

Workers' Compensation: The Case for Improved DoN Management

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Approved for distribution:

May 2003

A handwritten signature in black ink that reads "Paul E. Speer". The signature is written in a cursive style with a large, prominent 'P' and 'S'.

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Summary

Background

The Federal Employees' Compensation Act (FECA) provides for compensation to federal civilian employees who sustain disability due to work-related injury or illness. Each year, the Department of the Navy (DoN) pays about \$245 million in workers' compensation and related medical benefits under the FECA program. The cost of this bill is the highest among current federal agencies (and second only to the Post Office among program participants). The comparatively high costs have been an issue of concern since at least the late 1980s.

CNA first looked at DoN workers' compensation costs about 2 years ago [1]. At that time, we identified two DoN programs as particularly effective at controlling costs and giving appropriate concern to the needs of injured workers. Diligence in attention to claim status and the return of employees to the workplace as soon as possible were found to be the primary contributors to containing FECA costs. Our analysis suggested that \$300 to \$400 million in savings over 10 years might be possible from broader application of best practices. We recommended:

- The establishment of regionally consolidated teams to attend to long-term cases.
- Greater commitment at the activity and command level to return-to-work efforts.
- The establishment of program metrics directly related to effectiveness in case management.
- More focused high-level attention to the performance of local FECA programs.

The CNA study attracted considerable attention. In June 2001, the Deputy Chief of Naval Operations (Readiness and Logistics) addressed the Regional Commanders, asking them to personally take the lead in

implementing CNA recommendations [2]. CNO (N45) proposed a \$3-million annual budget to support regional FECA programs. In 2002, the Naval Audit Service began an assessment [3] to evaluate, among other things, compliance with return-to-work recommendations of the CNA report. Despite such attention, little of substance appears to have changed in the 2 years. In general, efforts to gain additional program resources failed. Worse, there are indications that program effectiveness is declining.

Tasking and study approach

The Deputy Assistant Secretary of the Navy (Safety) asked CNA to consider why the FECA program continues to be a problem and to provide concrete suggestions for improvement. We were asked to (a) examine the workers' compensation program again, (b) propose specific solutions, and (c) make the business case for implementing solutions.

To address these issues, we analyzed compensation data and conducted discussions with personnel at headquarters and regional levels (NAVSEA, NAVAIR, and NAVFAC; Southwest, Southeast, Mid-Atlantic, and Northeast).¹ The previous empirical analysis is updated to reflect 3 years of new data and expanded to more clearly identify where savings can be achieved. As before, we use an actuarial model to estimate the payoff that could be generated by applying DoN best management practices. Whereas the previous study focused on just two successful programs, we now more broadly identify effective programs and those where there could be improvement.

The FECA program—key issues

The FECA program is administered by the Department of Labor, Office of Workers' Compensation Program (OWCP). OWCP has primary responsibility for case management and is the sole authority in decisions as to eligibility and claim status. Within DoN, an Injury

¹ We use data on FECA payments to individual DoN claimants from 1998 to 2002. Data were provided to us stripped of personal identifiers in order to protect privacy.

Compensation Program Administrator (ICPA), usually located in a human resources or civilian personnel office (CPO), deals with claims on a day-to-day basis. Although the ICPA might have no direct control over claim status, his or her active involvement can help ensure that OWCP actions are timely and well-founded. ICPAs also assist in returning employees to work and in keeping local activities aware of cost and responsibilities.

Disability cases may be considered either *short-term* or *long-term*. Short-term cases are those expected to return to work within a year. Workers who do recover within a year are guaranteed their original position or an equivalent. Long-term cases include claimants without wage-earning potential (*permanent roll*) and others who may benefit from long-term recovery (*periodic roll*). Those on the long-term rolls are terminated from DoN employment, but have priority for reemployment on recovery. The focus of long-term case management is the periodic roll. There are now about 2,200 periodic roll claimants, accounting for \$75 million of the annual FECA bill. Past inattention to these claimants has proved costly, as the likelihood of return diminishes with time.

OWCP pays benefits and bills the Department of Defense (DoD). Billing procedures result in more than a 15-month lag in payment. For example, the FECA bill for 2003 (July 2002 to June 2003) will be received at DoD by early September 2003. That bill will be paid in October 2004, with fiscal year 2005 dollars. The lag in payment is significant in that realized savings from case management are pushed back some 2 years after investment of effort. Of particular concern is the disincentive the billing lag creates for light-duty and transitional employment. When an injured worker is on compensation, the expense is delayed and comes due as a “must pay” bill subject to limited scrutiny. Employment costs are incurred immediately and draw on payroll budgets that are limited and closely watched. With growing concern over competitiveness—due to potential outsourcing and BRAC closure—the attraction of postponing payroll cost is strong. This is despite current policy that calls for “every effort” to return recovering workers and offers exemptions from any hiring freeze [4]. The idea of accelerating FECA payments has on occasion been explored, but budgeting complications make change unlikely.

Until recently, DoN commands² or activities were directly billed for their share of FECA. Beginning in fiscal year 2004, the bill will be paid centrally, with a paper allocation of cost to commands. Commands may then further allocate to activities. The change in payment practice is for the administrative convenience of the comptroller. Disagreements over claim ownership have led to delays in paying FECA bills. Disagreements are usually the consequence of past realignment and base closures that make it difficult to match older claims to the activity now responsible for a job once held. It is unclear whether the new payment scheme substantially alters incentives to address costs.

Responsibility for FECA within DoN has been decentralized. Commands are delegated the primary responsibility for ensuring that compensation programs are effectively administered. With consolidation of local FECA offices, this line of authority is now somewhat weakened. Activity commanders have responsibility for return-to-work programs. DoD has the only central role, providing policy and support through the Civilian Personnel Management Service (CPMS). The 1993 establishment of this DoD office left no one in DoN with clear responsibility for the overall program. The Office of the Deputy Assistant Secretary of the Navy (Civilian Personnel/Equal Employment Opportunity) [DASN (CP/EEO)] does still coordinate flow of policy and information. That office could perhaps play a greater role, but has neither the staff nor clear responsibility to do so.

The FECA legislation has a number of flaws that create perverse incentives and make management a challenge:

- FECA provides unusually generous benefits, with tax-free payments of up to 75 percent of earnings. For some, this can mean greater income while on compensation than while working.
- FECA has no waiting period before the start of benefit, which is in contrast to the typical workers compensation program where an initial 3-day waiting period reduces incentives for speculative claims.

² We use the term “commands” to mean “major claimants” (e.g., NAVAIR, NAVFAC). The word “claimants” is reserved to refer to individuals receiving compensation.

- Compensation continues after retirement age, unless the claimant chooses retirement. More than 37 percent of the DoN FECA bill now goes to claimants over 65. This results in unnecessary administrative burden and distraction.
- The determination of legitimacy of claims is left solely to OWCP, an organization that is charged by law to be an advocate for claimant rights and which bears none of the financial consequences of abuse or case management.

Legislative proposals to correct several of these flaws have been offered to Congress, but never acted on.

Study findings

A summary of our study findings follows:

- The effectiveness of DoN's FECA programs is declining.
 - The expected lifetime cost of a claim is up 50 percent since our earlier study. This corresponds to an \$11-million jump in the average annual future FECA bill.
 - The percentage of new claims closed within a year is at the lowest level in a decade.
 - The percentage of cases removed annually from the periodic rolls is roughly half of 1999 levels.
- Specific explanations for the decline are not consistent across the program, but include (a) growing reluctance of activities to return workers to transitional jobs, (b) effects of various realignments in disrupting case management, (c) diminished opportunity, after past success in screening periodic rolls, and (d) costs related to expanded OWCP efforts at early intervention.
- More generally, the problems reflect a failure of program oversight. We find a lack of awareness as to program performance and misguided satisfaction in the stabilization of the FECA bill.
- The FECA bill has actually been declining slightly relative to inflation. However, this is simply the inevitable result of a

50-percent reduction in workforce and safety improvements over the last decade. Recent problems have sacrificed much of a larger gain that should have been expected.

