



State of Louisiana

**OFFICE OF
STATE INSPECTOR GENERAL**

OFFICE OF RISK MANAGEMENT

OPERATIONAL REVIEW

Report by

Inspector General Bill Lynch

Prepared for

Governor M. J. "Mike" Foster, Jr.

File No. 2-02-0002



State of Louisiana
DIVISION OF ADMINISTRATION

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M. J. "MIKE" FOSTER, JR.
GOVERNOR

BILL LYNCH
INSPECTOR GENERAL

MEMORANDUM

TO: Governor M.J. "Mike" Foster, Jr.

FROM: Bill Lynch *BL*
State Inspector General

DATE: Nov. 15, 2002

The enclosed report is an operational review of the Office of Risk Management which was requested by the Commissioner of Administration.

We recommend that the internal audit report be forwarded to the Commissioner for disposition after you have signed off on it. This review should satisfy the Legislative Auditor's concerns over the lack of internal auditing for ORM

BL/GL/rp
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Office of Risk Management Operational Review

Inadequate training, a lack of job knowledge, and an unwillingness on the part of employees, both at the lower and supervisory levels, to instill accountability in the conduct of their jobs, have contributed to serious problems in the internal control structure of the Office of Risk Management. The administration of Risk Management was responsible for this environment. For example, the office has lost or wasted more than \$300,000 during the past three years by failing to properly monitor its contracts.

For the last several years, the state budget policy has forced Risk Management to operate on a less than cash needs basis. This policy precludes an accumulation of assets for payment of estimated claims liability. The state budget policy has been a major contributor to an unfunded liability of approximately \$974 million as of June 30, 2002.

Julian S. Thompson was named the new director of Risk Management on May 14, 2002, succeeding Seth E. Keener, Jr., who served as director from Feb. 19, 1990, to Feb. 15, 2002. The review covered management practices prior to Mr. Thompson's appointment.

During the review, problems were brought to the attention of Mr. Thompson who immediately began corrective action.

Background

ACT 520 of 1980 created the Office of Risk Management within the Division of Administration and became effective on July 1, 1980. Subsequent laws expanded on Act 520 and provided for a comprehensive risk management program for the state. The agency provides workers' compensation coverage to all state employees, coverage for state property, employee bonds, crime, automobile liability and physical damage, comprehensive general liability, personal injury liability, boiler and machinery, medical malpractice, road hazards, and miscellaneous tort claims.

At the request of the Division of Administration, this office began an operational review of the Office of Risk Management on March 12, 2002. The scope of the review was limited to the following:

- Payment/disbursement function.
- Reserve valuations for all lines of insurance.
- Insurance premium.
- Contract administration.
- Corrective action for previous audit findings reported by the Legislative Auditor.

In accordance with office practice, matters involving litigation are not included in this operational review of the Office of Risk Management.

Summary of Findings

The following is a summary of findings revealed during the audit:

- I. **Payment/Disbursement Function - Risk Management's procedures for reviewing and approving invoices are not adequate to prevent improper payments of contract billings and to insure payments are made in accordance with state law and internal policies. Its employees' lack of training, knowledge of contracts, and clear delegation of responsibility has resulted in more than \$300,000 of improper payments.**
 1. More than \$280,000 of improper overcharges submitted by a contractor was approved and paid.
 2. More than \$36,000 was approved and paid to two contractors for services which were not under contract.
 3. The cost for attorney services from the Attorney General's office is not being allocated to all claims incurring the cost. As a result, premium calculations are inaccurate and full subrogation recovery is questionable.
 4. Invoices for elevator and escalator inspections are being paid without anyone at Risk Management reviewing the accuracy of the billed amount.

5. Payments are not being made timely, exposing the state to significant penalties.

II. Reserve Valuations - The reliability of claims reserve is questionable due to a lack of documentation and related data. Additionally, the absence of assets reserved for future payments of claims resulted in an unfunded liability to Risk Management which is approximately \$974 million as of June 30, 2002. This figure has not been audited.

1. Lack of adequate internal guidelines, supervisory attention, and pertinent information has rendered the amount of the current claims reserve as questionable.
2. Risk Management's unfunded liability for claims reserve is approximately \$974 million as of June 30, 2002.
3. The level of funding for premiums has caused Risk Management to use prior year residual cash to pay for current claims and operational expenses, reducing its cash balance to approximately \$27.7 million as of June 30, 2002.

III. Insurance Premium - Risk Management's ability to collect the amount required for its claims and operational expenses was limited.

1. Risk Management was appropriated \$25 million less than its estimated expenditures for fiscal year 2003. As a result, it was required to deplete its prior year residual cash to avoid an operating deficit.
2. If payments are made from the Future Medical Care Fund in fiscal year 2003, Risk Management does not have the available cash to replenish the fund as required by law.
3. Risk Management has applied its safety audit criteria in a subjective manner resulting in an unequal treatment of the Department of Labor.

IV. Contract Administration - Risk Management has failed to insure its contract procurement, management, and monitoring procedures are adequate to protect the state's interest and has exposed the state to the loss or waste of hundreds of thousands of dollars.

1. The agency failed to establish a contract monitoring program which controls and protects the interest of the state. Contractors drive the

activities associated with their contracts while Risk Management's monitor generally signs off on whatever is invoiced by the contractor.

2. Procedures for contract invoice review and approval fail to insure contractors are only paid according to their contract.
3. Procedures do not insure that the agency will meet all state contract requirements.
4. Contract review procedures are inadequate to insure contracts are free of errors and adhere to state law, agency policy, management's intentions, the request for proposal and the selected proposal
5. The procedure manual for contracts is outdated.
6. The agency failed to comply with all statutory requirements for contracts.
7. Contract files did not always contain the required documentation.

V. Previous Audit Findings - Risk Management's attempt to correct previous Legislative Auditor's audit findings has failed.

1. The focus of Risk Management in its response to previous audit findings was on a lack of employees with no thought given to other alternatives.

I. Payment/Disbursement Function

Risk Management's procedures for reviewing and approving invoices are not adequate to prevent improper payments of contract billings and to insure payments are made in accordance with state law and internal policies. Its employees' lack of training, knowledge of contracts, and clear delegation of responsibility has resulted in more than \$300,000 of improper payments. The process for reviewing and approving invoices for payment consists of no more than checking the math calculation rather than the substance of the contract terms. As a result, invoices have been improperly reviewed and approved for payment. The primary problems are:

1. Employees are reviewing and approving contract invoices without copies of the contract or knowledge of the terms of the contract, resulting in the overpayment of more than \$280,000 for one contract.
2. Contractors are allowed to perform services outside the scope of their contracts resulting in payment for services not under contract.
3. Attorney expenses associated with risk litigation are not allocated to all claims incurring the expenses.
4. Invoices are paid without a certification of amounts as accurate, or being in accordance with contract terms.
5. Failure to pay invoices timely has exposed the state to monetary penalties.

1. Contract Knowledge

Risk Management employees approved and paid more than \$280,000 of overcharges submitted by one contractor, CorVel Corporation which has an office in Metairie, La.

The handling of the CorVel contract by Risk Management is a component of several findings discussed throughout this report.

Employees required to review and approve invoices were not provided a copy of the contract and were not familiar with the compensation terms of the contract.

The two employees, Workers' Compensation Supervisors Page Feller and Debra Fitch, were assigned by Workers' Compensation Claims Manager Karen Jackson to review and approve payments for the CorVel contract. They stated they were not shown the contract or the fee-billing schedule associated with the contract. Both Ms. Feller and Ms. Fitch stated their review only consisted of checking the addition on the front page summary sheet of the invoice.

Ms. Fitch further stated Ms. Jackson did not provide her any guidance on contract monitoring duties. Risk Management designated the contract monitoring and liaison function to Ms. Jackson.

Ms. Jackson acknowledged she did not provide a copy of the contract to Ms. Feller and Ms. Fitch.

The CorVel contract requires the contractor to review invoices in accord with the workers' compensation medical fee schedule, to check for duplicate billings, inappropriate coding, and inappropriate charges. The fee schedule of this contract calls

for the contractor to bill 85 cents per line reviewed in the first year of the contract, 87 cents the second year, 90 cents the last year, and a \$6 flat fee for each Preferred Provider Organizations (PPO) invoice reviewed.

Our examination of the Aug. 1, 1999, through Jan. 31, 2002, contract payments revealed:

1. CorVel has charged and Risk Management has paid a fee of \$76 an hour for professional medical review services even though this fee is not in the contract. This has resulted in an overpayment of approximately \$280,000 over 2 ½ years.

Our examination of the contract and CorVel's contract proposal indicates professional medical review is part of the services to be provided by the contractor under the compensation terms listed in the payment schedule of the contract. Additionally, not only do we believe the services and compensation were already covered by the contract, the contract was very specific with the clause which states,

“The parties further agree that no other sums will be due or payable under the provisions of this contract...” of which the \$76 per hour fee was not included.

2. Line charges and PPO flat fees were intermingled in the summary and detailed billings making it impossible to audit the CorVel billings without the source documents. Even with the source documents, assumptions would have to be made concerning the lines and PPO charges reviewed.

According to CorVel representative, District Manager Deborah Tillman, there was a verbal agreement to pay the \$76 fee. Ms. Tillman stated when she first started working with the contract she became concerned about CorVel charging the \$76 fee without it being in the contract. Therefore, she contacted Ms. Jackson whom she claims said it was allowed.

Ms. Jackson said she does not remember discussing the \$76 fee with Ms. Tillman. However, Ms. Jackson stated that she thought it was industry norm to pay for such a fee.

Written documentation was not provided to support discussion of such an agreement, and most importantly there is no amendment to the contract for the \$76 fee.

