2022 U.S. Workers' Compensation Market Outlook

Helping you come through for your clients

RISK PLACEMENT SERVICES

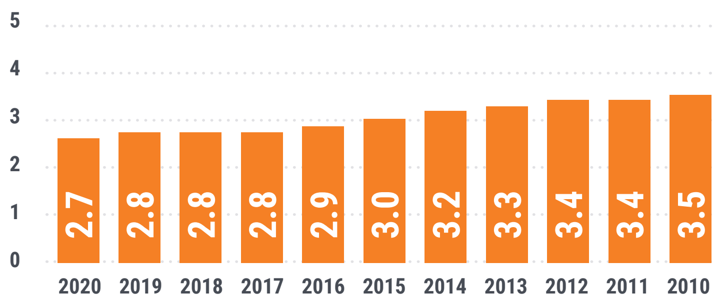
APPEARANCES CAN BE DECEIVING

The statutory Workers' Compensation market is a popular place for U.S. insurance companies and managing general agents (MGAs). The reason: consistent profitability, despite steadily decreasing rates and premiums.

Even 2020's dramatic 8.1% decrease in premiums[1] didn't mar this insurance line's track record.

A sustained drop in claim frequency is part of what makes the unusual combination of profitability and lower premiums possible. While the COVID-19 pandemic did contribute to a reduction in claim activity in 2020, claim frequency had been on the decline for several years as insureds have placed a greater focus on promoting a safety culture.

NONFATAL WORKPLACE INJURIES AND ILLNESS PER 100 FTE



Source: Bureau of Labor Statistics (BLS), Survey of Occupational Injuries and Illnesses

Yet, Patrick Edwards, Area Senior Vice President, Workers' Compensation Practice Leader, Risk Placement Services (RPS), cautions that the Workers' Comp market may hit some bumps in the road, sooner rather than later.

"Many of the metrics we use to measure the health of this market, such as decreased calendar year combined ratios, are better at showing us where the Workers' Comp market was, rather than where it will be," observed Edwards. "And while there's a correlation between the two, there has been too much disruption over the past two years, such as the Great Reshuffle, healthcare inflation and the COVID-19 pandemic, which needs to be taken into account. I believe that these factors and others, such as an aging workforce and the agile workplace, will have a negative impact on this market over the next few years."

Turmoil in the financial markets could also begin to have an impact on insurance line profitability, including Workers' Comp.

In May 2022, the Workers' Comp market applauded when the National Council of Compensation Insurance (NCCI) announced that 2021 preliminarily represented the fifth consecutive year of a calendar year combined ratio below 100. The fact that the accident year combined ratio had climbed above 100 made fewer headlines.

Turmoil in the financial markets could also begin to have an impact on insurance line profitability, including Workers' Comp.

"With equity markets and fixed-income assets down substantially in 2022, it may be difficult in the short term for insurers to offset continued rate decreases with investment gains. However rising interest rates could help bolster profits going forward, assuming that they aren't outpaced by the rising combined loss and expense ratios we've seen the last few years in California," noted L.J. Battagliese, Area President, RPS.

As of late August, the Bloomberg Global Aggregate Total Return Index of government and investment-grade corporate bonds had fallen more than 20% from its 2021 peak. Bond holdings make up a substantial portion of most insurance company investment portfolios.

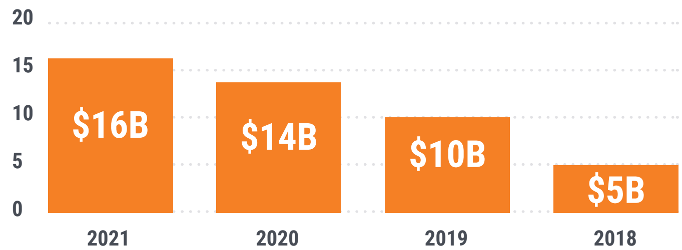
For 2021, the NCCI reported that investment gains accounted for slightly less than half of that year's Workers' Comp operating gains.

NEAR-TERM OUTLOOK

For the statutory Workers' Comp market, carriers will continue to see rate decreases through the remainder of 2022. Edwards anticipates a slowing of the already 40%–60% decrease in rate against most jurisdictions over the past 8–10 years.

The steady decrease in claims has created a healthy estimated Workers' Comp reserve redundancy of $16 billion, continuing a multiyear growth trend that began in 2018.

