California Coalition on Workers' Compensation

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LEGISLATIVE & EDUCATIONAL FORUM

CONTROLLING WORKERS COMPENSATION COSTS THROUGH RESERVE OVERSIGHT

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CONTROLLING WORKERS COMPENSATION COSTS THROUGH RESERVE OVERSIGHT

- **Unmanaged Claim reserves inflate workers' compensation program costs**

- **Rigorous reserve & claim oversight reduces**
  - Severity
  - Loss Ratios
  - Decreases claim frequency

Workers' Comp Costs are not Soley Driven by Injuries

How claims are reserved and managed

- What are the reserve practices of your carriers/TPA's?
  - Stated Expectations in reserving practices
  - Requirements for your reserving practices
  - Regulatory vs. Corporate vs. Tradition vs. AI driven
- Unmanaged Reserves = Distorted Financial Exposure
  - What does Reserve Management look like?
  - Is there a reasonable rationale behind the reserving practice?
  - Are expectations clear, documented, communicated, audited, and revised?
  - Teaching good reserves in the age of AI reserving and AI oversight?
- Outcome
  - Long tail Impact
  - Artificially inflated or deflated loss ratios
  - Loss of expertise in "pricing" the real claim impact
- Solution: **Disciplined reserve oversight at many levels and proactive claims management will improve financial stability of the claims program**

WHY IT MATTERS:

- **Finiacial Impact of Poor Reserve Management**
  - Direct impact on Loss Ratios and Premium
  - Experience Modification Factor, EMR/Ex-mod trends and long-term impacts
  - Inaccurate premium collection, market volatility, financial impact on real businesses
- **Creates:**
  - Budget Instability
  - Hidden Liabilities
  - Capital Inefficiency
  - Poor reserve/claims practices impact program viability
- **KEY POINT:**
  - Reserves are not just account tools – they drive your total costs of risk
  - Inflated costs allocated for risk, are not able to be allocated for growth

How Reserves are Set (Structural Challenge)

- **Established Early in Claim Lifecycle with Limited Medical Clarity**
  - Initial Investigation (Three Point Contact and beyond)
  - Preliminary Diagnosis
  - Adjuster vs Examiner – Semantics Matter!
  - Expectations of your Risk Management Team – Not just "HR/Claims," All have a role to play CFO, CRO, etc.
- **Regulatory Deadlines**
  - Self-Insured Programs
  - High Retention Programs
  - Guaranteed Cost Programs
  - Captive Programs
  - Incurred but not Reported (IBNR)
- **Results:**
  - High Reliance on assumptions
  - Built-in margin for error – and error costs $$$
  - Significant opportunity for mismanagement and exposure

Components of Claims Costs - Reserves are built from three cost drivers:

- **Medical**
  - Treatment, surgery, therapy, meds, diagnostics
  - Are the reserves really outlines for each of these
- **Indemnity**
  - Wage replacement, disability, settlements
  - Are all documents collected to set correct benefit rates
  - Are realistic time periods being reserved, or “standard practice”
  - Has the insured been given an opportunity for RTW opportunities
  - Is the examiner having continuing communication with the insured to ensure financial oversight in TD/PD benefit delivery
- **Expense:**
  - Excluded from Ex-mod, but in Loss Ratio calculation
  - Legal fees, case management, administrative costs
  - ULAE – Costs of claims administration (per claims costs factored in)
  - ALAE – attorneys fees, SDT fees, investigation fees
  - Litigation management
  - Costs of litigation in CA are up nearly 50% since 2019 (WCIRB study May 2026)

The Core Problem: Unmanaged Reserves

What happens Without Oversight

- **Reserves Become:**
  - Inflated (Cushioning)
  - Reactive vs. Strategic
  - Poorly updated
  - Auditing procedure
- **Adjusters Operate**
  - Without employer input
  - Without accountability metrics
- **RESULTS: Artificial inflation of total program cost.**

The Unknown is unknown.

Key Failure Points

- **Inflated Experience Modification (Ex-mod)**
  - Over-reserving increased reported losses
  - Drives higher premiums for 3 recent policy years
- **Under-reserving Risk**
  - Leads to large unexpected adjustments
  - Disrupts financial planning
  - CFO's and Risk Managers don't like surprises
- **Lack of Transparency**

  Employers cannot:
  - Identify high-risk claims
  - Influence outcomes early
  - Calculate Risk
  - Average costs of Litigated indemnity claim: ~$88k (WCIRB study May 2026)
  - Where to hedge bets and C&R claims
  - Poor Precedents in settlements that negatively impact the employer in perpetuity
- **Legal Escalation**
  - Poorly managed claims -> Litigation -> Prolonged duration -> Higher reserves

Operational Red Flags

What to Watch for:

- Stair-stepping reserves (Frequent incremental increases) without rationale
- Large adjustments (>10%) without justification
- Reserves not aligned with medical progress
- High reserves late in the claim lifecycle

The Cost Cycle of Poor Reserve Management

Inaccurate Reserves

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Inflated Loss Ratios

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Higher Ex-mod

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Increased Premiums

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Reduced Capital for Operations

