

*Finance, Management & Operations*

**LTC Risk Management,  
Auditing and Financial Controls**

Jillian Cataloni, EY

Lisa White, Bankers Life



**16th Annual Intercompany Long Term Care Insurance Conference**

# Why are these topics important?



- Three key reasons
  - Find risks you are not aware of
  - Ensure smooth-running operations
  - Mitigate company exposure to financial, reputational and other risks
- Companies with strong risk cultures proactively work to identify and prevent risk
  - Where do we not have transparency today?
  - What issues are we hearing about from our customers?



# Three lines of defense model



## Company Lines of Defense

1 <sup>st</sup> Line of Defense Front line and management level	2 <sup>nd</sup> Line of Defense Risk management function and controls	3 <sup>rd</sup> Line of Defense – Internal Audit	External Audit
<ul style="list-style-type: none"> <li>• <b>Purpose:</b> <ul style="list-style-type: none"> <li>• Execute business processes and operate controls to mitigate key risks</li> <li>• Owns the risk</li> </ul> </li> <li>• <b>Key Activities:</b> <ul style="list-style-type: none"> <li>• Control procedures operated within business processes</li> <li>• Oversight procedures operated by management</li> <li>• Reporting on risks, issues, mitigation plans, incidents and operational losses to support risk functions</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <b>Purpose:</b> <ul style="list-style-type: none"> <li>• Establishes the risk management framework for the first line of defense</li> <li>• Provides independent challenge and monitoring</li> </ul> </li> <li>• <b>Key Activities:</b> <ul style="list-style-type: none"> <li>• Risk program &amp; charter</li> <li>• Process, risk and control framework</li> <li>• Risk and control assessments oversight, standards &amp; guidance</li> <li>• Capital reserve calculations and scenario analysis</li> <li>• Risk quantification and treatment</li> <li>• Regulatory exam management</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <b>Purpose:</b> <ul style="list-style-type: none"> <li>• Provides assurance that the risk framework and the resulting policies and procedures are operating as intended.</li> </ul> </li> <li>• <b>Key Activities:</b> <ul style="list-style-type: none"> <li>• Determination of audit universe</li> <li>• Scheduling and coordination of audits and risk coverage</li> <li>• Audit execution</li> <li>• Board and executive reporting</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <b>Purpose:</b> <ul style="list-style-type: none"> <li>• Independent review of first three lines of defense</li> </ul> </li> <li>• <b>Key Activities:</b> <ul style="list-style-type: none"> <li>• Understand service requirements, determine audit scope, and establish the team</li> <li>• Identify SCOTs, perform walkthroughs, design test of controls and prepare audit strategy</li> <li>• Execute test of controls and perform general audit procedures</li> <li>• Conclude on overall review</li> </ul> </li> </ul>

Supported by sound risk cultures and practices. Well-aligned tone from the middle with the tone from the top.

# Three lines of defense in action!



- Operations Processes
- Actuarial Processes
- Management Oversight

# Case Study: Paid Past Policy Maximum



Is it possible to pay past the maximum allowable benefit?

# Case Study: Paid Past Policy Maximum



- Yes!
- Benefits are sometimes still being paid past the maximum allowable
- Actuarial may be able to help Operations if they have controls in place to scrub claim reserve extract



- How can we improve?
  - Develop a report applying the Actuarial logic to claim data for identifying policies that should have exhausted benefits
  - Add a control to the claims system to prevent this from occurring

# Case Study: Premium-Paying Maxed Cases



Is it possible that we are charging premiums on policies that no longer carry a benefit?



# Case Study: Premium-Paying Maxed Cases



- Yes!
- Policyholder may alert us that we are charging premiums on a policy that no longer has benefits
- Root cause could be system fails to lapse policyholders automatically upon reaching maximum



- How can we solve this problem?
  - Develop a report that identifies cases that have no remaining benefit but still show as premium-paying
  - Determine a system solution that notifies policyholders that benefits are exhausted and policies will be terminated (non-Restoration of Benefit policies)

# Case Study: Inaccurate Claim Payments



Is it possible that we could pay claims incorrectly?

