

ARIZONA DEPARTMENT OF ADMINISTRATION - RISK MANAGEMENT

A.R.S. § 41-622

Risk Management Fund	FY 1998 Actual	FY 1999 Estimate	FY 2000 Approved	FY 2001 Approved
FTE Positions	185.0	83.0	85.0 ^{1/}	85.0 ^{1/}
Personal Services	2,457,200	2,685,100	2,849,600	2,906,600
Employee Related Expenditures	544,900	598,900	621,900	649,200
Professional and Outside Services	128,500	212,400	212,400	212,400
Travel - In State	41,900	34,800	36,800	36,800
Travel - Out of State	5,200	10,400	13,400	13,400
Other Operating Expenditures	750,900	718,600	833,700	833,700
Equipment	92,300	53,600	57,800	53,600
Operating Subtotal	4,020,900	4,313,800	4,625,600	4,705,700
WC Losses & Related Expenditures	14,782,900	18,716,000	20,947,000	22,071,000
WC Attorney General Defense	208,300	256,800	0	0
WC Insurance Premiums	211,200	293,000	0	0
WC Loss Control Grants	150,000	150,000	0	0
Premium Tax	400,100	444,200	444,200	444,200
University Health Work Program	58,200	159,500	159,500	159,500
Risk Management Information System	0	233,200	0	0
RM Losses & Related Expenditures	25,195,600	36,953,900	33,944,000	34,347,000
Attorney General Defense	5,706,400	6,109,200	6,485,000	6,622,500
Insurance Premiums	4,266,500	5,821,900	6,205,400	6,205,400
Loss Control Grants	331,600	500,000	650,000	650,000
Year 2000 Loss Control Grants	0	9,500,000 ^{2/}	0	0
Total Appropriations	55,331,700	83,451,500	73,460,700 ^{3/}	75,205,300 ^{3/}
Fund Summary				
Risk Management Fund	38,648,700	62,396,300	73,460,700	75,205,300
Workers' Compensation Fund	16,683,000	21,055,200	0	0
Total Appropriations	55,331,700	83,451,500	73,460,700	75,205,300

Program Description – *The Risk Management section acts as the state’s insurance agent, which includes making property loss and liability payments, as well as developing and administering loss control programs. With the exception of certain limited areas of coverage, the state is self-insured, paying for its own losses and liabilities. Costs of claims are paid by the Risk Management Fund.*

Consolidate Funds and Line Items — Laws 1998, Chapter 242 consolidated the Workers’ Compensation (WC) Fund into the Risk Management (RM) Fund. As a result, the appropriation consolidates some Special Line Items previously funded from the 2 separate funds but used for essentially the same purpose. These include the

Attorney General Defense, Insurance Premiums, and Loss Control Grants Special Line Items. The Appropriations Report continues to separately list the Worker’s Compensation and Risk Management Losses and Related Expenditures line items due to legislative interest in this

^{1/} Excludes 104 FTE Positions funded from Special Line Items in FY 2000 and FY 2001, but appropriated as FTE Positions in the Attorney General’s budget rather than in this cost center.

^{2/} The \$9,500,000 appropriation for Year 2000 Loss Control Grants shall be used to reduce or eliminate state liability for service failures resulting from Year 2000 information technology problems. The \$9,500,000 shall be allocated by the Department of Administration to the Government Information Technology Agency for distribution to state agencies or departments to pay for Year 2000 information technology projects. Prior to expenditure of the \$9,500,000, the Government Information Technology Agency shall report to the Joint Legislative Budget Committee on its plan for expending the monies, including any expected annualization or continuing costs for FY 2000 and the anticipated reduction in state liability for service failures. Of this amount, \$5,500,000 is exempt from the provisions of A.R.S. § 35-190, relating to lapsing of appropriations, until the end of FY 2000. (General Appropriation Act footnote, as amended by Laws 1999, Chapter 6, 1st Special Session)

^{3/} General Appropriation Act funds are appropriated as an Operating Lump Sum by Fund, with a Special Line Item Lump Sum and an Attorney General Defense-Risk Management Special Line Item.

