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Risk Management Manual for the Public Transit Industry

Volume 2

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UMTA Technical Assistance Program

Risk Management Manual for the Public Transit Industry

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Prepared by
MacDorman and Associates
4808 North 29th Street
Arlington, Virginia 22207
in association with
Advanced Risk Management Techniques
Cambridge Systematics, Inc.
Public Risk and Insurance
Management Association
Peter Schauer Associates

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U.S. Department of Transportation
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LIST OF EXHIBITS

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IV. RISK FINANCING

The third step in the structured risk management program outlined in this manual is risk treatment analysis. Risk treatment involves the appropriate use of both risk control and risk financing tools. Chapter III explains how to control risk exposure. This chapter and the next describe ways of financing the losses that do occur regardless of efforts to prevent them.

Risk financing is the method an organization chooses to pay for accidental losses arising from the organization's operations. The two general risk financing options are:

- Self-funded retained risk - the retention of all or partial responsibility for loss payment by an entity or group of entities whose operations create the chance of loss.

- Commercial insurance - the transfer of financial responsibility for the loss to an unrelated entity (usually an insurance company) in exchange for money (i.e., a premium).

Three methods of risk retention are described in this chapter: self-insurance by an individual organization; pooling; and, the use of captive insurance companies. These mechanisms provide loss protection outside of the commercial insurance marketplace. Commercially purchased insurance is discussed in Chapter V.

FACTORS INFLUENCING THE RISK FINANCING DECISION

Deciding among risk financing alternatives is not a clearcut matter; it cannot be done quickly or without study. Ultimately, the best solution might be using a combination of both purchased insurance and self-funded retained risk. How does a risk manager choose what is best for his or her organization? The answer can be very different for two transit systems. Several factors must be taken into account when making financing decisions: the type of risk involved; internal financial and management capabilities; an organization's loss experience; and external considerations.

Risk Evaluation Results

The loss potential rating matrix described in Chapter II is a useful guide for planning a risk retention policy. The matrix, as presented in Exhibit IV.1, classifies risks by frequency--how many times a loss is expected to occur in a certain timeframe--and by severity--gauged by the dollar amount assigned to a loss. In analyzing severity, both the maximum probable and the maximum possible losses from an occurrence must be considered. Only after all risks have been identified, evaluated for severity and frequency, and classified can the most effective method(s) of treatment be determined.

EXHIBIT IV.1

LOSS POTENTIAL RATING MATRIX

Severity \ Frequency	Low	High
Low	Type A Low Severity Low Frequency	Type B Low Severity High Frequency
High	Type C High Severity Low Frequency	Type D High Severity High Frequency

- Quadrant A: Low-severity, low-frequency losses are included in quadrant A. Such things as minor theft, vandalism, routine injuries, and minor building damage fall into this category.

- Quadrant B: Low-severity, high frequency exposures are in quadrant B. These include bus and auto accidents, workers' compensation claims, and some general liability exposures.

- Quadrant C: Low-frequency, high severity exposures fall in quadrant C. These include boiler and machinery, property loss, large liability suits against the organization, data processing losses, permanent injuries, or major theft.

- Quadrant D: High-frequency, high severity losses are included in quadrant D. These types of losses are not common, but can involve property loss and some general liability exposures.

All areas but one, Type C: High Severity/Low Frequency, should be considered for self-funded retention, either in whole or in part. Because of the possibly catastrophic nature of Type C losses, some type of excess insurance is usually needed. Type A: Low Severity/Low Frequency risks can be retained because these are not significant losses; Type B: Low Severity/High Frequency risks can be retained because these are predictable losses; and Type D: High Severity/High Frequency risks require additional evaluation to determine the most economic treatment. The best treatment for this category of risks may be a combination of self-funded and excess insurance or pooled risk with reinsurance. These concepts are discussed in this Chapter and the next.

Risk Retention Capacity

Risk retention capacity reflects the ability of a transit system to absorb retained losses and still meet major financial and operating requirements. Funding needs equal expected losses and expenses.

Under a self-funded approach losses that occur with predictable frequency are assumed by the organization and paid as a normal operating expense or from a reserve fund. Even some portion of the less predictable losses can be retained as long as the amount retained does not threaten the solvency of the organization. Most self-insurers therefore provide for a cap, or stop-loss: a dollar amount above which purchased excess insurance covers claims. There is no standard method for determining how high this risk retention cap should be since each entity has unique characteristics including:

- the history of losses experienced by the organization
- the financial resources of the organization
- management's aversion to risk

A wide range of approaches to retention caps are suggested in risk management literature and practiced by the transit industry. One general rule often used by local governments is that it should be able to afford up to one-tenth of one percent of total annual revenues for losses stemming from a single occurrence, but that the total for all losses annually should not exceed one percent of total annual revenues.[1] At the other end of the spectrum, another industry source suggests that a per occurrence retention of 1% of operating budget, and a total annual loss (aggregate) retention of 10% of operating budget is not unreasonable. For example, a system with an operating budget of $25 million would retain $250,000 per loss with an

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[1]Phyllis Sherman, Basic Risk Management Handbook for Local Governments, Public Risk and Insurance Management Association (PRIMA), June 1983, p. 37.

annual aggregate retention of $2,500,000.[1] If a reserve fund for contingencies is available, it should be able to absorb unexpected losses and expenses up to a cap of 25% to 35% of the reserve fund.[2] Both a per occurrence and a total annual losses (aggregate) cap should be arrived at, and insurance commercial or otherwise, purchased to handle losses above these amounts. The percentages presented are examples only.

Each organization's situation must be reviewed. To determine the entity's risk retention capacity, the risk manager must consider:

- expected, probable, and maximum possible losses;
- financial and management resources;
- applicable laws and regulations; and
- premium saved in exchange for risk retained.

Loss History and Premium Rates

Current and projected insurance premiums and analysis of three to five years of loss data should help risk managers in deciding the most appropriate risk financing program. If the dollar amount of losses has been consistently below premium rates, self-insurance should be seriously considered.

Transferring risk of loss to an insurer is often more expensive than retaining or self-insuring risk. This is because the insurance premium not only includes an amount for expected losses, but also amounts for expenses of claim handling, safety, loss statements, taxes, underwriting, and overhead, plus an allowance for profit. The expense and profit increment is often equal to the loss increment resulting in the insurance buyer paying $2 of premium for each $1 or $1.50 of loss reimbursement.

Some of the premium cost categories (e.g., taxes and profit) do not directly benefit the policyholder and are avoidable under self-insurance programs. In addition, the self-insured organization holds a significant amount of dollars that would otherwise be paid to an insurance company in anticipation of future loss payments. Investment of these dollars in income-producing instruments represents a source of income that further decreases the cost of self-insurance.

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[1] Charles T. Bartholomae, A Manual on Risk Management for the Public Transit Industry, American Public Transit Association (APTA), September 1986, p. 40.

[2] Margaret W. Tiller, "Retaining Risk," Public Risk, January/February 1987, Vol. 1, No. 2, p. 11.

Administrative Responsibilities and Capabilities

Administering an in-house risk financing program requires loss prevention, claims management, and data processing services. If commercial insurance is purchased, the insurer assumes primary responsibility for most of these tasks. By purchasing commercial insurance an organization exchanges premium dollars for these services. To estimate what these costs are and to determine if these tasks could be performed less expensively by the transit system's staff or contractors, a simple rule of thumb is that approximately 30% to 35% of total premiums is used for administrative expenses. For example, if an insurance premium of $250,000 is paid, somewhere between $75,000 and $100,000 is used to cover this class of expenses.

If a self-funded approach is undertaken, the transit system should determine whether these administrative and management tasks should be handled in-house or contracted out. Increased administrative responsibility without the technical knowledge and expertise that an insurance company offers are commonly cited as disadvantages of self-insurance. However, independent vendors of these services can fill the gap left by a commercial insurer.

Regulatory Constraints

A transit system that wants to self-insure may be subject to state regulations requiring bonds or deposits, special taxes and assessments and other proof of financial responsibility. Motor vehicle liability and workers' compensation laws are likely to establish such special self-insurance requirements. Some states may require an application for permission to self-insure. Although municipal entities are frequently exempt from these requirements, state regulations should be investigated.

Partial Retention Options

There are a variety of methods in which risk can be partially assumed by a transit system if full self-funding is more of a risk than it feels it can safely absorb. Deductible and self-insured retention programs offer the insurance buyer the opportunity to retain some risk without losing protection for unexpected catastrophes. Deductible programs do not differ substantially from self-insured programs except that commonly:

- Under a deductible program, the insurer handles the claims, makes claim settlement decisions and bills the policyholder for the amount of the deductible.

- Under a self-insurance program, the self-insured organization assumes primary responsibility for claim handling and pays losses to the attachment point of the insurance beyond which the insurer is responsible for payment.

- Self-insured retention programs commonly allow for larger risk retention levels than do deductible programs.

Over a long period of time, deductible and self-insured retention programs produce savings of between 10% and 25% when compared to first dollar insurance coverage (i.e., no deductible or retention). These savings, however, are usually realized only by organizations whose premiums exceed $250,000 annually.

TRANSIT INDUSTRY RISK MANAGEMENT PRACTICES

As part of the preparation of this manual, a survey was developed to obtain information from transit systems on their current practices in the areas of risk financing, risk transfer, accident and claims management, and use of outside assistance. It was distributed nationally in June 1988 to over 350 transit systems of all sizes and modes. The survey instrument and tabulation of results are presented in Appendix F. A summary of responses describing operating characteristics and use of risk financing techniques is presented below. Additional references to this survey will be made in the chapters covering risk transfer (Chapter V), claims and crisis management (Chapter VI), and use of outside technical assistance (Chapter VII).

Service and Operating Characteristics

More than one-half (188) of the surveys were returned. About 24 percent of the respondents are city agencies, another 23 percent are local or regional joint powers authorities, 19 percent are special districts, almost 10 percent county agencies, another 5 percent are state-run systems, and almost 18 percent responded as other. Service areas of all sizes are well represented in the completed surveys, ranging in size from less than 50,000 residents to more than 2 million. Almost 43 percent the systems serve areas of between 50,000 and 249,999 residents.

Eighty (43 percent) of the respondents have fleets, including revenue and non-revenue vehicles, of less than 50. Another 38 (20 percent) have between 50 and 99 vehicles, 27 (14 percent) report between 100 and 249 vehicles, 17 (9 percent) between 250 and 499 vehicles, and 26 (14 percent) systems report a total fleet size in excess of 500 vehicles.

All modes of transit service are represented in the survey's findings: 93 percent (175 systems) operate buses; 7 percent rapid rail; 9 percent streetcar or light rail; 50 percent demand-responsive vehicles, and 20 percent other. Fixed-route service is operated by 98 percent of the respondents, and demand-responsive service by 60 percent. Almost all systems serve the general public (96 percent), and 86 percent provide service to elderly and handicapped riders.

Responses to the survey were also tabulated according to the size of the annual operating budget. There is a realistic distribution of different sized organizations in the survey's sample. The largest response (21 percent) comes from transit systems with budgets of between $2 and $5 million, followed by small agencies with budgets under $1 million (19 percent), and budgets of between $1 and $2 million (15 percent). Budget groups of $5 to $10 million, $10 to $25 million, and $25 to $100 million each have responses constituting 10 percent to 13 percent of the total survey's sample. Nine percent of responses are from the largest systems with budgets over $100 million.

Responsibility for Risk Management

There is little uniformity in the position held by the person responsible for risk management. The general manager is identified about 34 percent of the time, followed by a risk manager for 27 percent of respondents, and a finance director by 13 percent. Twenty percent replied that responsibility was held by some other position. Large organizations (500 or more vehicles) are most likely to have a full-time risk manager. Small transit systems (less than 50 vehicles) are most likely to place the risk management function under the control of the general manager. Middle-sized operations (100 to 500 vehicles) often place the responsibility with the finance director or risk manager.

Risk Financing Practices

Survey participants were asked how they receive coverage for three areas of risks: 1) vehicle liability, 2) directors' and officers' liability, and 3) workers' compensation. The results are summarized below. It is possible for one transit system to use more than one method of coverage per risk area. For example, a transit system can be self-insured for primary vehicle liability and use commercial insurance for excess coverage. Thus the cited percentages for use of different financing methods may not total 100 percent.

For vehicle liability coverage the purchase of conventional commercial insurance is the most widely used method of risk financing. Fifty-three percent of all respondents indicate its use. Self-insurance is the second most frequently cited method. Almost 47 percent of the survey's transit systems have self-insurance programs for vehicle liability. Of those reporting no self-insurance, the large majority rely on commercial insurance for primary coverage. Many systems with self-insurance also rely on commercial insurance, but for excess coverage. Other alternatives to commercial vehicle liability insurance include: participating in pools (19 systems); obtaining coverage through another agency (9 systems); participating in a state fund or other state assistance program (4 systems); using a captive insurer (1 system); and joint purchase from a commercial insurer (1 system).

Some differences are apparent in vehicle liability practices by the size of the transit system. Self-insurance is not widely used by small and medium sized systems; 73 percent of respondents with budgets below $10 million indicate no self-insurance for vehicle liability. Self-insurance is however commonly used by transit systems with budgets greater than $10 million--only 5 systems out of 62 of this size have no vehicle liability self-insurance. Pools attract small and medium sized systems. Of all those participating in pools, 68 percent are systems with budgets of less than $10 million.

For directors' and officers' liability coverage, the purchase of commercial insurance is again the most widely used method of loss protection. Over 40 percent report using insurance. Twenty-six percent, (49 systems) have self-insurance programs, and most of them do not use another arrangement for additional coverage. Of those which do have excess coverage, commercial insurance is the most common choice. Transit systems without self-insurance rely on commercial insurance 70 percent of the time. Alternative approaches include: obtaining coverage through another agency (11 systems); joining pools (12 systems); and participating in a state fund (5 systems). Differences in practices according to system size are not apparent.

Workers' compensation coverage is obtained through many sources. Almost forty percent of respondents indicate the use of some commercial insurance, primary or excess. Almost one-third (32 percent) rely on self-insurance, with or without additional coverage; 11 percent participate in a state fund; 6 percent obtain coverage through another agency; about 3 percent are in an assigned risk plan; and over 2 percent are in a pool.

Larger systems tend to self-insure for workers' compensation. In the survey, 82 percent of systems with budgets greater than $25 million had self-insurance. Small and medium sized systems with budgets less than $25 million do not typically self-insure workers' compensation. Of the 147 systems of this size, only 30 report self-insurance.

Self-insurance retention levels (SIRs) for all types of coverage vary by system size. There are two categories of SIR: per occurrence and aggregate. Both increase with the size of the transit system. For vehicle liability coverage, small to medium systems may have SIRs of $25,000 to $50,000 per occurrence and $250,000 to $500,000 aggregate. Systems with budgets of between $25 to $100 million may have SIRs in the range of $250,000 to $1 million. At very large systems, the ceiling of SIRs increases into the millions, with $3 to $5 million typical.[1]

Additional mention of the survey's findings will be made at appropriate places in this and following chapters.

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[1]The data provided by the transit systems did not specify whether their SIRs were per occurrence or aggregate limits.

SELF-INSURANCE

Program Scope

Certain types of risk lend themselves to self-insurance more readily than others as previously explained by the loss potential matrix (Exhibit IV.1). Workers' compensation and vehicle physical damage coverage are the most commonly self-insured. In workers' compensation it is likely that most of the losses will consist of relatively small payments at great frequency. Vehicle comprehensive and collision losses are generally predictable and are thus another good area for self-insurance.

Liability coverages are not as easily self-insured. Severe losses are more difficult to predict. Although workers' compensation and auto physical damage are limited in amount by statute and vehicle worth, very few states have limitations for tort liability damage awards.

Any risk retention program is subject to adverse claims experience. This includes both catastrophic claims or an unexpectedly large number of smaller claims. For this reason most self-insured organizations purchase excess insurance. The two most common types of excess insurance are per occurrence, which pays for losses above a specified amount up to the policy limit for each occurrence; and aggregate, which pays for losses above a specified amount up to the policy limit for the total of all occurrences during a set time period.[1]

Funding Methods

Self-insured losses are paid from one or a combination of two sources: the current budget and a contingency reserve. Organizations typically earmark an amount in the annual operating budget for losses that occur during that year. A portion of the liabilities that occur during a budget year remain unpaid at the close of the year. There is usually a four to five year tail on paying out all the claims incurred in a single year.

A self-insurance program needs to allow for this tail by establishing a reserve for the unpaid portion of liabilities on losses that occurred during periods of self-insurance. When these liabilities are discharged, through loss payment or other means, the reserve is reduced. Not all self-insured entities account for losses in this manner, but a growing number use this approach. Under this method, the ultimate liability for all events in the budget year is charged against that budget year, not deferred to the year of actual loss payment.

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[1]Margaret W. Tiller, "Retaining Risk," Public Risk, January/February 1987, Vol. 1, p. 12.

A second type of reserve, a contingency reserve, is established by many self-insured entities. This is used to pay losses that exceed the amount expected. Actuarial studies are often used to determine the amount for the incurred-but-unpaid loss reserve as well as the contingency reserve.

Reserve funds can be invested in low-risk financial instruments such as treasury bonds to earn interest until claims are paid. When using a commercial insurer, the insurance company keeps the interest. With self-insurance the transit system keeps the interest income. Although these earnings can be applied to reduce the annual reserve contributions, many entities use these earnings to build an additional risk margin in their self-insurance program reserves.

Program Management

Program administration involves arranging for loss prevention, claims administration, and data processing services. The transit system should determine whether these functions will be handled in-house or contracted out. Some self-insured entities purchase claims administration services from a firm specializing in this area, and data processing from a second company with this expertise. Other times claims administration and data processing services are procured from the same source. Some, but not many transit systems, also contract for loss prevention services.

With self-insurance, transit systems have more control over how claims are managed; important decisions regarding claims settlement are no longer the exclusive domain of the insurance company adjuster. Other factors to consider in deciding to contract for claims administration are the volume of claims, data processing resources, and the cost and requirements of any excess insurers. (Chapter VI discusses claims management and the use of contracted services.)

POOLING

Program Scope

Pooling is an agreement among a group of entities, such as transit systems, to jointly fund each others' losses. Members make contributions to the pool, which in turn pays losses. A pool typically handles the administrative functions that an insurance company provides including claims management, record keeping and loss control. Pooling is most common with public entities, although the passage of the Risk Retention Act of 1986, and the laws of a few states facilitated private sector pool formation.

