

The cover features a composite image of the Earth from space, with a cutout of the Texas state map. Inside the map cutout is a photograph of the Texas State Capitol building at night, illuminated with warm lights. The text is overlaid on the top and bottom of the image.

SORM

STATE OFFICE *of* RISK MANAGEMENT

Biennial Report to the 79th Texas Legislature

January 12, 2005



**Biennial Report to the
79th Texas Legislature**
January 12, 2005



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Mission Statement

The State Office *of* Risk Management will provide active leadership to enable State of Texas agencies to protect their employees, the general public, and the state's physical and financial assets by reducing and controlling risk in the most efficient and cost-effective manner.



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The Board of Directors and Executive Director of the State Office of Risk Management respectfully submit this biennial report to the 79th Legislature. This report is submitted pursuant to the requirements of the Texas Labor Code (Title 5, Subtitles A and D), Sections 412.032 and 412.042. The report highlights the activities of SORM during the past two years, and includes state agency information on financing, and state agency claims and expenditures for the periods of FY 2003 and FY 2004. Recommendations for statutory changes relative to the state employees workers' compensation insurance program and comprehensive statewide risk management program serving client agencies are provided in the report.

The State Office of Risk Management appreciates the opportunity to serve state employees and state agencies, and we look forward to working with the members of the 79th Legislature during the session.

Respectfully,

Jonathan D. Bow
Executive Director

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State Office of Risk Management Overview

Revisions to pages 1 through 7 are included at the end of this document.

The 2003-2004 biennium has seen growing stakeholder dissatisfaction in Texas with the workers' compensation system as a whole. Reports from independent research organizations, interest groups, and interim legislative committees have each detailed the crisis in rising costs for employers and poor outcomes for injured workers. Changes dictated by legislative reforms and Texas Workers' Compensation Commission (TWCC) rulemaking have required carriers to make significant investments to ensure compliance with changing rules and fee schedules.

The biennium has presented difficult challenges for the State's self-insured workers' compensation program administered by the State Office of Risk Management (Office), but it has also been a time of opportunity for noteworthy improvement in the Office's programs.

WORKERS' COMPENSATION EXPENDITURES REDUCED IN 2004

For the first time in seven years, the cost of providing workers' compensation benefits for injured state employees went down in FY 2004. The total required to provide indemnity and medical benefits was \$14 million dollars less than FY 2003 and \$22 million less than the liability projected by the system's actuarial consultant.

The rapid decrease in expenditures is the result of a number of factors, including improved claims processing by the Office, improved safety practices on the part of client agencies, and greater accountability on the part of agencies for losses.

These improvements have directly translated into savings for state agencies and the state as a whole. The total assessments to state agencies for payment of claims costs for FY 2005 is \$19.4 million less than FY 2003 and \$21.7 million less than FY 2004. In addition, the Office will return to client agencies approximately \$15.5 million in unexpended funds from the FY 2004 assessments.

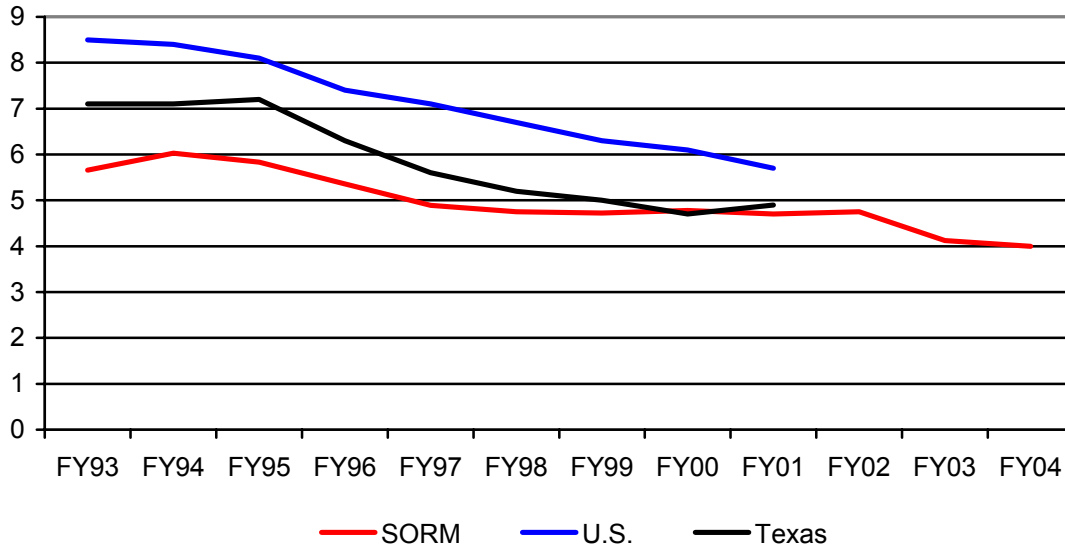
FEWER STATE EMPLOYEES INJURED EACH YEAR

New injuries to state employees have been significantly reduced during this biennium. On average, more than 1,000 fewer injuries have occurred annually for each of the previous two years than for the rest of the past decade. The Office attributes much of this reduction to significantly improved risk management and claims coordination efforts by covered agencies as a result of making those agencies more accountable for their injuries, as mandated by the Legislature.

The Office has supported agencies in this effort through increased agency visits, education, and assistance in implementing successful mitigating strategies at client agencies. The chart below compares the national and Texas statewide average injury frequency rate (IFR) to the average for the Office's program. IFR is a measure of the average number of injuries per 100 employees in a given year. While IFR data is not available for the U.S. or the state for 2002-2004, the Office's client agencies continued the downward IFR trend during that period,

finishing the year at 4.0 for FY 2004. This continuing reduction in IFR has contributed to the significant reduction in paid workers' compensation claims over the past two years.

U.S., Texas, and SORM IFR Rate History



Sources: Bureau of Labor Statistics, U.S. Department of Labor, Survey of Occupational Injuries and Illnesses in cooperation with the Texas Workers' Compensation Commission; SORM

STATE INSURANCE PURCHASING PROGRAM DEMONSTRATES SAVINGS

The Insurance Purchasing Program established by HB 1203, 77th Legislature, continued to expand in this biennium, and the Office has implemented four lines of sponsored insurance available to all covered state agencies: Directors' and Officers' with Employment Practices Liability, Short-Term Special Event General Liability, Automobile, and Volunteer policies. Savings as a result of centralizing these state insurance purchases exceeded a quarter of a million dollars for FY 2004 and savings are expected to continue to grow as new lines are evaluated and approved, or denied.

NEW STUDIES PROVIDE IMPORTANT BENCHMARKING DATA AND IDENTIFY WEAKNESSES IN PAST PERFORMANCE

The Texas Department of Insurance (TDI) conducted a study during the biennium in response to an interim charge on workers' compensation. This was the first study of its kind and the data revealed that while the Office's medical costs were similar to private sector expenditures, the medical costs in the Office's workers' compensation program during the calendar years of

1999, 2000, and 2001 were higher than the programs administered by the other self-insured state systems (University of Texas, Texas A&M University, and Texas Department of Transportation).

The study provided an opportunity for the Office to compare performance and identify differences between the programs that could account for the cost differentials. A number of factors were identified by the Office as influencing expenditures, including the lack of an implemented health care network in the Office's program, claims staff turnover exceeding 125 percent during the study period, lower adjuster salaries, and weaknesses in the Office's medical cost containment program.

The Office has taken steps to directly address these causative factors, including modification to claims procedures and organization, reinitiation of the proposal process for a health care network, and new FY 2005 contracts for medical cost containment services. These efforts and others are discussed in the "Core Components" section of this report.

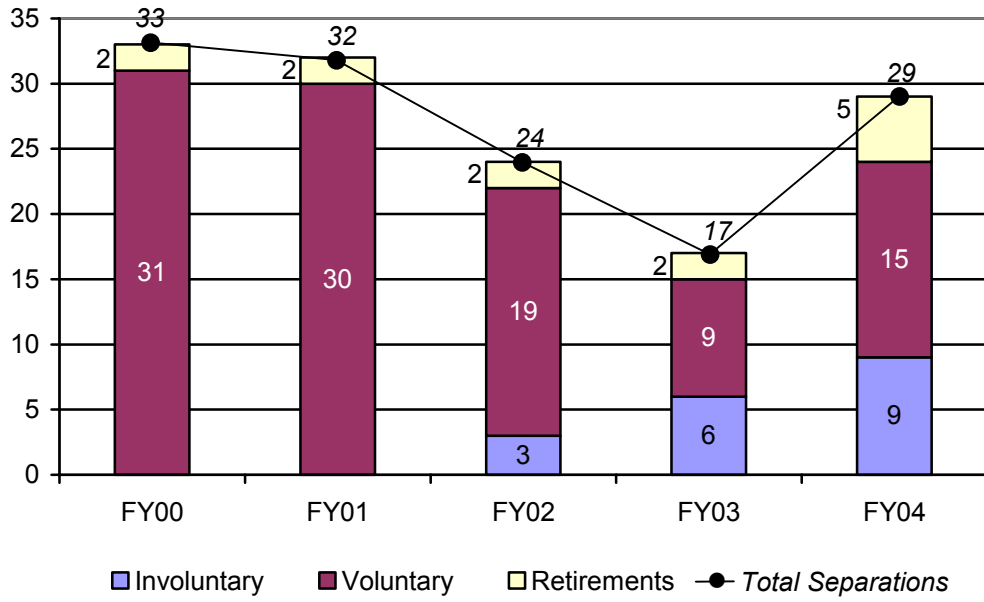
STAFF TURNOVER RE-EMERGES AS AREA OF CONCERN

Employee turnover at the Office increased from 13 percent in FY 2003 to 22 percent in FY 2004. In the first quarter of FY 2005 the Office lost six claims adjusters (11 percent of the entire claims staff). This is largely a result of competition from private workers' compensation insurance carriers in the Austin/Central Texas market. The Office anticipates additional claims personnel losses as private carriers expand operations in the Austin region, closing the fiscal year at a projected 26 percent turnover in claims staff.

The Office's loss of tenured staff to the private sector is largely a function of higher salaries in that sector. According to "A Survey on Organizational Excellence" prepared by the University of Texas for the Office and the State Auditor's online exit interviews, the majority of the Office's claims staff leave the agency for higher salaries. An informal exit interview of claims adjusters leaving the Office confirmed an average salary increase of 22 percent more than available agency salaries.

Turnover has been a significant historical concern, and the Office has consistently sought to retain and attract qualified staff by creating a positive work environment, by acknowledging professional achievement through reimbursement for work-related professional certification, supporting an active Employee Association, providing flexible and alternative work schedules, and other employee-friendly agency policies. Recognizing the significant draw of higher salaries in the Office's excessive turnover, the State Auditor's Office recommended significant adjuster reclassifications in FY 2000, which resulted in a temporary sharp decrease in claims staff turnover rates. However, the re-emergence of significant salary competition is increasing turnover once again.

