Approved: 2-3-93
Date

MINUTES OF THE HOUSE COMMITTEE ON LABOR AND INDUSTRY.

The meeting was called to order by Chairman David Heinemann at 9:09 a.m. on January 14, 1993, in Room 526-S of the Capitol.

All members were present except: Representative Cornfield (excused)
Representative Garner (excused)

Committee staff present: Jerry Ann Donaldson, Legislative Research Department
Kay Scarlett, Committee Secretary

Conferees appearing before the committee:

Bill Dempsey, Supervising Attorney, Kansas Insurance Department
Ray Rathert, Fire and Casualty Supervisor, Kansas Insurance Department

Others attending: See attached list

Bill Dempsey, Supervising Attorney, Kansas Workers Compensation Fund, Kansas Insurance Department, gave an overview of the Workers Compensation Fund and how it operates. The main purpose of the Workers Compensation Fund is to encourage the hiring and retention of handicapped employees by relieving employers of all or a portion of the liability of the worker's compensation claims. (Attachment 1)

Mr. Dempsey offered a piece of legislation as a result of the Legislative Post Audit. Chairman Heinemann responded that we would be accepting bill requests at a later date.

Mr. Ray Rathert, Fire and Casualty Supervisor for the Kansas Insurance Department, presented some basic information concerning workers compensation insurance rates. Kansas statutes require that workers compensation rates and rating plans be submitted to the Insurance Commissioner's office for approval prior to use. Kansas insurance statutes require that the workers compensation rates be reasonable, adequate, and not unfairly discriminatory. (Attachment 2)

Chairman Heinemann asked Mr. Rathert to return tomorrow to continue his presentation.

The meeting adjourned at 10:00 a.m. The next meeting is scheduled for January 15, 1993.

GUEST LIST

COMMITTEE: HOUSE LABOR AND INDUSTRY DATE: 1-14-93

NAME	ADDRESS	COMPANY/ORGANIZATION
Jim Allen	Topeka	PRM
Tom Slattery	Top	AGC of Ks
Richard Mason	"	KTLA
Art Brown	Topeka	KS. Imp. Dealers Assn
Rich McKee	"	KS Livestock Assoc.
Bill Curtis	Topeka	Ks Assoc. of School Bds
[illegible]	Topeka	Nat'l Electrical Contractors
CARL DAUGHERTY	COLUMBUS	EMPIRE DISTRICT ELEC
SHELBY SMITH	Wichita	EL-II
Billy Newman	Topeka	D of A.
Hal Hudson	~~NFIB / KS~~ Topeka	NFIB Kansas
ALAN COBB	Wichita	KS Assoc. for Small Business
Harry D. Helser	"	Ks AFL-CIO
Jim DeHoff	Lawrence	"
Roland Smith	Wichita	WIBA
Joe Furjanic	Topeka	KCA
Terry Leatherman	Topeka	KCCI
BRAD SMOOT	"	AIA
Bill Wempe	"	Ks. Ins. Dept.
KAY RATHERT	"	" " "
GEORGE WELCH	"	D of A
Marla Rutter	"	"
Wayne Maichel	Top	Ks. AFL-CIO

AN OVERVIEW OF THE WORKERS COMPENSATION FUND
AND HOW IT OPERATES
TESTIMONY PRESENTED TO THE KANSAS HOUSE
LABOR AND INDUSTRY COMMITTEE

BILL DEMPSEY, SUPERVISING ATTORNEY
KANSAS WORKERS COMPENSATION FUND
KANSAS INSURANCE DEPARTMENT
RON TODD
COMMISSIONER OF INSURANCE

I. HISTORICAL ANALYSIS

Since 1945, the Kansas legislature has been concerned with the employment of "handicapped" employees under the workers' compensation laws. In 1945, the "Second Injury Fund", the forerunner of the Workers' Compensation Fund was created. The statute was designed to encourage hiring "handicapped employees" by relieving the employer of liability for compensation on second injuries. However, the statute severely limited the availability of money from the Second Injury Fund. To be entitled to reimbursement, the employer was required to show:

(1) previous impairment of an eye, arm, hand or foot;

(2) a second injury to the same or different member of the body;

(3) resulting permanent total disability.

