

The financial information included in this report is based on the audited financial statements.
The financial statement audit report has since been withdrawn by the Washington State Auditor's Office,
which could affect the accuracy of the information contained in this report.

Office of Financial Management
Local Government Self Insurance Program
Report
for
Cities Insurance Association of Washington

Issued June 3, 2009

April 3, 2009

Shannon Stuber
Program Administrator
Local Government Self Insurance Program
Department of Risk Management
Office of Financial Management
PO Box 41027
Olympia, WA 98504-1027

Dear Sir:

In accordance with procedures established by the state risk manager, we conducted an examination of

Cities Insurance Association of Washington

otherwise referred to as the "Pool" or "CIAW"

SCOPE OF EXAMINATION:

This full-scope examination was conducted by the Local Government Self-Insurance Program (LGSIP) in the Office of Risk Management. The examination covered the years ended August 31, 2002, 2003, 2004, 2005, 2006, 2007 and 2008.

Our regulatory examination included such tests of the records and such other procedures as we considered necessary in the circumstances. The accuracy of the information provided by CIAW is the responsibility of the Pool's management. Our responsibility is to determine compliance with rules and standards adopted by the state risk manager in conjunction with the Property and Liability Advisory Board based on the information provided. Our examination included a review of the Pool's management and operational practices, an evaluation of the adequacy of reserves and a review of actuarially determined liabilities. In addition, our examination included tests to provide reasonable assurance that the Pool was in compliance with applicable laws and with rules adopted by the state risk manager.

The Pool is audited annually by the Washington State Auditor's Office. The Auditor expressed unqualified opinions on the Pool's financial statements for the calendar years 2002 through 2006. We placed substantial reliance on the audited financial statements for calendar years 2002 through 2006, and consequently performed only minimal testing for those periods. We concentrated our examination efforts on the years ended August 31, 2007 and 2008. We placed

high reliance on the work of the Pool's actuary and therefore did not conduct an independent review of the actuary's findings as part of the examination.

GENERAL HISTORY:

Cities Insurance Association of Washington is a public entity joint self-insurance program operating in the State of Washington. The Pool began operations in September of 1988. The Pool is capitalized by member public entities consisting of Washington cities and towns. The Pool provides liability, auto physical damage and property insurance to its members and an additional group of participants known as associate members.

The member policies are occurrence based; however, some coverages are on a claims made basis.

The Pool has a self insured retention of \$100,000 per liability claims per occurrence. As part of the \$100,000 each member retains an underlying retention of \$1,000, while the Pool pays \$99,000. The Pool also provides property insurance with a self insured retention of \$10,000, of which the member pays \$1,000 and the Pool pays \$9,000. The Pool has a stop loss policy which limits the amount paid by the self-insured retentions. The stop loss policy reimburses the Pool for monies paid during the claims settlement process after each claim is settled.

The Pool also provides loss prevention and risk management services to member cities and towns as well as and other participants, known as "associate members". The associate members include municipal taxing districts, such as irrigation districts, water districts, and fire protection districts. The associate members participate in the Pool's insurance, claims management, loss prevention, training, risk management and other programs offered to regular members.

MEMBERSHIP:

CIAW is owned by its members, and capitalized with contributions from member entities. The Pool is formed through an interlocal agreement as required by 48.62.031(2) Revised Code of Washington (RCW). The members agree to future assessments should the pool fail to meet funding requirements.

The member entities are eligible to serve on the Board of Directors. The Board consists of ten directors elected by members in three geographic areas. The members in each area vote to elect a representative to the Board from that area.

The Pool also maintains a category of members known as "associate members". These municipal entities do not sign the interlocal agreement, but sign an Associate Member Agreement instead. The associate members are not subject to reassessments. They do not vote in electing a representative to the Board, do not serve on the Board and do not have an equity interest in the program.

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Each associate member purchases insurance through an "Associate Member Agreement" with the Pool. Members are subject to additional assessments should the Pool require funds, but associate members are not subject to additional assessments, according to the terms of the associate member agreements. As of the end of August 31, 2008, the Pool membership consisted of 95 members and 162 associate members.

The Office of Risk Management has notified the Pool that the 162 associate members will be required to sign the interlocal agreement and join the self-insurance program as members by December 31, 2010 if they are to continue in the Pool's insurance program.

The Pool also insured a group of 63 tribal entities as associate members during the years ending August 31, 2004 and 2005. The Pool no longer provides insurance to this group.

The Pool has a formula approved by the governing body to provide for the dissolution and payment of equity to members. The Pool also has a policy to provide for termination of a member should the Pool determine the member no longer meets the Pool's criteria for membership.