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Reactive Claims Handling

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Higher Claim Severity

The Solution: Rigorous Oversight - Shift from Passive to Active Claims Management

- Reserve Accountability:
  - Audit reserves, provide feedback, expectations communicated and reexamined
  - Authority Review of Reserving – What are the specified benchmarks, are they reasonable, do they make sense
  - Regulatory Compliance
- Structured Claim Reviews:
  - Active management of claims
  - Delegation and expectations of managing the risk
  - Accountability – If there is no accountability, there is no improvement
- Early Intervention:
  - What is the written, communicated method to ID potential high exposure incidents
  - Is this being applied and refined to remain effective
- Employer Engagement:
  - Participate
  - Informed
  - Educate
  - Invested
  - Active Management
  - **GOAL: Control severity first to influence total cost**

Strategy 1: Aggressive Return to Work (RTW)

- Provide light duty within 24-48 hours
  - Does your clinic know you offer modified duty?
  - Does your clinic have accurate, current job descriptions?
  - Do you ask for specific limitations, not just “Off Work”?
- Predefined Transitional Job Roles
  - Have a bank of pre planned jobs to fit many needs
- Have an effective Interactive Process (*HR – Non Delegable Task*!)
- Continue the Conversation through the claims and recovery process

IMPACT:

- Reduces indemnity reserves
- Prevents claims from becoming “lost-time”
- Shortens claims duration
- Best indicator of claim litigation prevention and inflated claim costs containment

Strategy 2: Structured Claim Reviews

- Do you know what your claims look like right now?
- Quarterly reviews with:
  - Medical management
  - Litigation management
  - Resolution management
  - Managing expectations of the injured workers
- 90-day review before Unit Statistical Data (Ex-mod)
- Monitor you own loss ratio = (Incurred Losses + Expenses/ Premium)
- Require documented action plans
- Involve your broker and learn “what you don’t know”
- How effective and invested is your safety committee – create “buy in”

IMPACT:

- Eliminates “padding” of reserves
- Partnership is cultivated, it’s not just a claim – culture changes
- Employees see proactive process for recovering employees – deters fraud & malingering
- Drives claim closure discipline

Strategy 3: Early Medical Intervention

- Direct Care to Occupational Providers – KNOW your clinics/providers
- Prepared Job Descriptions and Mod Duty Options for Clinics
- Pre-Authorized Treatments for Frequent Injuries
- Deploy Nurse Case Managers Early on Critical Cases
- Know the Health Culture of Your Employees.
  - What does treatment look like to them?
  - Find the Best Way to Accomplish That Ideal

IMPACT:

- Reduces unnecessary treatment
- Shortens recovery timelines
- Mitigates psycho/somatization of injures on injured employees
- Controls medical cost inflation

Strategy 4: Reserve Control Mechanisms

- Set Threshold Alerts at Specific Benchmarks (i.e. $10k, $25k, $50k, etc.)
- Require Employer Approval for Major Reserve Changes (+ or -)
- Audit Legacy Claims for Clear Management to Resolution

IMPACT:

- Prevents Arbitrary Reserve Increases
- Improves Financial Accuracy
- You “Know” the Cost of your Exposure

SEVERITY vs FREQUENCY MATRIX

Intervention	Impact on Severity	Impact on Frequency
Immediate RTW	Reduces indemnity	Converts to medical-only claims
Early Reporting of Claims	Limits escalation	Prevents fraudulent claims
Oversight of Claims Admin.	Eliminates excess reserves	Identifies repeat risks

MEASURABLE OUTCOMES – With Disciplined Oversight

- Claim Severity
- Loss Ratios
- Experience Mod
- Premium Volatility
- Litigation Rates
- Claim Frequency Over Time

☞ Compounding Financial Improvement Over Multiple Policy Years

IMPLEMENTATION ROAD MAP

PHASE 1: VISABILITY

- Gain Access to Reserve Data – Learn how to Use a Loss Run
- Lean into your Broker
- Identify High-Exposure Claims

Phase 2: Control

- Implement Review Cadence
- Establish Reserve Benchmarks and Corollary Actions

Phase 3: Optimization

- RTW Program Evaluation and Implementation
- Medical Network Alignment – Do you know your clinic?
- Continuous Audits

"When performance is measured, performance improves. When performance is measured and reported, the rate of improvement accelerates." - Thomas S. Monson

FINAL TAKE AWAYS:

- RESERVES ARE THE MOST CONTROLLABLE DRIVERS OF WORKERS' COMPENSATION COSTS
- UNMANAGED RESERVES DISTORT REALITY AND INFLATE PROGRAM COSTS
- DISCIPLINED OVERSIGHT TRANSFORMS OUTCOMES

BOTTOM LINE:

☞ CONTROL RESERVES -> CONTROL SEVERITY

☞ CONTROL SEVERITY -> REDUCE FREQUENCY

☞ REDUCE BOTH -> LOWER TOTAL COST OF RISK