WORKERS’ COMPENSATION

EXPERIENCE MODIFICATION: PROBLEMS AND PITFALLS

By DAVE K. SMITH

The experience modification rating (EMR) is a workers’ compensation (WC) insurance rating device. Although it is increasingly relied on as a measure of safety performance, EMR is, in the author’s opinion, a poor measure of a firm’s true safety performance.

WHAT IS EMR?

EMR is a number that compares actual losses to expected losses in WC insurance. Experience rating is a mandatory program of individual risk rating. Different states have different systems, typically involving some rating organization (i.e., the National Council on Compensation Insurance or a state-specific group) that develops EMRs for individual employers.

A firm with a better-than-average loss experience receives an EMR of less than 1.0 (or 100 percent), which is credited to that firm’s WC premium. Conversely, a debit EMR of greater than 1.0 increases the premium. For example, “an experience modifier of 0.80 means the insured will receive a 20-percent discount on its WC insurance. A contractor with a modifier of 1.20 will pay a 20-percent surcharge on its WC premium” (Farmer and O’Neill 32).

WHY EXPERIENCE RATING?

Compensate for Classification Variations

For the purpose of rating, WC plans generally assign work activities to different classifications. In any classification, some individual variations will exist—often referred to as the “light and heavy” ends of the class.

For example, a roofing supply firm that delivers materials to rooftops is often classified as a building supply dealer. However, since its actual operations are more analogous to roofing contracting, this firm would be at the heavy end of the building supply class because the roofing exposure is “heavier” than that of a typical building supply dealer.

Roofing has several well-recognized hazards, including elevated falls, burns and extensive manual material handling. A typical building materials dealer does not have these exposures. In most states, the base rate for building supply dealers is about one-half of the roofing contracting rate. Therefore, EMR is designed to compensate for the under-rating of the roofing supply dealer.

For example, a roofing supply dealer (classified as a building supply dealer) with a 1.50 EMR might be considered excellent because the true exposure is much greater than other building supply employers with lesser injury exposures. In this case, the base rate is increased by 50 percent, but the roofing supply rate may be as much as 200 percent of the building supply rate. Thus, a 1.50 EMR would be considered “good” because of the variances in the classification system.

Provide Incentives for Safety

Although EMR is intended to promote safety measures in the workplace, some critics hold that “experience rating probably has negative influences on health and safety” (Jolley 209). Other research shows no conclusive link between safety and experience rating (Jolley 227). Yet, a new study by the National Council on Compensation Insurance concludes that the more a firm spends on workplace safety, the more its EMR declines, and that the greater amount spent on safety per dollar of premium, the greater the decline (Kahley and Sornberger).

EMR AS A MEASURE OF SAFETY

Contractor Pre-Bid Qualification

EMR is often used to prequalify construction contractors. Some have stated that an “EMR of 1.0 indicates that WC is not controlled,” while an “EMR of 0.5 indicates that employees are provided a safe work environment” (Roughton 33). Others recommend continued use of these rates as “they are excellent indicators of past performance” (Ryan 26). OSHA’s Process Safety Management standard requires evaluation, coordination and control of contractors. As a result, many plant owners use EMR to qualify contractors to meet these requirements (Angus 5).

High-Hazard Employers

The California Div. of Occupational Safety and Health has developed a high-hazard employee (HHE) program designed to reduce WC claims data. The legislation enables a threshold of 1.25 EMR. Employers with an EMR of 1.25 or greater are assessed a fee to support HHE and are subject to targeted compliance and consultation efforts (Policy & Procedure Manual C-171).

PROBLEMS WITH THE EMR SYSTEM

“Apples and Oranges”

Each state has a different system and, thus, different rules and regulations. Consequently, EMRs may not be comparable (Farmer and O’Neill 34). Furthermore, only reported injuries are measured—not all injuries (Jolley 218). Since reporting requirements often differ among these systems, an EMR developed from experience in one state may not be directly comparable to that developed in another state.

Self-Insured Employers

In some states, a large firm may qualify for self-insurance. In such a case, the employer does not purchase insurance from an insurance carrier or state fund, but rather pays for losses directly. In the case of contractor pre-qualification, a self-insured employer may create its own EMR, with no official oversight. The result: Potential discrimination against smaller insured employers that are rated by official organizations. Thus, a self-insured employer can manipulate data that the small insured employer cannot.

EMR Discriminates Against Small Employers

Small employers are subject to wider variation in EMR than large employers. Small employers face a high degree of randomness in injury occurrence, which is more predictable in large employers. In this case, “compensation experience is not a statistically significant indicator of safety performance” (Jolley 221). This is a variation of the law of large numbers—the probability of an event occurring (such as an employee injury) depends on...
a large number of separate, independent trials. Only events that may be repeated over a long period of time and that are statistically significant may be governed by probabilities (Vaughan 22).

**TABLE 1 EMR Increase**

<table>
<thead>
<tr>
<th>Condition</th>
<th>EMR</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995 (Actual)</td>
<td>1.05</td>
</tr>
<tr>
<td>1995 (Based on 1994 Expected Loss Rates)</td>
<td>0.88</td>
</tr>
</tbody>
</table>

**Conclusion**

If EMR is an inadequate measure of safety performance, how should safety performance be evaluated? EMR should be reviewed, but it should not be used as a “go, no-go switch.” The best course of action: Evaluate both results and activities occurring now to determine the firm’s current safety performance.

**References**


**Reader Feedback**

Did you find this article interesting and useful? Circle the corresponding number on the reader service card.

- **YES** 34
- **SOMewhat** 35
- **NO** 36