**How to Create & Implement a WC Cost Allocation System**

**Introduction: (5 minutes – 2:05 pm)**

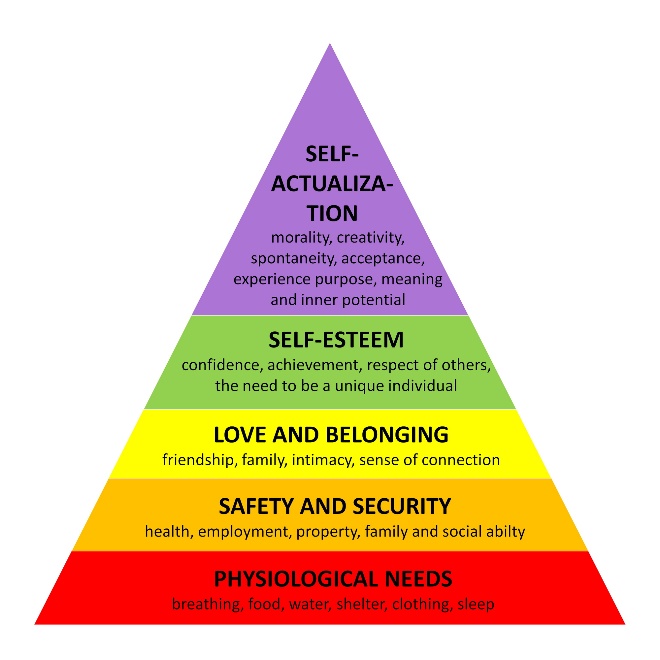
* Welcome to WC Mastery training
  + It’s not a question of HOW to manage WC
  + It’s about MOTIVATION and ENGAGEMENT in best practices
* Introduce 3 Major Points
  + Drivers of Behavior
  + Cost Allocation Systems & Examples
  + Steps to Implement Cost Allocation

**Main Point #1: Drivers of Behavior**

* Cost Allocation is Simply Motivating Behavior
  + “The only way to get someone to do something is by making them want to do it.”
    - – Dale Carnegie, How to Win Friends & Influence People
* ***Research Study: MIT “Large Stakes & Big Mistakes”:***
  + DRIVE – by Daniel Pink
  + Premise: A group of students was given a set of challenges:
    - Memorize digits
    - Word puzzles
    - Shooting a ball through a hoop
* Rewards: The cash rewards for performance were broken into three categories.
  + Small
  + Medium
  + Large
* Results:
  + mechanical skill only - rewards system worked as designed
  + Even rudimentary cognitive skill required: Opposite result
* Study has been replicated many times
* IF CAN UNDERSTAND WHY RESULT IT TRUE, YOU’LL UNDERSTAND HUMAN MOTIVATION & COST ALLOCATION

**Rosabeth Moss Kanter: Harvard Business Review**

* + **Hierarchy of Motivation at Work**
  + "*The key to motivation doesn't depend on elaborate incentive schemes. What makes a good work environment is getting better at stuff, or mastering a task."*



MEANING

MASTERY

MEMBERSHIP

MONEY

* Take aways:
  + If ONLY using Money in cost allocation, missing the point
  + Need to look to Meaning & Mastery for motivation
  + Cost Allocation works because give divisions Autonomy to control workers’ comp costs and ability to Master
    - Play guitar because enjoy it, not because going on tour
* **Examples of Profit Sharing:** 
  + **Charles Schwab** – Year 1903
    - Book “Succeed With What You Have”
    - “To no small extent the success of Bethlehem steel has been built up by our profit sharing system”
    - “…unique leadership hierarchy that afforded lower managers much independence and greater pay”
  + 80% of 22,000 men on profit sharing system
    - Bonuses computed on efficiencies;
    - Examples:
      * Mechanic: allotted time for work is 20 hours, if finishing w/in 20 hours gets 20% bonus, if finishes in 12 hours gets full pay and 20% bonus.
        + Free to work on other projects or go home
      * Armor Plates
        + Bonuses on quality of work rather than quantity
      * Other departments
        + Bonuses for efficiencies
        + “everything you save from this standard cost you will share”
  + **Andrew Carnegie:** First big American businessman to inaugurate profit-sharing
  + **Leadership Leverage Dial**
    - Top-Down
    - Bottom-Up
    - Flat
      * John Doerr “Measure What Matters”
      * *“I avoid asking people about their perception, I don’t ask do you feel your company is honest with you? I look at information flows. Does the company hord information, does it spread it out on a need to know basis, or is it flowing freely? If you go around your boss and talk to somebody more superior, are you punished or celebrated?*
      * *The flatter the org chart, the more agile the organization.”*
  + Additional reference:
    - **No Rules Rules – Netflix Book**
    - **Good to Great:**
      * 7 Factors in Good to Great Companies:
        + First Who, Then What:
        + “not a “genius with a thousand helpers” leadership model
    - **Simon Sinek – Start With Why**

