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Is Your Organization a Good Risk? A Candid Look at the Road Ahead

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Is your organization an attractive risk to underwriters? If not, you may find that you have limited options when it comes to workers compensation.

For a number of years, I have helped insurers sort out good risks from the not-so-good. My work is performed over and above conventional underwriting, which basically focuses on the class of business and the loss history. Underwriters rarely talk to potential insureds. Theirs is primarily a paper review. If there are questions or concerns, the issues are usually addressed through the agent.

As a student of risk management, I believe that if insurers really want to understand a risk, they must do more than review the paper.

outside on electrical poles or hooking up major power line transformers. The latter activities might be a red flag to the underwriter.

It's worth noting that even if the underwriter is comfortable with the list of recent projects performed by the potential insured, this list might not be indicative of the risks ahead.

Classifications of Employees

Employee classification is usually fairly straightforward, but interesting issues often arise. For example, in construction, employees might be classified as "finish carpenters," but the work might begin with a vacant lot and end with a building — therefore, framing carpenters, a higher risk class, are involved. The difference in relative risk, of course, is reflected in the rates paid for each class. Construction companies generally prefer to list as many "construction supervisors" as possible because the rates are lower — even though these supervisors might be directly involved in performing the physical work.

It's important to note that there are fewer than 600 class codes to choose from and many jobs don't fall comfortably within any one job classification. To cite just one example, there is a single class for teachers, but teachers of severely autistic children are at much higher risk for injury than teachers in regular classrooms.

Loss History

Underwriters look at your organization's past performance as the single most important factor in assessing your risk. In the world of insurance, this "look in the rear-view mirror" is considered the strongest predictor of future performance.

Has your loss ratio been favorable, over both the past year and the past three years? In other words, has your insurer made money?

Have you had any large losses? If your recent loss runs have several large or catastrophic losses, underwriters are likely to reject your account. Unless you are a very large risk (generating significant premium — in the range of a half million dollars or more) or in a very soft market (not these days!), employers with recent large losses usually end up in the state's assigned risk pool.

Does your organization have a pattern of losses? Underwriters will zero in on a pattern of falls from heights (even if minor), musculoskeletal claims, or repetitive-motion injuries. In my experience, repetitive motion claims are actually contagious. Single incidents are rare; where there is one such claim, there are usually several.

They need to engage senior managers directly in a friendly, open-ended conversation that focuses on what the employers do, how and where they do it, and, most important, the people performing the work. These conversations can provide a more nuanced picture of the true dimensions of the risk.

To help you assess your organization's risk profile, I'll provide a brief overview of the conventional underwriting process, discuss a few places where the paper process may fall short, and offer some recommendations for looking beyond the obvious that may be helpful to both insurers and risk managers.

Where Underwriting Begins

Unless your organization is self-insured, you probably purchase workers compensation insurance through an insurance agent. The insurer's underwriters perform a paper review of your history and your application for insurance. In most cases, they do not talk directly to you. The underwriters look closely at your class of business, which offers a general description of the type of work you perform. They also examine the different job classes for your employees and the rates associated with those classes. Underwriters want to ensure that the rates in your state are high enough to cover the anticipated losses. And most important to insurance underwriters is your loss history. Underwriters assume that your past performance is the single most important indicator of how well you will do in the future. Using data from the Bureau of Labor Statistics, they might compare your performance with other companies performing the same work. And above all, underwriters want to know if your current insurer made a profit on your account.

This type of risk assessment is both useful and necessary. Let's look at these basic risk factors more closely.

Class of Business

What exactly does your organization do? Is the work inherently risky? Many insurers avoid the really high-risk classes of business, such as logging, roofing, demolition, mining, high voltage electricity, and commercial fishing. Today, overseas consulting might be added to the list of inherently undesirable risks, particularly if the work occurs in the Middle East.

