

BOARD OF DIRECTORS MEETING (OPEN)

AGENDA ITEM 13a

ATTACHMENT 13a-I

CALIFORNIA COMMISSION ON HEALTH AND SAFETY AND WORKERS'
COMPENSATION (CHSWC) REPORT ON FRAUD RESEARCH

PRESENTED BY: CHSWC Executive Officer Christine Baker
and Workers Compensation Judge Lachlan Taylor

January 16, 2009



California Department of Industrial Relations
 Commission on Health and Safety
 and Workers' Compensation

CHSWC Report on Fraud Research
 State Compensation Insurance Fund
 San Francisco, CA
 January 16, 2009

Presentation by:

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 CHSWC Executive Officer
 Lachlan Taylor
 Workers' Compensation Judge

CHSWC Members

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Commission on Health and Safety and Workers'
 Compensation (CHSWC)

CHSWC Members:

- ✓ Appointed by the Governor and the Legislature.
- ✓ Represent employers and labor.

CHSWC's Mission is to:

- ✓ Oversee the health and safety and workers' compensation systems in California.
- ✓ Make recommendations for improvements.
- ✓ Conduct continuing examination of illness and injury prevention programs in California and other states.

CHSWC website: www.dir.ca.gov/chswc

Opinions of the speakers are not necessarily those of the Commission, the DIR, or the State of California.

Outline



The extent and varieties of WC fraud.

- Projects and studies
 - FAC medical payment accuracy study
 - Uninsured employers matching project
 - Underground economy
 - Access to coverage information
 - Under-reporting of injuries
 - Premium avoidance by insured employer
 - Split class codes, misreporting payroll
 - Insurance Commissioner's Task Force
- Conclusion

WORKERS' COMPENSATION IN CALIFORNIA

- Nearly 700,000 workplace injuries are reported every year in California.
- The cost to California employers was about \$17.6 billion in 2007.
- How much is due to fraud and abuse?

Measuring Anti-Fraud Return on Investment and Effectiveness

The California State Auditor Report on Workers' Compensation Fraud published in 2004¹ reported that:

- The Fraud Assessment Commission assessed and distributed over \$30 million a year to fight fraud.²
- Without measurements of fraud, the effectiveness of investments in fighting fraud could not be evaluated.
- Efforts to detect and prevent workers' compensation fraud need to be adequate.
- Cooperation between agencies to improve efforts to detect and prevent workers' compensation fraud is critical.

¹ <http://www.bsa.ca.gov/pdfs/reports/2002-018.pdf>
² it will be nearly \$50 million for 2009

Fraud in Workers' Compensation

Fraud takes many forms. To name a few...

- Claimant – false claim of injury, exaggerated claim of disability
- Medical provider – false reports, false bills, unnecessary treatment
- Employer/Insurer – false statements to deny payment of benefits
- Broker – embezzlement, conspiracy with employer
- Employer – under-reporting of payroll, misclassification of payroll, shell companies to avoid accurate experience modified rates
- Uninsured employer – willful uninsurance is grouped with fraud

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WORKERS' COMPENSATION MEDICAL PAYMENT ACCURACY STUDY

The Fraud Assessment Commission, with staffing furnished by CHSWC and with the cooperation of many insurers and employers, contracted with Navigant Consulting to conduct a study:

- Determine the extent of workers' compensation medical overpayments and underpayments of all types in order to allocate the appropriate level of resources to detect and evaluate suspected medical provider fraud in California.
- Develop baseline measurements for medical overpayments and underpayments of all types including suspected fraud, waste, abuse, billing and processing errors.

WORKERS' COMPENSATION MEDICAL PAYMENT ACCURACY STUDY

Approach of the study:

- Identify the extent of workers' compensation cases where medical provider over-payments and underpayments of all types exist, including mis-diagnosis, documentation errors, over-billing, medically unnecessary services.
- Review a sample of workers' compensation bills and supporting documentation for medical services paid by insurance carriers and claims administrators, as well as conduct a survey of injured workers to verify that they received these services.
- Identify the cost impacts.

