CLACKAMAS COUNTY BOARD OF COUNTY COMMISSIONERS

Policy Session Worksheet

Presentation Date: 5/10/16 **Approximate Start Time:** **3**:00 p.m. **Approximate Length:** 1 hr
Presentation Title: Risk Management Internal Audit Report
Department: Internal Audit
Presenters: Brian Nava, Internal Auditor and Shari Anderson, Treasurer
Other Invitees: Evelyn Minor-Lawrence, DES Director and Dwayne Kroening, Risk Manager

WHAT ACTION ARE YOU REQUESTING FROM THE BOARD?
This is an informational session, which will provide an overview of the results of the Risk Management Internal Audit.

EXECUTIVE SUMMARY (why and why now):
Internal Audit recently completed an audit over the Risk Management department at Clackamas County. This informational session will provide an overview of the key findings and recommendations outlined in the report. A brief summary of the key findings is outlined below and the full report is also available on the Internal Audit website at www.clackamas.us/internalaudit.

Key findings
Self-insurance rates and claims expense have significantly increased in the last few years. The burden of the increases affects the budgets of Clackamas County departments, and as a result, services to the public are less than they could have been.

Leveling procedures could be implemented to help reduce drastic swings in the overall amount allocated to County departments.

Risk factors and calculations which determine the insurance rates for County departments should be regularly evaluated. The risk factors and allocation calculation have not been formally evaluated since implementation in the late 1990's.

Claim approval tracking procedures should be improved to ensure adequate approval documentation is readily available.

Oversight of the third party administering casualty claims should be improved to ensure the payments are accurate and appropriate. Current procedures in place are not sufficient to prevent or detect duplicate payments and overpayments.

FINANCIAL IMPLICATIONS (current year and ongoing):

Is this item in your current budget? ☒ YES ☐ NO

Each year Internal Audit performs a risk assessment over Clackamas County and develops an annual audit plan. The annual audit plan details how internal audit anticipates spending their time throughout the calendar year. This plan is submitted and approved by the Internal Audit Oversight Committee (IAOC) and Internal Audit regularly meets with the IAOC to update them on Internal Audits progress and projects. The aforementioned audit was included in internal audits annual audit plan.

STRATEGIC PLAN ALIGNMENT:

- How does this item align with your Department's Strategic Business Plan goals?
  - This audit is part of the 2016 Internal Audit Plan approved by the Internal Audit Oversight Committee.

- How does this item align with the County's Performance Clackamas goals?
  - Building public trust through good government.

LEGAL/POLICY REQUIREMENTS:
N/A

PUBLIC/GOVERNMENTAL PARTICIPATION:
N/A

OPTIONS:
N/A

RECOMMENDATION:
N/A

ATTACHMENTS:
1. Risk Management Report
2. Risk Management Report PowerPoint

SUBMITTED BY:
Division Director/Head Approval _________________
Department Director/Head Approval _SA/bn_____________
County Administrator Approval __________________

For information on this issue or copies of attachments, please contact _____________@ 503-__________

Risk Management:

Insurance rate calculations and monitoring

March 2016

A Report by the Internal Auditor

Brian Nava
Clackamas County Internal Auditor

Shari Anderson
Clackamas County Treasurer

Executive Summary

Key Findings

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Key Recommendations

Our specific recommendations for management are included on page 16 of this report.

In summary, we made recommendations to improve:

- Allocation calculations,
- Oversight of the third party administrator, and
- Approval tracking.

Risk Management Response

The department generally agreed with our recommendations and is already implementing corrective action to address some of the weaknesses identified. The full response is at the end of the report.

Background

Clackamas County

Clackamas County has nearly 400,000 residents living within an area of approximately 1,900 square miles. Clackamas County employs approximately 2,400 full-time, part-time, seasonal and temporary employees, along with many volunteers. County government consists of departments organized to provide a number of services, including: transportation and development, sewer, public safety/law enforcement, tourism, public and government affairs, parks, libraries, community health and social services, taxation and assessment, housing, as well as internal administrative services.

Heritage Trail, Billie Hurley, DES

Risk Management

The County has elected to use self-insurance, unless they have determined it to be more efficient to purchase commercial insurance. The management and control of the County's risk management program is a function of the Risk and Benefits Division, within the Department of Employee Services (DES). A Risk Management Committee, consisting of various County department Directors, provides oversight of the risk management function. The day-to-day management is provided by the Risk Manager. The primary areas managed through this program are: liability, worker's compensation, vehicles and unemployment claims administration, loss control services, insurance, and contracts.

Risk management consists of six employees. Three are Safety and Loss Control Analysts (analysts). One analyst is generally allocated to departments at the Developmental Services Building, one analyst is generally allocated to departments at the Public Services Building (including the Clackamas County Sheriff's Office,) and the last analyst is fully dedicated to Water and Environment Services (WES). The WES analyst's salary is paid for by WES.

> *Management's philosophy is that the management of risk must be so much a part of County culture that it becomes a value rather than merely a priority that shifts as other priorities change. An established principle of managing risk, is to take steps to prevent loss. The goal of risk management is that every employee has the benefit of a systematic effort to be provided a safe, secure and healthful workplace.*
>
> - *Risk Management Website*[1]

Responsibility for hazard recognition and implementing controls to reduce risk resides with all County departments. The risk management unit is a resource that can be used to assist the various departments in identifying and mitigating risks. The department issues an annual report on the internet that provides information on reviews performed and incident activities. Generally, it is the responsibility of the individual departments to engage risk management for assistance in developing safety and health loss prevention plans.

Risk Management Allocation Overview

Risk management is accounted for in the Risk Management Claims Fund and consists of three cost centers:

- **Casualty (or Liability)**

  This account covers insurance against claims following negligence by the County's employees who cause injury to people or damage to property, equipment, or machinery. (i.e. liability claims, vehicle claims, etc.)
- **Worker's Compensation**

  This account provides money for medical services and disability compensation for workers who are injured at work or contract an occupational disease.
- **Unemployment Insurance**

  This account provides a source of income for County workers who have lost their jobs, generally through no fault of their own.

Each County department is allocated a portion of the cost needed to fund the accounts outlined above. Beyond the claims incurred by each County department, departments have little control over the amount of cost they are allocated.

[1] http://www.clackamas.us/des/risk.html

Audit Results and Recommendations

Clackamas County excels with the Risk Manual

Risk management has documented most policies and procedures related to the administration of risk management. Only one other municipality of the four surveyed has a similar up-to-date comprehensive manual describing the administration of risk management (Figure 9).

Opportunities exist to improve funding documentation

The County contracts with an actuary to perform actuarial projections of expected losses based on the prior loss history of the County. The actuary helps determine the total amount that should be funded to the aforementioned cost centers. Risk management's goal is to maintain an unpaid losses and allocated loss adjustment expense (ALAE) fund balance at the 75th percentile, as determined by the actuary. This is generally consistent with the goals of other counties who manage their self-insured funds.

There are a number of valid reasons why management may decide to deviate from the overall funding amount determined by the current methodology.

For example:

- The current fund balance meets the 75th actuarial objective, but instead of lowering the overall amount, management would like to build some excess fund balance while not increasing previous rates charged to departments.
- The calculation takes into account significant claims that are unlikely to occur in the future.
- Instead of determining the overall funding amount for the casualty and worker's compensation funds separately, management analyzes both funds together. This can occur when one fund has excess fund balance and one fund has a depleted fund balance, as compared to the actuarial 75th percentile objective.
- Competing or lack of resources could make it necessary to reduce the amount of funding to not meet the 75th actuarial objective.

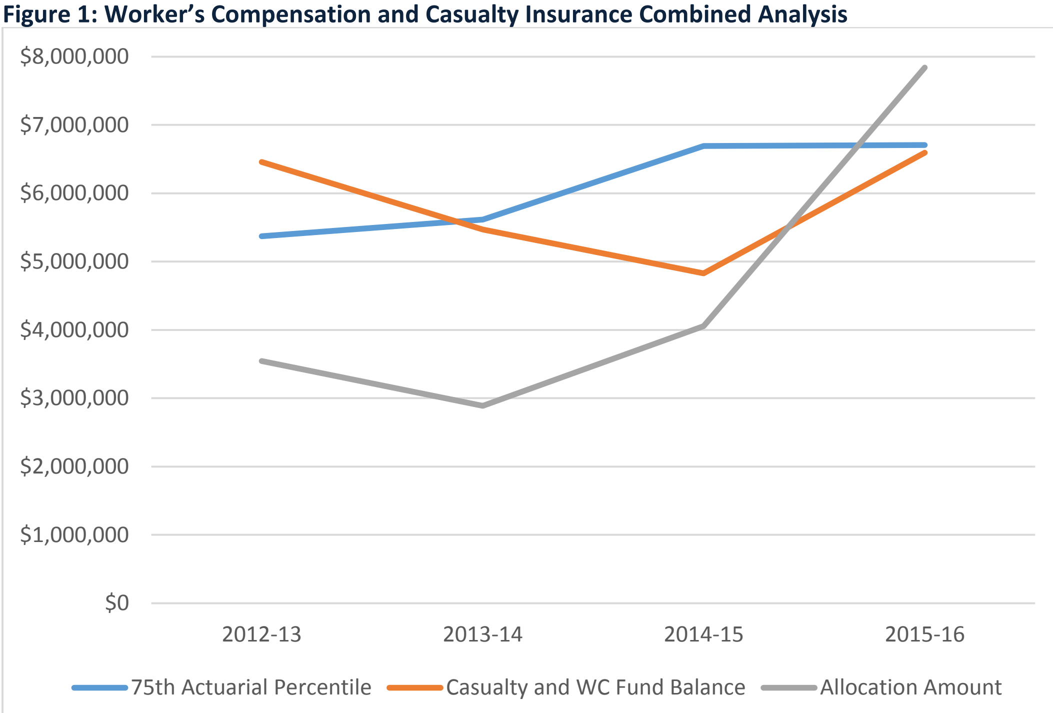
We identified instances where adequate documentation was not maintained to support the funding amounts. Lack of documentation increases the risk that errors could occur and insurance pools will be insufficient to pay the necessary costs.

***We recommend** risk management document the methodology to calculate the funding amounts and incorporate this methodology into the Risk Manual. Adequate documentation should then be readily available when deviations from this methodology are determined necessary.*

A few unexpected claims and underfunding has led to the recent significant increases in allocated charges

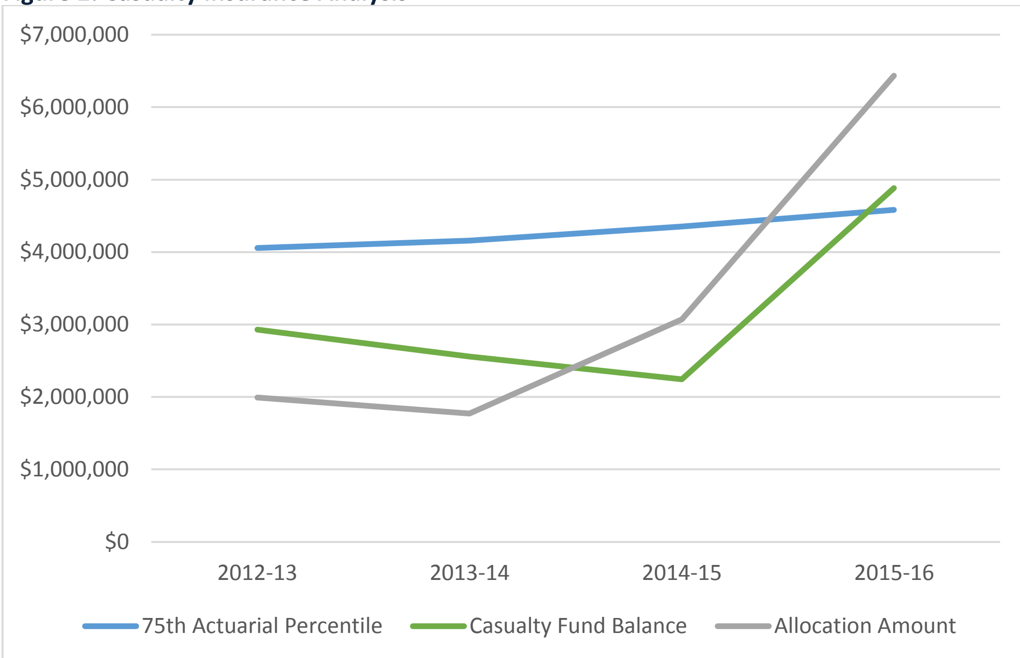
As shown in Figures 1 through 3, the casualty amount of funding has not been adequate to meet management's objectives and the worker's compensation (WC) amount has deteriorated significantly, such that the County is currently slightly below the management goal of the 75th percentile. Consequently, risk management has been forced to increase the amount of allocated charges in recent years to meet their funding goals for the casualty and worker's compensation fund (Figure 1).

