
The Significance of Experience Rating

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THE SIGNIFICANCE OF EXPERIENCE RATING

BY TERENCE G. ISON*

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I. EXPERIENCE RATING

A. *Introduction*

In the contemporary context of workers' compensation in Canada, there is probably nothing that is so fervently supported or so little understood as experience rating. Proposals for the widespread expansion of experience rating have been made and adopted, yet with no analysis

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of the consequences and with no reasons being given that could withstand serious reflection. It is as if a political steam-roller has made the widespread expansion of experience rating a part of inevitable destiny regardless of the consequences. In this climate, any questioning of the movement might be seen as irrelevant, perhaps even recalcitrant. Nevertheless, the aim of this paper is to contribute to an understanding of the significance of experience rating.

Our workers' compensation systems derive their primary revenue from assessments levied on employers. For calculating the amounts, the boards use an industrial classification system that allocates each employment to a class and often to a sub-class or rate group. A standard rate for that sub-class or group is established annually and expressed in terms of a dollar amount per one hundred dollars of payroll, with a maximum per worker. Where an experience rating plan is applied, the rate of assessment for each employer may be higher or lower than the standard rate for the sub-class or rate group. The variation is made pursuant to a formula which reflects the claims cost experience of the employer, though it may also reflect other factors. For example, there may sometimes be a frequency component in the formula. Also, an average or standard figure may be used for fatal cases instead of the actual cost. For the most part, however, experience rating means that the assessment payable by each employer is subject to annual variation above or below the standard rate for the sub-class or group by reference to the claims cost experience of that employer.

Experience rating is often referred to as a species of 'merit rating,' and the formulae that are used commonly refer to 'merit' and 'demerit' points. However, these terms are misleading. Experience rating does not reflect any mode of measuring any type of merit.

Exactly why a demand for the expansion of experience rating has been in vogue among corporate organizations is not entirely clear. It may be credible, however, that part of the explanation could lie in a false impression that employers have received from the figures supplied to them by some of the boards. In at least some jurisdictions, an employer receives a cost statement, often monthly, which shows the direct compensation costs, including medical aid costs, paid by the board in respect of each employee or former employee of that employer. The statement does not, however, show any apportionment of the other costs incurred by the board. For example, it may not include any apportionment of the cost of health and safety programs, rehabilitation services, allocations to the Second Injury Fund, the disaster reserve or other reserves, the administrative overhead, or any allowance for inflation in respect of future

benefits for past claims.¹ Thus, if a company compares what appears from the cost statement to be the aggregate cost of the claims of its employees with the aggregate amount being paid by the company in assessments, it may well appear that the company is paying far too much. Moreover, this will appear to be the case for most employers. The truth may well be that the real aggregate cost attributable to the company could be equal to or greater than the aggregate amount that the company is paying in assessments.

There is no doubt that many employers are under the impression that they are paying far too much in relation to the costs attributable to them, and false impressions drawn from these cost statements may be part of the explanation. Moreover, if the majority of employers believe that they are paying relatively too much in assessments, the belief would logically follow that some other employers are paying relatively too little, and this may well help to explain the demand for an expansion in experience rating.

B. *Claims Control*

Since experience rating involves the variation of an employer's rate of assessment by reference to recorded claims cost experience, it creates an incentive for the company to reduce its recorded claims cost experience. The easiest way of doing this will usually be by a program of claims monitoring and control.

The claims control practices that seem to be used most frequently are commonly legitimate. Probably the main form of control is for an employer to protest a claim or the continuation of benefits, or to appeal claims decisions. Unfortunately, there seems to be an increasing danger of employer protests becoming a normal routine, and hence reintroducing into workers' compensation the delays, the costs, and the therapeutic damage of the adversary system. Incidentally, in my experience as chairman of the Workers' Compensation Board in British Columbia during the years 1973-76, employer opposition to claims was rare except in classes covered by experience rating, or among those that were self-insured.

Of course the monitoring of claims by employers is not always injurious. Like so many things in life, a certain amount of it can be beneficial while too much of it can be damaging. The problem with current systems of experience rating is that they promote the monitoring

¹ Obviously, the cost statements should include an apportionment of these figures.

of claims by employers without creating any incentive to stop at the right amount.

Some of the more objectionable practices that have been adopted to reduce recorded claims cost experience include the following:

1. Discouraging workers from reporting claims.

2. Refusing to complete a Form 7 (employer's report to the W.C.B.) when requested to do so. This can be particularly important in Ontario where the Form 6 (worker's report to the W.C.B.) is not generally used and is commonly unavailable to workers.

