

FORENSIC ANALYSIS
of
COMMUNITY RESIDENCE INSURANCE SAVING PLAN
for
THE NEW YORK STATE WORKERS' COMPENSATION BOARD
by
BOLLAM, SHEEDY, TORANI & CO. LLP, CPAs

February 1, 2013



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EXECUTIVE SUMMARY

The New York State Workers' Compensation Board (WCB) regulates and monitors programs that offer workers' compensation insurance to employers in New York State, including group self-insurance trusts. WCB regulations require the WCB to ensure that the group self-insured trusts are financially viable and have remediation plans in the event a trust's financial stability needs to be restored. Primarily as a result of financial concerns regarding several group self-insured trusts, the WCB began a process of seeking an independent assessment of the financial and operational aspects of certain group self-insured trusts, and the entities responsible for the administration and management of these trusts.

The WCB retained Bollam, Sheedy, Torani & Co. LLP, CPAs ("BST") through a competitive procurement process in June 2008 to provide an independent assessment of several group self-insured trusts.¹ BST was engaged to perform a review of the Community Residence Insurance Saving Plan ("CRISP" or "Trust") during August 2011.

CRISP was created, effective December 15, 1995 to provide workers' compensation insurance to employers engaged in providing human services and residential facilities to children and adults. The Trust was governed by a Board of Trustees and managed by Program Risk Management, Inc. ("PRM") - the Trust Administrator whose duties were overseen by the Board of Trustees. The Trustees voted to dissolve the Trust, effective December 31, 2010, and the WCB began working with the Trustees to administer the affairs of the Trust and to liquidate Trust assets. Effective August 9, 2011, the WCB appointed a new Trust Administrator to handle the affairs of the Trust during run-off. This report addresses the issues and circumstances surrounding the formation and operation of CRISP and its \$32,375,129 audited member deficit as of October 31, 2012. The final gross allocable Members' deficit as calculated in our Deficit Reconstruction and 2013 Deficit Report amounts to \$60,715,450.

Our independent assessment of CRISP's operation began with a review of documents provided by the WCB, including the documents relating to the Trust's formation, e.g., Trust Agreement, Service Agreement, and By-Laws. We subsequently read and analyzed thousands of documents.

We also read and analyzed the workpapers relating to the audited financial statements provided by CRISP's financial statement auditor. In addition, we engaged a third-party actuary to provide an independent assessment of the Trust's claim liabilities, and a claims consultant to provide an independent evaluation of the Trust Administrator's claims handling practices.

We met with and/or interviewed by phone five Members and four Trustees, including the Chair and Secretary-Treasurer. We also interviewed, at length, the Trust's legal counsel who provided numerous documents beneficial to our examination. Representatives from PRM, the Trust's

¹ The services provided by BST were essentially an independent assessment of the duties, responsibilities, and actions of the Trust Administrator, Claims Administrator and the Trustees, and a financial analysis of the Trust's assets and liabilities. We did not provide any attestation services with regard to the Trust and/or the WCB.

Program Administrator; and PRM Claims Services (“CSI”), the Trust’s Claims Administrator declined, through legal counsel to be interviewed, but agreed to and did provide certain documents requested by BST . BST would like to acknowledge former PRM Executive Vice-President Edward Sorenson, in particular, for his assistance.² Similarly, through its counsel, M.P. Agency, the Trust’s marketing agent, furnished certain documents and responded in writing to questions prepared by BST. We met with the independent accounting firm, Marvin & Company, that audited the Trust’s financial statements, and we communicated with the Trust’s actuary. (Stergiou & Gruber, a.k.a. SGRisk, Inc.).

Additional information may become available and, accordingly, we reserve the right to modify our report.

During the past six years, BST has conducted a forensic analysis of thirteen group self-insured trusts on behalf of the New York State Workers’ Compensation Board. The trusts analyzed by BST were eventually taken over by the WCB because of the trusts’ deficit conditions. Over the course of their existence, these trusts sustained significant losses and moved into a deficit position primarily due to five factors:

- Insufficient premiums (often combined with unusually high premium discounts);
- Suppression of claim reserves or unrealistic claim reserving estimates;
- Questionable actuarial estimates (on certain occasions);
- Conflicts of interests by a trust administrator serving concurrently as claims administrator; and
- The financial incentive to make or save money.

The trusts many times failed due to limited oversight by the Trustees. In most instances, the impetus to form and operate a trust came from a trust administrator (some of whom lacked even the basic credentials) - who received a fee for their services, and as such, the best interest of the members was not always foremost. The Trustees often had little, if any, role in preparing the complex legal documents which established and governed the trust. They generally did not have these documents vetted by independent legal counsel, and on some occasions, Trustees stated that they never even saw or reviewed the documents.

For both members and trust administrators, the underlying theme about whether to get involved in the trust essentially concerned money: how much can I make (trust administrator and marketing agents), and how little can I pay to get workers’ compensation insurance coverage (trust members). The monetary factor greatly contributed to the trusts’ financial problems as the business objectives of the related parties (administrators v. members) were often diametrically opposed.

Specifically, the trust administrators and marketing agents had a financial incentive to recruit and keep as many members as possible in the trust - regardless of the members’ loss history; and the members tended to join the trust simply because it was the cheapest insurance they could

² Sorenson retired from PRM in April 2012.

procure. The evidence examined strongly suggests that members with good loss histories were generally not aware of the premiums paid by other members and/or their losses, and therefore were not in a position to question the members' continued membership in the trust.³ As such, there was always financial pressure for the trust administrators to at least create the perception that the trust was a financially viable entity (so they would not have to increase premium rates), otherwise new members, who are jointly and severally liable for the trust deficits, would not join the trust, or existing members would leave the trust - thereby reducing the trust administrators' revenues.

In certain respects, and as detailed below, the CRISP Trust was not dissimilar to the other trusts analyzed by BST, i.e., most of the factors noted above contributed to the dissolution of this trust.

Major Observations:

- 1) CRISP's Board of Trustees did not have a policy in place which required term limits for all Trustees, which may have resulted in the lack of fresh ideas, limited the diversity of the Board, and resulted in the concentration of power within a small group of Trustees.
- 2) The Trustees met on a regular basis, were engaged and informed about the operations of the Trust, and actively deliberated the issues facing the Trust; however, evidence suggests the Trustees did not always perform their fiduciary duties consistent with the Trust documents.
- 3) There appears to have been good information flow between the Trustees and their consultants, and Trustee decisions appear to have been based on thoughtful evaluation and discussion of information provided by the Trust's paid consultants. However, information furnished to the Trustees may not have been accurate on occasion, and not all of the decisions appear to have been in the best interest of the Members.
- 4) The Trustees proactively sought outside legal, claims and actuarial assistance to aid in their oversight of the Trust and the Trust's growing deficit position, and strove increasingly over the years to acquire from PRM more control over the Trust's operations. However, the Trustees never engaged in a competitive process to consider other potential Trust Administrators, despite admittedly having concerns with the Trust Administrator.
- 5) The Trustees approved and received compensation as authorized by the Trust Agreement totaling in excess of \$420,000, plus expenses. The compensation paid specifically to the Chair (ultimately totaling \$3,000 per month) was markedly inconsistent with compensation received by Chairs of other group self-insured trusts examined by BST, most of whom received no compensation. Additionally, there was no requirement for the Chair to specifically account to the other Trustees for time purportedly spent on Trust-related activities.

³ Sales marketing agents played a crucial role in the formation of the trust with the trust administrator and oftentimes steered their clients to the trust ostensibly because of the cheaper premiums. The agents did not always have prior experience with self-insurance trusts, which may have explained why they renewed their clients' contracts with the trusts even when the trusts were experiencing multi-million dollar member deficits.

- 6) The Trustees breached their fiduciary duties by authorizing additional payments of \$6,000 per month, plus expenses to the Trust Chair as full compensation for her participation on the Governor's Group Self-Insurance Task Force, despite the Chair clearly representing the collective interests of all group self-insured trusts, group administrators, and the Group Self-Insurance Association of New York.
- 7) The Trust's paid Counsel concurrently served as the Trust's Program Administrator's (PRM's) registered lobbyist and Qualifying Officer. While BST found no evidence to even suggest that the Trust's Counsel performed his duties in any way other than in the Trust's best interest at all times, his business relationship with PRM placed him in a conflict of interest situation with his concurrent role as Trust Counsel.
- 8) The Trust's Counsel played a key and constructive role in the formation and operation of the Trust and was paid fees that appear to be commensurate with his duties. However, there was no written contract with the Trust governing his fees or scope of services, which was not prudent from a legal or fiduciary perspective.
- 9) The Trustees failed to adopt a formal written investment policy. However, actual investment practices generally conformed to WCB investment regulations, 12NYCRR Part 317.8.
- 10) The Trustees failed to ensure the Trust's compliance with 12NYCRR Part 317.8 with respect to Trust equity investments not from American Institutions and subjected the Trust to unnecessary regulatory asset disallowances adversely affecting its overall funding status.
- 11) PRM served continuously as the Trust's Program Administrator until the Trust's termination in 2010 without any formal contract amendments or extensions.
- 12) There was no periodic, competitive process undertaken by the Trustees to determine or help ensure that fees paid to the Program Administrator were competitive, or that better services could be obtained elsewhere.
- 13) PRM incurred and failed to pay penalties for multiple procedural violations of the Workers' Compensation Law.
- 14) The Trust's paid marketing agent, M.P. Agency ("MPA") did not provide an acceptable or timely succession plan as requested by the Trustees to ensure continuity of the Trust's marketing activities after MPA's principals' departure from the firm.
- 15) Evidence suggests that MPA may have been in breach of its contractual obligations with the Trust in that it failed to continuously have Errors and Omissions coverage of \$2,000,000 per occurrence and \$2,000,000 in the aggregate as specified in its Marketing Agreement with the Trust.
- 16) On at least two occasions, MPA provided inaccurate underwriting information to PRM, resulting in the admission of certain Members that otherwise may not have met the Trust's criteria for admission.
- 17) The Trustees failed to develop member underwriting guidelines that were periodically reviewed or modified to reflect the Trust's changing market and financial conditions.
- 18) Chair Johnson allowed a Trust Member to leave the Trust without penalty and to receive a refund of prorated contributions in violation of Trust policy. This opportunity was not equitably offered to other Trust Members seeking alternate coverage at the time the Trust was about to dissolve.

- 19) Members with high experience modification rates were admitted to the Trust and were allowed to stay in the Trust despite continuing losses and high experience modification rates.
- 20) Premium discounts were granted by PRM to select Members without Trustee input or standard discount criteria approved by the Trustees. In the absence of standard criteria, the awarding of discounts was subject to manipulation for the benefit of select Members.
- 21) Despite having an apparent structured renewal process, Members with high experience modification rates were allowed to remain in the Trust, and
- 22) Despite poor loss histories, few Members appear to have been refused continued coverage by the Trust.
- 23) PRM Claim Services, Inc. (“CSI”), a firm controlled by PRM’s principals, served as the Trust’s claims administrator from 2001 to 2010, creating a possible conflict of interest situation whereby claims reserves could be established for the financial benefit of PRM and not the Trust. The Trustees, in selecting CSI, appear to have violated Article VI, Section 6a of the Trust Agreement that requires that the fiscal agent and/or administrator appointed by the Trustees “shall not be an owner, officer or employee of a third party administrator.” The failure of the Trustees and Trust Counsel, who drafted the Trust Agreement to ensure the independence of the program administrator and claims handling functions, may have had a material impact on the extent of the ultimate Member deficit.
- 24) PRM officials failed to exercise prudent oversight of its affiliate, CSI, which engaged in questionable claims reserving practices that misrepresented the Trust’s true financial condition to the Trustees.
- 25) CSI failed to properly advise the Trustees of a known reserve shortfall, may have provided erroneous and misleading information to the Trustees regarding CSI’s reserving practices, and failed to offer any viable explanation to the Trustees for the Trust’s inadequate reserves when questioned by the Trustees.
- 26) CSI’s failure to establish adequate reserves contributed to the Trust and PRM not increasing member contributions or assessments sufficient to cover the true deficit.
- 27) CSI’s understating of the Trust’s reserve liabilities and the under-reporting of these liabilities on the Trust’s financial statements may have painted a false and misleading picture of the Trust’s true financial position.

INTRODUCTION

A. Background

Every employer in New York State is required by the laws of New York to secure workers’ compensation coverage for its employees. Employers essentially have four options, joining a group self-insured trust, obtaining insurance from the New York State Insurance Fund, individually self-insuring, or obtaining insurance from a private insurance carrier.

With regard to the formation of group self-insured trusts, each group of employers must establish a trust fund that is financed by contributions from and assessments of its members. Title 12, Chapter 5, Subchapter B of the New York Codes, Rules and Regulations (“NYCRR”) establishes

the procedures, qualifications, and responsibilities for any group of employers that wishes to become, or which has been approved by the WCB to operate as a group self-insurer.⁴ Every group self-insurer must also have a set of documents that govern all aspects of the group's existence, which may include a trust agreement and by-laws.

In early to mid-1995, downstate New York-based insurance brokers Morton "Morty" Case and Priscilla "Pat" Hoffman from M.P. Alliance ("MPA") began exploring suitable alternatives to provide the statutory workers' compensation coverage at an appropriate rate for its client base of community residential social services agencies. They learned about group self-insured trusts and were referred to Thomas Arney in Albany, New York who reportedly had knowledge of both workers' compensation insurance and the group self-insurance model. Case, Hoffman, and Marshall Krassner of MPA met with Arney to discuss the formation of a trust for community residential social services agencies.

Following a number of meetings between these parties, an organizational meeting was held in Albany, New York on October 31, 1995, to form a group self-insured trust for employers providing community social services. Joining Case, Hoffman and Krassner were four Trustees representing community service providers; Arney⁵ and John Conroy of Program Risk Management, Inc. ("PRM"); David Johnson, CPA; Thomas J. Gosdeck, Esq. of Hill & Gosdeck LLC; and representatives of Chase Manhattan Bank. The Trustees approved a Trust Agreement (Exhibit 1), By-laws (Exhibit 2), and Indemnity Agreement (Exhibit 3), and appointed Johnson and Gosdeck as the Trust's accountant and legal counsel, respectively. The Trustees also approved contracts for PRM and The Alliance Group to provide program administration and marketing services for the newly-formed trust - Community Residence Self-Insurance Saving Plan ("CRISP" or "Trust").

On December 11, 1995, Arney sent to the WCB an Application for Group Self-Insurance (GSI-1), Agreement and Undertaking of Employer Group as a Self-Insurer (GSI-3), and other requested documents for review and approval. Seventeen (17) residential agency employers are identified as initial Trust participants (Exhibit 4). On December 14, 1995, the WCB Chair approved CRISP as a group self-insurer, effective December 15, 1995.

CRISP was established to provide workers' compensation coverage through a self-insurance program to employers engaged in the business of providing human services and residential facilities for children and adults. Each Trust member must be classified with Standard Industrial Classification (SIC) Code in the Major Indexes of 80-Health Services and 83-Social Services. From December 15, 1995 through December 31, 2010, approximately 450 employers joined CRISP.

⁴ The rules applying to the group self-insured trusts were originally covered under NYCRR Title 12, Chapter 5, Subchapter B, Section 316. Beginning January 31, 2001, the rules were modified and expanded.

⁵ On July 25, 1995, Arney formed Program Risk Management, Inc. Arney then served as the Program Administrator for a number of other group self-insured trusts. Previously, Arney served as a Program Administrator while working at Jardine Insurance Brokers New York, Inc. and Naples Risk Management.

The WCB determined that the Trust had a regulatory deficit of \$7,900,378 and a regulatory trust equity ratio of 57.88% as of November 30, 2009. Despite various remediation plans and actions being taken by both the Trustees and the WCB, the Trustees, on October 31, 2010, unanimously voted to cease providing Workers' Compensation coverage through CRISP as of December 31, 2010. The Trustees then began working with the WCB to settle outstanding claims and liquidate the Trust's assets. The Trust Members' regulatory deficit as of December 31, 2010, was identified by the WCB to be approximately \$24, 256,049, over three times the regulatory deficit of a year before.

In May 2011, the Trustees filed a civil suit against PRM, PRM Claims Services, and M.P. Agency ("MPA").⁶ On June 28, 2011, the WCB advised the Trustees and PRM that CRISP "has demonstrated an inability to properly administer its liabilities" and that the WCB would assume administration of the Trust. Effective August 9, 2011, the Trust's run-off was transferred to a State contracted group administrator.⁷

PRM received in excess of \$4.3 million in administrative management fees during the fifteen-year period, December 15, 1995 through December 31, 2010. PRM also received in excess of \$700,000 for loss control services during this same time period. In addition, a PRM affiliate, PRM Claim Services Inc., received in excess of \$3 million for the period May 1, 2001 through July 31, 2010, for claims administration services. MPA also received in excess of \$4.3 million in marketing fees for the period December 15, 1995 through September 30, 2009.

The WCB engaged Bollam, Sheedy, Torani & Co. LLP, CPAs (BST) during August 2011 to perform an operational assessment of CRISP and to assist the WCB in the financial reconstruction of CRISP's financial position as of October 31, 2012, and a roll-forward date that has yet to be determined. Since then, BST and other parties have assisted the WCB in its efforts to identify the reason(s) for CRISP's deficit financial condition and to determine whether PRM, MPA, and CRISP's Trustees prudently exercised their fiduciary and legal responsibilities, including actions to preserve the integrity of CRISP's funds. Our methodology and observations are detailed on the following pages.

B. Methodology

BST staff began their analysis by speaking with WCB officials to gain an overview of CRISP's financial condition and history. We also spoke with former Trustees, Members, and officials of NCA Comp, the third-party administrator hired by the WCB when it assumed control of the Trust's assets and management of the Trust's liabilities. We also received information from the Trust's program administrator, claims administrator, and marketing agent through their respective legal counsels.

⁶ On January 9, 2012, the complaint filed against PRM, PRM Claims Service, and M.P. Agency was "dismissed without prejudice to any future action" in State Supreme Court, County of Albany.

⁷ The WCB's new contract administrator is NCAComp, Inc.

BST engaged an independent actuary, a legal consultant, and an independent claims auditor to assist in our analysis of the loss reserves, legal responsibilities, and claims handling process, respectively.

BST subsequently reviewed thousands of Trust documents, including but not limited to, member files, trust formation documents, New York State Department of State records, audit reports, actuarial reports, Trustee meeting minutes, and general correspondence. In addition, we interviewed 11 individuals to date.

C. Chronology of Key Events

July 25, 1995 - Program Risk Management, Inc. (“PRM”) registers as a domestic business corporation with the New York State Department of State - Division of Corporations.

August 1, 1995 - PRM appointed as program administrator for the Health Care Providers Self-Insurance Trust (“HCPSIT”). Arney previously assisted in the formation of HCPSIT in 1992 while with another insurance firm.

August 14, 1995 - SGRisk submitted a proposal to Naples Risk Management to provide actuarial services for the Community Residence Self-Insurance Saving Plan (“CRISP”), a group self-insured trust for employers providing community services.

October 31, 1995 - Organizational meeting held in Albany, New York to form the Community Residence Self-Insurance Saving Plan (“CRISP”), a group self-insured trust for employers providing community services. In attendance were Morton “Morty” Case, Patricia “Pat” Hoffman, and Marshall Krassner from The Alliance Group; Janice Johnson, Sidney Paul, Steven Greenfield, and Janice Anderson serving as the initial Trustees; Thomas Arney and John Conroy of PRM; David Johnson, CPA; Thomas J. Gosdeck, Esq. of Hill & Gosdeck LLC; and representatives of Chase Manhattan Bank. Trustees approve a Trust Agreement, Indemnity Agreement and By-laws, and appoint Janice Johnson, David Johnson, and Thomas Gosdeck as the Trust’s Chair, accountant, and legal counsel, respectively. The Trustees also approve contracts for PRM and The Alliance Group to provide program administration and marketing services, respectively. Gallagher Bassett Services, Inc. is retained as the Trust’s third-party claims administrator. Trustees agree on a conservative investment program whereby investments would initially be in “relatively short term instruments having no more than three years to maturity.”

December 11, 1995 - Arney submits application for group self-insurance for CRISP to the WCB.

December 14, 1995 - WCB Chair approves CRISP as group self-insurer, effective December 15, 1995.

December 15, 1995 - CRISP begins operation as group self-insurer.

January 12, 1996 - Trustees approve document relating to \$170,000 no interest loan from MPA (Hoffman and Case) to Trust as “start-up funds.”

February 8, 1996 - Trustees advised that MPA loan has been repaid in full.

September 19, 1996 - Trustees approve loss control proposal from PRM that includes a \$2,500 monthly fee for site visits where standards were to be “measured.”

February 6, 1997 - CRISP’s auditors, Marvin & Co., conclude that CRISP’s financial statements for the period ended November 30, 1996, were presented fairly, in all material respects. The report noted a member deficiency of (\$258,163).

June 27, 1997 - PRM Claim Services, Inc. (“CSI”) registers as a domestic business corporation with the New York State Department of State - Division of Corporations.

February 4, 1998 - CRISP’s auditors, Marvin & Co., conclude that CRISP’s financial statements for the period ended November 30, 1997, were presented fairly, in all material respects. The report noted a member deficiency of (\$232,047).

May 1, 1998 - Trustees approve to add 30% equities to Trust’s overall investment portfolio.

July 30, 1998 - Chair asks Trustees to “consider some compensation for Trustees due to the time demands and liability risks assumed by the Trustees” and suggesting that “...there be a level of compensation paid to Trustees as a reflection of the seriousness of the duties of the Trustees.” Arney directed by Trustees to “undertake an informal review of this issue with other program administrators.” Arney presents proposal to Trustees for CSI to assume Trust’s claims administration, however, Trustees retain Gallagher Bassett.

November 1, 1998 - CSI appointed as third-party claims administrator for HCPSIT.

November 18, 1998 - Gosdeck begins tenure as CSI’s Qualifying Officer.

December 9, 1998 - Trustees unanimously approve that, effective January 1, 1998, Trustees be compensated \$750 for each in person Trustee meeting, the Secretary-Treasurer be compensated \$1,000 per year, and the Chairperson be compensated \$2,000 per year. Trustees further approve that “for Trustees who are employed by a not-for-profit organization, the compensation be paid to such organization and, for all other trustees, it shall be paid to the Trustee.”

January 20, 1999 - CRISP’s auditors, Marvin & Co., conclude that CRISP’s financial statements for the periods ended November 30, 1997 and November 30, 1998, were presented fairly, in all material respects. The report noted a member deficiency of (\$322,246).

March 9, 1999 - Trustees approve Arney's/PRM's receipt of commissions for the purchase of excess and other insurance on behalf of the Trust.

October 22, 1999 - Arney presents result of RFP for third-party claims administration. Trustees agree to retain Gallagher Bassett Service.

January 14, 2000 - CRISP's auditors, Urbach Kahn & Werlin, PC, conclude that CRISP's financial statements for the period ended November 30, 1999, were presented fairly, in all material aspects. The report noted a member deficiency of (\$322,386).

September 22, 2000 - Trust has 194 Members.

October 25, 2000 - Arney requests an increase to PRM's loss control fee from \$2,500 to \$5,000 per month. Trustees unanimously approve this request. The fee remained at \$5,000 per month through the end of the Trust.

October 31, 2000 - Trust executes new contract with MPA for Marketing Services through October 31, 2005.

November 15, 2000 - Tillinghast-Towers Perrin ("TTP") issues report relating to Gallagher Bassett's claims administration. TTP concludes "The quality of overall claim handling provided was generally unsatisfactory as compared to similar third-party administrators handling workers compensation claims."

January 19, 2001 - CRISP's auditors, Urbach Kahn & Werlin, PC, conclude that CRISP's financial statements for the periods ended November 30, 2000 and November 30, 1999, were presented fairly, in all material aspects. The report noted a member deficiency of (\$3,247,002). Note 10 addresses Trust management's plans to address the deficiency, including new underwriting guidelines, replacing the Trust's third-party claims administrator, and changing one of the Trust's investment advisors.

January 31, 2001 - Effective date of new WCB regulations.

February 22, 2001 - PRM presents TTP report on Gallagher Bassett. CSI makes presentation to Trustees to assume claims administration services. Trustees approve CSI as new claims administrator. Trustees replace Chase with Merrill Lynch as Trust's investment manager.

May 1, 2001 - Agreement for CSI claims administration signed by Chair Johnson and Arney through November 30, 2002.

May 10, 2001 - Trust has 217 Members.

May 24, 2001 - Chair introduces Edward Sorenson as PRM's new primary contact with CRISP and advises Trustees that PRM and MPA have reduced their commissions to 5% (from 6.25%) each due to Trust's financial problems.

October 26, 2001 - Trustees approve TTP to perform audit of CSI's claims administration practices.

November 30, 2001 - Trust bills Members a surcharge of approximately \$1,503,000. Most Members promptly pay their assessments with a few Members declining to pay. During March 2003, Trust initiates legal action against six former Members to recover a surcharge receivable of \$533,079, reaches settlements with five of these members for \$241,100, and determines the remaining funds due to be uncollectible.

January 11, 2002 - CRISP's auditors, Urbach Kahn & Werlin, PC, conclude that CRISP's financial statements for the periods ended November 30, 2001 and November 30, 2000, were presented fairly, in all material aspects. The report noted a member deficiency of (\$4,630,560). Note 10 addresses Trust management's plans to address the deficiency including implementation of new underwriting guidelines, replacing the Trust's third-party claims administrator on May 1, 2001, changing one of the Trust's investment advisors, and issuing a Member assessment in the amount of \$1,503,000 on November 30, 2001.

January 29, 2002 - TTP issues report relating to CSI's claims administration. TTP concludes "The quality of overall claim handling provided compares favorably to that of similar third-party WC claim administrators and is close to a best practices level... PRM utilized a team approach to integrate the GBS claims into the PRM process and was successful in achieving a smooth transition."

March 13, 2002 - WCB prepares a Summary of Funding Status as of November 30, 2001 for CRISP reporting a regulatory deficit of (\$7,309,905) and equity ratio of 24.86%. WCB notes that "an acceptable range of loss reserves was not presented in the actuarial report."

April 23, 2002 - WCB suspends addition of new members into the Trust, effective immediately.

May, 2, 2002 - WCB denies PRM request to lift new member suspension.

May 17, 2002 - Sorenson meets with WCB officials. Parties agree TTP will conduct an actuarial review of CRISP and that a fiscal review will be undertaken by an accounting firm. The Member freeze will remain in effect until the reports are completed and further remediation can be discussed.

January 1, 2003 - PRM and CSI sold by Arney to PRM's senior management - John M. Conroy, President; Edward A. Sorenson, Executive Vice President; Colleen E. Bardascini, Senior Vice President; and Gail S. Farrell, Senior Vice President.

March 27, 2003 - TTP issues findings Actuarial Evaluation of CRISP as of November 30, 2002. TTP finds the “deficit position of the trust to be roughly \$5.3 million as of 11/30/02” and “(r)ates and deviations used by CRISP as of 12/1/02 appear to be inadequate by roughly \$0.2 million.”

March 28, 2003 - CRISP’s auditors, Urbach Kahn & Werlin, PC, conclude that CRISP’s financial statements for the periods ended November 30, 2002 and November 30, 2001, were presented fairly, in all material aspects. The report notes a member deficiency of (\$5,728,199). Note 10 addresses Trust management’s plans to address the deficiency. Note 11 addresses management’s plans to take legal action against six former members to recover an outstanding assessment receivable of \$533,079.

May 29, 2003 - Trustees agree to reduce meeting fee to \$500 in light of the Trust’s deficit position, with the exception of the Chair.

May 29, 2003 - Trustees unanimously authorize “the continuing option to utilize retention plans in appropriate cases that meet trustee standards and directed counsel to review the existing contract to ensure that the retention plan contract adequately protects the Trust.”

December 22, 2003 - WCB issues final Summary of Funding Status as of November 30, 2002, for CRISP reporting a regulatory deficit of (\$7,108,575) and equity ratio of 43.45%.

December 2003 - PricewaterhouseCoopers (“PwC”) issues report concurring with SGRisk, Inc.’s actuarial calculation as of November 30, 2002, but finds that the range provided of \$9.4 million to \$11.5 million is “too wide.” PwC suggests a range between \$10 million and \$11 million and proposes a \$700,000 increase in reserves. PwC further indicates that based on the significant members' deficit reported in the audited financial statements and continued losses being reported, PwC would have “considered issuing a going concern opinion on this entity and may not have come to the same conclusion as the audited financial statements represent.” PwC also notes that the Trust’s 43% funded status and \$7,108,575 deficit would be less had paid indemnity assessments been accrued.

January 2004 - Trust ceases admitting new Members into Trust’s Retention Program.

January 12, 2004 - Sorenson disputes PwC’s findings in a letter to the WCB.

March 25, 2004 - CRISP’s auditors, Marvin & Co. PC, conclude that CRISP’s financial statements for the period ended November 30, 2003, were presented fairly, in all material aspects. The report notes a member deficiency of (\$5,365,964). Note 10 addresses settlement agreements with three former members recovering \$149,100 of outstanding assessment receivables. Note 11 addresses Trust management’s ongoing plans to address the deficiency and notes the Trust is deemed underfunded as it relates to New York State regulations.

July 2, 2004 - WCB issues Level I Review for the year ended November 30, 2003 reporting the Trust having a regulatory deficit of (\$7,535,415) and equity ratio of 40.02%. The WCB deems the Trust underfunded.

August 2, 2004 - Trust enters into a Consent Agreement with the WCB that, inter alia, eliminates discounts for new members, limits discounts to only ten renewing members of up to 10%, and prohibits the addition of new members for 12 months.

February 3, 2005 - CRISP's auditors, Marvin & Co. PC, conclude that CRISP's financial statements for the periods ended November 30, 2004 and November 30, 2003, were presented fairly, in all material aspects. The report notes a member deficiency of (\$3,205,064). Note 10 addresses the settlement agreements with two former members recovering \$92,000 of outstanding assessment receivables and that the remaining \$81,617 has been deemed uncollectible. Note 11 addresses Trust management's ongoing plans to address the deficiency and notes the Trust is deemed underfunded as it relates to New York State regulations.

March 7, 2005 - Trust has 231 Members.

June 1, 2005 – The WCB issues Level I Review for the year ended November 30, 2004 reporting the Trust with a regulatory deficit of (\$3,205,064) and an equity ratio of 53.50%. The WCB deems the Trust underfunded. The WCB identifies four equity securities which are not from American Institutions.

July 27, 2005 - Trustees unanimously approve to increase Chair Johnson's stipend to "\$1,000 per month in lieu of all other compensation paid by the Trust..."

March 1, 2006 - CRISP's auditors, Marvin & Co. PC, conclude that CRISP's financial statements for the periods ended November 30, 2005 and November 30, 2004, were presented fairly, in all material respects. The report notes a member deficiency of (\$999,299). Note 11 addresses Trust management's ongoing plans to address the deficiency and notes the Trust is deemed underfunded as it relates to New York State regulations.

April 20, 2006 - Trust has 361 total members of which 252 are active and 109 are inactive.

May 10, 2006 - Trust enters into a Consent Agreement with the WCB that continues restricted growth and discounts to Members.

May 18, 2006 - Trustees stipend restored to \$750 per meeting.

June 15, 2006 – The WCB issues Level I Review for the year ended November 30, 2005 reporting the Trust with a regulatory deficit of (\$3,359,919) and an equity ratio of 67.06%. The WCB deems the Trust underfunded. The WCB notes reserves estimates from prior year decreased by \$500,000 or 6%. The WCB identifies ten equity securities which are not from American Institutions.

December 1, 2006 - Trustees replace SGRisk with By the Numbers Actuarial Consultants (“BYNAC”) as the Trust’s actuary.

December 13, 2006 - Chair advises Trustees that PRM and MPA are back on full 6.25% commission.

March 22, 2007 - CRISP’s auditors, Marvin & Co. PC, conclude that CRISP’s financial statements for the periods ended November 30, 2006 and November 30, 2005, were presented fairly, in all material respects. The report notes a member deficiency of (\$180,425). Note 11 addresses Trust management’s ongoing plans to address the deficiency and notes the Trust is deemed underfunded as it relates to New York State regulations.

March 30, 2007 - Trust has 383 total members of which 260 are active and 123 are inactive

June 13, 2007 - PwC issues to the WCB an Analysis of Trust’s Actuarial Report. The report states the Trust’s recorded reserves were 5% below actuarial indications.

August 20, 2007 – The WCB issues Level I Review for the year ended November 30, 2006 reporting the Trust with a regulatory deficit of (\$3,087,837) and an equity ratio of 75.90%. The WCB deems the Trust underfunded. The WCB identifies 16 equity securities which are not from American Institutions.

March 10, 2008 - Trust enters into a Consent Agreement with the WCB that opens the Trust to a maximum of 30 new Members, commits the Trust to take action to achieve breakeven status for Contribution Year 2008, including issuing a supplemental bill to its Members if necessary, and requires the Trust’s submission of uncertified financial reports to the WCB on a quarterly basis.

