

CALIFORNIA JPIA

AGENDA ITEM

To: EXECUTIVE COMMITTEE

From: Jonathan Shull, Chief Executive Officer

Date: March 24, 2010

Subject: Recommendations of the Formula Review Ad Hoc Committee

At its meeting of February 24, 2010, the Executive Committee considered the recommendations of the Formula Review Ad Hoc Committee regarding suggested modifications to the Authority's funding model. Significant member input was received on the item, and the Executive Committee postponed action on the item until further meetings could be held to allow the members to gain a greater understanding of the proposed modifications. A copy of the February 24 Executive Committee report is attached as Exhibit 1.

Subsequent to the informational meetings, the ad hoc committee met once again to consider the input received from the members since its recommendations had been presented. This report presents the ad hoc committee's recommendations concerning the issues raised by the members as well as its recommendations regarding modification to the funding model.

Summary of Ad Hoc Committee's Recommendations

Increased losses incurred by the members over the past several years combined with the limitations in the primary deposit formula have placed the Authority in the unsustainable position of creditor to the members as significant long-term retrospective deposits are receivable from the members.

The Formula Review Ad Hoc Committee recommends that the Authority move away from this creditor role by transitioning from a retrospective funding model to a prospective funding model in which each coverage period is sufficiently pre-funded to cover all of the costs associated with providing protection to the members. Additionally, variable credibility weighting should be utilized to properly rate members based upon their relative size.

Consideration of Member Input

Several meetings were held over the past month to review the recommendations of the ad hoc committee and to garner input from the members regarding the proposed funding model. In

these meetings and through other discussions, the members have been able to gain a better understanding of the challenges facing the Authority and how the proposed model is intended to address the challenges. A number of suggestions have been made and issues have been raised during the meetings pertaining to the impact of the recommendations.

Many of the questions raised were previously considered by the ad hoc committee. Additional questions have since been addressed by staff. A number of questions or suggestions are policy issues that need to be addressed by the Executive Committee. The ad hoc committee met on March 16 to consider these policy issues and to develop recommendations for presentation to the Executive Committee.

Following are the policy issues considered by the ad hoc committee, its analysis, and its recommendations to the Executive Committee:

1. *Issue:* Implementation of the old formula would have generated \$4 million more than would be collected under the proposed formula. Should the funding levels be increased to collect \$4 million more through the proposed formula?

Analysis: The ad hoc committee focused on long-term solutions while being mindful of the impact to members. The primary goal was to fund upcoming coverage periods at higher confidence levels, and the proposed funding formula achieves that when compared to the current funding model. As can be seen from the “Cash Basis Cost of Coverage” (Exhibit 2), the lower cash collection is due to the suspension of the collection of retrospective receivables, and was a conscious decision in recognition of the current economic conditions. Also in recognition of the economy, the proposed liability formula changes are being managed such that the average increases do not exceed 10% in any one year during the transition period.

Under the proposed model with volatility limits of 0-35%, and an aggregate year-over-year change limited to 10%, the members in the liability program would see year-over-year adjustments as depicted in Column A of the following chart.

By increasing the funding target to the amount that would have been generated by the old formula, the aggregate year-over-year change is approximately 15%, , the year-over-year adjustment distribution would be shifted upward as more members would reach the 35% level as shown below in Column B.

By increasing the top end of the volatility band to 40%, while also increasing the funding target to the amount that would have been collected, again the year-over-year adjustment distribution is shifted upward, and now many members reach the 40% level as shown below in Column C.

Liability Program Year-Over-Year Volatility in Annual Contribution Comparing Old Formula to Proposed Formula			
	A	B	C
	Proposed Funding Target 10% Aggregate YOY, 0-35% Volatility Limits	Increased Funding Target 14% Aggregate YOY, 0-35% Volatility Limits	Increased Funding Target 14% Aggregate YOY, 0-40% Volatility Limits
Member Count	122	122	122
= 0	53	35	41
>0%	69	87	81
>5%	64	81	76
>10%	59	76	72
>15%	53	71	68
>20%	50	68	63
>25%	45	64	58
>30%	42	59	52
=35%	40	54	49
=40%	0	0	46

The workers' compensation program experiences similar impacts associated with collecting the additional funds.

Recommendation: Based upon its analysis and the reasoning behind the establishment of the 10% year-over-year limit and the 0-35% volatility limits, no change is recommended.

2. *Issue:* Should the liability and workers' compensation program retrospective balances be aggregated?

Analysis: This issue arose because retrospective balances are calculated separately for liability and workers' compensation, and it is possible for a member to have a retrospective deposit due in liability, yet have a refund in workers' compensation. Because the programs are separate from one another, the ad hoc committee recommended the funds not be aggregated and thus comingled. In addition, the committee has recommended refunds continue to be provided to the members, and aggregating the balances could have a budgetary impact on members that were counting on refunds. Finally, accelerating claim payments, benefit increases for injured workers, and increased actuarial funding estimates indicate a need for additional funding of the workers' compensation program. The credit balances many members are enjoying in the workers' compensation program are likely to be needed in the next several years to counteract the increased funding requirements.

Recommendation: No change is recommended

3. *Issue:* Should the pool continue to provide refunds to the members?

Analysis: Due to the poor economy, many members are anticipating the refunds that have been indicated in the retrospective computation spreadsheets approved by the Executive Committee in February. The committee also felt positive loss control efforts should continue to be recognized through the delivery of refunds.

Recommendation: The ad hoc committee recommends the pool distribute refunds to the members this year as planned. The committee also recommends that the decision regarding refunds be made annually in conjunction with the retrospective calculations. Finally, the committee recommends the amount of the refund (1/4, 1/8, etc.) also be determined annually.

4. *Issue:* Should there be a discount and/or refund to members with no losses?

Analysis: The introduction of variable credibility weighting makes the cost of coverage for smaller members less responsive to their experience than it was under the old formula. Some of these members have expressed interest in some mechanism that recognizes those that have experienced no losses over an extended period of time. The ad hoc committee was intrigued with the idea, and felt it worthy of additional exploration. The committee expressed a desire to recognize an agency with no losses as they received a discount under the old formula. Approximately 15 smaller members have had no claims for a five-year period. The total cost associated with giving a discount or refund to agencies with no losses is estimated to be less than \$300,000 overall. The committee also suggested that staff explore linking refunds to subjective measures, such as compliance with LossCAP recommendations, implementing policies and procedures, usage of training resources, etc.

Recommendation: The ad hoc committee felt staff should explore the concept with the goal of implementing something by the 2011-2012 coverage period.

5. *Issue:* Should former pool members be invoiced the entire amount of their retrospective deposit due?

Analysis: The committee recommended members pay their entire retrospective deposit when withdrawing from the pool. Such members would not benefit from the deferral of retrospective payments or be billed installments under some sort of payment plan. The purpose of addressing this issue is to treat former members the same as members that may elect to withdraw in the future.

Since 1978, five members have left the pool. Vernon left the pool after three years of membership and does not have a retrospective balance. The pool owes La Mesa \$16,771, while the other three former members owe the pool: San Juan Capistrano (left the workers' compensation program) - \$21,150, Victorville - \$127,610, and Laguna Hills - \$51.

Recommendation: The committee recommends former members be invoiced for the entire amount of their retrospective deposit due. The committee also recommends that a value be assigned to the coverage periods in which each former member participated, and those periods be administratively closed for the former members. They also suggested requests for payment plans by the former members be considered if necessary.

6. *Issue:* Should there be interest charged on the retrospective adjustments?

Analysis: Historically, there was no need for the Authority to charge interest to members on retrospective balances because on a pool-wide basis, the total retrospective receivable was relatively small. This meant that the Authority's opportunity cost for not having the use of this capital was also small, and was typically off-set by the value gained from the use of capital associated with refunds which were due to members. Under this set of circumstances, the interest that would have been collected, and the interest that would have been paid out, generally negated one another.

For many agencies, a similar dynamic occurred at the individual member level. When the four-year rolling retro was introduced in 1997, outstanding deposits applicable to certain coverage years were off-set by outstanding refunds in other years. A key factor facilitating this process was that the amount of refunds was similar to the amount of the additional deposits due. As such, this was an effective mechanism for cash-flow smoothing for a number of years until very recently when retrospective deposits began to grow exponentially, driven by the underlying claims activity.

As of today within the liability program, the pool-wide aggregate retrospective receivable is \$75.7 million, while the pool-wide aggregate retrospective payable (refunds due to members) is only \$318,013. The receivable is no longer off-set by the payable, and it is possible that it will continue to grow larger over the next few years until the new annual contribution reaches target funding levels. This prospect coupled with a long-term re-payment plan that could span over 10 years, introduces two primary concerns (1) the Authority's lost interest income is now reaching significant levels, and (2) the lack of relative fairness between members benefiting from large "no interest" loans vs. those benefiting to a much lesser degree from small "no interest" loans vs. those members having no "loans" whatsoever.

Charging interest is one way to effectively address both concerns. In addition, it provides an incentive for members to shorten the duration of their retrospective deposit financing by repaying the Authority any outstanding deposits due ahead of schedule.

In recognition of the difficult economic environment, the ad hoc committee recommends that no interest be charged to members during the transition period over the next three to five years; however, once target funding levels have been reached in each program separately, and payments on aggregate retrospective balances resume, at that time it is recommended that interest fees begin to accrue.

Recommendation: The ad hoc committee recommends that the Authority charge interest to members on retrospective deposit balances once each program completes its transition period. Similarly, if there are refunds due to members, the Authority should pay interest on any refunds due. It is also recommended that staff develop specific plans regarding the calculation of interest and how this process would be applied.

In addition to addressing the issues raised by the members, the ad hoc committee provided guidance on other issues pertaining to the implementation of the new funding model. That guidance is captured in Frequently Asked Questions (FAQs) attached as Exhibit 3.

Recommended Action

It is recommended that the Executive Committee consider the recommendations of the ad hoc committee in regard to the issues raised by the membership in the last several weeks and adopt or modify the proposed funding model as summarized below and in the FAQs.

- Transition from a retrospective funding model to a prospective funding model.
- Adequately pre-fund each year with an annual contribution that is computed at the 75% confidence level.
 - Phase-in the 75% confidence level funding to prevent an extraordinary initial increase.
 - Base annual contribution on individual members' experience and exposure with these elements variably weighted based upon the credibility of the past loss experience in predicting future loss experience for a member.
 - Proceed toward elimination of the retrospective computation for those coverage periods subsequent to the transition period.
- Defer payment of retrospective receivables until annual contribution grows to the 75% confidence level.
 - Once the annual contribution is funded at the 75% confidence level, compute outstanding member liabilities, and commence collection of retrospective receivables.
 - Withdrawing members would not be eligible for deferral of payments nor the benefit of the rolling retro's installment mechanism.
- Base new funding model on historical cost allocation methodologies for continuity.
 - Police and non-police exposures calculated separately (liability program).
 - Loss layers \$0 - \$30,000 and \$30,000 - \$750,000 to be maintained in allocation formula (liability program).
 - Public safety and non-public safety exposures calculated separately (workers' compensation program).
 - Loss layers \$0 - \$50,000 and \$50,000 - \$100,000 to be maintained in allocation formula (workers' compensation program).
 - Experience of past five coverage periods used to measure experience.