A movement toward pooling in the late 1970s accelerated again in the mid-1980s. Municipalities used pools to respond to the hard insurance market that forced some public entities to do without insurance entirely, accept larger than desired deductibles and SIRs, or cutback on limits of protection.

Workers' compensation was the first type of risk to be pooled. The recent insurance coverage crisis prompted widespread use of liability pools. Now pools cover workers' compensation, liability, property and even employee benefit coverages. The additional coverages help to create a desirable funding mechanism for the participating entities and a larger, more stable pool.[1]

Pooling, while viewed by some as an extension of self-insurance is, to the user, more like insurance than self-insurance. A transit system contributes to a trust fund and in turn receives coverage. Trust monies are used to pay losses above the pool member's deductible up to the pool's maximum retention. Excess insurance is often purchased and applies to the losses that exceed the pool's maximum retention. Safety, claims handling, legal, actuarial and other services are purchased for the pool.[2]

Public agency pools are operating in most states, and are being planned or studied in the others. Over 200 pools are currently operating with combined contributions in excess of $500 million. Participants include cities, counties, school districts, utility districts, water districts, special districts, and transit systems.

In our nationwide survey of transit systems, pooling was identified as a risk financing method, but its use is not widespread. Nineteen transit systems that responded to the survey use pools for vehicle liability coverage, twelve for directors' and officers' liability coverage, and four for workers' compensation. Pools specifically for transit exist in several stages of formation: some are fully operating, others are in the process of being organized. Exhibit IV.2 identifies transit risk management pools in various stages of operation or formation. Information about these pools (e.g., types of coverage, membership and financing techniques) and contacts are included in the exhibit.

To begin a pool many factors must be considered. Contributions should approach $1 million or more. Pool size should be at least 10 participants, which may vary depending on their size. These indicators of threshold feasibility are not, however, hard and fast rules.

The development of a successful self-insurance pool requires a sound business plan and firm commitment. Both the number and growth of intergovernmental self-insurance pools shows that they are more than a passing fad. Despite the cyclical nature of the insurance market, most pools have successfully increased

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[1] Practical Risk Management: The Professional's Handbook, P.O. Box 10093, Oakland, CA 94610, 1987. Topic B-13.

[2] Much of the discussion about pooling on the following pages is extracted from "Pooling - An Introduction for Public Agencies," published by PRIMA, 1987.

EXHIBIT IV.2

TRANSIT RISK MANAGEMENT POOLS AND INSURANCE BUYING GROUPS

GROUP NAME	CONTACT	INITIATION DATE	TYPE OF PROGRAM	COVERAGE OFFERED	FUNDING TECHNIQUE	MEMBERSHIP	MEMBERSHIP DURATION REQUIREMENTS	NOTES
Alabama Transit Risk Purchasing Group	Mr. Lee Alexander Suite 504 2101 Magnolia Avenue Alabama Transit Assn. Birmingham AL 35205-2827 (205) 324-9166	December 1, 1988	Group Insurance Buying Pool	Auto Liability	Premiums and Membership Fees	No current members Membership will be offered to urban and rural and specialized services. Considering offering to private operators.	Three years	Have not started offering any coverage yet.
California Transit Insurance Pool (CalTip)	Mr. Edward Gerber General Manager California Transportation Association 1400 K Street, Suite 301 Sacramento, CA 95814 (916) 446-4656	May 1, 1987	Self-Insurance Pool	Auto Liability; General Liablity; Physical Damage; Collision & Comprehensive	Member Contributions based on mileage and location	14 members (4 buses to 102 buses) Must be government entity.	Three years	Favorable first year
Indiana Transit Vehicle Insurance Study Commission	Mr. Martin Sennet Greater Lafayette Public Transportation Corp. P. O. Box 588 Lafayette, IN 47902 (317) 423-2666	Defunct	Self-Insurance Pool	Auto Liability	Member Contributions based on annual mileage	No members - Intended rural and urban excluding Indianapolis Transit Authority and South Shore Railroad.	Three years	Insurance became more affordable for potential members and effort was abandoned.
Michigan Transit Insurance Pool (MTIP)	Mr. Rick Kaufman Bay Area Transportation Authority 507 Wellington Traverse City, MI 49684 (616) 941-2324	December 1, 1987	Self-Insurance Pool	Auto Liability General Liability	Member Contributions based on mileage and ridership and location	19 members (5 buses to 150 buses) 6 urban 13 non-urban	Three years	Favorable experience as of August 10, 1988.
Mississippi Transit Risk Purchasing Group	Mr. L. T. Livingston Mississippi State Highway Department P. O. Box 1850 Jackson, MS 39215-1850 (601) 354-7172	Information has not begun	Group Insurance Buying Pool	Auto Liability	Premiums	No current members - Will be offered to urban, rural and specialized services.	Not established	Project is in initiation phase. No official name or detailed plans. Experiencing a problem in finding a sponsoring agency.
Paratransit Insurance Corporation (PIC)	Ms. Katherine Adcock PIC 4410 Power Inn Road Sacramento, CA 95826 (916) 545-4191	July 1, 1988	Self-Insurance Pool	Auto Liability	Member contributions based on vehicle characteristics	76 agencies (1 vehicle to 65 vehicles) Must be IRS 501(c)(3) Corporation; Must be social service transit	Three years	Coverage offered only for people to people, people to food or food to people.
South West Transit Mutual Insurance Company	David Snead or A. E. Johnson Arkansas Transit Assn. 1209 W. Third Little Rock, AR 72201 (501) 225-7100	March 1988	Risk Retention	Auto Liability	Premiums based on vehicle size, use and location	No members at this time.	Annual	Program not fully implemented because actuarial study indicated project not feasible.
Transit Mutual Insurance Corporation of Wisconsin (TMICW)	Ms. Nancy Kreutzman President Valley Transit Appleton, WI 54914 (414) 735-6101	January 1, 1986	Assessible Mutual Insurer	Auto Liability Uninsured Motorist	Member contributions based on mileage and loss record	16 members (3 vehicles to 200 vehicles) Open to any municipal transit.	Three years	Favorable experience to date; Group also pool-buys physical damage and excess reinsurance for members desiring higher liability limits.
Washington Transit Pool	Jeff Risten Administrator Community Transit Everett, WA	Proposed January 1, 1989	Self-insurance Pool	General Liability; Auto Liability; Errors and Omissions	Premium and Capital Contributions	11 members (15 to 550 vehicles)	Three years with a one year required notice.	Program not operational.

membership while retaining those who joined initially. Listed and discussed in Exhibit IV.3 are the factors thought to be most important to pool success.

Pool Formation

A self-insurance pool requires planning. It begins with the development of a business plan that will carry the group from a feasibility study to successful implementation. A business plan should address the following items.

Timetable

The timetable is a listing of all the tasks necessary for the implementation of a pool and the sequence in which they should be performed. The basic elements of such a timetable are shown in Exhibit IV.4. The time required by different organizations to accomplish these steps will vary; in some cases it may take two years, in others three months may be sufficient. Six months to one year is considered a customary period.

Membership

In most cases, membership is restricted to a single type of public entity. The decision is based on the fact that different forms of public agencies experience different types and degrees of risk in their daily operations. The delivery of safety programs and development of legal defense practices tend to be easier with homogeneous groups.

Pools are commonly established through the leadership of a statewide association. The advantages of this approach include using an established communication network for soliciting ideas and identifying interested organizations and capable project leaders from the association membership. Another approach is the establishment of a core group of interested participants who affiliate to organize the pool and recruiting others to join.

Legal and Regulatory Research

Initial legal work should be conducted to identify any limitations in state statutes dealing with the legal authority to organize a self-insurance pool. Specific enabling legislation and any other legal requirements that affect the pool's structure should be examined. In many states, intergovernmental cooperation acts or joint powers agreements serve as the basis for pool organization. In other states, establishing some form of nonprofit trust or corporation may be more suitable. Legal counsel can provide information about the advantages and disadvantages of each allowed structure.

The tax status of a self-insured pool should also be determined. Creating a self-insurance pool free from federal and state tax liability represents a significant savings for pools.

EXHIBIT IV.3

TEN KEY FACTORS FOR POOL SUCCESS

1. Sense of urgency -- Is there a sense that something must be done at this time?

   * Are agencies philosophically committed to finding alternatives to commercial insurance?
   * Are agencies continually being offered inadequate limits?
   * Are coverages which are offered extremely restricted?
   * Excessive premiums -- you must realize that premiums will not necessarily be any less with risk retention groups, or pools and they may often be more. After an actuarial analysis of future claims and funding, you may be told to set premiums at the same level as commercial insurance. But these groups provide a stability in premium that cannot be found in the commercial insurance market. They also offer many of the advantages spoken of above. If premiums seem to be the only concern of potential members, you may want to look at the purchasing group alternative.

2. Homogeneity -- An extremely important aspect of any group arrangements is that there is a good deal of homogeneity of interest and demographics among the various members.

   * Common crisis
   * Comparable exposures -- This does not merely include comparable liability exposures, but also the size and demographics of the agencies. A major blocking point will be fears of grouping small agencies with large agencies.
   * Similar objectives and goals

3. Risk sharing

   * There must be a real consensus that the group wants to share its risks.
   * Equitable capital contributions -- are initial capital contributions fair to all participants?
   * Rating plan -- What formula is used for determining premiums among various group members?
   * Spreading of risk

4. Political support

   * Construct a task force/committee on the issue -- A favorable task force recommendation can gain support for the concept.
   * The feelings of influential members and funding sources must be considered.
   * You should hold everyone together by involving everyone.

5. Prudent funding

   * Actuarial analysis
   * Adequate capital and premiums
   * Expense projection
   * Reinsurance (if available)

EXHIBIT IV.3

CONTINUED

6. Long-term commitment

    * Forcing long-term commitment is often necessary in order to overcome the premium focus of member actions. In a soft market commercial insurers may be able to undercut the groups premiums. It is vital that there is some mechanism to hold the members in the group, or retain a long-term commitment on their capital contributions. Create hardship and hurdles for anyone wanting to cut short their commitment.
    * Establish bylaws
    * Establish financial limitations
    * Establish policy terms and conditions (i.e., 3 year policies with annual renewal of premiums)

7. Quality underwriting

    * You must rule out covering unacceptable risks, either up-front or on renewals. Look hard at risks which should possibly be cancelled. See that these risks are being dealt with through risk management processes (see #8 below). Keep bad risks out and kick out those that fail to respond with good risk management.
    * Objective and consistent evaluation
    * Exposure sensitive rating -- are higher risk agencies charged accordingly?
    * Cancellation provisions

8. Risk management

    * Enforcing risk management standards is essential to reduce losses for the group.
    * Evaluation of exposures
    * Focused risk control program
    * Continuous monitoring

9. Cost effectiveness

    * Unbundled services: actuarial, legal, accounting, banking, captive management, reinsurance, brokerage
    * Effective claims handling
    * Recapture of investment income

10. Equitable profit/loss distribution

    * Formula determined up-front
    * Customized for: losses, premium size, years in program, capital contribution.
    * Assessability is important -- what happens when there is catastrophic loss? Be prepared to collect more from members when the finances of the group are jeopardized by catastrophic loss. Assessability may be necessary for the continued viability of the group.
    * Dollars one spends in participation in group should not impact pooling decisions

Source: Adapted from material presented by Tillinghast, Nelson, and Warren in "Pooling, An Introduction for Public Agencies," Public Risk and Insurance Management Association (PRIMA), 1987.

EXHIBIT IV.4

TASK TIMETABLE FOR POOL INFORMATION

Task	Month of Completion
Formation of the Core Group	1
Recruitment of Additional (Core Group) Members	2
Legal and Regulatory Research	2
Development of Objectives and Identification of Coverages to Pool	2
Selection of Consultants	2
Data Collection	6
Determination of Pool Structure	6
Preparation of Bylaws	6
Selection of Service Providers	7
If Required, Regulatory Review	7
Formal Membership Action	7-9

Source: "Pooling, An Introduction for Public Agencies," Public Risk and Insurance Management Association (PRIMA), 1987, p. 9.

Closely related to legal analysis is the review of regulatory requirements imposed on pools by departments of insurance or other state agencies. State authority over self-insurance pools varies greatly from one state to another; most state insurance departments are not involved, yet others require final approval of all program details.

Program Goals and Objectives

After creating a core membership group and conducting initial research into the legal and regulatory aspects of pooling, pool participants should develop a statement of objectives. This statement will assist in forming program boundaries as feasibility design efforts get under way and provide a focus for the pool's organizers. Some of the more common objectives are listed in Exhibit IV.5. These are examples only; they are used to illustrate the types of issues that should be identified early during pool formation.

Coverage Identification

Although pools can provide a wide range of coverages, the decision must be made as to whether the pool can effectively provide several coverages or should limit itself to the one line of insurance that has been difficult or expensive to obtain.

Budget Development

The planning and implementing of a pool will cost money, therefore some charge to participate for the feasibility study is necessary. A budget should be developed and approved by participants. Line items for the budget include consultant fees for program feasibility analysis, actuarial projections, legal research, travel, meeting expenses, and survey research. The fee serves to fund planning activities and to measure participant interest in the program.

The business plan, an important part of the feasibility study, may require expert advice. A discussion on how to go about obtaining outside technical assistance is found in Chapter VII of this manual. A preliminary step in a feasibility study is the preparation and conduct of a survey. A questionnaire is distributed to interested participants to determine:

. types of coverage desired;

. current coverage data including limits, deductibles, and coverage terms;

. exposure data; and

. claims history for the past three to five years.

Using this information a feasibility study will show the types of coverage for which pooling is feasible, the aggregate amount required to fund expected losses and expenses, the type of rating plans to be used, special coverage features to be

EXHIBIT IV.5

SAMPLE PROGRAM GOALS AND OBJECTIVES

1. *To better define the scope and terms of insurance coverage.* In a self-insurance pool, levels of deductibles, insurance coverages and various insurance policy terms are developed to suit the specific needs of pool members. Even if the final self-insurance pool establishes limitations on certain coverages, it is unlikely to withdraw completely from an area as private carriers often do. The owner/consumer nature of a self-insurance pool gives pool members greater latitude to decide on the risk exposures that their premium dollars cover.

2. *To improve the management of insurance related services.* Improved management of services could be one of the most important reasons for establishing a self-insurance pool. Because the pool selects providers in each service area, it can choose firms better qualified to provide specific services. For example, a claims adjusting firm which is not performing to a desired level of service can be replaced without causing significant changes elsewhere in the program. Other service areas include: loss control, cash and investment management, legal defense, and management information systems.

3. *To compile data for risk management programs.* The pool helps participants identify priorities for cost effective risk management by analyzing claims frequency and severity. Typically, the insurance industry has not provided sufficient claims data and other information desired by most public agencies.

4. *To improve cash management and benefit from investment earnings.* The flow of funds in a self-insurance pool differs significantly from purchasing insurance. Combination payment schedules can be adjusted and the reserves can be invested to benefit pool members. Earnings can be used to offset operating expenses or poor loss experience, to reduce future rate increases, or they can be returned as dividends to members. Retaining these investment earnings of pool premiums is an important objective of a self-insurance pool.

5. *To provide cost savings to pool members.* Premium reductions may be substantial during hard markets when insurance coverage is expensive and difficult to obtain, and more modest during soft market conditions. Even if costs escalate, pool members are able to directly relate increases to specific causes, such as poor experience or reinsurance rate increases. During hard markets many communities have experienced substantial premium increases without reason. Self-insurance pools do not guarantee that insurance costs won't increase, but historically, pools have provided members with coverage and service at a reduced cost.

Source: "Pooling, An Introduction for Public Agencies," Public Risk and Insurance Management Association (PRIMA), 1987, p. 9.

provided, capitalization or risk margin recommended, method of administration and legal organization form to be used, and investment program and cash flow projections for three or more future years. These features are, in turn, compared to those of the insurance programs of the potential participants. Advantages and disadvantages of a pool are thoroughly discussed and considered for action by the group.

Funding Methods

Contributions to a pool are used to finance the losses of its members. The manner in which members are assessed, financial resources are applied, and risk is shared are the basic financial issues for a pool.

Contribution Formulas

To fund the self-insurance program, contributions are required from participating organizations. Each pool member's share of aggregate pool funding needs is a critical determination. The contribution formula is frequently the result of compromise among members seeking an equitable method of sharing pool costs.

- Workers' compensation pools frequently rely on payroll as a primary factor in calculating each participant's annual contribution.

- The value of covered property is a common factor in determining contributions to property pools.

- Operating or general fund budgets is a common contribution base for liability self-insurance pools.

- Contributions for vehicle coverage are often measured by the number, type, and use of vehicles in possession of each pool member. Transit pools are more likely to use revenue miles, ridership, operating hours, or some combination of these factors to allocate pool costs by formula.

A composite rate, which considers all of these factors, can be developed for multi-line coverages.

During the initial years of program operations, the formula should be simple and free of unnecessary or complicating factors. Later, there will be an advantage to promoting loss control by adjusting annual contributions according to good or bad loss histories. Loss and other adjustment factors are then possible because of data the pool has developed. Unforeseen and unavoidable catastrophic losses experienced by an individual member are generally excluded from loss adjustment factors. Conversely, an entity, which experiences a significant number of vehicle claims in an area subject to control by the insured, should have them counted as part of its loss adjustment factor. Contribution formulas can be adjusted for members assuming different levels of deductibles. Some pools offer one deductible, e.g. $1,000, for each member. Others offer members a choice of deductible levels.

An example of a premium allocation formula used by the Transit Mutual Insurance Corporation of Wisconsin is presented in Appendix G-1. This formula bases each transit system's premium on three factors: 1) miles operated; 2) accidents per 100,000 miles; and, 3) the system's incurred loss dollars. Items (2) and (3) are used for calculating reward and penalty factors.

Financing Options

Self-insurance pools generally follow one of two financing operations: pure self-insurance and structured self-insurance.

Pure Self-Insurance: In pure self-insurance, annual contributions from members are collected to meet the projected costs for the program's upcoming year. This involves not only cash payments for losses incurred for the year, but also the creation of a reserve fund to pay for losses incurred but not reported, for losses which require more than one year to resolve, and expenses for program administration and contract services.

Under pure self-insurance, no risk is shifted from the pool to an insurance carrier via a reinsurance policy. This financing option often is referred to as "going bare." Pure self-insurance requires a refined and comprehensive study of losses. Since no upper limits exist on the resources required by the pool to pay losses, unless member agreements and coverage documents limit the pool's exposure to some predetermined funding level, a pure self-insurance pool may require:

. larger up-front contributions to "capitalize" or provide a large risk margin for adverse results;

. the ability to assess members for amounts over and above their normal contributions; and/or

. a line of credit, debt issuance, or other financing tool.

