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WORKER'S COMPENSATION INSURANCE FACTS

In 2003, the Legislature took a major step in reforming California's worker's compensation system by enacting multifaceted reforms that can potentially produce billions of dollars in savings for employers.

But considerably more work is needed to further overhaul a badly broken system and assure continued progress in transforming the worker's compensation system into an effective and efficient mechanism for serving injured workers.

With skyrocketing rates and general turmoil in California's worker's compensation market, it would be easy to point the finger at insurers as the culprit and focus for further reform. In fact, insurers are victims of the system, as are employers and injured workers.

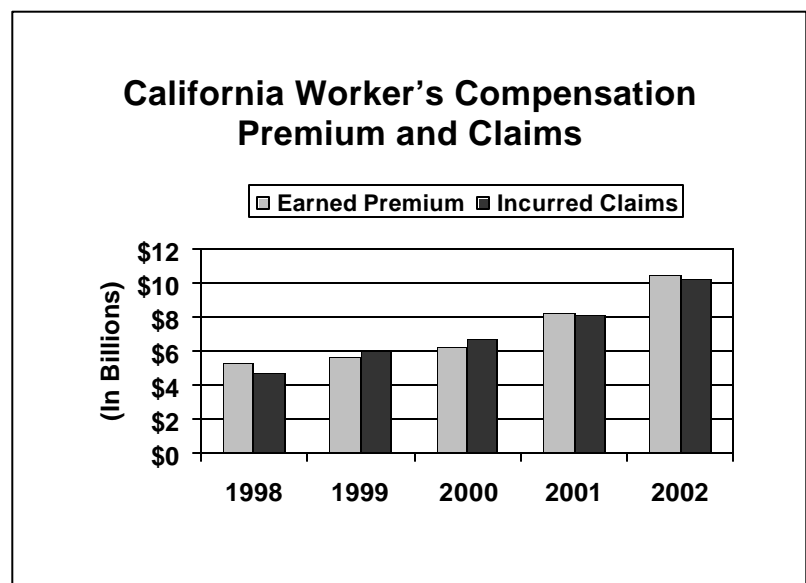
From 1998 to 2002, insurers writing worker's compensation coverage in California lost \$3.5 billion, paying out \$1.43 in claims and expenses for every dollar of premium collected. These figures do not come from insurers, but rather from an organization of public officials who regulate the industry – the National Association of Insurance Commissioners.

As a result of this lopsided revenue/expense ratio, it comes as no surprise that the rate of return for insurers is in the negative column and numerous carriers have gone bankrupt.

Here's a further, more detailed look at the data:

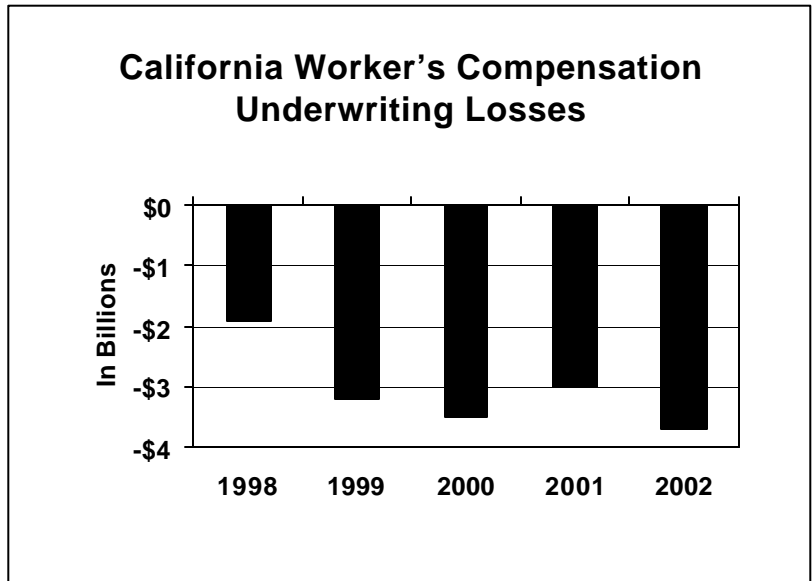
Simply stated, California's worker's compensation rate increases are due to rapidly rising costs, not the market downturn or mounting expenses. The National Association of

Insurance Commissioners (NAIC) noted that in 1998 worker's compensation claims totaled \$4.7 billion as compared to \$5.3 billion in premiums collected by insurers.



