



Richmond Office of the  
**CITY AUDITOR**

**OFFICIAL GOVERNMENT REPORT**



**AUDIT OF:**  
**Richmond Public Schools**  
**WORKERS' COMPENSATION**  
**PROGRAM**

**Report Issued: August 18, 2014**

**Report Number: 2015-03**

Richmond City Council Office of the City Auditor | Richmond City Hall | 900 E. Broad Street, Suite 806 | Richmond, Virginia 23219 U.S.A. | 804.646.5616 (tel)

*Committed to increasing government efficiency, effectiveness  
and accountability on behalf of the Citizens of Richmond.*

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# Richmond City Council

The Voice of the People

Richmond, Virginia

## Office of the City Auditor

### Executive Summary

August 18, 2014

The Honorable Members of the Richmond Public School Board

#### **Subject: Richmond Public Schools – Workers’ Compensation Audit Report**

The City Auditor’s Office has completed an audit of the Richmond Public Schools (RPS) Workers’ Compensation Program within the Benefits and Risk Management Department. Risk Management directs and oversees the planning, development and administration of the Workers’ Compensation Program. Presently, this Department provides broad guidance, management and oversight of workers’ compensation claims, but not limited to:

- providing guidance and direction to staff and external vendors
- approving denials of claims
- receiving/processing recovery checks
- jointly reviewing claims with the Third Party Administrator (TPA)
- approving requests for surveillance and field case management services

Risk Management engages and places heavy reliance on an external insurance consultant to provide all services and assistance pertaining to stop loss coverage and limits.

#### **Salient Findings**

- Contractual agreements with external workers’ compensation vendors do not adequately protect RPS’ interests. Risk Management has an over reliance on the third party administrator and external consultants to administer, provide analytics and oversight of workers’ compensation claims, which may not allow for proper contract administration and potentially increase healthcare costs.
- Risk Management is not performing safety inspections or re-inspections of facilities. This may lead to safety hazards not being found and remediated.

- Failure to identify, question, and dispute incorrect / inappropriate provider healthcare charges lead to unnecessary healthcare expenses.
- Lack of independence of physicians serving on the workers' compensation panel could lead to claimants not being referred to the most cost effective alternatives for treatment of injuries. This can result in unnecessary inflated healthcare costs.

A written response to this report was requested from RPS' Administration, however, due to lack of staffing, responses could not be provided.

The City Auditor's Office appreciates the cooperation of the Richmond Public Schools' staff. Please contact me for questions and comments on this report.

Sincerely,

*Umesh Dalal*

Umesh Dalal, CPA, CIA, CIG  
City Auditor

c: Dr. Dana Bedden, Superintendent  
The Richmond City Audit Committee  
The Richmond City Council

## COMPREHENSIVE LIST OF RECOMMENDATIONS

#		PAGE
1	Amend the contractual agreement with the TPA to require the TPA to: <ul style="list-style-type: none"><li>a) Issue itemized billing statements for all goods and services furnished by the TPA and/or its affiliates to allow proper evaluation of charges.</li><li>b) Cease issuing payments to itself for goods and services delivered by the TPA and/or its affiliates. Instead, require Risk Management to approve the charges for appropriateness and disburse it to the TPA.</li><li>c) Pre-certify/approve the delivery of all healthcare provider goods and services such as MRI, CT scans, etc.</li><li>d) Perform line item audits for all billing statements which equal or exceed \$500.</li><li>e) Submit written itemized requests/costs for all managed care services to the Risk Manager for documented approval prior to the delivery of these services.</li><li>f) Encourage the use of non-hospital network providers and mail order pharmacy services.</li><li>g) Detect, dispute and satisfactorily resolve health care providers' billing errors.</li><li>h) Update the estimate of the expected total cost of qualified claims on or before the close of each calendar month.</li><li>i) Furnish the Risk Manager monthly, detailed "return to work" status report.</li><li>j) Require monthly filings for reimbursement of excess workers' compensation claims against "Stop Loss" coverage and provide a monthly report to the Risk Manager for approval.</li></ul>	15
2	The School Board needs to amend the Sick Leave Policy that permits sick leave to supplement workers' compensation payments to cap total payments to pre-injury net compensation.	16

## COMPREHENSIVE LIST OF RECOMMENDATIONS

- 3 Redefine and establish specific responsibilities for the Risk Manager and the Risk Management Department for the TPA contract administration, reporting requirements, deliverables, and performance measurements. 16
- 4 Assign the authority and responsibility for all safety inspections, re-inspections, remediation, correction of deficiencies etc. to Risk Management as follows: 16
  - a) require a semiannual uniform physical safety inspection of all schools, facilities, real estate owned or leased, equipment, etc. and report all findings and proposed corrective actions/costs.
  - b) maintain an automated composite inventory of all safety inspections, safety findings/deficiencies, estimated costs to correct, estimated completion date, date of remediation of deficiency, current status, re-inspection/approval.
  - c) require quarterly safety reports to the Superintendent.
- 5 Develop and implement written policies and procedures for: 16
  - a) Administering and reporting workers' compensation stop loss claims.
  - b) Conducting, preparing and monitoring of the following elements of safety inspections:
    - Due date of inspections
    - Number and frequency of inspections
    - Safety report's content and approval
    - Identification/remediation/re-inspections of deficiencies
- 6 Require the Risk Manager's approval of the commencement, modifications and terminations of indemnity benefits. 16
- 7 Assign Risk Management the responsibility for monitoring and requesting replenishment of funds to the workers' compensation bank account. 16

