



## **Navigating Workers' Compensation: Self-Insured Group vs. Guaranteed Cost**

### **Introduction**

Workers' compensation insurance is a critical component of risk management for any business. It provides essential medical care and wage replacement for employees injured on the job, while also protecting employers from costly lawsuits. However, businesses often face a crucial decision when selecting their workers' compensation program: should they opt for a traditional "Guaranteed Cost" policy, or explore the alternative of a "Self-Insured Group" (SIG)?

This whitepaper will delve into both approaches, outlining their fundamental structures, advantages, disadvantages, and ideal scenarios, to help businesses make an informed decision that aligns with their financial capacity, risk tolerance, and operational goals.

### **Guaranteed Cost Workers' Compensation: Predictability and Simplicity**

Guaranteed Cost workers' compensation is the most common and straightforward type of policy. Under this model, an employer pays a fixed premium to an insurance carrier for a defined policy period, typically one year. In exchange, the insurance carrier assumes all financial responsibility for any workers' compensation claims that arise during that period, regardless of their frequency or severity.

#### **How it Works:**

- **Fixed Premium:** The premium is calculated based on factors such as payroll, employee classifications, industry risk, and the employer's experience modification factor (e-mod). Once set, this premium generally remains stable for the policy term.
- **Risk Transfer:** The primary benefit is the complete transfer of financial risk to the insurance carrier. The employer knows their maximum cost upfront.
- **Administrative Ease:** The insurance carrier handles all aspects of claims management, including investigations, medical bill payments, and legal defense, significantly reducing the administrative burden on the employer.

#### **Advantages of Guaranteed Cost:**

- **Predictable Budgeting:** Fixed premiums allow for clear and consistent



budgeting, eliminating unexpected costs due to large or frequent claims.

- **Reduced Financial Risk:** The employer is protected from catastrophic losses. Even if claims far exceed the premium paid, the insurer bears the additional cost.
- **Simplified Administration:** The insurer manages all claims and regulatory compliance, freeing up internal resources.
- **Accessibility:** Generally available to businesses of all sizes, including small and mid-sized enterprises, without stringent financial requirements.

#### **Disadvantages of Guaranteed Cost:**

- **Less Control:** Employers have limited direct control over claims management processes or the selection of medical providers.
- **No Direct Reward for Good Performance:** If a business has an exceptionally safe year with few claims, they typically do not receive a direct refund or dividend from the insurer for that policy period (though a good claims history will positively impact future premiums through the e-mod).
- **Potential for Higher Long-Term Costs:** The premium includes the insurer's overhead, profit margin, and a buffer for unexpected losses across their entire book of business. This can sometimes result in higher overall costs compared to self-insurance for businesses with excellent safety records.

#### **Ideal Candidates for Guaranteed Cost:**

- Small to medium-sized businesses.
- Businesses with limited financial reserves to absorb unpredictable claim costs.
- Companies that prefer a "set it and forget it" approach to workers' compensation.
- Organizations with fluctuating or unpredictable claims experience.

#### **Self-Insured Group (SIG): Shared Risk and Potential Savings**

A Self-Insured Group (SIG), also known as a group self-insurance trust, is an alternative workers' compensation funding mechanism where multiple employers, typically within the same industry or association, pool their resources to collectively self-insure their workers' compensation liabilities. Instead of paying premiums to a commercial insurer, members contribute to a common fund from which claims are paid.

#### **How it Works:**

- **Pooled Risk:** Members share the financial responsibility for claims that occur within the group. This allows smaller employers to gain some of the benefits of self-insurance that would typically only be available to very large corporations.



