

OSBM

STATE OF NORTH CAROLINA

**A Study of the
State Workers' Compensation Program**

As Directed by Session Law 2007-323, Section 23.3

March 2008



Prepared By:

*Office of State Budget and Management
In consultation with
Office of State Personnel
Office of State Controller*

[THIS PAGE IS INTENTIONALLY LEFT BLANK]

TABLE OF CONTENTS

<u>Section</u>	<u>Page</u>
Executive Summary.....	4
Introduction.....	6
Background.....	6
Effectiveness of Third Party Administration.....	7
Effectiveness of Current Funding Method.....	15
Necessity of Excess Coverage Policies.....	18
Other Operational Inefficiencies.....	19
Conclusions and Recommendations.....	21
Appendix A: Medical Benefits and Disability Compensation.....	24
Appendix B: Flowcharts.....	25

[THIS PAGE IS INTENTIONALLY LEFT BLANK]

EXECUTIVE SUMMARY

Section 23.3 of Session Law 2007-323 directed that the Office of State Budget and Management (OSBM), in consultation with the Office of State Personnel (OSP) and the Office of the State Controller (OSC), conduct a study of the Worker's Compensation Program (WC) in State agencies and institutions to:

1. Determine if Third Party Administration (TPA) of the program continues to be the most effective mode of administration;
2. Determine if the current method of funding is still the most effective method;
3. Determine whether excess coverage policies are needed; and
4. Identify any other operational inefficiency in program operations that might exist.

CONCLUSIONS AND RECOMMENDATIONS

With sufficient contract management, Third-Party Administration continues to be the most effective mode of administration.

- Using a TPA does not cost more than managing WC claims internally, and it likely costs less. For the State and Department of Public Instruction (DPI) programs, which use a TPA, administrative costs as a percentage of total costs were lower, as compared to the Department of Transportation (DOT), which administers its own WC Program without a TPA.
- Currently, the majority of State agencies and universities are not equipped to assume the additional responsibility of internal WC administration without a significant increase in staffing for the WC function. Neither are most agencies and universities prepared to develop their own provider networks.
- OSP does not allocate sufficient staff toward the State's TPA contract management. OSP staffing of the WC Program has decreased over the years, with diminished audit function.
- OSP should authorize an annual or biennial audit of the State's WC TPA.

The current method of funding is not the most effective method, because agencies and universities do not adequately budget for WC costs on a consistent basis through the biennial budget development process.

- Agencies and universities should budget for WC expenses as part of the biennial budget process. This would help agencies and universities better anticipate needs, rely less on lapsed salaries, and enable agency and OSBM budget analysts to track WC costs more accurately.
- In lieu of budgeting for WC through the budget process, State agencies and universities should study the feasibility of agency-funded payroll additives or set-aside percentages to help cover WC expenses. (This is more beneficial to larger agencies with more substantial payrolls.)
- The General Assembly should consider authorizing an actuarial valuation of the State's long-term WC liabilities.

Based on current available data, purchasing excess coverage policies cannot be justified.

- The State has experienced few and infrequent catastrophic cases, and this history does not justify excess insurance coverage at this time.
- If the State were to purchase excess coverage, it should consider creation of a WC Trust Fund to attract a private insurer, with each agency or university paying a premium based on a proportionate share.

There are operational inefficiencies in certain areas:

- Agencies and universities should assess where their WC function is located, and when appropriate, consider moving it from a human resource to safety function. Programs that operate under safety leadership illustrated more seamless communication with risk management and Occupational Safety and Health Administration (OSHA) reporting requirements.
- The State should authorize a study on the impact of combining WC program oversight and State disability retirement under one umbrella agency. Such an agency could provide a central database of cases and may better serve employees under both systems.
- The General Assembly should reconsider setting at least a 500-week cap on the duration of WC benefits, similar to that in other states. Such a cap would set an outer limit on duration of benefits (not dollars) and require settlement of claims within 10 years.
- Local Education Agencies (LEAs) should be brought under the State Return-to-Work policy more consistently. Not all LEAs have their own Return-to-Work policies. Those that do not should be required to follow State policy.
- Agencies and universities should encourage WC administrators to schedule regular discussions with the TPA to foster and enhance communication.

INTRODUCTION

Scope of Study

Section 23.3 of Session Law HB1473 directed that the Office of State Budget and Management (OSBM), in consultation with the Office of State Personnel (OSP) and the Office of the State Controller (OSC), conduct a study of the Worker's Compensation Program (WC) in State agencies and institutions to:

1. Determine if Third Party Administration (TPA) of the program continues to be the most effective mode of administration;
2. Determine if the current method of funding is still the most effective method;
3. Determine whether excess coverage policies are needed; and
4. Identify any other operational inefficiency in program operations that might exist.

This report outlines related findings with recommendations for improvements.

Methodology

In order to conduct the study, the OSBM study team performed the following tasks:

1. Reviewed statutory and policy language pertaining to the State WC program.
2. Reviewed the TPA contract and performance documents for pay structure, funding information, closure rates, and data/cost sheets, and compared TPA hours to Full-Time Equivalents (FTEs).
3. Reviewed WC cost reports from fiscal years 2002-03 through 2006-07.
4. Studied the WC Fund, Certified Budget, and claims payment process, including an assessment of whether agencies budget for WC costs and how lapsed salaries are used. Reviewed how different WC line items are used, and met with OSC to better understand this process.
5. Reviewed process for referring patients/employees for treatment for both medical and indemnity cases.
6. Met with WC administrators from the Department of Public Instruction (DPI) and the Department of Transportation (DOT) to understand their processes for paying claims, contracting with case managers, and/or setting up funding reserves. Compared these results to the overall State WC program, which uses a TPA (currently Key Risk Management Services).
7. Analyzed the benefits of excess insurance options, including rates, effect on premiums, and administrative impact.
8. Analyzed WC incident occurrences by agency and institution to detect patterns.
9. Reviewed existing safety/prevention programs at select state agencies and institutions to detect patterns and make useful recommendations.¹
10. Discussed with OSC the funding workflow and any compatibility issues between the existing WC program and BEACON system.
11. Discussed with OSP and the Department of State Treasurer the relationship between WC and other state benefits, such as disability or health insurance, and the impact of any change to the program.

BACKGROUND

The purpose of the North Carolina Workers' Compensation Act, G.S. 97-1, is to provide protection and benefits to all employees in the private and government sectors that are injured on the job. The Act is intended not only to provide swift and certain remedy to an injured employee, but also to ensure a limited and determinate liability for the employer.²

¹ Agencies interviewed were: Administrative Office of the Courts and the Departments of Agriculture, Correction, Health and Human Services, Insurance, Public Instruction, and Transportation. Universities interviewed were: Appalachian State, NC State, UNC-Chapel Hill, UNC-Charlotte, and UNC-Greensboro.

² See *State Government Workers' Compensation Program: Training Guide for WC Administrators* (OSP, September 2007).

The North Carolina Industrial Commission (NCIC) was created by the Workers' Compensation Act to administer the provisions of the Act.³ An employee's average weekly wage is used to determine the weekly compensation rate. The compensation rate for total and partial incapacity is equal to 66 2/3% of the average weekly wage, subject to a minimum and maximum amount established annually by the NCIC (Appendix A).

The State is self-insured and expenditures are paid from current operating budgets. Since 1987, OSP has provided technical assistance, consultation and training to assist agencies and universities with administration of their WC programs. In 1996, the State recognized that WC costs were escalating and that most agencies were only paying WC claims and were not managing cases effectively. Through the selective bidding process, the State contracted with a TPA to manage State WC claims. The contract was awarded to the firm of Key Risk Management Services with corporate headquarters in Greensboro and offices in Raleigh and Charlotte. All State agencies and universities, except for DOT, use Key Risk's services, although DPI does so through a separate contract.

EFFECTIVENESS OF THIRD PARTY ADMINISTRATION

Task 1: Determine if Third Party Administration (TPA) of the program continues to be the most effective mode of administration.

What the TPA Does

TPA services include coordinating accident investigations, determining State liabilities, paying claims, maintaining case files, managing a preferred provider network, coordinating return to work options, and assisting the Attorney General's Office (AG) with litigation management.⁴

The State's contract with Key Risk includes WC administration for State agencies and universities except for DOT, which administers its own WC program internally, and DPI, which has a separate contract with Key Risk (see Flowcharts 1-3 in Appendix B).

Costs of WC and TPA

Chart 1 shows WC claim expenditures (Medical Only claims plus Indemnity claims) for the past five years:

Chart 1 - Workers' Comp Claim Costs (excluding DOT)

	2002-03	2003-04	2004-05	2005-06	2006-07
State (non-DOT) claims	\$27,749,373	\$32,554,502	\$37,924,078	\$42,099,136	\$46,664,798
DPI claims*	\$25,460,904	\$28,282,660	\$31,822,634	\$37,581,937	\$39,468,293
Total Costs	\$53,210,277	\$60,837,162	\$69,746,712	\$79,681,073	\$86,133,091

*Includes split payments shared with local school units

The TPA attributes the increase in claim expenditures to higher costs of medical care, the extended length of time that some WC claims remain open, and the litigious nature of the WC industry.

³ The Rules of the Industrial Commission are regulatory procedures that must be followed to fully comply with the Workers' Compensation Act. The NCIC ensures that the law is followed, bills are in compliance with the NCIC Fee Schedule and disputes are resolved between claimants and employers.

⁴ Flowchart 1 (Appendix B) illustrates WC claim processing from the view of a state agency/university, while Flowchart 2 shows how a WC claim flows within the TPA.

Chart 2 illustrates WC administration costs (money paid to the TPA for its services) for the past five years:

Chart 2 - Workers' Comp Administrative Costs (excluding DOT)

	2002-03	2003-04	2004-05	2005-06	2006-07
State (non-DOT) fees	\$1,182,856	\$1,336,383	\$1,728,072	\$1,813,325	\$1,856,740
DPI fees*	\$1,461,270	\$1,396,887	\$1,672,835	\$1,767,710	\$2,155,495
Total Costs	\$2,644,126	\$2,733,270	\$3,400,907	\$3,581,035	\$4,012,235

*Includes split payments shared with local school units

WC administrative costs increased over the same period, but as a percentage of total WC costs (claims and administrative costs combined) they stayed relatively level at an average of 4.5% per year.

The total number of claims increased about 10% from 2002-03 to 2003-04, but since then remained relatively level:

Chart 3 - Number of Workers' Comp Claims (excluding DOT)

	2002-03	2003-04	2004-05	2005-06	2006-07
State (non-DOT) claims	6,175	6,844	7,260	7,307	6,835
DPI claims*	7,686	8,452	8,199	8,319	8,411
Total Claims	13,861	15,296	15,459	15,626	15,246

*Includes split payments shared with local school units; counts only new claims

The State is obligated to the fee schedule provided in Chart 4 through two separate contracts with the TPA. These costs reflect only the administrative costs for a WC claim, not the medical costs. Incidents where there are no lost wages are categorized as “Medical Only” claims; incidents with lost-work time and lost wages are known as “Indemnity” claims. Agencies may also file an incident report without further investigation, called “Medical Record.” These records serve as placeholders if a claim advances.

Chart 4 - Third Party Administration Fee Schedule*

	Per Indemnity (Lost Wage) Claims	Per Medical Only Claims	Per Medical Record Claim Filed	Key Risk Bill Review Savings
State (non-DOT) New Claims	\$895	\$160 (internet filed forms); \$165 (faxed or emailed forms)	\$35	TPA Receives 32% of Nurse Review Savings
State (non-DOT) Existing & Open Claims (transferred with new contract)	\$785 one-time maximum	\$0	\$0	
DPI New Claims	\$780	\$145	\$25	TPA Receives 20% of Total Bill Review Savings
DPI Existing & Open Claims (transferred with new contract)	\$175 one-time maximum	\$10	\$0	

*Excludes Add-on Expenses for Bill Review, Case Management, Litigation, etc.