## COMPREHENSIVE LIST OF RECOMMENDATIONS

- |    |  |    |
|----|--|----|
| 8  | Require the Finance Department to prepare monthly reconciliations of the self-insured bank account.  | 16 |
| 9  | Engage an actuarial to validate and / or determine the valuation of the reserve for future workers' compensation claims liability as of the close of business of each fiscal year. | 16 |
| 10 | Prepare a monthly reconciliation of indemnity payments to payroll records.   | 16 |

## *Overview*

### *Introduction and Scope*

The City Auditor's Office has completed an audit of the Workers' Compensation Program within the Benefits and Risk Management Department of Richmond Public Schools (RPS). The audit covers the 12-month period ending June 30, 2013. The objectives of this audit were to:

- Evaluate the economy and efficiency of operations;
- Determine the existence and effectiveness of internal controls;
- Evaluate compliance with laws, regulations, policies; and procedures

The auditors conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that the auditors plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for their findings and conclusions based on the audit objectives. The auditors believe that the evidence obtained provides a reasonable basis for their findings and conclusions based on the objectives.

### *Methodology*

Auditors performed the following procedures to complete this audit:

- interviewed management and staff;
- reviewed and evaluated relevant policies and procedures, and tested for compliance;
- reviewed and analyzed workers' compensation data;
- reviewed Virginia Workers' Compensation Act;
- performed other tests as deemed necessary; and
- conducted a walkthrough of the Third Party Administrator's (TPA) operations.

### *Management Responsibility*

The RPS Management is responsible for ensuring that resources are managed properly and used in compliance with laws and regulations; RPS Programs are achieving their objectives; and services are being provided efficiently, effectively, and economically.

***Background***

On-the-job injuries in Virginia are governed by the Virginia Workers' Compensation Act (VWCA). The Virginia Workers' Compensation Commission (VWC) is a State of Virginia agency that oversees the resolution of workers' compensation claims brought before them. The VWCA requires that employers pay:

- All necessary medical costs from a job-related accident or illness
- Payments for lost wages at two thirds of gross pay (tax free).

Enforcement and interpretation of this law rests primarily with the VWC.

RPS provides workers' compensation benefits to its employees from a self-insured fund, administered through RPS' Benefits & Risk Management Department (Risk Management). Risk Management directs and oversees the planning, development and administration of the Workers' Compensation Program. Presently, this Department provides broad guidance, management and oversight of workers' compensation claims, but not limited to:

- providing guidance and direction to staff and external vendors
- approving denials of claims
- receiving/processing recovery checks
- jointly reviewing claims with the TPA
- approving requests for surveillance and field case management services

Since 2007, Benefits and Risk Management's staffing level has remained flat with three full time positions. The staff is augmented by three contracted positions staffed by outside agencies. Two of the three contracted positions are part -time positions.

RPS has and continues to limit its claims liability (stop loss) by purchasing high deductible indemnity insurance. The limit has gradually increased since 1999. During the audit period the limit was \$650,000. Any claim over the limit is born by the insurance company and not RPS. This means that RPS is accepting a larger risk by raising the stop loss limit. On June 30, 2013 RPS had five workers' compensation claims, which have exceeded the stop loss limit.

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***For work related injuries, the Virginia Workers Compensation Commission requires payment for medical and lost wages.***

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Risk Management engages and places heavy reliance on an external insurance consultant to provide all services and assistance pertaining to stop loss coverage and limits. Such services include:

- strategy development
- risk assessment
- specifications
- solicitation of quotes
- conducting negotiations
- reinsurance / stop loss limits
- assistance in evaluating quotations
- placement of insurance

As of June 30, 2013 the top 10 workers' compensation claims by expenditure, reserves, and total incurred costs were:

<i>Date of Injury</i>	<i>Type of Injury</i>	<i>FY 2013 Payments</i>	<i>(A) Total Paid to Date</i>	<i>(B) Reserves</i>	<i>(A&amp;B) Total Exposure</i>
3/12/2008	Contusions - or bruise	\$32,260	\$250,403	\$277,955	\$528,358
3/23/2004	Sprain/strain/dislocation	\$32,409	\$195,578	\$250,714	\$446,292
12/17/1992	Contusions - or bruise	\$22,498	\$193,737	\$217,762	\$411,499
2/16/2007	Contusions - or bruise	\$31,826	\$181,000	\$186,201	\$367,201
12/12/2007	Electric shock	\$50,857	\$227,551	\$116,684	\$344,235
6/11/2012	Sprain/strain/dislocation	\$167,212	\$167,308	\$44,703	\$212,011
4/25/2011	Contusions - or bruise	\$69,198	\$131,341	\$70,650	\$201,991
8/9/2011	Cut/laceration	\$34,292	\$87,851	\$94,436	\$182,287
7/3/2012	Sprain/strain/dislocation	\$138,120	\$138,120	\$43,033	\$181,153
9/9/2011	Sprain/strain/dislocation	\$9,904	\$71,490	\$108,449	\$179,939

Risk Management engages the services of a TPA to adjudicate, administer, mediate, and settle workers' compensation claims. The services provided by the TPA include:

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***RPS has a TPA for managing workers' compensation claims***

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- Receive information related to employees' injuries
- Make determination of validity of the employees' claims in compliance with VWC regulations
- Process valid claims, which are inclusive of indemnity and medical claims
- Conduct investigations, when necessary
- Pay benefits, expenses and adjusts or settles each qualified claim

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Both RPS and the City of Richmond (COR) use a TPA to administer and adjudicate workers' compensation claims. Although the services provided are similar, the pricing structure for TPA services varies as depicted in the following table:

<i>Description</i>	<i>COR</i>	<i>RPS</i>
<i>Flat Annual Fee</i>	<i>\$95,000 for first 590 claims ( \$161 per claim)</i>	<i>\$71,028 for the first 365 claims ( \$205 per claim)</i>
<i>Bill Review - Reasonable &amp; Customary , PPO Network</i>	<i>18% of total savings</i>	<i>25% of total savings</i>

The COR's TPA provides additional services at no extra cost such as subrogation, access to the TPA's computer system, clinical consultations, etc. However, RPS' TPA charge extra for these claims data services.

