Workers' compensation reform means jobs, tax savings

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Introduction

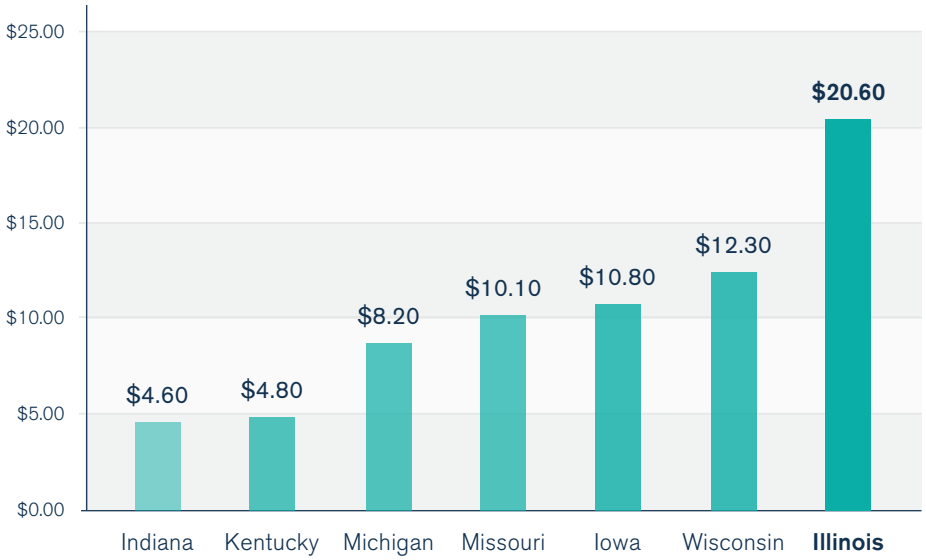
Illinois employers have made it clear that the state's workers' compensation system makes doing business costly — and has driven many businesses out. The system even heaps massive costs on state and local governments, which face workers' compensation claims by government workers regularly. If Illinois could embrace true reform, workers, businesses and taxpayers would all benefit.

Illinois' workers' compensation system is by far the most costly in the Midwest and the seventh-most-expensive system nationwide, according to a 2014 biennial study of all states produced by the Oregon Department of Consumer and Business Services.[1]

Workers' compensation has been a major pain point in Illinois for riskier industries such as manufacturing, construction and transportation, putting Illinois at a significant disadvantage in competing for jobs with other states, and running up hundreds of millions of dollars of excess costs for taxpayers.

Take, for example, the premium that employers must pay for masonry workers in Illinois. A business would save $16 per $100 of payroll by moving from Illinois to Indiana. Thus, a business with 100 masons making $45,000 per year would save $720,000 per year just on workers' compensation by relocating from Illinois to Indiana.

Workers' compensation premium for masonry workers
Premium per $100 of covered payroll by state for insurance class 5022



Source: National Council on Compensation Insurance, state regulatory agencies **@illinoispolicy**

Understanding Illinois' workers' compensation structure

Workers' compensation is a type of insurance required of employers to "make workers whole" by replacing lost wages and paying for medical benefits for workers who are injured as the result of a workplace incident. Workers' compensation also provides large payments for workers who suffer permanent injuries. In return for being "made whole," workers give up the right to file lawsuits against their employers for negligence. This is a trade-off: Workers who are hurt need not worry about lost wages and medical fees, and employers don't have to worry about negligence lawsuits over injuries. The system is "no fault," meaning that it does not matter if the employer did anything

wrong (i.e., was at fault) so long as the injury occurred in the course of employment.[2] Each state sets up and regulates its own system, and it is worth noting that Illinois courts lately have adopted a broad definition of what constitutes an injury in the course of employment.

While Illinois' current workers' compensation system can be fixed a variety of ways, many of which are spelled out in this report, it is also important to consider that workers' compensation is an industrial-age policy that doesn't necessarily fit many 21st-century workplaces. While the current system certainly should be fixed, alternative ways to administer the same type of benefits outside of the current system also should be considered.

Illinois' system is particularly costly for several reasons, including: Illinois holds the employer responsible for the full cost of an employee's injury even when a workplace event represents a tiny fraction of the injury's cause; loopholes in medical cost regulations; a high medical fee schedule; wage-replacement ratios that are out of line with those in surrounding states; high settlement payments; and the regulatory cost of long wait times to resolve claims for both workers and businesses. Industrial employers that leave Illinois or choose to expand elsewhere regularly cite workers' compensation as a reason for relocation. The heavy cost of workers' compensation is clustered in Illinois' higher-risk, blue-collar industries, the very same industries that, according to Bureau of Labor Statistics data, have been paying lower wages[3] in Illinois than in surrounding states and have been hemorrhaging jobs[4] from the Land of Lincoln.

This study will show the major cost differences for workers' compensation between Illinois and surrounding states, reveal which aspects and legal changes to Illinois' workers' compensation system have caused the most economic harm and job losses, explain the sections of Illinois law that are out of line with surrounding states, and suggest policy reforms to modernize Illinois' system. Adoption would bring costs more in line with other states, allowing Illinois workers to compete for good-paying jobs again. Another important factor to consider, which will be covered in a future report, is how Illinois' system drains taxpayer resources.

Recognizing the pain points

How much does workers' compensation insurance cost employers – and why does it hurt job creation?

In 2014, the Oregon Department of Consumer and Business Services released a biennial study of all states. The Oregon study compares workers' compensation costs among the states, averaged across industries, and shows that as of 2014, Illinois has the most expensive system in the Midwest and the seventh-most-expensive system nationwide. According to the study, the premium paid for workers' compensation insurance in Illinois is $2.35 per $100 of covered wages, which amounts to an additional 2.35 percent cost on all covered payroll, compared to significantly lower rates in surrounding states.

Workers' compensation premium-rate rankings for Illinois and surrounding states

Workers' compensation premium per $100 of covered payroll by state

State	Premium
Indiana	$1.06
Kentucky	$1.51
Michigan	$1.68
Ohio	$1.74
Iowa	$1.88
Wisconsin	$1.92
Missouri	$1.98
Illinois	**$2.35**

Source: 2014 Oregon workers' compensation premium-rate ranking summary **@illinoispolicy**

The Oregon rankings don't perfectly reflect reality because they reveal what state-by-state premiums would look like if each state had the same industrial and labor makeup as exists in the Oregon economy. However, the Oregon rankings allow for an apples-to-apples comparison of how costs compare across states under the assumption that they have the exact same industries.

The major problems for certain industries that are caused by Illinois' workers' compensation system are not obvious when looking at the overall average costs of the system. The Oregon rankings show that the average employer would save about $1.30 per $100 of payroll by moving its labor force from Illinois to Indiana. However, a 1.3 percent difference in payroll costs can be a major driver of success or failure for businesses that operate on single-digit profit margins and compete across states. Moreover, the overall major cost differentials between states are found clustered in a few industries, where the cost differences amount to a substantial portion of overall payroll costs between Illinois and other states.

Given the same industrial makeup, workers' compensation costs in Indiana are 55 percent lower than in Illinois. However, looking just at averages is not the best way to understand the economic pain Illinois' system causes.

For example, Marty Flaska,[5] the CEO of Hoist Liftruck Manufacturing Inc., moved his company of 300 workers to Indiana and cited the fact that he could save millions of dollars and avoid frivolous workers' compensation injury claims. The outsized cost of workers' compensation and the major areas of cost differential with other states are concentrated in riskier industries such as manufacturing, construction and transportation. The majority of white-collar desk jobs in industries such as business services, finance and technology have negligible workers' compensation costs; no significant savings are to be achieved between states in these sectors, which account for a large portion of Illinois' labor force.

A smaller portion of Illinois' workforce is in riskier industries such as manufacturing, transportation and construction than most surrounding states. But Illinois' workers' compensation system has a disproportionate effect on these sectors, and has certainly contributed to Illinois losing out on new manufacturing and transportation jobs.

Illinois has a smaller percentage of total jobs in riskier industries such as production (manufacturing), transportation and construction

Percentage of jobs in production, transportation, construction and all 3 industries combined by state

State	Production	Transportation	Construction	Combined
Indiana	12.8%	8.5%	3.8%	25.1%
Kentucky	10.6%	9.6%	3.8%	23.9%
Iowa	10.2%	8.3%	4.4%	22.9%
Wisconsin	11.4%	7.5%	3.5%	22.3%
Ohio	9.5%	7.4%	3.3%	20.3%
Michigan	10.4%	6.3%	3.0%	19.7%
Illinois	**7.5%**	**8.1%**	**3.1%**	**18.6%**
Missouri	7.2%	6.6%	3.7%	17.4%

