



Direct and Indirect Workers' Compensation Costs Explained

Workers' compensation claims have a variety of different costs associated with them. Some of these costs are expected costs, while others are unexpected. Here's the difference between these terms:

- Expected costs are those that are covered by workers' compensation insurance. Such expenses are commonly referred to as direct costs.
- Unexpected costs are those that workers' compensation insurance does not cover. These expenses are commonly referred to as indirect costs.

According to the [Occupational Safety and Health Administration \(OSHA\)](#), both direct and indirect costs can have a substantial impact on employers and their bottom lines. As such, it's important for employers to understand the difference between direct and indirect costs, how to reduce these costs and why it's important to do so.

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Direct vs. Indirect Costs

Direct and indirect costs are determined by which expenses workers' compensation insurance will or will not cover. To reiterate, direct costs are those that are covered by such insurance, which can include:

- **Employee Wage Benefits:** These benefits include temporary total, temporary partial, permanent partial and permanent total disability. Employers have to pay these benefits when an employee is unable to work or return to work in full capacity.
- **Medical Payments:** These payments refer to any medical costs needed to treat an employee's injury.
- **Vocational Rehabilitation Costs:** These expenses are any costs associated with an employee's rehabilitation (e.g., training and career counseling).
- **Death/Dependency Benefits:** These benefits are for the spouse or dependents of an employee who was killed by a work-related injury. Such benefits vary by state.
- **Legal Fees:** These fees include those associated with a workers' compensation claim, any civil liability expenses and settlement costs.

Indirect costs for a workers' compensation claim are those not covered by such insurance. These costs can vary depending on the extent of an employee's injury. Some indirect costs include:

- **Wage and Hour Costs:** These additional costs are incurred by employees who must work extra hours to compensate for another employee's time away from work. This includes hiring temporary workers or having employees work overtime to fill in for the missing worker.
- **HR Support Expenses:** This includes the increased work and time incurred by individuals who handle workers' compensation claims and related paperwork.
- **Claim Investigation Costs:** This includes costs associated with the investigation of a workers' compensation claim if there is a concern of fraud.
- **Hazard Mitigation Costs:** This includes costs associated with mitigating the hazard(s) that caused an employee's injury.
- **Production Deadline Extensions:** An injured employee's absence can cause delays in production, thus increasing production costs and negatively affecting business contracts.
- **Training Expenses:** This refers to the costs of training other employees to fill in for an injured employee if they are unable to return to work in their original capacity. This can be a temporary or permanent arrangement. If it's permanent, the company may have to cover the costs of hiring a new employee.
- **OSHA Fines:** If an employee is injured or killed at work, an inspection will be triggered and the employer may be subject to OSHA citations for any safety issues found during the inspection. Also, the more employee injuries and fatalities an employer experiences, the higher their business's incident rate will be — thus triggering more OSHA inspections.
- **Insurance Premium Expenses:** The more injury-related costs an employer experiences, the higher their experience modification factor will be. As a result, their business may be considered high risk and could receive increased premium rates.
- **Repair Costs:** Repair expenses associated with property or equipment can also be considered indirect costs, depending on whether or not the property or equipment was involved in an injury-causing incident.
- **Workplace Culture Concerns:** A company with a high rate of injury may encounter poor employee morale, particularly because employees may begin to think that their employer does not care about their well-being. Typically, the lower morale is within a company, the higher incident rates will be.
- **Reputational Struggles:** A company with a high rate of workers' compensation claims can garner a bad reputation. With a poor reputation, business contracts and qualified workers may be difficult to secure. A bad reputation can negatively impact an employer's bottom line and even lead to their business closing down altogether.

**Controlling these direct and indirect costs can be beneficial for employers.
That's why it's crucial to be proactive.**

Reducing Direct and Indirect Costs

It's important for employers to understand that investing in their safety programs can positively affect the outcome of direct and indirect costs. For instance, managing safety programs at a business and having employees actively engage in hazard identification can reduce the likelihood of injuries. By reducing injuries, direct costs related to expenses such as wage benefits and medical payments will also decrease. This will, in turn, lower indirect costs as well.

Having a successful safety program is the foundation of reducing workers' compensation claims. If an employer cannot eliminate workers' compensation claims, another way to reduce direct

and indirect claims is to proactively manage claims. This can involve working with employees to get them back to work quicker after an injury and following up with claims handlers. Furthermore, participating in the claims process can improve communication between an employer and their employees, as well as the employer and their insurance company.

Having an effective return-to-work program can also help with reducing direct and indirect costs. Having other work options for employees that fit within their medical restrictions encourages employees to return to work quicker, thereby reducing a significant amount of direct and indirect costs.

The Importance of Reducing Direct and Indirect Costs

Minimizing direct and indirect workers' compensation costs is critical. By reducing injuries, a company can continue to function normally, avoid interruptions and prevent issues with production or business contracts.

According to the [National Safety Council \(NSC\)](#), work-related injury costs for employers in 2019 totaled \$171 billion. This total can be broken down as follows:

- \$52.9 billion in wage and productivity losses
- \$35.5 billion in medical expenses
- \$59.7 billion in administrative expenses

Employers' uninsured costs (\$13.9 billion), property or equipment damage (\$5 billion) and fire-related losses (\$3.7 billion) also contributed to this total.

In breaking these costs down, the NSC found that such expenses came out to \$1,100 per employee. Further, the average cost per fatality was \$1.2 million, while the average cost of an injured employee's medical treatment was \$42,000.

Overall, by reducing employee injuries, employers can help create a positive work culture and lower workers' compensation expenses — thus minimizing both direct and indirect costs.



Contact Brady, Chapman, Holland & Associates to discuss your workers' compensation needs.