In addition to the flat fee for administering workers' compensation claims, the TPA's contract with RPS provides for additional fees. The majority of these fees are on a contingency (percentage of savings) basis. During the audit period, RPS' total reimbursement to the TPA was \$272,760 of which \$197,405 were contingency based fees such as:

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***In FY 2013, TPA costs totaled \$272,760***

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- OSHA reporting
- User Access annual
- Per claim / incident
- Indemnity per claim indexing
- Managed care services per hour
- Clinical consultation per call charge
- Telephonic case management per hour
- Usual, Customary and Reasonable 25% of savings
- Preferred provider organization (PPO) networks 25% of saving
- Complex file review per hour charge
- Peer review services charge per review
- Field case management services per assessment / per hour rates
- Allocated expenses incurred by the TPA

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Over the past three years, the TPA processed and paid workers' compensation claims as follows:

***Over the past three years, workers' compensation claims payments have increased***

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<i>Description</i>	<i>FY 2011</i>	<i>FY 2012</i>	<i>FY 2013</i>
<i>Indemnity</i>	\$243,953	\$264,221	\$259,773
<i>Medical</i>	\$605,257	\$829,894	\$936,225
<i>Total</i>	\$849,210	\$1,094,115	\$1,195,998

*Source: Sedgwick Report Statistics 2013*

As of June 30, 2013, RPS had 113 open workers' compensation cases, and \$2.6 million has been paid over the life of these open cases.

Under General Accepted Accounting Principles, RPS is required to reserve the funds/dollars necessary to pay future financial and legal obligations pertaining to workers' compensation claims. These future obligations are considered a legal liability and are reflected on RPS' financial statements. RPS engages the TPA to calculate and maintain the reserve amount to be provided. As of June 30, 2013 the reserve was \$3,435,444.

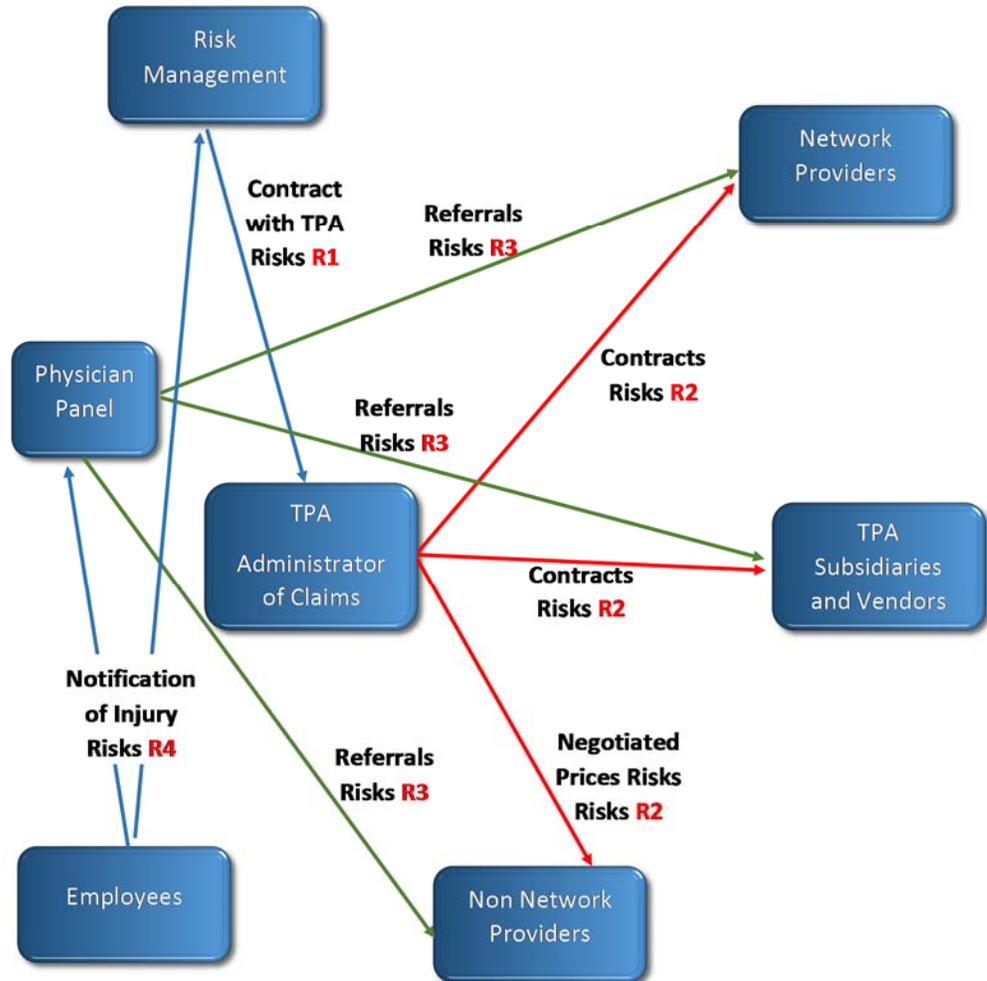
Prior to this audit, RPS had not performed an external review of the TPA's activities. During the course of this audit, RPS engaged a consultant to evaluate the TPA's conformity with best practices. The consultant's scope was limited to the evaluation of the TPA's conformity with best practices.

