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From Regulation, Raiding and Relationships: Discussions with Directors

Name	Title	Pool	Yrs. w/ pool	Yrs. In pooling	Yrs. In Risk Mgt.	Format	Date
Stan Corcoran	Executive Vice President	Massachusetts Interlocal Insurance Association	28	28	28	Personal	7/15/10
Mark Nestor	President	ICRMS (vendor)	N/A	29	36	Personal	7/30/10
Steve Craig	Managing Director	Virginia Municipal League Insurance Pool	8	18	26	Personal	12/8/10
John Neilson	Executive Vice President	PERMA	1.5	27	27	Personal	12/9/10
Pete Tritz	Administrator	League of Minnesota Cities and Towns Insurance Trust	30	30	34	Personal	12/10/10

Interview Questions:

3. What are your goals for your pool for the next five years? Have your goals for the pool ever been in conflict with the board’s direction? How did/would you address such a circumstance?

8. What new developments or future issues do you expect risk pools to encounter in the next five years? What new trends are developing for pool management? How do you suggest I prepare to meet these new challenges?

9. Reputational risk is an emerging issue for current pool managers. What policies and procedures are in place to protect your pool from this type of risk? How do you view the risk and what can I do to prepare myself to protect a pool and its board?

14. How much interaction do you have with the pool’s general counsel and/or attorney panel? What experience and knowledge do you look for in an attorney who will be working with your membership?

15. How do personal relationships and political correctness affect your management style in running a pool? What advice would you give a new pool manager dealing with a personal relationship between himself and a board member? Between a pool manager and service providers? How do you handle relationships between board members, especially potentially explosive relationships?

Introduction and Impressions

I began working for the Alaska Municipal League as a policy wonk and publications person the same day that the Alaska Municipal League Joint Insurance Association (AMLJIA) began business: July 1, 1988. I have watched the pool develop from its infancy. Within a few years, I decided the pool looked like an interesting venture. I transferred from the legislative position and began working as the sole loss control employee for the pool in 1992.

Fast forward 20 years and now I serve as the pool's executive director. Several years ago, during an annual evaluation, my board of trustees congratulated me for a commitment of on-going education and career development for pool staff. They cautioned me, however, not to neglect my own educational pursuits. I wasn't sure that this needed to be a formal educational endeavor; those of us in the pooling business understand that every day is a learning experience.

I decided to pursue the ARPM designation to demonstrate to my board I was following their guidance. I've found the experience to be both fulfilling and a little late. I say a little late because the ARPM 601 was largely a review course for me. I wish I had been exposed to the ARPM 601 topics before I took my job as executive director. As it was, I have learned most of these subjects over the past ten years either through osmosis or sometimes by making painful tuition payments to the school of hard knocks. I thought that the ARPM 601 was an excellent overview and I will now require anyone taking a management position in our pool to take the ARPM 601.

As described to me, the ARPM 602 interview process was intended to provide me with contacts within the pooling community. Working in pooling for nineteen years now, I already have a deep cadre of contacts and mentors within the pooling community. We often have conversations about what is going on in individual pools with respect to competition, new service offerings, coverage and the like. The interview process, however, allowed me to focus on a few subjects that don't often come up; board relations and personal relationships with staff and vendors, for example. These focused topics were both fun and revealing.

When pooling first began, many of the staffs were from the public sector with little or no exposure to commercial insurance. As neophytes, we saw ourselves as giving a big one-finger wave (the "California Howdy") to the commercial market. If they couldn't be reasonable, some thought, we'd do this ourselves. Over time, it seems that pooling has migrated more closely to the principles that the industry has refined over centuries of business. This may be necessary for future survival.

At the time, our membership, still stinging from the insurance crisis, saw the value in what we were trying to accomplish. They tended to be a loyal, like-minded membership. Pools that enjoy a committed and loyal membership don't need to chase the market. They can smooth out the highs and back-fill the lows and bring some sanity and stability to the pricing cycles.

As time has marched on, however, many of the original local government officials that created the pooling movement have retired or lost their elections. Turnover on the councils,

assemblies and governing boards of our members threatens our loyal and committed membership. If rate stability is part of your pool's mission, as it is in mine, then maintaining and fostering that same commitment and loyalty of old is an important competitive advantage. Pooled coverage is increasingly being viewed by new local government officials, particularly in the current economy, as a commodity.

It's not just the membership that may have taken this commodity view. Some regulators and legislators have also lost sight of the distinction between pooled self-insurance and traditional commercial insurance. While many pools did not require capitalization to form, over time some pools have amassed a sizable surplus. As we grown to understand the importance of having a savings account to help cushion the volatility of losses, react in hard market situations, and provide us with broader risk financing and servicing options, fewer pools are offering dividends. Instead, we are behaving more like traditional commercial companies and finding other ways of returning surplus to members including subsidizing rates and offering enhanced loss control services.

In today's economy, most public entities are struggling financially. Tax revenues are down. State shared revenues are down. In many venues, members are demanding a return of their surplus, seeing it as public money. Pools are well advised to craft target equity policies that explain how much capital they must have and why.

For pools that are struggling with solvency themselves, state regulators are paying attention. Any time a pool fails, all pools suffer. In many respects, we are all tarred with the same brush. Bad behavior of a sister pool, be it financially or morally, makes us all vulnerable to regulation and increased scrutiny. Regulation of pools is already beginning to catch hold in some jurisdictions. Reputations have been ruined in others. Pools need not fear regulation, however, if we are already behaving as though we were regulated, measuring our solvency using conventional insurance regulatory metrics and focusing on transparency in operations.

The personality of our pools is changing. Originally, many pool staffs were from municipal leagues, member cities or counties, or other public entities. Free from pre-conceived industry ideas, we were free to be innovative in creating coverage and risk management solutions anew. Aging now, we find ourselves replacing our retiring staff with people that have industry or prior pooling experience. This staff turnover requires building the skill sets that serve the membership. As a result, there is increased attention to cross-training and succession planning.

Over the years, strong bonds have formed as many of the pooling staff and boards have served together for decades. Pool managers need to be aware of and guard against preferential treatment. We need to have policies in place and adhere to those policies. We need to play fair. The same can be said of business partner and member relationships. It is important to recognize that while the business is a personal one, it is still a business. Pool managers ignore this at their peril.

We need to avoid conflicts of interest in not only our staff and board relationships, but also with other business partners. When selecting our attorneys we need to avoid conflicts by separating general counsel and defense counsel. Attorney selection should be based on their expertise as well as their ability to navigate the Devil's Triangle of communication between the pool, the member and the attorney.

Following is are the main points I took away from the conversations on these matters and others, as well as some observations on how they apply to me and our Alaska pool. Following that are transcriptions of the actual interviews.

Findings

3. Five Year Goals

Financial Stability

When asked about their goals for their pools in the next five years, several directors pointed to their strategic plans. Interestingly, the strategic plan for the Massachusetts health program is not a five year plan but a three year plan. Stan Corcoran, the executive vice president, explained that with the fast paced changes of health care reform, looking past three years didn't make sense.

Not surprisingly, nearly all the directors mentioned financial stability as one of their goals, although only one pool admitted suffering financial difficulties. Financial stability was used as a

proxy to mean both solid financial condition of the pool as well as pricing consistency and stability for the membership. I think Steve Craig summed it up the best for both points of view when he said, “We want to hold rates stable while maintaining surplus.” Most pools share these goals and often incorporate them into their mission statements.

Succession Planning

Another common theme of the near- and mid-term goals were issues surrounding succession planning. The majority of the participants I spoke with are over fifty-years of age, although even younger directors were considering the implications of losing other, long-term staff. Mark Nestor, a consultant who has managed several pools and now works with many more suggested one of the main goals that the pools he works with was succession planning.

For any one who attends conferences of pooling directors this should come as no surprise. When I look around the table of a board meeting or the hotel meeting room at any of the upper-level management conferences or seminars I attend, I am often struck by the amount of gray hair in the room. Succession planning is a timely topic.

For my part, I am making a concerted effort to cross-train team members, document procedures, and invite department heads to attend meetings that they ordinarily might not consider part of their job. Afterwards, they always come away with a better appreciation for how their part affects the whole. This approach is strengthening the team, providing the management team with a better appreciation of the big picture, and broadening the bench of

talent that our pool can draw from. As Pete Tritz observed, exposing the management team to the wider variety of topics enables him to get away from the day-to-day management and personnel supervision “and really focus a little more on policy and strategy.”

Benchmarking Data

Another recurring theme in the five year goals relates to benchmarking data. For many years, PERI and NLC RISC have been trying to sell pools on the idea of benchmarking. In the past, I have been skeptical of the value of benchmarking to compare one pool to another. There are a number of factors at play behind the numbers. Factors like immunity statutes, for example. Some states, such as Steve Craig’s Virginia, have very strong governmental immunity. In other states, tort caps are much lower than Alaska’s. As a result, I’ve always felt such state-by-state comparisons are inherently misleading or even meaningless.

However, prior to the interviews it never really occurred to me that the “benchmarking” could be used to compare our member’s data to other members or even our own pool’s performance to itself over time. While we all likely use metrics to measure our members and ourselves on a year-over-year basis, some of the discussions led me to consider new metrics that we could use to measure ourselves against ourselves.

For example, we commonly use the number of police officers as an exposure or underwriting measure. Since we have collected that data, Pete Tritz suggests we could also use liability cost per officer as a benchmarking tool. Going beyond the traditional pooling measurements of

financial strength like premium to surplus or surplus to SIR, Mark Nestor suggested some pools are measuring change in premium or surplus or even reinsurance ratio by line of coverage. I will have to try some of these to determine whether there is anything meaningful that reveals itself.

8. Trends and Emerging Issues

The Economy, Surplus and Regulation

The global recession has made life difficult for local government entities in the United States.

The general consensus was that these financial challenges for pool members will manifest themselves in increased scrutiny of surplus adequacy and retention.

“The pooling world is going to have to adapt to the realities of where the country is economically,” observes John Neilson. They’re going to have to find ways to be more efficient with public dollars.

There’s a “whole galaxy of issues relating financial crises and the financial crunch in the cities,” says Pete Tritz. “That’s a pile of money sitting there that somebody might want to use to solve some other problems.”

“See that pile of money?” Stan Corcoran asks rhetorically, “They’re gonna want some of that returned back to them. . . Once municipalities get desperate, they look for desperate solutions.”

“A lot of pools have just gathered surplus with no particular goal or object in mind,” Neilson noted. “To the extent that you’ve thought out and said, ‘we have a policy that says we should have two times the annual contributions in surplus’ . . . then you’ve at least got something you can point to.”

All the participants agreed that the best protection against a raid on a pool’s surplus is to have a written policy in place – and we all do. For my part, I think that establishing the floor is much easier, however, than determining the ceiling. Maintaining a minimum margin for negative loss development is obvious. Without a crystal ball, however, knowing what to hold for the future is less clear. Common measures of surplus to retention, for example, will necessarily vary as pools may increase retentions in the inevitable hard market to come.

“We’re trying to get at what those appropriate amounts are to imagine the different kinds of low probability but high cost catastrophes that might befall us,” Tritz said. Minnesota is exploring perfect storm scenarios of combining a tornado with twenty SIR hits with a reinsurer bankruptcy.

A simple target equity policy, while a good idea, may not be enough. State scrutiny of surplus is already happening in some states, New Hampshire being a notable example. In a December 30, 2010, report to the Governor and the Legislature, the New Hampshire Securities Bureau issued recommendations on appropriate reserves for pooled risk programs in New Hampshire. The Bureau gives a passing nod to some of the individual pool circumstances and goals such as “rate stability, rate certainty, rate security, long term solvency, appropriate use of assessments, etc.” and recognized that pools have “very different objectives in regard to any of these issues, depending upon what their members expect from the pool.”

After a brief discussion of the Association of Governmental Risk Pool’s Advisory Standards, Insurance Regulatory Information System (IRIS) tests, Risk Based Capital (RBC) and stochastic modeling, the New Hampshire Bureau ultimately recommends a cap on administrative expenses of 10 percent for health pools. It is clear to me that the New Hampshire Securities Bureau believes that some of the surplus of at least the Local Government Center should be returned to the membership.

Regulation may extend beyond a proscribed administrative ratio. “Because of some bad pool management, I think there may be some more interference or control from various Divisions of Insurance. To prepare for that, pools are beginning to look more at the IRIS tests than the earlier pooling standards,” Mark Nestor observed.

“There is this threat of national regulation. I think there are threats of insolvency” Neilson noted. I told him others disagreed. Steve Craig said, “I have a hard time envisioning Federal regulation, but tighter state regulation – certainly, and perhaps more consistent regulation from state to state.” Craig returned to this later stating, “Every state has an insurance commissioner and I’m not sure they’re going to be willing to cede any turf to the Federal government.”

Neilson mused, “In normal times I’d agree with that, but given the stress the governments at all levels – Federal, state and local – are under . . .

“NAIC went down this road about 20 years ago,” Neilson explained. He asserted that it was that effort that spawned what we now consider the basic pooling standards. The subsequent conversation was a fascinating pooling history lesson for me.

Whether it is national or state regulation, everyone agreed that increased regulation was a possibility to be mindful of. “If I were gonna place a bet,” Stan Corcoran said, “I’d say there’s more regulation coming as opposed to less.”

For my part, Alaska is behaving largely as though we were a regulated company. Our claims adjusters are licensed adjusters. The pool is licensed as an adjusting firm. We have staff with health and property/casualty brokers’ licenses. We are trying to maintain adequate surplus

without keeping too much. I will, however, start looking at IRIS ratios where appropriate as another means of measuring our solvency.

Other Issues and Trends

While I was most intrigued by the common discussion of surplus and regulation, there were other issues suggested by participants that I had not really considered before. Mark Nestor suggested that pools might be losing their edge over the commercial market in new coverage offerings. Despite that observation, the participants I spoke with all had some interesting thoughts on emerging issues.

Steve Craig suggested that the Green movement may create sick building claims as buildings become tighter. Pete Tritz has been thinking about the affect of the economy on potential fiduciary and bond default claims against member municipalities. John Neilson had thoughts on merger and acquisitions of various pools both horizontally to achieve overhead efficiencies and vertically into primary and excess layers. “Examples of this already exist,” Neilson said, but “it could be done on a much bigger level.”

9. Reputational Risk

“It takes twenty years to build a reputation and five minutes to destroy it.” -- Warren Buffet

“I think the risk is real,” says Steve Craig. “Perception is truth at the end of the day.”

“Reputational risk is real,” says John Neilson. “A lot of it you would think is just common sense.”

“Try not to be stupid,” advised Pete Tritz.

Everyone agreed that recent events among some of our sister pools have reflected poorly on those pools, but to some degree have the potential to tarnish our own reputations. A pool’s reputation is an important asset. Members are more loyal to a well-regarded company. Employee recruitment and retention is easier for companies with a good reputation. Potential regulators are less likely to focus the magnifying glass of regulatory scrutiny on pools with a good reputation and respected leadership. Competitors are less anxious to compete with a respected pool. These are all good reasons to protect our reputations.

Protecting that reputation is a matter of transparency in operations and common sense.

Neilson suggests that a set of core policies and practices should be set in place that “extend(s) from the very top to the lowest level.” These must be consistently adhered to and punishable by firing if people violate them.

Mark Nestor points out that “Most pools already have the policies and procedures in place to protect them from reputational risk. They just need to live up to their mission statement, business plan and operational plans.”

Stan Corcoran observed that the membership will measure pools against the yardstick they are held to. “One needs to look at what’s the practice that cities and towns have to follow with regard to accepting gifts?”

Nepotism, conflicts of interest policies, policies on gifts and meals all help, everyone agreed, but eventually it comes down to individual’s judgment and good faith. As Pete Tritz said, “Any policy, if you’re looking for a way around it, there’s a way around it. It just kind of comes back to the kind of people you hire and the kind of people you look for. “

Of course, in Alaska we have policies regarding conflicts of interest, policies guiding our service providers and the receipt of gifts. But writing a policy that can cover every conceivable potential threat to reputation requires more brainpower than I can muster. I subscribe to the school of thought that we need to use common sense. As a guide for decision making several participants referred to the oft-cited maxim, “How would this look on the front page of the newspaper?” Applying the “front page” rule to using the company credit card to pay for strippers, having pool board meetings out of state, referring legal work to your husband’s firm, holding large meetings at your own restaurant, taking tickets to sporting or cultural events or even renting from yourself would have prevented some pools from damaging their reputations.

14. Attorneys

What’s the difference between a good lawyer and a great lawyer? A good lawyer knows the law. A great lawyer knows the judge.

It is tempting to judge the public's opinion of attorneys by the hostile websites dedicated to lawyer jokes. However, as professionals that interact with attorneys on a daily basis, pool managers realize that attorneys can be our best partners. When asked about criteria for picking counsel, all the participants made a distinction between general counsel and defense counsel.

General Counsel

The participants generally agreed on criteria for selecting general counsel. First and foremost was an understanding of insurance law. Second was an understanding of municipal or public entity law. Further down the list was the cost.

Steve Craig didn't feel that the public entity angle was all that important for corporate work. "We've been sued three times in the last five years," Craig explained. "We don't need a local government attorney defending us; we need an insurance attorney."

Stan Corcoran suggested a criterion that made a lot of sense: political access. All things being equal, if a firm has good relationships with the regulatory bodies, the Governor's office or the Legislature, they would be preferred over firms with less political credibility.

This is not a new idea for Craig, either. "I'm not opposed to having a few delegates and senators as defense counsel," he admits. "It can't hurt me to have somebody up there to help

me if I have a problem. I'd love to figure out a way to do it, but I'd have to pay them \$250 per hour for the privilege."