The contract provides:

“No amendment to the contract to be issued in response to this Request For Proposal shall be effective unless in writing and signed by duly authorized

representatives of both parties and approved by the director of Contractual Review, Division of Administration.

“Expenditures under this contract determined by audit or the Office of Risk Management review to be ineligible for reimbursement and for which payment has been made to the Contractor, shall be refunded to the Office of Risk Management by the Contractor.”

Conclusions:

1. Risk Management paid more than \$280,000 in overcharges to CorVel Corporation for services included in the base contract.
2. Invoices submitted by CorVel commingled line and Preferred Provider Organizations charges, making it impossible to properly review any invoice without source documents.
3. The contract was not adequately monitored by the designated monitor, Ms. Jackson. The lack of adequate monitoring allowed the contractor to overcharge the state.
4. Ms. Jackson failed to provide either guidance or a copy of the contract to subordinate employees assigned to review and approve contract invoices.
5. Review and approval of contract invoices consisted of math verification only.

Recommendations:

1. Risk Management should recover the more than \$280,000 improperly charged.
2. Future invoices submitted by CorVel should have charges separated not only by claims number but also by each service being charged (i.e. line, PPO, etc.).
3. Employees assigned the responsibility of contract monitor should be trained for this duty, provided all pertinent information required for review and approval of invoices, and held accountable for monitoring the contract according to its written terms.

2. Invoice Approval Without Contract

Risk Management has used existing contracts as a means to pay for services which are not under contract. This has resulted in two contractors receiving over \$36,000 for services without a contract. The contractors were FARA Healthcare Management, a division of F.A. Richard and Associates, Inc. of Mandeville and Crawford & Co. of Dallas, Texas.

Additionally, Risk Management has authorized CorVel to provide services since Feb. 1, 2002, without a written contract. Because CorVel does not have a current contract, payments approved by Risk Management cannot be made through the state's contract payment system.

Risk Management has violated state rules promulgated by the Office of Contractual Review in the Louisiana Administrative Code, Title 34, Part V which requires written contracts.

For the FARA and Crawford contracts, Ms. Jackson was designated to the contract monitoring and liaison function. Since a new contract with CorVel has not been approved, no one has been designated to this function.

FARA

The Aug. 1, 1999, through July 31, 2002, contract with FARA was used to pay at least \$22,958 of charges for services not attributable to the contract.

FARA has a contract with Risk Management to provide utilization review services to ensure appropriate payment for health care services rendered to state employees eligible for workers' compensation benefits. Utilization review, as described in the contract, included coordinating and pre-certifying hospital admissions, re-certifying continued hospital stays, and providing second surgical opinions.

The contract with FARA has a fee schedule which provides:

- \$98 flat rate for each pre-certification and re-certification,
- \$114 flat rate for a second surgical opinion, and
- \$79 per hour plus allocated expenses to conduct audits of medical providers invoices and, if warranted, on-site audits.

According to Ms. Jackson, FARA was not assigned audits under this contract.

However, in addition to legitimate contract charges, FARA invoiced services and fees not related to the contract. These charges included:

- \$68 per hour for medical case management and vocational rehabilitation.
- \$150 per hour for miscellaneous physician billings review.
- \$74 and \$78 per hour for utilization peer review.
- \$74 and \$78 per hour for utilization review of letters and reports.
- \$78 per hour for preparation of correspondence to Risk Management adjusters.
- \$14.80 to \$46.80 per unit for miscellaneous office charges with no details of the charges.

According to Kirk Linderman, FARA client service manager, \$78 an hour is the standard FARA fee for utilization review services. He said FARA might have erroneously invoiced Risk Management its standard fee rather than the flat fees provided in the contract.

Crawford

Crawford invoiced and Risk Management approved and paid at least \$13,722 for services not under contract. The Office of Inspector General previously reported this finding last April 17, 2002. It is used here to further illustrate Risk Management's lack of reconciling contract invoices to contract terms. The contract provided for Crawford to audit the performance of Risk Management's staff in regards to its ability to handle subrogation claims and to issue a report with recommendations at the completion of the audit.

The contract provided for a \$50 per hour fee for auditing services. The total contract was for \$57,500 of which Crawford was paid \$50,648. Of the amount paid, at least \$13,722 was for subrogation recovery and not for auditing as per the terms of the contract.

CorVel

Risk Management authorized CorVel to provide services and approved the related invoices without a contract.

CorVel was awarded a new contract in February, 2002, but it had not been approved by the Office of Contractual Review as of July 1, 2002. Risk Management has requested retroactive approval.

State law provides a contract must be approved in writing by Contractual Review before it is valid and the state bound by the contract.

Beginning Feb. 1, 2002, Risk Management has approved invoices for services provided by CorVel without a written contract.

The proposed contract provides a rate of 81 cents per line reviewed, a \$6 flat fee per PPO reviewed, and \$68 per hour for an expert professional medical review fee. Our examination shows that even if the proposed contract had been approved, CorVel is billing the state \$76 per hour for expert professional medical services instead of the proposed fee of \$68 per hour. Based on the proposed contract, for the months of February, March, and April 2002, CorVel has over billed Risk Management \$2,641. As of July 1, 2002, the invoices had not been paid.

Conclusion:

1. Contractors were allowed to perform services without a contract. They were paid for these services by directing them through existing contracts.

Recommendations:

1. Risk Management should assess its needs for the services being performed without a contract. If the services are required, then Risk Management should follow the state's requirements for procuring a contract, in particular, a written contract.
2. Management should periodically and randomly monitor payments being made through contracts. Employees who cause payments to be made through existing contracts for services not related to the contract should be held accountable for their actions.

3. Unallocated Expenses

The method used for allocating attorney expenses associated with the Attorney General's Office to claims is flawed resulting in the misapplication of those costs used for premium development and subrogation recoveries from liable third parties.

Risk Management has an interagency agreement with the Attorney General's Division of Risk Litigation to provide legal representation for tort claims. In consideration, Risk Management agrees to pay Risk Litigation up to the contracted amount, which was \$10.7 million in fiscal year 2001 and \$11.07 million in fiscal year 2002. The amount paid by Risk Management is what is needed to finance the operations of the Division of Risk Litigation.

The contract has a fee schedule of \$75 to \$115 per hour, depending on the attorney's years of experience. This contract fee has no correlation to Risk Management's actual cost and is only used as a method of allocating the attorneys' expenses to the claims. In fact, the contract itself is a means for Risk Management to allocate Risk Litigation attorney costs to case files.

Risk Litigation is required to submit quarterly reports which identifies the attorney performing services, the claim file, and the hours worked. Accounts Receivable Supervisor Andre Metoyer applies the fee schedule from the contract and computes the charges for allocation to the claims. Using contract rates will cause the last quarter billing to exceed the contracted amount.

Risk Management will arrange the charges from the last quarter charges in descending order to ensure the larger costs are allocated but any remaining cost will not be entered into the detail of the system.

Under the present system, Risk Litigation charges have substantially more hours than are being allocated to claims. For fiscal year 2001, more than 10,000 hours equivalent to approximately 10% of total hours have not been allocated. This has resulted in the misallocation of Risk Litigation expenses to those claims receiving charges.

Additionally, hours equivalent to \$179,252 were not allocated because Risk Litigation provided the wrong file numbers, not because the billing was invalid. Risk Management did not attempt to correct the mistake.

Conclusions:

1. More than 10,000 hours for Risk Litigation attorney fees were not allocated to the claims incurring these expenses during fiscal year 2001.
2. Results similar to fiscal year 2001 will continue as long as Risk Management allocates Risk Litigation attorney costs using the contract fee schedule instead of a reasonable cost allocation plan.

Recommendation:

1. Risk Management should develop a cost allocation plan for distributing Risk Litigation attorney costs to all claims incurring these expenses.

4. Lack of Certification

Loss Prevention Manager Doris Copeland approved elevator and escalator inspection invoices for payment without knowledge of the accuracy of the amount invoiced.

The contract between Risk Management and Elevator Technical Services, Inc. requires the contractor to inspect the various types of elevators and escalators in state buildings. The fee charged by the contractor varies according to the type of equipment inspected or services provided and ranges from \$80 per hour to a \$325 flat fee during the first year of the contract.

Records indicate that Jack Oliver of Risk Management and Chuck Johnson of State Buildings and Grounds were designated as monitors for the contract. Mr. Oliver and his supervisor, Ms. Copeland, stated they were not aware of who was designated as monitor of the contract for Risk Management.

Ms. Copeland stated she approves invoices for payment which have an inspection report but does not verify the accuracy of the amount invoiced. She further stated that she thought Risk Management's accounting department checked the fees invoiced. Accounts Payable Supervisor Heidi Orr said accounting does not verify the fee charged because Mr. Johnson of State Buildings does.

Mr. Johnson confirms his staff checks the fees charged to ensure they are in accordance with the contract. He then sends a transmittal letter, with invoices, to Risk Management attesting to completion of inspections and requesting invoices be processed.

Neither Mr. Johnson's letter nor Risk Management's approval attest to the accuracy of the fees billed or the total billed. Since this is a contract of Risk Management, it is responsible for assuring the accuracy of invoices.

Conclusions:

1. Invoices are being paid without anyone at Risk Management reviewing the accuracy of the fees billed.
2. Risk Management failed to notify one of its employees that he had been designated as the contract monitor.

Recommendation:

1. Risk Management should develop definitive procedures which specifically identifies employees responsible for the accuracy of fees invoiced to the agency.

5. Untimely Payments

More than 50% of 70 payment files reviewed failed to meet either state law, internal policy, or contract requirements.

