



**Missouri Employers Mutual**

# **Breaking Down Work Comp Premium**

*Understand How it Can Add Up to Savings*

**For more information:**



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**MEM**  
Missouri Employers Mutual

*These recommendations were developed from national standards and sources believed to be reliable, however, no guarantee is made as to the sufficiency of the information contained in the material and Missouri Employers Mutual Insurance Company assumes no liability for its use. Advice about specific situations should be obtained from a professional.*

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# Introduction

Insurance decision makers like you want to know:

*“How is my workers compensation premium determined?”*

You’re understandably curious about how insurance companies arrive at the number on your bill. It’s also important for you to understand the factors that influence your premium, so you can begin taking steps to control costs.

Calculating your work comp premium can be complex, but it doesn’t have to be a mystery. Work comp carriers estimate and audit your premium based on your company’s:

- Payroll
- Classification Rate
- Experience Modification Factor (E-mod)

The formula is rather simple:

## A SIMPLE FORMULA

### Work Comp Premium Calculation

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**Payroll** x **Classification Rate** (per \$100 of payroll) x **E-mod** = **Premium**

*This simple formula is the basis for work comp premium, but there are numerous other factors that determine your final premium.*

# I. Payroll

Payroll is the basis for establishing your work comp premium. For every \$100 of payroll, companies charge a specific rate based on the type of work your employees complete.

Payroll is the basis for premium because in work comp, there are two benefits:

- **Medical:** the costs associated with treating an injury. These are not unique to your business, employees or industry.
- **Indemnity:** the amount paid to an injured employee in place of wages while he's off work. Indemnity benefits, or replacement wages, are unique to your business because they're calculated based on an injured employee's wages before he got hurt.

It stands to reason, then, that as payroll in your business rises, work comp premium could go up, as well.

Work comp policies are often issued with estimated payroll figures for the policy period. At the end of the period, a premium audit may be performed to determine the actual payroll. The difference between the audited and estimated premium will be billed or returned.

## A SIMPLE FORMULA

### Work Comp Premium Calculation

$$\textcircled{1} \text{ Payroll} \times \textcircled{2} \text{ Classification Rate (per \$100 of payroll)} \times \textcircled{3} \text{ E-mod} = \text{Premium}$$

## 2. Classification Rate

Payroll is multiplied by the base rate for each classification code in your business. Base rates are unique to each state, industry and carrier. To determine base rates, carriers in most states, including Missouri, reference an actuarial calculation provided by the National Council on Compensation Insurance, a work comp rating and data collection organization. NCCI has more than 600 classification codes for the work in your business to help ensure you pay the appropriate price for your level of risk.

MEM considers NCCI's rate indication, but more heavily weighs our own experience when setting base rates. With more than 14,000 policyholders and 20 percent of the Missouri work comp market, our loss experience reliably indicates what's happening with our policyholders and in Missouri.

### Classification Codes

Some types of work are naturally at a higher risk for workplace injuries. Your premium is based, in part, on the risk associated with the work completed in your type of business. For example, the lowest rate is typically given to clerical work, whereas a higher rate is assigned to riskier jobs, such as construction.

The tricky part in evaluating risk is that there are variations within an industry. Some industries generally classified as high-risk include staff that perform low-risk functions. For example, a roofing company may have a total of 12 employees, but only four of these are actually in the field climbing roofs. The other eight employees remain in the office performing low-risk tasks, such as sales and service. These factors are taken into account by using different classification codes for each type of work.

Avoid misclassifying high-risk employees as low risk to control your premium. This will be revealed during a premium audit and you'll end up paying the difference in premium. Review your classifications regularly to ensure ongoing accuracy.

### A SIMPLE FORMULA

## Work Comp Premium Calculation

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**Payroll** x

②

**Classification Rate**

(per \$100 of payroll) x

③

**E-mod = Premium**

### 3. Experience Modifier

An experience modification factor, or e-mod, is a calculation that uses your past loss experience to predict whether you're likely to have losses better or worse than the average for your industry.

Your business may not have an e-mod. To qualify in Missouri you must:

- Have premium of at least \$7,000 for one year or \$3,500 for two more years, AND
- Be an established business for a minimum of three years.

#### How is my E-mod Calculated?

In states that have adopted its use, such as Missouri, e-mods are calculated by NCCI.

If your e-mod is higher than 1.0, it means your losses are worse than what's expected for your type and size of business, and you can expect to pay more work comp premium for a period of time.

