Does Your Organization Practice Risk Management?

PARMA February 9, 2023

Recognize where the risk function fits in your organization and is that optimal

Depending on where you are in the risk process, you will get something from this presentation. If some of it seems too wonky, stay with it as it will mean something one day.

Also always be grateful to who mentored you along the way.

To me that was Ed Godwin and Tom Vance.

Ed passed away last summer as a result of illness from exposure in Vietnam in the sixties. Ed taught many through the IEA for twenty years and he was my boss and mentor at US Rentals.

Tom Vance and I met when I joined RIMS in 1988 and then I worked for him for twenty years.

Public Entity Risk Definition Discussed here today

For purposes of this presentation, we limit the presentation to Hazard Risk emanating from property, liability, and personnel exposures.

Operational, Financial and Strategic Risk are important, but most of what everyone in the room handles falls within the Hazard Risk arena.

Learning Objectives Today

- History of Public Entity Risk and Pooling
- Audience will learn something to take back
- Where Risk Management fits in the organization
- Reports and Elements of Risk Management
- Real World Examples and Tools to be Effective
- How to improve knowledge and standing in the profession

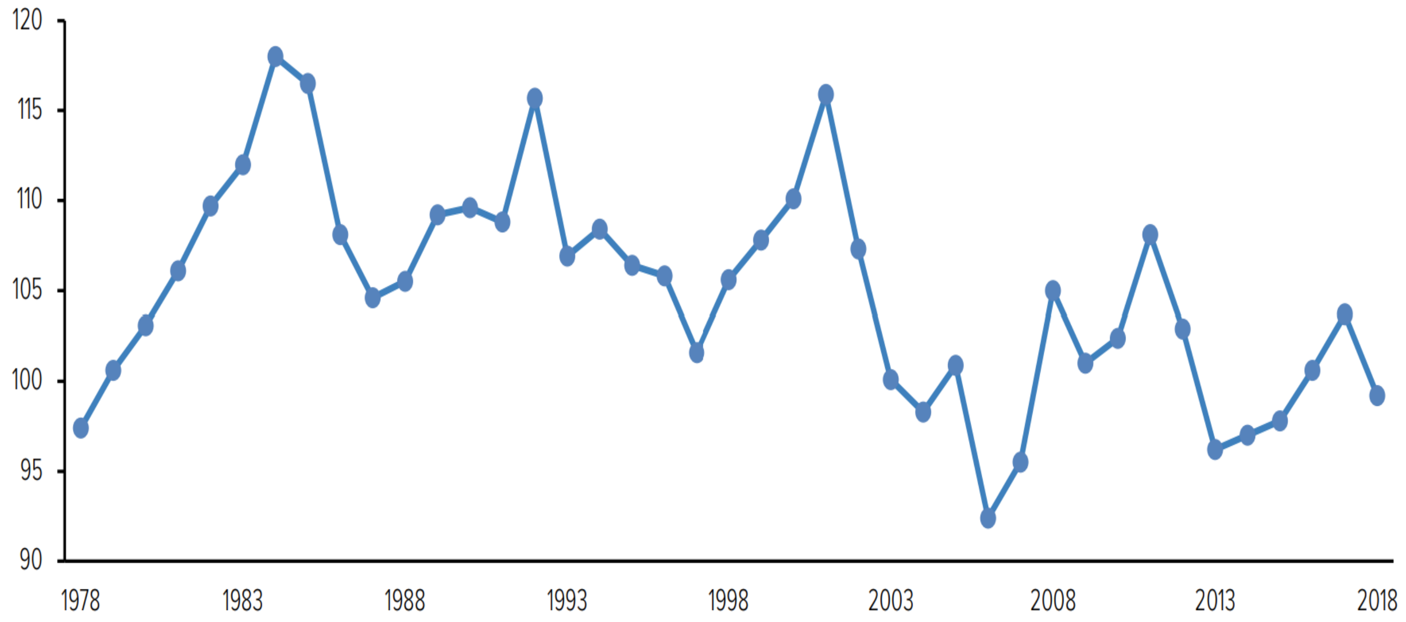
History of Risk Management in the Public Sector

