



CITY OF CHICAGO

DEPARTMENT OF FINANCE

Annual Report: Workers' Compensation

Issue date: September 30, 2022

The City of Chicago's Department of Finance ("DOF") is releasing its annual report on the civilian workers' compensation program ("Program") pursuant to Chapter 2-32, Article XIV of the Municipal Code of Chicago (2-32-1410 *et seq.*) This report summarizes Program activity during 2021.

Summary

The 2021 Annual Report summarizes key claim portfolio measures and discusses three key operational improvement initiatives: return-to-work, litigation management, and overall Program financial reserves.

The Program

A properly run workers' compensation program's performance is evaluated using a number of standard metrics, including those identified in Table 1 below.

Table 1: Summary of Key Measures, Calendar year data

| | 2017 | 2018 | 2019 | 2020 | 2021 |
|---------------------------------------|----------|----------|----------|----------|----------|
| New Claims | 1,434 | 1,284 | 1,175 | 861 | 1,014 |
| Closed Claims | 1,957 | 1,921 | 1,659 | 1,146 | 1,163 |
| Reopened Claims | 393 | 348 | 290 | 851 | 539 |
| Denied Claims+ | 303 | 352 | 260 | 73 | 95 |
| Open Inventory | 1,718 | 1,429 | 1,235 | 1,801 | 2,120 |
| Reserves on Open | \$346.4M | \$348.4M | \$312.5M | \$508.8M | \$532.8M |
| Total Paid | \$64.8M | \$61.8M | \$53.4M | \$58.1M | \$68.1M |
| Average Paid on Closed (at 12 months) | \$4,016 | \$4,509 | \$3,263 | \$2,352 | \$4,646 |
| Average Days to Close (at 12 months) | 146 | 144 | 119 | 76 | 84 |
| Average Paid on Closed (at 24 months) | \$11,969 | \$11,152 | \$5,984 | \$8,188 | n/a |
| Average Days to Close (at 24 months) | 270 | 250 | 155 | 142 | n/a |
| Total Claims with Payments Made | 3,112 | 2,988 | 2,913 | 3,158 | 3,546 |

*n/a denotes not available due to timing; 24-month data can only be reported 1 year in arrears.

+Beginning August 1, 2019, injuries reported with no medical treatment or lost time from work were converted to Electronic Incidents. Electronic Incidents do not have a compensability determination. This was a departure from the City's prior process of setting up every injury notice as a claim requiring a compensability determination. Therefore, the amount of claims considered for denial was reduced.

A cursory review of Table 1 above suggests year-over-year performance declined in four key areas between 2020 and 2021: new claims; open inventory; reserves on open; and total paid. However, further analysis and an understanding of key initiatives that were launched in 2021 show that was not the case.

For instance, the 18% year-over-year increase in new claims is explained by the COVID-19 pandemic, which temporarily suppressed 2020 new claim activity. (Fewer people at work during the pandemic resulted in fewer workplace injuries.) While claim activity increased in 2021 as employees returned to work fulltime, new claims continued to trend downward and were 13% below pre-pandemic levels (1,014 vs. 1,175). Open inventory, or the number of claims open at year's end, rose from 1,801 to 2,120 and were significantly above pre-pandemic levels (2,120 vs. 1,235). The multiyear increase in open inventory resulted from the on-going review of hundreds of claims the Committee on Finance ("COF") closed when it handled the Program. Many of these files were closed before COF satisfied its statutory payment obligations to injured workers. DOF had to reopen and review each claim in order to decide if they were properly closed. DOF's review is ongoing, and it expects the open inventory to decline in 2022 as this project concludes.

Reserves, which represent the ultimate probable cost of claims, increased by \$24M year-over-year and by \$220M from pre-pandemic levels. As discussed on page four, approximately \$20M of the \$24M year-over-year increase came from reopening the claims discussed above. The remaining \$4M increase came from new claim activity. The \$220M increase over pre-pandemic levels can be attributed to DOF's decision to jettison COF's reserving practices in favor of industry best practices, which call for estimating a claim's full value based on currently available information. Instead of following industry best practices, COF historically engaged in a practice known as "stair stepping," where reserves are raised incrementally to cover current payments. Stair-stepping is disfavored because it underreports a claim's value and can have adverse financial consequences when claims costs increase rapidly.