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area and differing actuarial assumptions for the 2 types of losses.

WC Losses and Related Expenditures — The approved amount from the RM Fund represents payments to WC beneficiaries for the state's liability resulting from workplace injuries, as well as related legal and loss adjustment expenditures for aspects of claims handled by the private sector rather than in-house. The FY2000 appropriation includes an increase of \$2,231,000 for self-insured Workers' Compensation losses and expenditures related to settling these losses. The FY 2001 appropriation includes a further increase of \$1,124,000. The approved amounts reflect the FY 2000 and FY 2001 actuarial estimates for the state, using a 70% confidence interval. Typically, we use the higher confidence level for Workers' Compensation losses due to their volatility. In this year's report, the actuary notes an increase in the cost of FY 1998 claims and states that future Workers' Compensation losses may be higher than predicted because 1) the state's costs are nearly 30% lower than standard in the insurance industry and 2) the state's historical data is unreliable before FY 1994, when ADOA began to self-insure for Workers' Compensation losses.

WC Attorney General Defense — This line item included funding from the WC Fund for the Risk Management Section's contract with the Attorney General's Insurance Defense Section. Since the WC Fund has been consolidated into the RM Fund, this line item is now included in the "Attorney General Defense" line item paid from the RM Fund.

WC Insurance Premiums — This line item included funding from the WC Fund to purchase private insurance policies where the state deemed it more efficient to cede risk to an outside insurer. Since the WC Fund has been consolidated into the RM Fund, this line item is now included in the "Insurance Premiums" line item paid from the RM Fund.

WC Loss Control Grants — This line item included funding from the WC Fund for loss control grants to state agencies. Since the WC Fund has been consolidated into the RM Fund, this line item is now included in the "Loss Control Grants" line item paid from the RM Fund.

Premium Tax — The approved amount from the RM Fund represents the estimated tax payable by the state as a self-insured employer, as authorized by A.R.S. § 23-961. The monies are used by the Industrial Commission of Arizona to fund the regulation of Workers' Compensation insurance.

University Health Work Program — This program is funded from the RM Fund and uses student nurses from the 3 state universities to perform health services for minor

work-related injuries or illnesses in lieu of treatment by private physicians.

Risk Management Information System (RMIS) — This line item was intended to fund replacement of the division's data management system. The department had intended to use the RMIS funding to purchase new information system software and replace computer services previously provided by the Information Services Division. However, the department was unable to procure a satisfactory information system. Consequently, the FY 2000 appropriation eliminates the Special Line Item and adds \$248,300 and 2 FTE Positions to the Operating Lump Sum for the division to run its own LAN and Risk Management Information System. In FY 2001, this amount is decreased by \$(4,200) to eliminate one-time equipment.

RM Losses and Related Expenditures — The approved amount represents funding from the RM Fund for estimated liability and property claims, settlements, and other losses, as well as related legal and loss adjustment expenditures for aspects of the claims handled by the private sector rather than in-house. The projected loss amount is updated annually to reflect current loss exposures and is based on an annual actuarial estimate. The approved FY 2000 amount includes a decrease of \$(3,009,900) and provides a total of \$33,944,000. For FY 2001, this amount is increased by \$403,000 and provides a total of \$34,347,000 for Risk Management losses. These amounts reflect the 50% confidence level in the annual actuarial study conducted for the state. Based on insurance industry trends and the state's loss history, the actuary predicts higher amounts for automobile, building property, criminal justice, and medical malpractice losses, but slightly lower amounts for highway operations and employment practices losses.

Attorney General Defense — This line item represents funding from the RM Fund for the Risk Management section's contract with the Attorney General's Insurance Defense section for legal representation in Risk Management-related lawsuits against the state. The appropriation funds 104 FTE Positions which are appropriated in the Attorney General's budget. Funding for these positions remains in the ADOA budget, since the department must pay for Attorney General services.