A pool funded in this manner should establish limits on the amount it will pay per claim. Any claims costs above and beyond these limits would revert back to individual members. Alternatively, a pure self-insurance program might levy assessments to generate funds for claims that exceed its limits. In either event, pools organizations should recognize the need for limits and address how to pay claims which exceed the resources of the pool.

Structured Self-Insurance. A second form of pool funding is structured self-insurance, which combines elements of pure self-insurance and components of the traditional insurance market. Under this arrangement, a significant portion of the contributions received from members is assigned to a loss fund from which claims are paid. In addition, reinsurance is purchased to protect against single large claims (per occurrence excess). Sometimes reinsurance is purchased to be excess of the cumulative dollar amount of the loss fund (aggregate excess). These policies are purchased at retention levels not readily affordable by an individual organization. For example, per occurrence excess coverage may begin above an initial payment by the pool of $300,000. Policies protecting against total cumulative payments from by the loss fund might begin after the loss fund has paid $1 million plus. These insurance components in the program provide a greater comfort level to members concerning the annual contribution required to pay claims, reduce the possibility of assessments, and hold down capitalization requirements.

Each risk-financing structure is a workable approach to establishing a self-funding program for insurance pools. The cost and availability of reinsurance usually dictate the extent to which the final program more closely resembles one of the above descriptions. It may be realistic to begin with a structured self-insurance program when contribution volume is low, and/or loss history data is incomplete. After the pool is established, a concentrated effort on building a loss history and financing structure suitable for pure self-insurance can be made.

Capitalization and Surplus[1]

Members of the pool must determine its desired level of capitalization. In addition to generating funds needed to conduct the business affairs of the pool and to pay expected losses, a surplus has many advantages. A surplus is the amount by which assets exceed liabilities. First, surplus funds can be invested and can become a source of income for the program. Second, the surplus can be used to fund losses and expenses that exceed the original projections. Although some limits may be placed on the size of a surplus held by a pool, its presence is highly desirable and should be a part of the pool's financial plan from program inception.

Specific capital contributions of members, over and above regular contributions can be used to create the initial surplus. Moreover, funds may be pledged from borrowing arrangements, such as letters of credit, certificates of participation or bond proceeds. Currently, there is a great deal of activity and research directed at capitalizing a loss-fund with borrowed funds; i.e., debt financing of self-insurance programs. To pay all or a substantial portion of loss with borrowed funds when current resources are available is probably not cost effective, but there are advantages to having credit available to smooth the peaks in cash flow that inevitably arise in a self-insurance program.

The emergence of a surplus (through whatever means) can result in questions about its ownership. If twenty members created a program which now has a surplus of $250,000, what is the individual right of any given member to that surplus?

---

[1]While there are some technical distinctions between the terms "capital" and "surplus," these differences are not material to this discussion, and we use the terms interchangeably in this section.

Specifically, under what circumstances does that member have a right to a return of surplus? The best designed pools determine the answers to these questions before the pool is implemented. This avoids disputes, lawsuits, and ill will that are sure to arise on this subject, if not resolved at pool inception.

It should be noted that loss reserves are needed to offset known liabilities and are not surplus. Operating on a cash, (i.e., not funding a reserve for incurred-but-unpaid losses) rather than an incurred basis, can put the pool in a dangerous financial situation.

Some pools discount the annual cost to members by the amount of investment earning on funds. In other words, the investment earnings are projected and assumed to be part of total membership contributions. Therefore, total funding needs of $200,000 might be met from member contributions of $180,000 and the balance from investment earnings. With proper technical advice and analysis, this is an acceptable funding approach.

Program Management

Managerial and operational issues need to be addressed by a pool. These issues include the development of bylaws, membership agreements, staffing, and pool management standards.

Bylaws

Bylaws define the organization's structure and its governance. A standard outline of organizational bylaws would at a minimum include the following:

. Purpose

. Eligibility

. Member powers and duties

. Board of Directors powers and duties

. Election of directors, officers

. Meetings, voting rights

. Dissolution provisions

. Committees

. Amendments

Additional topics can be added as needed. For example, a self-insurance pool may decide to offer additional coverages or open its membership to new types of organizations. Appendix G-2 provides an example of bylaws from the Transit Mutual Insurance Corporation of Wisconsin.

Member Participation Agreements

Member participation agreements establish the commitment and responsibilities of each pool member. Policies addressed by the agreements include:

. Legal authority

. Contributions and assessments

. Withdrawals and expulsions

. Member obligations

. Pool obligations

. Dividends

. Surplus ownership

Staffing Options

The two primary staffing choices are to hire pool staff or contract for services. A combination of the two works well. Exhibit IV.6 shows a continuum of potential involvement of a sponsoring organization in pool management along with the possible advantages and disadvantages associated with each structure.

Initially, most pools decide on a limited number of staff positions to minimize fixed overhead and administrative expenses. At the formation of a larger pool, some provisions should be made for a chief executive or administrative head employed by the pool.

Once established, pool activities fall into two categories: 1) ongoing pool management and administrative duties, and 2) specialized technical services. The first category includes:

. daily member relations

. program development

. oversight of financial affairs

. applicant and new member processing

EXHIBIT IV.6

CONTINUUM OF SPONSORING ORGANIZATION INVOLVEMENT IN POOL MANAGEMENT

	STRUCTURE*	POSSIBLE ADVANTAGES	POSSIBLE DISADVANTAGES
LOW	Endorsement by sponsoring organization of external program run by broker, service agent, etc.	No initial investment to organize, staff. Income to organization. Low expertise, time of staff. Broader coverages. Improved data collection. Possible lower cost through use of discounts, dividends. Targeted loss control. Stability.	Marginal cost reduction. Little or no control over: · services finances reserves data Lower identification with program. May reduce alternatives available to members by inhibiting competitors. Margin, if any, stays with providers.
MEDIUM	Operation by sponsoring organization, subcontracting some or all services.	Increased control over marketing, finances. Ownership of reserves, investment income. Focus on necessary services. Costs linked directly to amounts of services	Staff time to monitor service providers, finances, contract administration. Increased competition from other organizations.
HIGH	Operation by sponsoring organization, internal staffing for all functions.	Highest level of control. Maximum return to members, since all costs are internal. Direct, responsibe services	Highest overhead. May conflict with interests of members, from need to maintain programs Head-to-head competition with other insuring organizations Higher financial risk.

* Factors which influence choice of structure include: size of initial and potential group; availability of expertise and time to perform necessary planning, organizing, directing and control functions, either hired (internal staff) or purchased (contracts with consultants, brokers, service providers etc.); geographic area to be covered; existing competition.

** More than one approach might be used at the same time for an organization operating several different pools at different stages of development What may be appropriate to start a group may not be the best structure once the group has been operating, data is available, and reserves are starting to build. Continuous evaluation of alternatives will identify the most cost-effective method for providing each service

Source: "Pooling, An Introduction for Public Agencies," Public Risk and Insurance Management Association (PRIMA), 1987, p. 33.

. risk management service (e.g., loss control) monitoring

. contract administration and evaluation

. special projects

. board meeting support

These activities are best handled by individuals employed by the pool who report directly to the Board of Directors or Trustees.

Specialized technical services are often more efficiently and effectively purchased from contractors. These include:

. investment management

. legal defense

. safety training

. claims adjusting

. financial accounting

. actuarial services

Contracting allows for a change in the service providers as needed and makes it easier to respond to changing work loads.

In summary, most pools find internal staff better equipped to handle administrative and program development issues, while various technical services are delivered more effectively through contracting with outside agencies. Financial audits, actuarial services and program evaluation should always be done by outside contractors to insure objectivity and maintain credibility.

Management Standards and Operating Procedures

A set of standards for pool management prepared and published by the Public Risk and Insurance Management Association (PRIMA) is presented in Exhibit IV.7. These standards of performance address pool structure, insurance, membership, finance and contracted services.

Appendix H contains a sample pool operating procedures guide. This guide is only an example, and should be adapted to the management and operational needs of each individual pool. Another example of a working management plan is presented in Appendix I. It is the Business Plan developed when Transit Mutual Insurance Corporation of Wisconsin was first formed.

EXHIBIT IV.7

ADVISORY STANDARDS FOR POOL MANAGEMENT

A. STRUCTURE

1. Management should have on hand signed original copies of the appropriate legal form of organization (bylaws, charter, trust agreement, etc.). Counsel should be retained to advise on compliance with all appropriate statutes. There should be records of appropriate filings with regulatory agencies. Consideration should be given in planning to selection of appropriate tax status.

2. The fund bylaws should include policies for the selection of trustees which specify number, term of office, compensation (if any), powers, and duties, any eligibility criteria and indemnification for any liability costs.

3. The fund bylaws should include procedures for the dissolution of the pool in an organized fashion.

B. INSURANCE

4. There should be evidence of adequate and appropriate insurance coverage on persons governing and/or administering the trust. Trustees should have directors and officers coverage, fund managers should have errors and ommissions coverage and employees who handle trust funds should be bonded. If the pool administrators provide consulting services, specific errors and omissions insurance should be obtained to cover this exposure.

5. The fund bylaws should provide trustees with the power to approve the amound of reinsurance to be purchased by the pool. Any catastrophic coverage, excess loss coverage, specific stop loss, or other types of reinsurance purchased should provide the fund with adequate protection. There should be evidence of appropriate underwriting including sufficient funding, credible loss experience, and an adequate spread of risk, employing actuarial review and projection where relevant.

C. MEMBERSHIP

6. There should be legal agreements with members of the pool defining the responsibilities and benefits of each member, as well as the responsibilities of the pool management. All services to be provided should be explained in detail, so that their quality and quantity can be effectively audited.

7. The agreements should stipulate how any surplus will be divided up among the pool participants, including the basis for return (premium and/or loss experience), eligibility if a member withdraws, and eligibility to receive distributions related to years prior to a member's participation.

8. Agreements with pool members should incluoe a non-payment provision. This provision gives pool management the right to terminate the contract with any member which fails to pay its premiums, and to recover costs to collect any and all premiums that are earned pro rata for the period preceding contract termination.

EXHIBIT IV.7

CONTINUED

9. Reserves must be protected from appropriation by the governing body which controls the fund. This can be done by stipulating in the fund bylaws and member agreements that "funds are for the purpose of claims payments and are the property of members." However, the pool can maintain the right to make surplus distributions by adding: "any surplus funds may only be appropriated for uses other than claims payment and associated pool expenses through a decision of the board of directors."

D. FINANCE

10. Pool mamagement should see that standards on accounting practices are developed. These standards would encompass: 1) earned and unearned premiums, 2) accounting for losses, expenses and 3) investment income on a policy year basis which segregates each pool year, and 4) the requirement to consider loss development factors and incurred-but-not-reported loss reserves.

11. The fund bylaws should provide for a certified public accountant audit and an actuarial audit of reserves to be conducted annually within a reasonable amount of time from the close of the appropriate fiscal period. These audits should be conducted by outside professional organizations which specialize in such types of audits. The pool should publish the audit reports and make them available to each of its participating members.

12. Pool management should provide written investment and cash management policies in accordance with applicable state laws. These policies should also be stipulated in any agency agreements that the fund makes with banks or other financial advisor/investment firms. Investment results should be reviewed and compared periodically to various indices. Such a review will assist pool administrators and boards in determining whether or not a change in investment and cash management policies is required or if a new financial advisor/investment firm should be selected.

E. CONTRACTED SERVICES

13. Service contracts of the pool should clearly define the responsibilites of each party. The contractor must provide adequate reporting to the pool trust or governing body. Copies of this contract should be reviewed by legal counsel and should include E. & O. coverage, ownership of data, run-out etc., for each type of circumstance.

14. There should be evidence of periodic contractor management audits performed by an independent risk management consulting or auditing firm. Auditors should review the rating and allocation of costs between members, as well as the appropriateness of the quantity and quality of services being provided to the pool. Also, the cost effectiveness of pooling compared to alternative forms of risk funding and purchased insurance should be considered.

Source: "Pooling, An Introduction for Public Agencies," Public Risk and Insurance Management Association (PRIMA), 1987, p. 34-35.

CAPTIVE INSURANCE COMPANIES

Program Scope

A pure captive insurance company subsidiary is established by a non-insurance organization to exclusively insure the risks of the parent company and its affiliates. Because the risks insured in such an insurance subsidiary do not leave the immediate corporate family, there really is no transfer of risk. Therefore, such a program is more accurately described as self-insurance than insurance.

For the nature and size of even the largest urban transit system, single parent captive insurance companies do not offer any significant advantages that could not be obtained with an individual self-insurance program. However, an association or group captive created to treat the collective risks of a group of similar, but separately owned, entities is a risk financing option with significant potential to stabilize the cost and availability of insurance coverage.

An association captive permits a group of entities to pool their financial resources so that they can assume an even higher level of risk than any one of them could under an individual self-insurance program. Accordingly, a captive insurer can offer its owner-policyholders the self-insurance advantages of:

- Lower costs from reduced overhead.
- Investment income on premiums held to pay future loss costs.
- Lower cost catastrophic protection possible because of access to reinsurance companies without as many middlemen in the process.
- A broadened insurance policy form. In essence, the owners dictate the scope of coverage for their own policies.
- Control over the claim handling and more of a voice in the settlement of claims.

Much of the discussion about pools in the preceding section applies to captives. In fact, the sample materials presented from the Transit Mutual Insurance Corporation of Wisconsin actually pertain to a captive organization. A unique law benefitting governmental entities in Wisconsin has permitted the formation of the first known association captive to serve municipally owned transit systems. The Wisconsin captive began operation in 1986 offering its owner-policyholders $1 million of liability protection at roughly half the cost of similar protection in the commercial insurance market.

Association captives closely resemble group self-insurance pools but with the following limitations:

. Captives require domiciles favorable to their operation.

. Captives are regulated more closely than pools. This can increase organizational expenses by 2% to 5% when compared to pools.

. Captives typically have formal capitalization requirements which pools may not.

Another term frequently used with association captive is risk retention group. Risk retention groups gained authoritative approval under the Risk Retention Amendments of 1986. This act allows trade associations, professional societies, and other groups of nonprofit and for profit organizations to establish national group self-insurance programs, known as risk retention groups. The Federal act preempts state laws inhibiting the formation of liability risk sharing groups. It allows the groups to provide all types of liability coverage including directors' and officers' liability but excluding workers' compensation. Membership is limited to organizations with similar liability exposures by virtue of similar services, products, trade, or operations.[1]

Captive Formation

Like pool organization, captive formation requires detailed planning. The transit system should prepare a business plan and feasibility study before committing resources to a captive insurer. Such studies may be made by internal staff, brokers having captive experience, captive management firms or independent consultants. Best results come from a disinterested source which cannot benefit from implementation of a captive. Due to the extensive arrangements needed to organize a captive insurer, it should not be viewed as a short-term alternative to commercial insurance. Participation in a captive project requires long-term commitment, generally three to five years.

Captive insurance companies are typically domiciled in just a few locations because these locations offer a favorable environment in terms of:

. the amount of capital required in relation to what is normally required by most State Insurance Departments;

. freedom from income and/or premium taxes;

. limited insurance company regulation; and

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[1]Public Risk and Insurance Management Association, United Way of America Risk Management Guide for Nonprofits, R. Bradley Johnson, principal author, 1987, pp. 56-57.

- freedom from assigned risk pool and insurance company solvency fund assessments.

The locations that have attracted the most individual and association captives are:

- Bermuda Islands
- Cayman Islands
- Colorado
- Tennessee
- Vermont

While there are other locations favorable to the formation of captives, the above are the most popular and have perhaps the best banking, legal, accounting and captive management services to support such ventures. Further, the political and regulatory environment in these domiciles is favorable for captive formation and operation.

Funding Methods

Captive insurance companies are governed by a Board of Directors, heavily if not entirely composed of owner-policyholder representatives. The three forms of captive insurers are:

- Stock company - formed by selling stock to raise capital for the organization. Commonly, in an association captive, most or all of the stock is owned by the member policyholders.

- Mutual company - where the owner-policyholders provide the organization's capital, usually through charging higher premiums in the insurer's formative years.

- Reciprocal company - almost identical to a mutual.

Minimum capitalization requirements vary by jurisdiction. The range is usually \$250,000 to \$1 million, although smaller amounts are possible.

Program Management

Necessary management services include underwriting, accounting, legal, claims adjusting, and filing with authorities among others.[1]

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[1] Practical Risk Management: The Professionals Handbook, P.O. Box 10093, Oakland, CA 94610, 1986. Topic B-10.

Association captives and similar programs are most easily formed and operate best when:

- The entities interested in participating in such a venture have similar operations and are otherwise similarly exposed to loss.

- Long-term commitments (at least three years) can be obtained from participants.

- The group sets up a mechanism to screen applicants and monitor the performance of participants so that no single participant produces an undue financial burden for the organization.

- Premiums or costs of the organization are at least partially based upon the individual participant's loss experience.

- Loss prevention of participants is specifically and professionally addressed in a sincere effort to reduce the number and severity of losses.

- Financial management of the program is conservative and demonstrates a financially sound organization.

- Management control of the organization is firmly in the hands of the participants, not a captive management company or other organization providing ongoing services to the association program.

SUMMARY

The risk financing methods discussed in this and the following chapter entail trade-offs between the amount of risk assumed by a transit organization and the cost of protection against losses. Additional considerations entering into the decision process include administrative burden, stability of premium costs, control over settlements, purchasing power, flexibility, and cash flow demands on the organization. Exhibit IV.8 summarizes the comparative advantages of the risk financing methods described in this manual.

EXHIBIT IV.8

COMPARATIVE ADVANTAGES OF RISK FINANCING METHODS

ADVANTAGE	METHOD			
	SELF INSURANCE	POOL	CAPTIVE	COMMERCIAL INSURANCE
Least risk		△	△	▲
Stability of premium costs	△	▲	▲	
Reduced overhead charges	▲	▲	△	
Realized investment income	▲	▲	▲	
Professional risk and claims management	△	▲	▲	▲
Spread costs of loss prevention programs		▲	▲	▲
Least state regulation requirements	△	△		▲
Combined purchasing power for excess insurance		▲	▲	
Least administrative responsibilities		△	△	▲
Control over claims management	▲	△	△	
Retention of funds until claim is paid	▲	△	△	
Minimal formation or acquisition requirements	△			▲
Broadened coverage available		△	△	
Lower cost excess coverage		▲	▲	△

Full Advantage ▲

Partial Advantage △

APPENDIX F

RISK MANAGEMENT AND INSURANCE SURVEY INSTRUMENT AND SURVEY RESULTS

MacDorman & Associates and Advanced Risk Management Techniques (ARMTECH), 1988.

