



# **BIENNIAL REPORT**

**to the 81st Texas Legislature**

*December 31, 2008*

STATE OFFICE *of* RISK MANAGEMENT





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81st Texas Legislature  
December 31, 2008**



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The Board of Directors and Executive Director of the State Office of Risk Management (Office) respectfully submit this Biennial Report to the 81<sup>st</sup> Legislature. This report is submitted pursuant to the requirements of Texas Labor Code Sections 412.032 and 412.042 and Executive Order GWB 95-8.

The Office appreciates the opportunity to serve state employees and Texas state agencies, and we look forward to working with the members of the 81<sup>st</sup> Legislature during the legislative session. Please feel free to contact me at (512) 936-1502, or Paul Harris, the Office's government relations liaison, at (512) 936-1452, if you have any questions or require any additional information. We are available at your convenience to discuss any of the issues contained in the report and to provide necessary assistance.

Respectfully,

Jonathan D. Bow, J.D.  
Executive Director



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## **1. Methods to reduce the exposure of state agencies to the risks of property and liability losses, including workers' compensation losses**

Texas state agencies are exposed to a vast array of risks. To help agencies address those risks, the State Office of Risk Management (Office) utilizes multiple approaches, including, but not limited to: published guidelines; oversight in developing and maintaining effective risk management programs; specialized assistance and training; and comprehensive data collection, monitoring, and analysis.

### **Guidelines**

The Office publishes comprehensive program elements and methods in its Risk Management for Texas State Agencies (RMTSA) guidelines. The RMTSA guidelines are freely available to state agencies, and the public, on the Office's website at [www.sorm.state.tx.us](http://www.sorm.state.tx.us). The four-volume set of guidelines lays out the form, direction, and basis for developing and implementing a comprehensive risk management program to reduce property, liability, and workers' compensation losses in state agencies covered by Texas Labor Code, Chapter 501. The guidelines are designed to be supplemented with detailed programs, policies, and procedures that address each agency's unique mission and risks. While each agency must develop and maintain appropriate risk management programs, adoption of the guidelines as written is not mandatory. Agencies are encouraged to add and delete chapters as appropriate to optimize the programs for their businesses.

### **Oversight and Development**

The Office's risk management specialists provide direct on-site assistance and oversight to client agencies. On-site visits include periodic comprehensive reviews of each agency's risk management program and ad hoc on-site consultations that may be conducted upon request of an agency or whenever a specific health or safety issue has been identified. During the past biennium, the Office's risk management specialists conducted 574 on-site visits with client agencies around the state.

### **Assistance and Training**

Specialized assistance and training is available for a multitude of issues, including safety and health programs, claims management, claims analysis, indoor air quality, business continuity management, noise and lighting analysis, driving safety, fraud management, and many other exposures in the various classes of risk. The Office responds to requests for specialized needs through direct development or coordination through third parties.

### **Data Collection and Monitoring**

The Office analyzes risk management expenditures and loss data submitted by client agencies and performs baseline trend analysis to monitor emerging exposures and losses. The Office's web-based, interactive Risk Evaluation and Planning System (REPS) leads client agencies through the identification, analysis, and mitigation of identified risks. The

Office also conducts regular meetings with client agency risk management staff as well as specialized risk-related seminars to educate client agencies on emerging trends and to provide more in-depth education in risk management.

### **Other Methods**

The Office seeks to be responsive to the risks and needs of client agencies as they are identified and cooperates with other oversight agencies in implementing viable health and safety programs for state employees. Recent developments include joining a memorandum of understanding between the State Fire Marshal's Office and the Texas Facilities Commission, creating a cooperative framework for the agencies to communicate and work together to address risks from identified fire hazards or losses and to report any actions taken to mitigate the risks related to state property.

## 2. Operation, financing, and management of risks

Risk exists in every facet of state operations, exposing government to monetary, efficiency, resource, and public confidence losses. Risk managers are concerned with reducing the frequency and severity of losses to individual state agencies and, by extension, to the state government as a whole. In the course of its normal business operations the state is exposed to numerous potential losses, including, but not limited to: workers' compensation costs; fire damage; automobile accidents; lawsuits; and hurricanes.

Responsibility for the operation, financing, and management of risks shown below are shared between the Office and its client agencies and varies by risk. The Office's risk management program is concerned with all categories of risk and provides services to covered agencies and to other entities identified by statute, such as the Community Supervision and Corrections Departments, that are included in the state's self-insured workers' compensation program. In addition, covered agencies are required to have a designated risk management contact and claims coordinator(s) who have responsibility for oversight and reporting on agency risk management efforts, injuries, and losses at each agency.

**CHART A**  
**Statewide Risk Management Costs for FY '06 & FY '07**

	<i>FY '06</i>	<i>FY '07</i>	<i>Incr/(Decr)</i>	<i>% Incr/Decr</i>
State Agency Risk Management Programs	\$30,762,585	\$36,651,192	\$5,888,607	19.14%
Cost Containment	\$1,921,356	\$1,737,865	(\$183,491)	-9.55%
Settlements and Judgments	\$4,421,610	\$3,411,737	(\$1,009,873)	-22.84%
Bonds, Insurance, & Deductibles	\$17,991,551	\$20,939,981	\$2,948,430	16.39%
Actuarial Services	\$17,000	\$8,500	(\$8,500)	-50.00%
Court Costs & Attorney Fees	\$1,794,646	\$811,629	(\$983,017)	-54.77%
Statewide Risk Management & Claims Administration (AY)	\$6,816,913	\$7,607,580	\$790,667	11.60%
<b>Total Cost of Risk Management</b>	<b>\$63,725,661</b>	<b>\$71,168,484</b>	<b>\$7,442,823</b>	<b>11.68%</b>

*\* FY '08 data not fully reported for inclusion*

State agency program costs consist of risk management departmental salaries and benefits, staff training, supplies and equipment purchases, and other risk management-related client agency expenditures. Agencies have improved their focus on risk management programs by increasing funding for necessary staffing and safety equipment. There has also been increased participation in the state property insurance program. These increases in client agency risk management programs and increased use of insurance for loss indemnification are indicators of risk management mitigating and financing strategies that are anticipated to provide net reductions in costs of loss by reducing the ultimate frequency and/or severity of losses from operations.

