

# WORKERS COMPENSATION CLAIM COSTS AND TRENDS IN NEW JERSEY

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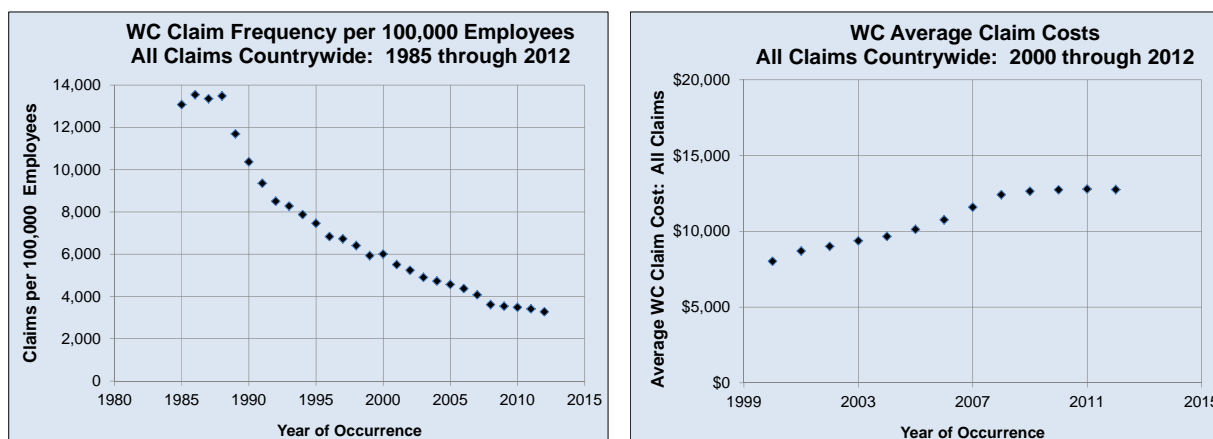
## Introduction

The cost and frequency of workers compensation (WC) claims vary greatly between the different states. Each individual state, or jurisdiction, has its own WC benefit structure, administrative system, and governing statutes. Compensation rates, maximum and minimum weekly benefits, automatic adjustments to maximum and minimum benefits, system utilization, industry mix, administrative efficiency, constraints on medical care, and general cost of living levels all vary, potentially significantly, by jurisdiction and represent a sample cross section of items that directly impact claim incidence and costs.<sup>1</sup>

As respects claim incidence, or frequency, there has been an overall downward trend to Countrywide WC claim frequency since the early 1990s. Generally, the observed long-term decline to claim frequency is common across all jurisdictions and industries.

The average claim cost, or severity, of WC claims naturally increases over time. Wage inflation has a direct impact on the cost of indemnity (wage replacement) benefits, while increases to the cost of medical services and pharmaceuticals have a highly leveraged impact on the cost of WC claims, where medical care is generally more complex and costly than services associated with general health care.<sup>2</sup>

Countrywide claim frequency and average claim costs are illustrated in the following graphs:



Actual metrics and their specific behavior over time vary widely by jurisdiction.

<sup>1</sup> For example, in Vermont, the maximum and minimum weekly benefits for WC claims are 150% and 50%, respectively, of the state average weekly wage (SAWW), \$816 (effective 7/1/2015). Total disability benefits are paid for the duration of disability, or life, and claimants receive an annual cost of living adjustment. In Mississippi, the maximum weekly benefit is 100% of the SAWW, and the minimum is fixed at \$25. The SAWW is \$702.91 (effective 1/1/2016). The maximum duration for all claims is 450 weeks (~9 years) with no cost of living adjustments. This illustrates differences in benefit structure and overall cost of living (the SAWW in VT is ~15% greater) between jurisdictions.

<sup>2</sup> In the early 1990s, the portion of WC benefit costs associated with medical services was approximately 40% of total benefit costs. Currently, that value is roughly 60%. This increase is a direct result of the greater cost inflation affecting medical benefits, relative to payroll inflation which impacts indemnity benefits.

The purpose of this paper is to examine and discuss metrics specific to the State of New Jersey (NJ). More precisely, the paper will:

- Present current and historical claim incidence rates (claim frequency) in NJ;
- Present current and historical estimates of average WC claim costs in NJ based on the most recently available insurance industry data;
- Benchmark claim frequency, claim costs, and overall costs against Countrywide metrics; and
- Discuss NJ's relative WC cost ranking compared to other states.

