Response to Sunset Staff Report

State Office of Risk Management

November 26, 2018

SORM
State Office of Risk Management
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November 26, 2018

Jennifer Jones
Acting Director
Sunset Advisory Commission
P.O. Box 13066
Austin, Texas 78711-3066

RE: Sunset Review of the State Office of Risk Management

Dear Ms. Jones:

Thank you for providing the State Office of Risk Management (SORM) the opportunity to respond to the issues and recommendations presented in the Sunset Advisory Commission's Staff Report. SORM is dedicated to transparency and successful implementation of its core missions. We believe that the efforts and initiatives undertaken in the past and planned by SORM will convey each of the core tenets of the agency's motto: *Praeparare, Praesidere, Perstare* – Prepare, Protect, Persevere.

Please find attached SORM's response to the issues and recommendations. Our executive staff has reviewed, evaluated, and discussed each of the proposed recommendations, as well as the effects of each recommendation upon SORM's mission to provide active leadership to enable State of Texas entities to protect their employees, the general public, and the state's physical and financial assets by reducing and controlling risk in the most efficient and cost-effective manner.

I look forward to continuing the relationship as we move through the remaining stages of the Sunset evaluation process, including the implementation of any recommendation or statutory changes.

Respectfully,

Stephen S. Vollbrecht,
JD, MA, AINS, AIS, MCP, MEMS
State Risk Manager, Executive Director

I. Statutory Mission Successes

SORM was initially created to address rising workers' compensation costs and workplace health and safety for State of Texas employees. Having reduced and stabilized these costs with the efforts of all participating agencies, SORM's missions have been subsequently expanded to provide further enterprise-level support and service in the risk management, risk transfer, and continuity of operations domains for Texas.

A. Funding Changes

When the State Office of Risk Management was created in 1997, in addition to expenditure authority appropriated by the Legislature, SORM was funded by three mechanisms: through interagency contracts with participating state entities in the risk management program, direct general revenue appropriations, and monies recovered from third parties though subrogation.

In 2001, Article 14 of HB 2600 (77R) required SORM to establish a cost-allocation program for the payment of workers' compensation claims and risk management services. SORM began the "reallocation" process in conjunction with the Comptroller and Legislative Budget Board (LBB) whereby the general revenue appropriated to SORM was appropriated to participating entities as part of each entity's baseline.

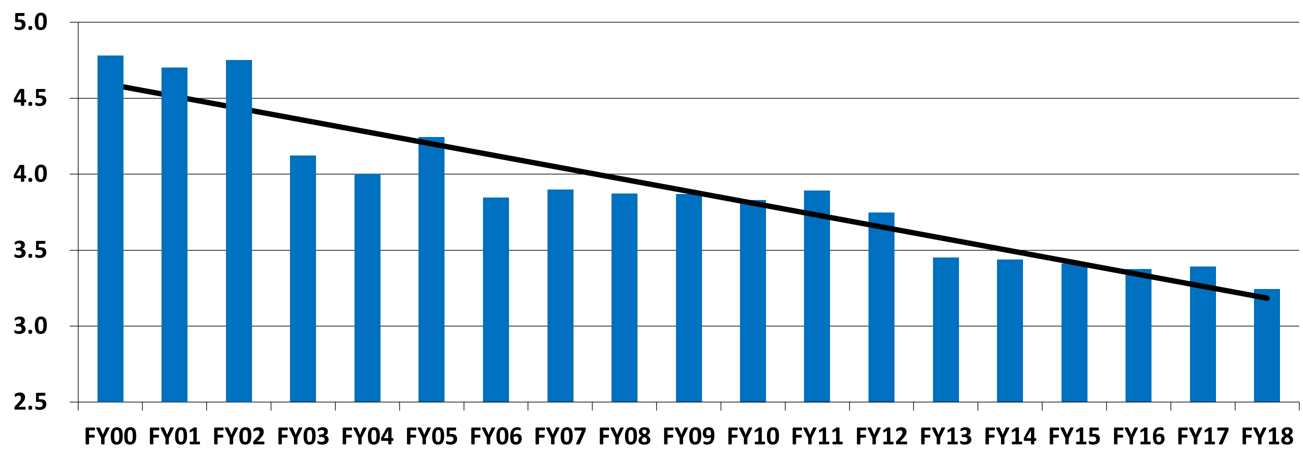
SORM's Fiscal Year (FY) 2004 risk assessment allocation for workers' compensation claim payments was approximately $78.6 million. Actuarial projections for workers' compensation claims costs were expected to continually increase by several million dollars each year upon reaching $70 million in FY2003. However, at the end of FY2004, workers' compensation claims costs had decreased to $55.8 million. Ten percent of the $78.6 million allocation total was carried forward to reduce the assessment total for the next fiscal year and approximately $15.6 million was returned to participating entities.

