
Study of the Workers' Compensation Claims Process for State Employees

A Report to the
Governor
and the
Legislature of
the State of
Hawaii

Report No. 96-5
January 1996

THE AUDITOR
STATE OF HAWAII

OVERVIEW

THE AUDITOR
STATE OF HAWAII

Study of the Workers' Compensation Claims Process for State Employees

Summary

This study was prepared in response to Senate Concurrent Resolution No. 203, Senate Draft 1 of the 1995 Regular Session which requested that the State Auditor conduct a study to improve efficiency, cost effectiveness, and accountability in processing claims filed against the State for workers' compensation benefits. This study was requested in response to legislative concern about expenditures and complaints about the processing of state employees' claims.

Like other employers, Hawaii state government is responsible for providing workers' compensation benefits to its employees who are injured on the job. Over the past five years, the State's expenditure for these benefits has increased from over \$13.5 million to more than \$25.6 million. In March 1995 the Legislature made an emergency appropriation of \$5.5 million to cover remaining claims for FY1994-95.

We found that State government has taken significant steps to better control the cost of workers' compensation claims by its employees. However our study found that these efforts have not yet produced an integrated workers' compensation *system*. No one department is fully accountable for overseeing, coordinating and reporting on claims for and costs of workers' compensation for all State employees. Responsibilities are fragmented among various agencies. State agencies are currently bogged down in processing claims. The State lacks standard guidelines and policies and procedures for claims management. "User friendly" information is needed.

Better management information is also needed. The lack of complete and accurate information on the State's claims and expenditures has hindered efforts to meet established accounting standards. As a result, the State could receive a qualified opinion in its *Comprehensive Annual Financial Report*.

Workplace safety and return-to-work programs achieve savings by reducing employee injuries and by returning injured employees back to work as soon as possible. We found that emphasis on safety and return-to-work programs varies among agencies. These programs should be an integral part of a workers' compensation system.

Hawaii's workers' compensation activities for state employees could benefit from strong leadership in providing effective oversight, coordinating agencies' responsibilities as employers, and compiling, analyzing and reporting needed



information. The advantages of centralization outweigh its disadvantages. We believe that the Department of Human Resources Development is the appropriate choice as system leader since it already centrally manages claims for many state agencies in the interests of cost control. The department will need additional resources to take over central responsibility.

Recommendations and Response

We recommend that the Legislature consider amending Chapter 26-5, HRS, the law establishing the Department of Human Resources Development, to assign responsibility for central oversight, coordination, and reporting for workers' compensation activities related to claims by state employees. The department would be held accountable and would have full authority and responsibility for: a) setting policies, goals and objectives for the system; b) managing workers' compensation claims on a centralized basis for all agencies in the executive, judicial and legislative branches; c) compiling and analyzing complete and accurate workers' compensation claim and expenditure information; d) integrating, coordinating and monitoring workplace safety and return to work programs; e) evaluating the costs and benefits of innovative cost control strategies; and f) developing a brochure which clearly and simply explains the entire claims process for all state employees.

The Department of Human Resources Development had numerous comments. The department is interested in centralizing the executive branch, but expressed concerns about handling all state cases due to the constitutional separation of the executive, legislative and judicial branches. The department is investigating new integrated personnel, workers' compensation and payroll information systems. The Department of Labor and Industrial Relations generally agreed with our conclusions. It agreed that safety and prevention programs are key components to reducing workers' compensation costs, and that efficient case management contributes to cost savings. The Judiciary does not agree with the recommendation to centralize its workers' compensation program under the Department of Human Resources Development. Besides noting that it is a separate and autonomous branch of government, the Judiciary maintains that the effectiveness of its system argues for its system's continued independence. Several of these agencies' clarifications have been incorporated into the report.

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Submitted by

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STATE OF HAWAII

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Foreword

This study was prepared in response to Senate Concurrent Resolution No. 203, Senate Draft 1 of the 1995 Regular Session which requested that the State Auditor conduct a study to improve efficiency, cost effectiveness, and accountability in processing claims filed against the State for workers' compensation benefits. The study was requested in response to legislative concern about expenditures and complaints about the processing of state employees' claims.

We wish to acknowledge the cooperation and assistance extended to us by officials and staff of the Department of Human Resources Development, the Department of Labor and Industrial Relations, the Judiciary, and other state and city and county departments.

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Chapter 1

Introduction

Like other employers, Hawaii state government is responsible for providing workers' compensation benefits to its employees who are injured on the job.

Over the past five years, the State's expenditures for these benefits have increased from over \$13.5 million to more than \$25.6 million. Expenditures have exceeded the initial appropriations. Transfers from other programs, and most recently an emergency appropriation, have been used to make up the shortfall.

Concerns about these expenditures and complaints about the processing of state employees' claims led to the passage of Senate Concurrent Resolution No. 203, Senate Draft 1 of the 1995 Regular Session. The resolution requested the State Auditor to conduct a study to improve efficiency, cost effectiveness, and accountability in processing claims against the State for workers' compensation benefits.

The study was to assess a variety of issues including the following: the structure of the system; the State's unfunded liability and reserving practices for claims; and incentives for workplace safety, accident prevention, and return-to-work programs.

The resolution asked the Auditor to submit findings and recommendations, including any legislative proposals, to the Legislature. This report responds to the Legislature's request.

Background

Nationwide, state workers' compensation laws provide injured workers with cash payments for a portion of lost wages, payments for medical services, and rehabilitation services. The concept behind these laws has been described as follows:

In exchange for giving up their right to tort actions, employees are to get swift and certain payment from the workers' compensation program without having to demonstrate that the employer was at fault. In exchange, employers enjoy limited liability for industrial injury or disease.¹

Between 1911 and 1948, all of the states enacted workers' compensation laws. Hawaii enacted its first workers' compensation law, Act 221, in 1915. The present law is Chapter 386, Hawaii Revised Statutes.

Basic elements of Hawaii's workers' compensation law

Chapter 386 covers both the public and private employment sectors. The law requires employers or a special compensation fund (described below) to pay compensation to employees or their dependents if the employee suffers personal injury either by accident arising “out of and in the course of employment,” or by disease “proximately caused by or resulting from the nature of the employment.” Compensation is not allowed for an injury incurred by an employee resulting from a willful intention to hurt oneself or another, by engaging in a physical altercation that is unprovoked and non-work-related (other than in self-defense), or by the employee’s intoxication.

In proceedings to enforce a workers’ compensation claim, the law presumes, unless there is substantial evidence otherwise, that the claim is for a work injury covered by the law, that the employee gave sufficient notice of the injury to the employer, and that the injury was not caused by intoxication or willful intention to injure.

Chapter 386 is a “no fault” law. It grants certain rights and remedies to employees and their dependents in the event of a work injury regardless of whether the employer is at fault. At the same time, it takes away employees’ right to sue employers in civil court for damages from the injury. Exceptions are injuries from sexual harassment or sexual assault, where employees can still sue.

Types of benefits under the law

Under Chapter 386, employees may receive benefits in various categories:

- *medical benefits* pay for treatment of the injury;
- *temporary total disability benefits* pay for wage losses while the employee is recovering;
- *permanent partial disability benefits* pay for permanent loss of some bodily function;
- *permanent total disability benefits* pay for the losses caused by the inability to return to work;
- *disfigurement benefits* provide additional compensation for permanent scars or deformities;
- *vocational rehabilitation services* are available in cases of permanent injury;
- *death benefits* give weekly benefits to the surviving spouse and children. A funeral and burial allowance is also provided.

Workers' compensation benefits are exempt from federal and state taxes.

Administration of the law

Chapter 386 puts the director of the Department of Labor and Industrial Relations in charge of all matters of administration pertaining to the law's operation and application. The director is given all powers necessary to facilitate or promote the efficient execution of the law. The director must supervise and take all necessary measures for the prompt and proper payment of compensation.

Special Compensation Fund

The law also includes the Special Compensation Fund, which was created in 1937. The fund has several purposes including: (1) enhance the employability of persons with pre-existing injuries, (2) reduce discrimination against persons with dependents, and (3) require employers to pay only for losses actually sustained in their employment. For example, the fund helps compensate workers who sustain injuries that worsen previous injury-related disabilities, those who do not receive prompt and proper workers' compensation from their employer, or those whose employers' default by moving to another state.

The state director of finance is the custodian of the fund and disbursements are made on the order of the director of labor and industrial relations. Fund receipts consist of charges made on self-insured employers and insurance carriers.

State of Hawaii as an employer

Generally, Chapter 386 treats state government like other employers. A significant difference, however, involves "security for compensation."

Private-sector employers must "secure" workers' compensation for their employees by one of several methods. Employers may purchase workers' compensation insurance from a private company, deposit security with the State, prove to the State that they are solvent and financially able to pay the compensation, or join a self-insurance or captive-insurance group. Sometimes employers will insure for claims exceeding a certain dollar amount.

In contrast, the state and county governments are not required to "secure" workers' compensation, although they may insure through an authorized carrier if they wish. Currently, state government is almost entirely self-insured. The Legislature appropriates funds to pay workers' compensation claims for state employees that will come due during the year, a "pay as you go" system. The Department of Human Resources Development provides centralized claims management (claims adjusting) services for many state agencies. Other agencies manage their own claims or, less commonly, contract with a private firm for claims management.

Recent state expenditures and claims

In FY1994-95, the State paid more than \$25.6 million for workers' compensation claims filed by its employees. In calendar year 1994, 3,416 new claims were filed; 3,745 cases were closed; and 5,825 cases were active. The oldest open case is from the 1940s.

In the past, shortfalls in funds initially appropriated to pay claims were covered by fund transfers authorized by the governor from savings of other programs as provided for in the state appropriations act. However, in March 1995 the Legislature made an emergency appropriation of \$5,531,787 to cover remaining claims for FY1994-95; no funds were transferred that year.

Problems with workers' compensation

Problems with workers' compensation have been identified extensively across the nation. Costs are a key issue for employers, insurers, and taxpayers. Fraud has also gained much attention.

Some observers believe the workers' compensation process has not served its original purpose. A recent report from the National Conference of State Legislatures summarized the philosophy underlying workers' compensation:

Inherent in the workers' compensation concept is the obligation to assure injured workers that the correct amount of benefits will be provided in a timely manner, with a minimum amount of dispute or need for litigation.²

Similarly, in Hawaii, a 1994 report of the Governor's Task Force on Workers' Compensation said, "The basic premise of the law is still valid—to provide a method for workers to get compensation for injuries incurred on the job without having to go to court."³

However, the governor's task force went on to say:

The clarity of the original purpose has been twisted out of shape by the usual push and pull of the various interest groups involved in the program. This has resulted in a system that is no longer efficient, no longer cost effective and no longer serves the constituency it was designed to benefit—the injured worker.⁴

The report said that most problems are in the operation of the system, not the law. The emphasis should be on making the system more efficient and cost effective.

Other writers have concluded that while the idea was to provide compensation “without the litigation and other sources of delay and antagonism found in the tort system,”⁵ the workers’ compensation system has not lived up to this expectation. Even after workers’ compensation laws were enacted, cases were still contested with time-consuming and costly administrative hearings, witnesses for both sides, and further legal delays.

The governor’s task force in Hawaii concluded, among other things, that existing data on workers’ compensation is not available on a timely basis and lacks sufficient detail for making fully informed policy decisions.

Recent developments in Hawaii

The 1994 report of the governor’s task force made recommendations for improving Hawaii’s workers’ compensation program as a whole and the State’s self-insured program. Cost control suggestions included overhauling the medical fee schedule, assessing the feasibility of managed care, establishing a workers’ compensation facilitator to assist employees with their claims, and strengthening safety education and return-to-work programs.

Act 234, SLH 1995, sought to reduce workers’ compensation costs of employers by such measures as limiting allowable medical charges, the frequency and extent of medical treatments, and strengthening the fraud provisions. Act 234 amended other provisions, including those related to the assigned risk pool. The act also required the director of labor and industrial relations and the insurance commissioner to conduct a comprehensive feasibility study of coordinated health care delivery systems as a potential alternative to the current system of providing medical care, services, and supplies under the medical care component of the workers’ compensation system. The study was recently forwarded to the governor.⁶

An earlier 1993 study of state government’s self-insured program by Advanced Risk Management Techniques, Inc. (ARM Tech), was conducted for the Department of Human Resources Development (then the Department of Personnel Services).⁷ The study recommended expanding centralized claims management for the remaining executive branch agencies and making certain improvements at the State Workers’ Compensation Division. The study also examined the desirability of state government using a third-party claims administrator but did not recommend this, citing a limited potential for cost savings and other factors.

Objectives of the Study

Our study had the following objectives:

1. Determine the roles, functions, and responsibilities of state agencies in the workers' compensation claims process for state employees under Chapter 386, Hawaii Revised Statutes.
2. Assess the efficiency, cost effectiveness, and accountability of the workers' compensation claims process for state employees.
3. Make recommendations as appropriate.

Scope and Methodology

Our study focused on the State of Hawaii as a workers' compensation employer. We examined the processing of workers' compensation claims of state employees from submission of a claim through compensability determination to the closing of a claim. We gave particular attention to the activities of the Department of Human Resources Development, which performs centralized claims processing on behalf of many state agencies. We also examined the role of the Department of Labor and Industrial Relations, which has key administrative functions under Chapter 386, HRS.

We examined the processing of claims in certain centralized and noncentralized executive branch agencies and at the Judiciary. We also obtained some basic information on how the Legislature handles workers' compensation claims of its employees.

We reviewed the possibility of centralizing claims processing for all state agencies and other approaches to improving the process. Other issues included how the State identifies its workers' compensation liability; the concept of reserves; and incentives for programs of workplace safety, accident prevention, and return-to-work.

We reviewed Chapter 386, pertinent administrative rules of the Department of Labor and Industrial Relations, agencies' mission statements, governor's directives, and guidelines of the national Governmental Accounting Standards Board. We also reviewed recent editions of the State's *Comprehensive Annual Financial Report* and the accompanying *Auditor's Compliance Report and Auditor's Report on the Internal Control Structure*.

We contacted the National State Auditors Association to identify techniques of other state governments for funding workers' compensation claims. For additional information, we contacted the National Conference of State Legislatures, the National Association of Insurance

Commissioners, the National Council on Compensation Insurance, and the International Association of Industrial Accident Boards and Commissions.

Fieldwork included interviews with administrators and staff at the Department of Human Resources Development, the Department of Labor and Industrial Relations, the Department of Accounting and General Services, and the Department of the Attorney General. We interviewed staff responsible for handling workers' compensation claims, workplace safety, and return-to-work programs at selected centralized and noncentralized agencies. We also interviewed union representatives, a representative of an injured workers organization, and workers' compensation administrators from the City and County of Honolulu, private sector, and other states. We reviewed functional statements, policies and procedures, meeting minutes, interagency memoranda, general literature on workers' compensation, recent reports on Hawaii, and other documents as applicable.

We examined a systematic sample of workers' compensation claims filed by state employees during calendar year 1994, from all centralized and selected noncentralized agencies. The purpose of the sample was to compare the rates at which claims were being accepted, denied, and denied "pending investigation."

Our work was performed from June 1995 through December 1995 in accordance with generally accepted government auditing standards.

Chapter 2

Description of the Process for Workers' Compensation Claims of State Employees

In this chapter, we describe the roles of state agencies in the workers' compensation claims process for state employees. We also describe the key stages in the process.

Just as in the private sector, the processing of claims against state agencies must adhere to the workers' compensation law, Chapter 386, Hawaii Revised Statutes, and administrative rules adopted by the Department of Labor and Industrial Relations. The basic steps in the process are similar for both the public and private sectors.

