cent, whereas the corresponding ratio for exclusive state funds was 5.8 percent. The administrative-expense ratio of private carriers is more likely to be in the area of 23 percent. The cost advantage enjoyed by state funds should be available to employers in the form of lower rates. However, as the Elson and Burton study demonstrated, Ohio's rates are above the national average.

Higher-than-average costs for Ohio's employees simply might be the result of higher-than-average WC benefits for Ohio's employees. According to Price (1979), benefits paid in Ohio appear to surpass the national average, although the benefit scale is typical of other states. Ohio contests a greater proportion of claims and perhaps larger benefits per claim. For instance, benefits in Ohio in 1976 were about 1 percent higher than in covered employment, placing them above the national average: only 15 other states paid at a rate at least as great as Ohio's. By comparison 14 other states (including New York, Illinois, and Pennsylvania) paid 0.50 percent to 0.69 percent of payroll in total benefits.

Samers and Kelly (1980) studied a third dimension of comparison between state funds and private carriers—the promptness with which claims are paid. This aspect of WC generally has been overlooked.

6. The estimate of 23 percent is based on my reexamination of the data presented by Price in his tables 8, 9, and 11. Table 11 reports expenses as 10.1 percent of premiums written for state funds in 1976. Table 9 reports expenses of $17.7 billion and premiums earned of $6.67 billion for stock and mutual carriers in 1976. Table 6 reports the ratio of premiums written to premiums earned. Given the difficulty in making comparisons, the wide variation in WC systems among states provides some information that bears on the issue-l debate. The Ohio WC system entails both larger costs and complexity, and emotion in the issue-l debate from private-insurance coverage. Private-insurance carriers to enter the market. A number of organizations have announced their opposition to this change, including the Ohio Manufacturers' Association, the Ohio Chamber of Commerce, the Greater Cleveland Growth Association, the Ohio AFL-CIO, and the Nationwide Insurance Company. Such a unique amalgam of interests opposing private competition for workers' compensation indicates the extent of confusion, complexity, and emotion in the issue-l debate. The passage of Issue 1 will not guarantee competition; it will merely permit private-insurance carriers to enter the market. The Ohio Department of Insurance will be responsible for regulating these carriers if Issue 1 passes.

Both economic theory and economic experience demonstrate the benefits of competitive markets to consumers. Therefore, arguments in favor of a state monopoly are viewed with skepticism. This Economic Commentary discusses workers' compensation (WC) in Ohio and compares public and private systems in the United States using the criteria of costs, benefits, and quality of service. With proper supervision a competitive market has the potential of reducing employers' costs and improving service to employees, with no change in benefits.

### Federal Reserve Bank of Cleveland

#### Economic Commentary

by Mark S. Sniderman

The state of Ohio, which currently forbids private-insurance companies from competing with state-run workers' compensation programs, is now in the throes of deciding whether to allow private-insurance carriers to enter the market. A number of organizations have announced their opposition to this change, including the Ohio Manufacturers' Association, the Ohio Chamber of Commerce, the Greater Cleveland Growth Association, the Ohio AFL-CIO, and the Nationwide Insurance Company. Such a unique amalgam of interests opposing private competition for workers' compensation indicates the extent of confusion, complexity, and emotion in the issue-1 debate. The passage of Issue 1 will not guarantee competition; it will merely permit private-insurance carriers to enter the market. The Ohio Department of Insurance will be responsible for regulating these carriers if Issue 1 passes.

Both economic theory and economic experience demonstrate the benefits of competitive markets to consumers. Therefore, arguments in favor of a state monopoly are viewed with skepticism. This Economic Commentary discusses workers' compensation (WC) in Ohio and compares public and private systems in the United States using the criteria of costs, benefits, and quality of service. With proper supervision a competitive market has the potential of reducing employers' costs and improving service to employees, with no change in benefits.

#### Historical Perspective

The industrialization of America brought with it social concern over the employer's responsibility for safety in the workplace. As was the case for many early social re-
Even prior to the audit, some reforms had been initiated. A system designed to protect fund-outlays and assure that the processing procedures were implemented. Even more significant was a new state law that mandated either a 25 percent rise in the state fund in the event of employment-related injury. The immediate result was an average rate increase of 10 percent and another 22 percent increase in 1976. Rates declined 19 percent in 1978 and have been relatively stable since.

