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**A Final**  
**Report to the Legislature**  
**and to the Governor**

**On the**

**Special Compensation Fund**  
**ARP Settlement Project**

**October 15, 2004**

**Minnesota Department of Labor**  
**and Industry**

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## **Background**

The Special Compensation Fund (SCF) is administered by the Department of Labor and Industry (DLI). The SCF assessment is levied on workers' compensation insurers and self-insured employers, based on the amount of workers' compensation indemnity payments (wage-replacement and permanent disability payments) made by each such insurer or self-insured business. This assessment funds the state's workers' compensation programs.

The largest single component of the SCF's expenditures (and therefore, the largest cost-driver for the assessments employers and insurers must pay) are the Second Injury (SI) and Supplementary Benefit (SB) programs, which account for more than half of the SCF's expenditures each year. Although these programs were ended by the Legislature in 1992 and 1995 respectively, payments will continue for a number of years until the disabled workers receiving benefits die or otherwise become ineligible. Between 1987 and 2000, the assessment rate fluctuated between 28 and 31 percent of paid indemnity.

On July 10, 2000, \$325 million in "excess surplus" was transferred from the Minnesota Assigned Risk Plan to the SCF. The Legislature directed the money to be used to reduce long-term liabilities in both the SI and SB programs. In February 2000, there were nearly 7,000 open claims, with future liabilities estimated at nearly \$1.365 billion.

The Legislature intended that DLI use these monies to liquidate or settle a significant portion of the ongoing SB and SI claims in order to reduce the ongoing assessments paid by insurers and employers in the state. The assessment rate subsequently dropped from 30% to 20% for indemnity payments made after July 1, 2000. This unprecedented reduction in the rate was made in anticipation of settlement of a substantial portion of these claims, and also due to the increased investment income provided by the appropriated funds.

The rate remained at 20% throughout 2001. However, in its 2002 session, the Legislature directed the transfer of \$250 million from the SCF to the state's General Fund, to help resolve a quickly-developing budget crisis (Laws of Minn. 2002, Ch. 220, Art. 13, Sec. 9, subd. 2, and Ch. 374, Art. 8, Sec. 6). During the 2003 legislative session, this transfer amount was increased to \$265 million (Laws of Minn. 2003, Ch. 128, Art. 11, Sec. 12). This reallocation necessitated a return to the previous assessment rate of 30% in order for the SCF to continue to meet its obligations to reimburse employers and insurers in a timely fashion for benefit payments.

## **Project**

Following the 2000 legislative appropriation, the DLI Special Compensation Fund established the Assigned Risk Plan (ARP) settlement project. The project's goal was to

provide lump-sum payments to injured workers to pay off or "settle" their ongoing workers' compensation benefits claims under the SI and SB programs. Four claims staff were hired for the project in fall 2000. Further assistance was provided to the project team by other DLI staff members.

The team began its work by creating databases and reports to track settlement information and outcomes. A spreadsheet was also developed to assist team members estimating the present value of open claims. The team then started reviewing open cases for settlement potential.

The SI and SB programs include a wide variety of cases, with dates of injury ranging from the 1960s to 1995, and claimant ages ranging from the 30s to the 80s. Health issues can be as serious as end-stage cancer or chronic vegetative states. Approximately 1,000 of the open claims were eliminated for consideration of settlement due to such factors.

Workers' compensation benefits are paid to injured workers by insurance companies and self-insured employers. When the state has liability for some or all of those benefits under the SI and SB programs, insurers and self-insured employers must submit claims to DLI for reimbursement. All settlements involve three parties: the injured worker, the insurer or self-insured employer, and DLI.

## **Phase I**

Phase I of the project focused on working with the insurers and self-insured employers who had the highest number of claims. During fiscal year 2001, more than 65 insurers and self-insured employers were contacted by the team. Through these insurers or employers, 600 injured workers were contacted to determine their interest in settlement. In addition, as new claims were presented to DLI by insurers or employers, DLI staff members reviewed those claims for settlement potential prior to establishing a weekly benefit stream for the individual.

During fiscal year 2001, 335 claims were settled, at a total cost of \$17 million. These settlements reduced the long-term liability by an estimated \$161 million.

## **Phase II**

The project team began Phase II in December 2001. Claimants were contacted directly to discuss fair and reasonable settlements of the ongoing SI and SB claims. Settlement offers reflected current financial marketplace conditions and life expectancy tables in assessing the fair present value of these claims.

This phase required the development of a new database that allowed merging address information with a letter to be mailed directly to claimants. Insurers and third-party administrators (TPAs), starting with those with the largest file counts, were contacted and asked to supply a current address and other information about each claimant, in a format that can be readily loaded to the "ARP Settlement Action Project"(ASAP) database.

Claimants were contacted by a letter and invited to participate in the program. ASAP team staff members handled the negotiations directly with the claimants and the insurer or TPA. Mediation services, provided by DLI staff mediators, were used to assist in negotiations and draft the settlement agreements. All agreements were submitted as a settlement stipulation to the Office of Administrative Hearings for final approval.

The procedure implemented by the team required an initial inquiry into whether the employee was represented by counsel in the matter. If not, negotiations were undertaken directly with the employee. An investigation into the health status of the claimant was conducted. Medical records were obtained and reviewed. If a serious health condition was noted (whether related to the claimant's work injury or not), the life expectancy assumptions were adjusted, and the present value of the claim was adjusted accordingly.