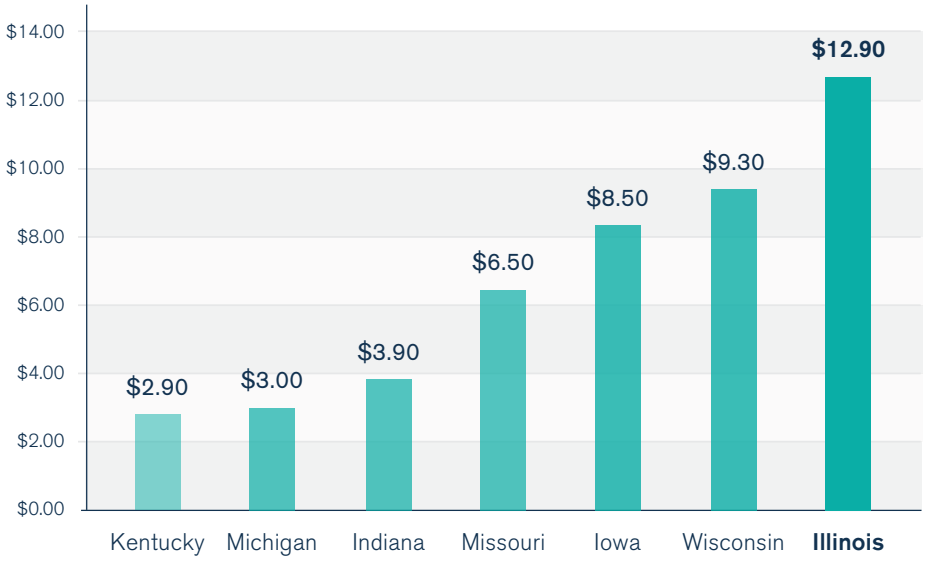
Source: Bureau of Labor Statistics, "Occupational Employment Statistics" **@illinoispolicy**

Illinois' workers' compensation costs for industries such as manufacturing, construction and transportation can be three to five times more expensive than in other states. One example of a manufacturing cost comparison is for train-car manufacturing workers, insurance class code 3881. The premiums for surrounding states range from $2.90 per $100 of payroll in Kentucky and $3.90 in Indiana, to $12.90 in Illinois. A business that manufactured train cars would save $9 per $100 of payroll by moving from Illinois to Indiana.

To show the effects of this range of differences, a business with 100 rail-car manufacturing employees making $45,000 per year would save $405,000 per year just on workers' compensation by moving from Illinois to Indiana.

Workers' compensation premium for rail-car manufacturing

Premium per $100 of covered payroll by state for insurance class 3881

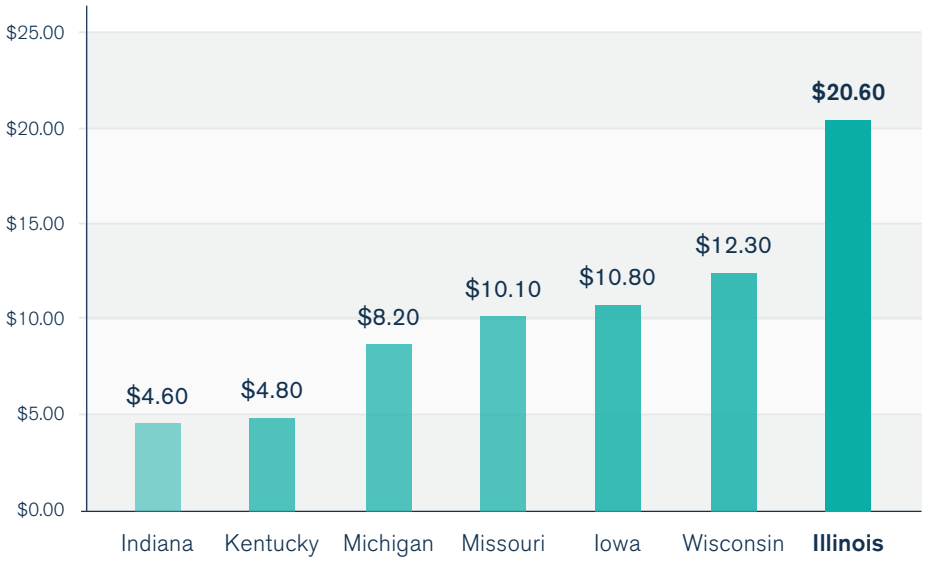


Source: National Council on Compensation Insurance, state regulatory agencies **@illinoispolicy**

In accounting terms, the present value of the savings a business would achieve by moving 100 manufacturing workers from Illinois to Indiana is $5.8 million in total, calculated using a 7 percent discount rate.

An example from the construction trades is masonry, insurance class code 5022. The premiums for Illinois and surrounding states range from $4.60 per $100 of payroll in Indiana to $20.60 in Illinois. In this case, a business would save $16 per $100 of payroll by moving from Illinois to Indiana. Thus, a business with 100 masons making $45,000 per year would save $720,000 per year just on workers' compensation by relocating from Illinois to Indiana.

Workers' compensation premium for masonry workers
Premium per $100 of covered payroll by state for insurance class 5022

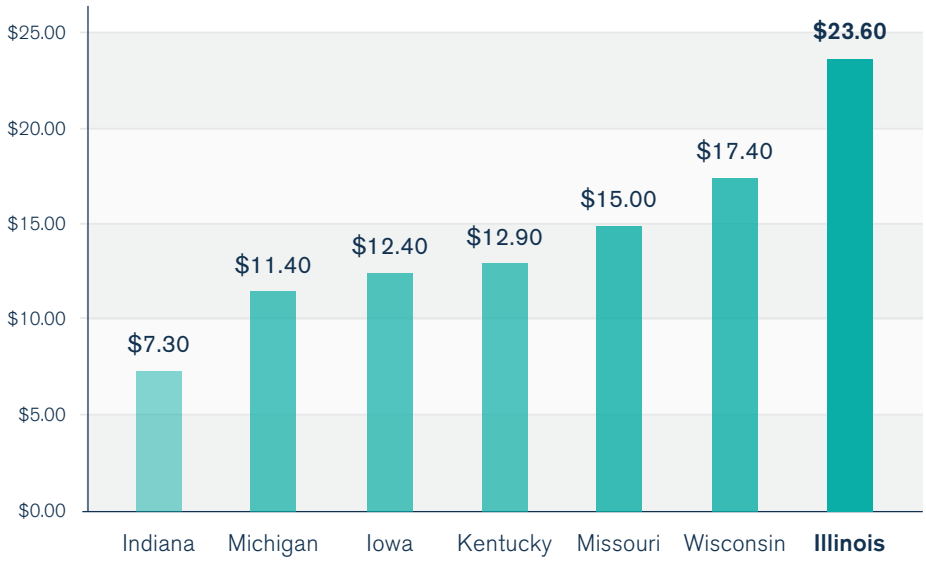


Source: National Council on Compensation Insurance, state regulatory agencies **@illinoispolicy**

The present value of this business savings from moving 100 construction workers to Indiana is $10.3 million in total, calculated using a 7 percent discount rate.

Finally, consider the transportation industry's truck drivers who deliver packages or parcels, insurance class code 7230. The premiums for surrounding states range from $7.30 per $100 of payroll in Indiana to $23.60 in Illinois. In this case, a business would save $16.30 per $100 of payroll by moving from Illinois to Indiana. Under this scenario, a business with 100 truck drivers making $45,000 per year would save $733,500 per year just on workers' compensation costs by relocating from Illinois to Indiana.

Workers' compensation premium for trucking: Parcel and package delivery
Premium per $100 of covered payroll by state for insurance class 7230



Source: National Council on Compensation Insurance, state regulatory agencies **@illinoispolicy**

The present value of this business savings from moving 100 transportation workers to Indiana is $10.5 million in total, calculated using a 7 percent discount rate.

In short, the regulatory cost of doing business in Illinois versus another state can be measured by the present value a small manufacturing, construction or transportation business could achieve by leaving Illinois for Indiana. When the value of moving to Indiana is in the millions of dollars just on the line item of workers' compensation alone, it's no wonder that industrial employers are leaving Illinois and few are moving to Illinois in these industries. This puts Illinois workers at an unfair disadvantage; they have a harder time keeping their jobs when Illinois businesses struggle to compete with businesses in other states and countries. Illinois' anti-business policy is ultimately anti-jobs and anti-worker.

Illinois needs real workers' compensation reform

A range of public figures have agreed that Illinois' workers' compensation system is broken, from Caterpillar Inc. CEO Douglas Oberhelman, who says Caterpillar is hindered from expanding in Illinois by the state's current workers' compensation laws,[6] to Illinois Attorney General Lisa Madigan, who describes[7] how it is difficult for her to defend the state against government-employee workers' compensation claims given the state's weak causation standard.

Illinois' unbalanced workers' compensation policy drives out businesses and jobs, eats into the budget of nonprofit organizations that provide crucial services, drives up taxpayers' costs for covering government employees, and raises the cost of private and public construction projects for individual consumers and taxpayers alike.

Many Illinois industrial companies are less competitive due to the state's workers' compensation law alone. Workers' compensation is a policy area ripe for reform in Illinois. Getting it right would establish fairness for both workers and employers, and would fix issues such as the high cost to employers, long injury recovery times, excessive waiting times for payments to injured workers, and the unreasonable burden of workers' compensation costs on taxpayers. A successful reform would result in more industrial investment, economic growth and job creation in the Land of Lincoln; faster

payments for injured workers; and likely hundreds of millions[8] of dollars in annual savings for Illinois taxpayers; with an overall reduction of fraud and abuse in Illinois' much-maligned system.

To understand the current system for workers' compensation in Illinois, this report will next address the recent legislative history on changes made to the workers' compensation law.

Legislative history

Gov. Rod Blagojevich's 2005 workers' compensation law

Illinois' recent history regarding workers' compensation legislation began with House Bill 2137, which former Gov. Rod Blagojevich signed into law in 2005. Public Act 094-0277[9] (formerly HB 2137), summarized on the Illinois Workers' Compensation Commission's website,[10] made several significant changes to Illinois' system. Some changes directly increased the cost of the workers' compensation system, while others were designed to contain and regulate costs.