**Main Point #2: Cost Allocation Systems & Examples**

* 3 Golden Rules of Cost Allocation:
  + Keep it Simple
  + Quickly provide feedback
  + Incentivize the Right Behaviors
    - Unintended consequences
* How are Operations Managers Held Accountable?
  + Control return to work, reporting claims culture, supervisor engagement
  + Goal should be to affect day-day decisions
  + Typically Profitability
* **Typical Cost Allocation**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 1 | 2 | 3 | 4 | 5 |
| Claim Costs | 350k | 200k | 200k | 200k | 50k |
| Allocated | 200k | 200k | 200k | 200k | 200k |
| Profits | $1.050m | $1m | $1m | $1m | $900k |
| Adjusted | $900k |  |  |  | $1.050m |

*No accountability at the level of control*

*No motivation to return an injured employee to light duty*

* **Full Cost Method**
  + Claims valued as of specified date at close of period
  + Budget based on 5 year-average
  + Make end-of-year adjustment based on actual performance

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1 | 2 | 3 | 4 | 5 | Total |
| Budget Based on 5- year Average | 40% | 35% | 10% | 10% | 5% | 100% |
| Budgeted Cost Allocation | 400k | 350k | 100k | 100k | 50k | 1,000,000 |
| Actual | 300k | 500k | 100k | 100k | 50k | 1,050,000 |
| Adjustment | (100k) | 150k | - | - | - | 150,000 |

*Training required on best practices to follow*

* **Full Cost w/ Free Labor Method**
  + If return employee to work, free labor for division
  + If do not return employee to work, indemnity charged to division
    - Free labor to maximum time limit & dollar amount
      * 10 weeks or $25k
  + Use variations that work for YOU
* **Handling Loss Development**
  + 2 methods:
    - Pick a date (like unit stat date for x-mod)
      * Jan 31st or similar
    - True up later in the year
      * Use an actuary to help
* **Lost-Time Method**
  + Each department is allocated WC costs based on number of lost workdays
  + Two options:
    - Cost per day
      * NCCI = $1500 / day
      * Your Company = $1,000 / day
    - % of total

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1 | 2 | 3 | 4 | 5 | Total |
| Budget Based on 5- year Average | 40% | 35% | 10% | 10% | 5% | 100% |
| Budgeted Lost Work-Days | 400 | 350 | 100 | 100 | 50 | 1,000,000 |
| Cost Per Lost Day | $1,000 | $1,000 | $1,000 | $1,000 | $1,000 |  |
| Actual | 300 | 500 | 100 | 100 | 50 | 1,050,000 |
| Adjustment | (100k) | 150k | - | - | - | 150,000 |

* **Flat Charge Per Claim Method**
  + $25k charged per claim;
  + Not reported w/in 24 hours $5k extra charge
    - Unintended consequence?
    - NCCI - $1,500 / day cost
  + If bring back on light duty w/in 4 days - 50% discount
  + Free labor on light duty
    - Unintended consequence?
  + Bonuses based on claims frequency
* Promoting:
  + Prevention
  + Reporting
  + Return to Work
* **Total Incurred w/ Refunds Per Claim Method**
  1. Take the total incurred each month
  2. Reporting w/in 24 hours = 20% refund
  3. RTW w/in 4 days = 30% refund
  4. Calculate 1 - 2 - 3 to get the total charge for the claim for the month, and subtract from any other previous charges

|  |  |  |  |
| --- | --- | --- | --- |
|  | May | June | July |
| Total Incurred | 10,000 | 7,500 | 7,000 |
| Reporting Refund | (2,000) | (1,500) | (1,400) |
| RTW Refund | (3,000) | (2,250) | (2,100) |
| Claim Cost to Unit | 5,000 | 3,750  (1,250 credit this month) | 3,500 (250 credit this month) |

* Monthly reporting on Status:
  + “if all conditions were met, you would have saved an additional $4,000”
* Need system to track RTW Dates & Injury Reporting
  + Coordinate with TPA/Carrier
* **Notes**
  + Where cap impact of one claim?
    - At retention level
  + How handle light-duty compensation?
    - Free Labor
  + Simple reporting options
    - Coding of payroll, accounting, etc.
  + **Worst to Best List**

**Main Point #3: Steps to Implement Cost Allocation**

* **Implementation Tips**
  1. Evaluate what want to motivate
  2. Develop method around goals
  3. Once determine method, critically analyze what will actually motivate
     + Unintended consequences
  4. Monitor and adjust
* Drive adoption with Success
  1. Good to Great:
  2. Kroger: Jim Herring, CEO (change to superstores in 80s & 90s)
     + *How do you make over 50,000 people, cashiers, baggers, etc embrace change? You don’t, not in one big event anyway; “we presented what we were doing in a way that people saw our accomplishments…to gain confidence from the successes, not just the words”*
* Pilot
  1. Identify most liberal or proactive manager for Pilot of new program
  2. Need senior management support, CEO, CFO
* Don’t get lost in numbers, tie back in to Human Motivation concepts