Approved: 2-19-93
Date

MINUTES OF THE HOUSE COMMITTEE ON LABOR AND INDUSTRY.

The meeting was called to order by Vice Chairman Al Lane at 9:03 a.m. on February 10, 1993, in Room 526-S of the Capitol.

All members were present except: Representative Heinemann (excused)
Representative Carmody (excused)

Committee staff present: Jerry Ann Donaldson, Legislative Research Department
Jim Wilson, Revisor of Statutes
Kay Scarlett, Committee Secretary

Conferees appearing before the committee:

Richard Mason, Kansas Trial Lawyers Association
Pat Nichols, Kansas Trial Lawyers Association
John Alworth, San Antonio, Texas

Others attending: See attached list

Copies of fiscal notes for HB 2116 and HB 2120 were distributed. (Attachments 1 and 2, respectively)

Continuation of Hearing on HB 2191 - Workers compensation, ombudsman program, benefit review conferences.

Richard Mason, Kansas Trial Lawyers Association, introduced Pat Nichols. Pat Nichols testified that the Kansas Trial Lawyers Association is in complete opposition to HB 2191. They believe it is unfair and completely without justification that the legislature should even consider creating a new component in the workers compensation system that by law precludes claimants from having the legal right to the presence of counsel when their rights are being decided. Specific provisions of the bill they find objectionable are addressed in their attached testimony. (Attachment 3)

Mr. Nichols also attached a copy of a letter from George W. Turner, Merlino & Schofield, Inc., Consulting Actuaries, of Atlanta, Georgia, regarding his review of the Kansas Workers Compensation Closed Claim Study at the request of the Kansas Trial Lawyers Association. (Attachment 4)

Richard Mason then introduced John Alworth, an attorney from San Antonio, Texas, who has done a lot of work in the area of workers compensation and appeared as an opponent to HB 2191. He discussed the benefit review conference and ombudsman program in Texas. In Texas attorneys are allowed to participate in benefit review conferences.

The meeting adjourned at 9:57 a.m. The next meeting is scheduled for February 11, 1993, at 8:00 a.m. in Room 313-S.

GUEST LIST

COMMITTEE: HOUSE LABOR AND INDUSTRY DATE: 2-10-93

NAME	ADDRESS	COMPANY/ORGANIZATION
Kay Gattert	Topeka	Ks. Ins. Dept
L. Ferguson	"	AP
Maria Ackman	"	LT. GOV.
Bill Morrissey	"	DHR/Work Comp
John M. Ostrowski	"	AFL-CIO
DICK THOMAS	"	DHR/WORK COMP
SHELBY Smith	Wichita	EL-II
TOM WHITAKER	TOPEKA	Ks Motor Carriers Assn
Steven WALJE	Lawrence	KS Govt Counc.
RICK RIGGS	TOPEKA	LEGISLATIVE POST AUDIT

STATE OF KANSAS

DIVISION OF THE BUDGET
Room 152-E
State Capitol Building
Topeka, Kansas 66612-1504
(913) 296-2436
FAX (913) 296-0231

Joan Finney
Governor

Gloria M. Timmer
Director

February 3, 1993

The Honorable David Heinemann, Chairperson
Committee on Labor and Industry
Statehouse, Room 112-S
Topeka, Kansas 66612

Dear Representative Heinemann:

SUBJECT: Fiscal Note for HB 2116 by House Committee on Labor and Industry

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2116 is respectfully submitted to your committee.

HB 2116 would create a Workers Compensation Board to hear and decide appeals of decisions made by administrative law judges and by the Director of Workers Compensation. The bill would eliminate appeals to the Director's office and to the district courts and would instead give the Workers Compensation Board sole authority for the initial appeal of workers compensation decisions. Decisions made by the Workers Compensation Board could be appealed to the Court of Appeals and to the Kansas Supreme Court. The Director of Workers Compensation would retain the administrative responsibilities now performed by that office.