- Pooling Workers’ Compensation late 70’s
- Pooling Liability mid-1980’s
- Why pooling?
- Where did the early Risk Managers come from?
  - Claims-General Adjustment Bureau (GAB), Aetna Claims School etc.
  - Underwriters
  - Brokers
  - Loss Control but to a lesser extent

Evolution of Risk Management and Insurance Cycle

- Combined Ratio = Losses + Expenses/ Earned Premium
- Combined Ratio below 100 equals an underwriting profit

Property/Casualty Insurance Combined Ratio, 1978-2018[1]



[1]Excludes state funds and other residual insurers.

Source: ISO®, a Verisk Analytics® business.

Impact to Total Cost of Risk for Public Entities due to good risk management Principles

- Pooling of mid-80's stabilized liability risk financing
- Late 80's psych claims struck public safety workers' compensation
- Workers' Compensation reform early 90's plus led to inexpensive pricing late 90's
- Success of pioneering risk managers resulted in a new status quo and caused the profession to become a victim of its success.
- Good risk management and risk modeling in the insurance industry led to a period of stable inexpensive cost of risk transfer
- New pools underwrote risks as if they could purchase insurance. That coupled with lower operating expenses and no profit motive and emphasis on loss control resulting in lower losses allowed capital in pools to accumulate

Rise and fall of knowledge base of Risk Managers in the Public Sector

- The 90's were a period of calm and stability. Rates stabilized in the liability market, property remained solid and workers' compensation enjoyed the results of the reforms early in the decade.

- Risk Managers achieved results and in the early 90's the original risk managers, most of whom had come from insurance companies late in their careers stated to retire. Retirement Wave Number 1.
- We won the cold war and in the early 90's we received "*The Peace Dividend*".
- *This Peace Dividend was not kind to public entity revenues when defense plants in many areas including Sunnyvale/San Jose, Long Beach and San Fernando Valley along with San Diego closed. Tax revenue plummeted.*
- Many entities as a result of revenue shortfalls instituted hiring freezes. The risk duties were assumed by assistants or secretary of the former Risk Manager with oversight or not from the Finance Director or Human Resources Director.

Organizations get lean and outsource specialty services

- Assistants who assumed risk roles lacked the insider knowledge of the insurance industry. Directors to whom they reported the increased scope of control and budget, but they were ignorant as well.
- This is the period in which the phrase *Our Broker Says,* or *The Pool Manager Says,* became common.
- 9/11 and the post recession hurt, but the event changed the property and excess workers' compensation markets.
- Enhanced retirement programs for public safety, 3@50 resulted in a binge of hiring. The average age of cops and firefighters dropped and in turn the incidence rates of severity of workers' compensation claims dropped. Auto accidents rose however, males under the age of 25 cause a lot of accidents even when they wear a badge.
- The recession of 2008-2011 hit revenue hard. Pension costs soared, layoffs occurred, positions unfilled and worst of all buy-outs of legacy employees including risk managers.

The New Normal, Borrow from Peter to Pay Paul

- Redevelopment Agencies dissolution, PEPRA, and the pension problems remain
- Governing bodies, Administrators, and Finance Directors discovered Claim Reserves.
- While in the past, reserves had been raided or funding confidence levels reduced, those had been short-term plans with a plan to backfill at a certain date. The challenge now became a permanent borrowing without a knowledgeable Risk Manager to explain the long-term nature of self-insurance. Pension funding was more important than loss funding. The feeling of hoping for better than expected results came in vogue.
- Losses struck with a vengeance, police liability, employment and sexual molestation hit the primary and excess liability market hard. Wildfires and the increased cost of construction resulted in historic rate increases for property insurance.
- The good news was that workers' compensation reform had worked and that line of risk remained relatively stable.

Where in the Organization should the Risk Function Report?