Insurance Premiums — The approved FY 2000 amount from the RM Fund includes an increase of \$90,500 for the cost of private insurance policies purchased for specific property and liability losses where the state deems it more cost effective to cede risk to an outside insurer. This amount is continued in FY 2001.

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Loss Control Grants — These grants from the RM Fund are made by the department to state agencies to implement loss control projects or programs that can demonstrate tangible loss/cost avoidance.

Year 2000 Loss Control Grants — This Special Line Item appropriation from the RM Fund funds loss control grants to various state agencies, in order to reduce the state's liability for service failures resulting from Year 2000 information technology problems. The monies are distributed by the Government Information Technology Agency (GITA). The approved FY 2000 amount eliminates the Year 2000 Loss Control Grants Special Line Item since 1) most of the state's Year 2000 problems should be addressed by the end of FY 1999 and 2) the FY 1999 appropriation is exempt from lapsing until the end of FY 2000. The approved FY 1999 amount includes a supplemental appropriation of \$5,500,000 for Year 2000 Loss Control Grants. This amount will be subject to a footnote in the FY 1999 General Appropriation Act requiring that 1) the department transfer the monies to GITA for distribution to other state agencies, 2) the monies be used to reduce or eliminate the state's liability for service failures resulting from Year 2000, and 3) GITA

report to the Joint Legislative Budget Committee prior to expenditure of the supplemental appropriation. The supplemental appropriation is exempt from lapsing until the end of FY 2000.

Other Issues: Risk Management Revolving Fund — The fund consists of monies collected by ADOA from state agencies for payment of Risk Management charges, as authorized by A.R.S. § 41-622. *(For a list of these charges, refer to the General Provisions section at the front of the Appropriations Report).* ADOA recommends to the Legislature the dollar amount to be appropriated for each agency's Risk Management charge based on factors including prior losses, current exposures, an outside actuarial study conducted for the department, and the statewide funding level estimated to be required for the fiscal year. Monies in the fund are appropriated by the Legislature for costs of the ADOA Risk Management section, including payment of certain state losses and related expenditures.

Risk Management Fund			
	<u>FY 1999</u>	<u>FY 2000</u>	<u>FY 2001</u>
Cash Balance Beginning of Fiscal Year	\$ 52,803,300	\$40,573,900	\$22,916,600
Revenue:			
Risk Management Collections			
General Fund	\$ 30,672,000	\$21,006,500	\$21,006,500
Other Appropriated Funds	14,443,700	11,041,500	11,041,500
Non-Appropriated Funds	6,992,600	5,220,500	5,220,500
Workers' Compensation Collections			
General Fund	8,088,700	8,049,200	8,574,900
Other Appropriated Funds	1,525,600	1,587,400	1,683,800
Non-Appropriated Funds	7,620,600	7,638,300	8,131,400
Insurance Losses Recovered	1,902,500	1,250,000	1,300,000
Loss Control Refunds	<u>38,200</u>	<u>10,000</u>	<u>10,000</u>
Total Funds Available	\$124,087,200	\$96,377,300	\$79,885,200
Expenditures:			
ADOA Risk Management	73,951,500	73,460,700	75,205,300
Year 2000 Loss Control	<u>9,500,000</u>	<u>0</u>	<u>0</u>
Total Expenditures	<u>\$ 83,451,500</u>	<u>\$73,460,700</u>	<u>\$75,205,300</u>
Prior Year Adjustments	<u>61,800</u>	N/A	N/A
Cash Balance End of Fiscal Year ^{1/}	<u>\$ 40,573,900</u>	<u>\$22,916,600</u>	<u>\$ 4,679,900</u>

^{1/} Typically, up to \$5,000,000 each year is reserved for Risk Management losses above the budgeted level. This leaves an estimated unreserved cash balance of \$0 the end of FY 2001.

