



# The Lone Star State Model for Helping Injured Workers

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# The Lone Star State Model for Helping Injured Workers

## Optional Participation in the Workers' Compensation System Has Served Texans Well: This Success Can Be Replicated in Other States

by Bill Peacock & Stanley Greer

*The workers of America adhere to voluntary institutions in preference to compulsory systems which are held to be not only impractical but a menace to their rights, welfare and liberty.*

~American Federation of Labor Founder and President Samuel Gompers,  
from an article published in the *American Federationist*, April 1916

### Executive Summary

Many states have attempted in recent years to fix the glaring flaws of their workers' compensation systems. Texas implemented perhaps the most successful of these reforms; its success relative to the rest of the country can largely be ascribed to the fact that it is the only state with a thriving private sector work-injury benefit option to state-mandated workers' compensation programs.

Several attempts have been made to replicate the success of Texas private sector alternative in other states. Unfortunately, those efforts have drawn the attention of advocates of the status quo who have opposed them. One of those, the U.S. Department of Labor, took the unusual step last year of launching an investigation of the alternatives to state-managed workers' compensation. The pretext for the Labor Department probe was that ineffective alternative plans result in cost shifting to the federal government, as injured workers have to seek medical and other benefits elsewhere.

This paper examines the relative effectiveness of both Texas' workers' compensation system and its private sector work-injury benefit system. It finds that both systems are well in comparison to mandatory systems in other states. It also finds, that in contrast to the claims of the federal government, employees and employers are better off under the Texas private sector work-injury benefit system, with improved claims handling, cost control, and return to work rates of injured employees.

### KEY POINTS

- Texas is the only state that does not require most employers to participate, i.e., subscribe, in the state workers' compensation program.
- Texas' voluntary (nonsubscription) system has benefitted employers and employees through shorter periods of disability after accidents, fewer claim disputes, lower costs, and faster claim payouts.
- Competition from private sector work-injury benefit plans has caused dramatic improvement in Texas' regulated system.
- The U.S. Department of Labor and other special interests are waging a fight against private sector work-injury benefit plans in Texas and in other states that are considering adopting the Texas Model.
- Competition in injury-benefit plans has made a significant contribution to the vibrancy of the Texas economy.

## Introduction

A little more than a century ago, Wisconsin became the first state in the nation to adopt and implement a workers' compensation system. By the middle of the 20th century, all 50 states had laws on the books establishing such a system. Since then, most every state has attempted to implement various improvements to its system to address weaknesses or cost overruns with varying success. Yet, in all states but Texas, employers are still mandated by law to purchase coverage.

In principle, at least, government-managed workers' compensation offers important benefits to employees and employers alike. When employees who are covered by workers' compensation are injured on the job, the system provides them with insurance for their medical costs and some of their lost pay, regardless of whether or not the employer is found to be at fault for the accident. In return, employees who are covered by workers' compensation waive their right to sue their employer for negligence and are not eligible, except in rare cases, to receive any other damages.

About 78 percent of Texas employers representing 82 percent of private sector employees are covered by the state's regulated workers' compensation system.

While this "grand bargain" has served the interests of the affected parties to some extent, it is fraught with a number of inherent problems. These problems are typically connected to the fact that the vast majority of employers of any significant size in all but one state are legally required to carry workers' compensation, and the benefits must conform to a host of statutory and regulatory requirements set by each state. As such, there is little or no opportunity for innovations or modifications to meet the needs of specific employers or employees.

In Texas, there is such an opportunity through "nonsubscription." Texas has one of the most cost-effective workers' compensation systems in the nation. Yet, while the state's regulated system of workers' compensation works well for many stakeholders, Texas allows either party, employers and employees alike, to choose to nonsubscribe. This actually makes both the regulated and the nonsub-

scription systems better. The Texas workers' compensation system has instituted numerous reforms to lower costs and improve return to work results in order to encourage employers to participate. In order to compete, alternative plans that serve nonsubscribers must offer even better results to lower costs while at the same time providing good benefits to treat injured employees and facilitate their return to work.

About 78 percent of Texas employers representing 82 percent of private sector employees are covered by the state's regulated workers' compensation system. What few realize is that while employers have an option to provide coverage, a similar option exists for employees to choose not to accept coverage should their employer offer it. These options help ensure the best possible system for all affected stakeholders as the regulated and unregulated systems compete and improve on each other's model. Both systems have improved claims handling, cost control, and the return to work rates of injured employees. If the competition between the two systems makes both better, why mandate one over the other?

Employers in other states who must participate in a state workers' compensation system have few options to help control medical costs. Many do not have the option to establish or purchase coverage through a network or have difficulty negotiating fees or removing medical professionals whose treatments they judge to be ineffective or even harmful from their network of providers. Consequently, in these cases, workers' compensation often covers costly treatments that are of questionable efficacy. Even in states with government-set fee schedules, fees are sometimes far higher than what would be paid for the same treatment if it were covered by group health insurance, and sometimes so low that skilled providers with established clienteles refuse to participate in the program.

Relatively recent developments in the nature of employment have rendered the workers' compensation system even more problematic. Both the fact that a far higher share of parents with preschool children currently need or wish to hold paying jobs than was the case in the past and substantially improved health and increased life expectancy have increased employee and employer interest in part-time employment. However, workers' compensation typically enforces strict minimum payments for loss of income due to workplace injury that sharply increase the employer's relative cost of hiring part-time vs. full-time workers. The result is substantially fewer part-time work opportunities for employees who want them.

## Reform Efforts

Numerous states have attempted in recent years to fix the glaring flaws of their workers' compensation systems by modifying statutory and rule provisions with some limited success. Texas implemented perhaps the most successful of these reforms, resulting in better outcomes for workers and premium rates among the lowest in the nation. Texas' success relative to the rest of the country can at least in part be ascribed to the fact that from the mid-1990's until recently, Texas was the only state to permit almost all private employers of all types and sizes to not subscribe to government-managed workers' compensation and, if they choose, set up their own work-injury benefit plans. About 20 percent of Texas businesses chose not to participate in the system in 2016.

Not subscribing to workers' compensation assuredly does not enable a company to avoid taking responsibility for its employees' safety. Texas employers who opt out lose the legal protection afforded firms by workers' compensation. If the employee of a "nonsubscribing" business is injured and the injury is found to be even partly due to employer negligence, the employer may be required to pay for actual medical costs and lost wages in their entirety and be liable for additional economic and non-economic damages plus attorney's fees. Many employers nevertheless regard opting out as far preferable to participation in workers' compensation because nonsubscription enables them to reduce costs and provide better outcomes for workers. They have more control over their expenses, can demand more accountability from their medical providers, and can encourage more personal responsibility and engagement by injured workers.

The Boca Raton, Florida-based National Council on Compensation Insurance (NCCI) gathers a wide array of data related to workers' compensation from all subscribing businesses in Texas and around the country that participate in state-managed workers' compensation systems. There has been less data available for nonsubscription, though recent efforts have improved the ability to quantify outcomes and costs—a subsequent Foundation publication will look more closely at these. However, the experience of many nonsubscribing businesses and their employees who have been hurt on the job, as documented by independent scholars such as Alison D. Morantz of Stanford University, offers compelling evidence that Texas is on the right track: findings indicate that under nonsubscription employees receive better wage replacement benefits, injuries and lost work time decrease, and employer costs drop as much as 50 percent. Decades of experience

indicate that Texas offers a viable model for states where workers' compensation is onerously expensive for many businesses and employees are routinely referred for treatments that are ineffective at helping them recover.

To many, however, the benefits of Texas' system of allowing options are not so obvious. In 2016, U.S. Labor Secretary Thomas Perez took the unusual step of launching an investigation of the "opt-out" alternative to state-managed workers' compensation. The pretext for the Labor Department probe was that ineffective alternative plans result in cost shifting to the federal government, as injured workers have to seek medical and other benefits elsewhere. It is possible, though, that opposition from workers' compensation insurance companies and trial lawyers influenced the Labor Department; the agency apparently had not received any complaints from injured workers or businesses regarding their experience under the Texas system.