After the claims manager had the information needed to assess the fair present value of the claim, an offer was conveyed to the claimant (either directly, or through an insurer or attorney, depending on the circumstances). If agreement was reached, a stipulation was drafted, submitted to a compensation judge for approval, and an award was issued if the judge approves of the settlement. Payment was then issued to the claimant by the insurer, and the SCF's share was subsequently reimbursed to the insurer.

Phase II of this project represented a more aggressive settlement strategy in order to overcome some of the challenges that the department faced during Phase I. The Department of Labor and Industry anticipated improved settlement results during this phase by performing administrative tasks internally, rather than burdening the insurance community for this service.

## **Conclusion**

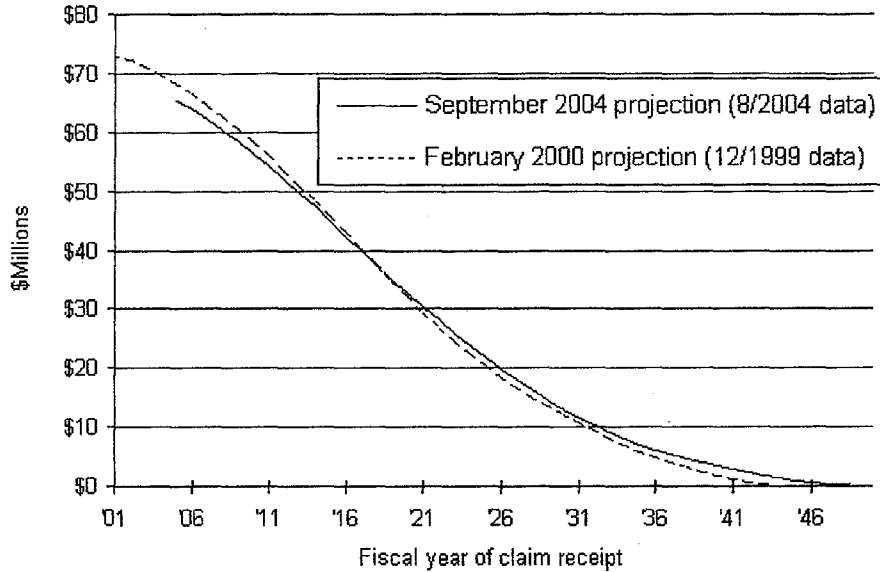
The project began to wind-down after the 2002 legislature directed the transfer of funds to the General Fund. Since the settlement process can be lengthy, lasting anywhere from 90 days to 18 months, the final payment made under this project was not made until 9/17/03.

Over the course of the project, more than 900 claims were closed through settlement at a benefit expenditure of less than \$60 million, eliminating an estimated \$450 million in future payments. The total administrative costs for salary and operating expenses during the project were \$457,611.

During the project, the \$325 million generated interest proceeds of \$35 million. This interest was dedicated to the payment of ongoing supplementary benefits and second injury reimbursement claims.

The long-term effect of the ARP Settlement Project will have a positive impact on the future liability for supplementary and second injury claims as evidenced in the attached graph; however, it is impossible to accurately quantify the effect. DLI is currently experiencing an increase in the number of inactive pre-1995 claims that are determined to be permanent-total disability, and thus affect the supplemental benefit exposure. DLI is developing strategies to identify the effect on future payment exposures. What is known is that the assessment rate has dropped from 30% in FY 2000 to 25.68% in FY 2005. This is partially due to settlements negotiated during this project.

**Supplementary Benefit and Second Injury Reimbursements:  
February 2000 and September 2004 Projections [1]**



FY of Claim Receipt	Projection (\$Millions)		FY of Claim Receipt	Projection (\$Millions)		FY of Claim Receipt	Projection (\$Millions)	
	Sep. 2004	Feb. 2000		Sep. 2004	Feb. 2000		Sep. 2004	Feb. 2000
2001		72.9	2018	37.4	37.5	2035	7.0	5.8
2002		72.1	2019	35.0	34.7	2036	6.1	4.9
2003		71.1	2020	32.6	32.0	2037	5.4	3.9
2004		69.8	2021	30.3	29.2	2038	4.7	3.1
2005	65.4	68.2	2022	28.0	26.7	2039	4.0	2.3
2006	63.9	66.5	2023	25.8	24.3	2040	3.4	1.6
2007	62.2	64.6	2024	23.7	22.2	2041	2.9	1.1
2008	60.3	62.5	2025	21.7	20.2	2042	2.3	.7
2009	58.4	60.4	2026	19.8	18.3	2043	1.8	.4
2010	56.3	58.1	2027	17.9	16.5	2044	1.3	.1
2011	54.1	55.8	2028	16.2	14.9	2045	.9	.0
2012	51.9	53.3	2029	14.5	13.4	2046	.6	
2013	49.6	50.8	2030	13.0	12.1	2047	.4	
2014	47.2	48.3	2031	11.5	10.7	2048	.2	
2015	44.8	45.7	2032	10.2	9.3	2049	.1	
2016	42.3	43.0	2033	9.1	8.0	2050	.0	
2017	39.8	40.2	2034	8.0	6.9			

1. Projections by Minnesota Department of Labor and Industry, Research and Statistics with DLI data. Includes supplementary benefit and second injury reimbursements. Projections assume no future settlement activity.

Minnesota Department of Labor and Industry, Research and Statistics, October 11, 2004.