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**FINANCE AND BUDGET COMMITTEE
FEBRUARY 14, 2007**

SUBJECT: WORKERS' COMPENSATION ADMINISTRATION

**ACTION: ADD 14 FTEs TO THE RISK MANAGEMENT FY07 BUDGET AND
AUTHORIZE NEGOTIATION AND EXECUTION OF CLAIMS SYSTEM
CONTRACT**

RECOMMENDATION

- A.) Amend the FY07 Budget to add 14 FTEs (full time equivalents) to Risk Management (see Attachment D) with no increase of expense or funding.
- B.) Authorize the Chief Executive Officer to negotiate and execute a 10-year contract with Valley Oak Systems for a Workers' Compensation Claims System for a cost not to exceed \$1.6 million.

ISSUE

For workers' compensation, Metro's claims administration has been performed using Metro employees, a staffing contract with Hazelrigg Risk Management Services, Inc. (13 contract employees) and a separate contract with First Health (1 contract Nurse Case Manager and bill review services). Metro also leases a claims administration computer system through Hazelrigg. With the pending expiration of the Hazelrigg and First Health contracts, a long-term solution to Metro workers' compensation claims administration staffing and information technology resources is required.

BACKGROUND

Metro's workers' compensation insurance policy with Travelers ended in 2001 after a full three years. Unable to renew at competitive rates and having a historically very high number of claims, Metro returned to self-insurance. Metro opted to self-administer claims rather than procure a third-party administrator for price and management control reasons. To administer new self-insured claims, the Board approved a contract in July 2001 with Hazelrigg to provide a claims system and leased workers' compensation claims examiners and support employees, managed by Metro employees.

Hazelrigg Contract Staffing

Since 2001, we have used 13 or more Hazelrigg employees to supplement our own employees to perform claims administration duties. Currently, the Risk Management Department's Workers' Compensation Unit consists of 49 Metro and contract staff members, including Special Investigations (SIU), Nursing, Labor Code Compliance,

Supervisory, Professional and Clerical employees managing an inventory of almost 2,200 claims with approximately 1,200 new claims every year. Approval of this Board item will add these 13 FTEs to the Metro regular staff. Most of these positions can be expected to be filled by the former Hazelrigg employees, some of whom have worked on our account for more than 5 years.

The current staffing level is consistent with industry best practices and benchmarking. Risk Management has reviewed other workers' compensation insurers for their staffing models (the industry standard is to evaluate the number of claims each examiner is required to adjust). Our staffing falls well within the surveyed insurers (Attachment A). The regulatory arm of the State of California for Workers' Compensation (Department of Industrial Relations, Division of Workers' Compensation, Audit Unit) was queried regarding industry practice for staffing a claims unit. They indicated that industry best practice was to have no more than approximately 120 claims per examiner. Our average claims per examiner in December 2007 were 114 (Attachment A).

Total Workers' Compensation staffing in Risk Management has declined substantially (almost 25%) over the last 4 years (Attachment B) resulting in substantial savings. Largely because of these reductions, Risk Management's budget for professional services, including contract staffing, has declined from just over \$4.0 million in fiscal 2005 to just over \$2.1 million for 2007.

Hazelrigg Claims System Lease

For the last five years we have leased a claims computer system through the Hazelrigg contract. The claims system is an "off-the-shelf" product available from Valley Oak Systems (portal VOS). System-related costs, as well as time and material expenses for professional information technology services, are part of the Hazelrigg contract and billed by Hazelrigg directly to Metro on a reimbursement basis. With the impending expiration of the Hazelrigg contract, Metro needs to enter into its own contractual relationship with the existing claims system vendor, Valley Oak Systems. Pricing estimates supplied by the vendor are shown in Attachment C.

First Health Contract Staffing

Also in 2001, Metro procured a separate ancillary workers' compensation services contract that includes nurse case management, medical bill review, utilization review, rehabilitation services and physician peer review services using First Health as the provider. On-site nurse case management includes the use of nursing staff for medical treatment authorization, medical case management and as a conduit for physician peer review services. Through the First Health contract, Metro currently employs a single Nurse Case Manager whose tenure exceeds 3 years. Risk Management is currently working on a scope of services to re-compete the ancillary workers' compensation services contract currently awarded to First Health. The new contract will not include any on-site nurse case management services as they will now be provided directly by Metro through the addition of one FTE.

FINANCIAL IMPACT

Annualized funding of \$1,029,837 for the addition 14 FTEs and \$224,860 for the claims system expense is included in FY07 Adopted Budget in Project 300004, Cost Center 5310 in Account 50316 (Professional Services). Approval of this recommendation will increase the direct labor and related benefits expenses. The increase in these line items will be more than offset with a corresponding reduction in professional services. Attachment D shows the Estimated Personnel Costs.

ALTERNATIVES CONSIDERED

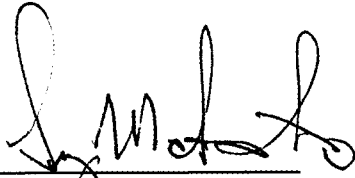
The current staffing contract could be re-procured and then awarded to Hazelrigg or a new vendor. This alternative was not recommended. As demonstrated in Attachment D, the current contract staffing prices offer no cost advantage over the use of Metro employees to perform the claims administration function. Further, selection of a new vendor(s) might mean replacement of up to 14 technical staff with years of accumulated knowledge of Metro claims processes and claimant information. Generally, 6 – 12 months is required for a new claims adjuster to become familiar with 100 – 130 claim files. This loss would result in significant intermediate-term performance problems including labor code violations, penalties, and degraded disability management resulting in cost increases.