- Limit year-to-year changes in annual contribution compared to prior year's primary and retro deposits to 0%-35% in the first year; annually review appropriate year-to-year limitations.
- Evaluate losses six months after the end of the coverage period to allow for additional claims maturation prior to application of formulas. Transition years and all prior years would be evaluated as of the last day of the coverage period.
- Discontinue special treatment of "property damage only" claims and automatic reserving of "slip and trip" claims.
- Waive the one-year membership withdrawal notice provision for members that joined the pool after July 1, 2007, in the event the member wishes to withdraw from the pool at the end of the 2009-2010 coverage period.
- Invoice members that elect to withdraw for the full amount of any retrospective deposits due, and make the entire amount due and payable upon withdrawal. Invoice former members for the full amount of any retrospective deposits payable.

Exhibit 1

Executive Committee Report of February 24, 2010 Regarding Recommendations of the Formula Review Ad Hoc Committee (Excludes FAQs that have been Revised in the Current Staff Report)

CALIFORNIA JPIA

AGENDA ITEM

To: EXECUTIVE COMMITTEE

From: Jonathan Shull, Chief Executive Officer

Date: February 24, 2010

Subject: Recommendations of the Formula Review Ad Hoc Committee

The Executive Committee directed the formation of an ad hoc committee of managers and finance officers to study the Authority's various funding and allocation formulas and to provide recommendations regarding suggested modifications. This report represents the result of the ad hoc committee's efforts.

Summary of Ad Hoc Committee's Findings and Recommendations

Increased losses incurred by the members over the past several years combined with the limitations in the primary deposit formula have placed the Authority in the role of creditor to the members as significant long-term retrospective deposits are receivable from the members.

The Formula Review Ad Hoc Committee recommends that the Authority move away from this creditor role by transitioning from a retrospective funding model to a prospective funding model in which each coverage period is sufficiently pre-funded to cover all of the costs associated with providing protection to the members.

Background

The Authority was formed in the late 1970s as a self-insurance pool designed with the principles of providing broad coverage at fair and stable rates, and with the security that the protection would be available over the long term.

Guiding Principles

The formulas employed in 1978 to share risks and allocate costs were based upon these guiding principles, and they have continued to guide the Authority as the formulas have been modified over the years. Those guiding principles stated in today's terms are as follows.

Overall Financial Strength and Security—In order to provide broad and stable protection for members over the long term, the Authority should have sufficient assets to pay today's obligations over the long run, and to build net assets, consistent with industry benchmarks, to provide protection from adverse developments.

Rate Stability and Fairness—In order to promote budgetary predictability for members and fairness within the rate structure, rates should reflect the experience and exposures of the individual members. More predictable losses should be retained, and more unpredictable, catastrophic losses should be tempered through risk sharing across the membership. Efforts should be made to avoid the creation of subsidies across divergent member types.

Simplicity—The financial formulas and processes should be understandable and explainable such that members can realize the efforts of their good risk management practices in the rate structure.

Cost Allocation

Under the current funding model, a primary deposit is contributed at the beginning of the coverage period, and retrospective adjustments are made subsequent to the coverage period to reconcile each member's share of costs based upon their actual experience and exposure. Over the years the funding model has been modified by the membership to reduce the year-to-year volatility of the annual cost of coverage for individual members. These modifications have included the implementation of the "rolling retro" and the introduction of primary deposit limitations.

Unfortunately, the loss experience of the members over the past few years has exposed some of the shortcomings of these modifications in regard to the long-term fiscal security of the Authority. Catastrophic losses and the general increase in frequency of mid-level losses incurred by the members have led to the insufficient contribution of the primary deposits within the constraints of the current funding model.

The Authority's reserves are used to pay for claims and lawsuits. When the cost of losses paid exceeds the amounts previously contributed by the members through the primary deposit, the Authority's investment portfolio is reduced until these funds are replaced through retrospective deposits. In other words, the costs not borne by the primary deposit are shifted to the retrospective deposit. The rolling retro provides payment of retrospective deposits in installments over an eight-year billing period. As such, the recent catastrophic losses that have been paid from the investment portfolio will not be fully recovered through the rolling retro until eight years after the coverage period in which they were recognized. This installment payment plan is akin to a revolving credit account in which the Authority acts in the role of creditor to the members.

Ad Hoc Committee's Analysis

The ad hoc committee created by the Executive Committee was composed of the Chair and Vice Chair of the Managers and Finance Officers Committees, as well as a number of other representatives of the Committees. Supporting the committee's efforts were several members of staff and actuarial and insurance consultants from Towers Watson (formerly Towers Perrin).

The committee began its work by affirming the guiding principles of financial security of the Authority, stability of year-to-year costs for members, fairness among member types, and simplicity and understandability of the funding model. The committee then assessed the Authority's current financial situation in relation to these guiding principles.

While the Authority has sufficient net assets to reflect a confidence level of approximately 75%, the committee expressed concern that a great portion of the Authority's assets, particularly in the liability program, are actually retrospective deposits receivable from the members. This is especially a concern in these challenging economic times in which the ability of some members to pay these receivables has been called into question.

Initially the committee focused its attention on the liability program as it has experienced the most volatility over the past few years. The committee felt that the findings made concerning the liability program would be transferrable to the workers' compensation program.

The committee made the following determinations:

- Individual member primary deposit increase limits have prevented the Authority from funding to the actuary's estimated funding needs. The program's adverse loss experience over the past few years has led the actuary to increase the funding estimates at rates exceeding the primary deposit increase limits. Therefore additional retrospective deposits are required to meet the funding estimate.
- Efforts to reduce volatility of the annual cash flow of the members have not been successful. While limits narrowed the band of volatility of primary deposits, there were no limits to constrain the volatility of the retrospective adjustments. In examining the combined annual contribution of individual members (primary deposit plus rolling retro installment payment), vast swings still occurred from one year to the next, with many members experiencing year-to-year changes in excess of 40%.
- The current weighting of experience and exposure in the primary deposit formula (50%/50%), does not recognize the inherent difference in the credibility of the loss experience of members of different sizes. Under the current weighting all members are treated equally in the application of the weighting factor. Standard industry practices follow the theory that a large member would have a more consistent loss experience, and therefore past loss experience would be more credible in predicting future losses. For this reason loss experience should be given greater weight in determining the costs borne by a larger member. Conversely, a smaller member would likely have less consistency

in its loss experience, so its loss experience would be less credible, and it should be given less weight in determining a small member's cost.

Following its initial review of the current funding model, the committee recognized that the insufficiency of the primary deposit would continue to shift the burden of the cost of coverage to the rolling retro, thereby forcing the Authority's reserves to carry the debt of the membership in perpetuity. Pro forma analysis showed that the current model was unsustainable as the debt load of the members would eventually exceed the Authority's lending capacity—ultimately affecting the Authority's ability to pay claims.

Pool-wide Findings

The committee first addressed the issues facing the pool as a whole. Primary among the issues addressed was the need for the Authority to get out of the credit business. In order to accomplish this, adequate funds need to be contributed by the membership at the beginning of a coverage period to support payment of claims and expenses associated with that coverage period. Based upon a review of industry standards, the committee established a goal of prospectively funding each coverage period at the 75% confidence level. Funding at this level should be adequate to fund all costs without the need for retrospective deposits.

Current funding of the primary deposit is at about the 50% probability level. The transition to funding at the 75% funding level will require a phased-in approach, as immediate implementation would result in an unpalatable increase in the annual contribution of the members. Even with the phased-in approach, the annual contribution to prospectively fund the coverage period combined with the continued payment of rolling retrospective deposit installments would present too great an initial increase if implemented immediately. Therefore the committee determined that the payment of retrospective deposits should be deferred during this transitional period as the program moves from retrospective to prospective funding. Once the aggregate annual contribution reaches the 75% confidence level, then the outstanding retrospective deposits would be repaid over time. The committee felt that it was important to recognize those members that were to receive retrospective refunds, so only the retrospective deposits would be deferred; net retrospective refunds would continue to flow to the members during the transition period.

Based on projected loss trends and exposure growth, it is expected that the transition, or phase-in, period would last approximately three years for the liability program. Extended cash flow projections indicate that the deferred retrospective deposits would be fully repaid in approximately eight to ten years. Positive claims development could result in a significant shortening of the repayment period. Exhibit 1 is a pro forma cash flow analysis of the transition from the current retrospective funding model to a prospective funding model.

Per Member Findings

Throughout its work, the committee was mindful of the impact that any change to the formula might have on the year-to-year cost to individual members. The committee also wanted to ensure that the formula maintained or enhanced incentives for members to demonstrate good risk management practices and control their own losses.

Credibility Weighting

The committee determined that “credibility weighting” would effectively promote accountability for members in the implementation of their risk management programs. As discussed previously, members with larger exposures (payroll) are likely to have more predictable, or credible, loss experience than those with smaller payrolls. Rather than treat members of different sizes by the same credibility factor as is done in the current formula (experience weighted 50% and exposure weighted 50%), a more appropriate weighting would be to weigh the experience more heavily for larger members. For smaller members, exposure would be weighed more heavily. The credibility weighting will vary within the range based on the size of the member.

The impact of experience credibility weighting is particularly noticeable for larger members as their efforts to reduce their losses could significantly reduce their share of pooled losses. Conversely, those that fail to implement strong risk management practices would likely experience greater losses and therefore face a larger share of pooled losses.

Smaller members typically experience fewer losses so they are more susceptible to volatility caused by fortuitous events. If a smaller member were to experience a large loss, under the current formula, it can have devastating impacts on the member’s cost of coverage. As an example, a small member experiencing very few losses might have an annual cost of coverage of about \$20,000. If that member were to experience a \$75,000 loss, the cost of coverage for that year alone would likely exceed \$120,000. To reduce this sort of volatility, it is appropriate to weigh exposure more heavily than experience in determining costs for smaller members.

The committee determined that experience credibility weighting would improve the fairness, or internal equity, within the program. Based upon a review of industry standards, the committee established a credibility weighting range of 20% to 80%. Under this methodology, the largest members would have their cost based 80% upon their experience and 20% upon their exposure. The smallest members would have their cost based 20% on their experience and 80% upon their exposure. There would be a sliding scale within the range dependent upon the exposure presented by each member.

Limits to Volatility

Mindful of the individual member impacts that could be experienced by changing the formula, the committee also recognized that the structure of the primary deposit limits was one of the contributing factors to the considerable debt owed by the members to the Authority. Further, the limits had not achieved the desired stability in the members’ annual contributions. Instead, the limits had merely shifted the volatility of the primary deposit to the retrospective adjustment.

An analysis of the year-to-year volatility in the total contribution made by the members over the past several coverage periods indicated significant volatility for the members under the current formulas (total contribution equals the member’s rolling retro deposit installment for prior coverage periods, plus its primary deposit for the upcoming coverage period). For example in 2007-08, more than half of the members experienced an increase in total contribution of over 30% from the prior year. The following chart demonstrates this volatility and projects the 2010-11 coverage period using the current formulas.

