



Testimony to the Legislature for Workers' Compensation Reform

House Bill 2486 & Senate Bill 2961

Submitted by:
STATE OF HAWAII
Department of Labor and Industrial Relations

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Executive Summary

OVERVIEW

This report is designed to provide the legislature and the public an overview of Hawaii's workers' compensation system, historical data from 1995 to 2002, and the Department of Labor and Industrial Relations' ("Department") justification and testimony for the Administration's Workers' Compensation Omnibus bills (H.B. 2486 and S.B. 2961). The Department will also explain the internal steps it is taking to address the soaring costs of workers' compensation in Hawaii.

The Department believes that opportunities for cost savings in H.B. 2486 and S.B. 2961 are substantial. Further, the Department believes we can maintain quality access to health care while containing or even reducing costs.

The State of Hawaii is poised for a construction boom as multi-billion dollars military housing projects are slated to begin in mid 2004. These projects are expected to last 10 years and will add jobs in construction and many other industries. The creation of these new jobs will expose more workers to work injuries, which we expect will likely increase workers' compensation claims. The Department, however, is committed to avoiding the mistakes of states such as California and Florida and is proactively taking steps to ensure its workers' compensation system does not impede and hinder the orderly growth and economic development of our state.

In 2002, the state of Oregon's annual Premium Rate Ranking for workers' compensation reported California and Florida as #1 and #2 for having the highest premium rates. Hawaii ranked #3. To put this in perspective, Hawaii's employees on an average paid \$3.48 for every \$100 they pay in wages. Both California and Florida have had to undergo drastic reform of their workers' compensation system in order to protect and relieve local employers from these burdensome costs.

The Department stresses that there is no "silver bullet" or single item that will help drive workers' compensation costs down. Rather, it is a multitude of structural and policy changes that need to be addressed.

FUNDAMENTAL COST DRIVERS

There are three fundamental issues that drive workers compensation costs nationwide: (1) workplace accidents, (2) administrative interference, and (3) duration.

An employer's ability to reduce and eliminate workplace injuries and illness, promptly treat and compensate the injured employee, and then return that person to work in the most expeditious manner greatly reduces costs. In Hawaii, employers have drastically reduced workplace injuries by 29%, since 1995, yet their cost per case has increased substantially.

Administrative interference is the burden placed upon employers and employees by the Department. These burdens include antiquated processing of workers' compensation claims, outdated rules and procedures that are either unclear or unwritten, and arbitrary patterns of practice that in all, delay the resolution of claims while in the department and adds to the cost of the claim.

MAJOR LEGISLATIVE RECCOMENDATIONS

- Clearly define and delineate who can be an attending physician. Provide a "gate keeper" system for employees and employers.
- Define and reasonably manage palliative care to minimize the cost, and likely abuse in this area.
- Redefine employment exemptions, allowing owners of small businesses to be exempt from paying workers' compensation insurance on themselves. This measure exempts anyone having a 50% interest in limited liability corporations, limited liability partnerships, and sole proprietorships from obtaining workers' compensation coverage.
- Define Medical Maximum Improvement to clearly establish when an injured employee is entitled to temporary total disability payments versus permanent total disability, and temporary partial disability, or permanent partial disability.
- Eliminate stress claims resulting from personnel action taken in good faith.
- Allow for employer-mandated choice of physician.
- Allow third parties to recommend an actuary to the director, which may be used to update the medical fee schedule.
- Clearly define acceptable Vocational Rehabilitation plans to control costs and allow greater employer input.
- Remove the minimum requirement for injured employees receiving temporary partial disability benefits.
- Create guidelines for arbitration and mediation of workers' compensation cases to allow and encourage parties to resolve claims through alternative dispute resolution. Arbitration and mediation will be efficient and cost-effective in resolving claims.
- Allow the Insurance Fraud Unit of the insurance Commissioner's office to investigate workers' compensation fraud.
- Allow emergency room providers to be reimbursed for usual and customary fees, not to exceed 200% of Medicare, for emergency room treatment during the first 48 hours after point of injury. This will ensure that injured workers receive the best care and treatment during their critical time of need.

SECTION I: INTRODUCTION

OVERVIEW

The Hawaii Territorial Legislature adopted the state's first Workers' Compensation law in 1915. The Workers' Compensation Law was enacted to ensure that employees who were injured or disabled on the job were provided with medical treatment and fixed monetary awards (indemnity). This law was Hawaii's first "no-fault" legislation in that it mandated there be a presumption that an employee's injuries were "work-related", while prohibiting an employee from filing civil actions against the employer for work-related injuries or illnesses.

Under current law, the employee sustaining a work-related injury or illness is entitled to medical treatment, wage loss benefits, permanent disability indemnity, disfigurement and death benefits. Any employer, including the State and County governments, employing one or more workers is required to provide workers' compensation coverage.

HISTORY

There have been two attempts in the 1990's to reform the state's workers' compensation system due to overwhelming pressure from both Hawaii's small business owners and labor officials seeking relief from the soaring costs associated with workers' compensation. The first effort was in 1995 with the enactment of Act 234, Session Laws of Hawaii. Act 234 was primarily targeted at controlling medical costs by establishing a medical fee schedule, which generally limits the reimbursement rate for medical services at 110% over Medicare. This Act also provided clear guidelines for what constitutes fraud and establishing penalties, and incentives for safety and health programs to reduce workplace injuries.

The second attempt to control workers' compensation costs occurred one year later in 1996 with the enactment of Act 261, which established the Hawaii Employers' Mutual Insurance Company ("HEMIC"). The legislature found that despite the reforms passed in 1995, many of Hawaii's small businesses were unable to find affordable insurance and were being unfairly placed in the state's assigned risk pool, which was established for high-risk employers. HEMIC was created to provide workers' compensation coverage to not only the high-risk employers, but to those small business employers who were unable to obtain insurance otherwise. In 1996, the state's assigned risk pool had 30% of Hawaii's businesses.

In 1994, Hawaii processed 61,353 workers compensation cases at an average cost of \$5,592 per case. Hawaii also ranked third in the nation that year in workers' compensation premium rate rankings. The premium rate ranking is compiled and adjusted by the Research and Analysis Section of the Oregon Department of Consumer and Business Services and reflects the amount of money spent on premiums for every \$100 of payroll wages.

In the eight years since the 1995 workers' compensation reform, the cost per case for workers' compensation has risen to an average of \$6,162. Once again, Hawaii is third in the nation in premium rate rankings. These increases have occurred even though workplace injuries and processed workers' compensation cases have significantly decreased by 29% from 1994 to 2002.

SECTION II. DISCRPTION OF DISABILITY BENEFITS

INDEMNITY BENEFITS

1. **Permanent Partial Disability ("PPD")**

Once an injured employee reaches the point of stability or maximum medical recovery, the employee may be sent to a physician to evaluate the extent of any permanent impairment. The evaluation will be used to determine the extent of the disability, which establishes the amount an employer will pay the employee for that partial disability. This is called a PPD award. PPD is an indemnity benefit and is payable even if the worker has returned to work.

PPD payments are calculated by multiplying the effective maximum weekly benefit rate (66 2/3% of wages) by the number of weeks specified for each disability in section 386-32, Hawaii Revised Statutes ("HRS").

2. **Disfigurement**

If an injury results in a permanent disfigurement, an employee may be entitled to additional compensation. Disfigurement includes scars, deformity, and discoloration. Laceration scars and surgical scars are reviewed six months from the date of occurrence; however, burn scars are evaluated after one year. Disfigurement awards are statutorily capped at \$30,000 and are separate from permanent partial disabilities.

3. **Death Benefits**

Where an industrial injury results in death, the surviving spouse and dependent minor children (including full-time students up to 21 years of age) are entitled to weekly benefits as provided in the workers' compensation law. Funeral expenses up to 10 times the maximum weekly benefit rate and burial expenses up to 5 times the maximum weekly benefit rate are also allowed.

WAGE LOSS BENEFITS

4. **Temporary Total Disability ("TTD")**

TTD payments are made to an injured employee if they are unable to work due to an injury that is not permanent in nature. TTD payments are temporary wage replacement benefits for the employee until they are able to return to work. TTD payments are calculated the same as PTD payments, which are equal to 66 2/3% of an employee's average weekly wage.

5. **Temporary Partial Disability ("TPD")**

TPD payments are made to employees who have an injury that causes partial disability that is not permanent, which diminishes the employee's ability to work. The employer must pay weekly TPD payments at the weekly benefit rate of 66 2/3% of the difference between the employee's weekly wages before the injury and the employee's wages after the injury.

6. **Permanent Total Disability ("PTD")**

If an employee is permanently injured on the job and unable to perform any kind of work, the employer pays the injured worker PTD payments. An employee's eligibility for PTD benefits is determined at a hearing held by the Department's Disability Compensation Division ("DCD").

PTD payments are calculated to equal 66 2/3% of an employee's average weekly wage, but no

more than the maximum weekly benefit amount annually set by the Disability Compensation Division. The current 2004 maximum weekly benefit amount is \$596.00.

7. Concurrent Employment Benefits

If an injured employee has two or more jobs and cannot work either job because of an injury they sustained on one of those jobs, they may be eligible for additional benefits from the Special Compensation Fund ("SCF"). The SCF will cover benefits from the second job that the employee worked at before being injured at the first job.

CLAIM MANAGEMENT

8. Vocational Rehabilitation ("VR")

If an employee has suffered permanent disability but can be vocationally rehabilitated, the employee is eligible for VR services to be paid by the employer. The injured employee selects his or her own certified provider of rehabilitation services. The employer or its insurance carrier may challenge the employee's right to vocational rehabilitation services. The injured employee is also entitled to collect TTD payments from the employer while enrolled in a VR program.

SECTION III: COMMON DEFINITIONS

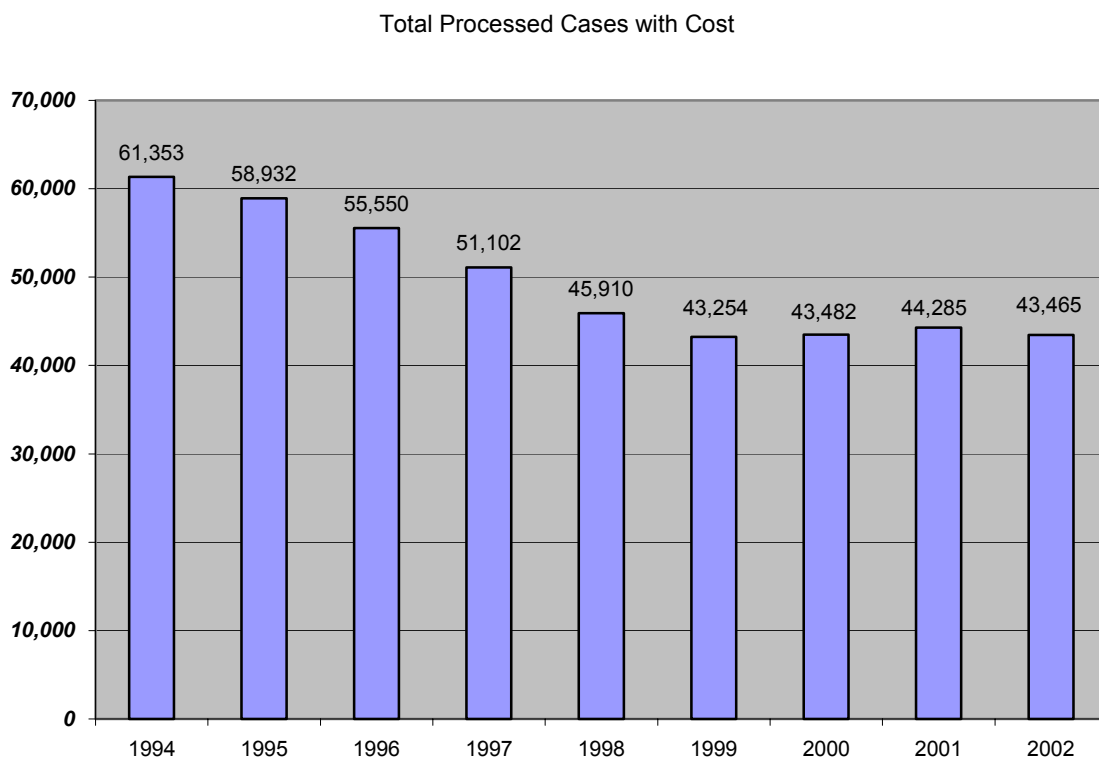
| | |
|---|---|
| Attendant Services | Cost of services of an attendant for a totally disabled employee. |
| Average Cost Per Case | Total compensation costs divided by the number of processed cases with cost. |
| Compensation Orders | Decisions made on controverted cases, on awarding of permanent partial disability and disfigurement, and on reopening cases. |
| Costs | All payments accorded to a claimant to include disability, death, disfigurement, vocational rehabilitation, attendant services, and medical payments. |
| Days Lost | Number of compensated days in which injured workers were not able to work because of temporary total disability. This excludes the three-day waiting period. |
| Disfigurement | Scar, deformity, discoloration, or other disfiguring consequences resulting from an injury or caused by medical, surgical, and hospital treatment of the employee. This is separate from permanent partial disability. |
| Employment | That portion of the work force covered by Workers' Compensation law. Annual average taken from the "Employment and Payrolls in Hawaii" report excluding federal government employees. |
| Event or Exposure | Identifies the circumstance which directly resulted in the injury or illness. |
| Industry | Identifies employers by the major type of activity in which they are engaged. |
| Medical | Costs for physicians, hospital care, medical and services and supplies. |
| Nature of Injury or Illness | Identifies the injury or illness in terms of its principal physical characteristic. |
| Occupation | Identifies the nature of work of the employee. |
| Part of Body | Identifies the part of the worker's body directly affected by the injury or illness. |
| Permanent Partial Disability | Injury or illness which results in the complete loss of any member or part of the body, or any permanent impairment of functions of the body or part thereof, regardless of any pre-existing disability. |
| Permanent Total Disability | Any injury or illness other than death, which permanently and totally incapacitates an employee from obtaining any gainful occupation. |
| Processed Cases | Cases which have been subject to screening procedures, where the injury or illness has been medically evaluated, and where all medical costs and workers' compensation payments have been calculated. Includes injuries and illnesses, which occurred in the report year or prior years. |
| Reported Injuries and Illnesses (Reported Cases) | All injuries and illnesses reported to the Disability Compensation Division. These reported injuries or illnesses may not have occurred during the report year. |
| Reported Fatalities | Any death resulting from an on-the-job injury or illness reported to the Disability Compensation Division |
| Source of Injury or Illness | Identifies the object, substance, exposure, or bodily motion, which directly produced or inflicted the injury or illness. |
| Temporary Partial Disability | A work injury or illness which causes partial rather than total disability for temporary periods. The injured worker is paid a weekly benefit amount of 66-2/3 percent of the difference between his average weekly wages before the injury and his weekly earnings thereafter for the duration of the disability. |
| Temporary Total Disability | A common type of disability where the work injury or illness causes total disability for temporary periods. The employer or insurance carrier pays the injured worker a weekly benefit amount of 66-2/3% of his/her average weekly wages for the duration of the disability. However, the benefit amount does not include the first three days of injury, and is neither more than the maximum weekly benefit amount nor less than the minimum weekly benefit amount. If the worker's average weekly wages are less than the minimum weekly benefit amount, the worker will be paid at a rate of 100 percent of his average weekly wages. |
| Vocational Rehabilitation | Cost of physical and vocational rehabilitation services. |

SECTION IV: ISSUES

1. Act 234 (1995) and Act 261 (1996) have been successful in promoting a safe and healthy workplace. Hawaii's employers have created an environment that has fewer workplace accidents.