Data used in this paper is from the New Jersey Compensation Rating & Inspection Bureau (NJCRIB), the National Council on Compensation Insurance (NCCI), and other miscellaneous sources of insurance industry information. The NJCRIB is the WC data collecting organization in New Jersey. The NJCRIB is an extension of the insurance industry, is licensed by the state, and analyzes WC claims data collected from all insurance companies doing business in the state. The NJCRIB uses this data to calculate premium rates and other rating values for all WC employee classifications.

The NCCI is the WC data collecting organization in 36 jurisdictions. The NCCI is licensed in states such as Florida, Virginia, the District of Columbia, Mississippi, etc. The role of the NCCI is identical to the role of the NJCRIB. The NCCI is an extension of the insurance industry and analyzes WC claims data collected from all insurance companies doing business in a specific state where the NCCI is licensed. The NCCI uses this data to calculate premium rates (or loss costs, depending on the jurisdiction<sup>3</sup>) and other rating values for all WC employee classifications. CA, DE, MA, MI, MN, NY, NJ, PA, and WI all have their own independent data collecting organizations. IN and NC do as well, however, the NCCI provides statistical services to the local organizations in those jurisdictions. Jurisdictions with exclusive state mandated WC insurance funds manage their own data and include ND, OH, WA, and WY.

Countrywide data used in this paper is based on NCCI data, which includes combined data only from those states in which the NCCI operates. States with exclusive WC insurance funds are excluded because data is generally unavailable. NJ and other states with independent data collecting organizations listed in the paragraph above, except NY and CA, are excluded because testing showed that the impact of data from these states on Countrywide metrics would be minimal. As respects NY and CA, material law changes over the past decade as well as the size, cost, and other unique attributes of these two states generate WC metrics with fundamentally different behavior than in any other jurisdiction. Data from NY and CA was excluded because data from these states would materially impact and distort Countrywide metrics due to the sheer size of these jurisdictions and the fundamentally different behavior of their WC metrics.

Footnote references throughout the paper provide additional detail and context around the text.

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<sup>3</sup> Some jurisdictions require filing of premium rates, which provide for benefits, claim related expenses, insurance company expenses, taxes, profit, etc. Others require the filing of loss costs. Loss costs are generally benefits and claim related expenses. Individual carriers then add on their own specific provisions for company expenses, taxes, profit, etc. The definition of loss cost may vary by state. Loss costs include benefits and claim related expenses in some states, while in others loss costs include only benefits, and insurance carriers must add on their own provision for claim related expenses, as well as other expenses, taxes, profit, etc.

## Claim Frequency

### Introduction

“Lost time” and “medical only” are the two most general categories of WC claims. Lost time (LT) claims are sufficiently serious to warrant lost work time of sufficient duration<sup>4,5</sup> such that the employee qualifies for wage replacement benefits. Conversely, medical only (MO) claims are cases where wage replacement benefits have not been and are not expected to be paid. MO claims are generally characterized by minor injuries requiring minimal medical treatment with little or no lost work time. Countrywide, LT claims represent only 25% of total claim volume, but generate 93% of total WC benefit costs. Conversely, MO claims represent 75% of total claim volume, but generate only 7% of total WC costs. NJ and Countrywide metrics are compared below:

WC Claim Incidence Distribution by Claim Type			
	LT	MO	ALL
COUNTRYWIDE	25%	75%	100%
NJ	33%	67%	100%

WC Cost Distribution by Claim Type			
	LT	MO	ALL
COUNTRYWIDE	93%	7%	100%
NJ	94%	6%	100%

The metrics above are based on 2012<sup>6,7</sup> data. Note that while a much greater percentage of claims in NJ are more expensive LT claims, the overall distribution of costs between LT and MO claims is almost identical to the Countrywide distribution. This is due to the much higher cost of MO claims<sup>8</sup> in NJ relative to other jurisdictions (discussed later in this paper).

