

# **MISSOURI PUBLIC ENTITY RISK MANAGEMENT FUND MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)**

Management of the Missouri Public Entity Risk Management Fund (MOPERM) offers this narrative overview and analysis of the financial activities of MOPERM for the fiscal year ended December 31, 2007. We encourage readers to consider the information presented here in conjunction with MOPERM's financial statements and notes to the financial statements to enhance their understanding of MOPERM's financial performance.

## **Fund Accounting**

A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. MOPERM, a corporate and political body created by the Missouri General Assembly, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. MOPERM is not considered to be a component unit of the State of Missouri. There are three categories available for governmental accounting: governmental funds, proprietary funds and fiduciary funds. MOPERM's funds are considered proprietary funds.

*Proprietary funds.* Proprietary funds account for governmental operations that are designed to be self-supporting from fees charged to consumers of the provision of those goods and services or where the government has decided that the periodic determination of revenues, expenses, and net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes. The accounting and financial reporting practices of proprietary funds are similar to those used for business enterprises and focus on capital maintenance and the flow of economic resources through the use of accrual accounting. Of the two types of proprietary funds, MOPERM maintains one type: Enterprise Fund. MOPERM's purpose is to provide liability and property insurance coverage to participating public entities, their officials and employees.

## **Overview of the Financial Statements**

This discussion and analysis is intended to serve as an introduction to MOPERM's financial statements. Typically, government financial statements would be presented as three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. However, as MOPERM uses only Proprietary funds, which present financial statement information in the same manner as government-wide financial statements only with more detail, we do not present government-wide financial statements as the information would be repetitive.

The financial statements, in addition to management's discussion and analysis, are comprised of the balance sheet; the statement of operations and changes in retro return reserve; the statement of cash flows and the notes to financial statements. The financial statements are prepared on the accrual basis in accordance with U.S. generally accepted accounting principles applicable to governmental enterprise funds.

The balance sheet presents MOPERM's financial position as of the end of the fiscal year. Information is displayed on assets and liabilities, with the difference between the two reported as retro return reserve. The retro return reserve of MOPERM reflect the resources available as of the end of the fiscal year to pay claims of participants when due. Over time, increases and decreases in retro return reserve measure whether MOPERM's financial position is improving or deteriorating.

The statement of operations and changes in retro return reserve presents information detailing the revenues and expenses that resulted in the change in retro return reserve that occurred during the current fiscal year. All revenues and expenses are reported on an accrual basis. This means that the revenue or expense is recognized as soon as the underlying event giving rise to the change occurs, regardless of when the actual

cash is received or paid. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods. For example, contributions due from a public entity, even though not yet paid by fiscal year end, will be reflected as revenue. Likewise, claims that occurred during the fiscal year under self-insured plans will be reflected as an expense, whether or not they have been paid as of the end of the fiscal year.

The statement of cash flows presents the cash provided and used by MOPERM categorized by operating activities, noncapital financing activities, capital and related financing activities, and investing activities. It reconciles the beginning and end-of-year cash balances contained in the balance sheet. The effects of accrual accounting and noncash activities, such as depreciation, are adjusted to supplement the presentation in the statement of operations and changes in retro return reserve.

The notes to financial statements follow the basic financial statements and provide additional information that is essential to a full understanding of the data provided in the financial statements.

In addition to the financial statements and accompanying notes, required supplementary information is presented illustrating MOPERM's past ten years of earned revenues and investment income compared to related costs of loss and other expenses incurred by MOPERM.

### Financial Analysis

The following tables present the summarized financial position and results of operations for the fiscal years ended December 31, 2007 and 2006. Additional details are available in the accompanying financial statements.

	2007	2006	Increase (Decrease)
<b>ASSETS</b>			
Cash and investments	\$ 85,475,887	\$ 68,147,445	\$ 17,328,442
Receivables	1,801,359	2,940,712	(1,139,353)
Capital assets	1,193,041	1,253,549	(60,509)
Other	13,236	214,122	(200,886)
Total assets	<u>\$ 88,483,523</u>	<u>\$ 72,555,828</u>	<u>\$ 15,927,695</u>
<b>LIABILITIES</b>			
Loss and loss adjustment expense	\$ 45,211,346	\$ 38,487,098	\$ 6,724,248
Other	10,263,235	8,886,479	1,376,756
Total Liabilities	<u>55,474,581</u>	<u>47,373,577</u>	<u>8,101,004</u>
<b>RETRO RETURN RESERVE</b>			
Designated catastrophic reserves	22,846,683	20,585,098	2,261,585
Invested in capital assets	1,193,041	1,253,549	(60,509)
Undesignated	8,969,218	3,343,604	5,625,614
Total retro return reserve	<u>33,008,942</u>	<u>25,182,251</u>	<u>7,826,691</u>
Total liabilities and retro return reserve	<u>\$ 88,483,523</u>	<u>\$ 72,555,828</u>	<u>\$ 15,927,695</u>

- MOPERM was established to offer liability protection to participating public entities, their officials and employees. MOPERM has been successfully providing member entities with broad coverages at stable and economical rates. Effective July 1, 2003, MOPERM's Board of Trustees approved the offering of property insurance coverage to its members. MOPERM increased its overall membership by 5 members during 2007, compared to an 18 member increase during 2006. The additional

members added in 2007 were relatively small entities. Total assets increased by \$15,927,695 in 2007 to \$88,483,523. The total increase in assets during 2006 was approximately \$10,600,500. Net loss and loss expense paid in 2007 was less than the amount paid in 2006 which resulted in an increase in cash for investments. During 2007, receivables decreased by \$1.1 million dollars. The majority of this decrease is due to a payment of approximately \$1.2 million received in 2007 from a previous excess liability insurance carrier. The receivable from the excess liability carrier as of December 31, 2007 approximated \$855,000. Capital assets decreased in 2007 due to the retirement/sale of old equipment, computers and one automobile. Other assets decreased by \$200,886 in 2007. This is the result of not prepaying 2008 premium for earthquake excess insurance.

