LEGISLATIVE RESEARCH COMMISSION

PROGRAM REVIEW AND INVESTIGATIONS COMMITTEE

School Insurance

Research Report No. 347

Prepared by

Rick Graycarek and Margaret Hurst

Kentucky Legislative Research Commission

David L. Williams
President, LRC Co-Chair

Jody Richards
Speaker, LRC Co-Chair

SENATE

Katie Kratz Stine
President Pro Tem

Dan Kelly
Majority Floor Leader

Ed Worley
Minority Floor Leader

Dan Seum
Majority Caucus Chair

Johnny Ray Turner
Minority Caucus Chair

Carroll Gibson
Majority Whip

Joey Pendleton
Minority Whip

HOUSE

Larry Clark
Speaker Pro Tem

Rocky Adkins
Majority Floor Leader

Jeffrey Hoover
Minority Floor Leader

Charlie Hoffman
Majority Caucus Chair

Bob DeWeese
Minority Caucus Chair

Rob Wilkey
Majority Whip

Stan Lee
Minority Whip

Robert Sherman, Director

The Kentucky Legislative Research Commission is a 16-member committee comprised of the majority and minority leadership of the Kentucky Senate and House of Representatives. Under Chapter 7 of the Kentucky Revised Statutes, the Commission constitutes the administrative office for the Kentucky General Assembly. Its director serves as chief administrative officer of the legislature when it is not in session. The Commission and its staff, by law and by practice, perform numerous fact-finding and service functions for members of the General Assembly. The Commission provides professional, clerical, and other employees required by legislators when the General Assembly is in session and during the interim period between sessions. These employees, in turn, assist committees and individual members in preparing legislation. Other services include conducting studies and investigations, organizing and staffing committee meetings and public hearings, maintaining official legislative records and other reference materials, furnishing information about the legislature to the public, compiling and publishing administrative regulations, administering a legislative intern program, conducting a presession orientation conference for legislators, and publishing a daily index of legislative activity during sessions of the General Assembly.

The Commission also is responsible for statute revision; publication and distribution of the *Acts* and *Journals* following sessions of the General Assembly; and maintenance of furnishings, equipment, and supplies for the legislature.

The Commission functions as Kentucky's Commission on Interstate Cooperation in carrying out the program of the Council of State Governments as it relates to Kentucky.

School Insurance

Program Review and Investigations Committee

Sen. Ernie Harris, Co-chair
Rep. Rick G. Nelson, Co-chair

Sen. Charlie Borders	Rep. Sheldon E. Baugh
Sen. Brett Guthrie	Rep. Dwight D. Butler
Sen. Vernie McGaha	Rep. Leslie Combs
Sen. R.J. Palmer	Rep. Charlie Hoffman
Sen. Joey Pendleton	Rep. Ruth Ann Palumbo
Sen. Dan Seum	Rep. Rick Rand
Sen. Katie Stine	Rep. Arnold Simpson

Project Staff

Rick Graycarek
Margaret Hurst

Greg Hager, Ph.D.
Committee Staff Administrator

Research Report No. 347

Legislative Research Commission
Frankfort, Kentucky
lrc.ky.gov

Adopted October 11, 2007

Reports Adopted by the Program Review and Investigations Committee, 1996 to 2007

Medicaid Prescription Drug Benefit Fraud, Abuse, and Cost Management, 2007

Kentucky Housing Corporation, 2007

Siting of Electric Transmission Lines, 2007

School Insurance, Report 347, 2007

Drug Courts, Report 346, 2007

Pollution Cap and Trade Programs in Kentucky, Report 343, 2007

Kentucky's Foster Care Program Is Improving, but Challenges Remain, Report 342, 2006

Planning for School Facilities Can Be Improved To Better Serve the Needs of All Students, 2006

Kentucky's Community Mental Health System Is Expanding and Would Benefit From Better Planning and Reporting, Report 340, 2006

Highly Skilled Educator Program, Report 339, 2006

School Size and Student Outcomes in Kentucky's Public Schools, Report 334, 2006

Information Systems Can Help Prevent, but Not Eliminate, Health Care Fraud and Abuse, Report 333, 2006

Implications of the U.S. Supreme Court's *Kelo* Decision for the Use of Eminent Domain in Kentucky, Report 330, 2005

Planning for Water Projects in Kentucky: Implementation of Senate Bill 409, Report 329, 2005

Kentucky Can Improve the Coordination of Protective Services for Elderly and Other Vulnerable Adults, Report 327, 2005

Improved Coordination and Information Could Reduce the Backlog of Unserved Warrants, Report 326, 2005.

Offshore Outsourcing of Kentucky State Government Services: Direct Contracting Is Limited but the Amount of Subcontracting Is Unknown, Report 325, 2005

Appropriate Management and Technology Can Reduce Costs and Risks of Computer Use by State Employees, Report 324, 2004

Uncollected Revenues and Improper Payments Cost Kentucky Millions of Dollars a Year, Report 322, 2004

Improving Fiscal Accountability and Effectiveness of Services in the Kentucky Transitional Assistance Program, Report 321, 2004

Human Service Transportation Delivery, Report 319, 2004

The Commonwealth Accountability Testing System, Report 312, 2003

Postsecondary Education in Kentucky: Systemwide Improvement but Accountability Is Insufficient, Report 311, 2003

The SEEK Formula for Funding Kentucky's School Districts: An Evaluation of Data, Procedures, and Budgeting, Report 310, 2002

East and West Kentucky Corporations, Report 308, 2002

An Analysis of Kentucky's Prevailing Wage Laws and Procedures, Report 304, 2001

Executive Branch Contracting for Services: Inconsistent Procedures Limit Accountability and Efficiency, Report 303, 2001

Performance-based Budgeting: Concepts and Examples, Report 302, 2001

Impact Plus, Report 300, 2001

Kentucky Housing Corporation Allocation of Federal Homeless Grant Money, Report 291, 2000

Progress Report on Coordinated Human Service Transportation System, Report 298, 1999

Personnel Pilot Projects: Design Weakness Limits Effectiveness, Report 295, 1999

Kentucky Early Intervention System - First Steps, Report 293, 1999

Health Insurance Market for Employees and Retirees of Kentucky State Government, Report 286, 1999

State Agency Service Contract Administration, Report 285, 1999

Review of the Kentucky Children's Health Insurance Program, Report 283, 1999

Motor Vehicle Registration Abuse, Report 282, 1999

Kentucky Medicaid Drug File and Prior Authorization System, Report 281, 1999

Division of Licensing and Regulation, Cabinet for Health Services, Office of Inspector General, Report 279, 1997

State Park Marinas, Report 278, 1997

Department for Social Insurance Eligibility Determination Process, Report 277, 1996

Cabinet for Human Resources Family Service Workers' Caseloads, Report 275, 1996

Kentucky Medical Assistance Program, Report 274, 1996

Foreword

In completing this report, numerous individuals provided valuable assistance. The authors of this report thank staff from the Department of Education, Office of Insurance, Office of Workers' Claims, and the Kentucky School Boards Association for sharing their knowledge. Among Legislative Research Commission staff, the authors recognize Jo Ann Ewalt, Brenda Landy, Greg Rush, John King, Linda Bussell, and John Perry for their help.

This report would not have been possible without information from school district officials, insurance agents, insurance brokers, third-party administrators, auditors, and insurers. Their input and insights are greatly appreciated.

Commendations also go to the more than 100 school district officials who completed a questionnaire about school insurance and risk management activities.

The authors would also like to acknowledge Harold Pumford from the Association of Governmental Risk Pools, Dottie Gray from the National School Boards Association, Constance Warner from the Public Risk Management Institute, Joe Greathouse from the Kentucky Association of Counties, and Wendy Zhan from the Ohio Legislative Service Commission for their assistance.

Robert Sherman
Director

Legislative Research Commission
Frankfort, Kentucky
October 11, 2007

Contents

List of Tables

List of Figures

Summary

The primary purpose of this report is to describe the types and amounts of property and casualty insurance that school districts carry. Unemployment insurance is also considered.

This report describes the school insurance market in Kentucky, including insurers, insurance agents, and the insurance selection process. It also describes the regulatory oversight of Kentucky's school insurance market and presents information about the Kentucky School Boards Insurance Trust (KSBIT). KSBIT is an organization created by school boards to provide insurance to Kentucky school districts.

This report has five recommendations.

Insurance Coverage

Basic to insurance is the relationship between premium and coverage. In general, premiums, or the cost of insurance, increase as coverage increases.

"Self-insurance" refers to school districts that retain primary, but not necessarily complete, responsibility for paying claims. Self-insurance is not used to describe an organization, such as KSBIT, that collectively insures school districts. Those entities are called risk pools.

State law requires that school districts carry property, boiler, auto liability, and workers' compensation insurances. If a district contracts with a third party to transport students, the district must also ensure the third party has auto liability insurance.

Although unemployment insurance is not technically an insurance program, school districts are required to participate and annually appropriate more than $7 million for unemployment benefit payments and administration.

Besides required insurances, districts typically carry general and educators' legal liability insurances, and auto property insurances. A few school districts carry other insurances.

District insurance decisions are potentially influenced by financial condition, level of risk aversion, claims history, and market conditions. Insurance coverage amounts and financial responsibility retained by school districts generally vary. This is due, in part, to a lack of regulatory and statutory requirements.

School districts determine how much property insurance to carry by using building replacement rates established by the Kentucky Department of Education. Several school district officials interviewed by staff expressed concern about the replacement rates. For some, the coverage amounts were considered inadequate.

School districts, whether self-insured or insured through a commercial insurer or risk pool, retain some risk. For self-insured districts, this is through a self-insured retention. For districts that are commercially insured or members of a risk pool, retention of risk is through a deductible. Self-insured retentions and deductibles represent the initial financial amount a district bears for any claim. In general, self-insured retention amounts are considerably greater than deductibles.

Recommendation 2.1

The Kentucky Department of Education should implement the following changes to its process for determining property replacement rates for school districts.

First, using the most recent RSMeans data, the department should adjust its property replacement rates by a standard inflation measure, such as the Producer Price Index, to account for the fact that the RSMeans data is typically more than 1 year old when it is applied.

Second, the department should consider using the regional cost indices available through RSMeans to calculate the cost of construction. Using regional costs could provide better estimates of local construction costs.

Third, the department's replacement rates should include estimated amounts for architect and engineer fees, bond sale costs, and other contingencies.

Recommendation 2.2

The Kentucky Department of Education should consider actively monitoring the types and amounts of insurance that school districts carry.

Selection of Insurance

To insure risks, Kentucky school districts most commonly purchase policies from commercial insurers or risk pools. Commercial insurers charge school districts a premium in exchange for assuming some amount of risk. Risk pools, such as KSBIT, operate similarly, with the exception that insured districts can be assessed an amount above their premium if the pool becomes insolvent. This is called joint and several liability.

School districts may also self-insure. Four school districts self-insure their workers' compensation risks; one self-insures its property. Other school districts also self-insure their auto property risks by maintaining an in-house body repair shop. Self-insured districts typically purchase reinsurance, which limits their potential losses.

Proponents of self-insurance emphasize lower costs. Critics point to increased financial risk, including high self-insured retention amounts and long-term financial responsibility for paying claims, such as workers' compensation.

The Kentucky school insurance market is dominated by KSBIT and Indiana Insurance, a commercial insurer. These two collectively insure most Kentucky school districts across all insurance lines. Depending on the insurance line, between 33 percent and 39 percent of districts purchased insurance from KSBIT and between 19 percent and 40 percent purchased from Indiana Insurance in the most recent year reported.

Insurance agents serve as the local contact for insured school districts. They provide various services to school districts and, on behalf of an insurer, provide school districts with bids.

School districts use different methods to solicit insurance bids. Some districts contact an insurer directly. Others advertise or work with a local insurance agent. In some instances, school districts use multiple methods.

According to Program Review staff's survey of school districts, the percentage of school districts that received more than one bid for a particular insurance line was generally less than 50 percent. Workers' compensation insurance was the exception. Fifty-three percent of districts reported receiving two or more bids.

Based on staff's interviews, many school district officials appear uncertain about which insurance lines should be bid and by which method. School districts typically receive two or three insurance bids for each solicitation. More bids are received for workers' compensation, on average, than other insurance lines.

Recommendation 3.1

The Kentucky Department of Education should make available to school districts a document identifying how districts should procure insurance services.

Regulation

The regulatory process varies for commercial insurers, risk pools, and self-insured school districts. Commercial insurers and risk pools are regulated by the Office of Insurance, but under different accounting standards. School districts that self-insure workers' compensation are regulated by the Office of Workers' Claims. Districts that self-insure property do not appear to be regulated by any state agency.

In 2004, the Office of Insurance became the regulatory agent for workers' compensation risk pools after a pool operated by Associated Industries of Kentucky collapsed. The Office of Insurance subsequently discovered a $5 million deficit in KSBIT's workers' compensation fund.

Concerns exist that self-insured school districts might not maintain sufficient financial reserves to pay all claims. Until recently, districts that self-insured workers' compensation had to maintain a surety bond equal to current and future claims.

Kentucky School Boards Insurance Trust

Net assets for KSBIT's workers' compensation, liability, and property insurance funds declined in recent years. Net premiums for each fund increased between 2000 and 2006, but reported deficits in the workers' compensation and liability funds likely stalled this trend. Over the past 5 years, the number of insured districts declined in the workers' compensation and liability funds.

In 2003, $1.3 million was transferred from KSBIT's unemployment insurance fund to another fund that was used to help shore up the trust's workers' compensation fund. Because the unemployment insurance fund does not bear any risk, school districts retain complete financial responsibility for claims payments. Some districts likely benefited at the expense of others.

Some program expenditures within the Kentucky School Boards Association appear disproportionately allocated to KSBIT. For example, all property taxes and utility and employee vacation expenses for the association's 19 programs are allocated to the trust.

Recommendation 4.1

Should the Kentucky School Boards Insurance Trust re-create its guaranty fund or establish a similar fund, it should do so only after providing all affected school districts with written notification.

Recommendation 4.2

The Kentucky School Boards Association should consider developing a method by which program expenses are proportionately allocated to the Kentucky School Boards Insurance Trust and other programs.

Chapter 1

Overview and Background

Introduction

On a rainy afternoon in 2005, a school bus returning from a field trip rear-ended a car in Knox County. No one on the bus was injured, but the car's driver required surgery. The bus driver's school district carried insurance that paid claims related to this accident.

Insurance is the transfer of risk from one entity to another. In general, the more risk assumed by an insurer, the higher the insurance premium will be.

To limit financial loss from such risks, school districts frequently carry insurance. All insurance functions in a similar manner. In exchange for assuming some degree of risk, insurance companies charge the insured a premium. The degree of risk assumed depends on various factors, including the amounts of deductibles and coverage. In general, the more risk assumed by an insurer, the higher the premium will be. Factors such as previous claims history and market conditions also affect what a district pays.

This report examines the types and amounts of property and casualty insurance that school districts carry. Insurers, insurance agents, insurance selection, regulations, and the Kentucky School Boards Insurance Trust (KSBIT) are also reviewed.

In this report, the types and amounts of property and casualty insurance that school districts carry are examined. Insurers, insurance agents, and the insurance selection process are described; as is the regulation of commercial insurers, risk pools, and self-insured school districts.

This report also describes various financial characteristics of the Kentucky School Boards Insurance Trust (KSBIT), which insures more Kentucky school districts than any other insurer.

Description of This Study

This is a study of workers' compensation, property, boiler, auto liability, general liability, educators' legal liability, and unemployment insurances that Kentucky public school districts carry.

How This Study Was Conducted

On December 14, 2006, the Program Review and Investigations Committee voted to have staff study school insurance for Kentucky's public school districts. The objectives were to describe school insurance in Kentucky, including the types of risks school districts face and how they insure them; explain the school insurance regulatory process; and review the Kentucky School Boards Insurance Trust.

To complete this study, staff analyzed reports and documents related to school insurance, including data provided by the Office of Insurance, the Office of Workers' Claims, the Kentucky Department of Education, and KSBIT. Staff also conducted an extensive Internet and periodical search.

Staff interviewed officials from 10 school districts, four insurers, two third-party administrators, two insurance agencies, and two independent auditors. Staff also contacted officials from the Public Risk Management Institute, the Association of Governmental Risk Pools, the National School Boards Association, and the Kentucky Association of Counties.

Staff conducted a survey of school district officials. District superintendents and finance directors provided information about workers' compensation, property, general and educators' legal liability, auto, and unemployment insurances. The questionnaire included questions specific to risk management activities. Responses from 105 of 175 school districts were received. Appendix A has the complete survey.