<sup>4</sup> States generally have a “waiting period” for wage replacement benefits ranging from 3 to 7 lost workdays. Wage replacement benefits are paid only if the disability exceeds the waiting period. The employee is retroactively reimbursed for wages lost during the waiting period only if the disability exceeds a specified duration defined as the “retroactive period.” For example, with a waiting period of 7 days and a retroactive period of 14 days, the claimant will begin receiving wage replacement benefits on day 8 of the claim, and will be reimbursed for lost wages during the waiting period (the first 7 days of the claim) only if the claim duration exceeds 14 days. Waiting and retroactive periods affect wage replacement benefits only. The employer (or the insurer) is responsible for funding the cost of all medical care, as provided for in underlying statutes and regulations.

<sup>5</sup> In NJ, the waiting period and the retroactive period are the same, 7 days. If the number of lost workdays is 8 or greater, the injured employee will receive wage replacement benefits on a going forward basis, and will be retroactively reimbursed for lost wages for the first 7 lost workdays.

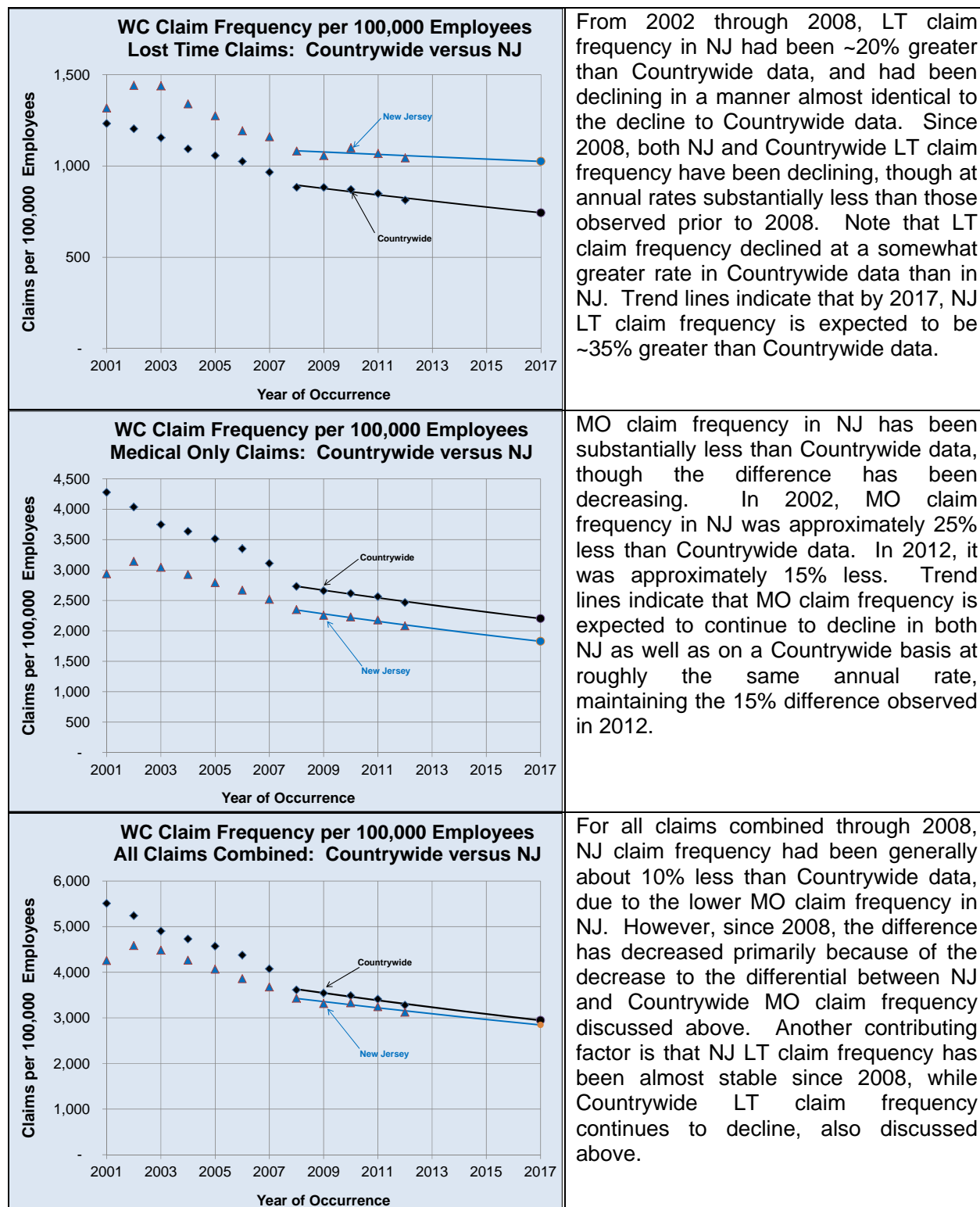
<sup>6</sup> Years, as used in this document, generally refer to the year of occurrence. 2012 therefore refers to data generated by all claims with dates of loss in 2012. Note that this is an approximation, given that underlying data used to produce this document may not precisely match the definition of 2012 as year of occurrence. The impact of this approximation is not material.

