Proper Reserving

When a workers’ compensation claim occurs, the insurer incurs a financial obligation to pay the future cost of the claim. Proper accounting requires the insurer to set aside the amount necessary to pay the claim. While the exact cost of this future obligation is unknown, the insurer needs to estimate the future cost of the claim as accurately as possible in order to set aside the appropriate amount of money to pay the claim. The money set aside to pay the claim is referred to as the claim reserve. [WCx]

It is common practice in the workers’ compensation field to break the reserve down into components. The three major components of the reserve are:

* Medical cost
* Indemnity cost
* Expenses

Some insurers will break the expense component into two parts, expenses and legal.

**Medical:**

**To establish** how much money should be placed in the medical component of the reserve, the workers’ compensation adjuster will estimate the cost of:

* Physicians
* Hospitals
* Diagnostic testing
* Physical therapy
* Ambulance
* Prescriptions
* Durable medical equipment
* Attendant care
* Other medical cost

A dollar amount is estimated by the adjuster for each of the above types of medical care based on the adjuster’s initial investigation establishing the nature of the injury and the level of severity of the injury. For a sprained ankle, the adjuster might assign the following amounts to each category:

* Physicians $1,000
* Hospitals
* Diagnostic testing $1,000
* Physical therapy $2,000
* Ambulance
* Prescriptions $ 250
* Durable medical equipment
* Attendant care
* Other medical cost \_\_\_\_\_\_

Total Medical Reserve $4,250

The medical reserving for an amputated hand might look like:

* Physicians $10,000
* Hospitals $25,000
* Diagnostic testing $ 2,000
* Physical therapy $ 5,000
* Ambulance $ 1,000
* Prescriptions $ 2,500
* Durable medical equipment $40,000
* Attendant care
* Other medical cost $ 2,000

Total Medical Reserve $87,500

**Indemnity:**

**To establish** how much money should be placed in the indemnity component of the reserve, the workers’ compensation adjuster will estimate the cost of:

* Temporary total disability (TTD)
* Temporary partial disability (TPD)
* Permanent partial disability (PPD)
* Permanent total disability (PTD)
* Rehabilitation / vocational expense
* Death benefits
* Dependent benefits

**A dollar amount** is estimated by the adjuster for each of the above types of indemnity benefit based on the adjuster’s initial investigation establishing the nature of the injury and the level of severity of the injury. For a sprained ankle, the adjuster might assign the following amounts to each category:

* Temporary total disability (TTD) $600 per week X 10 weeks = $6,000
* Temporary partial disability (TPD)
* Permanent partial disability (PPD)
* Permanent total disability (PTD)
* Rehabilitation / vocational expense
* Death benefits
* Dependent benefits \_\_\_\_\_\_

Total Indemnity Benefits $6,000

The indemnity reserving for an amputated hand might look like:

* Temporary total disability (TTD) $600 per week X 20 weeks = $ 12,000
* Temporary partial disability (TPD)
* Permanent partial disability (PPD) $600 per week X 250 weeks= $150,000
* Permanent total disability (PTD)
* Rehabilitation / vocational expense
* Death benefits
* Dependent benefits \_\_\_\_\_\_\_\_

Total Indemnity Benefits $162,000

**Expenses:**

**To establish** how much money should be placed in the expense component of the reserve, the workers’ compensation adjuster will estimate the cost of:

* Medical reports
* Independent medical examinations or peer reviews
* Experts
* Attorney
* Court reporters
* Surveillance
* Any other expense.

**As with** the medical component and indemnity component of reserving, an estimated amount is assigned to each expense category and the total estimated expenses is established. [WCx]

**Total Reserve:**

**The total reserve** on the file is the combined amount of cost estimated by the adjuster for medical + indemnity + expenses.

**The workers’ compensation adjuster** should establish the initial reserve within 48 to 72 hours of the claim creation. The adjuster should review the reserve whenever there is important new information obtained that impacts both the amount and type of medical treatment, or impacts the amount of indemnity that will be paid. It is often the goal of the adjuster to establish the ultimate estimated value of the claim (reserve) within 6 months of the initial report of the claim.

**Accurate reserving** is very important to the insurer in establishing the amount of money to be set aside for the claim. Accurate reserving is also important to the employer as the severity of the claims, as reflected by the reserving, is a part of the calculations used by the underwriters in establishing the premium for future years.