CITY OF HAMILTON
CORPORATE SERVICES DEPARTMENT
Legal and Risk Management Services Division

TO:	Mayor and Members Committee of the Whole
COMMITTEE DATE:	May 13, 2020
SUBJECT/REPORT NO:	2020 Property and Liability Insurance Renewal Report (LS20010) (City Wide)
WARD(S) AFFECTED:	City Wide
PREPARED BY:	John McLennan (905) 546-2424 Ext. 5736 Jody Yarmo (905) 546-2424 Ext. 5735
SUBMITTED BY: **SIGNATURE:**	Mike Zegarac General Manager, Finance and Corporate Services Corporate Services Department

RECOMMENDATION(S)

(a) That the Liability and Property Insurance coverage for the term January 1, 2020, to January 1, 2021, be renewed through Arthur J. Gallagher Canada Ltd. and Marsh Canada Ltd. at a cost of $7,748,615 (net of taxes) and be funded through the 2020 Risk Management Services (RMS) Budget of $6,600,074, $1,033,690 from the Tax Stabilization Reserve (110046) and $114,850 from the Waterworks Capital Reserve (108015), in accordance with Appendix “A”, attached to Report LS20010;

(b) That the 2021 Risk Management Property and Liability budget be adjusted to $7,748,615 and that the 2021 departmental and appropriate Boards and Agencies budgets be adjusted accordingly;

(c) That, to realize of a 7.5% discount, the primary layer of liability coverage for the term January 1, 2021, to January 1, 2022, be continued through Arthur J. Gallagher Canada Ltd. and Marsh Canada Ltd. at a cost of $2,173,750 (net of taxes) and be referred to the 2021 RMS Budget;

(d) That, to mitigate market volatility, the second layer of liability coverage for the term January 1, 2021, to January 1,2022 be continued through Arthur J; Gallagher Canada Ltd. And Marsh Canada Ltd. At a cost of $950,000 (net of taxes) and be referred to the 2021 RMS Budget;

(e) That the General Manager, Finance and Corporate Services, be authorized and directed to execute all associated documents related to the renewals of the Liability and Property Insurance coverage for the terms January 1, 2020, to December 31, 2020, and January 1, 2021 to December 31, 2021, through Marsh Canada Ltd., on behalf of the City of Hamilton;

(f) That four (4) permanent FTE be added to the Legal Services and Risk Management complement, namely a litigation solicitor, law clerk and two administrative assistants, and that the annual compensation costs totalling $393,000 be cost recovered from City Departments and appropriate Boards and Agencies in 2021 and;

(g) That the one-time costs of $20,000 related to equipment and materials in support of the additional complement be funded from the Unallocated Capital Reserve (108020).

(h) That staff be directed to assess insurance options and litigation staffing prior to August 2021 in order to consider possible insurance options for the City, and adequacy of staffing for in-house litigation for 2022; and

(i) That RMS report back to Council with a work plan for expanding enterprise risk management.

EXECUTIVE SUMMARY

The City's Broker and Risk Management staff have conducted an extensive review of the insurance market since 2019, confirming that other insurers are not currently taking on municipal business and that municipal premiums have again seen substantial increases. Similar to the rational and increases reported in 2019, the hardening market is a result of many factors, but mainly insurers narrowing the types of markets to pursue and a declining rate of return on their investments. COVID-19 is likely to drive these issues further in the next two or three years at minimum. For the City this leaves the single option of renewal with its existing insurer.

Staff is recommending renewal with the City's current insurer based on analysis of the most beneficial premium and coverage options offered, the high quality service and a history of beneficial premiums compared to other municipalities in past years. While the overall year-to-year increase of 17% in the City's annual premium is not insignificant, it is comparable, if not favourable, to the renewal experience of other Ontario municipalities.

The option to obtain the first layer of liability coverage through 2020 and all of 2021 provides a 7.5% discount ($293,740) on the premium and is recommended in the current and expected market. Analysis of the deductible at $1,500,000 is recommended to limit the increased costs as it provides added premium savings over the remaining term of 2020 and 2021. The alternative of a one year renewal of liability coverage would increase the premium by $117,500 for 2020 and leave the City open to the potential for a much higher increase for 2021 in this most volatile line of coverage. Availability of coverage at current limits is also a concern.