Only "specific members" of the body were included within the statute and, therefore, back injuries, heart attacks and mental disorders did not come within the coverage of the statute. Obviously, very few cases resulted in liability against the Second Injury Fund.

House Labor and Industry
Attachment 1
1-14-93

The legislature liberalized the statute in 1961 allowing for contribution by the Second Injury Fund where there was only an increase in impairment, not merely in cases where there was permanent total disability. Further, contribution was allowed for spinal, back, heart and emotional disorders. This statute was the predecessor of the modern Kansas Workers' Compensation Fund.

II. CREATION OF THE WORKERS' COMPENSATION FUND

Since the creation of the Second Injury Fund which was followed by the Kansas Workers' Compensation Fund (the "Fund"), the main purpose of the statute has been to encourage the hiring and retention of handicapped employees by relieving employers of all or a portion of the liability for the worker's compensation claim. The fund is authorized by K.S.A. 44-566(a) which provides for administration by the commissioner of insurance, receipt of revenue, assessments against insurance companies and self-insurers, and administration of the Fund.

The commissioner of insurance who is responsible for the administration of the Fund, oversees the receipt of revenue which originates from essentially two sources:

(1) K.S.A. 44-566a (b), assessments against insurance carriers and self insurers and group-funded workers' compensation pools.

(2) K.S.A. 44-570, non-dependent death case payments by employers to the Fund. K.S.A.

44-566a(b) formerly provided for funding via a four million dollar general fund entitlement until 1991. This money has been "loaned" to the Fund in July of each year since 1991 and repaid from assessment revenue in October of each year.

1. THE EMPLOYER KNOWINGLY HIRES OR RETAINS A HANDICAPPED EMPLOYEE - K.S.A. 44-567

The Fund may be required to relieve an employer of liability, either wholly or in part, when the employer hired or retained a handicapped employee with knowledge of the pre-existing condition and the employee suffers an injury resulting in disability contributed to or caused by the pre-existing impairment.

2. KNOWING MISREPRESENTATION OF A HANDICAPPED

CONDITION BY THE EMPLOYEE - K.S.A. 44-567(c)

The Fund may be required to relieve an employer of liability, either wholly or in part, if the employee knowingly misrepresented his health with regard to pre-existing impairments, disability, accidents, injury and diseases or facts regarding his physical condition.

3. INSOLVENT EMPLOYER - K.S.A. 44-532(a)

The Fund may be required to pay compensation, both medical and disability, to an injured employee under the following conditions:

(a) the employer has no insurance, and

(b) the employer is financially unable to pay, or

(c) the employer cannot be located.

4. COMPENSATION PAID UNDER A PRELIMINARY AWARD - K.S.A. 44-534 (a)

The Fund may be required to reimburse employers who have paid compensation, either voluntarily or pursuant to a preliminary award, that is later overturned or reduced.

5. COMPENSATION PAID PURSUANT TO A FINAL AWARD - K.S.A. 44-556(d)

The Fund may be required to reimburse employers who have paid compensation under a formal award which is later overturned or reduced on appeal to the district court, court of appeals or supreme court.

6. REIMBURSEMENT OF COMPENSATION PAID AN EMPLOYEE DURING AN APPEAL - K.S.A. 44-556(d)

The Fund may bre required to reimburse employers who have paid compensation pending appeal and after the appeal it is determined that the amount paid exceeded actual liability.

IV. RECOGNIZING POTENTIAL FOR CONTRIBUTION

BY THE FUND UNDER K.S.A. 44-567

By far, most cases against the Fund arise in cases where the employer knowingly hired or retained a handicapped employee.

1. BURDEN OF PROOF

The burden of proof is always squarely upon the employer to prove every element to establish Fund liability.