Members may leave the pool by giving a one year written notice prior to August 31 to terminate membership as of September 1 of the following year. The member forfeits equity in the program by leaving. Associate members may also leave by giving a one year notice in the same manner. Associate members have no equity in the Pool.

RESERVES:

The Pool is required to maintain minimum reserves in the amount of the actuarially determined liability for unpaid claims of \$7.43 million as of August 31, 2008. The Pool is also required to maintain secondary reserves to offset adverse claims development and rating inaccuracies. As of August 31, 2008 the Pool had assets of \$832,422 in cash and investments to fund the liability for unpaid claims. The Pool reports the liability of \$7.43 million as of August 31, 2008, but is not fully funding this amount. The Pool has, in the past, fully funded its liability for unpaid claims, but is not currently doing so. The comparative financial information located on page ten of this report provides information on changes in assets and liabilities over years.

The Pool also reports a receivable of \$7,000,796, which includes substantial insurance recoveries due to the Pool. The receivable for insurance recoveries has increased because the pool does not receive repayment from the stop loss policy until the claim is settled. The timing and recoveries of these payments will require that the Pool collect an additional surcharge to premiums annually, reassess members for past liabilities of the Pool, and/or make other arrangements with the stop loss insurance provider regarding the timing of the reimbursements or responsibility for handling claims at the stop loss attachment point.

The Office of Risk Management asks the Pool to submit a plan for approval to the state risk manager indicating how the Pool will increase reserves over the next three to five years to fund

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its expected claims liabilities and to establish secondary reserves. The plan is to be submitted within ninety days of the issuance of this report and the state risk manager will provide written approval within thirty days of the plan's submission.

STATE AND FEDERAL TAX EXEMPTIONS

Pursuant to IRS revenue ruling 90-74, income of municipal risk pools is excluded from gross income under Internal Revenue Code 115(1). RCW 48.62 provides an exemption from insurance premium taxes in addition to business and occupation taxes imposed pursuant to RCW 82.04.

AFFILIATED PARTIES AND TRANSACTIONS:

The Pool purchases loss prevention and risk management services from Canfield and Associates, a third party administrator owned by Brown and Brown Inc. The Pool also purchases financial, accounting and claims administration services from the third party administrator. The administrator also procures actuarial services on behalf of the Pool. In addition, the third party administrator procures brokerage services from Public Risk Underwriters, also owned by the same parent company as the third party administrator.

INVESTMENTS:

As of August 31, 2008, the Pool maintained deposits of \$30, 148 in the State Treasurer's Investment Pool as required by RCW 48.62.11(4).

FINANCIAL POSITION:

Regulations in place as of August 31, 2008 required the Pool maintain minimum reserves of \$7.43 million to fund the liability for unpaid claims as determined by the Pool's actuary.

The Pool's liability for unpaid claims was not fully funded as of that date.

AREAS OF OPERATION:

The Pool is a public entity joint self-insurance program operating in the State of Washington in accordance with 48.62 RCW and 82.60 Washington Administrative Code (WAC). According to information provided by the Pool, CIAW provides no services, including insurance, claims administration, loss prevention and risk management to entities outside of Washington.

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EXCESS INSURANCE:

The Pool maintains excess insurance contracts for liability with St. Paul Traveler's Insurance. The aggregate limits of coverage for general liability and auto liability are \$20,000,000 each. The Pool maintains excess insurance contracts for public official's liability with aggregate limits of \$10,000,000 and employment practices liability limits of \$5,000,000. Aggregate limits for employee dishonesty are \$500,000, and gross limits of coverage on the Pool's property program are \$125,000,000. Additionally the Pool purchases a stop loss policy for its liability program which reduces the risk of loss to members.

Per occurrence limits, combined with the Pool's self-insured retention limits, are \$10,000,000 each for general liability, automobile liability and public official's liability insurance. Per occurrence limits, combined with the Pool's self-insured retention limits, are \$5,000,000 for employment practices, \$25,000,000 for property damage and \$500,000 for employee dishonesty.

The Pool recorded premiums for excess insurance during 2008 of \$4,590,124. As of August 31, 2008, the Pool recorded a receivable of \$7,000,796 which includes substantial insurance recoveries due to the Pool. If the reinsurers are not able to meet their obligations under these agreements, the Pool would be liable for any defaulted amounts.

ACCOUNTS AND RECORDS:

The primary locations of the Pool's books and records are at the office of the third party administrator, Canfield and Associates, in Ephrata, Washington.