- The potential decline in the FECA bill has not eliminated the possibility for savings. We estimate that savings of up to \$140 million over 5 years are possible—if DoN as a whole could control costs as well as the best 25 percent of its programs. The cost of achieving these savings is probably less than \$3 million.
- What now distinguishes the best FECA programs is their ability to contain costs in the first few years of a claim. Such success relies on activity commanders meeting their responsibility to provide a pool of transitional jobs for recovering workers and for return to work. The best programs also show steady success in addressing their periodic rolls. Such effective long-term case management requires persistence and manpower.
- We find no one geographic region or command to have been uniformly superior or deficient in controlling costs in the last few years. At the level of the individual program, we see wide differences of performance. There are opportunities for improvement across the country.
- Base closures and realignments have churned responsibility for claims, interfering with consistent case management. Claims that have not had consistent management are among the most costly. Were these managed as well as others, the average FECA bill would drop almost \$7 million. The upcoming round of base closures presents a challenge that needs to be anticipated.
- The FECA program suffers from lack of central coordination.
 - The screening and resolution of older claims calls for a focused team effort and the services of specialists. Even the largest FECA offices can find it difficult to consistently follow up on older claims. The program could benefit from economies of scale if screening and investigative support were made available through a few FECA centers.
 - The current approach to establishing return-to-work slots is not working well. It depends on the goodwill of individual

activities. It does not reflect the reality that industrial activities where most injuries occur may not offer the most suitable positions for recovering or disabled workers. A more regionally coordinated approach to establishing job pools for return to work would be helpful.

- Oversight is too fragmented, with no one really aware of how individual FECA programs are performing.

Recommendations

We see three key problem areas to be addressed. These are the same areas of concern identified in our earlier study. The program needs:

- A more centralized approach to long-term case management.
- Greater attention to return to work.
- More central oversight and meaningful metrics of program performance.

Claims management centers for long-term claims

Issue: Claims filed in 1998 or earlier cost the Navy \$190 million in 2002. Despite the success of many programs in screening long-term rolls, there remains a backlog. Even among bigger programs, it is difficult—given the urgency of current claims—to maintain the consistent focus on older claims that is necessary. It is a job that requires dedicated specialists, but the scale of effort called for locally is usually too small to justify such focus.

Action: Establish two claims management centers—one on each coast—to provide support to existing FECA programs in older case management. Their role should be in screening older claims to confirm current status, establishing priorities for further action on cases where there is potential abuse or possibility of return to work, and supporting FECA offices with further investigative needs. The centers might take on a greater role with future BRAC closures.

NAVSEA already has two such centers to deal with closed shipyard cases. We suggest expanding on these, by adding to the existing

experienced staff.³ Alternatively, centers could be established in association with Human Resource Service Centers in Norfolk and San Diego. In either case, we recommend that the Office of the DASN (CP/EEO) be involved in oversight. Staff positions can be supported by major claimants, in proportion to their periodic rolls.

Resources: An additional five FTEs for 5 years in each of the two centers should be adequate to support a reasonable pace of work. After five years, a smaller team should be sufficient.

Cost: The incremental cost would be about \$750,000 a year, assuming GS-11/Step 5 salaries and benefits. Were contractors used, the cost might be \$1.5 million a year.

Payoff: We give the payoff to a 5-year effort. It is assumed that implementation occurs in FY04 and effects are observed a year later. A 2-year delay in the FECA bill further postpones the initial savings until FY07. Table 1 shows annual costs, benefits, and net returns.⁴ Break-even occurs in the first year of impact (2005 FECA bill, with savings in FY07). The benefit-cost ratio is 11.8, when calculated with present values. The internal rate of return is 108 percent. At contractor salaries, breakeven is delayed a year, the benefit-cost ratio becomes 6.6, and the internal rate of return drops to 71 percent.

Table 1. Payoff to long-term claims management (\$ millions)^a

| | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 | Total |
|-------------------|-------|-------|-------|------|------|------|------|------|-------|
| Cost | 0.75 | 0.75 | 0.75 | 0.75 | 0.75 | | | | 3.75 |
| Benefit | | | | 4.5 | 7.7 | 10.4 | 12.6 | 14.3 | 49.5 |
| Net return | -0.75 | -0.75 | -0.75 | 3.7 | 6.9 | 10.4 | 12.6 | 14.3 | 45.7 |
| Net present value | -0.75 | -0.73 | -0.70 | 3.4 | 6.1 | 8.9 | 10.4 | 11.5 | 38.1 |

a. Values are in 2002 dollars; present values are calculated using a 3.2-percent rate, discounting to 2004.

³ The West Coast center may close soon, reflecting a diminishing workload and upcoming staff retirements.

⁴ Benefits were estimated by assuming that DoN as a whole achieves the same level of success in older claims management (claims opened in 2000 or earlier) as the best 20 percent of current programs.

Encourage reemployment efforts

Issue: Our analysis suggests that the programs that are strongly committed to getting people back to work quickly (such as Portsmouth Naval Shipyard) are now the best at achieving savings. Effective reemployment efforts seem to have a powerful leveraged effect on the FECA bill. The establishment of an atmosphere where an injured worker is expected to return to work has indirect effects that are very apparent in lower overall costs.

Actions:

- Use metrics and audits to encourage activities to fulfill existing obligation to provide transitional employment and return-to-work opportunities.
- Encourage establishment of regional pools for return to work.
- Consider limited central funding for reemployment from the periodic rolls. Perhaps cover a year of employment for 10 to 20 people per year.
 - CPMS already manages a similar program for the Air Force.
 - We are concerned that a more extensive program could undercut incentives to establish well-designed local efforts.

Resources: None.

Cost: Perhaps none—so long as productivity exceeds wages and cost of job accommodations. To be conservative, we assume the equivalent of 30 full-time positions are hired from periodic rolls annually, with no net productivity for one year. This gives an incremental cost of \$1.5 million a year, assuming GS-7/Step 5 salaries.

Payoff: Table 2 shows annual costs, benefits, and returns. We show the payoff to a 5-year effort assuming planning starts in FY04 with implementation in FY05. Savings are first reflected in the 2005 FECA bills and realized in FY07. Breakeven occurs with the first year of savings (FY07). The benefit-cost ratio (calculated with present values) is 11.6. The internal rate of return is 182 percent. Benefits were estimated assuming DoN as a whole achieves the same success in newer claims management as the best 25 percent of current programs.

Table 2. Payoff to reemployment and early claims management (\$ millions)^a

| | FY04 | FY05 | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 | Totals |
|-------------------|------|------|------|------|------|------|------|------|--------|
| Cost | 1.5 | 1.5 | 1.5 | 1.5 | 1.5 | | | | 7.5 |
| Benefit | | | | 9.0 | 15.2 | 19.7 | 23.5 | 26.9 | 94.4 |
| Net return | -1.5 | -1.5 | 7.6 | 13.9 | 18.4 | 23.6 | 27.0 | | 87.5 |
| Net present value | -1.5 | -1.4 | 7.0 | 12.2 | 15.7 | 19.6 | 21.7 | | 73.2 |

a. Values are in 2002 dollars; present values are calculated using a 3.2-percent rate, discounting to 2004.

Central oversight

Issues: The DoN FECA program suffers from lack of central oversight and coordination.

Action: Establish an additional position under the DASN (CP/EEO) with responsibility for oversight of FECA programs. Alternatively, establish a position under the new Chief of Naval Installations (CNI).⁵ Responsibilities should include (a) evaluation of program performance, (b) oversight of claims management centers, (c) advocacy for program support, and (d) coordinating flow of policy and information.

Resources: One additional FTE.

Cost: Approximately \$125,000 a year, assuming a GS-14 position.

Payoff: The payoff is not separable from overall returns to other recommendations.

