PUBLIC ENTITY PARTNERS
BOARD OF DIRECTORS
MINUTES OF REGULAR MEETING
DATE OF MEETING: FEBRUARY 22, 2019
BRENTWOOD, TENNESSEE

The Board of Directors of Public Entity Partners ("PE Partners") met at 10:00 a.m. on February 22, 2019 at PE Partners' office in Brentwood, Tennessee in its regular meeting.

Board Members present included: Chairman Curtis Hayes, Vice-Chairman Randy Brundige, Victor Lay, Lois Preece, Todd Smith, Sam Tharpe, and Wallace Cartwright. John Holden participated via telephone conference call.

Board Members absent were: none

PE Partners staff present were: Dawn R. Crawford, President/CEO; Charles DeMore, Executive Vice President & CFO & Director of Human Resources; Jon Calvin, Director of Underwriting; Jim Morrison, Director of Claims; and, Anthony Ponessa, Director of Information Technology.

Also present were Russ Farrar, General Counsel; Margaret Mahery, Executive Director, TML; Charles "Bones" Seivers, President, TML Bond Fund; Cody Chapman, Partner with Callan & Associates, Inc.; Kevin Wick, Managing Director with PwC; Jordan He, Manager with PwC; and, Kris Kogut, Partner with PwC.

Chairman Hayes called the meeting to order and welcomed Lois Preece, Mayor of Niota, TN as PE Partners' newest Board member.

1. APPROVAL OF MINUTES

Chairman Hayes called for a motion to approve the minutes of the November 14, 2018 Board meeting. Motion was made by Lay; seconded by Brundige. Chairman Hayes asked if there was any discussion. There was none. PASSED UNANIMOUSLY.

2. INVESTMENT ANALYSIS REPORT FOR 2018

Crawford introduced Cody Chapman with Callan & Associates, Inc. to present a report on PE Partners' investment portfolio's performance for calendar year 2018. Chapman noted significant volatility in the investment markets due to Brexit, the China trade deal and US tariffs. Interest rates moved steadily higher in the first three quarters of 2018 before dropping in the fourth quarter in the equity markets.

Chapman directed the Board's attention to a report entitled *Investment Measurement Service: Annual Review* which presented an executive summary of PE Partners' investment performance for the year ended December 31, 2018. At year-end, PE Partners' portfolio of $285 million was comprised of 94% fixed-income securities and 6% cash and cash equivalents. He noted that PE Partners' 2018 composite investment return was down 13 basis points compared to the past year, most of which occurred in the first three quarters when equity markets were climbing. However, a long-term view shows PE Partners' investment return was 5.17%, exceeding both Bloomberg Barclays Municipal Index of 3.82% and Bloomberg Barclays Agency Index of 1.87%. He commented that PE Partners' portfolio is allocated as 54% municipal bonds, 45% government agency bonds, and 2% in US Treasury holdings.

Chapman noted PE Partners' portfolio duration was 10.0 years compared with the Bloomberg Barclays Agency Index of 4.01 years. He explained that duration is a measure of interest rate sensitivity compared with the length of bond lives and that PE Partners' portfolio has longer-dated holdings which normally will outperform shorter-dated holdings over time. He noted the over 80% of the portfolio has quality rating of AA and 9% rated as AAA.

Crawford informed newer Board members that the company's investment policy has restrictions as to what types of investment securities may be purchased and that, in general, PE Partners' philosophy has been to buy-and-hold highly-rated securities to maturity to get better interest returns over a longer period. Smith asked how that practice impacts cash flow which Crawford replied the company keeps between $10-$20 million in cash in LGIP, depending on what point of the cash flow cycle we are in. Tharpe asked how would cash flow be affected if there were a major incident in West TN to which Crawford replied that the company would pay claims but then be reimbursed by reinsurers under our large-loss policies. Brundige asked the reimbursement limits to which Crawford explained reinsurance reimbursement limits for property claims are $500,000 and go up to $125 million.

Chairman Hayes asked if there were any questions. After some discussion, Chairman Hayes asked for a motion to approve the 2018 investment analysis report. Motion was made by Tharpe; seconded by Cartwright. Chairman Hayes asked if there was any discussion. There was none. PASSED UNANIMOUSLY

3. CAPITAL MODELING STUDY

Crawford introduced Kevin Wick, Jordan He and Kris Kogut with PricewaterhouseCoopers, the independent actuaries who performed an extensive study of PE Partners' capital needs and adequacy levels as of fiscal year ended June 30, 2018. The last study was performed in 2014 as of FY 2013.

