



# Report Highlights

## Office of Risk Management

### Cost Savings Update - Fiscal Year 2015

DARYL G. PURPERA,  
CPA, CFE

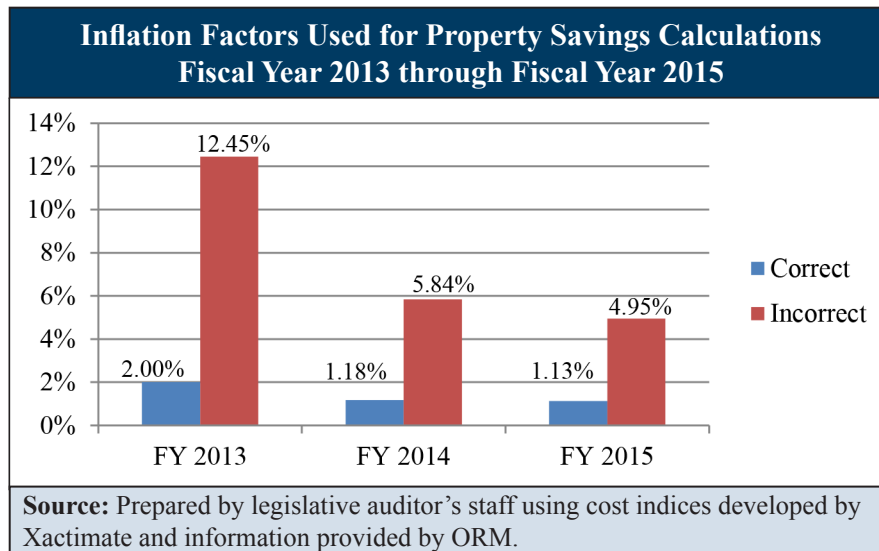
Audit Control # 40150027  
Performance Audit Services • June 2016

## Why We Conducted This Audit

On June 8, 2010, the Division of Administration's Office of Risk Management (ORM) awarded F.A. Richard & Associates (FARA) a five-year contract to privatize the state's lines of insurance and loss prevention services. Because the contract guaranteed that FARA would save the state \$50 million and ended on June 30, 2015, we conducted this audit to evaluate ORM's calculation of the final savings and any applicable penalties.

## What We Found

Overall, we found that the privatization contract resulted in net program savings of \$9.8 million over five years. However, FARA did not achieve the \$50 million in claims savings that the contract required. As of June 30, 2015, ORM calculated that FARA had achieved \$48 million (96%) of the \$50 million in guaranteed payment savings. However, we determined that ORM incorrectly calculated the inflation rate related to the property line of insurance for fiscal years 2013, 2014, and 2015. This mathematical error resulted in ORM applying an incorrect inflation factor during these three years which overstated FARA's claims savings. The correct and incorrect inflation factors used are shown below.



We calculated that FARA owes the state \$185,288 for not achieving the contractually-required \$50 million in guaranteed savings. Using the correct inflation factors, we found that the guaranteed savings as of June 30, 2015, should be \$43.8 million, or 87.6% of the \$50 million guaranteed by the contract. Since FARA did not achieve the \$50 million in savings as guaranteed, the contract requires that FARA refund the state 3% of the shortfall, up to \$1.5 million. While ORM agreed that it had used the wrong inflation rate in fiscal years 2013 through 2015 for property lines of insurance and therefore incorrectly calculated FARA's savings, it only invoiced FARA for \$59,252 (3% of the incorrect \$2.0 million shortfall). ORM stated that based on its professional judgment and day-to-day involvement with property claims, the inflation factors they used more accurately reflect the inflation rate for property lines of insurance during the contract period.