GROWTH OF ESTIMATED WORKERS' COMP RESERVE REDUNDANCY



Source: NCCI, State of the Line Guide

These healthy reserves were a factor in A.M. Best's decision to upgrade its outlook for the Workers' Comp insurance market from Negative to Stable in December 2021. They are also the reason that Workers' Comp combined ratios continue to look good on a calendar year basis while accident year ratios are deteriorating.

If 2022 plays out as many believe it will, the Workers' Comp market will experience its eighth consecutive year of profitability. For a cyclical industry, that's a long run.

"Every time I think the market has reached a point where rates are going to rise, they just continue to decrease," said Amanda N. Ikari, an Area Senior Vice President with RPS, who has worked in the Workers' Comp market for more than a decade. "Even COVID-19 failed to put a break on declining rates."

Mark Williams, Executive Vice President of Business Development, RPS, echoes Ikari's sentiment about this unusually long insurance cycle.

"The years of profitability within this insurance line are unprecedented, and that's why we see carriers continuing to enter the market," he said.

COMPETITIVE MARKET FOCUS

Because the Workers' Comp market is the "most attractive house on the block," according to Edwards, insurance companies and MGAs that are already in this market are looking to expand their book of business. They are doing so by entering into states where they previously didn't operate.

Another reason to move into a new state is to preserve existing business. Over the past two years, many companies have moved from states with a higher cost of living to ones that are more affordable.

"I've seen an increasing number of businesses either shift a portion of their business or move their entire operation to another state," reported Williams. "In these situations, the incumbent carrier can't retain the business unless they also operate in that new state."

Over the past few years, excess Workers' Comp rate increases have trended in the 5%–15% range.

Carriers are also increasingly willing to compete for higher hazard – and higher premium – business, a trend that Dayna Schneider, Area Senior Vice President of Underwriting, RPS, confirms.

"Brokers are asking us to provide quotes so they have a point of comparison to the insurers who are starting to dip their toe into a particular industry," Schneider noted. "Companies may carve out a higher-hazard segment where there's less competition or where the only current option is the State Fund."

While multiple insurers compete in the primary Workers' Comp business, in the excess market, where carriers work with self-insureds groups (SIGs) and joint powers associations (JPAs), as well as qualified self-insureds, it's a different story.

"In contrast to the primary market, where more than 200 carriers could be competing in a single state, there are six, active carriers that dominate the excess Workers' Comp market, each with a distinct appetite," explained Rafael Olivares, Area Vice President, at RPS. "In terms of price, most insureds in our market would benefit greatly with the addition of even just one additional carrier."

Over the past few years, excess Workers' Comp rate increases have trended in the 5%–15% range. Olivares anticipates that rates will continue to firm.

THE ROLE OF WEARABLES

There's no denying the role of loss control in the striking reduction in Workers' Comp claims. However, teaching workers not to lift more than a certain weight, or to get up and walk around after sitting for a certain period of time, is one thing. Making sure they do it is another.

Enter wearables.

A wearables technology program can help improve productivity and bolster a company's safety record. Items such as watches, bracelets and safety glasses with sensors can track the information being sought, based on the role of the employee.

Wearables can also be part of a return-to-work program. They can monitor an employee's physical movements and signal when they're pushing themselves too hard.

"With soft tissue injuries, wearables are similar to sports medicine in that they can have a positive impact on the healing process," noted Joe Clifford, Area President, RPS. "Wearables offer multiple benefits from both an injury prevention and injury recovery perspective."

However, in a competitive rate environment, it can be challenging to get insureds to adopt wearables. And often employees have privacy concerns about the data collected that the insured will need to overcome.

"Insureds often see this as an inconvenience," Williams explained. "That can make it a tough sale."

WANTED: EXPERIENCED EMPLOYEES

With the U.S. unemployment rate at 3.7% for August 2022, the labor shortage has continued even though pandemic disruptions have largely subsided. In order to fill open positions, even companies in high-hazard segments such as trucking and non-artisan trades have relaxed their hiring standards. Eager to get their new employees up and running, companies are rushing their training.

The result is an accident waiting to happen.

“In my experience, having comprehensive hiring practices with safety orientation and ongoing training is one of the best ways to prevent accidents,” observed Schneider. “It also creates a better performing risk.”

