

MEMBERSHIP Matters



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A PERSPECTIVE ON EXAMINING RISK HISTORY

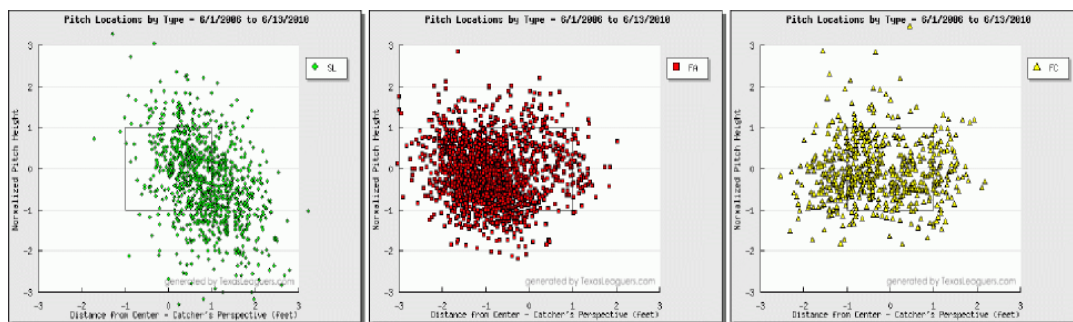
(Editor's note: The following article is extracted from an article on Reinsurance Structure Analysis written by Joel Kress, ARe, Underwriting Manager for Government Entities Mutual (GEM). The complete article is available in the Articles of Interest area at www.agrip.org.)

To be in the business of risk transfer, we must understand the very nature of risk. Although we feebly attempt to simulate, mitigate and regulate risk, we will never be able to eliminate it. It is for this very reason that understanding it, and knowing how others are measuring it, is important for those buying financial protection against catastrophic risk. Reinsurance contracts can cost a considerable portion of the primary risk transfer premiums; and, when properly analyzed and purchased, they can be an effective component in protecting the financial soundness of a risk bearing organization.

The process of making a reinsurance purchasing decision is typically: gather historical information, analyze and compare it, and select a self insured retention based on the presumption that the future should behave like the past. Risk is the undeniable fact that the future will NOT behave like the past.

Trying to be a little less obtuse, we should examine risk as reinsurers do. With the advent of computers and microprocessors, we are able to analyze historical data in a very complex manner.

As an example, let's take a baseball pitcher throwing baseballs over home plate during a baseball game. The object of the pitcher is to throw the ball in the strike zone, which is an imaginary box the width of home plate from the batter's shoulders to his knees. During a game a pitcher throws about 140 pitches, and roughly two-thirds of them are strikes. But, let's look at the actual results of those 140 pitches by three different pitchers.



The first pitcher drifted around the right side of the strike zone, the second was drifting left and the third pitcher was about even in his strike placement. So, based on this finite data we can say that over the course of a game, a pitcher has approximately a 2/3rd's chance of getting a strike. These are pretty good odds. But, now look closer at the outlier balls in the extremes of the graphs. There is a 7/140 or 5% chance of not just a "ball", but a pitch so wild that it threatens the safety of all those around home plate.

Through computer modeling, reinsurers are able to simulate not just what a couple of pitchers will pitch in a single game, but what happens if we compile every pitch (140) by every pitcher (2 pitchers) in every game (say, 162 games) since the invention of professional baseball (say, 100 years).

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AGRiP Members are listed in the **Membership** area and their websites are available in the **Links** area at www.agrip.org.

Association of Governmental Risk Pools

STATEMENT OF FINANCIAL POSITION

as of December 31

<i>Assets</i>		<i>2010</i>	<i>2009</i>
Cash and cash equivalents	\$	328,172	285,287
Investments - Certificates of deposits		607,685	508,532
Accounts receivable		5,961	1,526
Prepaid expenses		102,463	102,106
Inventories		2,535	5,229
Total current assets		<u>1,046,816</u>	<u>902,680</u>
Noncurrent assets:			
Capital assets, net of accumulated depreciation		12,751	18,354
Utility and lease deposits		730	730
Total noncurrent assets		<u>13,481</u>	<u>19,084</u>
Total assets		<u>1,060,297</u>	<u>921,764</u>
<i>Liabilities and Net Assets</i>			
Current liabilities:			
Accounts payable and accrued liabilities	\$	59,754	59,424
Deferred revenue		307,421	360,035
Total current liabilities		<u>419,789</u>	<u>366,845</u>
Net assets:			
Unrestricted		640,508	554,919
Total net assets		<u>640,508</u>	<u>554,919</u>
Total liabilities and net assets		<u>1,060,297</u>	<u>921,764</u>

STATEMENT OF ACTIVITIES

<i>Revenues</i>			
Dues	\$	484,449	450,138
Spring conference		140,304	134,427
August institute		60,865	58,650
Governance conference		217,965	210,156
Quality Education Initiative		79,536	107,288
Online subscriptions		22,700	22,700
Interest income		8,758	11,410
Other		15,855	22,093
Total revenues		<u>1,034,732</u>	<u>1,016,862</u>
<i>Expenses</i>			
Spring conference		108,894	109,796
August institute		68,146	86,759
Governance conference		151,806	163,145
PRIMA conference		3,986	3,897
Salaries and wages		344,999	363,793
Payroll taxes and benefits		139,126	151,733
Administration		57,375	49,711
Research consulting		23,260	29,987
Legal and professional		14,892	10,941
Office lease		16,988	16,233
Board expense		13,505	26,182
Depreciation		5,603	5,696
Other		563	1,085
Total expenses		<u>949,143</u>	<u>1,018,958</u>
Change in net assets		<u>85,589</u>	<u>(2,096)</u>
Net assets at beginning of year		<u>554,919</u>	<u>557,015</u>
Net assets at end of year		<u>640,508</u>	<u>554,919</u>