Organization of the Report

The remainder of this chapter presents the report's major conclusions and introduces the subject of school insurance. Particular attention is given to terminology and basic insurance principles used throughout this report. A brief history of major insurance events and a review of the Kentucky School Boards Insurance Trust's unemployment insurance fund conclude the chapter.

Chapter 2 describes school insurance in Kentucky. Required and commonly carried insurances, including deductibles and coverage amounts, are highlighted. Factors potentially affecting district insurance decisions are also discussed.

Chapter 3 describes insurers, insurance agents, and the insurance selection process used by school districts. Commercial insurers, risk pools, and self-insurance are described, including the benefits and costs of self-insurance.

Chapter 4 describes how commercial insurers, risk pools, and self-insured school districts are regulated. KSBIT is also considered. The chapter concludes by describing state programs to assist school districts or insurers in the event of financial difficulty.

Appendix A contains the questionnaire for the survey of school districts. Appendix B summarizes information for districts participating in the Kentucky School Boards Insurance Trust's unemployment insurance fund. Appendix C has school districts' property appraisal values. Appendix D has data on workers' compensation reports filed by school districts. Appendix E contains the Kentucky School Boards Association's response to this report.

Major Conclusions

This report has six major conclusions.
1. No state agency systematically monitors school districts' insurance decisions.
2. School districts carry different combinations of property and casualty insurance and may have different coverage amounts.
3. No risk pool, commercial insurer, or self-insured school district can eliminate all risks.
4. School districts solicit insurance bids at different intervals using different methods, in part, because of uncertainty about the bid process.
5. KSBIT's workers' compensation fund has a deficit of approximately $4 million. Prior to merging with its property fund in 2007, the trust's liability fund had a $1 million deficit. These deficits do not reflect a current inability to pay claims.
6. KSBIT created a fund in 2004 that was used to financially support its workers' compensation fund. The new fund received money from the trust's unemployment insurance and liability funds.

This report has six major conclusions.

1. No state agency systematically monitors school districts' insurance decisions.

2. School districts carry different combinations of property and casualty insurance and may have different coverage amounts.

3. School districts purchase insurance from commercial insurers and risk pools, or they self-insure. No risk pool, commercial insurer, or self-insured school district can eliminate all risks.

4. School districts solicit insurance bids at different intervals using different methods, in part, because of uncertainty about the bid process.

5. The Kentucky School Boards Insurance Trust's workers' compensation fund has a deficit of approximately $4 million. Prior to merging with its property fund in 2007, the trust's liability fund had a $1 million deficit. These deficits do not reflect a current inability to pay claims.

6. The Kentucky School Boards Insurance Trust created a fund in 2004 that was used to financially support its workers' compensation fund. The new fund received money from the trust's unemployment insurance and liability funds.

Self-insurance Defined

"Self-insurance" is the term applied to an individual school district that maintains primary responsibility for paying its claims.

"Self-insurance" has different meanings. In state statute, "self-insurance" is the term applied to any individual school district that is primarily responsible for paying insurance claims or a group of school districts that join together and share the risks of insurance. Insurance industry and accounting professionals only apply "self-insurance" to individual school districts. School districts that join a group are considered "risk pools" because risks are shared (Young and Reed).

School districts that join together to insure risks are called "risk pools." KSBIT is a risk pool.

This report will follow industry and accounting conventions. Self-insurance will only mean school districts that retain primary responsibility for paying claims. School districts that join with other districts to insure risks will be called risk pools. Under that definition, KSBIT is a risk pool.

Self-insured retention is the amount of loss initially borne by a self-insured district or a risk pool.

Throughout this report, the expression "self-insured retention" means the initial amount of loss that an entity pays. It is similar to a deductible except that self-insured retention amounts do not affect total insurance benefits and are generally higher.

Self-insured retentions are used by self-insured school districts and risk pools. For self-insured districts, the retention amount reflects the amount of loss initially borne by a district. For example, if a school district that self-insures workers' compensation has a self-insured retention of $250,000 the district is responsible for the first $250,000 in losses.

For risk pools, self-insured retention means the initial amount of loss borne by the pool. Although school districts that share risks via a risk pool are not considered "self-insured," the pool itself can be considered self-insured because it retains primary responsibility for paying claims.

Kentucky Association of Counties and the Associated Industries of Kentucky

To some extent, historical events have influenced the nature and direction of this report. In 1993, the Program Review and Investigations Committee adopted a report that examined the Kentucky Association of Counties' insurance funds (Commonwealth. Legislative. Program). Concerns about that association's funds, including its financial stability and management, were discussed. State statutory and regulatory changes relating to collectively insured risks were subsequently enacted.

In 2004, the Associated Industries of Kentucky, a workers' compensation risk pool, collapsed. Insufficient premiums and other factors appear to have contributed to the fund's insolvency. In order to pay claims, current and former participants were assessed almost $91 million in retroactive premiums.

Kentucky School Boards Insurance Trust

Responsibility for regulating workers' compensation risk pools was transferred from the Office of Workers' Claims to the Office of Insurance in 2004.

During the collapse of Associated Industries of Kentucky, concerns about the financial integrity of other workers' compensation risk pools arose. An executive order subsequently transferred regulatory authority from the Office of Workers' Claims to the Office of Insurance. The Office of Insurance then assessed the financial condition of each workers' compensation risk pool, including the one operated by KSBIT.

In 2004, KSBIT's workers' compensation fund had a $5 million deficit. In 2007, the deficit is $4 million. A deficit means long-run claims exceed total available assets. The fund has sufficient cash flow to meet current expenses.

Upon reviewing KSBIT's workers' compensation fund in 2004, the Office of Insurance reported a $5 million deficit. The office required the fund to carry a $6.5 million surety bond as additional financial protection. A surety bond is a financial guarantee by a third party to pay claims up to the amount of the bond should the trust's fund become insolvent.

According to the Office of Insurance, the fund's cash flow was sufficient to meet current expenses. In the long run, total claims were estimated to exceed total available assets by $5 million, which necessitated the surety bond.

KSBIT's workers' compensation fund ended fiscal year 2006 with a $4 million deficit. Premium increases, expenditure reductions, and other cost improvements likely contributed to this reduction.

Unemployment Insurance

School districts must provide unemployment insurance benefits. Although unemployment insurance is technically not an insurance program, it is important because school districts appropriate more than $7 million a year for these activities.

Public school districts in Kentucky must provide unemployment insurance benefits to their employees (KRS Chapter 341). Technically, unemployment insurance is not an insurance program because risks are not transferred from a school district to an insurer. Unemployment insurance is included in this report because it is an important component of school district risk finance activities. School districts appropriate more than $7 million a year for unemployment insurance benefit payments and administration. Districts pay for these benefits in one of two ways. One approach is for a school district to make periodic contributions to a third party that will process claims and transfer funds to the state's unemployment insurance fund whenever benefits are drawn by a district employee. Nearly all school districts use this approach, with KSBIT serving as the third party. Appendix B has data on school districts' contributions and benefit payments.

School districts can pay unemployment insurance benefits directly to the state or through a third party.

Three school districts choose to reimburse the state directly for each unemployment insurance claim.

Districts using KSBIT or a similar third party are less prone to spikes in unemployment insurance benefit payments because they make annual or monthly contributions. Making contributions regardless of actual claims means districts do not have immediate access to those funds during the fiscal year.

Districts that reimburse the state for each claim have greater control over their funds. Such districts only expend money when benefits are paid. Those districts may experience monthly swings in unemployment insurance expenditures as benefit payments may vary throughout the year.

Chapter 2

Insurance Lines, Deductibles, and Coverage Amounts

Introduction

School districts face numerous risks. These include the threat of property damage; injury to employees or students; and liability for actions of educators, staff, or board members. To limit monetary loss, school districts can attempt to control those risks, purchase insurance to mitigate losses from those risks, or do both.

Risk control is an important component in a school district's overall risk management strategy, but this report focuses on insurance. This chapter begins with a description of required insurances and then provides details of other common insurances carried by school districts. Differences in insurance coverage amounts, including factors that might contribute to these differences, conclude the chapter.

Required Insurances for School Districts

State law requires that school districts carry property, boiler, workers' compensation, auto liability, and unemployment insurances.

State statute and administrative regulation require school districts to carry property, boiler, workers' compensation, certain auto, and unemployment insurances (KRS 160.105, KRS 160.310, and 702 KAR 3:030). Other insurances are optional. Information in the following sections on required insurances comes primarily from staff's survey of school districts.

Property Insurance

KRS 160.105 and 702 KAR 3:030 require districts to insure buildings and structures they own at 100 percent of replacement cost.

School districts determine how much property insurance to carry by using mandated building replacement rates established by the Kentucky Department of Education (KDE).

Replacement Rates. To determine replacement cost, school districts must use specific square-foot replacement rates promulgated by the Kentucky Department of Education (KDE). These rates vary by building type. Table 2.1 lists the rates for the 2007-2008 school year.

Table 2.1
Kentucky Department of Education's
2007-2008 Property Insurance Replacement Rates

Building Type	Replacement Rate Per Square Foot
Elementary school	$137
Middle school	$137
High school	$149
Vocational school	$140
Central office	$139
Bus garage	$116
Storage building	$77

Source: Kentucky Department of Education.

According to KDE, these property replacement rates come from a nationally recognized building cost source, RSMeans Building Construction Cost Data. To calculate the amount of insurance to purchase, school districts multiply the square feet for each of their buildings by the corresponding KDE replacement rate.

Several school district officials, insurers, and insurance agents expressed concern that KDE's property replacement rates are inadequate.

Concerns. Based on staff's interviews with school district officials, insurers, and insurance agents, KDE's method for determining property insurance coverage may be inappropriate and inadequate. Officials identified several concerns.

School districts may be underinsured because the department's replacement rates do not allow for local variation in building costs and do not consider architectural, siting, and finance costs involved in replacing school property.

The most common concern was that KDE's rates do not allow for local variation in construction costs. This means a school district in rural south-central Kentucky applies the same property replacement rates as a district in the Louisville urban area, even though actual replacement costs might be different for the two districts. Consequently, some districts may be underinsured and others overinsured.

Many school districts do not have their property regularly appraised.

The extent to which school districts are underinsured or overinsured is unclear. In order to make such a determination, actual property values would have to be compared with the amount of insurance purchased according to KDE's replacement rates. For many districts, actual property values are unknown or outdated because the districts do not regularly have their property appraised. Ten years or more have passed since some districts had their last appraisal.

School district officials also noted that they could not carry more insurance than KDE's rates prescribed. Administrative regulation requires districts to carry insurance equal to 100 percent of the value determined by the department's replacement rates (702 KAR 3:030).

Another concern is that KDE's property replacement rates do not consider ancillary construction costs such as architectural, finance, and siting. By excluding these potential costs, school districts may be insufficiently insured and could end up paying these costs directly if a property insurance claim is filed.

A recent report by the Office of Education Accountability indicated concerns similar to the ones identified here and recommended three changes (Commonwealth. Legislative. Office). As of the start of fiscal year 2008, the Department of Education had not implemented those recommendations. Consequently, the Office of Education Accountability's recommendations are repeated as Recommendation 2.1 here.

Recommendation 2.1

The Kentucky Department of Education should implement the following changes to its process for determining property replacement rates for school districts.

First, using the most recent RSMeans data, the department should adjust its property replacement rates by a standard inflation measure, such as the Producer Price Index, to account for the fact that the RSMeans data is typically more than 1 year old when it is applied.

Second, the department should consider using the regional cost indices available through RSMeans to calculate the cost of construction. Using regional costs could provide better estimates of local construction costs.

Third, the department's replacement rates should include estimated amounts for architects' and engineers' fees, bond sale costs, and other contingencies.

School districts with property values greater than $100 million can carry insurance policies for less than the amount prescribed by KDE's property replacement rates.

Blanket Limitations. Districts with insured property values greater than $100 million can purchase an insurance policy with a blanket limitation, which caps an insurer's liability. According to administrative regulation 702 KAR 3:030, a blanket limitation policy must equal at least $100 million and at least 50 percent of a district's total property replacement cost. For example, a blanket limitation of $150 million means an insurer is only liable for claims up to $150 million even though a district's property may be valued at more than this amount. Claims exceeding the blanket limitation for a given occurrence would not be covered.

At least 23 districts in Kentucky have property values of $100 million or more; some have blanket limitation policies. Appendix C has a table listing property values by school district. Owensboro Independent, for example, has property valued at $128 million and has a blanket limitation policy. Jefferson County has property valued at $1.6 billion but does not have a blanket limitation.

Most school districts responding to Program Review staff's survey reported carrying flood, earthquake, and wind insurance.

Flood, Earthquake, and Wind Coverage. Most school districts responding to Program Review staff's survey reported carrying flood, earthquake, and wind insurance. Table 2.2 shows that 60 percent had flood coverage and 67 percent had wind coverage. Eighty-four percent reported carrying earthquake insurance.

Table 2.2
Percentage of School Districts With Flood, Earthquake, and Wind Insurance

Insurance	Yes	No	Unsure/ No Response
Flood	60%	25%	15%
Earthquake	84%	3%	13%
Wind	67%	10%	23%

Source: Program Review staff's survey of school districts; 105 districts responded.

Boiler Insurance

Administrative regulation requires districts with steam boilers, which are used to heat school buildings, to carry boiler and machinery insurance (702 KAR 3:030). Boiler and machinery insurance covers the contents of the building in which a steam boiler operates.

Most school districts have one or more steam boilers and a majority of those are insured through the district's property policy.

According to staff's survey of school district officials, 90 of 105 school district respondents reported having one or more boilers in their district. Of these, 85 indicated that their boilers were insured under their existing property policy or under a separate boiler and machinery policy. Five districts were uncertain about their coverage.

Workers' Compensation Insurance

Workers' compensation insurance provides payment to employees injured or sickened while performing work-related activities.

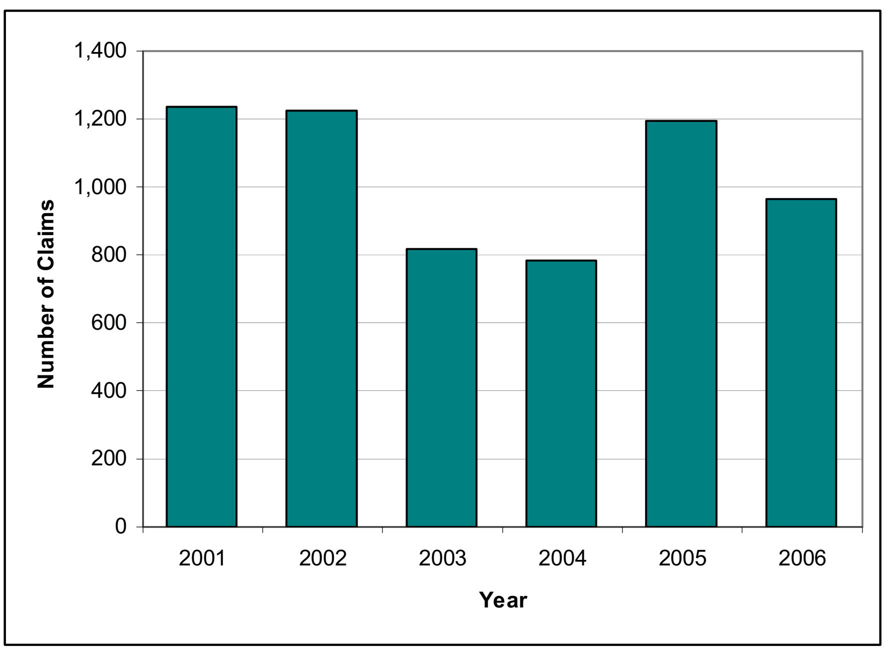
All public school districts in Kentucky carry workers' compensation insurance, which provides payment to employees injured or sickened while performing work-related activities. Insurers assess premiums based, in part, on a district's payroll amount, type of employee, and claims history.

Between 2001 and 2006, about 6,200 school district reports of injury that resulted in one or more missed days of work were filed.

Between 2001 and 2006, Kentucky school district employees filed about 6,200 reports of injury that resulted in more than one missed day of work.[1] Figure 2.A shows that the annual number of school district reports fluctuated during this time. There were approximately 1,200 reports in each of 3 years. In each of 2 years, there were approximately 800 reports. Appendix D has the number of reports filed by school districts from 2001 to 2006.

In Figure 2.A, 2004 workers' compensation data for the four self-insured school districts appeared incomplete; other years may also be incomplete. Figure 2.A, therefore, likely does not include all workers' compensation reports.

