PROPERTY & CASUALTY SELF-INSURANCE POOLING AND THE MISSOURI UNITED SCHOOL INSURANCE COUNCIL

WHAT IS A SELF-INSURANCE POOL?

A self-insurance pooling arrangement is a group of organizations, normally homogeneous in nature, banding together to create an association for the purpose of providing risk coverage and related services to its members. The members pay assessments into the association for the purpose of:

1) Funding a loss account for paying member claims as they occur
2) Procuring excess insurance or reinsurance to protect the pool from large losses
3) Hiring a staff – full-time or part-time, one person or multiple individuals
4) Engaging a brokerage firm and/or pool administrator depending on internal staffing levels
5) Contracting with a third party claims administrator to manage member claims
6) Engaging other vendors such as an actuary and auditor
7) Paying insurance-related taxes to help fund State agencies

While pooling is legal only in a handful of states for organizations outside the public sector, the vast majority of states allow these associations for their political subdivisions. Much of the enabling legislation was passed in the early-1980s and pools began forming shortly thereafter, especially in the wake of a very hard insurance market which hit in 1985.

WHAT ARE THE BENEFITS?

The member benefits of a pooling arrangement over the purchase of traditional insurance include:

- **Non-Profit Model** –
  Approximately 2/3 of a pool's revenue goes into a loss fund to pay claims. This means the majority of the funds come in as a dollar and go out as a dollar without the need to have a for-profit business involved, adding profit and overhead to the cost. And being non-profit keeps the mission of the organization focused solely only on serving the members.
- **Group of Peers** –
  Most pools are comprised of peer organizations so there is both an understanding of each other's operations and a trust through prior working relationships. It is also easier to sell the pool's risk to the reinsurance market as there are few unknown exposures.

- **Member-Controlled** –
  The majority of pools will elect a Board of Directors from the membership, although some smaller pools are governed by all members through a Committee structure. The Board will set policy, hire staff, contract with service providers, set self-insured retention levels, and preside over any claim disputes.
- **Tailored, Comprehensive Coverage** –
  A pool can tailor the coverage provided to its members through a unique Plan Document. There will be some restrictions imposed from the reinsurance markets, but pools tend to build in extra bells and whistles not available from standard insurers since their only objective is to provide broad, shared coverage.

- **Insurance Market Clout** –
  When the group goes out to the insurance or reinsurance marketplace looking for excess coverage, it goes out with a very large group and it gets the attention of carriers. A pool will be able to procure better terms than an individual because it not only demands more attention due to its size, but because it can afford to retain a large portion of the risk.

- **Retention of Investment Income** –
  While a standard insurer invests your premium dollars and adds that income to profit, in a pool you will invest the money accumulated in the loss fund and surplus account and retain that income to offset member assessments. Insurance operations will accumulate a great deal of cash over time because of the tail on claim payments. A mature pool may have investable assets of one to two times the total annual assessment.

- **Savings Stay in the Program or Distributed Back to Members** –
  A well-managed pool will accumulate a surplus over time which may be retained in the program to lower future rates or increase self-insured retentions, or may be distributed back to the membership in the form of a dividend. This decision is up to the Board and/or membership with some oversight from state regulators.

- **Pricing Insulated to a Great Degree from Market Cycles** –
  We all know insurance premiums in the standard market can swing up and down a great deal. However, because a pool only uses approximately 25% of its revenues to buy excess insurance, the market swings have much less impact on the overall cost of the program.

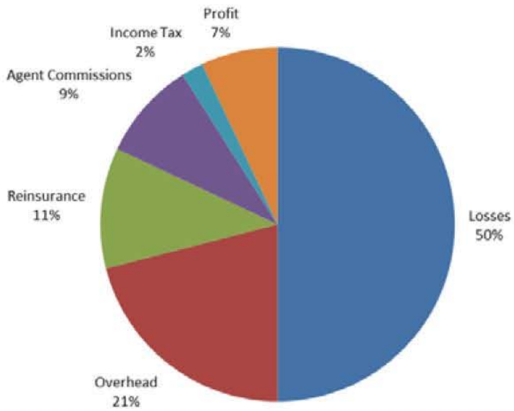
- **Emphasis on Loss Control Brings Lower Loss Costs** –
  Because money not spent on losses is money retained in the pool, loss control and claims cost containment become vital parts of the process. Pools normally will invest in safety staff or in an outside consultant to lead the effort.

- **Local Effort Turns from Procuring Insurance to Risk Management** –
  Pool members comment frequently about the ease of administering the program locally. A member normally does not continue using the competitive bid process once they join a pool. The Association's Board and staff will use competition in the procurement of the excess insurance, and because each member is an "owner" of the pool, most local public entity boards will feel comfortable that the program's administration, with the pool Board's oversight, will be looking out for their best interests.

