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ITEM ID: 2023-350-0

TRANSMITTAL DATE: October 20, 2023

MEETING DATE: October 27, 2023

TO: Board of Directors

FROM: Don O. Del Rio, General Counsel

SUBJECT: Discussion of Self-Insured Retention (or Deductible) Within the SCRRA Insurance Program Requested by Chairman McCallon

Issue

The Authority requires insurance to effectively manage its operating and other major risks and ensure its continued economic viability in the event of a catastrophic event. As part of the Authority's annual renewal of its insurance policies, and in consultation with its longtime insurance brokers Marsh and Price Forbes, the Authority evaluates the self-insured retention (SIR) amounts for its various policies of insurance from a risk, budget, and cost perspective, and explores whether and to what extent to recommend changes to the SIR amounts for consideration by the Board.

Recommendation

Receive and file.

Strategic Commitment

This report aligns with the Strategic Business Plan commitment of:

- **Modernizing Business Practices:** Continue to work collaboratively with our Insurance Brokers to obtain the most comprehensive insurance coverage available in the most cost-effective manner to ensure the continued viability of the Authority as a leading transportation provider.

Background

Insurance is a contractual arrangement whereby the Authority may transfer certain risks to insurers, thereby protecting its assets from destruction or its monetary resources from depletion. By doing this, the Authority is able to ensure its continued viability in the event of specified loss events.

SIRs (or deductibles) are a type of risk transfer mechanism contained in liability insurance policies. SIRs allow policyholders to reduce their premium in exchange for assuming some level of initial risk of losses. The insured agrees to pay a specified portion of each loss and the insurer pays the rest up to the policy limits.

Benefits from the use of SIRs include savings on insurance premiums, paying claims as they occur rather than in advance and having more control in the claims resolution and litigation process.

The Operating General Liability ("OGL") Insurance Program ensures that the Authority will have the financial resources to continue operations in the event of a catastrophic incident causing injuries to passengers or third parties and/or damage to their property.

The Authority's OGL policy is an indemnity type policy which is written on an "occurrence reported" basis. The policy is subject to an annual aggregate, meaning claims paid under the policy erode available limits for the balance of the policy year. Once one or more claims are paid in amounts totaling the policy limit, the insured subsequently will be without coverage for any future claims during that policy year. However, the policy contains a reinstatement clause which provides that, if a policy limit incident occurs, the Authority has the option to reinstate the full amount of the initial policy at 125% of initial premium.

Discussion

Each year during the annual insurance renewal process, the Risk Manager, working with our brokers Marsh and Price Forbes, shops the SCRRA insurance program to the underwriting market in London and Bermuda. The proposal to fill out the entire SCRRA insurance program is then presented to the Board for approval in advance of the new insurance period beginning July 1. As part of the approval process, the Board considers the scope and price of each different insurance policy (e.g., Employment Practices; Operating General Liability; Property) as well as the SIR (or deductible) attached to each policy of insurance.

From time to time, the Board has adopted a change to the level of an SIR, based on market conditions and the resulting change to the premium price for that particular policy. For example, in June 2014, the Board elected to increase the SIR for the Operating General Liability (OGL) policy from $4,000,000 to $5,000,000 for FY2014/15[1]. The change in the SIR amount for FY 14/15 resulted in an annual cost savings of approximately $375,000 from the prior fiscal year. Cost savings in reduced premiums have continued each year as a result of the increase to the SIR and total approximately $3.5 million in reduced premiums through FY23/24.

The next year, in June 2015, the recommended OGL policy SIR amount was $5,000,000. The Board was given the alternative to reduce the OGL policy SIR from $5,000,000 but elected not to do so. In fact, since the 2015 policy year, the SIR on the OGL has stayed consistent at $5,000,000. Although the OGL policy SIR has been kept at $5,000,000, other aspects of the Authority's Insurance Program have changed in the past seven years. For example, in 2019, the Employee Theft deductible under the Crime policy was reduced from $250,000 to $100,000. In 2020, the Pollution policy was modified to reflect a higher deductible, from $100,000 to $250,000, for the Authority's aging underground storage tanks. Ultimately, various factors, including market conditions, drive alterations of deductibles and coverage limits. Unfortunately, these factors often fall outside of the Authority's control.

One option for the Board is to create a reserve fund that can be used to satisfy the SIR in any per occurrence situation. This reserve would carry over year over year. However, because major loss events are rare, especially with the implementation of additional safety measures such as PTC, a multi-million dollar allotment of funds in anticipation of a major loss may sit idle for a long period of time. Alternatively, the Board may choose to provide year-to-year funding via the annual budgeting process (similar to the process described in the paragraph below). Because of the nature of major loss incidents, the ensuing litigation always takes years to conclude (as Oxnard did) and therefore the Board and Member Agencies would have at least several budget cycles to prepare and fund all or part of the SIR amount.

Please note that to fund more modest, ordinary course legal settlements that do not meet or exceed the self-insured retention, SCRRA currently allocates funds ($990,000 in FY24) in each annual Operating Budget. As we start our budgeting process for fiscal 2025, the Finance Team will work with the Legal Department to assess all potential claim liabilities estimated to be settled in the coming fiscal year and allocate the estimated costs in the annual Operating Budget. These funds will be earmarked for the specific claim settlements only as identified by the Legal Department. These funds will not be used for legal fees.

When the SIR is listed at $5,000,000, be advised that is an approximate deductible because the calculation of the final SIR for any given claim on the OGL policy will fluctuate slightly based on the economics of the particular claim (e.g., settlement amount, defense spend, etc.).

<u>Budget Impact</u>

Finance has worked with the Legal Department to allocate $990,000 in the annual Operating Budget for "Liability Claims / SIR". As we start our budgeting process for fiscal 2025, the Finance Team will work with the Legal Department to assess all potential claim liabilities to be settled in the fiscal year and allocate the estimated costs in the annual Operating Budget for "Liability Claims / SIR". These funds will be earmarked for the specific claim settlements only as identified by the Legal Department. These funds will not be used for legal fees.

<u>Next Steps</u>

The yearly evaluation of SIR amounts for the Authority's policies of insurance is a Risk Management priority as it relates to insurance premium costs in connection with the risk-tolerance goals of the Authority.

Prepared by:	Ray Barrera, Senior Counsel and Risk Manager Arnold Hackett, Chief Financial Officer
Approved by:	Don O. Del Rio, General Counsel