Underwriters also want to know if the actual work performed is correctly reflected in the class. For some companies, the basic class does not adequately reflect some of their outlying or marginal activities. For example, an electrical contractor may work mostly inside but, on occasion, may work

In addition, when I see relatively clean loss histories, I wonder if the employer would know how to respond if an injury occurred — would it know how to secure first-rate medical attention and how to care for the worker in those first important hours and days immediately following an injury? I wonder if there is an aging work force, where, with each passing year, the workers are at greater risk for cumulative trauma injuries. I wonder if the employer would commit to the use of light duty to speed the recovery for any injured employee. A clean loss history is certainly desirable, but it must be accompanied by a *commitment to do the right thing and a plan of action if an injury should occur*.

Finally, there is a conundrum in workers compensation insurance that makes the employer with a clean record potentially a bigger risk than an employer with a history of recent losses. Organizations with good loss histories pay less for insurance — they often have credit experience modifications, which lower the premiums below those paid by their competitors with histories of losses. In addition, to secure these desirable accounts, insurers often provide steep discounts as incentives. In these instances, the insurer collects substantially less premium, which leaves a smaller margin for profit should injuries occur.

On the other hand, a loss run with lots of activity, including large losses, doesn't necessarily indicate a risk that should be rejected. What has the organization learned from its experience? Did it improve its safety program? Was the serious injury a wake-up call? How did the employer respond to the adversity? I have talked to managers who respond to a big loss with an absolute commitment to never let it happen again. These can be very good risks.

In addition, companies with poor loss histories pay more for insurance — their experience ratings float upward with the frequency and severity of their losses. They usually are not eligible for discounts. In effect, by collecting more premium, there is a greater margin of error for the insurer. If the employer is willing to commit to "best practices" going forward, it might be beneficial for insurers to "ride the high mod" and write the account.

Growing Pains

One of the most important missing elements in "backward look" underwriting is understanding where an employer is headed. Success in business can lead to unanticipated risks. Is business good? Is the organization in a position to expand? If the answer is yes, then what might have been a good risk — even a slam-dunk — may now be covered with red flags.

Business Operations

Finally, underwriters usually look at your basic business status. They may check your credit rating with Standard & Poor's or a similar service. They want to make sure you pay your bills on time.

Beyond Conventional Underwriting

After underwriters complete their risk assessment using the above factors, they have a fairly clear picture of how good a risk you have been in the past. But to my mind, the underwriters really don't have much of a clue about the risks in your immediate future. In working with hundreds of employers over a decade and a half, I have come to believe that real risk assessment requires a step out of the conventional underwriting box. While each of the above items is *essential*, taken together they are not *sufficient*.

A paper review cannot provide a complete view of risk. "Yes" and "no" answers ticked off on a questionnaire fail to provide the underwriter with a sophisticated view of the risk. Digital responses cannot provide a three-dimensional picture of what is happening within an organization. It's my contention that true risk assessment requires an open-ended conversation with a key person inside the business. In the course of such a conversation, which could take anywhere from ten minutes to an hour, an underwriter should try to learn about the organizational philosophy and the spirit in which the work is performed.

Beware the Clean Loss Run

Loss runs provide a snapshot of injuries over a given time period. Conventional underwriting views a clean loss run as a huge positive factor. While most would agree, it may be worthwhile to look at clean loss runs more closely.

For example, I have heard managers of staff who perform physically demanding jobs describe the 25 years of loyal service that the work force has logged with pride: "We've never had a claim." But 25 years of physically demanding work places every one of their aging employees at risk. All too often, these loyal people have few transferable skills. They know the work they've been doing all their lives, but know very little beyond it. When these workers suffer from severe strains or sprains and the doctor says they can no longer perform the physically demanding work, they may be too old to learn a new trade. With no access to less demanding work, barred from continuing their trade, these workers are at high risk for retiring on permanent benefits — an expensive proposition for both the employer and the insurer.

In my experience, expanding companies are bad risks — and the burden of proof is on these employers to show me otherwise!