In my experience, it is easier to gain the political access that Massachusetts and Virginia mentioned through the membership. Local government service is frequently the spring board for election to statewide office. Several legislators in Alaska are former mayors or council members. If pressed, however, I would readily admit that attorneys are also highly represented in the Capitol Building.

While nearly all the participants acknowledged the value of having corporate counsel attend board meetings, in actual practice, this was split. "Normally, general counsel in the pools I've worked for has always been in attendance and has been party to everything that's going on," said John Neilson. That is not the case for him right now.

Sometimes meeting attendance is a matter of cost. "One could argue that they should (attend)," Stan Corcoran acknowledged, but cost is a factor. "In Boston, it's a high-brow firm, so if you're going to say – '\$450 per hour,' – I'll fill you in. I'll send you the agenda before the meeting and then send you the minutes."

Minnesota enjoys the benefit of in-house corporate counsel. Pete Tritz explains that he interacts with general counsel almost daily. "It's just kind of a walk down the stairs, so any of

the issues that involve legal considerations and lots of issues that don't . . . I pop my head in his door and we talk about it. . . I think that's a nearly ideal kind of working relationship."

Again, cost is a consideration. A pool the size of Alaska's can not afford an in-house attorney dedicated solely to corporate work.

For the most part, general counsel is the board's lawyer. The board selects the attorney or firm, though in nearly every case, management would have some input if the question of selection came up. While not a lifetime appointment, most pools don't change corporate counsel often. Several of these long-time pool managers had either not selected corporate counsel or had not done so in over fifteen years.

I found the discussions of general counsel interesting. Similar to the political access discussion above, I often recommend attorneys that we work with for judicial appointments. Alaska may be looking to replace our corporate counsel soon, as the solo-practitioner that has served as general counsel since inception is seeking a seat on the bench. Conflicted by losing experienced counsel and gaining a good judge on the bench, I recommended her. I think her chances of appointment are excellent.

In every case, general counsel didn't ordinarily handle defense work. In most cases, they were separate from coverage counsel, however in Virginia I understood the corporate firm also did the coverage work.

Defense

I was struck by the variety of options available to pool managers from bigger states like New York or Massachusetts. “The law of large numbers suggests that we can be a little more judicious and more restrictive to protect the downside of a conflict a little easier than you can,” John Neilson observed. At only 710,000 people statewide, Alaska’s entire statewide population is less than a single major city in any of the states from which the interview participants are from. Still, the issues are the same.

Nobody wanted to defense firms that do plaintiff’s work, at least against the membership. I agree in principle and largely in practice. However, I consider this “more of guideline than a rule.” We have some plaintiff attorneys that specialize in rural areas. They live there. They are very effective and understand the unique culture, economy and the often Third-World conditions in Bush Alaska. While Rural Alaska is unique, however, even older, heavily-populated states like New York face similar problems.

“You certainly don’t want some high-falutin’, expensive high-powered attorney from Manhattan up to Auburn, New York to litigate. That’s a mistake. You want to try and match up the geography,” Neilson observed. “There’s a great disadvantage to assigning the wrong attorney to a case.”

Everyone also agreed that selecting defense counsel on a case-by-case basis is important. We all hire lawyers or firms with competence in the area of law that we are potentially litigating.

Or in some cases – not litigating. “You need to match up the skill set of the attorney with the circumstances of the case,” says Neilson. “There are some cases where you know very early on that there is no way that this thing is going to be settled; it’s going to trial. You need a litigator on that file. It’s not optional.”

Another shared criterion was in the realm of communication and understanding who pays the bills. As Steve Craig put it, “We want someone who understands that while the legal canon says that they represent our member in the case, the pool is paying the bill and they need to be a partner at the table.” Pete Tritz agrees. “They have to be willing to kind of work with us and participate in those conversations about litigation strategy and so on.”

Selecting counsel that can walk the delicate balance of the tripartite relationship is important. Communicating to the member is a key element in member satisfaction, but the facts of the case, the preferences of the member, and the attorney’s appreciation of the risks of too much information all come into play.

In Minnesota, this is an important touchstone for Tritz. “We beat on them about communication a lot . . . to make sure that the city folks know what’s going on. . . You have to customize that stuff, too. Because some of them want to know everything that’s going on; some of them don’t want to be bothered with any of that kind of stuff. You kind of work with what you have, and again, the defense counsel has to be willing to do that.”

In Minnesota, Tritz is very open with the member councils. In Alaska villages where often everyone is literally related to everyone, I've been burned before by attorneys disclosing the terms of an upcoming settlement to the city council. Tritz admits that there is risk in over-communicating.

"Trying to stress – you can never control it absolutely – but you can try to stress to those folks that this is a privileged conversation. This data is therefore confidential under state law. 'It would be a criminal violation for you to release this data, don't you know?' Mostly it works. It's not a hundred percent."

In future cases when member councils insist on litigation updates, I think I'll try the Minnesota "criminal violation" approach.

Finally, there was one other important point for consideration: results. Pete Tritz explained, "Another almost sure way for a defense counsel to fall off the list is to do the thing of – 'we've got a great case, we've got a great case, we're going to win this, we've got a great case, oh my God trial's tomorrow. We gotta get this thing settled.' You only get to do that once."

Repeated, updated realistic evaluations of exposure and the chances of prevailing at trial are important considerations.

Actual monitoring of the results is a tool in Stan Corcoran's tool box, as well. "Once they're on board, evaluate them," he said. "Are they providing you a service? Are they keeping you in the loop? Success ratio. . . Did they win? Did they fail?"

Corcoran suggests that regardless of whether the attorney is "in-house or contracted out, you should have the same standard."

While somewhat at a disadvantage with the number of choices Alaska has for legal specialists, I'll pay closer attention to the potential conflicts between corporate, coverage, and defense counsel.

15. Relationships and "Political Correctness"

I'm reminded of the recent Farmers Insurance commercial where the "Professor" flashes slides of clients and the "class" of a half-dozen students tells what they know about them. You remember the one? "That's meatloaf. That is still Meatloaf."

It is a common belief that the pooling business is a "relationship business," but the quality and nature of the relationships can affect management of staff, service providers, and board members.

“I think those personal relationships are important with staff – in particular your department heads,” Steve Craig says. Already a long time employee of his pool, Craig was promoted from within. This creates special challenges, he allows. “I was the last one to figure out the relationship had changed. . . All of the sudden I was treated differently because I’m the boss.”

When the waking hours we spend at work outnumber the time we spend with family and friends, personal relationships in the workplace are inevitable. For long time directors like Pete Tritz, he has worked with some key staff for twenty to twenty-five years. “Being aware of one’s own prejudices is, I think, one of the hardest things that there is.” Tritz tries to remind himself of the risk of preferential treatment. “Be aware of that risk and remind yourself of the need to be especially careful,” he advises. You have to guard yourself against “the natural human tendency to cut a little extra slack for the people that you’ve known for a long time.”

Stan Corcoran recommends policies and procedures. When it comes to harassment-type issues, Corcoran says “We’ve got a pretty good process in place. If someone is uncomfortable, there is a procedure by which they can report it to their supervisor or go to the League.” John Neilson recommends nepotism policies, disclosure and transparency.

It was interesting to me that no one’s first thought about personal relationships jumped to intimate relationships.

Like Craig, I was also promoted from within, and his experience about the changing relationship from peer to boss resounded with me. As the director of a small pool, I have a much smaller staff and can't help but to have developed close relationships over time. I have learned the hard way to keep my own counsel.

With respect to personal relationships with service providers, many of the participants focused on business. Neilson's policy is to never be put in a position of being accused of being in someone else's pocket. Steve Craig agrees. "I don't do a lot of lunches. I don't want any holiday gifts. . . I try to make it a collegial and positive relationship, but its business. I don't need to know who their kids are and what they're doing on the weekend."

Still, it is a relationship business. Tritz points out that having a long-term relationship with a business partner works to the members' benefit. "I think about the way the folks with GenRe were willing to step up when we were trying to put together a pretty unique coverage solution to deal with some of the things connected with the Republican National Convention that was at St. Paul," he recalls. "A complicated thing, but basically because we had a good solid working relationship they were willing to say, 'Yeah, we trust what you're doing.' It's partly a personal and partly a business relationship, but part of the business relationship is them . . . knowing how we work, how we think, how we make decisions."

In Alaska, I try to invite service providers to our annual summer meeting. This is generally a low-key affair in a member city with some special team-building exercise associated with it.

Service providers usually jump at the chance to travel to Alaska on their company's dime. It provides the pool with the chance to better know our upstream risk partners and develop a better relationship. Personally, I can't say I'd be comfortable not knowing anything personal about our business partners. At least I know they exist. Woe is the pool that pays an excess premium to their broker just to discover years down the road that there really was no contract with a carrier. I've seen this happen.

Nearly everyone agreed that personal relationships with board members were also natural, although the degree to which these were cultivated varied from pool to pool. Some pools make a point to visit board members in their communities, take them to dinner, and spend time with them at conferences. Others allow the relationships to develop more organically. I don't know that there's one right way. "The main thing is to make sure they have confidence in you as the pool director," says Craig.

Transparency is a key to that confidence according to Corcoran. "They don't just rely on me," he explains. "We'll bring in the experts. The underwriter, to allow them to ask those questions directly." Stan told a story of his chairman asking him a question and then during a break asking the same question to the actuary. The answer was the same. "I'm glad to hear that," the chairman said. "I know I hear it from Stan, but it's also really good to hear it directly from you."

“They can trust what I say,” Corcoran says. “They can feel comfortable that they can have direct access to the experts and consultants if that’s the case. . . I think it engenders a strong sense of trust.”

Everyone was happy with their board’s behavior and rarely have experienced “explosive relationships.” Suggestions for dealing with that include good business and strategic plans as well as a strong chairman. “Having a really good relationship with the chairman,” and working on any potential issues ahead of time has helped Corcoran. John Neilson agrees. “If you have a strong chair, you can generally work around dysfunctional board members,” he noted.

There were some interesting discussions about how the board was selected. I have found that the director needs to be careful about being involved in the board selection process to avoid being accused of stacking their own deck.

Although I hate to pay more for a contract so that the actuary or other third-party provider can travel to Alaska, I may borrow a page from Corcoran’s book and make sure that the experts are at least available by teleconference. We used to do that all the time, but over time we have gotten away from it. I shouldn’t forget that there is turnover on the board and not everyone has had the chance to ask the questions that we all have about actuarial reviews, financial and claims audits and other specialties.

Executive Summary

The interview and report writing process has been an interesting one, requiring me to focus more closely on the discussions I had with the other directors. My challenge moving forward is to determine how to incorporate some of what we discussed into the management of our pool. These takeaways did not break cleanly into the original discussion topics. Rather, they were a blended result of the discussions.

For example, take the regulation and benchmarking discussions. Although pooling in Alaska is unregulated, our pool has made an effort to behave as though we are a regulated company. Although not required, all staff is licensed by the Division of Insurance in their area of expertise. Staff maintains their licenses through continuing education credits. We follow the Fair Claims Settlement Practices Act. I found the discussion of IRIS ratios and RBC tests an easy way to begin benchmarking ourselves in a way that has some meaning across jurisdictional boundaries. In preparation for our next board meeting, I will ask our finance manager to revise our current Target Equity report. In addition to the more traditional pooling ratios that we currently measure ourselves against, we will explore the IRIS ratios. Following that, we may explore the RBC tests as well.

Another change I expect to make as a result of these discussions is to further distance our coverage counsel from corporate counsel and defense. We are currently engaged in two actions brought by members against the pool for denials of coverage. In both cases, the

coverage counsel is defending us. This offers a potential conflict of interest as they end up defending their own advice with respect to the original denial.

Moving ahead, particularly if current corporate counsel is appointed to the bench, I may suggest that the board appoint current coverage counsel as general counsel and find some one else to advise us on coverage issues. Already, we are testing the waters with potentially new coverage advisors.

Thirdly, the discussions on reputations and relationships have made me review my current practices. Coming from a small state and small towns, it is in my nature to be a friendly, personable type. Arguably, too much so when it comes relationships with vendors.

I have found it easier to achieve the pool's goals with business partners that not only understand our pool, but think kindly of us. The discussions with other directors, their examples, and the recent experience of some of our sister pools are making me reexamine my approach. I still think that inviting re-insurers to our summer meetings in Alaska at their expense is a good idea. I will reconsider; however, how much trading dinners, bottles of wine and other friendly gestures is necessary to foster a business relationship. I will be asking myself, "How would this appear on the front page?" Generally, a great test for living in a fish bowl.

INTERVIEW TRANSCRIPTS

Following are transcripts from the interviews conducted between July and December 2010. All the interviews were in person and most were recorded with a digital recorder (which I struggled with). Interview participants were provided an opportunity to review the transcript of our discussion to add, remove or clarify material as they felt relevant. In some cases, I redacted material that was not germane to the point of the interviews.

**Stan Corcoran, Executive Director, Massachusetts Interlocal
Insurance Association**

July 15, 2010, Woodstock, Vermont

All-right Stan, tell me how many years have you been with the pool?

'82 was when I started. You do the math.

28 years. And the whole time in pooling?

Yes.

What was your background prior to that?

I started in public administration basically.

**So how much interaction do you have with the pool's general counsel and or the
attorney panel?**

That's a question of time or in terms of being the primary contact?

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Of being the primary contact.

Yeah.

And what experience and knowledge do you look for in an attorney who will be working with your membership?

There's a number of different questions—one is, I'm going to segment claims versus general counsel if you don't mind.

No, I think that's appropriate.

Let's deal with the general counsel. The corporate counsel, are they familiar with insurance groups? Are they familiar with insurance entities? Are they familiar with litigation? But the counsel itself you can separate the individual from the firm but to what extent does the firm have other specialties that we may find ourselves needing? What was really important to us, quite frankly I don't know how you put this in there but to what extent do they have [excerpted] credibility with the regulatory bodies and with the governor's office?

So you're regulated?

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Yes. We have a degree of regulation. But even beyond the regulation, for example if there are some competitive concerns that we have about practices to what extent do we have, I use the word credibility but political access that could help us in any arguments that we make. To what extent do they have a credible presence beyond just what we have for the League with the legislative bodies? So there's a number of things that we were looking at. That was certainly one, one of many. Are they just overall good general corporate counsel? To what extent do they have a broad range of experience for us? We have health, property casualty, workers' comp. The individual who was selected actually was an attorney with the Division of Insurance, understands the regulatory, understands insurance.

Has access, all of the above.

All of the above.

Who chooses? Did you choose him or does the board choose?

The board chooses general counsel but I have weight. We issue an RFP, we ask for qualifications. We let the board choose general counsel.

When was the last time you went through this exercise?

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Its been a long time. It may have been 15-20 years.

So you don't change counsel like people change underwear?

No. Another example is changing the partners or financial auditor which is every 5-7 years, we haven't done that. We've kept the counsel. That's a good question. Should we change? I don't know.

Ya know, I think you can dance with the girl that brung you, frankly. I have toyed with the idea of picking the counsel depending on the issue. Some attorneys are good on certain issues, some are good on others.

We've done that.

Even though this is the board's lawyer, there's other times like 'that's the board's lawyer but I'd really rather have someone else on this issue.'

That's right. We have the corporate counsel, sometimes there are issues related to personnel that you'd want to get someone who specializes in that, who rates a little bit better. Sometimes a particular type of litigation and then, it may be the firm itself, but its large enough that they will send another attorney to it. That's one of the things we looked at—what specialties are part of that firm, not just that individual. Is it a large

Stan Corcoran
Woodstock, Vermont
July 15, 2010

enough firm that they can bring somebody in who will be comfortable? This is all on the corporate side.

While we're on the corporate side, then it would be your recommendation to look for firms large enough to have depth on the bench as opposed to a solo practitioner?

Yeah. That would be my sense. That's another interesting point. Let me amend that. We have actually have a separate counsel for the health trust, and he's a solo practitioner, but I'm okay with that because I've got the corporate counsel over there, it's a combination of both. The other thing that I like about him is that he's a lot less expensive. He's actually more responsive because we are an important client of his. He understands particular legislation that affects cities and towns in terms of their ability to purchase health insurance. He's a labor counsel but he has a specialty with regard to health insurance and municipalities. And so we rely on him a great deal to interpret specific legislation of cities and towns that purchase healthcare.

However, on the larger corporate questions, we have this other corporate counsel. So in a sense, he's the specialist in healthcare and labor law and understands how cities and towns can operate in that environment. She isn't, she's just overall corporate counsel. So its interesting. We actually have a mix depending on the firm. We have more than one firm.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Does the lawyer attend all the meetings?

No. And one could argue that they should.

My lawyer would argue that she should and I argue that at \$150-175/hour, why?

Ours is more expensive.

Oh I'm sure.

In Boston, it's a high-brow firm, so if you're going to say \$450/hour—I'll fill you in. I'll send you the agenda before the meeting then send you the minutes.

That's kind of how I feel, too. But the board feels differently about it and its their counsel. Its their money. That's kind of how we're working it. How about defense counsel?

That depends on what program—workers' comp or liability. We have a TPA so we approve the defense counsel and we get reports on the utilization of that, but essentially that's the TPA assigning it.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

What are your criteria for approving counsel?

For us its they're not doing plaintiff's work. So we want them to pick their side. And the second is the degree of expertise and experience they have not just with insurance but also with public entities. And then after that, once they're on board, evaluate them—are they providing you a service, are they keeping you in the loop, that type of thing.

Success ratio.