<sup>7</sup> 2012 represents the most recently available data from the NJCRIB. This is because the NJCRIB must collect, compile, and examine data generated by every insured WC claim in the state. This multi-year lag between collection and publication is common and expected in the insurance industry.

<sup>8</sup> The percentage of MO claims in NJ is much lower than Countrywide (which lowers overall MO costs), but the average cost of an MO claim in NJ is much greater than Countrywide (which raises overall MO costs). The net impact is that the distribution of costs between LT and MO claims in NJ is roughly the same as Countrywide data.

## Claim Frequency Measurements

The following three graphs compare LT claim frequency, MO claim frequency, and total claim frequency between NJ and Countrywide data for 2002 through 2012. Trend lines indicating potential values for 2017 are provided as well.



## Frequency Trends

The graphs on the prior page compare NJ metrics to Countrywide averages. The trend lines on the graphs are based on the most recently available data, reflecting observed changes to frequency trend beginning in 2008. Generally, relatively steep declines to claim frequency are observed prior to 2008, followed by a much smaller annual decline subsequent to 2008. Observed trends are presented below for each claim category (LT, MO, Total).

### Lost Time Claims:

LT Claim Frequency Trends		
Time Period	Countrywide	New Jersey
2001 - 2012	-3.9%	-3.0%
2001 - 2008	-4.4%	-3.6%
2008 - 2012	-2.0%	-0.6%

NJ specific trends are very close to Countrywide measurements. Of note is that subsequent to 2008, NJ lost time claim incidence is almost constant, whereas Countrywide LT claim incidence continues to decline.

### Medical Only Claims:

MO Claim Frequency Trends		
Time Period	Countrywide	New Jersey
2001 - 2012	-5.1%	-3.8%
2001 - 2008	-5.6%	-3.6%
2008 - 2012	-2.4%	-2.7%

Generally, MO incidence in NJ has declined at a somewhat lower rate of decline over time than Countrywide measurements. However, since 2008, MO incidence in NJ has been declining at an annual rate roughly the same as Countrywide values.

### All Claims Combined:

All Claims Combined Frequency Trends		
Time Period	Countrywide	New Jersey
2001 - 2012	-4.8%	-3.6%
2001 - 2008	-5.3%	-3.6%
2008 - 2012	-2.3%	-2.0%