> In order to be relieved of liability under this section, the employer must prove either the employer had knowledge of the pre-existing impairment at the time the employer employed the handicapped employee or the employer retained the handicapped employee in employment after acquiring such knowledge.

K.S.A. 44-567(b).

Johnson v. Kansas Neurological Institute, 11 Kan.App.2d 161, 716 P.2d 598 (1986). The burden of proof required to be established by the employer is set forth in K.S.A. 44-508(g).

> "Burden of proof" means the burden of a party to persuade the trier of facts by a preponderance of the credible evidence that such party's position on an issue is more probably true than not true on the basis of the whole record.

2. NECESSARY ELEMENTS OF PROOF TO ESTABLISH FUND LIABILITY

A. HANDICAPPED EMPLOYEE

The employer must establish that the injured claimant was a "handicapped employee" to be entitled to contribution from the Fund, pursuant to K.S.A. 44-567.

A "handicapped employee" is defined by K.S.A. 44-566(b) as follows:

"Handicapped employee" means one afflicted with or subject to any physical or mental impairment, or both, whether congenital or due to an injury or disease of such character the impairment constitutes a handicap in obtaining employment or would constitute a handicap in obtaining reemployment if the employee should become unemployed and the handicap is due to any of the following diseases or conditions:

(1) Epilepsy;

(2) Diabetes;

(3) Cardiac disease;

(4) Arthritis;

(5) Amputated foot, leg, arm or hand;

(6) Loss of sight of one or both eyes or a partial loss of vision of more than 75% bilaterally;

(7) Residual disability from poliomyelitis;

(8) Cerebral palsy;

(9) Multiple sclerosis;

(10) Parkinson's disease;

(11) Cerebral vascular accident;

(12) Tuberculosis;

(13) Silicosis or asbestosis;

(14) Psychoneurotic or mental disease or disorder established by medical opinion or diagnosis;

(15) Loss of or partial loss of the use of any member of the body;

(16) Any physical deformity or abnormality;

(17) An other physical impairment, disorder or disease, physical or mental, which is established as constituting a handicap in obtaining or in retaining employment.

This list of statutory recognized impairments contained within K.S.A. 44-566(b) does not include spinal and back conditions, nor does it include carpal tunnel syndrome. However, the "catch all" category found in K.S.A.. 44-566(b)(17) has been interpreted by case law to include various back and spinal conditions as handicaps under the statute. Spencer v. Daniel Construction Co., 4 Kan.App.2d 613, 609 P.2d 687 (1980). Arguably, carpal tunnel syndrome would fit within the definition of the "catch all" category as well.

An employee is not a "handicapped employee" if he or she is not at a disadvantage in obtaining or retaining employment because of the impairment. Denton v. Sunflower Electric Cooperative, 12 Kan.App.2d 262, 740 P.2d 98 (1987) aff'd. 242 Kan. 430, 748 P.2d 740 (1988). The court in Denton went on to say that the word "impairment" as used in the phrase "physical or mental impairment" as contained in K.S.A. 44-566(b) and 44-567 connoted limitation of function. The court noted that to be a "handicapped employee", the employee must have functional limitations putting him or her at a disadvantage in obtaining employment or re-employment.

Whether or not an employee is "handicapped" is a question of fact to be decided on a case by case basis. Hinton v. S.S. Kresge Co., 3 Kan.App.2d 29, 592, P.2d 471 (1978).

The employee need not be denied employment because of his impairment to establish that he or she is a handicapped employee. Grounds v. Triple J Construction Co., 4 Kan.App.2d 325 606 P.2d 484 (1980). Nor does a handicap need to be demonstrably disabling. Oates v. Post & Danley Truck Lines, 3 Kan.App.2d 337, 594 P.2d 684 (1979); Carter v. Kansas Gas & Electric Co., 5 Kan.App.2d 602, 621 P.2d 448 (1980). Further, there is no requirement that the employee consider himself handicapped in order to establish a "handicap" under the statute. Oates v. Post & Danley Truck Line, 3 Kan.App.2d 337, 594 P.2d 684 (1979).