# Case Study: Inaccurate Claim Payments



- We sure can!
- First line of defense Claims Audit department reviews 3-5% of claims processed for financial accuracy
- Claims Audit, by its very nature, cannot identify all inaccurate claim payments



- How can we improve?
  - Accept that there may be larger problems
  - Develop analytical models to run against entire claim payment universe to attempt to identify cases that are potentially over or underpaid
  - Provide feedback to claims management on quality results and common errors

# Case Study: Waiver Of Premium



Are we properly applying waiver of premium  
to policyholders?

# Case Study: Waiver Of Premium



- Not always!
- A fresh perspective is helpful in identifying issues like this
  - Could we have the same problem?
- Waiver of premium is not always straightforward and it can be a challenging control to build into a system



- How do we prevent these mistakes?
  - Create and review a report identifying the policyholders on claim but not on waiver and on waiver but not on claim.
  - Investigate system enhancements to help apply waiver of premium correctly





Is an existing control working?

# Case Study: Claim Denials & Appeals



- Not sure!
- All claim denial decisions and appeal decisions are required to be reviewed by a committee before finalizing
- The honor system is used to ensure that all claim denials and appeals are reviewed



- How can we be sure all cases are reviewed?
  - Complete a niche audit to ensure protocols are being followed.
  - Compare systems data to manual logs. Be aware of risks of manual logs!
  - Name Chairs/Owners of the oversight committees in place



Are there issues related to inappropriate claim activity?

# Case Study: Red Flags



- You bet!
- It is estimated that up to 10% of all insurance claims are fraudulent according to the Coalition Against Insurance Fraud
- Company SIU Departments can share examples of fraudulent claims



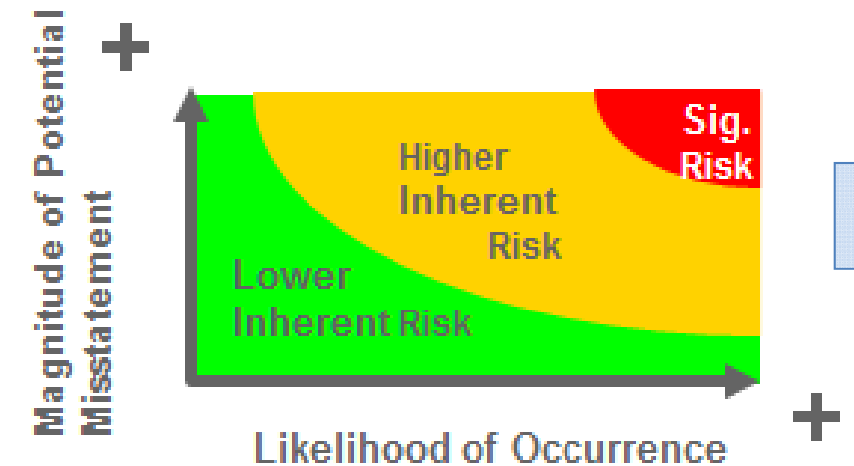
- What can we do to identify fraud?
  - Discover common attributes among known fraudulent claims
  - Build a series of models using analytical tools that identify “red flags”
  - Key claim experts should analyze the “flagged” cases



## External Audit viewpoint

- Identifying areas of focus
- Building a perspective on risk and controls
- Illustrative examples