Cash payouts for workers' compensation claims payments are shown in Chart B.

**CHART B**  
**Statewide Workers' Compensation Expenses Paid out for FY '06 & FY '07**

	<i>FY '06</i>	<i>FY '07</i>	<i>Incr/(Decr)</i>	<i>%</i> <i>Incr/Decr</i>
Workers' Compensation Claims Paid (Net of Subrogation)	\$43,755,813	\$41,066,302	(\$2,689,511)	-6.15%

As shown above, in FY '07, the state paid \$41,066,302 for workers' compensation claims. This figure is the sum of all workers' compensation payments made on behalf of claimants in FY '07, including those injured in preceding fiscal years. The reduction in workers' compensation claims payments in FY '07 continued a downward trend in costs arising from injuries to state agency employees. When analyzing workers' compensation costs, it is important to note that the numbers reported represent a snapshot in time. Further, workers' compensation payments are typically paid out over several years. Therefore, changes made to a risk management program or to claims administration in a given fiscal year may take several years to realize any financial consequence.

### **Risk Management**

Knowledge is key to empowering state agencies to manage their risks and losses. During FY '08, the Office continued to improve the accessibility of training to all state employees. By partnering with higher education client agencies, trainers were able to secure training facilities at participating universities at no cost. Because this training is delivered locally, participation by staff in remote locations is increased at little or no cost to those offices. Prior to these regional training seminars, travel costs and loss of productivity were significant barriers to client agencies' ability to train significant numbers of staff.

During FY '08, more than 5,815 students from 218 different state agencies attended 311 seminars offered in 37 Texas cities. As a result of implementing these seminars where the state employees are located, the number of state employees trained was increased by 13 percent over the last fiscal year, resulting in a reduction in travel costs for client agencies that no longer have to expend travel monies to send employees to Austin for training.

### **Workers' Compensation**

New injuries to state employees have been significantly reduced. While the state has seen small increases in injuries over the past two years on average, there are still 1,300 fewer injuries per year than occurred seven years ago (see "Accepted Claims" graph on pg. 11). Significantly improved risk management and claims coordination efforts by covered agencies and improved processes implemented by the Office have shared in improving this loss experience. Changes in the funding structure for workers' compensation have been key in emphasizing the value of effective risk management.

## Financing

For workers' compensation operations the Office is funded with a combination of General Revenue and Interagency Contracts (IAC). The Risk Management program, which includes health and safety issues as well as general risk management, and the Workers' Compensation Claim Payments are funded by IAC through annual assessments to state agencies pursuant to Chapter 412, Texas Labor Code. The assessments, similar to annual premiums, are determined by a formula based on historic full-time equivalent (FTE), payroll, claims, and claims cost data. A portion of the Pay Workers' Compensation strategy is also funded by IAC through the assessments. This funding is primarily used for medical cost containment services and other costs directly related to reducing claim payments.

The remaining administrative expenditures for the Pay Workers' Compensation strategy, other than the IAC funding, are funded by a direct General Revenue appropriation.

**State Office of Risk Management  
FY '08 Expenditures By Strategy  
and Method of Finance**

<i>Goal/Strategy</i>	<i>GR</i>	<i>IAC</i>	<i>Total</i>
Goal 1.1/Risk Management Program		\$2,039,973	\$2,039,973
Goal 2.1/Pay Workers' Compensation	\$3,580,198	\$2,167,926	\$5,748,124
<b>SUBTOTAL:</b>	<b>\$3,580,198</b>	<b>\$4,207,899</b>	<b>\$7,788,097</b>
Goal 1.1/Workers' Compensation Payments (separate appropriation)		\$44,063,138	\$44,063,138
<b>GRAND TOTAL:</b>	<b>\$3,580,198</b>	<b>\$48,271,037</b>	<b>\$51,851,235</b>

### **3. Handling of claims brought against the state**

Tort-related claims against the state are administered by the Office of the Attorney General. Other non-workers' compensation claims are the primary responsibility of each individual state agency. The Office gathers data on these claims from the agencies for reporting purposes but does not participate in the handling of those claims. The Office offers a statewide insurance program for general liability, employment practices, professional liability, and other non-tort related exposures.

The Office processes workers' compensation claims for all state agencies except three statutorily exempt agencies (Texas Department of Transportation, University of Texas System, and Texas A&M University System). State law provides that employees injured in the course and scope of their employment are entitled to receive benefits for reasonable and necessary medical care and indemnification of lost wages for lost time from work due to the effects of their compensable injuries. In most cases, injured workers are entitled to receive medical benefits to treat the effects of their work-related injuries or illnesses, without any specific time or cost limits.

Each state agency designates at least one claims coordinator who provides information about workers' compensation to injured employees and reports workers' compensation claims to the Office. The Office provides agency claims coordinators with training on handling claims and provides access to the Office's Claims Management System (CMS). The Office's automated CMS system automatically creates a claim when information is reported electronically to the Office by the agencies, or the information may be entered manually by Office staff. The CMS is the Office's central claims application, enabling assignment of claims, maintenance of records, monitoring of deadlines, and benefits payments. The CMS also interfaces with the Office's medical cost containment vendors, the Texas Department of Insurance (TDI)/Division of Workers' Compensation (DWC), the Office of the Attorney General, and the State Comptroller for the processing of state warrants. The Office utilizes a digital imaging system for receipt and record keeping of claim documents, including medical billing and submitted forms promulgated by TDI and DWC.

The Office devotes a staff of 40 adjusters located in Austin, of which 27 are assigned to manage all workers' compensation claims, assess compensability, and authorize payment of wage replacement (indemnity) and medical benefits. The Office processes approximately 700 indemnity payments each week, including direct claimant benefits, attorney's fees, and related payments required by law. Adjusters calculate the amount of indemnity payments based on each injured worker's average weekly wage, based on salary information provided by the employing agency. In FY '08, the Office processed approximately 36,800 indemnity payments, representing a continuing decrease in the number of active open claims administered from the previous year.

