

Workers' Compensation Reform Shows Power of Privatization

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Story By Matt Ryan

As I'm sure you've read by now, West Virginia completed the process of privatizing its workers' compensation system June 30.

When the process began, West Virginia was one of only five states (North Dakota, Ohio, Washington and Wyoming were the others) to provide workers' compensation insurance exclusively through a state fund. Now, in a move toward capitalism, West Virginia has taken after the rest of the nation, and businesses here are seeing the benefits of markets at work.

The process started during the 2005 legislative session with SB 1004, which converted the state-run fund to a private mutual company by the name of BrickStreet. Starting Jan. 1, 2006, Brickstreet was given a state-protected monopoly on offering workers' compensation insurance to the companies of West Virginia. Now, as of June 30, the state-granted protection for BrickStreet has ceased, and any private insurance company is free to compete within West Virginia.

Generally, consumer protection groups like to fight against "monopolies" and the supposedly too-high prices they charge. Without delving into this issue -- monopolies and the misconceptions about them are separate topics worthy of their own column -- it is generally assumed that fewer companies operating in a marketplace retain a bit more of an advantage in being able to favorably price goods. (In contrast, companies have no pricing power in the textbook example of "perfect competition.")

But consider this: Even with a state-granted monopoly on offering insurance during the past two and one-half years, BrickStreet saved West Virginia employers more than 30 percent in workers' compensation costs. Now that the market has opened up, expect companies to not only pay less still but to be offered with a greater range of products.

Paying less is fantastic, but do not undervalue the ability to purchase a more suitable insurance package. As of June 30, 162 private companies had filed with the West Virginia Office of the Insurance Commissioner, which will allow them to operate within the state. Of these, 24 are newcomers to the Mountain State.

Comparing the state's provision of workers' compensation insurance to BrickStreet's highlights the superior ability of the private sector to supply goods and services. Both systems had a state-granted protection against competition and operated in the same market, yet the private system provided the same services at a 30 percent discount on the public system. The crucial difference comes in the role of profits.

BrickStreet is responsible for, and gains from, its own actions; in economics terms, we would call them a "residual claimant." As such, BrickStreet -- its owners, shareholders and employees -- stands to benefit in direct proportion to how well it provides insurance. Should BrickStreet provide a quality product that companies value, it will profit; its protection from competition, or monopoly status, is separate from the fact that it still has the incentive to provide the best service possible since it gains from doing so.

Profits are often wrongly blamed for a range of society ills, yet they are the sole reason why the cost of workers' compensation insurance to West Virginia businesses fell during the past 30 months.

Now turn to the provision of workers' compensation insurance by the West Virginia state government. When providing goods and services, the government -- the people filling the public roles -- is rarely the residual claimant. Public servants have less of an incentive to perform their duties as best as possible since they do not stand to benefit from more efficient production or a more useful project.

That is no slight against those serving public roles; instead, it speaks to the outcome of placing otherwise productive individuals in an environment where they do not stand to benefit in proportion to their ability to provide valuable services to society. Further, companies must generate profits or cease operations -- sadly, the government can never

close up shop due to a lack of profitability.

When I write about different aspects of West Virginia, I usually try to provide a ranking or some sort of metric to place our scenario in relation to the rest of the country. We're generally at the wrong end of the spectrum regardless of the measure, but in looking for a comparison of state workers' compensation systems, I encountered a scenario that was a first for me. One group that ranks workers' compensation systems refused to include West Virginia in its rankings; the pre-2006 workers' compensation system was so archaic that it actually couldn't be ranked along with the others.

Last is one thing, but being dropped from the list? Here's to West Virginia joining the rest of country. Let's hope it doesn't stop here.

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