Improved metrics

Issues: There are no widely-reported metrics that meaningfully reflect effectiveness in FECA case management.

Actions: Develop metrics that are clearly related to day-to-day management. Evaluate individual programs and commands based on com-

⁵ Oversight through the DASN (CP/EEO) would seem most logical, given that FECA is primarily a human resources program. Oversight through CNI offices might best reflect the fact that FECA management is increasingly a regionally provided base support function.

parative performance and set goals for improvement. Establish an annual report that documents overall program performance in meeting goals. We elaborate on these actions below:

- To evaluate local FECA offices, we recommend the following metrics:
 - *Lost workdays*: Average lost workdays per lost-time claim.
 - *Long-term case closure*:⁶ Cases removed from the periodic roll divided by the number cases on the periodic rolls.
 - *Return to work*: Personnel returned to work from the long-term rolls divided by number of cases on the periodic rolls.
- To evaluate commands, we recommend a report on the year-end disposition of periodic roll cases and an explanation of unexpected cost increases at activities.
 - *Status of claims on periodic rolls*. Provide an annual breakdown showing current status of cases that began the year on the periodic rolls. For cases closed, provide a detailed breakdown to highlight results of claims management.
 - *Explanation of cost increase*. Provide an explanation of significant cost increases at activities (e.g., more than 15 percent increase at activities with a FECA bill over \$500,000).⁷

Resources: None.

Cost: Not significant.

Payoff: The payoff is not separable from the overall return to our other recommendations.

Organization of this report

In the first section, we give an overview of the FECA program, including descriptive statistics. Then we present our methods and the

⁶ Excluding cases transferred from the periodic to the permanent roll.

⁷ Such a requirement would have covered 16 activities last year.

empirical assessment of the savings that might result if more attention were paid to FECA management.

Overview of the FECA program

In this section, we briefly describe the major elements of the FECA program and its management. We then provide some descriptive statistics on the DoN workers' compensation program. Finally, we comment on negative trends that have become apparent in recent years.

The FECA Workers' Compensation Program

The Federal Employees' Compensation Act (FECA) provides compensation to federal civilian employees who are injured on the job. Like many workers' compensation programs, it is a no-fault system, with FECA being the sole avenue by which an injured worker may recover damages. The program is administered by the Department of Labor, Office of Workers' Compensation Program (OWCP). FECA operations are financed by OWCP, with costs reimbursed by federal agencies.

Benefits

An employee who suffers injury or illness related to employment is eligible for the following types of benefits:

- *Continuation of pay (COP)*. An injured employee continues to receive a regular DoN paycheck for up to 45 calendar days. This cost is not reflected in annual FECA bills.
- *Disability compensation*. After the COP period, employees may receive OWCP compensation for loss of wages. Payment continues for the period of disability, without limit.
 - While on full disability, a claimant receives up to 75 percent of prior earnings, tax free (66 percent, if no dependents).
 - With partial disability, compensation is paid for the loss of wage-earning capacity.

- *Schedule awards.* Lump sum payments are provided for loss of body parts or functions.
- *Medical benefits.* Payments are made for necessary medical services. Benefits can continue after return to work, without limit.
- *Vocational rehabilitation.* Vocational training may be provided. After training, a claimant is expected to seek work, and compensation is reduced to reflect wage-earning capacity.
- *Death benefits.* If a death is job-related, dependents are entitled to compensation. A surviving spouse will receive compensation until death or remarriage.

Reemployment

Injured workers retain restoration rights for 1 year; if fully recovered within the year, an employee has unconditional rights to his or her former position or a close equivalent. Partially recovered employees are not guaranteed their original job, but if they return within the year are to be placed in a suitable, comparable position. DoD policy [4] encourages use of light-duty positions to bring injured workers back quickly into temporary positions that are compatible with physical limitations.

Workers who recover after a year are entitled only to priority consideration for reemployment. Reemployment of such claimants usually makes sense. The employee is paid anyway; it makes sense to receive services for the dollars expended. DoD components do have the authority to exempt reemployed claimants from hiring ceilings [4]. Vocational rehabilitation can also be arranged to help a worker find employment elsewhere. Once rehabilitation is complete, the claimant is expected to actively seek employment. The full cost of rehabilitation and employment services is charged to DoN; the offer of a DoN position is usually a less costly alternative. Any claimant who turns down an offer of a suitable position will have benefits terminated. Once reemployed, a worker is subject to normal personnel actions, including reduction in force (RIF). A partially disabled worker subject to a RIF will continue to receive compensation for any lost earning capacity and medical benefits to which he or she is entitled.

DoD's Civilian Personnel Management Service

The Civilian Personnel Management Service (CPMS), Injury and Unemployment Compensation Division, was established within DoD to provide operational support and training to the services in injury compensation matters. Division staff serve as the primary contact with the Department of Labor. They maintain the program database with data from weekly OWCP tapes, and they initiate the internal charge-back process. CPMS also provides regional liaisons who serve as the point of contact between the services and local OWCP offices.

In addition, CPMS has managed a reemployment program for the Air Force. The Air Force implemented its Pipeline program in 1986. Under this program, installations receive one year of funding and the over-hire authority needed to reemploy any partially disabled worker—but they are expected to move the worker to a regularly funded position within a year. About 500 positions have been funded through the program to date.

DoN program management

Responsibility for oversight of DoN's injury compensation program is left to the individual commands. An Injury Compensation Program Administrator (ICPA), usually located in a civilian personnel office, deals with day-to-day management of claims. Their duties are to process new claims, monitor past claims, coordinate with activity managers and medical officers on light-duty assignments and return to work, coordinate with safety officials on mishap investigation, and advise activities on FECA trends. Activity supervisors are responsible for ensuring safety, seeing that claims are filed promptly, returning injured workers to work promptly, maintaining awareness of FECA costs, and supporting efforts to reduce costs. There is no clear leadership for the FECA program at higher levels, although program management and costs do periodically become an issue of concern. The office of the DASN (CP/EEO) comes closest to owning the program, with responsibility for civilian personnel programs in general.

The DoN human resources program was reorganized in the mid-1990s. Regional Human Resources Service Centers (HRSCs) were

established to provide many basic services. Injury compensation was purposely not included among those regionalized services. The intention was to maintain a local face—an ICPA familiar with cases—and a sense of responsibility for cost. Over the last few years, however, there has been a parallel consolidation of local human resources offices. Whereas in the past a major installation might have had its own people working on FECA, it is now likely to be served by a consolidated office. This has allowed for staffing efficiencies and has created opportunities for greater specialization in FECA management. At the same time, it raises concern among the commands over their weakened authority, excessive staff reductions, and diminished sense of direct responsibility for cost.

Descriptive statistics on the DoN FECA program

Last year, DoN (Navy and Marine Corps) paid \$248 million in FECA compensation and related expenses. Figure 1 shows the bills from 1988 to 2002. Costs are down from a 1994 peak, but remain high considering declining employment and improving mishap rates. DoN civilian employment has dropped from 296,000 in 1992 to 185,000 in 2002. There has been a 40-percent improvement in mishap rates over the same period. DoN costs are high in comparison to other services, even after accounting for employment differences.