Figure 2.A
Total Number of Workers' Compensation Reports Filed Annually by School Districts (2001-2006)



Note: The graph may not reflect all reports; some self-insured school districts may not have submitted all data.
Source: Program Review staff's analysis of data provided by the Office of Workers' Claims.

[1] During that time, about 240,000 reports were filed in Kentucky for all industries, according to data from the Office of Workers' Claims.

Auto Liability Insurance

School districts and transportation contractors must carry liability and indemnity insurance.

Liability and indemnity insurance are required for transportation services that are owned or operated by the board (702 KAR 5:030). Minimum insurance amounts are $2 million per occurrence combined for bodily injury and property damage; $500,000 for uninsured/underinsured motorist; and $20,000 per passenger for "no fault" coverage. Contractors that provide transportation services to school districts must also carry automobile liability and indemnity insurances (KRS 160.310).

Unemployment Insurance

Unemployment insurance is not purchased; school districts bear all unemployment insurance costs.

School districts must provide unemployment insurance. Unlike other insurances, unemployment insurance is not purchased. School districts retain all risk and pay all unemployment benefits. Almost all districts, though, make monthly contributions to KSBIT, which processes districts' unemployment insurance claims. In 2006, only Christian County, Covington Independent, and Hart County school districts did not participate in KSBIT's unemployment insurance fund.

Other Insurances Commonly Carried by Districts

In addition to required insurances, school districts carry somewhat different mixes of other insurances and purchase different amounts of coverage. This is due to market conditions and districts' level of risk aversion and claims history.

Besides property, boiler, workers' compensation, auto liability, and unemployment insurances, school districts carry different mixes of insurance and purchase different amounts of coverage. This is because state requirements and guidelines concerning the appropriate lines and amounts of insurance are either lacking or limited.

Factors Potentially Affecting District Insurance Decisions

Reasons school districts carry different insurances in different amounts include a district's financial condition, level of risk aversion, and claims history. Market conditions might also play a role (Young and Reed; Young and Fone).

Limited resources and competing demands require local school boards to make trade-offs. School boards must decide how much to spend on insurance versus how much to spend on other programs. Generally speaking, more risk-averse school boards will purchase more insurance than will other boards.

Risk aversion and financial condition are interrelated. School boards weigh the benefits and costs of purchasing insurance against the amount of risk they are willing to assume.

Recent claims history, including the number and dollar amount of claims, can also affect a school district's insurance decisions. A district that experiences few insurance claims over a long period might eliminate that coverage or increase its deductible. Either action could reduce the district's annual insurance premium. Similarly, a district with a high number of claims or expensive claims might lower its deductible. That could increase its premium.

The availability and price of insurance can affect the lines and amounts of insurance school districts purchase. One measure of market condition is the number of insurance bids school districts receive. More insurance bids, all else equal, suggest a competitive market. Table 2.3 shows the percentage of school districts that received a specified number of insurance bids for specified insurance lines.

Table 2.3
Percentage of Districts Reporting Specified Insurance Bids
(Most Recent Year)

	Number of Bids Received							
Insurance	**0**	**1**	**2**	**3**	**4**	**5 or More**	**Not Sure**	**Total**
Workers' Compensation	8%	24%	27%	15%	6%	5%	16%	100%
General Liability	3%	29%	32%	9%	2%	1%	25%	100%
Educators' Legal Liability	3%	28%	31%	9%	3%	1%	26%	100%
Property	3%	24%	35%	7%	4%	2%	26%	100%
Vehicle	3%	27%	34%	10%	2%	1%	24%	100%

Note: Due to rounding, figures may not total 100 percent.
Source: Program Review staff's analysis of school district insurance survey; 105 respondents.

Most school districts receive one or two bids for each insurance line. A few districts reported receiving no bids, but those generally reflect a district's decision to negotiate with an existing insurer only.

Most school districts responding to staff's survey reported receiving one or two bids for each insurance line. Districts received three or more bids less than 15 percent of the time. Workers' compensation bids were the exception. Districts reported receiving three or more workers' compensation bids more than 20 percent of the time. This may be because the number of workers' compensation insurers is greater than for the other insurance lines.

A small percentage of districts reported receiving no bids. According to survey responses and staff interviews, these school districts typically negotiated with their current insurer and did not solicit bids.

General liability and educators' legal liability had similar bid histories. This is not surprising since school districts almost always purchase these insurances from the same insurer.

Other Types of Insurance

Besides property, boiler, workers' compensation, auto liability, and unemployment insurances, school districts frequently purchase other insurances. These include general and educators' legal liability and auto property.

School districts typically carry general and educators' legal liability insurances. These protect the district from inappropriate or illegal actions by staff, teachers, or board members.

General and educators' legal liability insurances protect a school district from certain legal claims stemming from inappropriate or illegal actions by staff, teachers, or board members (KRS 160.160). School districts typically carry both lines of insurance.

General liability insurance may also include school violence and sexual misconduct provisions. Based on a survey of school districts, 63 percent of respondents reported carrying a general liability policy with a school violence provision, and 77 percent reported carrying a policy with a sexual misconduct provision. Remaining school districts either did not respond to this question or indicated that their general liability policy did not include these provisions.

Except for several larger school districts, most purchase auto collision and comprehensive insurances.

Vehicle property insurance, which includes collision and comprehensive coverage, was carried by most districts. Jefferson County and Fayette County did not purchase this line of coverage because each district has an in-house body and maintenance shop that performs vehicle repair work.

Less common insurances carried by school districts include aviation, laptop computer, and inland merchant marine. School district officials identified these insurances during staff interviews.

Aviation insurance provides coverage for students participating in flight school or other airborne activities. The Jefferson County school district purchases this insurance.

Laptop computer insurance typically covers district-owned laptop computers that students take home. Jefferson County has a laptop computer program and purchases laptop computer insurance.

Inland marine insurance covers bus radios and other communication equipment. Taylor County is an example of a school district that purchases this line of insurance.

Risk Transfer and Risk Assumption

School districts insure risks through commercial insurers, risk pools, or by self-insuring.

Kentucky school districts can choose to insure risks through a commercial insurer, a risk pool, or by self-insuring. With commercial insurance, a school district pays an insurer a premium in exchange for that insurer paying for certain losses. Risk pools operate similarly, with the exception that insured districts can be assessed an amount separate from their premium if the pool becomes insolvent. Each self-insured district assumes primary responsibility for paying losses.

In general, those differences are referred to as “risk assumption” versus “risk transfer.” Under self-insurance, a school district assumes the risk of financial loss. In its simplest form, all losses are paid by the district. With commercial and risk pool insurance, risk is transferred from a school district to the insurer. In its simplest form, all loses are paid by the insurer.

Deductibles and Self-insured Retentions

Most districts retain some financial responsibility for paying claims. For self-insured districts, this is called a self-insured retention; for commercially insured and risk pool member districts, this is called a deductible.

In many cases, commercially insured and risk pool member school districts do not transfer all risk, and self-insured school districts do not assume all risk. Districts retain some financial exposure. For commercially insured districts or members of a risk pool, this is through a deductible. For individually self-insured districts and organizations created as risk pools, this is through a self-insured retention. In general, districts that are commercially insured or members of a risk pool retain significantly less exposure than self-insured ones.

Deductible amounts varied both within and across insurance lines.

Deductibles. Table 2.4 identifies the most common deductible amounts for districts that are commercially insured or members of a risk pool. Most districts reported carrying no deductible on their workers’ compensation and general liability insurances. Districts most commonly reported $2,500 deductibles for educators’ legal liability and $1,000 deductibles for property and vehicle collision and comprehensive coverages.

Within each insurance line, school districts reported varied deductible amounts. For example, school districts reported deductible amounts between $0 and $500,000 for general liability insurances.

Table 2.4
Deductible Amount Per Insurance Line (Most Recent Year)

Insurance	Most Common Deductible	Percent of Districts	Lowest Deductible	Highest Deductible
Workers' Compensation	$0	97%	$0	$15,000
General Liability	$0	67%	$0	$500,000
Educators' Legal Liability	$2,500	67%	$0	$1 million
Property	$1,000	55%	$0	$25,000
Vehicle				
— Collision	$1,000	70%	$250	$10,000
— Comprehensive	$1,000	76%	$250	$1 million
— Liability	$0	47%	$0	$2 million
— Personal Injury	$0	46%	$0	$500,000

Note: The number of respondents varied by insurance line and ranged from 58 to 91.
Source: Program Review staff's analysis of school district insurance survey.

Self-insured retention amounts varied by school district.

Self-insured Retentions. Table 2.5 shows the self-insured retention amounts for each known self-insured school district by insurance line.[2] The amounts are significantly larger than the deductible amounts for commercially insured and risk pool member districts.

Table 2.5
Self-insured Retention Amounts

District	Workers' Compensation	Property
Floyd County	$250,000	n/a
Harlan County	$500,000	n/a
Jefferson County	$1,000,000	n/a
Pike County	$250,000	$100,000
KSBIT	$350,000	$1,500,000

Source: Staff's analysis of school district survey and interviews.

Self-insured retention amounts vary. Floyd County and Pike County school districts reported retaining responsibility for the first $250,000 per claim in workers' compensation liabilities. This means the first $250,000 in insured losses are paid by the district. Harlan County had a $500,000 self-insured retention. Jefferson County had a $1 million self-insured retention. KSBIT, a risk pool, reported a $350,000 self-insured retention.

[2] Although Fayette County and Jefferson County public school districts self-insure their vehicle property coverage, neither is considered here because all losses are borne by those districts.

Only Pike County is known to self-insure its property insurance. That district reported a self-insured retention of $100,000. KSBIT had a self-insured retention of $1.5 million for its property insurance risk pool.

Reinsurance is insurance that protects a self-insured entity from catastrophic loss. KSBIT and districts with a self-insured retention purchase reinsurance.

Reinsurance. Self-insured retention amounts are affected by the reinsurance market. Reinsurance is insurance that protects a self-insured entity from catastrophic loss. KSBIT and districts with a self-insured retention purchase reinsurance.

A self-insured school district pays a premium to a reinsurer, which in turn pays for losses above the district's self-insured retention amount. For a district with a self-insured retention of $250,000, a reinsurer will pay claims that exceed $250,000. A similar process applies to risk pools.

As with standard insurance, reinsurance coverage amounts are capped. Reinsurers pay claims that exceed a district's self-insured retention up to a certain amount. Continuing with the previous example, a district might purchase a reinsurance policy that covers losses from $250,000 to $1 million. In that case, the district would pay losses less than $250,000 and greater than $1 million; the reinsurer would cover losses in between.

Accessing the reinsurance market is similar to accessing the commercial insurance market. Self-insured districts request bids or search for reinsurers willing to underwrite them.

Reinsurers move into and out of the Kentucky school market. This can make it difficult for school districts to purchase reinsurance or for them to locate competitively priced reinsurance. As with commercial insurance, reinsurance premiums are regularly affected by broader market conditions and district-specific factors. Accessing the reinsurance market can be critical to continue operating as a self-insured district.

Coverage Amounts

School districts frequently purchase different amounts of insurance, in part, because state statute or regulation may not prescribe an amount.

Workers' compensation, general liability, educators' legal liability and vehicle insurance coverage amounts vary by school district. Neither state statute nor administrative regulation prescribe coverage amounts, so local school boards determine how much insurance to purchase.

Individual claim limits identify the maximum amounts an insurer will pay per claim. Depending on the insurance line, individual claim limits range from $500 to $25 million.

Per Occurrence. Table 2.6 lists the most common coverage amounts by insurance line, along with the percentage of survey respondents that indicated that amount. These amounts reflect individual, or per-occurrence, claim limits. For example, a $1 million individual policy limit indicates that an insurer will pay up to $1 million for each claim. Property insurance coverage amounts are not described in Table 2.6 because property insurance amounts vary by district according to KDE's replacement rates.

Table 2.6
Individual Claim Limit Per Insurance Line
(Most Recent Year)

Insurance	Most Common Limit	Percent of Districts	Lowest Limit	Highest Limit
Workers' Compensation	$1 million	61%	$100,000	$25 million
General Liability	$1 million	98%	$1 million	$5 million
Educators' Legal Liability	$1 million	99%	$1 million	$5 million
Vehicle				
— Collision	$2 million	49%	$100,000	$5 million
— Comprehensive	Actual cash value	47%	$500	$5 million
— Liability	$2 million	79%	$100,000	$5 million
— Personal Injury	$20,000	65%	$1,000	$5 million

Note: The number of respondents varied by insurance line and ranged from 57 to 94.
Source: Program Review staff's analysis of school district survey.

Aggregate claim limits identify the maximum amount an insurer will pay for all claims within a policy year. Depending on the insurance line, aggregate claim limits range from $500 to unlimited.

Aggregate. Aggregate coverage amounts represent the total amount an insurer will pay for all claims filed by a school district during a given policy year and are important indicators of insurance protection. Lower limits generally place a district at greater financial risk. Should total claims exceed a district's aggregate policy limit, the district will be financially responsible unless the district has an excess or umbrella rider. A benefit of lower aggregate limits is that insurance premiums are generally lower.

As with per-occurrence insurance coverage amounts, aggregate amounts were most consistent for general liability and educators' legal liability. Table 2.7 shows that more than four-fifths of school districts responding to the survey indicated that their aggregate limit for general liability was $2 million. Almost four-fifths of respondents reported a $1 million aggregate limit for their educators' legal liability.

Table 2.7
Aggregate Claim Limit Per Insurance Line
(Most Recent Year)

Insurance	Most Common Limit	Percent of Districts	Lowest Limit	Highest Limit
Workers' Compensation	$1 million	62%	$500,000	Unlimited
General Liability	$2 million	86%	$1 million	$5 million
Educators' Legal Liability	$1 million	79%	$1 million	$10 million
Vehicle				
— Collision	$2 million	40%	$500,000	$7 million
— Comprehensive	$2 million	44%	$500	Unlimited
— Liability	$2 million	68%	$300,000	Unlimited
— Personal Injury	$20,000	43%	$10,000	$5 million

Note: The number of respondents varied by insurance line and ranged from 28 to 93.
Source: Program Review staff's analysis of school district survey.

Premiums

Average premiums for workers' compensation, general liability, educators' legal liability, and vehicle insurances declined over the most recent 3-year period.

Although school districts responding to Program Review staff's survey usually included coverage amounts for only 1 year, most provided premium information for 3 years. Based on this survey, average premiums for workers' compensation, general liability, educators' legal liability, and vehicle insurances declined over a 3-year period.

Table 2.8 shows average annual premiums by insurance line.[3] Overall, average premiums declined over the most recent 3-year period. Average premiums for workers' compensation and general liability insurances initially rose from the first year to the second year before falling below the initial year's average in the most recent year. Average premiums for educators' legal liability and vehicle insurances declined each year. Only average property insurance premiums have increased.

Average premiums declined, in percentage terms, the most for vehicle and educators' legal liability. Higher average property insurance premiums may reflect higher property values associated with new school buildings built over this period.

[3] The number of school districts reporting a premium varied by insurance line and year.

Table 2.8
Average Premium Per Insurance Line and Year

Insurance	Most Recent Year	Second Most Recent	Third Most Recent	Change
Workers' Compensation	$122,529	$138,596	$135,202	-$12,673
General Liability	$29,235	$32,310	$31,299	-$2,064
Educators' Legal Liability	$15,831	$16,334	$18,826	-$2,996
Property	$90,157	$93,113	$87,376	$2,780
Vehicle	$64,727	$76,415	$80,337	-$15,610

Note: "Change" is from the third most recent year to the most recent year.
Source: Program Review staff's analysis of school district survey.

State Oversight Is Limited

Local school districts are largely responsible for determining other insurance coverage amounts and whether or not to purchase optional insurances.

State oversight of the lines and amounts of insurance school districts carry consists primarily of promulgating standard property replacement rates and auto liability amounts. Local school districts are largely responsible for determining other insurance coverage amounts and even whether or not to purchase certain types of insurance. This limited oversight means school districts occasionally carry different lines of insurance and different amounts of the same insurances.

Local decision making has benefits. School district officials likely have the best information about the types of risk confronting a district and know which insurance lines to carry.

It is also conceivable that local school district officials could make decisions that leave a district underinsured. That could place the district in a precarious financial position if a subsequent insurance loss was borne by the district.

The state does not systematically monitor the types and amounts of insurance that districts carry. More oversight may be appropriate.

More state oversight may be appropriate. At present, the state does not systematically monitor the types or amounts of insurance that districts carry. Without some amount of statewide information, a catastrophic event could cause significant financial difficulty for an inadequately insured school district. Such a district may need to raise taxes or lower expenditures in order to rebuild property, pay insurance claims, or maintain existing school operations. By monitoring the types and amounts of insurance that school districts carry, state officials could recognize whether districts are inadequately insured.