The 2005 law was notable in that it addressed workers' compensation in a comprehensive way. However, the promised cost savings did not add up. In a press release after the signing,[11] Blagojevich said, "Illinois is the 19th most expensive state in the nation when it comes to workers' compensation premiums. Illinois companies pay 40 percent more for workers' compensation than neighboring states Michigan, Wisconsin and Indiana."

The 19th-most-expensive state in 2005 became the fourth-most-expensive state for premiums in 2010, soon after Blagojevich's law went into effect, according to the biennial study by the state of Oregon. Illinois is currently the seventh-most-expensive state in the nation for overall workers' compensation costs and is easily the most expensive in the Midwest — notwithstanding the passage of the 2005 supposed reform bill and a 2011 reform bill, signed into law by then-Gov. Pat Quinn.

The following is a breakdown of the important changes included in the 2005 workers' compensation legislation:

1. Medical fee and billing changes

The 2005 legislation changed regulations regarding medical fees, medical utilization and patient balance billing.

Medical fees

The legislation created a workers' compensation medical fee schedule to regulate the cost for medical care sought through workers' compensation claims. The payment schedule was set to be the lesser of the actually incurred medical fees or "90 percent of the 80th percentile of actual charges" within a geographic area for a given procedure. The 80th percentile charges for a procedure in an area are initial charges that are more expensive than four out of five bills for that procedure in that area, and don't take into account significant cost savings that are negotiated through group health programs. Ninety percent of that amount is taken and set as a maximum that can be billed. The law also set up a Medical Fee Advisory Board to regulate and advise on this process.

Medical utilization review

The law created a way for employers to check the quality and medical necessity of health care services. This created an avenue for employers to reject certain health care procedures they think are unnecessary if another utilization-review physician supports denial of medical necessity.

Balance billing prohibited

The law required that medical bills be sent directly from the medical provider to the employer for reimbursement. If the employer does not pay the entirety of the bill, the medical provider is barred from billing the injured worker for the unpaid balance unless the Illinois Workers' Compensation Commission determines that the unpaid balance should not be a part of the final settlement paid by the employer.

2. Benefit increases and changes

One of the most direct ways in which the 2005 law drove workers' compensation costs higher was through increasing wage-replacement rates, settlement awards and the valuation of certain types of injuries.

Death benefits and burial expenses

The maximum award for a work-related death was raised to the greater of $500,000 or 25 years of wage replacement from the greater of $250,000 or 20 years of wage replacement. In addition, burial expenses were raised to $8,000 from $4,200.

Minimum and maximum wage-replacement rates increased, maximum benefits for disfigurement and body-part loss raised

One of the major cost drivers of the 2005 law came from increases in wage-replacement rates. In general, workers' compensation benefits are two-thirds of lost wages, untaxed. However, there are minimum rates of wage replacement that workers are guaranteed, as well as maximum wage-replacement rates that act as a cap on possible weekly benefits. The 2005 law put Illinois' minimum wage-replacement ratios out of line with those in surroundings states.

Minimum compensation rates increased

The minimum compensation-replacement rate was raised to the lesser of two-thirds of the state's actual minimum wage rate times 40 hours per week, or the employee's full actual wages, untaxed. The following chart shows the minimum replacement-rate increases per dependent, using the state minimum wage of $6.50 per hour in effect in Illinois in 2006:

Base rate: $6.50 X 40 = $260

Single person: $260 X 66 2/3% = $173.32
Person with 1 dependent: $260 X 76 2/3% = $199.32
Person with 2 dependents: $260 X 86 2/3% = $225.32
Person with 3 dependents: $260 X 96 2/3% = $251.32
Person with 4+ dependents: $260 (100% of calculation)

The idea behind this is to guarantee a decent wage replacement for low-income workers. However, it also ties part-time workers to a full-time wage-replacement schedule. And now, the numbers in the chart above are bumped up significantly based on Illinois' 2016 minimum wage of $8.25 per hour. In effect, a low-wage or part-time worker can get a pay hike by being on workers' compensation. This occurs when a part-time worker gets his or her entire lost wages replaced untaxed, which ends up being more money than when the same worker pays taxes.

With Illinois' current minimum wage of $8.25 per hour, any part-time worker with no dependents making $220 per week or less ($8.25 x 40 x 2/3) will get all wages replaced, untaxed, by being on workers' compensation. Adding dependents increases this minimum to $253 (one dependent), $286 (two dependents), $319 (three dependents) or $330 (four or more dependents). The costly effect of this change is compounded by the fact that permanent settlement payments also often are based on this minimum compensation-replacement schedule.

The law also defined temporary partial disability benefits and raised the maximum wage-differential replacement to 100 percent of the state's average weekly wage for partial disability injuries. In addition, maintenance benefits for vocational rehabilitation were defined and set as no less than a worker's total temporary disability rate.

Finally, the maximum number of weeks of benefits for disfigurement or the loss of a body part was raised by approximately 7.5 percent across the board. For example, the maximum indemnity payment for a thumb loss was raised to 76 weeks from 70 weeks, for an index finger to 43 weeks from 40 weeks, and so on to address the entire schedule of body parts including hands, arms, legs, feet, toes, eyes and ears.

3. Fraud statute established and miscellaneous other changes

The law established criminal penalties for fraudulent claims and made anyone convicted of fraud liable to the employer in a civil suit. So far, this fraud statute has seen little use. The law also addressed issues with vocational rehabilitation, the rate-adjustment fund, and expediting the Workers' Compensation Commission process; it also increased some penalties for violations and established a workers' compensation fraud statute.

Gov. Pat Quinn's 2011 reform efforts

While the 2005 reforms left Illinois with the fourth-most-expensive workers compensation system in the nation,[12] a further attempt to reform workers' compensation in 2011 made limited progress toward lowering costs.[13] Illinois improved from fourth costliest to seventh costliest, and remains the most expensive system in the Midwest.[14] Just as importantly, Illinois' system remains slow and bureaucratic and can fail to provide injured workers with timely reimbursement for medical costs and lost wages.[15] Here are some of the changes made by the 2011 law:

1. Reduction in medical fee schedules

Like most states, Illinois sets a medical fee schedule that determines how much a medical provider can charge to treat an injured worker.[16] The 2011 reforms reduced costs by cutting fees 30 percent across the board. Actual costs fell by only 24 percent, in part because some providers negotiate around the system.[17] Savings also were offset by doctors' billing for more complex office visits, although this effect appears to be small.[18]

Studies prior to 2011 showed Illinois' fees were among the highest in the nation.[19] According to the nonprofit Workers' Compensation Research Institute, or WCRI, fees for major surgeries were 200 percent higher than the fees for the same surgeries in Minnesota, and 340 percent higher than fees in Michigan.[20] Some of this difference may reflect a higher cost of living in Illinois but the sheer magnitude of Illinois' cost premium makes it unlikely this is the major factor. Furthermore, costs for many procedures are 200 to 300 percent higher under workers' compensation than for Medicare patients in Illinois, which strongly implies workers' compensation costs are significantly inflated for some procedures.[21]

Cutting across the board did bring savings but many costs, like those for major surgeries, remain significantly higher than in other states even after a 30 percent cut. For other fees the reverse is true. Prior to the cut doctors' fees exceeded the average in other states by 14 percent.[22] Those fees are now lower than in surrounding states although it is not clear whether quality of care has suffered. As noted before, doctors recouped some of the lost fees by billing for more complex visits.

Currently, Illinois' fees are likely higher overall than those in surrounding states or under Medicare in Illinois. Across-the-board fee reductions, while somewhat effective, were also inadequate. Further cost savings are possible, but expanding the crude approach risks cutting access to some medical treatments, and policymakers need to be aware of the unintended consequences of changing incentives to doctors.

2. Repackaging

Medical pricing regulations can indirectly affect overall costs through changing the incentives for doctors. For example, Illinois law permits doctors to sell the drugs they prescribe directly to patients. The practice, known as repackaging, allows doctors to resell drugs at an average mark-up of 60 to 300 percent over the prices charged by pharmacists.[23] The premium not only increases the cost of drugs that must be paid by employers but changes the incentives to doctors. As a result, doctors who repackage medications prescribe more of those drugs and workers who receive repackaged drugs spend significantly more time off work.[24]