Wick presented an overview of the risk management process applied in the study and the assumptions used, including the various risk categories of capital needs. He explained that while a lower range of risk, such as between 1-in-100 and 1-in-150 year levels, is common for regulators and some commercial carriers, such carriers have options available to them that risk pools do not, such as canceling a block of policies if the carriers determine they are under-capitalized. He also noted that global insurance regulation which sets European and other developed countries' target capital levels beginning at 1-in-200 is gradually being adopted in the USA.

Based on the prior 2013 study, PE Partners' Board of Directors had adopted a policy that capital reserve levels be determined based on a risk level range between 1-in-200 and 1-in-250 year levels. Wick emphasized the importance to the company and its membership that the Board update PE Partners' risk profile. As a result of the recent study, PwC proposed a couple of options for target risk ranges and presented rationale for each option and recommended to the Board a risk range between a lower level of 1-in-200 years and an upper level of two times 1-in-200 years, with which PE Partners management concurs. The impact of this recommendation is to increase the upper level of the current policy for current risk exposures and uncertainties. Based on these ranges, capital reserves could range between $92 million and $183 million, based on June 30, 2018 balances.

After much discussion among Board members with PwC representatives, a motion was made by Tharpe to accept the capital adequacy study and adopt a target risk range of between a 1-in-200 year level and two times 1-in-200 year level; seconded by Brundige. Chairman Hayes asked if there was any discussion. There was none. PASSED UNANIMOUSLY

4. LEGISLATIVE UPDATE

Chairman Hayes said because Farrar had to leave the meeting soon he would call on him to present an update of recent legislative bills at this time instead of under Other Business as shown on the agenda. Farrar asked Crawford to open the update and said he would comment afterwards. Crawford informed Board members about TN House Bill 370 concerning proposed legislation about open records that would be detrimental to PE Partners and thanked Mahery for agreeing to be on standby if PE Partners needs assistance. She also thanked Farrar and his lobbying team for their efforts. Crawford also informed Board members about TN Senate Bill 484 that would require all local governments to bid all insurance, including health, dental and vision insurance, each year. After Crawford's remarks, Farrar also commented on the current status of the bills and lobbying actions. Since this is an informational update, no action was required of the Board.

5. FINANCIAL REPORTS

A. Chairman Hayes called on DeMore to present the Statement of Revenues, Expenses and Changes in Net Position for the six months ended December 31, 2018. DeMore stated that gross earned premium was $36,811,390 which is $538,940 or 1.49% more than this time last year. Reinsurance premiums ceded of $4,801,915 was $134,130 or 2.72% less than last year. Net earned premium was $32,009,475, which is $673,070 or 2.15% more than the prior year. Investment income totaled $4,163,020, which was $955,901 or 18.67% less than last year. However, compared with this year's budget projections, investment income is $238,020 or 7.29% more. Total revenues of $36,285,764 were $292,222 or 0.80% less than last year's actual revenues but exceeded budget projections by $1,421,216.

In the expense category, DeMore stated total loss and loss adjustment expenses incurred were $26,854,585, which was fairly flat with last year at 0.73% more. Policy acquisition costs of $4,077,118 were $691,091 or 20.41% more than last year due to agent commissions. Total General and Administrative Expenses of $3,942,270 were 0.36% or $14,385 less than last year's actual expenses. Compared to this year's budget, administrative expenses are $577,153 or 12.77% less than projected. Total expenses were $34,873,974 which is 2.56% or $871,158 more than last year.

PE Partners' operating income at December 31, 2018 was $1,411,790. DeMore noted that operating income combined with the change in unrealized gains on investments of $1,046,533 for the current period resulted in an increase in net position of $2,458,323 for the six months ended December 31, 2018.

DeMore reviewed the Statement of Net Position as of December 31, 2018, which presented cash and cash equivalents of $17,712,427 and investments of $267,477,704. Premiums receivable were $3,707,458. Accrued interest was $2,767,874 and prepaid reinsurance was $5,205,458. The majority of reinsurance recoverable on paid losses of $1,857,693 represents mostly worker compensation reinsurance claims. Net fixed assets were $3,455,866, and total assets were $302,568,414, which is 1.20% more than last year.

Deferred outflows of resources of $1,082,780 related to PE Partners' net pension liability will be actuarially adjusted at the end of this fiscal year. Total assets and deferred outflows of resources were $303,651,194 at December 31, 2018.

Liabilities included net reserves for losses of $144,454,227; unearned premiums of $34,814,621; accounts payable and accrued expenses of $1,340,700; and dividends payable of $1,224,043. Total current liabilities were $181,833,591. PE Partners' net pension liability of $1,194,542 will be actuarially adjusted at the end of this fiscal year, as will the deferred inflows of resources of $5,740 related to the net pension liability. Total liabilities and deferred inflows of resources was $183,033,873.

When beginning net position of $118,158,998 is combined with this period's change in net position of $2,458,323, net position at December 31, 2018 was $120,617,321.

