

## Texas Municipal League Intergovernmental Risk Pool

### *Operating Company Covered*

### *By This Report*

Financial Strength Rating

### *Local Currency*

A/Stable/—

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### *RatingsDirect Publication Date*

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### *Major Rating Factors*

#### *Strengths:*

- Strong, well-established market position as a leading provider of workers' compensation and property/casualty insurance for governmental entities throughout Texas.
- A strong pricing advantage, with relative freedom from regulatory oversight regarding pricing.
- Very strong capitalization, supported by healthy earnings.

#### *Weaknesses:*

- Geographically concentrated in Texas.
- Limited member and premium growth opportunities given the focused member base.
- Increased risk retention could give rise to earnings volatility.

### *Rationale*

The insurer financial strength rating on the Texas Municipal League Intergovernmental Risk Pool (TML-IRP) reflects the organization's firmly established presence in the Texas local government market, very strong capitalization, and pricing advantages. Offsetting these strengths are the pool's geographic concentration in one state, limited member and premium growth opportunities because of its niche market, and potential rise in earnings volatility given the pool's increased risk retention.

TML-IRP maintains a proven platform as a leading provider of workers' compensation and property/casualty coverage to the Texas local government market and as the fourth-largest public entity risk pool in the U.S. based on 2007 gross contributions. The organization

provides coverage to 2,638 members (as of Sept. 30, 2008) and is firmly established in its market, as its very strong 98% member-retention rate year-over-year through both hard and soft market cycles demonstrates.

The high market penetration and very strong retention rate are results of the organization's historical ability to provide stable risk-financing and loss-prevention services for its members. This strength is in part because of TML-IRP's status as a governmental risk pool, which gives it relative freedom from regulatory oversight regarding pricing and allows it to respond quickly to changing loss trends.

The organization's capitalization is very strong, as measured by Standard & Poor's Ratings Services' risk-adjusted capital model as of Sept. 30, 2008 (including a 1-in-250-year probable maximum loss property catastrophe stress charge on an aggregate basis). Members' equity increased by 9% in 2008, reaching \$300 million, mainly because of strong earnings. As a result, in the fiscal year that ended Sept. 30, 2008, the board allocated a return of \$22 million of members' equity.

Partially offsetting these strengths, the organization is highly concentrated, with limited growth opportunities in its Texas market as the market becomes saturated. Competition from traditional commercial carriers remains minimal, as TML-IRP's very strong historical retention levels demonstrate.

To enhance its stability and reduce reinsurance expenses, the organization employs a risk-retention strategy whereby the internal reinsurance, stability, and large-loss funds retain a percentage of risk to mitigate reinsurance costs. The recent increase in retention of additional risks will continue to influence severity levels. We do not expect the increase to expose the capital base substantially to severe losses, but it might create earnings volatility.

### ***Outlook***

TML-IRP's growth opportunities are somewhat limited. We expect that members' gross contributions will be flat in 2009 and contingent on Texas Windstorm Insurance Assoc.'s (TWIA) legislation, which should be resolved by May 2009. Commercial insurers have entered and exited the market opportunistically with the hardening and softening of market prices. The lack of persistency in the competitive landscape continues to strengthen TML-IRP's presence by solidifying its relationship in the municipal market.

In 2009, Standard & Poor's expects that the pool will generate strong profitability in line with historical levels, with a combined ratio of 93%-95%. Operating performance could be more volatile because of changes in TML-IRP's risk retention, especially in its liability fund. Beginning Oct. 1, 2007, the pool no longer purchased third-party reinsurance protection for its liability fund, which might give rise to increased net losses. In 2009, we expect TML-IRP to grow members' equity in each fund and reach \$330 million-\$335 million on a consolidated basis, including a return of members' equity. We also anticipate that the capital adequacy will remain very strong and redundant for the current rating.

The organization operates as a single-state, risk-bearing entity for which exposure to legislative changes in Texas carries the potential to impose significant operating issues to the organization. TML-IRP is monitoring the Texas legislature as it discusses changes to TWIA that could affect the pool's operations. If there is a material legislative change in Texas that might impede the pool's operation, we could revise the outlook to negative. We could also revise the outlook to negative if TML-IRP suffers significant reserve development that leads to a material operating loss. Considering the pool's risk profile, a revision of the outlook to positive is unlikely in the medium term.