The discovery of the Ohio fund will probably not take as long as most had feared. The state-fund deficit has been growing steadily during the past four years, but although it is uncertain whether the deficit has yet been eliminated. The recovery stems in part from the higher employers' contribution rates, the 1976 rate increases, the fund-investment gains. The current and prospective actuarial condition of the state fund figure prominently in the opposition to Issue 1. For example, some opponents actually favor the entry of private carriers into the WC market, but not until the actuarial condition of the state fund is assured. Another Issue-1 opponent contends that the fund need not be subject to the same actuarial scrutiny as private-insurance carriers, in the belief that the Ohio state ultimately guarantees fund solvency.

Costs, Benefits, and Services

Most Issue-1 opponents fear that a competitive WC system would increase employers' costs. 

In the summer of 1975, an investigation of the Ohio WC program revealed questionable uses of funds and general mismanagement. In April 1976, Governor Rhodes appointed a new chairman of the Ohio Industrial Commission (OIC), whose first act was to authorize a complete audit. In March 1977 the audit concluded that the fund had a substantial actuarial deficit (1.1 percent). Soon after the release of the audit, the new OIC chairman stated that complete recovery of the fund could take as long as a decade. That same month, a Cleveland newspaper editorial planted the seeds of what has now become Issue 1: 

"... In view of the horrendous bureaucratic problems historically experienced by the Ohio system and the rising employer contribution rates, this would be a fit moment for the General Assembly to undertake a careful feasibility study of the best way to turn the mono-poly over to private insurance companies."


Table 1: Employers' Average Weekly Costs of Workers' Compensation Insurance As of July 1, 1978

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3. See Elson and Burton, p. 46.

4. The average adjusted manual rate is 1.376; Ohio's rate is 1.550.


forms, however, there was resistance to state control over private enterprise. The American system of compensation for the case of work-related injury was largely bound by precedents passed down from English common law. Until the fundamental framework it would be difficult to hold an employer in any part responsible for injuries sustained by his employees, where cases did fit some rather narrow liability definitions, the cost of litigation was often a major deterrent to employee action. Few states were relatively free of such laws prior to 1900.

In 1926, despite insurance mechanisms, the states and the federal government had been legislating in many European communities, the state of Maryland enacted legislation establishing a cooperative accident insurance fund and provided for the payment of death benefits in the event of an employment-related death. The act soon was rescinded, as attempts successfully attacked its constitutionality. Similar efforts in other states followed the Wisconsin initiative. In March 1977 the audit concluded that the OIC fund had a substantial actuarial deficit ($1.3 billion). Soon after the release of the audit, the new OIC chairman speculated (act as their own insurance company and not as private-insurance carriers, in the belief that the state of Ohio ultimately guarantees fund solvency. The current and prospective actuarial condition of the state fund figure prominently in the opinion to Issue 1. For example, some opponents actually favor the entry of private carriers into the WC market, but not until the actuarial soundness of the state fund is assured. Another Issue-1 opponent contends that the fund need not be subject to the same actuarial scrutiny as private-insurance carriers, in the belief that the state of Ohio ultimately guarantees fund solvency.

Costs, Benefits, and Services

Most Issue-1 opponents fear that a competitive WC system would increase employers' costs, reduce benefits, and put more red tape between the insured and the compensation system. To demonstrate these fears, Issue-1 proponents take the opposite stance. Each side cites supporting estimates of these three measures as of July 1978.

Table 1. Employers' Average Weekly Costs of Workers' Compensation Insurance As of July 1, 1978

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</table>


4. The average adjusted manual rate is 1.736; Ohio's rate is 1.550.


6. See Elson and Burton, p. 46.
forms, however, there was resistance to state control over private enterprise. The American system of compensation for the case of work-related injury was largely bound by precedents passed down from English common law. Under this legal framework it was difficult to hold an employer in any particular state responsible where cases did fit some rather narrow liability definitions, the cost of litigation often being a major deterrent to employer action. Even those relatively few claims which did arise prior to 1900.

