

The Liversidge e-Letter

An Executive Briefing on Emerging Workplace Safety and Insurance Issues

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An Electronic Letter for the Clients of L.A. Liversidge, LL.B.

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NDP tables motion to kill ER Says creates “degrading meaningless jobs” *To be debated Wednesday at Queen’s Park*

NDP leader Howard Hampton’s motion to be debated Wednesday; Labels experience rating “flawed”

While this issue has been politicized, all political partners do share one connection – all want safe workplaces

No question about it – the experience rating [“ER”] debate is highly charged at the moment and is as political as any issue can get. As I have always said, workplace safety and insurance [“WSI”] is “*more social contract than insurance contract and at its core it is political*”.

Workplace safety and insurance is political

I have always meant “political” in a broad context. The management/labour interests managed by WSI are unquestionably diverse. But they intersect at core junctions.

Worker and employer interests intersect on many levels

First and foremost, workers and employers want fewer on-the-job injuries. In fact, workers and employers share an objective to eliminate *all* workplace injuries. Workers and employers want effective return to work. Workers and employers want a sustainable system (whether labour publicly heralds the financial integrity of the system or not, if it goes belly-up, well, it will be workers that suffer, just as if premiums get so high as to start killing jobs, workers again pay the price). Workers and employers want a system that provides compensation as a matter of right and does not lay blame at anyone’s feet. Workers and employers want fairness and justice. Workers and employers want an administratively efficient system that does not bog either party down in red-tape. *So, what’s the problem?*

But, worker and employer interests do diverge

Notwithstanding this common ground, there is one understandable but powerful divergence between labour and management interests – *workers want benefits to be as generous and as high as possible and employers want WSI premiums to be as low as possible. And, it is within this classic contest that the current ER debate rages.*

It is also in this environment that very *positive* employer actions are kindled. Critics argue that these same motivations trigger *negative* spin off employer behaviours.

I will prove that ER does not engender negative corporate behaviour

While I will not deny that there are some outlier employer behaviours out there, and while I would be the first to stand in line and condemn those actions, *I adamantly assert that they do not flow from ER*. Just as cases where a few workers may fraudulently plot to submit phoney WSI claims do not at all speak ill of all workers generally, a few ill-informed and obtuse employers cannot be said to represent the legitimate behaviours of employers generally.

I however will go further. It is being alleged that the self-interested employer will engage in devious and improper actions to “close down” claims by either not reporting the injury in the first place or by forcing injured workers back to work too early in phoney “*make work*” jobs.

I will categorically prove that this thesis is itself flawed. But first, let us examine the NDP motion.

The NDP Motion – Immediately eliminate ER

Here is the NDP Motion:

Mr. Hampton – That, in the opinion of this House, the McGuinty government must:

Immediately direct the Workplace Safety & Insurance Board (WSIB) to eliminate the flawed “Experience Rating” program;

Immediately direct the Provincial Auditor to conduct an audit of the flawed “Experience Rating” program;

Recognize the fact that tens of millions of dollars have been drained out of the WSIB’s accident fund each year by employers who have learned how to play the game of “Experience Rating”;

Recognize the fact that Experience Rating reduces employer claims – not worker injuries;

Recognize the fact that the practice of experience rating actually encourages employers to mis-report or under-report injuries and occupational diseases, force injured workers back to work before they are medically ready, and pay workers sick pay rather than have them receive compensation benefits;

Recognize that this hides the true extent of workplace injuries and illnesses in Ontario;

Recognize that employers actually receive rebates after they have been penalized for workplace injuries and occupational diseases and deaths; and

Recognize that the rebates flowing to employers under the program often exceed the cost of the original fine. Addressed to the Premier of Ontario. **To be debated May 14, 2008.**

There is nothing new about these allegations

ER has long been controversial. Four years ago, in the March 26, 2004 issue of **The Liversidge e-Letter**, "**Experience Rating: The Concepts**", I said this:

Yet, this question still fuels the same controversy and conflict it did when these programs were introduced. Proponents remain of the general view that experience rating imports much needed equity to workers' compensation and point to declining accident rates as evidence of its effectiveness. **Opponents argue that experience rating simply affects employer claims management and reporting behaviour and it does not inspire accident prevention efforts. Experience rating becomes a flashpoint of discord perhaps reflective of other frictions, or, may simply mirror common insurance tensions.** Yet, it quickly becomes clear that both points of view have merit, and while labour and management sincerely wish to reduce occupational injury, experience rating, rather than acting as the locus of quality intervention, becomes instead the focal point of a different struggle, and what is lost at the end of the day is much needed cooperation.