RISK MANAGEMENT AND INSURANCE SURVEY
JUNE 1988

General Information

1. Date: ___/___/___

2. Transportation System Name: ______________________________

3. Address: ______________________________________

____

____

4. Person Completing Survey:* ______________________________
(Name)

________________________ ________________________
(Title) (Telephone Number - with Area Code)

5. Legal status of the transit system (check one):

a. ____ City Agency
b. ____ County Agency
c. ____ Local or regional joint powers authority
d. ____ State
e. ____ Special district
f. ____ For profit organization
g. ____ Other (describe) ____________________

____

____

6. Type of Federal operating assistance received (check one):

a. ____ Section 9
b. ____ Section 18
c. ____ Section 16(b)(2)
d. ____ Other (describe) ____________________

____

7. Population of area served (check one):

a. ____ Under 50,000
b. ____ 50,000 to 249,999
c. ____ 250,000 to 499,999
d. ____ 500,000 to 999,999
e. ____ 1,000,000 to 1,999,999
f. ____ Over 2 million

* Questions 8 through 23.

Transportation Operating Information

8. Current annual operating budget: $ ______________________

9. Total vehicle miles operated last fiscal year: ______________________

10. Current number of vehicles in fleet (both active and inactive):

 a. Revenue Vehicles

  . Motor bus ____________

  . Rapid rail ____________

  . Street car ____________

  . Light rail ____________

  . Demand Response ____________

  . Other ____________________ ____________

 b. Non-Revenue Vehicles ____________

 c. Total Vehicles ____________

11. Type of transit service provided (check all that apply):

		Approx. Percentage
a. _____	Fixed route	____________ %
b. _____	Demand responsive	____________ %
		100%

12. Types of passengers served:

		Approx. Percentage
a. _____	General public	____________ %
b. _____	Elderly and handicapped	____________ %
		100%

13. Number of passengers served last fiscal year: ____________

Insurance Practices

14. How does your transit system receive coverage for each of the following lines of coverage? (Check appropriate method for each line of coverage.)

	Line of Coverage		
Method of Coverage	Vehicle Liability	Directors & Officers Liability	Compensation
a. Conventional commercial insurance			
b. Through another agency (i.e., city or county)			
c. Assigned risk plan insurance			
d. State fund or other state assisted plan			
e. Own self-insurance program			
SIR level*	$		
f. Other risk financing arrangement			

(* Self Insured Retention)

15. If you checked (f) above, which other risk financing arrangement is used?

	Line of Coverage		
Arrangement	Vehicle Liability	Directors & Officers Liability	Compensation
a. Pool (joint powers or interlocal agency)			
b. Joint purchase from commercial insurer			
c. Captive insurer or risk retention group			
d. Other (describe) ______ ______ ______			

16. Does your transit system purchase its vehicle liability insurance through competitive bidding?

_____ Yes If yes, how frequently? _____ Annually

_____ No _____ Every three years

_____ Other (describe) _____________

____

17. What criteria is used to select vehicle liability insurance coverage? (Check all appropriate criteria. If you include all three criteria, please rank 1, 2, or 3.)

a. _____ Cost b. _____ Scope of coverage c. _____ Service

Claims Administration and Other Risk Management Services

18. Who in your transit system is primarily responsible for risk management and insurance matters? Check one:

a. _____ General manager b. _____ Fleet manager c. _____ Risk manager

a. _____ Finance director b. _____ Personnel manager c. _____ Other _____________

____

____

19. How are your vehicle liability claims adjusted? Check one:

a. _____ By the insurer c. _____ By an independent adjusting firm

b. _____ By the transit system d. _____ Other (describe) _____________

____

20. Who maintains the financial data for vehicle liability claims? (Check more than one if appropriate.)

a. _____ Insurer d. _____ Transit agency itself

b. _____ Insurance agent or broker e. _____ Records are <u>not</u> maintained

c. _____ Claims adjusting firm f. _____ Other (describe) _____________

____

____

21. If your answer to (20) above was (a), (b), or (c), do you:

a. Receive reports on a regular basis? _____ Yes _____ No

b. If yes, how often are reports received? ______________________________

c. Retain reports for at least five years? _____ Yes _____ No

22. How are claims records maintained?

a. _____ Manually b. _____ Computer

23. What insurance or risk management service providers have been retained by your transit system during the last three years?

a. _____ Loss control (safety) consultant

b. _____ Risk management consultant

c. _____ Actuary

d. _____ Claims auditor

e. _____ Other (describe) ______________________________

THANK YOU FOR YOUR ASSISTANCE!

Please return this survey by June 30, 1988 to:

MacDorman & Associates
Attn: Dianne Schwager
4808 North 29th Street
Arlington, VA 22207

SURVEY RESULTS

NUMBER OF RESPONDENTS BY TRANSIT SYSTEM FLEET SIZE

Fleet Size	Respondent	Percentage
0-49	80	42.6
50-99	38	20.2
100-299	27	14.4
250-499	17	9.0
500+	26	13.8
	188	100.0

NUMBER OF SURVEY RESPONDENTS BY SIZE OF OPERATING BUDGET

Budget Size	Respondents	Percentage
0-1 Million	36	19.1
1 Million - 2 Million	28	14.9
2 Million - 5 Million	40	21.3
5 Million - 10 Million	19	10.1
10 Million - 25 Million	24	12.8
25 Million - 100 Million	21	11.1
100 Million+	17	9.0
No Response	3	1.6
	188	100.0

DISTRIBUTION OF SURVEY RESPONDENTS BY LEGAL STATUS OF TRANSIT SYSTEM

Legal Status	Respondents	Percentage
City Agency	46	24.4
County Agency	18	9.6
Local or Regional Joint Powers Authority	43	22.9
State	9	4.8
Special District	36	19.1
For Profit	2	1.1
Other	33	17.6
No Response	1	0.5
TOTAL	188	100.0

DISTRIBUTION OF SURVEY RESPONDENTS BY LEGAL STATUS AND SIZE OF TRANSIT SYSTEM

LEGAL STATUS	TRANSIT SYSTEM FLEET SIZE GROUPS											
	0-49		50-99		100-299		250-499		500+		TOTAL	
	#	%	#	%	#	%	#	%	#	%	#	%
City Agency	32	40.0	7	18.4	5	18.5	1	5.9	1	3.8	46	24.2
County Agency	9	11.3	6	15.8	--	--	--	--	3	11.5	18	9.6
Local or Regional Joint Powers Authority	15	18.8	17	44.7	3	11.1	3	17.6	5	19.2	43	22.9
State	1	1.3	--	--	--	--	3	17.6	5	19.2	9	4.8
Special District	10	12.5	4	10.5	11	40.7	6	35.3	5	19.2	36	19.1
For Profit	--	--	--	--	2	7.4	--	--	--	--	2	1.1
Other	12	15.0	4	10.5	6	22.2	4	23.5	7	26.9	33	17.6
No Response	1	1.3	--	--	--	--	--	--	--	--	1	0.6
TOTAL	80	100.0	38	100.0	27	100.0	17	100.0	26	100.0	188	100.0

DISTRIBUTION OF SURVEY RESPONDENTS BY POPULATION CATEGORY

	Respondents	Percentage
Less than 50,000	22	11.8
50,000 - 249,999	80	42.7
250,000 - 499,999	28	15.0
500,000 - 999,999	23	12.3
1,000,000 - 1,999,999	20	10.7
Greater than 2,000,000	14	7.5
TOTAL	188	100.0

DISTRIBUTION OF SURVEY RESPONDENTS BY POPULATION AND TRANSIT SYSTEM SIZE

	TRANSIT SYSTEM FLEET SIZE GROUPS											
	0-49		50-99		100-299		250-499		500+		TOTAL	
POPULATION	#	%	#	%	#	%	#	%	#	%	#	%
Less Than 50,000	21	26.3	1	2.5	--	--	--	--	--	--	22	11.8
50,000 - 249,999	53	66.3	23	57.5	4	14.8	--	--	--	--	80	42.7
250,000 - 499,999	3	3.8	10	25.0	13	48.1	2	11.8	--	--	28	15.0
500,000 - 999,999	1	1.3	6	15.0	7	25.9	7	41.2	4	15.4	23	12.3
1,000,000 - 1,999,999	1	1.3	--	--	2	7.4	7	41.2	12	46.2	20	10.7
Greater than 2,000,000	--	--	--	--	1	3.7	1	5.9	10	38.5	14	7.5
No Response	1	1.3	--	--	--	--	--	--	--	--	1	0.5
TOTAL	80	100.0	40	100.0	27	100.0	17	100.0	26	100.0	188	100.0

TYPES OF TRANSIT SERVICES PROVIDED (i.e., MODES)

Mode	Respondents	Percentage
Motor Bus	175	93.1
Rapid Rail	14	7.4
Street Car	7	3.7
Light Rail	10	5.3
Demand Response	94	50.0
Other	37	19.7

NOTE: SYSTEMS MAY OPERATE MORE THAN ONE MODE

TYPES OF TRANSIT SERVICES PROVIDED BY TRANSIT SYSTEM SIZE

	TRANSIT SYSTEM FLEET SIZE GROUPS											
	0-49		50-99		100-299		250-499		500+		TOTAL	
MODE	#	%	#	%	#	%	#	%	#	%	#	%
Motor Bus	71	40.6	38	21.7	25	14.3	15	8.6	26	14.9	175	100.0
Rapid Rail	--	--	--	--	2	14.3	3	21.4	9	64.2	14	100.0
Street Car	--	--	--	--	--	--	1	14.3	6	85.7	7	100.0
Light Rail	1	10.0	--	--	--	--	1	10.0	8	80.0	10	100.0
Demand Response	33	35.1	23	24.5	17	18.1	9	9.6	12	12.8	94	100.0
Other	7	18.9	8	21.6	8	21.7	4	10.8	10	27.0	37	100.0
TOTAL	112	30.3	69	18.7	52	14.1	39	10.6	97	26.3	369	100.0

TYPES OF TRANSIT SERVICES PROVIDED AND TYPES OF PASSENGERS SERVED

Type of Service Provided		Type of Passengers Served	
Fixed Route	97.9%	General Public	95.7%
Demand Response	60.1%	Elderly and Handicapped	86.2%

TYPES OF TRANSIT SERVICES PROVIDED AND PASSENGERS SERVED BY TRANSIT SYSTEM SIZE GROUP

SERVICE & RIDERSHIP	TRANSIT SYSTEM FLEET SIZE GROUPS											
	0-49		50-99		100-299		250-499		500+		TOTAL	
	#	%	#	%	#	%	#	%	#	%	#	%
Fixed Route	77	96.0	38	100.0	26	95.8	17	100.0	26	100.0	184	97.9
Demand Response	40	48.7	28	69.7	18	75.0	10	66.7	17	66.7	113	60.1
TOTAL	80		38		27		17		26			
General Public	75	93.4	38	100.0	26	95.8	15	83.3	26	100.0	180	95.7
Elderly and Handicapped	67	82.9	37	97.0	22	83.3	12	75.0	24	95.8	162	86.2
TOTAL	80		38		27		17		26			

FREQUENCY OF INSURANCE PROCUREMENTS

Of the total number of respondenta, 128 (68.1) purchase vehicle liability through the competitive bid process. Of those who responded:

- 88 (68.7%) accept bids annually
- 21 (16.4%) accept bids every three years; and
- 18 (14.1%) accept bids at some other time period.

DISTRIBUTION OF SURVEY RESPONDENTS THAT PURCHASE VEHICLE LIABILITY INSURANCE THROUGH COMPETITIVE BID BY TRANSIT SYSTEM SIZE

	TRANSIT SYSTEM FLEET SIZE GROUPS											
	0-49		50-99		100-299		250-499		500+		TOTAL	
	#	%	#	%	#	%	#	%	#	%	#	%
Based on Total Respondents, YES:	56	69.7	28	78.8	18	66.7	10	50.0	16	66.7	128	68.1
Based on Those Who Said YES:												
Annually	37	66.0	23	84.7	12	68.8	6	50.0	10	62.5	88	68.7
Every Three Years	12	20.8	3	11.5	5	25.0	1	16.7	--	--	21	16.4
Other	6	11.3	2	3.8	1	6.2	3	33.3	6	37.2	18	14.1
No Response	1	1.9	--	--	--	--	--	--	--	--	1	0.8
TOTAL	56	100.0	28	100.0	18	100.0	10	100.0	16	100.0	128	100.0

CRITERIA USED TO SELECT VEHICLE LIABILITY INSURER AND INSURANCE COVERAGE

Criteria	Ranking 1	2	3	4	Did Not Rank	Total Percentage
Cost	38.6%	23.5%	6.5%	0.7%	30.7%	100.0
Scope	31.0	35.9	5.5	0.0	27.6	100.0
Service	1.5	10.8	66.1	0.8	20.8	100.0

CRITERIA USED TO SELECT VEHICLE LIABILITY INSURER AND COVERAGE BY TRANSIT SYSTEM SIZE

	TRANSIT SYSTEM FLEET SIZE GROUPS											
	0-49		50-99		100-299		250-499		500+		TOTAL	
	#	%	#	%	#	%	#	%	#	%	#	%
COST	64	78.9	34	90.9	22	79.3	14	75.0	19	75.0	153	81.4
1	27	45.0	12	40.0	36	26.3	4	33.3	10	50.0	59	38.6
2	13	20.0	7	23.3	5	26.3	4	22.2	7	38.9	36	23.5
3	5	8.3	3	6.7	2	5.3	--	--	--	--	10	6.5
4	--	--	--	--	--	--	1	11.2	--	--	1	0.7
9	19	26.7	12	30.0	9	42.1	5	33.3	2	11.1	47	30.7
SCOPE	61	77.6	33	87.9	20	70.8	12	66.7	19	75.0	145	77.1
1	16	25.4	10	31.0	6	29.4	5	37.5	8	44.4	45	31.0
2	27	45.9	7	24.1	6	29.4	3	25.0	9	44.4	52	35.9
3	2	3.3	5	17.2	1	5.9	--	--	--	--	8	5.5
4	--	--	--	--	--	--	--	--	--	--	--	--
9	16	25.4	11	27.7	7	35.3	4	37.5	2	11.1	40	27.6
SERVICE	54	68.4	29	75.8	19	66.7	10	50.0	18	70.8	130	69.1
1	2	3.8	--	--	--	--	--	--	--	--	2	1.5
2	4	7.7	7	24.0	2	6.2	--	--	1	5.9	14	10.8
3	38	71.2	14	56.0	10	56.3	8	83.3	16	88.2	86	66.1
4	1	1.9	--	--	--	--	--	--	--	--	1	0.8
9	9	15.4	8	20.0	7	37.5	12	16.7	1	5.9	27	20.8
OTHER	1	1.3	--	--	1	4.2	1	8.3	--	--	3	1.8
1	--	--	--	--	1	4.2	--	--	--	--	1	33.3
2	1	1.3	--	--	--	--	1	8.3	--	--	2	--
3	--	--	--	--	--	--	--	--	--	--	--	--
4	--	--	--	--	--	--	--	--	--	--	--	--
9	--	--	--	--	--	--	--	--	--	--	--	--

INDIVIDUAL RESPONSIBLE FOR RISK MANAGEMENT

Person Responsible	Respondents	Percentage
General Manager	63	33.5
Fleet Manager	8	4.3
Risk Manager	50	26.6
Finance Director	24	12.8
Personnel Director	4	2.1
Other	37	19.7
No Response	2	1.1
	188	100.0

INDIVIDUAL RESPONSIBLE FOR RISK MANAGEMENT BY TRANSIT SYSTEM SIZE

	TRANSIT SYSTEM FLEET SIZE GROUPS											
PERSON RESPONSIBLE	0-49		50-99		100-299		250-499		500+		TOTAL	
	#	%	#	%	#	%	#	%	#	%	#	%
General Manager	45	56.3	12	31.6	3	11.1	3	17.6	--	--	63	33.5
Fleet Manager	1	1.3	2	5.3	5	18.5	--	--	--	--	8	4.3
Risk Manager	13	16.3	9	23.7	4	14.8	5	29.4	19	73.1	50	26.6
Finance Director	8	10.0	6	15.8	6	22.2	3	17.6	1	3.8	24	12.8
Personnel Director	--	--	2	5.3	1	3.7	1	5.9	--	--	4	2.1
Other	12	15.0	7	18.4	7	25.9	5	29.4	6	23.1	37	19.7
No Response	1	1.3	--	--	1	3.7	--	--	--	--	2	1.1
TOTAL	80	100.0	38	100.0	27	100.0	17	100.0	26	100.0	188	100.0

GROUP RESPONSIBLE FOR CLAIMS ADJUSTMENT

	Respondents	Percentage
Insurer	61	32.4
Transit Agency	30	16.0
Independent Firm	68	36.2
Other	26	13.8
No Response	3	1.6
	188	100.0

GROUP RESPONSIBLE FOR CLAIMS ADJUSTMENT BY TRANSIT SYSTEM SIZE

	TRANSIT SYSTEM FLEET SIZE GROUPS											
	0-49		50-99		100-299		250-499		500+		TOTAL	
	#	%	#	%	#	%	#	%	#	%	#	%
Insurer	42	52.5	11	28.9	5	18.5	2	11.8	1	3.8	61	32.4
Transit Agency	2	2.5	3	7.9	5	18.5	6	35.3	14	53.8	30	15.6
Independent Firm	26	32.5	20	52.6	9	33.3	7	41.2	6	23.1	68	36.2
Other	8	10.0	3	7.9	8	29.6	2	11.8	5	19.2	26	13.8
No Response	2	2.5	1	2.6	--	--	--	--	--	--	3	1.6
TOTAL	80	100.0	38	100.0	27	100.0	17	100.0	26	100.0	188	100.0

MAINTENANCE OF FINANCIAL DATA FOR VEHICLE LIABILITY CLAIMS

	Respondents	Percentage
Insurer	75	39.9
Insurance Agent/Broker	49	26.1
Claims Adjusting Firm	59	31.4
Transit Agency	111	59.0
Not Maintained	0	0.0
Other	33	17.6

NOTE: BASED ON 188 RESPONDENTS. MORE THAN ONE RESPONSE WAS REPORTED BY SOME TRANSIT SYSTEMS.

