

**STATE RISK MANAGER'S REPORT**  
**REVIEW OF REGULATORY COMPLIANCE**  
**OF**  
**WASHINGTON RURAL COUNTIES INSURANCE PROGRAM**

*As of August 31, 2011 Issued April 22, 2013*

**Results:**

Based on audited financial information, Washington Rural Counties Insurance Program meets standards adopted by the State Risk Manager in most areas tested. One recommendation was made as a result of this review.

**Background:**

The State Risk Manager in the Office of Risk Management, a division of the Department of Enterprise Services, State of Washington, is responsible for regulatory oversight of local government joint self-insured risk pools formed under the authority of chapter 48.62 RCW. The law requires the State Risk Manager to adopt rules for risk pools to follow, adopted as Washington Administrative Code (WAC) 200-100. Those rules include standards for solvency, operations and management and require that risk pools maintain certain financial reserves in order to ensure that claims are funded.

The State Risk Manager determines whether risk pools are operating in a safe financial condition, according to the solvency regulations. The pool's compliance with those regulatory requirements is based on audited financial information provided by the Washington State Auditor's office. Pools that operate in an unsafe financial condition or in violation of statutory or regulatory requirements may cause the State Risk Manager to take administrative action.

**Areas Covered:**

We examined the Pool's compliance with regulatory standards adopted in rule by the State Risk Manager in the following areas:

1. Requirement for Annual Actuarial Study to Determine Unpaid Claims Liability
2. Financial Solvency/Required Assets
3. Presentation of Liabilities
4. Compliance with Reporting Requirements
5. Compliance with Membership Requirements
6. Financial Trends

## **Results of Review of Regulatory Compliance:**

### 1. Requirement for Annual Actuarial Study to Determine Unpaid Claims Liability

**Requirement: Risk pools must obtain an annual actuarial review which meets the following criteria:**

WAC 200-100-03001 requires that "(1) All joint self-insurance programs shall obtain an annual actuarial review as of fiscal year end which provides estimates of the unpaid claims measured at the expected and the seventy percent confidence level. . ."

WAC 200-100-020 (1) "Actuary" means any person who is a fellow of the Casualty Actuarial Society and a member of the American Academy of Actuaries.

**Result: A review of the actuarial report of Richard Fallquist, FCAS, MAAA, indicates that an actuary meeting the qualifications set forth above estimated the Pool's liability for outstanding unpaid claims at the expected level. The actuarial report for year ending August 31, 2011 did not contain a final estimate for unpaid claims at the 70% confidence level. One recommendation (see #3) was made.**

### 2. Financial Solvency/Required Assets

**Requirement 2.a: Risk pools must ensure claims liabilities are funded at the expected level by meeting certain standards for solvency and liquidity as follows:**

WAC 200-100-03001 states, in part ". . .(2) The governing body of the joint self-insurance program shall establish and maintain primary assets in an amount at least equal to the unpaid claims estimate at the expected level as determined by the program's actuary as of fiscal year end. . ."

WAC 200-100-020 (20) "Primary assets" means cash and investments (less any nonclaims liabilities).

**Results: Washington Rural Counties Insurance Program met this requirement by maintaining sufficient primary assets to fund claims liabilities at the expected levels as determined by the Pool's actuary.**

**Requirement 2.b: Risk pools must meet the above requirement to maintain primary assets and must also maintain other assets to fund claims liabilities at the 70% confidence level as follows:**

WAC 200-100-03001 states, in part, ". . . (3) The governing body of the joint self-insurance program shall establish and maintain total primary and secondary assets in an amount equal to or greater than the unpaid claim estimate at the seventy percent confidence level as determined by the program's actuary as of fiscal year end. . ."

WAC 200-100-020 (23) states that "Secondary assets" means insurance receivables, real estate or other assets (less any nonclaims liabilities) the value of which can be independently verified by the state risk manager.