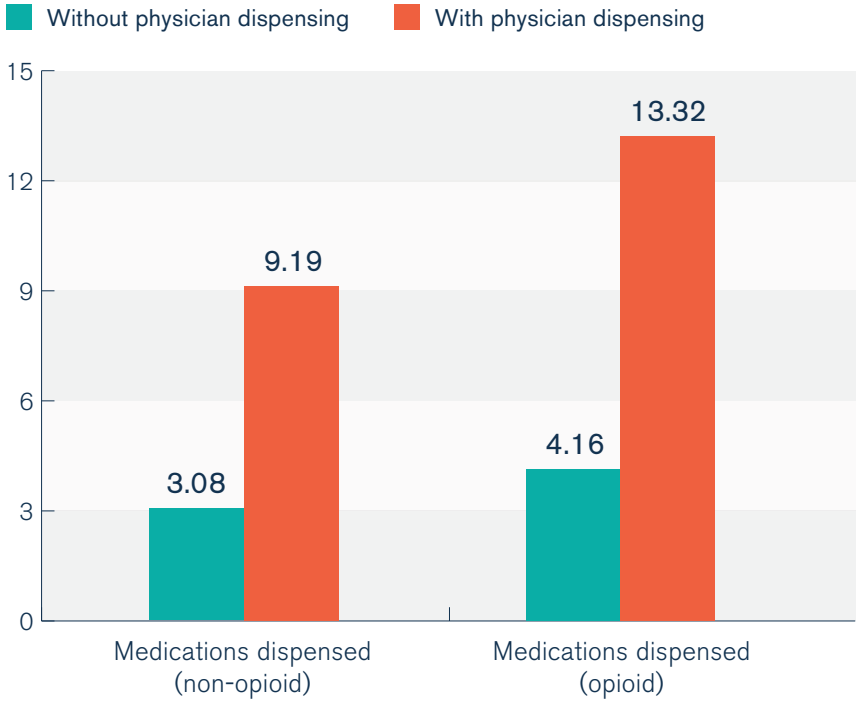
The 2011 reform bill sought to eliminate these mark-ups by imposing price controls.[25] Lawmakers prohibited doctors who repackage medicines from charging more than the average wholesale price of the drug plus a dispensing fee. While the law enjoyed some initial success it ultimately failed because lawmakers ignored the change in incentives for physicians. The New York Times reported that shortly after the law came into effect "doctors and companies have responded by exploiting loopholes in those rules and adopting new strategies to stay one step ahead."[26]

To avoid the rule, doctors began prescribing drugs in new doses. Because the different dose counts as a new drug, pharmaceutical companies were able to create new wholesale prices significantly higher than the prices charged by pharmacists for existing doses. For example, doctors used to prescribe one common muscle relaxant in 5- or 10-milligram doses. Now doctors prescribe the same drug in 7.5-milligram doses, but charge five times more than a pharmacist would charge for the 5- or 10-milligram dose.

Advocates for repackaging argue that it provides workers with greater convenience, but the practice also creates a conflict of interest between doctors and patients. Researchers at Johns Hopkins University found that when physicians are paid to dispense drugs they prescribe those drugs in greater quantities and workers spend more time recovering.[27] The problem is most acute when doctors prescribe opioids, a class of painkiller that includes morphine and heroin.[28] The researchers found that when physicians repackaged drugs they prescribed three times the number of medications per patient. With opioid dispensing, doctors prescribed 3.2 times as many medications as when doctors don't dispense.

Number of medications prescribed per workers' compensation patient

Average number of medications per patient prescribed by doctors with and without physician dispensing



Source: Jeffrey A. White, et al., "Effect of Physician-Dispensed Medication on Workers' Compensation Claim Outcomes in the State of Illinois," Journal of Occupational and Environmental Medicine 56.5 (2014): 459-464

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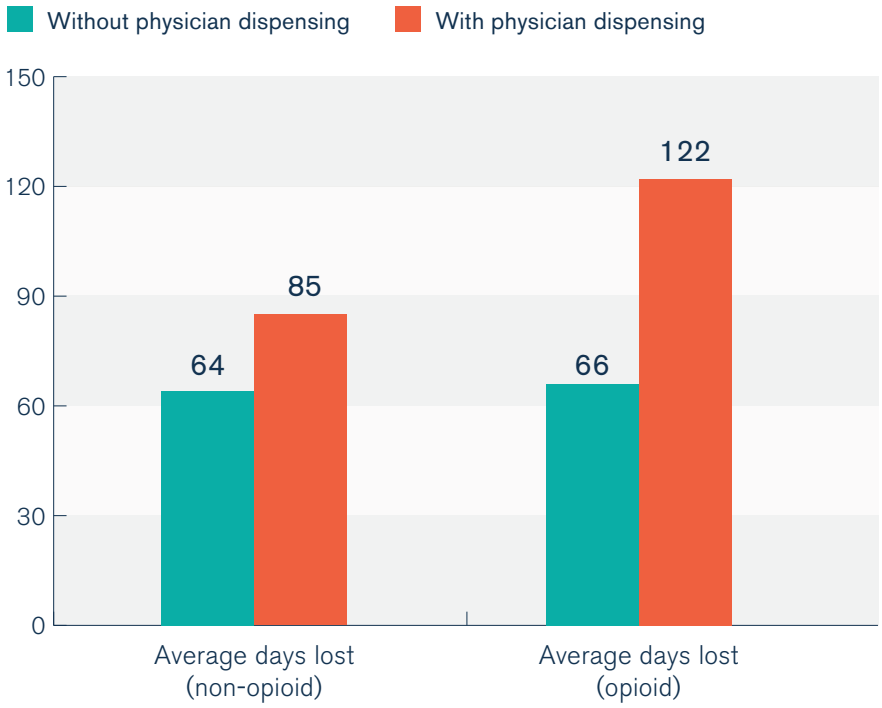
When there is a financial incentive to prescribe drugs there is an incentive to prolong treatment and keep workers off the job. But overprescribing as other costs for employers, and potentially serious health consequences for patients. Overprescribing can cause workers to miss more time from work — time during which their skill sets can erode. This has an obvious cost to the business, but also is a long-term cost to workers. Workers who are off the job for unnecessarily long periods of time face longer-term challenges in maintaining their skills. And when they are off work because their medications are overprescribed, they face the risks associated with the use of strong prescription drugs, such as addiction.

In cases when physicians prescribe medications, workers spend significantly longer time periods off the job.

Days of work lost per workers' compensation patient
Average number of days lost per worker with and without physician dispensing



Source: Jeffrey A. White, et al., "Effect of Physician-Dispensed Medication on Workers' Compensation Claim Outcomes in the State of Illinois," Journal of Occupational and Environmental Medicine 56.5 (2014): 459-464

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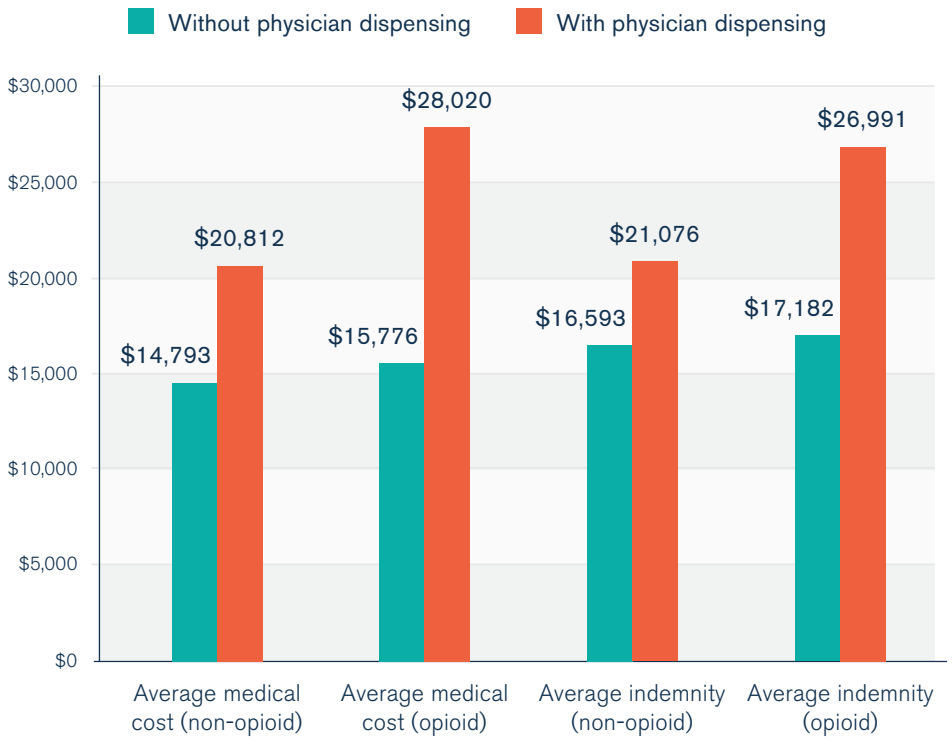
As a consequence of both higher prices and the higher rate of prescription, repackaged drugs account for half of all medication costs in the workers' compensation system.[29] When doctors have a financial incentive to prescribe drugs they have an incentive to prolong treatment. Researchers found that overall medical costs increase by 78 percent when the worker receives repackaged opioids.[30] Workers also spend nearly twice as long away from work. Indemnity payments, which reimburse workers for costs of sickness such as lost wages, increase by 57 percent.[31] Overall the average direct cost to business increases by 64 percent, or $22,092.[32]

Cost of physicians dispensing medication to workers' compensation patients
Average total cost per injured worker with and without physician dispensing



Source: Jeffrey A. White, et al., "Effect of Physician-Dispensed Medication on Workers' Compensation Claim Outcomes in the State of Illinois," Journal of Occupational and Environmental Medicine 56.5 (2014): 459-464

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Even this measurement may be an understatement of total cost because employers face additional costs when an employee is absent for a prolonged period. But there are also significant costs to the employee. The National Survey on Drug Use and Health found that prescription drug abuse is the fastest-growing form of drug abuse in America.[33] Opioid overdoses, once almost always a result of heroin abuse, are now increasingly the result of prescription opioid abuse, and a White House report described prescription drug abuse as an "epidemic."[34] Over-prescription in the workers' compensation system is not only a cost issue but also a public health issue.