I was going to say—how do you monitor it?

Yeah, how successful are they with the litigation. Review that—did they win, did they fail. We get a report from the claims manager in terms of the law-firms, in terms of cases they've tried, cases that have succeeded and their sense of just how well its working out. We also get monthly reports on the claims, defense work, how many claims they had, how much money we spent in that particular month and what we've accumulated total.

By firm?

By firm.

So number of cases? Amount of money spent I assume?

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Yes.

What do you do in the way of litigation management?

Essentially its delegated to the TPA firm. That's part of our litigation management program. One of the things that we need to be really careful of—its easy for a TPA to let the attorneys manage the case and then charge for all those hours. So when we bring in a firm to audit the TPA we ask that question—to what extent was it delegated too much to the law firm versus not? We ask for a report on that and what their sense of that is. We've had some comments in the past that they were letting too much of that be driven by the attorney versus driven by each other. That's not the case right now, but it had been in the past. That's why you have to continue to have audits of the claims staff.

By the way, what's interesting is, whether you have it in-house or contracted out, you should have the same standard. I'm not sure if its better one way or the other, it really depends. The standards should be the same. Having your own staff sometimes its harder to deal with those personnel issues. You kind of maybe let some things ride a little bit longer than you really should. I find that with the claims staff if there's an issue, we raise it and you can have that person reassigned or maybe not there. It actually

Stan Corcoran
Woodstock, Vermont
July 15, 2010

helps in our relationship—it helps the TPA to make those personnel decisions because we say to them, we've gotten complaints about this individual and having that third party provide that input helps them in making their personnel decisions.

Sure, because you can say look, you're not doing us any good when Stan won't let you work on his stuff so we're going to have to let you go.

Right.

Let's move to personnel. Wait, let me back up. Have you had an in-house claims staff?

No.

Okay, no. Let's move to personnel. That's got to be the most fun part of your job.

Its not so...

Not so bad?

No.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

That's good. How many staff do you have?

27-28.

And you don't have a crisis every month?

Well, no.

That's cool. [13.48]

Things come up but mostly its structural. There are issues that come up—you can pretty much, my belief is that mostly you have good people. Bad structure leads to bad outcome. If you're not putting, for example, loss control right now we've had a particular issue where a senior loss control person who is better suited for one thing than another. I've had to reorganize the operation so part of that is outside, contracted out, and part of it is inside. That was a deliberate move to be able to have a higher quality product and I think I've been able to get that. However, the next stage is to progress a little more in terms of clarification. I need to not have two different loss control divisions. We're actually undergoing—bringing someone in right now to help bring that along a little further to where it needs to be. Basically we're talking about a person who's in a retirement situation so its easing that person in that place working on succession

Stan Corcoran
Woodstock, Vermont
July 15, 2010

planning. But doing that in a way that is respectful of that person's contributions to the organization but recognizing that a change has to be done.

That's humane.

That's humane, yeah. I would say its not a crisis.

That's good. I've had it go both ways.

Goes in cycles probably. There were periods where I think we had in Massachusetts an entity called {inaudible} Against Discrimination and we've had individuals file suits for that entity against one or more supervisors. That was the old—but for whatever reason its at a good place. I'm not saying that will be next month or next year. Personnel is really difficult. Also be mindful that we tend to minimize the number of staff for that reason. Once you bring in more staff you geometrically increase the probability that you'll have staff issues. That's the nature of what it is. You've got to have somebody on board to be able to manage that and deal with that. I'm not saying its perfect, because I don't think anything is perfect—but its not at a bad place.

Do you have a human resources director?

Nope. Could we use one? Yeah, I think we could.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

At what size do you think you could use one?

Right now. Can you contract out for someone—there are some services that you can do that or maybe you need half-time or something, I don't know. Its one model. You know what personnel—there's always a need for something there's always something going on. We could probably use, overall the League itself, could probably use some resources there.

Oh the League's got lots of employees in addition to your 27.

I think we may have more than they do—its about 50/50 or maybe we one or two more.

I think when you're at 50-54 employees that HR function is not unrealistic.

No. The other thing we have is—I'm not including essentially the TPA — are private legal. They go out and is they're the pool. They have a business card that says the pool. And their desk is at our office for that—they come in at least once a week. So it's really good. Its integrated. And the location of the TPA's—I can see their building right across the street. The other TPA are essentially dedicated to us. They spun off of another organization with our blessing and encouragement and we are essentially their main client. So they report mostly directly to us.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

So they're not in-house but they're practically in-house?

Exactly.

That's working pretty well, apparently.

Oh yeah, I think it is. It is. It is.

So you have the advantage then I guess of saying we don't want this one on the account without the disadvantage of trying to do the humane thing...

Right, right. Also, sometimes there are cultural differences between folks who come out of the insurance industry—say a claims background or a health and wellness background or a sales background. On the other hand you have an advocacy group, a League, which has a separate—you're familiar with that.

Yeah.

Sometimes it helps to do that split because you can keep it in a sense more pure so its more in line with what they're used to in terms of the incentive system structure, etc., without necessarily causing confusion and difficulty on the other side with folks saying

Stan Corcoran
Woodstock, Vermont
July 15, 2010

“Well wait a minute, how come we don’t get some type of compensation for retaining business?” Or “We don’t have an opportunity to do that how come they’re getting that additional revenue?” It keeps that separate and I think it works okay. You always need to look at it and you always have to have a feedback mechanism. Okay, is it still working, is it not working, and do we need to make some changes? Right now, its okay.

So you’ve obviously considered bringing them in house?

Oh yeah.

Like when they spun off I’m sure that was a question you asked yourself.

It was. But we’re in a space in downtown Boston. If I were to bring them I would have to move out of the office because there isn’t enough space. If we’re in Boston then we’re paying a high per square foot rate which doesn’t make sense to bring a lot of folks in. Its much cheaper out there to satellite. So its just a business model there at work. What’s interesting is every place you go there are different approaches. You could bring somebody else and say you know what I’m gonna bring it all in house, I don’t know where I’m gonna get the space—you gotta pay the high cost per square foot in the city—that doesn’t make any sense.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Right. How about on the lobbying side? You must have issues like the firefighter presumption issue—did the League help you with that?

Oh yeah. Its actually been very supportive. But we don't cover police and fire. The statute is such that—they have legislation—well Tom covers them because he set up a special program for them. For us we don't insure them. It's a separate statute. What we do provide is a police and fire accident policy but it doesn't mimic the law. This is the limit of coverage you have this much indemnity and this much medical and that's it after that you're done with the individual. And that's a sponsored program.

You don't pool for it.

No, because every time we look at it we realize that the amount they're charging is less than cost. We say we can't make that work. I don't know how they make that work, but whatever. Let them figure it out and periodically look at it. Particularly when it comes to—if we're not happy with the service—but we weigh service versus cost and say you know what the members ultimately like the price. Occasionally there are issues with regard to the service of that, but its not so much that its worth our bringing it in house and charging twenty percent more.

But the lobbying I think is significant, particularly on the health side. That's been helpful. They have access, we don't.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Do you ever find yourself at cross-purposes with the League on legislative issues?

Not usually, but in the past there's been a legal question. The law firm that we had used in the past—the person was the corporate counsel for the governor and he was on that firm so occasionally, you know—they might just help them. Yeah, occasionally what we will do is we'll have—not a separate—we will on occasion utilize someone independent. For example, maybe someone who was an interim insurance commissioner who now is an attorney and has his own firm. We might use him on a particular issue. So yeah, it really depends—it makes sense if its awkward for the League to participate in that or they just don't have the extra cash.

Right. That seems to be my problem. Is that when it comes down to workers' comp issues or insurance issues, there's just no expertise on the League staff so it falls to us. It falls to me.

Same here. But they're doing that not so much for the pool they're doing that for the League. Not saying we're here lobbying for my end, no they're lobbying for the League because this is an important advocacy position and that makes sense.

Do you testify? Do you have to go to Senate Finance and testify?

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Its been a long time since I've gone up there. I've met in the past with different legislators. Its been a long time since I've had to do that.

That's also nice. It can be a real time drain.

I've been there and I get that. Where it just sucks your time in and you get up there and you're there all afternoon. It's the League that has credibility so if there's a particular issue they're usually the one's to do that. Some specific issue related to workers comp—okay so you want somebody to go up there and provide some information. It doesn't come up very often; you don't see it that much. If the issue broadly affects cities and towns, we'll have attorneys that will provide that for the League and they'll do it on behalf of the League and not for us. It has greater credibility when it comes from them.

So Massachusetts League has pretty good credibility is what I'm hearing?

Yes. And we know them, they don't know us.

That's okay, too.

That's just us other states are different.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Obviously. I'm going to move to a different question about personal relationships and political correctness and your management style in running the pool. How do personal relationships and political correctness affect your management of the pool?

First of all I'm one of the sexual harassment officers for the League. I've had individuals where I've had to speak to them at the League. They're not my employees but because that's my position I talk to them about that. You know those issues don't come up, we're pretty good about that. We've got a pretty good process in place. If someone is uncomfortable there is a procedure by which they can report it to their supervisor or go to the League, someone on their part and report the issue to them. So we're very careful about that. I don't know how diverse you would consider it, but we do have different nationalities now... it varies depending on the time. We probably are much more diverse on the insurance side than we are on the League side, that would be my take.

Why do you suppose that is? I mean you look around the table today, its still an old white man's game.

With the house side it isn't. It definitely isn't. It is female dominated. And you have one person from South America, one reports Hispanic, one black, its diverse. We had someone working for us who was from Nepal, no Tibet—she was Tibetan. Its all over

Stan Corcoran
Woodstock, Vermont
July 15, 2010

the place. This notion of it just all being white men, it might be at different times but its changing rapidly so I'm not sure I could really say that. Particularly in the health is a big change.

Right I would think that the health would be female dominated. That's been my experience, too.

Also I think you gotta look at the culture of say a place like Boston. Its been the forefront of--I don't want to use the word political correctness but you have to be very mindful of what you say. You can't make any assumptions. You can't use the words girls get coffee or gals. You don't need the word girls, you don't say that. Its men and women. So I think folks are really careful about that. If anyone suggests or says anything which anyone of that category, that is just it. They will be in my office immediately. And they know it.

How about relationships with board members?

I'm trying to think of that. We have a super relationship with them. We don't have term limits. The folks we tend to have on our board are ones that have actually served in League positions of leadership and so in a sense they've shown a demonstrated capacity for cooperation, teamwork and leadership.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

So with no term limits you probably have a pretty savvy board?

I have a very savvy board.

That's nice.

We do have new board members come in. Many places you have turnover for people who take another job at a community who is not a member of a program or if they are we have to—it isn't automatic because they're still the board member. The board has to take a vote.

What is the board selection process?

Nominating committee. That goes before the membership depending on the group. We have 3 boards. We also have some advisory groups that we put folks on to get a chance to see how well they perform in that environment and then make recommendations to the nominating committee. The nominating committee makes the decision and then presents it to the pool. The pool membership can actually make a recommendation for somebody else. Its worked fairly smoothly. We tend to have—I would say some of the best local officials. Not firebrands. We don't tend to have folks with a certain expertise. We try to get a big cross representation throughout the state.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Try to mix it up in terms of gender and diversity. Massachusetts isn't terribly diverse in terms of race—it tends to be mostly Caucasian.

So you don't have potentially explosive relationships between board members?

How would you handle that? I mean its nice if everything goes unanimous all the time. Do you have split votes very often?

I mean there are some differences. Typically what might happen is there's an issue and I think there might be a potential conflict I may talk to the board members ahead of time and say this is what we're trying to achieve. If I know someone feels particularly strong about it—if it needs to go offline. This is really helpful: the League director is particularly astute with that, too. Managing some of those political situations. Its an open board, the issues are brought out on the table. We tend to have people who are not divisive. Try to come to a solution when the issues are raised. If we come to some disagreement we can't resolve we table it and give it some thought and by the time we get to the next meeting it tends to be resolved. I think part of it is the vetting process of who you bring on the board. We've seen really good leaders who have demonstrated their capacity for consensus and come to good decisions. I'm not talking about {inaudible} because these have been the president of the League so those folks can make their opinions heard but its done in a way where people feel they're not being alienated. I think that's an awful lot of it, an awful lot of it. And then having a really good relationship with the

Stan Corcoran
Woodstock, Vermont
July 15, 2010

chairman and working with the chairman on any potential issues. We can make a phone call or two to resolve some of that. Seems to work out okay.

How often does the chairman change?

About every three years.

So you've got a three year term limit?

Yeah, but its informal really. Its not by by law, its informal. Its worked well, too. We like it and the board likes it as well.

Do you have anybody that has been a challenge?

Yeah, but mostly the new people. When new people come on we want to make sure that they—it might be somebody that for whatever reason they do not fit the bill.

{inaudible}

Its your turn.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Its your turn, right. So typically what we have is a chairman that is a member of all programs. So what that means is that sometimes there's a board member that's been there a while that isn't in all three and we say I'd like them to participate in all three.

So you have three boards?

Yes.

Do you do anything except have board meetings?

You know, occasionally I'll meet with them. We have new board members, I'll go out to wherever they want and review the material with them. If they have a difficult time with something, don't understand the issue I'll go back out again and review that. Take some time. They appreciate that. I also created an environment that's transparent which means that if they need—if we bring in the experts—they don't just rely on me. We'll bring in the experts, the underwriter, to allow them to ask those questions directly. Here's something that was really interesting and really helpful—a chairman did this one year. He asked me the question and I give him the answer and then at lunch he asked the actuary the question and she said basically the same thing. She said, I'm glad to hear that. I know I hear it from Stan but its also really good to hear it directly from you. What I like about that is that if its transparent they don't need to be worried that I'm trying to blow smoke at them. They can trust what I say and they can feel comfortable

Stan Corcoran
Woodstock, Vermont
July 15, 2010

that they can have direct access to the experts and consultants if that's the case. And they like that. I think what that engenders is a very strong sense of trust. Its more than just a pool administrator. Other folks—are independently coming—if we do an audit and you want to ask somebody about the result go ask them. Its okay. So I tend not to hide anything. And the other thing I do which I think is really critical—I alert them before a crisis happens. Or if something is about to happen I call them up right away. I say this is not good news, I want you to hear it first. This is the plan we have in place, we'll talk about it at the next board meeting but I don't want you to read about it in the paper. You do the same thing.

I do.

You've been at this since...

Been at it for a while. What are the goals for your pool in the next 5 years?

Here's what's significant. Every year we have a strategic planning session and we look at what are the challenges for the upcoming year. But more importantly with the health care reform, we're not gonna go 5 years. For health it's a 3 year plan.

We certainly have target surplus goals which are significant. Let's take the generic—the comp and liability. Given where cities and towns are right now, we constantly get back

Stan Corcoran
Woodstock, Vermont
July 15, 2010

to this long-term price stability. So more immediately is to get down to the target surplus goal. At the end of that period, then have modest growth in premium of 2 or 3 percent per year. Basically, a CPI index. And that's the financial goal. In terms of growth goals, I don't need any more growth. I'm not interested in top line. What I am interested in is bottom line. Bottom line meaning that the losses and the quality of risk continually improve. We may have folks come in, which is okay, but we don't need anymore members. We look and say you know what, what does that offer the pool? All it offers is they've got a lot of work to do, they could deplete the surplus that other members have generated. Why are we bringing them in? However, if there's a change in management that is very interested in risk management because they've come from another community where they demonstrated that, we give them almost a trial period. We'll give them plenty of free loss control services and if it turns out that their risk improves so that we can bring them in—we'll actually give them credit on their premium when they do come in for the work that they've done.

But you've asked the question so what are the immediate goals? The immediate goals for us are to continue to provide financial relief for the members. Next year if FY11 is gonna be difficult. FY12 will be a harder year just the nature of the lack of funding that's gonna be available. So we need to continue to provide financial relief in the form of credits and that will actually further reduce our surplus. And then the year after that we will then begin to have modest increases in the premium just to level off the surplus.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

So do you worry about the day of reckoning on that kind of stuff?

Oh yeah. It keeps me up. But this is what we do. Every year when we go to the board we provide them with a 5 year financial analysis and projection. Its an ongoing 5 year plan. Our pricing isn't done one year at a time; essentially its done 5 years. So there shouldn't be any surprises.

How do you pull that off? I mean you don't know what you're going to have to pay for excess or reinsurance necessarily.

We have a 3 year guarantee on our property reinsurance and we tend to get guarantees on some of the others. The other thing is you have to have a lot of surplus, which we do, we can kind of weather some of the liability. And we only do it for the larger members. I mean only the best experience members. We say what members if we lost would be a big hole in the program? Let's lock them up right now. That doesn't address exposure, but let's lock them up. And then what's left are those that may not have had a good experience, so those premiums will increase. We continue to look at that. Right now we're evaluating because we've locked up this much business given that we need certain rates from what is left it turns out that that's perhaps a greater increase than what the market will bear. We've got to look at that every year. We do, we look at it twice a year. We look at what our experience is showing. What's the monthly impact for our plan over 5 years. We take it very seriously. I need to go from

Stan Corcoran
Woodstock, Vermont
July 15, 2010

getting to that point in surplus—a modest 2 or 3 percent per year. And our financial plan gets us like that.

You think FY12 will be worse?