In 1995, the total processed workers' compensation cases with cost totaled 58,932. Due to increased safety and health programs enacted by Hawaii's employers, workplace injuries have been reduced to 43,465 in 2002.

Act 234 offered workers' compensation premium discounts for employers that implemented a certified, and effective, safety and health plan. Further, the legislative mandates of Act 261, requires HEMIC to vigorously promote and provide a high standard of workplace safety to those companies that it is required to provide workers' compensation coverage to.



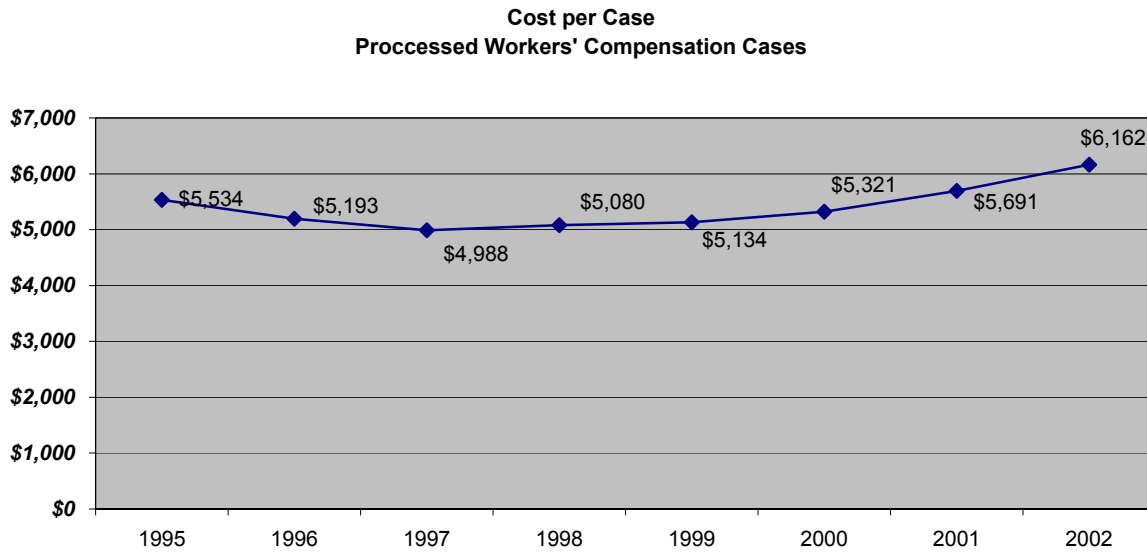
Graph 1. Department of Labor and Industrial Relations, State of Hawaii

This reduction represents a 26% decrease over eight years in the amount of work related injuries that require cost. Hawaii's employers should have seen instant and sustained savings as medical costs and lost days should have decreased concurrently with the declining injuries.

These savings were initially realized as total cost per case did decline for the first two years. However, medical, indemnity and wage replacement benefits began to rise in 1997, despite the decline of injuries in the workplace.

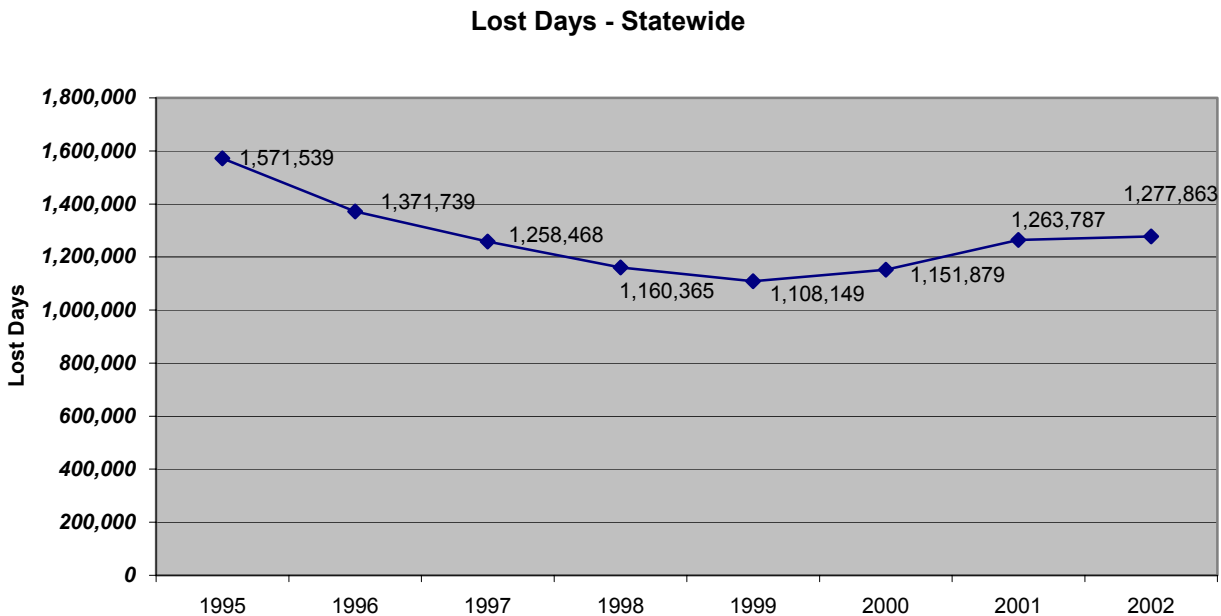
2. The cost containment measures of Act 234 have not been effective. Less claims have been filed on an annual basis. However, employers are now paying more per case for almost all benefit categories.

In 1995, the statewide average cost per case was \$5,534, as compared to \$6,162 in 2002.



Graph 2. Department of Labor and Industrial Relations, State of Hawaii

From 1995 to 1999 the state experienced a significant drop in Lost Days as claims decreased. However, even though cases have continued to decrease and stabilize, the state's Lost Days have increased steadily since 1999.

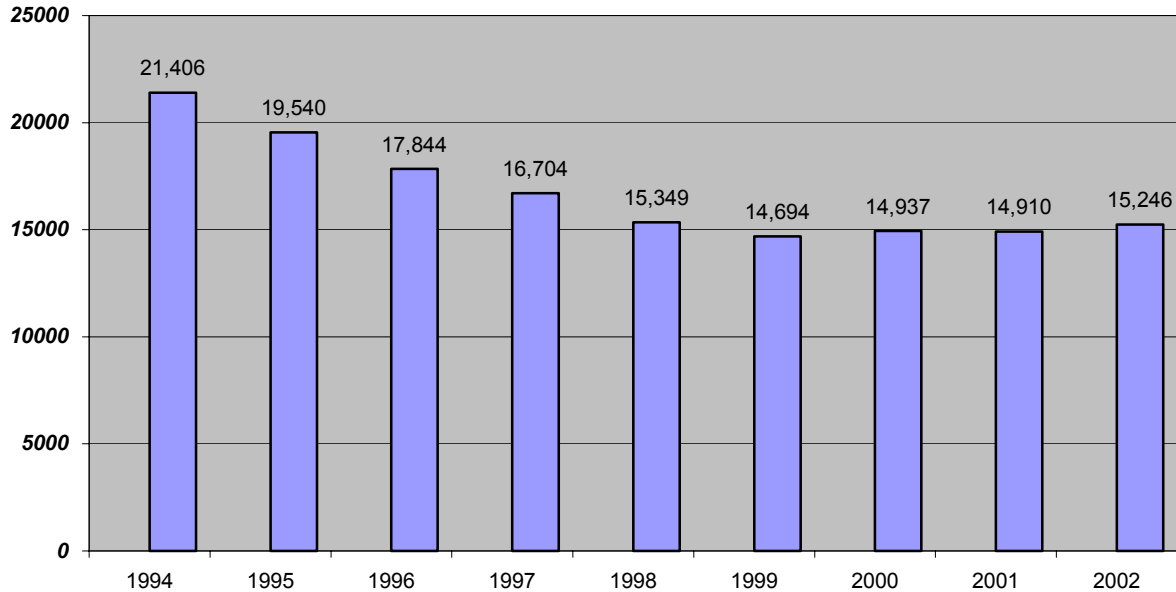


Graph 2.5. Department of Labor and Industrial Relations, State of Hawaii

The following graphs will show that while individual claims for indemnity, wage replacement and medical costs decreased over the past eight years, the costs associated with these benefits continue to escalate.

3. Statewide, temporary total disability cases have decreased by 21% since 1995 yet Hawaii's employers pay 17% more per TTD case.

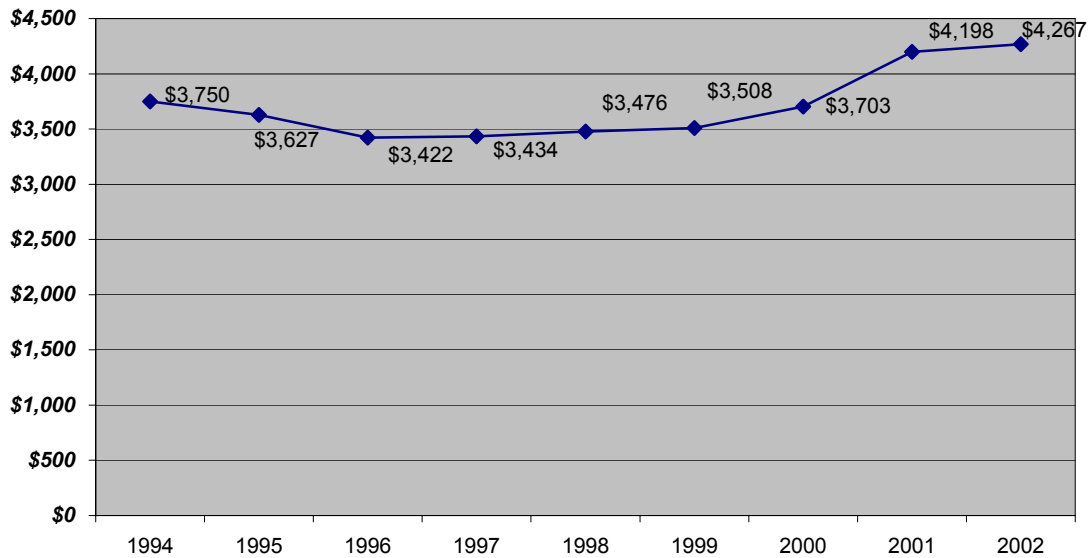
TTD Cases



Department of Labor and Industrial Relations, State of Hawaii

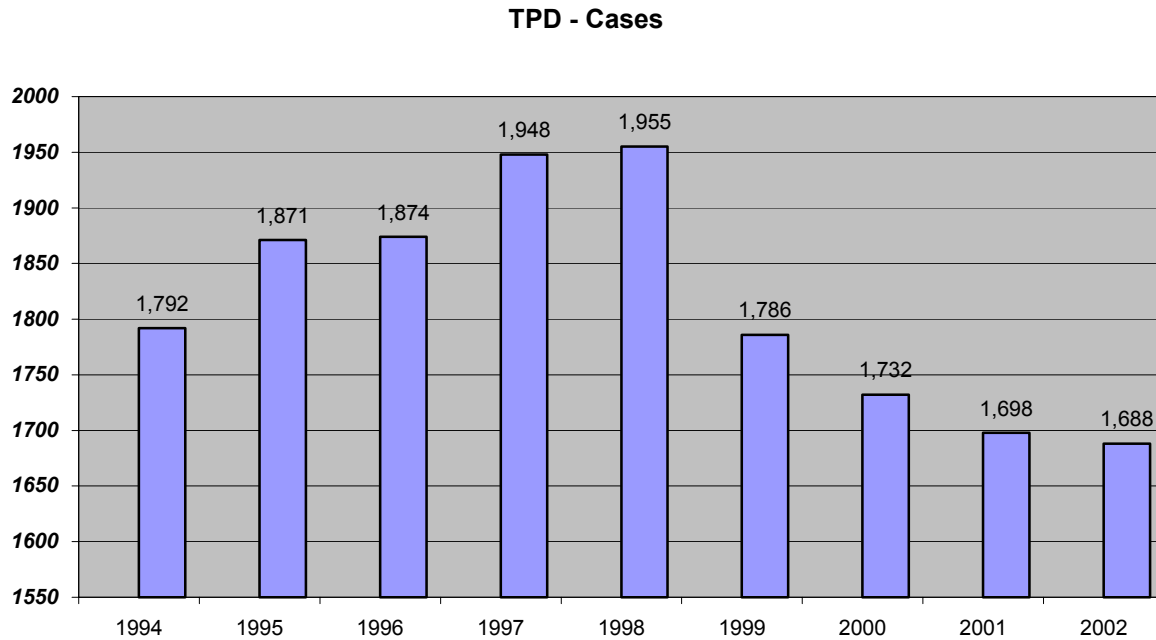
Graph 3.

TTD - Cost per Case

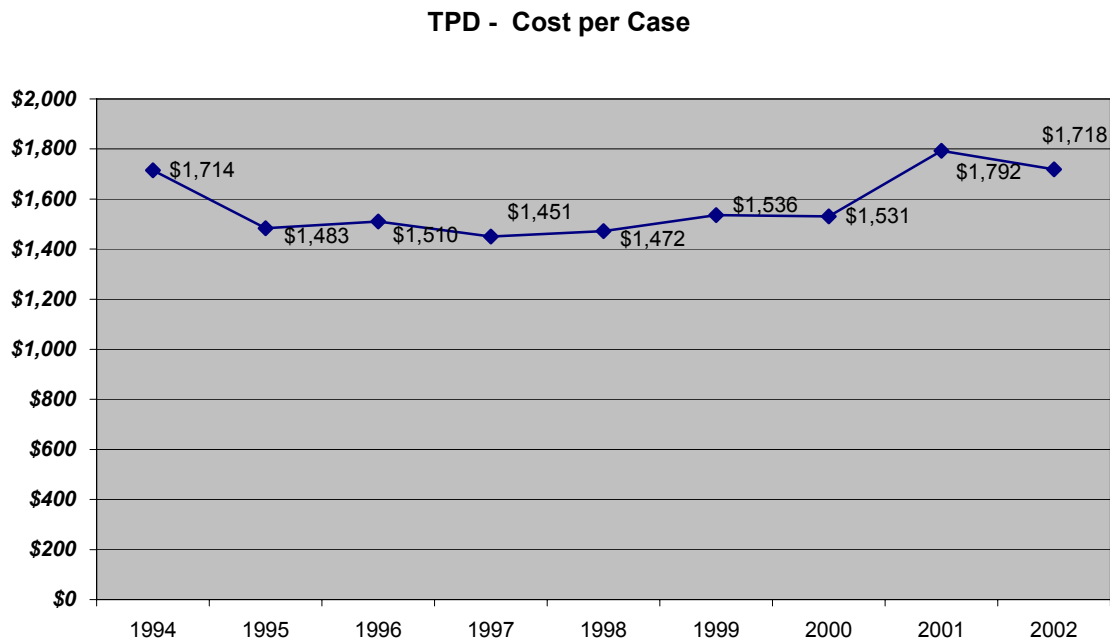


Graph 4. Department of Labor and Industrial Relations, State of Hawaii

4. Hawaii's Employers Are Paying More for TPD Cases. Temporary Partial Disability cases have decreased by 9% since 1995 yet Hawaii's employers pay 15% more per TPD case.

