

A photograph of a sunrise over a mountain range. The sun is partially obscured by a large, dark cloud on the left, with rays of light breaking through. The sky is a clear, deep blue.

A New Day For Healthcare

ACORD LOMA Insurance Systems Forum

Enterprise Risk Management Presentation

May 25, 2010



Overview

- Who we are and how our business model framed our problem
- What is ERM?
- Why we implemented ERM
- What we wanted to do...
- What we did...
- What happened...
- What we learned...
- and what we might do different

Who is Essence? What does it do?

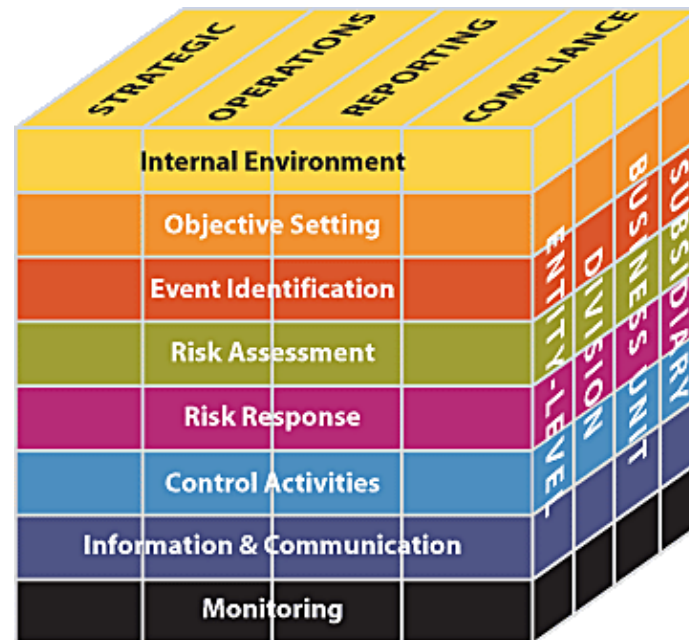
- Organizational history and ownership
 - Clinical and technology roots
 - Significant clinical and technology skills
 - Developing operational and risk assumption skills
 - Owned by world class venture capitalist
- Enables physicians to control their practice and assume risk:
 - Frequently works with delegated medical groups
 - Medicare Advantage Plans
 - Capitation funds care
 - Essence acts as back office

What is Risk Management?

- **Risk management** is activity directed towards:
 - Identifying risk
 - Assessing risks (quantifying into likelihood and Impact)
 - Mitigating risk (to an acceptable level)
 - Monitoring Risk.
 - Tying risks back to objectives.
- In businesses, risk management entails organized activity to manage uncertainty and threats. The program involves people and tools to identify and manage risks.
- Risk Response strategies include:
 - Accepting risk.
 - Mitigating the risk
 - Sharing the risk
 - Controlling risk

COSO ERM Framework

Objectives: The types of risk. All risks are categorized in to one or more of these groupings. A fifth grouping may be applied “Safeguarding Assets”



Activities: These processes will operate under the ERMP. The principle is to develop a risk management culture in all levels of the organization, and in all activities, from strategy development down to the front line.

Portfolio View of Risk: The ERMP will utilize a business unit perspective and an entity level perspective to develop a portfolio view of risk. This top to bottom approach helps balance the significance of risk and helps ensure all important exposures are managed.