<b><i>Benefit</i></b>	<b><i>Description</i></b>	<b><i>SORM's Average Total Caseload</i></b>
Temporary Income Benefits (TIBs)	Injured employees unable to work are eligible to receive TIBs after the seventh day of lost time for a maximum of 104 weeks.	404
Impairment Income Benefits (IIBs)	Workers become eligible for IIBs 104 weeks after the injury, or when the worker has a permanent injury and reaches maximum medical improvement. IIBs are paid based on a rating of the employee's disability in proportion to the entire body as assigned by a physician. For each percent of impairment, the employee receives three weeks of IIBs. For example, employees with an impairment rating of 5 percent receive 15 weeks of IIBs.	218
Supplemental Income Benefits (SIBs)	Injured workers unable to work, actively seeking re-employment, or participating in a vocational rehabilitation program may receive SIBs on a monthly basis if they have an impairment rating greater than 15 percent and are not earning at least 80 percent of pre-injury wages because of the injury.	47
Lifetime Income Benefits (LIBs)	Injured workers meeting specific statutory requirements may receive LIBs.	10
Death Income Benefits (DIBs)	While not an income benefit, beneficiaries of workers who succumb to fatal injuries may receive DIBs.	55

The Office has developed claims units dedicated to particular functions. Three units are assigned to handle claims on a submitting-agency basis. A fourth unit, the Medical Only/Customer Service unit, develops new adjusters and provides customer service, administrative support, and benefit administration for No Lost Time/Medical Only claims. The Office utilizes additional multiple methods for claims management, including, but not limited to, cost containment, case management, external medical reviews, and investigations.

In FY '08, the Office processed approximately 119,000 medical bills. The Office contracts with two cost-containment vendors that conduct comprehensive audits of submitted medical bills and provide other services. Currently, CorVel Corp. is assigned responsibility for auditing physician and hospital bills, and Forté, Inc., audits pharmacy bills. Forté also has responsibility for processing requests for preauthorization.

The vendors review bills to ensure that treatment is reasonable, necessary, and related to the compensable injury; identify duplicate bills and billing errors; and adjust bills for payment in accordance with the DWC fee schedules. Payment recommendations are submitted to the Office for review and verification and may be resubmitted to the vendors for correction. In FY '08, the Office was billed \$94.3 million for medical services. The cost containment functions provided by the vendors reduced these costs by \$66.2 million.

Additional savings were realized through the use of a preferred provider organization (PPO) operated by CorVel and through Forté's contract with ScripNet, a pharmacy benefit manager (PBM). The current PPO is different than the networks authorized by the Legislature in 2005 in House Bill 7, and is not mandatory. Similarly, the PBM provides discounts from participating pharmacies, but also is not mandatory. In FY '08, the PPO generated \$647,226 in savings, and the PBM generated \$421,320 in savings.

**Summary of Cost Containment Savings**

<i>Strategy</i>	<i>FY '06</i>	<i>FY '07</i>	<i>FY '08</i>
Total Medical Bill Audit Savings	\$84,011,427	\$74,499,274	\$64,899,875
Medical Bill Audit Savings Due to Duplicate Bill Savings	(\$12,594,152)	(\$10,622,218)	(\$5,448,966)
Net Medical Bill Audit Savings	\$71,417,275	\$63,877,055	\$59,450,909
PPO Savings	\$1,024,273	\$954,269	\$1,068,546
Preauthorization of Medical Services*	\$6,480,936	\$7,056,576	\$5,663,830
<b>Total Cost Containment Savings</b>	<b>\$78,922,484</b>	<b>\$71,887,900</b>	<b>\$66,183,285</b>

*\* Cost of procedures not performed at time of request, as estimated by the cost containment vendor. The Texas Workers' Compensation Act and DWC-adopted rules provide that health care providers are required to obtain preauthorization of certain medical procedures (e.g., psychiatric care and non-emergency hospitalizations) from workers' compensation insurance carriers prior to such procedures being performed. Preauthorization savings represent the avoidance of expenses related to unreasonable or unnecessary procedures prior to a treatment or service being provided and billed. Since a treatment or service was not authorized and no billing was received, the savings reported are cost-avoidance estimates provided by the Office's cost containment vendor.*

The Office utilizes case management to assist injured workers in accessing quality health care in a cost-effective manner to enhance their ability to return to work sooner. The Office employs one internal nurse case manager who contacts the injured worker, treating doctor, and employer and provides expertise to the adjuster in developing an appropriate claims handling strategy from a medical perspective. The case manager also assists in making determinations as to whether further telephonic or field case management is needed. In appropriate cases, the Office utilizes private vendors for field case management services performed by certified case managers, registered nurses, or licensed vocational nurses. Case managers meet with injured workers, consult with doctors about treatment plans, and may visit employers to assess the physical challenges that work may present to the injured worker.

State law and DWC rules require preauthorization and concurrent review by workers' compensation carriers for specific treatments. The Office may not pay the cost of these medical services unless preauthorization was requested and granted. The Office contracts with Forté to determine the medical necessity of services requiring preauthorization. In FY '08, Forté processed 6,707 preauthorization requests. Forté also processes concurrent reviews to determine the medical necessity of extending ongoing treatments that were previously preauthorized.

The Texas Workers' Compensation Act grants parties the ability to use medical examinations of the injured worker by an independent physician to resolve questions about the appropriateness of treatments. These required medical exams (RMEs) verify that ongoing and proposed care is reasonable, necessary, and related to the compensable injury. Peer reviews may also be used to verify whether medical services or prescription drugs are an appropriate course of treatment given an injured worker's diagnoses. These peer reviews involve a medical professional conducting a paper review of medical files. Both RMEs and peer reviews may identify a need for changes in treatment and may be relevant in the event of a dispute regarding entitlement to certain benefits.

The Office reviews impairment ratings received by injured workers and may, in appropriate circumstances, request an independent doctor review an impairment rating. Reviewing ratings helps to ensure the accuracy of impairment ratings and determine the appropriate benefits to authorize for injured workers.

