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Metro

JANUARY 12, 2005

TO: BOARD OF DIRECTORS

THROUGH: ROGER SNOBLE
CHIEF EXECUTIVE OFFICER

FROM: GREGORY KILDARE
EXECUTIVE OFFICER OF RISK MANAGEMENT

SUBJECT: HAZELRIGG RISK MANAGEMENT SERVICES – INSPECTOR GENERAL'S AUDIT

ISSUE

To provide background on the Inspector General's January report to the Executive Management Committee regarding Hazelrigg Risk Management Services (Hazelrigg).

BACKGROUND

Prior to Metro taking over self-administration in 2001, its workers' compensation claims and costs were among the worst in the California transit industry. During fiscal year 2000, Metro had 3,264 reported workers' compensation claims. Through November of fiscal year 2005, only 663 claims were reported with a projection until year-end of 1,591, a reduction of more than 50% since fiscal year 2000. Further, Metro's monthly lost workdays paid in August of 2001 were more than 11,000, but by November 2004 had declined to 4,875.

During 2002 and 2003, the Los Angeles County Civil Grand Jury conducted formal investigations into four government entities including the Los Angeles County Fire and Sheriff's departments, the City of Los Angeles Fire Department and Metro regarding their workers' compensation programs. In their final report, the Grand Jury lauded Metro's self-administrative program and provided an overview of Metro's program as a model for other government agencies. Recently, in a televised program, California Connected, Tom Higgins, then Chief of the Los Angeles County District Attorney's Workers' Compensation Fraud Division praised Metro's fraud prevention program for having more arrests and prosecutions over the last two years than any other comparable agency in California. Metro's success in its self-administration program was partially due to Hazelrigg Risk Management Services providing Metro with some of the more experienced claims personnel at the initial phase of Metro's self-administration program beginning September 2001.

The initial RFP for workers' compensation claims administration staffing received three proposers. Two of the three proposers declined to provide any services under the Metro's proposed rate structure because they determined the proposed rates would not provide reasonable compensation. Hazelrigg was the only vendor who agreed to be compensated according to Metro's proposed rates. Within sixty (60) days from inception, Hazelrigg informed Metro they could no longer provide services under the contracted rate structure because of substantial operating losses. Hazelrigg realized they had failed to calculate the benefits costs, overtime costs and overhead when they agreed to Metro's proposed rates. After several meetings, Hazelrigg indicated they would default on this contract. Without claims personnel provided by Hazelrigg, Metro's self-administered program could not operate. A failed workers' compensation administration program would have resulted in substantial delays in payments to injured workers and their medical providers, subjecting Metro to state imposed fines, penalties or other sanctions. The State Compensation Insurance Fund may well have taken over management of the program. Additionally, costly litigation with Hazelrigg would certainly have occurred.

In order to avoid default, Hazelrigg and Metro agreed to a new rate structure including the introduction of overtime premiums. This new agreement did not require a return to the Board, since the overall amount of the contract did not change and the Board did not approve a rate structure. Although the new rate structure agreement and other changes were not formally incorporated, both parties operated under such revisions.

Upon my return to Risk Management as Executive Officer in March 2004, well before the notice of an Inspector General Audit, I became aware that the contract was not formally modified. I alerted Hazelrigg and Procurement to the need to immediately modify the contract to reflect the revised rate structure. In June 2004, through further negotiations, Hazelrigg, Procurement and Risk Management successfully executed another rate structure below the current practice, with estimated savings of more than $100,000 annually. This information was communicated to the Inspector General verbally as well as in writing (Attached)

The Inspector General's audit and report to the Executive Management Committee implies that Metro overpaid Hazelrigg by as much as $800,000. Metro did not overpay Hazelrigg because the original terms of the contract were not in force following implementation of the new rate structure and the overall amount of the contract will not be exceeded. However, the agreement under which both parties operated should have been signed and incorporated formally into the contract. Following the Inspector General's recommendations, both Procurement and Risk Management have instituted additional safeguards to ensure that modifications are processed timely, time sheets are reviewed more thoroughly, and no payments are made under a contract revision until a formal modification is executed.

<u>NEXT STEPS</u>

None required.

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Interoffice Memo

Date:	September 24, 2004
To:	Dawn Williams-Woodson
From:	Greg Kildare
Subject:	Hazelrigg Audit Report

Thank you for providing an opportunity to respond to the draft audit of the Hazelrigg Risk Management Services (HRMS) contract and to provide a context for the findings.

The initial RFP for seconded employees received three proposers. The proposer's rate structures were different, so the MTA imposed a rate for all three proposers. At that time, two of the three proposers declined to provide any services under the MTA's proposed rate structure because they believed the compensation rate was substandard. Only HRMS agreed to be compensated according to the MTA's proposed rates.

HRMS employees began working under the new rate structure in September 2001. Within 60 days, HRMS informed the MTA they could no longer continue under that rate structure because of operating losses for the first two months. Apparently, HRMS neglected to include some benefits costs and overtime costs when they agreed to the MTA proposed rates. As a consequence, HRMS threatened to default on this contract. Default would have resulted in the MTA no longer able to administer workers' compensation claims causing substantial delays in payments to injured workers and their medical providers. These delays would have subjected the MTA to state imposed fines and penalties. With a default, costly litigation with HRMS would certainly have followed.

Therefore, a verbal agreement and subsequent practice allowed HRMS to continue working in which overtime premiums would be paid by the MTA and certain job classifications would be billed at new rates. Unfortunately, this verbal agreement was not formally amended into the contract.

As the new Executive Officer and as soon as I became aware of this deficiency in March/April of 2004, I alerted HRMS and Procurement to the need to immediately amend to contract to reflect a new rate structure. In June 2004, HRMS, Procurement and Risk Management successfully amended the contract with a rate structure below the current practice, saving the MTA more than $100,000 per year. Concurrently, I implemented safeguards to ensure that MTA management review all of the Hazelrigg invoices for consistency with the contract terms and conditions and to make sure that all of the HRMS employees' timesheets are signed by an MTA supervisor. I have also eliminated all HRMS overtime charges.

Also in the 4th Quarter of fiscal 2004, I asked Procurement and Ethics to conduct seminars for all Risk Management staff regarding basic MTA policies and procedures to ensure that all payments made to vendors are made under contract, and that all invoices are reviewed according to the terms and conditions of these agreements. Procurement will be responding independently of this memo.

If I can be of any further assistance, please let me know.

c: Lonnie Mitchell
Bruce Feerer
Richard D. Brumbaugh