



Finance Committee Memorandum

City of Arts & Innovation

TO: FINANCE COMMITTEE

DATE: OCTOBER 9, 2019

FROM: FINANCE DEPARTMENT

WARDS: ALL

SUBJECT: ANNUAL FINANCIAL REVIEW OF THE CITY'S SELF-INSURANCE TRUST FUNDS - FISCAL YEAR 2018-2019

ISSUE:

Receive, provide input on and forward to the City Council for approval an annual financial review of the City's Self-Insurance Trust Funds for Fiscal Year 2018-19.

RECOMMENDATION:

That the Finance Committee receive, provide input on, and forward to the City Council for approval an annual financial review of the City's Self-Insurance Trust Funds for Fiscal Year 2018-19.

BACKGROUND:

Effective fiscal year 2015-16, City staff began presenting to the City Council, through the Finance Committee, a financial and operational review of the City's Self-Insurance Trust Funds, including claim activity. This review includes the Workers' Compensation and General Liability Funds.

The Human Resources Department administers the City's Workers' Compensation program. The Risk Management Division of the Finance Department has responsibility for the oversight of General Liability program, whereas effective July 1, 2018 the City Attorney's Office is responsible for the management of claims submitted to the City.

The City purchases commercial insurance to help mitigate the costs of high severity losses, catastrophes, and high frequency losses shall they expend all available funds. The City carries two General Liability policies; a primary and an excess General Liability policy. The primary General Liability policy provides the City with an aggregate limit of \$20,000,000 and the Excess General Liability policy provides the City with an additional \$10,000,000 of coverage. Both the primary and excess General liability policies cover general and auto liability claims including but not limited to Law Enforcement Liability and Public Officials E&O. The City also purchases an excess Workers Compensation policy with an aggregate limit of \$25,000,000.

Both the General Liability and Worker's Compensation programs have self-insured retention's (SIR) of \$3,000,000. A self-insured retention (SIR) is the dollar amount that the City must pay before an insurance policy responds to a loss. This means the City has to pay the first \$3,000,000

of General Liability claims and the first \$3,000,000 in Worker's Compensation incurred. The City's insurance policies will then respond up until the aggregate limit afforded in the policy declarations. The City is responsible to pay for any additional claims costs incurred shall the City exhaust each of the policy's aggregate limits in addition to the self-insured retentions. The illustration below shows the thresholds of how large claims against the City may be paid.

General Liability & Worker's Compensation Policy Structure

General Liability	Workers' Compensation
Allied World National Assurance Company Excess Policy Limits \$10,000,000 Aggregate	Safety National Excess WC \$25,000,000 Aggregate
Safety National \$10,000,000 Occurrence \$20,000,000 Aggregate	
Self-Insured Retention \$3,000,000	Self-Insured Retention \$3,000,000

There have been no claims settled in the last 10 years that exceed insurance coverage under either program.

Each year, as the insurance policy is renewed, the existing structure with the \$3.0 million self-insured retention is re-evaluated to determine if a more beneficial (less risk exposure) option exists. This specific structure has been the best option for many years.

All City departments participate in the Risk Management program and make payments to the Self-Insurance Trust Funds based on actuarial estimates of the amounts needed to fund prior and current year claims and incidents that have occurred but have not been reported.

DISCUSSION:

Financial Overview

Attachment 1 provides an overview and analysis of all revenues and expenditures for the Self Insurance Trust Funds. Historically, the two largest cash outlays in the Funds are claim payments and outside legal fees. Claim payments in FY 2018-19 for the Workers' Compensation Fund and the General Liability Fund were \$4,231,000 and \$2,389,000, respectively. While claim payments are driven by many factors, outside legal expenses are a byproduct of claims in process and initiated during the year. For FY 2018-19, outside legal fees for the Worker's Compensation and General Liability funds were approximately \$285,000 and \$1,280,000, respectively.