The Office employs two staff members to investigate claims, including allegations of fraud. The investigators interview involved parties, conduct surveillance, review wage records with the Texas Workforce Commission, and check for previous personal injury claims. If investigators find evidence that a claimant knowingly and intentionally lied to receive benefits, they refer the case to TDI's insurance fraud unit. The insurance fraud unit reviews the case to determine if it should be referred to a district attorney for prosecution, pursued as an administrative violation, or dropped.

Because cases of provider fraud are more difficult and time-consuming than claimant fraud, the Office's investigators may coordinate with or provide assistance to investigators from other entities. During the biennium, the Office opened approximately 111 fraud cases. After investigation the Office referred 19 injured worker and four provider fraud cases to TDI's insurance fraud unit. The alleged fraud amount totaled \$100,662.87. Of the resolved cases, one claimant received deferred adjudication and was ordered to pay \$7,742.47 in restitution; another received deferred probation and was ordered to pay \$6,560.22 in restitution. Three indictments were issued for three separate matters involving benefit fraud. One third party pleaded guilty to perjury in relation to a pending provider fraud case, received deferred adjudication, and was ordered to pay \$2,000 in restitution and perform 100 hours of community service.

Although avoided costs cannot be precisely calculated, the Office estimates costs avoided when ongoing fraudulent activities are detected and stopped are approximately \$120,000 for the biennium. The avoided cost estimate does not include the deterrence value of fraud investigations activity.

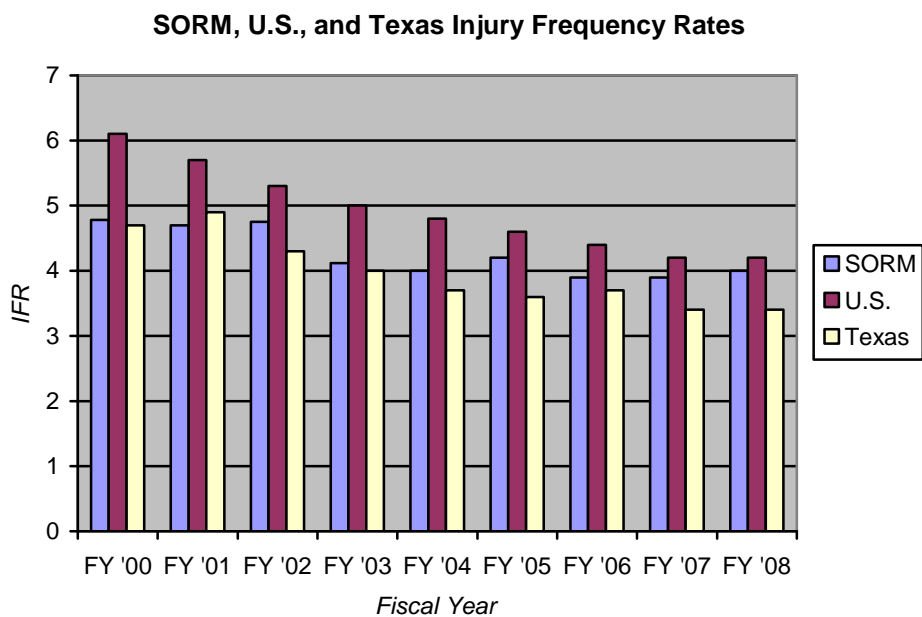
In claims where a state employee's injury is caused by a third party, the Office may be entitled to recover payments made for medical and indemnity benefits through subrogation. When processing claims, adjusters question injured workers and claims coordinators to determine whether any third party is involved. The Office employs a subrogation specialist who evaluates potential third-party liability and pursues cases both directly and through referral to the Office of the Attorney General when litigation is

necessary. The Office has recovered more than \$1.5 million through subrogation during the biennium.

Although the majority of workers' compensation benefits are paid without problems, disputes do occur regarding indemnity and medical benefits. When issues arise in a claim, injured workers, providers, and the Office follow the dispute resolution process in workers' compensation law, which provides separate processes for indemnity benefits, medical fees, and medical necessity disputes. The Office complies with decisions and orders issued by the DWC and reviews all matters for further litigation on a case-by-case basis.

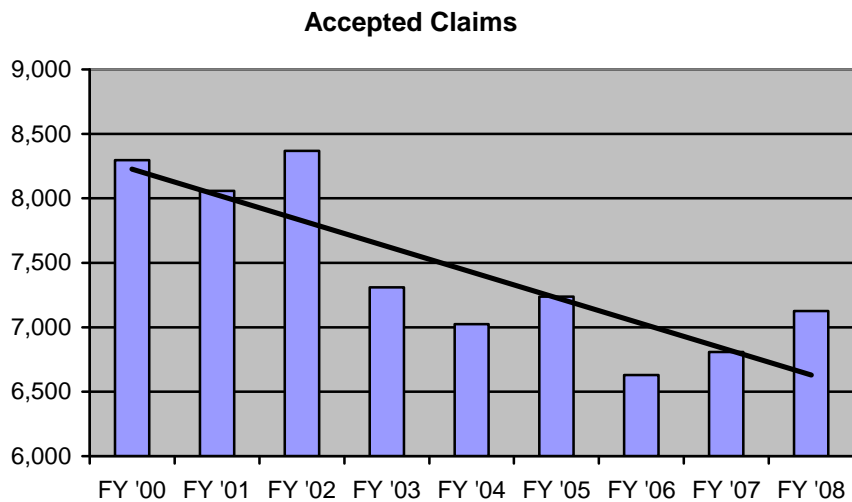
**4. Frequency, severity, and aggregate amount of open and closed claims in the preceding biennium by category of risk, including final judgments**

The total number of injuries per 100 FTEs has experienced a steady decline over the past decade. The Office has generally paralleled the injury rate of Texas private industry.