Figure 1. FECA bills over time, by DoD component

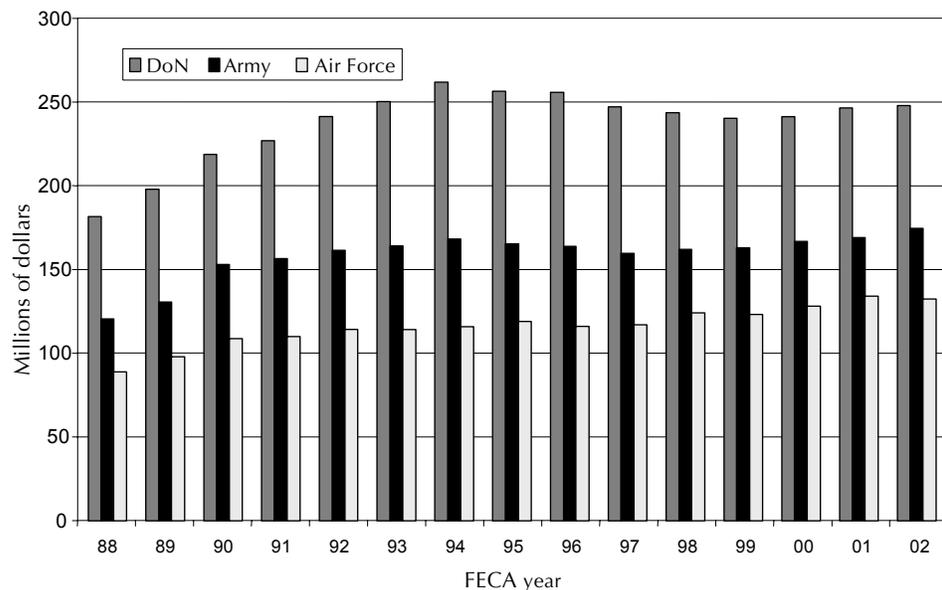


Figure 2 shows the distribution of the 2002 FECA bill by command. Most of the bill is associated with commands that have industrial activities, such as shipyards, aviation depots, and the warfare and public works centers. The NAVSEA share of the bill is declining, reflecting the BRAC closure of four shipyards.

Figure 2. DoN 2002 FECA bill, by command

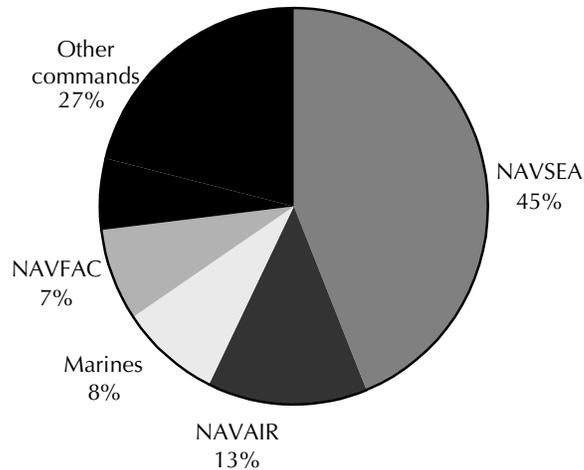
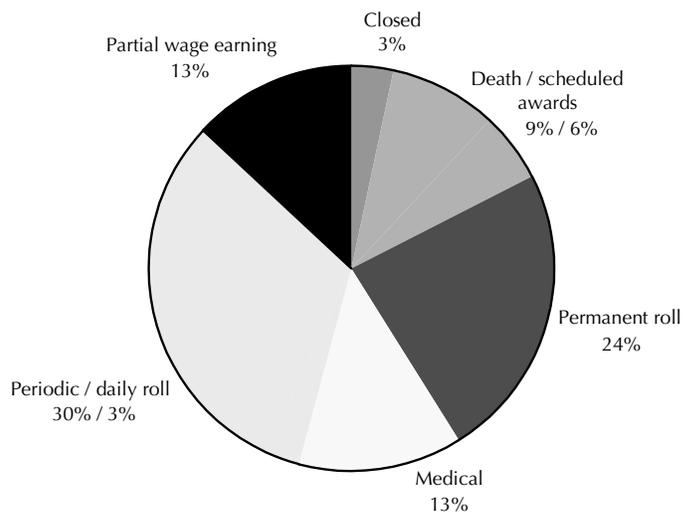


Figure 3 shows a breakdown of the FECA bill by case status. Permanent disabilities account for 24 percent of the bill. Death benefits and scheduled awards (for loss of body parts) together account for 14 percent. These are costs that are not easily managed away. The OWCP designation of permanent disability is not made without deliberation.

Figure 3. DoN 2002 FECA bill, by case status



Cases approved for medical benefits (not compensation) account for 13 percent of costs. These need watching to ensure that bills and any subsequent claims for compensation are related to the original injury. The claimants in partial wage earning status are those who have returned to work, with some disability.

The periodic and daily rolls account for a third of the FECA bill. Claimants on the daily roll are those for whom a finite period of disability is expected. Claimants on the periodic roll have indefinite, prolonged disabilities. These categories are the focus of case management. There is a potential for speeding return to work. For the periodic roll especially, these are claims that, if forgotten, can slip into extended disability from which return to work becomes unlikely.

Figure 4 shows the corresponding distribution of the cases by status. Many cases close promptly (most within the 45-day COP period). Only a relatively small number of claimants are receiving long-term compensation on the periodic or permanent rolls, but these few cases do account for the bulk of program costs.

Figure 4. DoN cases in 2002, by case status

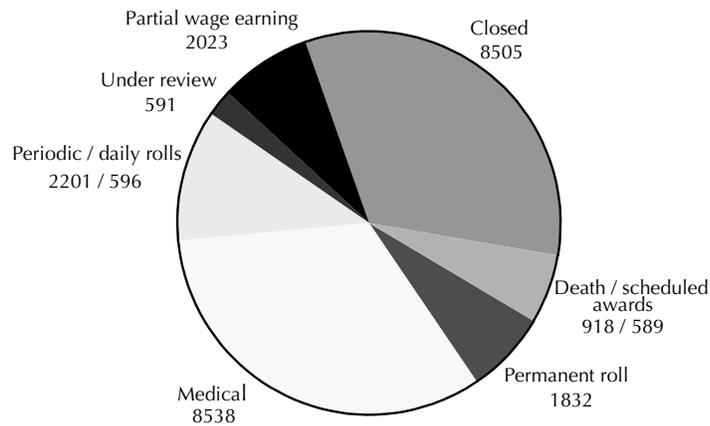
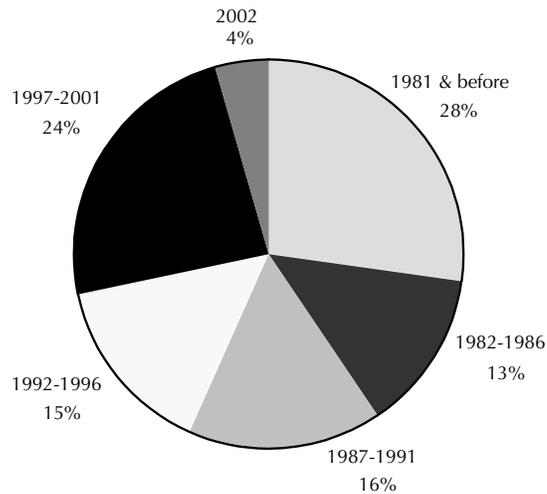


Figure 5 is a breakdown of the 2002 FECA bill by date of claim. Older cases are very much an issue. Over 70 percent of the bill is for cases that have been on the books for at least 7 years (1996 or earlier). It is the persistence of older cases that explains why it has been so hard to bring down program costs.