Our review showed 8 out of 21 or 38% of workers' compensation medical payments were made after the 60-day requirement provided by law, exposing the state to approximately \$7,900 in penalties.

Of the eight, two were 1-10 days late, two between 11-15 days late, two between 25-30 days late, and two were more than 90 days late.

LRS 23:1201.E. states medical benefits payable under the workers' compensation law shall be paid within 60 days after the employer or insurer receives written notice thereof. LRS 23:1201.F. further provides for a penalty equal to 12% of any unpaid medical benefits or \$50 per calendar day, whichever is greater. However, the \$50 per calendar day penalty shall not exceed \$2,000 in the aggregate for any one claim.

In addition, we reviewed 49 payments other than workers' compensation which did not bear a penalty. Other problems of the 70 payment files include:

- 26 payments were beyond the 30-day policy of Risk Management.
- 7 payment files were at CorVel beyond the 5-day turnaround contracted period.
- There was more than a week delay for processing 31 invoices for payment which had already received all required approvals. This has exposed these invoices to intentional and non-intentional misuse or loss.

Several activities can be attributed to slowing down the payment process causing a delay of payments. Some are:

1. Dual accounting and reporting systems are maintained which have overlapping functions. Both, Integrated Statewide Information Systems, the state's system, and Corporate Systems, a contracted internal system are used. Accounting expends a lot of effort to manually integrate information from the two systems.
2. There can be as many as seven approvals required before an invoice is paid.
3. There can be as many as six data entry verifications before a check is mailed.
4. Some employees consider invoice approval as secondary to other job functions. Some of the sampled requests for payments were at Risk Management for at least a week before being reviewed by the adjuster.

Conclusions:

1. Procedures employed by Risk Management are not adequate to insure payments are made in accordance with state law time requirements, exposing the state to monetary penalties.
2. Procedures employed by Risk Management are not adequate to insure payments are made within the time requirements of its own policy.

Recommendations:

1. Risk Management should develop policy and procedures which will insure that workers' compensation medical payments are paid within the time allotted by law.

2. Risk Management should develop guidelines which will meet internal policy of paying all invoices within 30 days.

II. Reserve Valuations

The reliability of claims reserve is questionable due to a lack of documentation and related data. Additionally, the absence of assets reserved for future payments of claims has resulted in an unfunded liability to Risk Management which is approximately \$974 million as of June 30, 2002.

The state operates a self insurance program and our review was limited to claims reserve and Risk Management assets available for future claim payments. Generally, claim obligations may extend over several years. Therefore, a claim reserve is an estimated future obligation. When insurance premiums are developed with consideration given to estimated future liabilities, the amount collected for premiums is more than operational expenses and claims paid for the premium year. Therefore, these excess premiums could be set aside to ensure assets are available to continue paying existing claims.

The primary points of interest are:

1. Documenting and setting the value for claims reserve has not been a high priority activity for Risk Management.
2. Risk Management's unfunded liability for claims reserve, utilizing information available, is approximately \$974 million as of June 30, 2002.
3. The maintaining of an asset reserve, if any, and the amount is dependent upon management philosophy.

1. Claims Reserve

Claims reserve are questionable due to inadequate internal guidelines, lack of supervisory attention, and the absence of pertinent information. As a result, we cannot render an opinion on the reliability of the reserve amount recorded by Risk Management to estimate the liability associated with each claim.

Claims adjusters and examiners use a combination of their experience, attorney recommendations, outside adjusters' investigations, and other reference material to establish a claims reserve.

When a case is opened, the claims adjuster or claims examiner sets a reserve with information available. The reserve should reflect the total expenditures expected for the claim. In order for claims handlers to properly set reserves, the employee must have the ability and resources to analyze the facts of a claim and effectively predict the life and estimated cost of the claim. Problems associated with the establishment of claims reserve are:

- The inability of Risk Management adjusters to perform field work has limited them to relying on second hand information from attorneys and outside adjusters.
- Some employees are not putting adequate evaluation into the establishment of claims reserve.
- According to supervisors, they do not have the time to adequately review subordinates case files because they have active case files of their own.
- Risk Management has not established a data base to assist its employees in formulating claims reserve.
- Written procedures do not provide guidelines for the establishment of claims reserve.

In the majority of the cases, information should be developed within a year. However, there are situations, especially when litigation is involved, where it may take more than a year to develop sufficient information.

Of 56 closed files reviewed, after their one year in existence, only 10 or 18% had reserves which were within 15% of the final cost of the case. The other files had reserves which were more than 15% above the final cost (24 or 43%) and reserves that were less than 15% of the final cost (22 or 39%). We used the 15% for demonstrative purposes only because there is no established standard.

Additionally, the procedures manual requires worksheets for the evaluation of a claim when establishing the initial reserve and documentation for adjustments to the initial reserve. Only 5 out of 56 files reviewed contained the required worksheets for the establishment of the initial reserve.

Conclusions:

1. The amount established for claims reserve is questionable as to its reliability due to lack of documentation and supporting supervisory review.

2. Risk Management has inadequate internal guidelines for establishing its claims reserve.
3. Risk Management does not have an established data base which could be used by its employees for establishing claims reserves.

Recommendations:

1. Risk Management should contract with an outside expert to perform a detailed analysis of its claims reserve.
2. Risk Management should provide its employees with comprehensive written procedures for establishing claims reserves.
3. Risk Management should consider establishing a data base to be used for the establishment of claims reserves.

2. Unfunded Liability

Risk Management's unfunded liability for current and future claims was approximately \$925 million as of June 30, 2001. This figure was derived from the estimated claims minus assets available to apply toward payment of existing claims.

On June 30, 2001, Risk Management reported a claims reserve of approximately \$618 million. Included in this amount is more than \$68 million for uninsured tort claims, consisting primarily of road hazard and medical malpractice claims, transferred to Risk Management in 1988.

Risk Management's claims reserve is an estimate of the total of directly related claim expenses, such as medical payments or compensation, and all direct non-claim expenses, such as legal fees, contract adjusters, court filing fees, etc.

At the end of a fiscal year, the actuary company of Tillinghast-Towers Perrin performs an actuarial analysis of reserves for the self insured coverage of the state. Based on the data provided by Risk Management, less the uninsured \$68 million, Tillinghast applies trends and development factors to estimate future losses. As with any estimate, there are inherent uncertainties, such as legislative tort reform, inflation, etc.; therefore, future losses can deviate from the estimates.

At the end of fiscal year 2001, Tillinghast estimated claims to be more than \$883 million while Risk Management estimated it to be as high as \$1.04 billion.

Based on Risk Management's unaudited June 30, 2002, figures, the estimated potential unfunded liability is approximately \$974 million (claims of \$1.002 billion minus cash of \$28 million).

Conclusion:

1. Based on information from Risk Management the state had an unfunded liability for claims of approximately \$925 million as of June 30, 2001. As of June 30, 2002, Risk Management's estimated unfunded liability is approximately \$974 million which has not been audited or analyzed by the actuary company.

Recommendation:

1. The commissioner of administration should work with legislative officials to determine an acceptable amount for the unfunded liability. To comply with their decision, the Risk Management director should develop a program to address the unfunded liability.

3. Lack of Assets Reserve

The level of funding for premiums has caused Risk Management to use prior year residual cash to pay for current claims and operational expenses, reducing its cash balance to approximately \$27.7 million as of June 30, 2002.

The state has used cash accumulation at Risk Management as a means of supplementing the state's operational cash requirement for the budget. For example, Risk Management was only allowed to collect approximately \$1.7 million and \$3.1 million for premiums to pay claims and operations in fiscal years 1992 and 1993, respectively. The remaining Risk Management expenditures were paid from accumulated cash, derived from actuarial developed premium billing from prior years, reducing the balance from approximately \$230 million to about \$16 million. This allowed the state to appropriate \$214 million for other budget needs but it also created a larger unfunded liability for future claim payments.

After fiscal year 1995, cash was allowed to accumulate to approximately \$170 million by the end of fiscal year 2000 by providing that premiums billed included projected cash flow needs plus an amount necessary to provide a cash cushion. Starting in fiscal year 2000, failure to appropriate sufficient premium revenue to cover claims and operational needs has reduced cash to approximately \$27.7 million by the end of fiscal year 2002.

The lack of a cash reserve creates:

1. Less flexibility for settling claims. Available cash provides the opportunity to take advantage of timely settlements when they are in the best interest of the state.
2. A potential funding crisis. In the event of a catastrophic occurrence, an overall budget crisis, or a management decision to move away from the self insurance program, the state would still have to provide funding to pay all existing claims.

Conclusions:

1. Risk Management has used prior year residual cash to pay current claims and operational expenses, resulting in the growth of an unfunded liability estimated to be \$974 million as of June 30, 2002.
2. Risk Management's cash balance was approximately \$27.7 million at the end of fiscal year 2002.
3. A low cash balance restricts Risk Management's ability for settling claims which may be in the best interest of the state.

Recommendation:

1. The commissioner of administration should work with legislative officials to determine an acceptable level of assets available to settle claims. To comply with their decision, the Risk Management director should develop a program to meet the goal.

III. Insurance Premium

Risk Management's ability to collect the amount required for its claims and operational expenses was limited. For fiscal year 2003, Risk Management may not have enough money to meet its claims, operational expenses, and Future Medical Care Fund requirements.

According to figures obtained from Risk Management, funding for premiums approved by the Office of Planning and Budget can differ significantly from the request submitted by Risk Management. For example:

<u>Fiscal Year</u>	<u>ORM Requested Premiums</u>	<u>OPB Approved Premiums</u>	<u>ORM Actual Expenditures</u>
2001-02	\$ 195,654,741	\$ 100,239,623	\$ 190,237,675
2000-01	279,962,480	114,124,534	159,893,702
1999-00	261,546,653	127,906,981	132,644,082
1998-99	252,594,351	147,254,569	156,313,609
1997-98	229,233,210	165,759,255	146,002,965
1996-97	350,086,643	227,485,898	171,777,140

In the past, there were fiscal years when Risk Management collected less premiums than it requested.

