



**WORKERS' COMP
TRAINING CENTER**

How to Create & Implement a WC Cost Allocation System

Introduction: (5 minutes)

- 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

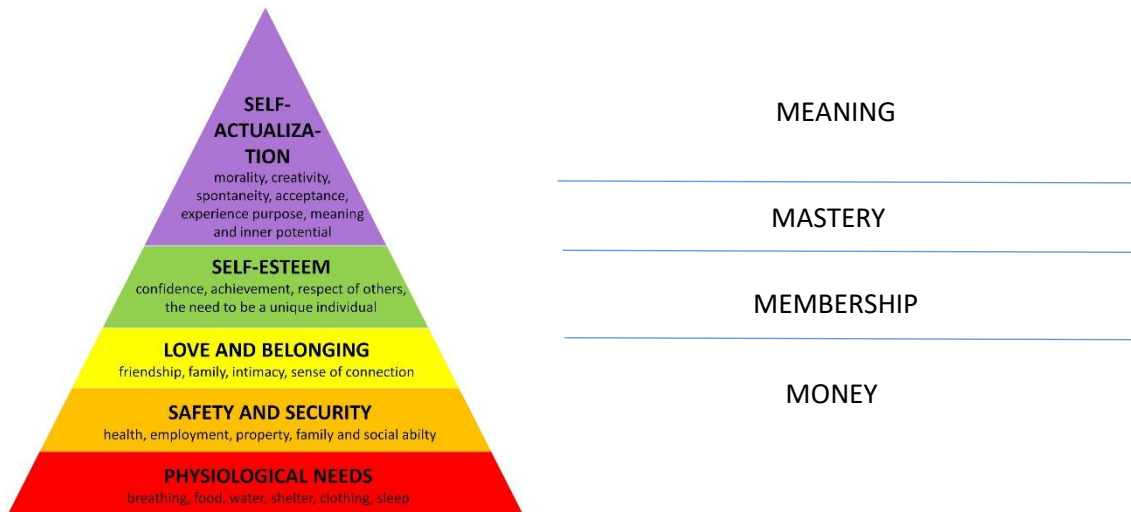
Main Point #1: Drivers of Behavior (15-20 mins)

- 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



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- 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."*



- Take aways:
 - If ONLY using Money in cost allocation, missing the point
 - Need to look to Meaning, Mastery, and Membership 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”



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- 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
- Additional reference:
 - **John Doerr “Measure What Matters”**
 - *The flatter the org chart, the more agile the organization.*”
 - **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

- No Gold Standard for Cost Allocation.
- 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
- **Full Cost Lag Time Discount**
 - 20% discount on claim charge if reported within 24 hours
- **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**
 - Don't get lost in numbers, tie back in to Human Motivation concepts

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 engaged 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