There is a maximum, one-time charge for claims transferred from a prior year at the start of a new TPA contract. For example, the State pays a maximum \$895 charge for all new Indemnity claims. If the claim started as Medical Only at \$165 and converts later to an Indemnity claim, the State pays the \$730 difference (\$895-\$165).

Through the process outlined in Flowchart 2 (Appendix B), the TPA determines the category of the claim. The TPA fees outlined above do not include other expenses that may occur during the life of a claim. Additional fees include court costs, costs of undercover operative and detective services to determine fraud, nurse case management services, or medical bill negotiation. Nurse case managers become involved and negotiate charges with providers and can reduce the total cost, in some cases by more than \$6,000. However, under the State contract, the TPA receives 32% of costs that it recovers under nurse case management. In 2006-07, a total nurse review savings of \$100,748 was reported, of which \$31,313 went to Key Risk.

Through medical bill negotiation, the TPA reviews medical charges and detects discrepancies within associated Current Procedural Terminology (CPT) codes. The NCIC fee schedule sets the rates that it allows to be paid for certain treatments. Key Risk then reviews those charges and negotiates the rates to achieve a further reduction. The TPA maintains a Preferred Provider network, labeled the “CompCare network,” consisting of physicians who will provide services for a negotiated rate. As part of this service, the TPA receives a percentage of these savings, as outlined in Chart 5 for a hypothetical DPI claim:

Key Risk reports that there are CompCare Network providers in 83 counties. Key Risk also maintains a more expensive option called “CompCare LX,” available in 97 counties. The State contract operates under the CompCare Network, while DPI opted for CompCare LX.

Chart 5 - Sample of TPA Network Savings

Billed Amount	\$100
NCIC Allowed Charge	\$80
CompCare Network Allowed Charge	\$50
Savings Achieved	\$30 (\$80-\$50)
Contractual 20% Savings to Key Risk	20% of Bill Review Savings
Resulting TPA Additional Charge	\$10 (\$50 x 20%)

The differences in these networks can be felt in the more remote counties. Agencies and universities in these areas have reported sending injured employees out of the county to receive medical treatment. This is especially true for those without significant on-site medical facilities. For example, Appalachian State University

reported that there are no CompCare network providers for some medical specialties in Watauga County. Although immediate injuries can be treated at Student Health Services or an emergency room, employees must be referred out of the county for some follow-up therapies.

Current Procedural Terminology (CPT) Code Comparison:

With WC claim expenditures increasing and medical bill negotiation such an important component of the TPA’s role, an analysis of CPT codes is useful. CPT codes describe medical, surgical, and diagnostic services in order to communicate uniform information about medical services and procedures. CPT codes provide a uniform language for the WC TPA, the NCIC, and the State Health Plan. But the allowed charges are not always the same.

The NCIC fee schedule establishes allowable charges for certain treatments. Key Risk then reviews those charges and negotiates the rates to achieve a further reduction. Chart 6 contains a comparison of allowable fees for the same CPT code as determined by: the NCIC; the WC TPA; and the State Health Plan (SHP).

Chart 6 - Comparison of Allowable Charges for CPT Codes

CPT Code	Description	NCIC Allowed Fee	Average Key Risk Allowed Fee	Average SHP Allowed Fee
99201	New patient visit, problem focuses approx. 10 min.	\$41.40	\$38.39	\$44.00
99202	New patient visit, expanded problem focuses, approx. 20 min.	\$66.68	\$61.68	\$71.00
99203	New patient visit, detailed history/exam, approx. 30 min.	\$91.97	\$85.07	\$105.00
99204	New patient visit, comprehensive history/exam, approx. 45 min.	\$137.97	\$127.62	\$156.00
99205	New patient visit, comprehensive history/exam, high complexity, approx. 60 min.	\$173.59	\$160.57	\$197.00
99211	Estab. patient visit, problem focuses, approx. 10 min.	\$20.11	\$18.60	\$27.00
99212	Estab. patient visit, expanded problem focuses, approx. 20 min.	\$36.21	\$33.49	\$45.00
99213	Estab. patient visit, detailed history/exam, approx. 30 min.	\$51.16	\$43.66	\$64.00
99214	Estab. patient visit, comprehensive history/exam, approx. 45 min.	\$79.33	\$73.38	\$100.00
99215	Estab. patient visit, comprehensive history/exam, high complexity, approx. 60 min.	\$125.31	\$115.91	\$145.00

In this comparison, the TPA's negotiated allowed charge is the lowest of the three. Although claim expenditures for the program have increased, the TPA appears to be holding costs down for these CPT codes.

What Internal Administration Would Do and Cost

DOT is not part of the State's or DPI's TPA contracts; instead, DOT uses internal staff to manage claims. Flowchart 3 (Appendix B) shows the workflow process for DOT. Chart 7 illustrates DOT's total WC expenditures (claim costs and administrative costs) for the past five years:

Chart 7 - DOT Workers' Comp Costs

Claim Costs

	2002-03	2003-04	2004-05	2005-06	2006-07
DOT Claims Costs	\$7,428,913	\$6,490,573	\$7,560,331	\$7,099,896	\$7,740,090

Administrative Costs

	2002-03	2003-04	2004-05	2005-06	2006-07
DOT Admin Costs	\$516,212	\$616,722	\$607,184	\$693,870	\$628,966

Number of Claims

	2002-03	2003-04	2004-05	2005-06	2006-07
DOT Claims	886	879	790	709	661

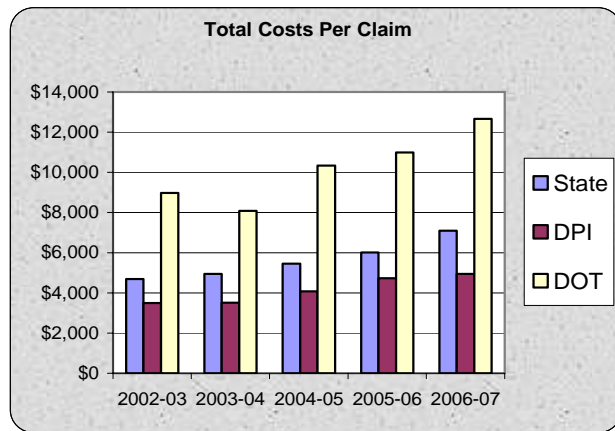
Within DOT, administrative costs increased from 2002-03 to 2006-07; as a percentage of total expenditures (claim costs plus administrative costs) they fluctuated with an average of 8% per year, which is higher than the 4.5% average of TPA-processed claims. The total number of claims per year (both Medical Only and Indemnity) decreased an average of 7% each year over the same period. In total costs per claim, the average increase per year for the agencies using a TPA and for DOT is fairly equivalent, ranging from 9.3% for DPI to 11% for the State (Chart 8).

Even if the State were to suspend use of a TPA for WC claims management, not every agency would be prepared to take on WC administrative responsibilities, at least not initially. Staffing levels would need to increase to reflect this duty.

Chart 8 - Total Costs per Claim

Agency or Group	2002-03	2003-04	2004-05	2005-06	2006-07	Average % Increase per Year
State	\$4,685	\$4,952	\$5,462	\$6,010	\$7,099	11.0%
DPI	\$3,503	\$3,512	\$4,085	\$4,730	\$4,949	9.3%
DOT	\$8,967	\$8,086	\$10,339	\$10,993	\$12,661	9.9%

DPI staff studied the requirements of operating WC administration in-house. DPI currently expends less than one FTE on WC administration, with the WC administrator involved in other duties such as unemployment and property. DPI also funds two full-time positions in the Attorney General’s Office to handle DPI cases. DPI has proposed expanding its internal staffing level to 13.5 FTEs at a cost of \$1.7 million in the first year, with nearly \$1.2 million in recurring annual costs. This estimate is nearly \$1 million less than the nearly \$2.2 million spent on administrative fees in 2006-07.



However, since this change only addresses administrative staffing and process changes, it is unclear what effect it would have on claim costs, which is the largest expense of a WC program.

Several points should be considered in weighing the advantages and disadvantages of continuing to use a TPA.

Advantages of using a TPA include:

1. **Administrative costs with a TPA can be lower.** Using a TPA does not cost more than managing WC claims internally, and it likely costs less. Looking at a five-year comparison of the State and DPI (with a TPA) and DOT (without a TPA), the total cost per claim with a TPA is lower than without. For the State and DPI programs, even though administrative costs increased over the period, they stayed relatively level as a percentage of total claim costs (4.5% per year). Administrative costs for DOT also increased over the same period, but as a percentage of total claim costs they averaged 8% per year compared to 4.5%.
2. **Staff can focus their efforts on other functions.** Although many positions per agency may be involved in WC administration, rarely is an entire FTE dedicated to the effort (see Chart 9, p. 13). If State agencies and universities assume internal State WC administration without a TPA, it would have an exponential effect on staffing needs to manage the program.
3. **The TPA handles daily bill payments.** As shown in the “Effectiveness of Current Funding Method” section below, the TPA works with the agencies, the Office of State Controller, and the Office of State Personnel to pay related medical and lost wage expenses. Resumption of internal WC management would consume much staff time and divert attention from other duties.

4. ***A TPA has expertise in this field.*** Although existing internal WC administrators have a grasp of WC management, new staff would require training to develop the skills to administer a program effectively, even with the best software programs.
5. ***The State would need to develop provider networks.*** This could involve developing the State's own version of a CompCare network and establishing contracts with providers across North Carolina to help control costs. It may be feasible for these contracts to dovetail with State Health Plan's Preferred Provider Option (PPO) networks, but this is unclear.
6. ***Most agencies and universities are not equipped to resume WC responsibility internally.*** In part, this may be because not all agencies or universities have high WC costs, particularly the smaller agencies. Few of the agency and university representatives surveyed in this study appear ready to begin the process of claims management, medical bill payments, and litigation preparation that a TPA provides.

Advantages of WC administration without a TPA include:

1. ***Agencies are more familiar with claim particulars.*** It can be argued that internal agency staffs know the unique aspects of their claims and the agency and campus culture better than a TPA. Internal agents have a vested interest in seeing that claims be closed satisfactorily. In-house administration would force these State WC administrators to be even more aware of cost containment because they would deal with the affected employees and supervisors on a daily basis.

Without a TPA, it would be even more important that WC be managed under a central agency, such as the Office of State Personnel, Department of Insurance, or State Health Plan. In South Carolina, the State Accident Fund functions as a single State agency reporting directly to the Governor. That agency is funded with premiums it collects from other State agencies, functioning similarly to an internal service fund. South Carolina officials report that the administrative costs to run the agency, including its legal department, premium calculations, payroll audits, and safety and loss control services, is less than 6% of total costs.

However, it is not clear that such a model could be duplicated in North Carolina, at least not at this time. The South Carolina State Accident Fund has existed since 1947. To make such a change in North Carolina would involve substantial personnel and budgetary changes. No State office is trained or equipped to take on a heavier WC administrative role at present. Few State agencies or universities claim that they allocated an entire FTE toward the WC function, although many positions have some part of this function.

TPA Compliance with Attorney General Filing Requirements

The Attorney General's (AG) office is used in all WC cases involving litigation.⁵ The AG's Office estimates that it requires more than \$760,000 in annual salaries to AG attorneys and staff for the State's WC Program. The State and DPI contracts state that files for litigated claims must be organized according to a specific 10-point format. Additionally, the file must be provided to the AG within 10 business days of the injured worker/claimant filing the appropriate form.⁶ Conversations with the AG's office indicated that this format is not always followed, although to what extent is not clear. The AG's office provided one recent case where the TPA did not follow the 10-point format and another recent case where the case files had not been fully provided within six weeks of the request date. The AG's office did not provide information on any older cases failing to meet these requirements. This limited information does not allow for further analysis, but suggests that an audit including a sample of litigated cases may be useful in quantifying whether or not this problem exists.

⁵ *State Government Workers' Compensation Program: Training Guide (September 2007).*

⁶ Such as Form 33: A Request That Claim Be Assigned for Hearing.