In 1962, after decades of insurance mecha-
nization and computer technology, Ohio had been legislated in many European com-

Even prior to the audit, some reforms had been instituted. A system designed to protect fund stability and reduce the sometimes pro-
2. See Martin W. Elson and John F. Burton, Jr., "Workers’ Compensation: Recent Developments in Employers’ Costs," Monthly Labor Review, vol. 104, no. 3 (March 1981), pp. 45-59. This study covers workers’ compensation costs for the states of Ohio, Pennsylvania, Virginia, and Wisconsin. Five states were selected for study: Arkansas, California, Colorado, Connecticut, and Delaware. District of Columbia, and Puerto Rico have WC laws. In 34 states insurance is sold strictly through private carriers; in 12 states a state-insurance program competes with the private carriers, though the state-insurers are limited to underwriting the state-syndicated program for work-related injury. The state-syndicate, therefore, operates a WC in-
surance monopoly (the others are Nevada, New York, North Carolina, Ohio, Washington, West Virginia, and Wyoming).

Ohio permits employers to self-insure (as their own insurance company and not under a state fund) if they can demon-
strate adequate financial solvency. Out of 240,000 employers in the state-WC system, only 320 are self-insured; though the self-insurers account for less than 1 percent of all em-

Table 1: Employers’ Average Weekly Costs of Workers’ Compensation Insurance As of July 1, 1978

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>45 types of employers</th>
<th>Rank</th>
<th>45 types of employers</th>
<th>Rank</th>
<th>45 types of employers</th>
<th>Rank</th>
</tr>
</thead>
</table>
| Alabama      | 11,043               | 9    | Alabama              | 11,043 | 9                    | 11,544 | 9
| Alaska       | 2,143                | 13   | Alaska               | 2,143 | 13                   | 4,679  | 13
| Arizona      | 2,316                | 13   | Arizona              | 2,316 | 13                   | 6,946  | 13
| Arkansas     | 1,425                | 13   | Arkansas             | 1,425 | 13                   | 11,920 | 13
| California   | 3,305                | 13   | California           | 3,305 | 13                   | 4,285  | 13
| Colorado     | 1,736                | 13   | Colorado             | 1,736 | 13                   | 14,170 | 13
| Connecticut  | 2,557                | 13   | Connecticut          | 2,557 | 13                   | 15,465 | 13
| Delaware     | 1,712                | 13   | Delaware             | 1,712 | 13                   | 2,972  | 13
| District of Columbia | 4,271 | 7 | District of Columbia | 4,271 | 7                    | 8,199  | 7
| Florida      | 3,223                | 13   | Florida              | 3,223 | 13                   | 13,779 | 13
| Georgia      | 3,133                | 13   | Georgia              | 3,133 | 13                   | 19,112 | 13
| Hawaii       | 2,508                | 13   | Hawaii               | 2,508 | 13                   | 3,964  | 13
| Idaho        | 1,564                | 13   | Idaho                | 1,564 | 13                   | 2,252  | 13
| Illinois     | 1,685                | 13   | Illinois             | 1,685 | 13                   | 3,063  | 13
| Indiana      | 5,186                | 8    | Indiana              | 5,186 | 8                    | 6,601  | 8
| Iowa         | 1,322                | 10   | Iowa                 | 1,322 | 10                   | 17,218 | 10
| Kansas       | 1,072                | 11   | Kansas               | 1,072 | 11                   | 2,699  | 11
| Kentucky     | 1,668                | 9    | Kentucky             | 1,668 | 9                    | 2,780  | 9
| Louisiana    | 1,844                | 5    | Louisiana            | 1,844 | 5                    | 4,092  | 5
| Maine        | 1,664                | 13   | Maine                | 1,664 | 13                   | 3,769  | 13
| Maryland     | 1,359                | 21   | Maryland             | 1,359 | 21                   | 2,526  | 21
| Massachusetts| 1,674                | 7    | Massachusetts        | 1,674 | 7                    | 2,757  | 7
| Michigan     | 2,003                | 4    | Michigan             | 2,003 | 4                    | 4,173  | 4
| Minnesota    | 2,220                | 4    | Minnesota            | 2,220 | 4                    | 3,733  | 4
| Mississippi  | 1,100                | 14   | Mississippi          | 1,100 | 14                   | 1,457  | 14
| Missouri     | 9,000                | 1    | Missouri             | 9,000 | 1                    | 5,198  | 1
| Montana      | 1,712                | 21   | Montana              | 1,712 | 21                   | 2,767  | 21
| Nebraska     | 8,065                | 7    | Nebraska             | 8,065 | 7                    | 1,485  | 7
| New Hampshire| 4,228                | 12   | New Hampshire        | 4,228 | 12                   | 2,178  | 12
| New Jersey   | 2,057                | 36   | New Jersey           | 2,057 | 36                   | 3,657  | 36
| New Mexico   | 3,751                | 4    | New Mexico           | 3,751 | 4                    | 2,475  | 4
| New York     | 1,518                | 17   | New York             | 1,518 | 17                   | 3,844  | 17
| Ohio         | 1,668                | 22   | Ohio                 | 1,668 | 22                   | 6,899  | 22
| Oklahoma     | 1,763                | 34   | Oklahoma             | 1,763 | 34                   | 2,654  | 34
| Oregon       | 1,516                | 17   | Oregon               | 1,516 | 17                   | 2,625  | 17
| Pennsylvania | 1,431                | 19   | Pennsylvania         | 1,431 | 19                   | 2,388  | 19
| Rhode Island | 1,389                | 23   | Rhode Island         | 1,389 | 23                   | 2,387  | 23
| South Carolina| 1,029               | 50   | South Carolina       | 1,029 | 50                   | 1,350  | 50
| South Dakota | 1,021                | 50   | South Dakota         | 1,021 | 50                   | 1,649  | 50
| Tennessee    | 1,101                | 15   | Tennessee            | 1,101 | 15                   | 1,666  | 15
| Texas        | 1,351                | 7    | Texas                | 1,351 | 7                    | 1,350  | 7
| Utah         | 1,078                | 13   | Utah                 | 1,078 | 13                   | 1,803  | 13
| Vermont      | 1,005                | 16   | Vermont              | 1,005 | 16                   | 1,645  | 16
| Washington   | 7,074                | 6    | Washington           | 7,074 | 6                    | 1,255  | 6
| West Virginia| 9,062                | 6    | West Virginia        | 9,062 | 6                    | 3,229  | 6

