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DEPARTMENT OF
HUMAN RESOURCES

RISK MANAGEMENT DIVISION

CITY OF SACRAMENTO
CALIFORNIA

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February 24, 2004

City Council
Sacramento, CA

Honorable Members in Session:

SUBJECT: RISK FINANCE PRINCIPLES

LOCATION AND COUNCIL DISTRICT: D-All

RECOMMENDATION:

Staff recommends adoption of the risk finance principles identified in the policy section of this report and immediate cancellation of the City's earthquake property insurance coverage.

CONTACT PERSON: Terrence L. Woods, Director of Human Resources, 808-7728

FOR COUNCIL MEETING OF: March 4, 2004

SUMMARY:

Due to the sharp rise in insurance premiums, Human Resources staff initiated an assessment of business practices to identify opportunities for the City to assume reasonable increases in risk in order to reduce premium costs. Due to the high cost of earthquake insurance and high deductibles, it is no longer cost effective for the City of Sacramento to purchase earthquake insurance coverage. Approved risk finance principles are needed to facilitate decisions such as the cancellation of earthquake insurance coverage.

COMMITTEE/COMMISSION ACTION: None

BACKGROUND:

- Historically, the Sacramento region has been less affected by seismic events and geologic hazards when compared to other portions of the state. There are no major faults in Sacramento County.
- Human Resources staff asked the City's insurance broker assess the maximum foreseeable loss (MFL) which could occur from an earthquake. MFL is the direct, total dollar value of a property loss excluding any indirect costs.
- Loss Control and Underwriting Services estimates that the MFL for the City of Sacramento is 2% of the total insured property value in the event of a magnitude 8.0 earthquake on the San Andres Fault near Los Gatos.

FINANCIAL CONSIDERATIONS:

- In FY 2004, the MFL for the City is \$16.9 million, and the annual cost of earthquake insurance coverage is \$596,000.
- The chance of an insurance recovery for an earthquake loss is low due to high deductibles applied to each damaged structure. Therefore, the purchase of earthquake insurance is not a good investment of City funds.
- Cancellation of the earthquake policy would result in a premium return of approximately \$198,000 in FY 2004. Premium savings for each subsequent year, in which earthquake insurance coverage is not purchased, will depend upon fluctuations in the insurance markets.
- There are no bond or trust requirements that compel the City to provide earthquake insurance coverage on collateralized properties.
- The City can apply for disaster assistance funding to repair uninsured structural damage caused by a major earthquake. It may be necessary to finance uninsured damage that is not covered by state or federal programs.

ENVIRONMENTAL CONSIDERATION: None

City Council
Risk Finance Principles
March 4, 2004

POLICY CONSIDERATIONS:

The following principles will be used to make risk finance decisions for the City of Sacramento including the cancellation of earthquake insurance coverage.

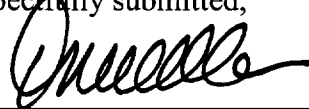
- Risk decisions will be based upon an evaluation of exposures balancing the probability of a loss, availability of insurance coverage, cost of insurance and likelihood of insurance recovery to assure a reasonable investment of City funds.
- To mitigate the assumption of additional uninsured risk, a City reserve will be established using funds that would have otherwise been used to purchase commercial insurance coverage.

The Human Resources Director will evaluate insurance coverage annually. The City Manager will submit information reports to the City Council annually regarding the status of commercial insurance coverage and the level of retained risk.

ESBD CONSIDERATIONS:

The City's insurance broker, Driver Alliant Insurance Services, utilizes small business partners in providing services such as the preparation of the earthquake hazard assessment.

Respectfully submitted,



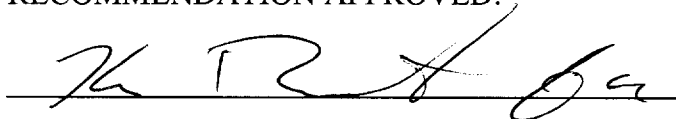
Terrence L. Woods
Director of Human Resources

Approved:



Ken Nishimoto
Deputy City Manager

RECOMMENDATION APPROVED:



Robert P. Thomas
City Manager

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RESOLUTION NO.

ADOPTED BY THE SACRAMENTO CITY COUNCIL

ON DATE OF March 4, 2004

RESOLUTION AUTHORIZING THE ADOPTION OF RISK FINANCE PRINCIPLES AND CANCELLATION OF EXISTING EARTHQUAKE PROPERTY DAMAGE INSURANCE.

BE IT RESOLVED BY THE COUNCIL OF THE CITY OF SACRAMENTO THAT:

1. The City Council adopts the following principles to guide decisions regarding risk financing.
 - a. Risk decisions will be based upon an evaluation of exposures balancing the probability of a loss, availability of insurance coverage, cost of insurance coverage and likelihood of insurance recovery to assure a reasonable investment of City funds.
 - b. To mitigate the assumption of additional uninsured risk, a City reserve will be established using funds that would have otherwise been used to purchase commercial insurance coverage.
2. The City Council authorizes the City Manager to cancel earthquake property damage insurance.

MAYOR

ATTEST:

CITY CLERK

FOR CITY CLERK USE ONLY

RESOLUTION NO.: _____

DATE ADOPTED: _____