



Texas Association of School Boards

Legal Services

P.O. Box 400 • Austin, Texas 78767-0400 • 512.467.3610 • 800.580.5345 • legal.tasb.org • legal@tasb.org

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The Board's Role in Risk Management

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Introduction

The high school burns down in the middle of the night. The building is a total loss and has to be completely rebuilt. A hurricane destroys the elementary school, the administration building and the bus fleet. There is no place for students to go to class, no place for administration to work and no buses to transport the students to and from school. The district's best teacher falls and seriously injures her back while putting up the bulletin board in her classroom. She will not be back to work for at least six months. Unhappy parents file a lawsuit against the district, the board and the superintendent alleging that their child was sexually molested at school. The parents and their attorneys hold a press conference, and the lawsuit is the lead story on the evening news. The budget forecast is grim and the district is forced to impose significant layoffs due to lower tax collections and decreasing enrollment. You are a school board member in one of these districts. What do you do?

Whatever the reason you may have had to run for the school board, chances are that dealing with issues like the ones above was not high on the list. And yet, events like these create some of the most difficult and challenging situations for any school district. There are risks inherent in governing or overseeing any organization, and school districts are no exception.

What is Risk and Risk Management?

What exactly is "risk"? And what can a school district do about it? Let's start with some basic definitions. According to Dan Borge, author of *The Book of Risk*, "risk means being exposed to the possibility of a bad outcome." Managing risk means "taking deliberate action to shift the odds in your favor—increasing the odds of good outcomes and reducing the odds of bad outcomes."

Options for Dealing with School District Risks

When it comes to dealing with risk, a school district can do any of the following: ignore the problem and hope it doesn't happen, self-insure, buy commercial insurance, or join a risk pool, also known as collective self-insurance. With the exception of the first option (ignoring the risk and hoping it does not happen), all of these are viable alternatives. Choosing the best alternative to protect your district's employees, property, and financial assets is not an easy task. In choosing the right solution a school district should consider a number of factors. The following is a compilation of questions to ask and issues to consider when choosing the best strategy for managing the everyday risky business of education.

Self-Insurance

If the district is considering self-insurance, it is important to know how much in claims (or losses) the district can afford to absorb financially, both over the long term and from a cash-flow standpoint. Even if the district purchases reinsurance or stop loss insurance, it is likely that the district will have to make the initial payment on a claim and wait for reinsurance reimbursement, which can take weeks or even months. For example, if the district chooses to self-insure workers' compensation coverage, can it absorb the cost of a large hospital bill which could be hundreds of thousands of dollars and which legally has to be paid within 45 days?

Another consideration for self-insuring is how claims will be handled. Will the district self-administer the claims or hire a third-party administrator (TPA)? If self-administering, does the district have the staff and computer systems capable of keeping up with statutory and regulatory requirements? If choosing a third-party administrator, how will the TPA be compensated? Beware of hidden fees and charges to the claim files that are not disclosed in the proposal. Always ask for a detailed listing of all charges that the administrator or affiliated vendors will be paid under the contract, whether directly paid by the district or charged to the claim file. When hiring a TPA, your district is turning over the checkbook to someone else. Make sure their interests are aligned with yours, and be sure the TPA really understands school district business.

Commercial Policy or Risk Pool

If purchasing a commercial insurance policy or joining a risk pool, the district should read the full policy or coverage document to fully understand what is covered and what is excluded. Relying on a summary submitted in a proposal or on the representations of an agent or broker could leave the district with gaps in coverage. For example, one risk pool does not cover the full replacement cost for roofs that are more than 25 years old. So if a district has a building built in the early 1990s and sustains damage to the roof, that risk pool's coverage will not pay to replace the roof and restore the building to its previous condition. The district will have to bear that cost. It is important that the district know that when evaluating coverage options.

When purchasing a commercial policy, the district should inquire where the claims will be handled. Does the carrier have a Texas presence or will claims be paid out-of-state, or even out of the country? Claims locations can have a significant impact on the quality of service the district receives in the event of a major claim. Likewise, the district should have some knowledge of the carrier's claims handling philosophy and service record. The Texas Department of Insurance keeps records of service complaints on all insurance carriers licensed to do business in Texas. Does the insurance company have experience

with Texas school districts? Will they know, for example, that after a fire, the district will need portable buildings? How fast will that carrier assist in getting those portables delivered? Or is that something the district staff will spend their time explaining to the carrier or worse, handling themselves.

Whether purchasing an insurance policy or joining a risk pool, the district should evaluate what strategies the provider has in place to reduce claims costs and return the district to normal operating conditions as quickly as possible. For example, does the insurance carrier or risk pool have a network of contracted medical providers to ensure that employees who are injured on the job can get quick and effective medical care? Is there a strategy for controlling pharmaceutical costs, especially for employees who are on long-term medications? Is there a panel of qualified attorneys knowledgeable about Texas law and governmental immunities to defend lawsuits against the district? Are there readily available damage appraisers who can be at the district in a matter of a few hours in the event of property damage?