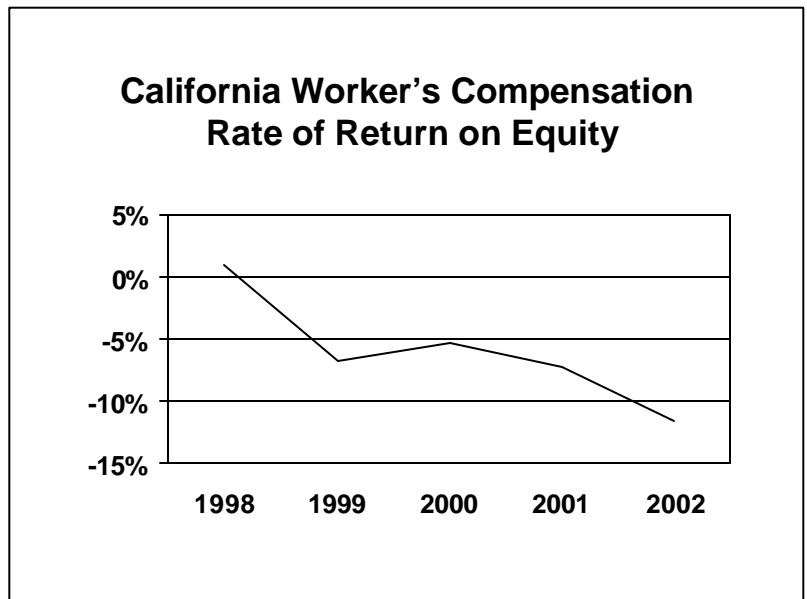
Since then, premiums **on average** have increased 96 percent while claims have increased 117 percent. The increase in premiums, as large as it has been, has not kept pace with the increase in benefits paid to injured workers.

With losses outpacing premiums, California's worker's compensation insurance market generated huge losses from 1998 to 2002 (the latest years that data is available), according to the NAIC. Claims and expenses exceeded premiums by \$15.3 billion over this period. Even when investment income and theoretical tax credits are taken into consideration, the NAIC estimates worker's compensation insurers lost \$3.5 billion, or 10 percent of premium over this period.



It is important to keep in mind that these are average figures and there are some exceptions involving a few individual companies that have reported gains. Focusing on isolated and limited gains, especially quarterly gains, is inappropriate because they can be extremely volatile and misleading when compared to huge losses in the past.

A good perspective of the insurance industry's fiscal situation in California is available from rate-of-return data. The rate of return for worker's compensation insurers has been steadily declining over the past five years in California. In 2002, insurers experienced a dismal **NEGATIVE** 11.5 percent return. This rate is in sharp contrast to the 10 percent return in 2002 for Fortune 500 companies. And, that 10 percent was the worst return in 10 years.



These disastrous losses drove 26 insurers from the California market from 1998 to 2002. Many of those insurers went bankrupt. And while California has the largest economy of any state, 22 other states have more insurers writing worker's compensation.

Embedded in the debate over costs and negative rates of return are salaries paid to insurance executives. It's a bogus issue. Based on data for all industries, compensation for officers amounts to 2.3 percent of receipts. Insurers on the other hand compensate officers equal to only 1 percent of receipts (premiums), or a rate less than half that of all industries.

Another important issue that critics raise in the debate over worker's compensation reform is insurer's investment income. It has even been incorrectly suggested that worker's compensation rates have increased dramatically due in large part to the sharp downturn in the stock market.

It's important to remember that property/casualty insurers (including worker's compensation insurance carriers) are not heavily invested in the stock market. Only 18 percent of the insurance industry's investments in 2002 were in common stocks.

While it is true insurers lost approximately \$17 billion in the stock market from 2000 to 2002, insurers are not allowed to base future rate increases on past investment losses. Even if insurers were permitted to recover in one year the \$17 billion loss, the impact on rates would have been less than 5 percent.

Officer Compensation	
<i>Industry</i>	<i>% of Receipts</i>
Arts and Entertainment	8.3%
Construction	3.3%
All Industries	2.3%
Hotels and Food Services	2.1%
Transportation	1.5%
Wholesale Trade	1.2%
Retail Trade	1.1%
Manufacturing	1.1%
Insurance	1.0%

Worker's compensation insurers are subject to regulation. Some critics contend that even stricter controls need to be imposed on insurers. ACIC disagrees with this contention. We believe that the current open competition system for regulating insurers must be preserved.

Only if open competition is allowed to continue with new cost saving reforms will the worker's compensation insurance marketplace be able to recover fully to the benefit of the consumer – employers and injured workers.

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The Association of California Insurance Companies (ACIC) is an affiliate of the Property Casualty Insurers Association of America (PCI) and represents more than 300 property/casualty insurance companies doing business in California. ACIC member companies write almost 40 percent of the total property/casualty insurance in California, including 53 percent of personal auto insurance, 43 percent of commercial automobile insurance, 35 percent of homeowners insurance, 31 percent of business insurance and 43 percent of the private worker's compensation insurance.