- Total liabilities increased by \$8,101,004 in 2007 to \$55,474,581. The increase in liabilities was primarily associated with an increase in loss and loss adjustment reserves for the liability line of business. MOPERM reserves 75% of annual liability contributions to pay claims. This percentage conservatively reflects past claims history. This reserve is reviewed annually by an independent actuary. The majority of the increase in Other Liabilities is unearned member contribution. MOPERM has no long term debt.
- Retro Return Reserve for 2007 increased by net income of \$7,826,691. Since its inception, MOPERM has refunded over \$7 million of contributions to the participating members. MOPERM's Board of Trustees did not declare a dividend in 2007.

	2007	2006	Increase (Decrease)
<b>OPERATING REVENUES</b>			
Contributions	\$ 22,349,103	\$ 21,923,084	\$ 426,019
Investment income	3,592,599	2,605,586	987,013
Other income (expense)	4,323	2,500	1,823
Total operating revenues	<u>25,946,025</u>	<u>24,531,170</u>	<u>1,414,855</u>
<b>OPERATING EXPENSES</b>			
Loss and loss adjustment expense	14,886,164	15,111,851	(225,687)
Excess insurance premiums	1,378,279	1,119,915	258,364
General and administrative	2,995,868	3,004,756	(8,888)
Total operating expenses	<u>19,260,311</u>	<u>19,236,522</u>	<u>23,789</u>
Net operating income	6,685,714	5,294,648	1,391,066
Unrealized gain on investments	<u>1,140,977</u>	<u>209,084</u>	<u>931,893</u>
Net income	<u>\$ 7,826,691</u>	<u>\$ 5,503,732</u>	<u>\$ 2,322,959</u>

- Contributions earned for 2007 increased by \$426,019. Approximately \$489,136 of the increase was attributed to the property line of business through addition of new members and a rate increase due to increases in earthquake excess premiums. Liability contribution was a negative (\$63,117) for 2007 due to no contribution rate change and the loss of some mid size members.
- MOPERM has invested approximately \$79.3 million, primarily in U.S. Government Agency Securities with final maturities of seven years or less with a one time call. Investment income consists of interest income, amortization of premium and discounts on bonds, and realized gains and losses on securities. Investment income for 2007 increased by \$987,013 due to an increase in total investments held by MOPERM. Because of the changes in interest rates in the investment market, MOPERM experienced an unrealized gain on investments of \$1,140,977 during 2007.

- Loss and loss adjustment expense decreased by \$225,687 in 2007. MOPERM paid out approximately \$663,000 less in claims in 2007 than 2006.
- Excess insurance premiums increased by \$258,364 in 2007. In 2007, MOPERM experienced increased rates on earthquake excess in the property line of business. The premium for excess insurance for property increases as new members are written.
- General and administrative expenses approximated 13.4% and 13.7% of total contributions earned for 2007 and 2006, respectively. These expenses decreased by \$8,888 in 2007. The majority of this decrease was due to decreased depreciation expense and maintenance services offset by increases in legal services, commission expense and other outside services.

## **FINANCIAL SUMMARY**

In 2007, MOPERM experienced some growth, adding a few new members and \$426,000 in contribution earned. Liability rates remained constant while property rates increased due to increased rates on earthquake excess premiums. MOPERM had a total of 927 contributors as of December 31, 2007. The growth in contribution revenue is attributed to the increase in the contribution rates for property.

Net income increased by \$2,322,959 even though MOPERM only had a \$426,019 increase in contributions. This is due primarily to the increase in investment income and unrealized gain on investments. The general and administrative expenses were down slightly from 2006 and loss and loss adjustment expense was less in 2007. Retro return reserves increased by \$7,826,691 in 2007. Overall, the financial position of MOPERM remains very stable.

## **Economic Environment and Next Year's Budget and Rates**

Since 1987, MOPERM has been a competitive alternative for local government agencies seeking to manage rising coverage costs against growing exposures and tight budgets. Rates are analyzed by an actuary each year and rate recommendations are made to management. Management analyzes the actuary's rate recommendations and suggests rate changes based on actual loss experience and the current insurance market.

The 2008 estimated contribution was down about 8% compared to the final 2007 contribution amount. The decrease was the anticipation of losing some of the larger members and the softening of the current market. Companies have re-entered the public entity market sector where there has been little interest the past few years. The total operating expenses are budgeted to rise about 3.2% to \$4.5 million over the final 2007 operating expenses of \$4.3 million. The largest increments are commission expense, excess insurance premiums, and salary and benefits. The total operating expenses are about 21% of total budgeted contribution. The loss and loss expense percentage remains constant at 75% of budgeted contribution each year. There have been no major insurance program changes for 2008.

## **Contacting the Fund's Financial Management**

This financial report is designed to provide our members and the public with a general overview of the Fund's finances and to demonstrate the Fund's accountability for the contribution it receives. If you have questions about this report or need additional financial information, contact the Fiscal Manager, Cathy Schulte, at PO Box 7110, Jefferson City, MO 65102, (573)751-1266 ext. 114 or e-mail [Cathy-Schulte@moperm.com](mailto:Cathy-Schulte@moperm.com).