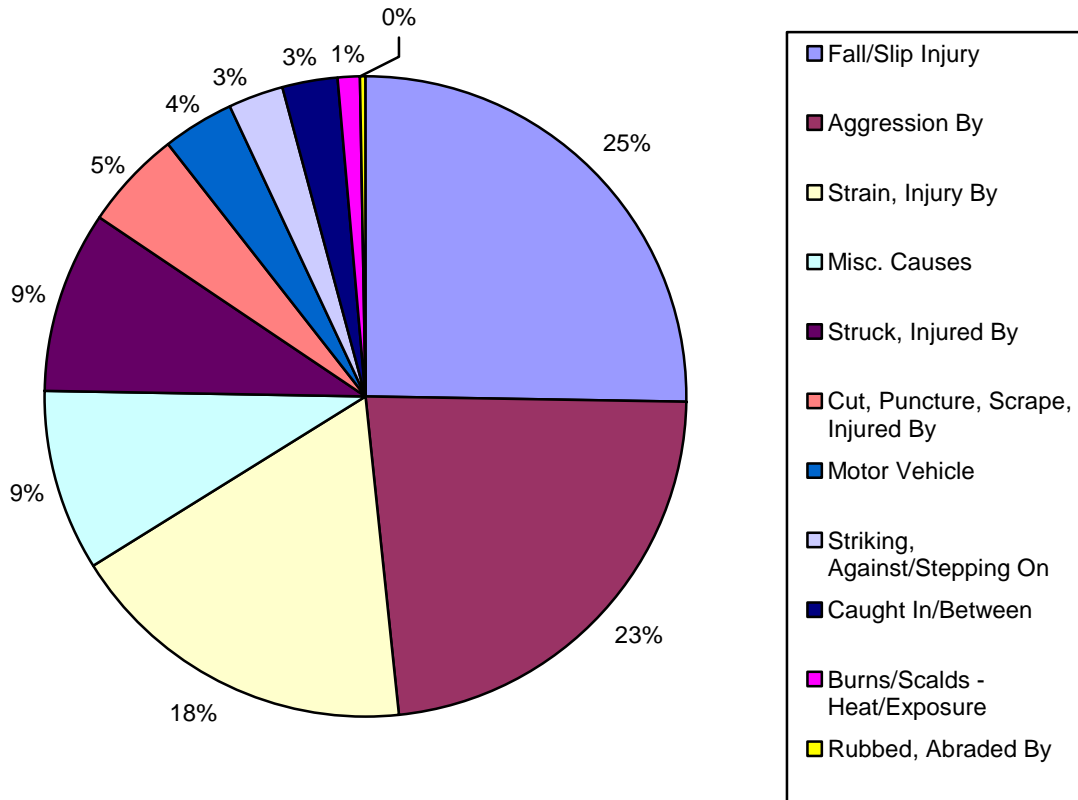
*\* FY '08 IFR for SORM is actual and estimated for Texas and U.S. based on FY '07 data*

Workers' compensation claims numbers vary year to year. Although the Office has seen recent upward trending, there has been a general downward trend in the total number of accepted workers' compensation claims for Texas state employees over the past decade.



During the past biennium seven covered employees died in work related accidents or incidents: one training accident; one aggression injury; one slip and fall; and four automobile-related deaths. Causes of injury for the preceding biennium are presented below.

### FY '08 Major Causes of Injury



The leading causes of injury during the biennium remained relatively stable, except for aggression injuries, which went down by 3 percent. As would be expected, the criminal justice, juvenile offenders, law enforcement, and mental health agencies account for the vast majority of aggression injuries within the state. It should also be noted that while motor vehicle accidents account for only 4 percent of all claims, they are the leading cause of work-related deaths.

Other losses incurred during the biennium include property and casualty claims, as reported to the Office. Most claims made during the biennium remain open and are uninsured. Claims listed may include claims where the state has immunity or has statutory liability caps in place to limit or prevent expenditure of state funds.

**FY '07-'08 Client Agency Frequency and Claims Data**

<i>Category</i>	<i>Number of Claims</i>	<i>Demand Amount</i>	<i>Loss or Paid Amount</i>
Aircraft or Boat Damage	5	\$0	\$0
Automobile Physical Damage	1,237	\$0	\$1,462,339
Automobile Liability	269	\$165,319	\$435,657
Crime	15	\$0	\$292,611
Directors' & Officers'	20	\$188,349	\$34,211
Electronic Data	40	\$4,829	\$45,152
Employment Practices	181	\$9,200	\$94,700
Environmental	1	\$0	\$0
Excess Automobile	8	\$0	\$13,188
Flood	1	\$0	\$0
General Liability	535	\$495,770	\$129,723
Inland Marine	2	\$0	\$1,050
Professional	13	\$0	\$98,306
Property	267	\$12,412,068	\$2,728,535
<b>Totals:</b>	<b>2,594</b>	<b>\$13,275,535</b>	<b>\$5,335,472</b>

**5. Identification of each state agency that has not complied with the risk management guidelines and reporting requirements of Chapter 412**

Agency	Issue
Midwestern State University	(1) Failure to provide automobile data to obtain quote through statewide automobile program nor a request for waiver  (2) Purchase of unapproved automobile policy without requesting or obtaining a waiver
Texas Woman's University	(1) Failure to provide a completed Directors' & Officers' application to obtain quote through statewide D&O program
Texas Southern University	(1) Failure to seek a waiver to purchase coverage prior to binding coverage outside of the statewide property program
Health and Human Services	(1) Failure to complete required Risk Evaluation and Planning System information
Texas Racing Commission	(1) Failure to meet statutory deadline for reporting risk management information (SORM 200)
Fire Fighters Pension Commission	(1) Failure to meet statutory deadline for reporting risk management information (SORM 200)
Board of Chiropractic Examiners	(1) Failure to report statutory risk management information (SORM 200)  (2) Failure to complete required Risk Evaluation and Planning System information
Commission on Jail Standards	(1) Failure to report statutory risk management information (SORM 200)
School for the Blind and Visually Impaired	(1) Failure to report statutory risk management information (SORM 200)
Texas Animal Health Commission	(1) Failure to complete required Risk Evaluation and Planning System information
Board of Medical Examiners	(1) Failure to complete required Risk Evaluation and Planning System information

## **6. Recommendations for the coordination and administration of a comprehensive risk management program to serve all state agencies, including recommendations for any necessary statutory change**

### **Statewide Self-Insurance for Property**

It is commonly assumed that the state self-insures its real and personal property. While it would be accurate to say that the state retains the risk of a loss, the absence of a specific insurance policy or funded and reserved program means that the State's real and personal property is in practice uninsured. The state has no funded reserves for losses to real or personal property and each agency makes an individual decision to either insure its property or retain any potential loss.

