The Importance of Classification Codes

**Simple Mistake that Costs Employers Money**

Employers who have a complete safety program, proper medical management of their workers’ compensation claims and a strong return-to-work program can overpay for their workers’ compensation insurance if they (or their insurance broker or their insurance company) make a simple mistake. The use of the wrong classification code(s) for their business is a simple mistake that has cost a lot of employers excessive workers’ compensation premiums.

The National Council on Compensation Insurance (NCCI) is the insurance data and rating bureau used in 38 states to set insurance rates. The 12 other states either utilized a modified version of the NCCI classification codes or have their own classification codes. The NCCI has over 700 classification codes to describe the work done by businesses. Some states that use their own classification codes, and not the NCCI codes, have in excess of a 1,000 codes. [WCx]

**Class Codes Are Job Definitions Used by Insurance Company**

Classification codes are basically a list of job definitions used by the insurance company underwriters to describe your business and to place your business in a group of businesses that do the same type of work. The classification codes are a four digit number with a job description definition assigned to each number. The classification codes are used by all insurers writing business in the state.

Classification codes are used for several reasons including:

* Employers within the same industry have similar exposure to risk of loss
* The cost of workers’ compensation can be fairly distributed among employers
* Large employers with many different types of operations and many different types of employees would be impossible to rate accurately if every employee or every occupation was individually rated
* The classification of employers promotes safety, as the employers knows they are being compared to other employers in the same business

**Every Code Assigned Rate Used to Calculate Premium**

Every classification code will have an assigned rate that is used to calculate the workers’ compensation premium. Improper classification of a business can result in the wrong rate being used to calculate the premium.

**3 Occurrences to Select Wrong Code**

**Insurance Broker**

The errors in classification codes occur most often with the insurance. Unless the broker is both very well versed in the 700+ classification codes AND has a very good understanding of the nature of your business, the broker may select the wrong classification code. The wise broker will ask the prospective client various questions designed to establish the types or work performed by the employer and the exact nature of the employer’s business. Based on the answers provided by the employer, the broker will assign a classification code for the business.

**Insurance Company**

A second point in the process where the employer may receive the wrong classification code is when the insurance company underwriter reviews the new coverage application. If the underwriter concludes the broker used the wrong classification code, the underwriter will change the classification code to the code the underwriter believes is a better match in describing the nature of the insured’s business. Of course, the underwriter can make the wrong selection as well, resulting in the employer being charged the wrong amount for the workers’ compensation insurance.

**Insurance Company Auditor**

A third point where the wrong classification code can be assigned to the employer is when the insurance company performs a premium audit after the policy period has ended. If the insurance company auditor reviews the policy application information and determines a different classification code should have been used, it again can be changed.

**Hire Premium Auditor If You Have Concerns**

If you as the employer have any concerns about whether the correct classification code is being used, you can hire an independent premium auditor to verify the accuracy of the premium you are being charged. As premium auditors normally work on a percentage of the savings basis, the employer who is concerned that an incorrect classification code (or other errors have been made in the calculation of the work comp premium) should hire an independent premium auditor. For assistance in locating a premium auditor, please contact us.