- The four areas to report in preferred order are:
    - Office of Chief Executive
    - Director of Finance
    - Human Resources
    - Office of Counsel
- Operating departments should have risk resources commensurate to their specific areas such as police liability and construction type work.
- Operating department loss control personnel should have a dotted line relationship to the enterprise-wide risk programs to ensure organizational consistency.

Why Administration is the best area to be located

- When part of Administration you hear more of what you need to hear.
- There is no filter from a department head that might not understand the organizational impact of an issue.
- Chief Administrator learns more about operations-no filter

Main Elements of a Risk Management Program

RISK ADMINISTRATION AND FINANCE

CLAIMS

INDUSTRIAL SAFETY

Risk Administration and Finance

- This area coordinates all programs including claims and industrial safety. Areas of specialization include:
  - Insurance Procurement
  - Pool Participation
  - Contractual Risk Transfer
  - Budget and Rate Making
  - Actuarial Analysis
  - Program Design
  - Internal Risk Consulting
- The larger the organization the more impact this area has on the savings to the entity.

Insurance and Pooling

- Determining what insurance to purchase or how to incorporate pooling into your program is more than a once a year task.
- Risks change, coverage changes and what worked in 1990 doesn’t necessarily work today.
- Coverage new to you? Fiduciary, Cyber, Drone, Med Mal, Deadly Weapons Coverage (not needed but it is hero coverage)

Contractual Risk Transfer

- Most in-house counsel do not have knowledge in how indemnification and insurance provisions coordinate.
- The insurance expert does. The risk manager is THE INSURANCE EXPERT
- Mutual indemnification provisions seldom achieve true risk transfer.
- Avoid horrible language such as *To the fullest extent allowed by law and contractor's insurance policies, contractor shall defend…..*
- The above language sometimes provides zero risk transfer due to the wording in the endorsements in contractor's policies.
- Negotiate terms from strength not after the bid is awarded.
- Then there is indemnification for Professional services especially architects.

Budget-Not for the budget office to determine

- Future estimates, stability and long-term objectives
- Risk costs don't track CPI
- Funding at expected losses equates to a budget adjustment four years out of ten.
- Most don't understand statistics.
- More concerning is that many public entities don't have the self-control not to raid loss reserves.

Actuarial Analysis and Program Design

- Data Rules
- Those who understand data rule
- What risks to retain
- What risks to transfer
- Retentions, limits and coverage
- This is how we have always done things isn't a response.
- Convincing Management to change….GOOD LUCK

Risk Consulting

- Risk and More
- When an “A” level Risk Manager has proven themselves, they tend to get asked to consult in other areas.
- Be the resource when the bid package is developed.
- Be on the negotiation team.
- Be part of the policy team at the Emergency Operations Center.
- Be included in Tabletop exercises and invite insurer to cyber exercise
- Floods, reimbursement expert, disaster claims

Claims

Liability and Property Claims

- Liability and property claims can be handled in-house or through a third-party administrator (TPA)
- Claims staffing can be a combination of the above. In-house staffing can be performed by loss control staff as an adjunct function. In-house personnel can provide a level of service to claimants whether they be students or residents that is challenging for TPA's to achieve.   In-house staffing can also be beneficial for consulting to operating departments.

Workers' Compensation

- Most workers' compensation programs are handled by a third-party administrator (TPA). There are large entities that handle claims in-house or have dedicated units at a TPA. The volume of claims required to maintain quality staffing makes this a challenge for all but the largest entities. Some entities disbanded self-administered units due to the challenge of maintaining trained staff through normal turnover and vacation and leaves of staff. It is beneficial for a dedicated staff person to monitor the TPA and serve as a resource to the injured worker.

Liability Claims

- TPA or In-House
- Price vs. Value
- In-house you have boots on the ground personal involvement.
- In-house can be a hybrid claims/safety person
- In-house can build the bench
- Vacancies however can ruin a program.