Higher-than-average costs for Ohio's employees simply might be the result of higher-than-average WC benefits for Ohio's employees. According to Price (1979), benefits paid in Ohio appear to surpass the national average, although the benefit scale is typical of other states. Ohio seems to grant more claims and perhaps larger benefits per claim. For instance, benefits in Ohio in 1976 were about 1 percent of payrolls in covered employment, placing them above the national average: only 15 other states paid at a rate at least as great as Ohio's. By comparison, 14 other states (including New York, Illinois, and Pennsylvania) paid 0.50 percent to 0.69 percent of payroll in total benefits.

Samers and Kelly (1980) studied a third dimension of comparison between state funds and private carriers—the promptness with which claims are paid. This aspect of WC generally has been overlooked in the literature. Table 8 reports the administrative-expense ratio of private carriers to be 10.1 percent of premiums earned, whereas the corresponding ratio for state funds was 7.0 percent in 1976. Table 8 also reports the ratios of premiums written to premiums earned for state funds in 1976 at 78 percent in Ohio. Ohio seems to grant more claims and perhaps larger benefits per claim. For instance, benefits in Ohio in 1976 were about 1 percent of payrolls in covered employment, placing them above the national average: only 15 other states paid at a rate at least as great as Ohio's. By comparison, 14 other states (including New York, Illinois, and Pennsylvania) paid 0.50 percent to 0.69 percent of payroll in total benefits.