- **Joint and Several Liability:** A critical aspect of SIGs is that members often assume "joint and several liability." This means that if one member becomes insolvent or cannot meet its obligations, the other members of the group may be responsible for covering that deficit.
- **Third-Party Administrator (TPA):** SIGs typically hire a TPA to manage claims, provide loss control services, and handle regulatory compliance.
- **Excess Insurance:** To protect against catastrophic individual claims, SIGs purchase excess or "stop-loss" insurance, which kicks in after a certain claim threshold is met.
- **Potential for Dividends:** If the group's overall claims experience is favorable and there's a surplus of funds, a portion of that surplus may be returned to members as a dividend.

#### **Advantages of Self-Insured Group:**

- **Potential Cost Savings:** By eliminating the insurer's profit margin and overhead, and by actively managing claims and loss control, SIGs can potentially offer lower long-term costs.
- **Greater Control:** Members, through their elected board of trustees, have more direct control over claims management, return-to-work programs, and loss prevention strategies.
- **Cash Flow Benefits:** Funds are often paid out as claims are incurred rather than a large upfront premium, which can improve cash flow for members.
- **Focus on Safety:** The direct financial stake incentivizes members to prioritize workplace safety and implement effective loss control programs, leading to fewer accidents.
- **Tailored Programs:** SIGs can often customize programs and services to the specific needs of their industry or group.

#### **Disadvantages of Self-Insured Group:**

- **Financial Risk (Joint and Several Liability):** This is the most significant drawback. Members are collectively responsible for the group's liabilities, meaning a financially struggling or high-claim member could impact others.
- **Administrative Burden:** While TPAs handle much of the day-to-day, the SIG itself requires active oversight from its members, including involvement in governance and financial management.
- **Unpredictable Costs:** While there's potential for savings, costs can fluctuate based on the group's overall claims experience. Assessments may be required if claims exceed expectations.



- **Collateral Requirements:** Members may be required to provide collateral (e.g., letters of credit, surety bonds) to secure their portion of the group's potential liabilities.
- **Exit Liability:** Leaving a SIG does not necessarily end your financial obligations. Members can remain liable for claims incurred during their participation, even years after exiting the group.
- **Regulatory Complexity:** SIGs are subject to specific state regulations and financial solvency requirements.

#### **Ideal Candidates for Self-Insured Group:**

- Businesses within a homogeneous industry with similar risk profiles.
- Companies with a strong commitment to safety and loss control.
- Organizations with sufficient financial stability to absorb potential assessments and collateral requirements.
- Businesses seeking greater control over their workers' compensation program and claims management.
- Employers looking for potential long-term cost savings and cash flow advantages.

#### **Key Considerations for Decision-Making**

When evaluating whether a Self-Insured Group or a Guaranteed Cost policy is the right fit for your business, consider the following:

1. **Risk Tolerance:** How comfortable is your business with assuming financial risk for workers' compensation claims?
2. **Financial Capacity:** Does your business have the reserves to handle potential assessments or collateral requirements?
3. **Claims History and Safety Culture:** A strong safety record and low claims frequency are crucial for maximizing benefits in a self-insured group.
4. **Administrative Bandwidth:** Do you have the internal resources or willingness to be actively involved in managing the workers' compensation program?
5. **Long-Term vs. Short-Term Goals:** Are you prioritizing predictable annual costs or the potential for greater long-term savings and control?
6. **Industry and Peer Group:** For SIGs, the stability and claims history of the other members in the group are paramount.

#### **Conclusion**

Both Guaranteed Cost and Self-Insured Group workers' compensation programs offer distinct advantages and disadvantages. Guaranteed Cost provides predictability,



simplicity, and complete risk transfer, making it suitable for businesses prioritizing stable budgeting and minimal administrative involvement. Self-Insured Groups, conversely, offer the potential for significant cost savings and greater control over claims and safety initiatives, but come with increased financial risk and administrative responsibility due to joint and several liability.

Choosing the optimal workers' compensation solution requires a thorough understanding of your business's unique risk profile, financial health, and strategic objectives. Consulting with an experienced insurance professional, like Ted Hamm Insurance, is crucial to analyze your specific needs and determine the most effective path to protecting your employees and your bottom line.