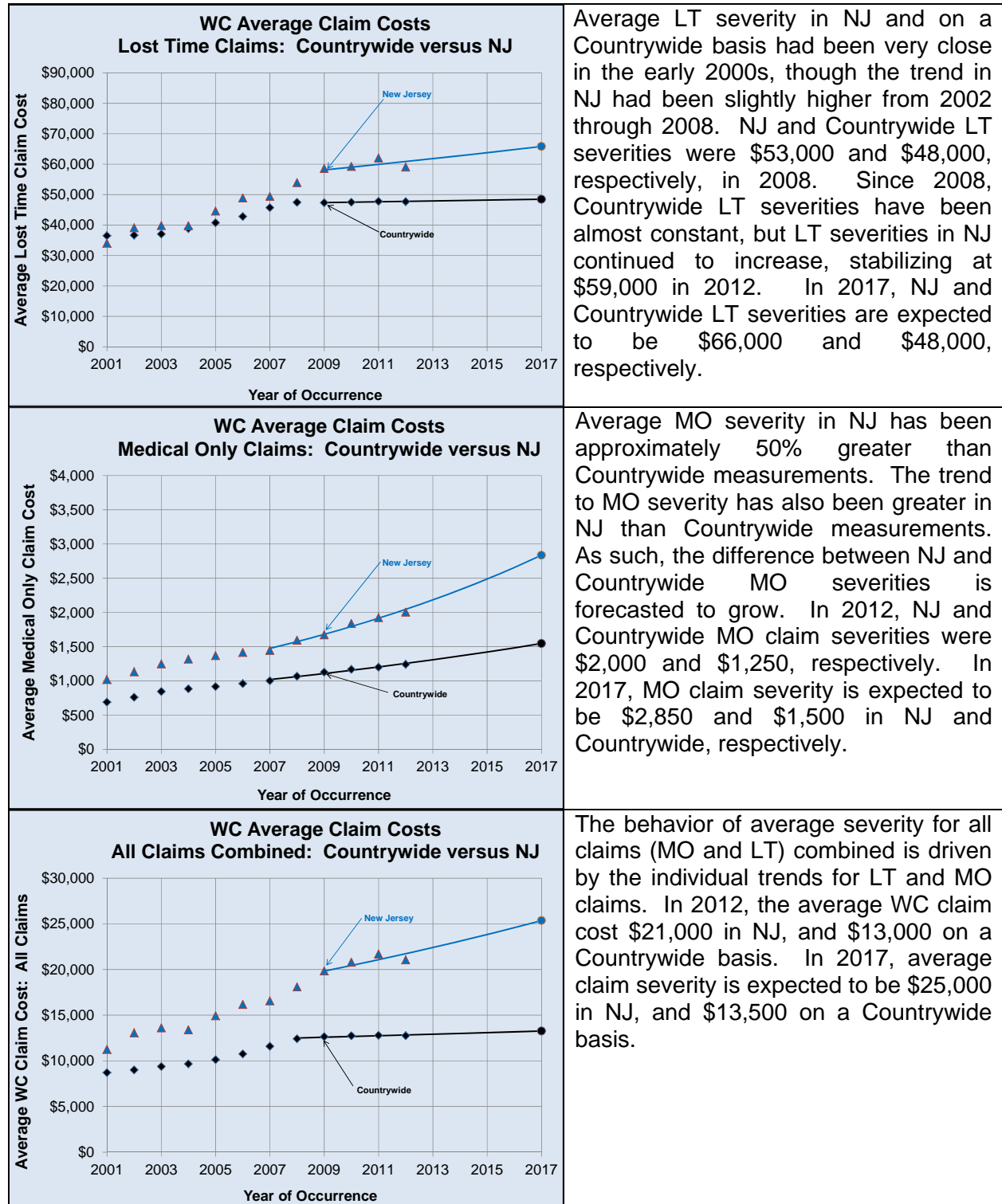
The trends in total claim incidence reflect the combined impact of LT and MO components.

Note that the change in trend in the 2008 time frame is generally a common phenomenon across most jurisdictions and is likely a direct result of the economic disruption that occurred at about the same time.

## Claim Severity

### Severity Measurements

The following three graphs compare LT claim severity, MO claim severity, and total claim severity between NJ and Countrywide data for 2002 through 2012. Trend lines indicating potential values for 2017 are provided as well.





## Severity Trends

The graphs on the prior page compare NJ claim severities and trends to Countrywide averages. The trend lines on the graphs are based on the most recently available data, reflecting observed changes to severity trends generally beginning in 2008. Observed trends are presented below for each claim category (LT, MO, Total).

### Lost Time Claims:

Lost Time Claim Severity Trends		
Time Period	Countrywide	New Jersey
2001 - 2012	3.0%	5.6%
2001 - 2009	4.0%	6.5%
2009 - 2012	0.3%	0.7%

NJ specific trends to LT claim costs are generally greater than Countrywide metrics. Since 2009, both NJ and Countrywide LT claim costs have increased only slightly, though NJ LT claim costs continue to increase at a greater rate than Countrywide metrics.

### MO Claims:

Medical Only Claim Severity Trends		
Time Period	Countrywide	New Jersey
2001 - 2012	5.2%	6.0%
2001 - 2007	6.1%	5.8%
2007 - 2012	3.7%	6.1%

Generally, MO costs in NJ have been increasing at rates somewhat comparable to Countrywide metrics, though more recently MO costs in NJ have been increasing at a greater annual rate. 2017 forecasts are \$2,850 and \$1,500 for NJ and Countrywide data, respectively.