Opioids are an important tool in treating pain and at least one study argues that the benefits of improved pain treatment outweigh the costs of addiction,[35] but when opioid abuse stems from unnecessary prescriptions, patients suffer the costs without receiving the benefits. Studies by both the WCRI and Johns Hopkins have both reached the conclusion that the higher levels of opioid prescriptions under workers' compensation are due to incentives and not medical need.[36]

The federal Centers for Disease Control found that a package of reforms in Florida, including a prohibition on physician dispensing of strong opioids, significantly reduced opioid abuse and overdose deaths in the state.[37] Although the Florida law did not prohibit physicians from prescribing strong opioids — it eliminated only the financial incentive to do so — physicians significantly reduced prescriptions of those drugs. The outcome drove WCRI's conclusion that the higher rates of prescribing were financially motivated and not driven by patient needs.[38]

While the 2011 Illinois reform recognized the importance of reforming physician dispensing, the reforms failed to address the underlying incentives. Employers have no ability to control costs while patients have no incentive to do so and lack the information to know when the doctor is acting against their best interest. When government sets the terms for buying services on behalf of others (whether workers and businesses or taxpayers) it has a responsibility to obtain the best possible deal, which may mean refusing to compensate doctors for repackaged drugs absent exceptional circumstances.

3. Introduction of Preferred Provider Networks

Managing a system as complex as workers' compensation can be tedious and bureaucratic, and imposes a one-size-fits-all approach on a range of workplaces. Allowing insurers more control over costs may provide a more nuanced approach to cost reduction than a simple fee schedule or prohibition on repackaging. Preferred Provider Networks, or PPNs, allow insurers to privately negotiate prices with in-network medical providers. Beyond simply negotiating lower fees, PPNs can accomplish savings by cutting the costs of bureaucracy.

Furthermore, without a PPN an injured worker must wait for a medical claim to be approved. The 2011 reform provides that the worker cannot be billed for medical procedures that a tribunal deems unnecessary, but this leaves the medical provider bearing the risk that a treatment will not be approved. PPNs guarantee payment for in-network treatment, adding certainty for employees and providers and also reducing costs. By keeping bureaucratic costs below those of the workers' compensation system and also giving medical providers certainty, PPNs can negotiate better rates without compromising service.

Although PPNs are able to obtain better rates, evidence suggests that for doctors' visits networks frequently negotiate fees above those set by the legislature. Several reasons for this are possible. As previously noted, unlike surgeries, the rates for doctors in Illinois never exceeded those in surrounding states by much and are now lower. Many economists, and the White House, have noted that health coverage including workers' compensation is part of an employee's overall compensation package.[39] Employers who reduce the quality of health coverage will have more difficulty recruiting and retaining good employees unless they pay employees higher wages. If it is cheaper to provide better health insurance than either pay more or lose good employees, then employers have a financial incentive to do so. But by the same measure, employees also suffer when employers are forced to provide benefits the employees do not value.

PPNs also have a financial incentive to recruit higher-quality doctors who are less likely to inflate costs by overtreating patients and can return employees to health more quickly. Doctors have a financial incentive to keep employees off work for longer and while the majority of employees would prefer a speedy recovery, a minority may seek to prolong their absence from work. Paying doctors more does not automatically lead to high quality: Simply raising the fee schedule would not guarantee better doctors. But when the PPN can choose which doctors to allow into its network, offering higher fees gives the PPN the ability to recruit better doctors and the freedom to reject lower-quality doctors.

Illinois employers have always been free to make arrangements with providers but employees have no obligation to use the employer-designated medical provider.[40] While most employees may want to recover and be able to return to work as soon as possible, some will prefer to shop for doctors willing to extend treatment and permit a longer employee absence from the workplace. If those employees opt out, even if the majority of employers prefer to use the in-network doctor, then the employer loses out on cost savings and it may no longer make financial sense to create a PPN.

The 2011 reform did not grant employers total control over injury claims, but it did moderate the ability of workers to opt out.[41] Illinois law provides workers with up to two choices of doctor, not

including any referral from the initial doctor.[42] This is designed to limit the ability of patients to look for a doctor who will follow the treatment path desired by the worker rather than follow best medical practices. That may include allowing a longer work absence or prescribing specific controlled substances. Under the 2011 reform the existence of a PPN counts as the workers' first choice.[43] Workers can still opt out, but if their employer has a PPN they can choose only one alternative doctor.[44]

Controlling costs is good for employers but also for the majority of workers who want high-quality doctors who will provide for a speedy recovery and to return to work as soon as possible. By the same measure, those employees lose out when opt-outs eliminate the cost savings from adopting PPNs and make it less likely that the employer will adopt a plan. While the 2011 reform increased the incentives for employers to create a PPN, insurance industry experts remain skeptical that the plan will deliver the same benefits as in other states because employees can still opt out. The law also requires that all plans be approved by the insurance commissioner, who has the power to reject any plan that does not provide for every medical eventuality.[45] That provision may make it difficult for insurers to get plans approved in much of the state and limit the effectiveness of the reform.

4. Alternative dispute resolution

Preferred provider networks can allow a more nuanced approach to cost reduction by giving employers freedom to develop a medical insurance package better suited to the needs of an individual workforce. Similarly, alternative dispute resolution potentially may improve employee welfare by developing more effective means to settle disputes over payment of benefits.[46]

Alternative dispute resolution means an alternative to the workers' compensation system of arbitrators and tribunals. While originally designed to be more efficient than a trial court, the workers' compensation arbitration system has evolved to serve the interest of trial lawyers at the expense of both worker and employer. The current system is slow and bureaucratic, not only imposing additional administrative costs on employers but also preventing workers from seeing legitimate claims processed in a timely manner. Just 38.2 percent of all claims are settled within the statutory limit of 14 days, during which time workers are left without income.[47]

The 2011 reform bill trialed a very limited version of alternative dispute resolution, known as collectively bargained workers' compensation. In a pilot scheme for the construction industry, the rules of workers compensation, including benefit levels, remain intact but employers and unions were allowed to agree to arbitrate claims outside of the workers' compensation system. Agreement is possible because both workers and employers have an incentive to eliminate unnecessary costs associated with inefficient bureaucracy: Employers save money and employees see their claims settled more quickly.

The collectively bargained approach may help reduce costs and delays for affected businesses but lawmakers should exercise caution in providing regulatory benefits to specific industries or groups over others. Competition can suffer when a fraction of businesses in an industry retain a benefit not available to others. Furthermore, smaller and minority-owned businesses are less likely to be unionized and would be ineligible for the benefit. Nevertheless, the pilot scheme deserves further attention and might be expanded as part of a comprehensive set of reforms toward alternative dispute resolution.

5. Payment caps for carpal tunnel syndrome

Reforms to repackaging, fee schedules, and even broader reforms such as the expansion of PPNs and alternative dispute resolution address some of the costs of treating injury but do not address the changing nature of injury in the workplace. This can leave employers responsible for injuries incurred away from the worksite.

The workers' compensation system was designed to treat industrial accidents such as a worker who loses an arm while operating a machine. These injuries, while not necessarily due to any negligence on the employer's part, can be clearly traced to a specific time and place. More importantly, the employer has the ability to reduce costs by improving workplace safety. Since the introduction of the workers' compensation system, the shift from manufacturing to services and improvements in safety have reduced the number of industrial accidents. At the same time, occupational diseases have become an increasingly important cost component of workers' compensation.

Unlike industrial accidents, occupational diseases are not accidents that occur at a specific time or place. They are injuries or diseases such as repetitive strain injuries or carpal tunnel syndrome that may manifest only over long periods of time. For an injury to qualify as an occupational disease, the harm should primarily emerge in the workplace, although the long gestation period sometimes makes it hard to determine all the factors involved. Furthermore, the disease may arise over many years of employment with different employers.

The workers' compensation system was designed to handle accidents, and was expanded to handle occupational diseases in the 1970s when workers were more likely to have a single employer across their career. Consequently, the system assigns full liability to the employer at the time the injury or disease manifests. Thus a small start-up business may find that a new hire has an injury, incurred over decades of performing the same duties, manifest at the beginning of his or her employment. Although the employer played little to no part in contributing to that injury that business is then responsible for the entire cost of not only treating the injury but also disability payments for the remainder of the employee's working life.

The 2011 reforms did not address the broader issue of responsibility for injury. Instead lawmakers capped payments for carpal tunnel syndrome; a common occupational disease that causes numbness or tingling in the hand.[48] While this did mitigate the problem, lawmakers avoided the broader question of how to address occupational diseases and, more importantly, did not make progress toward a system capable of handling the rapidly evolving nature of work and workplace injury.