MAINTENANCE OF FINANCIAL DATA FOR VEHICLE LIABILITY CLAIMS BY SYSTEM SIZE

TRANSIT SYSTEM FLEET SIZE GROUPS

	0-49		50-99		100-299		250-499		500+		TOTAL	
	#	%	#	%	#	%	#	%	#	%	#	%
Insurer	44	58.7	14	18.7	10	13.3	4	5.3	3	4.0	75	100.0
Insurance Agency/ Broker	28	57.1	14	28.6	4	8.2	1	2.0	2	4.1	49	100.0
Claims Adjusting Firm	21	35.6	14	23.7	11	18.6	7	11.7	6	10.2	59	100.0
Transit Agency	34	30.6	20	18.0	18	16.2	13	11.7	26	23.4	111	100.0
Not Maintained	--	--	--	--	--	--	--	--	--	--	--	--
Other	14	23.3	10	16.7	6	10.0	1	1.7	29	48.3	60	100.0

QUERY ON RECEIPT OF REPORTS

Of the total number of respondents, 104 (55.3%) receive reports on a regular basis. Of those who receive reports:

- 60 (57.7%) receive them monthly;
- 24 (23.1%) receive them quarterly;
- 7 (6.7%) receive them semi-annually; and
- 7 (6.7%) receive them yearly.

Of total respondents, 110 (58.5%) retain reports for at least five years.

QUERY ON RECEIPT OF REPORTS BY TRANSIT SYSTEM SIZE

	TRANSIT SYSTEM FLEET SIZE GROUPS											
	0-49		50-99		100-299		250-499		500+		TOTAL[1]	
	#	%	#	%	#	%	#	%	#	%	#	%
YES	43	22.9	29	14.5	14	7.4	10	5.3	8	4.3	104	55.3
TIME FRAME												
Monthly	20	33.3	14	23.3	12	20.0	8	13.3	6	10.0	60	100.0[2]
Quarterly	13	54.2	8	33.3	1	4.2	1	4.2	1	4.2	24	100.0[2]
Semi-Annually	4	57.1	2	28.6	--	--	--	--	1	14.3	7	100.0[2]
Yearly	4	57.1	3	42.9	--	--	--	--	--	--	7	100.0[2]
No Response	2	33.3	2	33.3	1	16.7	1	16.7	--	--	6	100.0[2]
TOTAL	43	41.3	29	27.9	14	13.5	10	9.7	8	7.7	104	100.0[2]
RETAIN REPORTS:												
YES	48	43.6	28	25.5	17	15.5	8	7.3	9	8.2	110	100.0

1 Percentages are based on the total survey sample of 188.

2 Percentages are based on the number of survey respondents (104) who responded "Yes" they receive reports on claims.

TYPES OF RISK MANAGEMENT SERVICE PROVIDERS RETAINED BY TRANSIT SYSTEM OVER THE LAST THREE YEARS

	Respondents	Percentage
Loss Control	54	29.2
Risk Management Consultant	47	25.4
Actuary	30	16.2
Claims Auditor	30	16.2
Other	24	13.0

METHOD OF MAINTAINING CLIAMS RECORDS BY TRANSIT SYSTEM SIZE

	TRANSIT SYSTEM FLEET SIZE GROUPS											
	0-49		50-99		100-299		250-499		500+		TOTAL	
	#	%	#	%	#	%	#	%	#	%	#	%
RECORDS MAINTAINED BY:												
Manual	46	57.5	18	47.4	14	51.8	7	41.0	9	34.6	94	50.0
Computer	32	40.0	23	60.5	17	63.0	15	88.2	25	96.2	112	59.6
RESPONDENTS BY CATEGORY	80		38		27		17		26		188	

NOTE: RESPONDENTS MAY HAVE CHECKED BOTH MANUAL AND COMPUTERS.

Insurance Practices: Budget Category: TOTAL SURVEY[1]

How does your transit system receive coverage for each of the following lines of coverage? (Check appropriate method for each line of coverage.)

Method of Coverage	Line of Coverage: Vehicle Liability	Directors & Officers Liability	Compensation
a. Conventional commercial insurance	100 (53.2%)	78 (41.5%)	74 (39.4%)
b. Through another agency (i.e., city or county)	9 (4.8%)	11 (5.9%)	12 (6.4%)
c. Assigned risk plan insurance	4 (2.1%)	0 (0.0%)	5 (2.7%)
d. State fund or other state assisted plan	4 (2.1%)	5 (2.7%)	21 (11.2%)
e. Own self-insurance program	88 (46.8%)	49 (26.1%)	61 (32.4%)
SIR level*	$ 1,000-7,500,000	$ 2,500-5,000,000	$ 140,000-4,000,000
f. Other risk financing arrangement	26 (13.8%)	13 (6.9%)	7 (3.7%)

(* Self Insured Retention)

If you checked (f) above, which other risk financing arrangement is used?

Arrangement	Line of Coverage: Vehicle Liability	Directors & Officers Liability	Compensation
a. Pool (joint powers or interlocal agency)	19 (10.1%)	12 (6.4%)	4 (2.2%)
b. Joint purchase from commercial insurer	1 (0.5%)		1 (0.5%)
c. Captive insurer or risk retention group	1 (0.5%)		
d. Other (describe) ____	4 (2.1%)		2 (1.1%)

____

____

[1] Percentages are based on total sample size of 188 respondents.

Insurance Practices: Budget Category: $0-$1M[1]

How does your transit system receive coverage for each of the following lines of coverage? (Check appropriate method for each line of coverage.)

	Line of Coverage		
Method of Coverage	Vehicle Liability	Directors & Officers Liability	Compensation
a. Conventional commercial insurance	22 (61.1%)	15 (41.7%)	13 (36.1%)
b. Through another agency (i.e., city or county)	3 (8.3%)	4 (11.1%)	3 (8.3%)
c. Assigned risk plan insurance	0 (0.0%)	0 (0.0%)	0 (0.0%)
d. State fund or other state assisted plan	1 (2.8%)	2 (5.5%)	4 (11.1%)
e. Own self-insurance program	8 (22.2%)	6 (16.7%)	5 (13.9%)
SIR level*	$ 1,000-500,000	$ 2,500-500,000	$140,000-500,000
f. Other risk financing arrangement	3 (8.3%)	4 (11.1%)	1 (2.8%)

(* Self Insured Retention)

If you checked (f) above, which other risk financing arrangement is used?

	Line of Coverage		
Arrangement	Vehicle Liability	Directors & Officers Liability	Compensation
a. Pool (joint powers or interlocal agency)	3 (8.3%)	3 (8.3%)	1 (2.8%)
b. Joint purchase from commercial insurer			
c. Captive insurer or risk retention group			
d. Other (describe)			

1 Number of respondents in category = 36.

Insurance Practices: Budget Category: $1M-$2M[1]

How does your transit system receive coverage for each of the following lines of coverage? (Check appropriate method for each line of coverage.)

	Line of Coverage		
Method of Coverage	Vehicle Liability	Directors & Officers Liability	Compensation
a. Conventional commercial insurance	15 (53.4%)	15 (53.4%)	13 (46.4%)
b. Through another agency (i.e., city or county)	2 (7.1%)	3 (10.7%)	2 (7.1%)
c. Assigned risk plan insurance	3 (10.7%)	0 (0.0%)	1 (3.6%)
d. State fund or other state assisted plan	1 (3.6%)	1 (3.6%)	3 (10.7%)
e. Own self-insurance program	4 (14.3%)	4 (14.3%)	3 (10.7%)
SIR level*	$ 0 - 1,000	$ 500 - 1,000	$ 0 - 250,000
f. Other risk financing arrangement	6 (21.4%)	1 (3.6%)	1 (3.6%)

(* Self Insured Retention)

If you checked (f) above, which other risk financing arrangement is used?

	Line of Coverage		
Arrangement	Vehicle Liability	Directors & Officers Liability	Compensation
a. Pool (joint powers or interlocal agency)	4 (14.3%)	1 (3.6%)	
b. Joint purchase from commercial insurer			
c. Captive insurer or risk retention group			
d. Other (describe)	1 (3.6%)		1 (3.6%)

1 Number of respondents in category = 28.

Insurance Practices: Budget Category: $2M-$5M[1]

How does your transit system receive coverage for each of the following lines of coverage? (Check appropriate method for each line of coverage.)

Method of Coverage	Line of Coverage: Vehicle Liability	Directors & Officers Liability	Compensation
a. Conventional commercial insurance	24 (60.0%)	22 (55.0%)	20 (50.0%)
b. Through another agency (i.e., city or county)	1 (2.5%)	2 (5.0%)	4 (10.0%)
c. Assigned risk plan insurance	1 (2.5%)	0 (0.0%)	3 (7.5%)
d. State fund or other state assisted plan	2 (5.0%)	2 (5.0%)	2 (5.0%)
e. Own self-insurance program	8 (20.0%)	4 (10.0%)	7 (17.5%)
SIR level*	$ 25,000-2,000,000	$ 50,000-500,000	$ 50,000-500,000
f. Other risk financing arrangement	4 (10.0%)	0 (0.0%)	1 (2.5%)

(* Self Insured Retention)

If you checked (f) above, which other risk financing arrangement is used?

Arrangement	Line of Coverage: Vehicle Liability	Directors & Officers Liability	Compensation
a. Pool (joint powers or interlocal agency)	2 (5.0%)		1 (2.5%)
b. Joint purchase from commercial insurer	1 (2.5%)		
c. Captive insurer or risk retention group	1 (2.5%)		
d. Other (describe)			

1 Number of respondents in category = 40.

Insurance Practices: Budget Category: $5M-$10M[1]

How does your transit system receive coverage for each of the following lines of coverage? (Check appropriate method for each line of coverage.)

Method of Coverage	Line of Coverage: Vehicle Liability	Directors & Officers Liability	Compensation
a. Conventional commercial insurance	11 (57.9%)	8 (42.1%)	9 (47.4%)
b. Through another agency (i.e., city or county)	1 (5.3%)	0 (0.0%)	0 (0.0%)
c. Assigned risk plan insurance	0 (0.0%)	0 (0.0%)	1 (5.3%)
d. State fund or other state assisted plan	0 (0.0%)	0 (0.0%)	3 (15.8%)
e. Own self-insurance program	8 (42.1%)	6 (31.6%)	4 (21.1%)
SIR level*	$ 25,000-5,000,000	$ 10,000-5,000,000	$100,000-350,000
f. Other risk financing arrangement	4 (21.1%)	3 (15.8%)	1 (5.3%)

(* Self Insured Retention)

If you checked (f) above, which other risk financing arrangement is used?

Arrangement	Line of Coverage: Vehicle Liability	Directors & Officers Liability	Compensation
a. Pool (joint powers or interlocal agency)	4 (21.1%)	4 (21.1%)	1 (5.3%)
b. Joint purchase from commercial insurer			
c. Captive insurer or risk retention group			
d. Other (describe)			

1 Number of respondents in category = 19.

Insurance Practices: Budget Category: $10M-$25M[1]

How does your transit system receive coverage for each of the following lines of coverage? (Check appropriate method for each line of coverage.)

Method of Coverage	Line of Coverage: Vehicle Liability	Directors & Officers Liability	Compensation
a. Conventional commercial insurance	12 (50.0%)	10 (41.7%)	8 (33.3%)
b. Through another agency (i.e., city or county)	0 (0.0%)	0 (0.0%)	0 (0.0%)
c. Assigned risk plan insurance	0 (0.0%)	0 (0.0%)	0 (0.0%)
d. State fund or other state assisted plan	0 (0.0%)	0 (0.0%)	7 (29.2%)
e. Own self-insurance program	22 (91.7%)	9 (37.5%)	11 (45.8%)
SIR level*	$ 12,000-7,500,000	$ 25,000-100,000	$150,000-500,000
f. Other risk financing arrangement	5 (20.8%)	4 (16.7%)	1 (4.2%)

(* Self Insured Retention)

If you checked (f) above, which other risk financing arrangement is used?

Arrangement	Line of Coverage: Vehicle Liability	Directors & Officers Liability	Compensation
a. Pool (joint powers or interlocal agency)	4 (16.7%)	3 (12.5%)	
b. Joint purchase from commercial insurer			
c. Captive insurer or risk retention group			
d. Other (describe)			1 (4.2%)

[1] Number of respondents in category = 24.

Insurance Practices: Budget Category: $25M-$100M[1]

How does your transit system receive coverage for each of the following lines of coverage? (Check appropriate method for each line of coverage.)

	Line of Coverage		
Method of Coverage	Vehicle Liability	Directors & Officers Liability	Compensation
a. Conventional commercial insurance	6 (28.6%)	6 (28.6%)	6 (28.6%)
b. Through another agency (i.e., city or county)	1 (4.8%)	0 (0.0%)	1 (4.8%)
c. Assigned risk plan insurance	0 (0.0%)	0 (0.0%)	0 (0.0%)
d. State fund or other state assisted plan	0 (0.0%)	0 (0.0%)	1 (4.8%)
e. Own self-insurance program	18 (85.7%)	12 (57.1%)	15 (71.4%)
SIR level*	$ 250,000-5,000,000	$ 5,000-100,000	$200,000-500,000
f. Other risk financing arrangement	1 (4.8%)	1 (4.8%)	2 (9.5%)

(* Self Insured Retention)

If you checked (f) above, which other risk financing arrangement is used?

	Line of Coverage		
Arrangement	Vehicle Liability	Directors & Officers Liability	Compensation
a. Pool (joint powers or interlocal agency)	2 (9.5%)	1 (4.8%)	1 (4.8%)
b. Joint purchase from commercial insurer			1 (4.8%)
c. Captive insurer or risk retention group			
d. Other (describe)			

1 Number of respondents in category = 21.

Insurance Practices: Budget Category: $100+M[1]

How does your transit system receive coverage for each of the following lines of coverage? (Check appropriate method for each line of coverage.)

	Line of Coverage		
Method of Coverage	Vehicle Liability	Directors & Officers Liability	Compensation
a. Conventional commercial insurance	10 (58.8%)	2 (11.8%)	5 (29.4%)
b. Through another agency (i.e., city or county)	1 (5.9%)	2 (11.8%)	2 (11.8%)
c. Assigned risk plan insurance	0 (0.0%)	0 (0.0%)	2 (11.8%)
d. State fund or other state assisted plan	0 (0.0%)	0 (0.0%)	1 (5.9%)
e. Own self-insurance program	17 (100.0%)	8 (47.1%)	16 (94.1%)
SIR level*	$ 100,000-10,000,000	$ 25,000-500,000	$ 250,000-4,000,000
f. Other risk financing arrangement	3 (17.6%)	0 (0.0%)	0 (0.0%)

(* Self Insured Retention)

If you checked (f) above, which other risk financing arrangement is used?

	Line of Coverage		
Arrangement	Vehicle Liability	Directors & Officers Liability	Compensation
a. Pool (joint powers or interlocal agency)			
b. Joint purchase from commercial insurer			
c. Captive insurer or risk retention group			
d. Other (describe)	3 (17.6%)		

[1] Number of respondents in category = 17.

APPENDIX G

TRANSIT MUTUAL INSURANCE COMPANY OF WISCONSIN

ALLOCATION FORMULA AND BYLAWS

PREMIUM ALLOCATION FORMULA

Effective 1-1-86

REVISED 12-10-87
for
Premium allocation beginning with year 1989

The allocation formula described below applies only to the premium for the basic liability insurance; it does not apply to the premiums for physical damage and excess insurance.

I. DEFINITIONS

A. Subject Years - The three year period's data used to calculate the reward and penalty statistics.

B. Miles Operated - The number of miles a transit system operates, both revenue and other.

C. Reportable Occurrence - Any occurrence resulting in present or future liability, monetary loss, or the potential for monetary loss, no matter how slight.

D. Accidents/100,000 miles - Divide the miles operated by 100,000 and then divide that number into the total number of "reportable occurrences".

E. Property's Financial Performance - Divide the total amount of payouts and reserves by the amount of premium paid in.

II. FORMULA STRUCTURE

A. The premium allocation formula is based on each property's performance on the following three factors:

1. Miles operated,
2. Accidents/100,000 miles.
3. The property's financial performance.

(Items 2 and 3 are reward and penalty factors.)

B. The official sources for the data used to calculate the above factors are as follows:

Factor	Official Date Source
Miles Operated	Miles reported by the transit systems directly to TMICOW

Accidents/100,000 miles-	Data for years 1982, 1983, 1984, and 1985 - Marsh & McLennan loss runs
	Data for years 1986 and beyond - TMICOW's loss data base
Property's Financial -	Data for years 1982, 1983, 1984 1985 - Marsh & McLennan loss runs
	Data for years 1986 and beyond - TMICOW's loss data base

All statistics are calculated on a calendar year basis with a cutoff of no earlier than June 30th of the current year for data to be included in the three subject years.

C. The subject years are determined as follows:

Premium for	Subject Years
1986	1982, 1983, 1984
1987	1983, 1984, 1985
1988	1984, 1985, 1986

1989 and beyond continuing as above.

D. The weights to be given to each allocation factor in determining the amount of premium for each individual property are as follows:

Year	1986	1987	1988 and beyond
% premium allocated by miles operated.	80%	70%	70%
% premium allocated by the accidents/ 100,000 miles.	10%	15%	15%
%premium allocated by a property's financial performance	10%	15%	15%

E. The effect of the reward and penalty factors will, however, be capped as follows:

Year:	1986	1987 and beyond
Upper limit	1.50	2.00
Lower limit	0.50	0.25

The upper limit is the maximum penalty that a property would receive based upon its poor performance.

The lower limit is the maximum reward that a property would receive based on its good performance.

III. Allocation Procedure

A. Assemble and calculate data for subject years for each property; i.e.:

	Year 1	Year 2	Year 3	Total of 3 Years	Premium Year
Miles Operated	X	X	X	X	X
# of Reportable Occ.	X	X	X	X	
Premium Paid	X	X	X	X	
Claims Paid and Reserved	X	X	X	X	
Accident Rate	X	X	X	X	
Financial Perf.	X	X	X	X	

B. Calculate average accident rate and financial performance for the entire group.

C. Calculate each property's variance from the average for accident and financial performance.

D. Allocate base premium based on annual allocation percentage (i.e., 70% 15% 15%).

E. Adjust the accident and financial performance parts of the premium by the variances as calculated under section III C.

F. Compare the premiums determined under section III D to section III E and adjust, if necessary, to stay within the caps defined in section II E.

G. Repeat section III E to make the individual premiums to be charged equal.

IV. Refunds

A. Unused premiums shall be held in an interest bearing "accrued but unpaid" dividend account for up to two years following the close of a calendar year.

