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RISK REPORT: Public Entity Risk Everybody Into the Pool

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Supporters of pooling mechanisms to buy insurance say they've been one of the insurance industry's big success stories.

BY SUSAN GUREVITZ

Once upon a time, from the mid-1970s through the early 1980s, there was a hard insurance market, with high prices and limited availability of liability coverage. It was a difficult era for colleges and universities looking to insure their risks. They were at the mercy of prices over which they had no control.

"We had to take control of our own destiny," explains Roger Fell, client executive of Marsh Inc.'s Philadelphia office. The market presented short-term challenges but long-term opportunities. Then the federal and state governments entered the picture to help with the critical hard-market situation, passing specialized legislation that enabled public entities and colleges and universities to form insurance pools to spread the risk and reduce their insurance costs. And, thus, a new strategy was born.

As with all cycles, that particularly hard market cultivated a concept for dealing with the difficulties of obtaining insurance. Pools, as lobbying groups and in different forms and structures, have been around since the late 1800s, but didn't really take off until legislation allowed two or more entities to form a partnership for buying insurance products.

As such, pools offer members the opportunity to reduce their insurance costs while advancing better loss-control measures and policies. Public entities, such as municipalities, school districts and related departments, were among the earliest industries to embrace the pool strategy, followed by the typically independent colleges and universities, which saw the benefits too.

Today, there are more than 480 public-entity pools and dozens of university pools. They tend to be

homogeneous—operated by all colleges or all specific types of public entities so their liabilities and exposures are similar. "Pools are one of the biggest success stories in insurance in the past 50 years," says Rich Terlecki, area senior vice president and co-managing director of Arthur J. Gallagher & Co.'s public-entity pooling niche.

Pools come in different shapes, sizes and concepts, but all offer a method for spreading the members' risk and act as insurance companies, except they're owned by the members. Captives are a version of pools, capitalizing the entity, sometimes forming a trust, and retaining enough premium income to pay out claims or secure coverages through the reinsurance market. They usually have members throughout the country. Risk retention groups are self-insurance vehicles, set up by federal legislation in 1981 to address the prohibition by most states of groups banding together to buy liability coverage. Risk retention groups may not be subject to state laws as are most pools. Some pools are just set up as purchasing groups, usually offering several lines of coverages, such as auto and general liability. Some are created to address just one risk, such as workers' comp.

Genesis Ltd., which is celebrating its 27th anniversary this year, is one of the older higher-education pools. A group of blue-ribbon colleges and universities, it's domiciled in Bermuda as a Class-3 reinsurance company and offers its 16 members, all shareholders of the corporation, general liability products and automobile liability. (See chart below). At one point it also offered property and workers' comp but deleted those services early on. Due to the power of group purchasing, which puts the pool into a better negotiating position, "we get extremely competitive pricing," says Marsh's Fell, who's also the administrator for Genesis. As with most pools, premium income is invested, and any surplus funds that aren't earmarked for claims are returned to the members in the form of dividends.

Fell points out that, because of the nature of the pool, which includes professional schools and other specific departments and risks, policies purchased are crafted for the universities and aren't "off the shelf." Thus, Genesis enjoys a 15 percent to 50 percent savings on its coverages and 50 percent off the list price of its environmental insurance.

"It's like retail pricing," says Fell, something akin to paying T.J. Maxx prices instead of Saks Fifth Avenue prices for the same designer clothing. "Carriers like to write a lot of risk at once because it's more cost-efficient and the acquisition costs are less," he says. He points out that Genesis is a desirable account too. "It all adds up to a healthy long-term business relationship and cost-effective risk transfer."

But not all risks are created equal, nor are they all easily identified. As enterprise risk management, or ERM, has swept the corporate landscape, how to deal with ERM is probably the newest development colleges and universities are confronting these days.