According to the Construction Industry Research and Policy Center, 44.5% of workers who were injured had two years or less of experience. Those who had been on the job for six months accounted for 30% of injuries.[2]

With experience often in short supply, older workers who have remained in the workforce are more critical than ever. They are also a growing percentage of the U.S. workforce. The Bureau of Labor Statistics (BLS) estimates that by 2026, the participation rate for workers aged 65 to 74 is projected to be 30.2%, compared with 17.5% in 1996.[3]

For older experienced employees who remain on the job, claim severity is higher as they take longer to recover. According to NCCI data, for workers age 65 and older, Workers’ Comp claim frequency continues to climb, compared to an overall decline in comp claims for other age groups in this data set. Those in this age group also spend more time off the job when injured: 16 days compared to an overall average of 8.[4]

While workers over the age of 55 account for 21% of Workers’ Comp claims, they are responsible for 31% of claim costs.

One trend Schneider is noticing is that employers are focusing on the whole health of the employee and creating a healthy work environment. That’s important given the disruption the pandemic created in employees’ personal and professional lives.

“When it comes to loss control, employers are now thinking beyond hazards and ergonomics,” she explained. “They recognize the investment in wellness initiatives and placing sincere emphasis on the safety and whole health of their workforce may have a favorable impact on their Workers’ Compensation experience.”

WORK FROM HOME

While workers are returning to the office in mid-2022, there's no question that work from home is here to stay, whether it's a full-time or hybrid arrangement. And while fewer employees coming into the office does lessen the chance an employee will slip in a puddle of water in the lobby, it also means that insurers need to consider new claims scenarios such as an employee:

- Tripping over their dog while getting a file, damaging their shoulder.
- Developing a bad back/degenerative disk associated with poor ergonomic conditions.
- Experiencing carpal tunnel syndrome due to a poor at-home computer setup.

The ease with which employees can work outside of standard business hours, Williams said, turns Workers' Comp into a 24-hour exposure.

"Another challenge that carriers will need to grapple with is the lack of witnesses to corroborate a claim," he added.

Work from home also has implications for how the coming-and-going rule is interpreted. For example, if an employee has an accident during their commute to the office, it's clearly not a Workers' Comp claim. However, if the employee works full time from home, that interpretation could change if the home is considered a secondary job site.

UNIQUE CHALLENGES, COMPLEX CLAIMS

As a statutory product, primary Workers' Comp differs from other Casualty coverages in a number of ways. All coverage is admitted in the primary market. Carriers have little control over their Workers' Comp policy form as language is fairly standard across all states. There are no limits, sublimits and exclusions to negotiate.

Given these parameters, Workers' Comp should be a fairly straightforward market. However, the various ways that a Workers' Comp program can be structured can add a level of complexity.

"Things can get complex in a hurry," noted Joe Clifford, Area President, RPS, who works with SIGs in Michigan. "Do you offer a refund based on claim performance? Is there a credit because your company is implementing wearable technology?"

In the excess market for SIGs, JPAs and qualified self-insureds, coverage can either be admitted or non-admitted. There are endorsements, such as communicable diseases. The treatment of allocated costs can also vary.

The long-tail nature of many Workers' Comp claims also makes things complicated. According to L.J. Battagliese, in California, it isn't uncommon for claims to remain open for three to five years or even close and reopen several times as an old injury flares up and prevents an employee from working.

> **The ease with which employees can work outside of the standard business hours, turns Workers' Comp into a 24-hour exposure.**

Construction, trucking, logging and forestry, mining, non-artisan contractors and staffing/farm labor all account for high-hazard occupations resulting in more Workers' Comp claims.

Cumulative trauma claims often start out simple but quickly grow in complexity and cost. These workplace injuries, such as hearing loss, tendinitis or carpal tunnel, result from repetitive motion extending over a period of time.

In a 2018 report, the Workers' Compensation Insurance Rating Bureau (WCIRB) of California stated that, "Cumulative trauma claims are significantly more likely than other indemnity claims to be represented, filed post-termination of the employee, and initially denied." In addition they were "found to be significantly more complex than other claims and much more likely involving multiple claims filed by the same claimant…"[5]

The WCIRB report also said these claims more frequently involved multiple body parts and mental trauma when compared to specific injury claims.

CHANGING THE RULES DURING THE GAME

The role of state insurance regulators in dictating coverage terms means that policy language can be amended at any time, not just when a policy renews. This happened in 2020 when many states declared COVID-19 to be an occupational illness during the middle of a policy year. This shifted the costs from an employer health insurance plan with limits, to a Workers' Comp plan with unlimited coverage for healthcare expenses.