Liability Program				
Year-Over-Year Volatility in Annual Contribution				
	Coverage Period			
	07/08	08/09	09/10	10/11
Member Count	113	118	122	122
>-50%	1	0	1	0
>-40%	4	0	1	0
>-30%	5	0	2	2
>-20%	9	2	5	4
>-10%	17	7	12	6
<0%	26	16	33	21
=0%	2	4	0	0
>0%	85	98	89	101
>10%	79	89	57	76
>20%	69	73	39	54
>30%	58	55	24	38
>40%	40	32	15	25
>50%	31	25	13	14
>60%	25	22	9	9
>70%	19	16	9	5
>80%	18	13	7	4
>100%	13	10	4	3

The committee determined that a range of 0% to 35% would effectively balance the desire to protect against extreme volatility against the need to collect sufficient funds to achieve the funding target. The introduction of an “off-balance factor” ensures that the total funding target is achieved. The committee determined that the limits should be reviewed annually to ensure that they continue to appropriately balance volatility with funding sufficiency.

Workers’ Compensation Program

Workers’ compensation does not typically demonstrate the same level of volatility as liability. Individual losses are constrained by state law, so “shock” losses like those in the liability program are less likely. Until the last two coverage periods, the workers’ compensation program had not experienced the financial challenges affecting the liability program. On the contrary, the

Authority, in aggregate, owes more retrospective refunds to members than there are retrospective deposits due.

However, changes to the state-defined benefit schedules and two unfortunate decisions by the Workers' Compensation Appeals Board have had a significant impact on the actuarial projections regarding funding needs for the program.

Faced with the increasing funding estimates for the program and to head-off the creation of a sizeable retrospective deposit receivable debt, the committee determined that it would be appropriate to apply the same strategies discussed above for the liability program to the workers' compensation program.

In applying the new funding strategies to the workers' compensation program, the program's favorable loss trends in previous years actually present a challenge. Rolling retrospective refunds due to previous years have partially offset the recent increases in the actuary's funding estimate. When comparing the total contribution of the members (primary deposit, plus/minus rolling retro deposit/refund installment) in 2009-10 to the funding estimate for 2010-11, a significant year-to-year increase is indicated. However, by reducing the funding target in the first year of the transition period to the level that would have been collected under the current formula, per member increases fall within the established 0% to 35% range.

Retrospective Computations

In considering a transition from a retrospective funding model to a prospective funding model, the ad hoc committee recognized the need to maintain the existing model for coverage periods prior to the transition—those through 2009-10. Additionally, the committee recognized that during the transition period, it is possible that adverse loss experience may require additional contributions from the members. As such, the committee determined that retrospective computations should continue during the transition period utilizing the new variable credibility weighting methodology.

After achieving 75% confidence level funding for both programs, it is anticipated that additional contributions would not be required for individual coverage periods. In fact, as the credibility weighting is implemented, rough equity among the members will be achieved, and, with the exception of the coverage periods through 2009-10, the committee anticipates that the retrospective computations will be discontinued.

Comparing Retrospective and Prospective Funding Models

There are many different elements involved in determining the members' cost of coverage under both models. Two documents are attached to explain some of the differences and similarities between the current model and the proposed model. Exhibit 2 is prepared in a frequently asked questions (FAQs) format to try to address specific concerns. It is a draft of the document that

will be shared with the members upon final approval of the new funding model. Exhibit 3 was prepared to demonstrate the comparison in costs on a per member basis between the current retrospective funding model and the proposed prospective funding model.

The Managers and Finance Officers Committees met on February 8 for a joint presentation and discussion, and recommended adoption of the ad hoc committee's recommendations by the Executive Committee.

Recommended Action

It is recommended that the Executive Committee adopt the recommendations of the ad hoc committee pertaining to revisions to the Authority's funding model as outlined below effective with the 2010-2011 coverage period.

- Transition from a retrospective funding model to a prospective funding model.
- Adequately pre-fund each year with an annual contribution that is computed at the 75% confidence level.
 - Phase-in the 75% confidence level funding to prevent an extraordinary initial increase.
 - Base annual contribution on individual members' experience and exposure with these elements variably weighted based upon the credibility of the past loss experience in predicting future loss experience for a member.
 - Proceed toward elimination of the retrospective computation for those coverage periods subsequent to the transition period.
- Defer payment of retrospective receivables until annual contribution grows to the 75% confidence level.
 - Once the annual contribution is funded at the 75% confidence level, compute outstanding member liabilities, and commence collection of retrospective receivables.
 - Withdrawing members would not be eligible for deferral of payments nor the benefit of the rolling retro's installment mechanism.
- Base new funding model on historical cost allocation methodologies for continuity.
 - Police and non-police exposures calculated separately (liability program).
 - Loss layers \$0 - \$30,000 and \$30,000 - \$750,000 to be maintained in allocation formula (liability program).
 - Public safety and non-public safety exposures calculated separately (workers' compensation program).
 - Loss layers \$0 - \$50,000 and \$50,000 - \$100,000 to be maintained in allocation formula (workers' compensation program).
 - Experience of past five coverage periods used to measure experience.
- Limit year-to-year changes in annual contribution compared to prior year's primary and retro deposits to 0%-35% in the first year; annually review appropriate year-to-year limitations.

- Evaluate losses six months after the end of the coverage period to allow for additional claims maturation prior to application of formulas.
- Discontinue special treatment of “property damage only” claims and automatic reserving of “slip and trip” claims.
- Waive the one-year membership withdrawal notice provision for members that joined the pool after July 1, 2007, in the event the member wishes to withdraw from the pool at the end of the 2009-2010 coverage period.
- Invoice members that elect to withdraw for the full amount of any retrospective deposits due, and make the entire amount due and payable upon withdrawal.

Additionally, it is recommended that staff be directed to invoice members and former members that have left programs, but continue to have retrospective deposits due, for the entire amount due and payable. This item was not considered by the ad hoc committee.

Exhibit 1

Pro Forma Cash Flow Analysis

CALIFORNIA JOINT POWERS INSURANCE AUTHORITY
Pro Forma Financial Statements

Exhibit GL
Sheet 1f

General Liability - Assuming Funding to 75% Confidence Level with Phase-In and Retro Rebates

	6/30/2008	6/30/2009	6/30/2010	6/30/2011	6/30/2012	6/30/2013	6/30/2014	6/30/2015	6/30/2016	6/30/2017	6/30/2018	6/30/2019
ASSETS												
1 Investments	\$79,322,694	\$82,194,838	\$72,041,437	\$69,588,776	\$72,979,522	\$83,882,962	\$97,979,358	\$119,536,648	\$144,703,334	\$170,715,111	\$197,737,438	\$226,147,057
2 Retro Deposits Receivable	\$66,418,037	\$80,176,220	\$94,261,143	\$97,105,807	\$97,105,807	\$94,660,570	\$89,770,096	\$79,757,857	\$67,152,523	\$54,466,049	\$41,779,576	\$29,093,103
3 Other Assets	\$3,726,751	\$3,875,821	\$4,030,854	\$4,192,088	\$4,359,772	\$4,534,162	\$4,715,529	\$4,904,150	\$5,100,316	\$5,304,329	\$5,516,502	\$5,737,162
4 TOTAL ASSETS	\$149,467,482	\$166,246,879	\$170,333,434	\$170,886,672	\$174,445,101	\$183,077,695	\$192,464,982	\$204,198,656	\$216,956,173	\$230,485,489	\$245,033,516	\$260,977,322
LIABILITIES												
5 Claims Payable	\$91,880,000	\$109,063,826	\$111,545,053	\$112,956,941	\$118,227,859	\$125,287,406	\$131,625,326	\$139,218,697	\$147,307,853	\$155,565,974	\$164,162,884	\$173,153,530
6 Retro Rebates Payable	\$7,733,850	\$7,589,417	\$8,831,265	\$8,501,053	\$7,182,781	\$6,052,497	\$5,029,000	\$4,005,504	\$2,982,007	\$1,958,510	\$988,132	\$368,729
7 Other Liabilities	\$5,715,186	\$5,943,793	\$6,181,545	\$6,428,807	\$6,685,959	\$6,953,398	\$7,231,534	\$7,520,795	\$7,821,627	\$8,134,492	\$8,459,871	\$8,798,266
8 TOTAL LIABILITIES	\$105,329,036	\$122,597,036	\$126,557,864	\$127,886,801	\$132,096,600	\$138,293,301	\$143,885,860	\$150,744,995	\$158,111,487	\$165,658,976	\$173,610,888	\$182,320,525
9 NET ASSETS	\$44,138,446	\$43,649,843	\$43,775,571	\$42,999,871	\$42,348,501	\$44,784,394	\$48,579,122	\$53,453,661	\$58,844,686	\$64,826,513	\$71,422,628	\$78,656,796
REVENUES												
10 Primary Deposits Earned		\$32,665,987	\$33,969,600	\$47,217,744	\$51,939,518	\$57,133,470	\$60,561,478	\$63,714,252	\$66,262,822	\$68,913,335	\$71,669,868	\$74,536,663
11 Net Retro Deposits Earned		\$22,967,665	\$12,519,932	\$2,528,590	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
12 Miscellaneous		\$176,000	\$183,040	\$190,362	\$197,976	\$205,895	\$214,131	\$222,696	\$231,604	\$240,868	\$250,503	\$260,523
13 Investment Income		\$3,145,475	\$1,726,092	\$1,512,870	\$1,461,364	\$1,532,570	\$1,761,542	\$2,057,567	\$2,510,270	\$3,038,770	\$3,585,017	\$4,152,486
14 Unrealized Gains (Losses)		(\$2,095,114)	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
15 TOTAL REVENUES		\$56,860,013	\$48,398,664	\$51,449,566	\$53,598,859	\$58,871,935	\$62,537,152	\$65,994,514	\$69,004,695	\$72,192,973	\$75,505,388	\$78,949,672
EXPENSES												
16 Incurred Claims		\$45,895,480	\$33,517,340	\$36,879,446	\$38,290,576	\$39,838,004	\$41,480,463	\$43,167,537	\$44,943,134	\$46,793,788	\$48,715,221	\$50,713,690
17 Reinsurance Premiums		\$5,863,140	\$8,942,000	\$9,299,680	\$9,671,667	\$10,058,534	\$10,460,875	\$10,879,310	\$11,314,483	\$11,767,062	\$12,237,744	\$12,727,254
18 Other Coverage Expenses		\$2,515,794	\$2,616,426	\$2,721,083	\$2,829,926	\$2,943,123	\$3,060,848	\$3,183,282	\$3,310,613	\$3,443,038	\$3,580,759	\$3,723,990
19 Contractual Services		\$492,238	\$511,928	\$532,405	\$553,701	\$575,849	\$598,883	\$622,838	\$647,752	\$673,662	\$700,608	\$728,632
20 General and Administrative		\$2,581,964	\$2,685,243	\$2,792,652	\$2,904,358	\$3,020,533	\$3,141,354	\$3,267,008	\$3,397,688	\$3,533,596	\$3,674,940	\$3,821,937
21 TOTAL EXPENSES		\$57,348,616	\$48,272,936	\$52,225,266	\$54,250,228	\$56,436,043	\$58,742,424	\$61,119,975	\$63,613,670	\$66,211,145	\$68,909,273	\$71,715,504
22 CHANGE IN NET ASSETS		(\$488,603)	\$125,728	(\$775,700)	(\$651,369)	\$2,435,893	\$3,794,728	\$4,874,539	\$5,391,025	\$5,981,827	\$6,596,115	\$7,234,168
23 TOTAL NET CONTRIBUTIONS PAID		\$41,731,036	\$43,034,649	\$46,894,601	\$51,293,232	\$55,815,199	\$61,876,432	\$67,581,229	\$75,251,563	\$80,495,172	\$83,332,844	\$86,252,759
24 CHANGE FROM PRIOR YEAR			3.1%	9.0%	9.4%	8.8%	10.9%	9.2%	11.3%	7.0%	3.5%	3.5%