***Competitive Position: Single-State Concentration Somewhat Limits The Pool's Growth***

TML-IRP is strongly positioned as a leading provider of workers' compensation, liability, and property insurance to the small-to-midsize Texas local government market. The organization maintains a strong but concentrated market position in Texas. With 2,638 participating members (about 73% of its target market) as of Sept. 30, 2008, the membership base remains strong, with year-over-year retention levels of about 98% in its three lines of business. In 2007, TML-IRP was the fourth-largest public entity risk pool in the U.S. based on \$146 million in gross contributions.

Table 1

<b><i>Texas Municipal League Intergovernmental Risk Pool/Business Statistics</i></b>					
<i>—Year ended Sept. 30—</i>					
<i>(Mil. \$)</i>	<i>2008</i>	<i>2007</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>
Gross contributions	152.5	145.0	141.8	137.7	127.9
(%) Growth	5.2	2.3	2.9	7.7	9.5
Net contributions	144.6	136.4	133.9	129.9	114.3
(%) Growth	6.0	1.9	3.0	13.6	10.5
Reinsurance utilization (%)	5.2	5.9	5.6	5.7	10.6
<b><i>Net earned contributions by line of business:</i></b>					
Worker's compensation (%)	45.2	44.3	44.1	44.6	44.0
Liability fund (%)	30.5	31.9	32.8	32.8	33.4
Property fund (%)	20.8	20.3	20.1	19.9	19.6
Other (%)	3.6	3.5	3.0	2.7	3.0

Table 2

<b><i>Largest Public Entity Risk Pools (Ranked By 2007 Member Contributions)</i></b>		
<i>Rank</i>	<i>Pool</i>	<i>Contributions (Mil. \$)</i>
1	California State Association of Counties Excess Insurance Authority	316.1
2	Alliance of Schools for Cooperative Insurance Programs	181.1
3	Protected Insurance Program for Schools	180.7
4	Texas Municipal League Intergovernmental Risk Pool	145.8
5	Municipal Excess Liability Joint Insurance Fund	138.0

Source: Business Insurance.

As of January 2009, TML-IRP had a 94% share of the largest portion of its target market: small-to-midsize cities in Texas (about 46% of membership). This demonstrates its strength in serving this segment. The pool does not provide coverage to large cities, such as Houston and Dallas, as these self-insure. Virtually all members use all three of the existing coverages, which further enhances TML-IRP's market penetration. However, the organization's growth opportunities remain somewhat limited given its single-state focus.

Table 3

<b>Texas Municipal League Intergovernmental Risk Pool Member Growth</b>								
<i>—Year ended Sept. 30—</i>								
	<i>2008</i>	<i>2007</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>
Total members	2,638	2,621	2,596	2,547	2,512	2,432	2,221	2,038
Additional members	17	25	49	35	80	211	183	61

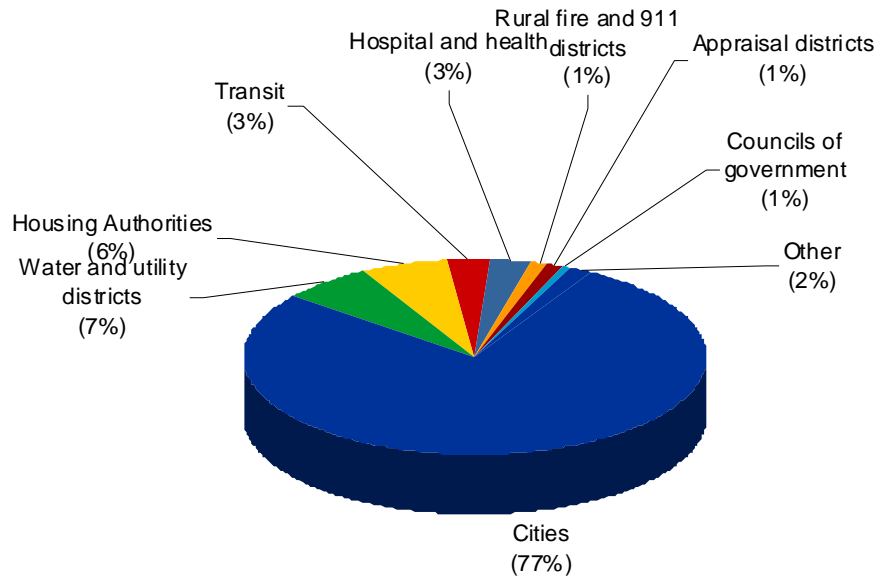
The high market penetration and strong retention illustrate the organization’s historical ability to provide stable risk-financing and loss-prevention services to its members. This strength is in part because of TML-IRP’s status as a government entity; as such, it benefits from relative freedom from regulatory oversight regarding pricing and exemption from mandatory participation in state guarantee funds. TML-IRP’s close association with the Texas Municipal League—an organization offering a mixture of legal, lobbying, and educational services to members—conveys a further advantage in maintaining TML-IRP’s market share and retention levels.