B. KNOWLEDGE OF HANDICAP

In order for the employer to be relieved of liability, either wholly or in part, the employer must hire or retain the handicapped employee after acquiring knowledge of the handicap. K.S.A. 44-567(b) provides:

> "In order to be relieved of liability under this section, the employer must prove either the employer had knowledge of the pre-existing impairment at the time the employer employed the handicapped employee or the employer retained the handicapped employee in employment after acquiring such knowledge."

Knowledge by the employer may be established by one of two ways:

(1) filing of a Form 88, which creates a rebuttable presumption of knowledge of the prior handicap. K.S.A. 44-567(b);

(2) By any other evidence sufficient to maintain the employer's burden of proof. K.S.A. 44-567(b).

Obviously the Form 88 filing is the preferred method of establishing proof of knowledge of hiring or retaining a handicapped employe.. The Form 88 is a form available from the director. The form requires the employer to list the employee's name, social security number and descriptions of the impairment as contained in the list in K.S.A. 44-566. The presumption of knowledge created when a form 88 is

filed can be rebutted where the employer merely lists reported injuries on the form. Knowledge of a prior injury does not constitute knowledge of a prior handicap. Johnson v. Kansas Neurological Institute, 240 Kan. 123, 722 P.2d 912 (1986); Carter v. Kansas Gas & Electric Co., 5 Kan.App.2d 602, 621 P.2d 448 (1980).

In Johnson, the claimant suffered a prior injury approximately seven and one-half (7-1/2) years prior to the date of the injury for which she sought compensation. The claimant had returned to her same job without restriction and had exhibited no symptoms prior to the second injury. The court held that the facts did not show a reservation in the mind of the employer in deciding to hire or retain the claimant.

While the reservation concept has been overruled by Denton v. Sunflower Electric Cooperative, 12 Kan.App.2d 262, 740 P.2d 98 (1987) aff'd. 242 Kan. 430, 748 P.2d 420 (1988), the logic used by the Johnson case is still sound. The evidence in Johnson certainly did not support a finding that the claimant had any functional limitation putting her at a disadvantage in obtaining or retaining employment. The most the employer had was knowledge of an injury, which, without more, is insufficient to meet their burden of proof.

Keeping in mind the basic purpose of the Fund, which is to encourage hiring or retention of handicapped employees, shifting all or a portion of the liability to the Fund in Johnson would not further the purpose of the statute.

In Carter v. Kansas Gas and Electric Co., 5 Kan.App.2d 602, 621 P.2d 448, (1980), the respondent asserted it had knowledge of a pre-existing impairment based on prior injuries in 1969 and 1974. In 1975, the claimant suffered a ruptured disc. The only evidence of the respondent's knowledge were medical records that showed the claimant had suffered muscle spasms due to trauma in 1969, and an unknown diagnosis, but a return to full duty in 1974. The court held that it could not be presumed that a single trauma back injury is likely to have recurring effects, particularly when the employee is returned to full duties. Therefore, knowledge of an injury will not in and of itself establish knowledge of a handicap.

An employer should therefore state the specific nature of the handicap such as chronic low back pain or chronic neck pain and avoid merely listing non specific injuries such as neck strain on the Form 88. However, it is not necessary that the employer describe in exact medical terminology the nature of the

impairment, so long as the description provided informs the director that the employee is handicapped and the nature of the handicap. Leiker v. Manor House, Inc., 203 Kan. 906, 457 P.2d 107 (1969).

If a Form 88 is not filed by the employer, the employer may still be able to establish knowledge of a handicap based on other evidence as long as the evidence meets the employer's burden of proof to establish knowledge. Examples of "other evidence" may include: testimony from the claimant that the employer was aware of his pre-existing impairment; information supplied by the employee on an employment application; information obtained from a pre-employment physical after a conditional offer of employment has been extended; testimony from the employer, including foreman and supervisors that were aware of the claimant's prior physical condition and prior workers' compensation claims which have been resolved by trial or settlement with the employee returning to his previous employment.