Looking ahead, long-duration COVID-19, defined as those who continue to show symptoms 30 days after they are infected, could be a significant source of cumulative trauma claims. According to the Journal of Occupational and Environmental Medicine, "approximately 5% to 8% of individuals who recover from an acute SARS-CoV-2 infection sustain a wide range of health effects affecting their ability to work."[6] And as the 2018 WCIRB report noted, cumulative trauma claim reporting is significantly slower than specific injury claim reporting.

HIGH HAZARD OCCUPATIONS AND MEGA CLAIMS

As is the case across Casualty insurance, some industries result in more Workers' Comp claims than others. In addition to construction and trucking, high-hazard occupations include logging and forestry; mining; non-artisan contractors, particularly those who work on streets and roads; and, staffing/farm labor.

At RPS, farm labor contractors are responsible for many of the MGA's large claims. Falls from ladders are the most significant issue, with inexperienced labor poised to increase that accident rate.

In Michigan, Clifford works with many SIGs in the high-hazard non-artisan contracting trades. In addition to falls, these industries also have larger claims involving trenching accidents and cave-ins.

It's not a surprise that occupations deemed high hazard make up a disproportionate number of the mega claims – Workers' Comp claims north of $3 million. These occupations also have high potential for occupational diseases as well as injuries.

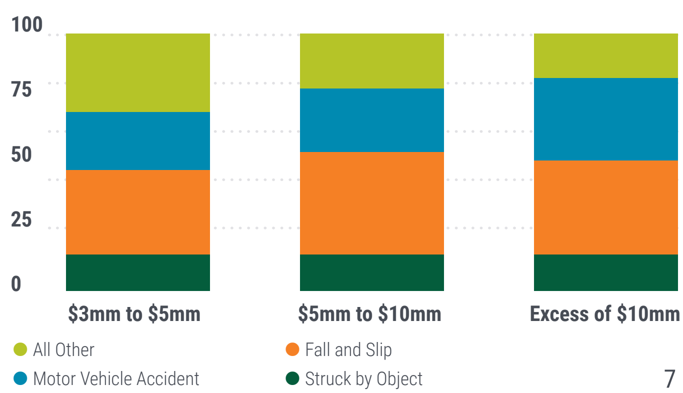
Medical costs are the primary driver of claims exceeding $3 million. It isn't uncommon for the compensation payments to be settled while the medical portion of the claim remains open.

And, as always, the state where the injury occurs plays a role.

"When you have a death claim, the survivor benefits depend on that particular state," Edwards explained. "So the claim outcome in Illinois will be different from the identical situation in California or even an adjacent state such as Iowa."

The sources of mega claims aren't radically different from those of more run-of-the-mill Workers' Comp claims.

SHARES OF MEGA CLAIMS BY CAUSE OF INJURY



THE PRIMARY MARKET

The structure of Workers' Comp depends on the state. Monopolistic or competitive? Independent state or an NCCI member?

From an insured's perspective, a significant divide is whether they can participate in the voluntary Workers' Comp market or must turn to the involuntary (assigned risk) market for their required coverage.

While in most states, the state fund governs the assigned risk, or involuntary, market; in others, the NCCI serves as the plan administrator. Regardless, this is never the market of first choice.

"This is no-frills coverage," said Ikari. "In California, the state fund doesn't offer loss control and lacks the claims-handling resources that you would find with a private insurer."

"Businesses that are forced into the assigned risk market have no choice about their coverage," Edwards added. "It's the market of last resort."

For businesses that operate in multiple states, the assigned risk market could mean having to deal with multiple state funds or a state fund and the NCCI, rather than dealing with a single carrier.

THE PROS AND CONS OF PLAN TYPES

In the voluntary market, guaranteed-cost plans continue to dominate for a number of reasons. Many businesses like the first-dollar coverage without any premium adjustments during the policy year.

For companies that can meet these financial requirements, a loss-sensitive plan can make sense, especially if they're working to get claims under control. Those insureds whose losses are better than expected can also benefit from premium credits.

However, sometimes the benefits of a loss-sensitive plan may be nonexistent.

"For a company with a good claims history that is considering a loss-sensitive plan as a way to save money, it still pays to do the math to see if the risk is worth it," advised Ikari. "Review the number of claims that came in under your proposed deductible and how much the total incurred was. You may find that the savings really isn't there."