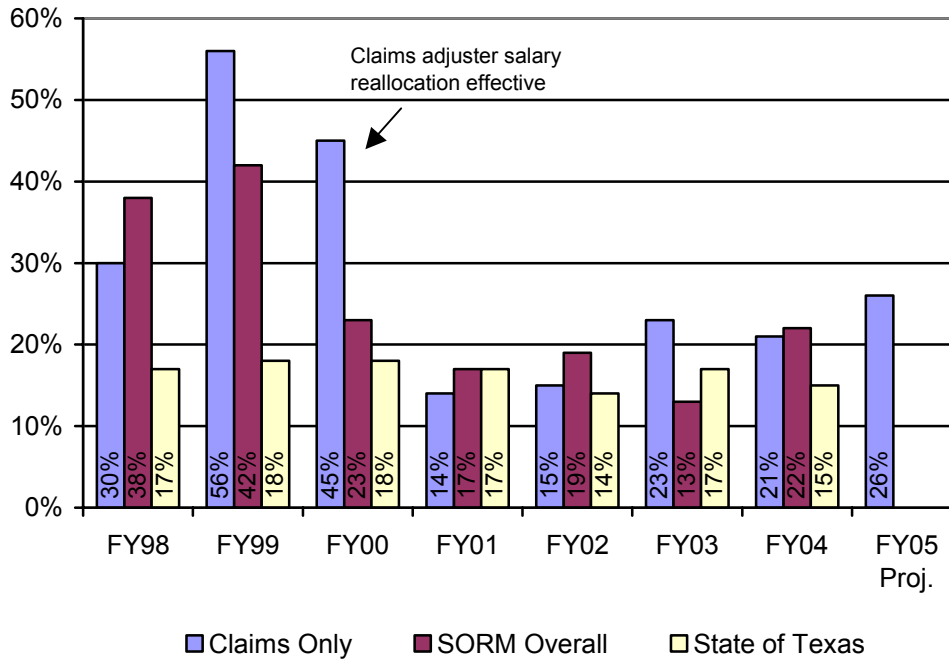
SORM Turnover



Source: State Auditor's Office

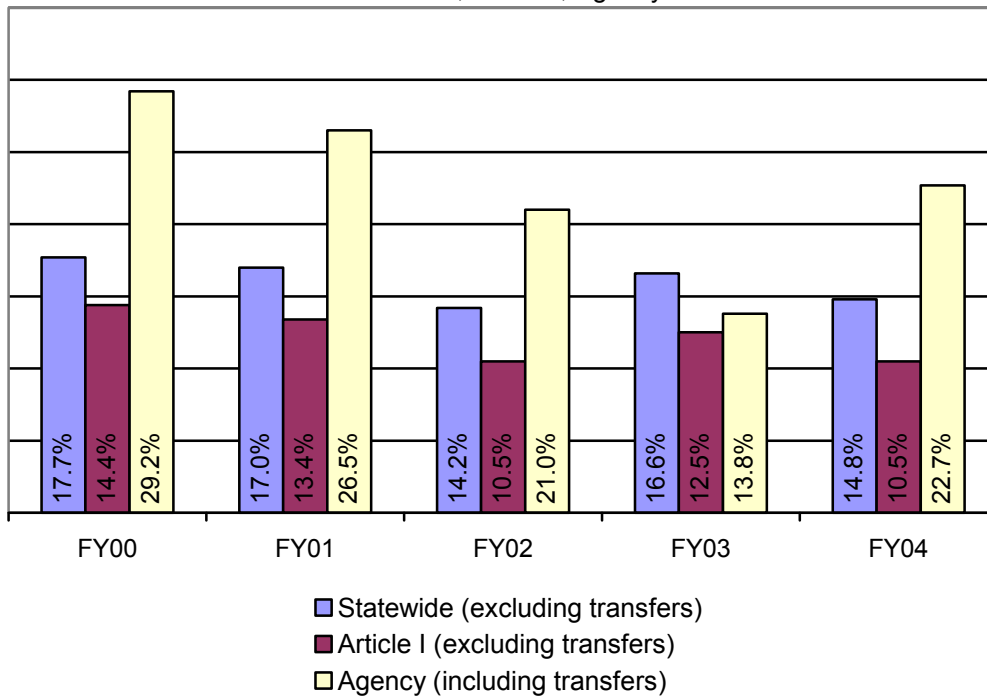
Turnover Comparison

Claims Only, SORM Overall, State of Texas



Turnover Comparison

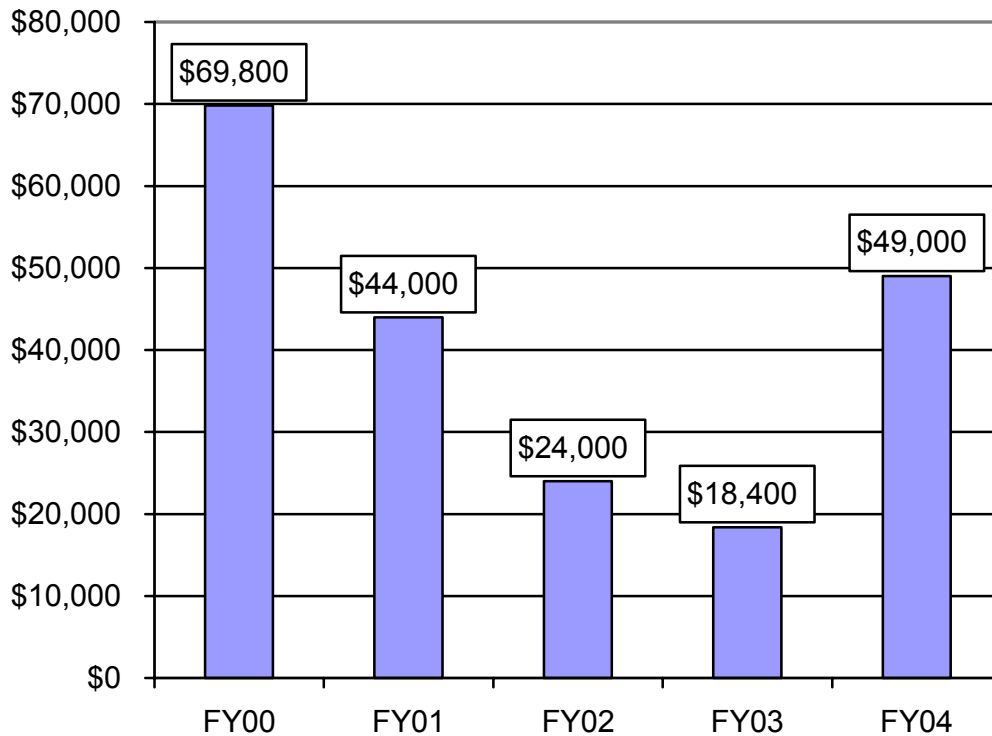
Statewide, Article I, Agency



Source: State Auditor's Office

The loss of institutional knowledge as a result of staff turnover has increased the cost of administering SORM's statutory programs in the short term. The cost to replace employees more than doubled in FY 2004, exceeding \$49,000.¹

Annual Cost of Turnover



¹ The methodology used to determine the cost of turnover was the same as used by the State Auditor's Office in its *FY 2004 Employee Turnover Statistics*

Core Components

Insurance Purchasing Program - HB 1203, 77th Legislature, instructed SORM to operate as an insurance manager for state agencies, including a requirement that the Office's Board phase in, by line of insurance, the requirement that a state agency purchase coverage only through the Office. The Office established administrative rules at 28 T.A.C. 252.301, *et seq.*, implementing the program, including application and reporting requirements. To date the Office has phased in four approved statewide lines of insurance: Directors' and Officers' with Employment Practices Liability (D&O/EPL), Short-Term Special Event General Liability, Automobile, and insurance for volunteers at state agencies. The Office performs specialized reviews on all proposed purchases for coverages, limits, insurer financial stability, loss controls, necessity, and appropriateness. The initial implementation of the statewide programs is approximately \$341,000 less than the direct bids to agencies, and additional future savings are anticipated as new lines are reviewed and implemented .

The total number of policies purchased by agencies is down for the biennium, largely due to elimination of bond purchases and the general prohibition on the purchase of employee dishonesty coverage. The premiums for the same period have increased due to overall market increases in response to 9/11 in the areas of property, automobile, and general liability. D&O/ EPL premiums have increased due to potential and actual losses resulting from the Enron, Arthur Anderson, and WorldCom incidents. According to industry forecasts, it is anticipated that D&O/EPL premiums should remain stable while property and general liability should gradually decrease. However, it is not yet clear how the recent hurricanes in Florida will affect property premiums. Most articles indicate the insurance industry may be able to absorb these losses without affecting financial stability. The property and general liability markets have increased capacities that also affect premium dollars, which should be reflected in costs in the next biennium. Insurance premiums are very dependent on external events, whether political, legal, weather-related or financial, and are therefore difficult to predict.

It should be noted that the data provided in the "State Agency Non-Workers' Compensation Losses" section of this report reflects increases in the total dollars spent on insurance premiums. These increases are partly due to market influences and, in some cases, the Office has specifically recommended that select agencies increase coverage to better protect against potential losses; however, the total increase cannot be attributed solely to these factors. The increases reported are based upon available data only and incomplete reporting by client agencies during prior biennia make accurate comparisons impracticable. It is anticipated that as agencies become more educated on and compliant with the Office's reporting requirements, the accuracy of data will increase over time. In addition, the Office has instituted safeguards, such as access to the Comptroller's system for approval of payment of premiums, which should improve the accuracy of insurance purchasing data.

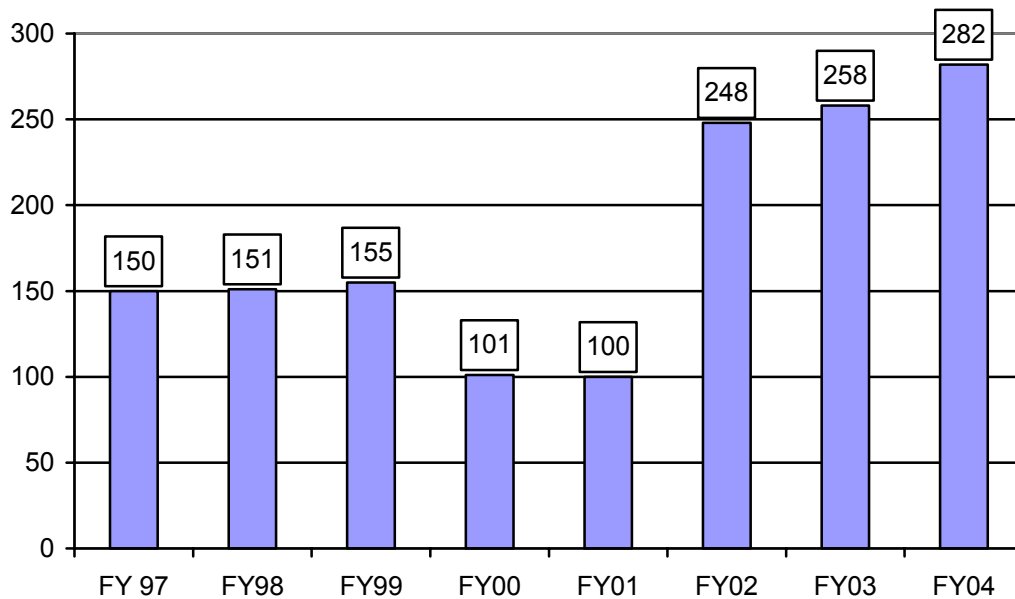
Although the Office has experienced difficulty in ensuring 100 percent agency compliance in the insurance purchasing program established by the Legislature, the Office continues to communicate with non-compliant agencies with the goal of agency adherence. While the Office does not have specific enforcement authority, Section 412.032 of the Texas Labor Code requires the Office to identify non-complying agencies to the Legislature. That

information is contained in the “412.032(b)(2) Non-Complying Agency Reporting” section of this report.

Risk Management Consultations - The Office conducts two different types of agency reviews, Risk Management Program Reviews (RMPRs) and On-Site Consultations (OSCs). RMPRs are a comprehensive analysis of each client agency’s policies, procedures, exposures, losses, and risk management efforts. OSCs are less formal visits to agencies intended to focus on specific problems or losses occurring at the agency or, upon request, to provide consultative assistance to an agency. A client agency may receive multiple OSCs and one RMPR in a given year.

During FY 2004, the SORM risk management specialists performed 32 RMPRs and 250 OSCs. The Office’s goal is that all state agencies receive a RMPR at least once every five years and an OSC not less than once every 2½ years, and agencies with significant exposures be evaluated on a more frequent basis. The following chart illustrates the increase in agency visits by the Office’s staff over an eight-year period.

Risk Management Consultation Visits to Client Agencies



During this past biennium, the Office began conducting quarterly Risk Management User Group meetings. The meetings are open to all state and local government risk managers and provide a source of education and information regarding risk management issues. The user group meetings have been well-received and attended by state agencies. The Office also analyzed state personal property losses and made statewide statistical information on losses

available to all agencies on its website. This important information is intended for use by client agencies to benchmark agency performance against statewide normative data.

The Office is encouraged that the efficacy of strong risk management efforts continue to be demonstrated as evidenced by the reduction in injuries and losses in the workers' compensation program.

Workers' Compensation Claims Management and Adjusting - In response to changing legal requirements, high claims loads, and increasing turnover pressures, the Claims Operations Division has continued to evolve over the past two years. The division established a Customer Service Call Center in May of 2002 to enhance customer service and that was expanded in FY 2003 to simultaneously function as an on-the-job training ground for in-house, entry-level claims adjusters.

The division's emphasis on succession planning has developed basic claims administration skills in all available staff to help cushion the losses of experienced staff to the private sector. A reorganization in early FY 2004 replaced administrative/clerical positions with licensed claims adjusters in the claims area to provide additional depth in claims processing staff.

Short-term results of these efforts have shown improved claims handling and reduced workloads for adjusters, allowed for closer scrutiny of claims and a higher closure ratio, and contributed significantly in reducing medical and indemnity claims costs by approximately \$14.4 million in FY 2004.

At the beginning of the last biennium, each of the Office's lost-time adjusters handled an average workload of 284 lost-time claims, while medical-only adjusters handled an average of 508 medical-only claims. The Office has been successful in closing inactive claims with open reserves that previously incurred costs but received only minimal scrutiny from adjusters. Currently each lost-time adjuster handles an average of 125 lost-time claims and administrative adjusters handle an average of 175 medical-only claims. This achievement represents the first time in the Office's existence that adjusters have handled workloads at or below the industry standard of 125-150 lost-time claims and 300-350 medical-only claims.²

To address high medical costs, the agency formed the Medical Management Review Team in August of 2002, consisting of a registered nurse, a licensed vocational nurse, and skilled adjusters with a high level of medical knowledge. By uniting experienced adjusters with trained nurses, the Office has targeted those claims with significant medical activity and monitors and audits for provider fraud, over-utilization of medical treatment, and medical treatment not related to the injury.

² Annual internal audit report, KPMG 2002

Medical Cost Containment - The incorporation of the Medical Cost Containment Oversight Unit into the Claims Operations Division has provided better support for the claims unit, better review of the processing of claim-related medical bills, and a streamlined method for auditing and administering the agency's medical cost containment contracts.

During FY 2004, the Office's medical expenditures accounted for \$32 million of the total \$56 million in claim expenditures. The Office's cost containment measures in FY 2004 resulted in a savings of more than \$76 million below billed charges for the workers' compensation claims fund and Texas taxpayers. These savings are detailed in the Office's Annual Cost Containment Report³ and are summarized below.

Summary of Cost Containment Savings

| Strategy | FY 2002 | FY 2003 | FY 2004 |
|--|---------------------|---------------------|---------------------|
| Total Medical Bill Audit Savings | \$60,261,042 | \$68,554,645 | \$91,976,556 |
| Medical Bill Audit Savings due to Duplicate Bill Savings | (\$17,670,569) | (\$19,277,164) | (\$17,975,621) |
| Net Medical Bill Audit Savings | \$42,590,473 | \$49,277,481 | \$74,000,935 |
| PPO Savings | \$491,142 | \$325,248 | \$237,504 |
| Preauthorization of Medical Services ⁴ | \$1,434,625 | \$2,083,739 | \$1,108,279 |
| Subrogation Recovery | \$252,689 | \$917,175 | \$1,197,775 |
| Total Cost Containment Savings | \$44,768,929 | \$52,603,643 | \$76,544,493 |

While those savings were significant, a number of studies indicated further savings could be realized. Beginning in FY 2005 two new vendors assumed responsibility for contracted cost containment activities, CorVel Corp. for bill review and Forté, Inc. for preauthorization. The Office is seeking additional savings through the cost containment strategies offered by these vendors and continues to monitor their performance closely. The new contracts allow for utilization of optional advanced cost containment services and provide for the transfer of duties between vendors should the performance of either vendor prove unsatisfactory.

