Workers' comp crisis may be costly

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A growing insolvency crisis in workers' compensation insurance, born from years of lax oversight by state regulators, is threatening to leave thousands of small businesses owing $600 million or more to New York insurance pools they trusted to pay claims from workplace death and injury.

Already, the little-publicized crisis has forced otherwise stable companies to lay off workers and curtail hiring plans during a critical point in the state's economic recovery.

And at some point, taxpayers could be forced to pick up the tab for whatever can't be recovered through lawsuits or other means.

State regulators got authority earlier this decade to require financial reports from so-called Group Self-Insured Trusts, private workers' comp cooperatives formed to help employers cut insurance costs, but it was already too late for some.

New York's Workers' Compensation Board, which regulates the trusts, received its first audited reports in May 2003, nearly a decade after these group insurance pools first surged in popularity. Those reports showed more than a dozen trusts with financial shortfalls, according to a task force report released earlier this summer.

The first trusts became insolvent in 2006.

The problems deepened abruptly in 2007 and 2008, when at least seven trusts administered by a Poughkeepsie-based business, Compensation Risk Managers, unexpectedly defaulted.

"There was little to no indication in the financial and actuarial reports submitted that there was financial distress of the magnitude ultimately identified," the task force wrote in its report.

The state's compensation board has sued CRM, seeking more than $400 million and accusing it, among other things, of providing inaccurate financial reports that hid the depth of its trusts' problems. The compensation board also hasn't ruled out legal action against other trusts and their advisers.

"We're going to aggressively pursue these entities that have been responsible for the insolvency of these trusts," said Brian Keegan, a spokesman for the Workers' Compensation Board.

The board also is assessing the employer members of the failed trusts for unfunded debts and for its own administrative costs going forward.

Group Self-Insured Trusts often were formed by companies in the same or similar New York businesses that banded together and kept an eye on one another's safety practices. It was a way to reduce the cost of workers' compensation coverage, which every company is required to have.

In the mid-1990s, insurance brokers became more active in forming the trusts, which grew in size in part because commercial workers' comp coverage was getting so expensive.

The administration of former Gov. George Pataki saw the trusts as an alternative at a time when business leaders were voicing alarm over workers' comp costs.

Robert Snashall, a Cazenovia attorney, was appointed to head the state's workers' comp board in 1995. He did not return calls seeking comment for this story.

"Skyrocketing workers' compensation costs are one of the main obstacles to economic growth and opportunity," Pataki said at the time, according to a report in the Syracuse Herald-Journal. "Robert Snashall understands this and will work to make sure the workers' compensation system is fair to both the injured worker and the employer who pays the bill."

Although he had the ultimate rule-making authority at the board, it's not clear whether Snashall immediately saw the risk that group self-insured trusts posed, particularly as they expanded and by some accounts, riskier companies were signed up, driving up claims.

Snashall joined CRM after completing his term as chairman of the compensation board and at one point sought to represent the troubled administrator in front of the board. He stepped down after ethical questions were raised, Keegan said.

Group self-insured trusts in New York reached a peak in 2007 with more than 18,000 active employer members, according to the task force. That number fell to 15,212 in 2008 and to just 4,250 last year.

"In the '90s ... it became less about a small group and more like a mutual insurance company," said Mary Beth Woods, director of financial administration for the compensation board. "A lot of people felt it was less expensive."

But, she added, they didn't appreciate the "joint and several" risk, where participants could be held responsible for the liabilities of the group.

And with actuaries, accountants, brokers, administrators and other managers relieved of much of the risk, problems could arise.

"The weakness in this structure is that the bulk of the decision-making is being done by individuals whose interests do not always align with those of the members," the task force said. "In fact, in the short term, these key agents may actually stand to benefit by being overly optimistic with much of the operating decisions including developing rates, setting reserves and issuing dividends."

The liabilities to members, meanwhile, can be hefty. The insolvent Builders' Self-Insurance Trust, for example, has 311 members and a minimum of $20 million in liabilities, Woods said.

Only 143 have made payments. The task force reported that, as of May 17, $6.4 million had been billed to members, and $404,200, 6.3 percent of it, had been collected. Overall, just 6.8 percent -- $33.8 million -- had been collected from all the trusts of the $497.9 million billed to trust members. Pledges of payment that haven't been received were not included.

One couple, Thomas and Diane Barber of Valatie, said their business had $7,500 in claims throughout its existence. But they've seen their assessment from the compensation board climb to $53,003, in addition to $70,923 they paid from 2001 to 2007 for their coverage. That's $123,927 in workers' comp insurance costs to cover $7,500 in claims. They've paid some of it, but the latest assessment requires a monthly minimum payment of $845.74. Their only source of income currently is Social Security, they said.

"This is a black hole that looks like it can never be filled," they wrote in a letter to legislators and media outlets.

"What we're dealing with is an incredible bill, people who are in denial about it, very poor communication from the Workers' Compensation Board, and pretty stern letters (from them) demanding payment," said Brooke Greenhouse, a central New York builder who was also a member of the Builders' Trust and a former president of the New York State Builders Association in Albany.

It was the state association that signed up its members in the trust. A former executive vice president, Philip LaRocque, also served as a trustee in the self-insured trust. He is no longer with the association, and efforts to reach him for comment were not successful.

Greenhouse and others wouldn't comment on the reason for LaRocque's departure.

Financial problems at the Builders' Self Insurance Trust surfaced early, and Marsh U.S.A., which had taken over administration, cited trustees' deep discounting of premiums to members and its unwillingness to pass along fees charged by regulators.

Marsh recommended that premiums be raised, but trustees rejected that because they feared the builders trust would lose members, according to a forensic accounting of the trust's finances.

Members did start quitting the trust in 2004, and by early 2009, the trust was insolvent and under the control of the Workers' Compensation Board.

There's a moratorium on the formation of new trusts, and a task force earlier this summer recommended ending the remaining group self-insured trusts. That's a shame, said attorney Rich Honen of the Albany firm Phillips Lytle LLP.

"I think these trusts were a good idea," he said Thursday. "The more successful ones were the ones with the good administrators."

He said First Cardinal Corp. of Latham administered a number of trusts that ran surpluses. But it's not forming any new trusts.

The compensation board assesses trusts to cover its own administrative costs in overseeing the system. After several trusts collapsed, Honen said that assessment for a group of trusts he represented jumped from $155,000 one year to $12.1 million the next. "The assessments were said to be to pay for the operation of the Workers' Compensation Board," Honen said. "But they coincided exactly with the (shortfalls) of the defaulted trusts."

Some wonder whether the current assessments the board is seeking from members of the failed trusts also is greater than it should be.

Greenhouse said the builders trust collected just $1.5 million in annual premiums, yet its obligation is now $20 million and rising.

"There seems to be a disconnect between $1.5 million of premiums and $20 million to $40 million in liabilities," he said.

The Workers' Compensation Board, for its part, is trying to ensure that disabled workers and their survivors continue to receive the benefit checks and payments for medical care that they're entitled to.

"We're trying to work with the members of the trust to buy ourselves some time," said Michael Papa, an associate attorney with the compensation board, "where members provide just enough money to meet the month-to-month obligations."

Meanwhile, legislation that would end the group self-insured trusts, with some exceptions for the healthiest ones, has been proposed by the Paterson administration. Efforts are also under way to relieve trust members of further liabilities with what's called an "assumption of workers' comp liability policy," Woods said. Those policies would carry a large one-time premium in return for peace of mind.

The legislation would further tighten regulatory oversight. The governor's office says it would have "no material impact" on the state budget.

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