Whatever the reason, the Labor Department's ability to conduct an investigation stems from federal law that requires all nonsubscriber injury benefit plans to comply with the standards of the federal Employee Retirement Income Security Act (ERISA). It is possible that some nonsubscribing businesses in Texas received subpoenas from the Labor Department ordering them to submit to the federal government voluminous and time-consuming paperwork documenting their ERISA compliance. Proponents of using the private sector alternative to helping injured workers have good reason to suspect that the real goal of Perez and other bureaucrats and their allied elected officials was to make opting out of workers' compensation so expensive and difficult that few businesses would choose to do so. Apparently, regulators, politicians, and special interests are worried that, unless the Texas workers' compensation opt-out is blocked by regulators or the courts, the Texas model will spread across the country.

## Cost of Group Health Insurance Shared by Employers, Employees

To understand why state-managed workers' compensation systems routinely fail to furnish workers with effective health care in a timely fashion and at a reasonable cost, it is helpful first to look at how workers' compensation resembles group health insurance plans in certain important ways, but sharply differs from them in others.

In 2015, according to the U.S. Census Bureau, employers helped pay for roughly 177 million Americans' health insurance, and this benefit for employees and their family

members is a major expense for businesses of all sizes. Private group health insurance, which emerged on a major scale during the 1940s, remains, despite the rapid expansion of Medicaid and other taxpayer-financed insurance programs in recent years, the primary means through which Americans under the age of 65 pay for their health care. In recent years, American group health insurance plans appear to have become more successful in keeping costs down. At the beginning of 2016, the Bureau of Labor Statistics reported that from 2007 through the end of 2015, annual medical-bill inflation slowly trended down from 5 percent to slightly under 3 percent—though a recent uptick temporarily brought the rate close to 5 percent during 2016.

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Most group health insurance is provided through networks, primarily health maintenance organizations (HMOs), preferred provider organizations (PPOs) or government-funded plans. These networks typically negotiate discounted fees with medical providers (doctors, hospitals, etc.) and attempt to manage utilization by denying payment for treatment deemed not medically necessary.

This effort to control costs is a part of why group health plans have played a key role in making possible what are, in many significant regards, the best outcomes achieved by any medical system in the world. For example, as physician and Hoover Institution Senior Fellow Scott Atlas pointed out in a January 2013 commentary for Fox News, cancer patients who receive treatment in the U.S. typically fare much better than their counterparts with the same malady in other countries:

American cancer patients, both men and women, have superior survival rates for all major cancers. For some specifics, . . . the breast cancer mortality rate is 52 percent higher in Germany than in the US, and

88 percent higher in the United Kingdom; prostate cancer mortality rates are strikingly worse in the UK, Norway, and elsewhere than in the US; mortality rate for colorectal cancer among British men and women is about 40 percent higher than in the US. Removing “lead-time bias,” where simply detecting cancer earlier might falsely demonstrate longer survival, death rates from prostate and breast cancer from the early 1980’s to 2005 declined much faster in the US than in the 15 other OECD nations studied (Australia, Austria, Canada, Finland, France, Germany, Greece, Italy, Japan, the Netherlands, Norway, Spain, Sweden, Switzerland, and UK). *The inescapable conclusion from objective data is that US patients have superior outcomes from nearly all cancers.*

Employers who offer group health insurance have taken steps that are legally and practically feasible to get costs under control. Figures from the Kaiser Family Foundation/Health Research & Education Trust 2015 Employer Health Benefits Survey, cited by writer Ellen Chang in an article for the MainStreet financial news service in 2015, show that, while employers continue to fork over the bulk of the cost of group health insurance premiums, the cost to employees is substantial:

Since 2005, premiums have grown an average of 5 percent each year, compared to 11 percent annually between 1999 and 2005. The average annual premium for single coverage is \$6,251, of which workers on average pay \$1,071. The average family premium is \$17,545, with workers on average contributing \$4,955.

The Kaiser Family Foundation/Health Research & Education Trust confirmed the trend in its 2016 survey, with costs up only 3 percent from the previous year.

Workers’ compensation functions similarly to group health insurance and other types of insurance in key regards. As insurance products, both group health and workers’ compensation premium rates are based largely on projected risk of losses and expenses. Applying this to workers’ compensation, premium rates also vary based on the type of industry, the classification of workers, safety programs and other risk factors. Companies may also lower their premiums by agreeing to pay higher deductibles or retrospectively adjusting their premium based on loss experience. Companies whose employees file fewer or less severe claims than the industry average may also be able to negotiate for a less expensive premium.

There are differences between the two systems, though. Perhaps the most fundamental difference is that while group health coverage for specific treatments and services is uniformly limited to the contract or policy terms, workers' compensation coverage, with or without a network, is set in statute to include all medical treatments, and with no employee cost-sharing. Since workers' compensation was established to replace a potential tort recovery by the injured employee, medical care cannot be limited by a contract or policy between the employer and the insurance company or plan. That is to say, the coverage for medical care in workers' compensation is set in statute and essentially includes all "reasonable and necessary" treatment as determined by nearly incomprehensible rules and regulations and dictated by agency and judicial decisions. Because nonsubscriber plans are not subject to the statutory coverage, employers are able to limit or expand coverage by policy language, much like group health.

Another difference is that unlike with group health care, only a few states like Texas allow the use of workers' compensation networks. This means there may be less opportunity in many states to negotiate discounted fees with providers. The lack of negotiated fees leads to higher costs for treatments in most cases because, generally speaking, medical costs are sought to be managed by controlling the price paid for services as well as utilization rates.

### **'Increasing Health Care Costs Tend to "Crowd Out" Increases in Wages'**

Profitable businesses that are able to increase employee compensation on a regular basis typically decide first how much aggregate compensation will go up, and then decide how much of the increase will go into higher cash pay and how much will go into more costly benefits. To the extent, then, that the growth in the cost of health benefits can be held in check, firms are able to increase wages and salaries (or employer contributions to retirement plans) more rapidly.

The concept that there is a trade-off between the growth of cash pay and the growth of noncash benefits like employer-provided health insurance is often associated with free market-oriented economists such as Scott Winship of the Manhattan Institute, but economists across the spectrum concur that such a trade-off is unavoidable.

In March 2010, Christina Romer, then the chair of President Obama's Council of Economic Advisors, and Mark Duggan, then the CEA's senior economist for

health care policy, coauthored a brief, but highly informative paper entitled, "Exploring the Link Between Rising Health Insurance Premiums and Stagnant Wages." After reviewing data from the Bureau of Labor Statistics' "Employer Costs for Employee Compensation" survey, Romer and Duggan sought to shed light on the extent to which "increasing health care costs tend to 'crowd out' increases in wages." They pointed out that, from 2000 to 2009, inflation-adjusted total compensation per hour increased by 1.3 percent per year, but, principally because of rising health care costs, workers' "average wage and salary compensation increased" by just 0.7 percent per year over the same period.

Employers who believe increases in cash pay help them attract and retain talented and conscientious employees more effectively than increases in noncash medical benefits can rebalance their compensation package over time by purchasing group insurance policies that give the businesses more control over the provision of medical care.

One source of the lack of cost containment in workers' compensation is that employees who file a claim through workers' compensation, unlike employees who file a claim through group health insurance, typically have no strong incentive or requirement to use an employer-designated medical provider.

A 2010 analysis issued by Coventry Workers' Comp Services explained why, specifically, the Pharmacy Benefit Management (PBM) model many companies have adopted successfully for their group health plans cannot be applied to workers' comp prescription management.

Network utilization is a key problem. Patients covered under a group insurance plan routinely learn that, if they choose to go outside the network of providers included in the plan, they will pay more out-of-pocket for care. Since many state workers' compensation laws do not allow employers and insurers to establish networks or require that employees stay within a health care network, there is no such incentive. Other states like Texas that do authorize the use of networks have significantly improved cost and utilization rates. Texas law requires employees covered by a workers' compensation network to access care within that network of doctors except for emergency situations or when they have obtained prior approval to access care out of network.

According to Coventry, the extraordinary difficulty of eligibility management in many state systems is a key reason

why workers' comp insurers "cannot negotiate the same low rates/discounts" for prescription drugs as a group health plan. It is not good business for pharmacies to offer significant discounts if the employer and its insurer are unable, in return, to steer significant numbers of customers into their stores.