How Much Money Can Be Saved?

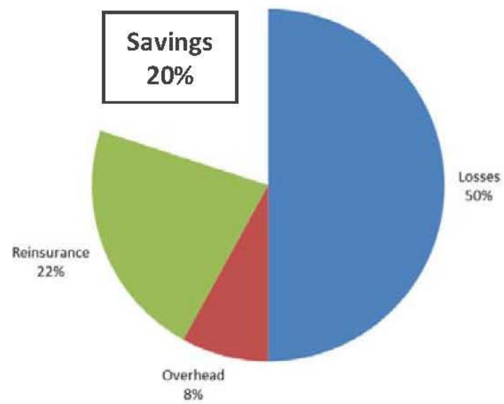
A standard insurance company's revenue is allocated according to the left chart on the next page. In contrast, membership in a self-insurance pooling program brings significant monetary benefits due to the exclusion of profit, income tax, agent's commissions, and greatly reduced overhead costs. The chart on the right represents the breakdown of revenue for MUSIC.

Standard Insurance Company Revenue Breakdown



Source: Insurance Services Office (ISO)

Group All-Lines Self-Insurance Revenue Breakdown



Source: Missouri United School Insurance Council

WHAT OTHER SERVICES CAN BE DELIVERED?

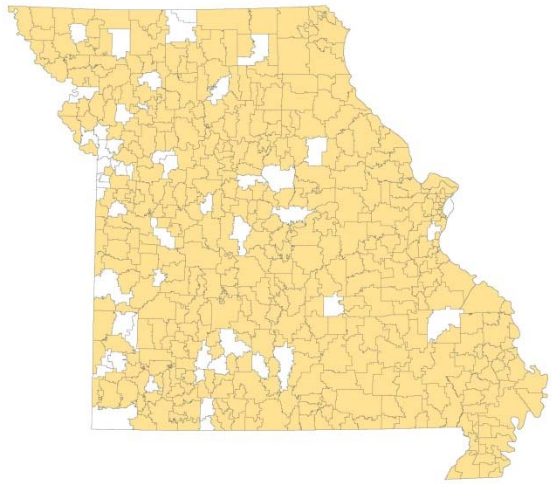
Pooling programs will normally develop a catalog of unique services over time to better serve its membership and work toward the reduction of claim costs. These are some common additions:

- **Loss Control** –
  The consultant would develop a Safety Manual for the pool and also assist individual members with programs such as physical inspections, safety committees, safety training, accident investigations, claims trend analysis, and vehicle safety.
- **Onsite and Online Training** –
  There are a myriad of resources available for training staff in the safety area as well as sexual harassment, bullying, cyber-bullying, and child sexual abuse prevention.
- **Workshops** –
  Many pools will conduct regional training on issues such as hot legal topics or workers' compensation cost containment.
- **Building Appraisals** –
  Offering a building appraisal service along with membership is a common practice.
- **Board Policy Service** –
  Some pools have developed their own board policy service and offer it at no charge to the member. Even if a member uses another service, they can still refer to the pool's templates for ideas.
- **Legal and Legislative Support** –
  When macro issues arise that demand intense legal work or legislative action, a pooling program can be a great vehicle to fund and staff those efforts.

HOW COMMON ARE PUBLIC ENTITY SELF-INSURANCE POOLS?

There are hundreds of public entity pooling programs in the country and several public school pools in surrounding states.

What Is MUSIC?



The Missouri United School Insurance Council (MUSIC) is a 30-year-old pooling program comprised of 90% of Missouri's public school districts and 67% of the community colleges. It is a mature program with a variety of value-added services, well-established reinsurer relationships, and a very healthy financial surplus.

MUSIC has assisted with several other state efforts by sharing some of its infrastructure such as its organizational documents, manuals and analytical tools, as well as using its relationships with reinsurers and other service providers to help a new pool get started.

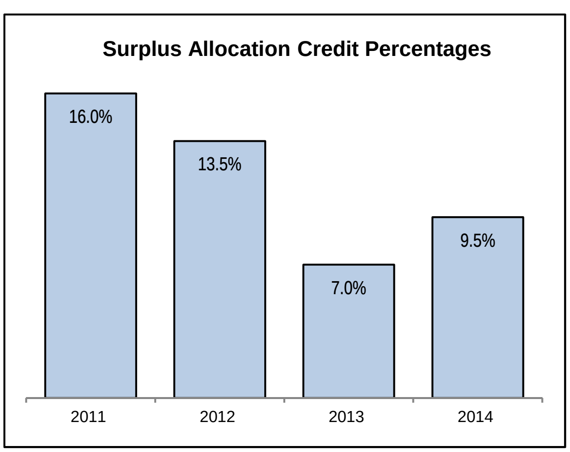
What Protections Are In Place?

