Tackling Workers' Comp Insurance Fraud with Data and AI

Beyond the Text is a Conning podcast that features insights from its Insurance Research Department. Hosted by Alyssa Gittleman, a Director and Head of Consulting and Customer Operations for Conning Insurance Research. Alyssa will invite analysts and guests to provide insights on recent publications and emerging industry trends.

Beyond the Text is intended to provide just that: going beyond Conning's typical research. Conning's analysts have deep industry knowledge and come from various backgrounds providing a greater level of context on industry trends for insurance professionals.

[Opening Music]

[Alyssa Gittleman (AG)]
Hello and welcome to Beyond the Text, a Conning podcast featuring insights from our Insurance Research department. I'm your host, Alyssa Gittleman, the Head of Marketing and Communications here at Conning. Join me as I welcome analysts and guests to provide insights on recent publications and emerging industry trends. Today I'm here with Jay Sarzen, a Director and property-casualty analyst in our Insurance Research department. He is also the author of our recently released workers' compensation report, "Eyes of the World, Using Data and AI to Fight Workers' comp Insurance Fraud." Thank you, Jay, for joining me here today.

[Jay Sarzen (JS)] (00:45)

Alyssa, thanks for having me. Appreciate it.

[AG]

And I guess before I go further, I do want to just mention that this report is available to purchase on our website, Conning.com. So Jay, let's dive into this and I was hoping before we really go into the meat of the report, could you share what the motivation was behind doing this report on fraud and workers' comp?

[JS] 00:48

Yeah, I think for one thing, everyone recognizes that workers' comp has been a hugely profitable line of business for insurers for most of the past decade, but there are some storm clouds forming around it. So, I set out trying to see what I could offer up to insurers that might help them mitigate the emergence of some of these storm clouds.

So, getting to some of the things that I'm seeing out there, number one, primarily accident-year loss ratios are deteriorating, which means that all of these insurers and all of these insurer employers have instituted these worker safety programs. They're reaching that point of diminishing returns. And no matter what they do, no matter what they throw at it, people are starting to get injured on the job with declining frequency. So, I think that number one is probably the biggest driver of this report. Number two, let's face it, fraud is a problem. And depending on how you define fraud and depending on what you look at as your scope of fraud, it could be anywhere from a $25 billion to a $40 billion problem.

That's a big number, and I think that insurers ought to be aware of it. So that in and of itself was a main reason why you want to tackle that report. You want to remove that from the cost equation. I'm seeing more sophisticated fraud schemes. It isn't just something very simple where someone fakes an injury. These schemes, these fraudsters have just embraced technology. They're leveraging it to a point where the old ways of fighting back just aren't going to be enough. So, I felt it was important to bring this to light for a lot of insurers.

And really, honestly, I think typically insurers have been very defensive when it comes to fighting fraud. Let's put them on offense. Let's make them proactive. So that's what really prompted me to dig into this topic and bring it to light for these folks.

[AG] 3:16

Thanks that's really interesting and that's a huge number too, the $40 billion. So, with that, in talking with you earlier, it sounds

like you had an idea of how this story was going to end when you were doing your research. When conducting your research, was that proven true?

[JS] 3:34

Yeah, I I always like to say that I go into something with an open mind, but the reality for me is that I've been looking at this issue for the better part of the last decade and the ending was kind of preordained. I think number one you're seeing a lot of really innovative vendors that have emerged onto the scene with some solutions that are designed to proactively detect fraud, especially in workers' compensation claims. So right there you have a sense that these vendors are chasing something. So, if they are in the market offering up these solutions, if there's smoke, there's probably some fire.

I think really what it comes down to is that insurers have to find a way to embrace this technology and to take it up. And, you know, at this point, I just want to be very clear. I didn't do a full survey. I didn't go out and ask 100 executives. I have a lot of contacts in this industry. And I reached out to a handful of them and said "What's preventing you from really embracing these emerging technologies that are designed to detect fraud in workers' compensation?" and to a T they all basically said "the juice isn't worth the squeeze."

In other words, is it really worth throwing all of this money and all of this time and all of this effort at a problem that we just kind of think is a cost of doing business? And we can dig into that a little bit more later on in the discussion. But I think that is really where my idea came from, is that insurers are aware of these technologies, but they need to be pushed to accept them.