### Observations and Recommendations

The diagram below depicts the risks related to internal control weaknesses:

#### Medical Claims Process

*The workers' compensation claims process is associated with several risks*



**Materialized Risks**

- R1 - Terms of contract favors TPA  
Poor Contract Administration  
No oversight over services provided or costs incurred
- R2 - Terms of contract not disclosed to RPS leading to risk of undue profits at RPS' expense
- R3 - Conflict of interest resulting in excessive costs to RPS
- R4 - Non employment related injuries reported  
Abuse of the program

*Improvements needed in internal controls*

According to the Government Auditing Standards, internal control, in the broadest sense, encompasses the agency's plan, policies, procedures, methods, and processes adopted by management to meet its mission, goals, and objectives. Internal control includes the processes for planning, organizing, directing, and controlling program operations. It also includes systems for measuring, reporting, and monitoring program performance. An effective control structure is one that provides reasonable assurance regarding:

- Efficiency and effectiveness of operations
- Accurate financial reporting
- Compliance with laws and regulations

Based on the audit procedures followed, the auditors concluded that the controls over the workers' compensation benefits function need improvement. Several factors contributed to this conclusion, such as:

- Risk Management's over reliance on the TPA and external consultants to administer, provide analytics and oversight of workers compensation claims may not allow proper contract administration.
- Contractual agreements with external workers' compensation vendors do not adequately protect RPS' interests.
- The authority, responsibility and oversight for workers' compensation wage disbursements are not properly aligned.
- Lack of safety inspections lead to risk or actual occurrence of safety hazards not being found and remediated.
- Failure to identify, question, and dispute incorrect / inappropriate provider healthcare charges can lead to unnecessary healthcare expenses.
- Lack of independence of physicians serving on the workers' compensation panel could lead to conflicts of interest and could result in unnecessary inflated healthcare costs.

- The TPA's lack of transparency and communication with their customers pertaining to the terms and conditions of their contractual agreements with hospital / participating providers can result in unnecessary inflated healthcare costs.

**Workers' compensation program management practices need improvements. (Risks R1 and R2 in the diagram)**

Risk Management has the responsibility to ensure compliance with the VWC's regulations while keeping costs to a minimum. The auditors found Risk Management to be in compliance with those regulations but did not find costs being kept to a minimum.

**Medical Claims:**

The TPA contract does not include specific deliverables and performance measures. Such items are essential for the effective management of the contract. The auditor's review of this contract found:

- The TPA is not responsible for reviewing, detecting, and resolving healthcare provider's billing mistakes prior to issuing payments to such providers. Billing mistakes include, but are not limited to, unbundling, billing for equipment/routine supplies, up-coding, charges which are in violation of compliance regulations, incorrect use of diagnosis, current procedural terminology (CPT) codes and modifiers, etc.

**Risk:** Questionable, excessive, inappropriate and non-allowable hospital charges will not be detected and corrected resulting in excessive expense to RPS. The audit identified that this risk has already materialized as depicted in the following examples:

- A hospital bill for outpatient surgery included charges of \$18,921 or \$3,180 per hour for post recovery room hold time of approximately six hours. A standard hospital room would have cost approximately \$837 for 24 hours (based on a review of the TPA's claims data). Neither the TPA nor the Risk Manager detected and disputed this charge.

*Contract  
Administration*

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*RPS' TPA contract  
does not include  
specific deliverables  
or performance  
measures*

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*Several examples indicated that Risk Management should have provided better oversight to control medical costs*

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- The TPA issued a reimbursement to a hospital for 80% of the hospital's billed charges even though a contracted independent third party reviewer questioned / disputed \$17,043 as inappropriate billing errors (i.e. unbundling). The Risk Manager never detected, questioned or approved the subsequent \$17,043 payment made by the TPA to the hospital.
- The TPA did not secure itemized hospital bills for \$8,297 and \$21,597 for emergency services and outpatient rotator surgery, respectively. Instead, the TPA adjudicated and paid these claims from summary billing statements. The Risk Manager never detected or questioned this practice.
- The records did not indicate that the TPA had adequate documentation to support the necessity of using an operating room for a cut on the head needing six stitches and related three Computerized Tomography (CT) scans. Charges for these services totaled \$12,364. Neither Risk Management nor the TPA questioned the medical necessity of these services.
- Annually, RPS purchases a stop loss policy, which limits RPS' loss on any claim to \$650,000. Contractually, the TPA is required to file claims that exceed the stop loss limit. However, RPS' contract is vague on this requirement and fails to establish filing and follow up deadlines for claims which exceed the stop loss limits. The audit disclosed neither Risk Management nor the TPA timely and accurately monitor and resolve claims that exceeded the stop loss limits.

**Risk:** Failure to seek timely reimbursement of excess workers' compensation claims reflects poorly on management and results in unnecessary expense, loss of time-value of money, drains cash flow, and distorts financial records. In addition, reserves for worker's compensation liability could be misstated. The audit disclosed untimely filing and receipt of reimbursements for stop loss:

- In one of the cases, the most recent excess recovery request pertaining to this file was almost two years ago. Presently, RPS is due \$104,470 from the excess carrier for claims exceeding the stop loss limit. Both the TPA and Risk Management could have tracked and requested payments in

a timelier manner. Both the TPA and Risk Management have used an incorrect stop loss limit for older claims.