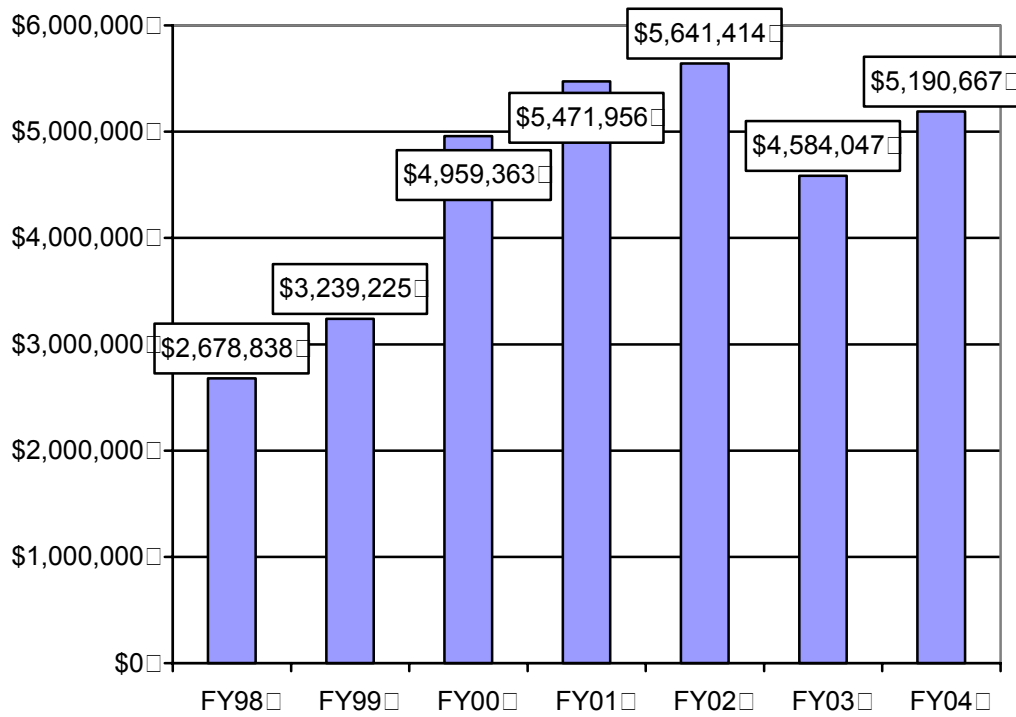
³ Annual Report on Cost Containment, FY 2004; State Office of Risk Management; October 15, 2004

⁴ The Texas Workers' Compensation Act and TWCC-administered Rules provide that health care providers are required to "preauthorize" certain specific medical procedures (e.g., psychiatric care and non-emergency hospitalizations) with workers' compensation insurance carriers prior to the procedures being performed. Preauthorization savings are the result of avoiding expenses by denying unreasonable or unnecessary procedures prior to treatment. The resulting "savings" are estimates provided by the cost containment vendor.

Significantly, the new contracts are based on a per-service pricing structure rather than a flat rate yearly fee. While the prior cost containment contract provided significant budgeting advantages, it largely lacked the incentives for accountability and timely quality improvements responsive to the ever-changing workers' compensation system.

The costs of medications for work-related injuries have been rising systemwide since the implementation of new law. By utilizing a Pharmacy Benefit Management (PBM) program through the cost containment contracts, the Office continues to receive savings on pharmaceutical costs. The PBM provides a prescription card to all injured workers' who are prescribed claim-related medications. When an injured worker presents the pharmacy card at a participating pharmacy, SORM receives a discount below the Pharmaceutical Fee Guideline. While an injured workers' participation in this program is entirely voluntary, the savings to the State make the PBM program a valuable asset in SORM's cost containment strategy.

Pharmacy Costs



Fraud Investigations - During this biennium the Office handled approximately 200 fraud referrals from internal staff and external contacts. Investigators in the General Counsel Division conducted an average of 20 surveillances each year. Of the completed

investigations, 27 cases were referred to TWCC’s Compliance and Practices Division for possible prosecution and/or administrative violations.

SORM continues to solicit the involvement and assistance of covered agencies in its efforts to combat workers’ compensation fraud. For example, through the combined efforts of the Texas Department of Criminal Justice (TDCJ) and SORM, the number of referrals in cases involving TDCJ personnel was increased through coordination with TDCJ’s Special Prosecuting Unit and cooperative investigations. This increased scrutiny and agency involvement directly resulted in reduced TDCJ claims costs during the biennium.

Fraud Case Summary

| | FY 2003 | FY 2004 |
|--|--|----------------|
| Number of Closed Investigations | 76 | 71 |
| Number of Indictments/ Prosecutions | 3 indictments (2 prosecuted in FY 2004, 1 still pending) | 4 prosecutions |

Training and Education - The Agency provides specialized training and education programs for state agencies ranging from administrative and statutory requirements for notaries employed by the State of Texas to defensive driving and forklift safety. With the exception of statutorily mandated courses, classes are developed and offered based on trend analysis of the risks and specific needs of client agencies. Training generally targets agency risk managers, safety officers, claims coordinators, and training staff.

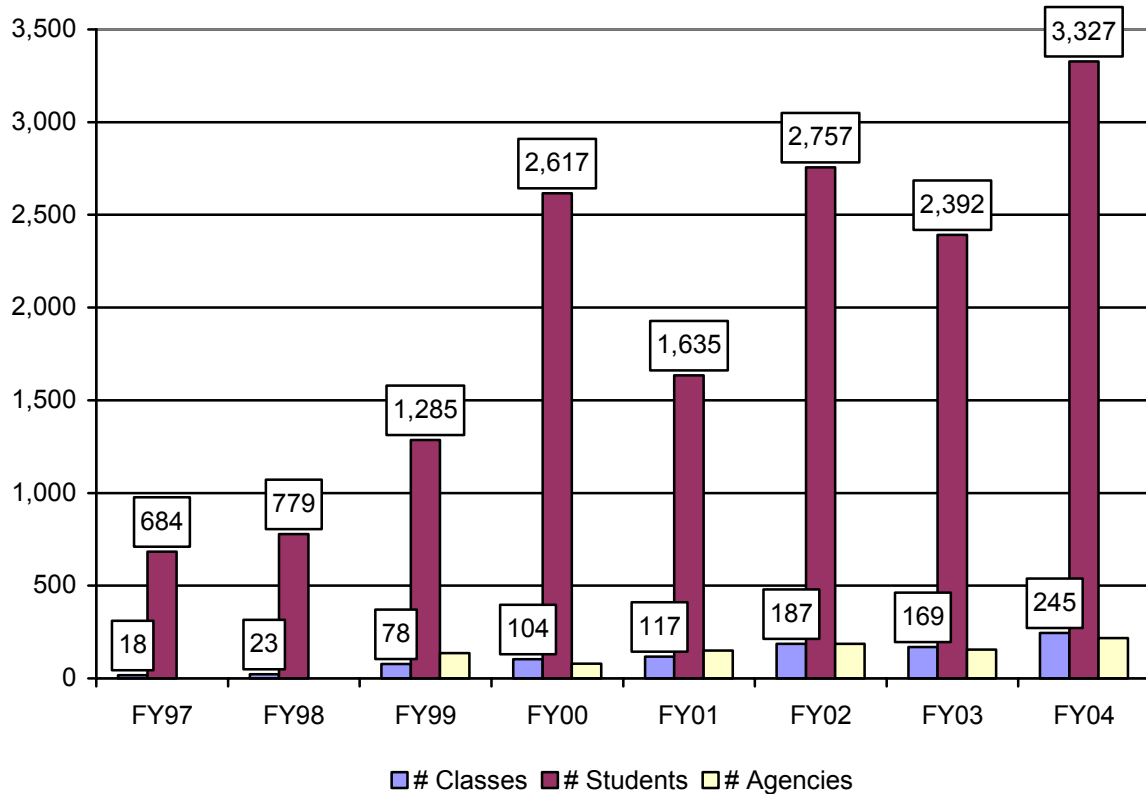
In the past biennium, the Office introduced an online training tool to help state agencies identify risks and mitigating strategies. This tool, the “Safety Puzzle,” condenses state and federal safety rules and regulations into an easy-to-read series of web pages. The puzzle earned an Achievement Award from the Texas Public Risk Management Association (Texas PRIMA) in November 2003.

The Office has also expanded its internal training in cooperation with the Claims Operations Division to prepare employees for licensure to adjust claims. Development of new adjusters has been a major strategy to address the Office’s barriers in attracting and retaining experienced, licensed adjusters and reduce the impact of agency turnover. In addition the Office continues ongoing efforts to provide continuing education to maintain its adjusters’ licensures and skills.

During FY 2004, SORM conducted 245 classes attended by 3,327 client agency employees. This represents a 39 percent increase in class attendance, with most courses offered by request.

Training Statistics

Includes safety, risk management, workers' comp, and adjuster CEU classes



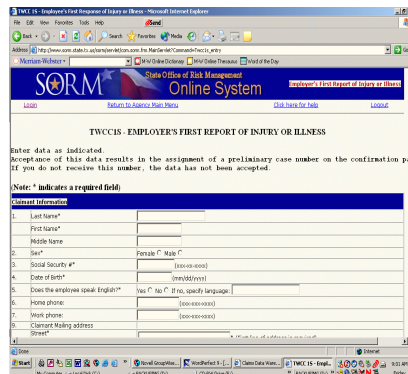
In addition to training classes, the Office publishes the quarterly *Risk-Tex* newsletter, attends client agency events to promote workplace safety, and facilitates a testing center for state employees seeking certification in the areas of risk management and workers' compensation as part of its training and outreach effort.

Information Technology - During the biennium the Office successfully implemented a secure, web-based system to collect risk management information from client agencies, generate workers' compensation and risk management reports, and automate collection of workers' compensation claims information via the Internet. This system was developed using open source programs and databases, avoiding significant costs for purchase and ongoing licensing of commercial packages.

The initial report of an on-the-job injury is now being reported online by all client agencies. Automation of this process has expedited processing of claims and has increased communications with agencies through the use of secure auto-notification email that immediately communicates to client agencies any changes in status of their workers' compensation claims. Additional reporting forms were also web-enabled and are the official reporting mechanism for supplemental information on client agency workers' compensation claims.

During the last biennium, the Office developed detailed Business Continuity Planning instructions, examples, and templates available to all state agencies and the public on the SORM website. The Office also continued development and maintenance of web-based Emergency Response Protocols, a series of detailed instructions on sequential actions to take in responding to various threats or emergencies. The protocols also link directly to additional information available from such sources as the Department of Homeland Security, FEMA, and others.

The Office is currently developing a robust, web-based Risk Management Information System (RMIS). RMIS will assist client agencies in performing detailed risk analysis, frequency/severity analysis, probability analysis, development of mitigating strategies to reduce risk of loss, and the creation of an individual agency risk management plan. RMIS will also provide client agencies with increased information on non-workers' compensation losses and will help agency management benchmark individual risk management program performance against agencies of similar size or type of operation.



SORM Funding and Financial Schedules

For FY 2004 net total expenditures were \$54,650,872. As of Dec. 28, 2004, the cash balance for the Workers' Compensation Claim Fund for FY 2005 was \$19,119,052. The transactions through Dec. 28, 2004 are summarized below:

| | |
|--|---------------------|
| Total assessments for Workers' Compensation Claim Payments | \$50,048,755 |
| Carry-forward from FY 2003 | 7,812,700 |
| Assessments due | (21,627,229) |
| Net collections | 36,234,226 |
| Subrogation recoveries | 311,334 |
| Expenditures for indemnity benefits | (7,082,146) |
| Expenditures for medical benefits | <u>(10,344,362)</u> |
| | \$19,119,052 |

Based on the most recent data, the Office currently estimates that total workers' compensation expenditures will be approximately \$56,000,000 for FY 2005, resulting in a total for the 2004-2005 biennium of \$110,650,872. The Office's 2004-2005 biennium estimate represents a \$26 million decrease over actual 2002-2003 biennium costs of \$136,256,784, and a \$46 million decrease over the Jan. 12, 2004 actuarial report projecting total expenditures of \$156,674,619 in the 2004-2005 biennium.

The following table summarizes administrative expenditures for SORM for FY 2004 and budgeted expenditures for FY 2005.

| Category | FY 2004 Actual | FY 2005 Budgeted | Biennium Total | Percent of Total |
|-----------------------|---------------------------|-----------------------------|---------------------------|-----------------------------|
| Salaries | \$4,350,191 | \$4,466,881 | \$8,817,072 | 57.7% |
| Other Personnel Costs | \$224,651 | \$79,330 | \$303,981 | 2.0% |
| Contracted Services | \$1,185,109 | \$2,667,164 | \$3,852,273 | 25.2% |
| Consumable Supplies | \$33,421 | \$51,937 | \$85,358 | 0.6% |
| Utilities | \$12,495 | \$20,168 | \$32,663 | 0.2% |
| Travel | \$110,351 | \$117,656 | \$228,007 | 1.5% |
| Rent - Building | \$8,476 | \$9,155 | \$17,631 | 0.1% |
| Rent - Other | \$14,186 | \$21,678 | \$35,864 | 0.2% |
| Other Operating | \$820,513 | \$893,303 | \$1,713,816 | 11.2% |
| Capital | \$107,901 | \$92,975 | \$200,876 | 1.3% |
| Total | \$6,867,294 | \$8,420,247 | \$15,287,541 | 100.0% |

Recommendations for Statutory Changes for Consideration by the 79th Legislature

The Office has been able to fulfill the vast majority of its duties under current statutory authority, although a number of issues were raised during the biennium that may warrant additional consideration by the Legislature.

Scope of Chapters 412 and 501 of the Texas Labor Code - Implementation of the Insurance Purchasing Program authorized by HB 1203, 77th Legislature, and the Cost Allocation (or Risk/Reward) Program authorized by HB 2600 and 2976, 77th Legislature, have met with reluctance by some client agencies to fully comply with established mandates.

The Insurance Purchasing Program, Chapter 412, provides that agencies subject to Chapter 501 of the Texas Labor Code may not purchase property, casualty, or liability insurance coverage without the approval of the Board of the State Office of Risk Management. An opinion letter from the Legislative Council in 2001 has created confusion about the Legislature's intent in regard to the participation of higher education in the insurance purchasing program. That opinion holds that the Legislature did not intend to include institutions of higher education in the scope of Chapter 412 and the opinion was recently forwarded to the Office as justification for non-compliance when a higher education institution purchased an unauthorized policy after the purchase was denied by the Office. The Office's authority extends only to reporting such non-compliance to the Legislature. Clarification of the scope of Chapter 412 may be warranted to avoid future confusion and clearly delineate the reporting requirements of the Office respecting non-complying agencies.