Members of the Workers Compensation Board would be required to have at least seven years experience in the practice of law and would serve six-year, staggered terms. Board members would belong to the unclassified civil service and would receive salaries equivalent to an administrative district court judge. The bill provides for a statutory nominating committee, composed of one member each from the Kansas AFL-CIO and the Kansas Chamber of Commerce and Industry, to select members of the Workers Compensation Board with approval from the Secretary of Human Resources.

HB 2116 also includes several technical changes to current statute. One provision would clarify that the demand transfer from the State General Fund to the Insurance Department's Workers Compensation Fund is subject to across-the-board budget cuts.

House Labor and Industry
Attachment 1
2-10-93

Another provision would strike language within KSA 1992 Supp. 44-510d, which pertains to repetitive use conditions, in order to bring that statute into compliance with a recent Kansas Supreme Court decision (*Stephens v. Sugar Creek Packing, 1992*). Finally, in the assignment of compensation for volunteer members of the Department of Civil Air Patrol, the average gross weekly wage would be increased from $433.80 to $476.38.

Any expenditures resulting from the passage of this bill would be in addition to the amounts included in the *FY 1994 Governor's Budget Report*, as amended. The minimal effect of HB 2116 would be an expenditure increase of $726,186 from special revenue sources. The bill would also increase State General Fund expenditures by an indeterminable amount.

The Department of Human Resources reports that the implementation of a Workers Compensation Board would increase expenditures from the Workmen's Compensation Fee Fund by $726,186 in FY 1994. The Department of Human Resources estimates salaries and fringe benefit costs of $420,870 for Board members and $129,344 for 4.0 support staff and personnel services. Within the Division of Workers Compensation, the Department anticipates the need for 1.0 Administrative Officer II and 3.0 Secretary II positions to coordinate Board activities. Other operating expenditures for the Board in FY 1994 are estimated to be $175,972, including $53,003 for one-time capital outlay.

The Office of Judicial Administration reports it cannot determine the net fiscal effect of HB 2116. Although caseloads would decrease for some district courts, the caseload for the Court of Appeals would increase under the bill. This shift in workload and judicial costs may or may not be offsetting. However, because KSA 1992 Supp. 44-556 stipulates that the venue for appeal is the county from which the cause of action arose, the Division of the Budget anticipates increased travel expenses for the Court of Appeals, but cannot determine the exact increase in State General Fund expenditures. In some instances, the Court of Appeals would have other cases to hear within a county of origin, besides workers compensation decisions; therefore, additional travel expenses would not be incurred. The provision concerning compensation for volunteers of the Department of Civil Air Patrol is not expected to have a significant impact on the State Self-Insurance Fund.

Sincerely,

Gloria M. Timmer

Gloria M. Timmer
Director of the Budget

cc: Dick Brock, Insurance Department
Sid Snider, Human Resources
Jerry Sloan, Judicial Branch

STATE OF KANSAS

DIVISION OF THE BUDGET
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Joan Finney
Governor

Gloria M. Timmer
Director

February 8, 1993

The Honorable David Heinemann, Chairperson
Committee on Labor and Industry
Statehouse, Room 112-S
Topeka, Kansas 66612

Dear Representative Heinemann:

SUBJECT: Fiscal Note for HB 2120 by House Committee on Labor and Industry

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2120 is respectfully submitted to your committee.

HB 2120 would make the following changes to the Workers Compensation Act:

1. The Workers' Compensation Fund would be "impled with particularity," which means that any impleading against the fund would be required to include specific information regarding the claimant's preexisting handicap and the specific physical or mental impairment.

2. Any impleading asserting liability against the fund would have to specify the basis of the employer's knowledge of the preexisting handicap.

3. The fund would be dismissed from any proceeding in which the impleading fails to include this specific information.

4. Should the fund be dismissed (see #3 above), all attorney fees incurred by the fund are to be assessed to the party responsible for the impleading.

House Labor and Industry
Attachment 2
2-10-93

HB 2120 would reduce expenditures from the Workers' Compensation Fund, although no reliable method exists to quantify the savings. The bill would have some administrative effects on the Insurance Department, but the effects could be managed within existing resources.