Figure 5. DoN 2002 FECA bill, by date of claim



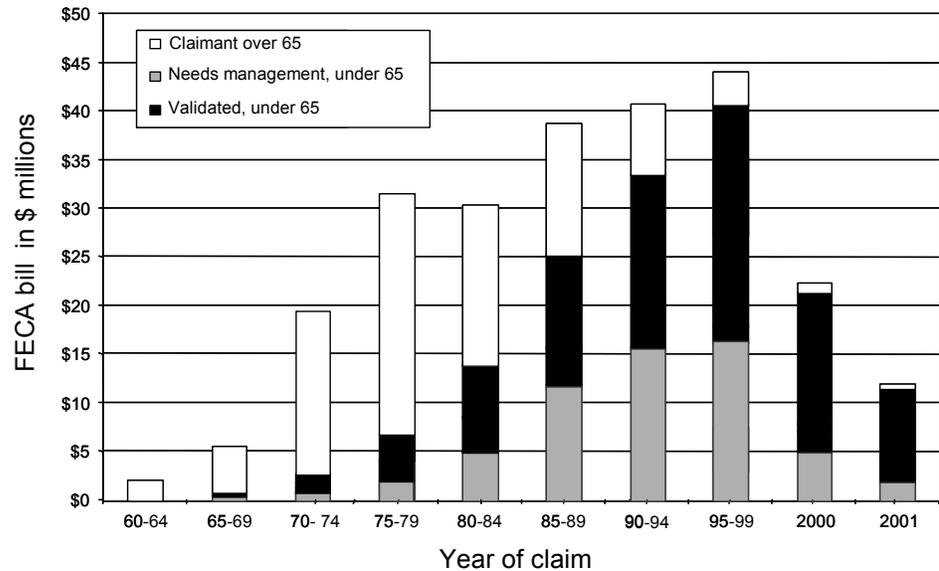
Finally, with aging of claims there has been a corresponding aging of claimants on long-term rolls. This has growing implications for the ability to manage costs. Not much can be done once a claimant passes retirement age, and more than 37 percent of the bill now goes to claimants over 65. Figure 6 is a breakdown of the FECA bill by date of claim. Areas shown in white represent costs attributable to claimants over 65. Below that are broken out the remaining costs, by claim status. We use “needs management” to represent the periodic and daily rolls, while “validated” represents the permanent roll, death benefits, scheduled awards, and medical coverage. Although not apparent in the figure, the bulk of the money attributable to claimants over 65 is for death benefits and permanent disabilities. Nonetheless, about 20 percent of claimants on the periodic roll are now over 65.

Recent negative trends in the FECA program

The effectiveness of DoN FECA programs has been in decline since 1999. This reverses what had been a period of success in case management. The management of both new and older claims seems to have suffered (see table 3 and figure 7). Evidence of the decline in effectiveness is as follows:

- The percentage of cases removed from the periodic rolls annually is at roughly half the 1999 level.

Figure 6. DoN FECA bill, by date of claim, case status, and claimant age



- Growth in the number of claimants returned to partial wage earning status has essentially stalled.
- The percentage of new claims reported closed within the first year is at the lowest level of a decade.
- For each new claim, the average amount paid out over 2 years has jumped 35 percent.

There are a number of possible explanations for declining effectiveness in the FECA program:

- *Disincentives to reemploy injured workers.* Activities are increasingly reluctant to return injured workers to duty. Reemployment efforts add to overhead payroll costs while lowering average productivity. Current accounting practices do not encourage the activities to appropriately balance these employment costs against their FECA bill
- *Base closures, realignments, and regionalization.* Base closures and reorganizations have resulted in a churning in ownership and responsibility for claims that interfere with consistent case management. As a group, those claims that have not had consistent ownership are among the most costly.

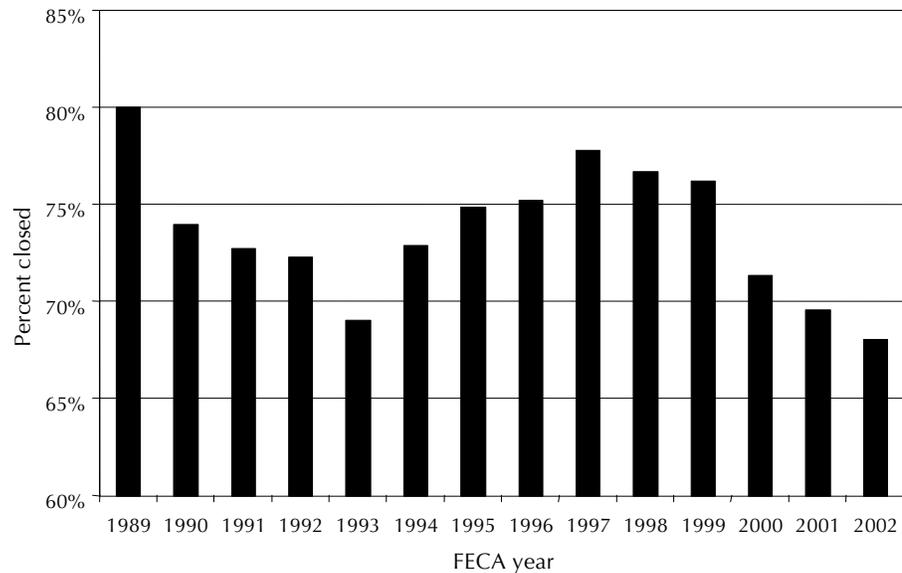
Table 3. Negative trends in DoN FECA case management

| | FECA years | | | |
|---|------------|---------|---------|---------|
| | 1998-99 | 1999-00 | 2000-01 | 2001-02 |
| Cost per claim, first 2 years | \$2,900 | \$3,100 | \$3,800 | \$3,900 |
| Reductions in the periodic roll ^{a,b} | 9.4% | 10.0% | 8.7% | 5.6% |
| Increase in partial wage earning cases ^b | 10.1% | 4.1% | 5.2% | 0.4% |

a. We exclude claims moved to the permanent roll.

b. The measures are based on 10 recent years of claims to reflect cases that are most manageable.

Figure 7. Percentage of cases closed in the first year, by FECA year



- *Reorganization of human resource offices.* Consolidation and staff reductions within civilian personnel offices (CPO) handling FECA claims may have left some programs with less than sufficient staff to aggressively address claims.
- *Exhaustion of opportunities.* Many programs did screen their long-term rolls in the late 1990s. This has led to substantial reductions in the number of cases on the periodic rolls. For some, the possibility of further success in long-term case management may now be limited.
- *External factors.* OWCP has increased its emphasis on early intervention and vocational rehabilitation. These programs can

add significantly to current expenses, but may not yet have shown offsetting returns. Furthermore, OWCP has made it increasingly difficult for an agency to talk with a claimant's doctor.

These explanations were suggested to us in discussions held with various FECA programs. Specific explanations for decline seem not to be consistent across programs. What we find troubling is a general lack of awareness of the extent to which performance is declining. This is a program with such problems that we must point to the failure of central oversight as the true explanation for high costs.

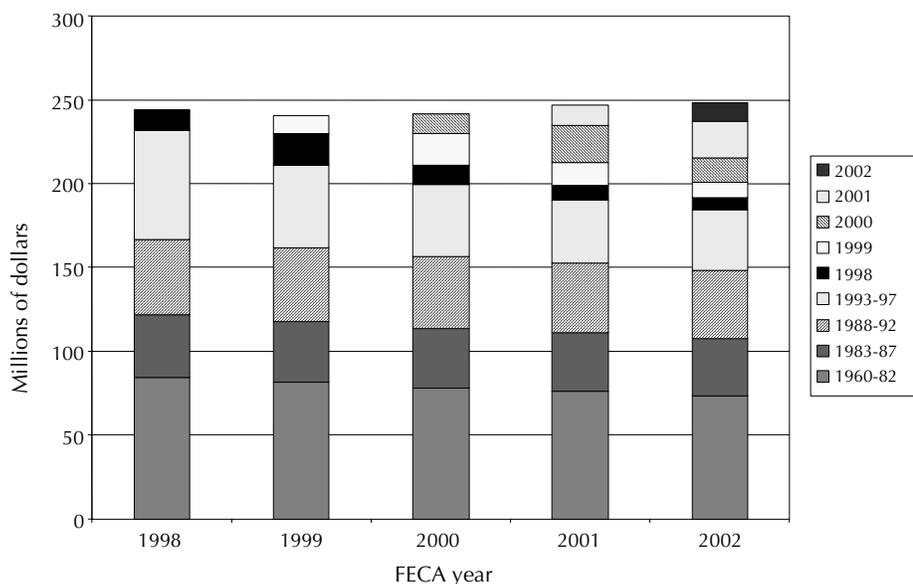
Methods and baseline projections

In this section, we describe our approach to projecting future FECA liabilities and potential savings. We provide a baseline projection of future FECA costs. We expand on the discussion of negative trends to show the cost associated with the recent decline in case management.