Problems associated with premiums are:

1. Risk Management's premium development on a cash needs basis and Office of Planning and Budget's approval of funds available (and not necessarily the amount required) has created existing or potential problems. For example, Risk Management was appropriated \$25 million less than its estimated expenditures for fiscal year 2003.
2. There is a lack of consideration for the legal requirement to replenish monies used from the Future Medical Care Fund.
3. Risk Management's "Safety Audit" program, which provides a 5% credit or 5% penalty of agency insurance premiums, is inconsistently administered.

1. Fiscal Year 2003

Risk Management was appropriated \$25 million less than its estimated expenditures for fiscal year 2003. As a result, it was required to deplete its prior year residual cash to avoid an operating deficit.

Risk Management primarily operates on funds it receives through premium collection and interest earned on investments. In order for Risk Management to have the ability to collect premiums, funds must be appropriated by the legislature to the various state agencies for insurance coverage.

For fiscal year 2003, Risk Management requested \$205.7 million for premiums but Planning and Budget has only included \$114 million for premiums and interest earnings in the state budget. Additionally, Risk Management will receive approximately \$16 million from the Deficit Elimination Act of 2002 making available total estimated revenue of approximately \$130 million.

Based on Risk Management's proposed \$205.7 million budget requirement less the \$50 million included for reduction of the unfunded liability, its estimated expenditures for fiscal year 2003 was approximately \$155 million. A comparison of fiscal year 2003 current estimated revenue and current expenditures shows a possible operating deficit of \$25 million. Expenditures for both fiscal years 2001 and 2002 exceeded \$155 million; therefore, the \$155 million estimate appears to follow the previous years trend.

In a June 28, 2002, letter from Deputy Commissioner of Administration Angele Davis, Mr. Thompson was advised judgments and settlements for road and bridge hazard occurrences will no longer be paid from the self insurance fund. Ms. Davis' letter does not indicate how road and bridge hazard judgments and settlements will be paid.

In his testimony to the Joint Legislative Committee on the Budget in July, 2002, Commissioner of Administration Mark Drennen stated that judgments and settlements for road and bridge hazards would require claimants to obtain an appropriation from the legislature.

Since 1997, the cost of road hazard claims, including judgments, settlements, and related administrative expenses, range from \$34.9 million to \$40.5 million. Should Risk Management not be required to pay for road hazard judgments and settlements from its fiscal year 2003 funds, it may have enough funding to prevent an operating deficit. Risk Management will continue to administer road and bridge hazard claims and pay associated expenses such as legal fees and court costs.

Act 61 of the 1988 regular session made road hazard coverage self insured and was incorporated into the risk management section of Title 39.

Conclusions:

1. Risk Management's estimated expenditures for fiscal year 2003 appear to be reasonable when compared to the two previous fiscal years expenditures.
2. For fiscal year 2003, Risk Management may have a \$25 million operating deficit. Risk Management will receive approximately \$130 million in revenues and has estimated its expenditures to be \$155 million. Should Risk Management not be required to pay for road hazard judgments and settlements from its fiscal year 2003 funds, it may have enough funding to prevent an operating deficit.

Recommendation:

1. Management should closely monitor all expenditures for fiscal year 2003 and explore all available sources for additional funding, including a supplemental appropriation.

2. Future Medical Care Fund

If payments are made from the Future Medical Care Fund in fiscal year 2003, Risk Management does not have the available cash to replenish the fund as required by law.

A \$10 million fund for the purpose of funding medical care and related benefits for individuals who have incurred these needs subsequent to judgments against the state or a state agency was established by ACT 20 of 2000. The ACT became effective July 1, 2000, and is known as LRS 39:1533.2, the Future Medical Care Fund. All court ordered payments for continued medical care of a claimant and administrative expenses are to be paid from the fund.

The \$10 million was transferred from Risk Management and is administered by the state treasurer. The fund is allowed to retain interest earnings which were \$844,767 through June 30, 2002.

A literal reading of Act 20 requires that at the close of each fiscal year, the state treasurer will transfer from the Self Insurance Fund to the Future Medical Care Fund an amount equal to monies expended from the fund for that fiscal year. Under a literal interpretation

of statute, the fund will increase in value equivalent to interest earned and would greatly exceed the original \$10 million in the future.

The chief fiscal officer for Risk Management believes that the intent of the legislation was that the interest earnings from the fund would be used to pay expenses of the fund. However, the law is very specific that the monies will be transferred from Risk Management's self insured fund.

Since inception there have been no payments from the fund, however, Risk Management expects payments from the Future Medical Care Fund will occur in fiscal year 2003. It is anticipated that Risk Management will use all its cash to pay claims and operating costs in fiscal year 2003. Therefore, there may not be funds available to reimburse expenditures made from the Future Medical Care Fund at the end of the fiscal year.

Conclusions:

1. Risk Management is not clear as to its responsibility in regards to LRS 39:1533.2.
2. Risk Management did not request funds to cover expenditures from the Future Medical Care Fund.

Recommendations:

1. Management should closely monitor all payments from the Future Medical Care Fund and insure funds are available to fulfill its obligation under the law.
2. Risk Management should request an Attorney General's opinion as to the intent of the Act and seek legislation, if necessary, to clarify the Act.

3. Safety Audits

Safety audits of state agencies are administered by Risk Management's Loss Prevention section on an arbitrary basis. The Department of Labor was given a failing mark while other departments with similar or the same infractions were passed.

LRS 39:1543 C. in part states "The Office of Risk Management, [Loss Prevention], shall conduct periodic loss prevention audits on each insured agency for the purpose of determining the agency's compliance with state law and loss prevention standards

prescribed by the Office of Risk Management." (emphasis added) LRS 39:1536 B (1) & (2) in part allows a 5% credit toward insurance premiums for agencies receiving certification for being in compliance with state law and loss prevention standards prescribed by Risk Management and a 5% penalty in premium cost for agencies failing a safety audit.

Criteria established by Risk Management for safety audits have not been applied uniformly to all agencies audited by Loss Prevention. Therefore, passing agencies may have failing deficiencies.

Loss Prevention conducts annual safety audits of agencies covered by the state's self insurance program. These audits are used to determine the effectiveness of a department's safety program and to provide insurance premium credits or penalties to the various departments.

The passing or failure of a department is determined by a field audit and an arbitrary decision by Loss Prevention Manager Doris Copeland.

The field officers performing a safety audit use a questionnaire to evaluate the various agencies and departments. The questionnaire outlines Loss Prevention's expectations of a department's safety program and is available to agencies on Risk Management's web site.

Ms. Copeland makes the ultimate decision as to which departments pass or fail. She has not provided this office with objective criteria for her decisions. According to Ms. Copeland, if one office or region within a department fails, then the department as a whole fails the safety audit.

Four departments were selected for evaluation of the field audits by this office; Department of Labor, Department of Corrections, Department of Agriculture, and the Department of Wildlife and Fisheries. Labor was the only department receiving a failing grade for its safety program.

According to Ms. Copeland, failure of any one of the following elements would cause a department to fail a safety audit.

- Conduct periodic safety inspections.
- Conduct the required amount of safety meetings with its employees.
- Conduct the required self audit (based on the questionnaire) prior to the Loss Prevention audit.

- Have on site driving records to determine which employees are eligible to drive state vehicles and identify drivers who are high risk.
- Have a high-risk driver policy.
- Maintain current inspection certificates for its boilers (if applicable).
- Maintain current inspection certificates for its elevators (if applicable).
- Have on site water vessel operator records (if applicable).
- Have a high risk water vessel operator policy (if applicable).

The above elements were used in our evaluation.

Labor had 11 infractions, Corrections had 8 infractions, Agriculture and Forestry had 24 infractions, and Wildlife and Fisheries had 6 infractions of the above elements. However, Labor was the only department failed by Loss Prevention while the other three departments were given passing certifications.

When presented with our results, Ms. Copeland defended her decisions by stating the intent of the law was to make agencies develop a loss prevention program. She said, if the agency made a good effort in trying to implement its safety program and the department as a whole was cooperative with Loss Prevention during the safety audit process, she gave this consideration when passing an agency. She stated that Labor was not cooperative.

LRS 39:1543 C. is very specific about passing certification being awarded only for compliance with state law and loss prevention standards prescribed by the Office of Risk Management. There is no rule or allowance in the standards prescribed by Risk Management which allows the Loss Prevention Manager, Ms. Copeland, to arbitrarily pass an agency that has failed a field safety audit. Risk Management promulgated its rules in 1988.

Additionally, our evaluation of the fiscal year 2002 safety audits disclosed that Loss Prevention does not maintain an audit tracking system which summarizes the results of field audits. This information is vital because if one office or region within a department fails, then the department as a whole fails the safety audit. There is no way to analyze Loss Prevention's statewide audit results for each department without analyzing each individual field audit.

Conclusions:

1. Pass or fail grades of safety audits are administered on an arbitrary basis.
2. Risk Management may have violated state law by passing agencies which did not meet the written requirements for safety audits.
3. Risk Management's criteria was promulgated in 1988 and may be too restrictive, especially the failing of one unit causing the whole department to fail.

Recommendations:

1. All safety audits should be performed and evaluated using objective criteria.
2. Risk Management should evaluate its current criteria, which was established in 1988, and consider a revision to the published rules.