Recommendation 2.2

The Kentucky Department of Education should consider actively monitoring the types and amounts of insurance that school districts carry.

Chapter 3

Insurers, Agents, and the Insurance Selection Process

Introduction

School districts frequently retain the services of an insurance agent, a broker, or an educational co-op to assist them in selecting insurance.

In this chapter, insurers, agents, and the insurance selection process are described. The chapter begins by examining the number and types of insurers underwriting school district insurance policies. Overall, Kentucky school districts purchase insurance policies from many insurers, but two insurers have the majority of the market. A brief discussion of insurance agents follows. The insurance bid process, including why school district officials are frequently uncertain about how to solicit bids, concludes the chapter.

Insurers

Kentucky school districts can choose to insure risks through a commercial insurer, a risk pool, or by self-insuring. Considerations of insurer type include differences in out-of-pocket expenses, premium payments, and potential financial liability.

Kentucky's school insurance market has had periods with many insurers followed by periods with fewer insurers. These swings can create significant problems for school districts.

Indiana Insurance, a commercial insurer, and KSBIT underwrite most school insurance policies in Kentucky.

Overall, Indiana Insurance, a commercial insurer, and the Kentucky School Boards Insurance Trust, a risk pool, underwrite most school insurance policies in Kentucky. In this section, all three insurer types are described as is the overall condition of the market.

Commercial Insurance

Commercial insurers are generally for-profit companies that provide a wide range of insurance products. In many instances, commercial insurers operate across state boundaries and sometimes internationally.

In Kentucky, many commercial insurers underwrite insurance policies for school districts. Indiana Insurance, by a considerable margin, underwrites the most policies. Other insurers have included Bridgefield Casualty, Netherlands, and St. Paul's Travelers.

Indiana Insurance is a business unit of the Liberty Mutual Group. According to company officials, Indiana Insurance operates in Illinois, Indiana, Kentucky, Michigan, Ohio, and Tennessee. Officials noted that between 8 and 78 percent of school districts in each of those states carry one or more policies underwritten by Indiana Insurance. In Kentucky, 45 percent of school districts reportedly carry one or more policies with Indiana Insurance.

Risk Pools

A risk pool is a group of entities with similar risk exposures that create, in effect, their own insurance company. Risk pools typically are formed along the basis of some common membership, such as school districts, counties, or municipalities.

Joint and several liability is a characteristic of risk pools. This means a risk pool can assess its current and past members if the fund has insufficient funds to pay claims.

Joint and Several Liability. A characteristic of risk pools is joint and several liability, which means that a pool with insufficient funds can impose and collect funds from current and past members. Leaving a risk pool, therefore, does not absolve a member of financial responsibility.

For example, Associated Industries of Kentucky, a workers' compensation risk pool, reported a multi-million dollar deficit in 2004 and entered voluntary rehabilitation the next year. A state-appointed rehabilitator assessed the pool's current and former members to pay claims. In September 2005, a Franklin County Circuit judge ruled that all pool members could be assessed in order to eliminate the pool's deficit and to pay injured workers. State statute now requires risk pools to notify members of any joint and several arrangement (KRS 304.48-200 and KRS 304.50-130).

History. Beginning in the 1970s, high insurance premiums or inadequate market access spurred the creation of many risk pools (Rosenthal; Young. "Pooling!"). The number of public entity risk pools has grown rapidly, and several hundred pools now exist (Pumford).

According to one estimate by a national organization familiar with public entity risk pools, about 85 percent of all political subdivisions have one or more lines of insurance with a public entity risk pool (Pumford).

In 1978, the Kentucky School Boards Association formed the Kentucky School Boards Insurance Trust to provide insurance to school districts.

In 1978, the Kentucky School Boards Association formed the Kentucky School Boards Insurance Trust to provide insurance to school districts. At least 23 other state school board associations offer insurance (National). Of Kentucky's contiguous states, Ohio and Illinois operate such programs. Due to various difficulties, Tennessee recently ended its program (Riley).

Benefits and Costs of Self-insurance

School districts primarily self-insure because it costs less than other forms of insurance.

Based on staff interviews and a literature review, school districts primarily self-insure because it costs less than other forms of insurance (Kollie; Moody; Randall). Compared to commercially insured districts, self-insured entities do not pay dividends to shareholders, they do not pay certain taxes, and they typically have lower marketing expenses (Moody). Self-insured entities also retain investment income and choose their own claims management. Consequently, self-insured school districts may have lower operating costs than commercial insurers, which may mean lower insurance costs.

Another benefit applies specifically to workers' compensation. Self-insured school districts and risk pools are not required to submit data to a national organization and pay certain fees as are commercial and certain other insurers. These other insurers pay an annual fee of up to several hundred thousand dollars to the National Council on Compensation.[1] Some insurers have concluded that paying this fee, while self-insured entities do not, places them at a competitive disadvantage.

Self-insured school districts accept greater financial risk than commercially insured districts and possibly districts in risk pools because self-insured retention amounts are generally higher than comparable deductible amounts.

Self-insurance also has potential costs. Self-insured school districts accept greater financial risk. This is evident by the higher self-insured retention amounts for self-insured districts compared to the lower deductible amounts for commercially insured districts. It is not uncommon for a self-insured district to retain responsibility for the first $100,000 in losses compared with $1,000 for a district that is commercially insured or in a risk pool. As a result, self-insured districts are at greater risk of underestimating insurance costs and budgeting fewer funds than necessary.

Self-insured school districts, particularly for workers' compensation, may not fully consider how long claim payments may continue, focusing instead on short-term cost savings.

School districts that self-insure workers' compensation may focus on short-term premium cost savings and not consider the accumulation of workers' compensation claim payments over time.

[1] The National Council on Compensation is an organization that gathers workers' compensation data from commercial insurers across the country, analyzes that data, and recommends state-specific workers' compensation rates.

Injured workers occasionally receive compensation for years. Expenses will continue to rise until the number or severity of new claims falls or claims from previous years are closed.

Comparison of Insurers

In this section, districts and insurance methods are compared based on the results of Program Review staff's survey of school districts. This analysis is limited to 1 year. It should also be noted that there are only four individually self-insured school districts.

School districts insured by commercial insurers and KSBIT were similar in types of insurances carried and payroll size.

KSBIT and Commercial Insurers. KSBIT members and commercially insured districts carried similar insurances. This included each of the insurance types examined in this report. KSBIT districts and commercially insured districts were also, on average, of equal size based on total payroll.

KSBIT districts typically had lower deductibles and were more likely to be located in southeastern Kentucky. Commercially insured districts tended to have higher deductibles and were more commonly located in western and eastern Kentucky.

Geographic representation generally differed. Southeastern Kentucky school districts predominately insured with KSBIT. Western and central Kentucky school districts more frequently reported insuring with a commercial insurer, typically Indiana Insurance.

The more notable differences in deductible and policy limits included the following:

1. Commercially insured school districts more frequently carried a deductible on their general liability policies than did KSBIT districts.

2. For property insurance, commercially insured districts typically reported higher deductibles than KSBIT districts—$2,500 or more compared with $1,000.

3. School district deductibles for vehicle collision and comprehensive insurances were nearly uniform at $1,000 for districts insured by KSBIT. Commercially insured districts' deductible amounts varied from $250 to $5,000.

4. Policy limits for vehicle liability were typically lower for commercially insured districts. Commercially insured districts more frequently reported vehicle liability policies with $1 million limits compared with $2 million limits for KSBIT districts.

These findings suggest that school districts with commercial insurance policies might bear slightly more financial risk than similar KSBIT districts. This is due to comparatively higher deductible amounts and lower policy limits on certain insurance policies.

Self-insured Districts. The primary difference between self-insured districts and those that insure through a commercial insurer or risk pool is the amount of risk retained. As noted by their high self-insured retention amounts, self-insured districts retain significantly greater financial risk than do other districts. Further analysis is limited by the fact that very few school districts self-insure.

Market Segmentation

In general, the Kentucky school insurance market is segmented. Different insurers underwrite school policies for each insurance type examined in this report.

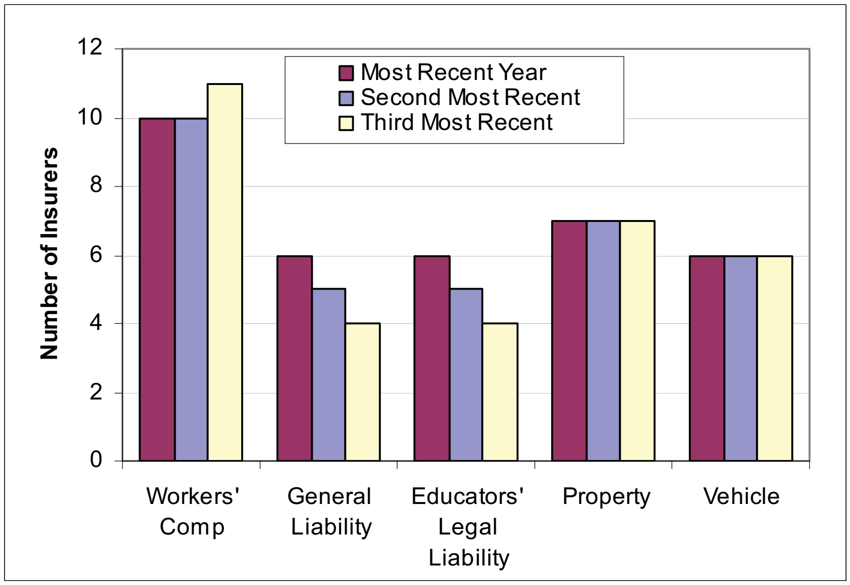
In general, relatively few insurers underwrite school policies for each of the insurance types examined in this report.

Figure 3.A identifies the number of insurers by each of five insurance types over the past 3 years. Liability insurance had the fewest insurers: between four to six insurers during the 3-year period surveyed. The numbers of insurers underwriting property and vehicle insurance were slightly higher, seven and six, respectively. Workers' compensation consistently had the most insurers, around 10.

The higher number of workers' compensation insurers may be partially explained by the relative ease of market entry. Several insurance officials interviewed by staff agreed that workers' compensation is the "easiest insurance line to get into and the hardest to get out of."

Ease of entry and exit among insurance lines may differ because workers' compensation payments usually begin relatively small but then accumulate over time as payments continue to claimants, potentially for years. This process—a slow buildup in an insurer's expenses—might encourage insurers to enter the workers' compensation market.

Figure 3.A
Number of Insurers of Kentucky School Districts
(By School Insurance Line and Year)



Note: The actual total number of insurers might be greater.
Source: Program Review staff's analysis of school district survey; the number of responses ranged from 77 to 94.

Insurers frequently enter and exit the Kentucky school insurance market. For example, between 2001 and 2006, 53 different insurers provided workers' compensation policies, yet there were no more than 11 insurers in any of the past 3 years.

Workers' compensation insurers must pay claims until the injured worker returns to work, benefits are exhausted, or the claim is assumed by another insurer. Even if the insured school district switches to a different insurer, responsibility for paying claims incurred during the previous insurer's contract period remains with that insurer. This phenomenon is evident in the number of insurers paying benefits compared to the number of insurers actively providing coverage. Based on Office of Workers' Claims data, 53 different insurers paid workers' compensation benefits on behalf of school districts between 2001 and 2006. However, there were no more than 11 insurers in any of the past 3 years.

Market Concentration

The Kentucky school insurance market is dominated by Indiana Insurance and KSBIT. These two collectively insure most Kentucky school districts across all insurance lines.

Table 3.1 shows the percentage of school districts insured for each insurance line by either KSBIT or Indiana Insurance. These figures reflect school district responses to Program Review staff's survey. With the exception of workers' compensation, Indiana Insurance and KSBIT insured approximately the same percentage of districts.

Table 3.1
Percentage of School Districts Insured by KSBIT or Indiana Insurance
(By Insurance Line for the Most Recent Year)

	Percent of Districts Insured by	
Insurance	**Indiana Insurance**	**KSBIT**
Workers' Compensation	19%	37%
General Liability	38%	38%
Educators' Legal Liability	35%	39%
Property	40%	33%
Vehicle	40%	33%

Source: Program Review staff's analysis of school district survey; 105 respondents.

Because all school districts did not respond to the survey, Program Review staff asked officials from Indiana Insurance and KSBIT to provide a complete list of districts that each insured. The Kentucky School Boards Insurance Trust replied. According to its data, the total number of districts insured by KSBIT during the last insurance year was 90 for workers' compensation insurance, 106 for general liability insurance, 90 for property insurance, and 97 for vehicle insurance. KSBIT provided insurance to more than one-half of Kentucky school districts.

Based on Program Review staff's survey, at least two-thirds of school districts purchase insurance policies from either KSBIT or Indiana Insurance.

Indiana Insurance did not indicate which school districts it insured. Officials from Indiana Insurance did declare their share of the Kentucky school insurance market to be about 45 percent. Because Program Review staff could not specifically identify those school districts, only districts that responded to the survey and that listed Indiana Insurance as their insurer were tallied for Indiana Insurance. Despite this limitation, staff determined that at least two-thirds of school districts purchase school insurance from either Indiana Insurance or KSBIT.

Eighteen school districts purchased certain insurances exclusively from Indiana Insurance and 19 purchased from KSBIT.

Many school districts purchased insurance exclusively from either Indiana Insurance or KSBIT. Based on Program Review staff's survey, 18 school districts purchased workers' compensation, general liability, educators' legal liability, property, and auto liability insurances from Indiana Insurance, and 19 school districts purchased those insurances from KSBIT during the latest insurance year. Only one other insurer, Netherlands Insurance, had even one school district purchase all insurances from it.

For some school districts, Indiana Insurance's and KSBIT's ability to underwrite all their insurance needs is attractive. Several school district officials noted their preference for maintaining an insurance relationship with one insurer rather than dealing with multiple insurers. Using one insurer generally means the school district has one insurance agent. Such districts might also only receive one bill.

Insurance Agents

Insurance agents are the local point of contact for school districts.

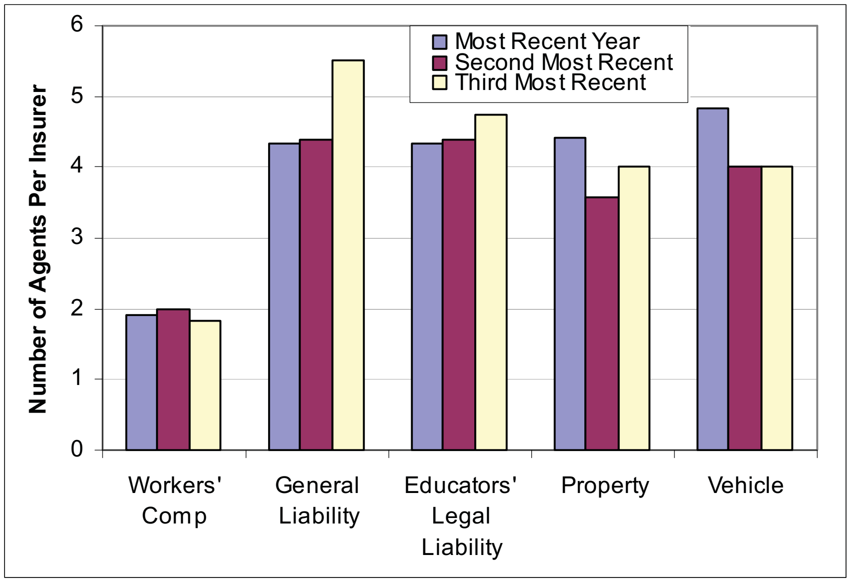
School districts generally purchase insurance through a local insurance agent or broker. Local insurance agents and brokers can represent state, regional, or national insurers. While insurers provide the actual coverage, insurance agents and brokers are the local point of contact for school districts.

The number of local insurance agents should not usually affect a school district's insurance costs. Insurance company underwriters should arrive at the same premium figure for each agent. According to officials from insurance companies and school districts, local insurance agents can compete by being more responsive or providing additional services, for example.

According to survey responses, the number of insurance agents providing school insurance policies varies by insurance line and year. Figure 3.B shows the number of insurance agents per insurer.

Overall, multiple insurance agents sell the same insurance line for the same insurer. For workers' compensation, there were approximately two insurance agents per insurer. For liability, property, and vehicle school insurances, the ratio of agents to insurers was generally 4 to 1. This difference was due to a lower number of workers' compensation agents and a higher number of workers' compensation insurers relative to the other insurance lines.