Figure 1: Worker's Compensation and Casualty Insurance Combined Analysis



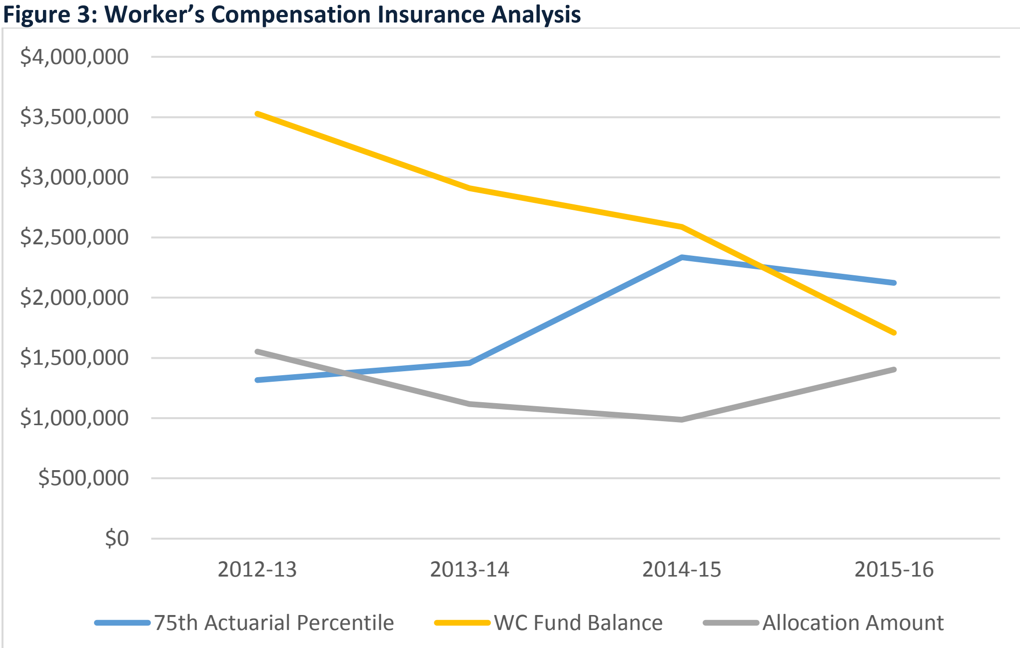
The significant increases to allocated costs associated with the casualty insurance fund have assisted risk management in achieving its funding goals.

Figure 2: Casualty Insurance Analysis



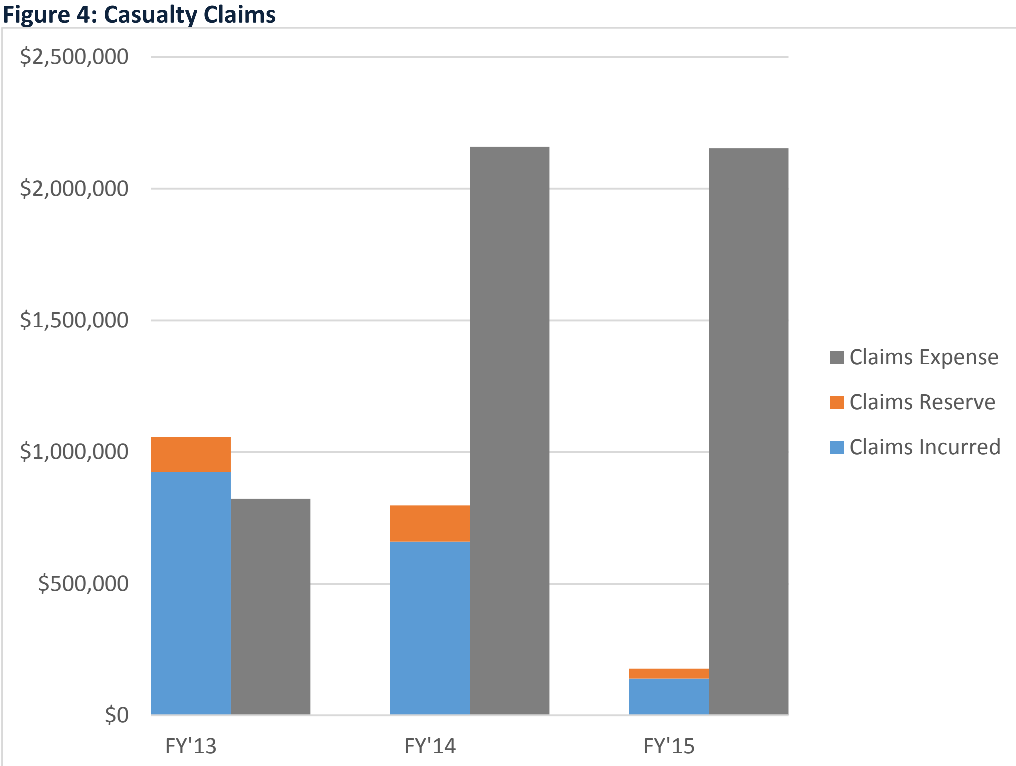
Allocated costs associated with the worker's compensation fund have remained relatively constant. This has helped reduce the burden on departments who have felt the increased casualty insurance allocated costs.

Figure 3: Worker's Compensation Insurance Analysis



Additionally, the actual claims expense may not financially implicate the County for a period of time after the actual date the claim was incurred. In Figure 4, we can see the total amount of claims expense from the County's financial management system has increased significantly in fiscal years (FY) 2014 and 2015, even though the actual amount of payments made on claims incurred during that same time period is significantly lower.

Figure 4: Casualty Claims



"Leveling" could reduce drastic allocation swings

Many other municipalities use a process referred to as "leveling". Leveling, in this context, is when risk management bills departments the same amount, even though they have achieved their funding goals. This creates a cushion to assist with the payment of significant unexpected claims. As shown in Figure 1, management reduced the amount to charge County departments in 2013-2014 when the County was very close to meeting their goal of having a fund balance at the actuarial recommended 75th percentile. Had management billed the same amount from the previous year, they would be above their funding goals and departments would generally still feel the same impact from the previous year. ***We recommend*** *risk management incorporate this process of "leveling", to help stabilize budgets for departments in the future as departments will have a better ability to more accurately perform long range budgeting.*

Departmental allocation calculation needs regular evaluation

As outlined in Section 2 of the Risk Manual[2], allocated costs are generally determined using the following factors:

- Most recent three fiscal years of payroll,
- Estimated current fiscal year payroll expenses,
- A risk adjustment factor, and;
- Most recent three fiscal year loss experience (claims) with a claim cap limit.
    - For example, in fiscal year 2014-15 worker's compensation claims were capped at $30,000 per claim, per occurrence; while casualty claims were capped at a $50,000 per claim, per occurrence.

Risk adjustment factors are not regularly revaluated

Risk factors have not been formally reviewed since implementation in the late 1990's.

The risk allocation process as well as the current risk adjustment factors were developed for use in the late 1990's allocations, by risk management and an actuary. The risk adjustment factors have not been formally reviewed for appropriateness since implementation. Updating risk factors may result in more accurate forecasting and increased efficiency in budgeting.

Adequate documentation was not maintained

While all factors do play a role in determining the amount allocated to each department, the "risk adjustment factor" is the only one that is based on management discretion. In the 2015-16 allocations the risk adjustment factor ranged from 1 through 7. Clear documented criteria did not exist to determine when a department would be ranked a risk adjustment factor of 1 and when they would be ranked a risk adjustment factor of 7.

For example, one department reviewed their risk adjustment factor with management related to their casualty insurance allocated charges for fiscal year 2016. Their risk adjustment factor was then reduced from 4 to a range of 1 through 3.2. They were able to cut their overall allocated casualty insurance costs in half. ***We recommend*** *management perform a regular formal review of departments' risk adjustment factors and develop clear documented criteria for the factors used.*

[2] Risk Manual effective 10/9/2013, http://www.clackamas.us/des/riskmanual.html

Ensure allocated amount received, matches amount requested

In fiscal year 2013, risk management received more in casualty insurance, than requested via their allocation calculation. In fiscal year 2014, risk management received some of their allocated funds in the wrong account. In both instances, these errors were not discovered by the County. ***We recommend*** *risk management ensure they receive the correct allocated amount and that funding is receipted to the correct cost center.*

Tracking of claim approvals could be improved

Neighboring counties generally employ a similar process of claims review as Clackamas County (Figure 5 & 9). An important element in that review is the interaction between Risk Management, County Counsel, County Administration and the Board of County Commissioners (BCC). Most claims only rise to the level that require approval from the Risk Manager and County Counsel (i.e. <$40,001). It was noted by management, that because all interaction between the County's current third party administrator (TPA) and the County, is performed by risk management, approval from County Counsel is not always maintained. We also found opportunities for management to improve the method of capturing BCC approval. Ensuring appropriate levels of approval are documented is an important aspect in supporting the action taken. ***We recommend*** *risk management develop a systematic way to track and have approval documentation readily available.*

Casualty claim payment review needs immediate attention

Management is responsible for ensuring internal controls are adequate to provide reasonable assurance that transactions are accurate, properly recorded, and executed in accordance with management's objectives. That same level of assurance is required for services and financial information provided to the County by independent third party service providers.

During the audit, we noted that management does not always have assurance that information processed through their third party administrator is accurate and reliable. The department has relied on an independent third party to process its casualty type insurance claims. This third party processes casualty eligible claims including payments to providers and individuals, and other non-claim payments and transactions. The third party processed over $2 million in expenditures in fiscal year 2015.

Currently no consistent method of tracking or reconciling claims exists over casualty claims processed by risk management's third party administrator.

