



CRM managers stalled payment of claims, ex-employee says

Craig Wolf • Poughkeepsie Journal • November 14, 2010

Compensation Risk Managers LLC was a troubled workers' compensation insurance company that left a trail of angry clients unexpectedly facing hefty payments.

Now, the company, known as Majestic Capital Ltd., has announced a proposed settlement of a lawsuit by the state Workers' Compensation Board and an investigation by the Attorney General's Office that it values at \$41 million. It's also pursuing a deal to sell the company and has included a "going concern" warning in its latest federal quarterly filings, a sign of growing financial troubles.

Some insight into how the company got to this point is offered by a former employee, Joseph Dorfman, who said CRM was chronically slow to pay claims coming in for several self-insured trusts that it managed because of what he said was a lack of money.

This was frustrating for some company claims adjusters, who wanted to help clients, he said.

Frequent discussions took place in which he urged managers to make money for payments available, but they often delayed paying, he said.

Dorfman, who lives in Dutchess County, worked for the company, a unit of CRM Holdings Ltd. and commonly called CRM, in its Poughkeepsie offices as a claims manager in the special investigation unit from March 2007 to September 2008, when 39 employees were laid off, he said. It was one of several downsizings as the company's original business plan, running self-insurance trusts, began coming apart.

He was there, he said in exclusive interviews with the Poughkeepsie Journal, when money got scarce in several workers' compensation self-insurance trusts that CRM ran, and complaints mounted from injured workers and doctors that they hadn't been paid.

In many cases, Dorfman said, "We couldn't release

checks to the injured worker because there wasn't enough money to release the check."

The Poughkeepsie Journal called several people who had handled claims at CRM, but none would comment. One explained that some departing employees were asked to sign agreements not to talk. Dorfman said he got what he called a "small severance" payment, but did not recall signing anything saying he could not talk. He is still looking for work.

CRM has denied accusations in lawsuits by the state Workers' Compensation Board and private parties that its management of trusts was poor. Majestic said in a statement Nov. 3 that it has a memorandum of understanding that outlines a proposed settlement of state charges against it.

Beyond confirming Dorfman's dates of employment at CRM, a company spokesman, Matthew Sheldon, said the company would have no further comment.

Dorfman cites his experience of nearly two decades in the workers' compensation field, including being a senior examiner and supervisor for AIG and working as a health and safety supervisor for United Parcel Service.

"I saw these egregious things because I've had experience in the industry," he said. "I knew that wasn't the proper way to run a claims department."

A claims manager reviews work done by staff to check out claims for payment, gathers facts, sees whether claims are valid and accurate and then

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approves or denies payments.

Dorfman would exhaust his authority and take matters up to his manager several times a day, he said.

There were layers of executives with rising levels of authority. If financial reserves on a case needed to be increased, it could go up to Chief Operating Officer Chester Walczyk, who could authorize up to \$250,000, he said.

CRM in May dropped its corporate name of CRM Holdings Ltd. and adopted Majestic Capital Ltd. On Sept. 21, Majestic said it had a deal to be acquired by Bayside Capital Partners LLC for about \$7.8 million. That company is now known as Bayside Equity Partners LLC.

The CRM company was born in Poughkeepsie in 1998, started by Daniel Hickey Jr. and Martin Rakoff, and looked like a darling startup with what appeared to be a solution to the high cost of workers' compensation insurance. It became a publicly traded company in December 2005, incorporated in Bermuda for what Hickey said then were tax reasons.

But it hit troubled waters. Its staff in Poughkeepsie, once more than 100 people, shrank to a shadow of that, though a company spokesman didn't respond to a request for current employment levels. It went from making millions in profit to posting repeated net losses, including \$7.9 million in the quarter that ended March 31, \$4.1 million in the quarter that ended June 30 and \$12.4 million in the most recent quarter. Those figures include both continuing and discontinued operations.

In May, it slipped to the edge of Nasdaq delisting because its share price fell too low too long, prompting a transfer to a different Nasdaq market with a Nov. 8, 2010, deadline to regain a share bid price above \$1 or face further steps toward delisting. Majestic last week implemented a reverse stock split, combining 10 shares into one. A reverse split pushes the price of a share up but does not raise the overall market value of the company. The Bayside purchase deal uses a share price of 45 cents, pre-split.