- The most recent (March 2014) excess recovery request for a 1998 claim included expenses which were incurred early in 2013. This means that the TPA waited almost a year before recovering these expenses from the excess carrier.

***Meaningful access to claims information***

***Access to claims information***

Auditors did not find evidence the Risk Manager used his TPA system access to monitor and oversee the efficient use of managed care resources, questionable and excessive provider charges, timely receipt of stop loss reimbursements, and claim reserves. The provided documentation substantiated that the Risk Manager participated in quarterly claims meetings with the TPA. However, there was no documentation to substantiate claim reserves, stop loss reimbursements, questionable and excessive provider charges etc. were discussed and resolved.

**RISK:** Inadequate analysis of the claims data impedes effective and efficient oversight and management of workers' compensation claims. This may result in miscommunication and unnecessary expenses for RPS.

***Indemnity Claims:***

As discussed previously, VWCA requires payment of two-thirds of the injured employee's wages as compensation for lost wages. These payments are referred to as indemnity payments. RPS engages the TPA to make these payments.

When employees suffer injuries that are compensatory under VWCA, payroll should cease and workers' compensation indemnity payments should begin. However, instances were found where injured employees received both payroll and workers' compensation indemnity payments. These duplicate payments were attributable to preventive controls not being in place to prohibit duplicate payments.

RPS has a decentralized payroll process. Various schools and other departments handle the input of payroll data. The duplicate payments were caused by the schools' failure to timely and accurately input injured employee's time as workers' compensation leave. Instead, such time was

often incorrectly inputted as sick leave. For this process to work correctly there must be a good coordination between Risk Management, the TPA, RPS' Payroll Function, remote locations and preventive controls in place which prohibit duplicate payments.

Risk Management does not have internal controls in place to ensure the accuracy of indemnity payments and to detect and prohibit duplicate payments being issued through both the payroll and workers' compensation system. The contractual agreement with the TPA does not require Risk Management's approval of indemnity claim payments. Instead, responsibility, oversight and control are fragmented between the TPA and RPS' Payroll Function. This has and continues to result in miscommunications, mistakes, overpayments and weak internal controls.

**Risks:** The employees can get paid incorrectly, which can result in financial losses. RPS adjusts such mistakes on future pay for injured workers' without recording an accounts receivable and requiring a refund for the overpayment(s). The audit found that this risk has and continues to occur as depicted below:

- Inaccuracies / disparities in average weekly pay (AWP) furnished by RPS' Payroll and average weekly pay disbursed by the TPA.
  - AWP furnished by payroll totaled \$105 as compared to \$240 calculated and paid by the TPA.
  - AWP furnished by payroll totaled \$266 as compared to \$291 calculated and paid by the TPA.
  
- Instances of injured workers receiving compensation for both sick pay and workers' compensation pay. These instances were attributable to RPS' failure to have controls in place requiring centralized authority over workers' compensation pay and timely reconciliations and remediation of exceptions.
  - Due to miscommunication / controls, Payroll issued sick leave pay to an employee and the TPA issued workers' compensation pay to the employee, resulting in overpayment of approximately \$2,700.
  - Injured employee received both workers compensation wage payments as well as vacation pay resulting in overpayment of approximately \$4,700.

Based on the above observations, the auditors have the following conclusions:

- Inaccurate payments to injured workers' continue to result in overstated expenses and understated accounts receivable without implementing an acceptable solution.
- Payroll is permitted to adjust injured employees' future W2 pay when necessary to correct overpayments or incorrect payments.

***RPS' Policy of supplementing workers' compensation indemnity payments needs to be revisited***

RPS' current policy allows injured employees to take sick leave to supplement workers' compensation indemnity payments (two-thirds of wages). This policy is generous and may result in the injured employee receiving more money than their take home pay as the indemnity payments are not taxable.

**RISK:** Allowing injured employees to supplement tax exempt workers' compensation indemnity benefits with accumulated sick leave with no dollar limitations could result in compensating the employee for more net pay than if they had worked. This situation would provide an incentive to prolong the date of return to work.

***Conflicts of Interest***

***The members of the Preferred Provider Panel of physicians have conflicts of interest (Risk R3 in the diagram)***

RPS administration appoints a preferred provider panel of physicians as required by section 65.2-603 of the Code of Virginia. The panel members are charged with a responsibility to treat all non-emergency workers' compensation illnesses and injuries and make appropriate referrals when specialized care is needed.

In order to maintain objectivity and independence it is essential that the physician panel members have no affiliation, ownership interest or be employed by any healthcare provider, conglomerate, or holding company. All three physician panel members are employees of Richmond area for profit hospital chains/ physician practices. These physicians are not in private practice. Frequently, these physicians make referrals for injured workers to their respective employers. This is a direct conflict of interest because it creates a risk that the physicians' professional judgment

regarding patient referrals, will be unduly influenced by the physicians' employment and compensation arrangements with for-profit hospital chains.