Figure 3.B
Number of Insurance Agents Per Insurer
(By School Insurance Line and Year)



Note: The actual total number of insurers might be greater.
Source: Program Review staff's analysis of school district survey.

Insurance Selection Process

Regardless of insurer or agent, every school district follows an insurance selection process, which varies by district.

Frequency of Bids

School districts solicit insurance bids at different intervals. The time between bid solicitations is largely due to local choice. Multiyear arrangements limit the amount of time staff devote annually to requesting and evaluating insurance bids. Shorter-term contracts may allow districts to capture premium reductions.

School districts solicit insurance bids at different intervals. For example, the Jefferson County school district requests bids every 4 years; Taylor County asks for insurance bids every 3 years; Covington Independent school district solicits bids every year.

Based on Program Review staff's interviews, the time between bid solicitations is usually due to local choice. Multiyear rate arrangements are preferred by some school districts because that limits the amount of time district staff devote annually to requesting and evaluating insurance bids. To protect a district from unanticipated future premium increases, long-term arrangements usually cap annual percentage increases. Should the increase exceed the cap, a school district can solicit other bids.

Other districts prefer more frequent bids. One advantage is the ability to capture premium reductions occurring in the market. One potential disadvantage is the annual commitment of staff resources to requesting and evaluating bids.

Insurers generally prefer long-term agreements. Locking in school districts can limit an insurer's expenses. Insurers interviewed by Program Review staff also noted that longer-term arrangements create a closer working relationship with school districts. As a result, an insurer might be better able to match a school district's insurance needs with an insurer's products and services.

Selection Methods

School districts use different methods to select insurance, including contacting an insurer or agent or soliciting bids.

When school districts do solicit insurance bids, they tend to use different methods. Advertising, contacting an insurance agent, or contacting an insurer predominated. Between one-half and three-fifths of survey respondents reported using one of these methods. School districts were most likely to contact an insurer for general and educators' legal liability insurances. Table 3.2 details these survey findings.

Table 3.2
Percentage of School Districts Using Each Bid Solicitation Method (Most Recent Year)

Solicitation Type	Workers' Compensation	General Liability	Educators' Legal Liability	Property	Vehicle
Advertised only	19	19	19	23	22
Contacted agent only	16	12	14	17	17
Contacted insurer only	19	26	26	19	22
Negotiated or renewed existing contract only	10	9	7	9	8
Multiple solicitation types	10	9	9	8	7
Other/Educational co-ops	10	11	8	8	9
No response	15	14	18	17	16
Total	100%	100%	100%	100%	100%

Note: Due to rounding, figures may not total 100 percent.
Source: Program Review staff's analysis of school district survey; 105 respondents.

Depending on the type of insurance, only 7 percent to 10 percent of school districts solicited bids using multiple methods. Similar percentages of school districts reported that they negotiated or renewed their contract with the current insurer.

Some school districts use educational co-ops to solicit, compile, and evaluate insurance bids. Educational co-ops are organizations that pool participating school districts' purchasing functions. For many purchases, such as office supplies, educational co-ops receive bulk discounts, which they pass along to school districts.

School districts that use educational co-ops for soliciting insurance bids do not receive discounts. Insurers individually rate school districts. This means that insurers create separate bids for each district in the educational co-op. Individual school districts then make the final decision on which bid to accept.

Concerns

School district officials seemed unclear about which, if any, insurance types had to be bid or how frequently.

Based on interviews conducted by Program Review staff, some school district officials were unclear about which, if any, insurance types had to be bid or how frequently. Much of the confusion is about the Model Procurement Code, which establishes that certain contracts valued at greater than $20,000 must be competitively bid. School district officials were not always certain which, if any, insurance types this applied to. School district officials also stated that they may purchase insurance through direct negotiation. Due to these different interpretations, the Department of Education should provide school district officials with a guide to the school insurance selection process, including how districts should procure insurance services.

Recommendation 3.1

The Kentucky Department of Education should make available to school districts a document identifying how districts should procure insurance services.

Chapter 4

Regulation and Review of School Insurance

Introduction

This chapter explains how insurers are regulated and how various fiscal and policy concerns have subsequently arisen. Within this context, the Kentucky School Boards Insurance Trust is also analyzed.

The chapter begins by describing the regulatory process for self-insured school districts. Particular concerns with self-insured districts' financial stability are then discussed. The following two sections examine the regulatory process for commercial and risk pool insurers and then examine the Kentucky School Boards Insurance Trust. The chapter concludes by examining state guaranty funds.

Regulation of Self-insured Districts

Self-insured school districts maintain primary responsibility for paying claims. They typically carry high out-of-pocket limits, known as self-insured retentions, and rely on reinsurers to limit their financial exposure.

Four school districts are known to self-insure workers' compensation, one district self-insures its property, and two districts self-insure their auto property.

As defined in this report, self-insurance only refers to individual school districts—not districts grouped by risk pools. Using this standard, four school districts are known to self-insure workers' compensation, one district self-insures its property, and two districts self-insure their auto property.

Districts that self-insure their property do not fall under any particular state agency's regulatory jurisdiction, but districts that individually self-insure workers' compensation are regulated by the Kentucky Department of Labor's Office of Workers' Claims. This office also administers the overall workers' compensation program, which includes processing all claims.

School districts that want to individually self-insure their workers' compensation risks apply to the Office of Workers' Claims. Before approving a self-insurance application, the office reviews a district's audited financial statements and conducts a financial analysis. It also determines whether a district has at least

$10 million in net assets. This process helps measure a school district's ability to pay workers' compensation claims.

The Office of Workers' Claims regulates school districts that individually self-insure workers' compensation.

Officials from the Office of Workers' Claims contact the Kentucky Department of Education when school districts apply to self-insure. Although KDE has no formal role, the Office of Workers' Claims seeks its input, particularly about districts' operational efficacy and unrestricted fund balances, which are important indicators of an applicant's financial stability.

Unrestricted fund balances are budgeted amounts set aside for unanticipated expenditures in a district's budget. Every Kentucky public school district is statutorily required to maintain a minimum 2 percent unrestricted fund balance (KRS 160.470).

School districts with unrestricted fund balances of less than 2 percent, but greater than 0, are placed on a KDE watch list. Low reserves can indicate financial difficulty, so the department notifies the Office of Workers' Claims whenever a self-insured district is on this list.

Financial Stability/Surety Bonds

A surety bond ensures workers' compensation claimants will receive benefits should a self-insured school district no longer be able to pay such claims. Legislation enacted in 2007 eliminated a surety bond requirement for school districts.

Until 2007, the Office of Workers' Claims required school districts to retain a surety bond equal to the amount of their workers' compensation claims, both incurred and incurred but not reported.[1] A surety bond ensures workers' compensation claimants will receive benefits should a self-insured school district no longer be able to pay such claims.

House Bill 296, enacted in 2007, eliminated this requirement. State regulatory officials have since expressed concern that self-insured school districts might maintain insufficient reserves to meet current and future claims expenses.

Although the surety bond requirement has been repealed, debate over its efficacy remains. Some school district officials reported that repealing the surety bond requirement was appropriate. They identified three primary reasons. First, as public entities, school districts have an ability to raise taxes. Proponents of repealing the surety bond suggest that higher taxes could be used to pay workers' compensation claims that exceed a district's current ability to pay. Second, some school district officials cited the

[1] A school district pays a fee to a surety bond provider in exchange for the provider assuming a predetermined amount of financial risk should the district become unable to meet the financial obligation guaranteed by the surety bond.

2 percent unrestricted fund balance requirement as evidence of their financial ability to pay unanticipated claims. Unrestricted fund balances, they claimed, can be used if workers' compensation claims exceed budgeted amounts. Third, self-insured school districts annually reserve money separate from their unrestricted fund balance to pay workers' compensation claims.

State regulatory officials and some insurance industry officials contend that taxing authority, unrestricted fund balances, and reserve funds provide insufficient or uncertain financial security for self-insured districts. Increased taxes are limited by school districts' ability and willingness to levy them and may also be affected by a state statute that subjects property tax increases of greater than 4 percent to a potential recall. Unrestricted funds are not required to be used to pay workers' compensation claims. By definition, "unrestricted" means these funds can pay for any necessary expenditure. Lastly, unless a district reserves funds for all current and future claims, as had been required with the surety bond, it is possible that a catastrophic event could place a district's workers' compensation payments in jeopardy.

Regulation of Commercial Insurers and Risk Pools

The Office of Insurance regulates commercial insurers and risk pools.

Commercial insurers and risk pools underwrite similar insurance lines and both are regulated by the Office of Insurance.

Regulation

According to the Office of Insurance, the process by which commercial insurers and risk pools are regulated is generally the same. It includes performing a financial analysis, conducting a financial examination, and holding meetings with management.

Property and Liability Risk Pools. Each group that wants to form a property and liability risk pool must file an application with the executive director of the Kentucky Office of Insurance for a license to operate in Kentucky (KRS 304.48-040). The office then examines the financial condition, affairs, and management of the group (KRS 304.48-110).

Risk pools must also comply with state statute and provide each member of the group with written evidence of coverage (KRS 304.48-200). This includes terms, conditions, and exclusions.

In Kentucky, five risk pools offer property and liability insurance.

According to Office of Insurance staff, five Kentucky risk pools offer property and liability insurance: Kentucky School Boards Insurance Trust, Kentucky Association of Counties, Kentucky League of Cities, Louisville Area Governmental Self-Insurance Trust, and Kentucky Housing Authority.

Workers' Compensation Risk Pools. In 2004, Executive Order 2004-835 transferred responsibility for overseeing workers' compensation risk pools from the Office of Workers' Claims to the Office of Insurance. Prior to that transfer, one of the largest collapses in Kentucky insurance history occurred: Associated Industries of Kentucky.

State statute now sets minimum financial standards for workers' compensation risk pools (KRS 304.50). The purpose is to ensure that these pools can provide adequate financial coverage for member employers' risks and liabilities.

In Kentucky, seven risk pools offer workers' compensation insurance.

According to Office of Insurance staff, there are seven workers' compensation risk pools in Kentucky: Kentucky School Boards Insurance Trust, Kentucky Association of Counties, Kentucky League of Cities, Kentucky Associated General Contractors, Kentucky Employers Safety Association, Kentucky Forest Industries Association, and Kentucky Retail Federation.

KSBIT's unemployment insurance fund is not directly regulated by any state agency.

Unemployment Insurance. The Kentucky School Boards Insurance Trust's unemployment insurance fund is not regulated by the Office of Insurance or any other state agency. One likely reason is because KSBIT does not assume any risk. School districts participating in KSBIT's unemployment insurance fund bear full financial responsibility for paying their own claims. The trust is an intermediary. In exchange for an administrative fee of 11.3 percent of district contributions, KSBIT reimburses the state unemployment insurance fund on a quarterly basis for claims to individual school district accounts. Appendix B has more detail on school districts' participation in KSBIT's unemployment insurance fund.

Accounting Standards

Commercial insurers and risk pools report accounting information differently to the Office of Insurance.[2] Commercial insurers are held to higher solvency and capital requirements than are risk pools. Further, commercial insurers must show that they have sufficient financial resources to pay all claims should they stop operating that day.

Although the ways in which risk pools and commercial insurers report accounting information differ, the Office of Insurance indicated that neither method is necessarily better. The regulatory process is similar for both types of insurers.

Kentucky School Boards Insurance Trust

This section briefly describes the origins of KSBIT. Following sections describe several financial characteristics of KSBIT, including an examination of its two deficit funds. A report by the Office of Insurance expected in fall 2007 may provide a more formal review of KSBIT's two deficit funds.

The Kentucky School Boards Association was established in 1936 as a private, nonprofit service organization representing local boards of education. All local school boards in Kentucky are represented by the association. Twenty-seven local school board members serve on the association's board of directors.

The Kentucky School Boards Insurance Trust was created in 1978.

In 1978, the Kentucky School Boards Association created the Kentucky School Boards Insurance Trust. According to association officials, the trust was created during a period of high premiums and limited insurance availability for Kentucky school districts.

Until 2007, KSBIT operated four funds: workers' compensation, property, liability, and unemployment insurance. At that time, the property and liability funds were combined.

Until July 2007, KSBIT operated four separate insurance funds: workers' compensation, unemployment insurance, property, and liability. KSBIT merged its property and liability funds and today operates three funds. The property and liability funds, however, will be considered separately in this report because the combined property and liability fund is too new for useful analysis.

[2] Commercial insurers apply statutory accounting principles; risk pools use generally accepted accounting principles. Public entity risk pools also follow standards established by the Government Accounting Standards Board.

Each KSBIT fund assesses its own premium and maintains its own membership.

Each KSBIT fund assesses its own premium and maintains its own membership. Kentucky public school districts are the primary participants in each fund.

Based on Program Review staff's interviews with school district officials, regulators, and insurance agents, KSBIT's current administrators have been generally credited with improving the trust's financial management.

Following the reports of deficits in the workers' compensation and liability insurance funds, management changed at KSBIT. Based on Program Review staff's interviews with school district officials, regulators, and insurance agents, current administrators have been generally credited with improving the financial management of KSBIT's insurance funds, particularly underwriting and claims management processes.

Financial Analysis

The Kentucky School Boards Insurance Trust's workers' compensation, liability, and property funds merit particular attention. Most Kentucky school districts participate in one or more of these funds. Participating districts share potential financial liability through joint and several liability. Unlike insurance policies purchased from a commercial insurer, school districts participating in a risk pool with joint and several liability can be assessed should the pool encounter severe financial difficulties.[3]

Net assets indicate how well a business is doing by showing the difference between assets and liabilities. Two of KSBIT's funds had negative net assets, or a deficit.

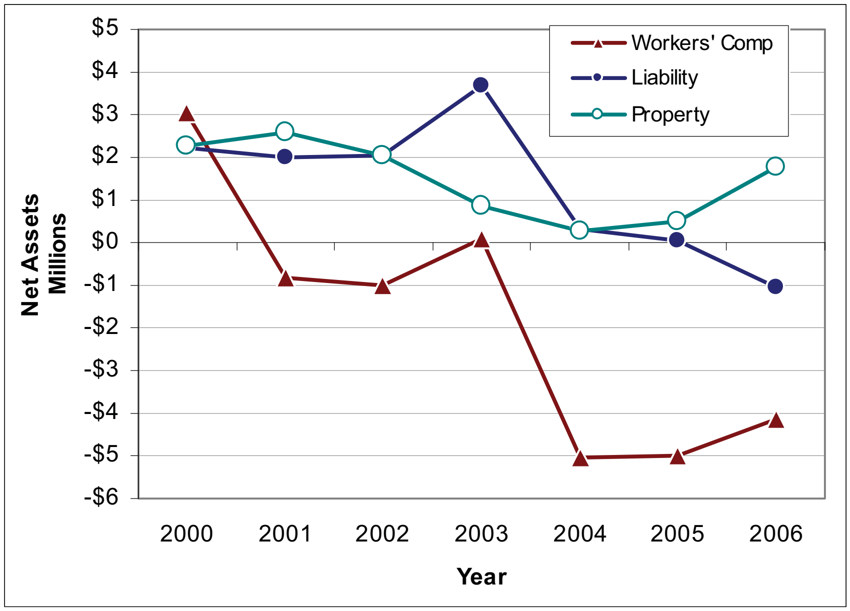
Net Assets. Net assets indicate how well a business is doing by showing the difference between assets and liabilities. Assets are those items that are owned or owed to an insurer. For example, premiums owed to an insurer would be an asset. Liabilities are items that an insurer owes or is obligated to pay. For example, a workers' compensation claim is a liability.

Positive net assets mean an insurer's assets exceed its liabilities. Negative net assets mean liabilities exceed assets. Negative assets, in this report, are considered a deficit.

[3] Unemployment insurance is not described in the following section because technically it is not an insurance fund.

Figure 4.A shows net assets for each of KSBIT's funds from 2000 to 2006. For each fund, net assets were lower in 2005 than they were in 2000. Due to a transfer from the liability fund to the workers' compensation fund in 2003, net assets for the liability fund are somewhat worse, and net assets for workers' compensation are slightly better.