3. Adopting a gimmick type of safety program which creates incentives for lower levels of management, or perhaps even for workers, to reduce recorded claims, possibly by creating peer group influence not to make a claim.

4. Delaying the completion of forms or omitting relevant information, thereby causing delays in the processing of a claim, perhaps causing the worker to turn to other sources of income.

5. Other practices mentioned under the headings that follow.

The extent of these nefarious practices is unknown, but they are not rare events. Also the first attempt at any survey work on this confirms that these practices tend to be associated with experience rating.² Moreover, it would be unrealistic to suggest that where experience rating is used, these practices can be prevented by any kind of policing activity.

Perhaps a solution that might seem ideal would be to recognize that while experience rating is of no use for safety purposes, it could have some beneficial influence on claims adjudication by encouraging employers to take an interest in claims, and to supply information to the boards. If this goal were to be sought, however, without risking the negative consequences mentioned in this article, the rate variations would have to be very small.

There are two basic problems with this idea. One is that as a matter of practical politics, this type of experience rating program would not be adopted. Secondly, even if adopted, it would be open to the objection that, like present experience rating plans, it would create an incentive for employers to provide only adverse information. One would think that fairness to workers should require employers to be under an equal incentive to provide any positive information, particularly when the information is of a type that is not readily available to workers.

Another possibility might be to allow an assessment credit wherever an employer provides any substantial information to the board beyond

² C. Walker, "A Labour Perspective" (Third Annual Workers' Compensation Conference on Experience Rating: Incentive or Disincentives, 16-17 September 1986) (Toronto: Corpus, 1986).

the basic requirements of the Form 7. It is doubtful, however, whether this would be practicable.

C. *The Influence on Health and Safety*

The argument most commonly used to justify experience rating is that it will promote occupational health and safety by providing an incentive to care. There is no difficulty in finding superficial support for that view.³ It is assumed and asserted that the variation of assessment rates by reference to the safety performance of the firms concerned will create an incentive to improve the safety performance. Of course if the rates really were being varied by reference to safety performance the conclusion would follow; but as explained above, that is not the case. Rates are varied by reference to claims cost experience and other claims data, and variations in these figures will commonly have nothing to do with safety performance.

Thus it is no surprise that in spite of decades of discussion on this subject, there is no empirical evidence to support the view that experience rating really does create an incentive to care. Indeed, such empirical evidence as there is suggests the contrary. The conclusion, with regard to safety performance, is that: "It appears, then, that experience-rating, or the lack of it, in workers' compensation has no observable effect on employer behavior."⁴

Part of the explanation is that accidents involve a cost for employers that is probably far in excess of workers' compensation assessments. There is, therefore, another economic incentive for the prevention of accidents that is more significant than experience rating; and that is probably enough to induce most employers to adopt the easy ways of reducing accidents, regardless of experience rating. If a company is not adopting further measures, it is probably because they would involve a high cost, and sometimes because their adoption might make the business uneconomical. Where that is so, a marginal shift in the workers' compensation assessment rate is not going to produce an improvement.

Another difficulty is that many and perhaps even most occupational disabilities result from disease rather than trauma, and with regard to the more serious diseases, experience rating can be of no benefit. These involve long latency periods, commonly in the range of 10 to 25 years,

³ See, for example, *Report of the Royal Commission on the Economic Union and Development Prospects for Canada*, vol. 2 (Ottawa: Minister of Supply and Services Canada, 1985) at 728.

⁴ J.R. Chelius & R.S. Smith, "Experience-Rating and Injury Prevention" in J.D. Worrall, ed., *Safety and the Work Force: Incentives and Disincentives in Workers' Compensation* (Ithaca: ILR Press, 1983) 128 at 136.

so that any incentive to care that depended upon claims' cost experience would be a long time in coming. Also serious disease cases often involve difficulties in attributing the etiology of the disease to employment with any particular employer. For these and other reasons, some experience rating plans omit claims for disease. Thus if experience rating had any influence at all on health and safety, it could be only to divert attention to physical hazards and away from the control of toxic contamination.

The historical use of experience rating might be another indicator of its significance. Experience rating has been associated with high levels of risk and with relatively high rates of assessment. For example, in British Columbia, health and safety problems have been endemic in the forest industry, in mining, and in construction; the same classes of industry to which experience rating has been applied for decades. Of course this does not prove that experience rating has been of no benefit, or that it has been harmful, but it contributes to a certain skepticism.