Not much has changed over the last four (4) years. Actually, not much has changed over the last 23 years that ER has been a large part of the Ontario WSI scheme. Employers support it. Labour condemns it.

All three Ontario political parties have supported ER when in government

However, it is telling that ER has survived and flourished under the political stewardship of all three Ontario political parties. Modern ER was introduced as a design experiment in 1983/84 under a Progressive Conservative government. Under the Peterson Liberals it underwent its first major expansion in 1986. Under the Bob Rae NDP it was applied to the entire system in 1992. It continued to be reformed and revised under the Mike Harris government in the late 1990s.

So, all three political parties have had their hands in the "ER pie". **No party (including the NDP) killed it when given the chance.** And, in that I think lies the real story – ER is a credible program.

ER manages the "moral hazard" of WSI

So, what does ER actually do? Why is it so prominent? I have written about this before, but it bears repeating. Experience rating deals with the management of "**moral hazard**" in workers' compensation insurance, which is the "**resulting tendency of an insured to under-allocate to loss prevention after purchasing insurance**".

The under-pinning economic theory

The underlying economic theory under-pinning experience rating is straight forward – **higher costs internalized by employers for injuries should translate into workplace safety expenditures.** Professor Paul C. Weiler in his seminal 1980 study explains that experience rating modifies collective liability in a positive manner, building on the theory that "**business reacts to economic incentives**". Economic theory advances the proposition that experience rating "**causes employers to take socially desirable preventative actions to reduce work accidents**".

Critics argue that this same theory motivates employers to hide claims and make-up phoney degrading jobs

ER critics have long argued that ER drives very negative behaviours, such as those set out in the NDP motion. I have addressed these concerns before and will speak to them head-on right now. **They are baseless.**

I addressed this criticism in February 2007 when I appeared before the **Standing Committee on Government Agencies**. As I reported in the March 12, 2007 issue of **The Liversidge e-Letter**:

If the self-interested business person says, "*I'm going to skirt the system. I'm going to pay the worker under the table not to come into work and I'm not going to report that claim to the Workplace Safety Insurance Board, and somehow I'm making money,*" he's not. "**He's not only breaking the law and open for the prosecution that I've outlined earlier, but there's no financial gain in it at all. If you go through the numbers, there's absolutely proof that you aren't better off skirting your insurance program by directly self-insuring. It's absurd. It doesn't happen. I've shown these numbers in the past**".

The critics allege two untoward ER outcomes. **The first** is that employers will routinely hide claims. **The second** is that an employer will force a worker back to a phoney and degrading "**make work**" type job that has no true economic value, and is offered simply to avoid WSI costs. **I will debunk both allegations.**

ER critics are alleging that ER *promotes* rogue employer behaviour. In other words, the business decision-maker is making an untoward but nonetheless rational business decision to promote its business self-interest. **Essentially the argument is this - employers will either hide claims or make up phoney jobs to save money.** I will show that the very employer the critics are concerned about - *the rational self-interested employer interested only in saving money* - will be the last person to behave in this fashion.

Employers are not dissolute social actors

Let me make this perfectly clear – I reject and am infuriated by allegations that Ontario's employers are cold-hearted, self-interested financial maximizing ogres who will engage in immoral and illegal behaviour to save a buck. Frankly, these allegations debase what I know are well intentioned motives of those today criticising ER, who as much as anyone, seek to promote workplace safety and effective return to work. While every successful employer keeps an eye to the bottom line, by no stretch can this be transformed into a licence to rationalize immoral or illegal behaviours. By even suggesting this, the critics do not understand at all the workings of the very programs they are attacking. **In short, the critics are not well informed.**

The first allegation – hiding claims

But, for the sake of argument, and to dispel this spurious thesis, let me assume that such an employer exists – *the self-interested employer that would do anything for a buck* – even break the law, not report claims and make up phoney jobs. **I will prove that even such an employer would not behave in the fashion alleged because of ER.**

Even the immoral employer won't do this because of ER

I will show that the very ER programs that are being slammed rationally deter even the immoral employer from behaving in this fashion.

It is virtually impossible to hide a claim

It is virtually impossible for an employer to hide a claim. I am not suggesting that it never happens – I am just saying that the checks and balances in the system make it almost impossible.

First of all, the doctor will send in a doctor's report (Form 8) and account directly to the Board. If this does not match with an employer's report (Form 7), a claim is established anyway. *This is almost an absolute fail-safe.* But, let us presume it doesn't work. To stop the claim, the employer will have to pay the worker directly, or the worker will go to the Board for wage loss payments.