March 11, 2008 - CRISP’s auditors, Marvin & Co. PC, conclude that CRISP’s financial statements for the periods ended November 30, 2007 and November 30, 2006, were presented fairly, in all material respects. The report notes a member surplus of \$119,304. Note 11 addresses Trust management’s efforts to eliminate the deficiency and notes the Trust remains underfunded as it relates to New York State regulations.

March 11, 2008 - Trustees discuss need for a succession plan from MPA. Case and Hoffman agree to “work on a plan for discussion at the next Trustee meeting.”

April 15, 2008 - Trust has 421 total members of which 283 are active and 138 are inactive.

May 19, 2008 – The WCB issues Level I Review for the year ended November 30, 2007 reporting the Trust with a regulatory deficit of (\$1,391,295) and an equity ratio of 89.61%. The WCB deems the Trust to have no funding issues. The WCB identifies 17 equity securities which are not from American Institutions.

June 2, 2008 - Trustees unanimously approve an increase in Chair Johnson's compensation to \$3,000 per month and Gosdeck's to \$2,500 per month, effective April 1, 2008.

June 13, 2008 - Trust and the WCB enter into a Memorandum of Understanding ("MOU") removing the "conditions and restrictions" imposed by the March 10, 2008 Consent Agreement and Consent Order. This agreement states, in part, that a supplemental assessment bill will be sent to Members not later than April 30, 2009, for any deficits occurring in the 2007/2008 Contribution Year.

June 30, 2008 - Governor David Patterson creates a Task Force on Group Self-Insurance to examine the reasons for defaults by a number of group self-insurers and to assess the long-term viability of the group model.

October 27, 2008 - Gosdeck emails a member of the Governor's Counsel's Office, recommending Chair Johnson's appointment to the Governor's Task Force.

November 19, 2008 - Lloyd's, London issues E&O policy to MPA for the period August 26, 2008 to August 26, 2009. Policy's limit of liability is \$1,000,000 per occurrence and \$1,000,000 in the annual aggregate, or 50% less than the required coverage limits set forth in MPA's Marketing Agreement.

November 30, 2008 - Trust has 430 total members of which 272 were active and 158 were inactive.

January 23, 2009 - Chair Johnson notes that "over the past year, the CRISP Board has asked Case and Hoffman to deliver a succession plan." Case informs Trustees that he "was unprepared to offer a plan at this time." Chair Johnson asks MPA to have specific information regarding their succession plan for the March meeting.

April 17, 2009 - Chair Johnson, Gosdeck, and group of Trustees meet with Hoffman at Johnson's apartment to address MPA's proposal to form a safety group.

May 29, 2009 - Trustees unanimously approve that the Trust compensate Chair Johnson \$6,000 per month for her services on the Governor's Task Force, retroactive to April 2009, thereby increasing Johnson's total compensation from the Trust to \$9,000 per month. Trustees discuss succession-planning issues with MPA and the renewal or non-renewal of the Marketing Agreement. Trustees approve July 31, 2009, as the new "drop dead" date for the Trust to advise MPA that the Trust was electing not to renew its contract.

May 29, 2009 - CRISP's auditors, Marvin & Co. PC, conclude that CRISP's financial statements for the periods ended November 30, 2008 and November 30, 2007, were presented fairly, in all material respects. The report notes a member deficiency of (\$1,826,333). Note 11 addresses Trust management's ongoing plans to address the deficiency and notes the Trust is deemed to have no funding issues as it relates to New York State regulations.

June 5, 2009 – The WCB issues Level I Review for the year ended November 30, 2008 reporting the Trust with a regulatory deficit of (\$3,583,470) and an equity ratio of 75.15%. The WCB deems the Trust underfunded. The WCB identifies 38 new purchases of foreign equities in 2008.

July 23, 2009 – The WCB meets with PRM and the Trustees to discuss the continuing deficit problem and remedial steps necessary to maintain the Trust’s solvency.

September 28, 2009 - Trustees vote unanimously to “support a surcharge of the deficit over a period of years if mandated by the WCB with PRM to provide options to the trustees.” Trustees also unanimously approve an increase to Gosdeck’s monthly compensation by \$1,500 retroactive to July 1, 2009, raising his monthly compensation from the Trust to \$4,000.

November 1, 2009 - PRM assumes Trust’s marketing rights from MPA via written agreement.

November 30, 2009 - Trust has 447 total members of which 265 are active and 182 are inactive.

January 2010 – The WCB identifies reserving problems with HCPSIT, another PRM-administered trust. The WCB retains KBM Management, Inc. (“KBM”), a third-party claims audit firm, to perform an “expeditious” quality assurance claims audit of the case basis reserves recorded on CRISP claims processed by CSI.

February 2010 - KBM issues report to the WCB identifying reserving deficiencies and administrative problems with CSI claims handling. KBM notes reserves of sampled case files had been increased by CSI just prior to the audit.

February 17, 2010 - Trustees approve Towers Watson (“TW”) to perform an independent case reserve assessment.

February 25, 2010 - Trust enters into a Consent Agreement with the WCB that includes a deficit reduction plan, providing estimates for contributions and expenses for the 2009-10 fiscal year. Plan also provides for Trust to achieve break-even for 2009-10 year, as well as a profit from which \$650,000 will be used to reduce the existing regulatory deficit. Failure to achieve the surplus indicated for Contribution Year 2010 will be cause for the WCB to close the Trust.

March 9, 2010 - TW issues report to Trustees. TW finds CSI’s reserving philosophy not consistently being applied and confirms case reserve increases by CSI in January and February 2010.

March 12, 2010 - Chair and Trust Counsel speak with Ed Sorenson and Gail Farrell from PRM/CSI and inquire about audit deficiencies. Farrell acknowledges audit’s findings and offers no explanations.

March 24, 2010 - Trustees discuss TW audit findings. Sorenson advises Trustees he will no longer support Farrell's and another CSI staff member's role in claims reserving and presents a 45-day remediation plan to the Trustees.

March 29, 2010 - CRISP's auditors, Marvin & Co. PC, conclude that CRISP's financial statements for the periods ended November 30, 2009 and November 30, 2008, were presented fairly, in all material respects. The report notes a member deficiency of (\$2,158,238). Note 11 addresses Trust management's ongoing plans to address the deficiency, including charging 5% for NYS Assessments and increasing rates for most employee classifications, and notes the Trust is deemed underfunded as it relates to New York State regulations.

April 12, 2010 - Gosdeck resigns as CSI's Qualifying Officer.

April 27, 2010 – The WCB issues a Level I Report for the year ended November 30, 2009 and deems the Trust underfunded with a regulatory deficit of (\$7,900,378) and a Trust equity ratio of 57.88%. The WCB reports Trust's purchase of additional foreign equities.

June 2010 - TW issues follow-up report to Trustees relating to reasonableness of case reserves. TW concludes: "The total variance (indemnity and medical reserves) between CRISP's case reserves and Towers Watson's recommended case reserves is 14.7%. We consider plus or minus ten percent (10%) a reasonable level of difference. However, this is a small sample specifically selected to test the philosophy and methodology."

July 12, 2010 - Trustees vote unanimously to engage counsel to pursue Errors and Omissions ("E&O") claims against CSI. Trustees also advised of special claims review undertaken at the Trust's request. 338 indemnity files were examined resulting in a "total increase in incurred of \$4,941,240."

August 1, 2010 - Trust executes contract with PMA Management Corp. ("PMA"), to provide third-party claims administration for the Trust, replacing CSI.

August 5, 2010 - Sorenson submits to the WCB "a plan of revenue enhancement and deficit reduction" that includes the immediate upward adjustment of all class rates by 5% applied to all renewals on a monthly basis, an increase in the NYS Assessment charge levied to CRISP Members to the full 14.2% NYCIRB published in October 2009, and an increase in the assessment charge to 18.1% effective October 1, 2010.

October 31, 2010 - Trustees unanimously approve for CRISP to cease providing Workers' Compensation coverage effective December 31, 2010, and to enter run-off. Trustees direct Sorenson to notify all Members accordingly on November 1, 2010, and to continue work on alternative programs.

November 1, 2010 - Trust advises Members via letter of Trust's closure.

December 31, 2010 - Trust ceases providing Workers' Compensation coverage for new claims.

January 10, 2011 - PRM reports to Trustees that all Members had obtained alternative coverage and that about \$15 million was needed to fully run-off Trust expenses. Trustees unanimously approve an assessment of \$7.5 million and an interest charge of ½ of 1 % per month interest for installments subject to WCB approval. Trustees also unanimously approve continuation of Johnson's and Gosdeck's "compensation at the current rate pending further discussion on July 1, 2011." Trustees advised that Trust has entered into an agreement with PRM for \$9,000 per month for the services of Sorenson and assistant Mark Crawford to help administer the Trust's run-off.

March 10, 2011 - Trustees unanimously approve a Member assessment in the amount of \$15 million.

May 13, 2011 - PRM reports to the Trustees that approximately \$300,000 in assessments had been collected in the first thirty days.

May 13, 2011 - CRISP's auditors, Marvin & Co. PC, conclude that CRISP's financial statements for the period ended December 31, 2010, were presented fairly, in all material respects. The report notes a member deficiency of (\$11,113,227). Note 12 addresses cessation of the Trust. Note 13 reports as assessment billing of \$14,965,000 to Members.

May 3, 2011 – The WCB issues a Level I Report for the year ended December 31, 2010, and deems the Trust underfunded with a regulatory deficit of (\$24,256,049) and a Trust equity ratio of 25.77%.

May 27, 2011 - Trustees file civil suit against PRM, CSI, and MPA.

June 9 and June 10, 2011 - Chair Johnson and Trust Counsel Gosdeck hold Member meetings in Albany and New York City, respectively.

June 17, 2011 - Chair Johnson sends memorandum to Members summarizing Member meetings and subsequent events. Johnson asks Members to advise her as to what amount they could pay toward their assessment by the end of July.

June 23, 2011 - Teleconference held between CRISP and WCB representatives. Chair Johnson expresses concern about PRM's performance and discusses Trust's assessment efforts. The WCB advises Trustees funds were insufficient to continue operation by the Trustees and that transfer process would begin "today."

June 28, 2011 – The WCB advises Trustees and PRM by letter that CRISP "has demonstrated an inability to properly administer its liabilities" and that the WCB will assume administration of the Trust, effective August 1, 2011.

June 28, 2011- Chair Johnson sends letter to Governor Andrew Cuomo questioning the WCB's decision to take over the Trust.

August 9, 2011 - CRISP run-off transferred by the WCB to NCAComp.

January 9, 2012 - Trust's civil complaint against PRM, CSI, and MPA "dismissed without prejudice to any future action" in State Supreme Court, County of Albany.

II. OBSERVATIONS

A. Trust Formation

The New York State Laws governing the formation of group self-insured trusts indicate that the group self-insured trust be formed by a group of employers in a similar industry. The Trust was formed on or about October 1995 through the joint efforts of Thomas B. Arney, President of Program Risk Management, Inc.⁸, Thomas J. Gosdeck, Esq. of Hill & Gosdeck LLC, Priscilla "Pat" Hoffman and Morton "Morty" Case of MPA, and an interested group of community service providers, including Janice Johnson, then Treasurer for the New York City YWCA's Board of Directors. Interestingly, Arney and MPA were the primary parties who discussed the formation of the Trust, not the group service providers. In fact, the Trust creation documents were not even drafted or formulated by the group service provider's representatives.

BST interviewed Ms. Janice Johnson who served as Chair of the Trust's Board of Directors for the Trust's duration. Ms. Johnson is a CPA licensed in the State of Mississippi and holds a Juris Doctor degree. At the time of the interview, Ms. Johnson was self-employed as a financial services consultant. Concerning the Trust's formation, Ms. Johnson said it was her understanding that the Trust was initiated by Thomas Arney from PRM, Hoffman, and Case. She recalled being approached by Hoffman, a partner with MPA, a New York City-based insurance brokerage firm about working on a project to save charities money on workers' compensation insurance. She previously knew Hoffman through a church group in New York City.

She was invited to a meeting with Hoffman, Case, and Marshall Krassner along with other social service provider representatives, and possibly Thomas Gosdeck, Esq. After this initial meeting, she recalled attending a meeting at the Fort Orange Club in Albany where she signed various Trust documents. It was her understanding these were prepared by Gosdeck.

Ms. Johnson said she had "zero knowledge" of workers' compensation insurance when she became involved and relied on the expertise of Gosdeck, Hoffman, Case, and Arney. However, she acknowledged understanding the joint and several liability aspect of the Trust from the beginning.

⁸ On July 25, 1995, Program Risk Management, Inc. was registered as a domestic business corporation with the New York State Department of State - Division of Corporations.

BST interviewed Gosdeck at his Albany law office. Gosdeck served as the Trust's Counsel for the Trust's duration. He stated that he was contacted by Arney and Case in or around 1995 about setting up a trust for human services providers. He knew Arney from some previous trust work and had performed due diligence on Arney's firm in relation to another trust. He did not know Case at the time.

Gosdeck said he was formerly the Counsel and Trustee to the Health Care Providers Self-Insurance Trust ("HCPSIT")⁹ also administered by Arney¹⁰ and PRM, but he resigned from that role after a year.¹¹ He said his firm is a lobbyist for the Group Self-Insurance Association of New York ("GSIANY"), but he was not involved in GSIANY's formation. He noted that his role as the Trust's Counsel involved the drafting of the Trust formation documents, advising the Trust on legal issues, and ensuring the Trust's compliance with WCB regulations. Gosdeck also drafted the minutes of all Trustee meetings, subject to Trustee approval.

Gosdeck's detailed minutes reflect that the aforementioned Fort. Orange Club meeting occurred on October 31, 1995. In attendance were Trustees Janice Johnson, Sidney Paul, Steven Greenfield, and Janice Anderson; Thomas Arney and John Conroy of PRM; David Johnson, CPA of Roth & DeChants, CPA's; Thomas Gosdeck, Esq.; Morton Case, Pat Hoffman, and Marshall Krassner of The Alliance Group¹², and three representatives from Chase Manhattan Bank.

Concerning the Trust's genesis, Case and Hoffman, through their legal counsel, advised BST that in 1995, MPA had a client base for insurance in the non-profit residential social service community, and there was no established promulgated rate for workers' compensation insurance for this group of employers. MPA was exploring suitable alternatives to provide the statutory coverage at an appropriate rate and learned about the group trust alternative. MPA was referred to Thomas Arney "as the person most knowledgeable as to the rules and regulations relating to W.C. in general and the trust option in particular." Case, Hoffman, and Marshall Krasner (reportedly then an executive with Alliance Insurance) met with Arney, and in subsequent meetings "there evolved the idea of a Trust to serve the nonprofit residential social service community needs for a W.C. group payment alternative." Case and Hoffman described Arney as being the Trust's "architect."

Minutes for the October 31, 1995 meeting report that Gosdeck presented, and the Trustees approved, the Trust Agreement¹³, Indemnity Agreement, and By-laws (see Exhibits 1-3) -

⁹ BST previously performed an in-depth forensic review of HCPSIT on behalf of the WCB.

¹⁰ Arney actively participated in the formation of HCPSIT in September 1992 while working for Jardine Insurance Brokers New York. Arney formed PRM on July 25, 1995, and PRM was appointed HCPSIT's administrator on August 1, 1995.

¹¹ This is confirmed by HCPSIT minutes for February 1994.

¹² The Alliance Brokerage Corp. was a firm affiliated at the time with MPA.

¹³ The 1995 Trust and Indemnity Agreements were signed by Trustees Janice Johnson, Steve Greenfield, Janice Anderson, and Sidney Paul. The Trust Agreement does not mention which members the Trustees were representing.

drafted by Gosdeck. The Trustees further discussed and elected not to assign seats on the Board of Trustees on the basis of trade association membership. The Trustees did approve that Members must belong to the Association of Community Living (ACL).¹⁴

The Trustees elected Janice Johnson as Chair and Steven Greenfield as Secretary, and appointed Gosdeck as Trust counsel and David Johnson as Trust accountant. The Trustees also approved service contracts for PRM and MPA to serve as the Trust's program administrator and exclusive marketing representative, respectively (see Exhibits 5-6). The Trustees also discussed a proposed contract with Gallagher Bassett to perform the Trust's claims administration function. It appears these appointments were made on the basis of personal and/or past relationships instead of active solicitation and review of competitive costs proposals usually suggested by prudent individuals acting in a fiduciary capacity.

Arney presented, and the Trustees approved, an "Errors & Omissions" insurance policy.¹⁵ The Trustees also adopted a conservative investment program with short-term instruments. Minutes further reflect that Arney made a presentation of the Trust's operations and allocation of responsibility among the various entities and informed the Trustees that "all community residences are eligible for membership in line with underwriting criteria that will look beyond strict financial data and will include a remedial process in which applicants may be brought up to minimum standards for participation."

Trust records show that on December 11, 1995, Arney transmitted an Application for Group Self-Insurance (GSI-1), Agreement and Undertaking of Employer Group as a Self-Insurer (GSI-3), and other required documents to WCB for review and approval. Seventeen (17) community agencies were identified as initial Trust participants. In correspondence dated December 18, 1995, the WCB sent to Arney a Notice of Qualification for CRISP as a group self-insurer, effective December 15, 1995.

Records and interviews indicate that Hoffman and Case loaned the Trust \$170,000 as "start-up funds" to facilitate the Trust becoming operational. The loan was approved by the Trustees on January 12, 1996, and executed via a loan agreement dated the same date. Trustee minutes for February 8, 1996, report that the loan had been repaid in full. The loan agreement contained no provision for the payment of interest, and there is no evidence that the Trust paid interest on the loan. Chair Johnson confirmed to BST that the loan was repaid, but she did not recall if interest had been paid. Case and Hoffman indicated the loan was repaid in full without interest.

Trust records indicate that by the end of January 1996, the Trust had attracted 35 Members and by the end of 1996, that number had increased to 106.

A space provided for Trustee Albert Brayson II's signature was unsigned on both documents. The By-Laws were unsigned.

¹⁴ The ACL's website www.aclnys.org notes that the statewide organization not-for-profit agencies that provide housing and rehabilitation services to people diagnosed with serious and persistent psychiatric disabilities.

¹⁵ It is believed this was actually a Directors and Officers policy.

B. Board of Trustees

Trustee meeting minutes indicate that seventeen (17) community agency or organization representatives served as Trustees during the Trust's tenure.¹⁶ Janice Johnson served as Chair for the Trust's duration. Four (4) Trustees were appointed at the Trust's inception, according to Trust records.

In addition to Chair Janice Johnson, BST interviewed three (3) additional Trustees - Ann Hardiman (Secretary/Treasurer), Antonia "Toni" Lasicki, and Dr. Peter Campanelli about their roles as Trustees, Trust operations, interactions with PRM, MPA, and other Trust consultants, and their understanding of their fiduciary duties. Chair Johnson and Trustees Hardiman and Lasicki were interviewed in person and Trustee Campanelli was interviewed by phone. All Trustees granted BST extensive interview time and each appeared to be candid and forthright in their responses to our questions. Input from these Trustees is reflected below, in the appropriate sections of this report.

BST also obtained and reviewed official Trustee meeting minutes for the period October 31, 1995 through July 5, 2011¹⁷, as well as numerous other documents relating to the activities of the Board of Trustees.

As noted above, the CRISP Trust Agreement and By-Laws were executed on October 31, 1995, and provided the framework for the Trust's operation, including the Trustees' duties and responsibilities.¹⁸ These documents were prepared by Gosdeck and presented to the Trustees for approval.¹⁹

Article IV, Section 1 of the original Trust Agreement states: "The operation and administration of the Trust shall be the joint responsibility of a Board of Trustees consisting of five Trustees..."²⁰ Section 2 provided that, with the exception of the terms for the initial Trustees, Trustee terms were to be three years with no Trustee serving no more than two consecutive three-year terms. The 2003 amended Trust Agreement allowed for the extension of Trustee service when "...the Board of Trustees shall determine that the best interests of the Trust

¹⁶ WCB records reflect only 12 Trustees serving, suggesting that all Trustees were not reported to or recorded by the WCB. Only one of the five members interviewed recalled the Trustee names.

¹⁷ BST reviewed approximately 80 sets of official minutes.

¹⁸ The Trust Agreement was amended in December 2003, and the By-Laws were amended multiple times.

¹⁹ In 1998, the Trustees independently retained the law firm of Rifken, Frankel & Greenman, P.C. to review Trust documents, and contracts and examine various legal issues. This firm also was retained to assist the Trustees with the Member assessment in 2001. Case and Hoffman advised BST that they had no role in the development of the Trust formation documents. The Trust formation documents - Trust Agreement, By-Laws, and Indemnity Agreement substantially resembled, in both form and substance, the Trust formation documents of the Health Care Providers Trusts with which Arney and Gosdeck were both affiliated.

²⁰ The 2003 amended Trust Agreement eliminated a set number of Trustees allowed to serve and indicated that "In order to reflect changes in the categories of providers entitled to participate in the Trust, the Board of Trustees may from time to time expand the size of the said Board of Trustees." Article IV, Section 1 of the By-laws provides for number of Trustees and their terms.

determine that extraordinary circumstances warrant such an extension of service...” Trust records indicate that this amendment allowed for the continued service of the Chair (15+ years) and other Trustees, such as Trustees Campanelli (14+ years), Hardiman (13+ Years), Lasicki (10+ years), and Anderson (8+ years) to serve beyond the two, 3-year term limitation.

Their lengthy tenures appear to have contributed to the Board of Trustees’ continuity and stability. However, this continuity may have strengthened the personal relationships among the Trustees, making it more difficult for the Trustees to act in a wholly objective manner, especially when it came to matters involving each other and/or the service groups they represented - specifically Chair Johnson’s compensation which is discussed later in the report.

Section 2 also alludes to the appointment of Trustees, but is silent with respect to the appointment process. Minutes reveal that Trustees were elected by the majority vote of the Trustees. Chair Johnson noted that the Trustees were essentially selected by MPA up until near the end of the Trust. She said, in her opinion, MPA’s Trustee selections did not always perform well. Regardless, if this was the case, it would seem that Johnson, as Chair of the Board, should have suggested and/or implemented a better process of selecting potential Trustees.

Concerning the Trustee selection process, Case and Hoffman informed BST that at the meeting in October 1995, MPA introduced five (5) executives from five (5) agencies who would qualify for membership and demonstrated an interest in membership and a willingness to serve on the Board. MPA made these recommendations “based on geographic and industry diversity as well as their personal knowledge of the individuals.” According to Case and Hoffman, the Trustees “selected all future Board Members, always executives of existing CRISP Members or affiliated associates of Trust members.” Case and Hoffman further indicated that the Trust formation documents “contemplated a Board of Trustees which would have limited terms thus revolving leadership.” They added that “... the initial Chairperson remained indefinitely in her position until the Trust was closed and the Workers' Comp. Board stepped in and removed the CRISP Board.”

Case and Hoffman further noted that the “Chairperson lost her initial agency affiliation with a Trust Member. A Board Member then created a nominal affiliation for the Chairperson with a subsidiary of his agency.” In response to this assertion, Johnson advised BST that she resigned as Treasurer of the NYC YWCA in 2003, at which time Dr. Campanelli wanted her to join the ICL Board because of her financial background. She served on the ICL Board for three years. When her term expired, she was appointed to the Board of an ICL affiliate, Joselow House where she stayed until May 2011.

Article IV, Section 7 of the Trust Agreement provides for the election “from among the Trustees a chairman and a secretary of the Board of Trustees” to be elected annually.²¹ The duties of the Chairman and Secretary-Treasurer are specified in Article VII of the By-Laws and acts of the officers are subject to the review and approval of the Trustees.

²¹ Article IV, Section 2 of the By-Laws also provides for the annual election of a Chair and Secretary-Treasurer.

As governance reforms have taken on greater relevance, it has become increasingly more important for boards to find the proper mix of trustees who have the appropriate mix of industry expertise and business perspectives. However, as noted above, Janice Johnson served as Chair for the Trust's duration. Trustee Steven Greenfield served as Secretary-Treasurer from the Trust's inception to May 1997, and Trustee Hardiman immediately assumed that role position and served through the Trust's dissolution. Based on BST's review of Trust documents and interviews, it appears that both the Chair and Secretary-Treasurers took their assigned roles seriously. However, as will be discussed in this report, certain actions taken by the Trustees were not consistent with the authorizing Trust documents or established underwriting criteria.

The failure to set and abide by term limits may have also created an atmosphere which lacked fresh ideas and new perspectives, and limited the diversity of the Board. Despite the apparent sense of commitment, the lack of an orderly Board rotation can create situations of ingrown possessiveness sometimes found on self-perpetuating boards, which does not always promote creativity and innovation during periods of rapid change. Additionally, the lack of term limits can result in stagnation, the concentration of power within a small group, and intimidation of the occasional new member - none of which contribute to the long-term success of any organization.

Furthermore, as certain Board members were compensated, there was little financial incentive to assume a subordinate board position or roll off the board entirely. From a best practice standpoint, and by far one of the most important board development practices, the recruitment and nominations process helps to assure that there is a long-range succession plan for board leadership. The current Trustees and the Trust Counsel failed in their endeavors to strategically address these issues. Their failure to implement a rotation plan was further exacerbated by Chair Johnson's admittance that she had "zero knowledge" of workers' compensation insurance when she became involved (in the trust) and relied on the expertise of others.²²

Article VII, Section 3 of the By-Laws empowers the officers to "to invest and reinvest all funds" of the Trust. This will be discussed in more detail below. Article VIII of the By-Laws makes provision for the Chair to create the following sub-committees: Education and Planning Committee; Accounting, Reserves and Premium Rate Committee; Safety Advisory Committee; and Membership Committee. BST found that no standing committees were formed but that ad hoc committees were established to address topical issues that arose.

Article V, Section 1 of the Trust Agreement provides for Trustee meetings to occur "semi-annually and more often if required."²³ Meeting minutes indicate that the Trustees met in person at least two times a year and conducted additional meetings via conference call as permitted by Section 1. Five or more such meetings per year were not uncommon. Most in person meetings

²² The 2010 Survey Data for Boards of Independent Institutions noted that 64% of independent institutions have term limits.

²³ Article IV, Section 5 of the By-Laws similarly addresses Trustee meeting frequency.

were held at the Union League Club in New York City.²⁴ Section 1 further required that “a quorum shall consist of at least fifty (50) percent of the said Board of Trustees.” Minutes show that official business was conducted only if a quorum was present and matters for vote were deferred when a quorum was not in attendance.

BST found that PRM provided the Trustees with a detailed briefing binder in advance of each Trustee meeting containing financial, claims, insurance, regulatory, marketing and other salient information to be addressed at the upcoming meeting. The material was sent by email in the later years and hard-copies were provided at the meeting. All Trustees interviewed felt that the Trustee meetings were productive and that they had sufficient information at the meetings to make decisions and fulfill their fiduciary duties. However, as will be discussed later the Trustees expressed concern that information provided by CSI regarding claims reserves may have been misleading and inaccurate.

Article V of the By-Laws provides for an annual meeting of the members. Records and interviews show that annual member meetings were held in conjunction with a scheduled Trustee meeting. Member attendance appears to have been minimal with only a handful of member representatives in attendance.²⁵ It is unclear if adequate notice was sent to Members announcing the annual meetings. Despite not being attendance, it does not appear that the Trustees provided the Members with electronic copies of the Trust’s audited financial statements, something that would have alerted the Members to the outstanding member deficit for which they were all jointly and severally liable. Instead, and for the most part, the Members’ insurance agent (MPA) continued to renew their membership in the Trust during which time the member deficit grew, and which amounts to \$32,375,129 (as of October 31, 2012).

In addition, Article V, Section 1 of the Trust Agreement requires the secretary, acting secretary, or his designee to keep minutes of all meetings, proceedings and acts of the Board of Trustees. This task was delegated to Gosdeck who took notes and drafted minutes that were sent to the Trustees for comment. The minutes were reviewed and formally approved by the Trustees at the subsequent meeting. BST found the minutes to be comprehensive, sufficiently detailed and well-written. All Trustees interviewed indicated the minutes presented an accurate summary of the meetings’ proceedings. There is no evidence that the minutes were distributed to the general membership on a regular basis and appear to have been made available only upon member request.²⁶

Article V, Section 1 requires that all actions by, and decisions of, the Trustees be by majority vote of the number of Trustees attending a meeting at which a quorum is present. Minutes and interviews reveal that Board actions were approved only by majority vote and in a majority of instances, the voting was unanimous.

²⁴ Gosdeck advised BST that he arranged for the meetings at the Union League Club which has a reciprocal agreement with the Ft. Orange Club in Albany of which he is a member.

²⁵ None of the Members interviewed recalled attending a general membership meeting. Members interviewed did not recall any regular communications between the Trustees and their agencies.

²⁶ None of the five Members interviewed recalled seeing meeting minutes.

Article V, Section 5 of the Trust Agreement allows the Trustees to designate “a fiscal agent and/or an administrator to administer the financial affairs of the Trust” and requires the fiscal agent and/or an administrator to “furnish a fidelity bond with the Trustees as obligee, in an amount sufficient to protect the Trust against the misappropriation or misuse of any moneys or securities held by or in the name of the Trust.”²⁷ Under this authority, the Trustees designated PRM as the Trust Administrator and available information indicates the Trustees received from them the required fidelity bond. The Trustees’ relationship with PRM and PRM’s performance on behalf of the Trust will be discussed in detail below.

Concerning their assessment of the Trustees’ level and quality of Trust oversight, Case and Hoffman indicated that based on their observations, “...the Trustees generally had a conscientious and careful attitude in providing oversight to the Trust and to its members.” They added that “...the Trustees had no prior directly relevant experience in the operation of a Trust vehicle of this type, and they may have been disadvantaged when Mr. Arney no longer was participating on behalf of PRM.”²⁸ If nothing else, Case’s and Hoffman’s statements reinforce the best practice of rotating board members and limiting terms.

In summary, information obtained by BST suggests that the Trustees appear to have performed most of their fiduciary duties substantially consistent with the Trust documents. There appears to have been good information flow between the Trustees and their consultants and certain Trustee decisions were based on thoughtful evaluation and discussion of information provided by the Trust’s paid consultants. Unfortunately, some of the information furnished to the Trustees may not have been accurate. As will be shown below, the Trustees proactively sought outside legal, claims, and actuarial assistance to aid in their oversight of the Trust and the Trust’s growing deficit position. The Trustees worked increasingly over the years to acquire from PRM more control over the Trust’s operations.

Trustee Compensation

Article V, Section 6 of the Trust Agreement grants the Trustees the authority to “establish, from time to time, a reasonable amount of compensation to cover attendance at meetings of the Board of Trustees and the performance of the normal duties of a Trustee which compensation may include reimbursement for necessary expenses incurred therein.” Pursuant to this authority, the Trustees approved payments to each Trustee as compensation for meeting attendance and to the Trust Chair and Secretary/Treasurer for services rendered on behalf of the Trust. The Trust’s financial statements report fees and travel reimbursements paid to Trustees or their organizations totaled approximately \$420,500 during the life of the Trust.²⁹

²⁷ Article IX provides for the execution of a Management Agreement “with a qualified entity” to perform tasks relating to the operation of the Trust.

²⁸ Case and Hoffman added the following relating to their assessment of the Trustees’ overall performance: “MPA did not ever claim to have the expertise or totality of information required to adequately judge the level and quality of oversight provided by the Trustees to the Trust and its members.”

²⁹ The payment of these Trustee fees is inconsistent with practices of 13 other trusts examined by BST.

Trustee minutes for July 30, 1998 report the Chair asking the Trustees to “consider some compensation for Trustees due to the time demands and liability risks assumed by the Trustees” and suggesting that “...there be a level of compensation paid to Trustees as a reflection of the seriousness of the duties of the Trustees.”³⁰ The Trustees “...expressed a desire to have compensation in line with that paid to the management of other similar organizations” and asked Arney to “undertake an informal review of this issue with other program administrators.”³¹

Minutes for the subsequent Trustee meeting on December 9, 1998 state: “There was consensus that a universal standard be applied to all trustees and a recognition that, while it is unusual for trustees of a not-for-profit organization to be compensated, CRISP is a for profit entity providing services to not for profit organizations and, therefore, compensation was appropriate given the absence of paid staff for the trust.”³² The Trustees unanimously approved that effective January 1, 1998, Trustees be compensated \$750 for each in person Trustee meeting, the Secretary-Treasurer be compensated \$1,000 per year, and the Chairperson be compensated \$2,000 per year. It was further approved that “for Trustees who are employed by a not-for-profit organization, the compensation be paid to such organization and, for all other trustees, it shall be paid to the Trustee.” Interestingly, Chair Johnson was not an employee of her representative member, but rather a consultant who was paid directly.