Oh absolutely. Here's why—the Federal stimulus money has just dried up. The state government isn't gonna be able to rely on that. Even though there's a projection that tax receipts will go up, the problem, at least in Massachusetts, is the rainy day fund that they've used to plug the holes in the budget, the structural gap—that's gone. They've gone through the rainy day fund, the federal money isn't there so you're looking at a structural gap of 2 billion dollars. Which a portion of that's got to come out of the aid that goes to cities and towns. So that means they're gonna be more desperate and looking for some kind of relief from us. But that's our plan—we have that relief in place for them. So we just declared, for example, an additional couple million dollars plus relief for them. This past June, before the end of the fiscal year. They were really grateful for that. We look at quarterly now and we release money quarterly. In the past it was annually, now its quarterly—can we do that? Given the investment money and investment returns, we can do that. The most important question is you don't want to get to the place where you can't pull out—they say wait a minute, you've given us all these credits etc we got used to it, that was the base. We're not hearing that that dividend and credits were one time.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

That's what worries me.

That's a good worry. You've got to look at the projection of the planning. A reduction in the surplus to that party—but then you pull out of it at 2 or 3 percent.

What's your total surplus?

93 million.

What your target?

Our target was to get it to 73-75 and we're on that target.

Now last year's investments were pretty good for us. This first half of the year's not been so great. I'm sure that's pretty much your experience as well. Do you invest in, what's your portfolio look like?

Mixed for the most part.

Bond heavy.

Bond heavy, 85 percent. Maybe 12, 13 percent in equity.

Stan Corcoran
Woodstock, Vermont
July 15, 2010

What new developments or future issues do you expect risk pools to encounter in the next 5 years?

I think one of the most important things we gotta look at is—we've got a pile of money and we're gonna have the intervention where people are gonna look at that money and want to do something with it. We're already experiencing that with the incident in New Hampshire. Making the assumption that it's a public entity. You have other folks who are looking at the pile of money saying you need to release that money. It depends again on the program. Health insurance—its changing so rapidly. Are you gonna have a pool or are you not gonna have a pool? You can't have a 5 year plan but you can have a 3 year plan. The issues facing health is the increase in the cost of healthcare. So, if each year you look at it and say from some miracle we've been able to keep it underneath ten percent. Okay, you did that. Next year, you have to do the same thing again. That—you kept the increase down but then you've got the same thing again—there has to be fundamental restructure in the healthcare we're providing the country. We need to get away from fee for service, we have to have some global payment reform. How do you get there? I don't know. But without that, its getting to the point where healthcare costs, particularly now they're going to eat up such a significant part of the budget, you're gonna have to look at can I afford to hire employees. Can we have enough employees to do the work? That is a really significant issue. The role of state and federal government in operations of these groups—local government in

Stan Corcoran
Woodstock, Vermont
July 15, 2010

particular I think—is significant. The regulations, etc. that are being passed—Medicare secondary payer, for example, and whether or not that’s going to happen. What we are going to look at is a reduction in staffing, increasing the plan for us to lower the price. See the pile of money? They’re gonna want some of that returned back to them. We may have other folks who are going to challenge that. In terms of exposures {inaudible} the financial burden on the municipality has become so huge that to what extent can they actually pay even for the reduced price of insurance? How long is that sustainable? Once municipalities get desperate they look for desperate solutions. So you could have a company come in and just low-ball the price then have towns go in that direction. They say why, it’s a commodity? What other choice do we have? The other reason—the timing—I think in the next 7 years there’s gonna be a wholesale shift in terms of the management of the municipalities. When new people come in they do not have the allegiance to the pool, they may not even have the background in municipal government. But where else are you gonna get these folks? So there’s gonna be a significant brain drain and a significant change in terms of understanding of the whole concept of what it means. We’re gonna have to re-educate a good deal of folks who may not be buying into the concept.

Do you see moves at the national level to regulate? Sort of thinking about the New York situation and the Kentucky situation. Do you see somebody picking up the banner and saying these really need to be regulated?

Stan Corcoran
Woodstock, Vermont
July 15, 2010

I think its gonna happen at the local level, I mean state level, yeah I do. I just think the government is on a tear right now. The notion that the private sector cannot solve the problem, that the markets will somehow work it out—the sense is that that's failed. In a sense, the government now has to come in and regulate. There's a backlash that's gonna happen with that because the government doesn't necessarily see the inefficiencies that they put in place. I do see that. I think the pools are in a very vulnerable place right now with regard to that. Whether the it's the unions that share information across the country because they see the vulnerability they play hardball. If they see a way to challenge the Leagues they're gonna do that. I think you're gonna have potentially the insurance commissioners take a look at that. They're gonna take a look at some of these failed groups—comp in particular—it's a difficult business and they may change the regulator and potentially with the health insurance, there might be more regulation. If I were gonna place a bet, I'd say there's more regulation coming as opposed to less.

Also with the Federal government needing lots of money because of the deficit, they're gonna look at places to get that additional revenue. I wouldn't be surprised if they came back and said you know what, you really should be taxed or you need to pay some money. In our state, we have what's called payment in lieu of taxes. Who knows what's gonna happen? But the federal money is gonna see a pot of money related to public entities and say why are they keeping it?

Stan Corcoran
Woodstock, Vermont
July 15, 2010

So what are you doing to protect your pool from that?

Part of it we can't protect. We do have to have lobbyists, etc, who have access to the policy makers. Let's leave it at that. Without that connection you could be extremely vulnerable.

Do you have a target equity policy that you can articulate, say this is why we need 93 million in capital?

Yeah we do. We hired two firms review it to address the reasonableness of it—we brought two firms in the board vetted it.

Sounds like you agreed you're a little heavy?

It depends what your goal is. My intuition says it could be a little higher that gives us much greater flexibility.

More options.

More options. Also, think about the position that we're in—we have an AIG company. If they get downgraded we have to go off of the market and we will not get as good of coverage particularly with regard to coastal wind coverage. We don't want to be in a

Stan Corcoran
Woodstock, Vermont
July 15, 2010

place where we have to tell the members guess what—you got wind, you know—this amount and we're only gonna provide this much coverage beyond it and its back to you. That would cause a lot of disruption. So having surplus actually helps us. Regulators don't see that potential scenario. I see its probably inevitable.

I see it as a challenge that's likely to come—whether it comes in 2 years, 3 years...

The challenge being the regulation challenge or the money grabbing challenge?

Greater involvement by regulators.

Finally I had this question that I wanted to ask in particular. Reputational risk is an emerging problem. What are your thoughts about that?

My sense is it has caused, I don't want to mention names, but certain practices fall outside of normal—of course you have decision making that is done in good faith but has resulted in intervention and then national exposure. One of the reasons I think that we're likely to see increases in intervention is a result of that. That's what I'm referring to. They've seen it out there—they're gonna ask the question, "I know you haven't been a problem but other groups have been an issue and we need to take a look at you and regulate you to a greater extent."

Stan Corcoran
Woodstock, Vermont
July 15, 2010

Are there certain policies and procedures you think you could put in place to stall that?

I think it is to the extent that we have good relationships with the existing policy makers and regulators that might make sense and that could be helpful. I think its gonna be a challenge. To the extent that we can, we should be transparent and have those policies in place if someone comes in and asks a question, rather than have legislation filed, we can say—you know we already have these policies in place. We are audited by X, you can see are policies in that regard, there's no need for you to come in and take a look at it. I am concerned nationally with regard to the issues that have taken place that they will want to look at our operation.

You know, its interesting. We had the attorney general talk to us years ago about what are some of the practices out there with regard to the placing of health insurance and some of the broker practices. I was really glad to be able to say we don't use brokers so we don't get into that. But they asked the question to what extent do you take tickets or go on any trips or anything from the people you work with? I was happy to say we don't do that. One needs to look at—what's the practice that cities and towns have to follow with regard to accepting gifts. The second question is how would you like that to appear in the newspaper? You get it. So it seems maybe overly cautious because its fairly restrictive with regard to cities and towns, but we should understand that that's where the line is and to the extent that one veers from that line you are vulnerable to

Stan Corcoran
Woodstock, Vermont
July 15, 2010

being criticized by your membership or anybody that chooses to take a look at your organization.

Okay, thanks for your time.

59:59

Mark Nestor, President, Independent Consulting & Risk Management Services, LLC

July 30, 2010, Anchorage, Alaska

[The recording of Mr. Nestor's interview was lost. The following is from notes of the conversation and follow up material.]

What are your goals for your pool for the next five years?

As a consultant working for 55 pools, I need to understand the business culture for each one. One solution or activity may be successful in one pool and not the next. As a CEO, you can dictate the timeline. As a consultant, I have no control over the timeline. The things that I am seeing in terms of goals for pools in the next five years include:

- Financial Stability
- Improving infrastructure
- Membership Service
- Benchmarking your data
- Succession Planning

Mark Nestor
Anchorage, Alaska
July 30, 2010

I need to assist clients with infrastructure and efficiency. One tool I use to do that, is my Pooling Operations Model. The model consists of eleven “buckets” of core pooling business processes. These processes all have to interface somehow. They help organize a business plan, including top priorities.

Program

Management: Overall management of internal operations for continued program success and continuity including strategic planning activities. This business process overlays all the core processes.

Finance: Management and transactional process to support business accounting and financial activities related to the property/casualty and workers’ compensation programs.

Actuarial: Management, data acquisition and review of key insurance elements vital to maintain a financially sound property/casualty program as determined by insurance standards and principles. This includes proper review and determination of premium rates and losses for all lines of business.

Underwriting: Proper evaluation and determination of appropriate exposure analysis and premium development per lines of business offered by the program.

Marketing: Direct client contact to support new and renewal business processes including acting in the capacity as the “Voice of the Client.”

Claims: The specific actions necessary to properly and expediently process a client's claim per the applicable coverage and line of business that was afforded during the claim occurrence date.

Loss Control: Specific training and risk management analysis with the client to limit, reduce or eliminate potential losses via avoidance, risk reduction, risk transfer or by risk management training.

Legal: Provides key business legal directions and guidance to core activities.

Reinsurance: Specific excess, facultative or treaty reinsurance to support full limits availability within the program, including governmental or regulatory compliance.

Customer Service: Process customers' specific insurance requests including policy issuance, endorsements, certificates of insurance and other program support activities.

IT Services: Systems and processes to support all core services and data management essential to company operations. Informational Technology underlies all the core processes.

Mark Nestor
Anchorage, Alaska
July 30, 2010

Succession planning is dominating a lot of pool attention right now. As long-time staff are retiring, developing staff capabilities and cross training for redundancies in core services is more important than ever.

What new developments or future issues do you expect risk pools to encounter in the next five years? What new trends are developing for pool management? How do you suggest I prepare to meet these new challenges?

One trend I'm seeing is increasing sophistication of data management. Many pools are upgrading their information technology infrastructure to better manage their data.

I'm also noticing some changes in coverage. Pools used to lead the commercial market in innovation. Sometimes, now I think the commercial market is leading the pools.

Because of some bad pool management, I think there may be more interference or control from various Divisions of Insurance. To prepare for that, pools are beginning to look more at the IRIS tests than the earlier pooling standards.

They are also benchmarking their own data using metrics like:

- Net premium to surplus
- Loss reserves to surplus
- Net leverage

Mark Nestor
Anchorage, Alaska
July 30, 2010

- Surplus to SIR
- Change in premium
- Change in surplus
- Administrative ratio
- Reinsurance ratio by line of coverage
- Coverage limits to premium
- Coverage limits to retention

Reputational risk is an emerging issue for current pool managers. What policies and procedures are in place to protect your pool from this type of risk? How do you view the risk and what can I do to prepare myself to protect a pool and its board?

Most pools already have the policies and procedures in place to protect them from reputational risk. They just need to live up to their mission statement, business plan, and operational plans. For example, so long as your pool has surplus guidelines and are living within them, you should be able to withstand scrutiny from either the membership, potential regulators, state government or the media regarding your surplus.

If a pool fails, it is bad for all of us.

Mark Nestor
Anchorage, Alaska
July 30, 2010

The threat to reputation is not always obvious. In the case of the Kentucky League, the pool got tainted by the League Association. The pool suffered because of the parent's actions.

How much interaction do you have with the pool's general counsel and/or attorney panel? What experience and knowledge do you look for in an attorney who will be working with your membership?

When looking for legal counsel, look for competency in the area that you need help, an understanding of insurance law, and understanding of municipal law and, of course, reasonable rates.

Most pools that I have worked for the attorney usually attends the board meetings.

How do personal relationships and political correctness affect your management style in running a pool? What advice would you give a new pool manager dealing with a personal relationship between himself and a board member? Between a pool manager and service providers? How do you handle relationships between board members, especially potentially explosive relationships?

I always try to remember that we live in a fishbowl. Major actions have consequences, so think ahead. Ask yourself, "How does the decision affect your board, members and business partners?"

Mark Nestor
Anchorage, Alaska
July 30, 2010

The International City/County Management Association (ICMA) has a good set of guidelines.

Using tools like the ICMA guidelines can help minimize board conflict. A detailed business plan and strategic plan can also serve well in this regard.

**Steve Craig, Managing Director, Virginia Municipal League
Insurance Program**

December 8, 2010, Key West, Florida

Okay. Steve—this is Steve Craig on the 8th of December, quarter 'til noon we're gonna have a little lunch at Banana Cabana Café. All-right Steve I think this is recording.

Okay.

Nothing you say can or will be used against you.

Got it. I don't need an attorney then?

No. So a couple of things I need to know. First of all, how long have you been in pool management?

I've been managing director for 8 years and was a deputy for 10 prior to that.

So a total of 18 years?

Steve Craig
Key West, Florida
December 8, 2010

18 years.

And years in risk management?

The same I guess.

Okay.

Oh you mean in insurance. 25. 26 I guess now.

So let's start with the first question—what are your goals for the pool in the next 5 years?

I guess I'd go to our strategic plan goals. We have these sort of broad areas. Financial stability is an area. Within that our goals are to ensure that we're able to continue to meet the mission which is of course kind of a canned answer. The specifics are we're seeing some challenges, like everywhere else, in terms of competition and trying to not chase the low price and maintain our market share in a challenging environment. That's one of our goals. We are working with our actuary to get a better handle since most of us don't report to NCCI the various rates and what that should be. That's become a big issue. Are our rates accurate?

Steve Craig
Key West, Florida
December 8, 2010

[At this point, the recording is interrupted. The following *italicized language* is from notes.]

Another issue is related to that. We want to hold rates stable while maintaining surplus. Another goal is to review our coverages and enhance them where we can. Examples include exploring the addition of airport coverage, cyber and pollution coverage on a pooled basis, excess flood coverage for zones A/V. Another big concern is succession planning. The League's executive director will likely be retiring in the next couple of years.

[At this point, the recording resumes.]

So I think its just the unknown of the outsider and how that might change. Our dynamic is a little bit different because only about 37 percent of our pool members are league members. So the league really doesn't have a whole lot of—I don't want to say they don't have a whole lot of influence but its muted compared to a league and pool who's membership is more or less simultaneous and housed together and all that. I think another sort of 5 year goal is we have a number of board members who are kind of at or approaching retirement age so our board's gonna look a lot different in 5 years. That's a critical thing for me. Just to make sure. I've been trying to do that I've got 2 or 3 comparatively young people—you know 40's, 50's—that I've brought in. I've got 3 board members that are relatively young and should be around for a while hopefully.

Steve Craig
Key West, Florida
December 8, 2010

So you don't have any term limits?

No. We used to. Years ago, but that got changed somewhere along the way.

It seems to me that term limits are counter-productive in a business where it takes a while to even get up to speed on what this organization does.

I would agree with that. Only meeting 4 times a year with very little action necessary between meetings, I think you're exactly right. It takes a full year just to go through the cycle. And probably 2 to really start to get it. It used to be 3 three year terms was the limit. There was probably some upside of that too—primarily if you get stuck with somebody who's counterproductive or just wasn't a good fit for whatever reason there's a way to get rid of them. We haven't had that problem, though, people change jobs often enough and retire and don't run again. But all that's been, you know, kind of {inaudible} I think it's a challenge, though, to continue to educate folks on what—they're coming into this blind with really no prior insurance background—trying to make sure they don't get off kilter on what I know to be the right answer. I mean, you know, what the board has previously agreed is the right answer. But somebody comes in new and they think they know something.

What do you do for education?

Steve Craig
Key West, Florida
December 8, 2010

Well, when a board members gets selected we have a board book that contains our bylaws, all the important documents. The major policies the board has set — relative to investments, dividends, membership remittance, underwriting guidelines, those kinds of things. Bylaws, member agreement. Roles and responsibilities of the board members is a document our general counsel created years ago. Things like that. Insurance vocabulary, a glossary. That kind of thing. I take that out and deliver it in person and I spend a couple of hours kind of walking through that and going over the strategic plan and talking about anything that's currently before the board that's something they need to be thinking about. I go down there and do that in person and that seems to work pretty well. That way they don't come in completely ignorant. And then I encourage them to call me—we mail our board packets out roughly two weeks before meetings—so I encourage them to call me and walk through any issues because a lot of times they're hesitant to say anything those first few meetings out of fear of exposing their ignorance. Which is understandable, since they don't have that background. So generally they'll call and ask me a few questions—what acronyms stand for. We've tried to get away from using acronyms in our reports for that reason.

After your general orientation do you have formal education they can take advantage of?

Steve Craig
Key West, Florida
December 8, 2010

We obviously pay for them to go to the trustee's conferences and encourage that. I think that's a great way to get them exposed—even though pools tend to hang out with their own board members, I think its still valuable. They don't interact with other boards as much. As you know we've done the executive exchange I think that's been helpful. I'm looking to kind of broaden that. In fact I talked to Steve Hansen about that. He was kind of interested in the concept.

Yeah, I think that that's been a nice learning opportunity for my board.

I do, too. Yeah we'll try to get more of those in next year as well.

All-right so are you doing that formally now?