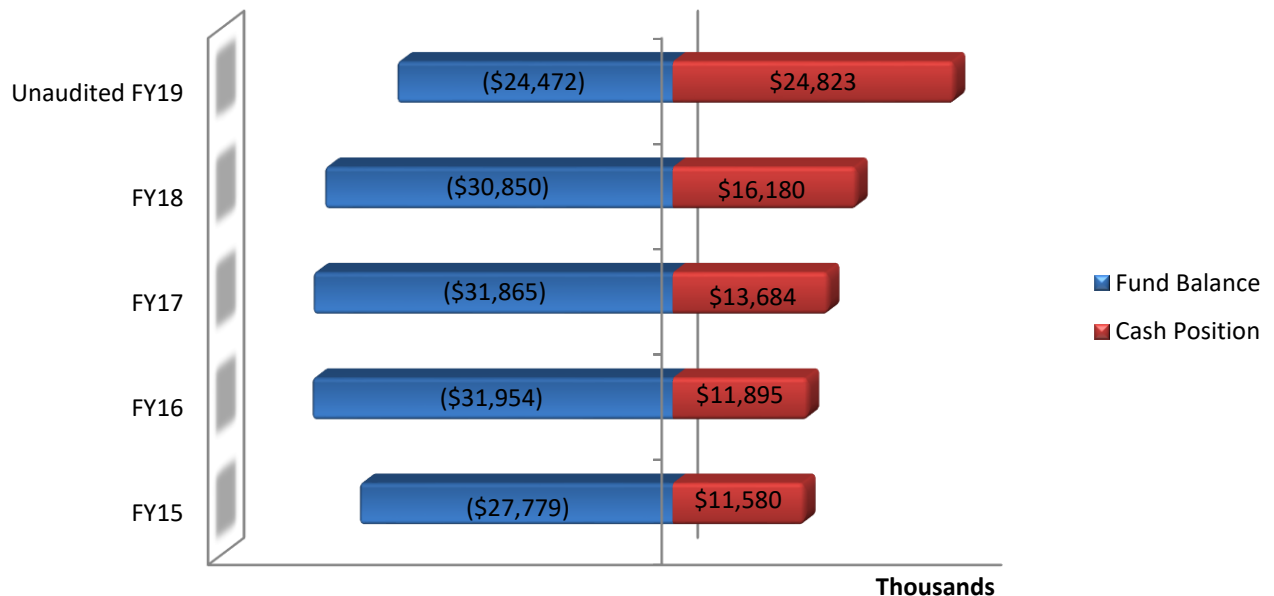
Cash Position and Fund Balance

Total cash currently on hand between both funds is approximately \$24.8 million, an increase of \$8.6 million from the prior year. The reason for the increase is primarily a result of additional contributions from the departments (\$5.3 million) as well as a decrease in claims and judgments (\$2.6 million).

The fund balance is negative and reflects the long term nature of many of the claims, in other words, there is not enough cash on hand now to cover all potential claims and liability payouts expected in future years. Currently, there is sufficient cash on hand to cover 51% of the long-term liabilities.

On November 28, 2017, City Council approved the Self-Insurance Trust Funds Reserve Policy establishing a 40% minimum funding level of the total combined current claims liability outstanding for the Self-Insurance Trust Funds effective June 30, 2018, increasing that minimum level to 50% effective June 30, 2020. In addition, if at any future point of measurement, the cash balance in any of these funds is more than 25 percentage points above the required minimum balance (e.g. above 75% after June 30, 2020), then staff must present a plan to the City Council as part of the subsequent budget process to reduce charges to the contributing City funds in a manner proportionate to the way that the funds were originally contributed. As of June 30, 2019, the unaudited cash on hand is projected to be approximately 51%.