Trust records show that payments to the Trustees were made in accordance with these provisions. Also, records show that the Chair and Secretary-Treasurer received the meeting attendance fee in addition to their annual compensation.³³ The Trustees and/or their employers continued to receive reimbursement for reasonable and necessary travel expenses.³⁴

Minutes for May 29, 2003 indicate that in light of the Trust’s deficit position, the Trustees, with the exception of the Chair, reduced their per meeting fee to \$500.³⁵

July 27, 2005 minutes report Acting Chair Campanelli explaining to the Trustees that “Janice Johnson, the Chair has been serving for nominal compensation during the past several years and has expressed concerns regarding the amount of time that she has been expending on the Trust’s behalf.” Campanelli further noted that Johnson “has expressed the opinion that the role has become much more expansive than she desired especially since she has no significant management role in an agency,” and that in discussions with Johnson, she “indicated that a stipend of One Thousand Dollars per month would provide her continuing incentive to continue

³⁰ The Trust purchased Director’s and Officer’s insurance to cover Trustee liability.

³¹ BST’s review of 13 other trusts revealed that a significant majority of trustees did not get compensated, and those that did, did not get compensated at this level. It remains unclear who Arney polled, if anyone, to ascertain how much group self-insured trustees received as compensation.

³² PRM was, in actuality, the Trust’s paid staff, as was David Johnson, the CPA hired by the Trust.

³³ The Secretary-Treasurer’s fees were paid to her employer.

³⁴ A representative of the firm providing accounting services to the Trust stated that the certain Trustees were issued 1099’s in relation to the Trustees fees they received. Certain fees were received directly by the organizations represented by the Trustees.

³⁵ Payment records suggest these payments were actually reduced to \$375 per meeting and were subsequently restored to \$750, effective May 18, 2006.

to serve and is, in his opinion, fair given the breadth of her service.” Campanelli suggested to the Trustees that “this compensation be personal to Janice Johnson and not be attached to her role as Chair.” The Trustees unanimously approved Johnson’s stipend to “\$1,000 per month in lieu of all other compensation paid by the Trust...”

Minutes for the Trustee meeting of June 2, 2008 reflect the Trustees’ unanimous approval of an increase in Johnson’s compensation to \$3,000 per month and Gosdeck’s to \$2,500 per month effective April 1, 2008. The minutes further note that “in accordance with a decision reached in an Executive Decision, the increases had been paid in the past two months.” It is unclear who made the “Executive Decision” or the basis for the increase, as the minutes for the previous Trustee meeting held on March 11, 2008, make no reference to a compensation increase.

On June 30, 2008, Governor David Patterson created a Task Force on Group Self-Insurance to examine the reasons for defaults by a number of group self-insurers and to assess the long term viability of the group model. The Governor appointed to the Task Force individuals representing, inter alia, government regulators, unions, business organizations, and group self-insurers. In an email dated October 27, 2008 to a member of the Governor’s Counsel’s Office, Gosdeck recommended Janice Johnson’s appointment to the Task Force. Gosdeck stated, in part:

I think that she would be a great member for the task force
She is a trustee and employed by a participant
She has been chair of the Trust since 1995 and taken it from fully
funded through a bad period when former claims administrators
badly underreserved and back to fully funded status. (sic)

Johnson was subsequently appointed to the Task Force, apparently on the strength of the recommendation from Gosdeck, who also served as the registered lobbyist for the Group Self-Insurance Association of New York (GSIANY).³⁶

Trustee minutes for May 29, 2009 indicate Johnson reporting the activities of the Task Force to the Trustees and asking the Trust “consider compensating her for the extraordinary amount of time involved in the process.” Johnson further suggested that “the Trust, PRM and MP Agency each pay Two Thousand Dollars per month to compensate her.” The Trustees unanimously approved that the Trust pay Johnson \$6,000 per month for her services on the Task Force, retroactive to April 2009. This action increased Johnson’s total compensation from the Trust to \$9,000 per month.

It remains unclear why the Trustees voted to pay Johnson \$6,000/month for services relating to the Governor’s Task Force - something not directly related to her role as Trustee of CRISP. Clearly, the continuity of the Board of Trustees may have played a part in the Board’s approval

³⁶ The Trust was a GSIANY member, paying annual dues ranging from \$1,000 to \$1,500.

process, as it is questionable why any prudent person in a leadership position would commit resources of an underfunded organization to such an endeavor.

Certainly, Johnson should be held to a higher standard for making such a questionable suggestion given the fact that she is a CPA and a non-practicing attorney, and should clearly have recognized that the Trust Members' contributions should not have been used to pay for her role on another Board. She should have reconsidered her commitment to the Task Force before accepting her role, or she should have requested compensation from the Governor or other sources prior to, or subsequent to her acceptance of that position. Gosdeck's ability to advise the Board impartially and exercise his fiduciary duties as Trust Counsel must also be questioned in light of the Trustees' decision to pay Johnson \$6,000/month. His ability to make a decision in the best interest of the Trust may have been compromised by the fact that he may have also been seeking additional compensation for duties as Trust counsel and his role with GSIANY.

For example, the September 28, 2009 CRISP minutes reflect the Trustees' unanimous approval to increase Gosdeck's monthly compensation by \$1,500 retroactive to July 1, 2009, raising his monthly compensation from the Trust to \$4,000/month. On January 10, 2011, after the Trust had been closed, the Trustees unanimously approved the continuation of Johnson's and Gosdeck's "compensation at the current rate pending further discussion on July 1, 2011."

As reflected above, fees paid to the Trustees, Chair, and Counsel increased substantially over the Trust's duration. Trust financial statements show that in 2000, Trustee fees totaled \$13,500 per year, or 0.6% of income. By the end of December 31, 2010³⁷, annual fees had increased to \$131,250, or 1.2% of income, and yet there was no process or policy in place which required Gosdeck or Johnson to document the amount of time they spent on Trust activities or the Governor's Task Force activities. While we did not ask this question of the Trustees, it is hard to imagine that they or their employers would have unilaterally paid consultants \$10,000/month without even asking for any documentation to support the payment, or that they would have approved of such an arrangement without a formal written agreement. The latter situation is even more disconcerting given the fact that both Gosdeck and Johnson have law degrees, and should realize that written agreements are not only a best practice, but also one way of avoiding potential future liability should someone question the nature and terms of an agreement.

The work performed by the Chair, Counsel, and Trustees on behalf of the Trust notwithstanding, BST found their fees to be unusual and inconsistent with the practices of numerous other group self-insured trusts reviewed by BST on behalf of the WCB. As such, BST spoke at length to the Chair, Counsel, and Trustees about the basis for these fees.

Johnson recalled that early on there was a great deal of turnover on the Board as Trustees who were appointed did not want to make the time commitment or lacked the necessary business expertise to properly fulfill their fiduciary duties as Trustees. She believed that experienced

³⁷ This represents a thirteen-month period.

people were needed and recommended that the Trustees' organization receive \$750 for each Trustee meeting.

Johnson indicated that 1099's were provided annually by Dave Johnson to the Trustees or their organizations, including her and confirmed Trustees were reimbursed for travel expenses to and from the meetings. To her knowledge, no Trustee ever declined accepting compensation.

Johnson recalled that her fee was increased to \$3,000 per year as Chair beginning in 1996 or 1997, and that Treasurer Ann Hardiman, who signed all checks, received \$1,000. At some point she indicated that her fee went to \$3,000 per month. She said she was not sure why or when this occurred, but added that her role increased, including more "hands-on" involvement with investments³⁸ and "refereeing fights between PRM and MPA." She was not required to provide an accounting of her time to anyone. She said she spent up to 20 hours per week on Trust business and has "50 pages" of emails to support that assertion.

Johnson stated that effective April 2009, she was given an additional monthly fee of \$6,000 to compensate for her work on the Governor's Self-Insurance Task Force and other Trust matters such as the filing of a lawsuit against MPA and PRM, resolving outstanding claims, and seeking alternative workers' compensation insurance for Members. She said she was spending two days a week in Albany from early 2009 through April 2011. She was not required to submit an accounting of her time to anyone. Johnson indicated that the Task Force was looking for an industry representative, as was GSIANY, and that Gosdeck supported her appointment to the Task Force. She said she was appointed, not as GSISNY's representative, but rather as that of the Trust. When she was appointed to the Task Force she was serving as a member of Joslow House, a related entity to ICL, a Trust member. She felt that PRM, MPA, and the Trust should have shared these costs and that the Trust should not have had to "eat it."

She noted that the \$9,000/month she was receiving from the Trust constituted 50% of her total income. She indicated that her other source of income is approximately \$6,500 per month from a broker/dealer. She added that her time spent on Trust matters prevented her from taking much outside consulting work. She provided BST with a document purporting to show time she spent on Trust matters in June 2011, totaling 152 hours for which she said she has yet to be compensated.

She said that in addition to her fees for June 2011 still being owed to her, she has approximately \$3,500 in expenses on her AMEX card relating to Member meetings she paid for. She also noted that she promised Gosdeck that she would pay him \$1,500 per day to help coordinate the Member meetings. In all, Johnson stated that there remains \$60,000 in outstanding unreimbursed expenses relating to the Trust's closure, including money owed to Dave Johnson, Marvin & Co., and the law firm of Couch White for Trust related work. She added that Gosdeck and Dave Johnson stood with her "side by side" during the Trust's dissolution process.³⁹

³⁸ The Trust engaged and paid two internationally-recognized investment managers. Therefore, the extent to which the Chair could have substantially contributed to the management of the Trust's investments is questionable.

³⁹ We were not provided with any detailed accounting of these reported expenses.

Johnson stated that Gosdeck “knows the business” and was a good choice as Counsel. There is no retainer agreement between the Trust and Gosdeck to her knowledge, and he was paid in accordance with fees set by the Trustees as noted in the minutes. Gosdeck’s invoices were sent to the Trust’s accountant, Dave Johnson, and payment checks were sent to Ann Hardiman for signature. This was confirmed by Hardiman. Johnson felt Gosdeck’s fees were appropriate and that Gosdeck provided the Trustees with good legal advice “to the extent possible.” Johnson added that in her opinion, Gosdeck “didn’t tell us strong enough what WCB expected” from the Trust on a regulatory basis.

Trustee Hardiman indicated that Chair Johnson dedicated a lot of her personal time to the Trust and that paying her some form of compensation was appropriate.⁴⁰ She added that Johnson spent a lot considerable time on the Governor’s Task Force and was a good advocate for the Trust. She characterized Johnson as a “fantastic leader” who did not want to be controlled by the administrator and tried to establish that the Trustees were in charge. It remains to be seen how Hardiman knows that Johnson dedicated “a lot” of her time to the Trust, or how she allegedly knows that Johnson was a “good advocate” for the Trust while serving on the Governor’s Task Force, as no evidence was brought to our attention that indicated that Hardiman participated in or attended the Task Force meetings.

Trustee Lasicki informed BST that Chair Johnson’s compensation was justified by all the work she did, but acknowledged there was no time accounting for the hours Johnson worked. Lasicki also noted that near the end of the Trust, Johnson was working 20 hours per week on the Governor’s Task Force. She said Johnson “represented the industry” on the Task Force and she was comfortable with Johnson’s compensation.

Lasicki’s conclusion that Johnson’s compensation was justified is not based on any first-hand knowledge, as she admittedly acknowledges that there was no time accounting for the hours Johnson allegedly worked. Additionally, this same observation would seem to contradict Lasicki’s assertion that Johnson worked 20 hours per week, as there is no accounting of Johnson’s hours. Once again, Trustees Hardiman’s and Lasicki’s ability to rationalize the payments made to Johnson appear to have been possibly impaired by their long-term continual relationship as Trustees with Johnson. Furthermore, Lasicki fails to provide any justification as to why Johnson deserved \$6,000/month for admittedly “representing the industry” (not the Trust) on the Task Force.

Trustee Campanelli also noted that Chair Johnson spent a large amount of time on Trust business and was able to substantiate this time to the Trustees. He similarly felt that Johnson’s compensation was fair. If what Campanelli says is true, i.e., Johnson was able to substantiate her time, then we must question why this alleged documentation was never produced by Johnson or the Trustees.

⁴⁰ Most, if not all Board members, volunteer personal time to board activities, as their employers do not pay them to serve on volunteer boards.

Gosdeck advised BST that Johnson and the Trustees were “responsible” and treated the Trust as a business.

Gosdeck stated that he felt he acted as a “straight lawyer” and acted appropriately in his role as Counsel. Gosdeck recalled that the Governor’s Office asked him for the name of a good GSIANY person to serve on the Self-Insurance Task Force. Gosdeck said the GSIANY staff was “bare bones” and he felt that Janice Johnson was highly qualified for the Task Force, and he recommended her. At the time she was a Director of ICL. He subsequently spoke to the Governor’s Office and was told Johnson was “heads above” others on the Task Force. Notwithstanding the veracity of this statement, this characterization should be tempered by the fact that Johnson, as a CPA and as Board Chair, supervised a Trust that had a ongoing member deficit. As detailed later in this report, Johnson blamed PRM, MPA, the WCB, and others, yet despite her continued existence as Board Chair, she and the other Trustees continually renewed their business arrangements with PRM and MPA.

Gosdeck confirmed that he was PRM’s registered lobbyist while serving as Trust Counsel. He felt this was not a conflict of interest as his work for PRM was minimal, and PRM never asked him to do anything that would conflict with his duties as Trust Counsel.⁴¹ Gosdeck emphasized that he had attained an AV Rating⁴² and would do nothing to jeopardize his standing in the legal community.

Gosdeck also acknowledged that he was the qualifying officer⁴³ for PRM Claim Services Inc. (CSI) to serve as a claims administrator. He said that PRM had an in-house qualifying officer, and Tom Arney asked him to assume those duties. Gosdeck said he consulted with then WCB Board Chair Bob Snashall who advised him that assuming that role would not be a conflict with his Trust Counsel duties, so he accepted. WCB records show Gosdeck began his tenure as Qualifying Officer on November 18, 1998. Documents provided by the WCB do not reveal any such confirmation that then Chairman Snashall advised Gosdeck that his role would not be a conflict.

Gosdeck told BST that WCB General Counsel Kenneth Munnelly was aware of his role when he (Munnelly) came to the WCB and he spoke to Munnelly about it. When Munnelly asked him to resign from the qualifying officer role, he did so. Trust records contain a letter dated April 12, 2010 from Gosdeck to Munnelly whereby Gosdeck resigned his role as CSI’s Qualifying Officer effective that date (Exhibit 7), and in the letter, Gosdeck acknowledges that “there is a real likelihood that a real or apparent conflict may exist”.

⁴¹ BST identified the lobbying relationship through a review of NYS public lobbying records.

⁴² AV Preeminent Rating is a lawyer peer review rating from Martindale-Hubbell defined as follows: “AV Preeminent is a significant rating accomplishment - a testament to the fact that a lawyer’s peers rank him or her at the highest level of professional excellence.”

⁴³ § 50 3-b/d of the New York State Workers’ Compensation Law requires that a company or corporation applying for a TPA license must have a Qualifying Officer to represent the company or corporation. This individual is responsible for overseeing the company’s conduct at Board hearings and ensuring that the laws and regulations of the Board are being followed. An individual can become a Qualifying Officer by being an attorney admitted to practice in New York or by being an individual who is not an attorney successfully passing a licensed representative examination.

Chair Johnson advised BST that she was unaware until near the end of the Trust that Gosdeck served as PRM's lobbyist, but added that this "didn't distress her." Johnson recalled the Trustees specifically asking Gosdeck early on about who he represented given his role in the self-insurance industry. Gosdeck told them he represented the Trust and the Trustees accepted that. Johnson said she similarly was not aware that Gosdeck was the Qualifying Officer for PRM until near the end of the Trust. Assuming Johnson's statements to be true, BST questions why Gosdeck never told Johnson or the other Trustees earlier about the potential conflicting relationships - especially if Gosdeck reportedly had been advised by the WCB Chair that this was not a conflict. As the Trust's trusted advisor, it would seem that this would have been one of the first things Gosdeck would have told the Trustees, especially given the increasingly constant demand for greater accountability and openness by licensed professionals.

Trustee Lasicki indicated that she knew Gosdeck was a lobbyist for PRM but had no problem with that. She was not aware until recently that Gosdeck was PRM's Qualifying Officer. She felt Gosdeck was "underpaid for years." She believed Gosdeck gave the Trust good legal advice. Overall, she felt CRISP had an "engaged Board" with "astute" Trustees and believed the Trust was "pretty well run." The latter statement appears very self-serving, and it is hard to imagine that the Members feel the same way, given the Trust's multi-million dollar deficit that accumulated during the administration of the Trust by Johnson and the other Trustees.

Trustee Hardiman stated that she was not aware of any conflicts of interest involving Gosdeck who she felt would have disclosed them. She could not recall if she knew that Gosdeck was PRM's lobbyist or Qualifying Officer. Concerning her compensation as Treasurer, Hardiman said she did not submit for meeting travel reimbursement as she received \$750 per meeting that went to her organization, the New York State Association of Community and Residential Agencies (NYSACRA). She later received an additional \$1,000 per year as Secretary-Treasurer which also went to NYSACRA. She said this was discontinued for a time after September 11, 2001, when the Trust was having financial difficulties.

Hardiman said that her duties as Secretary-Treasurer included signing checks, making fund transfers, and signing official documents such as the tax returns. Dave Johnson would prepare the checks and a person from Dave Johnson's office would send over a package with the checks and back-up material. She would review the material and send out the signed checks to the payees using envelopes supplied by Dave Johnson. She provided a sample payment packet to BST that confirmed her statements. BST's review of other trusts found that this work was done by the Trust Administrator and was included as part of the fee paid to the Trust Administrator.

Hardiman said she signed every check except for few signed by Janice Johnson when she was not available. She never signed any questionable checks and would contact Dave Johnson's office before signing anything she questioned. For example, sometimes there was a vendor she did not know, but she called Dave Johnson's office and received clarification before signing. She would sign about 6-10 checks per month, usually all at once. She occasionally would send a signed check back to Dave Johnson's office for mailing when the payment was due later in the month. She made weekly fund transfers by email and provided BST a sample email confirming her statements.

Based on the foregoing discussion, BST offers the following observations about Trustee and Trust Counsel compensation and responsibilities:

- The Trustees approved and received compensation as authorized by the Trust Agreement - which they also approved.
- Additional compensation paid to the Chair may not have been justifiable as her time and activities were not always documented and/or evaluated. Additionally, the Chair's substantial compensation was noticeably inconsistent with compensation received by Chairs of other group self-insured trusts examined by BST.⁴⁴ In the Trust's later years, compensation received by the Chair from the Trust constituted approximately half of her total earned income. BST must also question the Chair receiving substantial compensation without any requirement to specifically account to the other Trustees for time purportedly spent on Trust-related activities.
- Johnson suggested, and the Trustees later approved, the arbitrary payments of \$6,000/month that Johnson believed she deserved for participating on the Governor's Task Force, despite the fact that Johnson was clearly representing the interests of all group self-insured trusts, group administrators, and GSIANY. These substantial costs should not have been borne solely by CRISP as these duties were unrelated to Johnson's role as Chair of the Trust, a role for which she was already being compensated.
- The basis for the \$6,000 monthly fee paid to the Chair for participation on the Task Force cannot be correlated to the work she performed on the Task Force as the Trustees did not require, nor did she maintain, an accounting of time spent on Task Force matters.
- The Trust Counsel's role as PRM's lobbyist and Qualifying Officer should have been disclosed to the Trustees in a timelier manner, and a written opinion should have been sought and saved with regard to whether or not his dual roles presented a conflict of interest. While we did not unearth any evidence that the Trust's Counsel performed his duties in any way other than in the Trust's best interest at all times, his business relationship with PRM appears to have placed him in a conflict of interest situation with his role as Trust Counsel.
- The Counsel played a key role in the formation and operation of the Trust and was paid fees that are reportedly commensurate with his duties. However, there was no written contract with the Trust governing his fees or scope of services, which was not prudent from a legal or fiduciary perspective.

Trust Investments

Article VII, Section 6 of the Trust Agreement and Article VII, Section 3 of the By-Laws empower the Trust to invest surplus Trust funds not needed to meet current obligations. Trust

⁴⁴ The Chairs and Trustees of other trusts examined by BST typically received no additional compensation other than perhaps travel reimbursement even in case where the number of members was substantially greater than CRISP. While more than nominal Trustee compensation can serve as an incentive to devote substantial personal time and energy to a trust's activities, it can also serve as an incentive to make decisions that preserve the ongoing compensation itself, rather than the best interests of the trust, i.e. continuing a trust's operation in the face of mounting financial difficulties rather than aggressively seeking dissolution and viable insurance alternative for members.

records and interviews show that the Trust pursued a conservative investment strategy and that the Trustees, particularly the Chair, were actively involved in the oversight of the Trust's investments. Investments were discussed routinely at Trustee meetings.

We found no formal written investment policy. Johnson confirmed to BST that there was no written investment policy per se, and that the Trust followed WCB's investment guidelines.⁴⁵ She said that the Trust's investments were conservatively invested in CD's, bonds, and small/large cap blue chip investments. She noted that much of the funds were shifted to CD's in 2006 until 2008 that ultimately protected the investments from the economic downturn. Gosdeck noted to BST that the Trustees adopted an investment policy which should be reflected in the minutes. He said a Merrill Lynch representative was at the meetings, and he felt Trust investments performed well during the economic downturn.⁴⁶

The Trustees began discussion of an investment strategy at their very first meeting on October 31, 1995 where representatives of Chase Manhattan Bank made a presentation on investment options for Trust funds. The Trustees agreed on a conservative investment program whereby investments would initially be in "relatively short term instruments having no more than three years to maturity." Records show that in May 1998, the Trust moved to add 30% equities to its overall portfolio. In December 1998, the Trust's accountant "suggested the formation of a small investment committee of the Board," but the Trustees rejected this recommendation arguing that "the Trustees have sufficient contact as a whole." It appears that by mid-2000, an investment committee was established with Chair Johnson assuming the lead role in investment matters and the reporting of such matters to the Trustees.

On October 25, 2000, the Trustees "unanimously agreed to undertake a review necessary to replace Chase as an investment and banking service provider to CRISP." A committee was formed to solicit and interview new providers. Minutes of February 22, 2001 show the Committee interviewed four applicants and recommended "to place all funds with Merrill Lynch but not under the control of a single investment advisor" and to terminate the Trust's relationship with Chase.⁴⁷

Subsequent minutes show that Merrill Lynch representatives periodically attended the Trustee meetings to update the Trustees on investment matters and the status of the Trust's investment portfolio.⁴⁸

⁴⁵ A PwC report for the period ended November 30, 2002, identified the lack of a formal investment policy. In a response to the PwC report, Sorenson challenged this finding and indicated that investment strategies were discussed in the Trustee meetings, voted on, and documented in the minutes.

⁴⁶ The investments had an average balance of approximately \$7.5 million during 2008 and 2009, and the net investment income during those two years averaged \$185,575 for an average return of 2.47%.

⁴⁷ Minutes for January 14, 2005 report that Merrill Lynch representatives reported to the Trustees that their "general commission is approximately 1% of the fund value and that there are no commissions charged on trades. Merrill also noted that it gets no other fees from CRISP other than a commission for the mandated Letter of Credit that the Trust files with the WCB."

⁴⁸ Case and Hoffman asserted to BST that "The Trust employed a securities broker who was the Chairperson's personal friend." Minutes do not reflect any disclosure or discussion of this issue if, in fact, this was the case. Chair

Investments of Trust funds which are not necessary for the payment of short-term obligations are permitted in Section 317.8 of the Worker's Compensation Rules and Regulations as follows:

- Government Obligations
- Obligations of American Institutions
- Preferred Shares of American Institutions
- Equity Interests

Investments are not to exceed 5% of total Trust assets in any one American Institution. In addition, total Investments in American Institutions are not to exceed 25% percent of total Trust assets and those investments must maintain adequate ratings in order to be recognized as an acceptable asset.

Documents reveal that the Trust generally complied with the 5% and 25% limitations; however, the Trust did invest in equity securities which were not from American Institutions contrary to Section 317.8's requirements. As a result, the WCB disallowed these investments, adding to the Trust's regulatory deficit. For example, in 2004 the Trust had four (4) equity investments not from American Institutions resulting in a \$52,355 reduction in recognized Trust assets. Despite this disallowance, the Trust continued to invest in equities not from American Institutions. From 2005-2007, the number of equity investments not from American Institutions was 10, 16, and 17, respectively.⁴⁹ In its Level I reports for the periods ended November 30, 2006 and November 30, 2007, the WCB recommended "The Board of Trustees should take immediate steps to prevent the Trust from purchasing any more foreign investments." In its report for 2008, the WCB reported that there were 18 foreign corporations which the Trust may have more than one equity security totaling \$100,883 and that "in the 2008 fiscal year, there were 38 new purchases in equities of foreign corporations." The WCB disallowed \$100,883 from the Trust's assets.

In its 2009 Level I Report, the WCB reported the Trust had made 73 new purchases in equities of foreign corporations and disallowed \$231,861 from the Trust's assets. For 2010, the WCB found the Trust owned \$136,898 in equities issued by foreign corporations and disallowed this amount from Trust assets.

Trustee meeting records show that despite the Trust's ongoing non-compliance with Section 317.8, there was virtually no discussion or deliberation of this issue at the Trustee meetings.

Johnson confirmed to BST that the broker in question was an acquaintance from high school, but was not a close personal friend at the time. The fact that a number of financial services firms were solicited and interviewed by a committee of Trustees would tend to mitigate the Chair's influence over the final selection, any personal relationship notwithstanding.

⁴⁹ Interestingly, Trustee minutes for March 9, 2005 reference a comment from the Chair that the Trust's accountant "reported that international equities are not permitted."

In summary, the documents reviewed and the interviews conducted show that:

- The Trustees failed to adopt a formal written investment policy although actual investment practices generally conformed to WCB investment regulations.
- The Chair and Trustees were actively involved in the oversight of the Trust’s investment portfolio and pursued a conservative investment strategy that minimized the Trust’s exposure to volatile market conditions and provided a reasonable rate of return.
- The Trustees failed to ensure the Trust’s compliance with 12NYCRR Part 317.8 with respect to Trust equity investments not from American Institutions and subjected the Trust to unnecessary regulatory asset disallowances adversely affecting its overall funding status.

C. Program Administrator - Program Risk Management⁵⁰

Article V, Section 5 of the Trust Agreement provides for the appointment of a Program Administrator for the Trust, as follows:

The Trustees may designate a fiscal agent and/or an administrator to administer the financial affairs of the Trust. Any fiscal agent and/or administrator so appointed shall furnish a fidelity bond with the Trustees as obligee, in an amount sufficient to protect the Trust against the misappropriation or misuse of any moneys or securities held by or in the name of the Trust. The amount of the bond shall be determined by the Trustees and evidence of such bond shall be filed with the appropriate governmental agencies and departments.

Article VI, Section 6a of the Trust Agreement, inter alia, provides that “such fiscal agent and/or administrator shall not be an owner, officer or employee of a third party administrator.”

Article IX, Section 1 of the Trust’s By Laws requires that a Management Agreement “be negotiated with a qualified entity, as may be determined by the Trustees, for the purposes of efficiently securing the benefits for which the group self-insurance Trust was established and to carry out the intent of the Workers Compensation Law and shall perform all necessary and incidental tasks necessary for the orderly functioning of the trust.” This provision also provides for the administrator to contract with a third party administrator to handle claims administration. Article IX, Section 2 provides that the program administrator, under the supervision of the Chairman “act as manager of the group self-insurance program” and “work with the trustees and the third party administrator to establish an accident prevention program, review the experience

⁵⁰ PRM officials, through legal counsel, declined to be interviewed for the purposes of preparing this report, but did provide certain documents as requested by BST.

of the members to prevent recurrence of accidents and review and revise safety Rules and Regulations to be carried out by the members.”

As noted above, the Trust was formed through the collaborative efforts of Thomas Arney, Priscilla “Pat” Hoffman, and Morton Case. Arney remained the Trust’s Program Administrator from 1995 until his retirement from Program Risk Management, Inc. in 2003. All three individuals had extensive insurance experience. Prior to forming PRM, Arney was a senior executive with Jardine Insurance Brokers New York. While at Jardine, Arney was instrumental in the formation of the Health Care Providers Self-Insurance Trust (“HCPSIT”) and became HCPSIT’s program administrator. In April 1994, Arney left Jardine and became President of Buffalo-based Naples Risk Management (“Naples”). Arney remained HCPSIT’s program administrator at Naples. Arney formed PRM on July 25, 1995, and on August 1, 1995, he signed an Agreement for PRM to become HCPSIT’s program administrator at “a fee equal in amount to seven percent (7%) of the gross written contributions made by the Members to the Trust during the term of this Agreement.”

On October 31, 1995, three months after signing PRM’s Agreement with HCPSIT, Arney executed an Agreement for Services of Program Administration (“Administration Agreement”) with CRISP Chair Janice Johnson.⁵¹ Pursuant to the Administration Agreement (see Exhibit 5), PRM would develop loss control programs and risk management programs, recommend experience ratings of Members, serve as liaison with the WCB, evaluate and make recommendations regarding the suitability for new member participation, monitor the Trust’s financial condition, coordinate actuarial, accounting, auditing, legal, and other professional services and make recommendations to the Trust concerning policies, programs, by-laws, investments contribution rates, insurance policies, procedures, and forms. In addition, PRM would promote and act as broker/agent for Trust insurance services and supervise the activities of MPA, manage a Member contribution escrow account, review and approve/disapprove items submitted for payment, and other duties as may be assigned by the Trustees.⁵²

The term of the initial Administration Agreement was for five years, October 31, 1995 through October 31, 2000, and would automatically renew for successive terms of three years unless either party chose to terminate the Agreement. BST found no evidence of any subsequent Administration Agreement or amendments thereto being executed, suggesting the original Administration Agreement remained in force for the full term of the Trust.⁵³

For its services, the Administration Agreement provided that PRM would receive a fee equal to 6.25% of gross written Member contributions. Financial statements show that for the period October 31, 1995 through November 30, 2009, PRM received approximately \$4.4 million in

⁵¹ Gosdeck advised BST that he did not prepare the Trust’s Administration Agreement with PRM. He stated that Case and Arney agreed to the financial terms. PRM’s Administration Agreements with both CRISP and HCPSIT are substantially similar.

⁵² The Trust’s accounting function was out-sourced to a CPA firm, DeChants, Fuglein & Johnson, LLP.

⁵³ Gosdeck indicated that there were amendments to the Agreement; however, the amendments were not separate written documents, but rather reflected in the minutes.

Program Administration fees⁵⁴, or approximately 5% of gross written contributions for the period.⁵⁵ The fee percentage paid to PRM was consistent and within the range of fee percentages normally paid to program administrators.

In addition, PRM received separate fees for providing Loss Control Services to Trust Members. From 1997-2000, the fees were \$30,000 annually. In 2001, the fees were increased to \$60,000 annually where they remained through 2009. In 2010, the annual fee increased to \$65,000. For the term of the Trust, PRM received approximately \$733,000 in Loss Control fees. Loss Control and Safety Programs will be discussed in greater detail in Section J.

Trustee meeting minutes show that Arney discussed the Administration Agreement at the Trustees' first meeting on October 31, 1995. At the meeting, Arney agreed to review all bills submitted to the Trustees for payment, and the Agreement was modified to include this duty. Arney and Case presented their respective proposed service agreements, including disclosure of the provision under which MPA would continue to receive commission for Members it brings to the Trust even if its contract was not renewed.⁵⁶ The Trustees accepted and executed both contracts.

New York State Department of State records show that on June 27, 1997, PRM Claim Services, Inc. ("CSI") was registered as a domestic business corporation. On November 1, 1998, Arney signed an agreement appointing CSI as third-party claims administrator for HCPSIT.

Minutes reveal that on March 9, 1999, the Trustees discussed the payment of commissions due to Arney for services rendered as an insurance broker. Gosdeck advised the Trustees "that there is no inconsistency in Arney handling both roles and noted that a better premium for the program is better for the program making the roles compatible." Gosdeck added "that Arney has an obligation to obtain the best possible coverage at the best possible price in fulfilling his fiduciary responsibilities." The Trustees unanimously approved Arney "to continue to act as broker for the Trust and be properly compensated for such duties."

Minutes report that on May 24, 2001, the Chair introduced Edward Sorenson as PRM's new primary contact with CRISP. The Trustees were advised that Sorenson had "approximately twenty-five years experience in the Workers' Compensation industry." It was also reported that "both MPA and PRM had agreed to reduce their commissions to 5% each on all activity while the Trust sought to resolve its financial problems."⁵⁷ Sorenson continued as PRM's primary

⁵⁴ For the years 1995-2002, Program Administration Commissions and Marketing Commissions were reported separately on the financial statements. For 2003-2010, Program Administration Commissions and Marketing Commissions were combined under Program Administration Commissions.

⁵⁵ Records show that both PRM and MPA reduced their fees to 5% on or about May 24, 2001, when the Trust was experiencing financial problems.

⁵⁶ The MPA contract will be discussed more fully in the Marketing Section of this report.