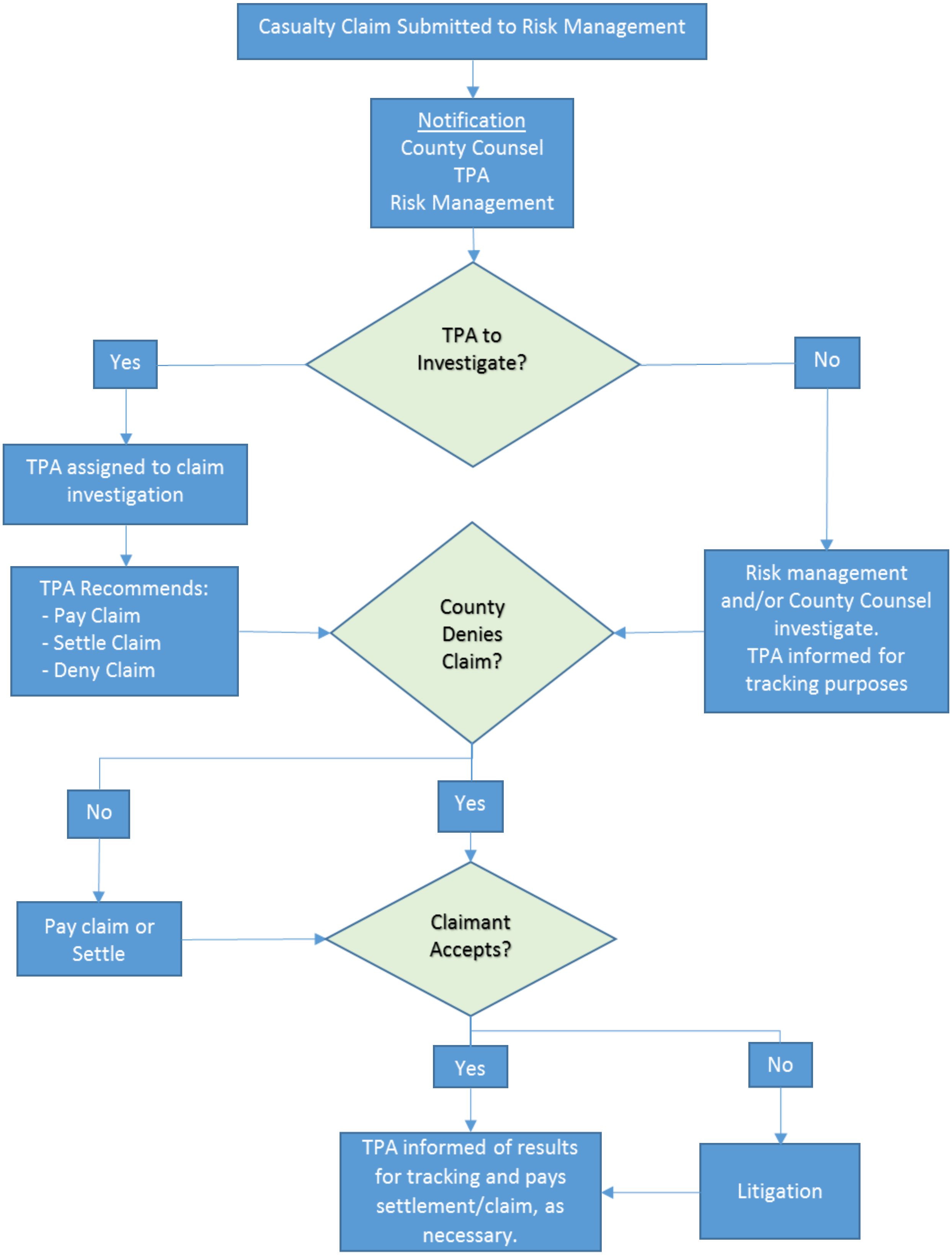
Risk management has read only access to the third party administrator's system to view claims and the amount of payment made on each claim. Management asserted periodic reconciliation of the third party administrator expenditures does exist to ensure appropriate payment has occurred. However, this analysis does not occur on a regular basis and exposure exists, such as:

- Being billed and/or making payment twice for the same claim, or;
- Overpayment on a claim the County is paying over an extended period of time.

Although no duplicate payments or overpayments were identified as a result of testing procedures performed, current processes and procedures in place would allow for these errors to occur and go undetected.

Department management should seek adequate assurance for the accuracy of all financial information they report. ***We recommend*** *management implement review procedures to ensure the integrity and accountability of the information from the casualty claims third party administrator.*

Figure 5: Casualty claims process



Additional insurance purchased appears adequate

The County has elected to retain exposure to loss primarily through self-insurance. The County will only transfer exposure through purchased insurance when the premium cost has been determined to be cost efficient to the exposure.

We were able to perform some high level comparisons of additional insurance purchased by our neighboring counties to that of insurance purchased by Clackamas County. In general, Clackamas County had elected to purchase additional insurance similar to that of the neighboring counties. Additional insurance is important when considering varying courses of action. For example, from fiscal year 2013 through fiscal year 2015 the County has paid approximately $1 million in on-going expenses related to one claim incurred in 2002 and received approximately $1 million in reimbursement as result of the additional insurance purchased. Without additional insurance, the costs of this one claim, over time, could deplete the worker's compensation insurance fund or cause the County to have to pay a significant amount of cost to cover worker's compensation.

Vehicle liability appears inequitable

Vehicle liability is encompassed in the casualty insurance allocation performed by risk management.

The two elements in the allocation calculation that would consider vehicle risk are:

- The risk adjustment factor, and;
- Actual claims (in conjunction with all casualty related claims)

By including vehicle liability in the casualty insurance allocation, all departments are absorbing vehicle liability costs. Other counties we spoke with indicated these factors may not equitably allocate the vehicle liability risk across departments. For example, departments that do not frequently operate a vehicle related to County business, would be helping absorb the vehicle liability risk. Three of the four self-insured municipalities we spoke with allocate costs associated with vehicle liability separately from casualty liability (Figure 9).

Figure 6: Average Casualty Claim Count Fiscal Year 2013 - 2015

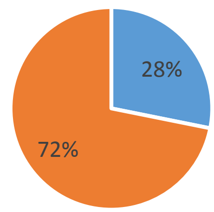
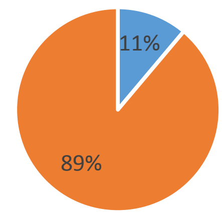
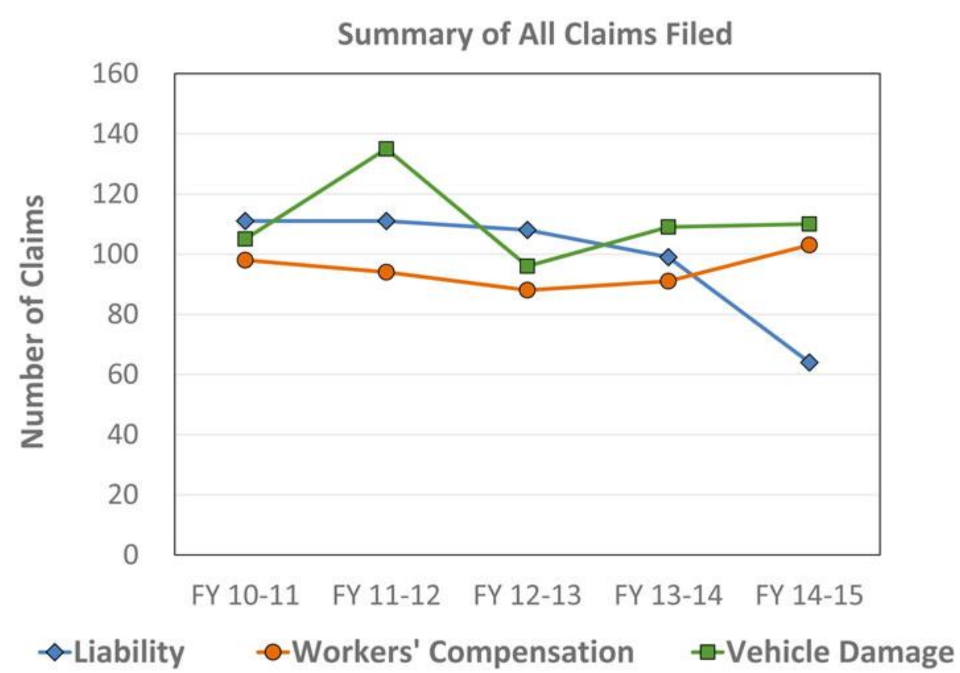


Figure 7: Average Casualty Claim Cost Fiscal Year 2013 - 2015



Further, by risk management's own analysis (Figure 8), the number of vehicle claims filed is as much, if not more, than liability (casualty) and worker's compensation claims filed in recent years.

Figure 8: Summary of all claims filed



Source: 2015 Risk Management Report

We recommend *risk management consider separating vehicle liability from the casualty insurance allocation.* This is based on the significance of the number of vehicle claims paid and filed in recent years, as compared to all casualty claims submitted and filed, respectively (Figures 6 through 8).

Long-term goals of risk management appear appropriate

Oregon Public Entity Excess Pool

The Oregon Public Entity Excess Pool (OPEEP) is one long term measure the County is taking to purchase additional liability insurance. As previously outlined in this report, additional insurance is one important aspect of effective claims management.

Create an actuarially sound fund

Current increases have allowed the worker's compensation and casualty fund the ability to meet its actuarial funding goal of the 75th percentile. Risk management has also recently contracted with a vendor to review their methodology for allocating costs to each department.

Promote safety

Continue to work with departments to promote safety and reduce risk. Limited resources do make this goal a challenge at times, but management is hoping to work with departments and continue to get their buy-in that safety is their responsibility and it is a priority.

Future claim consideration

The County is a defendant in various lawsuits. The likely outcome of these lawsuits is not determinable as of December 30, 2015; however, County management intends to defend these lawsuits vigorously and believes the likely outcome will not have a material adverse effect on the County's basic financial statements.

Recommendations in Summation

To improve risk management processes, we recommend department management:

- Document the methodology for determining the total funding amounts for casualty and worker's compensation. "Leveling" should be considered when appropriate.
- Develop procedures to ensure management maintains adequate supporting documentation related to the funding for casualty and worker's compensation. This is particularly important when management deviates from their standard methodology.
- Develop and document clear criteria for determining the subjective risk factors used which contribute in calculating each department's allocated amount.
- Formally regularly evaluate the allocation calculation and subjective factors used in the allocation calculation. An example of a subjective factor used in the allocation calculation is the risk adjustment factor.
- Implement procedures or verify procedures are implemented by other departments to ensure the allocated amount requested is received and received to the appropriate cost center.
- Develop a system to effectively track claim approvals and ensure documentation associated with those approvals is readily available (i.e. County Counsel, County Administrator, and the Board of County Commissioners).
- Implement review procedures to ensure the third party administrator providing casualty claims administration is billing the County the appropriate and accurate amount.
- Consider allocating vehicle liability (insurance) costs separately from casualty insurance.

Objectives, Scope and Methodology

Our audit objective was to evaluate the allocation and claims management processes.

We focused on the department's methodology to calculate the overall funding amount as well as the methodology to determine the amount to allocate to each of the County's departments.

To address our audit objective, we interviewed risk management department managers and employees, employees throughout the County, and employees from other counties throughout the state of Oregon who operate their self-insurance fund(s).

We interviewed agency managers and staff to understand procedures for determining the overall amount to allocate as well as the amount to allocate to each department. We learned of existing challenges the risk management department faced.

We reviewed state laws, administrative rules and management best practices related to the department and our audit objective. We also reviewed the department's risk manual and the 2013 through 2015 risk management report.

To understand the department's financial position, we reviewed documents on the department's revenues, expenses and budgets. We also reviewed the department's revenue and expense data we extracted from the County's financial management application. We were provided with detailed data from the third party administrator's casualty claim processing system and the County's worker's compensation claim processing system.

To understand actions staff took in making payment on claims, we reviewed seven transactions from the casualty claims fund and seven transactions from the worker's compensation fund. We selected these transactions judgmentally, looking to ensure adequate supporting documentation was available and the appropriate level of approval was documented. Our population consisted of expenses from the casualty and worker's compensation cost center from June 2014 to October 2015. The sample is not statistically representative of all expenses during the aforementioned time period.

An auditor from another organization, who was not involved with the audit, reviewed the report for accuracy, checking facts and conclusions against the supporting evidence. This auditor is a Certified Public Accountant and Certified Internal Auditor.

The courtesies and cooperation extended by officials and employees of the Clackamas County Department of Employee Services and County Administration during the course of this audit were commendable and sincerely appreciated.

Supplementary Information

How we compare to other self-insured municipalities

We spoke with staff and management from three counties and one city who self-insure their respective organizations to see how we compared. Two of the three counties surveyed, are neighbors of Clackamas County. Highlights from those conversations are outlined below.