Exhibit 2

Frequently Asked Questions about Revisions to the Funding Model

Exhibit 3

Comparison of Costs between Retrospective Funding Model and Proposed Prospective Funding Model

Combined Liability + Workers' Compensation Programs

2010/2011 Coverage Period

Comparison of Costs between Current Retrospective Funding Model and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF. Proposed vs. Current	Proposed Model	
	Combined Programs Paid 7/1/2009	Combined Programs Net Due 7/1/2010	Combined Programs Net Due 7/1/2010		YOY% vs. 2009	
1 Agoura Hills	174,467	214,145	193,460	-9.7%	10.9%	1
2 AHCCCA	13,847	19,578	3,646	-81.4%	-73.7%	2
3 Aliso Viejo	65,764	43,178	55,891	29.4%	-15.0%	3
4 Apple Valley	543,533	617,743	733,770	18.8%	35.0%	4
5 Area B	7,208	9,160	9,206	0.5%	27.7%	5
6 Area E	7,556	10,205	9,752	-4.4%	29.1%	6
7 Arroyo Grande	676,615	784,830	663,917	-15.4%	-1.9%	7
8 Artesia	157,362	229,614	212,439	-7.5%	35.0%	8
9 Atascadero	808,355	983,351	827,998	-15.8%	2.4%	9
10 Bell Gardens	738,055	1,191,089	807,743	-32.2%	9.4%	10
11 Bellflower	552,547	758,278	575,268	-24.1%	4.1%	11
12 Belvedere	80,431	93,669	91,217	-2.6%	13.4%	12
13 Big Bear City CSD	254,363	320,648	292,340	-8.8%	14.9%	13
14 Big Bear Lake	893,857	906,540	1,070,675	18.1%	19.8%	14
15 Bishop	257,581	268,488	257,581	-4.1%	0.0%	15
16 Black Gold CLS	9,481	10,940	11,036	0.9%	16.4%	16
17 Bradbury	11,436	14,863	15,439	3.9%	35.0%	17
18 Brawley	735,801	799,739	811,245	1.4%	10.3%	18
19 Buellton	89,224	103,403	99,418	-3.9%	11.4%	19
20 Burney FPD	20,715	26,240	27,963	6.6%	35.0%	20
21 Calabasas	530,222	625,185	663,324	6.1%	25.1%	21
22 Calexico	1,261,887	1,519,608	1,438,630	-5.3%	14.0%	22
23 California JPIA	27,792	31,650	37,519	18.5%	35.0%	23
24 Camarillo	635,507	802,344	567,937	-29.2%	-10.6%	24
25 Carpinteria	82,853	113,617	111,427	-1.9%	34.5%	25
26 CASA	71,063	120,245	82,794	-31.1%	16.5%	26
27 Cerritos	1,861,659	2,118,362	1,929,134	-8.9%	3.6%	27
28 Chino Hills	567,853	748,099	675,359	-9.7%	18.9%	28
29 Claremont	1,154,518	1,382,408	1,311,497	-5.1%	13.6%	29
30 Commerce	944,439	1,093,073	1,013,113	-7.3%	7.3%	30
31 Cudahy	204,815	218,659	221,626	1.4%	8.2%	31
32 CVAG	37,355	38,078	50,429	32.4%	35.0%	32
33 CVCC	8,287	8,386	11,187	33.4%	35.0%	33

Combined Liability + Workers' Compensation Programs

2010/2011 Coverage Period

Comparison of Costs between Current Retrospective Funding Model and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF. Proposed vs. Current	Proposed Model	
	Combined Programs Paid 7/1/2009	Combined Programs Net Due 7/1/2010	Combined Programs Net Due 7/1/2010		YOY% vs. 2009	
34 Dana Point	342,644	430,536	462,053	7.3%	34.8%	34
35 Diamond Bar	414,562	361,612	539,993	49.3%	30.3%	35
36 Duarte	237,578	287,014	225,145	-21.6%	-5.2%	36
37 El Centro	1,599,030	1,875,072	1,774,218	-5.4%	11.0%	37
38 ESTA	75,189	114,682	93,156	-18.8%	23.9%	38
39 Fillmore	213,809	241,029	186,515	-22.6%	-12.8%	39
40 Fountain Valley	732,340	968,048	732,340	-24.3%	0.0%	40
41 Gateway Cities COG	12,232	15,850	16,266	2.6%	33.0%	41
42 Goleta	259,236	329,052	292,234	-11.2%	12.7%	42
43 Grand Terrace	142,483	167,352	158,160	-5.5%	11.0%	43
44 Grover Beach	501,224	502,447	377,466	-24.9%	-24.7%	44
45 Guadalupe	135,205	129,429	155,305	20.0%	14.9%	45
46 Hawaiian Gardens	134,498	178,362	103,755	-41.8%	-22.9%	46
47 Hidden Hills	7,618	11,310	10,284	-9.1%	35.0%	47
48 Imperial	444,314	553,026	488,909	-11.6%	10.0%	48
49 Indian Wells	153,022	234,516	192,846	-17.8%	26.0%	49
50 Indio	1,439,112	1,729,154	1,852,973	7.2%	28.8%	50
51 Irwindale	930,029	973,715	1,038,184	6.6%	11.6%	51
52 La Canada Flintridge	336,421	379,470	350,243	-7.7%	4.1%	52
53 La Habra Heights	78,509	128,191	105,987	-17.3%	35.0%	53
54 La Mirada	798,196	828,117	858,082	3.6%	7.5%	54
55 La Palma	248,445	339,983	228,997	-32.6%	-7.8%	55
56 La Puente	256,074	261,033	299,907	14.9%	17.1%	56
57 La Quinta	471,497	474,551	474,623	0.0%	0.7%	57
58 La Verne	1,157,295	1,285,877	1,188,279	-7.6%	2.7%	58
59 Laguna Niguel	425,536	422,537	424,707	0.5%	-0.2%	59
60 Laguna Woods	116,708	93,743	116,255	24.0%	-0.4%	60
61 Lake Elsinore	694,348	675,849	765,336	13.2%	10.2%	61
62 Lake Forest	328,412	392,401	362,204	-7.7%	10.3%	62
63 Lakewood	1,170,542	1,226,663	1,186,076	-3.3%	1.3%	63
64 Las Virgenes COG	6,493	10,073	8,766	-13.0%	35.0%	64
65 Lawndale	373,167	473,561	400,436	-15.4%	7.3%	65
66 Local Govt Services	79,154	95,675	103,174	7.8%	30.3%	66

Combined Liability + Workers' Compensation Programs

2010/2011 Coverage Period

Comparison of Costs between Current Retrospective Funding Model and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF. Proposed vs. Current	Proposed Model	
	Combined Programs Paid 7/1/2009	Combined Programs Net Due 7/1/2010	Combined Programs Net Due 7/1/2010		YOY% vs. 2009	
67 Loma Linda	456,672	556,806	523,206	-6.0%	14.6%	67
68 Lomita	348,045	282,589	327,365	15.8%	-5.9%	68
69 Los Alamitos	406,341	468,597	421,723	-10.0%	3.8%	69
70 Malibu	666,356	644,225	670,089	4.0%	0.6%	70
71 Mammoth Lakes	795,017	864,028	864,302	0.0%	8.7%	71
72 Marin County MCTF	6,788	9,184	8,899	-3.1%	31.1%	72
73 MARTA	169,483	169,260	177,156	4.7%	4.5%	73
74 Maywood	1,531,434	1,842,781	2,067,436	12.2%	35.0%	74
75 Midpeninsula ROSD	423,251	459,376	457,871	-0.3%	8.2%	75
76 Mission Viejo	993,567	953,205	901,407	-5.4%	-9.3%	76
77 Monterey Peninsula RP	53,284	52,032	69,767	34.1%	30.9%	77
78 Moorpark	373,209	417,841	332,012	-20.5%	-11.0%	78
79 Morro Bay	657,918	662,574	633,716	-4.4%	-3.7%	79
80 Needles	253,463	213,198	182,630	-14.3%	-27.9%	80
81 Norwalk	2,227,004	2,618,454	3,006,455	14.8%	35.0%	81
82 Ojai	294,693	311,583	327,838	5.2%	11.2%	82
83 Palm Desert	586,588	792,294	501,842	-36.7%	-14.4%	83
84 Palos Verdes Estates	413,635	418,288	417,601	-0.2%	1.0%	84
85 Palos Verdes TA	13,446	16,237	17,592	8.3%	30.8%	85
86 Paramount	371,863	520,697	355,926	-31.6%	-4.3%	86
87 Paso Robles	1,177,104	1,162,711	1,080,281	-7.1%	-8.2%	87
88 Pico Rivera	1,141,257	1,271,048	1,138,920	-10.4%	-0.2%	88
89 Pismo Beach	586,444	765,848	645,784	-15.7%	10.1%	89
90 Pomona Valley TA	13,397	12,750	15,678	23.0%	17.0%	90
91 Port Hueneme	1,019,691	1,052,474	1,004,245	-4.6%	-1.5%	91
92 Poway	1,461,963	1,579,664	1,660,535	5.1%	13.6%	92
93 Rancho Palos Verdes	699,205	560,426	729,030	30.1%	4.3%	93
94 Regional Govt Services	19,435	29,686	26,237	-11.6%	35.0%	94
95 Rolling Hills	50,122	35,210	65,853	87.0%	31.4%	95
96 Rolling Hills Estates	226,045	241,882	238,672	-1.3%	5.6%	96
97 Rosemead	300,139	408,142	405,187	-0.7%	35.0%	97
98 San Clemente	441,430	672,684	595,931	-11.4%	35.0%	98
99 San Dimas	702,183	654,100	729,545	11.5%	3.9%	99

Combined Liability + Workers' Compensation Programs

2010/2011 Coverage Period

Comparison of Costs between Current Retrospective Funding Model and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF. Proposed vs. Current	Proposed Model	
	Combined Programs Paid 7/1/2009	Combined Programs Net Due 7/1/2010	Combined Programs Net Due 7/1/2010		YOY% vs. 2009	
100 San Gabriel	1,378,082	1,373,601	1,272,053	-7.4%	-7.7%	100
101 San Juan Capistrano	707,010	787,408	885,132	12.4%	25.2%	101
102 San Luis Obispo	2,104,592	2,597,850	1,791,187	-31.1%	-14.9%	102
103 San Marcos	815,284	935,194	982,994	5.1%	20.6%	103
104 San Marino	484,739	574,878	484,739	-15.7%	0.0%	104
105 Santa Fe Springs	1,225,727	1,772,831	1,471,756	-17.0%	20.1%	105
106 Santa Paula	1,025,542	1,212,071	1,213,205	0.1%	18.3%	106
107 SCAG	357,285	534,004	287,207	-46.2%	-19.6%	107
108 SEAACA	130,387	165,686	143,408	-13.4%	10.0%	108
109 Seal Beach	1,018,851	1,104,649	1,176,824	6.5%	15.5%	109
110 Seaside	858,211	1,186,822	967,198	-18.5%	12.7%	110
111 Seaside CSD	7,478	21,907	10,095	-53.9%	35.0%	111
112 Sierra Madre	452,270	659,996	555,828	-15.8%	22.9%	112
113 Signal Hill	510,905	629,352	517,967	-17.7%	1.4%	113
114 Solvang	158,265	196,612	138,520	-29.5%	-12.5%	114
115 South El Monte	291,316	318,219	274,714	-13.7%	-5.7%	115
116 South Pasadena	1,073,447	1,311,110	1,234,209	-5.9%	15.0%	116
117 Temple City	255,551	279,508	271,997	-2.7%	6.4%	117
118 Ventura Port District	154,185	183,721	154,639	-15.8%	0.3%	118
119 Villa Park	51,935	53,023	53,397	0.7%	2.8%	119
120 Walnut	242,745	284,345	292,770	3.0%	20.6%	120
121 West Hollywood	1,330,496	1,652,049	1,775,427	7.5%	33.4%	121
122 West-Comm	36,768	35,412	41,492	17.2%	12.8%	122
123 Westlake Village	83,623	92,944	85,294	-8.2%	2.0%	123
Pool	61,431,435	71,077,261	67,118,485	-5.6%	9.3%	