⁵⁷ Minutes for December 13, 2006 indicate that Chair Johnson advised the Trustees that both PRM and MPA were back on full 6.25% commission status.

liaison with the Trust throughout the remainder of the Trust's duration. BST was unable to interview Sorenson, but Sorenson did furnish various documents at BST's request.

Minutes reflect that on December 9, 2002, Sorenson agreed to send copies of both the PRM and MPA agreements to all Trustees with a summary of effective and expiration dates suggesting that the Trustees remained cognizant of the agreements' terms and conditions. There is no evidence that, except for PRM and MPA's voluntary reduction in fees from 2001-2006, there were any other contracts with PRM and MPA and therefore, the original PRM and MPA Agreements remained in effect for the Trust's full term. Minutes for January 10, 2011 following the Trust's closure, indicate that the Trust entered into an agreement with PRM for \$9,000 per month for the services of Sorenson and assistant Mark Crawford to help administer the Trust's run-off.⁵⁸

PRM records show that effective January 1, 2003, PRM and CSI were sold by Arney to PRM's senior management. The new stockholders were John M. Conroy, President; Edward A. Sorenson, Executive Vice President; Colleen E. Bardascini, Senior Vice President; and Gail S. Farrell, Senior Vice President.⁵⁹

BST spoke to Chair Johnson about her interactions with PRM and the level of services PRM provided. Johnson confirmed that PRM served as Program Administrator for the Trust's duration and that no other administrators were ever solicited by the Trust. She stated that she wanted to replace PRM but was unaware of any other qualified firms.⁶⁰ It remains unclear why Chair Johnson did not ask the WCB, as Johnson was well aware that the WCB had numerous other group self-insured trusts that reported to it on an annual basis

She said Arney ran the Trust and was the "voice of what would happen." Johnson opined that Arney "hated her guts," recalling that he once walked out of a meeting when she wanted to change auditors. Johnson said she assumed PRM received commissions on certain insurance placements like excess insurance, but PRM did not disclose the amounts received.⁶¹

Johnson indicated that when Arney began to phase out from PRM, he began to bring then PRM Senior Vice President John Conroy⁶² to the meetings. She indicated that she and the other Trustees preferred not to work with Conroy and made that known to Arney. Arney then went out and hired Ed Sorenson who became the Trust's liaison with PRM. PRM also brought on Mark Crawford to assist Sorenson. Johnson said that Sorenson believed in keeping the Board informed, and she spoke to him regularly. She said Sorenson got "flak" from Arney for being

⁵⁸ BST was unable to obtain a copy of this agreement but did confirm that payments to PRM in the amount of \$9,000 per month continued through at least May 2011.

⁵⁹ Conroy confirmed this in a prior interview with BST relating to HCPSIT. Conroy also told BST that he was Vice President under Arney and handled the firm's day-to-day operations and underwriting. Conroy noted Arney formed all trusts serviced by PRM except the Team Trust which they took over from another administrator.

⁶⁰ BST finds this to be an interesting comment in light of Gosdeck's knowledge of and relationships within the New York State self-insurance industry.

⁶¹ MPA advised BST that it played no role in the procurement of reinsurance or the selection of the reinsurer, and did not receive any fees or other compensation for such re-insurance placements.

⁶² Conroy was and remained PRM's Program Manager for HCPSIT.

much more open with the Trustees. Johnson said she worked well with Sorenson and was comfortable with him until 2011 when she discovered Sorenson had not done certain things he was responsible for relating to the Trust.

Both Johnson and Gosdeck noted that the Trustees were very troubled by the serious claims of under-reserving by PRM's affiliate, CSI, that came to light in 2010.⁶³ Johnson asserted that CSI misled the Trustees about the problem, acknowledged the problem when confronted, and offered no explanation as to the reasons for its occurrence. Gosdeck further told BST that he felt Sorenson was slow to acknowledge the growing claims reserve problems. Both Johnson and Gosdeck indicated that because of the reserving issue and other areas of concern, the Trust retained an Albany-based law firm and initiated litigation against MPA, PRM, and CSI.⁶⁴

BST also spoke to Trustees Lasicki, Hardiman, and Campanelli about their views of PRM's performance. Trustee Lasicki said she "only heard great things" about PRM from her Members⁶⁵ who felt PRM was responsive to their needs. She was satisfied with CSI's claims handling until early 2010 when she was "blown away" by the under-reserving. She said it "all sounded good" from PRM, and the Trustees relied on PRM's expertise. She said she had no indication that CSI had done anything "malicious" or that CSI was "incompetent." Lasicki felt the Trustees received a "lot of misinformation from Ed (Sorenson)." For example, she recalled that he could not produce a master list of the Members when asked. PRM also failed to tell the Trustees that Sorenson had a medical issue and was recovering out of state.⁶⁶

Trustee and Secretary-Treasurer Hardiman stated to BST that both Arney and Sorenson were "professional." She said that Sorenson "cared" and was a "great administrator" until near the end of the Trust when she heard he had some medical issues. She said Mark Crawford was also very good. She was very satisfied by PRM and was "taken aback by the flaw in the reserves."

Trustee Campanelli told BST that the Trustees received less information from Arney and more from Sorenson when he took over. He recalled Arney always having difficulties with the reserves and disputes with the actuary and the actuarial reports. He noted that these problems lessened in the later years. He felt Sorenson was responsive at the Trustee meetings but became less so near the end when he believes Sorenson may have had some personal issues.

Case and Hoffman indicated: "From MPA's vantage point at the time, PRM's level and quality of administrative services to the Members were excellent. There were very few, if any, complaints by Members."⁶⁷

⁶³ This will be discussed in Section L in greater detail.

⁶⁴ The suit was filed on May 27, 2011. The Complaint against PRM, CSI, and MPA was "dismissed without prejudice to any future action" in State Supreme Court, County of Albany on January 9, 2012.

⁶⁵ Lasicki is Executive Director of the Association for Community Living which represents non-profit mental health residential agencies across the state.

⁶⁶ BST was informed of the specific medical issues, but will not divulge the details in this report.

⁶⁷ Case and Hoffman added the following relating to their assessment of PRM: "MPA notes, however, that the services in question were the presumed expertise of PRM, not MPA. MPA did not ever claim to have the expertise

Based on the information presented above, it appears there was general satisfaction with PRM's overall performance and management of the Trust's affairs, especially prior to 2010. In the Trust's earlier years, Arney appears to have exercised more control over the Trust's activities with the Trustees under Chair Johnson's leadership asserting greater authority as the years progressed. Interviews and minutes show that PRM provided the Trustees with briefing material prior to each meeting and their staff made administrative, claims, and loss control presentations at the meetings. Trustees were generally pleased with and trusted the information PRM provided to them until it became apparent in 2010 that claims may have been substantially under reserved by PRM's affiliate, CSI, and that the inadequacy of the reserves was not fully disclosed to the Trustees by either PRM or CSI. The Trustees acted prudently in obtaining a "second opinion" to assess the reserve shortfall. The entire claim reserve issue will be addressed in detail in Section L.

It is important to note that by serving as both CRISP's Program Administrator and Claims Administrator, PRM and CSI were in a position to manipulate individual case reserves to portray the Trust in the most favorable financial light, thereby preserving their own financial interests as Program Administrator for CRISP and for the other trusts PRM administered. This dual role has been viewed by many in the industry as inherently conflicted, and some jurisdictions, such as the State of California, prohibit program administrators from having a financial interest in a claims administrator. The potential conflict is further exacerbated by the fact that as Program Administrator, PRM had responsibility "to coordinate actuarial services relating to prospective and present Members of the Trust" thereby having influence in establishing the Trust's reserve liabilities. This will be discussed in more detail in the Actuarial and Claims Handling sections of this report.

This dual role and the inherent conflict of interest, in fact, may have been prohibited by Article VI, Section 6a of the Trust Agreement that requires that the fiscal agent and/or administrator appointed by the Trustees "shall not be an owner, officer or employee of a third party administrator."

As discussed above, in addition to fees received from CRISP for program administration, claims management, and loss control, as a licensed insurance agency, PRM derived commissions for the brokering of various insurance policies on behalf of the Trust. The receiving of such commissions was disclosed by Arney to the Trustees in 1999. However, there appears to have been no disclosure by PRM to the Trustees as to the amounts of commission received, nor a request by the Trustees for such disclosure. BST was unable to obtain confirmation of commissions received by PRM for these insurance placements on behalf of CRISP.⁶⁸

or totality of information necessary to determine whether PRM performed all of its duties to the level and degree of care needed."

⁶⁸ In interviews relating to HCPSIT, PRM officials advised BST that PRM received a 5%-10% commission for excess insurance and a 10% commission for the HCPSIT's Directors' and Officers' insurance. PRM also received a commission from the premium financing company for processing financing applications. The commission initially was 1% of the amount financed and diminished to .75% and .50% as the process became automated. BST found

In addition to the insurance policies discussed above, Trust records showed PRM purchased at least two additional policies, automobile and general liability, on behalf of the Trust. The business automobile policy was purchased through National Continental Insurance with PRM employee Mark Crawford included as the insured driver. An invoice for the policy dated September 20, 2010, reflected an annual premium of \$188.00 and a commission to PRM of \$35.00. Both Chair Johnson and Gosdeck were shown a copy of the policy and invoice. Johnson said she had “no idea” what the policy was for and knew nothing about it until recently informed about it by the WCB. Gosdeck said he similarly was unaware of the policy.

Trust records also included a commercial general liability and property policy from Harleysville Insurance. CRISP was identified as the insured located at 900 Watervliet Shaker Road, Suite 250, Albany, NY 12205-1015, PRM’s office. The policy covered business personal property and appears to have been in effect from at least November 2008. The annual premium paid by the Trust was approximately \$700, and the broker was listed as SANNY, Inc.⁶⁹ Both Chair Johnson and Gosdeck⁷⁰ said they had no recollection of this policy. Johnson stated she was not aware if another Trustee may have requested that both of the above policies be set up, but added that she should have been advised of these policies if paid for by the Trust.

Penalties

The WCB may impose procedural penalties for violations committed by parties to a Workers’ Compensation claim during the administration of the claim or when paying medical benefits associated with the claim.⁷¹ Delinquent accounts are subject to the withholding of payments due under Section 15(8) of the Workers’ Compensation Law, or any other amount due from the

PRM’s commissions to be fair and reasonable, and properly disclosed to HCPSIT Trust. MPA advised BST that it did not receive any commissions from CRISP’s premium financing program, nor did it have a role in establishing or implementing the premium financing program.

⁶⁹ SANNY is Satellite Agency Network of New York, Inc. located in Canastota, NY. Trust records indicate that PRM entered into an Independent Strategic Agreement with SANNY in June 2001 to “receive assistance in accessing additional insurance company markets.”

⁷⁰ Invoices were addressed to CRISP c/o Thomas Gosdeck and records contain a fax from Gosdeck’s office to Sorenson transmitting one of the invoices.

⁷¹ Penalties are issued for the follows violations:

- WC Law Section 110 - failure of an employer to file a report of injury, (Board Form C-2).
- Law Section 13G1 - late payment of medical benefits.
- Law Section 13G - arbitration fees for disputed medical services.
- Law Section 25 - failure of a party to file a required form, unnecessary delay or late payment of conciliation or compensation awards.
- Law Section 114 - fraudulent practices or representations.
- Law Section 142 - fees for parties that appeal the decision of Board referee and the referee’s decision is upheld.
- WC Regulations Section 300.2 - failure to file a medical report.
- Regulations Section 317.22 - violations by group self-insured trusts.
- Law Sections 60.4 - parties that appeal the decision of Board referee in a claim under the volunteer ambulance or volunteer firefighter law and the referee’s decision is upheld.

Workers' Compensation Board, which may be used to satisfy the debt. Licenses issued by the Workers' Compensation Board (including licenses to act as self-insured or third party administrators) may be revoked or not renewed if the account remains delinquent. Civil judgments may also be filed for failure to satisfy this debt.

Minutes for July 12, 2010 reflect a discussion of penalties by Sorenson in response to an inquiry by the Chair regarding responsibility for the payment of penalties. Sorenson noted that if an appeal is lost, and a WCB penalty results, it was appropriate to allocate the Board penalty to the claim file. However, if a deadline was missed or other issue that is the fault of the TPA, then it was the responsibility of the TPA. Sorenson noted "CRISP should never pay a fine."

WCB records reveal that PRM incurred \$8,800 in unpaid penalties on behalf of the Trust for a number of violations for injuries occurring between 2006 and 2010. Approximately \$4,150 of the unpaid amount was past due to the WCB over 270 days as of October 12, 2011. Most of the violations related to the late payment of medical benefits under WCL Section 13G1. BST spoke to Gosdeck about the violations. He noted that when he heard about the number of filing violations he obtained a copy of the violations from the WCB which he reviewed. He approached PRM about it which had no response. He noted that the penalties ceased when PMA took over the claims function. BST subsequently determined that the penalties resulting from PRM's violations were eventually paid by CRISP.

In summary, the documents reviewed and the interviews conducted show that:

- Thomas Arney played a prominent role in the formation of CRISP in 1995, and PRM served continuously as the Trust's Program Administrator until the Trust's termination in 2010 with no formal contract amendments or extensions;
- There was no periodic, competitive process undertaken by the Trustees to determine or help ensure that fees paid to the Program Administrator were competitive or that better services could be obtained elsewhere;
- The fee percentage received by PRM for Program Administration appears fair and reasonable;
- PRM Claim Services, Inc., a firm formed, owned, and controlled by PRM's principals, served as the Trust's claims administrator from 2001 to 2010 creating a possible conflict of interest situation whereby claims reserves could be under-reserved and which may have benefitted PRM more than the Trust;
- PRM officials failed to exercise prudent oversight of its affiliate, CSI, which engaged in questionable claims reserving practices that misrepresented the Trust's true financial condition. CSI failed to properly advise the Trustees of the reserve shortfall, may have provided erroneous and misleading information to the Trustees regarding CSI's reserving practices, and failed to offer any viable explanation to the Trustees for the Trust's inadequate case reserves; and
- PRM incurred and failed to pay penalties for multiple procedural violations of the Workers' Compensation Law.

D. Actuary - SGRisk, Inc. and BYNAC

12NYCRR Section 317.19 requires, in part, all Trusts to submit on an annual basis an actuarial report certified by a qualified actuary verifying claims as defined in 12NYCRR Section 317.2c and the method of calculating such claims be based upon accepted actuarial standards of practice.⁷²

The actuarial reports provided an estimate of CRISP's reserve liabilities and expenses, which then allowed PRM, MPA, and the CRISP's Trustees to evaluate the reasonableness of the premiums (and discounts) it charged its Members. The cost of the Member premiums directly influences which employers joined CRISP as employers seeking coverage tend to select the carrier offering the lowest premium.⁷³ Furthermore, the cost of the Member premiums also had a direct impact on PRM's and MPA's revenues, as lower premiums often result in more Members, generating additional revenues for both PRM and MPA.

There existed a financial incentive for both PRM and MPA to solicit more employers to join CRISP, as PRM's and MPA's administrative and marketing fees, respectively, were based on the total number of employers to join the Trust and the employer Members' gross written contributions. Therefore, an increase in the Trust membership allowed PRM and MPA to better cover their fixed overhead costs and increase their profits, regardless of the Members' contribution to the Trust - or the Members' claims.

Pursuant to WCB policy, so long as a trust is at least 90% funded, the WCB does not implement remediation procedures for that trust. These remediation procedures may include such steps as limitation or elimination of the amount of allowable discounts provided to existing Members and/or the restriction or elimination of the number of new Members allowed to participate in the Trust. These procedures are designed to restore the Trust to a funded position and/or limit the exposure of additional Members to an under-funded trust. This fact was known to both PRM and MPA and is important for several reasons.

First, in the event that the WCB implemented these procedures for a PRM administered trust, such as CRISP, the procedures could have substantially reduced the fees earned by PRM and MPA. This is because PRM and MPA earned their administrative fees based upon the number and size of participants in the Trust, and if the Trust was precluded from accepting new Members, or was effectively priced as unattractive to current Members by virtue of the reduction or elimination of discounts, PRM's and MPA's fee base could dramatically decrease.

Second, PRM and MPA earned fees based upon the "gross written contributions" for a particular Member, which is exclusive of whatever discount may have provided to that Member, including participation in a Retention Plan. As PRM and MPA would receive the exact same fee regardless of whether or not a particular Member received a large discount or no discount

⁷² The rules became effective January 31, 2001.

⁷³ This was confirmed through interviews with Trustees and Members.

whatsoever, there existed no economic disincentive to provide the greatest possible discounts to Members regardless of whether or not the ensuing premiums collected were sufficient to meet the necessary reserves. Thus, there was a financial incentive for PRM and MPA to have CRISP appear to be at least 90% funded and for reserves to be set as low as possible.

PRM, pursuant to its Administration Agreement with CRISP, was responsible for coordinating actuarial services relating to prospective and present Members of the Trust. PRM selected SGRisk, Inc. (“SGRisk”), a New Jersey-based actuarial firm, which performed these services from the Trust’s inception to November 2006.⁷⁴ The President of this firm is Charles Gruber. According to a PRM official interviewed in relation to HCPSIT, SGRisk also performed, and continued to perform as of February 2010, actuarial services for other group self-insured trusts administered by PRM.

Gruber, through counsel, noted that SGRisk submitted a written proposal to provide actuarial services to CRISP on or about August 14, 1995 (approximately two months before the Trust documents were signed). It is unclear whether SGRisk was selected as part of a competitive process, however, Gruber’s counsel indicated that no written contract was executed between the two parties. The decision to engage SGRisk appears to have been Arney’s idea, as he (and PRM) had also been responsible for setting up another trust approximately three years earlier and had also engaged SGRisk to provide actuarial services for that trust. Regardless, Arney’s decision to not execute a written agreement with SGRisk, was at a minimum, imprudent.

Gruber’s counsel noted that initially Gruber’s primary contact person at CRISP was Arney, and that Gruber did not have any direct contact with the CRISP Trustees other than providing copies of certain correspondence.

Gruber’s counsel also noted that to the best of their knowledge, SGRisk received all necessary information to perform their actuarial services, and that their actuarial reports were provided to “CRISP’s administrator” (PRM).

SGRisk prepared independent actuarial reports on behalf of CRISP for the fiscal years ended November 30, 1995 through November 30, 2006.⁷⁵ Concerning the quality of work performed by SGRisk, Arney told BST in relation to HCPSIT that he was satisfied with SGRisk’s work, but added that after later seeing some other actuaries’ work; he thought that HCPSIT should have looked at other actuaries. Arney believed SGRisk was consistent in its actuarial approach.⁷⁶

⁷⁴ SGRisk was formerly known as Stergiou & Gruber Risk Consultants, Inc. (S&G). The other principal of S&G and SGRisk is E. James Stergiou. Interviews indicate that Gruber was the primary contact with CRISP. SGRisk was also selected by PRM to perform actuarial work for HCPSIT.

⁷⁵ BST was unable to obtain actuarial reports prepared by SGRisk for the period November 30, 1995 through November 30, 1998 as well as the report for the period ended November 30, 2000.

⁷⁶ Arney further noted that claims for HCPSIT were reserved on an individual claim-by-claim basis and that the incurred but not reported (IBNR) were established and recommended to the HCPSIT Trustees for approval.

Trustee meeting minutes reveal that actuarial and reserve issues were addressed regularly at the meetings by the Trustees, PRM, and MPA. SGRisk’s actuarial reports were typically presented to the Trustees by PRM. Records show that Gruber appears to have presented the report in person only one time, on March 6, 2000.⁷⁷

In the Trust’s early years, the Trustees supported a conservative reserving approach despite MPA’s assertions that such a strategy impeded their marketing efforts. For example, minutes for March 9, 1999 report: “During the financial report, the Trustees discussed the issue of reserves as they impact on the marketing efforts of MP Agency, who reported that the increase in the member deficiency of the Trust impairs their efforts.”⁷⁸ The Trustees approved continuation of the current conservative assumptions.⁷⁹

At the Trustee meeting of March 6, 2000, Gruber presented the Trust’s actuarial report for the year ended November 30, 1999. According to the minutes, Gruber advised the Trustees that there was “now sufficient experience with Trust operations to determine a pattern for losses and how to factor loss experience into ratemaking and reserve decisions.” Additionally, the minutes note that Gruber previously had been relying upon New York State factors that “have generally been higher than Trust experience.” Gruber referred to the pending State regulations that would prohibit deficits in Trust operations and reported that, based upon this policy, CRISP would be in a position of discounting reserves in order to avoid the deficit. Lastly, the minutes note that it was Gruber’s “opinion that the substantial change in the February 2000 IBNR level is a direct result of the change to discounted reserves.” He noted that this would “stabilize” but did “not have sufficient experience to determine when this stabilization may occur.”

During this meeting, Chair Johnson raised concerns regarding an increase in claim reserves from \$865,000 to \$2 million. According to the minutes, Gruber responded that in “early years there is a claims reserves build up as claims mature from low to substantial amounts and that the CRISP experience in his opinion is not unusual.” He recommended the Trust “continue to monitor it as it always has with PRM looking at case by case reserves and his firm looking at the aggregate reserves based upon actual experience.”

Two years later, the Trust’s audited financial statements⁸⁰ for the year ended November 30, 2001 reported a member deficit of \$4,191,978.⁸¹ The deficit was largely caused by a substantial increase in claims during 2000 which more than offset the total of the contributions during 2000. In a WCB Summary of Funding Status report, the WCB excluded over \$3 million in Trust assets

⁷⁷ In contrast, HCPSIT records show that an SGRisk representative attended HCPSIT Trustee meetings on an annual basis.

⁷⁸ It is unclear why MPA would be concerned about this as the continuity of the trust was not impacted by whether the trust grew at this point. It appears that MPA was solely worried about the additional commissions they may have lost if potential members decided not to join because of the reported reserve figures.

⁷⁹ The Trust’s member deficit was less than \$323,000 at the end of 1999.

⁸⁰ The Trust’s financial statements were prepared by DeChants, Fuglein & Johnson, LLP.

⁸¹ The deficit was later increased during 2002 to \$4.6M to reflect the fact that certain surcharges from some former Members may not be collected.

and calculated a regulatory deficit of \$7,309,905, or a trust equity ratio of 24.86%. The WCB also found that the 2001 actuarial report did not present “an acceptable range of loss reserves.”⁸²

In a letter to PRM’s Sorenson dated April 23, 2002, the WCB suspended the addition of any new members into the Trust, effective immediately. PRM requested that the suspension be lifted but the WCB denied this request in a letter dated May, 2, 2002. On May 17, 2002, Sorenson met with WCB officials and it was agreed that Tillinghast Towers Perrin (“TTP”) would conduct an actuarial review of CRISP and that a fiscal review be undertaken by an accounting firm.⁸³ The member freeze would remain in effect until the reports were completed and CRISP demonstrated actions to reduce the deficit position.

In a document addressed to Sorenson dated March 27, 2003, TTP presented the findings of its Actuarial Evaluation of CRISP as of November 30, 2002. In summary, TTP found the “deficit position of the trust to be roughly \$5.3 million as of 11/30/02” and “(r)ates and deviations used by CRISP as of 12/1/02 appear to be inadequate by roughly \$0.2 million.”⁸⁴

PricewaterhouseCoopers (“PwC”) performed the agreed-upon fiscal review and issued a report on or around December 2003.⁸⁵ Among its findings, PwC concurred with SGRisk, Inc.’s actuarial calculation as of November 30, 2002, but found that the range provided of \$9.4 million to \$11.5 million was “too wide.” PwC suggested a range between \$10 million and \$11 million and proposed a \$700,000 increase in reserves.

PwC further indicated that based on the significant Members’ deficit reported in the audited financial statements and continued losses being reported, PwC would have “considered issuing a going concern opinion on this entity and may not have come to the same conclusion as the audited financial statements represent.” PwC further noted that the Trust’s 43% funded status and \$7,108,575 deficit would be less had paid indemnity assessments been accrued.⁸⁶

Sorenson responded to the PwC report in a letter to the WCB, dated January 12, 2004. Sorenson, despite not being an actuary, disputed PwC’s findings regarding the tightening of estimated reserves (and the \$700,000 reserve increase), the basis of a “going concern opinion” based on the Trusts’ proactive approach to addressing the Member deficit, and the assessment accrual. Interestingly, Gruber, in an early 2002 memo to Sorenson, indicated that the Trust would need to increase its contributions by approximately \$1.2 million per year for four years to erase the

⁸² The Summary also noted: “An acceptable range of loss reserves was not present in the actuarial report. The reserve figure of \$7,051,093 used in the balance sheet was determined by taking an average of five actuarial methods, and applying a 6% discount rate. However, if the claims reserves are discounted at 5%, the reserve figure becomes \$7,302,174 and the deficit shown above would increase by \$250,081.”

⁸³ The Trust Member deficit had increased each and every year since 1997 and by the end of the 2002 fiscal year the Member deficit was \$5.7M (GAAP).

⁸⁴ Approximately 3.77% difference.

⁸⁵ The recommendation to use PwC during 2002 and 2007 was initiated by the WCB, not the Trustees.

⁸⁶ PwC also found that PRM maintained “a sole checking account” that was used for all PRM-operated Trusts in violation of WCB regulations.

deficit, suggesting that the tightening of reserves was not the issue, rather, contributions needed to be increased to offset the Trust's deteriorating financial condition.

In 2006, concerns arose relating to the work performed by SGRisk relating to other group self-insured trusts. Gosdeck recalled that upon learning of these concerns, the Trust approached Charles Gruber from SGRisk and advised him that he could remain as actuary if he paid for an independent review of his operation. Gruber refused and By the Numbers Actuarial Consultants ("BYNAC") was solicited and assumed the role as the Trust's actuary.⁸⁷

Concerning BYNAC, Johnson told BST that Sorenson from PRM told her that he felt BYNAC was putting more money in the reserves than was necessary. Sorenson said he felt BYNAC did not understand how fast PRM settled claims and was, therefore, over-reserving.

PWC issued another report on June 13, 2007, and had no major/significant findings, although they did note that the reserves report on the Trust's audited financial statements were 5% below the actuary's estimate.⁸⁸

As part of our analysis, BST retained Casualty Actuarial Consultants, Inc. ("CACI"), to review Gruber's and BYNAC's actuarial reports and provide an analysis of these documents. The CACI report to BST, dated October 13, 2011 (Exhibit 8) offered the following general observations:

Overall, SGRisk and BYNAC utilized methods in each report that were generally consistent with standard actuarial techniques (exceptions to this are noted on a report by report basis below), however, those methods were not always relied upon in making selections. Thus, CACI questions some of the selections as these selections tended to cause the estimated loss reserves in the earlier reports to be undervalued. Overall, the results within each report were mostly reasonable.

The estimates contained in the 10 reviewed reports mostly were within a range CACI would consider reasonable given the information the actuaries had at the time of preparation. As noted above, SGRisk's on again/off again use of the prior estimates in the selection process was unusual. Additionally, SGRisk's delayed use of CRISP's unique loss development factors was non-standard. However, in the end, neither of these items contributed greatly to the eventual closing of CRISP. Despite the shortcomings noted in SGRisk's reports, the estimates in SGRisk's reports are still within a reasonable range of the current estimates of ultimate losses (as of 12/31/10).

BYNAC's use of judgmental selections in the most recent periods, which tended to ignore the results of the incurred and paid methods, and the age adjustments implemented for those same periods in the 11/30/08 and 11/30/09 reports, tended

⁸⁷ Meeting minutes show that a BYNAC representative attended in person or by phone three Trustee meetings.

⁸⁸ The Trust did not have a Member deficit at this point.

to produce results that were less than reasonable for the most recent periods. Had the 12/1/06-07 and 12/1/07-08 estimates not been understated at 11/30/07 and 11/30/08, a deficit would have been reported at 11/30/07 instead of a surplus, and the deficit reported at 11/30/08 would have been larger (around \$3,200,000 instead of \$1,826,333). It is unclear whether this would have impacted CRISP's decision to continue operations since they continued operations when the deficit was \$5.7 million at 11/30/02.

Overall, SGRisk and BYNAC utilized generally accepted actuarial methods in most reports, although those methods were not necessarily followed. It does not appear that their decisions to occasionally veer from standard actuarial procedures directly led to CRISP's current financial situation. The biggest contributor, at least in magnitude, appears to be the large reserve changes implemented during 2010.⁸⁹ Based on CACI's experience, such increases are not unusual once a group decides to terminate. Neither BYNAC nor SGRisk could have anticipated the size of the increases implemented during 2010. In CACI's opinion, there were no actuarial errors or misjudgments that were so gross that they led directly to the insolvency of CRISP.

In summary, the documents examined and the interviews conducted reveal that:

- Neither PRM nor the Trustees required a competitive bidding process for the actuarial services provided to the Trust.

E. Certified Public Accountant - Marvin & Company, PC

12 NYCRR Section 317.19 requires, in part, all Trusts to submit audited financial statements prepared in accordance with Generally Accepted Accounting Principles (GAAP) and certified by an independent certified public accountant.⁹⁰ The largest liability and expense appearing on CRISP's financial statements relate to the Members' claims (loss reserves); accordingly, these account balances at any point in time are material to the overall fairness of the financial statements.⁹¹

Individual claim loss reserves were initially established by the Trust's claims administrators, Gallagher Bassett and later CSI upon notification and examination of the injury claims filed by its Members. The loss reserve amounts established by the claims administrator were, in turn, relied upon by CRISP's actuary when estimating loss reserves that were used as the basis for reporting the claim liability and expense on the financial statements prepared by the Trust's accountant, DeChants, Fuglein & Johnson, LLP ("DF&J"). CRISP engaged a public accounting

⁸⁹ The Member deficit had been substantially reduced by 2007 during which time there was a Member surplus of approximately \$120,000.

⁹⁰ The rules became effective January 31, 2001.

⁹¹ The loss reserves represent the amount the claims administrator believes CRISP will have to pay out as a result of injury claims.

firm (Marvin & Co. PC, 1996-1998, 2003-2010; and Urbach Kahn & Werlin PC, 1999-2002) to conduct an audit of CRISP's financial statements. CRISP also engaged SGRisk, Inc. to annually provide an estimate of the annual claim liabilities and expenses.

Inherent within GAAP is the principle of conservatism, which requires the preparers of financial statements to make evaluations and estimates, to deliver opinions, and to select procedures, and to do so in a way that neither overstates nor understates the affairs of the business or the results of operation.

While PRM had the responsibility to prepare the financial statements, it was the independent accountants' responsibility to determine whether the claims liability/expense amounts reported by PRM on behalf of CRISP were not materially misstated, and opining on the overall fairness of CRISP's financial statements. During the periods ended November 30, 1996 through December 31, 2010, Marvin & Co. and Urbach Kahn & Werlin PC concluded that CRISP's financial statements were presented fairly, in all material respects.

In conducting its audit, the independent auditor was obliged to follow Generally Accepted Auditing Standards (GAAS) used in the United States. Statements on Auditing Standards (SAS) provide guidance to auditors on GAAS in regard to auditing an entity and preparing a report.

SAS 73, *Using the Work of a Specialist*, requires the auditor to evaluate whether the specialist's findings support the assertions in the financial statements. SAS 73 applies to various specialists, including actuaries such as SGRisk and BYNAC. Accordingly, if the independent auditors believed SGRisk's and BYNAC's findings (claims reserves) were unreasonable; they should apply additional audit procedures, which may include obtaining the opinion of another actuary.

As discussed previously, TTP prepared an Actuarial Evaluation of CRISP as of November 30, 2002. In summary, TTP found the "deficit position of the trust to be roughly \$5.3 million as of 11/30/02" and "(r)ates and deviations used by CRISP as of 12/1/02 appear to be inadequate by roughly \$0.2 million."

In addition, PwC performed a fiscal review and issued a report on or around December 2003. Among its findings, PwC concurred with SGRisk, Inc.'s actuarial calculation as of November 30, 2002, but found that the range provided of \$9.4 million to \$11.5 million was "too wide." PwC suggested a range between \$10 million and \$11 million and proposed a \$700,000 increase in reserves. PwC further indicated that based on the significant Members' deficit reported in the audited financial statements and continued losses being reported, PwC would have "considered issuing a going concern opinion on this entity and may not have come to the same conclusion as the audited financial statements represent."

PwC actuaries reviewed the report completed by TTP as of November 30, 2002, and the actuarial report completed by SGRisk as of November 30, 2002, and concurred “with the methods and the point estimate developed by SGRisk, Inc.,” but felt SGRisk’s “range should be tighter...”⁹²

As noted above, SAS 73 requires the auditor to evaluate whether a specialist’s (including actuary’s) findings support the assertions in the financial statements. Accordingly, if the independent auditors believed SGRisk’s findings (claims reserves) were unreasonable, they should have applied additional audit procedures, which may include obtaining the opinion of another actuary. We reviewed the auditor work papers made available to us, and based on our examination of these documents, it appears the auditors evaluated the work of the actuary and tested certain assumptions. We did not find any evidence to indicate the auditors obtained information which suggested the reserves were materially misstated.

