EL DORADO LAFCO

LOCAL AGENCY FORMATION COMMISSION

AGENDA OF JUNE 24, 2009

REGULAR MEETING

TO:	**Francesca Loftis, Chair, and Members of the El Dorado County Local Agency Formation Commission**
FROM:	**José C. Henríquez, Executive Officer**
AGENDA ITEM #4:	**DETERMINE LAFCO'S GENERAL LIABILITY INSURANCE CARRIER**

RECOMMENDATION

Staff recommends that the Commission:

1. Receive the following information regarding LAFCO's general liability insurance options;
2. Receive the opinions from experts analyzing the various programs;
3. Approve the purchase of general liability insurance from the Special District Risk Management Association and supplemental insurance from Alliant;
4. Allocate any unspent monies in the general liability insurance category of the LAFCO budget into a reserve account and provide direction to staff on the basic framework of how the account should be structured; and
5. Direct staff to prepare and file the necessary paperwork.

REASON FOR RECOMMENDED ACTION

The Commission requested staff to return with expert analyses regarding the adequacy of general liability insurance coverage so that the Commission can decide whether to retain the County of El Dorado as its insurance carrier or switch to SDRMA and Alliant. Four expert opinions have all indicated that the SDRMA program is almost as comprehensive as the County's program. The supplemental insurance from Alliant would plug the most significant gap in SDRMA's coverage. Consequently, switching carriers would result in lower costs to the Commission without risking any significant exposure.

BACKGROUND

As the Commission is aware, in January the County's Risk Management Department notified LAFCO staff that this agency's general liability insurance premium for Fiscal Year 2008-09 was $29,592, a significant increase from the estimated premium of $3,000-5,000 given in March 2008. In the same conversation, Risk Management also indicated that LAFCO's premium for FY2009-10 would be approximately $30,000.

Since then, the Commission has grappled with the question of switching general liability carriers. At issue is whether another insurance policy exists that is just as inclusive as the County's program but less expensive. After the receipt of proposals, the budget ad hoc committee and LAFCO staff have recommended that the Commission purchase its insurance from the Special District Risk Management Authority (SDRMA). Alliant Insurance Services, Inc. also submitted a proposal for supplemental insurance that covers injunctive/declaratory relief claims (a party sues LAFCO over a decision and is asking the courts to set LAFCO's ruling aside), which is the biggest exposure not included in SDRMA's program. In staff's estimation, the two programs combined provide coverage that is just as comprehensive as the County's program. However, because the Alliant proposal was received the day of the May 27, 2009 meeting, the Commission was hesitant to switch carriers without further review.

In their discussions over the budget at the May 27 meeting, the Commissioners directed staff to get expert opinions on the various coverages to ensure that LAFCO that programs are comparable in their offerings. In addition, the Commission adopted the Final FY2009-10 Budget with an allocation of $30,000 in the general liability line item to give itself the flexibility to either retain the County or switch carriers. The Commission indicated that it would decide which carrier it would utilize at the June 24, 2009 meeting so that all carriers would be notified of LAFCO's decision prior to the beginning of FY2009-10.

Panel of Experts

Following the Commission's direction, LAFCO staff asked four experts, independent of each other, to compare the SDRMA program, the Alliant supplement and the County's program to determine the adequacy and comparability of coverage. In alphabetical order, LAFCO staff asked the following individuals to submit their analysis of the programs:

- Ron Grassi, Assistant County Administrative Officer, County of El Dorado
- Robin Johnson, Senior Consultant, Bickmore Risk Services and Consulting
- Andrew Morris, LAFCO Counsel, Best Best & Krieger
- Dennis Timoney, Chief Risk Officer, SDRMA

These four individuals were selected because of they offer a diversity of opinions. Messrs. Grassi and Timoney would have an opportunity to represent their respective programs. As your counsel, Mr. Morris would be in the best position to identify the types of claims that would most likely be filed against LAFCO and determine how the various programs cover those exposures. Mr. Johnson is from a consulting firm specializing in actuarial services, risk research studies, audits and benchmarking, risk management consulting and claim litigation management. He serves as an independent third party in the liability insurance field.