B. At the end of the two year period, or sooner, providing there are no large unsettled claims remaining, any unused premiums shall be returned to the members on the same final percentage basis that the premium for that year was charged to each member.

BYLAWS

FOR

TRANSIT MUTUAL INSURANCE CORPORATION OF WISCONSIN

ADOPTED: 1-8-86
AMENDED: 9-4-86

ARTICLE I

Name and Address. The name of the nonprofit corporation shall be the Transit Mutual Insurance Corporation of Wisconsin, hereinafter referred to as the Corporation. The principal office of the Corporation shall be located at 730 Washington Avenue, City of Racine, County of Racine, State of Wisconsin. The Corporation may have other offices, either within or without Wisconsin, as the Board of Directors may determine from time to time.

ARTICLE II

Section 1. Purpose. The purpose of the Corporation is to provide vehicle liability and uninsured motorist insurance up to stated amounts, for its member mass transit operators. The insurance coverages are to be provided on a non-profit basis.

Section 2. Powers of the Corporation. The Corporation may exercise all of the powers granted by law to a municipal mutual insurance corporation. Among its powers, the Corporation has the power to insure the mass transit operations of its members. The Corporation's powers include, but are not limited to, the power:

a) to issue insurance policies;
b) to purchase insurance;
c) to contract for claim administration, safety, actuarial, accounting and other professional services;
d) to conduct or contract for insurance studies and planning and to coordinate these studies or plans with any other political subdivision or public agency;
e) to employ an executive director and other employees as it deems desirable to accomplish its purpose;
f) to enter into contracts with the Wisconsin DOT for consultation or other services; and
g) to make, amend and repeal, by action of its Board of Directors, all its bylaws, rules, and resolutions, whenever such action is not inconsistent with the purposes of the Corporation nor in violation of any local, state or federal law or ordinance, and whenever such action is deemed necessary to the discharge of the powers, duties and functions of the Corporation.

ARTICLE III

Section 1. Members. Any Wisconsin municipality is eligible for membership in the Corporation if it meets each of the following conditions: (1) it operates a transit system, (2) it is already a member in good standing of the Wisconsin Municipal Transit Insurance Commission, (3) its governing body adopts a resolution that ratifies joining the Corporation, (4) it has purchased some insurance from the Corporation, (5) it contributes the required initial premium or assessed amount, and (6) its membership is approved by the Corporation's Board of Directors. The Corporation may set the effective date of any new membership to coincide with the beginning of any appropriate time period.

Section 2. Withdrawal. No member may withdraw from the Corporation during the first three years of its membership. Thereafter a member may withdraw from the Corporation only upon 12 months advance, written notice.

Section 3. Cancellation. The Corporation may cancel any member's participation in the Corporation upon two-thirds vote of the Corporation's Board of Directors, but only upon 60 days written notice.

Section 4. Exit Penalties. In the event a member improperly withdraws from the Corporation an assessment of 50% of their current premium plus a fair share cost of administration and any assessability shall be due on demand. A request for waiver for all or part of the exit penalty may be brought before the Board of Directors and may be authorized by virtue of ARTICLE IV, Section B of Corporation bylaws.

ARTICLE IV

Section 1. Directors. Each member shall nominate one director to the Corporation's Board of Directors. Directors shall be elected by the members. Each director shall have one vote. The directors shall each serve for a period of three years, except that their initial terms shall be staggered so that approximately one-third of the initial directors' terms are for one year, one-third are for two years and one-third are for three years.

Section 2. Compensation. Directors shall not be paid salaries or expenses by the Corporation.

Section 3. Removal. A director may be removed from office by a two-thirds vote of the Board of Directors or by the appointing member for misconduct, neglect of duty in office or for other good cause.

Section 4. Vacancies and Succession. Vacancies on the Board of Directors shall be filled by the appointing member within 60 days after the vacancy first occurs. Unless otherwise removed, a director shall hold office until a successor has been elected.

Section 5. Meetings. The Board of Directors may provide, by resolution, the time and place for holding meetings of the Board of Directors. Meetings may be held without other notice than the resolution. Regular meetings may also be held on the call of the President upon seven days notice given by telephone, by mail, by telegram or in person. In the absence of any designation in the resolution or in the President's call, the meeting shall be held at the principal office of the Corporation.

Section 6. Special Meetings. Special meetings of the Board of Directors may be called by or at the request of the President or of any two directors and shall be held at the principal office of the Corporation or at any such place as the directors may determine. Notice of any special meeting shall be given at least three days prior to the meeting. Notice may be given by telephone, by mail, by telegram or in person. Any director may waive notice of any meeting. The attendance of a director at any meeting shall constitute a waiver of notice, unless a director appears solely to object to the notice given. At each special meeting, no business shall be considered other than that designated in the notice; however, if all directors of the Corporation are present, any item of business, whether or not designated in the notice, may be transacted with their unanimous consent.

Section 7. Quorum. A majority of the Board of Directors shall constitute a quorum for the transaction of business at any meeting of the Board; but if less than a majority are present, a majority of those present may adjourn a meeting without further notice.

Section 8. Board Decisions. An act of a majority of the directors present at a meeting at which a quorum is present shall be the act of the Board of Directors, unless the act of a greater number is required by law or by these bylaws.

ARTICLE V

Section 1. Officers. The officers of the Corporation shall be as follows: President, Vice-President, and Secretary/Treasurer.

Section 2. President. The President shall preside at meetings of the Board of Directors. The President may sign all instruments for the Board of Directors. At each meeting, the President shall submit recommendations and information concerning the business, affairs and policies of the Corporation.

Section 3. Vice-President. The Vice-President shall perform the duties of the President in the absence or incapacity of the President. In the case of the resignation, removal or death of the President, the Vice-President shall perform such duties as are imposed on the President until such time as a new President is chosen.

Section 4. Secretary/Treasurer. The Secretary/Treasurer shall keep minutes of all meetings of the Board of Directors and shall maintain complete and accurate records of all financial transactions. The Secretary/Treasurer shall act as President in the absence of the President and Vice-President. All meetings of the Board of Directors shall be open to the public, except for sessions properly closed pursuant to Section 19.85(1) of the Wisconsin Statutes.

Section 5. Election. The Board of Directors shall elect one of its members as President, one as Vice-President, and one as Secretary/Treasurer. Each office shall be held for three years. Each officer, however, shall hold office until a successor has been elected and qualifies or until he or she is removed. The President may select a committee to nominate officers as necessary. Any two offices may be held by the same person except the offices of President and Secretary/Treasurer, and except the offices of President and Vice-President.

Section 6. Removal. Any officer may be removed by the Board of Directors whenever in its best judgment the best interests of the Corporation would be served thereby.

Section 7. Additional Duties. The officers of the Corporation shall perform such other duties as may from time to time be required by the Board of Directors, bylaws, rules and resolutions of the Corporation.

Section 8. Vacancies. If the office of the president, Vice-President or Secretary/Treasurer becomes vacant, the Board of Directors shall elect a successor from its membership at its next meeting. Such election shall be for the unexpired term of the office.

ARTICLE VI

Section 1. Annual Meeting. The annual meeting of the Corporation's members shall be held the second Wednesday in October.

Section 2. Powers. All the powers of the Corporation shall be vested in the Board of Directors. A simple majority shall constitute a quorum for the purpose of conducting its business and exercising its powers and for all other purposes. Any number of directors constituting a majority of those present, however, may adjourn a meeting to a later date.

Section 3. Order of Business. The order of business at the annual meeting shall be as stated in the meeting agenda sent to the members.

Section 4. Manner of Voting. Voting on questions before the Corporation shall be by voice unless roll call is demanded by any one director.

ARTICLE VII

Committees. The President or a majority of the directors may appoint a committee at any time to investigate, plan, or perform administrative duties assigned to them. These committees shall report to the President. Any committee member may be removed by the President or Board of Directors.

ARTICLE VIII

Section 1. Financial Contribution. Each member shall pay its annual premium and any assessed prorated amounts in excess of its premium on the terms established by the Corporation. Any member that fails to pay as required shall, upon resolution of the Corporation's Board of Directors, cease to be a member in good standing, and shall be ineligible to vote until full payment is made.

Section 2. Premium and Assessment Determination. The Corporation shall provide those levels and kinds of insurance coverage for its members that are determined by the Corporation to be appropriately, practically, and lawfully provided. The Board of Directors shall annually determine the insurance coverage to be provided by the Corporation during the following fiscal year, beginning on the next January 1st. The Board of Directors shall also annually estimate the total dollar amount in member premiums required to fund the insurance coverage to be provided by the Corporation. After estimating the total dollar amount required, the Board of Directors shall than allocate that amount among the members. The allocated amounts shall be determined and then paid by the members as an annual premium established in accordance with an agreed upon premium allocation formula. Thereafter, the members may be assessed prorated amounts in excess of annual premiums whenever funds beyond the total annual premiums are required by the Corporation.

ARTICLE IX

Section 1. Contracts. The Board of Directors may authorize any officer or officers, agent or agents of of the Corporation, in addition to the officers so authorized by these bylaws, to enter into any contract or execute and deliver any instrument in the name of and on behalf of the Corporation, and such authority may be general or may be confined to specific instances.

Section 2. Check, Drafts, or Orders. All checks, drafts, or orders for the payment of money, notes, or other evidences of indebtedness issued in the name of the Corporation, shall be signed by such officer or officers, agent or agents of the Corporation, and in such manner as shall from time to time be determined by resolution of the Board of Directors. In the absence of such determination by the Board of Directors, such instruments shall be signed by the Secretary/Treasurer or an Assistant Treasurer and countersigned by the President or a Vice-President of the Corporation.

Section 3. Deposits. All funds of the Corporation shall be deposited from time to time to the credit of the Corporation in such banks, trust companies, or other depositaries as the Board of Directors may select.

Section 4. Gifts. The Board of Directors may accept on behalf of the Corporation any contribution, gift bequest, or devise for any purpose of the Corporation.

ARTICLE X

Books and Records. The Corporation shall keep correct and complete books and records of account and shall also keep minutes of the proceedings of its Board of Directors and committees having and exercising any of the authority of the Board of Directors, and shall keep at the principal office a record giving the names and addresses of the members entitled to vote. All books and records of the Corporation may be inspected by any member, or member's agent or attorney for any proper purpose at any reasonable time.

ARTICLE XI

Fiscal Year. The fiscal tear of the Corporation shall begin on the first day of January in each year and shall end at midnight on the last day of December of that year.

ARTICLE XII

Waiver of Notice. Whenever any notice is required to be given under the provisions of Wisconsin law or under the provisions of the articles of incorporation or the bylaws of the Corporation, a waiver thereof in writing signed by the person or persons entitled to such notice, whether before or after the time stated therein, shall be deemed equivalent to the giving of such notice.

ARTICLE XIII

Amendment of ByLaws. These bylaws may be altered, amended, or repealed, and new bylaws may be adopted by a majority of the directors present at any regular meeting or at any special meeting, if at least seven days' written notice has been given of the intention to alter, amend, or repeal or to adopt new bylaws at such meeting of the Board of Directors.

APPENDIX H

POOL OPERATING PROCEDURES GUIDE

"Pooling: An Introduction For Public Agencies," Public Risk Management Association (PRIMA) in Cooperation with PRIMA's Pooling Section, 1987, p. 73-93.

FOREWARD

These sample Pool Operating Procedures were prepared for reference purposes associated with Seminars arranged by the Pooling Section of the Public Risk and Insurance Management Association (PRIMA).

Since each intergovernmental risk management pool is unique, its bylaws and operating procedures must be tailor-made. Pools differ widely in mission, size, staff, legal constraints, and complexity. These Sample Procedures are designed to be helpful to those who are organizing pools and for discussion purposes in comparing and evaluating ongoing pool administration.

Most of the following text was taken from documents supplied by well established pools operating in Michigan, Illinois, California, and Texas.

Operating Procedures

PREAMBLE

Pursuant to the authority given to the Fund Trustees under Article IX(D) of the Fund Bylaws, the Fund Trustees have adopted the following operating procedures for the effective administration of the affairs of the Fund. All Fund members are bound by these procedures and any future procedures promulgated by the Fund Trustees. Fund members are also subject to the provisions contained in the Bylaws.

1. PURPOSE

This is a group self-insured program which provides worker's disability compensation benefits to the injured employees of Fund members. Fund services are designed to provide municipalities with greatly improved loss control efforts, as well as to minimize the cost of worker's compensation claims. The Fund also supplies members with information about State administrative activities and group representation on legislative issues involving worker compensation. These services are furnished at minimum cost to Fund members.

2. AGREEMENT WITH SERVICE COMPANY

A. The Fund Trustees have approved an agreement with a service company which provides the following services:

1. Assists the Fund in securing aggregate excess reinsurance for all losses in excess of a stated loss amount.

2. Inspects the work places, operations, machinery and equipment owned or operated by the participating members of the Fund.

3. Consults with and advises the Fund and its participating members as to medical and nursing services, including hospitalization and rehabilitation, and as to legal services.

4. Compiles and files notices and reports required under the Worker's Disability Compensation Act, upon receipt of initial report from either the Fund or any participating member; conducts any necessary investigation in order to determine the liability of the participating member under the Worker's Disability Compensation Act; and, processes any and all lawful claims under rules established by the

Bureau and the Fund Trustees.

5. Furnishes the Fund and participating members with full and complete monthly reports of all accidents and occupational diseases, and of all payments made and reserves set up for benefits and expenses on account of liability and/or reasonably anticipated liability for accidental injuries and occupational diseases sustained by employees.

6. Adjusts the normal premium payable by participating members by allowing for favorable or unfavorable experience so as to determine and assign premium modifications for each member annually in accordance with rules established by the Michigan Bureau of Worker's Disability Compensation and with policies established by the Fund Trustees.

7. Bills for and maintains records of all premium payments to the Fund in accordance with such rules as the Fund Trustees adopt.

8. Makes annual payroll audits of participating members.

9. Prepares on behalf of the Fund and the participating members for all scheduled hearings before the Bureau of Worker's Disability Compensation and generally administers all other details pertaining to participating members' obligations to their employees under the Worker's Disability Compensation Act.

10. Performs such other related services as may be reasonably necessary for the operation of the Fund.

B. Each member is bound by the terms of any agreement between the Fund Trustees and its service company.

C. Each member hereby appoints the service agent of this Fund as its agent and attorney-in-fact to act in its behalf and to execute all contracts, and reports, waivers, agreements, excess insurance contracts, and service contracts; to make or arrange for payment of claims, medical expenses, and all other things required or necessary under Michigan law and as covered by the terms of this Fund Agreement and the rules, regulations and Bylaws as now provided or as hereafter promulgated by the Trustees and/or the Bureau.

3. PAYMENT OF CLAIMS AND AWARDS

A. All claims are investigated by the designated service company. The service company is authorized to settle claims up to a designated amount established by the Fund Trustees without advance notice or approval of the Fund Trustees. In such cases, the service company will file a subsequent report to the Fund Administrator and Fund Trustees. On claims in excess of this amount, the service company shall present the claim to the Fund Trustees for settlement authorization. In those cases where timely action is necessary prior to a scheduled meeting of the Fund Trustees, a three-member committee designated by the Fund Trustees is authorized to act on behalf of the Fund Trustees to authorize settlements or take other appropriate action.

B. With respect to all claims that are not settled, the Fund shall pay all lawful awards made by the Bureau against any Fund member predicated on a claim by an employee of any Fund member, arising out of and in the course of such claimant's employment, and which award shall have been sustained by the courts where an appeal by either party is taken.

C. Any lawful award entered by the Bureau against a member of the Fund, if the award is upheld on appeal, shall be a liability of the Fund jointly but not severally. If the Fund is unable to pay the award, the Fund or the Bureau shall individually assess those employers who were members on the date of injury to the extent necessary to pay the award. Liability of any member shall be determined on a proportionate basis in accordance with such member's net contribution to the Fund. An assessment shall be a contractual obligation of the member.

4. LIMITATION OF FUND'S LIABILITY

The liability of the Fund is specifically limited to such obligations as are imposed by the Worker's Disability Compensation Act.

5. SUBROGATION

Each member agrees that in the event of the payment of any loss by the Fund under this contract, the Fund shall be subrogated to the extent of such payment to all the rights of the member against any person or other entity legally responsible for damages for said loss, and in such event the member hereby agrees to render all reasonable assistance, other than pecuniary, to effect recovery.

6. EMPLOYER APPLICATIONS

Applications for Fund membership are submitted on an approved form to the Fund Administrator, or to the designated service company. The Fund Trustees consider and act upon each application. Concurrence by a majority of the Trustees appointed or elected, the Fund's excess insurance carrier and the Bureau of Worker's Disability Compensation is required in order for an applicant to be admitted as a member.

7. WITHDRAWAL FROM MEMBERSHIP

Any Fund member may withdraw from the Fund by giving at least sixty (60) days notice in writing to the Fund Trustees of its desire to withdraw. Any member which withdraws or is not in good standing shall not be eligible to receive any return from the Fund surplus accumulation until the applicable statutes of limitation shall expire on all open or potential claims for the fiscal year involved. Open claims for this purpose shall mean any situation where notice of injury was given to the member, whether or not the member shall have reported the injury. The premium for members withdrawing from the Fund, other than at the end of the Fund year, shall be determined by the Trustees.

8. MEMBERSHIP REVIEW AND TERMINATION PROCEDURE

A. When in the determination of the Fund Administrator a Fund member has engaged in conduct, other than non-payment of premiums, that warrants review of that Employer's membership status, the Fund Administrator shall file a written report with the Board of Trustees. Said report shall contain a summary of the facts and the Fund Administrator's recommendations regarding continued membership status.

B. A copy of the Fund Administrator's report shall be served by mail on the Fund member along with a Notice of Hearing of the Board of Trustees. Said Notice of Hearing shall include the place, date and time of the hearing and a request to have representation at the hearing. At its discretion the Board of Trustees may submit written questions to the Fund member, written answers to which must be mailed to the Fund Administrator no later than seven (7) calendar days prior to the date of the hearing. A Fund member objecting to the report and recommendations of the Fund Administrator shall submit a written statement to the Board of Trustees setting out in detail the basis for the objection and any other information the Fund member desires to submit. Said statement must be mailed to the Fund Administrator no later than seven (7) calendar days prior to the hearing.

C. The Board of Trustees shall meet at the time and place designated in the Notice of Hearing. The Fund member shall be entitled to be represented at the hearing and present an oral statement and other information.

