

PROFESSIONAL LIABILITY FUND
Finance/Investment Committee

Minutes of Meeting
January 22, 2021

The Open Session of the Finance/Investment Committee met at approximately 9:30 am on January 22, 2021 via Zoom video conference.

Committee Members:

Present:

Oren Haker (Chair)
Michael Batlan
Chris Karlin

PLF Staff Members:

Betty Lou Morrow
Carol Bernick

Guests:

Mark Higgins of RVK
Mike Williams of the Oregon State Bar

Notice of the meeting was given pursuant to ORS 192.640

Agenda:

- RVK December 31, 2020 Flash Report and update (Mark Higgins with RVK)
- December 31, 2020 Draft Financial Recap
- Cost of Claims
- Claims Reserves
- Audit Notification

Betty Lou Morrow opened the meeting turning it over to Mark Higgins of RVK.

RVK December 31, 2020 Flash Report and update

Mr. Higgins provided a brief overview of the PLF's portfolio performance. The total portfolio had an overall return of almost 14%. He recommended rebalancing equity funds which he and Ms. Morrow can further discuss. The portfolio, net of investment management fees, has outperformed the combined benchmark.

Chris Karlin asked Mr. Higgins how he thinks the market might react as more money is put back into the economy but more importantly at the tail end. Mr. Higgins stated they aren't able to reasonably predict the short term but when things start to tail off and the capital starts to go to work depending on how the Federal Reserve responds, there could be some volatility.

Mike Williams asked about rebalancing the fund, by approximately how much. Mr. Higgins replied it is approximately 3% overweight in equities, roughly \$2 million. Ms. Morrow stated part of this is due to the timing of the PLF's Primary Assessment renewal due date which causes an infusion of cash at the end of the year. To avoid this amount sitting in the bank account, some of the assessment funds were initially transferred to the short duration fund and then into domestic equities. Both of these funds were depleted somewhat as a result of large claims settlements near the end of the fiscal year.

Michael Batlan asked about the Real Estate fund. Mr. Higgins agreed that it is off target a bit. However, the movement of funds in/out of alternative asset accounts are a more complex approach than traditional funds. Ms. Morrow noted that the target "zone" gives some breathing room as values vacillate continually. Mr. Higgins stated nothing is egregiously off target and it is borderline as to whether or not rebalancing is necessary. Ms. Morrow stated there are funds in the Operating account which needs to be moved so she will begin rebalancing as she moves money out of the operating bank account.

December 31, 2020 Draft Financial Statements

Ms. Morrow reviewed the December 31, 2020 draft internal financial statements (material provided prior to the meeting). The \$7.5 million end year 2019 surplus was much higher than projected in October. This was mainly due to an unanticipated spike in market returns in the final two months of the fiscal year. There will be minor adjustments to the financial statements however there won't be any material adjustments other than the PERS liability. The PERS Actuarial report has not yet been received from the State but the expected PERS liability will be increased by a minimum of \$750,000.

Ms. Morrow stated that during the past year she has expressed an ongoing concern about the increasing number of attorneys that will be leaving private practice at the end of 2020. Carol Bernick asked how many attorneys were down from the prior year as of the last primary assessment due date of January 11th. Ms. Morrow indicated as of January 21st there was a decrease in renewals of approximately 351 covered parties which begins to be material in loss assessment revenue. Ms. Morrow and Mr. Higgins meet approximately every two to three years to discuss the financial goals of the PLF and whether or not the asset allocation continues to match those goals. Reduced revenue streams, along with a growing surplus will be considerations given to the financial modeling for the 2022 budget and beyond. They will be meeting in 2021 to work on this.

There were a number of budgeted items that were underspent/overspent. Budgeted items overspent can be explained mostly by conscious decisions made throughout the year knowing some budgeted items would be underspent such as travel, meals, etc. Some areas that were overspent were expenditures that would have been made in 2021, but were able to be completed during 2020 due to being underspent on so many budget lines. Some of the projects that the PLF was overspent on either due to moving projects ahead or necessity because of COVID were updates to the PLF website, legal/employment related issues, preparing for all staff to work remotely during the pandemic and physical changes within the office to make it a safe working environment to allow essential staff to continue coming into work as scheduled.