**RISK:** RPS could incur excessive and/or unnecessary costs, if the physicians on the panel do not refer claimants to the most cost effective alternatives. The auditor identified that this risk has already materialized as depicted in the following examples:

- In one of the cases, physical therapy services were delivered at a for-profit hospital at a cost of \$282. Identical services were available at an independent physical therapy center for \$100.
- Magnetic Resonance Image (MRI) of the spinal canal lumbar was charged at \$4,522 in a for-profit hospital outpatient setting as compared to \$600 for identical services delivered in an independent/non-affiliated imaging center.
- Typically, a treating physician writes a prescription for medication, which is filled by an independent registered pharmacy. The Auditor observed an example when a physician dispensed medication to the workers' compensation claimant and charged \$175 for 30 tablets. The same prescription medication was available at any Wal-Mart pharmacy at a cash price of \$4.
- The Auditor noticed instances of the TPA providing clerical or administrative functions (sending/receiving emails, issuing status reports, preparation of notes, scheduling healthcare provider appointments, placing telephone calls, etc.) through its subsidiaries or sub-contractors. The TPA billed for these managed care services within a range of \$85 to \$90 per hour. The auditor did not find any evidence to support if the Risk Manager questioned or disputed the necessity and the form of delivery of these services.

***Inadequate fiscal controls and ineffective cash management could result in potential financial losses***

- ***Inadequacy of reserves for workers' compensation liability***

It is customary to set aside a reserve for future workers' compensation claims liability. Generally Accepted Accounting Principles require an appropriate amount be reserved. Typically, the amount set aside is determined actuarially. However, RPS' contract

with the TPA requires the TPA to estimate the expected total cost of each workers' compensation claims. The auditor found that many times this estimate was based on the TPA's knowledge of expected short-term losses. An actuarial calculation would estimate total costs of the claims statistically with a long-term perspective.

**Risk:** The amount of reserves may not be adequate to cover the actual liability. The external consultant conducting an audit of claims files at RPS's request found several instances where the reserve amounts were inadequate.

- ***Opportunity for improving cash management practices***

At the beginning of each fiscal year, RPS's Finance Department transfers funds of approximately \$1 million (100% of annual budget for the line item) to its workers' compensation bank account to which the TPA's employees have access. The TPA is permitted to pay itself directly from RPS's bank account. Risk Management is not required to review and approve these disbursements. RPS' workers' compensation bank account is not being reconciled. Bank statements for this account are being mailed to the TPA. This means that RPS does not monitor activities of this bank account.

**RISKS:**

- This practice may represent inadequate cash flow management.
- It exposes a large amount of cash to the TPA's employees. Having access to a large amount of cash where the funding organization has little or no controls could provide enticement for abuse.
- There is no assurance that reconciling items are identified, researched, and resolved in a timely manner and that the bank account balance is correct.
- Such practices represent material internal control weakness. Controls are not present to monitor and detect inappropriate utilization of services and erroneous disbursements to the TPA. Proper segregation of duties does not exist. Consequently, there is a potential risk for misappropriation of funds.

*Safety inspections and correction of deficiencies identified need to be timely and effective to prevent injuries*

*Safety*

It is well known that RPS' facilities are in disrepairs. The auditor determined that Risk Management did not perform any safety inspections or re-inspections during the period July 1, 2012 through June 30, 2013.

**RISK:** Failure to perform routine inspections could compromise the safety of pupils, parents, teachers, employees and other visitors. Injuries occurring on RPS properties could expose RPS to legal liabilities.

***Recommendations***

The Superintendent needs to:

- 1) Amend the contractual agreement with the TPA to require the TPA to:
  - a) Issue itemized billing statements for all goods and services furnished by the TPA and/or its affiliates to allow proper evaluation of charges.
  - b) Cease issuing payments to itself for goods and services delivered by the TPA and/or its affiliates. Instead, require Risk Management to approve the charges for appropriateness and disburse it to the TPA.
  - c) Pre-certify/approve the delivery of all healthcare provider goods and services such as MRI, CT scans, etc.
  - d) Perform line item audits for all billing statements which equal or exceed \$500.
  - e) Submit written itemized requests/costs for all managed care services to the Risk Manager for documented approval prior to the delivery of these services.
  - f) Encourage the use of non-hospital network providers and mail order pharmacy services.
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  - h) Update the estimate of the expected total cost of qualified claims on or before the close of each calendar month.
  - i) Furnish the Risk Manager monthly, detailed "return to work" status report.
  - j) Require monthly filings for reimbursement of excess workers' compensation claims against "Stop Loss" coverage and provide a monthly report to the Risk Manager for approval.

- 2) The School Board needs to amend the Sick Leave Policy that permits sick leave to supplement workers' compensation payments to cap total payments to pre-injury net compensation.
- 3) Redefine and establish specific responsibilities for the Risk Manager and the Risk Management Department for the TPA contract administration, reporting requirements, deliverables, and performance measurements.
- 4) Assign the authority and responsibility for all safety inspections, re-inspections, remediation, correction of deficiencies etc. to Risk Management as follows:
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  - c) require quarterly safety reports to the Superintendent.
- 5) Develop and implement written policies and procedures for:
  - a) Administering and reporting workers' compensation stop loss claims.
  - b) Conducting, preparing and monitoring of the following elements of safety inspections:
    - o Due date of inspections
    - o Number and frequency of inspections
    - o Safety report's content and approval
    - o Identification/remediation/re-inspections of deficiencies
- 6) Require the Risk Manager's approval of the commencement, modifications and terminations of indemnity benefits.
- 7) Assign Risk Management the responsibility for monitoring and requesting replenishment of funds to the workers' compensation bank account.
- 8) Require the Finance Department to prepare monthly reconciliations of the self-insured bank account.
- 9) Engage an actuarial to validate and / or determine the valuation of the reserve for future workers' compensation claims liability as of the close of business of each fiscal year.
- 10) Prepare a monthly reconciliation of indemnity payments to payroll records.