[AG] 5:27

Okay, yeah, that makes sense. And I guess you're probably going to go into this a little bit more with what you just said, but I was hoping to go on to if there were any major surprises that you discovered while writing this report.

[JS] 5:38

Yeah, it's, again, not really a surprise, but it's really disbelief. I know insurers today are looking at fraud, and yes, whether it's $25 billion or $40 billion, it doesn't really matter. It's a lot of money. But when you spread it out across a number of different insurers and they're looking at, it's like, well, it's only $50 million for us or $20 million for this farm bureau, whatever the case may be. They're not looking at it as a problem that can't be overcome through slight rate increases, which we'll get to shortly because state insurance regulators are looking at the profitability of workers' comp insurers and saying "we're not going to let you increase rates."

So that kind of is a is a little bit of a rub. But these insurers aren't thinking ahead of what fraud could become, right? They're not envisioning a more sophisticated, more widespread fraud scheme with multiple players in the mix trying to build them out of money. And the really sad part is that no one knows what form this is going to come in. OK. I think everyone in, say, for property, for example, can look at, "oh well, the next time a major catastrophe hits, we're going to incur X billion dollars of losses."

That's not how workers' comp works. There are no billion-dollar workers' comp claims. It's death by 1,000 paper cuts. So, when you get more fraudsters entering the system and trying to engage in fraud, it's like bankruptcy as Hemingway said: "it just happened ever so slowly and then it was." You really don't even know that it's happening until your neck-deep into it. So, I want to be clear: I don't think any insurer is going to go under because of fraud. But it's a question of whether insurers are going to be willing to continue to accept this.

So when they're willing to accept it as a cost of doing business, they're basically saying, yeah, you know what, our insurance, they'll eat it. They'll eat the cost of it because it'll be baked into the premium and if we can get our state regulators to increase rates, great. If not, we just accept it because it just isn't that horrific of an issue for them. But I guess the alternative would be if they're willing to, if, if they don't want to hurt the business owners that are buying their workers' comp policy, then they accept slightly diminished loss ratios.

And you know, as I've said, they for the under the past decade, it's been well under 100. So do they say, OK, you know what, we'll accept a loss-rate combined ratio of 94 as opposed to the 91 that they've been getting. And that's not even bringing into account how accident-year loss ratios are coming into play. As I said, they're deteriorating, but their insurers are drawing down reserves

to cover over these deteriorating accident-year loss ratios and that's how they're making their combined ratios look so good. So there are a lot of issues. And when you ask me about a surprise, I mean, again, not a surprise per say, but I still shake my head sometimes that insurers continually rely on their special investigation units, and that's pay and chase, right? The payment has already gone out the door. Now you've identified that there could be an issue. So now we're going to do some observations and then hopefully claw that money back. It's very difficult to claw that money back, so I don't want to say it was a surprise, but it's more disbelief than anything else.

[AG] 9:25

Yeah, I definitely can see why that would, why you would feel disbelief there. I know that seems pretty crazy to me, all that money just going out.

I would love that. But, it does seem like the landscape is changing for insurers as far as fraud is concerned. So, can you give us a high level overview of what this looks like?

[JS] 9:46

Yeah, you know, fraud comes in many different forms. It could be employer fraud, it can be employee fraud, it could be medical provider fraud, depending on what angle they're looking to take and who's looking to benefit from the largest of insurance carriers. It could be anything. But I think the thing that I want to really stress here is that what we're seeing are more organized rings.

So it may be that an employer might unknowingly hire an employee who's been plugged into some fraudulent medical providers who will say "if you can get injured," and for the audience I'm making air quotes that you can't see, "you get injured on the job, I will attest that you need months and months of therapy. Now, you may not really need that months of therapy. You may only need a month of therapy, but I'll attest that you need seven months of therapy and I'll continue to bill the insurance carrier. You continue to act injured. And you and I can split the profits."

OK, this is the imagined conversation that I'm having between a fraudulent medical provider and someone who's an employee, right? And that definitely happens. But the biggest fraud is really payroll manipulation. And that's on the part of the employer. You can mischaracterize workers' in terms of their status, whether they're full-time or part-time, whether they are doing certain roles or doing different roles that may be more dangerous. Just last month there was a report from Maryland, the state insurance commissioner, they had a report that was issued in late February, and they estimated that in Maryland - this is just one state – 5,500 workers' were misclassified in 2024 as independent contractors and it cost insurers writing workers' compensation insurance in Maryland an estimated $58 million in insurance premium. Now that's $58 million. When you think about it in terms of that $40 billion number we were throwing around, it's nothing but it's something.

