difficult and hence the reason why that determination in some cases may occur only by the WCB following claim occurrence. When a policy is first issued, it is written on an estimated basis. If an employer does not claim all of its employees, the carrier auditor will make the adjustment at the time of audit. While an employer may want to exclude those he considers "independent contractors" from coverage, a carrier will not exclude these individuals if there is evidence that an employer/employee relationship exists with the "alleged independent contractor". Please also note, as an additional safeguard, that the New York Workers Compensation Manual has a rule that so-called independent contractors and their employees must carry their own coverage and produce a certification of insurance to the compensation carrier to avoid being classified as an employee.

The report also states that the problem of Independent Contractor status is not a statewide problem but rather a countrywide problem as other states have grappled with a similar problem. To single out New York is, therefore, irresponsible as it appears that it is not a fault of the carriers' procedures used to determine premium applicability, but rather a universal problem with the proper definition of an independent contractor which, by the way, has been a problem for workers compensation insurance determination for nearly as long as the system has been in existence.

Other inaccuracies, specifically with regard to the Rating Board, are also contained in the Report. The Report states that the Board mainly uses telephone audits to check insurance carrier audits of employers. This statement cannot be farther from the truth. All audits conducted are done via actual visits by Board auditors to the employer's site and physical examination of employer's payroll, journal and ledger records. It is very rare, as well, when the Board selects an insured for an audit review, that the insurance carrier has

not yet performed an audit for that employer. This is necessary information for the Board auditor since he/she is comparing the Rating Board audit results to the carrier audit results.

The Report also inaccurately defines the term “misclassification” for WC premium purposes. A misclassification is defined by the Institute as when an insured is classified in a lower rated classification. However, it fails to recognize that a “misclassification” can also occur when an insured is placed in a higher rated classification. In 2006, the Rating Board performed over 10,000 inspections and made over 1,500 classification changes which reported misclassifications of businesses where risks were incorrectly placed in both higher and lower rated classifications. It is also important to note here that the New York State Insurance Department, in their examination of the Rating Board’s auditing and inspection procedures required legislatively to be completed by the Department every three years, has found these procedures to be acceptable for the establishment of proper premiums. The Department also conducts examinations of carriers which would also reveal whether or not a carrier is meeting its obligation to conduct audits.

Finally, the Rating Board needs to once again address, as referenced in the Report, the denial by the State Insurance Department of the rate filing submission based upon the fact that carriers have not done an adequate job in policing fraud which is, according to the Report, rampant within the system. A Board subcommittee completed a report in 2006, and submitted it to the Department, which shows that the insurance industry has made significant dollar and resource commitments to fight fraud in New York. While it is possible that complete payroll data is not being reported in some cases, the extent of that exclusion has not been clearly established in this Report, or for that matter, any other report and should not have been used as the primary reason for disapproving the rate filing.

Therefore, in light of the numerous misstatements and inaccuracies, we believe that the Report’s findings have no validity especially as an indicator of employer payroll fraud within the workers compensation industry. What is clear is that significant further review and substantiation would be needed before arriving at any such conclusions.