Source: COSO

Eight ERM Activities

- **Internal Environment** – The internal environment encompasses the tone of an organization, and sets the basis for how risk is viewed and addressed by an entity's people, including risk management philosophy and risk appetite, integrity and ethical values, and the environment in which they operate.
- **Objective Setting** – Objectives must exist before management can identify potential events affecting their achievement. Enterprise risk management ensures that management has in place a process to set objectives and that the chosen objectives support and align with the entity's mission and are consistent with its risk appetite.
- **Event Identification** – Internal and external events affecting achievement of an entity's objectives must be identified, distinguishing between risks and opportunities. Opportunities are channeled back to management's strategy or objective-setting processes.
- **Risk Assessment** – Risks are analyzed, considering likelihood and impact, as a basis for determining how they should be managed. Risks are assessed on an inherent and a residual basis.
- **Risk Response** – Management selects risk responses – avoiding, accepting, reducing, or sharing risk – developing a set of actions to align risks with the entity's risk tolerances and risk appetite.
- **Control Activities** – Policies and procedures are established and implemented to help ensure the risk responses are effectively carried out.
- **Information and Communication** – Relevant information is identified, captured, and communicated in a form and timeframe that enable people to carry out their responsibilities. Effective communication also occurs in a broader sense, flowing down, across, and up the entity.
- **Monitoring** – The entirety of enterprise risk management is monitored and modifications made as necessary. Monitoring is accomplished through ongoing management activities, separate evaluations, or both.