### All Claims Combined:

All Claims Combined Severity Trends		
Time Period	Countrywide	New Jersey
2001 - 2012	4.1%	6.1%
2001 - 2009	5.1%	6.6%
2009 - 2012	0.3%	2.2%

The trends in the average cost per claim for all claims combined reflect the blended impact of individual components. The higher recent trend in NJ relative to the Countrywide average is due to the combined impact of continued growth to LT claim costs, the higher proportion of LT claims in NJ, and the relatively high growth to MO claim costs. 2017 forecasts are \$25,000 and \$13,500 for NJ and Countrywide data, respectively.

Note that the change in LT claim severity trend in the 2008 time frame is generally a common phenomenon across most jurisdictions and, similar to frequency, is likely a direct result of the economic disruption that occurred at about the same time.

## Total Cost Ranking

The cost of WC insurance varies widely among jurisdictions for the reasons stated in the introduction to this paper. Complicating the issue is the variation of industries between different states. The impact of this latter item is easily seen if the majority of payroll in one state is in the logging industry, and the majority of payroll in another state is in financial services. A comparison of the average WC cost relative to payroll between these two states does not have meaning, given how hazardous the logging industry is relative to the financial services industry. This concern is addressed by using a common distribution of payroll by WC employee classification for all states to measure cost. The ranking was calculated by obtaining the cost of benefits and claim related expenses<sup>9</sup> by WC employee classifications by jurisdiction<sup>10</sup>, and then averaging this information by jurisdiction using the assumed payroll distribution. The result of this exercise shows that NJ currently ranks in the top 10 most expensive jurisdictions. In fact NY, CA and NJ the three highest cost states, have metrics that are very close to one another, and are significantly greater than other states.

Average Cost of Indemnity Benefits, Medical Benefits,  
and Claim Related Expense per \$100 Payroll  
All Classifications  
Oliver Wyman Calculations

RANK	STATE	Average Cost per \$100 payroll
1	NY	2.31
2	CA	2.24
<b>3</b>	<b>NJ</b>	<b>2.20</b>
4	DE	1.72
5	CT	1.68
6	MT	1.58
7	AK	1.52
8	VT	1.49
9	GA	1.45
10	IL	1.37

<sup>9</sup> Claim related expense refers to expense costs attributable to individual claims and general claims administration expense. Expenses attributable to individual claims include, but are not limited to, the cost of legal defense, surveillance, private investigation, document production, independent medical examinations, and others. General claims administration expense would include salaries and overhead of adjusting staff and similar expenses.

<sup>10</sup> This approach was used in jurisdictions where the required information and underlying data was available. Jurisdictions where this information is not available include the four states with monopolistic state funds, that is, states with only one WC insurer that is a state sponsored insurance company. For these and other jurisdictions where the necessary data is not available, other publicly available information was used to estimate the rank of these jurisdictions.

The ranking reflects the actual cost of medical benefits, indemnity benefits, and claim related expenses, without consideration of insurance company related expenses, profit, taxes, and investment income offsets.<sup>11</sup> The ranking is therefore a true measure of the cost of benefits and claim related expense by jurisdiction.

The workers compensation employee classification with the highest payroll in most, if not all jurisdictions, is 8810, clerical employees. This is a very low cost classification and not a material source of claims. In the ranking exercise, 8810 represents about 40% of total payroll. If 8810 were excluded, the ranking is not materially changed, as illustrated below:

Average Cost of Indemnity Benefits, Medical Benefits, and Claim Related Expense per \$100 Payroll All Classifications Excluding Clerical Oliver Wyman Calculations		
RANK	STATE	Average Cost per \$100 payroll
1	NY	3.75
<b>2</b>	<b>NJ</b>	<b>3.54</b>
3	CA	3.49
4	DE	2.75
5	CT	2.73
6	MT	2.40
7	VT	2.34
8	GA	2.33
9	AK	2.28
10	IL	2.21

When measured without clerical payroll, NY, CA and NJ are still the three highest cost states, still have metrics that are very close to one another, and are still significantly greater than other states.