Workers' Compensation Claims

- TPA for all but largest entities
- Above a certain claim count an in-house liaison is required.
- Keep closure rates up
- Manage return to work program
- Manage the TPA and ancillary services
- Evaluate program
- Many entities have this position and think that it is a Risk Manager

Industrial Safety

- This function ideally should be staffed by a Certified Safety Professional
  - Field and Office work including drafting new programs, data analysis, and facilitating training classes
  - This position would manage an Executive Safety Committee to ensure that a safe workplace is promoted and maintained with support of upper management.

Industrial Safety/Loss Control

- This includes industrial, property, and liability
- Don’t follow cookie cutter approach
- Follow mandated training and loss reduction specific training
- Tailor programs, training, and inspections based on your needs
- Add value to the organization

We can only support one management person for the Risk Function, What do we do?

- Hire a strong generalist skilled in the following areas
  - Insurance policy language
  - Claims handling both workers' compensation and liability
  - Safety or engineering knowledge
  - Accounting and analytics
- Develop bench
  - Fill in for questions during vacation periods or turnover
  - Allows for spreading knowledge throughout organization
  - Ideally placed in Finance or Administration of a high visible operations area
- Avoid allowing position to be vacant for any length of time as continuity of programs is key for long-term stability

Broad Knowledge Saves Money

- What is wrong with Road Design?
- Is this City or Cal-Trans?
- Death Claim
- Adjacent to Large Venue
- Find other coverage
- Good testimony
- Social Media hurts plaintiff

- Santa Ana River was biggest flood risk west of Mississippi
- Corps of Engineers expanded riverbed and replaced bridges in 1980’s
- Area dedicated to Flood Control during project but never taken back
- City boundary in riverbed but county bike park under bridge
- Note two bridges and protected bike lane on “sidewalk”
- City owned venue with insurance for venue
- Plaintiff decedent jumps bridge opening falls on County bike path
- Risk transferred by insurance
- Defense Verdict

Broad Knowledge Saves Money

- What is wrong with the Road Design
- Horrific Injuries
- How was area built
- Find other coverage
- What about at fault driver?

- Westbound Katella between Convention Center and California Adventure
- 17-year-old driver claiming sun in eyes ran through five red signal heads. passed other stopped vehicles
- Family walking south from viewers right to left.
- Deceased child and other critical injuries
- No charges filed against driver
- Street improvements as part of Resort and Convention Center improvements less than five years prior to incident.
- Good Road Design?
- Motion for Summary Adjudication denied
- Why?
- The line of palm trees back of sidewalk were not in original approved street design.
- Coverage? Thanks to an Owner Controlled Insurance Program there was coverage available through Completed Operations coverage on the CGL.

Management and Evaluation of Programs

- Without measurement how can evaluations be made
  - Includes programs and vendors
  - Retentions, limits, insurers
- Data rules
  - Claims data
  - Trend Analysis
  - Evaluations
  - Reviews
  - Audits

SIR Evaluation Excess Workers' Compensation
Move from a $1M SIR
Total Incurred exceeding $500K 2007-2017
Trended 4% medical inflation *simplistic conservative if fully reserved on DOL

		Incurred		Trend 2017	$1.5M SIR	$2M SIR	
1	2009	$800,000		$1,075,000	$75,000	$75,000	
2	2011	$600,000		$760,000			
3	2011	$550,000		$700,000			
4	2009	$575,000		$800,000			
5	2015	$800,000		$850,000			
6	2010	$1,750,000		$2,300,000	$500,000	$1,000,000	
7	2010	$550,000		$735,000			
8	2009	$500,000		$700,000			
					$575,000	$1,075,000	
SIR	Premium	Savings	Save 10 Year	Cost 10 Year	Net Saving		
$1,000,000	$600,000						
$1,500,000	$440,000	$160,000	$1,600,000	$575,000	**$1,025,000**		
$2,000,000	$350,000	$250,000	$2,500,000	$1,075,000	**$1,425,000**		

- The prior slide is a simple analysis to determine level of SIR for a workers’ compensation program.
- Quote SIR at $1M, $1.5M, and $2M
- Trend all losses above $500K prior ten years as if total incurred was reserved in year of loss
- This is a conservative approach and does not reduce for present value nor long payout pattern.
- The savings do not consider long payout pattern and cash flow considerations.
- The twenty-year analysis was also conducted, and it yielded better results, by the way I kept the twenty year analysis in my back pocket in the event someone questioned my sample size
- Lesson: When selling a program be conservative with assumptions.