The pool’s limited growth opportunities as market saturation reaches its upper limit partly offset these strengths. Competitive pressures from traditional commercial insurers remain minimal, as TML-IRP’s extremely strong historical retention levels demonstrate. Commercial insurers have entered and exited the market opportunistically with the hardening and softening of market prices. This lack of persistency in the competitive landscape strengthens TML-IRP’s presence by solidifying its relationship in the municipal market. We believe a hardening cycle in the property/casualty market, especially in commercial property insurance, could further strengthen the organization’s retention levels.

Aside from these factors, TML-IRP operates as a single-state, risk-bearing entity for which exposure to legislative changes in Texas carries the potential to impose significant operating hurdles to the organization. For example, legislation could impose retrospective coverage on certain exposures that were not actuarially priced for in prior years.

**Membership Distribution By Gross Contributions (2008)**

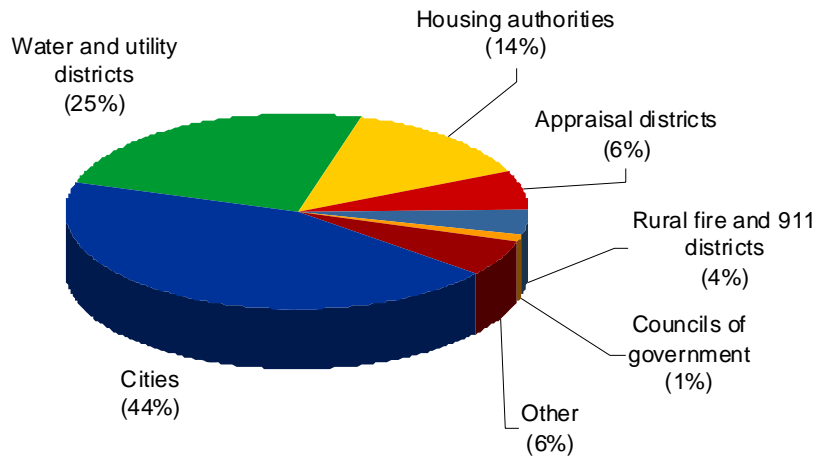
Total: \$153 million



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**Membership Distribution By Member Type**

Total members: 2,638



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**Prospective**

TML-IRP's growth opportunities are rather limited. We expect that members' gross contributions will be flat in 2009 and contingent on TWIA's legislation, which we expect to be resolved by May 2009. Because of the strength in membership retention, pricing advantages, and continued presence in its

market where other commercial carriers have entered and exited, Standard & Poor's expects TML-IRP's competitive position to remain strong over the long term.

***Management And Corporate Strategy: Extensive Knowledge Of The Local Market***

TML-IRP benefits from an experienced management team that continues to demonstrate a solid understanding of the various risks its members face, and it continues to run the operation conservatively and sensibly. The pool's strategy is to provide Texas municipalities and other units of local government with a stable source of risk financing and loss-prevention services at the lowest cost, thereby stabilizing members' insurance costs.

***Operational management***

The pool provides and maintains a stable, low-cost risk-financing system for its members. As part of this, it educates members about avoiding and reducing risks, and it controls losses with effective legal defense and claims handling. The pool also serves as an expert on risk management for cities, other units of local government, and the Texas Municipal League.

The various operational approaches the pool leverages to accomplish this include direct sales, proactive screening of claim frequency and severity levels by membership, voluntary loss-prevention programs, and risk-management programs for members out of compliance with expected loss levels. In particular, mandatory and voluntary prevention programs help maintain price stability across the various funds. The pool transitioned the medical bill review process to an in-house operation (500,000 bill line items per year). An outside contractor previously handled this function. By bringing this task in-house, the pool can better control the quality and cost of medical services.