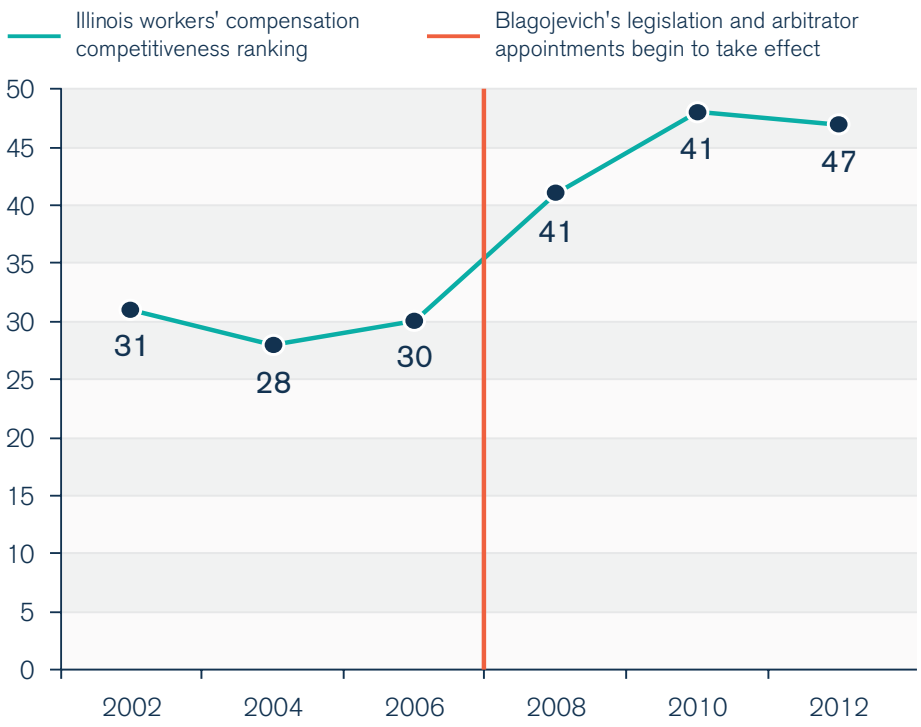
Solutions for Illinois' workers' compensation system

Fixing Blagojevich's 2005 workers' compensation law

The stated intention of Blagojevich's 2005 workers' compensation law was to make Illinois more competitive for jobs and new businesses. The law had the opposite effect. According to a study by the state of Oregon, Illinois ranked as the 31st-most competitive state for workers' compensation costs in 2002, the 28th-most-competitive in 2004, and the 30th-most-competitive in January 2006, before Blagojevich's legislation had begun to affect system costs. In other words, Illinois was slightly worse than middle of the pack in the years before the 2005 reforms started taking effect.

When the 2005 reforms took effect, Illinois' competitiveness plummeted, and the 2008 state of Oregon rankings showed Illinois as the 41st-most-competitive state. By 2010, Illinois' rank had dropped to No. 48 of the 50 states, plus the District of Columbia, and in 2012, Illinois hovered at the No. 47 spot in the competitiveness rankings.[49]

Illinois became dramatically less competitive after Gov. Rod Blagojevich's appointments and 2005 workers' compensation legislation
Illinois' national competitive ranking by year according to state of Oregon workers' compensation study



Source: State of Oregon workers' compensation premium-rate rankings summaries **@illinoispolicy**

What happened that made Illinois become so much less competitive so quickly? The answer to that question is made up of three components, all of which the current governor and General Assembly can address through executive action and legislative reforms.

1. Litigator-friendly arbitrators. Blagojevich appointed arbitrators and other workers' compensation officials who would make decisions influencing workers' compensation claims. An ally of the Illinois trial bar, Blagojevich had strong political connections to trial lawyers who wanted their friends deciding workers' compensation claims. A system staffed by trial lawyers will naturally result in litigator-friendly results that drive costs for employers. Gov. Bruce Rauner can fix this problem by appointing new arbitrators, and as of this writing, the process of cleaning house is under way.

2. Unfriendly courts. The Illinois Chamber of Commerce described a second factor in the costliness of Illinois' workers' compensation system in a research report, "The Impact of Judicial Activism in Illinois," which presents workers' compensation judicial rulings from an employer's perspective.[50] The report details some scarcely believable judicial rulings in workers' compensation cases, such as the following:[51]

• A worker who received compensation as a traveling employee when she slipped and fell on the ice in her own driveway (2013)

• A worker who received compensation as a traveling employee for injuries in a car accident in which he had used a company car to travel home after running a personal errand (2010)

• A worker who received compensation after injuring his shoulder while ramming it against a

vending machine in order to shake loose a bag of chips for a co-worker. This worker was covered under a so-called Good Samaritan concept, because he was trying to do a good deed for his friend. (2009)

A number of the problems implied by these rulings, such as the need to narrow the definitions of "causation" and "traveling employee," are addressed in Rauner's workers' compensation reform legislation, covered in another section of this report.

3. Cost drivers within the 2005 bill. A third factor, which the General Assembly should address through new legislation, are provisions of the 2005 reform legislation itself, which directly caused an increase to several cost drivers in the workers' compensation system. Here are some examples of those cost drivers and potential fixes for them:

• The 2005 bill instituted an approximately 7.5 percent across-the-board increase in indemnity payments for "permanent partial disability" injuries, measured by the number of weeks of wages that would be awarded. For example, an award for a thumb injury was increased to 76 weeks from 70 weeks of wages. The General Assembly can undo the cost-increasing effects of the 2005 legislation by simply rolling back the number of weeks of wages awarded in indemnity payments to pre-2005 levels.

• The 2005 bill raised the maximum award for certain injuries to the greater of 25 years of wages or $500,000 from the greater of 20 years of wages or $250,000. Lawmakers can change this maximum award to a more moderate amount such as the greater of 20 years of wages or $400,000, which would still constitute an increase in benefits from pre-2005 levels.

• Finally, the 2005 bill mandated that when workers who earn below certain lower wage thresholds are injured on the job, 100 percent of their lost wages must be replaced, untaxed. This equals an effective pay hike for these workers, many of whom are part-time employees, which creates a disincentive for these workers to return to work.

In general, across the workers' compensation system, injured workers have two-thirds of their lost wages replaced, untaxed. However, for workers who earn less than $220 to $330 per week,[52] depending on their number of dependents, all lost wages are replaced, tax-free. When an injured worker receives more take-home pay by staying home, this creates a strong disincentive to return to work. This also drives up the cost of any indemnity settlements and lost wage replacements that are based on these minimum replacement rates.

Revising minimum wage replacements

One option for reform on minimum wage replacements would be to split the difference between what the majority of workers receive (two-thirds of lost wages, untaxed) and what these lower-wage workers currently receive (100 percent of lost wages, untaxed). That would provide protection for lower-wage earners while preventing workers from achieving an after-tax pay hike by being on workers' compensation. For example, workers who fall into the current lower-wage categories could receive five-sixths of their lost wages, untaxed. This would still provide a cushion to protect lower-wage workers while removing the effective pay hike that current law gives these workers for staying home from work. Alternatively, the ratio can be made two-thirds of lost wages untaxed for all injured workers regardless of wage levels, up to a certain maximum.

Compared to surrounding states, Illinois' minimum wage replacements for total temporary disability are quite high as a percent of each state's average weekly wage.

Blagojevich's 2005 law put Illinois' minimum wage-replacement ratios out of line with surrounding states

State average weekly wage, or SAWW, minimum wage-replacement ratio, and minimum wage-replacement ratio as a percent of SAWW, by state

State	SAWW	Minimum wage replacement	Minimum wage-replacement rate as a percent of SAWW
Illinois	**$1,048.67**	**$220-330**	**21-31%**
Indiana	$736.67	$75.00	10.18%
Iowa	$813.99	$285.00	35%
Kansas	$813.98	$25.00	3%
Kentucky	$798.63	$159.72	20%
Michigan	$935.00	$0.00	0%
Minnesota	$989.00	$130.00	13%
Missouri	$844.69	$40.00	5%
Nebraska	$785.00	$49.00	6%
Ohio	$885.00	$295.00	33%
Wisconsin	$936.00	$0.00	0%

Source: State laws and state regulatory agencies

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Revising disability, maximum wage-replacement rates and other cost drivers

Other related cost drivers were not a part of the 2005 legislation but similarly put Illinois out of line with other states. In addition to Illinois' high minimum payout rates for total temporary disability, or TTD, Illinois has high rates for permanent partial disability, or PPD, and for permanent total disability, or PTD, along with high caps on maximum payouts for TTD, PTD and PPD.

Illinois' payout rates for TTD are $220 to $330 for the minimum and nearly $1,400 for the maximum. As a percent of the state's average weekly wage, Illinois' minimum wage-replacement rates are 21 to 31 percent; and Illinois' maximum wage-replacement rate is 133 percent of the state's average weekly wage. These minimum and maximum wage-replacement rates put Illinois out of line with surrounding states where the average minimum replacement rate is about 12 percent of the state's average weekly wage, and the average maximum wage-replacement rate is 117 percent of the state's average weekly wage. It's worth noting that although Indiana and Iowa have higher ratios on their wage-replacement rates, those ratios are taken as a percentage of each state's average weekly wage, which seems to be calculated as artificially lower in those states than in Illinois.

Minimum and maximum wage-replacement ratios in Illinois are out of line with surrounding states for total temporary disability

State average weekly wage, or SAWW, minimum and maximum wage-replacement ratios, and minimum and maximum wage-replacement ratios as a percent of SAWW, by state

State	SAWW	Minimum wage replacement	Minimum wage-replacement rate as a percent of SAWW	Maximum wage replacement	Maximum wage replacement as a percent of SAWW
Illinois	**$1,048.67**	**$220-330**	**21-31%**	**$1,398.23**	**133%**
Indiana	$736.67	$75.00	10.18%	$1,105.00	150%
Iowa	$813.99	$285.00	35%	$1,628.00	200%
Kansas	$813.98	$25.00	3%	$610.00	75%
Kentucky	$798.63	$159.72	20%	$798.63	100%
Michigan	$935.00	$0.00	0%	$842.00	90%
Minnesota	$989.00	$130.00	13%	$1,008.78	102%
Missouri	$844.69	$40.00	5%	$886.92	105%
Nebraska	$785.00	$49.00	6%	$785.00	100%
Ohio	$885.00	$295.00	33%	$885.00	100%
Wisconsin	$936.00	$0.00	0%	$1,404.00	150%

Source: State laws and state regulatory agencies **@illinoispolicy**

A similar comparison applies between Illinois and surrounding states for injuries that fall into the categories of PTD and PPD. The minimum wage-replacement rate in Illinois is 50 percent of the state's average weekly wage, making Illinois the highest of surrounding states. The maximum is 133 percent of the state's average weekly wage, once again making Illinois higher than the average of surrounding states. The chart below reflects the replacement ratios of PTD which is largely the same as the replacement ratios for PPD.