Our examination of the Trust’s documents and records also revealed that the reserve amounts reported on the Trust’s audited financial statements were not materially different from the estimated amounts noted in the independent actuarial reports.

In summary, the documents examined and the interviews conducted reveal that:

- The documents examined indicate the Trust’s auditors followed the requirements of SAS 73; and
- The reserve amounts reported on the Trust’s audited financial statements did not appear to be materially different from the reserve amounts estimated by the actuary retained by the Trust.

F. Marketing

The success of any group self-insurance plan relies, in part, on its ability to attract and differentiate itself from its competitors and to offer favorable premium discounts to members with good loss histories. Like other group self-insured trusts, CRISP was “broker-driven” in that the primary source of marketing was licensed insurance brokers. In this instance, Morton “Morty” Case and Priscilla “Pat” Hoffman were the Trust’s exclusive brokers. Brokers typically receive commissions ranging from 5% to 8% for each member they place with a trust.⁹³

As noted previously, Case, Hoffman, and their firm MPA⁹⁴ were central to the Trust’s formation and served as the Trust’s exclusive marketing agency from the Trust’s inception until October

⁹² PwC also found that PRM maintained “a sole checking account” that was used for all PRM-operated Trusts in violation of WCB regulations.

⁹³ PRM had marketing responsibility for HCPSIT.

⁹⁴ New York State Department of State records show M. G. Case & Co., Inc. was incorporated on June 24, 1975 and M.P. Agency, Inc. became the successor firm on April 12, 1988. Court documents reveal that MPA is a successor-in-interest to M.P. Alliance, a former division of Alliance Brokerage Corporation. MPA advised BST that Case and Hoffman have a 60% and 40% interest in the firm, respectively.

31, 2009, when PRM assumed the marketing rights through a purchase agreement with MPA.⁹⁵ As discussed above, Case and Hoffman loaned the Trust \$175,000 as start-up funds which evidence shows was repaid in full, without interest.⁹⁶

Case and Hoffman advised BST that “about 80 of the CRISP members were also property and casualty accounts of MPA or technically of a different insurance brokerage with which MPA was affiliated. (In more cases than otherwise, those CRISP members were property and casualty accounts first and then became W.C. members of the Trust, but it sometimes happened the other way.) (sic)”⁹⁷

CRISP, PRM, and M.P. Alliance signed an Agreement for Marketing Services (Exhibit 6) on October 31, 1995⁹⁸ appointing Alliance “...to provide marketing services to the prospective Members of the Trust...” and as “...the exclusive provider of marketing activities undertaken by them to prospective Members of the Trust.”⁹⁹ In addition, Section II of the Agreement provides that “...all applicants accepted for membership in the Trust shall be deemed to have been referred to the Trust by Alliance” and that “...no other broker, agent or other person, firm, corporation or association shall be eligible for compensation for any activity in providing service to any participant in the Trust...”¹⁰⁰

Section III of the Agreement further requires that all requests for membership are to be forwarded to PRM for acceptance and that the authority to accept a member rests with the Trustees upon PRM’s recommendation.

Additionally, Section V of the Agreement states that Alliance (hereinafter referred to as “MPA”) was to be compensated by a fee paid through PRM of 6.25% of the gross written contributions made by the Members to the Trust. In the event of return of premium, MPA would refund the commission. Section V(c) provided for MPA to earn the 6.25% commission “for so long as business provided on behalf of the Trust is retained and paid for by the member of the Trust and shall continue beyond the term of this Agreement.”¹⁰¹

MPA’s responsibilities were specified in Section VI of the Agreement and include that MPA would:

- Exert its best efforts to promote sales and marketing to all Trust Members;

⁹⁵ BST provided written questions to both Case and Hoffman through their legal counsel and received written responses which are referenced in this report.

⁹⁶Trustee minutes report discussion of this loan by the Trustees.

⁹⁷ Case and Hoffman stated that MPA did not have separate marketing agreements with any Trust members.

⁹⁸ A notation on the bottom of the Agreement notes an effective date of October 30, 1995.

⁹⁹ The Agreement was signed by Janice Johnson, Thomas Arney and Morton Case.

¹⁰⁰ Case and Hoffman stated to BST that the Agreement was prepared by Arney and Gosdeck and reviewed and commented on by MPA “without benefit of counsel.”

¹⁰¹ Case and Hoffman noted that MPA received its commission payments through PRM and when another broker or agent was involved, the 6.25% was “shared compensation.”

- Furnish information to PRM including report of activities, competitive marketing problems, information on poor credit risk member applicants, sales correspondence and complaints or comments from Members;
- Build and maintain an organization commensurate with the growth of and to strive to upgrade its facilities to furnish maximum service to PRM, the Trust and the Members;
- Provide services to PRM including attendance at meetings; communication of Trust policies to customers; visit PRM offices or Trust offices; maintain an adequate office; cooperate with PRM personnel; investigate and handle Member rejections, service problems and complaints; handle inquires, correspondence, and orders forwarded by PRM; speedy follow-up of all PRM inquiries received from PRM; and such other duties assigned by the Trust or PRM; and
- Remain licensed in accordance with the provisions of applicable state and federal laws and the rules and regulations promulgated thereunder.

MPA, under Section XII (b) of the Agreement, was required to “continuously and without interruption” maintain Broker’s Errors & Omissions (“E&O”) insurance coverage “in the face amount of not less than \$2,000,000 per occurrence and \$2,000,000 in the aggregate.” Also, MPA was required to “upon request provide reasonable evidence to the Trust and the Program Administrator that the said assurance is in place as required by this paragraph and shall provide immediate written notice to the Trust and Program Administrator of termination or material amendment of any such policy.”

The term of the Agreement under Section IX was from October 31, 1995 through October 31, 2000, and would automatically renew for successive three-year terms unless either party gave notice to terminate. On October 31, 2000, a new contract was executed essentially extending the original contractual terms through October 31, 2005, including the renewal provisions (Exhibit 9).¹⁰² It has not been ascertained by BST why the Agreement was renewed for a five-year term when the terms of the original agreement clearly state a renewal term of only three years.

PRM purchased the Trust’s marketing rights from MPA on August 28, 2009, and assumed the rights as exclusive Trust marketer effective November 1, 2009 through October 31, 2010. The aggregate purchase price was not to exceed \$1 million. CRISP and PRM subsequently entered into an agreement for marketing services on September 30, 2009, for a fee of 5.5% of gross written and paid contribution, effective November 1, 2009 (Exhibit 10).¹⁰³

Audited financial statements show that for the period October 31, 1995 through October 31, 2009, MPA received approximately \$4.3 million in Marketing and Program Administration

¹⁰² The 2005 Agreement replaced M.P. Alliance and Alliance with M.P. Agency as party to the Agreement. Section V (b) was also amended directing Member payments directly to PRM rather than to MPA.

¹⁰³ Where no sub-agent is involved, PRM’s commission was limited to the level of compensation paid to its sub-agents anticipated to be between 4% and 4.5% of gross written and paid contributions.

fees¹⁰⁴ or approximately 5% of gross written contributions for the period.¹⁰⁵ Fees paid to MPA appear to have been fair and reasonable and within the range of fees normally paid to insurance brokers to the extent MPA fulfilled its contractual obligations.

Trust records show the Trust served approximately 460 members during its tenure. Approximately 146, or 32% of total Members joined between October 1995 and December 31, 1997, and by the end of 2005, 364 Members, or approximately 79% of the total membership had joined. Between 2006 and November 1, 2009, approximately 86 new members joined, or 19%. Based on these figures, it appears that marketing was the most effective in attracting new members during the first ten years with the rate of new membership diminishing thereafter.

Marketing was targeted by MPA to community mental health and developmental disability residential agencies, including those agencies belonging to trade associations such as the Association for Community Living, NYS Association of Community and Residential Agencies, Coalition of Behavioral and Health Agencies, Supported Housing in New York, and Empire State Association of Adult Homes. As noted, MPA was also the provider of other insurance products, such as property and casualty insurance to a number of agencies joining the Trust. Therefore, it would appear that MPA's offering of low-cost workers' compensation insurance through the Trust supplemented and enhanced its overall insurance product marketing opportunities to the residential agency community.¹⁰⁶

Trustee minutes show that Case and Hoffman played prominent roles in the ongoing activity of the Trust. MPA's marketing exclusivity allowed Case and Hoffman to have a major impact on the Trust's operation and financial condition by virtue of the quality and financial stability of the Members they recruited into the Trust. To promote MPA's marketing efforts, the Trust also offered a premium financing program and a retention plan,¹⁰⁷ the latter for select Members only.

Trustee minutes reveal that marketing activities were discussed regularly at the meetings. Both Case and Hoffman attended virtually every Trustee meeting and presented a marketing report to the Trustees addressing such topics as new member solicitations, cancelled/non-renewed members, conference attendance, marketing constraints, and other marketing-related issues.

¹⁰⁴ For the years 1995-2002, Program Administration Commissions and Marketing Commissions were reported separately on the financial statements. For 2003-2010, Program Administration Commissions and Marketing Commissions were combined under Program Administration Commissions.

¹⁰⁵ Records show that both PRM and M.P. Agency reduced their fees to 5% on or about May 24, 2001, when the Trust was experiencing financial problems.

¹⁰⁶ Trustee minutes for January 23, 2009, suggest that MPA had marketing agreements in place with various organizations such as NYSACRA. Chair Johnson requested from MPA a copy of all such agreements.

¹⁰⁷ The International Risk Management Institute, Inc. (IRMI) defines a retention plan as: A type of dividend plan most often used only in connection with workers' compensation insurance. This plan provides that the net cost to the insured is equal to a retention factor (insurance company expenses) plus actual incurred losses, subject to a maximum equal to standard premium less premium discount. This can also be used for other lines of insurance. PRM managed a large retention program for HCPSIT.

Records suggest that a quarterly marketing newsletter was sent out by CRISP through 2007 but was discontinued in 2008.

Records and interviews reflect that the Trust's marketing efforts were affected by a number of issues, including the 9/11 terrorist attacks that limited the addition of additional New York City area Members due to reinsurance carrier restrictions, lack of aggressive upstate marketing by MPA, the Trust's growing deficit and Member assessment in 2001, WCB membership restrictions, reduced rates, and publicized problems relating to other self-insured trusts.

For example, minutes for December 9, 1998 reflect discussion of competition from the State Insurance Fund which, according to Case, "has been giving prospects a discount of up to 50% when the fund receives a Notice of Cancellation." Interestingly, the minutes also noted that "the Trust's success is attributable to the underwriting creativity demonstrated by PRM."

To address problems with marketing efforts in western New York, minutes for November 17, 1999 report that MPA "had entered into an agreement under which it would utilize the resources of PRM to assist in the marketing in the western New York area where CRISP had traditionally encountered difficulties in marketing."

BST performed an analysis of the geographic distribution of the Trust's membership. Records show that approximately 63% of the Members were located in New York City, Long Island and the counties of Westchester and Rockland, 21% from the mid-Hudson/northeastern New York State area, and the remainder, or about 15% from central and western New York State.¹⁰⁸ These findings tend to support that MPA's marketing efforts, at least its successful marketing efforts, were concentrated in the downstate New York area.

BST requested MPA to describe and furnish a copy of its marketing plan, if in written form. MPA responded that beginning in 1995, it had an "unwritten Plan which multiplied the applicants for membership in CRISP" receiving endorsements from six statewide social service associations with 800 total Members and introducing certain large independent agencies to join CRISP. MPA further stated that it made frequent mailings to association Members, advertised in association journals, spoke and distributed CRISP materials at association and non-association events, most of which were outside of the five boroughs of New York City. MPA also furnished to BST a sample of marketing brochures used to recruit new members. These samples brochures appear to have been produced in the Trust's early years.¹⁰⁹

MPA cited a number of factors inhibiting its marketing efforts for CRISP, including the WCB's suspending the admission of new members for about 18 months in the 1990's due to funding concerns, the WCB's subsequent limiting the addition of new members to 20 per annum,

¹⁰⁸ Approximately 1% of the Members reviewed had out-of-state business addresses.

¹⁰⁹ Chair Johnson noted that MPA produced and provided to the Trustees for approval marketing materials when the Trust began. She did not recall seeing any subsequent materials brought to the Trustees' attention. She added that MPA wanted the Trust to pay for posters which the Trustees rejected as they felt MPA was receiving a marketing fee and should incur this expense itself.

CRISP's re-insurer forcing the non-renewal of one large Brooklyn account and prohibiting the addition of new members based in the five boroughs of New York (as a special terrorism risk factor) within certain unspecified distances from Manhattan immediately after September 11, 2001, and the difficulty in attracting new members after the adverse publicity relating to the failure of the Healthcare Industry Trust of New York.

Despite concerns relating to the Trust's lack of growth, minutes show the Trustees expressed satisfaction with MPA's marketing activities. For example, minutes for May 29, 2003 note: "The Chair congratulated MP Agency on their marketing successes."

Trustee minutes beginning in 2008 reflect the Trustees' growing concerns relating to MPA's succession planning. Trustees were concerned about Case's and Hoffman's potential retirements and absence of marketing continuity after their departures. Minutes for March 11, 2008 report Trustee Lasicki citing the "need for long-term planning for marketing, specifically 5 to 10 years out." The Chair is reported to have agreed noting that "a succession plan was warranted considering the Board's fiduciary responsibility for continuance of the Trust." It was agreed that Case and Hoffman would "work on a plan for discussion at the next Trustee meeting."

Succession planning was discussed at the next meeting on June 2, 2008, at which time Case advised the Trustees that he had "signed an agreement reducing his role in the company from 80% to 50% making them (Case and Hoffman) equal partners..."¹¹⁰ Case noted that in light of the current marketplace, "it was difficult to find someone to take this role on at this point." Sorenson advised the Trustees that PRM had "a buy-sell agreement in place in the event of the departure of one of them for any reason to ensure the continuity of the business."

At a meeting on January 23, 2009, the Chair "indicated that over the past year, the CRISP Board has asked Case and Hoffman to deliver a succession plan." Case informed the Trustees that he "was unprepared to offer a plan at this time."¹¹¹ The Chair asked MPA to have specific information regarding their succession plan for the March meeting. At this meeting, Hoffman also advised the Trustees that negative media attention relating to self-insured trusts had "created an environment in which E&O (Errors & Omissions) concerns by brokers have jeopardized retention." Case and Hoffman indicated to the Trustees that they had "secured a separate E&O policy for their CRISP marketing activities."

The minutes of March 6, 2009 do not reflect discussion of MPA's succession, but the discussion resumed at the meeting of May 29, 2009. In Executive Session, the Trustees discussed succession-planning issues with MPA and the renewal or non-renewal of the Marketing Agreement. The Chair indicated that "financials of the deal is not the concern of the Trust but the proposed successor would be subject to Trustee approval. Case and Hoffman concurred."

¹¹⁰ MPA advised BST that Case and Hoffman are 60% and 40% owners of MPA, respectively.

¹¹¹ Case also told the Trustees that MPA would end its relationship with JLS and relocate, either with another agency or on their own. Case and Hoffman had been advised by the owner of JLS that there was a criminal investigation relating to JLS premium account transactions, but that this did not involve CRISP.

One Trustee noted that “several adult home participants left the trust due to dissatisfaction with MP Agency, with price being a contributing factor.” Case “disagreed with the characterization.” Trustees Lasicki, Hardiman, and Campanelli agreed to ascertain “why prospects choose not to participate” in the Trust. The Trustees also approved July 31, 2009 as the new “drop dead” date for the Trust to advise MPA that the Trust was electing not to renew the contract.

At the meeting of July 22, 2009, the Chair reported on the agreement in principal to transfer marketing rights from MPA to PRM. On September 28, 2009, the Chair announced that PRM and MPA had agreed upon terms for the transfer of marketing rights to CRISP, and the transfer of marketing rights was unanimously approved by the Trustees.

BST spoke to the Chair, Gosdeck, and three Trustees at length about the Trust’s marketing program. As previously noted, we were unable to directly interview Case or Hoffman in relation to this matter but did receive written responses to questions prepared by BST through MPA’s legal counsel.

Johnson confirmed that MPA handled all marketing activities for the Trust. All new members came through MPA and no other insurance brokers were involved. She was not aware of any specific written marketing materials and believed MPA marketed mostly through its client contacts. Johnson stated that Arney coordinated everything with Hoffman and Case, but that Sorenson did not get along with MPA, in her opinion, which she felt provided a good check and balance. She noted that Case and Hoffman were at the Trustee meetings except for Executive Sessions and characterized the Trust as “their organization.”

Johnson felt MPA did not do enough to market the Trust and the Trust became “stagnant.” Johnson stated that when the Board starting putting pressure on MPA to market the Trust, MPA approached some adult homes controlled by Oxford. MPA said Oxford wanted 5% commission for this placement and wanted the Trust to provide 2% from the “back end.” MPA claimed the homes’ loss ratios were good. Johnson said the Trust was not going to pay for this and that MPA was already receiving a commission. She added that MPA successfully recruited “Palm Beach Gardens”¹¹² and another agency from Oxford to join the Trust. Johnson claimed MPA understated Palm Beach’s payroll by 50%, resulting in an understated premium of \$125,000, and the discrepancy was later uncovered in a payroll audit. MPA reportedly told Johnson that it could not report the agency’s payroll in full.

Johnson indicated MPA proposed agencies that were not qualified. For example, she noted that MPA brought in the Developmental Disabilities Institute (“DDI”) to the Trust. This will be discussed in the Underwriting section of this report.

Johnson said Hoffman and Case were considering getting out of the business for personal reasons, but failed to build an organization to support the Trust in their absence. Sorenson wanted PRM to buy the Trust’s marketing rights from MPA, and an agreement was reached

¹¹² BST determined the agency in question was Palm Gardens Care Center LLC.

where PRM was to make monthly payments to MPA. The Trust closed before this occurred. Johnson noted that the formation of a captive with Liberty Mutual was explored when the Trust closed, but this never materialized.

Johnson noted that when the Trust's future was in doubt, she received a call from Trustee Campanelli saying that Hoffman contacted him and wanted to meet with him and the Trustees representing the larger agencies. Johnson contacted Hoffman and told her she should be present at the meeting and a meeting was held at Johnson's home. The meeting included Gosdeck, Johnson, Hoffman, Case, Campanelli, and Trustees Pierri and Lasicki. Hoffman said she wanted to set up a safety group consisting of the Trust's larger members. Johnson said that was not fair to the smaller Members of the Trust, and it was not pursued any further.

Johnson said that underwriting criteria was set up by PRM and MPA early on and was never revisited by the Board. She was not sure whether the guidelines were ever reduced to written form. She had no reason to believe there were any problems with Member underwriting. It would seem that as a CPA, non-practicing attorney, and compensated Trustee, Johnson would have realized that it was the Trustees' fiduciary duty to periodically revisit the underwriting criteria given the fact that the Trust had a Member deficit for all but one year of its existence, including a \$5.7 million dollar deficit by 2002. Clearly the parties responsible for admitting or renewing the Members (or supervising this process) failed to charge adequate premiums to cover the claims filed by certain Members.

Johnson said that the Trustees approved all new Members based on representations made by PRM and MPA. She recalled some proposed Members being denied membership and that there were "fights" between Hoffman and Sorenson relating to the risks posed by some proposed Members.

Johnson confirmed the Trust had a premium financing program from the beginning to attract new Members. In addition, she indicated that premium discounts were given to Members in the early years as well to attract new Members, even though the Trust was operating at less than breakeven. She said the Board of Trustees allowed 5% of the membership to receive discounts up to 10% at PRM's and MPA's discretion, but 95% of the Members received no discounts. She asserted that in the first year or two some Members received discounts up to 50% without the Board's knowledge. The Board finally asked why the deficit remained the same and was then told of the discounts. Johnson claimed the Board never knew what discounts a specific Member received. She noted that the Trust also paid the Members' WCB annual assessment.

Johnson said there were no dividends issued to Members but did note that ICL, Four Winds and perhaps two other large Members had retention plans for the term of the Trust. She was not made aware of this until the end of the Trust, and only when she was told inadvertently by Campanelli that ICL had received its annual retention reimbursement check.¹¹³

¹¹³ Campanelli indicated that ICL participated in the Retention Program for a few years and then stopped. Records suggest ICL participated in the program from 2004-2009. Records show that a total of eight (8) Members participated in the Retention Program.

Johnson noted that litigation had been initiated by the Trust against MPA, PRM, and CSI, and she provided BST with a copy of the litigation documents.

Gosdeck also confirmed to BST that MPA was the Trust's exclusive marketer. Concerning the marketing agreement between MPA and the Trust which seemed to favor MPA, Gosdeck said he would not have known about the Trust at the time to raise any questions about it. He said he consulted with the Superintendent of the State Insurance Department about the agreement's provision regarding MPA receiving commission on renewals essentially in perpetuity. He was told that renewals belong to the producer and this was not unusual. He said that Hoffman and Case focused on downstate marketing and did little upstate. This created more of a problem after September 11, 2001 when insurance costs increased in the downstate market where most of their Members were located.

He stated that Case had the loss information on potential new Members and provided financial information to the Trustees and PRM. He said Case and Mark Crawford from PRM would sometimes disagree about new Member referrals that were high risks. Gosdeck cited "Palm Beach Gardens" where Case "deliberately" understated the potential Members' payroll. When the payroll audit was later performed, the Member immediately came in and paid what was owed. He also cited the DDI as having similar problems.

Gosdeck indicated that at the time when PRM was going to buy out MPA's marketing rights, he and the Trustees obtained a copy of MPA's E&O insurance policy. To their surprise, they found that MPA was not insured in the capacity as the Trust's insurance broker as was required by the Marketing Agreement.¹¹⁴

Gosdeck confirmed Johnson's recollection regarding Case's and Hoffman's desire to create a safety group including only the large Trust Members. He attended the meeting at Johnson's home where the discussion got heated on this topic. The safety group was not pursued.¹¹⁵

Concerning underwriting guidelines, Gosdeck said that PRM relied on the information provided by MPA to bring in new Members and the Trustees approved new Members based on the representations from MPA and PRM. He noted that, on occasion, proposed Members would not be approved and he recalled few complaints from Trustees, other than those cited previously, about inappropriate Members being admitted.

Gosdeck acknowledged that the Trust had a retention plan early on, but the Trustees wanted it discontinued. He noted that existing retention Members could remain in the program but no new members could be enrolled. He noted that the contribution rates were approved by the Trustees based on the reserve and financial information presented to them by PRM. He thought there may

¹¹⁴ BST obtained a copy of the E&O policy in question.

¹¹⁵ Gosdeck said SIF, at the time felt safety groups for human services agencies were not profitable but has since established such a group.

have been a standard discount of up to 5%. He said the Trust paid the Members' NYS Health Care Reform Act Assessment. There were no Member dividends paid.

Trustee Lasicki similarly indicated that MPA was the Trust's exclusive marketer and also handled property and casualty coverage for a number of ACL members. She said that Case and Hoffman knew her membership well, and she knew both Case and Hoffman before she joined the Trust's Board. She said Case and Hoffman "seemed to be competent." She did not recall the specifics of MPA's marketing agreement nor seeing any marketing brochures produced by MPA for the Trust. She indicated that during the Trust's final years, the Trustees were pushing Hoffman and Case for a succession plan as they both were getting older. MPA's marketing efforts were getting more and more limited to the NYC area, and the Trustees wanted a broader state-wide presence.

She stated that initially the Trust was "Arney's and Morty's Trust" and the Board of Trustees fought to take control, telling them "you don't own the Trust." She recalled Case referring to the Trust as the "Case Retirement Insurance Saving Plan."¹¹⁶

Lasicki confirmed that when PRM wanted to purchase the marketing rights from MPA, the Board asked Case for proof of MPA's E&O insurance policy. Case and Hoffman would not produce the documents. When they finally did, it was found the policy was inadequate.

Trustee Hardiman characterized Case as a "typical insurance guy" who told a lot of stories. He would occasionally breach Members' confidentiality. Case would refer to the Trust as "my Trust" saying that he put up the money to start the Trust. She stated that MPA did a good job in the early years, and the Trustees wanted them to have more of a statewide presence. This became more of an issue after 9-11 when downstate insurance rates increased. She stated that MPA did not market well upstate, particularly in the later years, though MPA did have a booth at the statewide agency conferences. Hardiman stated that MPA did not seem to be interested in smaller agencies but rather the larger ones where they could earn higher commissions. She noted the Trustees were also concerned about MPA's lack of a succession plan.

Hardiman recalled that the Trustees had requested from MPA their E&O policy on a number of occasions, and when it was finally provided the policy was found to be deficient. She did not recall the specifics.

Campanelli stated that MPA felt that the Trust was over-reserving and that higher reserves would result in higher assessments that would not be good for marketing. He noted that MPA convened a small group of members to explore forming a safety group, but the Trustees disapproved this

¹¹⁶ Concerning this purported comment, Case, through his legal counsel, stated the following to BST: "This was a stupid (intended to be funny) joke of no merit or consequence to the Trust. Nothing was ever done, no activity ever undertaken with respect to the operation of CRISP to denigrate or disavow the basic purposes of benefit of the Trust, or for any special advantage of Mr. Case. MPA did not take a penny from the Trust, other than its marketing fees paid by PRM at the rate (or less than the rate) provided by the Marketing Agreement."

when they found out. He said MPA recommended Members with questionable premiums. He also understood that MPA did not have the required E&O policy and that Johnson and Gosdeck asked MPA to review their E&O policy a number of times. He was surprised that NYS law allowed brokers to collect premiums in perpetuity. Campanelli said he was not involved in PRM's purchase of MPA's marketing rights but felt it was a good move.

Campanelli's aforementioned statement regarding the negative impact assessments would have on the Trust's marketing efforts is illustrative of the mindset that contributed to the Trust's demise. Campanelli, as Trustee, should have realized that new Members or a large group do not necessarily equate to a better Trust, or better benefits for its Members. In fact, there is no such correlation. The increase in Trust size primarily benefitted MPA and PRM, as they received a percentage of the premium for every new Member that joined the Trust. From the Trust's perspective, a Member's premium should have been adequate to cover the Member's individual losses as well as a portion of the Trust's administrative costs.

Certainly the Trust documents do not make any reference to the Trust being a for-profit organization trying to increase Trust earnings, and if it was, the earnings theoretically should have gone toward the reduction in the Members' premiums as the Members were technically the owners of the Trust. Campanelli should have realized that an increase in reserves is essentially a move to reflect the expected claims against the Trust, and accordingly means Member assessments should be levied to keep the Trust out of a negative Member deficit position, something that could drive the Trust into insolvency - much like this Trust eventually experienced after having realized Member deficits in all but one year of its existence.

BST obtained a copy of MPA's E&O policy issued by Lloyd's, London dated November 19, 2008, for the period August 26, 2008 to August 26, 2009 (Exhibit 11) to determine its compliance with the Marketing Agreements (Exhibits 6 and 9).¹¹⁷ The insured parties are M.P. Agency, Inc. and Mus'ic, Inc.¹¹⁸

Section XII(b) of the Marketing Agreement requires MPA to "continuously and without interruption" maintain Broker's E&O insurance coverage "in the face amount of not less than \$2,000,000 per occurrence and \$2,000,000 in the aggregate." A review of the policy revealed that the limit of liability was \$1,000,000 per occurrence and \$1,000,000 in the annual aggregate, or 50% less than the required coverage limits set forth in the Marketing Agreement.

In addition, and perhaps of greater potential financial consequence to the Trust, the policy covered MPA's professional services relating "Solely in the performance as a marketing

¹¹⁷ The policy showed a retroactive date to August 26, 2004.

¹¹⁸ The policy also includes JLS Group, Inc. as an additional insured "but only as respects coverage for claims taht (sic) arise directly from marketing services performed by M.P. Agency, Inc (sic)" NYS Department of State records show Mus'ic, Inc. is a domestic business corporation formed on January 9, 2004. The Chairman/CEO is listed as Morton G. Case. MPA advised BST that Mus'ic, Inc. is an "entity with a business activity related to unemployment insurance which is in no way connected to CRISP or the subject of WC." JLS Group, Inc. was also named as an additional insured.

consultant.”¹¹⁹ The policy contained a Manuscript Endorsement as follows: “Excluded coverage for all claims arising out of insurance agent/broker related services.” In effect, no E&O coverage existed, at least for the period August 26, 2007 to August 26, 2009¹²⁰ for acts committed by MPA in its role as the Trust’s NYS licensed insurance broker.

A “Miscellaneous Professional Liability Application” on the letterhead of Hooghuis, Inc., a Mineola, New York-based professional liability specialty firm, was attached to the E&O policy obtained by BST. BST identified a number of noteworthy entries on the application.

Question 6 of the Application requests a detailed description of the services or business activities to be provided for which coverage is requested. The responses states that the services include marketing of workers’ compensation, unemployment insurance, and statutory disability insurance, primarily for non-profit social service type organizations.

Question 19 asks if the applicant uses a written contract to perform services for all clients. The “Never” box was checked, apparently in contradiction to the existence of a signed Marketing Services Agreement between MPA and CRISP.

Question 23 relates to existing professional liability policies. The response indicates the current policy expired on August 26, 2008, and carried the same \$1 million/\$1 million dollar limits of the policy renewal. This would suggest that the preceding policy did not meet contractual requirements as well. The expired policy is reported to have a \$2,900 annual premium. A sub-question relating to the length of time the coverage has been continuously in force was unanswered.

Also, MPA was required to “upon request provide reasonable evidence to the Trust and the Program Administrator that the said assurances is (sic) in place as required by this paragraph and shall provide immediate written notice to the Trust and Program Administrator of termination or material amendment of any such policy.” As noted, it was reported to BST that MPA failed to respond in a timely fashion to the Trustees’ request to provide a copy of the required E&O policy.

BST requested MPA to comment on the issues of concerns raised by the Trustees and their Counsel.

BST asked MPA to confirm if it had the required E&O policies in place and to provide copies of the policies. MPA responded as follows:

During most of the full term of the Marketing Agreements, MPA through JLS

¹¹⁹ As noted above, at the Trustees meeting of January 23, 2009, Case and Hoffman indicated to the Trustees that that they had “secured a separate E&O policy for their CRISP marketing activities.”

¹²⁰ The E&O insurance application indicates that a preceding policy expiring August 26, 2008 was in place carrying the same \$1 million policy limits. Therefore, assuming the preceding policy was for a one-year term, it appears that that MPA did not comply with the provisions of the Marketing Agreement for a minimum of two years.

Groups carrier maintained \$5,000,000 of E&O insurance coverage.¹²¹ When the relationship with the JLS carrier changed, MPA purchased \$1,000,000 per occurrence of E&O insurance coverage for the CRISP Trust activities.¹²² There was never a single claim or even a suggestion or threat of a claim by any Member with respect to any alleged or claimed error or omission by MPA in fulfilling its marketing activities for the Members at large or any of them.¹²³

Based on the evidence, MPA did not have in place at all times the required Broker's E&O insurance coverage in the face amount of not less than \$2,000,000 per occurrence and \$2,000,000 in the aggregate as contractually required. The fact that no claims were filed is irrelevant in BST's opinion.

Relating to MPA succession planning, MPA informed BST that it provided to the Trustees "a workable plan relating to a Safety Group." MPA provided to BST an April 2009 letter entitled "CRISP Board Meeting - 4/17/09, Succession Planning, Re: State Fund Safety Group Proposal" addressed to the Members. The letter cites the Trust's deficit and describes the detail of MPA's forthcoming proposal to the CRISP Board concerning formation of such a group. MPA considered this proposal to be a viable response to the Trustees' request for a succession plan that the Trustees rejected. The Trustees rejected this proposal.¹²⁴

Regarding the Trustee's rejection of this proposal, MPA offered the following comment:

This is a matter of opinion only. The CRISP Board of Trustees rejected MPA's recommendation of a Safety Group and then essentially terminated MPA as the Marketing Agent. It seems to MPA that a more highly experienced Board of Trustees, with a "hands on" approach to marketing and managing the program to attract new applicants would have made the switch to a Safety Group, long before CRISP became impossible or impracticable to continue as a fully funded Trust. We further believe the transfer of the Marketing function to PRM was erroneous. PRM's CEO

¹²¹ We were not provided with a copy of the JLS policy and, therefore, cannot determine the validity of this representation. In addition, we were not advised of the exact dates of MPA's purported coverage by JLS' policy.

¹²² Trustee minutes for January 23, 2009 indicate that Case reported to the Trustees that MPA "would leave JLS offices and relocate, either with another agency or on their own."

¹²³ MPA did not furnish copies of any E&O policies.