A sampling of cases where knowledge was established without the use of a Form 88 is helpful in determining the burden of proof necessary to establish knowledge under K.S.A. 44-567(a) which provides "any other evidence sufficient" may be used to establish knowledge.

In Oates v. Post and Danley Truck Lines, 3 Kan.App.2d 337, 594 P.2d 684 (1979), the court determined the evidence necessary to establish knowledge. In Oates, the claimant suffered a cerebral vascular accident in September 1975. The claimant applied for work with the respondent/employer and disclosed the cerebral vascular accident to the employer. The employer questioned the claimant about the condition and his ability to perform the work. The court found that the claimant was a handicapped employee and further found the employer had knowledge of the handicap based on the disclosure at the time of hiring.

In Grounds v. Triple J Construction Co., 4 Kan.App.2d 325, 606 P.2d 484 (1980), rev.denied 227 Kan. 927 (1980), the court found the employer had knowledge of a handicap based on the employer being personally aware the claimant had back trouble prior to the time the employer hired him. The employer was also aware that the claimant had previously had a workers' compensation claim in 1971 and that the claimant was required to wear a back brace.

In Spencer v. Daniel Construction Co., 4 Kan.App.2d 613, 609 P.2d 687 (1980), the court held that the employer had knowledge of a handicap based on a prior injury in July 1975. The claimant returned to work after the July 1975

injury and was advised by his supervisor that he should take it easy and not to bend, stoop or lift. The court affirmed an apportionment against the Fund for a second injury on August 22, 1975 and stated:

> "Here, claimant's employer know that he had injured his back. Claimant worked regularly with heavy pipe and was required by the very nature of his work to bend stoop and lift heavy objects. He had the classic symptoms of a herniated disc; i.e., low back pain, with pain in his right hip radiating down his right leg. He was under medical treatment and missed three nonconsecutive days' work during the three-week period due to the injury. He was advised by his supervisor not to bend, stoop or lift and to do only light work such as he could. It is unrealistic to say that a worker who does heavy construction work and complains of these symptoms does not have a physical impairment that constitutes a handicap in obtaining or in retaining employment. If he were tell a prospective employer in the heavy construction business about his symptoms, he would not be hired, and his own supervisor warned claimant that he might be terminated if he reported his injury through proper channels."

Id at 617.

In Hampton v. Professional Security Co., 5 Kan.App.2d 39, 611 P.2d 173 (1980), the court found knowledge again based on a pre-employment disclosure and questioning by the employer as to the employee's condition and ability to perform the work.

In Denton v. Sunflower Electric Cooperative, 12 Kan.App.2d 262, 740 P.2d 98 (1987) aff'd 242 Kan. 430, 748 P.2d 420 (1988), the court found that the supervisor's knowledge as to missed work because of back problems, and continuing back problems for approximately ten years was sufficient to establish knowlege of a pre-existing handicap.

"Mental reservation" on the part of the employer is not an essential element to establish Fund liability. Denton v. Sunflower Electric Cooperative, 242 Kan. 430, 748 P.2d 420 (1988).

C. CLAIMANT'S MISREPRESENTATION OR CONCEALMENT OF HIS PHYSICAL CONDITION OR HEALTH HISTORY

UNDER K.S.A. 44-567(c)

When the employee misrepresents or conceals his physical condition at the time of hiring, the employer will be presumed to have knowledge of the employee's pre-existing condition, if in connection with the hiring or retention, the employee knowingly misrepresents the existence of a handicap or other facts related to his physical condition. The misrepresentation statute under K.S.A. 44-567(c) operates as an alternative to knowledge to enable the employer to obtain reimbursement from the Fund and provides as follows:

> (c) Knowledge of the employee's pre-existing impairment or handicap at the time the employer employs or retains the employee in employment shall be presumed conclusively if the employee, in connection with an application for employment or an employment medical examination or otherwise in connection with obtaining or retaining employment with the employer, knowingly: (1) misrepresents that such employee does not have such an impairment or handicap; (2) misrepresents that such employee has not had any previous accidents; (3) misrepresents that such employee has not previously been disabled or compensated in damages or otherwise because of any prior accident, injury or disease; (4) misrepresents that such employee has not had any employment terminated or suspended because of any prior accident, injury or disease; (5) misrepresents that such employee does not have any mental, emotional or physical impairment, disability , condition, disease or infirmity; or (6) misrepresents or conceals any facts or information which are reasonably related to the employee's claim for compensation.