Staff recommend the renewal of the City's full suite of insurance coverages for 2020 at a cost of $7,748,615. The quoted cost of coverage for 2020 represents a 17% average increase annually over 2019 premiums.

Accompanying a 20% increase in the primary liability coverage is an increase in the deductible level to $1,500,000, which was determined as the optimal retention level among the combination of deductible/premium options presented to the City.

Accompanying a 6% increase in the Transit liability coverage is an increase in the deductible level to $500,000, which was determined as the optimal retention level among the combination of deductible/premium options presented to the City.

The recommendations include a future review of the market to be conducted in advance of expiry of insurance and development of potential alternative approaches (self-insurance, captive market, etc.). This report also recommends staffing in a phased approach by adding in 2021 only part of estimated staffing due to changes in work following the higher deductible, and a later 2021 assessment of the potential need for additional staff. Staffing need follows the change in nature of claims work from the higher deductible limits so as to limit higher claims costs, to avoid additional outside counsel costs, to support Enterprise Risk Management and otherwise assist the City's position as an insured in future renewals and insurance markets. The insurer was not willing to offer an option for the City to maintain its current deductible level on general liability, and advised that municipalities the size of Hamilton generally would not be offered the lower deductible the City had obtained in 2019 and earlier based on claims handling and risk assessments.

The City is currently running on a brief extension of insurance terms on 2019 rates which will expire on May 14th. As such, the decision on renewal of insurance is time sensitive.

Alternatives for Consideration – See Page 10

FINANCIAL – STAFFING – LEGAL IMPLICATIONS

Financial: The 2020 premium of $7,748,615 (net of taxes) will be funded through the 2020 Risk Management Services Budget. The total 2019 insurance premium expense was $6,600,074 (net of taxes). The 2020 renewal represents an increase of $1,148,541 (17%) in insurance premiums.

The 2020 Insurance Premium budget is $6,660,074 (net of taxes). The resultant shortfall of $1,148,541 (net of taxes) is recommended to be funded through the Tax Stabilization Reserve (110046) $1,033,690, and the Waterworks Capital Reserve (108015) $114,850.

Also, with the options offered for renewal with the current insurer were various levels of deductibles for general liability and transit coverage. The City was not offered the option to remain at its current $250,000 deductible on the general liability policy as the lowest amount offered was $500,000 which was indicated by the insurer to be at the low range of normal for similar large municipalities. Cost benefit analysis of deductible options based on claims over the last 9 years supports $1,500,000 as the best option for premium cost and claims costs though there is no certainty future claims will fit the same patterns. The following table illustrates a Cost of Risk (premium + claims expense) comparison between a $500,000 deductible and a $1,500,000 deductible.

Cost of Risk Comparison		
Deductible	**$500,000**	**$1,500,000**
Annual Average Cost of Risk 2011-2019	$5,123,000	$4,129,000
Incremental Annual Compensation Costs		$393,000
One Time Costs		$20,000
Total	**$5,123,000**	**$4,542,000**
Total cost avoided with $1,500,000 deductible		**$581,000**

Staff also recommends an increase in the transit liability deductible to maintain the premium increase to a reasonable 6%. The primary factor behind this recommendation is the significant decrease in ridership and associated claims over the first 4 months of 2020. Further, staff has reviewed the transit claims experience for the past 9 years and finds the trade-off of higher deductible for a lower premium to be a reasonable approach to controlling cost of risk in the current hard insurance market. The increase in the transit liability deductible will not require any additional staffing.

In addition to the premium costs, the higher deductible will tend to result in larger in-house claims expenses as the City will be responsible for claims and defence costs up to the amount of the recommended deductible. Control and mitigation of in-house claims costs will continue to come through the diligent claims and litigation handling efforts of Risk Management and Legal Services staff on the claims and litigation, and also an enhanced approach to Enterprise Risk Management, discussed below, and aided by assistance offered through the broker and insurer to municipal clients. Impacts on the budget for claims expense will depend on the number and value of claims going forward, and for future budget discussion.

Staffing: An effective response to larger and higher volume of claims will require additional staff to control claims expenses, limit outside counsel costs, support Enterprise Risk Management, and to improve the City's risk situation for future insurance procurements. Dispute Resolution Section staffing has not increased since 2005.