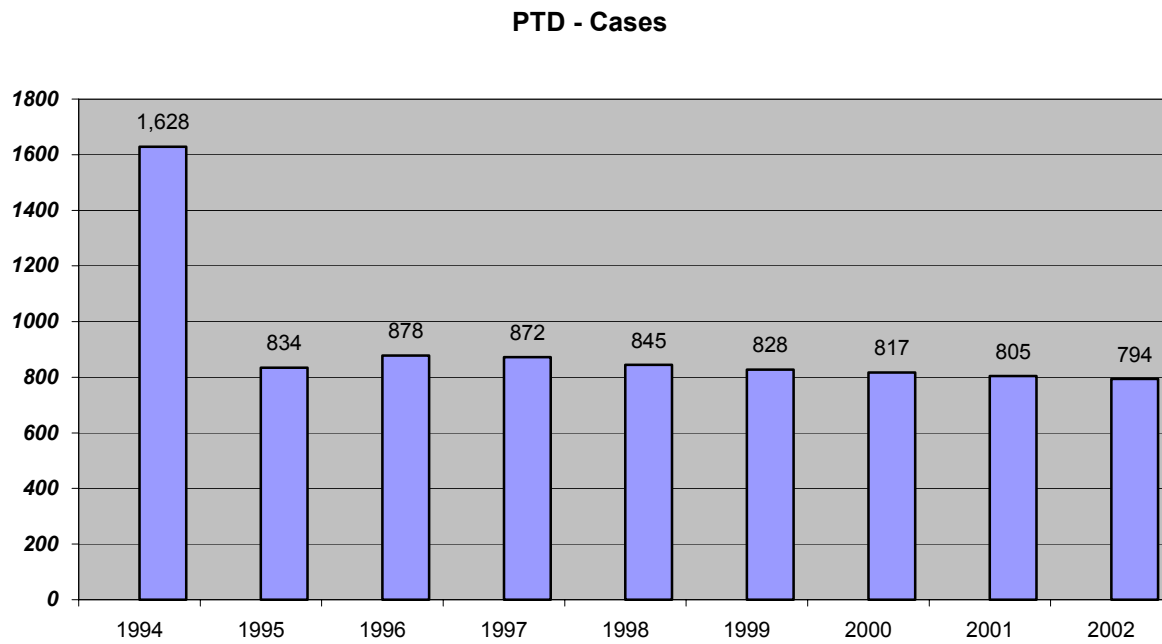


Graph 5. Department of Labor and Industrial Relations, State of Hawaii

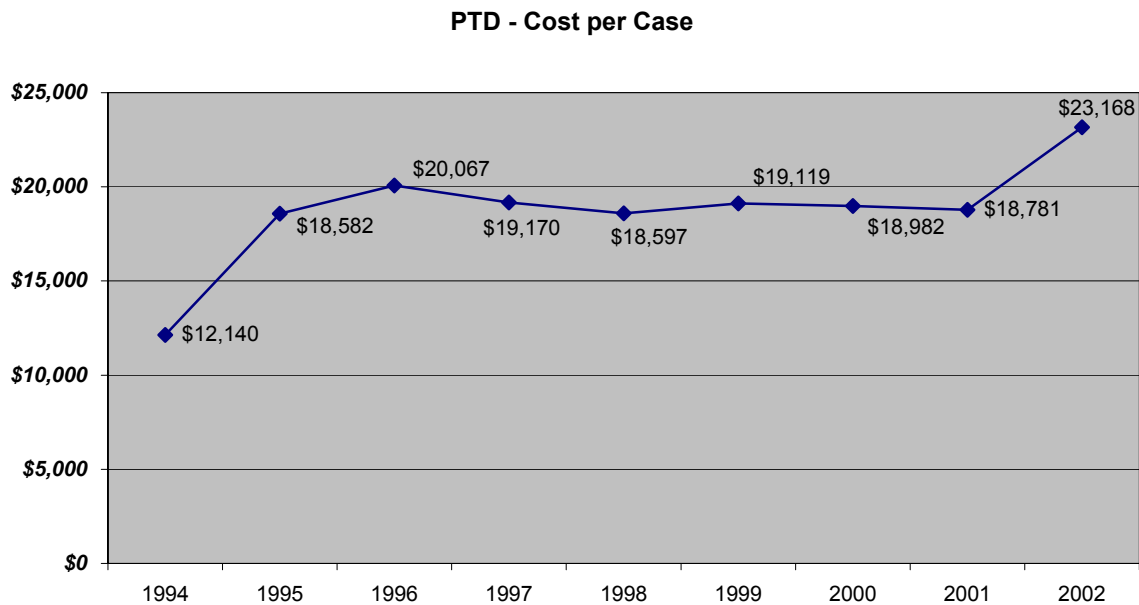


Graph 6. Department of Labor and Industrial Relations, State of Hawaii

5. Hawaii's Employers Are Paying More for PTD Cases. Permanent Total Disability cases have decreased by 4% since 1995 yet Hawaii's employers pay 24% more per PTD case.



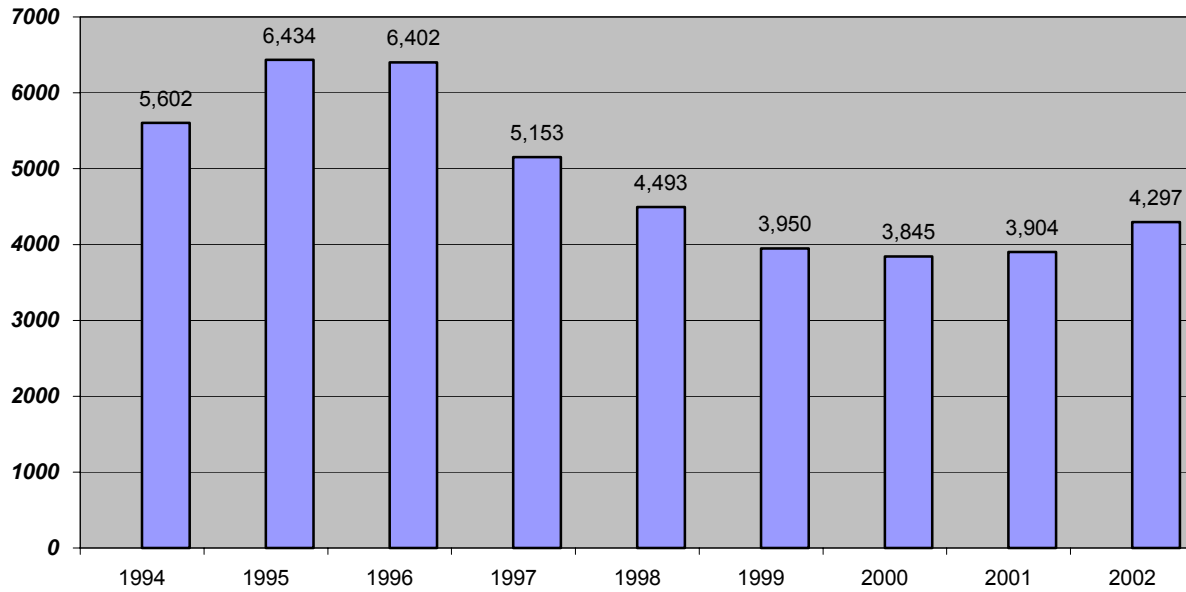
Graph 7. Department of Labor and Industrial Relations, State of Hawaii



Graph 8. Department of Labor and Industrial Relations, State of Hawaii

6. Hawaii's Employers Are Paying More for PPD Cases. Permanent Partial Disability cases have decreased by 33% since 1995 yet Hawaii's employers pay 2% more per PPD case.

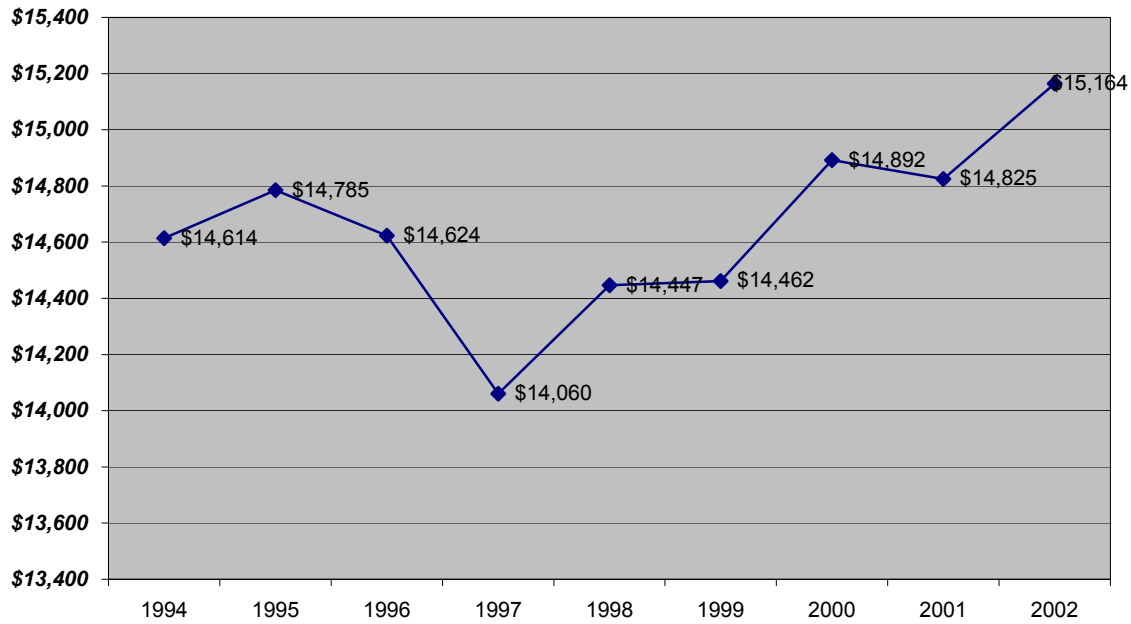
PPD - Cases



Department of Labor and Industrial Relations, State of Hawaii

Graph 9.

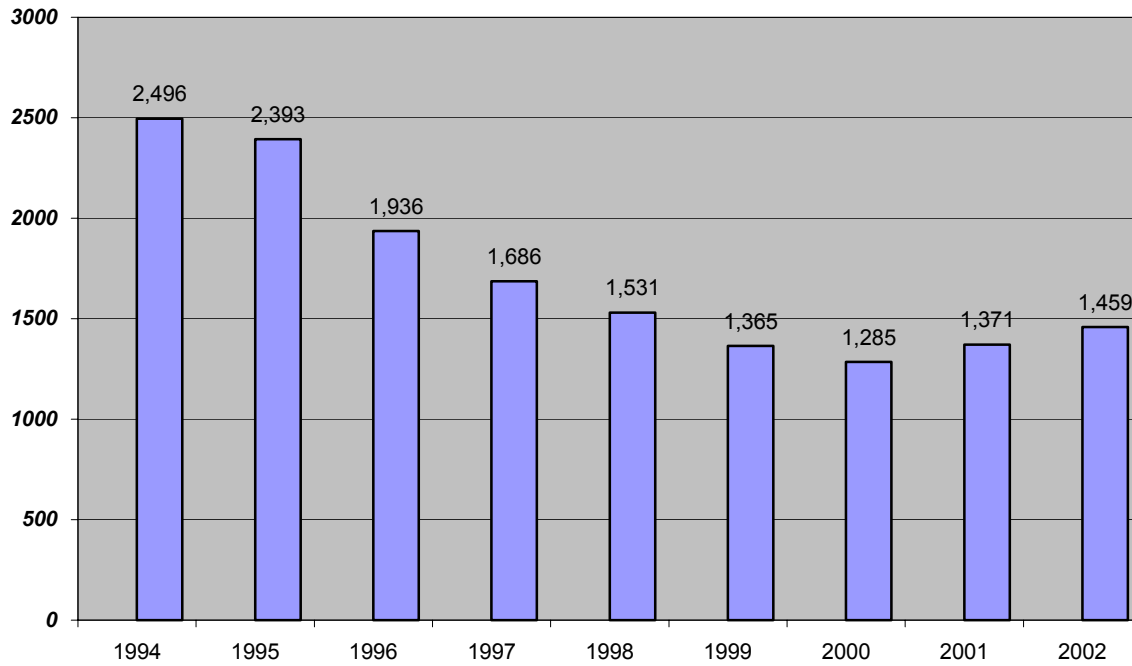
PPD - Cost per Case



Graph 10. Department of Labor and Industrial Relations, State of Hawaii

7. Hawaii's Employers Are Paying More for Vocational Rehabilitation. Vocational Rehabilitation cases have decreased by 39% since 1995 yet Hawaii's employers pay 31% more per VR case.