# Identifying areas of focus



Significant risks are those with both

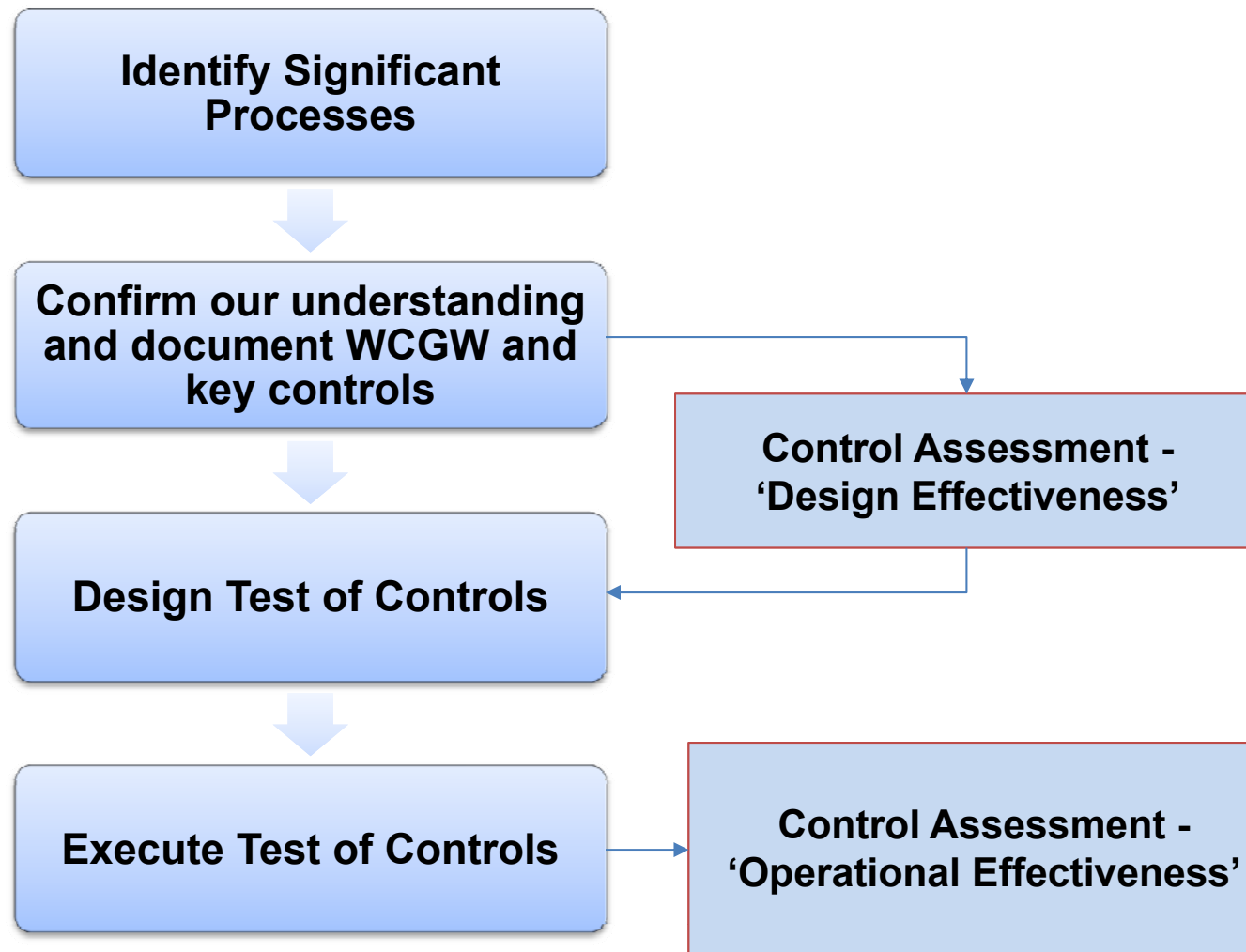
- (a) high likelihood of occurrence and
- (b) potential for a material financial impacts

## Considerations in developing and testing controls

- ▶ Identify significant accounts, relevant assertions, and disclosures
- ▶ Consider risk appetite and what is important to organization
- ▶ Identify related processes and areas of risk
- ▶ Think through “what could go wrong” (WCGW) items and perform walkthroughs of processes and existing controls
- ▶ Design of controls important in addition to execution of controls
- ▶ Document, document, document



# Building a perspective on risks and controls



# Examples of risk and control identification



Macro Risk	Sub Risk	Mitigating Controls	Preventive or Detective	Control Frequency	Control Owner	Appropriately Mitigated?
Incorrect premium amount is billed	Stale data used in billing run	The Billing Analyst performs data validation after uploading the billing run. Reconciliation of source file totals to uploaded totals are retained as evidence.	Detective	Daily	Jane Doe, Billing Analyst	Yes
		Billing Analyst receives an automated system-generated email when new billing file is uploaded to the billing system.	Preventive	As Needed	John Mack, IT Technician	
	Data files are invalidly manipulated before being uploaded to billing system	<b>Control Gap Noted</b> Data files are stored in a shared drive that can be accessed outside the Department. Files not appropriately secured.	-	-	-	No