The increase in deductibles requires enhanced effectiveness for litigation. The higher deductible means the City will be handling higher volumes and larger claims in-house, with resulting increases in workload and greater need for effective litigation response. This report recommends a phased approach, adding four permanent FTE in 2021, and a future assessment of costs and needs for an estimated additional three FTE based on claims experience into 2021.

Recent experience with larger litigation files completed in 2018/2019 showed the current staff in the Dispute Resolution Section of Legal Services faced challenges in managing caseloads and case preparation at the same time as preparing for cases involving larger trials. The required change in insurance deductibles for 2020 and 2021 however, will increase demand for in-house legal services with higher volumes and larger claims, and increasing the need for lawyers and support staff working as teams, which the current staff complement are unable to support. Without addition of staff the City's claims effectiveness will be reduced and costs will be pushed higher through either slow response or increasing need for outside counsel support. Additionally, experienced legal staff will be able to lend support to Enterprise Risk Management.

A preliminary assessment of staff needs suggests a seven FTE comprised of two litigation lawyers, two law clerks and three assistants. Rather than seek that level of staff addition at this time, the recommendation is to add four FTE, and assess future needs based on actual experience with claims work under the new insurance provisions. The staffing assessment would result in a future report on need and value of the additional legal positions in 2022.

Total annual cost of the four recommended FTE is $393,000, in addition to the compensation costs are associated one-time costs for equipment and furniture of $20,000. The staffing will begin in 2021 and will be allocated to the Departments and agencies. Permanent FTE are recommended because experience with contract staff has shown that it is difficult to attract and retain knowledgeable staff needed for the high level of service provided to the City.

As outlined in the financial implications section, the staffing costs are included in the avoided cost of premiums from the higher ($1,500,000) deductible.

Legal: Not applicable

HISTORICAL BACKGROUND

The City has acquired insurance through Marsh (formerly JLT) since 2011. Previously, dating back to amalgamation, insurance was acquired through the Frank Cowan Company. The move to JLT was the result of a full market review in which JLT was the successful bidder, at approximately $800,000 lower than the next lowest bidder. In April 2019, Marsh & McLennan Companies, Inc. purchased JLT.

Arthur J. Gallagher Canada Limited (formerly Pearson Dunn Insurance Inc.) is currently the City’s broker of record. Each year the broker oversees the placement of the City's insurance program as part of their contract duties. Marsh Canada Ltd. (formerly Jardine Lloyd Thompson Inc.) is a Managing General Agent who specializes in insuring municipal entities. A Managing General Agent is a party who is authorized by various insurers to act as an intermediary to accept placements from insurance brokers such as Gallagher.

Appendix B to Report LS20010 shows the last 5 years of coverages and related premiums acquired by the City through JLT.

POLICY IMPLICATIONS AND LEGISLATED REQUIREMENTS

N/A

RELEVANT CONSULTATION

Negotiation and discussions with insurers were conducted in association with the City's Broker of Record and insurer.
Comparator municipalities and other types of public sector entities were consulted.

ANALYSIS AND RATIONALE FOR RECOMMENDATION(S)

The premium increases for 2020 reflect the hard market trend that commenced in the latter part of 2018 and has worsened over 2019 and into 2020. The worldwide COVID-19 pandemic will serve to harden the market even further in the coming months. Some industry reports predict the COVID-19 pandemic to be the most expensive insurance event in history. Staff made inquiries through its broker, and directly with other municipalities, and determined substantial increases were occurring in the insurance market for several reasons, and in particular with municipal and public entity coverages. Direct comparisons with other municipalities are difficult due to differences in services and claims experiences.

The premium increase is largely the result of increases within liability coverage and can be attributed mainly to:

(a) The hardening of the global insurance market, primarily due to the combination of weather related catastrophic losses pairing with lower returns in the investment market.

(b) The present insurer's assessments of the City's claims history and exposures, which meant no other insurers were willing to quote for the City's 2020 coverage.

(c) Potential insurers' awareness of a number of high profile claims, or potential claims, including concerns with the Red Hill Valley Parkway.

(d) The principle of joint and several liability (1% rule) continues to exert immense pressure on claims reserving.

