

ARTICLES

3 Factors Used to Calculate Workers Compensation Premiums

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As the owner of same day transportation operation, understanding your workers compensation policy can be challenging to say the least! While business owners understand the requirements of carrying workers compensation for their operation, employees and financial stability, if you're unfamiliar with the ins and outs of this coverage (or benefits program as a whole), it can become quite confusing when you sit down to vet your options and pricing.

Workers compensation is essential to your business and, in most cases, required. Without it, organizations run the risk of incurring crippling financial liabilities associated with on-the-job employee injuries.

And while it's important to understand *why* your business needs a workers comp policy, it's equally important to understand *how* your premium rate is calculated. Continue reading to learn more about how workers comp premiums are structured.



Understanding the Cost of Workers Compensation Premiums

There are three primary factors that determine a business' workers compensation (WC) premium rate. For the most part, these factors are fixed by each state, and your insurance company's discretion is strictly limited.

Workers Comp Premium Rate Factors:

- Classification Code
- Rates
- Experience Modification Factor / MOD

Classification Code

- An independent advisory organization, the National Council on Compensation Insurance (NCCI), determines the classification codes for every occupation / type of work. These codes are used by insurance companies to identify the business type and estimated cost of a WC rate. If a business reports losses above or below the average industry rate for their type of work, their WC rate will adjust accordingly.

- Misclassification of your business can be costly, as some classification codes / types of work cost less to cover. For example, the correct classification for courier companies is "parcel delivery," which covers transportation of shipments weighing less than 100 pounds. If your business is currently assigned to a less costly classification, be forewarned that a sharp auditor can reclassify you and charge for the increased premiums you "should have" been paying ... going back *up to three years*. If the NCCI agrees, you face a costly, uphill battle.
- One piece of good news is that you *are* allowed to separate out all of your clerical, sales, foot messenger, and executive payrolls into cheaper classifications.
- Do you know what your proper workers comp classification code is? **Talk to you insurance agent about your business, classification code and WC program.** If adjustments need to be made to re-classify your organization, they will assist you in correcting the issue.

Rates

- Each WC classification has an assigned rate, which varies from state to state. For drivers, rates tend to range between \$6.00 and \$10.00 per \$100.00 of driver compensation. While this is an average, rates can run even higher. The rate is equivalent to a premium of between 6% and 10% of total driver compensation (i.e. Annual 1099 figures). By comparison, office and sales rates can be less than 1 % or \$1.00 per \$100 of an employee's compensation.
- Let's take a simple example of a courier company in a state with a \$7.00 driver rate and a \$.60 clerical rate. The courier companies pay its drivers \$150,000 and office staff \$45,000 annually. WC premiums would be \$10,500 for drivers (7.00 x 1500) and \$270 for clerical (.60 x 450).

Experience Modification

- To reward businesses with superior loss records and provide an incentive for others to reduce losses and associated claims, a percentage modifier is applied to the basic premiums of all but the smallest businesses.
- Modifiers or "mods" are calculated by the NCC and follow you wherever you are for coverage. The formulas used are complex, but the basic idea is to compare your business with the "expected" losses of a comparable business in your classification.
- For example, a mod of .82 would indicate that a business has few, if any, workers comp losses. These companies would pay only 82% of the basic premium assigned to their classification code. By contrast, a 1.82 mod is evidence of high losses, and the associated company would pay 182%, or almost twice their basic premium.
- There is some protection against one nasty loss sending your mod sky-high; **but every loss does impact your mod for a full three years.** And, once it's on your record, it isn't easy to escape your mod and start over.
- One last word about costs: It is illegal in almost all cases to pass on the cost of workers' compensation to those who may receive its benefits (i.e. your employees). But this wasn't always the case. This has been one significant cause of the decline in contractor commission rates compared to ten years ago. At that time, the government and insurance industry were only just beginning to crack down on companies using ICs. As more and more companies have begun paying WC on drivers, something had to give.



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