

**SUBMITTAL TO THE BOARD OF SUPERVISORS  
COUNTY OF RIVERSIDE, STATE OF CALIFORNIA**



**ITEM**  
2.11  
(ID # 2962)

**MEETING DATE:**

Tuesday, December 6, 2016

**FROM :** AUDITOR CONTROLLER:

**SUBJECT:** AUDITOR CONTROLLER: Internal Audit Report 2015-018: Riverside County Human Resources, Risk Management [District: All]; [\$0]

**RECOMMENDED MOTION:** That the Board of Supervisors:

1. Receive and file Internal Audit Report 2015-018: Riverside County Human Resources, Risk Management

**ACTION: Consent**

  
Paul Angulo, Director of Auditor Controller 11/4/2016

<b>FINANCIAL DATA</b>	<b>Current Fiscal Year:</b>	<b>Next Fiscal Year:</b>	<b>Total Cost:</b>	<b>Ongoing Cost</b>
<b>COST</b>	\$ 0	\$ 0	\$ 0	\$ 0
<b>NET COUNTY COST</b>	\$ 0	\$ 0	\$ 0	\$ 0
<b>SOURCE OF FUNDS: N/A</b>			<b>Budget Adjustment: NO</b>	
			<b>For Fiscal Year: N/A</b>	

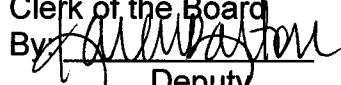
**C.E.O. RECOMMENDATION:**

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**MINUTES OF THE BOARD OF SUPERVISORS**

On motion of Supervisor Ashley, seconded by Supervisor Tavaglione and duly carried, IT WAS ORDERED that the above matter is received and filed as recommended.

**Ayes:** Jeffries, Tavaglione Washington and Ashley  
**Nays:** None  
**Absent:** Benoit  
**Date:** December 6, 2016  
**xc:** Auditor

Kecia Harper-Ihem  
 Clerk of the Board  
 By   
 Deputy

**2.11**

**SUBMITTAL TO THE BOARD OF SUPERVISORS COUNTY OF RIVERSIDE,  
STATE OF CALIFORNIA**

**BACKGROUND:**

**Summary**

We have completed an audit of the Riverside County Human Resources, Risk Management to provide management and the Board of Supervisors with an independent assessment of internal controls over risk management operations, information security, records management, and claim processes and procedures. We conducted the audit from March 20, 2015 through June 15, 2015 for operations for the period July 1, 2012 through April 30, 2015. We expanded our review of information that was provided through a new actuarial report regarding funding/confidence levels.

This report was made available on March 21, 2016 for a covered period of fiscal years 2015-16 and 2016-17.

Based upon the results of our audit, we identified an opportunity for improvement in confidence level funding. We determined internal controls over information security, records management and claims processes and procedures provided reasonable assurance that its objectives relating to these areas will be achieved. Reasonable assurance recognizes internal controls have inherent limitations, including costs, mistakes, and intentional efforts to bypass internal controls.

**Impact on Residents and Businesses**

Provide an assessment of internal controls over the audited areas.

**SUPPLEMENTAL:**

**Additional Fiscal Information**

Not applicable

**ATTACHMENT A.**

Riverside County Auditor-Controller's Office Internal Audit Report 2015-018: Riverside County Human Resources, Risk Management

  
Stephanie Pasi 11/28/2016

**Internal Audit Report 2015-018**

**Human Resources, Risk Management**

**Report Date: September 13, 2016**



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**ACC** | AUDITOR  
CONTROLLER  
COUNTY OF RIVERSIDE

Paul Angulo, CPA, MA  
Riverside County Auditor-Controller

Frankie Ezzat, MPA  
Assistant Auditor-Controller

September 13, 2016

Michael Stock  
Assistant CEO/HR Director  
Riverside County Human Resources Risk Management  
4080 Lemon St.  
Riverside, CA 92501

**Subject: Internal Audit Report 2015-018: Human Resources, Risk Management**

Dear Mr. Stock:

We have completed an audit of the Riverside County Human Resources, Risk Management to provide management and the Board of Supervisors with an independent assessment of internal controls over risk management operations, information security, records management, and claim processes and procedures. We conducted the audit from March 20, 2015 through June 15, 2015 for operations for the period July 1, 2012 through April 30, 2015. We expanded our review of information that was provided through a new actuarial report regarding funding/confidence levels. This report was made available on May 6, 2016 for a covered period of fiscal years 2015-16 and 2016-17.