Total Paid in 2021 is another measure where the numbers do not tell the whole story. Spending on indemnity, medical and expenses increased by \$10M from 2020. This was driven primarily by two factors: (1) an increase in claim activity caused by employees returning to work; and (2) the launch of a new strategic initiative to resolve litigated claims. Spending on temporary total disability benefits for new claims increased by \$4.2M year-over-year, but still remained 14% below pre-COVID levels. DOF launched a strategic initiative in 2021 to resolve litigated claims. This initiative, which is discussed in more detail in the following section, increased spending by \$4M. However, DOF estimates that resolving these claims earlier in their lifecycle reduced its future spend by between \$1.8M and \$2.8M. DOF in partnership with Gallagher Bassett (GB) launched specific litigation management initiatives to drive down long-term claim costs. There were approximately 140 additional cases resolved in 2021 than the 2018-2020 (3 year) average of 305 per year. The increased activity was aimed at closing older claims and reducing future, ongoing costs to the City. This added \$4.0M of spending in 2021 but keeping these litigated claims open would have cost the City an estimated \$5.8-6.8M through increased future payments. These actions reduced the City's future expenditures by at least \$1.8M, or over 40% of what it otherwise would have paid.

Operational Improvement Initiatives

DOF launched several significant strategic initiatives in 2021 that will drive down long-term program costs by an estimated \$4.7M over the next one to three years. These initiatives are highlighted in greater detail below.

Lost Workdays

The length of time an injured worker is off work is one of the most important claim outcomes monitored. It not only drives significant indemnity expenses, but also affects physical and emotional well-being of the injured worker and the productivity of City Departments.

Average lost workdays improved from 183 days in 2018 to 149 days in 2021, **a 19% reduction**, and from 168 days in 2020 to 149 days in 2021, **an 11% improvement**. Reducing the average number of days employees were off work reduced the Program's indemnity exposure (i.e., lost wages) by an estimated \$2.9M.

These results were driven by claim practice improvements and enhancements to the return-to-work program. Claims handling practices were modernized and professionally administered by experienced financial managers dedicated to reducing costs. In April of 2021, DOF developed and launched a Transitional Duty Work Program. This program offers employees the opportunity to gradually transition back to work, allowing them the chance to work in a modified capacity based on their work restrictions. In the first 8 months of the Transitional Duty Work Program (through December 2021), employees who otherwise would have remained off work were successfully placed into positions that could accommodate their work restrictions.

Figure 11: Average Lost Workdays (on all Claims) by Year

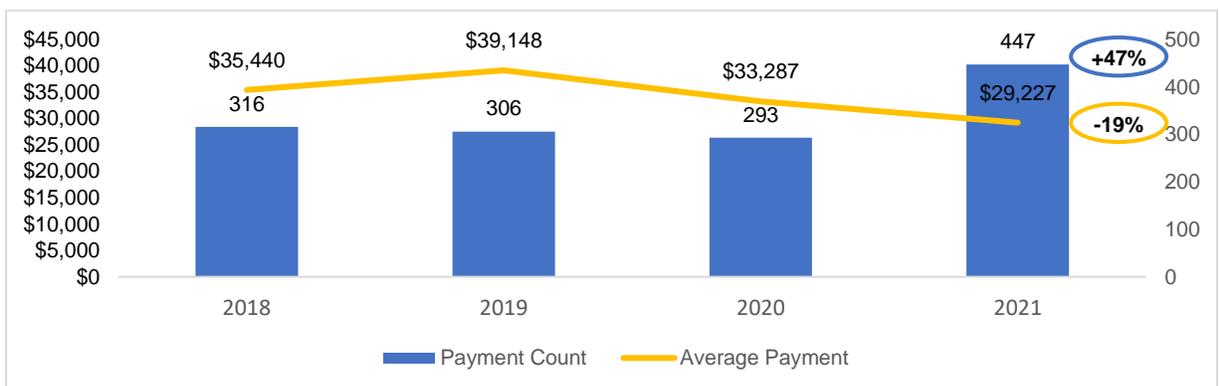


Claim Resolution

The majority of the City’s financial exposure comes from aged, litigated claims. DOF made a strategic decision in 2021 to address this backlog of approximately 1,500 claims in an attempt to reduce the City’s exposure. DOF actively sought to resolve its statutory obligations for claims rather than waiting for cases to go to trial. This resulted in a 47% increase in settlement activity compared to the 3-year average (447 claims settled in 2021 versus 3-year average of 305). Though activity increased, the average cost to resolve these claims decreased by 19% compared to the 3-year average (\$29,227 in 2021 versus 3-year average of \$35,958).