**MANAGEMENT RESPONSE FORM**

**APPENDIX A**

**RPS Workers' Compensation 2015-03**

<b>The Superintendent needs to:</b>			
<b>#</b>	<b>RECOMMENDATION</b>	<b>CONCUR Y-N</b>	<b>ACTION STEPS</b>
1	Amend the contractual agreement with the TPA to require the TPA to:		
1	a) Issue itemized billing statements for all goods and services furnished by the TPA and/or its affiliates to allow proper evaluation of charges.	N	RPS contracts the TPA to conduct the proper evaluation of charges for goods and services. The proper evaluation is dependent on having the expertise to assess medical need for goods and services rendered. RPS does not have the medical expertise on staff to make these assessments. RPS conducts periodic audits of the TPA by a third party audit firm when funds are available.
1	b) Cease issuing payments to itself for goods and services delivered by the TPA and/or its affiliates. Instead, require Risk Management to approve the charges for appropriateness and disburse it to the TPA.	N	RPS contracted an independent auditing firm in January 2014 with expertise in workers' compensation to review the existing handling of RPS claims by the TPA against workers' compensation best practices. In doing so the firm's auditor identified the issuance of payments to a third party by itself is a common practice for workers' compensation TPA's. This practice facilitates the timely handling and administration of claims. Introducing a requirement for Risk Management to approve the charges for appropriateness and disbursement would delay the timely payment for goods and services.
1	c) Pre-certify/approve the delivery of all healthcare provider goods and services such as MRI, CT scans, etc.	N	All healthcare provider goods and services such as MRI, CT scans, etc. cannot be pre-certified/approved because of Virginia Workers' Compensation regulations and /or the nature of the medical treatment needed, e.g. in the case of an employee having to go to an emergency room for care, the attending physician—not RPS -- needs to make the medical decisions relating to goods and services to administer appropriate care to the employee. For follow-up care, the TPA is already pre-certifying/approving most non-emergency care to determine if it is causally related to the injury. However, in the state of Virginia, due to workers' compensation regulations, the employer cannot dictate care, which precludes pre-certification.
1	d) Perform line item audits for all billing statements which equal or exceed \$500.	Y	The TPA has the capability to perform line item audits on billing statements for a supplemental charge. RPS will work with the TPA to determine the charges for these line item audits, determine a reasonable financial threshold to set for billing statements where the TPA will perform the audits, and implement as appropriate.
1	e) Submit written itemized requests/costs for all managed care services to the Risk Manager for documented approval prior to the delivery of these services.	Y	The TPA currently provides a written request for managed care services through the Risk Manager for approval. This process will be enhanced by adding a <i>specific timeframe</i> for the managed care services. This enhancement will further control costs.
1	f) Steer/encourage the use of non-hospital network providers and mail order pharmacy services.	Y	The nature of workers' compensation care-- because it is provided by specialized occupational health care providers-- makes it increasingly difficult to find medical providers who are not associated with hospitals and hospital networks. Currently, mail order pharmacy services are encouraged where appropriate and this practice will continue.

1	g) Detect, dispute and satisfactorily resolve health care providers' billing errors.	Y	The TPA is already detecting, disputing and satisfactorily resolving health care providers' billing errors.
1	h) Update the estimate of the expected total cost of qualified claims on or before the close of each calendar month.	Y	Risk Management will coordinate with the TPA on the delivery and timing of these cost estimate reports to RPS.
1	i) Furnish the Risk Manager monthly, detailed "return to work" status report.	Y	Risk Management will coordinate with the TPA on the delivery and timing of these "return to work" status reports to RPS.
1	j) Require monthly filings for reimbursement of excess workers' compensation claims against "Stop Loss" coverage and provide a monthly report to the Risk Manager for approval.	Y	Risk management agrees there is a need to amend the TPA contract and set a time frame for stop loss filings with the excess workers' compensation carrier by the TPA. However, the time frame would be semi-annually to align with excess carriers reviews. Future quarterly claims review meetings (already a standing meeting with the TPA, Risk Management and the School Board Attorney), will require the TPA to provide a specific report on what reimbursements have been submitted and received by the TPA for all claims exceeding stop loss retention to the Risk Manager for review.
	<b>TITLE OF RESPONSIBLE PERSON</b>		<b>TARGET DATE</b>
	Risk Manager		06/30/2015
	<b>IF IN PROGRESS, EXPLAIN ANY DELAYS</b>		<b>IF IMPLEMENTED, DETAILS OF IMPLEMENTATION</b>
	Position Vacancy		
<b>#</b>	<b>RECOMMENDATION</b>	<b>CONCUR Y-N</b>	<b>ACTION STEPS</b>
2	The School Board needs to amend the Sick Leave Policy that permits sick leave to supplement workers' compensation payments to cap total payments to pre-injury net compensation.	Y	RPS agrees to research what other school systems/municipalities are doing in relation to sick leave policies and workers' compensation and provide the information to the School Board for review.
	<b>TITLE OF RESPONSIBLE PERSON</b>		<b>TARGET DATE</b>
	Risk Manager		06/30/2015
	<b>IF IN PROGRESS, EXPLAIN ANY DELAYS</b>		<b>IF IMPLEMENTED, DETAILS OF IMPLEMENTATION</b>
<b>#</b>	<b>RECOMMENDATION</b>	<b>CONCUR Y-N</b>	<b>ACTION STEPS</b>
3	Redefine and establish specific responsibilities for the Risk Manager and the Risk Management Department for the TPA contract administration, reporting requirements, deliverables, and performance measurements.	Y	RPS agrees to redefine and establish specific responsibilities for the Risk Manager and the Risk Management Department for the TPA contract administration, reporting requirements, deliverables, and performance measurements.
	<b>TITLE OF RESPONSIBLE PERSON</b>		<b>TARGET DATE</b>
	Risk Manager		06/30/2015
	<b>IF IN PROGRESS, EXPLAIN ANY DELAYS</b>		<b>IF IMPLEMENTED, DETAILS OF IMPLEMENTATION</b>
<b>#</b>	<b>RECOMMENDATION</b>	<b>CONCUR Y-N</b>	<b>ACTION STEPS</b>
4	Assign the authority and responsibility for all safety inspections, re-inspections, remediation, correction of deficiencies etc. to Risk Management as follows: a) require a semiannual uniform physical safety inspection of all schools, facilities, real estate owned or leased, equipment, etc. and report all findings and proposed corrective actions/costs. b) maintain an automated composite inventory of all safety inspections, safety findings/deficiencies, estimated costs to correct, estimated completion date, date of remediation of deficiency, current status, re-inspection/approval. c) require quarterly safety reports to the Superintendent.	Y	Dependent on availability of funds to add a full-time employee or contractor to perform the recommended activities, RPS agrees to a, b, and c as outlined. Safety inspections are being performed by a temporary employee.