B. DeMore reviewed the internally-managed fixed income portfolio as of January 31, 2019. On this date PE Partners had funds invested with the Tennessee Local Government Investment Pool totaling $13,158,516 with an average return of 2.36%.

PE Partners' portfolio consisted of 61 municipal bonds and 36 agency bonds and one treasury security and had a book value of $277,460,821 and a market value of $267,279,850, representing a net unrealized loss of $10,180,971 at January 31, 2019. DeMore noted that while the average coupon rate of the entire portfolio was 3.415%, the average coupon rate of the municipal bonds alone was 3.636%.

C. DeMore presented management's recommendation for a dividend declaration of $6,500,000 to be considered for FY 2020. This dividend, if approved, would be issued as dividend credits for policies renewing July 1, 2019 through June 30, 2020 and would be allocated as follows: workers compensation-$2,900,000; liability-$2,950,000; property-$650,000. DeMore stated that dividends are a return of surplus to members and are calculated, in part, based on members' loss prior performance from inception. Over a twenty-year history, PE Partners has returned more than $112 million in dividends to members, which averages to over $5.1 million per year. He noted that the proposed $6.5 million dividend would keep PE Partners' reserve balance within the risk level approved by the Board based on capital reserve study performed.

Motion was made by Lay to accept the financial reports as presented, including the FY 2020 dividend declaration as recommended; seconded by Cartwright. Chairman Hayes asked if there was any discussion. There was none. PASSED UNANIMOUSLY

6. POLICY COVERAGE AND PREMIUM BASE RATE CHANGES – FISCAL YEAR 2020

A. Jon Calvin, Director of Underwriting, presented management's recommendations to the Board for proposed changes in policy coverages to become effective on July 1, 2019 as follows:

<u>Property</u>

- **Cyber Extension Option: Ransomware, Social Engineering, Data Restoration Expense**

<u>Liability Policy</u>

- **Gallagher Crisis Protect Program**

<u>Workers Compensation</u>

- **No change**

Smith asked about aviation coverage for members. Crawford said management would start the process to research this coverage and report back to the Board.

B. Calvin also presented proposed changes in premium base rates to become effective on July 1, 2019 as follows:

<u>Workers Compensation</u>

- **Base rate reduction:** **Decrease 2.70%**

<u>Liability</u>

- **General Liability:** **No base rate change**
- **Law Enforcement:** **No base rate change**

- **Errors and Omissions Liability: No base rate change**
- **Automobile Liability: No base rate change**
- **Automobile Physical Damage: No base rate change**

Property

- **Base rate reduction: No base rate change**

Calvin noted that the workers compensation base rate has increased only 5.0% over the ten year period 2008-2018, which demonstrates PE Partners' goal to provide rate stability the face of increasing medical costs and payroll bases.

Chairman Hayes asked if there was a motion to approve the recommendations for changes in policy coverage and policy premium base rates effective July 1, 2019 as recommended; motion made by Smith; seconded by Tharpe. Chairman Hayes asked if there was any discussion. There was none. PASSED UNANIMOUSLY

Chairman Hayes commented he is looking forward to the study about aviation coverage since the City of Livingston is now running its own airport.

7. CAPITAL BUDGET REQUESTS

Crawford explained two requests are being presented for budget consideration: a claims administration system and a request related to the new office building.

A. Claims Administration System

Crawford called on Anthony Ponessa and Jim Morrison to present the claims administration system request. Ponessa stated that the proposed claims administration system represents an organizational solution that would allow all of the company's different systems to be integrated into one system as opposed to having silos within individual departments as they are now. He said the challenge has been to keep data current that is common to and resides in each department's individual silo for all the different systems. He said Origami Risk is the company offering the claims administration solution being recommended and that other pools using the software have been contacted about their experience and satisfaction. Ponessa said this would be a phased approach whereby we would bring in claims or billing or different deductible programs.

Morrison commented that some elementary deficiencies exist which our current claims system does not allow us to address, much less moving from a silo effect of each department having its own system that makes it very difficult to make each system talk to each other. As one example, the current claims system takes an average of six months to prepare for a new update and requires extensive testing before applying the update in production mode. Consequently, claims personnel spend half of each year getting ready to test new reiterations in claims system updates which, in turn, diverts much of their time and focus from processing membership claims. With the Origami Risk system, updates would be pushed out quarterly seamlessly behind the scenes and would not require testing of the update's integrity and impact. He said the proposed solution would allow claims personnel to better service our membership rather than service our claims administration system. He said they are awaiting a solution starting with claims that would allow them together with client services, loss control and underwriting to interact with membership by letting any department see what another department is doing with respect to a single member at any point in time.