With respect to the Cost Allocation Program, the drastic change in funding structure has led to isolated but significant reluctance of some agencies to fully participate in the program. The previous funding structure was a partial reimbursement funding method, with direct appropriations to the Office for claims payments and a requirement for a 25 percent reimbursement by client agencies. When HB 2600 and 2976 were passed by the 77th Legislature, appropriations for claims were reallocated to client agencies as part of the agencies' baseline budgets for the payment of an "assessment" similar to an insurance premium to the Office, but a prior provision related to reimbursement of non-treasury funds in Chapter 506 was not modified (Section 506.022). The Office requested an Office of the Attorney General (OAG) opinion, which concluded in May of 2003 that the retention of the reimbursement provision operated to exempt those agencies from the Cost Allocation Program. Subsequently, one agency was statutorily exempted from all participation in Chapter 412 of the Labor Code pursuant to a Senate Finance Committee substitute to HB 2425, 78th Legislature. The Office has attempted to fully comply with the OAG interpretation that the Legislature intended the Office to operate under two distinct funding structures, but additional review by the Legislature of these issues may be appropriate.

Methods to Reduce the State's Exposure to Risk

Risks to Historical Documents and Artifacts - Several client agencies are responsible for archiving historical documents and artifacts. Some of these agencies either have no active fire suppression system or have a water-based system that would significantly damage or destroy important state treasures should a fire occur and the suppression system activate. Agencies that archive important state documents should conduct a risk analysis for potential damage or loss of such documents and determine a cost to provide adequate protection against fire, water, smoke, environmental deterioration, and other appropriate exposures. Each archiving agency should report the types of documents or artifacts at risk, the current level/type of protection implemented, and the proposed mitigating strategy(ies) to protect the documents along with a cost/benefit analysis of the proposed strategy.

Business Continuity and Management Planning - The Federal Emergency Management Agency (FEMA) maintains a list of major disasters declared in the 50 states, the District of Columbia, and nine U.S. territories. The State of Texas is at the top of this list, making it the most “disaster-prone” state, with 51 disasters formally declared between the years of 1976 and 2000. The next closest is California with 45.

The events of 9/11 create further concerns regarding continuity of government functions in the event of terrorist attack and the unique risks associated with the approximately 57 state agencies located within the Capitol Complex.

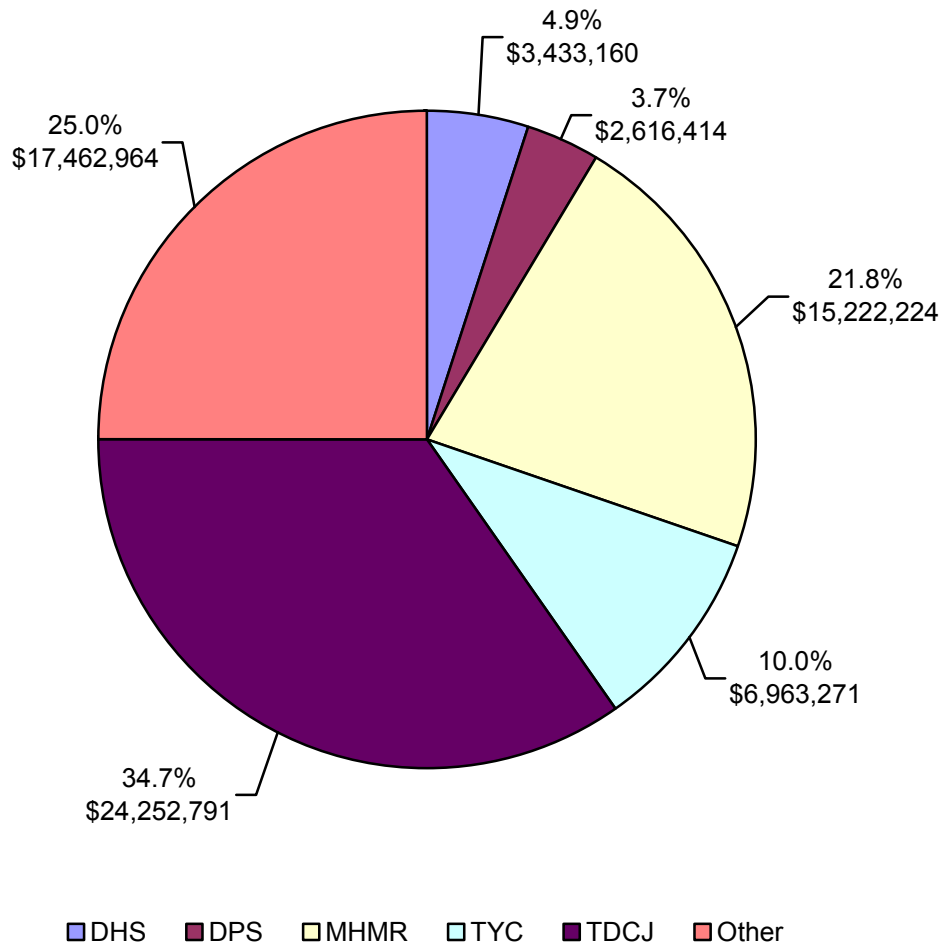
The Office assists state agencies in developing business continuity plans; however, these plans generally address only the particular agency’s critical business processes, recovery time objectives, and dependence on other agencies or entities. Certain disasters or actions could result in multiple agencies simultaneously being unable to perform critical state functions. At this time, there is no formal prioritization for restoration of agencies or functions. While the Office emphasizes agency-level business continuity plans, the Office’s authority does not extend to mandating high-level government and interoperability issues. The Office recommends that the Legislature consider mandating a functionally based restoration priority plan to be developed and maintained by designated state leadership, with particular emphasis on restoration of critical statewide functions affecting core business processes and/or multiple agencies. In the event of a significant natural or man-made disaster affecting core government functions, the existence of such a plan would be absolutely necessary to ensure those functions were restored in the quickest and most efficient manner possible.

The Office notes that business continuity plans, whether agency-based or general government-based, may contain sensitive information that could be used to purposefully disrupt continuity efforts in the event of terrorist action. It is further recommended that the Legislature consider a limited protection of such information from disclosure pursuant to the Public Information Act.

State Agency Workers' Compensation Claims and Losses

Workers' Compensation Losses - FY 2003

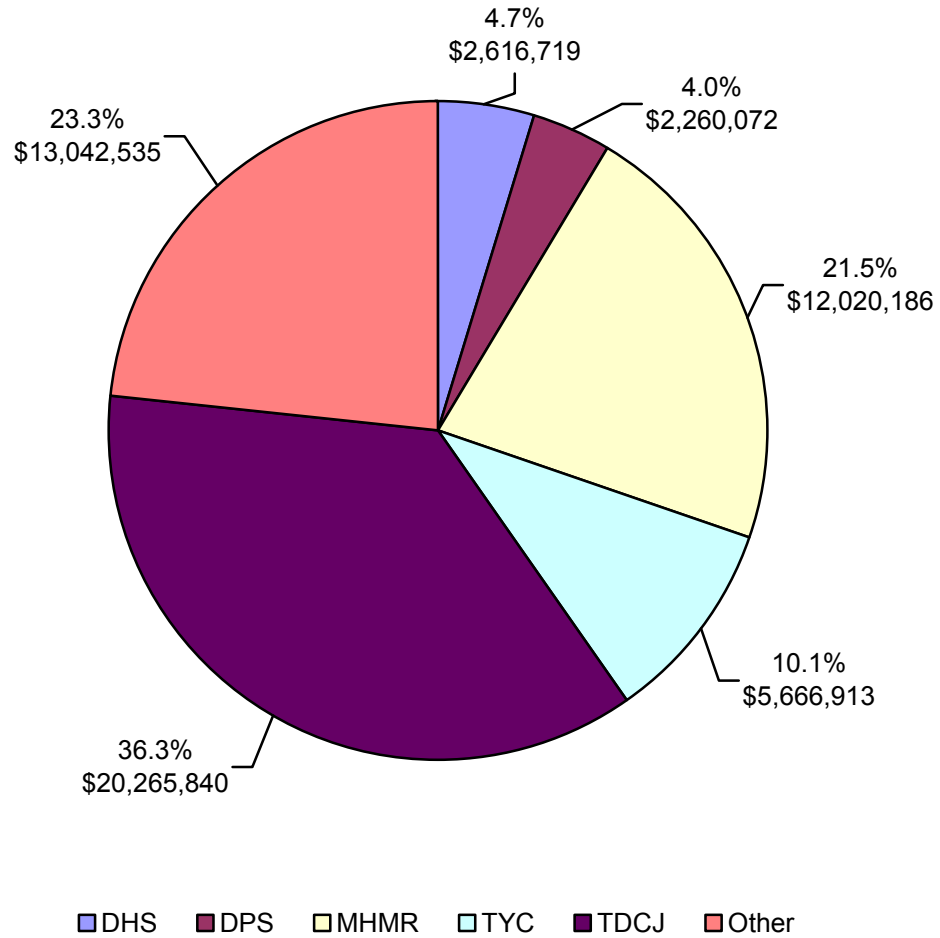
Total WC Losses: \$69,950,825



Note: These amounts are gross expenditures and do not include subrogations and restitutions.

Workers' Compensation Losses - FY 2004

Total WC Losses: \$55,872,266



Note: These amounts are gross expenditures and do not include subrogations and restitutions.

Summary of Losses - By Agency FY 2003

| Agency Name | Workers' Compensation | Property | % |
|---|-----------------------|--------------|-------|
| 101 - Texas Senate | \$ 69,018.24 | | 0.10% |
| 102 - House of Representatives | \$ 47,318.97 | | 0.07% |
| 103 - Texas Legislative Council | \$ 7,208.05 | \$45,554.81 | 4.23% |
| 212 - Office of Court Administration | \$ 8,688.75 | \$5,090.00 | 0.47% |
| 222 - 2nd Court of Appeals | \$ 1,970.25 | | 0.00% |
| 227 - 7th Court of Appeals | \$ 4,891.00 | | 0.01% |
| 241 - Comptroller's Judiciary S | \$ 430,360.02 | | 0.62% |
| 301 - Office of the Governor | \$ 802.75 | | 0.00% |
| 302 - Office of the Attorney General | \$ 516,181.08 | | 0.74% |
| 303 - Texas Building and Procurement Commission | \$ 311,614.24 | | 0.45% |
| 304 - Comptroller of Public Accounts | \$ 369,950.59 | \$15,450.00 | 0.53% |
| 305 - General Land Office | \$ 107,017.70 | | 0.15% |
| 306 - Texas State Library and Archives Commission | \$ 12,367.28 | | 0.02% |
| 307 - Secretary of State | \$ 27,527.21 | | 0.04% |
| 313 - Department of Information Resources | \$ 555.86 | | 0.00% |
| 318 - Texas Commission for the Blind | \$ 64,225.17 | | 0.09% |
| 320 - Texas Workforce Commission | \$ 1,494,389.42 | \$77,058.00 | 2.14% |
| 323 - Teacher Retirement System | \$ 101,525.05 | | 0.15% |
| 324 - Department of Human Services | \$ 3,433,159.64 | \$197,937.13 | 4.91% |
| 327 - Employees Retirement System | \$ 9,980.46 | | 0.01% |
| 329 - Real Estate Commission | \$ 40,753.20 | | 0.06% |
| 330 - Texas Rehabilitation Commission | \$ 368,038.62 | \$11,297.53 | 0.53% |
| 332 - Texas Department of Housing and Community Affairs | \$ 78,248.24 | | 0.11% |
| 335 - Texas Commission for the Deaf and Hard of Hearing | \$ 2,278.57 | | 0.00% |
| 342 - State Aircraft Pooling Board | \$ 2,343.00 | | 0.00% |
| 344 - Commission on Human Rights | \$ 68.96 | | 0.00% |
| 347 - Texas Public Finance Authority | \$ 757.49 | | 0.00% |
| 350 - Texas National Research Laboratory | \$ 592.00 | | 0.00% |
| 357 - Office of Rural Community Affairs | \$ 17,618.65 | | 0.03% |
| 360 - State Office of Administrative Hearings | \$ 10,794.75 | | 0.02% |
| 362 - Texas Lottery Commission | \$ 32,876.25 | \$6,166.25 | 0.05% |
| 367 - Telecommunication Infrastructure Fund Board | \$ 4,511.00 | | 0.01% |
| 401 - Adjutant General's Department | \$ 290,839.36 | | 0.42% |
| 405 - Department of Public Safety | \$ 2,616,414.34 | \$82,342.90 | 3.74% |
| 406 - Texas Military Facility Commission | \$ 18,046.08 | | 0.03% |