Liability Program

2010/2011 Coverage Period

Comparison of Costs between
Current Retrospective Funding Model
and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF.	Proposed Model	
	Paid 7/1/2009	Net Due 7/1/2010	Net Due 7/1/2010	Proposed vs. Current	YOY% vs. 2009	
1 Agoura Hills	149,512	177,964	172,186	-3.2%	15.2%	1
2 AHCCCA	11,763	15,904	15,880	-0.2%	35.0%	2
3 Aliso Viejo	60,463	37,248	48,735	30.8%	-19.4%	3
4 Apple Valley	428,988	469,995	579,134	23.2%	35.0%	4
5 Area B	7,208	9,160	9,206	0.5%	27.7%	5
6 Area E	6,470	8,871	8,735	-1.5%	35.0%	6
7 Arroyo Grande	417,715	491,494	417,715	-15.0%	0.0%	7
8 Artesia	73,646	115,547	99,422	-14.0%	35.0%	8
9 Atascadero	590,877	743,772	590,877	-20.6%	0.0%	9
10 Bell Gardens	442,001	678,460	596,701	-12.1%	35.0%	10
11 Bellflower	417,284	588,356	417,284	-29.1%	0.0%	11
12 Belvedere	41,804	62,553	56,435	-9.8%	35.0%	12
13 Big Bear City CSD	78,918	115,262	106,539	-7.6%	35.0%	13
14 Big Bear Lake	600,449	631,953	736,929	16.6%	22.7%	14
15 Bishop	257,581	268,488	257,581	-4.1%	0.0%	15
16 Black Gold CLS	9,481	10,940	11,036	0.9%	16.4%	16
17 Bradbury	8,920	12,322	12,042	-2.3%	35.0%	17
18 Brawley	329,231	360,457	329,231	-8.7%	0.0%	18
19 Buellton	53,268	59,361	56,755	-4.4%	6.5%	19
20 Burney FPD	16,295	21,640	21,996	1.6%	35.0%	20
21 Calabasas	423,841	509,962	572,185	12.2%	35.0%	21
22 Calexico	741,652	849,622	741,652	-12.7%	0.0%	22
23 Camarillo	498,666	612,896	498,666	-18.6%	0.0%	23
24 Carpinteria	44,487	73,880	59,633	-19.3%	34.0%	24
25 CASA	36,467	84,458	49,230	-41.7%	35.0%	25
26 Cerritos	1,384,700	1,530,711	1,384,700	-9.5%	0.0%	26
27 Chino Hills	389,831	553,513	489,811	-11.5%	25.6%	27
28 Claremont	706,008	853,546	706,008	-17.3%	0.0%	28
29 Commerce	597,773	661,124	597,773	-9.6%	0.0%	29
30 Cudahy	156,784	154,090	156,784	1.7%	0.0%	30
31 CVAG	37,355	38,078	50,429	32.4%	35.0%	31
32 CVCC	8,287	8,386	11,187	33.4%	35.0%	32
33 Dana Point	308,552	388,184	416,545	7.3%	35.0%	33
34 Diamond Bar	365,656	346,792	482,677	39.2%	32.0%	34

Liability Program

2010/2011 Coverage Period

Comparison of Costs between
Current Retrospective Funding Model
and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF.	Proposed Model	
	Paid 7/1/2009	Net Due 7/1/2010	Net Due 7/1/2010	Proposed vs. Current	YOY% vs. 2009	
35 Duarte	198,286	217,073	198,286	-8.7%	0.0%	35
36 El Centro	1,098,494	1,010,787	1,098,494	8.7%	0.0%	36
37 ESTA	54,343	66,866	65,014	-2.8%	19.6%	37
38 Fillmore	182,768	212,075	182,768	-13.8%	0.0%	38
39 Fountain Valley	732,340	968,048	732,340	-24.3%	0.0%	39
40 Gateway Cities COG	9,104	12,541	12,290	-2.0%	35.0%	40
41 Goleta	222,705	278,316	242,917	-12.7%	9.1%	41
42 Grand Terrace	112,781	129,469	118,062	-8.8%	4.7%	42
43 Grover Beach	269,553	289,547	269,553	-6.9%	0.0%	43
44 Guadalupe	57,408	60,120	77,501	28.9%	35.0%	44
45 Hawaiian Gardens	97,914	149,958	132,184	-11.9%	35.0%	45
46 Hidden Hills	7,618	11,310	10,284	-9.1%	35.0%	46
47 Imperial	299,546	359,848	299,546	-16.8%	0.0%	47
48 Indian Wells	111,551	179,788	150,594	-16.2%	35.0%	48
49 Indio	790,677	900,470	977,586	8.6%	23.6%	49
50 Irwindale	621,016	627,991	621,016	-1.1%	0.0%	50
51 La Canada Flintridge	296,929	341,057	296,929	-12.9%	0.0%	51
52 La Habra Heights	58,566	85,076	79,064	-7.1%	35.0%	52
53 La Mirada	627,092	609,677	627,092	2.9%	0.0%	53
54 La Palma	99,482	193,100	134,301	-30.5%	35.0%	54
55 La Puente	174,792	203,022	219,221	8.0%	25.4%	55
56 La Quinta	365,209	340,615	365,209	7.2%	0.0%	56
57 La Verne	719,181	811,077	719,181	-11.3%	0.0%	57
58 Laguna Niguel	381,014	351,210	381,014	8.5%	0.0%	58
59 Laguna Woods	108,370	84,347	108,370	28.5%	0.0%	59
60 Lake Elsinore	694,348	675,849	765,336	13.2%	10.2%	60
61 Lake Forest	247,685	324,620	253,223	-22.0%	2.2%	61
62 Lakewood	849,524	940,817	849,524	-9.7%	0.0%	62
63 Las Virgenes COG	6,493	10,073	8,766	-13.0%	35.0%	63
64 Lawndale	284,132	380,072	284,132	-25.2%	0.0%	64
65 Local Govt Services	43,433	54,426	58,635	7.7%	35.0%	65
66 Loma Linda	224,842	311,695	224,842	-27.9%	0.0%	66
67 Lomita	252,880	205,026	252,880	23.3%	0.0%	67
68 Los Alamitos	235,494	292,146	262,624	-10.1%	11.5%	68
69 Malibu	568,114	553,817	568,114	2.6%	0.0%	69

Liability Program

2010/2011 Coverage Period

Comparison of Costs between
Current Retrospective Funding Model
and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF.	Proposed Model	
	Paid 7/1/2009	Net Due 7/1/2010	Net Due 7/1/2010	Proposed vs. Current	YOY% vs. 2009	
70 Mammoth Lakes	597,060	645,125	597,060	-7.5%	0.0%	70
71 Marin County MCTF	6,788	9,184	8,899	-3.1%	31.1%	71
72 MARTA	147,561	137,448	147,561	7.4%	0.0%	72
73 Maywood	1,316,598	1,505,733	1,777,407	18.0%	35.0%	73
74 Midpeninsula ROSD	219,095	258,147	219,095	-15.1%	0.0%	74
75 Mission Viejo	716,269	725,266	716,269	-1.2%	0.0%	75
76 Monterey Peninsula RPD	16,612	35,123	22,426	-36.2%	35.0%	76
77 Moorpark	297,544	324,643	297,544	-8.3%	0.0%	77
78 Morro Bay	547,710	505,168	547,710	8.4%	0.0%	78
79 Needles	148,660	162,562	148,660	-8.6%	0.0%	79
80 Norwalk	1,253,941	1,423,865	1,692,820	18.9%	35.0%	80
81 Ojai	196,415	200,864	196,415	-2.2%	0.0%	81
82 Palm Desert	442,340	618,935	449,191	-27.4%	1.5%	82
83 Palos Verdes Estates	349,442	331,398	349,442	5.4%	0.0%	83
84 Palos Verdes TA	13,446	16,237	17,592	8.3%	30.8%	84
85 Paramount	234,432	375,513	253,740	-32.4%	8.2%	85
86 Paso Robles	682,839	717,901	697,474	-2.8%	2.1%	86
87 Pico Rivera	895,918	955,883	895,918	-6.3%	0.0%	87
88 Pismo Beach	417,758	537,435	456,137	-15.1%	9.2%	88
89 Pomona Valley TA	9,320	8,993	11,398	26.7%	22.3%	89
90 Port Hueneme	735,253	704,804	735,253	4.3%	0.0%	90
91 Poway	894,614	908,948	894,614	-1.6%	0.0%	91
92 Rancho Palos Verdes	636,756	495,734	664,421	34.0%	4.3%	92
93 Regional Govt Services	10,281	18,283	13,879	-24.1%	35.0%	93
94 Rolling Hills	46,235	30,336	62,417	105.8%	35.0%	94
95 Rolling Hills Estates	174,306	177,541	174,306	-1.8%	0.0%	95
96 Rosemead	195,764	283,558	264,281	-6.8%	35.0%	96
97 San Clemente	441,430	672,684	595,931	-11.4%	35.0%	97
98 San Dimas	623,853	547,029	623,853	14.0%	0.0%	98
99 San Gabriel	590,472	616,727	590,472	-4.3%	0.0%	99
100 San Juan Capistrano	701,909	766,258	863,982	12.8%	23.1%	100
101 San Luis Obispo	1,344,112	1,699,030	1,344,112	-20.9%	0.0%	101
102 San Marcos	815,284	935,194	982,994	5.1%	20.6%	102
103 San Marino	484,739	574,878	484,739	-15.7%	0.0%	103
104 Santa Fe Springs	616,065	918,967	692,249	-24.7%	12.4%	104