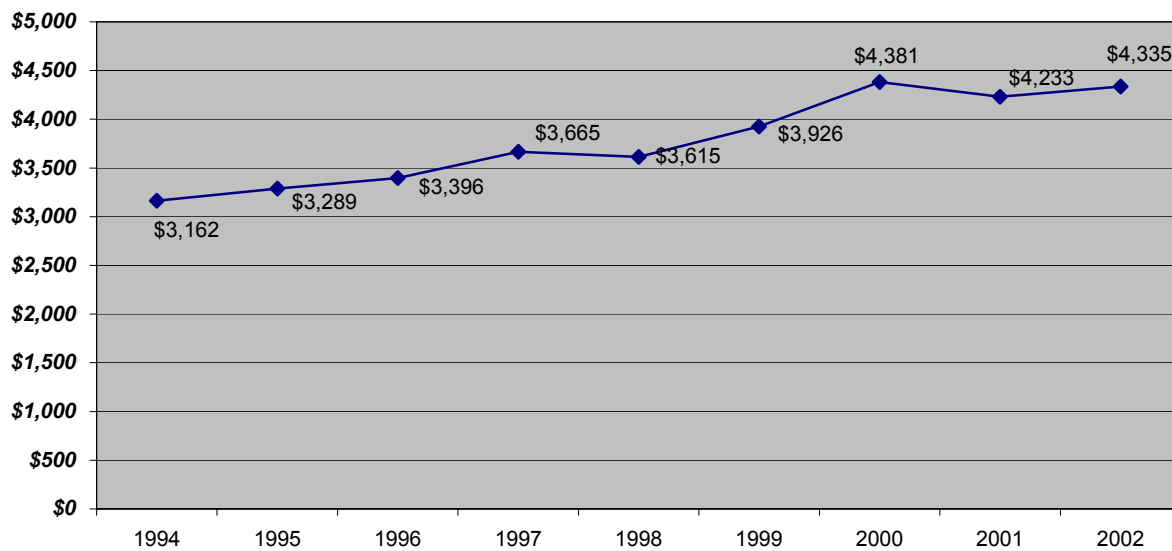
Vocational Rehabilitation - Cases



Department of Labor and Industrial Relations, State of Hawaii

Graph 11.

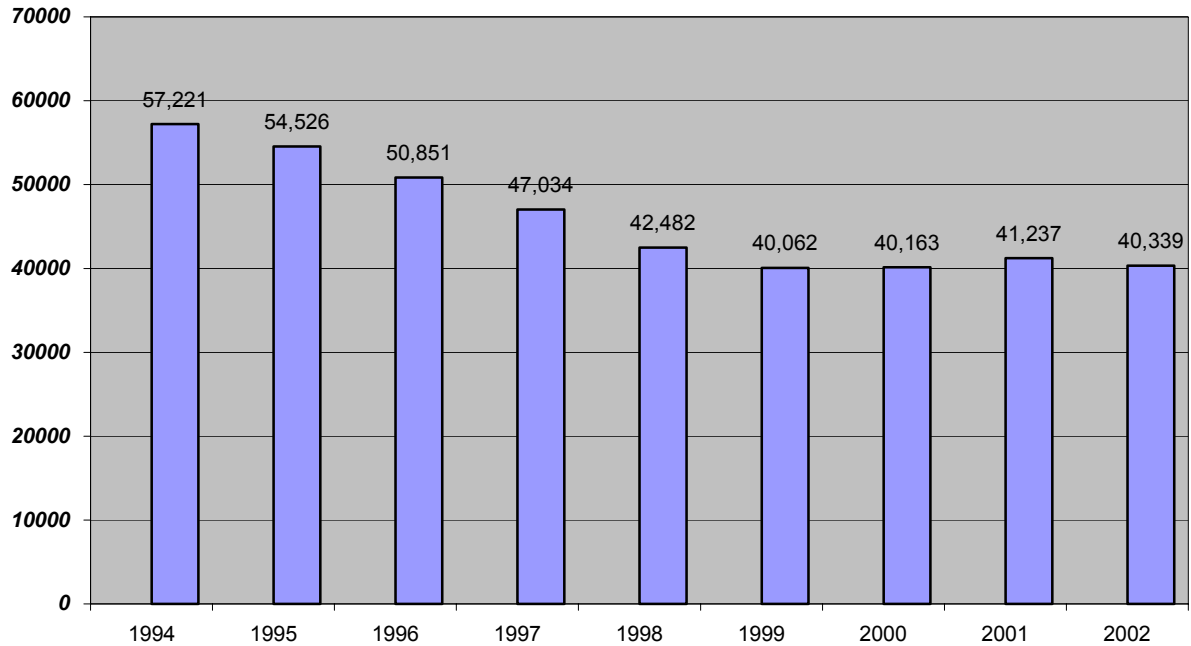
Vocational Rehabilitation - Cost per Case



Graph 12. Department of Labor and Industrial Relations, State of Hawaii

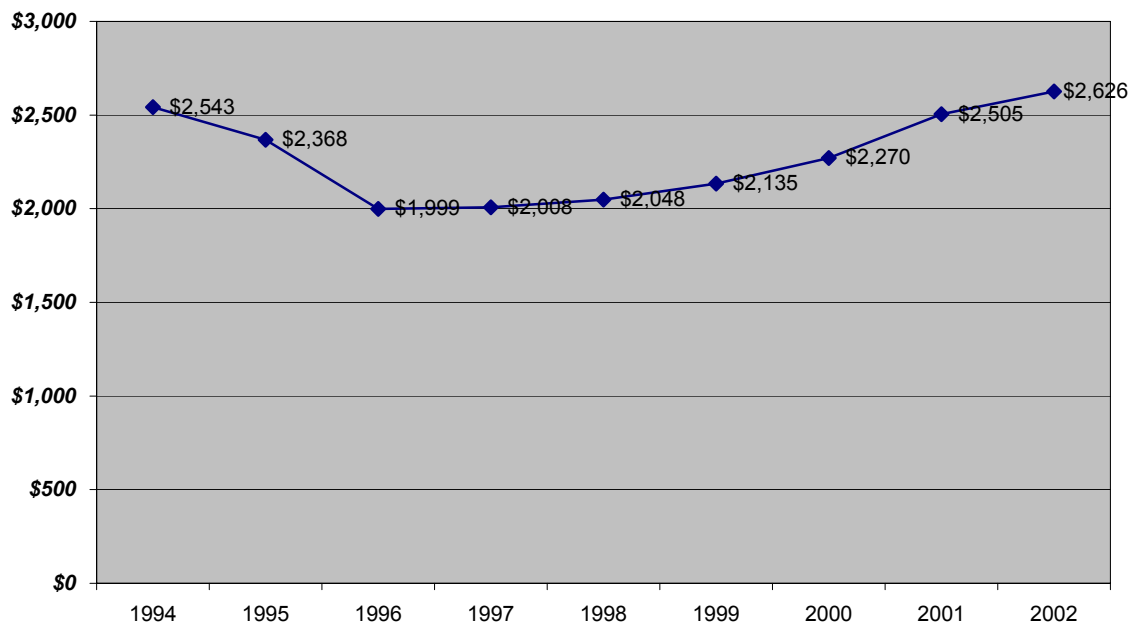
8. Hawaii's Employers Are Paying More for Medical Treatments. Medical cases have decreased by 26% since 1995 yet Hawaii's employers pay 10% more per medical case.

Medical - Cases



Graph 13. Department of Labor and Industrial Relations, State of Hawaii

Medical - Cost per Case

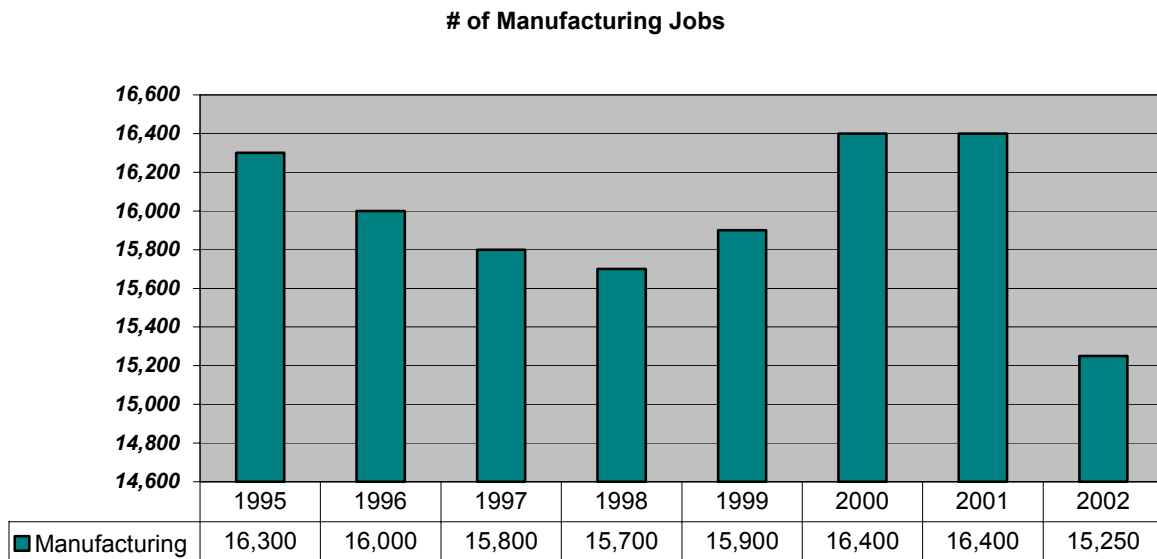


Graph 14. Department of Labor and Industrial Relations, State of Hawaii

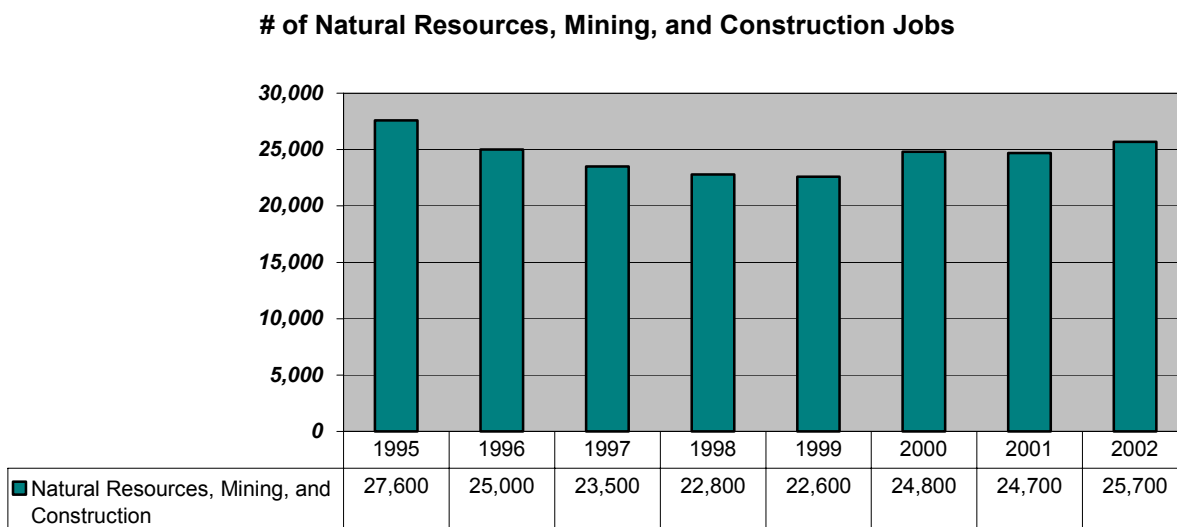
9. Why have costs per case escalated despite significant reductions in workplace injuries?

The major reforms of 1995 and 1996 sought to control costs by capping medical expenses at 110% of Medicare. As Graph 14 shows, the cost per case for medical expenses did, in fact, decline for 1996, however, costs began to escalate in 1997 to levels higher than in 1995.

The Department believes that some of the initial decrease in medical costs and the overall system are due to a number of factors, including the reduction of jobs in industries that are normally high in workplace injuries and illnesses such as construction, warehousing, retail trade, manufacturing, and professional, scientific and technical industries. The following graphs reflect those industries that greatly contribute to claims in the workers' compensation system. The graphs indicate a loss of jobs during the calendar years 1995 to 1997.

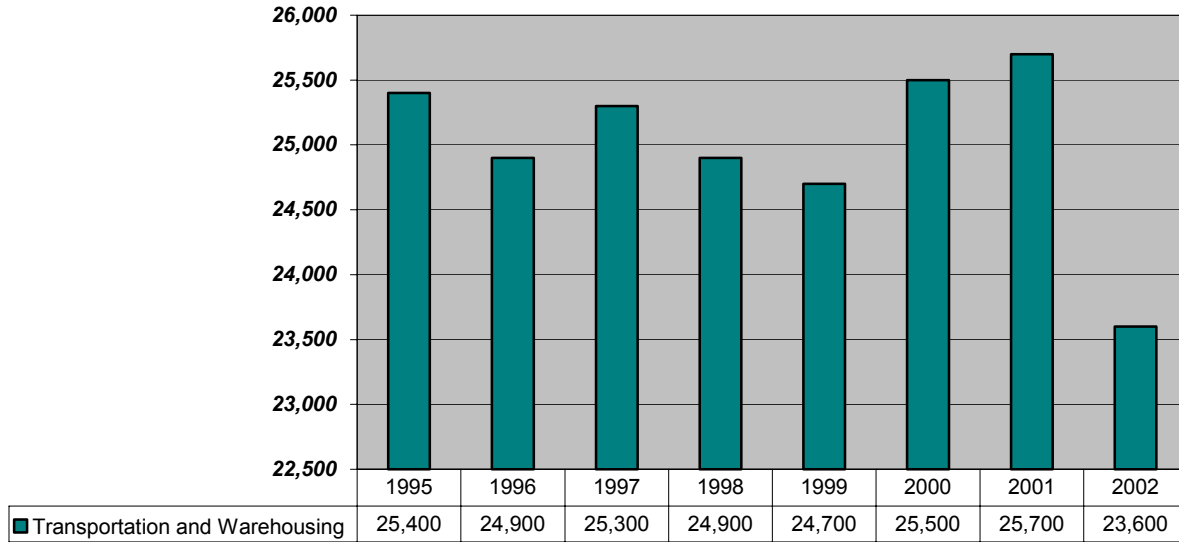


Graph 15. Department of Labor and Industrial Relations, State of Hawaii



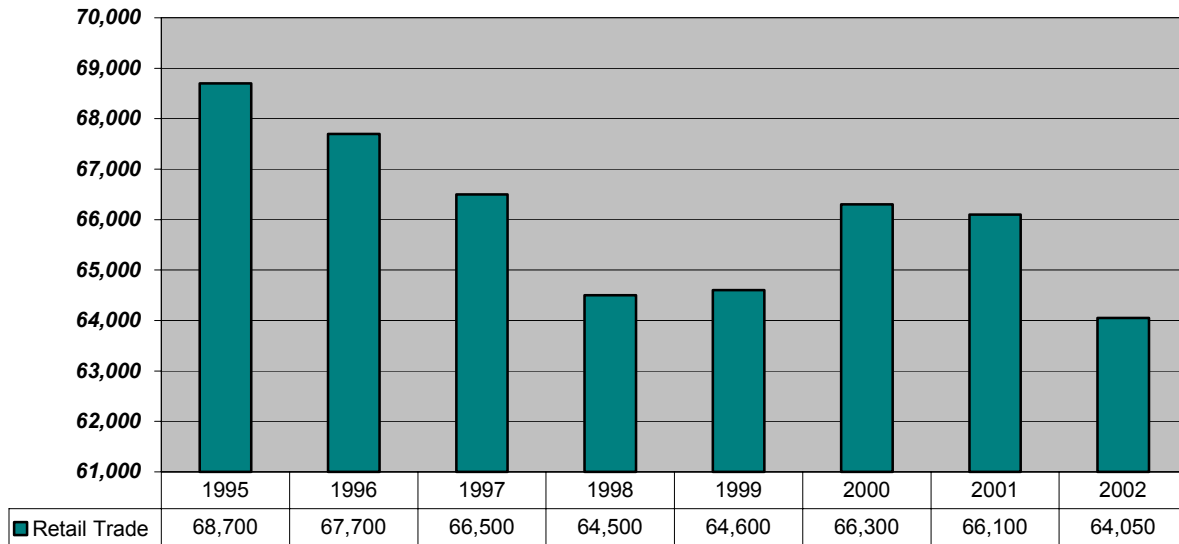
Graph 16. Department of Labor and Industrial Relations, State of Hawaii