You multiply that out times 50 states and even the people who pulled that report together admitted we probably didn't even catch all of it. So, you can just imagine what they didn't know and how bad the problem really is. So, that is another issue.

We're seeing the opioid crisis. We're not going to go into the whole fentanyl and the borders, but we are seeing a deep crisis right now in the United States of America with opioids. And whether a person who has become injured and has become addicted to them and wants to continue using them through fraudulent means or there are medical providers who will write prescriptions knowing full well that the person doesn't need them. Whether that person actually consumes them or turns to sell them on the black market.

There's all kinds of reasons why people want to get in on opioids and use them in a way that are for less than above-board purposes. So that's something that you need to be aware of. And then of course, I alluded to it, it's the good old fashioned "ow my arm it hurts," and that does happen. But I think a lot of folks really believe that that's the preponderance of workers' compensation insurance fraud, that an employee is simply faking an injury. And yes, that does happen but the bigger issue largely is with employers and payroll manipulation.

It's a huge problem.

[AG] 13:41

Thank you. That was a great explanation. So, it seems like the potential for fraud is everywhere. Could you share with us the tech-

niques that are available to insurers to help deal with this shifting landscape?

[JS] 13:53

Yeah, absolutely. As with most innovations in the insurance space, data is going to be the foundation. And, before I jump to the innovation part, Alyssa, I want to just acknowledge that a lot of the traditional techniques that are in place, your special investigation units that I mentioned earlier, medical canvassing, in person surveillance.

I mean, literally you have someone who may be out in a worker's compensation claim and you stationed someone out in a van outside of their house and you're seeing, wow, they're going to the gym every day. Now that may be a part of their person's prescribed physical therapy, or it may be that they're really not that injured. And that's where the in-person surveillance comes in. So, you know, I don't want to discount that because there may be some old school insurance folks listening to this who are saying, well, the SIUs are terrific.

They've worked for years and it's true, they have. But as I mentioned, I think fraud schemes are becoming a little more sophisticated and you need a little bit more oomph behind it.
So, some of the things that are available: number one, social media data. You would think that, well, if you're out on a worker's compensation claim, why would you post yourself doing strenuous activity? You're overestimating a lot of people. They have no qualms whatsoever about posting their weekend windsurfing or mountain climbing, who knows, whatever it is they're doing when wow, you're supposed to be nursing a lower back injury that's preventing you from doing your job.

[AG]

Right.

[JS] (15:22)

And, and that does happen, but it's also about employers. So, for example, if you're a landscaper and you have told your insurer that our folks are doing landscaping that's ground-based only, and yet you're posting social media pictures with your folks up in trees, topping off big pine trees, that's kind of a hint that you're probably engaging in some payroll manipulation. It's crazy, but it does happen. In my last report, Alyssa, we talked about wearable technology, understanding the conditions of the environment at the time an accident may have happened or what stress a particular individual might have put on his or her body as they lifted a box or as they moved a pallet or whatever task it is that they're doing.

A lot of that data can be gathered to do accident re-creation, to gauge injury severity. So, as you look at that data, you say, OK, well, yeah, the person didn't get injured. That was legitimate but this typically would require a month or two of therapy and rest, not for five months. So definitely wearable technology comes into play. I kind of hinted at my next point about robust data, about what a business is and what it does. It's the old "we mow lawns in the summertime and that's it." But now you're trimming trees, you're plowing snow, you're engaging in snow removal, you're breaking up ice dams on roofs.

There's a lot of things that can go wrong when you're doing all of those things. So to take all that data in, I think is pretty incredible. A lot of the data can be used as kind of standalone data. Nothing that you need to go do besides look at it and say, "Aha, there's an issue here." But more often than not, strong analytics are going to be required in order to make sense of the data. So I'll take you through some of them.

Text analytics number one is something that insurers can use. It's, as you're taking statements from people in an accident investigation, you're listening to their voices, you're looking at their statements that were provided to see if there are any inconsistencies in the statements. And again, it seems so elementary, but it's really, people change their stories all the time. And those nuances can be caught through text analytics.