**WORKERS' COMPENSATION MEDICAL
PAYMENT ACCURACY STUDY**

Findings:

- 21.9 percent of the sample dollars were paid in error (combined three reviews analysis).
- Total potential payment errors in the entire California workers' compensation system range from \$494 million to \$1,372 million (combined three reviews analysis).

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**UNINSURED EMPLOYERS MATCHING
PROJECT – CHSWC pilot leads to Labor
Code 90.3**

- Illegally uninsured employers impose substantial costs on the State of California, its employers and workers.
- Funding for the UEBTFF comes from an assessment on employers, \$33 million for 2009.
- CHSWC pilot in 1988 matched EDD records to WCIRB records, found 8.6% of employers uninsured, almost 20% in some industries.

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UNINSURED EMPLOYERS MATCHING PROJECT

Labor Code 90.3 directed Labor Commissioner to establish program based on CHSWC demonstration.

SB 869 in 2007 amended statutes so the program could become operational.

Program launched by DLSE in 2008. Early results suggest that 15% of employers are illegally uninsured.

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UNINSURED EMPLOYERS IN THE UNDERGROUND OR "GRAY" ECONOMY

- Underground or "gray" economy employers may represent a major fraction of the uninsured employer population.
- These employers may only be detected during the process of obtaining jurisdiction for Uninsured Employer Benefit Trust Fund (UEBTF)* workers' compensation cases.

* still commonly called the "UEF"

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UNINSURED EMPLOYERS IN THE UNDERGROUND OR "GRAY" ECONOMY

The purpose of the study will:

- Estimate the employers uncovered for workers' compensation and reporting to neither the workers' compensation nor the EDD system.
- Estimate the proportion of injuries in the "gray" economy.

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UNINSURED EMPLOYERS OPERATING IN THE UNDERGROUND OR "GRAY" ECONOMY

The approach of the study will:

- Analyze employers with claims in the UEF who are uninsured, but who are reporting employment to EDD.
- Calculate the percentage of UEF uninsured claims where employers did not report employment to EDD.
- Estimate uninsured employers in the "gray" economy.

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**ACCESS TO WORKERS'
COMPENSATION INSURANCE
COVERAGE INFORMATION**

- Workers' compensation coverage is required by law.
- DLSE is tasked with enforcing the statute.
- Past studies using sampling methodologies have found nearly 9% of employers at large, and nearly 20% in select industries, to be illegally uninsured.
- This creates an uncompetitive environment for employers, places injured workers at risk, and distorts premium pricing.

**ACCESS TO WORKERS'
COMPENSATION INSURANCE
COVERAGE INFORMATION**

Findings:

- The WCIRB rating bureau is the only entity that maintains coverage information for all employers insured by a carrier.
- The Office of Self-Insured Plans (OSIP) at DIR maintains coverage information for all self-insured employers, and publishes those records publicly on its website.
- Only "parties to a claim" may request coverage verification information from WCIRB through a paper-based, fee-based process.
- DLSE, DIR's Legal Unit and the CDI Fraud Unit have electronic access to coverage information for enforcement and prosecutorial purposes.
- The Contractor's State Licensing Bureau provides workers' compensation coverage information, as part of the licensing information via a public website.

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**ACCESS TO WORKERS'
COMPENSATION INSURANCE
COVERAGE INFORMATION**

Findings:

Public access to coverage information can:

- Deter employers from risking detection as illegally uninsured.
- Empower injured workers with information when employers balk at providing statutorily required information and forms.
- Speed up the process for contacting the correct adjuster, or adjusters when applicable.
- Deter broker fraud.
- Add a layer of suspected fraud detection, and allows for immediate awareness of mistakes to make any correction of information.

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ACCESS TO WORKERS' COMPENSATION INSURANCE COVERAGE INFORMATION

Findings (updated):

- Since the CHSWC report was issued in 2006, the number of states that have an online coverage website has risen to 29.
- At the time of the research in 2005, the 17 states with a coverage website did not report any complaints from industry or stakeholders.
- Assembly Bill (AB) 507 proposed a website requirement. Governor vetoed in 2008, saying that the website was laudable but that he was "concerned that the website would not be required to post the effective dates of coverage of a policy, thereby significantly diminishing the value of the information. More importantly, the bill does not contain any specified timing in which the information must be updated, potentially leading to inaccurate information on the website."