On the other hand, sometimes the workers' compensation system frustrates employers by refusing to allow provider fees high enough to persuade experienced, first-rate medical providers to participate in the program. But when businesses are free to negotiate and establish their own networks, they frequently pay providers more than what the statutory fee-schedule dictates, at the very least when the market dictates that it is necessary to attract and retain quality providers. Mark Adams of the Illinois Policy Institute succinctly explained why in a special report published in summer 2016:

Rather than cut costs by using cheaper doctors, employers are more selective than the workers' compensation system. They will prefer higher-quality doctors who do not overtreat patients, meaning that workers recover faster and return to their jobs sooner [citation omitted]. In this case, the employer and the employee benefit.

**'It Is in the Nature of Government That When Even a Slight Degree of Power Is Delegated, the Natural Tendency Is to Increase that Power and the Authority ...'**

Samuel Gompers, the founder and first president of the American Federation of Labor (AFL), the precursor to today's AFL-CIO, would not have been surprised by the array of ills besetting workers' compensation. For decades, participation in state-managed workers' compensation has been compulsory for the vast majority of employees and employers practically nationwide, and Gompers was, as we shall very soon discuss, a lifelong foe of government-mandated insurance.

According to a working paper by Stanford law professor Alison D. Morantz regarding voluntary vs. compulsory enrollment in workers' compensation, as recently as the 1970s, many state laws were still elective. From 1997, however, the year South Carolina transitioned to a mandatory system, until 2013, Texas was the only state in the U.S. "with a truly voluntary program." Some other states continue to exempt agricultural employers, employers of domestic workers and very small businesses (with one to

up to four employees), but the ranks of the exempt have grown smaller and smaller over the years.

Gompers would not have approved. Early in the last century, when many self-styled "progressives" began mobilizing support for enactment of state laws authorizing compulsory health insurance, Gompers was vociferous in his opposition. U.S. Labor Department economist Laura A. Scofea has suggested Gompers' stance was rooted in his belief that "a government insurance system would weaken unions by denying them the ability to provide social benefits."

However, there seems to be no good reason not to take Gompers at his word with regard to his and his organization's opposition to legislation proposing compulsory insurance by the state "for every person employed at manual labor and all other employed persons earning less than \$100 a month, unless coming under special exemptions." In a January 1916 article for the AFL-published *American Federationist*, Gompers charged that such a compulsory system would be "totally at variance with our national institutions and national spirit. . . ."

"The workers of America," he insisted, "adhere to voluntary institutions in preference to compulsory systems which are held to be not only impractical but a menace to their rights, welfare and their liberty." A proposal then on the table in New York, said Gompers, illustrated the dangers of making sickness insurance mandatory:

[I]t would build up a bureaucracy that would have some degree of control or authority over all the workers of the state. It is in the nature of government that when even a slight degree of power is delegated, the natural tendency is to increase that power and authority so that the purposes of the law in question may be achieved more completely.

The arguments of Gompers and his allies carried the day, and the progressive era ended without the passage of compulsory insurance legislation. Resistance to mandatory health insurance crossing party and ideological lines repeatedly thwarted efforts to impose it at the federal level until well into the Obama administration.

For example, a 1971 proposal by President Nixon to require employers to offer health insurance died due to lack of support from powerful Democratic committee chairmen in the House and Senate. In 1993, then-first lady Hillary Clinton helped doom her proposed health care

plan by including an employer mandate, which, according to a contemporary analysis for the Heritage Foundation by Robert Moffit, required all businesses to “provide at least the standard package” and to pay at least 80 percent “of the cost of the government’s standard health benefits package.”

During the 2008 Democratic presidential primaries, Barack Obama adroitly used his opposition to mandatory insurance against his rivals John Edwards and Hillary Clinton (in one TV ad, he drove the point home this way: “Hillary Clinton’s attacking, but what’s she not telling you about her health plan? It forces everyone to buy insurance, even if you can’t afford it, and you pay a penalty if you don’t.”)

Of course, Obama famously changed his tune regarding the appropriate use of compulsion in health care policy-making, and the Affordable Care Act (ACA) he signed into law in March 2010 included an employer mandate for businesses with 50 or more full-time or full-time equivalent employees. The ACA also included an individual mandate for millions of people who are not otherwise covered by health insurance. The individual mandate barely survived a Supreme Court challenge in 2012, and both it and the employer mandate remain highly controversial.

Opposition to the ACA mandates remains strong, despite weak enforcement. Michael Cannon of the Cato Institute reports that the IRS penalized only about half of the federal tax filers who skirted the individual mandate in 2014. The Obama Administration delayed implementation of the employer mandate several times, and even now that it has gone into effect, the vast majority of businesses are exempt because they have fewer than 50 full-time equivalent employees on their payrolls. To be precise, as Assistant Secretary for Tax Policy Mark Mazur once hammered home to Kelly Kennedy of *USA Today*, “about 96 percent of employers are not subject” to the employer mandate!

In sharp contrast, according to a fact sheet compiled by Texas Department of Insurance researchers, 35 state laws require explicitly, or, in the case of New Jersey, effectively, all nonfarm private employers, including those with just one or two employees, to furnish workers’ compensation coverage. Another 14 states require coverage for all nonfarm private employers with more than two, three, or four employees.

## Unscrupulous Doctors Profit at the Expense of Injured Workers and Their Employers

Moreover, in practically every state with mandatory workers’ compensation, the regulations regarding what kind of coverage employers must offer leave them far less leeway than does the ACA’s employer mandate for group health insurance. Incredibly, in 19 of the 49 states with mandatory workers’ compensation the employer who pays for the policy has *no say whatsoever* over the employee’s initial choice of a treating doctor, even if the employer or the insurance carrier has a managed care arrangement for workers’ compensation.

Government regulations that make it difficult if not impossible for the person who pays for a service to regulate the terms under which the service is furnished are, long experience has shown, a breeding ground for corruption. And over the past decade or so, especially, workers’ compensation programs in many states have been beset with scandals.

Illinois is an egregious case. The Prairie State workers’ compensation law is one of a number that permit doctors, even over the opposition of the owner of the policy and the insurer, not only to prescribe drugs but also to sell them to injured workers. According to research cited in an analysis by Austin Berg of the Illinois Policy Institute, published in May 2016, physicians who are routinely allowed to dispense drugs themselves “prescribe 3.2 times the quantity of opioid drugs they would prescribe otherwise.” Texas is one of only a handful of states with a pharmacy formulary for workers’ comp requiring most opioids and many other narcotics to be pre-authorized prior to dispensing and payment.

Opioids—natural opiates derived from poppy plants—may be prescribed to help a worker who has had a catastrophic injury deal with severe pain, for pain control after surgery, or for pain control. However, the evidence indicates that in Illinois and a number of other states unscrupulous doctors are abusing the system for personal profit at a great human cost. As Berg pointed out, “Illinois physicians can sell ‘repackaged’ pills at exorbitant mark-ups,” averaging between 60 percent and 300 percent.

Ron Vlasty, executive vice president of the Illinois non-profit group Family Guidance Centers Inc., described to Berg what he and his staff had seen:

We have patients who used to work, were injured, were prescribed a painkiller, and eventually became addicted. . . . They lost their job, lost their money, and then they came to us. We're the last stop before jail or death.

Strongly suspecting that greed was prompting some physicians to overprescribe opiates, in 2011 Illinois lawmakers tried to take away the bad incentives in the workers' compensation statute.

### Study was 'Unable to Find Any Medical Justification for the New Dosage'

The state House and Senate adopted and then Gov. Pat Quinn signed into law a package of reforms. Several provisions in the revised workers' compensation code were drafted to make reimbursement rates for physician-dispensed drugs the same as for pharmacies. However, in response, as Berg reported, unethical doctors "altered the dosage of existing drugs and presented them as new, more expensive drugs":

Take hydrocodone-acetaminophen, commonly known as Vicodin. It's one of the most popular painkillers prescribed to injured workers. A January 2015 study from the Workers Compensation Research Institute revealed that, after the new rules took effect, doctors began prescribing a previously rare dosage of the drug at \$3.04 a pill—double to quadruple the price for the same drug in other existing strengths. The study was unable to find any medical justification for the new dosage, and concluded financial motives were likely at play.