The employer or its representative engages in a process called claims management or claims adjusting. This involves such activities as the following:

- receiving employees' claims;
- investigating to determine whether the claim is compensable;
- reviewing physician reports and approving medical treatments and medical payments;
- determining wage replacement and disability payments;
- reaching settlements; and
- managing and directing disputed cases through the hearings and appeals process when necessary.

In the private sector, claims typically are managed (adjusted) by the employer's insurer for workers' compensation. In Hawaii state government, claims are usually managed by the employing agency or by the Department of Human Resources Development on the agency's behalf. One state agency retains a private claims adjusting company to manage some of its claims.

Roles of State Agencies in the Claims Process

The following is a summary of the roles of state agencies in processing workers' compensation claims filed by state employees. Agencies' activities vary according to their level of involvement and responsibility.

***Department of Labor
and Industrial Relations***

The Department of Labor and Industrial Relations is responsible for administering Chapter 386, promoting its efficient execution, and ensuring prompt and proper payment of compensation. The department must investigate injuries as necessary.

The labor department has original jurisdiction over all controversies and disputes arising under the law. It is authorized to adopt administrative rules to implement the law and has done so in Chapter 10, Title 12 of the Hawaii Administrative Rules.

The department's Disability Compensation Division records and maintains all workers' compensation forms, medical reports, and written statements submitted by employers and employees to the department. The division notifies employees of employers' denial of compensability and provides employees with information and necessary forms to protect their benefit rights.

To enforce the rules and fulfill the department's adjudication functions, the Disability Compensation Division conducts informal hearings, with staff hearing officers presiding, to determine compensability and payment amounts. The Labor and Industrial Relations Appeals Board, which is administratively attached to the department, conducts *de novo* hearings if determinations by the hearing officer are disputed; then the case, in effect, starts over.

***Department of Human
Resources
Development***

The Department of Human Resources Development, formerly the Department of Personnel Services, manages claims for many executive branch agencies, which employ about half of all state employees. Prior to 1985, each agency of the executive and legislative branches, and the Judiciary as a whole, managed its own workers' compensation claims. However, Act 285, the Supplemental Appropriations Act of 1984, required the department to establish a centralized workers' compensation program unit for the State.

The department carries out this centralized responsibility through its State Workers' Compensation Division. The division has 24 employees including 14 claim managers. The division manages claims for the following:

- Department of Accounting and General Services
- Department of Agriculture
- Department of the Attorney General
- Department of Business, Economic Development, and Tourism
- Department of Budget and Finance
- Department of Commerce and Consumer Affairs
- Department of Education (Oahu only)
- Office of the Governor

Lieutenant Governor's Office
Department of Hawaiian Home Lands
Department of Human Resources Development
Department of Labor and Industrial Relations
Department of Land and Natural Resources
Hawaii State Public Libraries
Department of Public Safety
Department of Taxation
Department of Transportation

These organizations are self-insured through the State for workers' compensation claims. They account for approximately half of the State's expenditures for claims payments; the noncentralized agencies make up the other half.

In addition to managing centralized claims, the human resources department has other responsibilities for workers' compensation. The State Workers' Compensation Division provides written and oral guidance to all executive branch agencies. This advisory function includes interpreting the workers' compensation law, sharing investigative techniques for determining compensability, and conducting workshops on new legislation affecting claims management.

The division also administers funds appropriated for workers' compensation benefits for general funded and some federally funded positions. In addition, the division reviews and approves *all* executive branch (centralized and noncentralized agencies') workers' compensation settlements. (Settlements are described at the end of this chapter.)

The Department of Human Resources Development has a Safety Branch that collects and monitors data for an extensive workers' compensation database for the executive branch. The Safety Branch also administers a Statewide Safety Program and coordinates the State Safety and Health Conference.

Centralized agencies

Employing agencies whose claims are centrally managed by the State Workers' Compensation Division record the injury on the appropriate forms and submit them to the division. They investigate the basic circumstances of the injury and report them to the assigned case manager at the division. The employing agency supplies data on wages and sick and vacation leave to the case manager.

Noncentralized agencies

State employees' workers' compensation claims are not fully centralized at the Department of Human Resources Development. The following are still not centralized:

Department of Defense
Department of Education (neighbor islands)
Department of Health
Department of Human Services
University of Hawaii
Judiciary
Legislature
Office of Hawaiian Affairs

Like the centralized agencies, the noncentralized agencies generally are self-insured through the State. However, the Hawaii Housing Authority purchases workers compensation insurance (through Alexander of Hawaii Inc.). The noncentralized agencies account for about half of all state employees and half of the State's expenditures for workers' compensation payments.

The noncentralized agencies turn to the State Workers' Compensation Division for advice as needed. Three units contract with Adjusting Services of Hawaii Inc. as case manager for all or some of their claims. These are the Department of Health's divisions of Adult Mental Health (including the State Hospital), Child and Adolescent Mental Health, and Alcohol and Drug Abuse. Also, the Hawaii Housing Authority uses Alexander of Hawaii Inc. to manage its claims.

Department of the Attorney General

The main activity of the Department of the Attorney General is representing both centralized and noncentralized agencies on appeals before the Labor and Industrial Relations Appeals Board. If the appeals board decision is appealed to the State Supreme Court, the Department of the Attorney General again represents the State. Also, the department sometimes represents state agencies in the informal hearings conducted by the Disability Compensation Division of the Department of Labor and Industrial Relations.

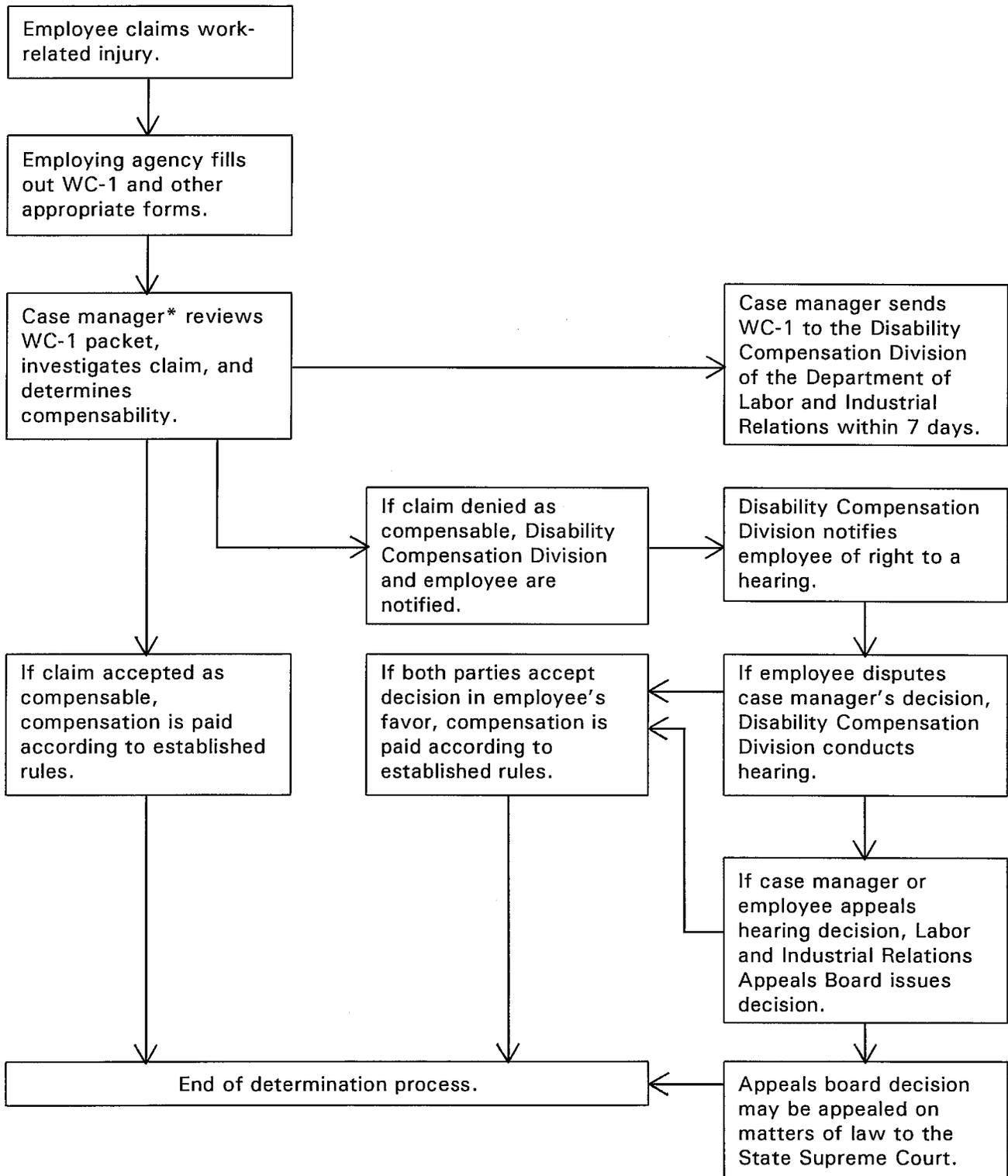
Department of Accounting and General Services

The Department of Accounting and General Services prepares vouchers for certain workers' compensation benefit payments. The department also must report the State's workers' compensation liability.

Key Elements of the Claims Process

The following narrative and Exhibit 2.1 describe the key elements of the workers' compensation claims process for state employees. The term "employing agency's representative" means the State Workers' Compensation Division of the human resources department or an outside company that manages an agency's claims.

Exhibit 2.1
Typical Elements in the Processing of State Employees' Workers' Compensation Claims



*The case manager may be a staff person of the employing agency, the State Workers' Compensation Division of the Department of Human Resources Development, or a private company employed to manage claims.

Start of the process

The claims process can be triggered in various ways. An employee may inform his or her employing agency of a work-related injury or illness. Or the employee may file a WC-5 form (Employee's Claim for Workers' Compensation Benefits) with the Department of Labor and Industrial Relations, with or without notifying the employing agency of the injury. Sometimes the first notice received by the employing agency or its representative is a medical provider's bill.

Employing agency's response

After receiving notice of a claim, the employing agency must prepare the WC-1 form (Employer's Report of Industrial Injury) to notify the labor department. The employing agency completes other internal forms and reports detailing the circumstances of the injury.

The employing agency or its representative sends the WC-1 to the State Workers' Compensation Division of the human resources department to receive a case number. The division then forwards the WC-1 to the Disability Compensation Division of the labor department within seven days of receiving notice of the injury. Most claims are accepted. Claims denied have frequently been denied "pending investigation."

Disposition of accepted claims

If the claim is accepted by the employing agency, the State provides compensation according to established rules including standard fee schedules and payment formulas established by Chapter 386, the administrative rules, and case precedents.

Disposition of denied claims

If the claim is denied by the employing agency, the Disability Compensation Division notifies the employee of this on a WC-18 form. The form instructs employees who believe their injury is work-related to protect their rights by filing a WC-5 with the division within 30 days and having their physician complete a WC-2 (physician's report).

After receiving the completed forms, the Disability Compensation Division schedules and conducts an informal hearing usually within four to twelve months. The hearing officer must issue a decision within 60 days of the hearing.

If either party appeals the ruling, the case goes to the Labor and Industrial Relations Appeals Board for a *de novo* hearing with formal procedures. The appeals process may take as long as two years.

A party who does not accept the appeals board's decision may appeal matters of law to the State Supreme Court.

Disposition of “pending investigation” denials

If it denies a claim “pending investigation,” the employer or its representative initially has 30 days to determine compensability. The Disability Compensation Division may grant additional extensions for more complex investigations.

For example, to investigate medical claims, employers can request a medical evaluation by a specialist. The evaluation is used in determining whether the claim is compensable and, if so, the amount. Evaluations may be delayed several months depending on the medical specialist or specialists involved. If compensability cannot be determined within the 30 days required by the rules, employers can request additional time.

If the employer continues to deny compensability after investigation, informal hearings and the appeals process are available.

Other proceedings and steps

If new evidence is discovered or medical aspects of the case change, either the employer or the employee may challenge the case in a new hearings and appeals process.

Employees may reopen closed cases; under Section 386-89c, HRS, the statute of limitations for reopening a case is eight years after the date of the last compensation payment.

Settlements

If an injured employee has received considerable medical treatment and still cannot return to work, a settlement with the State is made. The settlement usually terminates all employment and future compensation rights of the employee for a one-time cash payment.

All settlements with state employees within the executive branch are approved by the director of the Department of Human Resources Development before submittal to the Department of Labor and Industrial Relations for approval. The Judiciary approves its settlements and submits them to the labor department for approval.

Chapter 3

Conclusions and Recommendation

Hawaii's state government has taken steps to control the workers' compensation costs that it faces as a major employer. However, our study found that these efforts have not yet produced an integrated cost control *system*.

To ensure a systematic approach, we propose amending the Hawaii Revised Statutes to make the Department of Human Resources Development clearly responsible for overseeing, coordinating, and reporting on the State's management of its workers' compensation costs. The department would need additional resources to carry out this new mandate.

The department should directly manage each workers' compensation claim for all state agencies on a centralized basis. It should analyze the information needed to maintain and improve the system. Once adequate information is developed for analysis, the department can explore other options such as contracting out for claims adjusting services.

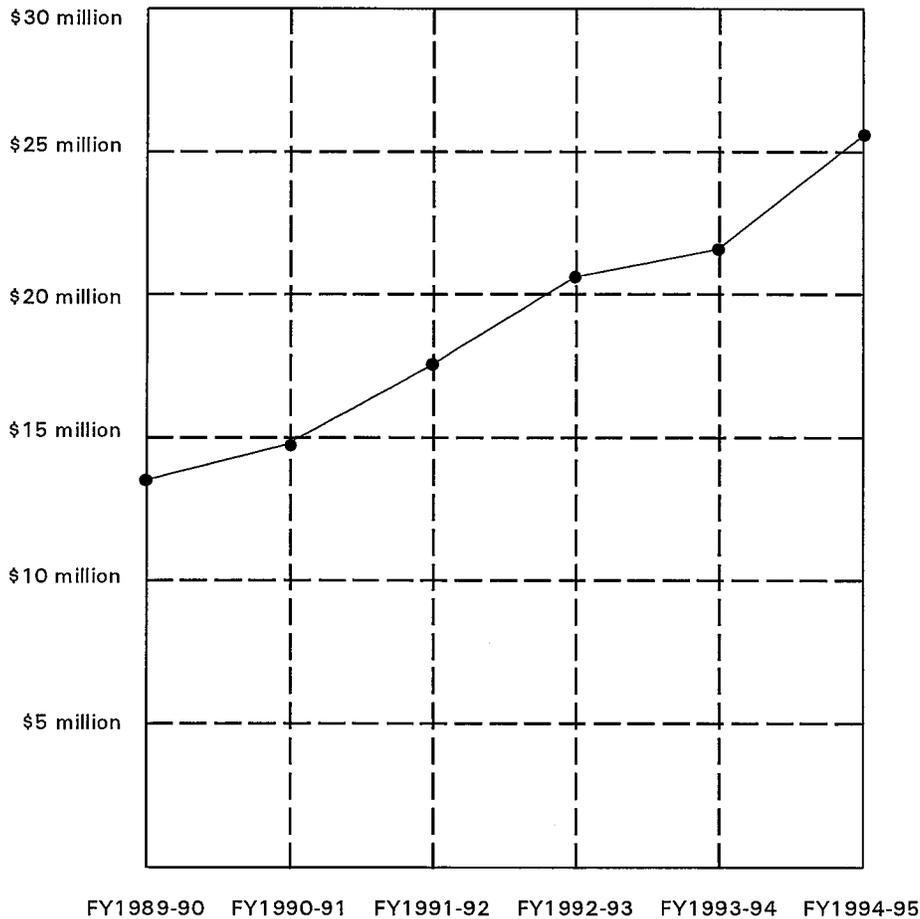
We believe that central accountability in the Department of Human Resources Development will best protect the interests of the State, its employees, and its taxpayers.

