PUBLIC RISK INNOVATION, SOLUTIONS, AND MANAGEMENT (PRISM)

General Liability 1 Program
Target Funding Guidelines

1. **PURPOSE**. The purpose of these guidelines is to give guidance to the Board of Directors in making annual funding decisions for the General Liability 1 Program. By adoption of these guidelines, the Board of Directors acknowledges that the long-term financial strength of the General Liability 1 Program is of utmost importance. There is a high degree of uncertainty in actuarial estimates due to the possibility of occasional catastrophic claims and inconsistent or inaccurate case reserving; therefore, the Board of Directors desires to fund the Program in a cautious and prudent manner and return dividends to its members in an equally cautious and prudent manner.

2. **TARGET FUNDING.** PRISM has determined that the target funding goal for the General Liability 1 Program is the actuarially determined 80% confidence level, discounted for investment income, and the result of the following ratios:

   Gross Premium to Equity ratio: Target <1.5:1
   This ratio is a measure of how equity is leveraged against possible pricing inaccuracies. A low ratio is desirable.

   Equity to Pool Retention ratio: Target >10:1
   This ratio is a measure of the maximum amount that equity could decline due to a singe loss. A high ratio is desirable.

   Outstanding Ultimate Reserves to Equity ratio: Target <5:1
   This ratio is a measure of how equity is leveraged against actuarial estimates. A low ratio is desirable.

   - Equity is the amount of cash equivalent available to pay claims in excess of actuarial expected losses discounted for investment income.
   - Gross Premium includes pool premium and reinsurance/excess insurance premium but does not include administrative costs.
   - Pool Retention is the maximum amount of exposure to a single loss retained by the pool over the most recent 5 years. The maximum exposure is based upon a 5-year weighted average consisting of 30%/25%/20%/15%/10% with the most weight (30%) placed on the most recent year and the least weight (10%) placed on the oldest year.
   - Outstanding Ultimate Reserves are the actuarially expected outstanding losses, discounted for investment income, in the pool layer as determined by a qualified actuary.

The ratios shall establish a range that will be considered the target funding range, however, such range shall be subject to a minimum of 80% confidence level.

3. **ANNUAL ACTUARIAL STUDY.** PRISM will conduct an annual actuarial analysis to assist the Board of Directors in making funding decisions on a prospective and retrospective basis.

4. **APPLICATION OF TARGET FUNDING CRITERIA**. After annual review of the overall confidence level and target funding ratios, the Board of Directors will be able to determine whether it is desirable to increase, decrease, or stabilize equity. The Board may take action in one or more of the following ways, although there are many factors for the Board to consider when making its annual funding decisions and other options may also be available. Most of the payout of excess liability claims takes place between 3 – 5 years, so adjustments in funding levels can be corrected over a corresponding period of time. Therefore, over the long term, a reasonably conservative approach is to target the middle of the range.

If Projected Equity is Below the Expected Confidence Level – the Board will adopt a funding plan to increase funding above the expected confidence level within the next year:

- Declare an assessment;
- Increase the rates for the next year;
- A combination of declaring an assessment and raising rates.

Utilize reinsurance to transfer retained risk or outstanding liabilities

If Projected Equity is Below the Target Range – Increase Equity to Get Within Target Range in 3 to 5 Years:

- Approve premium charges to the members at a higher level than the actual insurance costs; and/or
- Fund retained risk at a higher confidence level than the confidence level of the outstanding portfolio of losses.

Utilize reinsurance to transfer retained risk or outstanding liabilities

If Projected Equity is Within the Target Range – Determination to Maintain Equity:

- Approve premium charges to the members based on the actual insurance costs; and/or
- Fund retained risk at a confidence level consistent with maintaining equity.

If Projected Equity is Above the Target Range – Decrease Equity to Get Within Target Range in 5 to 7 Years:

- Approve premium charges to the members less than actual insurance costs;
- Fund retained risk at a confidence level less than the confidence level on the outstanding portfolio of losses; and/or
- Declare a retrospective dividend.

5. **RETROSPECTIVE DIVIDENDS.** The Board of Directors, using the target funding ratios as a guide, may declare a retrospective dividend at any time.

6. **PROSPECTIVE DIVIDEND.** To the extent the Board approves funding a new year at a confidence level less than the target 80%, the Board recognizes the difference between actual funding and the 80% confidence level as a prospective (up front) dividend.

7. **AMENDMENT.** This policy statement, amended by the Board of Directors March 1, 2019, shall be reviewed annually and reaffirmed or modified accordingly.