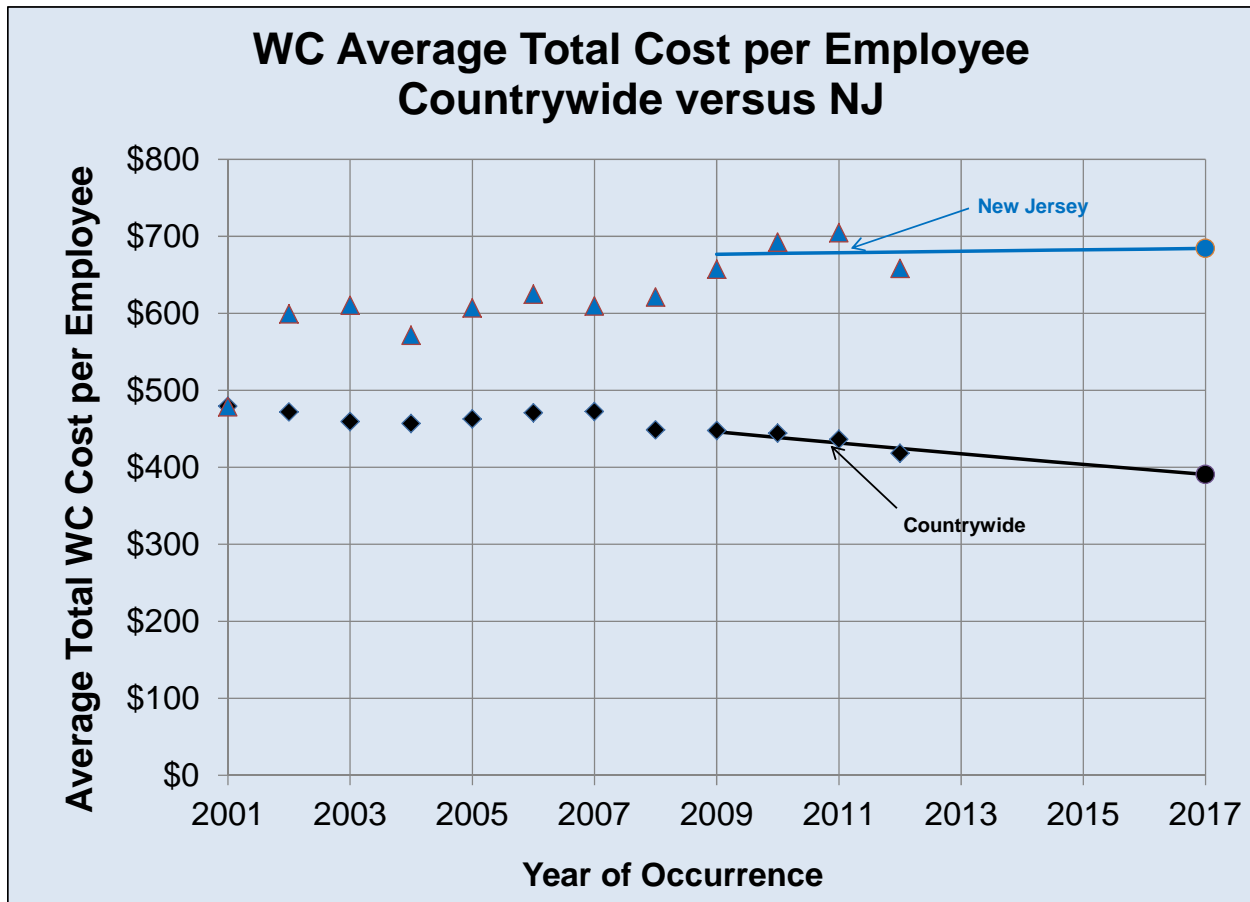
<sup>11</sup> Insurers will earn investment income on financial reserves established to fund claim payments. Insurers will often reflect anticipated investment income to offset premium rates. Investment income offsets (as well as any other insurance charge or discount) are not included in the rankings with the exception of the monopolistic state funds. Monopolistic state funds generally will establish premium rates with a substantial offset for investment income earned on financial reserves. The ranking of the monopolistic fund states *includes* any offsets for investment income in underlying premium charges. All other jurisdictions in the ranking do not. Therefore the monopolistic fund states include a potential offset not included in other jurisdictions. The result is the monopolistic fund states are likely too low in the ranking.