Liability Program

2010/2011 Coverage Period

Comparison of Costs between
Current Retrospective Funding Model
and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF.	Proposed Model	
	Paid 7/1/2009	Net Due 7/1/2010	Net Due 7/1/2010	Proposed vs. Current	YOY% vs. 2009	
105 Santa Paula	574,090	776,902	775,022	-0.2%	35.0%	105
106 SCAG	284,689	413,123	284,689	-31.1%	0.0%	106
107 SEAACA	88,127	95,840	93,627	-2.3%	6.2%	107
108 Seal Beach	567,501	652,318	567,501	-13.0%	0.0%	108
109 Seaside	459,536	680,744	535,572	-21.3%	16.5%	109
110 Seaside CSD	7,478	21,907	10,095	-53.9%	35.0%	110
111 Sierra Madre	290,959	477,083	338,058	-29.1%	16.2%	111
112 Signal Hill	271,156	387,937	272,806	-29.7%	0.6%	112
113 Solvang	137,659	167,454	137,659	-17.8%	0.0%	113
114 South El Monte	252,183	264,662	252,183	-4.7%	0.0%	114
115 South Pasadena	684,121	915,563	923,563	0.9%	35.0%	115
116 Temple City	200,962	237,422	229,184	-3.5%	14.0%	116
117 Ventura Port District	131,568	118,583	131,568	11.0%	0.0%	117
118 Villa Park	45,518	46,856	45,518	-2.9%	0.0%	118
119 Walnut	203,765	236,250	275,083	16.4%	35.0%	119
120 West Hollywood	1,011,040	1,291,558	1,364,904	5.7%	35.0%	120
121 West-Comm	36,768	35,412	41,492	17.2%	12.8%	121
122 Westlake Village	74,312	81,587	74,312	-8.9%	0.0%	122
Pool	42,947,870	49,533,513	47,251,690	-4.6%	10.0%	

Workers' Compensation Program

2010/2011 Coverage Period

Comparison of Costs between Current Retrospective Funding Model and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF.	Proposed Model	
	Paid 7/1/2009	Net Due 7/1/2010	Net Due 7/1/2010	Proposed vs. Current	YOY% vs. 2009	
1 Agoura Hills	24,955	36,181	21,274	-41.2%	-14.8%	1
2 AHCCCA	2,084	3,674	(12,234)	-433.0%	-687.1%	2
3 Aliso Viejo	5,301	5,930	7,156	20.7%	35.0%	3
4 Apple Valley	114,545	147,748	154,636	4.7%	35.0%	4
5 Area E	1,086	1,334	1,017	-23.7%	-6.3%	5
6 Arroyo Grande	258,900	293,336	246,202	-16.1%	-4.9%	6
7 Artesia	83,716	114,067	113,017	-0.9%	35.0%	7
8 Atascadero	217,478	239,579	237,121	-1.0%	9.0%	8
9 Bell Gardens	296,054	512,629	211,042	-58.8%	-28.7%	9
10 Bellflower	135,263	169,922	157,984	-7.0%	16.8%	10
11 Belvedere	38,627	31,116	34,782	11.8%	-10.0%	11
12 Big Bear City CSD	175,445	205,386	185,801	-9.5%	5.9%	12
13 Big Bear Lake	293,408	274,587	333,746	21.5%	13.7%	13
14 Bradbury	2,516	2,541	3,397	33.7%	35.0%	14
15 Brawley	406,570	439,282	482,014	9.7%	18.6%	15
16 Buellton	35,956	44,042	42,663	-3.1%	18.7%	16
17 Burney FPD	4,420	4,600	5,967	29.7%	35.0%	17
18 Calabasas	106,381	115,223	91,139	-20.9%	-14.3%	18
19 Calexico	520,235	669,986	696,978	4.0%	34.0%	19
20 California JPIA	27,792	31,650	37,519	18.5%	35.0%	20
21 Camarillo	136,841	189,448	69,271	-63.4%	-49.4%	21
22 Carpinteria	38,366	39,737	51,794	30.3%	35.0%	22
23 CASA	34,596	35,787	33,564	-6.2%	-3.0%	23
24 Cerritos	476,959	587,651	544,434	-7.4%	14.1%	24
25 Chino Hills	178,022	194,586	185,549	-4.6%	4.2%	25
26 Claremont	448,510	528,862	605,489	14.5%	35.0%	26
27 Commerce	346,666	431,949	415,340	-3.8%	19.8%	27
28 Cudahy	48,031	64,569	64,842	0.4%	35.0%	28
29 Dana Point	34,092	42,352	45,508	7.5%	33.5%	29
30 Diamond Bar	48,906	14,820	57,316	286.7%	17.2%	30
31 Duarte	39,292	69,941	26,859	-61.6%	-31.6%	31
32 El Centro	500,536	864,285	675,724	-21.8%	35.0%	32
33 ESTA	20,846	47,816	28,142	-41.1%	35.0%	33
34 Fillmore	31,041	28,954	3,747	-87.1%	-87.9%	34

Workers' Compensation Program

2010/2011 Coverage Period

Comparison of Costs between Current Retrospective Funding Model and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF.	Proposed Model	
	Paid 7/1/2009	Net Due 7/1/2010	Net Due 7/1/2010	Proposed vs. Current	YOY% vs. 2009	
35 Gateway Cities COG	3,128	3,309	3,976	20.1%	27.1%	35
36 Goleta	36,531	50,736	49,317	-2.8%	35.0%	36
37 Grand Terrace	29,702	37,883	40,098	5.8%	35.0%	37
38 Grover Beach	231,671	212,900	107,913	-49.3%	-53.4%	38
39 Guadalupe	77,797	69,309	77,804	12.3%	0.0%	39
40 Hawaiian Gardens	36,584	28,404	(28,429)	-200.1%	-177.7%	40
41 Imperial	144,768	193,178	189,363	-2.0%	30.8%	41
42 Indian Wells	41,471	54,728	42,252	-22.8%	1.9%	42
43 Indio	648,435	828,684	875,387	5.6%	35.0%	43
44 Irwindale	309,013	345,724	417,168	20.7%	35.0%	44
45 La Canada Flintridge	39,492	38,413	53,314	38.8%	35.0%	45
46 La Habra Heights	19,943	43,115	26,923	-37.6%	35.0%	46
47 La Mirada	171,104	218,440	230,990	5.7%	35.0%	47
48 La Palma	148,963	146,883	94,696	-35.5%	-36.4%	48
49 La Puente	81,282	58,011	80,687	39.1%	-0.7%	49
50 La Quinta	106,288	133,936	109,414	-18.3%	2.9%	50
51 La Verne	438,114	474,800	469,098	-1.2%	7.1%	51
52 Laguna Niguel	44,522	71,327	43,693	-38.7%	-1.9%	52
53 Laguna Woods	8,338	9,396	7,885	-16.1%	-5.4%	53
54 Lake Forest	80,727	67,781	108,981	60.8%	35.0%	54
55 Lakewood	321,018	285,846	336,552	17.7%	4.8%	55
56 Lawndale	89,035	93,489	116,304	24.4%	30.6%	56
57 Local Govt Services	35,721	41,249	44,539	8.0%	24.7%	57
58 Loma Linda	231,830	245,111	298,364	21.7%	28.7%	58
59 Lomita	95,165	77,563	74,485	-4.0%	-21.7%	59
60 Los Alamitos	170,847	176,451	159,099	-9.8%	-6.9%	60
61 Malibu	98,242	90,408	101,975	12.8%	3.8%	61
62 Mammoth Lakes	197,957	218,903	267,242	22.1%	35.0%	62
63 MARTA	21,922	31,812	29,595	-7.0%	35.0%	63
64 Maywood	214,836	337,048	290,029	-14.0%	35.0%	64
65 Midpeninsula ROSD	204,156	201,229	238,776	18.7%	17.0%	65
66 Mission Viejo	277,298	227,939	185,138	-18.8%	-33.2%	66
67 Monterey Peninsula RPD	36,672	16,909	47,341	180.0%	29.1%	67
68 Moorpark	75,665	93,198	34,468	-63.0%	-54.4%	68
69 Morro Bay	110,208	157,406	86,006	-45.4%	-22.0%	69

Workers' Compensation Program

2010/2011 Coverage Period

Comparison of Costs between Current Retrospective Funding Model and Proposed Prospective Funding Model

Member	Current Model	Current Model	Proposed Model	% DIFF.	Proposed Model	
	Paid 7/1/2009	Net Due 7/1/2010	Net Due 7/1/2010	Proposed vs. Current	YOY% vs. 2009	
70 Needles	104,803	50,636	33,970	-32.9%	-67.6%	70
71 Norwalk	973,063	1,194,589	1,313,635	10.0%	35.0%	71
72 Ojai	98,278	110,719	131,423	18.7%	33.7%	72
73 Palm Desert	144,248	173,359	52,651	-69.6%	-63.5%	73
74 Palos Verdes Estates	64,193	86,890	68,159	-21.6%	6.2%	74
75 Paramount	137,431	145,184	102,185	-29.6%	-25.6%	75
76 Paso Robles	494,265	444,810	382,806	-13.9%	-22.6%	76
77 Pico Rivera	245,339	315,165	243,002	-22.9%	-1.0%	77
78 Pismo Beach	168,686	228,413	189,646	-17.0%	12.4%	78
79 Pomona Valley TA	4,077	3,757	4,280	13.9%	5.0%	79
80 Port Hueneme	284,438	347,670	268,992	-22.6%	-5.4%	80
81 Poway	567,349	670,716	765,921	14.2%	35.0%	81
82 Rancho Palos Verdes	62,449	64,692	64,608	-0.1%	3.5%	82
83 Regional Govt Services	9,154	11,403	12,358	8.4%	35.0%	83
84 Rolling Hills	3,887	4,874	3,436	-29.5%	-11.6%	84
85 Rolling Hills Estates	51,739	64,341	64,366	0.0%	24.4%	85
86 Rosemead	104,375	124,584	140,906	13.1%	35.0%	86
87 San Dimas	78,330	107,071	105,692	-1.3%	34.9%	87
88 San Gabriel	787,610	756,874	681,581	-9.9%	-13.5%	88
89 San Luis Obispo	760,480	898,820	447,075	-50.3%	-41.2%	89
90 Santa Fe Springs	609,662	853,864	779,507	-8.7%	27.9%	90
91 Santa Paula	451,452	435,169	438,183	0.7%	-2.9%	91
92 SCAG	72,596	120,881	2,518	-97.9%	-96.5%	92
93 SEAACA	42,260	69,846	49,780	-28.7%	17.8%	93
94 Seal Beach	451,350	452,331	609,323	34.7%	35.0%	94
95 Seaside	398,675	506,078	431,625	-14.7%	8.3%	95
96 Sierra Madre	161,311	182,913	217,770	19.1%	35.0%	96
97 Signal Hill	239,749	241,415	245,161	1.6%	2.3%	97
98 Solvang	20,606	29,158	861	-97.0%	-95.8%	98
99 South El Monte	39,133	53,557	22,531	-57.9%	-42.4%	99
100 South Pasadena	389,326	395,547	310,646	-21.5%	-20.2%	100
101 Temple City	54,589	42,086	42,813	1.7%	-21.6%	101
102 Ventura Port District	22,617	65,138	23,071	-64.6%	2.0%	102
103 Villa Park	6,417	6,167	7,879	27.8%	22.8%	103
104 Walnut	38,980	48,095	17,687	-63.2%	-54.6%	104

Workers' Compensation Program

2010/2011 Coverage Period

Comparison of Costs between
Current Retrospective Funding Model
and Proposed Prospective Funding Model

Member	Current Model Paid 7/1/2009	Current Model Net Due 7/1/2010	Proposed Model Net Due 7/1/2010	% DIFF. Proposed vs. Current	Proposed Model YOY% vs. 2009	
105 West Hollywood	319,456	360,491	410,523	13.9%	28.5%	105
106 Westlake Village	9,311	11,357	10,982	-3.3%	17.9%	106
Pool	18,483,565	21,543,748	19,866,795	-7.8%	7.5%	