Summary of Losses - By Agency

FY 2003

| Agency Name | Workers' Compensation | Property | 0.00% |
|--|-----------------------|----------|-------|
| 411 - Texas Commission on Fire Protection | \$ 6,385.10 | 0.01% | 0.00% |
| 451 - Department of Banking | \$ 4,577.48 | 0.01% | 0.00% |
| 452 - Department of Licensing and Regulation | \$ 16,846.41 | 0.02% | 0.00% |
| 453 - Texas Workers' Compensation Commission | \$ 519,377.51 | 0.74% | 0.00% |
| 454 - Texas Department of Insurance | \$ 67,539.83 | 0.10% | 0.00% |
| 455 - Railroad Commission | \$ 76,769.53 | 0.11% | 0.00% |
| 457 - Texas Board of Public Accountancy | \$ 1,128.00 | 0.00% | 0.00% |
| 458 - Alcoholic Beverage Commission | \$ 160,369.66 | 0.23% | 0.00% |
| 459 - Texas Board of Architectural Examiners | \$ 47.00 | 0.00% | 0.00% |
| 465 - Texas Department of Commerce | \$ 757.42 | 0.00% | 0.00% |
| 466 - Office of Consumer Credit Commissioner | \$ 9,787.02 | 0.01% | 0.00% |
| 472 - Texas Structural Pest Control Board | \$ 898.97 | 0.00% | 0.00% |
| 473 - Public Utilities Commission of Texas | \$ 4,946.38 | 0.01% | 0.00% |
| 475 - Office of Public Utility Council | \$ 1,617.29 | 0.00% | 0.00% |
| 476 - Texas Racing Commission | \$ 129.00 | 0.00% | 0.00% |
| 479 - State Office of Risk Management | \$ 8,053.68 | 0.01% | 0.00% |
| 480 - Texas Department of Economic Development | \$ 2,015.00 | 0.00% | 0.00% |
| 501 - Texas Department of Health | \$ 1,733,918.74 | 2.48% | 1.67% |
| 505 - Cosmetology Commission | \$ 82,609.76 | 0.12% | 0.00% |
| 507 - Board of Nurse Examiners | \$ 35,296.02 | 0.05% | 0.00% |
| 508 - Board of Chiropractic Examiners | \$ 43.50 | 0.00% | 0.00% |
| 513 - Texas Funeral Service Commission | \$ 66.00 | 0.00% | 0.00% |
| 515 - Board of Pharmacy | \$ 1,057.54 | 0.00% | 0.00% |
| 517 - Texas Commission on Alcohol and Drug Abuse | \$ 10,185.47 | 0.01% | 0.00% |
| 529 - Health and Human Services Commission | \$ 35,711.93 | 0.05% | 0.00% |
| 530 - Department of Family and Protective Services | \$ 1,480,289.88 | 2.12% | 0.82% |
| 532 - Interagency Council on Early Childhood Intervention | \$ 1,511.70 | 0.00% | 0.00% |
| 533 - Executive Council of Physical and Occupational Therapy Examiners | \$ 6,383.75 | 0.01% | 0.00% |
| 551 - Department of Agriculture | \$ 67,242.67 | 0.10% | 0.00% |
| 554 - Texas Animal Health Commission | \$ 46,531.30 | 0.07% | 0.00% |
| 580 - Water Development Board | \$ 20,186.41 | 0.03% | 1.73% |
| 582 - Texas Department of Environmental Quality | \$ 205,894.87 | 0.29% | 0.00% |
| 592 - Texas State Soil and Water Conservation Board | \$ 318.00 | 0.00% | 0.00% |
| 655 - Texas Department of Mental Health and Mental Retardation | \$ 15,222,224.38 | 21.76% | 0.00% |
| 665 - Texas Juvenile Probation Commission | \$ 17,560.40 | 0.03% | 0.00% |

Summary of Losses - By Agency

FY 2003

| Agency Name | Workers' Compensation | Property | |
|---|-----------------------|--------------|--------|
| 694 - Texas Youth Commission | \$ 6,963,271.20 | \$5,413.00 | 9.95% |
| 696 - Texas Department of Criminal Justice | \$ 24,252,791.08 | \$41,920.09 | 34.67% |
| 701 - Texas Education Agency | \$ 60,199.03 | | 0.09% |
| 717 - Texas Southern University | \$ 318,221.89 | | 0.45% |
| 719 - Texas State Technical College System | \$ 155,614.92 | | 0.22% |
| 730 - University of Houston | \$ 703,208.99 | \$167,970.23 | 1.01% |
| 731 - Texas Woman's University | \$ 346,240.43 | \$11,000.00 | 0.49% |
| 733 - Texas Tech University | \$ 976,283.11 | \$43,225.65 | 1.40% |
| 734 - Lamar University at Beaumont | \$ 326,577.45 | | 0.47% |
| 735 - Midwestern State University | \$ 121,911.99 | \$15,484.35 | 0.17% |
| 737 - Angelo State University | \$ 28,103.00 | | 0.04% |
| 739 - Texas Tech University Health Science Center | \$ 1,255,520.87 | \$19,031.41 | 1.79% |
| 751 - East Texas State university | \$ 39,348.70 | | 0.06% |
| 752 - University of North Texas | \$ 284,780.65 | \$19,703.92 | 0.41% |
| 753 - Sam Houston State University | \$ 256,707.36 | \$15,819.00 | 0.37% |
| 754 - Texas State University - San Marcos | \$ 268,975.68 | \$10,000.00 | 0.38% |
| 755 - Stephen F. Austin State University | \$ 279,881.17 | \$24,074.26 | 0.40% |
| 756 - Sul Ross State University | \$ 33,557.60 | | 0.05% |
| 757 - West Texas State University | \$ 607.52 | | 0.00% |
| 759 - University of Houston - Clear Lake | \$ 63,980.87 | | 0.09% |
| 763 - University of North Texas Health Science Center at Fort Worth | \$ 235,986.63 | \$22,053.55 | 0.34% |
| 765 - University of Houston - Victoria | \$ 11,395.67 | | 0.02% |
| 767 - Southwest Collegiate Institute for the Deaf | \$ 11,598.08 | | 0.02% |
| 771 - School for the Blind and Visually Impaired | \$ 100,939.68 | | 0.14% |
| 772 - School for the Deaf | \$ 188,841.86 | | 0.27% |
| 781 - Texas Higher Education Coordinating Board | \$ 9,474.60 | | 0.01% |
| 783 - University of Houston System | \$ 4,191.00 | \$49,663.26 | 0.01% |
| 784 - University of Houston - Downtown | \$ 44,890.27 | \$15,040.82 | 0.06% |
| 787 - Lamar State College - Orange | \$ 168.38 | | 0.00% |
| 788 - Lamar State College - Port Arthur | \$ 46,154.03 | | 0.07% |
| 789 - Lamar University Institute of Technology | \$ 1,216.29 | | 0.00% |
| 802 - Parks and Wildlife Department | \$ 666,519.85 | \$130,001.28 | 0.95% |
| 808 - Texas Historical Commission | \$ 41,107.94 | | 0.06% |
| 809 - State Preservation Board | \$ 42,975.12 | | 0.06% |
| 990 - Unassigned - Includes Off-duty Peace Officers | \$ 15,317.38 | | 0.02% |

Summary of Losses - By Agency

FY 2003

| Agency Name | Workers' Compensation | Property |
|-------------|-----------------------|----------------|
| CSCD | \$ 1,443,054.68 | 0.00% |
| | \$ 69,950,824.81 | 100.00% |
| | | \$1,076,623.96 |
| | | 100.00% |

Summary of Losses - By Agency

Fiscal Year 2004

| Agency Name | Workers' Compensation | Property |
|---|-----------------------|--------------|
| 101 - Texas Senate | \$ 9,650.82 | \$5,875.42 |
| 102 - House of Representatives | \$ 69,257.81 | |
| 103 - Texas Legislative Council | \$ 8,765.99 | \$151,384.25 |
| 212 - Office of Court Administration | \$ 1,372.66 | |
| 213 - Office of the State Prosecuting Attorney | \$ 497.42 | |
| 221 - 1st Court of Appeals | \$ 6,356.62 | |
| 222 - 2nd Court of Appeals | \$ 20,084.26 | |
| 241 - Comptroller's Judiciary S | \$ 400,932.80 | |
| 301 - Office of the Governor | \$ 2,526.20 | |
| 302 - Office of the Attorney General | \$ 569,895.99 | \$5,142.45 |
| 303 - Texas Building and Procurement Commission | \$ 326,494.77 | |
| 304 - Comptroller of Public Accounts | \$ 104,302.41 | |
| 305 - General Land Office | \$ 93,174.80 | |
| 306 - Texas State Library and Archives Commission | \$ 15,878.20 | |
| 307 - Secretary of State | \$ 10,458.33 | |
| 313 - Department of Information Resources | \$ 1,503.45 | \$5,221.00 |
| 318 - Texas Commission for the Blind | \$ 44,934.37 | \$12,009.00 |
| 320 - Texas Workforce Commission | \$ 686,865.85 | \$239,942.27 |
| 323 - Teacher Retirement System | \$ 25,455.57 | |
| 324 - Department of Human Services | \$ 2,616,719.05 | \$23,455.45 |
| 327 - Employees Retirement System | \$ 63.00 | |
| 329 - Real Estate Commission | \$ 189.56 | |
| 330 - Texas Rehabilitation Commission | \$ 349,414.68 | |
| 332 - Texas Department of Housing and Community Affairs | \$ 31,902.75 | |
| 335 - Texas Commission for the Deaf and Hard of Hearing | \$ 523.15 | |
| 357 - Office of Rural Community Affairs | \$ 31,420.56 | |
| 360 - State Office of Administrative Hearings | \$ 4,112.55 | |
| 362 - Texas Lottery Commission | \$ 25,002.83 | |
| 367 - Telecommunication Infrastructure Fund Board | \$ 599.71 | \$6,282.00 |
| 401 - Adjutant General's Department | \$ 216,725.30 | |
| 405 - Department of Public Safety | \$ 2,260,072.44 | \$116,324.34 |
| 406 - Texas Military Facility Commission | \$ 22,130.42 | |
| 410 - Criminal Justice Policy Council | \$ - | \$62,965.00 |
| 451 - Department of Banking | \$ 516.43 | |
| 452 - Department of Licensing and Regulation | \$ 10,923.85 | |

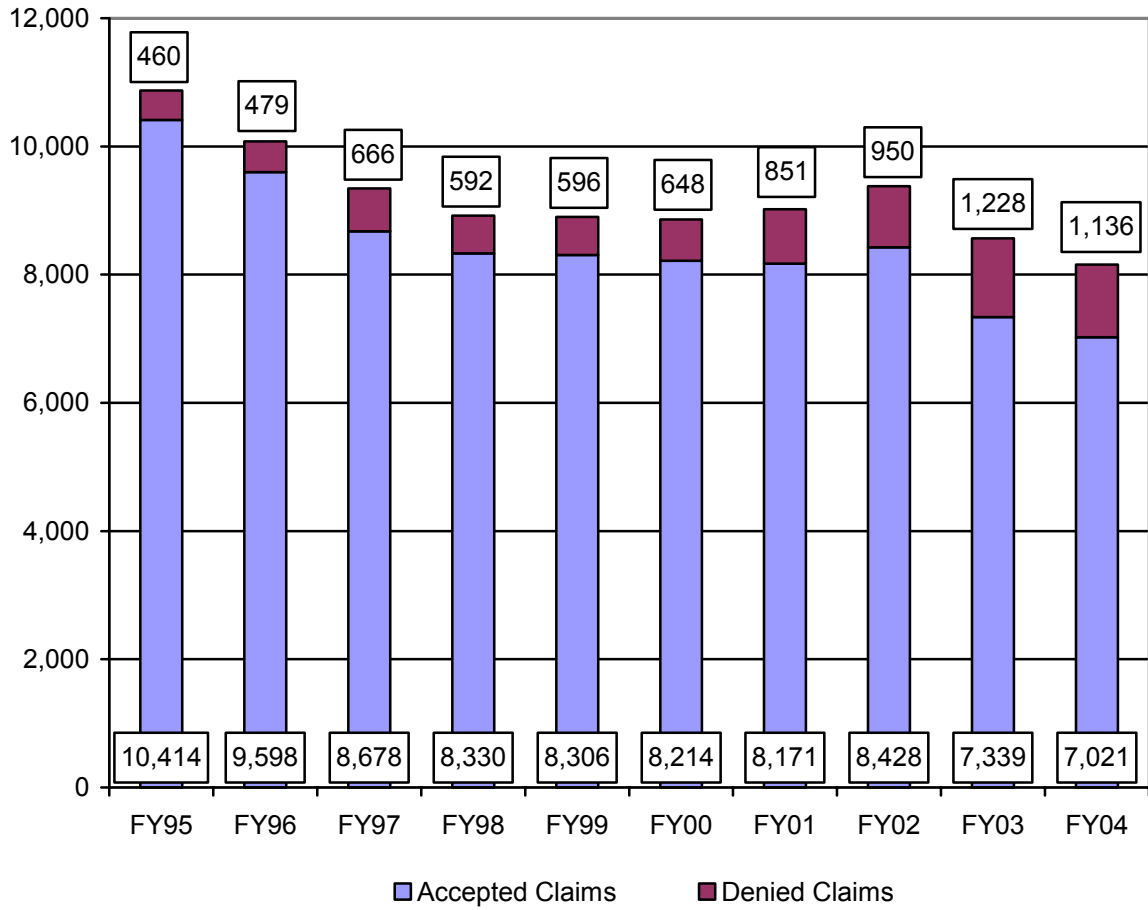
Summary of Losses - By Agency Fiscal Year 2004

| Agency Name | Workers' Compensation | Property | |
|--|-----------------------|----------|--------------|
| 453 - Texas Workers' Compensation Commission | \$ 280,707.96 | 0.50% | 0.00% |
| 454 - Texas Department of Insurance | \$ 87,883.57 | 0.16% | 0.00% |
| 455 - Railroad Commission | \$ 55,099.06 | 0.10% | 0.00% |
| 457 - Texas Board of Public Accountancy | \$ 3,564.56 | 0.01% | 0.00% |
| 458 - Alcoholic Beverage Commission | \$ 113,303.97 | 0.20% | 0.00% |
| 460 - Texas Board of Professional Engineers | \$ 2,367.26 | 0.00% | 0.00% |
| 465 - Texas Department of Commerce | \$ 584.65 | 0.00% | 0.00% |
| 466 - Office of Consumer Credit Commissioner | \$ 6,316.66 | 0.01% | 0.00% |
| 472 - Texas Structural Pest Control Board | \$ 1,587.24 | 0.00% | 0.00% |
| 473 - Public Utilities Commission of Texas | \$ 2,980.50 | 0.01% | 0.00% |
| 475 - Office of Public Utility Council | \$ 3,092.56 | 0.01% | 0.00% |
| 478 - Research & Oversight Council | \$ - | 0.00% | 0.70% |
| 479 - State Office of Risk Management | \$ 586.00 | 0.00% | 0.00% |
| 480 - Texas Department of Economic Development | \$ 300.00 | 0.00% | 0.00% |
| 501 - Texas Department of Health | \$ 827,162.53 | 1.48% | 0.00% |
| 505 - Cosmetology Commission | \$ 79,151.59 | 0.14% | 0.00% |
| 507 - Board of Nurse Examiners | \$ 26,957.32 | 0.05% | 0.00% |
| 515 - Board of Pharmacy | \$ 8,102.91 | 0.01% | 0.00% |
| 517 - Texas Commission on Alcohol and Drug Abuse | \$ 2,220.15 | 0.00% | 0.00% |
| 529 - Health and Human Services Commission | \$ 86,578.98 | 0.15% | 0.00% |
| 530 - Department of Family and Protective Services | \$ 1,466,611.27 | 2.62% | 1.04% |
| 532 - Interagency Council on Early Childhood Intervention | \$ 1,083.15 | 0.00% | 0.00% |
| 551 - Department of Agriculture | \$ 33,569.73 | 0.06% | 0.00% |
| 554 - Texas Animal Health Commission | \$ 35,028.32 | 0.06% | 0.00% |
| 580 - Water Development Board | \$ 4,473.49 | 0.01% | 0.00% |
| 582 - Texas Department of Environmental Quality | \$ 152,105.51 | 0.27% | 2.03% |
| 655 - Texas Department of Mental Health and Mental Retardation | \$ 12,020,185.84 | 21.51% | 1.38% |
| 665 - Texas Juvenile Probation Commission | \$ 19,664.03 | 0.04% | 0.00% |
| 694 - Texas Youth Commission | \$ 5,666,913.30 | 10.14% | 0.34% |
| 696 - Texas Department of Criminal Justice | \$ 20,265,840.04 | 36.27% | 4.59% |
| 701 - Texas Education Agency | \$ 36,488.07 | 0.07% | 0.00% |
| 717 - Texas Southern University | \$ 296,070.30 | 0.53% | 0.00% |
| 719 - Texas State Technical College System | \$ 186,204.85 | 0.33% | 0.30% |
| 730 - University of Houston | \$ 547,314.69 | 0.98% | 8.93% |
| 731 - Texas Woman's University | \$ 193,746.95 | 0.35% | 0.00% |
| | | | \$11,980.05 |
| | | | \$17,774.14 |
| | | | \$34,765.00 |
| | | | \$23,561.44 |
| | | | \$5,825.73 |
| | | | \$78,615.60 |
| | | | \$5,174.00 |
| | | | \$152,929.93 |

