Injury Schemes Seminar
Road to Recovery

Actuaries Institute
8-10 November 2015 • Hilton • Adelaide
Outsourced Claims Management
Driving better performance

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Agenda

1. Introduction
2. How significant is outsourcing?
3. Outsourcing trends
4. What is outsourced?
5. Why outsource?
6. Risks associated with outsourcing
7. Our observations
8. A simplified framework to drive better performance
9. Are outsourced providers doing a good job?
10. Key takeouts
1. Introduction

Why?
Exactly what are we talking about and why?

Observations
What have we observed and why are some of these issues occurring?

A suitable management framework
How can the risks be effectively managed and the best results obtained from our outsourced providers?
1. Three lines of defence model

**Executive Management / Boards**
- Sets “Tone from the Top”
- Establishes risk appetite and strategy
- Approves the risk management frameworks, methodologies, overall policies, and roles and responsibilities
- Leverages risk information into decision making process.
- Accepts, transfers or mitigates identified risks.
- Evaluates BU activities on a risk adjusted basis

**Internal Audit**
- Provides independent testing & verification of efficacy of corporate standard and business line compliance.
- Validates the overall risk frameworks
- Provides assurance that the risk management process is functioning as designed and identifies improvement opportunities

**Compliance / risk mgmt**
- Provides interpretation of regulations and disseminates to business units
- Monitor compliance with regulations
- Develop and monitor policies and procedures
- Risk assessment based compliance testing
- Advise on regulatory issues

**BU Process and Risk Owners**
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**First Line of Defence**
- "Owner" of the risk management process
- Identifies, manages, mitigates and reports on operational risk
- Loss data tracking (internal/external)
2. How significant is outsourcing?

**Keys Stats***

The three “outsourced” states provide workers compensation insurance to more than 6.5 million employees (more than 60% of the working population)

These three schemes were responsible for making payments direct to claimants of approximately $2.5 billion in 2012-13

Collectively they were responsible for managing almost 70,000 seriously injured workers (more than 1 week time lost)

* Source: CPM report October 2014
### 3. Outsourcing trends - pressures

<table>
<thead>
<tr>
<th>Key theme</th>
<th>Description</th>
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</table>
| **Budget Pressures** | • Federal and state budgets are under increasing pressure  
                           • Are schemes able to show the value of maintaining a fully staffed claims operation?                                                   |
| **Contestability**   | • The current Federal Government is looking at the contestability of all its agencies  
                           • They are looking at the recommendations from the Harper competition review  
                           • Will Government monopoly schemes continue to exist in their current form?                                                            |
| **People**           | • The management of these schemes requires a high level of specialty expertise (claims, legal, medical, etc)  
                           • Will Government wages policy allow it to employ the required expertise?                                                                  |
| **Technology / Digitilisation** | • Customer expectations of digital offerings continues to grow  
                           • Customer and claim analytics are becoming increasingly sophisticated  
                           • Are Government’s willing to invest the required capital in this area?                                                                 |
3. Outsourcing trends – general insurance

**Procurement**
- Procure-To-Pay
- Transaction Processing
- Strategic Sourcing
- Vendor Contact Centre

**Technology**
- Software Development
- Testing
- System and Application Maintenance
- Customer Technology Support
- Package/Enterprise Applications Support & Installation
- Application Development
- Network Infrastructure Management
- Database Management

**Finance and administration**
- Accounts payable
- General Ledger Accounting
- Lust-to-Dust
- Accounts Receivable
- Cash Management
- Technical Reinsurance accounting
- Regulatory Reporting

**HR**
- HR Services
- Payroll
- Processing
- Employee Contact Centre
- Benefits Administrator
- Recruiting Administration
- Employee Data Maintenance

**Claims**
- Claims administration
- Claims processing
- Reserving
- Actuarial
- Fraud detection & prevention
- Claims reporting

**Policy Admin**
- Technical reinsurance accounting
- Client data management
- Billing
- Policy Processing

**Underwriting**
- Information Gathering & Risk Selection
- Risk Assessment
- Account Structuring
- Rating
- Pricing
- Negotiation
- Issuance
- Account Servicing

**Sales**
- Commissions scheme
- Customer Analytics
- Market research
- Data Analysis
- Outbound Telemarketing
- Call Handling
- Help Desk
- Customer Fulfilment

**Underwriting**
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**Claims**
- Claims administration
- Claims processing
- Reserving
- Actuarial
- Fraud detection & prevention
- Claims reporting
4. What is outsourced?