of Transportation and Warehousing Jobs



Graph 17. Department of Labor and Industrial Relations, State of Hawaii

of Retail Trade Jobs



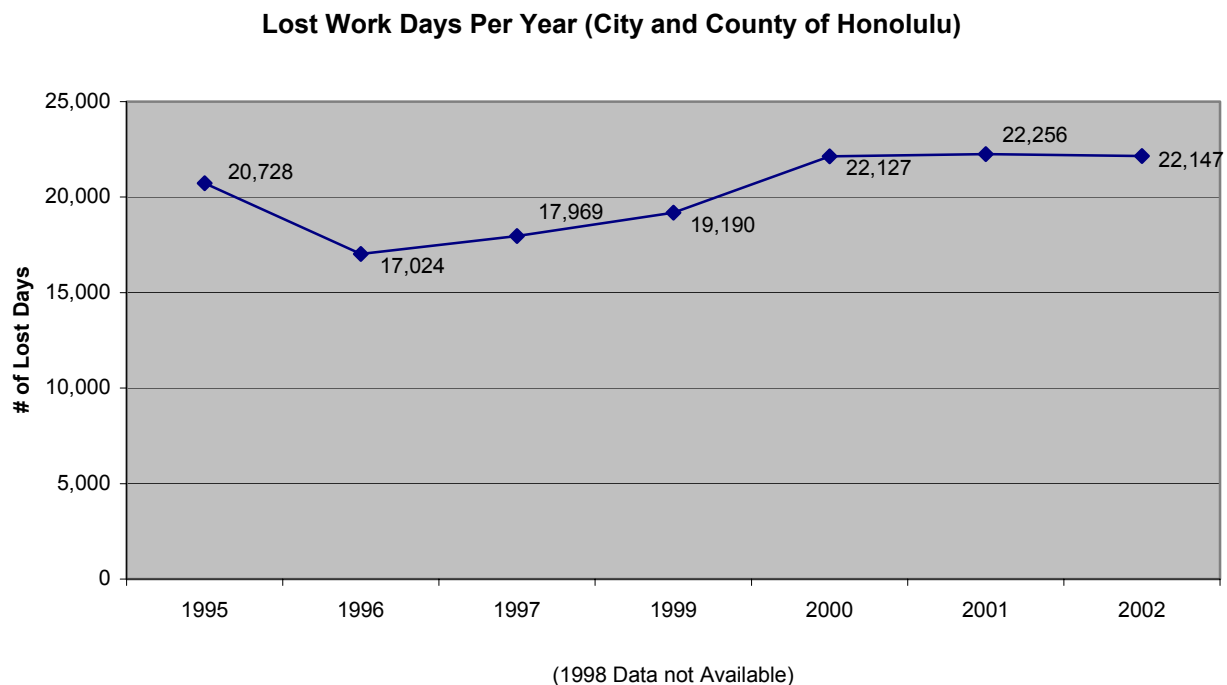
Graph 18. Department of Labor and Industrial Relations, State of Hawaii

The Department also believes that for the initial year following the reforms of Act 234 and Act 261, the law worked as it was intended in controlling medical costs and reducing workplace injuries. Unfortunately, the historical data also shows that wage replacement and indemnity benefits increased despite these factors. The data suggests that some healthcare providers adjusted to the lower payments by extending the duration of time an injured worker remained in the system and out of work.

CITY AND COUNTY OF HONOLULU

In order to confirm statewide results, as well as obtaining a perspective on how the 1995 and 1996 reforms have affected Hawaii's individual employers, the Department reviewed the experience of the City and County of Honolulu ("City"). The Department examined the City's "Lost Days" and compared it to their yearly TTD costs, medical costs and amount of claims processed from 1995 to 2002. The data shows that the City experienced an immediate decrease in expenditures during the first two years after the 1995 reform. However, in 1997, while claims continued to decrease, costs and lost workdays began to substantially rise.

The City and the Department agree that the correlation between increases in TTD, medical costs, and lost workdays are revealing. While the types and severity of injuries have not changed in the past eight years (only the frequency), the data indicates that injured employees are being treated longer, thereby delaying their return.



19. City and County of Honolulu and Department of Labor and Industrial Relations, State of Hawaii

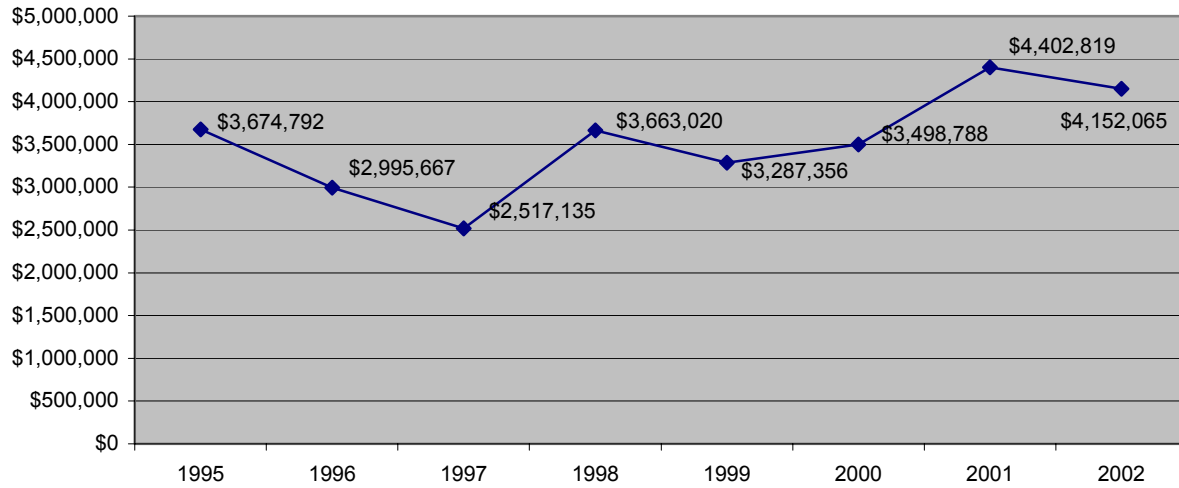
Graph

In 1995, the City had 788 loss time injuries as opposed to 515 loss time injuries in 2002. As graph 20, 21, and 22 illustrate, medical costs and TTD payments (City and statewide) did indeed decrease the initial two years after implementation of Act 234.

Act 234 is not a long-term solution. If Act 234 had been successful in the long term, TTD, medical, and lost days should have either continued to decrease at least stabilized.

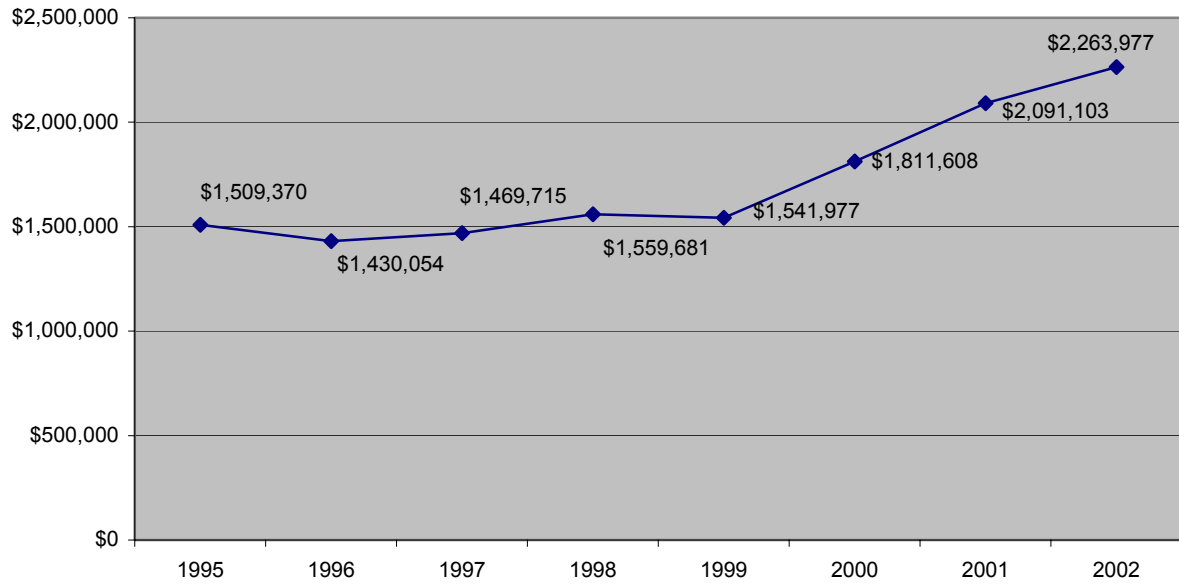
Instead, in 1997, while injuries continued to decline, medical, TTD, and lost days began to escalate. The increase of payments in TTD benefits (payments to injured workers who are not permanently disabled) clearly indicates a development of a trend - injured employees are staying out-of-work longer, and therefore, increasing their workers' compensation payments.

Medical Cost Per Year (City and County of Honolulu)



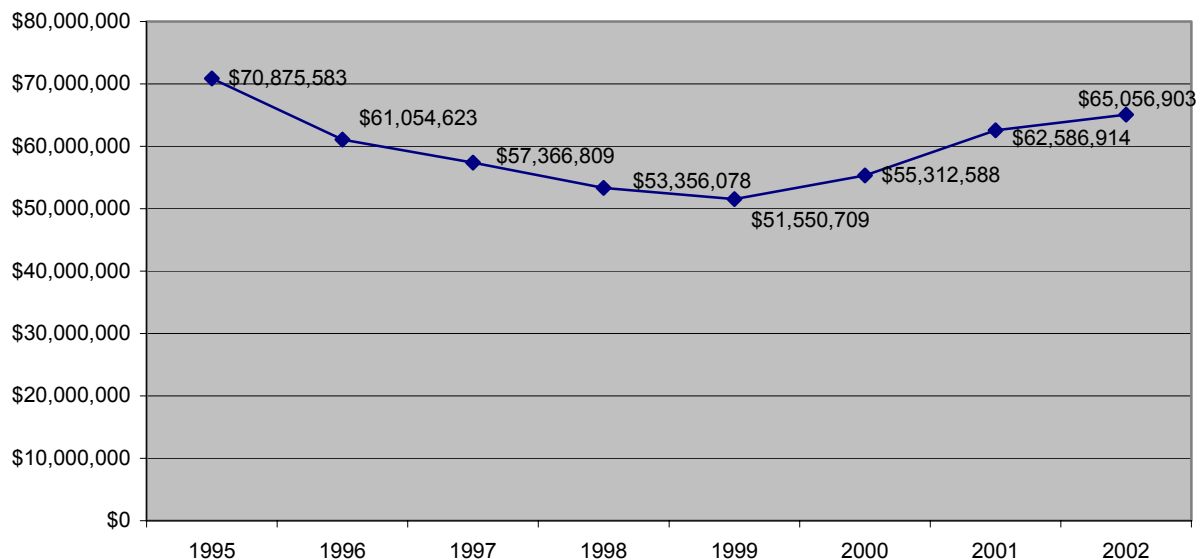
Graph 20. City and County of Honolulu and Department of Labor and Industrial Relations, State of Hawaii

TTD Payments Per Year (City and County of Honolulu)



Graph 21. City and County of Honolulu and Department of Labor and Industrial Relations, State of Hawaii

Total TTD Costs Per Year (State of Hawaii)



Graph 22. Department of Labor and Industrial Relations, State of Hawaii

The City has noted that in 1995, when the state legislature was proposing to cap medical fees at 110% of Medicare, members of the medical community who opposed this reform had predicted that if fees were decreased, providers would make up for the lower fees by treating injured employees longer. The data supports that prediction.

10. Hawaii's medical costs comprise only 40% of the overall cost of workers' compensation with indemnity comprising the other 60%.

Some argue that “medical costs are not high” because they comprise an average of only 40% of a workers' compensation claim. Since the 1940's, medical costs in Hawaii have always comprised only 40% to 45% of total workers' compensation costs. In 1995, medical costs comprised 40% and dropped to 35% in 1996. Medical costs have steadily increased back to the 40% level. The only difference is that on average, we pay (in dollars) more medical costs per case now than we did in 1995.

If the Act 234 reforms were effective, medical costs should have stabilized at 35% to 37% of the total costs for workers' compensation. The legislature did not decrease indemnity and wage replacement benefits, so indemnity costs should have stabilized to 70% of the total costs.

Factoring in that injuries had decreased during this time, total costs should have mirrored the declining injury rate. However, in two years time, medical costs for the state began to adjust back to 40% of the total costs with indemnity and wage replacement comprising 60% and all costs beginning to rise.

11. The rise in workers' compensation costs is due to three significant factors: (1) longer duration of cases, (2) care provided by healthcare providers other than non-medical doctors, and (3) inadequate control of vocational rehabilitation plans.

Act 234 capped medical fees, which health care providers can charge, at 110% of the Medicare Resource Based Relative Value Scale system ("Medical Fee Schedule"). This protected employers from the escalating costs associated with health care on the open market. An increase of the "market cost" of a surgical procedure would not increase costs in the workers' compensation system because the cost would be capped at the Medical Fee Schedule rate prescribed by congress for Medicare recipients.

The Department acknowledges that there are slight increases in health care costs when the U.S. Congress annually adjusts the Medical Fee Schedule and when the Director occasionally increases individual medical codes. However, these increases do not account for the medical cost experience versus lost days and rate of injury as experienced by Hawaii's employers, the City and the state.

DURATION

As Graph 21 and 22 illustrate, TTD payments increased substantially over the last eight years since the implementation of the 100% cap on the medical fee schedule. This means that injured workers remained out of work longer receiving medical attention. Duration of claims become an issue because claims that last longer than seven days increases costs substantially. The Department believes that three main factors have contributed to the extended length of time an employee is in the workers' compensation system:

- **Departmental Interference.** The Department must do a better job of expediting hearings and decision-making, as well as the processing of claims that come into the Disability Compensation System. The Department initiatives can be found on page 26.
- **Health care providers.** Data suggests that health care providers are extending the amount of time to medically treat and return an injured employee back to full employment. This results in increased TTD benefits for the employee and increased medical reimbursements for the provider.
- **Vocational Rehabilitation.** Allowing the employee to select his own vocational counselor without any employer involvement has created a system that extends the duration of a claim and places the employer and employee in an adversarial situation. This adversarial situation further delays recovery as the Department or the Labor Appeals Board must then adjudicate that controversy.