IV. Contract Administration

Risk Management's contract procurement, management, and monitoring procedures are inadequate, costing the state hundreds of thousands of dollars.

The evaluation of contract administration encompasses the review of procedures for procurement, management, and monitoring of contracts from contract solicitation to contract expiration. We did not review contracts for litigation and related services.

On April 17, 2002, our office issued a report regarding three contracts administered by Risk Management. Information from the April 17 report has been incorporated into this report.

Specific problems are:

1. Employees failed to monitor contracts for items of substance. Contractors have been allowed to deviate from contract terms. Additionally, Risk Management does not hold employees assigned as contract monitors accountable for their non-performance.

2. Employees are assigned the responsibility to review contract invoices without the benefit of guidance, a copy of the contract, or the benefit of reviewing the contract.
3. Procedures do not insure that the agency will meet all state contract requirements.
4. Contract review procedures are inadequate to insure contracts are free of errors and adhere to state law, agency policy, management's intentions, the request for proposal, and the selected proposal.
5. The contract procedures manual is outdated.
6. The agency failed to comply with all statutory requirements for contracts.
7. Contract files did not always contain the required documentation.

1. Contract Monitoring

Risk Management failed to establish a contract monitoring program which provides controls and protects the interest of the state. Contractors drive the activities associated with their contracts while Risk Management's monitor generally signs off on whatever is invoiced by the contractors.

Additionally, a contract monitor was not informed of being assigned the responsibility for monitoring a contract.

Four contracts (CorVel, FARA Healthcare Management, Crawford & Co., and Elevator Technical Services, Inc.) were previously discussed in this report. The issues raised herein, pertain to monitoring failures, which were not considered previously.

CorVel was allowed to charge a \$76 per hour fee for services already required and compensated in its contract; FARA and Crawford performed and were paid for services outside the scope of their contracts; and Crawford was paid for travel expenses when the contract did not allow for such reimbursements.

For three of the four contracts, Ms. Jackson was assigned duties of the contract monitoring and liaison function. Ms. Jackson approved or allowed payments outside the terms of the contracts. It is the monitor's responsibility to ensure the terms of the contracts were adhered to.

Additionally, State Loss Prevention Supervisor Jack Oliver, was assigned the contract monitoring and liaison function for the contract with Elevator Technical Services, Inc. Mr. Oliver was not aware of this responsibility until we interviewed him during the audit.

Conclusions:

1. The contract monitors have not assured that services are being performed and paid in accordance with contract terms.
2. An employee was listed as a contract monitor without being notified.

Recommendations:

1. Risk Management should develop a contract monitoring program which at the minimum informs, trains, and holds the employees accountable for their responsibility.
2. Management should, on a random basis, periodically review the work of the contract monitor to insure contractors are performing and being paid in accordance with the written terms of the contracts.

2. Invoice Review and Approval

Risk Management's procedures for contract invoice review and approval are inadequate to insure payments are made in accord with the contract.

Employees review and approve contract invoices for payment without the benefit of a copy or knowledge of the contract. This reduces the employee's review of these invoices to math calculation verification only.

Previously discussed in this report were the CorVel and Elevator Technical Services, Inc. contracts. Employees were assigned the duties of reviewing these contract invoices but were not provided guidance or a copy of the contract.

Two employees, Workers' Compensation Supervisors Page Feller and Debra Fitch, were assigned to review and approve billings for the CorVel contract but stated they were never shown the contract or the fee schedule associated with the contract. As a result, the contractor was improperly paid more than \$280,000.

Doris Copeland stated she approved invoices for the elevator contract which had an inspection report but does not verify the accuracy of the amount billed. She further stated that she thought Risk Management's accounting department checked the fees billed. Accounts Payable Supervisor Heidi Orr said accounting does not verify the fees.

As another example, Workers' Compensation Supervisor Bertha Meisner said she was assigned to review and approve invoices for the FARA utilization review contract but was not provided a copy of the contract. This condition likely contributed to FARA being paid \$22,958 of charges for services not attributable to the contract.

Conclusion:

1. Risk Management approves invoices for payment without assuring the work is being performed and the invoice amount is in accord with the contract fee schedule.

Recommendations:

1. Risk Management should develop comprehensive written procedures for the review and approval of contract invoices.
2. Employees should be trained on how to review and approve invoices.
3. Employees who are responsible for reviewing and approving contract invoices should have a copy of the contract.

3. Lack of Statutory Compliance Procedures

Risk Management does not have procedures requiring that performance evaluations for professional, personal, consulting, and social service contracts of \$250,000 or greater are submitted to the Office of Legislative Auditor as required by state law.

Lack of the procedures increases the risk of noncompliance with statutory requirements.

The contract policy and procedures manual includes procedures regarding the preparation of performance evaluations for contracts and their submission to the Office of Contractual Review. However, the manual does not address the required submission to the Legislative Auditor.

Bonnie Fuller, the contract supervisor, said her office has been submitting the evaluations to the Office of Contractual Review but was not aware of the state law regarding the Legislative Auditor.

Conclusion:

1. Risk Management does not have procedures ensuring compliance with state law requiring that contract performance evaluations are submitted to the Legislative Auditor for contracts \$250,000 or greater.

Recommendation:

1. Risk Management should establish procedures to ensure compliance with state law.

4. Inadequate Contract Review Procedures

Risk Management does not have adequate contract review procedures to insure contracts are free of errors and adhere to state law, agency policy, management's intentions, the request for proposal, and the selected proposal prior to submission to the risk director for approval.

Lack of adequate procedures increases the risk that contracts containing errors detrimental to the state are approved.

Although not in writing, Risk Management's practice for contracts originating from a request for proposal process has been that the contract supervisor, the accounting administrator, the pertinent claims manager, and the assistant director review the contract prior to submission to the director for approval.

Risk Management does not require the contract review staff to certify the accuracy of the contract in writing. Certification by individuals identifies the employee responsible for the review.

An example of these inadequate procedures was previously cited in the Office of Inspector General report dated April 17, 2002. This report contains a finding regarding the failure of staff to properly review and correct a recent contract containing an improper fee increase that would have cost the state nearly \$770,000 if the maximum of the three year contract had been reached. No one was required to certify the accuracy of the

contract before sending to the director for approval. The individuals acknowledged their reviews were only cursory.

Conclusion:

1. Risk Management does not have adequate contract review procedures to insure contracts originating from a request for proposal are free of errors and adhere to state law, agency policy, management's intentions, the request for proposal, and the selected proposal prior to submission to the director for approval.

Recommendation:

1. Risk Management should establish procedures that clearly define and delegate contract review responsibilities to appropriate staff, require the staff to certify the accuracy of the contract in writing, and hold the staff accountable for the assigned responsibilities.

5. Outdated Manual

Risk Management failed to maintain an updated policy and procedures manual for its contract unit. An outdated manual increases the risk of employees not performing their duties in accord with organizational goals and objectives.

The contract unit is responsible for obtaining required signatures, routing, and monitoring contracts through an approval process.

Review of the manual, last revised Jan. 1, 1996, revealed the following deficiencies:

1. At least 16 of the manual's 25 sections contain provisions that are not consistent with current policies and practices.
2. The manual lacks complete detailed (step by step) procedures to guide employees in processing the various types of contracts administered by the agency.
3. The manual indicates that a separate Contract Unit is organizationally located within the Administration Section under the direction of the state risk director. However, the current agency organizational chart shows the contract function is within the Accounting Section under the direction of the accounting administrator.

4. The manual references an old computer system no longer used for tracking contracts.
5. The manual lacks updated signing authority and thresholds for the approval of contracts and contract amendments.
6. The manual lacks any provisions regarding the signing authority and thresholds for the form used to initiate the drafting of a new contract.
7. The manual lacks updated billing guidelines and rates for adjuster contracts.
8. The manual references outdated Civil Service and state law provisions.
9. The manual references contract payment procedures which are not applicable.

According to Ms. Fuller, the agency never assigned anyone responsibility for insuring the manual stayed updated. Ms. Fuller said her office is currently updating the manual. Acting Assistant Risk Director Pat Reed said it is her intention that comprehensive policies and procedures are developed for all Risk Management operations including contract administration.

Conclusion:

1. Risk Management failed to maintain an updated comprehensive policy and procedures manual for its contract unit.

Recommendations:

1. Risk Management should update its policy and procedures manuals.
2. Risk Management should ensure that updated comprehensive policy and procedures manuals are distributed to employees and that they are held accountable for compliance with the manual.

6. Noncompliance with Statutory Requirements

Risk Management failed to comply with certain statutory requirements in all 8 contracts from a sample of 8. As a result, the best interest of the state may not be realized.

A judgmental sample of 8 contracts from a population of 81 active contracts as of April 30, 2002, was tested to determine if Risk Management complied with state law regarding contract administration. The population did not include litigation-related contracts (attorney contracts, expert contracts) since these were excluded from the review scope.

The tests revealed:

1. For 2 of the 8 contracts, Risk Management failed to prepare a cost benefit analysis as required by LRS 39:1497. In addition, Risk Management falsely certified to the director of Contractual Review the analyses were conducted.
2. For 5 of the 8 contracts, Risk Management prepared inadequate cost benefit analyses that appeared to be more form than substance.

State law requires a cost benefit analysis be conducted which shows it is more cost-effective for the agency to obtain the services from the private sector than providing the services itself. The analyses prepared for the 5 contracts included a standard blanket document Risk Management recently developed for its adjuster contracts. The documents appear insufficient since they provide no information regarding the feasibility and cost for the agency to hire new staff or reassign current staff to provide the services in-house. The blanket analyses simply said no employees of Risk Management could perform the services and listed the benefits for the services.

