INNOVATION

vs.

INERTIA AND REGULATION

Gaining a Competitive Advantage in Workers’ Compensation

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InsurCard®
Workers’ compensation inherently is a conservative line of insurance. Because the system has worked reasonably well for injured workers for 100 years, regulators are understandably cautious about “fixing what isn’t broken.” Additionally, though insurance companies desire greater efficiencies and lower costs, entrenched processes and legacy information systems can stand in the way of change.

Despite resistance and inertia, the workers’ compensation market has been a hotbed of innovation in recent years. Driven substantially by runaway claims costs, sweeping changes in the ways submissions are underwritten and claims are managed have been implemented by many insurers to rein in both medical and indemnity costs. Workers’ compensation insurers also have taken aim at underwriting and claims administrative processes to lower expenses, increase productivity, and improve broker, insured and claimant satisfaction.

Insurance companies that are most successful at controlling costs while improving customer satisfaction enjoy strong competitive advantages. This is especially true today since the workers’ compensation systems in many states are under increased stress as medical and indemnity costs continue to soar while premiums have fallen.

The Drivers of Change

Worker’s compensation insurers are locked in a perpetual battle against rising claims costs. Indemnity severity has consistently outpaced wage inflation, and medical severity is growing much faster than the medical care component of the Consumer Price Index. According to National Council on Compensation Insurance (NCCI) statistics, medical severity increased about 47 percent between 2002 and 2009.¹
Reforms to workers’ compensation laws in many states in the 1990s and the 2000s helped stem rising claims costs, but many benefits of the reform measures have since been overwhelmed by other forces driving up medical and indemnity severity and driving down premiums. The workers’ compensation combined ratio was 115 in 2010, up 5 points from 2009 and well above the level for commercial insurance lines overall, according to the NCCI. Initiatives to bring combined ratios in line focus on both the loss ratio – using innovative technologies and strategies to sharpen underwriting accuracy and to improve claim outcomes – and the expense ratio – through a variety of tools to improve efficiency and drive down costs.

Skyrocketing costs has been a persistent driver of innovation in workers’ compensation, but it is not the only one. Workers’ compensation is largely a commoditized insurance product, with service being an important differentiating factor among insurers. Service-related innovations of the past decade include simplifying and accelerating the new and renewal transaction process, streamlining premium payments, and making indemnity payments easier to manage for disabled employees.

Managing Workers Compensation Costs

**Underwriting and claims expenses**

The underwriting and claims administrative costs are the costs most directly under the insurer’s control. Containing these costs can shave critical points from the combined ratio.

**Reducing payment costs**

Debit cards are now widely used in both the public and private sectors for making payments to individuals, such as public assistance payments to welfare recipients. Especially for lower income individuals without bank accounts, a group which includes many workers’ compensation claimants, debit cards can be safer, cheaper and more convenient than cashing checks at check-cashing facilities. Checks also can be lost or delayed in the mail, whereas payments through reloadable debit cards almost always are timely and secure. Compared with checks, debit cards offer better protection and faster solutions if lost or stolen.

From the standpoint of insurers, a large carrier can save millions of dollars each year in processing expenses. InsurCard, the sponsor of this report, estimates savings of up to 85 percent. Having banks directly handle “lost-stolen” issues also saves resources and money for claims operations.
While seemingly a commonsense approach to handling indemnity payments using well-tested technologies, regulators in many states initially were reluctant to allow debit cards, and some continue to oppose it. Some of the issues raised as InsurCard sought approval included costs to recipients; the security of the funds and the accessibility of the funds. Since InsurCard has partnered with Visa, the security and accessibility issues were quickly addressed, and the expense concern was answered by arranging for the first ATM withdrawal to be free with fees for subsequent withdrawals capped at $1.50. InsurCard now is approved in 40 states, including California, New York, Florida and Texas.