	TITLE OF RESPONSIBLE PERSON		TARGET DATE
	Risk Manager		04/01/2015
	IF IN PROGRESS, EXPLAIN ANY DELAYS		IF IMPLEMENTED, DETAILS OF IMPLEMENTATION
	Position Vacancy		
#	RECOMMENDATION	CONCUR Y-N	ACTION STEPS
5	Develop and implement written policies and procedures for: a) Administering and reporting workers' compensation stop loss claims. b) Conducting, preparing and monitoring of the following elements of safety inspections: - Due date of inspections - Number and frequency of inspections - Safety report's contents and its approvals - Identification/remediation/re-inspections of deficiencies	Y	In relation to "a", RPS agrees to develop and implement written policies and procedures for administering and reporting workers' compensation stop loss claims. Dependent on availability of funds to add a full-time employee or contractor to perform the recommended activities, RPS agrees to "b", as outlined.
	TITLE OF RESPONSIBLE PERSON		TARGET DATE
	Risk Manager		06/30/2015
	IF IN PROGRESS, EXPLAIN ANY DELAYS		IF IMPLEMENTED, DETAILS OF IMPLEMENTATION
#	RECOMMENDATION	CONCUR Y-N	ACTION STEPS
6	Require the Risk Manager's approval of the commencement, modifications and terminations of indemnity benefits.	Y	RPS agrees to enhance the existing process. The existing process is the TPA provides a written notification to Risk Management that indemnity benefits will be paid for a specific time frame. The enhancement would be that the TPA has to receive approval from the Risk Manager prior to the commencement, modifications and terminations of indemnity benefits.
	TITLE OF RESPONSIBLE PERSON		TARGET DATE
	Risk Manager		4/1/2015
	IF IN PROGRESS, EXPLAIN ANY DELAYS		IF IMPLEMENTED, DETAILS OF IMPLEMENTATION
#	RECOMMENDATION	CONCUR Y-N	ACTION STEPS
7	Assign Risk Management the responsibility for monitoring and requesting replenishment of funds to the workers' compensation bank account.	Y	Risk Management already has the responsibility for monitoring and requesting replenishment of funds to the workers' compensation bank account.
	TITLE OF RESPONSIBLE PERSON		TARGET DATE
	Risk Manager		07/01/2015
	IF IN PROGRESS, EXPLAIN ANY DELAYS		IF IMPLEMENTED, DETAILS OF IMPLEMENTATION
			This is, and has been the practice.
#	RECOMMENDATION	CONCUR Y-N	ACTION STEPS
8	Require the Finance Department to prepare monthly reconciliations of the self-insured bank account.	Y	The Finance Department will prepare monthly reconciliations of the self-insured bank account.
	TITLE OF RESPONSIBLE PERSON		TARGET DATE
	Finance Director		06/30/2015
	IF IN PROGRESS, EXPLAIN ANY DELAYS		IF IMPLEMENTED, DETAILS OF IMPLEMENTATION
#	RECOMMENDATION	CONCUR Y-N	ACTION STEPS
9	Engage an actuarial to validate and / or determine the valuation of the reserve for future workers' compensation claims liability as of the close of business of each fiscal year.	Y	RPS agrees to engage an actuary to determine the valuation of the reserve for future workers' compensation claims liability as of the close of business for each biennium as defined by the state Department of Education.
	TITLE OF RESPONSIBLE PERSON		TARGET DATE
	Risk Manager		04/01/2015
	IF IN PROGRESS, EXPLAIN ANY DELAYS		IF IMPLEMENTED, DETAILS OF IMPLEMENTATION

#	RECOMMENDATION	CONCUR Y-N	ACTION STEPS
10	Prepare a monthly reconciliation of indemnity payments to payroll records.	Y	RPS agrees that Risk Management and Finance will coordinate to prepare a monthly reconciliation of indemnity payments to payroll records.
	<b>TITLE OF RESPONSIBLE PERSON</b>		<b>TARGET DATE</b>
	Risk Manager / Finance Director		03/31/2015
	<b>IF IN PROGRESS, EXPLAIN ANY DELAYS</b>		<b>IF IMPLEMENTED, DETAILS OF IMPLEMENTATION</b>