Systematic Cost Control By Employers Is Gaining Favor

The rising cost of workers' compensation is both a national and state concern. State government in Hawaii is concerned not only as a public policy maker and regulator, but also as the largest employer in the state. Strategies for systematic cost control are essential.

Payments for workers' compensation claims constitute a substantial cost to state government. From 1990 to 1995, expenditures rose from more than \$13.5 million to more than \$25.6 million. Payments were made from three sources: general, special, and trust funds. (See Exhibit 3.1.) State agencies bear additional costs of claims administration, adjudication, and other activities related to workers' compensation such as workplace safety and return-to-work programs.

**Exhibit 3.1
Workers' Compensation Expenditures for State Employees
1989-1995**



FUNDING SOURCE	FY1989-90	FY1990-91	FY1991-92	FY1992-93	FY1993-94	FY1994-95
General	\$10,402,100	\$11,594,268	\$13,367,553	\$15,910,885	\$16,623,170	\$19,547,636
Special*	\$3,036,027	\$3,289,594	\$4,261,560	\$4,579,047	\$4,580,424	\$6,058,495
Trust	\$44,644	\$62,027	\$66,755	\$272,245	\$348,944	\$40,622
TOTAL:	\$13,482,771	\$14,945,889	\$17,695,868	\$20,762,177	\$21,552,538	\$25,646,753

*Due to data limitations, the exhibit does not include amounts for state employees' claims paid from the Special Compensation Fund. Currently, these amounts are in the range of \$1.5 million annually.

Source: State of Hawaii Financial Accounting and Management Information System (FAMIS): Monthly Expenditure by Major Object reports; Department of Labor and Industrial Relations, Special Program Section; and the Workers' Compensation Special Compensation Fund Financial Statements and Forecast.

Elements of a cost-control system

Nationally and in Hawaii, efforts to control workers' compensation costs have included both statutory reform and management improvements. We identified some key characteristics of integrated employer programs:

- central accountability for cost control
- assertive, consistent, skilled claims management
- sufficient, readily accessible, and well-analyzed management information
- effective workplace safety and return-to-work efforts
- strong control of medical costs

The following discussion provides three examples of systematic cost-control approaches instituted by employers that have gained attention. One is a private employer in Hawaii. The others are state governments on the mainland known for their reforms.

Outrigger Hotels Hawaii

Hotel Operating Company of Hawaii, which manages Outrigger Hotels Hawaii, has approximately 2,400 employees in jobs such as housekeeping and office work. All workers' compensation costs are monitored through a central risk management office whose computer data base contains thorough case records for every on-the-job injury.

The company generates detailed data such as: injury incidence rates; average cost per claim and per employee; average medical cost per claim; and distribution of costs between medical costs (payments to health care providers) and nonmedical costs (payments for lost wages, disability settlements, adjusting costs, and legal expenses).

The company performs aggressive case management and emphasizes employee safety and training. Well-organized personnel and risk management departments are seen as crucial to cost control. The company claims success in controlling costs, and company officials have shared their workers' compensation strategies with state officials.

State of Connecticut

With about 50,000 state employees, Connecticut is comparable to Hawaii. Because workers' compensation claims costs for state employees were growing 21 percent faster than private-sector claims costs, Connecticut made major reforms in 1992 and reports significant cost savings as a result. In FY1994-95, workers' compensation expenditures of state government dropped 8 percent from the previous year.

Connecticut's system is centrally administered for all branches of government through the State Workers' Compensation Administrator in the Department of Administrative Services. The department has complete

information on all state government claims. It has established formal policies and procedures for claims handling. Overall state policy for the program is stated as follows:

BEFORE AN INJURY OCCURS: to provide a safe work environment and to promote safety in the workplace. Injury prevention programs are an essential part of the State Workers' Compensation Program.

AT THE TIME OF AN INJURY: to insure that an injury is reported immediately. An evaluation of the injury is conducted early and payments to the injured worker, and/or medical provider are issued promptly. All efforts to minimize hardship for an employee are emphasized.

AFTER AN INJURY OCCURS: to minimize the amount of time lost due to an injury and to place the employee back into the work environment as soon as it is medically possible either to the same position or to a modified job. Medical case management services, and light duty or alternative duty assignments are programs that help the employee return to his/her regular work quickly.¹

The department contracts with a third-party administrator for claims management and uses a managed care organization for medical services. Department staff oversee, monitor, and audit the activities of these two outside companies.

The third-party administrator is responsible for the administrative management of all state employees' workers' compensation claims from initial report, through compensability determination, to case closure and final settlements.

The managed care company is responsible for maintaining a statewide occupational medical care network and evaluating the medical status of each claim. The employee may choose a medical provider from a list of providers. The company screens and selects providers, and monitors their performance. In turn, the company is overseen by the Connecticut Workers' Compensation Commission.

State of Oregon

In Oregon, which has 55,000 state employees and volunteers, a single corporation administers state government's workers' compensation claims. The corporation, the State Accident Insurance Fund (SAIF), is an insurance carrier that is part of the executive branch of Oregon state government. Receiving no taxpayer support, the corporation derives all its income from premiums paid by policyholders and from return on its investments.

The corporation is self-supporting, not-for-profit, and publicly owned. The corporation provides workers' compensation insurance, manages claims, and pays benefits for state government, and for private-sector employers who choose to be insured through the fund.

The corporation's staff are responsible for claims management, loss control, return-to-work, fraud investigation, auditing medical bills, legal representation, underwriting, and marketing. Claims management staff receive extensive training. The corporation seeks to make quick, accurate decisions on claims and pay compensable claims as soon as possible.

Oregon has an innovative way of trying to keep workers' compensation costs down. Managed care organizations monitor medical treatment of injured workers. A 24-hour coverage pilot program includes state government as a participating employer. This is a residency-based universal health care system administered by the State or its licensed private insurance carriers. It combines group health insurance coverage with the medical portion of workers' compensation. The goal is to enhance delivery and cost-effectiveness of medical service. Possible advantages include no delays in obtaining treatment while compensability is being determined.

If the injury or illness is work-related, the claim is managed by SAIF. If the injury is not work-related, then it is paid for by the employee's managed care organization. (Due to its recent development, the pilot program has not yet been evaluated.)

Oregon claims that its return-to-work program resulted in major reductions in workers' compensation expenditures.

State of Hawaii Needs a More Systematic Approach

Hawaii's state government has taken significant steps to better control the cost of workers' compensation claims made by its employees. However, we found that the State has taken only partial action. A truly systematic approach—one of comprehensive, centralized management—has not yet been achieved.

The following discussion describes the progress made and the challenges remaining in developing a system. We discuss oversight; claims handling; management information and analysis; workplace safety; return-to-work; and medical cost control.

No single agency oversees entire program

No one department is fully accountable for overseeing, coordinating, and reporting on claims for and costs of workers' compensation for all state employees. Responsibilities are fragmented among various agencies. Key

officials are bogged down in processing claims, which leaves little time and resources available for oversight, management, and planning.

Responsibilities are fragmented

The Department of Labor and Industrial Relations, a key agency, is responsible for administering Chapter 386 with respect to both the public and private sectors, and ensuring prompt and proper payment of benefits. Through its Disability Compensation Division, the department focuses on recordkeeping, advising employers and employees, and resolving contested claims through informal hearings.

However, the labor department does not focus only on claims by state employees, and it does not represent the State as an employer. Rather, the department acts as a regulator of, and neutral third party between, the interests of both public and private employers and their employees who claim injury.

The other key agency, the Department of Human Resources Development, has specific, but not comprehensive responsibilities on behalf of the State as an employer. Act 285, the Supplemental Appropriations Act of 1984, required the department to use some of its general fund appropriations to establish a centralized workers' compensation program unit for the State and report on the unit's impact on the cost of claims. The governor has supported this centralized program and the Legislature has appropriated funds for its operations.

Act 285 did not define the meaning of "centralized." However, a 1985 governor's memorandum stated that in an effort to control "spiraling" costs, the department would eventually centralize all state employee claims.²

For the executive branch's self-insured program, the department's State Workers' Compensation Division currently manages claims for many state agencies, advises other agencies on claims management, approves all settlements, and administers appropriations to pay workers' compensation benefits for employees occupying general funded and certain federal funded positions. The department also has key responsibilities for workplace safety and return-to-work. The department says it lacks the resources to provide additional centralized services. Indeed, *decentralization* has also been discussed recently.

The department has said that the State has the responsibility "to lead and to do everything possible to reduce the cost of workers' compensation, which is being paid by tax dollars."³ Act 285 required the department to report to the 1985 Legislature on the effect of the centralized program on reducing the cost of workers' compensation claims against the State. A report was issued, but it did not discuss cost impact.

State is bogged down in claims processing

State agencies are currently bogged down in processing claims. For example, at the State Workers' Compensation Division, claims are handled by staff who range from personnel technicians to management. Top administrators at the division are heavily involved in day-to-day claims management. Administrators have little time to plan or manage for centralized claims. They lack the time and explicit statutory authority to effectively oversee and coordinate the needs of the State as a whole.

Division administrators acknowledge the need for attention to management and planning. However, during our study, the division administrator and the claims management branch chief were personally handling 100 and 250 individual claims, respectively. In addition, they were actively involved in other cases. The division administrator or the claims branch chief makes initial determinations of compensability in all centralized cases. The administrator approves all settlements in the executive branch. Review of settlements prior to approval is conducted by the administrator for noncentralized agencies and the branch chief for the centralized agencies.

Claims management is not consistent

An employer's management of workers' compensation claims should be both assertive and consistent.

Assertive claims management does not mean denying all claims. It does mean, however, not *automatically* accepting claims that may not be compensable under the law or paying medical bills that are not legitimate. The State Workers' Compensation Division describes case managers' dual responsibility as (1) assuring that legitimate claims are fairly, accurately, and timely processed so that the injured employee receives all benefits required by law and (2) denying claims that should not be paid. Assertive claims management also requires efforts to control fraud.

Consistent claims management fosters clear expectations and predictability. Spreading the handling of claims among many agencies lends itself to inconsistencies. Limited policies and procedures and uneven training and expertise also contribute to the problem.

Agencies' approaches differ

We found that state agencies vary in their approach to claims management. For example, the State Workers' Compensation Division has been perceived as taking a tougher approach in managing the claims of the centralized agencies. Our systematic sample supports this perception.

We sampled claims filed in calendar year 1994 from two groups: all centralized agencies and four noncentralized agencies (the Department of Education (neighbor islands), the Judiciary, the Research Corporation of the University of Hawaii, and the University of Hawaii). Of these two groups, we compared the rate of claims initially accepted, denied, and denied pending investigation. We found that the four noncentralized agencies as a group accepted a slightly higher proportion of claims as compensable than did the centralized State Workers' Compensation Division. The noncentralized group also denied claims "pending investigation" less often than the centralized division. (See Exhibit 3.2.)

**Exhibit 3.2
Claims Management Comparison, 1994**

Initial Disposition of Claims	State Workers' Compensation Division (Centralized Agencies)		Noncentralized Agencies	
	Number	Percent	Number	Percent
Claims accepted	225	83	191	90
Claims denied	45	17	22	10
Total number of claims	270	100	213	100
Claims denied pending investigation (a subset of claims denied)	41	15	18	8

Source: A systematic sample of WC-1s filed at the Department of Labor and Industrial Relations. Results of the sample are plus or minus 4 percent at the 95 percent confidence level.

While other factors may influence the rate of claims accepted and denied—such as the nature and complexity of claims—the different rates may also reflect different standards and approaches for claims management.

Our recent *Financial Audit of the Hilo Medical Center*, Report No. 96-4, revealed a case of particularly unassertive claims management in a noncentralized agency. We found that this state-run facility pays approximately \$1.3 million a year in workers' compensation claims costs. But the center does not monitor the status of open claims.

Once a claim is filed, the center continues to pay medical bills, salary, and other costs without limit. Although each medical bill and payroll charge is reviewed prior to payment, no one is responsible for managing each case or trying to minimize costs for these claims. No one evaluates the merit of each new claim or challenges claims that do not appear to be valid.

Officials of certain neighbor island offices of the Department of Education, where claims are not centralized, report such problems as excessive caseloads increasing the possibility of inappropriate charges. Cases cannot be properly managed and there is a lack of human and financial resources to rebut the employee's evidence.

Another example of inconsistency is the handling of claims denials. In managing claims for the centralized agencies, the State Workers' Compensation Division sends only basic information indicating that compensability is being denied while compensability is being determined. The letter provides little explanation of the nature of the denial and the reasons for it. However, the Judiciary, which manages its own claims, sends written notification explaining more specifically why further investigation is necessary and what happens next. This notification procedure promotes better understanding between employees and employers and builds goodwill.

Policies and procedures are limited

The State lacks standard guidelines for claims management for all agencies. Claims managers from the State Workers' Compensation Division and the noncentralized agencies report that claims are handled on a "case-by-case" basis. The division's claims managers rely heavily on oral consultation with their supervisors.

We know that each case may have unique aspects and that supervisors are a valuable source of information. Still, claims tend to have certain consistent attributes, such as the need to gather and evaluate information, as well as the basic reasons for accepting or denying compensability. Other states have established official policy and procedure manuals providing guidance on these subjects.

The State Workers' Compensation Division has been developing a detailed manual for its case managers. A recent study of the State's self-insured workers' compensation program by Advanced Risk Management Techniques, Inc. (the ARM Tech study) recommended that the division "create at least a rudimentary procedures manual to serve as a resource to claim handlers."²⁴ We found that the division has a draft procedures manual in its fourth rewrite. The draft manual contains much useful

information. However, while many case managers are familiar with the draft manual, several stated that they do not use it because it is not current. Some use a manual issued by a private adjusting company. Furthermore, noncentralized agencies vary in the development of policies and procedures.

Expertise and training are uneven

The background, expertise, and training of the State's claims managers vary widely.

On-the-job training is important. But claims managers also need regular formal training to guide them in managing their caseload and help ensure that claims are being handled consistently.

Formal training for claims managers in the State Workers' Compensation Division varies and appears somewhat limited compared, for example, to what is offered to claims adjusters in Oregon. Training for claims managers in the noncentralized agencies is largely on-the-job, and formal training is limited or nonexistent.

No systematic fraud monitoring occurs

We also found that neither the division nor the noncentralized agencies monitors claims for fraud formally and systematically. Efforts to control costs are weakened when a system goes unmonitored. Furthermore, this leaves the extent of fraud open to speculation and rumor.

Better management information and analysis are needed

We found that management information on workers' compensation claims against the State is weak in two key areas. First, information and analysis on all claims against the State is insufficient. This hinders overall management, planning, evaluation, reporting, and meeting established accounting standards. Second, information for managing the State Workers' Compensation Division is inadequate due to limitations in the areas of case status reports, case tracking, and case summaries.

Overall data and analysis are insufficient

Workers' compensation agencies must have ready access to accurate, consistent, complete, and timely data in order to carry out their responsibilities. Data are necessary in order for management to understand how the system is performing and what it costs.

In examining programs in other states, we found that a major concern is the need for complete and accurate information on all claims filed against the state. Several states report they have the ability to obtain complete and accurate information about all their claims. Two "reform" states—

Connecticut and Oregon—can readily obtain detailed information on claims both for state government as a whole and for individual departments.

Claims against the State of Hawaii are processed by a variety of agencies. A wealth of data is collected and reported about these claims by the Department of Human Resources Development and the Department of Labor and Industrial Relations. However, no one agency has the responsibility or authority to collect and analyze basic information and statistics for all claims against the State in all branches of government with the goal of purposefully managing the State's costs. During our study, we found it difficult to obtain reliable, consistent information about expenditures for these claims. The lack of information and analysis prevents meaningful efforts to plan, manage, evaluate, and report on the State's claims and costs.