FROM THE POOLSIDE

It appears that two new members will be elected to the AGRiP Board of Directors later this year when member Designated Representatives vote during November for nominees for two positions with terms to begin January 1, 2012. Current director **Steve James**, Deputy Director of the Maryland Association of Boards of Education (MABE), is ineligible to continue on the board since he has served the maximum two, four-year terms allowed under the association bylaws. In addition, **Terry Norwood**, President and CEO of Midwest Public Risk (MPR) in Kansas City, MO, has said that he does not intend to stand for re-election.

Only those persons or positions officially named by resolution of a member pool governing body as their AGRiP Designated Representative are eligible to be nominated or vote in the annual election of AGRiP board members. The 2012 nomination process will take place between October 17 and 31; with the election to occur by mail balloting November 11 to December 2.

Each three years AGRiP forgoes its August Institute for Management and Leadership in favor of a joint conference with the California Association of Joint Powers Authorities (CAJPA). For 2011, *Pools Built to Last* is the theme for the Wednesday through noon Friday, September 7-9 tri-annual joint conference in South Lake Tahoe. The conference includes an optional golf tournament on September 6. Attendees may choose from among three hotels for accommodations – an Embassy Suites or Harrah's or Harvey's Casinos. Daily room rates for single or double occupancy range from \$69 to \$149. A brochure describing conference sessions will be released soon. In the meantime, registration and hotel reservations may be made through the CAJPA website at <http://www.cajpa.org/Topics/Fall%20Conference/Pages/default.aspx>.

The joint conference offers sessions of interest for pool board members, executive management and for supervisors or staff involved in any pool departments or operational areas. Attendees from AGRiP member pools may register for the joint conference at the "member" rate, which is \$300 for registrations made by July 15, and \$350 thereafter. Fee for the golf tournament is \$125 for conference registrants.



Three pools received plaques at the 2011 AGRiP Spring Conference in Clearwater Beach, FL, commemorating three year extensions of their RECOGNITION for compliance with the association's Pool Advisory Standards for public entity risk or benefits pools. Displaying the plaques, from the left are **John Foehl**, President and CEO of excess pool Government Entities Mutual (GEM); **Michael Rhyner**, Executive Director of the Michigan Municipal Risk Management Authority (MMRMA) and **Betty DiMaria**, Chief Performance Officer for the Public Employer Risk Management Association (PERMA) in New York.

A revised set of Pool Advisory Standards approved earlier in the year by the AGRiP Board of Directors are now in effect following a member comment period that began May 2. The standards form the basis of the AGRiP RECOGNITION program for public entity risk or benefits pools whose documented policies and practices meet these best practice standards. The standards and an application form for RECOGNITION are available on the AGRiP website at www.agrip.org.

Job Postings for positions with public entity pools are listed on www.agrip.org. There is no charge for such listings. To list a position, email Harold Pumford at hpumford@agrip.org.

Activities Calendar

Joint Conference with CAJPA
September 7-9, 2011
South Lake Tahoe

AGRiP Governance and Leadership Conference
October 24-26, 2011
Atlanta, GA

AGRiP Spring Conference
March 5-7, 2012
Phoenix, AZ

Fourteenth Annual AGRiP Pooling Track
Held at PRIMA's Annual Conference
June 3-6, 2012
Nashville, TN

Additional information for AGRiP Conferences and Institutes are listed in the SEMINARS area at www.agrip.org.

That's a large data set (4,536,000) to work with, and reinsurers assume that over the course of the next baseball game's 140 pitches, the statistical chances of a strike or wild pitch will be the same as indicated by the historical data.

Although this is a reasonable assumption, those who purchase reinsurance need to be aware that there is a chance, say 5%, of getting that wild pitch (that which varies greatly from the 'expected'). And, an even smaller chance of the pitch landing way off the graphs, where no pitch has ever been pitched before. This is the "Black Swan" event conjured up by author Nassim Taleb.

It is easy to get caught in the trap of continuing to renew the same reinsurance structure, year after year. There may be a price and risk trade off that is not immediately evident without proper analysis. Likewise, changing SIR's to accommodate budgets imposed by external economic factors could prove to be a grave error in judgment. The decision to change SIR levels should be analyzed based on actuarially sound methodologies and an organization's appetite for risk.

Often, groups purchasing reinsurance have policies which define the amount of risk the group is willing to bear in relation to goals of targeted surplus. These policies offer guidelines, but should never be followed blindly without reason and judgment.

The three elements that should be understood by each reinsurance purchaser are the following:

- What is the correct reinsurance structure, regardless of price?
- What are the price differences between structures, regardless of risk?
- What is the risk associated with each structure and corresponding price?

Membership matters is a newsletter for Members of the Association of Governmental Risk Pools. To comment or contribute articles, contact:
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the pooling
community
to achieve
excellence in
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