The pool is functionally organized around three core self-sustaining operating funds, allowing for an effective use of a common capital base while maintaining the flexibility required to address each segment's capital needs. The three main funds are the workers' compensation fund, the liability fund, and the property fund.

***Financial management***

TML-IRP follows a very conservative investment strategy in compliance with the Texas Public Funds Investment Act, which requires local governments to invest in securities that will preserve principal, are liquid and highly rated, and that have no exposure to the equity markets (see the Investments And Liquidity section of this report).

To enhance stability and reduce reinsurance costs, the organization employs a risk-retention strategy whereby the reinsurance, stability, and large-loss funds retain a percentage of risk to mitigate reinsurance costs. This retention of additional risks will continue to influence severity levels. We do not expect the increased retention to expose the capital base substantially to severe losses, but as prior-year losses demonstrate, it might create earnings volatility.

In 2002, TML-IRP established the lifetime benefit fund to pay claims to beneficiaries of employees who were fatally injured on the job. The workers' compensation fund pays the lifetime benefits fund the present value of future claim payments to the beneficiaries. The claims are considered closed in the workers' compensation fund, and the lifetime benefits fund assumes the financial obligation for paying these claims.

In October 2007, TML-IRP created the coastal storm fund to cover windstorm and hail for properties located in the counties adjacent to the Gulf of Mexico with certain characteristics (such as being located more than 20 miles from the coast) to reduce the cost of coverage for members. This fund provides coverages that the property fund cannot readily provide because of reinsurance limitations.

### ***Enterprise Risk Management: Adequate For The Organization's Risk Profile***

TML-IRP's enterprise risk management (ERM) is adequate relative to its risk profile. Standard & Poor's largely attributes the pool's long-term success in its market to its ability to manage its operations' inherent risks adequately. Although reserving and pricing are TML-IRP's greatest risks, the organization's unique legal structure and business mission ultimately shape our view of its ERM.

TML-IRP's goal of providing a low-cost risk-financing system to its members exposes the pool to pricing and reserving risks. However, TML-IRP's rates are not subject to regulatory oversight, which provides some flexibility in pricing if underlying claim trends were to change. Every underwriting year, coverages are rated for each member, on established rates, adjusted by experience modifiers and discounts to reflect the actual loss experience of the members. The experience modifier is based on prior experience, adjusted by certain factors. TML-IRP engages a third party to evaluate its reserve adequacy, mainly for workers' compensation and liability, and recommend pricing for its insurance policies, which could create a conflict of interest. As a mitigating factor, auditors also review the pool's reserves.

TML-IRP cannot make retrospective premium calls if historical pricing was inadequate, but the board can address this potential deficiency in setting future contribution rates. The pool also offers loss-prevention services—including education and training and worksite risk assessments—to its members, which mitigate overall claims. In addition, TML-IRP has been successful in the long term in managing overall insurance risk (namely, reserving and pricing risk) by using third-party reinsurance and internal reinsurance, large-loss, and stability funds.

### ***Accounting***

TML-IRP prepares its financial statements using the accrual basis of accounting in accordance with GAAP as applied to governmental entities. Therefore, the pool follows the Governmental Accounting Standard Board's (GASB) standards. The pool complies with the provisions of GASB 31 by reporting unrealized gains and losses on investments as an income item. Standard & Poor's evaluates each fund individually. However, evaluation on a consolidated basis is more integral to the rating process.

The pool's eight operating funds are accounted for as self-sustaining business-like activities (enterprise funds). The core workers' compensation, liability, and property funds are the only funds that receive contributions from participating members and incur a monthly allocation of administration expenses. The four other operating funds serve as specialized operational funds. All of the funds report separate financial statements. However, capital is fungible within the organization with pre-approval from the board. Therefore, when Standard & Poor's evaluates TML-IRP's capital adequacy, it is calculated and viewed on a consolidated basis. Because it is an intergovernmental risk pool, the Internal Revenue Service recognizes TML-IRP's funds as political subdivisions. As a result, the organization does not incur any income tax expense.

Despite TML-IRP's objective of not producing profit but providing stable coverage throughout the cycles to its members, it has generated strong operating performance in the past five years. The pool's

five-year (2004-2008) average return on revenue (ROR) of 21.3% and an average combined ratio of 93.9% had a standard deviation of less than 5%, which is low. These results speak to the pool's ability to set contribution rates conservatively and manage claims volatility, which has led TML-IRP to return excess capital back to its members in the past five years.