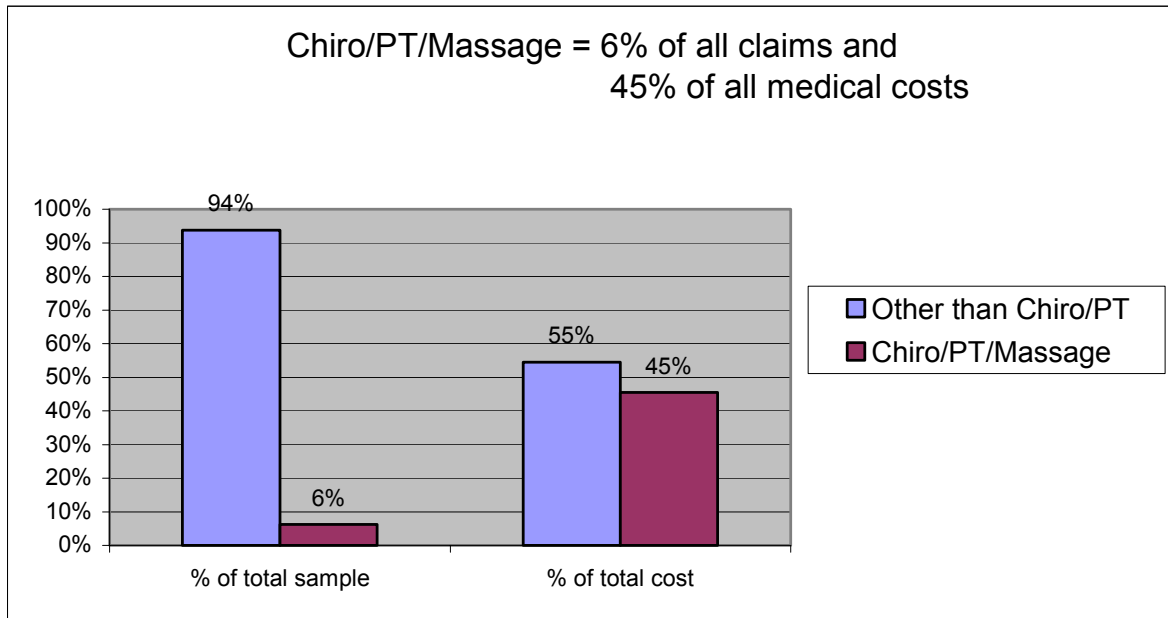
CARE PROVIDED BY CHIROPRACTERS, MASSAGE THERAPISTS, PHYSICAL THERAPISTS, ETC.

In 2003, the First Insurance Company of Hawaii ("First Insurance") presented to the workers' compensation community a survey that they had conducted on closed workers' compensation cases. The survey compared costs from medical doctors, massage therapists, chiropractors, and physical therapists. The sampling was a "snapshot" of 17,581 claims from calendar years 1995 to 2003.¹

¹ First Insurance does caution that this sampling does not take into account all massage therapists, chiropractors, and physical therapists. First Insurance also stipulates that the comparison of services are not an exact side-by-side comparison because medical doctors treat minor injuries that cost less as opposed to the majority of the services that massage therapist, chiropractors, and physical therapists perform.

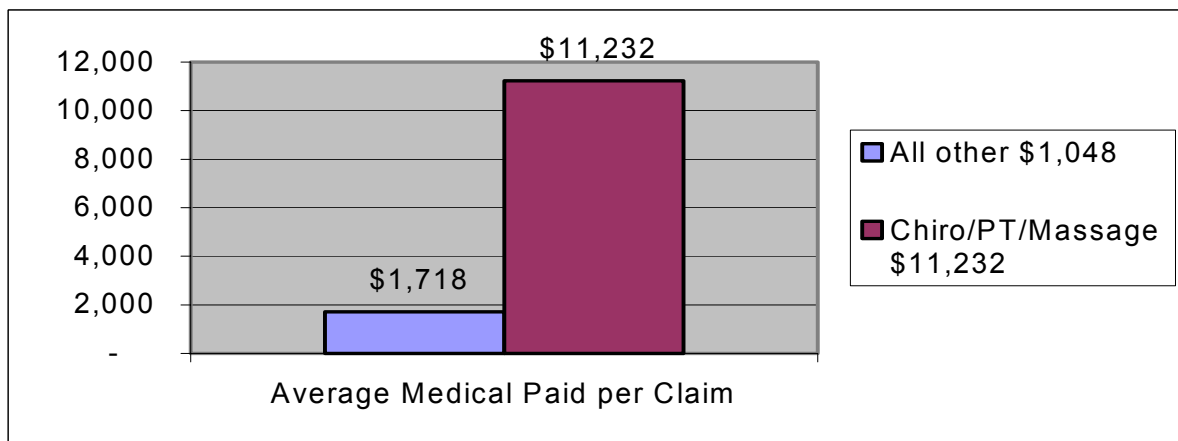
The Department is presenting these figures acknowledging the discrepancies identified by First Insurance. While it is not a perfect side-by-side comparison, it adequately reflects the disproportionate costs associated with providers of palliative care from the viewpoint of the insurance industry.

Graph 23 illustrates that of the 17,581 cases surveyed, 6% (1,088) of the claims were handled by massage therapists, chiropractors, and physical therapists. Medical doctors accounted for 94% (16,493) of the claims. In this sampling, the total costs paid out to medical doctors constituted 55% (\$45,619,701) of the costs, while the massage therapists, chiropractors, and physical therapists accounted for 45% (\$38,072,145) of the costs.

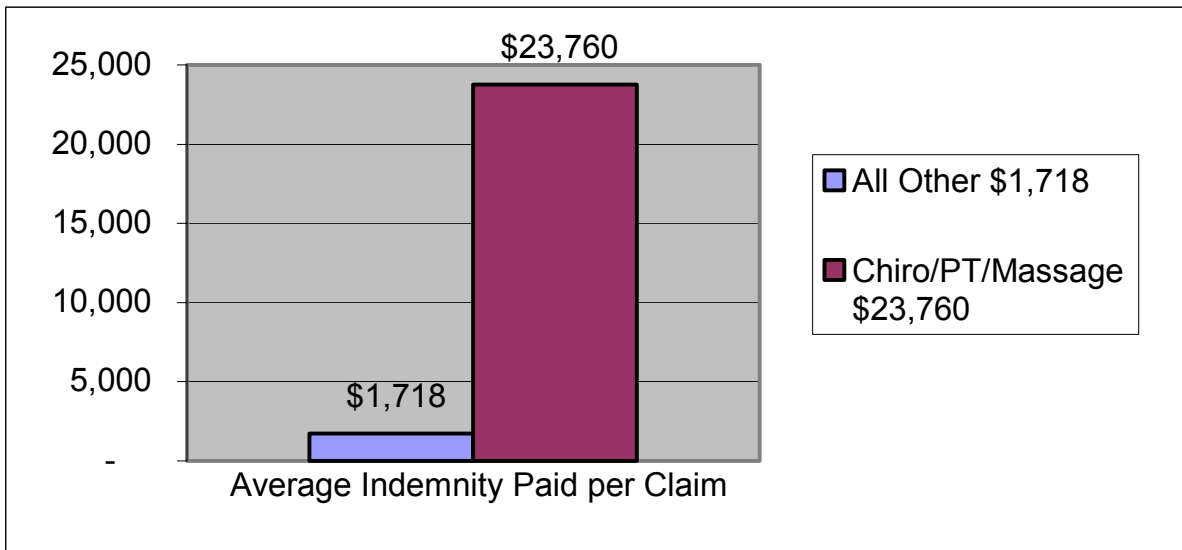


Graph 23. First Insurance Company of Hawaii

Graph 24 illustrates the discrepancies between the differing health care providers in medical costs per claim of the 17,581 cases. Graph 25, illustrates the average indemnity benefits paid per claim by medical doctor versus massage therapists, chiropractors, and physical therapists.



Graph 24. First Insurance Company of Hawaii



Graph 25. First Insurance Company of Hawaii

While the Department recognizes the above is a non-scientific survey, it does correlate with national studies comparing trends between the costs for services performed by medical doctors versus other health care providers providing physical medicine. A study from the Workers' Compensation Research Institute found that physical medicine care costs 30% more in some states when not being treated by a medical doctor.² The study does point out that Florida has been able to provide chiropractic treatments that cost less than medical doctors. Florida was able to accomplish this by enacting reimbursement rules that place limits on the number of chiropractic visits that will be reimbursed.

INADEQUATE CONTROL OF VOCATIONAL REHABILITATION PLANS

As Graph 12 and 13 show, the amount of cases being referred to vocational rehabilitation has dropped 64% since 1995 yet costs have increased by 31% over that same time period. The purpose of Vocational Rehabilitation ("VR") is to provide injured workers the training, guidance, and skills development necessary to enable the worker to return to suitable work "as quickly as possible in a cost-effective manner" (See HRS §386-25) required to get that employee back to work sooner. This benefit is supposed to assist employers by reducing their potential liability by ensuring that the claimant does not get categorized as permanently totally disabled. The increase in costs, lost days and TTD suggest injured employees are either staying longer in VR or the plans themselves are getting more expensive.

In either case, VR is meant to reduce the cost of workers' compensation. The studies show that Hawaii can do better in controlling vocational rehabilitation costs.

² *Patterns and Cost of Physical Medicine: Comparison of Chiropractic and Physical-Directed Care*. Richard A. Victor and Dongchun Wang. December 2002.

12. Hawaii ranks 3rd in Premium Rate Ranking.

In the late 1980's and early 1990's the State of Oregon decided to implement much-needed reform to their workers' compensation system and began to implement reform. In order to track their success, the Research and Analysis division of the Oregon Department of Consumer and Business Services began collecting data both locally and nationally. One of the reports that they produced and continue to publish is the Premium Rate Ranking. This report provides a gauge of how much payroll dollars Oregon employers pay for every \$100 of payroll in comparison to the nation. In 2002, Hawaii moved up five spots, by ranking third in the entire nation.

| 2002 Ranking | 2000 Ranking | State | Index Rate | Effective Date |
|---------------------|---------------------|----------------------|-------------------|------------------------------------|
| 1 | 3 | California | 5.23 | January 1, 2002 |
| 2 | 1 | Florida | 4.50 | January 1, 2001 |
| 3 | 8 | Hawaii | 3.48 | July 1, 2001 |
| 4 | 16 | Delaware | 3.38 | December 1, 2001 |
| 5 | 4 | Rhode Island | 3.29 | November 1, 1998 |
| 6 | 7 | Texas | 3.29 | January 1, 2002 |
| 7 | 2 | Louisiana | 3.19 | May 1, 2001 |
| 8 | 6 | New York | 3.13 | October 1, 2001 |
| 9 | 12 | Montana | 3.04 | July 1, 2001 |
| 10 | 5 | Nevada | 3.02 | July 1, 2001 |
| 11 | 18 | Alabama | 2.96 | March 1, 2001 |
| 12 | 17 | Connecticut | 2.90 | January 1, 2002 |
| 13 | 9 | Ohio | 2.89 | July 1, 2001 |
| 14 | 28 | Alaska | 2.87 | January 1, 2002 |
| 15 | 24 | Kentucky | 2.87 | September 1, 2001 |
| 16 | 10 | District of Columbia | 2.86 | June 1, 2001 |
| 17 | 20 | New Hampshire | 2.85 | January 1, 2002 |
| 18 | 11 | Oklahoma | 2.82 | 8/1/99 State Fund, 12/1/01 private |
| 19 | 15 | Illinois | 2.73 | January 1, 2002 |
| 20 | 14 | Colorado | 2.73 | January 1, 2002 |
| 21 | 22 | Minnesota | 2.60 | January 1, 2002 |
| 22 | 25 | Pennsylvania | 2.57 | April 1, 2001 |
| 23 | 13 | West Virginia | 2.53 | July 1, 2001 |
| 24 | 33 | Vermont | 2.45 | April 1, 2001 |
| 25 | 26 | Missouri | 2.39 | January 1, 2002 |
| 26 | 29 | Idaho | 2.37 | January 1, 2002 |
| 27 | 21 | Georgia | 2.32 | November 1, 2001 |
| 28 | 19 | Maine | 2.30 | January 1, 2002 |
| 29 | 31 | Tennessee | 2.30 | March 1, 2000 |
| 30 | 23 | Michigan | 2.25 | January 1, 2002 |
| 31 | 27 | New Jersey | 2.25 | January 1, 2002 |
| 32 | 32 | Wisconsin | 2.22 | January 1, 2002 |
| 33 | 30 | Mississippi | 2.21 | March 1, 2001 |
| 34 | 43 | North Carolina | 2.17 | April 1, 2001 |
| 35 | 34 | OREGON | 2.06 | January 1, 2002 |
| 36 | 42 | New Mexico | 2.01 | January 1, 2002 |
| 37 | 36 | Massachusetts | 1.98 | July 1, 2001 |
| 38 | 39 | Wyoming | 1.97 | January 1, 2002 |
| 39 | 45 | Nebraska | 1.93 | February 1, 2001 |
| 40 | 46 | Maryland | 1.84 | January 1, 2002 |
| 41 | 48 | Kansas | 1.84 | January 1, 2002 |
| 42 | 49 | South Carolina | 1.82 | May 1, 2001 |
| 43 | 41 | Iowa | 1.74 | January 1, 2002 |
| 44 | 47 | Utah | 1.67 | December 1, 2001 |
| 45 | 38 | Washington | 1.65 | January 1, 2002 |
| 46 | 37 | Arizona | 1.63 | October 1, 2001 |
| 47 | 40 | Arkansas | 1.62 | July 1, 2001 |
| 48 | 44 | South Dakota | 1.61 | July 1, 2001 |
| 49 | 51 | Virginia | 1.50 | April 1, 2001 |
| 50 | 50 | Indiana | 1.37 | January 1, 2002 |
| 51 | 35 | North Dakota | 1.24 | July 1, 2001 |

Graph 26. 2002 Oregon Workers' Compensation Premium Rate Ranking. Oregon Department of Consumer and Business Services

SECTION V: DEPARTMENT INITIATIVES

The Department recognizes that legislative changes alone will not alleviate the cost burden placed upon Hawaii's small business employers. Therefore, the Department has undertaken several internal initiatives to reduce the administrative burden placed upon workers' compensation claims.

1. Enforcement of Unwritten Rules by Administrative Hearings Officers

The Department has taken steps to ensure that a "rule" not promulgated by statute or rule is not enforced. These "unwritten rules" are arbitrary and add to the confusion of both the injured employee and employer.