Also, despite decades of experience rating for certain classes of industry, there has never appeared a real conviction within the boards that it has had any beneficial influence on health and safety. This lack of conviction appears from the decisions relating to the classes of industry to which experience rating is applied. It has generally been applied only to classes of industry in respect of which there has been a request from an employers' organization or a vote among the employers to have experience rating. The boards have simply acquiesced in the wishes of employers or their organizations. If there was any conviction that experience rating really did have a beneficial influence on occupational health and safety, one might have expected that the boards would have applied it to all classes years ago and regardless of employer wishes.

Even the theoretical argument involves a *non-sequitur*. If the assessment rates payable by employers are varied by reference to the recorded claims cost experience of each employer, that obviously creates an incentive to reduce the recorded claims cost experience. There are several ways of doing that, some of which have already been mentioned, that are probably easier and cheaper to adopt than any further measures for the improvement of health and safety.

The assertion that experience rating has a beneficial influence on occupational health and safety, or at least on safety, is contrary to the evidence and unsupported by logic. Moreover, the position is worse than that. Experience rating probably has *negative* influences on health and safety. For example, if a rate variation really is wide enough to have a significant impact upon an employer, a possible reaction may be to contract out some of the more hazardous types of work. When this happens, the work may be undertaken by smaller employers or independent

operators who lack the technical knowledge or the capital to use the safest methods and equipment, and who may operate under competitive pressures to incur greater risks.

Another perverse influence that experience rating has on health and safety relates to the use of statistical data. The common assumption that experience rating promotes safety assumes and asserts a correlation between claims data and accidents. Invariably in the literature of experience rating, claims data are used as if they were incidence data. Even in government publications, claims data are often used to produce "accident rates" without any apparent recognition that the data show no such thing. Also, the adoption of an experience rating program may require, as a matter of practical politics, the adoption of a theory or mythology that will justify its existence. That mythology is one which assumes a correlation between claims data and the incidence of accidents. Such a correlation will never exist exactly, and the extent of the deviation will never be known. The crucial point, however, is that experience rating itself creates an incentive to reduce the recorded claims experience, and it is almost bound to increase the deviation between accidents and recorded claims. Hence experience rating creates a demand for claims data to be used as if they were accident data while at the same time it makes them infinitely less reliable for that purpose. Moreover, since other programs of accident prevention commonly have no statistical data base except for claims figures, experience rating tends to promote distortions in the data base that is most commonly used for other programs of accident prevention.

There is another way too in which experience rating can have a negative influence on health and safety. Experience rating encourages a company to compare its rate of assessment with the standard rate for the sub-class, or with the rates being paid by other companies. If senior management believe that this comparison is a measure of safety performance, it may be seen as a rough measure of the efficiency of the company safety officer. Since claims costs can often be reduced more readily by the monitoring of claims than by measures to reduce risk, a company safety officer may be encouraged to spend time on claims monitoring rather than on safety activity. Indeed, in companies that have been subject to experience rating, it has not been too unusual to find a company safety officer spending more time in the claims division of a compensation board than he could possibly be spending on any safety activity. This is understandable. As well as the incentive of experience rating, part of the explanation is that the background and status of a company safety officer, as well as the economic and political pressures, make it easier for him to deal with workers than with senior management.

To the extent that he deals with safety matters, a typical company safety officer does not have the status or engineering background, or the authority within the company, to give direction to senior management with regard to the key determinants of risk (for example, plant location, plant design, choice of product, choice of materials, choice of equipment, *et cetera*). A company safety officer does, however, usually have a measure of status and authority to deal with workers and with lower levels of management. Hence, any safety activity may be focused on exhortation to these groups, including the use of personal protective equipment. Since the response to experience rating is considered a matter for the company safety officer, it may in this way tend to divert attention away from the ways of improving safety performance that have the greatest potential and towards those that are the least efficient.

D. *The Therapeutic Significance*

As mentioned above, experience rating encourages employers to establish routines for the scrutiny of every compensation claim. The incentive created, however, is not for an impartial scrutiny or open-ended enquiry, but for a partisan scrutiny. Experience rating creates an incentive to develop only negative information to disallow or to minimize a claim. These routines with this motivation are almost bound to generate within the company attitudes of suspicion towards claimants, and such attitudes are likely to be sensed by claimants. They cause anxiety and resentment, and their impact on the vulnerable psychological state of an injured worker can increase the gravity of a disability.

Related to this, the system must obviously include the detection and investigation of fraud; but if therapeutic damage is not to be inflicted upon legitimate claimants, the prevention of fraud must not be sought through a program that results in all claimants being treated with suspicion. The monitoring for fraud should be done by people who have an incentive, or at least a duty, to distinguish fraudulent from legitimate claims, not by people upon whom there is imposed an economic incentive to defeat or minimize any claim, however legitimate.