OSP Reorganization and Effect on Contract Management

During 2007, OSBM conducted an analysis of the human resources (HR)/payroll functional areas for those agencies and universities that will use BEACON for their HR/payroll function. These exercises, called Functional Area Mapping Exercises (FAME), allowed agencies/universities to provide data on positions with WC duties effective January 2007, but then to revise these figures as of June 2007. The positions were converted to FTEs based on the amount of time each position spent on WC. The June totals are included in Chart 9, along with the actual positions that have some involvement in the WC function. Universities that were included in this WC study but were not part of FAME are included in Chart 9 as well.

Not listed in Chart 9 is the Office of State Personnel, which requires separate analysis. OSP's current stated responsibilities for WC include administering the WC program for the State, contract management of the TPA, and assisting the Office of the State Controller (OSC) in determining proper payments to the Workers' Comp Fund by agencies and universities (explained in the Funding Method section below).

Since FY 2001-02, OSP has gradually reduced the FTEs allocated toward WC administration for the State. There is currently less than one FTE allocated to WC administration for the entire State (see Chart 10 on the following page).

The 2001-02 changes removed the WC Analyst position that had conducted bi-annual TPA audits and helped with TPA contract oversight. This position was not entirely removed from the WC program; this staff person was shifted to other duties but was available in the event that the WC/Unemployment Coordinator was away. In 2001-02, the WC function also lost a full-time technician position, which assisted with WC database management and tracking. Although the WC Coordinator's allocated FTEs for WC remained at about 0.4, the overall effect on the program was a reduction of resources.

In 2006, OSP added a WC/Unemployment Analyst position, which assists with research, data maintenance, and analysis. However, the employee does not serve in a much needed audit function. In 2007, the WC/Unemployment Coordinator position received additional duties to include Temporary Solutions oversight, WeSave Employee Discount program oversight, Worksite Wellness Program coordination with the State Health Plan, and supervision of eight employees. This change effectively reduces oversight of the State's WC program even further, while associated WC costs have been increasing.

These changes significantly reduce OSP's contract management capability. The program's oversight has largely been through an agency survey or on a case-by-case basis.

Chart 9 - WC Agency & University FTEs

Agency	6/30/07 FTEs	Positions with WC Duties
Agriculture	0.20	1
AOC	0.40	1
Auditor	0.10	1
CCPS	0.27	6
Commerce	0.20	2
Cultural Resources	0.47	4
DENR	1.91	16
DHHS	8.03	71
DOA	0.36	6
Correction	10.75	102
Insurance	0.19	2
Justice	0.50	3
Labor	0.40	2
Revenue	0.15	3
DOT	7.31	109
DPI	0.50	1
ESC	0.75	2
ITS	0.10	1
JJDP	0.65	9
Community Colleges	0.11	2
Lottery	0.04	2
School of Science and Math	0.20	3
OAH	0.03	2
OSBM	0.01	1
Sec. of State	0.13	3
Treasurer	0.10	1
Wildlife	0.15	1
State Agency Subtotal	34.01	357
Surveyed Universities, Fall 2007:		
Appalachian State	1.25	2
N.C. State University	1.50	5
UNC-Chapel Hill	1.50	5
UNC-Charlotte	1.25	2
UNC-Greensboro	1.25	4
Surveyed Campus Subtotal	6.75	18
*Above WC Grand Total	40.76	375

**Only Reflects Universities Surveyed in Study*

Chart 10 - Staffing Changes to OSP Workers' Compensation since 1996

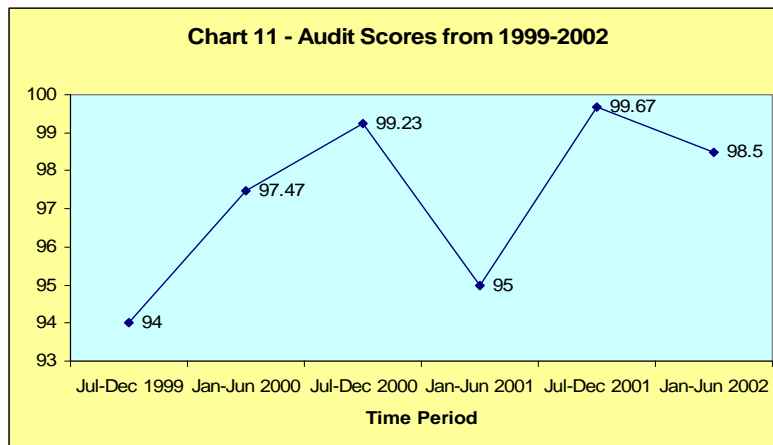
1996-2001	2001-2006	2006-2007	2007-2008
One (1) WC/Unemployment Insurance Coordinator position = (0.4 FTEs for WC)	One (1) WC/Unemployment Insurance Coordinator position = (0.4 FTEs for WC) . Position assigned additional "HR Generalist" duties.	One (1) HR Partner (WC & Unemployment Coordinator) position = (0.3 FTEs for WC) .	One (1) HR Partner (WC & Unemployment Coordinator) position = (0.25 FTEs for WC) . Duties expanded to other HR functions beyond WC and supervision of eight (8).
One (1) WC Analyst position = (1 FTE for WC) . Included contract oversight and audits.		One (1) WC/Unemployment Analyst position = (0.5 FTEs for WC) . Assigned for research, data maintenance; no audit role.	One (1) WC/Unemployment Analyst position = (0.5 FTEs for WC) . Assigned for research, data maintenance; no audit role.
One (1) WC Technician position = (1 FTE for WC) . Included WC database management.			
2.4 FTEs for WC	0.4 FTEs for WC	0.8 FTEs for WC	0.75 FTEs for WC

Key Risk Performance Audit/Survey Results

OSP has evaluated Key Risk’s performance either semi-annually or annually since TPA contracts began. Initially, from 1999-2002, OSP performed audits of Key Risk every six months. However, due to the reduction of OSP staffing for the WC Program and the amount of time it takes to audit the claims, the audits transitioned into surveys and were performed annually beginning with fiscal year 2002-03. The most recent survey covers fiscal year 2006-07.

In the initial OSP audits, agencies and universities were asked to report on specific objectives and targets from the contract, with explanatory comments and examples when needed.

OSP assigned each objective weighted points based on survey results from each agency/university. These points were converted to a score, with a possible range of 0 to 100. Chart 11 shows these scores. The general trend was upward, with an average score was 97.3. Based on specific agency/university comments, OSP pulled “problem” cases and examined them more closely, providing Key Risk with a list of specific problems.



From 2002-2007, OSP conducted annual surveys of Key Risk’s performance. The design of the surveys did not allow for the calculation of a numeric score. They simply note if specific requirements were met, with accompanying comments from agencies and universities.

Common complaints included frequent turnover of claim adjusters, inconsistent communication with some agencies, inaccurate medical payments, inaccuracies with salary continuation tracking and reporting, and cases sent to the AG’s office for litigation that were incomplete and/or not organized as requested. The most recent surveys indicate that Key Risk has attempted to address these issues, with at least some success, although the survey’s format does not allow for quantification along the lines of the earlier audits.

There has been no formal audit of the TPA or State's WC program since the OSP staffing changes of FY 2001-02. DPI is currently in the process of auditing the TPA separately, but those results are not yet complete. An audit of the State's program should reveal such information as:

- how the TPA's management of claims affects the State's WC costs;
- comparative cost information with other states;
- how the TPA's management of claims compares with the industry standard;
- how the TPA's case management service reduces the life of a claim and brings it to closure at the same rate as the industry standard;
- if the State's claims are closing at a normal rate for particular types of injuries;
- if the TPA is consistently complying with the AG's Office format requirements;
- how the TPA is performing as judged by experts in the field, rather than through case-by-case agency surveys.

Section Summary

Based on total costs and current organizational structures, using a TPA is still the most effective approach for agencies and universities. Using a TPA does not cost more than managing WC claims internally, and it likely costs less. In addition, the majority of agencies and universities are not prepared to take on the additional responsibility of administering WC claims internally.

However, claims administration with a TPA requires sufficient contract management, and the current oversight of the TPA's State contract is not sufficient. This has been mainly due to staffing changes that have taken place at OSP since 2001-02. Additional staff resources need to be dedicated to this program. It is also clear that no formal TPA audit has been completed in recent years. An audit is necessary to reveal how the State's program compares to other similar programs.

These conclusions are explored in more detail in the Conclusion/Recommendation section of this report.

EFFECTIVENESS OF CURRENT FUNDING METHOD

Task 2: Determine if the current method of funding is still the most effective method.

The State is self-insured, meaning that the State does not pay premiums to an insurance company for WC coverage. The State pays fixed costs for administrative fees, plus claims expenses. WC expenditures are paid from current agency or university operating budgets. According to the [State Budget Manual](#), Section 6.1.5, there are generally no appropriations to cover WC expenses. Each department, agency, or university is required to pay its claims out of its own appropriation. Agencies submit budget revisions to OSBM to transfer funds to cover these costs.

Agencies can set aside a certain dollar amount in their Certified Budgets, normally based on previous cost experience. Throughout the year, expenditures that exceed this budgeted amount are paid with lapsed salaries, adding a "pay as you go" element to WC expenses. For example, in FY 2006-07, the Department of Correction (DOC) Certified Budget for its Workers' Comp payment account was \$6,133,261. However, DOC's claims expense was \$15,889,107, which required that \$9,451,528 be paid from lapsed salaries.

The WC Fund

The current Workers' Compensation Fund utilizes a limited amount of WC expense planning. This fund, essentially a checking account, was created from initial deposits by agencies and universities equaling two months of average expenditures based on a three-year history of expenditures. The TPA draws from this fund to pay WC expenses on behalf of each agency/university, and the fund must be replenished at the end of each month to keep the current balance. The WC administrator must review the monthly report of claim expenditures for accuracy and send an approved copy to the agency fiscal officer. After this approval is received, monthly reimbursement to the WC Fund is made by the agency's fiscal office in the amount invoiced by OSC via an on-line transfer. Each fiscal year, OSC reviews the fund balances, and if the

current three-year average expenditure warrants, agencies may need to increase their fund balance (see Flowchart 4, Appendix B).

A criticism of this funding approach is that it is essentially pay-as-you-go. There is typically no formal, budgeted amount per agency, beyond the balances kept in the WC Fund, leading to a heavy reliance on lapsed salaries. The State's WC budgeting is inconsistent, and not every agency/university has a Certified Budget amount established in their Workers' Compensation payment account. Therefore, these institutions may run the risk of a significant expense requiring the use of lapsed salary or the potential delay of payments to settle a claim.

Impact of Lapsed Salary Usage

Most agencies and universities included in this study explained that lack of available funds in lapsed salaries or other budget lines did not prevent claims from being settled. But without a budgeted WC line, State institutions must identify funds to meet this requirement wherever they can find them.

Key Risk reports that the State's average cost per open claim in 2006 was \$8,947, while those remaining open since 2002 have an average cost of \$323,186. Excluding DPI or DOT, there are 310 State cases still open from 2002 or earlier. These cases are open because of ongoing litigation, multiple provider visits for second opinions, legal efforts that block an employee returning to work, or lack of available light-duty work. Since claims that remain open tend to be more expensive, agencies must work with the TPA to reach settlement and close claims and, where possible, return the employee to work.

In at least three cases, the TPA and the Department of Health and Human Services (DHHS) cited an inability to settle claims because of insufficient funds, lapsed salary or otherwise. The three cases are located within the Division of Mental Health (DMH) budget code, and total more than \$1 million in WC medical payments, excluding WC disability payments. DMH reports that the division periodically may wait for additional patient revenue before closing a claim, depending on the size of settlements. If sufficient funds are unavailable at the division level, DHHS may authorize the transfer of funds from another division to cover DMH claims, although the preference is for each division to cover expenses with its own resources.

All agencies and universities contacted for this study raised concerns about the ongoing use of lapsed salary for WC expenses in light of the rising costs of WC settlements and healthcare in general. The cost per WC claim continues to rise, in North Carolina and nationwide, and in both the public and private sectors. This rising cost creates an ever-increasing liability that remains unfunded in most agencies and universities.