Sincerely,

Gloria M. Timmer

Gloria M. Timmer
Director of the Budget

cc: Sid Snider, Human Resources
Dick Brock, Insurance Department

2120.fn

KANSAS
TRIAL LAWYERS ASSOCIATION
Jayhawk Tower, 700 SW Jackson, Suite 706, Topeka, Kansas 66603-3731
(913) 232-7756 FAX (913) 232-7730

TESTIMONY
of the
KANSAS TRIAL LAWYERS ASSOCIATION
before the
HOUSE LABOR AND INDUSTRY COMMITTEE
regarding
HB 2191 - OMBUDSMAN/BENEFIT REVIEW PROGRAM
February 8, 1993

The Kansas Trial Lawyers Association is in complete opposition to HB 2191. We will explain specific provisions of the bill we find objectionable. However, we want to state at the outset our great concern with the concept of this proposal. We believe it is unfair and completely without justification that the legislature should even consider creating a new component in the workers compensation system that by law precludes claimants from having the legal right to the presence of counsel when their rights are being decided.

We raise the following questions about specific provisions within this bill:

1. Page 1, Line 16 - The ombudsman will "assist injured employees". Does this mean they'll serve as their legal counsel or clearly serve in the capacity as advocate for the claimant? This is an extremely important question and the answer is basic to this whole bill.

2. Page 1, line 21 - The ombudsman <u>may</u> represent claimants. We assume this implies they also may <u>not</u> do so.

3. Page 1, lines 22-24 - The language here suggests ombudsmen will do more than assist (whatever that means) unrepresented claimants. In addition, they would assist employers and other parties to protect <u>their</u> rights under the act. This seems to us an indication the ombudsman will serve many masters, which means the claimant is left without someone upon whom he or she can rely to have <u>their</u> best interests in mind.

4. Page 1, line 38 - In describing the Benefit Review Conference (BRC) the bill indicates a review of "available information". This is far too general to provide the parties with a clear understanding of what will or will not be under consideration at the BRC.

5. Page 2, lines 3-5 - The secretary <u>may</u> adopt rules where a BRC would not be mandatory. What guidelines would the secretary follow to create such rules? The bill provides no direction to the secretary in this regard.

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Attachment 3
2-10-93

6. Page 2, lines 13-17 - We feel it is inappropriate for a Benefit Review Officer (BRO), who may or may not even be an attorney, to make the decision about whether a party had "good cause" to be unable to attend a scheduled BRC. The decision would obviously be judgemental and likely would lead to additional litigation and expense.

7. Page 2, line 34 - The BRO will be charged with mediating disputes "consistent with the act", even though the BRO may not even be an attorney. The Insurance Department's Task Force that created this proposal strongly considered requiring that the BRO <u>not</u> be a lawyer, which was overwhelmingly the sentiment of those on the Task Force. The point is it is very possible the Benefit Review Officers would not be attorneys trained in the legality of the act.

8. Page 2, lines 36-27 - Again, how could a non-attorney "thoroughly inform" all the parties of their rights under the act?

9. Page 2, line 39 - The BRO will insure that "any other information pertinent to the resolution" is contained in the claim file. Who decides what "any other pertinent information" includes? This could certainly prove to be another area of dispute and thus litigation.

10. Page 3, lines 4-5 - The BRO can pose questions to the claimant, the employer and the insurance carrier, but apparently no one having information of use to the claimant can be asked to contribute. Why not?

11. Page 3, line 29 - If the <u>claimant</u> commits fraud, the insurance carrier is relieved of the effect of signed agreements. What happens if the employer, insurance carrier, or anyone else commits fraud? We have to assume that under the wording of this bill the claimant would simply be out of luck.

12. Page 3, line 34 - The content of the "report" prepared by the BRO is described but the bill doesn't tell us what use will be made of the report. If, as the bill states, no formal record will be made of the BRC, why does the director need to have a "report"?