Risk pools, such as the TASB Risk Management Fund, have been around for more than 40 years and have a successful track record in serving the needs of Texas school districts. However, not all risk pools are created equal. Because risk pools are not regulated by the Texas Department of Insurance and are not subject to the protections of the state's insurance guaranty fund, it is even more important that the district carefully evaluate the strength, stability, and service record of any risk pool. First and foremost, a district should carefully examine the financial strength of the pool. How much money does the pool have in assets? How much in members' equity or fund balance? If faced with a large loss, can the pool quickly pay the claim? What is the pool's track record on making claims payments? How long does it take to get a claim paid? Would the district have to obtain a loan until the pool can make payment or wait on a reinsurance payment? What would the district have to do while waiting on the pool to get the cash to pay a loss? How stable is the pool in the event of higher than expected losses? Is there an assessment clause in the pool agreements that allows the pool to retroactively assess members if losses are higher than expected? Has the pool ever had an assessment? If so, how often and for how much? The district should require the pool to provide its most recent audited financial statements. Unwillingness or inability by a risk pool to produce an audited financial statement should serve as a red flag for any district considering joining the pool.

In evaluating a risk pool, potential members should also examine and understand the pool's governance and operation structure. Who is in charge? Who serves on the pool's board? How are they selected to serve on the board? Who carries out the work of the pool? Some pools are administered in-house by pool staff; others are managed by third parties. Understand who will provide the services to the district, their mission, and how they are organized and compensated. Is the administrator for-profit or not-for-profit? What are the administrator's financial incentives?

Since risk pools are essentially group or collective self-insurance mechanisms, districts should also consider how many members are in the pool and what kinds of entities make up the membership of the pool. Is pool membership limited to educational entities, so there are similar types of risk exposures, or is pool membership open to any type of local government? Claims of school districts can be very different from claims of cities, counties, and other local governments, and those differences can impact overall costs. Is the pool's membership base large enough to sustain a bad claims year (for example, a hurricane that damages several members)? Are there 60 pool members or 1,000 pool members who will absorb large claims?

When thinking about protecting their assets and employees, many organizations focus on the issues discussed above, which primarily address what happens after a loss. But it is equally important to focus on what can be done to prevent a claim or a loss from happening in the first place. A district's risk management provider should be an important partner in developing the district's loss prevention and organizational risk management programs. In evaluating providers, districts should consider what assistance the provider can offer in providing property and workplace inspections, training programs, accident prevention planning, safety and security audits, and effective return to work programs. Districts should also ask if these services are included in the premiums quoted or if there is an additional fee.

Legal Requirements

School districts have wide latitude in choosing their risk management approach. It is important, however, that the district meet the legal requirements to provide certain coverage, as well as comply with procurement laws regarding the purchase of insurance.

State law requires school districts to provide workers' compensation (WC) coverage to their employees. Districts have three options to meet this requirement: purchase a commercial WC policy, join a joint-self-insurance fund (i.e., risk pool) or individually self-insure. Tex. Lab. Code § 504.011.

Texas school districts are also required by the Texas Unemployment Compensation Act to provide statutory unemployment benefits for school employees. Tex. Lab. Code § 201.026. This responsibility can be met by becoming either a taxing employer or a reimbursing employer with the Texas Workforce Commission (TWC). A taxing employer pays a fixed unemployment tax determined by the state, while reimbursing employers reimburse TWC for the cost of their actual claims. School districts choosing to be reimbursing employers may contribute through participation in a risk pool that provides unemployment compensation coverage to members of the pool. These risk pool members remain reimbursing employers, although their costs may be fixed in the form of a contribution charged by the pool.

Although not required by law, most school districts also choose to cover other risks they face (e.g., loss of property, risks of litigation, etc.) through the purchase of commercial insurance or collective self-insurance, as described above. State law dictates how those decisions are to be made. The Texas Attorney General has opined that the purchase of insurance falls under the requirements of Texas Education Code section 44.031. Tex. Att’y Gen. Op. No. DM-347 (1995). As a result, any insurance contract valued at over \$50,000 in the aggregate must be procured in a manner specified by this statute. Joining an interlocal agreement (the method by which many risk pools are organized) is an acceptable purchasing method which meets legal requirements. Tex. Educ. Code § 44.031.

In addition, school districts should be mindful that they are prohibited from using agents or brokers of record for the procurement of insurance required to be purchased through the procedures found in Texas Education Code section 44.031. Tex. Atty. Gen. Op. No. JC-205 (2000).

Conclusion

Protecting your district’s most valuable assets—the students, employees, property, and financial resources—is a complex proposition. To ensure you make a wise choice, follow a few simple guidelines:

Beware of unusually low costs. Remember that if it sounds too good to be true, it probably is. Managing your risk by buying the cheapest insurance policy could turn out to be the most expensive option of all.

Know what you are buying. Make sure that your district’s exposures and specific needs are covered. Be especially mindful of flood coverage and the flood zone designation of each school building. Also, ensure that your coverage amounts will actually equal or exceed your potential losses.

Carefully check both coverage and exclusions to ensure that you will have the protection you need.

Choose a trusted partner. When times are tough, you will want a partner strong enough to provide the help you need. Know who you are doing business with and their track record.

This document is continually updated, and references to online resources are hyperlinked, at tasb.org/Services/Legal-Services/TASB-School-Law-eSource/Business/documents/bds-role-in-risk-management.pdf. For more information on this and other school law topics, visit TASB School Law eSource at schoolawesource.tasb.org.

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