

Reciprocals, Local Pools and the Commercial Market – What is Right for My Municipality?

You may be wondering if a pool is a good fit for your municipality. We've answered some of the most common questions we get asked about pooling. Take a few minutes to read the information below and then give us a call with any additional questions you may have.

1. What are some of the risks of creating a reciprocal?

When it comes to establishing a reciprocal it is important to be aware of the risk. Should the reciprocal collapse, members will need to fully rejoin the commercial market. In some cases, members may be on the hook for the payout of claims where the incident occurred during the years the municipality was covered by the reciprocal.

Sustainability and stability cannot be overlooked. The organization you partner with should be able to demonstrate decades of consistent, financially healthy performance.

Additional Reading:

[Ontario Municipal Insurance Exchange \(OMEX\) suspends underwriting operations](#)

2. What are some benefits of the commercial market to consider before jumping into a reciprocal?

In the lead up to starting a reciprocal, it is not uncommon to hear *'insurers only work for their 10% - 15% profit margins'*. While it is true that profitability is important for insurers, the statement is misleading in a number of ways.

First, what is called a profit in the commercial market is termed a surplus for a reciprocal, though treated differently. Both approaches should seek to buffer the operations.

Second, when the commercial market earns a profit this benefits municipalities. It means that insurance capital is more likely to flow into the sector leading to stable insurance limits and increased competition which ultimately results in lower premiums.

Third, the scale of a large commercial carrier has important benefits that a smaller reciprocal would struggle to realize. For example;

- Some insurers own the restoration firms used to complete the work required from insurance claims. Using these companies ensures better service at competitive pricing.
- Large insurers pre-secure agreements to ensure adequate adjusting staff after a major catastrophe, thereby reducing the post claim costs.
- Vast amounts of data and insights results in better forecasting of claims costs and more realistic pricing targets.

Fourth, reciprocals do not remove themselves entirely from the commercial market, they simply reduce the amount of capital purchased. Outside impact from the wider commercial market still exists.

Fifth, retro assessments for an extremely complex and 'long-tailed' segment like municipal operations is a significant risk that needs to be weighed against the insurer's profit margin (where that risk is fully assumed by the insurer).

Finally, a large insurer is not impacted to the same extent when a sizeable profitable client (or clients) finds an alternative solution.

3. What is a local pool?

A local pool is a group of participating entities who share similar exposures to accidental losses. The group, which is typically formed from geographically related municipalities (e.g. municipalities within Counties and Regions), benefits from the power of the collective in self-insuring. The group pre-funds estimated losses and administrative costs through annual premiums collected from participants based on loss experience.

4. What are some of the challenges of a pool?

While a pool may be quite advantageous to some, there are a number of challenges to consider first. Some of these challenges may be bigger hurdles than others. To ensure the success of your individual municipality and the future success of the pool as a whole the following challenges should be considered and addressed:

- Start-up challenges:
 - While a pool can look attractive in a hard market, the initial funding and start-up costs can be quite significant. This includes creating a base layer for the pool, costs for consultants, legal expenses and actuarial studies as well as other external professionals to help establish the pool.
- Greater assumption of risk – any and all claims received become the responsibility of the pool. You also assume risk when having to subsidize other pool members' losses.
- Political challenges – must have total commitment from all participating municipalities as well as delegated authority to set up a separate Board to oversee the pool.
- Ensuring adequate funding to meet current and future loss obligations. This can be significant in the inaugural years of a pool.
- Ongoing costs for administration – the pool will ideally function as a miniature insurance company. Staffing will be required which is an ongoing cost that needs to be considered.

5. Will a pool save money?

It is important to remember that a pool is a long term initiative with the main objective being to stabilize premiums as opposed to a dollar value in savings. Any savings seen from a pool will take a number of years to accumulate as the first years after establishment focus on adequately funding the pool. To do this, all members will pay the same annual premiums as opposed to premiums based on claims and risk which you will see in later years. This could result in higher premiums than what one was paying in the commercial market.

Implementing a solid risk management strategy will help reduce your exposure and lower claims and in turn, premiums.

6. What are the main things to consider before starting a pool?

There are a few things you should first consider before you begin to start a pool. These considerations will help determine if a pool is a good fit for a particular group:

- What is the optimal level of local and pool deductibles?
- What coverages will be included?
- Cost of risk – what is the total cost of risk?
- Establishing member premiums – what is the basis?
- Are members dedicated? What is the level of commitment from the interested parties?
- Consider the cyclical nature of the business. If you are considering a pool because of external factors such as a hard market, will a soft market entice members to leave the pool?
- Political involvement – how will future changes to council affect the commitment and involvement of the pool?
- Will the pool be led by an individual or team that has the expertise to guarantee success?
- How will the pool look for and manage new insurance trends?