¹²⁴ Chair Johnson and Gosdeck advised BST that the meeting referenced in this document occurred at her apartment in NYC on or about April 17, 2009. Johnson said she arranged the meeting with MPA, Gosdeck, and some Trustees after MPA had approached Trustees Campanelli and Pierri without the Chair's or other Trustees' knowledge about setting up a Safety Group with the State Insurance Fund for only the larger Trust Members. Johnson and Gosdeck felt it was inappropriate to explore options for only the larger Members at the expense of the smaller Members. Gosdeck felt it would have been a breach of the Trustees' fiduciary duty to only consider an option for larger Members of the Trust. Moreover, Johnson and Gosdeck noted that they had already gone to the State Insurance Fund previously and were advised that the Fund would not entertain a Safety Group for human services agencies at that time. The Safety Group was not pursued any further. MPA denies there was ever "any discussion as to the size of CRISP accounts which would be eligible for the Safety Group." MPA said there was discussion of 100% participation, but this was not realistic due to individual loss histories and payroll categories.

was based in Oregon, more than 3000 miles away from the situs of the Trust.¹²⁵ PRM had little visibility with the State WCB, less experience than MPA, and was unknown to the primary social service associations which were the basic source of referrals of new members. MPA attended the key association meetings. PRM did not.¹²⁶

With respect to the Trustees' reported concerns about its failure to maintain an adequate organizational structure to support the Trust's growth, MPA noted that there was "never any indication that a larger marketing organization was needed or desired." MPA reiterated the impact on downstate marketing after 9/11. MPA said that the size of its organization was not a limitation and that there was no request for a larger or different marketing organization until approximately 2007.

Concerning the sale of its marketing rights to PRM, MPA stated the following:

Mr. Case and counsel recall that Janice Johnson, the Chairperson of the CRISP Trust, wanted to end the Marketing Agreement without complying with the requirement that CRISP compensate MPA for Members introduced to CRISP by MPA post-termination. In any event, Ms. Johnson, and the balance of the Trustees wanted PRM to be the successor firm as Marketing Agent. While fashioned as a sale, what really happened was that MPA was being replaced by PRM, and MPA compromised as to the post - termination compensation due to it.

In light of the Trust's chronic deficit position, BST inquired of MPA whether or not the Trust's audited financial statements were routinely distributed to the Members. Such distribution would have alerted the Members to the Trust's financial condition, the implications thereof to their potential joint and several liability obligations, and if continued participation in the Trust was in their best business interest. MPA advised BST through counsel that to the best of their recollection the statements were sent to all Members in the Trust's first and perhaps second years. Thereafter, MPA recalled it doubtful if the statements were sent "automatically," but rather were made readily available to the Members or their accountants upon request or when MPA met with existing or prospective Members. MPA indicated it was "commonplace" for Members to request and receive the statements. MPA further noted that the audited financial statements were reviewed for Trustee approval at the March meeting and that all Members represented on the Board of Trustees had the chance to review the document as well as other Member representatives who may have been in attendance or requested a copy.

The apparent availability of the audited financial statements to the Members notwithstanding, BST believes that the routine distribution of this important document to all Members would have provided the Members a means to annually evaluate the Trust's financial condition.

¹²⁵ BST believes this relates to the relocation of PRM's Executive VP Ed Sorenson to Oregon in response to a personal matter.

¹²⁶ Thomas Arney and his related firms had been involved with WCB self-insurance programs since the mid-1990's.

In summary, the documents examined and the interviews reveal the following:

- The marketing strategy employed by the Trust and MPA resulted in a dramatic growth in membership during the Trust's early years particularly. MPA's Member recruitment effort was productive in the downstate New York area and less so in the upstate and western regions of New York State.
- MPA did not provide an acceptable or timely succession plan as requested by the Trustees to ensure continuity of the Trust's marketing activities after MPA's principals' departure from the firm.
- Despite losses and Member deficits in all but one year, the Trust Chair and Trustees did not review or order a review the Trust's underwriting criteria.
- MPA failed to produce suitable evidence that it "continuously and without interruption" maintained E&O insurance coverage "in the face amount of not less than \$2,000,000 per occurrence and \$2,000,000 in the aggregate" as required by Section XII (b) of the Marketing Agreement. Evidence suggests that MPA was not in compliance with Section XII (b) at least for the period August 26, 2007 to August 26, 2009 and, therefore, may have been in breach of its contractual obligations with the Trust in this regard during this period.
- MPA continued to renew Member policies with the Trust from 2000 through 2004 despite the fact that the Trust had multi-million dollar Member deficits during each of those years.
- MPA did not routinely provide prospective Members copies of the Trust's financial statements (which revealed large Member deficits), nor did they routinely provide the Trust's financial statements to Members who decided to renew their policies.
- On at least two occasions, MPA provided inaccurate underwriting information to PRM, resulting in the admission of certain Members that otherwise may not have met the Trust's criteria for admission.

G. Underwriting

Prudent business practices dictate that underwriting criteria be established, documented, and re-evaluated over time. We examined materials provided by PRM, MPA, and other parties, and determined that underwriting guidelines were established but inconsistently applied over the life of the Trust. Our ability to fully evaluate this critical operational component was hampered by our inability to interview representatives from PRM or to obtain PRM's internal underwriting guidelines. We did receive written responses from MPA to underwriting-related questions submitted by BST through MPA's legal counsel.

Article VI, Section 2 of the Trust Agreement states the following concerning the consideration of new members into the Trust:

The Trustees, after the inception date of the Trust, shall receive applications for membership from prospective new members to the Trust and shall consider such application for membership in accordance with the Rules for Self-Insurance, the terms of the Indemnity Agreement, and the rules and regulations established and promulgated by the Trustees for the admission of new members to the Trust. The Board of Trustees may delegate the ministerial authority for membership approval to the administrator or such other person as they select. For the purposes of this Section “ministerial authority” shall be construed to mean the authority to screen applicants for membership in the Trust, make a recommendation to the Trustees in accordance with the standards established by the Trustees and to execute documents on behalf of the Trust upon the written consent of all or a majority of the Trustees. All members of the Trust shall specifically acknowledge that they are jointly and severally liable for all claims made against the Trust. Members may terminate membership in the Trust only on the anniversary date of membership.

Article III, Section 2 of the Trust’s By-Laws states:

Additional members may be added to the Trust by vote of the Trustees of the Trust, in accordance with these By-laws and any applicable regulations governing the group self-insurance trust as adopted from time to time by the Workers' Compensation Board of the State of New York. To qualify for membership and to continue to be eligible for membership, an applicant must be a provider of community residence services and satisfy the following underwriting criteria:

- [i] A prospective member must be financially solvent, and must meet such other criteria as to financial qualification and otherwise as may be established by the Trustees;
- [ii] a prospective Member's expected loss rate must be within the parameters as determined from time to time by the Trustees;
- [iii] a prospective Member must satisfy all other requirements of the Fund's excess carrier or carriers, the Workers' Compensation Board of the State of New York; and
- [iv] A prospective Member must adhere to the safety policies and practices as outlined in the policies adopted by the Trustees from time to time.

Article III, Section 5 of the By-laws gives the Trustees sole authority to approve or reject new members as follows:

The approval or rejection of any application for admission by a prospective additional Member shall be subject to the sole and unfettered discretion of the Trustees, notwithstanding the qualification of the applicant and the satisfaction of the requirements of these By-laws and applicable rules and regulations, and the Trustees may approve or reject any such application for any reason, and no applicant shall be deemed to have any legal or equitable entitlement or right to membership in the Trust.

Based on these governing provisions, the Trustees had the authority to select new members from among eligible agencies and to establish their own selection criteria within the parameters established by their excess insurance carrier and applicable laws and regulations. Ministerial authority for such approval could be delegated to the Group Administrator or another third party “provided that such administrator or person designated is not an owner, officer, or employee of a third party administrator.”

Interviews and documents reviewed indicated that the Trust established underwriting criteria and that the Trustees had ultimate sign-off on the admission of new members based upon financial, loss and other information provided to them by MPA and PRM. The underwriting criteria was not memorialized and updated in a formal, standalone document, but rather documented in Trustee minutes and miscellaneous correspondence.

A Trust document prepared by Arney dated October 26, 1996, provided to a newly-appointed Trustee a flow chart relating to the underwriting process. The chart shows that MPA had primary responsibility for identifying prospective Members and obtaining preliminary workers’ compensation and operational information from the applicant. PRM then would review the information, and based on available information, prepare a preliminary qualification and issue a proposal to the applicant subject to the review and approval of any additional required information. If the applicant wished to proceed, MPA would then obtain loss and financial data and forward it to PRM for review. If the applicant met the underwriting standards, PRM would then fax the Trustees a worksheet with a summary of information for their comments and approval/disapproval. If the applicant was approved, PRM would prepare the policy documents, Trust booklet, and premium financing agreement and forward them to MPA which would collect the down payment from the applicant and deposit the funds in the premium financing account. The executed documents were then sent to PRM which then issued the insurance certificates and notified the claims administrator and WCB of the new Trust member.¹²⁷

¹²⁷ MPA reported to BST that “PRM gave MPA limited and specific instructions as to the MPA’s gathering of information relative to the PRM and Board determinations of an applicant’s suitability for membership.”

This document also provided the new Trustee with a copy of the Trust’s underwriting guidelines as follows:

Description of Facilities to be Covered:

Generally, a “not-for-profit” social service agency, providing residential care facilities and other human services. Size of residences will vary, from small, specifically devoted, temporary residential facilities of 10-14 beds, to larger, multiple location facilities with residential facilities from short, temporary, midterm (periods longer than 30 days) and SROs, to continuous long term living arrangements.

An “average” facility will have 60-110 beds, employ from 75 to 100 full-time or full time equivalents, working in congregate and scatter locations. Most providers offer other services as well, either for people with mental illness and/or other disadvantaged population. These may include residences, day treatment programs, vocational training and/or Case Management

Underwriting Standards

1. Must be a “voting” member in good standing of either ACL (Association for Community Living) or ESAA (Empire State Association of Adult Homes). Must provide a copy of their license from either DOH or OMRDD.
2. Must have been in operation for a minimum of three years and present financial documentation of such operations.
3. Financials must meet the review of the Trust’s consulting CPA, Roth & DeChants.¹²⁸
4. Must provide a minimum of three (3) years loss experience from the current carrier. Authorization letter to the NYCIRB and complete File History Reports as well as the latest Experience Modification calculations will be obtained.
5. Current Experience Modification cannot exceed 1.35%.
6. Must provide a copy of a current workers’ compensation policy.
7. Three-year loss ratio must be 50% or better.

¹²⁸ It is interesting to note that the Members’ financial statements had to be reviewed and approved, yet the Members were not provided (before joining the Trust) with copies of the Trust’s financial statements which revealed large Member deficits.

8. Must meet the minimum loss control standards to be established by the Trustees within the first year of operations.

9. All locations with more than 100 beds will be physically inspected by the Trust's Director of Loss Control. Every agency will be subject to a first year on-site review by the Director of Loss Control.

10. Any agency with a "serious loss" within the last four (4) years will be surveyed prior to acceptance. Serious loss will be at the discretion of the Program Administrator, but will include any incident for which a reserve and/or payment exceeds \$100,000. Losses or trends of losses will be carefully reviewed for current/proposed rating adequacy.

BST was unable to obtain a copy of any subsequent detailed written underwriting guidelines.¹²⁹ Trustee minutes reflect periodic general discussion of underwriting-related issues, but do not report any detailed discussions of underwriting criteria or substantive revisions to the criteria noted above throughout the life of the Trust.¹³⁰ However, minutes and other documents do reveal periodic modifications to criteria with respect to the types of agencies permitted to join the Trust. For example, an amendment to the By-Laws in May 2004 substantially expanded eligibility from providers of "community living" to "community living and residence services or community mental hygiene treatment of rehabilitation services, special needs educational services programs and other social services programs."

Johnson confirmed to BST that underwriting criteria was developed by PRM and MPA early on but was never revisited by the Board of Trustees. She was not sure whether the guidelines were ever reduced to written form, but she said she had no reason to believe there were any problems with Member underwriting. Johnson stated that the Trustees approved all new members based on representations made by PRM and MPA. She recalled some proposed members being denied membership. She recalled "fights" between MPA and Sorenson relating to the risks posed by some proposed members.¹³¹

Gosdeck advised BST that the Trustees relied on information provided to them by PRM and MPA on new member applicants. He recalled Case and Mark Crawford from PRM having

¹²⁹ BST did request a written copy or description of underwriting guidelines from both PRM and MPA through their respective legal counsels. None were received. MPA did provide an underwriting flow chart but no written underwriting eligibility criteria.

¹³⁰ Members interviewed had no recollection of the Trust's underwriting criteria.

¹³¹ The occasional "disagreement" between PRM and MPA relating to new member underwriting is exemplified in a memorandum, dated June 25, 1999 wherein Arney reminds Case that "...we can use additional discounts where we feel the risk warrants it..." and that "...we are willing to use the additional discounts to acquire "important" clients for the Trust." However, Arney goes on to say, "We particularly cannot use them when we have absolutely no underwriting data. A 'clean copy of the current policy' does not constitute underwriting data. Where we have the complete loss data and sufficient rationale AND some reasonable level of premium to work with, we will consider using the additional discount." Arney concluded by advising Case that only Arney himself could approve additional discounts to acquire a new member.

disagreements about new member referrals that were high risks. Gosdeck confirmed Johnson's previously-referenced statements relative to DDI, and further asserted that Case had deliberately understated the payroll for "Palm Beach Gardens" when referring the agency for membership. Gosdeck noted that when the payroll audit found the payrolls had been understated, the agency immediately came in and paid what was owed. Gosdeck noted that, on occasion, a proposed member would not be approved.

Gosdeck said the Trust had a retention plan early on, but the Trustees wanted it discontinued. He noted that retention members could stay in the retention program but no new members could be enrolled.

Trustees Hardiman and Lasicki confirmed Trustee approval of members based on the information presented to them by MPA and PRM.¹³² Neither recalled the specifics of the Trust's underwriting guidelines. Hardiman said there was "tension" between MPA and PRM, as MPA wanted to sometimes bring in marginal members. She felt MPA may have been "puffing up" the backgrounds of some proposed members. Hardiman further noted that MPA did not seem to be interested in smaller agencies, but rather larger ones that produced higher commissions.

MPA informed BST that as far as it was aware, PRM and the Trustees "always adhered to the underwriting criteria they adopted" and that the Trustees "had the final say as to each and every applicant." Concerning the accuracy of information it provided to the Trust on prospective members, MPA indicated that the following:

The information MPA delivered pursuant to its responsibilities was always accurate and no one ever claimed throughout MPA's tenure as Marketing Agent that it was less than fully accurate. On occasion, additional background information on applicant or applicant renewal would be requested by PRM staff before a quote could be released or coverage bound. Requests were always processed by MP staff if the client was cooperative.

BST examined the assertions that MPA had misrepresented the loss history for the Developmental Disabilities Institute (DDI). Trust records show that DDI was a Trust member from June 1, 2006 through October 13, 2010.¹³³ Records indicate that DDI's experience modifier was 1.37 in 2006 and steadily increased to 2.00, or 46%, by 2010¹³⁴, suggesting that DDI's losses grew substantially during its tenure with the Trust.¹³⁵

¹³² Trustee Campanelli did not recall the Trustees' approval of new members.

¹³³ We did not have access to the agency's application loss information.

¹³⁴ We have yet to ascertain why DDI was allowed to remain in the Trust when its experience modifier was clearly in excess of the allowable amount.

¹³⁵ DDI's Application for Participation, GSI-1.1, was signed by DDI's Executive Director Peter Pierrri on June 29, 2006. Mr. Pierrri later served as a Trustee from approximately November 2008 until May 2009. Mr. Pierrri was succeeded on the Board of Trustees by DDI's new Executive Director, Mr. John Lessard who served from September 2009 until December 2010.

With respect to the assertion that it deliberately misrepresented DDI's loss history, MPA denied that DDI's losses "were understated at any time." MPA indicated that DDI itself had employed an insurance consultant who "provided PRM with prior carrier loss runs and they were, as far as MPA knows, true, correct and complete." In addition, MPA noted that CRISP's safety officer visited DDI fifty-one (51) times in the first year that DDI was in the Trust.¹³⁶ MPA indicated that there was "no question then raised about discrepancies, if any, of loss experience reporting by DDI. This account made a \$1,200,000 contribution to the Trust. It was an important and valued account." MPA further asserted that in 2010, the "...Chairperson and PRM allowed DDI to withdraw from the Trust in the middle of a Trust Year and to receive a refund of in excess of Seven Hundred Thousand Dollars (\$700,000)."¹³⁷

With respect to the purported issues involving "Palm Beach Gardens" records suggest the agency in question is Palm Gardens Care Center, LLC, a Trust member from October 1, 2008 through December 31, 2010. Payroll audit records indicate that for the 2008-09 and 2009-10 policy years, the agency's payrolls were understated by a total of \$9,696,048, or by 48%, while earned contributions for the period were understated by \$213,123, or by 60%.

Concerning Palm Gardens, MPA advised BST that in 2008, it received an Acord insurance form from Oxford Insurance Brokerage certifying the payrolls of Palm Gardens by category that MPA forwarded to PRM. MPA noted that Palm Gardens had been an applicant for membership in the Trust in prior years but was rejected because it was then in bankruptcy proceedings for reorganization. MPA stated that it later heard Palm Gardens' "payroll numbers turned out to be understated" but did "not know that for a fact." MPA recalled that Palm Gardens "had no, or virtually no, losses, for the period in question, so the Trust and other Members actually significantly benefited from having (Palm Gardens) as a member." Records show that Palm Gardens had an emod of .69 during its tenure with the Trust, supporting MPA's assertion relating to Palm Gardens' low loss experience while a Member of the Trust.¹³⁸ It remains unclear why MPA did not attempt to determine if the payrolls had been understated when alerted to such. Regardless, Palm Gardens' failure to report its true payroll denied the Trust of certain Member

¹³⁶ Trustee minutes for December 13, 2006 report: "Sorenson reported that it has an approximately 30% loss ratio and is cooperating very well with the efforts of the CRISP loss control and claims team."

¹³⁷ Trust records show that DDI's last policy year ran from June 1, 2010 to June 1, 2011 and that DDI left the Trust voluntarily to obtain alternate coverage effective October 13, 2010, approximately 2.5 months before the Trust's dissolution. Chair Johnson confirmed to BST that DDI was allowed to leave the Trust during a policy year contrary to Trust policy and that DDI did receive an approximate \$700,000 pro-rated premium refund. Johnson recalled that DDI's President, John Lessard, also a CRISP Trustee, approached her saying that he needed to have insurance in place by September 2010. Due to the uncertainty of the Trust's future at the time, Johnson said she agreed to allow DDI to leave the Trust without penalty. She noted that this option was available to other Members but was "not publicized." She thought perhaps one other Member was allowed to leave in a similar fashion but was not sure. Johnson felt MPA was upset as they lost 6.25% commission on this large account.

¹³⁸ In response to MPA's comments regarding Palm Gardens, Johnson recalled that Ed Sorenson met with Palm Gardens after the payroll issue was discovered. When Sorenson asked why the numbers were not accurate, Palm Gardens said no one verified or asked about their accuracy. Johnson felt it was MPA's obligation to do so.

contributions that were never collected, nor pursued by MPA, PRM or the Trustees - despite their apparent fiduciary duty to do so.

As discussed above, Article VI, Section 6a of the Trust Agreement prohibits the Trust’s fiscal agent administrator and/or administrator from being an owner, officer, or employee of a third-party administrator. Therefore, based on the role delegated by the Trustees to PRM in the underwriting process and the concurrent role played by CSI, a claims administration firm also controlled by PRM’s principals, it would appear that the Trustees violated Article VI, Section 6a of the Trust Agreement. The inherent conflict of interest was manifested by the under-reserving by CSI and the absence of disclosure by its affiliated firm, PRM. Had the program administrator been a truly independent entity, perhaps the under-reserving would have come to light sooner.

BST determined that at least 20 Members had experience modification rates greater than 1.35 in their initial year of membership, including 9 who had experience modification rates (emod) equal to, or greater than 1.50. The admission of these Members would appear to have violated the Trust’s underwriting guidelines.

Industry experts interviewed (including an actuary) stated that it is not an industry practice to keep the same experience modification rate for several years. However, as reflected in Table 1, our analysis of the Member files revealed that 114 Members retained the same emod for at least three (3) consecutive years, including 15 members retaining the same emod for at least ten (10) consecutive policy years.

Table 1: Consecutive Years of Unchanged Emod

<u>Consecutive Years</u>	<u>Number of Members</u>
3	49
4	20
5	8
6	9
7	5
8	6
9	2
10	6
11	1
12	3
13	2
14	1
15	2
Total	114

Source: CRISP Member Files

This analysis would strongly suggest that the emods were arbitrarily assigned or assigned based on some other unknown criteria for these Members, rather than being based on the Member's actual loss history during the preceding year and may have resulted in the Members not being charged premiums consistent with their loss history.

In addition and of more significance, a number of Members were allowed to remain in the Trust despite having consecutive years of emods beyond the underwriting threshold of 1.35. This will be discussed in more detail in Section M: Renewal.

In summary, the documents reviewed and the interview results show that:

- The Trustees failed to develop underwriting guidelines that were periodically reviewed or modified to reflect the Trust's changing market and financial conditions.
- The Trustees and PRM failed to document in an appropriate form, the underwriting and membership approval process.
- The Trustees approved new Members based upon the representations made to them by PRM and MPA concerning applicants' appropriateness for membership.
- MPA provided to the Trustees and PRM inaccurate applicant information which was relied upon by the Trustees in good faith to make membership decisions.
- Chair Johnson agreed to allow DDI, a Trustee Member, to leave the Trust without penalty and receive a refund of prorated contributions in violation of Trust policy. This opportunity was not equitably offered to other Trust Members seeking alternate coverage at the time the Trust was about to dissolve.
- The Trustees and PRM failed to collect premiums due to the Trust in relation to a Member that understated their payroll.
- Members were encouraged to join the Trust despite the fact that the Trust was in a Member deficit position, and Members were not routinely provided with copies of the Trust's financial statements.
- Members with experience modification rates exceeding the Trust's underwriting guideline of 1.35 were admitted to the Trust and were allowed to remain in the Trust despite continuing losses and experience modification rates exceeding 1.35.

H. Discounts

Premium discounts are typically one of the methods used to lure potential members into a group self-insured trust. Given the highly competitive market for workers' compensation insurance, it was important that CRISP offer competitive discounts to prospective members and current Members, especially those with low loss rates. The success of any group self-insured trust is, in part, due to the ability to attract and retain members with low loss rates with the hope that the discounts will be offset with efficiencies realized over the long-run, provided the Members' cumulative loss rates do not materially increase.

Section 317.7 of the NYCRR (effective January 31, 2001) states the following:

“The contribution rates utilized by a group self-insurer shall not be inadequate or detrimental to the solvency of the group.”

Premium discounts are typically given to trust members based on their individual loss histories with higher discounts going to those members with fewer claims and lower aggregate losses, and serve as an incentive for members to emphasize safety and loss control efforts. BST found that discounts were provided to new and existing Trust Members on a discretionary basis.¹³⁹

Chair Johnson advised BST that the Trustees relied on PRM and MPA to set the appropriate contribution rates.¹⁴⁰ She indicated that when the Trustees asked about rates at one point, they were told that PRM and MPA were giving discounts and retention plans to certain Members that the Board did not know of or authorize. Trustees were also informed the retention plans would be stopped, but they were continued for some Members. Discount rates aside, it would appear that the Trustees should have gotten more involved in the discount or underwriting process, or at least reconsidered other trust administrators given the fact that the Trust was regularly realizing Member losses and regularly had a Member deficit - which was more than likely caused by insufficient Member premiums, unrealistic discounts, questionable underwriting, renewal of Members with large losses, or a combination of two or more of the above.

Johnson indicated that premium discounts were given to attract new Members in the early years, even though the Trust was operating at less than breakeven. She said the Trustees allowed 5% of the membership to receive discounts up to 10% at PRM’s and MPA’s discretion, resulting in 95% of the Members receiving no discounts. Johnson stated that in the first year or two some Members received discounts up to 50% without the Trustees’ knowledge. The Trustees finally asked why the deficit remained the same and were then advised of the discounts. As previously noted, there is no financial disincentive for PRM to offer premium discounts as they are paid a commission based on the Members’ undiscounted premium, and they have no obligation to reimburse the Trust when the claims expenses exceed the discounted premiums.

Johnson said the Trustees never knew what discounts a specific Member received. She noted that the Trust also paid the Members’ WCB annual assessment. Johnson believed the discounts given by PRM and MPA, and lack of adequate premium ultimately precipitated the Trust’s deficit.

¹³⁹ There were no dividends paid to Members as the Trust was consistently in a deficit position with no “excess” funds to distribute.

¹⁴⁰ MPA advised BST that it had no role in setting contribution rates and that PRM fixed the contribution rates, presumably based on WCB’s promulgated rates that served as the basic guideline and starting point. MPA stated that the Trustees had to approve rates and any variations from these basic rates. MPA said it had no reason to believe that the contribution rates were inadequate at the time. MPA noted that it was “PRM’s function to establish contribution rates, and PRM, not MPA held itself out as having expertise in that area.”

Gosdeck recalled a standard discount of up to 5% and that the Trust paid Members' WCB annual assessment. Trustee Hardiman did not recall if premium discounts were given to Members. Trustee Lasicki recalled some discussions in the early years regarding Member discounts and that Case was "pushing discounts." She said the discounts were reduced over the years. Trustee Campanelli said he learned later on that Members were given discounts and that the Trustees put a stop to it.

BST found little documentation for the Trust's earlier years regarding Member discounts. An internal PRM memorandum from Arney dated May 8, 2001 states, in part: "The maximum discount to be applied to any account is 25%-new and renewal." BST was unable to identify individual Member discounts based on available documents.

Minutes reflect little reference to Member discounts until February 22, 2001, when the Trustees discussed the advisability of ending discounts for participants with bad experience ratings. The Trustees unanimously approved "the underwriting plan with the understanding that in the normal case of an average long-term participant from an underwriting perspective a twenty-five percent discount is the expectation with the ability to seek approval to increase it in appropriate cases and to both reduce the discount and impose a penalty of up to an additional 25% of contribution especially in cases that have operated at a contribution deficit with additional review for participants with a loss ratio of greater than 50%..."

At the meeting of October 26, 2001, the Trustees were advised that "in unusual cases, with the approval of Sorenson discounts of up to 10% were offered but that in most cases the only incentive was the fact that participants do not have to pay the WCB assessment which currently exceeds 14%."

During the meeting of January 31, 2002, minutes report that Sorenson indicated to the Trustees the following with respect to discounts: "...discounting policies often tie PRM's hands with respect to very good applicants. He suggested that two issues are paramount in this regard. These are determinations of how much potential income is being affected and how the Workers' Compensation Board will view the discounts given CRISP's present financial situation." Case added that "...he needs the discretion to offer discounts of up to 20% and that the final decision lies with Sorenson" and that "...there are often negotiations regarding the amount of any discount between these entities." In response, minutes state that the Trustees "expressed concerns that some discounts may be exceeding the discretion given by them at earlier meetings and asked Gosdeck to provide copies of appropriate minutes to them. They also indicated a desire to honor commitments that have already been made by Case and approved by PRM." The Trustees directed PRM to "undertake an analysis of what discounts have been offered, develop a model for trustee consideration that will serve as the basis for CRISP discount policies and a cap for the maximum permissible discount and report quarterly to the trustees on all discounts offered."

At the meeting of March 7, 2002, Sorenson explained the current discount policy in effect for current renewals as follows: “If a discount is believed necessary by Case and Hoffman to ensure the renewal of a participant who has been a member with a good loss ratio, a discount of up to ten percent is offered from the rate that would otherwise be quoted. Crawford reported that forty-nine renewals made since July have included some level of discount.” The Trustees found this practice to be acceptable “as long as the discount is tied to performance...”

At the meeting of December 9, 2002, Sorenson advised the Trustees that “only the state assessment, which has dropped from 14.5% to 13.1%, was being offered except for a discount of up to ten percent when required to keep existing members with good claims records in the trust.”

It is important to note that discounts, albeit targeted to good performing Members, were being awarded in the face of the Trust’s consistent deficit position, which continuously exceeded \$3.2 million from 2000 through the end of 2004.

As a result of the Trust’s GAAP deficit of \$5,365,964 and Regulatory deficit of \$7,535,415 as of November 30, 2003, the Trust entered into a Consent Agreement with the WCB on August 2, 2004. The Agreement included a provision whereby existing Members would be charged the full manual rates with the exception of 51 Members already receiving discounts of 5% or 10% whose discounts could not be increased. The Trustees were given the discretion to offer up to ten (10) existing Members a discount of no more than 10% upon renewal. No discounts were permitted for new Members. A Consent Agreement dated May 10, 2006 continued these restrictions as did a Consent Agreement dated March 10, 2008.¹⁴¹

In an email dated July 30, 2004 to the WCB relating to the pending 2004 Consent Agreement, Sorenson notes, in part, the following: “What is available is the elective 5% or 10% discount for accounts that are profitable, long term participants and at threat of being lost to the Trust due to competition. As you can see, this discount is sparsely given and the total amount of aggregate discount for the Trust is \$127,000-less than 2% of the total contributions.”

We consulted with the Trust’s WCB-appointed program administrator regarding Member discounts. Available information suggests that PRM discounted the New York State Compensation Insurance Rating Board (NYSCIRB)¹⁴² rates when there were full rates and added a multiplier to the loss cost rates once this was implemented in 2007. It appears that they

¹⁴¹ A WCB Level I Report as of November 30, 2008 stated: Trust Members do not have a common renewal date. If applicable, membership discounts are not universal for all Members. Discounts are based on loss history, length of time with the Trust and competitive necessity. Discounts are only applicable to renewing Members and the discount ranges from 5 to 10%.

¹⁴² The New York Compensation Insurance Rating Board (NYCIRB) is a non-profit, unincorporated association of insurance carriers, including the State Insurance Fund. In conjunction with the New York Workers’ Compensation Law, the Insurance Law provides for the Superintendent of Insurance to designate a rate service organization to collect the loss, premium, and payroll data from each carrier, summarize this information, and develop an adequate rate structure.

charged the same rates for all Members regardless of experience. We found nothing in writing verifying what discounts and multipliers were used.

Concerning Member discounts, MPA reported to BST that Arney “permitted discounts of up to 40% on a flexible basis as determined by PRM, based on size of the Member payrolls and better past loss experience.” The discounts were later limited to the percentage of State assessment charges and gradually decreased and limited in the last years.

As noted elsewhere in this report, a number of Members remained in the Trust despite having emods in excess of the 1.35 underwriting threshold, oftentimes for multiple consecutive years. We were unable to determine what, if any, discounts these Members received due to the unavailability of detailed Member discount information.

In addition to the standard discount, and as discussed previously, the Trust implemented a “Retention Plan” to attract certain larger and better performing agencies into the Trust. Essentially, the Retention Plan offered select Members the ability to earn cash credit if actual losses were less than estimated losses. Records indicate that a total of eight (8) Members participated in this program.¹⁴³ PRM also operated a Trustee-approved Retention Plan at HCPSIT in which forty eight (48) Members participated.¹⁴⁴

As previously noted, Chair Johnson told BST that she was not made aware of the Trust’s Retention Plan until the end of the Trust and only when she was told “inadvertently” by Campanelli that ICL had received its annual retention reimbursement check.

Gosdeck acknowledged that the Trust had a Retention Plan early on, but the Trustees wanted it discontinued. He noted that existing retention participants could remain in the program, but no new Members could be enrolled. Records show no Members becoming a Plan participant after January 2004, and this is confirmed in an email from PRM to the WCB dated July 30, 2004.

BST had access to only a limited number of documents explaining the details and criteria for CRISP’s Retention Plan and found no evidence of any formal Trustee approval. Trustee minutes make few references to the Retention Plan with these references largely relating to the treatment

¹⁴³ Retention Plan Members included: Royal Care, Inc. (1/1/04-1/1/07); Jawomio, Inc. (1/10/03-1/10/10); Four Winds, Inc. (9/1/00-9/1/09); Project Hospitality, Inc. (9/1/03-9/1/09); PSCH, Inc. (11/9/02-11/9/09); Institute for Community Living (12/15/03-12/15/09); Herbert G. Birch Services, Inc. (7/1/02-7/1/03); and The Lake Grove School (10/5/00-10/5/03). Royal Care was terminated from the Trust for exceeding excess capacity underwriting guidelines.

¹⁴⁴ Notes to HCPSIT’s 2005 financial statements defined the Trust’s Retention Plan as follows: A loss sensitive plan that provides the insured (participant) with an opportunity to realize significant cost savings if losses are kept to a minimum. At inception of coverage, an estimate of losses is used to establish a deposit contribution. After the policy period has expired, a comparison of actual losses is made. If actual losses were less than estimated losses, a return contribution would result. If actual losses were greater than estimated losses, an additional contribution would result.

of the Retention Plan on the audited financial statements. However, minutes for May 29, 2003¹⁴⁵ reflect the Trustees unanimously authorizing “the continuing option to utilize retention plans in appropriate cases that meet trustee standards and directed counsel to review the existing contract to ensure that the retention plan contract adequately protects the Trust.”¹⁴⁶ As such, and contrary to Johnson’s statement, it appears both the Trustees and Johnson were aware of the Retention Plan’s existence and formally approved the Plan’s continuation. BST was unable to determine the criteria, if any, used to identify Retention Plan participants.