This type of fraudulent scheme would only work for short-term injuries (if it could work at all)

Realistically, this fraud - *and that is what it is* - would be workable for short term, minor injuries only. A significant injury will not only result in a multitude of medical reports being sent off to the WSIB (which would quickly expose the employer fraud) but the employer will be forced to pay wages "under the table" so to speak, indefinitely. As I will show in a moment, that is not financially viable (and remember, the allegation is that the financially self-interested employer will do this to save money).

But there is no financial gain in hiding short-term claims

But here is one gaping problem with all of this – there is no financial benefit for hiding the short term claim.

Here is how the numbers would play out in a "real life" example: A worker earning \$1,100 per week (\$882 net) is injured on-the-job and is off for three (3) weeks. The employer does not submit the claim and continues to pay the worker full salary even though disabled and off work. The employer pays about \$250,000 to the WSIB and doesn't report the injury buying into the ER critics' thesis that it is financially viable to do so. ***Except it isn't.***

How much must the non-reporting fraudulent employer pay to finance the fraud? *Well, that's easy* - three weeks salary - \$3,300. **How much does the employer save?** *Well, that's easy too.* **Nothing.** **In fact, this "scheme" will cost the employer!**

If the deviant clever employer does this, the employer will "save" the costs of the claim. Except, the claim would only cost the employer \$2,568. ***Yes, that's right.*** \$2,568 (\$2,259 past awards; \$935.55 projected future costs; \$1,242 overhead costs; 58% Rating Factor). ***So, let's see just how ever so clever this devious self-interested employer is*** – he will break the law and pay out \$3,300 to gain what? *To cost himself \$732.* ***Yup. If he had submitted the claim and played by the rules he would be \$732 ahead.***

Oh, and by the way, he has now opened himself up for a prosecution under the *Workplace Safety and Insurance Act* [WSIA] and could see his company fined \$100,000, himself

fined an additional \$25,000 and risks up to six (6) months in the hoosegow to boot. So, we are being asked to believe that this self-interested employer would actually behave in this fashion. *Would he?* No, not even the self-maximizing devious morally corrupt employer (even if there is one).

The second allegation – phoney jobs

The second allegation is that a rational business person will return a worker to unsustainable and economically unproductive employment in order to avoid ER surcharges. Implicit in this theory is that the ER programs encourage such behaviour. ***This, to be blunt, is simple nonsense.*** As I will show, for small, medium and large businesses alike, the rational, informed business person, even if inclined to present such an offer of employment (a thesis I reject), would not do so for business reasons. In other words, the rational pursuer of self-interest would not make such an offer for self-interested business reasons. *I will prove it.*

The spurious allegations are easy – the rational, honest explanation gets a little technical

The ER critics either don't understand the ER program they are slamming or are exploiting the hard-to-understand technicalities. ***But, it is in the technical details that the allegations are proved false.*** That though has been the problem with this debate from the get-go. The disparaging allegations are easy and can be summed in a sentence or two. The counter-argument though takes a little knowledge and a lot of ink. And, to make this all the more difficult, the WSIB - *the very author of the ER programs* – has been doing too little to defend and support its own programs.

Consider three examples – the allegations are fiction

Presume the following facts. A high wage earning skilled worker (\$69,400 per year or \$34.70 per hr.) sustains a fairly serious work injury, and is disabled from his pre-injury employment, but is fit for suitable employment. The employer presents the worker with a "make work" type job that is within his physical ability but has an actual economic value of \$7.75 per hour (2006 minimum wage). The employer chooses to pay the worker his pre-injury wage of \$34.70, a *de facto* \$27 per hour premium, ostensibly to acquire a financial benefit over potential ER surcharges. Let me look at a small, medium and large employer to see if this financial benefit actually presents itself. Presume that for all of these examples, had the employer not returned the worker to this unproductive employment, the worker would remain on claim for the long-haul. The examples use 2006 factors.

The small business example: 23 employees and a WSIB premium of \$63,519.85. That employer has "expected costs" of \$6,745.81, a rating factor ["RF"] of 40% (the minimum), a maximum rebate potential of \$2,698.32 and a maximum surcharge potential of \$5,396.65. For this "dodge" to work and to avoid ER costs the employer would be required to pay the worker's full salary for three years to avoid the case being "active" while the ER "window" remains open. So, even before the calculations are made, it is readily apparent that this astute, ever so clever business

person has scammed who? - *only himself*. For the three year period, he would fork out over \$166,200 in *extra* wages to avoid a \$5,396.65 surcharge. Would *any* employer do that? Certainly, the self-interested maximizing employer, the very beast the critics are worried about, *would not do it*. ***A stupid business decision of paying unsustainable, uneconomic wages cannot be transformed into a sound business decision even when subjected to the remarkable arithmetic of the Board's ER program.*** So, case number one debunked. Soundly.