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UNDER-REPORTING OF INJURIES

Under-reporting of occupational injuries and illnesses:

- May occur in response to increases in premium costs.
- Is often proposed as a partial explanation for the continuing decline in occupational incidence rates.

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UNDER-REPORTING OF INJURIES

Approach:

- Capture-recapture estimates of under-reporting using the Survey of Occupational Injuries and Illnesses conducted annually by the Bureau of Labor Statistics (BLS) and State workers' compensation data (WCIS).



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UNDER-REPORTING OF INJURIES

Findings:

- The most conservative estimate of reporting of workplace injuries in California suggests that 21 percent to 25 percent of lost-time injuries go unreported to WCIS. A less conservative estimate of underreporting implies that 40% of lost-time injuries went unreported.
- Reasonable alternate scenarios allow for the likelihood that reporting an injury to BLS increases the likelihood that it will be reported to the WCIS. Under these circumstances, researchers estimate that only about 2/3 of injuries are reported to WCIS. This incomplete reporting places California in the middle of the seven states researchers studied.

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MISREPORTING PAYROLL AND PREMIUM AVOIDANCE BY INSURED EMPLOYERS

Purpose of the study:

- Examine the reporting behavior of employers' reported exposure compared to premium rates in order to determine possible trends and relationships in under-reporting/misreporting.
- Examine self-insured employers' reporting behavior for any differences with insured employers.
- Describe reporting behaviors in low risk, low premium classes and high risk, high premium classes, at different premium rate levels in history.
- Determine the extent of under-reporting.

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PREMIUM AVOIDANCE BY INSURED EMPLOYERS

Approach:

- Analyze changes in reported exposure and premium rates over time, by different employers and by different risk and premium classes, using WCIRB data.
- Analyze whether misreporting changes relationships between exposure and premium rates, by comparing reported wages from the Current Population Survey, a Census Bureau survey conducted for the Bureau of Labor Statistics, with WCIRB reported payroll exposure.
- Analyze the extent to which X-mods correct for misreporting.

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PREMIUM AVOIDANCE BY INSURED EMPLOYERS

Findings:

- Substantial misreporting of payroll in jobs where the employer pays high workers' compensation premium rates.
- The under-reporting becomes increasingly more severe as the cost of workers' compensation increases.
- From 1997 to 2002, the level of underreporting of private industry payroll increased from 6-10 percent when premium levels were low (\$2.47/\$100 payroll) to 19-23 percent when premium levels were high (\$4.26/\$100 payroll).
- This translates to a change from \$19.5 - \$31.3 billion in 1997 to as much as \$100 billion in under-reported payroll in 2002.
- Under-reporting and misreporting increase as the premium rate for a class of workers increases. For very high-risk classes, as much as 65 percent to 75 percent of payroll is being under-reported or misreported.

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SPLIT CLASS CODES

- Some classes are "split" because payroll does not correctly measure exposure for workers doing same jobs with very different pay.
- Employers may cheat by reporting correct amount of payroll but reporting it in the higher-paid class, where premiums as a percent of payroll are lower.
- If mis-reporting of class codes is prevalent, rates become higher for higher-wage employees, and honest employers are subsidizing dishonest employers.

SPLIT CLASS CODES

Purpose of the study:

- Determine whether employers are misreporting lower-wage workers in class codes specifically designed for higher-wage workers.
- Determine the level that employers with high-wage workers are subsidizing the workers' compensation costs to employers for low wage workers.

SPLIT CLASS CODES

Approach:

- Evaluate the payroll reporting by firms against payroll reporting by individual employees, using WCIRB data and data from the Current Population Survey (CPS).
- Analyze the differences, if any, between reported aggregate payroll relative to true payroll in the split classes (high wage vs. low wage).
- Examine data for all monthly CPS surveys for the years 1996-2002.