Method for projecting future FECA liabilities

We use an actuarial model to project future payments and potential savings. Projections are made into future years using an approach referred to as a paid-loss extrapolation method. It is a simple and generally reliable method. To illustrate the basis of our predictions, we refer to figure 8.

Figure 8. DoN FECA bills, showing amounts paid by date of claim

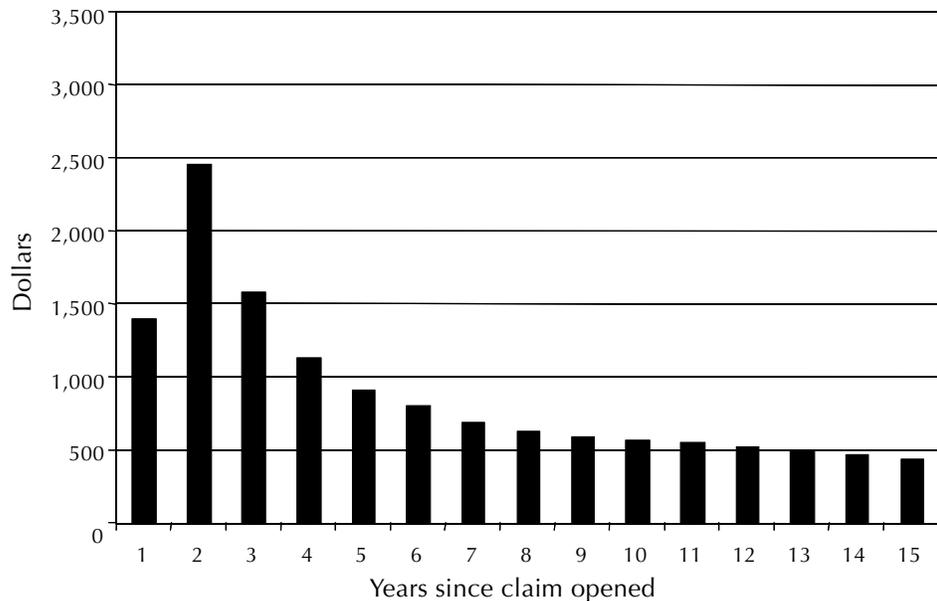


Changes in the overall FECA bill tell little about the success of a program because of confounding effects of changing employment levels and mishap rates. Instead, we focus on the individual components of

the FECA bill. Each year's bill is broken down by date of claim. To explain, consider the 2002 bill. The top block represents the 2002 bill for new claims opened that year. The next block down represents the 2002 bill on claims opened in 2001. Notice that you can follow the life-cycle costs of a particular cohort (cases opened in a particular year) by looking at blocks with the same shading and that these costs follow a fairly predictable pattern over time.

Figure 9 shows the typical pattern of life-cycle costs for the average claim. Costs are highest in the second year when medical expenses peak,⁸ decline noticeably for 4 or 5 years as many cases are resolved, and then settle in for a long tail of slowly declining payout to the few remaining claimants with long-term disabilities. These later payments decline because of occasional recovery, reemployment, or death. We emphasize that the probability of a case being resolved, whether through management or otherwise, is built in to the life-cycle costs. If the values seem low, remember that many claims close without compensation.

Figure 9. Payout over the life cycle of an average claim



⁸ Further, consider that the first year is effectively 6 months long because a claim may open on any day until the end of the year.

The pattern of life-cycle costs provides the basis for estimating how future program costs might evolve. For example, in 2003 we might expect costs attributable to 2002 claims to rise to 1.75 times their cost in 2002. Similarly, the bill for the 2001 cases will be about 65 percent of what was paid in 2002. We can predict the entire 2003 bill in this manner. (We will assume that new claims are constant at 2002 levels.) With the 2003 bill, we can then forecast the 2004 bill. It is a simple approach, but one that has the virtue of capturing the various aspects of case management. Further, it allows us to make comparisons across programs and to evaluate alternative approaches to management. We can do so by using an alternative pattern of life-cycle costs.

The model does have some negative aspects that limit its accuracy for long-term predictions:

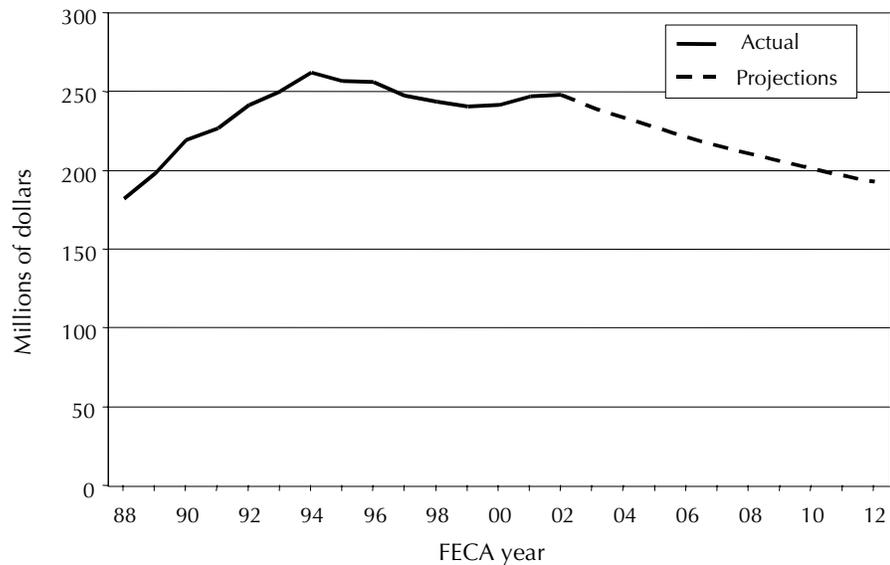
- Past performance is no guarantee of future performance.
- The extrapolation model works best with large populations. Smaller activities demonstrate too much volatility.
- The model does not explicitly consider such factors as age of claimant or nature of injury.
- The model is sensitive to assumptions on cost of living and medical inflation adjustments that are needed to restate historical payments to constant dollars.

At a practical level, it is essential to work with a consistent set of older claims. This actually proves to be something of a data challenge when evaluating individual DoN commands and personnel offices because of the shuffling of responsibility for claims in recent years.

Baseline projections

In figure 10, we present our baseline projections of the future DoN FECA bill. In this figure, projections are in constant 2002 dollars; past values are in the current year dollars. If we account for expected inflation, baseline projections are essentially flat, drifting down for 3 years and then gradually rising back to current levels.

Figure 10. DoN FECA bill projections^a



a. Projections are in 2002 dollars; prior values are in current-year dollars

The cost of recent declines in FECA management

While a declining FECA bill (relative to inflation) might seem to indicate an improving program, the decline is really just the inevitable result of a 50-percent reduction in the civilian workforce and improved mishap rates in the 1990s. In fact, the potential for a more significant decline in the FECA bill has already been lost.

Table 4 gives a breakdown of past and projected FECA bills, by date of claim. The shaded area tracks the progression of the smaller workforce as it gradually comes to dominate the FECA bill. Notice, for example, the steep reduction in payments that occurred between 1999 and 1994 for claims opened 1 to 5 years earlier. That smaller cohort, as it ages, is the primary reason for a declining bill.