Table 4

<b>Texas Municipal League Intergovernmental Risk Pool/Operating Statistics</b>					
	<b>—Year ended Sept. 30—</b>				
<b>(Mil. \$)</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Total revenue	173.9	163.9	158.9	152.7	136.8
Underwriting gain/losses	6.9	11.0	13.8	10.8	(1.3)
Pretax operating income	36.3	38.5	38.8	33.7	21.2
Return on revenue (%)	20.9	23.5	24.4	22.0	15.5
Return on average members' equity (%)	12.6	14.5	16.0	15.2	10.1
Return on assets (%)	6.5	7.4	8.0	7.4	5.0
Loss ratio (%)	72.5	69.1	68.2	70.0	77.4
Expense ratio (%)	22.7	22.9	21.6	21.7	23.7
Combined ratio (%)	95.2	91.9	89.7	91.7	101.1
Operating ratio (%)	30.8	29.6	25.3	17.2	9.7
Net investment income to net contributions (%)	26.0	21.5	15.0	8.9	10.8
<b>Cash flows</b>					
Net cash flow from operating activities	7.2	1.0	38.7	37.6	30.9
Net cash flow from investing activities	(3.5)	3.0	(33.2)	(43.2)	(38.4)
Net cash flow from financing activities	(0.4)	0.8	(0.1)	(0.1)	0.0

**Historical**

TML-IRP experienced unfavorable reserve development in its workers' compensation and liability funds in 2003, which drove the combined ratio to 118.9%. The pool adjusted rates upward but also leveraged the very strong members' equity balance by strengthening its reserves to offset anticipated higher future losses. As a result, the pool recorded underwriting losses in 2003 and 2004. Following 2004, operating performance improved because of solid underwriting, as demonstrated by the combined ratio declining to 91.7% in 2005, 89.7% in 2006, and 91.9% in 2007.

**Current performance**

Operating performance continued to be strong in 2008, with a combined ratio of 95.2% and an ROR of 20.9%. The pool generated \$36 million in pretax operating income in 2008, slightly lower than the \$39 million in 2007, partially because of \$10.5 million in net catastrophe losses stemming from Hurricane Ike. The pool benefited from improved results in its workers' compensation and property fund, with RORs of 20.3% and 16.0%, respectively, while the liability fund continues to produce strong results, with an ROR of 18.4%. Given the large loss fund serves as internal reinsurance, the fund's operating performance declined as it reported a negative 53.3% ROR in 2008 compared with a positive 59.5% in the prior year, as it recorded higher catastrophe losses.

TML-IRP's results benefited from \$12 million of favorable reserve development, mainly in the workers' compensation funds, before adjustments and eliminations. The result was that the combined ratio improved by 8 percentage points. Net investment income contributed about 17% to total revenues as of Sept. 30, 2008, and is a significant contributor to the organization's earnings. Historically, earnings from investments have provided funds to pay almost all operating costs, while membership contributions have been allocated to the payment of losses and loss-adjustment expenses. In the past five years (2004-2008), investment income has not offset the pool's operating expense, but the underwriting gain was strong enough to offset this difference.

In the first quarter of fiscal-year 2009, ended Dec. 31, 2008, TML-IRP continued to produce solid underwriting results. However, the pool's combined ratio increased to 93.7% compared with 73.6% from the prior-year period. Increased losses in both the liability and property funds hampered results, primarily because of prior-year reserve development.

Table 5

<b>Texas Municipal League Intergovernmental Risk Pool/Catastrophe Losses Incurred By Source</b>	
<b>Year</b>	<b>Net incurred losses (Mil. \$) Natural catastrophes</b>
2008	20.4 Hurricane Ike (\$10.5 million) and other storm losses (\$9.9 million)
2007	8.9 Hail, wind, tornado, lightning, and flood
2006	7.2 Hail, wind, tornado, and fire
2005	10.3 Hurricane Rita (\$5.0 million) and other storm losses (\$5.3 million)
2004	0 No catastrophe losses

**Prospective**

In 2009, Standard & Poor's expects that the pool will produce strong profitability in line with historical levels, with a combined ratio of 93%-95%. Operating performance could be more volatile because of changes in TML-IRP's risk retention, especially in its liability fund. Beginning Oct. 1, 2007, the pool no longer purchased third-party reinsurance protection for its liability fund, which might give rise to increased net losses.