**Results: Washington Rural Counties Insurance Program met this requirement by funding claims liabilities in excess of the 70% confidence level based on our calculations and estimates. The secondary assets consist of additional cash reserves, investments and other assets (property and equipment are excluded from this calculation). Also excluded are any nonclaims liabilities, including prepaid contributions.**

	Test 1 -Primary Asset Test (WAC 200-100-03001(2))		Test 2 -Secondary Asset Test (WAC 200-100-03001(3))
\$2,915,464	Primary Assets	\$2,929,305	Secondary Assets
\$1,441,286	Estimated Claim Liabilities at the expected level per actuarial estimate	\$1,578,000	Estimated Claim Liabilities at the 70% confidence level per actuarial estimate
RESULT:	PASS	RESULT:	PASS
	Estimated outstanding liabilities (Note 1) at the expected level must be less than primary assets (cash and investments less nonclaims liabilities)(Note 2)		Estimated outstanding liabilities (Note 1) at the seventy percent confidence level must be less than combined primary assets and secondary assets (receivables, recoverables, real estate and other assets that can be independently verified by the State Risk Manager)(Note 2)

(Note 1) The outstanding liabilities are estimated by an independent actuary meeting the requirements of WAC 200-100-020(1). The Pool did not provide an actuarial report containing an estimate of unpaid claims at the 70% confidence level as required (see recommendation below), or an estimate of ULAE (unallocated loss adjustment expenses). While the estimate appears reasonable for solvency purposes based on standard industry calculations, we could not verify the amount because it was not included in the actuarial report. We estimated ULAE, to be approximately \$48,000 (see #3). Using these estimates, the Pool meets solvency requirements.

Actuarial reports submitted as part of the annual report to the State Risk Manager are available by contacting Canfield and Associates, third party administrator for Washington Rural Counties Insurance Program at (509)754-2027. Contact information is also available by visiting the Pool's website at <http://wrcip.us/>.

(Note 2) The information used to calculate assets used in the Primary and Secondary Asset Tests were obtained from the audited financial statements. The audit reports are available on the State Auditor's Office website at <http://www.sao.wa.gov/EN/Pages/default.aspx> or by telephone at (360) 902-0370.

### 3. Presentation of Liabilities

**Requirement:** The estimated liability for unpaid claims as presented in the Pool's financial statements is supported by the actuarial report.

**RCW 43.09.200** Local government accounting — Uniform system of accounting. The state auditor shall formulate, prescribe, and install a system of accounting and reporting for all local governments, which shall be uniform for every public institution, and every public office, and every public account of the same class.

The system shall exhibit true accounts and detailed statements of funds collected, received, and expended for account of the public for any purpose whatever, and by all public officers, employees, or other persons.

The accounts shall show the receipt, use, and disposition of all public property, and the income, if any, derived therefrom; all sources of public income, and the amounts due and received from each source; all receipts, vouchers, and other documents kept, or required to be kept, necessary to isolate and prove the validity of every transaction; all statements and reports made or required to be made, for the internal administration of the office to which they pertain; and all reports published or required to be published, for the information of the people regarding any and all details of the financial administration of public affairs.

**Result:** Washington Rural Counties Insurance Program reports the amount of the liability for unpaid claims at the expected loss level as \$1,441,286 in its 2011 audited financial reports. The Pool reports the liability for unpaid claims at the 70% confidence level at \$1,578,000. The actuarial report does not include a final estimate for ULAE (unallocated loss adjustment expenses) or unpaid claims at the 70% confidence level. In order to determine whether the estimated liabilities for unpaid claims reported in the Pool's financial statements are supported by the actuarial report, the actuarial report must include the additional final estimates for unpaid claims at the 70% confidence level and the ULAE. WAC 200-100-020 (29) defines "unpaid claims" as obligations for future payment resulting from claims due to past events. This liability includes loss and adjustments expenses, incurred but not reported claims (IBNR), case reserves, and unallocated loss adjustment expenses (ULAE).

**Recommendation:** The Pool should ensure that it provides year end actuarial reports to the State Risk Manager which contain final estimates of unpaid claims liabilities at the 70% confidence level and the ULAE. Data provided by the Pool did not consider insurance provisions in the estimates provided. Using standard industry calculations, we estimate the Pool's liability for ULAE at \$48,000.

### 4. Compliance with Reporting Requirements

**Requirement:** The pool is required by WAC 200-100-60 to provide unaudited annual financial statements to the State Risk Manager within 150 days of fiscal year end, and audited financial statements are to be provided to the State Risk Manager within one year of the fiscal yearend date. If required by the State Risk Manager, a pool must provide quarterly reports based on its financial condition.

**WAC 200-100-60** requires that “. . . (1) Every joint property and liability self-insurance program authorized to transact business in the state of Washington shall submit the annual report to the state risk manager.