Scope of Analysis

It must be noted that there was a small difficulty in seeking these opinions since the County has never disclosed its terms and conditions of coverage to LAFCO. Indeed, this was noted in the analyses by both Messrs. Johnson and Morris. In this regard, Mr. Grassi is the only individual who would have access to this information, and as he notes, as a self-funded program the County has an advantage over other programs in that they can be inclusive in the types of claims the County can cover. The structure of the County program is as follows: It is self-funded up to $1M and buys $17M in excess insurance from the California State Association of Counties (CSAC). This excess insurance is underwritten by Alliant. It can be inferred, then, that the inclusiveness of the County program is up to $1M. After that amount, any claim filed with the County is subject to the CSAC excess insurance terms and conditions.

To aid Messrs. Johnson, Morris and Timoney in their analysis, LAFCO staff obtained a copy of the matrix utilized by Larry Costello, former risk manager for the County, in his comparison of the SDRMA and the County programs (if the Commission recalls, at the April meeting it had asked Mr. Costello to compare the SDRMA program with the County's program). This matrix contained the areas of coverage in the CSAC excess insurance; consequently, the matrix serves as a proxy for the County's program. While a copy of Mr. Costello's analysis was given at the last meeting, his synopsis was again appended to this report for the Commission's convenience (Attachment A).

All four were asked the following questions; however, Mr. Timoney's responses to the first two questions were provided in separate letters. Consequently, SDRMA's findings are appended to this report in Attachments E and F:

1. How well does SDRMA's program compare to other insurance programs available to local governments?
2. How well does SDRMA's program compare to the County of El Dorado's program?
3. Does the supplemental insurance offered by Alliant provide coverage for legal costs that may be incurred by LAFCO defending itself against injunctive/declaratory relief cases where the plaintiff is not seeking to recover actual damages?

Messrs. Timoney and Johnson were asked an additional question:

4. If there are areas of overlap between the SDRMA program and the supplemental insurance from Alliant, what would be the impact to LAFCO? Specifically, would any administrative obstacles/hurdles arise from having two insurance carriers in the event of a multi-area claim being filed against LAFCO?

Experts' Opinions and Summary of Conclusions

The experts' task was to ensure the Commission could make a valid "oranges to oranges" comparison between the County program and the SDRMA program/Alliant supplemental insurance. Three of the four experts opined that it was possible to draw an "oranges to oranges" comparison between the SDRMA/Alliant coverage and the County's program and felt comfortable to do so. Messrs. Johnson, Morris and Timoney (in addition to Mr. Costello's opinion) have indicated that the SDRMA program is as good as the coverage offered by the County. All four agree that the only exceptions to this conclusion are the following:

- The County's program offers a higher insurance limit; and
- Injunctive/declaratory relief claim insurance is not covered by SDRMA. However, all four indicated the Alliant supplemental insurance quotation provides sufficient coverage to LAFCO against injunctive/declaratory relief claims. The differences in opinion only vary in degree of assertion (from "yes it does" to "it doesn't say that it does but doesn't exclude it either").

Mr. Johnson did raise a concern regarding the SDRMA coverage for property damage that warrants further discussion (the same issue is discussed in his letter, Attachment C, page 2 of 30 and in his evaluation matrix, Attachment C, page 12 of 30). While Mr. Johnson's evaluation matrix provides more detail, his June 10, 2009 letter describes the types of exposures that maybe of the highest concern to LAFCO. A particular exposure Mr. Johnson wanted the Commission to be aware of related to Exclusion "D":

> Care, Custody, and Control, does not provide coverage for liability because of property damage to property in one's care, custody, or control. Typically, this exclusion is limited such that it would provide coverage for liability for damage caused to property one has rented but not assumed the liability under contract. If LAFCO rents office space and does not insure the property through a property policy, LAFCO may want to question SDRMA regarding the coverage.

LAFCO staff brought this concern to SDRMA's attention and Mr. Timoney provided the following response (also included here as Attachment G):

> The Care, Custody & Control exclusion under the Liability Coverage Agreement refers to property owned by the member. Since the agency rents space, (the building itself is not in the care, custody or control of the agency), if an agency employee damaged the building (or some part of the building), and the owner filed a claim against the agency, this would be covered under the General Liability coverage provided to the agency.
>
> The District owned property (desks, chairs office equipment) would be covered under the Contents Coverage of the First Party Property Coverage provided to the Agency.

When informed of Mr. Timoney's response, Mr. Johnson indicated that the language in the exclusion is "peculiar" and not "usually seen in other policies;" however, he indicated SDRMA's response does address his concern.

The opinions, in their entirety, are included in this report as Attachments B through F. As with all issues, it is staff's goal to provide sufficient documentation to the Commission so that it can make an informed decision on this matter. The information contained in these attachments assert the validity and fairness of comparing between the two general liability insurance options. With these analyses on hand, LAFCO staff made its recommendation below.

