



# CAMBRIDGE

## PROPERTY & CASUALTY

### SPECIAL REPORT

## WORKERS' COMPENSATION AND EMPLOYEE CLASSIFICATIONS

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Workers' Compensation premiums are determined by how an employee is classified, and there are hundreds of classifications.

Because Workers' Compensation policies are audited after the policy expires, each classification must be analyzed carefully to determine its correctness. The audits determine the actual payroll for the preceding 12 month period and the accuracy of the classifications used. The policy can be changed retroactively.

We would like to discuss several areas that cause audit problems.

1. The first area of audit problems relates to dividing payroll between two classifications.

An example of dividing payroll between two classifications would be an employee who spends a portion of his or her time in the office doing clerical functions and another portion of time delivering product to customers. Some employers will divide the payroll between the lower clerical rate and the higher driver rate. Payroll division is acceptable only under certain circumstances.

- a. The entries on the original records of the insured disclose an allocation of each such individual's employee payroll.

- b. Allocation must be based upon payroll actually incurred in each operation. An estimated or percentage allocation is not permitted.

- c. The allocation of payroll is not available for three special classifications:

- 1) Clerical
- 2) Drivers
- 3) Outside sales

2. In the example given above where an employee spends time in a clerical function and another portion of time in a driver function, the allocation of payroll rule would not apply and that employee would be charged based upon the highest rate, which is the driver rate.

3. Another issue that can cause audit problems is the use of code 4511, which is the quality control classification. Many manufacturing clients have quality control operations, and these operations are

typically in separate rooms used to analyze the quality of the insured's products.

The code 4511 rate is generally low; however, technically, the rate does not apply unless an insured, as a distinct enterprise, specializes in research or analytical problems. It is not available for any risk engaged in operations described by another classification (for example, plastics manufacturing) unless the code 4511 operations are conducted as a separate and distinct business.

Therefore, laboratories established for the purposes of supporting an entity's principal business are not classified as code 4511 and would be classified as the higher manufacturing rate.

If you would like a detailed description of the classifications that may apply to your operations, please contact us.