

NEW DEVELOPMENTS IN THE INTERACTION
BETWEEN NORTH CAROLINA STATE EMPLOYEE
BENEFITS AND THE WORKERS' COMPENSATION SYSTEM

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I. INTRODUCTION²

Although the interaction between the state employee benefits system and the workers' compensation system has some points of friction that have been the source of litigation,³ as a general rule, the two systems fit together fairly neatly. This paper provides a broad overview of the benefits available to state employees from the State and discusses how the receipt of workers' compensation benefits would affect these benefits. Finally, it discusses how the careful structuring of settlements can mitigate or avoid offsets of workers' compensation benefits against benefits from the State.

II. STATE WORKERS' COMPENSATION PROGRAM ADMINISTRATION

The State of North Carolina is self-insured for workers' compensation. Prior to 1996, the State's workers' compensation program was self-administered by each state agency. Presently only the Department of Transportation self-administers its program. The workers' compensation programs of the other agencies are administered by Key Risk Management Services.

The 1995 General Assembly established a three-year pilot program using an outside third party administrator in an effort to reduce the cost of claims filed by state employees. Key Risk Management Services was selected as the third party administrator for the pilot program. In late 1998, Key Risk was awarded a contract to administer the State's workers' compensation programs for up to 63 months beginning April 1, 1999, in exchange for a fee for each claim handled. Following the contract

¹ Narendra Ghosh, J.D., of Patterson Harkavy LLP was invaluable in the update of the latest edition of this paper.

² An earlier edition of this paper was submitted for review to the Teachers' and State Employees' Retirement System of North Carolina in order to ensure its accuracy. We were informed that, based on the advice of the Attorney General's Office, the Retirement System would not give an opinion regarding whether the information contained in this paper was accurate.

³ See, e.g., Estes v. North Carolina State University, 89 N.C. App. 55, 365 S.E.2d 160 (1988), appeal after remand 102 N.C. App. 52, 401 S.E.2d 384 (1991).

expiration in 2004, the process was re-opened for proposals and bidding. Key Risk was again selected as administrator and continues to operate under the 2004 contract. The terms of the contract and procedures for administering claims and decisions on liability and disability, medical and litigation management, and personnel training are contained in the State's request and Key Risk's proposal.⁴

The workers' compensation programs for the county and city boards of education are the responsibility of the State's Board of Education. N.C.G.S. § 115C-337(a). Key Risk Management Services was awarded a contract to serve as the administrator for workers' compensation for employees of the State's Department of Public Instruction and local school systems for three years beginning in 2001 and again in 2004.⁵ The current contract runs through 2007 and Key Risk is negotiating an extension.

III. STATE EMPLOYEE ELIGIBILITY FOR BENEFITS

All North Carolina state government employees are eligible to receive workers' compensation, including all agency and university employees and officers, state elected officials, and members of the General Assembly. In addition, part-time and temporary employees of the State, in addition to full-time employees, may receive workers' compensation. N.C.G.S. § 97-2(3); North Carolina Office of State Personnel, State Personnel Manual [hereinafter "Personnel Manual"], § 6, at 7, 11.⁶

A more limited number of employees are covered by the benefits administered by the Teachers' and State Employees' Retirement System of North Carolina, which administers short and long-term disability benefit plans and a retirement benefit plan. To be a member of the Teachers' and State Employees' Retirement System, an employee must be: a permanent full-time teacher or employee of a state-supported board of education or community college, or a permanent employee of the State or its agencies and work at least 30 hours per week for 9 months a year. N.C.G.S. § 135-3(1), 135-1(10), (25). Coverage under the plan ends once an employee terminates employment with the State, withdraws accumulated contributions, or dies. N.C.G.S. § 135-3(3).

IV. RELATIONSHIP BETWEEN STATE EMPLOYEE BENEFITS AND THE WORKERS' COMPENSATION SYSTEM

⁴ Attached as Appendix A is the accepted proposal for Third Party Workers' Compensation Administration.

⁵ Key Risk's April 2004 proposal to administer this program was patterned on its earlier proposal for other state agencies. It is attached as Appendix B.

⁶ Relevant excerpts of the State Personnel Manual, Section 6 are attached to this paper as Appendix C. The Office of State Personnel's workers' compensation handbook for employees is attached as Appendix D. These documents may be obtained online at www.osp.state.nc.us.

A. Legal Waiting Period

State employees who suffer an injury on the job or contract an occupational disease are expected to apply for workers' compensation benefits.⁷ Personnel Manual § 6, at 8. Like non-state employees, state employees will have a seven-day waiting period before they become eligible to obtain workers' compensation benefits. N.C.G.S. § 97-28. During this time, some employees will be able to receive their normal pay by taking accrued sick or vacation leave.