TML-IRP's investment strategy is conservative and complies with the Texas Public Funds Investment Act, which restricts investments to U.S. treasuries and low-risk, highly rated, government-backed securities held to maturity.

Table 6

<b>Texas Municipal League Intergovernmental Risk Pool/Investment Statistics</b>					
<b>(Mil. \$)</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Invested assets	563.5	519.5	488.2	454.0	427.1
% Growth	8.5	6.4	7.5	6.3	5.4
Total assets	579.6	534.9	503.8	467.6	438.5
Investment income (excluding realized and unrealized gains/losses)	28.8	26.8	24.4	22.1	21.1
Investment yield (%)	5.3	5.3	5.2	5.0	5.1
Realized capital gains/losses	8.8	2.6	(4.3)	(10.6)	(8.8)
Total yield (%)	6.9	5.8	4.3	2.6	3.0
<b>Portfolio composition (% of invested assets):</b>					
Long-term fixed income investments (%)	90.3	87.7	93.3	89.1	94.4

Table 6

<i>Texas Municipal League Intergovernmental Risk Pool/Investment Statistics (cont.'d)</i>					
<i>(Mil. \$)</i>	<i>2008</i>	<i>2007</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>
Short term investments (%)	6.2	9.2	4.4	9.6	2.8
Cash and cash equivalents (%)	3.5	3.1	2.3	1.3	2.8

As of Sept 30, 2008, the aggregate investment portfolio consisted primarily of fixed-income investments, with 14% allocated to U.S. treasuries and Ginnie Mae securities, 83% allocated to other highly rated 'AAA' securities issued by U.S. government-sponsored enterprises (i.e., Fannie Mae, Freddie Mac), and 3% allocated to cash and cash equivalents. In the 2009 fiscal year, TML-IRP started increasing its allocation to high-quality municipal bonds (only in Texas) that meet its investment guidelines given the attractive yields from these securities (4.4% of total invested assets as of year-end 2008). The pool continues to use three separate outside portfolio managers, which oversee about 75% of TML-IRP's invested assets, with the internal finance team managing the remaining 25%.

This conservative investment philosophy limits the inherent credit risks in the portfolio but hinders the organization's ability to produce higher returns during strong investment years. Given its conservative investment strategy, the pool has avoided the large investment losses that plagued the insurance industry's 2008 results. Therefore, TML-IRP reported a strong total yield of 6.9% for the year and a five-year (2004-2008) average of 4.5%. As of Sept. 30, 2008, the effective duration of the fixed-income portfolio was 3.53 years, which was close to the blended duration of the loss reserves (including all business lines) of 3.58 years. Moreover, investment income is a determining factor in setting the contribution rates of the pool's members.

The organization's liquidity is strong, supported by 10% of its \$564 million in invested assets allocated to cash and short-term investments. In addition, TML-IRP's conservative investment strategy, with high-credit-quality securities and no subprime exposure, is likely to continue and support the pool's future obligations.

### ***Prospective***

TML-IRP's investment portfolio risk profile will remain virtually unchanged in the long term. The Texas Public Funds Investment Act dictates this conservative posture, restricting the organization's investment options.

### ***Capitalization: Very Strong, Underpinned By Members' Equity***

TML-IRP's capital position is very strong, including a net aggregate exposure property catastrophe charge to incorporate the pool's probable maximum loss based on the 1-in-250-year return period. Capital is built on about \$300 million in members' equity as of Sept. 30, 2008, and supported by strong earnings.