Not formally. I'm just trying to think ok who would be a good person to invite.

Okay so at the beginning of that question you said you were going to go through the strategic plan.

Yeah. The first goal area as I said was financial stability. We already covered one is products and services. To continue to evolve to meet the changing needs of the members and as I've mentioned I've already said what kind of products we're looking at doing to try and round out. We're looking at obviously cyber is a new thing. Not a

Steve Craig
Key West, Florida
December 8, 2010

product or service but we're paying a lot of attention to that whole Medicare set aside or Medicare secondary payer issue. Those sorts of things. One goal is marketing communications type goals. So we have implemented a communications and marketing plan because not only do I have to educate our board members we gotta continue to educate our members and their governing officials. Its just a never ending job as you well know.

The strategic plan obviously has more volume. Have you ever been in conflict with the board's direction and how did you handle that? What were the circumstances?

When we stopped doing dividends that was probably the only time I've really been in conflict and I don't know if conflict would be the right word. But there was some healthy discussion about it—what it meant. I convinced them it was just hard to go from doing it to not doing it. It wasn't hard to continue not doing it. But it was certainly difficult to make that change. That's probably the only time we've really been in conflict. I have some that are pretty seasoned veterans that have been around and I've worked with for a long time. I think I have—I know I have—the respect of the board and confidence of the board so they're willing to follow my lead with the understanding that I'm accountable for the outcome. That's fair. We don't have a lot of that fortunately. I know there's some other pools that seem to have a lot more politics. We don't have any stacking of the board with ex-league presidents or any of that stuff that you hear about.

Steve Craig
Key West, Florida
December 8, 2010

I think a lot of that is credit to our executive director of the league because he doesn't do any of that. Its just a different culture—its always been it should be a business decision to be in the pool and he's always treated it as such.

What new developments or future issues do you expect risk pools to encounter in the next 5 years? What new trends are developing for pool managers? How do you suggest I prepare for these challenges?

Issues—certainly there is some regulatory potential as we discussed previously given what has happened in a few of our sister states and just because of financial solvency concerns generally. The whole Medicare secondary payer issue I think, while its been around for some time, its not where its ultimately gonna land I'm afraid and I don't know that pools are doing a very good job of having our houses in order to prepare for that—what the real cost of that's ultimately going to be. I think looking at our reserving practices and making sure that we're where we need to be is one. I think the whole medical marijuana issue is an interesting one—as it goes around the country what does that mean—does that become an ADA issue if its legalized for medical purposes? What does that do for return to work and driving vehicles and liability? A lot of open questions on something like that.

The green movement I think is an interesting potential area that we really haven't paid a lot of attention to. You have states like Virginia where local governments don't really

Steve Craig
Key West, Florida
December 8, 2010

have any authority unless the state expressly grants it to them so the idea of them passing ordinances to require or promote green anything—they can't do unless they have permission from the state so that's an issue. You've got building inspectors doing certificates of occupancy for those types of buildings that may be tighter creating sick building issues, they may have vegetative roofs that may have structural compromise issues. There's all kinds of little things that we haven't thought much about. Let's see, other emerging—the market—the change from a soft to a hard market is overdue for a whole lot of reasons that you know as well as I do and I'm not going to articulate here. The main one being capacity—they can't live off these paltry investment returns forever and interest rates start to rise that's gonna kill insurance companies portfolios big time. So what does that mean for reinsurance and retentions and our ability to pay?

The trap we all fall into is it's cheap we buy it. And then you don't want to know buy it because now all of a sudden you've got the risk. I think the trend for us is bigger and bigger retentions. Forced into bigger retentions which obviously creates a lot more volatility at the pool level. For example if you go back ten years we were paying about 2% of our premiums on comp for reinsurance with a \$400,000 retention. Now I'm paying 6% and a million retention. That's a big difference.

And so I'm not sure given what happened in the early 2000's with respect to not just NLC Mutual but other insurance companies and pools who goofed in the nineties—I want to make sure that doesn't happen again with pricing.

Steve Craig
Key West, Florida
December 8, 2010

I want to follow up on the regulatory potential.

That's an interesting one you and I discussed previously. I have a hard time envisioning Federal regulation, but tighter state regulation certainly and perhaps more consistent regulation from state to state. I don't necessarily think regulation is a bad thing.

Certainly compared to other states we have more of it in Virginia. We've had historically a very good relationship with our bureau. We certainly work very hard to make sure that's the case. We go to them a lot for advice, counsel, conference. Even if they're not required they've never told us well there's nothing that prevents you from doing it but we don't think it's a good idea. They typically say well you don't need permission to do that but here's our two cents. You know, whatever. So I think that relationship can be managed just like any relationship has to be and it just takes work.

Who is that regulator?

For us it is the state corporation commission, under which is the Virginia Bureau of Insurance. So there's an insurance commissioner and regulatory staff and those kinds of things. All pools in Virginia are regulated similarly. Of course there's only public entity pools for property and liability we have of course our private sector work comp pools in Virginia—contractors and retail merchants and things like that. So on the comp side all of them have to get their rates approved. That means that the state's actuary

Steve Craig
Key West, Florida
December 8, 2010

looks at them and says these are reasonable or not. We're not allowed to return any dividend money until we get approval from the bureau on any line of coverage. We are required to submit our financial statements each year—they have to be clean opinions. We are audited by the bureau they come out and spend about three weeks in our office about every third year. And look at everything—its like a financial audit—they're looking at internal controls—just like a financial audit. And its not a bad thing. So I think that every state has an insurance commissioner and I'm not sure they're going to be willing to cede any turf to the federal government. But I can certainly see them having more nationwide standards or model regulation—something to that effect. Like I said I'm not sure that's a bad thing. [14.49]

Okay let's move on. Reputational risk is an emerging issue for current pool managers. What policies and procedures are in place to protect your pool from this type of risk? How do you view the risk and what can I do to prepare myself?

Obviously, with what's happened in Kentucky and Tennessee and other places that's become a more pronounced issue. Policies and procedures—I'm not sure that we have a lot of policies and procedures. We have a governance policy and we have a gift policy—all the normal things you would have through a governance process. Which we did in '07 is the first time we did that. For years we sort of operated on the principle you treat it like its your own money and that seemed to work. But as our staff got bigger and we got younger people on board who didn't really understand how that worked we felt

Steve Craig
Key West, Florida
December 8, 2010

the need to have a little bit more defined. We have, for example, that you can't accept any gifts. Its not a written policy but our policy is we have no corporate credit cards. The company is not at risk for anything until its approved by me. A safety consultant has to get approval from the director of the department and then it comes to me to sign the checks by hand which I do every morning. I have the right to at any time say no way—we're not paying for the movie in the room we're not paying for the \$20 breakfast that's not reasonable. So we've had very little of that fortunately. We do have some sort of traditions—the board for example we don't go out of the state for meetings. Our sister—our competitor the county association has been to Costa Rica, the British Virgin Islands, they've been out to West Virginia—we just don't do that. So we're very conscious about the public perception. We're certainly attuned to it and wouldn't do anything to damage it.

I think the risk is real. Perception is truth at the end of the day. So if you end up in the paper in a negative light or a member is in a negative light it can have a profound impact on the member's moving coverage—there's a lot potentially there. Even if what happened isn't all that bad so I think we're mindful of it every day. In terms of how would this look in the paper. Often we remind our staff—we have a communication policy for example. And it talks about how when you send a letter or an email—we just remind them email is informal but everything you write you gotta think about being

Steve Craig
Key West, Florida
December 8, 2010

deposed and being on the witness stand. Everything you write you should have that in the back of your mind—how am I gonna feel reading this on the witness stand. That's kind of our guideline. So I think reputational risk is real and important.

Let's go to number 14. How much interaction do you have with the pool's general counsel and what experience and knowledge do you look for in an attorney that will be working with your membership?

We have a couple different things. Our general counsel does no defense work. And then we have a stable of defense attorneys that represent members who are appointed for claims. So our general counsel is—you know we have our very unusual situation of the 90 year old lead counsel who doesn't come to our meetings anymore and I have no interaction with. But their successor I'm already using—they're our coverage attorney. They for example rewrote our Local Government Liability policy which is a blend of law enforcement, public officials and General Liability. So we use them for that. We use them for legal opinions on various things that have to do with our operation and what we're doing.

Like personnel issues?

Steve Craig
Key West, Florida
December 8, 2010

No I do all of that by myself. And of course we have an HR director now so that's all done by her. We've had legal action before. The insurance company appoints an outside person who happened to be with our general counsel's firm by the way.

So you didn't have a conflict.

Did not have a conflict there. The main reason we didn't have conflict is we've had a rule from day one that our general counsel cannot do defense work.

Now why is that?

Because they help us with the policy and they shouldn't defend their own advice. We think that separation makes a lot of sense. And they don't like it, by the way, they want to do defense work because there's more money in it. But we told them—you can be the defense counsel but you can't be the general counsel. Your choice.

Now the second part of that question was what I'm looking for in general counsel—someone who has some idea about insurance. I will tell you that's an upcoming conflict with my board—going back to your other question—because they want somebody who's a local government attorney. I've had these conversations privately with the one

Steve Craig
Key West, Florida
December 8, 2010

in particular who's an advocate of that and he's named the person he would like it to be and I said I think that's a bad choice. We don't need a local government attorney we need somebody with insurance experience that gets it. We've been sued 3 times in the last 5 years by members—we don't need a local government attorney defending us we need an insurance attorney. So I've got somebody lined up that I think is the right person. They helped us with the merger they helped us with re-writing policies, those kind of things.

As far as what we're looking for with the members—that's a hard one for me because its been so long since we've had a new person on the panel—we've had this stable for so long. We wanted somebody who's firm wasn't taking plaintiff's work against local government, that was kind of a parameter. My predecessor had no plaintiff work period. Well, that's hard to sustain because every firm wants to do the full compliment for their clients. They can sue all the private sector people they want but not local government.

We're looking for somebody who's well versed in the compact of Virginia, sovereign immunity—we have a different group of comp attorneys than liability. So you know we want somebody well versed in the immunity, which is obviously the big 800 pound

Steve Craig
Key West, Florida
December 8, 2010

gorilla in our state as to how that works. Its fairly convoluted and complex—it's a lawyer's dream because its ambiguous sometimes. That's probably the big one. We want someone who understands that while the legal canon say that they represent our member in the case the pool is paying the bill and they need to be a partner at the table. We've had a few instances where we've had some conflict and those people aren't assigned any more cases at the end of the day. [22:22]

That I've always found to be kind of the difficult thing for them to struggle with—not everybody, those that didn't have problems are in the stable.

Its where we've gotten at odds with a member. That's typically it because in our professional liability policy they can block a settlement.

The member?

Yeah. But if they block the settlement and we go to trial we're only responsible for the settlement amount. They're responsible for anything over it including the defense cost from that day on.

Ours is similar—basically I'll call the member and say look we're going to settle this I called to see what you feel about it and let you know that it makes economic sense. If they say well we feel really strongly against it then I'm authorized to

Steve Craig
Key West, Florida
December 8, 2010

offer you the opportunity to take the risk yourself. We'll pay up to the amount I'm going to settle for, anything beyond, you can handle. Nobody has yet taken me up on that offer.

Mostly what we get is the opposite. We want to defend it and they will send us a letter demanding a settlement within their limit.

[Steve tells a couple of war stories here that he warns me ahead of time are not germane to the question.]

Do you ever use municipal attorneys? [26.13]

Here's what we will do—like the city of Suffix in our pool they're a large city, they have a full legal staff. We'll let them handle their own kind of small claims if we're pretty confident its gonna be a pretty routine matter. Or lets say it's a warrant and debt action or something where they've just gotta show up and file a response. On occasion, but not generally. The last thing we want is them to screw up and hand it to us. But we do let them go and do some simple things just because they're already there and it makes so sense to pay somebody to drive from Richmond if they can walk across the street and file it.

Steve Craig
Key West, Florida
December 8, 2010

We rarely use municipal attorneys. Now we don't have a lot of members that have an actual legal staff.

So they're doing it on a contract basis?

Generally. But it gets back into serving two masters. Even though the ethics code for the attorney says the client is the city, when it's the municipal attorney I'm not sure how much of the municipal work I'm getting billed for versus the litigation.

We find with our members the smaller ones, which is the vast majority, that don't have in-house counsel—they're very reluctant to call their counsel because they'll be billed. Which actually has proven to be a good thing for us because they call us. So we've actually created a few little coverages like we have a grievance procedure for public safety in Virginia—we actually threw in a coverage because we said rather than them wing it with no attorney, which is what they were prepared to do, we sent an attorney and then we added a coverage like \$2500 occurrence and aggregate—so you get one a year. That's proven to be pretty good. Of course we have our HR stuff now that we're doing.

I've got a similar coverage for administrative hearings that's up to \$10,000 per year on a 50:50 basis.

Steve Craig
Key West, Florida
December 8, 2010

Is that like EEOC?

Yeah.

We cover the administrative part but we don't cap it. Its just part of our coverage. Now there's a place where we get into a lot of conflict with members because either they're not aware of it or they choose to not exercise it, they'll want to hire their own attorney. He's billing 4 to 500 an hour, we pay 150-175 an hour. So they'll go get 100,000 in the hole with him and then they'll want us to pick it up and continue to use the same attorney. We're like nope, sorry. We don't do that. We have attorneys and we pay them a whole lot more reasonable rate and they're equally if not better than the person you hired so that's on you. We used to agree to pay our rate and then pick up the difference and then we decided we're not paying any of it because sort of like the HMO; we have a small stable of attorneys but we give them a lot of work.

That was going to be one of my follow up questions is have you got negotiated rates?

Yes. It varies by firm. On the comp side we pay anywhere between 105-140 depending—Northern Virginia is more expensive than Southwest Virginia up close to DC type thing. On the liability side it's a little higher—I would say we pay between 150

Steve Craig
Key West, Florida
December 8, 2010

& 180. With the exception of—we have one land use attorney who is the guy—I think we pay him about 200 and he's worth it. So unless it's a niche thing like that, and most of them have been around for a long time. You know, we kind of follow them from firm to firm.

That's comparable to what we're paying except we're pretty much paying everybody \$175/hour.

Oh really? Yeah, they give us a proposal and if it's less—great. We'll get a senator who's a lawyer and I say no problem have him call me. Then I say here's what we pay—here's our rate—and then we never hear back from them. Usually I tell them 150 on the liability side. I give them the lowest we pay. And that's for the partner, obviously for associates for paralegals its less. And usually we never hear back.

That's my strategy typically, too.

Its like yeah, we'd love to use you but here's what we pay.

We've got a fine stable of attorneys and they're all happy at 150-175.

And you know I'm not opposed to having a few delegates and senators as defense counsel. We got them as Plaintiff's counsel. It can't hurt me to have somebody up

Steve Craig
Key West, Florida
December 8, 2010

there to help me if I have a problem. I'd love to figure out a way to do it but I'd hate to pay 'em \$250/hour for the privilege. [31:20]

Okay thank you for that. How about personal relationships and political correctness in terms of how they affect your management style in running your pool? Do you want me to read the rest of it?

Yeah let me hear the whole question.

I didn't pick this just for you. What advice would you give a new pool manager dealing with a personal relationship between himself and a board member?

So this is board relationships, not employees or members?

Well the question is how relationships and political correctness affect your management style.

Okay, so I think there's 3 areas: there's employees, there's members, and there's boards. I could probably offer a comment on each one. [33:38]

Yeah let's do that.

Steve Craig
Key West, Florida
December 8, 2010

Okay, employees. First of all a lot of pool directors come up through in-house promotion like you and I. Now all of a sudden your former colleagues are your employees. That's a much more difficult transition—at least it was for me—than it was for them. I was the last one to figure out that the relationships had changed. It just wasn't the same. I don't know that I can articulate it any better other than to say that it was not the same. Maybe that doesn't happen everywhere; it certainly did in my case. All of a sudden I was treated differently because I'm the boss. So that's one thing. You've gotta have—I mean I think those personal relationships are important with staff—in particular your department heads. But there's a real dynamic there that takes a lot of getting used to all around if you're promoted from within. So for a new person I think that's something to pay attention to. Realize that its changed. Realize you've got to keep your own confidences more than you might have in the past. Realize that your new circle of colleagues is our group and that's where you need to go to commiserate or ask advice or share. You can't, you just can't, you gotta keep your own counsel. So that's with that.

With board I think that's the most critical relationship, obviously, for continued employment. The care and feeding of board members is important. Nothing more important than that. I think that a new pool person's gotta think about well what is this. Who is the leader of this organization? Is it the board or is it me? In a traditional CEO,

Steve Craig
Key West, Florida
December 8, 2010

the CEO is the leader and the board is charged with policy and the CEO is charged with leading. So I think that its important that you lead your board. I try to lead them where I think they need to go I mean at the end of the day what's the point otherwise? I think the personal relationships are important—I've visited with every one of my board members on their home turf. I've certainly broke bread with them a number of times and taken them to different places and trying to go to NLC RISC and get off-site and spend some time together. I think all of that is important. The main thing is to make sure they have confidence in you as the pool director. That's the number one thing. If they have confidence in what you are doing than you can get a lot done. If they don't then everything is a struggle so to me that is critical.

Members—I don't have a tremendous amount of interaction with members anymore. My role primarily right now is operations and I have people in the field. I tend to get involved more when its reached a certain level because of an issue or problem or a claim or something. And its been my personal feeling that I try to stay removed from the day to day because my people need somewhere to go and if I'm in on the initial decision than there's nowhere to go to resolve a conflict or correct something that you just missed or made a bad political choice or whatever it is. I don't know whether that's the right thing to do or whether that's the normal thing to do but it works in our case. Just from my personal background I have not been on the operations side. I'd been on the marketing and underwriting side and felt I needed really to focus on the finance, the

Steve Craig
Key West, Florida
December 8, 2010

technology, the personnel—the things I was inexperienced in. I actually found I liked it better.