An example of an unwritten rule the Department used to enforce was the \$15,000 wash rule. The Department's workers' compensation hearings officers would apply this rule and frequently denied settlement agreements if employers did not include a minimum payment of \$15,000 to an injured employee. These settlement agreements would be appealed to the state's Labor Appeals Board, where often they would be settled for the original agreed amount or less.

In denying these kinds of settlements, the Department delayed the closure of a claim and increased costs as employers were forced to continue paying wage replacement benefits while the Department paid more for administrative services. This unwritten rule was removed effective August 1, 2003.

2. Automation and On-line Services

The Department has undertaken steps to automate the Workers' Compensation branch of the Disability Compensation Division ("DCD"). The automation of the branch will allow for more accurate, expedient and efficient processing of claims.

The Department, in partnership with the state's insurance carriers and e-Hawaii, is developing a system to allow employers and insurance carriers the ability to transmit workers' compensation claims on-line and electronically, as opposed to mailing a paper copy, to the insurer and the Department.

While the Department is experiencing funding difficulties for this initiative, steps are being taken to explore optional funding streams, as well as exploring partnership agreements with insurance carriers to share staff resources in developing the needed applications.

3. Expedited Hearing Process

The Department is working on expediting the hearings process for workers' compensation claims. The ability to resolve disputes and render decisions on cases in a timely manner reduces the overall costs of the process.

4. Continuity of Administrative Hearings

The business community has long complained that the quick resolution of a case seems dependent upon which hearing officer is reviewing the case. Employers and employees have voiced concerns that decisions are not uniform and that the application of Section 386, Hawaii Revised Statute, differs from hearing officer to hearing officer.

To address this concern, the Department is developing procedures and guidelines aimed at making decisions more consistent.

5. Review and creation of Administrative Rules

A working group has been convened to review current administrative rules and recommend any changes. The group is comprised of outstanding lawyers that represent the state's unions, employers, and insurers. Recommendations from the team are expected by mid 2004. The group has also been asked to suggest rules to formalize and guide the administrative hearings process, settlements for cases, vocational rehabilitation and other procedural guidelines.

6. Hawaii Occupational Safety and Health Division ("HIOSH")

The Department has undertaken efforts to improve the functions of HIOSH's Consultation and Training Branch to ensure that employers are provided with timely comprehensive advice on how to design and implement effective safety and health programs. The Department has been proactive in getting Hawaii's businesses to participate in the Department's Hawaii Safety and Health Achievement and Recognition Program ("HI-SHARP") and Volunteer Protection Program ("VPP"). These programs are designed to help small and large companies ensure that they have an effective safety and health program to help reduce overhead costs, accident costs, and improve quality and productivity. Companies that attain HI-SHARP or VPP status are removed from the Department's programmed inspection list and given a minimum 5% workers' compensation premium discount.

The Department has also implemented the Safe Workplace Assistance Program ("SWAP"). SWAP is designed to augment the consultation section's personnel shortfall. The program will utilize outside occupational safety and health professionals to address the needs of small employers who often lack the financial resources to hire paid private consultants to assist them in meeting their obligations under the OSH Act of 1970.

The SWAP program consists of professional consultants, who volunteer their time and expertise *pro bono*, to provide companies with the consultation services needed to qualify them for the HI-SHARP, Pre-SHARP, and/or VPP. SWAP targets and attracts those professionals seeking to provide community service and ensuring a safe workplace.

7. Outreach & Education

The Department has initiated numerous programs to work with our customers to provide them with a better understanding of program requirements and to develop changes, which will improve the administration of the workers' compensation program, and to help employers maintain a safer workplace.

These initiatives include development of a better website that will enable employers, insurance carriers,

health care providers and injured workers with a better understanding of the workers' compensation program. In addition to providing basic information about workers' compensation, this website answer the most frequently asked question, provides a clear description of the claims process and eventually will enable downloading and electronic filing of reports.

The Department has begun conducting monthly employer workshops, providing information about programs, and more importantly, introducing the Department to our customers should they require assistance in the future. In addition, the Department actively participates in various workshops and provides training sessions to employers, insurance carriers, labor and health care organizations. These workshops provide valuable information to facilitate understanding of workers' compensation requirements and procedures and also provide an opportunity for our customers to identify concerns and discuss issues.

SECTION VI: PROPOSED LEGISLATION OF HOUSE BILL 2486 and SENATE BILL 2961

The following is a section-by-section explanation and justification of the Department's Workers' Compensation Omnibus bills. (H.B. 2486 and S.B. 2961)

1. SECTION 2:

Define Attending Physician and Palliative Care. (§386-1, HRS.)

The Department believes that an important aspect to controlling costs is to establish a "gatekeeper" process to ensure that palliative care services and the duration of medical treatment are not abused. The Department proposes to limit the attending physician, or primary health care provider, to medical doctors and dentists only.

The current system allows for fifteen treatments per injury for the first sixty days, and twenty treatments for therapists. Currently, the Attending Physician, who can be either a doctor of medicine, a dentist, a chiropractor, an osteopath, a naturopath, a psychologist, an optometrist, and a podiatrist, can authorize additional treatment for 120 days. Employers do have the right to deny this treatment.

The Attending Physician being proposed, allows for referrals to other health care providers (chiropractors, massage therapists, naturopaths, etc.) to provide treatment that the medical doctor deems necessary and is unable to perform himself or herself. The referrals are limited to a period of 60 days or fifteen visits, whichever occurs first, and cannot be made to any person or company that the attending physician has a financial interest in. This limitation is proposed to eliminate abuse of services.

The medical fee schedule already mandates that there be only one Attending Physician. This amendment seeks to codify that rule in statute.

Improvements to the Current System

The data presented by First Hawaiian Insurance of Hawaii suggests that alternative medicine is not a cost-effective means of treating the injured workers. The goal of workers' compensation is to restore an injured employee as far as possible to pre-accident status in a manner that is cost-effective for the whole system. If a medical doctor can provide the same treatment as a practitioner of alternative medicine at a lower cost to the system and the employer, then that is what should be mandated. As specified earlier, studies have shown that physician-directed care is less costly than chiropractic-directed care in most states.

Further, many employers complain that alternative medicine practitioners (chiropractor's, massage therapists, naturopaths, etc.) do not cure injuries and are inappropriate for workers' compensation. Limiting the Attending Physician to medical doctors, eliminates the argument and criticism surrounding alternative medicine being utilized for workers' compensation injuries, which is being paid by employers. This also ensures that the profession of the person responsible for coordinating the treatment plan for the injured employees is without controversy.

In defining and limiting palliative care, the State ensures that an employer is not paying for treatments that are not going to permanently cure the injury.

Questions/Answers

Q. Is it fair to limit the attending physician to medical doctors and dentists and exclude alternate health care providers such as chiropractors and massage therapists?

A. Workers' compensation is a **social insurance** intended to ensure that an injured employee receives the medical attention they deserve and expect. While providers should expect to be adequately compensated, workers' compensation was never intended to be a profit making enterprise.

Other health care providers are not excluded from providing services. The Department is simply insuring that the employee receives the necessary medical services in order to heal and return to work in the most cost effective manner.

The state legislature sought to control medical cost through a medical fee schedule. The idea was to cap the amount paid to providers. However, as we have shown in this report, the opposite effect has happened, as medical costs have increased.

The Department recognizes that alternative health care providers do offer quality services. However, the law must balance the needs of the injured employee and the financial health of the employer.

Q. Will medical doctors in organizations such as Kaiser Permanente and Straub be allowed to refer clients within their organizations?

A. This language is not meant to exclude health maintenance organizations such as Kaiser Permanente from referring clients within their system. It is meant to deter abuse of the system by not allowing the attending physician to refer the employee to an organization that financially benefits them.

Q. What happens if the injured employee needs services beyond the 15 referrals or after the 60 days?

A. The attending physician would petition the Department for additional services. The Director would deny or grant the request based upon the advice of the attending physician.

Q. Will palliative care be limited for those patients that have a deteriorating condition that require medication or services beyond the initial 15 referrals or after the 60 days?

A. The attending physician would petition the Department in cases of extreme mental or physical injury or illness that require additional palliative care.

2. SECTION 2:

Amend the Definition of Employment. (§386-1, HRS.)

The Department currently requires individual members with employees of a limited liability company and partners in a partnership to obtain workers' compensation coverage.

This amendment will give small business owners who meet certain exclusions the option to not obtain workers' compensation insurance regardless of the form of its business structure. This measure adds four new exclusions under the definition of "employment" relating to services performed by an individual who owns a major interest in the business: (i) a member of a limited liability company, (ii) a partner of a limited liability partnership and a sole proprietor.

Improvements to the Current System

This will allow owners and partners of corporations the ability to save costs by allowing them to not opt out in obtaining workers' compensation coverage for themselves as individuals.

Sole proprietors have been excluded from obtaining coverage; however, this will provide clarification to individuals who meet this exclusion. In addition, the reference to excluded services as defined in section 386-1, HRS, under both the workers compensation and temporary disability insurance laws, will provide consistency in exclusions with statutes of other department programs.

Questions/Answers

Q. Are there cost savings associated with this amendment?

A. Some limited liability companies and partnerships may experience immediate savings on their overall cost if they meet the exclusions and choose not to obtain workers' compensation coverage for themselves. It will also assist new and existing businesses by helping them determine if they will require specific types of coverage. Some employers who currently have coverage may be relieved from providing workers compensation and temporary disability insurance due to the broadening list of excluded services.

Q. Will current employees be required to form LLC's, LLP's, or partnerships as a condition of employment?

A. No. An employer cannot require this as a condition of employment.

3. SECTION 2 and SECTION 8:

Define Maximum Medical Improvement ("MMI") and Amend Temporary Total Disability. (§386-1 and §386-31, HRS.)

This measure defines MMI as the point when no further improvement in the employee's condition is expected from curative health care or the passage of time. This amendment would eliminate most palliative care and TTD payments after MMI has been achieved.

TTD is meant for injured employees whose total disability injury is not permanent and who are

expected to return to the workforce. This amendment, in concert with the definition of MMI, would limit TTD payments to 104 weeks.

In cases where the employee has not exhausted the 104 weeks, but there is disagreement on whether MMI has been reached, the employee would petition the Department for continuation of TTD payments for the remainder of the 104-week cap (2 years). If the injury continues to deteriorate, the employee can petition the Director for an extension of TTD payments beyond the 104 weeks.

Improvements to the Current System

The amendment would encourage employees that are capable, to return to work earlier. It would also establish a cap and platform to evaluate an employee for PTD or PPD payments. This process will likely motivate all parties involved to resolve the claim in the most expedient manner.

Questions/Answers

Q. Would capping TTD payments be unconstitutional or erode the employer's responsibility to provide benefits to an injured employee?

A. The Department does not believe so. Several states throughout the nation already cap TTD payments to control costs. For example, Massachusetts limits TTD payments to 156 weeks, while Minnesota caps TTD payments at 104 weeks.

By capping TTD at two years, the Department is encouraging employees who can return to work, to do so. With regard to the employer's responsibility to provide benefits to the injured employee, the cap will encourage a determination of the extent of the injury and whether the claimant is permanently disabled or entitled to an indemnity payment under permanent partial disability.

Q. Is two years a reasonable amount of time in which to cap TTD payments?

A. The Department feels that it is. While there are safeguards to allow for continuation of payments for injuries that deteriorate, there must be a point from which the employer and employee must decide if the total disability injury will ever heal and allow the employee to return to work. If not, then the employee should be evaluated for PTD/PPD, or, allow the insurer to adequately compensate the employee through an agreed upon settlement.

4. SECTION 3:

Redefine Mental Stress. (§386-3, HRS.)

This bill proposes to amend section 386-3, Hawaii Revised Statutes, by disallowing workers' compensation claims for mental illness or injury proximately caused by all personnel actions taken in good faith by the employer. Personnel actions include disciplinary action, counseling, work evaluation or criticism, job transfer, lay-off, promotion, demotion, suspension, termination, retirement, or other actions ordinarily associated with personnel administration.

This measure ensures that employers can exercise their lawful management right to take personnel action such as issuing a poor performance evaluation or not selecting an applicant for

a promotion without fear of workers' compensation liability.

In Mitchell v. State of Hawaii, DOE, 85 Haw. 250 (1997), the Court held that a teacher's stress-related injury resulting from disciplinary action taken by the employer in response to her alleged misconduct was compensable under workers' compensation law.

Consequently, in 1998, the legislature amended the H.R.S. 386-3 to exclude injuries arising from "good faith" disciplinary action from being compensable. However, under this 1998 amendment, injuries arising from all other good faith personnel actions are still compensable.

In December of 2002, the Hawaii Supreme Court rendered an opinion in the case of a firefighter against the City and County of Honolulu Fire Department, Davenport v. City and County of Honolulu, Honolulu Fire Department, Hawaii No. 23141, (2002). Mr. Davenport had filed for workers' compensation due to a mental stress injury he received while trying to attain a promotion. In Davenport, the Supreme Court opined that, under the "unitary" test, and without explicit exclusion from state law, a stress-related injury that stems from an essential function of the employer and results from an activity that serves an important interest of the employer is compensable.

In Davenport, the promotion process was an essential function of the employer and served an important interest of the employer. Thus, an injury that stems from such a process is compensable. Consequently, the Supreme Court held in Mr. Davenport's favor.

Improvements to the Current System

This measure will ensure that employers, who exercise their lawful right to take good faith personnel actions that are not disciplinary in nature, can do so without fear of economic reprisal in the form of inflated workers' compensation insurance costs and stress claims.

Employers will not be punished for making good faith personnel decisions that best serve their business. The current law as written, perpetuates the image of Hawaii as anti-business and should be changed.

Questions/Answers

Q. Would this amendment preclude mental stress altogether?

A. No. This amendment would only preclude stress caused by regular interaction of employers with employees in the normal course of their employment. It would not preclude a mental stress claim caused by the willful action of an employer who harasses an employee in bad faith.

Q. Is it the intent of the amendment to preclude a claim for mental stress if the employee suffers from paranoia, which causes a mental breakdown because the employee found the employers promotion process unfair?

A. Yes. Workers' compensation is insurance that is provided to an injured employee for medical treatment and benefits if impaired or disabled. This system was established to protect employees and the employer from litigation that could bankrupt the employer.

The Hawaii Supreme Court, in both the Mitchell v. Department of Education and Davenport v. City and County of Honolulu, Honolulu Fire Department decisions, stated

that if the Hawaii State Legislature had wanted to preclude personnel actions taken in good faith by employers, they should have explicitly included them in the law. Absent any specificity, all mental stress claims, excluding those caused by disciplinary action, would be compensable so long as they are work related.

It is understood that the employer has an obligation to provide a safe and healthy workplace. However, in cases where a person's mental well-being is subject to how they personally view an employer's personnel action that is taken in good faith, filing a claim for mental stress should not be allowed.