# Illustrative experience studies process



## 1. Gather Data

- Determine time period of study
- Ensure complete and accurate set of data from chosen time period
- Scrub data appropriately to remove inconsistent or irrelevant data
- Review data and make sure it is appropriate for use
- Implement data into data warehouse to perform experience study

## 2. Perform Experience Study

- Calculate and determine new assumptions
- Peer review of experience study calculations
- Document recommended assumptions

## 3. Obtain approval from management

- Hold regular meetings informing management of recommended assumptions changes
- Obtain formal sign off of new assumptions (including meeting minutes with management involvement and signatures)

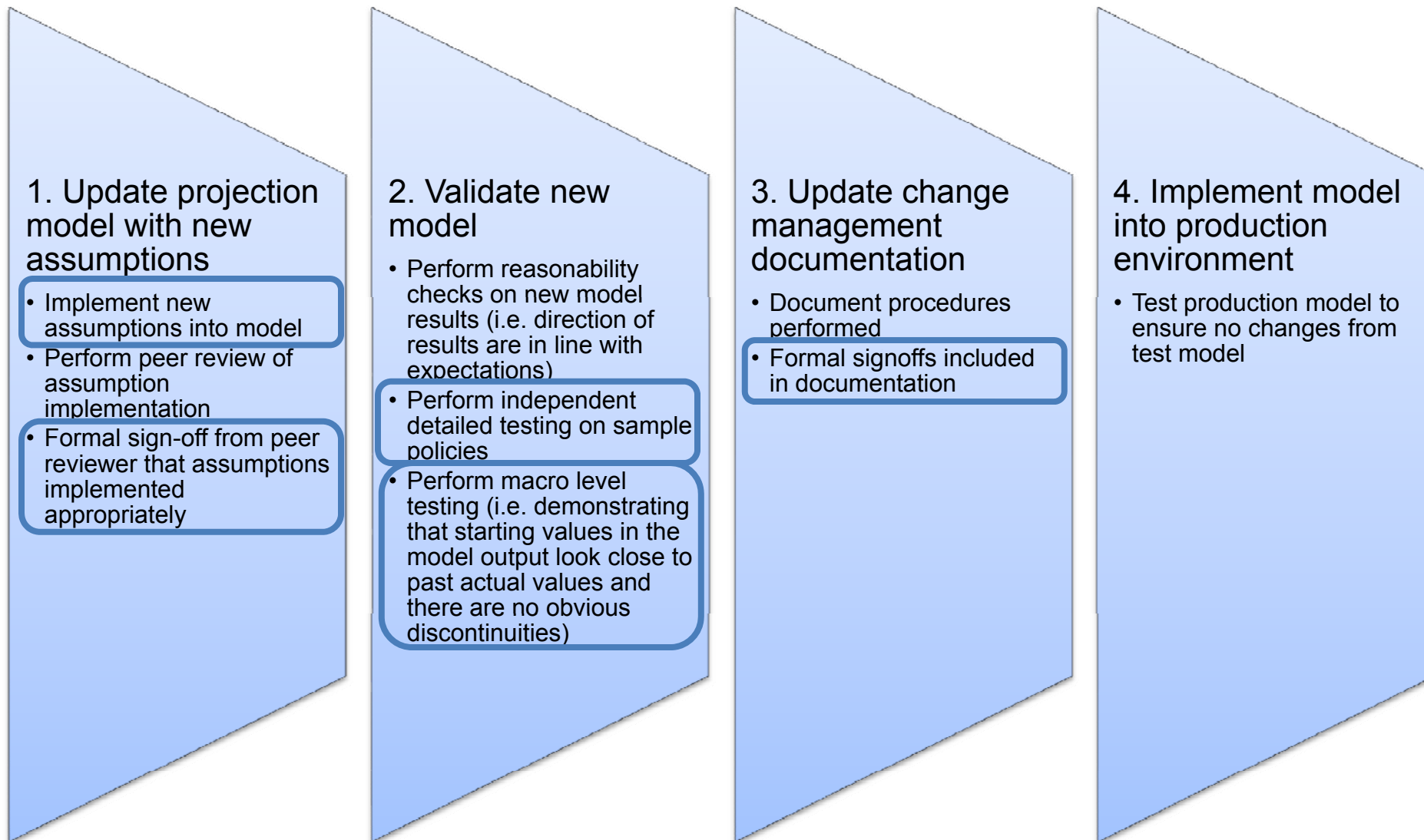
## 4. Implement assumptions in new model