One trend that Schneider is noticing is in the current premium rate environment, companies that are in a loss-sensitive plan, or even a captive, are moving back to the guaranteed-cost market. Whether this move proves to be successful remains to be seen.

A BELLWETHER STATE

With an economy larger than that of many countries, California represents nearly 25% of the Workers' Comp market.[7] Given the size of this market, Edwards and others look to it for indications of what lies ahead for the rest of the country.

In a year where the NCCI recommended double-digit rate reductions for the voluntary market in several states, the WCIRB had proposed an average 7.6% pure premium rate increase in California effective September 1, 2022. In mid-July, the state insurance commissioner rejected this proposal though he also didn't recommend a rate decrease, a sign that more challenging times may lay ahead.

"The excess market, which takes a longer view than the primary market—particularly guaranteed cost programs—has been raising rates for several years," noted Battagliese, who works with SIGs and self-insured employers. "This could be the year that we start seeing rate increases in the California market."

In May 2022, the WCIRB reported that the state's projected accident year combined ratio for 2021 is 112%. This compared to 101% for California Workers' Comp in 2020 and the NCCI's 2021 accident-year combined ratio of 102.

Another California trend worth watching is the emergence of insurtechs.

"One of the biggest sources of fresh capacity in the California market comes from insurtechs," Williams stated. "They are aggressive in their underwriting and willing to write just about any type of risk."

According to Williams, many of these new market entrants see themselves as tech companies, rather than insurers. As such, they are willing to be a low-cost underwriter of guaranteed-cost programs. Due to their lower expense ratio, they are less loss sensitive than traditional carriers that have been in this market for many years. Quoting, underwriting and binding are done with as little human intervention as possible. This makes for much faster turnaround, something that appeals to insureds.

SELF-INSURED GROUPS (SIGS) AND SELF-INSUREDS

Self-insurance is one of the most cost-effective program options in the primary market. The benefits of a self-insurance group (SIG) include more control over losses and the opportunity to share in the SIGs profits via dividends. SIGs also don't pay state premium tax or assigned risk market charges.

However, only 36 states allow SIGs. And forming a SIG can be a challenge, according to Clifford, who works with seven SIGs in Michigan with combined annualized premium of more than $60 million.

With an economy larger than that of many countries, California represents nearly 25% of the Workers' Comp market.

"It helps to have favorable market conditions, where carriers are increasing rates or moving out of the market. In addition to having a group of companies that are willing to pool their Workers' Comp premium, their premium needs to be at a sufficient level that self-insuring is a viable option," he explained. "The companies or organizations forming the SIG should also have minimal claims history so that they're starting with a clean pool."

Excess Workers' Comp, both aggregate and specific, covers incurred claim costs over specific limits. These add another layer of protection and help ensure the pool is financially sound in the event of adverse claim performance. The pool also pays for a third-party administrator, loss control and claims adjusting services.

Stability is another SIG benefit.

"SIGs have a long-term focus on meeting the Workers' Comp needs of a particular industry," said Clifford. "Over time, rates are more stable. Participants also don't need to worry about their carrier losing its appetite for their class of business."

PUBLIC ENTITIES

Cities, counties and school districts, as well as other public entities, turn to self-insurance for many of the same reasons that SIGs do, such as rate stability and more thorough claims handling. Olivares says that Workers' Comp self-insurance is also increasingly popular with hospitals and healthcare systems.

"In California, municipalities have a number of exposures, such as police shootings and wildfires, which would make it difficult to obtain Workers' Comp coverage in the voluntary market," observed Olivares.

A public entity needs to be approved by the state to become a qualified self-insured. An actuarial firm must determine their reserve funding. And like SIGs, qualified self-insureds need to carry a Workers' Comp excess policy.

The public entity/municipal government and health care segments have experienced the highest rate increases for Workers' Comp over the past couple of years. This is largely due to claims related to civil unrest and the pandemic. Olivares adds that the expansion of compensable diseases, such as lung cancer for a firefighter, has also influenced these rate increases.

The public entity/municipal government and healthcare segments have experienced the highest rate increases for Workers' Comp over the past couple of years, largely due to claims related to civil unrest and the pandemic.

ACCESS AND EXPERIENCE

Given the attributes that differentiate the Workers' Comp market from other casualty markets, often retail brokers can best serve their clients by working with a specialist who is focused on this market. That professional can help a retail broker weigh the pros and cons of the various program options and help present them to a client.

Schneider explains the benefits of working with an MGA that's a Workers' Comp specialist.

