INTRODUCTION

There is a compelling case for major change to the WSIB's classification and pricing system. Broadly, this case for change is based on the need for a simpler, fairer solution that shares the costs of the system fairly across all participants, and responds to the changing nature of work in Ontario.

BACKGROUND

Under the current system, Schedule 1 employers are grouped based on business activity – using a Standard Industry Classification (SIC) system that reflects the North American economy of the 1980's – and they pay premiums based on the principle of collective liability. The WSIB's pricing system implicitly assumes that business activity is an accurate indicator of expected claims costs. Accordingly, employers engaged in similar business activities are classified in the same premium "rate group."

Schedule 1 employers are divided into nine industry classes. Employers within each class are then subdivided into rate groups. The grouping of employers within a single rate group is based on similarity of business activities. Rate groups are further divided into classification units (CUs). CUs are used as a means of tracking the relative experience of various employer subgroups. Firms in a classification unit share similar business activities other characteristics. The pooled experience of the CUs in a rate group is used to calculate the premium rate for that rate group.

Premium rates are not calculated for CUs. All employers within a single rate group, no matter which CU they belong to or their payroll size, are charged the same premium rate (before any experience rating).

In principle, the classification system was designed to automatically monitor the relative risk of individual CUs so that if the accident costs of a particular CU diverged from the rate group average, it would be flagged and potentially moved to another rate group that is more reflective of its current risk. However, in practice, notifications of such anomalous CUs rarely occurs and when a CU is relocated, this is only done through a labourious manual process.

In practice, most classification changes initiated by the WSIB are rate group consolidations that are primarily due to individual rate groups becoming statistically non-credible. This happens when the number of employers and/or the number of claims in a rate group drop below the level where they provide an appropriate basis for premium rate setting. In the small number of cases where CUs are considered for re-assignment, it is usually with a general view to reduce WSIB costs to the industry more so than because of statistical justification or demonstrated and verified movement in risk.

Since the WSIB's pricing system is underpinned by the classification scheme, the lack of precision in classification produces premium rates that result in significant cross-subsidization among employers within rate groups given the much weaker link between business activity and risk that exists at present compared to the Ontario of the late 1980s. The WSIB's continued reliance on the current classification system serves only to perpetuate an increasingly ineffective method of assigning employers by outdated SIC-based business activities.

INEFFICIENCIES IN CLASSIFICATION AND PRICING

The following discussion highlights the challenges associated with a classification model that is becoming increasingly outdated and cumbersome. This classification system also contributes to concerns in the setting of premium rates, since it underpins the pricing model.

Changes in Industry Mix

Class D, Manufacturing, by far the largest WSIB industry sector, has been radically transformed in the last twenty years. To compete in the global economy today, companies have to be more flexible in terms of production processes and end products, often taking large orders from clients ranging from motor vehicle manufacturers to large home retail outlets, necessitating a switch in production from, say, brake pads to barbeque grills.

Example - Informal Consolidation of Rate Groups for Rate Setting

Under the SIC, there are unique business activities classified under RG 361: Non-ferrous Metals, RG 390: Other Stamped and Pressed Metal Products, RG 419: Motor Vehicle Assembly, RG 421: Other Motor Vehicle Parts and Equipment, RG 424: Motor Vehicle Stampings, and RG 425: Motor Vehicle Wheels and Brakes.

These rate groups still appear individually, but they are effectively a single rate group. They started off with unique premium rates, but over time, the WSIB realized there was significant overlap in business activities. All of these rate groups now have their accident experience pooled.

Cross Subsidization

Over time, rate group mergers have increased the range of cost experience among the CUs in affected rate groups. This leads to a number of undesirable consequences – creating a disincentive among employers to invest in workplace safety, encouraging price shopping, and stimulating appeals for re-classification. As noted above, with classification underpinning the rate setting process combined with the broad range of cost experience in a CU and rate group, employers that would drive higher claims costs would be subsidized by those employers within the same rate group that have lower claims costs.

Example - UFL Apportionment

The UFL represents the unfunded costs of past claims, but the component of the premium rate to pay for the UFL is determined based on rate groups' new claims costs. In a sense, this approach could mean new employers are paying for past employers' costs – because a rate group's new claims cost may not correspond to the costs it generated in the past.

Example - Construction Sector Relief

In 1999, the funding ratio for Class G: Construction stood at an untenable 16% compared to the Schedule 1 average of 50%. In response, the WSIB Board of Directors accepted a funding proposal to offer support to the construction industry by transferring the Class level UFL, to Schedule 1.