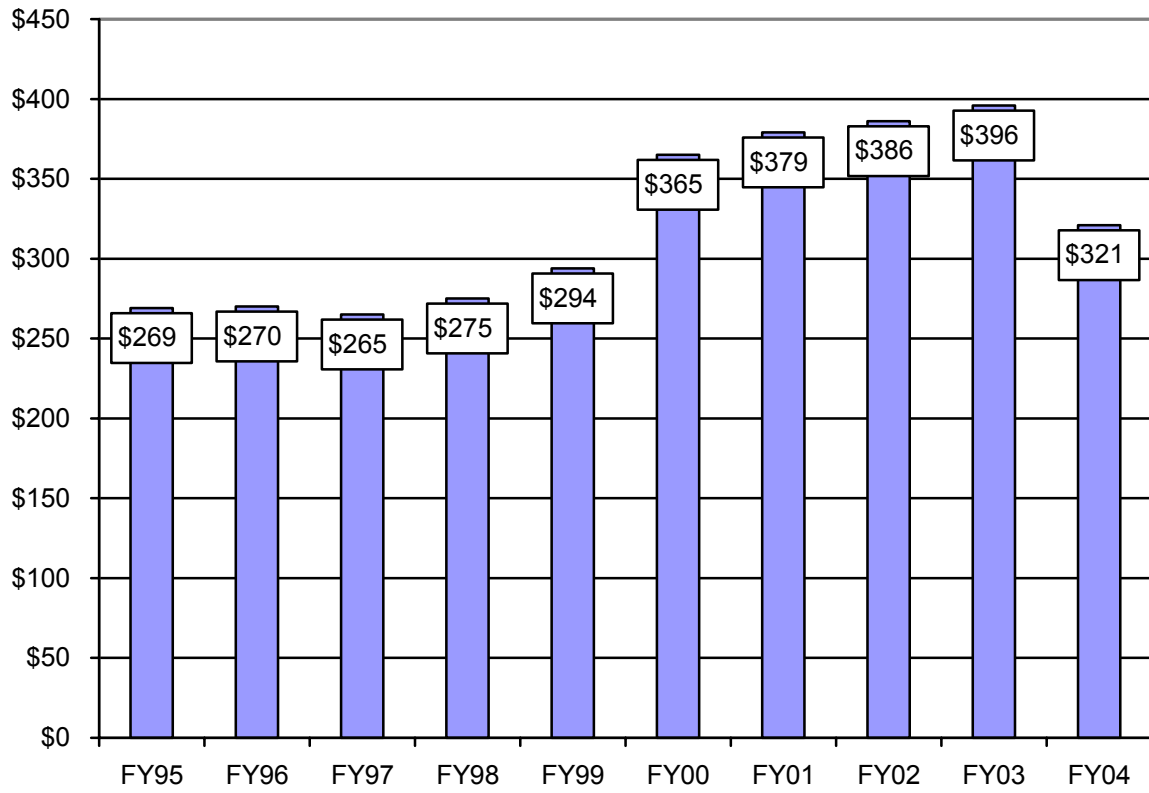
Summary of Losses - By Agency Fiscal Year 2004

| Agency Name | Workers' Compensation | Property |
|---|-----------------------|----------------|
| 733 - Texas Tech University | \$ 808,863.93 | \$34,857.80 |
| 734 - Lamar University at Beaumont | \$ 222,486.22 | \$21,742.75 |
| 735 - Midwestern State University | \$ 82,559.24 | |
| 737 - Angelo State University | \$ 30,267.06 | |
| 739 - Texas Tech University Health Science Center | \$ 641,508.75 | \$5,095.00 |
| 751 - East Texas State University | \$ 43,704.68 | |
| 752 - University of North Texas | \$ 213,855.86 | \$38,767.32 |
| 753 - Sam Houston State University | \$ 153,998.06 | \$20,496.32 |
| 754 - Texas State University - San Marcos | \$ 357,112.36 | \$18,670.84 |
| 755 - Stephen F. Austin State University | \$ 378,011.50 | \$27,828.99 |
| 756 - Sul Ross State University | \$ 15,673.73 | |
| 757 - West Texas State University | \$ 1,491.10 | |
| 759 - University of Houston - Clear Lake | \$ 86,487.32 | |
| 763 - University of North Texas Health Science Center at Fort Worth | \$ 186,298.96 | \$45,623.11 |
| 765 - University of Houston - Victoria | \$ 735.89 | |
| 767 - Southwest Collegiate Institute for the Deaf | \$ 11,821.12 | |
| 771 - School for the Blind and Visually Impaired | \$ 106,672.92 | \$38,635.00 |
| 772 - School for the Deaf | \$ 166,858.12 | |
| 781 - Texas Higher Education Coordinating Board | \$ 10,402.73 | \$10,714.00 |
| 783 - University of Houston System | \$ 9,422.97 | |
| 784 - University of Houston - Downtown | \$ 58,679.83 | \$6,169.00 |
| 787 - Lamar State College - Orange | \$ 19,380.79 | |
| 788 - Lamar State College - Port Arthur | \$ 13,314.07 | |
| 789 - Lamar University Institute of Technology | \$ 10,317.18 | \$23,759.00 |
| 802 - Parks and Wildlife Department | \$ 696,683.18 | \$461,275.63 |
| 808 - Texas Historical Commission | \$ 27,313.48 | |
| 809 - State Preservation Board | \$ 39,909.00 | |
| 990 - Unassigned - Includes Off-duty Peace Officers | \$ 34,041.14 | |
| CSCD | \$ 961,823.31 | |
| | \$ 55,872,266.11 | \$1,712,861.83 |
| | 100.00% | 100.00% |

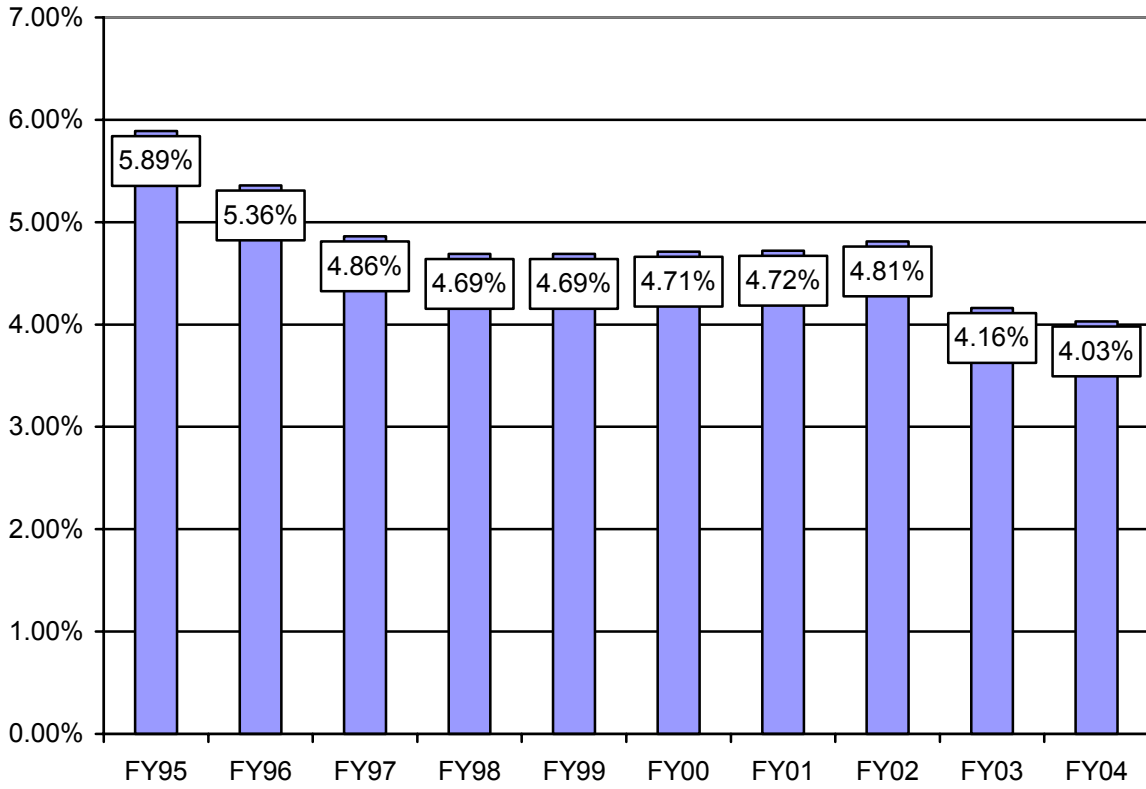
Workers' Compensation Claims



Workers' Compensation Losses: Cost Per FTE



Injury Frequency Rate



Recovery Summary FY 2003-2004

SORM collected the funds as detailed below in the subrogation program involving third-party liability reimbursements for workers' compensation claims paid and in court-ordered restitutions.

| | FY 2003 | FY 2004 |
|--------------|---------------------|-----------------------|
| September | \$8,473.75 | \$21,494.42 |
| October | \$60,984.88 | \$17,081.88 |
| November | \$1,430.55 | \$83,728.25 |
| December | \$81,604.25 | \$219,305.81 |
| January | \$240,491.89 | \$30,196.80 |
| February | \$40,289.35 | \$26,710.69 |
| March | \$40,624.73 | \$160,190.74 |
| April | \$298,887.38 | \$2,141.89 |
| May | \$28,180.50 | \$71,385.11 |
| June | \$4,217.21 | \$26,845.26 |
| July | \$95,087.38 | \$555,935.31 |
| August | \$37,995.55 | \$6,377.54 |
| Total | \$938,267.42 | \$1,221,393.70 |

State Agency Non-Workers' Compensation Claims and Losses

Insurance Policies FY 2003

| Type of Policy | # of Policies | Total Premiums | # of Claims | Amount Paid |
|---|---------------|--------------------|-------------|------------------|
| Professional Liability | 16 | \$235,818 | 13 | \$160,000 |
| Surety Bonds | 11 | \$3,052 | 0 | \$0 |
| Directors and Officers/Employment Practices Liability | 26 | \$1,234,957 | 11 | \$9,000 |
| General Liability | 13 | \$270,043 | 5 | \$727 |
| Property | 52 | \$5,973,503 | 35 | \$370,446 |
| Volunteer | 21 | \$20,468 | 0 | \$0 |
| Automobile | 20 | \$1,273,445 | 184 | \$203,353 |
| Crime (Employee Dishonesty) | 26 | \$94,799 | 18 | \$35,166 |
| Aircraft | 1 | \$236,777 | 0 | \$0 |
| Total | 186 | \$9,342,862 | 266 | \$778,692 |

Insurance Policies FY 2004

| Type of Policy | # of Policies | Total Premiums | # of Claims | Amount Paid |
|---|---------------|--------------------|-------------|------------------|
| Professional Liability | 11 | \$738,704 | 1 | \$0 |
| Surety Bonds | 4 | \$484 | 0 | \$0 |
| Directors and Officers/Employment Practices Liability | 22 | \$1,411,106 | 28 | \$3,971 |
| General Liability | 11 | \$220,736 | 12 | \$7,985 |
| Property | 42 | \$5,606,198 | 8 | \$6,985 |
| Volunteer | 7 | \$50,659 | 0 | \$0 |
| Automobile | 19 | \$1,198,148 | 76 | \$85,267 |
| Crime (Employee Dishonesty) | 13 | \$15,628 | 20 | \$199,004 |
| Aircraft | 1 | \$212,534 | 0 | \$0 |
| Total | 130 | \$9,454,197 | 145 | \$303,212 |

Non-Workers' Compensation Claims Frequency by Loss Type⁵

| Claim Type | FY 2003 | FY 2004 |
|------------------------|--------------|------------|
| Accident Insurance | 0 | 0 |
| Auto Liability | 301 | 115 |
| Auto Physical Damage | 249 | 326 |
| Boiler and Machinery | 2 | 0 |
| Crime | 24 | 29 |
| Directors and Officers | 127 | 63 |
| Electronic Data | 33 | 38 |
| Employment Practices | 227 | 82 |
| Environmental | 0 | 1 |
| Excess Liability | 21 | 0 |
| General Liability | 288 | 167 |
| Inland Marine | 5 | 5 |
| Professional Liability | 47 | 8 |
| Property Insurance | 103 | 41 |
| Total | 1,427 | 875 |