A second alternative to conduct a sole source negotiated extension to the Hazelrigg contract under the current terms is also not recommended. Metro's Procurement Department recommends against a sole source contract due to a possible conflict with the federal contracting requirements. Further, Risk Management has experienced turnover and morale problems in both Hazelrigg and First Health staff directly related to the impermanence of Metro's contractual relationship with these vendors. Several highly-skilled contract employees have resigned because of uncertainty regarding long-term prospects of continued contract employment at Metro.

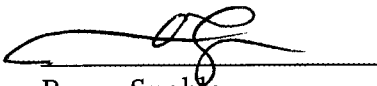
ATTACHMENTS

- A. CLAIMS PER EXAMINER BENCHMARKING
- B. WORKERS' COMPENSATION STAFFING
- C. PRICING ESTIMATE FOR WORKERS' COMPENSATION CLAIMS SYSTEM
- D. ESTIMATED ANNUAL FY07 PERSONNEL COSTS

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ATTACHMENT A

CLAIMS PER EXAMINER BENCHMARKING

	So. Calif. Gas	LAUSD	Adventist Health System	County of San Diego	WMATA	MTA December FY07
Claim Count (Open Inventory)	1,489	6,412	845	2,140	480	2,175
Examiners	12	47	8	20	5	19
Claims per Examiner	124	136	106	107	96	114
California Department of Industrial Relations Workers' Compensation Audit Unit Benchmark 120 or less						

ATTACHMENT B

WORKERS' COMPENSATION STAFFING

	2004	2005	2006	2007	Comments
Workers' Compensation Staffing					
SIU Staff	4	4	4	4	
Labor Code Quality Assurance Unit	-	-	2	2	
Metro WC Staff	24	32	30	29	FY2005 Board approves 8 addtl FTE's to handle Travelers (CSSC) claims in house following settlement of litigation
Hazelrigg Risk Services	21	21	15	13	
Constitution State (CSSC)	8	-	-	-	Metro assumes CSSC claims in FY 2005
First Health Nurse Case Management	7	6	5	1	
WC Program Staffing	64	63	56	49	
% reduction from FY 2004		2%	13%	23%	

ATTACHMENT C

PRICING ESTIMATE FOR WORKERS' COMPENSATION CLAIMS SYSTEM

Description	Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10	10 Year Total
1 Annual Software Maintenance Fee	\$ 65,500	\$ 68,775	\$ 72,214	\$ 75,824	\$ 79,616	\$ 83,596	\$ 87,776	\$ 92,165	\$ 96,773	\$ 101,612	\$ 823,852
2 Project Management Services	55,290	-	-	-	-	-	-	-	-	-	55,290
3 Additional contractor support	-	21,747	22,834	23,976	25,175	26,434	27,755	29,143	30,600	32,130	239,795
4 Training	16,720	17,556	18,434	19,355	20,323	21,339	22,406	23,527	24,703	25,938	210,302
5 Custom Reports/Custom interfaces as needed	12,350	-	-	-	15,000	-	-	-	20,000	-	47,350
6 Hardware	75,000	-	-	-	50,000	-	-	-	50,000	-	175,000
Grand Total	\$ 224,860	\$ 108,078	\$ 113,482	\$ 119,156	\$ 190,114	\$ 131,369	\$ 137,938	\$ 144,835	\$ 222,077	\$ 159,680	\$ 1,551,589

ATTACHMENT D

ESTIMATED ANNUAL PERSONNEL COSTS¹

MTA Employees					
Position	FY07 Mid-Range	Fringe Benefit Rate	Total Cost/Employee	No. of Positions	Total Cost
Office Assistant	\$ 32,802	58%	\$ 51,899	4	\$ 207,596
Admin Aide	\$ 45,822	49%	\$ 68,346	2	\$ 136,692
WC Analyst	\$ 55,578	45%	\$ 80,669	4	\$ 322,676
Sr. WC Analyst	\$ 59,571	44%	\$ 85,713	3	\$ 257,139
Nurse Case Manager	\$ 75,421	40%	\$ 105,734	1	\$ 105,734
				subtotal MTA Cost	\$ 1,029,837
Consultants - Hazelrigg and First Health					
Position	Hourly Rate	Annual Hours Paid	Total Cost/Employee	No. of Positions	Total Cost
Mail/File Clerk	\$ 25.00	1944	\$ 48,600	4	\$ 194,400
Claims Asst.	\$ 29.61	1944	\$ 57,562	2	\$ 115,124
Claims Examiner	\$ 45.32	1944	\$ 88,102	4	\$ 352,408
Sr. Examiner	\$ 50.53	1944	\$ 98,230	3	\$ 294,691
Nurse Case Manager	\$ 75.92	2080	\$ 157,914	1	\$ 157,914
				subtotal Consultant Cost	\$ 1,114,537
				Difference (reduction in expense)	\$ 84,700

¹ The hours paid for contract employees differ because of contract terms. The Nurse Case Manager, supplied by First Health, is paid for up to 4 weeks of non-work time including vacation/sick plus 8 paid holidays for an estimated 2080 hours. The other positions supplied by Hazelrigg are only paid for work time (excluding vacation, sick and holidays).