13. Page 3, line 36 - The above mentioned "report" will list a detailed statement of the unresolved issues. Again, if no one can make use of this information, why is it being documented?

14. Page 3, line 41 - Again, the BRO will be describing the rights the parties have to subsequent review. Without legal representation, the claimant will have to simply <u>hope</u> the BRO's advice is correct.

15. Page 4, lines 24 - 27 - The "report", which is different from any agreement the parties may have signed, is given to the director AND the claimant, employer and insurance carrier. Even though this report is supposedly not a part of the formal record, it would appear to us to have a similar affect. This blurs the lines between the alleged "nonadversarial, informal dispute resolution" and a formal legal proceeding.

16. Page 4, line 41 - The claimant may be represented by an ombudsman at the BRC. They also may not be so represented. But even if they are, remember this is the ombudsman whose job it is to assist unrepresented claimants, employers and other parties. To suggest an ombudsman will serve the function of an advocate for the claimant is at a minimum not required under HB 2191, and we believe unrealistic to expect in the real world.

17. Page 4, line 43 - The claimant cannot, by law, have an attorney present at a BRC. This is in spite of the fact an insurance adjuster, an individual who earns his or her living minimizing the payment of claims, will be present. Additionally, we believe the BRO will be evaluated not on the number of fair settlements agreed to, but simply on the number of settlements period. Obviously not all settlements are fair and certainly we believe this bill will result in an inordinate number of settlements leaving the injured worker with less than they deserve under the law.

When presenting this bill for introduction by this Committee, the Insurance Department's initial summary of the Benefit Review Conference proposal was "here is where we are taking the attorneys out of the system". At least that was an accurate description of what this is all about.

We want to encourage the members of the House Labor and Industry Committee to look beyond the simplistic and politically attractive notion of keeping the attorneys out of the process. HB 2191 may have that effect. Attorneys are resilient and will find other clients in need of their services. But the real issue is the fate of injured workers themselves. What happens to them and their families if they get treated unfairly under a new system?

KTLA is not suggesting you look at how HB 2191 may "hurt" attorneys. We are asking you to consider how it may well hurt Kansans injured on the job.

While we are adamantly opposed to HB 2191, we support an alternative which would reduce litigation, save money and still treat claimants fairly.

First, the Claimant Advisory Section of the Division of Workers Compensation is overworked and understaffed. We believe they provide a constructive service and it should be expanded by adding more personnel to handle more inquiries from all those with questions about the workers compensation system.

Second, especially from our perspective as claimants' attorneys, we want cases to be settled. We would support a mandatory settlement conference, perhaps at the time of the preliminary hearing. The goal of amicably settling claims before expensive litigation begins could still be accomplished, but without the need for a bureaucratic and expensive new step in the process and without any additional delay. If the Committee chooses to consider a mandatory settlement conference, we urge you to make it clear that someone from the employee's company or insurance carrier who has the authority to settle claims be present.

Thank you for the opportunity to comment on HB 2191.

MERLINO & SCHOFIELD, INC.
CONSULTING ACTUARIES

MATTHEW P. MERLINO, FCAS, MAAA, MCA

DAVID A. SCHOFIELD, FSA, MAAA, CLU, FLMI, ChFC

January 12, 1993

Mr. Richard H. Mason
Executive Director
Kansas Trial Lawyers Association
Jayhawk Tower
700 S.W. Jackson Suite 706
Topeka, Kansas 66603-3731

Re: Review of Kansas Workers' Compensation Closed Claim Study

Dear Mr. Mason:

Merlino & Schofield, Inc. (M&S) was requested by representatives of the Kansas Trial Lawyers Association (KTLA) to review an actuarial study prepared by Martin A. Lewis of Tillinghast, Towers/Perrin (Tillinghast). The report titled Kansas Workers' Compensation Closed Claim Study was performed by Tillinghast on behalf of the National Council on Compensation Insurance (NCCI). Our participation includes the review of the methods used by Tillinghast in reaching the conclusions contained in this study. We did not perform the additional analysis required to provide alternative conclusions regarding the items addressed in the report. However, in certain instances we described procedures that in our opinion would improve the accuracy of the results. We did not however obtain the data required to implement these alternative procedures.