Agency Set-Asides and Payroll Additives

Some agencies and universities have created other ways of budgeting for WC expenses. DOT budgets an annual payroll additive⁷ that provides funds for all WC expenses.⁸ This additive is similar to additives used for budgeting Social Security, Retirement, and other related expenses as an agency-funded percent of payroll. It is adjusted annually based on the prior year's expenses and the estimated rate of inflation. Funds from the additive have been sufficient to cover all WC expenses in each fiscal year, including settlements.

Budgeting for WC

Agencies and universities could budget for WC expenses as part of the biennial budget process.

Advantages of Budgeting for WC through the Budget Process:

1. ***Consistent applications*** – Agencies would budget an established amount based on claims experience for a two-year period. The current WC Fund consists of a two-month supply per agency based on a three-year average. Biennial budgeting would allow for more accurate expense forecasting. If planned well, agencies would not need to rely as heavily on lapsed salaries to cover deficits. The existing WC Fund would still have a role in the accounting structure for daily release

⁷ DOT's payroll additive for FY 2007-08 is 1.8433%.

⁸ Similarly, NCSU and UNC-CH budget for a fringe benefit or set-aside pool, a portion of which covers WC expenses.

to cover WC payments (Flowchart 4). When agencies have to replenish the amounts at the end of the month, they could take it from the budgeted account, following the existing process.

2. ***Increased accountability with WC expenses*** – Budgeting for WC would require agencies to forecast expenses for the two-year period. Site visits to agencies and universities demonstrated a trend that many of these institutions pay less attention to expenses when there is no formal budgeted line item. Lapsed salaries are viewed as a financial firewall. When there is sufficient lapsed salary to cover costs, agencies and universities may not track these expenses closely. Since the State is liable for WC benefits for the amount of the employee’s salary that derives from State funds, positions covered by non-State funds (such as grants) tend to get more attention; the additional funding must be located at some other source. Budgeted lines would increase the scrutiny by agency budget officers and OSBM because planning for expenses and not reacting to costs would be required.
3. ***Less reliance on lapsed salaries*** – The Legislature has requested more analysis of the use of agency lapsed salary funds. With a two-year budgeted amount for this purpose, there would be less need to use lapsed salaries. Lapsed salaries are often necessary for other expenses, such as overtime and shift premiums.

Disadvantages of Budgeting for WC through the Budget Process:

1. ***Initial cost*** – Agencies and universities are not accustomed to budgeting based on two years of WC expenses. Even most of those who have amounts set aside in Certified Budget lines consistently need to access lapsed salary funds because of shortfalls. The current WC Fund requires a two-month balance based on three years’ average expense history. Costs will need to be shifted in the initial stages to reflect the higher amount needed. Using DOC’s example from above, this could mean increasing the annual WC budget from \$6,133,261 to \$15,889,107. However, since the State is already paying this expense through the year with lapsed salaries, the expense should even out over time. Any unused amount would revert to the General Fund unless otherwise designated as a WC reserve.
2. ***Risk that unused funds will be used for another purpose*** – Some agencies have expressed concern that if any amounts are left over in a WC line item, they would be seized during the budget development process for some other purpose, or during a time of statewide budget shortfall. While this is not an unfounded concern, proper financial forecasting to achieve a break-even point should help avoid this issue. All appropriated funds are subject to this risk.

Long-Term Liability

Considering the traditional pay-as-you-go approach to WC expenses, there has been little analysis of the State’s long-term liability. This study has already acknowledged the importance of budgeting for WC costs. The next step is to understand what the long-term liabilities are through an actuarial valuation.

There has been significant attention to the long-term costs of retiree health benefits. Session Law 2007-467/HB 1529 established the Committee on Actuarial Valuation of Retired Employees’ Health Benefits. The committee’s primary goal is to conduct an annual actuarial valuation of State-supported retired employees’ health benefits under other post-employment benefits (OPEB) accounting standards set forth by the Governmental Accounting Standards Board (GASB). Although this law did not include WC liabilities as part of the valuation, the rising costs of WC may become a future area of concern worthy of a separate actuarial study.

Section Summary

The current funding method is outdated. WC expenses are increasing and agencies/universities need a better planning tool for these costs. By budgeting for WC expenses through the biennial budget process, State agencies and universities would engage in better forecasting. An alternative approach is to allow agencies and universities to experiment with a payroll additive to set aside funding for these costs.

However, the payroll additive may be seen as supplementary, and not as a substitute for two-year budget forecasting.

These conclusions are explored in more detail in the Conclusion/Recommendation section of this report.

NECESSITY OF EXCESS COVERAGE POLICIES

Task 3: Determine whether excess coverage policies are needed.

Why the Expressed Need?

According to the [State Budget Manual](#), Section 6.1.6, the use of State-appropriated funds or other public funds to purchase WC insurance from private insurance carriers is an inappropriate use of these funds and is not authorized unless otherwise approved by OSBM.

However, some agencies and universities have expressed interest in excess insurance or stop-loss coverage⁹ for catastrophic WC claims. UNC-Charlotte experienced a catastrophic WC claim in the spring of 2006 when an employee suffered severe burns from an explosion. The employee ultimately died as a result of his injuries. The total WC claim from that incident was \$1,398,769. If the explosion had occurred a few minutes earlier, other workers at the scene would have been severely injured as well, and the human and financial loss would have been much worse.

Since WC payments come directly from agency and university operating budgets, catastrophic claims, while unusual and uncommon, immediately place severe financial hardship on agencies and universities. Smaller entities, by nature of their smaller budgets, are particularly vulnerable during unexpected losses. The longer a claim remains open, the larger the overall payout is when the claim is ultimately settled.

Complicating matters, the WC field as a whole is constantly evolving, leading to increasing uncertainty in WC claim costs. The legal and regulatory environment is always changing with new decisions coming from the courts and the NCIC. Perhaps most importantly, the cost of medical care continues to rise faster than the rate of inflation.

State WC Trust Fund

The Department of Insurance (DOI) and the North Carolina Association of Insurance Agents (NCAIA) have discussed with OSBM and OSP a possible alternative to the existing WC structure. The result is an outline for creating a State WC Trust Fund.

Based on the State's loss experience, any purchase of commercial insurance should be "loss sensitive." This includes, but is not limited to excess coverage and/or annual aggregate stop-loss insurance coverage. In order for any of these plans to proceed, an insurance trust is mandatory. Otherwise an insurance carrier is highly unlikely to participate due to a perceived lack of financial stability.

The intent would be to use agencies already involved in the WC program, including OSP, OSC, AG, OSBM, Office of the State Treasurer, and the TPA. The Trust, once created, would be under the care, custody, and control of the State Treasurer. The Trust would be funded by invoicing State agencies based on permanent position count, regardless of funding source, as provided by OSP and UNC General Administration. The position counts include both general and specially funded positions. The Trust would have the following features:

⁹ *Excess insurance*: WC coverage above a specified expenditure level. For example, the specified expenditure level is \$100,000 and the excess insurance is \$1 million. After the losses exceed \$100,000, the excess insurance will pay for the losses up to a total of \$1 million. *Aggregate stop-loss insurance*: This coverage would be initiated when the State's total group of WC claims reached a stipulated threshold selected by the State. Typically, this threshold is 125% of the annual estimated group WC claim costs. The policy would pay claims up to any lifetime limit per employee.

- **Premiums** – Each agency and university would pay a premium based on several factors. Premiums paid would be non-reverting and could not be seized/utilized for another purpose (benefits from WC claims can go on for years).
- **Retention** – Each agency and university would have a minimum retention (deductible). The retention may vary from agency to agency and there may be an annual stop-loss on agencies’ retention.
- **Claims** – The Trust would pay \$1,000,000 of the final resolution (benefit) of a claim. Settlement authority would be at the State level, instead of the agency/university level as it stands currently. Attorney fees are not included under the current assumptions. Once a claim is paid, the agency or university would reimburse the Trust for its deductible.
- **Excess Insurance** – The purchase of excess insurance (annual aggregate or per claim stop-loss) is designed to (1) protect the Trust and agencies from catastrophic claims (in excess of \$1,000,000) and (2) stabilize the rate structure to State agencies. Commercial insurance carriers are not willing to provide insurance coverage to an unfunded or post-funded self-insurance program.

A WC Trust Fund could convert what is primarily an unbudgeted and unmanageable expense into a budgeted and manageable expense. The cost of the program would be based on an actuarial determination of loss reserves, cost of excess insurance, and administrative costs for claims administration. Each participating agency and university would pay into the Trust Fund based on its proportionate share. This proportionate share would be determined by classification of various job types, payroll, or number of positions and deductible amount.

Section Summary

Excess insurance may be an item for future consideration, but the State is not currently set up for it, nor is there a consistent need. Purchase of excess insurance would entail establishing a WC Trust Fund before a private insurer would provide coverage. Since there is not an established need for catastrophic coverage beyond isolated incidents, there is little justification for purchasing excess insurance at this time.

These conclusions are explored in more detail in the Conclusion/Recommendation section of this report.

OTHER OPERATIONAL INEFFICIENCIES

Task 4: Identify any other operational inefficiency in program operations that might exist.

Safety Office v. Human Resources

When an employee is injured on the job, numerous systems, agencies, and individuals are affected. In addition to the employee and his/her immediate supervisor, a WC case may also involve the TPA, human resources, risk management, the Occupational Safety and Health Administration (OSHA), the AG’s office, other attorneys, the NCIC, physicians, hospitals, the N.C. Retirement System, and the court system.

Efficient resolution of WC cases therefore requires all of these entities to coordinate and work together to the greatest extent possible.

This study involved asking each agency and university where its WC function was located, and why. Interviews with the agencies and universities revealed that with one exception, the WC function is placed in either the Safety office or Human Resources (HR) as shown in Chart 12.

At least three of the agencies and universities that placed their WC function in HR reported communication difficulties between the HR and Safety

**WC is within Safety, but Safety itself is within HR*
***WC part of the Insurance section, so it's not Safety or HR*

Chart 12 – Location of WC Unit

Agency or University	Safety or HR
Administrative Office of the Courts	Safety*
Department of Agriculture	Safety*
Department of Correction	HR
Department of Health and Human Services	HR
Department of Insurance	HR
Department of Public Instruction	Neither**
Department of Transportation	Safety
Appalachian State University	Safety
North Carolina State University	HR
University of North Carolina at Chapel Hill	Safety
University of North Carolina at Charlotte	Safety
University of North Carolina at Greensboro	HR

offices. Agencies and universities that placed their WC function in Safety indicated more seamless communication with risk management functions and OSHA reporting forms and requirements. A likely reason is that Safety offices typically include risk management and OSHA functions; therefore those that also include a WC function have coordination and communication practices in place and well established.

WC/Disability/Retirement Interaction

Analysis of the State's WC program would be incomplete without a reference to the interaction between WC benefits and the N.C. Retirement System Division's (RSD) disability programs.

With Short-Term Disability, a recipient's monthly benefit amount is reduced by any monthly WC payments received, with the exception of permanent, partial WC awards, which compensate employees for the permanent loss of or damage to a part of the body. Agencies/universities pay the benefit, and the RSD reimburses the agency. State agencies and universities inform the RSD that an employee is receiving WC benefits. There are opportunities for miscommunications in the process, but the RSD reports that it works reasonably well.

For an employee to transition to Long-Term Disability, normally after completing the requirements for Short-Term Disability, the agency and employee must apply with the RSD. Applicants for Long-Term Disability must request to receive these benefits within 180 days after monthly WC payments cease.¹⁰ Additionally, the Medical Board must approve the request. Upon approval, employment is terminated and WC benefits cease, with the exception of permanent, partial disability.