Previously, BST spoke to Arney concerning the genesis of the Retention Plan at HCPSIT. Arney indicated that HCPSIT was losing members to workers’ compensation carriers who had “cash flow” plans.¹⁴⁷ Arney said he tried to duplicate the Kemper insurance “cash flow” plan model at HCPSIT. In the long run, he felt the Retention Plan was not helpful to HCPSIT as the individual Members, and not the Trust, had the “float.”

Compared to HCPSIT, CRISP’s Retention Plan was relatively modest with only a maximum of eight (8) participating Members each with substantial annual payrolls. Participants signed a Workers’ Compensation Incurred Loss Retention Plan Endorsement for each year of participation. Records indicate that each Plan participant had good loss histories, except for Lake Grove School, which had emods of over 1.9 for two of its three years as a Plan participant.¹⁴⁸

At a Trustee meeting on July 12, 2010, PRM updated the Trustees on the operation of Retention Plans. PRM noted the Trust had five Plan Members, four of which were still active CRISP Members.¹⁴⁹ PRM explained the 30% of contribution plus the loss forecast is what was paid. Annual audits were performed and reconciled and six months after coverage period, a retention adjustment was calculated looking at actual losses plus claims fees. If losses were more than estimated the Member would be billed; if less than estimated, a refund was sent to the Member. This process was done annually until all claims were paid. Half of the savings were returned and all losses billed. Johnson commented on the implications of the Retention Plan in run-off citing ICL that “now faces a huge loss” that may result in “Trust payment of losses for medical bills and benefits that will be recovered in subsequent retention adjustments.” Sorenson said a policy to address retention losses must be in place when the Trust entered run-off.

¹⁴⁵ The meeting served as a joint Annual Meeting of the members and a regular Trustee meeting. Chair Johnson was in attendance.

¹⁴⁶ BST did not identify any subsequent reporting by the Counsel.

¹⁴⁷ IRMI defines a cash flow program as: Any insurance rating scheme that allows the insured to hold and benefit from loss reserves until paid as claims, e.g., deferred premium plans, self-insurance, and paid loss retros.

¹⁴⁸ During its tenure in the Trust from December 1, 2001-October 5, 2010, this Member had an average annual emod of 1.72.

¹⁴⁹ It is unclear why PRM identified the Trust as having five (5) Plan members rather than eight (8).

In summary, the documents reviewed and the interview results show that:

- Premium discounts were granted by PRM to select Members without Trustee input or standard discount criteria approved by the Trustees;
- In the absence of standard criteria, the awarding of discounts was subject to manipulation for the benefit of select Members;
- The Trust's limited-participation Retention Program helped attract certain larger payroll employers into the Trust. However, the Retention Program was not made available to all equally-situated Members as there appears to have been standard written criteria to determine which Members could participate.

I. Payroll Audits

Standard industry practices require audits of the Trust Members' payroll to reconcile the Members' premiums that were previously based on an estimate of the Members' payroll. The performance of these audits is imperative because of the direct correlation between the Member premiums billed and the payroll reported. As such, there exists a financial incentive for the Members to misclassify payroll for the riskier job positions in order to reduce their annual premiums.

Pursuant to Article VI, Section 5 of the Trust Agreement, the Trustees had the responsibility to ensure periodic payroll audits were performed for each of the Members. Our analysis of the Member files and other documents revealed that payroll audits were regularly performed by a third-party payroll auditor¹⁵⁰ and that the corresponding adjustments were made to the Members' annual premium, as necessary.¹⁵¹ BST also noted that a number of the payroll audits were missing.

J. Safety Programs

The implementation of a robust safety program is generally recognized as an insurance industry best practice and an effective method in which group self-insured trusts, and any insured organization, can potentially reduce their exposure to losses due to employee accident or injury.

Program administrators typically have primary responsibility for delivering loss control and safety programs to a trust's membership. Consistent with this, loss control services were embodied in PRM's Program Administration Agreement. Section 2(c) of the Agreement assigns PRM the responsibility to "design and develop safety programs and training for members and, present such programs to the members at regularly scheduled meetings, conventions and

¹⁵⁰ The payroll auditor was Charles E. Hock Associates, Inc.

¹⁵¹ This was confirmed by Member interviews.

seminars and at such other times and places as the Trustees and the Program Administrator may agree...”

Section 3(a) of the Agreement provides that PRM would receive 6.25 % of gross written contributions to perform all services under the Agreement, including providing safety programs. However, PRM received separate fees from the Trust for Loss Control Services. For the term of the Trust, these additional fees totaled over \$732,000. We were not made aware of any separate loss control agreements governing these fees, if they existed.¹⁵²

The Trustees were aware and approved the separate loss control fee arrangement with PRM. Minutes for September 19, 1996 reference a loss control proposal from PRM that included a \$2,500 monthly fee for site visits where standards were to be “measured.” Two Trustees indicated they understood that loss control was part of PRM’s administrative fee. Minutes report Case responded that MPA was receiving half this administrative fee for marketing services, and the Trustees unanimously accepted PRM’s proposal without any further discussion noted.

Minutes for October 25, 2000 show Arney requesting an increase to the loss control fee to \$5,000 per month due to the Trust’s growth and the addition of a second loss control specialist. Arney asserted that the increase would cover “approximately 90% of the cost of providing the service to CRISP.” The Trustees unanimously approved this request. The fee remained at \$5,000 per month through the end of the Trust.

Evidence indicates that the Trustees recognized the importance of loss control and safety to mitigate claims losses. The Trustees interviewed were generally satisfied with PRM’s loss control services and confirmed PRM’s distribution of safety literature, conduct of seminars, conduct of field visits, and issuance of written reports. Trustee Hardiman noted her organization remained with CRISP largely on the strength of PRM’s safety program and field presence. The Members interviewed offered no adverse comments relative to PRM’s safety program though they had varying recollections of site visit frequency.

PRM made formal loss control presentations periodically at Trustee meetings and safety issues were regularly discussed. For example, minutes for April 29, 2002 report that a discussion of the need for annual site visits, training, and addressing loss sources. The Trustees asked that a Safety Committee established in October undertake its activities; focus on high loss participants; regular agency contacts being made with all participants on a prioritized basis; a newsletter feature

¹⁵² PRM received separate loss control fees from HCPSIT and executed separate written agreements with HCPSIT for these services. Services under these agreement included: collecting and analyzing loss control and claims data; reporting annually to each participant compensable losses; preparing reports to the Trust regarding participants’ loss history and efficacy of participants’ loss control programs; consulting with and conduct annual site visits annually with each participant; preparing written site visit reports; conducting training and in-service programs to participants; developing jointly with the Trust and revise educational and training materials; and advising and consulting with the Trust on loss control issues.

discussing best practices from a safety perspective be implemented; and PRM put a timeline in place to effectuate these goals.¹⁵³

Subsequent minutes suggest that a Safety Committee¹⁵⁴ was formed and more attention was being given to Members with higher loss histories. At the Trustee meeting of May 18, 2006, PRM reported that its new loss control manager had “seen approximately 93% of participants—many several times.”¹⁵⁵

Case and Hoffman stated that PRM's level and quality of loss control services was “great most of the time, when a person named Augie was put in charge by PRM,” but “may have broken down for a period of time when a different individual by the name of Charles was put in charge by PRM.”¹⁵⁶

We did not have access to PRM's safety schedules, reports, and personnel, limiting our ability to fully assess the scope and quality of PRM loss control services. Accordingly, we were not able to verify the number of site visits performed and/or the findings, and therefore, we were unable to determine whether the fee paid to PRM was appropriate. However, available evidence suggests that the Trustees understood the importance of promoting a viable risk management program and supported PRM's efforts to implement a substantive safety and loss control process to mitigate Member losses.

K. Renewal Process

Prudent business practices dictate that a trust member's loss runs and loss history be reviewed and evaluated prior to accepting and/or renewing the member. In addition, a thorough and complete analysis of the trust's cumulative member deficit, if any, should be considered before member discounts are offered to the member.

The Trust Agreement does not specifically address the renewal process; however, Article VI Section 6(i) of the Trust Agreement authorizes the Trustees to “adopt and promulgate rules and regulations for the proper administration of the Fund, the admission of members to the Fund, the suspension of members, and the expulsion of members.”

¹⁵³ Arney prepared a comprehensive Safety and Health Manual for HCPSIT. BST is unaware if a similar manual was produced for CRISP.

¹⁵⁴ BST was not provided with any Safety Committee minutes.

¹⁵⁵ The “new” manager was the former PRM safety manager who returned from a term of absence.

¹⁵⁶ Case and Hoffman added the following relating to their assessment of PRM's loss control services: “MPA notes, however, that the services in question were the presumed expertise of PRM, not MPA. MPA did not ever claim to have the expertise or totality of information necessary to determine whether PRM performed all of its duties to the level and degree of care needed.”

Article III, Section 7 of the Trust's By-Laws gives the Trustees the authority to terminate Members from the Trust as follows:

Membership shall be continued for those members who continue to be engaged in the provision of community living programs except that the trustees may exclude or suspend any member from continued membership for failure to comply with these By-laws, failure to comply with applicable laws relating to Workers' Compensation, or failure to pay contribution due. Notice of termination shall be in writing and be given at least ten (10) days prior to the date of termination and shall be effective ten (10) days after the filing of due notice with the Chairman of the Workers' Compensation Board or the Self-Insurance Division of that Board and shall not alter, impair or annul any obligation for the payment of all contributions which were due during the time such entity was a member of the Trust.

Evidence indicates that the Trustees delegated this authority to PRM and MPA with limited involvement by the Trustees. Meeting minutes reflect that renewals were typically discussed by Case and Hoffman as part of their Marketing Report. Members renewed, departed, or approaching renewal were identified and discussed by MPA along with any exigent circumstances. The presentation was informational and served as the basis for discussion with the Trustees, but no formal vote on renewals was taken. It is not surprising that MPA and PRM took the lead in this process as their commissions were dependent on the Trust's ability to maintain paying Members -which may explain why Members were not discouraged from leaving the Trust during the five year period when the Trust's Member deficit exceeded \$3 million.

BST did not have access to all Member renewal records and, therefore, cannot offer an opinion on the substance or quality of the renewal process or the underwriting criteria governing renewals. BST did have the opportunity to review PRM's renewal activities relating to HCPSIT and found that PRM developed and implemented a structured Member renewal process.¹⁵⁷

Trustee minutes for February 22, 2001 do provide a glimpse into the renewal process. PRM noted that it would review of all participants with a loss ratio of 50% at least 90 days prior to the

¹⁵⁷ The renewal process was detailed in the *PRM Quality Systems and Procedures Manual - Tab Six Procedures for Renewal Processing, Experience Modification Calculations and Audits* (as of 2/25/05) and summarized in the *Trustee Manual*. PRM used a Renewal Checklist to track collection and review of financial and loss information for each Member renewal. Records show that Members had to supply their latest financial statements, details of significant operational changes, and estimated payrolls for the following year. PRM would review this information in conjunction with loss experience information and applicable rates and then calculate a renewal contribution. A Renewal Review form was then prepared summarizing such information as loss history, payroll history, contributions, worker classification, assessments/charges, discounts, and renewal contribution along with a renewal approval/ disapproval recommendation.

renewal date. Participants with a loss ratio of greater than 50% would be considered for non-renewal and the participant would be reviewed in the context of a plan to bring the participant back to the standards as well as authorize renewal. This could include pricing decisions to encourage the participant to seek alternate coverage. PRM would also consider reasons for consideration despite an inadequate loss ratio, such as a major claim affecting a participant with an otherwise adequate claims history, changes in management or facility, re-pricing, or other changes that could be reasonably anticipated as having a positive outcome. The Trustees approved this process.

MPA advised BST that it had no role in the Member renewal process “other than the responsibility for solicitation of the Members to re-up.” MPA indicated that PRM would determine the Member’s budgeted payroll for the upcoming year, and based on job classifications plus recent loss history PRM would create renewal cost quotes, taking into account market rates, and each Member’s total number of employees, employee classifications, and loss experience. MPA would then present PRM’s renewal cost quotes to the Member, attempt to get the Member to renew, and serve as a Member advocate relating to questions relating to the quote. MPA was given the opportunity to review and comment on all renewal quotes that were generally presented in writing to Members. MPA added that larger accounts or those produced by other brokers were handled on an individual basis and the approach varied but in all instances, MPA was always available for discussion with the Member, and to encourage their continued participation in the Trust.

BST selected a judgmental sample of 48 Members leaving the Trust prior to Trust’s dissolution on December 31, 2010. We reviewed the *Notice of Termination of Employer’s Participation in Group Self-insurance Plan Form GSI-3.1* for each of these Members and found the following with respect to the reason for membership termination as stated on the form:

Table 2: Member Terminations

<u>Reason for Termination</u>	<u>Number</u>	<u>%</u>
Obtained Coverage Elsewhere	23	48
Business Reason	16	33
Underwriting Reasons	6	13
Non-payment of Premium	3	6
Total	48	100

Source: WCB Form GSI-3.1

Based on this sample, it appears that while some Members were terminated for various underwriting reasons, most early Trust terminations related to Members voluntarily seeking coverage elsewhere. Also, it is unclear to what extent PRM and MPA evaluated a Member’s contribution and claims and analyzed the cost-benefit of the Member’s continued participation in the Trust. The continued and gradually increasing Member deficits from inception suggest that this may not have been done, as Members rarely were terminated for underwriting reasons.

As referenced in the Underwriting Section, 114 Members retained the same experience modification rates in excess of 3 consecutive years. Our analysis of Member data further showed that 50 Members were retained despite having emods in excess of 1.35 for one or more years. Table 3 summarizes these findings:

Table 3: Members with Emods > 1.35 By Total Years

<u>Total Years > 1.35</u>	<u>Number of Members</u>
1	17
2	13
3	8
4	3
5	5
6	0
7	3
8	0
9	<u>1</u>
Total	50

Source: CRISP Member Files

In addition, our analysis as reflected in Table 4 determined that 33 Members maintained emods greater than 1.35 for two or more successive years, with 7 Members retaining emods greater than 1.35 for more than five years.

Table 4: Members with Emods > 1.35 for Successive Years

<u>Successive Years > 1.35</u>	<u>Number of Members</u>
2	17
3	7
4	1
5	5
6	2
7	0
8	0
9	<u>1</u>
Total	33

Source: CRISP Member Files

We also found that a number of Members maintained emods well in excess of 1.35 over extended periods, but remained in the Trust. Examples are as follows:

- One Member had an average experience modification rate of 1.86 over an eight-year period. Over a three-year period, this Member's experience modification rate averaged 2.40. The Member's net negative contribution was in excess of \$990,000.
- One Member had an average experience modification rate of 1.72 over a nine-year period. The Member's total net negative contribution was nearly \$1.3 million.
- One Member had an average experience modification rate of 1.60 over a six-year period. The Member's net negative contribution was in excess of \$800,000.

In summary, the documents reviewed and the interviews conducted show that:

- The Trustees failed to fulfill their fiduciary duties by providing insufficient oversight of the PRM's renewal practices whereby Members with experience modification rates exceeding the Trust's underwriting guideline of 1.35 were permitted to remain in the Trust, subjecting the Trust to unnecessary loss exposure.

L. Member Deficit

Each of the CRISP Members is jointly and severally liable for the expenses and obligations of the Trust during the period the Member was in the Trust. Members' obligations are expressly noted in the Indemnity Agreements and the Trust Agreement.

Audited financial statements reveal that the Trust had a Members' deficiency (excess of liabilities over assets) for each year from 1996 through 2010, except for 2007 when the Trust realized a Members' surplus of \$119,304. The deficiencies ranged from (\$232,047) in 1997 to (\$11,113,227) in 2010.¹⁵⁸ From 2001 through 2010, the Trust experienced a regulatory Members' deficiency each year, ranging from a low of (\$1,391,295) in 2007 to (\$24,256,049) in 2010. During this entire period, the Trust did not achieve a 90% regulatory equity ratio.

Section 317.9 (b) (7) of the NYCRR (effective January 31, 2001) stipulates that a group self-insurer may be required to levy an assessment upon a group or its members (if the group is under-funded) to make up the deficiency, i.e., if the assets of the Trust are actuarially determined to be insufficient to enable the Trust to discharge its legal liabilities.

On November 30, 2001, the Trust billed its Members a surcharge of approximately \$1,503,000.¹⁵⁹ The amount of the surcharge was based on the amount of the deficit, each participant's loss history, and the length of time each participant was a Member of the Trust. Records indicate that most Members promptly paid their assessments with a few Members

¹⁵⁸ 2010 included 13-month period December 1, 2009-December 31, 2010.

¹⁵⁹ The Trust offered its Members the option of financing the amount due and agreed to incur the related finance charge. For the year ended November 30, 2002, total finance charges incurred were \$10,470.

declining to pay. On March 19, 2003, the Trust initiated legal action in Albany County Supreme Court against six former Members¹⁶⁰ to recover a surcharge receivable of \$533,079. The Trust and five of the Members entered into a Stipulation of Discontinuance in Albany County Supreme Court that ended the pending litigation and opened the door for the negotiation of individual settlement agreements between the Trust and those Members.¹⁶¹ The Trust's audited financial statements indicate these settlements totaled \$241,100. The sixth Member¹⁶² involved in the initial litigation filed for bankruptcy, and the remaining funds due from this Member were deemed uncollectible.

BST obtained a copy of an executed settlement agreement between the Trust and Hebrew Academy for Special Children, Inc., a Trust Member from April 1996 through May 2000. The agreement, signed by a Member representative and Chair Johnson, provided for the Member's payment of \$130,000 to settle all outstanding assessment funds due and the general release of the Member from any future liabilities relating to the initial litigation. In a letter dated December 16, 2011 to the State-appointed administrator, the Member disputed an assessment invoice arguing it had been released of such future liability by the settlement agreement. The WCB does view this and the other judicially sanctioned settlements as a valid release from liability for the Member deficit.

Based on the foregoing, the Trustees appear to have taken reasonable and prudent action to enforce its Member assessment.¹⁶³ However, despite these recovery efforts, the Trust continued to experience a deficit condition. A Level I Review by the WCB for the year ended November 30, 2003 found the Trust with a regulatory deficit of (\$7,535,415) and an equity ratio of just 40.02%. As a result, the Trust was required to enter into a Consent Agreement with the WCB effective August 2, 2004 that, inter alia, eliminated discounts for new Members, limited discounts to only ten renewing Members of up to 10%, and prohibited the addition of new Members for 12 months. It is uncertain what, if any, actions the Trustees would have taken had they not been required to enter into the Consent Agreement.

The WCB found the Trust to have a regulatory deficit and to be under-funded for the years 2004-2005. Based on its review of the Trust's audited financial statements for the fiscal year ended November 30, 2006 and independent actuarial and financial reviews performed on behalf of the WCB, the Trust was again deemed under-funded in a letter to PRM dated August 20, 2007. In a Level I Report dated May 19, 2008, the WCB found the Trust to have no funding issues with a 90% equity ratio for the fiscal year ended November 30, 2007.¹⁶⁴ In recognition of the Trust's

¹⁶⁰ These six former Members included: A Program Planned for Life Enrichment Housing Corporation (\$43,924); Hebrew Academy for Special Children, Inc. (\$144,456); Mini Travelers, Inc. (\$33,139); Project Real, Inc. (\$3,410); Transitional Services of New York for Long Island, Inc. (\$57,254); and Upstate Home for Children, Inc. (\$250,896).

¹⁶¹ On April 14, 2004, the Trust entered into a Stipulation of Discontinuance with Hebrew Academy for Special Children, Inc., Mini Travelers, Inc., and Project Real, Inc. On April 19, 2005, Stipulations were executed with Transitional Services of New York for Long Island, Inc., and Upstate Home for Children, Inc.

¹⁶² A Program Planned for Life Enrichment Housing Corporation.

¹⁶³ In her interview with BST, Chair Johnson attributed the deficit situation at that time to discounts given by PRM and MPA and overall lack of sufficient premium collected.

¹⁶⁴ The Trust showed a GAAP surplus of \$119,304 and a regulatory deficit of (\$1,391,295).

improved deficit condition, the Trust and the WCB entered into a Memorandum of Understanding (“MOU”) effective June 13, 2008. The MOU essentially acknowledged the Trust’s improved financial condition and removed the “conditions and restrictions” imposed by a March 10, 2008 Consent Agreement and Consent Order.¹⁶⁵ This agreement states, in part, that a supplemental assessment bill would be sent to Members not later than April 30, 2009 for any deficits occurring in the 2007/2008 Contribution Year.

WCB’s Level I Report for the year ended November 30, 2008, dated June 5, 2009 found the Trust’s Member regulatory deficit to have increased to (\$3,583,470) from (\$1,391,295) in 2007. Trust equity dropped to 75.15% in 2008 from 89.10% in 2007.

On July 23, 2009, the WCB met with PRM and the Trustees to discuss the continuing deficit problem and remedial steps necessary to maintain the Trust’s solvency. The WCB presented factors for the Trustees to consider in evaluating the Trust’s operation such as review of expenses, compliance with underwriting guidelines, booking of reserves on the balance sheet vs. actuary’s best estimate, identifying high risk Members, and pursuit of Section 32 Settlements. Remediation steps included setting Consent Agreement terms to include 2010 contribution rates based on results of a Break-Even report presented to the Trustees; monitoring the 2009 contribution year, sending out assessments, and collecting any shortfall by December 31, 2010, if necessary; changing the Trust’s fiscal year end to a calendar year end; and submitting a plan to WCB outlining steps to achieve a fully funded status by 2014. Minutes for September 28, 2009 show that the Trustees voted unanimously to “support a surcharge of the deficit over a period of years if mandated by the WCB with PRM to provide options to the trustees.”

Effective February 25, 2010, the Trust entered into a Consent Agreement that included a deficit reduction plan, providing estimates for contributions and expenses for the 2009-10 fiscal year. This plan also provided for the Trust to achieve break-even for the 2009-10 year, as well as a profit from which \$650,000 will be used to reduce the existing regulatory deficit. Failure to achieve the surplus indicated for Contribution Year 2010 would be cause for the WCB to close the Trust.

In a Level I Report dated April 27, 2010 for the year ended November 30, 2009, the WCB deemed the Trust underfunded with a regulatory deficit of (\$7,900,378) and a Trust equity ratio of 57.88%. In response to the Level I Report, the Trust developed “a plan of revenue enhancement and deficit reduction” that was presented to the WCB in a letter from Sorenson to the WCB, dated August 5, 2010”. The key components of the plan included the immediate upward adjustment of all class rates by 5% applied to all renewals on a monthly basis, an increase in the NYS Assessment charge levied to CRISP Members to the full 14.2% NYCIRB published in October 2009, and an increase in the assessment charge to 18.1% effective October

¹⁶⁵ Prior to the official finding of “no funding issues” the WCB entered into a Consent Agreement with the Trust on March 10, 2008. The Agreement, inter alia, opened the Trust to a maximum of 30 new Members, committed the Trust to take action to achieve breakeven status for Contribution year 2008, including issuing a supplemental bill to its Members if necessary, and required the Trust’s submission of uncertified financial reports to the WCB on a quarterly basis.

1, 2010. PRM estimated that the “total revenue adjustment upward for the rate and assessment changes is +\$1,965,992.” (sic)

Sorenson further indicated that the Trustees “are very aware that a member assessment is necessary and justified to reduce the ultimate deficit to zero” and that a plan was being developed. Sorenson stated that the Trustees intended to “find an alternative insurance program” for the Members prior to the Trust’s fiscal year end on November 30, 2010 if possible, but were “reluctant to issue an assessment to all current and former members so close to a planned Trust closure and run-off, at which time the ultimate values would be calculated and assessed.” Sorenson said the Trustees believed Members would stay in the Trust even at higher rates until alternative coverage could be found and that an assessment might cause Members to leave, early causing an even larger short-term funding problem.

As noted previously, in 2010 it became apparent that claims may have been substantially under reserved by PRM’s affiliate, CSI, and that the inadequacy of the reserves was not fully disclosed to the Trustees or Members by either PRM or CSI.

On October 31, 2010, the Trustees held a meeting via conference call during which the Trustees voted unanimously for CRISP to cease providing Workers’ Compensation coverage effective December 31, 2010, and to enter run-off. The Trustees directed Sorenson to notify all Members accordingly on November 1, 2010, and to continue work on alternative programs.¹⁶⁶

At a Trustee meeting on January 10, 2011, PRM reported that all Members had obtained alternative coverage as of the Trust’s termination date. PRM retained \$1.3 million in business, MPA retained about 75% of its book of business, and other Members used existing broker relationships. A PRM assessment proposal showed that about \$15 million was needed to fully run-off Trust expenses. Minutes indicate that Chair Johnson recommended doing 50% of the total assessment immediately. The Trustees unanimously approved an assessment of \$7.5 million and an interest charge of ½ of 1 % per month interest for installments subject to WCB approval.

The January 10 minutes further report the following:

Sorenson indicated that he would prepare drafts of the agreements and the note for the installment agreement and look at the end of the week for that project. The assessment should be out by the end of the month and as soon as possible we should make a proposal to the WCB. Once they approve, it can be billed to the participants. A target of January 25 to the WCB is realistic.

On March 10, 2011, after discussing the need to increase the level of the assessment to cover 12 months of claims, the Trustees unanimously approved a Member assessment in the amount of \$15 million, and on May 13, 2011, PRM reported to the Trustees that approximately \$300,000 in

¹⁶⁶ Records show that a letter, dated November 1, 2010 was sent by the Trust and PRM to the Members.

assessments had been collected in the first thirty days. PRM indicated that many Members were “making down payment commitments this month while others have committed to pay in full or are making plans to do so.”

On June 9 and June 10, 2011, Chair Johnson and Trust Counsel Gosdeck held Member meetings in Albany and New York City, respectively. In a memorandum to Members dated June 17, 2011, Johnson summarized the issues raised at the meetings and subsequent events. Johnson indicated she was assembling a master email Member list, having the independent auditors issue an official attest opinion on Members’ assessment calculations, retaining a consultant to handle communications between the Trust and Members regarding the assessments¹⁶⁷, and obtaining commitments from Members to pay assessment to forestall a Trust take-over by the WCB. She asked members to advise her as to what amount they could pay towards their assessment by the end of July.¹⁶⁸

On June 23, 2011, a teleconference was held between CRISP and WCB representatives. PRM was not represented. Minutes report that Chair Johnson summarized PRM’s role with the Trust since its inception and Sorenson’s role as PRM’s lead person since approximately 2000. She noted that some Members had reported that they did not receive from PRM assessment billings from or even communications relating to the Member meetings. Johnson opined that Sorenson’s personal situation “may be causing him to be more muddled than first thought” and that consultant back-up was being pursued. Johnson informed the WCB that she had “\$2.234 million in good, solid commitments if the trust continues in the control of the trustees.”

WCB legal counsel advised the Trustees “that with only \$600,000 of unpledged cash and investments left they cannot let the trust continue to be run by the trustees.” WCB legal counsel further noted that “\$3.1 million in investments was collateral for the \$2.3 million letter of credit, making the situation even worse from their (WCB’s) stand point.” Johnson and the Trustees requested “more time to collect more assessments, as well as the outstanding pledged amounts, but the WCB stated they did not want to take that risk.” The WCB advised that it would begin the transfer process “today.” Johnson asked that before moving forward, CRISP counsel have the opportunity to speak with WCB legal counsel who provided his direct contact number. It is evident that the WCB’s position and basis thereof was clear by the conclusion of the meeting.¹⁶⁹ It is further clear that neither the Trustees nor PRM accepted responsibility for the Trust’s extremely poor fiscal condition - despite receiving millions of dollars in fees (PRM) and over

¹⁶⁷ The Trust entered into a Management Consulting Agreement with Cody Management Services, Inc. effective June 16, 2011, for communications services relating to the pending member assessment. Under the terms, Cody received an initial retainer of \$25,000, of which \$15,000 was non-refundable and an hourly fee of \$175 to be applied against the retainer. Minutes show that the Trustees approved this agreement on June 20, 2011.

¹⁶⁸ Johnson advised BST that she has approximately \$3,500 in expenses on her AMEX card charges relating to Member meetings for which she has not been reimbursed. She also noted that she promised Gosdeck that she would pay him \$1,500 per day to help coordinate the Member meetings for which he has not yet been reimbursed. In all, Johnson stated that there is approximately \$60,000 in outstanding unreimbursed expenses relating to the Trust’s closure, including money owed to Dave Johnson, Marvin & Co., and the law firm of Couch White for Trust related work.

¹⁶⁹ The official minutes of the teleconference were prepared by Trustee Hardiman.

\$100,000 in Trustee stipends (Trustees). Had the parties responsible for administering and overseeing the Trust been more diligent in renewing Members and reserving claims, the Trust may not have been in such a poor fiscal position as of June 2011, and the Members may not have had to pay such a large assessment.

Consistent with its position presented to the Trustees on June 23, 2011, the WCB sent a letter, dated June 28, 2011, to the Trustees and PRM indicating that it has determined that CRISP “has demonstrated an inability to properly administer its liabilities” and that pursuant to 12 NYCRR Section 317.20(c), the WCB would assume the administration and final distribution of the group’s assets and liabilities, effective August 1, 2011. In addition, the WCB advised that administration of the run-off would be transferred to its third-party administrator, NCA Comp., Inc.¹⁷⁰

In apparent reaction to or anticipation of the WCB’s letter, Chair Johnson sent a letter, dated June 28, 2011, to Governor Andrew Cuomo questioning “the integrity of the leadership of the New York State Workers’ Compensation Board with respect to its oversight of the Group Self-Insurance Trusts (GSITs).” She highlighted the difficulties relating to managing CRISP and opined that the WCB never offered “any guidance or assistance.” Johnson spoke of her participation on the Governor’s Task Force and the inability to place Members with a State Insurance Fund Safety Group despite her efforts and the WCB’s purported support. Johnson detailed to the Governor Sorenson’s personal issues, his recuperation out-of-state, and his purported failure to follow-up on assignments and to maintain adequate communications with Members. Johnson referenced her request to the WCB to delay its takeover of the Trust for another month to address assessment questions and receive \$2.4 million in assessment levies committed by Members at the meeting on June 9 and 10. She noted that the Trust shortly will have collected \$2.5 million available to the Trust plus \$2.45 million in Letter of Credit collateral. Johnson argued that despite these efforts, the WCB was immediately taking over the Trust which she felt was not in the best interest of CRISP’s human service agency Members.

Chair Johnson’s letter to the Governor appears to be very self-serving, while at the same time deflecting potential blame from her, the Trustees, and PRM - the parties responsible for running and overseeing the day-to-day affairs of the Trust. For example:

- BST noted that Johnson did not provide or offer any explanation in her letter to Governor Cuomo as to why, despite being paid, that neither she, nor the other Trustees, did not terminate the relationship with PRM/Sorenson earlier if they (PRM) failed to “follow-up on assignments and maintain adequate communications with Members.”
- Johnson blames the WCB for not offering “any guidance or assistance” in managing the Trust, but she somehow fails to point out that she, the other Trustees, and PRM formed

¹⁷⁰ Johnson letter to Governor Cuomo indicates that she was advised by phone of the WCB takeover on or about Thursday, June 23, 2011.

the Trust and had the fiduciary responsibility to manage the Trust - not the WCB.¹⁷¹ She further failed to note that the WCB was communicating with her and the Trustees on a weekly basis during the latter years of the Trust's existence.

Johnson also mentions her role on the Governor's Task Force, yet she coincidentally fails to mention how BST advised her and the other Task Force members on January 8, 2010 of our findings relating to the failure of other group self-insured trusts. Interestingly, BST's findings with regard to these other trusts were not dissimilar to the reasons why the CRISP Trust failed, and were reported to Chair Johnson approximately 18 months before the CRISP Trust was taken over by the WCB.

BST noted that none of Johnson's comments to Governor Cuomo were mentioned in the November 2010 closure letter to the Trustees/Members. Accordingly, it would appear that she and the other Trustees may not have advised the Members about their concerns relating to PRM.

At the Trustees' final documented meeting on July 5, 2011, the Trustees discussed the Trust's financial status and its efforts to achieve the hard cap of \$2 million. The Trustees also discussed "strategies to continue to battle for the right to continue." The Chair indicated she and other interested Trustees would be having a phone conversation with the Governor's Office on July 6, 2011.¹⁷² The Trustees discussed "grass roots efforts to be undertaken by the members of the Trust through their respective associations."

