



February 11, 2021

To: GL2 Program Members

From: Gina Dean, CEO

Re: GL2 – Stakeholder Communications

As most of you are aware, the liability insurance industry is in a hard market cycle, which initially impacted California public entities, but is now affecting public entities across the country. As PRISM members begin their budgeting process, I want to take this opportunity to provide some background information on the state of the market and the status of the GL2 Program. Also attached are talking points and an information sheet that we hope you will find useful in communicating to your stakeholders

Background

The liability insurance industry continues to see significant increases in plaintiff demands, jury verdicts and high dollar claims – a continuation of what we have seen for the last several years. Claims that used to resolve for \$5M-\$10M are now costing public entities and their insurers \$20M-\$30M+. The so called Social Inflation that has had a huge impact on these costs continue to deplete the liability market's surplus, limiting the capacity and availability of reinsurers willing to write California public entity business. To illustrate this point, in 2015, PRISM considered 17 reinsurers for renewal of the liability programs, that combined had \$170M in capacity to offer. Looking ahead to the 2021/22 renewal, seven of those reinsurers no longer write public entity business in California, reducing the available capacity in the market to about 1/3rd of what it was in 2015. Those that are willing to continue their participation are increasingly judicious as to where they place coverage.

More and more we are seeing coverage modifications either in the form of sub-limits, aggregated coverage layers, certain coverages being provided on a claims-made basis, and/or exclusions or significant limitations on coverage. At the same time and for the same reasons, self-insured and pooled programs across the state are seeing a depletion in funding. This trend is affecting all public entities: counties, cities, schools, and special districts.

Although the COVID-19 pandemic has had more of an impact on workers' compensation than general liability, it has impacted the insurance markets overall. Concerns regarding potential exposure to loss, that may have been less concerning until recently, will likely yield coverage restrictions, new exclusions, and/or reduction in limits.



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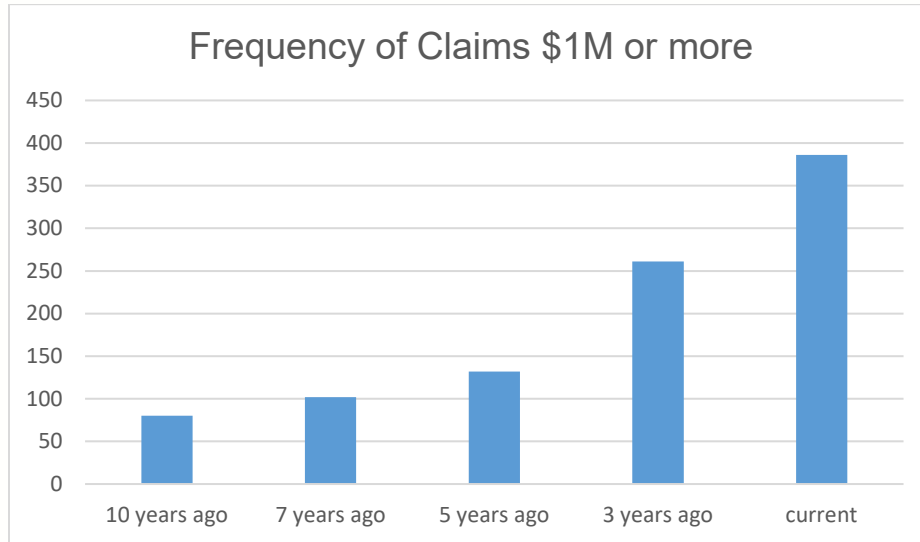
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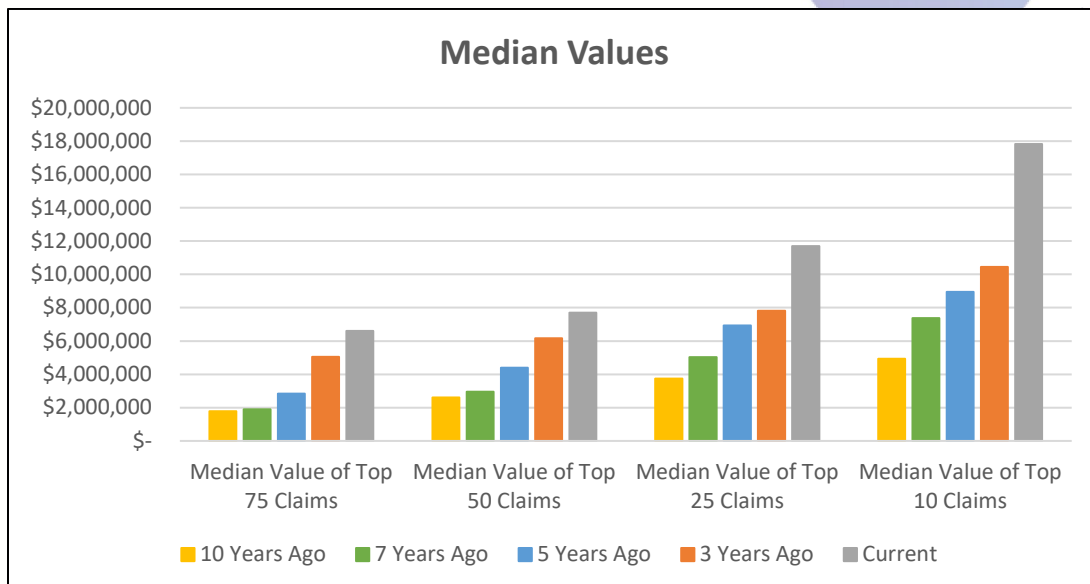
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As these issues affect the insurance industry, they also affect PRISM. We are experiencing an issue of both frequency and severity of claims. For example, the following graph depicts the frequency of claims valued over \$1M incurred by the GL2 Program over the last 10 years. The graph highlights the fact that until five years ago, the frequency of claims is what you would expect as a “normal” trend especially considering the Program’s growth during that time; however, the significant increase in frequency of high-value claims from then until now, was certainly unforeseen by the industry.