Table 4. Actual and projected FECA bills, by date of claim (\$ millions)

| | Date of claim (years before current) | | | | | | Total |
|------|--------------------------------------|------|------|-------|-------|------|-------|
| | Current | 1-5 | 6-10 | 11-15 | 16-20 | 21+ | |
| 1994 | 14.3 | 90.9 | 49.8 | 34.4 | 36 | 35.6 | 260.9 |
| 1999 | 7.4 | 54.6 | 45.6 | 40.6 | 29.2 | 62.7 | 240.3 |
| 2004 | 11.1 | 56.8 | 29.5 | 36.9 | 34.1 | 65.0 | 233.4 |
| 2009 | 11.1 | 54.7 | 25.3 | 22.8 | 29.6 | 62.4 | 205.9 |

With recent problems, gains that were once expected have been lost. Since our previous study, the expected life-cycle cost of each new claim has risen by 50 percent. This corresponds to an average \$10.5-million increase in the future annual FECA bills. Not only did DoN sacrifice the savings we thought were possible from broader implementation of best practices, it took a path that may add \$105 million to the cumulative FECA bill over the decade.

Figure 11 shows the life-cycle costs per claim, comparing expected annual payouts per claim in 1999 and 2002. Notice that current problems arise largely in the first 2 years of case management. After that, costs per claim come down proportionately over time, much the same as in 1999.

Figure 11. Change in the life-cycle cost per claim since 1999

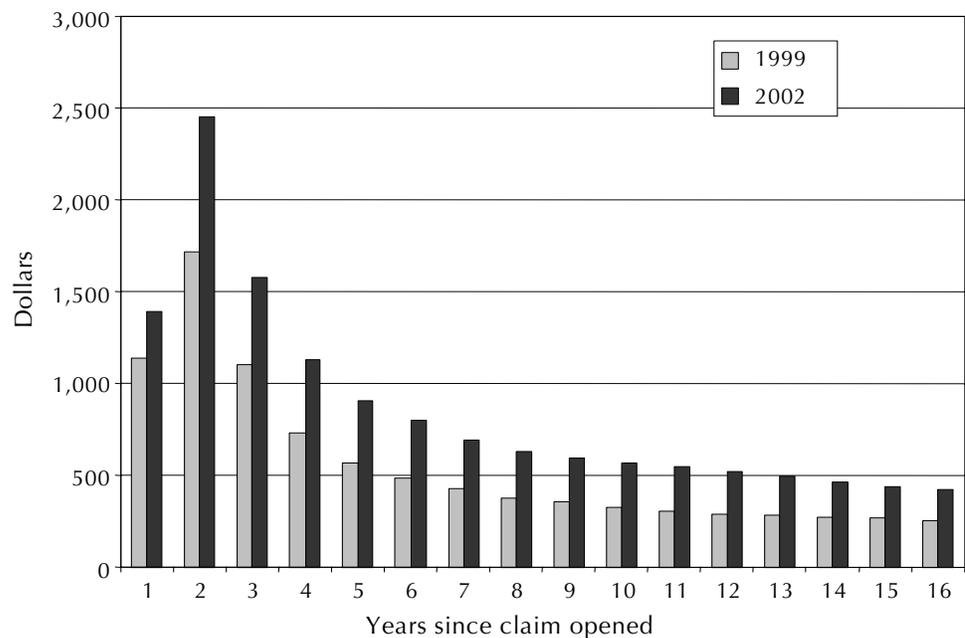


Table 4 also gives a sense of just how hard it is to turn program costs around without addressing older cases. Even dramatic reductions in current claim costs did not lead to a quick reduction in the FECA bill. However, as the older cohorts representing the large workforces of the 1970s and 1980s are gradually replaced, the relative importance of mishap prevention and newer claims management will increase.

The payoff to FECA case management

Our goal was to look for successful FECA programs and to determine the savings that might result if the Department of the Navy as a whole could match their success in case management. In our previous study, we considered two widely applauded programs as benchmarks. This time, in order to establish a more robust and attainable benchmark, we searched for the “best 20 percent” of DoN programs. The programs selected actually represent about 22 percent of the current FECA bill. They were chosen by searching for a combination that would produce the greatest Navy-wide savings. At the same time, we established a lower end, a group representing about 23 percent of the FECA bill that we refer as the “worst 20 percent.”⁹

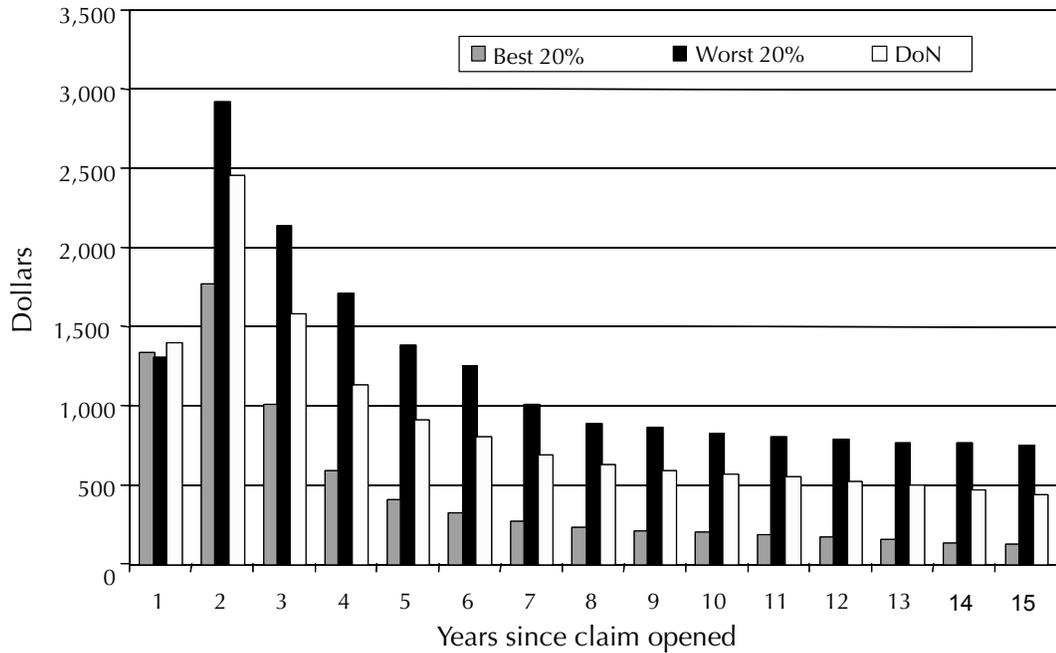
Comparisons of life-cycle costs

The differences among programs are made clear by a comparison of overall life-cycle costs. Figure 12 compares the best programs, with the worst, and with DoN as a whole. The figure shows expected payments over time for an average claim. A disadvantage to our current approach is that we know little about the specific management practices of the many programs included in our benchmark. The explanation for their success, however, is made apparent in this figure.

What distinguishes the best programs is their ability to contain costs in the first few years of the claim. Such success relies on transitional jobs for recovering workers and return-to-work programs. It is programs that are strongly committed to getting people back to work quickly, such as Portsmouth Naval Shipyard, that achieve savings. Although less apparent in the figure, the best programs also show steady success in addressing their long-term rolls.

⁹ However, we found that rankings of individual programs could vary widely, depending on criteria used.

Figure 12. Comparing life-cycle costs, DoN and the benchmark programs



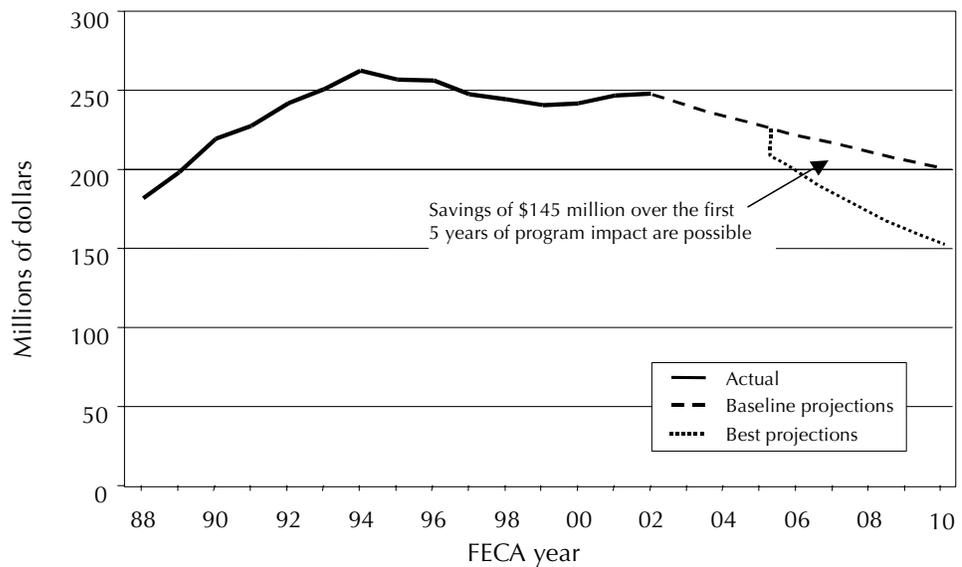
In terms of overall liabilities, DoN can expect to spend twice as much on the average claim (\$16,500) as the best programs (\$8,000). The worst programs will spend three times as much (\$24,500).