The Excess program has exceeded budget for the ceding commission. The budget was built prior to the finalization of negotiations with AON and reinsurers. The Excess program did not receive the anticipated share of the Investment income due to large settlement Excess claims near the end of the year. Nearly \$5 million was paid out in Excess claims towards the end of 2020. Early in 2021, and assuming retention will remain at the same levels, the program should see an increased allocation of the investment revenue. Mr. Karlin asked whether or not the Excess program is consolidated into the PLF statements. Ms. Morrow confirmed they are included in the consolidated balance sheet. The Primary program cannot fund the Excess program so there is a due to/from which drives the Excess bottom line. There is an aggregated balance sheet for reporting purposes, but there are also separate Excess and Primary balance sheets.

Ms. Morrow has the following preliminary list of items with regards to finances that she will be monitoring in 2021:

- Return on Investment, budgeted \$4.25 million
- Claims – Indemnity has increased significantly during the past year
- Claims – Expense
- Claims – Count
- Claims – Total cost
- Extended Reporting Coverage (ERC)
- Number of covered parties

Mr. Karlin made a comment that it would be helpful to have a separate income statement that removes the investment earnings. This would be helpful to show the variances and show the actual Net Position. The presentation of the information would help visually show the importance of investment income to the operation which would otherwise may not be as clear. Ms. Morrow said this can be done. However, reflecting on a previous comment made by Mr. Karlin to use the surplus net of investment revenue as a performance metric, Ms. Morrow commented it could never be viewed as a true performance metric as assessments were never intended to fully cover the cost of claims and operations.

Mr. Karlin stated commercial property insurance has dramatically increased by approximately 30-40% and that The Oregon State Bar may pass that onto the PLF. So we may need to keep that in mind for budgeting purposes. Mr. Williams from the Oregon State Bar stated there is a lease agreement in place until 2028, so the rate cannot be adjusted unless they attempt to re-negotiate.

Cost of Claims / Claims Reserves

December 31, 2020 actuarial recommendations

Overall claims liabilities have decreased. The actuarial report recommends adopting the following actions:

- Total Liabilities \$21.9 million (\$11.2 indemnity and \$10.7 million expense).
- Cost of new claims of \$23,000 (\$12,000 indemnity and \$11,00 expense).
- Increase ERC Liability by \$400,000 to \$3.6 million.

Ms. Morrow noted as 2022 budget considerations begin in May there will likely be a need to discuss the need to reduce the primary assessment in 2022 in order to stay within the Net Position. She would like the committee to consider a one-time payment to covered parties as opposed to reducing the assessment. Ms. Bernick commented she doesn't agree with this approach as the in-year payment seems too similar to an insurance payment and it would seem to set up expectations that will happen every year. There might be those that pay closer attention to the budget and ask/expect it going forward.

Mr. Oren asked what the driver was behind the ERC increase. Ms. Morrow stated this is related to an increase in ERC claims in addition to increased numbers of attorneys who have ERC. ERC exposure is increasing in both areas.

Audit Notification

Ms. Morrow noted the annual audit has been scheduled starting the week of March 8th which will be done electronically. Mr. Karlin asked who the auditors were, Ms. Morrow replied Kern & Thompson. Mr. Karlin asked how long they have been doing the audit. Ms. Morrow replied approximately 9 years. She understands that typically auditors are switched every five or so years and has submitted Requests for Proposals twice since her tenure however there had been no expressions of interest shown by other audit firms.

Other Items

Ms. Morrow stated the committee had previously discussed divesting bank loans from the portfolio. The funds were moved into equities without prior approval from the Board of Directors which should have been presented at the December meeting. Ms. Morrow will add this to the upcoming Board meeting agenda to ask the BOD to approve the motion. This approval will then be requested of the Board of Governors.

These minutes were approved by Michael Batlan and Chris Karlin