A hard insurance market is characterized by a high demand for insurance coverage and a reduced supply. Insurers impose strict underwriting standards and issue a limited number of policies. Premiums are high and insurers are disinclined to negotiate terms.

A number of different factors affect insurance pricing, but the following are common contributors to the hardening market:

(a) Catastrophic losses—Floods, hurricanes, wildfires and similar disasters are increasingly common and devastating. Years of costly disasters like these have compounded losses for insurers, driving up the cost of coverage overall.

(b) Claims costs—Claims are increasing in both frequency and severity year over year. One reason for this is that settlement verdicts for bodily injury claims are steadily rising. Attorneys are more inclined to take claims to trial. This extends litigation and significantly raises the cost to defend a claim. Additionally, advances in health care have made treatment more effective, and people are living longer, fuller lives even after a serious accident. While this is a positive trend, it has had an impact on compensatory damages and benefits.

(c) Underwriting standards—Insurers are struggling to overcome underwriting losses, especially given how low interest rates have remained in recent times. This has made carriers more cautious, and many are restricting the classes of businesses and lines of insurance they are willing to underwrite.

(d) Investment returns—Nearly every insurance carrier uses the funds it receives from premiums to invest in other markets. However, reduced interest rates have negatively impacted profitability, and carriers have a reduced their appetite for risk as a result.

(e) Reinsurance—Reinsurance is coverage for insurance companies. Carriers often buy reinsurance for risks they can't or don't wish to retain fully. However, reinsurance is becoming more expensive to obtain, which is causing carriers to increase their rates.

In addition to the presence of the hard global market, there are also the factors specific to Ontario municipalities, namely:

(a) Ontario's system of no fault auto insurance which requires payments to be made regardless of fault. Most HSR passengers are "first party" insured whenever they ride a bus.

(b) The continued presence of the legal principle of "joint and several" liability, also known as the "1% rule," whereby a plaintiff may recover all the damages from any of the defendants in a claim regardless of their individual share of liability. The legislation directs that a person injured by two or more negligent parties may collect full damages from any one of the negligent parties even if that party was only found 1% responsible for damages. As such, if the City is found by the courts to be even 1% responsible for a claim, it can be made to pay the full amount of the claim if the other negligent parties are unable to pay their share.

The Province has made promises to undertake a review of joint and several liability; however, any meaningful changes are unlikely in the near future. It should be noted that previous provincial governments have made similar promises but with no positive results for municipalities.

The City made a submission (Appendix C to Report LS20010) in October 2019 in response to the Province's request for first hand municipal accounts of the financial impact of joint and several liability. Numerous other municipalities made submissions as well. To date there has been no communication back from the Province.

(c) The high risk associated with being a public body with perceived “deep pockets” in an increasingly litigious society.

(d) Jurisprudence with continuously expanding grounds for the finding of liability on municipalities resulting in an ongoing expectation of a higher standard of care.

(e) Damage awards are getting larger. Court awards for severe bodily injury claims have increased dramatically in the last few years. These awards are primarily driven by the costs of providing future care for catastrophically injured persons. As the severity of awards increases so too does the exposure to municipalities who are, again, perceived to have deep pockets.

(f) The overall cost of claims has continued to rise at a rate in excess of premium growth. Individual claims are becoming more complex resulting in more time to manage the claim with more detailed investigation, more experts and more legal time involved in the process - at ever increasing rates. Even if the municipality is not liable for damages there are significant costs associated with simply defending claims.

(g) Municipal liability claims can have a “long tail,” which refers to claims that take a long time to become known and/or to settle. For example, the proximate cause for a claim may be in place years before damage occurs. The Building Department is particularly prone to this type of claim. Previous years claims are more difficult to manage as pertinent information is not always readily available. These types of claims will often take a longer time to resolve once in place.

The particular claims experience of the City is not one of excessive frequency leading to large cumulative totals for insurers. Rather, the severity of a number of anomalous large “shock” losses over the 9 year relationship with our present insurers has made the City a relatively unattractive/unprofitable risk.