In 2016 the Oregon Department of Business and Consumer Services (DBCS) published a biennial study that ranks each state according to total WC costs. The Oregon study considers the total net cost of WC insurance, and therefore includes, in addition to benefit costs and claim related expenses, insurance company related expenses, profit, taxes, investment income offset, as well as competitive adjustments and discounts provided by insurers to certain employers. The general ranking of the Oliver Wyman study is quite similar, but not precisely the same, as the Oregon study. The results of the Oregon study are presented below:

Average WC Premium Cost Oregon Department of Business and Consumer Services 2016 Biennial Study		
RANK	STATE	Average Cost per \$100 payroll
1	CA	3.24
<b>2</b>	<b>NJ</b>	<b>2.92</b>
3	NY	2.83
4	CT	2.74
5	AK	2.74
6	DE	2.32
8	OK	2.23
8	IL	2.23
9	RI	2.20
10	LA	2.11

Note that while there are differences in the ranking between the DBCS study and the Oliver Wyman studies, the general ranking is similar and, in fact, the same three states, NY, CA, and NJ, are the three highest cost states in the country in all measurements.

The following graph illustrates the average total WC cost per employee in NJ relative to Countrywide values. The distinguishing characteristic is that while average costs had ranged between 25% and 35% greater than Countrywide values through 2008, subsequent to 2008, Countrywide costs per employee have actually decreased, while NJ costs have increased materially, though the most recently available data indicates some level of stabilization.



## Summary

NJ is the third highest cost state when measuring the cost of benefits and claim related expense per \$100 payroll. In other rankings, NJ is consistently in the top three states as respects workers compensation costs. The underlying reasons for high WC costs in NJ include:

1. LT claim frequency in NJ has been higher than, and growing relative to, Countrywide data.
2. LT claim severity in NJ has been materially higher than and growing relative to, Countrywide data. Note that preliminary data for 2013 indicates that the decline in LT claim severity in 2012 was an aberration (see claim severity graphs), and that costs are once again increasing.
3. MO claim costs in NJ have been materially higher than, and growing relative to, Countrywide data.

Distinguishing characteristics within the NJ workers compensation system include:

1. Unlike many other states, there is no WC medical fee schedule in NJ. Physicians are permitted to charge “reasonable and customary” fees.
  - a. The lack of a fee schedule is likely an explanation for the very high cost of medical only claims in NJ. Medical only claim costs in NJ rank in the top five highest cost jurisdictions.
  - b. Medical cost containment expenses (MCCE) are extraordinarily high in NJ, and have increased materially over the past five years. MCCE include, but are not necessarily limited to, the cost of case management, bill reviews, and utilization reviews.
  - c. MCCE represents approximately 25% of the combined cost of medical benefits and MCCE in NJ.
2. Workers compensation claims, subsequent to settlement, may be reopened up to two years after the last date of payment of benefits and the employee can seek additional medical, temporary or permanent disability benefits.<sup>12</sup>
3. Claim related expense<sup>13</sup> is a higher than average portion of overall costs in NJ. Measured relative to losses, claim related expense has ranged between 19.3% and 19.8% in NJ for the past five years, meaning that for every dollar of benefit costs in NJ, there is an additional 19 to 20 cents of claim related expense cost. Claim related expense is generally 18.5% losses. The percentage difference may seem small, however, claim costs in NJ are high and the combined impact of higher claim costs with a higher percentage of claim related expense leads to high claim related expense costs in NJ on a per claim basis.

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<sup>12</sup> This applies only to Section 22 settlements. These are compromise and release agreements where the claimant will receive a disability rating, with the exception that in NJ, the claimant does have the option to reopen the claim, as described. Under a Section 22 settlement, the employer acknowledges that there is a WC claim. Section 20 settlements, however, may not be reopened. A Section 20 settlement is possible only when there are questions as to whether a claim is compensable as a WC claim under the NJ state act. Settlements under Section 20 are not considered WC payments except for insurance rating and data purposes.

<sup>13</sup> Claim related expense is also known as Loss Adjustment Expense (LAE). LAE has two components: Defense and Cost Containment Expenses (DCCE) and All Other Expenses (AOE). DCCE generally represents costs that may be allocated to individual claims and includes defense costs, medical cost containment expenses, and any other cost that may be attributed to a specific claim. AOE represents all other claim administration expenses that are not attributable to a specific claim.

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