INDEPENDENT CITIES
RISK MANAGEMENT
AUTHORITY

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ICRMA
Net Asset Policy

March 1, 2018

Change Record

Date	Description
10/19/2011	Initial approval of the policy by the ICRMA Board
03/01/2018	As part of the Governing Documents project, ICRMA worked to align its various policy documents and ensure that the right content was in the right place without unnecessary repetition. The original Net Asset policy did not contain the calculation language but rather referred to the bylaws for this detail. The change approved March 1, 2018 placed the calculation details into the policy document. At the same time, the bylaws approved that day removed the provisions providing details re calculation of dividends and bylaws. The revised net asset policy went into immediate effect following approval.

A. Introduction

This policy and procedure document shall be treated as one of **ICRMA's Governing Documents** and, as such, shall have the same effect as the **Joint Exercise of Powers Agreement for Insurance and Risk Management Purposes (Agreement)**, the **ICRMA Bylaws** and **Memorandum of Coverage (MOC)**.

If any provision of this document conflicts with the **Agreement**, the **ICRMA Bylaws** and **Memorandum of Coverage (MOC),** the then current version of those documents govern whenever approved.

B. Purpose

1. The purpose of this policy statement is to give guidance to the Board in making annual funding, dividend and assessment decisions for the ICRMA pooled liability and workers compensation programs. By adoption of this policy statement, the Board acknowledges the long-term financial strength of the ICRMA pooled program is of utmost importance.

2. The Board relies heavily on actuarial estimates when making financial decisions. Such estimates, though professionally developed, contain uncertainty due to the random nature of liability claims, the ICRMA's significant self-insured retention level, possible data errors, inaccurate case reserving and other unknowns. Accordingly, the Board desires to fund the ICRMA pooled programs in a cautious and prudent manner and return equity to its Members in an equally cautious and prudent manner. ICRMA seeks to conservatively fund the outstanding liabilities of its pooled programs and to maintain net assets sufficient to absorb substantial fluctuations from estimates.

3. To fund program years in a fiscally prudent manner, ICRMA collects contributions at an actuarially determined confidence level as determined by the Board annually. The ICRMA Board strives to annually collect at the <u>70% confidence level or higher</u> for the **liability program** and the <u>80% confidence level or higher</u> for the **workers compensation program** as determined by the actuary.

4. In addition, as provided in the ICRMA governing documents, dividends may be declared and paid solely at the discretion of the Board provided that the net assets of the program plus the reserves for unpaid losses, after dividend, equals or exceeds a <u>90% confidence level</u> (discounted for the liability program and undiscounted for the workers compensation program).

5. Nothing in this policy statement shall be applied or construed to require or mandate the Board to return Equity to the members in any particular year. Rather, the Board retains the sole discretion and authority to determine from year-to-year whether to return Equity based on the principles and policies in this policy statement and **ICRMA Governing Documents**.

C. Definitions

1. "**Claims Paid to Date**" is the amount actually paid on reported claims at the date of valuation. "Claims Paid to Date" includes those amounts paid for both defense and indemnity of claims.

2. "**Confidence Level**" is a statistical term used to express the degree to which an actuarial projection (usually "Ultimate Net Loss" or "IBNR") will be an accurate prediction of the dollar losses ultimately paid for a given program year or combination of years. The higher a "Confidence Level" the greater certainty the actuary has that losses will not exceed the dollar value used to attain that "Confidence Level".

3. "**Equity**" or "**Net Assets**" is the amount of assets remaining, after deducting all liabilities, including liabilities of unpaid losses discounted for investment income and estimated at the actuarially determined "Expected" or "Central Estimate" "Confidence Level".

4. "**Expected**" by industry standard translates roughly to the 50% to 56% "Confidence Level" as determined by the independent actuary.

5. "**Expected Liabilities**" is the total of all "Outstanding Reserves", "IBNR", discounted, at the "Expected" "Confidence Level" and "ULAE".

6. "**Incurred But Not Reported (IBNR)**" is the estimate of the funds needed to pay for covered losses that have occurred but have not yet been reported to the member and/or ICRMA. "IBNR" includes (a) known and unknown loss events that are expected to

be claims; and (b) expected future development on claims already reported.

7. "**Net Contribution**" includes the total contributions from Members less the excess insurance cost.

8. "**Net Present Value**" is the discounting of future cash flows to current values by taking into account the time-value of money.

9. "**Self Insured Retention**" is the maximum amount of exposure to a single loss retained by ICRMA.

10. "**Outstanding Reserves**" are the sum total of unpaid case reserves in the "Self Insured Retention" as determined by the ICRMA Claims Manager.

11. "**Ultimate Net Loss**" is the sum of "Claims Paid to Date", "Outstanding Reserves", and "IBNR", all within ICRMA's "Self Insured Retention". It is the estimate of the total value of all claims that will ultimately be made against Members for which ICRMA is responsible.