In addition to the increase in claims frequency, the following graph highlights the increase in the median value of claims in the Program over the last 10 years. Again, the graph highlights the “normal” inflation of claims from 10 years ago, which changed significantly starting three years ago.



One final graph, this one a depiction of social inflation of claims, is from an Advisen study on the Median Cost of a Single-Fatality claim. The graph highlights the increasing cost of a death claim; however, does not even contemplate a life care plan expense that can be one of the most expensive components of a serious injury claim.

Exhibit 1:



Safety in Numbers

Thankfully, for members of the GL2 Program, our size creates stability and offers economies of scale that could not be realized without being in a pool. We are able to leverage the volume we bring to the reinsurance markets to benefit all Program members, and in fact, new member applications to the GL2 Program have increased. That being said, the Program will likely see moderate rate increases in the coming year, with individual member's changes varying based on their own loss experience. It is because of our core values and because we are member driven, that we set premiums that are equitable for all members, based on an allocation that takes into consideration several factors including a member's size, SIR level, increases in exposure, and each individual member's claims experience.

PRISM's Response

PRISM has always been proactive in managing the GL2 Program with our market allocation approach to help manage the members' costs. Over the last several years, the Program has been loss challenged, forcing some members to take on individual corridor deductibles and/or increased self-insured retentions to manage the increase in premiums. As a group, we have also been able to retain more risk by growing the group corridor deductible, thus providing stability to the Program. This year will be no different as the liability market continues to harden. Planning for the future, the GL2 Committee held a

strategic planning session in 2018. Since that time, the Program has implemented all of the following: 1. Created a member scorecard to help members assess how they manage claims and their data, ensuring that every member is reporting their claims (loss data) on a monthly basis; 2. Created a Claims Review Committee 2 to assist members in managing high dollar claims; and 3. Revisited the Claims Handling Standard in Addendum B, and educating members on those Standards and best practices. This hard work by the Committee has improved the members' collective risk profile, and has certainly been noticed and appreciated by the Program's reinsurance partners.

The Big Picture

If we have learned from history, we know that joint powers authorities (pooling) have been the answer to turbulent markets. By staying the course, we will all benefit from our economies of scale, our leverage in the reinsurance markets, and our sharing of best practices to help manage risk and hard markets.

While the GL2 Program's premiums will increase for 2021/22, the premiums are still less costly than an entity would likely be faced with outside of PRISM. Recent membership applications have led to growth of the Program and has also allowed us to test the competitiveness of the Program. The three new members that joined GL2 in 2020 saved between 25%-75% on their premiums, dependent upon the stand-alone market or the JPA that they came from. In addition to premium savings, those entities also avoided coverage restrictions and limitations that were quoted outside of PRISM.