The material provided to us for review included a bound report titled "Kansas Workers' Compensation Closed Claim Study" and a separate document labeled "Interpretive Analysis of the Kansas Workers' compensation Closed Claim Study". These two documents were dated July 15, 1992 and July 16, 1992 respectively.

The data used in this study consist of a sample of 1,033 Kansas workers' compensation claims closed during the period January 1, 1990 through December 31, 1991. The claims selected were defined as being of a permanent injury nature. Commercial insurers contributed 909 claims and a self-insured claims administrator contributed 124 claims. While the claims included were closed during calendar years 1990 and 1991, the underlying accident dates ranges from 1979 to 1991. However, all of the claims contributed by the self-insured administrator have accident dates between 1987 and 1991. Thus the insured and self-insured categories do not have similar accident year distributions.

House Labor and Industry
Attachment 4
2-10-93

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The remainder of this letter summarizes our conclusions regarding the above mentioned report. Our comments are segregated into those related to the general procedures used in the analysis of the data and alternatively into specific observations regarding the conclusions contained in the Interpretive Analysis section of the report.

One shortcoming of the study is a result of inherent limitations related to studies performed on a data base consisting only of closed claims. Since closed claim studies are by definition based on a sample of claims closed during a particular time period, the sample may not be representative of claims expected to be incurred during a given time period. For example, claims closed during a particular time period may contain a relatively smaller or larger percentage of serious claims in comparison to less serious claims depending upon the growth rate of the underlying population or the particular accident years included in the study. This occurs because while claims closed in a particular period will consist of both large and small claims, generally the smaller claims will result from recent accident years whereas on average the larger claims will result from older accident years.

For example, if we have two groups of claims closed in 1991 but in which one (#1) contains claims occurring in 1987-1990 and the other (#2) contains claims occurring in 1975-1990 we would expect the average claim size for the later group (#2) to be greater than the former (#1), simply due to the difference in distribution by accident year.

Thus when using various subgroups of claims closed during a particular time period to test the significance of some variable it is important that the distribution by accident year within each of the two groups is relatively similar. Otherwise the difference in the two categories may be a result of differences in the distribution by accident year rather than the variable under consideration.

The second limitation related to closed claim studies is caused by the impact of inflation. Since claims closed in a particular time period consist of claims occurring over many accident years and include payments made over various time frames, the impact of inflation can result in two significantly different total payment amounts for two similar claims occurring in different accident years. This impact of inflation will also distort a comparison of claims closed during two different time periods. Inflation alone will result in an increase in the average closed claim size over time. For example, in the comparison of pre-Hughes versus post-Hughes claims, we would expect the inflation impact

alone to result in an increase in post-Hughes decision claims of perhaps 9 to 11 percent.

Thus in using claims closed in a particular time period to test the impact of selected variables, it is important to recognize the impact of loss inflation and potential differences in the distribution by accident year. We were unable to locate any reference to adjustments or consideration of these items in the report under review.

Methodology

The most significant shortcoming of the approach used to test the relationship between specific items and the average claim size results from a failure to remove the impact of other variables. Specifically, with regard to measuring the impact of the characteristics listed below the underlying data was not sorted in a fashion that would isolate the variables under review.

- o Self-Insured vs. Commercial
- o Attorney Involvement vs. No Attorney Involvement
- o Pre-Hughes vs. Post-Hughes

For example, in order to identify the correlation between average claim size and attorney involvement, it is necessary to eliminate other variables which may impact the average claim size. Instead of comparing an average of claims with and without attorney involvement, claims with similar characteristics other than the presence or absence of attorney representation must be selected. Otherwise we are unable to identify the impact of one variable at a time. If claims are selected at random and placed into two groups (attorney involvement and no attorney involvement) it is impossible to measure the difference in claim size attributable to attorney involvement and the difference related to other items such as injury type, accident year, impairment rating etc. That is, it may be that in general more serious claims are more likely to require attorney involvement and thus we are not measuring the impact of attorney involvement but instead are measuring the differences in the average claim size of more versus less serious claims.