When uninsured losses occur, the agency must absorb those losses in current budgets or request additional appropriations. In the event of a declared disaster, reimbursement by the Federal Emergency Management Agency (FEMA) does not become an option until agencies purchase insurance on facilities that sustained damage.

The Office recommends consideration of a true self-insurance program for state real and personal property with funding for additional amounts to procure excess coverage above the reserve for state facilities. Since state facilities are located throughout the state, the spread of risk is favorable to establishing a self-insured property program. Establishment of a first tier reserve with the purchase of excess coverage could prove to be the most effective approach to funding state property losses. Significant amounts of state and local funds are already being expended for the purchase of property insurance. Establishment of a self-insured program for all state property could avoid those existing expenditures and provide coverage to all state facilities, whether currently insured or not. A self-insured program would meet FEMA requirements for receipt of federal funds in a declared disaster, help the Legislature in leveling budgets and expenditure patterns, and assure that all state facilities could be restored should damage occur.

### **Catastrophic Claims in Workers' Compensation**

Prior to the 80<sup>th</sup> Session of the Texas Legislature, the Sunset Advisory Commission undertook a review of the operations of the Office. Sunset reported that, although the Office's cash-basis funding method keeps current expenditures low, the Office may not be structured to adequately protect the state against catastrophic claims. Pursuant to Senate Bill 908, 80th R.S., as codified at Texas Labor Code §412.0129, the Office was directed to report the findings of a study of options to prepare state agencies for catastrophic claims. The Office did not receive the Sunset-recommended funding to contract with a third-party consultant to analyze predicted costs of potential disaster or estimate the appropriate size for a catastrophe fund or level of insurance. However, the Office, working in conjunction with the Texas Department of Insurance, Workers' Compensation Research and Evaluation Group, surveyed state and political subdivision workers' compensation programs in Texas and other states to determine: (1) how these programs are funded; (2) their relative size and risk exposure as compared to the Office's

current program; and (3) what strategy, if any, the programs employ for catastrophic claims.

This report was submitted to the Legislature in September 2008 concluding that the Sunset-identified concern was justified and that the state should take steps to establish funding mechanisms to cover potential catastrophic losses. The actual mechanism chosen for this purpose should be determined by the Legislature after considering the costs associated with retaining the risk versus transferring the risk through reinsurance and should provide clear procedures for identifying when and how funding will be made available in such emergencies. Further, the Office has identified an associated risk that a catastrophic event or events of significant magnitude would overwhelm the Office's administrative resources to receive, adjust and process the large number of claims produced. The state should anticipate that additional costs will be incurred to meet obligations under the Labor Code in the event of a catastrophe.

### **Workers' Compensation Health Care Networks**

House Bill 7, 79<sup>th</sup> R.S., authorized the establishment of Workers' Compensation Health Care Networks (WCHCNs) to provide necessary services to injured employees. The Legislative Budget Board's (LBB) fiscal note to HB7, 79<sup>th</sup> R.S., identified increased costs of \$500,000 in FY '06; \$1,328,511 in FY '07; \$3,188,427 in FY '08; \$3,985,534 in FY '09; and \$4,782,641 in FY '10. It was assumed SORM would require one Programmer VI position (\$50,952/year) to perform system modifications to accommodate changes in automated processes related to the transfer to a contract for network health care. The LBB further assumed the Office would require one additional Administrative Assistant II position (\$23,052/year) and increased operating costs of \$1,000 each year to accommodate network notification requirements and handle injured worker customer service concerns during the network transition.

No funds were appropriated to the Office to implement a WCHCN; however, the Office undertook efforts to implement networks within current funding. The Office designed a Request for Information (RFI) to collect necessary information to design its Request for Proposal (RFP), and during FY '08 the Office published an RFP based on information received during the RFI process. After review of the proposals, the Office's selection committee concurred in a decision, determining to decline to make an award and to suspend the RFP for WCHCN services. After extensive review, none of the proposals provided sufficient required information to determine that an award would be in the best interest of the state. This decision was not a finding that the state's self-insured workers' compensation program might not benefit from a properly constructed and well-managed WCHCN, but only that it was not possible to determine that such a network, as described in the proposals received, would be in the best interest of the state at that time.

Resources for implementation of the WCHCN initiative have been requested in the Office's Legislative Appropriations Request to the 81<sup>st</sup> Legislature in order to fully comply with requirements of Chapter 1305, Insurance Code and related provisions, but are substantially lower than the LBB-projected costs in the HB 7 fiscal note.

In the alternative, the Legislature may explore an approach to network service for the State similar to special provisions already in place for political subdivisions under Section 504.053, Texas Labor Code. Political subdivisions appear to have been successful in implementing networks under Section 504.053 that are significantly less cumbersome to create and implement for a governmental body, but specific statutory changes would be required to include these provisions in Chapters 412 and/or 501.

### **Risk Management Training and Certification**

Risk management expertise varies significantly from agency to agency. With ever-increasing demands on state agencies to identify and manage risk, many agencies are not familiar with principles of risk management. Lack of experience and training can result in a failure to identify and respond to risk, increased losses, and injuries to employees and the public. The Office recommends development of a certification program for state agency risk managers similar to the program establishing minimum certification for state purchasing professionals. Such a program can help ensure that state agency personnel receive training and have proven competency in identification, analysis, mitigation, financing, and administration of risk. The program would have the potential to generate a significant reduction in exposure to significant loss and assist agencies in managing losses should they occur. Requiring certification of risk managers for all agencies with significant risks or losses could benefit the agencies and the state.