Figure 4.A
Net Assets Per KSBIT Fund, 2000-2006



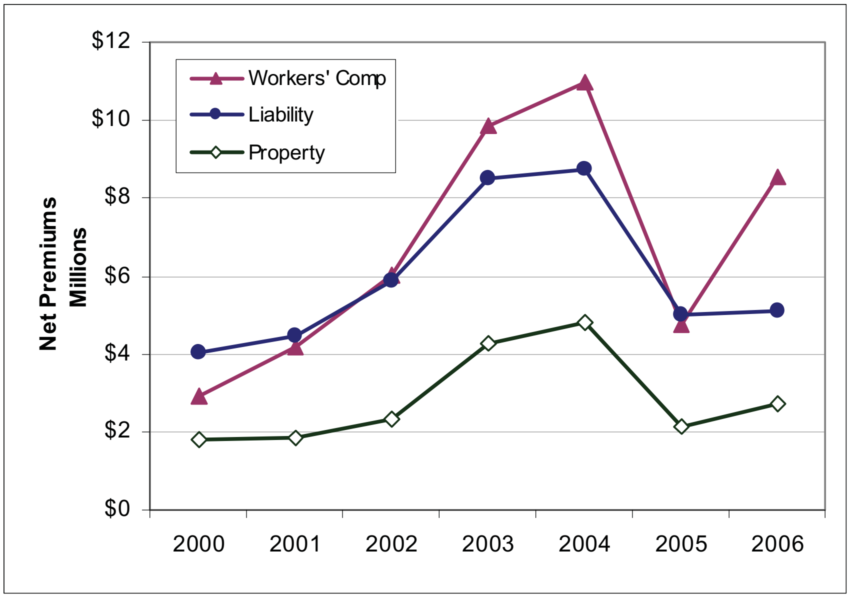
Source: Program Review staff's analysis of KSBIT's financial statements, various years.

Net annual premiums represent the premium amount available to pay losses after paying agent or broker commissions. Net premiums for each of KSBIT's funds generally grew between 2000 and 2006.

Net Annual Premiums. Net annual premiums generally represent the premium amount available to pay losses after paying agent or broker commissions. As Figure 4.B shows, net annual premiums for each of KSBIT's funds generally grew between 2000 and 2006, but some experienced a significant drop along the way.[4]

Still, net premiums in 2006 remained below the 2004 amount. Declining numbers of school districts likely contributed to this.

Figure 4.B
Net Premiums Per KSBIT Fund, 2000-2006



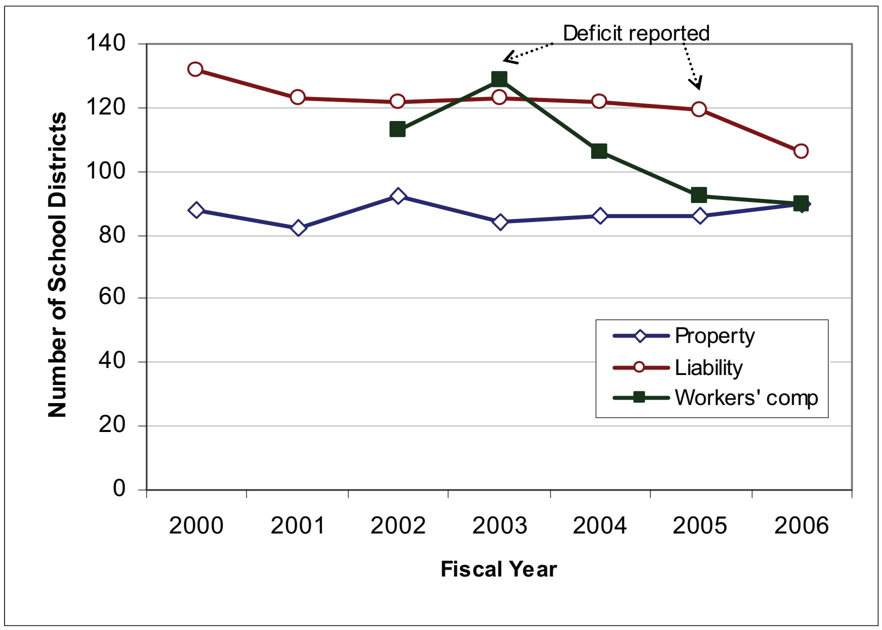
Note: Property fund data for 2003 to 2005, according to the Kentucky School Boards Association, reflect gross premium revenue.
Source: Program Review staff's analysis of KSBIT's financial statements, various years.

[4] Workers' compensation net premiums dipped between 2004 and 2005 because only 6 months of net premiums were reported in 2005. This is because KSBIT changed the workers' compensation fund's fiscal year. KSBIT's other funds had a July through June fiscal year. The workers' compensation fund had a January to December fiscal year. To get all funds on the same fiscal year, the workers' compensation fund's 2005 fiscal year lasted only from January to June.

The number of school districts insured by KSBIT's funds has declined since 2000.

Number Insured. As shown in Figure 4.C, the number of school districts insured by KSBIT's funds has declined since 2000. The Kentucky School Boards Insurance Trust's liability and workers' compensation funds had the most significant changes. For the liability fund, the number of insured school districts fell from 132 in 2000 to 106 in 2006. School districts insured by KSBIT's workers' compensation fund went from 113 in 2002 to 90 in 2006.[5] The number of school districts insured by the property fund remained relatively constant.

Figure 4.C
Number of School Districts Insured by KSBIT
Per Fund and Year, 2000-2006



Source: Program Review staff's analysis of data provided by KSBIT.

Negative net assets appear to lead to a drop in the number of insured districts. In 2004, the year after the workers' compensation fund reported a $5 million deficit, 33 school districts left the trust's workers' compensation fund.

Changes in the number of insured school districts appear related to KSBIT's financial condition. Whenever a KSBIT fund reported negative net assets (a deficit), the number of insured school districts dropped noticeably the following year. For example, 13 fewer school districts participated in KSBIT's liability fund the year after a deficit was reported in 2005.

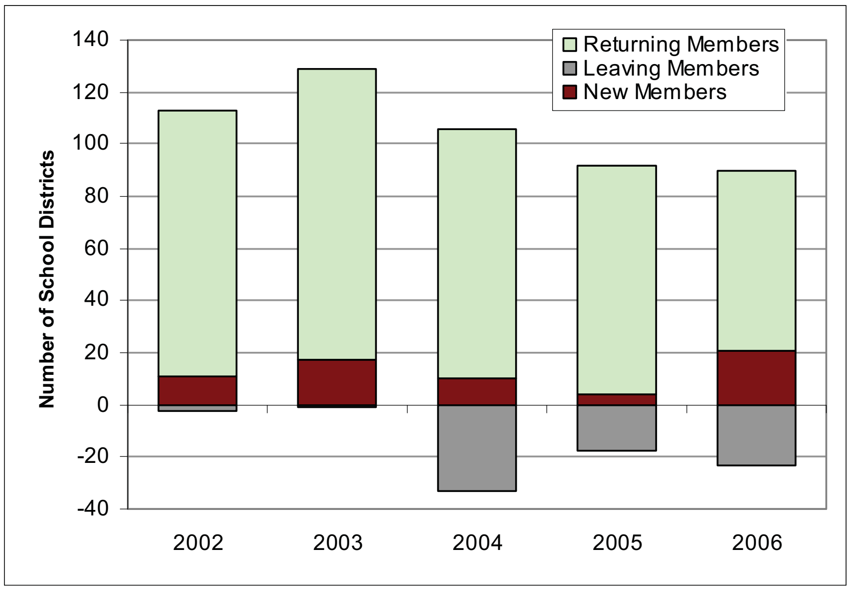
For the workers' compensation fund, participation fluctuated annually along with that fund's financial condition. The number of insured school districts peaked at 129 in 2003. At that time, the workers' compensation fund reported low, but positive, net assets.

[5] KSBIT did not provide data for years prior to 2002, in part, because officials have some concerns about the validity of that data.

By 2005, the number of insured school districts fell to 92, while net assets fell to negative $5 million.

Figure 4.D shows the number of leaving, new, and returning school districts in KSBIT's workers' compensation fund between 2002 and 2006. In 2004, the year after the worker's compensation fund reported a $5 million deficit, 33 school districts left KSBIT's workers' compensation fund, while only 10 new school districts were insured.

Figure 4.D
Membership Changes in KSBIT's Workers' Compensation Fund, 2002-2006



Source: Program Review staff's analysis of data provided by KSBIT.

Movement. Within each fund and across fiscal years, the mix of school districts purchasing insurance from KSBIT usually varies. School districts frequently move into and out of KSBIT's insurance funds. For example, one year a school district might purchase property insurance through KSBIT and the next year from another insurer.

Movement into and out of KSBIT's funds happens without restriction.

Movement into and out of KSBIT's funds is not restricted. The trust imposes no penalties and assesses no fees for entering any of its funds.[6] Similar organizations in some states charge entrance fees or contractually obligate school districts to remain with them for a certain period of time.

[6] An upfront "fee" is imposed on school districts that participate in KSBIT's unemployment insurance fund. This fee is used to pay initial, and potentially continuing, unemployment insurance claims.

Movement out of KSBIT does not absolve school districts from potential financial obligations should a fund become insolvent.

Movement out of KSBIT does not absolve school districts from potential financial obligations should the KSBIT fund that insured the district become insolvent. Joint and several liability binds all insured districts together to ensure payment of all current and future claims.

Other Issues

Two particular financial actions by KSBIT merit attention. First, KSBIT used money from its unemployment insurance fund to shore up its workers' compensation fund. Second, KSBIT appears to pay a disproportionate amount of the Kentucky School Boards Association's expenses.

During the course of this study, Program Review staff discovered two particular financial actions by KSBIT that merit attention. Staff disclosed these actions to the Office of Insurance. A report from that office in fall 2007 may address these issues.

First, KSBIT used money from its unemployment insurance fund to shore up its workers' compensation fund. Second, KSBIT appears to pay a disproportionate amount of the Kentucky School Boards Association's expenses.

KSBIT created a guaranty fund in 2004 to assist any of its funds that experienced financial difficulty. Funds were transferred from its property, liability, and unemployment insurance funds to its workers' compensation fund.

Unemployment Insurance Transfer. Just prior to the Office of Insurance reporting a $5 million deficit in KSBIT's workers' compensation fund in 2004, the trust's board of trustees established a guaranty fund.[7] The guaranty fund, as noted in KSBIT's financial statements, was created to assist any of its funds that experienced financial difficulty.

Considering the circumstances, it is clear that the guaranty fund was established to assist KSBIT's workers' compensation fund. Money was pooled from the trust's property, liability, and unemployment insurance funds but not from workers' compensation.[8] Almost $2.8 million was then transferred from the guaranty fund to the workers' compensation fund.

Although KSBIT's board of trustees approved these transfers, it is questionable whether funds should have been transferred from the unemployment insurance fund. The unemployment insurance fund is not a risk-bearing account. School districts retain full responsibility for paying their own claims, and their contributions do not pay for other districts' claims. KSBIT's primary role is remitting quarterly payments to the state unemployment insurance fund for benefit payments incurred. Consequently, all money in

[7] According to KSBIT officials, that guaranty fund has since been closed.

[8] The transfer amounts were property, $280,521; liability, $1,232,220; and unemployment insurance, $1,590,729. Funds transferred from the property fund were subsequently returned.

KSBIT's unemployment insurance fund belongs to participating school districts until benefit payments are made.

Transferring money from the unemployment insurance fund to the workers' compensation fund benefited some districts but not others.

Transferring money from the unemployment insurance fund to the workers' compensation fund benefited some districts but not others. For instance, school districts participating in the workers' compensation fund but not the unemployment insurance fund benefited because they did not directly contribute to the transfer.

School districts participating in the unemployment insurance fund but not the workers' compensation fund were worse off. Money was transferred from the unemployment insurance fund without any direct financial benefit accruing to them. Similar advantages and disadvantages apply to districts participating in both funds.

Recommendation 4.1

Should the Kentucky School Boards Insurance Trust recreate its guaranty fund or establish a similar fund, it should do so only after providing all affected school districts with written notification.

Some expenses, such as utilities, property taxes, property insurance, and building maintenance, are directly allocated only to the KSBIT program.

Allocation of Expenses. The Kentucky School Boards Association operates 19 programs, of which KSBIT is one. Based on the association's financial statements, expenses are allocated to each program. For example, salaries are allocated based on the projected amount of staff time spent in each program. Some expenses, such as utilities, property taxes, property insurance, and building maintenance, are directly allocated only to the KSBIT program.[9] According to Kentucky School Boards Association officials, these expenses are not allocated to the other 18 programs because doing so would dilute the accuracy of those programs' income statements. Those expenses instead appear under the administration category on the association's financial statements.

The Government Finance Officers Association recommends that the full cost of services, which include direct and indirect costs, be calculated ("Measuring"). The association notes the usefulness of this practice in organizational decision making, although cost may not be the only measure by which programs are evaluated.

[9] For 2006, these and other similar expenses totaled $223,000.

Ideally, the Kentucky School Boards Association should allocate expenses by category to each of its programs based on some proportionate measure.

Ideally, the Kentucky School Boards Association should allocate expenses to each of its programs based on some proportionate measure. This is what the association does with personnel costs. A similar method should be used to allocate other program expenses.

Recommendation 4.2

The Kentucky School Boards Association should consider developing a method by which program expenses are proportionately allocated to the Kentucky School Boards Insurance Trust and other programs.

Other State Funds

The final section in this chapter highlights state funds created to help insured entities that encounter financial difficulty.[10]

Emergency Revolving School Loan Fund Account

Certain public school districts that lose physical facilities due to fire or natural disaster are eligible for a loan from the state's Emergency Revolving School Loan Fund Account.

Repairing or replacing school buildings can be expensive. Even with insurance, school districts might end up bearing some costs. When that happens, districts must either appropriate funds from within their budgets or raise additional funds. School districts may also access a limited amount of state money.

Certain public school districts that lose physical facilities due to fire or natural disaster are eligible for a loan from the state's Emergency Revolving School Loan Fund Account (KRS 160.599 and 702 KAR 4:100). Created in 1974, this account provides loans to school districts with insufficient property insurance and no practical ability to incur additional debt. The fund operates as a revolving loan account. Loan repayments go back to the fund, where they may be loaned to other school districts as needed.

Loans from the Emergency Revolving School Loan Fund Account must first be approved by the Kentucky Board of Education upon recommendation from the chief state school officer. The maximum loan amount is $250,000. The maximum term is 10 years.

[10] Another program, broadly termed "Guaranty Trust Funds," does not apply to school districts. After the collapse of Associated Industries of Kentucky, the General Assembly passed legislation creating three separate workers' compensation guaranty trust funds (KRS 342.900). Each trust's purpose was to ensure workers' compensation payments to certain claimants if a self-insured or risk pool entity became insolvent. Public-sector risk pools and employers were specifically exempted from participating in those funds (KRS 304.904).

According to data from the Kentucky Department of Education, the most recent loans occurred in the 1990s. At that time, seven school districts received loans: Berea Independent, Clinton County, Floyd County, Fulton County, Harrison County, Johnson County, and McLean County. Loan amounts varied. Each loan was repaid by 2001.

Kentucky Insurance Guaranty Association

The Kentucky Insurance Guaranty Association provides for the payment of certain claims due to an insurer's insolvency.

The Kentucky Insurance Guaranty Association provides for the payment of certain claims due to an insurer's insolvency (KRS 304.36-030 and KRS 304.36-110). This does not apply to workers' compensation insurers or to districts with assets of at least $25 million. Because most school districts have assets in excess of this amount, most payments are not covered by this association. Similarly, KSBIT is not covered.

Works Cited

Commonwealth of Kentucky. Legislative Research Commission. Program Review and Investigations Committee. *Kentucky Association of Counties Self-Insurance and Loan Programs*. Research Report No. 271. Frankfort: LRC, 1994.

---. ---. Office of Education Accountability. *A Review of the School Facilities Construction Commission.* Research Report No. 332. Frankfort: LRC, 2006.

Government Finance Officers Association. "Measuring the Cost of Government Service." 2002. <http://www.gfoa.org/downloads/MeasuringtheCostofGovernmentService.pdf> (accessed: Sept. 6, 2007).

Kollie, Ellen. "Want to Save Big Money on Insurance?" *School Planning and Management* 44 (Feb. 2005): 18-24.

Moody, Michael J. "Self-Insurance: An 'Old Standby' Deserves Consideration." *Rough Notes* 149 (Dec. 2006): 28-29.

National School Boards Association. "Federation Member Entrepreneurial Activities." Fax to Rick Graycarek. Aug. 22, 2007.

Pumford, Harold. "RGraycarek-PPT." Email to Rick Graycarek. Aug. 20, 2007.

Randall, David. "Betting on Self-Insurance." *American City & County* 107 (June 1992): 16.

Riley, Claudette. "Lawmakers Want Tighter Rein on School Boards Lobby." *The Tennessean*. Jan. 17, 2006.

Rosenthal, Samuel "Self-Insurance Pools: Fantasy or Reality?" *School Business Affairs* 53 (June 1987): 28-30.