Figure 9: Comparison to Other Self-Insurance Funds

Question	Clackamas County	County 1	County 2	County 3	City 4
Is the cost associated with vehicle liability allocated separately from other insurance (e.g. worker's compensation, casualty, unemployment)?	No	Yes	No	Yes	Yes
Who does risk management report to?	Department of Employee Services	Deputy County Administrator in Support Services (includes Human Resources and Finance)	Chief Financial Officer	County Administrator	Bureau of Internal Business Services
Do you use a third party to assist in claims administration?	Yes	Yes	Yes	No	No
Do you have formalized and up to date policies and procedures for risk management?	Yes (Risk Manual)	Yes (Risk Policies)	No (Currently in draft form)	No	No (Current policies are out of date)
What is your ALAE funding level percentage?	75% Goal	70 - 90%	70 - 75%	75%	75 - 80%
What is your single claim approval level?	Figure 12	Risk Manager: $10,000 DC[3] Administrator: $50,000 BCC: Over $50,000	County Counsel: $10,000 BCC: Over $10,000	Risk Manager: $10,000 BCC: Over $10,000	Risk Manager: $5,000 City Council: Over $5,000
Participating in OPEEP[4] or plan to participate in OPEEP?	Yes	Yes	No	Yes	No

[3] Deputy County
[4] Oregon Public Entity Excess Pool

How our reporting structure compares to other municipalities

Self-insurance functions report to human resources, finance or a combination of both. In general, risk management believes human resources (i.e. the Department of Employee Services,) is the appropriate location for risk management. Risk management contends human resources connects the management of risk with the primary place that generates risk. In other entities where risk management reports to other departments, such as Finance, Clackamas County Risk Management did not see enough emphasis put on human factors and prevention related to those factors. There did not exist compelling information from management and staff interviewed from other self-insured funds which indicated one reporting structure was significantly better than the other.

Claims can be paid over time

Figures 10 and 11 present data as of November 2015, based on the date of loss the claim was incurred. The total reserve indicates the future amount the County anticipates paying out on those claims incurred in that period.

Figure 10: Casualty Claims

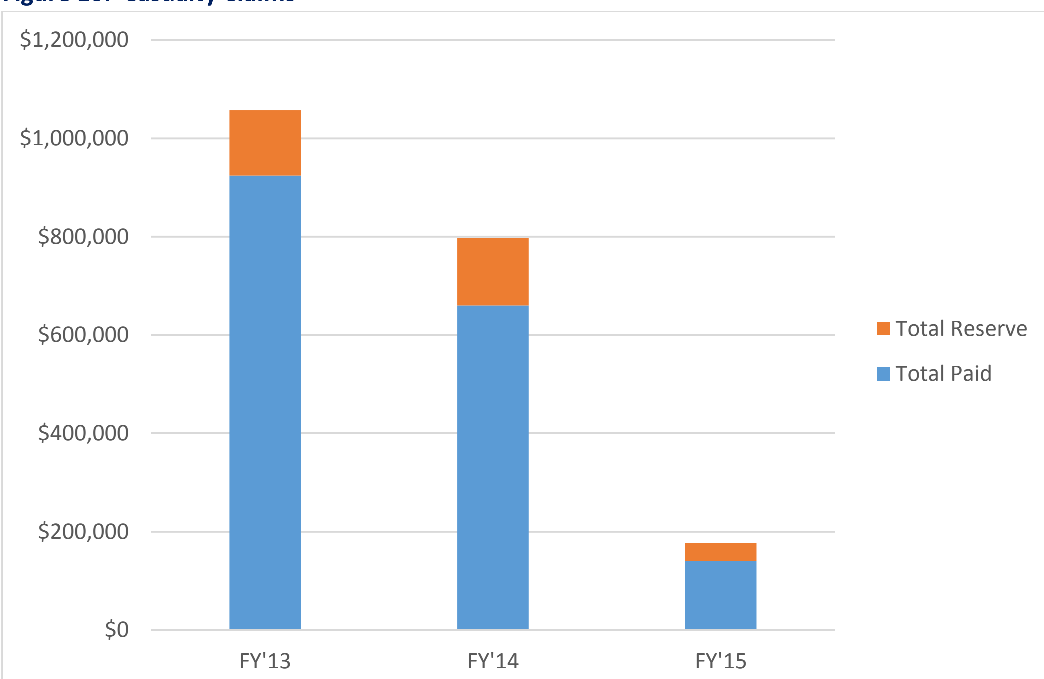


Figure 11: Worker's Compensation Claims

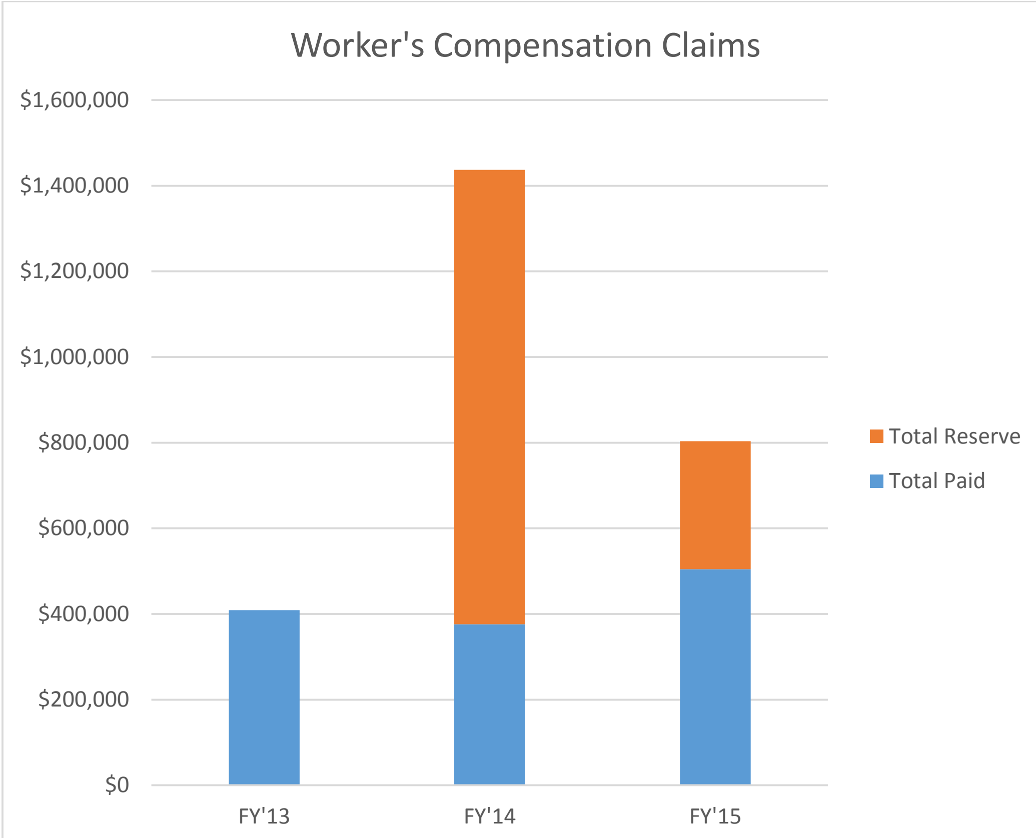


Figure 11 Note: There exists one worker's compensation claim that was incurred in fiscal year 2014 that accounts for 98.6%, or over $1 million, of the fiscal year 2014 reserve.

Individual claim approval levels

Figure 12: Casualty Claim Approval Levels

Approval Levels	Who Approves?
$0 to 5,000	Risk Manager
$5,001 to 40,000	Risk Manager and County Counsel
$40,001 to 80,000	Risk Manager and County Counsel with advisement from County Administrator
$80,001 to 100,000	County Administrator approval with Board of County Commissioner (BCC) advisement
Greater than $100,000	Requires formal BCC action

Worker's compensation approval is delegated to the Risk Manager and is only limited by the amounts authorized by the Finance department.

The County's policy is to defend itself against all nuisance claims. However, if the Risk Manager and County Counsel agree that the cost to defend a disputed claim is greater than the settlement amount, it is within their discretion to settle that claim (subject to the approval limitations described above).

Additional Insurance

Figure 13: Additional Insurance (as of November 2015)

Coverage	Deductible[5]	Limit
Property/Boiler Machinery	$25,000	$200,000,000[6]
Earth Movement	3% of property value[7]	$25,000,000[8]
Flood	$100,000[9]	$15,000,000
CCSO Inland Marine	$15,000	None
Volunteer Liability and Medical	$75[10]	None
Excess Worker's Comp.	$1,000,000	Statutory[11]
Excess Public Entity Liability	$1,000,000	$9,000,000[12]
Flood Plain Coverage	$3,000[13]	$500,000
Garage Liability	None	$1,000,000
Hull/P&I	$7,500 – M.J. Lee Ferry Hull $5,000 – Hull, all other vessels $2,500 – Protection and Indemnity coverage	None None $2,000,000
Marine Pollution Liability	None	$1,000,000
CCSO[14] Owned Aviation Liability	None	$3,000,000
Auto Liability – 15 Passenger Vans	None	$1,000,000

Allocated cost distribution has not changed

As shown in Figures 14 and 15, allocated costs have generally been distributed the same to each department, each year.

This is mainly attributed to:

- Risk factors have generally not been reevaluated nor changed in over 15 years.
- The calculation to allocate insurance costs has not changed in over 15 years.

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[5] All deductibles are paid by the department filing the claim, unless otherwise noted. The Risk Fund pays the first $5,000 of the $15,000 property deductible.

[6] Per occurrence.

[7] Minimum of $250,000.

[8] Per event.

[9] Additional coverage for high-risk flood plain locations is under a separate policy.

[10] Paid by volunteer.

[11] Coverage for loss on any worker's compensation claim (Part A) above a self-insured retention (SIR) level of $1 million up to the statutory limit per claim. Also includes a $1 million Employer's Liability excess (Part B) above a $1 million retention. The SIR level is met through a combination of Part A and Part B.

[12] Coverage for loss on Federal claims above a SIR of $1 million up to $7 million per claim.

[13] Deductible for each building and contents.

[14] Clackamas County Sheriff's Office

Figure 14: Worker's Compensation – Allocated Insurance Costs (by Department)

