Four Things You Should Know About Your Experience Modification Factor

BY KEVIN RING

As a simple indicator of how your safety record compares to previous years' expectations, this number deserves your attention.

If you call AISC member Douglas Steel Fabricating Company, you'll hear all about the company's low Experience Modification Factor and excellent safety record while you wait for the call to transfer. What is this factor? Why would you use it as a selling point to promote your firm? And how can you improve yours?

THE EXPERIENCE MODIFICATION FACTOR is a multiplier applied to the base rate of a firm's Workers' Compensation Insurance to determine its premiums. Most employers find that deciphering their Workers' Compensation Experience Modification Factor, or Experience Mod, is like reading the foreign language version of instructions for installing an electronic device. There is very often confusion about how the Experience Mod is calculated and how it ultimately affects what they pay for their Workers' Compensation coverage.

At its core, the Experience Mod is the ratio of the dollars the insurance company has to allocate this year to cover the costs of injuries to the dollars they expected to allocate during your prior three policy years. The amount of time included in the Experience Mod can vary if the renewal of your Workers' Comp policy changed. So, be sure to check with your agent.

Every work classification that exists, from file clerk to welder, has an *expected loss rate*. The rate is the amount of money an insurance company should expect to spend for employee injuries for every $100 of payroll.

For instance, if your expected loss rate is 1.0, for every $100,000 in payroll costs you are expected to have $1,000 in employee injury expenses. If you have less than that, your Experience Mod drops below 1.0, and, if you have more, it goes north of 1.0. The Experience Mod multiplies your base premium. Go above 1.0 and you pay a surcharge. Drop below 1.0 and you receive a credit.

Unfortunately, most employers are not familiar with this basic information about their Experience Mod. They see a number the insurance company has assigned, but many don't know the road taken to get there, or what can be done to adjust it.

Here are four key points employers should know about their Experience Mod to better understand the process and control their Workers' Compensation costs.

1. Frequency is worse than severity. An Experience Mod will be impacted more by 10 injury claims at $5,000 than by one claim at $50,000. The first $5,000 spent for every employee injury is counted dollar for dollar ($7,000 in California), thus all 10 of the small claims will fully impact the Experience Mod. With one $50,000 claim, 100% of the first $5,000 is included but only a percentage of the remaining $45,000 is counted. This percentage can vary between 4% and 80%, depending on the total amount the insurance company expects to spend on a company's employee injuries over a three-year period.

Although this approach gives greater weight to accident frequency than severity, severity is still relevant. When paired with frequency, severity of employee injuries will be even more detrimental to an Experience Mod. Employers that work to reduce the frequency of injuries and have a return to work program to help reduce severity are in the best position to control their Experience Mod.

2. Your Experience Mod is compared only within your particular industry. There is a misconception among many employers that their Experience Mod is as high as it is because they are being unfairly compared against less injury-prone occupations, such as file clerks and bank tellers. But in reality they only are being compared to other businesses within the same classification. Welders are compared to welders. Machine shop workers to machine shop workers. There are dozens of distinct manufacturing-related class codes, and many are very similar, so it is important to make sure your employees are correctly classified.

3. Don't assume that because your Experience Mod is below 1.0 everything is hunky-dory. Just because your Experience Mod is below 1.0, don't assume it can't be, or shouldn't be, lower. Make it a point to know what the minimum Experience Mod is for your company and strive to reach it. For example, if your Mod is 0.85, but the minimum Mod is 0.61, 0.24 of your Mod is controllable. With

Kevin Ring is the lead workers' compensation analyst for the Institute of WorkComp Professionals, which trains insurance agents to help employers reduce Workers' Compensation expenses. A licensed property and casualty insurance agent, he is the co-developer of a new Workers' Comp software suite that helps insurance professionals in working with employers. He can be contacted at 828.274.0959 or ***kevin@workcompprofessionals.com****.*

a $100,000 premium, lowering the Mod to the minimum would save $24,000. Lowering your Experience Mod even a few more points can save you significant money in the long run. Don't settle for average.

4. Insurance companies don't pay for your employee's injuries. Claims are paid by employers through the Experience Mod, often at 200% – 300% interest. Each state has a limit at which an employee injury ceases to impact the Experience Mod and when you have a very large claim, the insurance company does wind up footing some of the bill. In most cases, though, the insurance company is simply temporarily financing it on the employer's behalf.

No employer is expected to know everything about Experience Modification Factors. And, in fact, many insurance agents are baffled by its inner workings. But by possessing even the most basic information, such as why your Experience Mod is what it is, what it took to get to that point, and steps you can take to lower it, you'll find yourself saving hundreds, if not thousands of dollars in Workers' Compensation costs over the long run. **MSC**