### **Business Continuity and Management Planning**

FEMA maintains a list of major disasters declared in the 50 states, the District of Columbia, and nine U.S. territories. The State of Texas is at the top of this list, making it the most “disaster-prone” state, with 51 disasters formally declared between the years of 1976 and 2000. The next closest was California with 45. The events of Sept. 11 create further concerns regarding continuity of government functions in the event of terrorist attack and the unique risks associated with the approximately 57 state agencies located within the Capitol Complex.

Currently, the Office is tasked with assisting state agencies in developing business continuity plans; however, these plans generally address only the particular agency’s critical business processes, recovery time objectives, and dependence on other agencies or entities. Certain disasters or actions could result in multiple agencies simultaneously being unable to perform critical state functions. At this time, there is no formal prioritization for restoration of agencies or functions. While the Office emphasizes agency-level business continuity plans, the Office’s authority does not extend to mandating high-level government and interoperability issues. The Office recommends that the Legislature consider mandating a functionally based restoration priority plan to be developed and maintained by designated state leadership, with particular emphasis on restoration of critical statewide functions affecting core business processes and/or multiple agencies. In the event of a significant natural or man-made disaster affecting core government functions, the existence of such a plan would be absolutely necessary to ensure those functions were restored in the quickest and most-efficient manner possible. At a minimum, and ideally in conjunction with the statewide restoration priority plan, the

Office recommends that all state agencies be required to develop, maintain, and test a business continuity plan that meets minimum, pre-established standards.

The Office notes that business continuity plans, whether agency-based or general government-based, may contain sensitive information that could be used to purposefully disrupt continuity efforts in the event of terrorist action. It is further recommended that the Legislature consider limited protection of such information from disclosure pursuant to the Public Information Act.

### **Statutory Clarification**

Because the Office was created through the merger of two divisions, each split from two larger entities, the Office inherited provisions contained in two separate chapters of the Labor Code. The interaction between the two chapters is largely efficient, but some problems have been associated with operating a cohesive program given the retained language of the prior statutory chapters. For example, the definition of “state agency” differs between Chapter 412 and Chapter 501 -- Chapter 412 defines a state agency as “a board, commission, department, office, or other agency in the executive, judicial, or legislative branch of state government that has five or more employees, was created by the constitution or a statute of this state, and has authority not limited to a specific geographical portion of the state” and Chapter 501 defines a state agency as “a department, board, commission, or institution of this state.” This has led to questions regarding the access and responsibilities of certain entities covered under Chapter 501 with respect to Chapter 412 services. Since the Office’s responsibilities extend only to administering the programs and reporting noncompliance to the Legislature, clarification of the scope of Chapters 412 and 501 may be warranted to avoid future confusion, to specify access and responsibilities of the Office’s client agencies, and to clearly delineate the reporting requirements of the Office respecting non-complying agencies.

**7. Implementation of Section 412.054, relating to the development of Business Continuity Plans by state agencies pursuant to provisions of SB 908, 80<sup>th</sup> R.S. (State Office of Risk Management Sunset Legislation)**

Staff and resources recommended by Sunset to implement the statewide Business Continuity Planning (BCP) initiative were not appropriated during the 80<sup>th</sup> Legislature. The Office has notified state agencies of the statutory requirements, has published BCP guidelines on its website, and integrated BCP planning in the Risk Management Information System (RMIS). The Office's risk management specialists now review BCP plans as part of the Risk Management Program Reviews (RMPRs) conducted at client agencies.

Final reporting requirements and standards are in development to establish uniform review standards for completeness and viability. The Office has sought to establish an agreement to partner with the Governor's Division of Emergency Management (GDEM) on consistent BCP standards for all agencies subject to their respective authority. Training, funding, and resources for BCP and implementation may be available from the federal government; however, accessing those funds requires cooperation and coordination with GDEM, which serves as the state's single point of contact for federal participation. Resources for full implementation of the statutory BCP initiative have been requested in the Office's LAR to the 81<sup>st</sup> Legislature.

Current BCP planning documentation is available for review at [http://www.sorm.state.tx.us/Risk\\_Management/Business\\_Continuity/init\\_overview.php](http://www.sorm.state.tx.us/Risk_Management/Business_Continuity/init_overview.php).

**8. Implementation of Section 412.01215, relating to the development of Return to Work Coordination Services and Case Management pursuant to provisions of SB 908, 80<sup>th</sup> R.S. (State Office of Risk Management Sunset Legislation)**

Staff and resources recommended by Sunset to implement the statewide Business Continuity Planning initiative were not appropriated during the 80<sup>th</sup> Legislature. The Office has approached TDI and DWC to explore alternative options for implementation of the return-to-work (RTW) program and is actively evaluating approaches to address emphasis on RTW, including evaluating available case management and disability management approaches, considering appropriate guidelines and standards, and evaluating multiple methods for incentivizing RTW and for tracking RTW outcomes.

As of the date of this report, the Office has RTW guidelines published in Volume III, Section One, Chapter 5, of the Risk Management Guidelines for Texas State Agencies and is attempting to focus its existing Disability Management Team on disability management and enhanced RTW outcomes through use of the Official Disability Guidelines and Medical Disability Advisor treatment and RTW guidelines, medical profiling of claims information, and treatment planning. Resources for hiring the necessary case management expertise and full implementation of the statutory RTW initiative have been requested in the Office's LAR to the 81<sup>st</sup> Legislature.

Current RTW guidelines are available for review at [http://www.sorm.state.tx.us/RMTSA\\_Guidelines/Volume\\_Three/1Section1/315.php](http://www.sorm.state.tx.us/RMTSA_Guidelines/Volume_Three/1Section1/315.php).

## 9. Director's Section 412.042 report

Claims costs are now funded through IAC. The Office is administratively attached to the Office of the Attorney General, which provides significant administrative support and functions to the Office. The following data addresses General Revenue appropriations for administrative operations of the Office.