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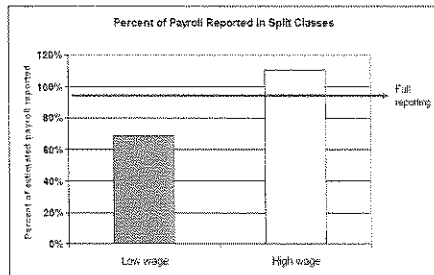
SPLIT CLASS CODES

Findings:

- 25 percent to 30 percent of low-wage payroll is being under-reported or being misreported in a higher-wage class.
- Reported payroll in the higher-wage class is about 10 percent higher than actual payroll and 14 to 18 percent higher than expected reporting for premium purposes.

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SPLIT CLASS CODES



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INSURANCE COMMISSIONER'S ADVISORY TASK FORCE ON INSURANCE FRAUD

Commissioner Steve Poizner convened a task force in 2007.

The Executive Officer of CHSWC was asked to chair the workers' compensation working group.

The Workers' Compensation Working Group made the following recommendations to the Advisory Task Force:

- Require employers to publicly disclose their workers' compensation coverage.
- Require the Insurance Commissioner to publish the workers' compensation coverage of every employer.

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INSURANCE COMMISSIONER'S ADVISORY TASK FORCE ON INSURANCE FRAUD

- Increase civil and criminal penalties for premium fraud, including misclassification of payroll and under-reporting of payroll.
- Increase civil and criminal penalties for willful failure to carry insurance. Existing law allows under-reporting to be punished as a felony, while being uninsured is only a misdemeanor. The law should allow willful lack of insurance to be charged either as a misdemeanor or as a felony.
- Review the cost benefit of requiring carriers, third-party administrators, and self-insured entities to send a statement of benefits document to patients to verify that services were actually rendered and the extent of those services and to include information on where and how to report suspected fraud.

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INSURANCE COMMISSIONER'S ADVISORY TASK FORCE ON INSURANCE FRAUD

- Conduct additional research on: (1) the misuse of "independent contractor" designation; (2) coverage fraud in temporary help and professional employment agencies; (3) medical billing practices; and (4) methods to require greater disclosure of employer coverage information.

The Task Force report "Reducing Insurance Fraud in California" was issued in May 2008.

<http://www.insurance.ca.gov/0300-fraud/upload/FraudTaskReport05-08.pdf>

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Conclusion

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ROSTER OF FRAUD STUDIES

- Workers' Compensation Medical Payment Accuracy Study (Navigant Consulting, Catherine Sreckovich, 2008)
- Uninsured Employers Matching Project. (UC-Berkeley, Frank Neuhauser, December, 1998)
- Uninsured Employers in the Underground or "Gray" Economy (UC-Berkeley, Frank Neuhauser, TBD)
- Under-Reporting Injuries (Boston University, Leslie Boden, 2008)
- Misreporting Payroll and Premium Avoidance by Insured Employers. (UC-Berkeley, Frank Neuhauser, August 2007)
- Misreporting Payroll for Split Class Codes and Premium Avoidance (UC-Berkeley, Frank Neuhauser, August 2007)
- Access to Workers' Compensation Insurance Coverage Information (CHSWC Staff, 2006)

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CHSWC, FAC and CDI PARTNERSHIP

Through these and future research studies, CHSWC, FAC and CDI will try to continue to partner to:

- Develop baseline measurements to detect the level of fraud in the workers' compensation system.
- Coordinate efforts to detect and prevent workers' compensation fraud.
- Potentially reduce the overall cost that fraud adds to the workers' compensation system.

These studies intend to benefit all members of the workers' compensation community.

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Are we doing enough?

\$50 million assessed and distributed by the FAC is about 1/4 of 1% of spending on workers' compensation.

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CHSWC website
www.dir.ca.gov/chswc

- ✓ Reports of CHSWC studies and projects
- ✓ Information bulletins
- ✓ Meeting notices and minutes
- ✓ Workers' Compensation Fact Sheets and Guidebook

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