Member's Response

There are several steps that can be taken during these turbulent times.

1. First, communicate the state of the market to all of your stakeholders so there is an understanding that this is an industry-wide problem. We are happy to participate on conference calls or attend meetings to assist with this communication, if so desired
2. The severity of claims is on the rise. If you are not yet participating in the Optional Excess Liability (OEL) Program, consider doing so.
3. Anticipate an increase in your own SIR funding being suggested by your actuary.
4. It may be tempting to consider increasing your SIR to save premium dollars; however, this needs to be weighed against the increased cost to fund the higher SIR. In addition, given these new severity trends, all things being equal, the bias should be toward transferring risk due to the uncertainty of these changing claim trends.
5. Defend claims that are defensible.
6. In a hard market environment, the quality of loss data will undergo additional scrutiny. Make sure your data is in good condition.
7. Finally, manage your individual risk by taking advantage of the best practices programs and service partner programs we offer.

Talking points for the GL2 Program

Individual Claim Examples

To describe the effects of social inflation on claims, below are several summaries of recent jury verdicts and settlements, many of which involve members of PRISM's GL2 and GL1 Programs:

- Jurors awarded \$45.4M against a southern California county to a girl who suffered sexual abuse for two years in a home where she was left despite evidence showing that an accused molester lived in the house.
- A southern California city was sued for dangerous condition of public property after a 16-year-old was struck by a car crossing a street at a crosswalk near his school. The driver of the vehicle was looking for an item that was on the floor of the passenger seat when he struck the teenager. The teen survived, but has multiple injuries including a brain injury. A jury found there to be a dangerous condition and awarded over \$23M against the City.
- A northern California county was sued after a family's vehicle was struck in an intersection late at night by a law enforcement vehicle that was responding to a call without lights and sirens on. Several members of the family were injured, and one young child was left with permanent brain damage. The case was settled for approximately \$27M.
- A southern California city agreed to pay \$12.5M to resolve a case in which a driver struck and killed a baby and injured the father of the child. The City was sued for dangerous condition of public property as the driver claimed his view was obstructed by foliage.
- A northern California city paid \$12M to settle a case in which a motorcyclist was struck in an intersection by a police car that was responding to a call. The injured motorcyclist lost a leg in the accident.
- A northern California county was sued for wrongful death after the decedent allegedly lunged at officers with a retractable knife and was then shot and killed by the officers. The county agreed to resolve the case for \$7M.
- Jurors awarded \$3.8M to a 72-year-old woman who was allegedly pushed by a city councilwoman. The plaintiff tumbled over a stack of chairs and suffered bruises and a torn rotator cuff.

Aggregate Claims Trends

- As both frequency and severity have risen for the GL2 Program, just like the general liability industry, the claims trend and lack of capacity will result in anticipated rate increases.
- The natural result of this significant change in losses is that PRISM has adjusted forecasts and rates to account for new loss trends, as have our carriers.

- The total number of claims in the GL2 Program over \$1M in the last five years has more than doubled. This is a big indication of how jury verdicts (and settlements) are increasing!

Benefits of Being in a Pool

Economies of scale benefits

- Access to insurance options. PRISM's size provides more leverage in the insurance market. PRISM has been able to secure unique reinsurance agreements largely due to the Program's premium volume.
- Maintaining broad coverage. Public agencies with stand-alone placements are seeing reductions in their coverage limits and/or exclusions. Although GL2 continues to face the potential for coverage restrictions, PRISM has largely been able to maintain broad coverage in the Program.

Equitability

- PRISM's members with large loss experience have better coverage and premium options in the pool than finding coverage alone, but members with less severe loss experience also receive benefits from pooling as they are recognized and rewarded through premium reductions.

General Market and Program Information

- The GL2 Program remains fully funded and is in a surplus position.
- The size of our Program, 21 members and nearly \$10B in payroll, offers great purchasing power to our members and provides much greater stability than smaller programs or individual risks.
- The liability market continues to harden. We continue to see a significant increase in plaintiff demands and high dollar liability claims. Jury verdicts (and settlements) are much higher than they have been in years past and that is affecting the industry's surplus.
- There are many factors causing this including tactics plaintiff's counsel are using (such as the use of the Reptile Theory) to drive up claims verdicts and settlements. The selection of appropriate defense counsel, who are experienced in dealing with these tactics, has never been more important.
- Markets continue to be more judicious with how and where they deploy their capacity and/or limit their exposure. The size, stability, and premium volume of the GL2 Program have attracted markets that may not consider participation otherwise.
- We have always been proactive in our management and funding approach, and this remains the same today. One of the strengths of the GL2 Program is the active involvement of the GL2 Committee and their ability to be flexible. This approach often means modifying the Program structure and the Program's retained risk to keep premiums as low as possible for the members.