Employees who miss work because of their disability and have accrued sick or vacation leave can, but are not required, to use this leave to receive their normal salary during the waiting period. N.C.G.S. § 135-104; Personnel Manual § 6, at 11-12. Under the workers' compensation system, these workers will later be paid at the usual workers' compensation weekly rate for this period of time if the period of disability lasts more than twenty-one days. N.C.G.S. § 97-28. The amount of workers' compensation later paid for this period is not offset against the amount paid for sick or vacation leave. However, the sick or vacation time used will still be considered used and no longer available to the employee. Personnel Manual § 6, at 12.

Employees who have no accrued sick or vacation leave or elect not to use accrued leave will not be paid during the seven-day waiting period for workers' compensation benefits. Id. If the disability lasts more than twenty-one days, the workers' compensation system would then pay the normal workers' compensation benefit due for this period of time. Id.

B. Receipt of Workers' Compensation Benefits Following the Waiting Period

Once the waiting period has expired, state employees eligible for workers' compensation benefits are required to draw them and go on "workers' compensation leave." Personnel Manual § 6, at 7, 11. In addition, these employees may be able to receive wage replacement benefits from: 1) accrued vacation and sick leave; 2) the State's short-term disability plan; 3) the State's long-term disability plan; and 4) the State's retirement plan. Whether workers' compensation benefits will be offset against these benefits will depend on the type of state benefit and the type of workers' compensation benefit at issue.

While on "workers' compensation leave," an employee continues to accumulate vacation and sick leave which is credited to the employee's account for use upon return to work. Personnel Manual § 6, at 13.

⁷ Certain categories of employees, including law enforcement officers and teachers injured by an act of violence, will not draw periodic workers' compensation benefits during the first one or two years of disability. These employees are covered by special statutory provisions that ensure that they will receive a full salary during these years. See infra at Part IV.C.

1. Accrued vacation and sick leave and return to work

Employees who receive workers' compensation benefits and who miss work as a result of their disability are eligible to use accrued vacation or sick leave to supplement their workers' compensation benefits.⁸ Personnel Manual § 6, at 12. An employee's workers' compensation benefits will generally amount to two-thirds of his or her regular salary subject to a maximum cap.⁹ Under the State's supplemental income program, the employee can use a set amount of earned vacation leave or sick leave each week in accordance with a schedule published each year by the Office of State Personnel. Personnel Manual § 6, at 12. The schedule sets out the amount of vacation and sick leave that may be used each week in order roughly to approximate the employee's pre-injury income.

The supplemental income program is not available to employees who have no accrued vacation or sick leave. By the same token, it is not available to employees whose employment is terminated because they will not be able to return to their jobs; these employees are paid their accumulated vacation and sick leave (including leave accumulated only during the first twelve months of workers' compensation leave) in a lump sum. Finally, this program is not available to those who are placed in a light duty job that pays less than their normal salaries. Personnel Manual § 6, at 12-13.

The state Personnel Manual specifically addresses the treatment of employees who have been released to return to work. Prior to "maximum medical improvement," if unable to perform the original position, the employee is to be placed in temporary limited work "suitable to the employee's capacity which is both meaningful and productive and advantageous to the employee and the agency." Personnel Manual § 6, at 9-10.

At maximum medical improvement, if able, the employee is to be returned to the original or equivalent position. If not able to perform such work, the state agency is to attempt to place the employee in another suitable position which is mutually advantageous and "is both meaningful and productive." If a suitable position is unavailable, the employee is to be given the first suitable vacancy and receive "work placement efforts." Personnel Manual § 6, at 10-10.1. The state agency is to "request stop payment of compensation and implement dismissal procedures" when the employee is at maximum medical improvement and "refuses suitable employment in keeping with the employee's capacity." Personnel Manual § 6, at 10.1.

⁸ Employees eligible for workers' compensation benefits may not draw accrued vacation or sick leave pay in lieu of accepting benefits. Employees eligible for workers' compensation benefits are required to draw workers' compensation benefits and may use accrued vacation and sick leave only to supplement these benefits. State Personnel Manual, § 6, at 11-12.

⁹ As of January 1, 2007, the maximum weekly rate of compensation was \$754.00 for injuries occurring after that date. The maximum weekly rate for injuries occurring after January 1, 2008, is \$786.00.

2. Short-term disability plan

The State provides a short-term disability plan for disabled¹⁰ employees who meet eligibility requirements.¹¹ The short-term disability plan begins to pay benefits following a 60-day waiting period. N.C.G.S. § 135-104(a). After that time, disabled employees receive benefits for 365 days, although they may also receive an additional 365 days of benefits if the State's Medical Board determines that they will likely be able to return to work during that period. N.C.G.S. § 135-105(b), (g).

