RISK MANAGEMENT – UNFUNDED IMPACTS

Infrastructure & General Government Appropriations Subcommittee 10.20.16

HOW RATES DETERMINED

- Risk Liability Fund premiums/reserves are determined by an independent actuary, and reviewed annually. Actuary determines amount Risk Management needs on reserve at the State Treasurer's Office in order to satisfy actuarial standards. If Risk Management does not maintain adequate reserves, it may become not actuarially sound – similar to a pension fund that has unfunded liabilities.
- Property rates are determined based on building values from a national valuation service (Marshall & Swift) or as reported and reviewed annually by agencies. Agencies add/delete properties each year which can change their premiums. If property claims exceed revenue in any year, there is no reserve fund to draw from.
- Auto rates are very low compared to the private insurance market (i.e. $150/yr per vehicle; $200/yr per bus).
- Risk both self-insures and purchases excess or catastrophic property and liability insurance from the commercial market. Prior to FY17, Risk was able to purchase this excess insurance at fairly flat rates. However, this past June, the excess liability bids came in higher than anticipated with significantly less coverage - based on significant losses the vendors experienced across the country and not specifically based on Utah's claims history. The best deal Risk was able to negotiate was similar coverage, with a higher self-insured retention (deductible) of $2M rather than $1M for approximately $50,000 additional cost to purchase.

RISK'S RATES COMPARISON TO PRIVATE MARKET

- FlatIron consulting compared Risk's rates to the market and Recent outside review of Risk Management's rates compared to the market concluded that "the rates are very competitive compared to the market, the coverage they represent provides broad – in some cases extraordinarily broad – protection, and they are backed by solid financial foundation ... At the same time, pricing for this broad coverage is low to very low compared to the market." (p. 14)

IF RATES NOT FUNDED

- Risk Management is required by statute to maintain the Fund in accordance with economically and actuarially sound principles.
- If Risk's rates are not fully funded or Risk has to borrow from funds on reserve at the Treasurer's Office, the liability fund may become not actuarially sound; Property fund may not have sufficient funds to pay claims.
- Federal regulations require premiums for each of Risk's customers to be charged equitably relative to others in the pool. This means that Risk cannot give a break to those that didn't receive sufficient funding while requiring the others to pay the full premium.
- If Risk's retained earnings go too far into the red, the federal government could disallow the ISF from receiving funding from federal sources and pay back a penalty.
- Because of the budget cycle, it will take 2 fiscal years for the increased premiums to go into effect to make up the shortfall.
- If Risk has insufficient funds, it may not be able to afford excess insurance. The choice to the State would then be to 1) self-insure all of its risks; 2) buy less coverage; 3) choose to leave some buildings uninsured; 4) direct Risk to cut back on the coverage it currently provides; or 5) some combination of the above.

CONCLUSION

Risk recommends that the Legislature fully fund Risk's premiums or direct Risk where to cut back on its coverage.