**Claims automation**

Innovative tools that help injured workers quickly receive appropriate care, and which help manage each case to optimize outcomes, are discussed in a later section. These same tools also help improve the efficiency of the claims management process and hold costs in check. Other innovative uses of technology in the claim management process include automated medical utilization review and automated bill review and repricing.

Presently, less than 20 percent of workers’ compensation-related medical bills are submitted and processed electronically, due largely to myriad state reporting guidelines, regulations and fee schedules, but experience with group benefits has shown that significant savings can be achieved through electronic transactions. Automated processing is expected to significantly increase in workers’ compensation in the coming years.

**Underwriting automation**

Automating the underwriting process can improve results by assuring that underwriting rules are applied consistently. But the most significant benefit of automated underwriting is a reduction in underwriting expenses. Applications are instantaneously screened for underwriting red flags and scored. Based on the output, the application is rejected, referred to an underwriter or, if it has a passing score, submitted for rating and further processing.

Underwriting and rating-rules engines can be embedded in automated underwriting workflow and document management systems. These systems can provide seamless end to end processing of submissions and renewals, as well as automation of other policy management functions throughout the policy lifecycle.

**Medical and indemnity costs**

Medical and indemnity costs comprise about 60 percent of the workers’ compensation combined ratio, and are growing again after being temporarily put into check by reform measures in a number of states.
Recent initiatives to control claims costs fall principally into three areas: predictive analytics to improve risk selection, data mining and artificial intelligence to combat fraud, and automating decision making and information sharing to improve claims outcomes.

**Predictive analytics for underwriting**

Predictive analytics for underwriting purposes is a system of scoring submissions based on characteristics that reflect expected loss costs. For workers’ compensation, a predictive model might be based on historical claims experienced related to various employer attributes.

There is nothing new about the concept of predictive analytics in insurance: standard actuarial pricing techniques are closely related to predictive analytics. In recent years, however, the process of generating scores has become more sophisticated, using advanced analytical tools and expanded data sources. The most accomplished companies in using predictive analytics have a strong competitive advantage since they can more precisely price their products and can better identify profitable market segments and dedicate resources to growing those segments.

**Fraud detection**

In 2000, the National Insurance Crime Bureau (NICB) estimated that workers’ compensation insurance fraud cost the insurance industry $5 billion per year, and was the fastest-growing insurance scam in the nation. More recently, the NICB reported that the number of suspicious or questionable claims increased sharply as the recession threatened workers with layoffs.

Insurers that are adept at combatting fraud can achieve material savings. The New York State Insurance Fund, for example, announced 154 arrests in 2009 resulting in $16.6 million in recoveries and estimated savings. Some fraud detection processes use cutting edge tools, and represent some of the most sophisticated applications of technology in the insurance industry.

Computerized fraud detection programs compare workers’ compensation claims against patterns derived from known fraudulent claims. Computer programs not only are faster and more consistent than human analysts, they also can take into account more variables than is practical for humans. Anti-fraud software used by Washington’s Department of Labor & Industries, for example, screens claims based on about 100 criteria, scanning for red flags such as delays between doctor’s appointments and care that is inconsistent with an injury.

**Claims management**

A coordinated response at the earliest, most critical point following an injury can favorably impact outcomes. Computerized tools improve decision making and enhance communication...
among the various people involved in managing a claim, assuring that an injured worker gets the most appropriate level of care as soon as possible, and that each step of the subsequent process is effectively managed to maximize outcomes.

The first point of contact following an accident often is a triage nurse in a nurse call center. Using treatment protocols and computerized tools to identify the level of expertise required for a particular case, a nurse can quickly determine the appropriate level of care and direct the injured worker to the best source of treatment. Artificial intelligence technologies drive many of these advanced decision support systems that enable a quick determination of the optimal course of action.

Critical information about the employee and his or her injury can be immediately entered into an online system, enabling adjusters, nurses, case managers, employers, insurers, medical directors and field review to quickly act on a claim. As the case progresses, updates are shared with other team members, assuring that everyone is responding with appropriate and effective actions to improve outcomes.