By promoting more suspicion and challenge in relation to claims, experience rating can also increase the number of physicians by whom a claimant is examined, again with therapeutic harm. Indeed, it is well recognized in medical literature that an unnecessary increase in the number of physicians by whom a patient is examined is a cause of psychological damage, and sometimes even of physical harm.⁵

⁵ For further discussion of this, see T.G. Ison, "The Therapeutic Significance of Compensation Structures" (1986) 64 Can. B. Rev. 605.

It may help to reflect on what commonly happens in a fairly typical bad back case. Consider the example of a worker who is 48 years old and has worked for the last 30 years in heavy industry. He may well be an immigrant who is not entirely fluent in English. In any event, he does not have the educational background or training for office work. The physique of the worker was never above average in the first place, and he finds it increasingly difficult to cope with heavy manual work.

The accident happens. When making a lift, the worker suddenly feels an excruciating pain in the back. There is no obvious cause, and the pain continues after the load has been dropped. The worker feels crippled and may even have a fear of paraplegia. He feels that his capacity to earn a living in the only way that he has ever known is threatened. Work-mates are bewildered. There is nothing visibly wrong and they can offer no comfort. Someone, perhaps the foreman, perhaps a company doctor, tells the worker that it's nothing serious and that after a rest he will soon feel better; but the worker knows that this opinion does not reflect any diagnosis, and for that reason, it is not reassuring. The reaction at home may be sympathetic or resentful, but either way, it offers no solution to what the worker sees as a crisis in his life. That night, and on successive nights, the pain is aggravated by muscle spasms, and even when the spasms abate, the pain continues.

In the ensuing days or weeks, some people, perhaps at the company or at a workers' compensation board, begin to treat the worker with suspicion. Even the attending physician, who may be well disposed towards him, only seems to offer modest suggestions for treatment, with no clear diagnosis and no promise of cure. At the same time, any recreational activity is in suspense and social life is impaired.

The compensation claim then becomes more controversial and more adversarial. The workers' credibility is questioned, perhaps by a company official or perhaps by a board doctor. Meanwhile, the worker is convinced that his disability needs more recognition and a better response than it is receiving. Understandably, the worker begins to exaggerate his symptoms. Comments about "functional overlay" then begin to appear on the claims file, and the worker recognizes that some people in authority are coming to perceive of his problem as primarily psychological. This adds to his anxiety and resentment for four reasons:

1. It is an ill-informed and insinuating response.
2. It seems like the introduction of an excuse to terminate compensation benefits and leave the worker in financial despair.
3. It seems to indicate the abandonment of any attempt to identify an organic cause of the disability, and thus seems to import also the abandonment of any hope of cure.

4. Labelling the condition as wholly or partly psychological is a stigma that could prejudice the future employment prospects of the worker.

Partly for these reasons, the ostensible diagnosis of "functional overlay" adds to the anxiety, aggravates the pain, and tends to entrench the disability.

We then have the classic bad back patient who sees himself, perhaps correctly, as the victim of a serious disability, of professional ineptitude, and of a gross injustice.

Of course this classic syndrome is not caused wholly or primarily by experience rating. A primary cause is the difficulty of diagnosis in bad back cases. Another cause is our failure to develop a system of alternative employment opportunities for people who have reached a stage in life at which heavy manual work has become too much for them. Nevertheless, a significant contributing cause is the suspicious attitudes and the adversarial postures that experience rating tends to promote.

What is usually needed in these bad back cases is a solution to the problem. Experience rating tends to stimulate only aggravations.

Much of the concern relates to the impact of experience rating on the practice of occupational medicine. If a company doctor is playing an active role in diagnosis and treatment, the judgments made in this process will inevitably have an impact on compensation costs. If the company is on experience rating, it would not be unnatural if at least some people in some companies should harbour the expectation that the company doctor will rank it as one of his responsibilities to reduce compensation costs as much as possible. Indeed, some company doctors appear to adopt that view, and to proclaim the guarding of corporate finances as their primary role, rather than the guarding of workers' health.⁶ If a company doctor is concerned about the cost of disabilities to the company, this may well add to the anxieties of patients, and it may tend to result in patients being treated with the suspicious attitudes that promote chronic pain syndrome.⁷

Experience rating can also lead to breaches in the confidentiality of the relationship of doctor and patient. Since the company has an interest in the return of an injured worker to work as soon as possible, it also has an interest in questioning the gravity of a disability. Thus, in industries that are on experience rating, it is fairly common for someone in the company to communicate with the attending physician to inquire about

⁶ See for example, *Brief of the Occupational Health Section of the O.M.A. to the Task Force on the Workmen's Compensation Board of Ontario*, 23 May 1973.

