Risk Management Division's Report of Analysis Regarding
Proposed Changes to the County's Property and Casualty Insurance Plan

Background

Risk Management is a Division of the Finance Department and serves as the property and casualty (P&C) administrator for the County. The Risk Management Division was established in May 2014 to provide risk prevention and mitigation services aimed at reducing the County's overall losses in a manner that supports the County's strategic mission and objectives. Risk Management works with Local Government departments and divisions to identify areas for training or prevention.

Risk Management facilitates claims adjustments, including property damage, bodily injury, and physical damage, procures the annual P&C insurance plan for the County, and reviews County contracts with vendors to ensure that vendors' insurance adequately protects the County's financial interests. An additional function of Risk Management is the recovery of County assets following disasters and drafting policies that support risk mitigation.

In 2015, Risk Management initiated the development of a Risk & Safety Committee, consisting of employees from various departments, in order to identify and mitigate risk and safety concerns to the County.

Risk Management also initiated and worked with the Volunteer Fire & Rescue Division to conduct a Request for Proposal (RFP) for Volunteer Fire & Rescue insurance services. This resulted in the County contracting for insurance services with a different insurance company, which provides an increased level of service to the Volunteer Fire & Rescue Division, and saved the Division approximately $50,000 in FY16, which accrued/accrues to the benefit of the volunteer stations.

The goals of Risk Management are to protect County employees and property, and the public, by providing a safe workplace and preventing catastrophic financial losses that have the potential to severely disrupt the County's operations and services to its citizens.

Risk Management is generally defined as exposure identification; risk evaluation; risk control; risk funding; and risk management administration, all aimed at minimizing the County's Total Cost of Risk.

Risk Funding

The County's current P&C insurance coverage is through a plan offered by VACORP, a risk retention pool comprised of Virginia counties. Albemarle County pays a fixed insurance premium annually for P&C coverage in the following areas: automobile liability, general liability, law enforcement liability, public officials liability, cyber liability, environmental liability, property damage, automobile physical damages, crime, and workers compensation. This is commonly called "guaranteed cost" or "fully insured" insurance because the premium does not fluctuate during the policy year unless there is a specific change in exposures, such as acquiring new property. The FY16 insurance premium to cover $127,972,621 million in property value and additional millions in liability coverage was $1,024,991, with an expected 4% increase in FY17, or $1,066,465.

Claims experience is an insurance term that includes the number, severity, and dollar value of insurance claims filed by the insured. Albemarle County historically has a low annual claims experience, resulting in the County paying more in annual premiums than it receives in claims proceeds (reimbursements) from VACORP. This is not an unusual concept in consumer-provided insurance. However, for an entity as large as Albemarle County, a multi-year, multi-phased risk management project to develop steps towards self-insurance, versus the guaranteed cost/fully insured approach, could potentially provide material savings over five to ten years and beyond.

In 2016, two initial steps were taken toward investigating the opportunity to assume more of the risk and therefore pay lower insurance premiums: (1) reviewing the County's property insurance deductible and (2) retaining an actuarial firm to analyze the County's ability and requirements to move towards self-insurance over multiple fiscal years. For many years the County's property insurance deductible has been $1,000 per claim, which is considered low in relation to the County's property assets. VACORP is offering deductible options of $25,000 and $50,000 per claim in FY17. The $25,000 deductible option would result in a premium reduction of $32,751 in FY 17 and the $50,000 deductible option would result in a premium reduction of $38,170 in FY17. Due to the County's low claim frequency and severity, the $25,000 deductible option may be the better choice for FY17 with the premium reduction of $32,751 being larger than the deductible amount of $25,000. The savings could be set aside in a Risk Management Fund to pay property claims.

Another potential funding source for the proposed Risk Management Fund is the difference between the budgeted insurance premiums and the actual insurance premiums in years that the County budgets for higher than actual premium amounts. Insurance rates and premiums are not finalized by VACORP until after the County has adopted its budget for the next fiscal year. Therefore, the County traditionally budgets for a 5% increase in insurance premiums to account for this unknown but anticipated increase in cost, which is a realistic budget increase for commercial insurance. The funds in years where the budgeted premiums exceed the actual premiums could be used to shore up the fund reserves. Currently, any residual funds become part of the General Fund fund balance at year-end.

Risk Management Fund

If the County's insurance plan is changed in FY17 to increase the deductible from $1,000 to $25,000 per claim, the County needs to be prepared to pay for any claims that are made in FY17. Therefore, Risk Management recommends the establishment of a Risk Management Fund for the purpose of paying claims from annual premium reductions. The fund is designed to be an internal service fund for budget and administration purposes, as well as providing reserve funds for unfunded losses. This fund would be managed as a trust fund, and any residual dollars would not be subject to appropriation for purposes other than paying P&C losses. Any balance remaining at the end of the fiscal year should be carried forward (re-appropriated) into the Risk Management Fund for the next fiscal year in order to build the reserve and to allow the County to ultimately move to a self-insured plan. There is a risk that the County could have an unusual and severe claims year in which the set aside premium savings would be insufficient to pay all of the property claims; however, the County's loss history shows that this risk is low, even in years of severe storms like a derecho or snow events.

Increasing the property deductible in FY17 aligns with early recommendations from the actuary firm hired by the County to research and analyze the feasibility of some level of P&C self-insurance. The firm suggests that the County consider increasing its risk retentions slowly over time.

Once the County has a mature Risk Management program and a strong reserve fund, the fund would be used to pay for additional expenses that a self-insured plan would necessitate, such as payment of claims in accordance with the County's coverage documents and claims handling guidelines, loss adjustment expenses, including defense costs and investigation costs, reserves on reported claims, reserves on incurred but not recorded claims (IBNR), deductibles or self-insured retentions (SIR's), actuarial studies, bonding, fees and commissions related to the insurance program, loss control services and safety programs, administrative and personnel costs for the County's risk management programs and division, insurance premiums, funded and unfunded losses in accordance with the County's coverage document and excess insurance coverage documents, and uninsurable exposures in accordance with the County's coverage document.

In conclusion, the Finance Administration staff recommends that the Board approve the establishment of a Risk Management Fund, as well as an appropriation of the insurance premium savings of $32,751 from the General Fund to the Risk Management Fund. If the Board approves the recommendations, staff will present an appropriation request to the Board for approval as part of the July 6, 2016 Appropriations agenda item.