Exhibit 3

Frequently Asked Questions about Revisions to the Funding Model

**California JPIA
Cash Basis Cost of Coverage
Old vs. New Formula Comparison**

Updated 3/15/10

Liability					
		Old Formula	New Formula		
	Amount Paid 7/1/09	Amount Due 7/1/10	Amount Due 7/1/10	Difference Between Old and New Formula	
Funding for Upcoming Year	\$ 33,969,600	\$ 37,098,997	\$ 47,327,000	\$ 10,228,003	27.6%
Rolling Retro Deposits/(Refunds)	8,978,270	12,433,543	(91,939)	(12,525,482)	-100.7%
Total	42,947,870	49,532,540	47,235,062	(2,297,479)	-4.6%

Change in Total Cash Basis Cost of Coverage, YOY From 7/1/09 to 7/1/10 (New Formula) \$ 4,287,192 10.0%

Workers' Compensation					
		Old Formula	New Formula		
	Amount Paid 7/1/09	Amount Due 7/1/10	Amount Due 7/1/10	Difference Between Old and New Formula	
Funding for Upcoming Year	\$ 22,567,742	\$ 24,496,814	\$ 23,789,634	\$ (707,180)	-2.9%
Rolling Retro Deposits/(Refunds)	(4,084,177)	(2,937,418)	(3,903,392)	(965,974)	32.9%
Total	18,483,565	21,559,396	19,886,242	(1,673,154)	-7.8%

Change in Total Cash Basis Cost of Coverage, YOY From 7/1/09 to 7/1/10 (New Formula) \$ 1,402,677 7.6%

Exhibit 2

Cash Basis Cost of Coverage Old vs. New Formula Comparison

California JPIA

Frequently Asked Questions (FAQ) about Revisions to the Funding Model March 18, 2010

In the past five years, Authority members have incurred eighteen claims in excess of one million dollars. In addition, a significant burden has been placed on the Authority's financial resources due to increasing excess insurance costs, the low interest rate environment, and growing long-term receivables resulting from the "rolling retro."

In the fall of 2008, the Executive Committee established an ad hoc committee of managers and finance officers to study the Authority's funding and allocation formulas and to provide recommendations designed to safeguard the financial integrity of the Authority and protect the members.

As a result of the ad hoc committee's extensive study and deliberation, the Authority will be implementing an updated funding model beginning with the 2010-11 coverage period. The new funding model will reflect many of the positive elements of the prior model, and it will eliminate some of its unnecessary complexities. This document provides a brief overview of the changes in the form of FAQs.

1) Question: Please summarize the proposed changes.

Answer: There are several main components to the changes:

- Each new coverage period will be funded through annual contributions. The annual contributions will be funded at the 75% confidence level to assure that the funds collected each year are adequate to pay all losses and expenses related to that year.
- Each member's annual contribution will be based on a formula that reflects that member's exposures and loss experience, *relative to the others in the pool*. Importantly, a credibility weighting factor is being introduced, based on member size, to assure rough equity among members over the long run. Smaller members' exposure (payroll) will be more heavily weighted, while larger members' experience (losses) will receive more weight.
- The rolling retrospective receivables (owed to the Authority by members) will be suspended for the next several years as the annual contribution grows to a fully adequate level.
- Once the annual contribution reaches full funding for the then-current year – which is estimated to take three years – the collection of prior years' retrospective payments will be re-instituted, with the total receivable from members expected to be paid off in the ensuing eight to ten years.

2) Question: What is credibility weighting?

Answer: Credibility weighting is a well-tested industry standard used to avoid adverse selection. More specifically, it is a method used in the formula to determine how much weight should be given to a member's experience (losses) vs. their exposure (payroll). The historical losses of a small agency are not a statistically reliable (credible) indication of that agency's future losses. The new formula recognizes this by assigning various credibility weightings to each member based on the size of their payroll. The minimum weight is 20%, the maximum is 80%. The smallest member's losses will weigh 20% and their payroll 80%. Conversely, the largest member's losses will weigh 80%, and their payroll 20%. All other members will slide on the scale between 20% and 80%, based on the size of their payroll.

The outcome will be that smaller members will have an annual contribution that is less loss-sensitive, while larger members will have an annual contribution that is more loss-sensitive. The use of credibility weighting is considered to be a best practice among public entity risk pools. It is anticipated that allocating costs among members in this way will make the annual contribution a more accurate estimate of the ultimate losses for each member within the coverage period.

3) Question: What is an off-balance factor?

Answer: An off-balance factor is a factor applied to an individual contribution amount to equitably adjust each individual amount in such a way that an overall desired contribution is achieved.

By using an off-balance factor, we are able to ensure that no other aspect of the calculation results in changing the total amount collected. For example, if the funding requirement is \$47 million yet after we run the calculation it results in the collection of \$46 million, then the off-balance factor would be applied to adjust the annual contribution amount of individual members up 2% so that an additional \$1 million is collected, and the full \$47 million funding requirement is achieved.

4) Question: What factors are used in the current formula?

Answer: Both pooled programs use experience (losses) and exposure (payroll) factors in the cost allocation formulas as well as a funding target determined by the actuary's estimate of funding needs. That funding target is allocated to members based on a percentage of their experience and exposure relative to the pool. Since the Authority's inception, simple weightings of both have been used to balance the factors.

The funding mechanism includes a prospective calculation (used to determine each member's primary deposit) and a retrospective calculation (used to collect additional amounts required and reallocate costs among the members). Police and non-police exposures (Liability Program), and public safety and non-public safety exposures (Workers' Compensation Program) are separated in the retrospective calculation. A separate workers' compensation excess pool deposit of .05% of payroll is also collected. Property damage only claims under \$2,000 are excluded from the experience factors in the Liability Program.

5) Question: What factors will be used in the formula that will be implemented in July 2010?

Answer: The new formula continues to use experience (losses) and exposure (payroll) to determine each agency's annual contribution. Experience factors include losses from \$0 - \$30,000 and losses from \$30,000 - \$750,000. Weights given to experience and exposure are more fully detailed in an earlier answer. Funding estimates are calculated separately for police and non-police exposures (Liability Program), and public safety and non-public safety exposures (Workers' Compensation Program). The workers' compensation excess pool deposit will be incorporated into the new funding estimate (and no longer invoiced separately). Smaller claims will no longer have a disproportionate impact on the formula. Therefore property damage only claims under \$2,000 will be included in the experience factors in the Liability Program because the multiplier effect in the previous formula has been eliminated. Once the annual contribution is being funded at the 75% confidence level, the need for retrospective calculations will be eliminated for future coverage periods.

6) Question: What is included in the annual contribution formula?

Answer: The annual contribution formula includes the following: the actuary's estimate of the ultimate claim costs, excess and reinsurance premiums, corridor/reinsurance self-funding (if applicable), expenses associated with the third party administrators, and Authority operating expenses.

7) Question: What is the cost impact going to be?

Answer: The liability formula changes are being implemented in order to manage the *average* increase to a level not to exceed 10% in any one year during the transition period. The formula review ad hoc committee has modeled the implementation such that annual cost increases are anticipated to be at or

below the rate of the pool's payroll inflation. Of course, for any individual member, the actual annual charge will vary based on exposures, experience, and retrospective adjustments due to prior years.

- 8) Question: Without the retrospective adjustments, how will I know that my agency's annual contribution is fair?

Answer: In order to ensure the financial integrity of the Authority and improve annual budgetary stability for members, the new formulas reflect a philosophy of "rough equity in the long run." The Authority has worked with actuaries and pooling experts to design an approach which will reward good risk management practices, penalize bad risk management practices, and achieve rough equity, as this is in the long term best interest of all of the members. The Executive Committee has adopted this approach, based on the work of the Ad Hoc Committee, and believes it is both fair and consistent with the Authority's member-focused philosophy.

- 9) Question: It appears the Authority has plenty of net assets. Why does the Authority need more money?

Answer: Much of the Authority's net assets are currently in the form of receivables from members, and the receivables are growing. The new annual contribution formula will stop their growth by adequately funding each coverage period in advance as originally intended. The goal is to maintain net assets as outlined in the Net Asset and Refund to Members Policies.

- 10) Question: What is the Authority's cash position?

Answer: The growth in member contributions in recent years has not matched the increase in claims and other expenses. From a long-term perspective the overall cash position has been declining; however the Authority's cash position should be sufficient to support the proposed temporary suspension of retrospective deposits when coupled with the the average annual increase of 10% in annual contributions.

- 11) Question: Will there be retrospective calculations in the future?

Answer: Yes and no.

- Coverage periods between 1978-1979 and 2009-2010 will continue to have a retrospective calculation performed until all claims are closed in each coverage period.

- A retrospective calculation will also be performed on the coverage periods during the transition period designed to fully fund the pool. A three-year transition is estimated and would thus include the 2010-2011 through 2012-2013 coverage periods.
- Once the annual contribution reaches full funding at the 75% confidence level, the retrospective calculation will no longer be necessary on future coverage periods.

12) Question: What is the anticipated repayment schedule for the outstanding retrospective deposits receivable, and how long does the Authority intend to suspend the retrospective deposits?

Answer: The plan is to suspend invoicing of the receivables during the transition period, which is anticipated to be three years, and then have the members repay them over the next eight to ten years. The repayment schedule could lengthen or shorten, however, depending on how losses develop. The actual retrospective deposits receivable will be recalculated annually, so each member will know exactly how their respective obligation is changing.

13) Question: Do you intend to freeze the retrospective refunds due to some members?

Answer: No. Refunds due will be paid to members in July for the coverage periods through 2008-2009. Refunds will be distributed based upon the net outstanding retrospective adjustment of each member. The formula review ad hoc committee recommended the decision to provide refunds be made annually in conjunction with the retrospective calculations, and that the amount of the refund also be determined annually.

14) Question: My agency is able to pay its outstanding retrospective contribution now. May we pay it now rather than waiting?

Answer: Yes. Your agency can pre-pay the receivable owed at any time, which could provide an advantage in your budgetary process. While pre-payment is appreciated and encouraged, incentives are not being offered for pre-payment.

15) Question: What happens if my agency withdraws from the Authority or a program?

Answer: Members that withdraw will not enjoy the benefit of paying retrospective deposits in installments as is provided under the "rolling retro," nor would payment obligations be deferred during the transition period. Thus any receivable due will be due and payable upon withdrawal. Members that withdraw from a program will continue to have retrospective obligations

annually until the all claims close for each coverage period of program participation.

16) Question: What coverage alternatives does my agency have if we decide to withdraw from the Authority?

Answer: The Authority has a one-year withdrawal notification, and withdrawal from a program may only be made at the end of a fiscal year. Commercial markets and other pools may offer alternative coverage options for your agency. Authority staff can provide appropriate assistance to your agency should you wish to conduct a comparison of alternatives.

17) Question: What are the Authority's financial targets? How will we know when there is enough money?

Answer: Consistent with the existing Net Asset and Refund to Members Policies, the Authority has adopted a target to build up to, and then maintain, net assets equal to a 95% confidence level. The exact dollar amount will change, over time, reflecting each program's accumulated loss experience. Both policies will be reviewed in conjunction with the implementation of the formula revisions.

18) Question: What will happen if the Authority becomes "over" funded?