Short term disability benefits are offset dollar-for-dollar by periodic workers' compensation benefits for temporary partial or temporary or permanent total disability.¹² N.C.G.S. § 135-105(c); Benefits Pamphlet, at 30. The short-term disability plan provides that employees will receive approximately 50 percent of their pre-injury weekly

¹⁰ By statute, disability is defined as: "[t]he mental or physical incapacity for the further performance of duty of a participant or beneficiary; provided that such incapacity was not the result of terrorist activity, active participation in a riot, committing or attempting to commit a felony, or intentionally self-inflicted injury." N.C.G.S. § 135-101(6). The Trustees of the Retirement System require that an employee be incapacitated only in the performance of his or her usual occupation. Teachers' and State Employees' Retirement System of North Carolina publication, "Your Retirement Benefits," January 2007 [hereinafter "Benefits Pamphlet"], at 28. (This publication is online at www.treasurer.state.nc.us.)

¹¹ To be eligible for short-term disability benefits, employees must: 1) have at least one year of contributing membership service in the Retirement System earned within 36 calendar months preceding the disability; 2) be found to be mentally or physically disabled for the further performance of their usual occupation; and 3) have had the disability continuously and incurred at the time of active employment. N.C.G.S. § 135-105(a); Benefits Pamphlet, at 29. There is no requirement that an application for short-term disability be filed by any particular time.

¹² Workers' compensation benefits for a "permanent partial disability rating" do not offset short-term disability benefits. N.C.G.S. § 135-101(21). See infra at 6. In addition, social security benefits do not offset short-term disability benefits. Benefits Pamphlet, at 30. A 1994 amendment provides for the offset from short-term and long-term disability benefits of "any monthly payments from the federal Veterans Administration, any other federal agency, or any payments made [for disability from National Guard Service] to which the participant may be entitled on account of the same disability." N.C.G.S. §§ 135-105(c), -106(b) (emphasis added). The Retirement System, however, does not apply this amendment to offset social security benefits from short-term disability. The legislative history and preexisting offset of social security from long-term disability benefits support the Retirement System's view that this language was enacted as authority to offset only government payments to veterans on account of the same disability for which the participant is receiving disability benefits. Benefits Pamphlet, at 30-31; Sess. Laws 1993 (Reg. Sess., 1994), ch. 769, secs. 7.30(s)-(v).

pay.¹³ Because workers' compensation benefits generally provide two-thirds of an employee's average weekly earnings, usually the workers' compensation benefits will completely offset the short-term disability plan's benefits.¹⁴

The workers' compensation lawyer should be aware of two features relating to the offset. First, even if an employee will draw only minimal benefits from the disability plan because of the offset, it may still be in the employee's interest to apply and qualify for short-term disability benefits. Those employees who are paid any monthly benefits under the short-term disability plan will earn retirement credits for the time they receive these benefits. N.C.G.S. § 135-4(y). In contrast, workers who receive solely workers' compensation do not automatically earn retirement credits and must, instead, buy them for a lump sum payment shared between the employee and employer. N.C.G.S. § 135-4(r); Personnel Manual § 6, at 14.¹⁵

Second, although periodic workers' compensation benefits for all total disability under N.C.G.S. § 97-29 and for partial disability based on wage loss under N.C.G.S. § 97-30 are offset from short-term disability benefits, compensation for a permanent partial disability rating pursuant to N.C.G.S. § 97-31 is not offset. N.C.G.S. § 135-101(21); N.C.G.S. § 135-105(c); Benefits Pamphlet, at 30. Consequently, at the time an employee who is partially disabled reaches maximum medical improvement, it may be to his or her advantage to accept compensation based on a rating under N.C.G.S. § 97-31 rather than to continue receiving benefits based on wage loss under N.C.G.S. § 97-30 in order to avoid the offset. See Gupton v. Builders Transport, 320 N.C. 38, 357 S.E.2d 674 (1987).

3. Long-term disability plan

Following the cessation of short-term disability benefits, eligible disabled state employees may receive benefits from the State's long-term disability plan.¹⁶ N.C.G.S. §

¹³ Under the disability plan, an employee's monthly short-term benefit will equal 50 percent of 1/12th of his or her annual base rate of compensation prior to the beginning of the short-term benefit period, plus 50 percent of 1/12th of his or her annual longevity payment, if any, to a maximum of \$3,000 per month. N.C.G.S. § 135-105(c); Benefits Pamphlet, at 30.

¹⁴ Highly-paid employees may be an exception to this general rule. These employees will receive less than two-thirds of their regular pay because of the maximum weekly rate on workers' compensation benefits. Depending on their salary, these employees' benefits under the disability plan may not be completely offset by workers' compensation, as the maximum rate payable for benefits under the disability plan is higher than that paid for workers' compensation benefits.