Key Observations

1. 3 different operational models depending on whether:
   - Outsourced – NSW, Vic and SA
   - Underwritten – WA, NT, Tas, ACT
   - Monopoly - QLD

2. End-to-end claims process is highly variable depending on the operating model.

3. The effectiveness and efficiency of the claims assessment process has a direct bearing on claims outcomes.

4. Variability exists in the use of claims partners within the same operational model.

5. Supporting functions are typically outsourced to varying degrees regardless of the operational model.

6. Limited system capability necessitates a comprehensive outsourced arrangement.
4. What can be outsourced?
5. Why Outsource?

The reasons for outsourcing should assist the scheme to meet its objectives.

Well accepted reasons for outsourcing:
- Improvement in cost level or cost reduction: 17%
- Efficiency improvements: 13%
- Improved focus on core business: 12%
- Access to specific knowledge, expertise and tools: 10%
- Quality improvement: 9%

Source: Business Briefing Issues - 20 Issues on Outsourcing and Offshoring.
5. Scheme Objectives

- **Customer Service**
  - Optimal recovery/health outcomes

- **Risk Management**
  - Reduce incidence & severity of claims
  - Reduce impact of volatile liabilities on the balance sheet

- **Competitive premiums/levies**
  - Premiums should offer customers value for money
  - Efficient and affordable

- **Financially sustainable**
  - Good experience for claimants
  - Improved health and quality of life for claimants
  - Improve RTW outcomes

- **Customer Service**
  - Financially sustainable
  - Optimal recovery/health outcomes

- **Focus on risk management at all stages**
  - Price signals should encourage risk management

Sound financial outcomes for the scheme and stakeholders

Good experience for claimants

Improved health and quality of life for claimants

Improve RTW outcomes
5. Misaligned Objectives

Scheme
Government goals
RTW
Health outcomes
Risk management

Outsourced Provider
5. Misaligned Objectives

Government goals
RTW
Health outcomes
Risk management

Scheme

Outsourced Provider

Profit

Risk Increases!
7. Risks associated with outsourcing workers comp claims

The universal risks + The Scheme Risk + Personal Injury claims risk

Most important risks for outsourcing

- Dependency: 51%
- Loss of control: 43%
- Impact on quality: 35%
- Loss of knowledge: 29%
- Info Security: 29%

- Misunderstood scheme objectives
- Ineffective monitoring procedures
- Lack of BCM arrangements
- Ineffective management and control of the outsourcing relationship
- Complex claims
- Decisions not black and white
- Scheme can develop a culture

Source: Business Briefing Issues - 20 Issues on Outsourcing and Offshoring.
### 7. Our observations

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7. Our observations

The contract and the remuneration is crucial in aligning objectives and driving the desired behaviours of the service provider. We have seen examples where this has been done poorly by some schemes.

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<th>Size</th>
<th>Observation</th>
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<td>Third Party Recoveries</td>
<td>Can be up to 5% of gross claims costs</td>
<td>We have seen contracts that do not address the issue of third party recoveries.</td>
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<td>We have rarely seen any remuneration designed around third party recoveries.</td>
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<td>Individual claim reviews have repeatedly provided many examples where a third party recovery was at least plausible.</td>
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<tr>
<td>Legal Providers</td>
<td>Can be between 5% to 10% of gross claim payments</td>
<td>Contracts we have seen are normally quite vague around the use of other service providers such as legal, investigatory or allied health.</td>
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<td>Normally rely upon the agents or regulators own panel arrangements.</td>
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<td></td>
<td>The use of legal firms and their subsequent use of barrister, etc is not governed.</td>
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<tr>
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<td></td>
<td>There is no transparency and hence no cost control.</td>
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<tr>
<td>Process audits</td>
<td>Varies</td>
<td>Many individual claim audits are designed around process.</td>
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<td>They give no indication of the quality of claims outcomes or claims leakage.</td>
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<td>Providers know this and ensure they pass the process audit.</td>
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<td>Often they are remunerated for this – without any impact on claims outcomes!</td>
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8. A simplified risk management approach

- Have a deep understanding of the claims strategy and how it influences the claims operational strategy.
- Understand the risks of the current state and future state operating model.
- Develop a fit for purpose 3 Line of defence approach based on strategy and operational model.