We conducted our audit in accordance with the International Standards for the Professional Practice of Internal Auditing. These standards require that we plan and perform the audit to obtain sufficient, reliable, relevant and useful information to provide reasonable assurance that our objective as described above is achieved. An internal audit includes the systematic analysis of information to evaluate and improve the effectiveness of internal controls. We believe this audit provides a reasonable basis for our conclusion.

Internal controls are processes designed to provide management reasonable assurance of achieving efficiency of operations, compliance with laws and regulations, and reliability of financial and non-financial information. Management is responsible for establishing and maintaining adequate internal controls. Our responsibility is to evaluate the internal controls.

Based upon the results of our audit, we identified an opportunity for improvement in confidence level funding. We determined internal controls over information security, records management and claims processes and procedures provided reasonable assurance that its objectives relating to these areas will be achieved. Reasonable assurance recognizes internal controls

**Internal Audit Report 2015-018: Riverside County Human Resources, Risk Management**

have inherent limitations, including costs, mistakes, and intentional efforts to bypass internal controls.

As requested, in accordance with paragraph III.C of the Board of Supervisors Resolution 83-338, management responded to each reported condition and recommendation contained in our report. Management's responses are included in the report. We will follow-up to verify if management was able to increase the confidence level funding to recommended levels.

We thank the Riverside County Human Resources, Risk Management management, and staff for their cooperation. Their assistance contributed significantly to the successful completion of this audit.

Paul Angulo, CPA, MA  
Riverside County Auditor-Controller



By: René Casillas, CPA, CRMA  
Interim Chief Internal Auditor

cc: Board of Supervisors  
Executive Office  
Grand Jury

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## Executive Summary

### Overview

Human Resources, Risk Management's (Risk Management) stated mission is "To protect the County of Riverside's resources (human and financial) from the risk of losses, by managing the risks through identifying and analyzing loss exposures (property, liability, earnings, personnel); examining the feasibility of alternative risk management techniques (risk control, risk financing); selecting the most appropriate risk management alternative to control exposures; implementing the best alternatives to resolve problems; and monitor risk management programs designed to meet intended goals." *Riverside County Human Resources – Risk Management website accessed November 3, 2015, <http://riskmgmt.rc-hr.com/RiskandInsuranceProgram.aspx>*

Risk Management staff specializes in various aspects of professional risk management services, including administering programs of self-insurance for general liability, vehicle liability, and medical malpractice.

The County of Riverside (County) participates in the California State Association of Counties/Excess Insurance Authority (CSAC/EIA). CSAC/EIA is a pooling/group purchase program consisting of other government agencies and was formed as a joint powers authority in 1979. The County is currently responsible for the first \$2,000,000 of each loss and CSAC/EIA for the excess coverage. CSAC/EIA requires member agencies to compile claims in accordance with the generally acceptable claims handling standards. These standards cover several topics including general procedures, instructions for administering a claim and required forms. CSAC/EIA requires participating agencies to have an audit every three years.

Risk Management maintains a claim file for every claim filed against the County. Claims are filed no later than six months after an occurrence with the Clerk of the Board who in turn forwards them to Risk Management for processing. California Government Code section 913 requires the County to give written notice of action on the claim within 45 days. Therefore, the gathering and timely processing of pertinent and relevant information is essential to the efficient and effective handling of claims management.

### Audit Objective

Our audit objective is to provide management and the Board of Supervisors with an independent assessment of Risk Management's internal controls over information security, records management, claims processes and procedures, and confidence level funding.

### Audit Conclusion

Based upon the results of our audit, we identified an opportunity for improvement in confidence level funding. We determined Riverside County Human Resources, Risk Management internal controls over information security, records management and claims processes and procedures did provide reasonable assurance that its objectives relating to these areas will be achieved.

**Internal Audit Report 2015-018: Riverside County Human Resources, Risk Management**

Reasonable assurance recognizes internal controls have inherent limitations, including costs, mistakes, and intentional efforts to bypass internal controls.

## **Confidence Level**

### **Background**

County of Riverside began its self-insured general liability program on July 1, 1982. Its current self-insured retention is \$2,000,000, with the CSAC/EIA's Liability Program II providing excess coverage. Claims administration services are provided by Risk Management.

On June 24, 2013, the Board of Supervisors adopted a 55% funding level (confidence level) policy thru fiscal year ending June 30, 2015 as a means to reduce charges to departments during the recent recession. As of January 13, 2016 the Board adopted a confidence level of 60%. The confidence level is the funding margin for the possibility that actual costs will be greater than estimated expenses.