Expansion requires hiring and training new people. Finding reliable people with good work habits is *always* difficult. Hiring means bringing a lot of strangers into the work force. Is the employer really good at this? Does it have a track record of bringing in good people? Does it know how and when to terminate people who are not working out? Do growth plans mean that the employer may be forced to hire any "warm body?"

The Tipping Point

Here's a real life situation: In 2000 I began working with a Massachusetts masonry contractor that had a stable crew of 25 workers, all of whom had been with the company for at least three years. The loss ratio was very good, below 20 percent. The company had plenty of work and kept the crew busy year round.

The next I heard — three years later — the loss ratio had zoomed above 200 percent and the insurer had terminated coverage, forcing the contractor into the assigned risk pool. What had happened?

In reviewing the file, I found that the contractor's payroll had gone from 25 full-time people to 70. The contractor had secured several large contracts and hired up quickly to meet the deadlines. The expansion more than doubled the crew and, as a result, the tight-knit camaraderie of the original crew was overwhelmed by the influx of strangers. The employer hired some good people and also hired some people who turned out to be marginal. Some new employees followed directions and safety protocols carefully, while others did not. The company had a rash of claims, a number of them questionable, involving soft tissue injuries. In a word, the employer lost control of the company. The work culture changed overnight from positive to negative, and the crew went from exemplary to questionable in a flash. Interestingly, some of the long-term employees were influenced by the new workers and ended up filing claims, not because they had serious injuries, but because they succumbed to the temptation of getting paid for not working. To be sure, there were serious injuries that absolutely required time away from work, but in too many instances, there were ambiguous lower back strains with little, if any, objective medical findings. Let's face it — handling cinder blocks all day is hard, demanding work. For some people, being paid not to work beats working. This employer's experience presents a powerful example of a "tipping point" — from good culture to bad, from managed to unmanageable, in the course of just a few months.

Managing Growth

Is every expanding organization a bad risk? Certainly not. Some companies manage expansion very well. Here are some actions that you can take to manage growth:

- Communicate with your core group of workers to enlist their help in integrating new employees.

- Establish a careful recruiting strategy, drawing upon existing networks wherever possible. Your most valued employees may be your best source for new workers (although even these referrals need to be checked out thoroughly).

- Develop a clear set of expectations for every open position. This includes job descriptions with enough detail to give a real flavor for the work. For example, if the working conditions are at all unusual, make this perfectly clear up front.

- Require a written job application. Read submissions carefully. Look for extended employment gaps and the reasons for leaving prior employment.

- Interview every applicant. Ask open-ended questions. See how applicants have handled adversity in their careers (but don't ask illegal questions, such as "Have you ever filed a workers compensation claim?").

- Check references. Push hard for full disclosure. If the prior employer will only verify "dates of employment," tell the employer that you assume this is a negative reference — that may sway the employer to reveal more.

- Orient and train new employees to your company's way of doing the work. Ensure that safety training is provided. Do not assume that new people bring good work habits to the table.

A Success Story

Recently, I talked to an electrical contractor whose work force expanded from 60 to 90 electricians and apprentices in less than a two-year period. While within my informal guideline of +30 percent per year, that's still a lot of hiring. This is precisely the kind of expansion that places an employer at high risk for bringing in marginal employees. Under normal circumstances, I would probably recommend that an insurer pass on this risk, but this particular contractor had handled the expansion with skill and foresight. In addition to a complete and thorough hiring procedure, management had integrated the new hires into work teams that were supervised by the best and most experienced managers. In the few instances when a new employee did not work out, management took action and terminated the employee immediately during the 90-day "probationary" period. This well-managed company was able to handle expansion cleanly and competently. It had plenty of work lined up, so it is now "right sized." This real-life example shows that expansion, while always risky, need not result in poor experience.