If your e-mod is less than 1.0, it means your losses are better than what's expected for your type and size of business, and you can expect to pay slightly less than your competitors.

You can see in the example, an e-mod of 1.25 means your premium could be as high as 25 percent more than if you had an e-mod of 1.0.

#### AN EXAMPLE

### E-mod Factor

#### ABC Company

Base Work Comp  
Premium ..... \$25,000  
E-mod ..... 0.75  
Estimated Premium .....  
..... \$18,750

Base Work Comp  
Premium ..... \$25,000  
E-mod ..... 1.00  
Estimated Premium .....  
..... \$25,000

Base Work Comp  
Premium ..... \$25,000  
E-mod ..... 1.25  
Estimated Premium .....  
..... \$31,250

The good news is that e-mods are not set in stone. NCCI calculates e-mods annually based on the company's loss and payroll data from the three prior years.

#### A SIMPLE FORMULA

### Work Comp Premium Calculation

$$\text{① Payroll} \times \text{② Classification Rate (per \$100 of payroll)} \times \text{③ E-mod} = \text{Premium}$$

### It Pays to Pay Attention to Your E-mod

Because e-mods have a direct correlation to how much work comp premium you pay, it's important to monitor your e-mod. You have the opportunity to improve your e-mod over time by maintaining a safe workplace and managing claims costs.

Here's a list of things you can start doing today to be more proactive:

- Create a safety program to prevent injuries and educate employees at all levels. And note: e-mods are influenced more by small, frequent losses than by large, infrequent ones.
- Create a return to work program. Reduce indemnity, or replacement wage, costs.
- Report injuries promptly. Ensure the employee receives timely treatment and prevent avoidable medical costs and prolonged recovery periods.
- Implement a claims management program. By managing your claims, you'll be able to focus on outstanding claim reserves and resolving open claims.
- Contact your agent if you think your e-mod is inaccurate. You may be paying more than you should due to incorrect or incomplete data.

#### A SIMPLE FORMULA

### Work Comp Premium Calculation

$$\textcircled{1} \text{ Payroll} \times \textcircled{2} \text{ Classification Rate (per \$100 of payroll)} \times \textcircled{3} \text{ E-mod} = \text{Premium}$$

## 4. Adjustments

There are many factors that influence your final premium. Not all work comp insurance companies are the same. Each may offer different premium adjustments for a variety of items.

Modified premium is premium after application of the e-mod, but before application of other credits and/or debits. Certain criteria are evaluated which apply credits and/or debits to the policy related to the unique conditions of your business. Carriers may consider your:

- Premises
- How safety is applied in your organization
- How employees are selected, trained and supervised
- Management's commitment to safety and cooperation with the insurance company
- Medical facilities

There are a variety of potential adjustments, but you can still estimate your premium without taking into account these factors. Just remember that the final premium may vary depending on the adjustments.

## Adding it Up

Now that you know the basic formula for work comp premium, you can arrive at an estimated premium for your business.

### Try It

Build It Contractors employs five carpenters that each make \$40,000 per year and two people in administration that each make \$50,000 per year.

Two class codes and their rates apply:

Carpentry (5645) \$17.06

Clerical (8810) \$0.31

Build It Contractors has a good e-mod of .80. What is the company's estimated premium?

REMEMBER THE SIMPLE FORMULA

## Work Comp Premium Calculation

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**Payroll** x **Classification Rate** (per \$100 of payroll) x **E-mod** = **Premium**

BUILD IT CONTRACTORS

## Work Comp Premium Calculation

**Class Code 1** [(payroll/100) x rate] + **Class Code 2** [(payroll/100) x rate] X **E-mod**

**Carpentry** [(\$200,000/100) x 17.06] + **Clerical** [(\$100,000/100) x \$0.31] x .80

\$34,120

+ \$310

x.80

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**Estimated Premium: \$27,544\***

*\*Remember, this is only an estimate and adjustments and fees may apply.*

## Start Saving

While you may not be able to directly control factors such as the classification rate assigned to your particular work, or the inherent safety level of the industry in which you operate, there are steps you can take to reduce your work comp premium. Now that you have a basic understanding of how your premium is determined, you're better equipped to start managing costs.

Your agent is a great resource to help you understand and control premium. If you need to find an agent, use MEM's tool at [www.mem-ins.com](http://www.mem-ins.com). You can also check out more MEM resources at [worksafecenter.com](http://worksafecenter.com).