Thus in this example a more accurate measure would result if we identified claims with similar characteristics other than the item under consideration and test the significance of the item under various conditions. While the type of claim is an important variable to consider when measuring attorney vs. non-attorney, other variables may be important when measuring other characteristics. In the case of pre-Hughes vs. post-Hughes the distribution by accident year and average date of payment is an important variable that must be considered before an accurate measure of the

Hughes decisions can be obtained. Additional information on the impact of plan design is described in the remainder of this letter.

An additional potential for misleading conclusions results when the data is sorted into various groups based upon differences in one characteristic without attempting to neutralize the impact of other variables. That is, when measuring the impact of one variable, the potential effect of other variables must be eliminated. Thus instead of sorting the entire data base into two groups based on the presence or absence of one variable, a sample of claims with similar characteristics other than the variable being measured must be used to test the significance of the variable under consideration.

Self-Insurance vs. Commercial Carriers

The plan design used in the report to measure the difference between self-insured and commercial insured claims administration illustrates the problem described above. Specifically, if the objective is to measure the efficiency of claims handling for self-insured programs compared to commercial carriers using the average claim size as the measure of efficiency, it is necessary to eliminate the impact of other factors that may affect average claim size. Without eliminating these other factors, it is impossible to distinguish the impact of the variable under consideration from the impact of other variables.

Potential factors, other than self-insured or commercial carriers, that may impact the average claim size would include differences in the industrial composition of entities contained in the self-insured claims data base as compared to the insured claims data base. For example, in the event the self-insured population contains on average industries with less hazardous operations, we could expect a relatively larger percentage of less severe claims than those contained in the insured population.

It would appear that a more appropriate method would be to compare claim size (in addition to other characteristics that are assumed to be indicators of the quality of claims handling) for claims with similar severity characteristics. That is, select claims with similar type of indemnity (e.g. permanent total), body part, impairment rating, etc. and then use this subset of claims to test the one variable under consideration.

An additional shortcoming associated with the analysis of the self-insured claims as compared to the commercial carriers claims includes the potential differences of the underlying hazards of the insureds and difference in the accident years involved. As shown on Exhibit II, Sheet 1 of the report, the self-insured claims data

does not include claims with accident dates prior to 1987, whereas the insured data includes claims with accident dates from 1979-1991. As shown on this exhibit, it appears the average closed claim size is on average smaller for the more recent accident years. As a result of the difference in the distribution by accident year for self-insured and commercial carrier categories, we would expect the average claim size for commercial carrier claims closed during the study period to be larger than the average claim size for self-insured claims.

On pages 3 and 4 of the "Interpretive Analysis" section it states self-insured claims exhibit shorter lag times to closure and fewer days from injury to return to work. Again, it does not appear that differences in the accident date distribution have been considered before these conclusions were reached. It would appear that accident date would affect both of the above mentioned items.

Further, due to the limited number of claims contained in the self-insured data set (124), differences in the underlying hazards of the industries contained in the self-insured data as compared to the insured data could result in differences in the average claim-size. We were unable to locate any reference to potential similarities or differences in the industries insured. This could be examined using payroll by rating classification for the groups.

Attorney Involvement

The primary limitation in plan design with regard to the evaluation of the impact of attorney involvement is the failure to control the impact of other variables. That is, factors with potential impact on cost other than attorney involvement were not equivalent or approximately equivalent. In order to test the impact of attorney involvement it is necessary to compare claims with similar characteristics other than the characteristic under consideration. Otherwise, it is impossible to distinguish whether the difference in outcome is a result of the factor under consideration or some other factor.