But it is interesting—I would actually encourage a new pool person to get out and meet the members, as much as you can. Because the longer you're out of that, people retire, pretty soon they don't know who you are. Which has its plusses and minuses.

You understand better what they're doing. You have a personal relationship with them.

How many members you have?

150.

See I've got 460. Its pretty hard —out of that 460 I probably have 150 with less than a 5,000 dollar premium. So those I wouldn't focus on necessarily. I focus on the ones that I know need focusing on—I have ten or so that pay me a million dollars a year. Those people I know. And see them regularly. We have quarterly meetings in our office for example with large members—I don't usually attend those meetings but I always go in and say hello. Its funny our culture has always been—my executive director is very hands off. And so I've always tried to afford my department heads the same courtesy that my boss affords me. That is you run your department, I don't

Steve Craig
Key West, Florida
December 8, 2010

interfere, you come to me when you need guidance and you're accountable for the results.

Now its interesting to me that when you talk about personal relationships it never occurred to you that you might have like a really personal relationship with somebody on your staff.

What do you mean?

Well I mean like we both know pool directors that ended up getting married to their secretary.

Who got married to their secretary?

[NAME REDACTED IN THE INTERESTS OF GOOD TASTE]

Oh true. Yes. Well you know its funny—down at the league we actually had our communications director and our deputy director got married. That's at least ten years ago. Outside of that I'm not aware of any personal relationships going on at work and I think we're a small enough group that I'd know. We don't have any policy against it. We have a policy against--for example we have a mother-daughter combo—one's in processing and one's in claims but they can't have anything to do with one another. We

Steve Craig
Key West, Florida
December 8, 2010

have some of those things in place but we don't necessarily have a written policy that prohibits fraternization. Number 1 its just not gonna work.

Number 2 I'm not sure its necessarily...

I don't think its necessary. I mean I met my wife at work we met in the carpool. It happens. You spend enough time at work.

That's your circle.

Exactly. So yeah we haven't run across—its certainly never been a problem where we are.

How about service providers? Personal relationships with service providers?

That is probably my main area of focus. I negotiate the re-insurance. I oversee all the vendor relationships pretty much. I review the contracts, interact with them. Whether its medical bill review providers, vendors, rehab nurses, whatever it is. Those are important. I think it's a place that often gets overlooked. Not so much on reinsurance but on some of the other one's I mentioned. I think it gets overlooked. I don't know about you but I'm sick to death of seeing contracts that limit liability and offer no accountability to whoever is selling you whatever their product is. Whether that's a

Steve Craig
Key West, Florida
December 8, 2010

claims system or whatever it is. I spend a lot of my time on outside contracts. And vendor relationships. In that area I make it a real point—I don't do a lot of lunches. I don't want any holiday gifts. I just don't need any of that mess.

So that's where you're drawing the line?

What I tell them is look—you don't have to come take me to lunch. That's not gonna help you keep the account. I want you to do a great job, that's what I'm looking for. I make it a real point not to do a whole lot with vendors.

So its not real personal its all business?

Yeah, it is. I try to make it a collegial and positive relationship, but its business. I don't need to know who their kids are and what they're doing on the weekend. Those are just not relationships I want to get too entrenched in. You might have to fire them at some point. In fact you likely will. You're gonna change auditors, you're gonna change brokers, you're gonna change vendors and there's no need to get too personally involved in that.

Let's go back to the social media thing. I hear a lot of people say—oh you got to get on Facebook. You got to get a twitter account. As a business you gotta do this.

Steve Craig
Key West, Florida
December 8, 2010

Right right. And a lot of our members are doing it.

I'm not convinced.

I'm not either. When I came to the league in 1991 we had 60 towns out of 180 that didn't have fax machines. And I only know that because we used to send out our legislative bulletin—we had it twice a week. It was done through Overnight Fax, we contracted that service out and 60 towns didn't have a fax machine and we had to mail theirs. And so we've evolved of course to where virtually everybody now has Internet and email and the ability to have that stuff—not having a fax machine is unheard of. In fact now you can fax from your computer. So its hard for me to understand why—who would want to follow us on Facebook? That's kind of... our communications director pointed out to me. She said I tell you what—that's my essential source of information on whatever I'm interested in. Whether its work or personal or anything I have it all routed to Facebook. And now of course now Facebook is thinking about expanding into email—it's a big play for them. An employee that doesn't have—let's say everybody doesn't have Internet—they have it at the entity but not every single employee has access to us. It's a great way for them to stay in touch and get our news letter and know what's going on. Not just us but whatever they're interested in personally or otherwise in their life. So I signed up for KLC's just to see what it was all about. Basically, all it is is the newsletter's been published click the link and go here. The train

Steve Craig
Key West, Florida
December 8, 2010

calendar's been updated. So its another way to push information out to your members.

That's all I see it is.

Well maybe they're not using it to its full capability.

They may not be but I'm just trying to identify is it even worth our doing it. Its not a heck of a lot of extra work. We're not doing extra stuff that's only for Facebook. We're just using it as another avenue—just like email or hardcopy or whatever it is to push information out to as many people as we can. I don't see the downside. I guess I'm trying to recognize that I don't want to be like the preceding generation that doesn't think we need a website. You know. We brought in this communications director, she's 30-35. I've got to let her do it. It doesn't cost me anything. Its free to set up an account. You can set it up such that your members can't make comments on your Facebook page. So your competitor can't sign in and bad mouth you. Now, if I can do away with that and its really just another way to push data then I'm willing to do them.

Now I'm less convinced on a blog—she wants to start a blog and I'm thinking who's gonna read the blog? I don't read any blogs—not a one. I have no interest. I certainly don't follow anyone on Twitter—nobody's got anything important enough for me to hear from several times a day on anything. I also signed up for—it was like the International City Managers Association Listserv. I had to get off of it. They were sending me so

Steve Craig
Key West, Florida
December 8, 2010

much stuff every day that—I think the challenge is to be careful that we're not overwhelming people with information. [46:53]

[short side conversation with other people]

I think that there's a balance in terms of recognizing that we don't overwhelm our members. I think there are pros and cons its something that we're gonna need to explore. It's the next thing that is here. I don't want to fall behind the technology or communications curve.

I don't want to fall behind our competition... [48:47]

Well we're way ahead of our competition. If you go on their website today their current newsletter is from 08. I don't want to fall behind period. I'm really trying to be mindful of what other pools are doing and what else is out there in the world. We're starting to do a whole lot more press releases. We've changed our newsletter quite a lot to do more success stories about members using our products, trying to inspire others. We've got somebody that can pay attention to that now and can really go out and interview people and take pictures and make it a more personalize newsletter. Members are always interested in knowing what other members are doing.

Steve Craig
Key West, Florida
December 8, 2010

But the goal is to always tie it back to they did something that we recommended or we gave them money for or helped them implement or gave them a product. Hopefully it inspires people to call us and say hey we could use that. It's a balance but I see the social media thing simply as another avenue of communication for those that care about it.

For what its worth I've enjoyed getting the emails from your outfit. They're looking better.

It used to just be a series of links. Now its stories—we're trying to make it a little bit more of a teaser.

I've shared some of that with my communications people, too.

Really I like it. She's done a bang up job. Part of it is I just want to give her some room to run. She's got all these ideas, some of them will work some won't. As long as I can minimize the downside. The other thing we did was we went to a monthly communication—we had a quarterly newsletter and then we were bombarding. Sometimes it's the same contact and they're getting like 8 emails a month from us. If its important enough to send out outside of the communication I have to know about it. And we do send things out from time to time but we try to minimize it and keep it all in that communication. So we went to our members and we said we heard what you said,

Steve Craig
Key West, Florida
December 8, 2010

we're gonna cut down on it here's what we ask—spend twenty minutes a month reading the communications we send. We're getting about a twenty percent open rate. That's actually pretty normal. I don't know if you noticed that I stole a title from one you wrote.

No I didn't notice.

It was um.. one you wrote about—I took the title verbatim I figured you'd see it. It was literally the title of your article I used it and wrote my own.

End of Tape [51.47]

John Neilson, Executive Vice President, PERMA

December 9, 2010, Key West, Florida

Its Dec. 9th, I'm here with John Neilsen, Executive Director of PERMA.

Currently Executive Vice President, effective January 1st I'll be President.

The first question that I've selected is what are your goals for your pool in the next five years?

Solvency.

That's a laudable goal, John.

Solvency, and I'm only half kidding about that as a goal. Our pool is in a very difficult environment from a regulatory standpoint, from a benefit level standpoint, from a competitive standpoint and at this juncture the pool had to go through a process of admitting some of its own sins and recognizing that there were some accounts that were poorly underwritten and some claims reserves that were not timely posted.

John Neilson
Key West, Florida
December 9, 2010

Upon my arriving there about 18 months ago, knowing that I was going to be succeeding to become the president of PERMA in fairly short order, I made it one of my number one objectives at that time to figure out what was going on and over the course of that time identified as I said some poorly underwritten accounts and some claims errors that I think had underwriting implications ultimately because they'd been slow to reserve. Understated claims reserves in the aggregate then lead to understated IBNR and loss development which leads then to undercharging pricing subsequently.

As I understand it there was some discounting of reserves as well that reinsurers weren't aware of?

Yeah I think that allegation is not true. I think NLC was aware that there was a discount because that has been in place since the inception of the program and I don't know how there would be a disconnect in that regard. So we've actually looked at whether or not the discounting should go on and been advised by our financial auditor and actuary that once you go down the discount road it's difficult to unwind it and you're better off just leaving it alone.

Why does he say that is?

I think its primarily because you'd have to recast all the financials that had ever been done. It's a monumental task to unwind a program that's been discounted for so long.

John Neilson
Key West, Florida
December 9, 2010

Would you have to unwind it or could you just make a footnote in the financials and say, drawing a line in the sand as of 2011?

I'm relying on expertise outside of my pay grade. They're telling me you don't want to go down that road it creates confusion. At this point in our history that's the last thing we need.

I hear you.

We're looking for stability and clear consistent direction.

From my perspective its helpful to be able to pull out financials from years prior and compare them and if they match, then you can actually take something from that.

Correct, if one set has been discounted and the other hasn't...

Then you have no history there. You almost have to go back at least 5 years and undiscount all that, which when you're pressed for solvency is just money down the drain.

John Neilson
Key West, Florida
December 9, 2010

We've decided its better if you're going to add conservancy to the analysis to do that on the claims side and then that will flow into IBNR and loss development and they'll pick it up on the actuarial side.

Okay, one of the reasons I was anxious to talk to you was this question here which is future issues that you expect pools to encounter and in particular I'm going to push you towards the question I'm really interested in—regulation. I mean you've had problems, Tennessee's had problems, Kentucky's had problems, what do you think?

There's a risk of Federal regulatory oversight at some point and that would be bad for pooling, I think. And so entities like AGRIP and NLC RISC/MIC and other interested parties I think would do well to try and defend against that possibility and prepare themselves for that eventuality should it arise.

Now I've spoken with other people about this and they're like well, the states don't want to give that, but I read the same trade journals you read.

In normal economic times I would agree with that but given the stress that governments at all levels—federal, state and local-- are under, given the threats to commercial insurance interests and the difficulty they're having turning a profit—there is sort of a

John Neilson
Key West, Florida
December 9, 2010

perfect storm that could be envisioned that could create havoc for the pooling industry as its come to be.

I wouldn't be surprised, because I know that at least my division of insurance director is getting to be the long term director. She's been there 8 years, maybe 10, and I know that she doesn't like pools particularly. She tolerates them, but I can just see them going to a conference, sitting in places like this with a round table of 9 of them, and all talking about their problems with pooling and end up concluding, "We've got to do something."

NAIC went down this road about 20 years ago. Its actually one of the main reasons that AGRIP exists today. We were all part of one happy family inside of PRIMA and the old PRIMA pooling section and somehow, about 1992-93, somewhere in there NAIC got the great idea—gee there's been a lot of insurance business has left the commercial market and gravitated to these pools. At that time pools were a relatively recent phenomena the earliest one's starting say in the late 70's and into the 80's. By the early 90's there was a sense that there was this big group of business that had moved and wasn't really particularly well regulated. If it was regulated it was done on a state by state basis. All of a sudden the NAIC said we've got to consider regulation and essentially called hearings. We asked PRIMA at the time to advocate for pools as an industry, as what we considered to be probably the best alternative that local governments of all sizes have—that's not to say that self-insurance isn't acceptable if you have a large enough

John Neilson
Key West, Florida
December 9, 2010

risk—but particularly for small governments joining together with other like entities was a very appropriate way to do business and ought to be defended as a best practice not attacked and dismantled by NAIC or anybody else. The answer we got back from PRIMA was we're an educational organization and we can't take a position of advocacy. They actually told us flat out that they were not going to help us with this. So there was a group of us that went and gave testimony, I observed it, I didn't give testimony but others within the pooling industry we chose as our representatives to go to Pittsburgh and testify and advocate that pooling served a noble purpose and that it ought to be exempted for good reasons from national regulation, the nuances, the needs of local governments in different states was not uniform and that the best way to regulate was two-fold: one through individual state regulation and second through our own efforts to self-regulate. It was at that time that the pooling standards that AGRIP has developed were first propagated and presented to NAIC as an alternative to regulation.

Now, John, the original pooling standards were a PRIMA development were they not?

PRIMA pooling section is where they started and then they've had a couple of evolutions. Essentially, when the split with AGRIP and PRIMA happened, we secured the rights to that program I'll call it for lack of a better term. There was a long drawn out negotiation to negotiate assets, pooling section members were actually given additional contributions to promote the pooling section back in the day—we generated several

John Neilson
Key West, Florida
December 9, 2010

hundreds of thousands of dollars in terms of revenue that was coming in just for pools and with the split we said well, shouldn't we be entitled to keep all or some major portion of those funds that were contributed by pools for pools? Along with that there was this discussion, what about the advisory standards, who would own that, who would continue it? We argued that the pooling industry, why wouldn't we have ownership of it? You don't want to have an advocacy role for pooling, after all, what happened with NAIC. So ultimately it worked out that that would then be handed over along with some money to basically help start AGRIP. That was the seed money that got us started.

So to follow up on that, not so much part of this interview but more just for my own purposes—who were the leaders in pooling at that time? Who did the testifying? Who were the hand picked, chosen people?

There was a guy from California who was the lead, I might have to send you an email if I can come up with his name for you—he died about 4 or 5 years after this, that's probably why you don't know of him. He was one of the champions and then Rufus Nigh and Lou Leigh were a couple of others that were involved in that, either in the preparation of the testimony or actually testifying. I'm sorry I can't remember this guy but he was from northern California, he was a pool CEO, he'd been around the pooling section he was very influential in CAJPA at the time and there was agreement among the group that we needed to speak with one voice. We needed to identify 2 or 3 people that could go and present the case for the pool.

John Neilson
Key West, Florida
December 9, 2010

Thanks. So back to the main question which was trends and developments or future issues you expect that we should encounter in the next five years, and what's developing in pool management.

There is this threat of national regulation. I think there are threats of insolvency. I don't think the circumstance with PERMA is unique by any means. I think there are a lot of pools that are struggling in comparison and that's largely a function of the fact that that underlying the government that they're serving—whether it's a school or a county or a city, special district what-have-you—they're struggling financially and the economic base is eroding the tax base and making dollars more and more dear in the public sector as a result. To the extent that pools are sitting on a lot of money in some cases or many cases even, they are prime targets to be raided—whether at the state or local level. I think there's going to be pressure put on pools to give up their surplus either by coercion, legislation, or just pressure because to the extent that the pools have surplus and the member municipalities don't—that's a problem. It becomes difficult to have the necessary discipline to say, "No these reserves are needed to pay for future claims that either haven't come in yet or have ultimate cost that haven't been presented yet.

At the risk of interrupting your thought process—what are some of the steps you think a pool can take to protect from a raid on surplus?

John Neilson
Key West, Florida
December 9, 2010

A couple of reactions to that. One would be you need to have a sense of your own pool's mind at the board level and the CEO level what an appropriate amount of surplus is. A lot of pools have just gathered surplus with no particular goal or object in mind. I think when you do that you are primed to be a target in that circumstance. To the extent that you've thought out and said, we have a policy that says we should have two times annual contributions in surplus, that's appropriate, or some percentage of your losses—pick whatever standard you wish to abide by. Then you've at least got something you can point to—its thought out, hopefully its reasonable and appropriate and then people will say, "Okay I guess we can't raid your fund, there's good reasons you've put aside this money."

There have been lawsuits as I think you are aware in New Hampshire and Connecticut and other places that have made that exact demand by the equivalent of share-holders, you know member municipalities or their employee unions who have come back and said, what do you mean you've got all this surplus? We need the money back here at the local level—give it back to your members, your by-laws provide for a return of surplus to members—give it back.

What do you call your surplus?

I don't have any surplus.

John Neilson
Key West, Florida
December 9, 2010

What did you call it before?

