

What Is Workers' Compensation Insurance?



Prior to the adoption of workers' compensation laws, employees who were injured or became ill due to their job had to file a lawsuit against their employer for any type of compensation to cover medical bills, disability or lost wages. In the event of the employee's death on the job, their family had to file a lawsuit against the employer to receive a death benefit. If the employer was not found totally at fault, injured employees or their families could be left with a large legal bill but no financial restitution.

To provide more protection for employees, states began adopting workers' compensation statutes. Today, every state but Texas requires employees to purchase workers' comp (and the Lone Star State still recommends the insurance).

Workers' comp serves as somewhat of a compromise. Employers assume liability for any work-related injuries or illnesses, regardless of who is considered at fault. And employees surrender their right to sue the employer for covered incidents, except in certain extreme cases.

A state-by-state issue

Each state determines the specifics of its own workers' comp requirements. This includes:

- Benefit amounts
- What disabilities or injuries are covered
- How each impairment is to be evaluated
- Required medical care and limits
- Claims management
- Dispute resolution methods

In addition, each state dictates whether the insurance can be issued by private insurance companies; if only the state will serve the market with its own workers' comp coverage, often called a "state fund"; or if there will be a combined approach.

State funds make it possible for every business to secure coverage, even those that cannot find coverage from a private insurer due to the individual situation or a high-risk industry. Currently, four states — North Dakota, Ohio, Washington and Wyoming — limit the market for workers' comp insurance to their own state-run pool. In Ohio and Washington, there are also limited cases in which a business can gain authorization to self-insure.

If your business has employees in multiple states, keep in mind that you will need to follow different requirements based on location.

Coverage basics

While there are certainly nuances by state, workers' comp generally covers any injuries an employee suffers while on business premises or anywhere they might be working in the "course and scope" of their position. This includes driving for work purposes, either in a business-owned or personal vehicle, with the exception of driving to or from work or for personal reasons during work hours. Also included are workplace violence, terrorist attacks and natural disasters.

In addition, state laws define which illnesses and occupational diseases are included in workers' comp coverage. This is particularly relevant for industries that involve toxic chemicals or pollutants.

Benefits to employees

For any injury or illness, all necessary and appropriate treatment is defined state by state, including expected treatment protocols and acceptable diagnostic tests.

If the employee is disabled, income replacement benefits are available under workers' comp and are based on whether the individual has suffered total or partial disability and whether it is permanent or temporary. Some states outline a maximum number of weeks this benefit is allowed, while others require payment for the duration of the disability. Total benefit payment is based on actual earnings or the state average wage for the employee's position.

The cost

Rates for coverage are determined by a rating bureau, which sets the baseline cost for insurance premiums. Some states have their own rating bureau, but most rely on private companies that provide rate recommendations based on collective data and trends, including business risks, benefit levels, state-specific regulations and health care costs.

Premiums vary by location and type of industry. Employers with annual premiums above a certain level can usually benefit from a good “experience rating,” which considers the company’s claim history as compared to others in the same industry. Demonstrating an ongoing culture of safety with few claims can help your rating.

Beyond state borders

Your workers’ comp policy includes a “Declarations” section, which names the specific states included in your policy.

What happens if an employee is injured in a state not named?

If that state has workers’ comp benefits that are more generous than the state(s) included in your policy, the employee can file a workers’ comp claim there, and you are left completely liable.

To solve this, you can have an “Other States” section added to your policy to name specific states where employees may occasionally work.

Be aware that this “Other States” section does not apply when only state-fund workers’ comp is allowed there or if you have regular operations in one of those states. If you do add a new state to your geographic operations, let your insurance professional know so it can be added to the “Declarations” page of your policy instead.

Are there any exceptions?

Sole proprietors and partnerships are typically excluded from workers’ comp requirements. However, if they elect to purchase coverage anyway, most states allow access to workers’ comp policies.

Once a non-owner employee is added to the business — including minors and non-citizens — mandatory workers’ comp may come into play. However, exceptions may remain (depending on the state), including:

- Any employees paid solely on commission
- Businesses with a limited number of employees — usually three to five
- Employees who are immediate family members of the business owner, such as a parent, spouse or child, with siblings and in-laws typically excluded from this “immediate family” definition

An important note for employers who use independent contractors: Most states consider uninsured contractors, subcontractors or employees of an uninsured subcontractor as *your* employee. This leaves you liable for any injuries they sustain while working for you. To provide some protection against this, it is wise to require any contractor or subcontractor to provide proof of their own workers’ comp coverage.

Nevertheless, this does not completely absolve you of responsibility, so, depending on your industry, you may still want to consider coverage. Your insurance professional can help you measure cost versus risk.

Key obligations

In addition to confirming coverage details, be sure to understand your policy obligations. In most states, you are required to keep accident records and report work-related accidents to the state workers' comp board and your insurer within a specific number of days. This requirement is mutually beneficial; studies show that faster injury reporting speeds medical treatment and benefit payments, which improves recovery time and employee satisfaction.

Be aware that employers are not typically protected by their workers' comp policy when they are found intentionally negligent or there are instances of sexual harassment, psychological stress or violation of migrant worker laws.

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