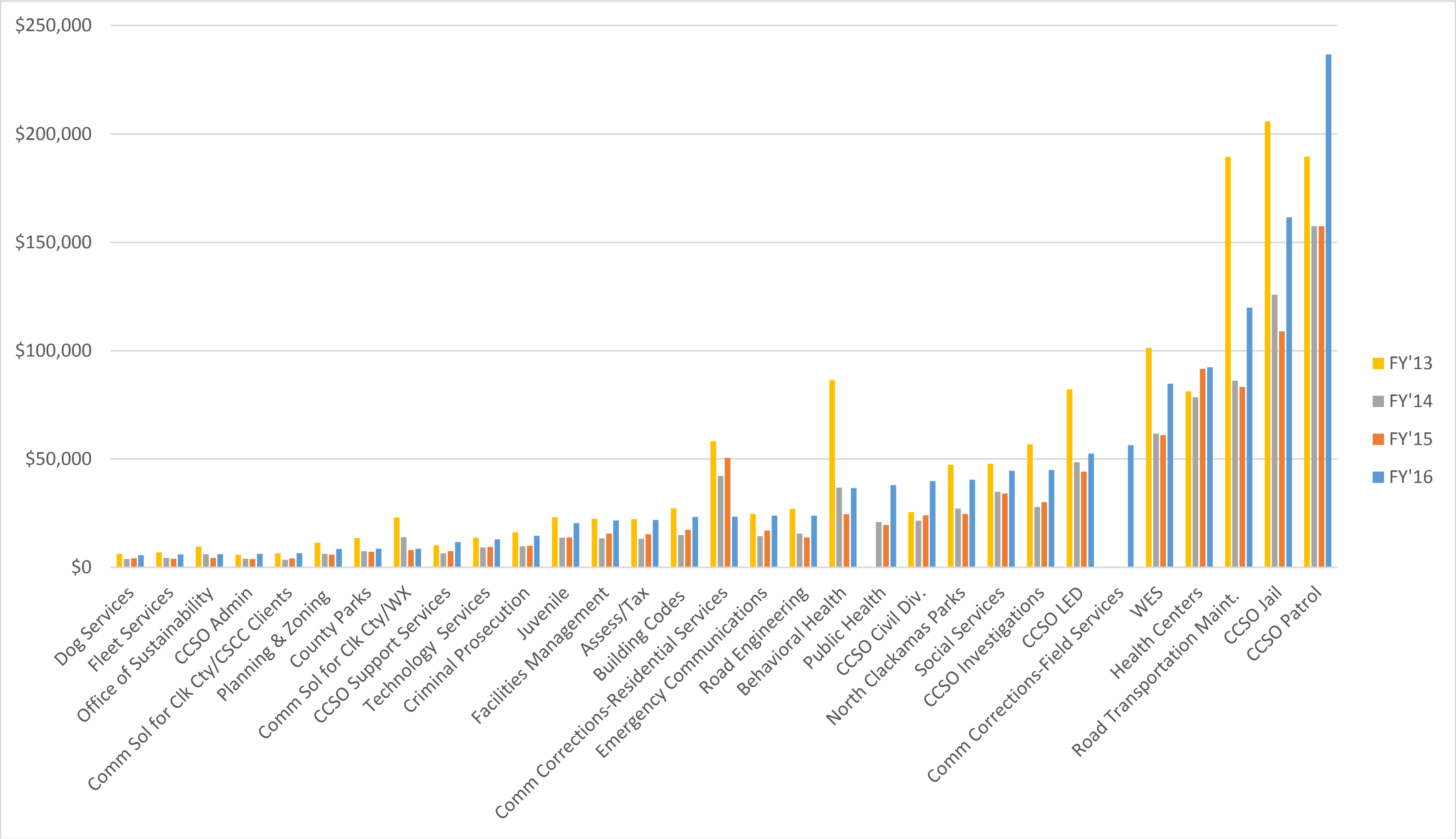


Figure 14 Note: Only departments with significant allocated amounts were included in this figure.

Figure 15: Casualty – Allocated Insurance Costs (by Department)

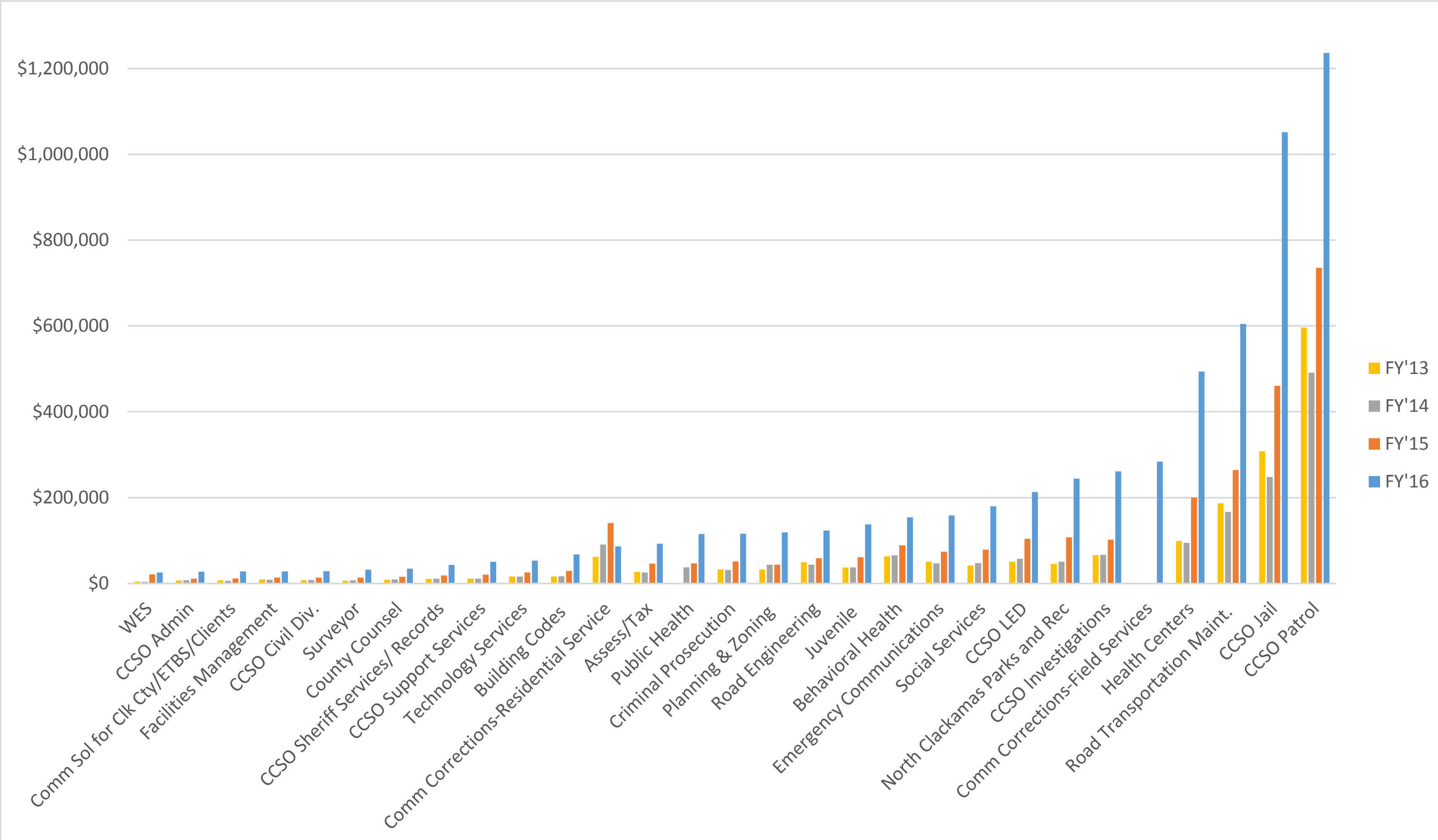
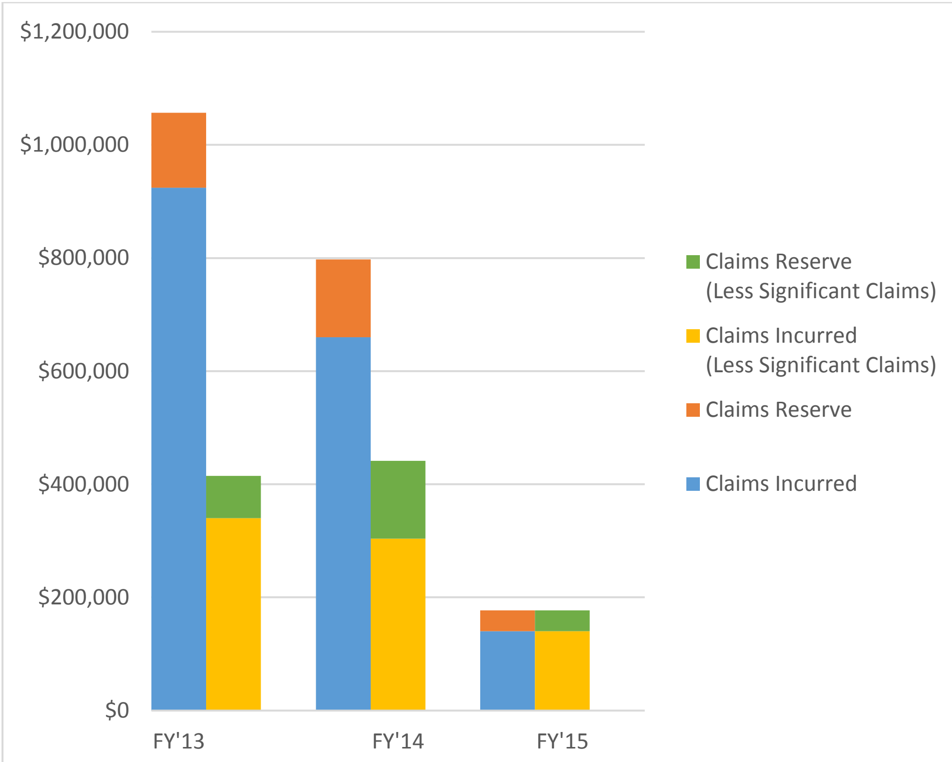


Figure 15 Note: Only departments with significant allocated amounts were included in this figure.

A few claims caused the significant increase in incurred costs

As shown in Figure 16, if we remove the three most expensive casualty claims incurred in fiscal year 2013 and the one most expensive casualty claim incurred in fiscal year 2014 we end with significantly lower costs.

Figure 16: Casualty Claims



County photos courtesy of Oregon's Mt. Hood Territory

EVELYN MINOR-LAWRENCE
DIRECTOR

CLACKAMAS COUNTY

DEPARTMENT OF EMPLOYEE SERVICES

PUBLIC SERVICES BUILDING
2051 KAEN ROAD | OREGON CITY, OR 97045

Risk Management's responses to Audit Recommendations:

Dwayne Kroening, Risk Manager, is the contact person responsible for corrective action.

1. Recommendation – Risk Management document the methodology to calculate the funding amounts and incorporate this methodology into the Risk Manual.

   Response – Agree. We are in the process of updating and refining existing documentation of the methodology used to calculate the funding amounts. Completion of this step by step process will be completed prior to January 2017 and will be executed as part of the 17/18 fiscal year allocation calculations. The written methodology will be placed in Section 2 of the Risk Manual when the update is complete.

2. Recommendation – Risk Management incorporate a process of "leveling", to help stabilize budgets for departments in the future as department will have a better ability to more accurately perform long range budgeting.

   Response – We generally agree that "leveling" is an important consideration in bringing stability to budgets and accurately performing long range budgeting. However, there are some other factors that must be considered as well.

   "Leveling" is one of the benefits of using the current allocation model because it uses payroll and claims data from multiple years. This diminishes some of the potential fluctuations that are caused by a large increase or decrease in payroll or claims from one year to the next. However, there are external factors that can influence the amount of the allocations that must be acknowledged.

   It bears noting that external factors such as economic stressors, property tax revenues, department funding streams, County strategic goal prioritization, can potentially influence the decision of how much to allocate. While Risk Management provides recommendations to the County Administrator for the allocation amount, the final decision is made by the County Administrator with consideration given to these external factors. Thus, the consideration of "leveling" and any agreed upon deviations will need to take into account all of the demands on available resources. Consideration has been and will continue to be given to minimizing swings in department allocations.

   The funding methodology noted in the first recommendation and response will include a step where the decision referenced above involving the County Administrator, including any

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deviation, is documented in written form (by email to all parties present for confirmation of the decision) and preserved in the allocation file kept by the Risk Manager.

3. Recommendation – Management perform a regular formal review of departments' risk adjustment factors.

   Response – We agree with the audit finding that no formal review of the risk adjustment factors has been completed. However, there have been informal reviews of these factors to some degree each year since the inception of the allocation model.

   It is important to note that the current risk factors were developed with the assistance of the professional expertise of an actuarial firm. The factors themselves were established using insurance industry data.

   With regard to the informal reviews that have been done in the past, each year when the allocations were calculated for the following year, thought was given to the appropriateness of the risk factors by the Risk Manager. Any changes in a department's risk exposure were considered. Also, there were discussions with department personnel when questions about the allocations would arise. These discussions often included the suitability of the risk factors. This occurred a few times each year.

   Department management is educated during mandatory workers' compensation training on the role risk factors play in the allocation model and the impact they have.

   Risk Management is currently conducting a comprehensive review of the allocation model with the help of an actuarial firm. An analysis of the risk factors based on insurance industry data (NCCI class codes and AM Best hazard index descriptions) is part of this review. The updated model will be completed in time for the 2017 allocation calculations in early 2017.