D. Following the hearing, the Board of Trustees shall affirm, modify, or reject the recommendation of the Fund Administrator. The Board of Trustees shall have the authority to place a Fund member on probation, the terms and duration of which it shall determine. A copy of the Board of Trustees' decision shall be served by mail on the Fund member.

E. In the event that the Trustees vote to terminate membership such termination shall not take place for at least 20 days after the member and the Bureau have received notice of the termination. The duration of the notice period shall be determined by the Trustees.

F. When a member has failed to pay its premium when due said member will be terminated from the Fund without a hearing. Said termination shall be effective at 12:01 a.m. on the 21st day after notice of termination has been received by the member and the Bureau.

G. The action of the Board of Trustees shall be final and binding.

9. PREMIUMS

A. The standard premium of Fund members is developed as in commercially insured plans, using rates published by the Worker's Compensation Rating Association based on published payroll classifications. Initially, the standard premium is based on experience modifications published by the Worker's Compensation Rating Association. In continuing Fund membership, each member is separately experience rated according to the formulas developed by the National Council on Compensation Insurance.

B. That portion of each member's contributions which shall not be required to pay claims, pay administration expenses and fees or to fund required or appropriate reserves may be returned to the members of the Fund from time to time when specifically authorized or approved by the Bureau.

10. METHOD OF PAYMENT

The Trustees of the Fund have established a payment schedule of one-quarter the annual premium paid in advance upon joining or renewal, and the balance in three successive installments of 25% each. This schedule is subject to change by the Trustees.

11. DELINQUENT PREMIUM PAYMENTS

A. Any eligible employer shall be required to make payment of the required premium as a condition of becoming or remaining a member of the Fund.

B. Any Fund member which fails to pay any premium or portion thereof within 20 days of the due date shall be terminated pursuant to Fund Bylaw IX(F).

C. Appropriate refunds and billings shall be made by the Fund at the conclusion of each annual payroll audit of each Fund member. Audited payroll billings shall be payable by Fund members within 20 days after the due date. A late payment charge of 10% of the billing shall be imposed and collected for any payment or portion thereof made after 20 days following the due date. A bona fide dispute between the Fund or any agent of the Fund and a Fund member over the audited payroll or any billing resulting therefrom, upon written notice to the Fund by the member within 20 days following the due date, shall be resolved pursuant to Fund Bylaw Article XI and no late payment charge shall be made during the period of dispute. A Fund member shall have 20 days following final decision by the Fund Trustees to pay a disputed audited payroll billing, and thereafter a late payment charge of 10% shall be imposed and collected on any amount paid thereafter.

12. INSPECTION OF FACILITIES. EQUIPMENT. AND RECORDS

The Fund Trustees, the service agent, and any of their agents, servants, employees or attorneys shall be permitted at all reasonable times to inspect the work places, plants, works, machinery, and appliances covered by this agreement, and shall be permitted at all reasonable times to examine members' payroll, personnel, injury and accident records, and members' books, vouchers, contracts, documents, and records of any and every kind which show or tend to show or verify the premium which is payable under the terms hereof. This right to inspect or examine shall continue after termination of membership with respect to all claims or matters arising during or relating to membership status.

13. SAFETY CONSIDERATIONS

Each member must follow the safety recommendations of the Trustees and the service company or any other agent of the Fund in order to provide safe and sanitary working conditions.

14. NOTIFICATION OF ACCIDENT AND REIMBURSEMENT TO FUND FOR PENALTY

A. Each Fund member must give immediate notification to the service agent on the prescribed forms of any accident and reported claim for any benefits whatsoever payable under the Worker's Disability Compensation Act.

B. Any penalty levied under Section 801(2) of the Act for failure to pay compensation benefits, medical expenses or travel allowances within 30 days after becoming due and payable, resulting from a member's failure to give timely notice to the service agent of an accident or claim for any benefits as heretofore described may, by a vote of a majority of the Trustees appointed or elected, be assessed against the member.

15. PROHIBITION OF UNAUTHORIZED PAYMENTS BY FUND MEMBERS

No Fund member shall make voluntary payment of weekly benefits or medical expenses or enter into any agreement with any employee or his agent committing payment or admitting liability for any worker's disability compensation benefits as provided in the Worker's Disability Compensation Act without the prior approval of the Board of Trustees or its designated service company. Any participant making such voluntary payments or entering into such an agreement may, by a vote of a majority of the Trustees appointed or elected, be held individually and separately liable for reimbursement to the Fund for all benefits and medical expenses paid or committed.

16. ILLEGAL EMPLOYMENT

No member shall employ any minor in violation of the Youth Employment Standards Act. Any member who employs a minor in violation of the Youth Employment Standards Act may, by a vote of a majority of the Trustees appointed or elected, be held individually and separately liable for any penalty payment incurred by the Fund as a result of an injury or illness incurred by a minor.

17. PENALTY FOR EMPLOYMENT OF PERSONS WITHOUT WORKER'S DISABILITY COMPENSATION COVERAGE

No member shall contract with any person, including contractors or subcontractors, who has not produced evidence of current worker's disability compensation insurance according to the provisions of the Worker's Disability Compensation Act. Any member who contracts with any person who does not have current worker's disability compensation insurance will be charged an additional nondiscounted standard premium based upon the full amount of the contract.

18. PERFORMANCE/REMOVAL OF FUND TRUSTEES

Fund Trustees are required to discharge their duties in good faith and with that degree of diligence, care, and skill which an ordinarily prudent person would exercise under similar circumstances. Grounds for removal include, but are not limited to, failure to attend regularly scheduled meetings, breach of confidentiality, conflict of interest and misuse of position.

19. TRUSTEE INDEMNIFICATION

Any person who at any time shall serve, or shall have served as a Trustee or officer of the Workers' Compensation Fund and the heirs, executors, and administrators of such person, shall be indemnified and held harmless by the Workers' Compensation Fund against all costs and expenses (including but not limited to attorney's fees of an attorney approved by the Trustees of the Fund), amounts of judgments and settlements reasonably incurred in connection with the defense of any claim, action, suit, or proceeding, whether civil, criminal, administrative, or other, in which he or they may be involved by virtue of such person's being or having been a Trustee; provided, however, that such indemnity shall not be operative with respect to: (1) the Trustee gaining any personal profit or advantage in his/her capacity as Trustee, (2) the dishonesty of a Trustee, (3) a Trustee's conflict of interest, (4) willful violation of a statute or ordinance committed by a Trustee or with the Trustee's knowledge or consent, or (5) any matter as to which the Trustee shall have been finally adjudged in such action, suit or proceeding to be liable for misconduct in the performance of his or her duties as trustee. The indemnification will not be operative for any settlement unless the settlement is approved by a majority of the Trustees appointed or elected.

The foregoing shall not be deemed exclusive of any other rights to which those indemnified may be entitled

POOL ORGANIZATION

a. Board of Directors

The By-laws establish a Board of Directors. Each member municipality elects one person to represent that municipality on the Board of Directors for a term of one (1) year. The member municipality may also select an alternate to serve when the delegate is unable to carry out his or her duties. The delegate and alternate need not be an elected official of the member municipality.

Each member municipality shall be entitled to one (1) vote on the Board of Directors. However, the Pool encourages both the delegate and the alternate to attend all board meetings. A quorum shall consist of a majority of the members of the Board. A simple majority of a quorum shall be sufficient to pass upon all matters, except as provided in Article V (g) of the By-laws. Except as provided in Article V (c) of the By-laws, voting shall be conducted by voice vote.

The Board of Directors elects one (1) of its members to serve as Chairman of the Board, and one (1) members to serve a Vice Chairman of the Board.

The Board of Directors is charged with determining the general policy of the agency. It has responsibility for (inter alia) hiring agency employees and independent contractors; setting fidelity bonding requirements for employees; amending By-laws; acceptance of new members; approval of annual budget; approval of annual and supplemental payments to the loss paying pool, etc. (See Article V of the By-laws).

Regular meetings of the Board must be held at least four (4) times a year—at least two (2) during the first half of the year and at least two (2) during the second half. Special meetings may be called by the Chairman, or by any three (3) directors. Ten (10) days written notice is required. Time, place and date of meetings is determined by the Chairman.

b. Meeting Notices

A Meeting Notice is usually sent ten days to two weeks prior to the meeting for Boards of Directors and Standing Committees that meet on a regular schedule. The Tentative Agenda can be mailed at the same time as the notice, or one week prior to the meeting. An organization's Bylaws or customary practice determines how and when notices of meetings should be prepared and sent. Notices should be in writing and mailed a specified number of days prior to the meeting.

The Meeting notice form may be a letter, memo, or postcard. The notice states the name of the meeting body, the purpose of the meeting, the day, date, time and place of the meeting, and the type of meeting. Procedures listed in the By-laws or developed by tradition should be followed exactly in sending out the notices. Notices of corporate stockholders meetings are sent in a sealed envelope along with a proxy for the use of the stockholder.

If a non-regularly schedules meeting is called, members should be telephoned first, then sent the meeting notice. This alerts other secretaries of the proposed meeting. A list of members will be found in the Board's Organizational File or in the Committee's Master File.

Meeting Notices should be typed on the organization's letterhead except in the case of postcards, which are usually preprinted. Letters or memos regarding meetings are usually signed by the president or chairman. Postcard notices and reply cards are typically viewed as coming from staff.

For a special called meeting, the Meeting Notice is sent according to the By-laws stating the purpose of the meeting and the fact that no other business will be discussed.

Most informal meetings are announced by way of a memo or phone call. Phone calls should be followed-up by a written notice for purpose of documentation.

The master of the Meeting Notice is placed in the Board's Minutes Book and a copy in the Current Meeting File. For a committee meeting, the master of the Meeting Notice is placed in the Master File, and a copy in the Current Meeting File. Documentation of the date the notice was mailed may be important at a later date.

c. Board - Administrator Relationship

The Board of Directors believes that the legislation of policies is a function of the Board and that the execution of the policies should be the function fo the administrators.

While the Board reserves to itself the ultimate decision of all matters concerning policy and expenditures of funds, delegation by the Board of its executive powers to the administrator provides flexibility or the administrator to manage the organization according to the provisions of the Board's policies and decisions, and allows Board members to devote their time to policy making and appraisal functions.

The Board holds the administrator responsible for the implementation of its policies and regulations, the execution of Board actions and decisions, the operation of organization programs and services, and for keeping the Board informed about activities, operations, and concerns. The Board will strive to procure, when a vacancy exists, the best professional leader available for the procure, when a vacancy exists, the best professional leader available for the administrator's position. The Board as a whole, and individual members, will:

1. Give the administrator complete authority for properly discharging all professional and legal responsibilities and duties.

2. Hold all meetings of the Board in the presence of the administrator except when administrator contracts and salary are under consideration.

3. Refer all concerns to the administrator for appropriate investigation and action.

4. Provide adequate safeguards for the administrator and his/her staff members so they can discharge their professional and legal responsibilities and duties.

The administrator will assist the Board in making decisions and establishing policies by giving Board members relevant facts, information, and reports. The administrator may not perform, cause, or allow to be performed any act that is unlawful, in violation of commonly accepted business and professional ethics, in violation of any contracts into which the Board has entered, or in violation of policies and regulations adopted by the Board.

d. Officers

Officers consist of a Risk Manager, a Treasurer and such other officers as may be established by the Board. All officers are appointed by the Board.

The Risk Manager is the chief administrative officer of the Agency and shall supervise and control the day-to-day operations of the Agency and carry out the policy of the Agency as established by the Board of Directors. His duties shall include (inter alia) — the execution of instruments as authorized by the Board; preparation of the annual budget; making recommendations regarding policy, creation of other Agency officers and employment of agents, consultants and contractors; monthly reporting of claims filed and payments made; employment of clerical, secretarial and other similar help; expend funds for administrative expense, and performance of such other duties as may be prescribed by the Board.

The Treasurer has charge and custody of and is responsible for all funds and securities of the Agency. The Treasurer is responsible for investment of the funds of the Agency and for maintenance of financial books and records of the Agency.

e. Committees

The By-laws specifically provide for committees of the Agency, and the workings of such committees constitute an important part of the management of this Agency.

There are six (6) standing committees:

1. Finance Committee;
2. Operations Committee;
3. Policy, Procedures and Administration Committee; and,
4. Membership, Revenue and Audit Committee.
5. Legislative Committee
6. Executive Committee

The Board has adopted a "Statement of Committee Responsibility" for each of the standing committees.

The Chairman of the Board appoints the chairman of each of the first five standing committees. While it is the responsiblity of each committee chairman to recruit the members of his or her committee, the Chairman and the Risk Manager will assist in such recruitment. Pool delegates and alternates are expected to serve in committee work.

Committees will meet as often as necessary during the year.

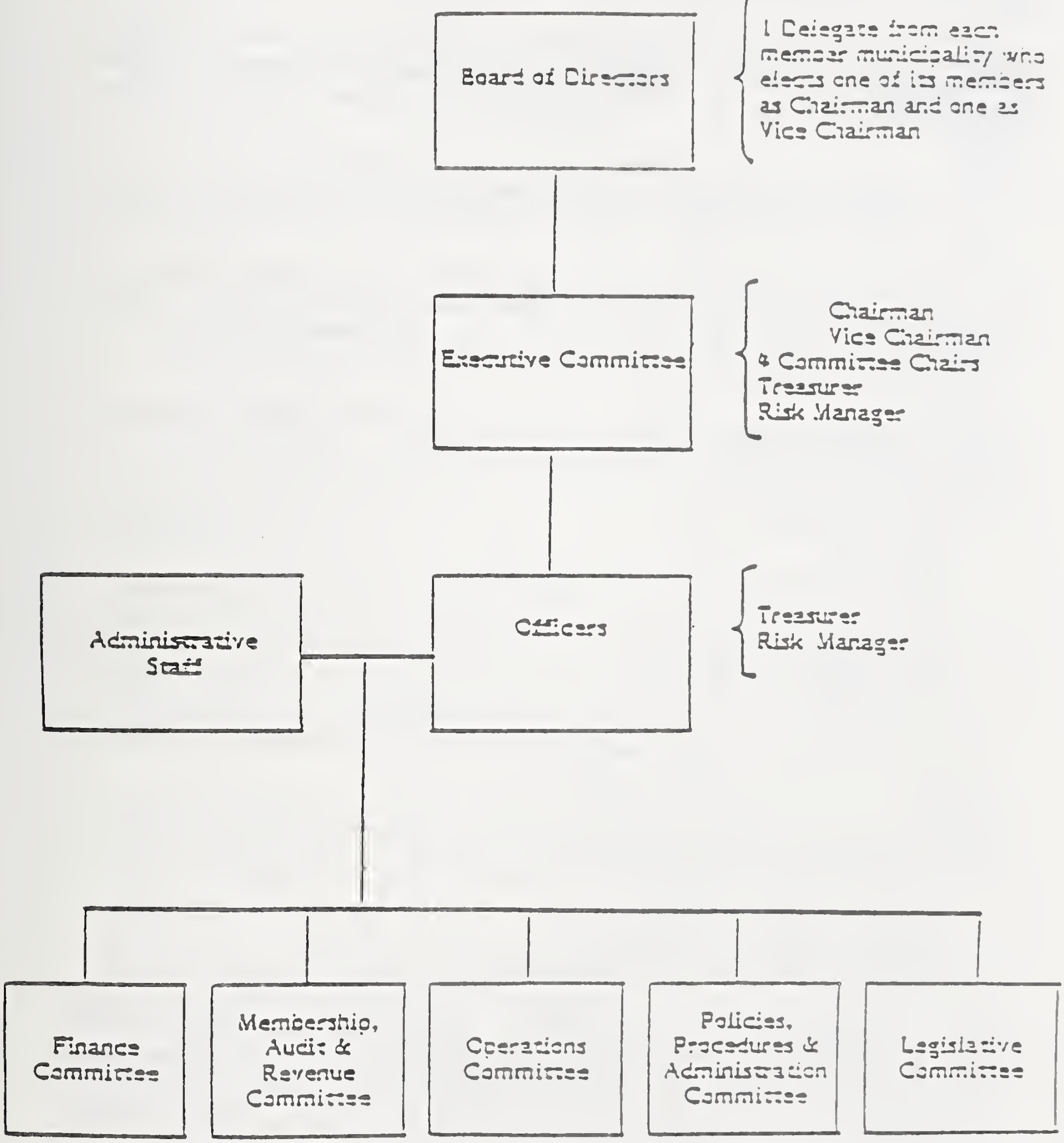
The Executive Committee is made up of the Chairman, Vice Chairman, Treasurer, and the chairman of each of the first five standing committees. The Executive Committee meets on call of the Chairman and generally considers major policy issues between meetings of the full board. The chairman reports on the deliberations of the Executive Committee to the full Board at its next meeting.

In addition, the Chairman may appoint an Ad Hoc Committee to study a particular matter. Such Ad Hoc committees will report to the full Board with recommendations on the particular matter studied.

The Risk Manager usually meets with each committee to give guidance and to answer questions.

Committees are expected to keep records (minutes) of their meetings. The original of such minutes is sent to the Risk Manager for inclusion in the permanent records of the Pool.

f. Pool Organization Chart



g. Budget Process

The By-laws provide that the Board of Directors shall approve a preliminary budget for administration by October 1 of each year. of course, such budget will be for the next fiscal year.

Further, the same section of the By-laws provide that by December 1 of each year the Board shall adopt a final budget and determine the amount of annual contribution to be made by each members and the date upon which the payment is due.

Thus, the preliminary budget is considered by the Board at the September meeting, and the final budget is approved by the Board at the November meeting.

The Risk Manager commences the preparation of the preliminary budget in August of each year for the following fiscal year. By the middle of August, the Risk Manager knows which municipalities will be members during the following year and he has been furnished the revenue base for each such member.

The Risk Manager first estimated the expenditures for the coming year. These expenditures include:

Excess Insurance Premium
Loss Fund
Loss Prevention and claims Handling Service

Legal Fees
Risk Manager's Office
Miscellaneous

Dividing the total of these expenditures by the total revenue base gives a rate per $100 of total revenue base.

The Risk manager recognizes the pool has only three (3) sources of revenue:

Contributions from Members
Interest Income
Application Fees for Membership

The Risk Manager estimates the numbers of applications (at $500 each) which can be expected. He knows that interest income will total about $185,000 for the year. The balance of revenue needed to fund the estimated total expenditures must then come from contributions from members. The amount needed divided by the total revenue base produces a rate per $100 of revenue base.