"We have a menu of carriers that the broker can access with one submission," she explained. "That means the broker doesn't have to blanket the market to ensure that their client receives a competitive quote."

Schneider adds that RPS will often work with brokers to create a customized Workers' Comp program that a broker can then market to a specific class of business.

A broker trying to start a SIG will also find it challenging without the right expertise.

"Many of the agents that I work with will approach us about starting a group," said Clifford. "They have lots of ideas but often they don't translate into a group fund."

The focus on a single line of coverage also means that a wholesaler has access to underwriters that the retail brokers lack. Not only is a wholesaler often able to obtain a more competitive quote, often they are the reason why a retail broker even obtains a quote.

Wholesalers are also experienced in dealing with "Difficult risks that have issues."

Many of the Workers' Comp placements that Edwards and his team work on are trying to avoid the involuntary market.

"We're like soccer goalies, trying to keep the ball in play on the field and out of the net—the field representing the specialty comp/voluntary space and the net representing the assigned risk/involuntary market space," Edwards said.

An experienced wholesaler can sometimes make a case for the insured when the submission is denied.

"It's important to understand why the submission was turned down," noted Ikari. "In situations where it's because of a large claim that was outside the insured's scope of work, I can go back to the underwriter and make a case for them. In one situation a $500,000 back injury claim resulted from an employee slipping on a slice of pizza in the back of a truck."

Carrier relationships and market expertise are especially critical in the excess market.

"While retail brokers have access to the same market that I do, my level of experience and carrier relationships means that I can create a more attractive program for their client," Olivares stated.

With a small group of carriers in the excess Workers' Comp market, Olivares believes that it's important to market accounts on renewal.

"It's the best way to ensure a competitive and comprehensive program," he explained.

A MARKET APPROACHING CROSSROADS

As an extremely long-tail market, it can be challenging to predict what lies ahead for Workers' Comp. Because claims can be open for years, it's difficult to reflect their true cost in the near-term market. For example, while initial Workers' Comp claims stemming from COVID-19 weren't as catastrophic as predicted, long-duration COVID-19 could turn out differently.

On the surface, the Workers' Comp market continues to move along the same smooth and profitable path that it has enjoyed for the past eight years—and longer in certain states. Yet there are subtle signs, such as rising accident year combined ratios, which signal that this cycle could be coming to an end.

Another cloud over the market is the difficulty in taming inflation, which at mid-2022 stands at a 40-year high. Inflation makes it more expensive for both carriers and insureds to do business. It also has an impact on both payrolls and medical costs.

Retail agents also need to begin to think about how they will compete with insurtechs. The expertise offered by Workers' Comp specialists will help them compete for underwriting terms and binding speed.

Given the attributes that differentiate the Workers' Comp market from other Casualty markets, carrier relationships and market expertise are especially critical.

CONTRIBUTORS

Patrick Edwards, Area Senior Vice President, Workers' Compensation Practice Leader

L.J. Battagliese, Area President

Joe Clifford, Area President

Amanda N. Ikari, Area Senior Vice President

Rafael Olivares, Area Vice President

Dayna Schneider, Area Senior Vice President of Underwriting

Mark Williams, Executive Vice President of Business Development

ABOUT RISK PLACEMENT SERVICES

Risk Placement Services (RPS) is one of the nation's largest specialty insurance product distributors, offering valuable solutions in wholesale brokerage, binding authority, programs and standard lines, plus specialized auto through its Pronto Insurance brand. Headquartered in Rolling Meadows, Illinois, RPS has more than 80 offices nationwide.

For more information, visit RPSins.com.

[1]"An Early Look at Workers' Compensation Results," NCCI Research Brief, January 14, 2021, accessed June 2022.

[2]"The Role of Employee Tenure in Construction Industries," May 2019, accessed June 16, 2022.

[3]"Labor Force Participation Rates for Workers Age 75 and Older," BLS, May 29, 2019, accessed June 17, 2022.

[4]"Latest Trends in Worker Demographics," NCCI Research Brief, May 2021, accessed June 17, 2022.

[5]"The World of Cumulative Trauma Claims, WCIRB, 2018, p. 34.

[6]"Attributes of Long-Duration COVID-19 Workers' Compensation Claims," Journal of Occupational and Environmental Medicine, accessed June 17, 2022.

[7]"Workers' Comp Market Will Turn…Eventually," Insurance Business, February 10, 2020, accessed July 5, 2022.

RPS42989 0922