The State may consider streamlining this process, so that oversight of WC and disability falls under one umbrella agency. Aspects of streamlining the process under one agency could include:

- Employers informing a central agency of cases where an employee has been on sick leave for a certain length of time, such as seven days. The case would receive a case manager, to make three-point contact with employee, employer, and medical provider to determine the best course of action.
- A central agency computer system to track information such as physician paperwork, absence days, and WC payments.
- The central agency providing RSD with reports of reimbursement amounts needed for Short-Term Disability. The RSD could audit these cases and verify if they should be reimbursed.
- The central agency could send a monthly report to RSD with all employees on Long-Term Disability. While the RSD could ensure that the recipients were paid, the central agency could continue to monitor their cases, help apply for Social Security, reduce payments for the Social Security offset, and inform the RSD to stop benefits when appropriate.

These are some possible steps that could be taken if WC and disability functions were consolidated under one agency. Analysts for this study were not able to take a more comprehensive look at these systems because of time constraints. But if an umbrella agency approach is considered, a further study should be conducted to consider what aspects could be included and what agency is the most appropriate to oversee WC and disability.

Lessons from Other States

North Carolina differs from neighboring states in that the State does not have a cap on the length of time that benefits can be paid. Virginia and South Carolina, for example, cap benefits at 500 weeks; Georgia caps them at 400 weeks. North Carolina law provides for indemnity benefits to continue until return to work, or past retirement age and until death.

There are 310 non-DOT, non-DPI State claims open from incidents that occurred prior to 2002. Of the WC expenses paid in FY 2006-07, only about 18% were for claims that were incurred during that 12-month

¹⁰ See [Teachers' and State Employees' Retirement System Handbook](#) from the Office of the State Treasurer.

period. Even a 500-week cap would allow a claim to stay open without settlement for more than nine years, but would establish a boundary of when the claim must be settled.

In 2005, Senate Bill 984 proposed a 500-week cap on the duration of benefits; the bill did not advance and received significant public resistance. Although this is an issue that goes beyond administrative matters, it has a bearing on the administration of the program and is worth mentioning in this report.

Section Summary

OSBM was able to find some areas that represent either an inefficiency or deserving of future study. Agencies and universities may wish to explore the location of their WC function, since those with WC administered by a Safety Office have a more consistent relationship with risk management and OSHA reporting requirements. WC and disability benefits could be better integrated, perhaps even under the same agency to reduce miscommunication and processing errors. The State should also reconsider placing a cap on the duration of WC benefits to limit future liabilities.

These conclusions are explored in more detail in the Conclusion/Recommendation section below.

CONCLUSIONS AND RECOMMENDATIONS

This report groups recommendations under the categories stated in Section 23.3 of Session Law HB1473:

Determine if Third Party Administration (TPA) of the program continues to be the most effective mode of administration: With sufficient contract management, TPA is the most effective mode of administration.

- Based on total costs and current organizational structures, using a TPA is still the most effective approach for agencies and universities. Using a TPA does not cost more than managing WC claims internally, and it likely costs less.
- Currently, the majority of State agencies and universities are ill-equipped to assume the additional responsibility of WC administration without a significant increase in staffing and training exclusively for the WC function. Although DPI has prepared a case for internal management without a TPA, that agency would still need to invest in 13 more FTEs for the WC function. Other agencies could face a proportional increase if they are expected to pay claims and manage cases.
- In most cases, State agencies and universities are not prepared to develop provider networks that could help reduce charges and provide the best service to employees. If this were to be developed, it should be done in conjunction with the State Health Plan provider networks.
- OSP does not allocate sufficient FTEs toward TPA contract management. Although contract management of the DPI program appears sufficient, OSP staffing of the WC Program has decreased over the years. The Program's auditing role has nearly disappeared since 2002, confined only to an annual, informal satisfaction survey of WC administrators and case-by-case reactive adjustments. OSP should increase its WC staffing to pre-2002 levels, including the reallocation of a position to serve in this auditing role. The current State contract expires in June 2008, with the option to extend the contract to June 2009. At the appropriate time, OSP should negotiate contract terms to be more consistent with DPI's current terminology and rate structure where possible.
- OSP should authorize an annual or biennial audit of the State's WC TPA. This study provides an introduction to TPA practices, but does not yield information about how the TPA's claims management compares with industry standards, if the State's claims are closing at a normal rate for particular injuries, or how North Carolina compares with other states at the claims management level. DPI is currently in the process of auditing its WC Program. The findings of that audit may be helpful for the State in developing its audit approach.

Determine if the current method of funding is still the most effective method: It is not, because agencies and universities do not adequately budget for WC costs on a consistent basis through the biennial budget development process.

- Agencies and universities should budget for WC expenses as part of the biennial budget process. While some agencies set aside certain amounts in their Certified Budgets, expenses can often exceed these amounts. Establishing a projected two-year WC amount in the budget process would help agencies and universities better anticipate their needs, rely less on lapsed salaries, and enable agency and OSBM budget analysts track WC costs more accurately. Ideally, unspent funds would not revert at the end of the biennium, but would accumulate as a reserve for future WC liabilities. Such a reserve would lessen reliance on lapsed salaries, as WC expenses fluctuate year to year and are unpredictable. The existing WC Fund would still serve a role as a checking and disbursement account with a minimal amount on reserve.
- In lieu of budgeting for WC through the biennial process, State agencies and universities should study the feasibility of payroll additives or set-asides, similar to additives used to budget FICA and retirement costs. As exemplified by DOT and N.C. State University, the additive amount is adjusted annually based on inflation and prior year's expenses. Additives can often cover an agency's WC expenses, but may be more beneficial for larger agencies and universities than small ones, as larger agencies could generate more funds with their larger payrolls.
- Since the State's long-term WC liabilities are largely undefined, the General Assembly should consider authorizing an actuarial valuation of this liability.

Determine whether excess coverage policies are needed: Based on current available data, excess coverage policies are not justifiable.

- The State has experienced a few cases of catastrophic loss, such as at UNC-Charlotte. However, these cases are infrequent. In order for an insurance company to provide coverage, it would need actuarial data that currently does not exist.
- Private insurers would not likely be attracted to a program without a WC Trust Fund. To the insurer, a trust fund lends a sense of financial stability. Each participating State agency would pay a premium based on a proportionate share. There could be considerable resistance from smaller State agencies who would not benefit from being in the same pool as larger agencies with heavier risk.

Identify any other operational inefficiency in program operations that might exist: There are several areas worth exploring:

- Agencies and universities should assess where their WC function is, and when appropriate, consider moving it from a human resource to a safety function. Agency and university WC programs that operate under safety leadership illustrated more seamless communication with risk management functions and OSHA reporting forms and requirements.
- The State should authorize a study on the impact of combining WC program oversight and State disability retirement under one umbrella agency. Such an agency could provide a central database of connected cases and may better serve employees who must migrate between WC and short-term or long-term disability.
- The General Assembly should reconsider setting at least a 500-week cap on duration of benefits, similar to that imposed by other neighboring states. Such a cap would set an outer limit on duration of benefits (not dollars) and require settlement of outstanding claims within 10 years – with an inevitable impact on reducing administrative and claims costs.

- Local Education Agencies (LEAs) should be brought under State Return-to-Work policy more consistently. Many LEAs (local public schools) have a return-to-work policy that mirrors the State's policy.¹¹ However, not all LEAs have their own policy. This is a potential area of inefficiency that should be addressed either as a result of this study, or come to light in the current DPI audit. If an LEA does not have its own return-to-work policy, it should be required to follow the State policy.
- Agencies and universities should encourage WC administrators to schedule regular discussions with the TPA to foster and enhance communication. Some agencies already observe this practice. UNC-Chapel Hill, for example, conducts weekly conference calls with the TPA to discuss outstanding claims. Although reliant on a competent adjuster, the result has been more frequent communication with Key Risk and identification of trouble areas that could develop into more expensive claims. Agencies and universities are in a position to demand this level of service from their TPA.

ACKNOWLEDGMENTS

OSBM wishes to acknowledge the staff and management of OSP, OSC, and the N.C. Department of State Treasurer, Retirement Systems Division, for their analysis and contributions to this study. Also providing valuable information through site visits and data were: the Administrative Office of the Courts, Appalachian State University, the Attorney General's Office, Department of Agriculture, Department of Correction, Department of Health and Human Services, Department of Insurance, Department of Public Instruction, Department of Transportation, N.C. State University, UNC-Chapel Hill, UNC-Charlotte, UNC General Administration, and UNC-Greensboro.

¹¹ See *State Personnel Manual*, Section 6, page 9.

APPENDIX A

Medical Benefits

Payments of all medical, surgical, hospital, nursing, sick travel, prescription drugs, and rehabilitation services that are prescribed by the treating physician to effect a cure of the injury are covered. Payments of all medical services are subject to the fee schedule established by the North Carolina Industrial Commission.

Disability Compensation

Compensation will be paid for several different types of disability resulting from a work-related injury or illness. The employee's average weekly wage will be used to determine the weekly compensation rate. Following is a brief explanation of this terminology:

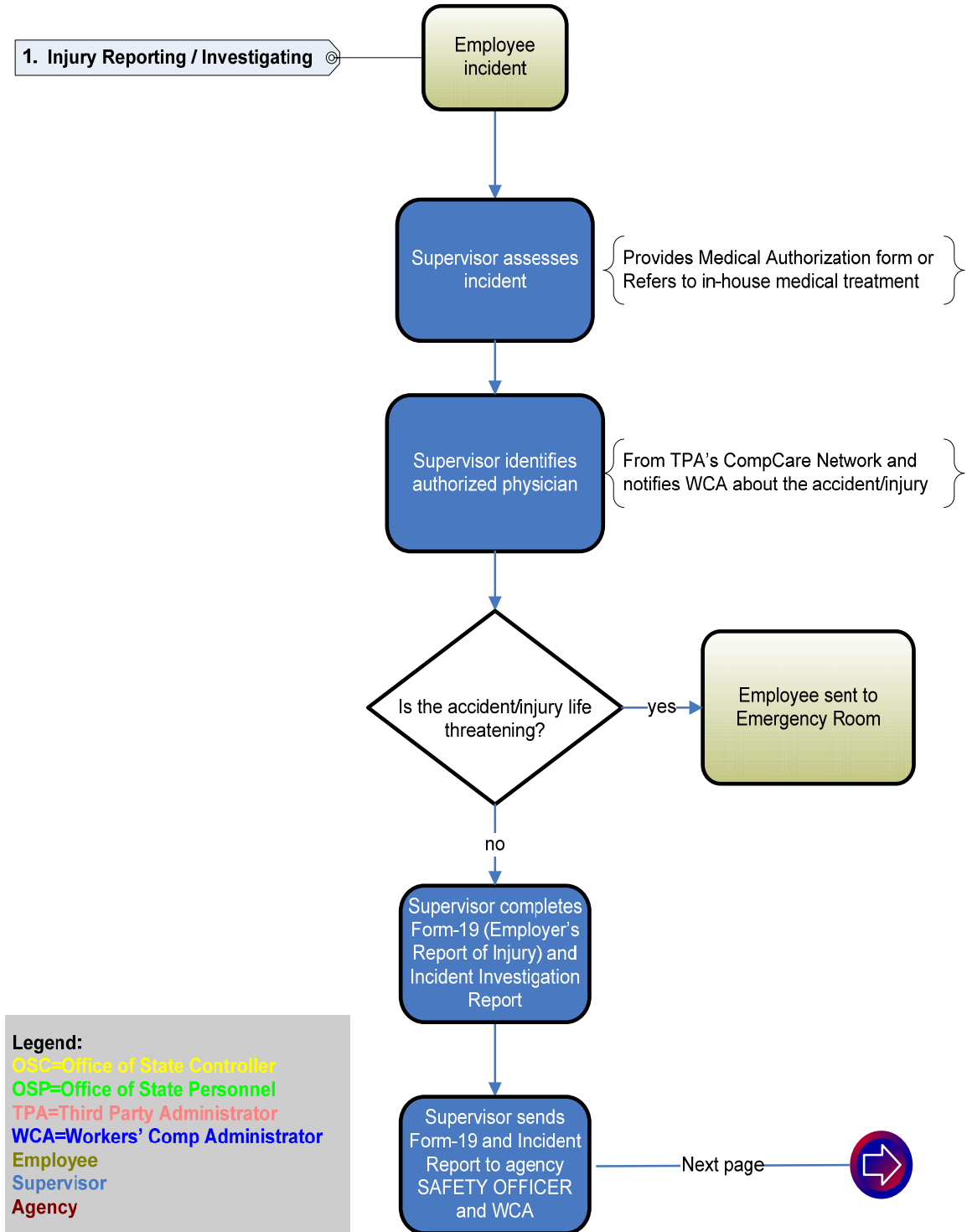
Average Weekly Wage: Any compensation paid under the Act is based on the average weekly wage earned by the employee. The average weekly wage is computed by adding all wages earned by the employee in the employment in which injured, including any special allowances, during the 52 week period prior to the injury. This total is divided by 52 to arrive at the average weekly wage. (See Workers' Compensation Act G.S. 97-2:5).