Case law is clear that the employee's misrepresentation must be knowing and not merely negligent. It is inherent in the term, knowingly, that some degree of awareness on the part of the employee be present. Collins v. Cherry Manor Convalescent Center, 7 Kan.App.2d 270, 640 P.2d 875 (1982).

In Collins, the court held that "knowing" as used in 44-567(c) refers to the claimant's state of mind. The claimant responded negatively to a question on the job application form asking whether she had a "physical disability". The court

held that the claimant's capacity to understand the question, her actual understanding and her belief in answering were all relevant to whether a knowing misrepresentation was made, and remanded the case.

As with all other elements necessary to establish Fund liability, the employer has the burden of proof in establishing a knowing misrepresentation.

D. CONTRIBUTION OR CAUSATION OF THE "HANDICAP" TO THE PRESENT INJURY OR DISABILITY - K.S.A. 44-567

The final element the employer must show is that the pre-existing impairment either caused or contributed to the present injury or disability of the claimant. The "but for" test is set forth in K.S.A. 44-567(a)(1) which provides as follows:

> "Whenever a handicapped employee is injured or is disabled or dies as a result of an injury and the director awards compensation therefor and finds the injury, disability or the death resulting therefrom probably or most likely would not have occurred but for the preexisting physical or mental impairment of the handicapped employee, all compensation and benefits payable because of the injury, disability or death shall be paid from the workers' compensation fund".

The test is whether the injury or resulting disability, not the "accident", probably would not have occurred "but for" the pre-existing handicap. Barke v. Archer Daniels Midland Co., 223 Kan. 313, 573 P.2d 1025 (1978). In Barke, the court stated:

> The new statutory test is whether the change in the physical structure of the workman's body (the injury) or the resulting impairment of his ability to perform work (the disability) "probably or most likely would not have occurred" but for the pre-existing physical or mental impairment of the handicapped employee.

Id at 318.

The "but for" rule requires that the pre-existing impairment be the proximated cause of the injury or disability. There is no requirement that medical evidence be used to establish the "but for" element under K.S.A. 44-567(a)(1).

E. CONTRIBUTION BY PRIOR IMPAIRMENT TO RESULTING DISABILITY UNDER K.S.A. 44-567(a)(2)

The test for contribution is set out in K.S.A. 44-567(a)(2) which provides as follows:

> "Subject to the other provisions of the workers' compensation act, whenever a handicapped employee is injured or is disabled or dies as a result of an injury and the director finds the injury probably or most likely would have been sustained of suffered without regard to the employees pre-existing physical or mental impairment but the resulting disability or death was contributed to by the preexisting impairment, the director shall determine in a manner which is equitable and reasonable the amount of disability and proportion of the cost of award which is attributable to the employee's pre-existing physical or mental impairment, and the amount so found shall be paid from the workers' compensation fund."

The award of contribution need not be based on medial evidence. K.S.A. 44-567 (a)(2). If the handicapped employee's impairment contributes causally to the injury or disability, the Fund may be liable for a portion of the compensation and benefits awarded to the claimant. The apportionment of the award is based on the amount of disability attributable solely to the second injury and the extent that the pre-existing impairment contributes to the second injury. Brozek v. Lincoln County Highway Department, 10 Kan.App.2d 319, 698 P.2d 392 (1985). The award of contribution must be equitable and reasonable and based upon all the evidence.