Repackaged opioid medications are a highly questionable means of treatment that is often dangerous. They are also very expensive, coming "at a total cost to employers (including medical costs and payment of lost wages) of more than \$22,000 per injury-related event."

Kickbacks are another abusive practice that seems to be endemic to workers' compensation. California's system especially has become notorious for this form of corruption. An expose published in April 2016, written by journalist Christina Jewett for the Emeryville, California-based Center for Investigative Reporting, focused in part on the tragic case of Priscilla Lujan. In early 2012, Lujan, then the mother of an infant son not yet six months old, was struggling with knee pain after an injury on the job.

Her workers' compensation doctor prescribed to her a medicated cream formulated by Kareem Ahmed, a millionaire executive. Ahmed had made his fortune selling such creams, and injured workers were his prime targets.

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According to California prosecutors, the doctor who prescribed a pain cream formulated by Ahmed to Lujan was just one of numerous physicians and chiropractors who did this after having received a bribe. Ahmed, the CEO of Landmark Medical Management, is now set to face charges for allegedly having paid out a total of \$25 million in kickbacks to entice medical providers to treat injured workers with opioid-infused creams for which his firms billed insurers as much as \$1,700 a tube. Insurers were billed a total of \$59,000 for creams prescribed to Priscilla Lujan alone!

Lujan has testified that the cream she was prescribed was packaged without the standard warning for medicines that are dangerous if swallowed. Unbeknownst to her, the cream she was rubbing on her knee was, in Jewett's words, a "loaded gun" that could kill an adult if ingested. Then, one evening early in February 2012, she let her baby son, Andrew Gallegos, use her fingers as a pacifier and gum one of the pistachios she had been eating. When she woke in the morning, his body was cold and his lips were blue. By the time the ambulance carrying them arrived at the hospital, Andrew was dead.

Police investigators would later tell Lujan her baby had been poisoned and question her about how it had happened. It was only then that she realized that it was the residue of pain cream left on her fingers after she treated her knee pain that had killed Andrew. No charges were ever filed against her. Ahmed has now been indicted for involuntary manslaughter, and he and some of the medical providers who prescribed his creams after taking his pay-offs are expected to be tried soon for handing out or accepting kickbacks. Incredibly, even after Lujan lost her baby and investigators turned their sights on Ahmed, his companies kept sending boxes and boxes of the pain

cream to her home. Of the \$59,000 billed to insurers for Lujan's creams, \$33,000 was racked up after Andrew's death!

Texas and a small number of states have recently implemented evidence-based treatment guidelines and a pharmacy formulary, which along with utilization and pre-authorization guidelines, have significantly reduced overtreatment and over prescription in workers' compensation. However, these states are so far the exception. A few other states continue to consider such options, but progress is slow.

### 'Workers' Comp Stands Out as an Easy Target for Scammers'

Why did Kareem Ahmed pick workers' compensation patients like Priscilla Lujan as his means for getting rich off compounded creams whose medical utility is highly questionable? Group health insurance plans, as a rule, have both an incentive and the ability to refuse to pay for exorbitantly expensive medicines that have not been demonstrated to be superior to far less costly alternatives. Most workers' compensation systems do not have similar protections. Some states like Texas do allow insurers to deny medically unnecessary care and prohibit payment for services and prescriptions that require and have not obtained pre-authorization, but again, these are the exception rather than the rule.

As Carol Crisci, Jason Hanford, and Barak Kassutto explained in a brief article published by the Coalition Against Insurance Fraud in June 2016, the compounded pain creams marketed in recent years by pitchmen such as Ahmed are exactly the type of product on which insurers who have control over their formularies look with suspicion:

A single tube can retail for up to \$10,000. Each new prescription—often offered as a “trial”—authorizes 10 refills. One “trial prescription” for one patient thus can generate nearly \$100,000. Compounding pharmacies justify these prices by including expensive and unproven ingredients. . . . More troubling is the lack of safety data. There are no studies of potential drug interactions or the stability of the drugs in cream form. This endangers public health. . . . The few proven ingredients [in compounded pain creams] also are available as vastly more-affordable over-the-counter products [such as Bengay, Aspercreme and Zostrix].

Rather than participants in private group health plans, the pain cream peddlers originally targeted federal government employees. According to Crisci, Hanford, and Kassutto, Tricare, which “covers active and retired military members and their families,” paid \$23 million for compounds in 2010. Costs subsequently skyrocketed to \$513 million in FY 2014 and \$1.7 billion during the first nine months of 2015. However, the federal government did at last begin to scrutinize compounding pharmacies, and most federal insurers have now “removed compounded pain cream from their formularies.”

Incredibly, however, many state workers' compensation systems and certain other carriers, most notably auto-accident insurers, are often still paying claims for compounded pain creams. This is a key reason why “workers' comp stands out as an easy target for scammers,” as Jewett observed.

Just how pervasive is the abuse by medical providers operating in the Golden State's workers' compensation system? Early in June 2016, Jewett cited an investigation concluding, “more than 100,000 injured workers have encountered” close to 100 medical providers “who are facing fraud charges,” mostly in southern California.

Given his own state's dispiriting track record with regard to protecting the interests of injured workers and their employers, one might think that L.A. Congressman Xavier Becerra, until recently the chairman of the U.S. House Democratic Conference and a member of the House Ways and Means Committee, would be reluctant to criticize how other states handle workers' compensation. But one would be wrong.

In October 2015, Becerra (now California's attorney general) joined with four other Democratic members of his own chamber and five U.S. Senate Democrats in signing a letter to U.S. Labor Secretary Tom Perez that decried a supposed “race to the bottom” in state workers' compensation laws. Becerra and his likeminded Capitol Hill colleagues were alarmed most of all by state “opt-out” laws,

which enable employers to set up their own [Employee Retirement Income Security Act]-based workers' compensation programs where employers can establish certain exclusions, heightened thresholds for causality and abbreviated time periods for employees to report an injury.

At the time this letter was posted, just two states, Texas and Oklahoma, had nonsubscription or “opt-out” laws that

roughly fit the congressional politicians' hostile description. The Sooner law had only been adopted a couple of years earlier, whereas in Texas workers' compensation has never been compulsory. Obviously, the congressmen and senators were deeply worried that other states would soon follow in the footsteps of Texas and Oklahoma. Oklahoma's opt-out system was recently ruled unconstitutional by the Oklahoma State Supreme Court, and now Texas again remains the only state where workers' compensation is optional.

In view of the exorbitant cost, corrupt practices, and ineffective and sometimes dangerous treatments for injured workers that plague the workers' compensation systems in Illinois and California, just what is it about the Texas approach that is so disturbing to many powerful people in Washington, D.C.?

### **The Burden of Mandatory Systems are Borne by Employers and Workers Alike**

Fundamentally, what riles proponents of a powerful regulatory state about how Texas addresses the provision of medical care and pay replacement for employees who are injured on the job is that it does not mandate a one-size-fits-all solution for employees, regardless of the size and nature of the business for which they work.

Superficially, the burden of mandatory participation in a state workers' compensation system is borne by the employer, but the reality, as we have already seen, is very different. Employers typically calculate how much money it makes good business sense for them to spend on employee compensation, cash and noncash combined, and adjust for higher workers' compensation costs by reducing cash compensation or other forms of noncash compensation over time.

Moreover, even workers who suffer similar occupational injuries or are diagnosed with similar occupational maladies frequently do not utilize workers' compensation benefits in the same way. For example, since the turn of the millennium the number of workers with severe chronic back pain who have undergone spinal fusion operations across the country has soared, as Steven Mikulan documented in a March 2016 article for *Los Angeles Magazine*.

According to a Healthcare Cost and Utilization Project estimate cited by Mikulan, insurers typically fork over between \$80,000 and \$150,000 for a procedure of this kind, "making spinal fusion not only a complex medical

Superficially, the burden of mandatory participation in a state workers' compensation system is borne by the employer, but the reality, as we have already seen, is very different.

procedure, but one of the nation's most expensive . . ." Employers are often required under workers' compensation laws to pick up the full tab. Yet, as Mikulan goes on to say, "a considerable number of medical experts believe the procedures are no more effective than physical therapy and can result in permanent postoperative pain."