Compensation Rate: The compensation rate for total and partial incapacity is equal to sixty-six and two thirds percent (66 2/3%) of the average weekly wage subject to a minimum and maximum amount established annually by the North Carolina Industrial Commission.

Waiting Period: Under the Act there is a waiting period before an employee can begin to draw compensation for time lost from work due to the injury. An employee is entitled to no compensation for the first seven calendar days of disability unless the disability continues for more than twenty-one days. These twenty-one days do not have to be consecutive and any workday in which the injured employee does not earn his full wages because of the injury is counted as a day of disability. Note that State Personnel Policy states that if an employee chooses to use leave for the waiting week, it will not be reinstated in the event workers' compensation becomes due for the same week.

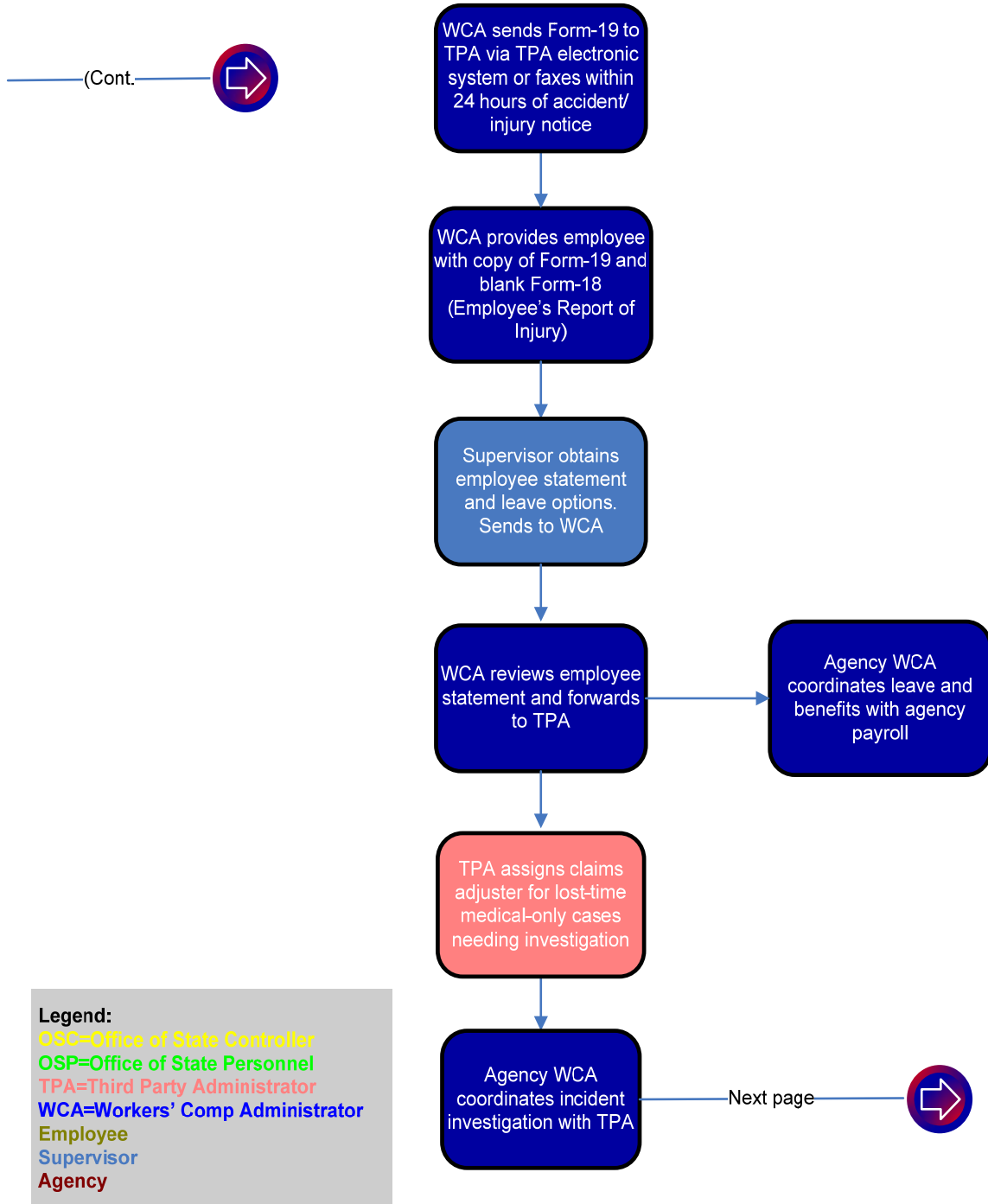
APPENDIX B: Flowchart 1 (page 1 of 3)

WC CLAIM PROCESSING: AN AGENCY'S PERSPECTIVE



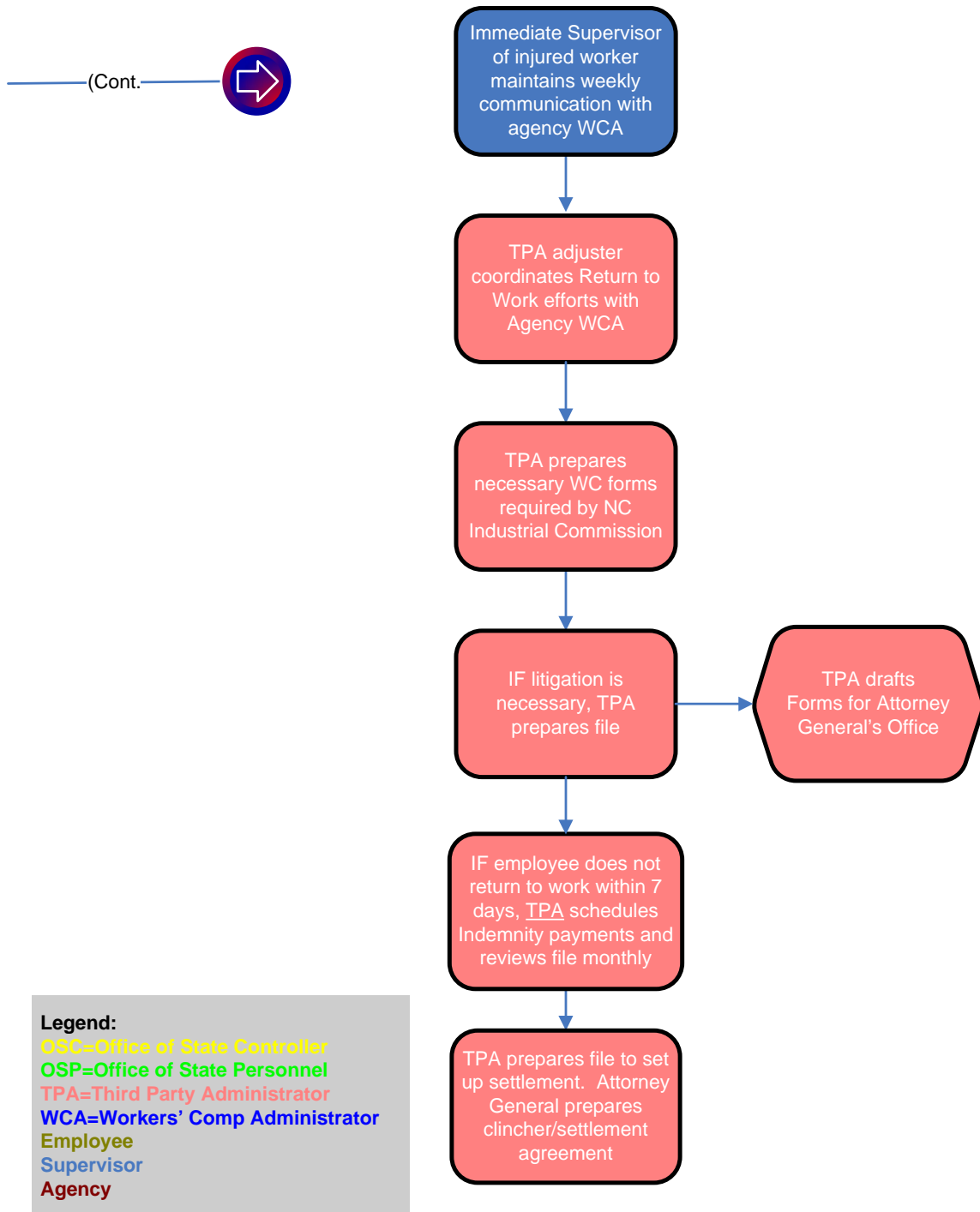
APPENDIX B: Flowchart 1 (page 2 of 3)

WC CLAIM PROCESSING: AN AGENCY'S PERSPECTIVE



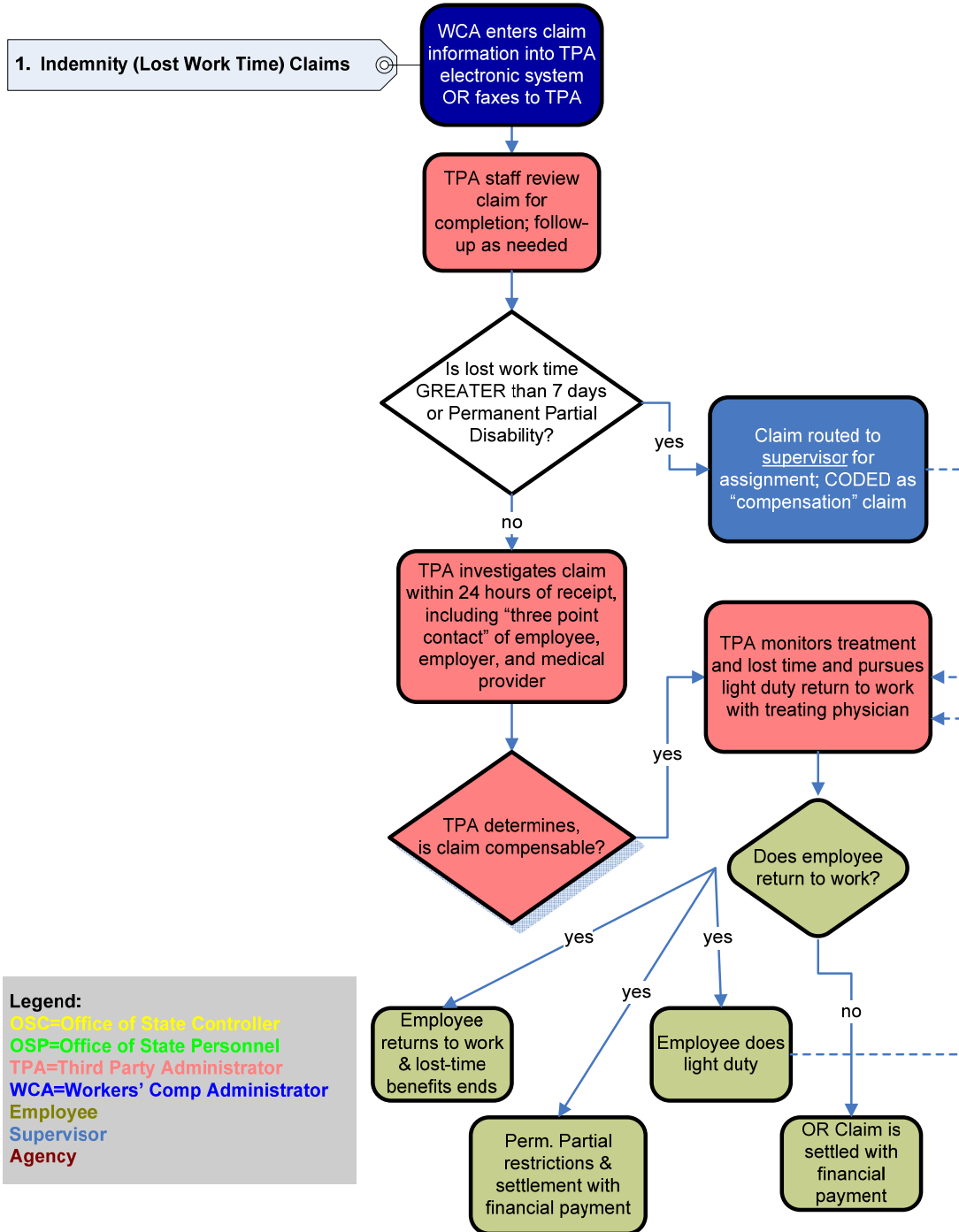
APPENDIX B: Flowchart 1 (page 3 of 3)