SORM continued to receive direct general revenue appropriations for the administration of workers' compensation until FY2006 when a portion ($2.5 million) of program funding was included in the assessments. Assessment funding continued to replace general revenue until FY2010 when SORM became wholly funded through an annual assessment.

In FY2012, the appropriation to the Office of the Attorney General (OAG) for SORM's administrative attachment, which was previously a direct general revenue appropriation to the OAG, became funded by SORM through its assessments. This was in addition to the funding for employee benefits outside of the agency's appropriation. SORM's current assessment is $22.2 million lower than the FY2004 assessment for claim expenditures and risk management services only.

B. Injury Frequency Rate

One of SORM's key performance measures is the *Incident Rate of Injuries and Illnesses per 100 Covered Full-Time State Employees*. This measure provides an objective measurement of the results of implementation of covered state entities risk management plans and the results of the Office's risk management program, related specifically to occupational injury. The injury frequency rate for the state employees' workers' compensation program administered by SORM has declined. The decline reflects not only the effectiveness of SORM's risk management program with identifying risks to covered state entities, but also reflects covered state entities actions in regards to implementation of recommendations to control and correct the conditions that lead to injured state employees.



C. Risk of Loss Transferred Through Insurance

As the full-service insurance manager for the State, SORM assists state entities with lessening the budgetary impact of loss through the purchase of insurance.

For example, in 2008, Lamar University sustained property damages due to Hurricane Ike. The university's participation in SORM's property insurance program afforded the university access to advance insurance funds to begin its recovery efforts.

In the Spring of 2014, The National Weather Service reported hail of 3½-inch diameters and larger falling along U.S. 380 north of downtown Denton. The University of North Texas (UNT) suffered hail damage to buildings in excess of $12 million. Through participation in the SORM's property insurance program, UNT only incurred a $100,000 out-of-pocket deductible.

When Hurricane Harvey made landfall on August 25, 2017, SORM's property program exposure for Tier 1 categorized counties was $4,244,936,988. The University of Houston and Texas Southern University had the only reported Harvey-related claims. Their extensive loss mitigation efforts after previous hurricanes helped reduce the overall total gross loss to $15,299,600. While these losses are significant, the efforts of these entities in mitigation and response is notable given the types of unmitigated losses experienced in other sectors. Both institutions received advance funds on September 12, 2017, and began their recovery efforts.

Shortly after Hurricane Harvey impacted the University of Houston, the institution experienced water damage to its pharmacy building. The extensive water damage throughout the building caused the university to relocate classrooms. Although the water damage is still being repaired, the estimated cost of this claim is currently $3,488,485 with a $100,000 out-of-pocket deductible.

D. Continuity of Operations Planning Program

In 2018, SORM established the Continuity Council to bring both public and private sector continuity planners within the State together to coordinate best practices in order to build strong, enduring continuity communities. SORM has also developed a national network to share information and provide mutual support with continuity coordinators from other states. SORM encourages continuity planning and coordination with other threat, risk and emergency plans to ensure a concise and consistent direction.

SORM and Texas Department of Emergency Management worked with FEMA to re-develop the non-federal guidance document and planning tools used to create COOP plans, recently approved and disseminated. SORM will implement Texas-specific applications of the FEMA COOP model to improve planning efficiency and effectiveness and reissue the Statewide Continuity Policy letter.

E. Cost of Workers' Compensation for Entities Referenced in Sunset Staff Report

Private insurance companies categorize various types of work into industry class codes to effectively estimate workers' compensation rates for the appropriate risk associated with the type of work being performed.

Workers' Comp class codes are three- or four-digit codes created by the National Council on Compensation Insurance (NCCI), an organization that gathers data and prepares objective Workers' Comp Insurance rates. NCCI created a standard classification system for more than 700 industries. These 700+ codes not only distinguish different job duties performed by employees, they also denote the amount of risk and type of hazard each job or work environment may entail. Each class code assigns a certain "value" based on these conditions.