⁵ FY 2004 SORM 200 data, Section 2, Part 2

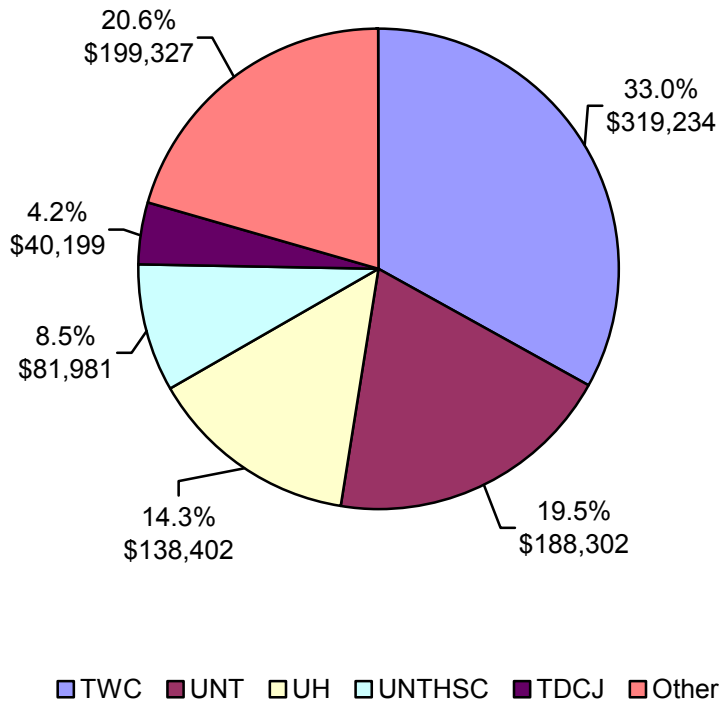
Non-Workers' Compensation Settlements by Loss Type⁶

| Claim Type | FY 2003 Settlement Amount | FY 2004 Settlement Amount |
|---------------------------|------------------------------|------------------------------|
| Accident Insurance | \$0 | \$0 |
| Auto Liability | \$331,272 | \$297,519 |
| Auto Physical Damage | \$178,621 | \$340,246 |
| Boiler and Machinery | \$0 | \$0 |
| Crime | \$35,166 | \$205,869 |
| Directors and Officers | \$5,931 | \$0 |
| Electronic Data | \$88,495 | \$88,448 |
| Employment Practices | \$212,750 | \$601,606 |
| Environmental | \$0 | \$0 |
| Excess Liability | \$0 | \$0 |
| General Liability | \$334,709 | \$38,847 |
| Inland Marine | \$10,079 | \$3,635 |
| Professional Liability | \$213,037 | \$126,453 |
| Property Insurance | \$655,084 | \$942,433 |
| Total | \$2,065,144 | \$2,645,056 |

⁶ FY 2004 SORM 200 data, Section 2, Part 2

Property Losses - FY 2003

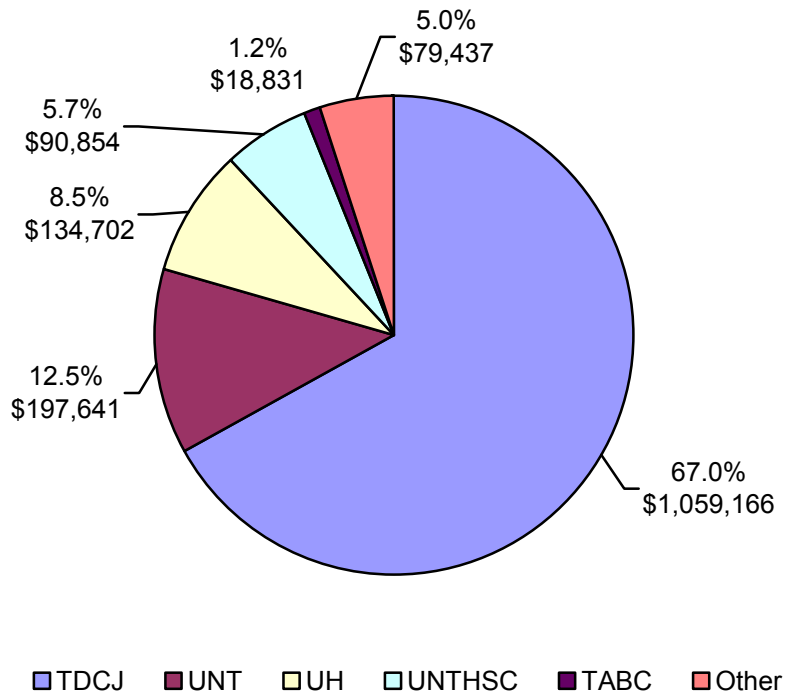
Total Property Losses: \$967,445



Source: FY 2003 SORM 200 data, Section 2, Part 2

Property Losses - FY 2004

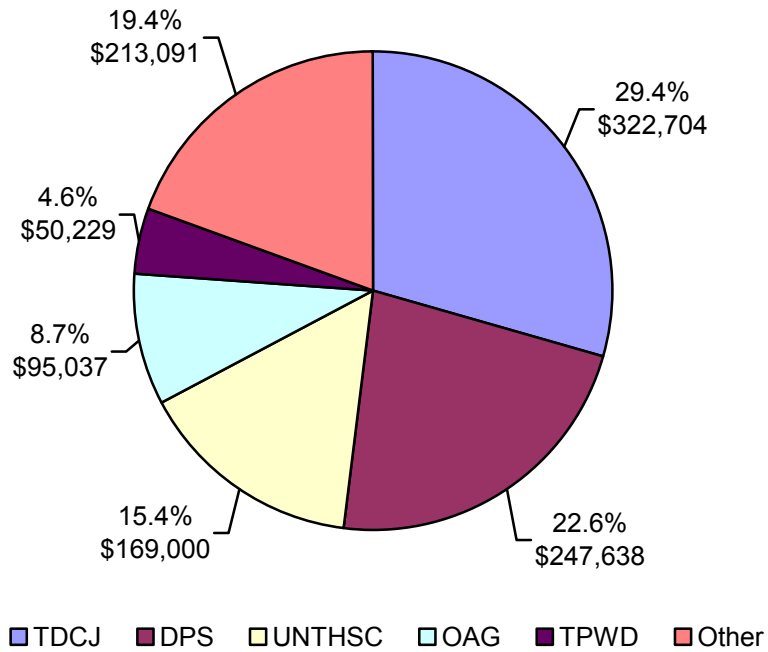
Total Property Losses: \$1,580,631



Source: FY 2004 SORM 200 data, Section 2, Part 2

Liability Losses - FY 2003

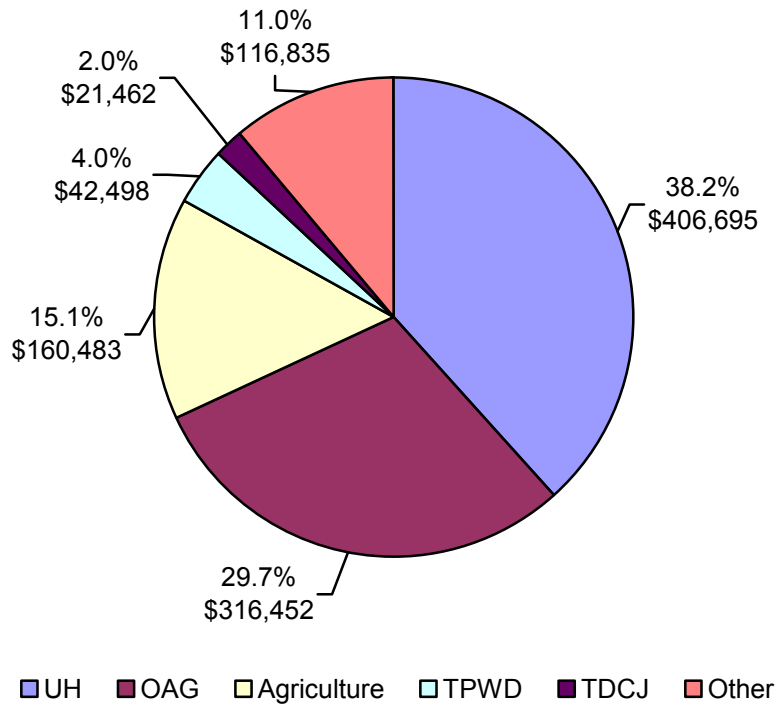
Total Liability Losses: \$1,097,699



Source: FY 2003 SORM 200 data, Section 2, Part 2

Liability Losses - FY 2004

Total Liability Losses: \$1,064,425



Source: FY 2004 SORM 200 data, Section 2, Part 2

412.032(b)(2) Non-Complying Agency Reporting

Texas Labor Code §412.032(b)(2) requires SORM report to the Legislature the identification of each state agency that has not complied with the risk management guidelines and reporting requirements of Texas Labor Code, Chapter 412. The table below identifies the agencies that were noncompliant with the statutory and derivative administrative requirements.

| Agency | Citation | Issue | Details |
|-----------------------------|--|---|--|
| University of North Texas | <p>28 TAC 252.303(c)</p> <p>Texas Labor Code §§412.011(e), 412.051(a)(2), 412.051(b); 28 TAC 252.302(a), (c)</p> | <p>Untimely filing of request for exception</p> <p>Unauthorized purchase of denied insurance policy</p> | <p>Agencies are required to submit applications for exemption no later than 30 days prior to the inception date of the policy. Agency submitted less than 30 days prior to inception date.</p> <p>Although notified exception to purchase a non-approved policy was denied, agency proceeded with purchase. No notification of future intent for compliance.</p> |
| Midwestern State University | 28 TAC 252.303(c) | Untimely filing of request for exception | Agencies are required to submit applications for exemption no later than 30 days prior to the inception date of the policy. Agency submitted less than 30 days prior to inception date. |

| | | | |
|--|--|---|---|
| Midwestern State University (Continued) | Texas Labor Code §§412.011(e), 412.051(a)(2), 412.051(b); 28 TAC 252.302(a), (c) | Unauthorized purchase of denied insurance policy | Although notified exception to purchase a non-approved policy was denied, agency proceeded with purchase. No notification of future intent for compliance. |
| University of Houston* *Currently in compliance | 28 TAC 252.303(c) Texas Labor Code §§412.011(e), 412.051(b); 28 TAC 252.302(a), (c) | Untimely filing of request for exception Unauthorized purchase of denied insurance policy | Agencies are required to submit applications for exemption no later than 30 days prior to the inception date of the policy. Agency submitted less than 30 days prior to inception date. Agency initially purchased non-approved policy. *After notification of noncompliance, agency purchased approved policy. |
| Texas Woman's University | Texas Labor Code §§412.011(e), 412.051(a)(2), 412.051(b); 28 TAC 252.302(a)-(d) | Failure to file application or request for exception | Agency purchased policy without notifying the Office. Agency has been notified and indicates future compliance. |
| Health and Human Services Commission* *Extenuating circumstances - consolidation | 28 TAC 252.201(a) | No agency risk management program which includes a safety and health program and a return-to-work program | *Agency staff currently working with Office staff in designing and implementing a risk management plan for all components. |

| | | | |
|---------------------------|----------------------------|---|--|
| Teacher Retirement System | Texas Labor Code §412.0121 | Failure to enter into an interagency contract with the Office to pay the costs incurred by the Office in administering Chapter 412 for the benefit of that state agency | The Office paid claims but agency failed to execute interagency agreement. Agency and the Office are discussing current agency concerns regarding the trust fund nature of its assets and alleged conflict with statutory subrogation provisions. |
|---------------------------|----------------------------|---|--|



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State Office of Risk Management Overview

Amendments to Pages 1 through 7 start here

The 2003-2004 biennium has seen growing stakeholder dissatisfaction in Texas with the workers' compensation system as a whole. Reports from independent research organizations, interest groups, and interim legislative committees have each detailed the crisis in rising costs for employers and poor outcomes for injured workers. Changes dictated by legislative reforms and Texas Workers' Compensation Commission (TWCC) rulemaking have required carriers to make significant investments to ensure compliance with changing rules and fee schedules.

The biennium has presented difficult challenges for the State's self-insured workers' compensation program administered by the State Office of Risk Management (Office), but it has also been a time of opportunity for noteworthy improvement in the Office's programs.

WORKERS' COMPENSATION EXPENDITURES REDUCED IN 2004

For the first time in seven years, the cost of providing workers' compensation benefits for injured state employees went down in FY 2004. The total required to provide indemnity and medical benefits was \$14 million dollars less than FY 2003 and \$22 million less than the liability projected by the system's actuarial consultant.

The rapid decrease in expenditures is the result of a number of factors, including improved claims processing by the Office, improved safety practices on the part of client agencies, and greater accountability on the part of agencies for losses.

These improvements have directly translated into savings for state agencies and the state as a whole. The total assessments to state agencies for payment of claims costs for FY 2005 is \$19.4 million less than FY 2003 and \$21.7 million less than FY 2004. In addition, the Office will return to client agencies approximately \$15.5 million in unexpended funds from the FY 2004 assessments.