We also found no agency collecting and analyzing comprehensive information on the administrative costs incurred by all the agencies in processing claims.

Lack of information undermines ability to meet accounting standards

A state's ability to identify its workers' compensation liability is not only a sound financial and management practice, it is a professional accounting standard. Hawaii's lack of information is making it difficult to meet the standard.

Since FY1992-93, Ernst & Young has advised the State in its *Auditors' Compliance Report and Auditors' Report on the Internal Control Structure*, to comply with Statement Number 10 of the Governmental Accounting Standards Board (GASB). The national board's statements apply to financial reports of all state and local governmental entities. Under "GASB 10," *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, these agencies, other than risk pools, are required to report an estimated loss from claims as an expense and as a liability if information is available indicating that it is probable that a liability had been incurred at the date of the financial statements, and the amount of the loss can be reasonably estimated. Failure to comply with the standard can result in a "qualified opinion" by auditors and jeopardize the State's bond rating.

In order to comply with GASB 10, the State needs to be able to identify all of its workers' compensation claims and expenditures for those claims. The Department of Accounting and General Services is responsible for preparing the State's Comprehensive Annual Financial Report and has been trying to obtain the information necessary to comply with GASB 10.

The department says that if payroll and third-party payment information for each claim were available, the amount of loss could be reasonably estimated. Once this information is obtained, then the department can hire an actuary to estimate the liability for claims incurred but not reported. However, the necessary information for actuarial estimates is not readily available. The department has found no basic information on claims and payments that is centralized in any of the state databases. The department says that payments made, corrections, and adjustments are available in individual claimants files, but manually retrieving this information would be too time- and labor-consuming.

The Department of Accounting and General Services says that if the State is unable to report its workers' compensation liability, the State could receive a qualified opinion in its *Comprehensive Annual Financial Report*. This means that the financial statements are fairly presented except as affected by certain areas where there is insufficient information.

Incomplete and inaccurate information is scattered among databases

Central to the State's information problem is the scattering of incomplete and inaccurate information among computerized databases.

Three major databases contain workers' compensation claim information. The Disability Compensation Information System of the Department of Labor and Industrial Relations has workers' compensation claims information for all public and private employers. However, this database does not contain sufficient detail on individual claim payments.

The Department of Human Resource Development has two databases that track workers' compensation claims information, the Comp2000 database and the Accident Information Reporting System (AIRS) database. However, Comp2000 tracks claim information only for centralized agencies, covering just half of the State's employees. AIRS includes payment and claim information for the executive branch but has proven to be inaccurate. According to the Department of Accounting and General Services, when efforts were made to trace temporary disability payments back to nine agency claim files, AIRS matched the dollar amount in only three files. The department found that corrected payments are not entered into AIRS. The human resources department does not regularly audit the integrity of the information in this database.

The Department of Accounting and General Services is currently attempting to use the State's payroll system to track workers' compensation payment information. However, since the payroll system contains social security numbers but not workers' compensation claim numbers, it is difficult to obtain payments by claim number for employees with multiple claims.

Ideally, the Department of Accounting and General Services says, it needs access to an automated system that includes each state employees' name, social security number, and workers' compensation claim number. Records should show individual claimant information, all claims filed by claimants, and the history of payments made, and incorporate any payment or other corrections. Once this information has been obtained, the department can hire an actuary to compute an estimate of the State's liability for claims which have been incurred but not reported. (The actuary will need to have ten years of data. AIRS contains only three years of data. The payroll system has twelve years of data.)

State Workers' Compensation Division lacks adequate internal information

The State Workers' Compensation Division does not develop all of the information necessary to manage its program. It lacks regular status reports on its claims management operations, adequate case tracking against statutory deadlines, and summaries of case status and activity.

First, the division does not require its claims managers to submit status reports on their caseload. Claims managers seem to be absorbed with keeping up with their daily tasks. They say most of their time is spent processing and verifying medical bills, corresponding with and phoning physicians and claimants, and reviewing medical reports.

A pilot reporting requirement begun in 1994 was discontinued because the supervisors' own caseload left them with little time to review the reports. Currently, the only reports are case summaries produced when claims are reassigned to another staff person.

Without comprehensive, periodic claim reports, the division lacks necessary information to formulate management strategy and monitor whether claims are being managed in accordance with established standards.

Second, case tracking is weak despite the human resources department's two automated workers' compensation systems. The Comp2000 database is used primarily to ensure timely medical payments meeting the 60-day time frame established in the medical fee schedule. The Accident Information Reporting System (AIRS) is designed to provide details on the types of accidents and costs so that agencies can analyze and reduce their workers' compensation costs.

Neither of the two systems tracks case activity against all of the time frames required by law. For example, under Section 386-31b, dealing with temporary total disability, the first payment of benefits must occur no later than the tenth day after the employer has been notified of the

disability. However, we were informed that it is not possible to obtain a printout of the number of claims that met this deadline.

Likewise, neither the division administrator nor supervisors track whether case managers have submitted written reports to the Department of Labor and Industrial Relations when compensability is denied under Section 12-10-73 of the Hawaii Administrative Rules. The administrator simply expects her staff to be professionals and meet their own deadlines.

However, we found that Oregon monitors the status of its claims against statutory and other time frames. This information can help administrators ensure that staff are managing their claims appropriately and expeditiously.

Third, claim files do not include an overall summary of claims management activity. Summaries could list, for example, the date of occurrence of the accident, the date the claim was filed, statutory deadlines, the date of first payment, type of payment, amount paid, listing of forms filed, hearing notices, decisions, and settlements. According to division staff, case managers are not required to document such information manually or enter such data in the Comp2000 database. Case managers may or may not utilize the Comp2000 notepad function for such a summary listing or create “tickler” files. Thus there is no quick way to determine the history of activity for a particular claim file without reviewing each document in the file.

Maintaining a summary listing/chronology on either the computer or the hard copy file (or both) is both a good business practice and common sense. A summary also serves as an index to identify documents in each file. Without this control, it is difficult to keep track of file contents. A consistent listing procedure would allow other staff to determine the status of any case at any point in time, for example if the case manager is ill, changes jobs, or retires.

The ARM Tech study recommended that the division equip each claim manager’s work station with a terminal and keyboard. This has been accomplished. ARM Tech also recommended that the Comp2000 system be fully implemented to utilize its capability to consolidate activity such as claims management, payment processing, management analysis, and the loss listings used by the department’s Training and Safety Division. This has not yet occurred.

Workplace safety and return-to-work will need more coordination

Workplace safety programs achieve savings by reducing employee injuries. Return-to-work programs achieve savings by returning injured employees to productive employment as soon as possible.

The Department of Human Resources Development has key responsibilities for safety and return-to-work programs in the executive branch. The safety program is administered by its Safety Branch, while the return-to-work program is administered by the State Workers' Compensation Division. The division's commitment to workplace safety and return-to-work programs is expressed in its mission statement:

To assist agencies of the executive branch in providing employees a safe and healthful workplace; delivering workers' compensation benefits; and to assist in returning our valued human resources to the work place as prescribed under the Hawaii Revised Statutes and related administrative rules.

We found, however, that the emphasis on safety and return-to-work programs varies among agencies.

Safety and accident prevention activities vary

Safety awareness and training programs for both management and staff are key to preventing accidents. The primary objective of the Safety Branch is to assist state agencies to comply with federal and state laws relating to occupational safety and health. This is done through training and identifying trends in accidents and injuries.

The branch acts as a consultant to the executive branch agencies. It has given on-site training in ergonomics and safety inspections, and has provided safer equipment for employees. The branch also awards certificates of merit to agencies that meet or exceed safety targets.

Implementation of, and commitment to, safety programs varies among state agencies. Some agencies, such as the Department of Education and the Department of Transportation, have developed excellent manuals integrating their safety and workers' compensation programs. Other agencies are less organized.

Return-to-work activities need monitoring

Claim costs rise when an injured worker is off the job. Extended time loss, mounting medical bills, and litigation costs increase claim expenses. To control these costs, return-to-work programs include establishing light-duty positions, modifying work environments to accommodate partially disabled employees, and accepting qualified employees from other agencies when the initial agency cannot accommodate its injured employees. Return-to-work programs help workers recover, be productive, and cut workers' compensation costs.

In April 1994, the governor issued Administrative Directive No. 94-02 establishing the policy that each department head give injured and disabled state employees priority consideration in returning to

employment. These employees are to be returned to their regular work, with or without reasonable accommodation, or assigned to light or moderate work. The Department of Human Resources Development is directed to develop a return-to-work priority program and assist in developing, maintaining, and implementing the program at the department and agency level.

To promote the intent of the April 1994 directive, the governor in October 1994 issued Administrative Directive No. 94-05, which made all departments, regardless of whether their claims are managed by the State Workers' Compensation Division, responsible for the cost of temporary wage loss replacement benefits (temporary total and temporary partial disability) under the workers' compensation law as long as the employee is on that department's payroll. Prior to the directive, these benefits, like other benefits, were being paid by the appropriation administered by the Department of Human Resources Development. The Department of Accounting and General Services is to assist in implementing the directive. The October 1994 directive also required the department to work in partnership with other departments to reduce the frequency of work-related injuries by providing or arranging for safety prevention and jointly providing for work inspections.

Since the April 1994 directive, the State Workers' Compensation Division has conducted workshops with all executive agencies and has written an informational brochure explaining the return-to-work program.

However, the division's Return-to-Work Unit consists of one registered nurse who primarily assists centralized agencies with individual return-to-work cases. At the time of our study, this nurse was spending more time as a medical consultant to the division's case management staff. The nurse was not assisting the noncentralized agencies and had no information on their return-to-work programs.

Also, the division is not monitoring the progress of the return-to-work programs at the centralized agencies by gathering statistics on the number of placements by agencies. The division has no plans to report statistics of the return-to-work program. Program documentation does not emphasize controlling costs.

State agencies have varying levels of involvement in return-to-work. Some agencies, like the Department of Education, have already developed policies and procedures. At the education department, this reportedly has resulted in at least nine injured employees being assigned to light duty assignments in the past year. At the Department of Accounting and General Services as many as six injured employees reportedly have been on light duty work assignments at one time. Other departments also

report some success in returning injured employees to work. These successes could be increased with more coordination and monitoring.

As a contrary example, the Hilo Medical Center has problems in workplace safety and return-to-work. In our recent financial audit of the center,⁵ we found that the center does not have programs in place to actively encourage job safety and minimize the occurrence of workers' compensation injuries. The center lacks aggressive safety programs that reward workers for remaining injury-free. Prevention of workers' compensation injuries would reduce the amount of payments the center is required to make on behalf of injured workers. Our audit report noted that the medical center should investigate the cause of each injury and ensure that future injuries can be prevented, and that the center should work with injured workers to rehabilitate them and get them back on the job as quickly as possible.

Control of medical costs is an emerging issue

Like the health care system as a whole, the medical treatment and reimbursement side of workers' compensation is complex. Over the past 20 years in Hawaii, medical benefits costs under workers' compensation have risen from about 27 percent to 43 percent of total workers' compensation benefits. Control of medical costs has proven difficult.

Aggressive claims management, fraud control, and tighter medical fee schedules can help control medical costs. However, these are only part of the picture. As other states have shown, systems such as managed care also hold promise. Hawaii is beginning to look at this option in relation to both private- and public-sector workers' compensation and the State has recently issued a report on the subject.⁶

Department of Human Resources Development Should Be Made Responsible for Oversight, Coordination, and Reporting

Hawaii's workers' compensation activities for state employees could benefit from strong leadership in providing effective oversight, coordinating agencies' responsibilities as employers (to include handling all agencies' claims in all branches of government), and compiling, analyzing, and reporting needed information. We believe that the Department of Human Resources Development, which has already been moving in this direction, is appropriate for this role. We propose that the Legislature consider amending the Hawaii Revised Statutes to clearly establish the department's responsibilities and authority, and provide the department with the resources needed to carry out its duties effectively.

Human resources department is the best choice

The principal "candidates" for centralized authority are the Department of Labor and Industrial Relations and the Department of Human Resources Development.

The human resources department is the best choice. It already centrally manages claims for many state agencies in the interests of cost control. It advises other, noncentralized agencies on workers' compensation, and has developed expertise in many workers' compensation matters involving state employees. The department also administers the statewide safety program and the return-to-work program.

While the labor department is the designated administrator of the workers' compensation law, we do not believe it is the best choice to represent the State as an employer. The department's primary responsibilities are promoting the efficient execution of the law and ensuring prompt and proper payment of claims—for both the public and private sectors. Furthermore, the department is heavily involved in adjudication of disputed claims and advising both injured employees and employers—in a neutral manner—on the process. These responsibilities may conflict with having oversight and management responsibility for controlling the cost of claims by state employees.

Legislation will be required

Currently, the State's responsibilities as an employer in the area of workers' compensation are set forth in a variety of sources: statutes, session laws, executive memoranda, interagency understandings, and agency functional statements, and so on. Moving toward a completely centralized approach can best be accomplished by amending Chapter 26-5, HRS, to establish a firm foundation for the program.

The new law should specify key duties and powers of the Department of Human Resources Development that begin with policy setting and encompass other responsibilities such as full centralization, data gathering, and development of other cost control strategies.

Set system-wide policies, goals, and objectives

The law should make the department responsible for developing policies, goals, and objectives for controlling the State's costs and reporting this information and analysis to the governor and Legislature on a regular basis. Policies and goals could be similar to those in Connecticut specifying what the State as an employer will do before, upon, and after an injury. Specific objectives could include, for example, reducing claims or costs by a certain amount each year.

Centralize all claims management

The department should also be made responsible by statute for centrally managing the claims of all state agencies in the three branches. (The exception would be rare instances such as the Hawaii Housing Authority, which has a workers' compensation insurer.)

Centralization has advantages and disadvantages. On the one hand, centralization could help ensure uniformity and objectivity in claims management, avoid duplication of effort, promote overall efficiency, and build expertise. It would get individual agencies' administrators out of the business of deciding whether to accept or deny employees' claims, which uses up valuable resources and can interfere with management goals such as coaching employees and addressing other agency priorities.

Centralization also has the potential to better control costs by ensuring that claims are managed assertively. As explained above, genuine case management is not always occurring at the noncentralized agencies.

On the other hand, centralization could lead to more bureaucracy and less individual attention to the injured workers' needs. Centralization could depersonalize claims management by removing it from the agency where the injury took place and possibly making it more difficult for employees to get information about their claim.

We believe that the benefits of centralization outweigh the costs. The ARM Tech Study recommended expanding the existing centralization to include the departments of Defense, Education (neighbor islands), Health, and Human Services, believing this would reduce workers' compensation loss payments by more than 1.2 percent. We recommend centralizing *all* claims management for all branches of government.

Gather and analyze data

Another statutory duty of the human resources department should be to compile and analyze complete, accurate, and timely information about state employees' claims for workers' compensation and the costs of administering and paying these claims. The department should also be required to develop reports, tracking systems, and case summaries necessary to operate centralized claims management.

The need for timely, complete, and accurate data cannot be overemphasized. This information must be collected according to a prescribed format not only for the benefit of management and planning, but also to enable the State to fully comply with national accounting standards. Once this information is obtained, the State can set a course of action to purposefully gain control over and manage its more than \$25 million annual expenditures for state employees' claims and the added costs of administering the system.

We recommend that the department identify its data needs and develop reporting requirements, in accordance with legislative directions. In this way, progress can be monitored and sufficient data will facilitate fully informed policy making.