12. "**Unallocated Loss Adjustment Expenses (ULAE)**" are settlement expenses that cannot be directly attributed to individual claims.

D. Important Net Asset Ratios

The Board will only consider returning "Equity" to the Members after evaluating and concluding the following ratios remain appropriate for the group prior to and following any potential return of "Equity":

1. **"Net Contributions" to "Net Assets" ratio: Target ≤ 2:1.** This ratio is a measure of how "Net Assets" compare to the rate at which the pool is taking on risk (or growing), measured by the current annual volume of contributions, less contributions passed through to reinsurers or insurers. A low ratio is desirable.

2. **"Outstanding Reserves" to "Net Assets" ratio: Target ≤ 3:1.** This ratio is a measure of how "Net Assets" are leveraged against possible reserve inadequacies. A low ratio is desirable.

3. **"Net Assets" to "Self Insured Retention" ratio: Target ≥ 5:1.** This ratio measures how conservative the "Net Asset" position is by virtue of how many retained occurrences the "Net Asset" amount could absorb. A high ratio is desirable.

4. **Reserve Development: Target ≤ 20%.** This is a measure of the change in aggregate ultimate losses from one valuation period to the prior valuation(s). Generally, the one-year and two-year reserve development to "Equity" threshold should be less than 20%. A low ratio is desirable.

5. **Change in "Net Assets": Target ≥ -10%.** This ratio measures the stability "Net Assets," from recent events. A decline in excess of 10% may signal a new adverse trend and warrant consideration of more conservative financial decisions in the near term. A positive or low-negative ratio is desirable.

6. **Annual Actuarial Study –** ICRMA will engage credentialed actuaries with appropriate experience to perform annual actuarial studies to assist the Board in making funding decisions.

E. Calculating Dividends & Assessments

1. **Criteria** – After annual review of the "Net Asset" position of the pooled programs, the program years to be adjusted and the important ratios, the Board will determine whether it is desirable to increase, decrease, or stabilize "Net Assets". If the Board desires to decrease "Net Assets", by returning "Equity" to the Members, it will not return funds from any given program year that will cause the funding of the program as a whole to fall below the 90% "Confidence Level".

2. **Definition & Limitations** – Dividends and assessments are defined and their limits spelled out in **ICRMA's Bylaws**.

3. **Dividends**
   - **a** ***Availability* –** The Board may declare dividends **ONLY** when funds available to a specific program exceed those available to pay for losses exceed known claims, and actuarially sound provisions exist for case development, for IBNR, for unexpected management expenses, and for unrestricted surplus. Specifically, dividends are available to be declared **ONLY** at such time as the program has equity, with liabilities actuarially stated undiscounted at a 90% confidence level.

b ***Calculation –*** The first dividend calculation may be performed five (5) years after the end of the program year. Additional calculations may be made each year thereafter until such time as the program year is closed.

  i The calculated amount represents the maximum dividend available to be declared.

  ii This amount shall be reduced if the two (2) succeeding years (after the fifth program year reaches eligibility) have negative equity, with liabilities actuarially stated at an expected confidence level.

  iii Each Member's share of any dividends shall be allocated based upon the method by which the contributions were collected, beginning with the oldest program year.

  iv However, until the last claim of a program year has been paid and the program year has been closed, the program year must maintain sufficient funds to satisfy the 90% confidence level discounted requirement.

c ***Distribution –*** Each Member's share of any dividends shall be allocated based upon the method by which the deposit premiums were collected, beginning with the oldest program year. However, until the last claim of a program year has been paid and the program year has been closed, the program year must maintain sufficient funds to satisfy the 90% confidence level discounted requirement.

4. Assessments

a ***Availability –*** The Board may levy assessments on the participants of any program year(s) when:

  i It is determined by the actuary that any program year is no longer actuarially sound; **OR**

  ii An accountant, auditor and/or other financial services provider advises that the assets of a program, as a whole, do not meet the expected discounted losses; **OR**

  iii Facts or circumstances appear such that the Board concludes that levying an assessment would be fiscally prudent.

In addition, the Board reserves the right to assess the Members of any program an amount determined by the Board to be necessary for the soundness of the program and to allocate such assessment to the Members in a fair and equitable manner.

b ***Calculation*** – There is no requirement that the program year be closed prior to making an assessment.

  i Each Member's share of the assessment shall be allocated based upon the method by which the annual contributions were collected for the risk-sharing layer of each program year being assessed.

  ii If such assessment is not sufficient to relieve the pool of its actuarially determined deficit in the year of the assessment, such assessment shall be levied each subsequent year until the actuarial deficit is relieved.

c ***Implementation*** – The Board determines the timing of the payment at the time the assessment is levied as well as any potential interest to be assessed on late payments.

F. Amendment

Unless otherwise specified all financial policies, approved by the Board, shall be reviewed and reaffirmed or modified at least once every three (3) years.