⁷ See for example, L. Keiser, *The Traumatic Neurosis* (Philadelphia: J.B. Lippincott, 1968) at 69 and Ison, *supra*, note 5.

the gravity of the disability and often to suggest a return to light work. If this is done in the presence and with the approval of the worker, it can be a constructive move in rehabilitation. However, where it is done behind the back of the worker, it can be another cause of anxiety, and hence of therapeutic damage. In any event, it can impair the confidentiality of medical information.

E. *The Influence on Rehabilitation*

The influence of experience rating on rehabilitation is also dubious. It can provide an incentive to employers to offer further employment to disabled workers, but even this can be counter-productive, particularly in cases involving a significant and long-term disability. If experience rating creates a pressure to provide future employment for a disabled worker, that pressure is applied only for a limited time. The estimated future cost of each claim is capitalized within two or three years of the date of injury and charged to the class funds. Thereafter, the future employment of that worker will not be reflected in the rate of assessment payable by the employer. Thus, if an employer has provided future employment only as a response to the influence of experience rating, there is an obvious risk that the employment may not last much beyond the time when the claim is capitalized at the board and that influence comes to an end.

Moreover, experience rating lacks the sensitivity to distinguish between genuine and phoney rehabilitation programs. Thus, in industries that are on experience rating, there is episodic evidence of unsavory practices, including:

1. Keeping people on the payroll who were injured at work, even though they are not reporting for work, and failing to report the injury to the W.C.B. (This can create a problem in establishing a claim if the injury does not heal).

2. Pressing claimants to return to work too soon.

3. Requiring claimants to report for work as a form of harassment or degradation when there is no work available that they are fit to do.

4. Creating "light work" programs which do not involve genuine work at all, or which only involve work that is unsuitable for the condition of the claimant.

5. Pressing an attending physician to certify a claimant "fit for light work."

Where these practices have been found or alleged, it has usually been in industries that are covered by experience rating or that are self-insured.⁸

⁸ See *supra*, note 2.

Some rehabilitation programs are not clearly genuine or phoney but somewhere between the two. Senior management may be well motivated in introducing a rehabilitation program that is intended to be genuine, and it may have support within the company from those with primary responsibility for rehabilitation. When an injured worker returns to work, however, the supervision is by junior line management personnel who may be unsympathetic to the program and reluctant to recognize the limitations on the activity of the worker that recovery from the injury requires. This can be particularly noticeable where the rehabilitation of the worker requires his transfer to another department of the company.

Also for optimum success, a rehabilitation program must be one that has the confidence of the worker, and this may be hard to promote if the worker knows that the employer has a financial interest in a rehabilitation proposal which is different from and may conflict with the interest of the worker. There is then an obvious risk that the worker will feel that he is being manipulated. He may suspect that the employer's judgments on such matters as the suitability of particular work to the condition of the worker are being made in the interest of the employer rather than in the interest of the worker. The confidence of the worker, which is so important to sound rehabilitation, is most likely to be inspired when an employer has no conflicting or potentially conflicting interest.

Of course it does not follow that financial incentives should never be used for rehabilitation. The point being made is that experience rating is too clumsy and insensitive for this role. Financial incentives for rehabilitation should be planned carefully for that purpose, and usually planned for the circumstances of a particular case.

Even if experience rating has any beneficial influence with regard to further employment with the injury employer, it can have a negative influence with regard to the prospects of future employment with other employers. This is particularly so in bad back cases. In industries that are on experience rating, the compensation claims records of applicants for employment are often a matter of concern to potential employers. With an expansion of experience rating, one would expect an expansion in the enquiries made by potential employers about previous W.C.B. claims by job applicants. This practice can be a negative influence on the hiring of people who have claimed workers' compensation.

F. *Equity Among Employers*

The strongest argument for experience rating is that it might achieve a more equitable distribution of cost among employers. It can help to enhance the industrial classification system in providing that companies

operating at higher levels of compensation cost pay proportionately more than those operating at lower levels of compensation cost. Even here, however, there is cause for concern. First, the lower levels of cost may be achieved in ways that are unrelated to the risk of injury or to genuine rehabilitation, and as mentioned above, experience rating rewards the anti-social ways of reducing cost as well as the beneficial ways. Moreover, since there are other incentives to adopt the beneficial ways of reducing cost, experience rating is more likely to promote the anti-social methods.