Industry codes for the five state entities referenced in the *Agency at a Glance* section of the Sunset Staff Report indicate that the work being performed has more risk and is more hazardous, which results in a more expensive workers' compensation rate. Based on the industry codes for the five entities identified in Sunset Staff Report, potential private insurance premiums would exceed the amount indicated in the allocation assessment.

F. Non-State Employees Served by SORM's Workers' Compensation Administration Program

Since SORM was created, it has provided workers' compensation claims administration for non-state employees. When a compensable work injury occurs, SORM ensures that the covered individual receives the same level of service and benefits as a covered state employee. Most of the compensable injuries can be directly linked to natural and/or man-made disasters and events.

II. Responses to Sunset Staff Report Recommendations

A. Issue 1 Recommendations

1.1 *Direct SORM to develop detailed contract management policies and procedures.*

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Staff Report.

1.2 *Direct SORM to include detailed, actionable performance measures in contracts.*

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Review process.

1.3 *Direct SORM to monitor its contracts more regularly and more closely to ensure proper performance.*

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Staff Report.

1.4 *Direct SORM to develop and require regular training for staff involved in the contracting process to effectively monitor contracts.*

SORM agrees with the recommendation and has begun initial implementation.

1.5 *Direct SORM to include detailed enforcement measures in contracts and apply enforcement tools consistently across contractors.*

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Review process.

1.6 ***Direct SORM to maximize opportunities to use OAG's contract and management expertise.***

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Review process.

B. Issue 2 Recommendations

2.1 ***Direct SORM to evaluate and adjust its workers' compensation healthcare network contract to obtain best value for the state, including providing adequate coverage for injured state employees.***

SORM agrees with this recommendation, but notes that workers' compensation health care networks are regulated by the Texas Department of Insurance (TDI). TDI has jurisdiction to determine the adequacy of a network to provide comprehensive health care services sufficient to serve the population of injured employees within the service areas of the network. The network's demonstrated ability to meet the access and availability standards of Texas Insurance Code Chapter 1305, Subchapter G, are evaluated by TDI during the application process.

Pursuant to Texas Insurance Code Section 1305.502, the TDI-Division of Workers' Compensation's Research and Evaluation Group issues an annual informational report card on workers' compensation health care networks. According to the *2018 Network Report Card*, SORM's current network had lower average medical costs than non-network for the first six months of injury. The average medical costs for SORM's current network are lower than non-network in 14 of 19 categories. The report card also indicates that there is no difference between the network's access to care and the satisfaction with care compared to non-network.

During the 2014 medical cost containment procurement, SORM received three responses to the Request for Proposal from workers' compensation networks that were interested in serving as the network for SORM's workers' compensation program. The current network was individually evaluated in the *2018 Network Report Card*; the other two respondents were included in the "other" category because those networks were considered too small in terms of injured employees treating in-network.

2.2 ***Direct SORM to evaluate the agency's medical bill quality assurance strategy and make any needed improvements to maximize cost savings.***

SORM agrees with the recommendation and has evaluated alternatives to the current outsourcing of this function. The following information was recently submitted to the LBB during the Strategic Fiscal Review of SORM:

> SORM's current medical bill review vendor utilizes an automated system to re-price bills, but does not perform detailed, manual reviews to maximize savings. An

operational change that could improve the success and effectiveness of the Contracted Medical Cost Containment Program is to transition from an outsourced vendor for medical bill audits to the performance of in-house medical bill audits performed by SORM's medical quality assurance (MQA) staff.

Placing medical bill review cost containment activities within SORM would give the agency more control over the turnaround times for final action on medical and pharmacy bills reviews and requests for reconsideration. Avoiding interest payments by complying with payment deadlines is a method to help contain costs. Direct responsibility for medical bill review cost containment activities would also eliminate the possibility of an administrative fine being imposed against SORM due to the non-compliance by a third-party vendor.

The majority of the MQA staff are experienced workers' compensation claims adjusters. This specialized experience is crucial since medical bill payment recommendations require a sophisticated understanding of the Texas Workers' Compensation Act, medical treatment guidelines, and medical fee guidelines. However, SORM does not have direct control over the expertise and knowledge of a third-party vendor's staff.

2.3 ***Direct SORM to include additional information in its cost containment reports to better demonstrate the agency's performance.***

SORM agrees with the recommendation, but notes that compliance with the staff recommendations may not be feasible with SORM's current case management system. SORM is willing to pursue available options for obtaining a new case management system.