When a mandatory workers' compensation law is in effect, workers with back injuries who make a reasonable assessment that the risks of a spinal fusion operation outweigh the benefits, and opt for physical therapy instead, still may end up helping pay for such operations for other workers who undergo them for their back pain. The cost comes out of every worker's pocket, not just the pockets of those who have the expensive operations. Workers' compensation as it exists across practically all the country today illustrates what Gompers had in mind when he warned that compulsory systems are a "menace" to the individual workers' rights, welfare, and liberty.

### **Only Five Percent of Texas Employees Are Not Covered by Workers' Compensation or Alternative Insurance Plans**

It should be added that, when one looks at businesses' actual practices, as compared to what they are legally able to do, the contrast between the Lone Star State workers' compensation system and those of other states is less stark than one might assume. In his paper published in summer 2016 regarding the severe problems of Illinois workers' compensation and how it might be reformed, Mark Adams pointed out that, while roughly a third of all Texas employers opted out of their state system in 2014, very small businesses are far more likely to opt out than others are:

Forty-three percent of businesses with fewer than five employees opted out compared to just 19 percent of businesses with at least 500 employees. Because most employers who opt out are smaller and by definition employ fewer people, only one-fifth of all workers in Texas are outside the system.

As the Texas Department of Insurance shows, other than Texas, four states exempt businesses with fewer than five employees from mandatory participation, and an additional 10 states exempt businesses with fewer than four, three, or two employees.

Texas businesses that are workers' compensation nonsubscribers are not legally required to furnish either medical or wage replacement benefits for work-related injuries or diseases. But the vast majority of nonsubscribing businesses of any significant size voluntarily offer a package of benefits for employees who are hurt on the job, although the terms and conditions on which they are available and the benefits themselves may differ substantially from what is required for subscribing businesses.

According to a fact sheet prepared by the Texas Department of Insurance regarding employer participation in the state workers' compensation system, in 2014, 20 percent of private-sector employees statewide worked for nonsubscribers. Among that subset of employees, 75 percent worked for employers who offered alternative nonsubscriber benefit plans. Consequently, only about 5 percent of Texas private-sector employees, most of them almost certainly employed by very small businesses that would be exempt in other states, do not have any form of injured worker coverage.

Moreover, based on the experience of other states, it is far from clear that the 95 percent coverage achieved in Texas as of 2016 would actually be higher if employer participation were mandatory. Take, for example, North Carolina, where businesses with three or more employees are statutorily required to either purchase workers' compensation insurance or self-insure. Despite what the law says, according to a 2012 article for the *Raleigh News & Observer* by Mandy Locke and David Raynor, out of at least 172,000 businesses headquartered in North Carolina with three or more employees at the time, fewer than 140,600 either carried workers' compensation policies or were self-insured.

Of course, the 5 percent or so of Texas private-sector employees who lack an injury benefit plan do have a recourse in case they are beset with a job-related injury or illness: They can go to court to be reimbursed for their medical expenses, lost work time, and other damages. As Mark Adams has explained, a Texas employer opting out of workers' compensation can potentially be liable for a very large judgment:

Texas employers that opt out of workers' compensation find themselves in the tort system. . . . [I]f a worker is injured because of the employer's negligence, the employer must pay both actual costs and punitive damages. Furthermore, Texas has removed many of the legal defenses available to employers; a Texas employer cannot avoid liability because the injury results from the actions of another employee or because the employee was partially responsible, and employers cannot claim that employees simply assumed a risk by taking the job. [Footnote omitted.] Thus, a Texas employer opting out of workers' compensation takes a significant risk if the employer fails to ensure a safe workplace.

Experience shows that Texas employers who do take advantage of their legal prerogative not to participate in the state workers' compensation system have indeed on a number of occasions faced multi-million-dollar damage suits. A fall 2012 report prepared for the New Street Group, an insurance industry and risk management consulting firm, and edited by Matthew Brodsky, is generally supportive of Texas' private injured worker benefits system, but cites a lawsuit filed by truck driver Lawrence Rene Montoya as an example of how nonsubscription cases can be dangerous for employers.

### **Nonsubscribing Businesses Have a Greater Incentive to Ensure Employees Are Safe**

In June 2009, Montoya, a recently hired employee of food and beverage distributor Ben E. Keith, got out of his vehicle to repair a stuck air-brake valve. While he was underneath the trailer, "the air brake disengaged, and Montoya was dragged 16 feet." He suffered severe burns, broken ribs, a broken left scapula, and a collapsed lung. After receiving plastic surgery and an array of other treatments, Montoya eventually recovered, and was under no physician restrictions three years later, when his case went to trial, though he said he continued to suffer daily physical pain and trauma.

Montoya's legal counsel contended to the jury that the company was at fault for its policy of allowing drivers to climb under tractor-trailers to make brake valve repairs and for failing to have the repair made before he and his trainer went out on the road. The defense contended that the basic method Montoya had used to attempt to repair the brake valve is in accord with Federal Motor Carrier Safety Regulations, and that the sole proximate cause for

the accident was his negligent failure to set his tractor brakes before trying to fix the valve.

The jury did not accept Ben E. Keith's defense. It found that the company's negligence was the proximate cause of the accident and awarded Montoya a total of \$8.59 million in damages. Rather than proceed with an appeal, Ben E. Keith ultimately settled with Montoya for an undisclosed sum.

If the company had been a Texas workers' compensation subscriber when the accident happened, the damages would have been capped at actual medical costs and the wage replacement and impairment benefits allowed under the regulated workers' compensation system. Montoya would have received far less money as compensation for his injuries, lost work time, and pain and suffering than he actually did. No normal managers want to see their employees injured, but the potential for judgments such as the one just discussed gives nonsubscribing employers in Texas an especially strong incentive to reduce risks down to as low a level as is feasible and to take care of workers when injured.

The nearly ironclad exemption from being liable in tort if found negligent when workplace accidents occur is indeed an important incentive for employers to participate in the workers' compensation system. What is it that persuades roughly 82,000 businesses operating in Texas, including quite a few with deep pockets and a great deal to lose, to take that risk, even as they seek to minimize it by investing time, creativity, and money into keeping their workplaces safe?

Sadly, because of the political hostility toward the workers' compensation opt-out of which the October 2015 letter to Labor Secretary Perez from 10 members of Congress cited above is just one small example, nonsubscribing Texas businesses that have developed their own benefit packages for workplace injuries and illnesses are generally reluctant to go on the record about why they made this decision and how it has worked out for them and their employees.

### **Frequency of 'Severe, Traumatic' Injuries 'Declines Substantially ... With Nonsubscription'**

Nonetheless, a scholarly working paper made available for public review in March 2016 by the John M. Olin Program in Law and Economics at Stanford Law School in

California shows the success achieved by large, multistate companies operating in Texas that have opted out of the workers' compensation system and adopted "customized occupational injury insurance plans" (or "private plans").

In her working paper—entitled "Rejecting the Grand Bargain: What Happens When Large Companies Opt Out of Workers' Compensation?"—Stanford law professor Alison D. Morantz confines her analysis of nonsubscribing employers to "large companies that operate in a homogenous manner across many U.S. states." The primary reason for the restriction on her scope is that "analyzing highly granular data from large *multistate* firms with many homogenous facilities allows me to mitigate many obvious sources of selection bias." Morantz adds:

The only prior econometric study of Texas nonsubscription, by Richard Butler, uses the firm as the unit of analysis. Because the study compares aggregate injury rates across subscribing and nonsubscribing firms, it is inevitably prone to selection bias. . . . [T]he fatality rates reported in the study suggest that in some industries, nonsubscribers are safer than other firms—and indeed, might have opted out of workers' compensation for that very reason. [Footnotes omitted.]

According to Morantz' findings, total injury costs per worker hour for employees doing basically the same jobs for the same employer are cut nearly in half in "the nonsubscription environment." Combined medical, wage-replacement, and legal costs average a total of 14 cents per worker hour in states where workers' compensation is mandatory, but just 8 cents per worker hour in Texas, where the employer takes advantage of its opportunity to offer a private injury-benefit plan.