The benefits of the services are not in question. However, the analyses failed to adequately address the necessity of contracting for the services.

3. For 1 of the 8 contracts, an interagency agreement, Risk Management falsely certified to the director of Contractual Review that a cost benefit analysis had been conducted when no such analysis was performed and not required.
4. For 4 of the 8 contracts, Risk Management failed to prepare a certification to the director of Contractual Review that certain statutory requirements regarding contract personnel and actions had been met.

Typically, the required certification letter is transmitted with contracts submitted to Contractual Review for approval. However, the 4 contracts in question were approved under the agency's delegated authority and did not require Contractual Review approval. Contract unit personnel acknowledged that the certification letter should have been prepared and maintained in the contract file for review if requested.

The issues of false certifications and failure to prepare a cost benefit analysis were previously cited in an Office of Inspector General report dated April 17, 2002. Risk Management took measures to resolve the findings of the previous report but fell short with respect to the adequacy of cost benefit analysis content. Without an adequate analysis, the necessity and cost-effectiveness of contracting the services rather than performing the services in-house cannot be substantiated.

Conclusions:

1. Risk Management failed to comply with statutory requirements regarding the preparation of cost benefit analyses and certifications on all contracts tested.
2. Cost benefit analyses contain insufficient information to justify obtaining the services from the private sector.

Recommendations:

1. Risk Management should develop procedures to insure compliance with all state laws and regulations regarding contract procurement. At a minimum, the procedures should assign and hold accountable, individuals responsible for contract procurement duties.
2. All contracts should be justified by cost benefit analysis.

7. Incomplete Contract Files

Files maintained by the contract unit for at least 3 out of 8 or 37.5% of contracts reviewed lacked certain documents required by Risk Management policy or the contract terms. The contract unit serves as the central repository for Risk Management contract documents.

Tests of files maintained on the 8 sampled contracts revealed:

1. For 2 of the 8 contracts, the contract unit file did not contain insurance certificates substantiating that the companies had errors and omissions coverage as required by the contract terms.

One company, under its three-year contract that expired July 31, 2002, was required to maintain \$1 million of errors and omissions coverage. The contract was solicited through a request for proposal process in 1999. Records indicate

the company included its insurance certificate in the proposal it submitted. However, this proposal and insurance certificate were not found in files maintained by either the contract unit or Workers' Compensation Unit.

The other company, under its medical records review contract that expires Sept. 30, 2002, includes a provision requiring the contractor to carry errors and omissions coverage with a minimum limit of \$500,000 per claim. Risk Management uses a standard blanket contract for medical records review services.

The contract unit file did not contain the insurance certificate. Review of Risk Management policy revealed that contractors for medical records review services are not required to maintain errors and omissions coverage. Ms. Fuller acknowledged the provision in the standard blanket contract is in error. She said there are plans to remove the provision when the next contract renewal period begins Oct. 1, 2002.

2. The contract unit file did not contain proof that the company owner and investigators employed by the company are licensed.

Risk Management policy provides that it contract for surveillance services from licensed investigators only. Investigators are licensed annually and companies are required to furnish proof of the license. After being advised of the lack of proof in the file, Lucille Gautreaux, a contract reviewer, obtained copies of the required licenses from the companies.

However, further inquiry revealed that in practice, Risk Management has not been requiring any of its surveillance companies to provide proof of valid licenses annually when the contract is renewed. Ms. Gautreaux said the proof is only required of first-time surveillance contractors.

Risk Management cannot substantiate that it is contracting with responsible companies when its files are incomplete and do not contain required insurance and licensing documents.

Conclusions:

1. Risk Management failed to maintain documents required by policy or the contract in at least 3 of its contract files.

2. Risk Management included a certificate of insurance provision in its standard contract for medical record review services that is not consistent with its policy and current practice.
3. Risk Management failed to obtain proof that the owners and investigators of surveillance companies under contract maintain valid investigator licenses.
4. Contract unit personnel were not aware of the requirement that the proof of valid investigator licenses be obtained annually upon renewal.

Recommendations:

1. Risk Management should ensure contract files are complete and required documents are safeguarded against loss.
2. Risk Management should determine if contractors providing medical records review services should be required to maintain errors and omissions insurance. The policy and standard blanket contract language should be revised accordingly.
3. Risk Management should establish procedures to ensure that proof of valid licenses are obtained from surveillance companies before contracts are executed.

V. Previous Audit Findings

Risk Management has failed to correct previous Legislative Auditor's findings.

The findings reported to management after the June 30, 2001, audit were for lack of an internal audit function and inadequate control over workers' compensation claims and reserves.

Corrective Action

The main focus of Risk Management in its response to previous audit findings focused on a lack of employees with no thought given to other alternatives.

INTERNAL AUDIT FUNCTION

The Legislative Auditor reported that Risk Management has failed to put into place an internal audit function for the past 8 consecutive years.

Management's response was that it had attempted in the past to establish an internal audit function but did not succeed. However, because of the loss of positions, management felt that the current choice of filling positions must be directed toward positions which will relieve the workload in the agency.

In its attempt, Risk Management established an auditor 2 position which was at a GS 17 pay level at the time. This action failed because:

- According to Civil Service's standard for the position of an auditor 2, it is a journeyman level position and would require supervision to perform audits. Generally, anyone filling this level position would lack the auditing knowledge and experience to perform the work needed.
- Based on the educational qualification required for this position and the low pay grade level of a GS 17, the employee filling this position could easily find a promotional opportunity after obtaining experience. In fact, this position was filled on two different occasions and both employees promoted to higher pay level non-auditing positions.

Standards for the Professional Practice of Internal Auditing as promulgated by the Institute of Internal Auditors provides that the internal audit activity of an organization should be independent, and internal auditors should be objective in performing their work. Internal auditors are considered independent when they can carry out their work freely and objectively.

These standards further provide that the chief auditor should be responsible to an individual in the organization with sufficient authority to promote independence and to ensure broad audit coverage, adequate consideration of audit communications, and appropriate action on audit recommendations.

MISSTATED RESERVES

The Legislative Auditor reported that for the past 5 years, Risk Management has misstated reserves for second injury claims and has not requested timely reimbursement.

The Second Injury Fund was established to encourage employment of persons with previous injuries or disabilities. LRS 23:1378 divides the financial responsibility for paying second injury claims between Risk Management and the Second Injury Fund.

Again, Risk Management responded with the excuse of reduced positions. It did not consider evaluating current work practices or determining other means which could be employed.

Conclusion:

1. Risk Management blamed the lack of personnel for its problems cited by the Legislative Auditor.

Recommendations:

1. The Division of Administration has already taken steps to provide an internal audit function, through the Office of Inspector General, to include the Office of Risk Management.
2. Risk Management should comply with its obligation regarding the Second Injury Fund.

VI. Audit Observations

During the audit, several activities were observed but a detail review was not performed. These observations are provided in a brief format with solutions for management's consideration.

Observation 1:

With the high dollar volume of claims and contracts administered by Risk Management, there are numerous opportunities for employees to conspire to misappropriate state assets.

During our review, we noted:

- Risk Management lacks internal monitoring procedures.

- Some key employees take little annual leave and when they do, no one performs the task of that position.
- Some employees have an opportunity to develop a close relationship with contractors.

Solution:

Implementation of a comprehensive system of internal controls. At a minimum the system should include:

- Random and unannounced temporary reassignment of high risk duties for at least a week at a time.
- Periodic independent internal audits.
- Higher ethics standards by adopting stricter agency regulations in regards to gratuities provided by contractors and acceptable associations with contractors.

Observation 2:

When obtaining information for the audit, there were some key employees who were the only ones that could provide us with the information. Should the key employee suddenly leave Risk Management, the office would be put in a difficult position to perform the functions of the employee.

Solution:

- Employees should be cross trained for several duties within their section.

Observation 3:

The claims council draws on the experience of employees for evaluation of difficult claims in regards to prospective settlements. The council is designed to make recommendations to the director of Risk Management. Under previous management, the decisions in the claims council were driven by the director instead of relying on the council's guidance and recommendations.

Solution:

- The director of Risk Management should not participate in the claims council but should use it to provide advice.

Observation 4:

The procedures manual for accounting was so outdated that the state no longer uses the accounting system referred to by the manual.

Solution:

- The procedures manual for accounting should be totally rewritten to correspond with current operations.

Responses:

Responses from Risk Management and CorVel are attached.

IG Comment:

The services which CorVel claims are extra actually are included in the contract and therefore not subject to additional compensation.

The contract specifically says "the parties further agree that no other sums will be due or payable under the provisions of this contract."

CorVel's assertion that omission of additional fees from the contract was an oversight by the Office of Risk Management is countered by the clear statement in the request for proposal saying "Proposer fees must include all the services described in the RFP." CorVel's proposal listed the services at issue but did not call for additional fees.

By granting the additional sums to CorVel, the Office of Risk Management gave CorVel a serious advantage over other proposers whose cost factors were evaluated on the basis of the stated fee schedule. The evaluation process assigned provided that the cost factor would be 33 per cent of the grade. In grading the

proposals, the evaluators did not consider any additional costs for CorVel, nor did the grading sheets contain any reference to additional costs.

It is clear to the Inspector General that CorVel was overpaid \$280,000 for services required by the request for proposal, the proposal submitted by CorVel and by the contract.