The impact of the above limitation is mentioned on page 18 of the "Interpretative Analysis" accompanying the Kansas Workers' Compensation Closed Claim Study. In this section of the report, Tillinghast states that whether (1) attorneys become involved in more serious cases, (2) attorney involvement causes high claim costs, or (3) there exists a combination of these two factors is not readily determinable from the data.

However, on the following page (i.e. page 19) of the "Interpretative Analysis" section, it is stated that "lag time from date of injury to return to work is also increased by attorney involvement". In our opinion a more accurate statement might be that attorney representation and settlement time appear to be correlated. However, even this statement cannot be conclusively supported due to the limitation in plan design mentioned previously. That is, does attorney involvement result in longer settlement lags or, alternatively, is it that more serious claims are more likely to seek attorney representation, and since more serious claims (with or without attorney representation) generally require a longer time to reach settlement, claims with attorney representation also require a longer time to reach settlement? Thus without measuring the impact one variable at a time, the effect of the independent variable cannot be determined.

In summary, in order to estimate the impact of one variable (e.g. attorney involvement or pre vs. post-Hughes), it is necessary to develop a comparison of claims with similar characteristics other than the specific item under consideration. In the event all other characteristics are not equal, an effort to adjust for differences should be incorporated before interpreting the results. Specifically, in the case of measuring the impact of attorney involvement the other characteristics contained in the data base that may potentially impact claim size include:

- o accident year- (i.e. trend, benefit level changes)
- o impairment rating
- o indemnity type (e.g. temporary total, permanent total, etc.)
- o injury cause (e.g. burn, strain, etc.)
- o age
- o sex
- o body part(e.g. head, trunk, etc.)

For example, rather than comparing the average claim with attorney involvement (i.e. $29,029) to the average without attorney involvement ($17,445) for all claims, a more accurate indicator would be to compare claims with similar indemnity type, injury cause and impairment rating from a similar accident year, or alternatively claims with similar characteristics other than accident year but after adjustment for inflation and benefit level changes.

A simplified example of this type of approach would be to compare the average claim size for back claims with and without attorney involvement at similar impairment ratings levels. A sample calculation using claims with impairment ratings ranging from 51-100% results in average indemnity of $51,310 and $85,559 for attorney and non-attorney involvement, respectively (See

Exhibit XXV, Pages 1 and 2). Due to the relatively small number of claims contained in this subset of the data sample, this result is not statistically significant. However, this comparison does illustrate the concept described above, with the exception there is no adjustment for loss inflation and benefit level changes. In any event, the results seem to indicate the potentially misleading results of comparing simple average claim sizes.

Hughes Decision

As mentioned previously, the comparison of simple averages without adjusting for changes other than the variable under consideration (i.e. in this example the Hughes decision) will potentially result in misleading conclusions. On page 6 of the "Interpretive Analysis" section of the Tillinghast report, this type of approach appears to be used to estimate the impact of the Hughes decision. One limitation of this approach is that using claims closed pre-Hughes to develop an average claim size to compare to the average claim size calculated using claims closed after the Hughes decision ignores the impact of inflation. In addition, the two groups of claims used (i.e. pre-Hughes and post-Hughes) are inconsistent with regard to the average lag between the accident date and the settlement date. Both sets of claims were incurred during the same accident years yet the pre-Hughes claims were closed approximately one year earlier.

With regard to the distortion resulting from the impact of loss inflation, we would expect claims closed on the average one year later to settle at a level equal to the annual trend rate (inflation) for workers' compensation in Kansas. In addition, since both groups of closed claims (before and after Hughes) included claims incurred in accident years 1979 through 1990, we would expect the claims closed after the Hughes decision to be relatively older claims and on average more expensive claims. For example, accident year 1986 claims included in the study and closed prior to the Hughes decision would have been closed sometime during the time period 1/1/90 to 11/26/90 and thus would on average have a lag between accident date and settlement date of slightly less than four years, whereas the 1986 accident year claims included in the post-Hughes average claim calculation would have been closed during the time period 11/27/90 to 12/31/91 and thus have an average lag between accident date and settlement date of slightly less than five years. As shown on Exhibit II, Page 1, the average claim size for claims closed during the time period selected for the study appear to be larger for the older accident years. That is, the average closed claim size and settlement lag appear to be positively correlated.