<u>Recommendation</u>

Staff submits that the decision on which program to purchase should rest on the answers to the following two questions:

- Which is the most comprehensive program available?
- Which program covers the most areas in the most cost-effective manner possible?

Comprehensiveness

The first question has been answered by the expert opinions. They all note that because the County is self-insured up to $1M, it presumably excludes little from its own coverage; consequently, SDRMA's program is not as comprehensive as the County in that regard. On the other hand, the County's insurance program structure must be kept in mind. The County achieves an $18M total limit because it purchases excess insurance from CSAC. So any claim over $1M is subject to the terms and conditions in the CSAC excess insurance program. As noted by the experts, because the CSAC insurance is nearly comparable to the SDRMA program in its scope, it is fair to say there is little difference in coverage for any claim over $1M. In that respect, the Commission loses little coverage by switching. Indeed, the only difference is in the limit amounts: $18M with the County versus $2.5M with SDRMA.

As it relates to injunctive/declaratory relief specifically, CSAC, like SDRMA, does not provide this type of coverage. Consequently, any injunctive/declaratory relief coverage by the County is by default only up to $1M. Through the Alliant supplemental insurance proposal, the Commission has the opportunity to purchase injunctive/declaratory relief claim insurance with a limit of $2M. Again, the only difference is in the limit amounts: $1M with the County versus $2M with Alliant.

In the matter of comprehensiveness, the Commission should make its decision based on how much insurance LAFCO truly needs and how much it should carry.

Cost Effectiveness

On June 17, the Assistant County Administrative Officer stated LAFCO's quote for FY2009-10 will be $64,797. As noted earlier, the Commission allocated $30,000 for GL insurance based on the quote given in February. In other words, the actual premium is $35,000 higher than your Commission-budgeted allocation in May. In terms of cost effectiveness alone, the cost comparison leans heavily towards purchasing the insurance from SDRMA and the Alliant supplemental:

Insurance Limit	County Quote*	SDRMA/Alliant Quote*
$2.5 Million	N/A	$5,615 ($3,680 SDRMA alone)
$5 Million	N/A	$7,190 ($5,255 SDRMA alone)
$10 Million	N/A	$11,130 ($9,195 SDRMA alone)
$17 Million	$64,797	N/A
Deductible	*None*	*Various, none higher than $2,000 for SDRMA claims, $1,000 for Alliant claims*

* Combined quote assumes the Commission would wish to purchase Alliant's supplemental insurance at the $2M limit at a cost of $1,935. The Commission does have the option to purchase this supplemental insurance with a $1M limit for $1,270.

However, the Commission should consider not only the cost of the premium itself for this year but also past experience because it can provide guidance in determining the impact to the budget for the foreseeable future. As noted in previous staff reports, the cost of the County's GL insurance has fluctuated for the past six years.

FY	Total LAFCO Budget	GLI Premium	% Change	% of LAFCO Budget
2004-05	$482,509.71	$ 4,200.00	--	1%
2005-06	$550,003.48	$12,982.00	209%	2.4%
2006-07	$540,064.40	$ 2,856.00	-78%	0.5%
2007-08	$471,687.00	$17,264.00	504%	3.7%
2008-09	$424,220.00	$29,592.00 (originally estimated at $3-5,000)	73%	7%
2009-10	$450,338.00	$64,797.00 (originally estimated at $30,000)	114%	14%

From staff's standpoint, this fluctuation has made it difficult to predict the premium when the LAFCO budgeting process starts between December and January. Up until last year, the estimates given by Risk Management around January used to be fairly accurate. That is no longer the case. As evidenced in planning for fiscal year 2008-09 and 2009-10, the estimates have not only been drastically inaccurate but also subject to change based on factors outside of this agency's experience. The County's self-insurance coverage requires the County to maintain strict funding requirements. Its overall costs determine these requirements, and all participants are required to assist in achieving those funding requirements based on a cost apportionment formula. If the County's overall costs go up, then the costs for all participants go up as well. So while LAFCO's premium is apportioned based on this agency's experience/exposure, LAFCO's costs will always be dependent on the overall losses the County experiences.

In addition, there is no memorandum of understanding between LAFCO and the County on this matter; LAFCO has no recourse but to "pay the bill." There is no procedural remedy to appeal an increase or a requirement on the County to notify LAFCO when either the rates increase or when the allocation formulas change. There is also no policy to normalize the premiums on participating agencies.