   A statement will be added to the allocation section of the Risk Manual by June 30, 2016 indicating that the allocation model, including the risk factors, will be formally reviewed for appropriateness and updated where necessary every five years or when a particular change is warranted. Informal reviews will continue to occur on an annual basis as before.

   Recommendation – Management develop clear documented criteria for the factors used.

   Response – We agree that clear documented criteria for the risk factors should exist. At the time the current factors were developed documented criteria existed. However, it has become obsolete due to the length of time since they were developed.

The current review underway will identify the industry standards that exist for the factors and notes will be added to the spreadsheet to describe the thought process behind any changes based on differences that may exist from the industry standard.

4. Recommendation – Risk Management ensure they receive the correct allocated amount and that funding is receipted to the correct cost center.

   Response – We are in agreement with the recommendation to the degree that Risk Management can determine that errors have been made in the accounting system and see they are corrected.

   Risk Management calculates the Casualty and Workers' Compensation allocations and provides the amounts, broken down by division, to Finance/Budget. Budget then places the amounts in each division's budget in the BRASS system. Receipt of those amounts into the Risk Fund is a process that occurs outside the Risk Division.

   By June 30, 2016, Risk Management will add a reminder to its year-end financial reconciliation procedure. The reminder will direct that a query from Peoplesoft Finance entitled CC_761_REV_Detail (for both Casualty and WC) be run around the second week of June which will be used to compare the aggregate allocated amount that has been collected (found on the the Rev Comparison Report) to what was provided to Budget at the beginning of the fiscal year. It will also be used to ensure the revenues were posted to the correct cost center. This will ensure that the Risk Fund has received the correct allocated total.

5. Recommendation – Risk Management develop a systematic way to track and have approval documentation readily available.

   Response – Agree. This recommendation relates to the need for a system to effectively track claim payment (specifically "settlements") approvals and ensure documentation is available.

   The audit report describes the process whereby liability claims are settled and the approval(s) necessary depending on the amount of the settlement.

   A procedure will be written by the end of May 2016 that describes the necessary documentation required before a payment is made. The process will describe the documentation of agreement (where appropriate based on the level of approval needed) between Risk Management, County Counsel, County Administration, the BCC, and the third party claims administrator concerning settling the case at the agreed upon amount. This documentation will become part of the claim

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file within the County's Risk Management Information System (RMIS) and be readily available either through a query or immediate access in the claims RMIS.

We believe that Section 5/ Claims Management of the Risk Manual is the most logical place for this written procedure to reside.

6. Recommendation – Management implement review procedures to ensure the integrity and accountability of the information from the casualty claims third party administrator (TPA).

   Response – Agree. We propose that the TPA undergo a biennial SSAE 16, Type II external audit of their financials. This will ensure the integrity and accountability of the exchange of financial information between the County and the TPA. The current TPA, Farrell and Associates has agreed and the first audit of this nature would audit the 15/16 fiscal year.

   In addition, Risk Management will conduct a reconciliation of its internal financial processing on at least a semi-annual basis. The reconciliation will cover the Casualty and Workers' Compensation areas. The reconciliation will include such things as; posting errors such as duplicates or omissions, data entry errors, settlement detail instructions not complied with, etc.

7. Recommendation – Risk Management consider separating vehicle liability from the casualty insurance allocation.

   Response – We agree that including vehicle risk within the general casualty area may raise a question about the equity between departments depending on the extent to which they use vehicles. However, the concern about any perceived inequity may be alleviated with an understanding of the degree to which vehicle risk exposure is contemplated in the risk factor assigned in the general casualty area. The current risk factor analysis we are performing gives weight in the general casualty risk factor to how much auto hazard exposure is being included. Departments with greater risk from driving are assigned a risk factor that takes this additional exposure into account.

   Having said this, we will conduct some research into the reasons other entities split out their vehicle risk from the rest of the casualty risk. This will be completed by the end of December, 2016.

Respectfully submitted,

Dwayne Kroening, CRM
Risk Manager

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Risk Management:

Insurance rate calculations and monitoring

March 2016

A Report by the Internal Auditor

Brian Nava
Clackamas County Internal Auditor

Shari Anderson
Clackamas County Treasurer

May 10, 2016

WHAT WILL BE COVERED

- Background
- Objectives, Scope and Methodology
- Audit Results
- Supplementary Information
- Follow-up
- Questions

Background

- Clackamas County has elected to use self-insurance unless they have determined it to be more efficient to purchase commercial insurance
- Day to day management is provided by Risk Manager
- Primary areas managed:
  - Liability (Casualty), which includes vehicles
  - Worker's compensation
  - Unemployment claims administration
  - Loss control services
  - Insurance
- Six employees
- Risk management allocates a portion of the cost needed to fund:
  - Casualty
  - Worker's compensation
  - Unemployment insurance

Objectives, Scope and Methodology

- Evaluate the allocation and claims management processes
  - Overall funding amount
  - Methodology to allocate to departments
  - Claims payment process
- To accomplish this goal:
  - Interviewed staff and management
  - Interviewed staff and management from other self-insured organizations throughout Oregon
  - Reviewed state laws, administrative rules and management best practices
  - Reviewed detailed transaction level data

Audit Results

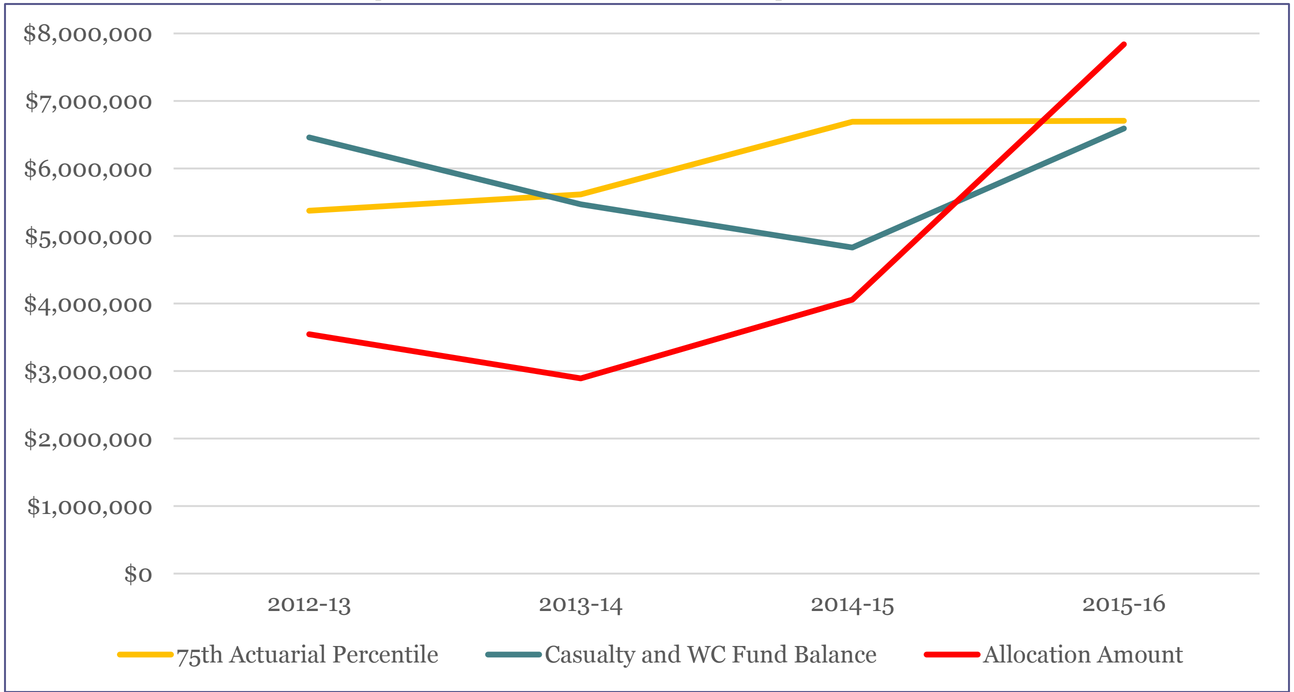
- Clackamas County excels with the Risk Manual

Question	Clackamas County	County 1	County 2	County 3	City 4
Is the cost associated with vehicle liability allocated separately from other insurance (e.g. worker's compensation, casualty, unemployment)?	No	Yes	No	Yes	Yes
Who does risk management report to?	Department of Employee Services	Deputy County Administrator in Support Services (includes Human Resources and Finance)	Chief Financial Officer	County Administrator	Bureau of Internal Business Services
Do you use a third party to assist in claims administration?	Yes	Yes	Yes	No	No
Do you have formalized and up to date policies and procedures for risk management?	Yes (Risk Manual)	Yes (Risk Policies)	No (Currently in draft form)	No	No (Current policies are out of date)
What is your ALAE funding level percentage?	75% Goal	70 - 90%	70 - 75%	75%	75 - 80%
What is your single claim approval level?	Figure 12	Risk Manager: $10,000 DC[3] Administrator: $50,000 BCC: Over $50,000	County Counsel: $10,000 BCC: Over $10,000	Risk Manager: $10,000 BCC: Over $10,000	Risk Manager: $5,000 City Council: Over $5,000
Participating in OPEEP[4] or plan to participate in OPEEP?	Yes	Yes	No	Yes	No

Audit Results

- Self-insurance rates and claims expense have significantly increased in the last few years. The burden of the increases affects the budgets of Clackamas County departments, and as a result, services to the public are less than they could have been.

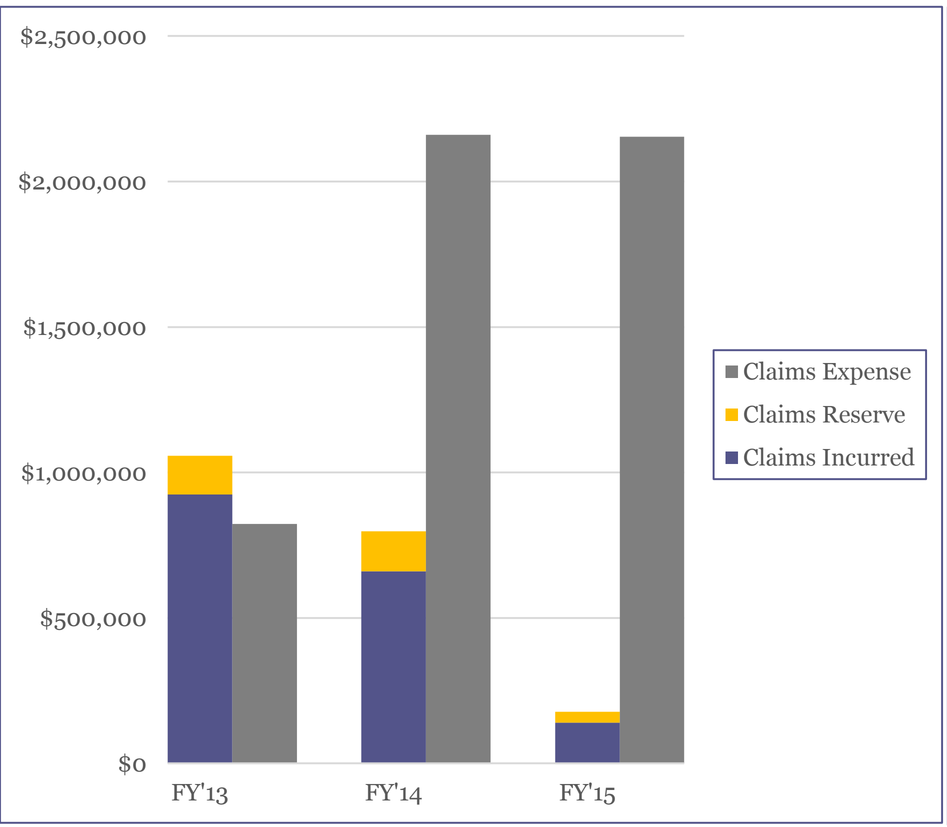
Worker's Compensation and Casualty Insurance Combined