BST spoke to Johnson about the events leading to Trust's closure. Johnson indicated that she wanted to keep the Trust solvent but that it became apparent that another assessment was necessary.¹⁷³ She was unsure of the extent of the deficit but felt there was enough premium and investments to cover \$10-\$13 million. She tried to process an assessment in February 2011. Sorenson advised her that \$5 million was needed, but she felt it was closer to \$15 million. She said Sorenson was "hyperventilating" when she told him this. The amount later rose to \$18-\$20 million. She said PRM then began to close claims more quickly. The WCB was told they would have \$5 million by June 30 but by May, Johnson felt there was no progress and arranged the Member assessment meetings in Albany and New York City.

At the meetings Johnson said she found out Members had no idea of their assessments from PRM, and the information they received was incomplete.¹⁷⁴ She also discovered there was no complete Member list and she had to compile her own list from various sources. Johnson indicated that Sorenson prepared an assessment allocation which she had reviewed by Marvin & Co. which found problems with the assessments. She said she collected \$1.2 million in two days

¹⁷¹ This is an interesting comment by Johnson, as it not only attacks the integrity of the WCB and other parties not involved in the administration of the Trust, but it also improperly implies (to the Trust Members) that it was the WCB's responsibility to manage the Trust.

¹⁷² BST is unaware whether this meeting occurred.

¹⁷³ The Members' deficit was approximately \$11 million by December 2010, so a large Member assessment was obviously inevitable.

¹⁷⁴ It is not presently known whether the Members were annually advised of the deficit by the Trustees, PRM-CSI, or MPA.

but needed \$2 million, so the WCB closed down the Trust. Johnson opined that the jump in the reported deficit by \$5 million in 2010 due to CSI's under-reserving presented a problem that ultimately could not be overcome.¹⁷⁵

Johnson said she was not aware of any conflicts or improprieties relating to the Trust's operations other than the issues raised in the lawsuit. As detailed in the following section, Johnson and the other Trustees apparently violated Article VI, Powers and Duties of the Trustees, Section 6a of the Trust Agreement stating the fiscal agent and/or administrator appointed by the Trustees "shall not be an owner, officer or employee of a third party administrator." The Trustees previously approved the appointment of CSI, PRM's affiliate, and therefore, knew of the apparent conflict of interest and apparent violation of the Trust Agreement. Johnson's failure to acknowledge this raises the question as to whether or not she and the other Trustees understood the implications and ignored them, or whether they were unconcerned with the apparent violation of the Trust Agreement. Regardless, neither is acceptable given the fact that she and the other Trustees were compensated by the Trust to carry out their fiduciary responsibilities.

Johnson said the Trustees were very troubled by the serious claims of under-reserving by PRM's affiliate, CSI, which came to light in 2010.¹⁷⁶ Johnson recalled that in January 2010, the WCB advised the Trust that there were problems with CSI relating to the HCPSIT Trust. BST also advised Johnson at our meeting with the Task Force that under-reserving was a major problem with most of the other trusts we had reviewed since 2006.

The Trustees asked Towers Watson¹⁷⁷ to perform a claims review.¹⁷⁸ Johnson noted that Towers Watson had performed a review a year earlier and given CSI a "thumbs up." Towers Watson issued its report in June 2010 which reported reserving problems at CSI. Following release of the report, Johnson said she arranged a conference call with Gosdeck, Sorenson, and Gail Farrell, PRM's Senior Vice President/Claims Manager. Johnson said that, to her surprise, Farrell agreed with everything in the critical report and offered no explanations. Gosdeck also confirmed this to BST.

Johnson further indicated that Farrell had added reserves at the end of January 2010 as the WCB was beginning a review of the claims. Farrell told the Trustees she had done this on an annual basis, and the Trustees were comfortable with that explanation. The WCB later told Johnson that such an adjustment was not done annually as suggested by Farrell. Johnson stated that when confronted, Farrell agreed that the annual adjustment was not done as she had represented to the Trustees. On this issue, Gosdeck recalled that NCAComp was asked to perform a sample review of PRM's claims reserves and found evidence of under-reserving. These were adjusted by PRM.

¹⁷⁵ Gosdeck shared Johnson's view that the under-reserving created a deficit that could not be overcome.

¹⁷⁶ This will be discussed in Section M in greater detail.

¹⁷⁷ Towers Watson is an internal risk management consulting firm formed in January 2010 by the merger of Towers Perrin and Watson Wyatt.

¹⁷⁸ Johnson indicated that Sorenson referred Towers Watson to the Trust.

When asked about this adjustment, Gail Farrell advised the Trustees that she makes an adjustment at the end of every year. This was later found not to be the case.

Gosdeck further told BST that he felt Sorenson was slow to acknowledge the growing claims reserve problems. He added that the minutes show PRM had misstated the adequacy of reserves, and the Trustees relied on Farrell's assurances about the reserves' adequacy. Gosdeck stated that he felt the issues that arose with the Trust's claims reserves were influenced by problems with HCPSIT which may have overwhelmed PRM, as HCPSIT constituted the bulk of PRM's business. Concerning PRM's contributing role with respect to the Trust's deficit, he said "at best it was inattention, at worst, it was willful."

Interestingly, Case and Hoffman characterized CSI's level and quality of claims handling services to Members as "excellent" with "very few complaints."¹⁷⁹ Regardless, it appears that under-reserving was an issue and may have been partly due to the fact that there is an inherent financial incentive for PRM to keep reserves low, as higher reserves would warrant premium increases, which may drive away current and prospective Members, and reduced membership would have resulted in lower income for PRM and MPA.¹⁸⁰ Consequently, it remains to be seen whether this was the impetus for under-reserving, although the financial incentive to do so clearly existed. Furthermore, and more importantly, the Trustees were aware or should have been aware of this financial incentive, and as a result, it would seem that they should have taken pro-active measures over the course of the Trust's existence to ensure that under-reserving by PRM-CSI was not an issue. For reasons unknown, and despite getting compensated for attempting to carry out their administrative duties, they failed to have an independent analysis undertaken during the period 2003 through the end of 2009. The Trustees also apparently did not mention this to the Trust Members.

Johnson and Gosdeck noted that the Trustees were very troubled by the serious claims under-reserving by PRM's affiliate, CSI, which came to light in 2010.¹⁸¹ Johnson noted that CSI misled the Trustees about the problem, acknowledged the problem when confronted, and offered no explanation as to the reasons for its occurrence. Gosdeck further told BST that he felt Sorenson was slow to acknowledge the growing claims reserve problems. Both Johnson and Gosdeck indicated that because of the reserving issue and other areas of concern, the Trust retained an Albany-based law firm and initiated litigation against MPA, PRM, and CSI.¹⁸²

BST also spoke to Trustees Lasicki, Hardiman, and Campanelli about their views of PRM's performance. Trustee Lasicki said she "only heard great things" about PRM from her

¹⁷⁹ Case and Hoffman added the following relating to their assessment of CSI: "MPA notes, however, that the services in question were the presumed expertise of PRM, not MPA. MPA did not ever claim to have the expertise or totality of information necessary to determine whether PRM performed all of its duties to the level and degree of care needed."

¹⁸⁰ As previously noted, low premiums were the primary reason why employers joined the Trusts.

¹⁸¹ This will be discussed in Section M in greater detail.

¹⁸² The suit was filed on May 27, 2011. The Complaint against PRM, CSI and MPA was "dismissed without prejudice to any future action" in State Supreme Court, County of Albany on January 9, 2012.

Members¹⁸³ who felt PRM was responsive to their needs. She was satisfied with CSI's claims handling until early 2010 when she was "blown away" by the under-reserving. She said it "all sounded good" from PRM, and the Trustees relied on PRM's expertise. She said she had no indication that Farrell from CSI had done anything "malicious" or that CSI was "incompetent." Lasicki felt the Trustees received a "lot of misinformation from Ed (Sorenson)." For example, she recalled that he could not produce a master list of the Members when asked. PRM also failed to tell the Trustees that Sorenson had surgery and was recovering out of state.

Trustee and Secretary-Treasurer Hardiman stated to BST that both Arney and Sorenson were "professional." She said that Sorenson "cared" and was a "great administrator" until near the end of the Trust when she heard he had some health issues. She said Mark Crawford was also very good. She was very satisfied by PRM and was "taken aback by the flaw in the reserves." She noted that Farrell made presentations at the meetings and painted a picture that things were going well. She said it was "not satisfactory how she (Farrell) dropped the ball" and believed Farrell "single-handedly brought us down." Hardiman said Farrell admitted she had failed, and Sorenson attributed it to Farrell having "personal issues."

Trustee Campanelli told BST that the Trustees received less information from Arney and more from Sorenson when he took over. He recalled Arney always having difficulties with the reserves and disputes with the actuary and the actuarial reports. He noted that these problems lessened in the later years. He felt Sorenson was responsive at the Trustee meetings but became less so near the end when he believes Sorenson may have become ill.

In summary, despite collective efforts to achieve solvency, the Trust's chronic and growing deficit position, revelations of claims reserve misrepresentations, and growing discord and distrust among the Trust's key agents made continued operations untenable. Further Member assessments would have only prolonged the inevitable. The solvency issue was also exacerbated by the fact that the Trustees did not seek an independent claims analysis during a six-year period, despite being aware of the inherent financial incentive for PRM-CSI to under-reserve the claims, and of under-reserving of claims in prior years.

M. Claims Handling Procedures/Practices

The handling and processing of claims is an integral part of the trust administration process. Article VI, Powers and Duties of the Trustees, Section 6a of the Trust Agreement provides that the Trustees "take all necessary precautions to safeguard the assets of the Trust" including but not limited to the "(d)esignation of a third party administrator" for the resolution and payment of claims pursuant to the Workers' Compensation Law. This provision further stipulates that the fiscal agent and/or administrator appointed by the Trustees "shall not be an owner, officer or employee of a third party administrator." PRM's Administration Agreement with the Trust is silent with respect to its role with respect to claims administration, however, Section 2(g)

¹⁸³ Lasicki is Executive Director of the Association for Community Living which represents non-profit mental health residential agencies across the state.

authorizes the Program Administrator to “perform such other and further duties as are or may be reasonably related to the administration” of the Trust.

The Trust initially engaged Gallagher Bassett Services, Inc. (“GBSI”) to serve as the Trust’s third-party claims administrator. Evidence suggests GBSI was selected upon Arney’s recommendation and that annual written contracts were executed between GBSI and the Trust.¹⁸⁴

Records indicate that the Trustees and PRM began having concerns in or around 1997-1998 relating to staff turnover at GBSI resulting in claims audit problems and complaints from Members.¹⁸⁵ In 1999, the Trust, through PRM, issued a Request for Proposals to at least six (6) risk management firms, including GBSI, for claims management services. In a report to the Trustees, dated October 22, 1999, Arney presented the RFP process and the results of PRM’s analysis of the vendors reviewed. PRM recommended that the Trust continue with GBSI with increased oversight from PRM. GBSI’s services were extended through November 30, 2002.

Records indicate that in 2000, concerns arose regarding GBSI’s reserving practices. In September 2000, the Trustees approved an independent Claim Best Practice Audit by Tillinghast-Towers Perrin (“TTP”).¹⁸⁶ In a report dated November 15, 2000, TTP concluded: “The quality of overall claim handling provided was generally unsatisfactory as compared to similar third-party administrators handling workers compensation claims. There are several improvement opportunities that should be addressed.” Specific findings included the following:

- One-third of the claim files reviewed received an overall satisfactory score and met best practices standards.
- Both GBSI offices experienced numerous reassignment of claims to new claim handlers with Melville (NY) frequently reassigning claims between two to six times during the life of the claim, which contributes to handling deficiencies and delayed closure.
- Both offices lacked aggressive medical and disability management to move the claim toward a timely closure.
- Case planning was more goal-oriented and lacked the claim handler's (sic) next steps to achieve the goals of maximum medical improvement and return to work,
- Case reserves practices, in our opinion, were often too optimistic.
 - While most case reserves eventually reached the appropriate level, many were late to recognize the most likely ultimate outcome.
 - Many cases were closed prematurely while the case was still medically active and, in a few instances, still active in the litigation process.
 - Several cases, in our opinion, were inadequately reserved based on the injury and documented socio-economic factors.

¹⁸⁴ Chair Johnson signed the contracts on behalf of the Trust.

¹⁸⁵ Minutes for July 30, 1998 reflect a discussion of retaining Arney’s firm, CSI, for claims handling to replace GBSI. Arney presented a proposed contract to the Trustees, but GBSI was retained. PRM Claim Services, Inc. was formed on June 27, 1997.

¹⁸⁶ The WCB advised BST that PRM/CRISP did not reveal this report to the WCB.

- Most medical bills were paid within 30 days of receipt from the provider, thus meeting accepted standards.
- Most litigated cases were appropriately referred to defense counsel and properly bandied.
- We saw consistent adherence to settlement authorities and communication guidelines with PRM in high-dollar cases.

Minutes for February 22, 2001 reflect that John Conroy from PRM presented the TTP report to the Trustees. Minutes report “Gail Farrell and Christine Weber from PRM affiliate, CSI, made a presentation regarding their interest in replacing GBS as the third party administrator. Both indicated that they had the ability to perform the services better and in a more cost effective manor (sic) on an in-house basis. They proposed handling everything from the Albany office using independent examiners and experienced staff with the ability to handle the entire state from the Albany area.” The Trustees unanimously approved entering into a contract with CSI for claims administration with the condition that TTP would be brought in to perform a review of CSI’s performance on a quarterly or other basis.¹⁸⁷ A contract signed by Chair Johnson and Arney was executed between CRISP and CSI for third-party claims administration, effective May 1, 2001 through November 30, 2002 (see Exhibit 12).¹⁸⁸ We were not aware of any formal contract extensions to this initial contract.

By retaining CSI, the Trustees may have violated Article VI, Powers and Duties of the Trustees, Section 6a of the Trust Agreement stating the fiscal agent and/or administrator appointed by the Trustees “shall not be an owner, officer or employee of a third-party administrator.” As discussed previously, these distinct functions are best administered independently of any financial incentives the program administrator might realize from the deliberate under-reserving of claims. By serving as both CRISP’s Program Administrator and Claims Administrator, both PRM and its affiliate, CSI, were in a position to manipulate individual case reserves to portray the Trust in the most favorable financial light, thereby preserving their own financial interests as Program Administrator for CRISP and for the other trusts it administered. The potential conflict is further exacerbated by the fact that as Program Administrator, PRM had responsibility “to coordinate actuarial services relating to prospective and present Members of the Trust” thereby having influence in establishing the Trust’s reserve liabilities.¹⁸⁹

On October 26, 2001, the Trustees approved that TTP be retained by PRM to perform an audit of CSI’s claims handling practices.¹⁹⁰ In a report dated January 29, 2002, TTP concluded: “The

¹⁸⁷ The Trustees explored the feasibility of initiating litigation against GBSI for alleged mishandling of claims, but apparently did not do so on the basis of legal analysis performed by Gosdeck.

¹⁸⁸ The Agreement provided for automatic renewal for successive terms of one year.

¹⁸⁹ Gosdeck advised BST that the Trustees had some concerns about PRM having both the administration and claims management functions, and wanted a “firewall” between PRM’s administration and claims operations. PRM assured the Trustees the two functions were independent of one another.

¹⁹⁰ It would seem, in retrospect, that the Trustees should have engaged TTP directly, as PRM was essentially given the authority to arrange an audit of itself.

quality of overall claim handling provided compares favorably to that of similar third-party WC claim administrators and is close to a best practices level... PRM utilized a team approach to integrate the GBSI claims into the PRM process and was successful in achieving a smooth transition.” Specific findings included the following:

- Eighty-two percent (82%) of claims reviewed received an overall meets/exceeds score. The overall score of 82% is commendable, especially since it had only been six months since the transition of claims from GBSI to PRM began.
- There was little difference in the results between the GBSI-initiated and PRM-initiated claims, indicating both run-off and new claims received proper attention from PRM.
- Generally, we found GBSI-initiated claims were documented by PRM with summaries of the claim activities to date and contained a plans for moving the claims toward conclusion.
- Most GBSI-initiated claims, where the worker was still on temporary total benefits, were aggressively managed to position the claim toward settlement.
- Case reserves practices were appropriate and most claims were reserved at a level commensurate with the expected claim outcome.
- With a few exceptions, medical bills were paid within 30 days of receipt from the provider, thus meeting accepted standards.
- Litigated cases were promptly and appropriately referred to defense counsel. Follow-up activities were effective in moving cases toward reasonable results.
- Medical-only claims were well handled with appropriate clarification of compensability, recovery, and disability questions and timely payment of related medical expenses.

TTP’s review reported a marked improvement in claims handling by CSI.

Trustee meeting minutes reflect regular discussion of claims issues by CSI staff, including Gail Farrell and Christine Weber. Discussion included providing the Trustees a summary of claims received and pending, settlements, recoveries, payments, and reserves. Minutes for December 9, 2002 reflect Farrell reporting “...CRISP now has a solid handle on reserves, claims have leveled off and we are successful in closing older claims. Claim frequency is also down from prior years.” At the meeting of May 29, 2003, Farrell again reported that reserves “now appear to be at adequate levels and that payments on older claims are catching up with both settlements and awards disposing of older cases.” She further advised the Trustees that progress was being made on §32 Settlements.

Minutes for January 14, 2005 note Farrell reporting an increase in subrogation efforts and an increase of funds being returned to CRISP. The Trustees congratulated PRM for its efforts “in both subrogation and in reducing claims in general.”

Records show that in or around January 2010, the WCB had identified reserving problems with HCPSIT, another PRM-administered trust. In response, the WCB retained KBM Management,

Inc. (“KBM”), a third-party claims audit firm, to perform an “expeditious” quality assurance claim audit of the case basis reserves recorded on CRISP claims processed by CSI. In its report dated February 2010, KBM reported on its review of 25 open files representing a total incurred of \$2,908,494.80 (indemnity, medical, and expense payments/reserves) prior to the audit and a total incurred of \$3,691,816.02 at the time of the audit. Interestingly, KBM noted that a net increase in case reserves of over \$783,000 occurred in the six-day period from the date KBM sent PRM/CSI its selection list to the day KBM began its field work.¹⁹¹ KBM estimated that the then current total of \$3,691,816.02 reserved by PRM/CSI for these 25 files could have been “understated by as much as \$1,639,336 or 44% of the current total incurred amount.”

KBM indicated that some of the concerns described in the report “jumped off the page” while reviewing the reserves. These concerns included PRM’s/CSI’s failure to file a C-250 when evidence of a prior injury, late payment of medical bills, overpayments of both medical and indemnity, penalties for not filing forms timely, untimely payment of awards, and late notice to the excess carrier. Overall, KBM concluded that PRM/CSI “failed to demonstrate the use of proper reserving techniques and to provide a satisfactory level of claims processing service on behalf of the Community Residence Insurance Saving Plan Self-Insurance Trust” and recommended a comprehensive quality assurance claim audit to determine if other file deficiencies were present.

Johnson told BST that upon learning of CSI’s reported increasing of case reserves, she and the Trustees asked PRM’s Senior Vice President/Claims Manager, Gail Farrell, about it. Johnson recalled that Farrell told the Trustees she routinely adjusted reserves on an annual basis, and the Trustees were comfortable with Farrell’s explanation. However, the WCB later informed Johnson that such an adjustment was not done annually as represented by Farrell. Johnson stated that when confronted about this inconsistency, Farrell acknowledged that the annual adjustment was not performed contrary to what she had represented to the Trustees. Gosdeck confirmed this chain of events to BST. We were unable to confirm this with either Farrell or Sorenson. This apparent misrepresentation of the facts to the Trustees and adjustment of reserves in anticipation of a claims audit serious questions about the integrity of PRM’s/CSI’s claims practices and abrogation of its contractual obligations to the Trust.

In or about February 2010, evidence indicates that the WCB advised the Trust about the reserving problems with CSI involving the HCPSIT Trust.¹⁹² During the course of KBM’s review of CRISP on behalf of WCB, the Trustees commissioned their own independent case assessment review by Towers Watson (“TW”).¹⁹³ The Trustees discussed this review on February 17, 2010, and they approved a contract with TW. At this meeting, Gail Farrell from

¹⁹¹ KBM reported that it sent PRM/CSI its file selection list on January 27, 2010 and that all of the reserve revisions noted in its report occurred between January 27, 2010 and February 2, 2010. KBM’s audit field work began on February 1, 2010.

¹⁹² Meeting minutes for February 17, 2010 noted the Chair reporting to the Trustees that she had become aware from WCB of reserving practice problems with all group trusts specifically relating to CRISP’s Program Administrator.

¹⁹³ Towers Watson is an internal risk management consulting firm formed in January 2010 by the merger of Towers Perrin and Watson Wyatt. Johnson indicated that Sorenson referred Towers Watson to the Trust.

PRM/CSI reviewed the claims audited by KBM and outlined the PRM response. Farrell advised the Trustees that when the claims were reviewed, PRM/CSI “made upward and downward adjustments where they felt that was appropriate and that the overall adjustments to the 25 claims chosen netted to an amount of approximately \$155,000.” Sorenson said this amounted to “something less than ten percent of the entire population of claims.” After this discussion, the Trustees went into Executive Session. Upon their return, minutes report “...the Trustees unanimously expressed their confidence in the work being done on their behalf by PRM and PRM Claims Services.”

TW was charged by the Trustees with reviewing the same case files examined by KBM and a sample of another 25 open claims to determine the reasonableness of the current case reserves.¹⁹⁴ TW’s report dated March 9, 2010 included, inter alia, the following findings:

- CRISP’s current aggregate WC reserves are within what we generally consider a reasonable estimation of expected ultimate payout. Based on the review sample, the variance between the Towers Watson estimate (indemnity and medical reserves) of \$2,388,693 and CRISP’s estimate of \$2,215,060 was 7.3%. We consider plus or minus (10%) a reasonable level of difference.
- While the stated reserve philosophy is appropriate, we found that the philosophy is not consistently applied. Consistent reserving practices are part of the case management planning process needed to manage claim outcomes and avoid financial liabilities. Although the variance percentage of 7.3% is within a reasonable level, many of the cases were very slow to develop appropriate case reserves to a more reasonable level based on case circumstances.
- As indicated above, the philosophy of reserving to ultimate probable costs based on circumstances was not always followed. In our opinion, current outstanding case reserves are within reasonable levels, however, 58% of the claims in the total sample (29 of 50) had case reserves increases in January and February of 2010.
- Prior to the February 2010 reserve changes, we noticed several claims that were inappropriately being paid without reasonable levels of outstanding future case reserves at various times during our test period from 2006 to present. This was particularly true in medical case reserves.
- In four cases, we found reserves small incremental changes (known as stair-stepping) that did not accurately reflect the value of the cases. In most cases, the outstanding case reserves were nearly depleted before the small increases were made. All cases reflected ongoing benefits that should have been evaluated for ultimate probable exposure.
- We agreed with CRISP’s most recent case reserves in 88% of the indemnity claims and 80% of medical case reserves reviewed.

TW recommended that PRM develop a remediation plan for the deficient cases, CRISP closely monitor case reserves on a regular basis, and that a follow-up review be performed in one year.

¹⁹⁴ TW performed its analysis from February 22-26, 2010.

While perhaps not as critical as KBM's report, TW found notable case reserving deficiencies and confirmed PRM's upward adjustment of case reserves in January/February 2010.

The Trustees discussed the results of the TW audit at a meeting on March 24, 2010. Minutes report that the audit "...showed severe under reserving prior to the adjustments early this year." In addition the minutes stated: "Contrary to Gail Farrell's assertions to the contrary, there was little evidence that there was an annual regular review and adjustment of claims. Gosdeck and the Chair discussed the claim review with Farrell and Sorenson during a conference call on March 12, 2010. Farrell admitted the essential conclusions contained in the audit without much further comment."¹⁹⁵ Minutes indicate that Johnson and Gosdeck suggested that if the Trust "has a short life span the claims should remain at PRM CSI but that Farrell should be excluded from any role in this activity. Johnson also suggested that PRM should be responsible to the trust for repayment of some of the moneys it paid for claims services during this period."

Chair Johnson mentioned to the Trustees that "...the auditor had contacted Farrell regarding major reserve discrepancies and Farrell agreed to the problem but did not contact Sorenson about this conversation until she was questioned by the Chair on this issue. Johnson noted that, in her opinion, Farrell did not understand the importance."

At this meeting, minutes report Sorenson "noted distress that almost half of claims reviewed had some issues noted by the auditors..." and "...an increased responsibility on his part and suggested that the Trustees must approve giving him this authority." When asked by a Trustee if the problem at CSI involved more than CRISP, Sorenson responded: "... this is not known for certain, but the severity was likely higher here because CRISP has more claims than the other trusts."

Sorenson further commented that these comments were "about a partner in the firm" and that "...this is a failure of CSI to perform as in the past that he is having trouble accepting." Sorenson said he "will not support any continuing role for Farrell or (Arthur) Coats in the future claims reserving or leadership" and that PRM "was willing to reimburse CRISP for the expense of the recently completed audit given the nature of the results of the audit." Sorenson put forth a 45-day remediation plan with the following goals:

1. Quantify adequacy of all open indemnity and medical reserves.
2. Correct reserve levels where needed.
3. Improve claim system edits and reporting in specific areas to eliminate shortfalls in reserves, as well as payments on claims with depleted or low reserves.
4. Establish management reporting to clearly identify results of reviews and assure ongoing proper activity with CRISP reserves.

The Trustees approved Sorenson's plan and the continuation of "PRM and PRM CSI in their current capacities." The Trustees further charged the Chair to work with Gosdeck "to negotiate

¹⁹⁵ Both Johnson and Gosdeck confirmed these events to BST during their interviews.

a financial settlement with PRM CSI for its damages sustained as a result of the inadequacies in claims administration.”

Following the official release of KBM’s findings, the Trustees asked TW to “perform a review of 10 open claims selected by CRISP to provide an independent opinion as to the reasonableness of case reserves.¹⁹⁶ TW issued its report in June 2010 that included the following overall finding:

The total variance (indemnity and medical reserves) between CRISP’s case reserves and Towers Watson’s recommended case reserves is 14.7%. We consider plus or minus ten percent (10%) a reasonable level of difference. However, this is a small sample specifically selected to test the philosophy and methodology.

Minutes for July 12, 2010 note the Trustees voting unanimously to engage counsel to pursue “E&O claims against CSI...” At this meeting Sorenson outlined various proposals for claims administration services to replace PRM/CSI. He noted that the WCB would be mandating separation of claims and administration under the revised rules and regulations that E&O carrier would not be writing future policies for group administrator TPAs in New York State. As a result, CRISP would need a new claims services provider. Four proposals were put before the Trustees for consideration and phone interviews would be scheduled.

Also at this meeting, a report was given to the Trustees of a claims review undertaken by former PRM employee Christine Weber at the Trust’s request. Weber was assigned to review each claim and report to Johnson and Gosdeck on a weekly basis. Minutes report that 338 indemnity files were examined, all over one year old, resulting in a “total increase in incurred of \$4,941,240.” Trustees were advised that Debbie Turner from TW reviewed Weber’s product and opined that the reserving was appropriate. Sorenson added that “even though case reserves increased by \$5 Million, there is sufficient IBNR reserves estimated by BYNAC within the same years as the reserves that were increased to more than support the reserve strengthening.” Sorenson also commented on the KBM review and while acknowledging reserving errors were made by CSI, he stated “the KBM review is slanted unfairly against CSI out of context.”

The Trustees terminated the CSI’s claims management contract and executed an Agreement for Third-Party Claims Administration Services, effective August 1, 2010 with PMA Management Corp. (“PMA”), a WCB-approved third-party claims administrator.¹⁹⁷

Gosdeck told BST that he felt Sorenson was slow to acknowledge the growing claims reserve problems. He added that the minutes show, in his opinion, that PRM had misstated the adequacy of reserves, and the Trustees relied on Farrell’s assurances about the reserves’ adequacy. Gosdeck stated that he believed the issues with the Trust’s claims reserves might have been influenced by problems with HCPSIT that perhaps overwhelmed PRM, as HCPSIT constituted

¹⁹⁶ TW reviewed an additional eight claims. The claim sample was selected by PRM at the direction of CRISP and consisted of open claims with recent significant increases in case reserves.

¹⁹⁷ BST was able to obtain only a Mark-up draft of the Agreement.

the bulk of PRM's business. Concerning PRM's contributing role with respect to the Trust's ultimate deficit, he said "at best it was inattention, at worst, it was willful."

Trustee Hardiman was similarly adamant about the under-reserving problem. She recalled that Farrell made presentations at the meetings and painted a picture that things were going well. Hardiman was not at the Board meeting when Farrell was reportedly confronted about the reserve problem. Hardiman said it was "not satisfactory how she (Farrell) dropped the ball" and believed Farrell "single-handedly brought us down." Hardiman indicated that Farrell admitted to the Trustees that she had failed and that Sorenson attributed the problem to Farrell "having personal issues."

Trustee Lasicki said she "only heard great things" about PRM from her members¹⁹⁸ who felt PRM was responsive to their needs. She was satisfied with CSI's claims handling until early 2010 when she was "blown away" by the under-reserving. She said it "all sounded good" from PRM, and the Trustees relied on PRM's expertise. She said she had no indication that Farrell from CSI had done anything "malicious" or that CSI was "incompetent." Lasicki felt the Trustees received a "lot of misinformation from Ed (Sorenson)." For example, she recalled that he could not produce a master list of the Members when asked. She recalled that PRM also failed to tell the Trustees that Sorenson had a medical issue and was recovering out of state.

As part of its review, BST retained KBM to review CRISP's claim files and determine whether claims were handled in accordance with written policy and industry standards, whether benefits were paid in a timely manner, and whether claims were appropriately reserved and adjusted as the cases matured. The audit examination included a sample of claimants' files with dates of injury from November 22, 1999 through January 12, 2010. The total dollar value of the claims audited is approximately \$971,500.¹⁹⁹ In its report to BST dated March 2012, KBM presented the following findings (Exhibit 13):

- Of the nine open claims reviewed, it was determined that three of the files had reasonable reserves for the known exposure. Of the remaining six open files, we believe five had low and one was mixed.
- Based on the audited claims, the administrators prior to NCA failed to provide a minimum level of claims processing service on behalf of CRISP. Industry averages require 95% procedural accuracy; we show that PRM only processed 25.89% of the medical bills within 45 days of receipt, and PMA processed them at 62.76%.
- The deficiencies described in this report involve overall claim management, undocumented payments, late payments, and poor transfer of information.
- Due to our limited file sample, we are unable to estimate the overall financial loss to CRISP generated by its prior administrators; however, of the seventeen (17) claims

¹⁹⁸ Lasicki is Executive Director of the Association for Community Living which represents non-profit mental health residential agencies across the state.

¹⁹⁹ KBM noted in its report that "...the transfer of information from PRM to PMA was incomplete and haphazard. Financial information is missing from files and NCA has even discovered the wrong financial information assigned to a file."

reviewed, eight (8) contained several financial errors (indemnity overpayments: \$1,009.47, medical overpayments: \$2,000.32, expense overpayments: \$500.00) and one (1) contained penalties (\$50) which is significant when interpolated to all the claims incurred during the Trust's entire active life.

In summary, BST offers the following finding relating to the Trust's claims handling practices:

- The Trustees acted prudently in seeking qualified “second opinions” when questions arose as to the claims reserving practices of both Gallagher Bassett and CSI, although the Trustees did not proactively seek similar opinions during a six-year period given the known inherent risk.
- The Trustees, by selecting PRM affiliate CSI as the Trust's claims administrator, appear to have violated Article VI, Section 6a of the Trust Agreement that requires that the fiscal agent and/or administrator appointed by the Trustees “shall not be an owner, officer or employee of a third party administrator.” The failure of the Trustees and Trust Counsel who drafted the Trust Agreement to ensure the independence of the program administrator and claims handling functions may have had a material impact on the extent of the ultimate Member deficit.
- CSI failed to establish adequate case reserves, resulting in the Trust and PRM not increasing Member contributions or assessments sufficient to cover the true deficit.
- CSI failed to properly advise the Trustees of the inadequacy of case reserves and offered no viable explanation to the Trustees as to the reasons for these inadequate reserves.
- The understating of the Trust's reserve liabilities by CSI (as noted by the Trust's claims consultants) and the underreporting of these liabilities on the Trust's financial statements may have painted a false and misleading picture of the Trust's true financial position.

SCHEDULE OF EXHIBITS

<u>EXHIBIT #</u>	<u>DESCRIPTION</u>
1	Trust Agreement, October 31, 1995
2	By-Laws, October 31, 1995
3	Indemnity Agreement, October 31, 1995
4	PRM Group Application Cover Letter, December 11, 1995
5	PRM Administration Agreement, October 31, 1995
6	MPA Marketing Agreement, October 31, 1995
7	PRM Qualifying Officer Resignation Letter, April 12, 2010
8	CACI Consulting Report to BST, October 13, 2011
9	MPA Marketing Agreement, October 31, 2000
10	PRM Marketing Agreement, September 30, 2009
11	MPA Errors and Omissions Policy, November 19, 2008
12	PRM/CSI Claims Administration Agreement, May 1, 2001
13	KBM Management, Inc. Quality Assurance Claim Audit Report to BST, March 2012