BL/KA

File No. 2-02-0002



State of Louisiana
DIVISION OF ADMINISTRATION
OFFICE OF RISK MANAGEMENT

J. "MIKE" FOSTER, JR.
GOVERNOR

MARK C. DRENNEN
COMMISSIONER OF ADMINISTRATION

September 13, 2002

Mr. Bill Lynch
State Inspector General
Office of State Inspector General
P. O. Box 94095
Baton Rouge, LA 70804

Dear Mr. Lynch:

Re: Response to File No. 2-02-0002

On behalf of this office, I thank you for the opportunity to provide a response to your draft report "Office of Risk Management Operational Review" dated September 3, 2002. Your report covered five major areas of concern: Payment/Disbursement Function, Reserve Valuations, Insurance Premium Development, Contract Administration and Previous Audit Findings. We, generally, concur with the findings and conclusions rendered in all five areas that were reviewed. Therefore, I will attempt to address the steps of corrective action being implemented by the Office of Risk Management.

I. PAYMENT/DISBURSEMENT FUNCTION

1. Contract Knowledge

Upon my review of the Corvel contract, I certainly understand the IG Office's concern relative to the overpayment of more than \$280,000 for one contract. We will bring these concerns to the attention of the Division's Legal Counsel and pursue recovery based on their recommendations.

Personnel in the Contracts Unit and Claims Unit have already attended initial training regarding the state contracts rules, regulations and procedures. In the Claims Unit specifically, Karen Jackson has received training in the area of contracts and RFP's as presented by the Office of Contractual Review and has attended a one day seminar on RFP's as presented by the National Institute of Governmental Purchasing (NIGP). This office supported Mrs. Jackson desire to become a member of this national purchasing organization that can provide another source of information in the preparation and evaluation of RFP's. In addition to the training received, this office has formed an RFP committee to participate in the RFP process from the drafting of the proposal through the review of the contract (prior to execution of the contract). This committee is comprised of four employees of ORM as well as a representative from the Office of Planning and Budget and/or the Legislative Fiscal Office.

Terry Grimball has been designated as the Contract Monitor and the contract liaison for the Corvel contract. She has been provided a copy of the contract as well as a contract performance log to document the activities of the contract relative to the payment of bills, ensuring work is performed in accordance with the terms of the contract and/or resolving complaints surrounding work of the contractor. Mrs. Grimball has been made aware that she is accountable for monitoring this contract.

2. Invoice Approval Without Contract

Payments made under the FARA contract which were not contract related and should have been paid against the appropriate claim files will be transferred from the contract payment file to the claim file within the next thirty days. Additionally, once the new contract is in place, the designated contract monitor and contract liaison for this contract will receive a copy of the contract as well as a contract performance log to document the activities of the contract whether it is payment of bills, ensuring work is performed in accordance with the terms of the contract and/or resolving complaints surrounding the work.

Employees have been instructed they will be held accountable if they begin services on contracts before the actual approved contract is in place, even if the services to be performed are a continuation of services with the same vendor as in the case of Corvel Corporation. Employees will be held accountable for initiating the RFP process in a time frame that will allow sufficient time to secure all of the necessary contract approvals prior to the expiration date of the current contract.

All invoices submitted for payment under a contract will comply with contract billing guidelines. Invoices with services that are not specifically addressed in the contract will not be processed for payment as in the case of the Crawford contract.

3. Unallocated Expenses

We have revised our allocation procedures to use an average hourly cost derived from the total amount paid to Risk Litigation by the total number of hours worked by Risk Litigation which will be applied on a quarterly basis and will include a cumulative adjustment. The new interagency agreement with the Attorney General's Office has been revised to reflect this change.

4. Lack of Certification

Chuck Johnson of State Buildings and Grounds who has contact with the elevator/escalator inspectors has been instructed to not only verify that the work was performed and that the charges are in accordance with the contract, but he is to so state on the invoice which he approves for payment by Risk Management.

This office has reviewed this contract to determine the appropriateness for ORM to procure this contract. We think that the appropriate agency to contract for these services is Facility Planning and Control, more specifically Office of State Buildings. I have discussed this with the Director of FP&C and I have confirmed our position in writing. The current contract expires June 30, 2004, at which time we expect FP&C will assume responsibility for initiating the RFP process.

5. Untimely Payments

One change that has just begun throughout the Claims Unit is adjusters/examiners are inputting claims directly into the computer system rather than completing a claim adds form and giving it to a clerk for entry into the Claims Management System. This new procedure will free up the clerks to input payments.

II. RESERVE VALUATIONS

1. Claims Reserve

We have taken steps to hold the supervisors and managers accountable for reviewing a specified number of adjuster's files. On litigated cases, the status of information required from defense attorneys will be monitored and followed up on when necessary. As a result of my concern for the adequacy of the claim reserves for each claim, we have initiated a consulting contract with the Ward Group to develop and recommend claims case reserve processes and procedures consistent with industry best practices. Seventeen of our adjusters just completed a two-week training program, which included training in reserving and evaluating claims.

III. PREMIUMS

5. Safety Audits

The Loss Prevention Manager was recently assigned the initiative to redesign the safety audit program that will be based on objective, measurable criteria. I have instructed her to develop a grade point system, which would tie the work being done to a numerical value rather than a narrative description of what is being accomplished at the agency.

The Loss Prevention staff has initiated mid-year audits. This will enable the Loss Prevention Officer to visit the agency six months after the audit to ensure requirements/recommendations to the agency have been completed. With the initiation of this mid-year visit, the Loss Prevention Officer can also review problems with trends, claims costs, accidents, etc.

I have issued a change in philosophy previously established by my predecessor. The redesigned safety audit program will allow each agency to pass or fail the audit down to and including the "L" billing level. This will allow the agency the flexibility to maintain its individual programs without fear that one mistake would cause everyone to fail.

IV. CONTRACT ADMINISTRATION

1. Contract Monitoring

This was addressed in *I. PAYMENT/DISBURSEMENT FUNCTION, 1. Contract Knowledge* above.

3. Lack of Statutory Compliance Procedures

ORM Contract Unit procedures have been revised to require that a copy of the Performance Evaluations for contracts \$250,000 or greater is to be submitted to the Office of Contractual and the Legislative Auditor.

4. Inadequate Contract Review Procedures

Policy and procedures require Contract/Grant Reviewers be required to review the accuracy of contracts which they process. Each reviewer initials and dates each contract request form. The use of a "check list" has now been implemented which will facilitate the review for accuracy and adherence to appropriate contract procedures. Contracts are also routed through the approval process for further review. The RFP Committee will review contracts requiring the issuance of a RFP before they are submitted to Civil Service or Contractual Review for approval.

5. Outdated Manual

The Contract Unit is currently updating the Policy and Procedures manual. The updated manual will contain policy and procedures for each type of contract issued by the ORM Contract Unit. The manual will also include updated signing authority, billing guidelines for adjusters and attorneys, contract payment procedures and the approval process. Maintenance of the Policy and Procedure Manual has been assigned to a Contract Unit staff member. A copy of the Contract Policy and Procedures will be provided to each Contract employee. Employees will be held accountable for adherence to the policy and procedures and will be a part of the PPR process.

6. Noncompliance with Statutory Requirements

Every new contract issued will contain a justified cost benefit analysis that will be completed by the appropriate Unit who receive the services. The analysis will be filed in the contract file. If a blanket analysis is justified, a copy will be kept in the Contract Unit.

Mr. Bill Lynch
Page 5
September 13, 2002

7. Incomplete Contract Files

The Contract Unit is currently updating a "checklist" for the issuance of contracts. Each Contracts/Grants Reviewer will be responsible for ensuring that proper documentation has been received before a contract is approved. Pertinent documentation will be maintained in the contract file or a separate attorney or adjuster file. The Contract Unit has amended its procedures to require that proof of valid license shall be requested before a contract is approved.

V. PREVIOUS AUDIT FINDINGS

Seeking recoveries from the Second Injury Fund is one of the components in the Claims Unit initiatives that are to be developed and implemented as a result of the Methods' Technology recommendations.

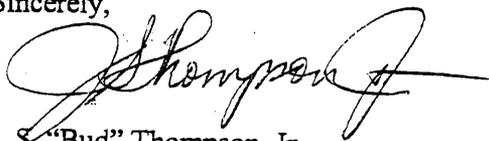
VI. AUDIT OBSERVATIONS

This office will include corrective action in our initiatives that we are undertaking in the various areas addressed in these audit observations.

Shortly after I reported to the Office of Risk Management as the State Risk Director, we received the Internal Operations Assessment Final Report from Methods Technology Solutions, Inc. As a result of their recommendations we have developed initiatives, which we expect to substantially improve the operational deficiencies in the Office of Risk Management.

I respectfully submit this response to be included in your above referenced report.

Sincerely,



J. S. "Bud" Thompson, Jr.
State Risk Director

JSTJR/PHR

CORVEL

September 16, 2002

Bill Lynch
Office of the Inspector General
State of Louisiana
Division of Administration
224 Florida Blvd.
PO Box 94095
Baton Rouge, LA 70804-9095

Reference: File No. 2-01-0002

Via Facsimile Message – 225-342-6761

Dear Mr. Lynch:

This will acknowledge receipt of your letter dated September 3, 2002 with accompanying draft report concerning your recent operational review of the Office of Risk Management. We thank you for extending the courtesy of an opportunity to respond to the findings regarding CorVel and take this opportunity to do so.

In the report, your auditors have taken the position that the charge made for professional fees during the term of our contract to provide our services for the Workers' Compensation Medical Fee Schedule Reimbursement Program is an overpayment and not defined in our "Contract for Service" which commenced August 1, 1999 and expired January 31, 2002. Your draft report, further, calculates the amount of the overpayment is \$280,000, based on the fact that payments were made over and above the fees outlined in the aforementioned contract.

Please be advised that our position is that we respectfully disagree with the findings of the auditors and state our position herein.