### Tex. Labor Code §412.042(a)(1) summary of administrative expenses

<i>Category</i>	<i>FY '08 Actual</i>	<i>FY '09 Budgeted</i>	<i>Biennium Total</i>	<i>Percent of Total</i>
Salaries	\$4,824,289	\$5,088,909	\$9,913,198	60.71%
Other Personnel Costs	\$503,339	\$333,268	\$836,607	5.12%
Contracted Services	\$1,815,045	\$2,415,520	\$4,230,565	25.91%
Consumable Supplies	\$50,845	\$50,000	\$100,845	0.62%
Utilities	\$4,073	\$4,330	\$8,403	0.05%
Travel	\$143,196	\$146,234	\$289,430	1.77%
Rent - Building	\$2,808	\$916	\$3,724	0.02%
Rent - Other	\$20,455	\$31,000	\$51,455	0.32%
Other Operating	\$404,049	\$469,300	\$873,349	5.35%
Capital	\$19,998	\$0	\$19,998	0.12%
<b>Total</b>	<b>\$7,788,097</b>	<b>\$8,539,477</b>	<b>\$16,327,574</b>	<b>100.00%</b>

### Tex. Labor Code §412.042(a)(2)(A) amount of the money appropriated by the preceding Legislature that remains unexpended on the date of the report

Of the total \$8.5 million appropriated for FY '09 administrative purposes, cash basis payments as of Dec. 22, 2008, total \$1,713,691 and an additional \$2,631,996 has been encumbered due to contractual or other obligations. Of the remaining balance of \$4,193,790, approximately \$450,000 has been incurred but not yet paid.

The Office has exercised \$45.5 million of its total authority for workers' compensation claim payments. Approximately \$1.8 million was carried forward from FY '08 assessments with the remaining amount collected by new assessments to client agencies. As required by Article IX, Section 15.02, collection of \$11.4 million has been deferred until mid-third quarter of the fiscal year and will be adjusted as necessary. As of Dec. 22, 2008, the cash balance remaining was \$23,581,559.

### Tex. Labor Code §412.042(a)(2)(B) estimated amount of balance necessary to administer Chapter 501 for the remainder of that fiscal year

The Office estimates that the full unexpended, unincurred, unencumbered balance of \$3.7 million for the administrative appropriation will be necessary for operations for the remainder of the fiscal year.

The Office estimates that roughly \$32 million will be necessary for workers' compensation claim payments for the remainder of the fiscal year. The remainder of the current balance will be applied toward the necessary amount for FY '08 or will be returned to agencies as directed by Article IX, Section 6.30.

**Tex. Labor Code §412.042(a)(3) estimate, based on experience factors, of the amount of money that will be required to administer Chapter 501 and pay for the compensation and services provided under Chapter 501 during the next succeeding biennium**

The Office estimates that \$9,587,914 for FY '10 and \$9,511,914 for FY '11, a total of \$19,099,828, will be required to administer the workers' compensation program and provide risk management and insurance services for the current biennium. This total includes exceptional item requests totaling \$2 million for the biennium. The Office's appropriation request is for \$3.78 million each year in General Revenue, the current base amount, with the remaining average \$5.77 million annually funded by interagency contracts through the annual assessments.

The Office is requesting authority of \$48 million in FY '10 and \$49 million in FY '11 for the appropriation to pay workers' compensation claims, funded by assessments. The Board of Directors determines the actual amounts to be collected each year based on the most current information available. The Office is requesting a single exceptional item of \$10 million each year in authority, should costs rise beyond the base request. As previously mentioned, the authority will be exercised only if necessary to pay statutorily mandated workers' compensation claim costs.

There are several factors that could result in potential increased costs. An immediate effect of the implementation of HB 7 networks could increase administrative and medical costs in the short term, with overall reductions due to improved treatment and outcomes seen in subsequent years. Decreases in administrative oversight and claims scrutiny due to resource reductions and the inability to retain trained, experienced staff may also have the effect of increasing overall costs.

**10. Insurance coverage purchased for state agencies, premium dollars spent to obtain that coverage, and losses incurred under that coverage**

Addressing many of the claims and losses experienced during the past biennium, state agencies acquired insurance coverages for a multitude of exposures. The following is a summary of policies acquired by fiscal year and line of coverage.

<i>Type of Policy</i>	<i>FY '07</i>		<i>FY '08</i>	
	<i>Number of Policies</i>	<i>Total Premiums</i>	<i>Number of Policies</i>	<i>Total Premiums</i>
Professional Liability	13	\$269,877	4	\$77,090
Directors' and Officers'/Employment Practices Liability	24	\$1,249,119	25	\$1,636,078
General Liability	12	\$352,106	17	\$373,571
Property	28	\$7,708,149	25	\$7,468,434
Automobile	31	\$710,754	33	\$657,715
Crime	13	\$78,990	9	\$63,953
Aircraft	1	\$194,010	1	\$233,417
Accident	17	\$71,095	18	\$65,887
Boiler & Machinery	4	\$35,403	1	\$22,270
Flood	1	\$1,124	40	\$60,096
Inland Marine	15	\$84,249	14	\$57,158
Umbrella	2	\$3,066	2	\$15,012
Workers' Compensation	2	\$1,528	2	\$4,781
Electronic Data	0	\$0	1	\$1,508
Excess Automobile	7	\$36,983	12	\$22,194
Excess Liability	9	\$20,026	13	\$28,147
<b>Total</b>	<b>179</b>	<b>\$10,816,479</b>	<b>217</b>	<b>\$10,787,311</b>

Non-Workers' Compensation Claims Frequency by Loss Type<sup>1</sup>:

<i>Claim Type</i>	<i>FY '07</i>	<i>FY '08</i>
Accident Insurance	0	0
Aircraft/Boat Physical Damage	2	3
Auto Liability	193	76
Auto Physical Damage	576	661
Boiler and Machinery	0	0
Crime	10	5
Directors' and Officers'	11	9
Electronic Data	9	31
Employment Practices	120	61
Environmental	1	0
Excess Automobile	8	0
Excess Liability	0	0
Flood	1	0
General Liability	392	143
Inland Marine	0	2
Professional Liability	8	5
Property Insurance	158	109
Surety Bond	0	0
Watercraft Liability	0	0
<b>Total</b>	<b>1,489</b>	<b>1,105</b>

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<sup>1</sup> FY '06 SORM 200 data, Section 2 Part 2