Secondly, experience rating introduces new inequities. In particular, it redistributes cost in a way that favours large corporations against small employers. It is normal in experience rating plans to exclude small employers, or to include them in a more limited way, perhaps using a more limited rate variation for small employers. This would not necessarily prejudice small employers if an experience rating plan operated in a state of balance, that is, if the 'merits' equalled the 'demerits,' so that the standard rate was unaffected.

Usually it is part of the aspiration of an experience rating plan that it will operate in balance in this way. However, more complaints are likely to arise from the award of "demerits" than from the award of 'merits.' The responses of the boards to those complaints sometimes produce an excess of 'merit' over 'demerit' points, thus causing a rise in the standard rate. When that happens, there is a cross-subsidy to large corporations from small employers who are not on the experience rating plan, or who are on the plan to a more limited extent.

The other distortion arises from the monitoring of claims. Large corporations commonly employ personnel for this purpose while smaller companies do not. This monitoring includes not only opposition to claims and the use of appeal processes, but also applications for the transfer of costs to the Second Injury Fund. To the extent that these applications succeed, the cost of those claims is distributed over all employers. Thus, these applications too create a cross-subsidy from smaller employers to larger corporations.

G. *The Influence on Perceptions of the Coverage*

Experience rating can produce or aggravate misconceptions with regard to the coverage of the *Acts*, thereby causing confusion in claims adjudication as well as in political processes.

It was the essence of our system of workers' compensation that benefits were to be payable automatically for disabilities resulting from employment. It was to be irrelevant whether a disability resulted from any fault on the part of the employer, and at least in serious disability and fatal cases, it was to be irrelevant whether a disability or death resulted from any fault on the part of the worker.

Experience rating, however, tends to produce a narrower perception of what the coverage is or ought to be. The ostensible justification generally used for experience rating is the assertion that it will create an incentive for the reduction of accidents. It is implicit in this that accidents resulting in compensation claims can be reduced at the choice of employers if they have the incentive. It almost, though not quite, follows from this that compensation claims, to be valid, should relate to accidents that are the fault of an employer. Whether or not this is the explanation, it is common to find in industries that are on experience rating that claims are opposed on the ground that the disability resulted from the fault of the worker, or alternatively, that it resulted from circumstances outside the control of the employer. While these contentions are legally irrelevant and are not generally accepted by compensation boards, the raising of such objections creates unnecessary controversy and delay in the payment of claims, with consequential risks of psychological damage to the workers concerned, as well as increased administrative overhead.

Where arguments of this kind fail as objections to the validity of a claim, they are sometimes re-asserted on an application to transfer the cost of the claim to the Second Injury Fund, or to some other general fund that will disperse the cost among other employers.

Thus in these ways too, experience rating contributes to misunderstandings and controversies in claims adjudication, to therapeutic damage, to higher administrative costs, and to inequities in the distribution of cost among employers.

H. *The Influence on Costs*

As explained above, the ostensible justification for experience rating is usually the assertion that it will reduce accidents, and that therefore and incidentally, it will reduce compensation costs. For the reasons explained above, that is not so. If an experience rating plan has any downward influence on costs, it is likely to be through the discouragement of claims, opposition to claims, and the confinement of benefits.

There are, however, several ways in which experience rating can *increase* the aggregate cost of compensation. First, there is the cost of operating the plan itself. The technical part, for example the computer programming, is relatively simple and cheap. Much of the other cost, however, is unrecorded. There is, for example, the cost of discussions relating to the design of the plan and the cost of ongoing explanations. There is also the cost of dealing with complaints about the administration of the plan, and the cost of dealing with the additional applications for transfers to the Second Injury Fund.

Secondly, there is the increase in cost that is caused by making claims administration and adjudication processes more controversial and more adversarial. Indeed, a veritable army of professionals and para-professionals has been spawned to deal with these controversies, and this is in addition to the time of internal company personnel. Part of this cost will appear as an addition to workers' compensation assessments, but a large part of the cost will be borne directly by employers, and by unions and other services acting on behalf of workers.

Thirdly, there are the costs resulting from the increase in the incidence of disablement (the therapeutic damage done by promoting broad-scale suspicion in claims administration, and by making adjudication more controversial and adversarial). Part of this cost will appear as an addition to workers' compensation assessments, and part may be reflected in payments from welfare and other sources.

Fourthly, there are the spill-over effects, such as the negative influence on labour relations.

Fifthly, experience rating fits into the same conceptual framework as full funding. Hence its adoption tends to impede any move towards current cost financing, a move which could enable the system to operate at lower overall cost in the long run, at least in Ontario and Quebec.

Finally, experience rating generates ongoing political pressures for the reduction of benefits and other restrictions on claims. These pressures inspire counter-pressures, with the result that ongoing political controversies create extra costs at the boards and elsewhere.