Coordinate the State's workplace safety and return-to-work efforts

The law should solidify the department's existing mission of assisting agencies with safety and return-to-work activities. For return-to-work, the department would have the responsibility and authority to oversee and monitor and report on agencies' efforts to establish light duty positions, modify work environments to accommodate partially disabled employees, and accept qualified employees from other agencies when that agency cannot accommodate its injured employees.

Evaluate cost control strategies such as third-party administrators

As previously discussed, other states have developed various approaches and strategies for cost control including third-party administrators. The third-party administrator's responsibilities usually include evaluating claims for compensability, determining benefits, issuing payments, fraud monitoring, contesting questionable claims, and representing the State at informal hearings.

We believe that it is too early to assess the costs and benefits of a third-party administrator. Only when the department has the authority and ability to gather accurate and complete information on all claims against the state and the costs of administering them will assessment of this issue be possible.

The ARM Tech study did not recommend using a third-party administrator for several reasons. These reasons included the following: the limited potential for cost savings; difficulties in getting a firm quote from companies (because they bill on an hourly basis and it is difficult to predict claims activity); uncertainty as to whether insurers in Hawaii could competently handle the large volume of state claims; a volatile insurance climate in Hawaii; and limits on the executive branch's ability to maintain and perhaps increase its control over the State's workers' compensation claims.

We think the ARM Tech conclusion is premature and pessimistic. Instead of managing claims in-house, the State could hire an adjusting company to manage all of its claims as is already done for a few agencies. The State would mainly plan and oversee the company. Another approach would be to hire an adjusting company to handle more difficult claims such as those involving stress or back injuries.

A principal advantage of using a third-party administrator is standardization of service. This may also be cost-effective. A recent study for a private-sector firm found that the quality of adjusting services contributes to reducing the average cost per claim. However, the cost of

hiring an outside company involves not only the contractual fees but also the incidental expenses necessary to administer the contract.

A third-party administrator may provide more efficient services than state agencies which are constrained by lengthy delays due to the civil service position classification system, and the difficulty of filling position vacancies during the current fiscal constraints. These constraints can delay the claims process and contribute to higher costs.

Although the ARM Tech study did not recommend that the State Workers' Compensation Division use a third-party administrator, the State may wish to revisit this issue. Examining feasibility of a third-party administrator would require, for example, analyzing what job classifications are appropriate for state employees who handle claims and developing standards for how many cases a claims administrator should handle. This information is necessary for comparing the costs of in-house claims management versus contracting out.

***Additional resources
will be needed***

If the human resources department is to take over central responsibility, it will need additional resources. One cost effective source of resources could be the reallocation of positions and funds from the noncentralized agencies.

With better management information and improved policies and procedures, some of the department's workers' compensation staff could be freed up for higher-level oversight, coordination, and reporting activities. Improved delegation could also help. In our contacts with private sector claims managers in Hawaii and workers' compensation administrators in other states, we found that top administrators do not personally manage claims (unlike the situation in the State Workers' Compensation Division). Also, compensability decisions are delegated to supervisors and staff.

Even with these improvements, additional staff would be needed, especially considering that the ARM Tech study concluded that the department's claims managers already have a higher-than-normal caseload.

Some additional claims management staff could be transferred from other agencies, as has occurred in the past, when their claims are centralized. We know from our study that at least three staff members are working full-time on claims management in noncentralized agencies and at least 23 are working part-time on claims. Probably there are others scattered throughout the agencies. However, it will also be necessary to ensure that some staff capacity remains at the agencies to handle the basics of workers' compensation.

Other Issues Need Attention

Reserves issue is complex

During our study we found certain other issues that need attention. These include reserves, managed care, and antagonism in the system.

The resolution that requested our study asked for suggestions concerning reserves. However, “reserve” can have more than one meaning. For example, it can be a method of funding workers’ compensation liability. According to the Department of Accounting and General Services, there is no federal requirement nor Governmental Accounting Standards Board requirement that the State establish a reserve.

Hawaii state government is mostly self-insured for its workers’ compensation liability, a status authorized under Chapter 386, HRS. The State funds its workers’ compensation liability through appropriations. The Department of Human Resources Development biennially requests a legislative appropriation based upon historical data on total general funded workers’ compensation expenditures and other trend factors.

According to the National State Auditors Association, states take a variety of approaches for funding workers’ compensation claims. Some states are like Hawaii; they are self-insured. These include, for example, California, Florida, Kentucky, North Carolina, Ohio, and Virginia. According to Florida’s state government insurance administrator, establishing a reserve was considered and abandoned due to the large financial burden it would create.

Oregon has established a reserve and a quasi-public fund that insures its state government workers’ compensation claims. In Oregon, reserves are computed, as each workers’ compensation claim is filed, for the life of the claim. This dollar amount is set aside in the fund. This administrator noted that the key to establishing a reserve is having enough money. The fund administrator noted that Hawaii does not have to set up a reserve because workers’ compensation bills are paid by state appropriations.

“Reserves” can also refer to requirements that insurers must meet in order to do business in a state, and to amounts identified with particular claims as a means of estimating potential liability. The issue of reserves is complex and is one of the areas that a centralized agency could explore in detail. Coping with this issue will require full cost information, which is not yet available.

Considerable antagonism exists between the State and injured employees

The workers’ compensation process is supposed to be as prompt and free of disputes as possible. However, we found that the claims process for state employees is often perceived as frustrating, inconsistent, and unfair.

There are charges of slowness in determining compensability, lack of readily available written information about the process, and a reluctance to provide information even upon request. Although workers' compensation laws are supposed to minimize litigation, many employees feel they must hire attorneys to advocate for their benefits and to obtain basic information about the status of their case.

The workers' task force representative and certain union officials regard the process as being unfair and weighted in favor of employers. Many of the complaints are directed at the State Workers' Compensation Division of the Department of Human Resources Development.

At the same time, a key state official expresses concern about abuse and sees the division as performing very well with a heavy caseload.

Naturally, some antagonism is bound to arise between the State as an employer, with its interest in avoiding excessive and inappropriate payments, and employees and their representatives, with their interest in obtaining the maximum allowed by the law as speedily as possible.

Although the nature of the system makes conflict inevitable, we did find that certain improvements could reduce some antagonism.

“Denied pending investigation” illustrates conflict

Injured employees and their representatives point out that denying claims “pending investigation” is a source of great frustration. They charge that this results in weeks or even months of delay, requiring employees to use their accumulated sick or vacation leave.

Critics of “denied pending investigation” also suggest that claims managers at the State Workers' Compensation Division may not fully understand that Chapter 386, Hawaii Revised Statutes, the workers' compensation law, contains a presumption that each claim is compensable. One critic says that nothing in the law explicitly authorizes “denied pending investigation.”

The State's perspective is quite different. According to claims managers at the division and at the noncentralized agencies, claims may need further information to determine whether if the injury is work related. Claims managers point to strokes, heart attacks, back injuries, and stress as examples of claims which often are denied until the circumstances are more fully investigated.

A recent change in the administrative rules of the Department of Labor and Industrial Relations may result in fewer denials. In response to the high volume of denials and their perceived frivolous nature, the labor department strengthened Section 12-10-73 of the rules to require that

employers who deny compensability must submit a written report to the department within 30 days. The labor department may grant extensions upon receiving the written explanation showing good cause. A labor department official reports a 75 percent reduction in the State Workers' Compensation Division's use of "denied pending investigation." The official noted that the reduction may be due to the stronger rule or due to the State Auditor's current study. The division has indicated it plans to provide more specific explanations when it denies claims in the future.

While efforts to resolve the issue of "denied pending investigation" apparently are underway, we also believe that better communications with employees claiming injury could help to reduce tensions in this and other areas. Next, we discuss how this might occur.

"User friendly" information is needed

The report of the National Conference of State Legislatures emphasized the importance of all participants in the workers' compensation system understanding their rights and responsibilities through such instruments as pamphlets explaining the law in simple terms.⁷

We found that the Department of Human Resources Development does not publish sufficient information describing the claims process for state employees. State staff involved in the process seem to have little time for responding to information requests. As a result, injured state workers are faced with the chore of understanding a process that is confusing without inadequate information.

The Department of Labor and Industrial Relations issues two informational pieces on workers compensation. One is the *Workers' Compensation Handbook for Employers and Insurance Companies*, which outlines the law and the *employer's* basic obligations. The other is a brochure for employees (both public and private) called *Highlights of the Hawaii Workers' Compensation Law*, which outlines the law and the injured *employee's* basic obligations.

Neither of these publications provides state employees with a sufficient understanding of the claims process. For example, the employee's brochure, while clear and helpful on the subjects it discusses, does not fully explain denials pending investigation, estimate the length of time that various stages in the claims process may take, or detail the procedures for reopening a claim. In the absence of adequate information, at least one employee organization—the Hawaii State Teachers Association—has had to develop its own informational handbooks.

A more detailed brochure would be helpful. One example is the booklet entitled *Information on Unemployment Benefits and Applicant Identification Card*, published by the Department of Labor and Industrial Relations. The booklet thoroughly describes claimants' rights and

responsibilities and the claims process including details of benefits, eligibility, disqualifications, time lines, and reopening claims. It gives claimants a realistic perspective on what they will face in seeking unemployment benefits.

Managed care has potential

Medical issues in workers' compensation are complex. As in the general health care system, cost control mechanisms include limited provider panels, utilization review, managed care, preferred provider organizations, and case management. A central oversight agency could evaluate all of these options.

To give one example, "managed care" describes a systematic way of delivering and administering medical services. Its goal is to control medical costs and to ensure that injured workers receive necessary medical treatment. Because medical costs are of great concern in workers' compensation, many states have adopted managed care for both the public and private sector. This approach represents a departure from the traditional focus on medical fee schedules and it limits employees' choice of a physician.

Managed care includes such techniques as the following:

- use of preferred provider organizations or health maintenance organizations (typically, these consist of a network of medical care providers who treat injured workers according to specific guidelines)
- medical bill review
- utilization review
- centralized claims administration

In the past few years, at least 13 states have adopted various managed care techniques to control medical costs in workers' compensation.

There are advantages and disadvantages to a managed care approach. On the plus side, a managed care program with a network of medical providers may provide more efficient treatment and monitoring of recovery. When an employee seeks medical care from a mutually agreed upon physician from the provider network, this can reduce adversarial tension between employers and employees. Established guidelines and better communication facilitate employees' early return to work.

Critics of the managed care network approach contend that managed care limits employees' right to choose their medical provider. Managed care may be perceived as an employer effort to limit medical services for

injured workers. Furthermore, critics may argue that managed care is a recent innovation in workers' compensation and that it is too early to evaluate on its effect on cost control.

In Hawaii, managed care is being explored for the entire workers' compensation system, not only for the State as an employer. The State Workers' Compensation Division has taken part in these discussions. A fully centralized division with greater management and planning capacity could contribute even more to the dialogue.⁸

Recommendation

The Legislature should consider amending Chapter 26-5, HRS, the law establishing the Department of Human Resources Development, to assign responsibility for central oversight, coordination, and reporting for workers' compensation activities related to claims by state employees to that department. The department would be held accountable and would have full authority and responsibility for the following:

- a. Setting policies, goals, and objectives for the system.
- b. Managing workers' compensation claims on a centralized basis for all agencies in the executive, judicial, and legislative branches.
- c. Compiling and analyzing complete and accurate workers' compensation claims and expenditure information, and information on the costs of claims administration, for all state agencies in all three branches. This information must be in sufficient detail to facilitate policy making and identification of the State's workers' compensation liability. The department would also be responsible for reporting to the governor and the Legislature on the accomplishment and potential for improving the State's workers' compensation system.
- d. Integrating, coordinating, and monitoring workplace safety and return-to-work programs of state agencies.
- e. Evaluating the costs and benefits of innovative cost control strategies such as third-party claims administration and managed care, and examining other systems issues such as reserves.
- f. Developing a brochure that clearly and simply explains the entire claims process for all state employees. The brochure should include a description of the roles and responsibilities of employees, employing agencies, and claims managers.

Notes

Chapter 1

1. John D. Worrall and David Appel, "Some Benefit Issues in Workers' Compensation," in *Workers' Compensation Benefits: Adequacy, Equity, and Efficiency*, Worrall and Appel (eds.), ILR Press, Cornell University, 1985, p. 3.
2. National Conference of State Legislatures, *The State of Workers' Compensation*, Denver, Colorado, January 1994, p. 11.
3. Hawaii, Governor's Task Force on Workers' Compensation, *Report and Recommendations*, Honolulu, November 28, 1994, introductory letter.
4. Ibid.
5. Berkowitz and Berkowitz, "Challenges to Workers' Compensation: An Historical Analysis," in *Workers' Compensation Benefits: Adequacy, Equity, and Efficiency*, Worrall and Appel (eds.), pp. 161-62.
6. Lorraine H. Akiba, Director of Labor and Industrial Relations, and Wayne Metcalf, Insurance Commissioner, *Report to the 1996 Legislature on Act 234, Regular Session of 1995*, Honolulu, December 26, 1995.
7. Advanced Risk Management Techniques, Inc. (ARM Tech), *State of Hawaii Executive Branch, Workers' Compensation Program Study*, Laguna Hills, California, February 24, 1993.

Chapter 3

1. Connecticut, Department of Administrative Services Workers' Compensation Program, *Procedures Manual*, March 1994, p. 8.
2. Memorandum to All Department Heads from Governor George R. Ariyoshi, Subject: Settlement of Workers' Compensation Cases, February 22, 1985.
3. Testimony submitted by James H. Takushi, Director, Department of Human Resources Development, to the House Committee on Finance, January 25, 1995.

4. Advanced Risk Management Techniques, Inc. (ARM Tech), *State of Hawaii Executive Branch, Workers' Compensation Program Study*, Laguna Hills, California, February 24, 1993, p. 4.
5. Hawaii, The Auditor, *Financial Audit of the Hilo Medical Center*, Report No. 96-4, January 1996, p. 18.
6. See Lorraine H. Akiba, Director of Labor and Industrial Relations, and Wayne Metcalf, Insurance Commissioner, *Report to the 1996 Legislature on Act 234, Regular Session of 1995*, Honolulu, December 26, 1995.
7. National Conference of State Legislatures, *The State of Workers' Compensation*, Denver, Colorado, January 1994, p. 12.
8. See Akiba and Metcalf, *Report to the 1996 Legislature*.

Responses of the Affected Agencies

Comments on Agency Responses

We transmitted drafts of this report to the Department of Human Resources Development, the Department of Labor and Industrial Relations, and the Judiciary on January 10, 1996. A copy of the transmittal letter to the Department of Human Resources Development is included as Attachment 1. Similar letters were sent to the Department of Labor and Industrial Relations and the Judiciary. The responses of the Department of Human Resources Development, the Department of Labor and Industrial Relations, and the Judiciary are included as Attachments 2, 3, and 4, respectively.

The Department of Human Resources Development had numerous comments. The department is interested in centralizing the executive branch, but expressed concerns about handling all state cases due to the constitutional separation between the executive, legislative and judicial branches. The department noted the need for additional resources to accompany any additional duties. The department is investigating new integrated personnel, workers' compensation and payroll information systems.

The department expressed concern over the year and selection of the noncentralized departments for our review of claims management. We chose the most recent complete calendar year, 1994. Our selection of the four non-centralized agencies was based on their being named in the Concurrent Resolution that requested the study.

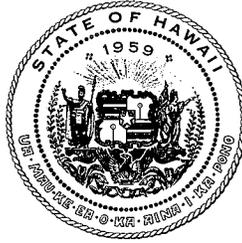
The Department of Labor and Industrial Relations generally agreed with our conclusions. It agreed that safety and prevention programs are key components to reducing workers' compensation costs, and that efficient case management contributes to cost savings. The department also made some comments on the workers' compensation law.