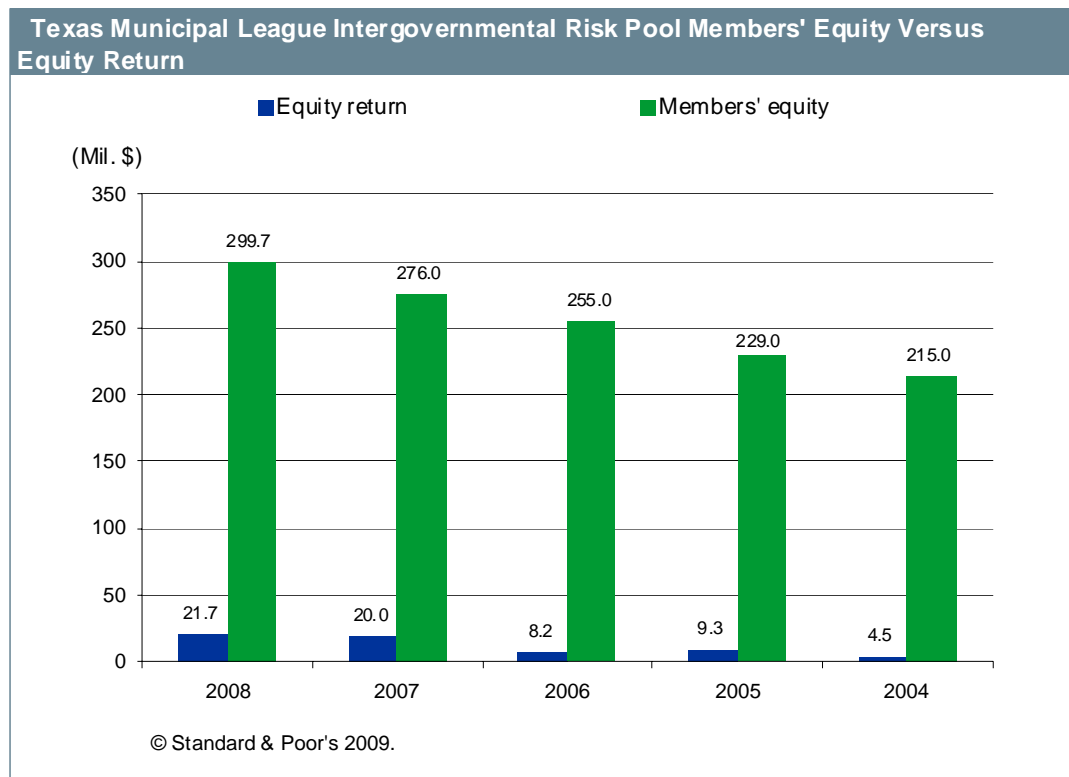
Table 7

**Texas Municipal League Intergovernmental Risk Pool/Capital Adequacy And Flexibility Statistics**

—Year ended Sept. 30—

<i>(Mil. \$)</i>	2008	2007	2006	2005	2004
Members' equity	299.7	276.3	255.2	228.9	215.1
Growth (%)	8.5	8.3	11.5	6.4	3.8
Operating leverage (%)	48.2	49.4	52.5	56.8	53.1
Liquid assets/technical reserves (%)	229.0	223.5	216.9	209.1	207.6
Loss reserves/members' equity (%)	81.3	83.1	87.3	93.9	94.7
Loss reserves/net contributions (%)	168.5	168.4	166.4	165.4	178.3
Reinsurance recoverables (on paid losses) to members' equity (%)	0.1	0.2	0.2	0.1	0.3

The board of trustees approved the use of an internal equity study, developed by the pool's finance department, as a guide for assessing the capital adequacy of the pool's equity. For the year ended Sept. 30, 2008, the board allocated a return of members' equity of \$21.7 million, including \$8.1 million in the workers' compensation fund, \$10.8 million in the liability fund, and \$2.7 million in the property fund. In the past five years, the return of members' equity totaled \$63.6 million.



Given the strength of the capital base, TML-IRP has retained a larger share of risk in the past two years. Standard & Poor's does not believe the increased retention will materially expose the capital base to severe losses, but it could cause volatility in earnings performance.

**Prospective**

In 2009, Standard & Poor's expects TML-IRP to grow members' equity in each fund and reach \$330 million-\$335 million on a consolidated basis, including a return of members' equity. We also anticipate that the capital adequacy will remain very strong and redundant for the current rating.

**Reserves**

We consider TML-IRP's reserves to be adequate. The pool writes a mix of business that includes short-tail lines, but it is primarily the long-tail lines of business that constitute a significant risk. The majority of the \$243.7 million reserve balance as of Sept. 30, 2008, is from the longer-tail workers' compensation and liability funds. These constituted 80% of the reserve balance and are a significant factor affecting the quality of TML-IRP's balance sheet. Mitigating factors are the pool's strong capitalization and the reserve balance, which constituted only 81% of members' equity in 2008. This percentage has been declining since 2004, when reserves constituted 95% of member's equity. TML-IRP changed its consulting actuarial firm in 2008 to an organization that better understands the pool's business risk. The actuarial firm recommended a release of some IBNR reserves, which led to IBNR reserves as a percentage of total reserves decreasing to 39% in 2008 from 41% in 2007.