Minimum and maximum wage-replacement ratios in Illinois are out of line with surrounding states for permanent total disability

State average weekly wage, or SAWW, minimum and maximum wage-replacement ratios, and minimum and maximum wage-replacement ratios as a percent of SAWW, by state

State	SAWW	Minimum	Minimum as a percent of SAWW	Maximum	Maximum as a percent of SAWW
Illinois	**$1,048.67**	**$524.34**	**50%**	**$1,398.23**	**133%**
Indiana	$736.67	$75.00	10.18%	$1,105.00	150%
Iowa	$813.99	$285.00	35%	$1,628.00	200%
Kansas	$813.98	$25.00	3%	$610.00	75%
Kentucky	$798.63	$159.72	20%	$798.63	100%
Michigan	$935.00	$0.00	0%	$842.00	90%
Minnesota	$989.00	$130.00	13%	$1,008.78	102%
Missouri	$844.69	$40.00	5%	$886.92	105%
Nebraska	$785.00	$49.00	6%	$785.00	100%
Ohio	$885.00	$442.50	50%	$885.00	100%
Wisconsin	$936.00	$0.00	0%	$1,404.00	150%

Source: State laws and state regulatory agencies **@illinoispolicy**

A reform for maximum wage-replacement rates would be to cap them at 100 percent of Illinois' state average weekly wage rather than 133 percent, which would put Illinois in line with what most surrounding states do. Illinois' minimum wage-replacement rates for PTD and PPD are also out of line with surrounding states at 50 percent of the state average weekly wage compared to an average of 14 percent in surrounding states.

Reviewing how Illinois calculates 'average weekly wage'

Also worth investigating is the manner in which Illinois' average weekly wage is calculated. Since 1979, there is only one year-long period during which Illinois' average weekly wage is recorded to have dropped, which was a drop of 1.1 percent from June 29, 2008, to July 1, 2009, according to the Illinois' Department of Employment Security.

Many of the legislative changes suggested in this section to address the cost drivers in the 2005 law are contained in House Bill 5754,[53] filed by state Rep. Keith Wheeler.

Blagojevich's 2005 workers' compensation legislation and the Blagojevich administration's policies in general put Illinois businesses and manufacturers at a disadvantage by driving workers' compensation costs to unsustainably high rates. Policymakers should repeal the mistakes made by the Blagojevich administration, particularly those in the 2005 law, to put Illinois' system back on a level footing.

Fixing physician dispensing

Repackaged drugs remain a major cost driver in workers' compensation: as much as half of all the costs of medication in the system. More importantly, the bad incentives created by repackaging are responsible for increasing the amount of time employees spend off work and may contribute to prescription opioid abuse. As long as doctors have incentives to prescribe more drugs they are likely to do so — at a cost to both workers and employers.

Setting price controls is unlikely to be effective. New drugs hit the market at a rapid pace, and government may respond slowly in approving prices for all new drugs. And relying on wholesale price has been shown as open to abuse. Other states have prohibited altogether reimbursements for repackaged drugs under workers' compensation, limited reimbursements to immediate pain treatment, or restricted the practice to rural areas where pharmacies might be hard to reach.

While this approach may appear interventionist, the government is not acting as a regulator but as a purchaser of services. In the workers' compensation system doctors are free to refuse to treat workers' compensation patients if they so choose, but employers have no choice but to compensate doctors at the charged rate. In this case it is the state's responsibility to negotiate for the best fee for service on behalf of employers and workers. Private insurers behave in the same way and often go further in negotiating not only fees and conditions for service but also deciding which doctors may participate in the network. It is entirely within governments' responsibility to taxpayers and workers to refuse to include repackaged drugs within workers' compensation when there is clear evidence that the practice is harmful.

A bill currently before the Illinois General Assembly would restrict physician dispensing. HB 5751 proposes to restrict physician dispensing to rural areas where there is no easily accessible pharmacist (defined as a pharmacist within 5 miles of the physician's office). The reform also would restrict dispensing to a 72-hour supply from the date of the accident, or 24 hours from the initial visit, whichever is longer. The bill would apply only to reimbursements under the workers' compensation system, and would allow PPNs to negotiate privately an alternative agreement.

The Rauner reform proposals

As part of his Turnaround Agenda, Rauner has proposed a series of reforms designed to reduce the cost of workers' compensation to make Illinois more competitive for business.[54] Rauner's reforms are explored below.

Reform of causation

At present the law requires that workers' compensation should cover any injury "arising out of and in the course of employment."[55] That idea arises out of the original founding principle of strict liability in a no-fault system, which holds the employer responsible for the costs of a workplace injury whether or not the employer is negligent in causing the injury. However, that principle assumes the employer has some control over the circumstances leading to an accident. Thus an accident may be preventable even if it is not the result of negligence. But as the system has evolved to handle a wider range of conditions such as occupational diseases,[56] any aggravation of an existing condition becomes a workers' compensation claim making the employer liable even when the employer has no control over the circumstances.

Today, the majority of states operate under a higher standard of causation such as requiring the workplace accident be the primary cause. The governor proposes that the standard in Illinois be raised from "any cause" to "a major contributing cause," meaning that the accident at work must be more than 50 percent responsible for the injury. That standard is consistent with many other states and is similar to some common tort principles.[57] Furthermore, the reform could be reasonably expected to reduce the costs of workers' compensation while keeping intact the founding principle of strict liability. However, policymakers should be careful to ensure that the more complex standard does not lead to increased litigation costs, which may reduce or eliminate the potential cost savings without providing similar benefits to workers.

Adopt AMA guidelines

As part of the 2011 reforms, lawmakers mandated that commissioners use the guidelines of the American Medical Association, or AMA, as one of five factors when determining the amount of awards for permanent partial disability.[58] Unlike some other states, including Indiana, Illinois does not make use of AMA guidelines mandatory. Evidence suggests that arbitrators make higher awards when they apply other factors.

The governor proposes extending the 2011 reform to make AMA guidelines mandatory and exclusive in determining the amount of rewards. The governor also proposes allowing commissioners the power to consider the opinion of an independent medical examiner alongside the records of the treating physician. Both measures would be likely to reduce overall costs.

Reforming traveling-employee policies

At present the law treats injuries as "arising out of and in the course of employment." In a now-overturned decision, the Illinois Appellate Court ruled that this should include an employee who slipped while traveling to work. The governor has proposed clarifying the law such that "traveling employees" are eligible for workers' compensation only if the travel was necessary for their job and was paid for by the company. It is unclear how much the proposed change would reduce costs following the reversal of the Appellate Court's decision by the Supreme Court.

Fee schedule reduction

As discussed above,[59] the fee schedule in Illinois significantly exceeds fees for Medicare and fee

schedules in other states for some surgeries. The governor proposes reducing fees 30 percent across the board with an exception for doctors visits, which are currently below average fees for group health. Evidence from past fee reductions suggests that medical providers will tend to recoup some of the lost revenue. The governor has claimed savings of 15 to 20 percent, which is below observed savings of 24 percent from the 2011 fee reduction of the same magnitude.[60]

Additional avenues for reform

The reforms described above are proposals to begin right-sizing Illinois' workers' compensation system. They are already in legislative form, as referenced throughout the solutions section. Below are additional reforms that legislators and policymakers should consider to further bring Illinois' costs and practices in line with other states.

Tying fee schedule to Medicare

Across the board fee cuts, like those enacted by the 2011 reform bill, may prove inadequate overall and could be excessive in some areas. The disparity between actual costs and the Illinois fee schedule exists because unlike most states, which tie their fee schedules to Medicare, Illinois' fee schedule is tied to billed charges. Those billed charges are not the actual fees paid but a sticker price that may be substantially higher than the fee insurance companies will reimburse. By contrast, Medicare rates more accurately reflect the negotiated market rate for treatments.

For some surgeries, Illinois' fee schedule is 200 to 300 percent higher than the price for the same surgeries under Medicare. Most states set fee schedules at a multiple of Medicare, allowing a slightly higher rate than Medicare to account for the increased administrative costs under workers' compensation. Illinois lawmakers could substantially reduce billed costs by simply replicating those laws and tying workers' compensation to Medicare rates for Illinois.

Reform treatment of occupational diseases

Most states added occupational diseases to their workers' compensation system during the 1970s. At the time, lawmakers might reasonably have anticipated that most of the workforce would have a single employer through their career. In this context coverage of occupational diseases made some sense. In a modern workplace the system imposes all the cost on whomever the employee works for at the time the disease manifests.