The medium business example: 93 employees and a WSIB premium of \$256,860.33. That employer has “expected costs” of \$70,020.13, a RF of 58%, a maximum rebate potential of \$40,611.60, and a maximum surcharge potential of \$81,223.20. The maxed out claim costs would drive a maximum surcharge for the employer. Again, for this “flim-flam” to work for the three year period, the employer would fork out over \$166,200 in *extra* wages to avoid a \$81,223.20 surcharge. A better deal than the earlier example. This time, the self-interested maximizing employer is getting a \$0.50 return for every \$1.00 invested in extra wages. ***He will go broke half as fast as the first example, but broke he will be.*** So, case number two debunked.

Lastly, the big business example: 1,787 employees and a WSIB premium of \$4.8 million, and a 100% RF. A “maxed out” claim of \$270,800 will have a cash impact in the same amount. This time, the numbers at least partially support the critics’ thesis – the \$166,200 in *extra* wages is less than the potential cash impact of the claims. In fact, there is a \$61,000 benefit. Now, this is a large employer. If unionized, the “make work” approach would be prohibited by the collective agreement. So, no worries there. Of course, for the critics’ worries to hold true, one would have to believe that a large sophisticated employer would be willing to fork out \$166,200 in inflated wages to a worker to do a job that does not have to be done in the first place! Instead of doing something “radical”, like finding sustainable, suitable employment that actually provides an economic benefit to the business. Of course, an employer this large will have more than this one accident, and would have to engage in such a “practice”, say 20 times. That means that for the critic’s concerns to hold water, this particular employer would have to fork out \$3.3 million in unearned wages! ***Unlikely. And, if any large employer did engage in such a practice, well, they would not be a large employer for very long.*** Third case debunked.

And, these examples have not even factored other relevant considerations such as severance and notice costs, low morale, low productivity and the cumulative affect of engaging in unsupportable business practices.

The bottom line: The very economic theories that the critics worry will motivate untoward behaviour actually will encourage the opposite – the provision of sustainable and economically vibrant suitable employment. The critics

cannot base ER policy development on a silly assumption that Ontario business will make unsustainable business decisions.

If employers are acting irrationally – it is because they do not understand

I have no doubt that some albeit very few employers may act in the manner feared by the critics. I am sure a few cases will be “exposed”. But, all this exposé will show is that these employers simply do not understand the inner-workings of the Board’s ER programs, in much the same manner the critics themselves are inadequately informed. *I fully understand why*. It is almost impossible for most employers to actually benefit from the business case method ER promotes because the arithmetic is so darn confusing. Most employers do not understand the WSIB ER reports, let alone feel at ease to engaging in various “what if” scenarios to test and price ESRTW alternatives. *I know most WSIB officials can't do it*.

This lack of understanding is entirely the Board's fault. The Board has not used its communication powers to better explain ER and make it easy for employers to facilitate the essential “what if” calculations (which by the way, I challenge WSIB employees to efficiently calculate).

The Board’s website provides the following: “*If your claims costs are lower than would be expected for a company of your type and size, you receive a rebate. If your claims costs are higher than would be expected for a company of your type and size, you are assessed a surcharge*”. Employer’s understand these general rules. What is not understood is the actual effect of individual cases, let alone how the case-specific business analysis should be addressed. This has been a long-standing weakness in the Board’s ER programs, which *requires* this knowledge and application to be effective.

The bottom line: I believe that the critics are well intentioned, but woefully misinformed. However, feathers have been so fluffed up that no one can back down. This has long passed being about ER. It is now about short-game politics. It is now about embarrassing the Board and the government (both of which have been giving the critics easy targets – everything that I have been saying in this series of **The Liversidge e-Letter** should have been said by the Board. Why the Board is slamming its own programs escapes me).

And, in just in case it is at all relevant – ER works!

Oh, and all the while an independent study has already concluded that ER “***functions well, encourages prevention and contributes to positive workplace health and safety practices***” (*Assessing the Effect of Experience Rating in Ontario*, June 2005, Institute for Work and Health).

NDP wants ER to be audited – I agree

The NDP has asked the Provincial Auditor to come in and assess ER. ***Actually, I tend to agree.*** The WSIB should stop its review. The critics won’t accept it anyway. Bring in the Provincial Auditor. Clear the air.