

Adequacy of Earnings Replacement in Workers' Compensation Programs

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family form, but squarely on the needs of children.

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In the early part of the last century, a social contract between labor, employers, and government was achieved, the like of which, arguably, has never been replicated. Workers were barred from suing their employer for work-related injuries and diseases in return for expeditious, though limited, compensation. Central to striking the compromise was mutual agreement that the workers' compensation system would provide adequate medical treatment, vocational rehabilitation, and recovery of lost earnings.

However, recent reforms, frequently motivated by cost control considerations, have, in the view of some in the workers' compensation advocacy community, seriously reduced the adequacy of benefits and undermined the social contract. Especially sobering is a decision from the Supreme Court of Canada on a matter challenging the tort bar. The language of this decision suggested that further erosion of workers' compensation benefit adequacy could be sufficient to void the social contract and force the court to re-open the door to litigating work injury compensation.

Whether workers' compensation benefits were ever adequate, and whether adequacy has diminished, are ultimately empirical questions. Step 1 in addressing these questions is defining "adequacy" and step 2 is measuring adequacy. This book takes readers a very long way on this two-step journey.

The authors note that while benefit adequacy is central to perceptions of the fairness of workers' compensation, there is no single definition of adequacy. Should adequacy be relative to a poverty standard or a policy standard, such as the proportion of lost earnings replaced by indemnity benefits? If a wage replacement standard is chosen, how might the proportion of lost wages replaced by workers' compensation

be assessed for a worker whose injury has compromised his or her ability to be employed in the future? The central problem in such a case is that it is impossible to know what that injured worker's lifetime earnings would have been but for the accident.

A number of alternative measures of adequacy are proposed and critiqued, with the strengths and limitations of each clearly set out. The various approaches to measuring adequacy are illustrated with appropriate simulations, based on the benefits prescribed by each state's workers' compensation statute. One of the valuable contributions of the analysis is its demonstration that the adequacy of a particular state's earnings replacement can vary widely depending on the measure used. Another contribution is the excellent discussion, expanded upon in appendices, of the data, methodology, and judgment calls necessary to perform each of the calculations, highlighting the fact that the assessment of adequacy can also be influenced by the initial assumptions. Further, the measures of expected benefits—both averages across all injury types (temporary, permanent, and fatal injury) and averages broken out by injury types—are very carefully done, and truly represent the state of the art for performing this type of analysis.

The authors also review the evidence from the small number of wage loss studies, based on data from a very few states, that measure the extent to which benefits actually paid to injured workers (as opposed to what the statute prescribes should be paid) replace lost earnings (a) immediately following the accident and (b) into the future. The amount the worker would have earned, but for the accident, was estimated in these studies using either matching methods or regression techniques (since this figure is otherwise unknowable). A central conclusion is that studies measuring actual wage losses are superior to the statutory benefit studies, principally because they measure actual benefits received, which may in part reveal information about how the workers' compensation statute is administered.

Whether based on studies measuring expected benefits payable under a workers' compensation statute or on studies measuring benefits actually received, the verdict for benefit adequacy is the same. Relative to the authors' preferred yardstick, which is that indemnity benefits should replace at least two-thirds of lost wages, benefit adequacy typically falls well short. Among the more alarming results are the dismal earnings replacement rates for fatal and

permanent partial and total disability claims. The failure to provide adequate compensation for these types of devastating workplace incidents, in my assessment, represents a threat to the continued viability of the historical compromise. There is a perception among many workers' compensation advocates, supported by very little information, that compensation for minor injuries is probably better under workers' compensation than under tort, and *vice versa* for more serious injuries and death. I think a valuable extension of this research would compare workers' compensation benefits to awards that one might expect in tort for similar injuries, after taking account of the cost, delay, and apportionment of fault between the worker and employer that are also part of the tort determination.

I have only a few minor quibbles. First, I wish the authors had provided more information on the actual results—that is, the statutory benefit amounts and lifetime income amounts that were projected in their analysis of expected statutory benefits—perhaps in an appendix. In addition, the many bar graphs comparing results across states would have benefited from showing the actual value of, for example, the replacement rate in each state. All of this information would be helpful to researchers who are trying to replicate these results as a starting point in pursuing future research, as well as for readers who wish to make their own determinations of adequacy.

Related to the issue of the metric that determines adequacy, there is a somewhat distracting focus on classifying a particular workers' compensation benefit as adequate if it replaces two-thirds of lost earnings, and inadequate if it does not. It is clear from the discussion contained in the concluding chapter that some members of the advisory panel overseeing the project upon which this volume was based may have had similar sentiments. Although the authors creditably defend the two-thirds replacement rate standard as a reasonable one, it is ultimately arbitrary, and adequacy is in the eye of the beholder. Taking the very key steps of explaining and estimating the various measures of adequacy was enough, in my view; emphasizing the two-thirds rule was not necessary.

Of necessity, this volume confines itself to looking at the adequacy of wage loss indemnification. Workers' compensation systems, as described earlier, provide a number of other benefits, including medical and vocational rehabilitation, and there may be tradeoffs between the benefits provided. That is, a state may

choose to offer relatively generous medical benefits, but at the cost of more modest wage loss benefits. I agree with the authors that the adequacy of wage-loss benefit compensation is an important issue in its own right, and that a fuller evaluation of all of the benefits offered by workers' compensation should be the subject of future research. Indeed, the concluding appendix of the book sets out an ambitious research agenda that should be the point of departure for many future dissertations.

This volume represents another in the Upjohn Institute's growing list of important contributions to the workers' compensation literature. It will be valued by both researchers and policy-makers. I would also recommend it to those who are new to workers' compensation, not least because the background information on the historical origin and the operation of workers' compensation is one of the best, and briefest, primers on the subject that I have read.

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Carve-Outs in Workers' Compensation: An Analysis of the Experience in the California Construction Industry. By David I. Levine, Frank W. Neuhauser, Richard Reuben, Jeffrey S. Petersen, and Cristian Echeverria. Kalamazoo, Mich.: W.E. Upjohn Institute for Employment Research, 2002. 175 pp. ISBN 0-88099-238-7, \$40.00 (cloth); 0-88099-237-9, \$18.00 (paper).

Workers' compensation is a state-specific, usually mandatory social insurance program providing workers with cash (indemnity) benefits and medical care for work-related injuries and diseases. Recent years have seen the emergence of various workers' compensation alternative dispute resolution (ADR) programs. Workers' compensation ADR has been characterized as an alternative to what, from the outset, was itself an ADR system (Lex Larson, *Larson's Workers' Compensation, Desk Edition*).

First introduced in the United States around 1910, workmen's compensation legislation was intended to provide adequate medical care and prompt, predetermined cash benefits "while limiting the employer's liability strictly to