Young, Peter C., and B.J. Reed. "Government Risk-Financing Pools: An Assessment of Current Practices." *Public Budgeting & Finance* 15 (Spring 1995): 96.

Young, Peter C. and Martin Fone. "Pooling: Faced With Increased Competition and Pressure to Diversify, Pooling is Entering a New Era." *Public Risk*. Oct. 1996.

Young, Peter C. "Pooling! The Real Debate." *Public Risk*. July 1998.

Appendix A

School District Insurance Survey

This is the online questionnaire that was distributed to school districts.

The Kentucky General Assembly's Program Review and Investigations Committee is conducting a study of certain school district insurances. As part of the study, a survey is being sent to every Kentucky school district. The survey asks questions about workers' compensation, general liability, educators' legal liability, property, and vehicle insurances. Short sections on excess/umbrella coverage, student accident and activity insurances, and risk management activities are also included. *Your response will help provide the most current and detailed description of school district insurance in Kentucky*.

To complete this survey we suggest that you have policy information readily accessible for each of the insurance types mentioned for the three most recent years. This information should include policy dates, premium, deductible, and coverage amounts, and bid information. We estimate that it will take between two and three hours to complete this survey.

Instructions

- Answer Questions 1 thru 10. (Additional explanation for some questions is available by left-clicking the text.)
- To print your responses for your records, click "**Print**" at the bottom of the survey. (Then select "landscape" format from your printer's preference menu.)
- Submit your responses by clicking "**Submit**" at the bottom of the survey. (If you receive an error message, our server may be busy. In that event, click the "Back" button on your browser, wait a few minutes, and then click "**Submit**" again.)
- We would appreciate your response by June 14, 2007.

We look forward to receiving your response.

---

1. School district ______ District 3-Digit Number ______

2. Name of person completing this survey ______

Questions 3-7

The following questions request information specific to workers' compensation, general liability, educators' legal liability, property, and vehicle/fleet insurances carried by your district.

3. Workers' Compensation

	Current Policy Year	**Previous Policy Year**	**Prior Policy Year**
Coverage Period (Mo/Day/Yr)	From	From	From
	To	To	To
Agency/Brokerage Name			
Insurer's Name			
Net Annual Premium			
Annual Deductible			
Coverage Limit			
-- Per Claim			
-- Aggregate			
Number of Reported Claims (Include all reports filed with the school district, even those that did not result in a workers' compensation claim.)			
Total Annual Payroll (Enter the final audited annual payroll amount for your school district. The audited amount is used by your district's workers' compensation insurer to calculate your premium.)			

Comments			
Quote/Bid Process			
For the most recent applicable year, how did the district solicit workers' compensation insurance coverage? *(To make multiple selections, press and hold the "Ctrl" button on your keyboard and then left click each item that applies.)*		Advertised Contacted insurer Contacted insurance agent Used consultant Other	If "Other", please specify.
How many quotes/bids were received?			
Please list the names of insurers that submitted a quote or bid.			

4. General Liability

	Current Policy Year	Previous Policy Year	Prior Policy Year
Coverage Period (Mo/Day/Yr)	From	From	From
	To	To	To
Agency/Brokerage Name			
Insurer's Name			
Annual Premium			
Annual Deductible			
Coverage Limit			
-- Per Claim			
-- Aggregate			
Does your current liability insurance policy include coverage for acts of violence on school grounds?			
Does your current liability insurance policy include coverage for sexual misconduct and molestation?			
Comments			
Quote/Bid Process			
For the most recent applicable year, how did the district solicit general liability insurance coverage? *(To make multiple selections, press and hold the "Ctrl" button on your keyboard and then left click each item that applies.)*		Advertised Contacted insurer Contacted insurance agent Used consultant Other	If "Other", please specify.
How many quotes/bids were received?			

5. Educators' Legal Liability

	Current Policy Year	Previous Policy Year	Prior Policy Year
Coverage Period (Mo/Day/Yr)	From	From	From
	To	To	To
Agency/Brokerage Name			
Insurer's Name			
Annual Premium			
Annual Deductible			
Coverage Limit			
-- Per Claim			
-- Aggregate			
Comments			
Quote/Bid Process			
For the most recent applicable year, how did the district solicit educators' legal liability insurance coverage? *(To make multiple selections, press and hold the "Ctrl" button on your keyboard and then left click each item that applies.)*		Advertised Contacted insurer Contacted insurance agent Used consultant Other	If "Other", please specify.
How many quotes/bids were received?			
Please list the names of insurers that submitted a quote or bid.			

6. Property

	Current Policy Year	Previous Policy Year	Prior Policy Year
Coverage Period (Mo/Day/Yr)	From	From	From
	To	To	To
Agency/Brokerage Name			
Insurer's Name			
Net Annual Premium			
Annual Deductible			
Coverage Limit			
-- Per Claim			
-- Aggregate			
Notable Endorsements/Riders			
-- Earthquake			
-- Flood			
-- Windstorm/Hail			

Does your district currently have or operate boilers?	
If "Yes", does your current property insurance policy provide coverage for those boilers?	
If you have boilers but your current property insurance policy does not provide coverage, does your district have a separate boiler/machinery policy?	

Insured Property Value			
Year of last formal property appraisal			
Is your current property insurance policy written to provide "actual cash value" or "replacement cost" coverage?	Actual cash value Replacement cost Not sure		
Does your current property insurance policy contain a blanket limitation?			
If "Yes", please enter the blanket limitation amount.			
Comments			
Quote/Bid Process			
For the most recent applicable year, how did the district solicit property insurance coverage? *(To make multiple selections, press and hold the "Ctrl" button on your keyboard and then left click each item that applies.)*		Advertised Contacted insurer Contacted insurance a Used consultant Other	If "Other", please specify.
How many quotes/bids were received?			
Please list the names of insurers that submitted a quote or bid.			

7. Vehicle/Fleet

	Current Policy Year	Previous Policy Year	Prior Policy Year
Coverage Period (Mo/Day/Yr)	From	From	From
	To	To	To
Agency/Brokerage Name			
Insurer's Name			
Net Annual Premium			
Annual Deductible			
-- Collision			
-- Comprehensive			
-- Liability			
-- Personal Injury			
Coverage Limit (Per Claim)			
-- Collision			
-- Comprehensive			
-- Liability			
-- Personal Injury			
Coverage Limit (Aggregate)			
-- Collision			
-- Comprehensive			
-- Liability			
-- Personal Injury			

Comments			
Quote/Bid Process			
For the most recent applicable year, how did the district solicit vehicle/fleet insurance coverage? *(To make multiple selections, press and hold the "Ctrl" button on your keyboard and then left click each item that applies.)*		Advertised Contacted insurer Contacted insurance agent Used consultant Other	If "Other", please specify.
How many quotes/bids were received?			
Please list the names of insurers that submitted a quote or bid.			

8. Excess/Umbrella Coverage

(In the table below, please identify which, if any, insurance policies are currently covered by an excess or umbrella policy. For those policies with such coverage, please provide the excess/umbrella insurer's name, the coverage amount, and the net premium.)

Insurance Category	Type of Coverage	Name of Insurer	Coverage Amount	Net Annual Premium
Workers' Comp				
General Liability				
Educators' Liability				
Property				
Vehicle/Fleet				

9. Other Insurances

Student Accident	
For the current fiscal year, did your district purchase student accident insurance?	
If "Yes", approximately what percentage of your district's students are covered by this policy?	
For the current fiscal year, did your district offer student accident insurance?	
If "Yes", approximately what percentage of your district's students elected this coverage?	
Student Activity	
For the current fiscal year, did your district purchase student activity insurance?	
If "Yes", are all sports and student extracurricular activities covered?	
If only some sports or extracurricular activities are covered, please list those activities.	
Unemployment Insurance	
Number of unemployment insurance claims for your district during calendar year 2006	
Over the past three years, indicate the approximate percentage of unemployment insurance claims that were appealed, either by the district or the claimant.	

10. Risk Management

Does your school district currently employ a risk manager?		
If "Yes", is your risk manager employed full-time or part-time in risk management activities?		
What types of service does the risk manager engage in? *(To make multiple selections, press and hold the "Ctrl" button on your keyboard and then left click each item that applies.)*	Safety inspections Staff training Other Not sure	If "Other", please specify
Does your school district currently receive any risk management services from outside the district?		
If "Yes", how frequent are those services?		
Who provides those services? *(To make multiple selections, press and hold the "Ctrl" button on your keyboard and then left click each item that applies.)*	Attorney Consultant Insurer Other Not sure	If "Other", please specify
What types of service are provided? *(To make multiple selections, press and hold the "Ctrl" button on your keyboard and then left click each item that applies.)*	Safety inspections Staff training Other Not sure Does not apply	If "Other", please specify

11. General Comments

Thank you for your participation.

To print a copy for your records, press the "**Print**" button *before* submitting your responses.

To submit your responses, please press the "**Submit**" button.

To clear ALL entries and start over, press the "**Reset**" button.

Appendix B

Districts Participating in the Kentucky School Boards Insurance Trust's Unemployment Insurance Fund in 2006

The table identifies each district's annual contribution amount, benefits paid, and the difference. Each school district also maintains a certain minimum balance and pays an administrative fee to KSBIT equal to 11.3 percent of contributions.

School District	Contribution	Benefits Paid	Difference
Adair County	$32,699	$15,906	$16,793
Allen County	31,547	15,287	16,260
Anchorage Independent	6,174	-	6,174
Anderson County	41,364	14,059	27,305
Ashland Independent	36,193	18,836	17,357
Augusta Independent	4,311	-	4,311
Ballard County	16,876	3,915	12,961
Barbourville Independent	6,283	1,730	4,553
Bardstown Independent	24,752	-	24,752
Barren County	49,365	8,574	40,791
Bath County	21,568	13,369	8,199
Beechwood Independent	10,099	-	10,099
Bell County	37,933	29,693	8,240
Bellevue Independent	8,278	6,748	1,529
Berea Independent	12,137	10,085	2,052
Boone County	163,334	10,114	153,221
Bourbon County	30,377	2,444	27,933
Bowling Green Independent	40,169	13,085	27,084
Boyd County	44,194	27,192	17,002
Boyle County	31,214	1,987	29,227
Bracken County	12,116	-	12,116
Breathitt County	31,443	6,263	25,180
Breckinridge County	28,866	5,418	23,448
Bullitt County	109,699	14,026	95,673
Burgin Independent	5,030	-	5,030
Butler County	22,244	14,762	7,482
Caldwell County	21,799	3,572	18,227
Calloway County	34,978	12,754	22,224
Campbell County	52,390	12,321	40,070
Campbellsville Independent	15,298	12,029	3,269
Carlisle County	10,410	2,920	7,490
Carroll County	21,619	2,980	18,638
Carter County	60,273	26,334	33,939
Casey County	28,559	-	28,559
Caverna Independent	9,246	7,611	1,635

School District	Contribution	Benefits Paid	Difference
Clark County	$60,094	$24,285	$35,809
Clay County	49,930	22,699	27,231
Clinton County	21,099	802	20,297
Cloverport Independent	4,522	4,502	20
Corbin Independent	23,706	23,899	(193)
Crittenden County	15,280	4,812	10,468
Cumberland County	13,046	6,057	6,989
Danville Independent	24,652	8,944	15,708
Daviess County	123,411	3,704	119,707
Dawson Springs Independent	7,538	-	7,538
Dayton Independent	10,515	9,490	1,025
East Bernstadt Independent	5,085	-	5,085
Edmonson County	24,264	11,826	12,438
Elizabethtown Independent	22,783	9,828	12,955
Elliott County	13,277	13,353	(76)
Eminence Independent	6,827	-	6,827
Erlanger-Elsmere Independent	21,842	-	21,842
Estill County	26,865	26,311	554
Fairview Independent	7,760	-	7,760
Fayette County	376,554	331,734	44,820
Fleming County	26,896	20,912	5,984
Floyd County	76,456	128,847	(52,391)
Frankfort Independent	12,044	11,522	522
Franklin County	66,542	16,850	49,692
Fort Thomas Independent	21,869	730	21,139
Fulton County	9,384	5,362	4,022
Fulton Independent	6,929	10,238	(3,309)
Gallatin County	16,554	7,876	8,678
Garrard County	30,781	7,457	23,324
Glasgow Independent	20,606	8,997	11,609
Grant County	38,216	8,601	29,615
Graves County	50,467	12,958	37,509
Grayson County	44,638	34,946	9,692
Green County	19,724	-	19,724
Greenup County	50,928	18,667	32,261
Hancock County	18,484	12,859	5,625
Hardin County	146,466	35,370	111,096
Harlan County	49,425	90,757	(41,332)
Harlan Independent	9,234	17,245	(8,011)
Harrison County	29,782	12,320	17,462
Harrodsburg Independent	10,256	6,963	3,293
Hazard Independent	9,560	34,468	(24,908)
Henderson County	79,477	30,907	48,570
Henry County	21,808	-	21,808

School District	Contribution	Benefits Paid	Difference
Hickman County	$9,368	$4,297	$5,071
Hopkins County	82,832	24,271	58,561
Jackson County	29,326	73,918	(44,592)
Jackson Independent	5,348	34,968	(29,620)
Jefferson County	1,024,172	311,432	712,740
Jenkins Independent	7,268	13,638	(6,370)
Jessamine County	83,524	15,973	67,551
Johnson County	39,399	514	38,885
Kenton County	126,163	23,595	102,568
Knott County	30,758	52,964	(22,206)
Knox County	55,921	35,755	20,166
LaRue County	25,143	1,838	23,304
Laurel County	91,247	34,292	56,955
Lawrence County	31,457	9,618	21,839
Lee County	13,777	3,453	10,324
Leslie County	22,370	17,081	5,289
Letcher County	40,467	41,671	(1,204)
Lewis County	28,579	2,426	26,153
Lincoln County	57,297	27,180	30,117
Livingston County	16,938	14,733	2,206
Logan County	37,461	10,700	26,761
Ludlow Independent	8,290	1,604	6,686
Lyon County	11,274	10,765	510
Madison County	106,039	53,705	52,334
Magoffin County	29,381	29,855	(474)
Marion County	33,909	17,955	15,954
Marshall County	47,536	30,087	17,449
Martin County	28,300	28,769	(469)
Mason County	53,518	9,157	44,361
Mayfield Independent	18,934	1,460	17,474
McCracken County	63,236	26,395	36,841
McCreary County	38,964	21,944	17,020
McLean County	19,219	17,380	1,839
Meade County	45,676	9,383	36,293
Menifee County	14,048	13,166	882
Mercer County	33,449	37,577	(4,128)
Metcalfe County	19,775	56,766	(36,991)
Middlesboro Independent	17,795	13,680	4,115
Monroe County	26,558	880	25,678
Montgomery County	45,936	25,949	19,987
Monticello Independent	10,267	5,890	4,378
Morgan County	26,559	13,347	13,212
Muhlenberg County	58,893	21,725	37,168
Murray Independent	22,543	33,929	(11,386)
Nelson County	47,567	23,810	23,757

School District	Contribution	Benefits Paid	Difference
Newport Independent	$25,079	$6,509	$18,570
Nicholas County	12,190	5,128	7,062
Ohio County	46,077	28,656	17,421
Oldham County	118,939	14,644	104,295
Owen County	18,835	12,632	6,203
Owensboro Independent	54,643	9,685	44,958
Owsley County	12,643	6,384	6,259
Paducah Independent	35,136	43,984	(8,848)
Paintsville Independent	9,410	4,412	4,998
Paris Independent	9,919	8,544	1,375
Pendleton County	30,714	6,349	24,366
Perry County	55,857	24,031	31,826
Pike County	119,002	84,809	34,193
Pikeville Independent	13,054	10,694	2,360
Pineville Independent	6,314	5,568	746
Powell County	29,325	16,523	12,802
Providence Independent	6,121	18,346	(12,225)
Pulaski County	87,576	27,858	59,718
Raceland Independent	10,144	-	10,144
Robertson County	4,021	-	4,021
Rockcastle County	35,331	12,755	22,576
Rowan County	36,709	41,546	(4,837)
Russell County	40,806	3,968	36,838
Russell Independent	21,780	6,416	15,364
Russellville Independent	13,857	15,185	(1,329)
Science Hill Independent	10,658	2,270	8,388
Scott County	71,759	12,432	59,327
Shelby County	64,505	24,264	40,241
Silver Grove Independent	3,547	3,686	(139)
Simpson County	32,203	5,595	26,608
Somerset Independent	17,253	19,114	(1,861)
Southgate Independent	2,097	1,420	677
Spencer County	27,676	11,847	15,829
Taylor County	28,159	-	28,159
Todd County	24,560	7,133	17,427
Trigg County	23,651	16,331	7,320
Trimble County	16,474	2,525	13,949
Union County	29,596	27,087	2,509
Walton-Verona Independent	12,038	-	12,038
Warren County	119,172	5,717	113,455
Washington County	22,264	16,363	5,901
Wayne County	33,233	2,502	30,731
Webster County	22,753	3,880	18,873
West Point Independent	1,967	3,460	(1,493)
Whitley County	56,993	18,297	38,696

School District	Contribution	Benefits Paid	Difference
Williamsburg Independent	$9,149	$2,412	$6,737
Williamstown Independent	11,155	-	11,155
Wolfe County	16,534	34,457	(17,923)
Woodford County	40,974	4,451	36,523
Total	$7,076,749	$3,250,479	$3,826,270
Net amount refunded to districts			($3,454,205)

Source: Kentucky School Boards Insurance Trust.