Example - Volunteer Firefighters (VFF)

When coverage for VFFs was reflected in the 2011 premium rate, the associated costs would have represented too great a burden for the affected rate group. Costs were therefore introduced to the rate group on a gradual basis, with the remainder shared across all rate groups in Class H.

Example - Claim Limit in Rate Setting

Though not necessarily material or frequent, there is a claim cost limit in the rate setting process. This is to counter the effect of many large claims coming into the system due to catastrophic workplace incidents. Beyond the limit, costs can be shared across all rate groups in the Class.

Rate Shopping Among Employers

There is a strong financial incentive for employers to be classified in a rate group with the lowest possible premium rate. Given the current overlap of business activities across rate groups, there is a strong incentive for newly registered employers and existing employers to request re-classification.

While the WSIB's Employer Services Centre and Employer Audit areas can identify incorrectly classified employers, by far the largest volume of re-classification requests are generated by employers , often with external professionals making requests or appeals on their behalf. As a result, and since there is no standard approach for this process, employers who do not have access to external professionals, or who do not engage in proactive activities seeking the lowest premium rate, are unfairly subsidizing the ones who actively seek to reduce their premium rate to their competitive advantage and potentially exploiting weaknesses in the current system.

At the same time, the complexity of the current classification scheme and the supporting Employer Classification Manual can lead to inconsistent interpretation and application. This is because many CU definitions could reasonably be considered to include multiple and overlapping business activities, and create confusion for employers with multiple business activities.

Example - Pharmacists

The supply of pharmacists is not specifically referenced in the Employer Classification Manual (ECM), leading to an inconsistent classification of the business activity by WSIB operating areas. The proper classification of the supply of pharmacists was initially raised at the Classification Review Group in 2007 but there was no resolution. WSIB Employer Audit

Services (EAS) has reviewed the classification of 14 employers belonging to a group of firms audited in 2009 and 2010 along with several non-audited firms that supply pharmacists. These firms were inconsistently classified in the three following CUs (shown with their 2012 premium rates):

- CU 8634-000- Nursing and other Health Care Operations (RG 857-01, $3.23)
- CU 7712-001- Supply of Non-Clerical Labour (RG 929-01, $4.93)
- CU 7711-001-Supply of Clerical Labour (RG 956-45, $0.21)

Example - Window Cleaning – Above Ground and Ground Level

Above ground window cleaning is classified under RG 748 with a premium rate of $18.31. The scope of business activities for above-ground window cleaning includes all window cleaning activities, both interior and exterior, which require the use of climbing devices of any kind. Such devices include extension ladders, scaffolds, stepladders, stools, swing stages, and similar devices.

Ground level window cleaning is classified under RG 923 with a premium rate of $3.73. The scope of business activities for ground level window cleaning includes all window cleaning activities, both interior and exterior, which *do not* require climbing devices of any kind.

In general, ground level window cleaning is part of a janitorial contract, but if the business uses any of the devices in the scope for above ground window cleaning, even if it is just a stool, the activity will fall into the above ground window cleaning classification.

Increasing Divergence between Business Activity and Risk

While the current classification system classifies by business activity, and not by process, the link between business activity and risk has increased as employers within a rate group adopt new technologies and production processes over different periods. In the past, when most business activities had relatively uniform processes, there was a more consistent risk profile for employers in the rate groups.

Example - Laser Cutting

Employers who were the first in their rate group to acquire new automated processes, such as computer-guided laser cutting, would continue to pay the same premium as their competitors whose workers continued to use hand-held jigsaws.

Experience rating programs should help to offset some of the differences in claims costs, but almost half of the employer accounts (approximately 110K) are not in any experience rating program. Also, while these programs reward the safer employers, they are not sufficiently timely and responsive to changes in risk.

Lack of Transparency

There is no formal process for reassigning CUs to different rate groups to reflect changes in risk. Currently, there is significant discretion for re-classification within the WSIB – unlike, for example, WorkSafeBC, where there are clearly defined parameters that support the re-classification of business activities.

Under the BC system, if a unique business activity shows a deviation of risk from the average risk of the larger group, it is automatically moved. This is often not the case in the WSIB system, even when a CU is believed to have a different risk profile.

Example - Trim Carpentry

The WSIB has been approached by industry representatives to move the trim carpentry business activity (CU 4274-000, Finish Carpentry) from RG 764 Homebuilding to RG 719 Inside Finishing. The 2013 premiums for these rate groups are, respectively, $9.10 and $7.51.

The industry has argued that, in the past, trim carpenters worked both inside and outside, installing trim and molding to new houses under construction. Over the last ten years, the work has evolved to the point where it is exclusively inside finishing, meaning workers may be exposed to lower risk.