As of Friday, the post-split stock price was \$4.30 per share, unchanged for the day.

CRM has found itself on the receiving end of eight lawsuits relating to New York self-insured trusts,

plus a securities lawsuit, and has come under the formal scrutiny of three state agencies: the Workers' Compensation Board, the Insurance Department and the Attorney General's Office.

The Insurance Department's inquiry sought information from CRM and received it, department spokesman Ron Klug said.

"That issue is still being looked at, so we really wouldn't be able to go into any more detail," he said. California insurance regulators are also involved, he said.

CRM told the federal Securities and Exchange Commission that it has fully cooperated with all investigations.

The lawsuit by the Workers' Compensation Board alleges fraud, unjust enrichment, breach of fiduciary duty, breach of contract, breach of duty of good faith and fair dealing and deceptive business practices.

The company has rebutted each lawsuit as it was disclosed and continues to defend itself in court. But Sheldon said it is not the practice of CRM or Majestic to comment on pending litigation.

The attorney general's investigation, as disclosed by CRM, involved allegations that the company and some officers had "engaged in fraudulent practices in connection with Compensation Risk Managers LLC's administration and marketing of workers' compensation group self-insurance trusts in New York and in connection with the company's initial public offering completed in December 2005."

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Sheldon quoted from a May 10 CRM filing with the SEC: "The company has cooperated fully with the New York attorney general's investigation. To our knowledge, the New York attorney general has not commenced a lawsuit against the company, its subsidiaries or any of the company's current or former directors or officers."

The attorney general serves as the state's lawyer and is thus counsel to the Workers' Compensation Board, a spokesman for the attorney general said. He had no comment on the proposed settlement.

CRM 'hurt a lot of people'

Dorfman said he decided to talk publicly about his views from an insider's seat after he said more and more people were hurt by the actions of his former company.

"They hurt a lot of people. They hurt their employees," he said. Those who worked for CRM, he said, find that "people look down on you, even if you had no control over it."

Small and midsized businesses got hurt, he said.

The current CEO and deputy chairman is James J. Scardino, who has been with the company since 2005 and CEO since May 2009, taking over first as interim head after the resignation of Hickey. The proxy statement said that in 2009 Scardino was paid \$582,388, including stock awards.

Rakoff left in 2006; Hickey in 2009. Each collected severance payments of \$3.4 million. Both also got millions from stock sales after the company made its initial public offering of stock in 2005.

The lawsuit filed by the Workers' Compensation Board in December asserts the company routinely discounted too far the insurance premium rates it set for the eight self-insurance trusts that it managed on behalf of thousands of employers who used CRM to arrange workers' compensation insurance, the kind that pays workers injured on the job. The board was seeking \$472 million in damages to cover bills for the former CRM trusts it had taken over.

The board claims CRM charged "inadequate member contribution rates" and that it recruited as members employers "with known poor loss histories and failed to maintain adequate reserves to cover such losses." The suit claims CRM "failed to promptly investigate claims," that CRM "engaged in dilatory

tactics," that it "failed to pay awards and installments of compensation to injured workers in a timely fashion" and that it "delayed claims proceedings and settlements."

Dorfman said injured workers and their medical providers repeatedly pounded CRM's phones saying they weren't getting paid in a timely way.

"A large part of my day was calling the providers back," he said. Sometimes, a worker on compensation would call, too, he said.

His staff often would bring cases to him that had exhausted their financial reserves, Dorfman said.

That, he said, was because CRM's management often had not put up enough money to cover claims and send checks. Their approach, he said, was "not putting enough reserves on a file when you know what the file is worth," and thus falling short of the ultimate full costs of the case.

A reserve is an allocation of money earmarked to a particular file, or case. The sum is usually estimated based on industry or government standards by actuaries, who analyze data on what injuries usually cost in medical aid.

"An injury's a claim, whether CRM is administering the claim or AIG or The Hartford," or other insurance companies, he said, and the sums should be similar.

But reserves frequently were short of what was needed to pay expenses, Dorfman said.

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"The check would be in the system on hold because there wasn't enough money in reserves to cover the check," he said, describing a typical problem he faced. Other claims managers were in similar spots on a regular basis, he said. "Everybody had sheets of checks on hold."

Dorfman said he and others in the firm fervently argued for lifting limits on claims so that injured workers and their medical providers could be paid, but that they faced frequent delays from upper executives.