Appendix C

Property Appraisal Per School District

Only districts that answered the relevant questions from Program Review staff's survey are shown. It appears that some districts entered the value of insured property instead of the property appraisal. Those districts are also omitted from the table.

School District	Property Appraisal	Appraisal Date
Allen County	$81,909,045	Not sure
Augusta Independent	6,901,760	Not sure
Ballard County	45,619,452	2006
Bardstown Independent	41,710,675	2007
Barren County	78,750,039	(blank)
Bellevue Independent	18,000,000	(blank)
Berea Independent	20,233,400	Not sure
Bourbon County	51,380,719	Not sure
Boyd County	70,623,500	Not sure
Boyle County	53,247,458	2003
Breckinridge County	70,456,984	(blank)
Bullitt County	246,879,742	Not sure
Calloway County	71,597,328	2003
Campbell County	114,292,044	2003
Carlisle County	16,683,622	Not sure
Carroll County	52,000,000	Not sure
Casey County	62,119,332	2006
Caverna Independent	20,127,270	(blank)
Christian County	202,000,000	2007
Clinton County	39,606,446	Not sure
Corbin Independent	55,856,691	2006
Covington Independent	117,560,337	2003
Cumberland County	27,644,342	Not sure
Danville Independent	47,249,228	Not sure
Daviess County	231,800,100	Not sure
Edmonson County	56,930,125	More than 10 years ago
Eminence Independent	11,286,000	(blank)
Erlanger-Elsmere	67,189,059	Not sure
Estill County	55,834,207	Not sure
Fayette County	727,037,994	Not sure
Fleming County	8,212,356	(blank)
Floyd County	189,027,000	Not sure
Franklin County	163,692,786	(blank)
Ft. Thomas Independent	67,643,519	Not sure
Fulton County	20,469,504	Not sure

School District	Property Appraisal	Appraisal Date
Gallatin County	$33,327,512	2006
Glasgow Independent	453,172,448	2007
Grant County	65,310,329	(blank)
Green County	36,341,960	Not sure
Greenup County	62,153,903	Not sure
Hancock County	36,777,650	2007
Harlan Independent	26,031,453	(blank)
Henderson County	157,509,809	2004
Hickman County	24,196,042	Not sure
Hopkins County	151,165,895	2007
Jackson Independent	12,365,559	2005
Jefferson County	1,630,133,089	2006
Jessamine County	166,421,150	(blank)
Kenton County	247,064,216	2000
Knox County	114,749,874	Not sure
Lee County	40,530,125	Not sure
Letcher County	92,214,944	Not sure
Lewis County	51,813,628	2002
Lincoln County	97,619,921	2002
Livingston County	42,985,671	2007
Lyon County	26,880,405	2004
Madison County	194,439,615	Not sure
Marion County	71,951,050	(blank)
Martin County	65,955,938	Not sure
McCreary County	66,908,506	2002
McLean County	50,716,288	2006
Meade County	88,319,893	Not sure
Mercer County	84,988,521	Not sure
Metcalfe County	37,466,998	2007
Montgomery County	78,944,982	(blank)
Monticello Independent	22,195,842	(blank)
Muhlenberg County	115,780,012	Not sure
Murray Independent	70,488,820	2003
Nelson County	112,768,293	2002
Newport Independent	75,154,677	2000
Oldham County	218,005,970	Not sure
Owen County	43,460,138	1999
Owensboro Independent	127,972,603	2003
Pendleton County	73,084,476	2004
Pike County	268,942,288	Not sure
Pikeville Independent	33,365,869	2006
Pineville Independent	15,100,363	More than 10 years ago
Powell County	43,376,905	1999
Raceland-Worthington Independent	27,524,331	2005
Rowan County	73,995,979	(blank)

School District	Property Appraisal	Appraisal Date
Russellville Independent	$39,832,072	Not sure
Science Hill Independent	7,298,396	(blank)
Scott County	164,547,687	2002
Somerset Ind.	35,000,000	2005
Taylor County	48,999,755	2002
Trigg County	52,495,782	2005
Trimble County	36,085,227	Not sure
Walton-Verona Independent	24,221,831	Not sure
Washington County	33,438,257	Not sure
Whitley County	100,475,766	Not sure
Total	$22,695,262,763	

Source: Program Review staff's survey of school districts.

Appendix D

Workers' Compensation Reports Filed by School Districts, 2001-2006

School District	Total Reports	Average Reports Per Year
Adair County	13	2.2
Allen County	19	3.2
Anchorage Independent	4	0.7
Anderson County	49	8.2
Ashland Independent	45	7.5
Augusta Independent	5	0.8
Ballard County	16	2.7
Barbourville Independent	4	0.7
Bardstown Independent	25	4.2
Barren County	27	4.5
Bath County	14	2.3
Beechwood Independent	22	3.7
Bell County	55	9.2
Bellevue Independent	9	1.5
Berea Independent	10	1.7
Boone County	115	19.2
Bourbon County	29	4.8
Bowling Green Independent	63	10.5
Boyd County	55	9.2
Boyle County	31	5.2
Bracken County	11	1.8
Breathitt County	52	8.7
Breckinridge County	28	4.7
Bullitt County	106	17.7
Burgin Independent	1	0.2
Butler County	35	5.8
Caldwell County	26	4.3
Calloway County	25	4.2
Campbell County	61	10.2
Campbellsville Independent	21	3.5
Carlisle County	6	1.0
Carroll County	16	2.7
Carter County	90	15.0
Casey County	21	3.5

School District	Total Reports	Average Reports Per Year
Caverna Independent	5	0.8
Christian County	63	10.5
Clark County	138	23.0
Clay County	58	9.7
Clinton County	13	2.2
Cloverport Independent	0	0.0
Corbin Independent	27	4.5
Covington Independent	63	10.5
Crittenden County	12	2.0
Cumberland County	12	2.0
Danville Independent	26	4.3
Daviess County	66	11.0
Dawson Springs Independent	12	2.0
Dayton Independent	4	0.7
East Bernstadt Independent	2	0.3
Edmonson County	15	2.5
Elizabethtown Independent	10	1.7
Elliott County	15	2.5
Eminence Independent	2	0.3
Erlanger-Elsmere Independent	35	5.8
Estill County	22	3.7
Fairview Independent	6	1.0
Fayette County	345	57.5
Fleming County	24	4.0
Floyd County	101	16.8
Fort Thomas Independent	4	0.7
Frankfort Independent	15	2.5
Franklin County	100	16.7
Fulton County	0	0.0
Fulton Independent	12	2.0
Gallatin County	16	2.7
Garrard County	65	10.8
Glasgow Independent	25	4.2
Grant County	48	8.0
Graves County	33	5.5
Grayson County	20	3.3
Green County	20	3.3
Greenup County	19	3.2
Hancock County	37	6.2
Hardin County	105	17.5

School District	Total Reports	Average Reports Per Year
Harlan County	51	8.5
Harlan Independent	7	1.2
Harrison County	23	3.8
Hart County	15	2.5
Hazard Independent	10	1.7
Henderson County	107	17.8
Henry County	31	5.2
Hickman County	4	0.7
Hopkins County	91	15.2
Jackson County	54	9.0
Jackson Independent	5	0.8
Jefferson County	529	88.2
Jenkins Independent	6	1.0
Jessamine County	39	6.5
Johnson County	18	3.0
Kenton County	76	12.7
Knott County	50	8.3
Knox County	43	7.2
LaRue County	10	1.7
Laurel County	65	10.8
Lawrence County	30	5.0
Lee County	12	2.0
Leslie County	34	5.7
Letcher County	49	8.2
Lewis County	27	4.5
Lincoln County	38	6.3
Livingston County	5	0.8
Logan County	31	5.2
Ludlow Independent	19	3.2
Lyon County	11	1.8
Madison County	79	13.2
Magoffin County	28	4.7
Marion County	22	3.7
Marshall County	22	3.7
Martin County	56	9.3
Mason County	27	4.5
Mayfield Independent	5	0.8
McCracken County	58	9.7
McCreary County	51	8.5
McLean County	15	2.5

School District	Total Reports	Average Reports Per Year
Meade County	32	5.3
Menifee County	12	2.0
Mercer County	32	5.3
Metcalfe County	19	3.2
Middlesboro Independent	7	1.2
Monroe County	28	4.7
Montgomery County	53	8.8
Monticello Independent	9	1.5
Morgan County	20	3.3
Muhlenberg County	58	9.7
Murray Independent	25	4.2
Nelson County	63	10.5
Newport Independent	21	3.5
Nicholas County	8	1.3
Ohio County	35	5.8
Oldham County	64	10.7
Owen County	33	5.5
Owensboro Independent	66	11.0
Owsley County	9	1.5
Paducah Independent	36	6.0
Paintsville Independent	4	0.7
Paris Independent	14	2.3
Pendleton County	28	4.7
Perry County	60	10.0
Pike County	86	14.3
Pikeville Independent	9	1.5
Pineville Independent	8	1.3
Powell County	42	7.0
Providence Independent	3	0.5
Pulaski County	76	12.7
Raceland Independent	13	2.2
Robertson County	1	0.2
Rockcastle County	26	4.3
Rowan County	52	8.7
Russell County	11	1.8
Russell Independent	16	2.7
Russellville Independent	13	2.2
Science Hill Independent	3	0.5
Scott County	41	6.8
Shelby County	33	5.5

School District	Total Reports	Average Reports Per Year
Silver Grove Independent	5	0.8
Simpson County	52	8.7
Somerset Independent	13	2.2
Southgate Independent	1	0.2
Spencer County	28	4.7
Taylor County	17	2.8
Todd County	10	1.7
Trigg County	34	5.7
Trimble County	15	2.5
Union County	18	3.0
Walton-Verona Independent	6	1.0
Warren County	110	18.3
Washington County	19	3.2
Wayne County	31	5.2
Webster County	40	6.7
West Point Independent	2	0.3
Whitley County	41	6.8
Williamsburg Independent	7	1.2
Williamstown Independent	2	0.3
Wolfe County	15	2.5
Woodford County	30	5.0
Total	6,222	1037.0

Source: Program Review staff analysis of data provided by the Office of Workers' Claims.

Appendix E

Response From the Kentucky School Boards Association

Answering Questions You May Have About the Program Review & Investigations Committee Report on School Insurance

For more than a quarter century, the Kentucky School Boards Association (KSBA) has been the primary insurer of Kentucky schools through the Kentucky School Boards Insurance Trust (KSBIT). This self-insurance pool of coverage is owned by school districts and managed by a board of trustees of school board members and school administrators. In 2005, a new Executive Director of KSBA took the helm of leadership of KSBIT along with a new Director of Risk Management, a new Director of Finance, and a new Underwriting and Marketing Manager.

As you review the Program Review & Investigations Report on School Insurance, we would like to provide you with some background information to answer questions that you may have about several of its findings.

<u>How did the KSBIT Workers' Comp Fund get in a deficit situation?</u>

- In 2004, our actuaries made a major increase in our claims liability projections. They projected an additional liability of more than $6.5 million. Hence, overnight KSBIT went from projecting a surplus for 2004 to posting a significant actuarial deficit. While the ultimate cost of potential claims of concern to the actuaries may take from five to 20 years to pay out, state law requires that workers' compensation funds show the ability to cover the total payout in each year's financial statement.
- Nationally, the workers' compensation industry faces a double-edged sword: higher health care costs plus tremendous growth in future liabilities from past claims. Compounding matters for the KSBIT fund is the fact that for several years KSBIT helped districts through tough fiscal times by offering workers' compensation coverage at rates that current management believes were, in hindsight, insufficient.
- KSBIT had a virtually non-existent underwriting program to set rates, and did little to no marketing of its unique services for school districts and thus was ill-equipped to maintain a high standard of service to districts and to compete in a soft market.

- With judicious fiscal management, we have reduced the deficit from $5 million to $3.5 million, and are making recognized progress on all of the goals we have set with the Kentucky Office of Insurance (OOI) to strengthen all of KSBIT's insurance funds.

Because of the deficit, is there any danger that KSBIT cannot pay claims?

No. KSBIT Workers' Compensation Fund has no immediate liquidity concerns and cash balances are substantial as related to annual premium levels. In addition, cash available to pay claims is projected to increase significantly during the next five years based on financial estimates presented to the OOI. As a redundant safeguard, the fund submitted a $6.5 million letter of credit from a Kentucky financial institution to the Office of Insurance to meet the statutory requirement of being able to cover all potential claims in the current year's financial statement.

What is KSBIT doing to eliminate the deficit in the Workers Comp fund?

KSBIT has worked closely with the Kentucky Office of Insurance (OOI) to strengthen its funds. New management has:

- Implemented a new underwriting system.
- Changed the rate setting process to use actuarially determined rates.
- Eliminated high fixed cost related to inefficient in-house claims operations.
- Lowered administrative costs and royalties to KSBA.
- Reduced reinsurance costs.
- Increased marketing efforts to expand the customer base.

Should the school districts in my legislative district trust KSBIT to cover their employees, property, and other needs?

Yes. While private companies have historically come and gone from the insurance market, KSBIT has always been here for Kentucky schools and will continue to be.

- KSBIT has the best insurance protection for districts. We consistently offer the policy coverage that districts need to fully cover losses, and, as stated in the report, districts are exposed to less risk because KSBIT will not sell districts less coverage than needed to offer a lower rate to win a bid.
- KSBIT is a non-profit insurance provider dedicated to keeping costs low for school districts. We don't pay stockholders; instead, we reinvest dividends into the program to keep the rates as low as possible.

- To protect school district staff and to lower claims costs, KSBA offers aggressive loss prevention programs tailored specifically to the needs of school districts that private insurers cannot offer, so we are confident that KSBIT is not only a secure choice for local districts but also the best one that they can make.

The report indicates school boards are unsure of the rules and regulations regarding bidding insurance and the types of coverage they should have. Can KSBA assist districts in this effort?

KSBA looks forward to working closely with the Kentucky Department of Education to provide additional training for boards of education in the procurement of insurance.

The report recommends that the Department of Education should make changes to its process for determining property replacement rates for school districts. As the primary provider for property insurance for local districts, does KSBIT agree?

We heartily endorse this recommendation and will work with KDE to advocate for any necessary regulatory or statutory changes.

The report raises a concern about transfer of funds from KSBIT's unemployment insurance fund to a guaranty program to help shore up the Workers' Compensation fund and recommends that this not happen again. What will KSBIT do to address this?

The guaranty fund was established by prior management in 2003. New KSBIT management shut down the guaranty fund in 2006 and agrees with the recommendation by LRC staff.

The report says that KSBIT bears a disproportionate amount of certain program-related operating expenses and personnel expense, and recommends that KSBA develop a different method for allocating expenses to Trust. What will KSBA do to address this?

Our existing process complies with this recommendation. In each budget year, KSBA performs a thorough review and analysis of the time spent by each employee on KSBIT and KSBA business. Indirect expenses, such as property tax, utilities, building maintenance, etc., are paid by KSBA and then KSBIT reimburses the association based upon a formula related to the percentage of time spent by employees on KSBA and KSBIT business. Other minor expenses for KSBIT, such as office supplies, postage, and telephone lines are reimbursed at only 10 percent of the total amount incurred by KSBA. Under no circumstance is 100 percent of any allocated expense assigned to KSBIT.

KSBA is dedicated to preserving the KSBIT Workers' Compensation Program to enable local school districts to provide this benefit to their employees at the lowest cost possible and, in turn, to be good stewards of local and state tax dollars. We welcome your questions about any of our insurance programs. Please contact us at any time.

Bill Scott
Executive Director
Kentucky School Boards Association
800-372-2962

Myron Thompson
Director of Risk Management
Kentucky School Boards Insurance Trust