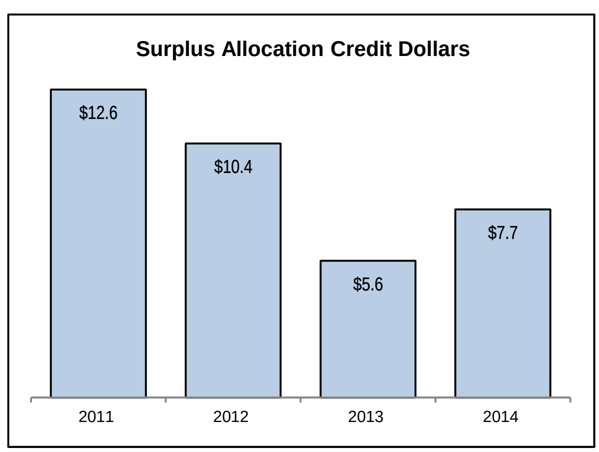
What safeguards are used to give members an assurance that a pooling program is safe?

1) **Excess or Reinsurance** –
   Insurance is purchased by the program above set self-insured retentions so large individual losses cannot deplete the fund.
2) **Regulation** –
   The Missouri Department of Insurance regulates pooling programs. They oversee financial solvency and business practices.
3) **Board Insurance** –
   The Board of Directors purchases fidelity coverage and errors and omissions insurance.

Is There A Potential Downside?

Pools, by their nature, are assessable if the money set aside to pay losses is ever determined not to be adequate. However, a well-managed program should never be in a position to require additional funds. For MUSIC, the member surplus is very strong and operates better than a 3:1 ratio of member assessments to member surplus. MUSIC has also now returned $36.3 million of surplus to the members from 2011 through 2014.



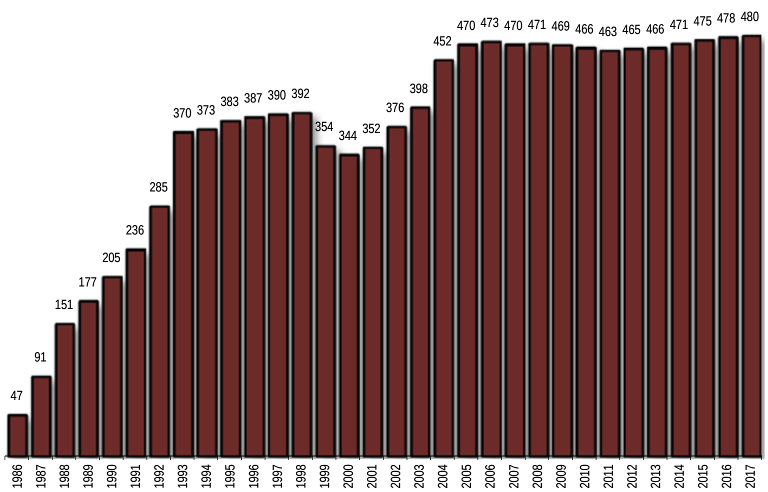


The Insurance Marketplace and Self-Insurance Pooling

The pricing of property and casualty insurance from the standard marketplace rises and falls in reasonably predictable patterns, although the precise timing and magnitude of the swings is not an exact science. However, there still are plenty of indicators to let us know when we may be due for a change. Today, we are in a very soft insurance market which began in 2014, but the recent hurricane activity so far in 2017 may be putting upward pressure on the market, and most experts are expecting rising premiums over the next year.

The cyclical nature of the industry will impact overall interest in a pooling program. Pool members experience pricing that does not change much as the market swings. In contrast, the standard market will move up and down more significantly and it is possible an individual pool member could purchase coverage at a slightly lower rate when the cycle is at its lowest. But as prices rise, pooling becomes much less expensive and will always be less in the long term. During the peak of a hard market, standard market pricing can be as much as double that available through a pool.

MUSIC Membership History



MUSIC has experienced this first hand as membership levels have been impacted by the market's ebbs and flows. The pool's first year was 1986, a year of rapidly increasing standard market premiums, and membership grew steadily until a soft market lingered through the latter half of the 1990's. Then, as the market hardened again in 2000 and 2001, membership began climbing until the next soft market beginning in 2004. The market became tougher again in 2011 through 2013 and MUSIC membership starting growing again as a result.

Conclusion

There are many wonderful rewards to being involved in a program such as MUSIC, not the least of which is the satisfaction of being part of something that has put millions of dollars back in the classrooms of Missouri. We estimate the total savings to Missouri schools over the last 32 years has been at least $300 million.