¹⁵ Employees whose short-term disability benefits are completely offset by workers' compensation will not earn retirement credits, as the statute requires that an employee be both "eligible for" and "paid" disability plan benefits to earn retirement credits for that month. N.C.G.S. § 135-4(y) (emphasis added).

¹⁶ Employees are eligible to receive long-term disability benefits for as long as they

135-106(a). Eligibility for these benefits, however, is conditioned on the termination of state employment. In the absence of an application for long term disability, the disabled employee will be able to continue on "workers' compensation leave" until the state agency employer determines that circumstances justify termination on the basis of "unavailability." Personnel Manual § 11, at 2.¹⁷ An employee on "workers'

remain disabled until they are eligible for unreduced service retirement. N.C.G.S. § 135-106(b). Employees are eligible for long-term disability benefits if they: 1) have at least five years of contributing membership service in a retirement system earned within 96 calendar months prior to the end of the short-term disability period; 2) apply to receive long-term benefits within 180 days after the end of the short-term disability, salary continuation payments, or monthly workers' compensation payment (apparently excluding payments for ratings for permanent partial disability), whichever occurs later; 3) are certified mentally or physically incapacitated for further performance of duty by the medical board, where the disability has been continuous, is likely to be permanent, and is incurred at the time of active employment; and (4) terminate their employment as a state employee. N.C.G.S. § 135-106(a); Session Law 2007-325, § 2 (Jul. 31, 2007). The 2007 edition of the Benefits Pamphlet reflects the wrong standard for long-term disability in light of the recent amendment to the provision in July 2007. See Benefits Pamphlet, at 28; Session Law 2007-325 § 2.

¹⁷ See supra at 4, for discussion of treatment of employees released to work. The policy for "separation due to unavailability when leave is exhausted" provides:

An employee may be separated on the basis of unavailability when the employee becomes or remains unavailable for work after all applicable leave credits have been exhausted and agency management does not grant a leave without pay, or does not extend a leave without pay period, for reasons deemed sufficient by the agency. Such reasons include, but are not limited to, lack of suitable temporary assistance, criticality of the position, budgetary constraints, etc.

...

Prior to separation, the employing agency shall notify the employee in writing of the proposed separation, the efforts undertaken to avoid separation and why the efforts were unsuccessful. The employing agency must also give the employee a letter of separation stating the specific reasons for the separation and setting forth the employee's right of appeal.

The burden of proof on the agency in the event of a grievance is not just cause, as that term exists in G.S. 126-35. Rather, the agency's burden is to prove that the employee was unavailable, that reasonable efforts were undertaken to avoid separation, and the reason the efforts were unsuccessful.

Involuntary separation pursuant to the policy may be grieved or appealed. The employing agency must also give the employee a letter of separation stating the specific reasons for the separation and setting forth the employee's right of appeal. The burden of proof on the agency in the event of a grievance is not just cause, as that term exists in G.S. 126-35.

compensation leave", therefore, will want to consider whether he or she should delay applying for these benefits in order to retain the option of returning to work. A 365 day extension for benefits under the short term disability plan is available in these circumstances if the State's Medical Board determines that the disability continues to be temporary and the employee will likely return to work during the extended period. N.C.G.S. § 135-105(b),(g).

As with short term disability benefits, there is a dollar-for-dollar offset against long-term disability benefits of weekly workers' compensation benefits for temporary partial disability under N.C.G.S. § 97-30 or for temporary or permanent total disability under N.C.G.S. § 97-29. N.C.G.S. § 135-101(21), N.C.G.S. § 135-106(b); Benefits Pamphlet, at 31.¹⁸ During the first 36 months of long-term disability, the monthly long-term benefit will equal approximately 65 percent of the employee's salary,¹⁹ offset by applicable workers' compensation or any social security disability or retirement benefits the employee "may be entitled" to receive, whether or not he or she elects to receive the retirement benefit.²⁰ N.C.G.S. § 135-106(b).

Rather, the agency's burden is to prove that the employee was unavailable, that the agency considered the employee's proposed accommodations for the unavailability and were unable to make the proposed accommodations or other reasonable accommodations.

Agencies should make efforts to place an employee when the employee becomes available, if the employee desires, consistent with other employment priorities and rights. However, there is no mandatory requirement placed on an agency to secure an employee, separated under this policy, a position in any agency.

¹⁸ In David v. N.C. Department of Correction, I.C. 606302 (Full Comm'n Nov. 29, 2000), a divided Full Commission ruled that the Department of Correction was entitled to a "dollar for dollar credit" for the long term disability payments received by the employee. In her dissent, Commissioner Ballance pointed out that the Retirement System, not the agency, gets the credit in these circumstances.