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ELECTED OFFICIALS AND MANAGEMENT:

The following persons served as the Pool's directors as of August 31, 2008.

<u>Name and Entity Represented</u>	<u>Occupation</u>
Wes Crago City of Ephrata	City Administrator
Laura Koenig City of Sultan	Clerk-Treasurer
Gina Anderson City of Woodland	Deputy Clerk-Treasurer
Kathy Lobdell City of Omak	Clerk-Treasurer
Pam Olsen City of Brewster	City Clerk
Carla Shirley City of Wilbur	Clerk-Treasurer
Kathy Bowman City of College Place	Planning Director
Teresa Camfield City of Lynden	Finance Director
Brian Asmus City of Liberty Lake	Chief of Police

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The following persons were responsible for the management of the Pool:

<u>Name</u>	<u>Title</u>
Mr. James Cherf Third Party Administrator	President Canfield and Associates

Committees:

As of August 31, 2008, the Pool's Board of Directors had established the following committees:

Executive Committee:

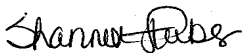
Wes Crago, Chairman
Pam Olsen, Vice Chair
Laura Koenig, Fiscal Officer

CONCLUSION:

Results:

1. We ask that the Pool submit a detailed plan to the state risk manager within ninety days to address the specific manner in which the Pool will fund the claims liabilities and establish reserves over the next three to five years.
2. We ask that the annual financial statement and report to members include disclosure regarding the ability of the Pool to obtain additional funds through reassessment of members. Currently, the information appears to include associate members in the group of members who are eligible for reassessment. Information provided by the Pool indicates that 95 members are subject to reassessment and 162 are not subject to reassessment, and therefore are not required to provide additional funds if reserves are not adequate to fund claims liabilities according to the terms of the associate member agreements.
3. We recommend the financial statements and annual report to members include updated information on the geographic regions and representation on the board. The Management Discussion and Analysis indicates that there are seven geographic regions and ten representatives to the board. Information provided to the examiner indicates that there are now three regions from which the ten representatives are elected by members in those regions.

We appreciate the cooperation of the Pool's governing body and management during our examination. We look forward to assisting the Pool in making these changes and providing additional information and assistance as necessary.



Program Administrator
Local Government Self-Insurance Program

RESPONSE:

The Pool responds that it will comply with all requests made as a result of this examination.

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COMPARATIVE FINANCIAL INFORMATION:

The comparative financial information below has been reviewed for accuracy by the Pool's management and board. Financial information for the years ended August 31, 2007 and 2008 was taken from the Pool's Annual Statements as filed with the Office of Financial Management. Amounts for the years ended August 31, 2002 through August 31, 2006 are taken from financial statements audited by the State Auditor's Office.

	2008	2007	2006	2005	2004	2003	2002
Assets:							
Cash	\$832,442	\$393,460	\$649,795	\$1,331,282	\$3,374,306	\$959,067	\$604,526
Investments		\$763,123	\$763,122	\$1,034,153	\$190,000	\$859,167	\$474,615
Noncurrent	\$172,028	\$75,000	\$87,500	\$100,000	\$112,500	\$125,000	\$125,000
Prepaid Ins				\$1,960,650	\$1,666,156		
Receivables	\$7,000,796	\$4,196,686	\$2,491,356	\$2,457,022	\$2,458,265	\$1,976,698	\$1,418,134
Total Assets	\$8,005,266	\$5,428,269	\$3,991,773	\$6,883,107	\$7,801,227	\$3,919,932	\$2,622,275
Liabilities:							
Unpaid Clams	\$7,428,339	\$4,864,482	\$2,475,194	\$2,221,657	\$2,180,331	\$921,667	\$484,170
Deferred Rev				\$2,208,799	\$3,121,703	\$534,997	
A/P			\$440,273	\$546,400	\$392,457	\$218,749	
Total Liabilities	\$7,428,339	\$4,864,482	\$2,915,467	\$4,976,856	\$5,694,491	\$1,675,413	\$484,170
Net Assets	\$576,927	\$563,787	\$1,076,306	\$1,906,251	\$2,106,736	\$2,244,519	\$2,138,105
Members	97	99	111	120	120	115	
Municipal Associate Members	160	157	160	172	158	151	
Tribal Associate Members				63	63		
Total	257	256	271	355	341	266	

Note: During the reporting periods 2004 and 2005, the Pool insured a group of 63 tribal associate members. The tribal associate members purchased insurance through the pool, but the policy year was not the same as that of other members and associate members. Because of the timing difference, an increase in assets and a corresponding liability for deferred revenue are shown on the Pool's financial statements and reflected in the above trend information.