Answer: Net assets will be evaluated annually, and any excess will be handled in accordance with the Net Asset and Refund to Members Policies.

19) Question: How will the members' loss prevention efforts be recognized?

Answer: The new formulas still reflect each member's annual loss experience – from 20% weight for the smallest members to 80% weight for the largest members. Your agency's actual costs will continue to be significantly influenced by your loss prevention efforts. Also, for past coverage periods, the retrospective payments due will be materially impacted by how the claims actually resolve, so continued diligence and cooperation with the claims management process is critical.

20) Question: My agency's losses have been trending downward. Will our costs increase?

Answer: As you may be aware, the Authority's members have sustained a number of large losses over the past few years. In addition, the reinsurance market has

hardened and Authority has experienced reduced investment income. These elements combined have negatively affected our actuary's estimate of future funding requirements as well as increased the premiums for insurance the Authority is able to secure from the marketplace. It is anticipated that these developments will lead to increased contributions by the members.

21) Question: How will members that join the pool after July 1, 2010, be treated?

Answer: They will pay annual contributions as determined by the new funding formulas.

22) Question: Has the Authority's growth over the past ten years caused this problem?

Answer: No. The addition of members to the pool during the past ten years has actually benefited existing pool members as costs have been spread over more agencies. Our strict underwriting process assures this and the Authority will continue to entertain "good" growth opportunities.

23) Question: If only 20% of a small member's annual contribution is based on their loss history, does this mean that effective loss control at their agency no longer makes a difference?

Answer: Effective loss control continues to make a difference. Members can and do influence their share of the funding estimate by maintaining or establishing best risk management practices in their locale. The best way to minimize future increases is to do everything possible to avoid costly claims. Adoption of best risk management practices will reduce claim severity in most cases. A reduction in future funding estimates is directly tied to a reduction in the severity of claims experienced by the pool and its members. Also, for past coverage periods, the retrospective payments due will be materially impacted by how the claims actually resolve, so continued diligence and cooperation with the claims management process is critical.

24) Question: Where does my agency fall on the sliding credibility weighting scale? Is my agency categorized as small, medium, or large?

Answer: The 2010-2011 Coverage Period Annual Contribution spreadsheets, located at <http://members.cj pia.org/Resources/Retro.aspx>, contains the credibility weighting scale for each member.

25) Question: Are claim reserves included in the loss data used to calculate the annual contribution?

Answer: Yes. The annual contribution formula takes into consideration the most recent five years of Net Incurred Losses.

$$\text{Net Incurred Losses} = \text{Actual Paid} + \text{Reserves} - \text{Recoveries}$$

The maximum amount counted per occurrence is limited to \$750,000 in the liability program and \$100,000 in the workers' compensation program. The Authority utilizes the same third party administrators for all claims within each coverage program; as a result, reserving practices are consistently applied to all members. In addition, reserves are periodically reviewed and evaluated by both staff and the claims committee for sufficiency and consistent application.

26) Question: If the aggregate funding target for 2010-11 will not be achieved at the 75% confidence funding level through the annual contribution, and on a pool-wide basis we actually plan to collect less than the target, why is the total not at least equal to the amount that would have been collected under the old formula?

Answer: The ad hoc committee focused on long-term solutions, particularly the desire to fund upcoming coverage periods at higher confidence levels. The proposed funding formula achieves that when compared to the current funding model. The lower cash collection is due to the suspension of the collection of retrospective receivables. This suspension was a conscious decision in recognition of the current economic conditions.

27) Question: Some members have participated in the pool for over 25 years and have experienced relatively few claims, with minimal incurred costs with the exception of the most recent few years, in which their losses have increased dramatically. Since the annual contribution only includes five years of claims experience in the calculation, are these long-time members with good overall claims experience, being penalized strictly based on their most recent few years of claims activity?

Answer: Stellar loss experience is recognized under the current formula, and the benefits have already been realized by members for past coverage years through retrospective refunds and lower primary deposits. Unfortunately the past several years of adverse loss experience are not isolated to one or two members; loss trends pool-wide have been negative. Industry standards include the recognition of the previous five years of loss experience as a reliable predictor of future loss experience (the Authority's excess and

reinsurance carriers request the previous five years of loss experience). In addition, extraneous factors, such as the legal environment, make the previous five years the most relevant for the purposes of estimating future costs.

28) Question: Is there a correlation between deferred maintenance/poorly maintained streets and public facilities and the rising cost of claims?

Answer: Deferred maintenance and aging infrastructure is playing a role in claims under \$750,000. Causes for the multi-million dollar claims are varied, and in many instances the member involved had a slim percentage of liability. Joint and several liability and the absence of another responsible party with assets, however, resulted in the pool being responsible for the settlements/judgments.

29) Question: Does the annual contribution establish a new higher baseline for subsequent calculations in future years? Is it possible for it to come down, given the planned pool-wide increase of 10% each year? Will my agency be able to influence that number and make it lower?

Answer: It is expected that the Liability Program cost, at the pool level, will increase 10% each year for the next three years. In the third year, it is projected that the program will be collecting its actuarially determined funding estimate at a 75% confidence level. Due to the fact that the funding estimate will include a provision for adverse fluctuations in claim costs (e.g. moving from 50% to 75% confidence level funding), the baseline for subsequent calculations will be higher. Prefunding at a higher confidence level diminishes the potential for large retrospective deposits during the transition period as well as future pool assessments.

Over the same time period, individual member's contributions may or may not increase by the amount the pool must increase. Some may experience increases beyond that of the pool as a whole, while others will increase less, and some may see no increases. Factors that will determine how much individual increases will be include 1) an agency's payroll growth relative to the pool's payroll growth, 2) an agency's loss history relative to the pool's loss history and relative to its own loss history, 3) the volatility bands used to limit individual member's annual increases, and 4) the off-balance factors used to ensure the full collection of the funding estimate.

Ultimately, the pool's losses are the largest component of the actuary's funding estimate. As the pool's relative loss history improves, the actuary's funding estimate will flatten out and may even decline. An example of this was seen in the Worker's Compensation program funding estimates from 2004/05 through 2009/10. Assuming that were to happen in the liability program, the relative performance of each agency, using the factors noted

above, against the pool will determine the answer to whether a member will see a decrease in their liability program cost.

Finally, members can and do influence their share of the funding estimate by maintaining or establishing best risk management practices in their locale. The best way to minimize future increases is to do everything possible to avoid costly claims. Adoption of best risk management practices will reduce claim severity in most cases. A reduction in future funding estimates is directly tied to a reduction in the severity of claims experienced by the pool and its members.

30) Question: Should there be consequences for members who do not report claims?

Answer: All members are obligated to report claims. The Memorandum of Liability Coverage states the following in Section 5 Conditions and Responsibilities: C. (ii). If a **Claim** is made against a **Protected Party**, the **Protected Party** shall immediately forward to the **Authority's** Claims Administrator every demand, notice, summons or other process received by the **Protected Party** of the **Protected Party's** representative.

In addition, the Authority consistently reviews the members' risk and exposures, and has developed a systematic system to ensure the members are performing due diligence. Through the Risk Management Evaluation process and the Loss Control Action Plan, members receive individual assistance in identifying potential liability, property, and workers' compensation issues and are reminded of pool protocol such as the obligation to report claims.

31) Question: The retrospective balances are calculated separately for liability and workers' compensation, and it is possible for a member to have a retrospective deposit due in liability, yet have a refund in workers' compensation. While the programs are calculated separately, will the invoice still combine them in such a way I can make a single payment? When will we be invoiced for the 2010-11 coverage year?

Answer: The invoice will combine both self-insured programs (liability and workers' compensation), and will net the total amounts due with applicable refunds. The 2010-11 invoices will be distributed to members in May.

32) Question: At present, the economic environment is very challenging for most members. Why do the formula changes need to happen now?

Answer: The current model is not sustainable. The cash flow implications of the current model could compromise the Authority's ability to pay claims within the next few years.

33) Question: How can we protect the pool from members who consistently have bad losses year after year, and who do not demonstrate a commitment to risk management?

Answer: The Authority actively assists the members by identifying, assessing, and assisting the members in controlling risk and exposures. A combination of systematic and ad hoc methods are incorporated into both methods to perform risk management due diligence. Systematic methods include the Risk Management Evaluation (RME), Loss Control Action Plan, training opportunities, and our annual Risk Management Awards. Ad hoc methods include the provision of risk management consulting services, review of incident reports and underwriting report submissions, provision of white papers, legal review and assistance, and so on. Loss analysis and trends are integral parts of the systematic methods. Since the RME is member-specific, analysis of individual losses is provided to give greater clarity and focus to areas of liability or worker safety that are most in need of attention.

In some instances, it may be appropriate for the Authority to actively intervene in the member's risk management efforts, or even require the member to address serious operational issues through a Performance Improvement Plan (PIP). For any member that was unsuccessful in completing the PIP, recommendations may be made to the Executive Committee to endorse the Memorandum of Coverage excluding coverage for activities or conditions of the member deemed to impose unreasonable risk on the Authority. This may include the imposition of specific copayments, deductibles, coverage limitations, or program participation cancellation.

When every effort fails to improve the performance of a member, the Authority's Joint Powers Agreement has a mechanism by which to cancel member participation in either a program or the pool. The primary interest in cancelling a member stems from a common belief that the other members will pay more if poor-performing members are allowed to remain in the pool. Also of concern is the pool's perceived image and the members' desire to have well-managed and respected members participating.

34) Question: Under the new annual contribution formula, will small members end up subsidizing large members or vice versa?

Answer: No. Small members will not subsidize large members, and large members will not subsidize small members. Variable credibility weighting is specifically included within the new annual contribution formula to ensure that rough equity is achieved on a long-term basis, and that each member receives a fair estimate of cost allocation using their relative share of both experience and exposure.

35) Question: Should interest be charged to members on their retrospective deposit balances?

Answer: Members with significant deferred balances are benefiting to a larger degree than members with smaller balances. Charging interest is one way to address this question of relative fairness, with the added benefit of supplementing the Authority's interest income from the investment portfolio. This option may also serve as an effective incentive for early re-payment of outstanding balances. The formula review ad hoc committee and Executive Committee will continue to analyze this concept in the coming months.

36) Question: Would a more simple approach to changing the formula be equally as effective at addressing the core problems, such as removing the caps on the primary deposit or eliminating the rolling retro?

Answer: The ad hoc committee considered these options, however, it was determined that completely removing the caps would result in unwanted excess volatility at the member level. By keeping the caps in place yet widening them, and shifting them upward, an effective balance was reached between preventing excess volatility, attaining aggregate funding sufficiency, and allowing the claims experience of individual members to impact their cost.

In light of the difficult economic environment, the ad hoc committee decided that all retrospective deposits due to the Authority should be temporarily suspended until the annual contribution reaches target funding levels over the next three to five years, at which time repayment of retrospective deposits should resume. It is anticipated that the combination of members paying a higher annual contribution under the new formula, and simultaneously being required to pay down aggregate retrospective balances would be too heavy of a burden, particularly given the severity of fiscal challenges which many members are facing.

In addition, a simple approach does not address other important issues that were uncovered through the modeling and analysis conducted by the ad hoc committee, particularly the fairness of the old cost allocation model as it relates to its exclusion of losses in the second layer, and its application of

equal credibility weighting to all members despite their non-homogeneous payrolls.