¹⁹ By statute, the employee will receive 65 percent of 1/12th of the annual base rate of compensation prior to the beginning of the short-term benefit, plus 65 percent of 1/12th of the annual longevity payment, if any, to a maximum of \$3,900 per month. N.C.G.S. § 135-106(b); Benefit Pamphlet, at 31.

²⁰ Accordingly, the long-term benefit will be offset by the amount of the reduced social security retirement benefit of any employee age 62 or older, whether or not the employee applies for these benefits. The long-term benefit, however, will not be offset by the amount of a social security disability benefit during the first 36 months unless the employee has actually been awarded these benefits. An employee who is totally disabled and insured under the social security system is entitled to receive social security benefits following a five-month waiting period. Employees age 65 and older, and who are insured under the system, are entitled to receive full social security retirement benefits. Disabled employees between 62 and 65 years of age have a

The July 2007 amendment to the long-term disability provision has altered the benefits scheme after the first 36 months of benefits. For employees who have not vested benefits as of July 31, 2007 (i.e. they did not have 5 years of service), long-term benefits cease after 36 months unless the employee has been approved and is in receipt of primary Social Security disability benefits. N.C.G.S. § 135-106(b); Session Law 2007-325 §§ 2, 4. The long-term benefit is then reduced by an amount equal to the awarded social security disability benefit. Id.²¹ For employees who have vested benefits as of July 31, 2007, long-term benefits continue after 36 months, but are reduced by an amount equal to the social security disability benefit to which the worker would have been entitled had he or she been awarded social security disability benefits. N.C.G.S. § 135-106(b); Session Law 2007-325 § 4. As with short-term disability benefits, long-term disability benefits will, therefore, generally be largely offset by workers' compensation and social security benefits.²² However, an employee eligible for long-term disability will automatically receive the \$10.00 minimum payment per month from the long-term disability plan, regardless of the amount of other benefits received. Id.

The present practice of the Board of Trustees of the Retirement System is to limit the offset for workers' compensation to the net amount after reduction for attorney's fees deducted and paid by the state agency directly to the employee's attorney. See Hunt v. N.C. State Univ., I.C. No. 839851, at Conclusion #4 (Dep. Comm'r Feb. 28, 2006) ("Defendants' credit for said disability benefits is reduced by the amount necessary to provide counsel for Plaintiff with an attorney's fee of 25% of the indemnity benefits due Plaintiff."), rev'd on other grounds by I.C. No. 839851 (Full Comm'n Apr. 13, 2007). This practice is consistent with the decisions of the North Carolina Court of Appeals on the treatment of attorney's fees paid by social security claimants. The Court of Appeals has held that the offset for social security disability benefits is limited to the net benefit amount after deduction of the beneficiary's attorneys' fees. Willoughby v. Board of Trustees, 121 N.C. App. 444, 466 S.E.2d 285 (1996); Smith v. Board of Trustees, 122 N.C. App. 631, 471 S.E.2d 121 (1996). The court reasoned that the beneficiary was not "entitled" within the meaning of N.C.G.S. § 135-106(b) to the

choice between receiving social security disability or reduced social security retirement benefits. The age at which an employee is entitled to the full social security retirement benefit increases incrementally for employees born after 1937 until it is age 67 for employees born in 1960.

²¹ If the long-term benefit ceases after 36 months, the benefit may later be restored retroactively to the date of cessation, however, if the Social Security Administration "grants a retroactive approval" for the disability benefit with a "benefit effective date" within the first 36 months of the long-term disability period. Id.

²² Highly-paid employees may be an exception to this general rule. These employees will receive less than two-thirds of their regular pay because of the statutory cap on workers' compensation benefits. Depending on their salary, these employees' benefits under the disability plan may not be completely offset by workers' compensation benefits as the maximum rate payable for benefits under the disability plan is significantly higher than that paid for workers' compensation benefits.

amount statutorily reserved and paid directly by the Social Security Administration to the beneficiary's attorney as fees. The court, however, drew a distinction between the attorneys' fees paid directly to the attorney and the costs which the beneficiary reimbursed to his attorney. The offset thus was not reduced by the expenses the beneficiary reimbursed to his attorney. Willoughby v. Board of Trustees.²³

The same features relevant to a workers' compensation lawyer with respect to short-term disability benefits are also relevant with respect to long-term disability benefits. First, as with short-term disability, it may be in the employee's interest to apply and qualify for long-term disability even if, due to the workers' compensation offset, he or she will receive only the \$10.00 minimum monthly payment. Those employees who do so will earn retirement credits for the time they receive even this minimal amount of disability benefits. N.C.G.S. §135-4(y). Employees who receive solely workers' compensation do not automatically earn retirement credits and must, instead, buy them for a lump sum payment shared between the employee and employer. N.C.G.S. §135-4(r).