One significant reason why costs are so much lower for nonsubscribing Texas operations of multistate companies is that "severe, traumatic" injuries decline "substantially (by about 47 percent in [Morantz'] preferred models) with nonsubscription." As Morantz explains, traumatic injuries are less susceptible than non-traumatic injuries "to both under-reporting and over-claiming." Traumatic injuries are also most "compatible with evidence-based medicine, and as such, are less likely to trigger unwarranted claim denials or excessive utilization of benefits." Consequently, the fact that severe, traumatic injury claims are only about one-half as frequent in the nonsubscription environment is almost certainly due primarily to the workplaces in Texas being much safer.

The “nonsubscription” companies studied by Morantz certainly do not save money by skimping on wage-replacement benefits. Private plans typically furnish such benefits starting from the first day of lost work, while workers’ compensation laws commonly require employees who are hurt on the job to wait seven days before receiving any wage replacement. Moreover, most Texas nonsubscribers “offer a wage replacement rate of 85-100 percent and do not cap the maximum value at the state’s average weekly wage,” whereas capping benefits at a lower rate is routine in workers’ compensation.

Apart from their superior safety records, what is it about businesses with private worker-injury plans that enables them to offer this benefit at such a low cost? Morantz cites “end-of-shift or 24-hour injury-reporting windows” and employer control over the pool of medical providers as possibilities, though her data were insufficient for her to estimate how much impact these standard features of private plans have. However, she was able to conclude that coverage exclusions on some treatments (e.g., chiropractor visits) and for some non-traumatic injuries and diseases, as justifiable as they may be, do not save employers much money.

As Morantz acknowledges, her study has several significant limitations. For example, she has only investigated how nonsubscription works for large businesses operating in multiple states, of which Texas is just one. A second important limitation is that she does not attempt to gauge to what extent, if any, private plans cause “costly claims to migrate to group health care plans or taxpayer-funded benefit programs” such as Medicare and Medicaid.

However, recent supplemental analysis furnished by Dallas-based PartnerSource, a 35-employee firm that helps companies determine whether private injury-benefit plans make sense for them and assists nonsubscribing companies and their insurers with the preparation and implementation of their ERISA-compliant plans, addresses key questions about small- and medium-sized firms that opt out of workers’ compensation and allegations of “cost-shifting.”

Over the course of the first half of 2016, PartnerSource worked with independent actuary Leigh Halliwell, who was formerly on the staff of the NCCI, to create a database of more than 160,000 injury claims filed over a 10-year period (2005-15) by employees of nonsubscribing companies. The claims in the database come from 33 different claims administration sources and constitute all

those to which PartnerSource had access. They emanate from employees of small, medium-sized and large businesses.

### **Within Six Months after Being Injured, 97 percent of ‘Option’ Employees Had Returned to Work**

Looked at in conjunction with data available from the Workers Compensation Research Institute (WCRI) and the Texas Department of Insurance, PartnerSource’s Texas “option” industry data confirm that nonsubscription is associated with positive outcomes for employers and injured employees across the board and specifically in the trucking/distribution, retail, manufacturing, restaurant, health care, and hospitality industries.

An analysis issued by PartnerSource reported that Texas nonsubscribing employers and employees benefit from shorter periods of disability after accidents, lower costs, and faster claim payouts than their counterparts inside the Texas state workers’ compensation system, and that Halliwell had confirmed those findings.

For example, after filing claims involving at least eight days of lost time, the “initial return to work rate,” which “measures the percentage of injured employees receiving income benefits who returned to work within six months of a work-related injury,” was 83 percent in Texas workers’ compensation, compared to 97 percent under the Texas Option.

Nonsubscribing businesses and their employees do even better relative to subscribers when it comes to helping injured employees continue working for a sustained period after they return:

[T]he sustained return to work rate measures the percentage of injured employees receiving income benefits [and being off the job for at least eight days] who have been able to sustain their return to work status. The sustained return to work status at [six months] is 75 percent for Texas workers’ compensation, compared to 96 percent under the Texas option.

As PartnerSource President Bill Minick explained in a June 2016 commentary for the trade publication *Risk & Insurance*, this review of more than 160,000 Option program claims strongly suggests that “cost-shifting” to government insurance programs and other private plans is actually more of a problem for state-controlled workers’

compensation plans than for private injury-benefit plans.

One reason why is that many small and medium-sized private plans, as well as nearly all large ones, “pay wage replacement benefits from the first day of disability, at a higher percentage of pay, and with no weekly dollar cap.” The wage-replacement benefits workers receive through state workers’ compensation systems are rarely, if ever, higher, and are in many cases far lower. Consequently, temporarily or permanently disabled workers on private plans are less likely to see the need to apply for Social Security Disability Income (SSDI) or other federal benefits to make up for their lost income.

Minick added that “meaningful progress on cost-shifting by workers’ compensation to SSDI” is hindered to a large degree by state programs’ failure to practice evidence-based medicine. Higher costs due to “late reporting of known accidents and injuries,” failure to receive timely medical treatment, to follow treatment instructions, and haphazard diagnostics by medical providers all contribute to delayed recovery and unnecessarily high costs in workers’ compensation systems, which inevitably tempt some employers, insurers, and employees to try to foist a portion of their expenses on someone else.

No form of insurance (or any other human institution) is perfect, but the best available evidence shows that Texas businesses as a group and nonsubscribers in particular do a far better job than most of their counterparts around the country at preventing serious accidents and, when necessary, addressing the needs of injured employees at a reasonable cost. However, no means of providing medical treatment and replacement pay for workplace injuries should be judged in isolation. One necessary feature of every effort to compensate employees who are hurt on the job is compatibility with an overall economic climate in which workers and businesses of all kinds can find good opportunities and improve their circumstances. As good as Texas’ workers’ compensation system is, allowing an option to unsubscribe makes the Texas model even better.

The Texas regulated workers’ compensation system has seen numerous reforms in the last few years reducing medical costs, improving dispute resolution, improving return-to-work outcomes, establishing evidence-based treatment guidelines, return to work guidelines and the nation’s first pharmacy formulary for workers’ compensation. These reforms reduced premiums by over 50 per-

cent and increased employer participation to new highs. According to studies by WCRI in 2001 and 2011, Texas went from having the highest medical costs of all states studied to one of the least costly after the reforms.

Yet, even with these improvements, Texas has retained the option to unsubscribe. There is no reasonable public purpose for eliminating the option. Any statute, rule, or regulation should have a clear and unambiguous public purpose. Texas workers’ compensation works extremely well despite Obama administration objections to the contrary. Costs are down, disputes are down, participation is up, and injured employees are receiving care and returning to work sooner. Therefore, if there is every incentive for employers to subscribe to the system, there is no rational basis to eliminate the option to unsubscribe. In fact, as good as the system is, it gets better and stays better if private market options challenge and compete against it. Many of the reforms implemented in the regulated system were first introduced in the nonsubscriber market and vice-versa. The two systems often learn from each other and implement initiatives that may have been tried first by the other before realizing success. Conversely, those that fail in one system may quickly be discarded as an option by the other.

More importantly, the nonsubscriber option is able to more quickly adapt and make changes as the plans are not burdened by laws or rulemaking that often delay implementation for months or years. Instead, they can quickly and economically implement procedures and coverages they believe are beneficial and eliminate those that are problematic.

While employers wait for similar reforms to be implemented in other states, employers in Texas have been able to respond on their own initiative and effect changes while still providing good coverage for their employees. In fact, some nonsubscribers chose to reenter the system and purchase policies after the reforms were implemented and proved to reduce costs. Again, the point is they had the choice of whether and when to enter the market.

The Lone Star State model for workers’ compensation is obviously compatible with an economy that furnishes good opportunities for diverse employees.

## **Economic Opportunity, Affordability Attract ‘Aspirational Middle- and Working-Class Families’**

According to one popular school of American economic development thought today, the principal thing states and localities need to do in order to succeed economically is accommodate the lifestyle and political preferences of a relative handful of highly educated, high-earning entrepreneurs and employees who mind little if housing, health care, and other necessities are expensive. In a July 2012 article for Slate magazine, one economist of this mindset, Raymond Fisman of Columbia University, went so far as to suggest that masses of ordinary Americans would benefit by relocating to high-cost states on the East and West Coasts and living off the “crumbs” of the “idea creators . . . who design iPhones and develop new drugs.”