- Perform change management controls

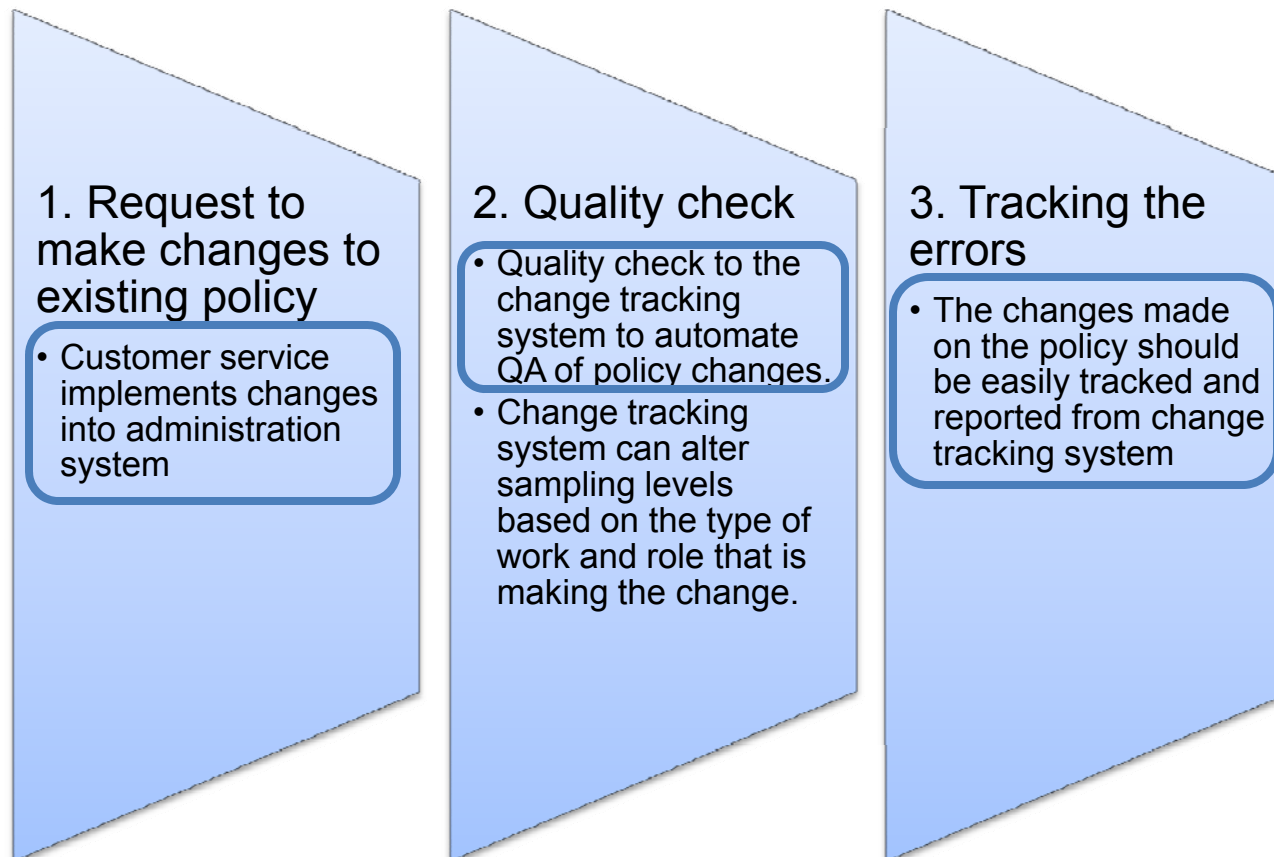
# Illustrative annual model update process



*i.e. projection models, loss recognition, claim reserve models*



# Illustrative policy modifications process



# Key takeaways



- 1** *Effective risk management and control is often a matter of culture*
- 2** *Management should consider the entire process end-to-end*
- 3** *Risks can be mitigated in two ways – prevention and detection!*