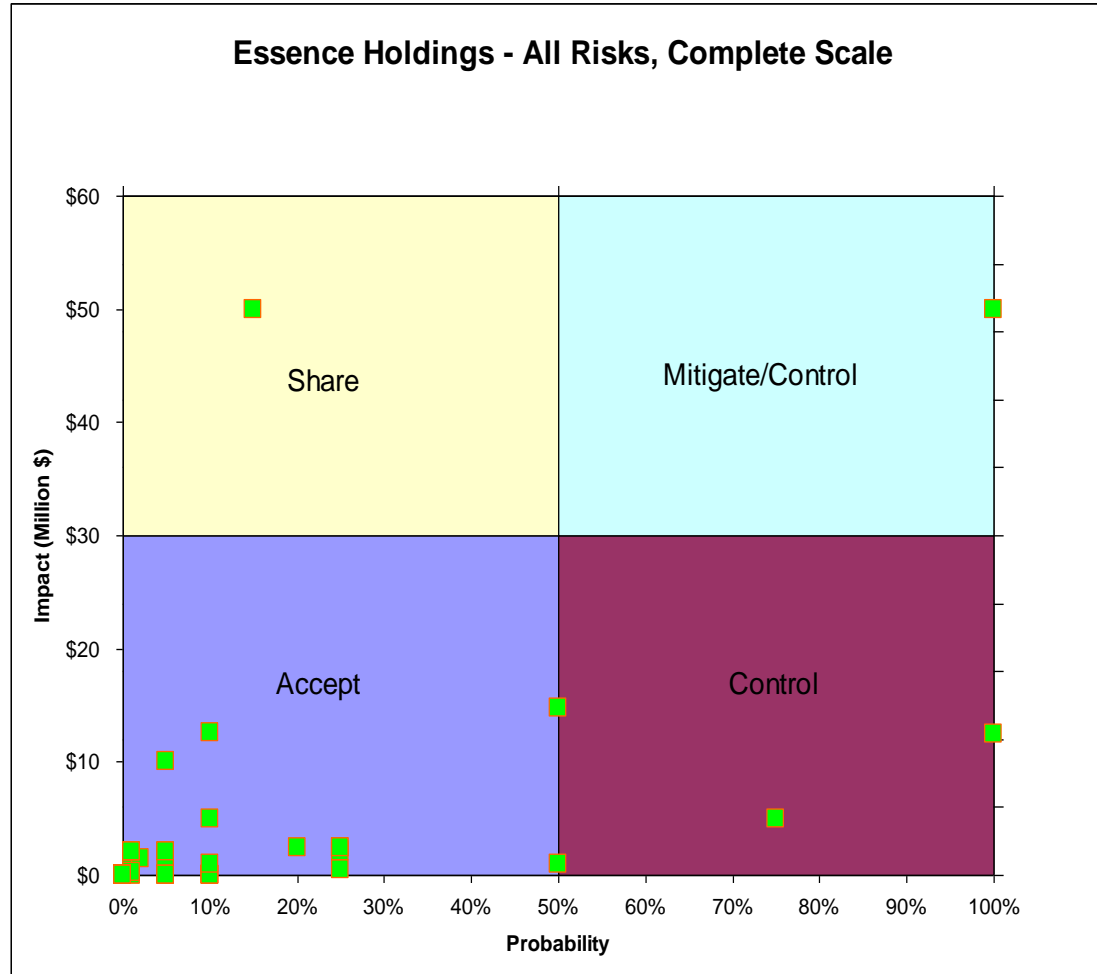
Event Identification Tools

- *Event Inventory: A listing of potential events common to an industry or functional area (Done)*
- Corporate Objective Analysis Workshop: Analyze objectives against external and internal factors
- Interviews: Key personnel are provided background material and interviewed to determine the functional link to business objectives, the risk factors related to the functions, their likelihood and impact
- Questionnaires and Surveys: Used for assessing potential risks from vendors or business partners. Can be used internally as a self check for process control.
- Process Flow Analysis: Draw a flowchart of the process and list potential risk events steps in the process
- Leading Event Analysis: Determine external or internal leading events, such as news stories and industry happenings.
- Loss Event Tracking – List the internal historical loss events and review cause/effect. List industry wide loss events and determine impact on Essence.
- Ongoing Events Identification – potential events are identified on an ongoing basis by reviewing specific indicators, both internal and external.

Identified Risks with Probabilities and Amounts

item #	Area of Concern	Risk	Category	Likelihood of Occurance (0.0-1.0)	Financial Impact (per \$1 Million)
1	Infrastructure and Technology	Security Breach - theft of data (from outside)	Compliance	5%	5.0
2	Infrastructure and Technology	Security Breech - theft of data from inside	Compliance	20%	2.0
3	Infrastructure and Technology	Massive EPHI publication	Compliance	5%	5.0
4	IT Product Development	Long Term Project Failure to Complete	Compliance	20%	5.0
5	Market and Growth	Non-Compliance with Brokers	Compliance	10%	
6	Market and Growth	CMS Rate reductions	Compliance	100%	12.5
7	Operations (Health Plan)	Non-Compliance (CMS un-reconcile)	Compliance	1%	0.5
8	Medical Management	Inappropriate denials	Compliance	10%	5.0
16	Compliance	Fines / Penalties / Sanctions	Compliance	5%	1.5
17					
18	Analytics	Data not used by appropriate person.	Operations		
19	Business Development	bad contracts	Operations	25%	2.4

Risk Management – An Extension of Strategy



Risk Control Strategies

- Low Probability, Low Financial Impact
 - Employee training
 - Work rules and operating procedure
 - Well trained supervisors and mid managers
- Low Probability, High Financial Impact
 - Insure
 - Share risk with vendors
 - Hedge risk
- High Probability, Low Financial Impact
 - Defined processes (CMMI Context)
 - Increased management oversight
 - Technology innovation
- High Probability, High Risk
 - Internal control
 - Separation of duties
 - Personal responsibility, transparency and reporting

Why we Implemented ERM - Leadership Drivers

- Key concept:
 - the risk of not achieving the enterprise's goals was relatively high due to the fast growing, entrepreneurial nature of the enterprise in two directions, technology and health care. Executives determined that the enterprise would benefit by institutionalizing a risk management framework that would place more rigor on goal development and ultimately achieving those goals.
 - With diverse businesses operating under the Essence umbrella, executive leadership desired a consistent assurance that various management teams were operating in an acceptable risk management envelope, and that their risks could be quantified and rolled up to a portfolio view of risk.
 - Leadership determined that a corporate risk management program would engage management on consistent issues important to the enterprise, internal control and reporting that ultimately would help the enterprise respond to stress, set realistic goals and achieve them

Why We Implemented ERM - Management Drivers...

- Among the many risks we faced – which may be similar to those you face – we faced an unusual risk:
 - Given our owners, risks of not making our strategic commitments would have dramatic results. Organizationally we had an early history of not making realistic commitments or keeping reasonable ones.
- Essence also faced significant complexity from the health care environment, Medicare rules and uncertainty about local market conditions
- Rapidly growing enterprise without a well defined strategic planning process
- Rapidly building management infrastructure
- Integrate new mid-level management who came with a diversity of backgrounds and skill levels
- Actively engaged an several market niches while a key business segment emerged
- A well defined ERM would be responsive to new regulations and regulatory bodies involved in the core business segment

What we did...