We'd call it net equity which is probably a better term. There's a variety of terms you can call it. Surplus is probably the least desirable. Net equity. Net retained income, those are all good words to use. [15:00]

Okay, so to go back to the original question—like I said I didn't want to interrupt your flow—but I asked what sort of developments or trends you saw coming in the future, emerging issues. You gave me national regulation, struggling solvency issues, surplus grab—

I think you could see some mergers and acquisitions kind of things. I think you could see pools recognizing that they're trying to compete in a market that isn't big enough to hold both of them and that rather than beat each other up and chase each other to the bottom on price in order to stay in business that ultimately they're really damaging both programs. So I think you could see some strategic efforts to match up independent or regional pools. California would certainly be ripe for that—California's got a hundred plus pools in that state alone and a lot of them are little pools that it would seem appropriate to have some effort to try and aggregate those in some more efficient fashion. You've got a lot of overhead in some cases chasing relatively small risk that's been aggregated together at a county level. That's a very common approach.

John Neilson
Key West, Florida
December 9, 2010

You could also see, I think, the possibility of sort of a segregation market so that there might be primary pools. Rather than just consolidating them into one bigger pool, you might see a horizontal type aggregation where one pool would be primary and then another pool would be excess for several primary pools. There are examples of that that already exist in different parts of that area. I was in California for an excess pool, the Independent Cities Risk Management Authority of Los Angeles, it was an excess pool but it was only done for roughly 30 member municipalities. It could be done on a much bigger level. SELF tries to do this for their schools program on an excess level. I think Mike Fleming, his program, I think they work on both a primary and an excess level. His is a very, very good program. I think people are going to have to become more creative and more nimble and the pooling world is going to have to adapt to the realities of where the country is economically. The idea that local government is going to be starved and everything is just going to stay the same for pools I think is naïve. They're going to have to adapt and find ways to be more efficient with public dollars no less than anyone else at some point.

Okay. If we can go back to this merger-acquisition idea? Have you done any of that? I can see why it makes more sense to cooperate than compete if you really buy into the mission, but at the end of the day the practical issues of egos and who's surplus is going to cover who's losses is complicated and hard to achieve.

John Neilson
Key West, Florida
December 9, 2010

I'm not saying they're going to be driven there out of good will, I'm more suggesting that they may be forced to do that or they'll both go out of business.

If there's a will or a necessity that requires it, cooler heads can probably figure out ways to solve those kinds of problems. Its not going to happen just because people are altruistic—we should really be more efficient it would be good government to do that—that's not a winning argument but we're driving each other out of business, I lost x million dollars, you lost x million dollars, shouldn't we try and join forces here and come up with some more efficient way to do this or we're both vulnerable—I think that's the kind of dynamic that its going to be. [20:07]

Let's talk about reputational risk. Reputational risk is an emerging issue for current pool managers. What policies and procedures are in place to protect your pool from this type of risk and how do you view the risk? What can I do to prepare myself to protect the pool and its board?

Reputational risk is real. A lot of it you would think is just common sense—you don't use the pool's credit card to pay for strippers; probably not the smartest thing you could ever do. You need to have a set of core policies and practices in your pool that extend from the very top to the very lowest level and that are consistently adhered to and that are punishable by firing if people violate them.

John Neilson
Key West, Florida
December 9, 2010

Is that something that you have to have in writing? Don't go into the strip club with your credit card?

You can't anticipate every nuance but your policy should have some reasonableness standard, whatever you want to use, some level of common judgment that a prudent person would abide by. My pool certainly has policies that address those issues. We have policies about accepting gifts, we have policies about double-dealing.

What's double-dealing? I'll give you a hypothetical example, how about that? Just hypothetically. You can have a contract manager of a pool, who's hired to administer the program, who also turns around and hires the auditor or hires the claims division to do that kind of thing.

Email those policies to me if you can.

Okay I can do that. That's what you're asking?

That's what I'm asking.

To the extent that you can have someone put in authority to then further enrich themselves through awarding contracts or hiring people or giving gifts.

John Neilson
Key West, Florida
December 9, 2010

Or rent it to their own place.

Right. Again, suppose a CEO had a spouse who was an attorney and they happened to do all their legal work through that firm. Or at least a large percentage of it. Or they had the husband and wife, the CEO and spouse, they happened to own a restaurant. Every function that was important to the pool was going to bring in 500 or 800 people to an important dinner would just happen to be run through their restaurant. Its corrupt. Its not appropriate.

That damages reputational risk. it damages people's confidence in just the day-to-day dealings of the pool. They may be doing everything else right, but those kinds of activities undermine public confidence and trust in the enterprise. It gives everyone a black eye. And usually it isn't reserved just for the offenders, it expands to other parties in the industry and that's really the biggest concern I have about it. Not so much what happens to the individual pool, they created their own problems. But now people say that's how all pools are and it crosses state lines.

That's why I selected the question I selected. I'm interested in what does it mean to the rest of us? And I, like you, think it has potential downstream ramifications for the entire industry. How many of these do they have to see with the rare coins or your investment vehicle or whatever.

John Neilson
Key West, Florida
December 9, 2010

The state of Ohio.

Your hometown. Maybe not your hometown but your familiar with the case.

It wasn't a pool in that case, it was the State Treasurer, but the damage is done and it does it flows downstream. We're all painted with the same brush after the fact.

Again, the best defense is to have policies in place and then judiciously and consistently apply the policies. [25:15]

All-right, thank-you that was interesting. Next question: how much interaction do you have with the pool's general counsel and/or attorney panel? What experience and knowledge do you look for in an attorney who will be working with your membership?

I would distinguish between general counsel and attorneys that are doing defense work for the pool. Not all pools make that distinction. I think they do that at some risk to their pool by not segregating those things. Same kind of things we were talking about—could be some double dealing opportunities that jump in.

The relationship I have with counsel is very close. He is actually counsel to the board, primarily. His contract says that the client is the board of trustees of the pool. That's

John Neilson
Key West, Florida
December 9, 2010

particularly important in light of the fact that again, in the pool I'm working for in New York, PERMA, it is a contract management arrangement so that my company, the party that gives me my paycheck, is a different party than the pool itself. So you have PERMA and then a group called Northeast Associate Management, Inc. who I work directly for and who PERMA hires to be their contract manager. So there always needs to be clear lines written as to who the attorney is working for, who the client is. In this case, particularly where there's a contract manager, there's a very clear line between those. It does get somewhat blurred between a CEO and a board and there can sometimes be conflicts that are created because the staff has different interests than the board does.

Have you seen that happen in PERMA?

It hasn't been an issue in PERMA because there is such a clear line. That's one advantage—its very clear who the general counsel works for and who's interests he's articulating.

Do you have your own counsel? Does Northeast have its own counsel?

We do we have our own counsel but we frankly work with them only in cases that there is an obvious conflict where the interests are so divergent that we need to get both sets

John Neilson
Key West, Florida
December 9, 2010

of attorneys involved. But they exist; we have the contacts and relationships that can be accomplished if it should arise.

The general counsel in our pool generally does not attend board meetings and that is unusual. Normally general counsel in the pools I've worked for has always been in attendance and has been party to everything that's going on. For the most part, general counsel with PERMA is brought in on an ad-hoc or case by case basis. There is a demarcation line as I suggested earlier the general counsel is prohibited under his contract from doing any defense work on behalf of the pool. [28:09]

He's prohibited to do defense work?

Correct. There is a panel and the claims department is the party that normally will involve other defense counsel in a litigated file and the board from time to time approves or updates their approval for who's on the attorney panel, otherwise the claims managers or his designees are free to select anyone from that panel. No further interference or involvement from the board.

I'd say I have interaction with them once a month, about. Something like that.

But I want to just kind of follow up on what we're talking about here. How much are you paying the defense panel? Is that part of the criteria?

John Neilson
Key West, Florida
December 9, 2010

They are required to provide rates so that they essentially are—to get on the defense panel they have to meet certain criteria—that they've been practicing law in ways that we think suggest that they're professional in our area of required knowledge.

That's the second part of this question, let's just expand on that. Experience and knowledge you look for in an attorney who will be working with the membership?

For defense counsel we want them to be solely defense counsel and not working both sides of the deal. There are a lot of firms that will go both ways, we don't engage those, we don't recommend them for approval on our attorney panel. We certainly look, in a state as diverse as New York, at their geography. We generally are not going to assign somebody from upstate to go down to New York and litigate. We're not going to send somebody from Manhattan up to Albany to work up there. Those are completely different environments and even if they're practicing the same type of law there's a great disadvantage to assigning the wrong attorney to a case. You certainly don't want some western New York, which is essentially an extension of the Midwest, some high-falutin' expensive high-powered attorney from Manhattan up to Auburn, New York to litigate—that's a mistake. You want to try and match up the geography, ideally they have had extensive experience in whatever jurisdiction you're going to litigate in. If I'm in Seneca County or if I'm in Albany County or Schenectady County there are certain attorneys that we want to try and have litigate in those circumstances. We're a mono-

John Neilson
Key West, Florida
December 9, 2010

line pool, so all we care about is comp, they need to have expertise in our field. Rates are important; we try to get a good value for the service they provide.

Now is that a challenge in the more urban districts?

Its more challenging in urban than rural, albeit in rural areas there's often a much more limited choice of who your alternatives are.

So what kind of money are we talking about, John?

It varies greatly. In some parts of New York State we're paying probably \$250/hour. Other parts of New York State its probably more like \$75 or \$80/hour. [35.34]

Another area, another criterion, would be you need to match up the skill-set of the attorney with the circumstances of the case. What I mean by that is there are some cases where you know very early on that there's no way this thing is going to be settled—its going to trial. You need a litigator on that file, its not optional. You can't choose your buddy who's really good at cutting deals because there isn't going to be a deal to cut. We're going to have to take this all the way through trial and probably to appeal after that so you want to get your best people litigating.

John Neilson
Key West, Florida
December 9, 2010

Right. We've got a pretty limited stable ourselves: there's the law enforcement guy, there's the personnel guy, the sort of general slip and fall, the business liability sort of guys. We've got a pretty limited stable really, we don't have a really deep bench.

Alaska's got a million people living in it?

600,000

Half a million people? New York's got like 20 million people. The law of large numbers suggests that we can be a little more judicious and more restrictive to protect the downside of a conflict a little easier than you can.

That's a two edged sword—there's probably more attorneys as a consequence—more suits.

Right. One other thing, coverage counsel. Another area that I have had quite a bit of experience in and my advice would be again not to have your general counsel get intermingled with coverage counsel. They ought to be separate, distinct parties.

Do you let coverage counsel do any defense?

John Neilson
Key West, Florida
December 9, 2010

No. You can be defense counsel, you can be general counsel or you can be coverage counsel. You can't intermix. Pick a side and defend that interest or offer to defend that interest. Generally you're not going to use a panel to be your general counsel, you're going to pick one person for that.

[At this point (38:13), the recorder dies. The following is recreated from notes of the conversation.]

15. How do personal relationships and political correctness affect your management style in running a pool? What advice would you give a new pool manager dealing with a personal relationship between himself and a board member? Between a pool manager and service providers? How do you handle relationships between board members, especially potentially explosive relationships?

John mentioned that he has seen instances where people have hired friends. When there are performance issues, this becomes very difficult. Consequently, he recommends nepotism policies, disclosure and transparency. At a minimum, the CEO must disclose potential conflicts of interest.

John Neilson
Key West, Florida
December 9, 2010

When it is a board member, again disclose. You might have to disqualify the board member. Generally, you want to be careful not to be accused of self-dealing; of providing disparate pricing, coverage, or pool resources to your buddies.

With respect to service providers, do not be put in a position of being accused of being in someone else's pocket. John's guideline is meals only—nothing over \$50.

As far as explosive relationships amongst board members, he can make suggestions, but the board themselves have to assume some ownership. CEO might alert the chair and suggest intervention. If you have a strong chair, you can generally work around dysfunctional board members.

**Peter Tritz, Administrator, League of Minnesota Cities
Insurance Trust**

December 10, 2010, Key West, Florida

Today is December the 10th, I'm with Pete Tritz. Pete what's your title?

The Administrator of the League of Minnesota Cities Insurance Trust

And how long have you been doing this?

Since 1980.

So that's 22 years? 23 years?

30 years.

30 years. And you've been with the pool the whole time?

Yes.

Pete Tritz
Key West, Florida
December 10, 2010

Were you with the pool prior to that?

The pool didn't exist prior to that.

Okay. And your years of pooling would be about 30?

That would be about 30. [chuckling]

Okay. And years in Risk Management?

Oh, you could probably add about 3 or 4 onto that I guess.

Okay. Call it 34. So the first question is, what are your goals for your pool in the next 5 years, and have your goals for the pool ever been in conflict with the board's direction?

Well in terms of my goals, really, I guess, three--three main goals I would like to get accomplished.

One is I want to get the staff structure changed around just a little bit more. Kind of in the midst of that right now, but to really get it put in place—a structure that will

Pete Tritz
Key West, Florida
December 10, 2010

essentially make the succession when I decide to leave go nice and smoothly hopefully. It really is a matter of changing around what have been the current kind of main division heads—claims manager, loss control manager—switching them from reporting to me to reporting to the associate director and then also shifting the underwriting manager position from being a contract position to a staff position and getting those things done. That way we'll have the pieces in place the transition will work. And that will also enable me to get away from, you know, much more of the day-to-day management and personnel supervision and really focus a little more on policy and strategy and those kinds of things. So that whole, kind of, get the staffing right is one of the goals.

A second goal that I really do want to get done and we're probably about half-way there is to get in place a simplified and better premium rating system for liability coverage. What we have right now is kind of a—well, its kind of a combination of a traditional ISO type of approach plus a sort of traditional E&O rating type of approach with a lot of modifications and tweaks and its complicated and requires a lot of data. It's a lot of work. It works okay in terms of allocating costs appropriately but the goal is to come up with something much simpler that will work just as well. And I think that can be done, it looks like we can do it with about 5 data elements and do just as good of a job of allocating risk. That will make life simpler for the cities; it'll also make life simpler for underwriting in terms of the amount of data and paper to be processed. And what I really see it allowing us to do is to shift—shift what the underwriting staff spends there time doing away from lots of detailed calculation and more toward, you know, real risk

Pete Tritz
Key West, Florida
December 10, 2010

evaluation—risk consulting, risk advice and so on. And of course it implies a kind of a shift in the kind of people we have in these positions, too.

Currently it's a TPA right?

Yeah, but its dedicated staff and they're housed with us.

So that's a second goal. And actually one of the interesting things that I hadn't thought about when we went into it, but, what we're doing there is really looking at the main categories of liability loss which are land use police employment, sewer backups, administrative errors and omissions, streets and sidewalks, and then kind of a catch all everything else. And for each of those risk areas, identifying an exposure measure that we can use validating that statistically. One of the things that it occurred to me or struck me as we were making progress on this was well we now have the basis for being able to do some valid benchmarking among cities. So we know that statistically numbers of police officers is a valid risk measure for police liability exposure. So what that tells us is then not only can we use that for rating, but it also makes it possible to do benchmarking among cities because we know that doing a comparison based on liability claims per officer or liability claim cost per officer is a statistically valid way to do that. So similarly with employment its FTEs for sewers it turns out to be numbers of connections and so on. So that's the second project.

Pete Tritz
Key West, Florida
December 10, 2010

A third kind of major goal is to really continue refining and maybe completing the kind of fund balance management model—kind of the stress testing model we’ve been developing. And there’s still some kind of loose ends on that. The model as it is designed right now kind of says here’s a minimum that’s reasonable to maintain but it doesn’t—we need to figure out how to quantify well just how far above that do we want to target. And I think that’s important just to get those things sort of a rationally-based policy in place as a way to respond for when the challenges come from regulators or legislators or members or any of the number of people who might think we have more money than we need. Maybe in fact we do.

So I think strategically those are some of the things. You know, a number of other goals—I think we want to continue strengthening the online training resources we are able to offer—the loss control training resources—we’ve got some decent stuff now on HR and land use but as cities’ budgets are getting tighter they can’t afford training, they can’t afford to even travel for training, so I think just continuing to build that resource is another main focus. [8:45]

I want to just segue right into the second question then which was new developments and future issues you expect to encounter. What are the emerging issues for pool management--you hinted at surplus grabs?

Pete Tritz
Key West, Florida
December 10, 2010

Well, I think that's certainly one of them. I think that's one we absolutely have to be prepared for. And I suppose you could think of that as almost a subset, perhaps, of just a whole galaxy of issues relating to financial crises and the financial crunch in the cities. I think that's one of them that's a pile of money sitting there that somebody might want to use to solve some other problems.

Another is I think to just sit back and think about different kinds of claims or risks that we might be exposed to. We talked a little earlier today about just the idea of if the city were in a bankruptcy—might we right now be vulnerable to being made part of the assets for the creditors through, you know, liability claims against individuals. I think that's a risk we have to think about and there are probably others as well.

Bill Heberton has mentioned the idea that the federal budget crunch and the rising cost of Medicare could very well lead to a push at the federal level to get rid of state tort caps and immunities and limits and so on because, in effect to the extent that a city's liability is limited or that they are immune, those are at least some claims that potentially fall back on the Medicare system. I think that's a pretty interesting insight. It's a dynamic that hadn't occurred to me but I think he's absolutely right and there's any number of those kind of potential risks out there that I think we just need to be really trying to identify and spot and think about and some of them might not be very obvious.

Pete Tritz
Key West, Florida
December 10, 2010

What about regulation?

I don't see that as a major concern. I haven't seen anything—we haven't seen anybody pushing for more regulation of us and I don't know that anyone has any real reason to—I mean that's one of the things you always kind of watch out for—is maybe somebody's set up to take that kind of run on us and decide to try and put regulation on us. I don't see any groups either that would seem like they have an incentive to do that or that are doing it but I think that's something we've gotta watch for.