Second, although the Teachers and State Employees' Retirement System offsets workers' compensation periodic benefits for total disability pursuant to N.C.G.S. § 97-29 and for partial disability based on wage loss pursuant to N.C.G.S. § 97-30, it does not offset benefits for permanent partial disability based on acceptance of a rating pursuant to N.C.G.S. § 97-31. N.C.G.S. §§ 135-101(21), 135-106(b); Benefits Pamphlet, at 31. Consequently, at the time an employee who is partially disabled reaches maximum medical improvement, it may be to his or her advantage to accept compensation based on a rating under N.C.G.S. §97-31 rather than receive benefits based on wage loss under N.C.G.S. §97-30 in order to avoid the offset. See Gupton v. Builders Transport, 320 N.C. 38, 357 S.E.2d 674 (1987).

4. State Employees' Retirement Plan

The receipt of workers' compensation benefits has no effect on the amount of retirement benefits received.²⁴ Once an employee becomes eligible for unreduced

²³ The Court of Appeals also concluded in Smith v. Board of Trustees that widow's insurance benefits under the Social Security Act are "separate and different from social security disability benefits" and accordingly are not subject to offset from the long-term disability benefit under N.C.G.S. § 135-106(b).

²⁴ Workers' compensation benefits also have no effect on pension benefits of local government employees participating in the State's retirement system. Employees of counties and cities and other local governmental units are covered by the Local Government Employees' Retirement System if their employer has agreed to participate. N.C.G.S. § 128-23. A local government employee is entitled to a disability retirement benefit if permanently disabled from performing his or her job after five years of creditable service or after one year of creditable service if a law enforcement officer, fireman or rescue squad worker disabled from an accident in the performance of duties. N.C.G.S. § 128-27(c). Following the Court of Appeals decision in Cox v. City of

retirement benefits,²⁵ benefits from the State's long-term disability plan will cease. N.C.G.S. §135-106(b).

5. The Faulkenbury Decision

The previous discussion of the state disability program applies only to employees who retired after January 1, 1988. A different system applied to employees who retired before that date, when the present short term and long term disability programs did not exist. Before January 1, 1988, disabled employees who qualified received "disability retirement" benefits from the State. Unlike the payments from the present short and long-term disability programs, these retirement payments were not offset by workers' compensation or social security benefits.

As a result of the Supreme Court's decision in Faulkenbury v. Teachers' & State Employees' Retirement System, 345 N.C. 683, 483 S.E.2d 422 (1997), the option to accept "disability retirement benefits" in lieu of short term and long term disability benefits still exists for employees (a) who have five years of membership service and thus were vested in the State Retirement System on January 1, 1988 and (b) who become disabled following this date. These employees may elect to receive a "disability retirement" benefit with no offset for workers' compensation or social security in lieu of the present short and long term disability plan benefits. The "disability retirement" normally will yield more generous benefits and thus usually should be selected by qualified employees. Since this is not always true, however, an individual assessment - including income tax considerations -- is required. It may be more advantageous, for example, for an employee to select benefits under the Disability Income Plan when there is limited life expectancy because of the life insurance available under this plan or when disability occurs close to age 65.

Winston-Salem, 157 N.C. App. 228, 578 S.E. 2d 669 (2003), the Commission denied a credit to the public employer for disability retirement benefits paid under the Local Government Employees' Retirement System because the benefits were the result of joint employee/employer contributions. Cox v. City of Winston-Salem, I.C. 910497 (April 5, 2004).

²⁵ Workers' compensation benefits have no effect on unreduced retirement benefits and reduced early retirement benefits. An employee who is not a law enforcement officer is eligible for unreduced benefits after: 1) he or she reaches age 65 and completes 5 years of creditable service; or 2) he or she reaches age 60 and completes 25 years of creditable service; or 3) he or she completes 30 years of creditable service at any age. A law enforcement officer is eligible for unreduced retirement benefits after: 1) he or she reaches age 55 and completes 5 years of creditable service; or 2) he or she completes 30 years of creditable service. An employee who is not a law enforcement officer is eligible for reduced early retirement benefits after: 1) he or she reaches age 50 and completes 20 years of creditable service; or 2) he or she reaches age 60 and completes five years of service. A law enforcement officer is eligible for reduced early retirement benefits after he or she reaches age 50 and completes 15 years of creditable service. N.C.G.S. § 135-5(b16).

The Retirement System provides employees qualified to make this election with a comparison of the benefits payable under the present long term disability plan and "disability retirement" under the Faulkenbury decision.²⁶

C. Special Salary Continuation Plan For Law Enforcement Officers And Other Designated Positions

The State provides a special salary continuation plan for law enforcement officers and specific other employees²⁷ who are disabled in the course of their official duties.

²⁶ The Retirement Systems' standard letter explaining the alternatives is attached as Appendix E.

²⁷ § 143-166.13. Persons entitled to benefits under Article.