It may well be partly for these reasons that the assumed beneficial influence of experience rating has not been found in practice. For example, the industries to which experience rating has been applied in Canada have commonly been industries with relatively high assessment rates. Of course this does not prove that the higher rates resulted from experience rating. These industries have been high hazard industries. Nevertheless, it is at least a plausible possibility that experience rating may have contributed to the higher rates.

Again, some compensation boards in Canada have used experience rating fairly broadly while others have not used it at all. Yet I have never heard it suggested that a multi-jurisdictional comparison would show that experience rating has resulted in lower overall costs.

The New Zealand experience is also food for thought. New Zealand does not have experience rating. The average rate of assessment paid by employers in New Zealand is 77 cents per \$100 of assessable payroll (though it would be about \$1.21 if it were not for a transitory adjustment to reserves). At either of those figures, the average rate of assessment is much lower than in workers' compensation in Canada. Moreover, the

coverage is in many respects broader than in Canada. In particular, it is not confined to disabilities resulting from employment. Of course international comparisons of this kind are notoriously difficult, and of course the lower rates might be explained by other factors. This comparison is not proof that experience rating results in higher costs; but it is another cause for skepticism about any assertion that experience rating results in lower costs.

It is also important to bear in mind here that workers' compensation in Canada came about in the first place at the initiative of employers largely because of discontent with the old system of employers' liability. There was also dissatisfaction with that system among workers and unions. Employers' liability involved the delays, the formalities, the controversies, and the enormous administrative costs of the adversary process, which workers' compensation was intended to abolish. That system also involved experience rating.

I. *Success Measurement*

After the implementation of an experience rating plan, it is common to proclaim that its adoption has been a success. Such claims are manifestly unwarranted. No experience rating program has ever been introduced in Canada (or elsewhere to my knowledge) in conjunction with any research that would even attempt any measure of its significance.

One problem is the difficulty of developing a research design that will control for the concurrent operation of other variables that might affect claims records. There is also the difficulty of obtaining any injury or accident figures that are independent of claims.

Another problem is that there is no way of measuring the harm that is done by experience rating, or at least no method that has any hope of being used in practice. Thus, it is possible for a system of experience rating to be inflicting the most horrendous damage and yet for it to appear within a compensation board that the system is operating smoothly. Most of the damage would occur outside the board, and it would not readily be attributed to experience rating as the cause. To the extent that the damage occurs within a board, most of it would occur outside the department that is administering the experience rating plan, and again, most of it would not readily be attributed to experience rating as the cause.

I. *Conclusions on Experience Rating*

Of course the problems mentioned above can be mitigated or aggravated by the choices made in the detail of the formula, but there

is no formula that will avoid the problems, or that can even achieve a substantial reduction.

To sum up my thoughts on experience rating:

- Its overall influence on occupational health and safety is probably negative;
- It causes therapeutic harm, increasing the gravity of disabilities;
- Its influence on rehabilitation is probably beneficial in some circumstances, but in aggregate and on balance, is probably negative;
- Its influence on the efficiency of claims administration and on the quality of adjudication is negative.

It is uncertain whether experience rating increases or decreases the level of workers' compensation assessments, but it certainly increases the other costs of occupational disablement.

It may contribute to equity in the distribution of costs among employers, but any benefit in terms of equity is vastly outweighed by the other negative effects, and experience rating also creates some new inequities.

Experience rating is contrary to the public interest, contrary to the interests of workers, and probably contrary to the interests of employers, or at least the majority of employers. The only clear benefit of experience rating is the contribution that it makes to the prosperity of the professions.

The expansion of experience rating has not resulted from any research to assess the significance of what is being done. Instead, economists using nineteenth century market theory provide the ostensible justification, board actuaries or outside actuarial firms provide the charisma of 'professional' authenticity, the compensation boards provide the technology, corporate organisations provide the political clout to ensure that it happens, and the legal and medical professions apply their skills to cope with the resulting controversies.

Part of the problem is that our structures for system development in relation to workers' compensation have deteriorated in recent years. They have become more political and less analytical. In particular, we have not had a royal commission on workers' compensation for two decades, and major system changes are being made without any real analysis of the significance of what is being done.

Needless to say, these conclusions relate only to experience rating in the context of workers' compensation. Different considerations would apply to the use of experience rating in relation to, for example, automobile insurance, or a comprehensive plan of compensation for disablement.

II. OTHER FINANCIAL INCENTIVES TO CARE

A. *Introduction*

A conclusion that experience rating has a negative influence on occupational health and safety does not mean that workers' compensation cannot provide financial incentives to care. Indeed, there are several ways in which workers' compensation has been so used, or in which it might be used, and which are summarized below.