County of Riverside contracts with Bickmore, a risk management-consulting firm, for actuarial services. The specific objectives of the study are to estimate the County's liability for outstanding claims by fiscal year, project ultimate loss costs for future fiscal years, and provide funding guidelines to meet these liabilities and future costs. Per actuarial studies prepared by Bickmore, November 4, 2015, estimated ultimate cost of claims and expenses for claims incurred during the 2015-16 and 2016-17 program years to be \$24,548,000 and \$27,074,000, respectively. These amounts include losses, allocated loss adjustment expenses, and unallocated loss adjustment expenses. Allocated loss adjustment expenses is the direct cost associated with the defense of individual claims (legal fees, investigation fees, court charges). Unallocated loss adjustment expenses is the cost to administer claims to final settlement, which may be years in the future (claims adjusters' salaries, taxes).

Bickmore's actuarial report from November 2015, estimated the program's liability for outstanding claims to be \$68,135,000 and \$72,637,000 for June 30, 2015 and June 30, 2016, respectively. Furthermore, at the time of Bickmore's aforementioned report, it estimated program assets of \$22,586,000 for June 30, 2015 and \$33,537,000 for June 30, 2016, both years with the program funded below the expected confidence level.

Because actuarial estimates of claims costs are subject to some uncertainties, Bickmore recommends that an amount in addition to the discounted expected loss be set aside as a margin for contingencies. Generally, the amount should be sufficient to bring funding to the 75% or 85% confidence level for primary programs. Minimal acceptable level for the County should be the 70% confidence level. Funding at the 60% confidence level is a step in that direction, and means that the funds collected will be enough to cover costs 60% of the time, or alternatively the funds collected will not be enough to cover costs 40% of the time. The actuarially recommended 70% confidence level reduces the likelihood of running out of funds to 30%. In all cases, if an adverse loss scenario were to occur, and reserves become depleted, the County would require use of additional Unrestricted Net Assets (UNA). See the table below with prior two fiscal years of actual data for the impact on unrestricted net assets:



Fiscal Year	Funding at *70% Confidence level	Funding at *55% Confidence Level	Difference	Liability Insurance Revenue**	Liability Insurance Expenses**	Impact on UNA***
2013-14	\$19,186,000	\$16,557,000	\$2,629,000	\$26,663,147	\$25,593,990	\$1,069,156
2014-15	30,984,000	26,975,000	4,009,000	51,807,826	54,919,617	(3,111,791)

\*Bickmore Actuarial Study, October, 25, 2013

\*\*Contributions/Donations, Stop Loss Reimbursement, Other

\*\*\*All Expenses

\*\*\*\*Unrestricted Net Assets

A key factor to consider in determining funding policy is the degree to which stability is required in the level of contributions to the program from year to year. If you elect to maintain assets at a low confidence level, the chances are much greater that future events will prove that additional contributions should have been made for old claims. The additional contributions for old claims may be required at the same time that costs are increasing dramatically on new claims. The burden of funding for increases on past years as well as on current years, may well be prohibitive.

The CSAC/EIA standards states that based upon the actuarial recommendations, the member should maintain reserves and make funding equal to or exceeding the present value of expected losses and a reasonable margin for contingencies.

The State Controller's Office "requires catastrophic reserves, incurred loss reserves and incurred but not reported reserves to be funded with cash and /or investments to provide for the payment of losses. All reserves must be segregated in restricted accounts or accounted for separately and used exclusively for the purpose for which they were intended."

**Audit Objective**

Our audit objective is to provide management and the Board of Supervisors with an independent assessment of Risk Management's appropriateness in confidence level.

**Audit Conclusion**

Based upon the results of our audit, maintaining reserves below actuarial consultant recommended levels will continue to have a negative impact on future actuarial reports and may require the continued use of unrestricted net assets.

**Management position concerning the conclusion: Concur**

**Comments:**

The Human Resources Department agrees with the audit conclusion. Maintaining a confidence level below 70% has decreased the fund's assets to a level greatly below the actuarial determined amount needed to pay claims. We are in discussions with the Executive Office on a plan to return to a 70% confidence level. The first step was to increase the fiscal year 2016/17 funding requirements to the 60% confidence level.

**Actual/Estimated Date of Corrective Action:**

The Human Resources Department will continue to work with the Executive Office on returning the confidence level to 70%. Increases in the confidence level will depend on the ability of county departments to absorb increases in the internal service rate.

**Estimated Cost to Implement Recommendation (if material):**

The amount would have to be actuarially determined in the year of change in the confidence level occurred. The difference in the fiscal year 2016/17 funding requirements to raise the confidence level from 55% to 60% was \$1,990,000. If the confidence level was raised to 70%, the necessary increase in funding would have been \$6,601,000.