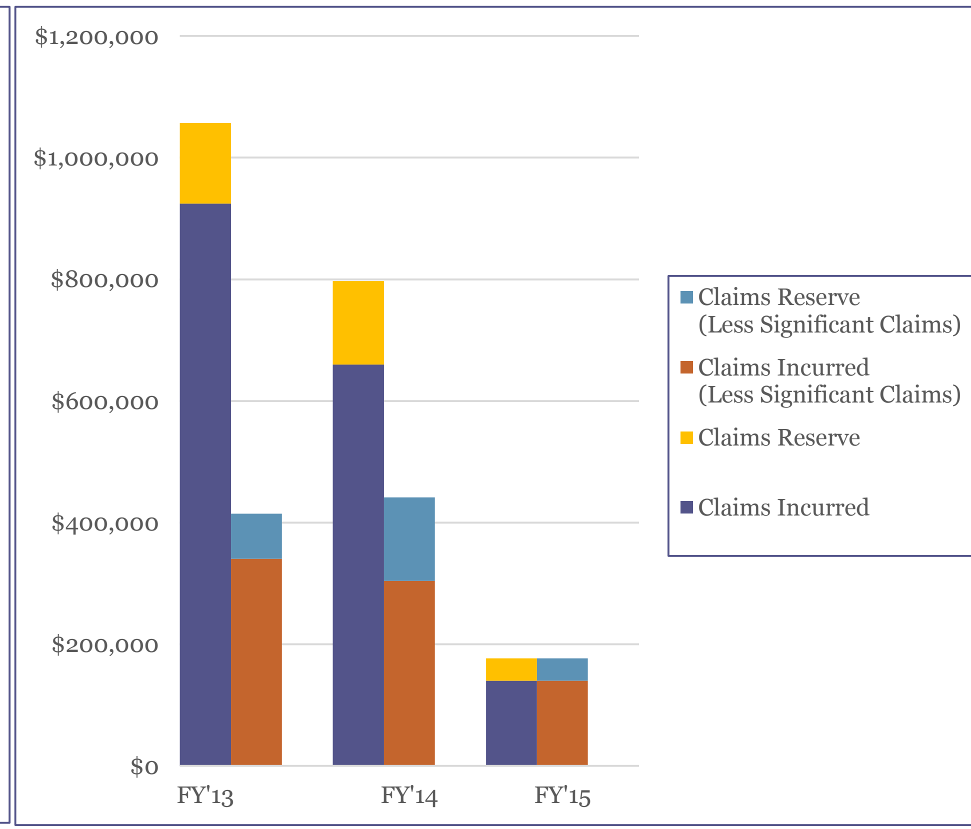


Audit Results

- A few unexpected claims and underfunding has led to the recent significant increases in allocated charges
- "Leveling" could help reduce drastic allocation swings

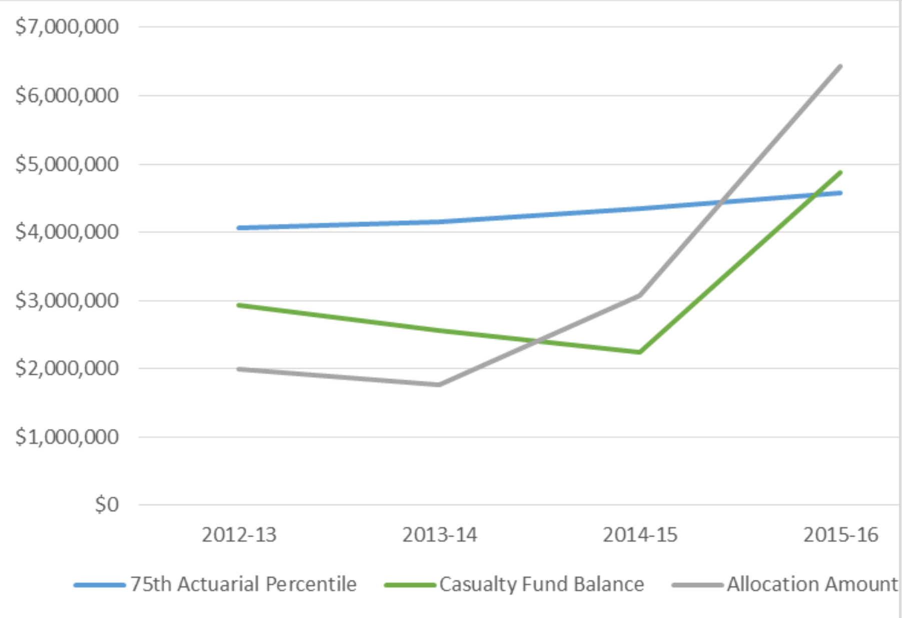
Casualty Claims

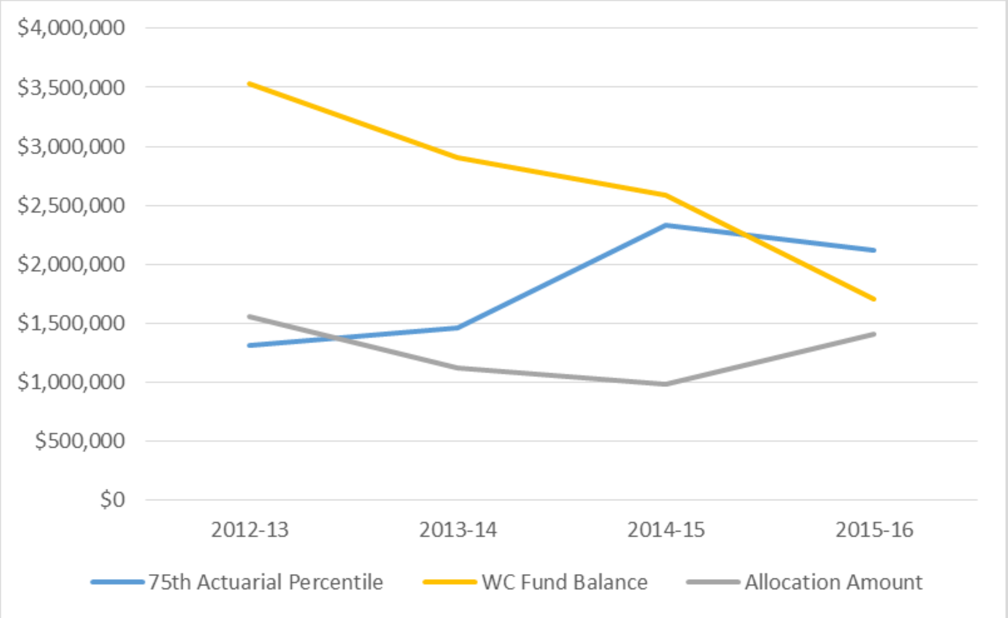




Audit Results

- We recommended management document the methodology to calculate the overall funding amounts and incorporate this methodology into the Risk Manual
- Adequate documentation should then be readily available, especially when deviations from this methodology are determined necessary

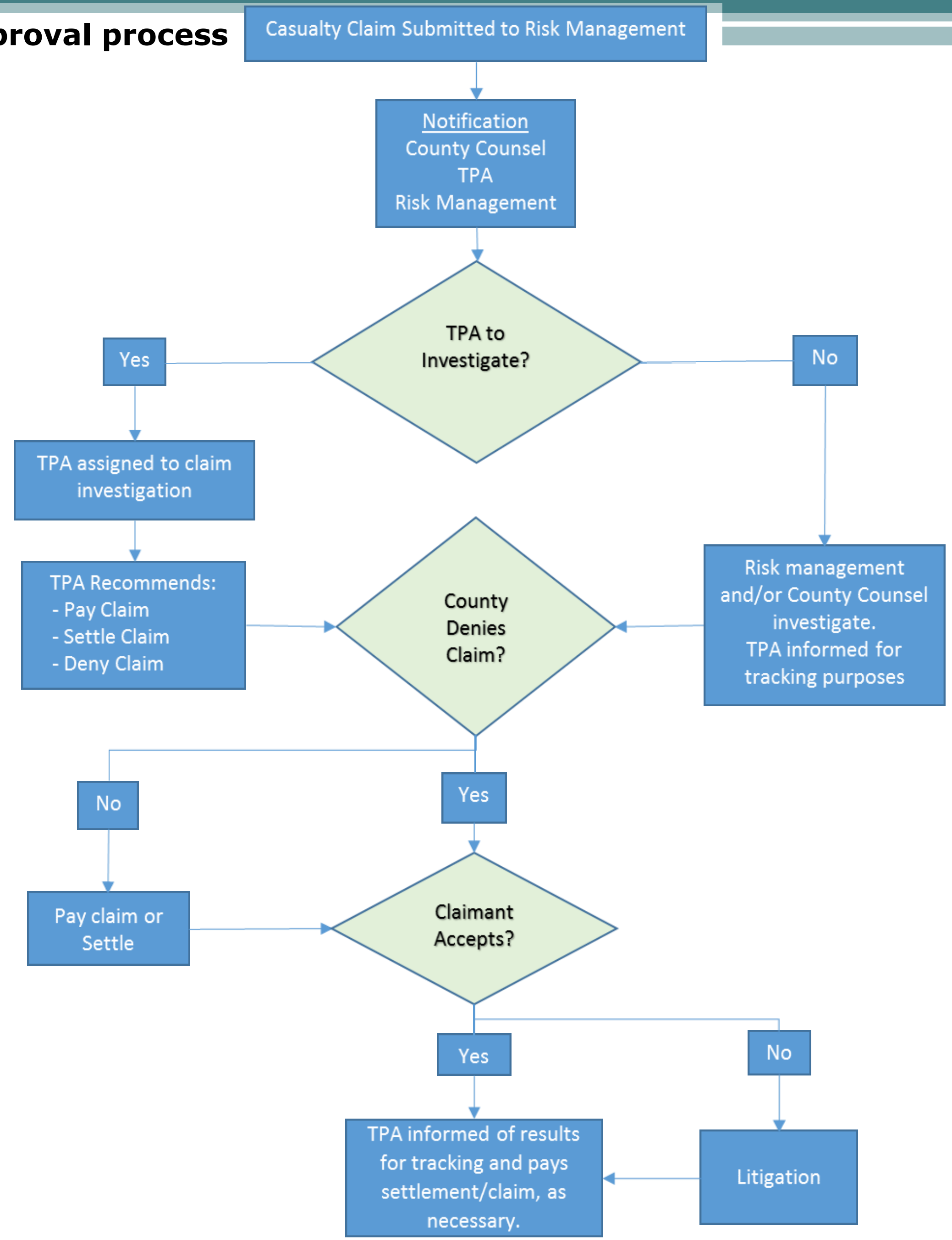




Audit Results

- Clear documented criteria should be developed and maintained related to subjective risk factors
- Risk factors and calculations which determine the insurance amounts for County departments should be regularly formally evaluated
  - The risk factors and allocation calculation have not been formally evaluated since implementation in the late 1990's
- Ensure allocated amount received, matches amount requested

Casualty claim approval process



Audit Results

- Claim approval tracking procedures should be improved to ensure adequate approval documentation is readily available

Casualty claim approval levels

Approval Levels	Who Approves?
$0 to 5,000	Risk Manager
$5,001 to 40,000	Risk Manager and County Counsel
$40,001 to 80,000	Risk Manager and County Counsel with advisement from County Administrator
$80,001 to 100,000	County Administrator approval with Board of County Commissioner (BCC) advisement
Greater than $100,000	Requires formal BCC action

- The County's policy is to defend itself against all nuisance claims. However, if the Risk Manager and County Counsel agree that the cost to defend a disputed claim is greater than the settlement amount, it is within their discretion to settle that claim.