WC CLAIM PROCESSING: AN AGENCY'S PERSPECTIVE



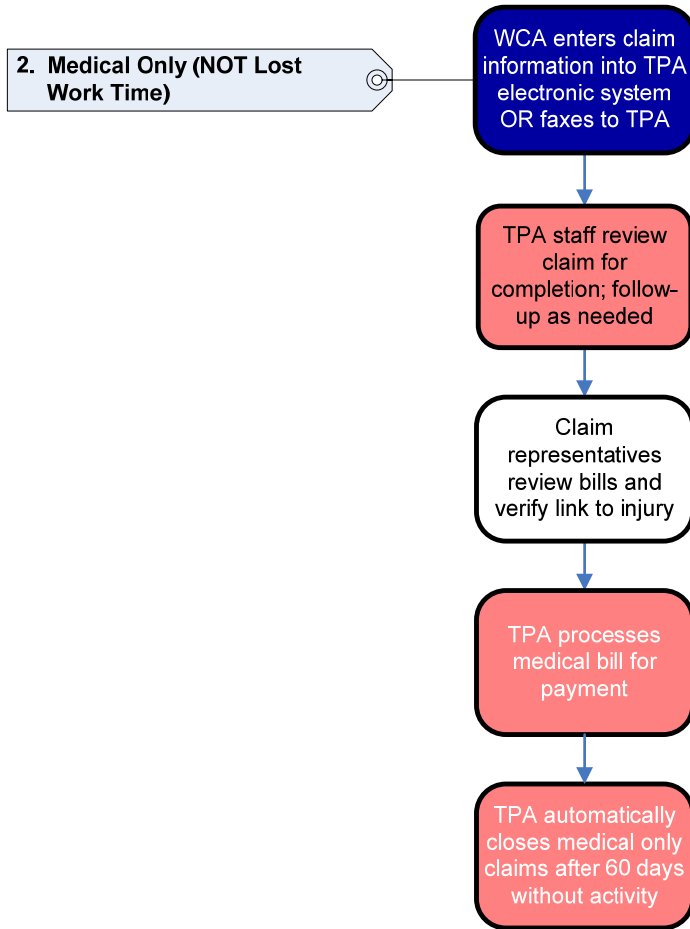
APPENDIX B: Flowchart 2 (page 1 of 2)

WC CLAIM PROCESSING: TPA'S PERSPECTIVE



APPENDIX B: Flowchart 2 (page 2 of 2)

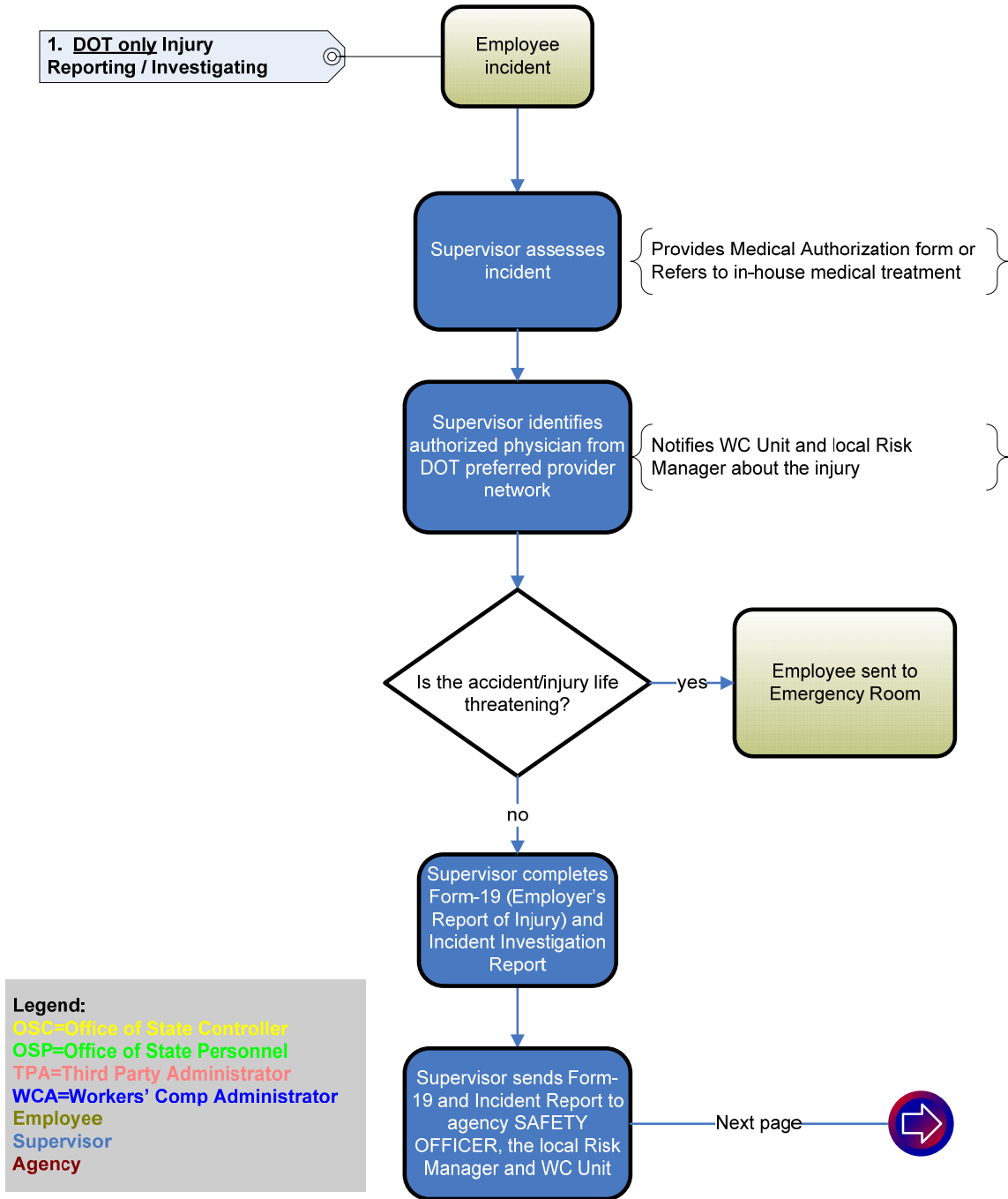
WC CLAIM PROCESSING: TPA'S PERSPECTIVE



Legend:
OSC=Office of State Controller
OSP=Office of State Personnel
TPA=Third Party Administrator
WCA=Workers' Comp Administrator
Employee
Supervisor
Agency

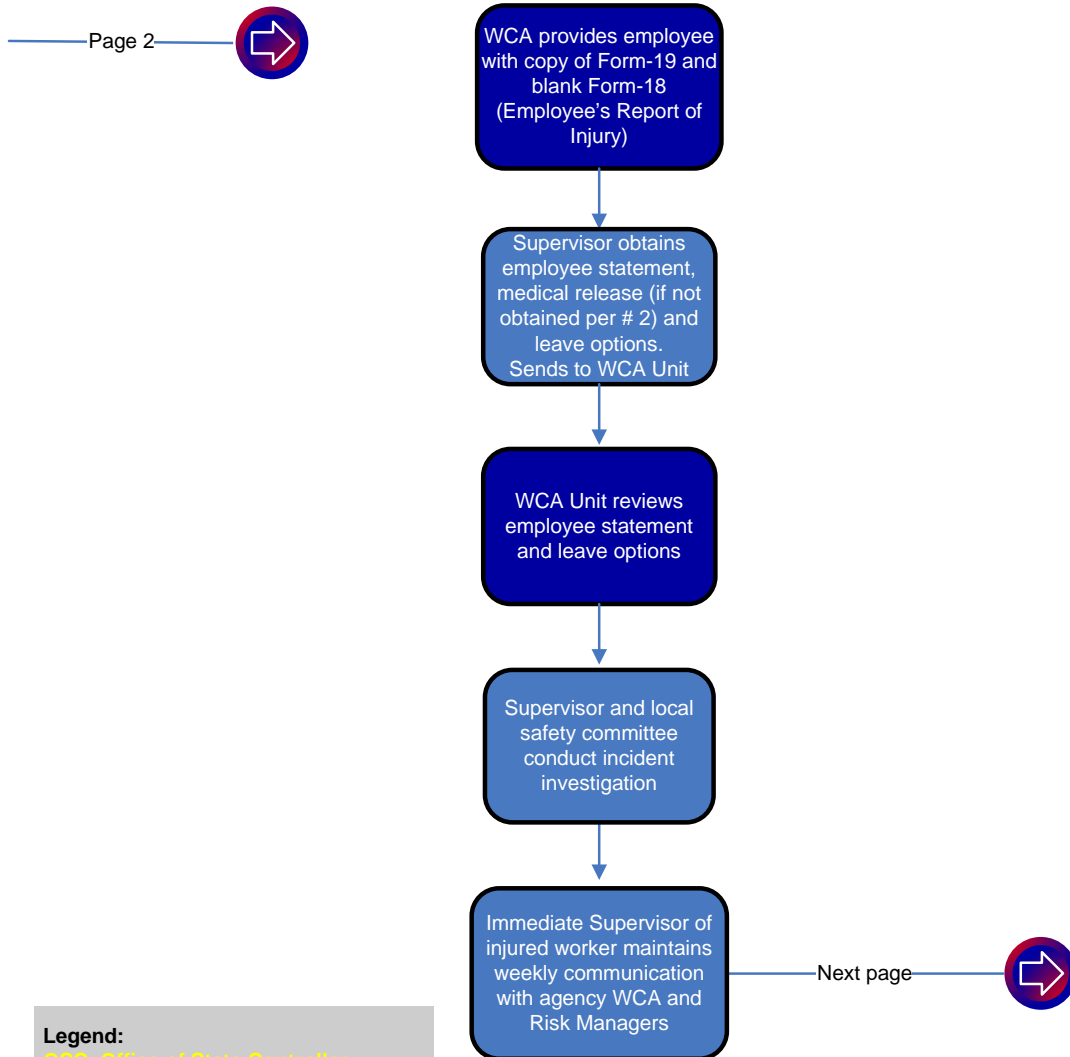
APPENDIX B: Flowchart 3 (page 1 of 3)


WC CLAIM PROCESSING: DOT




APPENDIX B: Flowchart 3 (page 2 of 3)