More Rate Groups Becoming Statistically Non-Credible

When the classification system was introduced, there were more than 200,000 lost time injuries (LTIs) generated by Schedule 1 employers. This number has dropped to approximately 80,000, as automation, effective prevention programs and the structural decline of relatively risky industries all contributed to reducing the number of workplace injuries.

Since statistical credibility is measured to a large degree by the number of LTIs, rate group mergers have become the standard option to maintain credibility. The current classification system, which started with more than 220 rate groups, has seen a significant contraction over time, down to 155 today. The main reason for the reduction is that, as individual rate groups become statistically non-credible, they are amalgamated so that premium rates can be calculated.

Because the outdated SIC is still being used, forced rate group mergers often result in new rate groups that include business activities that have little in common. This causes confusion among employers and increases their skepticism regarding the fairness of premium rates.

Special Operations

Under the Ontario Regulation 175/98, Special Operations include the following activities: large bridge construction, millwright and rigging work, wrecking and structural demolition, structural steel erection, form work (high-rise), and steel reinforcing. These operations are always a business activity in their own right and classified separately from the remainder of the employer's business activity.

Under the regulation, firms are eligible for multiple rates, and there is a requirement to maintain a properly segregated payroll record. In the absence of such a record, the highest rate is applied. This rule, however, is not applicable to small employers (i.e., firms whose total payroll is less than five times the maximum insurable earnings).

Special Operations must first be classified separately before the remainder of any contract is classified. Where the Special Operations activity accounts for less than 10% of the total direct insurable earnings for the entire contract, and is considered by the WSIB to be integral to the main activity of the contract, it is not classified separately but instead is classified as part of the contract.

Example

An HVAC contractor under RG 707 takes the contract to supply and installs an HVAC system on a high-rise building, requiring the unit to be hoisted to the top of the building.

The hoisting of the unit falls under RG 737 Millwright and Rigging Work at a higher rate. If the labour portion of the contract was less than 10% of the contract, then it would be considered as part of the contract under RG 707, but if it is more than 10% it would have to be separately rated. This adds a significant amount of complexity for the WSIB staff who must make the appropriate classification decision.

Technological Change

When the SIC was developed in the late 1980's, no one anticipated the way new technologies and services would radically transform the Ontario economy. Automation, for example, has resulted in much safer work environments, which has a direct impact on a pricing system whose statistical credibility is based on a measure of lost time injuries.

Additionally, the SIC did not anticipate the internet or any of its related activities such as electronic retailing, VOIP communication services, telephone re-sellers, etc.

Example - Telecommunications

Technological change has made RG 983-05, Telecommunication Carriers, increasingly outdated. The SIC definition at the time referred to telephone type services, so the classification was originally intended for telephone and telegraph companies. With new technology, the rate group has been revised to include internet companies, telephone re-sellers (e.g., Primus), VOIP, etc.

Little analysis has been done as to whether the risk of these new activities is similar to the original activities. Under other classification systems, services such as internet, VOIP, etc., have a unique classification, different from telephone companies.

Example - Solar Energy

Another industry that did not exist under the SIC was solar power. Solar panels are a relatively new technology and were not in the original classification system. They are currently in two rate groups, RG 704, Electrical and Incidental Construction Services with a 2013 premium of $3.60 and RG 707, Mechanical and Sheet Metal Work at $4.06, depending on whether the solar panels are for electricity or for heating.

The classification was based entirely on business activity, with no consideration of the actual risk involved for the two types of solar energy activities. In NAICS, for example, there is a unique classification for solar panels, 237130 (Alternative Energy).

WSIAT Decisions

Some recent Workplace Safety and Insurance Appeals Tribunal (WSIAT) decisions re-classified employers on the basis of risk rather than business activity. While the WSIAT uses a “best fit” rule in their classification decisions, they do not appear consistently support the business activity classification system used by the WSIB. WSIAT decisions highlight inconsistencies when process overrides business activities because employers with the same business activity would potentially be classified into different rate groups.

CONCLUSION

Over the last twenty years, the North American economy in general, and the Ontario economy in particular, has experienced significant changes – in both employment and industry mix. These changes have been brought about by such factors as free trade, technological change, appreciation of the Canadian currency. As a result, the current WSIB classification system has become hopelessly outdated, with classification changes being done on a reactive, *ad hoc* and infrequent basis.

This situation has resulted in a classification and pricing system that is inefficient, unfair, and which fails to recognize the true nature of work in Ontario in 2013 and beyond.