- The Committee held a Strategic Planning Session in 2018, which led to reaching the following goals and objectives:
 - creating a member scorecard to help members assess how they manage claims and their data,
 - ensuring members are electronically submitting loss data on a monthly basis,
 - creating a Claims Review Committee 2 to assist members in managing high dollar claims,
 - revisiting the Claims Handling Standard in Addendum B, and
 - educating members on those Standards and best practices.
- Implementation of this strategic plan has already impacted the Program in a positive way based on reinsurers' response on the 2021/22 renewal.
- We are not unique in experiencing rate increases for liability coverage as the claims environment in California and across the nation is increasingly adverse for public entities.
- Our membership increased last year and three new members joined the Program in the 2020/21 year. This shows that the Program is still competitive in the market.
- The benefits of pooling shine brightest during a hard market when our economies of scale, our leverage in the reinsurance markets and our sharing of best practices help our members manage risk.



GENERAL LIABILITY 2 MARKET OVERVIEW: Hard Times

The liability insurance industry continues to see significant increases in plaintiff demands, jury verdicts and high dollar claims – a continuation of what we have seen for the last several years. Claims that used to resolve for \$5M-\$10M are now costing public entities and their insurers \$20M-\$30M+. The so-called Social Inflation that has had a huge impact on these costs continue to deplete the liability market’s surplus, limiting the capacity and availability of reinsurers willing to write California public entity business.

- Claims trends have affected PRISM, just as they have affected the industry.
- We continue to see a significant increase in Plaintiff demands and high dollar liability claims, driven higher by tactics Plaintiff’s counsel are using (such as the use of the Reptile Theory), and affecting the industry’s surplus.
- Markets continue to be more judicious with how/where they deploy their capacity and/or limit their exposure.
- The active involvement of the GL2 Committee and their flexibility in modifying the Program structure and the Program’s retained risk to keep premiums as low as possible for the members is a great strength
- The Program is still competitive in the market, with 6 new members having applied for membership in the 2019/2020 year & 3-4 more thus far for 2020/21.



Individual Claim Examples

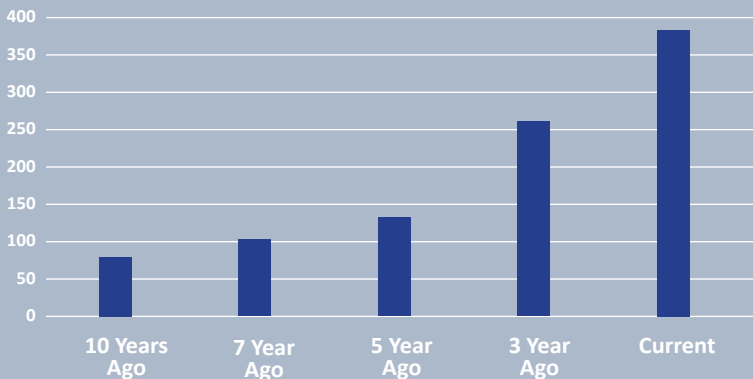
Northern California Settlements

- Law enforcement wrongful death claim: \$7M
- Motorcycle claim: \$12M
- Law enforcement vehicle involved claim: \$27M

Southern California Settlements

- Dangerous conditions claims:
 - ◊ obstruction by foliage: \$12.5M
 - ◊ near school: \$23M

Frequency of Claims Values (\$1M or more)



Median Claims Values (in millions)



Benefits of Being in a Pool

Economies of Scale

PRISM’s size provides more leverage in the insurance market, allowing us to secure unique reinsurance agreements.



Public agencies with stand-alone placements are seeing reductions in their coverage limits and/or exclusions. PRISM has largely been able to maintain broad coverage in the Program.

Equitability

PRISM’s members with large loss experience have better coverage and premium options in the pool than finding coverage alone.



Members with less severe loss experience are recognized and rewarded through premium reductions.

The benefits of pooling shine brightest during a hard market when our economies of scale, our leverage in the reinsurance markets, and our sharing of best practices help manage risk.