Chairman Hayes asked if there were any questions. Crawford said she had included quote information for $475,900 for the first year which includes data conversion and implementation costs, and then drops

to under $300,000 for the following two years each. Because Origami Risk is web-hosted software, she said it is difficult to compare its cost with our current system costs which is on servers that require equipment, backup systems and staff time to maintain. She said in terms of a fixed cost, the Origami Risk system would cost more annually but when indirect and variable costs of overhead and personnel time are also considered, it would probably be a wash. She added that because the proposed system would definitely be an enhancement to the membership operations, management is requesting the Board to approve the system.

Chairman Hayes asked if there were any questions of Crawford and if not, he would entertain a motion. Motion was made by Cartwright to approve the claims administration system as presented; seconded by Lay. Chairman Hayes asked if there was any discussion. There was none. PASSED UNANIMOUSLY

B. Buildings

Crawford informed Board members that a nonbinding letter of intent to purchase the current building for $2.3 million had been received and was based on a recent appraisal performed. Since the prospective purchaser is also the general contractor for our new office building, she said when they asked how soon the current building could be vacated she replied it was dependent on them. She requested approval from the Board, subject to legal review and sign-off, to move forward to execute a contract for the sale of the current building. Motion was made by Tharpe and seconded by Brundige to approve the execution of a contract to sell the current office building as presented.

Crawford directed Board members' attention to a capital budget request for the new office building based on a current cost estimate of $5,754,567, which includes the building shell and interior build-out but excludes the cost of furnishings, decorating, office equipment and any future change orders. She asked the Board's approval to move forward with this capital budget request as it currently stands with some reasonable variation for change orders as they may come along in the normal course of things. She stated any abnormal things would be brought back to the Board for approval.

Chairman Hayes asked if there were any questions. Smith asked if the new office building got approval before his coming on the Board to which Crawford replied yes. Chairman Hayes asked if there was a motion to approve. Motion was made by Brundige; seconded by Smith. Chairman Hayes asked if there was any discussion. There was none. PASSED UNANIMOUSLY

Crawford mentioned that recent photos of the building constructor are included in the Board packet. Cartwright asked the name of the general contractor to which Crawford replied Steelhead Building Group based in Brentwood, TN.

8. APPOINTMENT OF BOARD MEMBER

Chairman Hayes stated that while Mayor Lonnie Norman was appointed as a member of the Board of Directors at the last Board meeting, Mayor Norman is not eligible since the City of Manchester is not a member of PE Partners. Therefore, Chairman Hayes recommended Dr. Christa Martin, Vice-Mayor of Columbia, TN to fill the vacant position of director on the Board of Directors.

Motion was made by Tharpe to appoint Christa Martin as director, subject to ratification by TML's Board of Directors; seconded by Cartwright. Chairman Hayes asked if there was any discussion. There was none. PASSED UNANIMOUSLY

Chairman Hayes asked Crawford to provide a list of cities not currently insured by PE Partners.

9. DATE OF NEXT MEETING

The date of the next Board meeting will be Saturday, June 22, 2019 at 8:30 a.m. in Memphis, Tennessee in conjunction with the Tennessee Municipal League's annual conference location.

10. OTHER BUSINESS

A. Crawford provided information about TN Senate Bill 480 which is also being monitored because it proposes to eliminate the exemption of local governments from having to bid their insurance coverage if they purchase it from a governmental pool, such as PE Partners, (as under a different statute than discussed earlier). Regardless of the outcome of Senate Bill 484 as discussed earlier, the effect of Senate Bill 480 would require local governments to bid their insurance even if purchased from a governmental pool.

B. Crawford directed attention to information in the Board packet about the upcoming NLC-RISC Trustees conference to be held May 15-17, 2019 in Ft. Lauderdale, FL. She mentioned that PE Partners reimburses Board members for their registration and expenses for attending this conference as well as the National League of Cities conference in November and the TML annual conference. She mentioned that due to the change in conference dates this year neither she nor DeMore would be able to attend. However, she encouraged Board members to consider attending and to let Heather Hughes know before April 1st if they planned to attend in order to finalize registrations.

C. Chairman Hayes asked Crawford about PE Partners' organizational smart goals that were referenced in a recent newsletter and said he would like to see them. She said the smart goals are set at the beginning of each fiscal year and updated quarterly and that she would provide a copy to him. Chairman Hayes asked whether any strategic planning is offered. Crawford said she would welcome the opportunity for a strategic planning retreat with the Board. Chairman Hayes said he would like each Board member to think about it and put it on the agenda for discussion at the next Board meeting in June in Memphis.

11. ADJOURNMENT

Chairman Hayes asked for a motion to adjourn. A motion was made by Tharpe and seconded by Brundige. PASSED UNANIMOUSLY. Meeting adjourned at 12:29 p.m.

William Curtis Hayes, Chairman

Charles DeMore, Secretary