Shrinking the Business

If growing a company entails risk, shrinking one is an even riskier situation. Any company facing layoffs or widely fluctuating levels of employment is at very high risk for unanticipated losses. It's not hard to understand why. When an employee receives a pink slip, whatever loyalty he or she might have felt toward the organization is at risk. Depending on the local economy and the employee's transferable skills, an employee facing a layoff may see a bleak future indeed. Unemployment benefits usually end after 26 weeks, half a year, but workers compensation benefits can go on for many years. Faced with these realities, laid-off employees often find themselves in a "moral hazard" zone where there is a strong financial incentive to report an injury. Many workers — especially those in dying industries — have performed physically demanding or repetitive work all their lives. They often suffer from ailments that, while painful, did not prevent them from working. When faced with the prospect of their jobs ending, however, workers may find that the pain becomes more noticeable and the symptoms more agonizing. These long-term, loyal employees may well find themselves telling their stories to a sympathetic doctor.

In addition to the risk of claims being filed by laid-off workers, there is ongoing risk for the employees who remain behind. Retained employees experience the stress of watching their fellow workers pack up and leave. Often, they are asked to take on more and more work without any additional resources. Workers experiencing this kind of pressure are at increased risk for injuries.

Defining a Good Risk

Based on my experience, I have identified some characteristics that are common to good risks. These include:

- an experienced and competent crew whose members feel that they are a valued part of the team;
- good pay and benefits, to ensure that good workers are not lost to the competition;
- planned growth, with minimal fluctuations in the work force;
- a sense of shared pride in the work;
- subcontractors who mirror the organization's values and fit into the overall team; and
- a fundamental focus on the basics: good housekeeping, attention to detail, relentless attention to safety, and high standards in every aspect of the work.

Do-It-Yourself Underwriting

Regardless of how insurance underwriters view your organization, you need to approach the future with your eyes open. Ideally, you are "right sized" with an experienced work force that is stable and motivated. If you've had some injuries or near misses in the past few years, make sure you've integrated any necessary safety remedial actions and training follow-up into daily operations. If you fall into the minority of employers with no recent claims, take the time to review your post-injury management procedures so that you are fully prepared should an injury occur.

If expansion is on the agenda in the coming months, stay alert to the many hazards of hiring new people. Recognize that hiring strangers may be the most difficult and risky part of managing your business. Take the time to go through the proper steps to ensure that your hiring process has a good chance to succeed. Make sure your current employees welcome the newcomers. Above all, keep an eye on the new employees during their first days and weeks to make sure they have positive work habits and are doing their jobs safely.

If, on the other hand, you are facing potential staff cutbacks, take the time to do things the right way. If an employee files a workers compensation claim in the face of a layoff, manage the claim tightly. Alert your insurer's claims people to the layoff situation. Train your supervisors to follow every step in your post-injury response system. Finally, stay alert to the inevitable stresses on the workers remaining behind after the layoffs have been completed.

If you have a well-managed workers compensation program, you want to ensure that your agent — and any prospective insurer — is aware of your strengths. Make sure your agent is aware of your return-to-work program and good safety culture. If you've had a recent large loss but have taken definitive steps to prevent recurrence, document your corrective actions and make this documentation available to a potential insurer. This proactive communication will ensure that your workers compensation insurance is the best quality — and best priced — available.

Underwriting your own organization is a careful look at the past combined with a candid look at the road ahead. While it's important to recognize both your past successes and your failures, there is never cause for complacency. The future belongs to those who are best able to manage risk. And risk, like a roadway, is subject to constant change.

Jon Coppelman is a consultant in risk and human resource management with more than 15 years of experience. He has worked with both insurers and individual insureds to bring a best practice approach to injury management. Through his consulting, systems design, and training, he has motivated and educated more than 4,000 employers to take control of workers compensation. He divides his time between LynchRyan, a national consulting firm, and his own company, Coppelman Associates, which is based in Worcester, Mass. He can be contacted at *jcoppelman@hotmail.com*.