Q. Is this legislation even necessary given that mental stress claims comprise only 1.5% to 1.6% of reported cases?

A. Yes. While mental stress on average is 1.6% of all claims reported (466 claims for calendar year 2002), the Department processes over a thousand a year (1,265 for 2002). In 2002, 504 claims had costs that required Hawaii's employers to pay \$6.3 million and absorb 37,484 of lost days of work.

Some have argued that because the amount of cases reported and money paid out each year is relatively small when compared against the total workers' compensation costs, that this is a non-issue.

This reasoning suggests that (1) we should wait until mental stress claims become a bigger problem and (2) that as long as my neighbor keeps taking my individual tools as opposed to my tool box, that there is no fundamental problem.

While \$6.3 million may seem minimal compared to the total amount of \$268 million in workers' compensation benefits paid out in 2002, we should be diligent and proactive to contain this situation. We should also be mindful that \$6.3 million is a tremendous amount of money to the employers who pay it.

5. SECTION 4:

Allow Employer Mandated Choice of Physician, Expanded Fees for Emergency Room Care, and Allow Greater Flexibility in the Medical Fee Schedule. (§386-21, HRS.)

Employer Designated Choice of Physician

The Department proposes to amend this section to allow Hawaii's employers the opportunity to provide their employees with an employer-designated healthcare provider list of at least three attending physicians and/or physician networks, of which 50% must practice on the island where the injured employee resides. If the employer wishes to develop and implement an employer-designated healthcare provider list, then the employee would be mandated to see that physician for the first 120 days from the day of injury. The injured employee would then be allowed to "opt out" of the plan after the 120 days are complete and see a physician that is not on the list. This would allow employers greater success in entering into contracts with physician networks and/or managed care organizations for workers' compensation in order to control costs.

Expanded Fees for Emergency Room Care

This provision would allow for usual and customary fees to be charged for Emergency Room

Care up to 48 hours from point of injury. The usual and customary fees would be capped to not exceed 200% over the Medicare Medical Fee Schedule. This provision would ensure that employees injured on the job receive prompt, quality care.

Allow Greater Flexibility in the Medical Fee Schedule

Currently, if a provider wants to adjust the medical fee schedule, they must petition the Department with the specific codes they want to be reimbursed at a higher level. The Director is mandated to perform a statistically valid survey of the prevalent charges for fees for services. This process can be extensive and very time consuming, taking up to a year to complete. By the time the Director is ready to go to public hearing, the data is outdated.

This amendment would allow third parties to submit to the Director an actuary, if the Director deems valid, which can be used in updating the fee schedule. This would expedite the process of making adjustments to the Medical Fee Schedule and ensure that providers are reimbursed adequately.

Improvements to the Current System

Employer-designated provider lists will allow an employer to control duration. As this report notes, claims have gone down yet TTD, medical, and Lost Days have increased. This suggests that injured employees are being treated longer. This will allow employers greater input as to who can provide treatment.

This will also help employers to control costs by allowing them to designate physician networks or directed care organizations to provide care. The Workers' Compensation Research Institute has shown that "...workers' compensation medical networks are generally associated with much lower medical costs: 16 to 46 percent lower if the injured worker is treated exclusively by network providers and up to 11 percent lower if the worker is treated predominately, but not exclusively by network providers."³

Further, allowing employers to provide a list of physicians for the employees to choose from would decrease delays in the workers' compensation system when conflict arise. Currently, if either an employee or employer disagrees with the recommendation of the healthcare provider, the employer may send the employee to an Independent Medical Examiner ("IME"), at the cost of the employer, to be evaluated. A hearing is then scheduled to review the records of both providers. This process creates delays in resolving the case. The employer-designated choice of physician would reduce the need to hire an IME since the employer would have 120 days of medical history compiled by a physician the employer had already selected. It would save employers additional costs and expedite treatment and compensation of the injured employee.

³ *The Impact of Initial Treatment by Network Providers on Workers' Compensation Medical Costs and Disability Payments.* Sharon E. Fox, Richard A. Victor, Xiaoping Zhao. August 2001.

Questions/Answers

Q. How is the selection process done and how do we ensure that the employee is protected?
The selection process would be left to the employer and its insurer. The Department believes that there are enough safeguards in the law to present a provider from not adequately treating the injured employee.

Further, the Department would be willing to amend this section of the bill to require the employer to allow the employee to select his or her family doctor as the attending physician under certain circumstances.

The overriding impetus for this measure is to manage and contain costs. The current system is failing and employers must have more control in order to reign in costs.

Q. Employers are already allowed to enter into managed care agreements and choice of physician. What is the reason for this amendment?

A. This is true, however, the employee is not obligated to receive treatment from the directed or managed care program, or see the employer's choice of physician. This lack of obligation has been raised as one of the reasons managed or directed care has not achieved great success in Hawaii.

Q. What if the employer does not provide the employee with an employer-designated healthcare provider list of at least three attending physicians and/or physician networks?

A. Then the employee is still free to choose his or her own attending physician. The law would mandate that an employer must provide the list with at least three attending physicians and/or physician networks to the employee before an injury occurs.

6. SECTION 5:

Housekeeping to Conform the Section with §386-1. (§386-22, HRS.)

This amendment would require the Attending Physician to designate artificial members and other aids.

7. SECTION 6:

Amend Vocational Rehabilitation. (§386-25, HRS.)

Vocational Rehabilitation costs have experienced rapid growth (31%) since 1995. Fundamental structural changes to the program are sorely needed to allow greater input by the employer in plan implementation and effectiveness. Section 6 of this bill clearly defines acceptable Vocational Rehabilitation plans to control costs.

Under the current law, the employee selects his or her own vocational rehabilitation plan and vocational counselor, without any input or oversight by the employer. In other words, the employer has “no voice” in developing the employee’s vocational rehabilitation plan. The amendment removes the employee's sole right to self refer and mandates the allowance of greater participation between the attending physician, vocational rehabilitation plan designer, employer and employee in plan design and plan review of a vocational rehabilitation program. The amendment also mandates that the employer, employee and plan designer conduct a review for

effectiveness of the plan after 26 weeks for extension approval. If a disagreement exists on the design of the plan or its review, then any party can petition the Director to settle the disagreement. The amendment would also limit vocational rehabilitation to a maximum of 104 weeks and disallow vocational or academic instruction permitting the employee to become self-employed.

The amendment also allows for an employer to redesign the injured employee's job through changes to the work process or function, providing alternative work within the employee's ability, or locating reemployment for the employee to satisfy an employer's obligation under vocational rehabilitation.

Improvements to the Current System

Employers and employees would see faster return to work and greater cost control.

Mandatory reviews and a cap on the length of VR programs, will reduce costs, and prevent outrageous costs associated with vocational rehabilitation programs that exceeds the scope of the workers' compensation program. The system envisioned in this bill requires the employer and employee to work together. This greater interaction will ensure that the employer is paying for services that are effective in rehabilitating the injured worker.

Questions/Answers

Q. Will the 104-week maximum duration for vocational rehabilitation start after the plan design and stop during the plan reviews? What happens if the employer or employee delays the plan design or review?

A. The 104 weeks encompasses the entire process from start to finish. It does not wait for plan creation or stop for the 26 week review. This amendment requires the employer and employee to work together to develop and agree upon a reasonable plan. If at any time any party feels the other is impeding progress or a disagreement exists on the effectiveness of the plan, then that party may petition the Director to make a decision for the group.

Q. How does the redesign and modification of an employee's old job or finding a new job satisfy the requirements of vocational rehabilitation?

A. The purpose of vocational rehabilitation and workers' compensation is to restore the injured employee's earning capacity, as nearly as possible, to the level which the employee possessed before the accident. If an employer is able to redesign the employee's workplace or find them alternative employment that allows the employee to work in their present condition and compensates them at the level in which they enjoyed prior to injury, that should satisfy the intent of vocational rehabilitation.

Q. Is it fair to disallow vocational or academic instruction permitting the employee to become self-employed or attend college?

A. This is a matter of equity. While an injured employee is entitled to vocational rehabilitation to restore his or her earning capacity, the employer should not be forced to fully fund an injured employee's education to start their own business.

Workers' compensation was established to protect the injured worker but also the employer and fellow employees. The state must balance the needs of all parties involved

and come to an equitable agreement that is fair to all parties.

Q. Do other state's cap the duration of vocational rehabilitation?

A. Yes. In states that do offer vocational rehabilitation, there are several that cap the amount of costs and duration of the plan. State's such as Maryland cap their duration at 104 weeks, Minnesota at 156 weeks; and Louisiana at 56 weeks.

The Department feels that a cap of 104 weeks (2 years) is a reasonable and fair period of time. The Department is not requesting that the cost be capped.

8. SECTION 7:

Amends Frequency Guidelines. Housekeeping. (§386-26, HRS.)

This housekeeping amendment is to ensure that the ability to set utilization guidelines by the Director does not interfere with the new amendments proposed in §386-1, HRS. The amendment also clarifies and reiterates employer's ability to enter into "Choice of Physician".

9. SECTION 9:

Amend Temporary Partial Disability. (§386-32, HRS.)

This amendment seeks to remove the minimum requirement for injured employees receiving temporary partial disability (TPD) benefits. Currently, temporary partial disability benefits are awarded to injured employees who are released to light duty work or work with restrictions. Their earnings on light duty are less than their regular wages. Therefore, 66-2/3% of the difference between the employee's average weekly wages before the injury and the employee's weekly earnings on light duty are paid for by TPD.

Currently, TPD is subject to the maximum and minimum weekly benefit amounts for the year of injury, similar to the requirements for temporary total disability benefits where the employee is totally disabled for work.

Improvements to the Current System

Currently, some employees may receive more than their actual wages earned while collecting TPD due to the minimum weekly benefit requirement. This may deter an employee from returning to work at their usual and customary job because they can earn more while disabled and on light duty. This will encourage employees who can return to work, to do so.

Questions/Answers

Q. What is the income level of the persons that will be affected by this amendment?

A. This amendment will affect anyone earning less than \$20.00 an hour.

10. SECTION 10:

Provides an Amendment for Alternative Dispute Resolution. (§386-32, HRS.)

This amendment establishes a strong public policy encouraging arbitration and mediation in resolving differences. It is patterned after Hawaii's arbitration laws, chapter 658. This amendment also provides the fundamental requirements of a valid and enforceable arbitration/mediation agreement. It sets forth rules governing arbitration/mediation in the workers' compensation system.

Arbitration and mediation should be encouraged so that cases pending hearing before the Department can be resolved through an alternative means. This will reduce the Department's caseload, and the duration of time that the case is in the workers' compensation system.

It is not intended to add another layer to the Department's hearing process. A decision by the arbitrator/mediator can only be vacated by the Director of the Department of Labor and Industrial Relations ("Director") if an award is procured by fraud, corruption, or other undue means. The Director may also vacate the award if there is evidence that there was partiality, corruption or misconduct by the arbitrator. Further, the parties can enter into binding arbitration.

Finally, this amendment follows the state's policy to encourage parties to resolve disputes through arbitration. The Hawaii Supreme Court has repeatedly acknowledged this strong public policy. For example, in *Loyalty Dev. Co. Ltd. v. Wholesale Motors, Inc.*, 61 Haw. 483 (1980), the Court stated, "As a matter of public policy established by the legislature in HRS Chapter 658 arbitration is to be encouraged of resolving differences, thereby avoiding litigation." Arbitration and mediation have been proven to be cost-effective and efficient in resolving civil actions and employment disputes. We believe it will be equally effective in the workers' compensation system.

Improvements to the Current System

In utilizing alternative dispute resolution, benefits for work injuries would be delivered in a timely and possibly less-adversarial manner. This would minimize adverse conditions associated with workers' compensation to both the injured worker and the employer. This alternative route to settling disputes over benefits or treatment would be resolved with minimal involvement from the Department. These alternatives are often more efficient and cost effective to settle disputes as opposed to the administrative agency process. This process would expedite decisions and save the workers' compensation system from additional costs

Questions/Answers

Q. Does the Director have any oversight over the arbitration and mediation process?

A. Yes. The Director may vacate an award if it is procured by fraud, corruption, or other undue means or if there is evidence that there was partiality, corruption or misconduct by the arbitrator.

Q. Can an employer require an employee to enter into arbitration or mediation?

A. No. An employer cannot force an employee to enter into arbitration and mediation. The proposed amendment also ensures that employers cannot require prospective employees to agree to arbitration and mediation as a requirement for employment.

11. SECTION 11 and SECTION 12:

Amend the Fraud Violations and Penalties and The Insurance Fraud Investigations Unit. (§386-98 and §431:10C-307.8, HRS.)

This measure expands the state’s insurance commissioner’s jurisdiction to investigate and prosecute workers’ compensation fraud. The insurance commissioner has been aggressive and successful in investigating and prosecuting automobile insurance fraud, and we believe it’s a natural for the state’s insurance commissioner to expand his office’s expertise to workers’ compensation fraud.

Act 234 was enacted in 1995 to address the growing problem of fraud in workers' compensation claims. There have been very few fraud cases investigated and prosecuted by the Department. This is mainly due to an unwillingness by employers or employees to file complaints with the Department and resource constraints.

The following graph represents the total fraud complaints investigated by this Department:

| PERIOD | TOTAL COMPLAINTS FILED | COMPLAINTS FILED AGAINST EMPLOYERS, DOCTORS, VOCATIONAL REHAB | COMPLAINTS FILED AGAINST EMPLOYEES/CLAIMANTS |
|--------|------------------------|---|--|
| 1999 | 15 | 4 | 11 |
| 2000 | 32* | 22 | 10 |
| 2001 | 16 | 10 | 6 |
| 2002 | 20 | 14 | 6 |
| TOTAL | 83 | 50 | 33 |

*10 Complaints filed by one claimant.

Thirty-four, or 41% of fraudulent complaints filed during the period 1999-2002, were withdrawn or settled. Eighteen, or 55% of the employer’s fraudulent complaints against claimants were upheld. None of the complaints filed by employees/claimants against employers/insurance carriers/physicians/vocational rehabilitation (VR) were upheld.

Employers have complained that the investigation and prosecution of fraud is too costly. Most insurers say that once they have uncovered fraud, they usually settle the matter with the employee and sever future payments. Currently, any award that is won is paid into the state's Special Compensation Fund. Insurers also explain that it is rare to find a perpetrator of fraud that could reimburse the paid benefits as well as attorney's fees.

The amendment being proposed would allow the party who successfully investigates a fraud situation and win a determination, shall receive fifty per cent of any award granted. The amendment also clarifies that the successful party shall recoup all payments made and receive reimbursement for attorney's fees. These amendments provide greater incentive to employers and employees that pursue fraud.

Improvements to the Current System

Currently, the state does not vigorously combat fraud. This amendment would place the investigation of fraud into the agency best equipped to pursue fraud. Actively pursuing fraud not only saves the system money and resources by catching and prosecuting offenders, but it also deters those who might take advantage of workers' compensation.