7. What is needed to start a pool?

Starting a pool is no small task. There are many fundamental operational, administrative, and legal tasks that need to be completed before you can be on your way. The list below is a brief summary of some of the elements required:

- Initial feasibility study to determine and define these key elements:
 - Actuarial: initial study for optimal structure
 - Legal: set up member agreements
- Set up governance and structures to ensure equal votes among members
- Establish rules for joining and leaving the pool
- Determine the organizational structure including where the pool is located

- Determine operating costs: total cost of the program
 - Local deductible
 - Funding the pool layer
- Claims handling – adjusting and legal
- Administration – including loss control, investment, actuarial and accounting

8. What if a member wants to leave the pool?

Prior to forming your pool, members should have defined and agreed to a set of obligations and responsibilities. These parameters should help guide the group when and if a member chooses to exit the pool.

The exiting member may still hold a financial obligation to the group and pool. If, after exiting the pool they receive a claim from a year in which they were a member, the member and/or the pool will be responsible for the payout of the claim. This can become tricky because of the long-tailed nature of certain claims.

Ultimately, the exit of a group member can significantly impact the stability of the remaining members moving forward. Ensuring a proper time commitment from each member is crucial to help ensure the success of a pool.

9. What happens if the pool needs to be dissolved?

During the initial formation of the pool, agreements will have been established in the event the pool needs to be dissolved. This will include items such as the division of assets among members.

It is important to remember that although the pool may be dissolved, claims made and received for years when a member was insured under the pool will be the responsibility of the pool and the members.

10. What happens if one member uses significantly more of the funds than other members?

Part of performing an annual actuarial review is to help ensure this doesn't happen. If a member has higher claims, their annual contribution to the pool will reflect that. It is key to maintain financial integrity to ensure long term stability of the pool.

11. What is the basic structure of a team managing the pool?

There are many different roles required to effectively manage a pool. It is up to your group how to best fill and manage the roles. The list below represents some of the positions required. Depending on your group's specific circumstances, the internal structure may look different:

- Risk Manager
- Claims Administration
- Legal Team (typically external)
- Actuarial Team (typically external)
- Board Representative(s) from each member.
- Optional local insurance broker familiar with pools

12. Why should you choose an insurance partner, not just a provider.

An intangible commodity like insurance may lead you to believe that all carriers are the same. When you choose to partner with IPE, you're not only purchasing an insurance policy, but also an entire program designed to reduce your total cost of risk. The Intact brand, scale and buying power are important factors to consider when weighing the benefits of the commercial market as opposed to a pool structure.

13. What are the benefits of working with an MGA?

There are many benefits to working with an MGA. Not only can an MGA help provide your organization with long term stability but they provide the knowledge and expertise of highly skilled and specialized professionals ensuring you have information you need to make informed decisions for your municipality.

An MGA has the authority to write and service business on behalf of strategic partners who share a commitment and dedication to protecting specialized organizations. Because partners are long-term participants on the program, they understand the nature of fluctuating market conditions and complex claims you have access to many invested backing partners to help build a tailored insurance program for your municipality's specific needs.

An MGA is a partner who is focused on providing a complete insurance program specific to your municipality that includes complimentary value added services that help drive down the cost of claims and innovative first to market products and enhancements. When working with an MGA, you receive personalized service and expertise from a full-service, local and in-house team of risk management, claims, marketing and underwriting professionals.

Unlike a reciprocal model, a policy issued by an MGA is a full risk transfer vehicle not subject to retroactive assessments but rather a fixed term and premium. This results in an adequately priced program that helps to ensure longevity.

14. What are the best ways to manage insurance premiums?

To best manage your premiums, it is important to understand that in order to do so, you must improve the performance of your municipality. This is done in a number of ways, for example:

- Risk profile – assess your municipality's risk profile and learn how you can lower your overall risk with the help of our risk management services.
- Loss history – by reviewing your loss history, you can proactively mitigate potential future claims.
- Engaged proactive risk management – ensure routine inspections are implemented across your municipality in all areas. Our **Centre of Excellence** has resources to help get you started.
- Technology can be an excellent tool to help automate and accurately track many different aspects of risk. There are a number of different products that can help your municipality effectively handle risk. IPE has partnered with leading risk management software provider, ClearRisk to help bring enhanced risk management solutions to your municipality.
- Training can help ensure your teams are up to date on the latest standards and best practices when it comes to creating safe, strong and resilient municipalities. IPE offers a variety of webinars and seminars to help support your municipality's training practices.
- Information management – detailed records, reporting and documentation not only minimize stress but also demonstrate due diligence. An effective information management strategy helps your municipality stay on top of things like inspections, renewals.

If you have any questions regarding reciprocals, local pools, or the commercial market, contact your Company Representative or [connect with us here](#).