Quarterly Safety Statistical Report

Work Unit-All				**Report Period**		
Current Quarter			Prior Yr Qtr	Year to Date		Prior YTD
Employees		Hours Worked		Total Hours Worked	3,806,839	3,702,347
Full Time	1,871	997,908	995,465	Total Recordable Injuries	203	167
Part Time	1,273	308,775	282,936	Total Ergonomic Injuries	10	15
Totals	3,144	1,306663	1,278,401	Total Other Recordable	193	152
				Total Disabling Injuries	30	26
Total Recordable Injuries		67	52	Total Days Away From Work	6,990	4,480
Total Ergonomic Injuries		3	5	Total First Aid Injuries	21	30
Total Other Recordable Injuries		64	47			
Total Disabling Injuries		10	4	**Incident Rates per 100 ee**		
Total Days Away From Work		1,404	1,658	Total Recordable Injuries	10.67	9.02
				Total Ergonomic Injuries	0.53	0.81
				Total Other Reportable	10.14	8.21
				Total Disabling Injuries	1.58	1.4

Quarterly Safety Statistical Report

- This report is done for each operating department and entity wide.
- The information is helpful for department and Executive Safety Committee to understand the level of injuries occurring in order to make improvements as necessary.
- Similar reports are created annually benchmarking against departments in similar entities.
- This data is reviewed at the Executive level quarterly and is effective is promoting safe work practices across the enterprise.

Workers' Comp Claims

Period	I/A Leave	LIGHT DUTY	PERM MOD	W COMP	EXCESS	New Indem	Total Incurred		
July									
August									
September									
October									
November									
December									
January									
February									
March									
April									
May									
June									
Total									
YTD Budget									

Liability Claims

Period	Payments	Prior Year	New Claims	Prior Year	Litigated	Prior Year	Reserves	Prior Year
July								
August								
September								
October								
November								
December								
January								
February								
March								
April								
May								
June								
Total								
YTD Budget								

Monthly Claims Statistics

- What is measured and reviewed gets attention
- Tracking the components of workers’ compensation and liability claims on a monthly basis compared to the prior year figures and the year to date budget allows for trends to appear early.
- The ability to identify and react to trends early assist in claims handling, loss control opportunities along with budget and fund management.
- Monthly meetings with claims and loss control personnel to share knowledge pays dividends.

Benchmark Claims Work Comp Claims Data
Dept of Industrial Relations Annual Reports
Example 9 Cities with Police and Fire

City	Open Claims	Total Liability	Total Employee	Total Wages	Cases/EE Five Yr Avg	Liability/EE Five Yr Avg
A	437	$17,843,769	3,106	$251,752,974	13.98	$6,782
B	284	$17,641,791	2,635	$196,322,152	10.83	$7,356
C	1,938	$67,838,837	5,708	$474,036,762	30.13	$12,455
D	711	$25,787,086	2,386	$191,737,510	30.32	$11,309
E	174	$5,984,662	889	$68,811,471	18.49	$7,104
F	445	$21,790,093	1,421	$140,683,654	35.7	$17,325
G	314	$15,433,929	1,696	$114,172,085	18.21	$8,215
H	680	$37,309,724	1,431	116,292,937	39.41	$21,022
I	656	$39,104,937	1,888	138,508,555	36.4	$18,336

Benchmark Claims Work Comp Claims Data

Dept of Industrial Relations Annual Reports
Example 4 School Districts and 2 School JPA's