The Judiciary does not agree with the recommendation to centralize its workers' compensation program under the Department of Human Resources Development. Besides noting that it is a separate and autonomous branch of government, the Judiciary maintains that the effectiveness of its system argues for its system's continued independence.

All three agencies suggested some additional technical clarifications and corrections in our draft. We incorporated some of these in our report. Where we let the draft text stand, we conclude our evidence supports the draft text as circulated.

The response of the Department of Human Resources Development, numbering some 141 pages, was too long to include in its entirety. We have instead included only the department's point-by-point comments. The remainder consists of various data tables and excerpts from its Accident Information Reporting System procedures manual. The entire response is available for inspection at our office.

STATE OF HAWAII
OFFICE OF THE AUDITOR
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917



MARION M. HIGA
State Auditor

(808) 587-0800
FAX: (808) 587-0830

January 10, 1996

COPY

The Honorable James H. Takushi, Director
Department of Human Resources Development
Keelikolani Building
830 Punchbowl Street
Honolulu, Hawaii 96813

Dear Mr. Takushi:

Enclosed for your information are three copies, numbered 6 to 8 of our draft report, *Study of the Workers' Compensation Claims Process for State Employees*. We ask that you telephone us by Friday, January 12, 1996, on whether or not you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Friday, January 19, 1996.

The Department of Labor and Industrial Relations, Judiciary, Governor, and presiding officers of the two houses of the Legislature have also been provided copies of this draft report.

Since this report is not in final form and changes may be made to it, access to the report should be restricted to those assisting you in preparing your response. Public release of the report will be made solely by our office and only after the report is published in its final form.

Sincerely,

A handwritten signature in cursive script, appearing to read 'Marion M. Higa', with a small flourish at the end.

Marion M. Higa
State Auditor

Enclosures

BENJAMIN J. CAYETANO
GOVERNOR OF HAWAII



JAMES H. TAKUSHI
DIRECTOR

JAMES C. KIRCHHOFER
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF HUMAN RESOURCES DEVELOPMENT
830 PUNCHBOWL STREET
HONOLULU, HAWAII 96813-5081

January 19, 1996

RECEIVED

JAN 19 5 44 PM '96

OFFICE OF THE AUDITOR
STATE OF HAWAII

Ms. Marion M. Higa
State Auditor
Office of the Auditor
465 S. King Street, Room 500
Honolulu, Hawaii 96813

Dear Ms. Higa:

Thank you for the opportunity to review your draft report, *Study of the Workers' Compensation Claims Process for State Employees*. I feel it is through on-going reassessment and learned discussions that we are able to improve operations.

In this light, I am transmitting our response to your draft report. I feel that the scope of the study did try to address the enabling resolution which was to study our workers' compensation claims processing and make recommendations for improvement. The claims process is a very important part of our program but it is not the entire program and I am open to discussing refinements to the total workers' compensation system which includes proactive measures such as safety and morale issues.

We have reviewed the draft and have identified many statements which must be corrected or explained. We have also detected certain inferences to the effectiveness of our division operation, staff proficiency, and the structure of Hawaii's entire workers' compensation system which either are not correct or, uncorrected, would leave the public with a wrong impression. These areas also require our comment as claims management professionals, as dedicated public servants, and, as representing Hawaii's largest employer.

Our point-by-point responses are assembled in Attachment A. Supporting charts or other data are also enclosed.

We have some observations and comments to offer as professionals in the field of human resources. The thrust of the Workers' Compensation Division is to handle claims management in the most efficient and professional manner. We are trying to accomplish this mandate as best we are able to. Our staff is extremely dedicated and professional and I applaud their efforts to serve both the people of Hawaii, assist the claim management of injured employees and return them to productivity as soon as possible. It must be pointed out that our current staff caseload is 200 cases per case manager while the industry average, we understand, is about 135 cases.

Industry Trend & Cost

The Department of Labor & Industrial Relations (DLIR) reported that claims filed for all local industries have decreased from 1992 through 1994. As an employer, we continually strive for more efficiencies and reinforce effective workplace safety concepts through education. However, with diminished resources, we are only able to make incremental headway. Our Return to Work Priority Program (RTWPP) is a no-cost example made possible by dedicated human resource staffs from all departments and DHRD divisions. Although the effectiveness of the RTWPP was temporarily compromised due to available positions being “frozen” by the recent Reduction-in-Force, we are confident that the program will regain momentum within the departments.

According to DLIR statistics, the State of Hawaii, self insured for its workers’ compensation program, has the lowest average cost per claim when compared to four other local sectors. We think this is a positive sign, albeit a small one, that we are doing our best to lower workers’ compensation costs.

State of Hawaii (DHRD)	\$2373 per claim
Insured companies	\$4229 per claim
Self-Insured, private industry	\$3457 per claim
City & County of Honolulu	\$3222 per claim
Construction Industry	\$6384 per claim

Because our case load is high, I have temporarily reassigned professional staff from several divisions to assist the Workers’ Compensation claims adjusters. Even this temporary staffing shift is not enough to shorten professional claims processing. We are going one step further, even in this mode of budget reductions. I have administratively moved our State Safety Branch, whose emphasis is on safety prevention, education and agency consultation, to our Workers’ Compensation Division. This will facilitate proactive safety programs and help reduce the workers’ compensation claims being filed. Our safety program has been very proactive in safety awareness and education, utilizing low- or no-cost means. Unfortunately, it has been impacted by the recent elimination of the unexpended balance previously held in our in-service training fund.

Centralization

If we are to – and we want to – centralize the executive branch, we would need about 30 additional experienced staff and necessary computers on which to manage and process the additional case work. This still means that we would be working with a partially-computerized database without historical data, and which could not carry us through the next few years. To capture the data this study said was necessary (now stored in files transferred over to us by the departments whose claims we assumed) would take 253 data entry clerks working full time for one year to complete the previous 10 years of claims information. This represents a one-time cost of over \$5.3 million just for temporary personnel services and does not take into account leased computers or space.

If it is the study’s suggestion to have DHRD handle all state workers’ compensation cases, we have some concerns because of the constitutional separation between executive, legislative and judicial branches. We have, however, assisted the legislative branch in an advisory or technical level and we will gladly do so if called upon in the future. It may be more economical and more efficient if we were more directly involved in assisting the legislative branch in the handling of its claims.

January 19, 1996

Page 3

Automation

As your report noted, the State has several different data programs, written over the decades for different purposes, that do not integrate to come up with good management information and tools. We have investigated computer and software technologies in depth and have established excellent working relationships with many of our sister state data entities. I feel that we, with the technical expertise of my automation staff, are on the doorstep of an integrated Human Resource Management System that would be able to finally integrate personnel, payroll and other data. This is a wise long-term investment that should be considered even at a time when funds are tight because we will benefit from the operating efficiencies and management information it will provide. It must also be mentioned that in the year 2000, many of the state's major computer applications will have to be replaced or modified to accommodate the new millennium.

Emphasis on Safety

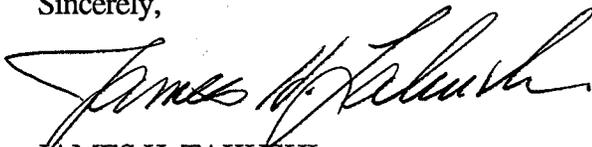
In your study, we have been compared to other entities with different workers' compensation systems or with better safety programs. I began our safety program in early 1970s and am proud to say that our five staff members serving 24,000 civil service employees, do a tremendous job. One measure, in my mind, is to look at the state's cost per claim cost. But I am not saying this is the best we can do — I agree with you that we can do more and do it better. But we need resources. The Outrigger, I understand, has a safety staff of five for 2800 employees. So if we are really interested in running a safer and less costly state workers' compensation program, we have to creatively look at accident prevention and better work force relations programs as the means to prevent claims from occurring.

Changes in Hawaii's Workers' Compensation Industry

Granted, we are Hawaii's largest single employer. We do follow established laws relating to workers' compensation as best we can given the painful limitations we have on our resources. If it is the legislature's intent in looking to reform Hawaii's workers' compensation system, then, I respectfully request that this department be included in working on such reform measures. The Department of Human Resources Development has a real stake in helping to reform such a critical industry, our experience and expertise have not been utilized as it should be. Just as public employee unions are involved, we too should be invited to participate.

Thank you for the opportunity to respond to the study. We are both partners in making government operations as fair, equitable and cost efficient as possible. I respect and understand your role. Over the years, I have been impressed by the progress and impact you and your staff have made to make state government more efficient.

Sincerely,



JAMES H. TAKUSHI
DIRECTOR

Enclosure

STUDY CITATION OR INFERENCE

DHRD RESPONSE OR CLARIFICATION

Page 1, paragraph 1

Like other employers, Hawaii State Government is responsible for providing workers' compensation benefits to its employees who are injured on the job.

Benefits are not limited to on-the-job injuries but include disease proximately caused by or resulting from the nature of the employment.

Page 1, paragraph 2

Expenditures have exceeded the initial appropriations. Transfers from other programs, and most recently an emergency appropriation, have been used to make up the shortfall.

DHRD knew that expenditures would exceed the appropriations and notified the prior administration of this. However, because there was a budget proviso which allowed for the transfer of funds from other departments, the administration didn't feel that it was necessary to increase the allocation but rather to use existing, restricted funds.

Page 1, paragraph 7

In exchange for giving up their right to tort actions, employees are to get swift and certain payment from the workers' compensation program without having to demonstrate that the employer was at fault.

This is an incomplete statement which leaves out an important component of the original trade-offs. Employers also gave up the right to deny employees' claims on the basis that the employee was at fault.

Page 2, paragraph 3

Chapter 386 is a "no fault" law. It grants certain rights and remedies to employees and their dependents in the event of a work injury regardless of whether the employer is at fault.

The employee doesn't have to prove the employer was at fault in order to receive benefits nor can the employer deny benefits on the basis that the employee was at fault.

Page 2, paragraph 4

Permanent partial disability benefits cover wage loss and disfigurement, vocational rehabilitation services are available in cases of permanent injury, death benefits give weekly benefits to the surviving spouse and children.

These statements are only partially correct and over simplify who may receive these benefits. For example: not all employees receive vocational rehabilitation services in cases of permanent injury.

Page 3, paragraph 2

The fund helps compensate workers who do not receive prompt and proper workers' compensation from their employer.

This statement is not accurate, and therefore should either be clarified or deleted.

Page 5, paragraph 3

The 1994 report of the Governor's task force made recommendations for improving Hawaii's workers' compensation program as a whole and the State's self-insured program.

It is unclear as to whether the task force actually made recommendations for the State's self-insured program.

Page 6, paragraph 1

Objectives of the Study

We feel that the objectives stated were not consistent with resolution.

STUDY CITATION OR INFERENCE

DHRD RESPONSE OR CLARIFICATION

Page 7, paragraph 2

They examined a systematic sample of workers' compensation claims by State employees during calendar year 1994, from all centralized and selected non-centralized agencies.

Questions: 1) Why was calendar year 1994 selected? 2) Why were only selected non-centralized agencies used? 3) What is the importance of comparing the rates at which claims were being accepted, denied, and denied pending investigation? 4) Why weren't the same comparisons made with other large insurers and/or third party administrators? 5) Whose records and what statistical data were examined?

Page 11, paragraph 5

They investigate the basic circumstances of the injury and report them to the assigned case manager at the division. The employing agency supplies data on wages and sick and vacation leave to the case manager when replacing lost wages to an employee.

Most employing agencies do not investigate the basic circumstances of the injury. Most agencies only report the details of a claimed event primarily based upon information provided by the employee. Some agencies complete a supervisor's Accident Report, created by DHRD's Safety Branch, to identify why an accident has occurred and what an agency can do to prevent it from future similar occurrences. Although employing agencies do supply wage data, primarily on the WC-1, they do not provide the SWCD with sick and vacation leave data as this isn't necessary to the calculation of TTD or TPD benefits.

Page 12, paragraph 4

The DAGS prepares vouchers for workers' compensation benefits payments.

This is an inaccurate statement. Not all benefits are paid through the summary warrant voucher system.

Page 13, Exhibit 2.1 Flow Chart Constructed by Auditor's Staff

There are a number of inaccuracies in the flow chart, a gross oversimplification of the process, and an appearance that this abbreviated flow chart only applies to how Claims are handled by the State of Hawaii. They skipped all of the steps taken before a Claim is assigned to a case manager. It looks like a case manager investigates all Claims assigned to him or her. This is absolutely not the case. By their own statement, the SWCD investigated only 17% out of the 270 Claims reviewed which had been filed in 1994. (See page 24.) The number of Claims sampled was only 14% of the new Claims filed in 1994. (See page 4.)

Page 14, paragraph 3

The employing agency or it's representative sends the WC-1 to the Disability Compensation Division of the Labor Department within seven (7) days of receiving notice of injury.

The employing agency sends the WC-1 to SWCD where it is numbered (DLIR/DCD case number). This document is then distributed to the Disability Compensation Division, employing agency, injured employee, and AIRS with a copy retained for the file.

STUDY CITATION OR INFERENCE

DHRD RESPONSE OR CLARIFICATION

Page 15, paragraph 2

For example, to investigate medical claims, employers can request a medical evaluation by a specialist. The evaluation is used in determining whether the claim is compensable and, if so, the amount.

This statement is partially incorrect. While the reasons for requesting medical evaluations may vary, the selected physician doesn't determine "amounts".

Page 15, paragraph 6

If an injured employee has received considerable medical treatment and still cannot return to work, a settlement with the State is made. The settlement usually terminates all employment and future compensation rights of the employee for a one-time cash payment.

This is inaccurate. The amount and/or duration of medical treatment received by an injured employee does not dictate whether or not a settlement is made. Furthermore, the majority of negotiated settlements do not include a waiver of reemployment rights or of future rights to receive additional compensation. There are a number of positive reasons for settling claims:

- 1) the employee receives the benefits in a lump sum which isn't always the case when we are paying pursuant to a decision;
- 2) the employee receives the benefits faster as they don't have to wait for the DLIR to schedule a hearing;
- 3) it saves everyone time.

Page 15, paragraph 7

All settlements with State employees are approved by the director of the DHRD before submittal to the DLIR for approval.

This is not an accurate statement. The director of the DHRD, or his designee, approves all settlements only for those departments within the executive branch of government.

Page 24, paragraph 1

We sampled claims filed in calendar year 1994 from two groups: all centralized agencies and four non-centralized agencies (DOE-neighbor islands, Judiciary, Research Corp. of the University of Ha'waii, and the UH). Of these two groups, we compared the rate of claims initially accepted, denied, and denied pending investigation. We found that the four non-centralized agencies as a group accepted a slightly higher proportion of claims as compensable than did the centralized SWCD. The non-centralized groups also denied claims "pending investigation" less often than the centralized division.

First of all, the source of the data was not identified. Also, it is unclear as to why 1994 was chosen to extract this data. The sample appears to be incomplete as it represents approximately 14% based on the information on page 4, paragraph 1. In identifying non-centralized agencies, they failed to include Department of Health, Department of Human Services, and Department of Defense, which would account for a large number of claims handled by non-centralized agencies. It did not elaborate on the number of cases voluntarily accepted once the investigation was completed or the number of cases that actually went for a hearing to determine compensability. It also failed to document the conclusive results. Would the omitted data have an impact on the statistics which were presented in Exhibit 3.2?

STUDY CITATION OR INFERENCE

DHRD RESPONSE OR CLARIFICATION

Page 24, paragraph 3

Our financial audit of Hilo Medical Center revealed a case of particularly unassertive claims management in a non-centralized agency. We found that this state-run facility pays approximately 1.3 million a year in workers' compensation claims costs. But center does not monitor the status of open claims.