The approach Texas has taken for economic development is altogether different. As Joel Kotkin and Wendell Cox emphasize in a survey of the Lone Star State’s economic regions appearing in a recent special edition of *City Journal*, Texas lawmakers regularly favor, whether by design or not, policies that keep both living and business costs down. Although, as Kotkin and Cox document, Texas has done very well at attracting young-adult residents with at least a bachelor’s degree education, the “economic opportunity and affordability” fostered by the state attracts “aspirational middle- and working-class families” alike.

Optional participation in the workers’ compensation system fits in well with Texas’ general approach to economic development. It helps make it possible for business owners to offer attractive wages for employees who are only moderately skilled or part-time as well as those who are highly skilled and able to work long hours. As previously discussed, when businesses are able to furnish an excellent insurance plan for injured workers at a low cost, most or all of the savings normally go into higher cash pay for employees or better 401(k) or vacation benefits.

In 2015, the average annual total compensation for Texas private-sector employees, including full-timers and part-timers, was \$50,675, after adjusting U.S. Commerce Department data for interstate differences in cost of living with indices calculated and published by the Missouri Economic Research and Information Center, a state government agency. Cost of living-adjusted compensation in Texas was higher than in all but two other states, and roughly \$5,400 above the national average.

Kotkin and Cox emphasize that, in addition to many “young, educated workers,” the estimated one million domestic migrants who have moved to the Houston and Dallas-Fort Worth metropolitan areas over the past 15 years “include many blue-collar workers seeking a better future. . . .” Flexible workplaces that are able to offer schedules suitable for parents of small children surely help explain why “the four big Texas cities all rank above the national average . . . in children per household.” Among the 50 major American metropolitan areas, in children per household, “Houston ranks third, Dallas-Fort Worth fourth, San Antonio fifth, and Austin sixth.”

## **In the Wake of the Great Recession, Every State Is Under More Pressure to Capture as Great a Share as Possible of All Domestic Growth**

Ample evidence that voluntary workers’ compensation is better than a compulsory system at protecting the legitimate interests of employers and employees and promoting prosperity for all types of people has been available for many years. Yet, it was only recently that other states began to investigate the Texas model seriously and consider to what extent it could serve as the basis for overhauling their own systems.

One important reason for the rapidly rising interest among state policymakers in the Texas workers’ compensation model has been reduced economic growth. Throughout most of the seven-and-a-half years since the end of the last recession, overall U.S. employment and incomes have risen only at a snail’s pace. Consequently, every state is under more pressure to capture as great a share as possible of all domestic growth.

In May 2013, a breakthrough was achieved when Oklahoma Gov. Mary Fallin signed S.B.1062, a sweeping revamp of Sooner State workers’ compensation including provisions authorizing any employer to exit the statutory system and offer a private benefit instead.

While the Oklahoma opt-out represented an attempt to replicate Texas’ success in encouraging firms to compete with one another to offer good coverage and claims service and superior medical outcomes without breaking the bank, the ability of employers to opt out was, unlike in Texas, subject to a number of statutory conditions. Peter Rousmaniere and Jack Roberts summarized them in a paper published by the New Street Group the month S.B.1062 was adopted:

[E]mployers must pay benefits at least equal to those mandated in the existing statutory system. Employers, however, have extraordinary discretion in designing benefits and managing claims. . . . All employers in Oklahoma must continue to provide work-injury benefits, whether through the existing state system or under these new provisions.

Another important difference between Texas nonsubscription and the Oklahoma opt-out was that, unlike nonsubscribing Texas employers, employers opting-out in Oklahoma would “retain immunity from virtually all negligence suits based on unsafe conditions or safety issues.”

While Oklahoma’s private plans were legally required to offer benefits equivalent or superior to those furnished under state workers’ compensation, the early results showed the benefits from other provisions. For example, employers could “require immediate reporting of injuries, control the selection of treating doctors, separate occupational from non-occupational medical conditions,” and decide when recovering employees must come back to work. Private plans enabled employers to reap large cost savings and sharply curtail the number of claims disputes.

A data analysis released by the Association for Responsible Alternatives to Workers’ Compensation in September 2016 showed that, over the course of two years, opt-out employers in Oklahoma achieved 70 percent savings in injury claim costs, compared to employers that stayed in workers’ compensation. Roughly 3.7 percent of private-plan claims were disputed, compared to 15 percent for workers’ compensation plans. Moreover, the private plans typically furnished better wage-replacement benefits for injured employees than workers covered under the state system.

After the new Oklahoma plan was adopted, a reform coalition including several large multistate employers that had already successfully implemented private plans for their Texas operations began pushing for enactment of opt-out legislation (in all cases more akin to the Oklahoma model than Texas’ pure voluntarism) in a number of states, including Tennessee.

Unfortunately, shortly before this paper was written, the Sooner State Supreme Court put an abrupt halt to elected officials’ modest, but very promising deregulation of workplace-injury insurance. Incredibly, *Vasquez v. Dillard’s*, the legal case used by a 7-2 majority of the justices on the court to void Oklahoma’s opt-out plan, hinged on

whether a claimed shoulder/neck injury suffered by an employee while at work for an opt-out company stemmed from a preexisting condition.

As Justice James Winchester explained in his dissent, joined by one other justice, if the company and its medical experts were correct in asserting that the plaintiff’s ongoing medical problems were the result of a preexisting condition, then she would not have been entitled to have her treatment covered under the state workers’ compensation system. Moreover, if a court determined the company’s assessment was wrong, it could simply have ordered the company and its insurer to cover the treatment while leaving S.B.1062 fully intact. Instead, egged on by the trial lawyers and major insurance company trade groups who had filed amicus briefs in the case, seven justices chose to disregard the facts at hand in order to, in Winchester’s words, “correct the Legislature.”

## Proposed Federal Takeover of Workers’ Compensation Is Latest Threat to Voluntarism

Attorneys who benefit from all the litigation stemming from claims disputes under state workers’ compensation statutes, such as Bob Burke of Oklahoma City, applauded the *Vasquez* decision’s judicial activism. Insurance trade association attorney Steven Bennett went so far as to predict that this ruling could deter legislatures in other states from “going forward with any opt-out provisions.”

However, as Minick pointed out to journalist J. Todd Foster, before the judicial death sentence came down, the “two-year experiment in Oklahoma” had already appeared to provide “concrete confirmation that the meaningful successes achieved through the Texas alternative to workers’ compensation can be exported to other states.” Minick expects Sooner lawmakers will eventually try to pass new legislation permitting private injury-benefit plans that can withstand challenges in the Oklahoma judiciary. He also expects other states to continue pursuing workers’ compensation alternatives.

Former Labor Secretary Perez and other zealous champions of bureaucratic regulation of business inside the agency he headed also clearly are not assuming that *Vasquez* will suffice to quash challenges to compulsory participation in government-formulated injury-benefit plans. In March 2016, in an interview with Howard Berkes of National Public Radio, Perez confirmed that he had, evidently in response to the letter he had received from a handful of Capitol Hill politicians a few months earlier,

launched a probe focusing “on a practice by thousands of employers in Texas and Oklahoma to opt out of conventional state workers’ compensation in favor of [private] benefits plans. . . .”

Over the course of the Labor Department investigation, an undisclosed, but apparently substantial number of nonsubscribing businesses received subpoenas from the agency ordering them to prove that their injury-benefit plans complied with ERISA. Perez apparently hoped to find evidence that ERISA insurance plans in Texas were improperly restricting employee access to benefits.

Judging by the report ultimately issued by the Labor Department in October 2016 (“Does the Workers’ Compensation System Fulfill Its Obligations to Injured Workers?”), however, Perez and his team did not actually find any instances of ERISA noncompliance. At least, if they did, the report’s authors did not deem them to be of sufficient importance to mention.

Instead of citing instances where employers have failed to comply with ERISA requirements such as uniformity of benefits for eligible employees and transparency, the Labor Department report prodded Congress to establish new “standards” for workers’ compensation and authorize federal bureaucracies to step in if state “workers’ compensation programs fail to meet those standards.” If Congress

takes the bait, future Labor Department chiefs who share Perez’ predilection for mandatory workers’ compensation will find it much easier to enforce their preferences. However, unlike the Oklahoma option, the Texas model does not require an alternative plan that would provide federal oversight of ERISA requirements. Therefore, if the federal regulators restrict or eliminate the ERISA alternative plans in Texas, the result would simply be the elimination of the many benefits such plans furnish for well over a million Texas employees; it would not require Texas employers to purchase workers’ compensation policies.