School	Open Claims	Total Liability	Total Employees	Total Wages	Cases/EE Five Yr Avg	Liability/EE Five Yr Avg
A	628	$16,502,565	8,957	$442,312,567	7.18	$1,439
B	292	$21,677,478	2,455	$120,881,926	12.46	$6,726
C	104	$4,082,798	5,374	$306,949,561	2.2	$727
D	207	$4,529,599	4,728	$216,496,178	4.61	$1,110
JPA	1034	$53,947,912	22,715	$1,119,417,070	5.11	$2,518
JPA	266	$7,372,976	10,942	$567,804,415	2.98	$822

Benchmark Claims Data

- The Self-Insurer Annual Reports you complete are compiled by the Department of Industrial Relations in an Annual Report.
- This is a valuable resource to use to benchmark against similar sized entities.
- The two tables provided include (1) cities with police and fire operations and (2) school districts and school JPA’s.
- The data provided is very instructive with considerable variability between entities.
- The Annual Report includes who administers the claims.
- What isn’t included but is easy to add is the PAR score of the Claims Administrator.

Reviews and Evaluations Nothing Should Be a Surprise

- Vendor management and Evaluation is critical
  - Maintain drop file of notes or email which were or not followed up on
  - Utilize on annual review Reviews are both positive and negative
  - Inform your vendor on categories you value and will score them on
- Items to score
  - PAR Score
  - Claim Audit score
  - Timeliness of quotes, certificates and renewals
  - Advise on coverage gaps and uninsured exposures
  - Innovation of deductible or SIR level modification
- Annual Review Scoresheet
  - I found a nice weighted scoresheet on the RIMS bulletin board a number of years ago which I tailored for my needs.
  - The first time I utilized it my broker liked the score of 89 but when we drilled into the numbers that score was due to overweighting on areas that they excelled but some areas that were also important did not score as well. There is almost always room for improvement.
  - I have known TPA's that struggle to meet a client's claim audit score and then are surprised when an RFP is circulated.
  - Utilize this system to review your own operational results.
  - Remember what I said earlier about data! Data Rules and He Who Knows Data Rules

Category	Expected Points	Weight	Weighted Points	Scored Points	Comments
Back Office Support					
Accuracy	90	1	90		Correct certs and policies
Communication	85	1	85		Policies uploaded timely
Qualitative	90	1	90		Billing and policies withing X days
Delivery					
Coverage analysis	90	1	90		Identify gaps and uninsured exp
Communication	85	1	85		Respond within X days of inquiry
Claims Mngt	85	0.5	42.5		Little need but some need
Innovative Solutions	90	1	90		What alternatives to fund exp
Renewal					
Market Analysis	90	1.5	135		Estimates at 10/1, 1/1 and 3/15
Timely strategy	85	1.2	102		Market plan delivered by 11/15
Negotiation	90	1.5	135		Comparison est by 1/15
Post Renewal	90	1.2	108		Thorns and roses discussion 9/15
Total	970		1,052.5		

How you can become the Risk Manager in Demand or get elevated in your Organization

- Education not just training
  - Why training at PARMA, COSIPA, and Pool In-Service meetings are no enough
- MBA not MPA
  - Statistics are not just for enrolled actuary to know.
- ARM and CPCU bring proof of your dedication to the profession
- Manage up, don’t be managed.
- Learn the phrase *I’m planning to* rather than *What do you think?*
- Practice RMBWA, thanks to Peters and Waterman <u>In Search of Excellence</u>
  - Risk
  - Management
  - By
  - Wandering
  - Around

Additional Resources

- Read daily: The Wall Street Journal, Your local mainstream newspaper
- Read weekly: your local community news, alternative weekly, Business Insurance, Pleasure Books
- Listen to podcasts: Rimscast, Geeks, Geezers Googlization, National Brokers, Revisionist History, Against the Rules. Any other interesting listens to make your commute productive. Stretch your mind

<u>Questions</u>

Do you know if FEMA reimburses claims to the entity if all members of the EOC have not been trained?

Answer: *I don't know. I know that my agency made a huge effort to train all EOC members. Almost by definition given turnover there might be members without full certification but likely if the agency has made a good faith effort and most EOC members are trained then they won't require 100% compliance.*

Questions

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