Cash Position and Fund Balance



Claims Liability

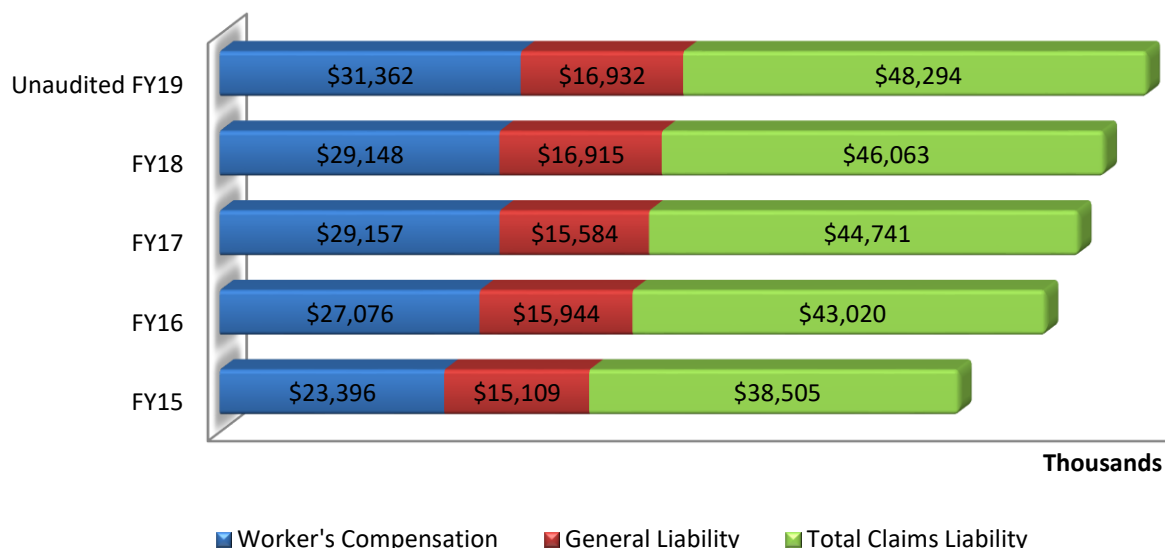
It is important to recognize that the claims liability amount recorded in each fund is an estimate of the amount for which that claim will ultimately be settled. These claims are often resolved for less than the total amount reflected in the claims liability figure, and that full amount of cash is not required to service the total claims liability. Additionally, in both funds, but particularly with Workers' Compensation, the actual outlay of cash is many years away (as many as 30 or more) for much of the outstanding liability.

Being self-insured requires valuing the City's claims liability for incurred claims losses and maintaining appropriate reserve funds to meet these future liabilities. In accordance with accounting standards, the City engages an actuarial consultant to perform a complex analysis of claims for both the Worker's Compensation and General Liability funds, the result of which is the determination of the total claims liability for each fund at the end of each fiscal year. The recorded estimate for total claims liability is based on the result of this study and includes an estimate for claims incurred but not reported and for allocated loss adjustment expenses. The actuary's

estimated liability considers the effect of inflation, recent claim settlement trends, frequency and amount of payouts, and other economic and social factors.

Following is a historical look at the trend of claims and judgment liability for the General Liability and Worker's Compensation funds.

Claims and Judgment Liability By Fund



The trend for the total claims liability, as determined by the actuary, has been increasing for several years. Despite cash outflows being volatile from year to year, the estimated annual increasing liability will create an even greater negative fund balance. Increasing the internal charge for services from departments will have a positive impact on cash position of the trust funds, but will put additional pressure on operating budgets throughout the City. Based on the estimated cash balance percentage of 51% at the end of fiscal 2018/19, there is no immediate need to increase internal charges for services from departments.

FISCAL IMPACT:

There is no direct fiscal impact associated with this report.

Prepared by:	Nancy Garcia, Controller
Certified as to availability of funds:	Edward Enriquez, Chief Financial Officer / Treasurer
Approved by:	Carlie Myers, Deputy City Manager
Approved as to form:	Gary Geuss, City Attorney

Attachments:

1. Self-Insurance Trust Fund Analysis
2. Presentation