(a) The following persons who are subject to the Criminal Justice Training and Standards Act are entitled to benefits under this Article:

- (1) State Government Security Officers, Department of Administration;
- (2) State Correctional Officers, Department of Corrections;
- (3) State Probation and Parole Officers, Department of Corrections;
- (4) Sworn State Law-Enforcement Officers with the power of arrest, Department of Corrections;
- (5) Alcohol Law-Enforcement Agents, Department of Crime Control and Public Safety;
- (6) State Highway Patrol Officers, Department of Crime Control and Public Safety;
- (7) General Assembly Special Police, General Assembly;
- (8) Sworn State Law-Enforcement Officers with the power of arrest, Department of Human Resources;
- (9) Juvenile Justice Officers, Department of Juvenile Justice and Delinquency Prevention;
- (10) Insurance Investigators, Department of Insurance;
- (11) State Bureau of Investigation Officers and Agents, Department of Justice;
- (12) Director and Assistant Director, License and Theft Enforcement Section, Division of Motor Vehicles, Department of Transportation;
- (13) Members of License and Theft Enforcement Section, Division of Motor Vehicles, Department of Transportation, designated by the Commissioner of Motor Vehicles as either "inspectors" or uniformed weigh station personnel;
- (14) Utilities Commission Transportation Inspectors and Special Investigators;
- (15) North Carolina Ports Authority Police, Department of Commerce;
- (16) Sworn State Law-Enforcement Officers with the power of arrest, Department of Environment, Health, and Natural Resources;
- (17) Sworn State Law-Enforcement Officers with the power of arrest, Department of Crime Control and Public Safety;

N.C.G.S. § 143-166.14.²⁸ Under this plan, covered employees will receive their full salary for a period of two years from the date the employee is incapacitated. *Id.* A special provision for teachers and other employees of state educational institutions injured in an act of violence provides them their full salary for up to one year. N.C.G.S. § 115C-338(a),(b). During the time these provisions apply, employees will be ineligible to receive workers' compensation for total or partial disability based on wage loss under N.C.G.S. § 97-29 and § 97-30. N.C.G.S. §§ 143-166.16, 115C-338(b). However, they are eligible to receive all other benefits under the Workers' Compensation Act, including compensation for a permanent partial disability rating pursuant to N.C.G.S. §97-31. *Id.* At the end of this period of time, these employees will be treated like other state employees, and will be subject to all provisions of the North Carolina Workers' Compensation Act.²⁹ N.C.G.S. § 143-166.14, 143-166.16. The statutory scheme thus may favor acceptance of a permanent partial disability rating under N.C.G.S. §97-31 where an employee is partially disabled, as benefits under that section may be available whereas the benefits under §97-30 may not be awarded during the salary replacement period.

V. SETTLEMENT OF WORKERS' COMPENSATION CLAIMS

A. Offset of Benefits

The existence of the offset for workers' compensation total and partial benefits based on wage loss against the State's short- and long-term disability benefits

(18) Sworn State Law-Enforcement Officers with the power of arrest, Department of Revenue;

(19) Sworn State Law-Enforcement Officers with the power of arrest, University System.

(b) The following persons are entitled to benefits under this Article regardless of whether they are subject to the Criminal Justice Training and Standards Act:

(1) Driver License Examiners injured by accident arising out of and in the course of giving a road test, Division of Motor Vehicles, Department of Transportation.

(2) Employees of the Department of Correction injured by a direct and deliberate act of an offender supervised by the Department or while performing supervisory duties over offenders which place the employees at risk of such injury.

²⁸ Note that deputy sheriffs are not included within this plan.

²⁹ Employees covered by the law enforcement salary replacement program will have two years following the end of the period in which salary is paid to file their workers' compensation claim. N.C.G.S. §§ 143-166.16, 97-24. This statute provides that the state department head shall determine the "cause of the incapacity and to what extent the claimant may be assigned to" alternative work. The decision of the department head is filed with the North Carolina Industrial Commission and becomes final unless the claimant within 30 days files a request for hearing before the Commission. N.C.G.S. §§ 143-166.18 - 166.19.

introduces a notable anomaly for the workers' compensation lawyer. Presently, the Board of Trustees of the Retirement System will not impose the offset to final settlement agreements or "clincher", as it views payments under such agreements as a compromise of a disputed claim and something other than "disability income benefits under the North Carolina Workers' Compensation Act." N.C.G.S. § 135-101(21).³⁰ The consequence of this treatment of clincher agreements is that, where the worker qualifies for disability benefits under the State's plan, it may be exceedingly advantageous for him or her to enter into a clincher agreement. Because the offset would be avoided following the clincher, the employee's total monthly benefit would remain the same and the employee would, besides, receive the payment from the clincher agreement. Thus, even clinchers that give the employee significantly less than the present value of the expected workers' compensation benefits may be in the employee's interest.