If enough money was reserved for a claim, they'd approve it. But if not, "They would just say, 'I have to get back to you on it,' " and then they'd push it up the chain of command and ask that a new report be prepared on the case, he said.

"They didn't approve the reserves for the last report, and would come back and ask for another report," he said.

The eight trusts are closed now, pushed to that end by the Workers' Compensation Board.

The board in 2008 had cracked down on CRM in an administrative proceeding that ultimately resulted in CRM surrendering its license to run self-insurance trusts in the state.

In its charges, the board claimed "repeated failure to pay awards and installments of compensation to injured workers in a timely fashion; repeated failure to file the proper forms with the board; engaging in improper delay tactics; routine failure to set adequate reserves in connection with claims ... and submitting false information to the board and to its clients." In the settlement, the company made no admission of guilt but agreed to exit the business that led to its founding.

Employers face bills

The board has taken over the work that the trusts were doing as well as their remaining financial assets. But those assets fall short of estimated liabilities, so the state has billed all the trust-member employers for what it calculates to be the shares of the debt for which they are liable under the law.

That has stunned employers like Rick Harris, owner of R.C. Harris, a plumbing and heating contractor based in Pleasant Valley.

Harris got his first bill last year from the state, saying his share of the shortfall in the CRM-managed Elite Contractors Trust he had joined was \$82,675.

Then, the Workers' Compensation Board got the results of a forensic audit on the trust and computed a new bill. This second bill, in May, boosted his debt to \$115,633.

"And it says here there's no end to it," Harris said.

He's been offered installment payment terms, but even those are tough to meet in this economy. Harris said his lawyer has advised him not to pay.

"My company's been in business for 27 years and we're struggling like the next guy," he said. "This is going to put a lot of people out of business. It's going to put a lot of people on unemployment.

"I had 40 men," Harris said. He's now down to 10. "Now you'll find me out in a ditch. I'm up all night estimating jobs."

About 2,000 employers statewide, including at least 170 in Dutchess, Ulster, Orange and Putnam counties, had insurance as part of this trust. It was one of eight that CRM managed in return for fees. In 2007 and 2008, the seven others were terminated by the Workers' Compensation Board.

Auditing of Elite Contractors Trust revealed more liabilities and, in 2009, the board said the Elite fund had a deficit of \$62.2 million, 15 times higher than CRM had estimated before surrendering its license

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to run such trusts, the Poughkeepsie Journal reported last year — hence the assessment bills to Harris and the others. CRM maintains its innocence and has denied allegations of mismanagement.

The Healthcare Industry Trust of New York, or HITNY, a CRM-managed self-insurance trust, was closed by the Workers' Compensation Board and a fund was set up and an administrator named to handle its affairs.

Health Quest Systems, based in Poughkeepsie, pays into that fund, said David Ping, vice president of strategic planning and business development for Health Quest.

He said, "It's not an insignificant amount," but did not provide specific numbers. Health Quest owns three hospitals and other operations and has about 5,000 employees overall.

Self-insurance approach founders

The future of the self-insured workers' compensation trust field is in question. A commission set up by Gov. David Paterson reported that it thinks the practice should be ended and existing trusts wound down.

Adam Friedlander, president and founder of The Friedlander Group in Westchester County, a specialist in workers' compensation, competes with self-insurance trusts run by various managers as well as with standard insurance companies. He offers "safety groups" insured by the State Insurance Fund, an alternative method.

Friedlander began writing articles in 1998 cautioning against self-insurance trusts as risky.

"At the time they were considered underfunded," he said. "There were lots of them. It was a problem. A lot of brokers didn't understand that these trusts were underfunded and what that meant."

It meant that one day, the liabilities would catch up with the shortage of money, and the employers who were members would find out what "joint and several liability" for trust members could bring — surprise bills — he explained.

Speaking of self-insured trusts in general, and not of specific companies, Friedlander said the model suffered from lack of a true competitive advantage.

"The only way they could compete was to have very

competitive pricing up front," he said. "But it turned out to be too competitive.

"If there is not a better mousetrap," Friedlander said, "then over time, what would be responsible for and justify the lower pricing? The answer is nothing. They didn't have a better mousetrap."

Reach Craig Wolf at cwolf@poughkeepsiejournal.com or .



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