Positively SIIA...Positively Connected
Connecting the Self-Insurance Industry for Positive Risk Solutions

The Essential Trustee
Trustee Training 101
Trustee Responsibilities

Learning Objectives

• Overview of group self insurance
• Causes of self insurance group failures
• Fiduciary responsibilities
• Plan administrator and vendor management
• Financial statements
• Fund management strategy
Group self insurance:
an organization of businesses joined together for
the common purpose of providing cost-effective,
stable workers’ compensation coverage to its
members
Homogeneous Self Insurance Group: an organization of businesses of a single industry or closely related industries; an example would be a home builders’ self insurance group composed of construction and other artisan contractors that specialize in the building of single or multi-family dwellings.

Heterogeneous Self Insurance Group: an organization of businesses of multiple industries.
A self insurance group....

- Establishes its own service contracts with third party administrators (TPAs), financial auditors, investment advisors and other vendors.

- Performs basic functions for the members.
  - Issues policies
  - Pays losses
  - Manages funds/investments

- Purchases excess insurance coverage to financially protect the group on a specific and/or aggregate basis.

- May refund surplus to the members based upon the group’s by-laws and membership documents and in accordance with state regulations.
Why choose group self insurance?

- Lower up-front premiums
- Surplus distributions
- Access to industry specific loss control services
- Stability through marketplace cycles
- Access to best practice claims management
- More control overall
Why Have Groups Failed?

Failure of Groups in NY and California

- 8 “Trusts” managed by the same administrator closed down by regulators in NY in 2008 – administrator’s license revoked in NY, leaving behind a deficit of $500 million.

- Administrator permitted to continue to operate groups in CA
Why Have Groups Failed?

Failure of Groups in NY and California

“Fatal” flaws:

- Conflicts of interest - group administrators and TPAs seeking to grow the business by keeping rates artificially low and understating losses;

- Inability of the state to monitor and assess the true status of each operating trust;

- Trustees not understanding what is really going on with their program;

- Inability to collect on “Joint and Several” Liability.
Why Have Groups Failed?

Failure of Groups in NY and California

- Principal Issues
  - Rogue, perhaps even felonious, management
    - Where was Board/Trustee oversight?
  - Trustees not relying on annual actuarial review and audited financial statements.
  - Inadequate state oversight
    - Failed to see problem until too late
    - Took wrong steps to address (assessing all members in all groups) causing downward spiral

**Bottom Line – Trustees have a responsibility to understand and manage their program**
Fiduciary Responsibility

What constitutes fiduciary responsibility?

As a trustee, you must focus exclusively on the best interest of the fund. For example, when voting on the need to raise the premium rates offered by the group self insurance fund, you cannot consider the negative impact the rate increase will have on your own company.
Fiduciary responsibilities may include:

• Finding and understanding any potential conflicts of interest.
• Eliminating members who exert a negative influence on the fund.
• Overseeing investments and distributions.
• Obtaining dependable financial procedure audit opinions.
• Obtaining dependable actuarial rate and reserve analyses.
• Above all, making sure the fund is financially solvent and in compliance with all state regulations.
Fiduciary Responsibility

Group self insurance bylaws may include:

• How and when meetings are held
• Who is eligible to participate in the fund
• Voting rules
• Details on banking and investments
Fiduciary Responsibility

Issues and voting responsibilities

- Vendor contracts and management
- Claim settlement offers
- Regulatory compliance verifications
- Surplus distribution
- Excess insurance policies
- Rate levels
- Incurred But Not Reported (IBNR) loss provisions
Plan Administrator & Vendor Management

Administrative services managed by Trustees

- Association sponsors
- Plan administrators
- Third party administrator
- Loss control service provider
- Excess insurance carrier
- Business services
  - Accounting
  - Actuarial
  - Investment advisor
  - Bonding
  - Executive liability insurance
- Sales or marketing
Plan Administrator & Vendor Management

Association Sponsor

- Often required by state rules for homogeneous funds
- Can be an industry, trade, or professional organization
- Fund may have several association sponsors

Plan Administrator

- Hired by the board of trustees
- Carries out established board policies
- Provides consultation to the trustees
- Manages day-to-day fund operations
Plan Administrator & Vendor Management

Third party administrator

• Administrates and adjudicates the fund’s claims
• May provide other services such as loss control

Loss control services

• Develops safety plan for the group
• Provides training for fund members
• Industry specific
Excess insurance

- Provides financial protection for the fund
- May be subject to state regulation
- Carrier should be financially strong
- Protection from long-tail workers compensation claims
- Typically written on reimbursement basis
- Good record keeping essential
Plan Administrator & Vendor Management