By another measure of service quality—satisfaction with the way in which claims are handled—Ohio's WC system appears to offer the possibility of an improvement in promptness with which claims are paid. Evidence reported in this Economic Commentary does not strongly indicate Ohio's current WC system, but neither does it give reason to praise it. Perhaps more relevant to the discussion is whether the long-term public interest is best served by monopoly or by competition. In light of Ohio's experience just prior to 1976, this is a meaningful choice. Those concerned with workers' welfare might be willing to compromise contested cases than other carriers, yet they still lose a much greater proportion of the litigated claims than other insurers.

Concluding Remarks

WC is currently a much-debated topic throughout the nation. Several states recently have reconsidered modifications in rate-setting or benefit provisions. State legislatures set the benefit levels and establish oversight rules and market structures; the latter influences the economic cost of insurance and the administrative process governing claims and payments. Issue 1 determines whether a change in competition is better than in existing case law, or vice versa. While Ohio contested cases at the same rate as the national sample (18 percent), Ohio's WC system is the only state with no change in either case. Private coverage would appear to offer the possibility of an improvement in the promptness with which claims are handled.

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The state of Ohio, which currently forbids private-insurance companies from competing with the state-run workers' compensation program, is now in the throes of deciding whether to allow private-insurance carriers to enter the market. A number of organizations have announced their opposition to this change, including the Ohio Manufacturers' Association, the Ohio Chamber of Commerce, the Greater Cleveland Manufacturers' Association, the Ohio Chamber of Commerce, the Greater Cleveland Growth Association, and the Nationwide Insurance Company. Such a unique amalgam of interests opposing private competition for workers' compensation indicates the extent of confusion, complexity, and urgency in the Issue 1 debate. The passage of Issue 1 will not guarantee competition; it will merely permit private-insurance carriers to enter the market. The Ohio Department of Insurance will be responsible for regulating these carriers if Issue 1 passes.

Both economic theory and economic experience demonstrate the benefits of competitive markets to consumers. There-fore, arguments in favor of a state monopoly are viewed with skepticism. This Economic Commentary discusses workers' compensation (WC) in Ohio and compares public and private systems in the United States using the criteria of costs, benefits, and quality of service. With proper supervision, a competitive market has the potential of reducing employers' costs and improving service to employees, with no change in benefits.
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Samos and Kelly (1980) studied a third
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ness with which claims are paid. This
aspect of WC generally has been overlooked
in the issue-1 debate. Since WC is designed
to protect against the interruption of in-
come and not necessarily those of the Federal Reserve Bank of Cleveland. The author
wishes to thank Michael F. Bryant for his con-
tribution to the historical section.

The views stated herein are those of the author
and not necessarily those of the Federal Reserve
Bank of Cleveland or the Board of Governors of the Federal Reserve System.

Federal Reserve Bank of Cleveland
September 21, 1981

The industrialization of America brought
with it social concern over the employer's
responsibility for safety in the work place.
As was the case for many early social re-
form movements, arguments in favor of a state monopoly
did not strongly indict Ohio's
system entail both larger costs and
benefits than the national average, although
timeliness of payment is an important
dimension of comparison between state
funds and private carriers—the prompt-
ness between uncontested and contested
cases, the incidence of contested cases also
appears to offer the possibility of an im-
provement in the promptness with which
claims are handled.

Evidence reported in this Economic
Commentary does not strongly indicate Ohio's
current WC system, but neither does a basis
for praise emerge. Perhaps the most funda-
mental aspect of the issue-1 debate is the
comparative features and other carriers, yet they still lost a much
greater proportion of the litigated claims
than other insurers.

Concluding Remarks
WC is currently a much-debated topic
throughout the nation. Several states recently
made modifications in rate-setting or benefit provisions. State
legislatures set the benefit levels and estab-
lish oversight rules and market structure; the
latter influences the economic cost of in-
surance and the administrative process
governing claims and payments. Issue 1
discusses a change for a change in market structure from mono-
opoly to competition.

Despite the difficulty in making com-
parisons, the wide variation in WC systems
among states provides some information
that bears on the issue-1 debate. The Ohio
WC system entails both larger costs and
benefits than the national average, although
not much different from the national aver-
age in either case. Private coverage would
appear to offer the possibility of an im-
provement in the promptness with which
claims are handled.

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