There's biometric and behavioral analytics. I think that's kind of self-evident. You've got someone who is being deceptive. You know, you can tell that through their eyes, through their voice inflection. It's a little bit out there, but it is being used.

Predictive analytics is probably going to be your best bet. So that's where you're able – a vendor is able to take disparate bits of information about an accident, about a person, about a person's known associates, and bring it all together and determine if

there is a possible presence of fraud. That deeper analysis on that is called that link analysis. So Alyssa, you and I have known each other for a little while. And let's just say you're involved in some really shady behavior and people know that I'm connected to you and I stake a claim; just knowing you who's been involved in shady behavior (for all of our listeners, she's really not, I'm just using this to illustrate the example), but if you were, that would cast a shadow upon me, and it would bring some suspicion to the table. So that's where that link analysis comes into play.

I think that one thing you have to remember in all of this, however, is that despite all these tools that are out there, none of them are absolutely saying with 100% certainty that fraud has happened. It's simply saying we feel there's enough smoke here to merit a deeper look. So a lot of that is going to be wrapped up in what's called a fraud risk score. So, whether you're using text analytics, biometrics, predictive analytics or link analysis, there are vendors that can bring it all together and say this claim we feel has a number, it's a 70.

And any insurer can set its own pain threshold. If it says yeah, if anything is above 80 on your spectrum, we feel that we need to dive a little bit deeper into a claim, but you can, if you're an insurer, you can say, look, I'm very nervous and I can set it as low as 30. So, if you have a score that's anything above 30, they may put a different set of eyes to it. It all depends on what pain threshold an insurer has. But I think the thing to remember in all this is that there's nothing that absolutely says 100% that fraud is taking place.

Going back to my earlier example, when you're doing that surveillance of that person is going to the gym, well, you just can't say, oh, that person's going to the gym, therefore that person is committing fraud because that person's out on worker's comp claim. As I said, it could be just the prescribed part of the physical therapy. So, there are a lot of tools out there that are helping these insurers overcome these groups, these rings that are engaging in more sophisticated fraud schemes. You just can't fight them with two guys in a van sitting outside the person's house.

[AG] (21:03)

Right. And as I understand it, the vendors that provide the innovation you were just talking about are always seeking to push the envelope, so to speak.

So, what innovation in the space do you see coming at some point in the future?

[JS] (21:16)

I think what we've talked about is pretty innovative and the truth is that - I made this point earlier - most insurers have not really fully embraced what's available to them. So, you know, they're not leaders, they're fast followers and they need to really begin to embrace what's out there first. But because you asked the question, I'll try to answer it. I have and I want to be very clear this is my own view, OK? There's no real evidence to suggest that anything what I'm about to talk about is being worked on. But there is that potential fusion between wearable technology and fraud detection tools, some of those that I just talked about, even though that wearable technology is out there, it only provides data points, OK? It doesn't give you any insights that fraud may have been committed or if there's any fraud presence. I mean, it's possible to do, but as I said, no one's really talking about it. I really think that the next innovation that we're going to see is largely going to be what we already have.

So the predictive analytics, the link analysis, it's just that the AI is going to become a lot smarter, a lot sharper, a lot quicker. It will potentially be able to offer you up a real time assessment that something is afoot. And you as an insurer or you as an employer need to be aware that something is imminent as opposed to right now, it always is an accident that has happened, now we have to determine if it's fraudulent. OK, so in the current state, it's more that someone gets injured, you pay the workers' comp claim, you let it go along for a little bit, and then you might say something is a little bit suspicious.

That's where you're bringing in the SIU. These new tools are kind of bringing it back beyond the SIU and bringing it a little bit closer to the point of when the accident occurred. I'm saying that given how smart AI is becoming, you could bring it even closer to the point of the accident that I believe is where the innovation is going to happen.

[AG] (23:36)

That's great.

[JS] (23:37)

Well, we'll see.

[AG]

Thank you so much. That's a wrap for today's episode. Thank you, Jay, for joining me today, and thanks for going beyond the workers' comp market with us.

And thank you all for listening to today's episode of Beyond the Text. If you're interested in learning more about what you heard today, you can purchase our reports at Conning.com. You can always send questions to insuranceresearch@conning.com, too. We hope you will subscribe to this podcast and join us for our next episode as we stay up to date on industry trends. Thank you.

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