Manager/Supervisor Risk Management
#3 – 11/8/11
A twice weekly e-mail training for YCPARMIA members

TOPIC: RISK FINANCING

This is a dry topic, so I'll keep it short. For our purposes there are three basic options available to employers to pay for the adverse consequences (claims/suits for money damages) of risk. All three options result in hits on the entity's general fund. An employer can:

- Retain the duty to pay;
- Transfer the duty to pay to someone else; or
- Share the duty to pay.

Retaining the risk (or self-insuring) simply means that when a claim or expense has to be paid, the entity writes the check. While the entity retains control of its money, it is difficult to budget for the inherently unpredictable patterns of claim frequency and severity. A single serious claim can have a catastrophic impact on the entity's finances.

Transferring risk, again in its simplest form, involves buying insurance. The entity pays a premium, and the carrier pays the claims (as long as they are covered, and there are adequate limits). Of course the carrier is in business to make a profit, and its risk management decisions are often oriented to its bottom line rather than the insured's, or its employee's, immediate interests.

In the late 1970's California was faced with an "insurance crisis" when the industry decided to stop writing policies for public entities (probably because of a combination of police exposures, deep-pocket suits, and claim frequency). Up to that point public entities carried large retentions ($100K to $1M per claim), and then purchased insurance for protection from large or catastrophic losses. Risk and claim services were provided by the insurance companies, often at an additional cost.

Risk sharing was the evolved response by the public entities when faced with the inability to purchase insurance. The entities entered into pooling agreements with other public entities by forming joint power authorities. These JPA's pooled their resources to pay claims, obtain professional risk and claim services, and to develop specialized responses to the unique exposures that they collectively faced. Today the vast majority of California Public entities are members of JPA's, at both the primary and excess levels, carry large self-insured retentions (SIR's), and share (rather than transfer) their risk with other members. Due to the success of the JPA's in addressing their member's risk, penetration into the public entity market by the insurance industry is now largely limited to a few specialized products.

Next Topic: YCPARMIA