By taking these steps, the City reduced by an estimated 40% what it otherwise would have paid. Specifically, the \$4M in additional spending in 2021 is estimated to reduce the amount the City otherwise would have spent on these claims by \$1.8M to \$2.8M. It will take several years to resolve this backlog but doing so will meaningfully reduce the City’s financial exposure.

Figure 2: Settlement activity, showing the count of settlement payments by year and the average cost per payment

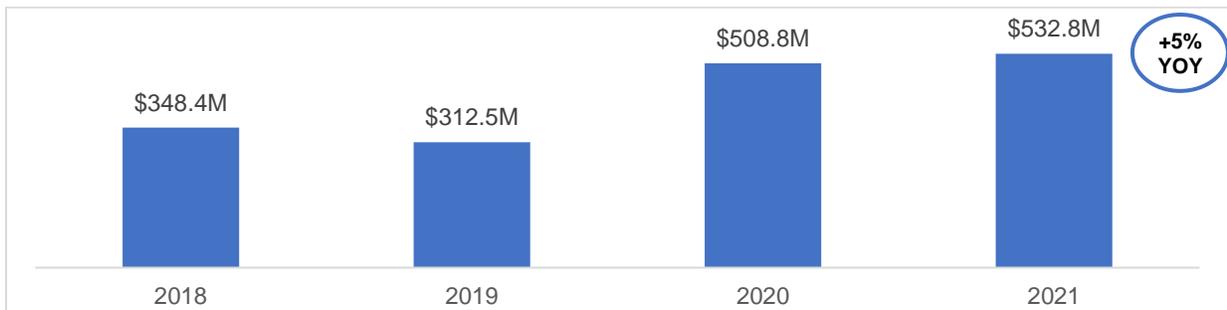


Financial Reserves

Reserves on open claims are an important financial measure that quantify the total financial exposure and represent the City's aggregate liabilities. DOF discovered during the Program's transition that COF did not follow industry standard practice for reserving claims, which calls for reserving a claim based on its ultimate probable cost. During the transition DOF and GB discovered that COF frequently raised reserves by small, incremental amounts to cover current payments only (i.e., stair stepping). This meant reserves were not adequate and did not reflect the City's aggregate liabilities. As a result of this discovery, DOF and GB reviewed all open claims and calculated reserves based on industry standard practice. As described in detail in the 2019/2020 report, this caused reserves to increase by nearly \$200M between 2019 and 2020.

In 2021, reserves increased by another \$24M, or 5%. Of the \$24M increase, \$19.9M came from re-opening the hundreds of claims that were prematurely closed, as described on page 2. DOF reopened all of these claims and established new reserves where necessary. These efforts are ongoing and by the end of 2022, DOF will be in a better position to report on the full scope of the City's liabilities.

Figure 3: Reserves on Open (Total Incurred) of the Civilian Program



Conclusion

2019 and 2020 were critical years for establishing governance, controls, and claim handling best practices. In 2021, DOF expanded its strategy and made significant progress in reducing lost workdays, returning employees to work more quickly and resolving open claims. These actions resulted reduced future spending by \$4.7M. DOF will continue to build upon these improvements going forward.

Appendix – Glossary of Key Terms

- New Claims: Claims setup within the period
- Closed Claims: Number of claims where the status changed from open to closed during the period
- Reopened Claims: Number of claims previously closed, that were re-opened within the period
- Open Inventory: Number of claims with a status of open at the end of the period
- Total Paid: Total amount paid in the period for all categories of spending (indemnity, medical, and expense) during the period. Includes all accident dates. Cash basis.
- Reserves on Open (Total Incurred): The total expected financial exposure for claims open at the end of the period
- Lost Workdays: The number of days an injured worker received temporary total disability payments