Shock losses are unpredictable and, therefore, essentially impossible to predict and mitigate with any reasonable certainty. Legal and Risk Management Services, in conjunction with various client departments, has had a number of successes in controlling loss when a frequency becomes apparent. The reductions in claims expenses for sidewalk trip and falls, sewer back-ups, and police pursuits serve as prime examples in this regard. Overall LRMS saw a reduction of approximately $1,700,000 in the in-house claims expense for 2019, which marks the second year in a row of a marked reduction against the average. However, for 2020, it is anticipated that liabilities for outstanding claims will increase to reflect current and anticipated claims, Red Hill Valley Parkway claims being the main exposure.

Insurance comparisons to other municipalities are difficult. Services vary as do appetites for risk, deductible levels, and limits. The City of Hamilton is very clearly a “full service” municipality with police, paramedic, fire, transit, water treatment, and power generation all within the exposure portfolio along with the more basic municipal services. Many municipalities do not renew coverage on January 1 and, therefore, have yet to encounter the financial realities of the hard global market.

LRMS has confirmed a similar renewal experience with one reasonable comparator municipality, while three other reasonable comparators report significantly higher increases, one at 83%. In addition, these comparators are experiencing increased deductibles and some reduction in limits. It is important to note that while the City’s general liability deductible is increasing, there has been no reduction in the limits of coverage.

ALTERNATIVES FOR CONSIDERATION

Alternatives for coverage from other providers is not an option for the 2020 renewal. Traditionally, the insurance market available for municipal entities has been limited. Municipal operations pose a unique challenge to insurers; in general, insurers prefer to concentrate their expertise on one sector of an industry. A single-tier municipality such as Hamilton has diverse operations (e.g. Emergency Services including EMS, Police Services, and Fire), Public Works (Construction, Roads Maintenance etc., Transit, Parks, Recreation, Water and Wastewater, Public Health, and so on). The underwriting criteria of general insurance markets does not easily accommodate a municipal entity the size and scope of Hamilton with its variety of operations. The availability of markets willing to insure municipalities is further complicated by provincial downloading of services to municipalities, by legislative changes, and by broader court decisions. Even among those insurers who will insure a municipality, market options for the City are further limited as many do not have the capacity to insure large municipalities. As such, RMS staff and the City’s broker were unable to source any competitive bids.

Within the options offered for renewal was the alternative for the City to continue the first two layers of liability coverage beyond a one-year period and taking the proposed terms 20 months to December 31, 2021. The City would receive a 7.5% premium discount on the first layer of general liability if it opts for the 20 month approach. The 7.5% discount creates a savings of $117,500 for 2020 and a savings of at least $176,250 for 2021. Further, by not proceeding with the 20 month option would put the City back into what is likely to be an even harder market. COVID-19 in particular is likely to add uncertainty for insurers and have an impact on rates of return on investments in the next few years.

Also, with the options offered for renewal with the current insurer were various levels of deductibles for general liability and transit coverage. Staff has opted for a general liability deductible of $1,500,000 and a $500,000 transit deductible based on analyses described in the Financial Implications section of this report.

Lastly, as alternatives, the City could raise the uncertainty and costs of the market and any potential impact from COVID-19 with the province with a renewed request to provide additional protection from liabilities. This request may not see any helpful response but at least these growing costs are issues the province had asked about in the slowly developing review of municipal liabilities.

As referenced earlier, Legal and Risk Management Services has experienced two consecutive years of significant positive budget variance for Claims Expense, largely due to risk mitigation efforts towards certain high cost liability claim categories. With a hard market necessitating an increased retention of risk, in the form of higher deductibles, it is incumbent upon LRMS to expand its program of Enterprise Risk Management. The principles of risk identification, risk analysis, risk prioritization, and risk control will continue to provide the framework, with expansion coming in the form of a higher level of risk consciousness across the corporation spurred by a top-down / bottom-up alignment of risk focused objectives.

ALIGNMENT TO THE 2016 – 2025 STRATEGIC PLAN

Our People and Performance
Hamiltonians have a high level of trust and confidence in their City government.

APPENDICES AND SCHEDULES ATTACHED

Appendix “A” - City of Hamilton 2020 Property and Liability Insurance Renewal Coverages and Limits and Premium Comparison

Appendix “B” - City of Hamilton 2020 Property and Liability Insurance Renewal Deductible Options

Appendix “C” – Mayor Eisenberger’s Correspondence to the Attorney General re: Joint & Several Liability