- Executive team developed consensus that we had a risk management problem and needed a program
- CFO managed initial actions
- Hired consultant to assist. The consulting firm who had prior experience with Essence. Consultant assigned had experience as health plan COO and CFO.
- Conducted an internal discovery process and used it to design a program tailored to:
 - Have the classical elements of a Enterprise Risk program
 - Adapt them to our current capabilities
 - Reflect unique organizational and cultural aspects of Essence
 - Significantly improve communications in the mid-level management cadre and improve their perception of risk and their ability to help us manage it.
 - Build Risk Management awareness in the culture of Essence

Implementation Activity...

- Implementation
 - Over the period of one quarter, through a series of facilitated meetings, the management team developed Essence's ERM based on the COSO framework
 - Senior management and departmental management were engaged in the concepts and practical implementation of the framework
 - A Risk Manager was appointed to operate the program, reporting to the General Counsel
 - The Board was engaged in the program, and regular reporting began
- First Year Operation
 - The ERM was introduced and encultured through the Employee Handbook, regular meetings with departments, an internal website and other tools
 - As the program rolled out, departments were engaged and began requesting risk management assistance
 - Special focus was placed on developing the Corporate Risk Appetite with Sr. Management and the Board

What we learned...

- It worked!
 - We have a defined strategic planning process that includes risk management.
 - We are more aware of the risks we face
 - We manage them better and more proactively
 - Our mid-level staff are managing better and communication better than before.
 - We have a systematic cause and effect method to review problems and opportunities
- Engaging staff was key
 - Explain risk and why it is important
 - Allowing them tools, time and talent to sort through their operations
 - Create an environment where discussions of risks and problem are part of normal management practices

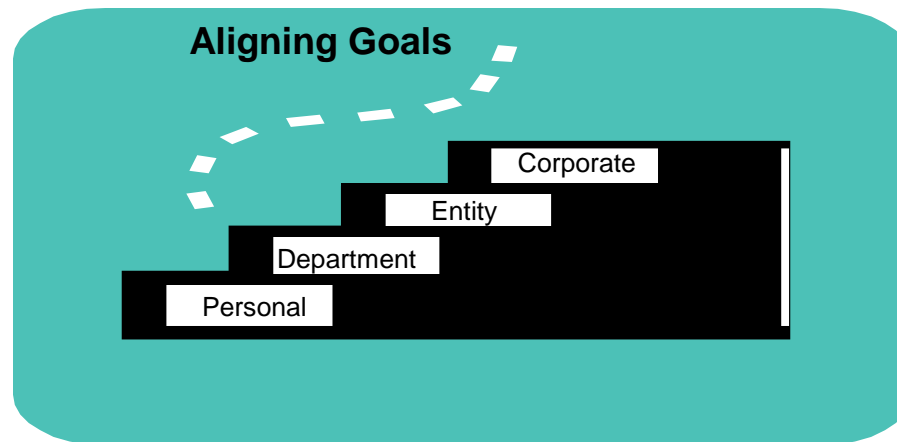
Lessons Learned

- Risk Manager – Choose your risk manager carefully. We appointed a capable person, but that person had other compliance duties in a critical compliance area.
- The ERM concept became ingrained in everyday activities, as well as our strategic planning process. As a result, we've learned that the program is not as time consuming as we initially thought. It supported our attempt to change our culture from reactive to proactive without adding additional meetings to everyone's plate.
- The ERM brought the need for diversification to a whole new group of individuals – it wasn't just executive management's problem. The ERM process enabled us to address health care reform proactively rather than starting from behind. Addressing change proactively rather than reactively.

Outcomes of Enterprise Risk Management Program (ERMP)

- Consistent approach to aligning strategy, processes, and knowledge to minimize surprises and losses while capitalizing on business opportunities.

- Aligning goals:
 - Corporate
 - Entity
 - Department
 - Personal



- As a result of ERMP, Essence will be better enabled to respond in a manner that reduces the likelihood of negative outcomes and increases the ability to seize additional opportunities, thus reducing volatility and helping Essence to reach its strategic objectives.