But I think as with that whole issue of surplus amounts—I think we have to anticipate what those questions are and how we might answer them. If that challenge is raisable, how do we know these guys are solvent? Well okay, then we have to be prepared to provide all that information and we can certainly do that. And then, you know, the flip side is well maybe you got too much money. Well, we have to be prepared to respond to that kind of question. Or, you're not handling claims properly or you know, we have to be prepared to respond to those. So I think its really trying to anticipate what the questions might be and make sure that we're prepared to answer them.

So you've anticipated the question of maybe you have too much money and we want some? What have you done to position your pool to protect yourselves from a grab of your members assets?

Pete Tritz
Key West, Florida
December 10, 2010

Well, I think what we've done is to try to develop some methods that we can then embody into a policy or into a formal policy of the trust that says here's what we think is an appropriate amount of fund balance or surplus for the pool to be holding and here's why this is the appropriate amount.

And the way we're trying to get at what those appropriate amounts are are to imagine the different kinds of low probability but high cost catastrophes that might befall us. So whether its say just an unexpected way out of the line frequency of large losses so we have a retention accumulation problem. So we would look at, all-right, what would happen if we caught twenty in a year—what does that do to our fund balance situation? Or suppose we had the catastrophic storm loss—you know the tornado that blows through a number of cities--so we've got a hundred million dollars of loss scattered around and at the same time a major reinsurer tanks and is unable to meet their requirements. How much are we out? You know that works out in our case to be about 40 million dollars. So what happens if we take a 40 million dollar hit in that way?

On the investment side, our major risk is because of our investment policies really an interest rate risk so what happens if we were to see a twenty percent decline in the value of our investment portfolio? So its kind moving, working through a number of those kinds of contingencies and then essentially backing into a fund balance target by saying well—look at some of the basic bare-bones minimums—3 to 1 premium to

Pete Tritz
Key West, Florida
December 10, 2010

surplus, 4 to 1 reserve to surplus, how much money do we need to have so that we could withstand any one of those stressors and still have enough to meet those bare-bones minimum requirements? So it's a way to kind of come up with a rational way to come at a dollar amount for fund balance.

Another one of the stressors we look at is well what if we're wrong on our reserves? So we look at, well lets see, suppose our losses turn out to be twenty percent higher than what we have reserved. And what is the dollar cost there? So, you know, it's a matter of looking at these various stressors and looking at these various minimums and then just making sure we can handle any one of those stressors and still meet that whole series of numbers. So its really, and again its certainly not a guarantee but it's a way to say yeah there is a rational, reality-based policy behind the amounts we're holding.

I think that that sounds like about all you can do.

I think so.

As long as its written and you can point to it and say no there's a reason that we're holding that kind of money. Now if you do that and you find yourself still with surplus, I expect that you may be thinking about ways to deliver that back to the members.

Pete Tritz
Key West, Florida
December 10, 2010

Absolutely, absolutely. And we actually use that as a guide—I mean just because of the way we do our rating on the property casualty side its very typical that we have some funds available to return and so we regularly do that. And we do use this policy as a guide for amounts to return. Now we also have a—we haven't typically had a lot of extra money in work comp but our stress test is suggesting maybe we do have more than we need right now.

Well Bill is suggesting maybe you don't have enough.

Yeah, well I think that's—those are the questions. [20:12]

When you're returning that in the rating process are you returning it in the rate or do you identify it as credit or how are you doing that?

No, we actually return it as a check.

So a dividend.

It's a dividend. It is actually a dividend.

And you do dividends every year?

Pete Tritz
Key West, Florida
December 10, 2010

In the property/casualty program we have. It's an individual decision every year. The amounts can vary quite widely.

Its going to vary, sure.

And that's why we build that margin into the rates. The idea that here's projected loss and here's what it costs to cover expense—rates plus investment income comes out here. That gives us a question if the losses are more than expected, if losses are at or below projection then that money is available either to increase surplus if we need to or just return it to the members as unneeded funds. I mean that's kind of the model we worked on for quite a while. [23:22]

How about a reputational risk? Again, it's an emerging issue for current managers. What policy and procedures are in place to protect your pool from this type of risk?

You know I was looking at that question I was trying to think of how—what policies and procedures. I don't know how to answer that other than to say we are probably a whole lot more transparent than the way some pools operate. I mean its pretty wide open and everything we do available for anybody that wants to look at it. We also, I think, are pretty careful on all of the major decisions we make to build those records and document what are the reasons for it, what was the thinking, how does this all fit

Pete Tritz
Key West, Florida
December 10, 2010

together so those questions are always there. The other piece of it—I don't know how to say this other than to say—"Try not to be stupid."

Anyway, I think those kinds of things, you know you think about the Kentucky situation and some of the stuff that just became standard practice there—I mean, what were they thinking?

I think it creeps up on you, it must creep up on you.

I think that's it.

It didn't shock the conscience the first time they went to this restaurant. And then it's a little bit more and a little bit more. And once you look at it at the end of the day you say, "What were they thinking?"

I think that's it. That sounds like pretty much the way it developed.

You can't really codify moral behavior— but I think that you could put policies and procedures in place that relate to conflicts of interest, the taking of gifts, how much you're willing to accept in the way of a meal and things like that.

Pete Tritz
Key West, Florida
December 10, 2010

Those kind of things, of course in Minnesota its already a state law on a lot of that stuff. You know having, like you say nepotism policies in place, its all good stuff to have but...

But its pretty tough to legislate morality.

Yeah, at the end of the day, I'd say maybe it's easy to legislate it for people who are lower down in the supervisory hierarchy. It's hard to do for people in top management positions—its hard to legislate it. I think you ultimately have to end up relying on those individuals' judgment and good faith. Because any policy, if you're looking for a way around it, there's a way around it. It just kind of comes back to the kind of people that you hire and the kind of people you look for.

That, and I'd suggest the tone at the top as well.

Yeah, I think so. I think of codes of ethics and I think what it kind of boils down to is well, if you really have to be told that stuff, its probably not going to do any good to tell you that stuff. You know what I mean? [28:44]

A different question—kind of in a totally different direction. How much interaction do you have with the pool's general counsel and or your attorney panel, your defense panel, can you just tell me a little bit about what you're

Pete Tritz
Key West, Florida
December 10, 2010

looking for when you hire somebody like an attorney and what the level of involvement is?

Sure. I guess I'd like to answer those questions separately because the general counsel and defense counsel are kind of two different bags. General counsel the interaction is almost daily because Tom Grundhoefer, who is also the league general counsel, serves as trust general counsel and its just kind of a walk down the stairs so any of the the issues that involve legal considerations and lots of issues that don't involve legal consideration, so, I pop my head in his door and we talk about it. Because he's not only a very good legal mind but he's also just a very good general mind. I think that's a nearly ideal kind of working relationship there. The general counsel's input is just an on-going daily part of life. Its just one of the resources that is there and one of the people we interact with. What you need there is obviously very solid knowledge of municipal law and law relating to governing the pool and also the right kind of person—somebody that you can work with effectively. It also, of course, has to be somebody that the board members would have trust and confidence in. Its one of those issues, for us its kind of easy, because Tom and I worked together for close to 25 years now. We know each other's strengths and weaknesses well.

On defense counsel its a little bit different. Primarily, our claims people who handle that. We do have a an in-house position. Litigation manager is essentially what the job title is but its an attorney who's experienced in litigation who's job is really to oversee

Pete Tritz
Key West, Florida
December 10, 2010

litigation activity by any of the various firms that we use. In selecting who those firms, obviously you look for expertise in particular kinds of areas so there is a couple of firms — really three firms that we would tend to use for any land-use litigation. There's really two firms that would handle the bulk of the police liability litigation. Employment litigation tends to be handled about half by in house counsel and half by one particular outside firm and so on. Expertise is one thing.

I would say a problem-solving attitude is another. They have to be willing to kind of work with us and participate in those conversations about litigation strategy and so on. If they are a firm who's approach is well if you assign it to us we're in charge and we'll let you know when its done—well that's not going to work. We've sort of evolved that stable of attorneys over time. There are changes—people are added and people are occasionally dropped but it tends to be a pretty stable group that we use.

Another almost sure way for a defense counsel to fall off the list is to do the thing of—“we've gotta great case, we've gotta great case, we're going to win this, we've gotta great case, oh my God trial's tomorrow we gotta get this thing settled.” You only get to do that once. So that kind of willingness to work with us early on and continually updated realistic evaluations of what is our case here? What are our chances? What is our exposure? What are our problems if we were to take this to trial? Those are the kinds of things considered.

Pete Tritz
Key West, Florida
December 10, 2010

Does cost come into it?

Cost comes into it when we're making the decisions of who are we going to assign to this particular file. There are cases that we have where we know who we want on this because that's what they're good at and that's what we're going to pay them to do. There are other cases though where we might be very specific—we might handle it in-house—we might say this is one we'd like to have assigned to a junior person in the firm. So its kind of an evaluation of what you need on the individual case. What level of expertise and skill.

It sounds to me like between Gronli and your litigation manager your involvement is somewhat limited to the fires.

Yeah, and there rarely are any fires. My involvement tends to be more kind of a matter of sometimes its one or the other might want to just bounce ideas off, here's how we're thinking about playing this one what do you think? And its more just kind of almost round tabling it a little bit, getting more points of view. Its an area frankly, in terms of day to day claims oversight and management, I don't have to think about it very much because that's an area where I'm very comfortable with the staff that we've got in place.

So do you have more authority than Doug for example? Have you delegated all your settlement authority to Doug? Or does the board even have any authority?

Pete Tritz
Key West, Florida
December 10, 2010

Nothing has to go to the board.

So its entirely staff?

Its entirely staff. The formal, Doug has put in place some kind of policies on what levels, you know settlement authority for the adjuster, for the claims supervisor, and those kinds of ways. None of that has to come to me.

So the buck stops at his desk?

Yeah. But it is also, like many other kinds of things, if Doug is looking at something and scratching his head and trying to decide what to do he'll come in and we'll talk. Its not so much that he needs to come to me for the authority but its more just... he might come in and say here's kind of what I'm thinking anything I'm missing here that I should be thinking about? So it's not a matter of formal authority it's more a matter of, and again it's from having worked together for a long time, kind of respect for what I can bring to help him and vice versa. It's not an authority kind of thing, more just kind of a part of the resources I suppose. [38:30]

So how about the membership? I mean are you looking for anything in particular with respect to how they interact with your membership?

Pete Tritz
Key West, Florida
December 10, 2010

You know, the tricky thing about the attorney's now. A lot of that is really built into some of the standards that we have in place but it's—we beat on them about communication a lot. Just because it is such a—to make sure that the city folks know what's going on. And that's, you kind of have to sometimes even, well not sometimes, you have to customize that stuff to. Because some of them want to know everything that's going on. Some of them don't want to be bothered with any of that kind of stuff. You kind of work with what you have. And again the defense counsel has to be willing to do that.

Very often when there's say a meeting with a city council and so on, there will be somebody from our staff there as well—whether it's the litigation manager or it could be any of several people. But somebody there for those reasons. And trying to stress—you can never control it absolutely—but you can try to stress to those folks that this is a privileged conversation. This data is therefore confidential under state law. It would be a criminal violation for you to release this data don't you know? Mostly it works, its not a hundred percent. But, that kind of thing can happen. [41:20]

All-right, final question Pete, and then we can wrap it up. How do personal relationships and political correctness affect your management style in running the pool?

Hmm. Personal relationships.

Pete Tritz
Key West, Florida
December 10, 2010

That's not very well written. Does that mean like intimate relationships or does that mean my buddy, I hired my buddy?

I think, I don't know what political correct means, I'm not even going to try to answer that part. I think there is a danger, especially when you're in a situation like we have where you've been working with people for a long time and you really have become personal friends. I think there is that danger that you kind of overlook things you maybe shouldn't overlook. I don't know what you do about that other than try to be aware of that risk and remind yourself to second guess your own judgments. Its very difficult when its somebody that you've known a long time and would think of as a personal friend to an extent. It is very difficult to have to call them on the carpet. Sometimes you've got to do it and its not fun and its not pleasant and afterwards you don't feel good about it. I think its—I don't know what else you can do other than to just be aware of that risk and remind yourself of the need to be especially careful second guessing yourself.

Well let's say a 25 year employee, always been a top performer, runs into some kind of a problem—whether it be a DUI or some other issue—do you treat them differently than you would treat somebody new? Is there room for treating people disparately depending on the relationship that they have and their performance and history with the program?

Pete Tritz
Key West, Florida
December 10, 2010

I don't know that I'd put it exactly that way I think the behavior expectations have to be the same for everyone. I think perhaps the remedy that you apply is affected or tempered somewhat by what the person's history is. There's a difference between the person that's been there 5 years and every 6 months there's a little kind of questionable thing versus the person who's been there 15 years and has never had an issue except this one kind of stupid thing. That enters into it and I think it kind of goes back to that point—I think in those situations you do have to just be very careful to question your own decision making. Say am I doing this right? Am I making excuses for an old friend? It's very hard to do. It's hard to force yourself to do it and it's hard to make sure that you are doing it. Being aware of one's own prejudices is I think one of the hardest things that there is.

Right, that's well put. What advice would you give a new pool manager dealing with a personal relationship between himself and a board member?

You know if there were a personal relationship between the new pool manager and a board member I would have a real question of how that person became the new pool manager. I don't know how that happens—a board hiring someone with whom a board member has a personal relationship. I don't know what personal relationship means here but in that context it kind of sounds like we're talking about you know a romantic, intimate...

Pete Tritz
Key West, Florida
December 10, 2010

You know, I don't know. Because I've asked this question 5 times, I've thought about what kind of personal relationships do I have with my service providers, with the staff, with the board? I feel that I have a pretty good relationship with everybody on the board and have some sort of personal connection with each one of them. Did I have that connection prior to having this job? Sometimes. On the other hand, do I have any other sort of outside relationship with them—pretty much not.

How about relationships between service providers on yourself? Do you have any rules on that or thoughts on that? [53:25]

Well I think much the same kind of thing. I think its, as you know, some long standing relationships with the Berkley folks, also with some reinsurers like the Genesis folks. And I think you have to always be sort of aware of that—I mean yeah they're people I've known a long time and like and respect but is that unreasonably coloring any of my decision making? I don't know what you do other than just try to remind yourself to be aware of that. You know, those relationships of kind of knowing and trusting each other I think often work in our favor.

You'd like to think so wouldn't you?

Pete Tritz
Key West, Florida
December 10, 2010

I think about the way the folks with GenRe were willing to step up when we were trying to put together a pretty unique coverage solution to deal with some of the things connected with the Republican National Convention that was at St. Paul—a complicated thing but basically because we had a good solid working relationship they were willing to say, “Yeah we trust what you’re doing.” So I mean it’s partly a personal and partly a business relationship but part of the business relationship is them kind of knowing how we work, how we think, how we make decisions.

It’s a very personal business I think. It’s about personal relationships whether it’s between you and your member or you and your service provider or you and your board. I think it all has to be relative you can’t take the personal part of it out—if you’re just a robot it’s not going to be very effective.

I think that’s a good way to put it. The flip side that comes with that is you just sort of have to be aware of...

How’s it look?

Well how’s it look and the natural human tendency to cut a little extra slack for the people that you’ve known for a long time.

Pete Tritz
Key West, Florida
December 10, 2010

Have you had any relationships between board members that were potentially explosive?

That we've never had.

People in Minnesota are so nice.

Either that or they're just really, really discreet and sneaky. No I mean we've had situations where you could kind of see board member A and board member B maybe getting on each others' nerves. Nothing that's ever come close to being an issue.

In 30 years of doing this have you ever seen a minority and a majority on your board that spans more than a single issue?

No. Not on the Trust board no, never had that. The ethos has always been very much let's talk this through and find a consensus. It's not unheard of but it doesn't happen very often that there's a divided vote. There are sometimes different sides will be argued pretty strongly but usually they'll get to agreement and usually it ends up being unanimous votes. Sometimes, I mean you know one of our board members, he's very definite on what he thinks about whether we in fact need to have two different investment managers, he thinks we'd be better off to lump it together. I disagree with

Pete Tritz
Key West, Florida
December 10, 2010

him and we argue about that once a year at investment review time, put it to the board and the board votes 6 to 1. It's not in any way out of line or inappropriate.

He's doing what he feels his job is.

Well and it is his job and it is absolutely an appropriate issue and question for the board to talk about, think about and decide. So no there's nothing at all inappropriate about it. But it is unusual for there to be divisions that end up being an actual divided vote.

Well that's really all I have. Thank-you for your time. Thank-you for your mentorship I do call you periodically.

You know there was a question on there that I don't think we talked about and that is the situation where my view might differ from the board's view of long-term direction?

Yeah there was it was at the beginning—have your goals for the pool been in conflict with the board's direction? [1:00]

You know, not very often and not in a way that's ever been a problem. I think really my job is to put together recommendations that take into account as much as I can everything that they need to be thinking about—identifying what are the factors to consider, give them my advice on how I would put them, weigh them and balance them

Pete Tritz
Key West, Florida
December 10, 2010

and so on. Not to say that they always agree. I think it is also true that its sort of incumbent on them to also take into account all that information and analysis and then form their own decisions. We've been very fortunate I think just in our board members. They tend to do that. And when they disagree with the staff recommendations I can say it's been for very valid reasons. Their judgment of how this weighs against that is different than mine.

But it's their organization.

At the end of the day I wouldn't say that the board and I always agree but we always have gotten to a point where we can move on and move forward and do it in a way that reflects what we should do. I've never had one where that's really been a serious problem but not to say it can't come up.

Right. Well thanks again, Pete and good luck getting home.