2.4 ***Direct SORM to provide additional information and resources regarding return-to-work programs.***

SORM agrees with the recommendation and has begun implementation. In addition, SORM has been evaluating the possible alternative of outsourcing this service.

2.5 ***Direct SORM to collect and report lost-time outcomes and return-to-work information currently required by statute.***

SORM agrees with the recommendation, but notes that compliance may not be feasible with SORM's current case management system. SORM is willing to pursue available options for obtaining a new case management system.

C. Issue 3 Recommendations

3.1 ***Require SORM to regularly review and update risk management guidelines for state entities.***

SORM agrees with the recommendation and has begun implementation.

3.2 ***Direct SORM to use existing data to determine state entity risk levels and needs, and to prioritize resources and requirements by risk.***

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Staff Report.

3.3 ***Direct SORM to develop and use a standard assessment tool to focus on key areas of risk during site visits.***

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Review process. SORM subscribes to A.M. Best's Underwriting and Loss Control Center, which offers recognized industry standards to accurately assess risk. The center provides access to an underwriting guide to evaluate risks by business and/or service type and a loss control manual with industry standard checklists. During on-site inspections, SORM uses these tools to tailor the assessment to the individual needs of the entity.

3.4 ***Direct SORM to regularly solicit and use customer input to better tailor risk management services and resources.***

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Review process.

3.5 ***Direct SORM to develop objective tools to help state entities determine whether to transfer risk through purchasing insurance.***

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Review process. SORM is emphasizing the development and adoption of the ISO 31000 enterprise risk management framework and techniques for governance, risk management, compliance, and general agency decision-making based on risk-informed data at an enterprise level in Texas.

3.6 ***Direct SORM to provide state entities with easy-to-use materials and templates for continuity planning.***

SORM agrees with the recommendation and notes that implementation began prior to the Sunset Review process.

D. Issue 4 Recommendations

4.1 *Continue the State Office of Risk Management for 12 years.*

SORM agrees with the recommendation.

4.2 *Update the standard across-the-board requirement related to board member training.*

SORM agrees with the recommendation.

4.3 *Direct SORM to strengthen oversight by updating the Board regularly on identified problems and improvements.*

SORM agrees with the recommendation. The Executive Director presents an update regarding agency operations during each quarterly Board meeting.

SORM also agrees with the recommendation to seek exceptional item funding to enhance efficiency. The following information was recently submitted to the LBB during the Strategic Fiscal Review of SORM:

> Full implementation of a comprehensive, configurable, and cloud-enabled Risk Management Information System (RMIS) would integrate SORM's statutory programs - enterprise risk management, insurance purchasing, workers' compensation claims administration, COOP planning, and current and future operational systems. The ideal RMIS will provide substantial document management functionality and advanced tracking and management reporting capabilities to enable the State of Texas to consolidate, monitor, and analyze data regarding the overall cost of risk for the purposes of risk and response decision-making. The minimal system must allow multiple internal and external users to access and upload information and documentation; contain a high level of system security; contain analysis features; have robust, user-friendly reporting features; include the ability to integrate with other systems; support remote access; and be capable of converting or migrating data from existing legacy systems to facilitate deprecation. The system should be accessible by the Legislature and all state entities and institutions of higher education that receive services from or through SORM.
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> A fully integrated system where relational data is continuously updated can provide real-time information for preparedness, mitigation, response, and recovery. Through data revision, verification, and updating, the data in a RMIS would become more refined, insightful, and contemporary to address statewide issues as they arise. Centralization would ideally support simultaneous availability of information at multiple levels and for different purposes. Uniform, consolidated data could be used by

individual state entities and the state enterprise to conduct analytics, identify risk trends, develop strategies, and inform decision-making and long-term planning. Access to detailed, up-to-date, comprehensive data on losses should increase the ability to proactively address risk.

A consolidated collection of data could be used for predictive catastrophic event and risk modeling. Statewide predictive risk modeling would allow SORM and other entities to perform more detailed risk and insurance analyses and enhance statewide risk and insurance strategies. This data could also support trend tracking and benchmarking of state-owned assets subject to significant risk exposures. The consolidated data could further be used to obtain better competitive market rates for uninsured state-owned buildings and contents. Readily available and accurate underwriting data can expedite risk transfer through insurance. Each entity's costs for retained and transferred risks could be tracked and analyzed.