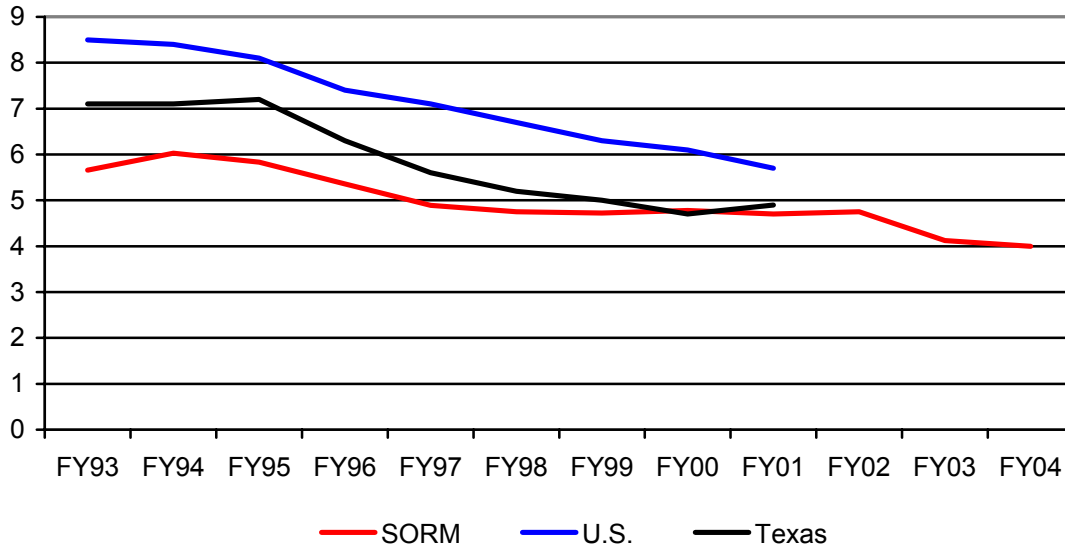
FEWER STATE EMPLOYEES INJURED EACH YEAR

New injuries to state employees have been significantly reduced during this biennium. On average, more than 1,000 fewer injuries have occurred annually for each of the previous two years than for the rest of the past decade. The Office attributes much of this reduction to significantly improved risk management and claims coordination efforts by covered agencies as a result of making those agencies more accountable for their injuries, as mandated by the Legislature.

The Office has supported agencies in this effort through increased agency visits, education, and assistance in implementing successful mitigating strategies at client agencies. The chart below compares the national and Texas statewide average injury frequency rate (IFR) to the average for the Office's program. IFR is a measure of the average number of injuries per 100 employees in a given year. While IFR data is not available for the U.S. or the state for 2002-2004, the Office's client agencies continued the downward IFR trend during that period,

finishing the year at 4.0 for FY 2004. This continuing reduction in IFR has contributed to the significant reduction in paid workers' compensation claims over the past two years.

U.S., Texas, and SORM IFR Rate History



Sources: Bureau of Labor Statistics, U.S. Department of Labor, Survey of Occupational Injuries and Illnesses in cooperation with the Texas Workers' Compensation Commission; SORM

STATE INSURANCE PURCHASING PROGRAM DEMONSTRATES SAVINGS

The Insurance Purchasing Program established by HB 1203, 77th Legislature, continued to expand in this biennium, and the Office has implemented four lines of sponsored insurance available to all covered state agencies: Directors' and Officers' with Employment Practices Liability, Short-Term Special Event General Liability, Automobile, and Volunteer policies. Savings as a result of centralizing these state insurance purchases exceeded a quarter of a million dollars for FY 2004 and savings are expected to continue to grow as new lines are evaluated and approved, or denied.

NEW STUDIES PROVIDE IMPORTANT BENCHMARKING DATA AND IDENTIFY WEAKNESSES IN PAST PERFORMANCE

The Texas Department of Insurance (TDI) conducted a study during the biennium in response to an interim charge on workers' compensation. This was the first study of its kind and the data revealed that while the Office's medical costs were similar to private sector expenditures, the medical costs in the Office's workers' compensation program during the calendar years of

1999, 2000, and 2001 were higher than the programs administered by the other self-insured state systems (University of Texas, Texas A&M University, and Texas Department of Transportation).

The study provided an opportunity for the Office to compare performance and identify differences between the programs that could account for the cost differentials. A number of factors were identified by the Office as influencing expenditures, including the lack of an implemented health care network in the Office's program, cumulative claims staff turnover of 108% percent from FY 1998 – 2000, lower adjuster salaries, and weaknesses in the Office's medical cost containment program.

The Office has taken steps to directly address these causative factors, including modification to claims procedures and organization, reinitiation of the proposal process for a health care network, and new FY 2005 contracts for medical cost containment services. These efforts and others are discussed in the "Core Components" section of this report.

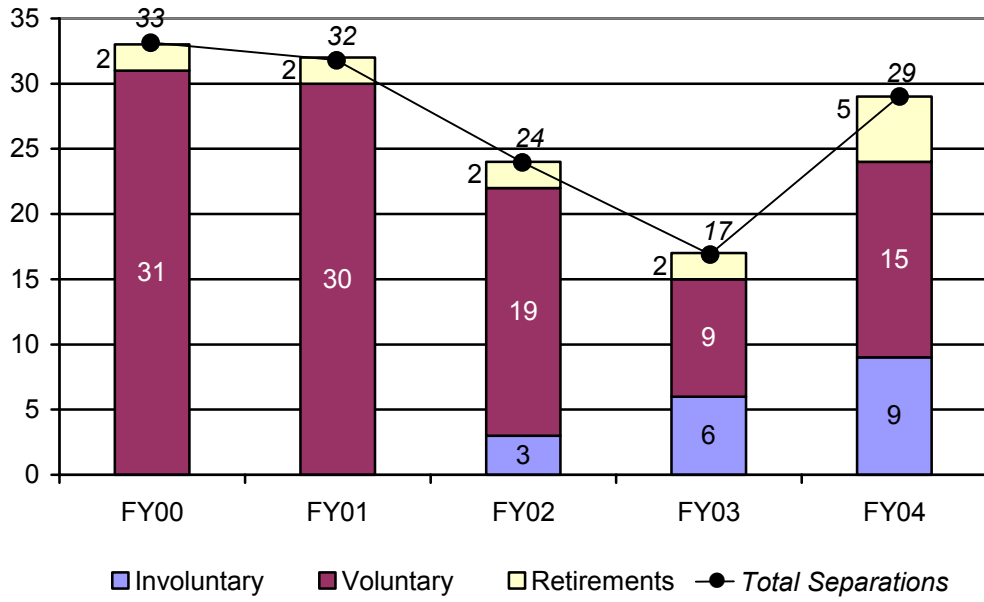
STAFF TURNOVER RE-EMERGES AS AREA OF CONCERN

Employee turnover at the Office increased from 13.8 percent in FY 2003 to 22.7 percent in FY 2004. To date in FY 2005 the Office has lost six claims adjusters (13 percent of the entire claims staff). This is largely a result of competition from private workers' compensation insurance carriers in the Austin/Central Texas market. The Office anticipates additional claims personnel losses as private carriers expand operations in the Austin region, closing the fiscal year at a projected 39 percent turnover in claims staff.

The Office's loss of tenured staff to the private sector is largely a function of higher salaries in that sector. According to "A Survey on Organizational Excellence" prepared by the University of Texas for the Office and the State Auditor's online exit interviews, the majority of the Office's claims staff leave the agency for higher salaries. An informal exit interview of claims adjusters leaving the Office confirmed an average salary increase of 22 percent more than available agency salaries.

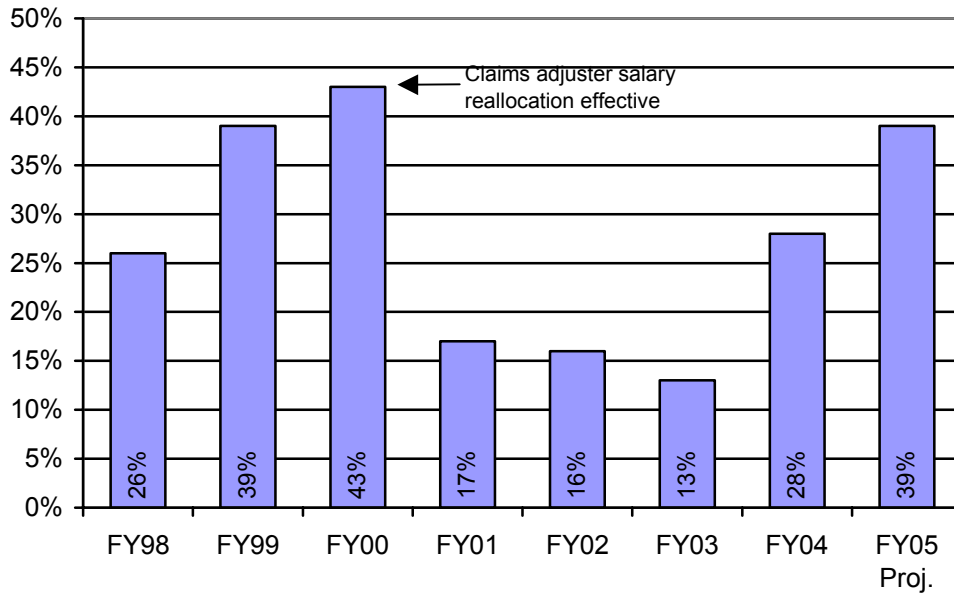
Turnover has been a significant historical concern, and the Office has consistently sought to retain and attract qualified staff by creating a positive work environment, by acknowledging professional achievement through reimbursement for work-related professional certification, supporting an active Employee Association, providing flexible and alternative work schedules, and other employee-friendly agency policies. Recognizing the significant draw of higher salaries in the Office's excessive turnover, the State Auditor's Office recommended significant adjuster reclassifications in FY 2000, which resulted in a temporary sharp decrease in claims staff turnover rates. However, the re-emergence of significant salary competition is increasing turnover once again.

SORM Turnover



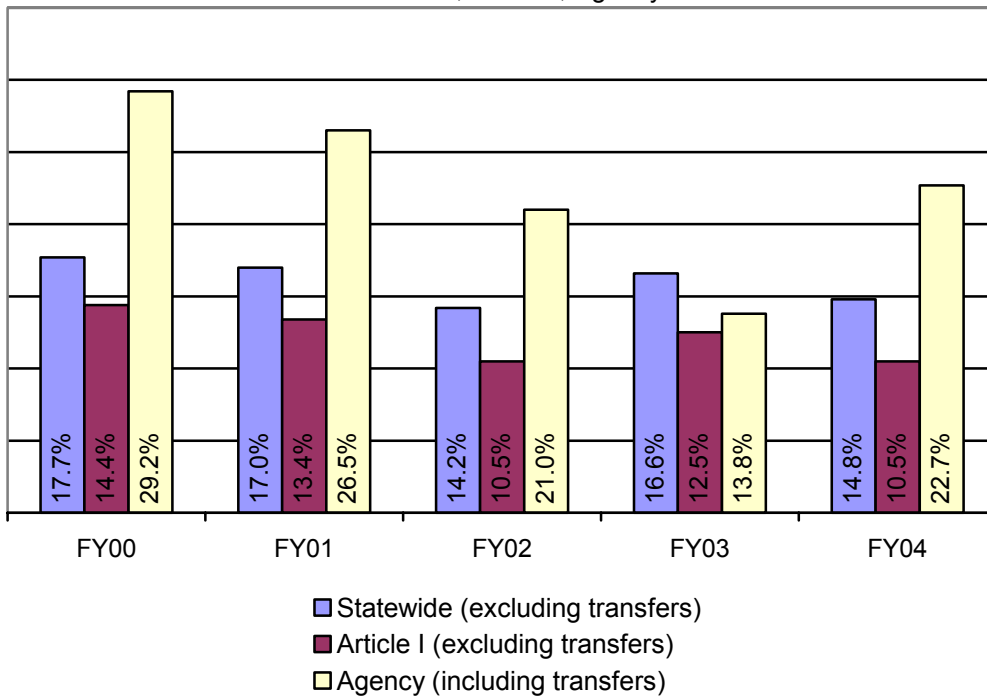
Source: State Auditor's Office

Claims Staff Turnover



Turnover Comparison

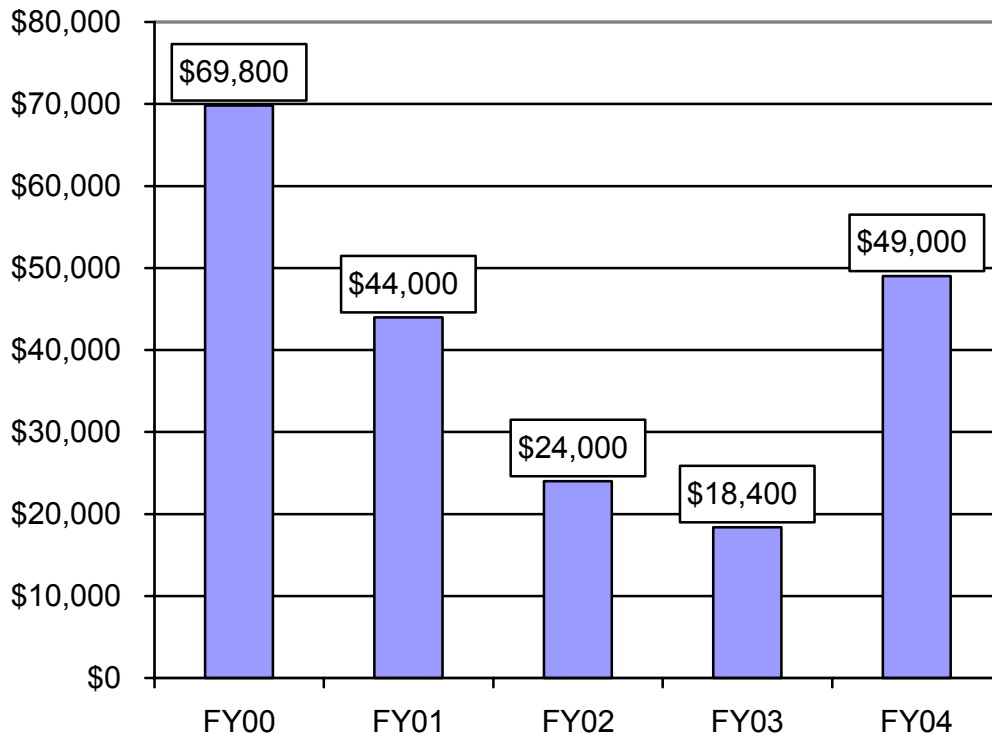
Statewide, Article I, Agency



Source: State Auditor's Office

The loss of institutional knowledge as a result of staff turnover has increased the cost of administering SORM's statutory programs in the short term. The cost to replace employees more than doubled in FY 2004, exceeding \$49,000.¹

Annual Cost of Turnover



¹ The methodology used to determine the cost of turnover was the same as used by the State Auditor's Office in its *FY 2004 Employee Turnover Statistics*