In cases where apportionment of the award is appropriate, the Fund is entitled to a credit under K.S.A. 44-510a for compensation paid or to be paid to the claimant on a prior accident. The credit statute, sometimes referred to as the anti-pyramiding statute prevents the claimant from receiving double compensation

for the same permanent disability. Spencer v. Daniel Construction Co., 4 Kan.App.2d 613, 609 P.2d 687 (1980).

MEMORANDUM

TO: House Labor and Industry Committee

FROM: Kansas Insurance Department

SUBJECT: Workers' Compensation Insurance Ratemaking

DATE: January 13, 1993

Good morning my name is Ray Rathert, I am the Fire and Casualty Supervisor for the Kansas Insurance Department. Insurance Commissioner Ron Todd has requested that I appear today and present you with some basic information concerning workers' compensation insurance rates.

Kansas insurance statutes require that workers' compensation rates and rating plans be submitted to the insurance commissioner's office for approval prior to use. We are a "prior approval" state meaning that every rate, rating plan, minimum premium and every classification proposed by an insurance company must be submitted for our review and approval before it can be placed into effect and used by an insurance company in our state. The statutes provide that an insurance company may do this individually or they may engage the services of a rating organization to function on their behalf. In Kansas, every carrier that is writing workers' compensation is a member of or a subscriber to the National Council on Compensation Insurance. The National Council on Compensation Insurance headquartered in Boco Raton, Florida, is a voluntary, non-profit, statistical and ratemaking organization. It is owned and supported by the insurance companies writing workers' compensation throughout the country. The NCCI's primary function is to prepare and to administer the submission of rate filings, rating plans and the system for writing workers' compensation insurance in approximately 32 states. The NCCI provides assistance to about one-half of the remaining states.

Approximately 400 insurance companies are licensed to write workers' compensation in Kansas but only 230 companies actually wrote premium which totaled over 340 million dollars in Kansas during 1991.

Kansas insurance statutes require that the workers' compensation rates be reasonable, adequate and not unfairly discriminatory. These are the statutory standards imposed by the Insurance Code that must be satisfied in our review of rates and rating plans. We refer to workers' compensation insurance as a statutory coverage simply because all the benefits contemplated by the policy are contained within the workers' compensation insurance laws. In brief, the coverage provides various benefits resulting from work related injury or illness.

From a historical perspective, the workers' compensation law was one of the first "No Fault" statutes in the state of Kansas. The law and the policy assures payment will be made to an injured worker without regard to who or what may have been at fault in causing the work related injury or illness. On the other hand, in exchange for the statutorily guaranteed compensation, injured workers relinquish their right to file a

House Labor and Industry
Attachment 2
1-14-93

damage suit against their employer. By making the workers' compensation benefits the exclusive remedy for on the job injuries and accidents, employers are provided a protection from being financially ruined by a single claim. In return for a known expense which we refer to as premium, the insured employer receives insurance to cover the cost of the large unknown, unbudgeted accident.

The workers' compensation insurance benefit system is pre-funded. This means that the premiums from policies written during a particular calendar year are intended to meet all future claim payments made under these policies. An insurance company writing a workers' compensation policy today is at extreme risk because there is simply no guarantee that the premium collected on the current policy will be sufficient to meet the benefit costs and operating costs in the future. There is no opportunity for the company to recoup deficit amounts on these current policies when the total losses and expenses exceed the premium which has been received.

In Kansas, the amount of premium written is considered adequate or sufficient to determine overall rate needs. Therefore, as we review the rate filing submitted by the NCCI each year, we are principally reviewing and analyzing the premiums and losses of policies issued in our state.

The principal financial data used in considering a Kansas rate filing is the comparison of premium to losses and expenses from all policies whose coverage began in a particular calendar year. This is called policy year data. A second comparison is made of the calendar year premium to the losses and expenses which occurred during a particular year. This is called calendar-accident year data. Currently, the NCCI utilizes two years of data in attempting to project the rate needs for the coming year. They utilize very sophisticated actuarial techniques to make their rate determinations in each filing that is proposed. One technique used is to adjust the premium for the years under review to make certain that the analysis allows for any rate changes that have been placed into effect since the premium was written. The losses paid are likewise adjusted to allow for statutory law changes that have been placed into effect. They also include factors to adjust losses to reflect the current costs.