In contrast, SDRMA's policies restrict rates from increasing or decreasing by more than 15% each program year. LAFCO has experienced first hand that level of stability. As the Commission is aware, LAFCO purchases its Worker's Compensation Insurance from SDRMA. Since 2005, LAFCO's premiums for this policy have been stable in terms of both monetary amount year over year and as a proportion of the budget:

FY	Total LAFCO Budget	Workers' Comp Premium	% Change*	% of LAFCO Budget
2005-06	$550,003.48	$2,745.00	--	0.5%
2006-07	$540,064.40	$1901.99	-31%	0.4%
2007-08	$471,687.00	$1,845.79	-3%	0.4%
2008-09	$424,220.00	$1,377.70	-25%	0.3%
2009-10	$450,338.00	$1,200.00 (est)	-13%	0.3%

* LAFCO staff has been aggressive in qualifying the agency for additional incentives and discounts, allowing it experience decreases larger than 15%.

Because of the scope of coverage and the cost effectiveness of the program, purchasing the SDRMA program in conjunction with the Alliant supplemental insurance makes the most fiscal sense for the agency. Not only would the Commission receive comparable coverage at a lower cost, the Commission does not have the funds to retain the County anyway. As noted earlier in this report, in May the Commission allocated $30,000 into the Final Budget for general liability premium to give itself the flexibility to decide in June. Since then, the County has notified LAFCO that the GLI premium will be $64,797; approximately $35,000 higher than what is in next year's budget. At this point, there are only two ways to retain the County insurance within the parameters of the adopted budget:

1) The County lowers its premium to the allocated amount; or
2) LAFCO staff employee to be laid off.

The County has not offered #1 and LAFCO staff strongly recommends against #2. Mr. Morris, in describing the difficulty of simply using the CSAC coverage to evaluate the comprehensiveness of County's program, writes, "Because the County's basic coverage applies to claims of up to $1 million, the vast majority of potential LAFCO claims would be covered by the County, rather than by the CSAC excess coverage." Experience bears him out: The combined cost of the last two lawsuits against LAFCO was under $100,000. By this measure, the Commission should evaluate how much that first $1M of coverage should cost: $65,000, $30,000 or $5,700.

A third way to look at this issue is the economists' concept of "opportunity cost." Defined as "the value of the next best alternative forgone as the result of making a decision," this principle assists the decision maker with not just looking at the cost of the action taken but also at the cost of an action not taken. In this case, the cost of retaining the County is not just the expenditure of nearly $65,000 for insurance. It is also the cost of what the Commission forgoes for not purchasing almost identical insurance at the price of $5,700:

- Laying off an employee would have drastic consequences on agency performance; and
- Utilizing the cost savings to establish a reserve, which could be used for
    - Legal defense;
    - Help minimize the impact to funding agencies for LAFCO's budget next fiscal year
    - Offset the cost of any special study the Commission wants to outsource.

From a comprehensiveness of coverage standpoint, cost effectiveness measure and opportunity cost, all three point to switching general liability carriers and purchasing an SDRMA policy with a limit of $2.5M and purchasing the Alliant supplemental insurance with a $2M limit.

Allocated Funds

The budget allocates $30,000 for general liability insurance so that, theoretically, there were sufficient funds to pay the premium for either the County program or SDRMA/Alliant. If the Commission adopts staff's recommendation and switched carriers, it should re-allocate the excess funds to a reserve account. Staff recommends moving $24,385, which is the balance after the SDRMA/Alliant premiums are backed out, into a reserve account. Staff will return at a later date with a draft policy governing when and how those reserves may be used. Until then, the reserves will be considered “off limits” by staff. However, at this meeting the Commission should provide direction to staff on the basic parameters of the reserve account (how and when it can be used) and how it should be structured (whether there should be a super majority to disburse any funds out of the account) so that staff can draft policy language that better reflects the Commission’s preferences.

Attachments

Attachment A: Larry Costello’s Synopsis of GLI Coverage Comparison
Attachment B: Ron Grassi’s Analysis of GLI Coverage
Attachment C: Robin Johnson’s Analysis of GLI Coverage
Attachment D: Andrew Morris’ Analysis of GLI Coverage
Attachment E: Ellen Mirabal Doughty’s Analysis of GLI Coverage
Attachment F: Dennis Timoney’s Analysis of GLI Coverage
Attachment G: Dennis Timoney’s Response Regarding Care, Custody and Control Exclusion