(2) The annual report to the state risk manager shall require the following information to be submitted in electronic form:

(a) Unaudited annual financial statements, including attestation, as provided to the state auditor's office;

(b) Actuarial reserve review report on which the net claims liabilities at fiscal yearend reported in the unaudited financial statements are based;

(c) Copies of all insurance coverage documents;

(d) List of contracted consultants;

(e) Details of changes in articles of incorporation, bylaws or foundation agreement;

(f) Details of services provided by contract to nonmembers;

(g) List of members added or terminated. Such reports shall be submitted to the state risk manager no later than one hundred fifty days following the completion of the joint program's fiscal year.

(3) Audited financial statements shall be provided to the state risk manager within one year of the program's fiscal year end and comply with requirements for submission of audited financial statements established by the state risk manager.

(4) All joint self-insurance programs shall submit quarterly financial reports if, in the estimation of the state risk manager, the financial condition of a program warrants additional quarterly reporting requirements. . .”

**Results:** The Pool met this requirement by providing both audited and unaudited financial statements within the time required. The Pool is not required to report quarterly. Washington Rural Counties Insurance Program received an unqualified opinion on its audited financial statements for FY 2011 from the State Auditor.

## 5. Compliance with Membership Requirements

**Requirement: Participants in the Pool’s insurance program must sign the interlocal agreement and must also be responsible for the contingent liabilities of the program if assets are insufficient.**

WAC 200-100-02005 provides that “Membership in a joint self-insurance program requires the execution of a foundation agreement. Only members may participate in risk-sharing. Only members may participate in the self-insured retention layer, and only members may participate in the joint purchase of insurance or reinsurance”.

RCW 48.62.141 requires that “Every joint self-insurance program covering liability or property risks, excluding multistate programs governed by RCW 48.62.081, shall provide for the contingent liability of participants in the program if assets of the program are insufficient to cover the program’s liabilities”.

**Results: The Pool is in compliance with this requirement. Our review indicates that participation in the Pool’s excess and self-insured retention layer is limited only to those members signing the Pool’s interlocal agreement, which provides for shared risk and joint responsibility for liabilities. The agreement also provides that members are responsible for the contingent liabilities of the program if assets are insufficient.**

## 6. Financial Trends

**Requirement: Risk pools are required to notify the State Risk Manager if solvency requirements are not met (WAC 200-10003001(2)) and the State Risk Manager is required to monitor trends over time and take action when programs experience adverse trends which may require the State Risk Manager to take additional actions.**

WAC 200-100-03001 states, in part “. . . (4) The state risk manager shall evaluate the operational safety and soundness of the program by monitoring changes in liquidity, claims reserves and liabilities, member equity, self-insured retention, and other financial trends over time. Programs experiencing adverse trends may cause the state risk manager to increase frequency of on-site program review and monitoring, including increased communication with the governing body and requirements for corrective plans. . .”

**Results: Financial trends show the increases and decreases in assets, liabilities, revenues and expenses. The information below was taken directly from the audited financial statements of FY 2011. Upon review, no adverse financial trends were noted (See Attachment A).**

**Attachment A-Washington Rural Counties Insurance Program Trends in Assets, Liabilities & Membership**

	Year Ended						
	8/31/2011	8/31/2010	8/31/2009	8/31/2008	8/31/2007	8/31/2006	8/31/2005
	per audited f/stmt						
<b>ASSETS:</b>							
Cash and Cash Equivalents	\$2,916,612	\$2,865,080	\$2,762,283	\$2,333,752	\$2,139,431	\$2,186,107	\$1,748,792
Member Contributions Rec.	(\$1,159)	\$5,482		\$66,358	\$31,211	\$63,638	\$85,539
Accrued Member Deduct. Rec.	\$13,841	\$8,674	\$26,648				
<b>TOTAL CURRENT ASSETS</b>	<b>\$2,929,294</b>	<b>\$2,879,236</b>	<b>\$2,788,931</b>	<b>\$2,400,110</b>	<b>\$2,170,642</b>	<b>\$2,249,745</b>	<b>\$1,834,331</b>
Equipment (Net of Acc Dep)	\$3,772	\$7,544	\$11,315	\$15,087	\$0	\$0	\$0
<b>TOTAL NONCURRENT ASSETS</b>	<b>\$3,772</b>	<b>\$7,544</b>	<b>\$11,315</b>	<b>\$15,087</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>
<b>TOTAL ASSETS</b>	<b>\$2,933,066</b>	<b>\$2,886,780</b>	<b>\$2,800,246</b>	<b>\$2,415,197</b>	<b>\$2,170,642</b>	<b>\$2,249,745</b>	<b>\$1,834,331</b>
<b>LIABILITIES:</b>							
Deferred Revenue	\$0	\$0	\$0	\$0	\$0	\$313,057	\$0
IBNR	\$694,385	\$746,636					
Case Reserves	\$746,901	\$950,461	\$1,745,558	\$1,750,241	\$1,528,853	\$1,297,453	\$1,199,099
ULAE	\$0	\$127,500	\$83,936				
<b>TOTAL LIABILITIES</b>	<b>\$1,441,286</b>	<b>\$1,824,597</b>	<b>\$1,829,494</b>	<b>\$1,750,241</b>	<b>\$1,528,853</b>	<b>\$1,610,510</b>	<b>\$1,199,099</b>
<b>TOTAL NET ASSETS</b>	<b>\$1,491,780</b>	<b>\$1,062,183</b>	<b>\$970,751</b>	<b>\$664,956</b>	<b>\$641,789</b>	<b>\$639,235</b>	<b>\$635,232</b>
Number of Pool Members	8	8	8	8	8	8	8
Average Equity Per Member <sup>1</sup>	\$186,472	\$132,772	\$121,343	\$83,119	\$80,223	\$79,904	\$79,404