What are the potential savings?

To give a more concrete sense of the differences in program performance, we project FECA bills over time. We look at the potential Navy-wide savings that might result from applying best management practices on a broader scale. Figure 13 shows the savings from the rest of DoN (including the Marine Corps) matching the success of the best programs. It is assumed that implementation begins in 2004, with the first effects observed a year later.

Despite a declining FECA bill, past success in case management, and aging of claims, the potential for savings is large. Savings of \$145 million over 5 years are possible. Achieving such savings will require attention to older case management and strong support from activities and commands for light-duty and return-to-work programs.

Figure 13. DoN savings from matching current best management



Are the savings from older or newer case management?

The potential savings come from effective management of both new and the older claims. Our projections provide us with details on savings by cohort. Considering claims opened in 2000 or earlier to represent older claims, some \$50 million in savings can be attributed to older claims management. The remainder of \$95 million we attribute to aggressive attention to newer claims.

Savings by region and command

In tables 5, we break down savings by command and geographical region. The table gives potential savings, allocated between older and newer case management. In addition, the table gives overall FECA costs, number of cases on periodic roll, and an estimated life-cycle cost per claim. These regions do not correspond to the regional shore commands. Rather, we have included all civilian personnel office within a geographical area, whether or not they are under the regional command. California and southwest, for example, includes Marine Corps and NAVSEA facilities that are not managed by Navy Region Southwest. We did exclude the BRAC shipyards from regional totals because of the clearly distinct management of their program.

Table 5. Breakdown of savings by command and geographical region

| | FECA bill (\$ million) | Periodic roll cases | Life-cycle cost (\$) | Savings (\$ million) | |
|---------------------------|---------------------------|------------------------|-------------------------|----------------------|--------------|
| | | | | New cases | Old cases |
| Command | | | | | |
| NAVSEA | 110.6 | 903 | 12,970 | 17.3 | 7.3 |
| NAVAIR | 33.7 | 289 | 19,950 | 15.9 | 3.6 |
| Marines | 21.0 | 229 | 13,780 | 10.6 | 2.7 |
| NAVFAC | 18.6 | 148 | 19,290 | 6.5 | 3.7 |
| PACFLT | 14.7 | 100 | 16,970 | 14.7 | 1.9 |
| Sealift Command | 10.1 | 133 | 15,830 | 2.3 | 4.1 |
| LANTFLT | 7.5 | 84 | 8,380 | 2.1 | 0.6 |
| BUMED | 6.2 | 67 | 9,350 | 2.5 | 0.8 |
| CNET | 4.4 | 38 | 19,450 | 1.2 | 1.0 |
| NAVSUP | 4.0 | 36 | 8,570 | 0.3 | 0.2 |
| Geographical region | | | | | |
| California & southwest | 55.1 | 430 | 19,743 | 35.7 | 9.8 |
| South & south central | 33.4 | 347 | 14,337 | 13.8 | 5.3 |
| Capital area | 26.5 | 262 | 9,487 | 4.1 | 4.5 |
| Northwest & Alaska | 25.7 | 165 | 12,462 | 16.3 | 0 |
| Norfolk area | 23.7 | 345 | 10,344 | 6.8 | 4.9 |
| Northeast & north central | 20.9 | 215 | 13,241 | 2.0 | 2.3 |
| Hawaii | 9.9 | 36 | 11,274 | 2.2 | 3.4 |

Cost of lack of consistency in case management

Total savings in table 5 do not add up to the savings predicted for DoN. One reason, of course, is that the tables are not complete. We have left out smaller commands, BRAC shipyards, and a number of claims not easily identified by region or current command. There is a more significant issue here, however. In calculating disaggregated savings, we considered only cases under consistent ownership and management during 1999 to 2002. To do otherwise would have unfairly attributed cases to a region or command that might have had little to do with the case management.

About 9 percent of claims have not had consistent case management over this time period. This is a result of base closures, realignments, and regionalization. The churning of responsibility for claims has interfered with consistent case management. As a result, these claims

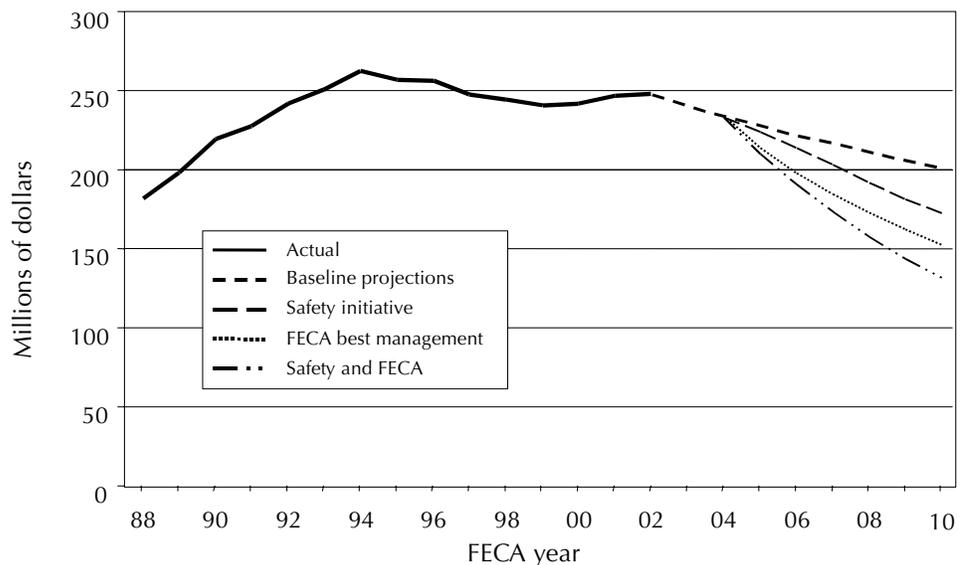
are among the most costly. Our estimate of overall DoN savings reflects the current management of all claims. The disaggregate estimates reflect only the more consistently managed claims, and savings are measured against a baseline that reflect this consistent management applied to all current and future claims. The difference between the two estimates, about \$35 million over 5 years, is a measure of the cost of churning responsibility for claims.

Potential impact of safety initiatives

One final question of interest to us was the possible impact of future safety initiatives on potential FECA savings. There is a goal to bring down mishap rates by 50 percent over 5 years. Clearly, this would result in lowering the FECA bill. It is somewhat less clear how the initiative might affect the potential for savings described above.

In figure 14, we show the projected savings with the safety initiative alone, with best FECA management, and with a combination of both efforts. It is assumed that the safety initiative takes effect in 2004 and results in a 10-percent decline in first-year claim costs in that year and each of the following 4 years. Savings from the safety initiative are \$72 million in cumulative reductions in the FECA bill over 5 years. The combined savings from both would be \$210 million, just a little less than the sum of the savings predicted for each initiative alone.

Figure 14. Comparing safety initiatives and improved FECA management



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