Thus, even ignoring the inflation impact, we would expect the post-Hughes average closed claim to be larger than the pre-Hughes

average closed claims due to the difference in settlement lag for the claims contained in each of the two groups. In order to illustrate the impact of these two items (i.e. trend and settlement lag), we have adjusted the averages as shown on Page 6 of the "Interpretive Analysis" section of the Tillinghast report.

In the report, Tillinghast states that the post-Hughes average claim based on accident years 1986-1990 is $24,525 as compared to the pre-Hughes average claim size of $21,411. Due to the difference in settlement lag a more appropriate comparison would be to use accident years 1986-1990 for pre-Hughes ($21,411) and accident years 1987-1991 for post-Hughes($26,410). Also the pre-Hughes average ($21,411) should be adjusted for one year of loss inflation. Assuming an average annual trend rate (inflation) of 9% the adjusted pre-Hughes average would be ($23,338). Thus the increase resulting from the data would be +13% rather than the +33% shown in the Tillinghast report.

Statistical Analysis

As stated previously, due to the failure to properly segregate the claims data the conclusions summarized in the later pages of the "Interpretive Analysis" section of the report are not conclusively supported. For example, the table shown on page 28 of the "Interpretive Analysis" section which summarizes the results of the statistical test performed on the closed claim data is subject to misinterpretation. Due to the failure to hold additional variables constant, the test used does not result in a conclusion regarding a specific correlation between the specific variable noted and the dependent variable (e.g. average claim size). That is, the test used only results in a measure of the probability that there is a difference in the two claim samples. However, due to the number of variables other than the specified variable potentially contributing to the difference in average claim size, the test does not result in a conclusion with regard to the impact of one particular variable. For example, the application of the t-test to the data sorted into attorney involvement and no attorney involvement groups does not result in a conclusion with regard to the impact of attorney involvement on claim size, but instead, only concludes that there is a difference in the average claim size of claims with attorney involvement versus claims with no attorney representation. The test does not offer any conclusion with regard to a cause and effect between attorney representation and average claim size because other variables such as indemnity type, impairment rating, injury cause, etc. have not been held constant. Thus there may be a positive correlation between attorney involvement, average claim size and one or more other variables. Without investigating each potential variable individually, the

correlation between the specific variable and the average claim size cannot be measured.

The other applications of the t-test shown in this table do not offer definitive conclusions since again other variables that may impact average claim size have not been held constant. In order to test the significance of the impact of each characteristics, a more specific sample of claims must be selected. Otherwise it is not possible to reach a conclusion regarding the impact of a particular variable with any degree of certainty.

SUMMARY OF FINDINGS

1. Failure to Account for the Impact of Other Variables - The most significant shortcoming of the methodology employed to test the relationship between specific items and the average claim size is the failure to remove the impact of other variables.

2. Only Closed Claims Studies - Since closed claims studies are by definition based on a sample of claims closed during an isolated period, the sample may not be representative of claims expected to be incurred during that period.

3. Inflation Ignored - Our understanding is that the claims data was not adjusted for loss inflation. This is important, particularly when attempting to compare pre and post-Hughes claims, since the inflation impact alone could result in a post-Hughes increase of 9-11 percent.

4. Self Insured V. Commercial Carrier Comparison Flawed - No attempt was made to look at the industrial composition, the degree of hazardous occupations, etc. of the businesses represented by the self-insured and commercial carriers.

5. Misleading Implications of Test Results Related to Attorney Involvement - The plan design used does not result in any definitive conclusion regarding the impact of attorney involvement. In order to test the impact of attorney involvement, it is necessary to compare claims with similar characteristics. Placing random claims in only two groups (those with and without attorneys) makes it impossible to measure the impact, if any, on average claim size.

Sincerely,

George W. Turner, FCAS, MAAA