Business services

• Accounting
  o Financial audit
  o Tax service
  o Annual reports
  o Preparation of audited financial statements

• Actuarial services
  o Reviews losses and reserves
  o Advises on reserve adequacy
  o Determines level of funding required for solvency
  o Assists in determining rate appropriateness
Business services (con’t)

• Investment advisor
  o Manage and protect assets
  o Maximize investment returns
  o Maintains portfolio in accordance with state regulations and guidelines

• Bonding
  o Covers individual members (policyholders)
  o Protects against fraudulent acts of individuals
  o Typically required by state
Plan Administrator & Vendor Management

Business services – executive professional liability

- Directors and officers (D&O)
  - Coverage written for trustees
  - Designed as management errors and omissions coverage
  - Defends claims of adverse financial consequences as a result of managerial decisions

- Errors and omissions (E&O)
  - Coverage written for professional advice and service individuals or companies
  - Protects against claims of negligence or inadequate work
Plan Administrator & Vendor Management

Sales/Marketing

- Board of trustees determines strategy
- Attract new members
- Retain current members
- Options
  - Direct marketing
  - Exclusive agent or broker
  - Open network
Information from financial statements

- “Income”
- Member distributions
- Operating expenses
- Assets
- Liabilities
- Fund reserves
- Total member equity/dividends payable
Self Insurance Group differences

- Can not close a fiscal year until all claims closed
- Loss reserves are estimates
- Workers Compensation is a ‘long tail’ line
Financial Statements

Balance sheet

- **Assets**
  - Cash
  - Reinsurance recoverable
  - Premium receivable
- **Liabilities**
  - Losses and loss adjustment expenses
  - Accrued expenses and other payables
- **Surplus/member’s equity/policyholders’ dividends payable**

Income statement

- **Revenues/Expenses**
- **Excess revenues (expenses)**
- **Federal income tax provision (credit)**
Frequently asked questions

Q. What happens if revenues exceed operating expenses?
A. If revenues exceed operating expenses, members can receive dividends.

Q. What happens if expenses exceed revenues?
A. Members face an assessment to bring the fund back to solvency.

Q. Are group self insurance funds considered taxable?
A. The answer can vary depending on how the group is structured and operates, along with state regulatory requirements.

Q. How long can workers compensation claims take to pay out?
A. Long tail payouts can take as long as 50 years.
Fund Management Strategies

Long Term Stability

VS.

Short Term Gain
Insurance cycle:
The terms “hard market” and “soft market” are used to describe favorable or unfavorable buying conditions for the insurance consumer.
Fund Management Strategies

**Soft market conditions**
- Profits down
- Rates low
- Intense price competition
- High limits with large capacity
- Flexible contracts

**Hard market conditions**
- Increased profits
- High rates
- Low limits
- Restricted coverage
Areas of responsibility for goal setting by Trustees:

• Underwriting
• Loss prevention
• Claims administration
Fund Management Strategies

Underwriting Strategy

• Inclusive
  o Allows higher loss ratios
  o Likely to result in higher losses
  o Premiums remain higher in soft market
  o Effective loss control can lower losses

• Exclusive
  o Focuses on “best in class”
  o Will eliminate potential participants
  o Losses generally low
  o Rates remain competitive in soft market
Loss Prevention Strategy

- **Proactive**
  - Costs more on front end
  - Reduces losses and total claims costs
  - Service tailored to specific industry
  - Requirement for membership

- **Reactive**
  - Assumes ‘bad’ loss ratios will continue
  - Service directed at high loss ratio members
  - Can miss defects of members not ‘serviced’
Fund Management Strategies

Claims Administration Strategy

- **Aggressive**
  - Early detection
  - Accident investigation
  - Strong medical case management
  - Transitional duty
  - Prompt dispute resolution
  - Appropriate settlements

- **Passive**
  - Undefined reporting procedures
  - Slow dispute resolution
  - Lack of direction on medical providers
  - Reluctance to settle claims
The bottom line: Successful groups are those that thrive in both hard *and* soft markets because they have LOYAL members.
To summarize:

• A self insurance group allows like-minded businesses to pool their premiums to pay workers compensation losses of its members.

• Trustees have a *fiduciary responsibility* to make decisions based on the interest of the group without regard to personal impact.

• Administrative and business functions of the group are under the direction of the group’s Trustees.

• In order to make sound financial decisions, Trustees must understand the group’s financial statements.

• Groups should be managed to provide long term stability for the members rather than short term gains.