Rather than introduce a complex system of liability that may inflate legal costs without providing additional benefits to employers or workers, policymakers should look at more comprehensive solutions for removing occupational diseases from the workers' compensation system. Economic studies, as well as a White House report, have indicated that employers have to compensate employees more when workers face increased risk or frequency of injury. Instead of requiring employers to compensate employees for injuries out of the employers' control, lawmakers should consider allowing employers to contribute directly for their own share of cost through higher wages. Lawmakers may also consider hybrid measures such as employer contributions to savings accounts that follow the employee.

PPN reform

Even while there are substantial benefits to tying the fee schedule to a more representative cost list such as that provided by Medicare, private insurers may still be able to obtain lower overall costs. Private insurers not only set fee schedules but also can choose among medical providers. In many cases, this may involve paying above the fee schedule rate to secure better-quality doctors who will avoid unnecessary treatment and return employees to work more quickly at a lower overall cost.

Expanding access to PPNs not only reduces costs but benefits workers through potentially higher-quality health care and faster approval of medical expenses. Despite the 2011 reforms workers and employers may not receive the total benefits of PPNs because workers are still free to opt out. This not only reduces the ability of businesses to control costs but may discourage some employers from establishing PPNs. Eliminating the opt-out could reduce costs and benefit the majority of workers who value timely treatment.

Additionally lawmakers need to review the regulatory barriers to approving a new PPN. The interests of employers and workers are more closely aligned than the law recognizes, and increasing flexibility is likely to benefit both parties. While well-intentioned restrictions may be designed to prevent employers establishing PPNs that provide lower levels of benefits, they also raise the cost of establishing all PPNs and may prevent beneficial PPNs from being established. There is insufficient evidence to judge the total impact of these regulatory barriers, but lawmakers need to be aware of the trade-off and monitor those costs.

Local government cost-saving reforms

Local governments have a responsibility to their taxpayers to ensure that workers' compensation costs are appropriately managed. They can achieve this by vigorously defending themselves against claims and enacting other forms of cost savings. One step they can take is to make sure that they have access to a sufficient number of claims adjustors and workers' compensation defense attorneys to successfully defend against inappropriate claims. They can also utilize PPN networks to manage the cost of health care for injured government employees. Furthermore, local governments can create and institute more robust light-work programs so that injured workers who cannot return to their original work positions can instead return to employment in open positions that do not aggravate the original injuries. State and local lawmakers can consider ways to incentivize local governments to take advantage of these types of programs that will ultimately save taxpayers money.

In addition, an opt-out system as described below can be utilized by local governments as an alternative to Illinois' workers' compensation system.

Modernizing Illinois' workers' compensation system for the 21st Century

Illinois' workers' compensation system is one of the oldest workers' compensation systems in America, dating back to 1911.[61] Since then, the workplace has changed significantly. For example, a far smaller percentage of Americans are now employed in heavy industry, and an increasing percentage of the workforce now balances work with child or elder care.[62]

Although businesses have developed new solutions to these evolving challenges, such as telecommuting and flexible workdays, workers' compensation has not evolved at the same pace. And more Americans who work in the gig economy now find themselves forced into rigid classifications that treat workers as employees or independent contractors but allow for no in-between category. For these and many other Americans, workers' compensation has become an inflexible barrier to progress.

Impact of workers' compensation on innovation

More than 60 percent of households with children have either a single working parent or two

parents working.[63] Half of all people who provide unpaid care for an elder also work full time, and two-thirds have a job outside of their care responsibilities.[64] Telecommuting and flexible work hours are one way in which parents, or adults with elder care responsibilities, are able to balance work and home responsibilities.

The federal government has drastically expanded telecommuting, citing not only the benefits to parents but also the environmental benefits of reducing physical commuting.[65] But at the same time several major employers including Yahoo have eliminated their telecommuting programs.[66] While those employers gave no specific reason, and a combination of factors may have contributed to their decisions, some evidence suggests that the legal liabilities created by workers' compensation may be one factor employers consider.

When a professor slipped and fell on a pile of papers in his home office, a tribunal in California found that because the accident occurred during the course of work that he was eligible for workers' compensation, even though the university had provided him with his own office and had no control over the professor's home work environment.[67] Courts in Oregon found similarly for an interior designer who tripped over her dog while retrieving samples from her garage.[68]

Even when the law ultimately supports the employer it can create substantial risk. In Tennessee a woman was attacked by her neighbor while making lunch in her kitchen, but because she was telecommuting, and her employer had not designated a specific work area, the lower court found that her entire home was considered her workplace.[69] The decision was ultimately overturned by the state Supreme Court but only after extensive litigation. The case highlights the considerable ambiguity surrounding innovation in work practices and the need for "permissionless innovation."

These cases raise costs to employers and make them less likely to permit telecommuting, eliminating the environmental benefits from reduced commuting,[70] the benefits to other commuters from cutting congestion[71] and, most significantly, the benefits to working caregivers. Furthermore, when employers do permit telecommuting they are more likely to impose restrictions that curtail the total benefits. For example, legal experts advise employers to allow telecommuting only with formal arrangements that closely resemble the workers' compensation definition of a workplace by setting rigid working hours and limiting the employee's workspace to one room of their home.[72] But the definition under workers' compensation is based on early 20th-century industrial work that often fails to understand 21st-century work practices.

An employer who sets rigid rules for telecommuters cannot be held liable if the worker leaves the home before the end of the day to pick up his or her child from school, or slips while checking email late at night. But a more flexible work arrangement might be better for both the employee and the employer. The law's inflexible definition of a workplace is not rooted in modern work practices, and these restrictions impose an unnecessary burden on workers.

Illinois' workers' compensation imposes an additional burden on working parents because unlike many other states, there is no exception for domestic work. Families who wish to hire nannies or au pairs to watch their children or caregivers for their elderly relatives are still required to carry workers' compensation. If a family wants a live-in au pair or nurse, workers' compensation rules are designed around an industrial environment, such as an engineer who works on an oil rig. If a worker is injured in the middle of the night because an oil fire spreads to crew quarters it makes sense that employee is eligible for workers' compensation. But it makes less sense that a family providing free board to an au pair should be subjected to the same no-fault system.

While all workers can potentially be caregivers to children or adult relatives, evidence suggests that the burden falls most heavily on women, who have entered the workforce in substantial numbers since the introduction of workers' compensation. For this reason, the White House has recognized

that encouraging telecommuting and flexible work scheduling is one tool to facilitate increasing female participation in the workforce, not only by making it easier for women to balance work with other commitments but also by making it easier for men to take on greater domestic responsibilities.

Beyond the impact on incorporating telecommuting and flexible work scheduling into existing work practices, workers' compensation poses even more significant challenges for the increasing number of workers' in the "gig" economy. While estimates vary, it is possible that as many as 90 million Americans participate in the gig economy.[73] Yet the current system allows only for a worker to be either an employee or an independent contractor, with no in-between classification. For millions of Americans, that means that even if the platform company would prefer to provide some benefits, such as a flexible savings account to cover costs associated with injury, that company is prohibited from doing so.

Avenues for reform

The workers' compensation system continues to be important for many workers, especially in the construction and manufacturing industries, or in other hazardous workplaces where the risk of accident remains relatively high. Those workers can benefit greatly from reforming the current system but keeping intact the founding principles. But those workers comprise an increasingly small segment of the American labor force.

There are more radical approaches to reforming the system that may better cope with changes in the workplace, such as exempting telecommuters, domestic employees, and small businesses, which require greater flexibility. But even these changes are reactive. Telecommuting has existed as a problem to workers' compensation for more than two decades without spurring reform. The 21st century requires a system that can be as dynamic and innovative as the rest of the economy: In other words, it should allow for "permissionless innovation."

That means workers and businesses need greater freedom to reshape the workers' compensation system around new technologies and working practices without having to wait for government to develop a legal framework first. The 19th-century concept of a "company town," once common, is now rare. Employees have more choice, can more easily move between jobs and are more responsive to the quality of benefits offered than may have been possible before. While imperfect, workers' and employers' interests can still be better aligned than the inflexible work contract imagined by the law. The modern system needs then to incorporate greater worker choice at the expense of rigid regulation.

Instead of defining in detail the rules that determine how workplace injury is treated, the state should set the broad rules of the game and let workers and businesses determine the details based on industry specifics and even on the individual worker's circumstance. In a forthcoming report, the Illinois Policy Institute will lay out a path for redesigning workers' compensation for the 21st-century workplace.

Conclusion

True workers' compensation reform could create a win-win for workers, businesses, taxpayers and policymakers. Substantial reforms, such as a combination of those described in this report, would result in better job creation, lower government expenses and increased tax revenue as a result of more robust economic growth. Furthermore, the rights and protections for workers in legitimate workplace injuries easily would be protected within the context of overall reform.

First steps toward reform should be taken as soon as possible, and should include putting Illinois' wage-replacement ratios and medical costs in line with other states, removing the incentive for physicians to overprescribe powerful drugs, and clarifying key definitions such as that of a traveling employee. Furthermore, a number of additional reforms should be considered to help local governments be better stewards of taxpayer dollars.

As Illinois begins to take on substantive reforms, policymakers also should consider and develop policies that would make the system more compatible with a rapidly evolving 21st-century workplace. Such reforms, which would allow a kind of opt-out from the general system, will be explored in a future Illinois Policy Institute paper.

The economic impact of workers' compensation reform likely would measure in the billions of dollars per year for the private economy in Illinois, and probably would lead to hundreds of millions per year in savings for taxpayers. If Illinois lawmakers get this right, it would be a major step in the right direction for putting Illinois' economy and public budgets on a more sustainable course.

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