Page Four, Paragraph 4. (1) of the aforementioned contract outlines the fees described for Reimbursement Schedule Review. It further outlines specific services to which those fees apply, all of which are considered the industry "norm" of a fee schedule review service. However, the next page begins to describe "**Specialist Review**," "**Medical Consultation**," and "**Surgery Specialist Review**," all of which provide for additional "work units per bill."

A registered nurse, or other medical professional, with the training and background to assess certain procedure codes and claims as the need arises, typically performs these services. This level of service is typically referred to as "bill auditing" and/or "utilization review." CorVel, as most vendors providing these services, has a standard procedure chart which flags when the nurse gets involved. Those instances include but are not limited to the following examples:

- a. All hospital bills, both in-patient and out-patient, to review for appropriateness and relatedness of all services and procedures as well as to identify unbundled or

uncovered charges and any billing errors, comparing the bill and itemized charges with documentation from admit and discharge summaries, progress notes, and operative reports.

- b. All surgery and/or multiple procedures bills to review for appropriateness and relatedness of procedures and to insure that multiple procedure rules are applied appropriately, and that correct modifiers have been used for level of provider.
- c. Anesthesia bills to determine appropriateness of charges and codes for levels of providers and service rendered.

These services are a necessary component required to maximize the savings we deliver to our customers by eliminating charges that are excessive, in error, or unrelated to the claim. Review of medical reports and/or documentation is necessary to perform this level service and must be performed by a medical professional. This is a standard component of the service to achieve the goal of maximum savings not only with CorVel, but also with all other like-vendors. This service is always delivered with a charge for professional services at an hourly rate and charged in increments of an hour for the time the medical professional has actually devoted to the review of bills, supporting medical documentation, and/or medical reports, not only by CorVel, but also of other like-vendors.

Furthermore, it is apparent that the language in the contract, beginning on page five, recognizes that this additional level of service should command fees in addition to the "per line fee" of the standard fee schedule reductions, as evident by the inclusion of the language "**additional**" ... "**work units per bill.**" The dispute arises merely from the fact that there is no language present that defines neither a "work unit" nor how the "work unit" fee will be calculated.

It is CorVel's position that the mere absence of the language describing these does not negate the intents of the parties to the contract, nor the service to be delivered to achieve its purposes, nor does it relieve the obligation of the Office of Risk Management to fairly compensate the contractor for the service it required and was provided. CorVel's position is that this was simply a case of oversight on the part of the contract writer. In such cases, the Louisiana Civil Code, Chapter 13, dictates "Interpretation of Contracts" which we cite as follows, along with our position in each element.

CC2045

Art. 2045. Determination of the intent of the parties

Interpretation of a contract is the determination of the common intent of the parties.

Acts 1984, No. 331, § 1, eff. Jan. 1, 1985.

The common intent of both parties of the contract was to deliver "quality, efficient, and cost effective services" on the State's behalf in the reimbursement of medical costs for which the State was obligated to pay for its Workers' Compensation Claims.

We believe that the greatest cost effectiveness in those reimbursements is affected by professional medical review, to be performed by a medical professional, in cases where warranted. It would appear that this belief is in common with the Office of Risk Management, as evidenced by the language throughout the Request for Proposal issued by the Office of Risk Management requiring some levels of review be performed by medical professional.

CC2049

Art. 2049. Provision susceptible of different meanings

**A provision susceptible of different meanings must be interpreted with a meaning that renders it effective and not with one that renders it ineffective.
Acts 1984, No. 331, § 1, eff. Jan. 1, 1985.**

It is CorVel's position that the provision of the contract describing "Specialist Review," "Medical Consultation," and "Surgery Specialist Review" was susceptible to the more common industry meaning of "bill auditing," "utilization review," and/or "professional review." We further assert that there is a requirement contained in the contract as well as the RFP for a medical professional perform this level of review. This is the common practice among all vendors who deliver such services. To imply that this is the same service as a normal fee schedule review does render it ineffective since failure to use a medical professional for this level of review would fail to achieve the desired outcome.

CC2052

Art. 2052. Situation to which the contract applies

**When the parties intend a contract of general scope but, to eliminate doubt, include a provision that describes a specific situation, interpretation must not restrict the scope of the contract to that situation alone.
Acts 1984, No. 331, § 1, eff. Jan. 1, 1985.**

It is the position of CorVel that the auditor's comments that the service of Professional Review should be included in the normal fee schedule review, the cost of which should be covered by those defined fees, is in conflict with this Article. We feel it is evident in the contract language, on Page Two, Paragraph 2. E., that the Office of Risk Management intended some levels of review to be at a higher level and required they be performed by a registered nurse and/or physician advisor. We also assert that the contract provided for "additional work units" for these services.

CC2053

Art. 2053. Nature of contract, equity, usages, conduct of the parties, and other contracts between same parties

A doubtful provision must be interpreted in light of the nature of the contract, equity, usages, the conduct of the parties before and after the formation of the contract, and of other contracts of a like nature between the same parties.

Acts 1984, No. 331, § 1, eff. Jan. 1, 1985.

CC2055

Art. 2055. Equity and usage

Equity, as intended in the preceding articles, is based on the principles that no one is allowed to take unfair advantage of another and that no one is allowed to enrich himself unjustly at the expense of another.

Usage, as intended in the preceding articles, is a practice regularly observed in affairs of a nature identical or similar to the object of a contract subject to interpretation.

Acts 1984, No. 331, § 1, eff. Jan. 1, 1985.

CorVel asserts that this seemingly doubtful provision should be interpreted in view of the purpose of the contract, to provide a high level of review services. CorVel also asserts that a contract for these same services, which the Office of Risk Management entered into with Beech Street Corporation directly before the term of this contract, contained the provisions for the payment of professional fees at the rate of \$85 per hour with a \$150 minimum per bill, a higher fee than the CorVel fee in question. Additionally, the Office of Risk Management has recognized the error in the expired contract in question. The new contract between CorVel and Office of Risk Management has perfected this provision by adding the rate to be charged for the professional fee.

In the language of the Article cited above from the Louisiana Civil Code as respects "equity," CorVel asserts that it would be unfair and unreasonable for Office of Risk Management to expect the cost of registered nurses and medical professionals to be absorbed in a "per line" rate that is already substantially below the industry standard. We assert that this is evidenced also in the Beech Street contract wherein the "per line" fee is \$1.50 with a four-line minimum. This means that the fee for any one bill with only one line commanded a fee of no less than \$6. In the CorVel contract, that same bill would have a fee of only an average of \$.87 over the life of the contract.

CorVel further asserts that the professional review performed by the medical professionals affected a greater savings for the State than it would have had in absence of this review. The State has already derived the benefit of the service, using the "Explanation of Review" promulgated by CorVel, which contained explanations to the providers supporting the further reductions as dictated by those medical professionals. For the State to now assert that the fees are not owed is grossly inequitable since CorVel has incurred significant costs in the employment of medical professionals to provide this service to the State.

As respects the Article's language of "usage," CorVel asserts that the standard practice in the industry, among all like-vendors who provide these services, charge professional fees for reviews and/or audits performed by medical professionals. This is known to the staff of Office of Risk Management, as the auditor acknowledges in the draft report wherein he states "Ms. Jackson thought it was the industry norm to pay such a fee."

CC2054

Art. 2054. No provision of the parties for a particular situation

When the parties made no provision for a particular situation, it must be assumed that they intended to bind themselves not only to the express provisions of the contract, but also to whatever the law, equity, or usage regards as implied in a contract of that kind or necessary for the contract to achieve its purpose.

Acts 1984, No. 331, § 1, eff. Jan. 1, 1985

CorVel again asserts here, as respects this Article, that the failure of Office of Risk Management to provide provisions for this situation does not alter the fact that it is the industry norm, it was contained in their prior contracts as well as the subsequent contract, and it is necessary to achieve the purposes of the contract.

CC2056

Art. 2056. Standard-form contracts

In case of doubt that cannot be otherwise resolved, a provision in a contract must be interpreted against the party who furnished its text.

A contract executed in a standard form of one party must be interpreted, in case of doubt, in favor of the other party.

Acts 1984, No. 331, § 1, eff. Jan. 1, 1985.

CC2057

Art. 2057. Contract interpreted in favor of obligor

In case of doubt that cannot be otherwise resolved, a contract must be interpreted against the obligee and in favor of the obligor of a particular obligation.

Yet, if the doubt arises from lack of a necessary explanation that one party should have given, or from negligence or fault of one party, the contract must be interpreted in a manner favorable to the other party whether obligee or obligor.

Acts 1984, No. 331, § 1, eff. Jan. 1, 1985.

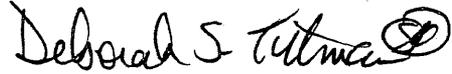
Since the Office of Risk Management furnished the text of the contract, and since the controversy stems from their omission of definitions, terms, and provisions, it is CorVel's position, in view of this most basic doctrine of contract law, that the interpretations of the contract must be in favor of CorVel.

In addition to the aforementioned arguments supporting CorVel's position, it should be noteworthy to point out to the Inspector General that services provided by CorVel under this contract have resulted in a **savings for the State and its taxpayers in the amount of \$10,443,235.17** over a two and one half year period, net of fees charged for the service. The savings reports documenting this are enclosed herein. This is an average of over \$4,000,000 per year. We note in the Office of Risk Management's Annual Reports that

during the years that Beech Street performed this service, the savings averaged around \$2,500,000 per year, while the fees, as outlined above, were substantially higher.

Please feel free to contact me at any time to discuss any item submitted here.

Very truly yours,

A handwritten signature in cursive script that reads "Deborah S. Tillman". The signature is written in black ink and includes a stylized flourish at the end.

Deborah S. Tillman
District Manager