"It's an issue that many schools are grappling with," says Fell. Individual schools are listing all their risks

and setting priorities, such as the risk management of facilities, human resources, finance and technology transfer. Fell believes reputation risk is the most important aspect of ERM for these universities. And it will continue to be an important issue.

Unlike Genesis, the New York State College and University Trust offers its 30 members only workers' comp coverage. Most of the schools are located in the northern part of the state—in the Syracuse, Rochester, Buffalo region—with some located in New York City. There are small schools, like Union College, through to the largest member, Ithaca College with 6,000 students. The pool began in 1994 with a combined \$82 million in payroll for the group, which has since grown to more than \$1 billion in payroll.

"We take all schools with similar risk with good experience," explains Ted Coviello, risk manager at St. Lawrence University and vice-chairman of the pool. Schools have to maintain their risk levels or could be tossed out of the pool. "Their experience mod factor must be one or below," he says. Experience mod is a calculation based upon the number of claims and severity of the claims over a set period of time. It also dictates the size of a member's premium.

Not just any school can apply to join the trust. Member schools must meet certain criteria. They must undergo a loss-control survey, have a written safety program and be committed to loss prevention as basic requirements. For the past year or so, the trust had considered augmenting its services and creating a purchasing group for property/casualty insurance, specifically for the purchase of auto, liability and umbrella coverage. However, now that the property/casualty market has gone soft, "we've decided to delay it for six months until renewals," says Coviello. "It's not quite as attractive now."

Besides, the schools aren't exactly complaining about their property/casualty costs because "the schools are very good at keeping a handle on claims." The pool's claims are handled according to a loss-sharing formula, based upon the size of the claim.

"All of the members are responsible for paying the claims, which is why loss control is such a critical factor," Coviello says.

Losses are not the only attention-getter at the trust. What has grabbed the group's focus these days are the new workers' comp laws proposed by New York's new governor, Eliot Spitzer, and recently passed by the state legislature. Although it's still too soon to anticipate how the new laws might affect the trust, the governor does predict that employers' costs will be reduced by at least 10 percent to 15 percent.

"It's a fairly significant proposal, but we don't yet know what the impact will be on the entire group," Coviello says.

That's also the case for public-entity pools, which Harold Pumford calls "local government at its finest."

Pumford is chief executive of the Association of Governmental Risk Pools, otherwise known as AGRiP. Public-entity pools have become very popular in recent years as an attractive alternative to the open market. According to a recent survey of AGRiP's members, probably more than 74,000, or 85 percent of all public entities, are involved with pools. Annual member contributions total \$5 billion to \$7 billion for property/casualty pools, and benefits run between \$8 billion to \$10 billion. Pumford estimates that the total assets managed by public-entity pools range from \$50 billion up to \$75 billion.

Pools encompass the spectrum of public-entity organizations, including state agencies; higher and public education; all forms of local governments (cities, towns, townships, boroughs, counties and parishes); and a vast array of "governmental" special districts such as health-care facilities and not-for-profit organizations. They tend to focus upon specific types of risks so "they develop the expertise in managing risk and communicating it to their members," Pumford says.

Typically pools offer property coverage, liability, workers' comp and employee benefits. No two pools are alike, Pumford points out. Some pools require members to participate in more than one product line. Cities/towns and school districts are the most common types of pools.

During the Katrina disaster, 80 percent of all pools in the New Orleans area sustained losses, including a pool office itself and the pool executive's home. In fact, since the controversy over the lack of drivers for the school buses that were supposed to evacuate people from New Orleans, the pools are now brokering mutual agreements with bus drivers in the northern part of the state to pick up the slack should their New Orleans' neighbors need to be evacuated again.

In addition, pool members are now focusing upon developing online training resources for their memberships, expanding beyond compliance training and offering information on risk management issues. And Pumford believes pools are doing a better job of correlating contributions with actual exposures.

"There's more reward to those that do well and higher costs to those who have more claims," he says.

Thus, as our story ends, everyone lived happily ever after, depending upon how many claims they have, of course.

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