Audit Results

- Oversight of the third party administering (TPA) casualty claims should be improved to ensure the payments are accurate and appropriate
- Current procedures in place are not sufficient to prevent or detect duplicate payments and overpayments
- Management is implementing reconciliation procedures to resolve this issue
- Management indicated the TPA has agreed to have an independent review performed over the TPA's internal controls

Audit Results

- Additional insurance purchased appears adequate

Coverage	Deductible[5]	Limit
Property/Boiler Machinery	$25,000	$200,000,000[6]
Earth Movement	3% of property value[7]	$25,000,000[8]
Flood	$100,000[9]	$15,000,000
CCSO Inland Marine	$15,000	None
Volunteer Liability and Medical	$75[10]	None
Excess Worker's Comp.	$1,000,000	Statutory[11]
Excess Public Entity Liability	$1,000,000	$9,000,000[12]
Flood Plain Coverage	$3,000[13]	$500,000
Garage Liability	None	$1,000,000
Hull/P&I	$7,500 – M.J. Lee Ferry Hull $5,000 – Hull, all other vessels $2,500 – Protection and Indemnity coverage	None None $2,000,000
Marine Pollution Liability	None	$1,000,000
CCSO[14] Owned Aviation Liability	None	$3,000,000
Auto Liability – 15 Passenger Vans	None	$1,000,000

Audit Results

- Vehicle liability appears inequitable
  - Encompassed in casualty insurance allocation
- Consider separating vehicle liability from casualty insurance allocation

Figure 6: Average Casualty Claim Count
Fiscal Year 2013 - 2015

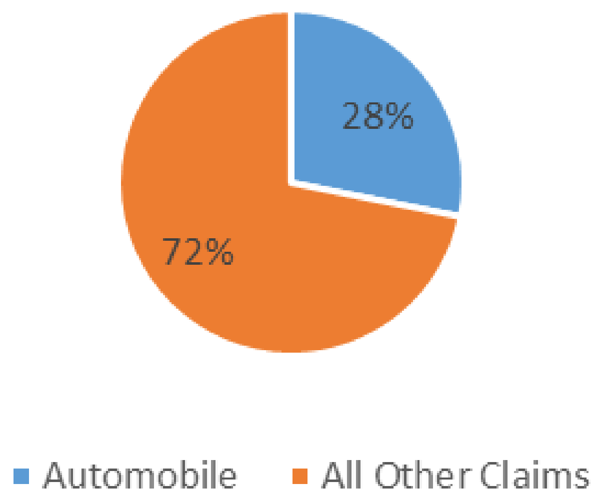
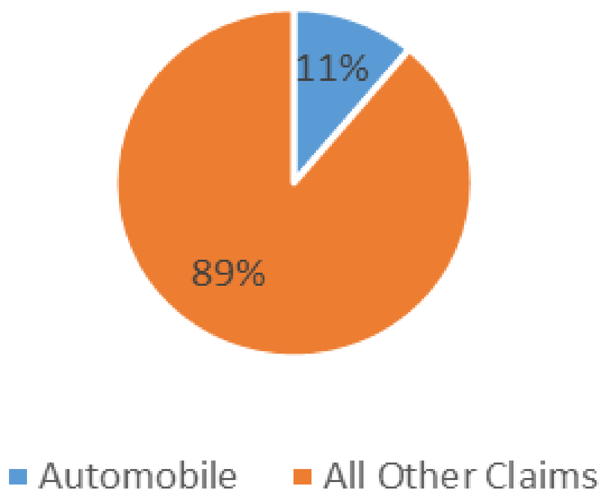


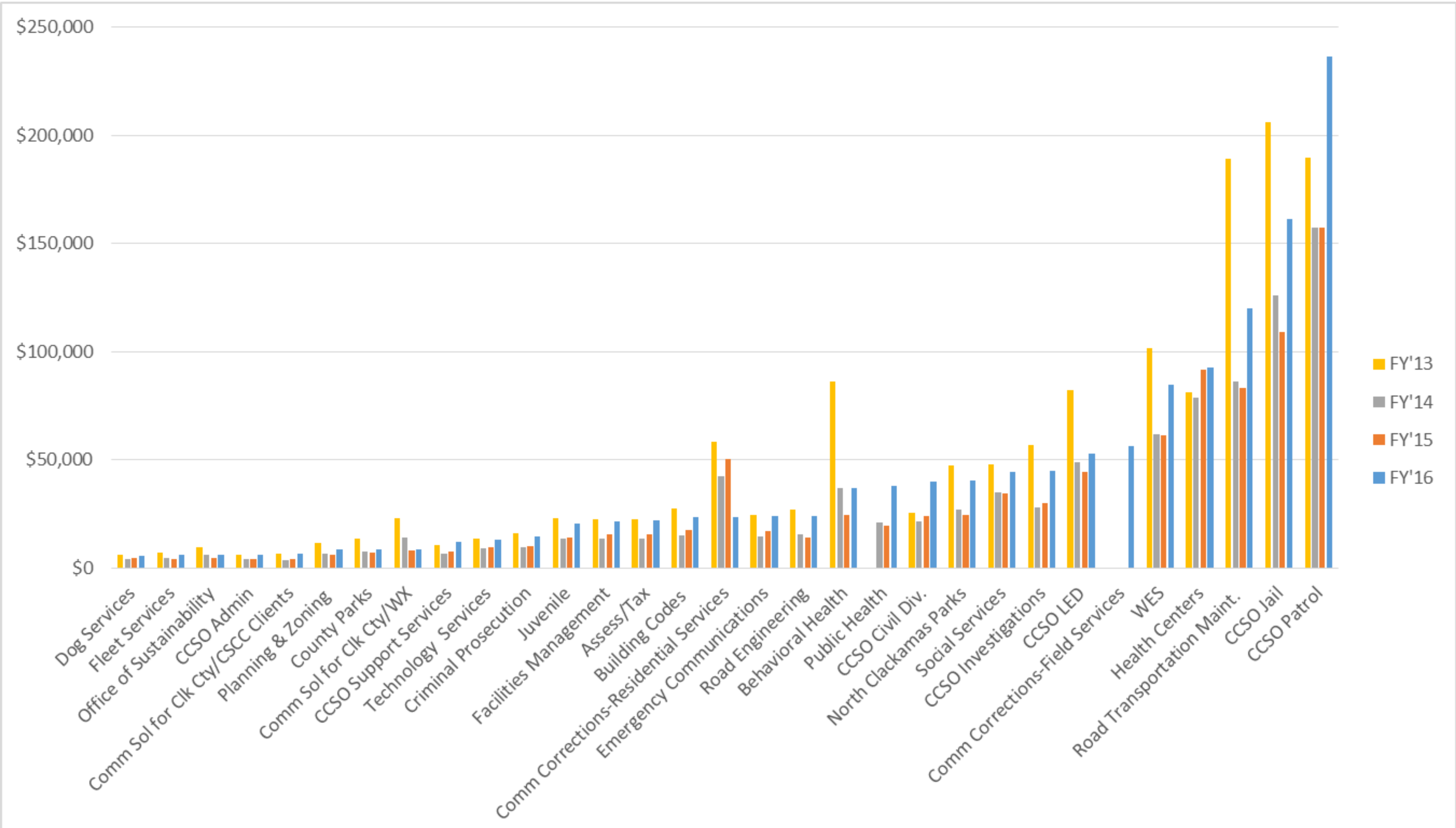
Figure 7: Average Casualty Claim Cost
Fiscal Year 2013 - 2015



Supplementary information

- Allocated cost distribution has not changed

Worker's compensation



Supplementary information

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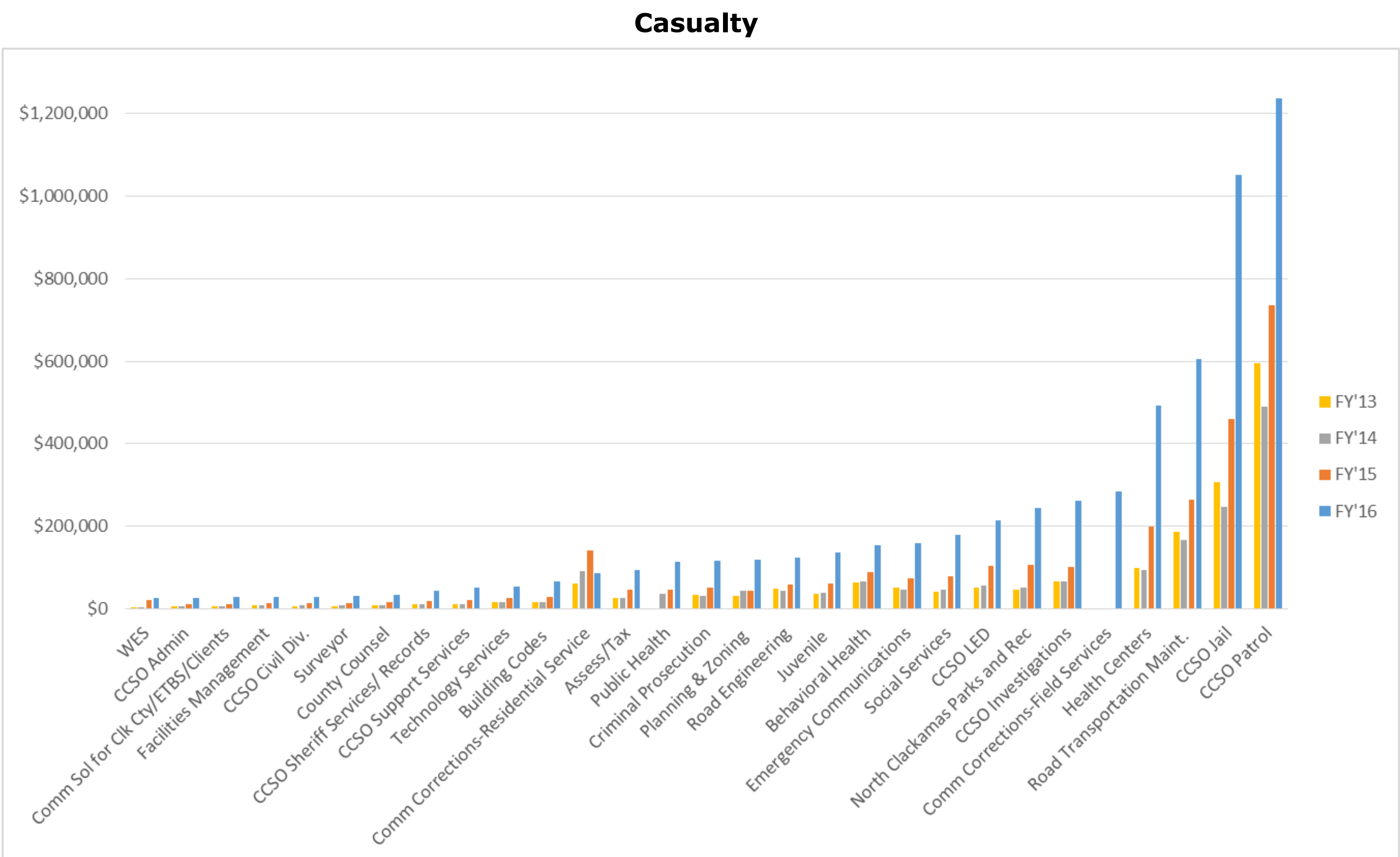

Follow-up

- Management generally agreed with all audit recommendations
- Management is in the process of implementing procedures to address all audit recommendations
- Follow-up by Internal Audit to ensure procedures have been implemented is anticipated to occur in calendar year 2017

Acknowledgements

- Thanks to Evelyn Minor-Lawrence, Dwayne Kroening, Jan Oyama, other risk management employees, other County departments and other self-insured organizations for their assistance
- The courtesies and cooperation during the course of this audit were commendable and sincerely appreciated


Time for
Questions

Contact Us

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