2nd line of defence is the key differentiator.
8. A simplified risk management framework – 3 LOD

<table>
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<tr>
<th>1st Line</th>
<th>2nd Line</th>
<th>3rd Line</th>
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<tr>
<td>Risk Ownership</td>
<td>Risk Control and Monitoring</td>
<td>Independent Assurance</td>
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### 1st Line: Risk Ownership
- Executive committee
  - Supported by Risk Taking Business Units
  - Owners of risk within the business
  - Delegated authority from the Board to develop and implement the strategy,
  - Measure and manage business performance, develop and implement internal control and risk management framework
  - Ensure that the business is managed within the agreed risk appetite

### 2nd Line: Risk Control and Monitoring
- Risk Oversight committee
  - Supported by Compliance, Risk Management and Risk Modelling
  - Provides objective oversight of the management of risk. Key activities include
    - Designs and deploys the overall risk management framework aligned to strategy across the organisation
    - Implements a robust monitoring programme for adherence to framework, strategy, policies and procedures
    - Performs analytics and aggregated risk reporting

### 3rd Line: Independent Assurance
- Audit committee
  - Supported by Internal Audit
  - Provides independent and objective assurance over the effectiveness of corporate standard and business compliance
  - Assurance that the risk management process is functioning as designed and identifies improvement opportunities

---

The Risk Management strategy must work top down and bottom up. Value of day to day risk and control activities needs to be effectively communicated and embedded. Engagement from business is essential.

The Risk Management function must have sufficient capabilities, business acumen and experience to play an active role in strategic or business risk related debates within the business and is objective and independent from operational functions.

The function needs to be independent from the organisational activities. Has appropriate standing within the organisation and shall carry out its assignments with impartiality.
8. Ideal 2nd line – improve contract management

Prudential Practice Guideline 230
- Develop a risk management framework
  - Determine definition of operational risk appropriate to size, business mix and complexity
  - Identification of human resource needs, monitoring and supervision
  - Consider fraud risk arising from both internal and external resources
  - Address project risk with a project management framework and include:
    - Business case
    - Cost/benefit analysis
    - Risk identification and assessment
    - Stakeholder sign-offs
    - Delegations
    - Monitoring
    - Post-implementation review

Prudential Practice Guideline 231
- Risk consideration of beneficiaries (claimants and policyholders)
- Materiality considerations
- Service level agreement
  - Address subcontracting and consider back-to-back arrangement on security, confidentiality, offshoring compliance and access to information
  - Flexibility to accommodate change in process
  - Monitoring procedures
  - BCM arrangements
  - Default arrangements
  - Terminations risks and procedures
  - Pricing arrangements
  - Dispute resolution mechanisms
- Develop an outsourcing team with necessary skills
  - Liability and indemnity issues
  - Offshoring, consider
  - country, contractual and compliance, access and counter-party risk
    - Choice of law, security
  - Management and control of the outsourcing relationship
    - Devote sufficient resources
      - Monitoring framework appropriate for size and nature of arrangement
      - Support audit function, specifically regarding access
8. Ideal 2nd line – improve contract management

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    - Choice of law, security
- Management and control of the outsourcing relationship
9. Monitoring

Requires a pro-active and dynamic approach to risk based monitoring and analytics

- Analyse scheme experience to proactively identify risks
- Assess consequences/severity of risks to stratify risks
- Apply a range of tools / instruments / strategies to prevent / mitigate risks, focusing on the key risks
- Monitor and evaluate the effectiveness of tools / instruments / strategies
- Review current risks, identify new risks
9. Quality Assurance

- There is one key question to which we rarely receive a good answer
- “Is your outsourced provider doing a good job?”
- Individual claim file reviews that focus on the quality of outcomes
- Is squarely the responsibility of the risk owner
- Not only identifies problems but can also be used for training / education
- Requires claims management expertise
- Otherwise it becomes a process audit
10. Key Takeouts

- The scheme is the risk owner
- Outsourcing can be very valuable but it increases risk
- Be vigilant
  - Pro-actively manage your provider
  - Monitor, monitor, monitor
- Put an appropriate risk management framework in place

- “Don’t outsource your brain” Len Boehm