**Service improvements**

Some of the activities that lead to lower claims and administrative costs also result in improvements in service that are appreciated by brokers, employers and injured workers. More efficient claims management not only results in lower costs to insurers and employers, it also can lead to much greater satisfaction by injured workers, who appreciate immediate professional attention to their cases. Automated underwriting tools not only reduce costs, they result in faster transactions, increasing the satisfaction of both agents and policyholders. Reloadable debit cards, can overcome many of the frustrations encountered by injured workers in dealing with checks, especially those without bank accounts and who would otherwise pay check-cashing fees.

Other initiatives are focused principally on enhancing service, though reducing costs is a corollary benefit in some cases. Innovative service enhancements can provide important points of differentiation among insurers that otherwise are selling a substantially undifferentiated product.

**Automated quotes and submission**

Because underwriting and pricing for smaller policies is highly suitable for automation, workers’ compensation underwriters were pioneers within the commercial lines sector in developing automated quotation systems. Insurers that provide agents with automated quotes, combined with easy online processes for submitting submissions and rapid turnaround on binding and policy issuance, not only will keep agents happy, but will impress policyholders.
A few insurers provide agents with systems that not only automatically quote premiums, but also bind and issue policies at the point of sale. One of the first fully automated systems, CyberComp, which now is owned by AmTrust North America, was launched in 1997. CyberComp also gives agents real-time access to billing and claims status. In 2009, when owned by Swiss Re, CyberComp had a distribution network of 13 regional wholesale agencies and more than 600 retail agents, and processed about $100 million in premium.

**Pay as You Go Workers Compensation**

Pay as You Go Workers Compensation premium billing and payment removes the need for employers to estimate annual payroll premiums and eliminates down payments and large year-end adjustments. This service, which is offered by third party providers, integrates with payroll software or third-party payroll services. Employers pay workers compensation based on actual payroll, not on estimates and adjustments. This simplifies the premium payment process and can improve employers’ cash management.

**A Look Ahead**

Workers’ compensation insurers ceaselessly struggle to remain profitable, but it is nonetheless a highly competitive line of business in those states where competition is permitted. The winners of the future are those companies that are best able to control claims frequency and severity, reduce administrative costs and provide superior service to agents, employers and injured workers.

The first step towards success always is paying attention to the fundamentals. Companies need to be outstanding at basic claims and underwriting blocking and tackling. Furthermore, many insurers still lag in basic information technology, and could see significant gains through the use of well-established technologies. Once the fundamentals are in place, however, the top performing companies will seek out innovative new ways to achieve competitive advantages. The goal remains the same – keep costs low and service levels high – though the means of achieving that goal will continue to evolve.

Claims and underwriting technologies to control claims costs continue to progress. More powerful predictive models are emerging as advanced data mining and artificial intelligence technologies enable insurers to identify and quantify previously unidentified features and relationships that impact outcomes.

More sophisticated models also will help to manage complex tasks such as medical utilization reviews. Bill adjustment also will benefit from technology, though electronic pre-payment may one day support provider-group fee schedules in real time, avoiding the after-
the-fact adjustment process. Additionally, already effective pharmacy benefit management (PBM) programs may include pre-paid debit cards that pay a pre-agreed amount at point of purchase, avoiding costly reviews and adjustments.

Agents and brokers naturally gravitate towards those insurers that are easiest to work with. Providing producers with tools to simplify new and renewal business transactions increasingly is a necessary cost of business, and will be a competitive arena going forward. In addition to conducting business through proprietary portals, insurers will need to adapt to online exchanges. After many false starts and failures, what may prove to be the first viable insurance exchange was launched in 2010. The Lexis/Nexis Insurance Exchange is described as a “single entry collaborative insurance placement platform.” If it gains traction, performing in a rapid-paced online environment will change the rules of competition for insurers.

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NOTES
1: “Calendar-Accident Year Underwriting Results Using Data Valued at December 31, 2009,” NCCI