WC CLAIM PROCESSING: DOT



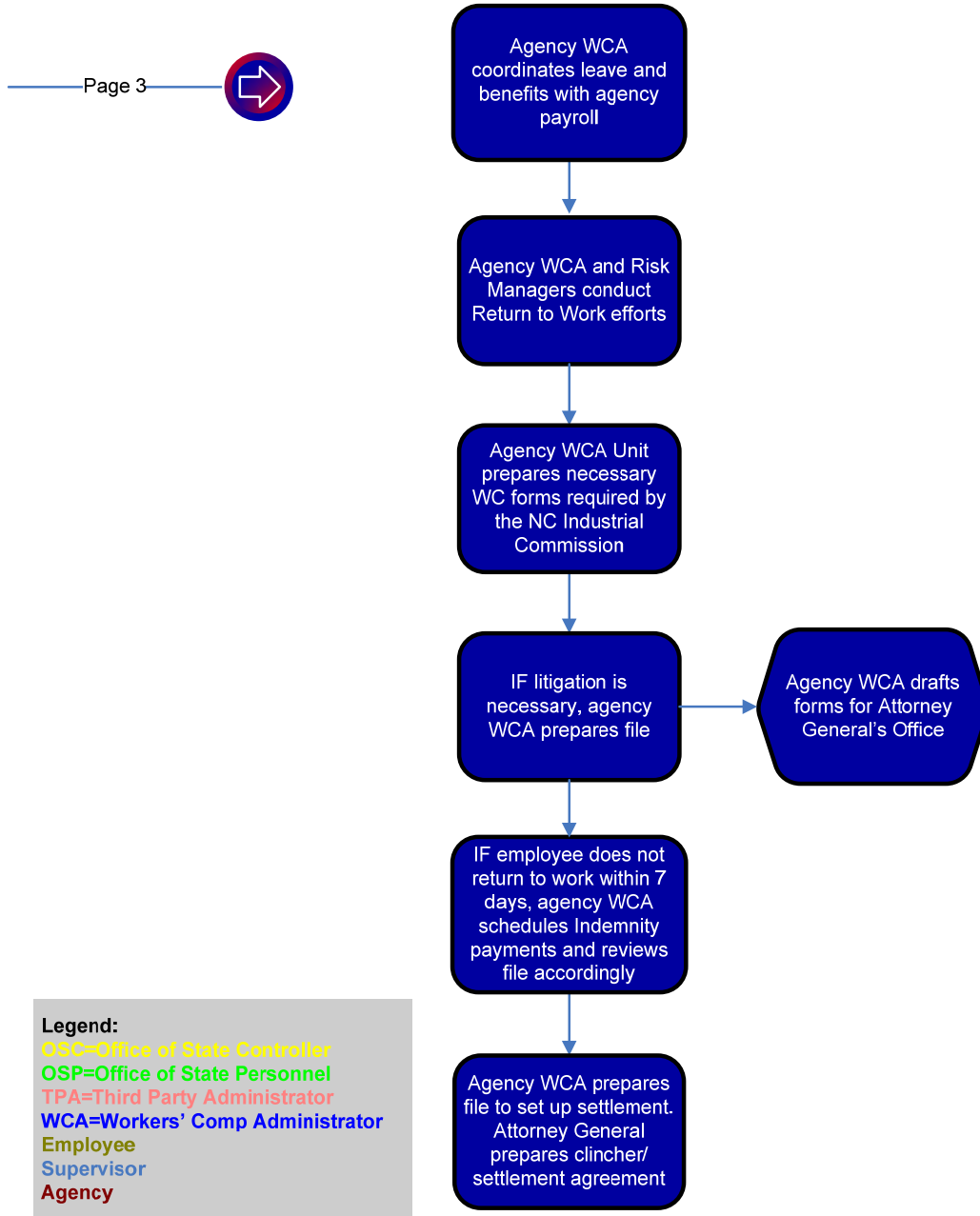
Page 2 

Next page 

Legend:
OSC=Office of State Controller
OSP=Office of State Personnel
TPA=Third Party Administrator
WCA=Workers' Comp Administrator
Employee
Supervisor
Agency

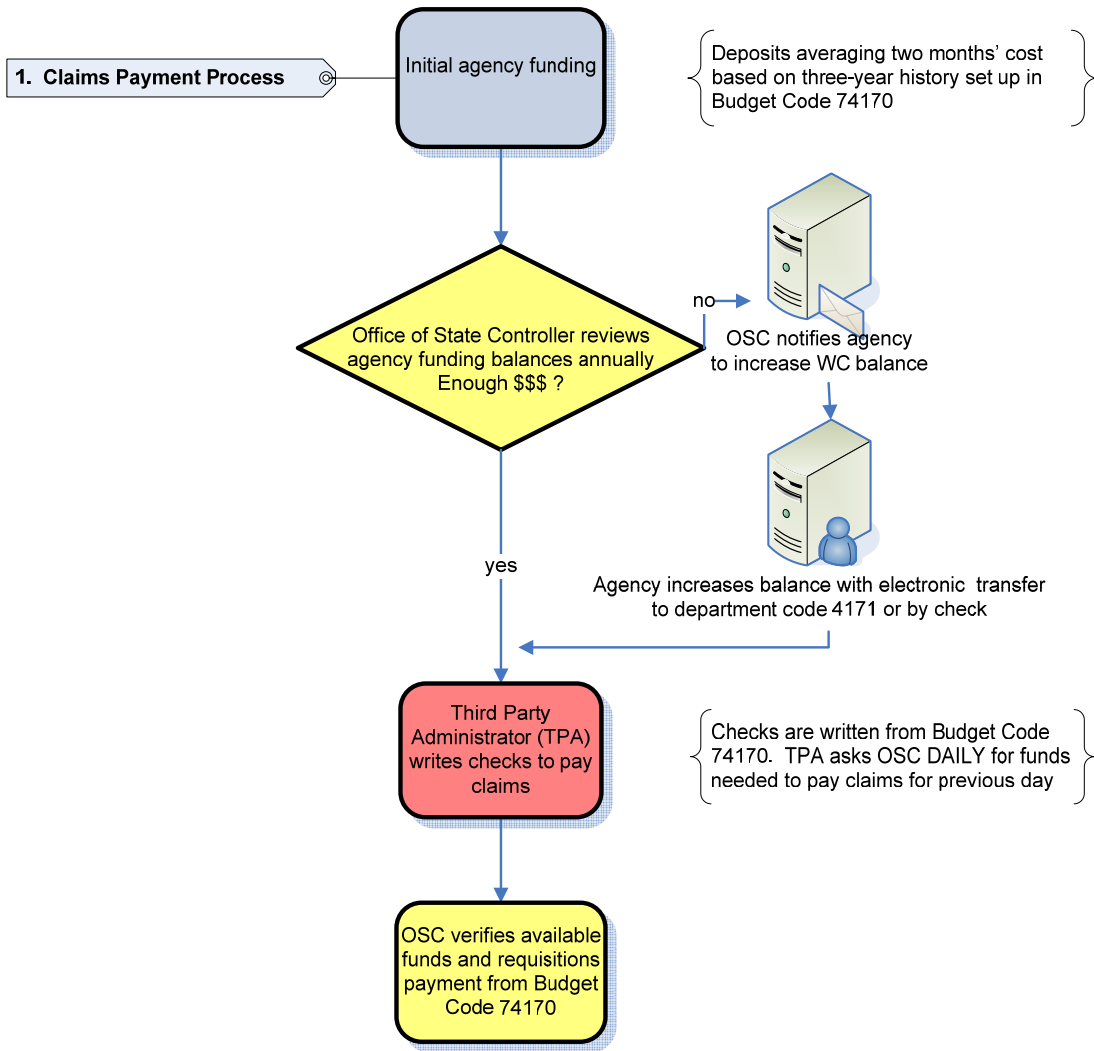
APPENDIX B: Flowchart 3 (page 3 of 3)

WC CLAIM PROCESSING: DOT




APPENDIX B: Flowchart 4 (page 1 of 3)

WC FUNDING

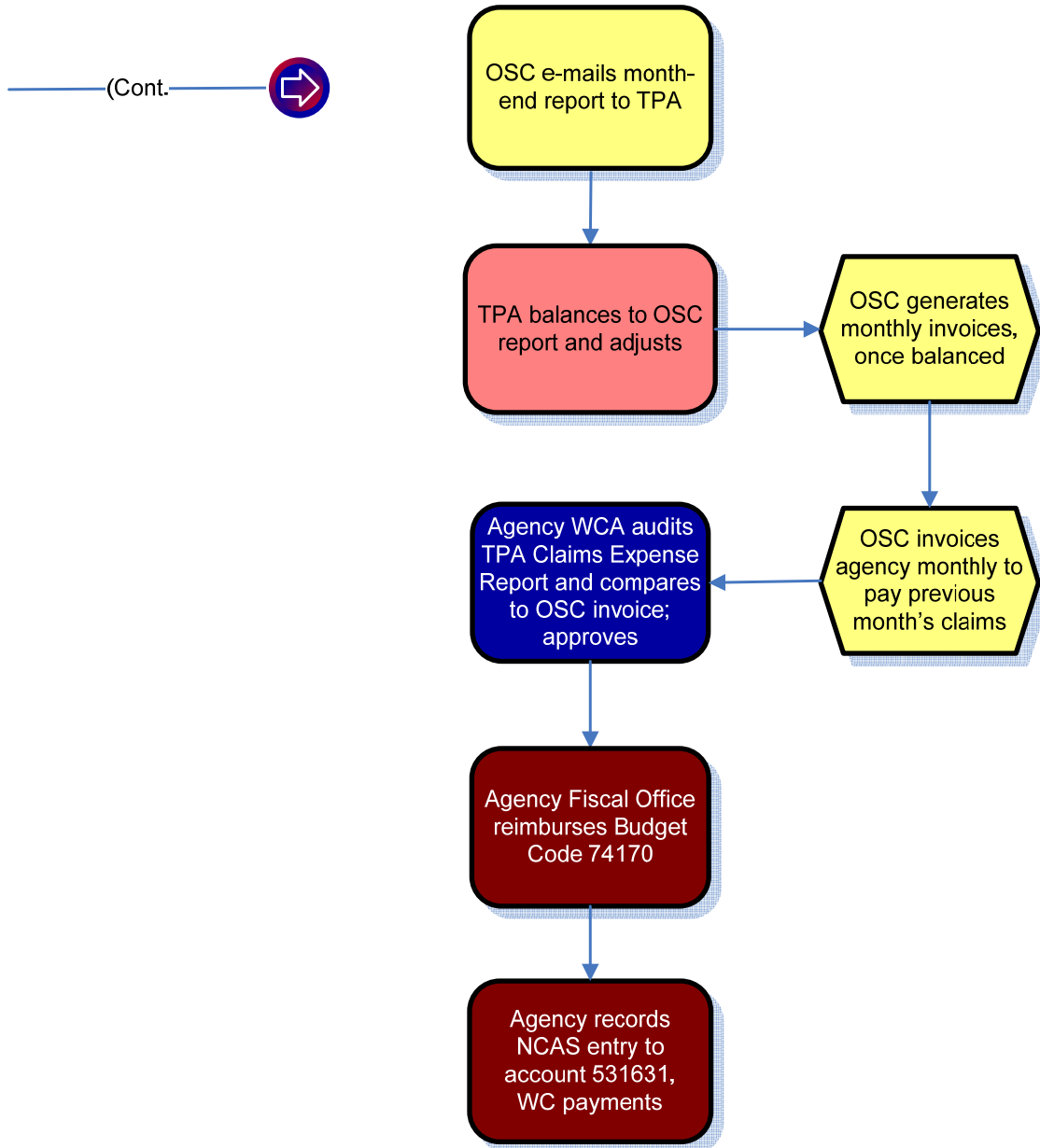


Legend:
 OSC=Office of State Controller
 OSP=Office of State Personnel
 TPA=Third Party Administrator
 WCA=Workers' Comp Administrator
 Employee
 Supervisor
 Agency

Next page 

APPENDIX B: Flowchart 4 (page 2 of 3)

WC FUNDING



Legend:
OSC=Office of State Controller
OSP=Office of State Personnel
TPA=Third Party Administrator
WCA=Workers' Comp Administrator
Employee
Supervisor
Agency

APPENDIX B: Flowchart 4 (page 3 of 3)

WC FUNDING