Specifically when was the financial audit conducted? It has been our experience that Hilo Medical Center currently employs a Personnel Technician for the purpose of administering benefits to injured employees as well as maintaining and managing claims. Although our experience in dealing with this Personnel Technician has been limited to working with him in an advisory capacity, we are aware of cases in which he has successfully defended the State's position at administrative hearings at DLIR/DCCD.

Page 26, paragraph 3

Formal training for claims managers in the State Workers' Compensation Division varies and appears somewhat limited compared for example to what is offered to claims adjusters in Oregon.

It is unclear as to what kind of training is being offered in Oregon. Clarification is needed in addressing whenever training would apply to all adjusters in Oregon (public, private, and self-insureds)? Who provides this formal training and at what cost? Formal training is provided to new employees at SWCD by the management staff utilizing a training manual purchased from Adjusting Services (copies of this manual was provided for the auditors' review). In addition to the initial formal session, training is provided on an ongoing bases. (See Exhibit A.) Due to the State's budget restrictions, we could not afford to send our entire staff to conferences and seminars which charge a tuition fee to attend. As a result to minimize the cost we allow a few employees to attend who are asked to present the training material to the staff. We also conduct in-house training at no cost to the State.

Page 26, paragraph 4

We also found that neither the Division nor the non-centralized agencies monitor claims for fraud formally and systematically. Efforts to control costs are weakened when a system goes unmonitored. Furthermore, this leaves the extent of fraud open to speculation and rumor.

Fraud as defined under Chapter 386-98, HRS, is an act to willfully make a false statement or representation for the purpose of directly obtaining any compensation or payment or for the purpose of avoiding on behalf of employer or carrier any compensation or payment under this chapter. Based on this statement, there appears to be an assumption that there is a large number of cases involving fraud. When in fact the actual cases identified are not substantial. This statement is also inconsistent with the statement made on page 24, paragraph 1 in which reference is made to a larger number of cases being investigated. One of the reasons investigations are conducted is to either identify or prevent fraud from occurring.

Page 26

First, information and analysis on all claims against the State is insufficient. . . . Second, information for managing the State Workers' Compensation Division is inadequate due to the limitation in the areas of case status reports, case tracking, and case summaries.

The information and analysis of all claims against the State is an issue of integration of information among all government agencies - Judiciary, Executive, and Legislative. Three issues become readily apparent. First, if it is technically feasible to integrate all statewide workers' compensation data given that each database was developed inde-

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Page 27 Lack of information underlines ability to meet accounting standards

...In order to comply with GASB 10, the State needs to be able to identify all of its workers' compensation claims and expenditures for those claims...

...However, the necessary information for actuarial estimates is not readily available. The department has found no basic information on claims and payments that is centralized in any of the state databases...

pendently with its own specific definitions. Secondly, whether it is within the legal scope of responsibility of the SWCD is a question that needs to be addressed. Further, if the SWCD is given the responsibility as the Auditor suggests, then the issue of confidentiality of information among the different branches of government is brought out.

The issue of limited management information capability will be addressed by the new HRMS. Granted that the HRMS software that was procured, PeopleSoft, does not have a "Workers Compensation" module. However, the existing Comp2000 pc software provides a framework in which functions can be developed and replicated with the software development tools provided with the PeopleSoft software. This includes case tracking, status reports, and summaries. DHRD's initial estimate for the development of the WC module in PeopleSoft following the functionality of Comp2000 was approximately \$400,000. This includes the ad hoc and standard reporting capability functions that the Auditors make reference to. Comp2000 is not the "end all" product, since the SWCD requires other functions beyond the capabilities of the software. Functions such as image processing should be applied to the wc paper intensive process. The HRMS is designed on the basis that users from each agency would access and maintain their WC data in a central repository. Each agency would have their own ad hoc and standards reporting tools for their data to provide them utility and incentive in maintaining accurate data. The SWCD would have reporting tools to conduct statewide analysis.

The primary problem with compliance is that the claims management function is de-centralized among and within each government entity: executive; judicial; legislative; and quasi-governmental agencies (i.e.. OHA). The IBNR (incurred-but-not reported) portion of the GASB 10 requirement would be impossible to formulate without all files and incoming mail in one location.

Stating that a single reserve database would solve this problem is a gross over-simplification of the problem. Although portions of the required information is located in numerous databases, each data system was designed for specific end-users. These systems, such as FAMIS, OFIS, Payroll, AIRS, and Comp2000, were designed for exclusive tasks. Compounding the problem is the fact that these systems were design during different technology periods over a 20 year period. They are not readily compatible. As each discipline strives to optimize the potential of their separate systems, parallel data requirements result in a duplication of effort.

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Page 28 para 3-6

Incomplete and inaccurate information is scattered among databases

...Three major databases contain workers' compensation claim information...

...this database does not contain sufficient detail on individual claims payments...

...DHRD has two databases that track workers' compensation claims information, the Comp2000 database and the Accident Information Reporting System (AIRS) database...

...Ideally, the Department of Accounting and General Services says, it need access to an automated system that includes each state employee's name, social security number, and workers' compensation claim number...

The issue of a shared single human resource data base which satisfies the data requirements of diverse end-users is addressed in the Department's HRMS project. The DHRD is aware of the GASB 10 requirement, but not to the detail that will be required for application specifications. This will be done in conjunction with the development of the integrated personnel/payroll system by DAGS, DHRD, and any agency involved in GASB 10. DHRD is aware of the shortcomings of the payroll system and its ability to track payments to individuals on WC. The new integrated system will be designed to address these issues.

As stated in the preceding comment, each database was design for a specific task. AIRS was never intended to be a workers' compensation application. It was designed as a safety compliance/management tool. Some of the information collected were also relevant to the workers' compensation system and was offered to the departments as an incentive to participate in the safety application. AIRS was never intended to be the State's primary workers' compensation claims management tool.

Comp2000, however, was purchased with the expressed intent of facilitating the processing of workers' compensation claims. It offered custom invoice processing capabilities as well as a host of case management tools and reports. Utilization of the software's potential, unfortunately, is limited by:

- 1) Incompatible State systems
- 2) Scarce human resources
- 3) De-centralized claims management

A database is only as good as the information which it can accurately capture. We can not interface with the State's Payroll, FAMIS, or OFIS systems. This greatly limits the information that can be captured without obligating considerable data entry resources. Sparse resources which SWCD has primarily directed toward assisting with the delivery of benefits. For example, without an existing electronic Leave Accounting system or the ability to interface with the payroll system, the ability to produce a 10 day statutory report through Comp2000 is impossible.

SWCD has always utilized Comp2000 as a management and claims processing tool. The Division employs Comp2000 ad hoc reports as templates to produce daily custom relational data reports which address the diverse daily management requirements of the office and to track statutory compliance areas which have been identified as

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core functions of the Division. Additionally, the claims' managers utilize Comp2000 as a benefits tracking and review cue by printing custom reports. The Return-to-Work nurse employs the Vocational Rehabilitation data file in Comp2000 to track the rehab status of the Division's claimants. Finally, the large majority of the Cost Containment Section's work-hours is consumed by data entry requirements of the DAGS FAMIS system. The Section employs Comp2000 to generate and maintain the volumes of documents which the State's accounting system requires.

At the existing staff level, increasing the utilization of Comp2000's abilities would put a detrimental strain on the Division's primary function of delivering benefits. Additional limitations on the utilization of Comp2000 is further perpetuated by the fact that SWCD only possesses the resources to manage only a portion of the State's total case load. Because the Division can barely support the existing utilization level, the data entry requirements to maintain a database for the entire State is prohibitive.

The Auditor does not realize that all of the wc related databases were not developed in any unified fashion, neither were they intended to be. For the past 10 to 20 years, the development of applications were done independently without regard to the cross-functional impacts they had. Traditionally, the State developed application systems for each government function on an as needed basis. For example, payroll (over 20+ years ago) was developed to basically pay employees - not to track wc claims. WC was developed to manage wc claims - not to track payroll expenditures. AIRS was developed to manage accidents - not to track payroll expenditures or wc claims. The resulting effect from these independent applications is application "silos". Information is not shared, redundant information is maintained, and integration of the data is virtually non-existent. Therefore, the data is not incomplete or inaccurate, from the perspective of what each function requires. When you attempt to integrate the data to form generalized reports, then the deficiencies and inaccuracies become apparent. The data in each application was not intended or designed for integration, therefore some elements may be incomplete to provide a comprehensive report. The HRMS will replace both the AIRS and Comp2000 databases. Much of the information in the AIRS is replicated in the Comp2000 database and vice-versa. However, it should be noted that neither one can replace the other - both have strong shortcomings.. Comp2000 does not have support from its vendor anymore. Documentation is poor since it has been customized to the point of its inability to receive updates and newer releases. The Auditor, however, recommends that

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Page 29, paragraph 4

A pilot reporting requirement begun in 1994 was discontinued because the supervisors' own caseload left them with little time to review the reports.

This is not completely accurate. We dispensed with reporting requirements at the request of our case managers. Their workload was so overwhelming that it was an issue of priorities. Our primary purpose is, and always has been, to ensure the timely payment of benefit to or on behalf of an injured State worker.

Pages 29 through 30

State Workers' Compensation Division lacks adequate internal information

...The State Workers' Compensation Division does not develop all of the information necessary to manage its program...

...Without comprehensive, periodic claim reports, the division lacks necessary information to formulate management strategy...

...Neither of the two systems track case activity against all of the time frames required by law...

Given the Division's history of deficiencies in staffing and equipment, SWCD's attention has been centered on improving the timely delivery of benefits due to our injured workers' under HRS 386. The Division's electronic information capabilities have, therefore, been concentrated on facilitating mechanical processing functions. These functions are:

- 1) The notification of injury and processing of DLIR's WC-1.
- 2) The payment of benefits due to claimants and providers.

SWCD agree's with the Auditor's assessment that the potential management tools which could be implemented utilizing Comp2000 are untapped. For example, although Comp2000 has available features for a potential reserving

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system, without the ability to exchange information between the State's Leave Accounting System, FAMIS, and Payroll systems, the resources required to maintain the reserve information are prohibitive.

SWCD's present and future energies, however, should be centered on using the framework of Comp2000 and integrating these features into the HRMS application and processes.

The HRMS project is attempting to re-engineer the entire human resource information processes and procedures. The project aspires to provide a single relational database which satisfies the State's diverse end-users (i.e. Payroll, Safety, DAGS Risk Management etc).

As one of the processes explored by the HRMS studies, triggers based on workers' compensation statutory reporting, filing, and payment requirements, have been identified and are planned to be assembled into future design specifications.

The Legislative Auditor did not contact anyone from the DHRD's data processing staff regarding the development of the Human Resource Management System (HRMS) and other efforts to processing of workers' compensation. The Workers' Compensation (WC) system has been identified as one of the five core areas for automation by DHRD and is priority No. 2 for development under the new Human Resource Management System.

The HRMS project undertook a nine-month process documentation and reengineering of five core DHRD functional areas – Position Management, Personnel Actions, Workers' Compensation, Leave Accounting, and Recruitment. The resulting information will be used in the development of the new HRMS system currently awaiting the Governor and B&F's approval for RFP release. Once the RFP is awarded, the first priority of applications to be developed under the HRMS is the Position Management and Personnel Action modules, which form the basis on which all other applications will be built.

It should be noted that since the HRMS project was initiated in 1993, the Department of Accounting and General Services has pursued an integrated approach with DHRD on a new personnel/payroll system. The integration with payroll processing will enable the State to address some of the interjurisdictional issues that the Auditor has brought out as well as other issues not specific to workers' compensation. With appropriate funding, DAGS and DHRD believe that we can have an operational system HRMS within a short timeframe.

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Page 30, paragraph 1 (last sentence)

The Administrator simply expects her staff to be professionals and meet their own deadlines.

It should be stated that this is a requirement of the job to meet all statutory obligations under Chapter 386, HRS, and related rules and regulations.

Page 30, paragraph 2

However, we found that Oregon monitors the status of its claims against statutory and other time frames.

It is unclear as to the procedure or mechanisms that Oregon uses in monitoring the status of its claims to ensure that statutory and other timeframes are met. However, SWCD case managers utilize a diary system which helps them to identify specific dates for case review, enabling them to meet statutory and other timeframes.

Page 30, paragraph 3

Claims filed do not include an overall summary of claims management activity. Summaries should list date of occurrence of the accident, date claim was filed, statutory deadlines, date of first payment, type of payment, amount paid, listing of forms filed, hearing notices, decisions, and settlements.

It is unclear as to what this statement was based upon when files were not reviewed as part of the audit. It should be noted that file documentation is an integral part of case management. In addition, all payment types and amounts are identified, logged, and totalled. Statutory deadlines are not just documented in files but are also monitored by a calendar and computer diary system. (Copies of all file forms were provided to the auditors for their review.)

Page 30, paragraph 4

Maintaining a summary listing/chronology on either the computer or the hard copy file (or both). A summary also serves as an index to identify documents in each file. Without this control it is difficult to keep track of file contents. A consistent listing procedure would allow other staff to determine status of any case at any point in time; for example, if the case manager is ill, changes jobs or retires.

As stated previously, it is unclear as to the source of this information as a file review was not a part of this audit. However, the case managers are required to document each of the files and, as previously stated, to identify the payment type and the amount which is logged and totalled. Status of a claim can be determined by reviewing current documentation in file.

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Page 32, Paragraph 3

(Another paragraph needs to be inserted between Paragraphs 3 and 4.)

The October 1994 directive also required the department to work in partnership with other departments to reduce the frequency of work related injuries by providing or arranging for safety prevention and jointly providing for work inspections.

The committee which developed the Return to Work Priority Program Procedures was formed in November, 1993. It included from the Department of Human Resources Development representatives from the divisions of Recruitment and Examinations, Classification and Certification, Labor Relations, State Workers' Compensation, Director's Office and Department Personnel Officers or their designees from the Departments of Health, Human Services, Accounting and General Services, Labor and Industrial Relations, Education, and Human Resources Development. After 14 months of committee work, a meeting of all executive branch personnel officers, and consultation with the Hawaii Fire Fighters Association, Hawaii Government Employees Association, and United Public Workers (we also provided a copy to Hawaii State Teachers Association), the Return to Work Priority Program Procedures were finalized and issued on December 20, 1994. It was later revised on March 10, 1995 with consensus from the Department of Labor & Industrial Relations Disability Compensation Division.

Page 32, Paragraph 4

Since the April 1994 directive, the SWCD has conducted workshops with all executive agencies and has written an informational brochure explaining the return-to-work program.

The committee has continued to meet as needed to evaluate the implementation of the program. However, the division's Return-to-Work Unit consists of one registered nurse who primarily assists centralized agencies with individual return-to-work cases. At the time of our study, this nurse was spending more time as a medical consultant to the division's case management staff. The nurse was not assisting the non-centralized agencies and had no information on their return-to-work programs.

Page 32, Paragraph 5

However, the division's Return-to-Work unit consists of one registered nurse who primarily assists centralized agencies with individual return-to-work cases. At the time of our study, this nurse was spending more time as a medical consultant to the division's case management staff. The nurse was not assisting the non-centralized agencies and had no information on their return to work programs.

At the time of the audit which occurred during the state-wide Reduction-in-Force, the amount of time spent on the Return-to-Work program was limited because of the Reduction-in-Force (between August 1 and October 31, 1995) contained provisions in its guidelines that gave placement of RIF employees higher priority over placement of injured employees to positions. The primary function of the nurse is medical management. The nurse is available to all agencies by phone or present at return-to-work meetings with the agencies. The nurse collects information on a quarterly basis from

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Page 32, Paragraph 6

Also, the division is not monitoring the progress of the return-to-work programs at the centralized agencies by gathering statistics on the number of placements by agencies. The division has no plans to report statistics of the return-to-work program. Program documentation does not emphasize controlling costs.

non-centralized agencies on their return-to-work programs. For centralized agencies the nurse coordinates with personnel offices regarding injured employees who are ready for the return-to-work program.