Workers' compensation claims activities could be streamlined, which would improve adjusters' productivity levels and compliance with regulatory reporting requirements. State entities would have the ability to report injuries 24-hour a day. A RMIS can easily transmit claims activity data to and from external sources; compare claims to drive decision making; and deploy rules-based decision-making tools to automate clerical activities that keep the claims process moving. The claims management module of a RMIS provides adjusters with automated access to forms, rates, rules, and regulations to streamline their adjudication process. Built-in compliance rules evaluate claims activity to automatically fill out the correct document from a library of forms and letters of correspondence. An indemnity benefits rules engine further evaluates claims to calculate average weekly wage (AWW) and indemnity benefits. Furthermore, adjusters would have a search engine that provides access federal and state laws, regulations, and rates.

III. Additional Issues for Consideration

A. Statutory Clarifications to Improve Operations

1.1 State Entity Definition in Texas Labor Code Chapter 501 and Chapter 412

The inconsistency in the definition of state entity in Texas Labor Code Section 501.001[1] and Labor Code Section 412.001[2] has created some confusion regarding which state entities are subject to the requirements to develop a risk management program and submit a COOP plan to SORM. A

[1] Labor Code Section 501.001(6) "State agency" includes a department, board, commission, or institution of this state.

[2] Labor Code Section 412.001(4) "State agency" means 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*.

similar uncertainty exists regarding SORM's obligation to review a state entity's insurance purchase before the purchase occurs. The limitations in Texas Labor Code Section 412.001(4) may serve to unintentionally exacerbate these issues.

1.2 Annual Report by State Entities

Currently, Texas Labor Code Section 412.053(b) requires state entities to report the information required by Section 412.053 "not later that the 60th day before the last day of each fiscal year." State entities do not have complete data prior to the close of the fiscal year, therefore, SORM has modified this process to request that state entities report the data between September 1 and October 30 each year. To ensure SORM receives accurate and timely reports, SORM recommends amending Texas Labor Code Section 412.053(b) to require annual reporting "not later than the 60th day after the last day of each fiscal year."

1.3 Indoor Air Quality Seminar

In December 2002, the Department of State Health Services (DSHS) developed guidelines on indoor air quality pursuant to Health & Safety Code Chapter 385. In 2015, SB 202 (84R) transferred a number of functions from DSHS to other entities. Section 3.030 of the bill repealed Health & Safety Code Chapter 385, thereby removing all references to a state entity voluntarily establishing guidelines for indoor air quality in government buildings. However, Government Code Section 2165.305 still requires SORM to conduct an annual, one-day educational seminar on indoor air quality. Similarly, the indoor air quality rules (guidelines) adopted by DSHS in 25 Texas Administrative Code Chapter 297 have not been repealed.

1.4 State Employee Waiver of Workers' Compensation

The Texas Tort Claims Act (TTCA) creates a specific waiver of immunity for state employee workers' compensation claims. Workers compensation for state employees was created through Labor Code Chapter 501. Texas Labor Code Section 501.002(d) is clear neither Chapter 501 nor the general workers' compensation provisions authorize a cause of action or damages against the state, a state entity, or an employee of the state beyond the actions and damages authorized by the TTCA. Texas Labor Code Section 406.034 states that an employee can agree, in writing to waive workers' compensation during the first few days of employment. SORM interprets this provision as being inconsistent with Texas Labor Code Chapter 501. It is prudent to clarify that state employees cannot waive workers' compensation coverage.

B. Opportunities for Advancement

The following information was recently submitted to the LBB during the Strategic Fiscal Review of SORM:

> In SORM's Biennial Report to the 81st Legislature, the agency brought attention to the common assumption that the State self-insures its real and personal property. The State does retain the risk of a loss; however, a significant portion of the State's real and personal property is, in practice, uninsured. SORM's Biennial Reports to the 84th and 85th Legislature, the Office recommended the adoption of an enterprise-level retention commensurate with the size and scope of enterprise operations and the reliance upon (re)insurance for catastrophic events only.
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> A self-insured retention limit could lead to a significant reduction in premiums. The State would assume an amount of the primary risk and transfer the remaining risk to an excess coverage policy for larger, catastrophic losses, which is consistent with other state jurisdictions. In addition, a mandatory program will expand the population served and increase demand for insurance services.