Table 8

<b>Texas Municipal League Intergovernmental Risk Pool/Members' Equity</b>					
	<b>—Year ended Sept. 30—</b>				
<b>(Mil. \$)</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Incurring but not reported (IBNR)	94.2	94.3	95.7	95.6	79.7
Total reserves	243.7	229.7	222.8	214.9	203.8
Percentage of IBNR to total reserves (%)	38.7	41.1	43.0	44.5	39.1

TML-IRP has good claims management. Its liabilities are capped. The pool performs a claims audit every three years, and any claims greater than \$500,000 need the board's approval before being paid. The good claims-management process has supported the pool's favorable reserve development in the past five years, including \$11.6 million of reserve releases before adjustments and eliminations for fiscal year-end 2008. The reserve releases were primarily from the \$9.5 million in the workers' compensation fund and the \$3.7 million in the reinsurance fund.

Table 9

<b>Texas Municipal League Intergovernmental Risk Pool/Reserve Development</b>					
	—Year ended Sept. 30—				
<i>(Mil. \$)</i>	2008	2007	2006	2005	2004
Workers' compensation	(9.5)	(4.9)	(2.7)	4.0	(3.1)
Liability	0.5	(5.9)	(6.1)	(7.2)	(1.8)
Property	(0.4)	0.2	(1.1)	(1.1)	(0.4)
All other funds	(2.2)	1.8	1.3	2.2	1.7
Total development before adjustment and eliminations*	(11.6)	(8.8)	(8.6)	(2.1)	(3.6)

\*Negative values indicate favorable development.

### **Reinsurance**

The organization's reinsurance program is good relative to TML-IRP's risk profile. TML-IRP obtains third-party reinsurance coverage from a portfolio of highly rated outside carriers, mainly for its property fund. In addition, TML-IRP operates three internal funds (reinsurance, stability, and large-loss funds), which function as an extra reinsurance cushion for high-severity claims. As of Sept. 30, 2008, the pool had about \$44 million in reinsurance recoverables with minimal credit risk exposure. Of this, 98% was from carriers rated 'A' or higher, and the remaining 2% was from the National League of Cities Mutual Insurance Co. (NLC-MIC).

Since 2007, TML-IRP started retaining most of its liability risk (including aviation) on its books and no longer purchases third-party liability reinsurance except for a small quota-share participation (22.5% of \$2 million excess of the pool's \$3 million first-layer retention) by NLC-MIC. Since 1984, the pool has paid about \$68 million in premiums to reinsurers (excluding NLC-MIC) and collected about \$6 million in liability loss payments (excluding aviation). The liability fund has never had a loss that exceeded \$2.5 million. Furthermore, the pool's exposure to losses from any single occurrence is capped not only by the Texas tort claims caps but also by the limits of liability purchased by each member.

Property catastrophe exposure is contained within the existing third-party reinsurance program. First-tier (coastal area) windstorm and hail coverage requested by pool members is covered through TWIA, which offers policies capped at \$4.2 million covering both building and contents. Coverage of more than \$4.2 million is placed through TML-IRP. All major concentrations of catastrophic exposure (south, middle, and east) are less than TML-IRP's current \$100 million catastrophic reinsurance protection.

### **Financial Flexibility: Limited Compared With Traditional Stock Insurance Companies**

The pool's financial flexibility is somewhat limited when compared with traditional stock insurance companies because of its lack of access to the equity market. TML-IRP has the ability to secure and use debt financing, though it has never tapped this form of financing. TML-IRP does not have the authority to assess its members. Likewise, members do not have the benefit of withdrawing equity from TML-IRP even when they decide to leave the pool. The organization's primary means of enhancing its capital base and managing its liabilities and risk remains with the use of optimal reinsurance structures, particularly in its property coverage.

**Ratings Detail (As Of 30-Mar-2009)\***

**Operating Company Covered By This Report**

**Texas Municipal League Intergovernmental Risk Pool**

Financial Strength Rating	
<i>Local Currency</i>	A/Stable/—
Counterparty Credit Rating	
<i>Local Currency</i>	A/Stable/—
<b>Domicile</b>	Texas

\*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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