The nurse is monitoring the progress of the return-to-work cases at the centralized agencies by gathering statistics on the number of placements by agencies. Statistics are being collected to evaluate the program. The purpose of the return-to-work program is to assist injured employees to return to work; a by-product of this program should be a reduction in overall workers' compensation costs. The literature reviewed by the auditor's staff are operational and procedural manuals.

Page 32, Paragraph 7

State agencies have varying levels of involvement in return-to-work. Some agencies, like the Department of Education, have already developed policies and procedures. At the education department, this reportedly has resulted in at least nine injured employees being assigned to light duty assignments in the past year. At the Dept. of Accounting and General Services, as many as six employees reportedly have been on light duty work assignments at one time.

These DOE policies and procedures referred to are the Return to Work Priority Procedures recently developed in December of 1994. Our monitoring of the RTWPP and injured employee cases show that for Oahu some employees returned to volunteer work; six were assigned to light duty in the past year.

Page 33, Paragraph 2

As a contrary example, the Hilo Medical Center has problems in workplace return-to-work. ... Our audit report noted that the medical injuries. center should investigate the cause of each injury and ensure that future injuries can be prevented, and that the center should work with injured workers to rehabilitate them and get them back on the job as quickly as possible.

This is not a fair statement. In our on-going support and evaluation, we know that HMC is concerned about workers' compensation and related costs. However, the facility has very limited staff resources assigned to workers' compensation due to other facility priorities. We are and have been providing HMC additional return to work and safety support even despite our high staff work load. We are informed that the neighbor island facilities of the Division of Community Hospitals received the RTWPP information by the last quarter of calendar 1995 so their programs may not have been underway when the audit occurred. They should now be underway.

Page 34, paragraph 3

Moving toward a completely centralized approach can best be accomplished by amending Chapter 386, HRS, to establish a firm foundation for the program.

If statutory changes are required, then Chapter 26-5, HRS, should be amended.

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Page 35, paragraph 5

The need for timely, complete, and accurate data cannot be overemphasized. This information must be collected according to a prescribed format not only for the benefit of management and planning, but also to enable the State to fully comply with national accounting standards.

The department initiated attempts to collect accident and illness data prior to 1980 as a requirement to meet OSHA record keeping rules and as a means to obtain timely information to identify accident trends. Each department provides monthly, quarterly, and annual reports of their accident and injury profile so that timely decisions can be made to develop strategies to mitigate accident causes (see attached reports). As to government standards, this report, the Accident Information and Reporting System (AIRS), can be used to complete the OSHA 200. AIRS was not designed to meet other requirements. See participation by the Accounting and General Services regarding the development of AIRS and the purpose of AIRS.

AIRS data is maintained in calendar format to assist agencies in meeting OSHA and DLIR (Disability Compensation Division) reporting requirements. It is not designed to report on a fiscal year basis. When data is requested in a fiscal year format, there are difficulties and problems. For example, AIRS will treat data paid on March 1 and October 1 as payments in that calendar year. It would not separate the March payment into one fiscal year and October payment into the next fiscal year.

What is accuracy? What does "as of December 31, 1995" mean? It means that whatever was in the system at that time is reported. For instance, medical bills incurred in December and paid in February is reflected back to the previous year, so the "as of December 31, 1995" close-out report would no longer be accurate. Similarly, all vouchers in transit that don't meet cut off deadlines would revert back to the previous year. Why? Workers' Compensation requirements dictate that cost incurred in a calendar year must be recorded for that year. Therefore, the "as of" data for the year end may not be finite.

For planning purposes, year after year, the system repeats itself. AIRS is a management information system for identifying accident trends and injury pooling on both statewide and agency basis so that corrective strategies and corrective actions can be taken to eliminate or mitigate the cause of injuries.

Page 36, paragraph 4 and 5

The Armtech study did not recommend using third party administrators in the State for several reasons.

In commenting on the Armtech statement regarding the use of a third party administrator, it should be noted that they in fact consulted with one of the largest third party administrators in the state of Hawaii prior to concluding with this recommendation.

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Page 36, Paragraph 1

The law should solidify the department's existing mission of assisting agencies with safety and return-to-work activities. For return-to-work, the department would have the responsibility and authority to oversee and monitor agencies' efforts to establish light duty positions, modify work environments to accommodate partially disabled employees, and accept qualified employees from other agencies when that agency cannot accommodate its injured employees.

We disagree. The auditor's implication is that the RTWPP should be centralized under DHRD. A successful RTWPP entails knowledge of the department's recruitment, placement, classification, labor relations (and other subject areas)- expertise that is now at the department level. Because the RTWPP has been in operation only a short time, we have not contemplated centralization especially since it seems to be going well. We are therefore unable to estimate the additional staffing requirements centralization will require. Under current economic times, we feel the program should operate as it is now.

Page 36, paragraph 6

A principal advantage of using a third party administrator is standardization of service. This may also be cost-effective. A recent study for a private sector firm found that the quality of adjusting services contributes to reducing of average cost per claim. However, the cost of hiring an outside company involves not only the contractual fees but also the incidental expenses necessary to administer the contract.

It is not clear as to the statistical data or the source of the information used in formulating this statement. Third party administrators do not guarantee a standardized handling of case. There is also no data that we are aware of which supports the statement referring to a reduction in the average cost of claims.

Page 38, paragraph 3

The DHRD biennially requests a legislative appropriation in accordance with a budget of scheduled workers' compensation claim settlements.

Our request for the workers' compensation appropriation is not based on settlements but rather upon historical data on total general funded workers' compensation expenditures and other trend factors.

Page 38, paragraph 7

However, we found that the Claims process for State employees is often perceived as frustrating, inconsistent, and unfair. There are charges of slowness in determining compensability, lack of readily available written information about the process, and a reluctance to provide information even upon request.

This report does not identify the percentage of employees filing claims who are making these allegations. From January 1, 1993 through December 31, 1995, the SWCD received 5,498 claims. Of those newly filed claims, 617 were investigated. This comes out to our investigating an average of 11% per year. We aren't saying that we are perfect or that we are meeting the needs of all employees filing claims, or that we don't need to make future improvement in the way we are managing claims. However, we do meet the needs of more than 80% of employees whose claims we handle. That is an extraordinary accomplishment in light of less than adequate staffing.

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Page 39, paragraph 6

Critics of "denied pending investigation" also suggest that Claims managers at the State Workers' Compensation Division may not fully understand that Chapter 386, Hawaii Revised Statutes, the workers' compensation law, contains a presumption that each claim is compensable. One critic says that nothing in the law explicitly authorizes "denied pending investigation."

Utilizing the words "denied pending investigation" is not based upon the State's perspective. 12-10-73(a), Subchapter 3, Administration provides that "When an employer files a report of industrial injury denying compensability or indicating compensability is not accepted for reasons such as pending investigation, the director shall review the report". Amendments to Chapter 10, Title 12 of the Administration Rules related to workers' compensation became law effective December 8, 1994. A feature of the amendment to 12-10-73(a) was to delete the wording "pending investigation". This fact was pointed out to the auditors on numerous occasions. We see nothing in this report which indicates whether or not other self-insured, self-administered employers, third party administrators, or insurance carriers used the same language in controverting claims. To suggest that we may have changed our basis for denying claims because of the State Auditor's Study is absurd. The change in wording began even before the amendment became effective. It began under the prior administration after a number of discussions with certain union officials.

Page 40, paragraph 1

While efforts to resolve the issue of "denied pending investigation" are apparently underway, we also believe that better communications with employees claiming injury could help to reduce tensions in this and other areas.

"Denied pending investigation" is a non-issue. This was deleted from the administrative rules effective December 8, 1994. While we agree that open communication with injured employees may reduce adversity, it may not always be possible as many of the injured employees may already be represented even before we receive their claims.

Page 40, paragraph 3

We found that the State does not provide efficient information describing the claims process for State employees.

We do provide an insert with the initial letter which explains the process and the employees' entitlement. (A copy was provided to the auditor for their review and record.)

Page 40, paragraph 5

For example, the employees' brochure, while clear and helpful on the subjects it discusses, does not fully explain denials pending investigation, estimate the length of time that various stages in the claims process may take, or detail procedures for reopening claims.

This statement refers to a DLIR publication. It should be noted, that investigations, time frames involving various stages of a claims process, or detailed procedures for reopening claims cannot be generalized as it would depend on the merit of each case and therefore vary accordingly.

BENJAMIN J. CAYETANO
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January 16, 1996

RECEIVED

JAN 17 10 48 AM '96

OFC. OF THE AUDITOR
STATE OF HAWAII

Ms. Marian Higa
Legislative Auditor
Office of the Auditor
465 South King Street, Room 500
Honolulu, Hawaii 96813

Dear Ms. Higa:

Thank you for the advanced draft copy of the Study of the Workers' Compensation Claims Process for State Employees. I commend your staff for the quality of the report as well as their professionalism in the conduct of this study.

We do have the following minor comments which I believe will more accurately portray the workers' compensation law:

- Page 2 Relating to categories of benefits: Specifically "permanent partial disability benefits" are not "wage loss" and can be more accurately be described just as "compensation due to permanent loss of some bodily function". "Disfigurement" appears to be redundant as it is described two bullets below.
- Page 3 Relating to Special Compensation Fund: Two other significant categories of payments are "benefit adjustments for permanently and totally disabled workers and delinquent employer payments."
- Page 10 Paragraph 4: The department has not contracted hearings officers to conduct workers' compensation administrative hearings. We contract for TDI and PHC complaint hearings.

I would also like to convey my concurrence with your assessment that 1) upon availability of funds, the Disability Compensation Information System needs to be improved and enhanced, 2) safety and prevention are key components to reducing workers' compensation costs, 3) efficient case management also contributes to cost savings, 4) information to claimants and all

Ms. Marian Higa
Page 2
January 16, 1996

parties would be greatly enhanced by creation of a Facilitator office which we are proposing to the 1996 Legislature and 5) the coordinated health care delivery system report to legislature recommending a pilot program may provide solutions to improve delivery of timely and reasonable quality medical care to our injured workers at a reasonable price while also reducing bureaucratic processes and paperwork.

Thank you for this opportunity to comment on your study.

Very truly yours,


Lorraine H. Akiba
Director



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Sharon Y. Miyashiro
ADMINISTRATIVE DIRECTOR

Clyde W. Namu'o
DEPUTY ADMINISTRATIVE DIRECTOR

January 19, 1996

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JAN 19 4 32 PM '96

OFF. OF THE AUDITOR
STATE OF HAWAII

Marion M. Higa
Office of the Auditor
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917

Dear Ms. Higa:

Thank you for providing the Judiciary a draft report on the, *Study of the Workers' Compensation Claims Process for State Employees*. Pursuant to your cover letter dated January 10, 1996, we are respectfully providing you with comments to your recommendation contained therein.

The Judiciary, as the third and co-equal branch of government, has been responsible for its own personnel system, including the area of workers' compensation administration, since 1977. The workers' compensation branch within the Judiciary has continuously evolved and developed in an effort to achieve its goals and objectives as set forth in *Chapter 12, Workers' Compensation, The Judiciary Personnel Manual of Policies and Procedures, June 1992*. We are very satisfied with the progress in our workers' compensation program, which aggressively manages claims, while creating a positive, nonadversarial relationship with our employees.

As outlined on page 6 of your report, the audit focused on three objectives: (1), to determine the roles, functions, and responsibilities of state agencies; (2), to assess the efficiency, cost effectiveness and accountability for claims processed for state employees; and (3), to make recommendations regarding (2) and (3). Based on the findings contained in the draft report, it is your recommendation to assign centralized responsibility and authority to DHRD for all aspects of claims management for state employees.

The Judiciary is not in agreement with the recommendation for the centralization of workers' compensation filed by all state employees, including the Judiciary, under the authority and responsibility of DHRD. As a separate and autonomous branch of government, the Judiciary has always strived to increase efficiency and provide cost effectiveness and accountability on its workers' compensation claims. The Judiciary currently consists of 14 separate divisions, i.e., District, Family, and Circuit courts of

the First, Second, Third, and Fifth Circuits, as well as the Appellate courts and Administration. Claims filed by employees of The Judiciary are handled and managed by the workers' compensation branch in the personnel office of the Judiciary. Policies and procedures are in place and are reviewed annually to ensure standardization in the claims process and to make it less burdensome on the employees of the Judiciary who file for workers' compensation benefits.

Our workers' compensation branch chief holds an independent adjusters license (number 102599). He oversees all workers' compensation matters including recommending approval of all settlements for claims filed by employees of the Judiciary, establishing policies and procedures for filing of claims, handling return to work accommodations, as well as responsibility or claims management. Assistance and advice are provided by attorneys from the Employment Relations Division of the Department of the Attorney General, or from private counsel.

Training is offered on a continuous basis to all 14 divisions within the Judiciary by the workers' compensation branch. The intent is to familiarize all employees with the Hawaii workers' compensation system, and the Policies and Procedures as set forth in the Personnel Manual, as well as to familiarize supervisors and administrators with the management aspects of our workers' compensation system.

Concerning the issue of cost control, the Judiciary retains the services of a private auditing company to review workers' compensation medical bills. For your information, the audit company reviewed approximately \$43,000.00 of provider charges and of that amount, the Judiciary paid out approximately \$33,000.00, a savings of approximately \$10,000.00. Total cost paid by the Judiciary for this service was \$139.00.

We understand that the problems in workers' compensation on a state wide basis is a complex one. We recognize that the task of doing a thorough investigation is a difficult one. The draft report attempts to identify the problems with workers' compensation for state employees. The report refers to two sources, one of which is the 1994 report of the Governor's Task Force, which concluded "among other things, that existing data on workers' compensation is not available on a timely basis and lacks sufficient detail for making fully informed policy decisions." Furthermore, reference is made to a 1993 study of state government's self-insured program (by ARM Tech), conducted for DHRD. The study recommends the centralization of the remaining executive agencies and making certain improvements at the State Workers' Compensation Division.

The conclusions and recommendations favor systematic cost control and a comprehensive, centralized management to be responsible for oversight, coordination, and reporting for all claims filed by state employees. The report designated the State Workers' Compensation Division as the centralized agency. The draft report cites, as justification, that claims management is not consistent. Exhibit 3.2 is used to show a comparison between the State Workers' Compensation

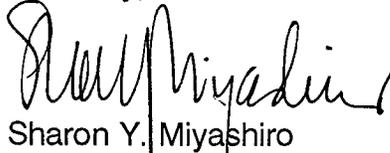
Division and the noncentralized agencies, which includes the Judiciary and how, based on the number of claims denied or denied pending investigation, the State Workers' Compensation Division is "taking a tougher approach" in managing claims. Our records reflect the following:

<u>Initial Disposition of Claims</u>	<u>Judiciary 1994</u>		<u>Judiciary 1995</u>	
	<u>Number</u>	<u>Percent</u>	<u>Number</u>	<u>Percent</u>
Claims accepted	34	67%	34	52%
Claims denied pending investigation	17	33%	31	48%
Total number of claims	51	100%	65	100%

Based on the above data, the Judiciary takes exception to Exhibit 3.2 on Claims Management Comparison.

The Judiciary has independently worked towards meeting the objective of its own policies and procedures as well as striving for efficiency and accountability in the area of workers' compensation. We have provided you with information on what The Judiciary has done to meet these goals and objectives. Based on our effectiveness and success in dealing with problems in the area of workers' compensation, the Judiciary would be in favor of continuing to independently manage all aspects of workers' compensation for all Judiciary employees.

Sincerely,



Sharon Y. Miyashiro
Administrative Director of the Courts