B. *A Token Safety Audit*

An employer might be allowed an assessment credit on the result of a safety audit of a nominal or token nature. For example, points may be awarded for having a safety committee, having certain notices in place, and having personal protective equipment available. A safety audit of this type only indicates whether an employer is making certain nominal gestures. It may or may not indicate real safety performance. For this reason, it is a waste of resources as well as being potentially counter-productive and unfair in distributing compensation costs among employers. It can also divert attention from real achievement in health and safety.

C. *A Real Safety Audit*

Another possibility is a variation in assessment rates based on real safety audits. For example, the audit might include a scrutiny of the design of plant, the choices and uses of machinery and equipment, the existence and control of toxic substances, and a testing of emergency procedures. Something on these lines has been undertaken by insurance companies in a limited range of situations, such as the off-shore drilling rigs. It is not practicable, however, for safety audits of this type to be undertaken by a workers' compensation board among the general range of employers.

What is practicable is for an audit to be undertaken in respect of a particular hazard that is of significant concern at the time, so that at least that hazard can be reduced. For example, in 1974 the *Workers' Compensation Act* in British Columbia was amended to provide that the Board may vary the rate of assessment as between different employers or levy supplementary assessments according to the estimated exposure of workers to industrial noise.⁹ The implementation of that section was halted in 1976. Such realistic incentives for the protection of workers' health appear to have little prospect of survival in the political process.

⁹ *Workmens' Compensation Amendment Act 1974*, S.B.C. 1974, c. 101, s. 24A, adding s. 40A to the principal Act.

D. *Penalty Assessments by Reference to Claims Experience*

In Ontario, the Board can and does levy a penalty assessment where the claims experience of an employer is consistently much greater than the average experience for the rate group. There is anecdotal evidence that this type of penalty assessment provides an incentive to improve safety performance by the companies upon which the assessment has been levied, or where a company is coming very close to such an assessment. It is arguable, however, that the system is counter-productive by creating a disincentive to care before the situation has become extreme. Also, it is open to many of the same objections as experience rating. For example, the company may respond by an increasingly negative posture towards claims rather than by improving safety, and there is anecdotal evidence that companies do sometimes respond in this way. Also, this type of penalty assessment is of no use for the prevention of serious disease.

E. *Penalty Assessments by Reference to Observed Conditions*

The most promising use of workers' compensation assessments as an incentive to care is the imposition of penalty assessments by reference to observed conditions.

Since these assessments are a direct response to the existence of hazardous conditions, they cannot be avoided by any manipulation of claims.

These penalty assessments do not involve the same administrative or political problems as real safety audits, and since all employers are not being assessed contemporaneously, there are not the same problems of equity among employers. Of course an assessment might be imposed upon one employer as a response to hazardous conditions while similar conditions at another place of employment may not have been discovered, but that risk is inherent in almost any program of law enforcement. In criminal proceedings, for example, it is no defence that other offenders have not been caught.

Given the limited range of circumstances in which prosecutions can be useful, penalty assessments of this type are the only sanction that can be used on any broad scale for the enforcement of occupational health and safety requirements.¹⁰

¹⁰ See T.G. Ison, "Re The Uses and Limitations of Sanctions in Industrial Health and Safety" (1975) 2 Workers' Comp. R. 203.

F. *Penalty Levies*

In British Columbia, the Board may also levy an additional assessment upon an employer where a disability or death has resulted substantially from the gross negligence of an employer or the failure of an employer to adopt reasonable means for the prevention of disabilities or to comply with the orders, or directors of the Board or with the regulations of the Board.¹¹

This does not, of course, mean that the Board investigates fault on every claim. The practice is that in some of the extreme cases of serious neglect by an employer resulting in injury or disease, the Board imposes an additional assessment. It is infinitely better than experience rating in that the enquiry focusses upon the existence of hazardous conditions. Moreover, the disadvantages of experience rating do not apply. For example, the kinds of cases in which a penalty levy is imposed are not the kinds of cases in which a claim is likely to be discouraged or opposed by an employer.

III. OVERALL CONCLUSIONS

Adjustments to workers' compensation assessments have great potential as an incentive to care if the adjustments are made as a direct response to the existence of hazardous conditions. Indeed, such adjustments are essential to the fulfillment of government responsibilities in occupational health and safety. This requires a program of inspection and penalty assessments, and perhaps also penalty levies. Experience rating, however, is very damaging.

¹¹ *Workers' Compensation Act*, R.S.B.C. 1979, c. 437, s. 73(2).