It is important to note that the policy of the Board of Trustees may be subject to change concerning the imposition of the offset. The practitioner should be aware that reliance on the present policy could result in a reduced recovery in the future. Care should be taken to ameliorate the potential danger with language concerning the categorization of the lump sum in the compromise settlement agreement.

The financial incentive to enter a clincher is less the closer the employee is to attaining an unreduced service retirement, as long-term disability benefits would cease once an employee becomes eligible for retirement, although workers' compensation benefits would continue.

B. The State Comprehensive Major Medical Plan

The State of North Carolina Teachers' and State Employees' Comprehensive Major Medical Plan ("State Health Plan") has a right to recover excess payments made to any persons, insurance companies or other organizations. N.C.G.S. §135-40.13(g). However, those rights were significantly expanded by the passage of a statutory provision effective July 1, 2004, and amended on August 27, 2006, establishing a right of subrogation, a right of first recovery against liable third parties, and a lien on damages recovered by the third party.³¹ The plan has contracted with an outside company in order to facilitate recovery of such payment.³²

³⁰The "no offset" policy was confirmed with the Retirement Systems in November 2007.

³¹ N.C.G.S. § 135-40.13A. Liability of third person; right of subrogation; right of first recovery:

(a) The Plan shall have the right of subrogation upon all of the Plan member's right to recover from a liable third party for payment made under the Plan, for all medical expenses, including provider, hospital, surgical, or prescription drug expenses, to the extent those payments are related to an injury caused by a liable third party. The Plan member shall do nothing to prejudice these rights. The Plan has the right to first recovery on any amounts so recovered, whether by the Plan or the Plan member, and whether recovered by litigation, arbitration, mediation, settlement, or otherwise. Notwithstanding any other provision of law to the contrary, the recovery limitation set

The State Health Plan has advised that the primary purpose of the statute was to allow recovery of payments in tort claims. While the language of the statute mirrors that of tort actions (“damages” and “liable third party”), full consideration of the potential implications to workers’ compensation claimants has not been made. However, in the event that the Plan should seek subrogation in a settled workers’ compensation claim, the provisions of N.C.G.S. § 97-17 should apply.

Further, it should be noted that an issue exists regarding whether the State Employee's health plan covers work-related injuries following a final settlement. The State Health Plan specifically excludes charges “for services rendered in connection with any occupational injury or disease arising out of and in the course of employment with any employer, if (i) the employer furnishes, pays for or provides reimbursement for such charges, or (ii) the employer makes a settlement payment for such charges, or (iii) the person incurring such charges waives or fails to assert his or her rights respecting such charges.” N.C.G.S. § 135-40.7(4). Accordingly, the employee's lawyer should consider whether specific provision should be made at the time of settlement for coverage for future medical expenses.

The attorneys in the Workers' Compensation and Tort Claims Section of the North Carolina Attorney General's Office work with these issues daily. They can be

forth in G.S. 28A-18.2 shall not apply to the Plan's right of subrogation of Plan members.

(b) If the Plan is precluded from exercising its right of subrogation, it may exercise its rights of recovery pursuant to G.S. 135-40.13(g). If the Plan recovers damages from a liable third party in excess of the claims paid, any excess will be paid to the member, less a proportionate share of the costs of collection.

(c) In the event a Plan member recovers any amounts from a liable third party to which the Plan is entitled under this section, the Plan may recover the amounts directly from the Plan member. The Plan has a lien, for not more than the value of claims paid related to the liability of the third party, on any damages subsequently recovered against the liable third party. If the Plan member fails to pursue the remedy against a liable third party, the Plan is subrogated to the rights of the Plan member and is entitled to enforce liability in the Plan's own name or in the name of the Plan member for the amount paid by the Plan.

(d) In no event shall the Plan's lien exceed fifty percent (50%) of the total damages recovered by the Plan member, exclusive of the Plan member's reasonable costs of collection as determined by the Plan in the Plan's sole discretion. The decision by the Plan as to the reasonable cost of collection is conclusive and is not a "final agency decision" for purposes of a contested case under Chapter 150B of the General Statutes. Notice of the Plan's lien or right to recovery shall be presumed when a Plan member is represented by an attorney, and the attorney shall disburse proceeds pursuant to this section.

³²The information sent to an attorney requesting a reduction in the lien and to Plan participants is attached as Appendix F.

consulted regarding the proper way to structure clincher agreements to address medical insurance issues and avoid offsets.

VI. CONCLUSION

With careful attention to the relevant statutes, regulations, and provisions of the benefit plans available to state employees, the workers' compensation attorney can structure an employee's benefits under the various applicable plans to maximize the benefits received by the employee.