## Conclusion

In the wake of the judicial repeal of Oklahoma’s option, no other state currently joins Texas in allowing employers to choose whether to or not to subscribe to the worker’ compensation system. Nevertheless, career Labor Department officials apparently remain convinced that, unless it can somehow be abolished or at least impaired by Washington, D.C., the Texas model will be emulated in state after state. In light of the fact that more and more elected officials across the country are learning about how employers and employees alike in Texas and Oklahoma have benefited from the availability of alternatives to statutory workers’ compensation, this may well turn out to be the case. ★

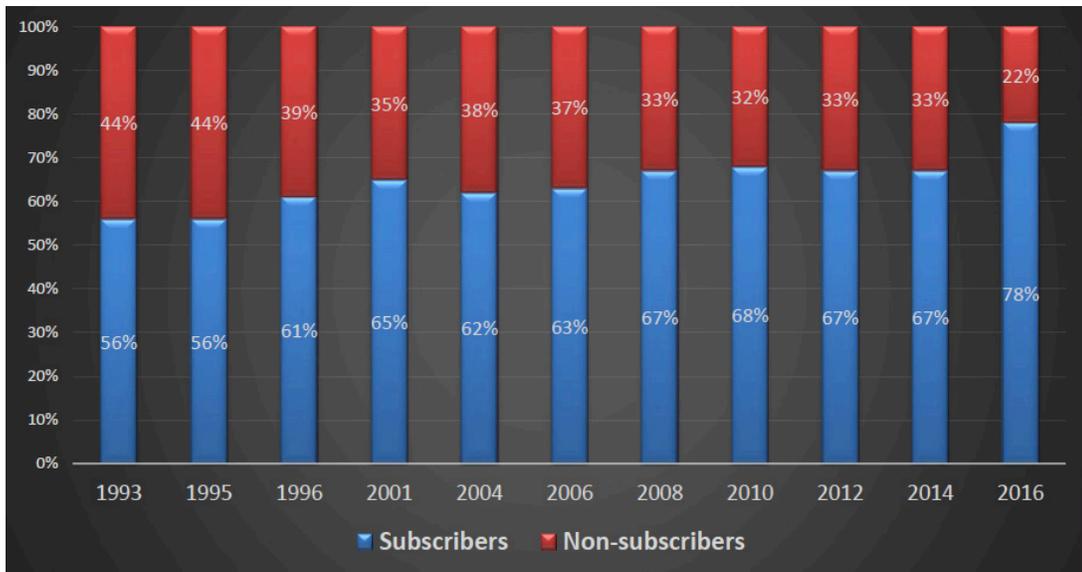
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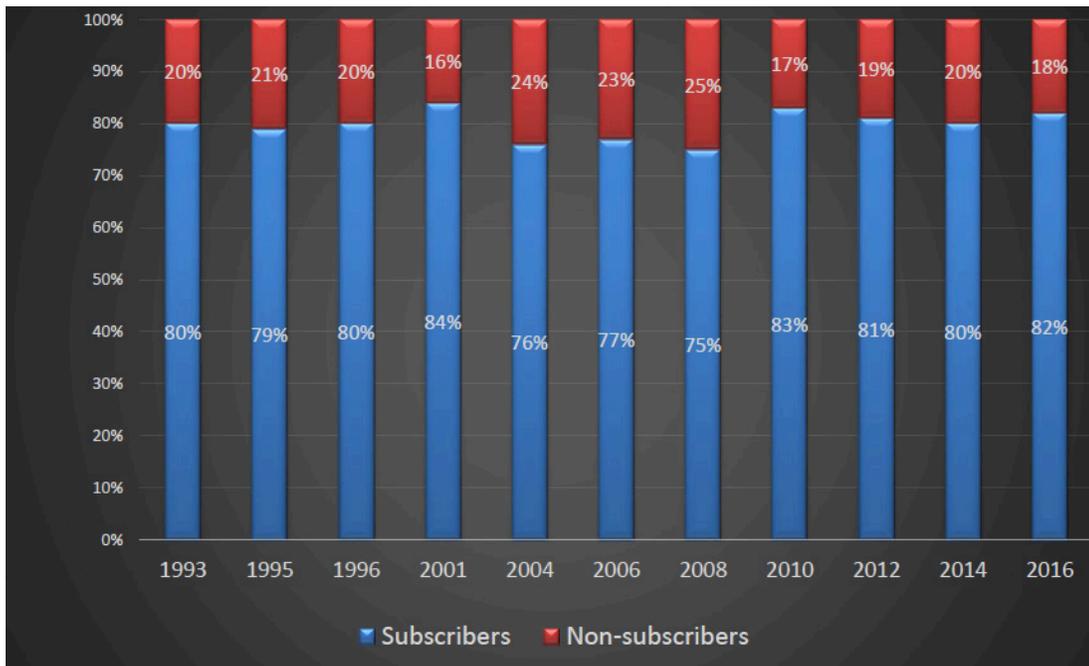
**Appendix**

**Percentage of Texas Private-sector Employers that are Subscribers and Non-subscribers: 1993-2016**



Source: *Survey of Employer Participation in the Texas Workers' Compensation System*, 1993 and 1995 estimates from the Texas Workers' Compensation Research Center and the Public Policy Research Institute (PPRI) at Texas A&M University, 1996 and 2001 estimates from the Research and Oversight Council on Workers' Compensation and PPRI, and 2004-2016 estimates from the Texas Department of Insurance Workers' Compensation Research and Evaluation Group and PPRI.

**Percentage of Texas Private-sector Employees Employed by Subscribers and Non-subscribers: 1993-2016**



Source: *Survey of Employer Participation in the Texas Workers' Compensation System*, 1993 and 1995 estimates from the Texas Workers' Compensation Research Center and the Public Policy Research Institute (PPRI) at Texas A&M University, 1996 and 2001 estimates from the Research and Oversight Council on Workers' Compensation and PPRI, and 2004-2016 estimates from the Texas Department of Insurance Workers' Compensation Research and Evaluation Group and PPRI.

### Primary Reasons Non-subscribers Did Not Purchase Workers' Compensation Coverage 2008-2016

Primary reasons given by non-subscribers	Percentage of non-subscribers				
	2008	2010	2012	2014	2016
Employer had too few employees	26%	25%	17%	21%	26%
Employers are not required to have workers' compensation insurance by law	11%	13%	17%	19%	24%
Workers' compensation insurance premiums were too high	26%	32%	15%	17%	18%
Employer had few on-the-job injuries	9%	12%	17%	20%	18%
Medical costs too high/Employer felt they could do a better job than the Texas workers' compensation system at reducing the costs of on-the-job-injuries	4%	5%	10%	16%	6%

Source: *Survey of Employer Participation in the Texas Workers' Compensation System*, Public Policy Research Institute at Texas A&M University and the Texas Department of Insurance Workers' Compensation Research and Evaluation Group, 2016.

### Primary Reasons Why Large Non-subscribers (500+ employees) Did Not Purchase Workers' Compensation Coverage 2008-2016

Primary reasons given by non-subscribers with 500+ employees	Percentage of large non-subscribers				
	2008	2010	2012	2014	2016
The employer felt the company could do a better job than the Texas workers' compensation system at ensuring that employees injured on the job receive appropriate benefits (medical and wage loss)	NA	28%	20%	30%	30%
Medical costs too high/Employer felt they could do a better job than the Texas workers' compensation system at reducing the costs of on-the-job-injuries	13%	10%	24%	23%	31%
Employer not required to have workers' compensation insurance by law	NA	2%	14%	15%	17%
Workers' compensation insurance premiums were too high	49%	50%	23%	21%	14%

Source: *Survey of Employer Participation in the Texas Workers' Compensation System*, Public Policy Research Institute at Texas A&M University and the Texas Department of Insurance Workers' Compensation Research and Evaluation Group, 2016.

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