<sup>1</sup> Note: The unrestricted assets at the expected confidence level from audited financial statements were used for this analysis. An additional \$136,714 was restricted on the Pool's audited financial statements in compliance with regulatory requirements, resulting in final unrestricted net assets of \$1,351,294 at the 70% confidence level, and estimated average net assets per member of \$168,912.

**Conclusion:** We appreciate the cooperation and assistance of the Washington Rural Counties Insurance Program and staff of Canfield and Associates, the Pool's third party administrator, during this process. One recommendation was made (see #3) as a result of this review.

**About Washington Rural Counties Insurance Program:**

The Washington Rural Counties Insurance Program was formed through an inter-local agreement between several rural counties in 1998. The agreement allowed the joint purchase of insurance, joint self-insuring, joint hiring or contracting for risk management services and claims administration. The Pool contracts with a private firm for claims administration, insurance broker and risk management services and hence has no employees of its own.

An eight-member Board of Directors governs the Pool. Each county has one representative on the Board of Directors. The Pool operates under state law (Chapter 48.62 RCW) and must seek approval from the state Office of Risk Management within the Department of Enterprise Services for changes in its operation. For the year under audit, the Pool operated on a budget of approximately \$3.1 million.

### **About State Risk Manager Regulatory Compliance Reviews:**

RCW 48.62 provides authority for local governments to join or form a self-insurance program together with other entities, to jointly purchase insurance or reinsurance with other entities, and to contract for or hire personnel to provide risk management, claims and other administrative services. The State Risk Manager in the Office of Risk Management, Department of Enterprise Services, is authorized by RCW 48.62 to adopt rules for self-insurance programs formed under this chapter to follow. The rules contain standards for operations and management, claims administration, solvency, including frequency of actuarial studies and claims audits, and standards for contracts between self-insurance programs and private businesses.

In order to ensure compliance with these standards, which are adopted as Washington Administrative Code (WAC) 200-100, the Local Government Self-Insurance Program, under the direction of the State Risk Manager, conducts periodic reviews of joint self-insurance programs and, when necessary, provides for further investigation of those programs that are not operating in a safe and sound financial manner as required. The State Risk Manager may take certain administrative actions, including the issuance of a cease and desist order, when a program operates in violation of chapter 48.62 RCW or does not operate in a financially safe manner.

Each local government member of a joint self-insurance program is responsible for providing monies to the pool to pay claims for the years in which they were a member of the pool. Even if a member leaves a pool, a reassessment, or “cash call”, can occur in later years, requiring local government members to provide additional monies for past funding deficiencies for years in which they were a member. For this reason, the Local Government Self-Insurance program takes proactive measures to monitor the financial health of local government risk pools and to communicate the results of monitoring and periodic compliance reviews before adverse financial trends affect the pool and its local government members. Frequent reviews of compliance with the State Risk Manager’s rules are undertaken and the results are reported, in writing, to the board of directors and management of the pool.

Questions about this report should be addressed to the Local Government Self Insurance Program or the State Risk Manager, located at the Department of Enterprise Services, by telephone at 360-407-8153, or at [shannon.stuber@des.wa.gov](mailto:shannon.stuber@des.wa.gov). The Department of Enterprise Services is located at 1500 Jefferson Street, PO Box 41466, Olympia, WA 98504-1466.