Prior to the September Board meeting, the Risk Manger would meeting with the Finance Committee. The Finance Committee would prepare the preliminary budget, present it at the September meeting, and move its adoption.

h. Accounting System

The Pool accounts for all revenues and expenses on an accrual basis. This simply means that revenues are recognized when earned and expenses are recognized when incurred, regardless of when the cash is actually received or disbursed.

There are three major monthly tasks associated with the maintenance of the Pool's financial records. These are:

(1) the computation of the monthly loss deductible billings to members and posting of payments received (the timely maintenance of the accounts receivable ledger);

(2) the recording of cash inflows, outflows, and accrued (incurred by not yet paid) expenses; and,

(3) the timely preparation of monthly financial statements.

The first task aries from the agreement of members to pay a $1,000.00 deductible per occurrence. Cumulative payments made on claims are billed to the members up to the $1,000.00 limit. The Risk Manger's office is responsible for determining the amount to be billed the community, and for making any necessary adjustments.

The document used to prepare the monthly deductible billings is the deductible activity report. Increases (billed to members) and decreases (credited to members) for the current month are detailed by claim period and claim number on the deductible activity report. The increases are generally payments made on a particular claim, and credits are generally recoveries (usually subrogation or reimbursements).

The second task is primarily concerned with the preparation of two monthly worksheets — cash receipts and cash disbursements. Cash deposits and transfers to checking, money market and investment accounts are recorded on the cash receipts worksheet. Payments made to those people or organizations who have provided services or goods to and transfers to the claims handling accounts and transfers for investments are recorded on the cash disbursements worksheet. Finally, accrued expenses are accounted for in the general and standard journals. Separate details are maintained on investment transactions and interest income earned on these transactions. The documents used to prepare the monthly worksheets are invoices for services rendered or goods provided, cancelled checks, deposit slips, bank account statements, and computer documents.

The third task is the preparation of the monthly financial statements. Interest income earned in the current month is allocated to each membership year. The account balances from the records are consolidated and presented on the revenue and expense comparisons and the balance sheets.

i. Financial Statements

The Risk Manager's office publishes quarterly financial statements, consisting of:

1. A balance sheet (a listing of assets, liabilities and fund balance as of the last day of March, June, September, and December), and

2. Statement of Revenue and Expense for prior claim years, and

3. Revenue and Expense Comparison for current claim year.

It should be stressed that these quarterly statements are unaudited. The financial statements for March are published at end of May, June statements are published at the end of August, September statements are published at the end of November, and December statements are published at the end of February of the next year.

j. Annual Audit

ARTICLE VIII, section (i) of the By-laws requires that the Board of Directors shall provide to the members an annual audit of the financial affairs to be made by a certified public accountant at the end of each fiscal year in accordance with generally accepted accounting practices. A copy of the annual report must be delivered to the Chief Executive officer of each member. The audited statements and accompanying management letter for prior years have been delivered to each delegate with the specific request that they be delivered to the Chief Executive Officer for that municipality. (The delegate may or may not be the Chief Executive officer).

The 1979 audit report received a "qualified opinion" because the newness of the operation did not provide auditors with sufficient loss data, history and age to allow them to form an opinion as to the adequacy of the loss reserves. The 1980 and 1981 reports were unqualified. The 1982 financial statement received a qualified opinion due only to a change in accounting procedures and resulting non-comparability between years.

The audited reports for each fiscal year clearly show the results fo operations by membership year. If assessments for additional funds are necessary, these assessments will be levied against only those members who had joined as of the membership year requiring additional funding.

k. Banking and Investment

On February 21, 1979, two resolutions were passes by the Board of directors. The first, authorized the creation of a custodial agreement and an investment advisory service with the (Bank). This approved the deposit of moneys into a trust account at the Bank. Upon the direction of the Treasurer, Chairman of the Finance Committee or Chairman of the Board of Directors, the Bank is to make purchases and sales of securities and make transfers into the checking account. The Bank is to reinvest dividends, interest, and other income as directed.

The resolution states that the Bank may invest in:

(1) obligations issued or guaranteed in full by the United States Government;

(2) savings account;

(3) repurchase agreements with financial institutions where such savings accounts, certificates of deposit or repurchase agreements are fully collateralized by securities issued or guaranteed by the United States Government.

In addition to sending a monthly statement of assets to the Chairman of the Board, Chairman of the Finance Committee, and the Treasurer, the Bank is to notify the Treasurer of the maturity of any securities.

Although the Bank may suggest sales, investments, and/or other action with regard to this trust account, the Bank incurs no liability for such advice. For these services, the Bank charges 1/2 of 1% of the market value of the fund at the close of each quarter (March, June, September, December).

21. Loss Prevention

Pool loss prevention services will be contracted on a when-needed basis. This does not mean, however, that the responsibility for loss prevention is not yours. The program is designed so that your own loss costs are reflected in your own risk finance costs - through losses assumed under your deductible and increases (or decreases with good loss experience) in your pool allocation charges. It is therefore in each city's own best interest to control loss in the most cost-effective means possible. If you need help, call the Fund's General Manager. If problems are found to be common to all or most cities, outside counsel may be obtained and paid by the Fund. If a loss control problem is unique to your city, you may be able to reduce losses by an amount greater than the fee you pay outside counsel - contact the Fund's General Manager for assistance.

Inspectors

insurance (excess) inspectors, such as fire protection, safety and boiler - as well as OSHA, other government agencies, or contract loss control engineers - may legitimately visit city facilities. Government inspectors often have legal authority to order changes; insurance and contract inspectors do not - except that boiler (but not fire) inspectors may suspend coverage if a condition is unusually hazardous. Recommendations of fire inspectors which involve spending money should be submitted in writing and channeled through the Fund's General Manager.

Non-government inspectors acting on behalf of or through the Fund will (or should) not inspect your facilities without prior authorization from the Fund; the General Manager will give your advance notice.

Loss Control

From time to time, the Fund will promulgate rules on safety, security of fire protection, and they will appear in the pool manual. However, it is recommended that the Fund's General Manager be contacted first for each new project which either:

1) Involved construction of anew building, addition or substantial remodeling; or

2) Involved installation of or other change in on-site fire protection such as sprinkler systems, fire extinguishers, etc.

APPENDIX I

TRANSIT MUTUAL INSURANCE COMPANY OF WISCONSIN

BUSINESS PLAN

(11/26/85 ARM Tech)

TRANSIT MUTUAL INSURANCE COMPANY OF WISCONSIN
BUSINESS PLAN

The purpose of this document is to outline how Transit Mutual Insurance Company of Wisconsin (TMICW) will operate. The overall goal of the organization is to provide its member policyholders with a source of stable, reasonably priced liability and uninsured motorists insurance. In delivering this insurance protection, TMICW will operate differently than traditional insurers.

The primary difference is that the organization will be run with active involvement of the Board of Directors. All major operating decisions will be made by the Board. Naturally, the organization's elected officers will be the most active Board members and, particularly during TMICW's first few months of operations, will assume many of the day-to-day functions that will ultimately be contracted to one or more contract service providers. Until these providers are engaged, the Board of Directors will actually perform many of the functions that will ultimately be contracted out. The period of transition will be outlined in each of the major functions described in the sections which follow.

During this current period of formation, the group of potential policyholders has elected an interim Board of Directors and three officers: President, Vice President and Secretary/Treasurer. This interim body will govern the affairs of the organization and carry out its business until the permanent Board is elected from those organizations that formally execute the Articles of Incorporation.

GENERAL ADMINISTRATION

To carry out the day-to-day management of the organization and execute the decisions of the Board of Directors, TMICW intends to contract with a qualified individual or firm. The current plan is to have this general administration contract agreed to by February 15, 1986 at which time it will be submitted to the Insurance Department for review and approval. The expected general administration functions to be covered by this contract are outlined in Exhibit 1 appended to this report.

Until the general administration contract is finalized, the Board of Directors will carry out these general administration functions. During this interim period, the major activities and manner in which they will be handled are:

- **Premium Billing and Collection** - Michael Glasheen, TMICW's Secretary/Treasurer, will invoice member policyholders and collect premiums.

- Treasury/Banking - Mr. Glasheen will also open checking and interest bearing accounts in which to deposit premiums collected and from which to pay claims, organization formation expenses and operating expenses.

- Accounting - Nancy Kreutzman, TMICW's President, will set up the organization's books on an interim basis and account for receipts and expenditures. Ms. Kreutzman will prepare interim financial reports for the Insurance Department until such time as the contract general administrator assumes responsibility for this function. State reports will be submitted on the State Insurance Department's quarterly and annual reporting forms.

- Policy/Certificate Issuance - Mr. Glasheen will send an insurance policy to each member policyholder along with the initial premium billing. Mr. Glasheen will also issue certificates of insurance as may be required.

The balance of general administration functions listed on Exhibit I are not expected to require any significant attention prior to the execution of the General Administrator contact. However, if issues in these areas do arise, the organization's President, Nancy Kreutzman, will handle them, call Board meetings or authorize other Board members to address such issues. Because the Board members are already actively involved in insurance and the formation of TMICW, they will be able to handle these matters swiftly and efficiently.

CLAIM HANDLING

Proposals have been solicited and received from two recognized contract claim administrators, GAB and Crawford & Co. The proposals are currently undergoing review by the Board and an organization will be selected on December 4. Following that selection, a contract will be negotiated with the selected vendor and submitted to the Insurance Department for approval by December 18, 1985.

The claim administrator will be formally engaged and authorized to handle member policyholders claims on January 1, 1986. The claim administrator will provide computerized loss experience reports to TMICW and its policyholders. The services of the claim administrator will be professionally audited every two to four years. The results of the claim audit will be made available to the Insurance Department.

SAFETY/LOSS CONTROL

Potential members of TMICW are already actively involved in active programs to prevent automobile liability losses. A safety committee for the group now exists that has a safety awards program to promote safe operating practices among individual drivers as well as all transit systems in general. Currently safety efforts are supplemented by services from Marsh & McLennan, Inc. - the organization's insurance/reinsurance broker - and Sentry Insurance Company - the current provider of phsyical damage insurance coverage.

After the formation of TMICW, the current safety committee and awards programs will continue. If Sentry Insurance Company continues as the physical damage insurer, its services may also continue. Marsh & McLennan will continue as the organization's insurance/reinsurance broker and will provide general support to the safety efforts of member policyholders.

The organization's safety committee may decide that additional safety services are needed to supplement the activities of the safety committee and the services which may or may not be provided by Sentry Insurance Company and Marsh & McLennan. Accordingly, $10,000 has been budgeted to allow for the safety service needs. A determination of the need for services and the selection of any needed safety service provider will be made by July 1, 1986. Copies of any contracts entered into in this regard will be submitted to the Insurance Department for review and approval.

ACTUARIAL SERVICES

By April 15, 1986, TMICW will have solicited actuarial service proposals and retained a qualified firm. The contract for actuarial services will be submitted to the Insurance Department for review and approval.

The actuary is expected to perform the following services:

- Review the organization's loss recordkeeping system and help to establish loss reporting formats that facilitate actuarial analyses, financial reporting requirements and State Insurance Department reporting requirements.

- Review TMICW loss experience and provide estimates of incurred liabilities for 1986 and recommended loss funding levels for 1987.

- Reformat loss information in a fashion that meets State Insurance Department reporting requirements.

- Review TMICW's premium allocation mechanism and suggest refinements that will improve the equity of the plan (this service is optional and requested only if TMICW members feel the current allocation system needs refinement).

The actuarial reports will be provided to the State Insurance Department. Actuarial services will be provided annually.

CPA SERVICES

Annually, TMICW will have its books audited by a Certified Public Accountant qualified to audit insurance companies. Such an organization will be retained by TMICW by no later than April 15, 1986. The negotiated contract will be submitted to the Insurance Department for review and approval.

Services to be performed by the CPA include:

- Review and refine the accounting procedures and methods used by TMICW to assure they facilitate preparation of standard financial reports and State Insurance Department Reports. While the CPA firm will be used to help design an accounting system, they will not do the accounting as this would professionally disqualify them from performing a financial audit at the close of the first year's business operations.

- Perform a financial audit of TMICW's 1986 operations. The audit will be submitted to the State Insurance Department for review.

- Assist in the preparation of quarterly and annual State Insurance Department reports.

CPA and actuarial services will have to be coordinated to produce sound results. Because of the technical nature of these services and the requirement of independence on the part of the CPA firm, it is expected that these services will indefinitely be procured on a contract basis.

FUNDING

The State Insurance Department requires that TMICW establish an account with at least $100,000 on deposit representing TMICW's required minimum Expendable Surplus for 1986. This will be accomplished by having one or more participating policyholders prepaying their insurance premium in December. The deposit premium for Valley Transit in Appleton alone represents sufficient funds to meet this requirement. Further, Appleton has procedures in place that allows it to prepay its insurance premiums in this fashion.

Additionally, it is expected that the claim administration firm will require an escrow deposit from which to pay claims in behalf of TMICW. This escrow deposit will have to be funded by January 1, 1986 to permit settlement of small and non-complex claims. Accordingly, an amount - probably no greater than $10,000 - will have to be received in December and forwarded to the claim administration firm. This will require collecting whatever this amount is in addition to the $100,000 required for expendable surplus.

Many of the participants', whose public entity accounting and funding practices do not permit the prepayment of insurance, premiums will be collected after January 1, but no later than January 15, 1986. Deposit premiums for all 16 participants are listed in Exhibit 2. This money will fund retained losses to TMICW's retained limit of $1 million per occurrence and necessary organizational operating expenses for 1986.

No later than six months following the end of each policy period, TMICW will determine its outstanding liabilities and expenses incurred for the policy year to determine if initial funding is adequate to cover such liabilities and expenses. If additional funds are needed, assessment invoices will be sent to policyholders of the coverage year requiring additional funds and additional monies collected no later than 12½ months after the end of that coverage year. Thereafter, funding nwill be evaluated annually for each coverage year. Assessments will be made pro rata using the deposit premiums as the basis of proration. Each coverage year will be accounted for separately. Further, if any coverage year produces a surplus, monies will be refunded, but no sooner than five years after a policy year has ended or until all claims for a policy year have been settled, whichever shall first occur.

Records of assessments and refunds will be submitted to the Insurance Department. Deposit premiums will be adjusted annually by the Board of Directors to reflect anticipated expenditures for the coverage year then upcoming. A key component of such anticipated expenditures is the estimated loss component, which will be provided by the contract actuarial service firm. Differences in the fashion in which premiums are determined will be filed with the State Insurance Department. Premium rates for 1986 will be filed with the Insurance Department by January 30, 1986. TMICW's President, Nancy Kreutzman, will make this filing.

A pro forma balance sheet as of January 1, 1986 and a pro forma income and expense statement for 1986 are appended in Exhibits 3 and 4.

Exhibit 1

TRANSIT MUTUAL INSURANCE COMPANY OF WISCONSIN

General Administration Functions

Financial and Accounting

- Collect premiums
- Pay expenses
- Invest funds
- Perform accounting
- Obtain CPA and actuarial audits

Underwriting

- Collect exposure data from policyholders
- Review applications from prospective policyholders
- Calculate base premiums and experience factors
- Audit exposures and adjust premiums accordingly
- Issue policies, binders and certificates
- Negotiate reinsurance

General Management

- Obtain claim administration audits
- File reports required by Insurance Department
- Organize material for Board of Directors, Executive Committee and other committee meetings
- Communicate with policyholders on organiztoinal issues and results
- Coordinate claim settlement decisions

Exhibit 2

TRANSIT MUTUAL INSURANCE COMPANY OF WISCONSIN

FINAL PREMIUM ALLOCATION

Property	Miles	Rewards/ Penalties	Total	Comparison 100% Miles	Deviation
Appleton	$108,802	$30,774	$139,577	$139,249	$327
Ashland	$13,650	$1,747	$15,397	$17,469	($2,073)
Beloit	$24,748	$3,167	$27,915	$31,673	($3,758)
Eau Claire	$62,730	$12,123	$74,852	$80,284	($5,431)
Fond du Lac	$27,631	$5,976	$33,607	$35,363	($1,756)
Green Bay	$121,265	$44,232	$165,497	$155,200	$10,297
Janesville	$45,920	$10,285	$56,205	$58,771	($2,565)
Kenosha	$72,205	$13,122	$85,328	$92,411	($7,083)
Manitowoc	$23,823	$7,470	$31,292	$30,489	$803
Merrill	$6,330	$1,701	$8,032	$8,102	($70)
Oshkosh	$58,654	$15,314	$73,968	$75,068	($1,100)
Racine	$131,308	$46,719	$178,027	$168,053	$9,974
Rice Lake	$7,418	$1,899	$9,317	$9,494	($177)
Sheboygan	$81,602	$27,258	$108,860	$104,437	$4,423
Watertown	$10,137	$1,453	$11,590	$12,974	($1,384)
Waukesha	$43,727	$11,808	$55,536	$55,964	($428)
***	$0	$0	$0	$0	$0
@@@	$0	$0	$0	$0	$0
TOTALS	$839,951	$235,049	$1,075,000	$1,075,000	($0)

Exhibit 3

TRANSIT MUTUAL INSURANCE COMPANY OF WISCONSIN

Pro Forma

Balance Sheet
January 1, 1986

Assets	
Cash and Receivables	$1,065,000
Escrow Deposit with Claim Administrator	10,000
	$1,075,000
Liabilities	
Unearned Premium Reserve	$ 975,000
Policyholders' Surplus	
Expendable Surplus	$100,000
TOTAL LIABILITIES AND POLICYHOLDERS' SURPLUS	$1,075,000

TRANSIT MUTUAL INSURANCE COMPANY OF WISCONSIN

Pro Forma Income/Expense Statement
Calendar Year 1986

Income	
Premium	$975,000
Contribution to Expendable Surplus	100,000
TOTAL INCOME	$1,075,000
Expenses	
Incurred Losses	$ 775,000
General Administration	50,000
Claim Administration	50,000
Safety Services	10,000
CPA Services	10,000
Actuarial Services	40,000
Claim Auditor	4,000
Corporate Legal Counsel	6,000
Miscellaneous	30,000
TOTAL EXPENSES	$975,000
Expendable Surplus Allowance	$100,000
TOTAL EXPENDABLE SURPLUS ALLOWANCE AND EXPENSES	$1,075,000

Notes

1. Income and expenses based on participation of current 16 members of Wisconsin Municipal Transit Insurance Commission.

2. Incurred loss estimate assumes retention of $1 million per occurrence and includes a margin for contingencies.

3. No reinsurance expense appears as exhibit contemplates TMICW will issue policy with coverage limit equal to retained $1 million per occurrence.

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