The concept of premium adequacy is for the premium collected at the current rates to equal the losses expected to be paid under the current statutory benefit provisions. The current rate filing in effect in Kansas anticipates a target cost ratio of 73%. This means that the insurance companies anticipate paying losses and loss adjustment expenses equal to $.73 out of every dollar of premium that is received. The

NCCI develops their basic indicated rate need by dividing the target cost ratio into the actual cost ratio. In the current filing, the target cost ratio is .730 whereas the average cost ratio was .8635. The mathematics of the indicated change based only upon experience (premium and losses) was +18.3%. This is arrived at by merely dividing .8635 by .730. The indicated rate change based upon experience is further modified by the indicated change in the trend factor. Trend reflects the direction and amount of the increases or decreases in claims costs based on recent history to project the "trend" of losses into the future period in which the rates will be used. The current rate filing was modified by +7.5% increase to reflect the change in overall trend in our state. There is also a change in the level of expenses anticipated in the rate filing. In 1992 this was +0.4%. The NCCI also considered the premium change necessary to allow for the change in the benefit provisions in 1992. This amounted to +0.4%. After calculating the modifications necessary based upon the actual experience, the change in trend factor, the change in expenses and the change in benefit provisions, they determined a rate need of +28.2%. This was further modified by the effect of the change in the assessment for the workers' compensation fund and the director's office that added another +2.5%. The bottom line of the requested rate change in the 1992 filing amounted to a 31.4% increase; however, only a 21.7% increase was approved by Commissioner Todd.

In addition to the insurance department's review, the Commissioner submitted the entire 1992 NCCI rate filing to an independent actuary for review. The actuary's analysis revealed slightly different needs than the NCCI based upon the fact that, in his opinion, the fixed expenses of the insurance companies did not increase at the same rate as the indicated change based upon the loss history developed by companies. In view of that, the actuary recommended and the Commissioner subsequently approved an overall rate change of only 21.7%. Only time will tell whether the Commissioner's adjustment to the last rate proposal was proper, but it was based upon the recommendations of an independent actuary who is skilled in the review of NCCI rate filings.

I am leaving with you today a publication of the NCCI entitled Ratemaking...The Pricing of Workers' Compensation Insurance. We reviewed this document and believe it to be a very good overview of the ratemaking process of workers' compensation coverage.

I would also like to point out that the NCCI has been the subject of a thorough examination by actuaries within the National Association of Insurance Commissioners as well as the consulting firm of Milliman and Robertson which had Arthur Anderson as a subcontractor to assist them in the project. This was done principally because there had been a long standing suspicion by regulators of the data collection and data quality

used by NCCI in its rate filings. The National Association of Insurance Commissioners was also concerned with the fact that the complex nature of workers' compensation filings, combined with the fact that the NCCI is the only ratemaking organization in most states, created a situation where there was certainly limited incentives to develop techniques that might result in lower rates. The states of Florida, Iowa, Nebraska and Oregon were appointed by the NAIC to conduct the examination of the NCCI. These states then selected the firm of Milliman and Robertson to actually conduct the examination with oversight from this group.

The major findings of the group were, generally, that the NCCI was accurately handling the information received from their companies. They also found that the NCCI policies on data quality needed clarification and stronger enforcement. A third finding was that the NCCI system for ratemaking and experience rating used a large amount of hard copy input and had little validation at the time of data capture. In order to compensate for the system's deficiencies, the NCCI currently performs extensive manual intervention. Although the initial examination is complete, there are several areas that remain unresolved. Although the basic rating techniques were currently found to be valid, the NAIC will continue to review and monitor the NCCI ratemaking procedures during the next several years.

I will be happy to answer any specific question that any member of this committee might have. Thank you very much.

Respectfully submitted,

_____
Raymond E. Rathert

RER:crf
1705.A